

## **The Elusive Syndicate and the Price Hike**

Professional economists in the country must be a sorry lot. While they have difficulties in correctly comprehending the nature and causes of the periodic increases in prices, just about everyone else seems to know the answer with certainty. Politicians, business chambers, bureaucrats, civil society people, media and even the laymen are all in perfect unanimity as to what or whom to blame for the price increases. After every bout of price increase, a syndicate (of a small number of businessmen and perhaps government functionaries) is invariably identified as the culprit that creates an artificial shortage to make excessive profit at the expense of the hapless public. This was the case about three years ago when the prices of soybean oil, onions and some other essential products increased abruptly. The then Minister of Commerce was held responsible for failing to take the syndicate to task, and he had to resign. The same problem arose anew when the prices of sugar and some other items rose sharply a few months ago. Predictably an elusive syndicate was held responsible for this. The media even named the Commerce Minister Altaf Hossain Chowdhury and his sidekick the Adviser, Barkatullah Bulu as accomplices of this syndicate. Both have been removed since then. A new Minister, widely regarded as one of the few untainted members of the current Cabinet, was brought in. He lost no time in pointing finger at the alleged syndicate for the increase in the prices of essential goods that caused so much distress among the common people. Even the Parliamentary Standing Committee on Commerce made loud noises about the pernicious activities of the syndicate just as they did on the previous occasion. They revived the old suggestion to reinvigorate TCB in order to counterbalance any shortages created by the syndicate in the market. The near identical features of the events three years ago and now (the allegations and the criticisms, the actions taken and those promised and importantly the absence of any positive outcome) are remarkable and beg serious questions regarding the near universal prognosis.

Last time when the prices, especially of soybean oil, had risen sharply I asked an old friend, who is now a leading businessman of the country, about syndication and high prices of soybean oil. He told me that there indeed was a syndicate and named a few people who he believed were among the members of that syndicate. These people would be certainly among the richest businessmen of the country. The corroboration of the first part of the syndicate hypothesis encouraged me. However, his very next comment took me by surprise. He said that if the syndicate were not in operation, the price of soybean oil would be a good deal higher. Later on, when I made some inquiries I found that the price of soybean oil in Bangladesh at that time was lower than that in the neighbouring countries.

A similar situation seems to prevail now. The bulk of the consumption requirement of sugar is imported; domestic production before the recent sugar price hike hardly met about 10 per cent of the total consumption of over a million ton. Needless to say that the sugar price in the local market is closely linked to the international price. The current international market price of sugar is about \$490 per ton CIF. The landed price at the port gate would then be \$704 per ton after paying various import related taxes, which now amount to 43.75 per cent. Before the reduction a short while ago, the taxes amounted to a

hefty 74 per cent. The landed price then would have been \$853 per ton. Now add a conservative 35 per cent to cover profits of the importer, wholesaler and retailer, interest, transport and storage costs, and *chandas* of various kind, and the retail per ton sugar price would be \$950 per ton (\$1152 per ton before the tax reduction). Thus the consumer price of sugar at the current exchange rate would be 67 taka per kilogram (81 taka per kilogram before the tax reduction). The market price is (was) significantly below this amount. Hence, if a syndicate does exist in the sugar market, as believed by most people, it is actually holding the sugar price *down*. Competition could only further raise the sugar price. If keeping the sugar price low is the *only* objective, it would seem that the syndicate is doing an adequate job! (We are not asking here the vexing question how the syndicate holds the price below the normal import cost.)

The syndication hypothesis as an explanation of the market behaviour raises other difficult questions. The sudden appearance and the equally sudden disappearance of syndicates need to be explained. If forming a syndicate is profitable and if its members are powerful enough to defy the government (is there any law that prohibits syndication?), then it should continue to operate indefinitely until it breaks up due to either internal dynamics or external constraints. The question is why do the syndicates loose their grips even without any visible government action (unless one regards making a lot of noise as action)? If the syndicates have control of the market as alleged, why should they reduce supply (hoard) all of a sudden? If they are interested in earning maximum profits, they should *always restrict* supply (as the OPEC cartel does) in order to keep the price at a level that ensures maximum profit. They should be neither increasing nor reducing the price i.e. market supply (price) should be stable at the profit-maximising price. But the behaviour of the syndicates seems to be contrary to what the profit maximising behaviour suggests.

