Organisation for Economic Co-operation and Development

DAF/COMP/GF/WD(2019)49

Unclassified **English - Or. English**

17 November 2019

DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE

Global Forum on Competition

MERGER CONTROL IN DYNAMIC MARKETS – Contribution from Kenya

- Session III -

6 December 2019

This contribution is submitted by Kenya under Session III of the Global Forum on Competition to be held on 5-6 December 2019.

More documentation related to this discussion can be found at: oe.mcdym.

Please contact Ms. Lynn Robertson [E-mail: Lynn.Robertson@oecd.org], if you have any questions regarding this document.

JT03454776

Merger Control in Dynamic Markets

- Contribution from Kenya –

1. The Competition Authority

1. The Authority safeguards competition by, among others, regulating market structure. Regulation of market structure involves analysis of mergers. Kenya’s merger regime applies to all persons in so far as they engage in trade and services.

2. Background of the dynamic markets

2. The modern competition dynamics presents many difficulties in predicting how markets will evolve in order to support regulatory interventions and enforcement decisions in cases where they depend on an effects-based analysis of the likely future effects of the merger.

3. Specifically, the static dimension of competition is usually related to price competition, given the set of products or services that are marketed by firms. Innovation is certainly another important factor that affects market structure.

4. Dynamic competition may be characterized by persistent dominance of the incumbent leader or by action-reaction whereby incumbents are overtaken by a rival whose incumbency itself could then be short-lived. The nature of market dynamics depends on such factors as the **type of innovation, either drastic or non-drastic, the uncertainties involved in R&D activities, the nature of patent protection and of knowledge spill overs, and the intensity of product market competition**. The dynamic evolution of market structure depends on both abilities and incentives of the incumbent and the rivals to innovate.

5. Currently, the standard paradigm overly concentrates on market definition, market shares and derived predictions about price changes, all the while overlooking how a merger might affect innovation.

6. Applying traditional methods yields narrow market definitions, which can lead to an exaggerated assessment of market power. Therefore some new sets of criteria for competition analysis of high technology markets is desired in definition of markets and evaluation of the market power. A wider approach therefore that includes the way technology competition occurs in dimensions such as customer needs and responses to product innovation is needed to assess competition in dynamic markets.

7. Further, competition in New Economy requires looking beyond current market figures. For example, the first-mover in a given market constantly faces the threat that another firm introduces a better version or an entirely different product that eliminates the demand for the leader's product.

8. In this context, an indispensable element of market power assessment in New Economy industries is the examination of **actual and potential innovative threats to leading firms**. This generally involves the assessment of the likelihood of future races for market dominance and the consideration of competitive threats based on new technologies

that differ radically from those used by the incumbent. As innovation contributes to technical and economic progress and consumer benefit, a dynamic approach suggests giving more attention to the efficiencies generated by the transaction.

3. The Kenyan context

9. In Kenya, the Authority considers dynamic effects when assessing the level of competition in a market, for example future entry and exit. It uses tools like market definition, concentration and price pressure indexes (GUPPI) in assessing the level of competition in a market. The Authority however faces difficulty of applying wrong market definition or narrow definition of markets in fast-moving markets, whereby some vital market participants are left out.

10. The Authority has developed a dynamic competition perspective of market definition by revisiting and restating the Merger Guidelines in a way that explicitly clarifies and defends the role of dynamic competition. The updated Merger Guidelines of July 2019 incorporate adaptive regulations that promote innovation.

11. The Authority remains open to the emerging trends in market definition based on constantly evolving dynamics associated with digital markets, big data, multi-sided platforms, non-price effects of conduct, arrangements or mergers (such as innovation, variety and quality) and/or other market developments. It also considers the multi-sided market approach to market definition in platforms. Additionally, it refers to precedencies from other jurisdictions that have dealt with similar cases in defining market and analysing competitive effects of the mergers.

12. The Authority considers the markets for platforms and ICT as dynamic markets. It also considers the competitive pressure posed by potential competition, and treats assessment of potential competitors in the same way it handles assessment of actual/current competitors. It also recognizes that potential competitors can present a potential competitive constraint to the merged undertaking.

13. A proposed merger could discourage a potential market entrant or simply eliminate the prospect of a viable competitive threat. With respect to unilateral effects, the Authority considers the potential of the merger to cause loss of potential competition among other factors. It also considers entry likely when it is economically profitable at pre-merger prices and when these prices can be assured by the potential entrant. Prices cannot be assured by the possible entrants when the minimum increment of supply offered by the potential entrant is sufficient to cause a reduction in market prices.

14. The Authority in assessing likely entry considers that the longer it takes for potential entrants to become effective competitors the lesser the likelihood that the incumbent undertakings will be deterred from exercising market power. Additionally, it also looks at how foreclosure practices may deter entry by potential competitors.

