European Competition Day
Brno, Czech Republic

14 May 2009

"Keeping Markets working effectively: Europe's challenge in recessionary times"

Philip Lowe
Director General
DG Competition

Ladies and Gentlemen,

DG Competition's objective is to make markets work well for the benefit of business and consumers. Even though they may formulate that objective differently, I think that it is one shared by all the National Competition Authorities that apply EC competition law and form part of the ECN.

In **general**, we agree that markets are the best way to organise the delivery of goods and services to society at the best conditions, i.e. in terms of price, quality, choice and innovation. We work to achieve effective markets through enforcing our antitrust, cartel, mergers and state aid rules. We also work with other parts of the Commission or national governments to achieve competition-friendly regulation, where necessary.

What market players expect us to deliver is a level playing field, predictability in terms of our enforcement action and timely decision-making.

In **times of crisis**, however, events can make the continuity of existing business models and market functioning unsustainable without corrective action. Normally corrective action would be taken by the affected company itself – for instance by amending its business model. But a crisis such as the one we are experiencing might also justify other forms of intervention, applicable to all companies, such as state aid.

State aid to the financial sector

Early on in the crisis Member States decided it was necessary to inject large amounts of state aid to the financial sector. The European Commission and DG Competition in particular, suddenly found itself on a front line because of our powers to scrutinise State aid.

From the start of the crisis, our objective in applying the State aid rules was to preserve the level playing field for European banks, by preserving competition between banks in different Member States and between banks that had different risk profiles. Ultimately our aim has been to ensure that Member State aid measures would not undo all the benefits of the Single Market, and would not distort competition to the extent that a return to normal market functioning would be delayed.

At the same time, it has been crucial that we provide a rapid response to Member State rescue measures for individual banks and national schemes to support the banking sector – to provide legal certainty and help restore financial stability.

In the interests of speed and efficiency we have been flexible on process – but firm on the principles underpinning the state aid rules.

I strongly believe that those principles have helped lay the groundwork for economic recovery, which we all hope will not take too long.

In the last six months we have adopted over 50 measures approving individual aid measures and schemes, as well as three sets of guidelines setting out the principles applicable (General guidance, Recapitalisation and Impaired Assets). We are currently working on guidelines covering the next – and very important – phase, namely restructuring.

If we allow piecemeal recapitalisation of banks without structural repair measures it will merely lead to further bail-outs, perpetuate competition distortions, artificially keep in place inefficient market structures and block the way to long-term viability.

Our aim is to ensure that banks return to profitability on the basis of sustainable business models. This will allow them to compete successfully without state aid and help restore market trust and confidence in the financial system, which in turn will result in lending to the real economy being resumed.

In addition long term State support could lead to serious moral hazard by changing the incentives of aid recipients and their competitors, and affecting their risk taking behaviour.

Aside from restoring stability to the banking sector, the second most difficult process that we are going to have to face in coming months, is the need for regulatory reform.

As announced in its 4th March 2009 Communication to the European Council on 'Driving the European Recovery', the Commission intends to propose a regulatory reform programme to put in place a viable and stable framework for financial markets with all necessary controls of systemic risks.

This regulatory programme and the restructuring of banks are complementary routes to the same goal of the return to viability of individual banks and of the

European banking sector as a whole. Banks must operate on the basis of sound business models in a regulatory framework in which they can compete on the merits with balanced incentives without state aid. They must be able to exit the market or restructure when they are no longer competitive, without triggering the systemic consequences that have characterized the current crisis.

State aid to the "real" economy

State aid issues are of course not confined to the financial sector. Even before the end of last year, the effects of the credit crisis were being felt in the “real" economy and Member States began to consider what measures they could take to tackle that crisis too.

The European state aid rules are designed to support measures for jobs and growth. State aid can bring sustainable benefits for a whole region, a whole sector or the whole economy if it raises productivity (e.g. aid for R&D&I), meets needs the market does not meet (e.g. risk capital for SMEs), or manages transition and minimises the social costs of economic change (e.g. aid for employment or training).

As part of reforms in recent years, we have significantly simplified and streamlined state aid rules. The General Block Exemption Regulation offers Member States the possibility of granting 26 types of aid with minimal administrative burden. These include: access to funds for risk capital, R&D&I, training, environmental protection, disadvantaged regions and female entrepreneurs.

Specifically in response to the current crisis, in November 2008 the Commission adopted a "European Economic Recovery Plan" – as part of that initiative, on 17 December 2008 the Commission adopted a Temporary Framework for state aid rules to help Member States tackle the effects of the credit squeeze on the real economy. These measures are in place until 2010.

The purpose of the scheme is to give Member States flexibility in providing aid to tackle the crisis, particularly for SMEs. For instance, it allows companies with liquidity problems resulting from the crisis to benefit from temporary grants, it gives Member States scope to guarantee loans to businesses, and encourages companies to continue to invest for a sustainable future (development of "green" products).

Again, our aim has been to be flexible on process – by facilitating national umbrella schemes – but firm on the underlying principles. It is important that we resist pressures to allow Member States to adopt protectionist measures and provide long term support to ailing national companies, contrary to the principles of fair competition between companies throughout Europe.

Mergers and the crisis

To date, the European Commission has seen only a relatively limited number of mergers directly related to banking (or other financial firm) rescue and restructuring. Some of these – such as the Lloyds/HBOS merger in the UK, and the

Commerzbank/Dresdner merger in Germany - have been dealt with by National Competition Authorities.

It is also likely that as the worst of the financial sector turbulence calms down, there will be further mergers. The same applies to other areas of the real economy where the effects of the economic downturn may result in some consolidation.

