

Speech of David Lewis, Chairperson of the Competition Tribunal of South Africa on Competition and Development

*The multiple, and often conflicting, objectives and demands that faced South Africa's first democratic government have influenced both the competition law and in its privatization initiative. In addition to the orthodox standard objectives and instruments of competition law and policy, the Competition Act obliges the competition authorities to consider industrial policy objectives into its decision making. For its part, while competition and efficiency considerations informed the privatization drive initiated by the government after 1994, a range of other objectives - industrial policy, access by poor consumers and black shareholders, fiscal considerations - are also present. How have these standard instruments of competition policy - anti-trust law and privatization - balanced these multiple objectives and has it been possible to maintain a focus on promoting competition in the face of these often conflicting objectives? What role have the antitrust authorities played? Are they listened/consulted by Government?*

The fact that there are multiple objectives enshrined in our anti-trust statute is well known. Apart from their insertion into the general objectives and purport of the Act these multiple objectives are particularly explicit when we investigate and decide mergers. We are mandated by our Act to decide whether a merger is likely to result in a substantial lessening of competition but we are also required, in our decision, to consider the impact of the merger on a number of defined 'public interest' factors, these being the merger's impact on a region or sector, on employment, on the ability of small firms or firms controlled by historically disadvantaged persons to become competitive and on international competitiveness. Strictly speaking a merger which is found to substantially lessen competition may be permitted if its positive impact on the spread of black ownership is thought to outweigh its negative impact on competition; and a merger which is thought to have no negative, or even a positive, effect on competition falls to be prohibited if it is decided that it will have a counterbalancing negative impact on employment.

The impact of these public interest insertions into our Act has been discussed at length in ICN conferences and in a number of other international fora. Suffice to say that our experience over the last eight years has shown that, despite strong initial misgivings in the international competition community, it is wholly possible to carry out a statutory mandate which requires sensitivity to a number of industrial and social policy considerations without compromising the core objectives and approaches of orthodox competition law and policy. It is my strongly held view that the work of all competition authorities is, in one way or another, influenced by these type of considerations. Hence when a merger is prohibited by considerations of national security or a cartel is tolerated because it enhances export revenue, anti-

trust considerations have been compromised by broader industrial and social policy considerations. That these may be contained in complementary legislation rather than in the anti-trust statute itself makes little or no difference. Indeed, I believe that the fact that, as in our case, these considerations are clearly defined and limited in the competition statute and that the balancing of non-competition and competition considerations is carried out by the competition authority, better ensures that the core competition considerations carry the greatest weight in the final decision. It is noteworthy that public interest considerations have never determined a decision to approve or reject a merger, though they occasionally have given rise to the imposition of conditions.

However, I want to take this opportunity to consider what I believe to be a more serious incursion of non-competition objectives into the efficacy of competition law and policy. In particular I want to draw on the South African experience to examine the implications for competition law and policy of different modalities of privatization.

The South African economy, in common with a great many other developed and developing countries, was, until relatively recently, characterized by the presence of a number of powerful state owned enterprises. This was, and to some extent still is, particularly true of the large public 'utilities' in telecommunications, public transport and electricity generation and distribution. But it was also true of a diverse range of other sectors – for example steel, petroleum and basic chemical feedstocks, airlines and forestry. Certain of these state owned enterprises – notably the steel and petroleum companies – were privatized in the 1970's and '80's, while others – for example telecommunications and airlines - were recently privatized, or part-privatised by the first post-apartheid government. Still others – for example electricity and public transport - remain state owned enterprises.

The character of the enterprises privatized in each of these periods is quite distinct as are the drivers that underpinned the privatization process. The SOE's that were privatized in the earlier period were in sectors where private ownership and functioning markets were well-established in other parts of the world – they were generally not licensed undertakings but simply part of the heavy industrial infrastructure that the state had been obliged to provide in the early periods of industrialization. Hence the most important privatizations of this period are found in the steel and petrochemical markets where two large SOE's – ISCOR and SASOL respectively - were sold off to the public. Parts of their markets – for example, the retail petroleum market – were and sometimes still are subject to high degrees of regulation, including price regulation, while, others, for example, steel, were left largely unregulated, although, in the case of steel its pricing decisions were constrained in the first period of its existence as a privately owned company.

