Fair Trading Commission
Economics Department

COMMODITY BOARDS IN JAMAICA: A FRAMEWORK FOR ANALYSIS

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1. Introduction

Commodity Boards regulate a significant part of Jamaica's agricultural sectors. These statutory Boards were established in the 1940s and 50s during which period shortages and price increases were widely experienced in the country. The powers of these Boards revolved around price controls, licensing and other regulatory requirements (this is discussed in greater detail below).

In addition to these statutory Boards, the Agricultural Marketing Act 1944 provides 'blanket' legislation under which representative associations may implement marketing plans for commodities for which there is no existing legislation allowing for the establishment of a Commodity Board. Under the Agricultural Marketing Act, the powers of the appointed associations mirror those of the statutory Boards. In other words, there is legislative scope for allowing price control and regulations to be introduced in respect of all agricultural commodities.

The following provides a discussion of the framework for analysis of the Commodity Boards under the Fair Competition Act (FCA). This preliminary analysis is based on the following Boards:

- the Coconut Industry Board set up under the Coconut Industry Control Act 1945;
- the Banana Board set up under the Banana Board Act 1953;
- the Rice Industry Board set up under the Rice Industry Board Act 1956;
- the Cocoa Industry Board set up under the Cocoa Industry Board Act 1957;

Section 2 looks at the economic principles behind free market competition and market control measures. This sets out the framework for an analysis of the costs and benefits of the Commodity Boards in Jamaica. Section 3 discusses the ways in which the costs and benefits may be weighed and ways to go forward on this issue.

Although past analyses have been carried out by the FTC on the same questions, it is proposed that the issue be re-visited for two reasons. First, the proposed analysis goes deeper than the previous ones. Second, all Commodity Boards will be analyzed simultaneously rather than separately. This is considered suitable as the Boards are similar in many ways and the same principles should be used in the analysis of every one. This also provides a 'global' analysis that would provide a better perspective than a partial analysis would.

2. Competition *vs* market control

Competition lies at the heart of any successful market economy and is crucial to the protection of consumers' interests and the efficient allocation of resources. It is this widely held premise that has spawned the growing importance of competition legislation in many countries, Jamaica included. Competition is a process whereby firms constantly try to gain an advantage over their rivals and win more business by offering more attractive terms to customers or by developing better products or more effective ways of meeting their requirements. Competition has several dimensions of which price is only one, albeit in many markets the most important. It encourages the development of new or improved products or processes and, in the long run, enhances economic growth and living standards.

The objective of the Fair Competition Act (FCA) is therefore to ensure that the benefits of the competition process in Jamaica are unhindered by anti-competitive activity. Specifically, the FCA aims to promote, as far as possible, competitive pressures on prices and free entry – and exit – of players, to the extent that this is beneficial to the economic health of the country.

The mandate of the Commodity Boards, however, appear to conflict with the aims of the FCA. As summarized in Table 1, the Boards have powers to, amongst others, control prices and distribution as well as set out and enforce licensing requirements. Indeed, the legislation provides wide-ranging powers to the Boards. At least for the Boards reviewed in Table 1, subject to the provisions in their respective Acts, the Boards:

> "shall have power, for the purposes of discharging any of its functions under this Act, to do anything and to enter into any transaction which, in the opinion of the Board, is necessary to ensure the proper discharge of its functions"[1]

Therefore, the term "market control" used in this paper reflects the wider roles and powers of the Commodity Boards beyond price control. While there may be benefits from imposing some form of centralized market control, there are strong reasons as preferring, *to the extent possible*, a decentralized free market system. The following discusses the disadvantages, with a focus on the impact on competition, and benefits to market controls.

[1] See section 2 of the Cocoa Industry Act. For the other Boards, see section 12 of the Banana Board Act, Section 5 of the Rice Industry Act and Section 20(s) of the Coconut Industry Control Act.

Table 1: Summary of the powers of selected Commodity Boards

Powers	Cocoa Board	Banana Board	Rice Board	Coconut Board
Fixing of retail and wholesale prices	Implied by distribution control	3	3[1]	3[2]
Distribution control[3]				
– Exclusive purchasing rights	3(shared[4])	3(for export)	3[5]	3(for copra)
– Exclusive dom. selling rights	--	--	3[5]	3(for copra)
– Exclusive rights to export	3(shared[4])	3	3[5]	3 (for copra)
Quantity controls[6]	--	3 (for export)	--	--
Setting licensing requirements	3	3	3	3
Setting quality standards	3(for export)	3	3	3
Carrying out R&D activities	3	3	3	3
Setting and collection of cess	3	3	3	--
Participation in market	3	3	3	3

Notes:

[1] The Rice Board also has powers to fix prices for services connected with rice processing;

[2] The Coconut Board has powers to fix prices for all products listed in the schedule, which extends beyond copra;

[3] The Rice Board also has explicit powers to prohibit or regulate imports or exports of rice;

[4] The rights of the Cocoa Board to purchase and export cocoa are shared with licensed cocoa dealers and manufacturers of cocoa products.

