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International Cartels Logic and Cases

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ABSTRACT

This article gives a general overview of cartels. The development of cartels started in the late 19th century. During this period large businesses emerged and this marked the official beginning of the contemporary cartel movement. The typical story of cartels may not be one of their rise and fall, but rather of their growth, boom, collapse, rebirth, steady decline, and eventual criminality. But up until the 1980s, cartels were a necessary part of the global story of big business, not their absence. They had an impact on organizational change, corporate strategy, and technical advancement. Regarding cartels just as a "conspiracy against the public" sidesteps a number of crucial issues and obscures the vast differences in the goals, forms, and services offered by cartels.

Keywords
Cartels, types of cartels, international cartels.

Introduction what are cartels?

A cartel refers to an agreement between two or more independent firms who collude to control the terms of business in a particular market (Dick 1996). Cartels are formal or informal agreements, national or international organizations, of manufacturers or traders, designed to reduce or suppress competition in a particular market. Cartels control production and distribution. The main activities in which they engage are: fixing prices, limiting supply, dividing markets, fixing quotas for sale or manufacture, and pooling profits among member firms. Although some state-sponsored cartels are considered acceptable, such as OPEC in the export of oil or DeBeers in the diamond industry (Gupta et al 2010), illegal private cartels between companies have been seen operating on a variety of worldwide markets, including those for metals, vitamins, chemicals, semiconductors, chemicals for air travel, textiles, graphite electrodes, synthetic rubber, and semiconductors. Graham and Richardson (1997) noted, "While competition is familiar to most, few reflect deeply on cooperation. Almost all market competitors are firms—business organizations (social groupings) that are, for the most part, internally cooperative, not competitive."

Cartels originated in Germany during the 1870s conceding with the growth of this country. Many analysts believe that the successful operation of cartels was responsible for German aggression, which led to two world wars. During World War I the government of Germany utilized domestic cartels to produce armaments and other materials. In the next two decades, German firms continued to cooperate with each other in order to control production. One of the most important was I. G. Farbenindustrie, which produced chemicals and dyestuffs. By the outset of World War II, in Germany, all industry was controlled by cartels, supervised, and encouraged by the government. Cartels are primarily employed for:

- ✓ **Central Sales Control**. In this case, the members of the cartel define and specify prices and sales conditions, maximum total sales, and quotas. Moreover, they determine standards for the quality or distribution of goods within limited territories.

- ✓ **Central Purchase Control.** Are agreements between buyers joined in a central agency or purchase company, which acts only after consulting with all the members of the group? The purpose is to keep the price down.
- ✓ **Production Control.** This agreement consists of restrictions on production directly or indirectly. An indirect restriction of production is for instance the fixing of prices at a defined level. While a direct restriction is realized by determining production quotas, by pooling agreements to limit production in a specified amount. In the cases when the quantity produced will exceed the specified or fixed quantity, the production will be suspended. Moreover, this kind of agreement consists of the setting of standards for the quality of production.
- ✓ **Control of Territorial Market**. Consists in the division of markets among different partners simply by agreements, patent licenses, or trademark licenses. The first kind of agreement involves the restriction of production to the quantity, which every partner can sell in the market assigned to him. The second consists of the giving of patent licenses by the members of a firm in a particular country. And finally, the division of the market may be realized by using trademark licenses. American law prohibits the licensing of trademarks but this can be done in a number of other countries.

Types of Cartels

There are several types of cartels that operate in a way or another.

Domestic Cartels: a way for companies to limit market access for foreign firms. In general domestic cartels are considered to restrain trade and are illegal, but participation in international cartels is not sanctioned.

