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COMPETITION COMMITTEE**

**Competition and Inflation – Note by Portugal**

30 November 2022

This document reproduces a written contribution from Portugal submitted for Item 12 of the 139th OECD Competition Committee meeting on 29-30 November 2022.

More documents related to this discussion can be found at  
[www.oecd.org/competition/competition-and-inflation.htm](http://www.oecd.org/competition/competition-and-inflation.htm)

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## Portugal

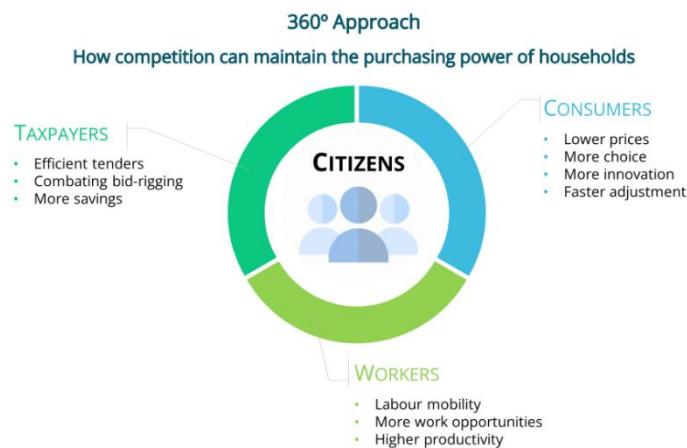
### 1. Introduction

1. Inflation has been rising in many economies around the world. Year-on-year inflation in the OECD is estimated up to 10.25% in September 2022.<sup>1</sup> Likewise, the Euro area annual inflation is estimated to be 10% in September and Portugal follows the same trend, with an estimated inflation in September 2022 up to 9.8%.<sup>2</sup>

2. In the face of the loss of real disposable income caused by inflation, governments have been implementing various support measures. In September 2022, and following measures implemented since the beginning of 2022, the Portuguese Government moved forward with a package of measures to support households in the face of the increase in prices. The measures amount to a total cost of 2.4 billion euros (1% of the GDP), covering income, transports, energy (electricity, gas, and fuel), pensions, young people, and house rents.<sup>3</sup> Likewise, in September 2022, the Portuguese Government approved a package of 1.4 billion euros to support firms and the social economy aimed at mitigating the impact of the increase of energy prices.<sup>4</sup>

3. Competition policy does not aim to address surging inflation in the short-term. Nonetheless, competition can play an important role in protecting purchasing power in times of inflation and in mitigating the impact of current macroeconomic conditions on households in their different roles as taxpayers, consumers, and workers, as summarised in Figure 1.

Figure 1. Competition and the purchasing power of households



Source: AdC (2022), Issues Paper Competition and purchasing power in times of inflation, available [here](#).

<sup>1</sup> OECD Data on Inflation CPI, available [here](#).

<sup>2</sup> Flash Estimate – September 2022 “[Euro area annual inflation up to 10.0%](#)”, Eurostat, 107/2022.

<sup>3</sup> More information on the anti-inflation support measures to households is available [here](#) (in Portuguese).

<sup>4</sup> For more information see [here](#) (in Portuguese).

4. Competition can induce a reduction in prices and drive productivity and innovation, which are key for economic recovery. Competition can also contribute to the efficiency of public spending – an important aspect in the face of the implementation of public reforms and investments put forward following the Covid-19 pandemic and lockdown measures.

5. As such, the Portuguese Competition Authority (Autoridade da Concorrência – AdC) decided that it was key to reach out to stakeholders in Portugal, to raise awareness as to the role of competition in the context of inflation and economic recovery.

6. In August 2022, the AdC published an issues paper on “*Competition and purchasing power in times of inflation*”, with a set of key messages to the Government and to firms.<sup>5</sup>

7. In addition, in June 2021, the AdC sent to the Government an issues paper on “*The role of competition in implementing the economic recovery strategy*”, with a view to contribute with set of competition principles to be embedded in the recovery plan.<sup>6</sup>

8. The present contribution outlines insights based on these two papers and on the wider work of opinions and recommendations that the AdC has put forward regarding specific policy measures aimed at mitigating the impact of the increase in prices in Portugal.

