

# THE KEY PRIORITIES AND OBJECTIVES OF THE COMPETITION COMMISSION OF SOUTH AFRICA

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## I. INTRODUCTION

The profile of competition policy—and of the competition authorities—has grown substantially in South Africa in recent years. This is due partly to the work of the authorities and partly to heightened awareness of the importance of competitive rivalry for the country's growth and development. A few widely reported cartel cases in the past two years have especially focused the attention of the public and policy makers on the authorities. At the same time, studies of the challenges facing the South African economy have highlighted as concerns high levels of concentration and anticompetitive conduct.

Given the highly concentrated nature of the South African economy, competition policy was identified by the newly elected ANC government at the outset in 1994 as being an important part of the program of reforms. For example, the largest conglomerate grouping, Anglo-American, was identified as controlling entities accounting for 43 percent of the capitalization of the Johannesburg Securities Exchange in 1994, with the largest five conglomerates controlling 84 percent.<sup>1</sup> Moreover, several of these groupings were effectively family-controlled. In addition, current and former state-owned enterprises had quasi-monopoly positions in important industries such as steel, basic chemicals, and telecommunications. Furthermore, the apartheid government's development agenda had focused on minerals and energy-intensive activities and deliberately not on diversified manufacturing and service activities, given the systematic under-education of the black

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<sup>1</sup> For a review of patterns of continuity and change, see N. Chabane, A. Goldstein, & S. Roberts, *The Changing Face and Strategies of Big Business in South Africa: More than a Decade of Political Democracy*, 15 INDUS. & CORP. CHANGE 549–78 (2006).

majority. Against this background, competition policy has had a central role under democracy because it is part of a set of policies aimed at transforming the economy, increasing participation, addressing entrenched interests, and subjecting firms to greater market discipline through liberalization.

The Competition Act of 1998, which came into force in 1999, provided for the establishment of the Competition Commission and Competition Tribunal, both independent institutions responsible for investigation and adjudication of complaints and mergers. There is also a specialist Competition Appeal Court. The Commission spent much of the first five years focusing on merger evaluation. This was to a large extent because the founding legislation introduced compulsory premerger notification above certain thresholds of combined assets and turnover. Not surprisingly, this meant the authorities from the outset bore a heavy burden of work.

The lower profile of enforcement action in the early period was also due to a belief that with the liberalization of the economy and its relatively developed nature, businesses would understand and observe good competition practices. For example, while the 2003 Organization of Economic Cooperation and Development (“OECD”) peer review of South Africa noted that “[t]o a surprising extent, competition policy in South Africa is merger policy,” it observed that this is understandable in the context of South Africa’s relatively high level of development.<sup>2</sup> Unfortunately the recent cartel cases have suggested that this was somewhat naïve and that anticompetitive conduct is more widespread than previously thought.

However, merger activity provided a good basis for building the capacity and reputation of the institution. This has been due to the large numbers of mergers notified to the Commission — in excess of 400 transactions in most years, with a significant proportion

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<sup>2</sup> M. Wise, *Competition Law and Policy in South Africa*, OECD Global Forum on Competition Peer Review, Paris (Feb. 11, 2003).

being international in scope. Extensive public merger hearings in the Competition Tribunal (“Tribunal”) have involved in-depth analysis of the potential anticompetitive implications. Thus, the Tribunal rulings on such mergers have built up a substantial body of competition law in this area in a relatively short space of time.

The changes currently underway in Commission priorities are partly driven by the institution and partly by factors in the wider political and economic environment. The Commission has identified the need to more proactively focus on contraventions, including both collusion and abuse of dominance. The introduction of a Corporate Leniency Policy three years ago, which was recently revised to provide more certainty for applicants, has had a significant effect on cartel busting.

