South Africa’s Pioneer Settlement: an innovative way to remedy competition law violations in developing countries?

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Introduction

- Persistence of coordinated outcomes
  - Extensive regulation
  - Explicit cartels
  - Conduct designed to exclude entrants in bread
  - Prices historically sticky downwards, underpinned by the information exchange
- In November 2010 the Competition Tribunal confirmed the consent and settlement between Commission and Pioneer Foods (one of the cartelists)
  - to restore competition in the relevant markets
  - punish Pioneer
  - compensate victims
  - deter future misconduct by Pioneer and other firms

Background – Pioneer's conduct and theories of harm

- Bread cartel
  - Involving Pioneer, Premier , Foodcorp and Tiger brands
  - Premier and Tiger brands applied for leniency in terms of leniency policy
  - In February 2010, Tribunal found that Pioneer engaged in price fixing, imposing a fine of R169 million
  - Pioneer then approached the Commission with the intention of settling all cases against it
- White maize products cartel
- Involved all major players in the milling of white maize, including Pioneer
  - From 1998 to at least 2007
  - Price fixing arrangements at national and regional levels
    - *Uniform price lists, timing of price increases and the implementation*
  - Attended meetings and held telephone conversations
  - Limited and prevent price competition

Background – Pioneer's conduct and theories of harm

- Milled wheat products cartel [flour]
- Involved all major players in the milling of wheat, including Pioneer
  - Price fixing and customer allocation arrangements
  - Attended meetings and held telephone conversations
  - Agreements were national and regional, mutually reinforcing
  - Information exchange complaint
  - Having uncovered the cartels, concerns about not observing competitive outcomes
  - Commercial sensitive information submitted and received
  - Investigation on-going
  - Exclusionary predatory pricing conduct
  - designed to exclude entrants in bread
  - Through fighting brands

Pioneer consent and settlement agreement

Fines and Remedies

- Corrective justice permissible under SA competition law
  - which is responsive to issues of distributional equity and fairness
- Institutional differences with the USA and Europe
  - Private enforcement of Competition law is weak
- Fines and deterrence
  - Concerns about the inadequacy of fines
  - Concerns that fines do not directly benefit the consumer and may lead to higher prices
- Remedies have both deterrence and desistance
  - Desistance because the competition authority can increase the intensity of competition by imposing remedies which can be monitored

