

ABSTRACT

Competition Policy in Sri Lanka

by

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In 1989, the Sri Lanka's Ministry of Industries prepared an important statement of industrialization policy calling for export-led growth along lines of Sri Lanka's comparative advantage. This report recommends that a competition policy suitable for supporting this goal would embody six objectives:

- (1) broad-based economic efficiency;
- (2) anti-monopsony;
- (3) social justice *cum* employment creation;
- (4) efficiency via economies of scale;
- (5) creating international competitiveness; and
- (6) maintaining a business climate congenial to multinational corporations.

The report recommends that Sri Lanka's Fair Trading Commission be upgraded to a National Competition Council with presidentially-appointed members. The Council would be charged with promoting domestic competition and with enhancing Sri Lanka's competitiveness in the world economy.

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COMPETITION POLICY IN SRI LANKA

A report presented to
the Industrialization Commission of Sri Lanka

by

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1. Introduction; organization of the report

This report is the outcome of a study conducted in Colombo during the month of September 1991, pursuant to a request from the Industrialization Commission of Sri Lanka to the U.S. Agency for International Development. The writer, an economist and Institute Fellow of the Harvard Institute for International Development, has previously served as advisor to the governments of Kenya and Morocco on design of competition policy, preparation of enabling legislation and establishment of implementing machinery. During his stay in Sri Lanka he interviewed managers of more than 16 enterprises in nine industrial and service sectors¹ and met with senior personnel of 11 public and private agencies.

The document is organized as follows: following a brief summary of conclusions, section 3 presents the main body of the report. It begins with a review of the statutory objectives for competition policy as set forth in the Fair Trading Commission Act of 1987, and offers a revised set of objectives which the writer considers more attuned to the Ministry of Industries' December 1989 industrialization strategy paper. The section then discusses the current role of the Fair Trading Commission in defining and implementing competition policy in Sri Lanka, examining one case recently considered by the FTC and another one currently before it in order to highlight issues which it is felt should weigh heavily in the Commission's deliberations.

A following subsection relates the Sri Lankan context to the evolution of competition policy in other countries, identifying tasks that cannot be addressed efficiently without some machinery for implementing such policy. A special subsection cites evidence from South Korea, where competition policy is coming increasingly to the fore. The section then considers options for reform of the FTC. A proposal is presented for transforming it into a Presidentially-appointed National Competition Commission. Section 3 concludes by citing the need to equip the FTC, whether or not reorganized, with investigative resources, and proposing the use of senior lecturers in management as part-time consultants.

The final section, 4, distills additional observations on competition and competition policy in Sri Lanka from the writer's interviews and analysis.

A series of seven appendices lists the industrial branches, companies and agencies where the writer conducted most of his interviews; summarizes the competition policy cases before the FTC during the period 1989-September 1991; summarizes five recent cases of acquisition of enterprises listed on the Colombo Stock Exchange; tabulates the caseload of agencies in India and South Korea that correspond to Sri Lanka's FTC; compares the extent of oligopoly in industrial branches of the U.S. and Morocco; and describes a procedure by which the FTC could exploit its current role in authorizing pharmaceutical prices to circulate comparative price information and enhance competition in the market.

¹ Not counting a group of manufacturers of exercise books whom the writer met jointly at the Ministry of Industries.

2. Executive summary

The objectives for competition policy set forth in the Fair Trading Commission Act of 1987 have been overtaken by the recent evolution of Sri Lanka's industrialization policy. The report proposes a consolidated list of six objectives to accord with current industrialization policy: broad-based economic efficiency, anti-monopsony, social justice *cum* employment creation, efficiency via economies of scale, creating international competitiveness, and maintaining a business climate congenial to multinational corporations.

Designing a competition policy that maximizes social goals involves recognition of the multiple trade-offs among these objectives. For example, concentration of market power can be tolerated, even encouraged where it will serve to strengthen export performance, but it should be resisted in branches where export prospects are minimal. The agency charged with implementing competition policy should have authority to negotiate and monitor export targets as a precondition not only for permitting takeovers, but even for allowing dominant firms in some markets to retain their existing shares.

The Fair Trading Commission has fortunately been liberated from an earlier focus on price controls, but as presently organized it cannot be expected to move much beyond policing the more blatant anti-competitive practices. Its intervention thus far in the field of economic concentration has overlooked the export dimension. The report examines two recent cases of economic concentration coming before the FTC, namely the soap and electrical cable industries, where capability and/or willingness to export should have been or should be a key consideration.

Sri Lanka does not need a competition enforcement agency with a confrontational approach that disrupts the segment of the capital market where companies are acquired and disposed of, or threatens to break up any company that leads its market because it is efficient. At the same time, any modern economy should be equipped to deal with anti-competitive practices, just as any state protects its citizenry against armed robbery. Attention is called to the example of South Korea, which found it desirable to introduce competition policy and gradually add teeth to it as a means of rectifying social and economic imbalances that crept in while the state promoted exports by facilitating market concentration.

Moreover there are categories of untraded goods and services where price control is the only alternative to maintaining competition in order to keep prices near marginal cost. The option of abolishing the FTC and doing without any machinery to implement competition policy is therefore not recommended.

Instead, the report proposes the FTC's transformation into a Presidentially-appointed National Competition Council (NCC) that would make competitiveness and enhancement of competition central foci of development policy and have the political clout to promote them in dealing with powerful economic agents.

The need is also cited to endow the FTC/NCC with investigative resources capable of analyzing product markets to assess the probable impact of permitting or forestalling concentration. Sri Lanka's current fiscal constraints appear to rule out hiring qualified staff on a full-time basis. The alternative of contracting for industry studies with senior lecturers of the University of Sri Jayewardenepura's Management Faculty and Post-Graduate Institute of Management is proposed, and the hope is expressed that foreign aid would be forthcoming to finance this for, say, three years on an experimental basis.

3. Competition Policy in Sri Lanka

Taking note of Sri Lanka's Fair Trading Commission (FTC) Act of 1987, as amended by the Industrial Promotion Act of 1990, together with the operation of the FTC under those acts, the Industrialization Commission has asked itself whether and, if so, how the FTC Act and the operation of competition policy in Sri Lanka should evolve so as best to promote the objectives of industrialization strategy as set forth in the government's current policy statement².

As in so many areas of policy formulation, governments that take seriously the issue of competition as it operates both among domestic firms and between domestic and foreign producers find themselves pursuing a set of partly contradictory objectives. Determination of competition policy consists of establishing trade-offs among these objectives, and the principal goal of this report is to analyze these trade-offs in the case of Sri Lanka and seek an optimal course of action in light of national objectives.

Goals of the 1987 FTC Act revisited

The original FTC Act requires the Commission to "have special regard" to eight "matters"³:

- (a) the protection of the interests of consumers of articles;
- (b) the provision of necessary incentives to producers of articles;
- (c) the necessity for ensuring reasonable rates of return on capital employed in the production of articles or the provision of services;
- (d) the allocation of resources among different sectors of the economy of the country;
- (e) the efficient operation of public corporations engaged in the production of articles or the provision of services or in any activity connected with or incidental to the production of articles or the provision of services;
- (f) the control of inflation;
- (g) other objectives of economic and social policy of the Government; and
- (h) guidelines that may from time to time be given by the Minister.

Disregarding (g) and (h) as catch-all and (d) as not embodying any normative concept--it doesn't even specify that resource allocation should be efficient--we are left with five considerations that can be regarded as objectives. In effect, the FTC is to protect consumer interests; safeguard producer incentives, including assurance of an adequate rate of return on capital; pay special heed to efficient operation of state enterprises; and control inflation.

² A Strategy for Industrialisation in Sri Lanka. Ministry of Industries, Colombo, December 15, 1989.

³ Fair Trading Commission Act, No. 1 of 1987, Part II. section 6, page 2.

A striking characteristic of these statutory objectives is their virtual irrelevance to competition policy, which is not only not the sole instrument of state policy for meeting the five objectives, but for only one of the objectives--arguably that of protecting consumer interests--is it even a major policy instrument. Clearly at the time the FTC Act was drafted the traditional goals of price control, to which the FTC devoted most of its resources until enactment of the Industrial Promotion Act of 1990, were uppermost in the minds of the draftsmen.

For safeguarding producer incentives and controlling inflation, macroeconomic policy, i.e. fiscal and monetary policy--including exchange rate determination--and foreign trade policy, is a much more powerful tool than either competition policy or price control. The impact of macroeconomic policy on consumer interests is also undeniable. Efficiency of state enterprises is a separate issue; in any case implementation of almost any kind of competition policy tends to drive more public corporations out of business than the number who are pushed towards efficiency.

