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COMPETITION AND POVERTY REDUCTION

Contribution from Brazil

-- Session I --

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-- Brazil --

1. Introduction

1. The economic progress of countries has frequently been measured by their income growth. In the last decade, however, much attention has been rightly devoted to the type and quality of the growth experienced by countries. Today, it is widely recognized that the gross domestic product (GDP) should not be the only tool to measure the welfare of a country, since its growth is not always related to the improvement of the living conditions of the majority of the population. A country's income growth rates do not mean much if they are not related to the reduction of inequality, the increase of social mobility and the creation of opportunities to the poorest.

2. Brazil has recently obtained major successes in translating income growth into reduction of poverty and inequality. Different studies show that the improvements in the social arena obtained by Brazil in the last years have been unprecedented. The income of the poorest has experienced a significant expansion, leading to a great reduction of poverty rates, as well as to a major fall in the inequality index such as the "Gini coefficient". According to a recent research, while the Brazilian GDP grew in average 5.1 % over the last five years, the gains in living conditions in the country corresponded to those normally obtained by a country whose economy expanded averagely more than 13 % per year.¹

3. Several political, economic and institutional reforms explain the inequality reduction and the distributive gains achieved by Brazil in the last decades. Since 1988, Brazil experiences a stable democracy, where different political groups establish a fruitful debate over the country's future and alternatives. In this time, inflation was controlled and markets were reformed to allow private investments, reduce barriers to international trade, induce competitions and introduce transparent regulation. In the social area, the minimum wage was highly increased and new models of welfare programs were implemented, which proved very effective in reducing poverty.

4. As a part of the market reforms, a new competition law was enacted in 1994, which introduced merger control in Brazil and reshaped the Brazilian Administrative Council for Economic Defense (CADE) as an independent agency with broad powers to deal with conducts that posed danger to the competitive structure of markets. Since then, Brazilian competition policy has grown in importance and achieved several accomplishments. The anti-cartel program, which relies on the use of advanced investigative tools, such as dawn raids and leniency, is internationally respected. The recently adopted pre-merger notification system has proven to work well, with the review timing being in line with the best international practices.

¹ Douglas Beal, Enrique Rueda-Sabater, and Teresa Espirito Santo. "Introducing the BCG Sustainable Economic Development Assessment: From Wealth to Well-being". 27 November 2012. Available at https://www.bcgperspectives.com/content/articles/public_sector_globalization_from_wealth_to_well_being/.

5. Brazilian competition law is aligned with other public policies in that it rests on a genuine confidence in the market system as a mechanism that creates wealth and enhances the overall efficiency of the country's economy. And as one that must be controlled not to allow that concentration and abuse of economic power result in the decrease of opportunities to small entrepreneurs, which could jeopardize the promise of social mobility that is central to a market economy. A competition authority may contribute in different ways to the creation of an environment that improves the living conditions of the poorest, as we are able to perceive from CADE's recent experience.

2. Competition enforcement as a tool for protection of poor consumers

6. This section presents a few Brazilian cases that had relevant impact in the life of the poorest in Brazil, particularly in the field of essential goods and services. First, it describes a pending case in the cement market, which substantially affects, among other matters, a public housing policy for the poorest. Then, it analyses the extent of the negative effects of retail fuel cartels and it highlights a cartel case that affected the public health sector. Finally, it makes reference to a recent dawn raid in the salt market that has an indirect impact in basic provisions.

2.1 Cement market

7. The first example concerns the cement market, considering that anticompetitive practices that lead to higher prices of building materials may affect infrastructure investments as well as housing. To highlight the importance of this market, an international cartel in the sector was investigated by many countries, including the EU, Germany, France, UK, Poland, South Africa, Pakistan, Egypt, Taiwan, Korea, Romania and Argentina.

8. In Brazil, the cement market has been subject of a deep anticompetitive investigation from the former Secretariat of Economic Law ("SDE") of the Ministry of Justice. The investigations started back in 2006 and concluded for the existence of a substantial cartel that resulted in an increase of construction costs in general, including housing. This is a key-sector in Brazil, considering that: (i) cement is an essential product to civil construction; (ii) demand for cement remained high in the past two decades; and (iii) Brazil still has a "housing debt" to work on.

