



## Speech

### Economic dynamism: A global perspective

*Hon Andrew Leigh MP\**

I acknowledge the Gadigal people, Traditional Custodians of the land on which we gather today, and pay my respects to their Elders past and present.

Thank you to the Sydney University School of Economics for hosting today.

I have fond memories of my first-year economics class in Merewether in 1991.

In the seat next to me was my friend Justin Wolfers — now a professor at the University of Michigan, and co-author of a major first-year textbook.

Last month, I gave a talk to Justin's Economics 101 class at the University of Michigan, reflecting on the power of economics in public policy.

It's a lesson our first-year Sydney University lecturer embodied.

In 1991, he was just another dashing macroeconomics lecturer, but Yanis Varoufakis would go on to enter the Hellenic Parliament, and serve as one of the most significant finance ministers in Greek history, attempting to help navigate his country's economy through the 2015 debt crisis.

He had quite the influence on his students — my parliamentary colleague Chris Bowen, who delivered the 2019 Lecture, is another student of this era.<sup>1</sup>

At that time, the School of Economics was a mere 69-year-old whippersnapper.

It's hard to believe it celebrated 100 years in July.

Congratulations to Garry Barrett for your leadership of the school, as well as your pioneering microeconomic research, especially on inequality.

### Professor Warren Hogan

I also pay tribute to the late Professor Warren Hogan and acknowledge his family, former colleagues and friends.

Professor Hogan was a 30-year veteran of this school, from 1968. He was also a significant contributor to economics in Australia and New Zealand.

As Tony Aspromourgos put it, Hogan was known for his 'formidable intellect and an equally formidable personality'.<sup>2</sup>

It was none other than Warren Hogan who pointed out an error in the paper of future Nobel Prize winner Robert Solow.

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\* Assistant Minister for Competition, Charities and Treasury. Speech delivered at the Warren Hogan Memorial Lecture, University of Sydney at the School of Economics, 14 November 2022.

1 Chris Bowen MP, 'Economics and Modern Challenges: Climate Change and Health' (Warren Hogan Memorial Lecture, University of Sydney, 20 November 2019).

2 Tony Aspromourgos, 'Warren Pat Hogan, 1929–2009' (2019) 86(273) *Economic Record* 289, 289–93.

It was Hogan who wrote the book with Ivor Pearce on the Eurodollar — a market consisting of obligations denominated in US dollars but issued by non-US banks.

Warren Hogan wrote broadly on public policy issues, covering finance, international development, immigration, airlines, aged care and more.

Hogan served as an adviser to Treasurer Philip Lynch. And as a director of Westpac — a position he held for 15 years — he stood up to Kerry Packer following a bid to take control of the bank.

Professor Hogan believed in quantitative rigour.

Yet when asked about his contribution to the discipline, he said it was the quality of the school's honours students that stood out most.<sup>3</sup>

My father Michael Leigh, a former academic in the Sydney University Department of Government, spoke warmly of his many conversations with Professor Hogan in the Merewether tearoom. My dad remarked that although they came from different disciplines, Professor Hogan had a genuine enthusiasm for helping colleagues across the social sciences.

A prolific writer and a generous colleague, it's fitting that we recognise Professor Hogan's lasting influence on the economics profession.

It's an honour to return to the University of Sydney to deliver the 11<sup>th</sup> Annual Warren Hogan Memorial Lecture.

## Economic dynamism

Today, as Warren Hogan might have put it, I want to explore beyond 'the factory gate' and provide a global perspective on economic dynamism.<sup>4</sup>

In fact, this is the third in a series of lectures where I have focused on the potential to boost dynamism and put Australia on a faster growth trajectory in decades to come.

In August, at the Australian National University — where Professor Hogan earned his PhD — I spoke about the indicators suggesting Australia has become less competitive.<sup>5</sup>

Last month, across campus at a Sydney Ideas event, I spoke about Fred Hilmer and the National Competition Policy reforms of the 1990s — the biggest competition reforms in the lifetimes of most Australians — and the powerful lessons they provide for how greater economic dynamism can boost productivity.<sup>6</sup>

Today, I want to go global. In this talk, I will draw on three examples of competition reform from around the world:

- the United States and the great trust breakup of the early 1900s;
- Germany and the breakup of industrial giant IG Farben; and
- Canada and the long road to modern competition law.

