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THE ECONOMICS OF COMPETITION AND CONSUMER POLICIES

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**THE ECONOMICS OF COMPETITION AND CONSUMER POLICIES:
THE DEVELOPING COUNTRY'S PERSPECTIVE**

By

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1. Introduction

1. When a country strives to attain highest economic growth, it tends to cast aside policies that may pose impediments to the attainment of such goal, such as those concerning consumer protection. However, it becomes more developed and its people enjoy a higher living standard, issues concerning rights of consumers would naturally emerge. Thus, while the challenge of how to best balance the interests of consumers versus those of producers is faced by all governments, it is more complicated for emerging countries that are going through a transition phase from a formally producer-oriented economy to that of more consumer-oriented one. This paper seeks to address the specific economic and practical problems that governments of a developing country experience in the formation of consumer and competition policies.

2. The Economics of Consumer and Competition Policy

2. Basic economics tell us that in a contestable market, competition will yield most efficient resource allocation generating lowest cost, greater choice in terms of quality and variety of both product and service. Thus, both consumer and competition interests are harmonious. Of course, in markets where effective competition is not viable, regulation will be required.

3. In many developing countries, however, consumers are often denied the fruit of competition because of various state rules and regulations deters entry of alternative suppliers or products. In such cases, removing those restrictions would appear to be the straight forward solutions. While this may sound simple and obvious, in reality it is extremely difficult to do so. This is because introduction of competition into any market affects the distribution of rents across different interest groups that are politically difficult to administer. More importantly, these barriers may have been constructed in the first place as part of the country's policy to develop local industry.

4. For example, the Ministry of Finance of Thailand had had to procure monetary coins from a single local producer, whose bidding price is likely to have been raised to match those of other bidders overseas that face high tariff wall. The attempt to remove the tariff in order to allow foreign bidders to compete on equal footing was thwarted by the fact that the particular sole producer in Thailand received investment incentives to pioneer local coin production. It is commonplace for industrial policy to be at variance with competition or consumer policy. Similarly, many people in developing countries suffer from high utility prices and sub-standard services or worse, denied access to such facilities altogether, as a result

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of state monopolies in public utilities. But the decision to privatise state enterprise is very much a political as economic.

5. To sum up, competition can go a long way in protecting consumers. While it is true that competition cannot safeguard “all” consumer interests, but it does so for most “basic” consumer interests – i.e., excessive price, lack of choice, low quality product or service -- that are often inadequately protected in most developing countries.

6. Consumer problems that cannot be solved by market competition, such as false or deceptive advertisement, require consumer laws. Health and safety issues are also part of consumer law and policy. Here, consumer and competition policy may be in variance with each other. The following section will address this issue in details.

3. Developing Country’s Consumer and Competition Problems and Challenges

7. Most developing countries face greater consumer and competition problems than do their more developed counterparts. This is because competition in many markets tends to be limited by the relatively small domestic market protected by high tariff walls and a restrictive strict foreign investment regime that deny imported products and foreign suppliers. Liberalisation that would surely benefit consumers can come at great costs for economies whose suppliers are not competitive and where import duties contribute to a major part of government revenues. At the same time, consumers in developing countries are generally less informed than their counterparts in developed countries, and thus more vulnerable to deceptive marketing schemes.

8. All this implies that consumer policy in developing countries would tend to be excessively reliant on “hard” state rules. In the absence of effective market mechanism that would help ease at least the “basic” consumer problems such as price, quality, availability and choice of products or services, state regulations would be required to protect consumers. At the same time, the less likely that a consumer can make an “informed” decision, the more likely that the state would have to implement “hard” rules such as banning or standardisation of a particular product or service. Such rules are much more likely to create market distortions than softer rules such as disclosure rules.

9. This is certainly not good news as most developing countries face weak regulatory capacity such that excessive regulations may result in widespread damaging “regulatory failure”. It is an observed fact that given limited regulatory capacity, the relevant authorities often resort to “simple” and “visible” rules such as price controls rather than those that are more complex and less visible, such as competition rules. It is also another observed fact that “market-based” regulations such as taxation are less commonplace than “hard” rules such as total ban on a particular product or service. This is usually the case because tax issues often come under the purview of the Ministry of Finance, whose mandate does not cover consumer protection. Such hard rules may not only cause severe distortion to the market, but also not effective in achieving the intended goal of protecting consumers.

