



ECONOMICS

THE ELEVEN NEGATIVE EFFECTS OF COMMERCIAL RESTRICTIONS

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The Socialist Government's proposed Law on Trading Hours represents a clear step backwards in terms of business freedom. It will not only be detrimental to consumers, whose freedom will be restricted when it comes to deciding when and where they wish to buy, but will also provide false protection to small businesses, because it does nothing to promote their modernization. The official figures according to Spanish Region clearly show that liberalization has not only had no detrimental effect on trade, but that the most restrictive Spanish Regions are the ones that have the fewest small businesses, create the least employment and have the least dynamic commercial fabric, whilst also presenting the highest inflationary pressures.

Official Statistics: Liberalization is Not Detrimental to Small Businesses

It is commonly argued that free trading hours are detrimental to small businesses. However, the reality, as reflected in official statistics, proves exactly the opposite.

In 1996 a policy of progressive liberalization of trading hours commenced, a policy that received new impetus in the year 2000. This policy granted the Spanish Regions a certain degree of flexibility, which enabled some regions to pursue the course of liberalization further than others. Eight years on, the statistics show that small businesses have fared better in the Spanish Regions that carried their liberalization policies the furthest compared to those that chose to maintain more severe restrictions.

It is an interesting exercise to compare the development of small businesses in the Spanish Region in which large stores open on the largest number of Bank Holidays and Sundays (Madrid, the most liberal region, where shops open on 21 Bank Holidays and Sundays a year), with the Spanish Region where they open on the fewest number of days (the Basque Country, where they do not open on any Bank Holiday or on Sundays). In this respect, we can compare these two figures, whilst also producing a comparison with the national average throughout the 1998-2002 period.

- In the Madrid Region (+ 6.0%), a larger number of trading companies was created than at a national level (+ 1.9%); the Basque Country witnessed a decrease in the number of companies set up (- 6.8%).

- In the Madrid Region, the number of trading establishments increased by 4.3%; at a national level the number of establishments increased by 0.4%, whilst the Basque Country witnessed a decrease of 8.0%.

**NUMBER OF TRADING COMPANIES
1998 - 2002**

Central Directory of Companies, INE

	RETAIL TRADE	SALE OF MOTOR VEHICLES	WHOLESALE TRADE	TOTAL
BASQUE COUNTRY	-7,9%	-3,3%	-4,9%	-6,8%
MADRID REGION	2,3%	10,2%	13,9%	6,0%
NATIONAL LEVEL	-1,0%	6,0%	7,9%	1,9%

**NUMBER OF TRADING ESTABLISHMENTS
1998 - 2002**

Central Directory of Companies, INE

	RETAIL TRADE	SALE OF MOTOR VEHICLES	WHOLESALE TRADE	TOTAL
BASQUE COUNTRY	-9,3%	-3,1%	-6,0%	-8,0%
MADRID REGION	0,0%	10,8%	14,0%	4,3%
NATIONAL LEVEL	-2,9%	6,6%	7,5%	0,4%

- In the Madrid Region, the number of employees in the retail trade increased by 37.5%, whilst in the Basque Country it only increased by 18.7%, at a slower rate than at a national level (+19.1%).
- In the Madrid Region the unemployment rate within the retail sector fell from 16.25% to 5.17%, whilst in the Basque Country it fell from 11.07% to 7.47%. In terms of the national average, the rate fell from 14.36% to 8.34%. That is to say, the Madrid Region reduced its unemployment rate within the retail sector by 11 points, the national average witnessed a decrease of 6 points and the Basque Country a decrease of only 3.5 points.

UNEMPLOYMENT RATE (%) IN THE RETAIL TRADE. 1998-2003

	BASQUE COUNTRY	MADRID REGION	NATIONAL AVERAGE
1998	11,07	16,25	14,36
2003	7,47	5,17	8,34

SOURCE: INE.

