Competitiveness, Investment Climate and Role of Competition Policy in Turkey

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Foreword

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Gamze Őz (2005) *"Legal and Institutional aspects of Competition Policy in Turkey and Its Impact on Investment"*

Izak Atiyas (2005) *"Competition and Regulation in the Turkish Telecommunications Industry"*,

Esen Sirel, Sezin Elçin and Sülyeman Cengiz (2005) "*Regulation, Liberalization and Competition in Turkish Domestic Airlines Market"*

Aydin Çelan, Tarkan Erdoğan and Erol Taymaz, *"Fast Moving Consumer Goods: Competitive Conditions and Policies"*

Esat Serhat Guney, *"Restructuring, Competition and Regulation in the Turkish Electricity Industry"*

The present Report provides an overview of the range, nature and type of issues confronted in the implementation of competition law-policy in Turkey, and its implications for the investment climate, productivity and competition. This Report could not have been prepared without the invaluable information, and insights provided by Mr. Halil Baha Karabudak, Head of Department II, Turkish Competition Authority, Mr. Güvan Sak, General Director of TEPAV/EPRI and Mr. Gokan Akinci, Sr. Investment Officer, Foreign Investment Advisory Services, The World Bank Group.

Executive Summary

1. During the past two decades, Turkey has adopted various free market oriented policies such as liberalization of controls over trade and investment, deregulation and privatization, and other structural economic reforms. The measures include entering into a Customs Union Agreement, other initiatives to more closely align its policies and institutions with the European Union. While bi-lateral trade with the EU has markedly increased to over 50%, the amount of FDI that Turkey attracts remains small ($1.6 billion in 2003)—significantly lower than many comparator and competing countries. This in large measure is attributed to a wide range of problems with the 'investment climate' which includes such factors as policy instability, anticompetitive business practices, corruption, inadequate legal and regulatory framework, and public sector and corporate governance problems.

2. In 1997 the government established an independent Competition Authority and Competition Board to implement the Competition Law which had been enacted a few years earlier. The law essentially parallels the competition rules of the EU, dealing with anticompetitive business practices such as cartels and collusive agreements to fix prices, allocate markets, bid-rigging; and other restrictive agreements; abuse of market position by dominant firms; mergers, acquisitions and joint ventures between firms that may restrict or distort competition. The law also has provisions permitting the Authority to engage in 'competition advocacy' by reviewing and commenting on various public policies and regulatory decisions, and institutional arrangements that unnecessarily limit competition.

3. The Competition Authority is reasonably funded and consists of well trained experts. The application of the competition law-policy is mainly driven by complaints though the Competition Board may also institute investigations into situations where competition infringements have occurred or are likely to occur. During the past eight years the vast majority of the cases have been 'demand driven'--only 11% of the cases were initiated by the Board. The selection and appointment process of Board members has in place a system of checks and balances and measures to prevent 'capture' by influential political and/or business interest groups. The Competition Board is the adjudicative body that decides on case matters, and there are rights of appeal to the State Council. However, Board members can also participate in an investigation, which is controversial as it conflicts with the principle of separation of investigation and adjudication functions in judicial processes. Recently a large number of decisions have been overturned on appeal. There are legislative proposals to rectify this situation, and also other amendments to improve the effectiveness of the competition law-policy.

4. The Competition Authority has concluded over 2000 matters relating to a wide range of anticompetitive business practices spanning Turkish industry. It has developed a reputation of being one of the best managed and effective

government bodies—a view shared by the OECD, EU and this Report. The case matters handled and decisions rendered have particularly focused on abuse of dominant market position and restrictions on entry or expansion in markets. In addition the vast majority of the M&A and JV transactions have been permitted, which include many transactions involving foreign investors. These and other actions such as pro-active competition advocacy, coupled with the generally coherent and consistent approach of the Authority, are conducive to increasing competition and entry, and likely to attract both domestic and foreign investment, and improve productivity.

5. However, there are areas for further strengthening the administration and effectiveness of the competition law-policy. The measures identified include expanded use of 'consent' orders and issuance of business advisory opinions; and more targeted information dissemination and program of compliance in both the public and private sector. This could reduce costly litigation, frictions with other public policies and regulatory bodies, and also the number of complaints which are not substantive or fall outside the scope of the law and dissipate administrative resources. It is also suggested that more communiqués and guidelines be issued by the Authority on factors it considers in assessing fines and various remedies, the approach taken to different competition infringements, and establish *de minmus* principles for exempting agreements involving mainly small firms. To enhance business confidence, the Authority expedite the publication of recent case decisions and provide more details on factors considered and dissenting views.

6. There is ambiguity in the inter-face between competition law-policy and different sector specific regulations, such as in the provision of electricity and telecommunications services. Also, the heritage of past government policies and regulations have given rise to dominant market position by state owned or controlled monopolies, and large private sector firms. This has facilitated various anticompetitive practices by incumbent firms, against which the Competition Authority has taken a number of enforcement actions. The anticompetitive practices and market structures, reversals in government policies, and non-transparent or discriminatory decisions by regulatory bodies have been pointed out by investors as dissuading investment. As a consequence, there is insufficient investment and productivity levels are low—especially in the two critical infrastructure areas of electricity and telecommunications. For example, in the electricity sector alone, Turkey needs 5 to 6 times the total FDI that occurs in the economy as a whole! Meanwhile combined transmission and distribution losses are about 20%--much higher than countries such as Greece and Hungary. In telecommunications, total factor productivity is about 64% of the US ('best practice') levels, and various anticompetitive practices has limited the expansion by firms into value-added services. There is an urgent need to clarify and resolve various regulatory governance issues and to strengthen the role of the Competition Authority, in safeguarding and encouraging competition.

7. In the past two years, the government has accelerated liberalization of the domestic air passenger market, where the Competition Authority had also previously put forward proposals for increasing competition and entry. The increased competition has increased domestic passenger travel by 63%, and some city-pair air fares have been reduced by as much as 70%. The increase in competition has also had positive effects on the dominant state owned Turkish airlines. It too has had increases in the volume of passengers, and productivity. And the new entry and expansion by existing carriers has led to increased investment.

8. Another sector examined is the fast moving consumer goods (FMCG) market, which is going through dynamic change. This sector comprises of a wide range of food, grocery, pharmaceutical, cosmetics, detergents and other house-hold consumption items. Although there have been competition related complaints, only a few cases were substantive to warrant investigations. The greater risk to competition, entry and increased investment stems more from draft law proposals

9. The benefits of competition, and the effective role played by the Turkish Competition Authority are evident in a wide range of its case specific and competition advocacy activities. This has been beneficial to positively conditioning the investment climate, by reducing barriers to entry emanating from both policy based and private sector restrictive business practices, and in increasing competition. In addition, as implementation problems have arisen, the Competition Authority has been calibrating its administrative practices, and proposed amendments to the law. However, the effective application of competition law-policy principles has been thwarted by the lack of clarity and consistency in the government's regulatory policy and decisions in several instances—especially in the electricity and telecommunications sectors. The government needs to have an integrated and coherent approach toward competition policy in all sectors of the economy. The instruments of Turkey' competition law-policy contains provisions to permit this, while also allowing for certain exemptions and exceptions where necessary to meet other social-economic objectives.

I. The Role of Competition Policy in Fostering Investment and Competitiveness

Introduction

1. During the 1980's Turkey changed its course towards economic development. From State-led planning and strategic interventions, it embraced more free market oriented policies to encourage private sector led economic activity. In addition, it set its goals towards integrating with the advanced and larger market economies of the European Economic Community. After the long-standing 'Association Agreement' signed decades earlier[1], formal steps were taken to closely align its policies and institutions with that of the European Union. In January 1996, Turkey and the EU finally created a Customs Union, which removed all but few tariffs between the two trading partners. One of the requirements of the Customs Union also required implementation of an effective competition law-policy. In 1997, the Government set up the Turkish Competition Authority (Rekabet Kurumu) to implement Law No. 4054 to protect and promote competition. This law, which had been published earlier in the *Official Gazette* (December 2004*),* essentially parallels the European Economic Community rules. The Turkish competition law-policy has now been in effect for about eight years.

2. This Report is motivated by the facts that although Turkey's decision to embark on structural economic reforms and integrate with the European Community has reaped benefits, there remain significant short-falls in it economic and legal policy framework. As the ensuing discussion indicates, several of the issues relate to the 'investment climate' and the degree of competition prevailing in key sectors of the economy In this connection, this Report provides an overview of the design and implementation of Turkey's competition law-policy, and *its role in shaping the business climate for increasing competition, investment and productivity*.

3. Generally speaking, the term "competition law-policy" encompasses instruments that address government economic and regulatory policies, *and* private sector restrictive business practices that significantly distort the competitive process; thereby undermining the efficient functioning markets. The competitive process entails independent decision-making and rivalry between existing (and potential) business entities in terms of such factors as prices, output, market share, quality, service, and/or other conditions affecting the value of goods and services. The primary objective of competing businesses is to profitably acquire, retain and increase the patronage of clients for their products. However, while individual

[1] The Association agreement was signed in September 1963 and became effective in the following year. A characteristic of Turkey's reform program has been the 'stop-go' nature of the process, both in terms domestic policies as well as in its relations with the European Union.

firms compete against each other, the 'investment climate' in which this takes place is determined by a number of factors—especially government economic and regulatory policies as well as by business strategies of mainly incumbent firms. Public policies can either promote or inhibit competition and adversely affect firm business decisions to invest, expand output, and/or enter into new markets. Indeed, empirical experience suggests that private sector anticompetitive business practices are often rooted in poorly conceived and implemented public policies. Such situations especially arise when policy-makers and regulators are 'captured' by politically connected firms, engaged in self-serving rent-seeking behavior.

4. A lax competition law-policy may prevent effective competition from occurring and impede the structural reform process. Inefficient incumbent firms may become entrenched and insulated from the pressures to reduce costs, invest and innovate. In contrast, an overly strict application of competition law-policy may inhibit pursuit of legitimate business strategies such as vigorously competing on basis of superior economic performance, or exploiting available efficiencies by acquiring less productive firms. An effective competition agency has to be able to judiciously discern between such situations. It should aim to prevent the most egregious anticompetitive policies and business practices that reduce consumer welfare. In addition, the law enforcement functions--including encouraging voluntary compliance with the law--and competition policy advocacy functions of a competition agency need to be balanced in order to promote competition.

5. As a backdrop, the questions which this Report focuses on are:
   (i) What are the principal features of the design and implementation experience of Turkey's competition law-policy?
   (ii) What has been the nature and type of cases investigated (and resolved), and sectors where competition problems have arisen?
   (iii) To what extent and on what issues has the Turkish Competition Authority (TCA) been engaged in competition advocacy?
   (iv) What has been the impact of the TCA's competition law enforcement and competition advocacy activities, on a case specific, sector and /or broader 'investment climate' basis? Have TCA's activities likely resulted in lower prices, increased output, entry, increased investment?
   (v) What has been the nature of the impediments to fostering competition in Turkey?
   (vi) How can the design, implementation, and impact of competition law-policy be strengthened?

6. In gauging the impact of competition law-policy, a few caveats need to be borne in mind. One of course is that a wide range of public policies as well as the inherent structural characteristics of the economy have a bearing on competition, and also on the investment climate. These would include trade, investment, labor market, ownership and macro-economic instruments such as monetary, fiscal and exchange-rate policies. Also factors such as geography and natural resource endowments. The examination of such policies and factors falls outside the scope

of this Report. Another caveat is that while a well construed competition law-policy is a 'general policy of general application', that is it covers or should cover all sectors of the economy--it is applied on a case-by case basis. The cases usually arise from complaints received from individual firms or customers. A particular action by the competition authority may, therefore, resolve anticompetitive behavior by one or more firms in the situation at hand, but may or may not have a sector or economy wide impact. In addition, there is the usual problem of the lag between a particular action, and the measurable impact that may follow—which can be quite long. In this context, successful competition advocacy activities are more likely to have wider impact at the sector or economy level. In other words, the actions taken under competition law-policy do not necessarily have a one-to-one correspondence with increased investment, productivity or overall improvement in the investment climate. The levers of competition policy are not like those employed in macro-economic policy such as interest rates or money supply. However, *credible* competition law-policy can have widespread deterrent effects against anticompetitive behavior. The credibility in large part is determined by business perceptions regarding the probability of an illegal anti-competitive practice being detected, investigated, prosecuted, and subjected to appropriate levels of fines and/or other remedies. In addition, wide publicity given to cases, dissemination of information, having a responsive demand driven complaint process (giving weight especially to complaints from customers than competitors), encouraging compliance with the law and providing incentives such as 'leniency' programs, enhance the credibility of and competition agency and policy

Turkey's Investment Climate Challenges

7. Over the past decade EU-Turkey bi-lateral trade has increased consistently. About 58% of Turkey's total exports are destined to--and about 52% of the imports emanate from--the EU. The Customs Union has undoubtedly benefited both economies. However, the increased trade has not led to increased foreign direct investment (FDI) which normally tends to occur in tandem with international trade. FDI is an important vehicle for transfer of technology and modern organizational methods that result in increased productivity. Moreover, while on average domestic investment is several times larger than FDI; the two tend to be highly correlated[2]. FDI often acts as catalyst for domestic investment and vice-versa[3]. Turkey, given the size of its economy and domestic markets, labor force and wage structure, and large industrial base and related infrastructure, should be a magnate for FDI. This is not the case. In 2003, all FDI was USD 1.6 billion, which amounts to only 1.2% of the total FDI flows to developing and transition market economies, or 0.04% of the flows to the OECD countries, of which

[2] Globally, net private capital flows on average are bout five times that of FDI. In Turkey they are about seven times indicating more the small magnitude of FDI than large amount of domestic capital….Turkey is viewed as a capital short economy.

[3] See the World Bank Reports: *Global Economic Prospects Report (2003), and World Development Report (2005): A Better Investment Climate for Everyone.*

Turkey is a member. Countries such as Bulgaria, Croatia, Hungary, Poland and Romania all received higher amounts of FDI in absolute and relative terms.

