Accelerating competition for greater competitiveness

Margarida Matos Rosa

November 2024[1]

Abstract

This paper examines the emerging shift toward *ex ante* regulation in competition policy, with particular focus on digital markets and labor mobility. Through analysis of recent regulatory initiatives including the Digital Markets Act and restrictions on non-compete clauses, it indicates how targeted regulatory intervention can accelerate competitive outcomes in markets characterized by entrenched market power. It is argued that while traditional *ex post* competition enforcement remains essential, complementary *ex ante* approaches may more efficiently address structural competition problems in specific contexts.

1. Introduction

Microeconomic theory indicates that when markets are in a perfect state of competition, openness and equilibrium, regulation is unnecessary. Given that such state is a desirable, yet virtually unattainable objective, markets continue to need regulation and competition enforcement mechanisms which both compensate for imperfections, or market failures. Traditionally, this has translated into a regulatory framework in sectors such as communications, energy or finance, alongside competition enforcement. This is examined in section 2 of the paper.

A typical feature of competition enforcement, if we exclude merger reviews, is that it occurs *ex post*, i.e. competition authorities investigate firms' behavior which happened in a recent past. Such behavior ranges from abuse of dominance to cartels and exchange of information. In many instances, investigations start with leniency requests from firms having participated in a cartel. Additionally, claims from excluded competitors, complaints by consumers, and market enquiries by competition authorities can also trigger investigations.

However, antitrust proceedings typically face a long timeline before reaching a final decision in court. Digital competition cases not been an exception. This has meant that contenders for such markets have been weakened, or driven out, by roughly a decade-long foreclosure.

Other markets can exhibit features of weakened competion conditions. One such market, no other than labor, has recently been under scrutiny by policy-makers. The reasons for concern differ from those in digital markets. Indeed, the policy driver in this case is the need to restore labor mobility, a pre-requisite for competitive markets.

Both labor and digital markets are the object of fierce discussion about whether their shortcomings should be addressed by *ex ante* regulation. These issues are examined in sections 3 to 4 below.

[1] Revised in March 2025.

2. When is regulation needed

Microeconomic theory indicates that a *perfect market* is defined by certain theoretical conditions known as *perfect competition*[2], or *atomized competition*. In theoretical models, this equilibrium state, referred to as Pareto optimality, is achieved when the supply of a particular product or service intersects with its demand at an equilibrium price point. This state also means that there is efficiency both in allocation of resources and in production.

Because perfect competition rarely exists, the theory of imperfect competition was later created[3] to explain a more realistic state of markets, somewhere between perfect competition and a monopoly. In this theory, firms do not produce identical goods, but rather "goods that are close substitutes for one another". Moreover, if there is collusion between firms, i.e. cartels, competition will not be perfect.

But first, let us go back to perfect competition and assess the necessary conditions to assume perfect competition. After all, competition policy will intervene to restore such conditions. These include having:

- many buyers and sellers (i.e. atomized demand and supply) where no participant in the market has power relative to prices, i.e. they are price-takers;
- homogeneous products or services, i.e. perfect or close substitutes, so that a price increase in one good will result in a shift to another good;
- buyers which are rational, seeking to maximize utility;
- sellers which are rational, seeking to maximize profits;
- no barriers to entry, nor exit, in the market;
- no externalities;
- no economies of scale nor network effects;
- perfect factor mobility, including labor;
- perfect information.

Needless to say, in concentrated markets, i.e. monopolies and oligopolies, firms' profits are higher. New entrants to the market may be prevented from competing because of abusive behavior from dominant firms. For this reason, governments have empowered competition agencies to deter and sanction firms that collude in pricing or production, or abuse their market power. Such agencies also identify barriers to entry, expansion, and exit, proposing measures to eradicate those which are unnecessary.

In other words, competition authorities strive to make markets more competitive because this will bring more welfare to consumers (including firms, which can also be consumers) and an efficient allocation of scarce resources. With lower barriers, new firms can enter the market, achieving a state that is closer to perfect competition.

---

[2] The theory of perfect competition was first devised at the end of the 19th century by French political economist Léon Walras. In the mid 20th century, the theory was further enhanced by Kenneth Arrow and Gérard Debreu.

[3] Edward Chamberlain published "Monopolistic Competition" in 1933.

But this near perfect state of competition can take a long time to materialize[4]. This is why sector regulation is needed: it can open markets traditionally dominated by a single firm, or just a few of them. This is the case in network industries (de Streel and Larouche, 2020), often former state-owned monopolies, such as telecommunications[5], energy, transportation, postal services. Regulation acts as a much needed catalyzer for new entrant firms to emerge. Ultimately, although it may sound utopian, if pro-competitive sector regulation is effective, it may tend towards being reduced. This would be the case once competitive conditions in regulated markets strengthen, and supply is atomized.

