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Working Party No. 3 on Co-operation and Enforcement

Monopolisation, Moat Building and Entrenchment Strategies – Note by Korea

11 June 2024

This document reproduces a written contribution from Korea submitted for Item 2 of the 139th meeting of Working Party 3 on 11 June 2024.

More documents related to this discussion can be found at
www.oecd.org/competition/monopolisation-moat-building-and-entrenchment-strategies.htm

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1. Introduction

1. Monopolization, economic moat building and entrenchment are major strategies that businesses employ in today's economy to secure competitiveness and bolster their positions in a market.

2. A "moat" is a trench, usually filled with water, that is dug and surrounds a castle to protect the place from enemy's attack. The term "economic moat" refers to a unique advantage that protects a business from competitors. An economic moat can be built through various means, such as brand recognition, economies of scale, network effects and high switching costs. To fend off rivals and enhance competitiveness, businesses adopt the strategy of building an economic moat by creating high entry barriers or fostering customer loyalty so that they can prevent rivals from entering a market and strengthen their positions. Namely, an economic moat is one of the factors that provide a competitive advantage to a firm, particularly by preventing market entry of competitors.

3. Entrenchment of a company refers to a situation in which a company secures and maintains a dominant position in a market. An economic moat can help a company easily maintain its dominant position. Without an economic moat, however, a company can effectively maintain its dominance by creating competitive advantages based on strategies such as exclusive dealing to prevent competitors' market entry. Entrenchment is a broader way of reinforcing a position in a market compared to building an economic moat.

4. As such, the strategies of monopolization, economic moat building and entrenchment are major strategies to increase competitiveness and dominance in a market. If exploited or unfairly employed, however, they would restrict consumer choice and distort the competitive landscape. Appropriate regulation and supervision of competition authorities are necessary to prevent such risks.

5. In this context, the KFTC imposed sanctions in early 2023 on Kakao Mobility, a major ride-hailing service provider in South Korea, and Google, a global platform giant, for their anticompetitive conduct: Kakao Mobility leveraged its dominance in one market (the non-exclusive general ride-hailing service market) into an adjacent market (the franchise ride-hailing service market) through the manipulation of its passenger-driver matching algorithm; and Google prevented game developers from publishing apps on One Store, the competing app store, to maintain and reinforce the dominance of Google Play, its own app store. The two cases will be elaborated on below.

2. Case 1: Kakao Mobility's Abuse of Dominance

2.1. The market status

6. Passengers can hail a taxi driver on their smart phones by using ride-hailing apps. In the process of defining relevant service markets, the KFTC defined two markets in which ride-hailing services through apps: (i) the non-exclusive general ride-hailing service market (hereinafter the "general ride-hailing market") for all affiliated and non-affiliated taxis and (ii) the franchise ride-hailing service market exclusively for affiliated taxis (hereinafter the "franchise ride-hailing market").

Figure 1. Ride-hailing services through the Kakao T application

Ride-hailing types	Ride-hailing fee
General Ride	free of charge (midsize taxis regardless of being affiliated with Kakao T)
Blue Ride	up to ₩3,000 fee per ride (franchise taxis called “Kakao T Blue”)

Source: KFTC press release (Feb 14, 2023)

7. Currently, dozens of ride-hailing apps are operating in the Korean general ride-hailing market, among which Kakao T app, owned by Kakao Mobility, holds more than 90% market share.

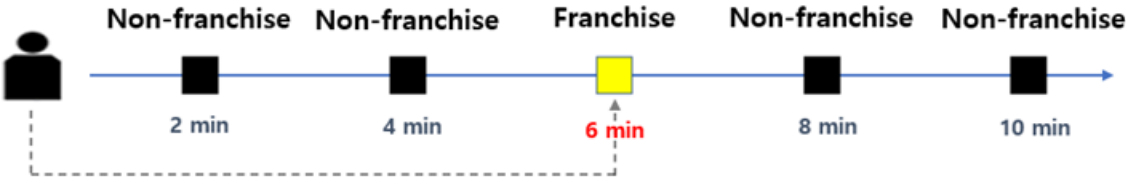
8. In the franchise ride-hailing market, about nine companies are competing with each other, among which Kakao T Blue operates 73.7% of all franchise taxis in terms of the number of taxis.

