Global Forum on Competition

COMPETITION AND POVERTY REDUCTION

Contribution from El Salvador

-- Session I --

This contribution is submitted by El Salvador under Session I of the Global Forum on Competition to be held on 28 February and 1 March 2013.
COMPETITION AND POVERTY REDUCTION

-- El Salvador --

1. Defining poverty and identifying its causes.

   1. In El Salvador, the measurement and definition of poverty is through the method of poverty line as a parameter taking the value of the Basic Food Basket (CBA). This means that the poverty rate is directly related to income, classified in extreme poverty, households in which their income is less than the cost of the CBA and relative poverty, households are those whose incomes is less than the cost of the extended CBA (dressing, house, healthy, education etc.) It is relevant to mention that El Salvador does not create the extended CBA, for this reason we assumed that is equal to twice the value of the CBA.

<table>
<thead>
<tr>
<th>CBA/Sector</th>
<th>Urban (Type of household with 3.72 members)</th>
<th>Rural (Type of households with 4.24 members)</th>
</tr>
</thead>
<tbody>
<tr>
<td>CBA</td>
<td>$182.60</td>
<td>$143.90</td>
</tr>
<tr>
<td>CBA extended</td>
<td>$365.20</td>
<td>$287.70</td>
</tr>
</tbody>
</table>

   Source: Its own elaboration based on data of the Household Survey Publications Multipurpose publication. (EHPM) 2011

   2. The average monthly income in 2011, was for a total of $486.67, the urban $574.46; the rural $321.59 and for the Metropolitan Area of San Salvador, up to $670.53.

   ![El Salvador: Average Monthly income 2011](image)

   Source: Its own elaboration based on data of the Household Survey Publications Multipurpose publication. (EHPM) 2011

   3. According to these data, nationally 40.6% of households in poverty and of these, 12.2% are in extreme poverty and 28.3% in relative poverty. The graph below shows the percentages of poverty nationally, in urban, rural and in the Metropolitan Area of San Salvador (AMSS).
El Salvador: Proportion of households in poverty 2011

Source: Its own elaboration based on data of the Household Survey Publications Multipurpose publication. (EHPM) 2011

4. The following table shows the evolution of poverty in rural and urban areas from 2007 through 2011.
1.1 **Is this a correct measurement method?**

5. According to the United Nations Development Programme (UNDP) data, the methodology of measuring poverty used in El Salvador has become an obstacle for building an economy based on the welfare of people. This phrase is explained because a sustainable measure should contain statistical information on the multiple dimensions relevant for welfare, for example the security level, the standard of living, income, level of education received, health, social security, employment status of others. The definition of poverty taken only on the income variable prevents the onset of social and public policies on human development.

1.2 **The new methodology of measuring poverty: Multidimensional poverty**

6. In July 2010, Oxford University and the United Nations Development Programme (UNDP) launched at a policy forum in London, a new poverty measure that gives a “multidimensional” picture in order to deepen the understanding of this phenomenon and create public policies to eradicate poverty.

7. Poverty measured by the Multidimensional Poverty Index (MPI) defined as: “The Measure to portray the many deprivations faced by the most severely disadvantaged. The MPI reflects the incidence of multidimensional deprivation, and its intensity, how many deprivations people experience at the same time. Also, can be used to create a comprehensive picture of people living in poverty, and permits comparisons both across countries, regions and the world and within countries by ethnic group, urban or rural locations as well as other key household and community characteristics.”

8. According to this guideline, El Salvador government supporting by the UNDP, have been developing a new method to the poverty measure. This method it’s in it phase of qualitative research, preliminarily established as basis for measuring the dimensions housing, employment and leisure. As preliminary data, in El Salvador has estimated a Multidimensional Poverty Index at the household, national 61.1%.

9. In the dimension associated housing as privation the following:

- Tenure (No property rights acquired).
- The quality of the materials: the roof stands
- Endowment for rest furniture (chairs and bed)

10. It builds the idea of **decent housing:**

- All basic services: electricity (private connection), water (pipe inside the house) and toilet (bath washable).
- Clearly separate spaces (two-story house)

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4 Source: Preliminary findings. Systematization of 8 focus group. UNDP El Salvador. 2012.
• A garden with flowers and greenery
• Brick wall or concrete block, and ceramic floor. The roof in good condition is associated with the minimal of housing.