Pioneer consent and settlement agreement

Design and Objectives

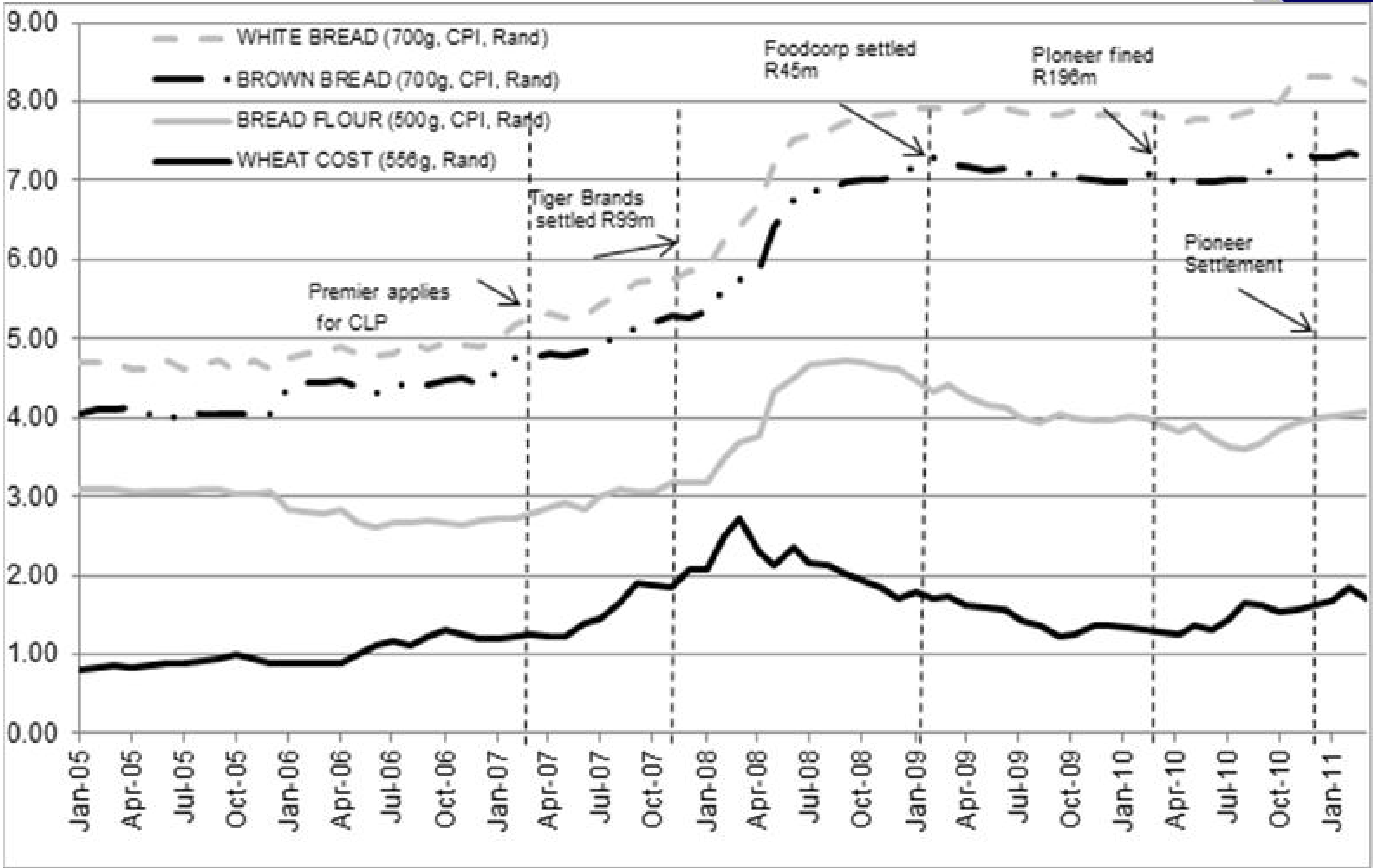
- Under SA competition law, the consent and settlement agreement needs to be "appropriate" and 'suitable"
  - Suitable in the sense that it is an agreement that suits the contending interests of the Commission, as the proxy of the public interest, and the respondent, and in that sense, can be appropriate as between themselves
  - Pioneer undertook in terms of the settlement agreement to:
  - Desist from the conduct, continue its compliance program and cooperate with the Commission
  - Pay an administrative penalty of R500 million to the National Revenue Fund
    - *Separately and in addition, the Commission, Treasury and Economic development department agreed to create an Agro processing Competitiveness Fund of R250 million*
  - Adjust the prices of selected products for an agreed period to reduce gross profits by R160 million
  - Maintain and increase capital expenditure by R150 million

- The administrative penalty
  - Amounted to about 5.6% of Pioneer Milling and Baking division
  - Pioneer's conduct affected the structure of the markets, the Commission decided not just to address anti-competitive effects through punishment and deterrence but also to address the structure of the markets
    - *Agro processing Competitiveness Fund aimed at facilitating new entry specifically small to medium enterprises*
    - *This is aimed at introducing competition and instability into historically stable markets to the benefit of poor consumers*
    - The price reduction commitment
  - Intended to undermine the effects of anti competitive behaviour on prices
  - Prices of bread and flour products went up due to the cartels and strategic behaviour underpinned by information exchange and have been sticky downwards following the uncovering of cartels
  - Direct consumer benefit as well stimulates rivalry and enables small non vertically integrated firms in bread
    - Commitment to increase capital expenditure
  - Aimed at increasing output as well as contributing to the creation of jobs

The impact of the price reduction commitment

- Implementation mechanism
  - Average realised gross profits of the selected products over the base period would be compared with the average realised profit over the comparative period
  - Minimum levels of gross profit reduction were set for each identified product category to ensure a meaningful effect for consumers
  - To mitigate on the likelihood of predatory outcomes, a minimum realised gross profit thresholds was set
  - Commission committed to monitoring bread and flour prices
- The current impact
  - Global increases in food prices recently because of increases in wheat prices and energy
  - South Africa is a net importer of wheat
  - Before the implementation of the pricing commitment wheat prices had been increasing

