Natural Monopoly and it's Regulation

Contents

INTRODUCTION

The concept of natural monopoly presents a challenging public policy dilemma. On the one hand a natural monopoly implies that efficiency in production would be better served if a single firm supplies the entire market. On the other hand, in the absence of any competition the monopoly holder will be tempted to exploit his natural monopoly power in order to maximize its profits.

This course work will take a closer look at the model of natural monopoly. It will address those areas where an unregulated natural monopoly is generally considered to be the cause of concern, before offering a brief overview of the regulatory process and some of its specific regulatory tools. It should be noted that this work mainly aims to provide an introduction to the vast literature on this topic, which has fascinated many economic and legal scholars over the years.

The aim of this work - learning Natural Monopoly and it's regulation. In order to achieve the aim following tasks need to be solved:

- To learn the essence and influence to the effectiveness of natural monopoly;
- To find out the methods of state regulation over natural monopolies;
- To analise natural monopolies in modern Uzbekistan;
- To observe state regulation over natural monopolies in the Republic of Uzbekistan

The objectives and tasks of this work define its structure. The work consists of Introduction, 2 chapters, Conclusion and the list of used Literature.

Actually, the following issue is one the most controversial issues in Economy of Uzbekistan, because in order to achieve new circuits of economic development it is necessary to take into consideration particular qualities and problems based on all spheres of Production and particularly the infrastructure. The reformation of natural monopolies has become more urgent for the last few years. Specialists are searching for the ways of solving tasks based on tariff of goods and services in natural monopolies, and other tasks as well. More effective regulation methods are processing and alternative ways of attraction of investments are also elaborating.

In the following course work periodical stamp materials and normative law acts are used. In Literature this topic is worked up enough good.

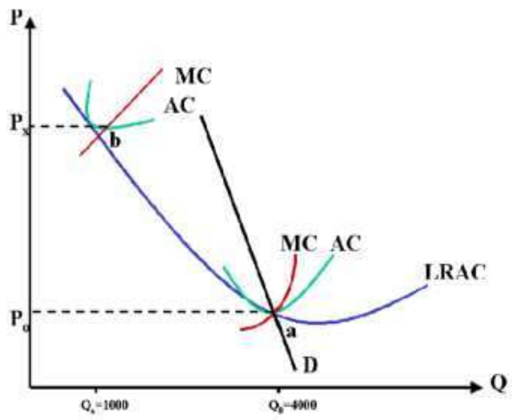
CHAPTER I. THEORETICAL ASPECTS OF NATURAL MONOPOLY AND IT'S REGULATION

1.1 THE ESSENCE OF NATURAL MONOPOLY

A monopoly is a firm which is the only one producing and selling a particular product. A **natural monopoly** is a monopoly in an industry in which it is most efficient (involving the lowest long-run average cost) for production to be concentrated in a single firm. This market situation gives the largest supplier in an industry, often the first supplier in a market, an overwhelming cost advantage over other actual and potential competitors, so a natural monopoly situation generally leads to an actual monopoly. This tends to be the case in industries where capital costs predominate, creating economies of scale that are large in relation to the size of the market, and hence creating high barriers to entry; examples include public utilities such as water services and electricity.

While in other situations a monopoly can lead to restricted output, higher than necessary prices, and production that is inefficient (at higher average cost) than would occur with many producers, a firm that is a natural monopoly produces at lower average cost than would be possible with multiple firms.

Figure 1



All industries have costs associated with entering them. Often, a large portion of these costs is required for investment. Larger industries, like utilities, require enormous initial investment. This barrier to entry reduces the number of possible entrants into the industry regardless of the earning of the corporations within. Natural monopolies arise where the largest supplier in an industry, often the first supplier in a market, has an overwhelming cost advantage over other actual or potential competitors; this tends to be the case in industries where fixed costs predominate, creating economies of scale that are large in relation to the size of the market, as is the case in water and electricity services. The cost of constructing a competing transmission network is so high that it effectively bars potential competitors from the monopolist's market, acting as an early insurmountable barrier to entry into the market place.

Companies that take advantage of economies of scale often run into problems of bureaucracy; these factors interact to produce an "ideal" size for a company, at which the company's average cost of production is minimized. If that ideal size is large enough to supply the whole market, then that market is a natural monopoly.

