Competition

The Story So Far

Competition policy promotes rivalry among firms to maximize societal and economic welfare. In advanced economies, competition policy includes antitrust laws that protect consumer welfare from monopolistic behavior and other rules to prevent collusion, unfair practices that restrict competition and other abuses, and barriers to market entry and exit.

As China has reached a more advanced development stage, it has ratcheted up its competition policy objectives. Beijing passed a long-awaited antitrust law in 2008 after 13 years of discussion. The 2013 Third Plenum plan declared “developing an environment for fair competition” a priority. However, long-standing instincts favoring the interests of state-owned enterprises (SOEs) over consumers—and domestic firms over foreign ones—are still embedded in the Chinese system, with little regard for consumer welfare or fair competition.

- Since May 2013, the State Council has streamlined a wide range of administrative procedures related to business registration and taxation. New business registrations have risen steadily in recent years as a result, and in 2018, the World Bank recognized progress by substantially increasing its scoring of China’s “ease of doing business” compared with other countries. The State Council has promised to similarly reduce barriers to market exit, but progress has been much more limited.

- In June 2016, the State Council launched a “fair competition review mechanism” to clean up anticompetitive policies issued by government agencies at all levels. However, the mechanism did not clarify whether industrial policies should be considered anticompetitive, did not establish a transparent process to identify which current policies were anticompetitive, and did not prevent new anticompetitive policies from being implemented.

- Beijing has updated several competition-related laws since 2013 to reflect changing market conditions. In November 2017, China revised its 24-year-old Anti-Unfair Competition Law to cover emerging issues, such as commercial bribery and competition in new technologies like software and networks. In August 2018, the government also passed a new E-commerce Law to govern competition between internet companies. And it is in the process of revising patent and antitrust laws, ostensibly to strengthen legal protections for companies, although unequal enforcement between state and private firms and between domestic and foreign firms remains a major concern.

- In March 2018, China’s National People’s Congress (NPC) approved a government restructuring plan that merged functions from various agencies responsible for enforcing competition policy. The new agency, named the State Administration for Market Regulation (SAMR), now oversees all aspects of China’s competition policy regime, including business registration, mergers and acquisitions (M&A) reviews, pricing policy, food security, consumer protection, and intellectual property protection. On paper, the SAMR’s creation reduced the influence of industrial policy regulators, but these bureaucratic changes have yet to drive any real improvement in China’s competition regime as measured in our indicators.

Methodology

Competition policy is an amalgam of law, economic analysis, and politics, and gauging outcomes is challenging. Our primary indicator looks for convergence in reviews of foreign versus domestic mergers conducted by the SAMR. Supplemental data look at the number of merger cases reviewed, disclosure of results of competition-related court cases, new business starts and closures (market entries and exits), and the ability of firms to obtain viable profits in healthy markets.

Quarterly Assessment and Outlook

- We downgrade our assessment of competition policy reform from neutral to negative for the first quarter of 2020 because authorities disproportionately scrutinized foreign mergers, and the domestic business environment deteriorated.

- The share of mergers involving foreign firms that came under review surged to 32% in 1Q2020, the highest in at least five years. New company registrations decreased, while the pricing power of large listed companies increased at the expense of smaller companies.

- Beijing promised improvements in the competitive environment in China, this time with a focus on the judicial system, but did not offer a timeline for action.

This Quarter’s Numbers

China’s competition environment deteriorated in 1Q2020 as authorities disproportionately targeted foreign firms in their merger reviews. The State Administration of Market Regulation (SAMR) reviewed 49 foreign-involved mergers, 4 fewer than in 4Q2019. By contrast, only 26 domestic-only mergers were reviewed, 23 fewer than in 4Q2019. The
The COVID-19 pandemic affected China’s judicial transparency as numerous government offices shut down. In 1Q2020, the Supreme Court published 15,904 new competition-related cases on its website, 32% fewer than in 4Q2019.

The pandemic also affected reporting on competition data. Instead of releasing market entry data as usual, SAMR informed the press in July that “on average around 20,000 new companies were registered per day in 1H2020,” suggesting that China’s business environment had not changed since last year, when registrations were at the same level. Third-party data, by contrast, showed that new company registrations plunged to an average of 18,300 per day between February and April, slightly lower than in the past year.

Despite the weak business environment, listed company pricing power increased in 1Q2020. Notably, the pricing power of listed private companies in China reached the OECD level for the first time. The improvement was likely caused by a sharper reduction in costs than an increase in revenues during the pandemic. This phenomenon suggests that these companies, which are usually larger in size and more powerful than others in the market, either exploited lower prices from their vendors or reduced investments in the period. Neither is a good sign for the business environment.
**Policy Analysis**
Beijing made new reform pledges in the first half of 2020. On May 18, authorities released a document ("Guidance on Speeding Up the Improvement of the Socialist Market Economic System in the New Era") that pledged to deepen economic reform with a focus on “strengthening protection of property rights and improving market allocation of resources.” It defined a “high-standard market mechanism” as one that provides effective incentives through property rights, facilitates the free flow of production factors, allows flexible price adjustments, promotes fair and orderly competition, and enables efficient companies to grow and inefficient ones to exit. It dedicated an entire section to explaining how it will use the judicial system to pursue these goals.

On July 22, the Supreme Court and the National Development and Reform Commission released an opinion on how to provide such judicial services. The opinion detailed the role of the judiciary in each step of market competition, including treatment of firms of different ownership, protection of property rights, contracts and dispute resolution, regulation and administration, social justice and fairness, and the handling of foreign-related disputes. The opinion specifically promises to (1) repeal regulations that distinguish market players by ownership and that treat private firms unequally, (2) discipline the government from infringing (e.g., illegally seizing or freezing) private property rights, and (3) strengthen privacy protections.

These promises will take time to implement. The opinion itself did not specify any targets or timeline, and it contained so much detail that implementation would require significant adjustments and interministerial coordination beyond the judicial system. For example, “repealing regulations that distinguish market players by ownership” would require abolishing the newly passed Foreign Investment Law as well as the Law of State-owned Assets in Enterprises. Neither can be done in the near term. Promised steps to prevent the government from infringing on private property rights would require more checks and balances. For now, these statements are not convincing to private investors.

In addition to improving the judicial system, Beijing also committed to improving the business environment. On July 21, the State Council released an opinion that promises to (1) streamline administrative procedures for investment, production, trade, and employment and (2) improve the quality and efficiency of government services such as tax administration and trademark registration, among other measures. This opinion is not a concrete policy change, but it is an additional signal that authorities see a need to prioritize market mechanisms.