A subsequent section of the FTC Act requiring the Commission to determine whether a given monopoly or merger situation or anti-competitive practice operates or is likely to operate "against the public interest", adds a set of objectives more relevant to competition policy:

- (i) maintaining and promoting effective competition between persons supplying goods and services;
- (ii) promoting the interests of consumers, purchasers and other users of goods and services in respect of the price and quality of such goods and services and the variety of goods and services supplied;
- (iii) promoting through competition the reduction of costs, the development and use of new techniques and products and facilitating the entry of new competitors into existing markets;
- (iv) maintaining and promoting balanced distribution of industrial activity and employment; and
- (v) maintaining and promoting competitive activity in export markets.

Objectives of competition policy suited to Sri Lanka's current industrialization effort

The thrust of industrialization policy as described in the Ministry of Industries' 1989 statement, prepared some three years after the FTC Act, is different from the foregoing. The Ministry statement calls for export-led growth along lines of Sri Lanka's comparative advantage. In the writer's view, a competition policy suitable for supporting this goal would embody the following six objectives (the order given does not necessarily reflect priorities among objectives):

1. **Broad-based economic efficiency:** by enhancing competition among domestic producers in a given branch, to oblige some or all of them to reduce unit costs, offer their

products to domestic consumers at lower prices, and in the process become more competitive on the world market, both in exporting and competing with imports.

2. **Anti-monopsony:** by enhancing competition among domestic producers in their purchase of domestic inputs, to oblige them to offer 'fair' prices to local suppliers, especially farmers and small-scale subcontractors.

3. **Social justice *cum* employment creation:** to prevent large producers from abusing their market power to destroy or hamper the growth of efficient smaller enterprises and creation of employment in the latter, with their customarily greater use of labor per unit of investment.

4. **Efficiency via economies of scale:** in branches where efficiencies attainable via economies of scale outweigh those attainable through competition: among multiple producers, to allow one or more of these to attain sufficient size to exploit the economies of scale, even if the number of viable producers is thereby reduced.

5. **Creating international competitiveness:** to facilitate the formation of producing and/or trading units with sufficient economic power to absorb the overhead costs of breaking into new markets, including both export markets and domestic markets hitherto dominated by imports.

6. **Maintaining a business climate congenial to multinational corporations (MNCs):** to avoid overly zealous enforcement of competition policy against foreign investors, thereby running the risk of antagonizing and scaring them off. (This objective is more likely to characterize the strategy of implementation of competition policy than to figure as an explicit goal.)

Contraction of the FTC's price control role

Prior to passage of the Industrial Promotion Act (IPA) of 1990, the Fair Trading Commission had price control authority over 47 commodities or commodity categories. Four of these, whose prices were actually set by the FTC, were 'essential' consumer items referred to the Commission by the Director of Internal Trade, doubling as the Controller of Prices⁴. With the remaining 43 items, prescribed by the Minister of Trade on the ground of market dominance by producers, control of prices was exercised by requiring that manufacturers obtain the FTC's authorization for price increases.

Like their counterparts in a growing list of countries, Sri Lanka's industrial policymakers concluded that price control, rather than protecting consumer interests, was discouraging investment and entrepreneurial initiative, retarding growth and threatening to

⁴ The items in question are wheat flour, bread, pharmaceuticals, and imported hoes (known as 'mammothies' in Sri Lanka).

make consumers ultimately worse off. Accordingly the IPA rescinded the nine sections of the FTC Act relating to price control, substituting two new provisions:

(i) a new section 18 of the FTC Act, authorizing the Controller of Prices to ask the FTC to control prices of food items or pharmaceuticals in cases of 'unreasonable' increases or 'excessive' prices; and

(ii) section 23 of the IPA Act, authorizing the FTC to review the price of any article and, to the extent considered necessary to combat 'unreasonable' prices, recommend that importation of the article be allowed at a customs tariff rate recommended by the FTC.

As of September 1991 the only food items subject to price control were wheat flour and bread. Conversely all pharmaceutical products were subject to price control, and a considerable share of the FTC's staff resources were devoted to applying mark-up formulae to cost data submitted almost daily by local manufacturers and importers of the nearly 2,000 items authorized for distribution in Sri Lanka. The remaining 43 products/categories were in effect 'deprescribed' by the IPA.

In the first half of 1991 the FTC reviewed price increases during 1990 for four groups of products under section 23 of the 1990 Act, requesting six firms to submit data and attend a hearing. After inquiry the Commission decided that none of the instances constituted "gross abuse in pricing", and therefore recommended no reductions in import duties⁵.

The FTC and competition policy: anti-competitive practices

Appendix B, a summary of competition policy cases coming before the FTC, shows the Commission dealing with six cases of alleged anti-competitive practices (ACP) during 1989-September 1991. According to a March 1991 memorandum of the Ministry of Trade and Commerce, "in spite of publicity given, the practices which have been reported do not include major anti-competitive practices normally found in trading". The ministry therefore proposed that the FTC Act be amended "to specifically prohibit...better known and internationally accepted anti-competitive practices", namely:

- “(a) Exclusive supply dealing arrangements
- (b) Exclusive purchasing contracts
- (c) Long term supply contracts
- (d) Restrictive terms
- (e) Selective distribution system
- (f) Tie-ins
- (g) Restrictions on the supply of parts or other inputs required by competitors
- (h) Restrictive licensing policies.”

⁵ FTC, "Report on Inquiry held by the Fair Trading Commission under Section 23 of the Industrial Promotion Act", 21st May 1991.

The FTC and competition policy: economic concentration

Appendix B shows the FTC having thus far concluded four inquiries into 'monopoly situations', with another three cases pending as of September 1991. A number of interviewees expressed the view that this area offers the greatest potential for acts by the FTC--of omission as well as commission--running counter to the nation's industrialization objectives.

For example, the FTC Act would give the Commission authority to move against producers who join forces for the purpose of exporting their products. Formation of a single trading company to market abroad products that compete on the Sri Lanka market could be viewed as a "monopoly situation" subject to regulation. Current FTC management has disavowed any intent to interfere with such initiatives, but if one were redrafting the FTC Act today one would probably exempt them outright, as do industrial countries that pursue active competition policies.

Economic concentration and export performance. In its monopoly inquiries thus far the FTC has paid little or no attention to the export dimension. In the writer's view this dimension ought to have been considered in the FTC's review of the soap industry, since on the one hand several small producers have exported modest quantities in the past and are actively exploring export markets, while on the other hand the market leader, Lever Brothers (LB), will not export in competition with Unilever subsidiaries in other countries, and most potential importers of Sri Lankan soap products are host to such subsidiaries.⁶

Soap is not a high-technology industry, and it seems clear that economies of scale, though by no means overwhelming, are sufficiently important, and unit profit margins sufficiently low, that soap manufacturers confined to small shares of the Sri Lankan market by LB's dominance will lack an economic basis for breaking into export markets.

The writer heard much praise expressed for LB's industrial performance, even by competitors who claimed it was not guiltless of anti-competitive practices (though even here the complaints were muted). Several competitors' comments were tantamount to an admission that the Sri Lankan consumer would be paying more for a lower-quality product had it not been for LB.

On the other hand it can reasonably be argued that LB would do a greater service to Sri Lanka at this point by gradually ceding the soap market to local enterprises and moving on to higher-technology products. The writer was informed that high-level discussions have already taken place with Unilever concerning the possibility of LB (Ceylon) moving into the bio-

⁶ This statement should be qualified insofar as company policy would allow a unit in Country A to sell to an importer in Country B, where B also has a Unilever subsidiary, after clearing the sale with the latter. But in practice this happens rarely if at all, and LB (Ceylon) does not include exports in its corporate planning.

technology field. Other areas mentioned as suitable LB targets were processed foods, and petroleum-based powder for washing machines--at present another enterprise imports the powder, then perfumes and packs it.

None of these observations imply a recommendation by this writer that the government should compel LB to divest itself of existing assets or even refrain from further investment in soap production. One of the six objectives proposed above for competition policy is to maintain a business climate congenial to foreign investment. The writer is in no position to assess what harm "bashing" LB over its role in the soap market might do *vis-à-vis* negotiations with other multinationals.

However it is the writer's view that the FTC is not doing justice to the public interest ramifications of LB's dominance of the soap industry when it fails to raise the foregoing points and suggest that high government authorities should at the very least consider ways of diminishing LB's dominance in a low-technology sector where it bars itself from exporting and where local firms are ready to assume a greater role.