A further discussion and understanding requires more microeconomics:

Two different types of cost are important in microeconomics: **marginal cost**, and **fixed cost**. The marginal cost is the cost to the company of serving one more customer. In an industry where a natural monopoly does not exist, the vast majority of industries, the marginal cost decreases with economies of scale, then increases as the company has growing pains (overworking its employees, bureaucracy, inefficiencies, etc.). Along with this, the average cost of its products decreases and increases. A natural monopoly has a very different cost structure. A natural monopoly has a high fixed cost for a product that does not depend on output, but its marginal cost of producing one more good is roughly constant, and small.

A firm with high fixed costs requires a large number of customers in order to have a meaningful return on investment. This is where economies of scale become important. Since each firm has large initial costs, as the firm gains market share and increases its output the fixed cost (what they initially invested) is divided among a larger number of customers. Therefore, in industries with large initial investment requirements, average total cost declines as output increases over a much larger range of output levels.

Once a natural monopoly has been established because of the large initial cost and that, according to the rule of economies of scale, the larger corporation (to a point) has lower average cost and therefore a huge advantage. With this knowledge, no firms attempt to enter the industry and an oligopoly or monopoly develops.

William Baumol (1977) provided the current formal definition of a natural monopoly where " an industry in which multi-firm production is more costly than production by a monopoly". He linked the definition to the mathematical concept of subadditivity; specifically of the cost function. Baumol also noted that for a firm producing a single product, scale economies were a sufficient but not a necessary condition to prove subadditivity.

The original concept of natural monopoly is often attributed to John Stuart Mill, who (writing before the marginalist revolution) believed that prices would reflect the costs of production in absence of an artificial or natural monopoly. In *Principles of Political Economy* Mill criticised Smith's neglect of an area that could explain wage disparity. Taking up the examples of professionals such as jewellers, physicians and lawyers, he said,

"The superiority of reward is not here the consequence of competition, but of its absence: not a compensation for disadvantages inherent in the employment, but an extra advantage; a kind of monopoly price, the effect not of a legal, but of what has been termed a natural monopoly. independently of. artificial monopolies [i. e. grants by government], there is a natural monopoly in favour of skilled labourers against the unskilled, which makes the difference of reward exceed, sometimes in a manifold proportion, what is sufficient merely to equalize their advantages. If unskilled labourers had it in their power to compete with skilled, by merely taking the trouble of learning the trade, the difference of wages might not exceed what would compensate them for that trouble, at the ordinary rate at which labour is remunerated. But the fact that a course of instruction is required, of even a low degree of costliness, or that the labourer must be maintained for a considerable time from other sources, suffices everywhere to exclude the great body of the labouring people from the possibility of any such competition.

So Mill's initial use of the term concerned natural abilities, in contrast to the common contemporary usage, which refers solely to market failure in a particular type of industry, such as rail, post or electricity.mill's development of the idea is that what is true of labour is true of capital.

1.2 THE NECESSITY OF REGULATION OVER NATURAL MONOPOLY

Many supposed natural monopolies are the subject of various types of regulation. As described above, under conditions of natural monopoly the market is best served when one firm supplies total market demand. Public interest theory claims to provide an explanation for government intervention in what may be considered a market imperfection. The need to avoid duplication of facilities, particularly fixed costs, would serve as a justification for traditional entry regulation. Consider in this respect the restructuring of the telecom industry in the United States that broke up the Bell system to AT&T, while forbidding Regional Bell Operating Systems to enter the lines of business assigned to AT&T in order to prevent destructive competition.

Under perfect competition prices of goods equal marginal cost, as firms engage in a competitive bidding process. Under conditions of monopoly, the profit - maximizing behavior of the incumbent firm will lead to a higher price charged to consumers and a lower output. It enables the seller to capture much of the value that would otherwise be attained by consumers. Monopoly pricing thus results in a wealth transfer from consumers of a product to the seller. At the higher price, at which the monopolist tries to maximize profits, a group of potential consumers will be excluded as they will not be able to afford the product at the higher (artificially set) price. Thus, monopoly leads to the classic case of the occurrence of dead weight losses: the part of the consumer surplus that the monopolist cannot appropriate but consumers lose.

Now as a result of the monopoly pricing scheme, these consumers may be forced to consume more costly substitutes or less useful products, although society's resources would be better used producing more of the good provided by the monopoly firm. Furthermore, the argument goes that by limiting output the monopolist underutilizes productive resources.

The argument of the negative consequences of monopoly on economic welfare has been the subject of heavy debate. This article will not venture into the broad discussion of welfare economics, monopoly and distributive justice (for an introduction, see Tullock, 1967; Rahl, 1967; for case studies on the consequences of monopoly pricing and welfare, Albon, 1988). We can, however, focus on a few of the arguments concerning the case of natural monopoly which challenge the relevance of the alleged allocative inefficiency. The classic opposition to monopoly rents as opposed to everyday rent-seeking by the common man is that monopoly rents are the result of an artificial scarcity rather than a natural scarcity (Schap, 1985).