[5] The Rice Board has general powers to regulate and control the distribution of rice.

[6] Quantity controls refer to the powers to limit quantity purchased by Board.

2.1 Disadvantages of market control measures

2.1.1 Inaccuracies of price control

It is commonly accepted that the determination of prices should, as far as possible, be set by the market. Only when a market does not exist (for example, in the case of pollution) or when a market is flawed would there be reason for intervention. Flawed markets could arise, for example, in highly concentrated markets where a small number of firms control a large share of the market. A pure monopoly is an extreme case.

Even in these cases where some form of intervention is thought to be necessary, the recommended remedies tend to be structural. This includes the prohibition of certain practices and potentially the separation of activities within the dominant players. Indeed, competition legislation provides the platform for the application of such remedies. Only in the extreme case of monopolies where there are very high barriers to entry such that structural remedies may not be sufficient would direct price control be the preferred solution, for example, price regulation applied to monopolized utilities. In other cases, direct price controls are not the recommended solution.

Price controls are rarely seen in a favorable light because regulators are almost never able to estimate the true market price with sufficient accuracy due to incomplete information, on both supply and demand conditions. On the supply side, regulated companies often have strong incentives to mis-represent or conceal information. On the demand side, it is extremely difficult for an authority to gather all information about the preferences and demand patterns of the consumer. Further, even if all the information were available, the ability of a regulator to digest and process the information to replicate a market outcome is limited. It is for this reason that a free market system is considered superior to centrally planned economies. Consequently, where the free market system is not functioning smoothly, structural remedies aimed at constructing the appropriate market *structures* are preferable to remedies aimed at replicating market *outcomes*.

It is extremely important to ‘get the prices right’ as prices act as powerful signals in resource allocation. Consequently, if the regulator fails to set the correct price such that the centrally set prices diverge from the true competitive market price, strong economic repercussions may result. Both over-pricing and under-pricing have their own dangers. Prices in excess of the true market value would be detrimental to consumer welfare. Under-pricing, on the other hand, leads to depressed incentives for potential new players to enter the market and for existing players to invest in innovation and development of the industry. Furthermore, price control, coupled with the obligation to purchase or sell all that is supplied or demanded at the centrally set price could lead to significant problems of stockpiles.[2]

2.1.2 Incidence of risk in quantity control measures

Price control schemes are often accompanied by an obligation on the part of the Board to purchase and/or sell all that is supplied and/or demanded at the price set by the Board. One exception is found in the Banana Board which has the power to constrain, for specified periods, the amount of bananas that it would purchase from the growers at the set price (this applies only to bananas for export).

These powers could be problematic. Consider an example whereby the Board sets a relatively high price for bananas. This would encourage growers to increase production. Once the crop is harvested, the growers either have to sell to the Board for export or for sale in the domestic market. If, however, the Board then decides that it will limit the amount of bananas it will purchase, such that the growers cannot sell all of their crop to the Board, it will create an excess supply in the local market, leading to depressed prices.

The powers to control both price and quantity would shift the risk of over-supply from the Board to the growers. As the Board is not obliged to purchase all that the growers

[2] The Australian wool industry provides a good example. A price support scheme was set up with the objective of smoothing out price fluctuations for farmers. The inability of the authority to correctly predict world demand and prices lead to the accumulation a large stockpile of wool. Due to Australia’s position as a major wool supplier in the world, the authorities were unable to sell the wool on the market as the increase in world supply would have been so substantial that it would have severely depressed wool prices. It took the authorities more than a decade to release the surplus of wool.

wish to sell, there would be no risk of stockpiling at the cost of the Board. Instead, the growers are left ‘holding the baby’ in the event that there is an over-abundance of the produce, even if this may have been a result of the (false) signals provided by the price set by the Board. Indeed, the need for constraints on quantity purchased, *in addition to* price controls, reflects the high error rate of price control schemes. If the price were correctly set, there would be no need for quantity constraints. In responding to the incentives provided by the price, the farmers’ output would match the quantity that the Board would wish to purchase.

2.1.3 Erection of barriers to entry

A more general problem with market control schemes is that they often create high barriers to entry. Broadly speaking, these are conditions that make entry to a market unattractive or impossible for potential new players. This reduction in competition hampers the innovation and development of the market, thus reducing the rate of productivity and efficiency improvements. In the long run, these barriers could threaten the growth and sustainability of the very same industry they sought to nurture. Two examples of barriers to entry, relevant to Commodity Boards in Jamaica, are discussed in the following.

