COMPETITION DISTORTIONS IN INDIA – A CUTS DOSSIER

(CDI-38: October to December, 2017)

For earlier Dossiers please see: http://www.cuts-ccier.org/Competition_Distortions_India.htm

Periodic dossiers look at the interface of policy issues which have an impact on competition in India. Such impact could be negative, positive or mixed, depending on sectors and markets. In these dossiers, news as published is utilised without verifying its accuracy, but ensuring its veracity.

The purpose is to flag issues and provide food for thought to the layman as well as to the policymakers and regulators. A detailed analysis has not been undertaken as it would require deeper examination of the issues, particularly in terms of cost and benefits.

We are pleased to present to you the CUTS Competition Distortion Dossier Edition No: 38 for the quarter of October-December 2017. As always, we have attempted to capture interesting stories having an impact on competition, in sectors such as energy, steel, digital finance and telecommunications.

In continuation with the theme of the previous issue, we discuss potential impact of continued protectionist policy decisions in favour of domestic firms. These can alter collective firm behaviour to the larger detriment of a particular sector, thereby hampering consumer welfare and global competitiveness in the long-run. Furthermore, we highlight how sub-optimal implementation of certain market regulatory tools to meet public welfare objectives can distort competition and possibly have the opposite impact. Important pro-competitive measures in sectors such as power, digital payments and telecommunications have been elucidated as well.

Contents

A. Trade Policies

1. Anti-dumping duty imposed on certain Chinese, EU steel products

The Indian government imposed anti-dumping duty on imports of certain flat steel products from China and European Union (EU) for five years to guard the interest of domestic players from cheap in-bound shipments. The duty was imposed after the Commerce Ministry's Directorate General of Anti-Dumping and Allied Duties (DGAD) recommended duty on such imports. In its findings, the DGAD had concluded that 'colour coated/pre-painted flat products of alloy or non-alloy steel' has been exported to India from these regions at below the normal value, due to which domestic industry has suffered material injury.

http://www.moneycontrol.com/news/business/economy/antidumping-duty-imposed-on-certain-chinese-eu-steel-products-2415203.html

Food For Thought

As discussed in previous editions of the CDD, the Government of India has constantly pursued protectionist measures in the steel industry. We have been arguing that the imposition of anti-dumping duty for longer periods of time can artificially constrain fair competition and harm the consumer. This is starting to play out already as the current market scenario in the Indian steel industry is tending towards growing concentration.

The top players in the sector are eyeing smaller ones and have reportedly successfully lobbied for protectionist trade measures like anti-dumping duties and simultaneously raised the prices of their products by almost 20 percent.[1] *With anti-dumping measures continuing, competition in the downstream market is also being affected. For instance, while steel makers exploit the protectionist measure to their advantage by increasing prices, the cost of production of downstream users increases, thereby impacting the competitiveness of employment-oriented user industries, mostly in the small and medium enterprise (SME) sector.*[2] *In short, the rising steel price has given a tough time to other industries, which use steel as a raw material.*[3] *Furthermore, despite the fact that top steel producers are reeling under the burden of Non-Performing Assets (NPAs), they have still tended to gulp small debt-ridden players in order to gain greater control over the market. To this end, they have also argued and lobbied in favour of protectionist measures. In effect, they have reportedly been able to monopolise the market*

[1] See www.dnaindia.com/business/report-dna-investigation-steel-firms-playing-monopoly-passing-on-cost-to-consumers-2551927

[2] See https://economictimes.indiatimes.com/industry/indl-goods/svs/steel/steel-makers-misusing-protectionist-measures-eepc-india/articleshow/62528158.cms

[3] See www.tribuneindia.com/news/ludhiana/industry-to-go-on-strike-from-jan-11/520381.html

and smaller producers (which are facing debt crunch) continue to accumulate losses and record negative growth numbers.[4]

In the absence of adequate competitive constraints in the domestic industry, concentration would further increase, thereby raising entry barriers and resulting in consumer welfare loss. Although it is known that both competition and anti-dumping laws originated with the same objective of promoting free and fair competition in the market;[5] *the present scenario suggests that levying anti-dumping measures for longer periods and without actual requirement might actually distort domestic competition and introduce an unfair and anticompetitive element. Granting protections to domestic players also influences and encourages them to utilise such measures to their maximum advantage, which usually ends up harming consumers as well as SMEs.*

2. Government starts safeguard duty probe on solar cells

India has started a probe to determine imposition of safeguard duty on surging imports of solar cells with a view to protecting domestic manufacturers. Domestic manufacturers had approached the Directorate General of Safeguards (DGS) with a complaint that their market shares have remained stagnant despite rapid expansion in demand for solar cells in the country. Solar cells, electrical devices that convert sunlight directly into electricity, are imported primarily from China, Malaysia, Singapore and Taiwan.

