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The Benefit of Competition Policy for Consumers

Contribution

by

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Decrypting Competition policy for achieving consumer benefits in
developing countries

Regulation is a complex balancing act between advancing the interest of consumers, competitors and investors while promoting a wider ‘public interest’ agenda.

-David Parker

I. Background – a wider understanding of competition distortions

1.1 Competition is a process of economic rivalry between market players to attract customers. Such market players can be multinational companies, domestic firms, wholesalers or retailers of various goods and services. The World Bank has defined Competition as a situation in a market wherein firms or sellers independently strive for the buyer’s patronage in order to achieve a particular business objective e.g., profits, sales and/or market share.

1.2 All forms of economic transactions are usually done with a motive of earning a profit. However, at times when the tendency to make profits is stretched too far by market players, it can result in market malpractices. One such malpractice is anti-competitive practices, when a player resorts to unfair means for undertaking its operations. One common practice is when competitors enter into covert and overt agreements among themselves to raise prices, allocate markets among them or restrict output (see Box 1). Such practices stifle the possibility of consumers to obtain quality goods or services at low cost – which is an expected outcome of well-functioning markets.

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1.3 In order to protect consumers from such practices, many countries have developed competition laws implemented by a national competition agency. Furthermore, many regional authorities (like EAC, COMESA, SADC, ECOWAS, ASEAN, etc.) have also realised the importance of promoting competition laws as part of evolving well-functioning regional markets. In addition to curbing anti-competitive practices, a competition law is designed to promote the process of competition in markets, so that rivals can compete on merit and do not indulge in market malpractices.

1.4 Apart from practices of market players, government policies and praxis sometime distort the process of competition in markets (Box 2). While competition agencies are empowered and equipped to take actions against anti-competitive practices by market players, in most

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**Box 1: Geographical market allocation in Cable TV services**

A practice that was common in the town of Jaipur (India) was when cable TV service providers allocated the whole of the town among themselves – so that there was possibility of competition among them. The system was such that it did not create any incentive for the players to improve their services, which was ordinary. Consumers could not change the service providers, as one operator was not permitted to enter the other’s operating area. After a long legal battle and campaign by CUTS and others, this system was quashed.


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**Box 2: What is competition distortion?**

Competition distortion denotes a situation in which companies do not compete under equal conditions. Some of them are placed in an advantageous position as a result of government policies, regulations or praxis. Inappropriate regulations and policies by national, state and local governments can cause such market failures. It promotes inefficiency in the market, as underperforming firms are not compelled to improve their performance. Such sectors are often characterised by a sluggish growth rate.

If countries eliminated such policies that distort competition in markets, they could grow rapidly. An example is the Indian automotive sector, which is one of the fast-growing sector in the country. This was a result of the government decision to abandon many of the limits on foreign investment in the automotive industry over the last decade or so. Quite remarkably, India is also exporting automobiles overseas. This is something that was unthinkable earlier.

Sometimes, sectoral policies affect competition. The Sugar Act of Kenya prevent the establishment of a sugar mill within the radius of 40Kms of an existing one. This prevented establishment of sugar mills in the country, and sugar farmers had to spend considerable time and money on transporting their stock. The Government of Kenya realised this over time, and recently issued license for the establishment of a new Sugar Mill (Butali Sugar) in 2012, which brought smiles to many farmers in the Kakamega area of Western Kenya.

*Source:*

countries these agencies can only advise governments about these policies and their effects. In order to evolve well-functioning markets, it is necessary to identify such competition distorting policies and highlight how they affect consumers and/or producers. In recent times therefore, discussions on the need for promoting competition has been taken beyond the national competition agencies, to the level of policymaking as well. This is why there has been renewed interest on the subject of competition policy. Competition policy is essentially a commitment by government to promote competition in all sectors of the economy. This entails a thorough process of scanning of economic elements of key policies and legislations in order to assess their impact on competition in the market.

II. Need for Competition Policy – a holistic approach

2.1 A free market is based on the principle of survival of the fittest, compelling firms to make continuous effort to enhance efficiency and offer a wide range of choice to their customers. However, there is a need for regulating the process of competition in such a market economy – and hence the role of the competition enforcement agency becomes extremely crucial and relevant. Competition forces firms for optimal allocation and utilisation of available resources. Thus, competition is a necessary tool to promote efficiency and innovation which finally leads to greater productivity, economic growth and consumer welfare.