Import Cartels: defensive responses by companies that purchase the goods of export cartels. An import cartel is formed when all the rival companies while importing a given product cooperate. An Import cartel may be used as a protectionist trade policy tool to limit imports. Moreover, cartels may be used as a device to manage demand and the price of crucial inputs, such as resource commodities. The motivation of members of an import cartel is to shape the price and quantity of imports. However, the import cartel results in distorted and higher relative prices of imports. Consequently, the cartel inflicts production and consumption inefficiencies, which low the social welfare in the economy

Export Cartels: An agreement between firms on export prices, division of markets or any other group action in foreign markets. Most governments of industrial and developing countries encourage export cartels because they are viewed as important in building international sales. Developing countries see export cartels as a mechanism for development. We think to focus my intention on export cartels because they are increasingly coming to be viewed as an instrument of strategic trade policy. Export cartels vary in terms of their scope and constituency. So they are categorized as follows:

Pure Export Cartels are directed exclusively at foreign markets. Vs. **Mixed export cartels**, restrain competition in the exporting country's home market as well as in foreign markets.

National Export Cartels include suppliers only from one country. Vs. **International export cartels**, which include producers from several countries.

Private Export Cartels involve private agreements but the best-known export cartels have resulted among national governments.

Moreover, export cartels can be categorized in:

Resource Cartels. The formation of such cartels depends on the proportion of location and the abundance of factor endowments that a country has. In principle, resource goods are traded in perfectly competitive markets in which individual firms have no significant influence on price. Over the years, there have been many attempts to form export cartels in resource products such as coffee, oil, bauxite products, phosphate, tin, copper, iron, tea, bananas, natural rubber, nickel, pepper, cobalt, etc. The average life of a multi-country resource sector cartel is relatively short. Some cartels have enjoyed success: oil, phosphates, and coffee, but others faltered rapidly: bananas, bauxite, copper, and tin.

Export Cartels in Manufactured and Technology Goods. Manufactured products and technology goods are commonly traded in imperfectly competitive markets, which provide firms with greater opportunities to shape the price of their products. The manufactured or technology product requires a substantial investment in R&D or other fixed costs, and moreover, needs know-how and expertise.

The Logic of Cartels

Cartels have the possibility to create super-normal profits in international markets. Cartels are created under some conditions. First, the demand for the product must be relatively insensitive to price changes, i.e. inelastic. Second, the supply of the product must also be relatively intensive to price changes. Differences in the height of entry barriers (as we discussed above), the degree of market transparency, product homogeneity, frequency of interaction, and business cycle sensitivity render some industries more vulnerable to cartelization (Hellwig & Hüschelrath, 2017). In order to create effective and successful cartels members must be able: to reach an agreement, collude with each other, detect breaches of the agreement, and punish firms that breach. Collusion is when firms in a market coordinate their behavior for the purpose of producing a supra-competitive outcome (Harrington Jr, 2017). The degree to which enterprises internalize the effect of their production and pricing choices on the sector's output and price level is impacted by collusion. Enforcement is a crucial aspect of cartels because cartel members have the incentive to cheat by selling or producing more than the quantity assigned or with lower prices. In a few words, if legal provisions do not maintain the cartel, there is a constant threat to its existence as each participant tries to maximize its profits. The ability of a cartel to punish is essential because courts will not remedy the breach of an illegal contract. The scope for gains in a cartel is greatest when the cartel controls much of the world’s production, when there is little ability on the part of consumers to switch away from the product, and when alternative sources of supply are difficult to develop. Maphwanya (2017), studies a sample of 28 detected cartels between 1999 and 2012 and finds that more than 50% of the cartels involved five or fewer members.

Cartels can affect customers by limiting competition and driving up costs, which is why they are frequently viewed as unlawful and anti-competitive in many nations. Many countries permit and support cartels when they are in the public interest. ***Defenders*** claimed that cartels stabilize markets, reduce costs of production, eliminate high tariffs, distribute profits equitably, and benefit the consumer. On the other hand, those who ***object*** to cartels point out that prices are higher and output is lower when firms do not engage in competition. Today their disadvantages

are considered to outweigh their advantages; legal barriers often restrict the development of new cartels.

