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FOREWORD

As soon as the new government came into power in 2004, it announced its resolve to promote healthy competition in the market place with professionally run regulatory institutions. This timely report assembled by Pradeep S. Mehta and his team has taken stock of the progress on the competition scenario in India as the government has reached a mid-term point, thus offering an insight on where we are, and where do we need to go.

I do not propose to argue the case of how competition promoting measures can help higher economic growth, which has been done eloquently in the first chapter: Prologue--An Overview. Added to this, how should the future agenda be steered, with time lines, has been elucidated in the last chapter: the Epilogue--Way Forward.

The report has captured all possible elements of the market dynamics vis a vis promotion of competition. It has also looked at some sectors, such as telecom and electricity in the area of infrastructure and in the equally crucial area of social infrastructure like health care and education, as case studies. Many other crucial issues will be covered in its next edition in 2009. It is also hoped that this report will become a regular biennial feature.

One unique feature of the report is an assessment of the popular perception of the scene in the country through an index. The sample is a robustly constructed number with a healthy mix of informed stakeholders, which has been described in the report, and I do not wish to say more at this point. It shows that while the landscape on competition is not too bright, it is also not bad. Things have changed since the reforms began, and people do acknowledge the same. But is that enough? That is the question which this report raises and answers.

In the past, the Indian economy was characterised by significant government involvement marked by dominance of large state-owned public sector enterprises. India embarked on the path of economic reforms during 1990s by shifting to market-driven economic policies. The thrust of reforms has been to preserve and promote competition as a means to ensure efficient allocation of resources, resulting in the best possible choice of quality, the lowest prices and adequate supplies to consumers.

Competition & Regulation in India - A Status Report

Most importantly, unlike many other reforming economies, India is following a mixed-economy approach, where the public sector is required to compete with the private players, rather than handing over the public sector units to the private sector. Examples of these include: airlines, telecom etc. Exceptions include the electricity sector, while other sectors are being opened up gradually. On the one end of the spectrum, we have one of the lowest rates in the telecom sector with large number of private players. On the other end we have the electricity sector, where we there is hardly any competition and thus poor growth and a huge supply shortage. This conundrum raises two critical issues. Firstly that of competitive neutrality i.e. providing a level playing field for all. The other one is the overlap of the competition authority vs. sectoral regulators. These two issues have been addressed in some depth in this report.

In any economic system, the state can play many roles of which three can be identified as important. There are: (1) as a producer of marketable goods and services, (2) as a regulator of the system, and (3) as a supplier of “public goods” and “merit goods” like primary education and public health.

The decreasing role of state as a producer of marketable goods and services and the increasing role of market in such areas simultaneously enhance the role of state as a “regulator” and “facilitator”. The regulatory role comes into play in order to maintain competitive conditions in the market and to ensure that every one follows the basic rules of the game. These issues have been assessed in this report in some depth, and a future agenda has been outlined succinctly.

Since the advent of economic reforms in India, there have been considerable changes in our policy arena, with increased reliance on market forces. Along with policy changes, we have also adopted a new competition law in 2002 as a follow up to our market oriented economic reforms. The new law has been amended in 2007 and should be fully operational soon. Additionally, we have regulatory laws in several sectors, opened up for private players, which were hitherto reserved for public sector. This upsurge in interest in competition and regulatory laws in India reflects the substantial changes that have been taking place in the policy paradigm.

The productivity and efficiency benefits associated with markets can be reaped only if the market remains competitive. Legislation is required to prevent the degeneration of the market structure to a monopolistic or a near monopolistic situation.

Our new competition law therefore seeks to: a) prohibit anti-competitive agreements (including cartels) which determine prices, limit or control or share markets or results in bid rigging, etc., b) prohibit abuse of dominant position through unfair or discriminatory prices or conditions (including predatory pricing) limiting or restricting production or denying of market access, etc., and c) regulate combinations, (i.e., mergers, acquisitions, etc.) that cause or are likely to cause an appreciable adverse effect on competition.