However, this success, particularly in the uncovering of a cartel formed by the major national bread bakeries, has led to public outrage. This has been coupled with a political environment that is more skeptical of unregulated capitalism and favors a more activist state. In addition, recent analyses have highlighted the negative effects of continued extremely high levels of concentration and associated anticompetitive behavior.<sup>3</sup> As a result, the expectations of the competition authorities have increased. Substantive amendments to the Competition Act are also making their way through parliament at the time of writing.<sup>4</sup> These amendments seek to increase the authorities’ powers and introduce criminal sanctions for individuals involved in cartels, as described in more detail below.

The discussion begins with a look at the more proactive approach to enforcement and prioritization of the Commission in recent years before assessing the outlook, including the focus on knowledge management and building the Commission’s capacity.

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<sup>3</sup> For example, in a 2006 paper, Aghion et al. found high markups in South Africa that were associated with lower levels of productivity growth and employment. P. AGHION, M. BRAUN, & J. FEDDERKE, COMPETITION AND PRODUCTIVITY GROWTH IN SOUTH AFRICA (Harvard University, CID Working Paper No. 132, 2006).

<sup>4</sup> September and October 2008.

## II. ENFORCEMENT

The concentrated nature of South Africa's economy together with a legacy of protection, state ownership of strategic industries, and official sanctioning of cartels in many markets under apartheid suggests a major role for enforcement by the Competition Commission. In recent years this emphasis has been reinforced by an economic policy framework that has identified increased competitive rivalry as crucial for faster and more broad-based economic growth.<sup>5</sup> In addition, the key role of the competition authorities has been noted by the South African president in successive state of the nation addresses. This focus has been further supported by the uncovering of cartels aided by the Commission's corporate leniency policy ("CLP") and recent Tribunal rulings on abuse of dominance.

### *A. Cartels*

The South African Competition Act includes a per se prohibition of cartels; however, in the first eight years of the new authorities, there were very few prosecutions reflecting these contraventions apparently not being prioritized. This is surprising given that the South African economy exhibits conditions supportive of collusive behavior. Collective setting of prices and other terms was explicitly sanctioned in many industries by the apartheid regime before 1994. While systematically excluding Blacks from political, social, and economic rights, the apartheid regime supported its main constituencies through state-sanctioned marketing boards in almost all agricultural products.

As already noted earlier in this chapter, the South African economy is highly concentrated and business and social networks have historically overlapped, specifically in White business. Industry associations have typically operated to lobby government, and information appears to be widely shared among firms enabling ex post monitoring of rivals'

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<sup>5</sup> See Deputy President Phumzile Mlambo-Ngcuka, A Catalyst for Accelerated and Shared Growth—South Africa (ASGISA): A Summary, Media Briefing (Feb. 6, 2006), available at <http://www.info.gov.za/speeches/briefings/asgibackground.pdf>.

performance. The concentration of industrial activity in three or four main regions, substantial distances from each other, also makes market segmentation and monitoring relatively easier.

The 2004 introduction by the Competition Commission of a CLP has played a significant role in the uncovering of several major cartels in recent years.<sup>6</sup> These include alleged cartels in milk and dairy products, bread and milling, medical supplies for state and private hospitals, structural steel products, and various other products associated with infrastructure and construction. Particularly in agriculture, since the first democratic government swept aside the marketing boards in 1996, it has become clear that in many markets, private companies merely continued the centralized price determination (and related arrangements) such as market allocation and information exchange under their own auspices.

The Commission's recent experiences raise three main points.

First, for leniency to be effective, a credible threat that a cartel will be uncovered is required. It is in this context that the Commission has identified sectors and markets in which there are strong indications of anticompetitive outcomes that need its attention.

Second, once a leniency application has been received, the further option of settlement at reduced fines, together with leniency for related markets possibly not covered in the first CLP, can have a domino effect revealing much wider collusion. This requires a careful management of the process and a good understanding of the grounds for suspicion. Of the recent cartel cases, this was most obvious in the case of bread in which information from a distributor in a single province led to a leniency application and information on the national market. This was followed by a second applicant who provided information on collusion in the related milling of wheat and maize for human consumption.<sup>7</sup>

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<sup>6</sup> See Competition Commission of South Africa, Corporate Leniency Policy, at [http://www.compcom.co.za/resources/Government%20Gazette\\_111.doc](http://www.compcom.co.za/resources/Government%20Gazette_111.doc).

