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**Non-competitive behaviour: Case
Studies from the cement and
pharmaceutical sectors**

Mahvash Saeed Qureshi

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Table of Contents

Abstract.....	1
Case Study 1: Cartelisation by the cement manufacturers.....	1
Case Study 2: Merger in the pharmaceutical sector	6
References.....	13

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Non-competitive behaviour: Case Studies from the cement and pharmaceutical sectors

Mahvash Saeed Qureshi¹

Abstract

Evidence suggests that undue industrial concentration and unreasonable monopoly power have remained a major problem in the history of growth of Pakistan's corporate sector. Cement, pharmaceuticals, tobacco, sugar and vegetable ghee are some of the sectors where restrictive trade practices have been witnessed quite frequently. Though, a competition legislation and authority were established as early as 1970, enforcement of the ordinance in most cases has remained a myth. The law is outdated and needs amendments in light of the changing global and national conditions. This paper attempts to review two cases of anti-competitive behaviour, cartelisation in the cement sector and merger activity in the pharmaceutical sector, witnessed in Pakistan. The relevant provisions of the law and their enforcement in each case are also discussed. The analysis reveals that the competition authority is a weak body lacking power and resources to take appropriate actions and implement its orders.

Case Study 1: Cartelisation by the cement manufacturers

1. Factual Presentation

Introduction

According to the Economic Survey of Pakistan, 2000-01, there are 24 operating cement units in the country with total installed capacity of 16,300 thousand tonnes.² Out of these 24 units, 4 with installed capacity of 1,831 thousand tonnes are in the public sector and 20 units having capacity of 14,440 thousand tonnes are in the private sector.³ The total production of cement was recorded at 7.2 million tonnes during July-March 2000-01 as compared to 7.1 million tonnes in the same period of 1999-2000, showing a marginal increase of 1.4 percent.

The capacity in the sector has been rising continuously. In the year 1995, there was an under-supply of 0.4 million tonnes, this gap was later reduced in 1996 and there was a shortage of 0.1 million tonnes. A situation of over supply was witnessed in the period 1997-98 when excess supply of cement jumped from 0.7 million tonnes to 4.5 million tonnes, respectively. By the end of the year 2000, demand could only touch 9.91 million tonnes and with the capacity having gone up to 16 million tonnes, much capacity remained idle.⁴

1 The author owes a debt of gratitude to Dr. Shahrukh Rafi Khan, Executive Director, SDPI, for extensive and valuable comments. Thanks are also due to Sajid Kazmi, Research Associate, SDPI and Ms. Kishwar Khan, Economist, Monopoly Control Authority, for their useful discussions and insights.

2 Source: Govt. of Pakistan, *Economic Survey 2000-01* (Chapter 3, pp. 38)

3 In case of cement, none of the producers has a large market share making concentration not an important issue.

4 Source: Report on the Cement Sector prepared by Monopoly Control Authority 1999 and Pakistan and Gulf Economist, Nov 12-18, 2001.

The sharp fluctuation in cement prices and relatively lesser demand for cement in the past few years are responsible for slower growth in cement production.⁵ Infact, there has been a visible decline in the contribution of the construction industry to the Gross Domestic Product over the decades and the share has fallen from 4.2% in 1969-70 to 3.4% in 2000-01. This is one of the reasons for a slow overall economic activity of the country and a stagnant share of the manufacturing sector in Gross Domestic Product over the last three decades.⁶

Foreign Direct Investment (FDI) in the sector has been a small percentage of the total FDI for the past many years. During July-March 2000-01, FDI in the cement sector was US \$ 15.2 million, which amounts to 6.54% of the total FDI received during that period. In view of the excess capacity in the industry, this is hardly surprising.

Pakistan has large quantities of both limestone and gypsum and a large domestic market. Cement was one of the few industries with an established base in Pakistan at the time of independence in 1947, when there were five cement factories. Pakistan currently produces five types of cement: Portland Grey, Portland Slag, Sulphate Resistant, Super Sulphate Resistant and White. Historically, Pakistan has been exporting cement whenever it had surplus capacity. It exported considerable amount of cement during the 1960s and 1970s. However, currently, the exports are stagnant.⁷

In 1972, the Government of Pakistan nationalized cement factories and consolidated them under the State Cement Corporation of Pakistan. The current wave of privatization has reversed that initiative.