3.1. Applicable cases in Kenya

15. The digital transformation is changing business models, methods of production and distribution, and the way firms compete. Digital technologies have reduced the cost of entering some markets, even across borders. For instance, platforms allow small firms to sell online seamlessly to foreign customers and become “micro-multinationals”. Digitalization has also reduced the costs of scaling up production, advertising and

distribution for new entrants. For example, the availability of cloud computing services provides smaller and newer firms with a flexible access to a significant computing power without investing in physical infrastructure.

16. Cognizant of the aforesaid, the Authority has revised its market definition guidelines to encompass new emerging issues such as big data, multi-sided markets, zero-priced markets and the issue of algorithms.

17. The Authority considers substitutability of the products being offered by the virtual markets and identify if there exists a constraint from physical markets. Most of the digital markets are multi-sided in nature. Virtual markets enable the market players to meet in an artificial marketplace where they are able to carry out the process of buying and selling. The Authority considers substitutability at one side of the market in contrast with the wider market for the basic products.

18. The Authority considers non-price markets to encompass dynamic markets, even though such platforms attract payments once they acquire a certain threshold of users. Indication of market dominance may exist where direct payments are introduced but the traffic accessing the platform does not significantly change. Non-price markets enable users to engage in multi-homing practices since a user of such platforms can easily switch between platforms. Entry barriers are significantly reduced in this market and the platforms compete on attracting the most traffic by increasing quality of content, reliability and accessibility.

19. The Authority has handled several transactions in digital markets and identified an inadequacy in the Law and guidelines in entirety in dealing with cases of the digital nature. These cases have involved general advertising, classified advertising, job advertising, banner advertising, taxi-hailing apps and online payment platforms, among others. Some of these cases are:-

3.1.1. MyDawa & Africa Healthcare MasterFund PTE Limited

20. The Authority in its assessment defined the product market as the market for digital pharmacies, which can operate as single-sided or multi-sided market[1]. For example the **Mydawa** can host other pharmacies in their online platform and connect them with the customers at a fee, which is not the case.

21. Therefore, the two step approach was adopted, where the platform was considered as a product on its own and thus assessed with regards to competition with the other platforms. It does not compete with other online platforms in providing a platform for more than two pharmacies marketing their products to prospective customers (c2c) since the platform is only for its pharmacy. However, it competes with such platforms in terms of the customer group seeking pharmaceutical products, since their objective is to get the pharmaceutical product either conveniently and/or at a low price.

22. The digital pharmacy was well-thought-out to compete with brick and mortar pharmacies, plus other online pharmacies such as Pharmacies Direct Kenya, which is an online pharmacy platform with the distribution done by Malibu pharmacy. The online platforms are in their very nature dynamic in that they diversify from one line of business

[1] In single-sided platforms, the online pharmacy links only one group of customers with its own pharmacy store (warehouse) whereas the multi-sided platforms serve two or more distinct customer groups.

to another. For example, Jumia, an online retail shop, diversified to Jumia food delivery services, and Uber, an online taxi operator, diversified to food delivery services (Uber eats).

23. Consequently, the online pharmacy platform as a product is faced with effective competition. Factor that determine substitutability in this case include, but not limited to, **Convenience factor/drug needs** – the extent of convenience (duration) of accessing the pharmaceutical products - for instance pain killers. **MyDawa** delivers the pharmaceuticals within 4 hours from the time an order is placed, while Pharmacy Direct Kenya delivers within 24 hours. Therefore, based on the emergency/timely needs of certain drugs such as painkillers, the online pharmacies compete with the brick and mortar pharmacies and health centres which have pharmacy services. There are approximately 96 private pharmacies providers in Nairobi and 1985 nationally.

24. The **Africa Healthcare Ltd** covers 4 medical insurance covers out of 43. The number of medical insurance covers that a pharmacy accommodates plays a role in terms of the substitutability, recognizing it's an online pharmacy which is convenient due to the door step delivery. Therefore, medical insurance covers they offer is key for substitutability. This demonstrates that barriers to entry in digital pharmacy trading is low. The concept of defining a single market encompassing all customer groups was also adopted here. Thus, more than two approaches can be adopted in defining a digital market.

3.1.2. OLX B.V & Walie Holdings Limited

25. This is another example, where two relevant markets were defined: online classified advertising[2] and Banner advertising services. The market frequently involves both a publisher, who integrates advertisements into its online content, and an advertiser, who provides the advertisements to be displayed on the publisher's content. Other potential participants include advertising agencies that help generate and place the ad copy, and ad server which technologically delivers the ad and tracks statistics, and advertising affiliates independent promotional work for the advertiser.

