Michael Grenfell: Should competition authorities intervene in digital markets?

It is standard, even formulaic, for speakers at a conference to say what an honour it is to have been invited to speak there. But for me, at this ITIF / IEA conference, it is no mere platitude to say that.

Speaking at an event hosted by the Institute of Economics Affairs is, for me, a particular honour. Since I was a student in the early 1980s I have watched the work of the IEA with interest and admiration. I understood how in your early wilderness years you were a lonely, consistent, principled – and brave – voice for the economic and policy tenets you believed were good for our society. And then I saw how you were finally heeded and made the political weather, in this country and across the globe. Over the years I, like many others – whether or not they fully agreed with your analyses and your prescriptions – have learned a very great deal from you. It is an immense privilege to be able to make a small contribution to your deliberations today.

As for our co-hosts, ITIF – the Information Technology and Innovation Foundation – I'm afraid I didn't know you all those years ago when I was a student, for the simple reason that you weren't founded till 2006, a quarter of a century later. You bring a fresh perspective, based on studying the relation between public policy and new digital markets.

The fusion of the 2 organisations' specialisms – the IEA's tried and tested economic insights meeting ITIF's insights into the dynamics of the new world of tech – establishes, it seems to me, an excellent basis for our deliberations today, on the subject of competition and digital markets.

I am well aware that there is a widespread view in the tech sector, and perhaps among some here, that competition and antitrust authorities and agencies – including the UK's Competition and Markets Authority (CMA), where I work – are the big bad guys in this story. Like any kind of busybody state regulator – it is said – we interfere in the smooth functioning of markets. And as with all such interventions, we supposedly make things worse for digital markets. Instead of rewarding innovation, and giving incentives to more – on this narrative – the dead hand of bureaucratic interference stymies creativity, depriving the public of the transformational benefits that new tech has delivered and continues to deliver.

Let's start with some basics, and I apologise if what I'm about to say is a bit too obvious, but occasionally I think that, amidst the immense complexity of work in this sector, the obvious does bear repeating. So, to rehearse the basics in this area. The first point is that market competition is hugely beneficial to all in society. Businesses that face effective competition dare not raise prices, or cut down on quality standards, for fear of losing customers to their competitors (and so losing money). So when businesses face effective competition, they have every incentive to keep prices low, to improve quality – and to innovate, so as to make prices more competitive through enhanced efficiency, and so as to be able offer ever-improving products and services. We all benefit as consumers from this process delivered by market competition. And because effective competition spurs businesses to increase efficiency, overall economic productivity improves, which in turn facilitates greater economic growth, and hence more job creation – so delivering enhanced economic well-being for society as a whole.

But the second basic point is that, just because these benefits are outcomes of a free and open competitive market, it doesn't follow that businesses should be wholly left to themselves. Adam Smith understood that businesses left to themselves can, and typically do, seek to protect themselves from competition. They might do it, for example, by choosing to collude rather than compete with each other. As Smith famously expressed it in The Wealth of Nations:

> People of the same trade seldom meet together… but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices.

Adam Smith, The Wealth of Nations, Book 1, Chapter X

And if they do that, competition is diminished or eradicated, and its benefits as we've described them – such as the downward pressure on prices, the upward pressure on quality, and the spur to innovation, that competition delivers – are likewise diminished or eradicated.

Another, no less dangerous, threat to competition arises where a business acquires market power or dominance in a market. This occurs where businesses either are monopolies or are so strong in a market that they are unconstrained in their commercial conduct by fear of losing customers to their competitors, and so – unlike businesses that face effective competition – those businesses with market power or dominance have far less incentive (and sometimes no incentive) to keep prices low, to keep quality high, to innovate. And that way competition and consumers lose out.

So what does all this mean for digital markets and the new economy? Let me say at once: my view – and I think the view of most competition authorities – is that the digital revolution and the emergence of online platforms is overwhelmingly a force for good. It helps competition, it innovates – and consumers benefit. Enormously so.

Let's take online shopping as an example. I appreciate that this is just one aspect of the multifaceted digital economy, but it is one which will perhaps be particularly familiar to most of us, for the simple reason that, as ordinary consumers, millions and millions of us make use of it in our day-to-day lives.

Here are a number of pro-competition, pro-consumer benefits that the emergence of online shopping has delivered:

- First, at a basic practical level, it is really convenient to buy goods at the press of a button or the touch of a screen, from the warmth of one’s home or (in a busy life) on a mobile service while travelling. And of course coronavirus lockdowns made that added convenience a near-necessity – there was almost no other way to buy many products.