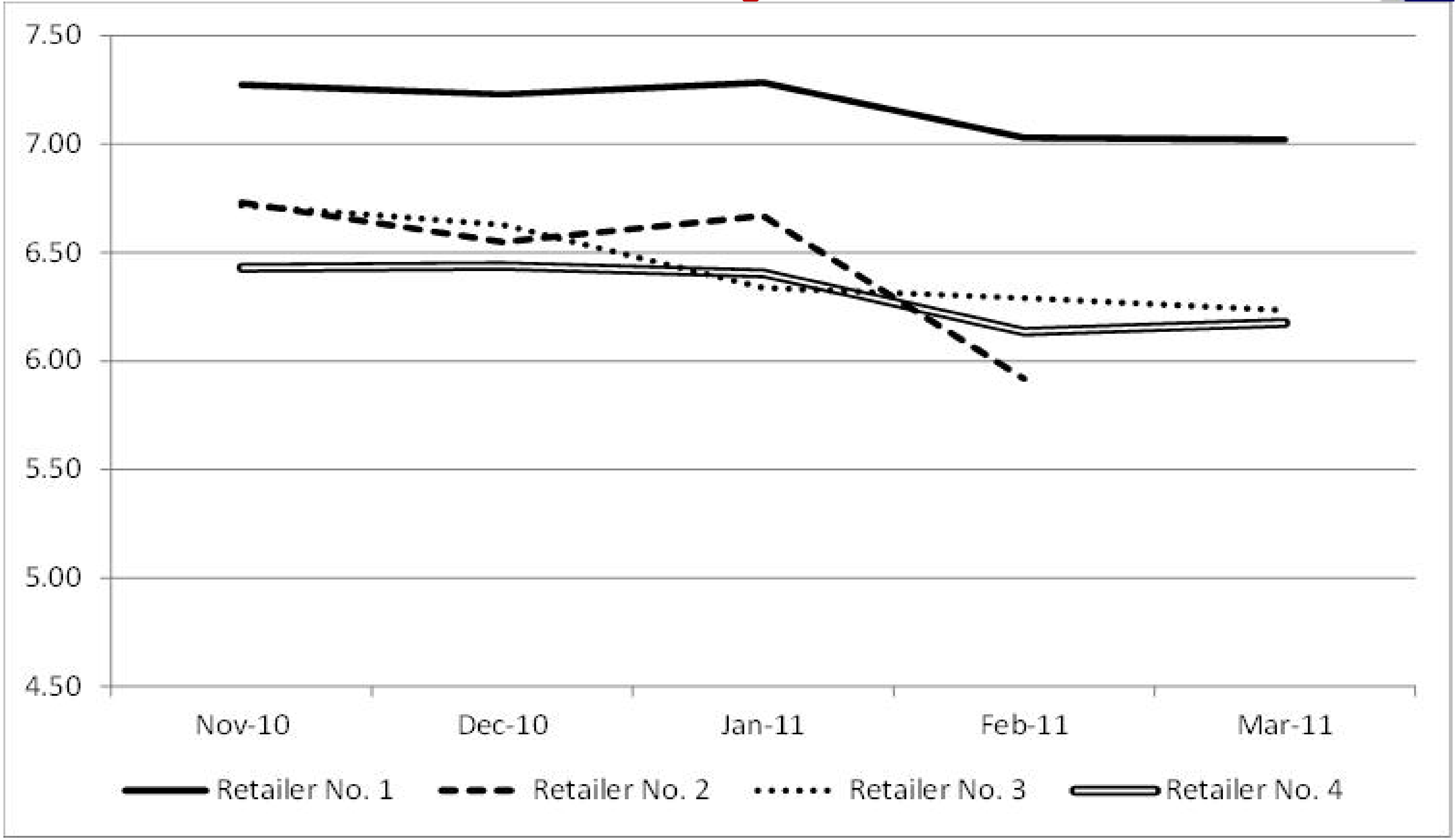
National bread and flour prices



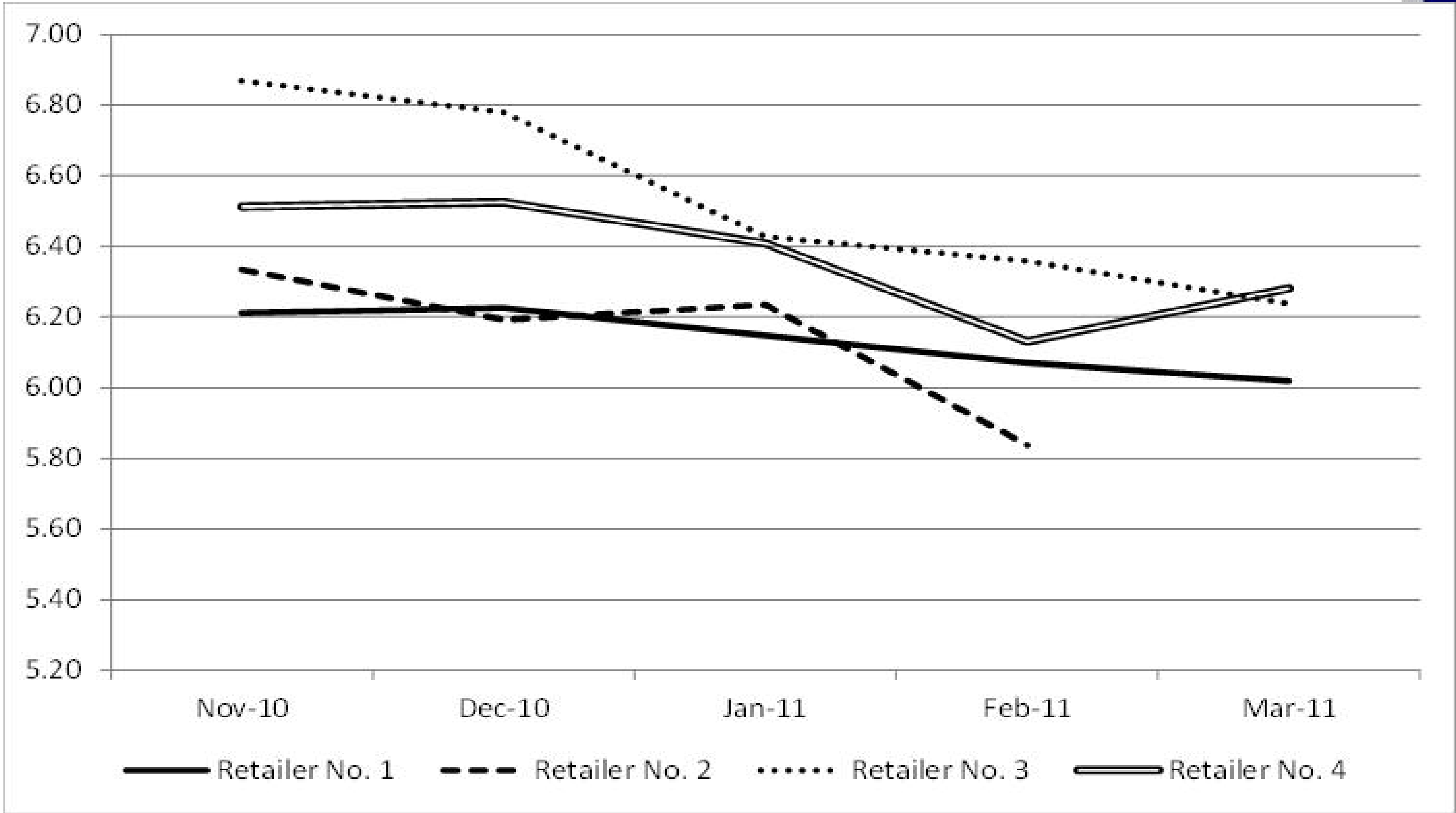
The impact of the price reduction commitment

- Recent developments
  - Pioneer has reportedly, following the implementation of the agreement, increased its volume growth at the expense of competitors. Business Report (National) 21 February 2011, p. 19
  - Competitors have publicly acknowledged that trading volumes have been negatively impacted, particularly in flour, as a result of the highly competitive trading environment.
  - An article by the Business Report in February noted how Tiger Brands' Albany bread was losing market share to Pioneer Foods' Sasko bread. Business Report (National) 21 February 2011, p. 19

Average wholesale price from all suppliers per retailer, white bread 700g



Average wholesale price from all suppliers per retailer, brown bread 700g



The impact of the price reduction commitment

- Pricing data from retailers indicates that
  - the price reductions made by Pioneer have translated into cheaper bread prices for end-consumers

– *In light of the recent increasing global inflationary pressures on food prices and South Africa's position as a net-importer of wheat*

  - *Since November 2010, the national price of brown bread decreased by around 11 cents per loaf, and stabilised at a lower level of around R7.30/loaf (nominal CPI up to March 2011),*
  - *while the national price of white bread has been stable at around R8.31/loaf in March 2011.*
  - Had it not been for the interventions of the Competition Authorities, consumers would have been faced with higher prices

Conclusion

- The Pioneer consent and settlement agreement is designed to address the negative impact of carte activity
- It provides for the opportunity to re store competition which may not be addressed solely by administrative penalties
  - The creation of the Agri-fund aims to lower the barriers to entry into the agro processing industry
  - The price reduction and capital expenditure terms seek to constrain Pioneer, compensate and disgorge some of its profits to the benefit of affected consumers and improve the competitive dynamics of the relevant markets.
- The Pioneer consent and settlement agreement is innovative and far reaching, because
  - The anticompetitive conduct was clearly identified together with the theories of harm.
  - The identification of the specific theories of harm led to the identification of the appropriate and sufficient remedies.