The retail trade index published by the Spanish National Statistics Institute (INE) indicates the following:

- Retail sales continued to grow in spite of the increase in the number of Bank Holidays and Sundays on which large stores opened.
- Among the Spanish Regions that have large urban centres, the least restrictive presented retail sales increases that were substantially higher than those recorded in the regions that were most restrictive. In the Madrid Region, retail sales grew by 2.5 percentage points more per year than in Catalonia (which only permits stores to open on 12 Bank Holidays and Sundays a year).

“The IMF believes that 10% of the Spanish economy’s current unemployment rate is due to free trade restrictions and that removal of these barriers would generate some 216,000 additional jobs”

With regard to the overall development of employment and unemployment, the Madrid Region witnessed increases in employment and decreases in unemployment that were clearly higher than the national average, especially in terms of female unemployment. There is general agreement that trade restrictions account for a considerable part of the unemployment rate. The International Monetary Fund believes that 10% of the Spanish economy’s current unemployment rate is due to free trade restrictions and that removal of these barriers would generate some 216,000 additional jobs.

In terms of price inflation, the Madrid Region once again presents better results. For example, the price trend in Catalonia is clearly more inflationary than in the Madrid Region. These figures have been ratified by the reports produced by the International Monetary Fund, which highlight the fact that trade restrictions have an inflationary effect (they add a tenth to the inflation rate) and that the most restrictive Spanish Regions present the highest inflation rates.

The Real Reason Behind the New Free Trade Restrictions

In spite of the fact that the new Spanish Socialist Government has this information at its disposal, it has just sent a draft law to Parliament which restricts the authorities’ freedom when it comes to establishing trading times ... The question we must ask is why exactly the Government would wish to take a step in this direction when it has been proven to be mistaken.

For some time, the theory of collective election has been able to explain why liberalizing the markets is politically costly. **Reforming productive sectors that are protected from competition has a political cost.** The benefits generated by interest groups, which take the form of pressure groups, are concentrated on a much lower number of beneficiaries than those who benefit from liberalizing policies. The selective influence exercised by these groups is intense and this translates into political temptations to cede to sectorial pressures and win the votes of these groups.

This state of affairs is detrimental to society as a whole (the famous “welfare triangle of loss” which is described in economics manuals, plus other negative collateral effects), but this loss is diluted among a wide-ranging group: that of consumers. These sectorial protection policies, which are harmful in themselves, when applied to the entire economy, result in a fossilized system of production, a stagnant economy and lower levels of employment. In the end everyone loses. We all lose.

“These sectorial protection policies, when applied to the entire economy, result in a fossilized system of production, a stagnant economy and lower levels of employment”

The restrictions on freedom of trade proposed by the Socialist Government are an example of this approach. This law is clearly based on an electoral motivation, rather than on a desire to promote a programme of national economic development. Small businesses are made the subject of this electoral adulation by offering them this alleged protection.

This false protection is based on introducing a more restrictive approach to retail trade policy in the Spanish Regions, consisting of the following measures:

- A reduction in the number of Bank Holidays a year (from 12 to 8 days) on which large stores are authorized to open.
- A reduction in the number of hours per week (from 90 to 72 hours) that this kind of store can remain open.

We should point out the fact that the legal regulation of these trading hours as a “minimum” benchmark is only a formal practice. **In reality, political pressure means that these minimum benchmarks end up becoming maximum levels in the Spanish Regions,** except in cases where the Regional Government in question exercises strong leadership and deep-seated convictions in defending the general interest.

Those affected most directly, of course, are consumers, who find their rights are curtailed. That is to say, we are all victims of Socialist reform.

Small businesses are also deceived, for two reasons:

- The Law does not offer any measure with which small businesses can modernize or reduce their fiscal burden. In short, there is no provision to enhance their competitiveness.
- Statistical figures clearly demonstrate that restricting trading hours offers no protection to small businesses. **The Spanish Regions with the fewest trading restrictions** – especially those that have large populations centres – **are, precisely, the ones that have created the largest number of small businesses and the greatest number of jobs** in small enterprises.

