

Interview with Dr. Hiroshi Ohashi, Professor of Economics, University of Tokyo

The Digital Economy & Competition Policy

By Japan SPOTLIGHT

Competition policy is a key infrastructure in a market economy. It seeks to prevent monopoly power and achieve free and fair competition. In a perfectly competitive market, where price mechanisms function well, deadweight loss is eliminated and economic welfare in society is maximized. In the real world, however, the market is often distorted in the presence of market power. We observe many such cases in the brick-and-mortar industries, and some claim that the situation is even worse in the digital economy.

The Organization for Economic Cooperation and Development (OECD), the Paris-based international organization, has held discussions on a variety of topics related to innovation and competition over the last decade. In January 2018, it organized a workshop for competition policy officials on digital-related topics, in light of growing concerns over competition in major digital markets, including platform-based business models being rendered more complex due to network effects and demand-side economies of scale. Is the digital economy heading for pro-competition or anti-competition? How are these concerns to be moderated? We are at the outset of an era when the digital revolution is proceeding at an unprecedented pace, much faster than any other technological revolution in the past.

We interviewed Dr. Hiroshi Ohashi, professor of Economics at the University of Tokyo and a distinguished expert on economics and competition policy in Japan, about this rapidly progressing technology's impact on competition policy.

(Interviewed on July 23, 2018)

New Issues Arising from Digital Economy in Competition Policy

JS: Digital technology has started to influence many economic, social and even political aspects of our life. We call it the Fourth Industrial Revolution. Many economists, including in the OECD, say that among its effects, the impact on competition policy should not be neglected. What consequences do you think the digital economy will have for competition policy? Will existing competition policies and laws work well in addressing this issue? If not, how should we adjust our competition policies and laws to the digital economy?

Ohashi: Existing competition policies and related laws face three new challenges.

The first is the rapid and unprecedented rates of innovation, in



Dr. Hiroshi Ohashi

particular related to artificial intelligence (AI) and Big Data. New technology advances at nearly exponential rates, and the changes brought about by innovation have big impacts on every facet of our daily lives, both for good and for worse. This rapid progress of technology is primarily prompted by the availability of real time data, obtained through web browsing, smartphone and GPS usages, and so forth. Detailed and unstructured Big Data are being actively utilized for ventures and new businesses to create new services and products.

The second is the emergence of big platform providers (such as GAFA — i.e. Google, Apple, Facebook and Amazon — and BAT — Baidu, Alibaba and Tencent) that find it easier to collect real-time data. These companies have begun to compete with the retail business, such as Walmart, as they directly mediate between producers and consumers through the

Internet. Competition between the real world and digitalized cyberspace is one of the big issues to be discussed in the light of

competition and commercial laws and their enforcement.

By the way, some say that department stores are also mediators between producers and consumers, so why should we care so much about Internet transactions? In the case of department stores, sellers and buyers are physically on the same spots. However, in digital platforms, there is something that only the platform operators can observe: activities such as who purchases what, and which websites particular buyers search through to reach their purchases or non-purchases. Those activities are recorded on their platform domain, and such information in the real-time Big Data has not been shared with other players involved in the platform. Thus, the platformers could have strong negotiating power by taking advantage of the informational asymmetry between platform operator and those companies who use the platform, mostly SMEs.

Let us take an example. Uber provides a matching service for taxi rides among passengers and taxi companies in the United States. Should a traffic accident involving Uber happen, Uber might not be responsible for the accident in Japan, because it has no legal responsibility for taxi operations under the matching service. Such a legal framework differs from one nation to another, but digital platform operators' activities are borderless, and goods and services and also data are transacted beyond borders. While we are beginning to talk about this, we have little international consensus or rules that handle many such issues involved in digital transactions. How we approach sharing services in terms of the existing legal framework is one of the urgent issues facing us.

