

**Consumer Council**

**Submission to LegCo Panel on Food Safety and Environment Hygiene  
"Fresh Pork Supply"**

**Introduction**

1. The Consumer Council is pleased to provide its view on the allegations triggered by the price war on pork meat and to take part in the Panel discussion on ways to ensure economic efficiency through effective market competition.
2. The Council notes the recent concerns expressed by wholesale pork buyers regarding the substantial price reductions of supermarkets to undercut wet market retailers who purchase product from the wholesalers.
3. **The Council's primary concern in this matter is that consumers are able to make their food purchasing decisions in a fully competitive market that reflects low prices, wide product choices, and high standards of service.**
4. Reductions in retail prices are to be welcomed, and can reflect the dynamics of the market as market participants take advantage of emerging economies of scope and scale and adjust to changes in consumer demand. However, the Council notes that there have been intensifying concerns by consumers with an increase in market power of supermarkets, and with a possible decline in small retailers in wet markets as a competitive choice.

**Competitive Conduct**

5. The Council understands the dynamism of a fully competitive market is often complex. The manner in which markets develop can be distorted if any market participants use their market power, either unilaterally or through joint action, to undermine the competitive process. This will lead to long-term detrimental consequences for consumers. Certain short-term benefits for consumers might mask underlying structural distortions or anti-competitive conduct such as misuse of market power or collusive action.
6. In light of the information reported by the media and our information on hand of structure of fresh pork market, the Council is concerned with three issues regarding competition in the market:
  - Whether the two supermarkets lowered prices with the intention to limit competition;
  - Whether the bidding mechanism under Ng Fung Hong, the dominant supplier in the pork market, allows for price discrimination against any buyers that has an impact on market competition;
  - Whether the collective action taken by the fresh pork buyers, has an effect in reducing market rivalry and lessening competition.

7. The Council would like to set out some information for the Panel's consideration on its position in this matter.

### **Allegation of Predatory Pricing**

8. With regard to the allegation of anti-competitive conduct in the retailing of pork meat, the Council's understanding is that there is an allegation of below cost retailing by supermarkets, and that this is having a detrimental effect on competition for the product. This practice is commonly referred to as 'predatory pricing' and in the experience of competition authorities in other comparable economies that have competition laws is difficult to prove.
9. Leaving aside the question of what is the actual 'cost' and whether the retail price offered is below the measure of cost, the examination of this conduct must first begin with an assessment of whether the market participant engaging in the conduct has market power. This in turn requires an assessment of what is the relevant market in which there is power, and what is the relevant market where that power is being used to undermine the competitive process. For example, if a market participant that does not have market power is engaging in the pricing conduct, it will not likely be a concern.
10. Importantly, it also needs to be emphasized that the concern should not be to protect existing competitors but that the concern is firmly centered on whether the competitive process is being undermined to an extent that competitors are unable to participate in the market.
11. In general terms, taking advantage of market power is, in most cases, indicated where the firm has engaged in conduct which would not be profit maximising in a competitive market (i.e. in the presence of one or more efficient competitors and the constant threat of new entry).
12. In the context of predatory pricing, if a regulator examining the pricing conduct was to draw a conclusion that there was a competition concern, it would have to illustrate that
  - there is a high probability that losses being incurred in the 'below cost' pricing will be recouped within a reasonable period of time; and
  - that the conduct will have the effect of deterring entry and deterring any market participants that have survived, from engaging in price competition even when the predator has raised prices above cost in the recouping stage because the predator can use its market power to resort again to the predatory price. The end result being that consumer will pay higher prices.
13. This analytical approach is consistent with the Government's illustration of an example of 'predatory behavior' that may involve abuse of market position in its *Statement on Competition Policy* (paragraph 7(a)).

### **Supply Side Monopoly**

14. It has been stated to the Council by pork buyers' representatives that Ng Fung Hong controls around 90% of supply into the market and has practiced

discriminatory pricing, with a subsequent detrimental effect on the competition between wet markets and supermarkets.

15. An analysis of this issue begins with a similar approach to the allegation on the demand side. In other words, an assessment of what is the relevant market in which Ng Fung Hong operates and whether it has market power. If some buyers are given more favourable terms, the market power of those buyers would also have to be examined to ascertain whether the alleged price discrimination is being induced for anti-competitive purpose or effect. The study should therefore include an examination of market power on the part of suppliers and buyers, i.e. not only Ng Fung Hong, but also the pork buyers and major supermarket chains.
16. In examining the conduct of all parties, there needs to be a clear explanation of how market power is being *misused* through discriminatory pricing. Discriminatory pricing is more often than not a normal functioning of the market, which is reflecting economies of scale brought about through volume discounts, lower transaction costs etc.
17. The Government's *Statement on Competition Policy*, with some paraphrasing, also provides a basic test upon which the facts of the allegation can be tested in this regard. Paragraph 6(d), which relates to discriminatory standards, indicates that the impairment of 'economic efficiency' or 'free trade' is the basic test upon which discriminatory conduct should be tested.
18. Leaving aside the question of what 'free trade' actually means, the term 'economic efficiency' is a commonly used and understood term that can be used as a reference to gauge whether there should be a concern with the alleged discriminatory pricing.

#### **Collective Action by Fresh Pork Buyers**

19. Paragraph 6(c) of the Government's *Statement on Competition Policy*, states that horizontal agreements such as price-fixing and joint boycotts:

*"intended to distort the normal operation of the market, deprive supply or choice to the target of the boycott, and have the effect of impairing economic efficiency or free trade."*

may warrant more through examination.

20. It is acknowledged that co-operation on prices and supply arrangements among competing buyers would not of itself be anti-competitive. For example, if they are small firms whose major purpose behind the co-operation is to improve their competitive position rather than reduce market rivalry. In these circumstances co-operation may improve efficiency without hurting the interest of consumers.
21. The Council notes that pork buyers have currently bargained for favorable terms, and that their market power, as a collective group would not be insignificant. Their collective action therefore needs to be examined to ascertain whether:
  - (a) it has been used to force high prices at the wholesale level on the buyers' competitors (e.g. supermarkets); and

(b) this has resulted in prices at the retail level (for both wet markets and supermarkets) being higher than would otherwise be the case.

**Way Forward**

22. The Council is aware that COMPAG has asked the Environment and Food Bureau (EFB) to present a report and to examine the allegation of anti-competitive conduct, pursuant to the Government's sector specific approach to competition policy. The Council would be happy to assist in whatever way it can, and to contribute to the discussions of EFB's report.
  
23. As the market regulator, the Council believes EFB would have access to the necessary information that would assist its analysis of the above issues and therefore provide the public with a solution to this competition matter.

Consumer Council  
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