Competition authorities, in turn, are concerned with market failures, which are suboptimal market outcomes. They may be due to several factors (Motta and Peitz, 2020), including economies of scale or scope, direct or indirect network effects, switching costs and lock-in effects, asymmetric information, and behavioral biases by consumers.

Firms' behavior may aggravate such failures through collusion, vertical agreements, contractual clauses, and business practices deemed abusive. This is why another aspect of competition authorities' mission is to investigate cartels and abuses of dominant position, and to prevent mergers that would significantly reduce competition in the market. Moreover, competition authorities can review government subsidies so that these do not distort competition in the market.

3. *Ex ante* regulation as a competition tool

It was not without much resistance that a new approach to competition started to make its way in the mid-2010s. This was due to the emergence of digital markets, which exhibit unique features (Autoridade da Concorrência, 2019). Indeed, such markets are characterized by the large volume and diversity of data they collect about their users, and the strong network effects between different groups of market participants – the sides of the market. Network effects refer to the additional value of joining or using a multi-sided platform because of an increase in the number of users or quantities consumed. They thus capture the effect that a user of a product or service has on the value of the product/service for other users.

Digital platforms can be integrated in ecosystems that supply a wide range of products and services. Many of these do not require a monetary payment. Users pay with their usage data, captured by these services. Another economic rationale underlying these ecosystems is to capture users and their attention (Prat and Valletti, 2022), so as to direct them to monetized markets of the ecosystem, such as online advertising.

These characteristics of digital ecosystems lead to winner-takes-all situations, effectively closing the market to contenders. With some of this in mind, the European Commission opened its first

---

[4] Economic regulation can be defined (Dunne, 2015) as "any State-imposed, positive, coercive alteration of – or derogation from – the operation of the free market in a sector, typically undertaken in order to correct market defects of an economic nature, and to be distinguished from regulation that pursues a predominantly social aim". In these situations, regulation is adopted to correct market failures in given markets. Absent such regulation, the persistence of monopolistic and oligopolistic market structures may extend beyond socially optimal timeframes.

[5] The regulation of telecommunications provides a good example of pro-competitive, *ex ante*, sector regulation. Once a state monopoly, the incumbent firm may continue to benefit from structural bottlenecks, namely legacy infrastructure. Hence the need for regulation that grants access to networks and allow for new entrants to succeed.

investigations in the early 2010s. However, these became protracted, in part due to the novel aspects of dominance in digital markets. Then ensued a perhaps lengthier path in the European courts. As an example, the Google Shopping case, initiated in 2010, was decided by the Commission in 2017 and confirmed by the European Court of Justice (ECJ) in September 2024. During this 14 year-period, some of Google Shopping's competitors closed, while potential competitors may have been discouraged to enter the business of comparison shopping services. In other words, Google abused its dominant position in the search engine market to benefit its own shopping services by displaying these first in Google's search results. Google had thus abused its dominant position to the detriment of its own competitors.

This investigation had significant policy implications. It established, for the European Commission, a need for *ex ante* regulation in digital platforms. Other cases ensued over the decade, confirming, at the Commission, this need. The experience obtained by the European Commission and European national competition authorities yielded, in 2022, an EU strategy for digital markets' wrongful practices. And so, *ex ante* regulation was established both through the Digital Markets Act (DMA) and the Digital Services Act[6] (DSA).

The purpose of the DMA, which as *ex ante* legislation is an originality in the competition field, is to ensure contestability and fairness in EU digital markets (European Commission, n.d.). It translates into reducing barriers to entry, and balancing market power between gatekeepers and their business users. To consumers, such objectives are expected to induce more innovation and choice in digital ecosystems.

The Digital Markets Act establishes that several practices do not need to go through *ex post* investigations: because their harm is presumed, they are forbidden *ex ante*. So-called gatekeepers[7], are unavoidable trading partners. They are dominant firms who determine access to platforms. This is why, under the DMA, they are prevented from deploying *self-preferencing*, i.e. placing their own products ahead of other, similar, competitor products. They are also forbidden to prevent users from connecting with business providers outside of their platform, and to prevent users from un-installing any pre-installed software or app if they so wish.

As *ex ante,* or preemptive regulation, the DMA has the undisputable advantage of accelerating compliance, thus decreasing the incidence of anti-competitive behavior. This is due primarily to the fact that the burden of proof is shifted from the European Commission to gatekeepers, as they need to demonstrate compliance. The implementation *of ex ante* regulation in digital markets was consequently deemed more efficient than awaiting the resolution of resource-intensive and protracted competition proceedings.

