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**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS  
COMPETITION COMMITTEE**

**ROUNDTABLE ON COMPETITION IN THE CONSTRUCTION INDUSTRY**

**-- Note by Turkey --**

*This note is submitted by the Delegation of Turkey to the Competition Committee FOR DISCUSSION at its forthcoming meeting to be held on 11-12 June 2008.*

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## **1. Introduction**

1. Construction business in Turkey is a very competitive and unconcentrated market where plenty of undertakings operate as determined in an earlier decision by the Competition Board.<sup>1</sup> As a result, no competition issues have been addressed directly in the construction industry under the Act no 4054 on the Protection of Competition (Competition Act). However, competition issues were discussed in many markets related to materials used in the construction industry such as cement, ready-mixed concrete, and aerated concrete. Thus, this paper will focus on those sectors due to their relevance.

2. Cement market, which is prone to cartel activity, together with ready mixed concrete and aerated concrete markets have been investigated more than 10 times in Turkey during the Turkish Competition Authority's (TCA) 11-year enforcement record. Although this sector has not gone through a serious investigation during the last one year, there were many mergers and acquisitions transactions which were examined with care during this time period. Moreover, complaints were received from the "ready mixed concrete" sector last year. But none of these complaints ended up in a serious investigation. It is also important to mention a rather recent Competition Board (decision making body of the TCA) decision concerning the follow-up of this sector. According to this Competition Board decision<sup>2</sup>, all undertakings active in the cement and ready mixed concrete sectors have to send information about their production, sales and capacity information to the TCA every three months. The enforcement of this decision is about a year old.

## **2. Market characteristics**

### ***2.1 General Information on Cement Markets in Turkey***

3. There are many cement plants that are homogeneously distributed all over Turkey. Having said that the concentration of cement factories in the Northwestern part of the country is greater as that part of the country has the highest population density which is also the most developed region. The country's total clinker production capacity is 39 mn tpa (tones per annum) and cement grinding capacity is 66 mn tpa, ranking Turkey as the second largest in Europe and the seventh largest in the world. The Turkish cement sector was fully privatized in the 1989-1997 period. Privatization and ensuing merger and acquisition transactions altered the ownership structure in the industry and led to the emergence of three major groups within the country:

- Multinationals;
- large domestic groups;
- independents (These are family owned, usually one-plant producers with no connections either to first or second group).

4. Similar to this sector's rich history of antitrust cases all over the world, the Turkish cement industry has often been the subject of investigations by TCA during its 11 year enforcement. The subject of these investigations is mostly about collusive behaviour in the form of price setting or market sharing in local markets. In the last few years the cement producers in the Mediterranean, Aegean, Marmara and Central Anatolia regions, which produce approximately 75 percent of total cement production in Turkey, were subject to a series of collusive behaviour investigations and were found guilty and penalized. There

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<sup>1</sup> *Acquisition of Garanti Koza by Balfour Beatty* (dated 3.8.2000, numbered 00-29/307-174).

<sup>2</sup> Competition Board decision dated 19.9.2006, numbered 06-66/889-M

are some facilitating practices which lead to continuation of cartel behaviour in this sector. They are information exchange, standardization procedures and geographical pricing systems. Geographical pricing systems exist in Turkish markets.

## 2.2 *Market Definition*

5. Cement is basically defined as white and grey cement. Grey cement is generally used as the main additive in construction and infrastructure sectors whereas white cement is used in the production of additives, filling substances, architectural and decorative concrete, prefabricated exterior facades etc. However, all types of cement are produced from clinker after some additives are added. Cement is also divided into bagged and bulked cement according to its marketing methods.

## 2.3 *Barriers to Entry*

6. There are certain features that facilitate anti-competitive practices especially in cement market. First of all, this market is characterized by entry barriers such as requirement to have significant amount of capital, economies of scale, vertical integration and the need to set up a distribution system. Following explanations are granted in one of the cement decisions of the Competition Board regarding entry barriers in the sector.<sup>3</sup>

7. The requirement to have *significant amount of capital* is considered deterrent for the firms to newly enter the market. The Competition Board states that the European Commission evaluates the need for high amount of capital as entry barrier without taking sunk costs into account. The deficiencies in capital markets are determinative for capital needs to be considered as an entry barrier. Due to asymmetric information in capital markets, new firms with smaller balance sheets can only raise a loan with higher interest rates because they are expected to be more likely to go bankrupt. Any undertaking willing to enter this market by constructing a new factory with a capacity of 1 million ton/year, regarded as the optimal scale in the sector, will need to invest USD 100 million. The cement sector is an oligopoly market with undertakings having large amount of capital. This structure increases the need for capital for firms to newly enter the market. Furthermore, the Competition Board considers it obvious for firms to newly enter the market to have difficulty to find credit or to be in a position to endure high capital cost due to the existing problems in capital markets in Turkey. Therefore, the Competition Board decides that sunk costs and the need for capital constitute serious entry barriers in the cement market.