The export dimension should also figure in the FTC's consideration of some of its current merger/takeover cases. In the processed meats case, Keells Food Products already exports, through agents, about 2% of its output to the Maldives, and reports it is taking steps to develop Middle Eastern markets.⁷ Ceylon Cold Stores has not yet exported meat products. Its acquisition by Keells could open up a channel for CCS products to be exported.

Export potential is more doubtful in the hostile takeover move against Kelani Cables (KC) by the management of Alucop Cables and associates. (Appendix C gives existing market shares for three categories of products fabricated domestically, deducing the market concentration in the event the takeover succeeds.)

The writer interviewed principals of Kelani and Alucop. Alucop management claimed they were making losses on PVC cable, and expressed the view that Kelani and Associated Cables were using more profitable products to cross-subsidize their output of the product. Kelani expressed the view that a prime object of Alucop in the alleged takeover was to be able to limit production and raise prices.

Kelani has already exported small quantities of copper wire bars, coiled strips and enamelled wire. In 1990 all its exports were to the Maldives, totalling about Rs.89,000⁸,

⁷ Customs' External Trade Statistics - 1990 gives a figure of Rs.2.8 million for exports of sausages and related meat products, over 99% of it to the Maldives. The Export Development Board's computer file attributes 90% of this to 16 trading companies (75% to just two companies). Keells Food Products' 1990/91 annual report refers (page 3) to "our supplies to tourist resorts in the Maldivian Islands". According to the same report, KFP's 1990 turnover was Rs.124 million.

⁸ According to EDB data and Customs' 1990 External Trade Statistics.

roughly one-tenth of one per cent of output (this excludes indirect export of enamelled wire by way of supplying a GCEC transformer manufacturer). Management said exports cover marginal cost but make little or no contribution to overheads. Kelani recently purchased a machine for making enamelled wire with 50% reduction of import duty against a commitment to export 50% of the machine's output. This is proving tougher than expected so Kelani is requesting a grace period to develop export markets plus three more years to reach the 50% target.

Conversely Alucop sees no export prospects (and its 1990 exports were zero). Management describes the challenge as being rather to hold part of the domestic market against imports, notably from China, while retaining the current 50% import duty. It sees electrical cable manufacture as not sufficiently labor-intensive to cater to Sri Lanka's comparative advantage.

Kelani partially agrees with this, claiming that 65% of product value represents raw materials, mainly imported. The PDP Consultants' May 1990 report to the Ministry of Finance, "Implementational Aspects of a 4-Band Tariff System for Sri Lanka"--hereinafter the PDP 1990 report--assesses the effective protection coefficient for PVC cable at 3.96, based on 1985 cost data, as against 1.0 representing ability to compete internationally.

It is not this writer's intention to prejudge acquisition cases now before the FTC. The cases have many ramifications which cannot be properly evaluated on the basis of a few interviews. However once again the writer believes that the FTC's deliberations will not be complete unless it evaluates the likelihood that a proposed acquisition would result in a producing and marketing unit with significantly greater export potential than the existing separate units. If this appears unlikely, then the classical disadvantages of diminished competition in the domestic market should be given full weight.

In the electrical cables case, accounts given to the writer about previous steps taken by cable manufacturers to fix prices suggests that, the smaller the number of competitors, the more likely this is to happen and the more difficult it will be to counter.

An international perspective on Sri Lankan competition policy

The Kelani-Alucop case raises the general issue as to whether traditional 'anti-trust' policy has a useful role to play in Sri Lanka. In many countries there are proponents of the free-market approach who regard much of competition policy as implemented by fair trading commissions and analogous agencies as an interference with the market which tends on balance to stifle initiative and inhibit economic progress. Better, they say, to reduce trade barriers and ensure import competition, actual or potential, against any move by producers with strong market power to raise prices above c.i.f. import levels, or ensure export outlets for suppliers whose selling prices monopsonists or oligopsonists seek to depress below f.o.b. export levels. (It is in this spirit that section 23 of Sri Lanka's Industrial Promotion Act was enacted.)

Belief in the efficacy of free markets also extends to that portion of the capital market featuring the buying and selling of controlling shares in companies. At any given time in a market economy some enterprises are on the ascendancy, through aggressive management and exploitation of new technology, while others are stagnant or on the decline as a result of weak management and/or antiquated plant and technology. Using scarce resources to extend the lives of doomed enterprises retards economic growth, and one means of orderly exit is for progressive units to acquire the assets and goodwill of declining ones. A key issue of competition policy in any country is: under what circumstances does the public interest militate against allowing such acquisition?

International consensus on controlling restrictive business practices. There is a broad consensus in industrial countries that, regardless of what policies one adopts in respect of permitting or controlling concentrations of market power, abuses of such power in the form of restrictive business practices (RBP) should be prohibited and punished, in some cases as criminal offenses. All these countries treat it as a matter of public policy that individuals and associations of individuals engaged in business enterprise should be free to purchase, produce and sell goods and services of their choice, in the desired amounts, under the most favorable conditions obtainable, subject only to safeguards imposed by law to protect specific public interests. As regards the most blatant RBP, there is no more support for tolerating them than there is for saying society should turn a blind eye to armed robbery.

For purposes of comparison between the volume of cases transacted by Sri Lanka's FTC and the corresponding agencies in a neighboring country, Appendix D tabulates the cases dealt with in 1985 by the Department of Company Affairs in India's Ministry of Industry and its Monopolies and Restrictive Trade Practices (MRTP) Commission, established already in 1969. A total of 231 references were received or enquiries instituted under the monopolistic-restrictive-unfair trade practices sections of the MRTP Act. Given that India's population is about 50 times that of Sri Lanka, an equi-proportional volume of ACP business for the FTC would have comprised merely four cases!

It is widely asserted that the pendulum of anti-RBP enforcement in the U.S. and other industrial countries has recently swung back towards greater tolerance of behavior that was formerly treated as anti-competitive. This applies particularly to vertical integration, where suppliers of certain types of products, notably consumer durables whose manufacturers have an interest in ensuring effective after-sale service, are allowed these days to engage in formerly prohibited practices such as picking and choosing their outlets and maintaining minimum resale prices. Nevertheless, tolerance of such practices is limited to situations where the presence of competing brands allows purchasers a reasonable amount of choice.

Control of mergers and acquisitions. Most industrial countries also adhere to the doctrine that, absent significant economies of scale in production or marketing, the more operators in a given branch the better. This is not only to maximize competition and consumer choice, but also to decentralize economic decisionmaking by diffusing the responsibility, burdens and rewards of management among as many people as possible. At

the same time most authorities will not interfere with moves toward economic concentration until a certain threshold is passed.

Several countries have adopted a percentage share of the domestic market as such a threshold--e.g. 25, 33 or 40%. A knotty problem that presents itself in enforcing such a rule is that of delimiting the market in terms of both geography and product specification--i.e. what products to regard as close substitutes for those comprising the focus of an inquiry. Partly to finesse this issue the U.S. applies a somewhat more sophisticated test: namely, any merger or takeover that government economists estimate will enable the combined unit to charge a 5% (under some conditions, 10%) higher price during at least 12 months is treated as anticompetitive and will normally be disapproved.⁹

In a small, low-income country the number of enterprises that the domestic market can support in any industry beyond the handicraft stage will necessarily be limited. Comparing Sri Lanka with Australia, for example, the populations are of equal size according to the IBRD's *World Development Report 1991*¹⁰, yet Sri Lanka's measured GDP is only 3% of Australia's. Depending on how narrowly markets are defined, many Sri Lankan industries come across as highly concentrated compared to their counterparts in Australia, let alone the U.S.¹¹ Yet one would not recommend that Sri Lanka's Fair Trading Commission wield its authority under section 15.1.c of the FTC Act to break up the dominant firms in all these industries.

Increasing the exposure of domestic producers to competition from imports will not directly affect prices of goods and services whose domestic production costs are lower than import parity. This applies to goods with a high weight/value ratio that makes shipping costly, e.g. many construction materials; it applies to goods of which Sri Lanka is already a competitive exporter; and it applies to services such as domestic transport and communications, finance, and insurance.

In these cases, if one wants to protect consumer interests by ensuring that prices do not

⁹ During 1982-86 over 7,700 mergers were reported to the U.S. Federal Trade Commission and Department of Justice, under a 'Pre-Merger Notification' law requiring that a firm with assets or sales exceeding \$100 million give advance notice of any acquisition of assets exceeding \$15 million. Litigation occurred in only 56 cases, with the government succeeding in blocking nearly all the contested mergers. Data are not available on the breakdown of the remaining cases between (i) those where the government made no objection, and (ii) those where government concerns were accommodated by, for example, sale of one or more company divisions to third parties. See S.C. Salop, "Symposium on Mergers and Antitrust", *Journal of Economic Perspectives* 1 (Fall): page 4.

