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Competition in the Digital Economy

Contribution by The Competition Commission – South Africa

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A. INTRODUCTION

1. The rapid growth of the information and communications technology (ICT) sector has fuelled the proliferation of digital markets in recent years.¹ The digital economy can be described as a platform-based ecosystem of ICT-based products and services.² Digital platforms are normally organised around physical or virtual platforms that enable distinct groups of economic agents to interact with each other. Often, one side of the market is subsidised with the income derived from the other.³
2. Digital markets have dominated global competition law conferences and literature for the past few years. These debates have typically focused on the threat of global or national monopolies due to "winner takes all" tippy digital markets, how best to deal with the economic power of the FAAGs (Facebook, Amazon, Apple and Google) and the inadequacy of national competition law and regulation to deal with these threats.

¹ Toma, F. I. (19 March 2018) The Challenges of Digital Markets for EU Competition Law: The Case of Android. [Internet]. Available at: https://unctad.org/en/PublicationsLibrary/tn_unctad_ict4d08_en.pdf. [Accessed on 27 March 2019].

² Toma, F. I. (19 March 2018) The Challenges of Digital Markets for EU Competition Law: The Case of Android. [Internet]. Available at: https://unctad.org/en/PublicationsLibrary/tn_unctad_ict4d08_en.pdf. [Accessed on 27 March 2019].

³ Kuoppamaki, P (19 May 2015) Tying and two-sided digital platforms. Page 2-3.

3. South Africa, as with many developing countries, share these concerns as we are subject to the same economic forces present in these markets, and our online search and social media is similarly dominated by the FAAGs. Our regulations and competition law are also substantially based on best practice emanating from Europe and the US, resulting in the same gaps identified elsewhere. If anything, we lag behind on addressing these threats, being impotent to act against such global economically powerful companies and waiting for solutions to be driven from elsewhere. This is a mistake.
4. However, there are also some distinguishing features of developing market economies such as that of South Africa which means our agenda around digital markets needs to be broader. These features are existing concentrated markets and vast inequality and poverty.
5. The South African economy exhibits high levels of concentration, in large part a result of our history whereby apartheid denied the majority of the population the opportunity to participate in the economy. However, many developing country markets are similarly concentrated given limited domestic markets on the demand side and limited capital and skilled labour on the supply side. The disruptive nature of digital markets may be harnessed as a force to reduce concentration in the economy and address the existing market power of domestic incumbents. It may do so where competition policy has failed.
6. The South African economy is also amongst the most unequal in the world with high levels of unemployment and poverty. Again, this is a product of our history. It is also something that other developing countries are battling as they undergo the path of development. We face the threat that the Fourth Industrial Revolution may result in greater global and domestic inequality, and that digital markets entrench global companies at the centre of our economies. However, that same disruptive force also provides an opportunity to enhance inclusion in markets which has lacked to date. We need to find means to tip the balance towards beneficial participation rather than exclusion.

B. SHARED GLOBAL COMPETITION THREATS

Dominance of global giants

7. Internet use in South Africa is dominated by global search and social media giants much like other major markets globally. These include Google search, WhatsApp messaging, Facebook, Twitter, YouTube, Instagram and LinkedIn. In addition, we have our own Internet giant in the form of Naspers which built its position through acquiring shares in

Chinese social networking and gaming firm 'Tencent' early on. Naspers also has shares in Indian online travel company 'MakeMyTrip', Brazil mobile marketplace 'Movile' and Russian internet firm 'Mail.ru', amongst others. Naspers also holds shares in old economy broadcast and print media.

