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Competition Policy Review Panel
Research Paper Summary

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Title: Assessing the Potential Impact of a National Champions Policy on Canada's Competitiveness

Subjects Addressed:

- Arguments for and against government policies aimed at creating national champions
- Canadian experience and policy to date
- Experiences from the European Union, Southeast Asia and Australia

National Champions:

A national champion is a domestically-based company that has become a leading competitor in its global market. Champions can be fostered by standard pro-market policies - the creation of a large domestic market, expanding trade, and ensuring intense competition. More controversial, and the focus of this paper, is whether specific champions should be promoted with subsidies, R&D support, preferential procurement, export support, trade barriers, prevention of foreign takeovers, and other protections.

Arguments in favour of a targeted strategy supporting national champions:

Proponents of this strategy argue that national champions create extraordinary spin-offs in the local economy, and hence governments should support their success. Arguments for this approach include:

1. Infant companies need help in certain industries to overcome incumbents' advantages of scale, specialized knowledge, lack of start-up costs, and experience.
2. Subsidies to national champions in high-technology areas can help them compete more effectively in an international oligopoly, thus keeping more of the profits and jobs in the country and enhancing international competition, increasing consumer choice, and lowering prices.
3. R&D subsidies to national champions can attract internationally mobile researchers.
4. Promoting the agglomeration of clusters can create spillovers that help participants become ever more innovative and competitive. Clusters of traded industries pay higher wages, and produce more patents. Large champions are often at the centre of world-class clusters.
5. In countries with small domestic markets, help is needed so firms can achieve critical mass to compete and overcome this disadvantage.
6. Government investments can supplement large companies' investments in plant and equipment, thereby enhancing their productivity and long-term competitiveness and creating jobs.

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7. Some industries are strategic to the future of a country, e.g. to national security (defence industry), energy security, and economic vitality (technology industries). They often require significant upfront capital investment, justifying subsidies or permission of mergers leading to dominance or monopoly positions.
8. Manufacturing with its tradeability and greater propensity to drive R&D is considered by some to be critical to an advanced economy and demands an industrial strategy to ensure that it stay vibrant.
9. Government may need to correct short-term market failures, e.g. while a company undergoes a financial crisis or restructuring.
10. Government may need to correct market failures that do not account for externalities (e.g. pollution, the need to promote non-traditional energy sources to tackle climate change).
11. Government is also often called on to rescue failing companies or industries to prevent or slow down massive job losses.

Arguments against a targeted Strategy supporting National Champions:

According to the authors, the research indicates that the costs to the overall competitiveness of the economy outweigh the benefits that might accrue to the targeted industry or firm. Thus, government support for specific national champions is unlikely to assist Canada in achieving its prosperity potential.

Arguments for this position are:

1. Companies usually achieve global leadership from competing intensely, not from being shielded against competition. Research by William Lewis and Michael Porter concludes that competition in the domestic market begets efficient, productive firms which are better able to compete on global markets. Policies to protect business lead to stagnation by making those businesses complacent, reducing the impetus for evolution, and interfering with the process whereby more efficient companies replace less efficient ones. Rather than protecting firms in a small domestic market, government policy needs to maximize available market size through expanding access to other markets.
2. In addition, governments have not had a distinguished record in discerning market trends and implementing successful business strategies (i.e. picking the 'right' champions that ultimately were successful). For example, Japan tried to build national champions in the 1970s/80s, but many of the more successful and competitive champions (automobile, robotics, fax/copier machines) were not in the industries receiving special support (aircraft, software, retail). In general, governments often choose to support specific industries, especially those with poor economic prospects, and keep supporting such firms or industries long after it is clear that success is not achievable. Keeping failing companies afloat has no economic justification. The social costs of allowing these failures can be significant; but the real solution is to address skills requirements and transition costs for the affected workers.

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3. Finally, subsidies and protection for a national champion begets retaliation in other countries, and all countries end up diverting resources with no improvement to the world-wide state of the industry. Rather than using targeted measures, governments should support clusters through public policy aimed at developing national capabilities through education, infrastructure, publicly funded research, and effective competition policy.

The National Champions Debate in Canada:

In Canada, competition policy is decidedly tilted away from the creation of national champions. Yet, three of our key industries operate in ownership frameworks consistent with a national champion approach: airlines, telecommunications services, and banking. The evidence indicates that such ownership restrictions have not helped Canada's competitiveness – nor have they created national champions who are true global leaders.

In 1985, the Macdonald Commission pointed to the problem of Britain subsidizing ailing industries, and of France choosing firms for prestige rather than economic reasons and being unwilling to abandon failures. Canada had committed some of the same errors, especially subsidizing ailing industries, though the commission also identified several success stories. It recommended free trade; strengthening the labour, capital, technology, and management inputs to the economy; and assisting workers to adjust rather than firms or industries.

Michael Porter's 1991 study *Canada at the Crossroads* concluded that successful policies should create a competitive environment, not cozy partnerships between businesses and government. It also argued that Canada's clusters were not benefiting from vigorous rivalry and that firms suffered from a lack of both external pressure and domestic rivals.

The Institute for Competitiveness & Prosperity has found little evidence that government support in Canada has been instrumental in creating the country's global leaders. Only a handful of Canada's global leaders were the result of deliberate government support, e.g. Bombardier, CAE, CHC, and Nortel, but nearly all our global leaders have achieved this status through their own efforts.

Approaches to National Champions in other Countries:

National champion policies are part of government economic strategies in France (Airbus, Agency of Innovation, 2005 Beffa report recommending support to national champions), Italy (protection of domestic ownership of telecommunications national champion), and Spain, either to support strategic firms/industries or to shore up failing firms/industries. Germany and UK do not support national champions specifically. The EU Commission pursues a pro-market and has penalized cartels and states trying to protect 'their' companies. China's approach to national champions is still evolving, along with its economic policies overall. Australia embraced market oriented policies. Otherwise, national champions do not figure prominently in public policy around the world.

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Japan's current industrial policy according to the Ministry of Economy, Trade and Industry (METI) is geared towards innovation, productivity improvement through increased internal competition, fostering the spirit of Asian dynamism, and improving business environments across Asia. Government continues to play a significant role in economic strategy. A major element of Japan's industrial policy is the production of an "Innovation Superhighway Concept" in which coordination between industry, academia, public organizations and the government will prioritize R&D in strategic areas.

Conclusions:

Successful firms achieve success through the pressure of competition. In addition, governments have not established a good track record of choosing the "right" firms or industries and of knowing when to admit defeat. Rather than attempting to promote and protect specific national champions, government should see its role as a catalyst sustaining positive change in our economy. Economic policy needs to be focused on creating supportive conditions for success and innovation through investments in specialized human capital, infrastructure, and institutions, and on generating an environment of competitive pressure domestically and internationally.

Clusters are important, but cluster development should be supported indirectly through public policy aimed at developing national capabilities through education, infrastructure, publicly funded research, and effective competition policy. Governments should monitor our successful clusters and firms and ensure that Canada's environment is not disadvantageous relative to other countries.

Where small markets are a significant limitation, government should maximize available market size through expanding access to other markets.