Regarding Albania, it would depend on the particular setting and sector. There may be examples of cartel-like behavior or anti-competitive activities in some businesses, despite the fact that cartels are typically detested and regulated in most nations, including Albania. According to Albania's Competition Law, the government agency in charge of upholding the law and looking into anti-competitive behavior, such as cartels, is the Competition Authority.

Case study Widget Manufacturing Cartel

The Manufacturing of Widgets Cartel was a collection of five businesses that produced and distributed widgets to customers all over the world. These businesses—Company A, Company B, Company C, Company D, and Company E—were prominent participants in the widget industry, and they collectively held a considerable portion of the world's production.

Establishment of the Cartel. Following informal discussions and agreements, the executives of the five corporations decided to join a cartel in order to boost their earnings and market dominance. They banded together in order to stifle competition among themselves and pursue anti-competitive behavior. To end competition and increase profits, the cartel decided to regulate prices, restrict production, and divide market shares among its members.

The Widget Manufacturing Cartel maintained its anti-competitive pact by operating clandestinely, conducting secret meetings, and engaging in criminal activities. To maintain their cartel agreement, they took a number of actions, including communicating confidential business information, keeping tabs on one other's output levels, and enforcing sanctions against violators.

The Cartel's effects. The widget market and consumers suffered a number of consequences as a result of the cartel's anti-competitive actions. The cartel was able to maintain artificially high widget prices by setting prices and restricting production, which increased expenses for consumers. Due to the cartel's anti-competitive actions, other potential competitors were unable to enter the market, which decreased customer choice and hampered innovation.

Discovery and Legal Actions: The Widget Manufacturing Cartel was identified and was subject to legal repercussions following a thorough investigation by the competition authorities. The member companies received large fines from the competition authorities for their anti-competitive actions, and the executives implicated were charged with crimes for their involvement in the cartel. Millions of dollars in fines were imposed on the firms, and the CEOs might go to jail. The Widget Manufacturing Cartel was broken up as a result of the legal activities, and the member companies suffered major monetary and reputational damages. The fines and legal repercussions functioned as a disincentive for further anti-competitive behavior, increasing market competition that benefited consumers and encouraged innovation.

The Widget Manufacturing Cartel case serves as a stark reminder of the serious repercussions of engaging in anti-competitive behavior, such as the formation of cartels, including monetary fines, legal actions, and reputational harm. In order to safeguard consumers and advance fair competition in the market, it also emphasizes the significance of competition laws and regulatory authorities in spotting and combating cartels and other anti-competitive actions. Businesses must adhere to competition rules and be aware of the legal and financial repercussions of participating in cartels or engaging in other anti-competitive activities.

De Beers Consolidated Mines the Diamond Cartel

The well-known diamond mining and trade corporation De Beers is headquartered in South Africa. De Beers has a reputation for exerting cartel-like control over the world diamond market, despite the fact that neither the corporation nor the courts have ever used the word "cartel" in connection with De Beers. An outline of the so-called "De Beers cartel" is given below:

Background: Cecil Rhodes formed De Beers in the late 19th century, and the company made a substantial contribution to the global diamond industry, particularly in the South African diamond mines. De Beers eventually gained control over a sizeable share of the world's diamond production, which helped it establish a monopoly in the diamond industry. About 65% of trade in rough diamonds is controlled by De Beers, through mines in South Africa, Botswana, Namibia, and Tanzania. The control that De Beers has over the diamond business has raised antitrust concerns in the U.S. since 1945, and the company still faces an indictment brought by the Justice Department in 1994. De Beers executives say that they cannot travel to the United States without risking arrest.

De Beers Consolidated Mines is an effective cartel in the diamond industry. Most of the major producers belong to a marketing cartel formed to maintain the price of diamonds at a high level. De Beers maintained its dominant position in the industry by using its numerous worldwide companies to buy up new sources of diamonds, control the distribution of industrial diamonds, and the production of synthetic diamonds. De Beers is an effective cartel because it controls production, dominates trade, and influences demand (by spending millions every year on advertising).

