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COMPETITION AND COMMODITY PRICE VOLATILITY

Contribution from Ukraine

-- Session I --

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COMPETITION AND COMMODITY PRICE VOLATILITY

-- Ukraine --

1. In the recent years, considerable price hikes have taken place in the food product markets of Ukraine. First and foremost that concerned essential food products, such as sugar, dairy products, grits, meat, oil, and the like.

2. 2008-2009 saw price hikes for a number of products caused by crisis events and other reasons. By way of example, in 2009, in connection with flu epidemics in Ukraine, prices for such food products recommended by doctors for prevention of flu, as lemons and garlic, grew by more than 100%. In order to determine those "guilty" of growth in prices for lemons, the experts traced the chain from importers of those fruits to the retail chains, which sell them to the ultimate buyers. The analysts estimated that wholesale suppliers were specifically responsible for raising the prices in the *importer/wholesale suppliers/retail* chain. The Anti-Monopoly Committee of Ukraine in the period of speculative demand started investigation in relation to such price hikes for the said products. As a result, "G" LLC, one of Ukraine's largest wholesale suppliers of lemons, was fined UAH 100 thousand. The Committee found that the said company, abusing their monopoly, started unreasonably setting excessive sales mark-up of 80-300 percent for lemons, which they used to sell to supermarkets in batches. Based on the conclusions of the investigation, such behavior of wholesale suppliers became one of the root causes for growth in retail prices for lemons. In the course of examination of the case, "G" LLC lowered the release prices for lemons to the economically reasonable level and the representatives of the company publicly admitted the violation and committed to not engage in such behavior in future.

3. We should note that Ukraine introduced government regulation of prices for broad range of food products (flours, bread, macaroni foods, grits, sugar, beef meat, pork, poultry, boiled sausage products, milk, cheese, sour cream, butter, chicken eggs, and oil) and services of their wholesale and retail sales. Such regulation shall be provided in compliance with the Law of Ukraine "On the prices and pricing" and in compliance with the Cabinet of Ministers of Ukraine Resolution No. 1548 dd. 25 December 1996 "On setting of powers of executive authorities and executive bodies of city councils in relation to regulation of prices (tariff)"

4. The central executive authority in Ukraine assigned to control the pricing situation in the core socially important markets is the Ministry of Economic Development and Trade of Ukraine, which supervises the State Inspectorate for Price Control that provides ongoing monitoring of prices for socially important food product markets in retail.

5. In compliance with the Cabinet of Ministers of Ukraine Resolution No. 1222 dd. 17 October 2007 "On the approval of the Procedure of declaration of changes in wholesale and release prices for food products" wholesale and release prices set by business entities engaged in business of food production, in the event of change in prices for food products by more than 1 percent within one month shall declare such changes.

6. That being the case, a business entity shall always obtain a written conclusion of the State Inspectorate for Price Control (Derzhzhinspektsiya) that such changes are economically reasonable and

have its declaration approved with the authorized agency (the Council of Ministers of the Autonomous Republic of Crimea, regional, Kyiv and Sevastopol city state administrations).

7. We should note that the introduced government regulation of prices for food products fails to provide appropriate restraints of their unjustified growth and, not infrequently, provokes artificial growth in expenses, increase in the number of intermediaries between food producers and retailers that, in turn, results in unjustified growth in prices.

8. The price fluctuations, which took place in 2008-2011 in Ukraine and the relevant actions of the Antimonopoly Committee of Ukraine related to termination of the violations of the competition law, are best illustrated with the situation, which existed in sunflower oil market as one of the most consumed products forming part of the core diet of Ukrainian consumers.

9. The oil and fat market is one of the most promising sectors of agricultural production. Oil products are in increasingly higher demand in the world market. This, in turn is caused by re-focusing the diet to oil and fats of vegetable origin due to their physiological benefits and more affordable prices in comparison with animal fats and dynamic growth in production of biodiesel fuel in the world based on oil against the background of progressing growth in prices for mineral energy resources and reduction in their natural reserves.

10. Ukraine's share in the world market of oil production (all oil types) in 2010/2011 was more than 21%, i.e. second only to the EU countries. The dominant consumers of oil in the world market include the EU, countries of Near East, North America and the CIS.

11. A comparative analysis of retail prices for sunflower oil in the 2011's Ukraine and other countries of the world demonstrated that the prices are generally lower than in the surveyed countries (1.3 USD/liter in Ukraine, 1.4 USD/liter in Russia, 3.1 USD/liter in France, 2.25 USD/liter in Argentina, and 4.6 USD/liter in Turkey).

12. The domestic market demand for sunflower oil is met completely. The consumption in the domestic sunflower oil market remains nearly the same and amounts to nearly 400 thousand tons of oil a year. In accordance with the Ministry of Health requirements, the level of sunflower oil consumption per person a year is 13 kg.

