



COVID-19 Excessive Pricing or Price Gouging- the South African Experience

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Treatment of excessive pricing in South Africa

- The law prohibits dominant firms from charging “excessive prices” to the “detriment of consumers and customers”
- Up until 2018, an excessive price was a price which bears no reasonable relation to economic value
- The question of which price corresponds to economic value was put to the test in two key cases

Case 1: Mittal Steel

Conditions:

1. Mittal had a quasi-monopolistic position protected by important entry barriers (also, in small economies unlikely that new entry occurs in sectors characterised by large sunk costs).
2. A former public monopolist in flat steel
3. No sectoral regulator
4. Difficult to devise easy remedies to facilitate entry

- Complaint alleged that Mittal was selling its flat steel products at excessive pricing

Decisions:

- The Tribunal found that Mittal was super-dominant
 - Its import parity pricing was evidence of excessive pricing
- On appeal, the Competition Appeal Court set aside the Tribunal’s decision and remitted the matter back to the Tribunal for determination
 - The matter was then settled out of court

Case 2: Sasol Chemicals

Conditions:

1. Sasol Chemicals, a successor to a state-owned firm and had benefited from state privilege favours, just like Mittal Steel
2. No sectoral regulator
3. Difficult to devise easy remedies to facilitate entry

- Complaint alleged that Sasol was excessively pricing purified propylene and polypropylene

Decisions:

- The Tribunal found the price charged by Sasol was excessive pricing
- On appeal, the Competition Appeal Court reversed the decision of the Tribunal and found the prices in question not to be excessive

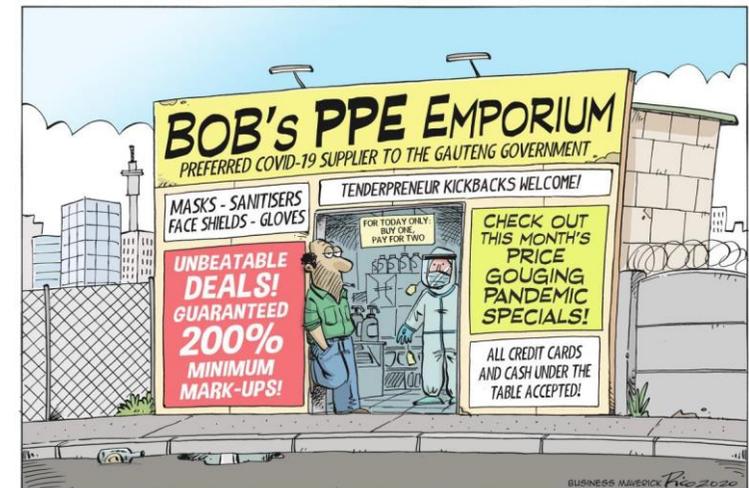
Treatment of excessive pricing in South Africa

- Unhappiness about the outcomes of the Mittal and Sasol cases, led others to argue that the law on excessive pricing needed to be refined
- In 2018, the excessive price prohibition was revised, important changes were made on the “definition of excessive price” and the “burdens of proof”
- **Economic value** replaced with a **price which is unreasonably higher than a “competitive price”**
- The revision added some indicative factors, but not a closed list, to be taken into account including:
 - Price cost margins, internal rate of return
 - Prices charged (by the respondent or relevant comparator firm) in similar but competitive markets
 - length of time the prices have been charged at that level
 - Structural characteristics of the relevant market
 - Any regulations made by the Minister regarding the calculation and determination of an excessive price
- On the burden of proof, if there is a prima facie case that a price charged by a dominant firm is excessive, the onus shifts to the respondent to prove that the price is reasonable