Description of the Case

Though no major merger and acquisition activity affecting the domestic market has been witnessed so far in the cement sector, there is evidence of collusive behaviour by the firms. In October 1998, the Monopoly Control Authority (MCA) of Pakistan noticed a simultaneous and uniform price increase of Rs. 100 per bag by the cement manufacturers. This sudden and unparalleled increase in the price of cement was met by a strong reaction from consumers all over the country.

The All Pakistan Cement Manufacturing Association (APCMA) and individual manufacturing units attributed this increase to the increase in the cost of inputs and high taxation. They considered the price increase as the only way out for the cement manufacturers to avoid closure of the manufacturing units, which were facing huge losses due to low demand and low prices during the preceding years. While justifying their actions, the cement manufacturers referred to an example where in the face of suppressed demand in June 1998, one of the manufacturers lowered the price from Rs. 208 per bag of 50 kg to Rs. 156. The rest followed suit for fear of being kicked out of the market, since there is not much difference in the quality of the cement being produced by different manufacturers.

5 The lesser demand for cement over the years has been attributed mainly to two factors: political instability in the country and continuously rising prices of cement.

6 Source: Government of Pakistan, *Economic Survey 2000-01* (Chapter 1).

7 However, keeping in mind the recent post-war rebuilding efforts in Afghanistan, there is anticipation that cement might be imported from Pakistan in the future. Iran would be the major competitor in this regard and effective policies and quick action on the part of the Government of Pakistan are required to capture markets in Afghanistan.

2. Legal Issues

The Monopoly Control Authority (MCA) is a statutory, quasi-judicial body established in its present form to administer the Monopolies and Restrictive Trade Practices (Control & Prevention) Ordinance, 1970. The broad objective of the legislation is to provide for measures against undue concentration of economic power, monopoly power and restrictive trade practices. The law spells out circumstances, which shall be deemed to constitute the above, and under **Section 3** of the ordinance prohibits these clearly defined situations.

Under **Section 6** of MRTPO, unreasonably restrictive trade practice has been defined as any practice, which unreasonably prevents, restrains or lessens competition. These include agreements

- (a) between actual or potential competitors of
 - *fixing the purchase or selling prices or imposing any other restrictive trading conditions with regard to the sale or distribution of any goods or the provision of any services;*
 - *dividing or sharing of markets for any goods or services;*
 - *limiting the quantity or means of production, distribution or sale with regard to any goods or the manner or means of providing any service;*
 - *limiting technical development or investment with regard to the production, distribution or sale of any goods or the provision of services;*
 - *excluding by means of boycott any other or undertaking from the production, distribution or sale of any goods or the provision of any services;*
- (b) between a supplier and a dealer of goods fixing minimum resale prices including
 - *an agreement with a condition for the sale of goods by a supplier to a dealer which purports to establish or provide for the minimum prices to be charged on the resale of the goods in Pakistan; or*
 - *an agreement which requires as a condition of supplying goods to a dealer the making of any such agreement;*
- (c) In addition to these enumerated practices, the Authority may identify others which are found to be unreasonably restrictive. For example, it might well find that restrictions, in distribution agreements which limit the customers or territories of distributors are unreasonably restrictive in certain circumstances. ‘Agreement’ here has been defined to include any arrangement or understanding whether or not in writing and whether or not it is legally enforceable. This would mean that unwritten collusive agreements would fall within the definition of the word ‘agreement’. This is an important provision because restrictive arrangements and agreements are quite often not in writing.

MCA assesses the impact on public interest in any of the above mentioned situations and through evidence collection focuses on the issue for analysis. Under **Section 11** of the MRTPO, in case of unreasonably restrictive trade practices the order of the authority may:

- (1) *require the person or undertaking concerned to discontinue or not to repeat any restrictive trade practice and to terminate or modify any agreement relating thereto in such manner as may be specified in the order;*
- (2) *require the person or undertaking concerned to take such actions specified in the order as may be necessary to restore competition in the production, distribution or sale of any goods or provision of any services.*

Section 12 of the MRTPO deals with the orders of the Authority and lays down the parameters within which the Authority will function. The orders of the Authority have been specifically related to the situation being investigated, i.e. separate remedies have been provided for situations of concentration of economic power, monopoly power and trade restrictive practices.

