A South African Perspective

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Abstract

When South Africa made the political transition to a democracy in 1994, the new government inherited an economy characterized by racial inequality, an uncompetitive manufacturing sector and high concentration levels. Within the setting of the democracy, these problems have to be addressed urgently to ensure that all South Africans have equal opportunities to participate in the formal economy. This poses an enormous challenge to government and provides the rationale for competition policy. The pieces of competition legislation that preceded the country’s current Competition Act (no. 89 of 1998, as amended) have been unsuccessful in attempts to lower the high concentration levels. The current Act became effective on 1 September 1999 and pursues multiple objectives. This paper provides an overview of the evolution of competition policy in South Africa, with a specific focus on how the new Act and the institutions administering it may contribute to lowering concentration levels and address the issue of ownership in the economy, which is still predominantly concentrated in the hands of the white population.

When South Africa made the political transition to a representative democracy in 1994, the new government inherited an economy that was characterized by racial inequality, poverty, an uncompetitive manufacturing sector, state-owned monopolies, conglomerates and high concentration levels (OECD, 2003: 2-3). Within the setting of the democracy, these issues need to be addressed urgently to ensure that all South Africans have equal opportunities to participate in the formal economy. This poses an enormous challenge to government and also provides the rationale for competition policy.

Competition policy is embodied in competition legislation and is more commonly found today than before the 1950s. Countries also enforce competition legislation in a more rigorous manner than before (Shelton, 1998: 1; Mouton et al., 1977: 1). South Africa had ineffective competition legislation prior to the current one, as these pieces of legislation failed to effectively lower the high concentration levels in the economy. The literature suggests various reasons for the high concentration levels, including: (i) the Poor White problem and British dominance in the South African business sector, which the government tried to deal with by establishing large state-owned enterprises to create employment opportunities for the Poor Whites and to compete with the British enterprises that operated in South Africa and (ii) protective policies which the government implemented to protect South African industries against foreign competition. Both these reasons resulted in a decline in competition in the economy and increased the risk of firms engaging in anti-competitive activities (OECD, 2003: 3).

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4 A conglomerate is established when two firms in different industries merge their activities (Arnold, 2001: 579).
5 Concentration levels in industries are high when industries are dominated by a relatively small number of firms that collectively own almost the total market share of the industry.
6 The South African economy is predominantly occupied by oligopolies, implying that a relatively small number of firms dominate in markets, which lowers the level of competition. Some examples of these markets include the banking and insurance sectors and the cement and pharmaceutical industries.
7 E.g. Eskom and Iscor.
During the 1970s the Mouton Commission of Inquiry\textsuperscript{7} launched an investigation into the effectiveness of South Africa's first comprehensive competition legislation, the Regulation of Monopolistic Conditions Act 24 of 1955\textsuperscript{8}. They found that the 1955 Act “had been unsuccessful in preventing a dramatic increase in oligopolies” (Competition Commission, 1999: 1). This piece of legislation was replaced by the Maintenance and Promotion of Competition Act\textsuperscript{9} in 1979 and the Competition Board was appointed to administer the Act. However, the Competition Board faced great difficulty\textsuperscript{10} in applying the Act in a consistent manner due to the subjective nature of its content (Fourie, 1987a: 334). This caused the Act to lose its effectiveness and credibility.

On 1 September 1999 the new Competition Act became effective, Act 89 of 1998\textsuperscript{11}. Three independent institutions were established to administer it, i.e. the Competition Commission\textsuperscript{12}, Competition Tribunal\textsuperscript{13} and the Competition Appeal Court\textsuperscript{14}. According to these institutions, the 1998 Act (as amended) provides “a far more powerful competition law regime than the one that South African businesses and consumers were previously accustomed to” (Competition Commission, 2000a: 16). Multiple objectives have been included in the Consolidated Act and in each annual report the Commission evaluates their performance by comparing it to the stated objectives.

Despite all the changes that have been made to competition policy in South Africa, concentration levels (especially in the manufacturing sector\textsuperscript{15}) remain high and ownership within the economy is still predominantly concentrated in the hands of the white population. This fact stimulated the researcher's interest in studying the evolution of competition policy in South Africa and to determine to what extent the Consolidated Act addresses the remaining problems that have been discussed.

The objectives of this paper are to explain the theoretical rationale for competition policy, discuss the political-economic rationale for competition policy in South Africa, to give an overview of the evolution of competition policy in the country, to explain selected sections of the Consolidated Act and to assess whether the Competition Authorities are applying the Act properly and whether the Act’s objectives are achieved.

1. RESEARCH METHODOLOGY

The research is of a descriptive and subjective nature and involves a review of the literature. The paper contains both a theoretical and a practical analysis. For the practical analysis the researcher used the current Competition Authorities’ case reports and media releases as sources. The paper is structured as follows: section 2 defines market power, explains the implications of having firms with market power in industries and discusses the theoretical rationale and the political-economic rationale for competition policy in South Africa. Section 3 gives an overview of South African competition policy over the past fifty years. This overview

\textsuperscript{7} From here and onwards referred to as the “Mouton Commission”.
\textsuperscript{8} From here and onwards referred to as the “1955 Act”.
\textsuperscript{9} From here and onwards referred to as the “1979 Act”.
\textsuperscript{10} One of the Competition Board’s challenges was the interpretation of “public interest” within the context of the 1979 Act. Although “public interest” was an important factor which the Competition Board had to take into consideration when investigating cases of alleged anti-competitive business practices, the 1979 Act did not specify how “public interest” should be interpreted (Fourie, 1987a: 333).
\textsuperscript{11} From here and onwards referred to as the “1998 Act”. This Act was amended in 1999 and twice in 2000 [Consolidated Act (undated): 1]. Where in this paper the researcher makes reference to the original version of the 1998 Act, the reference will be cited as the “1998 Act”. If reference is made to the 1998 Act with all its amendments incorporated, the reference will be cited as the “Consolidated Act” and the Consolidated 1998 Act will then be used as reference.
\textsuperscript{12} From here and onwards referred to as the “Commission”.
\textsuperscript{13} From here and onwards referred to as the “Tribunal”.
\textsuperscript{14} These three institutions are listed in increasing order of hierarchy.
\textsuperscript{15} “In the latest (1996) manufacturing census, for 46 per cent of the 57 main product groupings the largest four firms account for more than half of output, while in a further 35 per cent of groupings the four firm concentration ratio is between 0.25 and 0.50” (Chabane et al., 2003: 5).
explains the economic rationale for competition policy in South Africa, with a specific focus on the manufacturing sector. Cases that were investigated by the current Competition Authorities are also reviewed. Section 4 concludes.

2. MARKET POWER AND THE RATIONALE FOR COMPETITION POLICY

Case and Fair (1999: 297) define market power as “an imperfectly competitive firm’s ability to raise price without losing all demand for its product”. Imperfectly competitive firms therefore have some degree of pricing power (which perfectly competitive firms do not have). Firms with market power may be tempted to abuse their power by engaging in anti-competitive activities, such as collusion. Collusive behaviour results in lower production levels and higher prices relative to the perfectly competitive outcome, causing a market failure to occur. In order to regulate the degree of market power that firms have, prevent firms from abusing their power and to address the issue of market failures, regulation is required. These issues can be addressed by competition policy.

“On a general level, the objective of competition legislation is to address the issue of market failure as a result of anti-competitive behaviour and to provide a framework for the regulation of merger activity in an economy” (Competition Commission, 2000a: 10). Despite this, some countries, like South Africa, have included ancillary objectives in their legislation. This is usually done to co-ordinate competition policy with other macroeconomic policies and goals and to address country-specific problems. In South Africa’s case the country’s political history provides an additional rationale for implementing competition policy. South Africa has a long history of racial segregation, colonialism and apartheid, which caused income, wealth and ownership to become very unequally distributed between racial groups. These inequalities need to be rectified.

(a) The theoretical rationale for competition policy

i) Market power

A firm is said to have market power if it is able to increase the price of its product without losing all demand for it. If a firm is not able to do so, it has no market power, as is the case under perfect competition. Perfectly competitive firms are price takers and can either incur losses, make normal profits or make

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16 Perfectly competitive firms are price-takers of the market-determined prices for their products and face perfectly elastic demand curves. If these firms raise their products' prices above the market-determined prices, they will lose all demand for their products. Perfectly competitive firms therefore do not have any market power.

17 Arnold (2001: 701) defines a market failure as “a situation in which the market does not provide the ideal or optimal amount of a particular good”.

18 To achieve multiple objectives successfully, competition legislation has to be drafted carefully, especially when some of the legislation’s objectives may be conflicting. When objectives are in conflict, the Competition Authorities have to be provided with guidelines on how the objectives should be weighted. Without such information, the Competition Authorities have to use their own judgment. This increases the risk of lobby groups attempting to influence the Competition Authorities’ decision-making process to reap economic rent.

19 The reason why it is so important to take a country's history into account is that the past offers explanations for the country's current position.

20 The skew distribution of ownership in the economy provides the political-economic rationale for competition policy.
economic profits in the short run, but in the long run\textsuperscript{21} they can only make normal profits. Also, in the long run, perfectly competitive firms are both production and allocation efficient\textsuperscript{22}.

Imperfectly competitive firms\textsuperscript{23} (with market power) are, however, the rule rather than the exception and perfectly competitive firms are seldom found reality. The extent of a firm’s market power can be measured by the Lerner index\textsuperscript{24}:

\[ L = \left( \frac{P_i - MC_i}{P_i} \right) \]

The index has values of between (and including) zero\textsuperscript{25} and one (Pindyck and Rubinfeld, 2001: 341). The higher the value of the index, the more market power a firm has. The size of a firm’s market power is inter alia determined by the elasticity of the demand curve it faces. The more elastic the demand curve, the more sensitive consumers are to price changes, which implies that the producers only have limited market power. There is an inverse relationship between the elasticity of a demand curve and the extent of a firm’s market power. The elasticity of a demand curve is in turn influenced by the following factors: (i) the number of close-substitute\textsuperscript{26} products that are available (Case and Fair, 1999: 117); (ii) whether the product is a necessity\textsuperscript{27}, e.g. food, or a luxury item, e.g. a car (Koutsoyiannis, 1975: 48); (iii) the number of firms in the relevant market and (iv) the way in which those firms in the relevant market interact with one another (Pindyck and Rubinfeld, 2001: 345-346).

When a market has a relatively large number of firms, \textit{others paribus}, the level of competition between them tends to be higher\textsuperscript{28}, compared to a market with only a few firms. However, having a relatively large number of firms in a market offers no guarantee that competition levels will be high. A market may have of a relatively large number of small firms, but may be dominated by a few firms with market power, which lowers the level of competition. This is the case of oligopoly. Awh (1976: 323) defines oligopoly as “the market structure in which a few sellers who clearly recognize their mutual interdependence produce the bulk of the market output.” An oligopoly therefore takes the prices and output of its competitors as given and then sets its product’s price.