11. In the work dimension, people in poverty consider work only the paid work (employment) rather than subsistence activities they undertake. In rural areas, for example, do not call work to farm work every day assuming you do not report income. Nor do they consider the job work from home.

12. In the work dimension deprivations are associated with the following:

• Lack of a fixed salary (monthly payment)
• Work instability (work few days a year)
• Do not have the training necessary to work
• Do not have work experience

13. The entertainment dimension refers to the opportunity for fun and entertainment and to have physical space for these activities. In turn, the fun opportunity is related to the lack of time to develop that, because of the subsistence labor (domestic crops, washing clothes, watering poison, firewood, etc.). Additionally in rural areas, they do not have adequate space for recreational activities and in the urban by discrimination.

1.3 What factors cause poverty?

14. Under the method of measuring poverty based on income currently used in El Salvador, poverty is caused by lack of income to purchase the CBA. The direct factors that affect lack income are employment representing the source of household income and education level as the possibility to earn income.

15. The formal jobs are associated with higher average incomes and lower poverty rates. Thus, it is determined that unemployed population, 23% are in extreme poverty and 35.1% in relative poverty. Underemployed population, 16.8% are in extreme poverty and 31.2% in relative poverty. Finally, people categorized with decent work representing only 6.3% of poverty.

16. As for the low level of education, "The incidence of income poverty is inversely related to the education of the people." The Human Development Report of UNDP El Salvador has estimated that poverty rates are zero for the population with university education (about 17 to 18 years of schooling) unlike with zero education population, whose poverty rate is 57%.

2. Competitions effect on markets for essential items, in principle.

17. According to economic theory, it is desirable market where demand and supply are in equilibrium. In a competitive market, the equilibrium point is the result of decisions of millions of consumers and producers. The equilibrium prices (Pe) and the equilibrium quantity (Ce), provide the greatest welfare of society as a whole, ie efficiency.

18. In a market with no competition (monopoly or oligopoly), reduces the level of production and also increase the prices of goods or services they produce. In the market for essential goods and services,
consumers have few or no options to purchase a substitute product and purchasing power will decline further due to the price increase. This distortion will produce shortages and reduced units consumed, since the price increase translated to economic inefficiency.

19. Competition is not a one-dimensional phenomenon where only the prices offered are valued, but also technological innovation and increased product quality. The work pro competition, making the Superintendence of competition, is designed to protect market efficiencies in order finally to preserve consumer welfare and not to replace the pure competitive process.

20. The main problem of an anti-competitive market is not in the price increase, but limiting the production of that good or service essential. A higher price creates distributive problems. As for limiting production, market shortages will cause even higher prices that may not acquire the poorest. According to UNDP data; 2007 and 2008 a consequence of the food prices increase, this produce an higher prices and extremely and relative poorest.

21. The premise is that competition improves market conditions for consumers who are in poverty: In 2012, the Competition Superintendence rejected a merger in the telephony market. This refusal was an incentive for one of the operator’s involved, who announced an increased investment by an amount between $ 40 and $ 50 million in the country, increasing jobs and promotions in the telephony sector. We show, according to this case, that competition improves the conditions of the population, in a sector that accounts for 4.13% of the market basket.

3. **Competition effect on markets for essential items, in reality.**

22. The goods considered essential, according to the CBA are⁵:

23. French bread, (wheat flour), tortillas, (rice, meats, grease, eggs, fluid milk, fruits, beans, vegetables and sugar. The essential services are: electric energy, potable water, gas en sanitary infrastructure⁶.

24. Based on the National Household Income and Expenditure Survey (ENIGH), then presents the importance of certain goods considered important in the economy of all consumers. The CBA represents

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⁶ Human Development Report El Salvador 2010: From poverty and consumerism to the welfare of the people. UNDP 2010
the area of food and soft drinks with a structure on annual consumption of 19.8% of the consumption structure of Salvadoran consumers.

