BACKGROUND NOTE

Entrepreneurship and Competition Policy

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Fazio (2010) identifies two major views that link competition and entrepreneurship. One is that of Kirzner who sees competition as analytically inextricable to entrepreneurship as incumbents and new entrants compete for market shares. The other is that of Schumpeter who sees entrepreneurship as the creation of new markets through innovation, which leads to competition among the innovating firms.[1]

To promote healthy competition, policies that regulate markets should help entrepreneurs level the playing field by ensuring equal market access in terms of selling products and obtaining inputs. Such competition policy should limit the existing market players' ability to collude by prohibiting market incumbents from creating artificial barriers to entry, preventing anticompetitive mergers, and prohibiting discrimination against small and new market players.[2] When competition policies are properly implemented, they would encourage entrepreneurship by sending clear signals that individual initiative, enterprising, and responsible risk-taking activities are properly valued. Failure to regulate anticompetitive behavior actively would foster a culture that tends to discourage changes, competition, and contestability in the marketplace.

[1] Obaji and Oluga (2014) classifies entrepreneurship into three groups: behavioral, occupational, and synthesis. Kirzner and Schumpeter belong to the first group.

[2] Refer to the discussions in, among others, Audretsch, Baumol, and Burke (2001); Golodner (2001); Audretsch, van Leeuwen, Menkveld, and Thurik (2001); and Kemp and Lutz (2006).

Although a healthy competitive market encourages entrepreneurship and innovation, empirical studies on the direct relationship between competition policy and entrepreneurship are few and inconclusive. Choi and Phan (2006), for example, using the United States data from 1968 to 1993, proxies competition with the share of large firms in the economy and the amount spent on competition policy, and argues that competition has a positive and significant effect on the formation of new firms. Fazio (2010) discovered the same positive relationship using data on new business registrations and the Global Competition Review ranking of national competition authorities for 32 countries. However, the study shows that better competition policies only encourage entrepreneurship after a certain threshold. This is because the difference between a bad and a very bad regulatory regime is not as stark as the difference between a mediocre and a good one.

Conversely, Schaper et.al (2008) finds no relationship between entrepreneurship and a highly ranked competition policy when investigating the correlation between competition policy and entrepreneurship by using data on three existing indices: the Global Entrepreneurship Monitor, the Global Competition Review, and the Antitrust Index. This outcome may be influenced by poor data issues as the data could be too crude of a measurement. They also contend that competition policy may not be the primary factor that drives entrepreneurship because the decision to start a business is driven primarily by a confluence of factors, such as personal motivations, demand opportunity, and access to resources. Capelleras, Mole, Greene, and Storey (2008) further argues that a country's level of entrepreneurship is relatively fixed, leaving regulatory regimes with a limited impact on the level of entrepreneurial activity, which is driven more by entrepreneurial background and skills.

Regardless of the mixed empirical findings, healthy competition remains essential for driving markets to operate efficiently. In this regard, appropriate competition policies would continue to play a role in encouraging markets to function efficiently.

Digital Entrepreneurship and Competition Policy

Recent rapid advances in digitalization have created new challenges for implementing fair competition policies, particularly with the emergence of the coronavirus disease (COVID-19) pandemic, which has pushed consumers and businesses to shift dramatically toward online channels.

