

Chapter 2

Implementing Competition Policy in Developing Countries

Why is the topic important for pro-poor growth?

Achieving the Millennium Development Goals requires rapid and sustained growth in developing countries. It is now widely accepted that the private sector must be the engine of growth, and that governments must create environments that allow the private sector to flourish.

Competition is essential if markets are to work well for the poor. When firms have to compete vigorously, they must find better ways to produce and distribute goods and services. Competition benefits consumers both directly, through lower prices, better quality and an improved choice of products, and indirectly, through its impact on economic growth. As women constitute a larger share of very poor people, women especially will benefit from the impetus given to growth by the existence of competitive markets.

The provision of services by central and local governments contributes significantly to the welfare of the poor. Competition is important for the effectiveness of government procurement (for example, in the provision of rural infrastructure), as anti-competitive practices by suppliers will reduce what governments can achieve with the funds available.

Jobs are an important route to poverty reduction. Competitive markets are more likely to provide the poor with opportunities to be employed or to start their own small business. These opportunities include export-oriented industries. “Competitiveness” is not synonymous with “competition”, but firms and sectors are far more likely to be competitive internationally if they operate within competitive domestic markets.

Competitive domestic markets benefit farmers. They will be in a more favourable position if the markets in which they buy their inputs, arrange transport of their crops to market and sell their outputs are competitive.

The analytical framework “Accelerating Pro-Poor Growth through Support for Private Sector Development” reflects the importance of competition policy to the poor. It discusses the effects of entry and exit barriers to entrepreneurship and the contribution made by competition to innovation and productivity.

Such views are complemented by a growing body of evidence on the link between growth and poverty reduction. The World Bank’s *World Development Report 2005* emphasised the importance of competition for investment and noted how competitive pressure leads to innovation, new products and new technology. When it released *Asian Development Outlook 2005* in April 2005, the Asian Development Bank headlined its view that effective competition policies are needed “if Asian countries are to maintain their high rates of growth and employment”.

The existence of competition policy reduces uncertainty for business and is an important element of a good regulatory package for private sector development. There are also indications that, by reducing the scope for arbitrary decisions by officials, competition law reduces the scope for corruption, which hurts the poor. However, given the practical

implications of transition, it will also be necessary to adopt measures to assist any groups adversely affected by such changes.

Competition policy, including competition law, is needed because markets do not always work well. Anticompetitive actions by firms are one cause, but inappropriate regulations by national, state and local governments are also frequent causes of market failure.

What do we know so far and/or still need to know?

There is a widely held view that competition policy makes a positive contribution to economic growth. An OECD paper, based on a survey of members and invited non-members who participated in the 2002 Global Forum on Competition, concluded that: “There are strong links between competition policy and numerous basic pillars of economic development ... There is persuasive evidence from all over the world confirming that rising levels of competition have been unambiguously associated with increased economic growth, productivity, investment and increased average living standards”.

Competitive markets allow new firms to enter, efficient firms to thrive and sub-standard firms to fail and exit. An OECD study of 53 countries conducted in 2002 found a strong correlation between the effectiveness of competition policy and growth (Dutz and Hayri, 2002). In 1999, the Australian Productivity Commission found that its National Competition Policy reforms mean that “national output [is] ... 2.5% higher than otherwise – an amount equivalent to almost one year of economic growth”. This estimate did not include the dynamic efficiency gains also expected to flow from the competition reforms.

There is increasing information on the harm anti-competitive practices in both national and international markets can do to developing countries. Examples of domestic anti-competitive practices that especially affect the poor include:

- i) Ring tendering for polythene pipe supplied to the Nepal Drinking Water Corporation,¹ and for school construction in China.²
- ii) Flower exports from Morocco being made uncompetitive by the combined effects of a trucking cartel, a freight forwarding cartel and compulsory use of the national airline.³
- iii) Cartels of companies buying tea, sugar and tobacco forcing down returns to farmers in Malawi,⁴ and cartels for retail sales of flour, bread and poultry affecting retail prices in Peru.⁵
- iv) “Bundling”⁶ by dominant firms, such as the action of a gas company in south-western India forcing new customers to buy hot plates when they were connected to the gas supply.⁷

