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# **Privatization, Predatory Pricing, and Monopoly in Egypt**

## **Examination of Alleged Abuse in the Cement Industry**

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**January 2003**

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This Letter is submitted by IBM Business Consulting Services (IBM), successor-in-interest to the business and operations of PwC Consulting, formerly a business unit of PricewaterhouseCoopers LLP. Novation of this contract to IBM is pending.

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# Privatization, Predatory Pricing, and Monopoly in Egypt

## I. The issue

One of principal benefits of privatization is that formerly government-owned firms are freed to compete in the market while relieving the Egyptian people of the burden of costly subsidies. Privatization gives firms an incentive to become more market responsive and globally competitive. Nevertheless, it is sometimes contended that private firms in Egypt collude to restrict competition and to impose higher prices on consumers of their products, thereby reducing the benefits of privatization. There is also a concern that a single firm will become so dominant in an industry as to constitute a monopoly or near monopoly that will impose high, non-market prices on its customers. These possibilities suggest the need for a *competition policy* to control the risks that private firms will attempt to cartelize or monopolize the markets in which they operate.

In this paper, *competition policy* is defined broadly, to include all those policies that influence competition --- trade, private investment, privatization, and regulatory policies. Too often *regulation* is viewed as the sole or principal effective response to anti-competitive practices, but this is usually not the case. Taking this broader view, this paper a) assesses an example of an alleged abuse observed in Egypt, b) identifies the fundamental policy alternatives, and c) suggests policy directions that are appropriate for Egypt. The paper will be divided into two sections, addressing respectively concerns of *predatory pricing* and of *monopoly*.

Some privatized companies, particularly foreign-owned ones, have recently been criticized in the Egyptian press and elsewhere for having engaged in “predatory pricing,” intended to drive out of business weaker, locally-owned firms. Presumably prices would then be raised as the industry is cartelized or even monopolized by a single competitor.

Such criticism, whether merited or unfounded, has consequences. The launches of at least two privatization efforts – both fertilizer companies – appear to have been delayed because of concerns of criticism based on competition issues.

While privatized firms hold – or potentially hold -- important positions in some industries in Egypt, issues of competition policy extend to all firms, whether privatized, private from establishment, or government-owned. Competition policy is addressed in the context of privatization policy because a) perceived or alleged anti-competitive practices among privatized firms are sometimes used as an argument against privatization itself or in favor of government maintaining a participation in the shareholding, and b) privatization policy can be a tool for creating more competitive markets.

## II. Claims of competitive abuse in Egypt - Example

A specific accusation of predatory pricing appeared in *Al Ahrām* on November 14, 2002.<sup>1</sup> The article states that cement prices in Egypt have dropped dramatically – an LE 70 fall -- since the beginning of the third quarter, from LE 190 to 120 per ton. Only one example is given to support this: sales by a privatized, foreign-owned cement company from Assiut selling in Sinai at LE 120 per ton. The claim is that, considering transport costs, this price represents a sale at LE 5 below “direct costs” and LE 40 less than “true” costs. The claim is that this is predatory pricing, that it is perpetrated by foreign-owned cement companies (although only one is named, in connection with the LE 120 per ton example), and that “The foreign companies will then raise the price of the cement to almost LE 400 per ton.” The article also briefly cites two other industries where supposed “pricing chaos” is observed, iron and gravel.

A construction contracting executive (cement consumer) is quoted as saying that LE 130 per ton is a “fair” price, claiming that cement companies in past years had (in the translated words of the article) “exploited the growing reconstruction trend in Egypt, raised prices and realized huge profits in no time.”

The article goes on to say that another cement executive claims that the cement prices should be “no less than LE 160,” the “true” cost. It appears from the article that “true” cost is meant to be average *total* cost per ton, including bank interest and all costs other in addition to the out-of-pocket costs (probably what is meant by “direct costs” in the article) attributable to production activities. The marginal cost of production of a ton of cement, which would be lower than out-of-pocket costs per ton, appears not to be considered in the article.

## III. “Predatory Pricing”

The “predatory pricing” claim is that a strong competitor in an industry (or multiple competitors working in cooperation) will sell at a price below average cost in order to drive one or more weaker competitors out of business, only to raise prices when competition is eliminated. Monopoly pricing is assumed to be long-term so that the investment in below-cost pricing can be recovered with an adequate return. If the monopoly cannot be sustained, there is little reason for the supposed predator to invest in its establishment -- and there is little reason for others to be concerned.

