Competition & Contestable Markets for Economic Diversification & Flexibility

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Agenda

- Anti-trust & the macroeconomic environment
- Competition Law Frameworks
- Role of SoEs in the MENA/ GCC region
- Governance of SoEs and GREs
- Competition & economic diversification
- Key takeaways

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What is Antitrust/Competition Law?

- **Antitrust or competition law or policy** : economic policy, laws and regulations dealing with monopoly and monopolistic practices and addresses issues arising from the behaviour of firms operating under different market structure conditions and the effect this has on economic performance
- Most antitrust or competition laws have provisions dealing with market structure such as mergers, acquisitions, monopoly, dominant market position and concentration, as well as behaviour, such as collusion, price fixing, and predatory pricing
- Rapid proliferation of competition regimes across the globe is driven by trade liberalisation, often necessitated by a need for legislation as part of a country's commitment to multilateral (WTO) or FTAs, technological change and the need to protect the rights of businesses and consumers at large.

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Well designed pro-competition policies lead to higher productivity growth, innovation & economic growth

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Competition Policies

- Competition leads to an **improvement in allocative efficiency** by allowing more efficient firms to enter and gain market share, at the expense of less efficient firms (the so called *between-firms effect*)
- Competition **improves productive efficiency** of firms (the *within-firms effects*), as firms facing competition seem to be better managed
- Competition can improve **social as well as economic outcomes**: e.g. growing evidence that competition in the provision of healthcare and education can improve quality outcomes
- Promoting competition tends to **increase innovation**. Firms facing competitive rivals innovate more than monopolies
- More competitive markets result in higher productivity growth. Enforcement of competition laws and removal of regulations hindering competition result in better **economic growth prospects**

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Contestable Markets

- A contestable market is one with low/zero entry and exit costs i.e. there are no barriers to entry and exit
- For a market to be perfectly contestable, relevant industry technology would be readily available to potential entrants
- 3 key conditions for market contestability
  - Ability / legal right to use the best available technology
  - Legal freedom to enter a market
  - Relative absence of sunk costs / exit costs

⇒ natural monopolies are the least contestable markets

- Note: opening up a market to potential entrants may be sufficient to encourage efficiency, and deter anti-competitive behaviour (e.g. of broadband operators allowed to use Telecom infrastructure)

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Contestability and Regulation

Making markets more contestable

- **De-regulation**: i.e. reducing barriers to entry to liberalise a market
- **Tougher competition laws** acting against predatory behaviour by existing firms / tough rules against cartels
- **Changing nature of technology:** has brought down entry costs and made prices more transparent for consumers (e.g. Internet retailing)
- **New business models** that challenge established players e.g. Low cost airlines

Barriers to contestability

- **Raising rivals costs**
  - Vertical integration giving control over the supply-chain
  - Import tariffs / protectionism
- **Reducing rival's revenues**
  - Bundling – offering some extra products for free
  - Selling spare capacity at low prices
- **Cross-subsidisation**
  - Using profits from one market to cut prices in another

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Competition laws across the globe

- History of modern competition laws begins with **Canada's Competition Act** of 1889. The law prohibits offences such as price fixing, bid rigging, resale price maintenance, price discrimination and predatory pricing.
- **US Sherman Act of 1890** formed the bedrock of competition law and prohibited agreements among competitors that unreasonably restrained competition and monopolised trade.
- **EU competition law** is based on articles 101 and 102 of the Treaty on the Functioning of the European Union. Article 101 prohibits agreements, decisions and concerted practices that prevent, restrict or distort competition, whereas article 102 prohibits abuse of dominance.
- Competition laws typically set-up **competition agencies/authorities**