The question arises whether the same really can be said about an unregulated natural monopolist. Early on, Posner (1969) rightly noted that market power in the latter case stems from cost and demand characteristics of the market, not from unfair or restrictive practices.

The condition of natural monopoly raises the question whether internal efficiency, cost minimization by the firm, is achieved under natural monopoly. Does a monopoly firm put its resources to the best possible use within the existing state of technology?

Modern antitrust economists have used the term 'X-Inefficiency' to indicate the internal wastes that occur when a firm acquires monopoly power and is no longer pressured by strong competitors to keep its costs at the competitive minimum. Often-cited legendary examples are US Steel, General Motors, Sears, IBM and American Airlines. These giant firms, which once dominated their industries, are accused of falling victim to their own inefficiencies (Mueller, 1996). Empirical data suggest that the amount to be gained by increasing X-efficiency is significant (for a review, see Leibenstein, 1966).

Generally, in a competitive market firms have an incentive to reduce costs, in order to obtain higher profits by selling at the same price or a price between the old price and the new cost level. Although cost reduction might be shortlived in a competitive situation, as competitors reduce their production costs and adjust their prices to those of their direct competitors, the concern for survival provides a firm in such a market with a strong incentive to minimize costs (Dewey, 1959). If a firm fails to anticipate or match the cost reductions of its competitors, it might suddenly find itself in a market dominated by its competitors. Where there are no significant entry barriers the threat of potential competition will hold price down to cost. Otherwise other firms will enter the market at the same scale of production, sell at a slightly lower price and capture the whole market for as long as it is profitable.

Also, it could be argued a monopoly firm has an even stronger incentive to minimize costs in order to gain maximized profits. Since the threat of a counter reaction to its pricing schemes is absent, it does not face the risk that the consequential benefits will only be short-lived.

Technological developments have been the drive behind the transformation of certain natural monopoly markets to more competitive outcomes. Most notably, this is the case for the more recent changes in the telecommunications industry, where the enhancement and development of microwave and satellite technology has come to provide a strong substitute for the traditional cable networks. The value of technical development should not be underestimated. Technological progress often reduces production costs or creates new products and has been of enormous importance to economic welfare.

The classic argument goes that monopoly firms lack an efficient incentive to promote technical change and invest in expensive R&D programs. Allegedly, a monopoly firm would discourage progress. By virtue of its protected position it would not fear that a rival will promote products and production methods and would therefore not be driven to pioneering himself. Real-life observations regarding the introduction of new technology in monopoly firms seem to validate this criticism - witness the long life of equipment in telephone industries. This is often the case, regardless of whether the monopoly firm is conducted as a public or private monopoly (Dewey, 1959). Some empirical data suggests that small, profit-seeking firms are responsible for most major innovations (Scherer, 1984).

However, there are strong arguments that provide indications that contradict the traditional allegations concerning the case of under-innovation under monopoly.

Even when assuming that a monopoly firm will not introduce new products unless the cost of the new product is less than the marginal cost of the old (as sunk costs are bygones), there is no reason the same could not be said about competitive firms (Fellner, 1951).

Furthermore, an important point has to be made. The fact that an industry is a monopoly does not mean than only one firm is pursuing research and development in its technology. Through the presence of external forces it is likely that the incumbent monopoly firm will feel the pressure to spend time and money on innovation, in order to safeguard its position (Posner, 1969). Certainly in an unregulated market, with free entry, successful research in the field of production methods could seriously threaten the position of natural monopoly firms. Although a natural monopolist is less concerned about survival, the possible threat of the introduction of new technology in substitute markets should provide monopoly firms with a strong incentive to anticipate such developments through R&D expenditure (this relates to the theory of contestable markets, see Section 8).

At the other end of the spectrum Schumpeter (1950) holds that there is a positive relation between innovation and market power. A monopoly firm would be a strong instead of a poor innovator. Superior access to capital, the ability to pool risks and economies of scale in the maintenance of R&D laboratories are likely to advance industrial technology.

Because of social considerations, government may often feel the need to ensure the provision of certain products or services at a lower-than-cost price to some consumers. For instance, it is quite common that governments demand the provision of ‘universal services’ to consumers by telephone companies, the availability of minimum services at reasonable prices, even to small and distant communities where the small scale of operation may lead to very high costs, which often results in the occurrence of losses.