Claims of predatory pricing have been made in virtually all market economies for more than a century. The claims are almost always instigated by one or more market participants whose profitability is threatened by low prices of their competitors. It is in the interest of these threatened competitors to raise the accusations, whether directly or through allies in government, politics, or the press. Ironically, the objective of the accusers is often a price-fixing arrangement that conforms to their own special interests and is to the detriment of the interests of consumers.

Clearly, industry competitors, particularly weaker ones, have a motive to complain about low prices and to blame the “unfair” pricing practices of other competitors.

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<sup>1</sup> El Barghouthy, Mohamed, “Collapse in the Cement Market,” *Al Ahrām*, Cairo, November 14, 2002, p. 3.

Consumers, by contrast, benefit from low prices and therefore do not usually instigate claims of “predatory pricing.” This might indicate shortsightedness on the part of consumers (although these are often well-established businesses in their own right, sophisticated in their industry), or it may indicate that consumers see no substantial threat that they will be worse off in the long term, even if weak competitors are driven from the market.

But does predatory pricing make sense from the point of view of the alleged perpetrators? If a cut in price is indeed “predatory,” then the perpetrator must “invest” in selling at below his average cost. There are so many risks in a predatory pricing strategy that one must seriously question its rationality. Among the things that may go wrong for the predator are:

- Competitors are not driven out of business.
- Driving competitors from business takes longer than anticipated, or requires lower product prices than anticipated.
- Competitors are driven from the market, but competition from increased imports prevents the predator from imposing the anticipated price increases.
- The capacity of the failed producer is acquired by a stronger competitor, or it may remain idle until such time as prices are raised by the predator to profitable levels. The existence of this capacity is a continuing threat to the predator’s strategy. *Driving a competitor to bankruptcy does not destroy productive capacity.*
- The predatory strategy proves to be less profitable than many other alternative uses of the funds invested in the predation effort. In fact, the availability of investment alternatives, or the payment of dividends to shareholders, makes it unlikely that the highly risky predation effort would be undertaken in the first place.

There are legitimate business reasons – not involving the establishment of a monopoly or cartel -- for cutting prices or selling “below cost,” however defined. For example:

- To respond to changes in supply and demand. Price movements can be particularly volatile in industries characterized by high fixed costs.
- To maintain business operations despite very difficult business and pricing conditions that are deemed to be temporary. For example, some state-owned textile companies in Egypt frequently sell below their costs.
- To build a business before economies of scale are attained. For example, when Ford Motor Company was started early in the 20<sup>th</sup> century, cars were sold below cost to build demand until production could be increased to economic levels.<sup>2</sup>
- To avoid laying off workers in a temporarily depressed market. In other words, labor costs are quite reasonably viewed as fixed in the short term. *Otherwise, employee layoffs would be the response to every change in supply and demand.*
- To build market share in a new geographic territory.

These are far more economically rational reasons for selling near or even below cost than the usually unrealistic hope that monopolistic prices might one day be established and maintained. This is why the concept of predatory pricing has little

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<sup>2</sup> DiLorenzo, Thomas, “The Myth of Predatory Pricing,” Cato Institute, Washington, 1992, p. 7.

respect among economists. It is also why the U.S. Supreme Court has stated, “There is a consensus among commentators that predatory pricing schemes are rarely tried, and even more rarely successful...Cutting prices in order to increase business often is the very essence of competition...economic realities tend to make predatory pricing conspiracies self-detering.”<sup>3</sup> In fact, there are no unambiguous examples in the United States of a monopoly having emerged through predatory pricing tactics.<sup>4</sup>

According to the U. S. Federal Trade Commission (FTC), if pricing below cost is prohibited, “...much legitimate conduct may be chilled because there are many good reasons for pricing below cost for a limited period.” The FTC goes on to say, “If the seller cannot recoup its losses [from alleged predatory pricing], the below cost sales not only are unlikely to injure competition, but also probably did not arise as part of any intentional anti-competitive scheme.” Referring to “very difficult and resource-intensive” below-cost pricing investigations, the FTC observes that “most ultimately conclude that there was no violation.”<sup>5</sup>

Can competitors be hurt by pricing competition in a free market? Can some be driven to bankruptcy? Of course, but this is normal, and it is one of the mechanisms by which markets adjust to changing conditions of supply and demand or by which mistakes are corrected. The purpose of competition is not to ensure that weak competitors remain in business. As the FTC puts it, “Most modern competition law, including that of the United States, focus on protecting consumer welfare rather than individual competitors.”<sup>6</sup> Modern economies are dynamic, ever-changing, and free markets ensure *adaptation* to that change. This is more important than ever in today’s world, characterized by an accelerating rate of technology-driven change. Stagnation is the inevitable consequence of failure to adapt. Most state-owned firms in Egypt and elsewhere offer ample evidence.

