

## Canadian Perspective on Competition

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### INTRODUCTION

The authors set out to test (i) whether larger markets result in greater concentration and (ii) whether greater concentration increases the exercise of market power. The empirical work of James Rude and Murray Fulton to test these factors for Canadian agribusiness is based on the structure-conduct-performance (SCP) approach. We appreciate their effort and the importance of empirical work on the subject using data from the free trade era.

Our comments are organized as follows: First, we provide a brief summary of their paper. Second, we indicate from the antitrust perspective the importance of concentration in market power analysis. Third, we give our reservations with regard to their testing of the concentration and market power hypothesis.

### A BRIEF SUMMARY OF THE PAPER

The study examines the impact of increasing the size of the market on concentration. A larger market should lower concentration and prices. This proposition is in the context of examining the impact of trade liberalization which would increase the size of the market. The authors then examine evidence on concentration for the period prior to the Canadian-United States Trade Agreement (CUSTA), 1983-1988, and for the period following the signing of the Agreement, 1989-1996, when the market was supposedly larger.

Their principal result is that there is no significant change in concentration between the two periods. Only two sectors have a decrease in concentration. There is an increase in concentration for some industries. Decreases

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\* The views are those of the authors and not necessarily those of the Competition Bureau, Industry Canada.

are probably not the result of trade liberalization. Increased concentration is attributed to factors such as supply-management, transportation costs and tastes. There is therefore no relationship between increasing the size of the market (or trade liberalization) and concentration.

The study then examines whether concentration leads to increased market power. The authors do not detect a statistically significant relationship between concentration and performance. This is similar to the past results of many SCP studies. The authors found a statistically significant positive relationship between concentration and market power but there is generally a lack of relationship between trade liberalization and markup, except in three sectors.

## **AN ANTITRUST PERSPECTIVE ON CONCENTRATION IN MARKET POWER**

Rude and Fulton have treated broad sectors as product markets. The geographic market is always Canada. As antitrust practitioners we have a different view of market definition. Product markets are defined to determine which products are demand-side substitutes. These are products that are reasonably interchangeable by consumers for the same purposes when price, use, and qualities are considered. Geographic markets are defined by determining the location of firms that produce the same product to determine supply-side substitution. This is the area where customers can turn to other suppliers and transportation costs may be the determining factor.

The Standard Industrial Classification (SIC) is the system used to collect and analyze data on the activities of firms. The SIC classifications do not correspond to antitrust economic markets. In a properly defined antitrust economic market we know that concentration will be a good proxy for market power. We define antitrust markets by asking if a hypothetical monopolist could increase prices by, say, 5 percent in the proposed market. The SIC classifications have product markets that are either too broad or too narrow. The geographic market suffers from the same defect. For example, potato chips might be part of a broader snack products market. Should soft drinks be treated as a separate product market? We thought so and found many geographic markets in Canada based on the location of plants and the shipment patterns of bottlers.

**Table 1: Mergers in Agriculture and Agri-food, 1986-2000.**

86/87	87/88	88/89	89/90	90/91	91/92	92/93	93/94	94/95	95/96	96/97	97/98	98/99	99/00
7	29	20	20	22	24	15	8	13	20	22	27	22	23

Source: Monteiro, Joseph, Statistics on Canadian Mergers Examined By The Competition Bureau (1986-1998), *Canadian Competition Record*, Winter 1998-1999, pp. 64-71.

We think that the inconclusive statistical results flow from these problems and the use of the SCP model. The discussion of the results in the paper makes a compelling case for addressing the issues at a lower level of aggregation. Rude and Fulton note that Heinz has a monopoly in jarred baby food in Canada. We can add that this is due to Heinz winning an antidumping case against Gerber. The Canadian sugar industry, which is a monopoly-duopoly, also won a dumping case against the United States and others in 1995, and now faces no import competition. The authors can cut and simplify the discussion on entry barriers and sunk costs by linking it to the Herfindahl index. We can presume that in industries with a low Herfindahl these are not important.

## DATA ISSUES AND CONCLUDING REMARKS

A number of mergers have occurred after 1996 in the agribusiness sector. From our records, mergers that have been reviewed by the Competition Bureau are shown in Table 1. In other words, one-third of all mergers in the agribusiness sectors has occurred in the years after 1996 in comparison to the mergers that have occurred in the previous ten years. Without commenting on the significance of these mergers, had a similar study been done with regard to telecommunications we would have had no hesitation in indicating that the results would have been affected significantly if the last few years were omitted.

The authors have made a good attempt to investigate whether the agribusiness sector is becoming more concentrated in Canada and whether increased concentration leads to more market power. Their results should be interpreted with caution. Their research we hope will stimulate further work in this area at a more disaggregated level.