

Industrial Policy and Competition Policy: Conflict or Complementarity?

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The Pros and Cons of Industrial Policy



Outline

Industrial policy encompasses trade policy, financial market policy, intellectual property (IP) policy, fiscal policy, foreign economic policy, and competition policy.

1. Why is it in the spotlight now?

- *Description of Europe's new industrial policy.*

2. Competitiveness is crucial for meeting the objectives of Europe's new industrial policy.

- *Large body of economic evidence.*
- *In the long run, Europe's competitiveness will hinge on its ability to innovate and adapt.*

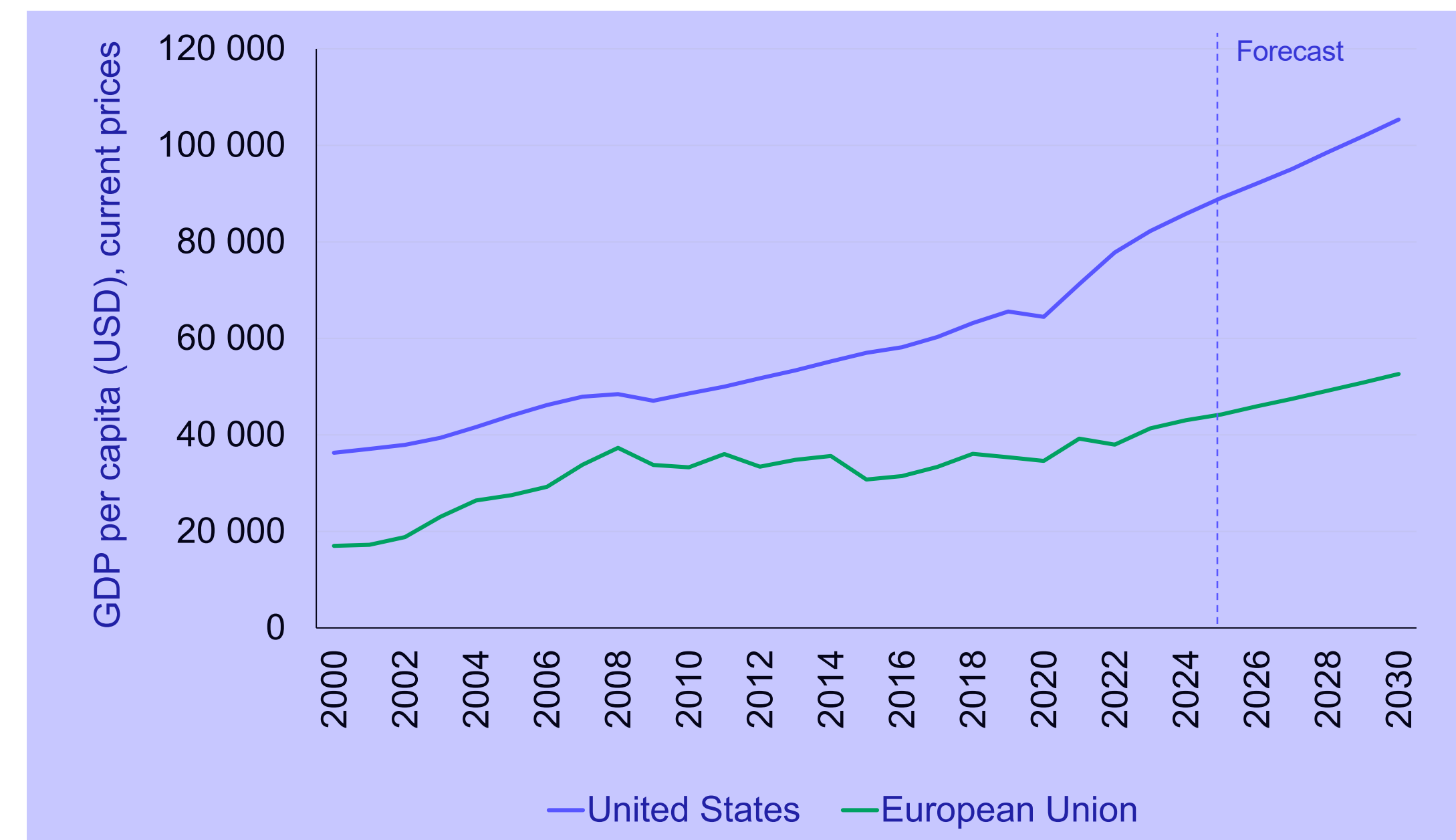
3. Can an activist industrial policy be pro-competitive?

- *Yes, if designed correctly.*

4. Leveraging competition policy to advance industrial policy: evolving stance and enforcement.



GDP per capita



Source: Keystone analysis of IMF data.

Why this debate? Why now?



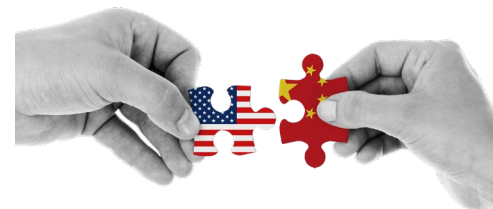
Pressure on EU productivity

- Productivity gap with the US mainly explained by the tech sector.
- Concerns that Europe is falling behind in innovation.
- Only four of the world's top 50 tech companies are European.
- Effects of the “China Shock” on the internal market.¹



Global supply chain disruptions - need for resilience

- Geopolitical shocks exposed Europe's dependence on foreign supply in key sectors (e.g. semiconductors, energy, pharmaceuticals).



Geopolitical shifts and its effect on EU industry

- Rising US-China tensions increase uncertainty for Europe and dampen investment.
- Lower access to overseas markets for European firms.