Freeing firms to face the risks and rewards of the market, and removing business decisions from the political realm are among the principal advantages of privatization. Mistakes of state-owned firms are perpetuated with large and continuing subsidies because closing such firms is not consistent with the objectives, almost always short-term, of political decision makers. Re-politicizing business by interfering with private pricing decisions is a major step backwards.

Not only does aggressive price competition usually serve an economic purpose in assuring market adjustments to ever-changing economic conditions, lower prices also benefit consumers. These consumers may be families and individuals, or they may be other businesses for which lower costs are conducive to survival. In times of economic recession, as much of the world faces today, lower prices in one sector are a stimulant to economic activity in another sector.

Furthermore, because the supposed object of “predatory pricing” is to monopolize a market to the detriment of consumers, competition *policies that further reduce or eliminate the possibility of sustaining a monopoly will be sufficient to ensure that competitors have no incentive to pursue pricing strategies designed to attain monopolistic pricing.* That is, regulating “predatory pricing” is superfluous,

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<sup>3</sup> Matsushita Electric Industrial Co. v. Zenith Radio, 1986; cited in DiLorenzo.

<sup>4</sup> DiLorenzo, *loc. cit.*

<sup>5</sup> Federal Trade Commission, Washington, D.C., letter commenting on Egypt’s draft Anti-Trust and Anti-Monopoly Law, October 22, 2002, p. 14.

<sup>6</sup> *Ibid.*, p. 4.

protecting against monopoly is sufficient. Anti-monopoly policies will be addressed below.

#### A note on dumping

These accusations of predatory pricing do not constitute, as sometimes alleged, instances of “dumping.” “Dumping” is a term used in international trade that has traditionally meant selling in a foreign market at a price below that in the domestic market. More recently, as in US law, it has come to mean “selling a product abroad below cost.” “Cost” is not defined in US law, and this has led (perhaps intentionally) to arbitrary application where differing cost standards may be claimed by disputants.

The usual economic rationale for anti-dumping duties is not that a monopoly will allegedly result. Rather, most economists favoring anti-dumping rules base their views on the desire to protect the domestic industry from peculiar, temporary conditions of over-supply affecting a foreign country. This is termed “sporadic dumping.” That is, anti-dumping duties in these cases seek to protect domestic industry from cycles of contraction and expansion abroad.

John Gunn, an expert in international trade policies, and a former student of Jacob Viner, author of a landmark monograph on anti-dumping theory, states:

My judgment is that anti-dumping duties have not been used primarily in cases of alleged predatory pricing, but more often against governmentally-subsidized exports that continued over years at a time, or against direct government production, where dumping was used in cases where global recession or foreign recession reduced demand for the product... Sporadic dumping, too, is more often associated with such attempts to smooth the market... than to predatory efforts, although the latter has occurred.<sup>7</sup>

That there is a rationale for anti-dumping policies in international trade does not mean that the application of the concept is always free from abuse. In various countries, including the United States, dumping litigation or the threat thereof can be a tool for harassment of one’s competitors. Exaggerated accusations of dumping are backdoors to protectionism. Where costs are not precisely defined, as in the US law, the door is opened wider.

#### **IV. Comment on the cement industry allegations**

The *Al Ahram* article expresses the fear that because one company has sold at LE 120 per ton in Sinai, that a “foreign bloc” of cement companies will soon impose prices “five times” as high on the market. This is a strange claim given that several foreign-owned firms represent in total only about one-third of cement production capacity in Egypt. Government-owned firms control approximately the same percentage of capacity. Also, LE 120 per ton is only LE 10 less than the cited construction industry executive suggests is a “fair price,” only slightly below current average prices, and slightly above average prices in some recent months.

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<sup>7</sup> Gunn, John, Professor Emeritus of Economics, Washington and Lee University, correspondence of December 2002.