¹⁰ Pages 204-5.

¹¹ The present writer once quantified this comparison between the United States and Morocco, a country of 46% more population than Sri Lanka and double its per capita GNP (data from IBRD, *World Development Report 1991*, op. cit.) See Appendix F.

exceed marginal cost for long, the only alternative to promoting competition in the domestic market is price control, with the tremendous drag it exerts on production and distribution. The writer found a broad consensus that the functioning of a Fair Trading Commission which keeps a minimum number of operators going--not, to be sure, at the cost of subsidizing inefficient producers--while watching over them to forestall blatant price-fixing, is a far preferable alternative to price control.

Lessons from Korean experience

To its credit, Sri Lanka is looking closely at the experience of South Korea to see what elements in that country's successful industrialization strategy might be adapted to Sri Lankan conditions. Study tours of business people and officials to Korea (and Japan) are currently being organized, *inter alia* to look at the organization and functioning of export trading companies.

During the writer's stay in Sri Lanka the FTC chairman and consulting economist attended a symposium on "Corporate Policies and Competition for Development" in Seoul, organized by UNCTAD and the Korea Development Institute, where Korean economists said their country has found competition policy to be an essential tool for rectifying imbalances arising during the industrialization push. Korea's Fair Trade law was enacted in 1980 in response to what the authorities have described as "adverse effects of the government-directed economic policy...:

- Distortion of resource allocation, particularly in the area of capital;
- Weakening of initiative and entrepreneurship in the private sector;
- Overconcentration of economic power among the nation's large conglomerates;
- Unfair trade practices by monopolistic enterprises;
- Deteriorating international competitiveness of domestic industries due to relatively high import restrictions and other protection..."¹²

Through subsequent amendments in 1986 and 1989 Korea's FTC acquired new authority to mitigate concentrations of economic power by restricting financial flows among member companies of a conglomerate and regulating mergers and acquisitions. A 1989 amendment accorded the FTC enhanced status as an independent regulatory agency, and provided harsher sanctions for many contraventions of the law.

Appendix E reproduces the Korean FTC's latest tabulation of its legal interventions during the ten years 1981-90. Slightly over half the corrective measures taken fall under the heading of unfair trade practices. The FTC intervened fairly actively in the mergers and acquisitions field, but most cases were resolved through consent actions.

In the September 1991 symposium an economist member of Korea's Fair Trade

¹² Government of Korea policy statement reproduced as UNCTAD document TD/B/RBP/42, August 1987, p. 18.

Commission concluded as follows from his country's experience¹³:

It is sometimes argued that monopoly is necessary to obtain efficiency, whereas competition tends to be wasteful in the early stage of economic development. Although the logic of this argument may not be entirely denied, it should be noted that eventually "artificial" monopoly not only hampers economic efficiency itself, but more importantly, discourages the competitive spirit of society that is the real engine of economic growth. Private monopolization by government intervention may give rise to community of interest and concomitant "government failures", which cannot be eliminated easily in a society marked by traditional communitarianism and bureaucratic authoritarianism. Competition policy or fair trade policy should therefore be assigned a foremost position in the agenda for long-run self-sustaining economic growth. Unless the general public is market-minded, market-oriented economic policy cannot succeed.

Reforming the FTC to make it equal to its task

Fulfilling the objectives proposed for the FTC in the preceding sections is a daunting task. In the first place, it must acquire the capacity to define specific product markets and then analyze them. This includes measurement of market shares, a datum that is not recorded in any government statistics. Companies devote considerable effort to measuring their shares and those of competitors, and have access to sources, notably distributors, which the bureaucracy cannot easily tap. Rough estimates of market share prepared by the FTC were challenged authoritatively by several interviewees.

As regards the analysis phase, no other permanent government agency is called upon regularly to examine such complicated issues of national industrialization strategy. The FTC should detect, document and evaluate anti-competitive practices; predict the impact on competition and prices of allowing specific mergers and takeovers; estimate the minimum scale of output necessary to achieve reasonable economies of production, i.e. evaluate industry cost functions; forecast the degree of international competitiveness associated with alternative industry structures; and maintain a business climate congenial to foreign investors.

Secondly, in order to put its findings into practice, the Commission needs sufficient 'clout' to challenge powerful business interests and negotiate arrangements that further Sri Lanka's industrialization objectives. It will need to establish, monitor and enforce conditions for allowing firm A to take over firm B--for example, that the combined unit must attain exports of Y dollars by a given year, or X% of output. Going further, the public interest might call upon it to enforce such a condition for allowing firm C to maintain a dominant share in its domestic market.

¹³ Kyu-Uck Lee, "Corporate Policies in Korea: With Special Reference to Competition Policy", paper presented to UNCTAD/KDI symposium, Seoul, September 1991, page 51.

Where restrictive business practices are concerned, the Commission must convince powerful enterprises of its capacity and intent to monitor their behavior and impose effective sanctions. For example, if company A has been allowed to acquire competitor B on condition that it not use its enhanced market power to undercut small residual competitor C, the Commission should keep an eye on the industry and be ready to act promptly if the condition is violated. Such a situation could arise in the processed meats sector if Keells Food Products' acquisition of Ceylon Cold Stores is confirmed.

In many countries state-owned enterprises are among the worst offenders against rules of fair competition. Several of the writer's interviewees claimed that Sri Lanka is no exception to this rule, and that state enterprises not uncommonly seek to impose tie-in sales. Three of the anti-competitive practice cases brought before the FTC during 1989-91 involve state enterprises. Public corporations usually have powerful defenders at high levels of government, not to mention the bureaucracy. An effective FTC must be able to challenge these agencies.

In its present form the FTC was constituted as a regulatory arm of the Ministry of Trade, replacing the National Prices Commission under the same ministry. Appointment of the FTC's seven members is entrusted to the Minister, who is supposed to choose persons of "wide experience...hav(ing) shown capacity in the field of industry, law, trade, commerce or administration." Economics is not even mentioned as an eligible field!

During the Commission's first three years the price control function consumed the bulk of its resources. In the four 'monopoly situations' it has investigated thus far, the Commission has ruled unequivocally in favor of the market-dominating enterprise--i.e. found that the enterprise was not acting against the public interest. The FTC also appears to have moved gingerly in the field of anti-competitive practices. Its 1990 annual report (see Appendix B) indicates that the FTC dropped its investigation of the imposition of a minimum tariff for containerized cargo once it learned that the Ministry of Shipping had supported the request of the Association of Container Terminal and Depot Operators to, in effect, fix the price.

To be sure, one does not want a confrontational FTC that punishes efficient firms for increasing their market share and interferes with every shift of ownership in an industry on the ground that it would increase concentration. In every sphere of regulation, there is an optimal balance between allowing the market to function--in this case the market in controlling shares of business enterprises--and forestalling practices that sooner or later impede the market.

Proposal to establish a National Competition Council. In this writer's view it would be desirable to reorganize the FTC as a **National Competition Council (NCC)**, making competition policy in its broad sense a central focus of national development policy. The FTC/NCC should be freed of its status as an appendage to a particular ministry. The option favored by the writer would be to have the members appointed and chairman designated by

the President. Moreover, if suggestions offered here for broadening the FTC/NCC's scope are eventually accepted, it would be desirable to make more than one member full-time (at present, only the chairman is full-time.)

To be sure, no change of structure can be regarded as a panacea. The NCC's effectiveness will depend on the persons appointed as members, particularly full-time members, and on the investigative resources they mobilize. A minister can appoint the same people as a president; conversely a president, acting on names submitted by his counsellors, can select persons less qualified and impartial than those formerly appointed by a minister.

However it was this observer's impression that the FTC's present status leads it to be regarded in both government and the private sector as something of a bureaucratic backwater. It does not even have direct access to the Minister for Trade, dealing instead through a Minister of State in that ministry. The Presidential Tariff Commission, whose members are appointed by the President, appears to be taken much more seriously.

Provision of investigative resources to FTC/NCC. Regardless of whether the FTC's status is modified, it cannot possibly do justice to the factors it is called upon to weigh in its deliberations unless steps are taken to give it access to more investigative resources than it now commands. Government salary scales do not enable the Commission to fill its post of chief economist with a qualified person, and at present it relies on part-time contract services of an experienced consultant, formerly an FTC member and one-time chief economist. All other economist posts are vacant. During the heyday of its price control work the Commission had as many as ten accountants, but this is now down to one or two.

The writer was persuaded that, given present fiscal constraints in Sri Lanka, it would be fruitless to call upon government to authorize a special salary scale to enable the FTC or a successor body to hire qualified economists and persons with business management training and experience. The only near-term solution appears to be that of enabling the FTC to engage part-time services of qualified consultants additional to the present economist.