There are very good reasons that underlie this reality, as we shall see below. The commercial distribution segments that have witnessed by far the strongest

growth in recent years are made up of medium-sized stores (supermarkets) and, behind them, small businesses. Let us consider, once again, the example of the Madrid Region:

**TRADE SECTOR IN THE MADRID REGION
ANNUAL AVERAGE GROWTH (%)**

DEVELOPMENT (1995-2002) ACCORDING TO TYPE OF ESTABLISHMENT	NominalGAV	Real GAV	Jobs
Hypermarkets (over 2,500 m2)	9,15	6,32	1,49
Supermarkets (between 2,499 and 400 m2)	14,97	11,99	9,69
Super-service stores (between 399 and 120 m2)	10,86	7,98	5,83
Self-service stores (between 119 and 40 m2)	11,03	8,15	6,06
Other non-specialized establishments (mainly food)	10,35	7,49	3,95
Department stores	5,49	2,75	2,61
Food, drink and tobacco retail trade in specialized stores	10,37	7,51	4,03
Clothing retail establishments	10,77	7,89	4,36
Retail trade in footwear and leather items	9,29	6,46	3,02
Furniture, lighting and other household furnishing retail establishments	17,77	14,71	7,14

SOURCE: Statistics Institute. Madrid Region.

If we were to highlight the segments that compete with small businesses, especially in large urban areas, the first and main competitor would consist of medium-sized stores (supermarkets) and convenience stores. It is important to remember that a large number of supermarkets, who compete very directly with small businesses, do not open on Bank Holidays, which means that the legal reform the Government aims to introduce will not “protect” small businesses from their main competing segment.

Another competitor consists of small convenience stores, which directly compete with small businesses in terms of trading hours, given that they do open on Bank Holidays (for example, stores managed by Asian traders). However, the legal reform will have no effect within this segment.

Fallacious Arguments for Justifying Restrictions on Trading Hours

The obvious electoral basis of the Socialist initiative is founded on arguments that are worth examining:

- It is stated that users only accept greater freedom in terms of trading hours if the service provided does not entail any extra cost.
- It is stated that longer trading hours necessarily involve higher labour costs and that these costs are passed on in the form of higher prices. Therefore, it is claimed that when consumers go to a convenience store they know they are going to pay a higher price so that the shop can recover its service costs.
- It is stated that consumers do not seem to be demanding longer trading times than those that currently exist.
- It is pointed out that other European countries (despite important exceptions, such as Ireland and Sweden) have not introduced total freedom when it comes to trading times.
- It is questioned whether the Spanish Regions with the strongest trade liberalization policies have actually created more employment.

- It is argued that it is essential to take into account the working conditions and the employees' ability to reconcile their jobs and their family life.

“The restriction of free trade and of trading hours are measures of clear Socialist inspiration: little respect for economic freedom and individual decision-making regarding when and where to buy”

In short, it is argued that restricting trading hours is for the good of the consumers and companies, whose freedom to exercise their activities is limited. The paternalism of this approach is only too evident.

Although it may seem obvious, we should begin by reminding ourselves that trade is, by definition, a service. Its value-added dimension consists of placing a series of goods at consumers' disposal featuring a series of conditions based on quality, price, place and time. As part of the service, time is just as important as the other aspects. For the several million individuals who do their shopping on Bank Holidays today, this possibility is a very important element. Every company is free to offer its services, or not, at the times that best suit its business interests. However, **to co-actively restrict free trade and force the public to buy at times or in establishments other than those of their own choosing**, as the Socialist Government proposes, **entails a direct reduction in their well-being**, obliging them to buy at places that are most inconvenient and, furthermore, at higher prices. These measures are of clear Socialist inspiration: little respect for economic freedom and individual decision-making regarding when and where to buy.

An **essential failing in this model is that it does not take into account the fact that different shopping times or days of purchase may be of different value to consumers**. The opportunity cost of a purchasing time during the working week can be high (workers may have to stop working for an hour, output decreases, as does income for that hour). A purchasing time on a Sunday may not, on the contrary, have any opportunity cost at all (incorporating as it does an element of enjoyment). In more technical language, the “shadow price” corresponding to the two times is very different.

