COMPETITION DISTORTIONS IN INDIA – A CUTS DOSSIER

(CDI-42: October to December, 2018)

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: 42 for the quarter of October-December 2018. In this edition, we continue to cover stories of distortionary trade policies in the steel and renewable energy sectors.

Moving on to the digital economy, we first cover the digital communications sector where Telecom Regulatory Authority of India (TRAI) is contemplating regulation of Over-The-Top communication services, such as WhatsApp. Additionally, we address the distortions that could emanate from the government's recent policy measure that bars e-commerce marketplaces from exercising actual ownership over the inventory and restrict their ability to predominantly sell their own products or products of those companies over which they hold significant control.

We also cover initiatives that could contribute positively to competition. These include setting up of the Competition Law Review Committee – which is an opportunity to readjust India's competition regime to address changing economy-wide circumstances. Lastly, we highlight policy initiatives by the Reserve Bank of India, i.e. enabling mobile wallet interoperability and setting up of a Public Credit Registry which could help promote competition in the digital payments and credits market respectively.

Contents

A. Trade Policies

1. India Imposes Anti-dumping Duty on Chinese Steel Products

India has imposed anti-dumping duties of up to US$185.51 per tonne for five years on certain varieties of Chinese steel to guard domestic players from cheap imports from the neighbouring country.

In its anti-dumping investigation, the Directorate General of Trade Remedies (DGTR) stated that dumped imports of 'straight length bars and rods of alloy steel' from China have increased in absolute terms during the period of probe (2016-17). While recommending the anti-dumping duty, DGTR said the goods have been exported to India from China below normal value and India's domestic industry has suffered material injury on account of the imports.

Source: https://economictimes.indiatimes.com/articleshow/66281376.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst

Food For Thought

As discussed previously (CDD Edition 41 and CDD Edition 40), anti-dumping duty is measure intended to ensure a level-playing field for domestic players and promote fair trade. However, its imposition in the long-run can have unintended consequences on the industry and consumers. These include protection of the industry from competitive pressure leading to inefficiencies and increase in input costs that are eventually borne by the consumer.

In the present context, the prolonged levy of anti-dumping duties has indeed started to show its adverse side. For instance, it was recently reported that steel prices have shot upwards by 40 percent in 2016-17 which has, in turn, started to impact India's real estate sector.[1] The manufacturers of wagons for the Indian railways have also been impacted because steel remains the largest cost-component for wagon making.[2]

Other than this, it was also noted by a Parliamentary Committee in July 2018 that the anti-dumping measures were actually ineffective and imports of Chinese steel products

[1] See https://realty.economictimes.indiatimes.com/news/industry/significant-rise-in-steel-prices-in-past-one-year-impacting-real-estate-credai/65039020

[2] See www.thehindubusinessline.com/money-and-banking/with-steel-prices-on-the-rise-wagon-industry-finds-the-going-tough/article24961751.ece

had increased by eight percent.[3] This raises questions about the effectiveness of the duty itself and merits its detailed re-evaluation (such evaluation should include revision of the underlying rationale and a detailed impact assessment). Despite these effects, Indian steel manufacturers have regularly demanded the imposition and extension of anti-dumping duties and the same have been granted in their favour.[4] In this manner, a measure that is intended to promote fair competition might turn out to have the opposite effect that is not healthy for the main industry and other relevant industries. As mentioned earlier, the end loser of the prolonged imposition remains the consumers as they might end up bearing the increased costs of distorted competition.

Given that international prices of steel are likely to remain muted in near future and pressure from cheap imports are still prevalent, it is clear that such measures cannot fully tackle the underlying issue and improve the competitiveness of domestic firms.[5] Moreover, given the fact that the industry has become accustomed to such protection and the unsustainability of the measure itself, it is safe to say that there is a dire need to explore long-term solutions to the anti-dumping duty instead. This could entail a detailed re-assessment of the logic behind anti-dumping duties and whether it was able to reach the intended objective or not. If not, other more effective alternatives to achieve the same goal in the long-run could be explored, including re-orientation towards exports instead of depending on domestic sales alone.

2. Safeguard Duties on Solar Cell Imports

In July 2018, the Government of India imposed a safeguard duty on import of solar cells from China, Malaysia and other countries for a period of two years. The duty is to be imposed in the following manner: 25 percent for the first year, 20 percent for the subsequent six months and 15 percent in the remaining six months. We covered the preliminary effects of its application in the earlier quarter (*CDD Edition 41*). However, it was too early to gauge its effects at the time. With the duty now about to cross the 6-month milestone, we have made an attempt to track its preliminary effects in this latest quarter.