## 2. Relationship between competition and inflation

9. The current surge in inflation has been related to the reopening of the economy following pandemic lockdown measures. While demand increased, there have been supply shortages and bottlenecks of commodities and intermediate goods. The conflict in Ukraine and temporary factory shutdowns have further disrupted global supply chains.<sup>7</sup>

10. Energy inflation has taken a significant role in driving headline inflation (see Figure 2). The conflict in Ukraine has been contributing to a further soaring in energy prices, especially because of constraints in the gas market. Still, non-energy industrial goods and services as well as food inflation have also been important.

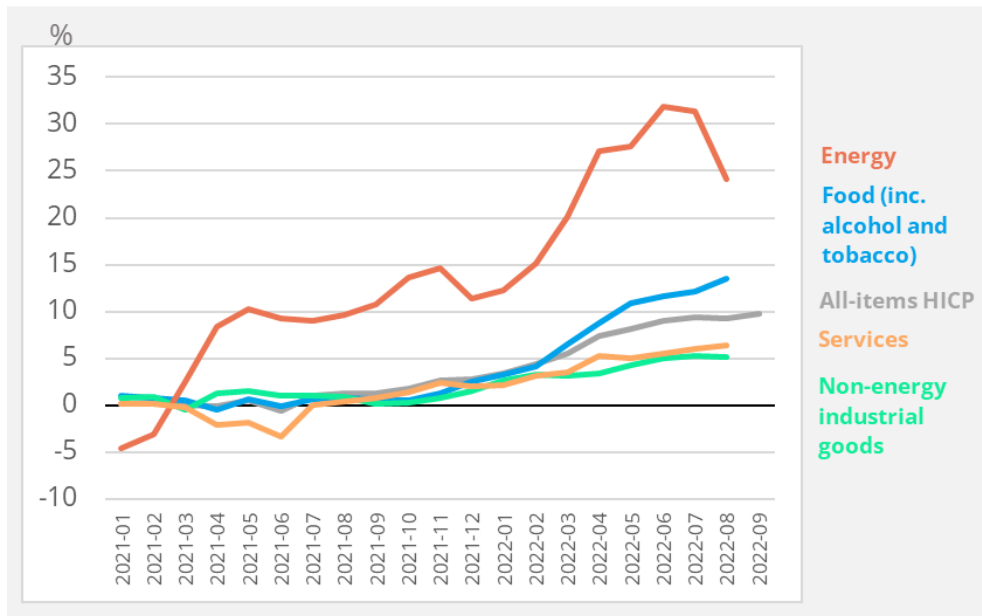
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<sup>5</sup> Available [here](#).

<sup>6</sup> Available [here](#).

<sup>7</sup> Cf. [Economic Bulletin - June 2022](#), Banco de Portugal; [Economic Bulletin - May 2022](#), Banco de Portugal; and [Economic Bulletin Issue 4, 2022](#), European Central Bank.

Figure 2. Harmonized index of consumer prices (HICP) in Portugal, 2021/01-2022/09



Source: Eurostat, available [here](#).

11. The surge in inflation seems to be driven particularly by the challenging international factors that mark the current macroeconomic scenario, rather than the long-standing increasing trend on average industry concentration and markups.<sup>8</sup> This, however, does not imply that competition does not play a role in the current inflationary context nor that the increase in concentration could not be making it harder for macroeconomic policy measures to stabilize inflation.

12. Indeed, the OECD has already acknowledged the “*importance of competition policy for achieving optimum economic growth, long-term price stability and for encouraging more rational consumer behaviour*” in its 1971 OECD Council recommendation concerning action against inflation.<sup>9</sup>

13. In its paper on competition in times of inflation, the AdC highlights mechanisms in which more competitive markets can play a key role in times of inflation.