A variety of different oligopoly theories\textsuperscript{29} have developed over the years, all of which share three common characteristics: (i) a relatively small number of buyers and sellers participate in the market; (ii) either homogeneous or differentiated products are produced and (iii) entry barriers\textsuperscript{30} either makes market entrance difficult or impossible for potential competitors (Arnold, 2001: 555). Even if potential competitors are able to

\textsuperscript{21} Under perfect competition, long run equilibrium is where \( P = MR = LMC = LAC \) (the price per product is equal to the product’s marginal revenue, is equal to long run marginal cost per product, is equal to long run average cost per product).

\textsuperscript{22} According to Pareto, firms are production efficient if they produce at the minimum per-unit cost, which is at the minimum point on their LAC curve, and they are allocation efficient if \( P = MC \).

\textsuperscript{23} This includes monopolistic competitors, monopolies and oligopolies.

\textsuperscript{24} “\( P \)” is the price of product “i” and “MC” is product i’s marginal cost.

\textsuperscript{25} In a perfectly competitive market the Lerner index has a value of zero (as the price of product “i” is then equal to its marginal cost).

\textsuperscript{26} The more substitutes a product has, the greater the variety consumers have to choose from and the more sensitive they are to price increases of one product, relative to its substitutes.

\textsuperscript{27} The demand for necessities, \textit{others paribus}, less elastic, while the demand for luxurious goods tends to be more elastic.

\textsuperscript{28} The firms can compete so fiercely that they create an environment that closely resembles a perfectly competitive market where competitive prices are charged for products.

\textsuperscript{29} Some of these theories include the kinked demand curve theory, the price leadership theory, the Cournot model, Bertrand model, Stackleberg’s model, etc. (Arnold, 2001: 563, 565; Koutsoyiannis, 1975: 216, 225, 233).

\textsuperscript{30} Two forms of entry barriers may exist. The first is legal barriers that forbid potential competitors from entering the market. The second possible entry barrier is scale economies that are realized by the existing firms in the market (Arnold, 2001: 555).
enter the market, competition levels will not be raised unless the market power of the dominant firms is lowered.

ii) The social costs of market power under monopoly and oligopoly

One of the most widely used measures of social costs or welfare losses is consumer surplus. Consumer surplus is defined as the difference between the price that consumers are willing to pay for a product and the price that they actually pay for it. To estimate the social costs of monopoly, the size of consumer surplus is measured in the case of a monopoly and compared to the outcome under perfect competition. The outcome under a monopoly is illustrated as follows:

**Price**

![Diagram showing profit-maximization and social costs under monopoly.](source)

Figure 1 shows the downward-sloping demand curve (D), the marginal revenue curve (MR) and the marginal cost curve (MC). To keep the illustration simple, MC is assumed to be constant and equal to average cost (AC). Under perfect competition, the individual firm’s demand curve is the same as its marginal revenue curve. Profit-maximizing perfectly competitive firms will produce the quantity of products that corresponds with the point where price (P) equals marginal cost (MC) and the marginal cost curve intersects the demand curve, which is at point E. Output level $Q_c$ is produced and a per-unit price of $B$ is charged for the product. Consumer surplus is equal to the area FBE.

On the other hand, when a monopoly produces the product, it maximizes profit by producing the quantity of products that corresponds with the point where MC is equal to MR, which is at point D. The monopoly will produce output level $Q_m$ and charge a price of $A$ per unit of the product. Consumer surplus is now equal to the area FAC. Consumer surplus is therefore relatively larger under perfect competition, than under monopoly. The social cost of having a monopoly producer is equal to area ACEB, i.e. the size of the area lost due to having a monopoly rather than perfectly competitive firms produce the product. This area is, however, not all welfare that is lost to society. Area ABD'C is reallocated to producer surplus, but triangle CDE represents the dead-weight loss or welfare that is lost to society. McGee (1988: 20-21) finds evidence in support of this discussion. Next, the approach followed by Black et al. (1999) to measure the social cost of monopoly is discussed.

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31 Producer surplus is defined as the difference between what a producer is willing to receive for its product and what it actually receives for it.
Black et al. (1999: 34) employed the efficiency criteria of Pareto\(^{32}\) to measure the social costs of monopoly. They use the following graph as illustration:

**Quantity of good Y**

\[ \text{Figure 2. Monopoly, oligopoly and inefficiency} \]

Source: Black et al. (1999: 35)

In figure 2 the production possibility frontier \((R_0 T_0)\) for the production of goods X and Y is presented. The slope of the frontier measures the marginal rate of product transformation (MRPT) and in a perfectly competitive market \(\text{MRPT}_{xy} = \frac{\text{MC}_X}{\text{MC}_Y} = \frac{P_X}{P_Y}\) (Black et al., 1999: 6). If both products X and Y are produced by perfectly competitive firms, the price ratio of the two goods is equal to the marginal cost ratio and combination C is produced. Black et al. (1999: 34) then assume that good Y is produced by a monopoly, while good X is still produced by perfectly competitive firms. This shifts the production level to point \(M_0\), where the monopoly produces less of Y than the perfectly competitive firms have produced.

The implications of the discrepancy between the production level under perfect competition and the monopoly can be assessed by using Pareto’s two criteria for efficiency. Section 2.2.1 explained that perfectly competitive firms are both allocation and production efficient in the long run. When a monopoly produces good Y, it is neither production, nor allocation efficient in the short or the long run, as it charges a price for Y that exceeds the product’s marginal cost (\(P_Y > \text{MC}_Y\)). This results in the price ratio (\(P_Y/P_X\)) being smaller than the marginal cost ratio (\(\text{MC}_X/\text{MC}_Y\)). The discrepancy between the slopes of the frontier and the price line (\(P_M P_M\)) is shown in Figure 2. The price line is no longer tangent to the frontier, as its slope is smaller than the frontier’s. The price line intersects the frontier at point \(M_0\). When combination \(M_0\) is produced, less of Y is produced compared to the outcome under perfect competition.

All firms with market structures other than perfectly competitive and monopoly and with more market power than perfectly competitive firms, but less than monopoly (e.g. monopolistic competitors and oligopolies) produce quantities of output that fall between the levels of perfectly competitive firms (C in figure 2) and monopoly (\(M_0\) in figure 2). This results in a social cost to or excess burden on consumers. Only one of these market structures is studied in this paper, i.e. oligopoly. In oligopoly, the dominant firms may abuse their market power by colluding with one another. This leads to lower production levels and higher product prices, relative to the perfect competitive outcome (Needham, 1969: 154). The most extreme form of collusion is a cartel. When firms enter into a cartel arrangement, it is either enforced explicitly by a contract or

\[^{32}\text{These are production and allocation efficiency. Van den Bergh and Camesasca (2001: 5) identify a third category of efficiency, i.e. dynamic efficiency. Dynamic efficiency is “achieved through the invention, development, and diffusion of new products and production processes that increase social welfare” (Van den Bergh and Camesasca, 2001: 5).}\]

\[^{33}\text{Where “MC}_X\text{” is the marginal cost per unit of good X, “MC}_Y\text{” is the marginal cost per unit of good Y, “P}_X\text{” is the price per unit of good X and “P}_Y\text{” is the price per unit of good Y.}\]
by a tacit agreement between the parties involved. “Cartel behaviour is bad for consumers, business and efficient markets; and, unlike joint ventures, has no countervailing benefits. The OECD Report on Hard Core Cartels states that the cartelisation of a market leads to an average price increase of 10 per cent and a reduction in output of 20 per cent, with some price increases as high as between 30 and 35 per cent” (Competition Commission, 2000b: 17).

iii) Measurement of industrial concentration levels

Various34 measures can be used to calculate the level of concentration at different industrial levels, i.e. at the main group (3-digit SIC35), group (4-digit SIC) or subgroup (5-digit SIC) levels. Concentration measures are divided into two groups, i.e. absolute and relative measures. Absolute measures are divided into discrete and summary measures36 (Leach, 1992: 387-388). The two absolute measures most often used are the CRn ratio and the Herfindahl Hirschmann Index (HHI) (Fourie and Smit, 1989: 242). The CRn ratio37 is defined as the “percentage of total market sales (or capacity, or employment, or value added, or physical output)” contributed by the “n” leading firms in a market and the HHI38 measures the sum of the squared market shares of all the firms in a particular market (Annual Report, 2001: 49).

The following thresholds are used to classify the level of concentration in a market according to the Herfindahl Hirschmann Index (HHI):

Table 1. Thresholds of the Herfindahl Hirschmann Index (HHI)

<table>
<thead>
<tr>
<th>Herfindahl Hirschmann Index value</th>
<th>Extent of concentration in market</th>
<th>Maximum increase in HHI allowed before merger application likely to be unsuccessful</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 – 1000</td>
<td>Unconcentrated</td>
<td>N/a</td>
</tr>
<tr>
<td>1000 – 1800</td>
<td>Moderately concentrated</td>
<td>100</td>
</tr>
<tr>
<td>1800 and above</td>
<td>Concentrated</td>
<td>50</td>
</tr>
</tbody>
</table>

Source: Case and Fair (1999: 352)

Another absolute measure of concentration is the Rosenbluth Index39 (RI)40. This index takes the number of firms and any inequality in the distribution of market shares between firms in a market into account (Smith and Du Plessis, 1996: 4). Although the RI is used less often, it is an important measure in countries where market shares are unequally distributed between firms in specific industries. Fedderke and Szalontai (2004: 13) warn that the RI may not always be an appropriate measure as it may understate41 the level of concentration in a market.

34 “Ideally the choice of (concentration) measure should depend on the question that is being analyzed, and should not be decided in isolation or on a priori grounds. Each measure highlights different dimensions of the phenomenon (concentration) and sheds light on different aspects or issues” (Fourie, 1996: 115).

35 “SIC” is the abbreviation for Standard Industrial Classification codes used in the classification of industries. The higher the number of digits, the more narrowly defined the industry.

36 Discrete measures do not take all the firms in an industry into account when calculating the level of concentration, while summary measures do (Leach, 1992: 387).

37 A discrete measure.

38 A summary measure.

39 A summary measure.

40 “… the Rosenbluth is directly related to inequality of firm size and inversely related to the number of firms” (Leach, 1992: 388).

