

THE DAVID HUME INSTITUTE



AN HISTORICAL LOOK AT THE BENEFITS  
OF COMPETITION POLICY

Lecture to The David Hume Institute  
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Director-General of Fair Trading

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## FOREWORD

It was the good fortune of The David Hume Institute that early in his term of office Mr John S Bridgeman, Director-General of the Office of Fair Trading, was willing to give a public lecture under the auspices of the Institute.

Mr Bridgeman starts his lecture by engaging David Hume in a hypothetical conversation regarding international trade, competition policy and consumer affairs. This reveals many aspects of David Hume's writings that resonate with current thinking on these topics. At this point the Director-General turns to the question of the "Scottish Dimension" and whether this calls for any special treatment from the Office of Fair Trading. While acknowledging the uniqueness of Scotland, the argument is made that this is not, in itself, an issue in terms of competition policy or consumer affairs. Recent cases concerning electricity supply and salmon production are utilised to explain this position.

In the third and final element of the lecture, Mr Bridgeman draws on recent cases concerning as varied fields as the Law Society of Scotland and the Faculty of Advocates rules, the Securities and Investments Board and the Personal Investment Authority disclosure rules, and the activity in the market for residential estate agencies services of the Solicitor's Property Centres in Aberdeen and Edinburgh to bring out something of his own approach to the work of the Office of Fair Trading. This is seen to be a concern that regulatory intervention should enable "competition between suppliers to be conducted on a fair and reputable basis".

The lecture was delivered before a well informed and appreciative audience in the Royal Society of Edinburgh. There followed a lively and good-spirited question and answer session which is, unfortunately, not captured here. The David Hume Institute is delighted to be able to make Mr Bridgeman's lecture available to a wider audience through publication in our Occasional Paper series. As always in our publications, the views expressed are those of the author alone, the Institute holding no collective opinion upon the issues raised.

*Hector L MacQueen and Brian G M Main  
Directors of The David Hume Institute*

## Introduction

I am most pleased to have the opportunity to address you this afternoon. I feel I have already come to know The David Hume Institute quite well through its work of a few years ago on mergers. This took the rather sceptical view—and I share it! This is also my first official visit to Scotland as Director General of Fair Trading. I have to say that I delight in working outside London, but in case you think that my presence here suggests someone unacquainted with, or unsympathetic to, Scottish concerns let me try to dispel that idea. During my 30 year career with the British Alcan Aluminium group, there were many occasions when I found myself in Scotland. Furthermore I lived for 12 years in Warkworth on the Northumbrian coast—I'd better describe it as 91 miles from Murrayfield.

Amongst the aluminium operations for which I was responsible, at one time or another, there were smelters and hydro-electric power stations in the Highlands, chemical operations at Burntisland in Fife, rolling mills at Falkirk and Polmadie and metal distribution centres at Aberdeen and Glasgow. So quite apart from the fact that my middle name is Stuart and I had a Scottish great grandmother—I do feel rather at home here.

Neither are my experiences of Scotland confined to business. My family and I also enjoy its hospitality with annual holidays at Sherramore on the Upper Spey (it's a few miles from Laggan on General Wade's military road)—sometimes we go there on our own and sometimes with friends, always together as a family. Here we can enjoy countryside of the most amazing beauty and I can do battle with trout of the most amazing cunning!! It is at Sherramore that I "*Feed on ambrosia, drink nothing but nectar, breathe incense only, and walk on flowers*". I hope that some of you will know in whose debt I am for that quotation.

During my short time at the OFT there have already been some high profile "Scottish cases", to which I will return. And, unlike the "Scottish play", I will name.

In thinking about themes for my talk today, I thought I would try to bring together three elements: a focus on the inspiration for this celebrated Institute, David Hume, the Scottish dimension to the work of the Office of Fair Trading and some of my own approaches to the OFT's work.