1.3 METHODS OF STATE REGULATION OVER THE NATURAL MONOPOLIES

Price Control

Price control, although driven to the background in the years of deregulation, has been of increased importance in the recent trend of privatization in Europe. From a public interest perspective, price control should allow regulators to set prices at a level which induces allocative and productive efficiency. This part provides a brief, non-technical introduction to some of the tools governments have at their disposal to assure that firms meet consumer demand at efficient cost levels. For a more in-depth look at the different forms of price regulation and its analysis, reference is made to Chapter 5200, Price Regulation, which also deals with natural monopoly.

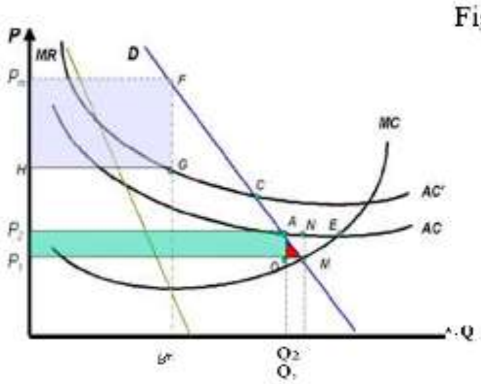


Figure 2

Without regulation, Q_m in Figure 2 represents the profit-maximizing output of the monopolist and the demand, in turn, determines the market price Pm. The monopoly earns a positive economic profit represented by the area of the rectangle PmFGH. Welfare maximization to society as a whole is achieved at the quantity-price of Pi, Qi. In other words, regulating authorities should set a price P1 (marginal cost pricing) in order to maximize economic welfare. However, at price P_1 consumers will buy a quantity of Q_1, whereas AC is NQ_1, which is greater than the price P_3. This will result in a total negative economic profit, shown by the area of the rectangle P_1P_2AM. In the long run, the monopoly firm will not stay in business. If the commodity or service provided is desirable, the only way to keep the monopoly firm in business is to provide a public subsidy to the amount of P_1 P_2 AM.

The political problems associated with subsidization, its implementation and financing and the difficulties of calculating demand and MC have led to the application in the public utility field of average cost pricing. In Figure 2 such a price is P_2, determined by the intersection of the demand and long-run AC curve. The output under average-cost pricing, Q2, is greater than the unregulated monopoly output of Q_m. Also, part of the welfare costs arising from restricted output by an unregulated monopoly is eliminated. Expansion of output, from Qm to Q2 provides benefits to consumers that are greater than the additional costs.

On the other hand, average cost pricing can hardly be deemed entirely satisfactory either. Under average cost pricing, when Q_2 is produced, welfare losses are caused because at this point average costs (the AC curve) exceed marginal costs (MC). Graphically, the AMO triangle in Figure 2 represents this consequential welfare loss. When applying a rate-of-return policy, regulating agencies focus on the rate of return on invested capital (accounting profit) earned by a monopoly (fair rate of return) (Moorehouse, 1995). Allowing regulated firms to acquire a total sum that consist of annual expenditure plus a reasonable profit on capital investment, the so-called ‘fair’ rate of return, was constructed by American courts and the regulating bodies in order to meet constitutional demands of utilities to set prices on a 'just and reasonable' level.

This can be formulated as E + (r - RB) where E represents the firms annual expenditure, r is the multiplier, representing the fair rate of return, and RB the rate (attributed value of the capital investment).

If the realized rate of return is higher than what is considered to be a normal return, then the price must be above average cost. In a trial-and-error fashion regulators try to locate the price where profit is normal, for example, where price equals average cost.

Allowing the regulated monopolist a fair rate of return creates various economic problems that have to be taken into account. Auditing costs involved in determining the firms capital base are considerable. Especially the determination of r, which should reflect a level of return that is satisfactory to attract investment, is problematic. Looking at other 'comparable' industries or applying the capital asset pricing model, where one looks at the returns obtained by investors from a portfolio of investments, as modified by the difference between the returns from shares in utilities and those from more general market shares, it is clear that these are imperfect methods for determining a rate of return that potential investors will demand from the regulated industry.

Also, the perverse effects on incentives that occur when applying the standard rate of return policy are perhaps even more troublesome (Train, 1991). The regulated firm has an incentive to inflate its capital cost figures, since higher costs imply higher absolute returns (Baron and Taggart, 1977, on profit - maximizing behavior under rate of return regulation, see Hughes, 1990). If the regulator sets the fair rate of return above the cost of capital, the regulated firm is likely to utilize more capital than if it were unregulated. Thus, it might use inefficient high capital/labor ratios for its output. Also, average cost pricing diminishes the monopolist's incentive to minimize costs. Figure 2 illustrates some of the consequences of this behavior. Inflation of costs shift the actual AC curve to

AC'. At a price of P_2 losses occur, therefore, regulators grant a price increase to cover the higher costs (point C).