2.2. Kakao Mobility’s anticompetitive conduct and the KFTC’s remedies

9. While providing the general ride-hailing service through the Kakao T application, Kakao Mobility gave preferential treatment to the affiliated franchise taxi drivers in the passenger-driver matching process in order to attract more drivers to its franchise taxi fleet.

10. Since the launch of its franchise ride-hailing service in March 2019, Kakao Mobility has implemented a manipulative passenger-driver matching algorithm. When a passenger made a General Ride request, the algorithm gave priority to its affiliated drivers and excluded unprofitable short-distance rides under 1km when connecting affiliated drivers with passengers to maximize their profits.

Figure 2. The passenger-driver matching process prioritizing franchise drivers

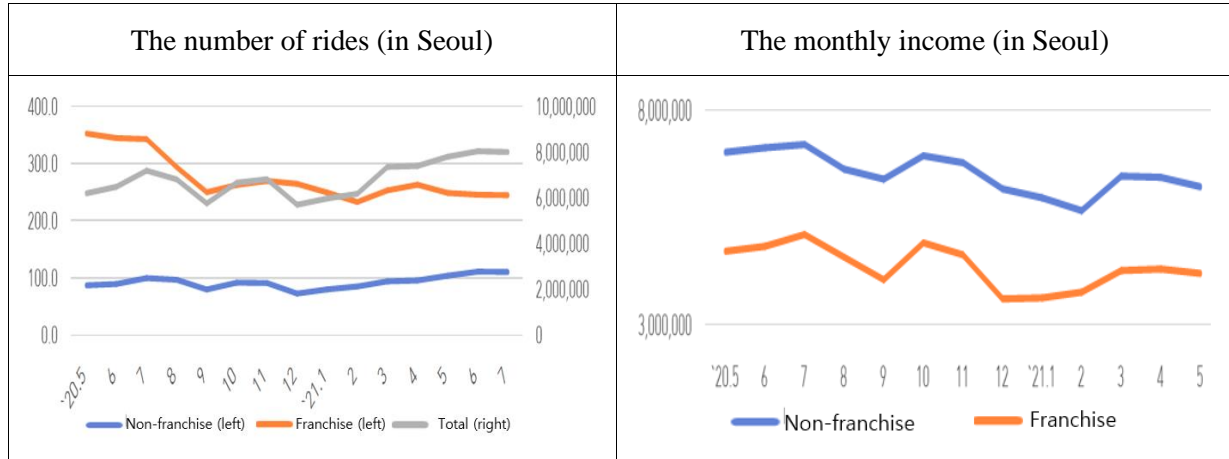


Source: KFTC press release (Feb 14, 2023)

11. Such manipulative matching algorithm resulted in a relatively higher income for affiliated drivers than for non-affiliated drivers. It served as an incentive for non-affiliated drivers to join the Kakao’s franchise network, which in turn, allowed Kakao Mobility to easily expand its fleet.

12. More specifically, from May 2019 to July 2021, affiliated drivers took 35-321 more rides and earned 1.04-2.21 times more than their non-affiliated counterparts on a monthly basis. Consequently, Kakao T Blue's dominance has significantly strengthened in the franchise ride-hailing market, with market share soaring soared from 14.2% in 2019 to 73.7% in 2021.

Figure 3. Franchise drivers vs. Non-franchise drivers: The number of rides taken & the monthly income earned through Kakao T in Seoul during the implementation of the matching algorithm prioritizing franchise drivers

