Competition Distortions in India – A Dossier

(CDI-21: July–September, 2013)

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

Periodic dossiers look at the interface of policy issues which has an impact on competition in India, which can be both negative and positive. News as published is used without verifying their accuracy. The purpose is to flag issues to the layman as well as to the specialised policymakers and regulators, rather than be judgmental about them. This would require greater analysis particularly in terms of cost and benefits.

We are pleased to bring before you the Competition Distortions Dossier Edition No: 21 for the third quarter: July-September 2013. As always, we have captured several interesting stories, a mix of good and bad. There are many instances of potential competition distortions caused by trade policy tools such as import duties and adopting protectionist approach by not allowing firms to import their equipment or goods.

We have always held the stand that while such policy tools are necessary to assist the domestic industry, they may not be ideal from a competition policy point of view. Also, they are quick-fixes that do not serve a long term goal of encouraging competitiveness of domestic industries by artificially insulating/shielding them. In some cases, we can agree that some local factors inhibit their competitiveness, and thus they need protection. But such protectionism needs to be rationally analysed and the fundamental problems be resolved.

There are instances of violation of the competition owing to lack of proactiveness shown by government over the past few years in terms of introducing and implementing reforms in certain sectors, which can be seen in this edition as well. These are cases pertaining to the electricity sector and incense stick industry. In both the cases delay in reforms is causing loss to industry as well as consumers.

We also welcome the steps taken by the government in which it has shown its disagreement over the demand of major telecom companies operating in India to hold their license for providing services in key circles after 2014 and skipping the process of auction altogether. Such measures would create an environment for new players to enter the market, ultimately leading to benefits for consumers.

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A. TRADE POLICY

1. EGoM Mandates Use of Local Gear in UMPPs

Those bidding for ultra-mega power projects will now have to source equipment from domestic manufacturers. They will also have to offer the most competitive rates based on overall plant efficiency.

This was decided by an Empowered Group of Ministers (EGoM) headed by Defence Minister A. K. Antony, which gave its go-ahead for the latest standard bidding documents.

The move to make it mandatory to source equipment from domestic manufacturers is bound to help companies, such as BHEL, L&T and Bharat Forge-Alstom, all of which are suffering from lack of fresh orders. The Minister of Heavy Industries and Public Enterprises, Praful Patel, has been asking the government to make it mandatory for Ultra Mega Power Projects (UMPPs) to source equipment locally.

http://www.thehindubusinessline.com/industry-and-economy/egom-mandates-use-of-local-gear-in-ultra-mega-power-plants/article5052977.ece

Food for Thought

In a bid to enhance the sale of locally produced equipment that are used in the power producing plants, an EGoM has taken a decision to make it mandatory for UMPPs to procure equipment from the domestic manufacturers. The step from the part of EGoM could be treated as the result of proposal floated by the Heavy Industries Ministry in which it has recommended that all future UMPPs should be sourcing equipment from domestic companies like BHEL and L&T which have been experiencing a lean patch owing to steep fall in fresh orders during past few years. It is supposed that the move would help these companies to revive their fortune. At present two functional UMPP in India i.e. Tata Power at Mundra and Reliance Power at Sasan had imported equipment for their plants.

Few other decisions regarding tariff rates have also been taken by EGoM. It has been decided that power producers can increase cost per unit charged to consumers if there is any hike in fuel cost. Both Tata Power and Reliance Power have reported losses due to increase in the price of imported coal.

Intention of the government to stabilise the condition of domestic heavy industry holds ground up to a certain extent, however the method adopted could not be justified as it is a complete protectionist approach which would not be beneficial in terms of promoting competition within domestic industry. Rather the approach should be to build capacity of domestic players in terms of producing quality and cost effective equipment, which would enable them to compete with their foreign counterparts in the open market, which in turn would provide more choice to players setting up power projects in India.

Apart from this, Association of Power Producers of India (APPI) has expressed their dissatisfaction over the entire development. According to APPI such rigid approach on the part of government would hamper investments in the power sector. It is advisable for the government to be flexible in order to promote competition while taking such decision which involves important economic sectors such as power.