8. In South Africa, the following companies are considered 'internet giants':
 - 8.1. Online search services: Google, with limited presence of Yahoo and Bing.
 - 8.2. Social Networks: WhatsApp is the largest social network with an estimated 16 million users at the end of 2016 (out of a total of 21 million internet users at the time). It is followed closely by Facebook with 15 million active users, YouTube with 8.5 million, Twitter with 7.5 million and LinkedIn with about 5 million.
 - 8.3. E-commerce Platform: Takealot is the largest online retailer in South Africa. It started operating in 2001. Takealot is part of internet and media conglomerate, Naspers, which operates in more than 120 countries. Amazon is not particularly prominent in the South African market, focusing more on cloud services than online retailing.
 - 8.4. Matching services: There are two large e-hailing businesses in South Africa, Uber which had 13 462 registered drivers in 2018 and Taxify (rebranded Bolt), which had 20 459 drivers on their platform in 2018. Both operate only in the denser South African cities of Johannesburg, Cape Town, Durban, Pretoria and Port Elizabeth. Local companies have tried to operate in this space but have not been sustainable. Airbnb is also highly active in South Africa and is the dominant accommodation matching service. Again, smaller local platforms are trying to get traction in the market but do not have the brand and reach of Airbnb.
9. These global giants pose a particular enforcement challenge for smaller developing country markets whose own economies are dwarfed by the valuations of these companies. There is a limited ability to effectively challenge global merger activity or pursue complex market conduct cases given the relative unimportance of our markets to these firms. This is particularly the case for those without a strong in-country physical presence, such as search and social media companies, as the regulatory reach is far more limited with most evidence located elsewhere.
10. For this reason, the Commission is of the view that there is a greater need for coordinated enforcement action both regionally and globally.

- 10.1. Firstly, a global legal instrument will need to be developed to allow for greater coordination amongst competition authorities in regulating digital platforms. This legal instrument will ensure that the competitive behaviour of global giants is equally scrutinised across jurisdictions (regardless of size).
- 10.2. Whilst the lead jurisdictions will need to be at the forefront of merger control to contain increased concentration in these global markets, they will also have to take a lead on regulating market conduct of these firms. However, from a global coordination perspective, there needs to be an effective means for any remedial action to be rolled out across developing countries too.
- 10.3. Regional or continental coordination in the case of Africa is also an imperative. This will provide more leverage in dealing with issues that may have a regional or continental dimension, such as development imperatives or digital firms with a stronger regional presence than their position globally.

Regulatory Design

11. There is a global concern that the design of competition legislation as well as other legislation and regulation is not adapted to some of the challenges of digital markets. South Africa shares these concerns as our own legislative and regulatory systems have often been modelled on those in more mature jurisdictions which are also facing these challenges. A few areas are worthy of highlighting:

- 11.1. *Competition law*: - On merger control there is a concern that significant acquisitions of start up companies may not trigger the usual thresholds for merger notification given that these are typically turnover, or asset based. For instance, Facebook/WhatsApp (2015) was not notifiable in South Africa because WhatsApp did not generate any revenue in the country. While South Africa does have the power to investigate small mergers⁴ even after they have been completed, these do not need to be notified to the authorities and thus this may raise additional challenge in dynamic digital markets. On market conduct, the expert report for the EU on competition law in digital markets raises the point that for dominant digital firms there might need to be a reverse onus for them to demonstrate why certain conduct is net efficiency enhancing and not restrictive of new entry. This is not the

⁴ In terms of section 11 of the Competition Act 89 of 1998, mergers are categorised into small, intermediate and large based on requisite financial threshold. In terms of section 13 of the same Act, a small merger does not require mandatory filing with the competition authorities and can be implemented without the statutory approval of the competition authorities. In terms of sections 13A and 14A all intermediate and large mergers require mandatory filing and approval (with or without conditions) with the competition authorities prior to their implementation. The implementation of an intermediate or large merger without the requisite approval is a contravention of the Competition Act.

case currently in South African law as it is incumbent upon the authority to demonstrate exclusionary practices.

11.2. *Regulation more broadly:* - Concerns have also been raised across a number of sectors about the fact that the current regulatory framework does not apply to new, disruptive technology, which gives these firms an unfair competitive advantage over regulated incumbents. For instance, the current regulatory framework for land transport in South Africa does not specifically cater for e-hailing firms. Traditional metered taxis have raised the concern that area restrictions and price regulation applied to their business model is not applied to e-hailing firms, placing the traditional model at a competitive disadvantage. Similar concerns have been raised by broadcasters where streaming services such as Netflix are not subject to local content requirements and local procurement practices.