<sup>7</sup> The consent order for the second applicant in the bread case has been confirmed by the Tribunal. The milling cartel case has yet to be finalized.

Third, there is a public expectation that the penalty will reflect the impact of coordination, and that there will be demonstrably more competitive outcomes following the prosecution of the cartel. In South Africa, bread prices increased soon after the cartel began being prosecuted, which led to questions as to whether the firms were just passing on the fine to customers. The Commission has been under pressure to evaluate the prices following prosecution with the case also adding fuel to those calling for criminalization.

To improve the incentives for firms to apply for leniency, the Commission introduced a new CLP early in 2008. This provides greater certainty to applicants that they will receive leniency if they are both first and comply with the requirements in terms of cooperation and information provision. It does not distinguish between instigators and the other cartel members, all of whom are equally afforded the opportunity for leniency. It also allows for firms to first apply for a marker, then for conditional leniency (the leniency is conditioned on cooperation leading to the prosecution of the remaining cartel members).

While the CLP has aided in prosecution of hard-core cartels, there are still indications of widespread interaction between firms of an anticompetitive nature—which the firms do not necessarily see as problematic. In several cases, firms have gotten together to share information and discuss “stabilizing” prices, which they did not view as troublesome as they apparently believe that no agreement had been reached or kept to. Given the undynamic and concentrated nature of many markets, there is clearly a need to pay further attention to issues such as information exchange. Finally, there is a long way to go for a competition culture to become entrenched, and unsurprisingly, coordinated conduct will continue to be a key area for the Commission with substantial resources being directed to major cartel investigations.

*B. Abuse of Dominance in a Small, Open, Developing Economy: Post-Chicago or Mid-Atlantic?*

In recent years there has been renewed international attention on abuse of dominance, including that surrounding the European Commission's review of Article 82 of the EC Treaty. This has happened in the context of increasing recognition among economists of the scope for strategic behavior on the part of dominant firms to engage in anticompetitive abuse of their position. This has been termed a "post-Chicago synthesis" by Kovacic and Shapiro<sup>8</sup> while, in a 2007 paper, John Vickers characterized an emerging "mid-Atlantic" consensus among economists based on rigorous foundations for abuse of dominance concerns flowing from meeting the Chicago School critique.<sup>9</sup>

The effects-based rather than form-based analysis motivated by this approach has important implications for a small, open and developing country such as South Africa. South Africa's distance from other industrial economies and the legacy of state support and protection for many industries under the apartheid regime means that, in general, markets are more concentrated and entry barriers are higher than in other industrial economies. As described earlier, there are also dominant firms in important industries that do not owe their position to innovation or risk-taking investors but to state sponsorship and support.

These realities suggest that applying the same standards as in European jurisdictions will yield greater concerns in South Africa about unilateral abuse. Furthermore, the negative implications of this abuse for economic efficiency and consumer welfare will likely be greater and more persistent in South Africa. While this may be true at the level of generality, addressing such behavior rests on detailed, case-by-case analysis of the actual conduct and effects to meet the tests set down in the Competition Act. This is the challenge fully recognized by the Competition Commission.

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<sup>8</sup> W. Kovacic & C. Shapiro, *Antitrust Policy: A Century of Economic and Legal Thinking*, 14 J. ECON. PERSP. (2000).

<sup>9</sup> J. Vickers, *Competition Law and Economics: A Mid-Atlantic Viewpoint*, 3 EURO. COMPETITION J. 1–15 (2007).

Recent Competition Tribunal rulings on abuse of dominance have demonstrated the entrenched nature of dominant firms in many areas of the economy and the scope of anticompetitive abuse by those firms to extend and protect their dominance and to exert their resulting market power. In one case, the national flag-carrying airline had been engaged in various inducements to travel agents to favor it over rivals. In another, the Tribunal found there had been excessive pricing by the dominant flat steel producer, compounded by a range of ancillary conduct that had operated to entrench the firm's market power and ensure the maximum monopoly price could be charged.<sup>10</sup> Other pending cases referred to the Tribunal but yet to be ruled on include those related to cigarettes, fixed-line telecommunications, fertilizer, and beer.