Source: www.dgtr.gov.in/sites/default/files/Solar-Final_Finding-English_0.pdf

[3] See www.theweek.in/news/biz-tech/2018/07/27/Anti-dumping-measures-against-China-ineffective-says-parliamentary-committee.html

[4] See www.business-standard.com/article/markets/domestic-steel-companies-to-urge-centre-for-anti-dumping-duty-revision-118032000043_1.html

[5] See https://economictimes.indiatimes.com/industry/indl-goods/svs/steel/domestic-flat-steel-prices-likely-to-face-temporary-pressures-from-cheap-imports-icra/articleshow/66936559.cms

Food for thought

The rationale behind the imposition of a safeguard duty is to provide temporary protection to the domestic industry from harm brought in by increased imports. Reportedly, there has been an approximate 47 percent decline in the imports of steel from the target countries during 2017-2018.[6] *Meanwhile, the market shares of domestic solar panel makers are on the rise.*[7] *However, most of the cell and panel manufacturing capacity that is located in the Special Economic Zones of India have not benefitted because they also have to pay the safeguard duty in case they wish to cater to the domestic market.*

Overall, while these might seem beneficial from the perspective of domestic manufacturers of solar cells and panels, the effect is the exact opposite on other stakeholders, primarily solar power project developers (and naturally so). Indian solar power project developers—unlike local panel makers, benefit from cheap imports.[8] *The safeguard duty has increased their costs and solar power capacity addition has slowed down.*[9] *Moreover, the decision to impose the safeguard duty has also infused policy uncertainty, thereby hurting investor sentiments and jeopardising the viability of existing solar power projects.*[10] *Experts also believe that it might directly impact the small residential rooftop customers (however, this claim would need a detailed examination).*[11]

This poses interesting and larger questions regarding the competitive landscape of India's manufacturing ecosystem, the impact on the incentive structure for business consumers, end users and India's broader renewable energy ambitions. Such a scenario ripens the opportunity and necessity to weigh the costs of this decision as against its benefits.

---

[6] See www.financialexpress.com/industry/safeguard-duty-import-of-solar-cell-declines-domestic-firms-market-shares-up/1411310/

[7] *Ibid*

[8] See https://qz.com/india/1511463/safeguard-duties-didnt-help-indias-solar-sector-in-2018/. The exact differential between imports and domestic manufacturers and any quality differential has not been explored here.

[9] *Ibid*

[10] See https://thewire.in/energy/national-solar-mission-target-india

[11] See www.electronicsb2b.com/industry-buzz/the-safeguard-duty-on-solar-imports-to-india-a-boon-or-a-bane/

B. Policies Inhibiting Competition

3. TRAI Seeks Comments on Regulating OTT Services

TRAI released a consultation paper entitled 'Regulatory Framework for Over-The-Top (OTT) Communication Services'. Through this consultation, TRAI seeks to analyse and discuss the implications of the growth of OTT services as can be regarded the same or similar to the services provided by telecom service providers (TSPs), the relationship between TSPs and OTT players, whether any change is required in the current regulatory framework and the manner in which such changes should be effected, if any.

Source: www.trai.gov.in/sites/default/files/CPOTT12112018.pdf

Food for thought

An OTT service provider offers Information and Communication Technology (ICT) services, but neither operates a network nor leases network capacity from a network operator. Instead, it relies on the global internet and access network speeds to reach the user, hence going 'over-the-top' of a TSPs network.[12]

The fact that TRAI has contemplated designing a regulatory framework for OTT services is a welcome step towards addressing the issues that different stakeholders are facing in the communication ecosystem. More importantly however, it is an opportunity to ensure that the regulatory framework is designed primarily for the benefit of the consumer. From the consumers' perspective, we can foresee some possible distortionary effects of sub-optimal regulation – which are important to consider and pre-empt.

