Acumen: International Journal of Multidisciplinary Research
ISSN: 3060-4745 IF(Impact Factor)10.41 / 2024
Volume 2, Issue 6

THE IMPACT OF COMPETITION ON ECONOMIC GROWTH

Abduvohidova Durdona Sobirjon qizi

1st year student of Gulistan State University

Tel number: +998 93 048 49 06

E-mail: durdonaabduvohidova19@gmail.com

Abstract: In this article, we discuss about the significant role of competition in economic development. It highlights the role of competition in supporting innovation, increasing economic efficiency, producing higher-quality products and services. Furthermore, it explores the challenges associated with negative consequences of excessive or unfair competition, such as predatory price wars, issues of resource inequity and potential harm to smaller businesses. On the other hand, the impact of competitive pressures from foreign markets, measured by trade freedom, is dependent on the country's technological gap. In particular, the results show that trade freedom has a stronger negative impact on growth as countries move closer to the technological frontier. Such an impact of trade freedom on growth applies to all countries, including MENA ones.

Key words: competition, innovation, productivity, consumer, technological gap, monopoly, technological frontier, trade freedom, economic growth.

Introduction: In today`s fast-paced world, the competitive environment has rapidly developed in almost all sectors, especially in the economy. In macroeconomics, competition refers to the process by which countries compete with each other for resources. In microeconomics, it refers to the process by which individual companies jockey with each other to appeal to consumers. Competition is a fundamental characteristic of market economies, playing a crucial role in determining the dynamic of supply and demand, pricing and innovation. In economics, competition refers to a process by which various sellers each try to offer better, higher quality products, lower prices and other advantages to choosing their wares over a rival`s. These forces companies to optimize their operations, ultimately benefiting consumers and fostering economic growth. However, alongside these benefits, there are also challenges, such as unfair competition, price wars, putting local businesses out of business. Competition in business is a fact of life for any industry and carries advantages and disadvantages for both sides of the transaction. While competition stimulates innovation and

generates more choices, too much competition can hurt smaller businesses. Ultimately, large companies reduce consumer options. This article explores the impact of competition, highlighting both its advantages and disadvantages.

Most traditional economists believe increased competition leads to greater benefits for all economic participants. One of the most significant advantages of technology in economy is e**fficiency and innovation.** Competition encourages businesses to find ways to improve efficiency, lower costs, and develop new products and services. Economic analysis indicates more competitive markets lead to both increased innovation and greater overall economic growth as a result. If entrepreneurs feel the need to compete with other companies, they have an incentive to provide more unique and far less rare products for their customers. Competition also leads many brands to develop new products regularly to stay relevant to consumers. At the same time, the presence of competition also creates lower prices and wide choice for consumers. The large number of competitors in the market and their efforts to attract people to sell their products open up a wide range of opportunities for consumers. When a large number of companies compete with each other, one of the easiest ways for one to gain a competitive advantage over the others is to offer lower prices. As such, greater market competition leads to greater price competition, resulting in retailers passing on lower costs to their consumers. Product differentiation due to competition among sellers often gives consumers greater decision-making power. In a competitive economic environment, customers can choose between different products from a wide variety of brands rather than buying the same identical products one week to the next from a small number of companies or even a single firm. It has an affect on job creation. Fierce competition is expected to stimulate firms willingness to invest and their demand for labor. There are two key channels through which competition may lead to job creation. First, competition exerts downward pressure on prices and thus reduces the level of rents (or price markups) charged by firms. Second, producers can invest some of their productivity gains to expand their activities in other markets, thus raising their demand for labor and creating jobs. These two mechanisms both increase demand for jobs, bringing new, more, and better jobs into the economy.

Just as there are two sides to a coin, while competition benefits consumers and promotes economic growth, it also has some negative consequences. One of the most pressing issues is the emergence of monopolies. In a monopoly situation companies drive competitors out of business. Competition in business decreases an individual companies market share and reduce the available customer base, especially if demand

is limited. A competitive market can also force lower prices to stay competitive, decreasing profit margins for each sale or service. Another challenge is the environment, which has a significant negative impact on the population. In the pursuit of lower costs and higher profit, competition could drive businesses to ignore environmental sustainability, leading to pollution and depletion of natural resources. While competition plays a crucial role in economic growth, it is important to mitigate its potential downsides through appropriate regulations, social policies and corporate responsibility initiatives.