(a) Control of distribution

The Commodity Boards have at least some degree of control in the distribution of the products. This comes in the form of one or more of the following:

- exclusive rights purchase;
- exclusive rights to sell to the domestic market;
- exclusive rights to export; or
- rights to control and limit imports

Each of these exclusivity measures has the potential to limit entry and reduce competition in the respective markets.

The problems are exacerbated by import restrictions. Imports often provide a significant source of competitive pressures that are especially important when one large player dominates the domestic industry. Import restrictions, either by outright prohibition or high tariffs, therefore constitute a barrier to entry for new players from abroad. In some cases, for example rice, the Board has powers to regulate and prohibit imports. Even for commodities for which the Boards have no such powers, import restrictions external to the Board may apply. While there may be justifications for restriction imports, one of the effects would be a reduction in competition.

Further, import restrictions may also magnify the disadvantages of a market control system. If, for example, the Jamaican commodity market is rendered inefficient due to the market control systems (for reasons discussed above), there would be an increasing need for import controls so as to protect the inefficient industry from import competition. The ability of the Board to enact such controls would sustain the industry in such a way that would perpetuate the existing inefficiencies. Although trade barriers are due to fall under WTO rules, this would still provide an incentive towards lobbying for the continued protection for as long as possible.

The effects of exclusivity on competitive pressures are potentially less problematic in the export sector if Jamaica is not a dominant producer in the world market. In this case, even if the relevant Board were the sole exporter from Jamaica, it would face competitive pressures in the world market. Nonetheless, the argument is still true that such exclusivity may still stifle innovation in the development of measures to improve competitiveness and increase share of the world market.

(b) Licensing and regulatory requirements

The price control and exclusive marketing system automatically leads to the need for the creation and enforcement of licensing and other regulatory requirements. Consider, for example, the exclusive rights to market granted to the Boards. In order to enforce this, it is necessary to keep track of all quantities of the relevant commodity that is produced and sold in Jamaica so as to ensure that no other party is illicitly circumventing the law. This is evident in the wide-ranging powers of the Boards to, for example, set and enforce licensing conditions and registration of growers, dealers and manufacturers and the collection of returns and other necessary information.

The degree of bureaucracy and regulation imposes a cost on the players in the market. This acts as a disincentive for the expansion and development of the market by existing players. In addition, new players will also be discouraged from entry. The need for such regulatory measures stems only from the establishment and enforcement the market control system. As such, these measures are justified only insofar as there are benefits to the system in place. To the extent that the benefits are deemed to be few, the regulatory measures impose additional and unnecessary costs.

2.2 Benefits of market control systems

While there may be significant disadvantages, as discussed above, there are also some reasons supporting the establishment of market control systems. Indeed, the origins of the Commodity Boards reflect at least a historical, if not current, need for their existence.

As mentioned before, market control measures could be justified if there is some kind of market failure. Examples are discussed in the following.

2.2.1 Reduction of price fluctuations

The desire to avoid excessive price fluctuations has historically been a reason for the establishment of price control schemes. Excessive fluctuations result in unpredictability that could be harmful for the development of the industry, especially if the players are small and do not have the financial resources to ride out the cycles. In this regard, a centrally set price, coupled with an obligation on the part of the Commodity Board to purchase all supplies could be beneficial. The Board would have the resources to purchase and hold stocks when prices are low, in the anticipation of selling when prices improve. The centrally set price would be such that the growers would themselves not face such large fluctuations. For the scheme to be successful, however, the fluctuations must be temporary and not reflect material, permanent changes in market conditions. The expectation must be that the price would revert to some predicted level.

2.2.2 Consolidation of market power

In the case where a commodity is exported, there may be a need to consolidate the domestic industry in order to make Jamaica better able to compete on the global scene. The consolidation could benefit Jamaica in several ways – an improvement in Jamaica's bargaining position; achieving the scale economies to make it feasible to establish Jamaica's own distribution channels worldwide; and being able to run aggressive promotion and marketing campaigns abroad. In this instance, a Commodity Board with the exclusive purchasing and exporting rights would be better able to carry out these activities than small individual growers would be.

2.2.3 R&D externalities

Similarly, by consolidating across all the small growers, a Board would be able to finance R&D activities. R&D is often costly – too costly for small individual players – but has large spillover benefits. Once an innovation is discovered, the benefits could be enjoyed by all players in a way that is not exclusive as the use of the innovation by one player often does not reduce its availability and benefits to another player. This makes R&D very suitable for a Commodity Board where the Board centrally organizes and funds R&D activity on behalf of the industry.