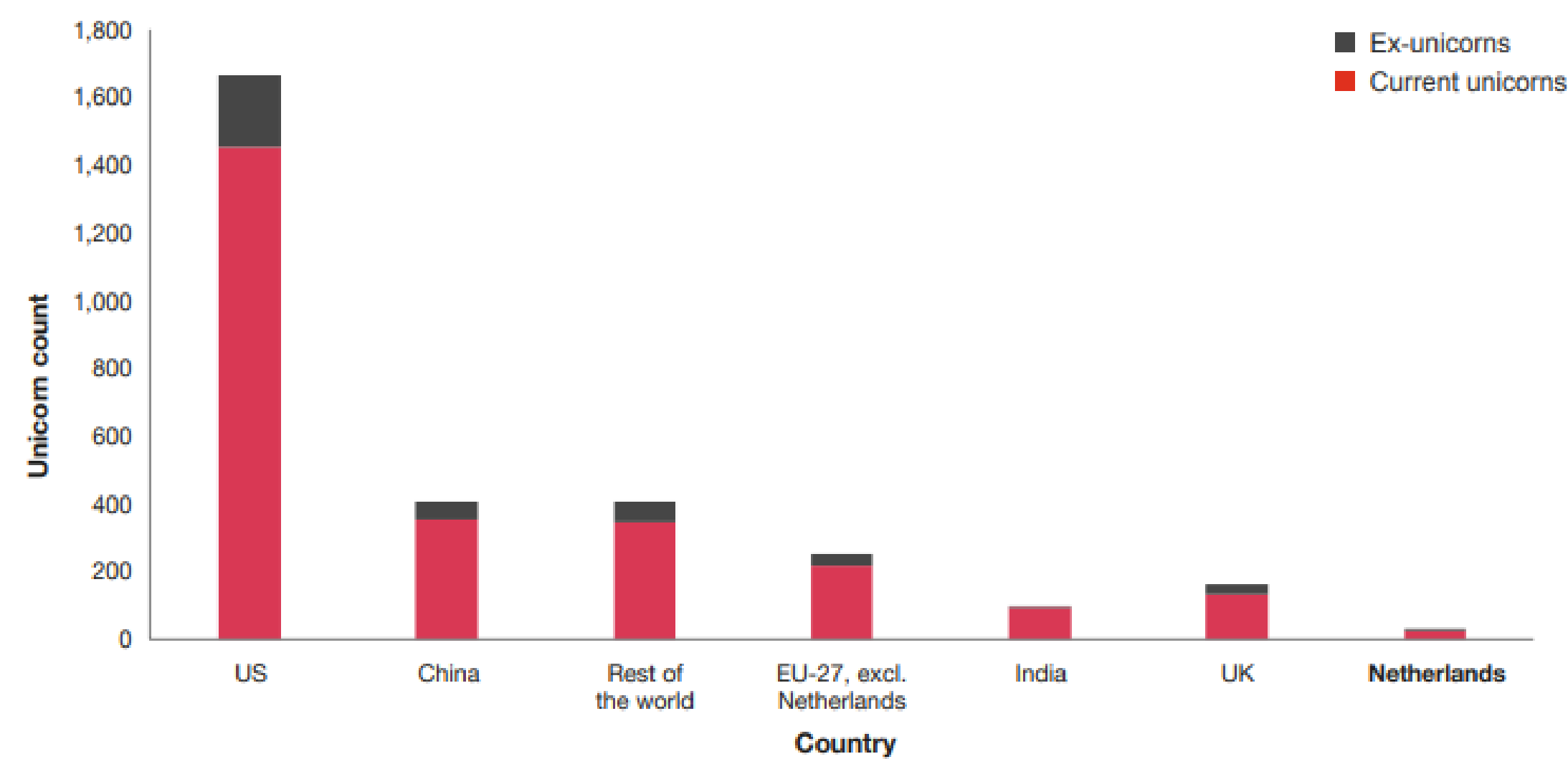


Revival of industrial policy worldwide

- Countries like the U.S. (CHIPS Act, IRA although uncertain under Trump) and China are aggressively using industrial tools to boost domestic capabilities.
- Big shift in relationship with the U.S.

Why this debate? Why now?