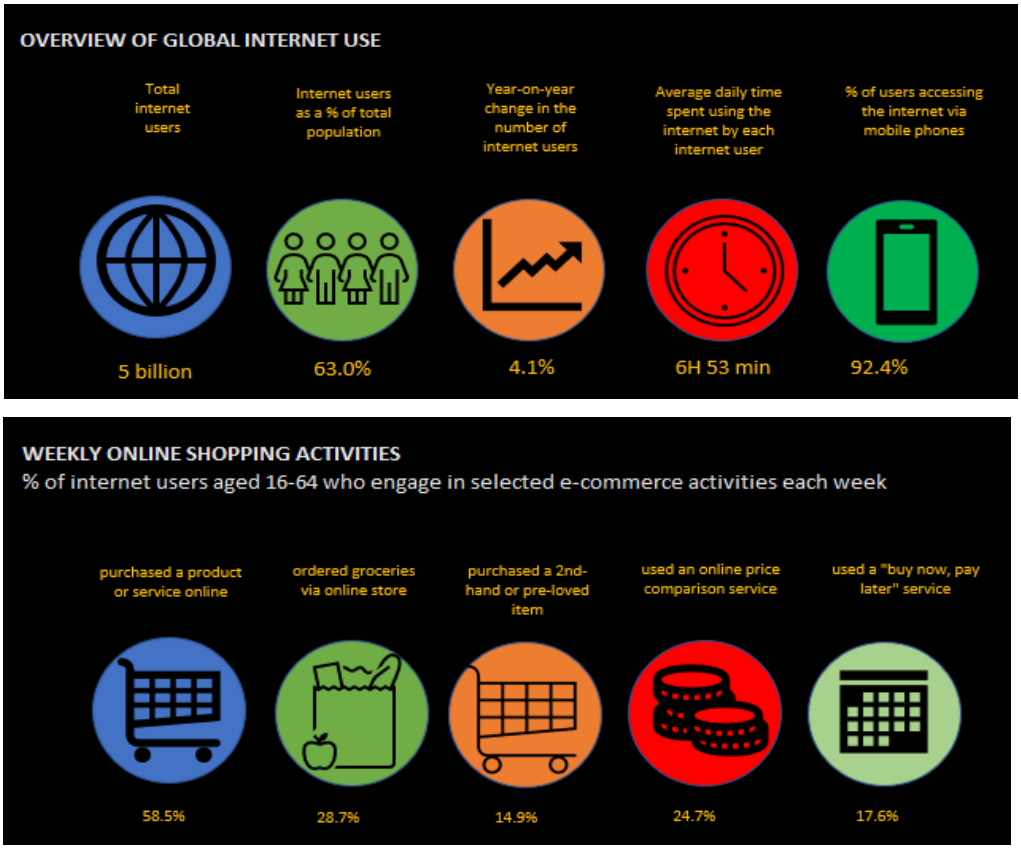
The rise of mobile technology liberates businesses and consumers from the confinement of their offices and computers to work and/or transact business. The International Telecommunication Union estimated that 63% of the world's population used the internet in 2021, a 17% increase from 2019. This rapid expansion was largely driven by rising internet penetration in developing economies, which increased from about 47% in 2019 to 57% in 2021. A large part of this increase was fueled by the advancement of internet access via mobile device technology, which accounted for 92% of internet access in 2021 (Figure 1). Further, the weekly online shopping activities show that most internet users used the web to buy a product or service.

Flourishing digital entrepreneurship has become more pervasive in economies with higher internet penetration, leading to geographical inequality implications because of the digital divides or differences in internet access across locations. Internet penetration varies greatly in developing Asia, with East Asia leading the way with 72% in 2020 and the Pacific trailing with 17% (Figure 2). As a result, there will be some disparity in how digital entrepreneurship develops across the subregions. Global initiatives and government interventions may be necessary to level the playing field on this front.

Indeed, the COVID-19 pandemic exposed the flaws in long-standing business and consumer practices. Firms realized that they could not continue doing business as usual, and that they needed to accelerate their transformation agendas. Accenture (2022) reports that, to minimize the disruptions caused by the pandemic, most companies surveyed are now accelerating their plans to upgrade the digital technologies they use and are focusing on building a digital core to allow them to simultaneously transform multiple parts of their enterprises. Similarly, youth entrepreneurs in the Asia and Pacific region are also using available digital technologies to respond to the COVID-19 pandemic and to support their path to resilience (Youth Co:Lab 2021).