8. *Economies of scale* have an important effect over fixed cost and cost of labour in cement sector because the main process is simple, the product is homogenous and technology is applicable by everyone. Therefore, the undertaking to newly enter the market has to invest in great amounts and produce at a great scale to be able to carry out price competition. It is accepted that optimal capacity is 1 million ton per year. The cement market that has had excess supply previously due to incentives granted, faces great narrowing in demand after economic crises in the country and then the earthquake. Excess production in the sector that is saturated is tried to be decreased via export. The Competition Board evaluates that excess supply in this sector constitutes an entry barrier. Likelihood of new firms' entry into the market is low even in case of increase in demand due to excess capacity and the existence of firms benefiting economies of scale.

9. *Vertical integration* is another issue considered as entry barrier in this cement decision. Cement is produced from clinker after some additives are put in. Cement is the main input for ready-mixed concrete. Due to this intertwined structure of clinker, cement and ready-mixed concrete, the existence of

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<sup>3</sup> See *Cement* case (dated 19.10.2006, numbered 06-77/992-287). The explanations regarding entry barriers in the cement market were taken from the contribution by Turkey to the Roundtable on Barriers to Entry held within the Competition Committee on 19-20 October 2005.

firms that operate at production levels of each of these products with an integrated system is regarded as entry barriers by the Competition Board. Integrated firms that operate in clinker, cement and ready-mixed concrete markets do not only create difficulties for independent cement or ready-mixed concrete producers that are in need of these materials to use them as main ingredients of their production, but also constitute serious entry barriers for the new comers. Any undertaking willing to enter clinker, cement and/or ready-mixed concrete markets has to bear the hardships and disadvantages because there are producers that produce all the three products in the market. If a firm willing to enter the ready-mixed concrete market also produces clinker and cement, it would enjoy cost advantages. Therefore, the requirement to realize similar integration to enter an integrated market for a new investor can be said to constitute an important entry barrier.

10. *Distribution system* is another factor examined as an entry barrier in the cement sector. Especially, it is necessary to sell packaged cement through a distribution system. The current distribution system requires distributors to buy all requirements from a single cement producer. Therefore, new cement producers have to set up a new distribution network if they want to distribute their products. Moreover, consumers of cement are scattered widely and this increases the number of distributors to be set up.

#### **2.4 Product**

11. Apart from entry barriers, cement market has some other characteristics enabling anti-competitive practices such as homogenous nature of the product. Besides, it is a product which is produced by a limited number of producers, which cannot be stocked as it should be consumed in a short period of time (no more than 3 months) and which can be sold within a specific geographic area because of high transport costs. Moreover, due to the difficulty to differentiate cement, addressing different customer groups does not seem very likely. For instance, cement cannot be differentiated in colour, smell, like or packing unlike soaps. That's the reason why price is the only tool to increase competition within the market.

#### **2.5 Elasticity of Demand**

12. Another feature of the cement market is the fact that price elasticity of demand in the cement sector is low. Price elasticity of demand can be defined simply as the reaction of quantity of demand with respect to price changes. When the price elasticity of demand is low, the bargaining power of the customers would be low and it would be contrary to the common interests of the producers to have price reductions. If producers reduce prices, they could not face demand increases that would produce profits. This situation would also lead to permanency in agreements on price fixing among the undertakings that are active in the relevant product market.<sup>4</sup>

#### **2.6 Excess Supply**

13. It should be mentioned that in certain regions there is excess supply in cement market and the Competition Board considers that in markets where there is excess supply healthy competitive conditions necessarily do not emerge and conditions may occur that encourage and facilitate cartels restricting competition.<sup>5</sup>

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<sup>4</sup> Information Note prepared and served as a basis for the Competition Board Decision Concerning the Follow up of the cement and ready mixed concrete sectors (dated 19.9.2006 and dated 06-66/889-M).

<sup>5</sup> *Cement* (dated 26.7.2008, numbered 07-62/740-268).