### **A conversation with David Hume (1711-1776)**

It is tempting to imagine what a conversation with David Hume might be like, and what his views on the contemporary problems I face in the competition and consumer world might be. I have readily, and with anticipation, succumbed to that temptation. He was a distinguished man of letters with an impressive range of interests—his views would be bound to stimulate. (I hasten to add at this stage that I have, as yet, been unable to satisfactorily compare my years in Montreal, in French Canada, as Strategy Advisor to Alcan's Chairman, with David Hume's time in Paris; he acted as Secretary to the British Ambassador.) But to continue: Adam Smith, Hume's close friend, considered him after his death "as approaching as nearly to the idea of a perfectly wise and virtuous man as perhaps the nature of human frailty will admit"<sup>1</sup>. That in itself was a great, if somewhat daunting, recommendation. I also became intrigued by the prospect of a conversation with David Hume because I suspected we would find ourselves in large agreement about many fundamentals of business and consumer behaviour, and perhaps also matters of policy. I did find that—and I found it reassuring.

Whilst it is true that Hume is largely known to financiers and economists for his writings on money and interest there are other works which help reveal his approach to market and fair trading issues. He is, of course, well known as an important influence on his friend Adam Smith<sup>2</sup>. But his views on a number of topics were significant in their own right. In his analysis of the free-trade issue, Hume met the mercantilist arguments head-on: "Trade and growth among nations does not involve a conflict of interest" he suggested. Even where foreign expansion involved some competition with home industry he argued that the stimulating effect of such competition on the home "spirit of industry" facilitated any adjustment.

I agree wholeheartedly with this. Foreign competition is normally beneficial, and indeed competition in today's domestic markets is increasingly driven by international considerations. As consumers and businesses become more mobile and as newer communication and trading technologies develop and diffuse, so markets are subject to competitive pressures from new sources. Certainly, British Aluminium in Scotland faces a very wide ranging set of pressures. Bauxite is plentiful and mined and traded worldwide. Aluminium smelted in Scotland is essentially a global commodity with its price fixed daily on the London Metal Exchange by representatives of international buyers and sellers. The official prices set there each morning after trading are used by producer countries and the majority of the world's industry for pricing aluminium as a raw material. Whatever the cost of manufacture, in whatever currency, the international selling price for all output is the same. Commodity markets are now generally international in scope, to the benefit of all. Of course, national and local markets still exist, they remain the norm for many products—but business has an increasingly international flavour.

### **Hume and trade**

In Hume's day, the influence of mercantilist principles was to be found not just in the writing of informed commentators or scribblers but in the actual policies followed by government. We will all allow some dispute, looking retrospectively, at how much of a coherent doctrine underlay such policies. Be that as it may, these policies interfered with natural market mechanisms in such diverse areas as foreign markets, the operation and development of colonies, shipping and domestic industry. I will not go into this in any great detail. That is done elsewhere by those more informed than I<sup>3</sup>. But perhaps most noteworthy, from my viewpoint, were the chartered trading companies, such as the Hudson Bay Company and the East India Company, which were given exclusive monopoly trading rights in specified regions of the world. It is difficult to believe that these monopoly trading companies did once exist; they were very akin to the state monopoly trading companies of the former communist states.



Hume maintained<sup>4</sup> that international specialisation and competition was the only firm basis for prosperity. He remarked that “as a British subject I pray for the flourishing commerce of Germany, Spain, Italy and even France itself”,<sup>5</sup>—a sentiment which marks him out, perhaps, as a European by instinct. He did after all live abroad in Vienna and Turin, as well as Paris and other parts of France. Quite what he would have made of the move to a single European currency I do not know, but his endorsement of the French was remarkable even then, given the wars that took place in Europe. Whilst modern trade theory and the search for the sources of national competitive advantage are now considerably more developed than in Hume’s day, I think his conclusion on the benefits of international trade stand up, even if contemporary reasoning is now more complex.

### **Hume and competition**

The mercantilist’s approach to international trade was mirrored in part in domestic policy, and not just with overtly protectionist measures like tariffs. The common law term monopoly, plus the legal sanctions of patents granted by the King, were of particular importance in the seventeenth and early eighteenth centuries. Historians may differ on the extent and duration of monopolies and cartels over that period; they may argue about the impact of liberalisation, and what would now be called anti-trust measures, such as the 1624 Anti-Monopoly Act. But at one time or another, mining, coal, tin, alum, wine, salt, glass, soap and pins all seem to have been affected<sup>6</sup>. Interestingly some of these remain highly concentrated today.

