

# Competition

## and Development

### THE POWER OF COMPETITIVE MARKETS

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## Equal Opportunity to Compete

**South African competition policy promotes both fair market practices and economic empowerment for previously disadvantaged racial groups.**

*Competition law in South Africa acknowledges that ensuring open, free, and competitive markets today requires addressing the injustices of the past. The law is exerting a subtle influence over the way in which South Africans do business.*

In both developed countries and in the newly liberalized economies of the developing world, the essential aim of competition law is to ensure that consumers realize the benefits of a free and open marketplace.

By addressing issues such as mergers, abuse of dominant market position, and collusion between competitors, these laws are designed to prevent companies from taking advantage of their customers by fixing prices or skimping on quality. The underlying idea is that true competition in the marketplace produces a range of efficiencies and associated benefits that the competing firms, in their quest to win customer loyalty, will feel compelled to pass along to consumers.

In recent years, many developing countries have introduced new competition laws in conjunction with other economic reforms such as trade and investment liberalization and privatization programs. While some governments have simply copied laws from Europe, the United States, and Canada, others believe that these laws must reflect unique national circumstances and historical realities.

This is nowhere more evident than in South Africa, where the former apartheid regime imposed rigid barriers that severely limited the economic participation of racial groups categorized as blacks, coloureds, and Asians. Indeed, the country is bound by the legacy of an economy where, for over a century, power was concentrated in the hands of a few large white-owned firms. The current government is attempting to encourage broad-based ownership of



IDRC: Peter Bennett

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enterprises and an environment of dynamic competition. So much so that its competition law mixes considerations of purely economic efficiency with those of equitable wealth distribution and considers the particular needs of firms that are owned or controlled by previously disadvantaged racial groups.

## A privileged few

There are several reasons why South Africa's economy is so highly concentrated, explains Genesis, a South African consulting firm that participated in IDRC-supported research on competition policy. One reason is the central role played by the diamond industry since the late 1800s. Since diamond mining required the deployment of large amounts of capital and specialized expertise, mining companies and the finance houses that backed them had to be big enough to take on the task. The risk involved with developing individual diamond properties encouraged further consolidation: if investors joined together to form large consortia, they could spread the risks associated with particular digs across a wider range of projects.

The economic Goliaths borne of the diamond industry continued to grow — leading the charge, in the first part of the 20th century, into coal and platinum mining and then into manufacturing. Their dominance was only matched in the latter part of the century by the state-owned companies operating in transportation, telecommunications, iron and steel, oil and gas, and armaments.

The other major contributor to the highly concentrated nature of economic ownership and participation in South Africa, Genesis researchers explain, was the series of laws and policies known collectively as apartheid. Introduced in the 1920s to advance the interests of South Africa's white (predominately Afrikaner) working class, the apartheid system favoured whites through job quotas, generous minimum wage provisions, superior educational opportunities, and agricultural protection measures. Conversely, apartheid laws denied the non-white majority any meaningful economic role by repressing black workers' wages, providing other racial groups with only minimal education, and forbidding them to unionize or to enter the professions.

After the fall of apartheid in 1994, the incoming African National Congress (ANC) government had both social and economic reasons for instituting a competition policy that could address — and potentially reverse — the highly concentrated, exclusionary nature of the South African economy.



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## New competition regime

Under the former National Party regime, a Competition Board had been in operation since 1979. However, its limited mandate and purely advisory role within the Ministry of Trade rendered it ineffective. Today's competition apparatus, by contrast, is independent and much more vigorous. Three agencies are responsible for implementing the *Competition Act* of 1999: a Competition Commission that studies possible threats to open competition and makes recommendations; a Tribunal that weighs the arguments and produces rulings; and an Appeal Court that reviews and can overturn the Tribunal's edicts.

Vani Chetty, a lawyer who has represented many businesses before the competition authorities, believes those authorities have had a real impact on South Africa's economic life. They have “grown from a fledgling institution with very little credibility to one with much greater stature and knowledge,” she says. “Whereas businesses in particular were reluctant in the beginning and unsure of what they had to do to comply with the competition law, today they are aware of what penalties are involved and they put a lot of money, time, and effort into making sure that they comply at all levels.”

Still, the competition agencies have faced considerable challenges, partly because the *Competition Act* has two distinct mandates: economic and social. Some of the Act's objectives are purely economic — its stated purposes include, for example, “to promote the efficiency, adaptability and development of the economy”; “to provide consumers with competitive prices and product choices”;

and “to expand opportunities for South African participation in world markets.” These goals align closely with the broader economic aims of the ANC government, which embraced free market policies when it took power and sought to take advantage of the new export opportunities that came with the lifting of the international community’s anti-apartheid economic sanctions.