8. This "FDI paradox" has been noted by the McKinsey Global Institute (MGI) amongst others. Paradox because Turkey does not have any overt barriers to FDI. To further enshrine the principle of equal treatment of domestic and foreign investors, Turkey adopted a new FDI law in 2003. But, a survey by YASED (Foreign Investors Association) conducted in March 2005 reveals that while members were positive on the economic environment in Turkey they listed negative factors such as insufficient legal framework, bureaucratic red-tape and high taxes as obstacles to FDI.

9. Several factors including those just mentioned determine FDI *and* domestic investment. The list would include the general macro-economic conditions, political environment, taxes and available incentives, labor wages and skill, energy costs, transportation and telecommunications infrastructure, R&D capability, among others. In a comparison with 16 other countries Turkey ranked lower (that is, 12th and greater) in all of these factors[4]. 'Competitor countries' of Central and Eastern Europe ranked better. In addition, a World Bank study indicates that of the 1000 or more firms surveyed, a high percentage identified corruption (63%), financing (78%), policy instability (88%), anticompetitive practices (61% and taxes and regulations (73%) as adversely constraining their operations and investment decisions[5].

10. The MGI points out that on average, Turkish productivity is only 40% of US levels, and only slightly more than half of its own potential. Drawing on sector and firm specific research, factors identified to inhibit improvements in productivity include monopolistic markets, especially in the provision of vital infrastructure services such as telecommunications and electricity, and insufficient competitive pressures. Achievable productivity improvements were analyzed on the basis of reorganization of functions and task in existing establishments without requiring new capital, gains that would accrue from new investments, and the effect of potential new entrants. It was stated that: "Fair and intense competition in all sectors will ensure that the retained earnings available for reinvestment occur in the most productive companies[6]"……thereby generating investment for growth.

11. Turkey's industries tend to be 'dualistic' in terms of not only urban and rural segmentation, but also foreign vs. domestic firms, and formal and informal sectors. Dutz et al. (2003), for example, point out that average labor productivity in FDI companies was 35% higher than the average for all manufacturing plants. Also, average productivity increased at a higher rate in foreign-owned, than in

[4] See TÜSIAD and YASED (2004): *FDI Attractiveness of Turkey: A Comparative Analysis.*
[5] See Batra, Geeta, Daniel Kaufmann and Andrew Stone (2003) *"Investment Climate Around the World: Voices of the Firms from the World Business Environment Survey"*
[6] McKinsey Global Institute (2003) *"Turkey: Making the Productivity and Growth Breakthrough"*, page 4.

domestically owned plants. Over time the productivity gap narrowed but was not likely to vanish for a long time. FDI also had positive spill-over effects as productivity levels of local firms was higher in sectors where there was greater FDI involvement. One interpretation for this observation that FDI not only diffuses technological and other types of knowledge but also generates increased competitive pressures on domestic pressures.

12. Among the range of product market barriers and other factors adversely affecting productivity of Turkish industry, the MGI also examined the 'degree of informality', that is the extent to which enterprises (mainly small establishments) operating in the market evade regulatory obligations such as paying taxes, respecting labor codes and meeting various product market obligations. This could stem from lax enforcement of regulations by government authorities and/or unnecessarily high regulatory burden which creates incentives for non-compliance. Generally speaking, smaller establishments are likely to be in a better position to do this than larger firms. In any case, it creates cost differentials between firms, and dampens productivity as informal less productive firms stay on conducting business without investing and modernizing their operations[7]. Effective regulatory reform and leveling the field of enforcement of government policies would rectify such situations from developing.

13. Governance as a broader issue in terms of "rule of law" and predictability of policies has been mentioned as constraining investment by a number of studies[8]. Dutz et al (2003) state:

> "……the main unaddressed obstacles to increased FDI in Turkey are governance and institution-related problems related to rule of law and competition. The most important legal and judicial constraints relate to insufficient clarity and insufficient respect for the rule of law…….the government as rule-maker has failed to address underlying legal ambiguities in a timely fashion, raising the question of whether the lack of clarity in the underlying rule is *intentional, in order to give public decision-makers the required degrees of freedom to grant special treatment and exemptions whenever politically convenient*." (page 24, emphasis added.).

The authors point out the absence of a level playing field between different firms, and the failure of the relevant regulatory body to enforce pro-competition rules as having rapidly sent negative signals to future investments.

14. A FDI Confidence Index, based on a survey which tracks the impact of political, economic and regulatory changes on foreign investment intentions and

[7] MGI estimates that in some sectors such as dairy processing, the informality related cost differential was high as 20%. In fast moving consumer goods (convenience grocery and related products) the cost differential was 10%. Ibid, page 63.

[8] See for example OECD (2002) *OECD Reviews of Regulatory Reform: Turkey-Crucial Support for Economic Reform";* and Dutz, Mark, Melek Us and Kamil Yilmaz (2003) *"Turkey's Foreign Direct Investment Challenges: Competition, Rule of Law and EU Ascension"* (mimeo).

preferences of the leaders of the world's leading companies, indicates that between 1998 and 2000, Turkey was not listed among the top 25 countries. However, in 2001 it made the list and ranked 23rd, off the list in 2002, ranked 24th in 2003, and again off the list in 2004[9]. Aside from not ranking high as a major FDI destination, this variation could be reflective of the unstable policy environment that prevails in Turkey. For example, in 2001 the Turkish Government cancelled 46 contracted power projects based on build-operate-transfer (BOT) and transfer-of-operating rights (TOR). While subsequently a constitutional court decision ruled against the government decision and ordered the contracts be honored or the parties be compensated, to date no actions have been taken[10].

15. However, it is not only the issues relating to public governance which deter investment in Turkey. There are also problem areas with respect to private sector corporate governance. Very few companies are listed on the Istanbul Stock Exchange (ISE). Turkey is still developing an 'equity culture'. But the future does not bode well if the current situation and corporate practices continue. The majority of the listed companies on the ISE are controlled by a single family as the controlling shareholder, which "renders many protections of minority shareholders ineffective".[11] Companies issue shares with multiple voting rights, do not disclose information on ownership structures, or necessarily adopt international financial reporting standards, inflation accounting, and consolidated reporting. In addition, there is no mandatory arbitration required as means for resolving shareholder conflicts. According to the World Bank's *Doing Business* Report, Turkey's Disclosure Index is significantly lower than other jurisdictions (2 vs. 7 for best practice, 5.6 for high income OECD, and 3.6 for Eastern Europe-Central Asian countries). The report by the Commission of European Communities on Turkey's progress towards accession also concluded effective enforcement of company law as well as intellectual and industrial property rights remained limited[12].

16. While trade and investment liberalization measures are pro-competitive, they are not sufficient. Experience in other countries indicates that domestic markets can still remain insulated from the intensity of competitive pressures by anticompetitive situations in domestic markets such as cartels formed between domestic and international firms, exclusive dealing and restrictive distribution contracts, monopolization of local inputs including distribution channels, high transportation costs, as well as factors such as inefficient ports, customs, and

[9] See A.T. Kearney,Inc., *"FDI Confidence Index"*, Global Business Council, October 2004, Volume 7

[10] Issues relating to the telecom and electricity sector are discussed in greater detail in Section III of this Report, and in the papers prepared for this project by Atiyas (2005) and Guney (2005)

[11] See the report by the Institute for International Finance (April 2005) *Corporate Governance in Turkey: An Investor Perspective,* and accompanying press release (page 2).

[12] See Commission of the European Communities (2004) Regular Report on Turkey's Progress Towards Accession, Chapter 5. Page 91.

bureaucratic red-tape, etc[13]. In the case of Turkey, businesses have also complained about various import policies even in the wake of the Customs Union and other bi-lateral agreements. For example, while import licenses are not required for industrial products, they are required for after sales parts and services. Despite privatization of a parastatal company with monopoly rights over the imports of alcoholic beverages, arduous document requirements, high duties, and non-transparent administration of import policy continue to limit market access. In public tenders, a law gives domestic bidders 15 percent preference over foreign firms. Industry has raised concerns on the discriminatory price control policies for imported pharmaceuticals. And arbitrary changes, lack of notification and information, certification and implementation of phytosanitary and other standards.

17. Various studies on Turkey's manufacturing sector also point to persistence of high concentration despite trade liberalization. In addition, while increased import penetration generally led to lower price-cost or profit margins of Turkish firms, this was not the case for private sector firms in highly concentrated industries. One interpretation offered by one of the study authors is the: "…presence of a possible implicit collusion among domestic and foreign firms in more concentrated industries or importers and domestic manufacturing firms may be parts of the same firm and opening of the manufacturing industry to world trade has not influenced effectively the competitiveness of these industries…..trade liberalization is not sufficient for the competitive domestic market, some additional measures are needed to improve the competitiveness of industry"[14] Among the measures identified are an effective competition law-policy.

18. It is evident from the preceding discussion that Turkey needs to address a wide range of issues if it is to attract both foreign and domestic investment, increase

[13] For further discussion on these points see Khemani, R.S., and Mark Dutz (1996) *"The Instruments of Competition Policy and Their Relevance for Economic Development"* PSD Occasional Paper No. 26, The World Bank.

[14] Cihan Yalcin (2000) "*Price-Cost Margins and Trade Liberalization in Turkish Manufacturing Industry: A Panel Data Analysis"*. Research Department Discussion Paper No. 37, Central Bank of Turkey, Ankara. Also, Kivilcim Metin-Ozcan, Ebru Voyvoda and Erinc Yeldan (2000) "*On the Patterns of Trade Liberalization, Oligopolistic Concentration and Profitability: Reflections from Post-1980 Turkish Manufacturing"*, Department of Economics Discussion paper No. 00-12, Bilkent University, Ankara. Ayse Mumcu and Unal Zenginobuz (2001) *"Competition Policy in Turkey"* Paper prepared for the Economic Research Forum 8th Annual Meeting, Cairo, 15-17 January, 2002.
High profits or price-cost margins may be viewed as likely to attract entry by new firms, either through green-field investments or through mergers and acquisitions. The former is not likely to take place if there are various barriers to entry, including advantages incumbent firms have which are difficult to replicate or overcome. Also, entry via M&A is not likely if the transaction price is high which is likely to be the case when incumbent firms earn excess profits. Discussions with one of the investment firms indicate this is indeed the case. Due to high reported (and unreported) profits, and very short pay-back periods for their investments, Turkish firms tend to over-value their firms and demand high acquisition prices. For such reasons, there have been very few outright mergers involving foreign firms in Turkey. Most transactions are for acquiring stakes in or joint-ventures with existing firms, which while bring in new investment, do not necessarily increase the prevailing degree of competition in the industry.

productivity and foster sustainable growth. Indications are that steps to improve and implement policies in many of the above noted areas are being taken. The International Management Development's (IMD) World Competitiveness Report (2005) indicates that overall, Turkey's competitiveness is on the rise. In 2004 it ranked 55th out of 60 economies whereas in 2005 it ranks 48th. Also, FDI is predicted to grow as much as US $ 8 billion as investors show greater interest in specific transactions[15]. However, whether this investment is realized and Turkey continues to enhance its relative competitive position will very much depend on consistent and conscious efforts to improve its economic and regulatory policy framework.

The Importance of Competition

19. Although a competition law-policy is not a panacea for all of the problems discussed above, it is an important if not critical driver for fostering investment and augmenting productivity. However, the mere adoption of competition law-policy does not ensure competition will occur, and competition may exist in industries and markets without having specific competition legislation in place. But, as nations such as Turkey embark on liberal trade, investment and other related market reforms, an important consideration to be taken into account is to what extent are there necessary safeguards to protect, nurture and promote competition. Particularly in preventing important segments of a developing or transition market economy from becoming dominated by few large and politically well connected enterprises? Moreover, empirical experience clearly indicates that it is very difficult to inject competitive discipline once firms are dominant or become dominant—particularly when this occurs through poorly conceived and implemented public policies such as selecting 'national champions' or giving preferential treatment in privatization of state owned firms The *ex ante* 'benefits of incumbency' raise even higher the barriers for new entrants.

20. Where an effective competition law-policy plays an important role is ensuring there is a framework for protecting and promoting the process of competition and not competitors. That all firms are treated fairly and equally, and there is accountability and transparency in government-business relations. Also, where this is not the case, there are legal recourse mechanisms to adjudicate and judiciously resolve matters. When properly administered, competition law-policy

[15] See Oxford Analytica (12 May 2005) which lists KocsFina/Unicredito (Italy) interest in acquiring the troubled Cukurova Group's Yapi Kedi bank (YKB); Teliasonera agreement to buy 27% interest in Turkcell, and prospects for privatization of several State-owned assets in the insurance, steel and other sectors. See also Vorkink (2005). Bahri Yilmaz (2003) *"Turkey's Competitiveness in the European Union: A Comparison with Five Candidate Countries—Bulgaria, The Czech Republic, Hungary, Poland, Romania, and the EU15"*(Ezoneplus and Jean Monnet Centre for Excellence) computes Revealed Comparative advantage (RCA) and Comparative Export Performance (CEP) measures for these countries. Briefly Turkey is relatively competitive in raw material and labor intensive products but less so in case of more value-added capital intensive and research based products—areas where FDI generally tends to augment. The Czech Republic and Hungary have been making impressive gains in narrowing the competitiveness gap with the EU15. Both these economies receive in absolute and relative terms more FDU than Turkey.

tends to promote greater coherency and consistency in the government's economic management and policy decisions. It broadens opportunities for participation in the economy by facilitating entry through actions designed to prevent abusive business practices, lowering barriers to entry, and competition advocacy in favor of more pro-competitive public policies and economic regulation. In the areas where government interfaces more directly with business such as in public procurement and privatization, effective competition policy reduces opportunities for engaging in corruption. Through these direct and in-direct impacts, increased competition makes business stronger by forcing managers to become more cost effective, focus on productivity, innovation, R&D, and improve product quality and services. And overall results in better allocation of resources and a more flexible, dynamic economy.