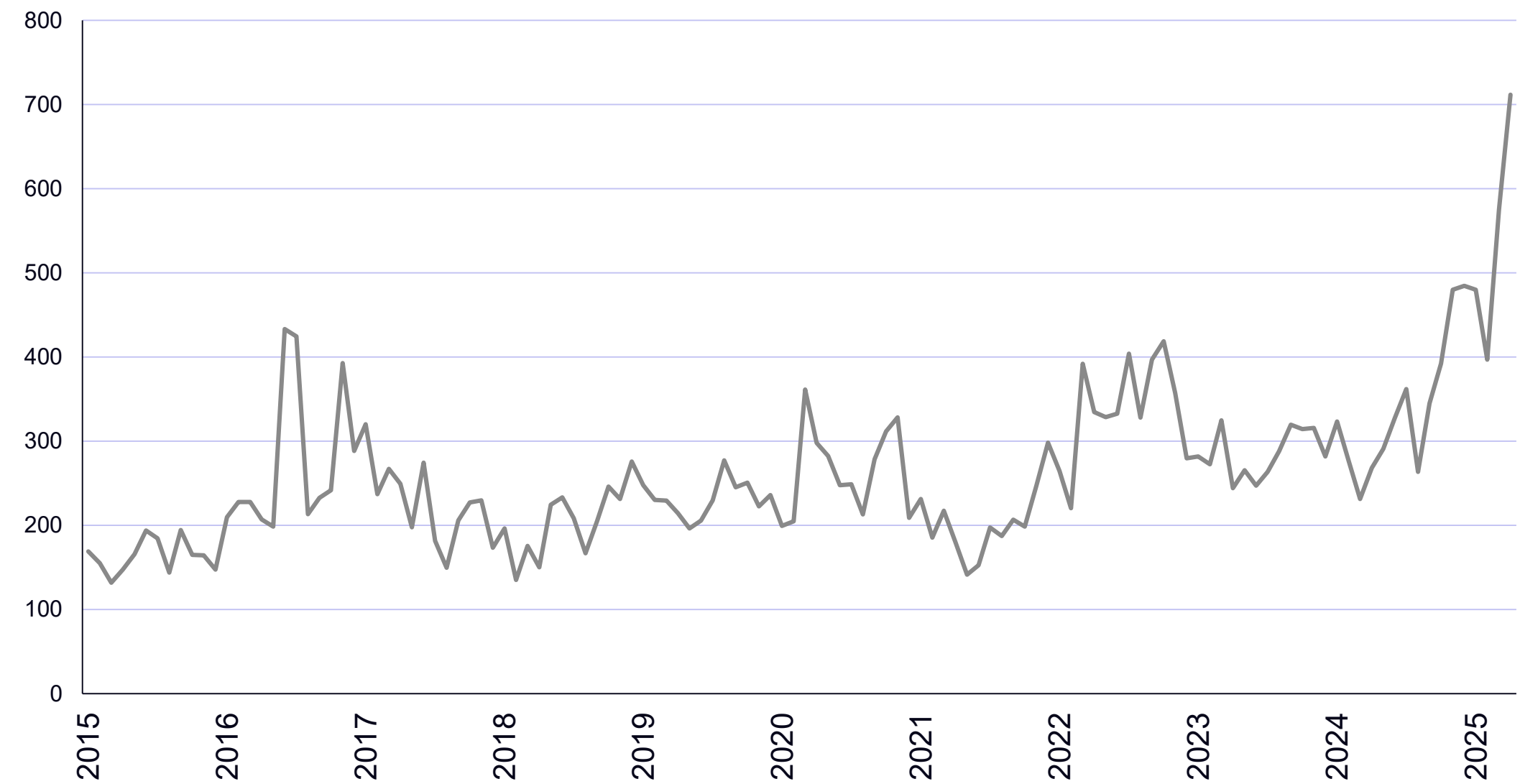
Unicorns in EU vs US, 2024



Sources: Dealroom, PwC analysis.

Source: PwC, “The grass is greener on the other side”.

Monthly EU economic policy uncertainty index, 2015-2025

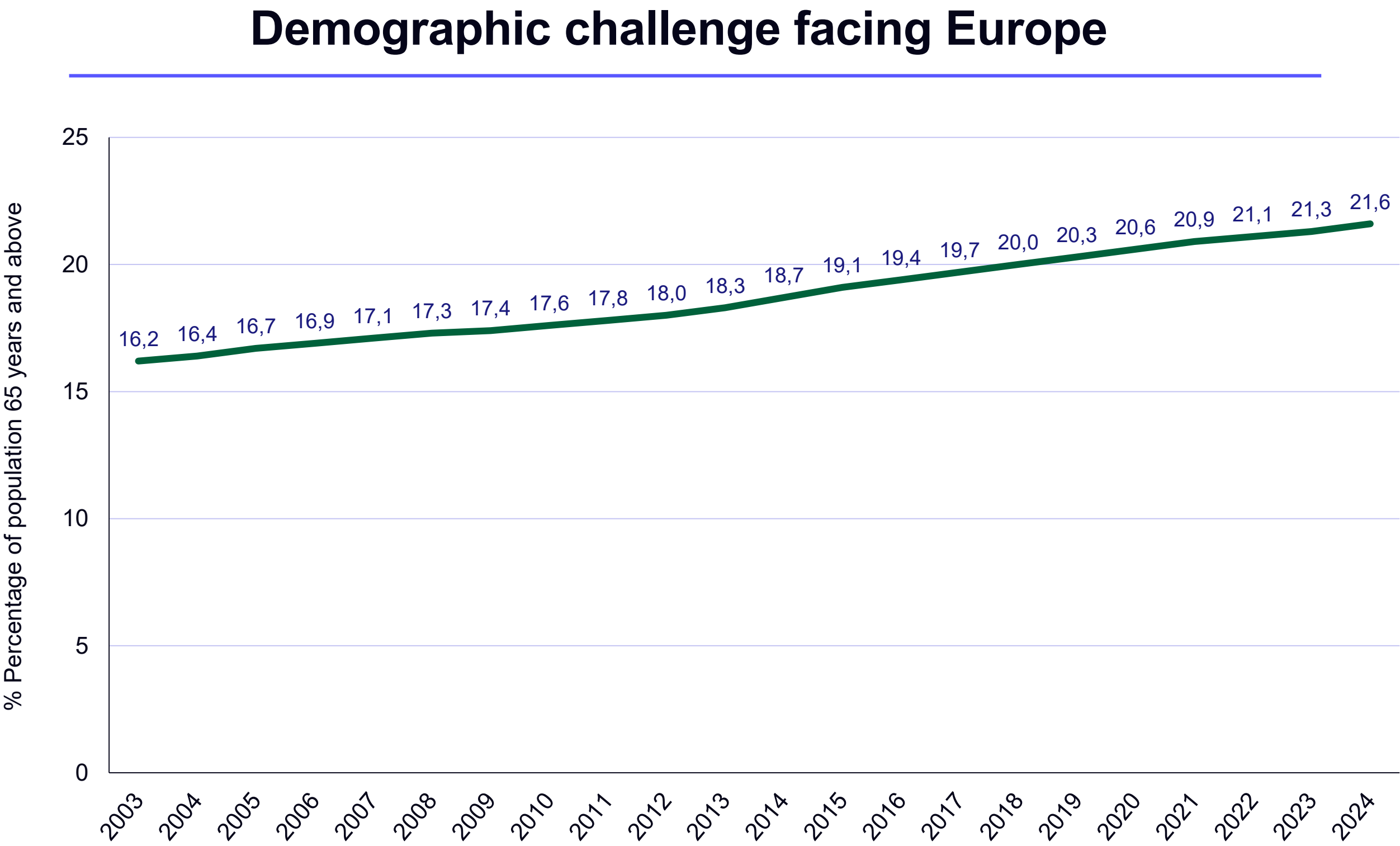


Source: Keystone analysis of Economic Policy Uncertainty data for the EU (Scott R. Baker, Nicholas Bloom, and Steven J. Davis, “Measuring Economic Policy Uncertainty”, 2016)

Notes: The index of economic policy uncertainty (EPU) is based on a monthly count of articles that contain a triple of terms about the economy (E), policy (P) and uncertainty (U). The raw counts are scaled, standardized for each newspaper’s variation, averaged across papers in a country by month, and normalized. For the EU, the index is based on data for France, Germany, Italy, UK and Spain.



