

## **Competition in the Supply Chain of Pork**

### **PURPOSE**

This paper summarizes the deliberations of the Competition Policy Advisory Group (COMPAG) in examining the competition issues in the supply of pork and the Group's conclusions.

### **BACKGROUND**

2. In early May, the two large supermarket chains lowered their retail price of pork. Pig buyers boycotted the auctioning of live pigs in the slaughterhouses on 6 May. This resulted in a suspension of supply of fresh pork at retail outlets on 7 May. To examine whether there was any competition issue that would require attention, COMPAG looked into the competition situation in the supply chain of pork, in particular the following questions –

- whether there was any monopolizing of pork supply;
- whether there was any abuse of collective market power by pig buyers; and
- whether predatory pricing was adopted by the two supermarket chains and whether there was monopoly of the retail pork market.

### **THE PORK MARKET**

3. There are three types of pork available in the market –

- Pork from freshly slaughtered pigs;
- Chilled pork – the pork is chilled immediately after the slaughtering process and is to be stored and displayed in chillers between 0° C – 4° C; and
- Frozen pork – the pork is frozen immediately after the slaughtering process and is to be stored and displayed in freezers at or below – 18° C.

The current market shares of the three types of pork are as follows :

Pork from freshly slaughtered pigs	51%
Chilled pork	3%
Frozen pork	46%

## **ORIGIN OF LIVE PIGS AND PORK**

4. There is no restriction on the origin of live pigs supplied to the Hong Kong market. The Government maintains a level playing field for any importer of live pigs, requiring all imported pigs to meet only the necessary health standards and sanitary requirements which are equally applicable to local pigs. Before 1988, places including the Mainland, Malaysia, Taiwan and Thailand had exported live pigs to Hong Kong while local pig farms have all along met part of the supply. In recent years, only the Mainland and local pigs remain in the market. The fact that live pigs from the Mainland have been able to win over the Hong Kong market from their competitors from South-east Asian countries was in itself an illustration of the existence of competition. There is also no restriction on the quantity of imported live pigs and live pigs supplied by local farms. Imported live pigs and local ones are free to compete for a bigger share in the local market.

5. Similarly, there is no restriction on the origin of chilled and frozen pork, subject to the necessary health standards and sanitary requirements. A number of sources are now competing against each other in the local market, including Thailand, Australia, USA, Brazil and Denmark and the Mainland.

## **THE IMPORT LEVEL**

### ***Live Pigs***

6. For the export of Mainland live pigs into Hong Kong, the Ministry of Foreign Trade and Economic Cooperation (MOFTEC) (對外貿易經濟合作部) has appointed NFH as the sole agent. There have been concerns that the sole agent status of NFH has resulted in virtual monopoly of the fresh pork market.

7. It is generally true that the larger the number of players, the more intense the competition will be. Should there be no sole agent, there may be a larger number of importers who will compete against each other.

However, it should be noted that although NFH does not face any competition as an importer of live pigs from Mainland, it still faces competition in the larger pork market as Mainland live pigs are not the sole source of pork for local people. There is also pork from local pigs, chilled pork and frozen pork, although the preference of some household consumers for buying pork from freshly-slaughtered pigs has given live pigs an edge over chilled and frozen pork. Nevertheless, consumers have the choice of turning to other sources for pork if the price of fresh pork from Mainland pigs becomes excessively high. In fact, other consumer groups including restaurants, Siu Mei shops, younger families and families with westernized habits have turned to use much more frozen or chilled pork in lieu of fresh pork in the recent years. This is evident from (i) the decrease in the number of live pigs slaughtered despite the increase in population; and (ii) the increase in the volume of frozen and chilled meat imported.

8. The sole agent system in respect of the export of livestock is part of the Mainland's economic and trade policy. Moreover, NFH itself has not adopted any anti-competitive practice. We therefore do not consider that there is strong justification to suggest the abolition of the sole agent system.

### ***Chilled and Frozen Pork***

9. The import of chilled and frozen pork, as in the case of live pigs, is free from restrictions except for the necessary hygiene and sanitary requirements. The Hong Kong market is open to all suppliers.

## **THE AUCTION/WHOLESALE LEVEL**

### ***Live Pigs***

10. There is no formal wholesaling of live pigs as such. Live pigs from the Mainland and 50% of local pigs are auctioned at the slaughterhouses every day. (The other 50% of local pigs are sold by local farmers to pig buyers or pork retailers on farm.) However, the role of pig buyers in the slaughterhouse is, to some extent, similar to that of a wholesaler. A pig buyer may be appointed by a number of retailers to procure pigs through auctions. Each retailer may only require a small number of pigs. In the auction, the pig buyer procures the total number of pigs he needs for distribution and distribute the pigs amongst the various retailers appointing him, thereby indirectly assuming the role of a

wholesaler.

11. There have been concerns that the abuse of collective market power by pig buyers hinders free competition in the pork market and inflates the price of fresh pork. COMPAG acknowledged that collective/collusive action taken by any group of trader to maintain the price of a commodity at a certain level, including the boycott action taken by pig buyers in May 2002, is anti-competitive.