21. Drawing on background research conducted by the World Bank Group Figure I indicates that levels, and rate of growth in per capita GDP tend to be higher in countries where *local* markets have higher entry and competition. [16] Analyses of data for another sample of countries finds that net market entry can account for more than 30 percent of productivity growth. Firms facing strong competitive pressures are at least 50 percent more likely to innovate than those not subject to such pressure.[17] In yet another study, improving policy predictability was found to increase the likelihood of new investment by more than 30 percent. And reduction in barriers to competition in such sectors as telecommunication and electricity can bring a surge of new investment.[18]New entrants stimulate incumbent firms to increase productivity to maintain their profits and be more responsive to customers to maintain their market shares. Moreover, economies with greater micro-economic flexibility as evidenced by entry and exit of firms tend to weather better economic shocks.

22. Evidence of the benefits that competition can bring are not lacking in Turkey. For example, during the 1980's Turkey liberalized its financial markets by eliminating controls on interest rates, reductions in directed credit programs, and relaxation of entry barriers. The results? Foreign banks entry led to reductions in overhead expenses of domestic commercial banks and strengthened profits. In addition net interest margins were lowered, cost of capital came down and greater variety of financial instruments and services became available. Positive developments also occurred in areas of financial and operations planning, credit analysis and marketing, and human capital[19]. In the domestic air passenger market, where Turkey has recently liberalized certain routes, prices have fallen by as much as 70

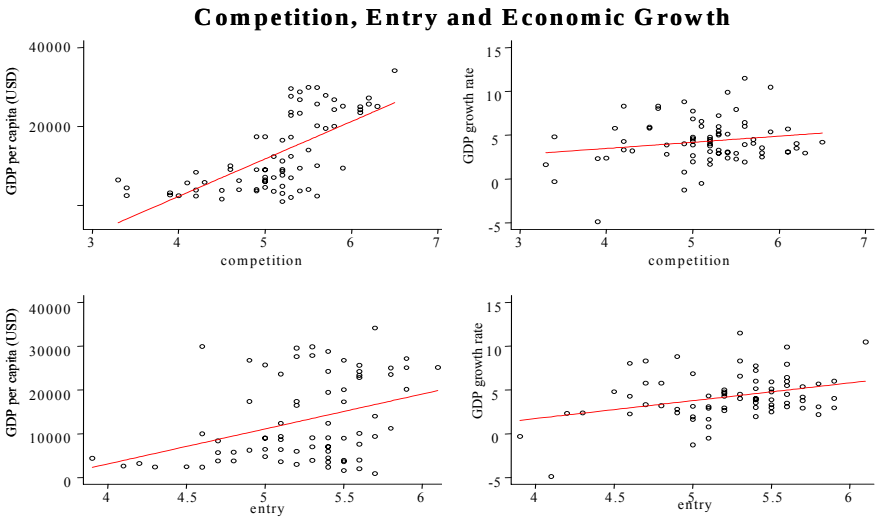
[16] World Bank (2003) Global Economic Prospects Report (2003): *"Investing to Unlock Global Economic Opportunities"*
[17] World Bank (2005) "*World Development Report: A Better Investment Climate for Everyone"*. (Page 3)
[18] Ibid. Page 2.
[19] See Cevdet Denizer (2000) *"Foreign Entry in Turkey's Banking Sector, 1980-1997"* World Bank Policy Research Working paper No. 2462.

percent, and the volume of travel has increased by more than 60 percent. The new entrants have increased frequency of flights and have invested in new aircrafts[20].

The challenge for Turkey is to embrace and expand the application of similar pro-competition policy initiatives to a wider range of key economic sectors. To do so would realize its aspirations to attract greater investment, increase productivity and competitively integrate into the EU and larger global economy.

[20] See Esen Sirel, Sezin Elçin and Sülyeman Cengiz (2005) "*Regulation, Liberalization and Competition in Turkish Domestic Airlines Market"* This paper has been prepared as part of this project and is discussed in greater detain in Section III of this overview report.

Figure-I



Source: World Economic Forum and World Bank SIMA Indicators. "Competition" is the average response in each country to the question "In most industries, competition in the local market is (1=limited and price-cutting is rare, 7=intense and market leadership changes over time)." "Entry" is the average response to the question "Entry of new competitors (1=almost never occurs in the local market, 7=is common in the local market)."

II. The Design & Implementation of Turkey's Competition Law & Policy

Introduction

1. Effective implementation of competition law-policy is more likely to occur when the law and responsible competition agency have at least the following attributes:

    i. The law applies to all economic entities engaged in commercial economic activity—be they owned and operated in the private or public (government) sector.

    ii. The competition agency is an independent body whose decisions are insulated from political, business and/or other stake-holder interference and influence.

    iii. It has reasonable level of financial resources, and expert staff and key decision-makers/management have requisite knowledge and experience in such subject areas as: business, industrial organization economics, finance, competition and regulatory law, and other relevant fields.

    iv. The nature and scope of the law-policy and the mandate of the agency are clearly delineated, especially in its inter-face with other government economic and regulatory policies. The agency is empowered to engage in 'competition advocacy' to promote competition principles in government policy formulation and decisions.

    v. It periodically issues policy statements, procedural and other guidelines, and publishes its decisions to better inform the business community and general public.

    vi. It has an active 'program of compliance' to educate and foster greater adherence and understanding of the law, especially by business.

    vii. Cases are handled expeditiously, decisions are clear and consistent, and there exists provisions for second review, rights of appeal, and a system of checks and balances that ensures accountability and transparency.

    viii. There are complementary provisions for 'private actions' available to injured parties where decisions by the competition authority are viewed as providing insufficient relief and/or compensation for anticompetitive business practices.

ix. In serious infractions of the law, sufficient level of fines and penalties are levied so as to deter future illegal business practices.

2. These features of the economic-legal framework and institutional design ensure 'due process,' reduce uncertainty, and foster greater business and investor confidence in matters that are reviewed by the competition authority.

3. In *large* measure, the Turkish Competition Law and the Competition Authority (TCA) possess most of the above mentioned features. During the past eight years, the TCA has built up a diverse base of case and industry specific, as well as government economic and regulatory policy related experience in its law enforcement and competition advocacy functions. In addition, as unforeseen weaknesses and problems with the application of the competition law-policy have been encountered, the TCA has proposed various amendments and adopted administrative changes to strengthen and improve its effectiveness. *A recent 'peer review' conducted by the OECD (2004) noted that the TCA had made "excellent progress and has developed a reputation as one of Turkey's most effective and best administered agencies"(p.2). This report* ***fully concurs*** *with this view, but there still remains significant room for strengthening the role of the TCA in maintaining and encouraging competition in the Turkish economy.* The effectiveness and the positive impact of Turkey's Competition Authority in fostering competition, productivity and investment has at times been impaired by: (a) the heritage of past as well as continued government policy interventions resulting in monopolistic structures and practices; (b) the lack of a competition culture in both the private and public sectors; and (c) the need for greater delineation and clarity in the respective roles and functions of the TCA vis-à-vis various government departments and agencies regarding the inter-face between competition law-policy and other economic and regulatory policies. While some of these problem areas fall outside the immediate mandate and/or direct influence of the TCA, there remains scope for further strengthening and improving the application of competition law-policy by the TCA itself. These and other points are discussed in greater detail in the ensuing sections.

Salient Features of Turkey's Competition Law[21]

4. In connection with forming a Customs Union with the European Economic Community, Turkey is required to adopt a competition law-policy regime that substantively corresponds to the EU model namely, Articles 81 and 82[22]. As such, Turkey enacted Law No. 4054 in 1995. The main objectives of the law are to protect competition by preventing agreements, decisions and practices that restrict or distort competition in the markets for goods and services. The

[21] For further details an English language version of Turkey's Competition Law can be website:www.rekabet.gov.tr.
[22] Previously Articles 85 and 86 of the Treaty of Rome (1957).

substantial provisions of the Turkish competition law can be summarized under three principal headlines:

5. *Prohibition of practices (agreements concerted practices and decisions) which prevent, restrict or distort competition (Article 4)*

   The definitions and examples of practices falling under this Article are almost identical to those of the European Community competition rules, namely Article 81. It covers such anticompetitive business practices as cartels to fix prices, allocate markets and/or customers, bid-rigging, tying agreements, and other collusive forms of behavior that impede or restrict the ability of existing or new firms to enter and expand their business.

6. *Prohibition of abuse of dominant position (Article 6)*

   This provision is also similar to provisions (Article 82) of the EC Treaty, and covers abuse of market position by one or more dominant enterprises acting together. It is aimed at anticompetitive business practices such as price and non-price predatory behaviors including exclusionary horizontal and vertical agreements, various discriminatory practices, including foreclosing markets for products, inputs, and distribution channels that limit, eliminate and/or distort competition. As in the EU model, dominance is defined as the power of an enterprise or group of leading enterprises to determine prices, output and other economic parameters independently of competitors and customers in the market. No specific market share threshold is specified as determining dominance.

7. *Control of mergers and acquisitions (Article 7).*

   Turkey's competition law prohibits and declares void the merger of two or more enterprises or acquisition by an undertaking or by a person which would create or strengthen dominant market position, and impedes competition significantly either in the whole or a substantial part of Turkey. The TCA is required to issue communiqués to announce categories of mergers and acquisitions (M&A) which are considered legally valid, and require permission by prior notification.

8. Under related provisions (Articles 5 and 8) exemptions and 'negative' clearance certificate may be granted by the TCA for certain agreements and concerted practices, and mergers and acquisitions that are likely to contribute technological and economic progress and enhance consumer welfare.

9. The other salient features of the Turkish competition law are that it applies equally to all enterprises, be they public or private, foreign or domestically

owned, conducting commercial economic activities in Turkey[23]. Public sector (state) owned and operated enterprises are subject to the competition law unless there are explicit provisions in accompanying legal and regulatory policies that permit practices that would otherwise be deemed illegal. Investigations into alleged anticompetitive business practices can be initiated on complaints received from injured parties (competing businesses and consumers) and/or *ex officio* on its own volition by the TCA. In addition, it contains provisions for the TCA to engage in 'competition advocacy' by providing opinions on government policies and regulations that impact on competition. The inherent approach of the law is to prevent anticompetitive business *behavior* and not prevent large firms or market concentration unless it will likely give rise to monopolistic practices.

The Turkish Competition Authority and Competition Board

10. The TCA is established as an independent administrative and financially autonomous body that has the sole responsibility for implementing the competition law. It comprises of an eleven member Competition Board[24] that includes a President and two Vice-Presidents who oversee various technical and other related departments engaged in investigation, financial, human resource and other administrative functions. The technical departments are organized along sector specific lines in order to build knowledge and expertise in the functioning of relevant industries and markets. Annex I provides the organization chart of the TCA. In 2004, the TCA budget was US$ 12.5 million (17.8 Trillion Turkish liras) with a staff complement of 304 persons. Aside from the eleven Competition Board members and 21 senior management staff, the TCA has about 100 professionals with expertise in competition and regulatory economics, law and other related fields. The remaining staff comprise of clerical, technical and other support persons[25].

11. While Board members are appointed by the Council of Ministers based on nominations from the Ministry of Trade, State Planning Office, the Court of Appeals, the Council of State, the Council of Higher Education, and the Turkish Union of Chambers and Exchanges (representing the private sector), they are not subject to directives from any of these or other government bodies and business

[23] Law no. 4054 has been interpreted to also apply to enterprises not engaged in production but sales in Turkey. The acquisition of Tongkook Synthetic Fibres Co. Ltd (South Korea) by E.I. Dupont (US based firm) was cleared by the TCA as both exported to, but had no significant assets in Turkey.

[24] The terms Turkish Competition Authority, Competition Board, and Board are used interchangeably in the ensuing discussion.

[25] The Competition Authority's budget comes from a portion of the fees levied (viz., 0.04%) on the registered capital by newly established corporations, and on existing corporations increasing their registered capital. This approach ensures that the TCA's autonomy is not threatened by the budgetary appropriation and allocation processes of the Ministry of Trade & Industry to which it is deemed related, and/or any other government authority. Under omnibus legislation applicable to all autonomous regulatory bodies being currently considered, the number of seats on all multi-member boards would be reduced to maximum of seven members, with limited one term appointment of six years.

associations. Also, once appointed (for a renewable term of six years)[26], the members can only be removed from office by a court judgment for committing specific offenses. Measures to prevent conflicts of interest and abuse of office after serving as a Board member are also specified in the law. The appointment terms of the Board are staggered, with a third of them renewed every two years, respecting certain ratios of members drawn from the various entities indicated. The eligibility criteria specify certain areas of expertise, education and minimum of ten years of related professional experience

12. As indicated, cases can be initiated based on complaints received or *ex officio* by the Competition Board. Available information shows that only 11 percent of the cases were initiated by the Board—thus the majority of the cases reviewed have been complaint driven. Cases are referred to, adjudicated, and decided upon by the Board. The TCA staff have broad investigatory and evidence gathering powers including entering unannounced company premises and seizing necessary documents. Strict time-frames are set in the competition law for initiating, investigating, hearing and deciding on cases[27]. If on receipt of a substantive complaint, it is decided to conduct a preliminary investigation, it must be completed within 30 days[28]. The Competition Board then has 10 days to decide on launching a formal investigation. The deadline for completion of this investigation is six months, which can be extended for an additional six months if required. Post completion of the investigation, the parties have up to 75 days for rebuttal of charges, with proviso for a further extension of 30 days. Hearings can be requested within a 30 to 60 day window, and the hearings can last a maximum of five days. The Board's final decision must be handed down within 15 days of completion of proceedings. In merger and acquisition cases, prior notification requirements and related time-frames are also specified. Transactions where the parties combined market share will exceed 25 percent or the aggregated sales turnover exceeds TRL 25 trillion (approximately US$ 17 million) must be notified and cleared by the TCA. If however, no action is taken in 15 calendar days, the M&A is deemed to been cleared[29]. The specified time-frames ensure that the process is fairly predictable and cases are handled in an expeditious manner. However, appeals of Board decisions are quite common, which delay the final resolution of cases. Between 1999 and 2004, about 45% of the Board decisions were appealed to the Council of State. The EU in its progress report

[26] As indicated in end-note 4, legislative proposals to reduce the size and limit the term of members of autonomous regulatory bodies is currently being considered. This reduces the probability of having such boards becoming a 'sinecure' for favored and politically connected individuals.

[27] The TCA must inform parties within 15 days of commencement of an investigation. Copies of any evidence against them must be supplied, and no decision can be made by the Competition Board on information not available to the parties, and not given the right to defense. Other safeguards such as holding of hearings, including 'in camera' to safeguard business confidentiality are also provided for.