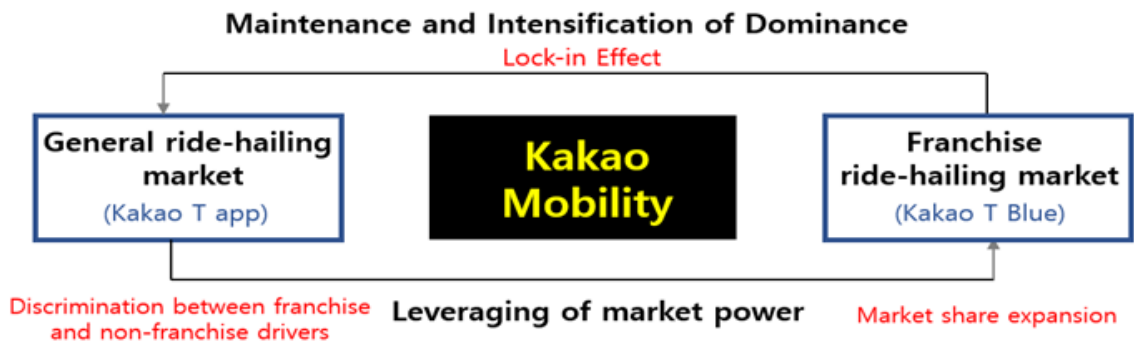


Note:
Source:

13. Also, in the general ride-hailing market, Kakao Mobility’s dominance has maintained and strengthened with a market share increase from 92.99% in 2019 to 94.46% in 2021 in terms of the number of ride arrangements, which increased the possibility of raising service fees charged to passengers and drivers.

14. In a nutshell, Kakao Mobility abused its overwhelming dominance in the general ride-hailing market to give preferential treatment to its affiliated drivers; which enabled Kakao Mobility to leverage its market power into the franchise ride-hailing market, restricting competition; and which in turn, led to weakening competition in the general ride-hailing market, entrenching its powerful position and locking in consumers.

Figure 4. Maintained and intensified dominance in the general ride-hailing market driven by the increase in the number of franchise taxis



Source: KFTC press release (Feb 14, 2023)

15. The KFTC concluded that Kakao Mobility abused its market dominance and imposed a KRW 27.1 billion (EUR 19 million) fine and remedies: Kakao Mobility must eliminate discriminatory elements in the driver assignment algorithm and ensure the ride acceptance rate is calculated fairly without discrimination—which indicates the proportion

of ride requests a driver accepted compared to the total number of requests the driver received—when matching drivers to a passengers based on the rate.