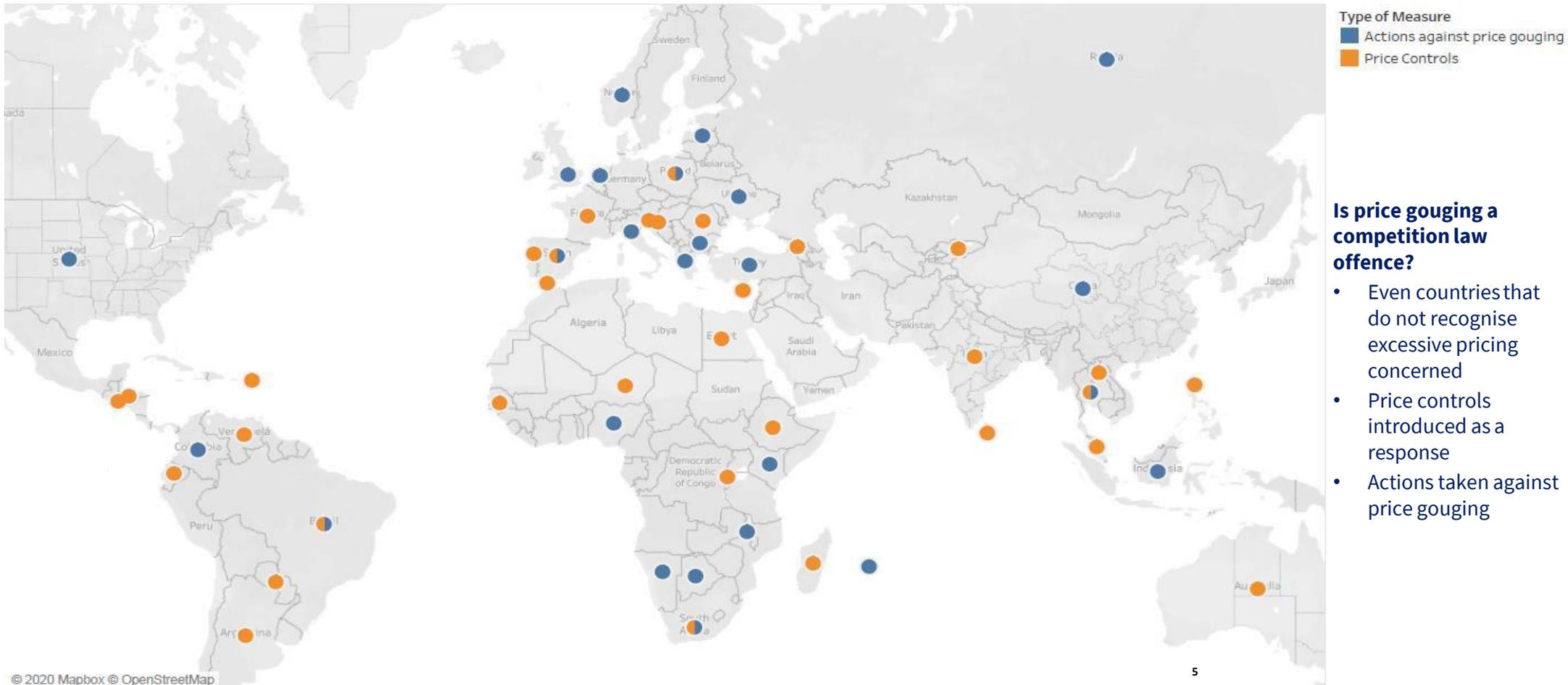
2020, an extra ordinary year

Covid-19 out-break

- January and February 2020
- Although no case reported in South Africa, demand for consumer products such as hand sanitizer, cleansing wipes, and toilet paper suddenly spike
- Those who could afford stock piled, those who could not afford went without
- Public outrage at the dramatic increase in price for personal protection equipment (PPE)
- **Moral reasons drove the public outrage**
 - High prices characterised as unfair, occurring in the anticipation of a Covid-19 crisis
 - Amoral sellers (profiteers) gaining at the expense of the poor consumer
 - High prices seen as “forced on poor consumers”, consumers have no choice {PPE anticipated would be a life necessity}
 - PPE seen as critical goods, unfair that the rich will be able to acquire but not the poor
 - Amoral profiteers not adding an value to the transactions