## 2.7 *Transparency and Oligopolistic Nature of the Market*

14. Cement producers in Turkey are publishing and announcing price lists for their customers and distributors at certain intervals. Nevertheless, actual prices are lower thanks to discounts given. Demand in the region, number of producers whose cement is sold in the region, region's openness to competition and transportation distance are the factors that determine the discount rate.<sup>6</sup> Moreover, due to existence of common distributors serving different producers, it is possible for these rival producers to learn the actual prices applied by their competitors in a short period of time. Therefore, cement market can be described as a transparent one having the characteristic of a tight oligopolistic market with few producers.<sup>7</sup>

15. Information on regional demand having high level of accuracy that is obtained via market surveys carried out by cement producers as well as activities of Turkish Cement Manufacturers' Association enables cement producers to involve in anti-competitive practices such as sharing the most profitable sales among each other.<sup>8</sup> Moreover, statistical infrastructure enabled by activities of the Turkish Cement Manufacturers' Association regarding information gathering and distribution of the information gathered facilitates tracking the results of anti-competitive agreements on setting regional production and sales among cement producers.<sup>9</sup>

## 3. **Types of collusive activities**

16. Price fixing<sup>10</sup>, market sharing<sup>11</sup>, exclusion of competitors from the market<sup>12</sup> and the control of supply<sup>13</sup> are the most common type of unlawful collusive behaviour that cement producers are involved in. Sometimes vertical restraints<sup>14</sup> can also be the object of the investigation where the producers attempt to prevent interregional trade of the distributors. As can be seen, all those activities are closely related to cartelization among the undertakings.

## 4. **Enforcement approaches**

17. The Competition Act prohibits anti-competitive agreements, decisions and concerted practices in Article 4. The scope of the term "agreement" under the Competition Act is wider than the one under civil law as can be seen from the reasoning of Article 4 which is as follows: "... *the term agreement is used to refer to all kinds of compromise or accord to which the parties feel bound, even if these do not meet the conditions for validity as regards the Civil Law. It is not important whether the agreement is written or oral.*"

<sup>6</sup> See footnote 4 and *Cement* case in footnote 2.

<sup>7</sup> See *Cement* case in footnote 3

<sup>8</sup> See *Cement* case in footnote 6

<sup>9</sup> Ibid.

<sup>10</sup> See for instance the following cement cases: (dated 24.4.2006, numbered 06-29/354-86); (dated 19.10.2006, numbered 06-77/992-287); (dated 26.7.2007, numbered 07-62/740-268). See also the following ready-mixed concrete cases: (dated 2.10.2006, numbered 06-68/927-266); (dated 19.10.2006, numbered 06-77/991-286).

<sup>11</sup> See *Cement* case in footnote 6.

<sup>12</sup> See *Clinker* case (dated 20.9.2007, numbered 07-76/908-346).

<sup>13</sup> See ready mixed concrete case (dated 3.10.2006, numbered 06-69/931-268)

<sup>14</sup> See *Cement* decisions (dated 5.12.2005, numbered 05-81/1118-320); (dated 24.4.2006, numbered 06-29/354-86)

18. Moreover, the prohibition also covers anti-competitive concerted practices in addition to such agreements. To quote the reasoning of Article 4, “*Even if the existence of an agreement between the parties cannot be established, direct or indirect relations between the undertakings that replace their own independent activities and ensure a coordination and practical cooperation are prohibited if they lead to the same result.*” In line with this reasoning, third paragraph of Article 4 of the Competition Act overtly says that in cases where the existence of an agreement cannot be proved, but that the price changes in the market, or the balance of demand and supply, or the operational areas of undertakings are similar to those markets where competition is prevented, distorted or restricted, constitutes a presumption that the undertakings are engaged in concerted practice (concerted practice presumption). The reasoning of Article 4 goes on to provide the justification for the presumption as “*In a legal regime where agreements restricting competition are prohibited, these agreements are generally made in secret and proving their existence is quite difficult, sometimes even impossible. For this reason, in case the circumstances stated in the third paragraph of the article exist, presumption that undertakings are engaged in concerted practice has been accepted. Thus the burden of proof for not being engaged in concerted practice has been passed to the relevant undertakings and it has been intended to prevent that the Act became unworkable due to the difficulty of proof.*”