- Second, they represent an alternative to traditional ‘bricks-and-mortar’ shopping. This is not to say that online shopping is necessarily better than going to a physical shop. Each has its advantages and disadvantages; for example, it is often easier to browse goods, and feel their quality, in a physical shop, not to mention the pleasure that a shopping trip can bring. But the fact that the 2 alternatives are available is in itself a good thing: the competitive advantage of each enables them to spur each other on to innovate (click-and-collect is an example) and so to make a better offering to the consumer.

- Third, the convenience relates not just to shopping, but to shopping around – that is, we as consumers more easily compare the offerings of competing suppliers, so as to find the best deal. Online, we can shop around at the press of a button or the touch of a screen, without having to walk for hours or to drive miles. And if it’s easier for customers to shop around, the retailers (and the manufacturers who supply them) have to compete that much harder to retain customers – their customers are more choosy, less “captive”. They therefore have to strive harder to keep prices competitive, and quality standards high.

- Another innovation of tech – price comparison websites – facilitate this. If it is easier for customers to compare prices, suppliers have to compete more keenly on price. So too for yet another innovation – online review sites – enabling customers to compare the quality of competing goods and services, and thereby forcing suppliers to compete more keenly on quality too.

So as a competition authority we see digital markets, the tech sector, online commerce and platforms, as essentially good for competition, good for choice, good for consumers, good for innovation, price and quality – and ultimately good for all our economic well-being.

But let’s remember Adam Smith’s warning. If businesses are completely left alone, anti-competitive practices can emerge, and these benefits of market competition will be lost. As competition authorities, we need to be vigilant on this. There is a balance to be struck: we should encourage and support tech, but at the same time we must beware that tech companies don’t overreach in such a way that the benefits they bring are lost to the public.

And the fact is that many of the big online platforms have, or may have, or risk acquiring, market power, where their commercial conduct is not sufficiently constrained by effective competition, allowing them more easily to exploit their customers. And then the temptation is – moreover – to use that market power to reinforce it still further, squeezing out current competitors and blocking the path for new entrants which are potential competitors offering new waves of innovation. If that happens, we as consumers – we as a society – risk losing the benefits of market competition I've described: lower prices, better quality, more choice, greater innovation.

So there are clear and major benefits, for consumers and society, from the tech revolution. And there are also clear and major risks for consumers and society if tech corporations acquire, entrench and exploit market power. The role of competition policy and competition law enforcement is to steer a course where, as a society, we capture the benefits and minimise the risks.

As for the point about competition interventions punishing innovation, let me say this. It is competition that drives innovation, not monopoly. Yes, businesses of course innovate in the hope of earning profits, and ideally monopoly profits! That is the Schumpeterian argument (Joseph Schumpeter, Capitalism, Socialism and Democracy, Harper & Brothers (New York), 1942). But they compete more strongly to be the successful innovator, and therefore innovate more, when they face effective competition. That is the Arrow argument (Kenneth Arrow, 'Economic Welfare and the Allocation of Resources to Invention' in The Rate and Direction of Inventive Activity: Economic and Social Factors, edited by the Universities-National Bureau Committee for Economic Research and the Committee on Economic Growth of the Social Science Research Councils, 609–26, Princeton University Press (Princeton), 1962.). So we are generally unconvinced by arguments that we should leave the tech giants with market power for fear if harming innovation. They will innovate more, and better, the more they face competition.

Let us apply this to the real world of digital markets, and talk about some specifics of what the Competition and Markets Authority (CMA) has been doing in these markets.

Last year, in July 2020, we published the report of our market study into online platforms and digital advertising. The market study had found that two major global tech companies, Google and Facebook (now Meta) – whose services so many of us use, and benefit from – currently have market power in search advertising and display advertising respectively and, in addition, that this is accentuated by the presence of each company at various levels of its advertising supply chain often known as the 'ad tech stack', essentially vertical integration. Our market study noted, among other findings, that these factors make it harder for rivals (and potential competitors) to compete against the two tech giants and that, as a result, those 2 corporations are able to impose exploitative pricing and terms and conditions on both ends of the advertising market that depend on them: publishers of content (for example, newspapers) displayed on the platforms and, at the other end, companies advertising their products on these platforms.

And these kinds of concern underlie some of the cases we are currently investigating under the Competition Act prohibitions on anti-competitive agreements and conduct – cases where we suspect that anti-competitive practices, reinforcing market power, might be occurring. They furnish examples of where, for all the benefits that the digital platforms have brought to consumers, their position and their conduct might now be causing consumer detriment.