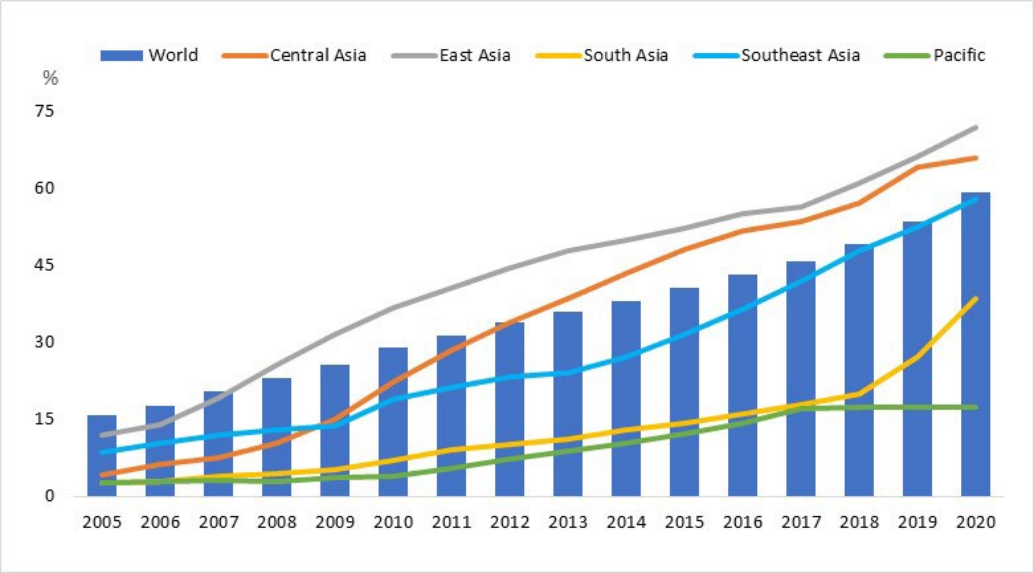
The adoption of digital technologies may benefit entrepreneurs in a variety of ways because digital tools enable firms to reduce costs, increase revenues, maximize their comparative advantage, explore new business opportunities, and adopt new business models (Nambisan, Wright, and Feldman 2019; Soluk, Kammerlander, and Darwin 2021). Also, it could assist entrepreneurs in overcoming some of the challenges caused by a lack of appropriate institutions, particularly for rural entrepreneurs who lack physical infrastructure (Amankwah-Amoah 2018; Sohns and Revilla Diez 2018; Soluk, Kammerlander, and Darwin 2021). More importantly, the digitalization of entrepreneurship can improve economic and social returns by raising entrepreneurial activity and innovation productivity (Burtch et al. 2018; Katz et al. 2014; Kenney and Zysman 2016), and by creating new work structures through redefined industrial and sectoral boundaries (Malone 2018; Sundararajan 2016).

Figure 1: Global Internet Use



Source: Kepios. 2022. *Digital 2022 April Global Statshot Report.* Digital 2022: April Global Statshot Report — DataReportal – Global Digital Insights.

Figure 2: Share of Internet Users to Total Population



Source: International Telecommunication Union. https://www.itu.int/en/ITU-D/Statistics/Pages/stat/default.aspx (accessed 18 May 2022).

Although digitalization has created new entrepreneurial opportunities and provided numerous benefits, it has also transformed the nature of the risks and uncertainties that firms and consumers face. Platform-based business models, strong multisided network effects, access to and use of large amounts of data, high start-up costs, low variable costs, and economies of scale and scope enable a small number of incumbents to maintain their strong competitive advantage and significant market share (Cremer, de Montjoye, and Schweitzer 2019; Baker Mckenzie 2021). Key players in the digital markets can use their position in one market to expand and establish their businesses in adjacent markets to the detriment of their competitors, resulting in monopolistic power that is often detrimental to healthy competition (ADB 2021). They can also be "data-opolies", which possess and control vast amounts of data, often coming from the public domain, and exclusively use them to leverage their market power. As a result, concerns about market concentration, competition, data protection, and privacy have grown, and modern competition policies will need to be adjusted and polished to account for issues discussed in the following paragraphs.

It is widely agreed that competition authorities must deal with the digital economy's rapid rate of change and innovation by considering market dynamics better and rethinking the use of

traditional tools and concepts, such as market definition, market concentration and power, and consumer harm (OECD 2016). However, how to accomplish this in light of new and complex challenges of enforcing competition law in the digital economy era remains a question.[3] In the digital world, for example, physical market boundaries are not well defined because digital markets can be two-sided or even multisided, with one side of the platform charging zero price to consumers. All of this makes it difficult for competition authorities to define relevant markets and, consequently, market dominance because measuring market power and domain would be difficult, particularly in a multisided platform setup.

It is common for digital markets to be vulnerable to "tipping" in which a winner takes most of the market, potentially reducing consumer welfare in the long run. Tipping occurs in markets with multisided platforms when there are positive network effects, users prefer single-homing 6ecause of high switching costs, services are provided for free, data collected from users over time and across space makes the platform more appealing to use, review and reputation systems are in place to build trust, and platforms offer complementary offerings (Bedre-Defolie and Nitsche 2020). Preventing such tipping in markets with multisided platforms is a new area that authorities must address.

While large amounts of data are collected and used in digital markets, regulating them is difficult. The use of algorithms to collect, analyze, and process data can be a competitive advantage that could become anti-competitive 6ecause of abuse of market dominance. For this reason, machine learning-based applications are often regarded as natural monopolies (Rider, Sileno, Gordon 2021; Narechania forthcoming). Regulators should devise a way to limit intrusive data collection and protect the rights of consumers, whose data is being exploited, without undermining companies' competitiveness.