[28] Systematic information is not available on the time taken between receipts of complaints the TCA decides to conduct a preliminary investigation. Some businesses have complained that the TCA is not as expedient in handling initial complaints as it is once a formal investigation is underway.

[29] If however the notification form is incomplete and/or additional information is requested by the Board, the 15 day period only starts when such documentation is viewed complete.

noted that in 2004, only 21 out of 196 cases were concluded in the judicial review process.

13. In the course of conducting investigations, the TCA can impose interim relief orders where serious and irreparable damages may occur to competition, such as driving out or undermining a competitor from conducting viable operations. In addition during a preliminary stage of inquiry, the Competition Board may provide an opinion to an infracting party how it can stop violating the Law. However, this provision has been interpreted as not being sufficiently broad enough to terminating an investigation at any stage and settling matters by a 'consent decree', as is the case in many other jurisdictions[30]. This tends to limit the ability of the Board in avoiding costly litigation and creating incentives for greater compliance with the law. This also adversely impacts on the ability of the TCA in adopting 'leniency' and 'whistle blowing' programs which several jurisdictions, including the EU have adopted[31].

14. The decisions are written and published by the TCA and in the official gazette, respecting business confidentiality. Some commentators have however pointed out that there is considerable delay in the publication of the decisions. The decisions can be appealed to the Council of Ministers which may be up-held, reversed and referred back to the Board. One of the controversial features is that the investigations are led by one of the Board members. Although this was envisaged to allow for informed decision-making, it calls into question and compromises the principle of separation of investigation and adjudication functions normally recommended in judicial processes[32].

15. Another controversial area relates to the 'burden of proof' in cases of 'concerted practices' under Article 4 of the law. Concerted practices may come about in highly concentrated (oligopoly) markets due to inherent interdependencies between firms in their pricing, output and other business decisions in order to respond to and meet competition. However, under the Turkish Competition Law, each firm, in order to avoid liability, has to prove that this is the case and not due implicit or covert cartel behavior on "….proven economic and rational ground"[33].

16. As indicated above, the law also enables the TCA to provide opinions on policies and regulations referred by other government ministries, issue exemptions and 'negative clearances' on business arrangements and market situations that do not

[30] An amendment to the law to this effect is currently under consideration.
[31] Under such programs a party or parties may plea or be offered lenient treatment for violating the law if it agrees to provide evidence against others engaged in the illegal activity.
[32] Statutory amendments to rectify this situation by eliminating Board member participation in investigations are currently being put forward. However, in the interim, the State Council has reversed the Competition Board decisions in some 40+ cases, which seriously reduces the effectiveness of the competition law.
[33] For further discussion, see Gonenc Gurkaynak (2002) *The Problem with Turkey's Competition Regime"*. International Financial Law Review. As the writer points out, this is fundamentally different from the EU principles.

result in infractions, issue communiqués relating to its mandate and administrative practices, and perform other related functions. These and other safeguards ensure that the Turkish Competition Authority and Board not only constitutes an independent and autonomous agency, but are not likely to be 'captured' by political, business or other stake-holder interest groups.

Nature and Scope of Cases Reviewed.

17. Tables 1 to 10 provided by the Turkish Competition Authority indicate the range and type of matters handled under the Competition Law No. 4054 until the year 2003. Cumulatively, the TCA has received 2576 applications alleging anticompetitive business practices and market situations of which 2103 matters were concluded (Table 1). More than half of these matters, namely 1140 (Table 5) relate to issues that were rejected as either not being substantive or falling outside of the scope of the law and responsibilities of the TCA. This high number is likely due to the lack of general knowledge and/or information relating to the nature and scope of the law and mandate of the TCA—quite understandable given the transition nature of the Turkish economy, and newness of the competition law and institutions. However, it is also indicative of the need for the TCA to conduct more public information and dissemination activities, as this would cut down unnecessary administrative time spent on unrelated matters[34]. Between 1997 and 2003, such cases have increased from 4 to 265 (seeTable5). While indeed the TCA has held various national and international conferences and workshops, a more targeted program may be warranted, particularly aimed at business associations (of small and medium sized enterprises), consumer groups and other civil and non-governmental organizations across different regions. Generally speaking, these are more likely to be the source of such complaints.

18. In each year, a significant number of matters are concluded, as well as new cases opened. The proportion of files carried over from one year to the other, have been declining suggesting that as experience has developed, there is increased efficiency in handling cases. However, at the end of 2003 a significant large number of cases, viz., 473 matters remained pending and were carried over into the following year (see Table 2). Moreover, as the EU has noted in its progress report on Turkey, a high percentage of the decisions by the Competition Board are appealed, and there are a large number of cases that are pending in the judicial review process.

[34] On a related note, Gamze Őz (2005) *"Legal and Institutional aspects of Competition Policy in Turkey and Its Impact on Investment"* reports that a survey (unpublished) of judges and lawyers of the Ankara Bar reveals lack of "necessary means and skills to investigate the underlying facts and undertake an economic analysis….may lead to undesirable results in the enforcement of competition law….and cause inconsistency of decisions." (page 37).

19. There were 212 substantive cases (Table 3) that fell under Article 4 or 6 and the two combined. As mentioned, Article 4 primarily relates to illegal agreements, concerted practices and business decisions that impede competition by enterprises engaging in price-fixing, restricting output, allocating markets and/or customers, and other discriminatory price and non-price behavior. Article 6 covers situations of abuse of market position by one or group of dominant firm(s) such as price and non-price predation, tying arrangements, prevention of entry and/or expansion of firms into the market. Over the review period, the total numbers of cases under the two provisions of the law are about the same (namely, 83 vs. 76 matters). Relative to other jurisdictions, with competition laws, the incidence of these cases is quite high. This is likely reflective of the heritage of past protectionist policies and government interventions in the Turkish economy, and the lack of a competition culture it has fostered. For example, in one particular case matter resolved by the Competition Board, the City of Ankara granted to a commercial firm BELKO Ankara Kömür the monopoly rights to import and sell coal. Other firms were prohibited by the City from engaging in the market. As a result of complaints, BELKO was charged with excessive pricing and abuse of dominant market position. The City subsequently abolished the monopoly rights granted to BELKO in compliance with the Competition Board's opinion (See Box 1).

20. Table 4 provides additional information on the actions taken by the Competition Authority, including whether the agreements were horizontal or vertical in nature, the amounts of fines (sanctions) imposed as well as merger cases handled. Among the Article 4 cases, it is notable that more cases relate to horizontal than vertical agreements. Moreover, in recent years there have been more such cases than abuse of dominance (Article 6). The Table also indicates that the total level of fines imposed (also when computed on an average fines per case basis) tend to vary and do not display any trend. However, infractions relating to merger and acquisition cases are imposed less sanctions. Some critics have suggested that the TCA has a lax treatment towards M&A activity. A counter-argument would be that such activity represents an important vehicle for restructuring industry to exploit available efficiencies, entry and expansion into markets, and domestic and foreign investment. More in-depth analysis of the changes in market structure and impact of M&A activity would be beneficial in this regard.

Cartel, Price-Fixing and Other Illegal Agreements Investigated.

21. Some of the cartel and price-fixing cases, including bid-rigging and market sharing agreements, that have been successfully prosecuted by the TCA relate to products such as cement, bakeries, bus services, poultry, distribution of news papers and periodicals, corrugated containers, fertilizers, sale of advertising time on TV channels and insurance. In cement there have been a number of cases, including repeat offenders. Anticompetitive practices in some of these products, especially cement and fertilizers, have also been experienced in other transition market, as well as, advance economies suggesting industry and market specific factors at play (e.g., homogeneity of products) and not just country specific

characteristics. The TCA has also successfully challenged the fee-setting and entry restriction policies of several professional associations. These include associations of architects and professional engineers, and tourism and travel agencies. In the case of the former, the TCA argued that the authorizing statute did not explicitly permit the association to set prices for architect and engineering services. In the case of the tourism and travel agencies, the association was found to setting unjustifiably high registration fees which deterred entry of new firms. However, in the cases of associations dealing with the medical, dental and legal practitioners, the TCA has been less successful as the enabling laws authorize setting of fees as well as qualification entry standards[35].

22. In the area of vertical restraints, the TCA has generally played a less active role in prosecuting matters. This stance is quite appropriate given the pro-competitive, investment and efficiency enhancement aspects of many voluntary vertical contractual relations between upstream and downstream suppliers of goods and services. The relatively few cases that have been investigated pertain primarily to resale price maintenance which dictates minimum prices retailers can charge for products, restrictive distribution arrangements which prevent dealers from making sales in territories of other dealers and suppresses 'intra-brand' competition, and tying contracts. With respect to the last practice, in 2002 the TCA took action against a ports operator that specified vessels use a particular port services company. This tying arrangement prevented entry and competition by other port service agents. In another matter, the Competition Board ruled against the exclusive requirements imposed by manufacturers that prohibited cigarette retailers from displaying brands of competing manufacturers on the same display-racks.

23. The TCA has also re-assessed previous exemptions granted so as to more closely align its policies with that of the EU. Among the matters reviewed and revoked include an exemption granted to a bank that required retail establishments to honor only its brand of credit card. Another case pertained to allowing a dominant firm to enter into 'non-compete' contracts with retailers carrying solely its brands of products in the 'salty snacks' market. The third matter related to exclusive contracts with food retailers by a firm providing on-line order services to customers. In all these cases the previously issued exemptions were re-assessed as creating barriers to entry without enhancing economic efficiency. Since 2002, the TCA has essentially harmonized its policies regarding vertical restraints with that of the EU[36]. The convergent approach being adopted not only facilitates greater competition, but lowers regulatory and transaction costs for European and domestic firms in their vertical contracting relationships of doing business in Turkey.

[35] See OECD (2005) op cit; Rekabet Kurumu (Turkish Competition Authority): Annual Reports on Competition Policy Developments in Turkey (various years); __Implementation of Competition Policy in Turkey 1997-2003, (Ankara 2004).

[36] Further information can be found in OECD (2005) op cit and references cited therein.

Abuse of Dominant Market Position Cases Investigated

24. In the area of abuse of dominant market position, the cases that the TCA has primarily focused on relate to practices which raise entry barriers or exclude competition. In the major cases litigated, the dominant firms abusing their market position have been operating primarily in regulated sectors and are presently, or previously State owned/controlled entities. For example, a number of cases have arisen in the telecom and electricity sectors which are discussed in greater detail in the next Section (III) of this Report. Briefly, Turkcell, which is partly State owned and another firm Telsim, were found to exercise joint-dominance over the essential infrastructure required to provide national roaming capability by competing GSM mobile telephone service companies. This exclusionary practice was deemed illegal and the Competition Board imposed the single largest fine totaling to TRL 30.4 trillion (approx. USD 20.4 million) on the two firms. However, the execution of the Board's decision and collection of the fines has been stayed by the Council of State, pending appeal by the parties. Another telecom case relates to Turk Telekom (TTAS)--the State owned monopoly providing land line infrastructure services. The Competition Board found TTAS of excluding competition by charging discriminatorily high prices to independent service providers (ISP) offering dial-up internet services in competition with its own subsidiary operation. In a subsequent matter, TTAS, which is also the only provider of ports for ADSL broad band high speed telephone line based service, refused to allocate ports to other competing ISPs. As a result of the Board's actions, TTAS ceased its practices until access rules for firms could be worked out. In the electricity sector, a company (ÇEAŞ) that was granted a monopoly concession for the distribution and transmission of electric power in one of the designated areas, refused to provide system interconnections to independent power generating facilities. The company was fined (TRL 9.5 trillion or approx. USD 6.4) and ordered to cease its practices. Other abuse of dominant market position cases have arisen in the distribution of liquid carbon-dioxide, and also coal namely, the BELKO case which was mentioned above. These cases are illustrative of the anticompetitive market structures and consequent anticompetitive business practices that existing or past public policy and regulatory interventions facilitate. Considering that many of the products and services are important inputs in the production processes of other firms, they result in higher costs, lower profitability and reduced investment that undermine competitiveness.

Merger & Acquisition Transactions

25. Tables 7 and 8 indicate that the vast majority of merger, acquisition and joint-venture cases are allowed to proceed. Of the total of 531 such cases, 287 fell within the scope of the law. Two hundred and fifty-six transactions posed no significant issues, 29 were allowed to conditionally proceed on basis of structural and other undertakings, and only two cases were prevented. In a large number of

the mergers and joint-ventures, the transacting parties are either solely foreign firms and/or domestic with foreign firms. There appear to be fewer transactions involving only domestic firms. It is notable that foreign firms have also participated in privatization transactions, suggesting adoption of principles of 'national treatment' by the TCA and Turkish government. The overall pattern of M&A activity corresponds to that of advanced and experienced antitrust jurisdictions where the vast majority of mergers and acquisitions are permitted to proceed. In some cases these transactions are permitted to proceed with certain conditions in order to safeguard competition. For example, a proposed joint venture (JV) between Migros Türk A.S. and Metro AG (which also entailed FDI into Turkey), was allowed to proceed in certain markets but not in others given their existing presence. In addition, in markets where the JV was permitted, the two super-market chains agreed not to enter into the same market as separate entities in order to preclude the possibility of anticompetitive horizontal price and/or market share agreements that would otherwise be facilitated. However, an application for forming a joint venture between 39 firms to supply liquefied petroleum gas (LPG) was completely rejected. Here the JV was clearly aimed at increasing concentration and coordinating prices between competing entities. Another case that was not permitted acquisition via privatization of a fertilizer manufacturing firm (IGSAS-Toros Gübre after taking into account factors such as barriers to entry and resulting dominance in the relevant markets[37].