Price Discrimination

Charging consumers different prices relative to what they are willing to pay, even though the costs of producing and supplying the goods or services are the same, has been demonstrated to enable allocative efficiency. With this technique, often referred to as Ramsey pricing, information on the price - elasticity of the different goods should allow for efficient price setting (the higher the price-elasticity, the closer the price needs to be set to marginal cost) (Ramsey, 1927). The objection often heard is that such a pricing scheme involves a wealth transfer from the consumer (consumer surplus) to the producer. Also, severe price discrimination, often termed predatory discrimination, is an effective method by which competition may be crushed out (see however for a detailed and comprehensive account McGee's case study of the Oil of Indiana case, 1958).

The classical analysis of price discrimination was set out by Pigou (1920). A distinction between three degrees of discrimination was made. The first degree involves a different price set for every unit purchased by every consumer, in such a way that virtually all the possible consumer surplus is obtained by the producer. Although this pricing mechanism can be efficient, as marginal decisions are made as marginal cost, it is often opposed on income distributional grounds: the transfer from consumer to producer. Second-degree price discrimination consists of pricing groups according to their willingness to pay, where all those with a demand price above a certain level are charged one price, while those with a lower demand price are charged a lower price. Third-degree price discrimination comes into effect when consumers are divided into separate groups, each group is charged a different monopoly price. This technique is of course strongly dependent on the possibility for the seller to identify groups in each specific case, which will vary according to market circumstances.

Peak-Load Pricing

When demand follows a periodic cycle, during which demand might be high at certain times and low at others, peak-load pricing might offer a way to achieve marginal cost pricing. As marginal cost generally rises with output, price variations will allow it to reflect the higher costs. This allows for the moderation of the demand cycle while establishing a more effective use of capacity (Crew, Fernando and Kleindorfer, 1995). Higher pricing during periods of peak demand might discourage use and save costly capacity, whilst lower prices when demand is low might encourage use of capacity that otherwise would have been left idle.

Incentive Regulation

Many of the problems arising from the pricing models, such as the Averech - Johnson model find their origin in the absence of incentives to operate at minimum cost levels. The motivation behind incentive regulation is to provide the firm with the motivation to behave more consistently with regard to the social optimum.

Price-Cap Regulation or RPI-X

Requiring the firm to increase its prices for each year within a given period by no more than the retail price index (RPI) minus a variable factor (X) which is the agency's assessment of the firm's cost-efficiency potential, price-cap regulation was found to be superior to the fair rate of return method both in terms of efficiency and administrative costs (Littlechild and Beesley, 1992). The system, as described above, would require less information from the firms to the regulating bodies, which would not only make this model less costly but also diminish the capture problems associated with rate of return regulation.

Chapter II. Analysis and Uzbek practice of regulation over Monopolies

2.1.Competition Legislation and Institutions

A competition policy enforcement body in Uzbekistan was established for the first time in 1992, as the Department of Antimonopoly and Pricing Policies of the Ministry of the Finance. The function of this body was to oversee the observance of anti-monopoly provisions in Uzbekistan.

In 1996, the Department was transformed into the Committee on Demonopolisation and Competition Development of the Ministry of Finance, and for the first time it was given the status of a legal entity, though it still remained under the jurisdiction of the Ministry of Finance. At the same time, the Committee was given additional functions, and empowered to implement the observance of the requirements on consumer rights protection legislation, natural monopolies, and advertising.

Improvements to the existing legislative framework for competition and regulatory policy were highlighted as a priority area for reform by the Anti-Monopoly Committee (AMC). With the assistance of international experts, the AMC identified several areas where amendments or new legislation were needed, including: demonopolisation in commodity markets; anti-collusion measures; shareholder and property rights protection; rate-setting for regulated utility monopolies; false advertising; and consumer rights protection.

The Law of the Republic of Uzbekistan on Competition and Restriction of Monopolistic Activities in the Market was adopted in 1996. This Law determines organisational and legal bases for the prevention, restriction, and suppression of monopolistic activity and unfair competition, and is directed towards providing conditions for the formation and effective functioning of a competitive market within a liberalised economy.