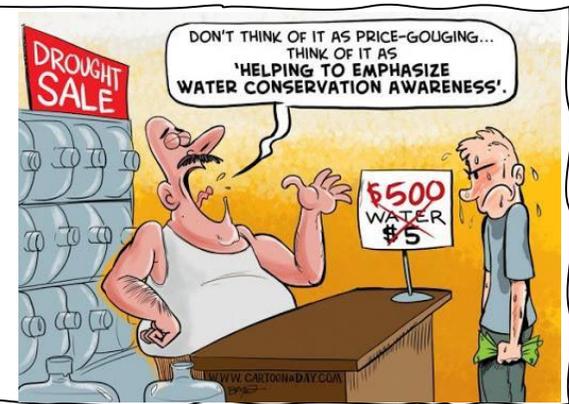
SA, not alone in expressing concern about price-gouging during the Covid-19 pandemic



The case for and against price gouging prohibitions

- **Case against price gouging prohibition**

- Price gouging prohibition sets a price cap
 - Prices lose some of their ability to function as an incentive for and a signal to buyers and sellers
- Price gouging is an efficient and desirable market response that brings demand into line with supply
 - Price gouging means that those who value the product most highly are the ones who buy it (demand)
 - The high prices signal scarcity and encourages suppliers to increase supply (supply responses)

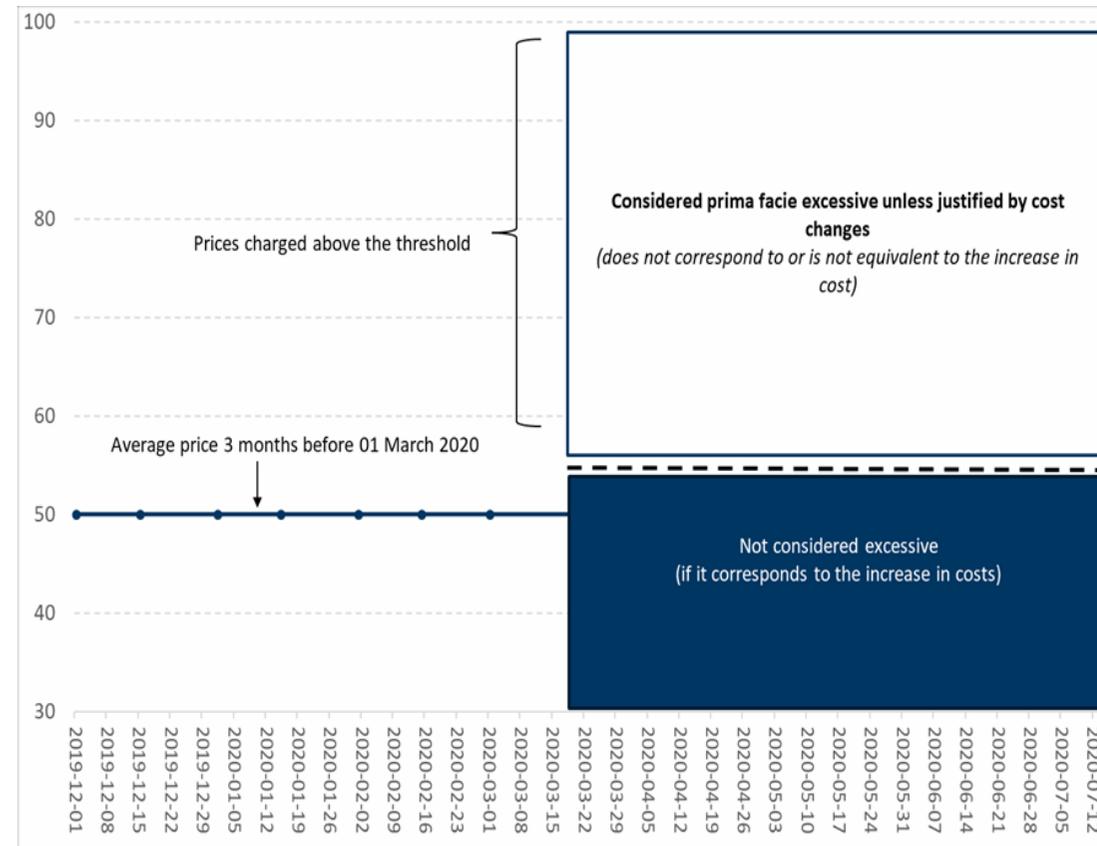


- **Case for price gouging prohibition**

- For critical or essential goods such as food or PPE, it is unlikely that there is a large variation in the value consumers put on the products
 - But if income differences largely drive willingness to pay, outcomes observed as result of price gouging do not represent a socially optimal allocation of goods, but only the inability of the poor to pay
- High prices do not have an effect on quantity, to the extent that they reflect hoarding this is a signal that demand will decline afterwards