26. Table 9 provides an overview of the industrial sectors where applications of infringement of the competition law have been investigated. The most frequent and highest incidence occurs in food & beverage, transportation, telecommunications, and the chemical & petroleum products. As previously mentioned, there have also been numerous cases in the cement sector. Further analysis of disaggregated data and cases is warranted before drawing any conclusions but Mumcu and Zenginobuz (2001) note that sectors such as chemical & petroleum products have high levels of concentration, barriers to entry and state owned firms. These sectors also display a high incidence of M& A activity (Table 10). In transportation there are various regulations at the local and national level that facilitate anticompetitive practices. In food & beverages, there is low import penetration, and in the beverage segment, concentration levels are quite high. Table 10 indicates extensive restructuring has taken place across the various sectors. As already noted, there have been a high number of M&A transactions in chemical & petroleum products than in other sectors. The sector with second highest level of M&A activity was food & beverages. The case examples cited above, which are considered as among the more significant matters reviewed by the TCA, are also illustrative of these general trends.

[37] Serdar Dalkir and Ekrem Kalkan (2004) *"Predicting Potential Welfare Effects of Actual and Hypothetical Merger Proposals in the Turkish Privatization Program"* (mimeo) analyze the IGSAS-Toros case using a merger simulation model. They find that the transaction, if permitted would have given rise to increased prices in the nitrogenous fertilizer market and support the TCA's in preventing the merger as part of the privatization program.

27. The majority (90%) of the cases investigated by the TCA are complaint driven. An overly aggressive application of competition law can adversely impact on investment and economic efficiency. In this connection M&A activity is an important vehicle for restructuring industry, facilitating entry and domestic and foreign investment, exploiting scale economies and other synergies between firms. The pattern of cases reviewed, including the level and diversity of M&A activity, suggests that the enforcement actions of the TCA are balanced, with focus on the most egregious anticompetitive practices of illegal agreements, concerted actions and abuse of dominance by firms.

28. The deterrent effect of the law against anticompetitive business practices and M&A activity has also been called into question. In 2003, the Competition Board imposed fines in 13 out of 303 cases concluded. Moreover, in no case has the maximum allowable fine been imposed. And until a recent amendment, most fines were not paid or collected while the cases were being appealed.[38] In addition, there is significant variation in the fines imposed, and the basis on which they have been determined is not clear. No communiqué or guidelines on the principles used to calculation of fines and other remedies have been issued. Also, it appears that the briefs prepared by experts on cases to the Competition Board do not indicate the nature and extent of damages, and/or the allocative and other cost distortions, or the magnitude of the illegal profits earned by firms that result from anticompetitive practices. Such analysis would guide the Board in better assessing the level of fines that ought to be paid by the firms in order to penalize, recover costs, and deter infractions of the Law.

Exemptions, Exceptions and Limitations in Application of Competition Law

29. The Turkish competition law allows for certain 'block' exemptions (Article 5) and 'negative clearances' (Article 8) from application of provisions dealing with agreements or concerted practices, or mergers and acquisitions, by enterprises or decisions of associations of enterprises if they are likely to lead to new developments and technological progress in production of goods and services that benefits consumers and does not eliminate competition in a substantial part of the relevant market. Under these and related conditions, an exemption or negative clearance certificate can be granted for a period of up to five years, which can be renewed if circumstances continue to warrant. This provision allows for flexibility in the application of competition law so as not to unnecessarily inhibit innovation, change and modernization in industries and markets. As Table 5 indicates, the TCA authority has granted or conditionally decided in favour such clearances in the vast majority of applications falling within its scope.

[38] The appeals and judicial review of Competition Board decisions has made it difficult to collect fines which reduce the deterrent effect of the law. An amendment to the law introduced in 2004 requires fines to be paid within 90 days of the Board's decision whether or not an appeal has been made to the State Council. As payment of fines can impose a heavy financial burden on the firm and its operations, the Council can grant a stay in the execution of the fine pending hearing of appeal, and/or can require posting of a bond by the appellant(s).

30. However, aside from this discretionary authority, there are areas where the application of the competition law may be limited by other laws, regulations and government actions. Examples relating to setting of fees and entry restrictions in professions such as medical and legal practitioners have already been mentioned. Also, in the wake of the 1999 financial crisis, emergency legislation was adopted to exclude bank mergers from the purview of the competition law[39]. Bank mergers are controlled by the Banking Regulation and Supervisory Agency. The competition law is also not applicable to State agencies and bodies, including State owned enterprises that may be created by specific legislation. For example, in a case involving abuse of dominant market position by a state owned sugar firm (TFA), the Competition Board ruled the matter as falling outside its mandate as the sugar prices and policies were determined by a government ministry. Similarly, the health ministry regulates the prices of many pharmaceutical products. To be fair, similar jurisdictional issues and frictions between the competition authority and other government laws, regulations and bodies (at both the national and sub-national) level exist in other countries as well[40]. However, for transition economies with a long history of state interventions, such situations tend to adversely impact on a greater portion of the economy.

31. The TCA has issued various communiqués with respect to the substantive provisions and application of the law. An additional communiqué dealing with the area of 'program of compliance' would be useful--that is how the TCA balances its law enforcement responsibilities and fostering voluntary compliance to avoid costly litigation, through such measures as 'consent decrees' and business advisory opinions. Also, the TCA should be mindful that the burden of the law falls more heavily on small than large businesses, and expand its program of information dissemination and compliance measures towards this segment of the business community. In this connection, establishing *de minimus* thresholds and principles for exempting certain agreements between such types of firms would reduce uncertainty. For example, small businesses wishing to form 'buying groups' to counter the market power of large firms and/or collectively exploit transaction and other efficiencies could be one such area where such an exemption could be envisaged.

Competition Advocacy

32. Articles 27 (g) and 30 (f) of the Turkish Competition Law empower the TCA to provide directly or upon application to the Ministry necessary amendments to be made in the competition legislation, and also provide opinions on legislation and decisions concerning competition policy. Using this authority, the TCA has not been shy in engaging in 'competition advocacy' where deemed necessary and important. Available statistics indicate that since the year 2000, the TCA has

[39] However, bank services such as loan rates, issuance and contracts relating to credit cards, various fees and charges are still covered under the competition law.
[40] For example www.internationalcompetitionnetwork.org and the publications and papers relating to competition advocacy.

issued an increasing number of opinions on various government policy and regulatory matters: from 16 in the initial year to a peak of 42 in 2003, and 25 in 2004.

33. A sample of matters where the Competition Board has provided pro-competition arguments and/or attempted to stem the intrusion of public policies into the proper functioning of markets is indicative of the wide range of issues that have been confronted. Among the range of markets and industries that have been covered (among others) are: petroleum, natural gas, electricity, hypermarkets for consumer goods, ports, press, banking sector, bankruptcy, accounting, and more recently state aids.

34. For example, the Competition Board strongly objected to a draft law prepared by the Ministry of Industry regarding the establishment of hypermarkets that contained measures limiting competition between large and small retailers. The draft bill proposed restrictions on the establishment and location of large retailers, and their pricing and marketing strategies, in order to protect the smaller retailers. In addition, it contained provisions that overlapped and conflicted with those found in the existing competition law. In advancing its arguments, the Board referred to structural developments in other countries, the impact of changing technologies and the adverse impact on entry, investment and consumer welfare the proposed bill would have. While the bill is not dead, it is not expected to advance further.

35. In another matter the Board conveyed to the Izimir Chamber of Commerce that proposals by the Unions of Artisans and Tradesmen to fix prices of bread, meat and related transportation services would violate the competition law unless it was clearly stated that these were maximum or recommended prices. With respect to a draft bill regulating the distribution of magazines and other periodicals, the Board was successful in amending provisions relating to exclusive dealing contracts between distributors and retailers in favour of non-discriminatory treatment of competing distributors. In banking, the new Bank Act (1999) eliminated differences between public and private banks. However, interventions through Budgetary Acts continued in the selection of banks where public institutions and organizations would deposit their funds. The Board has supported the Turkish Union of Banks position that such discriminatory practices be removed through amendments to the Budgetary Act and Bank Act.

36. From these examples, it is evident that the TCA's competition advocacy activities can stem in a number of ways. In addition, it has also engaged in competition advocacy as an integral part of investigating cases where public policies have facilitated anticompetitive situations and practices—as the BELKO case illustrates. However, not with standing the various opinions and interventions that the TCA has actively engaged in, the outcome or impact of its interventions, except in the above noted examples, is not always evident. A follow-up analysis of specific interventions would be advisable, and publicize the positive impact of

improved competition or lack thereof. In addition, examination of various competition advocacy activities by the TCA suggests that it tends to be more re-active than pro-active in its interventions. It would be beneficial to conduct more systematic competition and regulatory impact assessments of key sectors where public policies and industry practices are distorting competition.

37. It needs to be noted that the Competition Board is not always requested to provide its opinions and/or that it does not become aware of new policy and regulatory proposals in a timely fashion. Also, the load of other law enforcement and case matters relating to fulfilling its overall mandate are likely factors. Successful competition advocacy requires timely actions. In this connection, it may be noted that the Prime Minister's office had issued a communiqué (in 1998/2001) encouraging various government departments and agencies to consult the TCA in advance on proposals and regulations that impacted on competition policy. But not all government agencies necessarily comply with this request or welcome the TCA's opinions. This introduces inconsistencies in the way regulatory policies are formulated in respect to competition related matters. For example, the OECD in various reports points out the differences in the interface between the competition law-policy and the laws dealing with the telecommunications and electricity sectors. The Telecommunications Act requires consultations between the TCA and Telecommunications Regulatory Authority (TRA), but the same is not the case in regards to the Energy Market Regulatory Authority (EMRA). In practice, the opposite is the case. The TCA and EMRA have established a protocol for periodic consultations while the relationship between the TCA and TRA are somewhat acrimonious according to some commentators[41].

38. The European Union has specifically indicated that Turkey needs to adopt state aid legislation and establish a state aid monitoring authority. Given the build-up of the diverse experience in assessing competition in a wide range of industries, and how different public policies can distort markets, the TCA has argued that the EU's requirements on violations of competition and supervision of state aid are tasks that are integral to the effective implementation of competition law, and that these functions should be assigned to the Competition Authority. Moreover, its independent standing, and the parallel nature of Turkish competition law with the Treaty of Rome articles 81 and 82, better position it to meet these obligations. It would also remove the possibility of conflicts and overlapping responsibilities if another agency were to be created to monitor state aids. These arguments certainly merit consideration. However, thus far no decision has been made in this regard by the Prime Minister's office. The EU has noted the lack of progress and that the TCA is quite well staffed and trained in administering competition law-policy.[42] In its overall assessment, the EU states:

[41] See OECD (2002) op cit, page 81, and OECD (2005) op cit, page 38. Also the discussion with respect to these two sectors in Section III of this Report.
[42] See Page 92.

39. "In the field of anti-trust rules, harmonization with the *acquis* appears reasonably well advanced. However, the state aid framework Law has not been adopted, and therefore, no alignment with EC Treaty rules on state aid control. Major efforts concerning alignment in the adjustment of state monopolies and companies having exclusive and special rights are needed. An efficient enforcement of all competition rules must be ensured and the role of the Competition Authority in the economic policy-making process needs to be strengthened considerably."[43]

Concluding Observations and Remarks

40. In the relatively short span of eight years, Turkey has made significant progress in the implementation of competition law-policy. The major provisions of the Law parallel that of the European Union, and the Turkish Competition Authority has deservedly earned a reputation of being a professional, well administered and competent body in discharging its mandate. As various legal, institutional design and other problems have been encountered, the TCA has sought amendments and changed its administrative and other practices to improve its effectiveness. Through both enforcement actions and competition advocacy, it has not shied away from trying to rectify anticompetitive business practices and government policy interventions, and put forward more pro-competition alternatives. However, as indicated in the preceding discussion, there remain significant challenges in fostering competition in various segments of the Turkish economy. The pro-investment and competitive impact of the TCA is often thwarted by other government economic policies and regulations. This is particularly the case in infrastructure service sectors such as electricity, telecommunications, and transportation—all providing important inputs into the production processes of downstream economic activities. The experience of other countries suggests that these sectors are important drivers for increasing investment, productivity and competitiveness. The Government of Turkey should accord priority to clarifying and delineating the role and functions of the TCA vis-à-vis other regulatory bodies in these areas. It also needs to adopt a more integrated approach towards fostering competition, and where possible give precedence to competition policy considerations in general and sector specific regulations and policy interventions, where at present there is a proclivity to unnecessarily limit prices, output and entry in markets. Given the expertise acquired by the TCA in assessing competition and efficient functioning of various industries and markets, the Government should consider expanding TCA's role to include monitoring and controlling anticompetitive state-aids, consistent with the Customs Union Agreement with the EU. Not to do so would result in costly duplication and conflict with the mandate of the TCA to foster competition. In this connection, it may be re-called that the *OECD Review of Regulatory Reform in Turkey* (2002) pointed out that governance and regulatory structures were weak and contributed to the 2001 economic crisis, and:

> "Competition policy institutions are in place and active, but competition policy is not yet fully integrated into the general policy framework for regulation. Many features of state-led development remain. Reforms have been announced, but implementation is slowed by crisis. The lack of public awareness about competition policy and the new institutions is indicative of the uncertain status of competition in public policy and debate." (Page 83).

[43] Ibid. Page 94.

Elsewhere, the OECD Report while commending the reform efforts underway pressed for accelerating the "depoliticisation" of the public sector and fighting corruption.

41. It is recognized that policy actions in this regard do not fall directly within the ambit or control of the TCA. Decisions in this regard will need to be made at higher Ministerial levels such as the Prime Minister's Office and/or through legislative changes. None the less the TCA could be more vocal in its position, and also support its arguments by documenting the costs that various anticompetitive practices and policies impose on enterprises, consumers and the economy generally. And by doing so promote more informed policy decision making. At present, most of its case briefs, particularly on competition advocacy, tend to be 'polemic' in nature. It should also consider being more pro-active and stepping-up its competition advocacy function instead of primarily providing input into policy changes when requested. In addition, a number of the amendments to the law put forward by the TCA and others require actions: The particular proposals that would encourage a better investment climate include:

    --Changes in measures to expand 'consent orders' and providing business advisory opinions.

    --Clarifying and issuing of a communiqué on factors the TCA considers in assessing fines and acceptable remedies.

    -- Expand its staff in-house training and other educational programs in areas as economics of fines', conducting competition and regulatory impact analysis of public policy based interventions.

    -- Adopt a more strategic and targeted approach in information dissemination and program of compliance activities, in both public and private sectors. With respect to the latter, particular focus should be on small and medium sized firms, local and regional governments and areas, and in-house legal practitioners in firms.