14. First and foremost, more competition induces firms to compete more fiercely with one another, benefiting consumers via lower prices, better quality, and more variety.

15. Second, firms in more competitive markets and with lower search and switching costs are less likely to be able to benefit from inflation in the form of larger mark-ups.<sup>10</sup>

<sup>8</sup> The increasing industry concentration and markups in the last decades have been discussed in several papers, namely De Loecker, J., J. Eeckhout, and G. Unger (2020), “The Rise of Market Power and the Macroeconomic Implications”, *Quarterly Journal of Economics*, 135(2), 561–644.

<sup>9</sup> OECD, *Recommendation of the Council concerning Action against Inflation in the Field of Competition Policy*, [OECD/LEGAL/0097](#).

<sup>10</sup> See, e.g., Gwin, C. R. and Taylor, B. A. (2004), “The Role of Search Costs in Determining the Relationship between Inflation and Profit Margins”, *Journal of Money, Credit and Banking*, 36(1): 139-149.

16. Lastly, a more competitive economy is more likely to adjust more swiftly to unanticipated shocks.<sup>11</sup> More competition pushes firms to change their prices more frequently as a response to competition pressure and/or changes to underlying factors, which in turn can reduce the time that inflation takes to return to the level prior to the shocks that triggered it, in the first place.<sup>12</sup>

### 3. Actions taken in response to high levels of inflation

#### 3.1. Advocating for the role of competition policy in times of inflation

17. In the aftermath of the COVID-19 pandemic and in the context of inflation, the AdC has been highlighting key messages to decision makers, firms, and other stakeholders, with the aim to promote competition and innovation.

18. In its issues paper on competition and purchasing power in times of inflation, the AdC noted that it is key to remove unnecessary barriers to entry and expansion of new players in the market and to reduce switching and search costs. The removal of unnecessary barriers to entry and expansion can induce factor mobility, a faster entry of firms in the market and a more swiftly response to supply shortages.<sup>13</sup> In this context, the AdC has highlighted several recommendations made throughout the last years which focus on the removal of unnecessary barriers. These recommendations cover different areas, namely FinTech, road, rail, maritime and port sectors, electronic communications, and energy sectors. The AdC also highlighted that the current context further strengthens the case for implementing those recommendations.

19. Competition enforcement, especially combating cartels in public procurement, is also key to avoid waste of public funds. Furthermore, promoting competition in public procurement, beyond issues of enforcement, is crucial to ensure that public tenders are well participated and efficiently designed, to deliver better value for money. While the AdC has been long advocating for the importance of promoting competition and efficiency in public procurement, this effort gains added relevance at a time where optimizing public procurement could free-up resources that could be put to better uses, such as recovery strategies or support to households.

20. In addition, it was emphasized that each firm must set its prices and strategies in the market in an autonomous manner (*vis-à-vis* their competitors in the market). Thus, temporary supply chain disruptions or any form of public price announcements should not be used to disguise a concerted practice.

21. The AdC has also made a few considerations regarding price controls as these are often implemented in times of inflation. On this, it is important to draw attention to the

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<sup>11</sup> Genakos, C., and Pagliero, M. (2022). “Competition and pass-through: evidence from isolated markets”. *American Economic Journal: Applied Economics*, 14(4), 35-57.

<sup>12</sup> Eurosystem (2006) “Competition, productivity and prices in the euro area services sector”, Task Force of the Monetary Policy Committee of the European System of Central banks.

