

THE ROLE OF COMPETITION IN  
IMPLEMENTING THE **ECONOMIC**  
**RECOVERY** STRATEGY



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## THE ROLE OF COMPETITION IN IMPLEMENTING THE ECONOMIC RECOVERY STRATEGY

The Covid-19 pandemic and the lockdown measures have had an immediate impact on the economy, harming businesses, workers and consumers, in general.

Competition, as a driver of productivity and innovation, is key for the economic recovery. Competition also contributes to an inclusive recovery by delivering prices that are more competitive and by boosting the creation of new employment opportunities - important aspects to face the decline in household income. It is, thus, important to consider the dimension of competition in the current economic recovery agenda.

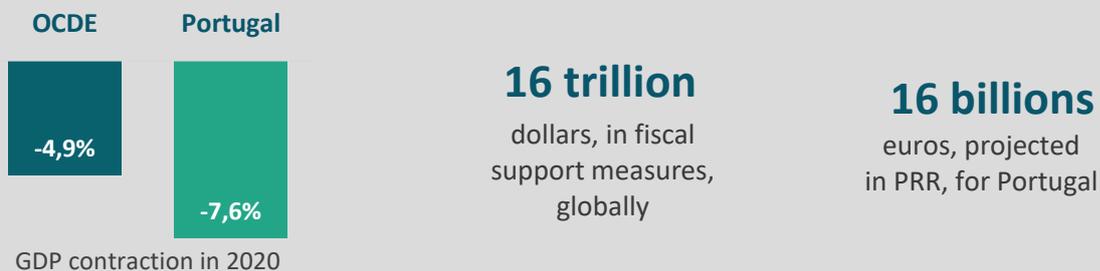
The AdC has identified a set of principles for promoting competition, so that these can be considered when implementing the national economic recovery strategy.

### I. Competition as a catalyst for economic recovery

The Covid-19 pandemic has had significant consequences on the performance of economies, with a slowdown in GDP growth in the OECD and Portugal.<sup>1</sup>

Several governments have responded to the current crisis with fiscal support measures for the economy, already accounting for 16 trillion dollars.<sup>2</sup> These measures have contributed to more optimistic growth projections for the global economy, and for Portugal, for 2021/22.<sup>3</sup>

The national economic recovery strategy, which includes the Recovery and Resilience Plan (PRR), foresees a set of reforms and investments, based on three dimensions - resilience, climate transition and digital transition.<sup>4</sup>



Given the sizeable financial support, **it is essential to ensure that the implementation of reforms and investments does not inadvertently distort competition conditions in the markets.** International experiences show that relaxing competition has a negative impact on efficiency and productivity, weakening the conditions for a sustainable and resilient economic recovery.<sup>5</sup>

<sup>1</sup> During 2020, GDP growth in the OECD slowed down by 4.9% and at the national level, GDP decreased 7.6% in volume (growth of 2.2% in 2019). GPEARI/GEE, [Boletim Mensal de Economia Portuguesa](#), February 2021 and INE Notice, [Contas Nacionais Trimestrais \(Base 2016\) – Estimativa Rápida a 30 dias. 4º Trimestre de 2020 e Ano 2020](#), February 2021.

<sup>2</sup> International Monetary Fund (2021) [Fiscal Monitor: A Fair Shot](#), abril 2021.

<sup>3</sup> The International Monetary Fund (IMF) estimates global economic growth of 6% in 2021 and 4.4% in 2022 (in terms of real GDP) ([World Economic Outlook](#), Abril 2021). Banco de Portugal estimates a GDP growth in Portugal of 3.9% in 2021 and 5.2% in 2022 (Banco de Portugal, [Boletim Económico](#), March 2021).

<sup>4</sup> [Recuperar Portugal, Construindo o futuro - Plano de Recuperação e Resiliência](#) (PRR) (in Portuguese).

<sup>5</sup> OECD (2020) [The Role of Competition Policy in Promoting Economic Recovery](#).

**Competition is a key factor for a favorable economic environment by encouraging firms to be more efficient** and to offer better conditions to consumers.