In all these cases, the positions of the dominant firms are at least partly due to intervention and support by the apartheid government. With steel, basic chemicals (including fertilizer), and telecommunications, the firms had been state-owned. The airline continues to be state-owned after a short period as a privatized entity. In short, the firms are not generally ones whose positions derived from innovation or risk-taking investments by private agents.

Moreover, the historic support for capital-intensive and monopolized activities such as steel means supra-competitive markups and barriers to entry in products used as intermediate inputs by more labor-absorbing activities (notable in a country in which unemployment rates have been above 30 percent). This applies as equally to broadband pricing by the incumbent fixed-line operator as to the monopoly pricing of steel and basic chemicals for the competitiveness of downstream manufacturing.

The South African Act broadly adopts a total welfare standard. The objectives place economic efficiency and the opportunity for small and medium firms to participate alongside consumer welfare. The specific abuse of dominance provisions that pertain to exclusionary

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<sup>10</sup> See S. Roberts, *Assessing Excessive Pricing—The Case of Flat Steel in South Africa*, 4 J. COMPETITION L. & ECON. 871-891 (2008).

abuses generally require demonstration of an anticompetitive effect that outweighs any pro-competitive, technological, or efficiency gain. In the historical context of the South African economy and the need for more effective competitive rivalry as part of transforming the economy to be more dynamic and adaptable, the Commission views it important to address the ability of dominant firms to entrench such positions and obtain their returns from them. This is especially so in priority sectors, identified by the Commission because of their importance for economic development and the negative impact that anticompetitive conduct may have.

### *C. Priority Sectors*

Over the past year, the Commission has developed its position with regard to prioritization related mainly to having a greater impact from its enforcement actions. The prioritization approach relates both to the determination of priority sectors and the basis on which specific cases will be prioritized.

The three main criteria for the wider prioritization of sectors and cases are: (a) the impact on poor consumers; (b) their importance for accelerated and shared growth; and (c) the likelihood of substantial competition concerns based on information the Commission gathers from complaints and merger notifications. As the most egregious breaches of the Competition Act, cartels are unsurprisingly a focus in their own right, with the CLP proving effective in increasing their detection and prosecution.

The Commission is also taking a more proactive stance in the four selected priority sectors. In each sector, the Commission is reviewing available data and evidence on potential anticompetitive conduct. This may then lead to more specific investigations and initiation of formal complaints in what will generally be a multi-year program of work. The sectors identified in 2008 are.

- Food and agro-processing.* Agricultural markets were among the most regulated by the apartheid government. In 1996, two years after the first democratic elections, the government swept aside the Control Boards that had governed the marketing and price determination of most agricultural products in the interests of the predominantly white farmers. These farmers had also been supported by tariffs and quotas on imports and subsidized finance. Co-operatives had also had a very important role to play in the provision of inputs and the storage, processing, and packaging of products. The cartel behavior uncovered in recent years in areas such as dairy products, bread, and maize meal suggests that the private concerns in agro-processing and food have engaged in far-reaching anticompetitive behavior to the disadvantage of both consumers and farmers. The importance of food to poor consumers and the high levels of poverty in South Africa mean this has had a particularly negative impact on welfare. Moreover, the impact on the returns from farming clashes with the government's objectives to support entry of black farmers into commercial agriculture and to broaden rural development.
- Infrastructure and construction.* An important component of the government's plan to achieve more rapid growth is a far-reaching program of investment in infrastructure. After sustained economic growth over the past decade, infrastructure is now a major bottleneck that is being urgently addressed, led by investments in transport and energy by the major parastatals in these areas. Anticompetitive behavior increases the costs of this state-led investment as well as more broadly raising the costs of investment by private firms. Internationally, there have been high profile investigations into construction and infrastructure projects such as by the Netherlands' NMa and the U.K.'s Office of Fair Trading, which have uncovered extensive bid-rigging. The close-knit nature of the South African

business community as well as the apartheid legacy of regulation by government and industry groups suggests that it may well be a problem in South Africa.