    --Establish *de minimus* principles for exempting agreements involving small firms, including such areas as forming of 'buying groups'.

    --Expedite the publication of recent case decisions and the key factors that were considered by the Competition Board, including dissenting view-points.

    --Reduce the back-log and number of cases carried forward each year. Also, clearly indicate the TCA policy and time-frame in responding to initial complaints.

In addition, the TCA should consider re-visiting its communiqués relating to mergers, acquisitions and joint-ventures not only in light of changes in this regard to bring it into greater harmony with EU guidelines, but also detailing the methodologies employed in assessing various competition related factors such as market definition, barriers to entry and 'market power'.

Finally, the TCA should consider expanding the English language version of its otherwise well constructed web-site to include more cases, communiqués and other documents of likely interest to the international investor community.

TABLE 1- Applications and Files Concluded (5.11.1997-31.12.2003)

		1997	1998	1999	2000	2001	2002	2003	*TOTAL*
Infringement of Competition	**Application**	22	177	220	255	213	265	406	**1558**
	Concluded	9	44	306	262	211	217	303	**1352**
Merger/ Acquisition	**Application**	8	59	80	103	82	115	113	**560**
	Concluded	5	52	76	101	88	102	107	**531**
Exemption/ Negative Clearance	**Application**	0	245	44	41	42	35	51	**458**
	Concluded	0	12	64	23	52	31	38	**220**
TOTAL	**Application**	30	481	344	399	337	415	570	**2576**
	Concluded	14	108	446	386	351	350	448	**2103**

TABLE 2- Files at the End of the Year (1997-2003)

	Application	**Concluded**	**Transferred to the coming year**
1997	30	14	16
1998	481	108	389
1999	344	446	287
2000	399	386	300
2001	337	351	286
2002	415	350	351
2003	570	448	473

TABLE 3- With Regard to the Files Concluded by Final Decision as a Result of Initial Examination or Preliminary Inquiry/Investigation, Their Distribution by Relevant Articles of the Act No. 4054
(1997-2003)

(Excluding Those Rejected or Deemed to Have Been Rejected due to Considering Unworthy of Examination and Those Deemed to Fall Outside the Act)

	Article4 Agreements & Concerted Practices	**Article 6 Abuse of Dominant Market Position**	**Articles 4 and 6 together**	**TOTAL**
1997	2	3	0	**5**
1998	3	2	0	**5**
1999	9	10	13	**32**
2000	21	16	16	**53**
2001	12	19	10	**41**
2002	18	15	5	**38**
2003	18	11	9	**38**
TOTAL	**83**	**76**	**53**	**212**

Table 4 Trends in Competition Policy Actions[1]

	Horizontal Agreements[2,5]	Vertical Agreements[2]	Abuse of Dominance[2,4]	Mergers[3]
2004: matters opened	24	14	32	92
Matters in progress	15	5	10	3
Matters concluded	39	19	41	107
Total sanctions imposed (TRL million)	15,601,915	7,649,830	2,488,607	14,853
2003: matters opened	40	8	28	91
Matters in progress	30	10	19	18
Matters concluded	28	7	27	81
Total sanctions imposed (TRL million)	4,567,638	5,198,582	39,960,321	35,372
2002: matters opened	38	7	24	65
Matters in progress	18	9	18	8
Matters concluded	39	4	28	61
Total sanctions imposed (TRL million)	22,956,113	317,169	1,136,376	2,908
2001: matters opened	20	7	26	39
Matters in progress	19	6	22	4
Matters concluded	16	9	16	46
Total sanctions imposed (TRL million)	172,234	7,877,954	1,799,225	949
2000: matters opened	17	11	18	57
Matters in progress	15	8	12	11
Matters concluded	16	12	25	51
Total sanctions imposed (TRL million)	1,193,663	515,894	-	608
1999: matters opened	18	12	24	30
Matters in progress	14	9	19	5
Matters concluded	4	3	5	25
Total sanctions imposed (TRL million)	4,320	-	-	-

1. Data are for applications of the Competition Act by the Competition Authority, and do not include negative clearances, exemptions, opinions, and matters determined to be irrelevant under the Act.

2. The total number of non-merger matters opened in 2004 was 70; in 2003, 76; in 2002, 69; in 2001, 53; in 2000, 46; in 1999, 54.

3. Includes mergers reviewed in privatisation proceedings but excludes mergers that were below notification thresholds or otherwise deemed out of scope.

4. Includes cases in which both Articles 4 and 6 were applied.

5. Includes cases in which both horizontal and vertical agreements were involved.

Source: OECD Peer Review of Turkey's Competition Law and Policy: Note by the Secretariat, and Turkey, 2005.

TABLE 5-Concluded Applications Concerning Infringements of Competition (1997-2003)

	Those Concluded by Final Decision As a Result of Initial Examination or Preliminary Inquiry/Investigation	Those Rejected or Deemed to Have Been Rejected due to Considering Unworthy of Examination	Those Deemed to Fall Outside the Act	TOTAL
1997	5	1	3	**9**
1998	5	36	3	**44**
1999	32	38	236	**306**
2000	53	62	147	**262**
2001	41	40	130	**211**
2002	38	81	98	**217**
2003	38	115	150	**303**
TOTAL	**212**	**373**	**767**	**1352**

TABLE 6- Negative Clearance/Exemption Decisions (1997-2003)

	Exempted	Granted Negative Clearance	Conditionally Decided	Out of scope	Those that are not exempted or granted negative Clearance	Total
1997	0	0	0	0	0	**0**
1998	1	11	0	0	0	**12**
1999	11	17	21	15	0	**64**
2000	5	8	6	4	0	**23**
2001	16	13	19	4	0	**52**
2002	12	11	7	1	0	**31**
2003	11	10	16	0	1	**38**
Total	**56**	**70**	**69**	**24**	**1**	**220**

TABLE 7- Decisions for Mergers, Acquisitions and Joint Ventures (1997-2003)

	Those Permitted	Those Granted Conditional Permission	Those Not Permitted	Those Deemed Out of Scope	TOTAL
1997	1	0	0	4	**5**
1998	25	6	0	21	**52**
1999	31	1	1	43	**76**
2000	46	3	1	51	**101**
2001	39	4	0	45	**88**
2002	54	6	0	42	**102**
2003	60	9	0	38	**107**
TOTAL	**256**	**29**	**2**	**244**	**531**

TABLE 8- Nature of Mergers/Acquisitions (1997-2003) (Excluding those out of scope)

	Mergers						Acquasitions						Joint Ventures						Privatizations					
	99	00	01	02	03	04	99	00	01	02	03	04	99	00	01	02	03	04	99	00	01	02	03	04
Foreign-Foreign	2	4	2	3	2	3	8	19	17	28	29	48		1	1		3	3						
Domestic-Foreign		1			1		5	6	13	14	18	14	4	4	4	2	4	2		1			2	3
Domestic-Domestic				2	2	1	4	9	4	13	10	5		2	2	4		2	1	5			8	10
Total	2	5	2	5	5	4	17	34	34	55	57	67	4	7	7	6	7	7	1	6	0	0	10	13

Table 9: Distribution by Sectors of Applications for the Infringements of Competition

	99	00	01	02	03	04
Printing and Publishing, Reproduction of Records, Cassettes and Similar Media	1	4	2	6	0	3
Furniture, White Goods, Toys, Sports Equipment, Musical Instruments, Jewelry	0	2	1	1	0	0
Office Equipment and Computer	0	1	1	0	0	3
Glass	0	0	1	0	1	1
Iron and Steel	0	2	1	0	0	1
Metal (Except Iron)	0	0	0	0	0	0
Electricity/Electronics	0	1	0	0	0	0
Electricity/Gas/Water	0	0	0	2	2	3
Financial Services	1	1	1	1	2	2
Food Products and Beverages	2	8	2	8	9	17
Cement, Construction Equipment	0	0	0	2	1	3
Pulp, Paper and Paper Products	0	0	0	0	0	0
Land Vehicles, Aircraft, Sea Vessels and Railway Carriers	2	1	3	2	0	5
Chemical Products, Petrochemicals, Petroleum Products, Fertilizers	0	3	8	6	4	8
Mine and Mining	0	2	2	0	1	2
Machinery and Equipment Manufacturing	0	1	1	2	0	1
Clay and Ceramics	0	0	1	0	0	1
Plastic and Rubber Products	0	0	0	0	0	0
Health, Education, Sport, and Self-Employment Activities	2	2	2	3	11	9
Agricultural and Livestock Breeding, Forest Products	0	3	1	2	1	3
Textiles and Ready Made Clothes	0	1	0	0	0	0
Telecommunications	1	1	3	6	10	14
Medical Instruments, Optical Instruments	0	0	1	1	1	1
Tourism	1	0	0	0	1	0
Tobacco Products	0	0	0	2	1	4
Transportation	1	7	6	9	6	9
Others	0	0	3	0	1	1

Table 10.Mergers and Acquisitions

	99	00	01	02	03	04
Printing and Publishing, Reproduction of Records, Cassettes and Similar Media	0	1	2	1	1	4
Furniture, White Goods, Toys, Sports Equipment, Musical Instruments, Jewelry	1	0	0	2	1	1
Office Equipment and Computer	0	2	0	6	3	1
Glass	0	1	1	0	1	0
Iron and Steel	0	1	1	2	0	4
Metal (Except Iron)	0	0	0	0	1	0
Electricity/Electronics	0	0	4	4	5	5
Electricity/Gas/Water	0	1	1	1	2	6
Financial Services	2	2	1	6	1	3
Food Products and Beverages	6	7	1	9	10	5
Cement, Construction Equipment	0	4	4	1	5	0
Pulp, Paper and Paper Products	0	1	0	2	8	2
Land Vehicles, Aircraft, Sea Vessels and Railway Carriers	4	5	6	4	2	5
Chemical Products, Petrochemicals, Petroleum Products, Fertilizers	3	19	10	11	19	27
Mine and Mining	0	0	0	1	3	6
Machinery and Equipment Manufacturing	1	2	4	2	5	5
Clay and Ceramics	0	0	0	0	0	0
Plastic and Rubber Products	0	0	0	2	1	1
Health, Education, Sport, and Self-Employment Activities	0	0	0	2	1	0
Agricultural and Livestock Breeding, Forest Products	0	0	0	0	1	0
Textiles and Ready Made Clothes	3	1	2	1	0	2
Telecommunications	1	2	2	3	4	0
Medical Instruments, Optical Instruments	1	0	0	0	1	0
Tourism	0	0	0	0	0	0
Tobacco Products	1	0	0	0	1	0
Transportation	0	2	2	3	1	5
Others	1	2	0	2	2	7

BOX-1

BELKO CASE

The Belko case is illustrative of how ill-conceived public policy can give rise to anticompetitive market structure and behavior, and the effectiveness of competition law enforcement and advocacy in remedying the situation. The case also clarified the objectives of Turkish competition law, its scope of application, principles used to define the relevant market, and approach towards such issues as what constituted 'excessive prices'.

In June 1999, the Turkish Competition authority (TCA) received a complaint that the City of Ankara Governor's Office Board of Hygiene had granted to "Belko", a private company the *sole* right to import and sell coal used for heating purposes. Importation and sale by other firms was prohibited. In effect, the Ankara city government via regulation had created a monopoly and had simultaneously prevented new entry. The TCA conducted an investigation and in hearings which included written and oral arguments and evidence, the Competition Board determined that:

--The relevant market was imported fragmented coal for heating purposes in the city of Ankara and neighboring areas.

--The product is a basic commodity that had no close substitutes in context of factors such as consumer preferences, legal regulations etc.

--That Belko was a dominant firm and had abused its market position by charging excessively high prices. It had been granted monopoly position legally by city regulations, which also foreclosed the market to new entry, and its prices were not subject to competitive discipline. The city had not put in regulations to prevent abuses and measures relating to pricing and pricing strategies, and the company was therefore subject to the Competition Law 4054.

An An administrative fine was imposed on Belko of TL41.023 billion (US$___). In addition, the City of Ankara Governor's office was informed of the Board decision, and also recommendations on how to establish a competitive environment for coal. The city subsequently abolished the monopoly right granted to Belko.

In gauging "excessive prices" the Board did considered concepts such as the competitive pressures that normally would be generated by potential competition, which was non-existent in the case due to regulated barriers to entry. It determined that Belko's excessive prices were in part due to not high profit margins but inefficiencies and high costs—itself an indicator of lack of competition.

The Competition Board in its decision stated:"….*As the main purpose of the competition law is the elimination of problems resulting from concentration and particularly the protection of the community from excessive prices, toleration of monopolistic pricing which is one of the major practices leading to them, is contrary to this purpose……qualifying as legal the monopolistic pricing which generally has a heavier cost over social welfare sets contradiction ….with the purpose sought by the competition law…."*

The TCA has tried to assert (not always successfully) where possible its jurisdiction in matters dealing with infringement of competition, even when other government policies and regulations may seek to mandate otherwise.

III. Competition and Regulatory Issues in Selected Key Sectors

Introduction

1. As indicated in the preceding discussion, Turkey's competition law-policy inter-faces with a number of sector specific and general economic policies and regulations. The objectives of these policies and regulations may not always be consistent with promoting competition, and frictions arise. Given the benefits that usually flow from competition, the challenge for different authorities and policy-makers is how best can competition be safeguarded while also meeting other social, economic and political objectives? This Section first examines some of the nature and type of competition issues that have arisen in Turkey's electricity and telecommunications industries. Generally speaking, when regulatory and related policy-institutional reforms are properly instituted, these two sectors become major drivers for attracting a large proportion of domestic and foreign direct investment. However, a study by MGI (2003) points out that during the past decade, Turkey received a very small fraction of the total FDI in the electricity and telecommunications industries when compared to countries such as Poland, Brazil, Chile, Czech Republic and Argentina.[44] Among the major impediments identified are the continued monopoly presence of state owned enterprises due to the slow pace of privatization, and a non-level playing field confronted by private enterprises. Also the lack of a clear regulatory framework and policy reversals, which have injected uncertainty. This Section also discusses competition and regulation issues in two additional sectors of the Turkish economy namely, the domestic airline passenger and fast-moving consumer goods markets. In recent years, the prevailing state of competition in these two sectors has improved significantly. The material presented draws on four studies commissioned as part of this project and other related reports[45].