Competition & Regulation in India - A Status Report

Regulating cartels and abuse of dominance are two crucial action areas for the new competition authority, as well as the sector regulators. The issues surrounding these two enforcement challenges have been captured in the report with several examples from our own history and other countries. The implementation of the competition law is not without its problems. Whether it be with respect to anti-competition agreements or the abuse of the dominant position or mergers and acquisitions, the critical question to examine is whether a particular decision or action has had the effect of reducing competition. There is, of course, the standard controversy between the structuralist and the behavioural approaches. Two important elements of market structure are market concentration and barriers to entry. Any action by a firm which increases either concentration or the barriers to entry will be deemed, under the structuralist approach, as violative of the maintenance of competition. On the other hand, the behavioural approach looks at the conduct of the firm rather than structural infringements. The structuralist approach minimizes the cost of enforcement because it removes the requirement to show that an arrangement is harmful. However, there is no way by which any competition or regulatory authority can get away without establishing that a particular action has had an adverse effect on competition. It needs to establish what actions and under what circumstances will they constitute violation of the principles of competition.

The other dilemma is on how to strike a balance between competition policy and industrial policy. Many argue that we need to have global size players (national champions) to be able to compete in the global economy, while many argue that we need fleet footed players to be able to compete in the global economy. In regard national champions, the examples from post-war Japan and Korea are quoted, which protected their domestic industry by tariff protection, regulated entry and thus created national champions. However with good hindsight they too allowed a large number of domestic players, in sectors such as steel, automobiles and electronics, thus creating healthy competition at home. It is only then that the Korean and Japanese manufacturers could become competitive in the global economy. However, the situation has changed hugely since then aided by the WTO etc, and we cannot take similar approaches in developing our industrial sector. Or local firms do need to face competition at home to be able to compete globally, otherwise if the state has to give them extra protection or leverage, we may end up with crony capitalism, a question raised by the Prime Minister at a meeting in New Delhi in June, 2007.

While competition authorities exist to maintain competition, regulatory authorities for various sectors have also come to occupy an important place. Where competitive markets cannot exist, the regulatory authorities mandate is to mimic competitive outcomes to the extent possible. Infrastructure sectors like power fall mainly in this category. States also generally use regulation with a broad connotation to achieve a wide range of non-market objectives such as ensuring universal and equitable access, consumer protection and maintain safety and healthy standards. More importantly, it identifies and addresses subsidies and cross-subsidies in the provision of services. This, however, is a potential area of political intervention. Government often finds means to get around regulator's prescriptions in relation to subsidies, if they are found to be politically inconvenient.

Competition & Regulation in India - A Status Report

Apart from political interference, the existence of large number of sectoral regulators together with a competition authority may raise the issue of overlap and conflict. The ideal solution could be to legislate clear mandates for regulators and the competition authority. It is best to leave the determination of competition principles to the competition authority. Across sectors, some common principles of competition must prevail.

Establishment of competition authority by itself does not resolve all problems relating to the creation of competitive conditions. Unless there is a strong political will, even the competition and/or the regulatory authority may not be able to function effectively. However, in order that competition may prevail, competition and regulatory laws need to be supplemented by an appropriate Competition Policy which will ensure a full play of competitive forces. Such a programme must oversee all government policies so that there is no intended or unintended adverse impact on competition. In general, there should be no barriers to entry. In some areas, minimum criteria for entry may be prescribed. These prescriptions should strictly be in the nature of prudential norms. A move in this direction has been made by the Planning Commission as a part of the exercise on the 11th Plan Document. That needs to become a part of the public discourse, and then head towards an implementable resolution of the Government. Once adopted as public policy, an assessment must be done of all policies and practices of the government to draw out and be removed, so that markets function fairly. This report has dealt with the evolution and framework of a Competition Policy in India, and is worthy of reading.

Efficiency is associated with competition. In order to maintain competitive conditions, three things are needed. First, there should be appropriate competition laws to prevent market abuse. This is preventive in character. Second this must be supplemented by competition policy which will ensure that all government policies tend to promote competition. This has a positive dimension because there are many policy-induced anti-competitive outcomes, which have been captured well in the report. Third, sectoral regulation becomes important in areas where there are natural monopolies. Under such circumstances, it is necessary to establish appropriate relationship between sectoral regulators and the competition authority. The political economy constraints need to be taken into account while framing competition and regulatory laws and more importantly in drafting competition policy. But if the government is truly committed to a process of liberalisation, this should become less of a problem. Only if reform is introduced by stealth it becomes a hurdle.

I am indeed happy that CUTS International have brought out this report, the first of a series, to explore many issues relating to an effective enforcement regime for competition and regulation. I commend this report to all, who wish to see India progress faster and deliver economic growth with equity.

[C. Rangarajan]