Indeed, there have already been several leniency applications received in this broad sector, including regarding structural steel products, cast concrete products, and plastic pipes where investigations and prosecutions are proceeding.

- *Banking.* Following mounting concern about the level of bank charges and the arrangements governing the payments system, the Competition Commission launched an inquiry into these issues with an independent panel of experts.<sup>11</sup> Although participation was voluntary, all the major banks did so. The inquiry report was completed in June 2008, at which point the Commission began its review of the recommendations in consultation with other relevant stakeholders such as the National Treasury and the Reserve Bank.
- *Intermediate industrial products.* The South African economy is unusual in developing a strong industrial base in heavy industry but relatively weak capacity in more diversified manufacturing. The comparative advantage in capital-intensive intermediate industrial products comes despite the high levels of unemployment, especially among those with low skill levels. The skewed industrial base is due to South Africa's resource endowment, its having the cheapest electricity in the world, and its receiving the extensive support of the apartheid government.<sup>12</sup> Under apartheid, the government sought to develop strategic industries such as steel, but did not want to encourage labor-intensive manufacturing. The apartheid government also did not support broad-based consumer demand, instead seeking to limit the participation of black people in the economy, including in education and

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<sup>11</sup> For details of the inquiry, including Terms of Reference and submissions, see Competition Commission of South Africa, Banking Enquiry, at <http://www.compcom.co.za/banking>.

<sup>12</sup> A. Black & S. Roberts, *The Evolution and Impact of Industrial and Competition Policies*, in J. Aron, B. Kahn, & G. Kingdon (eds) SOUTH AFRICAN ECONOMY POLICY UNDER DEMOCRACY (2008, forthcoming).

training. The legacy is entrenched dominant industries with a low cost base, but that may charge local customers monopoly prices on an “import parity” basis even where there are substantial net exports.

Notably there have been no formal market inquiry provisions in the South African Competition Act prior to the amendments discussed below. Therefore, the focus on these sectors is based on voluntary cooperation, not the power of the Commission to summon information or conduct search and seizure type operations. These powers become available only if and when there is evidence to indicate reasonable grounds for suspecting anticompetitive breaches of the Act by identified companies, leading the Commission to initiate a complaint.

### **III. OUTLOOK**

In the next three to five years, the main challenge for the Commission is to continue to build on the existing platform described above. As the Commission’s impact increases, it can expect to be subject to greater demands and scrutiny of its actions, especially in delivering on its mandate to address anticompetitive conduct and to demonstrate the benefits of doing so. This will involve explaining the benefits of active competitive rivalry in specific sectors where a cartel has been uncovered or where exclusionary abuses have been addressed. The Commission will also face a growing need to work with government departments, other regulators, and public agencies to ensure the roles of the competition authorities are understood, including how they fit into the bigger competition picture. This clearly implies greater attention to advocacy going forward.

The expectations on the competition authorities have been starkly brought home in the amendments going through Parliament at the time of this writing.<sup>13</sup>

#### *A. Amendments*

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<sup>13</sup> September and October 2008.

The amendments currently under consideration by Parliament give the competition authorities greater powers in four main areas:

- *Market inquiries:* An inquiry can be conducted by the Commission on its own initiative or on request from the Minister of Trade and Industry “(i) if it has reason to believe that any feature or combination of features of a market for any goods or services prevents, distorts or restricts competition within that market; or (ii) to achieve the purposes of [the Competition] Act.” The terms of reference must be published in the *Government Gazette* and the Commission must publish a report at the end of the inquiry. The report may include recommendations on policy, legislation, or regulation, with the Commission also being able to initiate complaints arising from the inquiry. While the Commission has been able to study a particular sector or market on its own initiative (and has done so in several cases), the main feature of the amendment is that the Commission now has the power to require information from firms as part of such an inquiry.
- *Complex monopolies:* The amendment specifies that complex monopoly conduct is that which has the effect of substantially preventing or lessening competition in a market if (a) at least 75 percent of goods or services in a market is supplied by five or fewer firms, and (b) two or more of these firms conduct their business affairs in a conscious parallel manner without agreements among themselves. Firms can demonstrate that technological, efficiency, or other pro-competitive gains outweigh the anticompetitive effect. The Commission can investigate conduct if it has reason to believe that complex monopoly conduct exists and can apply to the Tribunal for a declaratory order against two or more firms if (a) at least one of the firms has at least 20 percent of the relevant market, and (b) if the conduct has resulted in high entry barriers, exclusion of other firms, excessive pricing, refusal to supply other

firms within that market, or other market characteristics indicating coordinated conduct. The Tribunal may make an order pertaining to the conduct of the firm(s) to address the anticompetitive effects of such conduct. Contravention of the order is designated as a prohibited practice.

- *Criminal sanctions for cartel offenders:* A director of a firm or a person in a position of management authority commits a criminal offence if the person causes the firm to commit the cartel offence (section 4(1)(b) of the Competition Act) or the person knowingly acquiesces in the firm engaging in the conduct. The person would be prosecuted by the National Prosecuting Authority following a finding by the Competition Tribunal or Appeal Court that the firm committed the cartel offence or a consent order being issued with regard to same. This impacts the application of the CLP of the Commission to the firm as, by applying for leniency, the directors and management may incriminate themselves. The amendments allow the Commission to certify a person as “deserving of leniency” and to make submissions to the National Prosecuting Authority in that regard.
- *Concurrent jurisdiction:* The amendments establish concurrent jurisdiction of the competition authorities and other regulatory authorities with regard to an industry or sector subject to sector-specific regulation by which the Competition Commission will exercise primary authority with regard to prohibited practices and merger review. The administrative manner in which concurrent jurisdiction is to be exercised must be determined through agreement between the Competition Commission and the other regulatory authority. Concurrent jurisdiction had been contemplated prior to the amendments; however, issues of jurisdiction have bedeviled competition cases in recent years, especially in telecommunications cases.

These amendments have passed through the parliamentary committee process and the National Council of Provinces. At the time of writing, they still have to be voted on in the National Assembly, following which they will be signed into law by the president of the Republic. If passed, as is expected, the amendments will clearly have a significant impact on the activities of the Competition Commission.

#### *B. The Commission as a Knowledge Organization*

To deliver on its mandate regarding the major challenges it faces requires the Commission to continually strengthen its capacity for analysis and enforcement. At the same time, the legal and economic consulting fraternities have grown to provide to cases the services required by private parties. In addition, the increasing attention to competition policy around the world has meant competition practitioners have become more mobile internationally. These factors have been reflected in escalating salaries in the private sector and a relatively high staff turnover, with several staff members being attracted to competition authorities in Ireland and New Zealand as well other regulatory bodies in South Africa.

In response, the Competition Commission has focused on building effective knowledge management practices in the organization together with ongoing training and nurturing of international links that make the Commission an attractive and challenging place for those wishing to advance their careers. The focus on the Commission as essentially a knowledge institution is linked to improving the methodology which generates the knowledge at the heart of case analysis, and the collation, storage, and retrieval of information that builds the knowledge base of the organization.

The knowledge base and practices are key to a more strategic approach to the Commission's work, from prioritization through to an understanding of impact and the ability to do authoritative advocacy work. It also enables the Commission to adapt to the mobility of personnel and skills by ensuring retention of the information and knowledge generated.

Finally, the Commission is increasingly looking at its role in the context of the development of competition authorities in the southern African region and on the African continent as a whole, and is actively promoting greater cooperation between agencies. In this regard, the Commission is participating in regional groupings, in particular the Southern African Development Community, as well as developing stronger bilateral relationships.