The writer investigated the availability of consultants through (i) the Faculty of Management Studies and Commerce, Departments of (a) Business Administration and (b) Commerce, and (ii) the Postgraduate Institute of Management (PIM), both part of the University of Sri Jayewardenepura. He was advised that five or six senior faculty members would be available for consulting up to half-time, and some could arrange to work 2-3 months full-time if given advance notice. Consulting fees were described as being in the vicinity of Rs.1,200 per day of full-time work equivalent, or around Rs.25,000/month.

Students at the Faculty do 2-3-month internships, which the faculty is anxious to increase up to one year. Interns could help conduct market surveys as part of their course assignments. The PIM cited its new MBAs as another potential recruitment pool. These are more mature individuals, typically with five years of experience before starting the program.

Should fiscal constraints make it impossible in the near term to increase government's annual transfer to the FTC, equal to Rs.3,825,000 in 1990¹⁴ in order to finance the requisite consulting services, in the writer's view it would be worth designing a project of, say, three years' duration to seek funds from foreign technical assistance. The object would be to support the establishment of a data base in respect of the structure of Sri Lankan industries and markets, conduct *ad hoc* studies of particular industries, and demonstrate the feasibility of gathering the information largely through local consulting services. An interested foreign donor might wish to have foreign consultants also participate in a conceptual or, at the outset, supervisory role, but it should be taken into account that senior foreign consultant time costs 25-30 times as much as the local fee cited above, not counting international travel.

4. Additional findings from interviews and analysis

In the course of the writer's interviews on and analysis of the competition scene in Sri Lanka certain findings emerged which are not cited in detail in the preceding section, but which the writer regards as consistent with the conclusions and recommendations of that section. Some of these findings are presented in this concluding section.

1. Anti-competitive practices. Noting the small number of instances of purported anti-competitive practices (ACP) recorded by the Fair Trading Commission--three in the FTC's 1989 annual report, two in the 1990 report and only one new complaint thus far in 1991 (oral information)--the writer sought nearly all interviewees' impressions concerning the prevalence of such practices in Sri Lanka.

The general consensus was that many 'classical' ACPs are currently not reported to the FTC. Key reasons cited were: (i) lack of awareness in the business community of the FTC's existence and its willingness to hear and resolve complaints¹⁵; and (ii) a feeling that seeking government intervention against a competitor would provoke escalation of the 'game' and make matters worse.

Some of the specific practices cited:

- i. A manufacturer showed the writer letters from retailers of his product complaining that a competing manufacturer was trying to impose tie-in sales. The case has not been reported to the FTC.

¹⁴ Rs.3.5 million of the government grant is described as recurrent, Rs.325,000 as capital. According to the FTC's 1990 annual report, in that year an additional Rs.763,202 of income was earned in the form of fees paid by companies to have their applications for revision of price ceilings acted on by the Commission. Starting in 1991 such fees will presumably be limited to the pharmaceutical sector.

¹⁵ One interviewee suggested the FTC should consider adopting some tactics from the successful publicity campaign undertaken by the Colombo Stock Exchange.

- ii. A manufacturer complained formally to the FTC that salesmen for a market-dominating competitor were pressuring retailers to alter their counter and poster displays to favor the competitor. However the retailers were unwilling to put their complaints in writing, and the FTC ruled the case had not been proven. Subsequently the manufacturer showed the writer a letter from the competitor acknowledging that overzealous salesmen had in fact engaged in some of the practices alleged and promising corrective action. The salesmen's zeal was blamed on offending practices of a seller in an unrelated product field.
- iii. Several interviewees cited an incident involving Ceylon Tobacco Company (CTC) before the FTC was established. A multinational competitor attempted to challenge CTC's monopoly position in the Sri Lanka cigarette market. CTC is alleged to have bought up large quantities of the new entrant's product, stored it until deterioration set in, and then flooded the market. The competitor eventually withdrew.

Several managers of market-leading firms complained that competitors resorted to misleading imitations of their products and advertising in order to arouse consumer interest and increase market share. Such practices are addressed by patent and trademark laws rather than by antitrust legislation and machinery. The Department of Internal Trade frequently receives complaints from companies that their competitors are shaving approved Sri Lankan standards to reduce costs.

Notwithstanding the allegations of anti-competitive practices, the writer was impressed by the number of interviewees who described Sri Lanka as relatively free of cutthroat marketing practices reportedly widespread in other countries. Several market-dominating multinational corporations (MNCs) were described as interested in protecting their image, to the extent of welcoming competition from local firms up to a limited market share. An MNC manager cited as a major advantage of removal of price controls that local competitors were now better able to establish a foothold in the market by underselling him at prices high enough to cover their costs.

2. Price-fixing. Strong anecdotal evidence was presented that competing producers in several industries consult before raising prices. Producers in one industry are less than secretive about a monthly luncheon at a Colombo hotel. Where smaller producers stay alive by underselling the market leader, the consultation focuses on differentials to be maintained in an industry-wide price rise.

World-wide, almost all competition legislation prohibits price-fixing among competing producers or distributors--though interestingly enough, it is not included among the specific anti-competitive practices which Sri Lanka's Ministry of Trade proposed in March 1991 to list in an amendment to the FTC Act (see page 7 above). At the same time consultation about price changes is widespread and difficult to document, notwithstanding use by authorities in some countries of records of trunk telephone calls between competitors.

Price-fixing by bidders on official tenders can place a heavy burden on a government

budget, and authorities in industrial countries devote particular efforts to detecting and punishing the practice. One interviewee with an earlier background in the packaging industry cited personal experience with bid-rigging in that sector. The writer heard non-specific allegations that some public sector personnel countenance and profit from the practice.

Inter-company consultation unquestionably preceded several of the 1990 price increases reviewed by the FTC, and the Commission was not unaware of this. However consultation does not necessarily lead to prices above marginal cost, and the Commission did not find the increases in question unreasonable given cost movements. In the face of indications that producers in an industry are using a variety of tactics to wrest market share from each other, and do not hesitate to widen price differentials where it offers promise in this regard, the FTC should not be expected to devote its investigative resources to documenting instances of consultation.

3. Competition in the import sector. The writer sought observations from several interviewees as to whether market dominance among importers of significant product categories was being exploited to create situations of scarcity and inflate margins. One interviewee cited instances where importation of a given product was in effect monopolized by domestic producers of similar products, meaning that imports took place in amounts and at prices favorable to them.

Other interviewees stressed the openness of the Sri Lankan import trade, and pointed to the wide variety of imported consumer products and brands currently available in local shops. They noted that the earlier system of exchange controls and import quotas had been the greatest source of anti-competitive practices in Sri Lanka, and that liberalization had given a tremendous boost to competition.

Mention was made that imported substitutes for CTC products and matches had quickly appeared on the market on previous occasions when industrial action interrupted local production.

A manager of one company active in importing noted that the rise of the dollar *vis-à-vis* the main European currencies since January 1991 and the rupee's tendency to follow the dollar, with only a 4% devaluation over the 8-month period, had caused a significant decline in the rupee equivalent of prices stated in sterling/francs/DM (between 13 and 14.5% according to the writer's calculations based on IMF data). However, the manager went on, his company had faced no competitive pressure to reduce rupee prices of imports from Europe, and had therefore not done so. Noting the existence of a financial barrier to entry into distribution of the goods in question, the manager surmised that potential competitors had waited to assure themselves the differential would last long enough to make such a commitment worthwhile, and that competition could surface in the near future.

4. Effect on competition of uneven application of tax and other regulations. Every government faces a Herculean task in trying to ensure that its laws and regulations impact

evenly on all economic agents in a particular category. Whenever this is not the case, some agents gain a competitive advantage over others. Several businessmen complained to the writer about competitors who allegedly gained unfair advantage by underinvoicing imports or importing substandard products and were not called to account by the authorities.

The writer's attention was called to a complaint by the Ceylon Textile Manufacturers' Association (CTMA) concerning extraordinary advantages given to a Korean company which bought a state-owned textile mill and established a GCEC-approved venture, Kabool Lanka Pvt. Ltd., to manufacture fabric and garments for export. The CTMA charged that Kabool obtained the plant at a highly concessional price, and said government's permission for it to sell 20% of output as substandard in year 1 and 10% thereafter, with customs duty payable only on imported raw materials and not the value of the finished product, gave Kabool an unfair competitive advantage over non-GCEC operators.

The writer is in no position to evaluate the complaint, but with any regime of fiscal and trade concessions it is unavoidable that some established producers will regard the state as having accorded unfair competitive advantage to new investors.