Under **Section 14** of the MRTPO, the MCA is empowered to conduct enquiry in circumstances constituting undue concentration of economic power and unreasonably restrictive trade practices. It was under this provision of the ordinance that the MCA decided to look into the matter.

3. Analysis of the case vis-à-vis the MRTPO Provisions

After careful consideration of the relevant information, MCA initiated an enquiry to unfold the causes of the uniform price increase in the cement industry. All Pakistan Cement Manufacturing Association (APCMA), individual units and users associations were also associated with the inquiry.

MCA found that there had been no increase in lease money, furnace oil and excise duty since June 1997. On the contrary, during the period mentioned, the level of taxation had been reduced and the price of furnace oil had also been reduced by Rs. 800 per ton. However, there had been only a marginal increase in electricity charges in late 1997. Thus, the claim of APCMA of substantial increase in input prices as well as the tax rate was falsified. The APCMA and owners of individual units could not justify their action with a satisfactory explanation to the MCA authorities and based on its analysis, the MCA was convinced that the manufacturers had under tacit agreement increased the price prevailing in the market in early October i.e., Rs. 135/bag to Rs. 235/bag in mid October, 1998.

MCA established that the manufacturers had through cartel formation increased the price of cement. The action of APCMA and individual units contravened the provision of **Section 3** of the MRTPO, which prohibits any restrictive trade practice in the market, along with **Section 6**, which prohibits any agreement between competitors of fixing the selling/purchasing prices. Thus, cartelization and collusion between the manufacturers in terms of **Section 6(1)(a)** was proved and it was recognized that the sole purpose of the cooperation among producers was to gain monopoly profits.

The firms had successfully colluded to increase price giving rise to anti-competitive behaviour in the market. Consumers were compelled to consume less because of the higher price and lower production leading to loss of consumer welfare and inefficiency in the market. This meant substantive public and national loss as cement is an important industrial sector and has strong linkages with the rest of the economy.

4. Decision of the enquiry

Thus, MCA refuted the argument by APCMA regarding substantial increase in input prices. It held a series of meetings and hearings and concluded that the price increase had no economic justification and was motivated by the desire to increase profit margins.

The MCA decided to take action and issued show cause notices to the manufacturers under the **Section 11** of the MRTPO, 1970.

Under **Section 12(c)** of the MRTPO, APCMA was ordered to break the cartel and reverse the price to that prevailing prior to the increase. It was further directed to remove restrictions on capacity utilization with immediate effect and to utilize full production capacity to lower overhead expenses and overall cost.

Moreover, MCA ordered APCMA to deposit a sum of Rs. 4.25 billion, earned by the industry as additional revenue from the price increase between mid October 1998 and Feb. 1999, to the Baitul Mal and the same to be disbursed to the consumers on duly verified claims.⁸ MCA further imposed a fine of Rs. 100,000 on each individual unit and in case of continued non-compliance another Rs. 10,000 per day per unit.

The controversy continued and the cement manufacturers refused to lower the price. Instead of implementing the orders, the industry reacted by accusing the government of market interference. The representative of the cement manufacturers decided to go against the orders of the authority, moved to the provincial High Court and got stay orders. The manufacturers were not bothered about the fine as it was so small and did not even deposit the ordered amount of Rs. 4.25 billion to the Bait-ul-Mal. At the same time, wholesalers and dealers stopped buying cement fearing that a fall in price would lead to losses. The situation soon became of great concern as downstream consumers and builders faced hardships in purchasing cement.

Finally, the government intervened and despite the MCA's theoretical independence, persuaded it to close the case. The Ministry of Commerce after negotiations lowered the excise duty and the price was set at Rs. 200 per 50 kg bag.

5. Recommendations

The more or less simultaneous announcement of price increase by all undertakings regardless of their location, technology or process used and period of entry in the market was a sufficient condition to prove cartelization in the cement sector. In this situation, although, MCA acted in favour of the public, yet it was not able to communicate its efforts to the consumers. If consumers had been mobilized, it would have given MCA leverage in the political economic decision matrix. By raising the prices, the producers wanted to exploit the consumers as there is no substitute available for cement in the market. Despite MCA's strong reaction to the monopolistic attitude of the manufacturers, ultimately it was the latter who benefited as the price fixed by the government favoured them greatly.