For instance, one of the queries put forth by TRAI indicated that the regulatory or licencing imbalance between OTTs and TSPs could be the reason behind the current bleak investment scenario in the telecom sector (investment in the underlying networks is being negatively impacted due to lack of regulation or lack of level-playing field). However, it has been pointed out that the real reason behind the drop in the TSPs' revenues cannot be attributed to 'cannibalisation' of revenues by OTT services, but, on the one hand, the failure of TSPs to adapt to evolving technologies, and on the other hand, the failure of the government to provide a supportive regulatory regime.[13]

[12] See www.trai.gov.in/sites/default/files/CPOTT12112018.pdf

[13] CUTS submission available at: www.cuts-ccier.org/pdf/CUTS_comments_on_regulatory_framework_for_OTT_communication_services.pdf

Placing new age services under traditional regulatory regimes might lead to unintended consequences.

As per CUTS' consumer perception survey conducted in Rajasthan (to examine the perceived impact of OTT services on consumers' economic and social lives) ensuring quality control and fixing accountability of OTT service providers does not necessarily require them to be subjected to stringent regulations. The costs of stringent regulation (intended for consumer welfare) are usually passed on to consumers, who may find themselves in catch-22 situation. Consequently, other less intrusive options such as market-based incentives, self-regulation and co-regulation need to be encouraged to ensure market development as well as consumer welfare.

In addition to this, TRAI also contemplated the appropriate classification framework for OTTs. While it might be possible to segregate the nature of communication as interpersonal or social, segregating service providers based on this classification might lead to artificial distinction and may not stand the test of time. This is because the service providers likely to be segregated as social communication providers allow users to have interpersonal communications. Similarly, service providers which are likely to be segregated as interpersonal communication providers, can potentially allow social communications. Consequently, irrespective of presumed nature of the service provider, it will be important to examine how users are utilising such service in order to decide on the nature of classification, if any.

Lastly, the overall objective behind this exercise is to create a level playing field for competitors. However, this may not necessarily be achieved by increasing the costs of new market entrants to match the costs of incumbents but can also be achieved by reducing the costs of incumbents to match the costs of new entrant. In other words, there is a need to revisit the regulatory framework for incumbent TSPs and to ensure that they are subject to reasonable and proportionate regulatory requirements to address relevant risks posed by TSPs in a manner that they are able to compete with OTT service providers.

4. Government Tightens E-commerce Norms

The Commerce and Industry Ministry introduced new Foreign Direct Investment (FDI) norms for e-commerce barring online retailers from selling products of companies in which they own stakes. This disallows them from entering into exclusive deals for merchandise, unveiling norms that industry figures warned could upend India's US$18bn e-commerce industry. Barring e-commerce marketplaces from selling products of firms in which they own stakes could hit Amazon in particular, given that it has several such joint ventures

According to a senior government official, the basic idea behind this move is to tackle 'anti-competitive behaviour' by e-commerce entities.

Source: www.livemint.com/Industry/R5OXoHyAYa9l1RXck7fgpK/Blow-to-Flipkart-Amazon-as-govt-tightens-ecommerce-norms.html

Food for thought

As per the new FDI norms, an entity having 'equity participation' in e-commerce market place entity or its group company, or having control on its inventory by e-commerce marketplace entity or its group company, is not permitted to sell its products on the platform run by the marketplace.

The underlying logic is that in case of equity participation/control, the e-commerce entity does not remain a marketplace entity but turns into inventory based entity – FDI in which is not permitted. As highlighted by Pradeep S Mehta,[14] "Government may not be wrong in its clarificatory policy on FDI in e-commerce, as it was a case of backdoor entry in Multi-Brand Retail Trade (MBRT). But vital issues remain to be resolved to promote healthy economic democracy". Mehta further pointed out that the present norms (Press Note 2/2018) are applicable only on foreign platforms which raise certain concerns – for example, whether this discriminatory treatment between foreign and domestic platforms will not affect India's effort towards promoting a competitive economy? At the time when protectionism is looming large on global economy, such discrimination would undermine any effort to counter it.

Moreover, exclusive dealing restrictions seem to have been imposed to tackle anti-competitive behaviour on the marketplaces. The trigger for the introduction of this norm can be traced back to the regular complaints by small traders who cried foul against e-commerce giants, such as Flipkart and Amazon over practices of preferential treatment to its own products and deep-discounting. However, the approach taken by the government is to treat exclusive dealing agreements as 'per-se' anti-competitive which goes against the well-recognised practice of competition authorities that assess exclusive dealing under the 'rule-of-reason' standard.[15] The rule of reason approach demands a detailed investigation into the alleged practices and requires a case-specific

[14] Secretary General, CUTS International and member of the Government of India's Think Tank on e-commerce.