Given that it affects income and the supply of employment, demand is not fixed, which contradicts all the conclusions of the Socialist model. It is obvious that more extensive opening hours will entail increases in activity levels, associated supply of employment, output and income, which will also lead to an increase in demand. Higher demand and high fixed costs will entail lower average costs and lower prices. Furthermore, all these effects on the supply of employment will be especially significant in the case of the large urban centres, featuring greater difficulties when it comes to reconciling working hours and family life.

It is stated that more extensive trading hours will necessarily entail higher labour costs. However, this ignores any possibility of making the working day more flexible. **A more flexible employment framework and trading times more carefully adapted to demand would very probably lead to lower labour costs, not higher**. Furthermore, if it is true that shorter trading times lead to lower costs and lower prices, why not open only three days a week, or two, or one?

More extensive trading hours, with normal marginal costs, means greater use of fixed capacity, which reduces average unit cost. In a competitive market, this translates into lower prices. This is basic economic theory. In this respect, **restricting trading times:**

- **Will lead to price increases** for basic products.
- **Constitutes a regressive measure** which mainly affects the middle and working classes, whose purchasing power is eroded.

● **Is detrimental to families and especially to those in which both spouses work**, which certainly does not improve the main challenge facing our labour market: that of increasing the working population and levels of employment.

“76% of consumers are in favour of full freedom in terms of trading hours. This contradicts the Government’s thesis”

Even if it were true – and we can see that it is not – that longer trading hours necessarily lead to higher costs, the argument that users only accept greater freedom in terms of trading hours if the service provided does not entail any cost increase, is not true:

- The enormous expansion of convenience stores is an incontestable reality: greater freedom in terms of trading times, featuring higher prices and many consumers who are prepared to pay a higher price. The thesis is refuted.
- Specialization means that there will be some establishments that open on Bank Holidays and others that do not. Consumers will decide where they wish to buy and whether they are prepared to pay more in order to enjoy extended hours. In fact, this is exactly what is happening in the various trade sub-sectors. In short, **why not allow shops to specialize and consumers to decide freely?**

According to the latest surveys carried out by the Consumers and Users Organization (OCU), 76% of consumers are in favour of full freedom in terms of trading hours. This contradicts the Government’s thesis. Something consumers are certainly not clamouring for is reduced trading times, which is the direction this Law is taking us in.

The existence of fixed capacity installations (premises, physical establishments) provides an incentive to use this capacity to the maximum. The restriction of trading hours thus reduces the use of productive capacity and, therefore, productivity. However, was not raising productivity one of the Government’s main objectives?

Questioning the fact that **the Spanish Regions with the highest levels of trade liberalization are the ones that have created the most employment** shows, quite simply, a refusal to acknowledge the official statistics. The comparative figures between, for example, the Regions of Madrid, Catalonia and the Basque Country, all similar regions in terms of their economic and social structure, speak for themselves, as we have already observed.

The argument based on reconciling family life and employment has no grounds whatsoever:

- **Many more workers are penalized in terms of reconciling family life and employment due to the reduction in trading hours** (consumers that currently buy at large stores on Bank Holidays) than those who benefit from this restrictive measure (employees who work at large stores on Bank Holidays).
- There are an increasing number of households in which both spouses work and an increasing number of single-parent homes. These households are directly affected by the reduction in trading hours.
- The Government does not seem to believe it is worth considering making the working day more flexible in order to reconcile employment and family life, something that is perfectly feasible and, in fact, is already practiced by many companies within the trade sector.
- Neither does it seem to believe it is worth considering the possibility of creating new flexible contracts which would enable, for example, young people to combine their studies with a job in the trade sector on certain Bank Holidays.