Why this debate? Why now?



Source: Keystone analysis of Eurostat data



Europe's new industrial policy

Twin transitions: green and digital

- European Green Deal & Digital Compass guide strategic direction.
- Need to “skill up” Europeans
- Emphasis on climate neutrality, digital sovereignty, and energy security.

The European Green Deal

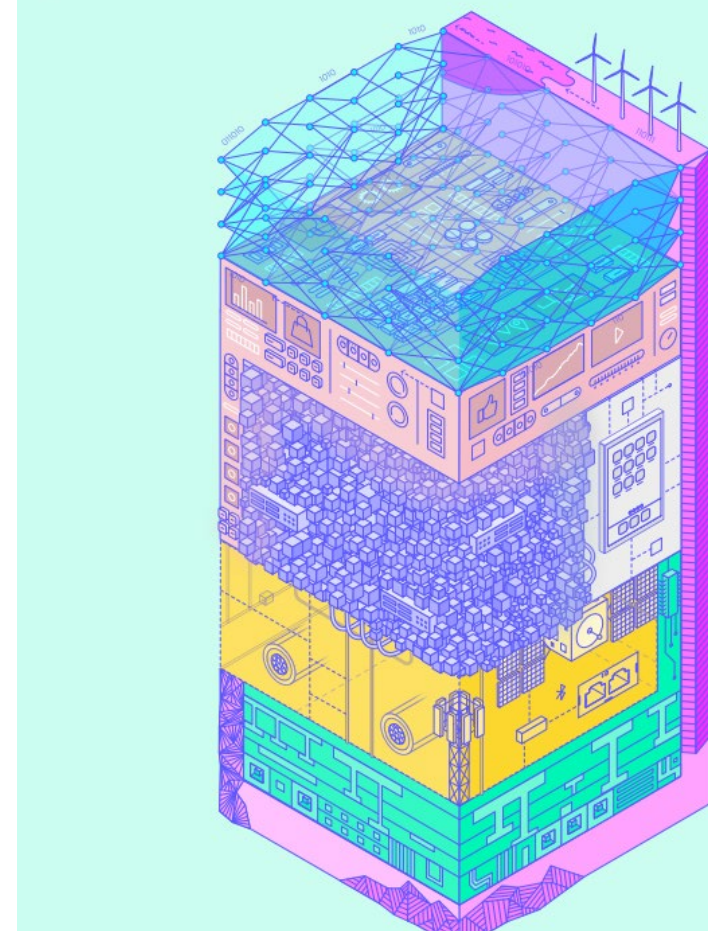
Striving to be the first climate-neutral continent

2030 Digital Compass: the European way for the Digital Decade

Strategic Autonomy & Resilience

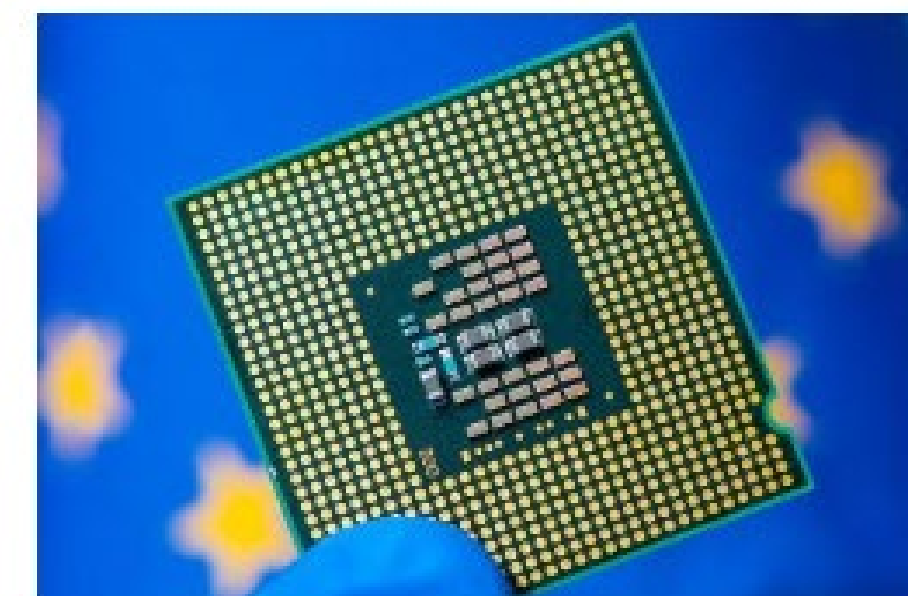
- Reducing dependencies in key technologies (e.g. chips, batteries, clean tech).
- Building capacity in critical raw materials and digital infrastructure.
- **European Defence Industry Reinforcement through common Procurement Act (EDIRPA)** with a budget of €300 million over two years

EuroStack – A European Alternative for Digital Sovereignty



Major policy tools in play

- State aid for **IPCEIs** (Important Projects of Common European Interest): coordinated investments in e.g. batteries value chain, hydrogen.
- **Net-Zero Industry Act**: boosting clean tech manufacturing.
- **EU Chips Act**



Competitiveness remains crucial
to achieve the new goals



Competitiveness remains key for these goals

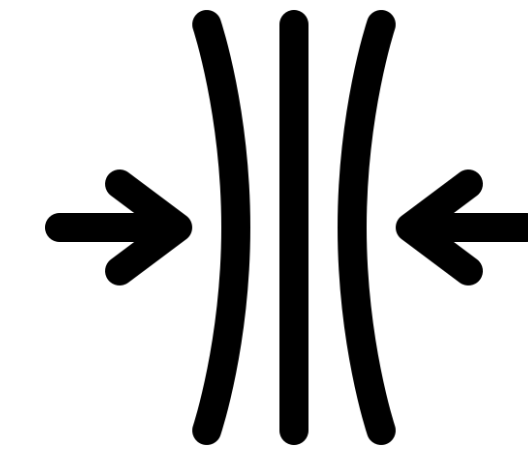
Greater competitiveness leads to greater..