10. For example, the price control authority in Thailand found the price of 250 ml. bottled drinking water excessive, and so placed a cap on the price which consumers can be charged for the particular product. This prompted all producers to stop producing the product as the maximum price set happened to be below the actual cost of producing it. As a result, consumers are denied the product altogether and had to purchase 500 ml. or 1 litre bottles instead. Similarly, softer price control measures that require suppliers to “declare” maximum prices charged to the authority in order to protect consumers from excessive pricing may instead facilitate tacit price collusion that are adverse to the interests of consumers. These are only a few examples of many misguided and erroneous consumer protection measures.

4. What can be done?

11. In light of the regulatory capacity constraint, developing countries should attempt to make greater use of market mechanism and rely less on state rules to deal with more basic consumer issues such as excessive price, limited choice and low product or service quality. Here, competition law and policy can play an important role in promoting and safeguarding greater competition in the market. In most cases, one will find that competition is constrained by governing state rules and regulations. Restrictive licensing regimes, exclusive concessions and restriction on foreign investment are often the major underlying factors impeding effective competition in the market.

12. Indeed, market liberalisation may undermine industrial development goals. Here, a careful analysis is required to evaluate the benefit derived from protecting a particular industry against the costs born by other industries, in particular the downstream industries as well as consumers. Also, sunset clause should be implemented to ensure that protected industries seek to improve their competitive edge within a given period of time. Unfortunately, such analysis or sunset clauses are rare. Protection is often provided with little or no quantitative justification and granted indefinitely.

13. As for consumer problems that do not arise from lack of effective competition in the market, such as deceptive or false advertisement, inappropriate marketing schemes, product liability, etc., the need to regulate to protect consumers is inevitable. Consumer protection in these areas in most developing countries remains relatively weak because the competent authorities often reside under the Ministry of Commerce or other Ministries whose major mandate is not to protect consumer interests. With relatively weak non-government consumer advocacy groups, chances that these measures will be overly restrictive causing harm to the competitive environment in the market are often slim.

14. The same may not be true for the regulation of health and safety standards in some countries where the competent authorities reside within the Health Ministry or other Social Ministries. Here, measures designed to protect consumers may be administered with little or no consideration of their impact on competition in the market.

15. For example, a study by Thailand Development Research Institute (2006)¹ found that the banning of a lower quality steel beam was attributed to the fact that the particular steel requires relatively more advanced skill in welding, which is rare in Thailand. As a result, structures built from lower quality steel beams can be rather unsafe. Following a collapse of a structure using such steel beams, the product was banned altogether.

16. Here, the banning of the product not only failed to solve the problem at its root cause, but also led to the bankruptcy of many small producers who were unable to produce higher quality steel beams due to limited technological capability. At the same time, consumers are deprived of less expensive lower-quality steel beams that are more cost-effective for building lighter structures. As a result, consumers and retailers had had to resort to illegal substitutes that flourished in the absence of effective monitoring. This case illustrates a consumer protection measure that not only damaged the industry, but failed to protect consumers. Such botched consumer protection measures are commonplace in many developing countries.

17. It is imperative that before implementing any consumer protection law that will limit consumers' choice, the competent authority need to assess a) the relative efficacy of various regulatory measures b) the cost of implementing, enforcing and monitoring such measures and c) potential adverse economic impact. These exercises require a comprehensive set of data and a thorough analysis that are often unavailable.

¹ Thailand Development Research Institute (2006), *A Study on the Impact of Restrictive private practices and state regulations in 6 Selected Industries in the Agriculture, Manufacturing and Service Sectors*, 2006

18. To conclude, from a developing country's view point, consumer and competition policies are rarely in variance with each other. More worrying are misguided consumer protection measures that are adverse to both consumers and competition in the market at the same time. What is sorely needed are greater appreciation of market mechanism and more sophisticated regulatory impact assessment of any consumer policies both ex ante and ex post.