For example, the implementation of regulatory and legislative reforms, in the 1990s, aimed at eliminating an extensive set of barriers to entry and expansion of firms and to innovation in Australia, played a crucial role in boosting the competitiveness of the Australian economy.<sup>6</sup>

**Competition is also a catalyst for productivity** by attracting investment, stimulating the creation of qualified employment and boosting exports of products, services and ideas.<sup>7</sup>

Empirical evidence shows that low levels of management practices are associated with a less competitive environment, which explains part of the differences in productivity between countries.<sup>8</sup>

## II. Principles to promote competition in the context of the economic recovery

We highlight a **set of principles to promote competition, efficiency and innovation** in order to strengthen the path to an inclusive and sustainable economic recovery.

### A. REMOVAL OF UNNECESSARY BARRIERS TO ENTRY AND EXPANSION

**It is essential to remove unnecessary barriers to entry and expansion of new players in the market, in order to promote competition and to boost economic recovery.** Public policies that create or reinforce unnecessary barriers hinder economic growth.

For example, the reform “*Empresa na Hora*” (“*Business on the Spot*”), implemented in 2005, aimed at reducing costs with the establishment of new firms in Portugal, contributed to a 25% increase in the entry of new firms and a 4% increase in employment (per year).<sup>9</sup>

**Promoting competition by removing unnecessary barriers can also boost firms’ incentives to innovate.** The lack of a competitive environment benefits incumbents and makes it harder for firms to enter and expand in the market, reducing incentives to invest in innovative and disruptive technologies.<sup>10</sup>

**Furthermore, the removal of unnecessary restrictions on the access to professions will promote a competitive environment and a more efficient allocation of resources,** fostering

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<sup>6</sup> According to a 2005 report, these pro-competitive reforms initiated in the 90s increased GDP growth by 2.5% and boosted the average household’s annual income by 7 000 Australian dollars. Cf. Australian Productivity Commission (2005), [Review of National Competition Policy Reforms](#).

<sup>7</sup> See Relatório do Conselho para a Produtividade/ Council for Productivity, (2019) [“A Produtividade da Economia Portuguesa, 1.º Relatório do Conselho para a Produtividade”](#); and CMA. (2015). [“Productivity and competition A summary of the evidence”](#).

<sup>8</sup> Bloom, N., Genakos, C., Sadun, R., & Van Reenen, J. (2012). “Management practices across firms and countries”. *Academy of Management Perspectives*, 26(1), 12-33; and Bloom, N, Lemos, R., Sadun, R., Scur, D. & Van Reenen, J.(2014). “The New Empirical Economics of Management”. NBER Working Paper 20102.

<sup>9</sup> Félix, S. & Maggi, C. (2019). “What is the impact of increased business competition?”. Bdp Working Papers 4.

<sup>10</sup> Vide, e.g., Foster, L., Haltiwanger, J. e Krizan, C.J.(2006). “Market Selection, Reallocation, and Restructuring in the U.S. Retail Trade Sector in the 1990s.” *Review of Economics and Statistics*, 88(4): 748–58; Bloom, N., Draca, M.e Van Reenen, J (2016) .“Trade Induced Technical Change? The Impact of Chinese Imports on Innovation, IT and Productivity.” *Rev Econ Stud* 83 (1): 87-117; and Correa & Ornaghi. (2014). “Competition & Innovation: Evidence from U.S. Patent and Productivity Data”. *The Journal of Industrial Economics*.

competitiveness and economic resiliency. It also contributes to re-training opportunities. In a context of rising unemployment, it is even more important that workers are not deprived of opportunities for reintegration in the labor market. The PRR foresees a reform to reduce restrictions to access self-regulated professions.

We highlight the AdC's recommendations regarding self-regulated professions, aimed at reducing restrictions to access these professions (Box 1).