Innovation



Growth



Resilience

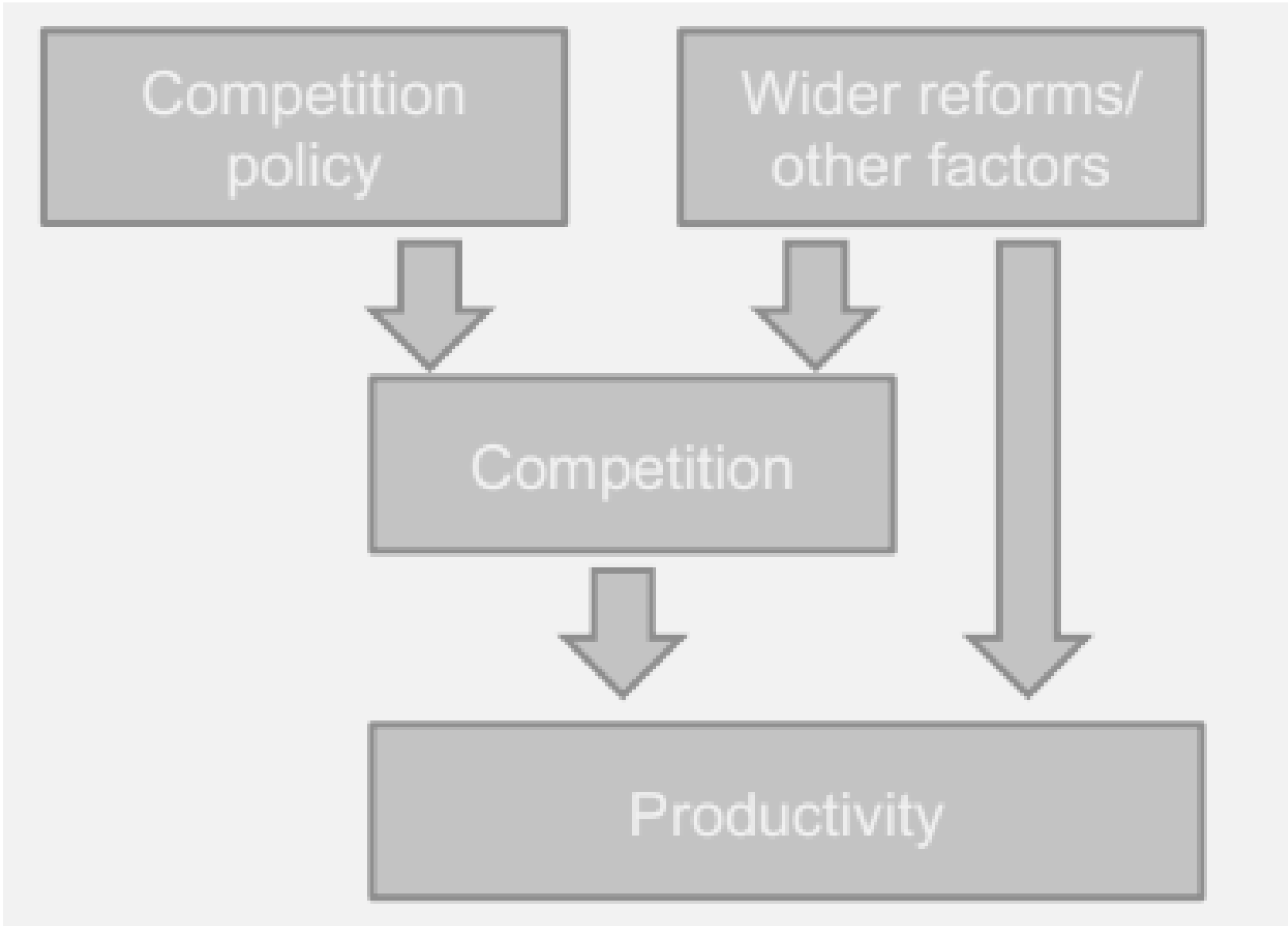
“There is a question about whether vigorous competition policy confl
But.....“stronger competition not only delivers lower prices, but also to
So....“competition policy should continue to adapt to changes in the e

“At a time of tremendous opportunity for the UK, effective competition has a key role to play in driving economic growth, investment, and innovation.”

Sarah Cardell, UK CMA



Competitiveness increases productivity



Three channels by which
competitiveness can drive
productivity

Channel 1

Competition acts as a disciplining device, placing pressure on firm managers to become more efficient.

Channel 2

Competition ensures that more productive firms increase their market share at the expense of the less productive.

Wider Benefits of Competition
Policy and Enforcement

Channel 3

Competition drives firms to innovate and create new products and processes.

Productivity and competition

A summary of the evidence

Source: CMA, “Productivity and competition”, 2015; CMA, “Wider benefits of competition policy and enforcement”, 2023.



Competition increases innovation and growth

What does economics tell us?

