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The State Incentives to Oligopoly in Face of Small and Medium-sized Enterprises in Latin America

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Abstract

The participation of Micro, Small & Medium Enterprises (MSMEs) in the economies of the developing countries is essential, at the same time that we face a global increase of enterprises concentration in the sense of creation of large economic conglomerates that have the main world market shares.

The oligopolies' matter, especially in Latin America, is correlated to the democratisation and privatisation processes of the economy of those countries which occurred more intensely in the beginning of the 1990's, after the fall of the dictatorships and infusion of neoliberalism prevailing in the local State policies. Therefore, despite constitutionally most of the Latin-American countries are protected by rules that value the social justice and the distribution of wealth, the globalised economy, through economic liberalism, undertook a process that lead to the current scenario of oligopolistic presence of domestic or international enterprises, although normally with transnational size.

Henceforth, considering those conditions as paradigms of a structural condition conniving with oligopoly and consequently, the lack of incentive to the productive efficiency of MSMEs, there should be a discussion, especially within the Latin America scope, concerning the examples and

references associated to such issues and the possible solutions for implementation of conditions of development for those enterprises and, consequently, provide compulsion to the necessary increase of competition, for the sake of favouring the entire society.

Introduction

According to the last study (2010) of the International Finance Corporation (IFC), a member of the World Bank, there are 125 million formal Micro, Small and Medium-Sized Enterprises (MSMEs) in the set of 132 analysed economies, including 89 million in emerging markets.

The participation of MSMEs in the economies of the developing countries is essential, at the same time that we face a global increase of enterprises concentration in the sense of creation of large economic conglomerates that have most of the world market share.

Those elements generate a challenge that will be emphasised herein, among others, which is the major existence of oligopolies in most of the national markets. Also in 2000, UNCTAD verified the oligopoly in those countries as a major issue to be tackled by governments and the World Bank working in partnership.

The oligopolies matter, especially in Latin America, is correlated to the democratisation and privatisation processes of the economy of those countries which occurred more intensely in the beginning of the 1990's, after the fall of the dictatorships and infusion of neoliberalism prevailing in the local State policies. Therefore, the globalised economy, through economic liberalism, undertook a process that lead to the current scenario of oligopolistic presence of domestic or international enterprises, although normally with transnational size.

In Brazil, as well as in several developing countries mainly in Latin America, three political programmes that created and still perform such condition, among others, are the following:

- the practice of the national champions theory, especially by contributions of public investment, thus building a private relation between the State and the large national enterprise, its stock in the stock exchange and the public interest for the profit;
- the indirect imposition of the government to the antitrust divisions of adopting a lenient posture against the acts of concentration so that certain economic and political agenda is met, despite the fact that in principle they give effect or strengthen the oligopoly, they

- are encouraged by financing and investment in public programmes; and
- lack of parameters of the antitrust division to judge the acts of concentration associated to the legal and normative concepts of social justice and human dignity and preference to those of the merely economic theory of ‘social wellness’ (in excess of the producer/consumer).

Henceforth, considering those conditions as paradigms of a structural condition conniving with oligopoly there should be a discussion, concerning the examples and references associated to such issues and the possible solutions for implementation of conditions of development for those enterprises and, consequently, provide compulsion to the necessary increase of competition, for the sake of favoring the entire society.

The global oligopoly is nowadays the most characteristic form of supply while the centralisation of capital, combined with the decentralisation of production, commercial and financial management, reorganise the economy and geopolitics of the world. The mergers and ongoing acquisition on the planet since the end of the 20th century dramatically altered the international market power relationships, leading economies beforehand domestic to global performance in competitive levels which current boundaries are given by way of interdependence between companies.

In this sense, François Chesnais said that this oligopolistic condition refers to the interdependence between firms, including ‘firms not reacting to more impersonal forces coming from the market, but personally and directly to their rivals’.¹

These take their mutual dependence marketplace, by all kinds of agreements (technical cooperation, joint determination of standards), of which not much fits the antitrust laws.

The constitutive relations of the oligopoly become in themselves, inherently, an important factor of barriers to entry, in which other elements (such as sunk costs or the magnitude of the investments in R&D) can then graft.²

In this scenario, since the 1980s, due to the economic crisis and the consequent adoption of neoliberal doctrine of the International Monetary Fund (IMF) and the World Bank, in force is a political and economic platform of deregulation of the financial sectors of developing countries, included therein Latin America, as well as a process of greater appreciation of the private sector to conduct themselves, of free competition and freedom of contract. The state, therefore, due to this booklet, should work towards minimum intervention in the market and the

internationalisation of the domestic economy as prerequisites for a good management of the economy.