Moreover, even were there only one producer of cement in Egypt, the price of cement could not increase by five times or to LE 400 per ton because imports (and considering the high cost of transport) would be substituted and demand would drop dramatically. Clearly under these circumstances, the expectation of raising prices so far above market in the future is not a motive for selling at 120 today.

While quoting a cement executive who condemns one of his competitors for lowering prices to LE 120, the article quotes a cement consumer who estimates that LE 130, less than 10% higher, is a “fair price” and condemns cement companies for charging much more in the past. But should one be surprised to hear cement executives blaming their competitors for charging prices that are “too low” and to hear a cement consumer blaming cement companies for charging prices that are “too high”? Each is simply arguing his own special interest, with no substantive economic justification on either side. Referring to these problems of defining predatory pricing, including the difficulty of determining what cost standard should be used, the FTC observes, “Regardless of the standard used, it is difficult for sellers to know their precise costs at the moment of a sale.”<sup>8</sup>

As a solution to the alleged instance of “predatory pricing,” the article concludes that the Supreme Council for Cement, a producers’ price-fixing cartel, should be reinstated. This will be in the special interest of cement producers, particularly weaker ones, who want to shift the costs and risks of their own business decisions to cement consumers. Yet, the whole purpose of competition policy is to *prevent* such price-fixing arrangements by cartels and monopolies. Ironically, the article proposes that a price-fixing cartel must be established to raise prices and to “protect” consumers from the eventual emergence of another, theoretical price-fixing cartel.

### Cement price trends

Certainly the supply and demand picture is less favorable today for producers in Egypt than it was a few years ago. Increases in production capacity have outpaced increases in local consumption. Below are the figures from 1995 and 2002.<sup>9</sup> It should be kept in mind that average prices among suppliers reflect differences in cement quality, supply and demand conditions in local markets, and timing of sales, as well as differences in pricing policies.

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<sup>8</sup> Federal Trade Commission, *op. cit.*, p. 12.

<sup>9</sup> Statistics are from industry and financial sources, except where otherwise noted.

(000 MT)

	1995	1996	1997	1998	1999	2000	2001	2002
Total capacity	17200	17700	19200	21200	24600	27050	28600	31000 <sup>10</sup>
Egypt consumption	18001	19480	21153	23727	27541	26334	26751	25840 <sup>11</sup>
Exports	267	428	410	91	33	46	79	2801 <sup>12</sup>

Consumption has declined slightly since 1999, yet capacity has increased significantly. Capacity will increase further in 2003 to more than 33,000 tons. Under these supply and demand conditions, it is normal that prices will decline. There is no reason to suspect a conspiracy by foreign-owned producers, who in any case represent only about one-third of capacity today.

The sharp rise in exports in 2002 reflects over-capacity in the industry. Because of transport costs, cement companies only export when they have no choice --- margins are necessarily low, and quite possibly negative on various cost bases. Yet because fixed costs are high, it makes sense for cement companies to sell product as long as variable costs are covered. In the short-term, labor should also be considered fixed, otherwise workers would be laid off whenever sales fall.

Clearly, the business decisions to increase capacity in recent years were made in anticipation of higher demand than has proved to be the case. There is nothing unusual in this. Businesses take risks, and sometimes the results do not meet expectations.

Following is the range of average product prices of three cement companies (Suez, Torah, Helwan) from 1996 to 2001:

1996	160.4 to 170.9
1997	174.3 to 177.4
1998	175.2 to 190.0
1999	180.9 to 208.0
2000	169.9 to 199.6
2001	162.2 to 180.0

As an indication of more recent prices, Kawmeiah prices averaged 148 between July 1, 2001, and June 30, 2002. At Sinai Cement, the average monthly price from January to October, 2002, was LE 139, with a low of 112 in May and June, a high of 166 in July, and a level of 125 in October.

Current prices (December 2002) range as follows for six cement companies:

Helwan	140
Torah	139
Assiut	137
Beni Suef	135
Amereyah	130
Qena	130

<sup>10</sup> El Barghouthy, *loc. cit.* (New lines came on stream, particularly at Egyptian Cement.)

<sup>11</sup> Annual estimate based on sales through September of 19,385,000 MT (x 1.33).

<sup>12</sup> Annual estimate based on exports through September of 2,101,000 MT (x 1.33).

