

Sector Inquiry: A Glimpse Into the Cement Industry by the Turkish Competition Authority

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The Turkish Competition Authority ("**Authority**") published its final report into the cement sector ("**Report**") on its website recently. The Report sheds light on future enforcement by the Competition Board ("**Board**"). Although it is not possible to directly attribute the Report's conclusions to the Board at this stage, the report could be seen as an idea generator for future Board practices. The Report could also have an impact on the depth of future preliminary investigations and investigations. This article provides a brief summary of the Report.

The sector inquiry was not conducted to pinpoint specific competition law violations by a particular undertaking, or a group of undertakings. Rather, the Report aims to make a competitive analysis, reflecting the long-term and holistic view of the market structure, as well as behaviors of independent market players in many different aspects, based on micro data-sets taken from undertakings and customers.

1. Cement Sector and Competition Authority Experience

The Report outlines the structure of the cement sector in Turkey and in the world, as well as development of competition law processes in this sector, including discussion of past Board decisions. Particularly noteworthy are explanations of sector characteristics and problems which have influenced Board determinations during investigations, as well as approaches taken against these problems.

Seasonal Sales and Relation with Pricing

The cement sector has a periodic demand structure, noted in the Board's past decisions. It was found that demand reduces in September-October and revives in March-April. Investigation defendants frequently argue that price increases related to periodic demand changes and were caused by economic necessity. Nevertheless, the Report concludes that in the Board's violation decisions, prices did not line up with the demand pattern. Rather, the Board found that when demand decreased, there was no relative price reductions and the upward movements of price periods were independent of the demand pattern. Therefore, the Board found that investigation defenses based on the periodic demand structure were not established upon satisfactory economic basis and the Board places low weight on hypothetical defenses which ignore other information and documents.

"Maverick" Firms

"Maverick" firms cause discomfort to market players which are motivated to make agreements on anti-competitive issues. Attempts can be seen by other companies to take the maverick out of the market. If this is not possible, attempts are seen to convince the maverick be part of an anti-competitive agreement."

Vertical Integration and Manipulation of the Ready-Mixed Concrete Market

Vertical Integration within the cement market or ready-mixed concrete market can introduce uncertainty about whether a price or region sharing agreement exists. Cement producers show a tendency to make horizontal agreements in the classical sense. The ready-mixed concrete market can be manipulated via the power derived from the vertically integrated structure. It is possible to increase the price or profit levels in the ready-mixed concrete

market by limiting the competitiveness of producers which are not operating in the cement market. Therefore, it is important to consider cumulative effects when examining the cement or ready-mixed concrete market, as well consider changes in price or cost.

Customer Sharing and Unusual Price Movements

The nature of customer sharing produces the same economic results as price determination. Therefore, almost all Board decisions inspected customer sharing and price determination claims together, examining price levels in this context. When evaluating extraordinary pricing claims, the Board considers whether price changes can be explained by economic and rational reasons. It considers whether the price change can be explained by parameters such as cost, capacity, stock quantities, demand structure, general economic indicators, growth, and external markets affecting price formation. In other words, the Board does not directly consider a price increase alone to be a violation. The Board does not accept seasonality defenses regarding price changes. Rather, the Board reaches a conclusion by using all inspection and evaluation tools available.

New Entrances to the Market and Entry Barriers

The Report notes that the cement industry's problematic competitive issues create entry barriers to the cement industry, inhibiting new entries in a sufficient, timely and predictable manner. The Report notes both economic and legal entry barriers.

2. Economic Analysis of the Cement Industry

The report analyses four economic aspects of the cement sector.

a. Statistical Industry Analysis

National

The Report notes that:

- Between 2010 and 2014 (excluding 2012) the cement sector grew well above both the Turkish economy and the construction sector.
- After 2013, the cement price inflation is clearly above the inflation rate.
- There is no direct reflection of the seasonal demand on cement prices.
- Production and sales follow a parallel course but production is always more than sales. Therefore, there is a supply surplus and a positive stock situation.
- Prices have risen above inflation, excluding a price decrease between the end of 2012 and the beginning of 2013.
- Price levels are not directly related to cement sales (demand), seasonality and supply surplus in general terms.

City Based

A key Report finding is that there is no clear positive correlation between price and concentration in the cement sector. Even when the concentration level is relatively low, price levels remain close to those in high concentration observations.

The report concluded that:

- By examining graphics / charts combined with the market concentration for undertakings and price level, it is seen that the market shares and power of undertakings is low at a national level. However, this reflection changes in favor of certain undertakings in certain cities.
- Significant differences exist for concentration levels between cities.

- The level of concentration may have been negatively affected by the number of undertakings making sale to the cities. However, this effect is quite invalid for some cities.
- There is no clear positive or negative correlation between the concentration level, the number of undertakings, and the average prices in the cities.
- Price differences within the same city may have increased due to the rise in number of undertakings selling to the same city.

Undertaking Based

The Report notes that:

- City-based shares of undertakings are highly variable. These shares can be used to interpret the market power of undertakings in particular cities.
- In terms of production, the first five undertakings generally realize 50% -60% of market production.
- Each city is dominated by a certain undertaking.
- The number of cities where a particular undertaking conducts sales activities is usually limited to 10-20 cities (but can exceed 50).
- Determinations can vary for bulk and bagged cement, but have not changed much over the years. This will be a sign of stability in the market.