11.3. *Taxation:* - a further area of unfair competition relates to the taxation regime that domestic firms are subject to relative to global digital firms. Whilst this issue is not necessarily new as multinational taxation has been the subject of tax reforms and developments in transfer pricing, the digital economy has thrown up new challenges. In particular, where firms are located abroad, and the sales transaction occurs online with no physical movement of goods. This situation also permits digital firms to exploit tax havens to lower their overall tax rate, enabling them to out-compete domestic digital rivals too.

12. These types of challenges indicate that a process of regulatory review is required if South Africa is to catch up with the shifts to the digital age. Some of these reviews are already underway, such as changes to tax laws as well as the National Land Transport Act. Whilst the answer in some cases may be to bring the digital firms under the same regulatory regime (e.g. in taxation), in other cases the shifts have revealed the inadequacy of the current regulatory regime and the need to move to a relaxation in regulation (e.g. metered taxis). However, this review needs to be a thoughtful process and one which should not be hastily undertaken.

Enforcement toolkit

13. The Commission shares the view of many jurisdictions globally that the economic analytical techniques are adequate for digital markets. However, these are complex markets that require deep understanding and specialisation if investigation and enforcement is to be competent. This is not unlike healthcare, financial and even telco markets. Currently the investigative teams in merger control and market conduct make

use of specific tools to assist in guiding their decisions. This may include relevant market determination (for competitive constraints), market shares (for dominance), future dynamics based on predictable developments (such as known entry/exit), and established theories of harm typically based on identifying potential price effects.

14. Digital market investigations require certain tweaks to these tools if enforcement decisions are to be accurate and effective. For instance, constraints on innovation rather than price may be relevant for free services, or the price of advertising and not the service itself; market power from data that is unique and non-replicable rather than share of revenue; market definition which determines the extent to which old economy models interact with online versions which are disruptive and may replace them. Similarly, investigations also need to carefully consider consumer behaviour when faced with cases in digital markets.
15. For these reasons, the Commission has embarked upon a process to build investigator knowledge of these markets and update their toolkit for investigations. These initiatives include the following:
 - 15.1. Development of appropriate digital market investigative tools:- We have embarked on a programme to develop a set of internal investigative guidelines for digital market investigations including what information is to be requested and how it may be analysed, the theories of harm to be explored and how market boundaries may be delineated.
 - 15.2. Remedial measure assessment: – considering the challenges faced by the EC in their remedy design of the Google Shopping case, at this point in time, the Commission has embarked on a programme to assist with remedy design in the context of digital markets. Factors such as how to monitor compliance, what remedy to impose and the suitable length of time to impose for that remedy are of interest.
 - 15.3. Advisory panels and collaborative knowledge building: - the Commission is arranging a tech-industry advisory panel that can provide insights to the business models and strategies of these markets. This would assist investigation teams to appreciate better the likely rationale for certain merger activity, the potential strategy that may be pursued and hence what to investigate. We are also seeking collaboration with the tech industry taskforces of competition authorities in other jurisdictions in order to draw in lessons and experience on appropriate investigative techniques.

- 15.4. Use of technology for investigations: - There are also some initiatives on the use of digital tools internally, such as potentially drawing in data analysts on ex officio cartel investigations and tapping into our vast store of information.
16. There are also other challenges presented by digital markets, such as the speed of market development, the dynamism in new start ups and acquisitions as well as the extent of collaborative or partnering arrangements to exploit opportunities. These suggest that an authority such as the Commission may also need to change some of its work processes and approach to guiding firms in the digital economy.
- 16.1. The speed of market developments suggests that as an authority we need to either engage in proactive market scanning for conduct concerns or develop the ability to respond far quicker to market conduct cases. The ACCC has adopted a proactive approach whereby digital markets with features that might provide the incentive and ability to engage in exclusionary conduct are investigated on pre-emptive basis. There is much we can learn from this and possibly adopt in a developing country context.
- 16.2. On the speed of response, South Africa does have interim relief measures on market conduct, but the bar is set very high by the courts for such interventions.
- 16.3. There is also probably scope for more guidance from authorities on what types of conduct or collaborations in the digital context are likely to warrant careful investigation and possible prohibition. Enforcement guidelines that are clear and specific would assist digital enterprises in achieving greater certainty that their behaviour lies within the boundaries of the law.

