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Abstract

This study examines how deregulation affects product market competition and thereby productivity. Productivity grows when firms ameliorate their performance, which they will be unwilling to do in the absence of competition. It obliges firms to renounce high rents and cut costs, which increases static efficiency. However, static efficiency boosts productivity only temporarily. Long-term gains are derived from dynamic efficiency, which competition promotes in two ways. First, it increases incentives to innovate, and secondly, it accelerates creative destruction. Since regulations impede the free entry of rivals, they ensure firms a quiet life. Deregulation has therefore great potential to boost productivity growth.

Deregulation impacts on productivity indirectly through three channels. First, the threat of rivals leads to internal restructuring which refers to a process where factors of production are reallocated within firms. Secondly, when rivals do enter the industry, interaction between firms intensifies. This results in innovations being created at a faster pace. Thirdly, intense interaction causes external restructuring where resources are reallocated between firms, from inefficient and shrinking to efficient and expanding firms. The two last-mentioned channels increase the dynamism of the market and have therefore a larger impact on productivity vis-à-vis internal restructuring.

This study describes the process of regulatory reform in Finland. In addition to a country-level analysis, deregulation and its consequences are examined in service station and restaurant industries, which have experienced extensive reforms. The purpose was to see whether deregulation has induced external restructuring in these sectors. This was done by examining variation in employment growth on one hand and correlation between changes in employment growth and labor productivity development on the other hand. The results give indication of external restructuring in both industries. Given that the reforms occurred simultaneously with the recession of the 1990s, the detection of restructuring attributable to deregulation would require further investigations, however.

Key words	Deregulation, competition, productivity, entry
Further information	