#### **Box 1. AdC's Recommendations to reduce barriers in self-regulated professions**

The 2018 AdC's Action Plan<sup>1</sup> proposes legislative and regulatory changes for self-regulated professions in order to promote competition:

- ✓ **Separate the regulatory function from the representative function** for self-regulated professional associations
- ✓ **Reassess the reserved activities for professionals enrolled in professional associations**
- ✓ **Identify alternative ways to obtain the necessary qualifications**
- ✓ **Reassess the legal and regulatory criteria related to traineeships**, required for registration in a professional association
- ✓ **Eliminate rules that restrict (i) ownership of professional associations; and (ii) the management of professional associations** by people who are not professionals registered in a given professional association
- ✓ **Allow multidisciplinary practice** in professional associations
- ✓ **Abolish restrictions on the free establishment of notarial services**
- ✓ **Remove rules that require auditors to send strategic information to the Professional Association of Auditors (Order of ROC)** related to the exercise of public interest functions

Note: (1) AdC (2018) [AdC's Action Plan to a Legislative and Regulatory Reform](#) (in Portuguese).

**The removal of unnecessary barriers to entry, expansion and innovation in different sectors of the economy can contribute to a sustainable economic growth.** The AdC issued several recommendations aimed at removing barriers to entry and promoting competition in a set of key sectors of the Portuguese economy, such as the energy, transport and port sectors, telecommunications, among others. The implementation of these measures in the current context can deliver cost savings and, thus, contribute to boost competitiveness and the economic recovery.

**In the energy sector, the AdC issued several recommendations** to the Government and the sectoral regulator (ERSE)<sup>11</sup>. Amongst these are the recommendations regarding the elimination of transitory tariffs for the sale of natural gas and electricity to end-consumers, the relevance of diplomatic efforts towards the elimination of double tariffs for the use of the transmission network in the cross-border trade of natural gas between Portugal and Spain (tariff pancaking), the importance of an assessment of investments in the transmission and distribution networks for electricity and natural gas, alongside with the importance of bringing the remuneration rates of regulated assets in the sector closer to those of risk-free assets.

**Regarding measures to promote innovation and openness, we also highlight the AdC's recommendations regarding the framework of electric vehicle charging.** In 2019, the AdC

<sup>11</sup> See, e.g., [AdC Comments on the Plan for Development and Investment for Natural Gas Distribution Networks for the 2021-2025 period](#), 13/04/2021 (in Portuguese); [AdC Comments on the Plan for Development and Investment for Electricity Distribution Networks for the 2021-2025 period](#), 22/09/2020 (in Portuguese); AdC (2018), [Analysis of the Road Fuels Sector in Mainland Portugal](#) (in Portuguese); AdC (2017), [The Bottled Liquefied Petroleum Gas in Mainland Portugal](#) (in Portuguese); AdC (2017), [Sector Inquiry on the supply of natural gas to industrial consumers](#) (in Portuguese).

argued for a reassessment of the legislative framework for electric vehicle charging, in order to simplify the organizational model and increase the efficiency of the system.<sup>12</sup>

**The AdC's recommendations for the road, railway, maritime and port sectors are likely to contribute to the economic recovery**, and generate savings that have a multiplier effect in the economy (Box 2).

### Box 2. AdC's Recommendations to reduce barriers in transports

The AdC has made proposals for legislative and regulatory changes for the **road, rail and maritime sectors and for the port sector** in order to promote competition.<sup>1</sup>

#### **Road Sector**

- ✓ **Abolish a set of disproportionate requirements**, namely:
  - i. **Mandatory licensing regime for freight operators** using solely motor vehicles between 2.5 tonnes and 3.5 tonnes
  - ii. **Minimum capital requirements to start the business**, imposed on certain operators
  - iii. **Access and price restrictions** for the market of long-distance bus routes
  - iv. **Quotas and geographical restrictions** for taxis to access the market and pick up passengers in other municipalities
  - v. **Geographical restriction on the location of driving schools**
  - vi. **Licensing requirements of a minimum number of vehicles to start the activity**, imposed on certain operators

#### **Rail Sector**

- ✓ **Regulate the legislation applicable to the certification of train drivers**
- ✓ **Abolish the maximum period of validity for railway licences**
- ✓ **Favour a competitive tendering for public service contract for rail passengers transport**, establishing public service obligations