2.2 However, competition cannot be achieved automatically and needs to be nurtured, especially in countries that have only recently started promoting private participation in their economies. Given the background of considerable government intervention in these markets, sectoral policies were traditionally developed such that it favoured the incumbent government player (state owned enterprise). With the changing economic order and the nature of these markets, there is a need to review these policies and refine them so that they are aligned with the government’s strategy to promote private sector development.

2.3 This sets the rationale for countries to seriously consider infusing principles of competition policy (Box 3) in key markets of their economies. This might not be done overnight and should not be attempted in haste, but needs to be planned in a systematic manner. Therefore, there is a need for economic planners and policymakers to appreciate benefits of competitive markets, and take lead in the process of competition reforms. Needless to say that due to political-economy issues, some of these changes will need considerable push from the ground, to fructify. Hence the involvement of civil society, academia and media in such processes is critical.

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5 Such policies/legislations can range from ‘provision of exclusive rights’ to ‘imposing entry barriers’ in markets, etc.
2.4 In the practitioner’s parlance, competition law is considered to be a subset of competition policy. Competition policy has implications on the entire gamut of government policies that determine competition in a specific market (Fig 1). An appropriate competition policy comprises:

- Micro economic policies that enhance competition in local and national markets
- Competition law designed to prevent anti-competitive business practices
- Well-designed sectoral regulatory framework to promote competition in markets

**Box 3: Principles of Competition Policy Reforms**

In 1993, in his report to the Government of Australia on Competition Policy, Prof Frederic Hilmer identified the following six areas for undertaking competition policy reforms:

- extension of the reach of the Trade Practices Act 1974 to unincorporated businesses and state and territory government businesses;
- extension of prices surveillance to state and territory businesses to deal with circumstances where other competition policy reforms had proven inadequate;
- application of competitive neutrality principles so government businesses do not enjoy a competitive advantage over their private sector competitors simply as a result of public sector ownership;
- restructuring of public sector monopoly businesses;
- review of all legislation that restricts competition;
- provision for third party access to nationally significant infrastructure.


**Fig 1: Competition Policy and Other Policies interface**

Source: CUTFS, 2008
2.5 On the one hand competition law is developed to regulate market failures which results in overall economic welfare, which includes consumer welfare. While on the other, competitive market resulting from an effective competition policy makes decision-makers more conscious about costs and benefits of a policy intervention. This consciousness brings about efficient decision making as well. Also in regulated sectors, a well-designed regulatory framework (and institution) is able to facilitate fair competition.

III. Expectations from effective competition (policy and practice)?

3.1 Some of the significant bearings of pro-competitive policies and practices are enumerated below:

- **Low Prices**
  The immediate advantage of a competitive market is low prices of the goods sold. A competitive market provides the consumers a wider spectrum of price choices and the consumers then can make choice so as to buy products or services at a price band that they are comfortable with.

- **Better Quality**
  Presence of a number of competitors can force companies to invest more in research and development (R&D) of the product or service in question. Enhancement of quality of the product or service provides consumers a choice to procure an enhanced quality product at a comparatively lower price.

- **More Choices**
  Owing to the fact that competition ushers in lower prices coupled with better quality of goods, allows the consumers to have several choices which in turn provides the consumers the right to exercise choices for purchasing a product.

- **Innovation**
  Large number of competitors in a market compels the manufacturers and producers of goods and services to constantly innovate their product to keep themselves ahead of their rivals.

- **New Entrants**
  One of the aims of a functional competition policy is to remove entry barriers in a market. This allows new entrants into the market; providing consumers the right to exercise her/his choice. Such a situation characterised by ease of entry in the market also helps the overall economy.

- **Better Services**
  Competitors often provide certain additional services that allow them to either acquire or retain customers. Competition allows the competitors to provide better and timely services to consumers.

- **Check on Concentration of Economic Power**
Concentration of economic power occur when the market is dominated by a single or a handful of firms. Competition reduces such concentration of economic powers and enhances economic democracy and transparency in an economy.

IV. Lack of competition (policy and practice) and consumer welfare

4.1 An expected outcome of a functional competition law is a better deal for consumers, in terms of access, quality, choice and price of goods and services in the market. Apart from the fact that a sound competition law provides greater bargaining power for the consumer, it also helps her/him get lower prices for goods and services, without compromising quality. Further, the consumer enjoys a wide spectrum of products from various suppliers, since the barriers to enter the market for these suppliers are reduced considerably or completely obliterated.