DG Competition's priority is to ensure that we maintain effective scrutiny of mergers in the EU for competition problems. The purpose of our competition test is to ensure that consumer welfare is preserved – both in the shorter term, maintaining financial and economic stability, **and** in the mid- to long-term, by preserving competitive market structures.

We believe that the EC Merger Regulation constitutes an appropriate and sufficiently flexible tool for merger control enforcement in times of crisis as well as in normal times. But, of course, the crisis does throw up some procedural and substantive challenges. Some of these are directly linked to Member State intervention in the economy as a result of the crisis.

In terms of **procedure**, how do we deal with nationalisations? The EC Treaty is neutral on the question of private or public ownership; but, we have to ensure that nationalisation measures comply with the Treaty rules on competition. For a start, we have to assess whether any nationalisation measure is a merger within the meaning of our merger rules – that is something we assess very carefully, on a case-by-case basis.

Do we need to adjust the timing of the review process in times of crisis? Timing of the review process is always important to the merging parties and may be even more pressing in case of rescue mergers. However, in order to carry out an effective and thorough review of whether any particular merger is likely to give rise to competition concerns, we need enough time. And under our rules, if necessary we can allow the parties to derogate from the normal standstill obligation, and implement a merger immediately, pending the outcome of our review.

In terms of our **substantive assessment** of the competition impact of a merger in crisis conditions, again, we see no need to adjust our existing rules. The EC Merger Regulation already allows the Commission to take into account rapidly evolving market conditions in its competition assessment. It is sometimes argued that in times of crisis, it would be appropriate for the Commission to be able to take into account other, wider, considerations, such as employment. However, experience has shown that a legal instrument such as the EC Merger Regulation is most effective when it is directed to one single objective. I do not see how it would be possible to agree on the wider objectives that should be taken into account in our assessment. Nor indeed, do I see how it would be possible to agree on how these objectives should be implemented. The test would just be too complex.

Under the EC Merger Regulation Article 21 Member States do, of course, have the right to prohibit on public policy grounds mergers that we might otherwise approve. But they do not have the right to clear mergers that we would prohibit on competition grounds.

Where applicable, we can also take into account a failing firm defence. We would of course examine any such defence very carefully – and it would have to meet strict conditions.

Interestingly, what the crisis has disclosed is a possible difference of approach between the Commission and some NCAs in relation to the issues of public policy considerations in crisis mergers and the failing firm defence.

Antitrust policy and the crisis

In recent years we have made **cartels** – arguably the most harmful type of competition infringement – a priority. We have implemented a comprehensive policy framework for cartels, including a very successful leniency programme and an effective fining policy. This has been a priority we have shared with most if not all members of the ECN.

As a result we have a very strong enforcement record against cartels. That is not about to change because of the crisis.

It may be unavoidable that in times of recession companies will suffer. There is a risk of reduced profits and overcapacity – but this cannot justify collective action through so-called "crisis cartels" aiming to reduce capacity or production. Ultimately it is the consumer who pays the price of cartels like these – or indeed, any other kind of cartel.

It is true though that the Commission does have the option of reducing the cartel fine it would impose if the company in question is unable to pay. A reduction of this kind could only be granted if paying the fine would endanger the economic viability of the company and cause its assets to lose all their value. While this situation might occur in the context of the crisis, we would make an extremely careful assessment before granting any such reduction.

Of course, collective action can take other forms, some of which may be less harmful than cartels. However, any such cooperation would have to satisfy the EC competition rules – it would have to fulfil the requirements foreseen by Article 81(3). And we will of course view any argument related to the economic crisis with considerable scepticism. As I have already said, it seems extremely unlikely that any agreement on prices or output could be justified.

We have also been putting a lot of effort into action against unilateral conduct such as **abuses of dominance**. We have put our enforcement activities on a sound economic footing and are focussing our resources on those infringements that cause the most harm to consumers. In December of last year we adopted our Guidance on enforcement priorities in relation to exclusionary abuses of dominance, but we have been applying the principles underlying the Guidance for some time, notably in IT cases such as the Telefonica margin squeeze case, in Microsoft, and in yesterday's Intel decision. We are also focussing on the energy sector, with the E.On and RWE commitments decisions, and other ongoing cases.

I believe that our focus on eliminating consumer harm – rather than protecting inefficient competitors – will stand us in good stead in the current crisis.

These are all sectors which are very important for consumers and for the competitiveness of European business.

In times of economic recession, allowing consumers to make the best use of their buying power is essential. The recession cannot be an excuse for the burden of the downturn to be transferred, through cartels and abusive practices from companies which are doing badly, to consumers in general.

Conclusions – lessons from the crisis

You will have gathered that I think the best way out of the current crisis is a robust and rigorous competition policy.

Having said that, the crisis has and continues to have an effect on the way we go about enforcing competition policy. Naturally, governments and companies alike are faced with very real constraints as a result of the crisis. We have to make sure that we don't put procedural obstacles in the way of necessary and urgent rescue measures which aim to stabilise our economies. But equally, we would be failing at our job, and failing the European consumers and the economy as a whole, if we did not ensure that these measures comply with competition principles. The route to recovery lies with competitive markets, not markets where inefficient and ailing companies are propped up by state support, illegal cartels or abuses of market power, nor markets where consumers pay to support structures which are not sustainable.

In order to ensure competitive markets, we also need competition-friendly regulation. We need to work hard to export the principles of open and fair competition to regulatory initiatives. We need to ensure that any future regulatory initiatives in the financial sector – whether at global or European level – take account of competition principles. Again, the same applies to other sectors of the economy, as well as to horizontal measures such as consumer protection initiatives that cut across many areas.

I don't think that this is a new idea – it is something we have been working on at the European Commission for several years, in the context of the Lisbon Agenda for competitiveness and growth - but the importance of the idea is highlighted by the current crisis.