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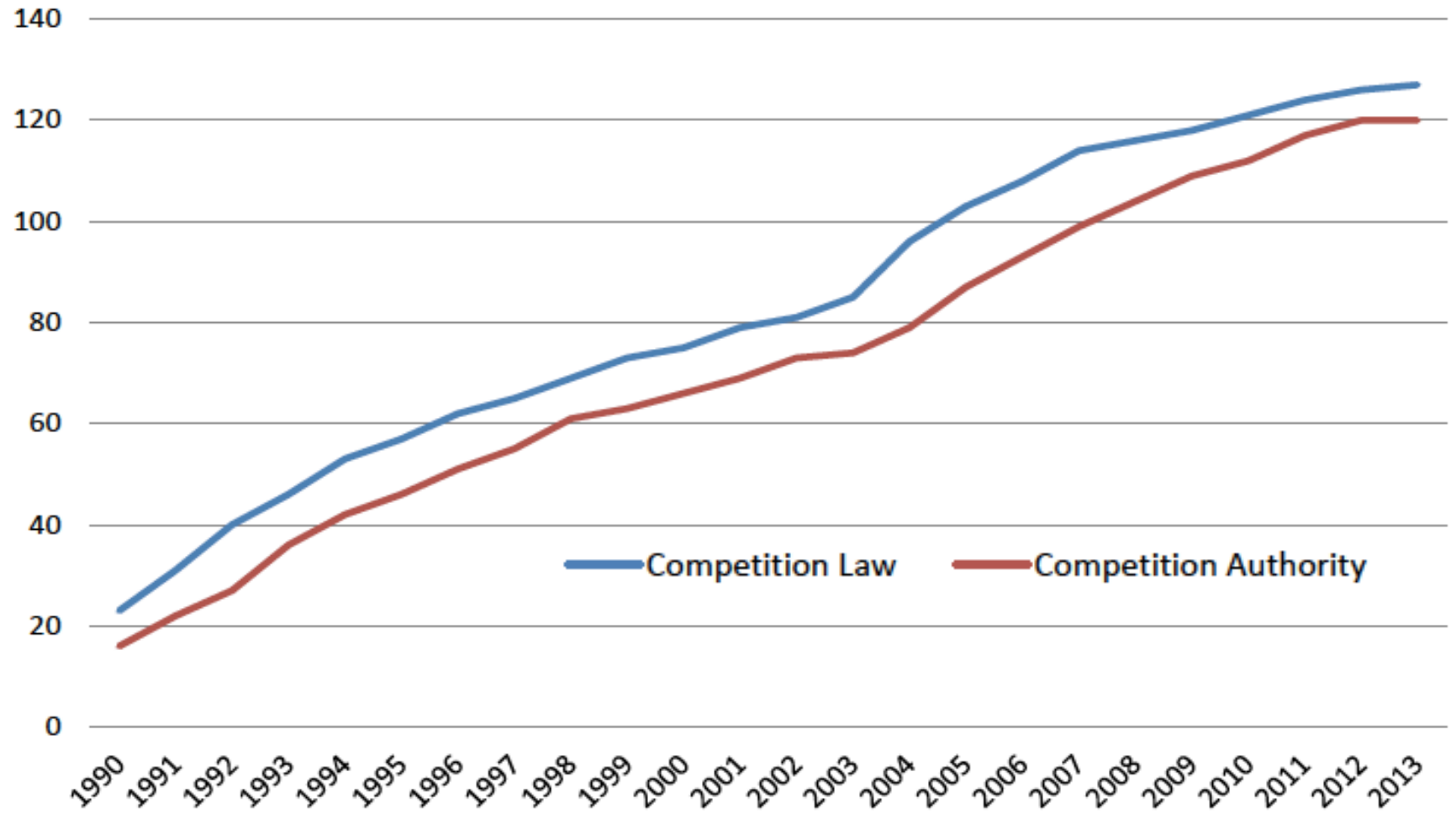
Number of jurisdictions with Competition Law & Competition Authorities increased 500% between 1990 and 2013



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Competition laws in MENA/GCC