According to a report on the cement industry in Pakistan, published by the Monopoly Control Authority, none of the producers in the cement sector has a large market share, which raises the chances of collusion. Unlikely to the conventional assumption that cartels break down under pressures of excess capacity and there exists a negative correlation between cartelization and excess capacity, this case may be viewed differently. Excess capacity gave colluders a stronger bargaining position in their negotiations about pricing and production and as in tacit collusions, the firms with excess capacity could punish deviators more harshly making deviations less likely to occur.

The cement industry, which is a central part of the construction industry, creates job opportunities for millions in the country and is currently running below 50 percent of the installed capacity. The

8 Baitul Mal was established in Feb. 1992 under the provisions of Pakistan Baitul Mal Act 1991 to provide assistance to those in need, especially minorities, who are not covered by *Zakat*, a religiously mandated charity in Islam.

government should have put emphasis on this fact and instead of increasing the price of cement should have allowed export rebate and introduced other incentives for those successful in breaking into export markets, while ensuring internal competition. The government could have also taken measures such as reallocation of resources to infrastructure development, housing and industrialization, to activate this sector.

Furthermore, the amount of penalty imposed was very low as compared to those in other countries. Instead of siding with the defaulters, the government should have increased their fines due to non-compliance.

A serious issue is that of the jurisdiction of the authority. Once MCA had taken up an issue, it should have been left to the judgment of MCA and there should not have been any interference from the government or Courts in its working. Not only theoretical but practical independence is also crucial for the Authority to have the desired image of a strong and impartial body.

Since it was a question of public interest and the “cement mafia” had clout with the government, the Authority should have involved different consumer organizations, NGOs and experts. This would have put pressure on the government and it would not have knelt down to the demands of the producers. A countervailing force in the political-economic context to avoid rent-seeking would have been created. In reality, there are no mechanisms of involving other civil society groups and representatives of citizenry in MCA’s advocacy and outreach programmes. Though consumer movement in the country is in its nascent stage, yet there are some groups actively pursuing public interest issues in Pakistan.⁹ Partnerships with such groups and members of academia could be a useful vehicle to reach its constituency and help it to enhance competition.

Advocacy is an important function of the competition authorities around the globe. Through advocacy, competition authority provides advice, influence and participates in government’s regulatory and economic policies to promote competitive industry structure, firm behaviour and market performance. MCA lags behind in this also as it doesn’t have strong media links. It should lay more emphasis on educating and awaring the general public on whose behalf it acts. Thus, there is an urgent need to revitalize this important institution and strengthen it to give relief to the public.

Case Study 2: Merger in the pharmaceutical sector

1. Factual Presentation: *Introduction*

The pharmaceutical industry, which in Pakistan was almost non-existent at the time of independence in 1947, is now the second largest in the country. It has been growing steadily over the years and this growth is linked with the increasing population and rising urbanization.¹⁰ The total pharmaceutical market in the country is currently estimated at US \$1000 million, with a five percent annual growth.

At present there are over 400 licensed pharmaceutical companies in Pakistan, including 26 multinationals. All top pharmaceutical companies are multinationals and in the list of the first twenty largest pharma companies, there is no domestic manufacturer. The market shares of multinational companies (MNCs)

9 For example, The Network for Consumer Protection and Consumer Rights Commission are now active in various consumer right issues.

10 For example, during 1993-97, the industry grew by a compound growth rate of 23.7 percent.

and local companies have been changing over time. In terms of volume, the balance has tilted in favour of the local companies in recent years and 60 percent of the volume is produced by them. In value terms also, the national companies have been claiming a greater share of the pie over time. Whereas, 32 MNCs accounted for 70-80% of the value of the pharmaceutical market in Pakistan in early 1990s, today it stands at only half of the market value.

The pharma industry is one of the most highly regulated sectors in the economy and is subject to government controls and monitoring with respect to prices and registration. Pakistan is perhaps the only country where the government has imposed duties and taxes on such an essential industry. Sales tax is levied on medicines and pharmaceutical products besides imposing regulatory duty on the import of raw materials, other intermediate goods and packing material.