[15] See www.ftc.gov/system/files/documents/public_statements/1421189/abbott_-_icn_workshop_11-2-18.pdf

remedy. This is because exclusive dealing agreements may confer substantial pro-competitive benefits and it may be wrong to automatically treat them as anti-competitive. Before coming out with such a measure, it is crucial to: (a) assess whether or not there has been an appreciable adverse effect on competition in the relevant market; and (b) weigh the pro-competitive benefits against the anti-competitive effect. This lies within the sole prerogative of the Competition Commission of India and should be dealt with accordingly. Sans such an ex-post analysis led by the competition regulator, such measures tend to distort competition rather than promote it.

C. Policies Promoting Competition

5. Competition Law Reforms to Remove High Entry Barriers

In pursuance of its objective of ensuring that Legislation is in sync with the needs of strong economic fundamentals, the government has constituted a Competition Law Review Committee (CLRC) to review the Competition Act. During the past nine years, the size of the Indian economy has grown immensely and the country today is amongst the top five economies in the world and poised to forge ahead further. In this context, it is essential that Competition Law is strengthened and re-calibrated to promote best practices which result in the citizens of this country achieving their aspirations and value for money. The focus of further reforms will be on designing competition law to remove high entry barriers.

Source: https://economictimes.indiatimes.com/news/economy/policy/competition-law-reforms-to-remove-high-entry-barriers-mca-secretary/articleshow/66220818.cms

Food for thought

The CLRC is a welcome step towards readjusting India's competition regime to address changing nature of the economy and tackle new-age competition distortions that currently lie outside the radar of the law but are nonetheless adversely impacting consumer welfare. Digitisation of the economy is also inducing substantial changes in the existing market structure and behaviour of firms, as well as posing newer competition concerns.

In order to make the most of this opportunity, CUTS recommended that the Committee's efforts should recognise the importance of: (a) identifying new age competition concerns, including that may be foreseen in the context of Indian economy taking into in account its dynamism; (b) flagging concerns that could be dealt with by a *competition policy approach, which could also include bringing competition reforms at the national and state levels and recommend adoption of a National Competition Policy; and (c) flagging concerns that would not require changes in the present competition acts and rules, but will require changes in enforcement approach (including interpretation, protocols and guidelines).*[16]

Apart from this, it has also been reported that the Committee will focus on the removal of high entry barriers and provide easy access for those suffering from anti-competitive conduct.[17] *In order to do so, it will be crucial to reanalyse the end objective of the competition law – is it broader than just ensuring economic efficiency and consumer welfare? Should it be structured to cater to total welfare and take into account the interest of competitors (thereby seeking to adjust market structure)? What are the new-age entry barriers that could be included in the analysis (such as control over data and generation of network effects)?*

6. RBI's Solution for MSME Loan Woes

As per Deputy Governor Viral Acharya, the Reserve Bank of India (RBI) is preparing a public credit registry, which will help reduce interest rates for borrowers due to easier risk assessment. A public credit registry (PCR) will give banks the entire profile, including past loan details, and also regular income flows of borrowers. This can make a lender more confident and also reduce the rate of interest for a borrower as the risk assessment becomes easier, according to Acharya.

When asked about privacy concerns of such a registry, Acharya admitted it was a 'delicate' matter and advocated an access rights design upfront rather than a lot of information being gathered by companies. He also said that in most countries with public credit registries, there existed a separate legislative framework focussing on critical aspects, including access rights.

Source: www.livemint.com/Industry/w9JztGuB7FG2JXg3aihN4K/RBI-solution-for-MSME-loan-woes-Public-credit-registry.html

---

[16] For more recommendations, see CUTS Submission to the CLRC available at: www.cuts-ccier.org/pdf/CUTS-CIRC_Submission_to_Competition_Law_Review_Committee.pdf

[17] See https://economictimes.indiatimes.com/news/economy/policy/competition-law-reforms-to-remove-high-entry-barriers-mca-secretary/articleshow/66220818.cms

Food for thought

As the Indian financial sector continues to evolve rapidly with the advent of FinTech and digital markets, any attempt from the regulator to further disrupt the market should be weighed against the costs likely to be incurred and the benefits likely to be accrued. With the Indian Credit Information Companies (CICs) -- that are already regulated by the RBI, being a fairly recent addition to the Indian lending landscape, a move from the regulator to unleash a disruptor by way of launching PCR may pose a challenge to their existence. It may pave the way for a conflict of interest as the regulator of PCR will also act as its operator. Additionally, the PCR may also exercise a competitive constraint on the Information Utilities introduced by the Insolvency and Bankruptcy Code, 2018.