2. Duty on Flat Panel TVs to Stop Misuse of Scheme

Now, get ready to shell out more for getting a flat panel television set from Thailand, Dubai or Singapore.

Starting August 26, the government has decided to levy 36 percent customs duty on LCD and LED television sets that passengers bring along with them as part of the duty-free baggage allowance of Rs 35,000.

The price arbitrage had turned into a lucrative business proposition with several carriers taking flights to South East Asia and making a killing in the domestic market.

For example, a 32-inch TV set in Thailand costs around Rs 17,000 to Rs 18,000 and in India it ranges between Rs 30,000 and Rs 35,000. A customer who bought a 42-inch TV in Dubai some days ago paid Rs 33,000, whereas a comparable model of the same brand available on an e-retailer's website costs around Rs 55,000.

http://timesofindia.indiatimes.com/business/india-business/Pay-duty-on-flat-panel-TV-imports-from-August-26/articleshow/21927873.cms

Food for Thought

Indian television set manufacturers have been provided with relief by the government's decision in which it has decided to levy 36 percent customs duty on LCD and LED television sets that passengers bring along with them as part of the duty-free baggage allowance. According to the baggage rules all passengers above the age of 10 years returning after more than three days stay abroad were allowed to bring articles up to a value of Rs. 35,000, if these are carried on the person or in the accompanied baggage of the passenger.

According to domestic television manufacturers, the practice of importing television sets from countries like Thailand, Dubai and Singapore has been established in such a way that some electronics malls in Thailand and Dubai deliver the TV sets at the airport for the convenience of the passengers flying to India. The price differential also triggered tourism packages which were built around the purchase of a flat panel TV. Few industry experts admitted that such imports added upto 10 to 15 percent of domestic sales.

The argument given by industry people and the step adopted by the government is fair enough as it is duty of government to safeguard the interest of domestic industry. It would definitely help domestic television industry to enhance their sale of television sets and hence improve overall profit. It would also create level playing field for domestic players and hence enable them to compete with foreign manufacturers of television sets.

However, it could also be labelled as a protectionist measure on part of the government. Rather than adopting such measures that defuse competition, endeavor should be made to build capacity of domestic television industry, so that they become more cost-effective and match the prices being offered by television companies in countries like Thailand, Singapore, Dubai, etc. It would infuse the spirit of competition in domestic industry and would also serve consumer interest in an effective manner.

B. DELAY IN REFORM

3. Closed Access in the Power Sector

Given how certain industries tend to lend themselves to natural monopolies, regulation is always a tough business since bringing in competition is near impossible. While the complete absence of mobile phones when such services were introduced in 1995 allowed competition to flower, the same couldn't be said of the landline business monopolised by public sector undertakings (PSUs) – Bharat Sanchar Nigam Ltd (BSNL) and Mahanagar Telephone Nigam Ltd (MTNL).

This magic formula of introduction of competition in natural monopolies is precisely what the government tried to replicate in the power sector through Electricity Act 2003. Given the power lines coming into customer homes and offices are owned by individual power companies, how can competition be brought in?

http://www.financialexpress.com/news/editorial-closed-access/1149350

Food for Thought

Of late, there have been efforts taken by the government to inject competition in sectors largely dominated by state owned enterprises. Telecom could be considered as one sector which has transformed from being a natural monopoly dominated by PSUs like BSNL and MTNL to highly competitive sector with presence of large number of players leading to several benefits for consumers at large. Regulatory interventions and policy changes at regular intervals could be termed one of the key factors responsible for such transition over a period of two decades.

However, government's endeavour to replicate the experience in power sector which again could be considered as a natural monopoly, through introducing Electricity Act, 2003 have not been able to meet the desired goal.

Electricity Act, 2003 was passed by the government replacing the earlier laws for developing a liberal framework for development of the power industry, promoting competition and protecting interests of consumers. The Act included provisions related to open access for everyone having 1MW consumption or more. It means that these consumers are free to purchase electricity from suppliers of their own choice. However, till date there is no clear guideline for proper implementation of rule regarding open access. Moreover states like Rajasthan, Punjab, and Madhya Pradesh have come up with orders for restricting such open access.