4.2 However, a competition law (as witnessed in many developing countries) does not have the jurisdiction in acting against government policies that lead to anti-competitive outcomes in the market (or even lead to opportunity for anti-competitive practices). It can, at the most, advise the government (only when such advice is sought) on the effects of these policies. It is therefore critical for senior government officials, policymakers, practitioners, etc. to be aware of the impact that sectoral policies can have on competition in the market. This would help engage them in discussions/deliberations when such policies are found to affect consumers and/or producers adversely. Cuts has initiated a project (referred to as the CREW project) which aims to examine policies/legislations/statutes/programmes to assess how they influence competition in certain key sectors and the resulting benefits for consumers and producers.

4.3 In the following paras an illustration of the impact of competition distortions (in policy and practice) on consumers has been presented. It is segregated into two sub-sections (i) Competition distortions and consumers and (ii) Anti-competitive practices and consumers.

4.3.1 Competition Distortions and Consumers

**Trade policy**

Trade policies around the world have witnessed an increasing trend in relaxation of quantitative restrictions and reduction of tariffs. On one hand the trade barriers are reduced to facilitate trade between countries. While on the other such an increase in trade and economic activity resulting from an ‘open door’, liberalised regime is often accompanied with greater opportunities for anti-competitive conduct, as the size of the market increases.

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6 Competition Reforms for Enhancing Social and Economic Welfare in Developing Countries, referred to as CREW project (www.cuts-cclie.org/CREW)
An interesting feature of trade is ‘inverted duty structure’. This refers to a situation when the duty on a finished product is lower than that on raw materials and immediate products. This is a distortion when the higher duty on the raw materials results in high production costs than the selling price of the imported finished products and hurt domestic manufacturers, who rely on the raw materials for production.

Another aspect is that of the trade remedial measures. The World Trade Organisation (WTO) agreements prescribe remedial measures such as anti-dumping and safeguards which are often seen as protectionist measures and used to boost the domestic industries.

In some countries, certain laws (Exclusive Agents Law in Lebanon)\(^7\) impede competition as it provides exclusive rights to one or two market players to import and distribute goods in the country. The argument is that it would help maintain the quality of such goods coming into the country.

*Illustrations*

A petition seeking anti-dumping duty on polypropylene imports from Oman, Saudi Arabia and Singapore was filed by the Reliance Industries Limited (RIL) and supported by another domestic producer Haldia Petrochemical Corporation Limited (HPCL). Resultantly, in November 2010, the Finance Ministry announced the imposition of anti-dumping duty on polypropylene imports from Oman, Saudi Arabia and Singapore for a period of 5 years starting July 30\(^{th}\), 2009, the date of imposition of provisional anti-dumping duty. Such a petition needed further scrutiny since it was forwarded by domestic oligopolists who jointly controlled the market and concerted to create entry barriers for the new entrants.

In the Philippines, rice importation can only be done by the National Food Authority (NFA). In spite of the fact that country is unable to meet its domestic demand for rice, it was able to argue for a quantitative restriction (QR) on the importation of rice at the WTO (which is currently under consideration for this QR to be retained till 2017). The impact of this QR and the NFA monopoly is that domestic rice continues to be sold at a premium, when imports can easily help reduce the cost of rice for the consumers. A strong political-economy factor seems to be at play, which affects the consumers.

*Procurement Policy*

There are many procurement policies that are biased towards a certain firm or entity over the others. This distorts competition neutrality (between the public and private market players) either by providing a preference clause, riders or conditionalities or

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\(^7\) CUTS (2012), ‘Understanding the state of domestic competition and consumer policies in select MENA countries’, Jaipur, India
produce anti-competitive outcomes in a manner in which they might be implemented.

**Illustration**

In the instance of Indian Railways procurement of concrete sleepers, the extent of malice was gauged by the Parliamentary Standing Committee on Railways (2004). The Committee observed that the procurement of concrete sleepers had become a sensitive issue owing to the fact that many unscrupulous manufacturers had formed a cartel to secure orders by unfair means or interfered with the procedures in such a manner that they barred the entry of any new entrant into the market. The committee also noticed that there exists a regional imbalance in the setting up of sleeper manufacturing units. In procuring 16 million broad gauge sleepers the Railways awarded contracts to the existing 71 firms and ignored the new 24 firms in entirety.

**Financial Policy**

Certain economic decisions taken by the government or agencies lead to distortions, which not just hurt consumers but also the economy as a whole.