The combination of big data and computer algorithms is also altering the competitive landscape in which businesses operate. Companies may enter into more price and trading agreements as

[3] This discussion draws from Cremer, de Montjoye, and Schweitzer 2019; WEF 2020; Gilbert 2020; Baker McKenzie 2021; Jenny 2021; and UNCTAD 2021.

they rely on algorithms to improve their pricing models, customize products and services, and predict market trends, which may lead to a cartel behavior. Another challenge is distinguishing potential cartel behavior from market operation and machine learning adaptation of market trends.

Google, Amazon, Facebook, Microsoft, and Apple have reportedly made more than 400 acquisitions in the last decade (Coscelli 2019). Although some of these mergers are small in scale and may not pose a problem on their own, the systematic acquisition of potential competitors may reduce market contestability and harm consumers in the long run.[4] Monitoring and regulating these practices to ensure efficient market operation and to prevent the formation of anti-competitive behavior by dominant firms are new challenges that must be addressed.

These are just a few of the issues that confront the digital economy, which could easily be expanded given the rapid pace of change in digital market technology and structure. Regardless, the challenge for competition authorities remains in ensuring that competition policies protect consumers without causing harm by interfering in complex businesses that are both rapidly moving and not fully understood (Shelanski 2013).

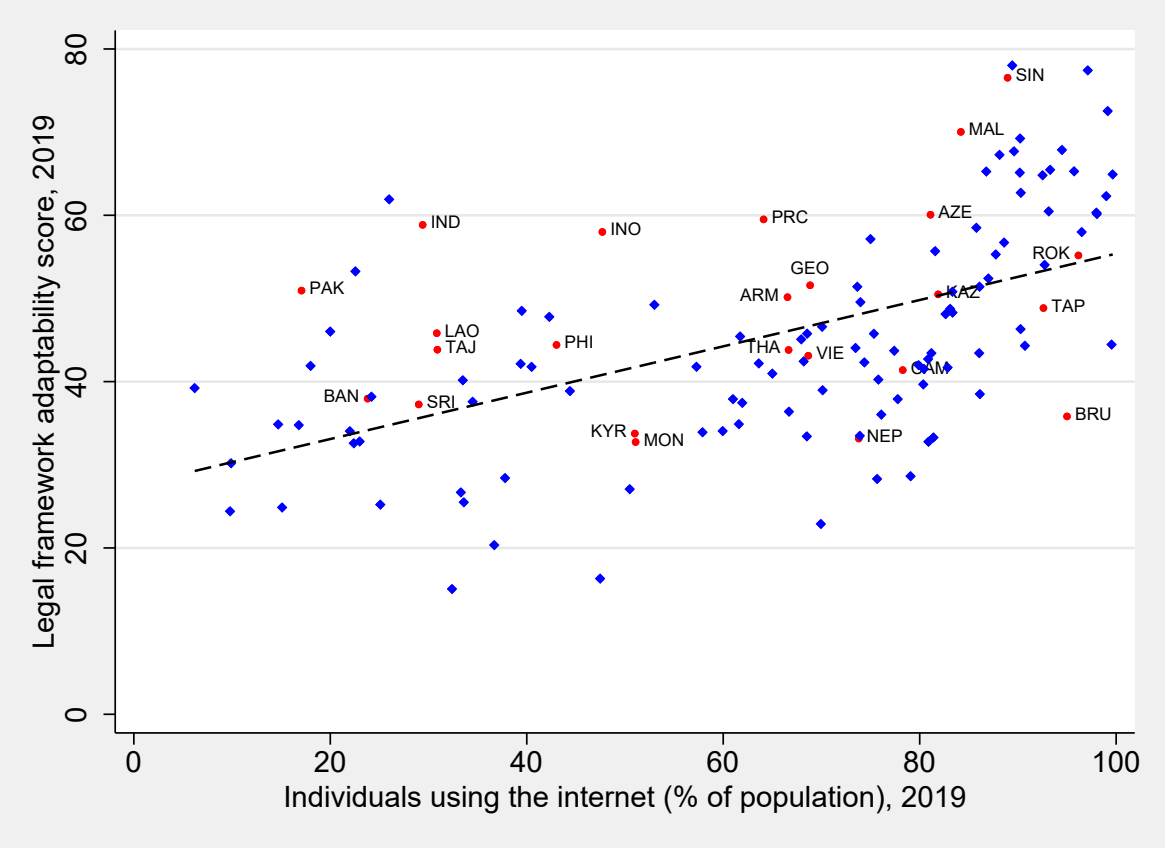
Only a few countries have made significant progress in regulating digital markets. The World Economic Forum's most recent survey on the adaptability and progress of countries' digital legal frameworks suggests that even countries with widely distributed information and communication technology (e.g., the Republic of Korea and Japan) still need to adapt their legal framework to promote more vibrant digital business environment (Figure 3). According to UNCTAD data,[5], only 34 of the 60 countries in Asia and the Pacific have data protection legislation, 6 have draft legislation, 16 have no legislation, and 4 have no available information. In terms of e-transactions, 50 countries have legislation, 3 have draft legislation, 2 have no legislation, and 5 have no data.[6]