26. This market was defined as a single market encompassing all customer groups. It did not include the banner advertisement[3] market since it serves a different customer group which includes advertisers who own a website.

3.1.3. Tim Bidco 1's Travelopia and Enchanting Africa.

27. Tim Bidco 1's Travelopia specializes in tourism related service offerings such as expeditions, tailor made holidays, full service holidays, marine holidays, educational trips and events based holidays. ***Enchanting Africa*** is involved in booking trips and tours to African destinations from abroad, and the market was defined as the market for tourism packages.

[2] Online classified advertising includes email marketing, search engine marketing (SEM), social media marketing, many types of display advertising (including web banner advertising), and mobile advertising.

[3] Specifically, banner advert is a particular kind of online advertising resource that often shows up at the top or side of a webpage. It is a Hypertext Markup Language (HTML) construct that displays a given advertisement and, when clicked, takes the user to the advertiser's site: available at: https://www.techopedia.com/definition/32924/banner-ad.

28. The main challenge here was in the calculation of the relevant turnover generated in Kenya due to the model of operation of one of the parties. This party involved customers outside Kenya buying tourism packages in Kenya from the affiliated entity located in another jurisdiction and thereafter the entity contacts the Kenyan subsidiary which then organizes for the tourism package.

29. After a lengthy consideration of competition law and policies, the location of the customer was considered not to dictate where the turnover was generated but rather the location of the service where the relevant turnover was attributed to.

4. Conclusions

30. A special analytical framework is neither necessary nor desirable for merger review in innovation intensive markets. However, market definition and assigning market shares are particularly challenging tasks in rapidly changing sectors. The complexity of mergers in high innovation sectors may require rethinking the merger review process (i.e. strict time limits), increasing sector specific expertise in competition agencies, and taking pro-active steps to prepare for mergers in high innovation markets.

31. In addressing dynamic markets, competition agencies need to rethink how to best protect citizens, ensure fair markets and enforce regulations while allowing new technologies and business to thrive. This may require considering the implementation of:

- ***Adaptive Regulation*** – Shift from "regulate and forget" to a responsive, interactive approach. Competition agencies need to continuously engage with the merging parties to better understand the relevant market. Reduced period for conducting impact assessments is encouraged in an evolving market with rapidly changing technologies. Competition agencies, thus need to stay abreast with market dynamism by conducting impact assessments to assess the effect on the market;
- ***Regulatory sandboxes-***Prototype and test new approaches by creating sandboxes and accelerators. Competition agencies need to create widely adopted regulatory sandboxes as an innovative regulatory initiative. Sandboxes test dynamic markets with actual market participants, subject to certain safeguards and oversight. Several have been launched with the specific intent to foster market development that advances competition policy and specifically merger review, including through thematic sandboxes. Sandboxes can help regulators gain a better understanding of dynamic markets and develop evidence-based regulations that promote inclusivity and better regulation of market competition.
- ***Outcome-based regulation-*** Competition agencies better focus on results and performance rather than form when dealing with regulation in dynamic markets.
- ***Risk-weighted regulation-*** A move from one-size fit-all regulation to a data-driven, segmented approach by competition agencies may be required. Specifically, merger analysis in dynamic markets may need to take a case-by-case approach where each transaction presents different ways analysing the market.
- ***Collaborative regulation-*** Align regulation nationally and internationally by engaging a broader set of players across the ecosystem.

32. As we have highlighted above, the traditional merger review framework can be applied to innovation intensive markets. However, some customization in approach is required regarding: defining markets and assigning market shares; assessing the significance of changes in market structure; giving proper weight to benefits consumers reap through innovation; assessing the ability of merging parties to exclude or restrict competitors; and designing appropriate remedies.

33. The Authority is also looking into certain elements of dynamic markets such as open finance and digital finance which are key to the Kenyan market. This will guide in the examination of actual and potential innovative threats to leading firms, as a critical element of accessing market power of firms in new era markets.

34. Developing common principles in international competition policy in dealing with the effects of the New Economy should become a top priority. In particular, merger reviews should deal with convergence in analysis in defining the product and geographical market in dynamic markets. This is in line with the regional and international collaborations in order to stay abreast with the new developments of dynamic markets.

35. In line with its Substantive Assessment of Merger Guidelines, which considers both structural and behavioural remedies, the Authority makes use of highly customized behavioural remedies, sometimes accompanied with a required divestment. This may be the best way to address potential competition problems in such markets. There is also the possibility of ordering joint ownership by competitors of certain critical assets, or mandating conditions making joint ownership attractive to the merging parties, especially in a highly concentrated market such as the telecoms industry.