12. COMPAG believes that an effective safeguard against such collective/collusive action succeeding in reducing the room for competition is the absence of restriction to entry to the trade. As long as there is no barrier to entry, traders who took collective/collusive action would not achieve their aim as others would enter the trade and fill the place when there is demand. In the case of pork, while in the recent price war over pork most pig buyers have acted collectively for a short period (one day), the system is not conducive to the sustained success of these actions because –

- Retailers are not bound by any rule to appoint a pig buyer. The daily auction at the slaughterhouses is open for all to attend. In fact, some retailers do attend the auction themselves to procure the pigs they need. The hiring of the service of pig buyers is only a practice which meat retailers have found expedient over the years. The name of the successful bidder and the price of each lot of live pigs are made known immediately after the bidding. This ensures that the auctioning is conducted fairly.
- There is no discriminatory restriction on who can become a pig buyer. Any person can offer his service as a pig buyer to meat retailers.
- Some local farms and meat retailers negotiate business deals themselves without involving pig buyers. In these cases, pig buyers only help to arrange for the delivery of live pigs ordered by meat retailers from farm to slaughterhouse.

Should there be similar incidents in the future, retailers may enlist the service of buyers who do not join the action or newcomers may emerge to fill in the service gap left by pig buyers who take collusive action to adversely affect the trading. Retailers may even organize themselves to

co-operate in the auction to eliminate the need for the service of pig buyers.

13. There are also concerns about the potential for manipulation of prices given that NFH provides product into the downstream live pig market and its subsidiary company, Shing Lee (Meat Supplies) Hong Limited (SLH), also operates as a buyer in that market in competition with others. COMPAG notes that although in theory the possibility of price manipulation exists, any attempt at such anti-competitive act would only be successful if SLH first attracts a considerable number of pork retailers to form business deals with the company so that the pigs it successfully bids at however high a price would have recipients at the other end. In reality this is unlikely to happen because retailers who have appointed SLH as their agent are free to engage the services of other pig buyers or participate in the bidding themselves if the prices at which SLH bids for pigs are too high. Again the system is not conducive to the success of any attempt at price manipulation.

14. The distribution chain of chilled and frozen pork is similar to that of other commodities. There is no indication of anti-competitive practice in the trade of chilled and frozen pork.

## **THE RETAIL LEVEL**

### ***Pork from freshly slaughtered pigs***

15. There have been queries as to whether the two large supermarket chains have adopted a strategy of predatory pricing, i.e. selling below cost of the purpose of driving out competition followed by substantial price increase. At this stage, we cannot find evidence to substantiate the suspicion, as –

- It seems unlikely that the supermarket chains are selling below cost. From our observations on the price at which live pigs were sold to the supermarkets and other costs involved in the process prior to sale, the supermarkets are likely to be selling at a narrow profit margin rather than below cost.
- The two supermarkets' market share was about 5% before they lowered the price of pork. After the lowering of pork price, their market share increased to around 15%. Realistically they cannot

aim at claiming a lion's share of the local pork market within a short span of time.

Even if the supermarkets practise predatory pricing, they are not likely to carry it through, as any significant price lift after an initial price lowering would induce market stalls for selling fresh pork to re-enter the market, given that there is little barrier to entry.

16. Chilled and frozen pork is mostly sold by supermarkets and fresh provision shops specializing in frozen and chilled meat products. The retail practice is normal. There is no indication of anti-competitive practice.

## **CONCLUSION**

17. According to the Statement on Competition Policy, in assessing whether a business is anti-competitive, the determining factor is "whether a business, through abusing its dominant market position, is limiting market accessibility and contestability and giving rise to economic inefficiency or obstruction of free trade to the detriment of the overall interest of Hong Kong." In the local pork market –

- There is a free play of market forces. There is no restriction on the origin of products and the Government maintains a level playing field for all at the import, wholesale and retail levels;
- The collective boycott action of live pig buyers in May 2002 was an anti-competitive practice, but conditions are not favourable for such anti-competitive practice or to be carried through or to sustain; and
- There is likely to be a higher degree of competition in the trading of Mainland live pigs (hence fresh pork) if there is more than one importer. However, other types of pork are available and NFH does not have a monopoly in the pork market. NFH has also not adopted any anti-competitive practice.

We therefore conclude that there is as much competition in the local pork market as the Government can foster. It is not necessary for the Government to take any action to intervene in the operation of market forces.

18. Nevertheless, it is recommended that the Government should observe closely the following areas –

- The operation of NFH and SLH to ensure that there will not be any collusion or arrangements between the two companies that are to the disadvantage of other buyers on the bidding floor;
- Any change in the rules of live pig auctioning to ensure that the trading of live pigs at that level is fair for all competitors;
- Prices offered/set by all market participants at all levels to ensure that there is no anti-competitive practices such as predatory pricing or collusion amongst members of a trade that aims directly or indirectly at maintaining prices at a certain level or forcing other players out of the trade.

**Competition Policy Advisory Group  
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