- **Jordan is first Arab country to have adopted competition legislation** in 2002. In others such as Algeria, Saudi Arabia, and UAE, competition legislation and authorities were introduced more recently as a result of WTO
- Even where competition is regulated**, not all SOEs are included in the remit of the relevant laws** and sometimes are explicitly excluded; e.g. in Egypt, public utilities managed by the State are not subject to the Competition Law, while private utilities may apply to the Egyptian Competition Authority for total or a partial exemption
- **Difficulty of enforcing competition laws on SOEs.** Little political/ economic incentive to investigate anti-competitive practices of government enterprises; limited experience of competition authorities in investigating SOEs; delineation of oversight authority between competition authorities & sectoral regulators has not always been made clear

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Competition Laws in KSA & UAE

- Key focal points of KSA & UAE Competition laws : Anti-competitive agreements; abuse of dominant positions; corporate transactions such as mergers that can result in a market becoming less competitive

Key features of both UAE and KSA Competition Laws include:

- Clear aim of combatting monopolistic practices
- No absolute prohibition on price fixing whereby even dominant businesses have certain grounds which permit them to fix prices
- De minimis thresholds of market share, below which the prohibitions on restrictive agreements will not apply (typically 40% of transactions)
- Widespread exemptions: UAE excludes entire sectors as well as SMEs; both laws exclude public and wholly owned SOEs
- Agencies and Distributorships can be exempted from competition law
- Merger control procedures
- Specify financial and operational sanctions for breaches of competition law

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Role of SoEs in the MENA/GCC

- Vision of the SoEs changed over time from instruments of nation-building and infant industries protection to one of a source of competitiveness
- SOEs account for 20-50% of GDP across the Gulf region. In KSA state's stake in SOEs amounts to 19.8% of GDP; in UAE 21.8% and in Qatar, 23.1%.
- But degree of state participation in MENA economies remains covered in secrecy: lack of data & statistics, no consolidated reporting
- Majority of SoEs in MENA remain "elephants among gazelles": inefficient, often characterized by lower productivity, a drain on fiscal resources & facing difficulty competing with private sector incumbents
- Why do SOEs under-perform? State ownership: lack of accountability, distorted incentive structures, lack of innovation and risk taking incentives ; multiple missions & conflicting objectives; fragmented oversight

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Role of SoEs in the MENA/GCC II

- But there are “islands of excellence”: companies, which demonstrate a level of economic performance & sophistication in governance and strategy (e.g. Emirates, Etihad, Qatar Airways). This is sometimes a result of the special privileges & exemptions from regulations
- There have been targeted privatisations (Egypt, Tunisia, Morocco) & SoE downsizing programs in the recent past
- Sectors such as banking and telecoms have been successfully liberalised
- Growing role of SWFs as owners of SOEs can improve performance: e.g. ownership rights in a number of SOEs were transferred from the Bahraini government to Mumtalakat, especially when its expertise as an equity investor was considered useful to facilitate IPOs of SOEs

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“Strategic” SOEs in GCC I

	Telecom	Finance	Electricity	Oil and gas	Transport	Construction Real Estate	Infrastructure	Other
Bahrain	Bahrain Telecommunications Company	National Bank of Bahrain Al Ahli United Bank Securities and Investment Company		Bapco Banagas Bafco Bahrain National Gas Expansion Company Bahrain Lube Base Oil Company Gulf Petrochemical Industry Company Tatweer Petroleum				Bahrain Tourism Company Aluminium Bahrain
Kuwait	Mobile Telecommunications Company (Zain) National Mobile Telecommunications Company	Kuwait Finance House Gulf Bank Al Ahli bank of Kuwait		Kuwait Petroleum Al Soor Fuel Marketing Company	Kuwait Airlines Livestock Transport and Trading Company			Kuwait Cement Company
Oman	Oman Telecommunication Company	Bank Dhofar National Bank of Oman Bank Sohar	Electricity Holding Company	Oman Petroleum Development Oman Oil Company Oman Gas Company Oman LNG	Oman Air		Oman Post	Raysut Cement Company Oman Cement Company ORPIC
Qatar	Qatar Telecom	Qatar National Bank Masraf Al Rayan Al Khalij Commercial Bank	Qatar Electricity & Water Company	Qatar Petroleum Qatargas	Qatar Airways	Barwa Real Estate Company	Q-Post	Gulf International Services Industries Qatar