#### **Maritime Sector**

- ✓ **Implement an alternative regulation model of public service obligations** for cabotage between mainland Portugal and the Portuguese islands

#### **Port Sector**

- ✓ **Amend the legal regime applicable to port tariffs for services provided by the port authority**, based on a common transparent and cost-oriented formula
- ✓ **Foster the role of the private sector** in pilotage services, port towing and cargo handling port operations
- ✓ **Redesign port terminal concessions**
- ✓ **Liberalize the access to towing and piloting port service markets**
- ✓ **Amend the regime for obtaining Pilot Exemption Certificate (PEC)** in order to reduce administrative costs and granting automatic extensions

**Notes:** (1) AdC (2018) [AdC's Action Plan to a Legislative and Regulatory Reform](#) (in Portuguese); AdC (2018) [Competition in the Portuguese Ports Sector](#) (in Portuguese); AdC (2018), [Recommendation on the liberalization of passenger rail services](#) (in Portuguese).

**The AdC has also made important recommendations aimed at removing barriers to entry of new business models based on digital technologies**, such as in the financial services sector.<sup>13</sup>

<sup>12</sup> [AdC Comments on the proposed amendment to the electric mobility Regulation](#), 17/10/2019 (in Portuguese).

<sup>13</sup> AdC (2018), [Technological Innovation and Competition in the Financial Sector in Portugal](#); and AdC (2021) [Competition in the Financial Sector in Portugal – Follow-up of AdC's Recommendation in the context of Issues Paper FinTech](#) (in Portuguese).

In the field of electronic communications, the AdC alerted for the importance to limit the excessive loyalty policies (including loyalty renewal) that characterize this sector.<sup>14</sup> At a time when consumption patterns are changing, consumers, families as well as firms should not be prevented from switching to telecom operators that best fit their preferences and allow them to optimize their spending.

## B. PROMOTING COMPETITIVE AND EFFICIENT PUBLIC PROCUREMENT PROCEDURES

The State, as a procurer of goods and services, can play an important role in promoting innovation and competition. Public procurement is a relevant part of the Portuguese economic activity, representing around 9.18% of GDP and 20.89% of public spending.<sup>15</sup>

It is, thus, crucial to ensure that public tenders are well participated and efficiently designed. Competition in public procurement is a vital element in ensuring that public funds are used efficiently.

The opportunity for savings generated by promoting efficiency, competition and combating bid-rigging in public procurement is substantial. It also contributes to the fight against corruption (Box 3).

### Box 3. The impact of competition and efficiency in public procurement

#### MORE PARTICIPANTS IN TENDERS REDUCE THE PAID PRICE

Ilimi (2006)<sup>1</sup> estimates that a 1% increase in the number of bidders decreases the equilibrium bid by about 0.2%.

Public spending

▼ 47%

#### MORE COMPETITIVE TENDERS CAN REDUCE SPENDING

The introduction of competitive bidding for durable medical equipment in the U.S. has led to a 47.2% fall in spending, mainly driven by a 44.8% price reduction.<sup>2</sup>

Contractual value

▲ 30%

#### BID-RIGGING GENERATES SUBSTANTIAL OVERCHARGES

Cartel overcharge estimates are found in the ranges of 10-15% to 20-30% of the contractual value.<sup>3</sup>

Public spending

▼ 22%

#### EFFICIENT TENDERS GENERATE SAVINGS

The removal of passive waste by optimizing the efficiency of procedures generates savings around 22%.<sup>4</sup> Corruption and poor management in public procurement can generate losses of around 10 to 30% of public investment.<sup>5</sup>

#### Notes:

- (1) Ilimi. (2006). "Auction reforms for effective official development assistance" *Review of Industrial Organization*, 28(2), 109-128.
- (2) Ding, H., Duggan, M., & Starc, A. (2021). "Getting the Price Right? The Impact of Competitive Bidding in the Medicare Program". National Bureau of Economic Research (No. w28457).
- (3) Davies & Ormosi (2016) *A methodological framework to capture the various economic impacts of competition enforcement*; e Smuda (2014) "Cartel overcharges and the deterrence effect of EU competition law" *Journal of Competition Law & Economics*, 10 (1): 63-86.
- (4) Bandiera, Prat & Valletti (2009) "Active and Passive Waste in Government Spending: Evidence from a Policy Experiment", *The American Economic Review*, 99(4), 1278-1308.
- (5) OCDE (2016) *Preventing Corruption in Public Procurement*.

