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Jacques Pelkmans

Mutually Intrusive:

How Germany and the EU Help Each Other in Fostering Competition

After a brief reminder of the crucial role of competition in the EU internal market, both in terms of design and expected economic effects, the stimulating role of Germany in developing an effective EU competition policy is emphasised first. With the profound transformation of the Union and its internal market, the significance of EU competition policy has increased over time. Other EU policies have also contributed to the promotion of a more competitive internal market. This has led to ever stronger EU influence prompting greater competition in Germany in a number of previously sheltered sectors or activities. However, the latter trend is unlikely to be very different in many other Member States: Germany is probably not a special case.

Competition and Change, the Drivers of Market Integration

The crux of market integration in Europe has always been to create opportunities to benefit from comparative and competitive advantages, static as well as dynamic, by enabling cross-border mobilities in the Union. Such actual or potential cross-border movements or establishments are likely to exercise considerable discipline on the price/cost margins of larger players and will often prompt deep changes in corporate behaviour over time and lead to innovation in quality, product differentiation, product costs or production processes. They will also develop different ways of serving customers thereby widening choice. Sometimes, change in specific markets induced in this way can be quite unsettling, leading to restructuring given economies of scale (and scope) and gradual consolidation at the European level. For consumers, the benefits are likely to consist of far wider choice than before and sharper price competition, but they may well extend to the eventual benefits of a greater spur for innovation in products and processes. When new entrants respond with new business models – whether with mini-mills in the steel industry (1980s), mass production in white goods (1960s) causing havoc in the industry, satellite TV as an alternative to incumbent terrestrial networks, purchasing syndicates of supermarkets across intra-EU borders, low-cost no-frills airlines or even more generally the notion of going back to “core business” and divesting internal business ser-

vices to more specialized enterprises – the prospect of having access to a vast EU internal market can serve as a leading determinant. Indeed, new business models may well be a catalyst of change in one sector and, in other instances, the inevitable consequence for a company in responding to fiercer competition generated in the internal market.

This perspective on the crux of EU market integration clarifies immediately that the establishment and proper functioning of the EU internal market is not primarily about the famous textbook effects of trade creation and trade diversion. These comparative static effects under restrictive assumptions of simple tariff theory have long had the useful function of underlining the (in principle, better) alternative to a customs union, namely, world liberalisation of trade. Moreover, they show that as long as tariffs in one or several customs union partners remain fairly high, trade diversion (entailing negative welfare effects and irking third countries) risks significantly reducing the net benefits of the customs union. Of course, this approach remains relevant for the EU internal market of temperate zone agricultural goods, which still operates behind high tariff walls. Otherwise, simple static tariff theory tells us next to nothing about the economic benefits of a competitive EU internal market in goods and services.

The more interesting and much larger benefits of market integration are derived from induced productivity effects, when forced to overcome X-inefficiencies in order to survive or pre-empt takeovers, and from behavioural and structural determinants of corporate strategies which may well gradually “Europeanise” once previous forms of sheltering no longer apply. Over the five decades of EU market integration, not all these types of effects can be solely attributed to the EU internal market – indeed, whether and to what extent technological change and different wholesale and retail business models (which in turn depend on new technologies) are exogenous or endogenous is extremely difficult to establish with authority – but the deepening and widening of the EU internal market has undoubtedly facilitated, if not accelerated, the pro-competitive impact of these developments. This essay is of course not the place to ana-

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lyse systematically the tremendous dynamism in goods and services markets – and to some extent in capital markets as well – in interaction with the permanent ambition to improve the internal market. The key words are “competition and change”, made possible by the removal of regulatory barriers of an almost infinite variety, overcoming the distortive heterogeneity of Member State rules (where such diversity is unjustified and merely a deadweight loss) via EU regulation or reference to common standards, the emergence of EU rules to prevent EU-wide market failures and the pursuit of a common competition policy.

The competitive internal market which engenders these economic gains is not only a result of EU competition policy. Competition in the internal market is nothing less than “systemic”, as it is the outcome of a wider treaty design when properly applied. The three main determinants of competition in the internal market are (1) EU competition policy based on Articles 81 – 89, EC (in the Lisbon Treaty, Articles 101-109), (2) the negative and positive integration of the internal market itself, manifested in free movement, the right of establishment, harmonisation (in fact, EU regulation nowadays) and mutual recognition and (3) the nature of the EU common policies (such as trade, agriculture, transport, environment, energy and to a degree even the euro). The following factors will all lead to a more competitive internal market: the more pro-market the common policies are (while carefully ensuring the avoidance of market failures), the more complete free movement and the right of establishment are (also, in services), the greater the extent to which mutual recognition will be applied by Member States (and supervised by the Commission), the more “Better Regulation” principles will be followed in legislating new EU regulation (and in amending the existing regulatory *acquis*), the better EU competition policy will protect competitive processes without exception and the better the EU level, together with national regulators, will ensure that the opening of network markets is not only pro-competitive inside

Member States but indeed EU-wide, even when this requires investment in infrastructure and some degree of centralisation of the combination of anti-trust and regulation. An additional pro-competitive force may well be found in the national competition policies of the Member States.