**Illustrations**

In August 2012, Securities and Exchange Board of India (SEBI) - the capital market regulator announced its decision to park its surplus funds in fixed deposits of PSU banks, even if the returns offered by them were lower than that of private banks by up to 10 basis points. The investment policy of SEBI is guided by the sole criteria of ‘highest returns’. However, the above decision was backed by the consideration to derive ‘high returns’ as well as ‘safety of funds’. Safety is an important criterion but to say that private banks do not offer the same levels of security is incorrect. If that were so, what about the investors who bank with private banks?

Government ‘subsidy’ is often considered an issue of contention, from a competition perspective. It entails a huge financial outlay (backed by a legislative instrument) for the government with the main aim to help citizens in a country. An example follows how these subsidies (and the amount spent by the Government) had little impact on ordinary Zambians. In 2011 the Zambian government introduced a subsidy measure to provide maize at subsidised rate to Millers, who were then expected to pass on the price reduction to the consumers leading to reduced price of maize-meal. However, the Millers acted in concert and kept the price of maize meal at the retail end, high. So, a policy (and considerable revenue expenditure in terms of subsidies) aimed to ultimately help consumers ended up being non-effective. The Government realised this in 2013 and knocked off the subsidy for the Millers. This seems to have created a ‘shake-up’ in the system and some Millers are now buying maize straight from the farmers.
Industrial Policy

An industrial policy primarily aids to provide guidelines for the effective coordination between the various sectors of the economy. The premises on which an industrial policy is formulated are: sustainable productivity, enhance employment, optimum utilisation of human capital, attain international competitiveness, etc. Despite the positive intentions behind the policy at times they lead to creating anti-competitive outcomes as illustrated below.

Illustration

One significant example of such policy distortion is the case of Fleet Equity Requirements for Domestic Passenger Air Services. According to India’s Civil Aviation Requirement (CAR) Section 3 Part I and III, a scheduled service operator using aircraft with a take-off mass of 40,000 kg or more must purchase or lease a minimum of five aircraft with start-up equity requirement of Rs 500 million. Also as an airline’s fleet increases up to five planes, equity requirement grows by Rs 200 million. The aircraft take-off mass less than 40,000 kg, the minimum start-up fleet is five aircraft with minimum equity requirement starting at Rs 200 million and growing by Rs 100 million with every five additional aircrafts. However, for non-scheduled operators, the fleet requirement as stated by the CAR is minimal, requiring possession of just one aircraft. Owing to the high cost involved in the civil aviation sector these regulations increase barriers to entry.

4.3.2 Anti-competitive Practices and Consumers

In this section, three categories of anti-competitive practices have been explained, vis-à-vis their implications on consumers.

Anti-Competitive Agreements

Anti-competitive agreements entail an agreement between enterprises at either same level of production or at different levels with the ultimate objective of raising prices and increasing profits. Such agreements include price fixing, bid-rigging, market allocation either on basis of product or geographically (Box 4), tie-in agreements, exclusive dealing or distribution agreements, refusal to deal and resale price maintenance.
Abuse of Dominant Position

Dominance of an enterprise is judged by the power of such enterprise to operate independently of competitive forces or to the disadvantage of its competitors. Dominance in itself is not anti-competitive in nature, however, abuse of such dominance is. Abuse of dominance is broadly categorised as: exploitative and exclusionary in nature. The various ways in which exploitative abuse could be exercised are: refusal to deal, forced line selling, predatory pricing, non-price predation, price discrimination, IPR abuse and excessive pricing. While way in which exclusionary abuse is practiced is exclusive dealing arrangements.

Box 5: Abuse of dominant position by beer brand in Rwanda

Bralirwa is the dominant brewery in Rwanda with a market share of over 85% (CUTS, 2012), and has been resorting to various practices that raise competition concerns. One of them is the fact that they recommend the price at which their brand has to be sold at retail outlets, bars. The other is that they enter into exclusive contracts with the retail outlets/bars – which debar them from selling the other brands (BMC and imported beer) in their outlets. So, consumers are often over charged and their ability to choose is restricted, as a result of the practices of Bralirwa.

Source: CUTS study in Rwanda (2012)
**Anti-competitive Combinations**

Combination refers to mergers and acquisitions between parties. Merger is a fusion between two or more enterprises resulting in formation of a single entity. In a merger the identity of either both the firms or of one is lost. Control of combinations is necessary since mergers can lead to the concentration of market power in a business entity and thereby increase potential of the resultant business entity to use the market power so achieved in a manner which impedes competition and affect consumers. The adverse effects of combinations includes: reduction in the number of players in the market, increase in the market share of the resultant entity and may also lead to unilateral or coordinated effect of the combined firms or entities.

