Do online markets effect competition?

(MM Sharma)*

Of late, media is abuzz about the ongoing clash between the retail physical markets and online markets (e-tailers). A recent news item in The Financial Express of 16th October, 2014 “Online and offline retailers are on war path at present with the latter accusing e-tailers of resorting to predatory practices to grab a larger share of the $525 billion retail market in the country. In fact, traders body CAIT has threatened to move the Supreme Court and Competition Commission of India (CCI) if government failed to act on complaints of alleged unfair trade practices by ecommerce firms like Amazon, Flipkart and Snapdeal” evoked my interest to examine if there are any competition issues or are real issues being brought up or is it only a media hype?

Can the e-tailers, a small part of the overall electronic commerce in India, estimated to be over INR 400 Billion in 2013 and dominated by online travel & booking portals for movie tickets, such as MakemyTrip, Yatra, BookmyShow etc. in the private and IRCTC in the public sector, be accused of violating the competition laws of India? Are the perceived threats to competition for real? Or should the threat to the Physical retail stores, from growing popularity of the e-tailers due to penetration of the internet in semi urban centres now, be taken as a threat to competition per se? Or more simply, should a threat to competitors (physical retailers) be taken as threat to competition as such? Conceptually, competition law is enacted to protect and prevent “competition” and not the “competitors”! After all, both have co-existed in the West for so long!

Further, even in the above context, are there no serious anti-competitive practices in the electronic commerce activities, of which e-tailers, like flipcart, snapdeal are a constituent? What are the lessons for an emerging economy like India from the experience of e-commerce activities in the developed economies where competition issues are taken very seriously?

Before analysing both, it will be interesting to have a flavour of a real case study in India. The case in hand is about a physical market player trying to get the sale of its products promoted through online portal of Snapdeal. The complaint was filed in the Competition Commission of India (CCI). The complainant was engaged in selling various products like pen drives, hard disks, laptops etc. and wanted to sell its products online through the portal of Snapdeal, and had started selling it online through Snapdeal initially too but the online sale was scrapped in January, 2014 by Snapdeal because the complainant was not in the list of the “authorised online channel partners” of ScanDisk India, the Indian sales office of SanDisk Corporation, USA, also engaged in the business of manufacture, distribution and sale of non-volatile memory drives or flash drive and storages devices of different capacities, SD cards, micro SD cards, solid state drives etc., and thus a competitor of the complainant. Obviously, SnapDeal and ScanDisk India had some agreement to market the latters’ products online for Indian consumers, which may have been subsequent in time to the agreement which Snapdeal had with the complainant firm. The focus of the complaint was that through this method SanDisk and

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SnapDeal, in collusion with each other, were trying to stop the complainant from offering competitive pricing which was much below than the other sellers of the same product.

However, instead of taking the next step, i.e. investigating this complaint, CCI vide its order dated 19 May, 2014 had closed the case holding that "both offline and online markets differ in terms of discounts and shopping experience and buyers weigh the options available in both markets and decides accordingly. If the price in the online market increase significantly, then the consumer is likely to shift towards the offline market and vice versa. Therefore, the Commission is of the view that these two markets are different channels of distribution of the same product and are not two different relevant markets." An appeal challenging this order of closure has been admitted by the Competition Appellate Tribunal (COMPAT) on 08 October, 2014 and the matter is sub judice.

The question naturally arises whether the CCI was correct in holding both the online and offline “markets” as one and the same as mere different platforms/suppliers now available for sale of the same product to the same customer instead of being two distinct “markets” competing with each other. Was it a competition issue or a case of breach of contract by snapdeal for which the remedy lies with the civil courts and not in CCI? Since the matter is sub judice, the question is open to a judicial decision.

Adverting to our set of propositions i.e. whether there are real “competition” issues or an ill-informed media is just being gradually made to taking up cudgels on behalf of a weak competitor and what, if any, could be the “real” competition concerns that have emerged outside India?

Since internet intensifies price competition, this may not be liked by most of the physical retailers and they may just be trying to protect their margins by trying to restrict price competition online so they can continue to compete on non-price elements such as service and presentation in-store. Filing complaints in CCI could be the easiest way to do so by camouflaging this as a genuine competition issue. Incumbents might defend their conduct using efficiency-based arguments based on limiting free-riding, improving service, or protecting brand signalling of quality. These can be legitimate concerns, and sometimes the firms are quite frank and say they are simply protecting what most consumers still choose to use: bricks-and-mortar sales outlets. Difficult questions of balancing efficiency, exclusivity and exclusion have arisen in such cases in traditional markets in other jurisdictions and similar questions are likely to arise in India when assessing restraints of online commerce.

On the other hand, there could be genuine contractual issues in existing physical retailers trying to use online platform for mitigating decline in profits and the online portals trying to resist, for objective commercial considerations, which may eventually lead to foreclosure of opportunity to use the online portal for smaller, often, domestic players, as noticed in the above case. Online portals are supposed to provide use of their platform on equitable and fair terms, to benefit the end consumer with lower prices.

