<u>Analyse the economic rationale for a competition policy, such as that in the UK, which is intended to limit potential abuses arising from the exercise of monopoly power or anti-competitive practices, illustrating your analysis with reference to at least two examples of competition policy.</u>

The prevention of monopolies arising in the UK market is essentially for the purpose of the consumer. If monopolies were to form then prices would rise beyond recognition as there would only be one supplier of possibly essential goods leaving no option for the customer to pay the extortionate prices they are asked to pay.

There are two types of monopoly, the pure monopoly and the natural monopoly. The difference between the two being that a pure monopoly is the only supplier in that field of output, with no close substitute and no threat of competition, whereas a natural monopoly is a company which once it is established can produce at an increased level of output at a lower cost therefore forcing its smaller competitors out of business.

Another form of market domination is in the form of an oligopoly, which is the cooperation of several companies to achieve the same scale of market domination. Such as the collaboration between Lloyds and TSB. The reasoning behind the possibility of market domination is due to an almost inelastic demand for certain products, i.e. cigarettes and petrol. This is why monopolies can cripple an economy if they gain market control as people require some products no matter what the price; therefore no competition equals no price variance.

To prevent such domination occurring the office of fair trading and suchlike public sector bodies put in place laws to control price fluctuations and seek to introduce fresh competition into certain sectors of trade to create a higher level of competition. These regulators can also block takeover moves or any similar business activities which it believes may lead to the rise of a monopoly.

A good example of this is within the u.k. supermarket industry where only a few major companies dominate the market. If one were to buy out another, this would increase the possibilities of a monopoly occurring. This very thing happened last year with asda attempting to buy out the struggling Safeway. The office of fair trading believed that allowing asda to do this would be dangerous and therefore blocked the takeover bid and also disabled the possibility of other major competitors from doing the same. The office of fair trading decided the best option was to allow Safeway to be bought by a peripheral company and the company which came forward was Morrison's. This meant that there would then be another major competitor within the U.K. supermarket industry. This gives a good example of both the power of the so called regulators to prevent a monopoly rising and their ability to place competition in areas they believe is dominated.

An example of a regulator preventing unfair competition was the investigation into price fixing allegations of football shirts. The accused included JJB sports as the outlet and the suppliers Umbro as well as several major clubs and the English FA. Britain's office of fair trading stepped in to investigate the problem. They found that smaller companies had attempted to sell kits at a discounted price but were being refused the opportunity to purchase the kits by the manufacturers. This meant that JJB continued to fix the price of kits at around £40 for adult and around £30 for junior sizes with barely any competition. The office of fair trading extended its investigation to all the major sports retail outlets across the U.K. with 2 out of the 10 investigated being fined. The fines incurred by all the parties concerned amounted to £18.6 million. The fines were allocated as follows:-

-JJB sports were fined the largest amount of all concerned with a total of £8.373million

-Umbro the main manufacturer involved were fined £6.64million

-Manchester United plc were the most heavily fined of the clubs involved with fines totalling £1.652million

-the remainder of the £18.6million fines was put onto the FA and the other clubs involved.

The office of fair trade was aided in its quest to punish the involved, by an act put in place allowing them to punish any company thought to be practising unfair trade with a fine of unto 10% of the company's annual turnover. This act was known as the competition act.

The Competition Act 1998 gives the Office of Fair Trading the power to investigate and intervene in circumstances where an organisation has practices which have the object or effect of preventing, restricting or distorting competition in the UK. The Director General of Fair Trading, Mr John Vickers, said:

"Contract terms between suppliers and customers should generally be freely negotiated. Trade association rules that unduly restrict commercial freedom reduce customer choice". (www.legal day.co.uk).

The question is how to define fair trade and when is it right for somebody to say that certain business activities aren't fair. A good definition of fair trade is "Fair Trade is a trading partnership, based on dialogue, transparency and respect that seek greater equity in international trade. It contributes to sustainable development by offering better trading conditions to, and securing the rights of, marginalized producers and workers – especially in the South".(www.ifat.org)

Another example of a possible monopolisation was within the IT market, inkjet cartridges. There are four main suppliers of printers in the u.k, Hewlett Packard, canon, Lexmark and Epson, between them supply 90% of the printers sold in the u.k. OEMs such as in the football jersey case had control over the supply of the products. This meant they could control competition and not allow new competition into the market for this product. The European believed there were unfair practises within the inkjet industry for sometime, so when the ukcra were tipped of about the limited supply of spare parts they contacted the office of fair trade. The market for inkjet cartridges in the u.k was valued at approximately £700million with around 40million cartridges being sold annually. The u.k printer industry was valued at £350million. The report also showed that third party cartridges were between 20 and 40% cheaper than the major suppliers. The oft therefore decided there were 3 main issues which needed to be dealt with to improve competition:-

-unclear pricing

-comparisons between cartridges are not possible

-warranty information for printers is unclear

The oft therefore declared that a testing method for printers be derived and utilised within the next year to provide a fairer trade for the consumers. (www.ukcra.co.uk)

The main fact that arises from all of these examples is that if monopolies are not prevented then prices would become extortionate. This could easily cause a widening of the gap between the rich and the poor.

The reasons why monopolies are bad for an economy are:-

-resource misallocation

-increased costs

-redistribution of income from consumer to monopolist

-restricted consumer choice

-price discrimination

Despite these reasons against allowing monopolisation to occur monopolies do bring some advantages to the market:-

-economies of scale i.e. monopolies may benefit from price reductions not available to smaller companies.

-high expenditure on research and development

Overall though the cons still outweigh the pros of a monopoly economy.

The regulators such as the oft are clearly an essential part of today's economic environment, if competitive trade is to continue. Without such organisations consumers would find themselves purchasing goods in an increasingly declining market. If monopolisation were to in the cigarette industry there would still be the same demand for tobacco as ever but supply would decrease and therefore price would rise shifting the whole demand curve. This is because cigarettes are an inelastic product where consumers will pay what ever is asked of them because it would be seen as an essential product by smokers. The chances of monopolisation in the modern market are particularly low due to the fair trade act and the ability to create competition in areas necessary. This means it is unlikely that we will have to pay high prices because of a lack of competition, but unfortunately we still have to pay tax!