Disruption, Concentration, and the New Economy

(This editorial is based on the article “Disruption, Concentration, and the New Economy” which appears in Livemint on 2nd January 2019.)

The idea that a new economy had arrived was part of the hysteria surrounding the tech-bubble of the late 1990s and early 2000s. Investors and financial institutions bid up technology sector stock prices to unprecedented highs. The new economy was variously heralded as the knowledge economy, the data economy, the e-commerce economy and so on.

What is the New Economy?

- **The new economy is a buzzword describing new, high-growth industries that are on the cutting edge of technology and are the driving force of economic growth.**
- The new economy is commonly believed to have started in the late 1990s, as high tech tools, particularly the internet and increasingly powerful computers, made their way into the consumer and business marketplace.
- The new economy was seen as a shift from a manufacturing and commodity-based economy to one that used technology to create new products and services at a rate that the traditional manufacturing economy could not match.

Changing Structure of Markets

- **The growing dominance of leading technology firms has occasioned an intense debate about the trade-offs between efficiency and market power (i.e more efficient tech companies gather more market power thereby giving rise to monopolistic trends), while raising questions about what the changing structure of markets will mean for innovation and the distribution of wealth in the future.**
- With respect to efficiency and competition, there is already cause for concern. There is a steep decline in annual initial public offerings, showing that those young firms are increasingly agreeing to be acquired, rather than trying to grow into large public firms.
- **At the same time, exit rates within many industries have remained relatively flat despite an increase in productivity dispersion. In other words, weaker producers aren’t being knocked out of the market, implying a lack of dynamism in many sectors of the economy** (for example, a small tech company X is weak against the big company G, but that doesn’t force X to shut down, instead it keeps on running on weak growth and profits).
- Though there is no evidence of market concentration/monopolization happening in the market, there is a chance for a higher price shift later on due to this **market disruption.**

What is Market Disruption?

- Market disruption is a situation wherein markets cease to function in a regular manner, typically characterized by rapid and large market declines.
- Market disruptions can result from both physical threats to the stock exchange or unusual trading (as in a crash).

- In either case, the disruption creates widespread panic and results in disorderly market conditions.

- **Firms are gaining market share by becoming more efficient, and not simply by snatching up other firms while antitrust authorities stand aside.**
- Another development is the growing importance of “intangibles” such as software and intellectual property which researchers suggest could be driving an increase in market concentration.
- Moreover, distinguishing among industries, tech companies show that higher concentration is correlated with rising productivity in some sectors, and with growing market power in others. In consumer-facing industries, researchers have found productivity gains while research also suggests that consumers have benefited in the form of lower prices. The broader point is that we cannot say definitively that rising concentration has been harmful to consumers.
- Well-known market leaders such as Facebook and Google have been offering many products and services for free (which obviously benefits consumers), and their business models have raised a number of pressing questions.
    - For example, one must consider whether the exchange of personal data for the use of such services constitutes a fair trade. There is also the matter of whom these companies do charge for services, and whether those costs (say, for the advertisements you are forced to watch) are being passed back to consumers (in the form of better/new technological solutions).
- **Innovation is driven largely by competition,** both within an industry and further afield, as well as by the threat of future competition. So, even if one is not too worried about the effects of concentration on innovation today, one still must consider whether that could pose a threat to future dynamism.
- **Market disruption (involving big-tech) is slowing down investment, research and development, or the diffusion of innovation from superstar firms** (FAANGs: Facebook, Amazon, Apple, Netflix, and Google - they guard their IP and technology as trade secrets and therefore the trickle-down formula doesn’t work here).
- **In addition to stifling competition, this practice (of concentrating market power and the capacity to innovate, in the hands of a few big tech companies) is also discouraging financing by venture capitalists** (because VCs prefer to fund start-ups or companies that bring new ideas to the table, and seldom invest in big traditional tech companies like Google).

Way Forward

- **There are a number of possible reasons for the low diffusion of information and technology amongst players in this industry.** From intellectual property (IP) protections to constraints on labor mobility between firms, much of the system is designed for protecting self-interests and one’s own profit. But whatever the cause, it is clear that we should be worrying even more about the future of productivity than its present (because if big-tech keeps on consolidating the market, sooner or later the process will make productivity of small firms negligible).
- Therefore, policymakers should be particularly worried about how the behavior of superstar firms today could affect competition in their industries tomorrow.
- Politicians and regulators should take a hard look at whether IP and proprietary agglomerations of data are being used to stifle competition or prevent the diffusion of new knowledge and technologies across sectors. And they should consider policy instruments that go beyond the scope of traditional antitrust.
    - For example, some have suggested that individuals should have a right to their individual data. This could potentially improve diffusion because firms would become purchasers of data, rather than sellers. No longer tied to any one platform, individuals could distribute their data to competing firms. Policymakers could also start to push for more interoperability between platforms, which would limit how much users could be tied to any particular platform.
- **In terms of** labour**, policymakers could intervene in a number of ways.** For example, there might be a case for antitrust action against “non-compete” contracts*, which essentially impose restraints on trade (of labour, in this case).
- **Can policymakers win back the public’s confidence, maintain global economic stability, and find ways to accommodate widespread technological disruptions all at the same time? That will be a key question in 2019—and beyond.**

What are Antitrust Laws?

- Antitrust laws also referred to as "competition laws," are statutes developed by the U.S. Government to protect consumers from predatory business practices by ensuring that fair competition exists in an open-market economy.
- These laws have evolved along with the market, vigilantly guarding against would-be monopolies and disruptions to the productive ebb and flow of competition.

Antitrust laws in India

- For years, India had its own version of competition law, which was enacted through legislation called the Monopolies and Restrictive Trade Practices Act 1969 (MRTP Act).
- This legislation, based on principles of a “command and control” economy, was designed to put in place a regulatory regime in the country which did not allow concentration of economic power in a few hands that were prejudicial to public interest and therefore prohibited any monopolistic and restrictive trade practices.
- Post-economic liberalization in 1991, it became imperative to put in place a competition law regime that was more responsive to the economic realities of the nation and consistent with international practices.
- Consequently, in 2002, the Indian Parliament approved comprehensive competition legislation — the Competition Act 2002 (Competition Act), to regulate business practices in India so as to prevent practices having an Appreciable Adverse Effect on Competition (AAEC) in India.

What are ‘non-compete’ contracts/agreements

- A non-compete agreement is an agreement between an employer and an employee in which the employee agrees not to use information learned during employment to enter into competition in subsequent business efforts.