The Pro-Competitive Influence of Germany

The “systemic” function of competition in the EU internal market has initially been due, in no small measure, to Germany. Nowadays, this pivotal contribution is sometimes forgotten. The central place of EU competition policy in the Rome Treaty was forcefully advocated by the German negotiators. Germany had just gone through the process of setting up its own competition policy, a much stronger variant of anti-trust than in any of the other five EEC countries¹ and a great contrast to its pre-war tradition of cartels. Germany can be regarded as the architect of the EU competition regime, as both its insistence and its head start created a very strong position in the Spaak report and in the textual proposals later. The competition articles of Rome have survived five decades of treaty change unscathed, even though their application has evolved over time, some times drastically so.

In the first two and a half decades or so, Germany remained a major force in matters of EU competition. Commissioner Von der Groeben, the first Competition Commissioner, was an activist policy maker and quickly ensured the Commission’s reputation as a powerful trustbuster. European business suffered perhaps from the somewhat legalistic culture in this policy domain (e.g. huge numbers of notifications of horizontal and vertical agreements, without much regard for the “effect” of such agreements on competition), but the message was crystal clear. Germany remained a staunch advocate of a pro-competitive stance in the internal market, whether through competition policy or via pro-market positions regarding liberalisation of EU trade policy. The UK and France, later followed by all Member States, also saw the benefits of enacting more powerful national competition policies in the wake of the German example.

Of course, one should not idealise this leadership too much. One could go too far ahead of the troops. The much greater acceptance throughout the Union of rig-

¹ And the UK for that matter; note that the other EFTA countries at the time neglected this issue, sometimes justified by the “openness” of their small economies, which was thought to generate enough competitive exposure anyway.

orous competition policy in 2010 ought not make one blind to the struggles of making competition policy meaningful in the lingering presence of widespread interventionism in the EU economy. A telling example is the Commission transparency directive of 1980 (based on Art. 86, sub 3, EC), which was an attempt to obtain clarity about the financial interdependence between national governments (or public agencies or development banks) and “their” state-owned enterprises. Whether and to what extent state aids were given in these nebulous or unreported relationships was totally unclear. The reporting obligations would serve as a basis to pursue a policy of reducing these distortions. Not only did several EU countries take the Commission to the ECJ (though the ECJ sided with the Commission in 1982), but the Director General of DG Competition – indeed, a German – was compelled to leave.

Germany also led by example in goods markets. It had developed a high-quality and powerful industrial sector, giving it a prominent position in the internal market as well as in many markets throughout the world. When competition from the NICs (Newly Industrialising Countries) arose, Germany demonstrated that dynamic adjustment away from simple textiles and clothing, toys, shoes and other relatively low-skill intensive goods to high-skill and technology-intensive goods was entirely possible. Its pro-competition and free-trade stance (at least in industrial goods) did not have to be watered down.

Looking back with the knowledge of today, it is good to realise that the leadership and consistency of the Germans with respect to competition in the internal market, impressive though it was, had been built on a fairly narrow basis: the industrial goods markets. Once the Union and its internal market started its transformation, beginning with the Single Act, German leadership waned, and frictions or signs of footdragging became more numerous.

Triple Intensification of Competition in the Internal Market

Since the mid-1980s, policy-driven competition in the EU internal market has gradually intensified in three distinct ways. All three have selectively presented considerable problems of adjustment for Germany. These three forms of intensification of competition include:

- the “deepening” of the internal market;
- the “widening” of the scope of the domains falling under the internal market; and

- a shift towards more pro-market common policies, also causing competitive exposure in the internal market to be enhanced.