- One such phenomenon is where platforms use business customers' data to squeeze out competition – for example by copying products that they can then sell as their own or by gaining access to customer details to market directly to them. Without going into specifics, broadly this kind of issue – the suspected abuse of data obtained by a platform so as to gain a competitive advantage over business rivals – is the subject of an investigation we launched this June concerning Facebook, part of Meta, with the European Commission launching a parallel investigation.

- Another issue has been the announcement by Google that it proposes in effect to abolish third party cookies on Google by way of a 'Google Privacy Sandbox'. The aim is to limit the spread of personal data to others, and it can be seen as a response to demands for greater protection of personal privacy. But it carries the risk that the third parties which would lose access to data as a result are rivals in digital advertising dependent on Google which would thereby be placed at a competitive disadvantage in digital advertising, with a risk of reinforcing market power enjoyed by Google and distorting competition. So in January this year we launched a formal investigation under the Competition Act. Because this has involved taking into account both competition and privacy considerations, I am pleased to say that we have throughout liaised closely and productively with the UK's privacy regulator, the Information Commissioner. And Google has engaged constructively with us; as we have announced, Google is proposing commitments with a view to an agreed resolution to address the CMA's competition concerns. We are not there yet, but the CMA is certainly willing to explore this route.

- And a third is conduct by Apple in relation to iPhones, including specifically Apple requiring the suppliers of apps that appear on the iPhone to receive customers' payments exclusively through its own AppStore payment system, and prohibiting use of competing payment systems. This is a set of issues which other competition jurisdictions are looking at, including in the United States antitrust litigation brought by Epic Games (the developer of Fortnite) against Apple and in the EU an ongoing competition investigation by the European Commission.

In the cases I've mentioned, we have relied on the CMA's existing competition law powers. But because of the need to gather evidence and hear arguments from all interested parties, which is necessarily time-consuming, and because of the procedural rights that are – rightly – accorded to businesses under investigation, applying traditional competition laws is often a slow process. As we all know, digital markets are, by their nature, fast-moving – so if we seek to protect competition by tackling anti-competitive practices in the traditional way, there is a significant risk that, by the time we have a decision (and by the time any appeals are exhausted), the damage to competition will already have been done, and market power will perhaps have been further entrenched.

To meet this concern, the Government – accepting the recommendations of the Furman Review which it commissioned and of the CMA's subsequent market study – is proposing a pro-competition regulatory regime to be implemented by a Digital Markets Unit within the CMA. This would set prescriptive rules for those platforms with particularly strong power in relevant markets – under a defined concept of 'strategic market status' – so that some of the risks to competition can be pre-empted ex ante.

It can't all be done by us at the CMA. Cooperation is needed nationally between public authorities with regulatory responsibility for digital markets, and last year the Digital Regulation Cooperation Forum was established, enabling us to work closely alongside other regulators with a strong interest in digital markets, including Ofcom, the Information Commissioner and the Financial Conduct Authority. Cooperation is also needed with fellow authorities internationally – the tech giants operate globally and we often need to tackle any abuses globally

I said earlier that this is about a balance between supporting tech and interfering when it overreaches. But actually that's not quite the right way to put it. As upholders of market competition, we welcome the innovation that the dynamic businesses in the tech sector have brought. They benefit consumers and the economy as a whole. We agree with those who warn that we need to be careful that our interventions don't weaken incentives to innovation. But it is precisely because we want to incentivise dynamic businesses and innovation that we are concerned about the risk that firms with market power behave in such a way as to reinforce that market power, creating barriers to new innovators entering the markets, and reducing or even removing the possibilities of and incentives for the kind of innovation that the tech revolution promises. And for this reason we will continue, with vigour, to address anti-competitive practices that threaten market competition and new entry by a fresh wave of dynamic innovators, and that threaten the benefits to consumers, to choice, to innovation, and to all of us in society that market competition – and digital markets in particular – can offer.

Dr Michael Grenfell is an Executive Director on the Board of the Competition and Markets Authority (CMA) – the UK's primary competition and consumer protection agency – where he is responsible for enforcement of competition and consumer protection laws. He joined the CMA in January 2014, where he was initially a Senior Director for competition in the regulated sectors, before moving to his current position in July 2015. Before he joined the CMA, he was a solicitor in private practice for 25 years, specialising in UK and EU competition law and sector regulation, including, from 1998 to 2013, as a Partner at the international law firm Norton Rose Fulbright. He has written and broadcast widely on competition, regulatory and consumer issues, and was co-author of Coleman and Grenfell on The Competition Act 1998 (OUP). He has an M.A. in history and law from Cambridge University, and a Ph.D in political thought from the London School of Economics.