Price gouging and competition law in South Africa

- **First Covid-19 case reported on 5 March 2020**
- **On 15 March 2020**, South Africa declared the COVID-19 pandemic a National Disaster in terms of the Disaster Management Act No 57 of 2002
- On 19 March 2020, the Minister of Trade and Industry published Consumer Protection Regulations
- **Consumer protection regulations**
- The regulation states that a price will be *prima facie* excessive:
 - if there is “**a material price increase**” on a specified good or service during the specified period which, either -
 - a) does not correspond to or is not equivalent to the increase in the cost of providing that good or service, or
 - b) increases the net margin or mark-up on that good or service above the average margin or mark-up for that good or service in the three-month period prior to 1 March 2020.



Leaving no stones unturned: the case against Babelegi



- Babelegi sold dust masks to industrial customers
- It had a market share of less than 5%
- Between 31 January and 5 March 2020, Babelegi alleged to have engaged in excessive pricing
- Conduct took place before **Consumer Protection Regulations**
- Under South African law,
 - firm presumed to be dominant in a market if mkt share = 45% or more
 - firm with than 35% mkt share but has market power can be found to be dominant in a market

• Tribunal decision

- Babelegi is dominant because it has market power
 - “successively and boldly increased its mask prices during this period, thus behaving to an appreciable extent independently of its competitors”
 - Infer market power from the behaviour of the firm (market definition not necessary)
 - Emphasised the context of a pending Covid-19 outbreak
- High mark ups during the month of February evidence of a prima facie case of excessive prices (retail pricing)
- High prices to the detriment of customers and consumers

Table 1. Prices and markups of facial mask markups earned by Babelegi between December 2019 and March 2020

Sequence of events	Cost per box (Rand)	Cost per mask (Rand)	Selling price per box (Rand)	Selling price mask (Rand)	Markup (%)
9 December 2019	41	2.05	50.60	2.53	23
31 January 2020	41	2.05	91	4.55	122
4 February 2020	41	2.05	85	4.25	107
10 February 2020	41	2.05	350	17.50	753
5 March 2020	41	2.05	500	25	1120
18 March 2020	440	22	550	27.50	25
26 March 2020	440	22	550	27.50	25

Source: Competition Commission referral to the Tribunal on 9 April 2020.

See Ratshisusu and Mncube (2020), Journal of Antitrust Enforcement

- Competition Appeal Court decision pending
- The case was heard on 4 September 2020



Leaving no stones unturned: the case against DisChem

- A pharmaceutical retailer, with presence through out South Africa
- Sold surgical masks
- Commission alleged that in March, surgical masks were excessive
- The price increases at play for three different categories of facemasks were 261%, 43%, and 25%, and occurred around 9 March 2020
- *Conduct took place before Consumer Protection Regulations*

- **Tribunal decision**
- DisChem is dominant because it has market power
 - Infer market power from the behaviour of the firm (market definition not necessary)
 - Dis-Chem was able to materially increase its prices in the context of a global health crisis independently of its competitors, customers or suppliers
 - The public had been encouraged to wear a surgical mask in March

- High mark ups during the month of March evidence of a prima facie case of excessive prices
 - DisChem increased prices in March (compared to prices prevailing in January and February) without a direct link to cost increases (retail pricing)

- High prices to the detriment of customers and consumers

- DisChem has chosen not to appeal the Tribunal case, concern about the harm to its brand, even it does not think that it priced excessively

Pouncing at every shadow? settlement agreements

To date about 38 settlement agreements concluded

Products range from face masks, hand sanitizers, to food items maize meal (staple food) and chicken eggs