Studies of international cartels investigated by the European Commission and United States competition authorities illustrate their large impact on poor countries. The World Bank’s *Global Economic Prospects 2003* noted that six international cartels overcharged developing countries by USD 3 to USD 7 billion in the 1990s. A 2001 paper⁸ estimated that 16 international cartels overcharged developing countries by between USD 16 and USD 32 billion in 1997 and found that prices fell by 20% to 40% following the break up of the cartels. A study of cartels for aluminium, steel and heavy electrical equipment estimated that they had overcharged Kenya by USD 111 million, Zimbabwe by USD 141 million and Southern African Customs Union members by USD 1.1 billion in 1999.⁹ A study of one

major cartel (vitamins) found that suppliers had overcharged developing countries that lacked a competition law by more than countries that had such a law.¹⁰

Much has been written by economists on the harmful effects of monopoly on prices, output and consumer welfare. However, there has been little empirical research into the impact of competition policy on national economies and very little on the impacts on developing countries.

There are several possible reasons for this, including limits on the availability of data. Most developing countries have a relatively short history of competition law. Countries that have adopted competition laws since about 1990 often accompanied it with other significant policy changes including privatisation, deregulation and trade liberalisation. Separating the effects of these policies is a challenge.

In the case of transitional economies, the appropriate sequencing of policy changes, including the introduction of competition, is of great importance. The experiences of Russia and Syria, for example, highlight the need for better understanding of how to introduce competition to transitional economies.

More empirical research on the harm caused to developing countries by inadequate competition, and on the effects of increasing the intensity of competition through the adoption of competition policy and law, would be of value.

Developing countries are short of finance and skilled people and must choose carefully how to use them to their best advantage. For small countries that are members of regional groups, a regional competition law could enhance the impact of the domestic law. Co-operation arrangements with developed countries could provide help with staff training through exchange programmes and information exchanges.

What are the big controversies?

Competition policy and law is still new in much of the world and there are a few areas of controversy. The main ones seem to be:

Does every country need a competition law?

Some people argue that if a country is open to trade and investment, it does not need a competition law. Openness to trade and investment can have large and beneficial impacts on competition. However, foreign investment can bring heightened concern in developing countries about competition and, in any case, some goods and services cannot be traded internationally. Competition policy and law can benefit all countries, whatever their size and level of development, but the law must be appropriate to their needs.

What is the right relationship between competition law and sector regulators?

Sector regulators are required where competition cannot work effectively, such as with natural monopolies. Regulated sectors generally include major public utilities that are important for consumer welfare. Decisions made by sector regulators include technical issues and pricing or profit ceilings. However, some decisions by regulators are on matters that affect competition. In these cases, their decisions should reflect competition principles. If not, there can be distortions in the use of national resources that can harm consumers, including the poor.

Does having a competition law mean developing countries cannot have an industrial policy?

Every national competition law includes some allowances for national priorities, and there is no necessary conflict between competition and industrial policy. Well-designed policies can be complementary. The “Development Box” approach in the World Trade Organization (WTO) arrangements is relevant not only for industry, but also for agriculture.

How should the introduction of competition policy, including its enforcement structure, be sequenced?

There are specific constraints that are characteristic of the degree of development of an economy, and of its society as a whole. There is a need to investigate the extent to which a blueprint approach can be used to address the question of sequencing.

What sort of policy implications and suggestions for donors can we give?

The overall policy implication for donors is the need to recognise the contribution that effective competition can make to the welfare of the poor. As the 2001 Nobel Prize winner Joseph Stiglitz said: “Strong competition policy is not just a luxury to be enjoyed by rich countries, but a real necessity for those striving to create democratic market economies”.