41 Fourie (1996: 103) also warns that the RI should be used with great care. Although the RI’s value increases as the distribution of market shares among firms grows more unequal, the true state of this unequal distribution may be “hidden” by a simultaneous increase in the number of small firms in the market.
Of the relative measures, the Gini coefficient⁴² and the Lorenz curve are the most familiar measure. Measuring the relative distribution in, or unevenness in the spread of some measure of business activity⁴³ among firms in a market, they reflect the level of concentration, or domination by a relatively small number of firms (Fourie and Smit, 1989: 242). Markets with high concentration levels due to a few firms dominating the market, may suffer a loss in competition as a result of the abuse of market power by dominant firms. If market shares are unequally distributed between firms, some of the firms may become dominant players with market power and consequently lower competition in the market.

iv) The predicted behaviour of firms with market power

The Structure-Conduct-Performance (SCP) paradigm was developed and first introduced by Edward Mason in the 1930s (Smit, 1999: 6). Mason postulated that a one-way causal link exists within the paradigm, with causality running from market structure, to conduct, to performance (Van den Bergh and Camesasca, 2001: 24). The original form of the SCP paradigm is illustrated as follows:

Table 2. The structure-conduct-performance (SCP) paradigm

<table>
<thead>
<tr>
<th>Structure</th>
<th>Conduct</th>
<th>Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Perfect competition</td>
<td>Marginal cost pricing</td>
<td>Allocation efficiency and equity</td>
</tr>
<tr>
<td>Imperfect competition</td>
<td>Departures from marginal cost pricing</td>
<td>Inefficiency and possible monopoly profits</td>
</tr>
</tbody>
</table>

Source: Reekie (1989: 38)

The original one-way causal link in the paradigm predicts that when concentration levels in markets are high (structure), it gives an incentive to firms to collude (conduct) and to raise the prices of their products to increase their profits (performance) (Black et al., 1999: 41). If this is true, then in order to address anti-competitive conduct and performance, a market’s structure has to be regulated. The structure can be changed through lowering entry barriers to the market, thereby making it easier for potential competitors to enter (Smit, 1999: 10). As discussed earlier, lowering the entry barriers will only contribute to higher levels of competition if, in conjunction with competitors entering the market, the market shares and the market power of the dominant firms in the market are lowered. One of the objectives of competition policy is to regulate the market power of firms and to give special attention to dominant⁴⁴ firms and ensure that they do not abuse their dominant positions.

Demsetz (1973) questioned Mason’s argument that high concentration levels always result in collusive behaviour (Reekie, 1991: 20). Demsetz introduced his “efficiency hypothesis” which postulates that all large firms do not necessarily engage in collusive activities and conduct business in an anti-competitive manner. “He argued that the high degree of market power and ownership concentration in many markets across the world is merely the outcome of a competitive process in which superior low-cost firms manage to outperform their less efficient counterparts” (Black et al., 1999: 42).

The complex organization of markets raised the question of whether this complexity could be captured by the simple SCP paradigm with a one-way causal link between market structure, conduct and performance (Reekie, 1991: 29). The validity of this link was tested empirically at Harvard University, the Massachusetts Institute of Technology and in several countries, including South Africa (Smit, 1999: 11; Reekie, 1999: 269).

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⁴² The Gini coefficient can take on values of between and equal to zero and one. A coefficient value of equal to zero indicates that market shares are equally distributed between the firms in a market. This implies that the market has a perfectly competitive market structure. The closer the value of the Gini coefficient is to one, the more unequally distributed market shares are between firms in a market and the more concentrated the market is.

⁴³ An example of a measure of business activity is the proportion of total industry output produced and supplied by a specific firm. This measures the firm’s market share.

⁴⁴ “Dominant firms are able to make profits by constraining supply and raising prices above marginal (and average) cost. Where there are a small number of firms in an industry, they can collude in stead of competing with one another in order to collectively generate monopoly profits” (Chabane et al., 2003: 1).
The results that were found contradicted the perception that a single one-way causal link exists (Smit, 1999: 6). Some researchers found feedback effects which ran from conduct to structure (Van den Bergh and Camesasca, 2001: 25). Once multi-directional causality and the feedback effects were found in the paradigm, it could no longer be used to make accurate predictions about the possible outcomes of concentrated markets. Despite this, some countries continue to use the paradigm as a point of departure in trying to understand industrial organization (Smit, 1999: 13-14).

b) The political-economic rationale for competition policy in South Africa

This section summarizes the main historical events that contributed to the development of high concentration levels in the South African economy. In 1814 Britain gained ownership of the Cape Colony from the Netherlands (Terreblanche, 2002: 179). After diamonds were discovered along the Orange River in 1867 and gold reefs along the Witwatersrand in 1886, a large number of foreigners immigrated to South Africa to share in the new employment and profit opportunities (McCarthy and Du Plessis, 2004: 11). The large-scale extraction of gold and diamonds advanced the development of the mining sector.

The discovery of gold and diamonds also attracted large foreign investments to South Africa. Due to the high risks and costs involved in conducting business in the mining sector, large capital outlays were required to make business profitable. Small mining enterprises had no choice but to merge to be able to enjoy economies of scale and conduct business profitably. This created a highly concentrated mining sector that was dominated by entities with “considerable economic power” (Mouton et al., 1977: 30).

The growing foreign demand for gold and diamonds was conducive to growth in the mining sector - a sector that became a large contributor to the country's foreign exchange earnings via exports (Nattrass, 1981: 145). As the sector expanded, demand for manufactured goods such as dynamite and mining equipment increased (Du Plessis, 1999: 37). The manufacturing sector was only in its infancy and its stock of capital was insufficiently low to enable the sector to provide for the total increase in demand for manufactured goods. The higher export earnings from the mining sector made the import of capital goods more affordable. This had a remarkable impact on the development of the manufacturing sector, as it enabled the sector to provide in the demand for manufactured goods (McCarthy, 1992: 449). Hereby a close link was established between the mining and manufacturing sectors.

“Mining houses started to diversify their activities and moved into the industrial (manufacturing) field, both directly and indirectly, allowing capital accumulated in the mining enterprises to be used to expand South African industrial capacity” (Nattrass, 1981: 164). This diversification caused conglomerates to develop in the mining sector (Mouton et al., 1977: 30). “Conglomerate control and dominance also extended into the manufacturing sector. It encompassed activities immediately downstream of the mining industry including mineral processing and chemical production. Industries that produced the key inputs for these sectors, particularly metals and engineering industries, were also characterized by conglomerate domination together with state-owned production (for example, Iscor). There were also close links with the financial sector. This served to reproduce and further extend conglomerate control of the other productive sectors” (Chabane et al., 2003: 6-7). The development of conglomerates increased the concentration of economic power and caused the level of competition in the economy to decline.

By the time that South Africa was decolonised and became the Union of South Africa in 1910, the power structures of the British were well established. After the election in 1924 the Pact government became the governing party. The Poor White problem had by then taken on serious dimensions and the government was pressurized to address this problem urgently (Van der Berg, 1992: 126). Government followed an inward-

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45 South Africa, having a scarcity in capital, managed to attract foreign capital to the new profit opportunities that were created after gold and diamonds were discovered. This foreign capital made an invaluable contribution to the development of the mining sector (Thompson, 2000: 110).

46 It seems that the formation of conglomerates contributed to the development of South Africa’s predominantly oligopolistic market structure.

47 The Pact government was a coalition between the National Party, under the leadership of General JBM Hertzog and the Labour Party, led by Colonel Cresswell (Thompson, 2000: 160).
oriented industrialization policy and wanted to create employment opportunities for the Poor Whites through enhancing the industrialization process (McCarthy and Du Plessis, 2004: 13). This was achieved through greater direct and indirect government intervention (Terreblanche, 2002: 274).

The apartheid era, which commenced after the National Party won the 1948 election, saw the continuation of policies that protected the South African economy from competition, causing concentration levels to remain high (Belli et al., 1993: 2). The National Party’s main objective was to “raise the status of Afrikaners and erase the indignities they had suffered at the hands of the English” (McGregor and McGregor, 1990b: 351). Government wanted to create a welfare state for the white population, at the expense of other racial groups. Hence they passed apartheid laws that heralded the start of the apartheid era.

The growing inequality between the whites and other racial groups and the discrimination against the latter caused political unrest in South Africa. The political instability that the country experienced from the 1960s and onwards and the oil crises during the 1970s changed the attractiveness of investment opportunities in the country. A climax was reached in 1985, when South Africa experienced a debt crisis. Foreign countries imposed economic and financial sanctions to express their opposition to the apartheid regime (McCarthy and Du Plessis, 2004: 13). Exchange controls that were imposed on residents and non-residents of South Africa restricted the amount of capital that could be moved from the country. As a result, domestic firms could only take a limited amount of capital from the country to make foreign investments and also, mergers and acquisitions were poorly regulated. As a result new opportunities emerged for domestic firms to grow through mergers and acquisitions (McGregor and McGregor, 1990b: 352).

In 1987 the National Party agreed to the privatization of the large corporations, but only if it was in the public’s best interest. Through privatization the economic power of powerful state-owned monopolies could be broken and the high concentration levels could be lowered (Terreblanche, 2002: 77). In 1992 the African National Congress (ANC) declared the need for a more equal spread of economic power away from conglomerates and the urgent need for effective competition policy to deal with monopolies and mergers (Ready to govern in Terreblanche, 2002: 88; OECD, 2003: 5).

3. COMPETITION POLICY IN SOUTH AFRICA: 1955-2004

This section provides an overview of competition policy in South Africa since 1955. Its main focus is on the manufacturing sector, where the market structure is predominantly oligopoly and the need for regulation obvious. The aim of the section is twofold. Firstly, it aims to familiarize the reader with the highly concentrated structure of the manufacturing sector. Secondly, it discusses the three competition Acts that South Africa has implemented since 1955. Each Act is discussed within the context of the highly concentrated manufacturing sector.

a) The Regulation of Monopolistic Conditions Act of 1955

South Africa’s first comprehensive competition legislation, the Regulation of Monopolistic Conditions Act, dates back to 1955 and the Board of Trade and Industry was placed in charge of administering the Act (DTI, 1997: 13). The 1955 Act opposed, but did not per se prohibit, anti-competitive conduct by firms (Mouton et
al., 1977: 9). The functions of the Board were that of “investigating (firms’) conduct, recommending remedies, and negotiating and supervising compliance (with the 1955 Act)” (OECD, 2003: 4). The Board did not enjoy independence from the government and their activities were restricted to mandates to investigate specific cases, which they received from the Minister of Trade and Industry (Mouton et al., 1977: 12).