The same question can be asked in competition policy. Issues such as platformers monopolizing data or increasing their market share in a certain service are those on which we don't have clear answers yet. For example, as a company monopolizes data, it can enlarge its business very easily as data and intangibles are scalable. Thus, the economic impacts that the platform operator wields would spread at a significant speed, so much so that the existing brick-and-mortar business shops could possibly be expelled from the market. In reality, there are more and more producers selling their products only on the Internet, and not even displaying them at shops, to avoid expensive transaction costs. We are coming closer to a world in which you have to buy goods only through a platform like Amazon.

Strong network effects imbedded in the platform business have double blades. One blade is to improve social efficiency: as the platform business gets bigger, the platform itself would become more efficient in operation to the level where a brick-and-mortar business could never reach. This leads to the other blade, which is socially detrimental: because of the demand-side economies of



scale, the platform business tends to become monopolistic. A market becomes winner-takes-all. Without facing viable competitive platforms, the successful and monopolizing platform would become a focus of attention with regard to anti-competitive conduct. As the single platform could build up a sovereign state, a ruling platform operator for example would conquer the whole business by forcing each business entity to follow its Non-Disclosure Agreement (NDA).

All this mentioned above means that a platform has become almost a public infrastructure. This leads to my third issue. Since this public infrastructure is run by a private business, we may have to discuss the issue of regulation for public utilities like gas and electricity. In Europe, they are now trying to adopt a discipline to put the conditions for transactions on equal and fair ground with the SME businesses involved in platforms. They aim at preventing any arbitrary change of contracts with those SMEs in favor of the platform operator. In my view, the idea behind this discipline being introduced is to make sure that the platform provided is operated in a transparent and fair way. Of course, there may be another interest of their own in the light of their industrial policy. Europe may have been interested in creating a digital platform for the interest of their industries. Thus, this issue of rulemaking for the platform business could become an issue of competition among nations' industrial policies.

Need for International Rules on Platform Business

JS: In that case, will we need to discuss and adopt some international rules for the platform business at organizations like the OECD?

Ohashi: It is not easy to achieve an international consensus at this moment, as each nation has its own perspective and interests on this issue. In my view, the Japanese perspective seems to be closer to the European one. Though our anti-trust act was made after US law, in terms of its practice, our regulators are closer to the European outlook. Our views on platforms would be also close to the European one, and I think European policy development in this domain could be helpful to the Japanese policy discussion as well. On the other hand, the US view on free flow of data is an important concept for us to keep in mind. How to strike a balance between the concept of free data flow and that of the General Data Protection Regulation (GDPR) is a crucial point for us to think about. By the way, China also has a different perspective on this issue, as it does not appear to have reciprocity in terms of free flow of data: it protects its domestic market while asking the other nations for free flows.

JS: Through a variety of informal international gatherings, we would need to achieve a consensus by taking advantage of peer review pressure.

Ohashi: We should work on achieving consensus, preferably at a much faster pace. Though the concept of free flow of data is to be respected, in the light of competition law it would be necessary to avoid excessive dominance by data suppliers. Consumer rights regarding data must be secured, since the data owned by the suppliers originally come from the personal information of consumers. It is not straightforward to find an answer as to whether such data are to be monopolized by the platform operators or by consumers. This is probably the philosophy behind European law for protecting personal information, recently legislated as the GDPR, and it also depends on how we frame our growth strategy utilizing free flow of data.

JS: After having heard your views, I think there would be a similarity between Big Data and electricity. Will we need regulations for Big Data as a public utility?

Ohashi: Whether Big Data is to be considered essential goods, such as electricity or gas, could be up to how valuable specific data are for users. The value of data could differ depending upon how the data are used. It can be difficult to define the universal value of data in general, which would make data uniquely different from electricity.

At this moment, if you have an Internet service such as a search engine or map in Japan, you would need to provide your personal information and thus you cannot control the outflow of your privacy into the Internet. It would be far better if we could put a price on each datum, since then consumers would know in advance that they would be providing their personal information at a certain price and to whom. Whether you prefer your privacy flow into a public space to be under control or not may depend on each person's value judgement.

JS: We will need to think about a balance between privacy protection for consumers and the need for an institution that would avoid harming innovation and entrepreneurship on the producers' side.

