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A MONOPOLISTIC STATE IN COMPETITIVE MARKETS

How State Ownership and State Intervention affect competition

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To my family,

Graziella, Paolo, Ilaria, Luca and Pietro.

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EXECUTIVES SUMMARY

The State has a central role in the economy of every World's nation. The modality and the size of its intervention affect other market's players and the degree of competition. A first type of State intervention is the direct ownership of enterprises (called "State Owned Enterprises" or SOEs). An SOE is a "special" form of undertaking which most of the time enjoys a privileged financial condition and a statutory monopoly over its core activity. These privileges are granted in order to pursue objectives that competition and private ownership are considered to be inefficient or incapable to pursue (market failures). Two examples of goals that an SOE is usually entrusted are the Universal Service Obligation, the requirement to serve in a non-discriminatory way all citizens, and income redistribution. However, these objectives and special privileges granted to SOEs, generates a greater incentive and an expanded ability to behave anti-competitively, compared to private enterprises. Indeed, when an SOE is found in a condition to compete with other player's in a market can disadvantage or drive out of the markets its competitors pricing predatorily or rising rivals' costs.

During the 1980s and 1990s political movements and economic ideologies started to blame SOEs of being inefficient, founding for a new theory of "Government failures". In particular it was believed that the source of inefficiency came from the public form of ownership, thus alleging that a change in the ownership structure (privatizing state monopolies) could solve the government failures. However, the effect of privatization on competition is much worse than keeping a state monopoly: selling SOEs to private parties have the only effect of transforming a public monopoly into a private one. The same incentives to abuse of the condition of dominance are common to both private monopolies and SOEs. Therefore, contrary to the initial expectations, privatization is found to (1) increase the control of the State in the market, (2) created not fully private companies, but often hybrid forms of public-private ownership, (3) no change or a decreasing of the degree of competition in the market.

A third type of state intervention is the liberalization of markets. The three main elements of a liberalization policy are (1) the deregulation of the market opening the former legal monopolies to competition, (2) the regulation of the market through external agencies, (3) the control of the Competition Authority to all the players in the market. These policies bring under the same light both public and private enterprises, thus creating a playing field for genuine competition. However, according to the type of regulation implemented, the playing field created is more or less leveled, in other words, even after the privatization of the public monopolies and the application of competition law to all the players in the market, remains situations in which competition is hindered. The main issues generated by an "inefficient" ex-ante intervention (regulatory intervention) are: the incentives of the incumbent and entrants to invest, the incentive of the incumbent to invest strategically, the incentive of the a vertically-integrated producer (VIP) to foreclose the entrants' access to essential facilities, the customers' lock-in and the presence of switching costs. The presence of these issues may hinder the beneficial effects of a liberalization policy.