Public sector monopolies tend to work poorly and the attempt to establish a PCR can derail the nascent payments industry. As per the public choice theory, any State intervention should be directed towards addressing a market failure.[18] *It runs on the assumption that markets work well in most situations without State intervention and a move by the State to expand its powers and functions should be treated with scepticism. In that regard, it seems only reasonable to wonder about the necessity and role of the PCR. Is it being launched as a regulatory intervention in response to a specific market failure? Will it overlap with the business of the credit bureaus? Will it compete with the use of credit bureaus and scores? Does it adopt privacy by design approach to safeguard privacy and data protection concerns of customers?*

However, as an upside, the PCR has been claimed to consolidate otherwise fragmented consumers' databases that sit in different repositories, tackle information asymmetry that hurts good borrowers, reduce interest rates for borrowers due to easier risk assessment thus solving the credit problems at the grassroots, amongst others. Thus, while the move to set up a PCR may be welcomed, there should be an arm's length between the regulator and the Registry; as well as optimal regulation to be adopted in order to ensure fair competition in the market and pave the way for a level playing field.

7. RBI Norms to Facilitate Payments between Mobile Wallets

With the RBI releasing operational guidelines on interoperability of prepaid payment instruments (PPIs), mobile wallet users will soon be able to transfer funds from one

[18] See https://blog.theleapjournal.org/2017/08/rbis-proposal-for-public-credit-registry.html

wallet to another, and eventually, from their wallets to bank accounts through the unified payments interface (UPI) platform.

It will also allow mobile wallets to issue UPI handles and cards. This will enable non-bank PPIs to act as quasi-banks in terms of payments, increasing tension between mobile wallet companies and payments banks, said industry experts.

By allowing PPIs to issue cards for withdrawals, mobile wallets will be almost on par with payments banks. According to experts, the only difference will be that payments banks will pay interest on deposits, while wallet balances will not yield any return.

Source: www.livemint.com/Industry/KJjmn5NoAczkYvKrL6wpGI/New-RBI-norms-put-mobile-wallets-on-par-with-payments-banks.htmlm

Food for thought

As we transcend into a digital economy, there is a need to ensure availability of infrastructure to facilitate digital transactions and extract the benefits that come with it. One such critical necessity is enabling interoperability of PPIs, i.e. allowing consumers to directly transact amongst different PPIs. Interoperability in digital financial services is laced with pro-competitive effects and is said to promote financial inclusion thus boosting the economic growth of a nation.

Interoperability ensures a level playing field within the payments industry between banks and non-banks. It increases competition and enhances consumer welfare by 'driving down costs, facilitating innovation and improving compliance.'[19] Its lack thereof limits the payment options and impacts access for consumers. Indonesia, Madagascar, Pakistan, Rwanda, Sri Lanka, Tanzania and Thailand are some of the country markets that are fully interoperable and have benefitted from increase in competition and interoperability in digital payments.[20]

Learning from these countries, India too has set on a journey of adding interoperability as a feature of the payments industry. However, such envisioned interoperability access to non-banks is not direct. PPIs can be issued in form of wallets or cards – when issued in form of cards, interoperability needs to be enabled by relevant authorised card networks; however interoperability across wallets will be enabled through UPI. UPI is a payment system developed by the National Payments Corporation of India (NPCI), a

[19] See http://finance.du.ac.in/du-finance/uploads/pdf/Reports/watal_report271216.pdf

[20] See www.cuts-ccier.org/Payments-Infrastructure/pdf/Research_Report-Competition_assessment_of_payments_infra_in_India.pdf

bank owned entity, on which the RBI retains considerable influence. Further, in case of cards, non-bank PPI issuer can participate directly in settlement process (clause 4.2) subject to compliance with card network settlement system and guidelines. However, in case of wallets, settlement can happen only through sponsor bank, as UPI does not allow non-banks direct participation in settlement (clause 5.5). This is problematic as the transfer of funds from wallets to bank and bank to wallets through UPI takes away the essence of operability from interoperability and this over regulation comes at the expense of consumer welfare.

Thus while designing regulation, it is significant to take into account the rising market power of non-bank PPIs and reliance of customers on them to create a level playing field and ensure market contestability.