3 John Lodewijks, 'A Conversation with Warren Hogan' (2007) 83(263) *Economic Record* 446, 446–60.

4 Ibid.

5 Andrew Leigh, 'A More Dynamic Economy' (FH Gruen Lecture, Australian National University, 25 August 2022).

6 Andrew Leigh, 'A Zippier Economy: Lessons from the 1992 Hilmer Competition Reforms' (Sydney Ideas Speech, University of Sydney, 17 October 2022).

Each is a fascinating story because these competition reforms were not driven by blind ideology but by a practical desire to boost living standards and ensure that economic power is broadly distributed across the community.

I will explore the causes and consequence of each example and their relevance to the Australian economy — an economy where the business start-up rate and job switching have declined, while market concentration and markups have risen.

### The United States — The *Sherman Act*<sup>7</sup>

First, the *Sherman Anti-Trust Act* ('*Sherman Act*') in the United States. For this case study, I will draw largely on United States Senator Amy Klobuchar's excellent 2021 book, *Antitrust: Taking on Monopoly Power from the Gilded Age to the Digital Age*.<sup>8</sup>

The *Sherman Act* was passed in 1890 on the back of a wave of popular concern — particularly in the American Midwest, where anti-monopoly sentiment had always been strong — about the rise of trusts.

J D Rockefeller's Standard Oil Company epitomised the public's concerns.

Rockefeller established Standard Oil in Cleveland, Ohio around the time of the American Civil War.

This was well before the invention of the automobile, and, at the time, oil was primarily refined to produce kerosene for lighting. It was a necessity of life for American households.

Standard Oil expanded aggressively, and by 1870 it controlled nearly all the oil refineries in Cleveland.

During the following decade, it either acquired competitors or threatened to eliminate them by predatory pricing and similar practices.

By 1880, Standard Oil and associated companies supplied over 90% of all kerosene oil produced in the United States.

Then, in 1882, Rockefeller established the Standard Oil Trust. In effect, this was an oil refining, distribution and marketing cartel controlled by his dominant Standard Oil company.

Other industries soon followed, with large companies forming monopolistic trusts in sectors such as steel, tobacco, beef, sugar, flour, cotton and agricultural harvesters.

The idea of the trusts was simple: if two competitors swap shares, then their interests are aligned.

Instead of fighting to maximise company revenue, their incentives are to maximise industry revenue.

No need for secret meetings in smoke-filled rooms — with common ownership, competitors suddenly aren't so keen on stealing market share.

With common ownership on the rise in the Australian economy, it's an insight that is relevant today.<sup>9</sup>

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<sup>7</sup> *Sherman Antitrust Act 1890* (US).

<sup>8</sup> Amy Klobuchar, *Antitrust: Taking on Monopoly Power from the Gilded Age to the Digital Age* (Vintage Books, 2021).

<sup>9</sup> Andrew Leigh and Adam Triggs, 'Common Ownership of Competing Firms: Evidence from Australia' (2021) 97(318) *Economic Record* 333, 333–49.

Popular antipathy towards these 19<sup>th</sup> century trusts, particularly from farmers, was palpable.

Trusts kept consumer prices high, paid too little to farmers and workers, and made millions by pocketing the difference.

This public sentiment led to the *Sherman Act*, which passed through the United States Congress in 1890 by a vote of 242-0 in the House and 52-1 in the Senate.

The *Sherman Act* prohibited contracts, combinations or conspiracies that were in restraint of trade, as well as the monopolisation of markets.

But then not much happened. It fell to the Department of Justice to enforce the new law, and United States administrations over the next 15 years proved somewhat reluctant to litigate.

This began to change in 1901 when, following the assassination of President William McKinley, Theodore ‘Teddy’ Roosevelt became President.

Less than a year after taking office, the Department of Justice launched legal action against the Northern Railroads Trust.

The case made its way to the Supreme Court, which in 1904 found that ‘monopolies deprive the public of the advantages that flow from free competition’ and broke the Trust into independent railroads.

Teddy Roosevelt was re-elected in 1904 and, buoyed by the success of the railroads case, increased the number of antitrust cases dramatically from 1905.

And, in 1906, the Department of Justice commenced litigation against the Standard Oil Trust.

At this point, mention must be made of Ida Tarbell, a pioneering investigative journalist who, in 1904, wrote *The History of the Standard Oil Company*.<sup>10</sup>

Tarbell highlighted its abuses and misdeeds, particularly those of its owner, John D Rockefeller.

In the years from 1901–14, the United States government brought 136 lawsuits against monopolies.<sup>11</sup>

The result was a more dynamic, and vibrant economy.

Government action transformed the industrial landscape and led to a more competitive economy.

The United States reforms have three big lessons for us today.