It's not easy to identify the factors that underpinned this period of privatization. What is clear is that the privatised firms in question dominated important markets characterized by high entry barriers. Publicly owned dominant firms, near

monopolies, whose pricing practices were subject to regulation of one sort or another were converted into privately owned and, in significant part, unregulated monopolies. The prospect of new entry – which commercial considerations, largely related to scale issues, rendered unattractive – were further undermined because they occurred at a time when large investments in South Africa were singularly unattractive particularly for the large multinationals who were the only potential competitors for these newly privatized competitors. Aside of course from the obvious factors inhibiting investment in apartheid South Africa, potential entrants in these markets would have been well aware of the still intimate and privileged links between the state and the privatized entity thus further deterring new large scale investment.

The upshot of this is that the erstwhile state owned enterprises were able to consolidate their monopolistic control of critical markets. I hasten to add that this does not refer to a large number of firms in a diverse range of markets. But it does characterize several firms producing key intermediate products. Certain of the enterprises referred to – for example SASOL, the petroleum and chemicals company – have been able to grow into successful multinational companies in their own right; others were absorbed into giant multinationals. Control of the steel monopoly, for example, has, in recent years, been acquired by the Arcelor-Mittal group.

For South African consumers the implications are stark: when purchasing critical intermediate products, for example steel, they are confronted by what we have in a recent decision of the Competition Tribunal termed ‘uncontested firms in incontestable markets’, essentially firms whose pricing is unconstrained by actual or potential competition or by regulation.

From the perspective of competition law, these are firms that are not compelled to resort to illegal exclusionary conduct in order to maintain their monopolies. The upshot is that these firms may ‘exploit’ their super-dominant status – that is, to say, ‘exploitative abuses’, particularly monopolistic or excessive pricing which cannot be cured by new entry, are a distinct possibility in these markets. I would vouch that, South Africa’s particular circumstances notwithstanding, we are not the only anti-trust jurisdiction faced by this problem. It is for this reason that we, in the South African competition authorities, want the ICN unilateral conducts working group to include an examination of exploitative abuses in its work programme. It helps explain why our legislature chose to make excessive pricing a *per se* prohibited abuse of dominance. I should stress that small economies may well be characterized by a number of monopolistic markets and these will not always have state ownership in their recent history. However, it is clear that a period of state ownership retards competition well into the post privatization period – in particular, privileged links between the privatized enterprise and the state are easily maintained and leveraged into commercial advantage against actual or potential new entrants .

The South African Competition Tribunal has recently published a decision in which it has found the monopoly steel manufacturer guilty of excessive pricing. We have, in arriving at our decision, elected not to pass judgment on the level of price. This contrasts with the approach that most of the European decisions on excess pricing take and which both the plaintiff and respondent in this case urged upon us. We have, in other words, refused to assume the mantle of a price regulator, but have rather stayed with a competition authority's core concerns with structure and conduct. Our finding is that the firm's structural super-dominance complemented by ancillary conduct designed to segment its markets and prevent arbitrage between these market segments has resulted in a price in excess of that which would have prevailed absent the offending conduct which itself relied on the firm's structural advantage. We would greatly value feedback from our fellow ICN members on this decision. It is an honest attempt to deal with a severe problem – that of exploitative abuse - that is probably confined to relatively small economies, in other words to the majority of the jurisdictions represented here, and which most frequently has its origins in past privatizations that gave rise to unregulated monopolies. This is an extremely difficult issue but not one which can be wished away by either its technical difficulties or by a doctrinaire distaste for concepts like 'excessive pricing'.

The experience of the post apartheid privatizations has, I fear, not been a happy one either. Here multiple and conflicting objectives on the part of government have clearly bedeviled the privatization process and the post-privatisation regulation of the privatized firms. The privatization of the fixed line telephone monopoly is an interesting, if depressing, case in point. Here the government elected to sell off a large, though minority share, to a US operator, SBC, with the latter effectively assuming responsibility for the management of Telkom. We can speculate on the basis for the government's decision sell off a large stake in the enterprise whilst continuing to hold on to a majority stake in the firm. The decision to sell off a stake was, it seems, driven by a combination of fiscal considerations and the correctly perceived need to introduce an efficient, world class operator into the local telecommunications market. I surmise that the reasons why government nevertheless chose to retain a large stake are to be found in a combination of fiscal considerations (a desire to maintain an ongoing share in the future profit streams of the monopoly), black economic empowerment (a desire to retain a shareholding that could later be used to introduce majority control by black investors) and the desire to use the telephone monopoly as an instrument of redistribution (for example, by rolling out telephone services to the rural and low income urban areas). These are all laudable objectives but they have come at the expense of competition considerations which would have been best served by a full privatization coupled with the immediate licensing of a second and even third national fixed line operator.