C. FACILITATING DISRUPTION TO REDUCE CONCENTRATION

The potential for de-concentration

17. Digital markets have greatly opened the space for entrepreneurs and disruptive entry. These business models overcome many of the entry and scaling challenges typically faced by small businesses. New customers can be serviced at little extra cost and cloud computing offers processing power equal to that of large firms. Entrepreneurs in the 'old economy' products can also now leverage the consumer reach and logistics of online marketplaces. This has real potential benefit in a country like South Africa with highly concentrated markets and self-evident barriers to broader economic participation. Indeed, digital market entrants may even succeed where competition policy has failed.

18. Domestically this has been most obvious in the banking sector where digital entrants are introducing innovative pricing models, such as no-fee banking services, which has put pressure on our concentrated 'bricks and mortar' bank sector to do the same. These digital banks are not constrained by historical entry barriers such as the need for a branch network.
19. However, and in other markets where the same opportunities exist, such as insurance and healthcare, we have not seen quite the same progress. More could also be done in banking to open up to other fintech initiatives. Given the level of concentration, digital entrants complain that the large incumbent firms remain in control of access to customers, using this leverage to secure partnerships rather than disruption of their own business. Their control of vast stores of customer transactional and behavioural data means that they are also able to pursue these opportunities alone and shut out the next generation of entrepreneurs.

A pro-active approach

20. Policymakers and regulators in developing countries must also focus their efforts on how to support entrepreneurs to unleash these opportunities and de-concentrate markets. Doing so would directly address the twin objectives of competition policy, namely more competitive and more inclusive markets. This support may be best achieved through proactively unblocking whatever hindrances remain for these digital entrants as the incumbency position of old economy firms can be used to frustrate such entry. Ownership of data and access to customers or distributional channels are market features which continue to favour large firms purely by dint of their size and incumbency, not superior product offering.
21. Data, for example, is seen as a source of significant advantage in the digital age. It is also the basis for many new services as well as old ones. Whilst data is at the heart of remedying the FAAGs power, there is also tremendous scope for a general regime on data portability and interoperability to open markets to new innovative businesses, whilst still ensuring privacy and security of personal data.
22. Financial services are once more a great example of this. Customer transactional and behavioural information is a key source for risk assessment and appropriate product offering. The Open Banking initiatives in the UK and France have ensured the largest banks make that data available to trusted third parties. This enables new financial service providers to emerge because they now have the information required to design and price

products well, but also levels the playing field against the large banks as there is no longer an informational advantage. The result has been more innovation, even from the banks themselves as they seek to stay ahead of the new start-ups. Developing countries can learn from these initiatives.

23. Data is just one example and other practices by even current old economy models work against either smaller digital direct competitors or those wishing to offer complementary services rather than the full package. These practices include exclusivity or MFN arrangements with partnering firms or distribution channels. They also include bundling / tying of products or other self-preferencing arrangements.
24. Whilst we often associate these with digital platforms, they are as much a feature of the old economy platforms in data rich sectors such as financial services. The recommendations of the expert panel for the EU on a Competition Policy for the Digital Era that the onus should be on dominant firms to show that these types of arrangements are not restrictive of competition may also be appropriate in the context of existing incumbents too even if they are not purely digital platforms.

Pre-emptive strike against a concentrated digital future

25. Of course, a proactive approach has another massive benefit, namely that it may well prevent the digital markets that do emerge from becoming concentrated and less inclusive over time. Such rules would mean that the same advantage from data accruing to digital first-movers is not used to create an unassailable lead, or that similar tactics of self-preferencing in the supply of complementary services is not used to exclude new start-ups. After all, if there is one lesson for competition policy from the FAAGs debate is that it is incredibly hard to address that economic power once it is in place.
26. One of the potential advantages of developing countries is that some of these digital markets are not as well developed, or there is still scope for new entry and growth as a large part of the population is not yet connected. This means that there is still space to keep these markets competitive and not have the difficult task of either regulating entrenched monopolists or seeking to develop entrants in their presence.
27. In pursuit of this objective, the Commission is considering a number of potential initiatives that might enhance its ability to pro-actively open up existing markets but also put in place rules to prevent digital markets becoming concentrated.