Electricity Sector

2. Turkey has been engaged in reforming the electricity industry during the past two-decades, including opening up much of its power generation segment to private sector participation. However, the process has been of a 'stop-go' nature and there have been several reversals of policy decisions that has not bode well for investment and productivity[46]. In addition, due to the lack of a

[44] Op cit., page 87.
[45] See Gamze Öz (2005); Esat Serhat Guney (2005); Izak Atiyas (2005); Esen Sirel et al (2005). See also, McKinsey Global Institute (2003) and OECD (2002).
[46] As previously mentioned (Section I, Para 14) in 2001 the government cancelled 46 contracted BOT and TOR projects and despite the constitutional court decision, the matter of reinstating the contracts or compensating the investors remains pending.

clear legal-regulatory framework, various opportunistic and anticompetitive behavior has occurred. Although 'reforms' permitted Build Operate and Transfer (BOT) and Transfer of Operating Rights (TOR) projects with long-term purchase contracts, competition did not occur as the state remained the sole buyer. While legal unbundling of various segments in the electricity supply chain (generation, transmission, distribution) was instituted during the 1990's and lastly in 2001, again the state remained the sole monopoly or in dominant control in different segments. For example, while the state entity EÜAŞ operates 61% of Turkey's total installed generation capacity the state-owned TETAŞ controls 85% of the wholesale market. Similarly, the state entity TEDAŞ has a 73% share of the total electricity distribution infrastructure and supplies 95% of the customers.

3. A study by MGI indicates that Turkey has the high transmission and distribution loss (19%)) when compared to countries such as Mexico (15%), Hungary (13%) and Greece (7%) among others. In some regions such as Anatolia losses are as high as 70%. There are also significant productivity gaps. Total Factor Productivity (TFP) of Turkey's electricity sector stands at 75% of that of the United States. It is 60% in transmission and generation. While capital productivity is above 90%, what pulls down Turkey is low labor productivity (37% of US measures in generation, and 21% in transmission and distribution)[47].

4. In terms of nominal Kilo-watt per hour (KWh) prices, Turkey is 21% above the OECD average for industrial users, and 25% below the OECD average for residential users of electricity. In terms of purchasing power parity, it is much higher on both accounts (170% and 69% respectively)[48] However, as in most countries, the ratio of residential to industrial price ratio is higher than one (between 1.02 to 1.09) implying a policy of cross-subsidization in favor of residential customers—largely due to political efficacy in regulatory pricing decisions.

5. To effectively meet Turkey's electricity demand, both domestic and foreign direct investment will need to be energetically marshaled. Estimates of the required investment vary. MGI places it between US$ 32-45 billion in generation alone (for the period 2001-2011) whereas a high growth demand scenario suggests amounts as high as US$91 billion (by the year 2020). Regardless of which estimate is considered, it translates to between US$ 3.2 to US$ 5.7 billion per year—three to five times the FDI Turkey receives per year for all sectors of the economy. Clearly the problem of the investment gap is urgent. There is some evidence that this is recognized in government policy circles. Recent legislation such as the Energy Market Law (2001) and the Foreign Investment Law (2003) coupled with espoused plans for accelerating privatization and de-regulation are in the right direction. However, credibility

[47] See MGI (2003) pages 166-167.
[48] MGI op cit. Similar price statistics are also contained in Esat Serhat Guney (2005)

of these initiatives will depend on consistent follow-up actions, most notably the proper design and implementation of an accountable and transparent legal-regulatory framework and governance structure. The risks that the government will not use the privatization program to obtain high transaction prices at the expense of competition, so as to fund other needs of the treasury cannot be ruled out. Indeed some potential investors have stated that they are unlikely to invest unless the electricity market is genuinely competitive and various laws-policies are made more coherent and consistent with one another; there is a more level playing field between state-and private sector entities; and the slow judicial processes are improved, including incorporating international arbitration in agreements[49].

6. These concerns are not unfounded, given the history of government policy changes and reversals, but also the anticompetitive practices investigated by the Turkish Competition Authority (TCA). Between 1999 and 2004, seven complaints were brought to the attention of the TCA. One related to ÇEAŞ, a privatized state company that was acquired by a family group whose operations included a long term concession granted by the Ministry of Energy and Natural Resources to transmit electricity. Two autoproducers complained that ÇEAŞ did not sign or obey existing provisions of agreements to provide access to the transmission facility. The TCA determined that ÇEAŞ had abused its dominant market position of an 'essential facility' (namely the transmission lines) by denying third party access, and hindered competition. The company was fined TL 9.5 trillion (approximately US$7 million) and was required to alter its business practice. The second major case related to TEDAŞ, the state owned electricity distribution company, which was accused of abusing its dominant market position by increasing the electricity prices at more than the inflation rate. The investigation by the TCA was dropped because the company had not made large profits, and high prices were more due to high costs and inefficient operations, which could only be corrected by structural changes that fell outside the Competition Authority's mandate.

7. In addition to the forgoing cases, the TCA has reviewed a twenty-two mergers and acquisitions (M&A) in the electricity sector between 1998 and 2004. Fourteen of these transactions were between solely foreign owned firms or foreign and domestic firms. All cases were cleared, some on a conditional basis. In 2004, six of the eight M&A transactions in the electricity sector involved foreign firms—a significant increase over previous years where such transactions averaged one or two. This increase could in part be due to changes in the laws mentioned above, and also foreign firms positioning themselves for increased investment and operations as market liberalization continues. Clearly, the administration of the competition law has not impeded foreign investment.

[49] See Esat Serhat Guney, op cit

8. Pro-competition initiatives by the TCA worth mentioning are the review of 17 privatization transactions of electricity distribution assets by TEDAŞ. In these transactions, the TCA was successful in preventing price discrimination and transfer of further operating or production rights without its review. Other recommended measures such as removing or limiting the exclusivity clauses in concession agreements, allowing distribution companies to set prices independently within a given band, and permitting large customers to purchase electricity from alternative source could not be realized until enactment of the Electricity Market law (2001). The TCA provided input into the drafting of this legislation. In addition, to avoid frictions and problems between the jurisdiction of the TCA and the Energy Market Regulatory Authority (EMRA) the two bodies entered into a protocol to meet periodically to review matters impacting on their respective mandates.[50]

Telecommunications

9. The Turkish telecommunication sector has also not only been subject to various policy changes and reversals, but also to some of the most egregious anticompetitive business practices fomented by the state owned/controlled entities. The relationship between the TCA and the Telecommunications Authority (TA) has been "less than satisfactory"[51]--even acrimonious, according to some commentators. This has arisen in large measure because of ambiguity in regulatory policy and split jurisdiction between the TCA and TA. The competition authority interprets its jurisdiction to extend over anticompetitive practices in the telecommunications sector, whereas the telecoms sector regulator holds the view that it does not. In 2002, a protocol of cooperation was signed between the two authorities to meet at least on a quarterly basis to review and resolve competition related issues that may arise. A coordination committee was established requiring each to provide written opinions before decisions on competition issues are made, but in practice these arrangements have not worked well.

10. Various studies on the telecommunications sector indicate that:
    - Overall the state of competition in the sector has improved over the past decade. And there has been new domestic and foreign investment. But, this is significantly less than other EU ascension candidate countries and the EU average. According to one study, in Turkey investment in telecommunications runs at 11.9% of sector revenue compared to an average of 29.7% for other EU candidate countries, and 23% EU average.[52] Significant regulatory governance and other challenges remain to be addressed, and are preventing attracting

[50] Esat Serhat Guney, op cit provides further details.
[51] Izak Atiyas (2005) *"Competition and Regulation in the Turkish Telecommunications Industry"*,
[52] Erkan Akdemir, Erdem Başçi and Gareth Lockley (2005) "*The Turkish Telecommunications Sector: A Comparative Analysis"* in Turkey Economic Reforms & Ascension to the European Union, edited by Bernard M. Hoekman and Sübidey Togan, The World Bank and CEPR. Page149.

investment, increasing productivity and achieving the full potential that the sector could contribute to Turkey's economic growth and development.

- Ninety percent of total telecommunications revenues are from wire-line and wireless services. There has been rapid growth in both segments, and relative to its income level, Turkey has achieved wireline penetration rates similar to developed countries although on a lines per capita basis it's below the OECD average. In wireless telecommunications, the growth rate has been much faster and the penetration rate is comparable to countries with similar income levels.
- In nominal terms, wireline fixed charges in Turkey are lowest among OECD countries, and usage charges are close to the OECD average. However, in purchasing power parity terms (PPP) they are much higher. In either nominal or PPP terms, international calls in Turkey are 60-80% higher than the OECD average, and also higher than all countries including central European countries. Through increased competition and lower prices, usage and concomitant productivity increases could be achieved.
- McKinsey Global Institute estimates that total factor productivity (TFP) is around 64% of the US level. In the wireline, where not much liberalization and competition has taken place, TFP is around 66%. Due to state-monopoly, distorted management focus and incentives has led to inadequate capital investment in improving the infrastructure and further automation, and developing the market for a wide range of services that line telecom companies offer in other countries. In the more competitive wireless segment the TFP index is 59% and is attributed licensing terms which have created substantial network redundancy, which has lowered capital productivity, higher prices and much lower output. Lack of national roaming at fair prices, high interconnection charges, and high consumer taxes further exacerbate the situation against increasing usage and productivity improvements.[53]
- While Turkey has relatively low internet access costs (on a PPP basis), it has a very low number of house-holds with internet connections

11. The TCA has investigated and levied fines in a number of cases relating to mainly abuse of dominant market position by incumbent telecom companies including state-owned Turk Telekomunikasyon A.S (TTAS) which until recently had statutory monopoly over fixed line infrastructure and voice services. The major cases relate to:[54]

    (i) Restrictive practices in the mobile handset and telephony market.

[53] Op cit. Pages 125-26, and 140-142.
[54] See Atiyas (2005) for further details.

In this case Turkcell, which had market share in excess of 65% of total subscribers, instituted agreements with retail distributors of major brands of handsets such as, Ericsson and Panasonic that prevented them from marketing competing brands with SIM cards and subscriber lines. In addition, it imposed various re-sell price restrictions, exclusivity contractual terms, and penalized distributors that did not adhere to its terms. The practices made it difficult for the complaints to access distributors and enter the market to compete effectively.

(ii) National Roaming, Essential facility Doctrine and Mobile Infrastructure.

This case related to the joint dominance of Turkcell and Telsim over the GSM infrastructure. These firms were accused of refusing access to their infrastructure which would have enabled competing companies to offer national roaming service. And require them to invest in duplicate and possibly redundant GSM infrastructure, which in any case would take significant amount of time and prevent them from entry and expansion in the market.

(iii) Access to Internet Infrastructure and Competing Internet Service Provision (ISP).

The Association of Internet Service Providers complained that the Turk Telekomunikasyon A.S (TTAS), which had monopoly over wirelines had doubled the tariffs for leased lines used by ISPs with no apparent increase in costs, refused to rent Primary Rate Interface (PRI) lines and instead forced them to rent Virtual Points of Presence (VPOPs) installed under its subsidiary. In addition, TTAS engaged in a number of other anticompetitive markets such as, predatory pricing in the market for residential internet services, limiting the capacity leased to ISPs, forced ISPs to disclose confidential commercial information relating to customers, and increased royalties to be applied to satellite earth stations by 240-6300%

12. The OECD (2002) amongst others has called for measures to ensure that regulations and regulatory processes in the telecommunications sector are transparent, non-discriminatory and applied effectively. Also to reform the regulations to stimulate competition, and to strengthen the scope and effective application of competition law-policy.[55] It is critical for Turkey to address these issues. As various research shows, a competitive telecommunications sector is positively associated with investment, competitiveness and higher economic growth.[56]

[55] Op cit. Pages 156-57.
[56] See for example, Waverman, Leonard, and Lars Hendrik Röller (1997) *" Telecommunication Infrastructure and Economic Development: A Simultaneous Approach"* Competitiveness and Industrial

Domestic Air Passenger Travel Market

13. Until recently, the Turkish domestic air passenger travel market was served solely by the state-owned carrier, Turkish Airlines. Since October 2003, the government has relaxed regulations and allowed private carriers to service various routes. As a result, due to new entry, increased competition, lower prices and greater choice, domestic air passengers increased by 63% in 2004. In addition, the increased passenger traffic was not only in new private carriers but also in Turkish Airlines due to its lower airfares caused by competitive pressures, and 'net-work effects' of higher usage of air transport services.[57]

14. While no single factor can legitimately claim to have caused the change in government policy towards domestic air services market, it is note-worthy that in 2001 the TCA provided an opinion report arguing in favor of opening up the market to private enterprises. In addition, the 'demonstrative effect' of the experience in other countries, including the various EU liberalization initiatives likely played a role to play. None the less, although the recent initiatives are in the right direction, and have already resulted in positive benefits such as new entry, investment and increased employment, more needs to done to secure competition and realize potential productivity gains.

15. Among the pro-competition measures recommended by industry and other experts are:
    - Complete efforts to fully privatize Turkish Airlines. Currently 1.8% of the shares are privately owned and previous efforts to sell 20-30% could not be realized due to global economic crisis. However, new entry and investment is not likely to occur where the state carrier will continue to be a dominant player without measures of accounting transparency, and a clear legal-regulatory framework.
    - Clearly establish the rules and regulatory framework governing airline code-sharing agreements and strategic alliances. Various studies and empirical experience point to increased operational efficiencies and net-work economies of scale from such arrangements, but also potential for anticompetitive practices, and therefore need to be counter balanced.
    - Review and revise current policies on allocation of landing/airport slots on a more competitive basis, such as through abolition of historical rights given to Turkish Airlines and periodic auctions. Presently, slot allocations are provided by the State Airports Authority and Turkish Airlines, the involvement of which creates conflict of

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Change. CEPR Working Paper No. 1997 Also: Waverman, Leonard, Meloria Meschi and Melvin Fuss (2005) *"The Effect of Wireless Telecommunication on Economic Development in Africa"* Presentation at American Enterprise Institute, Washington DC, USA

[57] For further details see Esen Sirel et al, op cit.

interest in terms of increasing competition and entry. The Turkish Airlines is responsible for allocating slots until the last three days and the State Airport Authority allocates them in the last three days—which hardly facilitates planning and investment decisions of competitors. Moreover, the historic rights clause further entrenches the incumbency benefits of Turkish Airlines.