Basic conditions for free market competition[4] are yet to flourish in Uzbekistan. Dense regulation of the economy, a legacy of the Soviet system, was reduced somewhat, but basic free market competition exists in only a few areas, for example, through the development of micro-enterprises and joint ventures. However, there is an extensive informal economy (black economy) that includes all sectors. The State continues to control and shape the economy in all strategic sectors, especially raw materials and agriculture.

Privatisation of large industrial enterprises, the demonopolisation of a number of industries and the cotton market, and the liberalisation of foreign trade policies are moving ahead very slowly. One of the most important preconditions for a market economy reform policy, the convertibility of the Uzbek currency (the Soum), has been announced frequently; but it has only been implemented in certain segments. All banks are in the State sector, or heavily regulated by the Government, and a capital market does not exist.

Institutional Framework

Uzbekistan has made substantial progress, since the beginning of reforms, to develop an institutional framework for all commercial activities and to promote the establishment of a competitive business environment in the country. The development of the framework is still in progress. As of now, it includes, amongst other measures and actions:

- The establishment of the AMC;

Development of a programme entitled ‘The Concept of Overseeing compliance is within the remit of the State Committee, which also considers cases of legal infringements, issues appropriate decisions, provides the violators with the ‘cease and desist’ orders, and initiates cases/investigations, and appeals to the Court when it is appropriate.

The Department of Analysis of Commodity Markets and Anti-monopoly Regulations - This Department’s main functions include:

Overseeing compliance with antimonopoly legislation and the reorganisation of undertakings which are either natural monopolies, or those with a dominant position in financial and product markets, including during the process of privatisation and breaking up of state

- State Anti-monopoly Policy’, which formulates the main objectives of the Government’s competition and regulatory policy;
- Enactment of several laws, such as the laws *‘On Competition and Restriction of Monopoly Activity in Commodity Markets’, ‘On the Limitation of Monopolistic Activity ’, ‘On Natural Monopolies ’, ‘On Protection of Consumers’ Rights, ’* and *‘On Advertising. ’*

The central objectives of the Government’s competition and regulatory reform programme - implemented by the AMC - are: to develop competition and entrepreneurship in Uzbekistan’s economy; to regulate the activities of monopoly enterprises; to prevent abuse by firms with dominant market positions; to enforce sanctions on firms who engage in unfair competition; and to protect consumer rights. The emerging institutional framework and policy objectives are generally consistent with international practice.

The State Antimonopoly Committee

The structure of the State Antimonopoly Committee is as follows:

The Regional Divisions of the Committee - Regional Divisions of the State Committee of the Republic of Uzbekistan on Demonopolisation and Competition Development are the bodies, which carry out the implementation of policies in the spheres of competition development, limitation of anticompetitive behaviour, regulation of the activity of natural monopolies, consumer rights’ protection, and advertising, in various regions of the Republic.

The Department of Methodology and Coordination of Activities of Antimonopoly Bodies - This Department conducts organisational, methodological and information dissemination work on the issues of demonopolisation and competition development, antimonopoly legislation, legislation on consumer rights’ protection, natural monopolies, and advertising.

The Department of Enforcement of Compliance with Legislation on Competition - This Department supervises the compliance with anti-monopoly legislation, legislation on natural monopolies, and other normative acts.

- enterprises;

- Coordinating development of demonopolisation programmes;
- Developing practical measures aimed at the stimulation of business activity in monopolised industries and product markets;
- Supporting free competition; overseeing compliance with antimonopoly legislation in acquisitions of more than 35 percent of a company's stock; and
- Overseeing transactions by natural monopolies.

The Department of Monitoring the Economic Reforms in Capital Construction Sector - This Department is in charge of overseeing compliance with anti-monopoly legislation; supervision of meeting the requirements of resolutions and instructions of the Cabinet of Ministers of the Republic of Uzbekistan; minutes of the Economic Panel of the Cabinet of Ministers; and other normative acts targeting budget disbursement in construction as well as in production of construction materials.

In addition, Uzbekistan has a Press Centre and an Antimonopoly Policy Improvement Centre. The Antimonopoly Policy Improvement Centre was established with the view of strengthening the practical orientation of research and development in the sphere of anti-monopoly legislation and legislation on consumer rights protection. It helps in increasing the knowledge of specialists in the sphere of international practice of anti-monopoly regulation; and in creating a modern system of training and retraining of personnel in the sphere of antimonopoly policy.