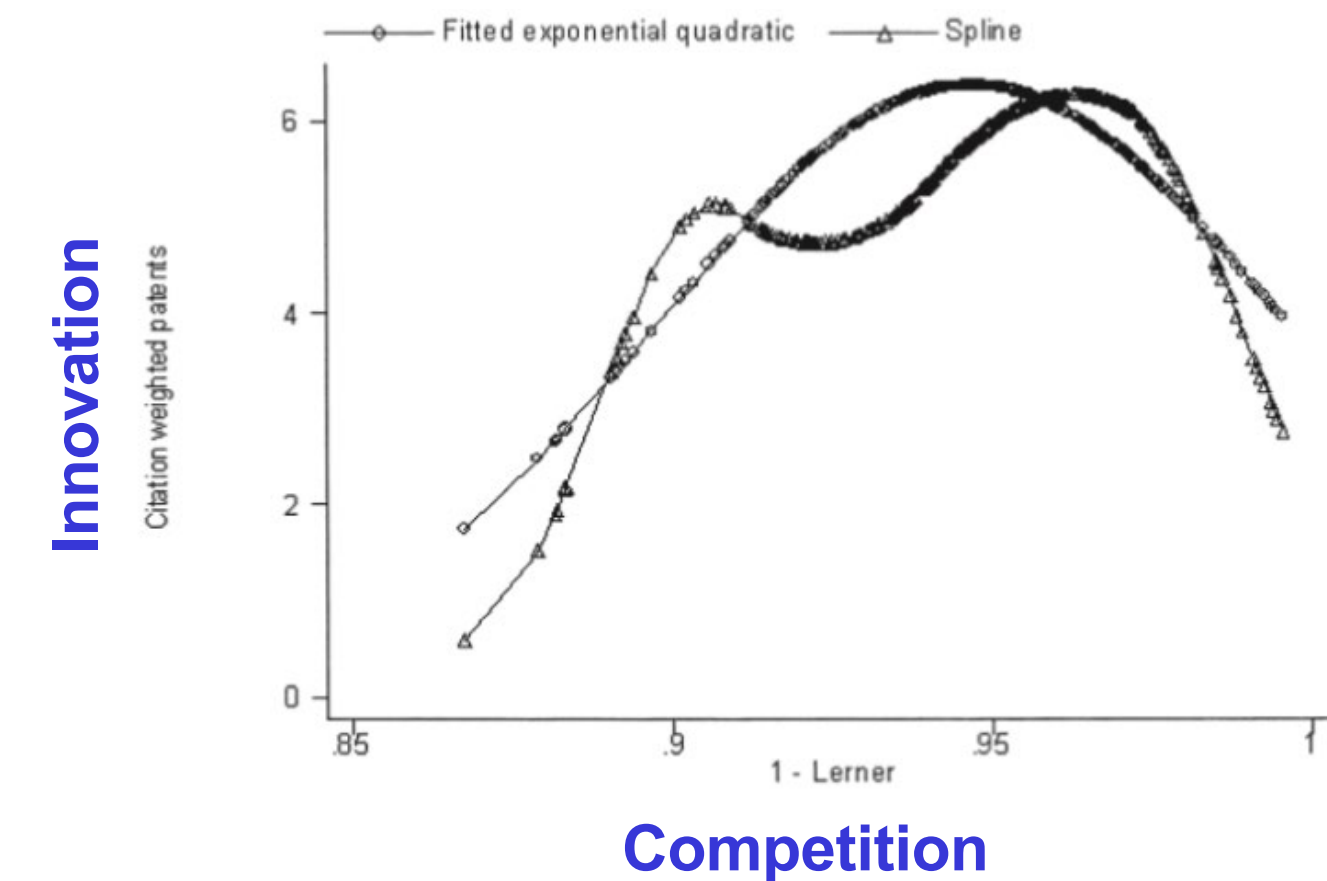
Seminal inverted-U model (Aghion et al, 2005)

- Firms have incentives to compete *for the market* to escape competition *in the market*.
- At high levels of competition, important to weigh up potential dynamic efficiency losses versus static efficiency gains.

Empirical evidence still mixed

- Empirical evidence from the 1990s showed that less concentrated industries had a larger number of patents. Within an industry, larger firms tended to innovate more (Blundell, et al 1999).
- Hashmi (2013) finds a negative relationship between competition and innovation using US data. Beneito, Rochina-Barrachina and Sanchis (2017) find a positive relationship between competition and innovation in Spain.

Aghion et al (QJE, 2005) - An inverted-U effect of industry competition on innovation



Note: Every marker on the figure is an industry

For the cases most often examined in-depth (Phase 2) by competition authorities, competition is already low, so further reductions in competition are likely to not only put upward pressure on prices, but also to chill innovation.



See Rachel Griffith and John Van Reenen, "Product market competition, creative destruction and innovation", CEP 2021.

John Van Reenen, "Does competition raise productivity through improving management practices?" International Journal of Industrial Organization, 2011.

Competition fosters resilience

What is resilience?

- The extent to which business models are robust to shocks.
- There is a lack of resilience when the risks are borne by society rather than firms (who should bear them in well-functioning markets).

A well-recognised cause is market concentration or dependence on a small number of suppliers.