Indeed competition was further compromised by an agreement to extend the partly privatized firm's monopoly for five years – that is, to say government agreed not to

license a new operator for five year - in exchange for a commitment on the part of the partly privatized monopoly to roll out a specified number of telephone connections to the rural areas. The telephone monopoly kept its side of the bargain and rolled out telephone connections to the rural areas but at such high prices (which were, of course, precisely enabled by weak regulation and the absence of competition) that before long the rate of disconnection exceeded the rate of connection.

What we have in the Telkom case is a company whose controlling shareholders, until recently, effectively represented an alliance between a foreign multinational and the South African government – in short some shareholders vastly experienced in the vagaries of operating in a regulated market and other shareholders with powerful links to a government whose objectives in maintaining a stake were already diverse and conflicting.

The telecommunications regulator was established a short while before the privatization. Its establishment and the management of its subsequent relationship with government and the legislature was the responsibility of the same ministry that represents government qua shareholder in Telkom. It should come as no surprise to learn that regulation of fixed line telephony has never been effective from a competition perspective. Indeed, although the part-privatized Telkom was only granted a five year monopoly, it took a further 2 years to license a second fixed line operator effectively giving Telkom a 7 year monopoly. It is now a year since the license was issued and there is still no effective fixed line competitor for Telkom. Telkom's US partner sold out its interest in Telkom as soon as it became apparent that a second license was to be issued, thus establishing that its major interest was in the short term monopoly rents that it could and did extract.

It is important to add that because competition did figure, even if not very prominently, in the diverse range of objectives that informed the privatization in the first place, the regulators were, in their founding statutes, given certain competition jurisdiction, particularly with respect to abuse of dominance. The establishment of the regulators predated the Competition Act and we now have to deal with the vexed problem of concurrent and overlapping jurisdiction. Needless to say Telkom has used this jurisdictional uncertainty in order to avoid competition jurisdiction altogether. It will come as no surprise to learn that our fixed line telephone costs rate as amongst the highest in the world.

Here then is a tale of two botched privatizations. There are further examples but these suffice to illustrate our point. Here you have a jurisdiction in which there is an effective competition statute and an effective competition authority. However competition is seriously impeded in key sectors that have, by virtue of the products that they provide, major knock-on effects into the rest of the economy. The first example outlined here is of a privatization that predated competition legislation by some considerable period in a sector – steel – that is no longer ordinarily subject to regulation. However, a public and hence regulated monopoly was converted into

a private and unregulated monopoly which was, for a variety of reasons, able to consolidate its super dominant status in its markets. Here then you have an unregulated private monopoly, one that is constrained neither by competition, actual or potential, nor by law. The upshot is the potential for unilateral exploitative abuses which we have to confront doctrinal niceties and conceptual difficulties notwithstanding.

In the other instance, we have a powerful state owned monopoly that was partially privatized. Government held on to a majority stake in the company for a variety of reasons, none of which have any relationship to competition. Here the presence of multiple objectives has impacted negatively on competition. The negative effects take a variety of forms. The most explicit is the trade off made between, on the one hand, the extension of a statutory monopoly, and, on the other, redistributive considerations in the form of expediting the roll out of telephone connectivity to the rural areas. The weakness of the regulator and unresolved jurisdictional disputes between the regulator and the competition authority are further manifestations of conflicting objectives.

In summary then, although our competition statute does embody multiple objectives we have had little difficulty in balancing these with our core mandate to promote and protect competition. Where competition law and the competition authorities have been less successful is in influencing the mode of privatization. Here the presence of multiple objectives has severely impacted on the positive impact that privatization may have had on competition. There are signs that this is beginning to change. The competition authorities have jurisdiction over the sale of controlling stakes in SOEs and have, on at least one occasion, prevented a sale of a state owned forestry asset that would have undermined competition. In general the enhanced standing of the competition authority has strengthened its position as an effective advocate. However, in critical instances, telecommunications being the most glaring example, it seems that the mode of privatization has given rise to a market riven by anti-competitive distortions which the competition authorities have, at best, only a limited ability to cure.