Anticompetitive Business Practices

One of the primary instruments, by which the Anti-Monopoly Committee implements competition policy, is through its Register of Monopoly Enterprises. This policy instrument is common for many other CIS countries as well.6 Uzbek enterprises that are considered as 'dominant' - defined by statute as generally having a market share of at least 65 percent, and under certain conditions, a market share of at least 35 percent - are listed on the Antimonopoly Committee Register. Therefore, they must declare their prices and profits for AMC's approval.

The regulatory and licensing barriers are the continuation of the Soviet 'system of permissions,' whereby one must obtain approval from the authorities to embark on even the smallest task. Although Central Asian governments are vocal in their support and praise for the open and free market system, businesses have to seek permission from the Government at every step of operations.

The 'permissive' entrepreneurial climate, characterised In addition, registered monopolies, once they agree with their input suppliers and output buyers on volumes, delivery times, and other conditions and prices, must register the transaction terms with the AMC along with their expected profits. In certain cases - typically for infrastructure (utility) monopolies - the AMC directly determines prices and profits.

2.2 NATURAL MONOPOLIES IN MODERN ECONOMY OF UZBEKISTAN

Telecommunications Sector

The telecommunications industry plays a critical role in Uzbekistan, which inherited the bulk of its fixed telephony network facilities from the former Soviet Union. The country has made progress since independence in upgrading its fixed telephony system and building new wireless communication networks, struggling valiantly to bring its telecommunications system up to the standard found in developed countries.

With just over 1.6 million telephones at the end of 2002, for a penetration of less than seven percent, the country suffers from outdated and poorly maintained analogue equipment. In 1996, the Government began inviting foreign telecom companies to invest in Uzbekistan in their own right. In 2000, Uzbekistan created a national telecommunications holding company, UzbekTelecom, in the first step towards privatising the sector, but has been moving slowly along this path.

Telecommunications has been one of the most attractive sectors of the country for foreign investment in the last decade. However, the main telecommunication facilities are still owned by the State. Current strict regulation on hard currency convertibility, as well as poor economic conditions, has hampered further development of the sector.

Taming sugar monopoly

Consumers expressed sharp discontent with increasing sugar prices. Following this the State Committee opened investigations against Shakar Investment, the sole sugar producer in Uzbekistan.

The research showed that Shakar had jacked up its prices following a worldwide increase in sugar prices, in spite of having sufficient stocks in its warehouses. A press release from the State Committee noted that Shakar took undue advantage of its monopoly. Further, the firm supplied sugar via direct agreements instead of exchange trades. The average price for sugar at exchange was about Sum 782, 200 per tonne, while retail prices ranged between 1, 200-1,400 sums per kilo.

The Committee held the action by Shakar as violation of Section 5 (2) of the competition law and was ordered to cease from the abuse of its dominant position.

Pursuant to the Committee’s recommendation, the Economics Ministry, after assessing the production and consumption of sugar in the country, directed Shakar to increase supply of sugar through the exchange route from 38,000 tonnes to 140,000 tonnes. This measure will not allow artificial resale of sugar and promote price stabilisation.

Energy Sector

Uzbekistan is the largest electricity producer amongst the Central Asian Republics, and a net exporter of electricity. The country has a total installed generation capacity of 11,283 MW. Uzbekistan has achieved self-sufficiency in energy after gaining independence in 1991. However, maintenance of its power systems has deteriorated over the past few years, and some generating units have ceased operation. Much of the equipment in generation, transmission and distribution systems is outdated and extremely inefficient.

The energy sector in Uzbekistan is entirely State-owned. Electric power generation was controlled by Uzbekistan’s Ministry of Power Engineering and

Electrification until February 2001 when, by a Government Decree, the Ministry was transformed into the Uzbekenergo joint-stock company. However, its actual status, functions, and structure did not change significantly.

In 2001, growing demand for electricity, and depreciation of existing power generating facilities in the country, motivated the Government to develop a long-term programme for the reconstruction and development of the sector for the year 2001-10. This programme aims to extend the life of current power plants, as well as to increase their generating capacities.

Further, a timetable plan for privatisation of enterprises producing electric power was developed in June 2004. A key tool in the privatisation process was the Decree of the President of the Republic of Uzbekistan No. PD-3202 dated January 24, 2003 On Measures to Cardinally Increase Share and Importance of the Private Sector in the Economy of Uzbekistan. This was intended to speed-up the development of private sector, increase its role and importance in the country's economy, and improve the system of corporate governance of privatised enterprises.

Inefficient Local Monopolies

Every district or a town often has one small-size enterprise that is a monopoly within its territory. In theory, they could compete, but they do not, due to their territorial affiliation. For example, three regional repair shops function in Samarkand: Siab, Temiryul and Bagishamal.