During the 1970s the Mouton Commission launched an investigation to determine the effectiveness of the 1955 Act and they also published their empirical results of concentration measures that they calculated from data of the year 1972 (Mouton et al., 1977: 27). They found high levels of concentration in all four of the sectors of the economy that they studied (Mouton et al., 1977: 41). This confirmed that the market structure of the economy was predominantly oligopoly (DTI, 1997: 13). They also criticized the 1955 Act for not allowing the Board to act independently of government (OECD, 2003: 5). The Mouton Commission concluded that the 1955 Act was ineffective and “that oligopoly had intensified dramatically in spite of the Act” (DTI, 1997: 13). Consequently, new competition legislation was promulgated.

b) The Maintenance and Promotion of Competition Act 96 of 1979

The Maintenance and Promotion of Competition Act 96 was promulgated in 1979 and the Competition Board was appointed to administer the Act (Reekie, 1999: 257; OECD, 2003: 5). The 1979 Act did not prohibit restrictive practices or anti-competitive behaviour per se (Smith, 1992: 469). In this regard, the 1979 Act was identical to its ineffective predecessor. The Competition Board was “an administrative body without executive authority which was housed within the Department of Trade and Industry and made recommendations to the Minister (of Trade and Industry). The Minister then decided on whether to accept or reject the recommendations, and the action to be taken” (Roberts, 2003: 7; OECD, 2003: 5).

In 1984 the Competition Board launched an investigation into restrictive practices. As a result of this investigation, the 1979 Act was amended in 1986 and the following practices were classified as being prohibited per se: (i) resale price maintenance; (ii) horizontal price fixing by firms; (iii) horizontal collusion between firms to divide a market between them and (iv) horizontal collusion by firms to ensure success when tendering for projects (OECD, 2003: 5; Fourie, 1987b: 227). These amendments empowered the Competition Board “to act not only against new concentrations of economic power but existing monopolies and oligopolies, the scope to examine financial institutions and agricultural cooperatives and control boards (previously exempted), and the mandate to consider deregulation and privatization of state-owned enterprises” (DTI, 1997: 14). Despite these changes, the Act remained “inadequate to deal with the competition challenges facing South Africa” (Hartzenberg, 2002: 7).

55 During the time that the 1955 Act was effective, the Board dealt with only eighteen investigations (OECD, 2003: 4).
56 These are manufacturing, wholesale and retail trade, construction and transport (Mouton et al., 1977: 39).
57 The literature discusses a variety of reasons for the high prevalence of oligopoly, including scale factors, protectionism, poor regulation of merger activities and the development of conglomerates (DTI, 1997: 13; OECD, 2003: 3).
58 From here and onwards referred to as the “1979 Act”.
59 Because anti-competitive business practices were not prohibited, firms conducting these practices could not be prosecuted.
60 The function of the Competition Board was set out as “to supervise restrictive practices and monitor acquisitions” (Mouton and Lambrechts (1982), in Fourie, 1987a: 341).
61 This quote evidently shows that the Competition Board could not act independently of government.
62 These challenges refer to the highly concentrated market structure in the South African economy (especially in the manufacturing sector), which resulted in lower levels of competition.

i) Market structure of the manufacturing sector

The Mouton Commission’s pioneering work on measuring concentration levels in the manufacturing sector was followed up only several years later by researchers such as Fourie and Smit (1989), Leach (1992), Fourie (1996) and Smith and Du Plessis (1996), due to the unavailability of data to conduct these studies (Fourie, 1996: 97).

The results of Fourie and Smit (1989: 244, 251) confirmed the existence of high concentration levels and they found that concentration increased from 1972 to 1982. Leach (1992) measured concentration for the period 1972 to 1985 and criticized Fourie and Smit (1989) for having used a relative concentration measure, the Gini coefficient (Fourie, 1996: 106; Leach, 1992: 386). “Leach argued that absolute measures were superior to relative measures because they took cognizance of both inequality and the number of firms” (Smith and Du Plessis, 1996: 4). A discrete measure used by Leach, the 80 per cent occupancy count, showed no change from 1972 to 1985. He also found that the value of the RI, on average, declined from 1972 to 1985. Leach concluded that in total there was no change, or perhaps a marginal decline, in the sector’s concentration levels from 1972 to 1985 (Leach, 1992: 396). Leach’s findings clearly contradicted those of Fourie and Smit (1989).

When the Central Statistical Service (CSS) released a new comprehensive data set that enabled researchers to measure concentration levels, Fourie used this data set and repeated the study done by himself and Smit in 1989 to determine the validity of Leach’s claim of a decline in concentration levels from 1972 to 1985 (Fourie, 1996: 98). Fourie also wanted to add his results to the Mouton Commission’s results to get an idea of the trend in concentration levels (Fourie, 1996: 104-105). Fourie’s results are presented below:

<table>
<thead>
<tr>
<th></th>
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<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>CR3</td>
<td>0.3417</td>
<td>0.3867</td>
<td>0.3517</td>
<td>0.3667*</td>
</tr>
<tr>
<td>CR4</td>
<td>0.4237</td>
<td>0.4065</td>
<td>0.4278</td>
<td></td>
</tr>
<tr>
<td>CR10</td>
<td>0.5564</td>
<td>0.5631</td>
<td>0.5592</td>
<td>0.5848 **</td>
</tr>
<tr>
<td>Herfindahl</td>
<td>0.0966</td>
<td>0.0910</td>
<td>0.1005</td>
<td></td>
</tr>
<tr>
<td>Horvath</td>
<td>0.2431</td>
<td>0.2597</td>
<td>0.2602</td>
<td>0.2639 **</td>
</tr>
<tr>
<td>Rosenbluth</td>
<td>0.0622</td>
<td>0.0591</td>
<td>0.0597</td>
<td>0.0591</td>
</tr>
<tr>
<td>Gini</td>
<td>0.7019</td>
<td>0.6241</td>
<td>0.6209</td>
<td>0.6438 *</td>
</tr>
<tr>
<td>Average number of firms</td>
<td>401</td>
<td>590</td>
<td>576</td>
<td>656</td>
</tr>
</tbody>
</table>

Source: Fourie (1996: 106)

? Due to data unavailability the statistical significance with regard to CR3 cannot be tested.
* Change statistically significant at 5 per cent level.
** Change statistically significant at 10 per cent level.

NOTES:
1. These averages are based on 29 sectors, and exclude the category “other manufacturing industries”.
2. CR3 averages for 1982-1988 was calculated from a frequency distribution provided by the CSS, with all categories included (Fourie 1996: 106).

The results confirm high and increasing concentration levels, as found by Fourie and Smit (1989). Fourie (1996: 107) found the decline in RI’s value from 1972 to 1988 as statistically insignificant, thereby contradicting Leach’s findings. It can therefore be concluded that the manufacturing sector was confronted by high and increasing concentration levels during the 1970s and 1980s.

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63 The 80% occupancy count counts the number of firms that collectively contribute a total of 80 per cent to the total sales of an industry (Leach, 1992: 389).
64 The Central Statistical Service is known today as Statistics South Africa.
65 In this study Fourie measured concentration at 3-digit levels.
66 “The main weakness of his (Leach’s) calculations is the exclusion of four industries, especially two large and very highly concentrated industries, the tobacco industry (Rosenbluth value of 0.58) and the petroleum industry (Rosenbluth value of 0.31)” (Fourie, 1996: 107).
ii) The predicted behaviour of firms with market power

The original version of the SCP paradigm postulated that a one-way causal link (running from structure to conduct to performance) exists. It is very important to know whether the SCP paradigm is valid in the manufacturing sector and, if found to be valid, the direction that causality runs in the paradigm. The reason is that the direction of causality determines how policy should be implemented. When the validity of the one-way causal link was questioned internationally, the paradigm was tested in several countries, including South Africa (Smit, 1999: 11; Reekie, 1999: 269). Leach (1997) found “a strong and significant positive correlation between the degree of concentration and the profitability of industries within the manufacturing sector of South Africa” (Black et al., 1999: 42). This finding either proves one-way causality or is evidence in support of Demsetz’s efficiency hypothesis (Reekie, 1999: 269). Reekie (1991) also tested the validity of the claimed one-way causal link and found evidence in support of it (Reekie, 1991: 36). Fourie and Smith (1998) also support this finding (Reekie, 1999: 269).

“Internationally the SCP paradigm has been discredited as too simplistic and the emphasis has moved to more comprehensive game theoretic models” (Theron, 2001: 621). Despite the SCP paradigm losing its popularity internationally, the Competition Board was convinced by the validity of the paradigm’s original one-way causal link, as explained by the following quote: “Daar kan dus aanvaar word dat struktuur gebreke in die Suid-Afrikaanse mark tot beperkende praktyke sal lei” (RSA, 1985: 30, in Fourie 1987a: 346).

When alleged restrictive business practices were investigated, the Competition Board had to determine whether the practice was in the public’s interest and if not, they had to refer the case to the Minister of Trade and Industry to decide on the appropriate action to take (McGregor and McGregor, 1990a: 326). The Competition Board’s interpretation of “public interest” was influenced by arguments brought forward by the respective parties involved in the investigations. The Competition Board admitted that they had no easy task when deciding what was in the public’s interest and this uncertainty led to inconsistent application of the 1979 Act (Fourie, 1987a: 336-337).

iii) Economic and political changes during the 1990s

In 1994 South Africa made the political transition to a representative democracy. The ANC inherited an economy that was characterized by high concentration levels, inequality between racial groups and trade protection. The government wanted to restructure the economy, as these stated problems act as constraints to economic growth and development (OECD, 2003: 5). The ANC’s objectives included liberalizing trade and breaking the economic power of conglomerates to lower concentration levels and to spread ownership more equally.

On 2 December 1994 South Africa joined the World Trade Organisation (WTO), thereby committing to liberalizing trade over time (Du Plessis, 1999: 68). Through trade liberalization South Africa’s domestically produced goods and services became exposed to import competition. Trade liberalization usually lowers import competition can be expected to improve resource allocation and application, and limit the abuse of market power by domestic firms” (Hartzenberg, 2002: 2).
concentration levels as foreign companies’ products and services penetrate the liberating country’s markets (Hartzenberg, 2002: 1), but in South Africa’s case it caused concentration levels to rise in some sectors of the economy (Roberts, 2003: 4). The reason is that inefficient South African firms either closed down or were acquired by more efficient ones to create new entities that had a better chance of competing successfully in the international markets. This left markets with fewer competitors and higher concentration levels (Chabane et al., 2003: 12).

What might have lowered concentration levels and at least started to address the issue of an unequal spread of ownership in the economy was the break-up of conglomerates. Despite the ANC’s initial fears that these break-ups would result in the withdrawal of foreign investors’ investments from these companies, the break-up process started in 1993 with Gencor\(^73\) (Smith, 1992: 476; Chabane et al., 2003: 12). As trade liberalization and the break-up of conglomerates had contradictory effects on concentration levels in some sectors, it is impossible to conclude without thorough investigation whether concentration levels in the economy as a whole, but more specifically in the manufacturing sector, declined during the 1990s. The changes in the concentration levels in selected parts of the manufacturing sector are investigated next.