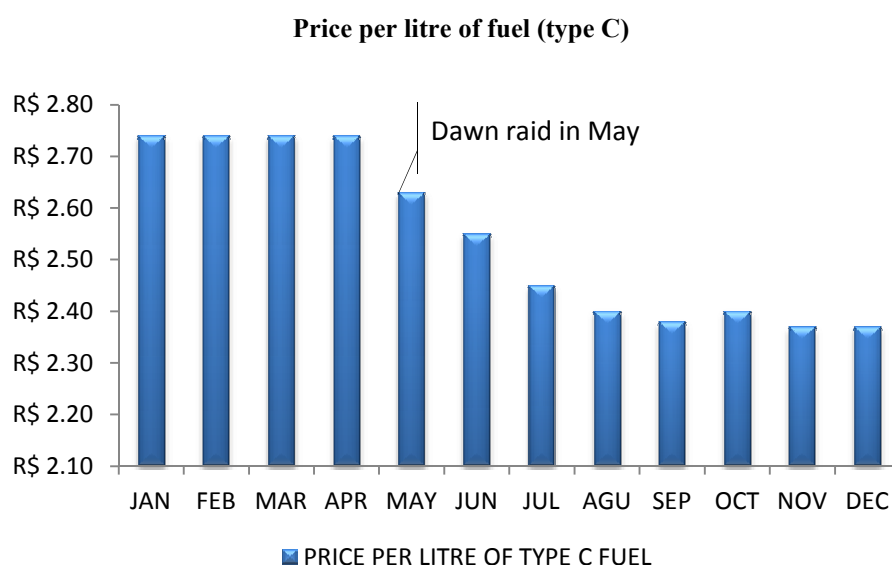
9. SDE calculated that the federal governmental program for housing to low-income families ("Programa Minha Casa Minha Vida") represented a demand of 11 million tons of cement (233 million cement bags of 50kg each), which totalized approximately R\$ 6,3 billion (around US\$ 3,15 billion). The case is still awaiting trial at the Brazilian Competition Tribunal, the current administrative decision body of the Brazilian Administrative Council for Economic Defense (CADE).

2.2 Retail fuel cartels

10. The retail fuel market is also interesting for the study of the relationship between competition and poverty, particularly in some countries, which remain highly dependent on its highway network for cargo and people transportation. In Brazil, highway network represents for 62% of total cargo transportation of the country, and even greater in regard to agriculture related products.² Among other possible reasons, this dependence is a legacy of a traditional public policy that favored the construction and development of roads and high-ways, rather than trains, subways and alternative transportation means. Henceforth, high prices of fuel have a direct impact on the day-to-day life of the poor people, since transportation costs affect directly the final prices of basic goods as well as bus tickets and inter-state bus tickets.

² Cf. Brazilian Institute for Applied Economic Research (IPEA). Available at: **Error! Hyperlink reference not valid.**, pages 33-34 (last access on August 2012).

11. One particular case illustrates the positive impact of competition enforcement in this sector for consumers in general, which includes the poorest for the abovementioned reasons. A dawn raid carried out in 2007 uncovered an important gasoline cartel in the city of João Pessoa, capital of the State of Paraíba. The effects on prices – before and after the cartel – can be easily noticed in the graphic below:



12. Fuel prices dropped from R\$ 2,74 to an average of R\$ 2,40 per liter – more than 10% difference. Considering an average of 8 million liters of fuel consumption per month in the city, multiplied by the R\$ 0,34 cents savings per liter from the difference between price before and after the cartel, a general saving of around R\$ 2.720.000,00 (over 1 million Euros) for the city is reached.

13. In addition, a strong competition advocacy effort has been made in Brazil during the last decade, particularly in the fight against cartels. Among these efforts is the institution of a National day of fight against cartels, which uses the retail fuel cartels as an example to easily expose the negative effects of this anticompetitive practice for consumers and for the country as a whole.

2.3 Industrial and medicinal gas markets

14. In 2003, the former Secretariat for Economic Law (SDE) started an investigation on a cartel among the main players in Brazil's industrial and medicinal gas markets. And it conducted dawn raids that collected vast amounts of evidence against the companies. After the investigative proceeding, SDE sent the case to CADE with a recommendation for condemnation. CADE found companies guilty and set fines for 25% of each company's revenue in 2003. White Martins Gases Industriais Ltda's fine was doubled because it had already been previously found guilty of an anticompetitive practice.

15. This was an extremely important case for competition enforcement in Brazil due to the high fines imposed and the market involved. On the one hand, CADE's decision raised the importance of private law suits for reparation of damages caused by cartels. On the other hand, it highlighted the negative impact of the cartel to the Brazilian health sector, since the products involved in the cartel were used to carry out medical treatments. It had a direct impact on the costs of patients and hospitals, disabling the use to other patients and treatments. The decision also indicated that the market affected by the cartel plays a role on the definition of the amount of fines.

2.4 Salt market

16. CADE's General Superintendence held in September 2012 a dawn raid of documents and electronic material in an investigation against an alleged salt producers' cartel in the state of Rio Grande do Norte. The action had operational support of Federal Highway Police (PRF) from the states of Rio Grande do Norte and Rio de Janeiro.