Ohashi: If we wish to continue enjoying the merits of the existing Internet service, a balance must be struck between the consumers' benefits in letting the data be used by others, and the need for their privacy protection. Though the time span of new technology might be short and the platform operators could be replaced by others quite often, I think it reasonable to say that the platform business is considered to be a social infrastructure. We would need public policy consideration in providing such a public good. If the platform market tends to be monopolized, and the market also features a kind of public good, we need in theory some type of regulation to avoid market power that could be exercised by a platform provider. How to find a balance between social efficiency achieved by a monopolizing platform provider and the abuse of market power exercised by it is an important issue to discuss both domestically and internationally. If Japan promotes a radical reform for privacy protection unilaterally, platform businesses will avoid providing their services in Japan. We should work on a reform proposal that other nations could support in some international policy discussion venue like the G20.

JS: Could the WTO be revitalized by being a venue for rulemaking for the digital economy?

Ohashi: Yes. This is certainly a hot issue and I think it would be desirable to put competition up for international discussion,

including trade aspects. In the Cancun Round they tried to discuss the issue of trade and competition, but in vain. Many years after this failure, each nation is now implementing its own competition policy with little harmonization effort. There are, I believe, two large downsides of this current implementation of national competition policy.

One is the issue of mergers. A review of cross-border mergers is currently organized by each nation in which companies are involved in the merger. The format of the review is provided in the native language of each jurisdiction. In this case, the legal costs for the prospective merging parties must be enormous. I think it would be far better to have a common and universal format for a review or for judgement criteria. The existing review system could cause enormous waste of resources and one country's negative judgment on mergers and acquisitions could lead to a failure of the whole process. I think this could be modified by harmonization efforts on competition policy across countries.

The other issue is related to cartels. Since each nation's anti-trust laws are applied in an extraterritorial manner to an international cartel, the surcharges levied differ from nation to nation. Thus, the sum of these surcharges altogether would work as double taxation. There is no perspective on whether these fines are to be balanced with the deadweight loss in social welfare caused by the cartel and the effects of future deterrence. This is how independent implementation of a nation's anti-trust laws could cause enormous costs for a company. I think it would be better to harmonize competition rules internationally in the WTO or other international policy forums in order to save these societal costs. We have informal policy platforms like the International Competition Network (ICN), the OECD or UNCTAD but they may not be venues for rule-making.

Less Equality

JS: Each platform seems to realize what we call the “sharing economy” — such as in the case of Uber where more people can be a beneficiary of a taxi service by sharing a ride. Will this lead to a correction in the expansion of inequality under capitalism?

Ohashi: No, I do not think so. The information gap between the platform operators and its users as I explained above would be expanded. In this regard, I think inequality will increase, not decrease. Looking at the changes in company rankings over, say, 30 years, you can see that the distribution in market capitalization values has been



skewed. For example, in 2007, the top three companies were Exxon Mobil (\$489 billion), General Electric (\$387 billion), and Microsoft (\$294 billion), and now (in 2017) they are Apple (\$796 billion), Alphabet, the holding company of Google (\$675 billion), and Microsoft (\$539 billion). We can see the third placed company in 2017 has larger market capitalization than Exxon Mobil in 2007. Also we should note that the distribution gap in the top group is also expanding. It might be intriguing to see if this can be compared to the enormous inequality between capitalists and labor in the 19th century. I would not be surprised if someone says that the kind of society described in *Das Kapital* by Karl Marx is emerging again.

JS: In this regard as well, will we need to fix rules for protecting consumer rights?

Ohashi: In particular, in the case of Japan, we will need to reduce information asymmetry between the platform operator and the SMEs. To achieve this promptly, I think one idea would be to follow a European-type discipline such as the GDPR or a regulation on promoting fairness and transparency into Japanese law. This might be a good solution for domestic business and SMEs. As for international rule-making, we may need to think about other countries' practices, including China, and try to achieve more rigorous rules based on an international consensus. J.S

Written with the assistance of TapeRewrite Corporation. *Japan SPOTLIGHT* takes full responsibility for the translation of this interview which was conducted originally in Japanese.