There is nothing remarkable or “chaotic” in this price behavior given the fluctuations in supply and demand over the period. The article’s claim of a precipitous drop, from LE 200 to LE 120 today, is simply not supported. Prices averaged well below LE 200 in 2001. Nor is lower, let alone “predatory,” pricing by a “foreign bloc” supported. Certainly cement companies, Egyptian-owned and foreign-owned, would prefer higher prices but this is no justification whatever for regulatory intervention in pricing decisions. Prices appear to have recovered since the May – June period of seasonally low demand.

Another apparent objective of the article is more subtle: to suggest that producers in one locality be isolated from producers in other localities. This is why transport costs from Assiut to Sinai are cited to support the claim of predatory pricing. But markets do not operate on a cost-plus basis. Producers from other regions cannot be barred because they refuse to price their products uncompetitively on some specified cost-plus basis. Formulas that effectively reserve markets to local producers constitute a restraint of trade in most countries with competition policies. The FTC states, “...our experience has also shown that some types of joint conduct are never, or almost never, justified. These include agreements to fix prices, divide territories, or reduce output.”<sup>13</sup>

### Conclusion

Obviously consumers benefit from lower rather than higher prices, particularly in times like now when the economy is weak. Construction activity is stimulated when investors seek to take advantage of lower prices for building materials. If prices are kept artificially high by a cartel, then cement production will decline to a level less than it otherwise would have been. Cement workers will be laid off, and employment prospects elsewhere in the construction industry will decline. Cement industry investors will benefit, but the costs are transferred to others, including labor.

The purpose of competition is not to ensure that weak competitors remain in business, nor is the purpose of competition to ensure that businesses are protected from the consequences of their own errors, from changes in supply and demand, or from the bad outcomes that are always a possible consequence of the risks inherent in even the most reasonable business decisions. To protect competitors against such errors, changes, and risks only ensures economic stagnation. Public enterprises in Egypt offer a good example of the high costs to society that result from efforts to resist changing circumstances and efforts to insulate business from bad decisions and bad outcomes. Egypt should not attempt to duplicate the consequences of failed government ownership by imposing cartelization and excessive or superfluous regulation.

Prices fluctuate in a free market, and these fluctuations can be particularly significant in industries like cement with high fixed costs. The fact that some competitors sell at low prices is no indication whatever that there is a plot to monopolize the market. Even if there were such a plot, it would be almost certainly be doomed to failure. There is very little evidence anywhere of monopolies having been created through predatory pricing. Reducing prices is a rational response to changing supply and demand conditions. Lower cement prices today are the mechanism by which the relationship between capacity and consumption will be brought more nearly into

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<sup>13</sup> Federal Trade Commission, Washington, D.C., *op. cit.*, p. 13.

balance. There is no justification for the establishment of a pricing cartel or other monopolistic practices to favor special interests in the cement industry.

#### **IV. Anti-trust and monopoly law**

As mentioned above, competition policy, broadly defined, should focus on preventing the establishment of sustained monopolies.

There are two excellent and recent papers, both prepared from a legal perspective, that address competition policy in Egypt, and there is no need for us to attempt to duplicate their work:

1. The letter, cited above, from the U.S. Federal Trade Commission to the U.S. Agency for International Development in Cairo, assesses Egypt's draft Anti-Trust and Anti-Monopoly Law. Those drafting the law should consider carefully the advice offered in this letter, which reflects long experience with the issues in the United States (including lessons from past errors), as well as sound economic reasoning. The letter consists of detailed comments on each article of the draft law.
2. A working paper published by the Egyptian Center for Economic Studies (ECES) entitled "On the Formulation and Enhancement of Competition Law in Emerging Economies: The Case of Egypt." The authors are Bahaa Ali El Dean and Mahmoud Mohieldin.

The FTC paper does not presume to address issues of enforcement in Egypt. The ECES paper does address enforcement issues, as well as offering assessments of comparative competition policy experiences in Poland, Hungary, and Mexico.

The following comments on these papers are limited to issues of economics and to incentives to invest in Egypt. Therefore the discussion covers the concept of perfect competition, which figures in the ECES paper; non-regulatory means of protecting against the establishment and maintenance of monopolies; and the enforcement context in Egypt.