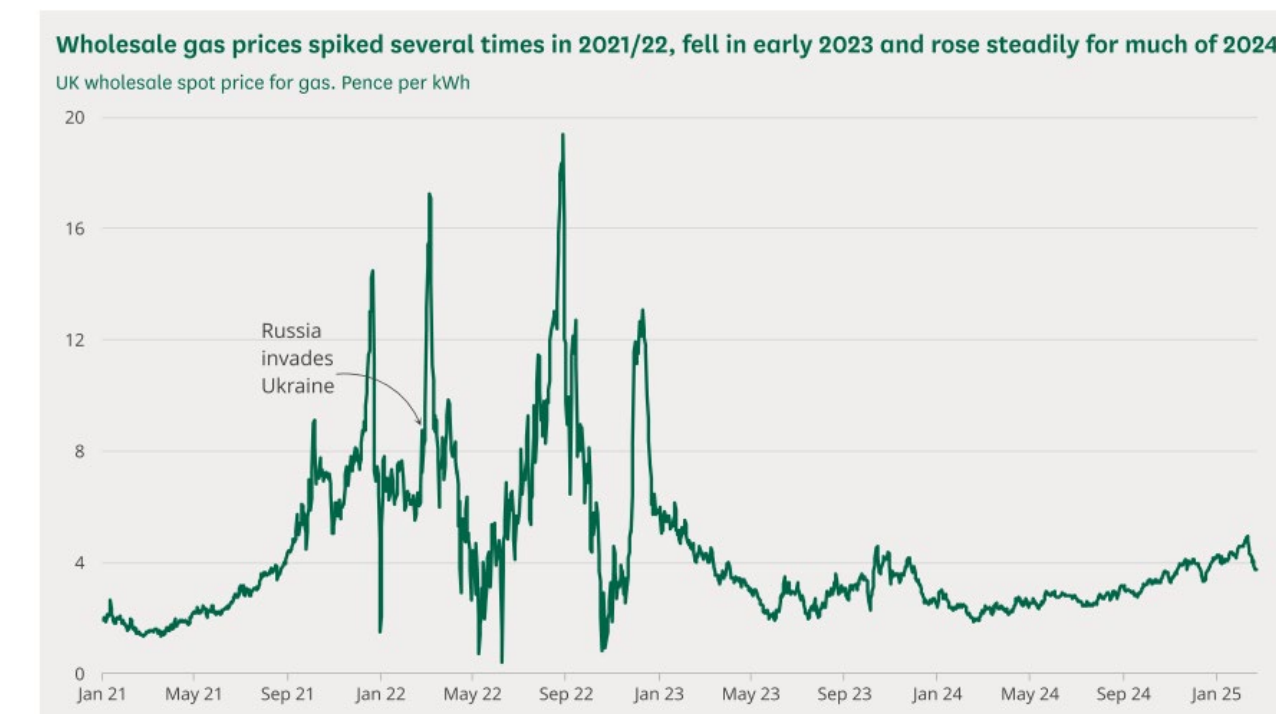
- In concentrated markets, during times of significant demand uncertainty, suppliers are less concerned about losing market share to competitors and therefore do not invest in meeting excess demand. This was evident in many concentrated markets during Covid.

However, the pursuit of resilience presents trade-offs for competition policy.

- Trade off as some measures will increase “normal” price levels or limit short-run efficiencies (for e.g. when a merger is blocked on long-run stability grounds despite short-run efficiencies).
- Competition policy can address structural risks (horizontal and vertical concentration) but not non-structural causes (foreign dependence). For example,
 - Statutory audit market study (CMA, 2019): the market was dominated by the “Big Four” due to a series of mergers that survived antitrust scrutiny, which failed to appreciate the risks to market resilience arising from greater concentration. The CMA conducted a market study and made a series of recommendations to support the emergence of new competitors that were being taken forward by the then government.
 - Retail energy: While the market had many suppliers, a surge in wholesale gas prices from September 2021 and Ofgem’s retail price cap, led to the failure of many smaller suppliers. Competition wasn’t the issue here and instead financially risky business models led to the government having to put a supplier into “special administration” supported the government.

Statutory audit services market study

Final report
18 April 2019



Can an activist industrial policy be pro-competitive?

Yes, if designed correctly

Firms may divert efforts from competing in the marketplace to competing for government handouts.

- Risk that industrial strategy props up inefficient firms at the expense of consumers and innovation.
- Industrial policy should be targeted at:
 - removing existing impediments to competition (such as a lack of financing for startups);
 - investing in education, skills, housing, health and infrastructure; and
 - addressing market externalities (such as high-risk green technology).



Distortionary tools:

- Unconditional subsidies to certain firms without a clear market failure rationale;
- Lax enforcement of competition policy.

Draghi report (September 2024)

The future of European competitiveness

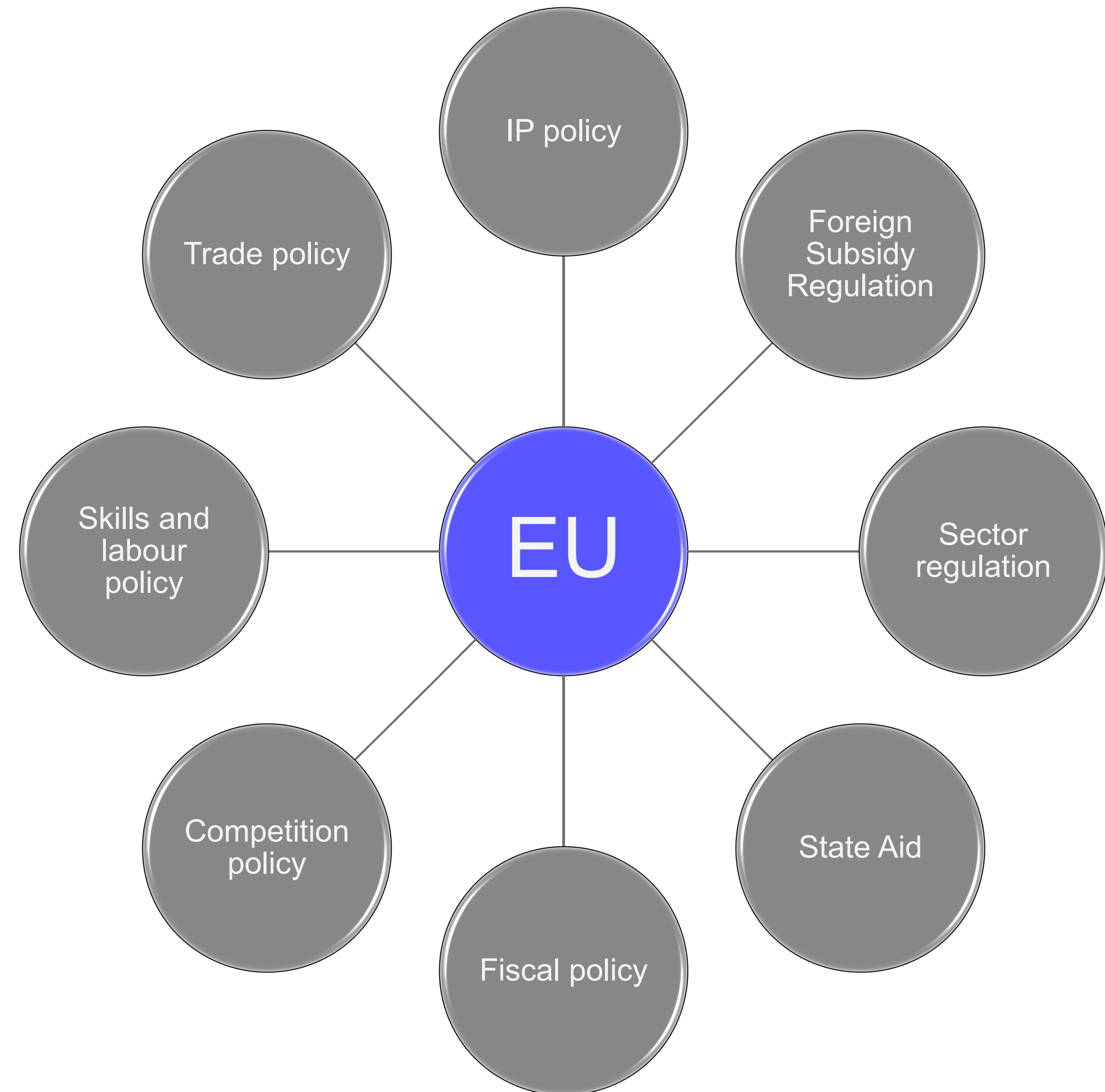
Part A | A competitiveness strategy for Europe