Increasingly, developing countries want to adopt appropriate competition regimes, but need help. Specific national issues must be identified clearly and the analysis of what help is appropriate requires close attention. In providing the help needed, it is desirable that donors harmonise their activities to avoid the possibility of duplication or of leaving gaps. There is significant scope for additional support from donors in four major areas:

Policy research to build and disseminate the evidence base

More empirical research on the impact of competition policy and law in developing countries, as well as on best practice, would be of considerable value. Worthwhile areas for research include the four areas of controversy previously mentioned.

Culture of competition

A “culture of competition” is where the rules and benefits of competition are widely known and form a natural part of the background for decisions by firms and governments. Building a culture of competition and an effective competition regime is a long-term endeavour, and not just a matter for one-off events. Competition must be “mainstreamed” in all sectors.

Advocacy is needed for a new competition regime to succeed. Politicians and officials need to understand why competition is good for the economy, and how to apply its principles to government decisions. There is a need to overcome opposition from the business sector by emphasising the benefits competition law can provide, such as cheaper inputs and the contribution competition law and policy can make to creating a good pro-investment climate.

Some NGOs, especially consumer groups, can be strong allies for competition policy and law because they know how it can benefit consumers. Donors could find it effective to fund relevant work by reform-minded NGOs, especially those based in developing countries. For example, the UK Department for International Development (DFID) has funded research and advocacy programmes (such as the Consumer Unity and Trust Society

[CUTS] 7-Up projects)¹¹ that include participation by local consumer groups, and has funded the preparation of materials by Consumers International for use by consumer organisations.

Bilateral technical assistance and capacity building

Help is needed in formulating a competition policy and law, and in developing and strengthening the institutions that will enforce the competition law, including the training of specialist staff. Assistance can be provided by funding training programmes organised by the competition authority in the donor's country, including staff exchanges, and by funding studies of barriers to competition in important sectors of the economy.

There is scope for donors to support proposals for roundtable forums on competition policy and law for senior policy makers from developing countries.

Programme funding

Donors can fund the technical assistance and capacity building programmes of international and regional organisations.

The United Nations Conference on Trade and Development (UNCTAD) has a well-established programme of technical assistance and capacity building activities.¹² It also organises annual meetings of the Intergovernmental Group of Experts on Competition Law and Policy (IGE), a useful forum for competition officials in developing countries.

Membership of the International Competition Network (ICN) is open to competition authorities of all countries. A "virtual" organisation, the ICN addresses both practical enforcement issues and policy issues, and seeks convergence of best practice. The ICN's Competition Policy Implementation Working Group seeks to identify the key elements needed for successful capacity building and competition policy implementation in developing and transition economies.

The World Bank is active in policy research and capacity building on competition policy issues.

While competition policy has been removed from the scope of the Doha Round, the WTO continues to provide technical assistance on competition to a number of developing countries.

"Peer reviews" can be a valuable way to objectively assess the operation of national competition laws. Some have been undertaken by the OECD, with donor support,¹³ and UNCTAD presented peer reviews of Jamaica and Kenya at its conference in November 2005.

Donors can assist organisations working to create a regional competition policy as part of a regional economic structure, such as Carribean Community (CARICOM), Common Market for Eastern and Southern Africa (COMESA), West African Economic and Monetary Union (UEMOA) and *Mercado Común del Sur* (MERCOSUR). Assistance may be needed by Africa, Caribbean and Pacific countries (ACP) in identifying and negotiating their objectives in the forthcoming Economic Partnership Agreement (EPA) negotiations.

Recommended best practices

Modern regulatory regimes for private sector development should include competition policy regimes. Some of the practices to be encouraged in the design and operation of a competition law are outlined below.