- 27.1. Proactive case initiation (market conduct): - the Commission aims to continually monitor and keep abreast of investigations and referrals in other jurisdictions. The aim of this would be to proactively explore whether we face similar situations (global platforms after all have the same business model globally). This is in line with the ACCC approach of also initiating investigations where the digital market has the conditions present for market power and potential abuse.
- 27.2. Proactive conduct rules: -regulators in developing countries need to consider what market conduct rules might need to be applied to all digital firms even if they are not dominant in order to prevent a concentrated market. Already the expert report for the EU on Competition Policy in Digital Markets has suggested a shift in onus for dominant digital firms on certain conduct, but we also need to consider whether these or other conduct may apply more broadly in tippy, 'winner takes all' markets. Whilst this may place some restrictions on business models, this needs to be weighed against preventing markets reaching a tipping point and the challenges of regulating dominant incumbents.
- 27.3. Advocacy efforts:- the Commission is building up its advocacy programme to ensure we are vocal in the forums where the work of other regulators or departments may be required in order to put in place rules that may address things a competition authority cannot, such as general data privacy and portability rules. These other regulatory forums may also provide the rules relevant to ensuring more open markets from the start before such markets reach the point of concentration.
- 27.4. Review of merger filing guidelines: - the Commission is also in the process of reviewing its merger filing guidelines. This is to ensure that merger filings received are complete and include all the details required for the Commission to accurately investigate Digital Markets mergers.

D. FACILITATING A MORE INCLUSIVE DIGITAL AGE

28. Even if we are successful in regulating dominant global firms and de-concentrating domestic markets through digital disruption, there remains the challenge of inclusion. The applies at the individual, firm and national level. As reported by the BBC, AI pioneer Andrew Ng ended his speech to an Amazon technology gathering with the following important message *“With the rise of the Internet, we’ve created tremendous wealth, but we also contributed to wealth inequality. Let’s make sure that this time, with the rise of AI, we take everyone along with us.”*

Individual exclusion

29. In South Africa, as in many developing countries, there is still not universal access to broadband. Whilst mobile broadband coverage may be pervasive in a country like South Africa, there is a demand gap as low-income individuals are unable to afford the devices and the data costs in order to access digital services. Currently only 56% of the SA population access the Internet, but usage levels are low even for a large portion of those that do have access.
30. This lack of access is highly problematic as economic, social and political life shifts online, threatening to exclude those who are even currently included. For instance, many job or university applications are now online only. Participation in democracy requires accessing the political debates which have shifted from print to online. There is a real threat of not just economic exclusion, but also exclusion from full participation in society.
31. Responding to these challenges requires a domestic focus on the development of broadband infrastructure and a reduction in data costs. South Africa has a highly concentrated mobile sector and the Commission is currently in the process of conducting a market inquiry into high data costs. However, even if data costs are reduced, it is apparent that there will also be those too poor to participate extensively in the digital age if private paid access is the only means of access. The Data Market Inquiry has therefore also recommended that there is the development of free public WiFi in lower income areas to ensure greater inclusion. This is not something that can easily be provided by the fiscus given the inevitable budget constraints of national and local government in developing economies, and therefore models are being explored to fund such access.
32. An obvious approach are public private partnerships whereby access to government facilities and wayleaves constitute the contribution of government, whereas private firms may offer a free WiFi for a limited period or volume in exchange for also holding the opportunity to develop other revenue sources. These may include a premium service but could also include advertising-based models.
33. However, frequently the biggest beneficiaries of these types of initiatives are the global search and social media giants whose services would be accessed via free public WiFi and who would convert that personal data into value through advertising or other services. In fact, the ability of domestic PPPs to generate revenue may be limited by the fact that global firms may extract that value.