In the researcher’s search for more recent studies on concentration levels in the manufacturing sector that are similar to those\(^74\) referred to earlier, only one study\(^75\) could be found. The researcher constructed a table\(^76\) that contains data on the extent of concentration\(^77\) in a variety of major groups and subgroups in the manufacturing sector that were calculated by Statistics South Africa\(^78\). Unfortunately the classification of most of the groups have changed from the 1980s to the 1990s, inter-temporal comparisons of these groups are difficult. Therefore, only those major groups and subgroups whose classification has not changed were included in the table. The data on concentration levels during the 1980s have been included to form a picture of the trend.

The CR4 measure shows that seven\(^79\) out of the eighteen groups experienced increases in concentration from 1988 to 1996. The other eleven groups’ concentration levels either remained relatively unchanged or decreased. Although many of these groups experienced increases in concentration during the 1980s, some of them show declines during the 1990s. For eight\(^80\) of the eighteen groups the RI’s value increased from 1989 to 1991, while for all of the groups, except two\(^81\), the RI’s value decreased from 1993 to 1996.

Fedderke and Szalontai (2004: 31) found evidence in support of earlier researchers’\(^82\) findings of high concentration levels in the manufacturing sector. They found mixed results\(^83\) for the RI, making it impossible to conclude whether concentration levels in the manufacturing sector overall increased or declined from 1972 to 1996 (Fedderke and Szalontai, 2004: 7).

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\(^73\) Other examples of conglomerate break-ups include Anglo American Corporation, Sanlam and Liberty Life (Roberts, 2003: 3).


\(^76\) See Appendix A.

\(^77\) As measured by the four-firm concentration ratio (CR4), ten-firm concentration ratio (CR10), Herfindahl Hirschmann Index (HHI) and the Rosenbluth Index (RI). The former three measures were chosen based on the fact that they are the measures that are most often used in the literature. The RI was included due to Fedderke and Szalontai (2004) having used this measure in their study.

\(^78\) This information was published in their Census of Manufacturing for 1988, 1991, 1993 and 1996.

\(^79\) These groups are: Butter and cheese; Beverages; Manufacture and refining of sugar and golden syrup; Cocoa, chocolates and sugar confectionary; Women’s and girls’ clothing; Footwear and Glass and glass products.

\(^80\) These groups are: Butter and cheese; Beverages; Slaughtering, dressing and packing of livestock; Manufacture and refining of sugar and golden syrup; Cocoa, chocolates and sugar confectionary; Footwear; Iron and Steel Basic Industries; and Glass and glass products.

\(^81\) These groups are: Beverages and Women’s and girls’ clothing.


\(^83\) In some of the groups, concentration levels increased from 1972, while they declined in others.
Based on the results of Fedderke and Szalontai (2004) and the figures in the table in Appendix A, concentration levels in the manufacturing sector remain high, despite the efforts that have been made to break up conglomerates’ economic power and having implemented competition policy. The persistence of the high concentration levels served as one argument\(^\text{84}\) in favour of formulating new competition legislation that could replace the 1979 Act (Du Plessis, 1999: 130). The next section discusses South Africa’s current competition legislation, the Consolidated Act.

d) The Consolidated Act

This section only discusses selected sections of the Consolidated Act, including the Act’s objectives, briefly explaining some of the business practices that are prohibited by the Act and the procedures that are followed when a merger application is processed. Three case studies\(^\text{85}\) are also included.

In 1998 South Africa adopted new competition legislation, Competition Act 89 of 1998, which became effective on 1 September 1999. The formulation of the 1998 Act was preceded by extensive consultations with policy makers of other countries to ensure that the best qualities of their competition legislation be incorporated into the new legislation, while taking the country’s specific needs into consideration (Lewis, 2000: 1). Similar to the 1998 Act’s predecessor, public interest issues\(^\text{86}\) have been included in the Act.

In terms of the 1998 Act three independent institutions were established to replace the Competition Board and administer the Act: the Competition Commission, the Competition Tribunal and the Competition Appeal Court. Each institution received a specific mandate. The Commission is responsible for “merger evaluations; investigations; exemption evaluations; advisory opinions; policy and research; education and information; and legislative reviews” (Annual Report, 2001: 7). The Tribunal deals with inter alia complaints and merger cases referred to them by the Commission and consider applications for large\(^\text{87}\) mergers (Competition Commission, 2000a: 17). Any cases that the Commission and Tribunal are unable to decide on are referred to the Competition Appeal Court.

The Competition Appeal Court has the highest jurisdiction of the three institutions and is in the position to change any decision that has been made by the other two institutions. No court in South Africa, not even the Supreme Court of Appeals, has jurisdiction over the Competition Authorities (Lewis, 2000: 2). The next section briefly discusses the amendments that have been made to the 1998 Act and introduces the reader to the objectives of the Consolidated Act.

\(^{84}\) Other arguments included globalization and trade liberalization that exposed South Africa to international competition and required South Africa to produce more efficiently and “the perceived ineffectiveness of the previous Competition Act (1979 Act) in a number of areas of application” (Competition Commission, 2000a: 16; Du Plessis, 1999: 130). An investigation that was launched by the Department of Trade and Industry found the 1979 Act to be inefficient. They proposed that the Act be replaced by new legislation that could deal with issues that were not addressed by the then current Act. Some of these issues included that the 1979 Act did not deal with vertical mergers and pre-merger notification to the Competition Board was not compulsory (OECD, 2003: 7).

\(^{85}\) These cases were all handled by the current Competition Authorities.

\(^{86}\) The same public interest issues have been included in both the 1998 Act and the Consolidated Act. These are set out in section 16(3) of the 1998 Act and in section 12(3) of the Consolidated Act. The Competition Authorities have to take these public interest issues into account when deciding whether a merger should or should not be allowed. Examples of these considerations include the effect a merger may have on employment and ensuring that small and medium-sized enterprises (SMEs) owned by previously disadvantaged individuals are not restricted from successfully competing in the economy [Consolidated Act (undated): 26].

\(^{87}\) As stipulated by specific thresholds in the Act.
i) Amendments to the 1998 Act and the amended Act’s objectives

The 1998 Act was amended\(^{88}\) in 1999 and twice in 2000. The following eight objectives have been included in the preamble of the Act:

1. “provide all South Africans equal opportunity to participate fairly in the national economy;
2. achieve a more effective and efficient economy in South Africa;
3. provide for markets in which consumers have access to, and can freely select, the quality and variety of goods and services they desire;
4. create greater capability and an environment for South Africans to compete effectively in international markets;
5. restrain particular trade practices which undermine a competitive economy;
6. regulate the transfer of economic ownership in keeping with the public interest;
7. establish independent institutions to monitor economic competition; and
8. give effect to the international law obligations of the Republic”\(^{89}\)

Source: Consolidated Act\(^{90}\): 2

Even though the purpose of competition policy is to remedy market failures and regulate mergers, the objectives listed above show that the Competition Authorities are not only concerned with competition-related issues. The second, third, fifth and sixth objective are standard objectives in competition legislation (Singleton, 1992: 3). South Africa’s political-economic history provides the rationale for having included the first objective and gives an additional rationale for including the sixth objective. The fourth objective is usually pursued by trade policy and the seventh objective has already been achieved.

In order to achieve the second, third, fifth and sixth objective successfully, these have to be pursued as long term goals. If effective competition legislation is applied properly, the highly concentrated industries can be reformed and anti-competitive practices can be removed from the economy, making it possible to successfully achieve the objectives. Since the current competition legislation was effectively implemented only seven years ago and Statistics South Africa has not released a Census of Manufacturing since the one for 1996, it is difficult to evaluate whether the competition authorities are successfully achieving the second, third, fifth and sixth objective, which can only be achieved once concentration levels are lowered. The Commission’s Annual Report for 2004 includes a statement\(^{91}\) by the Commissioner\(^{92}\), which shows that the Commission has a clear understanding of what is expected of them.

Reekie (1999: 258-259) has criticized the Act for containing objectives that generally fall outside the jurisdiction of competition policy (i.e. the first and fourth objective). Although Reekie recognizes the importance of addressing past inequalities, he is convinced that competition policy is not the appropriate instrument to use. The researcher took cognizance of Reekie’s argument and hence decided to discuss each of

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\(^{88}\) These amendments included clarifications of definitions in the Act, the removal of loopholes and the addition of sections to the Act (Competition Commission, 2001a: 5).

\(^{89}\) The intended meaning of this objective is unclear, but the researcher suspects that with this objective the competition authorities aim to bring South African competition law in line with international obligations that exist due to the signing of certain international agreements and belonging to institutions such as the WTO. Objective eight will not be discussed any further.

\(^{90}\) Undated.

\(^{91}\) “We (the Commission) are an independent, economy-wide agency that investigates, controls and evaluates restrictive practices, abuses of dominant position, and mergers. The overall objective is that of promoting and maintaining competition in the market. Our goal of achieving a more just and vigorous economy is expected to, amongst other things, provide consumers with competitive prices and product choices. Our role is therefore to level the playing field so that enterprises, big and small, can compete fairly” (Annual Report, 2004: 1).

\(^{92}\) Advocate Menzi Simelane.
the relevant objectives separately, to determine to what extent competition policy is able to successfully achieve these objectives.

The first objective aims to address the unequal spread of ownership in the economy. “The present-day government recognized the need to use the promotion of SMEs as a means to address past inequalities, create jobs, upgrade skills, redistribute income, democratise the economy, reduce poverty and ensure economic growth. SME development and Black Economic Empowerment (BEE) are commonly seen as broadening the economic base, thus making it more inclusive of the previously disadvantaged black majority” (Strydom, 2002: 7; Smith, 1992: 464). The implementation of BEE charters in industries have resulted in the transfer of ownership to previously disadvantaged individuals. As a result, there are an increased number of mergers and acquisitions that contain a BEE component, which could show that the business sector supports the government’s empowerment policy (Erwin, 2003: 3; Competition Commission, 2004a: 6). However, sufficient progress has not been made in empowering the majority of the group of previously disadvantaged individuals and ownership in the economy is still to a great extent concentrated in white hands. To keep in line with government’s empowerment policies an argument can therefore be made for having included BEE as an objective in South Africa’s competition legislation. In the pursuit of BEE, it should not merely result in the transfer of ownership from a few white individuals to a small black elite. BEE should be applied in the interest of everyone, or at least the majority of the previously disadvantaged individuals.

The fourth objective aims to reform the South African economy into one that can successfully compete in global markets. “Over the past years, the government’s economic strategy has been to create growth and employment through developing the domestic sectors and making the economy more competitive” (Annual Report, 2001: 5). This quote supports the fact that objective four falls within the jurisdiction of the government’s trade policy. Despite this, competition policy has an important role to play in assisting trade policy to achieve the objective of a more competitive economy. For a country to experience export-led growth, domestically produced goods have to be able to compete in global markets. The protectionism that South African industries enjoyed during the 20th century contributed to the development of highly concentrated and uncompetitive markets.