<sup>13</sup> E.g., Foster, L., Haltiwanger, J. and Krizan, C.J. (2006). “Market Selection, Reallocation, and Restructuring in the U.S. Retail Trade Sector in the 1990s.” *Review of Economics and Statistics*, 88(4): 748–58; Bloom, N., Draca, M. and Van Reenen, J (2016), “Trade Induced Technical Change? The Impact of Chinese Imports on Innovation, IT and Productivity.” *Rev Econ Stud* 83 (1): 87-117; and Correa, J. A., & Ornaghi, C. (2014). “Competition & innovation: Evidence from US patent and productivity data”. *The Journal of Industrial Economics*, 62(2), 258-285.

potential risks to competition of imposing a price cap, as well as to likely alternative policies that may achieve the same objective. The aim of the AdC in this regard is to raise awareness to contribute to informed policy decisions.

22. In its June 2021 paper on the role of competition in the implementation of the economic recovery strategy, the AdC highlighted a set of competition principles regarding the provision of public funding to firms following the pandemic and the lockdown measures.<sup>14</sup> It was noted that financial support should:

- Be proportionate, well targeted, and must not result in adverse effects on competition.
- Be based on objective criteria and, if possible, applicable to the several firms in a sector to minimize distortions between competing firms.
- Be targeted to firms that are not in financial difficulties prior the Covid-19 pandemic. This is a particularly relevant recommendation for policymakers in Portugal given that economic literature points out that “*zombie firms*” (i.e., highly indebted, and unprofitable firms) have had a significant presence in Portugal between 2005 and 2017 and that this type of firms is less likely to recover or exit.<sup>15</sup>
- Incorporate a restructuring plan for the firm and an effective and transparent exit strategy, particularly when dealing with inefficient firms that survive mainly at the expense of financing.
- Have a limited duration. The duration of the financing must not exceed the time strictly necessary to ensure a sustainable recovery, minimizing a negative impact on the incentives to compete and innovate in the market.
- Incorporate corrective measures if financing results in competitive distortions. Measures must be proportionate, appropriate, feasible and properly monitored to correct identified competition problems.

### 3.2. Raising awareness to risks to competition in policy support measures

23. Many national governments have adopted measures to contain the surge in energy prices (electricity, natural gas, oil), although with different degrees of impact in terms of the conditions of competition in the market. These measures have ranged from (i) direct subsidies to the most affected households and/or companies; (ii) reductions in the tax burden on final energy prices; to (iii) direct intervention in market prices (e.g., price caps or price freezes), amongst others.

24. In Portugal, the Government has already approved packages of temporary measures focused on (i) reducing the tax burden on the final price of electricity, natural gas, and road fuels; (ii) direct support to the most vulnerable consumers of bottled LPG; (iii) direct intervention in market prices (namely at the wholesale level of natural gas and at the retail

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<sup>14</sup> These recommendations are in line with the principles highlighted by the OECD, in the discussion of the role of competition in economic recovery and the Commission Notice on state aid of the European Commission. OECD (2020) [The Role of Competition Policy in Promoting Economic Recovery](#) and [Commission Notice on the notion of State aid as referred to in Article 107\(1\) of the TFEU, C/2016/2946](#).

<sup>15</sup> Carreira, C., Teixeira, P., & Nieto-Carrillo, E. (2021). “Recovery and exit of zombie firms in Portugal”. *Small Business Economics*, 1-29.

level of bottled LPG); and (iv) the possibility for household consumers to switch from the liberalised market for natural gas to the regulated market.

25. In the last 2 years, the AdC has issued over 13 opinions in the electricity, natural gas, bottled LPG and road fuels sectors, some of those relating to measures to contain the surge in energy prices.

26. Overall, the AdC's role has been to raise awareness as to the risks that some public policy measure may bring on competition conditions. The AdC further advocates for the competitive neutrality of public policy measures, and seeks to put forward alternative measures, or adjustments to the measures under discussion, that are less distortive to competition.

27. In what follows we highlight a subset of opinions by the AdC that relate to policy measures to contain energy prices.

### ***3.2.1. Road fuels and bottled LPG***

28. In October 2021, the Parliament approved a law that makes it possible to set temporary margin caps in any of the commercial components that make up the retail price of simple road fuels and bottled LPG.<sup>16</sup> According to the law, the margins caps are set by the Government, upon proposal from the Portuguese Energy Regulator (ERSE) and after hearing the AdC. Furthermore, the law foresees that the period during which margin caps are imposed must be limited in time.