First, change takes time. Sometimes, it isn’t enough to pass legislation; it also needs to be rigorously enforced.

Second, it’s vital to engage the public. Ida Tarbell, Teddy Roosevelt and others were passionate about getting a fair deal for consumers. They argued the case for reform in moral terms as well as economic terms.

And third, competition isn’t just about consumers; it’s also about suppliers. In the case of US antitrust reforms, farmers were a vital constituency in pressing for reform.

Alas, despite the establishment of the Federal Trade Commission in 1914, the 1920s proved to be a high-water mark in antitrust enforcement. Economic depression and war intervened, and antitrust enforcement in the United States did not take off again until after the Second World War.

10 Ida Tarbell, *The History of the Standard Oil Company* (McClure, Phillips & Co, 1904).

11 Thomas McCraw, *Prophets of Regulation* (Harvard University Press, 1984).

## Germany — The IG Farben breakup

It is from this period that my next example comes — the breakup of the German chemical conglomerate, IG Farben, in 1952.

IG Farben was formed in 1925 by a mega-merger of several large German chemical companies.

At the time, it was the world's largest chemical company and one of Germany's most innovative firms, home to three Nobel Prize winners.

Notoriously though, it became a key supporter of the Nazi Government, played a key role in the German war effort, and was instrumental in the Holocaust.

The company used slave labour from the Auschwitz concentration camp. An IG Farben subsidiary supplied the Zyklon B poison gas that was used to murder over one million people. One writer labelled IG Farben 'Hell's cartel'.<sup>12</sup>

In the aftermath of the war, the Allied Forces occupying Germany seized IG Farben's assets. Then, in 1952, the company was broken into three companies as well as a dozen smaller businesses.

Two of the larger companies, BASF and Bayer, are still in existence. The third, Hoechst, is now a subsidiary of the Sanofi pharmaceuticals group.

A recent paper by economist Felix Poege<sup>13</sup> has found that IG Farben's post-war breakup increased competition.

Innovation strongly increased measured by the quality-weighted patent count. Both IG Farben's successor companies and their competitors became more innovative.

Clearly, important historical factors were also at play, but the paper concluded that none of these factors explain the increase in innovation better than the breakup of IG Farben.

The lesson of IG Farben is that more competitors equals more innovation.

Even though the company had been quite innovative in the pre-war period, greater diversity in the post-war period led to more new ideas.

Australia's competition laws have no broad-based divestiture powers, and the Australian Government is not proposing to change that.

But the IG Farben experience is a reminder of why competition authorities today scrutinise mergers to ensure that they will not result in a substantial lessening of competition.

It is also a reminder of using post-merger analyses to inform the next pre-merger analysis. In effect, post-merger analyses help competition authorities build a better feedback loop.

What is striking about the IG Farben example is that it relates not to consumers prices, but to the impact on research and innovation.

Today, the importance of innovation cannot be overstated.

Competition encourages firms to innovate in their business processes and use their staff more effectively.

12 Diarmuid Jeffreys, *Hell's Cartel: IG Farben and the Making of Hitler's War Machine* (First Metropolitan Books, 2010).

13 Felix Poege, 'Competition and Innovation: The Breakup of IG Farben' (Research Paper No 22–24, Boston University School of Law, 2022).

In competitive industries, companies are forced to ask themselves what they need to do to win market share from their rivals.

That might lead to more research and development, the importation of good ideas from overseas, or adopting clever approaches from other industries.

Whatever its source, innovation is vital to growth in productivity and living standards for Australians.

### **Canada — The 1986 Competition Act**

Finally, let's turn to Canada.

As in the United States, popular concerns about business 'combinations' driving up prices led Canada to enact a competition law in 1889, a year before the *Sherman Act*.

The impact of the new law was limited because it relied on somewhat vaguely worded criminal offences, which were difficult to prove in court.

This state of affairs remained for decades, despite periodic attempts at reform.

The number of cases taken to court remained small.

One expert described the old Canadian law as 'pious anti-monopoly posturing that had no effect on anything'.<sup>14</sup>

Pressure for reform started to build in the 1960s and 1970s. Business remained hostile and it was not until 1986 that Canada enacted a new competition law.

The new laws retained criminal offences for egregious conduct such as price fixing, bid-rigging and predatory pricing, but the drafting of the law was clarified and improved.

Importantly, key areas such as mergers and abuse of dominance were now covered by civil provisions and a specialist competition tribunal was established.

What did this all amount to? Well, it may have taken nearly a century, but it meant the Canadian economy was finally protected by a modern competition law.