##### Perfect competition

The ECS paper states, "...the concept of perfect competition is useful for two reasons: as a benchmark and as an institutional characterization of some markets, e.g. primary commodities." The paper continues, "Since there is widespread diversion from the ideal paradigm [perfect competition], there is a necessity for corrective intervention by government."<sup>14</sup>

This is a misuse of the theoretical construct of perfect competition, and it can lead to important policy errors. Far from being an "ideal paradigm," perfect competition, were it ever to exist, would characterize a stagnant market devoid of innovation. Markets work because they offer incentives, particularly high profit incentives, to invest and innovate. It is the attraction of profits above normal that energizes a

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<sup>14</sup> Ali El Dean, Bahaa and Mahmoud Mohieldin, "On the Formulation and Enhancement of Competition Law in Emerging Economies: The Case of Egypt," Egyptian Center for Economic Studies, Cairo, 2001, p. 4.

dynamic modern economy. Perfect competition is a static concept, commonly used as a teaching tool in introductory courses in economics. The reality of markets today is one of rapid change, continual innovation, “creative destruction” in Schumpeter’s words. “Perfect” connotes “desirable,” and the semantic bias is unfortunate. The ideal, in Egypt as elsewhere, is dynamic markets that continually allocate and reallocate resources, not stagnant or “perfect” ones.

The concept of predatory pricing is an example of the misuse of the concept of perfect competition. As DiLorenzo states:

The theory of predatory pricing fails to recognize that price cutting--even below average cost--is a normal activity in competitive markets. That is because the theory is derived from the so-called perfect competition model of economic theory. In an ideal, or "perfectly competitive," market, every firm charges an identical price, and in equilibrium that price is equal to average total cost.<sup>15</sup>

The FTC paper makes clear by implication that perfect markets are not the ideal by which market practices and regulatory policies should be judged. Attempting to apply a standard of “perfect competition” would undermine, not advance, the objectives of competition policy.

#### Non-regulatory protections against monopoly

An open economy is the best defense against cartels and monopolies. Egypt’s economy has been plagued by restraints on competition, but these restraints, as so often is the case elsewhere, have mostly been sanctioned by government. The former cement pricing cartel is an example. Another example is government-subsidized pricing that discourages the entry of competitors to the market. History shows that monopolies and cartels are rarely persistent in the long-term unless enforced by government policy.

Cartels and monopolies, where they may be established, are threatened by a) members withdrawing in order to increase sales, b) imports, c) entry of new competitors, and d) new technologies. Therefore, restrictive trade practices -- high import duties and non-tariff barriers -- should be discouraged; the market should be open to foreign investors; regulatory approvals for establishing a business and for new project investments, whether foreign or domestic, should not be cumbersome; and the introduction of new or more efficient technologies should not be impeded by special interests or regulatory obstructions. Egypt’s accession to the World Trade Organization is a quite positive development that will help to ensure that the country’s markets are open.

Privatization policy can also help to ensure that markets are open. Where constraints on competition exist among public sector companies, the privatization process should help to ensure (as it appears to do in practice in Egypt) that such constraints do not persist after privatization. Where there are only one or two domestic competitors in an industry and cartelization is feared, a privatization might be designed to disperse ownership by breaking an existing enterprise into two or more competing privatized companies. Nevertheless, if a market is open to imports, even a single domestic competitor may not constitute a threat to consumers. The FTC offers, “For example,

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<sup>15</sup> DiLorenzo, *op. cit.*, p.

if there is only one company selling semiconductor chips in a country, that company would control 100% of the domestic market. But if Intel were poised to enter that nation's market, the domestic company's 100% market share would give it little market power, as a practical matter."<sup>16</sup>

### Enforcement context in Egypt

There is a very good discussion of the Egyptian enforcement context in the ECES working paper. Because this is such an important determinant of the effectiveness of any regulatory policy, such as embodied in the draft Anti-Trust and Monopoly Law, some comments follow. As Ali El Dean and Mohieldin state, "Enforcement issues represent the main difficulty in introducing competition law... Establishing an efficient enforcement agency capable of implementing sophisticated competition legislation can only be seen as a long-term objective."<sup>17</sup> The ECES paper goes on to cite "...the problem of judges in emerging economies who often lack the necessary training to enforce sophisticated laws that require economic analysis."<sup>18</sup>

Indeed, one of the fundamental reforms required in Egypt, as noted by both foreign and Egyptian observers, is that of the court system. In addition to concerns of economic expertise expressed in the ESCS paper, the slow pace of litigation, with even relatively simple cases dragging on for years, raises further questions as to the enforceability of competition policy in Egypt.