With this policy, due to the inclusion of Latin American countries in a globalised international market, foreign direct investment rate (FDI) increased considerably. In Argentina, for example, while in 2000 the stock of FDI was about US\$21,140mn, in 2010 jumped to US\$29,840mn. In Brazil, in 2000 it was US\$51,946mn and in 2010 it went to US\$188,637mn. In Chile, in 2000 the amount was US\$11,154mn and reached the level of US\$60,146mn in 2010 – and then there was a considerable increase in all Latin American countries.³

This wave of internationalisation of Latin America economy has taken place since the 1990s, with the expansion of business in this region from various sectors of economic activity into new markets abroad.

Big Business and Oligopoly: Key Factors of Dissociation with a Defence Policy of SMEs

Normally, the predominant perspective in studies on internationalisation focusses on companies in the internal factors that lead to this phenomenon.

In Latin America, there was a significant increase in FDI from the 1990s, a time when the economies of the region, from the neoliberal policies of the IMF and the World Bank, have adopted plans of monetary stabilisation and implemented market-oriented reforms (privatisation). More open to a growing oligopolistic competition, Latin American countries have seen some of its largest companies develop strategies to reach overseas markets as well as access to capital and technology.

However, we intend to draw attention to the effectiveness of the role played by the government to the success of multilatinas not only as deregulation agent of domestic economies but also in an attempt to foster by economic dynamism, including the promotion of expansion of certain companies. The trend of concentration of wealth and market in the hands of a few business leaders is one of the consequences of such policy, as the antitrust agencies cast a blind eye to major mergers and acquisitions (M&As) in the analysis of mergers.

Efficient international expansion of multilatinas depends much, simultaneously, of inorganic growth through acquisitions and joint ventures. Considering overseas acquisitions, compared to Latin companies of local operations, those of global reach make on average almost four times more joint venture operations and six times more business M&As.

What must be considered about the oligopoly capitalism in Latin America is that, 'in decreasing the base of accumulation that is relevant to capital, capital its own is responsible for destroying the excess of capital in operation. Companies break, obsolete or surplus production structures are eliminated, acts of the capital centralisation process, to keep running the capital in a smaller base of accumulation, with higher profits for those who remain'.⁴

Mexican and Brazilian economic conglomerates dominate the list of top investors abroad, followed by Chile and Argentina. Chile, in turn, has the largest number of companies on the list such as retailing and distribution of energy. Obviously, they are 'champions' in the concentration and centralisation of capital in their countries of origin in order to control much of varied economic activities.

On the emergence of national champions companies, says Leandro Bruno Santos, based on Michalet: "the multilatinas are those champions after a long historical process of concentration and centralisation of capital in their home bases under state support. The author relates the theory to a concrete situation, but it cannot be assumed that all multilatinas will be domestic champions, because it depends on historical and spatial conditions or otherwise, the particular conditions of each socio-spatial formation. The concentration and centralisation remain important as theoretical parameters, while the role of the state which had been raised should be analysed for its relevance in the broader process of capital accumulation and power."⁵

The specific concept of 'national champions' is considered by some scholars restricted in Latin America, Brazil, in the face of the policies of the National Bank for Economic and Social Development (BNDES). This Bank, a financial institution of the government, acts since 2002 practically performing loans to big companies in order to invest for the consolidation of those on the global stage. This purpose, namely, to encourage large domestic companies to become victorious competitors in the international market is the so-called 'theory of national champions.'

The economic policy of national champions is not restricted to direct, positive, monetary investment, but is part of a set of factors observed in much of Latin America, factors of which are the permission of certain concentration acts which would be in the government's aim.

What happens is the following: "we find a direct participation of the State not only to allow for the economic concentration, but also for its promotion. Such interference occurs always, in our view, for the sake of an irrational logic of preserving a biased structure of the concentration of

wealth in capitalism. We see therefore a reversal of nationalisation of enterprises: privatisation of the state in which it passes to undergo ever more intensely to gains and losses inherent in the market game.”⁶

There is, therefore, an indirect imposition of governments to antitrust agencies to adopt lenient stance in the face of mergers to fulfill certain political and economic agenda. Advocates, for example, Giovanni Dosi, an Economics Professor at the School of Advanced Studies Sant’Anna in Pisa, Italy: “I propose that developing countries build domestic oligopolies able to compete with foreign oligopolies, both nationally and internationally.”⁷ For the supporters of this theory, there is no contradiction between competition policy advocacy and market concentration, especially if taken into account the global market.