Product Based

The Report notes that:

- Bulk cement is sold more than bagged cement.
- At least 60% of cement sales per year are bulk cement.
- The price of bulk cement is higher than bagged cement.
- There is high degree of similarity in price trends for certain (but not all) bulk cement products.
- Price movements for differentiated bagged cement products are very close to each other.

Client and Client Type Based

Purchase differences were detected for different groups of customers: dealer, industrial, contractor, ready-mixed concrete plant etc.

The Report notes that:

- While the customer range for bulk cement is primarily ready-mixed concrete facilities, bagged cement is mostly sold through dealers. Dealers occupy a considerable customer share for undertakings, but the largest customer group for several undertakings is ready-mixed concrete plants.
- Customer types preferred CEM I 42.5 and CEM II 42.5 products. However, some customers use these products in a very intensive way and some purchase a wider range of products.
- Similarities in price movements are seen over time. However, prices can be quite close to each other and quite different and/or high prices may be offered to customers. For example, offered to rival ready mixed concrete facilities, public sector or non-governmental organizations.
- Most customers purchase from a single company (particularly for bagged cement).
- Almost half customers use only one product. However, rare cases exist with customers purchase up to 12 products.

b. Price-Cost-Demand Analysis

The report demonstrates that there is no strong correlation between prices and costs. It noted that recent price changes are rarely and very little effected by cost changes. Past costs are insufficient for many cities to influence today's price.

The Report states:

"Price changes are mostly affected by past period price changes and it is not possible to observe a clear relationship between price and cost changes in both long term and short term. Therefore, on analysis, it was not possible to observe a positive relationship between the economic sense and theoretically expected price and cost, and it was observed that the relationship was often negative. This means that if an undertaking reduces the costs of cement production, the prices will not always decrease relatively, but may even increase."

The Report goes on about the relationship between price and demand:

"There is no long-term balance relationship between price and demand in cities outside Hatay and Karabük. In particular, it is emphasized that the effect of current and past demand changes cannot be observed on prices in important consumption regions such as Ankara, İzmir, Antalya, Adana, Mersin, Diyarbakir, Trabzon."

c. Joint Pricing Analysis

The Report emphasizes:

"The term "Joint Pricing" used in the report is not referring to any claims or evidence of violation, the term is only used to emphasize that firms are maximizing their profit in any kind of togetherness. In this sense, pricing behaviors can originate from oligopolistic dependence and rational preferences, as well as concerted practice or agreement between undertakings."

"By the use of econometric models in the analysis of the Joint Pricing behavior, real prices were compared with the hypothetical prices that would emerge as the result of hypothetical alliances of cement firms aiming to maximize their profits together."

"It can be said that the common behavior in the sector in terms of the cities and years is Joint Profit Maximization. It can therefore be argued that the price levels observed in the cement industry in recent years are above the price levels that are expected for oligopolistic competition in general, with the exception of some observation areas in this section. Although it can be said that the general reflection in terms of economic analysis is Joint Profit Maximization, on the other hand, from the legal point of view, it is not in terms of the sector inquiry made within the scope of this study to say which way the form of behavior emerges. Joint Pricing behavior may have emerged as a result of rational preferences within firms' oligopolistic dependency, as well as through Competition restrictive agreement or concerted action."

d. Efficiency and Competition Analysis

The Report calculates an efficiency score using bulk CEM I 42.5 production and input cost data for the production of this product alone, as well as the total gray cement production and the input cost data for this production.

The average variable costs are calculated for the same period as the efficiency scores. When compared, it was found that there was a negative relation between them. Accordingly, the average variable costs decrease as the efficiency scores increase.

3. Conclusion

The Report presents the following conclusions:

- The results of the analysis show the existence of competition problems which have been pointed out by the Competition Board's decisions in the past years. However, it is beyond the Report's scope to determine whether the issue is due to claims of competition violation expressed in complaint petitions, or to the rational

preferences of firms in the context of oligopolistic dependence.

- Complaint petitions frequently mention high price increases and district sharing claims.
- When the sale price of gray cement is evaluated within the scope of price increase claims, a direct relation with economic parameters such as seasonality, demand, and cost cannot be established. Econometric simulations also revealed that undertakings acted with "Joint Profit Maximization" behavior in most of the regions.
- The relationship between activity scores and the costs has been established. It has been found that high efficiency brings low costs. However, when the price-activity relationship was examined, it was observed that high prices were applied despite the high efficiency in 45 points for CEM I 42.5 and 48 points for all gray cement types.
- Taking into account the fact that firms with low activity are considered, it is thought that firms operating in the sector should increase their efficiency levels and that this increase should give birth to expected effects from a competitive market.
- When examined in terms of market share claims, the industry is far behind the level of competitiveness it should have. The main reason of this observation is the distribution of sales volumes.
- According to the analysis results, more than half of cement usage in cities was obtained from inner city terminals. In addition, it was observed that there are usually two undertakings conducting sales into a city on the same dates. It cannot be determined whether an increase in the number of undertakings selling to cities creates downward pressure on prices.
- It is seen that the shares of undertakings throughout the country are generally in a symmetrical course, with about 50% of the market dominated by five undertakings. All findings strongly suggest that the market is concentrating on regional and even provincial internals, and that competitive dynamics are not actively working. "

The Report's determinations could shed light on the subsequent enforcement approaches and implementation. Preliminary investigations or analyzes will likely be carried out in the future, in line with the Report's findings.

Related Practices

- [Antitrust and Competition](#)
- [Commercial Contracts](#)
- [Distribution, Franchising and Agency Agreements](#)