Large companies seeking to merge faced detailed scrutiny by the competition regulator.

Businesses that engaged in price-fixing or abused their dominance were more likely to find themselves in court.

Indeed, the new Competition Tribunal ruled for the Canadian Competition Bureau in all four major abuse of dominance cases in the decade or so after the reforms commenced (although one was a partial victory).

The first case under the new provisions involved Nutrasweet, at the time the world's leading supplier of artificial sweeteners for soft drinks such as Diet Coke and Diet Pepsi.

It was found to have engaged in conduct to exclude competing suppliers from the market, for example, by offering buyers substantial price discounts for displaying the Nutrasweet logo on their packaging.

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14 Michael Bliss, *Northern Enterprise: Five Centuries of Canadian Business* (McClelland and Stewart, 1987) 367.

In another important case, the Tribunal found that aggressive acquisitions of smaller competitors by the dominant firm in the commercial waste market on Vancouver Island were intended to maintain a virtual monopoly.<sup>15</sup>

It isn't surprising then that, in a 1998 study of how the new laws had fared, one commentator exclaimed that 'Canadian antitrust is back!'<sup>16</sup>

The Canadian experience highlights, perhaps even more than the United States, that change takes time and that it is vital to persist with reform efforts in the face of opposition from self-interested parties.

It also illustrates the benefits of broad legislative provisions that can be directed at a wide range of conduct impeding competition.

And, while a range of factors may have been at play, it is notable that industry concentration in Canada fell significantly in the decade following the 1986 reforms.<sup>17</sup>

Of course, the regime was not perfect and, as in many economies, significant concerns have arisen in recent years about whether it remains effective in light of digital platforms and rising market concentration.

In this year's budget, finance minister Chrystia Freeland described productivity and innovation as 'the Achilles heel' of the Canadian economy.

As an initial step, the Canadian Parliament enacted important reforms to its competition law in June this year, including increasing maximum penalties.

The Canadian Government has also flagged reforms around access to justice and considering the impact of uncompetitive markets on consumers and workers.

The Canadian Government intends to launch a thorough review of the country's Competition Act.<sup>18</sup>

## Conclusion

Competition is essential to boosting living standards and building a resilient economy.

The United States trust-busting example shows change takes time, it takes passion to engage the public and argue the case to get a fairer deal for consumers and suppliers.

The German case study shows that more competitors equals more innovation — proof that regulators around the world are right to closely scrutinise mergers.

The Canadian example shows how vital it is to persist with reform efforts in the face of self-interested opposition.

Competition is one way to build resilience — a diverse and dynamic economy is also a resilient economy.

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15 Jeffrey Church and Roger Ware, 'Abuse of Dominance under the 1986 Canadian Competition Act' (1998) 13(1/2) *Review of Industrial Organization* 85, 85–129.

16 Thomas Ross, 'Introduction: The Evolution of Competition Law in Canada' (1998) 13(1) *Review of Industrial Organization* 1, 1–23.

17 Ray Bawania and Yelena Larkin, 'Are Industries Becoming More Concentrated? The Canadian Perspective' (SSRN Paper, March 2019) <[https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3357041](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3357041)>.

18 Matthew Boswell, 'Seizing the Moment to Build a More Competitive Canada' (Speech, Canadian Bar Association Competition Law Fall Conference, 20 October 2022).

It means we are better equipped to deal with unexpected shocks and absorb, adapt, and solve the challenges of an uncertain world.

The Australian Government is committed to reforms that produce a more dynamic, competitive economy.

Recently, we passed through parliament a law that increases the maximum penalty for anti-competitive conduct — bringing Australian penalties in line with those in comparable jurisdictions.

We have also banned unfair contract terms, protecting consumers and small businesses from contract terms that allow the more powerful party to unfairly cancel the contract or unfairly change prices.

The Australian Competition and Consumer Commission's new *Digital Platform Services Inquiry* proposes major changes to the way that platforms are regulated, and we have launched a new consultation on its recommendations.

Our focus is on ensuring that Australia's competition law is fit for purpose, so the economy is fit for the challenges of the future.

Professor Hogan devoted his entire professional life to economics and improving public policy.

Since Adam Smith, our profession has promoted the virtues of open and competitive markets.

Yet over recent decades, Australian markets have become more concentrated. Markups have risen, while start-ups have fallen. The share of employees starting a new job has dropped.

As history tells us, competition reforms can change lives for the better, delivering growth with fairness.

Inspired by the boldness of past competition reformers, we are working to build a more dynamic, more productive, economy.