<table>
<thead>
<tr>
<th>National household Income and Expenditure Survey 2005-2006</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Entry</strong></td>
</tr>
<tr>
<td>-----------------------------------------------------------</td>
</tr>
<tr>
<td>Food and non-alcoholic Beverage</td>
</tr>
<tr>
<td>Alcohol, drugs and sniff</td>
</tr>
<tr>
<td>Clothing and footwear</td>
</tr>
<tr>
<td>Housing, water, electricity, gas and other fuels</td>
</tr>
<tr>
<td>Furniture, household equipment and routine household repair</td>
</tr>
<tr>
<td>Health</td>
</tr>
<tr>
<td>Transportation</td>
</tr>
<tr>
<td>Communication</td>
</tr>
<tr>
<td>Recreation and culture</td>
</tr>
<tr>
<td>Education</td>
</tr>
<tr>
<td>Restaurants and hotels</td>
</tr>
<tr>
<td>Miscellaneous goods and services</td>
</tr>
</tbody>
</table>

Source: National Household Income and Expenditure Survey 2005-2006

25. According to the CBA, the Competition Superintendence (SC) has been sanctioned anticompetitive practices and ordered the realization of market studies on competition conditions issuing policy recommendations that seek to strengthen and improve the conditions of competition in the following markets:

a) Wheat Flour

b) Sugar

c) Rice industry

d) Gas and other fuels

e) Electric sector

a) **Wheat Flour market**

26. In the year 2008, the SC initiated disciplinary proceedings against MOL S.A and HARISA SA, who accounted for 97.82% of the market for wheat flour. After extensive investigations both economics agents were sanctioned for being material, legal and economic evidence of market division of the wheat flour in the whole country, showing a degree of rivalry that showed maximum stability in the market.

27. **Impact**: The lack of rivalry in the market reduces incentives to innovate and invest in more efficient technology. The market division agreement allowed the increase in prices of wheat flour. In a

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market with inelastic demand, no substitutes, the price increase lowers the purchasing power of buyers in relation to other essential goods and services, directly affecting household consumption. Also be an input affects, increases the price of their end products. The administrative chamber of the Supreme Court of Justice outlawed the procedure, because, in their opinion, the search warrant issued by the judge in civil and commercial matters was incomplete. Currently this Office has begun a process under the Constitutional Chamber of the Supreme Court of Justice (CSJ) against the judgment delivered by the Administrative chamber of the Supreme Court of Justice.

b) Sugar market

28. In 2010, the SC initiated an infringement ex-officio procedure on the market for wholesale distribution of bulk white sugar, against Sugar and Derivatives Distribution, SA de CV (Dizucar), operator with a market share of 75%. Dizucar was sanctioned by evidence found differentiated pricing and discriminatory restriction on the sale of the product, concluding that this economic agent committed the practice of abuse of dominant position. It is currently under study by the Administrative Chamber of the Supreme Court of Justice.

29. The SC has estimated that in 2010, the product of the anticompetitive practice by DIZUCAR, Salvadoran households overpaid an estimated $12,483,372.32 in buying sugar for consumption.

c) Study on the characterization of agribusiness rice and competitive conditions in El Salvador

30. The rice sector in El Salvador is protected by treaties and agreements, including those for the administration of tariff quotas based on the FTA (TLC) between The United States, Dominican Republic and El Salvador, the DR-CAFTA, the trade policy of the Central American Tariff System SAC and El Salvador agreements with third countries.

31. Such protection imposes barriers to entry of new competitors, leading to a highly concentrated market. The Superintendence of Competition felt that the agribusiness rice and producers overpaid approximately $8.8 million, according to the agreement price of paddy rice. This amount is transferred to the overpayment made by final consumer for payment of rice for consumption.

d) Study on conditions of competition in the field of liquefied petroleum gas and other fuels

32. According to the National Household Income and Expenditure Survey (ENIGH 2006), the area of housing, water, electricity, gas and other fuels accounts for 22% of household spending Salvadorans. In this respect the SC sanctioned in the fuel sector an abuse of dominant position.