http://www.thehindubusinessline.com/economy/govt-starts-safeguard-duty-probe-on-solar-cells/article10001892.ece?utm_source=email&utm_medium=Email&utm_campaign=Newsletter

Food For Thought

India's installed solar capacity is expected to reach 20 gigawatt (GW) by the end of the present financial year and by 2022, India is targeting to reach the 100 GW mark.[6] *Most definitely, reaching the century mark would require a major and consistent policy-push. However, protecting domestic players by imposing safeguard duty might be counterproductive to the government's capacity installation goals.*

This is primarily because rather than protecting the domestic industry, the imposition of safeguard duty can raise equipment costs, thereby impacting price competitiveness of solar

[4] See www.dnaindia.com/business/report-dna-investigation-steel-firms-playing-monopoly-passing-on-cost-to-consumers-2551927

[5] See www.ijrra.net/Vol2issue4/IJRRA-02-04-37.pdf

[6] See http://pib.nic.in/newsite/PrintRelease.aspx?relid=173830

power and increasing the tariff borne by end consumer. This can hinder India's shift from conventional modes of power generation to its renewable counterparts like solar. While the government's objective is to rightly improve the quality and manufacturing capacity of India's solar equipment manufacturers, it also needs to concurrently retain the price competitiveness of solar power so as to ensure that it remains a viable alternative for Indian consumers.[7] *Besides, the capacity of domestic firms to replace the imports following the imposition of the safeguard is questionable as they have a lot of challenges, which would imply that the imports would continue to come albeit at a higher price due to the duty component.*

This means that the imposition of safeguard duties and other import restrictions might not be the real solution to challenges being faced by the domestic industry. These include lack of economies of scale, lack of vertical integration in the supply chain and lack of an ecosystem to build technical expertise. In order to tackle these challenges, policies should ideally focus on unshackling the growth constraints to domestic industry and making it more competitive. Experts have also highlighted the need to explore alternative mechanisms by stating that, "better to encourage people to buy Indian modules with some sort of financial incentive than to punish buyers of modules with tariffs that will be unlikely to result in thriving manufacturing industry and will further strain India's already painful margin situation."[8]

B. Policies Inhibiting Competition

3. Government plan may bring non-essential drugs under price control

A proposed amendment to the four-year-old Drug Price Control Order (DPCO) aims to bring non-scheduled drugs under price control by changing the price setting method. Non-scheduled drugs are those that are currently outside the price-control regime. About 370 drugs are currently under price control.

The proposal by the National Pharmaceutical Pricing Authority (NPPA) and the Department of Pharmaceuticals (DoP) suggests scrapping the current method of fixing the ceiling price of drugs on the National List of Essential Medicines (NLEM) by adopting the simple average of brands having market share of over one percent and instead taking the simple average of all brands and generics.

http://economictimes.indiatimes.com/articleshow/61185270.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst

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[7] See https://energy.economictimes.indiatimes.com/energy-speak/how-would-anti-dumping-duty-impact-india-s-solar-sector/2660

[8] See remarks of Paula Mints at: www.thehindubusinessline.com/specials/clean-tech/an-unwarranted-change-in-stance/article9898298.ece

Food For Thought

A drug price control mechanism seeks to enable broad access to reasonably priced medicines and simultaneously allows enough R&D incentives for pharmaceutical companies to invest in innovation, thereby maintaining a balance between two goals and promoting efficient market outcomes. As per the current Indian framework, any company that wants to launch a new scheduled drug has to apply to the drug regulator (NPPA), which fixes the retail price accordingly. Companies that launch a combination or single dose drugs that were not part of the essential list before 2013 continue to remain outside price control. However, under the new proposal, if a company is launching a new drug that might be a combination of a scheduled and a non-scheduled drug that was not part of the essential list, the regulator will fix the ceiling price of the drug. Under the draft amendment, this will be based on the price applied by the manufacturer that takes a lead in seeking approval for the new drug. Patented drugs will not fall under this formula.

This proposed move is naturally expected to impact the aforementioned balance and the Indian Pharmaceutical Alliance (IPA), a group of leading domestic drug companies, highlighted its possible distortionary impact on innovation incentives and raised concerns by stating that such an amendment could 'kill competition and compromise growth'. The price control mechanism is generally utilised to lower individual drug prices, but this generally happens at the cost of discouragement to investment. Competition is compromised when there is a genuine possibility that the competitive market process (sans price control) can lead to optimal pricing.