The consequence is thus a “shared power without the need for overt collusion; the identity price is the general rule, and competition takes the form of physically indistinguishable differentiate products through design and particularly through advertising.”⁸

The national champions, therefore, ‘can benefit from loans guaranteed by the state or implicit support raising the rating of its debt and reduce borrowing costs. It also helps access to natural resources, specific budgetary allocations, tax benefits and exemptions by supervisory authorities.’⁹

In Argentina, for example, in 2007, in the cement market, the Antitrust Commission confirmed that three companies dominated 96 percent of the business. In short distance fixed telephony, Telefónica and Telecom controlled 80 percent of the market. After the engulfing of Quilmes by Ambev, 81 percent of the beer consumed in Argentina comes from a single Brazilian company. The Cablevision-Multicanal merger happened stating that, nationally, these two firms held ‘dominant’ position, with 51 percent of cable TV subscriptions.

Still, from 1999 to 2006, the *Comisión Nacional de Defensa de la Competencia*, Argentine antitrust agency, analysed 489 economic concentration, of which 94 percent were authorised, only five percent were subordinated to the fulfillment of any condition imposed by the agency and less one percent was denied.¹⁰ i.e. low rates of impediment and even subordination to conditions in view of the amount of concentration led to the Argentine agency.

It is still worth considering that there is an obligation of analysis by the agency as they fall within the following thresholds (Law 25,156, article 8): acts involving the participation of companies or groups of companies in a quota equal or greater than 25 percent or more of the relevant market;

or when the sum of the total turnover in the country of all the companies concerned is more than the sum of US\$200mn; or even when the total turnover worldwide, of all the companies is more than US\$2,500mn, i.e. only large companies are subject to examination by the antitrust agency.

In Brazil, in turn, according to Law 12.529/11, the Conselho Administrativo de Defesa Econômica (CADE, the Brazilian antitrust agency) should analyse the merger that portray one of the following: at least one group involved in the operation has registered in the last balance sheet, gross annual sales or total turnover in the country, in the previous year to the operation, equivalent to or greater than R\$ 400,000,000.00 (four hundred million reais); and at least one other group involved in the operation has registered in the last balance sheet, gross annual sales or total turnover in the country, in the previous year to the operation, equivalent to or greater than R\$30,000,000.00 (thirty million reais) (Art. 88, I and II). As it turns out, it is also of great size and relevance of companies in the domestic market.

The oligopoly is also present vehemently in Brazil. In partnership with the British counterpart Edmund Amann, the expert in Brazil Werner Baer, Professor of the Department of Economics of the University of Illinois (US), investigated 19 sectors of the country and found a strong concentration in 14 of them, in which the top four companies hold over 60 percent of the market. The branch with less competition is the petrochemical, with a 91 percent rate; automotive industry (85 percent), wholesale trade (80 percent), mining (79 percent) and food and beverages (76 percent) respectively. The broadband internet in the country, in turn, in 2014, was controlled by just four companies: Hi, Telefonica, Net and GVT. They dominated 90 percent of broadband in the country.¹¹

But even with very high levels of concentration in the Brazilian market, CADE, from January to July 2015, judged 192 cases of mergers, approving restrictions with 5 of them and not condemning any.¹²

In Chile, the Subsecretaría de Telecomunicaciones (telecommunications agency) reveals that in 2013, three companies of this sector concentrated 98.7 percent market share, with 37.34 percent Movistar, Entel 37.26 percent, and Claro 24.11 percent. The Chilean national air traffic, in turn, as reported by the National Board Aerea in 2010 was concentrated on LAN Express (40.8 percent) in the SKY Airline (16.9 percent) and LAN Airlines (38.7 percent). With regard to pharmacies, the newspaper Estrategia News informs that this sector is concentrated, in 2010, in three companies, namely: Salco (25 percent), Fasa (30 percent) and Green Cross (40 percent).

The *Tribunal de Defensa de la Libre Competencia* (TDLC), the Chilean antitrust agency, according to data from Organisation for Economic Co-operation and Development (OECD), from 2004 until March 2015 only 25 concentrations were submitted to that body, and that of the total, 11 mergers were approved, only two failed and in 12 cases the TDLC did not issue resolution about.