17. The operation took place in the cities of Mossoró, Natal and Rio de Janeiro. There were nine search and seizure warrants against companies and union headquarters - seven of them in Mossoró, one in Natal and one in Rio de Janeiro, where the groups kept commercial offices.

18. The searches are based on Cade's request granted by the Federal Court in Natal, Mossoró and Rio de Janeiro, because of union public statements affirming that the companies constantly met to discuss product price and production quantities - which in theory constitutes cartel. An economic study done by Cade showed that, since the start of such meetings between the companies, the price of salt increased to levels close to what they would be if there was a monopoly in the sector. It was noticed that, since 2008, the price of salt for human consumption to the final consumer is 50% higher than the inflation rate in the period, according to the Brazilian National Consumer Price Index (INPC).

19. Salt production companies allegedly involved in the cartel account for about 80% of national production, which explains the significant impact a cartel in the sector has on the prices of salt – raw material for chemical and pharmaceutical industry – and salt for human consumption.

3. Competition policy as a tool for economic and social inclusiveness

20. Competitive markets are vital mechanisms for the creation of wealth and the reduction of poverty. Competition creates the right incentives for companies to make better products, reduce its prices and invest in innovation. Competitive markets are also key elements to social mobility in a country, since they allow companies to enter freely in new markets and small entrepreneurs to develop their ideas and to contest the incumbents.

21. The existence of a market economy, however, does not guarantee by itself that the forces of competition will be in the right place to promote innovation and to drive firms to make their business more efficient. Markets may be controlled by one or few companies, which can use their power to obstruct the entry of new competitors and to charge supra-competitive prices. Small companies may be dependent on essential facilities controlled by dominant firms and are usually vulnerable to conducts that foreclose markets.

22. A sound competition policy must address these concerns, contributing to the creation of inclusive markets through the leveling of the economic playing field. Competition enforcement must impede that dominant companies create artificial restraints and, when they do, it must be able to unblock the paths to effective and fair markets, allowing younger firms to develop themselves and to compete on the merits of their business.

23. In its history, CADE has recurrently showed its commitment to the combat of unreasonable market restraints that endanger the environment to entrepreneurship and innovation, which is fundamental to the success of new companies and small firms. In 2009, CADE considered illegal a reseller loyalty program implemented by the largest Brazilian brewing company, because it found that the program could squeeze competitors out of the market through the creation of artificial barriers and the elevation of rivals' costs.

24. More recently, CADE reaffirmed its concern with the maintenance of an economic environment that favors investments in innovation, when it analyzed a case that was initiated after the Brazilian National Association of Automotive Parts Manufacturers (ANFAPE) complained about the policies that some major vehicle manufacturers adopted in the market of auto-parts. ANFAPE claimed that the car manufacturers were attempting against competition by initiating legal proceedings to block the entry and hinder rivalry in the market of automotive parts. On the other side, the manufacturers argued that their actions merely represented a legitimate enforcement of valid intellectual property rights regarding the industrial designs on external auto-parts. Although the Secretariat of Economic Law (SDE) of the Ministry of Justice had decided, after a preliminary analysis, to close the case, arguing that the registrations held by the car makers was legitimate, CADE determined that a deeper investigation was needed to confirm that the car makers were not abusing their dominant position.

25. In its decision, CADE recognized that the main goal of intellectual property law is to promote innovation, but noted that in some situations the misuse of patent rights can lead to great damages to competition, not only by reducing the welfare of consumers, but also by compromising the incentives to research and development that IP law is supposed to guarantee. Although the proceeding is still pending further investigation and a final decision by CADE, it is clear that the mere existence of valid intellectual property rights will not be accepted as an excuse for dominant firms to implement practices that illegally obstruct the activities of competitors, harming competition and diminishing the economic space for smaller entrepreneurs to develop their products and ideas.

4. Conclusions

26. This paper addresses the relation between competition and poverty in Brazil. Providing a general framework of the topic as well as a historical approach on the liberalization of the Brazilian markets during the 1990s, it describes a few competition cases that had a great impact on poor consumers, such as cement for housing, fuel for transportation and industrial gas used to health care. In addition, it also examines competition policy as a tool for the maintenance of a favorable environment to entrepreneurship and innovation, which seems essential to enable small business and to promote job creations through the concept of inclusiveness, before reaching these final remarks.

27. Aside from the important role that competition policy and enforcement can play for poverty reduction, this study highlights the value of a constant evaluation of the impact of competition policy. It enables the quantification of the benefits of competition enforcement and advocacy activities to consumers, particularly the poorest for purposes of this research. As suggested by OECD, this exercise is becoming increasingly widespread because of the mounting pressure on competition authorities, as well as regulators in general, to be more transparent and accountable.