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“Strategic” SOEs in GCC II

	Telecom	Finance	Electricity	Oil and gas	Transport	Construction Real Estate	Infrastructure	Other
Saudi Arabia	Saudi Telecom	Samba Financial Group Riyadh Bank Al Rajhi Bank Alinma Bank Al Khalij Commercial Bank Saudi Investment Bank Banque Saudi Francis SABB The Company for Cooperative Insurance	Saudi Electricity Company	Yanbu National Petrochemical Company Saudi Kayan Petrochemical Company National Gas and Industrialisation Company Saudi International Petrochemical Company National Petrochemical Company Rabigh Refining and Petrochemical Company	Saudi Public Transport Company The National Shipping Company of Saudi Arabia Saudi Railways Organization	Saudi Real Estate company	Saudi Post	
UAE	EITC Etisalat	National Bank of Abu Dhabi Abu Dhabi Commercial Bank Union National Bank Dubai Islamic Bank Commercial Bank of Dubai Union National Bank Abu Dhabi National Insurance Company Emirates NBD Tamweel	Dubai Electricity and Water Authority Abu Dhabi Water and Electricity Company Sharjah Electricity and Water Authority	ADNOC Emirates National Oil Company Emarat TAQA	Emirates Etihad Dubai Ports Roads and Transport Authority Sharjah Transport	Nakheel Emaar Properties Arkan Building Materials Company National Corporation for Tourism and Hotels Dubai Public Transport Agency	Emirates Post	Dubai Holding Abu Dhabi Ship Building Company Dubal

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Some insights from the Global Competitiveness Index for MENA (WEF)

- Despite recent privatization efforts, most national economies remain state-dominated (particularly in extractive industries) & not sufficiently diversified
- **Competition remains constrained** throughout the region: the level of domestic competition and openness to foreign trade and investment remains below OECD levels for most countries.
- **Efficiency and productivity could be improved** by continued liberalisation, privatization, reducing regulatory barriers to entry for domestic companies, and making business environments more welcoming for FDI and more conducive to the growth of SMEs

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Value & ranking of select MENA countries in Global Competitiveness Index (competition sub-indicators)

	Intensity of local competition, 1-7 (best)	Extent of market dominance, 1-7 (best)	Effectiveness of anti-monopoly policy, 1-7 (best)	Prevalence of trade barriers, 1-7 (best)	Prevalence of foreign ownership, 1-7 (best)	Burden of customs procedures, 1-7 (best)	A. Competition	B. Quality of demand conditions	6th pillar: Goods market efficiency
Bahrain	5.21	4.20	4.59	5.03	5.46	5.16	5.26	4.44	4.98
Egypt	4.24	3.33	3.58	4.02	3.36	3.80	4.02	3.82	3.95
Jordan	5.40	4.29	4.24	4.07	4.43	4.79	4.82	4.21	4.62
Kuwait	5.21	3.39	3.06	4.16	2.68	3.44	4.28	4.03	4.20
Morocco	5.12	3.74	3.49	3.60	4.76	4.26	4.63	3.88	4.38
Oman	4.60	3.19	3.72	4.65	4.15	4.53	4.80	3.86	4.48
Qatar	5.74	5.08	5.04	5.17	4.46	5.18	5.48	5.28	5.41
Saudi Arabia	5.40	4.25	4.26	4.57	3.69	4.62	4.79	4.33	4.64
UAE	5.90	5.10	4.91	5.47	5.66	6.05	5.79	5.26	5.61
MENA	**4.97**	**3.80**	**3.81**	**4.31**	**3.95**	**4.14**	**4.58**	**4.12**	**4.43**