Theoretical basis: According to standard economic theory, competition is defined as a market situation in which suppliers strive for consumers in a way that induces them to become more efficient and capable of offering a wide variety of products and services at lower prices. Economists have long been interested in analyzing the role of competition for innovation and economic growth, hence, many theoretical arguments as well as empirical studies trying to explain such relationship were presented in literature. In general, theoretical models identify two opposing effects regarding the role of competition for innovation and growth.

Conventional wisdom - dating back to Adam Smith - predicts that competition induces a better allocation of resources and spurs efficiency, which ultimately increases consumer welfare and promotes economic growth. In a competitive market a product will be offered at a price based on the competition between different suppliers, while if there is no sufficient competition, as in the case of a monopolized or cartelized economy, market participants may obtain dominant market positions that allow them to set higher prices in their favor, hindering allocative efficiency from materializing which in turn leads to lower growth rates. Moreover, the fight for and the defence of monopolies may lead to a misallocation of investments, which further results in a loss in economic efficiency[1] .

On the other hand, Schumpeter (1942) claimed that monopolies are more innovative than firms with small or even negligible market shares since they are able to offer their products at a higher price than in a competitive market, which will allow them to reap greater returns to their innovations. Consequently, Schumpeter argued that competition is detrimental to innovation and thus hampers rather than foster economic growth, as it reduces such monopoly rents that reward successful innovators and thereby discourages R&D investments, whereas monopoly market structures

[1] Romero, 2003, Voigt, 2009, Peterson, 2013.

would lead to higher rates of innovation and subsequently growth pointing to a tradeoff between static and dynamic efficiency. Schumpeter's hypothesis has been used to justify the creation of national champions (Voigt, 2009).

On the other side, Schumpeter's theory introduces a more nuanced understanding by suggesting that monopolistic firms may have an edge in innovation due to their ability to secure monopoly rents, thus incentivizing them to invest in research and development. This viewpoint highlights the potential trade-offs between static efficiency—achieved in competitive markets—and dynamic efficiency—achievable through monopoly structures. Amid the above arguments, Aghion et al. (1997) and Aghion et al. (2001) extended the Schumpeterian growth framework and managed to develop new models of competition and growth by introducing the possibility that more competition could be conducive to innovation and economic growth through the "escape-competition" effect. More precisely, competition may increase the incremental profits from innovating, and thereby encourage R&D investments aimed at "escaping competition", particularly in sectors where incumbent firms are operating at similar technological levels; i.e. "neck-and-neck" sectors, since intensive competition between firms will increase each firm’s incentive to acquire or increase its technological lead over its rivals.

Furthermore, new endogenous growth models introduce the notion of "technological distance" and underline its significant role in determining the impact of competition on innovation. They postulate that competition could have opposite effects on innovation incentives depending on whether firms were initially closer to or farther below the fringe in the corresponding industry. In particular, new endogenous growth models predict that competition should be growth-enhancing in sectors where incumbent firms are close to the technological frontier and/or compete "neck-and-neck" with each other, since in those sectors the "escape competition" effect should be the strongest. On the contrary, competition reduces innovation incentives and therefore productivity growth in industries where innovating firms are far below the frontier, as the Schumpeterian effect is more likely to dominate in these sectors (Aghion and Howitt, 2005).

In this context, Aghion and Howitt (1998) build upon Gerschenkron’s idea of "appropriate institutions" and emphasize the role of "technological distance" in the growth process; claiming that different institutions or policy designs will affect productivity growth differently depending on a country’s distance to the world technological frontier (Aghion and Howitt, 2005). The argument is based on the

following reasoning: For countries with low levels of technology i.e. far from the frontier, it is recommended that they follow an imitation-based economic policy to exploit the results of existing innovations. In terms of competition policy, this means that trade liberalization is more favorable for these countries in order to attract foreign direct investment and promote technological progress through the adoption of foreign technologies. On the contrary, business liberalization in this stage discourages investing in research and development and hence innovation, since the higher entry threat of technologically advanced firms decreases the incumbent's expected pay-off from innovating.

Dicussion of results: The main aim of this analysis is that the ongoing debate over the relationship between competition, innovation, and economic growth reflects two distinct yet compelling perspectives in economic theory. On one hand, traditional views, rooted in the works of Adam Smith, posit that competition drives efficiency, fosters resource allocation, enhances consumer welfare, and ultimately propels economic growth. This perspective foregrounds the critical importance of competitive markets in preventing monopolistic behaviors that can adversely affect pricing and investment decisions.