3. Case 2: Google’s Abuse of Dominance

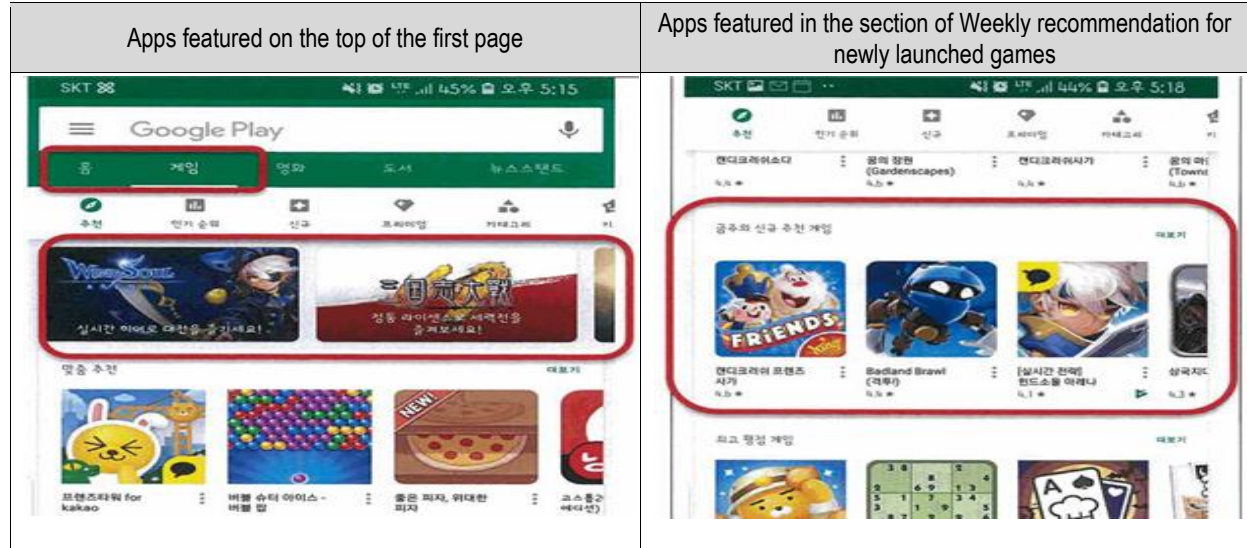
3.1. Market Status

16. An app store is a digital platform that connects app developers and consumers, and Google Play and One Store are app stores for Android devices. Game apps are crucial for app store operators, as more than 90% of revenues of Google Play and One Store come from games. Particularly, Google Play, as a gatekeeper that accounts for an overwhelming market share in both international and domestic markets, has a superior bargaining position compared to its business partners—game developers.

17. In reality, app stores are the only distribution channel for mobile games, and the market has been on the rise domestically and internationally.

18. Google can increase app visibility by placing an app on the first page of Google Play, which is called “Google Play featuring”. Likewise, Google offers various promotion and marketing services for apps, including support programs for overseas product launches, and these services were considered very important for app developers. Google used its promotion and marketing support programs to impose specific requirements on game developers

Figure 5. Google Play Featuring



Source: KFTC press release (Feb 14, 2023)

3.2. Google LLC’s anticompetitive conduct and the KFTC’s remedies

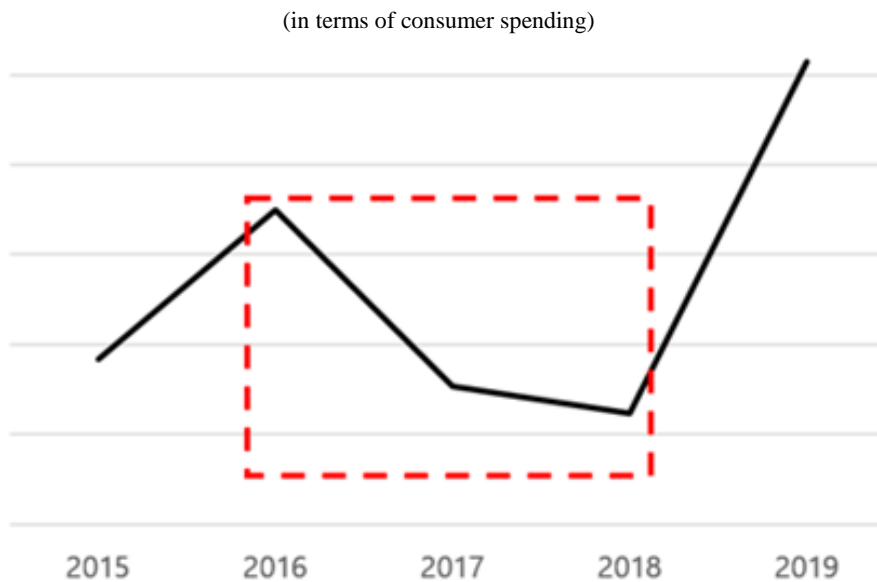
19. As a dominant player in the Android app store market, Google prevented mobile game developers from publishing apps on One Store, a competing app store. Google required game developers to release their apps exclusively on Google Play in exchange for promotion and marketing support, such as Google Play featuring and assistance with overseas product launches.

20. Google has continued such practice since June 2016, when One Store was launched, to April 2018, when the KFTC initiated an investigation. Google targeted not only major game developers (e.g., Netmarble, Nexon and NCSoft) but also small to mid-sized ones, encompassing the entire Korean mobile game market.

21. Google specifically focused its efforts on large-scale games, which generate a significant portion of the revenue in the mobile game market, and it led to the exclusive release of top-tier titles through Google Play, foreclosing One Store in terms of distributing new games.

22. As a result, the late entrant in the app store market, One Store failed to secure new games and major content, and its value as a platform has decreased. The absence of new titles on its platform decreased the number of paid users; and the decreased number of paid users led to greater difficulties publishing new games. Through this vicious cycle of negative network effects, One Store saw a continuous decrease in revenues.