Hume, along with other writers, condemned these monopolies and cartels<sup>7</sup>. What is less well understood by historians is the interaction in those days between the protectionist trade policies, the regulatory barriers to competition, the Crown privileges and the private agreements between persons seeking profit (often through Guild rules). And these are all features which can continue to apply today.

Cartels then have a long and dishonourable history. Hume observed them in his day and condemned them. For me their elimination remains a top priority, and I am pleased that my predecessor, Sir

Bryan Carsberg, launched a Cartel Initiative in February 1995. I have given it vigorous support. Cartels—bid rigging, price fixing and market sharing arrangements—offer few, if any, efficiency benefits to society, whatever the participants may sometimes plead. I hope that the present consultation on UK competition policy will eventually lead to much tougher laws to deal with such cases, both in terms of my investigatory powers and in the penalties that can be exacted on conviction. That would be a most welcome development. Strengthening of the law to deal with monopoly would also be desirable. I have in mind the Government's previous proposals to give me stronger investigatory powers, and some form of interim measure by means of which the "ring could be held", so to speak, while an investigation is under way. I believe this too would be a major step forward. There may well be other desirable steps that can be taken. I should add here that my Cartels Task Force is next week visiting Scotland to publicise its work and make contacts with anyone with points or allegations to put. It will be in Edinburgh at 10.00 am next Wednesday 20th March at Victoria Quay. Any whistleblowers amongst you need not of course wait so long. Please feel free to approach me after. However, this is all for the future.

### Hume and consumers

Back in time with consumer policy, Hume has little directly to say. Modern consumerism is largely a product of the middle and late twentieth century, leading to notions of the "rights" of consumers and the balance of responsibilities between consumer and producer. In the eighteenth century, "*caveat emptor*" largely held sway. But Hume would certainly have been aware of weights and measures legislation. It was a criminal offence to supply bread and ale in short weights<sup>8</sup>, while other legislation allowed local justices to fix the price of some products according to weight and other relevant market conditions. Various royal decrees sought to establish basic standards of measurement.

Of course, during Hume's lifetime the circumstances of the average consumer were unlike today. Everyday life was very different. Consumers were less numerous but almost certainly more self reliant. The Scottish population in 1755 was 1¼ million, some 25% of what it is now<sup>9</sup>. The agrarian revolution was in its infancy. The

industrial revolution was being born. The standard of living was very much lower and the range and complexity of products available to consumers was quite small. Buyers were faced with few products that were not within their range of experience, and geographic mobility was low. This is not to say that Hume would have been unacquainted with consumer problems. But these seem likely to have been confined to the wealthy. Financial crises, such as the South Sea Bubble (1721) occurred when Hume was a boy and no doubt there were many more local scams, such as charlatan doctors tending the sick. Fraud and dishonesty in trade, alas, have been with us since commercial dealings began—at least since the Babylonians 4,000 years ago.

Nevertheless, David Hume seems to have come to entertain certain ideas of fair trading. In the posthumous edition of his *Essays and Treatises on Several Subjects*, the author's advertisement, which he had prefixed to the volume, speaks of practices "contrary to all rules of candour and fair-dealing". The idea of a sense of fairness or justice in commercial dealings, based upon consensus view, would of course fit well with his philosophical approach to the individual.

I am sure then that a conversation with David Hume would be stimulating for me—indeed for us all! Both because of his obvious awareness of competition and, to a lesser degree, consumer matters, and because of his familiarity with matters Scottish. That is my second theme for this afternoon.

### **The Scottish Dimension**

It is a common occurrence for a regulatory authority to be presented with claims that someone, be it the complainant or the object of the complaint, is a special case deserving special treatment. I am, of course, acutely aware that devolution and regional government are once again at the centre of policy debate in Scotland and elsewhere in Britain, and that this is based on a desire for a recognition of each country's special features.

As you might expect I have no public views on the regional government issue, but it is sometimes suggested that either Scotland

is a special case in competition and consumer matters, or that my treatment of Scottish cases has been at odds with cases elsewhere.