4.4 Most competition laws are equipped to take actions against the above anti-competitive practices. Such enforcement actions help preserve consumer welfare as is evident from Fig 2 below. However, the process of competition enforcement in developing countries is affected by various factors (resource constraints, coordination with other government agencies, policymakers’ attention, stakeholder support, etc.) and hence their implementation is often weak. In order to strengthen competition regimes and utilise the power of competitive markets for social and economic welfare purposes, it is critical that a comprehensive programme for competition policy reforms is undertaken in countries. In addition to identifying weaknesses in enforcement of a competition law, such a programme would also review policies/laws/programmes/administrative actions to see how the principles of competition are embodied in them.

![Competition enforcement leading to consumer welfare](image-url)
V. In conclusion: Goal-setting for competition policy reforms

5.1 There should not be much doubt that a well-designed competition policy allows consumers to derive benefits from interacting in the market. Competition authorities can only act against anti-competitive practices. In order to promote competition in markets, the principles of competition policy (Box 3) must be incorporated in policies/laws/programmes/administrative actions. This calls for a wider and more comprehensive understanding of the principles of competition policy, which can be achieved by expanding the frontiers of the discussions on competition issues and include senior policymakers, parliamentarians, business leaders, academia and civil society in such a dialogue.

5.2 Needless to say and as evident from various examples including that of CUTS, consumer organisations/civil society can play a crucial role in enhancing awareness on competition issues, especially its impact on markets/economy/citizens, especially in developing countries. The question, however, is how to make this happen. The possibilities are – (i) to identify and convince senior policymakers and planners of this need; (ii) to create a scope for consumer/civil society engagement in policymaking; and (ii) create awareness among consumers/civil society to engage on this issue.

5.3 Civil Society Organisations (including consumer organisations) could act as a catalyst to ensure that consumer benefits have higher visibility in discussions on economic policymaking including on competition. However, there is a need to enhance understanding of civil society on competition issues, especially how policies and practices in key sectors can nurture (or hinder) competition. In order to achieve this, the link between competition (resulting from policies and practices) and consumer welfare needs to be well elucidated.

5.4 The role of CSOs is vital since they have the ability (and often the mandate) to act as a bridge between the regulator, the regulated and the consumers at large. In developing countries, it is critical to identify such ‘champions of competition policy’ among CSOs. Such organisations can help the government/policymakers analyse possible distortions that can arise as a result of policies and practices in key sectors. They can also inform and educate the polity, business, consumers etc. such issues.

5.5 To facilitate interest on competition issues around the world, a network referred to as the International Network of Civil Society Organisation on Competition (INCSOC) was envisaged by CUTS and established in 2001. INCSOC is a coalition of civil society organisations, research institutions, academia, individuals and even parliamentarians pursuing the goal of promoting a healthy competition culture in the world. Currently INCSOC has members from over 60 countries.

5.6 INCSOC is conceptualised on the premise that there is a need for building a network of stakeholders so that competition regimes at the national levels can be strengthened and
developed where absent. In order to give *Competition* visibility as a public policy issue and also mobilise wide-spread support for the same, INCSOC initiated a campaign to declare 5\textsuperscript{th} December as *World Competition Day* (WCD)\textsuperscript{8}. WCD has already received considerable support from around both developing and developed countries, and every year several countries have started to observe World Competition Day on this date. To operationalise this, INCSOC has urged the United Nations Conference on Trade and Development (UNCTAD) to take this proposal to the United Nations General Assembly for adoption of 5\textsuperscript{th} December as World Competition Day.

5.7 CUTS continues to raise awareness and understanding on the need for promoting competition and expanding the scope of the discussions on competition issues, to touch key areas of policy and praxis, especially in developing countries. As indicated earlier, the CREW project (www.cuts-ccier.org/CREW) aims to develop a methodology to help compute impacts of competition (or the lack of it) on consumers and on producers in key markets. Once this methodology is developed and validated, CUTS hopes that it can be applied across other developing countries/markets as well. It is anticipated to help policymakers, government departments/agencies and the international community to better appreciate the role of competition in achieving social and economic welfare in developing countries.

\textsuperscript{8} To see further details visit: http://www.incsoc.net/World_Competition_Day.htm
References


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