The DMA is expected to allow for a competitive digital ecosystem to develop, serving as a swift complement to EU competition law. It is seen a faster means of remediating certain types of anti-competitive behavior in digital markets. Yet, *ex ante* regulation presents a notable limitation: its potential inadequacy in adapting to rapid developments in the digital business, and a possible failure to capture novel anti-competitive behavior from firms. This means that *ex post*, competition enforcement will remain the "tool of last resort" for competition infringements. Moreover, several digital markets remain outside of the scope of the DMA, but within the reach of national competition authorities (Matos Rosa, 2024).

---

[6] The Digital Services Act is oriented towards consumer protection, which is not always in the remit of competition authorities. It is, therefore, not addressed here.

[7] Gatekeepers are large digital platforms providing any of a pre-defined set of digital services ('core platform services'), such as online search engines, app stores, and messenger services.

4. Non-compete clauses: gathering momentum

As seen in section 2 above, one of the conditions for perfect competition in each market is labor mobility. Competition policy thus plays a role in keeping labor markets open and competitive by initiating antitrust proceedings on cases of no-poach agreements among competitor firms. Such agreements, by which companies agree not to poach or hire workers from each other, restrict the mobility of workers and can harm competition in several dimensions (Autoridade da Concorrência, 2021)[8]. Moreover, they limit the individual freedom of companies to define their strategic business conditions, including hiring or setting wage conditions.

No poach agreements amount to labor market collusion: they are illegal from a competition law perspective. As such, they can be pursued by competition authorities. And yet, another type of restriction to labor mobility, outside of the competition realm, is under scrutiny.

Policy-makers are increasingly aware of shortcomings in the labor market when locked by individual contracts. *Non-compete clauses* are deemed harmful to workers, in ways that go beyond the scope of competition policy. They can also be viewed as protective of firms' *investment* in workers and of trade secrets[9]. Nevertheless, a more comprehensive analysis tends to lead to the conclusion that such clauses cause harm to competitive conditions in a given market, reducing innovation at firms' level, decreasing the competitiveness of a given sector, and having a broader negative impact on economic growth (Australian Treasury, 2024).

This may pave the way for a ban or restriction of non-compete clauses. Just as with digital markets, *ex ante* regulation may more efficiently deal with harms to competition. With this in mind, the U.S.

[8] These agreements can:

a. Introduce inefficiency in the downstream markets, by distorting the allocation of the labour input. This loss of efficiency may imply a lower quantity/quality pair downstream. Limit production in the downstream markets. They can artificially limit the amount of labour available to each competitor at any given time, restricting their ability to expand production as a strategic reaction in the downstream market.
b. Lead to a decline in the quality and/or variety of products and services provided to consumers, as well as reduce innovation in sectors where labour mobility is a relevant element in the innovation process.
c. Have an instrumental role in the implementation of a market sharing strategy. In particular, if the companies' business model is based on customer portfolios and competitors agree not to dispute each other's customers.
d. Have an instrumental role in the implementation of a strategy that aims to promote specialization, among competing companies. E.g., if it consists of an agreement to allocate areas of expertise, avoiding the recruitment of a specialized workforce.
e. Signal that the interaction between competitors in the downstream market is not competitive.
f. Amount to an indirect wage fixing strategy, by indirectly affecting the prices of the inputs in question (wages and other forms of compensation).
g. Dampen investment in human capital, leading to a reduction in the quantity and/or quality of the labour supply in the future.

[9] Non-compete clauses can be embedded in merger deals through what is known as *ancillary clauses*. While these can be approved by competition authorities under strict conditions, it should be stressed that they should not encompass a larger-than-needed number of key individuals, nor to be valid through a longer-than-needed period.

Federal Trade Commission issued a final rule[10] in April 2024 banning non-compete clauses in employee contracts. It estimated the decision would cover 18% of U.S. workers and lead to new business formation growing by 2.7% per year.

5. Concluding thoughts

Much like sector regulation, *ex ante* rules that force an immediate improvement of competitive conditions in areas such as the digital sector or labor markets can be viewed as desirable. This is true when they contribute to unlock entrenched markets that show little or no progress towards being more competitive. *Ex ante* rules can solve structural market inefficiencies and accelerate a change in the non-competitive *status quo*. As we witness the impact of the DMA and other *ex ante* digital policies over the coming years, perhaps future research may further demonstrate such positive outcomes. As to non-compete clauses, enlarging empirical research to additional geographical areas may also prove useful for the policy debate.