13. The total consumption includes oil consumed directly as commodity by ultimate consumers (population) via the retail and oil used as a raw material for manufacture of other food products (mayonnaise, margarine products, bread and bakery products, confectionary products, and the like). In the recent 10 years domestic consumption has never exceeded 20% of the total sunflower oil production in Ukraine. The rest of the produced sunflower oil (over 80%) is exported from Ukraine. In other words, a conclusion may be made that sunflower oil market in Ukraine is export-oriented.

14. Ukraine is a leader in export of sunflower oil (over 2.6 million ton), providing 65% of the global exports to 63 countries of the world. No considerable fluctuations in prices for these socially important products take place in the world; however, the ever increasing demand for oil, failures of oil-bearing crops in other countries, except for favorable factors, also adversely affect the pricing situation in Ukrainian domestic market.

15. Therefore, in the period of unfavorable climatic factors, poor harvest of sunflower seed in Russia and South America, unsatisfied demand for oil, high worldwide prices for oil in the late 2010 Ukrainian producers greatly increased export of oil. Such actions broke the demand/supply balance in domestic sunflower oil market whereby December 2010 to January 2011 retail prices for sunflower oil in Ukraine grew rapidly by more than 20 percent.

16. The recent years have also seen changes in product range of consumption by general public sunflower oil from non-refined loose sunflower oil to refined packaged (bottled) sunflower oil and, therefore, the AMCU in their investigation defined this market segment as a separate refined bottled sunflower oil market.

17. Of more than 40 oil extraction plants operating in Ukraine, 25 largest ones produce more than 90% of total sunflower oil and most sunflower seed processing capacities (nearly 75%) are owned by 15 companies, which have material impact on market formation, its pricing and export policy.

18. In 2009-2010, the main participants in refined bottled sunflower oil market were "S" Subsidiary Company with Foreign Investment (*foreign investment*), "K" LLC, and "P" CJSC. The total share of those three largest market participants until spring 2011 was 60% and, whereas the shares of other market participants are considerably lower and marginal, refined bottled sunflower oil market structure can be defined as oligopoly.

19. "S" Subsidiary Company with Foreign Investment supplies refined sunflower oil under own trademarks "OK", "OV", "OI" packaged in plastic bottles in the range from 0.5 liter to 5 liter, has extensive distribution system operating throughout the territory of Ukraine. "S" Subsidiary Company with Foreign Investment once started producing sunflower oil under social brand "R" to support socially vulnerable population groups.

20. "K" LLC via extensive distribution system sells oil trademarked "SchD", "S", "ChD", "ChZ", "L", Private Label "P" for FOZZY GRUP corporation and Natura Verde, store chain of METRO Cash and Carry Ukraine LLC, and produces sunflower oil under social brand "G".

21. We should note that another company, which fills oil in considerable volumes, "KG" PJSC became one of the leaders in 2010/2011 marketing year.

22. The AMCU provides ongoing monitoring of changes in pricing situation in that market and operation of the main participants of the market.

23. Such monitoring has become the subject of price investigation the AMCU in sunflower oil market. A number of actions were taken based on the results of the completed investigation, in particular:

24. In 2008, the Committee examined a case on violation of the law on protection of economic competition by business entities operating in the sunflower oil market, on the fact of fast and considerable growth in prices for sunflower oil. In the period from the late July to mid-October 2007, the average weighted prices in Ukraine for vegetable sunflower oil grew by virtually 60 percent. The revealed circumstances demonstrated existence of collective monopoly in the sunflower oil market and behavior of those business entities dominating the market showed elements of abuse of monopoly (dominant position). Based on the findings of the case examination, the acts of "S" Subsidiary Company, "K" LLC, which included unjustified increase in wholesale and release prices for sunflower oil in July–August 2007, were recognized as abuse of monopoly (dominance). "K" LLC and "S" Subsidiary Company admitted the violation and paid a fine in the amount of UAH 2,000 thousand. In pursuance of the Committee's recommendations, the said companies lowered the wholesale release prices for oil by 10-15 percent.

25. In future, with a view to preventing steep unjustified growth in prices for sunflower oil and destabilization of the situation in the entire market, the AMCU, upon review of the materials provided by the State Inspectorate for Price Control, in the event of market trend towards gradual growth in retail prices for sunflower oil in case of lowering or stable purchase prices for sunflower seed, made recommendations, which their addresses are bound to consider, in relation to prevention of unjustified increase in prices.

26. In **November 2008**, in order to prevent violations of the law on protection of economic competition by the Committee were provided **recommendations to be considered** by "S" Subsidiary Company with Foreign Investment, "K" LLC and "P" CJSC to take action in relation to lowering the wholesale release prices for sunflower oil to the appropriate level stipulated by the purchase prices for sunflower seed.