It is true that Scotland is a very particular country, with its own special demographic, geographic, historical, legal, educational and cultural traditions. These distinctive features give it an identity that is undoubtedly unique. But that is a one sided story. Although the distinctive features of Scotland are obvious, what is not so obvious is if there are any differences from a competition or consumer perspective. Perhaps more striking economic differences exist between, say, Edinburgh and the Western Isles, than they do between, say, Edinburgh and London (both of which are rival metropolitan and financial centres)? I hesitate to mention Glasgow, but that was recently, I believe, the European City of Culture. Are Glasgow and Edinburgh then more different than Edinburgh and London? Perhaps there is also more similarity between, say, milk or beef producers in Scotland and England than there is a difference?

As for consumers, there are clearly some distinctive preferences. Sales of white pudding or curling equipment do not occur much outside of Scotland. In many areas, such as architecture (with the tenement tradition) and media and leisure (with the Daily Record and the Scotsman), distinctive Scottish products exist. Many such as whisky, salmon and woollens find buyers elsewhere. However, Scottish consumers, in turn, seem to find Japanese cars and consumer electronics, American computer software, restaurants and soft drinks and even English football players equally as attractive. In short, consumers have some local preferences but they also seem to be subject to a growing sameness in the British Isles.

It is, perhaps, a more open question whether the public interest, for a competition authority, is any different in Scotland than in the rest of the UK. Certainly the MMC, in those cases which Directors General have recommended be referred to it, have not found any distinguishing peculiarities in Scotland, nor employed an approach which differs in any discernible way from that used elsewhere. The MMC's reports on local bus markets, for example,<sup>10</sup> illustrate this. Indeed it would be rather surprising if they did adopt a distinctive approach.

It has been suggested that some of the recent developments in the utility sector lack consistency. In particular, I recommended allowing the merger of ScottishPower with Manweb, whilst opposing the PowerGen – Midlands Electricity and National Power – Southern Electric mergers, both of which were sent to the MMC for investigation as to the competitive impact of the vertical integration of generation with distribution. I have also made recommendations about mixed utility mergers, but these have not so far involved Scottish companies.

Why then did I recommend apparently different treatment to superficially similar cases? Was this biased in favour, or in opposition, to Scottish interests? I am afraid the truth is more mundane. Whatever the merger case, my advice to the Secretary of State will always include an assessment of the effect of a merger on the structure of markets in which the parties are engaged, and on the effectiveness of competition in those markets. Where a merger leads to a significant increase in concentration, there are immediate grounds for concern, even though these may be allayed if the market is open to newcomers, (including newcomers from abroad) or is subject to rapid technological change.

In the ScottishPower – Manweb case, exactly this approach was followed. It necessitated identifying precisely the market involved and actual and potential competition within it. The key factor here is that the Scottish and English (and indeed Welsh) markets for electricity are largely separate. There are interconnectors, but these have very limited capacity, in terms of market size. Given this limited physical interconnection, the vertical integration of Scottish Power with Manweb is much less significant and is unlikely to have a significant effect on competition. This conclusion would, of course, have been wrong if there were a single combined market with the possibility of substantial power flows over all of mainland Britain. This is precisely why the English vertical mergers raised competition concerns, especially when the energy markets are in process of further liberalisation. In my view a full examination of the proposed structural changes on the likely development of competition was needed.

The importance of foreign competition can be seen in another recent merger case, Booker-McConnell's link with Marine Harvest International. Whilst this combination gave the company over 25% of Scottish salmon production, the market is not so narrowly defined. Scottish salmon prices are very heavily influenced by foreign competitors, chiefly Norway. In those circumstances, the merger again raised no market power concerns.

I hope David Hume would have agreed with my reasoning and conclusions so far. But what of some even more recent and on-going cases in the financial and professional services field? David Hume did after all work as librarian for the Faculty of Advocates for some time.

My general approach to financial and professional services matters is to treat them like other goods and services. They occupy a more important part in the economy today than in Hume's time, and their importance is likely to grow. They also present some major challenges to competition and consumer policy. Generally, financial and professional services are complex products, infrequently purchased by consumers and with the potential for significant adverse monetary or other consequences when things go wrong.

Taking financial services first, I am aware that the Scottish financial community is one of long standing, centred on this city. It makes up a significant part of the Scottish economy, accounting for 15% of the country's GDP and more than one out of every 10 jobs. I will not recite all the notable financial inventions, for which Scots have been, and continue to be, responsible. But these include the watermark on banknotes, the overdraft and the branch banking system. More recently Scots have pioneered electronic home banking.

