



**DIRECTORATE FOR FINANCIAL, FISCAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

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ROUNDTABLE DISCUSSION ON PREDATORY FORECLOSURE

-- Note by Turkey --

This note is submitted by the Turkish Delegation to the Competition Committee FOR DISCUSSION at its forthcoming meeting (14-15 October 2004).

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PREDATORY FORECLOSURE

WITHIN THE TURKISH COMPETITION LEGISLATION

I. General Framework:

1. Due to certain motives, undertakings may tend to apply predatory prices. Regardless of whether legal or illegal, in order to be reasonable, predatory pricing requires presence of certain conditions. First of all, as it aims at driving the rivals out of the market and augmenting the prices to a level well above the competitive price, access to the market must be difficult or must require a significant cost. Otherwise, the enterprise would bear losses stemming from the practise but would never achieve an occasion to increase its prices because of the consecutive newcomers. Therefore, predatory pricing is supposed to be unreasonable in cases the importation of the relevant product or access to the market being relatively easier. "Beer" may be a typical example for the product markets, in which enterprises may tend to drive competitors out of the market, as importation of a relatively cheap product will increase its price significantly and entrance to the market and access to the final consumer require a high amount of investment. Daily newspaper market, as well, may constitute another typical example. Importation of a daily newspaper is almost unreasonable because of the "linguistic barrier" as well as the economic life of the relevant product.

2. *Interaction between International Trade and Predatory Pricing:* In cases where international trade of the relevant product is possible and feasible, theoretically, predatory pricing can not exist. Competitors operating in the trade partners can wait till the relevant enterprise gives an end to the predatory pricing and then access to the market. Domestic competitors, too, can survive as they can supply their products in foreign commerce.

3. *Collective predatory pricing; price fixing, or concerted practise:* Even though cartels are usually established to keep the prices artificially above the competitive prices, the parties to a cartel may also tend to act together to another end, namely to drive a particular competitor out of the market. In that kind of behaviour, price-fixing is concerned, rather than a predatory pricing. When the same behaviour is valid but a price-fixing agreement does not exist, the practise may be called "concerted practise". Turkish Competition Authority handled a similar case. Leading liquid-gas marketing enterprises have engaged in a price fixing agreement against a local liquid gas company. As the scope and the marketing capacity of the local enterprise were very limited, the below-cost supply agreement was valid in one particular city. The significant price difference between neighbouring cities constituted an evident for the price-fixing agreement.

4. *On Nature of the Predatory Pricing:* To our opinion, two abuses, in exact names "predatory pricing" and "use of the economic power acquired at a certain market in order to possess a dominant position at another one" must be assessed separately. We firmly believe that the competition agencies must attach further importance to latter type of behaviour, as the enterprise practising that type of an abuse, finances its short-term losses more easily and consequently the consumers indirectly pay for the illegal practise.

5. The situation is much more complicated when services sector -in general-; the transportation sector -in particular- is concerned. Transportation sector is the typical example for the operations where the fixed costs occupy a significant portion of the total costs. Enterprise A can augment its prices to the same level as its costs but then the loss may get higher as the demand will be less. Hence, the enterprise A can claim that the low price is justified by this market structure. Another problematic sector is newspaper market. Below-cost pricing, in this particular sector, can be justified as it increases the commercial advertising revenue.

II. Experience in Turkey:

6. Article 6 of Turkish Competition Act bans abuse of dominant position. Paragraph (a) of the above-mentioned Article cites to "preventing, directly or indirectly, other enterprises in its area of commercial activities or practices, which aim to impede the activities of the competitors in the market". Therefore, the undertakings that hold a dominance in the relevant market can be accused of predatory pricing. The case law is similar to that of the European Community. The prices have to be below the average variable cost to be identified as "predatory".

7. ***TDI Case:*** One of the most interesting cases that the Turkish Competition Authority has dealt with was in the maritime transportation sector. In this particular case, state-owned company **Maritime Enterprises of Turkey** (TDI) was accused for charging excessive prices at a certain domestic line, where it is the monopoly, and fixing the prices significantly below the prices at another domestic line, where competitors exist. The facts that the Competition Authority examined in this particular case:

8. *Does TDI possess a dominant position?* Article 6 of the Competition Act identifies and bans the abuse of dominant position and paragraph (a) of the relevant Article involves the predatory pricing practise. "Use of the economic power acquired at a certain market in order to possess a dominant position at another one", is, too, mentioned within the Article 6 (paragraph (d)). Therefore, the first examination is assessing whether the accused company or companies hold a dominant position.

9. *How can TDI finance its losses?* Operating at another line as a natural monopoly, TDI can easily finance its losses at the relevant geographical market by fixing the prices higher than competitive level at the former. Instead of another geographical market (a line in this case), the company concerned might have a dominant or monopoly position at any other product market. A third way to finance the losses stemming from predatory pricing may be called as "loss leading profit". The Office of Fair Trading of the United Kingdom made some researches in the field and concluded that this behaviour is common, especially in the retailing sector. The remedies that a competition agency might propose vary depending upon the way of financment of the loss. If the relevant enterprise holds a monopoly position at any other geographic or product market, then this market can also be examined. In cases where the enterprise holds a natural monopoly position, the competition agency may request the firm to distinguish the accounts of two operations. So called "Structural Separation" Remedy, however, is not requested by Turkish competition Authority so far.