29. Before the adoption of the law, in September 2021, the AdC sent comments to the draft law that was under discussion in the Parliament.<sup>17</sup> The AdC highlighted that regulatory regimes of price or margin caps can bring competition risks (e.g., exit of operators and shortage of supply, reduction of investments, focal point of collusion). The AdC also noted that the duration of a regime of price/margin caps should be the shortest possible that allows addressing the underlying public policy objective. Lastly, the AdC reiterated alternative paths, namely the relevance of ensuring the effectiveness of third-party access regime to logistics infrastructure to promote competition and access to competitive imports.

30. Following the approval of the law, the AdC issued subsequent opinions, in May and in August 2022, on the methodology to be used to compute the margin caps.<sup>18</sup> In its opinions, the AdC advocated for alternative measures to promote competition in the market, namely: (i) the elimination of barriers to entry/expansion, in particular regarding the implementation of the access to storage facilities to third parties under FRAND terms; and (ii) the introduction of solidarity tariffs, that target consumers in a vulnerable position.

### ***3.2.2. Natural Gas***

31. In April 2022, the AdC sent comments to the Portuguese Energy Regulator, ERSE, in the context of a public consultation on a set of extraordinary measures within the scope of the National Gas System (SNG).<sup>19</sup> Those extraordinary measures aimed at obviating the effects arising from the price surge in the wholesale natural gas market.

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<sup>16</sup> Law no. 69-A/2021, October 21st, available [here](#) (in Portuguese only).

<sup>17</sup> More information available [here](#).

<sup>18</sup> More information available [here](#) and [here](#).

<sup>19</sup> More information available [here](#).



32. The AdC highlighted that those initiatives were likely to foster competition in the natural gas market, ensure the stability of supply to end customers and, consequently, mitigate the risk of insolvency of agents of market that operate in the SNG. Some of the measures were in line with the AdC recommendations issued in its 2017 Sector Inquiry,<sup>20</sup> namely auctioning part of the natural gas from the long-term take-or-pay contracts from Nigeria, by the incumbent operator, at the Sines terminal, to third party operators. The incumbent operator, that was state owned prior to the liberalization process, inherited these contracts, which were negotiated by the Portuguese Government.

33. The AdC also highlighted that it would be key to eliminate the tariff "pancaking" in gas imports by pipeline in Campo Maior, to deepen the development of the Iberian gas market (MIBGAS).

34. More recently, in parliamentary hearings, the AdC sought to raise awareness as to the potential impact on competition of some of the policy measures adopted by the Government to face the spike in natural gas prices. In particular, the AdC noted that the measure which allowed consumers from the liberalized market to return to the regulated market could hinder the liberalization process and have longer term consequences for market efficiency.

35. Underlying these measures was the aim to allow more consumers to benefit from the regulated tariff, which in turn are more competitive because the regulated market is supplied with the natural gas acquired under the long-term take-or-pay contracts.

36. As alternative measures to achieve the same policy goal, which is to reduce retail prices for consumers, the AdC highlighted that the above-mentioned auctions of part of the natural gas from the long-term take-or-pay contracts from Nigeria, by the incumbent operator to third parties, would allow pursuing the same policy objective, while simultaneously promoting competition in the market.

#### 4. Conclusion

37. As the economic recovery takes a priority role, competition advocacy and competition law enforcement can contribute to keeping markets open and competitive, which can ensure a swifter adjustment of the economy to unanticipated shocks. Thus, defending the Portuguese economy from anticompetitive behaviour, and advocating for competition principles to be embedded in current efforts by policymakers in the face of inflation and economic recovery continue to be priorities for the AdC in 2022.<sup>21</sup>

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<sup>20</sup> Available in Portuguese [here](#).

<sup>21</sup> The AdC's Competition policy priorities in 2022 are available [here](#).