- Adopt clear accounting and audit standards and institute transparent reporting measures Turkish Airlines allegedly receives direct and indirect subsidies—which are not compatible with EC Treaty obligations, disadvantage competitors.
- Liberalize the licensing of airport ground handling services to encourage greater entry and competition. Currently, two companies (Havas and Celebi) provide such services and the duopoly structure results in reduced competition. Each of the firms is licensed to service specific airports and there appears to be no turnover or change in the airports they service—even though the licenses are valid for given periods. Each firm has 50% of the ground handling service markets.

16. These recommendations would further cement the tangible benefits that both the industry and consumers have realized in the short span since the government has initiated policies to increase competition and entry in the domestic airlines market.

FMCG Retail Market

17. One of the sectors undergoing dynamic change in Turkey is the Fast Moving Consumer Goods (FMCG) retail market. This sector consists of a wide range of products purchased by house-hold consumers such as food, beverages and other grocery items, tobacco, pharmaceuticals and medical good, cosmetic and toilet items, etc. Food items account for about a third (32%) of the total volume of sales followed by such items as textile apparel and footwear (11%), household appliances (9%), hardware (7%) and pharmaceuticals (9%) among others. The sector contributes about 11% to Turkey's GDP and 8% of employment. In terms of GDP, this sector is larger than in other major developing and transition market economies viz., India, China and Brazil.[58] The major retail and wholesale trade, and different product segments have important linkages with agriculture and various manufacturing establishments. Given its relative importance, both public policy and private sector business practices can have wide repercussions on productivity and the investment climate of the country.

18. The principal sales outlets in FMCG consist of hypermarkets, supermarkets, grocery convenience stores, specialized outlets (e.g., green grocers, butchers)

[58] MGI (2003), Data is for 1998. The FMCG sector in Poland is of same size in GDP terms but has a larger share of employment (12%). In US the sector's contribution to GDP is 8% and accounts for 11% of total employment.

restaurants and snack buffets as well as open vendors in bazaars and streets. The available data relates primarily to the organized sector and a significant segment of the sector consists of 'informal' businesses which are estimated to account for more than 40% of total sector employment, and approximately 30% of FMCG retail, and 20% of suppliers' market shares.[59] As various reports point out, the persistent prevalence of 'informality' adversely affects productivity by (i) creating a non-level playing field with respect to establishments in the formal sector, and (ii) reducing the incentives for traditional firms to modernize their operations.[60]

19. Turkey's FMCG is going through rapid structural change. The rapid development and relative importance of modern retail formats has led to various complaints, mainly by incumbent smaller establishments that favor the status quo or wish to limit the degree of direct competition from the larger hyper-and supermarket chains. However, four-firm concentration levels in the retail chain sector are estimated to be between 10.8% and 11.5% of sales—much lower than in many European countries. And while four-firm concentration ratios exceed 50% in some segments of the supplier industries such as dairy, confectionary, fish, spirits, liquor and wines, tobacco, deterrents, amongst others, the competitive dynamics and entry conditions preclude possible exercise of market power and serious infringements of competition law-policy. [61]

20. There are about 195,000establishments in the retail trade segment, with an average size of 2 persons. Entry-exit and rank turnover statistics are not available but given the increase in the total number of establishments was about 10,000 between 1998 and 2001, there appears to be significant fluidity in the industry. Moreover, computations of a 'Trade Restrictiveness Index' (TRI) which covers wholesale and retail trade ranks Turkey low in terms of impediments to establishing domestic retail firms.[62]Also, Turkey has no specific law regulating the retail-wholesale trade markets. Contrary to most other developing and transition economies, there are no significant restrictions on foreign firm entry, and are subject to same national treatment principles as applied to domestic firms. The TRI component relating to establishing foreign retail firms is lower than the average for EU-15 member countries.

21. Some modern hyper- and super-market retail chains in Turkey, including those established as joint-ventures with foreign investors (Migros-Turk), date back to the mid-1950's. However, during the 1990's there has been a surge of foreign direct investment that includes such firms as Carrefour, Promodes,

[59] Aydin Çelen, Tarkan Erdogan, and Erol Taymaz (2005) "*Fast Moving Consumer Goods: Competitive Conditions and Policies"*. Pages13
[60] See MGI (2003) op cit.
[61] Aydin Çelen, Tarkan Erdogan, and Erol Taymaz (2005) op cit., Pages 4-5
[62] The World Bank Group's "Doing Business" indicators also indicates that the number of days required to set up a new business is significantly less than other European countries such as Italy, Poland, Hungary, Slovak Republic, and Spain.

Metro International, and Tesco. Retailers such as Wal-Mart are reputed to be planning entry into the Turkish market. The Turkish Competition Authority (TCA) has examined four cases relating to mergers and joint-ventures involving foreign investors. All of these transactions were permitted to proceed[63]. In addition, the TCA has examined 23 cases regarding complaints by retailers about below-cost (predatory) pricing and discriminatory practices by suppliers. All of these complaints were rejected by the Competition Board given the low barriers to entry and concentration levels, and dynamic market conditions. One of the complaints brought by the Chamber of Small Grocery Shops (Bakkallar Federasynu Odasi) alleged discriminatory pricing and other practices that favored large retailers. However, the Board deemed these practices were not competition infringements since the small and large retailers differed in their volume of purchase, product range and other factors. As indicated in Section II of this Report, small retailers can overcome such situations by organizing and forming 'buying-groups' with certain undertakings regarding their pricing and other behavior to prevent lessening competition. The TCA could consider issuing a communiqué in this connection.

22. There have, however, been two cases where the Competition Board has had to rule against firms engaging in anticompetitive business practices. One related to a complaint brought by the Istanbul Food Wholesale Traders Association (IGTOD) against a number of suppliers that included both domestic and foreign firms. These firms individually had violated the law by imposing sales restrictions on downstream distributors. Among the foreign firms were Procter & Gamble, Marsa Krafts Jacob Suchard, Unilever and LeverElida. In the second case, the foreign firm Frito-Lay was found to have abused its dominant market position in the salty-snack food market by imposing exclusivity restrictions on retailers preventing them from selling competing brands.[64]

23. There are other practices followed by firms in the FMCG sector that could give rise to competition issues, which have also been experienced in other jurisdictions[65]. These include 'price-flexing', which entails price discrimination across local markets and listing and slotting fees for popular branded products, tied selling and various extortionary contract terms. However, the incidence of such practices has not been widespread in Turkey so as to cause serious violations of the law.

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[63] No conditions were imposed on three of the four mergers. One case (Metro-Migros joint-venture) was granted conditional approval but the parties later did not proceed for unrelated reasons.

[64] See Aydin Çelan, et al op cit., also discussion in Section II. These cases led to the TCA withdraw its communiqué and exemption policy with respect to exclusive dealing.

[65] Competition Commission (2000), "*Supermarkets: A Report on the Supply of Groceries from Multiple Stores in the United Kingdom"*, presented to Parliament by the Secretary of State for Trade & Industry (www.Competition-Commision.org.uk). Cases have arisen in the FMCG sector in South Africa, Canada, US, France among others.

24. As can be expected when competitive intensity increases, incumbent firms commence lobbying for protection. Competition authorities, whether in industrial or developing economies need to be vigilant to ensure that markets do not get distorted. Such has been the case in Turkey. In 2001 a draft law was proposed to regulate the establishment of stores with sales area of over 250 square meters. Permission would be required by a special Board consisting of the municipal government, Chamber of Commerce, consumer associations and the TCA. The suggested Board would consider such factors as locational distance from the city center, demand-supply conditions, competitive situation of small retailers. Sores of larger than 1000 square meters would need to be located at least 5 KMs away from the city center. The TCA lodged its objections against the proposed law and subsequent amended drafts which the Ministry of Trade and Industry prepared. The 2003 version excluded restrictions on store size. However, it included redundant provisions relating to predatory prices and other forms of conduct already covered by the competition law. Yet another draft was put on the agenda in 2004 that among other restrictions sought to limit the sales of private label products by large stores to 20%, and low price sales promotions and rebates. The TCA again strongly registered its views that such restrictions limited competition, harmed consumers and small and medium sized manufacturers of private label products for the large retailers. Currently the law is not on the policy agenda of the government.

25. In brief, there are no significant market competition problems or impediments to both domestic and foreign direct investment confronted in the FMCG sector. The problem of informality does impede productivity improvements but this area falls outside the scope of competition law-policy. This also applies to the availability of urban land for entry on medium to large scale in not only the FMCG, but also other service sectors. However, these issues will need to be resolved by other policy initiatives, such as greater enforcement of tax collection among others.

Concluding Observations and Remarks

26. Interventions by incumbent firms, including state-owned/controlled enterprises, and lack of a coherent legal-regulatory framework in the electricity and the telecommunications sectors have impeded competition and productivity improvements. Inadequate regulatory governance has also been attributed to failures in attracting investment. The government needs to attach priority to addressing these issues. The 'blue-prints' to do so are available from the experience of other economies in these industries, including the EU, which Turkey aspires to join. The government, at various points in time, has articulated its goals to further de-regulate and inject competitive market reforms. However, the pace has been recognizably slow, and credible efforts to translate the announcements into concrete actions should be taken in a defined and short time-frame. The benefits that accrue from competition are

clearly observable from the experience in not only the limited experience in the electricity and telecommunications markets, but in such markets as the domestic air passenger market, where also further steps to strengthen and promote competition are feasible, and advisable. In the fast moving consumer goods market, there is dynamic change talking place. Few serious competition issues have arisen. The challenge in this sector is for the government not to intervene, and give currency to pressures from various self-serving interest groups, who seek to limit competition and introduction of new innovative distribution systems.

IV. General Conclusions and Recommendations

1. Pulling the threads together of the preceding discussion, it can be concluded that during the past two decades or so since Turkey embraced market oriented reforms, the state of competition and overall economic performance of the economy has improved (with the exception of the brief but significant recent economic crisis in 2001). Among the various structural reforms and policies that the government has adopted includes the enactment of a general competition law-policy framework. The implementation of this law-policy has progressed well by all accounts—by the OECD and the EU—a view which this Report fully concurs with. The Turkish Competition Authority (TCA) is deservedly considered as amongst the professional and effective government bodies in not only Turkey, but also by its peers within the OECD and International Competition Network. During the past eight years, it has received, investigated, prosecuted and effectively prevented a significant number of anticompetitive business practices as well as engaged in competition advocacy entailing a wide range of markets, industries and public policy and regulatory interventions. In doing so, it has correctly focused on particularly those competition infringements that impact on entry and expansion of firms—critical determinants of not only competition but marshalling domestic and foreign investment. In addition, the application of the law has allowed the vast majority of M&A and JV transactions to proceed. These transactions are the primary vehicles for FDI, as well as for efficient restructuring of industry. It is evident that the competition law-policy has not been applied discriminately, and all firms have been treated equally according to national treatment principles. In the area of competition advocacy, the TCA has been pro-active in reviewing various regulatory policy proposals, some put forward at the behest of self-serving industry stakeholders and interest groups, and often has been able to prevent or mitigate the creation of barriers to entry and competition. In this connection, it has also been able to prevent some privatizations of state enterprises that would have resulted in monopoly or market dominance by the acquiring private sector firm(s).Thus, it can be confidently concluded that through case specific enforcement and competition advocacy activities, the TCA has certainly contributed to improving the investment climate as it relates to specific industries and markets, and also on a broader basis. And through such actions has likely resulted in and/or set the stage for increased competition, investment, and productivity improvements.

2. There are areas where the provisions and application of competition law-policy by the TCA could be further strengthened. These are detailed in greater detail in Section II of the Report and relate to measures to expand the use of consent orders and issuance of business advisory opinions; and more targeted information dissemination and program of compliance in both the public and private sector. The lack of appreciation of the benefits of competition appears to be prevalent, perhaps even more, in the public sector than in the private sector. This would reduce costly litigation, frictions with other public policy

and regulatory bodies, and also lodging of complaints that are not substantive or fall outside the scope of the law. It is also suggested that the TCA issue more communiqués on factors it considers in assessing fines and various remedies, approach to specific competition infringements, and establish *de minmus* principles for exempting agreements involving small firms such as formation of 'buying groups'. Expedited publication of recent cases decided with more details on factors considered and dissenting views, and reduction in back-log of pending cases is also recommended.

3. In addition, there are number of proposed changes in administrative practices and amendments to the competition law that the TCA itself has sought to improve its effectiveness. Among these are separation in the investigative and adjudication functions of the Competition Board members, and suggestions that its mandate be expanded to cover the monitoring and review of state-aids. Some commentators have also suggested that the review of Bank mergers, which were exempted during the recent economic crisis, be reinstated as falling under the purview of the TCA. This Report endorses these initiatives while recognizing that the decisions in this regard do not rest with the Competition Authority but with other bodies such as the Treasury, State Council and the legislature.

4. Many of the egregious competition problems seem to emanate from public policies and regulations, particularly due to ambiguity regarding the jurisdiction of the TCA and other government ministries and regulatory bodies in matters that inter-face with competition law-policy. This is especially the case in the electricity and telecommunications sectors which are critical for attracting investment and enhancing productivity in the economy. The regulatory governance issues need to be addressed on an urgent basis. The TCA has not shied away from asserting its mandate. It should continue to do so, and consider strengthening its arguments with data and information relating to prices, costs, reduced output and services, and who the winners are at whose expense.

5. The suggested actions and continued implementation of competition law-policy, and its greater integration into government economic and regulatory policy decision-making, will result in an improved the investment climate in Turkey. It will foster greater consistency and coherency, and accountability and transparency in dealing with competition related issues. And reduce business uncertainty which will contribute to attracting more investment—the principal driver for productivity, competitiveness and economic growth.

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Competitiveness, Investment Climate and Role of Competition Policy in Turkey

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