2.2.4 Social redistribution

Domestically, there may be a need for social reasons for averaging prices across the country. Some commodities may be seen to be necessities such that it is deemed desirable to maintain a system, which allows consumers to purchase the good at the same price regardless of location. The rural consumer, for example, would face the same prices as the urban consumer. This would require an averaging of transport costs, as it would cost more to transport the goods to some locations than to others. Often, some form of exclusivity in distribution would be necessary to achieve this. Without exclusivity, other distributors could enter the market and target the low-cost consumers and offer them the product at a lower price. As the low-cost consumers shift to the new entrants, the average transport cost for the remaining consumers would increase, leading to a rise in the prices they face. This process could go on until the entire cost averaging scheme unravels.

2.2.5 Risk pooling

Commodities are often vulnerable to disasters such as hurricanes and diseases. Insurance against such risks may not be available at a reasonable cost commercially. Consequently, it may be necessary to implement a risk-pooling and insurance scheme by a centrally governed Board.

3. Weighing the costs and benefits: the way forward

It is evident that there are both costs and benefits to centrally governed market controls. As such, the benefits resulting from the establishment of each Commodity Board must be weighed against the costs. As can be seen from section 2.1, many of the potential disadvantages of a market control system stem from, directly or indirectly, the resulting lessening of competition in the market. With regard to this, the FCA provides a framework for the appropriate cost-benefit analysis. Specifically, the analyses of the effects of price fixing and exclusive dealings are provided for within Sections 17, 20, 33 and 34 of the Act.

In addition to the prohibitions against anti-competitive behavior, the FCA also provides a framework for the analysis of the benefits of such practices. Under the Act, authorizations may be granted so as to allow the relevant practices to continue if the Commission believes that the practices are beneficial. Broadly speaking, a practice may be authorized under sections 17 or 20 if it is deemed to contribute to:

(a) the improvement of production or distribution of goods and services; or

(b) the promotion of technical or economic progress

while allowing consumers a fair share of the resulting benefits.

In other words, the provision for authorization allows for a balanced assessment of the costs and benefits of Commodity Boards in Jamaica.

In order to carry out the appropriate analysis, the following preliminary questions should first be asked:

- *Are the reasons justifying the existence of the Boards still valid?*—the Commodity Boards in Jamaica were established approximately 50 years ago in response to the market conditions prevalent then. The powers of some Commodity Boards have since been altered by legislative amendments to their respective Acts. Nonetheless, an important question to ask is whether the market conditions that prevailed then still exist now. It may be the case that circumstances have changed such that there is no longer justification for the extensive powers granted upon the Boards. Put differently, the applicability of the Boards to current day conditions should be carefully studied.

- *Are Commodity Boards the best means of achieving the objectives?*—even if the problems that the Boards are meant to overcome still exist, the question still arises – are Commodity Boards the best means of overcoming the problems? It may be that, over time, alternative solutions may have arisen that could solve the problems more effectively. If so, the specific role and powers of the Boards may need to be revisited.

- *Have the Commodity Boards created unanticipated problems of their own?*—The creation of significant market power for the Commodity Boards through their powers to fix prices and control distribution may have, over time, led to inefficient market structures that hinder the development and progress of the industries themselves. Such problems could result for several reasons:

- ownership structures and vertical or horizontal integration that magnify the large market powers already bestowed upon the Boards. This is possible given that the Boards are empowered to participate in the markets directly;
- governance issues as the representation of the Board may be skewed to the interests of particular players such that it no longer reflects the wider interests of the industry.
- creation of barriers between domestic and export sectors that hinder the movement of players between the markets and the consequent implications;
- the creation of flawed incentive structures, for example, are there any incentives to increase efficiencies within the Board? In most cases, the Boards have the power to collect cess to fund their activities. This gives rise to the question of whether the Board has any incentives to be more efficient. After all, the Acts also provide for government guarantees to the Boards' debts in an event of a default.

In order to facilitate such an analysis, a detailed study into the activities of each Board as well as the market conditions prevalent in each industry should be carried out. It is anticipated that the analysis covers, amongst others, the following issues:

- the activities of the Boards;
- the extent to which the Boards exercise their powers;
- the degree of the Boards' direct participation in the market;
- the current market structure in terms of number and size of players;
- the degree of imports and exports;
- the productivity of the Jamaican industry compared to those in other countries.

The analysis would allow a determination to be made as to whether the benefits of a Board are sufficiently large to justify the reduction in competition, or if there are reasons to recommend changes to the relevant legislation.