33. The process was initiated by complaint against Shell Company in El Salvador, SA (Shell) and Esso Standard Oil, SA Limited (ESSO). These operators were sanctioned for zoning sector price of gasoline. This anticompetitive practice significantly distorted prices of gasoline. Besides, being an input product, has a direct productive activities, industrial, commercial or service and ultimately affected all impacted on the basic food basket.

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e) Electric sector

34. In 2006, there was the presentation of the electricity sector study. In 2008, an electricity distribution company was sanctioned for being who abused their dominant position by preventing a competitor interconnection to its network.

35. Despite the achievements made in the detection and punishment of anticompetitive practices in the market for essential goods and services, it is important to mention that all operators sanctioned such practices lawsuits have been filed before the Administrative Chamber of the Supreme Court of Justice (CSJ), alleging the illegality of decisions handed down by the SC. Up to now, the Administrative Chamber of the Supreme Court of Justice, has not yet ruled on the legality or illegality thereof, making it impossible to measure the impact of the SC resolutions have resulted in these markets.

4. Competitive markets versus pro-poor government controls/interventions

36. According to the Salvadoran government's economic policy, interventions in economic activity should be exceptional. State intervention in the competitive market process has been embodied in strategic sectors of the economy that cuts across all economic sectors of the national market, for example in the field of electricity, liquefied gas, telephony, the sector finance, medicine and others. State intervention is outlined as such from social policies and fiscal policies aimed at protecting agriculture, industry, investment and finally to the most vulnerable population in terms of poverty through the imposition of tariffs, taxes and subsidies.

37. Although the state intervenes on behalf of the most vulnerable population and economic theory states that such intervention distorts the market, in order to protect and promote competition, the Superintendence of Competition has legal authorization to order studies and to issue opinions and recommendations about draft laws and state policies that may block or impair the competitive process. Some examples are found in the rice market and market of Liquefied Petroleum Gas (LPG).

38. The study in the rice market, issued important recommendations to increase competition in the sector. As already mentioned the rice market is protected to encourage domestic production and protect food security however, represents high barriers to entry, restrictions on international trade and therefore restricted to the competitive process.

4.1 Subsidy liquefied petroleum gas (LPG)

39. In El Salvador, the State provided a generalized subsidy to Liquefied Petroleum Gas (LPG) for over thirty years, until 2010. Although subsidies are intended social welfare, the LPG, presented problems to rationalize public spending and targeting.

40. In 2008, the LPG subsidy represented $140 million of public spending, increasing the burden on public spending and thus affecting the fiscal deficit, so it became necessary to rationalize. This rationalization was addressed through the targeting of the subsidy, according to World Bank data, it was established that this subsidy was regressive, meaning that higher income strata are benefitting and reached only 26% of poorest households. According to Human Development Inform (HDI El Salvador 2010), the LPG subsidy not addressed to the poor because 20% of the poorest households do not use propane, In contrast, they cook with wood.

41. In 2011, the program began targeting and rationalization of public spending LPG subsidy. In order to identify potential recipients to receive the LPG subsidy were implemented various strategies for the creation of databases that have enabled the socioeconomic characteristics of families and businesses, and their consumption structure in electricity. The new subsidy is available to those households in their electric bill have consumed an average of 199.99 kWh in the last twelve months\(^{12}\) and those households that have electricity, the poorest strata of society, i.e. the poorest strata of the Salvadoran population.

4.2 Drugs sector

42. The health sector represents an expense of 4.3% of total household income, according to the National Household Income and Expenditure Survey (ENIGH) 2005-2006, health and pharmaceutical expenditure includes expenditure on medical and hospital services.

43. Given that health spending of Salvadoran households is representative and based on the studies, recommendations and opinions relating to drug industry adopted or issued by the SC, the Board of Directors adopted a common position in order to improve access to drugs, the quality and availability in the market, making the following recommendations:

1.1 Reforming intellectual property laws authorizing parallel imports;

1.2 Reforming intellectual property laws in order to regulate compulsory licenses on terms more favorable to competition.