The basis for Reekie (1999)’s criticism against having public interest issues and ancillary objectives included in the Consolidated Act is that the objectives may be conflicting. In such a case, competition authorities have to make difficult trade-offs between which objectives to pursue (Reekie, 1999: 259). Dave Lewis has defended the inclusion of ancillary objectives and public interest issues in the Act. He argues that the high levels of poverty and inequality need to be addressed urgently and this requires that all the country’s policies need to be directed towards addressing these problems (Lewis, 2000: 3). Lewis (2002: 2) made a statement that illustrates the importance of having included these objectives: “Hence, in a country like South Africa while we, the Competition Authorities, may well understand the pitfalls in balancing competition and the public interest, we equally recognize that a competition statute that simply ignored the impact of its decisions on employment or on securing greater spread of black ownership, would consign the act and the authorities to the scrap heap.” One shortcoming of the Consolidated Act is that it does not provide guidelines for the

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93 The government’s ability to promote SMEs can be constrained by restrictive practices that are conducted by firms and the high prevalence of oligopolies in the economy. The concentrated market structure of the economy may make it difficult for SMEs to compete with established large firms with market power. This stresses the urgency with which the high concentration levels in the economy need to be lowered.
94 An example of a case containing a BEE component is the joint venture between Rustenburg Platinum Mines Ltd and the Royal Bafokeng Nation (Annual Report, 2003: 32).
95 “The Commission has adopted the approach that competition in the domestic market is of primary importance. Accordingly, the Commission has rejected arguments that mergers should be allowed if they would lead to foreign competitiveness where this comes at the expense of local consumers. Nevertheless, where such mergers lead to inefficiencies that will be passed on to consumers, or where the pricing behaviour of the merged entity will be constrained by the presence of import competition, the Commission will not stand in the way of local firms growing to become competitive” (Annual Report, 2003: 30-31).
96 The chairperson of the Competition Tribunal.
weighting of the ancillary, compared to the purely competition-related, objectives in investigations (Competition Commission, 2003b: 14).

ii) Regulation of prohibited practices and mergers

ii.i) Regulation of prohibited practices

ii.i.i) An overview of prohibited practices

The main objective of regulating prohibited practices is to ensure that business is not conducted in a way that is harmful to competitors or in a way that lowers the level of competition in the economy (Competition Act97: 6). “Prohibited practices”98 are divided into two categories, i.e., abuse of dominance and restrictive practices. The latter is again divided into horizontal and vertical practices. Examples of horizontal practices include “price fixing, dividing markets in terms of specific allocations and collusive tendering.” Vertical practices include “the practice of minimum resale price maintenance” (Competition Commission, 2000a: 17). Only the abuse of dominance and prohibited vertical practices are discussed in this paper.

ii.i.ii) A base of dominance

Section 7 of the Consolidated Act defines dominance as follows: “A firm is dominant in a market if –
(a) it has at least 45%99 of that market;
(b) it has at least 35%, but less than 45%, of that market, unless it can show that it does not have market power; or
(c) it has less than 35% of that market, but has market power.”
Source: Consolidated Act100: 17

Before a case of alleged abuse of dominance101 can be made against a firm, it first has to be proven that the firm is dominant in its market, by using the criteria quoted above. When a firm fits the criteria in (a), there is no defence against dominance; if it fits the criteria in (b), the defendant has to prove that it does not have market power and if it fits the criteria in (c), the onus lies on the competition authorities to prove that the firm has market power (Annual Report, 2000: 35).

It should be noted that it is not the size of a firm per se that poses the problem. The size of a firm only becomes a problem when dominant firms abuse102 their market positions (Black et al., 1999: 43). Large firms

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97 Undated.
98 Prohibited practices are regulated by Chapter Two of the Consolidated Act.
99 These percentages can either be calculated using a firm’s total annual turnover or total assets on its balance sheet [Consolidated Act (undated): 16]. “And, in addition, the (competition) authorities must stipulate in advance how, in relation to specific industries these percentages are to apply” (Reekie, 1999: 267). The percentages are considered as being arbitrary values and only serve as guidelines to the Competition Authorities (Reekie, 1999: 269).
100 Undated.
101 Examples of such cases include the South African Raisins vs. South African Dried Fruit Holdings Ltd, the Commission vs. Sappi Fine Papers (Pty) Ltd and GlaxoSmithKline (Pty) Ltd and Boehringer Ingelheim (Competition Commission, 2001b: 15; Competition Commission, 2002: 10 and Competition Commission, 2004a: 9).
102 According to Section 8 of the Consolidated Act “it is prohibited for a dominant firm to –
(a) charge an excessive price to the detriment of consumers;
(b) refuse to give a competitor access to an essential facility when it is economically feasible to do so;
(c) engage in an exclusionary act, other than an act listed in paragraph (d), if the anti-competitive effect of that act outweighs its technological, efficiency or other pro-competitive gain; or
may realize economies of scale that enable them to produce at relatively lower costs and this may be beneficial
to consumers, who pay lower prices for products. The Competition Authorities should, however, be cautious
when firms that apply for a merger argue that economies of scale will result from a merger. Evidence\textsuperscript{103}
shows that these so-called “promises” of scale economies seldom materialize. The next section discusses the
case where GlaxoSmithKline South Africa (Pty) Ltd and Boehringer Ingelheim were accused and found guilty
of abusing their dominant positions.

\textit{i.ii.iii) Case study: A abuse of dominance by GlaxoSmithKline South Africa (Pty) Ltd and Boehringer
Ingelheim\textsuperscript{105}}

On 17 September 2002 the Treatment Action Campaign (TAC) filed a complaint against GSK and other
pharmaceutical manufacturers for allegedly abusing their dominant positions\textsuperscript{106} (Coode, 2002: 1). The
Commission’s investigation found GSK and BI guilty of having engaged “in the following restrictive practices:

1. Denied a competitor access to an essential facility\textsuperscript{107};
2. Excessive pricing\textsuperscript{108};
3. Engaged in an exclusionary act\textsuperscript{109}.”

Source: Coode (2003: 1)

GSK and BI owe their dominant positions to the fact that they have patents for the manufacturing of some
anti-retroviral medicines (Competition Commission, 2003c: 2). These patents created monopoly
manufacturers in the relevant markets, which made it possible for the firms to raise their products’ prices
above competitive prices without the fear of losing all demand for it. This happened to the detriment of
those seeking treatment for HIV/AIDS. Before the case was referred to the Tribunal, GSK and BI
approached the Commission in an attempt to reach agreements that would make a referral to the Tribunal
unnecessary (Annual Report, 2004: 13). “In terms of these agreements we (the Commission) agreed not to
refer the complaints to the Tribunal on condition that GSK (four) and BI (three) issued a total of at least
seven licences for their patented anti-retroviral drugs to generic manufacturers” (Annual Report, 2004: 13).
With this agreement the Commission wanted to lower GSK and BI’s dominance in the relevant market by

(d) engage in any of the following exclusionary acts, unless the firm concerned can show technological,
efficiency or other pro-competitive gains which outweigh the anti-competitive effect of its act –

(i) requiring or inducing a supplier or customer to not deal with a competitor;
(ii) refusing to supply scarce goods to a competitor when supplying those goods is
economically feasible;
(iii) selling goods or services on condition that the buyer purchases separate goods and services
unrelated to the object of the contract, or forcing a buyer to accept a condition unrelated
to the object of the contract;
(iv) selling goods and services below their marginal or average variable cost; or
(v) buying up a scarce supply of intermediate goods or resources required by a competitor.”

[Consolidated Act (undated): 17, 18].

\textsuperscript{103} For example, the proposed merger between BP, Shell and Caltex (Theron, 2001: 633), the proposed merger
between Tongaat-Hulett Group Limited and Transvaal Suiker Beperk, Middelen Ontwikkeling (Pty) Ltd, Senteeko (Edms) Bpk, New Komati Sugar Miller’s Partnership and TSB Bestuursdienste and the merger
between Distillers Corporation (SA) Limited and Stellenbosch Farmers’ Winery Group Ltd (Competition
Tribunal, 2000b and Competition Tribunal, 2002).

\textsuperscript{104} From here and onwards referred to as “GSK”.

\textsuperscript{105} From here and onwards referred to as “BI”.

\textsuperscript{106} These practices were allegedly conducted in the markets for anti-retroviral medicine (Coode, 2003: 1).

\textsuperscript{107} This is a violation of section 8(b) of the Consolidated Act.

\textsuperscript{108} This is a violation of section 8(a) of the Consolidated Act.

\textsuperscript{109} This is a violation of section 8(c) of the Consolidated Act.
allowing competitors to enter and increase the level of competition in the market. The next section discusses prohibited restrictive vertical practices.

ii.i.iii) Prohibited restrictive vertical practices

Section 5 of the Consolidated Act defines prohibited vertical practices as follows:

“(1) An agreement between parties in a vertical relationship is prohibited if it has the effect of substantially preventing or lessening competition in market, unless a party to the agreement can prove that any technological, efficiency or other pro-competitive, gain resulting from that agreement outweighs that effect.
(2) The practice of minimum resale price maintenance is prohibited.
(3) Despite subsection (2), a supplier or producer may recommend a minimum resale price to the reseller of a good or service provided –
   (a) the supplier or producer makes it clear to the reseller that the recommendation is not binding; and
   (b) if the product has its price stated on it, the words ‘recommended price’ appear next to the stated price.”

Source: Consolidated Act\textsuperscript{110} 15-16

When a firm is accused of an alleged restrictive vertical practice, the onus is on the defendant to prove that the practice is not harmful to its competitors and to consumers (Competition Act\textsuperscript{111} 7). The following section discusses the case of how Toyota South Africa Motors (Pty) Ltd was found guilty of practicing minimum resale price maintenance (RPM).

ii.i.iii.i) Case study: Toyota South Africa Motors (Pty) Ltd\textsuperscript{112} practicing RPM\textsuperscript{113}

RPM is practiced when an entity that is in a vertical relationship with others in a market structure fixes the price at which the next entity in line should sell the product or service. The practitioner of RPM also sees to it that the next entity in line does not extend discount to the buyer of its product or service (Ntuli, 2004: 1). “It is clear that RPM can be detrimental to consumers as it prevents them from negotiating discounts on the price of products/services” (Ngwenya and Ngonyama, 2004: 2).

In 2004 the Commission found Toyota guilty of practicing RPM. This followed after the Commission launched a formal investigation to find the reason why the automobile industry charged such high prices for new vehicles (Ntuli, 2004: 1). Despite the continuing appreciation of the rand against other currencies since 2002, the prices of domestically manufactured motor vehicles and imported ones remained high. This gave the Commission reason to suspect that motor-vehicle manufacturers and dealers were conducting anti-competitive practices, possibly including the practice of collusion (Competition Commission, 2004b: 1-2).