19. While using the presumption, the Competition Board thinks that a strict observance of the wording of third paragraph of Article 4 would require *demonstrating an impact occurred in the market or parallel behaviours*. However, if defences, which argue that in oligopolistic markets undertakings are in a mutual dependency and as a result relevant behaviours emanate from such dependency, are accepted, then the Competition Board has to rule that there appears no violation in the absence of extra evidence in addition to parallel behaviours.<sup>15</sup> However, if extra evidence indicating *coordination* among undertakings is found in addition to parallel behaviours, the Competition Board considers that there would be no need to employ the presumption as there would already be a concerted practice contrary to Article 4. The Competition Board thinks if it is accepted that there must be evidence indicating *parallel behaviours and coordination*, then the presumption would be ineffective. As a result, the Competition Board states that;

- Standard of proof to utilise the presumption is lower than the one to prove concerted practice meaning that the presumption can be used if there are some indications of coordination even if it cannot obviously be shown that there is explicit coordination directly concerning the matter in question among the undertakings.
- It is not necessary to demonstrate impact occurred in the market in the sense that there is no need to prove parallel behaviours, it is sufficient to prove the existence of behaviours that is not ordinary under competitive conditions (or existence of behaviours similar to those in markets where competition is distorted) such as exchange of strategic, secret information (such as markets shares, price, sale quantities etc) among undertakings. Under such circumstances, the presumption could be used even if existence of an agreement cannot be proved.

20. The presumption is especially valuable in markets like cement market where there are repeated investigations and the undertakings are well aware of the value of certain documents such as organisers, jotters in proving the time and place of anti-competitive practices.<sup>16</sup> As a result, they develop means to conceal documents indicating anti-competitive practices and therefore it becomes hard to find evidence.

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<sup>15</sup> See *Cement* in footnote 3.

<sup>16</sup> *Ibid.*

21. For instance, in one case concerning cement market,<sup>17</sup> the presumption is used to demonstrate violation of Article 4 of the Competition Act. In this case where parallel price increases among four cement producers operating in Aegean region were the subject of the investigation, an overt text of an agreement showing the violation of the Competition Act by the undertakings could not be found. However, there were many findings demonstrating existence of infringements of competition in the market. In this case, in line with the concerted practice presumption, cement prices in Aegean region were analysed and as a result parallel and high price increases were observed. The possibility that costs might explain such increases was discarded due to cost-price comparisons proving that costs during the relevant year followed a stable course. Therefore, it was seen that price increases have been realised independent of costs.

22. To give a brief account of the analyses carried out during the investigation in general, for instance, in 2002, despite price falls in packed cement from January to April, prices charged by some cement producers doubled in a short period of time -four months- beginning from April. Increase in inflation and exchange rate in this period was around 20% whereas costs incurred by the cement producers remain unchanged. To be more specific, prices by some cement producers were increased more than 100% with no relation to and therefore independent of costs, while inflation rate and exchange rate were 21% and 23% respectively in April-October of 2002 in İzmir, the largest city in the Aegean region.<sup>18</sup> Moreover, in 2003, the increase in price of bagged cement in June-December in the gulf region of northern part of the Aegean region around 50% despite the fact that the inflation rate was around %2,20 and increase in exchange rate was minus. The increase in price was independent of costs. Price comparisons with other regions demonstrated that price of the same product was up to 65% higher in Aegean region than for instance that in Ankara although changes in costs between the two regions were minimal.

23. Moreover, during the TCA's on the spot inspections investigation, the two documents found were regarded as signs of coordination among competitors in the sense that the competitors held a meeting to realise price fixing practice. One of these documents indicated that one of the cement producers was appointed as the secretariat to organise the "business". In brief, business meant the prevention of unfair competition, unnecessary practices, price decreases, discounts and dumpings; as well as the preparation of regional plans on production-consumption. The other document showed that the cement producers held meetings in certain cities and those cement producers operating in a certain city attended the relevant meeting. However, it must be underlined that these two documents were only supporting documents indicating coordination among competitors and they were not the main element that the decision was based on. On the contrary, concerted practice presumption based on price increases is at the heart of the decision and the use of the presumption does not require the existence of such supporting documents.

24. Furthermore, the defence against allegations by the Competition Board that the cement producers were in a relationship of oligopolistic dependency was also assessed in the decision. Although undertakings in markets such as cement market could be in a relationship of oligopolistic dependency, the behaviours of the cement producers were more than what oligopolistic dependency could justify. First of all, all undertakings in the market follow decrease in prices to a certain extent to avoid losing market shares. However, when there is increase in prices, it should not be a preferred policy under normal conditions as sales by an undertaking which does not follow increase in prices will rise to a great extent. Moreover, under normal conditions, an undertaking which intends to increase the prices runs the risk of not being followed by the rivals and as a result it avoids increasing prices unless it is obliged to do so. However, in case all the undertakings are certain that a price increase by an undertaking will be followed by others, then serious rise in prices could happen. On the other hand, rise in costs might also justify

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<sup>17</sup> Ibid.