1.3 Reforming the Regulation of Proprietary schools eliminating import control of responsible professional medicine CSSP records;

1.4 Avoid the introduction of news and unnecessary entry barriers to new competitors, such as preventing holders of pharmacies and other health establishments duly authorized that have a directly importing drugs;

1.5 Promote competition by implementing proactive policies of generic substitution, such as the adoption of rules to promote the prescribing and generic use, implementation of monitoring mechanisms to ensure the efficacy and safety of generic drugs, and performing information campaigns to professionals and the public;

1.6 Remove practices and drug laboratories consisting fund, grant or give seminars, royalties or other perks to doctors in any form to be submitted;

1.7 Implement policies grounded in international quality standards in the field of medicine, such as funding for the conversion of industrial companies to international standards, including technological transformation projects, promoting a culture of productivity and quality nationally positioning the issues of quality and productivity as a priority, and improving infrastructure to support best practices in quality and productivity;

1.8 Avoid placing the prohibition laws prescribe medications, consultations and discounts by laboratories and drug stores to retailers;

\(^{12}\) Agreement No. 1153. The executive body in the Field of Economic. [www.cdc.org.sv](http://www.cdc.org.sv)
1.9 Laws include a ban on vertical price fixing and other supply conditions and discounts by laboratories and drug stores to retailers;

1.10 Reform the status of CSSP, disabling the participation of professionals with ties to drug companies in the drug sector, or to assign responsibility for verification of medicines at a different institution of CSSP.

44. The institutional position of the Board of Directors derives from on The Constitution and the Universal Declarations of Human Right. Its starting point is the consideration that health is a fundamental human right, and medications are necessary to satisfy property directly.

45. The human right to health is collected with its terms by our Salvadoran Constitution when Article 65 says:

“The health of the inhabitants of the Republic constitutes a public good. The State and people are obligated to see to its conservation and restoration.

The State shall determine the national health policy and shall control and supervise its application…”

46. Furthermore, our Salvadoran Constitution, Article 1 sets:

“(…) it is the obligation of the State to secure for the inhabitants of the Republic, the enjoyment of liberty, health, culture, economic well-being and social justice.”

47. The purpose of issuing a position on the issue of drugs was the increase competition in the sector, through the opening of that market. Although, the position contains a recommendation regulating drug prices in the sense that if the price band fixation of reference prices or maximum prices for medicines are needed to ensure access to them population, such measures can and should be applied. In addition, the position provides that measures of price regulation limit competition and thus must be exceptional, as in the case in question, based on the nature and purpose of the good or service in question, in checking their need and always restricted to the essentials. Thus, in the case of medicines, all measures of price regulation should consider the cost structure differentiated between brand name drugs and generic drugs, the conditions of competition in products, and applied to a special list of drugs national interest.

5. Competition effect on poor, small entrepreneurs and job seekers, in principle.

48. From an economic perspective, and in a context of competition, all the economics agents are rivals in the market (smalls entrepreneurs, medium and large rivals) seeking to gain more market share, trough the implementation of more efficient methods of production, innovation and improvement in the quality of products. In a competitive market will be displaced weaker rivals, i.e. those that produce inefficiencies and welfare losses in the market.

49. However, in a market without competition, from the point of view of supply, economics agents have no incentives for innovation, improved product quality, technology or investment in productive capacity. From the point of view of demand, consumers will pay higher prices and lower quality products procured by reducing their purchasing power to cover the essential goods and services. The lack of competition becomes an incentive for inefficient markets, affecting all consumers.
5.1 *Competition effect on job seekers, in principle*

50. Employment is defined, economically, for the curves of supply and demand for labor. People offer their work and it is companies that claim. Unemployment has a negative relationship with GDP (gross domestic product) (PIB for its acronym in Spanish), called *Okum Act*\(^{13}\), which says that every 2% drop in GDP, relative to potential GDP, unemployment increased by 1%.

51. The Gross Domestic Product (GDP) of a country is the result of the sum of consumption, investment, the trade balance (exports minus imports) and government consumption. The GDP and employment generation are in a positive relationship because GDP growth means increased consumption, investment, exports, government spending, which will lead to an increase in labor supply.

52. A perfectly competitive market ensure no consumer surplus and producer, working as an incentive for the demand side to consume an optimal price and quantity and the supply side, to invest in innovation, technology and disposal barriers to entry for future competitors, for example ensuring an efficient market. This is how the free market competition is an efficiency factor that favors the increase of GDP of a country, affecting, in turn, positively on employment.