Competition depends mainly on barriers to entry that may prevent new firms from accessing the market. A fundamental precondition for the existence of intensive competition is that market entry is fairly easy. This should apply for both domestic and foreign entrants.

Also, based on recent empirical literature on competition and growth, this work takes into account the distance from the technological frontier as a possible determinant of economic growth, both as a single explanatory variable, and also as a factor of an interaction term with both business freedom and trade freedom indices to explore whether the effect of competition on economic growth may change depending on the level of the technological gap between the observed country and the country which is the technological leader. The leader country (technological frontier) is identified as the country with the highest labour productivity in the sample, while the technological gap is calculated as the ratio of labor productivity of the country under consideration to the labor productivity in the leader country. Accordingly, the technological gap variable ranges from 0 to 1, with lower values indicating larger gaps. Labour productivity is measured as GDP per person employed (constant 1990 PPP $), and is obtained from the World Development Indicators.

The above idea depicts regression results when standard economic variables are controlled for. This indicates that more intensive domestic competition tends to slow down the growth rate of an economy regardless of the country's technological gap. Such results assert the basic Schumpeterian argument of the tradeoff between static and dynamic efficiency; where competition discourages the incumbents' incentives to innovate and hampers economic growth by sweeping away monopoly rents that reward successful innovators. The standard control variables are all significant and have the expected signs. More precisely, we observe that more trade openness and increased investment enhances economic growth, whereas higher inflation rates and the rapid expansion of government consumption expenditures can slow down the growth of the economy.

Conclusion: In this paper, we tried to revisit the puzzling relationship between competition and economic growth, focusing on how the country's distance to the technological frontier can influence the impact of competition on growth. Within **capitalist economic systems**, the drive of enterprises is to maintain and improve their own competitiveness, this practically pertains to business sectors. The most important aspect of competition is that in order for it to continue, without leading to the permanent dominance of one side, there must be "competitive relations between equal parties."[2] However, the home improvement industry's high demand opened up many opportunities for companies committed to high-quality, affordable service. Competition between businesses or individuals to achieve competitive advantage and attract customers or resources benefits consumers and stimulates economic growth. In particular, business freedom was used to proxy 206 for domestic competition due to the entry or the activity of other firms in the market, and trade freedom was employed to proxy foreign competition through the threat of entry of foreign firms or products to domestic market.

On the other hand, as countries get closer to the technological frontier, the economic policy adopted should aim at promoting innovation in order to invent new products and production techniques or improve the quality of the existing ones. Within competition policy context, this implies that business liberalization is more beneficial for such countries, since the increased possibility of entry in the market and thus the higher potential competition from the incumbent firm incentivizes both the incumbents and the entrants to invest more in innovation, as it offers the only way to survive in the

[2] Michael Brecher. The world of protracted conflicts, May 26, 2016 - p. 11; citing Gary Goertz; Paul F. Diehl (June 1993). "Enduring Rivalries: Theoretical Constructs and Empirical Patterns". Vol. 37, No. 2 147-171 - p.

market. Whether it's direct or indirect, competition is a fact of life for almost any business. Economic competition allows the so-called "invisible hand" of the market to reward the most effective seller, rather than relying on a central committee or monopoly to plan the economy. In simple terms, this means whoever provides the best product at the lowest price is likely to receive the highest rewards, at least theoretically. Competition is not a struggle of all against all. Competition occurs where interests clash, and cooperation arises where interests are aligned. "Competition is the main condition of the market, one might say its law."

REFERENCES:

1. Competition Economics: Imperfect and Perfect Competition written by MasterClass (Featured masterclass instructor - Paul Krugman)
2. Competition and Economic Growth: An Empirical Analysis with Special Reference to MENA Countries. Marwa M. Gomaa Cairo University
3. Acemoglu, D. P. Aghion, and F. Zilibotti (2006), "Distance to Frontier, Selection, and Economic Growth", Journal of the European Economic Association, 4(1): 37–74.
4. Aghion, P., C. Harris and J. Vickers (1997), "Competition and growth with step-by-step innovation: An example", European Economic Review, Elsevier, 41(3-5): 771-782
5. **The-Effects-of-Competition-on-Jobs-and-Economic-Transformation.** **(**equitable growth, finance & institutions insight)
6. Assessing the impact of competition authorities` activities (OECD)
7. https://en.wikipedia.org/wiki/Competition_(economics)