APPENDIX A - AGENCIES AND BUSINESS ENTERPRISES INTERVIEWED

(Interviews conducted during the period 10-26 September, 1991)

Enterprises

Conglomerates

Aitken-Spence & Co. Ltd.

Hayleys Limited

Beverages & processed meats

Ceylon Cold Stores Ltd.

Keells Food Products Ltd. (processed meats)

Pure Beverages Co. Ltd. (beverages)

Biscuits

Maliban Biscuits Manufactories Ltd.

Electric cables

Alucop Cables Ltd.

Kelani Cables Ltd.

Exercise books

(group of manufacturers gathered at Ministry of Industries)

Market Research

Survey Research Lanka (Pvt) Ltd.

Packaging

Amico Industries (Ceylon) Ltd.

Shoes

Bata Shoe Company of Ceylon Ltd.

D. Samson Industries Ltd.

Soap etc.

Agra Chemical Industries Ltd.

Harischandra Mills Ltd.

Lever Brothers

Shiek Industries (Pvt) Ltd.

Swadeshi Industrial Works Ltd.

Agencies

Central Bank of Ceylon

Ceylon Chamber of Commerce

Colombo Stock Exchange

Export Development Board

Fair Trading Commission

Federation of Chambers of Commerce & Industry of Sri Lanka

Industrialization Commission

Ministry of Industries

Ministry of Trade & Commerce, Department of Internal Trade

Securities & Exchange Commission of Sri Lanka

University of Sri Jayewardenepura, Faculty of Management Studies & Commerce

**APPENDIX B - SUMMARY OF COMPETITION POLICY CASES BEFORE FAIR
TRADING COMMISSION DURING JANUARY 1989-SEPTEMBER 1991**

Year initiated	Classification¹⁶	Description
pre-1989	ACP	Building maintenance & janitorial services - Already before 1989 the FTC received one or more complaints alleging predatory pricing by the market leader in this sector. The investigation was "recommenced" in 1989, with the FTC publishing a notice of inquiry and inviting the public to submit evidence. In July 1989 it requested the dominant firm to supply information relevant to the investigation. The firm failed to respond, and the FTC sued to force compliance. Court proceedings were underway as of September 1991.
1989	ACP	Cigarette distribution - A retailer complained that a distributor of Ceylon Tobacco Co. (CTC) products had imposed a conditional purchase on him, i.e. supplying brand X only on condition that he purchase an equal quantity of brand Y. CTC reported the distributor had misunderstood its instructions, and the matter was settled to the complainant's satisfaction.
1989	ACP	Salt - Several retailers complained of a conditional selling practice by the Salt Corporation (supplying bulk salt on condition that 20% additional volume of packaged salt be purchased). The corporation admitted the practice but said it was in transition to new marketing arrangements, whereby from 1990 bulk salt would be sold only to "registered industries" to ensure hygiene and correct weights. The FTC report on the case concludes by referring the matter to the Commissioner of Internal Trade on the ground any ongoing offense would be "a violation of the Consumer Protection Act rather than of the FTC Act".
1989	Monop.	Toilet & laundry soap industry - The FTC published a notice of inquiry and invited evidence as to whether the monopoly situation prevailing in this industry was against the public interest. Subsequently three small competitors of Lever Brothers (Ceylon) (LB), which accounts for 70-80% of the Sri Lanka soap market, wrote alleging alleged anti-competitive practices by LB. They complained about new LB investments to increase its market share still further, and accused LB salesmen inter alia of affixing posters over those of competitors. The investigation was concluded in 1990, the FTC noting LB's dominant position but indicating there was no evidence that the firm "had operated against the "public interest"" (quotation marks in source.)
1989	Monop.	Motor car batteries - A "preliminary investigation" was initiated in 1989 and concluded in 1990. The FTC's finding was identical to that in the Lever Brothers case.
1989	Monop.	Aluminium foil & lining - Focus of this investigation was Acme Aluminium Co., with a market share exceeding 80%. FTC finding identical to car battery case.

¹⁶ As classified by FTC: ACP = anti-competitive practice, Monop. = monopoly situation.

- 1989 Monop. **Glass bottles** - The Sri Lanka Pharmaceuticals Assoc. complained that Ceylon Glass Co. (CGC), with a dominant position in the market, was responsible for a shortage of glass bottles. The complaint also cited terms of payment, quality and price increases. The FTC accepted CGC's explanations, based on a surge in demand, delay in start-up of production, and increased raw material and production costs. CGC promised remedial measures in regard to quality.
- 1990 ACP **Minimum tariff for containerized cargo** - The FTC investigated imposition of a minimum tariff by the Association of Container Terminal & Depot Operators (ACTDO). From the 1990 annual report it appears that the investigation was dropped once the FTC learned that the Ministry of Shipping had requested the Dept. of Exchange Control to implement the ACTDO-proposed minimum tariff. No justification is cited for the ministry's request.
- 1990 ACP **Gas cylinder distribution** - Dealers of the Ceylon Gas Co. were accused by competitors of tying sales of cylinders, in whose importation the Gas Co. has a monopoly, to sales of gas cookers also distributed by the company. The FTC "requested" (the term "ordered" is not used) the Gas Co. to instruct its dealers to desist from the practice, and asked the Dept. of Internal Trade to have its local inspectors follow up the matter in the two districts where the complaints originated.
- 1991 ACP **Steel products distribution** - A hardware merchants' association complained to the FTC when the Ceylon Steel Corporation advertized a 10% trade discount for dealers and cooperative societies buying at least 50 tons of rolled products on condition that not less than 10% of the purchase comprise specified processed goods (wire rods, nail wire, barbed wire, etc.) [This reporter was told informally that the FTC regarded the complaint as more appropriately handled by the Dept. of Internal Trade under the Consumer Protection Act.]
- 1991 Monop. **Animal feed industry** - A poultry breeder is objecting to purchase of the Sri Lanka Oils & Fats Corporation, a public corporation undergoing privatization, by Grain Elevators, a subsidiary of the multinational Prima, on the ground that resulting monopolization will raise animal feed prices. A court injunction has suspended consummation of the sale pending an FTC inquiry. The fact that the sale was approved by Cabinet makes FTC jurisdiction ambiguous.
- 1991 Monop. **Processed meats** - Small producer of processed meats (Goldi) has complained that takeover of Whittalls, owner of Ceylon Cold Stores, by Keells Food Products will give Keells undue market power in this sector. An interim injunction was obtained but then dissolved. The FTC has published a notice of inquiry.
- 1991 Monop. **PVC cables** - Kelani Cable has complained that a hostile takeover of itself by principals and associates of Alucop Cables through purchases of stock, totalling 35% thus far, will create undue market power in this sector. It requested an FTC investigation and also sought an injunction, which was granted, suspending all transactions in Kelani Cable shares.¹⁷

¹⁷ Source: FTC Annual Reports of 1989 & 1991, and interviews by the author.

**APPENDIX C - NOTES ON FIVE CASES OF ACQUISITION INVOLVING
COMPANIES QUOTED ON COLOMBO STOCK EXCHANGE**

Carson Cumberbatch & Co. (CCC). This company, an agency house operating in several sectors including tea estate management, was taken over by a private Sri Lankan company, the Sri Krishna Group, which bought 51% of its shares through the Stock Exchange. Some CCC managers went to court. An out-of-court settlement was reached whereby several operations, including insurance, tea marketing and travel, were hived off to a separate company or companies. Transactions stretched over three or four years up to late 1990. Competition is reported to be vigorous in the sectors concerned, so no antitrust issues were raised.

E.B. Creasey. This company is a distributor of imported products, including Cow & Gate. It was taken over on the Stock Exchange by a U.S.-based pharmaceutical distributor, Muller & Phipps, likewise a locally listed company. Again, no significant market concentration has resulted.

Lankem. This market leader in pesticides and insecticides, which since 1984 also produces paints, started out as a subsidiary of Shell Oil and was sold to a local private group upon Shell's nationalization in the 1960s. In 1990 E.B. Creasey (i.e. Muller & Phipps) acquired a controlling interest through transactions outside the Stock Exchange as part of a package deal including transfer of some private companies. Lankem has thus joined a conglomerate, but no evident impact on concentration in the agro-chemicals market has yet resulted.

Ceylon Cold Stores. Controlling interest (56%) held by Whittalls Estates & Agencies. CCS is second behind Pure Beverages (which has over 60%) in the market for aerated waters, produces other foodstuffs including processed meats, where it is a distant second. Labor disputes disrupted production, leading government to take control in December 1988. Share transactions were suspended until August 1991. Meanwhile Keells Food Products, the market leader in processed meats (85-90%), has taken control of Whittalls, giving it close to a monopoly in this sector and raising the issue of excess concentration (FTC has formally launched an inquiry--see Appendix B). Keells expresses intent to keep CSC's processed meat business going as a separate operation. A number of interviewees supported Keells' takeover of inefficient CSC on the ground that it will enhance competition in the much larger carbonated beverages sector.