The deepening of the internal market, especially for goods, enhanced competition directly through a massive assault on technical barriers (e.g. via the New Approach), the removal of regulatory barriers over a much wider spectrum than before the Single Act, the removal of customs controls inside the internal market, and several horizontal approaches such as more open and competitive procurement, (strict) product liability and EU trademarks and copyrights. This assault was accompanied by a sharpening of EU competition policy. In anti-trust, one can mention a tougher anti-cartel approach, in particular via leniency, stricter conditions upon (or removal of) exemptions (e.g. in cars) and a firmer approach to exclusionary abuses. This extended to state aid, an area where Germany turned out to be anything but a pro-market leader. Examples include the privileges of Volkswagen, some spectacular aid cases in former GDR, the perpetual saga of shipbuilding subsidies and the long-postponed *Jahrhundertvertrag* on phasing out the towering coal subsidies.

The widening of the scope of the internal market can be summarised in five steps: from goods to selected services (transport and financial services first), to professional services, to network industries, to horizontal services liberalisation and finally to capital. Moving beyond the goods markets has occasionally been problematic for Germany, such as in transport, selected network industries and horizontal services (e.g. the infamous Bolkestein directive, now 2006/123). When opening up markets other than goods, EU competition policy automatically follows. It now applies in network industries, albeit together with EU regulation and the functioning of national regulators, and to many services sectors (beginning with the four combined German insurance cases in early January 1986, which represented a breakthrough for the development of an internal insurance market). Furthermore, EU competition policy itself was widened by EU merger control in 1989 after many years of resistance by the competition authorities in Germany, France and the UK.

The intensification of internal market competition via common policies has been most conspicuous in trade policy, which has become outright liberal via the multi-lateral and the FTA routes (plus GSP and the Everything but Arms initiative). After the Transport Council lost the ECJ case brought by the European Parliament in 1985, the common transport policy has also become pro-market in all six modes. For Germany, even a superficial

comparison of road transport interventionism by Minister Weber in 1967 (e.g. quotas) with today's regime will make clear the U-turn that this liberalisation implies. The very gradual but clear (increasingly) pro-market trend in agriculture is perhaps no longer as difficult as it would have been a few decades ago (because nowadays many small German farmers are only part-time farmers) except for its positioning on the high single-farm payments for the mega-farms in Eastern Germany, which have by now become efficient.

EU Returning the Favour to Germany?

One might interpret recent pressure from the EU on Germany as a returning of the favour on competition in the internal market. There is a larger number of recent examples of the EU wanting Germany to accept more competition than examples of Germany extending its advocacy of the past to the newly liberalised domains of the internal market. In such instances, sectors or regions were not competitive, enjoyed "cosy" sheltering arrangements or had fallen victim to socio-political blockages.

An arbitrary list of such pressures might include:

- the old EU misgivings about the Landesbanken of the regions (Laender) where forms of capture or political influence led to distortions; the suspected bad management of these banks has meanwhile led to their possible demise or consolidation, presumably in a more rational arms-length framework;
- the almost eternal coal problem; in fact, a genuine EU internal market for coal has never existed since 1951, the beginning of the ECSC; the number of German coalminers has drastically shrunk, but subsidies per miner easily still reach 100 000 euros or more, not counting considerable pension outlays, and this after decades of adjustment;
- resistance to the modern EU state aids logic in some high-profile cases;
- deep misgivings about horizontal services liberalisation, in combination with the posted workers directive (even though the latter unconditionally imposes host-country control, based on minimum wages); the real problem in Germany is the puzzling lack of political will to enact statutory minimum wages, as most other EU countries have for decades, including countries such as Austria and the Netherlands, which have had far lower unemployment rates than Germany for a long time (including during the crisis);

- lingering resistance against open EU-wide competition on product conformity assessment and accreditation, in various ways, until given up very recently in the framework of the 2008 "goods package";
- the lonely position Germany assumed in electricity liberalisation during the first stage (between the 1996 directive and the revision in 2003), where it maintained the option of negotiated (instead of regulated) third-party access, with obvious anti-competitive outcomes;
- the huge feed-in financing of the windmill industry over a period of ten years, where one can ask serious questions about the manufactured competitive advantages for German players in a new industry, even though such state aids would never be allowed were it not for CO₂ reduction;
- the abortive state aids to Opel when even the Opel board experts publicly held that they were "without industrial logic";
- the fierce resistance of the German government against unbundling in the electricity sector, although in the meantime both E.ON and RWE have offered such remedies ("commitments") in anti-trust cases with the Commission.

One is tempted to conclude from these examples and other ones that Germany remains ambivalent about the deepening and widening of the internal market today. The EU returning the favour of a competitive internal market to Germany is likely to be good for Germany in the longer run. But in the short to medium run, it might be politically difficult to continue the path of further deepening and widening (e.g. more in services and selectively in labour market regulation, in addition to a genuine EU patent) given recurrent anxieties in German society.