- i) The design of the law should reflect the level of economic development of the country concerned, the structure of its economy and its constitution and culture. A competition law should not simply be transplanted from a developed country, or even from another developing country. A competition law should not stand alone, but should be part of a well-designed package of measures to create the right environment to allow competitive markets to benefit the poor.
- ii) The introduction of competition policy should be reflected in the annual and medium-term plans and budgets of governments. Activities supported by donors should be adequately planned and appropriately monitored.
- iii) The focus of a competition law should stay as close as possible to the objective of fostering competition in markets. Other social and political objectives should, ideally, be targeted through more specific measures in other legislation. Exceptions and exemptions should be minimised as competition law is most effective when applied broadly to the economy, including to state-owned enterprises.
- iv) Whatever division of responsibility between sector regulators and the competition authority is chosen regarding competition issues, there should be an effective working relationship between the regulators and the authority.
- v) A competition authority should be independent of government in its day-to-day decisions. This has implications for the selection of people to be appointed to the authority. The authority should have an adequate budget and should be staffed by competent officials.
- vi) A new competition authority needs to prioritise its work carefully. A good rule of thumb, at least initially, is to concentrate on cases where entry barriers seem high, where prices seem high and where consumers will benefit most. These initial targets should include those with the least substantial vested interests that would oppose change. That is, to improve support from consumers and politicians for the new competition law, the competition authority should choose an early “winner”.

Notes

1. Adhikan, R. (South Asia Watch on Trade, Economics and Development, Kathmandu), presentation at FIAS Conference, Sri Lanka, June 2004.
2. OECD (2002), *Global Forum on Competition 2002*.
3. USAID (United States Agency for International Development) study reported at International Competition Network Workshop, Paris, February 2002.
4. CUTS (Consumer Unity and Trust Society, India) (2003), *Spine Chilling Experiences of Anti-Competitive Practices in Malawi*.
5. CUTS (2002), *Challenges in Implementing a Competition Policy and Law*.
6. “Bundling” involves a dominant firm compelling purchasers of the product for which it is dominant to buy another product as well, which they might not want or might be able to obtain more cheaply elsewhere.
7. CUTS (2002), *Competition Policy and Law Made Easy*.

8. Levenstein, M.C. and V.Y. Suslow (2001), "Private International Cartels and their Effects on Developing Countries", background paper for the World Bank's *World Development Report 2001*.
9. Jenny, F. (2002), paper presented at WTO Regional Workshop on Competition, Mauritius, November 2002.
10. Clarke, J. and S. Evenett, (2003), "The Deterrent Effect of National Anti-Cartel Laws: Evidence from the International Vitamins Cartel", *Antitrust Bulletin*, No. 3.
11. CUTS is an NGO based in Jaipur, India. The first "7-Up" project undertook research and advocacy on competition policy in seven developing countries that had adopted competition law (four in sub-Saharan Africa and three in south Asia). This two-year project, funded by DFID, concluded in February 2003. CUTS is currently undertaking "7-Up 2", a study of competition policy in several countries in Asia. This project is funded by SECO (the State Secretariat for Economic affairs of Switzerland) and DFID. CUTS recently commenced "7-Up 3", which will undertake research and advocacy on competition policy in seven countries in sub-Saharan Africa, and which is being co-funded by NORAD and DFID.
12. See Competition policy for Development: A report on UNCTAD's Capacity Building and Technical Assistance Programmes (2004), <http://r0.unctad.org/en/subsites/cpolicy>.
13. DFID funded the peer review of South Africa's competition law and policy undertaken at the OECD Global Forum on Competition in 2003.

Further reading

Brusick, P. et al. (eds.) (2004), *Competition, Competitiveness and Development: Lessons from Developing Countries*, UNCTAD, Geneva.

Cook, P. et al. (eds.) (2004), *Leading Issues in Competition Regulation and Development*, Edward Elgar, Cheltenham, UK.

CUTS (2003), *Pulling Up Our Socks*, Jaipur, India.

DFID (UK Department for International Development) (2004), *How to support competition policy and law*. A "How to..." note in the "Working with the Private Sector" series, available from DFID.

Mehta, P. (ed.) (2005), *Towards a Functional Competition Policy for India*, CUTS and Academic Foundation, New Delhi, India.

World Bank (2004), *World Development Report 2005: A Better Investment Climate For Everyone*, World Bank and Oxford University Press.

The competition sections of the websites of the OECD, the WTO, UNCTAD and the World Bank, and the website of the International Competition Network (ICN) contain extensive information that includes material on the development impacts of competition policy and law.