	Intensity of local competition,	Extent of market dominance,	Effectiveness of anti-monopoly policy	Prevalence of trade barriers, 1-7 (best)	Prevalence of foreign ownership	Burden of customs procedures	A. Competition	B. Quality of demand conditions	6th pillar: Goods market efficiency
Bahrain	61	33	25	12	18	19	15	34	22
Egypt	127	103	78	100	125	80	121	82	112
Jordan	38	26	33	98	76	34	37	51	43
Kuwait	59	95	115	92	136	106	94	65	85
Morocco	70	64	84	124	53	60	54	76	64
Oman	112	110	61	38	96	45	41	78	51
Qatar	17	11	15	9	71	17	8	5	7
Saudi Arabia	37	29	32	49	115	38	43	40	41
UAE	9	10	19	3	10	4	3	6	3

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OECD Guidelines on Corporate Governance of SOEs: Main Principles

- **Rules-based environment. SOEs should be subject to the same rules** and regulations as other enterprises. They should compete on a level playing field with private enterprises and not distort competition.
- **Reinforcing the ownership function.** The state administration should exercise SOE ownership on a whole-of-government basis. The **state ownership function should be separate from the regulatory function** to avoid conflicts of interest.
- **Equitable treatment of shareholders.** The state should not have any undue advantages over other investors in SOEs.
- **Transparency and disclosure.** SOEs' objectives and performance should be disclosed and reviewed.
- **Stakeholder relationship.** SOEs and their owners should treat employees, creditors and affected communities fairly and equitably.
- **Boards of directors.** The boards are the SOEs' highest decision-making bodies. They should exercise their powers free of political interference.

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OECD CG Guidelines for SOEs, II

- **Develop an ownership policy.** Governments should issue an ownership policy defining objectives
- **Overall rationales for state ownership**
- **Enterprise-specific rationales**
- **Legal and regulatory framework:** should ensure a "level playing field" with private sector
- **Market consistent financing.**
- **Non-discriminatory public procurement of SOEs**
- **Eliminate political donations** by SOEs

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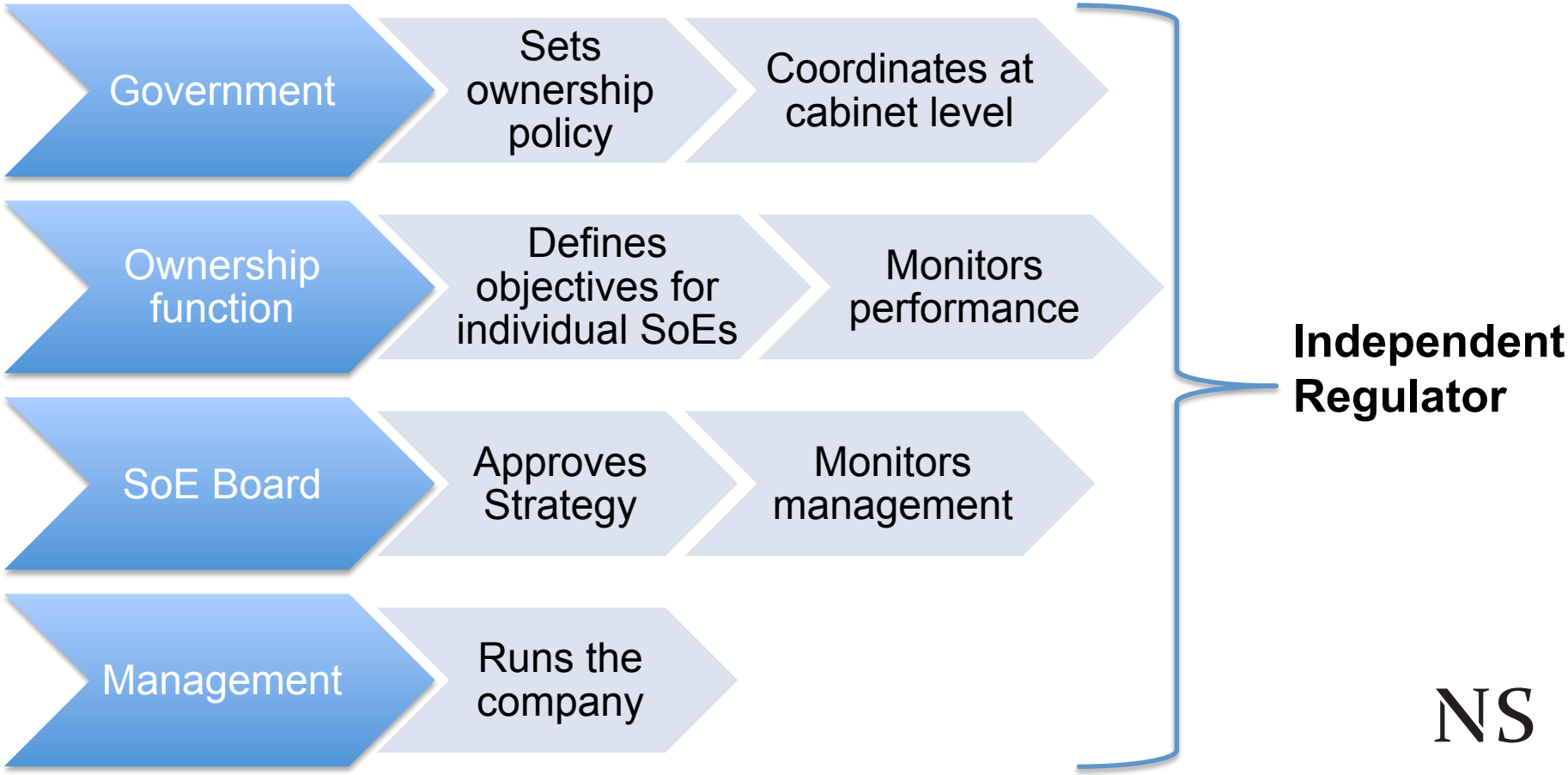
OECD Guidelines on Corporate Governance of SOEs