How Special is the German Ambivalence?

Zooming in on Germany's ambivalence about the competitive internal market should not be done without explicitly taking the EU context into account. One can of course take the view that every Member State is "special" – when it comes to the details, that is likely to be correct. Nonetheless, it does not take much effort to find more or less similar examples of resistance or deeper ambivalence in many other EU countries. These objections or frictions emerge when purely domestic reforms of substance are introduced, when domestic reforms are required by the framework of the Lisbon

process or indeed when reforms are part and parcel of developing the EU internal market.

In this light, there seems to be no reason why Germany ought to be singled out or regarded as “special”. In network industries, for a long time a bloc of EU countries (with France and Belgium as frontrunners) attempted to undermine, discredit or slow down the stepwise liberalisation, if only because the propensity of public utilities workers to strike in disrupting ways in order to retain their privileges was quite high in these countries. The obverse is found as well. Whereas the UK favoured deeper financial market regulation in the Financial Services Action Plan (2000 – 2005), it did everything it could to keep the ensuing draft regulation as “light-touch” as possible, which is one reason the EU was ill-prepared to prevent the crisis or better deal with it among Member States. A sharp contrast to Germany’s long-standing commitment to competition policy is found in the Netherlands, where a solid and EU-based competition law only saw the light in 1997 (the Commission regarded the country as a cartel “paradise” until the early 1990s). Examples of stubborn, unjustified resistance by a single Member State are plenty. Take Romania’s recent enactment of a new excise duty, which is illegal in the EU under indirect tax harmonisation, and hence null and void. Or consider the long-standing Dutch refusal in the 1990s to respect two ECJ rulings on the mutual information on technical or regulatory barriers directive 83/189 until the Securitel case made this impossible, thereby suddenly saddling the 83/189 Committee and the Commission with almost 400 instances of Dutch decrees and technical annexes, nearly causing two Dutch ministers to resign. Also, superdominance is not unique to Germany. If Italy is the relevant market for broadcasting services, can one argue that Mediaset is up against the competition of three RAI networks and a fringe of small commercial channels, or can one reasonably maintain that there is a superdominant “collective” between RAI and Mediaset due to the fact that the owner of the latter has a decisive influence over the nominations and key issues of the former?

To end these examples with an extreme one, the overdue horizontal liberalisation of services was originally prompted by the many and occasionally incredible barriers to effective competition in the internal market. These barriers had little to do with services sensitivities connected to the labour contents of these activities (which formed the core of the debate on the Bolkestein draft directive, including in Germany) but rather with anti-competitive regulation. Few economists in Europe seem to know that until the draft proposal by Com-

missioner Bolkestein, no less than seven EU countries (of 15 at the time!) employed or could employ an “economic needs” test for certain cases of entry. Thus, in these Member States, a local committee composed of one’s competitors was to assess how welcome (what economic need?) the new entrant actually was. Only since 29 December 2009 (when directive 2006/123 had to be transposed into national law) can we be sure that these anti-competitive needs tests no longer exist. It shows that in a range of EU countries, the mindset of wanting a competitive internal market was really one of goods, not services.

All in all, Germany seems a normal case where the spectre of competitive exposure often raises fears, just like it does in other EU countries, or upsets cosy arrangements, sometimes even hand in glove with local politics.

Conclusions

The pursuit of competition in Germany has been greatly facilitated by Germany’s ever deeper integration in the EU internal market. In turn, this internal market has itself deepened and widened whilst competition has intensified. This was once initiated by Germany itself.

Today, the German pursuit to foster competitive market conditions at home can no longer be seen as separate from the EU pursuit to arrive at and maintain a competitive internal market covering as many economic activities as possible. In particular, the widening of the EU internal market’s scope and of its competition policy have engendered a degree of ambivalence toward competition in Germany, as traditionally sheltered activities have become (more) exposed to rivalry and efficiency pressures. Indeed, Germany’s long-standing pursuit and the EU’s pro-competition stance with respect to the internal market have become mutually intrusive. The recent ambivalence in Germany is interesting for observers in other Member States precisely because Germany was long regarded as an icon for anti-trust in Europe. However its internal sensitivities about greater competition in domains hitherto shielded against the internal market do not seem to represent a special case. More or less similar sensitivities are easily observed elsewhere in the Union. One might also suspect them to be temporary. In the longer run, if proper care is taken to prevent market failures, the mutually intrusive pursuit by Germany and the EU at large is bound to be good for both Germany and the Union economy.