27. In order to prevent violations of the law on protection of economic competition **in 2009** one of the AMCU's regional territorial departments provided recommendations to 2 business entities, which operated in sunflower oil sale (distribution) services market in relation to prevention of unjustified increase in prices for oil in the region, which they complied with.

28. In **2010**, another territorial department of the AMCU provided recommendations to a state-owned enterprise with foreign investment in relation to taking action to remove consequences of actions of using and dissemination of information, in particular, in advertisements and labels of sunflower oil bottles under trademarks "Oleyna" with a note "Oleyna is a cholesterol-free oil", which showed elements of the violation qualified under Article 15¹ of the Law of Ukraine "On the protection from unfair competition" that is to say: dissemination of misleading information, in the form of communication by a business entity to undefined group of parties by means of advertising incomplete and inaccurate information, which would affect the intent of such parties in relation to purchasing the products of such business entity. The recommendations so given were observed.

29. In **2010**, with a view to preventing the adverse pricing situation in the sunflower oil market, the AMCU gave "S" Subsidiary Company with Foreign Investment and "K" LLC recommendations (which the addressees are bound to consider) to take action in relation to refraining from unjustified increase in prices for sunflower oil of the most common trademarks of the social brand. These recommendations were provided in pursuance of the requirements laid down in the instruction of the First Deputy Prime Minister of Ukraine dd. 27 August 2010 in relation to unconditional compliance with the Government's resolutions on the matters related to food products supply to general public at affordable prices and stable functioning of the food market.

30. In **January 2011**, the AMCU examined the case based on the elements of the violation by 3 dominant suppliers of sunflower oil in Ukrainian retail by abuse of dominance in the sunflower oil market by setting the product sale prices, which would have been unable to set if considerable competition had existed in the market. Based on the results of analysis of information obtained in the course of examination of the case, defendants were found to have no sufficient economic grounds for simultaneous significant increase in wholesale sale prices for bottled (packaged) sunflower oil from September 2010 to January 2011. One of the reasons, which would give rise to such synchronous growth in the said prices, is unjustified setting of prices for sunflower oil dominant suppliers oil in the retail chain.

31. Under such conditions, in the course of examination of the case with a view to increasing supply in Ukrainian domestic market, the AMCU permitted 14 business entities to take a concerted action in the form of *Concerted Competitive Behavior Agreement* between the said business entities in sunflower oil market for 3 months. The subject was making of the agreement in compliance with the Concerted Action Memorandum between the Cabinet of Ministers of Ukraine and major companies operating in oil and fat market in relation to prevention of growth in prices for sunflower oil in domestic market. The expiry date of the agreement is 15 May 2011. The sunflower oil producers have undertaken to draft the action plan in relation to stabilization of prices for bottled sunflower oil in domestic market. Within the framework of the Memorandum, the producers have also undertaken to ensure stable and uninterrupted supply of oil to the domestic market and to avoid shrinking of production and supply of oil in the domestic market. In turn, the Cabinet of Ministers of Ukraine promised the producers to facilitate provision of stable situation in the oil and fat product market and introduce no export quotas for sunflower oil.

32. As the share of concerted actors in the nation-wide sunflower oil market far exceeded 35 percent and the said concerted action in compliance with Ukrainian legislation are related to setting of prices and other terms for purchase or sales of products, limitation of production, markets, distribution of markets, they might result in restraint of competition in the nation-wide sunflower oil market. In other words, such actions show a potential of restriction. That being said, they would be allowed subject to availability of the relevant terms and conditions, such as improvement of product sales and rationalization of production.

33. The concerted actors provided rationale for positive impact of their actions, which will facilitate a socially significant effect that domestic prices for oil in Ukrainian consumer market stabilize and total product supply to the domestic market will become higher.

34. As a result of taking the said action, Ukrainian markets saw more business entities, which sold sunflower oil in domestic market whereby the oil sales in domestic market grew and the prices for packaged oil reduced. As the permit for such concerted action was given only for 3 months (until 15 May 2011), they resulted in no durable change in the commodity market structure and, hence, significant restraint of competition in that market.

35. Therefore, the activities of the Anti-Monopoly Committee not only facilitated stabilization of the situation in oil market and increase of supply and entry of other oil producers to the domestic market.

36. The violations of the law on protection of economic competition in sunflower oil market were terminated in a total of 7 cases in 2008-2011 (2 in nation-wide markets) with recommendations given to 8 business entities. In 7 cases, the subject was sunflower oil price hikes.

37. Among the seven violations detected and terminated in that market, 3 were qualified as abuse of monopoly, 1 as anti-competitive concerted action, 2 as unfair competition, and 1 as failure to furnish information on request of the AMCU.