The *Competition Act* is also designed to serve social objectives such as “[promoting] a greater spread of ownership, in particular to increase the ownership stakes of historically disadvantaged persons.” The Act’s public interest provision also allows the Competition Authorities to take into account the impact of mergers on employment, in a country where unemployment rates are among the highest in the world. This aspect of the Act can be seen as a complement to a broader network of policies and laws known collectively as Black Economic Empowerment (BEE), where the term “black” is used to signify Africans, people of mixed race, and Indians. BEE aims to promote black ownership of businesses (through targets established in industry charters), transfer skills to and aid the advancement of blacks within companies, and encourage employment creation for the black majority.

There are specific issues the Act instructs competition authorities to examine in instances where cases have a potential to either impede or advance the broader aims of BEE. As University of Cape Town researcher Neo Chabane notes in a paper published by IDRC partner Trade and Industrial Policy Strategies, the Act allows anticompetitive practices where they promote the ability of black-owned and -controlled enterprises to become competitive. “Decisions on mergers on public interest grounds,” she

adds, “... take into account the effect that the merger will have on the ability of black small businesses or firms to become competitive.” In some cases, mergers that might normally be rejected on the grounds they would reduce marketplace competition may be exempted if they support the goals of BEE. Meanwhile, competition authorities are mandated to reject mergers that would lead to substantial job losses.

## Commission and Tribunal at odds

Recent cases provide no definitive indication that competition authorities have settled on a formula for balancing the Act’s distinct — and sometimes competing — social and economic goals. Differing views persist on how to serve the Act’s objectives in practice.

In one case, for example, a small producer of treated wooden poles, Nationwide Poles, had discovered that it was paying a higher price for its “creosote” wood preservative than its competitors, since the large firm Sasol Oil was offering discounts for higher volume purchases. Nationwide complained that this constituted discrimination against smaller firms — an issue of some concern both because of the government’s desire to see a larger portion of the economy devolved into the hands of smaller companies, and because small- and medium-sized firms are seen as a promising avenue through which the previously excluded black population can take on a more meaningful economic role. The Competition Tribunal ruled in favour of Nationwide, partly based on its determination that Sasol was acting out of market dominance and that the 3 to 4 percent price differential was significant enough to constitute a barrier to small firms operating effectively in this market. However, the Appeal Court overturned the Tribunal’s decision, arguing that there was no evidence to show that Sasol’s pricing structure had undermined Nationwide’s ability to compete.

In another case, the Competition Commission had recommended that a takeover of a branch of Barloworld Equipment Finance by Wesbank have conditions attached to it. Concerned that many of Barloworld’s customers — small- and medium-sized industries owned by previously disadvantaged people — might lose access to credit after the merger, the Commission wanted to ensure the company would be committed to continuing to serve those customers. The Tribunal, however, believed that a number of marketplace conditions already protected the customers and approved the merger without conditions.



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## A quiet impact

The ongoing disagreement between the competition agencies over when and how they should act to uphold the “public interest” components of the *Competition Act* underscores a broader debate in South Africa. Some economists, for example, have been puzzling over whether competition policy is really the right vehicle for promoting social goals. Lawyer Vani Chetty ventures, meanwhile, that while public interest hasn’t trumped purely economic arguments in cases like those mentioned earlier, competition law has helped advance awareness of equity issues and promoted positive change in less visible ways.

“I would say it’s had a more quiet impact,” she says, “because the requirements of the Act get structured into transactions. The Commission may never hear about it, but when I am advising a client on how to do a merger, I make sure that the employment provisions are understood, so that this does not become an issue that would make the transaction problematic. Business is concerned with getting the deal done as quickly as possible, so it wants to take care of those concerns.”

But the competition regime is still in its infancy and the number of cases with BEE considerations before competition authorities is starting to grow, observes researcher Neo Chabane. “As more and more companies change their ownership structure in order to reflect suggested racial ownership ratios, the competition authorities will have to deal with an increasing number of mergers which have

been agreed on in order to enable companies to comply with the relevant charter in their industry.”

Taimoon Stewart, IDRC partner and international trade specialist affiliated with the University of the West Indies, has been following the South African experience. The domination of developing-country economies by powerful local elites, including some Caribbean countries, she says, was cemented into place by deliberate policies of racial exclusion. Stewart believes that the impact of competition policy on social equity in South Africa is probably less dramatic than many may have expected, but that the process of debate and disagreement may ultimately prove to be positive.

“It appears that they are moving toward a rigorous application of the law and the development of a solid jurisprudence,” she says, “rather than a willy-nilly application that would in the end weaken the law and be exposed to challenge.”

*This case study was written by Stephen Dale, an Ottawa-based writer. It is partially based on the study, Promoting Competitive Markets in South Africa, by Stephan Malherbe, Andrew Myburgh, Jacob Kosoff, and Paul Anderson, of Genesis Consulting and An Evaluation of the Influence of BEE on the Application of Competition Policy in South Africa by Neo Chabane.*

*The views expressed in this case study are those of IDRC-funded researchers and of experts in the field.*

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