34. This does raise the debate as to whether a digital tax on global search and social media firms is appropriate in a developing country context given that these firms are often the financial beneficiaries of greater broadband access. Furthermore, the vast profits recorded by global search and social media platforms (even after accounting for a period of start-up and investment) indicates that the value of the data provided by online visitors far exceeds the value provided, even if the service is free. It is important to begin a debate about whether more value can be provided to the individuals using this service, not only in the policing of hate speech and fake news, protection of privacy and service innovations, but also to the overall cost of using digital services which includes the device and data costs. It seems some of the global giants are considering this with initiatives such as satellite Internet coverage, and any developments in this regard would be welcome.

Domestic jobs and firm inclusion

35. As many recognise, the Fourth Industrial Revolution has the potential to make redundant many classes of jobs across the global economy. However, it is also recognised that many more different jobs may be created in the process. The students of past industrial revolutions and the disruptions that occurred would even forecast that more jobs may be created than will be destroyed.

36. Jobs will be created in the various digital businesses that are emerging to fill consumer and business needs. These may be the highly skilled data analyst positions, but also the less skilled warehouse, delivery and driver jobs. Demand for content production has never been stronger as the FAAGs look to boost online attention to their sites, and even AI applications need a massive injection of processed data, video and images that is frequently compiled by a human workforce. There are also opportunities in manufacturing the new devices, the minerals and component inputs to those devices and even rolling out the broadband networks on which the digital economy will run.

37. However, whilst there will be many new jobs created, a critical question for developing countries such as South Africa is where those jobs will be located. Whilst many of the physical aspects of digital markets such as distribution of goods for e-commerce will have to be located domestically, this is certainly not the case for new service or product development, as well as the back-office work of online services.

38. There is a distinct risk that the digital age is dominated by global firms from developed economies given that most services can be delivered globally, and global scale

economies provide a distinct advantage. In this context there is a likelihood that the developed economies see the bulk of back-office jobs, either due to convenience or political and social pressure within those countries. If this were to occur, the strides made by many developing economies in integrating into the global economy may be reversed.

39. In order to avoid this potential outcome, more needs to be done to ensure that digital markets are also open to domestic start-ups and challengers, and that global firms share in the rewards that they derive from developing markets.

39.1. On the first point, ensuring more open digital markets at the outset through the pro-active regulations discussed above should not only serve the de-concentration agenda, but should also ensure that these markets remain open to domestic challengers. However, there remains the challenge of developing the skill base and seed capital for participation. This is a local challenge but also one in which the global firms may contribute.

39.2. On the second point, there does need to be a greater commitment from global firms that do extract value from developing economies to also ensure that these economies share in that value. Such firms should ensure that product innovation and back office jobs do not exist in the headquarter countries of global MNOs only and are distributed to centres across the globe. Providing opportunities in countries in which these firms profit will not only create jobs, but also provide the skill base for local entrepreneurs to develop digital firms.

E. CONCLUSION

40. The enforcement of competition law in digital markets has been a prominent theme of global dialogues in recent years as well as academic research. In response, agencies in other jurisdictions have engaged in a deliberate programme to upgrade their skills, investigative tools and proactive enforcement activities alongside advocacy initiatives aimed at regulation. The CCSA has started an advocacy initiative to highlight the digital market issues and there are also some other divisional initiatives, but there needs to be a deliberate internal programme around internal skills development and enforcement. The debate and enforcement action have moved beyond the Big Four (Facebook, Apple, Amazon and Google) and data privacy which impacted our daily work less, and we are increasingly being confronted by national merger activity and potential market conduct that might shape local digital markets into the future.

41. As digital markets are likely to be a priority sector for the Commission, it would be useful to develop a strategy which will ensure that competition policy and law can contribute to ensuring that the new realities of the digital economy work to the benefit of South African citizens. This strategy can focus on (i) updating all the analytical tools at the disposal of the Commission (i.e.: enforcement, advocacy and the like) to ensure that they are able to adequately account for the efficiency benefits which may be realised from the digital economy; (ii) ensuring that the complementarities that exist between competition law and other law regimes are also to the benefit of citizens.