The existence of a cartel does not necessarily imply higher market prices. In certain situation the cartel can actually reduce prices (natural monopoly). For example, if importers can get a substantial reduction in the price and freight cost if they purchase in bulk, then larger importers can out compete the smaller ones. Furthermore, if a few of the large importers form a syndicate to import very large amounts, they can further reduce the price and drive out the small importers. They can now behave like a monopolist. Depending on what the reduction in cost is, it is possible that the final price could be lower than the competitive price even though the cartel earns high profit. However, in most situations the cartel price will be higher than the competitive price implying a loss of welfare.

Why does the price of a commodity increase suddenly? This cannot be answered unambiguously in abstraction as the reason will differ from case to case. One can of course provide a litany of reasons as in a Sure Success student exam note book, but this would be less than useful. What is needed is a careful study to establish the cause of the price hike in each case. Let me weave a hypothetical story of a sudden price increase. Suppose a commodity S is imported by a number of importers and together they hold a stock that meets the demand of the country for three months. The lead time for the import of S is about 45 days. Now let the international market price of S increase substantially (say 20 per cent). Some of the importers would be discouraged from importing because they could

not be sure if the higher price will be sustained or not; if the price falls, they could suffer substantial losses. Suppose the price does not fall; on the contrary it increases by a further 25 per cent. By this time more than a month has elapsed and the sugar stock has declined to less than 2 months' demand. Still the importers are uncertain about the price movement and hesitate to import the requisite amount. Meanwhile the international price increases by another 40 per cent. The hesitation to import dwindles the stock of S to only one month's requirement. This is of course known among the importers and traders. They are now sanguine that the price of S will rise sharply. Hence, they hold back the existing supply, i.e. hoard. Domestic price starts increasing rapidly and soon more than doubles. Well-meaning people are indignant and blame the hoarders for the price increase. A little thought will make it clear that hoarding in this case is actually performing a useful function of rationing the reduced supply over a longer period. The increased international price raises the financing requirement for imports of S and this may also discourage the small importers from importing. Suppose, in this situation the big importers get together and decide to import a large amount of S that meets most of the requirement of the country. When the imported good starts arriving in the market, the domestic price of S starts declining and settles toward the import cost at the higher international price. In this scenario, while it is true that a syndicate has been in operation, what is also true is that if there were no syndicate, price could have been higher.

The story illustrates the pitfalls of jumping to conclusions. Going after the syndicate in the above case does not serve any useful purpose. The moral of the story is that it is absolutely essential we first determine the cause of the price increase. Only then we can design an appropriate policy. The country has suffered from sharp price increases on many occasions in the past. But seldom, if ever, were there any investigation to determine the real cause of the price increase. It seems the government (and others) always thought they knew the answer. As a result we do not still have any strategy to combat a sharp increase in prices. Of course there is no dearth of 'suggestions' to control prices. The Parliamentary Committee recently suggested that the TCB ought to be able to reduce the domestic sugar price with the 100 crore taka fund it presumably had at its disposal. This amount of fund does not cover the cost of even 5 per cent of the sugar requirement, i.e. if used it could hardly make a difference to the market supply. If the Committee was implying that the fund should be used to subsidise sugar, the sugar price could be reduced by less than 2 taka per kg. i.e. by less than 4 per cent. Such a small reduction will be hardly noticed. What the Committee seems to have missed entirely is that even if TCB were highly efficient, they could not profitably sell imported sugar at less than the current market price. Hence, it would actually suffer a loss if it were to import any sugar. Before giving gratuitous suggestions, the Committee could have asked the Ministry, or any credible organisation, for a scientific assessment, backed up by data and evidence, of the underlying causes of the increase in the prices of essential commodities. This would have helped the government to chalk out the right course of action to combat the price hike.

The strategies employed by all developed and numerous developing countries to control prices, ensure quality and prevent unconscionable business behaviour are consumer law and competition law. The former protects the consumer against unfair business practices while the latter prevents the rise of collusive behaviour, monopolisation of the market and price manipulations by the business community. A consumer law for Bangladesh has been

in the making for more than a decade. The effort did not go very far during the tenures of the last two governments. During the tenure of this government a draft consumer law prepared by Bangladesh Tariff Commission (on behalf of the Ministry of Commerce) went through all requisite administrative procedures. However, the penultimate authority, the Cabinet, in its infinite wisdom decided to shelve it indefinitely. The government has not even mooted a competition law as yet. In a way it has chosen not to have any effective mechanisms to regulate the market and control unfair business activities. Ordinary citizens are destined to suffer many more episodes of aberrant market behaviour.

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