Kelani Cables. Buying on the Stock Exchange, management and associates of Alucop Cables quietly increased their total holding of Kelani shares to a reported 35%. Management of Kelani sought to withhold allotment under an April 1991 rights issue, precipitating the current court case. Kelani claims that the relevant markets are divided as follows (see following page):

SHARES IN DOMESTIC MARKET FOR ELECTRICAL CABLES & ACCESSORIES
(excluding telecommunications cables)

<u>PRODUCT</u>	<u>M a r k e t s h a r e (%)</u>									
	<u>D o m e s t i c p r o d u c e r s</u>									
	<u>Import</u>	<u>Dom.- total</u>	<u>KCL</u>	<u>ALUCOP /CEI</u>	<u>ACL</u>	<u>KML</u>	<u>RUHUNU</u>	<u>GEM</u>	<u>EPL</u>	<u>Subtotal ALUCOP/ CEI+KCL</u>
PVC cable	0	100	40	15	30	10	5			55
Enamelled winding wire	30	70	70							70
Electrical accessories	30	70		40				20	10	40
Electrical switchgear & wiring accessories	100	0								

Kelani also claims that ALUCOP/CEI's linkage with the sole importers/distributors of electrical switchgear and wiring accessories gives it additional market power, making the average market share of an ALUCOP/CEI + KCL combination still higher.

APPENDIX D - INDIA'S MRTP ACT: PRINCIPAL TRANSACTIONS DURING 1985

Part A - Actions of Dept. of Company Affairs, Ministry of Industry

I. Registration of MRTP Undertakings (Note A)

Transactions during 1985:

	"Large" (assets = Rs. 1 b. +, but not "Dominant")	"Dominant" (assets = Rs 10m. to 1b.)	Both "Dominant" and "Large"	Total
1. Default notices issued to unregistered firms considered by department to be potentially subject to the law				86
2. Gross new registrations	244	1		245
3. Net cancellations of registration (arising mainly from five-fold increase of asset threshold in 1985)				256
Number of undertakings registered as of 12.31.85	1,563	60	59	1,682
Applications for registration pending as of 12.31.85				44

II. Registration of Agreements Relating to Restrictive Trade Practices:	Registered during 1985	Registered at End of 1985 (cumulative)			Pending
	7,129	34,670			613

III. Actions in Regard to Economic Concentration

Section of MRTP Act:

	No. of Proposals Disposed of during 1985	...of which: (percentages)				Ruled Exempt
		Approved	Rejected	Withdrawn		
21 - substantial expansion of existing undertakings	144	58%	19%	9%	14%	
22 - establishment of new undertakings	332	55%	23%	12%	10%	
21 - modification of previous orders under Sec. 21	5	100%				
22 - modification of previous orders under Sec. 22	14	93%		7%		
23(2) - mergers/amalgamations of existing undertakings	11	91%		9%		
23(4) - takeovers	7	72%		28%		
References to MRTP Commission under Secs. 21-23	0					
25 - authorization for single person to hold more than ten company directorships	0	(5 applications received during 1985)				
27 - references to MRTP Com. to consider divestiture orders (Note B)						
30 - share capital transactions involving MRTP undertakings	187	51%	26%	23%		

Part B - Actions of MRTP Commission - Transactions during 1985

Section of MRTP Act:	References Received/ Enquiries Instituted	Reports Submitted/Enquiries Disposed of:				Cases pending at end of 1985:
		Cease and Desist Order	Consent Order or "Undertak- ing Accepted"	Enquiry Closed	Total	
31 - monopolistic trade practices	1					2
Other provisions regarding monopolistic trade practices	1					2
10(a) - restrictive trade practices case originating from:						
(i) complaint by trade or consumers' assoc. or 25+ consumers	4					13
(ii) reference from central or state gov't	0					0
(iii) applications filed by Dept. of Company Affairs	16	5	9	5	19	28
(iv) Commission's own knowledge or information	113	4	5	48	57	138
36(B) - unfair trade practices case originating from:						
(a) complaint by trade or consumers' assoc. or 25+ consumers	13		1	2	3	15
(b) reference from central or state gov't	0					0
(c) applications filed by Dept. of Company Affairs	0					0
(d) Commission's own knowledge or information	83		29	28	57	74

Notes

Note A - An "MRTP undertaking" is any firm or interconnected group of firms with total assets of not less than Rs. 1 billion (equivalent to U.S. \$81 million at the average official exchange rate in 1985), or any "dominant" firm or interconnected group of firms with assets of not less than Rs. 10 million (= U.S. \$0.8 million).

Note B - Few transactions take place under this section. No references were made in 1985 and no cases were pending as of year-end. A single case of a textile mill, on GOI appeal to the courts since 1974, was finally dismissed during 1985.

Note C - One of the twenty-eight cases was referred to the police and another is described as having been "rejected."

Source: Min. of Industry, Dept. of Company Affairs, 15th Annual Report on Execution of MRTP Act (New Delhi, 1987). Summarized in C. Gray, "Antitrust as a Component of Policy Reform: What Relevance for Economic Development", p. 414, in D.H. Perkins & M. Roemer (ed.), *Reforming Economic Systems in Developing Countries*, Harvard, Cambridge, 1991.

APPENDIX E - REGULATORY ACTIONS OF KOREA'S FAIR TRADE COMMISSION, 1981-1990

Law Enforcement Activities

- From 1981 to the end of 1990, the Commission has taken as many as 4,804 corrective measures. In 1990 alone, 389 corrective measures were taken.
- Statistics show that the majority are warnings, correction orders, and recommendations for correction. Warnings have been issued in up to 3,448 cases over a ten year period. Most of them have been employed against delayed reports, or as an early warning against possible violations.

(Type of corrective Measures('81~'90))

(Number)

Measure Classification	Complaint	Surcharge	Correction Order	Recommendation for Correction	Warning	Total
Abuses of Market-Dominating Position	-	-	7	3	2	12
Mergers & Acquisitions	1	-	2	-	302	305
Capital Investment Regulations	1	-	13	4	42	60
Collaborative Activities	-	1	11	25	28	65
Prohibited Activities of Trade Associations	4	-	85	30	60	179
Unfair Trade Practices	17	-	617	493	1,465	2,592
International Agreements	-	-	-	42	1,549	1,591
Total	23	1	735	597	3,448	4,804

Source: Fair Trade Commission, Government of Korea, "Monopoly Regulation and Fair Trade in Korea", 1991, Seoul.

Distribution of Four-Firm Concentration Ratios in Moroccan and U.S. Manufacturing

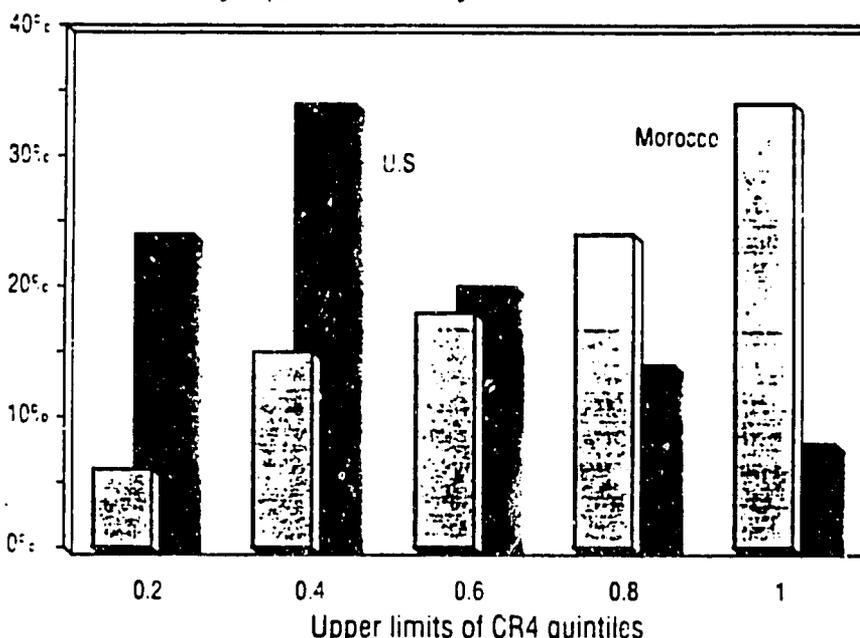
Range of Four-Firm Concentration Ratios	Number of Industries		% of All Industries		% of Total Output*	
	Morocco	U.S.	Morocco	U.S.	Morocco	U.S.
80-100%	45	22	46%	4.9%	33.7%	8.9%
60-79%	21	55	21%	12.2%	24.9%	13.9%
40-59%	19	118	19%	26.2%	18.3%	20.5%
20-39%	11	169	11%	37.5%	16.2%	33.9%
0-19%	2	87	2%	19.3%	6.9%	22.8%
Total	98	451	100%	100%	100%	100%

* Measure of output is sales in Morocco, value added in United States.