**In the long run, Europe's
competitiveness will hinge on its ability
to innovate and adapt.**



Industrial policy needs complementary tools

**Competition policy is not
the only (or even the main)
policy tool**



Leveraging competition policy

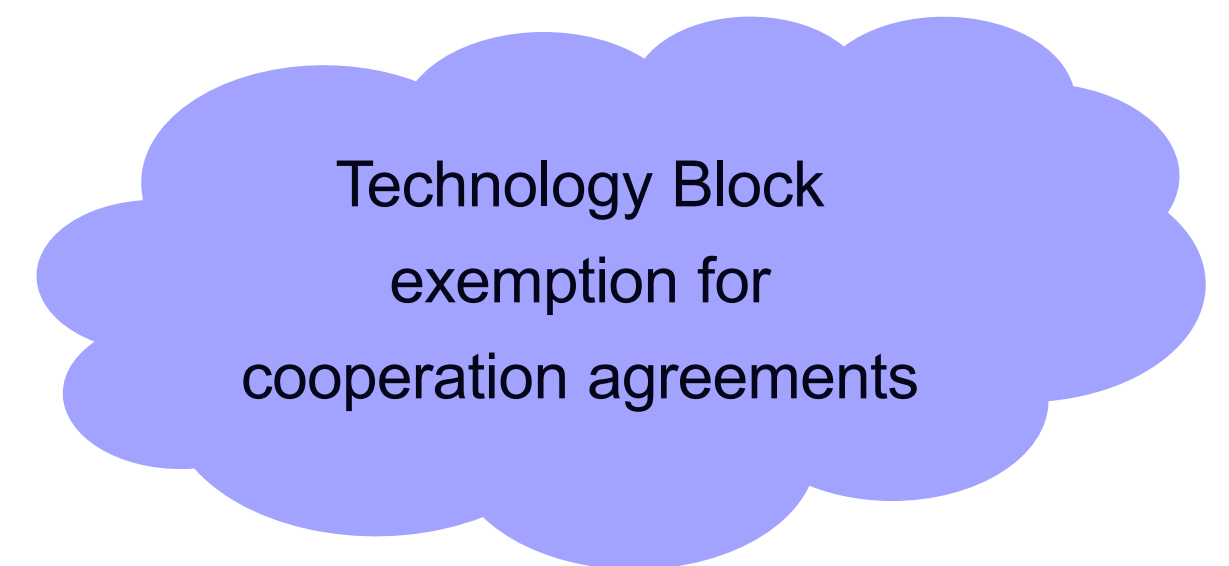


Competition agencies need to be “forward-looking and agile”

Recommendations from the EC’s 2025 Competitiveness Compass



EU Competitiveness Compass



Merger control – unhelpful pressure on the agencies

Should merger analysis consider other public interests, like green technology transitions, protecting national industries, and fostering innovation?

- Competition authorities already examine unilateral effects on innovation (Dow/DuPont, 2017; Bayer/Monsanto (2018), Illumina/Grail (2024))
- It is simply rising up the agenda...but should not distract away from price competition assessment. (*Guillaume Lorient, ICN 2025*)

Efficiency defence?

- Dynamic considerations set against the traditional static considerations. **EU Merger Guidelines consultation recognise these trade offs.**
- Empirical evidence on them materialising is limited.

Role of remedies

- Behavioural remedies
- Who bears the risks?



Embed competition principles in industrial policy



The CMA Growth and Investment Council will have an important advisory role to provide 'expert knowledge and stakeholder insights' on opportunities for growth

Competition authorities could advise governments on how to achieve policy goals with minimal competitive distortion.

- Taking the example of subsidies for semiconductor fabs, the competition authority can guide structure it as a competitive process open to multiple firms, perhaps even foreign investors, with conditions that prevent misuse of funds.
- This ensures the subsidy addresses the supply security goal but doesn't unduly entrench one company.

Identify priority sectors

- Authorities can identify priority sectors where competition issues might hinder industrial objectives – for example, noting if a crucial input (like rare earth minerals processing) is controlled by very few players, and recommending relevant policy tools.
- Tools such as market investigations (e.g. UK).