- **The reduction in trading hours could lead to lower sales and, as a result, workers being laid off.** Those most seriously threatened are employees at large stores. **Unemployment is an original way of reconciling family life and employment.**

“Socialist economic policy, which fails to promote modernizing structural reforms and entails greater expenditure and a higher deficit, will end up reducing growth and directly affecting small businesses and employment”

The most rigorous academic studies on the small business sector in Spain (for example, those carried out by Casares relating to the period 1976-1997) reveal that sales and employment within this sector are mainly determined by the development of associated private consumption. Socialist economic policy, which fails to promote any modernizing structural reforms and entails greater public expenditure and a higher budget deficit, will end up reducing economic growth and directly affecting small businesses and employment, especially female employment (49% of jobs in small businesses are carried out by women, compared to 37% female employment throughout the economy as a whole).

Finally, we might pose the following question. If the Government is so convinced that its arguments are valid when it comes to a service sector such as that of trade, should it not apply these same restrictions to other sectors that provide services on Bank Holidays, such as the entertainment sector? Why not apply it to cinemas, for example? No cinemas should open on Sundays. Cinema-goers would supposedly benefit from lower prices and the employees from improved working conditions. What is the problem then? Of course, Socialist “theses” always prove to be inconsistent.

Conclusions. The Eleven Negative Effects of Reducing Trading Hours

The Socialist Government’s Draft Law on Trading Hours is a regrettable step backwards in terms of domestic trade policy and will have eleven negative effects:

- 1. It will be detrimental to all consumers**, who will be forced to shop where they do not wish to buy, when they do not wish to buy and at higher prices.
- 2. It will reduce the overall job supply, with the consequent effect of contracting economic activity.**
- 3. It will be more difficult for the public as a whole to reconcile family life and employment.**
- 4. It will halt the growing rate of economic activity.**
- 5. It will reduce the growth of net employment within the trade sector, especially in terms of female employment. This reduction may result in a net loss of employment.**
- 6. It will reduce the growing rate of productivity within the trade sector and, the refore, that of the economy as a whole.**
- 7. It will provide an obstacle to new investment.**
- 8. It will halt economic growth and job creation in the Spanish Regions that are most restrictive.**
- 9. Lower economic growth will have a direct effect on sales and employment in small businesses.**
- 10. It will have a negative effect on price developments.**
- 11. Due to its regressive nature, it will have negative effects in terms of income distribution.**

In addition to the above, **the Law entails five other negative considerations:**

1. It fails to offer real protection to small businesses, because it does not contain any measures that encourage and promote modernization.
2. It does not contain any measure to reduce taxes within the small business sector.
3. It does not contain any measure to reduce taxes on profits made by small businesses (for example, regarding income tax for self-employed workers).
4. It represents a policy in which the Government “hides its head in the sand” in relation to the “second licenses” for the Spanish Regions. If this matter is not resolved, the European Union will impose penalties on Spain.
5. Neither does it resolve the problems entailed by policies that impose “other barriers” to free trade practiced by the Spanish Regions.

In short, **the Law on Trading Hours will not protect those it is intended to protect, whilst also being detrimental to all consumers.**

“The modernization of small businesses should be promoted through changes in labour regulations, improved forms of direct aid and tax reductions”

How to Really Help Small Businesses

A policy of supporting modernizing trends in small businesses must be combined with changes in labour regulation, incentives and tax reductions:

- Improving the regulations on part-time employment.
- Establishing generally more flexible labour regulations for self-employed workers and small and medium-sized companies.
- Improving regulations concerning flexible contracts that, for example, will enable young people to combine their studies with jobs on Bank Holidays.
- Additional forms of direct support. An example: the budget of the Ministry of Industry, Tourism and Trade to modernize trade throughout Spain comes to nearly 3 million euros. That of the Madrid Region comes to 6 million euros.
- Reducing taxes that relate to small business activities. When the Partido Popular was in government it took various steps in the right direction, such as eliminating, for example, the Tax on Economic Activities (IAE) which was previously established by the Socialists, PSOE. These tax reduction measures should be continued.
- Reducing taxes on profits earned through small business activities. The Partido Popular Government progressively reduced the income tax levels (IRPF) which had been raised by the Socialist Government during its period in government. This is another policy the Government should continue to pursue.