A cumbersome litigation system, combined with regulators and judges ill-trained to handle the complexities of competition regulation, may undermine rather than promote the rule of law. For example, under such circumstances, special-interest plaintiffs may use the law as a means of harassment of more efficient competitors. The recent cement industry accusations in Egypt suggest that there will be no shortage of unhappy competitors willing to use the law for such purposes. *In short, an ill-equipped enforcement system may serve to turn competition laws and regulations into a tool for undermining competition.* Moreover, investment in the economy will be deterred rather than encouraged if there are fears that competition laws and regulations will be used by competitors to gain advantage rather than to protect consumers, or if legal procedures will be long and cumbersome.

As a solution Ali El Dean and Mohieldin suggest a *per se* regulatory system in which clearly defined rules, as opposed to the rule-of-reason in advanced economies, are applied. There is substantial merit to this suggestion, although there remains reason for caution: the *per se* rules embodied in law may themselves be anti-competitive. For example, a *per se* rule reflecting the conventional wisdom that "selling below cost" is by definition bad, would be destructive of competition. If the *per se* approach is taken, the rules should be few and well-targeted. For example, proof that an agreement among competitors exists to divide markets geographically or by customer would be an appropriate *per se* offense,<sup>19</sup> as would an agreement among competitors to price according to an agreed "cost-plus" or other formula.

## **V. Conclusions**

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<sup>16</sup> Federal Trade Commission, *op. cit.*, p. 6.

<sup>17</sup> Ali El Dean and Mohieldin, *op. cit.*, p. 13.

<sup>18</sup> *Ibid*, p. 14.

<sup>19</sup> Federal Trade Commission, *op. cit.*, p. 14.

Predatory pricing as a prelude to monopoly or cartelization is a theoretical construct with little relation to reality. In the USA, “there have been hundreds of federal antitrust cases based on claims of predatory pricing, economists and legal scholars to this day failed to provide an unambiguous example of a single monopoly created by predatory pricing.”<sup>20</sup> Evidently, the concept of predatory pricing is flawed in theory as well as in practice.

Claims of “predatory pricing” usually prove to be fictions perpetrated by special interests seeking to raise prices at the expense of consumers. The probability of a predatory pricing scheme yielding an adequate return to the perpetrator by generating monopoly profits is rarely great enough to justify initiation of the effort, let alone produce success. Even if a competitor were driven to bankruptcy, industry capacity is not destroyed but becomes available to new investors at a price based on market conditions for the products produced. The *Al Ahram* article cited above appears to reflect a classic case of special interests seeking favors from government: concentrating benefits among a privileged few (cement companies in this case), while broadly dispersing costs among consumers.

Privatized firms have not instigated predatory price declines. Rather the price declines in 2002 simply reflect a significant increase in capacity coupled with a more modest decline in demand. There is no reason to restrain privatization activity on the basis of experience in the cement industry. Nor does there appear to be any reason to suspect that privatization is conducive to anti-competitive practices. *By contrast, in the cement industry privatization has coincided with the abandonment of former anti-competitive price fixing practices.*

While an anti-monopoly law is in theory desirable for Egypt, it seems that reform of the judicial system is a greater priority if not a prerequisite. Egypt may, in the interim, be better off relying on non-regulatory competition policies, such as free trade and open entry to markets. While a second-best solution, this may be the best attainable under current circumstances. Also, the costs of not having an anti-monopoly law and regulation may not be as high as may first be feared. Today, Egypt faces a greater challenge in convincing investors that they can earn adequate returns on their investment than in combating monopolists that are earning profits that are too high. The prominent monopolies or price-fixing arrangements in Egypt are sanctioned by government, although private collusive arrangements no doubt exist as well. It appears at this stage in Egypt’s development that government policies are more likely to be the cause of economically destructive competitive restraints than private collusion.

It does appear feasible, even under existing enforcement conditions in Egypt, to devise *per se* rules that would make a positive contribution to the competitive environment. But devising appropriate rules places a heavy burden on the legislature, and therefore it is urged that law makers be carefully advised on appropriate rules by experienced regulators in other countries. As pointed out earlier, inappropriate rules may hinder rather than promote competitive markets.

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January 15, 2003

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<sup>20</sup> DiLorenzo, *op. cit.*, p. 9.