Firms who have settled are all small firms most have not admitted guilt {**questions on whether any of the firms is indeed, truly, a dominant firm**}

Fines have been very “very” small, in most cases linked to the size of the overcharge

• **Product: chicken eggs**

- A community-based butchery, **Mzansi Meat and Chicken** alleged to have excessively priced its 5-dozen large- and medium-sized eggs in contravention of the Regulations
- The butchery agreed settlement terms with the Commission:
 - which included making a monetary contribution of **R 12 000 {612 Euros}** to the COVID-19 Solidarity Fund
 - immediately desisting from excessively pricing the items concerned
 - reducing its mark up on those items to an agreed percentage for the duration of the national disaster

• **Product: Dust face masks**

- Auction and Salvage Net alleged to have made excess profits amounting to **R9 521.74** in March 2020
- Gross profit margin was 29.2% seen as unreasonable
- Settlement requires the respondent to donate R9 521.74 to the Covid-19 Solidarity Fund

• **Product: Hand sanitisers**

- Evergreens Fresh Market sold a total number of 45 units of 500ml bottles of Alphasel hand sanitisers to its customers for R189.95 each, and made a gross profit of **R2 855.25** during March 2020
- Mark-up on hand sanitisers is 50.1% and gross profit margin of 33.4% for March 2020, respondent maintains that 33.4% margin is consistent with other products
- Settlement requires the respondent to donate hand sanitisers amounting to the value of **R1 800.00** to the Tembisa Provincial Hospital

• **Product: 25kg Maize Meal (staple food)**

- Commission –using historic profit margins – finds that **Cambridge Food** charged excessive prices for maize meal without any corresponding increase in costs
- Without admitting liability and in order to avoid protracted litigation and costs, Cambridge Foods concludes a settlement agreement
- Cambridge Foods agrees to donate essential goods to the value of **R 24 947 {1 272 Euros}** (being a value related to the alleged overcharge) to a community-based project

Discussion

- While the DisChem and Babelgi cases are about South African competition law, they are not just about South Africa....
- The cases raise important issues on the concept of dominance
 1. The Competition Act relates the concept of dominance to “a market”, is the Tribunal’s approach of disregarding market definition appropriate [even in the Covid-19 context]
 2. Do substantial price increases, for a short period of time, indicate dominance or substantial market power?
 3. If the price increase itself indicates (a) dominance, (b) excessiveness and (c) detriment to customers or consumers; then it seems that the dominance requirement is no longer a limiting factor on the prohibition of excessive pricing
 4. The Tribunal in the Babelgi and DisChem cases tries to introduce an “abnormal circumstances relating to the Covid-19 crisis” as the important imitation to its approach, it is not clear whether the Competition Appeal Court will endorse this approach
 5. Questions remain on whether the Tribunal will apply the same principles to other disruptions, e.g., an increase in the demand for ice cream during one very hot month
- South African competition law has multiple goals, including low prices and ensuring the ability of small firms to participate in markets
 - The cases raise importance of low prices to consumers in competition law but also important trade-off issues (concern about small firms)

Discussion

- Equity, justice and competition law, is there a moral side of competition law
 - Tribunal condemned Babelegi's prices as "reprehensible," exploiting customers "amidst a crisis when these customers are at their most vulnerable and their choices limited." Should justice and equity be part of the competition law assessment, together and in equal standing to efficiency
- Should we tolerate short term market failures, even when they are exploitative? The Babelegi and DisChem cases suggest, No
 - In Babelegi, the Tribunal wrote that "competition authorities are, at times of crisis and instances of exploitative price abuse, duty-bound to act."
 - In DisChem it noted that a "competition authority might be in dereliction of its duty if it did not intervene in a timely manner in states of natural disasters or emergencies to protect vulnerable consumers against exploitative firms. Take for instance a natural disaster such as a severe drought in South Africa. How long should a competition authority wait until the market "settles" or reaches equilibrium before it intervenes to protect consumers against pricing abuses by the suppliers of fresh or bottled water?"



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