The AdC has put in place initiatives to raise awareness to the impact of bid-rigging in public procurement and to the benefits of competition in tenders. In these sessions, the AdC raises awareness of procurers to the high costs of bid rigging, to the main signs of collusion that they

<sup>14</sup> AdC (2020), [Loyalty policies in telecommunications services](#).

<sup>15</sup> Based on OECD data for 2018 ([Government at a Glance](#)).

should be aware of, as well as to the best practices in the design of tenders, with a view to promoting competition and efficiency.

An efficient allocation of resources is key to create favourable conditions for a sustainable economic recovery.

In 2021, the AdC's "**Campaign Fighting Bid-Rigging in Public Procurement**"<sup>16</sup> will focus on the **target investment areas**, namely in the areas of health and infrastructures, with awareness-building sessions to public procurers.

**In the current context, we reiterate a set of measures that can contribute to a better management of public spending, in favor of a resilient economic recovery** (Box 4). Amongst others, we highlight the importance of giving priority to competitive procedures, given the savings generated in terms of public spending (Box 3), with proportional requirements that promote participation and ensure competitive neutrality, including technology-wise.

We also reiterate the recommendation put forward by the AdC in the comments developed to the exceptional regime of Decree-Law no. 10-A/2020 on public procurement (article no. 2), about the relevance of limiting the use of the direct awards and ensuring that it is only applicable for reasons of effective extreme urgency.<sup>17</sup>

#### **Box 4. AdC's recommendations to promote competition and efficiency in public procurement**

We highlight some of the AdC's recommendations to various sectors of the economy aimed at promoting competition and efficiency in public procurement.

- ✓ Favour **competitive tenders**
- ✓ **Avoid predictability** in public procedures
- ✓ Set **objective and clear requirements and rules of procedure**
- ✓ Ensure **competitive neutrality, including technology-wise**, in tender procedures
- ✓ Set **appropriate deadlines** for bid submission
- ✓ **Avoid qualification requirements that are restrictive** and unnecessary
- ✓ **Widen tender participation to as many potential bidders** as possible; refrain from excluding potential participants just because they have not participated in previous tenders
- ✓ **Consider the division of the contract into lots if needed to promote bidder participation**, while taking into account that the form of splitting the contract into lots should mitigate the risk of collusion
- ✓ **Reduce the costs incurred by participants in bid preparation**
- ✓ **Establish clear and objective performance and functional requirements**

These principles are in several AdC's recommendations for various sectors, such as in the [Best practices for awarding public road passenger transport service contracts](#), February 2021; [Best practices for awarding outdoor advertising concession rights](#), June 2020 (in Portuguese); as well as in the Issues Paper [Technological Innovation and Competition in the Financial Sector in Portugal](#), October 2018.

<sup>16</sup> AdC (2015), [Best practices guidelines for fighting bid-rigging in public procurement](#) (in Portuguese).

<sup>17</sup> [AdC Opinion on the Draft Law No. 41/XIV/1st in the context of public procurement](#), 30/10/2020.

### C. PROMOTING COMPETITION AND EFFICIENCY WHEN DEPLOYING STATE SUPPORT

The national economic recovery strategy aims at “restoring the ability of firms to resuming their activity”.<sup>18</sup> The strategy defines a set of investments to mitigate the business-financing gap, given firms' solvency issues. In particular, the PRR foresees direct and debt financing to firms.