The Ministry of Power has repeatedly been coaxing states to implement the open access regime, but it has hardly any impact. The problem is that the regulators are hesitant of exercising their powers, as they exist on the mercy of the state governments. Furthermore, most of regulators are retired bureaucrats and have hardly any competence to understand the market principles relevant to the power sector. However, there are but very few exceptions. For example, in Navi Mumbai the electricity regulator has ensured that an open access regime was implemented in 2011-12. There are two main private players in the region, Reliance Infra and Tata Power Company Limited, competing to supply power to consumers with loads even below 1MW under the open access regime.

4. Agarbatti Industry Resorts to Imports for Bamboo Sticks

Agarbattis, or incense sticks, are used daily in millions of homes in India, but most of them are now being made with bamboo, a key input sourced from China or Vietnam. That is because forest regulations on bamboo transportation and labour shortage are making the raw material scarce in India, forcing manufacturers to turn to imports.

A large part of the Rs 3,500-crore domestic agarbatti industry is now importing nearly 70 percent of its bamboo stick needs, said Ambica Krishna, chairman and managing director of Ambica Agarbathies and Aroma Industries. The industry is currently importing 250 lorry loads of bamboo sticks of 10 tonnes each every day at an import duty of some 28 percent, he said.

http://articles.economictimes.indiatimes.com/2013-08-17/news/41420898_1_bamboo-labour-shortage-raw-material

Food for Thought

Incense stick producers in India are struggling with the shortage of bamboo, one of the key inputs required for manufacturing incense sticks, at domestic level. The shortage has left manufacturers with no other option but to import bamboo from countries like China and Vietnam. At present around 70 percent of bamboo required by the industry is imported from these countries. Import has led to increase in the input cost due to which several small and medium players are considering raising prices to maintain their profit margin, while larger companies perfectly placed in the market are creating pressure on them with aggressive pricing.

One of the main reasons behind this situation is the existing forest regulations on bamboo transportation and shortage of labour which makes the raw material scarce in India, forcing manufacturers to turn to imports. According to forest officials transportation of forest produce poses problems for the industry. For transporting bamboo sticks from place to place, users of forest produce as raw material are required to take transit permission from the forest department.

Considering the given situation, it is advisable for the government to introduce reforms in procurement, transportation and utilisation of forest produce. Otherwise it might lead to creation of uneven field for small and medium level incense stick manufacturers as increased prices due to increase in input cost will result in decrease in their market share. Adopting such reforms would also help in creating employment in rural areas as companies would be required to employ local people for the entire process of procurement of forest produce.

C. MIXED BAG

5. Aviation Ministry's Airport Privatisation Bid Criticised

………………………………A global tender for the six airports – at Chennai, Kolkata, Ahmedabad, Jaipur, Lucknow and Guwahati – will be floated soon, a government official said, requesting anonymity.

The rationale for private-sector equity participation is "not clear" in the case of these six airports, currently operated by the Airports Authority of India (AAI), Maunu von Lueders, Regional Vice-President, Asia Pacific, International Air Transport Association (IATA), wrote in a letter to Indian Aviation Secretary K.N. Shrivastava.

http://www.livemint.com/Politics/P4VeJsckwC0I46IETprpdK/Aviation-ministrys-airport-privatization-bid-criticized.html

Food for Thought

The idea of the government to privatise the recently renovated six airports has attracted criticism from stakeholders across the aviation sector. Apart from unions and political parties, the IATA has also opposed privatisation of more airports in India owing to the fact that privatisation of the metro airports has led to hike in various charges i.e. aircraft landing charges, charges for the processing of passengers and freight and other charges related to the use of airport infrastructure, levied at various airport. One can take the example of the Delhi airport, managed by Delhi International Airport Limited (DIAL), which is now one of the most expensive airports in the world. According to IATA it is not necessary for the government to go for privatisation in order to attain internal expertise for proper management of the airports as it could be done through awarding a management contract to a company having expertise in this field.