Sources: U.S. - L. G. Reynolds. *Microeconomics* - Third Edition, Irwin, 1979, 212, based on U.S. Bureau of the Census, Census of Manufactures, 1972. Special Report Series: Concentration Ratios in Manufacturing.

Morocco - analysis of 1986 Industrial Survey. T. Mounsif and C. Gray

Share of manufacturing output in each CR4 range



Explanation: an industrial branch's four-firm concentration ratio (CR4) is the proportion of sales (Morocco) or value added (U.S.) accounted for by the branch's four largest firms. For example, the 40-59% range of CR4s comprises all industrial branches such that between 40 and 59% of sales/value added is accounted for by the four largest firms.

Going from left to right in the graph, one moves from industries with low CR4s--the four largest firms account for a relatively small share of total branch output--to those with high ratios. The bars above 1 represent the proportion of aggregate industrial output (in all branches) occurring in highly concentrated industries, i.e. those with CR4s between 80 and 100%. The table and graph show that Moroccan industry is much more concentrated than U.S. industry--about one-third of U.S. industrial output occurs in branches with CR4s between 20 and 39%, but branches with CR4s above 39% account for successively lower shares of output. The converse is true for Morocco.

Source: C. Gray, "Antitrust as a Component of Policy Reform: What Relevance for Economic Development", p. 414, in D.H. Perkins & M. Roemer (ed.), *Reforming Economic Systems in Developing Countries*, Harvard, Cambridge, 1991.

APPENDIX G - PROPOSAL FOR THE FAIR TRADING COMMISSION TO CIRCULATE COMPARATIVE DATA ON PHARMACEUTICAL PRICES

The Fair Trading Commission authorizes changes in posted prices of pharmaceuticals, at importer's [or ex-factory], wholesale and retail levels, on the basis of importers' and local manufacturers' submissions of revised cost data. Since FTC computer files contain each product's authorized retail price at any given moment, it would be feasible for the Commission, in collaboration with the health authorities, to prepare a periodic report, say quarterly or semiannual, comparing the unit cost at retail of competing products in each major therapeutic category per 24-hour course of treatment as recommended for an average patient.

Such reports are prepared in several industrial countries, either by the health ministry itself or by a private agency. For example in France it is done by the ministry, in Germany by a private agency with the title 'Pharmaceutical Information Service'. The reports are circulated to health providers who prescribe medicines, in order to heighten their awareness of relative costs of alternative products to their patients or the latter's insurers. Doubtless manufacturers and distributors also study the report closely. Private individuals who want to ensure that their prescriber is pursuing the least expensive reliable option can also obtain the reports. The authorities in several countries believe that this improvement in the flow of market information has enhanced competition in the pharmaceutical sector.

Page 30 following reproduces a sheet from a recent issue of the German publication. Page 31 depicts a Lotus 1-2-3 spreadsheet designed to provide similar information for Sri Lanka. The horizontal bar-graph at the right end of each line illustrates clearly the comparative unit costs of the alternative products. It is generated automatically by a command imbedded in the spreadsheet.

The proposed spreadsheet was furnished to FTC management, which expressed interest in examining the feasibility of such an exercise in consultation with the Ministry of Health.

**Extract from German publication Arzneimittel Informationsdienst, Preisübersicht
(Pharmaceutical Information Service, Price Summary)**

PREISÜBERSICHT**ORALE NEUROLEPTIKA / V. D.**bezogen auf die Kosten der geringsten üblichen Tagesdosis¹

Wirksubstanz Dosierungsbereich der Tagesdosen in mg bei ambulanter Therapie	Handelsname Hersteller	Handelsform	Preis der DP in DM	Kosten/ geringste übliche Tages- dosis in DM ¹	Graphische Darstellung der Preisverhältnisse	
I. Dragees, Kapseln, Tabletten						
A. Schwache Neuroleptika						
a) Phenothiazine und Derivate						
Promazin 50-200 mg		PROTACTYL 25 mg Wyeth	50 Drg. zu 25 mg	9,53	0,38	
			500 Drg. zu 25 mg	62,10	0,25	
		PROTACTYL 50 mg Wyeth	50 Drg. zu 50 mg	16,99	0,34	
			500 Drg. zu 50 mg	102,46	0,20	
		PROTACTYL 100 mg Wyeth	50 Drg. zu 100 mg	31,49	0,31	
		500 Drg. zu 100 mg	201,44	0,20		
Promethazin 50-150 mg		ATOSIL Bayer	20 Drg. zu 25 mg	4,80	0,48	
			50 Drg. zu 25 mg	10,75	0,44	
			250 Drg. zu 25 mg	46,32	0,37	
Levomepromazin 50-200 mg		NEUROCIL 25 mg Bayer	20 Tbl. zu 25 mg	7,11	0,71	
			50 Tbl. zu 25 mg	16,17	0,65	
			250 Tbl. zu 25 mg	63,52	0,51	
		NEUROCIL 100 mg Bayer	50 Tbl. zu 100 mg	45,21	0,45	
			250 Tbl. zu 100 mg	182,88	0,37	
Thioridazin 50-200 mg		MELLERETTEN Sanofi	20 Drg. zu 10 mg	3,71	0,93	
			50 Drg. zu 10 mg	8,20	0,82	
			250 Drg. zu 10 mg	32,05	0,64	
		MELLERIL Sanofi	50 Drg. zu 25 mg	10,27	0,41	
			250 Drg. zu 25 mg	38,24	0,31	
		MELLERIL RETARD 30 Sanofi	30 Tbl. zu 30 mg	13,29	0,74	
			100 Tbl. zu 30 mg	36,47	0,61	
			500 Tbl. zu 30 mg	150,68	0,50	
		MELLERIL 100 mg Sanofi	20 Drg. zu 100 mg	14,68	0,37	
			50 Drg. zu 100 mg	32,16	0,32	
			250 Drg. zu 100 mg	113,70	0,23	
		MELLERIL RETARD 200 Sanofi	10 Tbl. zu 200 mg	14,03	0,35	
			50 Tbl. zu 200 mg	55,64	0,28	
	250 Tbl. zu 200 mg	213,60	0,21			
Suforidazin 50-150 mg		INOFAL Sanofi	20 Drg. zu 50 mg	14,34	0,72	
			100 Drg. zu 50 mg	55,96	0,56	
			500 Drg. zu 50 mg	231,25	0,46	
Prothipendyl 40-200 mg		DOMINAL Homburg	50 Drg. zu 20 mg	11,36	0,45	
			250 Drg. zu 20 mg	43,10	0,34	
		DOMINAL FORTE 40 mg Homburg	20 Drg. zu 40 mg	5,97	0,30	
			50 Drg. zu 40 mg	12,73	0,25	
			250 Drg. zu 40 mg	49,36	0,20	
		DOMINAL FORTE 80 mg Homburg	50 Tbl. zu 80 mg	15,11	0,15	
		250 Tbl. zu 80 mg	60,30	0,12		
Chlorprothixen 50-150 mg		TARACTAN 5 mg Roche	50 Drg. zu 5 mg	4,92	0,98	
			250 Drg. zu 5 mg	22,96	0,92	
		TARACTAN 15 mg Roche	50 Drg. zu 15 mg	7,81	0,52	
			250 Drg. zu 15 mg	34,23	0,46	
		TARACTAN 50 mg Roche	50 Drg. zu 50 mg	18,57	0,37	
			250 Drg. zu 50 mg	77,02	0,31	
		TRUXALETTEN Tropon	50 Drg. zu 5 mg	6,99	1,40	
		TRUXAL 15 mg Tropon	50 Drg. zu 15 mg	8,75	0,58	
			250 Drg. zu 15 mg	37,23	0,50	
		TRUXAL 50 mg Tropon	50 Drg. zu 50 mg	20,71	0,41	
	250 Drg. zu 50 mg	87,16	0,35			

¹ Angaben des Dosierungsbereiches bei ambulanter Therapie nach HEINRICH, K. (Psychiatrische Klinik der Universität Düsseldorf, Deutsche Apotheker Zeitung 43 (1976), 1617-1623)