<sup>18</sup> Ibid. The decision also includes price analyses in other cities such as Aydın, Manisa and counties such as Ayvalık, Burhaniye, Edremit. Because İzmir is the largest city of the region, it is selected here as example.

increase in prices. However, it was shown in the decision that abnormal increase in prices was independent of costs. In addition, price comparisons with relatively competitive markets and the two documents found were supporting the concerted practice presumption. Therefore, the oligopolistic dependency defence was not credible.

25. At the end of the investigation, the undertakings subject to investigation could not provide rational and economic facts such as increase in demand as the cause of price increase.

26. It should be mentioned that without the use of concerted practice presumption, it would not be possible to prove a cartel agreement of such a secret nature in sectors in which competition law and instruments of proof are known. But coordination and parallel prices should be shown to argue for a concerted practice. Indeed this is a good example to show the Competition Board's approach in dealing with cartel cases in the cement industry.

27. As mentioned before, it is not easy to find clear evidences any more in this sector. First of all, due to plenty of investigations that were carried out in the sector, undertakings learnt about the competition law and enforcement. Secondly, evidences are not strong any more. Thirdly, IT related forensic activities are lacking to attain more evidence. To overcome these difficulties the Competition Board decided recently that all undertakings active in the cement and ready mixed concrete sectors shall send information about their production, sales and capacity information every three months.<sup>19</sup>

## 5. Mergers

28. In 2007, 18 out of 232 merger and acquisition cases were finalized in the construction, cement and other construction related materials industry<sup>20</sup>.

29. In Turkey, merger control provisions in Article 7 of the Competition Act are also applicable to privatization transactions conducted by the state<sup>21</sup>. In that respect, in 2005 9 cement factories which were under the control of the state were put up for sale<sup>22</sup>. When the concentration effects were taken into consideration, the Competition Board did not permit the acquisition of 4 factories by the highest bidder on the grounds that it would either create a "collective dominance" or "dominance" in the relevant markets.<sup>23</sup>

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<sup>19</sup> Dated 19.9.2006, numbered 06-66/889-M.

<sup>20</sup> Annual Report of the TCA 2007

<sup>21</sup> To ensure timely review of such transactions, the Competition Board issued a communiqué in September 1998 (Communiqué 1998/4) specifically addressed to privatisation transactions administered by the Privatisation Administration. This was later amended to cover all privatisation transactions carried out by any public institution or organisation. Accordingly, privatisation transactions subject to Communiqué 1998/4 if certain conditions are met.

<sup>22</sup> In year 2005, the cement factories belonging to Uzan Group and confiscated by the Saving Deposit Insurance Fund (TMSF) were put up for sale in Turkey. Since TMSF is a public institution, this transaction is considered as an acquisition via privatisation and thus it is evaluated under the Communiqué 1998/4.

<sup>23</sup> First of all, the Competition Board did not permit the acquisition of **Ladik** cement factory by the highest bidder based on the fact that it would create a collective dominance, whereas it permitted its acquisition by the second successful bidder. With respect to privatisation of **Sanhurfa** cement factory, the Competition Board denied its acquisition by one of the two successful bidders as collective dominance would be created in the relevant market and instead permitted its acquisition by the other bidder. Finally, the Competition Board did not permit acquisition of **Gaziantep** and **Van** cement factories by the successful bidders due to creation of dominance in the relevant markets.

Following the Competition Board's decision concerning the cement factories, successful bidders in two<sup>24</sup> cement factories filed an appeal to the Council of State<sup>25</sup> and the Council of State ceased the enforcement of the decision basically based on the claim that the Competition Act no 4054 didn't mention "collective dominance" but "dominance".

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<sup>24</sup> Ladik cement and Şanlıurfa cement factories

<sup>25</sup> According to Article 55 of the Competition Act no. 4054, appeals may be made to the "Council of State" within due period against the final decisions, measure decisions, fines and periodic fines of the Board, as of communicating the decision to the parties. Appealing against decisions of the Board does not cease the implementation of decisions, and the follow-up and collection of fines.