The enterprises could have competed with each other within the city territory, but they continued functioning only in their districts and maintained their local monopoly positions.

The inefficiency of enterprises guided by the territorial principle lies in their inability to use the same resources, located nearby, but in different administrative districts, thus creating, in this instance, three supply chains.

An analysis of the situation produced a competition reform, in the form of the trade tender for contracts stipulating servicing zones allocated for tender (single district and multi-district contracts). It helped to raise the interest of previously non-competing companies for promoting competition among them.

Consumer Protection

The Law on the Protection of Consumer Rights was enacted on April 26, 1996. The Department of Provision of Consumer Rights' Protection and Regulation of the Advertising Market oversees compliance with the Laws On Consumer Rights Protection and On Advertising. The main objectives of the Department include the creation of information dissemination on undertakings and individuals, and products, as well as the improvement of entrepreneurial and customer culture.

Consumers are also establishing public organisations to protect their rights recognised by the Government. These organisations, together with the Committee or on their own, may provide support for resolution of issues related to the rights of consumers. There are several voluntary consumers' organisations in Uzbekistan. The Association of Consumer Rights Protection, which also has regional offices, is one of them.

CONCLUSION

A functional market economy in Uzbekistan depends on the creation of a truly competitive environment. Effective promotion of anti-monopoly regulation and natural monopolies is essential during the transition process.

Over the last few years, the formation of a competitive environment has considerably strengthened, due to the following factors:

- Government measures have been adopted to reduce the share of the Government sector in the economy;
- The Government has also reduced the sphere of State regulation and management of enterprises;
- The economy has been demonopolised, and competition has developed within the framework of the industrial and regional programmes; and
- Prices and foreign trade activities have been liberalised.

To increase the effectiveness of the market economy in the future, the State of Uzbekistan needs to harmonise the legal and economic conditions for promoting competition, and enforce these laws, prevent market dominance, improve the existing Anti-monopoly Law, and the Law on the Protection of Consumer Rights. These few steps will hopefully reduce corruption.

THE LIST OF USED LITERATURE

1. Abdel Khalik, A. Rashad (1998), ‘Incentives for Accruing Costs and Efficiency in Regulated Monopolies Subject to ROE Constraint’, 26 Journal of Accounting Research, 144-174.
2. Adams, G. and Yellen, Janet L (1996), ‘Commodity Bundling and the Burden of Monopoly’, 60 Quarterly Journal of Economics, 475-498.
3. Babilot, George, Frantz, Roger and Green, Louis (2007), ‘Natural Monopolies and Rent: A Georgist Remedy for X Inefficiency among Publicly Regulated Firms’, 46 American Journal of Economics and Sociology, 205-217.
4. Baish, Richard O. (1997), ‘The Role of the California Public Utilities Commission in Western Gas’, 27 Natural Resources Journal, 805-810.
5. Baron, David P. and Besanko, David A. (1994), ‘Regulation and Information in a Continuing Relationship’, 1 (3) Information Economics and Policy, 267-302.
6. Berg, Sanford V. and Tschirhart, John (1998), Natural Monopoly Regulation: Principles and Practice, Cambridge, Cambridge University Press, 564 p.
7. Bold, Frederick C. (1997), ‘Responses to Energy Efficiency Regulations’,8 Energy Journal, 111-123.
8. Bowman, Ward S. (2006), ‘The New Haven, A Passenger Railroad for Nonriders’, 9 Journal of Law and Economics, 49-59.
9. Law of the Republic of Uzbekistan about Natural Monopolies from April 24, 1997 of No 398-I
10. Lordkimpanidze T., Christie S. of CUTS (2004), ‘Competitions Regimes in Uzbekistan’, <<http://competitionregimes.com/pdf/Book/Asia_Pacific/34-Uzbekistan. pdf>>, last visited January 2014
11. Mueller, Charles E. (1996), ‘Antitrust Overview’, Antitrust Law and Economics Review, <<http://webpages. metrolink.net/~cmueller/i-overvw.html>>, last visited January, 2014.
12. Review Article’, 17 (2) Atlantic Economic Journal, 68-73.

13. State Committee on Demonopolisation and Competition Development website, <<http://www.antimon. uz/eng/o1.html>>, last visited January, 2014.

14. President works "The global financial-economic crisis, ways and measures to overcome it in the conditions of Uzbekistan" (2009), <<http://www.jahonnews. uz/eng/sections/politics/book_by_president_islam_karimov. mgr>>, last visited January 2014.

15. Transition to Deregulation', 44 Law and Contemporary Problems, 125 ff.