53. According to Household Survey Publication Multipurpose 2011, data (EHPM) the annual growth rate of GDP was 1.5%, the national unemployment rate was 6.6%. The underemployment rate is 32.7% in the urban area.

**El Salvador: Urban PEA as employment**

![Chart showing employment rates](chart.png)


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6. **Competition’s effect on poor, small entrepreneurs and job seekers, in principle**

54. Competition results in several benefits:

   a) Reduced price: Companies set prices attractive strategies to achieve more customers consuming their goods or services.

   b) Improved quality: To oust their rivals, operators improve the quality of their products.

   c) Promoting innovation: The innovation reduces costs and maximizes the benefits of the companies, which often are transfers to consumers.

55. Under conditions of competition, anticompetitive practices impede access of new operators, e.g., in the market for white sugar in bulk, Sugar and Derivatives Distributor, SA de CV (Dizucar) conducted a discriminatory restriction on the sale of those goods; preventing market entry of new competitors. Another example in El Salvador is in the market for wheat flour, in which the anti-competitive market division by traders HARISA S A and MOLSA has caused massive bankruptcy bakeries in the country, which results in the failure of small businesses.

56. "At present the interest aroused SMEs (PYME its acronym in Spanish) at government and business and the ongoing efforts to develop them efficiently, with increased competitiveness and impact comes from the realization that SMEs are a key factor in economic development and social development. SMEs are major generators of employment and wealth in each country participating significantly in the creation of gross domestic product. Another reality is that creating a job in SMEs requires a much smaller capital investment than in large companies, thus being a sector of great social impact."

57. SMEs are expected to benefit from clear rules to compete in their respective markets, identifying niches that allow you to be more competitive against its competitors. Salvadoran MSEs representing 99.4% of all firms and generates more than 699,000 jobs. The more flexibility a company has to change its environment will be more competitive against its competitors so job seekers or poor workers would benefit from the competition that strengthens the competitiveness of SMEs.

58. In 2011 came into force the amendments to the Law on Procurement and Contracting Public Administration (LACAP its acronym in Spanish) aimed at promoting the development of micro and small enterprises (MSEs). In El Salvador, there are micro enterprises 463.803 subsistence microenterprises 158.574, 13.208 small businesses; 2.624 medium, and 772 large companies only.

59. The reform is to enable MSEs to obtain at least 12% of the annual budget for state public procurement as an incentive to increase the number of bidders in public procurement market, thereby avoiding the tender commission collusive. Similarly, the increased participation of the SMEs will allow the production of more employment opportunities for the Salvadoran population.

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14 Challenge and Opportunity of Salvadoran SMEs: building an agenda for development. FUNDE http://www.fundes.org/uploaded/content/publicacione/936703854.pdf


7. **Competition policy toward poverty**

60. The Competition Law of El Salvador aims to promote, protect and guarantee competition, by preventing and eliminating of anti-competitive practices in order to increase economic efficiency and consumer’s welfare. In that sense, the Competition Act promotes a more competitive and efficient market transparent and accessible, encouraging the dynamism and growth in benefit of the consumer. The purpose is to establish clear rules economics agents, regardless of their size; they can carry out their business in a free market.

61. In that sense, the Competition Law in El Salvador, safeguard undistorted market where all participants can have clear rules and order is the gain consumer preference. For this reason, competition policy should not make a distinction between the poor and the rest of society. As has been stated, in some cases it is necessary to intervene with subsidies and price regulations to try to reassure the poor access to essential goods and services; however, such intervention is always exceptional.

62. Competition policy aims to protect the economic efficiency, to be successful with that objective is necessary to prioritize and focus research efforts, study and detection of anticompetitive practices in the markets for basic food basket, for example, the wheat flour market, rice, sugar, oil, services such as electricity, transport and others. It should be noted that experience has shown that markets products and services of CBA have distortions in competition, thus as part of the public policy priority on reducing poverty should highlight the importance of eradicating practices anticompetitive markets goods and services of CBA as one of the key elements in combating poverty.