Let us admit that to the end consumers, online and offline markets are not really separate. Many “shopping journeys”, mainly in metropolitan cities, do take place purely along one of those channels; but increasingly the line is blurring. As we all readily experience, some shoppers start searching in the real world, then go online to comparison shop, and then make the purchase; some go the other way; and some consumers start online, dip into a shop and pop back online again. Some even go online while in-store, comparison shop with other bricks or clicks outlets, then show these rival offers at check-out, which stores can then match or better, or lose that customer. To the consumer then, online
and offline options are merging; and firms are experiencing this too, moving towards providing service in both channels to meet growing customer expectation.

Thus, in assessing business practices, the competition authority must take into account the above shoppers’ journey and think more from the consumers’ perspective. There is a need to have a view on how a potentially anti-competitive restraint might affect this market environment, rather than on the particular form of ‘restraint’ that is used.

So, then, what are the real competition issues that may plague the sale of products or services through the online portals or the e-tailers? Are there any hidden consumer risks in e-commerce in general?

**Consumer risks** - Alongside the huge benefits that the internet provides for consumers in terms of improved information and choice, new sources of consumer detriment are emerging. For example, fake reviews, undisclosed commercial blogging, complex tariff structures, misleading or skewed search results, drip pricing, concealed recurring payments, and complex bundling can all harm consumers’ interests and distort competition. Problems may be even worse in markets characterised by information asymmetries, consumer biases (including to inertia) or vulnerability, like those in semi-literate populace in semi urban Tier -2 and Tier -3 towns or in rural areas. The Consumer fora need to act quickly to protect consumers and need to act comprehensively, recognising that the online world is international. CCI also need to act so consumers do not lose trust in online markets themselves, so that internet-based trade can continue to flourish and offer them the information and confidence they need to exercise effective choice.

**Competition risks** - The Internet has lowered search costs but not to zero because consumers have exogenous search costs and firms adopt tactics to make more difficult for consumers to compare prices. Although the Internet has expanded the geographic scope of transaction, most of the e-commerce still takes place within neighbouring areas because consumers prefer to shop within limited distances both for cultural and for security reasons. Though distribution costs were generally lowered as the Internet allowed manufacturers and consumers to trade directly and online retailers to carry a much wider variety of products. However, buying on-line may create information asymmetry because consumers cannot test the product they are going to buy and so it is more difficult for retailers to build a reputation. As a result, Internet is making price competition more intense, geographic markets are becoming wider and it is also allowing consumers to buy products that would not be available in the physical world.

Globally, there have been two types of competition issues, one common to both physical and online market place and the other unique to e-commerce. The former is notice in (i) Resale price maintenance (RPM). RPM is treated very seriously in all jurisdictions as an infringement by ‘object’, because it has such a high potential for restricting competition, and consumers may end up paying more than is necessary. The second type of issue noticed are (ii) internet minimum advertised pricing (IMAP) acting to set a price floor online. IMAP and other vertical restraints that prohibit the advertising of any prices online, or ban online sales outright have also been a concern. IMAP restrictions soften intra-brand competition, reduce discounting and can mean higher prices for consumers ;(iii) Dual pricing restrictions raise similar issues. Setting a higher price for online sales may be seen as a way of restricting passive sales; (iv) Price ceilings and platforms-Restraints that set price ceilings can operate to soften price/commission and competition on the platforms, and any resulting increased costs of sales may be passed through by third party sellers to consumers. Price parity and price relativity agreements have come up in a number of antitrust cases and (v) Preventing selective distributors from selling through platforms- like the one seen in the Indian case study above. There are many other practices which can be mentioned, such as, access to platforms, online-targeted advertising, MFN clauses or the “Price parity “ or “Best price” agreements between seller and an electronic trade platform, under which the physical sellers undertakes not to charge on that platform a price that is
higher than the price that he charges on other platforms. Such agreements are condemned by most competition authorities. (the recent Apple e-book case being one example).

Under the Indian competition law, these practices will attract intervention from CCI only if the e-tailer is found “dominant” in the “relevant market” and the determination of each itself will be a difficult task before CCI.

**New wine, old bottles, and telling the difference**- One question that naturally arises. Are the issues in online sales in any way or substantially any different from what are found in physical sale? The answer has to be in negative. Internet or online markets, like mobile networks, exhibit strong “network effect” i.e. the value of the product or service increases with each added user, which reduces the variable cost to almost zero for large players, like Google or Facebook with billions of users worldwide. Like in the case of economies of scale, network effects can make it hard for a new firm to enter the market where the minimum viable scale of Network is large in relation to the size of the market. Online markets with network effects are characterized by such inherent “entry barriers” for new entrants because of large networks of existing players created due to their “first mover” advantage, for which they cannot be blamed. However, what also must concern competition agencies is the other, non-price predatory behaviours exhibited by existing and dominant players such as excluding rivals from “platform software”, as was seen in the above case study.

Such conducts are likely to be repeated in developing countries like India as more and more retailers are likely to include the online platform as an alternate mode of retail sale, as noticed in the recent joint venture between Kishore Biyani of the Future Group (Big Bazaar) and Amazon India. CCI has to act swiftly and intervene when breaches of competition law are significantly and artificially preventing consumers from exercising effective choice. Similarly, consumer authorities should be prepared to intervene quickly and comprehensively when breaches of consumer law are distorting the information consumers need to be able to choose.

Thus balancing the potential competition issues with the numerous advantages for the consumer without sounding too interventionist should be the ideal approach for the fair trade regulator.

(2289 words)