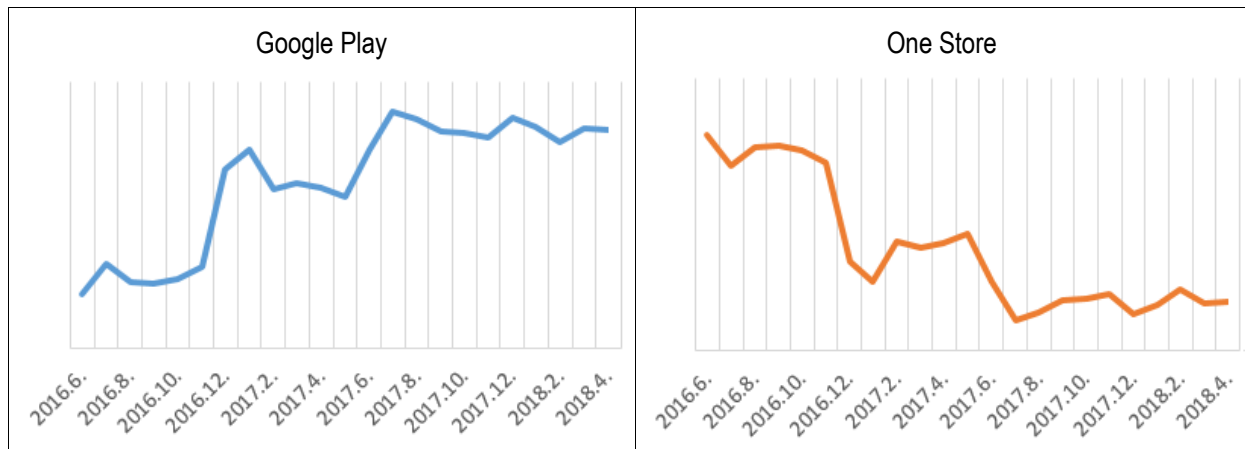
Figure 6. One Store’s sales trend affected by Google’s exclusive dealing



Note: Due to the exclusive dealing, One Store experienced negative growth in 2017-2018
 Source: KFTC press release (Feb 14, 2023)

23. Consequently, Google succeeded in entrenching its dominance in the app store market. While One Store lost more than half of its paid users, Google Play’s paid users increased by about 30% along with an increase in market share from about 80% in 2016 to more than 90% in 2018—which indicates Google’s enhanced market power.

Figure 7. The market share trend of Google Play & One Store influenced by the Google's exclusive dealing (in terms of consumer spending)



Source: KFTC press release (Feb 14, 2023)

24. In April last year, the KFTC concluded that Google restricted competition to entrench its market power in the app store market and imposed remedies and a KRW 42.2 billion (EUR 29.6 million) fine for abusing its dominance.

4. Conclusion

25. A dominant company wants to build an economic moat based on its entrenched position to prevent competitors from entering the market while employing a range of strategies that can increase consumer dependence on its products and services. However, these strategies are likely to involve abuse of dominance and other anticompetitive conduct, so competition authorities must exercise supervision and intervention as needed.

26. Taking advantage of dominant positions in the relevant platform markets, Kakao Mobility and Google Play attempted to block competitors' entry into the markets; build an economic moat; and further entrench their market dominance. The KFTC's enforcement actions against Kakao Mobility and Google Play carries great implications in a sense that a competition authority exercised aggressive action against anticompetitive conduct of the two dominant firms so that consumer choice was expanded and the diversity of products and services was ensured.

27. When it comes to the Kakao Mobility case, it is noteworthy that the KFTC prevented leveraging of market power in the ride-hailing service market that can significantly affect people's lives, recognizing that anticompetitive conduct in a market (the non-exclusive general ride-hailing service market) can restrict competition in an adjacent market (the franchise ride-hailing service market).

28. The Google case has significance that a competition authority put the brakes on the global platform giant seeking to maintain and boost its dominance in the app store market. Especially, acting as an important platform, an app store can influence the entire digital markets, so the KFTC's enforcement action is expected to contribute to reviving competitive pressure in the app store market and further promoting innovative and dynamic growth of the overall mobile ecosystem.