Government policy categorizes drugs into controlled and de-controlled. Under the 1993-94 Statutory Regulatory Orders of the Ministry of Health, approximately 821 drugs come within the controlled category where the total number of registered drugs is 24,000. However, even the de-controlled drugs are monitored and regulated by the government.

A large number of MNCs in the pharmaceutical sector contribute to domestic production, but mainly for formulations. This creates a demand for the intermediaries, which are not produced domestically in the desired quantity, and hence have to be imported. For production of drugs currently about 95% of the raw material is imported by both the local and multinational companies. Pakistan's annual bulk drug import is estimated to be approximately US \$ 400 million. According to the *Economic Survey 2000-01*, the total imports of drugs and medicines during the year 1999-00 was Rs. 13,429 million whereas, the total export for the same period stood at Rs. 3,040 million.

The representative body of the local companies is Pakistan Pharmaceutical Manufacturers Association (PPMA), which at present has a membership of 181 companies. Pharma Bureau in Pakistan primarily represents pharmaceutical MNCs under the umbrella of Overseas Investors' Chamber of Commerce & Industry. In 1993, there were 32 pharmaceutical MNCs but their number has reduced over the last decade to 26 owing to mergers between big pharmaceutical companies. MNCs operate as commercial identities or have a presence as subsidiaries owned and run by local entrepreneurs. According to the 1995 survey by Pharma Bureau, there were ten American, eight British, six German, one Japanese, one Dutch, and one French MNCs operating in Pakistan.

Description of the case

Glaxo Wellcome Pakistan Limited was formed in 1996 through the merger of Glaxo Laboratories Pakistan Limited and Wellcome Pakistan Limited.¹¹ The objective of the merger, as stated by the firms, was to become a market leader in the pharmaceutical industry of Pakistan and to be recognized as a global research based company. Glaxo Group Limited, U.K., and its nominees hold about 70 percent of Glaxo Wellcome Pakistan's shares.¹²

11 This merger was the result of the merger between the parent companies abroad.

12 In December 2000 the parent Glaxo-Wellcome located in United Kingdom, merged with another already merged pharmaceutical company, SmithKline-Beecham, leading to the largest ever merger in the pharmaceutical industry. This four firm merger gave rise to a conglomerate internationally known as Glaxo-Smith-Kline and still known as Glaxo Wellcome Pakistan Limited in Pakistan. In Pakistan, Glaxo-Wellcome and Beecham are still two separately licensed firms and have not yet applied for a joint license.

The Monopoly Control Authority took suo moto notice of this merger as it was considered to have a significant impact on the pharmaceutical market structure and decided to examine the case.¹³ For this purpose, advice was solicited from the Pharma Bureau of Information and Statistics (PBIS) and Ministry of Health (MoH).

The MoH advised MCA to analyze the combined share of the merged companies along with the market share of their individual products. The reason for such an analysis was that the share of the undertakings may not be higher than the statutory limit of the Monopoly and Restrictive Trade Practices Ordinance (MRTPO) but the share of their individual products may well be above that limit. For example, on the one hand, Wellcome had 53.5% and 41.8% market share for two of its products and Glaxo had 60.6% market share for the production of Ventolins and on the other hand, the overall individual share of Wellcome and Glaxo was only 8.60% and 5.98% respectively.¹⁴ Thus, data regarding the nature and substitutes of individual products was to be worked out. Information was therefore called from the Pharma Bureau of Information and Statistics, Pakistan Pharmaceutical Manufacturers Association and the Ministry of Health.

2. Legal Issues

Monopoly Control Authority (MCA) is a statutory, quasi-judicial body established in its present form to administer the Monopolies and Restrictive Trade Practices (Control & Prevention) Ordinance, 1970. The broad objective of the legislation is to provide for measures against undue concentration of economic power, monopoly power and restrictive trade practices. The law spells out circumstances, which shall be deemed to constitute the above, and under **Section 3** of the ordinance prohibits these clearly defined situations.