Chilean law does not provide numerical thresholds to define the scope of the inspection system. However, there is a Guide on concentrations which indicates that it will not be investigate those horizontal operations that are below certain Herfindahl–Hirschmann Index (HHI) levels. These thresholds are not standard closing because it does not exclude the possibility of control by the *Fiscalía Nacional Económica* (FNE) or the eventual notification of the operation to the FNE.

HHI thresholds included in the Guide to FNE on Concentrations are limited in scope, are not binding, and its application is dimensioned to horizontal operations submitted to the FNE, entity that reserves the right to investigate operations that do not meet the thresholds under one of the following special circumstances: (i) one of the parties involved is a potential competitor; (ii) a Party is a leading innovator and a strong independent competitor (a “maverick” company); or (iii) there are current or recent signs of coordination.

This oligopolistic situation presented in the Latin American country markets, as exemplified above in relation to three major economies that dominate the list of foreign investments, is strengthened by their governments, and shows a preference towards production efficiency at the expense of allocative efficiency and also limits the economic and political power already quite limited for SMEs.

The national market for Latin American countries in view of the low level of development, calls for a promotion by the government granting a greater contribution of SMEs, taking into account the requirements of those in the economy conditioned to the low levels of technology adoption, little qualification of its employees and/or the employer himself, a relative administrative fragility, and low productivity.

In this scenario, as indicated by Emilio Zevallos V., we come across with “the demands of the new economy that in the process of globalisation has developed a new production and institutional framework that calls for substantial improvements in business processes, flexibility, quality and low prices, and, for countries, systemic productive development policies.”¹³

On the other hand, given the current globalised environment, Ana Maria Nusdeo ponders that, in practice, the possibilities are remote that

countries like Brazil issue differing decisions of those countries where the headquarters of multinational companies are based. However, Nusdeo points out that there must be a careful and an effort “affirmation of competition to protect the interests of the country, with the imposition of remedies deemed necessary to do so, or the even more radical solution of denial of operation.”¹⁴

The high degree of productive efficiency of big corporations, combined with the ease in raising credit and also to the indulgence of the state and, more than that, to a state policy model encouraging these major economic actors, reduces the possibility of SMEs in the trading market in the face of consumers, making it difficult to insert new actors into the economy, new actors that can contribute to the development of countries in which institutional and financial fragility, with social consequences, is latent.

Research conducted by Santander Bank in 2013 showed that 99 percent of companies in Latin America are micro, small and medium enterprises. The study, conducted with data’s from the World Bank, the International Labour Organisation, the Inter-American Development Bank and the Economic Commission for Latin America and the Caribbean showed that about half of these companies are in the informal sector and that a high percentage of them respond to a goal of self-employment or livelihood, not an ambitious or growth potential, as well as informality and access to credit are compromised.¹⁵

It is also worth to note the study of Krekel, Van Der Woerd and Wouterse, for whom there are three categories of small and medium enterprises whose extinction is a natural consequence of the antitrust current policies in the face of high levels of concentration. One type concerns those companies ‘whose direction, production methods and financial or commercial structure are inappropriate; they are working at the limit of profitability and only remain for border protection force, still in force, or by a more or less precarious persistence’¹⁶ linked to the past. They have become so marginal companies whose ‘natural selection’ of the market does not give truce.

Another type of SMEs endangered situation with regard to family businesses that still resist the demand of professional managers, and belonging to a single owner, or a single family without extinction of this continuing process. And lastly, we can mention those that are far from achieving an optimal size, and “its products can be industrialised, for lower costs, by important companies.”¹⁷ These small and medium enterprises as well, according to the aforementioned authors, succumb to the concentration of larger companies.

Conclusion

With this analysis, it is understandable that the development of small businesses, therefore, regarding antitrust policies, basically depends on the following programmes:

- effective control *ex ante*, on the debasement of oligopolies through stricter decisions with respect to the concentration acts (worth pointing out that all those under the supervision of the antitrust agencies are, as a rule, large acts);
- clearer and more objective insertion of human rights in the analysis of the antitrust agencies, teleologically to the dignity of the human person in order to ensure proportional balancing to the concentration acts effects on the widest possible number of factors; and
- finally, the encouragement of SMEs by sharing information of companies forming part of the oligopolistic group with other companies in the sector, under the supervision of the antitrust agency (in order to avoid undue and untied information exchanges for the decision goals), with the aim of minimising the technological and informational imbalance involving distribution logistics methods and storage products, among others, to a larger structural and performative balance, always with proportionality and reasonableness (in order to avoid exacerbated transfer efficiencies).

Endnotes

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