10. *Does TDI have sufficient capacity to meet the aggregate demand?* This is, to our view, an important criterion, as the price policy could not be identified as "predatory" otherwise. As long as the supply capacity of an enterprise remains less than the aggregate demand, the possible consequence of the practise is a reduction at the enterprise's revenues. The competitors, under this situation, survive thanks to the gap between the aggregate demand and the supply capacity of the predator enterprise. Therefore, a below-cost pricing policy of an enterprise, which can not cover the aggregate demand, will not easily be identified as a "predatory pricing".

11. *At which point is the price level located?* In some cases, the prices may be fixed below the average total costs but above the average variable costs. As in the EU, in Turkey, too, this price policy is not assessed under the title of "predatory pricing". In this particular case, the reporters needed to deal with another question. Prices of the TDI might be below its average variable cost, but this might be stemming from the fact that the cost structure of TDI is quite different than its competitors. Relatively older ferries of TDI are claimed to consume more oil besides the fact that the workers of TDI are evidently paid higher salaries than that working at rival private companies. This phenomenon will be discussed at an imaginary case.

12. There still exist certain questions about predatory pricing. Is a case where a dominant firm fixes its prices below its operation costs necessarily a predatory pricing?

COST-----PRICE (Enterprise A)		COST-----PRICE (Enterprise B)	
100	80	80	75

At this imaginary case, a dominant enterprise (A) fixes its price below the cost and forces its competitor to do the same. However, A can claim that this practise is a normal conduct in the flow of trade as it has to compete despite its relatively higher costs.

13. *Duration of the practise:* Launching a new product in the market, promoting the reputation or market share of a particular product may require a special pricing policy, hence may justify a below-cost pricing. However, in order the justification to be acceptable; the practise must be in conformity with the justifying aim. In cases where the below-cost pricing lasts for longer than 6 months, than the suspect of predatory pricing overweighs the justification.

14. *Does TDI claim a reasonable justification?* Given that the price policy is one of the most important decisions that the enterprises are supposed to determine by themselves, the interruption of a competition agency should be possible in very limited cases. The claims of the TDI to justify the price policy are assessed carefully.

15. **The Coca-Cola Company Case:** A very comprehensive case, dealt with by the TCA is the Coca-Cola Company Case. Coca-Cola is accused in this particular case of practising predatory pricing at carbonated soft beverage market. Coca-Cola and Pepsi hold a collective dominant position in non-alcoholic beverage market in Turkey in general, the dominance being more characteristic when cola drinks are concerned. Both companies also hold brands in the carbonated soft beverage market within their economic unities; however, their positions in this latter market is relatively weaker when compared to their market positions in the cola drinks market. Sensun, the brand held by the Coca-Cola Company, fixes relatively lower prices for its products. Within the Prosecution Report, besides the above-mentioned analyses (how do accused firm(s) finance the looses; whether the prices are below the average variable costs; if affirmative, the duration, dominant position test) exists also another analyse in regards with the brand reputation and consumer fidelity.

16. Within the analyses, the "short term average variable cost" is identified as the composition of the inputs, package, variable production and variable marketing and distribution costs items; "short term average total cost", as variable average cost plus fixed costs fixed marketing and distribution costs, general administrative costs and finance items. The reporters detected that the price of Sensun products has remained below the short-term average total cost during 33 months within last 36 months; but remained below the average variable cost during one month, only. The conclusion in this regard was that "the outlet sales prices remained well below the average total cost and close to the average variable total cost.

17. The Prosecution Report involved certain scenarios, assuming that the alleged predatory price practitioner has fixed the prices below costs; a) in order to drive the competitors out of the market; b) to acquire the local small sized rival companies and become a monopoly; c) because of its relatively weaker situation in the relevant product market. The reporters of the case have suggested the Competition Board to request the Coca-Cola Company to present the Board periodically its cost/revenue analyses, however the Competition Board rejected this and did not request the Company to do so.

18. The Competition Board has concluded that the above the average variable cost prices are not practised with an intention of driving the rivals out of market. The Competition Board gives this Decision on 23 January 2003 and the Prosecution Report is publicised on the Official Gazette.

Conclusion

19. Predatory foreclosure covers a larger area than predatory pricing does. Excess capacity can serve the leading example among predatory foreclosure behaviour. Claims in this field are assessed case by case. Turkish Competition Case Law involves more cases -in number- relevant with predatory pricing. First step is usually identifying the commercial behaviour exactly. The practise may be a predatory pricing or abusing the advantages of the dominance in a certain market in order to gain a competitive advantage in another (or some others), according to the sources for financing the losses stemming from the predatory pricing. The action may be executed by one single undertaking holding a dominant position or by a few of them in case of a collective dominance.