This proposed amendment is a part of the broader initiative of the government to make healthcare affordable and previous moves in this direction have been covered in Editions 36 and 37 of the CDD.[9] *Although the intent is in the right place, the regulator and government should bear in mind the fragile nature of the pharmaceutical industry and the need to maintain the right balance between affordability and the incentives to invest.*

Although price control is widely used across the globe, it remains a controversial tool which has the potential to impact profit margins (when set too low) or impacting generic competition (when set too high).[10] *Therefore, a balanced formula for calculation of price-control is a must which incentivises the industry as well as benefits the consumer (taking the simple average of all brands and generics seems to impede the incentives to invest).*

[9] Available at: www.cuts-ccier.org/pdf/CDIDossier-Apr%E2%80%93Jun2017.pdf and www.cuts-ccier.org/pdf/CDIDossier-Jul-Sept2017.pdf

[10] See www.cuts-ccier.org/pdf/Is_there_a_Bright_Future_Ahead_for_Indias_Pharmaceutical_Market.pdf

4. Mergers involving Central oil and gas PSUs exempt from Competition Commission nod

Combinations including mergers, acquisitions and amalgamations involving Central Public Sector Enterprises (CPSEs) operating in the oil and gas sector have been exempted from seeking the nod of the Competition Commission of India (CCI) for five years.[11] The move, which is being carried out in 'public interest', comes even as the government said in a statement that it was undertaking a number of key economic reforms to fuel the growth and that these included 'consolidation of government-run oil companies'.

www.thehindu.com/business/Industry/mergers-involving-central-oil-and-gas-psus-exempt-from-competition-commission-nod/article20697454.ece

Food For Thought

The move to exempt combinations operating in the oil and gas sector lies in consonance with the government's broader explicit goal of merging oil public sector undertakings (PSUs) into an integrated oil behemoth. The intent therein is to create an entity which can compete internationally with companies, such as Exxon, BP, Shell, Chevron, and Tota.[12] The underlying rationale is that such consolidation will enable the new entity to benefit from economies of scale and will impart an ability to invest in large projects.

However, experts have highlighted the inherent dangers of such a move. First of all, in the absence of scrutiny by the national competition regulator, creation of a behemoth will/can have an appreciable adverse effect on competition and might create an entity having unbridled power over India's power sector as well as provide the entity the ability to influence the future strategy and implementation of policies in the sector.

Secondly, it has been highlighted that the rationale of economies of scale does not hold true as the cost of discovery or cost to produce does not depend on the size of the company, but on the ability, technical prowess and expertise of the entity.[13] There appear to be several considerable costs involved in the process, especially to competition and consequent harm to the consumer. Hence, it might be beneficial for the Central government to either revisit the rationale of providing this exemption or provide definite, quantifiable and objective criteria which could justify that the move in fact lies within the wide and undefined scope of the 'public interest' provision. Setting such criteria will be useful in objectively evaluating similar proposals in future.

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[11] Notification available at: www.cci.gov.in/sites/default/files/notification/Notification-22.112017.pdf

[12] Shenoy Bhamy V., *Does India Need a Giant Integrated Oil Company?*, EPW (April, 2017)

[13] *Ibid*

The redeeming feature is that such merged entities are not exempt from the Competition Act per se, which means that if there are any market failures, the CCI could be approached by the victims/interested parties.

C. Policies Promoting Competition

5. Government plans to allow consumers to switch power service companies

Consumers will be able to change their power suppliers just like telecom services, after a proposed amendment to the existing Electricity Act is approved. Changing the *status quo*, the Electricity Amendment Bill provides for segregating the distribution network business and the electricity supply business. This separation was not previously present and was impeding consumers from effectively switching power companies. The separation will give consumers an option to choose from multiple electricity service providers. The bill would also provide direct benefit transfer of subsidy to farmers to improve efficiency in power consumption.

https://timesofindia.indiatimes.com/business/india-business/govt-plans-to-allow-consumers-to-switch-power-service-companies/articleshow/61902767.cms

Food For Thought

India's energy demands are growing rapidly, driven by several factors including urbanisation and industrialisation. Future increase in energy consumption is inevitable and the electricity sector is expected to play a leading role in the energy mix. In this backdrop, power supply portability and separation of distribution from supply appears to be a step in the right direction and is bound to reinvigorate competition in the electricity sector.

This changes the current scenario, wherein the power distribution utilities are responsible for operating and maintaining the distribution system in their licenced areas. As state distribution companies (which currently enjoy a monopoly position) will face competition, investment in the sector is expected to increase. The amendment will also positively impact quality, availability, affordability and reliability of electricity supply. Theoretically, it will make switching costs negligible and will empower the consumer.