The specific investigation into Toyota’s conduct was launched after a prospective buyer of a new Toyota Corolla had found “that a number of Toyota dealerships offer(ed) the same discounts on the new Toyota Corolla range. He also reported that salespersons advised him that failure to implement these discount structures would expose them to a stipulated fine\textsuperscript{114}.\textsuperscript{115} (Competition Commission, 2004b: 1-2). These allegations gave the

\begin{flushleft}
\textsuperscript{110} Undated.
\textsuperscript{111} Undated.
\textsuperscript{112} From here and onwards referred to as “Toyota”.
\textsuperscript{113} This case was never referred to the Tribunal. In such a case the report that is prepared by the Commission remains confidential information and may not be viewed by the public. This section makes extensive use of two sources, i.e. Competition Commission (2004b) and the media released by the Commission on 6 May 2004 (Ntuli, 2004).
\textsuperscript{114} Italics added.
\textsuperscript{115} This is clearly a violation of section 5(3)(a) of the Consolidated Act.
\end{flushleft}
Commission enough reason to launch an investigation to determine whether Toyota was guilty\(^{116}\) of practicing RPM.

During the Commission’s investigation they found a copy of the document that was sent to all Toyota dealers in which the resale price and discount terms were prescribed (Competition Commission, 2004b: 2). This document proved that Toyota was guilty of practicing RPM and the case could be referred to the Tribunal to take appropriate action. Before the case was referred, a consent agreement was reached between the Commission and Toyota, whereby Toyota agreed to pay an administrative fine of R12 million (Ntuli, 2004: 1). This case was not the first where a consent agreement\(^{117}\) was reached, but with this case the seriousness of the offence of practicing RPM\(^{118}\) is emphasized.

**ii.i.iv) M**erge regulation

**ii.i.iv.i) A n overview of merger regulation**

Section 12(1) of the Consolidated Act defines a merger as:

“(1) (a) For purposes of this Act, a merger occurs when one or more firms directly or indirectly acquire or establish direct or indirect control over the whole or part of the business of another firm.

(b) A merger contemplated in paragraph (a) may be achieved in any manner, including through –

(i) purchase or lease of the shares, an interest or assets or the other firm in question; or

(ii) amalgamation or other combination with the other firm in question.”

Source: Consolidated Act\(^{119}\): 24

The Commission does not need to be notified of all proposed mergers. The Consolidated Act distinguishes between three merger sizes\(^{120}\), i.e. small, intermediate and large mergers (Hartzenberg, 2002: 9). Small mergers are not required to be notified, unless it becomes apparent within six months after the merger that it caused a substantial decline in the level of competition in the particular market (Consolidated Act\(^{121}\): 27). Intermediate and large mergers require notification to the Commission (Competition Act\(^{122}\): 11).

The Commission follows four steps\(^{123}\) when processing a merger application:

1. The relevant product and geographic(al) markets are defined.
2. The market shares and market concentration ratios are calculated.

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\(^{116}\) In 2003 the Tribunal interpreted section 5(2) of the Consolidated Act. They decided that, in future, the Commission only has to prove that a firm practices RPM and no longer that the outcome of this practice is anti-competitive. If a firm is found guilty of practicing RPM, it can immediately be prosecuted (Competition Commission, 2003a: 1).

\(^{117}\) Consent agreements have also been reached in cases such as the Commission vs. the Board of Healthcare Funders, the South African Medical Association and the Hospital Association of South Africa and the Commission vs. Pretoria Association of Attorneys (Annual Report, 2004: 15-17).

\(^{118}\) Another example of a RPM case is Pee Dee Wholesalers vs. Federal Mogul Aftermarket (Annual Report, 2003: 27).

\(^{119}\) Undated.

\(^{120}\) The Minister of Trade and Industry and the Commission determine the thresholds of the different merger sizes [Consolidated Act (undated): 23].

\(^{121}\) Undated.

\(^{122}\) Undated.

\(^{123}\) These four steps show that the authorities use the SCP paradigm as a framework when merger applications are processed (Theron, 2001: 620).
3. The criteria set out in section 16(2)\textsuperscript{124} of the Act are used to evaluate the relevant market.
4. If it is concluded that a merger will result in a substantial lessening of competition, claimed efficiency, technological or other pro-competitive gains are assessed.”


The first step is the most vital one in investigating a proposed merger (Theron, 2001: 622). The competition authorities and the parties that are involved in a merger case often disagree on the definition of the relevant market. The parties often try to define the relevant market as broadly\textsuperscript{125} as possible to improve their chances of a successful merger application. The competition authorities have to find the most accurate definition of the relevant market, which in most cases, is more narrowly defined than the parties’ definition. After the relevant market has been defined, step two follows. The concentration ratios indicate how concentrated the relevant market is\textsuperscript{126}. After all the factors in steps three and four have been taken into consideration, public interest issues, as stated in section 12A(3)\textsuperscript{127} of the Act have to be taken into consideration.

When the Commission is unable to decide whether an application for a merger should be approved or rejected, it may refer the case to either the Tribunal or the Competition Appeal Court. The next section discusses the merger case of JD Group Limited’s application to merge with Ellerine Holdings Limited.

\textit{ii.i.iv.ii) Case study}\textsuperscript{128}: The proposed large merger between JD Group Limited\textsuperscript{129} and Ellerine Holdings Limited\textsuperscript{130}

JD’s application to merge with its competitor, Ellerine, was turned down by the Tribunal (Theron, 2001: 628). At the time the Commission received the merger application, JD and Ellerine were composed as follows:

\begin{itemize}
  \item \textsuperscript{124} Section 12A(2) in the Consolidated Act.
  \item \textsuperscript{125} A broad definition for the relevant market includes more competitors, thereby lowering concentration levels.
  \item \textsuperscript{126} Here the importance of a correctly defined relevant market is realized. When it is defined inaccurately, the concentration ratios will not reflect the true state of concentration in the market and the competition authorities may make wrong decisions about the merger application, to the detriment of consumers.
  \item \textsuperscript{127} “When determining whether a merger can or cannot be justified on public interest grounds, the Competition Commission or the Competition Tribunal must consider the effect that the merger will have on –
  \begin{itemize}
    \item a particular sector or region;
    \item employment;
    \item the ability of small businesses, or firms controlled or owned by historically disadvantaged persons, to become competitive; and
    \item the ability of national industries to compete in international markets” [Consolidated Act (undated): 26-27].
  \end{itemize}
  \item \textsuperscript{129} This section makes extensive use of the case report that was released by the Tribunal: “In the large merger between JD Group Limited and Ellerine Holdings Limited”, Case No: 78/ LM/ Jul00 (Competition Tribunal, 2000a).
  \item \textsuperscript{130} From here onwards referred to as “JD”.
  \item From here onwards referred to as “Ellerine”.
\end{itemize}
Table 4. The composition of JD

<table>
<thead>
<tr>
<th>Name of Store</th>
<th>Number of Stores</th>
<th>Age of Brand</th>
<th>Target Market</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bradlows</td>
<td>8/0/9*</td>
<td>Est. 1900</td>
<td>LSM 5-8</td>
</tr>
<tr>
<td>Russels</td>
<td>17/2/13</td>
<td>Est. 1943</td>
<td>LSM 4-7</td>
</tr>
<tr>
<td>Joshua Doore</td>
<td>12/5/33</td>
<td>Est. 1973</td>
<td>LSM 4-7</td>
</tr>
<tr>
<td>Giddy's Electrical Express</td>
<td>9/0/56</td>
<td>Est. 1958</td>
<td>LSM 4-7</td>
</tr>
<tr>
<td>Price 'n Pride</td>
<td>23/31/39**</td>
<td>Est. 1983</td>
<td>LSM 3-5</td>
</tr>
<tr>
<td>Score</td>
<td></td>
<td>Est. 1977</td>
<td>LSM 3-5</td>
</tr>
</tbody>
</table>

Source: Competition Tribunal (2000a: 3)
Total number of stores: 678(659)

Notes
- * These figures are based on the totals in the 1999 Annual Report. The figures in brackets are those given to the Commission in May 2000 and reflect the changes since 1999.
- ** The store figures for Score and Price 'n Pride are combined (Competition Tribunal, 2000a: 3)

Table 5. The composition of Ellerine

<table>
<thead>
<tr>
<th>Name of Store</th>
<th>Number of Stores</th>
<th>Age of Brand</th>
<th>Target Market</th>
</tr>
</thead>
<tbody>
<tr>
<td>FurnCity</td>
<td>5/0/50*</td>
<td>20 years</td>
<td>LSM 4-7</td>
</tr>
<tr>
<td>Ellerines</td>
<td>218/250*</td>
<td>50 years</td>
<td>LSM 3-5</td>
</tr>
<tr>
<td>Oxford</td>
<td>24/0/42</td>
<td>30 years</td>
<td>LSM 3-5</td>
</tr>
<tr>
<td>Town Talk</td>
<td>114/110*</td>
<td>20 years</td>
<td>LSM 3-5</td>
</tr>
<tr>
<td>Royal</td>
<td>24/240*</td>
<td>25 years</td>
<td>LSM 3-5</td>
</tr>
</tbody>
</table>

Source: Competition Tribunal (2000a: 6)
Total number of stores 489

Notes
- The figures supplied by the parties to the Commission in May 2000. The figures in brackets are taken from the 1999 Annual Report (Competition Tribunal, 2000a: 6).

When considering the markets targeted \(^{131}\) by JD and Ellerine, it becomes apparent that JD’s business is almost equally spread over lower-, middle- and high-income groups. Ellerine, on the other hand, predominantly targets lower-income groups.

There was a dispute between the parties and the Commission about the definition of the relevant product and geographical markets relevant for this merger application (Competition Tribunal, 2000a: 10). “The Commission holds that the relevant product market comprises furniture and appliance retailers serving the LSM 3-5 category and which provide credit to consumers” (Competition Tribunal, 2000a: 10). The parties had a broader definition and included discount furniture companies (Theron, 2001: 629). The Commission criticized the parties’ definition. “Approximately 99% of Ellerine’s sales are credit sales, and the equivalent figure for JD’s LSM 3-5 purchasers is only marginally lower” (Competition Tribunal, 2000a: 11). Therefore, it was appropriate to divide the market into a cash and credit market. Discount furniture and appliance companies’ sales are predominantly cash and not credit sales and therefore these companies should not be included in the definition of the relevant product market (Competition Tribunal, 2000a: 11, 14).