My Office has been quite active in this field. On the retail financial services front, the new product and commission disclosure rules of the Securities and Investments Board and the Personal Investment Authority came into force for "life products" in January 1995. These rules have increased and standardised the information given to investors about such products. I hope, like me, you welcome them as enabling consumers to make better decisions and for more effective

competition to occur. Amongst you will be, no doubt, some of the winners and losers of that process.

As for “non-life products”, my officials continue to consult with the Personal Investment Authority on new disclosure rules. I have not reached any conclusions on this yet. Indeed the PIA have not even finalised the rules. Nevertheless I will be looking for broadly equivalent disclosure across competing products. This is the only satisfactory basis for effective competition.

I would try to explain my position to David Hume in terms of the weights and measures legislation he knew. The aim of that was to ensure consumers were not short changed and could compare product offerings. It also enabled competition between suppliers to be conducted on a fair and equitable basis. Dishonest or inefficient traders would be rooted out. I think of many modern issues in these terms. I hope David Hume would concur.

As for professional services, I wish to mention two cases. One of my predecessors made two reports in 1992 about multi-disciplinary practices, concerning the Law Society of Scotland and the Faculty of Advocates rules.<sup>11</sup> In both cases, my predecessor found rules preventing such practices anti-competitive. I agree with that. Generally, businesses should be free to form associations to meet market demand. Any restraints on that have to be very well justified. Here too, I think Hume would agree. He was after all something of a polymath—philosopher, economist, historian. He was the embodiment of a multi-disciplinary practice!

The second case is that of Scottish residential estate agency services. Some of you may know that this was yesterday referred to the Monopolies and Mergers Commission as a complex monopoly investigation. This is a particularly interesting case. The Scottish legal system, housing market and the role of estate agents are all quite different in Scotland from the position in England and Wales. This has taken some time to properly analyse. Indeed for some 10 years my Office has been trying to remove an imbalance between solicitor and non-solicitor estate agents, prompted initially by complaints from the Scottish Consumers Council, the Royal Institution of Chartered Surveyors, the National Association of Estate Agents and

others. At first the issue was addressed by taking the Solicitor's Property Centres in Aberdeen and Edinburgh to the Restrictive Trade Practices Court (Scotland) in 1993 and 1994. But an opinion delivered earlier this year by Lord Marnoch ruled that the agreements of such bodies were not registrable. Consequently, I have had to use other competition legislation. We will have to see what the MMC now makes of this and I will comment no further.

So is Scotland a special case? In my narrow competition and consumer terms I think not. The same high standards of proof, the same analytical methods and the same processes are applied in my Office to Scottish cases as they are to any other.

I do not think this conclusion would surprise David Hume. His life was devoted to discovering general propositions in economics and philosophy. My considered view is that it would be uncharacteristic for him to claim that Scotland was different. According to one commentator,<sup>12</sup> "Hume's ambitions were to lay the foundation for a would-be Newtonian science of man". Given that, he would hardly allow for special cases.

In conclusion, I feel sure that David Hume, like me, would be able to reconcile the proposition that Scotland was wonderfully unique with the search for a standard approach to competition and consumer matters. I hope I have convinced you of that today. Of course we might not have agreed on all the points of detail. But then it is the detail which, perhaps, makes everything unique—isn't it?

## NOTES

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7. Hume, David, *History of England*, 5, p.458, quoted in Levy, *ibid*.
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11. OFT, *Law Society of Scotland: rules prohibiting the formation of multi-disciplinary practices*, June 1992, and, OFT, *Faculty of Advocates: proposed rule prohibiting advocates from forming legal relationships*, June 1992.
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## **Books**

The Deregulation of Financial Markets

*edited by Richard Dale, Woodhead-Faulkner, London, 1986*

Governments and Small Business

*Graham Bannock and Alan Peacock, Paul Chapman, London, 1989*

Corporate Takeovers and the Public Interest

*Graham Bannock and Alan Peacock, Aberdeen University Press, 1991*

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*Michael Hay and Alan Peacock, Alden Press, Oxford, 1992*

The First Decade

*edited by Nick Kuenssberg and Gillian Lomas, Edinburgh University Press, 1996*

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