[4] Gautier and Lamesch (2020) and Latham, Tecu, and Bagaria (2020) examined acquisitions made by big tech firms and find no evidence of killer acquisitions, i.e., acquisitions of innovative firms to prevent future competition.

[5] https://unctad.org/page/data-protection-and-privacy-legislation-worldwide.

[6] https://unctad.org/page/e-transactions-legislation-worldwide.

Figure 3: Legal Framework's Adaptability to Digital Business Models



ARM=Armenia; AZE=Azerbaijan; BAN=Bangladesh; CAM=Cambodia; GEO=Georgia; INO=Indonesia; IND=India; KAZ=Kazakhstan; KYR=Kyrgz Republic; LAO=Lao People's Democratic Republic; ROK=Republic of Korea; SRI=Sri Lanka; MAL=Malaysia; MON=Mongolia; NEP=Nepal; PAK=Pakistan; PHI=Philippines; PRC=People's Republic of China; SIN=Singapore; THA=Thailand; TAJ=Tajikistan; TAP=Taipei,China; VIE=Viet Nam.

Note: Digital legal framework refers to the response to the survey question "In your country, how fast is the legal framework of your country adapting to digital business models (e.g., e-commerce, sharing economy, fintech.)?" [1 = not fast at all; 7 = very fast]. The score is from 0 to 100 (highest). Red colored dots refer to Asian Development Bank's developing member economies.

Sources: International Telecommunication Union. https://www.itu.int/en/ITU-D/Statistics/Pages/stat/default.aspx; World Economic Forum. Global Competitiveness Report 2020. https://govdata360.worldbank.org/indicators/h6ab6fd84?country=BRA&indicator=41640&viz=bubble_chart&years=2019&indicators=944; and World Bank World Development Indicators online database (accessed 9 August 2022).

To deal with the digitalization era, it is not necessary to completely overhaul the existing competition laws and policies because some of their provisions will still be relevant. Policies should continue to emphasize encouraging competition and new firm entry (dynamic competition) rather than defining markets and limiting market power (static competition) (Audretsch, Baumol, and Burke 2001). Policymakers should be more concerned with removing barriers to entry and exit rather than ensuring the proper number of firms competing in a market.

Although mergers and acquisitions can facilitate the expansion or improvement of products and services by providing the needed capital, they can also eliminate competition. To this end, care and due diligence must be exercised in evaluating mergers and acquisitions so that they do not harm a healthy competitive environment in which innovation is likely to occur. As nicely put by Varian (2021): "…no competition authority is going to be able to determine whether the acquisition of a one-year-old, three-person company is going to confer significant competitive advantage to an incumbent. Picking winners is hard for seasoned venture capitalists and virtually impossible for those outside the industry."

Entrepreneurs in developing countries have also complained about the high costs of using global tech giants' platforms, and some developed countries have sued these tech giants although often to no avail. This observation strengthens the case for competition authorities in developing-countries to monitor these tech behemoths and prepare for the potential positive spillovers of the resolution of these legal cases (First 2021).

Further, these global digital corporations indirectly assert their rights over people's personal and public data by collecting, using, and retaining them for exclusive use, and occasionally selling them for profit. Governments should act to steward these public resources by establishing public digital data infrastructures that are secure and protective of the data rights of those who provided them, and making them available for research and policy-making purposes. As suggested by Singh (2018) "Developing countries need to understand both privacy rights and economic value/ownership aspects of data, and their interplay. Digital platforms that dominate and shape complete sectors urgently require new regulatory approaches" (p. 73).

For most developing countries, lack or absence of appropriate physical and data infrastructures, efficient financial institutions, capable human resources, and cases of unjustified government regulations that raise the cost of doing business remain greater impediments to digital entrepreneurship growth than weak competition law enforcement. Overcoming these challenges should be a higher priority. However, this is not to say that developing-country governments should disregard innovation or digital market issues when enforcing their competition policies. Although competition policies may not be the most important driver of innovation or digital market development, they remain an important tool for preventing things from going wrong (First 2021).

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