Next, the relevant geographical market had to be defined. Again the parties attempted to define the market as broadly as possible by including independent furniture companies in their definition (Competition Tribunal, 2000a: 20). “In its investigation, the Competition Commission established that the relevant geographic(al) market was local. Consumers generally only buy furniture in a 50 km to 80 km radius (from their homes). It was further found that small, independent furniture retailers could not be considered competitors of chain stores such as the JD group and Ellerine, as small stores tend to operate on a cash basis, rather than a hire purchase basis” (Competition Commission, 2000b: 15). Also, the parties argued that their products’ prices were determined at a national level, while credit conditions were formulated at group level, but regulated on the national level (Competition Tribunal, 2000a: 17). When prices are set at a national level, local competition is not a relevant factor and therefore regional independent companies cannot be included in the definition of the relevant geographical market.

\(^{131}\) As measured by the Living Standards Measurement (LSM). LSM groups range from LSM 1 to LSM 8. The former group has the lowest living standard (and is therefore the poorest) and the latter group has the highest living standard (and is therefore the most affluent) [Lamb et al., 2000: 42, 43].
Next, the concentration levels in the relevant market had to be determined by using two concentration measures, i.e., CR4 and HHI (Competition Tribunal, 2000a: 19). The parties supplied the competition authorities with calculated HHI figures, but due to the dispute regarding the definitions of the relevant market, these figures were not reliable. In the parties' calculations they included companies that do not form part of the relevant market. The following table summarizes the HHI figures that were presented by the parties:

Table 6. HHI based on total turnover of furniture and household goods

<table>
<thead>
<tr>
<th>Company</th>
<th>Turnover R/million</th>
<th>Market share</th>
<th>HHI pre-merger</th>
<th>HHI post-merger</th>
<th>Change in HHI</th>
</tr>
</thead>
<tbody>
<tr>
<td>JD Group</td>
<td>1.832</td>
<td>9.5</td>
<td>90.9</td>
<td>184.8</td>
<td></td>
</tr>
<tr>
<td>Game/ Dion</td>
<td>1.966</td>
<td>10.2</td>
<td>104.7</td>
<td>104.7</td>
<td></td>
</tr>
<tr>
<td>Profurn</td>
<td>1.764</td>
<td>8.9</td>
<td>78.7</td>
<td>78.7</td>
<td></td>
</tr>
<tr>
<td>Makro</td>
<td>1.450</td>
<td>7.5</td>
<td>57.0</td>
<td>57.0</td>
<td></td>
</tr>
<tr>
<td>Ellerines</td>
<td>780</td>
<td>4.1</td>
<td>16.5</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lewis</td>
<td>1.815</td>
<td>9.4</td>
<td>89.2</td>
<td>89.2</td>
<td></td>
</tr>
<tr>
<td>OK/Hyperama</td>
<td>798</td>
<td>4.2</td>
<td>17.3</td>
<td>17.3</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>19.213</td>
<td>100</td>
<td>532.7</td>
<td>610.1</td>
<td>77.4</td>
</tr>
</tbody>
</table>

Source: Competition Tribunal (2000a: 20)

The Commission recalculated the HHI figures using their definition of the relevant market and got the following results:

Table 7. HHI based on turnover of furniture and appliance shops directed at credit sales in LSM 3-5 (excluding Independents)

<table>
<thead>
<tr>
<th>Company</th>
<th>Turnover R/million</th>
<th>Market share</th>
<th>HHI pre-merger</th>
<th>HHI post-merger</th>
<th>Change in HHI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profurn</td>
<td>530</td>
<td>17.2</td>
<td>295.8</td>
<td>295.8</td>
<td></td>
</tr>
<tr>
<td>Relyant</td>
<td>712</td>
<td>23.1</td>
<td>553.6</td>
<td>553.6</td>
<td></td>
</tr>
<tr>
<td>Ellerines</td>
<td>600</td>
<td>18.2</td>
<td>484.0</td>
<td>1135.7</td>
<td></td>
</tr>
<tr>
<td>JD Group</td>
<td>382</td>
<td>11.7</td>
<td>128.9</td>
<td>128.9</td>
<td></td>
</tr>
<tr>
<td>OK/Hyperama</td>
<td>500</td>
<td>16.2</td>
<td>262.4</td>
<td>262.4</td>
<td></td>
</tr>
<tr>
<td>Lewis *</td>
<td>300</td>
<td>9.8</td>
<td>98.0</td>
<td>98.0</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>3084</td>
<td>100</td>
<td>1809</td>
<td>2324</td>
<td>515</td>
</tr>
</tbody>
</table>

Source: Competition Tribunal (2000a: 22)

* Note that, cognizant of Lewis' spread across the LSM segments, based on a cash sales turnover figure of approximately R1.3 billion, we have included a figure of R400 million for Lewis in our recalculated HHI. This is an estimated LSM 3-5 turnover figure for Lewis based upon a similar LSM 3-5 sales to total sales ratio for Profurn (Competition Tribunal, 2000a: 22).

The Commission found significantly higher values for the HHI, showing that concentration levels were not as low as were argued by the parties. To support this finding, the Commission calculated the CR4 and got the following results:

Table 8. CR4 of the relevant market

<table>
<thead>
<tr>
<th>Company</th>
<th>CR4</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profurn</td>
<td>19.5%</td>
</tr>
<tr>
<td>Relyant</td>
<td>26.2%</td>
</tr>
<tr>
<td>Ellerines</td>
<td>22.0%</td>
</tr>
<tr>
<td>JD Group</td>
<td>13.3%</td>
</tr>
<tr>
<td>Total</td>
<td>84%</td>
</tr>
</tbody>
</table>

Source: Competition Tribunal (2000a: 23)

JD and Ellerine would have formed a merged entity with a market share of 38.3% in the relevant market. The results of the concentration measures were only one of the factors the Commission and Tribunal took

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132 This was done by including data of both regional independent furniture and appliance firms and discount stores in the calculations of the HHI. As a result, the HHI figures did not display the true state of high concentration levels in the relevant market and reflected lower concentration levels.

133 Calculated by summing the market shares of the JD Group and Ellerine in Table 8.
into consideration. They also took account of the fact that Ellerine primarily targets lower income groups and almost all its sales are on credit (Competition Tribunal, 2000a: 25). If the merger was allowed, the new entity would have served almost all of the LSM groups and the size of its market share would probably have made it a dominant player in the relevant market.

The Commission also took cognisance of public interest issues. The parties argued that allowing the merger to take place would create an entity with the ability to offer extended financial services to the public and “bring the banking to the unbanked” (Competition Tribunal, 2000a: 31). The Commission was not convinced by this argument, as the new entity would only provide credit services and not savings facilities to its customers. The proposed merger did not carry a risk of employment losses and none of the other public interest issues in the competition legislation were relevant in this case (Competition Tribunal, 2000a: 32).

“The Commission strongly felt the proposed merger would primarily affect low-income consumers who buy furniture on credit. The merger would significantly affect consumer choice, reduce competition in an already concentrated market, and create opportunity for possible future abuses of market power, primarily with respect to raising prices” (Annual Report, 2001: 31). The Tribunal agreed and rejected the merger application.

4. CONCLUSION

This paper discussed the rationale for competition policy from a South African perspective. Section 2 explained the theoretical rationale for competition policy. The overriding goal of competition policy is to remedy market failures and to provide a framework for regulating mergers. Market failures occur due to the absence of perfectly competitive markets in reality and the prevalence of imperfectly competitive market structures, such as monopoly and oligopoly. These structures pose a risk to competition in markets, as they may encourage anti-competitive conduct by firms, which impacts consumers in a negative way.

In South Africa’s case the country’s political history provides an additional rationale for competition policy. European and British settlement caused the indigenous population to be deprived of their land and the discoveries of gold and diamonds resulted in the development of conglomerates in the economy. These two events caused ownership to become concentrated in the hands of the white population at the expense of other racial groups. The economy became highly concentrated, especially in the manufacturing sector and, although South Africa has had comprehensive competition legislation since 1955, this failed to lower concentration levels effectively.

Since South Africa has become a democracy in 1994, several changes have been made to policies and in 1999 new competition legislation became effective. Eight objectives are stated in the preamble of the Consolidated Act - some of them need no introduction as they have traditionally formed part of competition legislation, but others generally fall outside the jurisdiction of competition legislation. The latter have specifically been included to promote the country’s competitiveness in the ever-globalizing world and to address the inequalities between the white population and other racial groups. The current legislation has only been effective for seven years and, as was discussed in section 3, the Act’s objectives cannot be achieved within a short period of time. However, from the research it becomes apparent that, although the Competition Authorities are only in their infant shoes, they have a clear understanding of what is expected from them and they aim to apply the Act actively and in a proper way.

The high frequency of cases on alleged restrictive business practices that are conducted by firms may suggest one of two things. First of all, it may imply that the business sector is not yet fully informed about the contents of the Consolidated Act and therefore do not realize that there are practices that are prohibited by the Act. Alternatively, it may show that businesses do not yet respect the Act and the Competition Authorities and are not willing to co-operate with them.

Finally, if the Competition Authorities can continue with their serious approach in applying the Consolidated Act and can convince the business sector to abide by the contents of the Act, then it may be possible to reform the uncompetitive, highly concentrated South African economy into one where all South Africans have equal opportunity to participate and compete in the formal economy. Achieving this could contribute towards economic growth and development that benefits all South Africans.
### APPENDIX A. CONCENTRATION INDICES AND RATIOS – THE SOUTH AFRICAN MANUFACTURING FIRMS

Calculated using gross output of firms

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Butter and cheese *</td>
<td>CR4</td>
<td>0.5329 (52)</td>
<td>0.6049 (52)</td>
<td>0.6133 (50)</td>
<td>0.6139 (50)</td>
<td>0.9104 (48)</td>
<td>0.8853 (41)</td>
</tr>
<tr>
<td></td>
<td>CR10</td>
<td>0.7981</td>
<td>0.8607</td>
<td>0.9077</td>
<td>0.9022</td>
<td>0.9970</td>
<td>0.9911</td>
</tr>
<tr>
<td></td>
<td>HHI</td>
<td>0.1060</td>
<td>0.1636</td>
<td>0.2395</td>
<td>0.2271</td>
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<td>0.2974 (459)</td>
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Notes
* Subgroup
Those groups without an asterisks (*) represent major groups.
The number of firms is in parentheses.

\(^\text{c}\) Herfindahl Hirschmann Index
\(^\text{o}\) Rosenbluth Index
REFERENCES

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DU PLESSIS, S.W.F., 1999. Die Ontwikkeling van die Suid-Afrikaanse Nywerheidsektor en 'n Kritiese Valuering van die Huidige Beleid. Thesis submitted for the degree of Masters in Economics and Business Sciences (Economics) at the University of Stellenbosch, South Africa.