For the time being, the rationale for such policy intervention finds support in the fact that bringing faster competitive conditions to markets is conducive to improved micro and macroeconomic conditions.

For policy-makers, relying on a more assertive competition policy is a significant lever for greater productivity, increased global competitiveness and innovation, and more resilient economic growth.

References

Acemoglu, D. 2024. "The Simple Macroeconomics of Artificial Intelligence", *Economic Policy, 2024; eiae042,* *https://doi.org/10.1093/epolic/eiae042*

Almunia, J. 2010. *Competition v. Regulation: where do the roles of sector specific and competition regulators begin and end?"*, Speech. European Commission: https://ec.europa.eu/commission/presscorner/api/files/document/print/en/speech_10_121/SPEECH_10_121_EN.pdf

Arrow, K., and Debreu G. 1954, Existence of an Equilibrium for a Competitive Economy, Econometrica Vol. 22, No. 3 (Jul. 1954), pp. 265-290 (26 pages). The Econometric Society.

Australian Treasury. 2024. Non-competes and other restraints: understanding the impacts on jobs, business and productivity. Issues paper. Competition Review. April 2024. https://treasury.gov.au/sites/default/files/2024-04/c2024-514668-issues-paper.pdf

Autoridade da Concorrência. 2021. *Labour market agreements and competition policy. Issues paper*. https://www.concorrencia.pt/sites/default/files/Issues%20Paper_Labour%20Market%20Agreements%20and%20Competition%20Policy.pdf

[10] The rule was challenged by a district court in August 2024, which issued an order stopping the FTC from enforcing the rule on September 4. The FTC stated then that it was considering an appeal and that the decision did not prevent the FTC from addressing non-compete clauses through case-by-case enforcement actions. However, under the current administration and FTC leadership, this has become significantly unlikely.

Autoridade da Concorrência. 2019. *Digital ecosystems, big data and algorithms*. Issues paper. https://www.concorrencia.pt/sites/default/files/processos/epr/Digital%20Ecosystems%2C%20Big%20Data%20and%20Algorithms%20-%20Issues%20Paper.pdf

Cabral, L. et al. 2021. *The EU Digital Markets Act - A report from a Panel of Economic Experts*, http://dx.doi.org/doi:10.2760/139337.

De Streel, A., and Larouche, P. 2020. *Interplay between the new competition tool and sector regulation*. Expert study. European Commission: https://competition-policy.ec.europa.eu/system/files/2021-03/kd0120577enn.pdf

Dunne, N. (2015), *Competition Law and Economic Regulation: Making and Managing Markets*, Cambridge University Press.

European Commission, n.d. *Regulation (EU) 2022/1925 of the European Parliament and the Council of 14 September 2022, relative to the contestability and fairness in markets in the digital sector, altering Directives (EU) 2019/1937 e (EU) 2020/1828 (Digital Markets Act)*: https://eur-lex.europa.eu/legal-content/PT/TXT/HTML/?uri=CELEX:32022R1925&from=EN

European Commission. N.d. The Digital Markets Act: ensuring fair and open digital markets. https://commission.europa.eu/strategy-and-policy/priorities-2019-2024/europe-fit-digital-age/digital-markets-act-ensuring-fair-and-open-digital-markets_en

European Commission. N.d. Case AT.39740: Google Search (Shopping). https://competition-cases.ec.europa.eu/cases/AT.39740

Federal Trade Commission. 2024. *FTC announces rule banning noncompetes*. Press release. April 23, 2024. https://www.ftc.gov/news-events/news/press-releases/2024/04/ftc-announces-rule-banning-noncompetes

Matos Rosa, M. 2024. *Digital markets: why extended enforcement is expected*. Journal of Antitrust Enforcement. Oxford University Press. https://doi.org/10.1093/jaenfo/jnae008.

Motta, M. 2004. Competition policy: theory and practice. Cambridge University Press.

Motta, M. and Peitz, M. 2020. Intervention triggers and underlying theories of harm. Expert study. European Commission. https://competition-policy.ec.europa.eu/system/files/2021-03/kd0420575enn.pdf

OECD. 2021. *Ex ante regulation and competition in digital markets:* https://www.oecd.org/daf/competition/ex-ante-regulation-and-competition-in-digital-markets-2021.pdf

Prat, A. and Valletti, T. 2022. *Attention Oligopoly*. American Economic Journal: Microeconomics. Vol. 14, No 3, August 2022. https://www.aeaweb.org/articles?id=10.1257/mic.20200134

U.S. Department of Justice. 2007. *The role of competition agencies in regulated sectors*. Speech by S. Chemtob: https://www.justice.gov/atr/file/519376/dl