However, while promoting competition at the retail level for better and more cost-effective service delivery to end consumers is justified, the approach suggested is also prone to rent-seeking and with the existing weak distribution network, the proposed segregation will be unviable. Proper implementation and requisite readjustments in this regard will make this *policy a win-win situation for all relevant stakeholders and would be beneficial to improving the financial health of the sector.*

6. Interoperable mobile wallets in 6 months

The Reserve Bank of India (RBI) directed companies and banks to make know-your-customer-compliant prepaid payment instruments (PPIs), such as mobile wallets, interoperable amongst themselves through Unified Payments Interface (UPI) within the next six months. UPI is a payments system launched by National Payments Corporation of India (NPCI) in August 2016 that facilitates instant fund transfer between two bank accounts on a mobile platform, without having any details of the beneficiary's bank. KYC is a process through which financial institutions verify information about customers to ensure services are not misused.

www.livemint.com/Industry/lOITgGgnJLidZJU5m0IMbP/Interoperable-mobile-wallets-in-six-months-RBI.html

Food For Thought

Interoperability is the ability for different systems to connect with one another. Interoperable payment systems make it easier for people to send payments to anyone and receive payments from anyone quickly and affordably.[14] *From the perspective of financial service providers, interoperability promises to decrease market entry barriers and opens up the market to new business opportunities and novel products. It opens up established proprietary payment systems and gives an opportunity to all competitors to achieve economies of scale, thereby increasing competition. From the perspective of policymakers, interoperability promotes higher adoption of digital financial services, increases volume of transactions and is a means to bring the financially excluded into the financial system, thus fostering financial inclusion.*[15]

Enabling interoperability between PPIs is an initiative in the same direction and in principle appears to be a pro-competitive move. However, the fact that all PPIs are to be made interoperable through UPI seems to be a sub-optimal solution. As UPI is a bank-led payment system, it acts as an actual competitor in the payments landscape. Making all PPIs interoperable through UPI does not fix the much talked about level-playing field issue.[16]

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[14] See www.cgap.org/sites/default/files/interoperability.pdf

[15] See www.cgap.org/sites/default/files/interoperability.pdf; www.cuts-ccier.org/pdf/Facilitating_Interoperability_in_Digital_Finance_Services%20_in_India.pdf and www.cuts-ccier.org/pdf/Enabling_Effective_Competition_in_Mobile_Money_Market.pdf

[16] See www.cuts-ccier.org/Payments-Infrastructure/pdf/Level_The_Playing_Field_To_Leverage_The_Potential.pdf and www.cuts-

In order to truly leverage the potential of digital payments (and DFS generally), what is required is direct and interoperable access for non-banks to Real Time Gross Settlement (RTGS) platform which is currently being operated by the RBI, wherein direct and interoperable access to non-banks is missing.[17]Also, there is scope for infusing competition at the NPCI level so that the payments systems such as UPI itself face competitive constraints and the Indian regime makes rooms for innovations in the payment platforms business.

7. TRAI backs net neutrality with recommendations, opposes any discriminatory treatment of data

After more than a year of debate, the Telecom Regulatory Authority of India (TRAI) said it opposed any 'discriminatory treatment' of data, including blocking, slowing or offering preferential speeds or treatment to any content. TRAI recommended that, 'the licencing terms should be amplified to provide explicit restrictions on any sort of discrimination in Internet access based on the content being accessed, the protocols being used or the user equipment being deployed'.

www.thehindu.com/sci-tech/technology/internet/trai-backs-net-neutrality/article21037516.ece

Food For Thought

The principle of net neutrality entails that Internet Service Providers (ISPs) should enable access to all content and applications regardless of the source, and without favouring or blocking particular products or websites. In the absence of net neutrality, broadband service providers could potentially give preference to some content providers over others for a certain price. Practically, this would mean that bigger content providers, who can afford to pay the extra buck, would be able to access 'fast-lanes' in the internet ecosystem and thereby deliver content faster (at the cost of slowing down others).[18] It is quite evident that such a scenario would strengthen the dominance of those at the top and make it even harder for new and innovative competitors to displace the incumbents.

ccier.org/Payments-Infrastructure/pdf/Draft_Research_Report-Competition_assessment_of_payments_infra_in_India.pdf

[17] For instance, see www.openbanking.org.uk/

[18] See www.wired.com/story/why-net-neutrality-matters-even-in-the-age-of-oligopoly/

TRAI's move in support of net neutrality principles evidently promotes the creation of a level-playing competitive field and ensures that the internet remains open so that all content providers can compete effectively sans discrimination. Its importance also lies in the fact that it encourages fair access to the internet and protects consumers from having the cost of internet go up (in the absence of such a provision, consumers might have to pay more for fast lane tolls). It keeps the competitive and open spirit of the internet intact and ensures that the next Facebook or Google can grow and compete without fear of discrimination.[19]

DISCLAIMER:

This information has been collected through secondary research and CUTS C-CIER is not responsible for any errors in the same. The press clippings used here have been suitably adapted/summarised to convey their essence to the reader without any distortion of content.

[19] See www.cuts-ccier.org/pdf/Advocacy-CUTS_Comments_on_Net_Neutrality.pdf