**State support should be proportionate, well targeted, and should not result in adverse effects on competition.** These principles are in line with those highlighted by the OECD, in the discussion of the role of competition in economic recovery<sup>19</sup>, and in the European Commission Notice on state aid.<sup>20</sup>

**State support should be based on objective criteria and, if possible, applicable to the several firms in a given sector in order to ensure competitive neutrality** – i.e., in order to minimize distortions between competing firms in the market.

**State support for specific firms, if needed, should be targeted to firms that were not in financial distress before the start of the Covid-19 pandemic** and that will likely remain financially viable after the pandemic.

Empirical evidence shows that the continued funding of inefficient firms that only survive at the expense of financing (i.e., zombie firms)<sup>21</sup> contribute negatively to productivity and to efficiency in resource allocation. Between 2005 and 2016, this type of firms had a significant presence in Portugal.<sup>22</sup>

**Thus, in deploying financial support to firms, it is important to forestall a restructuring plan<sup>23</sup> and an effective and transparent exit strategy for public financing<sup>24</sup>,** particularly when dealing with inefficient firms that survive mainly at the expense of public financing.

**In order to ensure an effective exit strategy, state support should be limited in duration.** The duration of the financial support should not exceed the time strictly necessary to ensure a sustainable recovery, so as to avoid a negative impact on the incentives to compete and innovate in the market.

**If state support introduces competitive distortions, corrective measures should be foreseen.** Measures should be adequate, proportionate, feasible and effectively monitored to correct the identified competition problems.

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<sup>18</sup> AdC's translation of “restaurar a capacidade das empresas em retomar a sua atividade” in [Recuperar Portugal, Construindo o futuro - Plano de Recuperação e Resiliência](#) (PRR), p. 7 (in Portuguese).

<sup>19</sup> OECD (2020) [The Role of Competition Policy in Promoting Economic Recovery](#).

<sup>20</sup> [Commission Notice on the notion of State aid as referred to in Article 107\(1\) of the TFEU, C/2016/2946](#).

<sup>21</sup> The loss of competitiveness of the Japanese economy in the 1990s has been associated with the prevalence of zombie companies. See, e.g., Caballero, R., Hoshi, T., & Kashyap, A. K. (2008). “Zombie lending and depressed restructuring in Japan”. *The American Economic Review*, 98(5), 1943–1977.

<sup>22</sup> Carreira, C., Teixeira, P., & Nieto-Carrillo, E. (2021). “Recovery and exit of zombie firms in Portugal”. *Small Business Economics*, 1-29.

<sup>23</sup> See the following European Commission communications: (i) “Guidelines on State aid for rescuing and restructuring non-financial undertakings in difficulty (2014/C 249/01)” and; (ii) “Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak” (JOEU, C 0911, 1-9).

<sup>24</sup> Carreira et al. (2021) (sup. Cit.) concludes that restructuring strategies are needed in enhancing recovery of “zombie” firms.

## Removal of unnecessary barriers to entry and expansion

To foster economic recovery, it is key to remove unnecessary barriers in the different sectors of the economy. See, for example, the AdC's recommendations regarding:

- Access to self-regulated professions
- Business models based on digital technologies (e.g., FinTech)
- In the road, rail, maritime and port sectors
- In the electronic communications
- In energy and electric mobility

## Promoting competitive and efficient public procurement procedures

Public procurement procedures should:

- Be competitive
- Not be predictable
- Set objective and clear requirements and rules of procedure
- Ensure competitive and technological neutrality
- Set appropriate deadlines for the submission of bids
- Avoid restrictive qualification requirements
- Include the largest number of participants
- Not exclude participants for not having participated in other procedures
- Consider splitting the contract into lots, if needed to promote participation
- Reduce the costs incurred by participants in bid preparation

## Promoting competition and efficiency when applying state support

State support should:

- Be based on objective and non-discriminatory criteria
- Ensure competitive neutrality, minimizing distortions between firms in the market
- Apply to sectors and not specific firms
- Be targeted to firms that were not in financial distress prior the Covid-19 pandemic
- Incorporate a restructuring plan for the firm and an effective and transparent exit strategy
- Have a limited duration
- Incorporate correction measures, in case the state support introduces distortions to competition