The law under **Section 5** has prohibited creation or maintenance of unreasonable monopoly power in any market. Specifically under **Section 5(b)**, the law prohibits anti-competitive mergers and acquisitions. Such situations apparently are not very common at the present time, and the Ordinance permits the Authority to determine which of them should be prohibited.

According to the **Section 5** of the ordinance, (1) unreasonable monopoly power shall be deemed to have been brought about, maintained and continued if-

- (a) *there has been created or maintained any such relationship between two or more undertakings as makes them associated undertakings where they are competitors in the same market and together produce, supply, distribute or provide not less than (one third) of the total goods or services in such market;*
- (b) *there has been any acquisition by one person or undertaking of the stock or assets of any other person or undertaking, or any merger of undertakings, where the effect of the acquisition or merger is likely to create monopoly power or to substantially lessen competition in any market, including any acquisition which creates any such relationship as is referred to in clause (a).*
- (c) *any loan is granted by a bank or insurance company to any of the associated undertakings of amounts greater or on terms more favourable than for loans made available to other undertakings in comparable situations, or any loan is granted by a bank or insurance company to a person or undertaking not associated with it on the condition or understanding that the borrower or any of its associated undertakings will make any loan to a person or undertaking associated with the lender.*

13 The merger of two other pharmaceutical MNCs, Cyanamid Pakistan Ltd. and Wyeth Laboratories Pakistan Ltd. was also to be examined

14 Similarly, the total market share of Wyeth-Cyanamid Pakistan Ltd. was to be 4.7% after the merger, whereas, Cyanamid had 57% market share for one of its products, namely Antituberculosis.

(2) No such relationship, acquisition, merger or loan as is referred to in sub-section (1) shall be deemed to have the effect of bringing about, maintaining or continuing unreasonable monopoly power if it is shown-

- (a) *that it contributes substantially to the efficiency of the production or distribution of goods or of the provision of services or to the promotion of technical progress or export of goods;*
- (b) *that such efficiency or promotion could not reasonably have been achieved by means less restrictive of competition; and*
- (c) *that the benefits of such efficiency or promotion clearly outweigh the adverse effect of the absence or lessening of competition.*

Under **Section 11** of the Ordinance, in case of contravention of Section 3-

- (i) *where the authority is satisfied that there has been or is likely to be a contravention of the provisions of Section 3 and that action is necessary in the public interest, it may take one or more of such orders specified in Section 12 as it may deem appropriate.*
- (ii) *Before making an order under sub-section (1), the authority shall give notice of its intention to make such order stating the reasons thereof to such persons or undertakings as may appear to it to be concerned in the contravention to show cause on or before a date specified therein as to why such order shall not be made; and*
 - (a) *give the persons or undertakings an opportunity of being heard and of placing before it facts and material in support of their contention.*
- (iii) *an order made under the sub-section (1) shall have effect notwithstanding anything contained in any other law for the time being in force or in any contract or memorandum or articles of association.*

Under **Section 12** an order of the authority in case of unreasonably monopoly power—

- (a) *require the person or undertaking to divest himself or itself of the ownership of any stock or shares or other beneficial interest in any undertaking or of assets within such time and under such conditions as may be specified in the order;*
- (b) *require the person concerned to divest himself of any position held by him as an officer, director or partner in any undertaking within such time and under such conditions as may be specified in the order;*
- (c) *require the person or undertaking concerned to divest himself or itself of the management or control of any undertaking within such time and under such conditions as may be specified in the order;*
- (d) *prohibit the person or undertaking concerned from acquiring the stock or assets of, or the undertaking from merging with, any other undertaking;*
- (e) *limit the total loans which may be made by any bank or insurance company to any single individual or undertaking, or to any undertaking associated with such bank or insurance company;*
- (f) *limit the investments of any undertaking engaged in the banking, investment or insurance business;*
- (g) *require the person or undertaking concerned to take such actions specified in the order as may be necessary to restore competitive prices and eliminate restrictions on output or entry of competitors in the market.*

3. Analysis of the case vis-à-vis the Provisions

Glaxo Wellcome Pakistan Ltd. manufactures, exports and distributes pharmaceutical and animal health products. Since its merger in 1996, the profitability and the liquidity of the company has been increasing consistently. This is evident from a comparison of the company's key ratios with the entire sector's median over the three years from 1997-99 as shown below in the Table 1:

Table 1: Glaxo-Wellcome Pakistan Ltd's key ratio comparison with the Industry's average

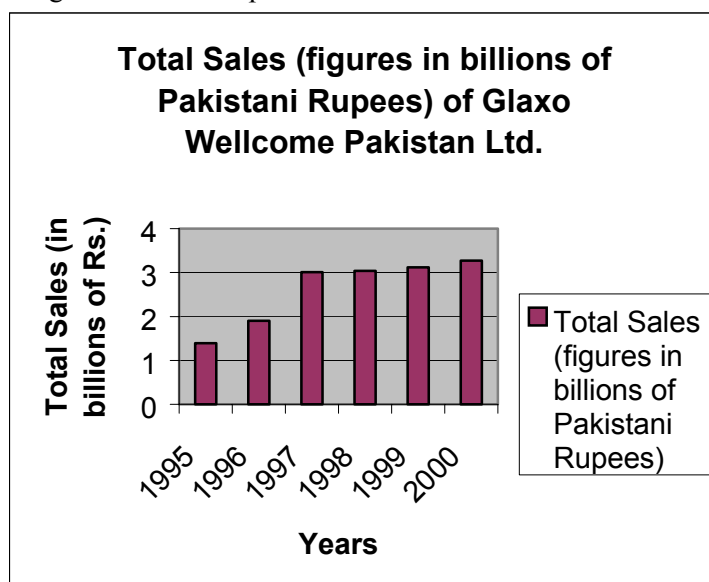
	1997	1998	1999	Industry Average
Current ratio*	2.31	2.60	2.84	1.57
Debt leverage	0.56	0.48	0.38	.83
Times interest earned	26.75	19.8	88.24	5.27
Net profit margin %	8.55	10.83	12.15	6.55
Return on equity %	15.39	19.85	19.21	15.39
Earnings per share(Rs)	7.23	10.63	11.31	5.2
Dividend per share(Rs)	3.5	4.0	5.5	--

Source: www.jang.com.pk/thenews/investors/jun2000/cc.html#1

Note: * Current Ratio = Current Assets/ Current Liabilities

The above table clearly shows that Glaxo Wellcome outperformed other firms in the industry during the subsequent years after its merger. This trend has continued in the recent past as well and during the year ending December 2000, sales at Glaxo-Wellcome Pakistan Ltd. increased 4.5% versus the year 1999. The total sales of the company as in December 2000 were reported to be Rs. 3.27 billion compared to the Rs. 3.12 billion in 1999. This was the fifth consecutive year of sales increases for the firm, and since 1995 sales have increased a total of 135%.¹⁵

The bar chart below gives a clear-cut picture of the increase in sales of the firm over the years:



The company's gross and net profits are also escalating every year. As Table 2 shows, between the year 1998-99 and 1999-00, the gross profit of the firm jumped from Rs. 565 million to Rs. 720 million. Information on the company's earnings before interest, taxes, depreciation and amortization (EBITDA) for 1999 and 2000 is also summarized in the Table below:

15 Source: <http://profiles.wisi.com>

Table 2: Gross and Net Profit of the firm for 1999 & 2000 (in million Rs)

	1999	2000
Sales	3123.45	3265.51
Cost of Sale	2558.07	2545.39
Gross Profit	565.38	720.11
Net Profit	379.58	501.85
EBITDA Margin (%)	18.10	22.05

From the statistics earlier cited, it is evident that the Glaxo-Wellcome merger has increased the market share of the firm tremendously. The merger seems to have strengthened the monopoly power of the firm, thereby, increasing the sales and profit of the company manifold.

This seems to be in confirmation with the **Provision 5(b)** of the MRTPO, which defines unreasonable monopoly power if the merger of associated undertakings creates monopoly power and reduces competition in the market. Under **Section 11** of the Ordinance, MCA issues show cause notices to the firm and gives the undertakings an opportunity of being heard. Under **Section 12(d)**, it has the authority to prohibit a merger with adverse impacts on the market.