- **Ownership of SOEs is separated from policy making & regulation**
- Each ownership decision should be taken at the appropriate level



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Competition Laws & Transforming SoEs

- **Competition laws alone are not sufficient** in ensuring a level playing field for SOEs and private enterprises
- **Attaining competitive neutrality is an important policy objective** to improve economic efficiency and fairness of competition between SOEs and private companies, but also for future development of private sector
- **Competitive neutrality** can be understood as a regulatory framework (i) within which public & private enterprises face the same set of rules and (ii) where no contact with state brings competitive advantage to any market participant
- SOEs should be subject to **appropriate corporate governance frameworks** in order to maximise their effectiveness and reduce potential market distortions resulting from their privileged position.

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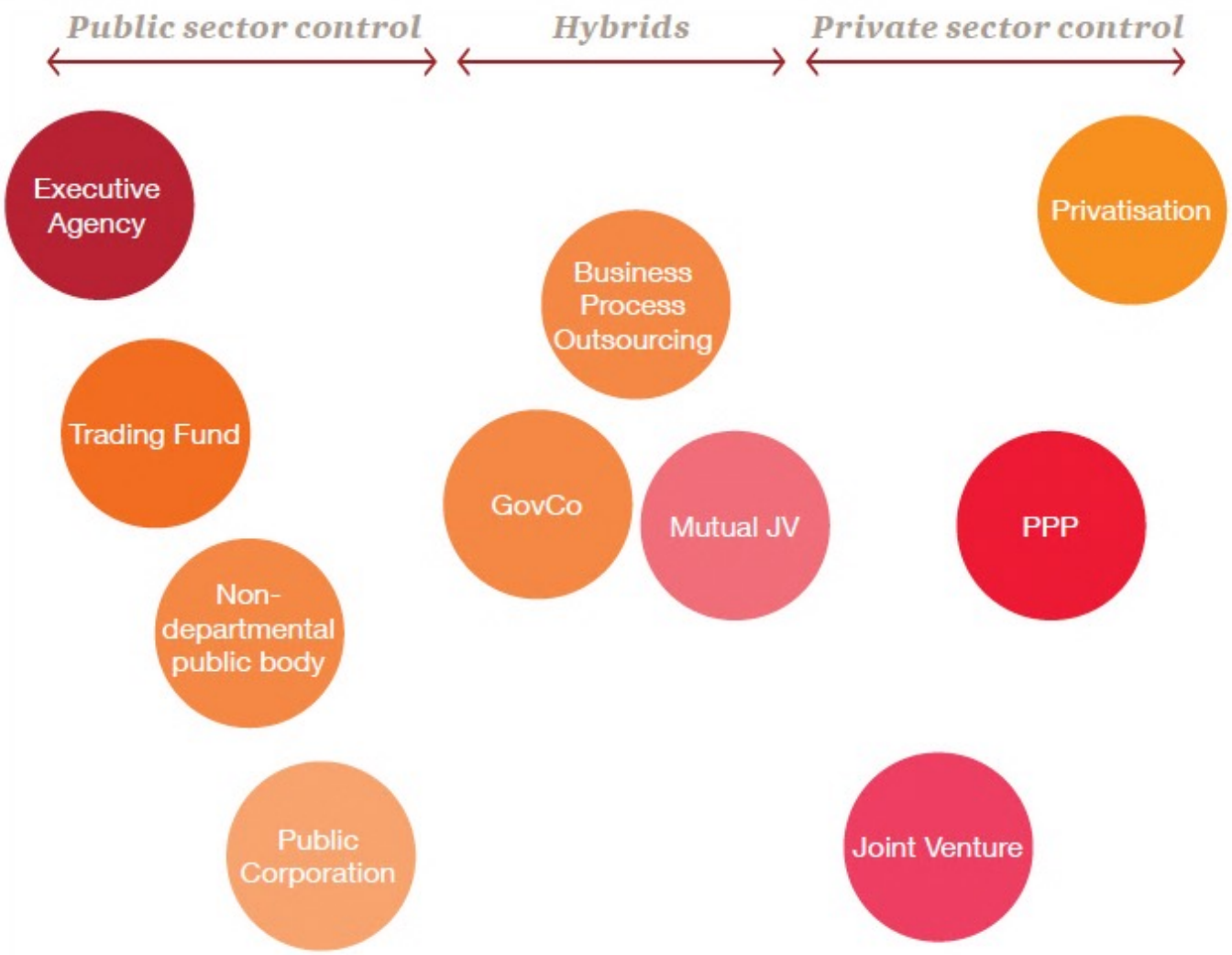
Economic diversification policy should lead to ‘corporatisation’ of SOEs, privatisation, PPP…

- Models which governments might choose on the path to private ownership
- Sequence reforms
- Privatisation in Saudi, Kuwait, Oman
- PPP: Saudi ‘New Cities’, Expo 2020, Qatar World Cup



Potential effects of privatisation on GCC (excluding oil assets & companies)

SIZE OF GCC PRIVATISATION PROGRAMMES	POTENTIAL BENEFITS OVER 15 YEARS ACROSS GCC	
SALE OF 25% OF GOVERNMENT ASSETS	1	Create value in GDP terms of approx. US$100 billion
	2	Shift 300,000 public sector jobs of GCC nationals to the private sector
	3	Permanently reduce GCC government budgets by 5%

Source: "Creating a Sustainable Privatisation Programme in the GCC", Oliver Wyman 2016. Notes: These effects exclude the privatisation of state oil companies and oil assets. If included, the benefits would be far greater

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Key Takeaways

- Economic diversification, flexibility & transformation depends on an active, dynamic and empowered private sector
- GCC market structure & role of SOEs need to be transformed to allow competition & contestable markets
- Consider sequencing of reforms in terms of corporatisation, splitting up of SOEs and their subsequent privatisation in order to ensure a competitive climate & neutrality
- Develop and adopt CG standards for SOEs
- Separate policy-making from regulation by establishing independent regulators
- Competition frameworks need to be buttressed by PPP, privatisation

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Thank you

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