Further, the stance adopted by the government in this case is unlike the public-private partnership (PPP model) airports in Delhi, Mumbai, Hyderabad and Bangalore. The AAI holds certain percentage of stake, i.e. 26 percent stake in Delhi and Mumbai and 13 percent in Hyderabad and Bangalore airports. AAI this time will not be under any obligation to invest in the private companies that will compete to run the six airports as the Ministry has taken a decision to allow the private players to have 100 percent stake.

However, according to few experts, change of ownership is not a bad idea as it would help in engaging top class airport companies which would further lead to adoption of global best practices, greater competition, higher non-aeronautical revenues and improved consumer welfare.

All the above mentioned points should be taken into consideration by the government before arriving at any conclusion. It should be kept in the mind that huge public fund has been invested for developing these airports and any policy regarding privatisation and/or disinvestment should be focused upon maximising consumer welfare and economic growth.

6. Licence Extension: TRAI to Support Auctions

The companies have moved the Delhi High Court to seek a direction to the Department of Telecommunications for extension of their licence to operate by paying a fee as a mark-up on the sum they paid when they were given the original licences. In an open house on the topic of spectrum reserve price, the regulator is learnt to have indicated that the demand by the companies, principally Global System for Mobile communications (GSM) players was difficult to accept. The regulator has, however, on most other issues adopted an industry supportive position as compared with the adversarial position it had adopted a year ago.

http://www.indianexpress.com/news/licence-extension-trai-may-support-auctions/1161048/

Food for Thought

The Telecom Regulatory Authority of India (TRAI) has shown its disagreement over the demand of major telecom companies, such as Vodafone, Bharti Airtel, and Idea operating in India to hold their license for providing services in key circles after 2014 and avoiding the process of auction altogether. Telecom companies have taken the shelter of court on the whole matter proposing they would prefer to pay extra amount over the actual fee they incurred to bag the license earlier. However, TRAI seems not to be interested in accepting such arrangement and has indicated during an open house meeting that all licence holders have to surrender their spectrum and go through the auction process for available spectrum in the 1800MHz or the 900 MHz at new reserve prices.

The approach adopted by TRAI is commendable as it would certainly help in infusing competition in the telecom sector. Fresh auctioning of spectrum would help new players to enter the market. Further, entry of new players would also lead to improved services for consumers. It would also help in attracting fresh investment in the sector. However, such transition would take some time as entry for new players in telecom sector would require huge investment as well as they have to face tough competition from already well-established players in the market. Saying this, it does not mean government should not go for such reformatory steps, as ultimately it would benefit the consumers by providing them more choice.

7. Govt ask Private Coal Miners to Sell Surplus to CIL

After exhausting all available options to increase coal production, the government has decided to incentivise private sector coal mines to sell their surplus produce to state-run Coal India but with the assurance they can get it back at a profit in future.

To ensure the proposal has wide-ranging support, the government plans to set up a committee that will include financial sector luminaries like HDFC Bank Chairman Deepak Parekh, ICICI Bank Chief Chanda Kochhar and others to fine tune it.

http://www.indianexpress.com/news/govt-works-on-plan-to-ask-private-coal-miners-to-sell-surplus-to-cil/1154071/

Food for Thought

In its recent attempt to enhance the production of coal in the country, the government has come up with an idea of encouraging private sector coal miners to produce more coal than they need for their units. The excess coal will be sold to Coal India and the producers will have the right to buy back the coal in future at a price close to the current price.

In order to ensure proper implementation of the entire concept, government would be setting a panel to be chaired by BK Chaturvedi while Planning Commission member Saumitra Chaudhuri, HDFC Bank Chairman Deepak Parekh and ICICI Bank Chief Chanda Kochhar are likely to be inducted as members of the panel. The panel would examine the benefits of coal banking system and optimal utilisation of surplus coal.

The original proposal was floated by the Association of Private Power Producers. According to the association, Coal India could make an advance payment during the banking period to the private coal producers and recover the amount by selling the coal to its customers.

If executed properly, the plan would prove to be a milestone in terms of increasing the production of coal in India. It would also help in upgradation of technology used for mining. Further, incentive for producing surplus coal would help in inducting healthy competition among the private coal producers.

It is indeed a tragedy that while we have surplus coal in India, we are still resorting to costlier imports because of policy distortions.