4. Decision of the enquiry

Although, MCA took the initiative to investigate the merger and PBIS and MoH provided information in this regard, MCA failed to take any action against the merged companies and the matter was closed. There were a number of reasons put forward by the MCA on this account. Firstly, calculating the market shares of individual products along with the identification of their substitutes was a complicated task and the Authority lacked qualified staff for this exercise. For a thorough and careful analysis to address the issues involved in the determination of market shares data from reliable sources is required. This is an expensive and time-consuming task that MCA cannot afford.

Another consideration of MCA might have been that since MoH is responsible to look after issues relating to drug policy formulation and drug prices, therefore, MCA might not want to interfere in this Government regulated industry.

A close look at these justifications shows that they are unconvincing and unimpressive. The merger resulted in decreasing competition in the market and substantially increasing profits for the firm. Thus, it was the responsibility of MCA to complete the enquiry and take the appropriate actions. If the enquiry had shown an increase in efficiency of production, where the benefits of such an efficiency outweighed its adverse impacts on the economy, MCA should have allowed the merger and not taken any action against it. The way the case has been wrapped up without leaving a trace, clearly indicates political, bureaucratic and corporate pressures to close the case. This kind of behaviour is not very uncommon in developing countries where governments lack the courage to confront large multinational conglomerates. By their sheer size and lack of accountability to host governments, these multinational corporations can limit competition and reduce gains for the consumer and national economies of the developing countries.

5. Recommendations

Since the 1990s, closer integration of the global markets through liberalisation and globalisation have contributed to significant increase in mergers and joint venture activities through out the world. This worldwide merger activity has different implications for developing economies as mergers and tie-ups, even if taking place in the advanced economies, can adversely affect these developing economies. Whereas, jurisdictions in industrialised countries may object to any international merger activity on account of its welfare reducing effect on their economies, most of the developing countries simply don't have the regulatory infrastructure to voice their concerns. The international merger of Glaxo Group Ltd. and Wellcome Laboratories and their subsequent merger in Pakistan is an example of such a situation. Though the merged company grabbed a significant share of the market, yet no substantive action was taken against them. There do not seem to be any rules in the MRTPO, which would indicate how to deal with situations in which parent companies merge abroad, making any initiative taken by a body ambiguous and futile.

The presence of so many MNCs in an industry with mergers taking place between them over the years is some thing that goes against the interest of the general public in a developing country. Local companies find it extremely difficult to compete with these giants especially in costs and advertising campaigns. Though, with the passage of time, the combined market share of domestic firms is increasing, there does not seem to be any single local firm, which can successfully compete in size and resource utilization with these transnational firms. The Government of Pakistan has always patronized foreign firms to attract foreign investment. These companies pull different kinds of strings to maintain their control and though, the operation of these firms in Pakistan is a small percentage of their global operations, they are nonetheless remunerate.¹⁶

In order to investigate this case thoroughly and monitor the merger, a committee of MCA and MoH should have been set up. The combined effort of the two bodies would have had solved the problem of lack of qualified staff and would have helped collect reliable data even of individual products. At the same time, MCA should be given more powers to draft and implement its decisions. Not only theoretical but also practical independence is crucial for the Authority to have the desired image of a strong and impartial body.

Since the merger was of an international origin, the case should have been discussed with the Head Office of the company in UK. Furthermore, the accounting practices of these large MNCs should be duly checked as some information might be concealed such as via transfer pricing. The general stance taken up by pharmaceutical firms to defend their merger is that high cost of production and low profits have forced the manufacturers to merge or to close down their production. They also refute the allegations that they make fabulous profits. According to them, a look at their returns on equity gives the impression that pharma companies are involved in profiteering where as, in reality they are utilizing the resources in a better way and not over charging the consumers. However, these explanations need to be rigorously established.

An important point in this regard is the customs duty and sales tax on raw materials and finished pharmaceutical products, imposed by the Government. People living in developing countries are poor and as no adequate public health is provided, the medicines have to be bought by the patients themselves. The consumers ultimately bear the burden of taxes as the demand for medicines is usually inelastic. Therefore, in the public interest, the Government should exempt medicines from duties and taxes as these are essential items and their use cannot be avoided.

¹⁶ For example, in the recent extension of General Sales Tax (GST) to drugs, the MNCs managed to get relief by getting a 5% cut in import duties on materials.

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