The "De Beers Cartel" was established because De Beers reportedly used anti-competitive tactics to retain its hegemony in the diamond industry. Early in the 20th century, De Beers employed a tactic known as the "single-channel monopoly," in which it took control of the whole diamond supply chain from mining to distribution. De Beers accomplished this through a number of strategies, including developing global networks of distributors and purchasers, buying diamond mines, and forming strategic agreements with other diamond producers.

Operation of the "De Beers Cartel": It's well documented that De Beers used strategies like price fixing, market allocation, and production control to rig the supply and demand of diamonds and keep prices high.

De Beers was accused of manipulating the supply of diamonds by hoarding vast amounts of them and releasing them gradually into the market to keep prices stable. Additionally, they entered into exclusive agreements with diamond buyers, preventing them from purchasing from other vendors and keeping control of the diamond distribution network.

Impact of the "De Beers Cartel": The "De Beers cartel's actions have been criticized for manipulating the diamond market and inflating prices artificially, but supporters of the group counter that De Beers has helped the diamond industry stay stable and expand.

Legal Actions and Changes: Over the years, De Beers has been involved in legal disputes involving anti-competitive behavior, primarily in the United States. De Beers and the U.S. Federal Trade Commission (FTC) settled claims of price fixing and anti-competitive behavior in 2004. De Beers agreed to stop purchasing diamonds from particular mines as part of the settlement to allay worries about anti-competitive behavior.

In the years thereafter, De Beers has worked to increase transparency and make changes to its business operations, abandoning the "single-channel monopoly" approach.

In conclusion, the "De Beers cartel" has long been the subject of discussion and judicial scrutiny in the diamond industry. The word "cartel" is not used by De Beers or in judicial processes involving the corporation, despite the fact that De Beers has been the target of legal actions and altered its business methods. However, the past actions connected to the "De Beers cartel" have sparked worries about anti-competitive behavior in the diamond business and have emphasized the significance of competition laws and regulatory scrutiny to promote fair competition and safeguard consumer interests.

The Organization of Petroleum Exporting Countries (OPEC)

OPEC is an international organization concerned with coordinating the crude-oil policies of its member states. Iran, Iraq, Kuwait, Saudi Arabia, and Venezuela are the five oil-producing nations that created the international corporation in 1960. OPEC has 11 members – Algeria, Indonesia, Iraq, Iran, Kuwait, Libya, Nigeria, Qatar, Saudi Arabia, United Arab Emirates, and Venezuela. OPEC headquarters is located in Vienna, Austria. In the late 1950s, the amount of oil produced worldwide was greater than the demand. As a result, the price of oil, which was controlled by the oil companies, dropped, and with it dropped the amount of money the oil companies paid to the oil-producing nations. In reaction of this situation was formed OPEC. During the 1970s, the oil supplies in non-OPEC countries were reduced, and the organization raised the price of oil. Moreover, OPEC sets production ceilings, specifying the quantity of the oil that each member country may produce. In the 1980s some OPEC nations ignored the production ceiling and this resulted in overproduction and a drop in oil prices. OPEC has also used the supply of oil as a political tactic, for example, stopping the delivery of oil to nations supporting Israel in the Arab-Israeli War of 1973.

The main goal of OPEC is to coordinate and harmonize national petroleum policies in order to maintain stable oil prices on the world market while safeguarding member nations' economic interests.

OPEC has recently encountered a number of difficulties and chances that have influenced its operations and had an impact on the world oil market. Let's examine some crucial components of OPEC's case study in more detail:

Oil Price Volatility: The fluctuating price of oil has been one of OPEC's biggest problems. For OPEC members as well as for the global economy, changes in oil prices can have enormous geopolitical and economic repercussions. Through production quotas and agreements among its members to control oil production and stable prices, OPEC has attempted to control oil prices. For instance, OPEC and non-OPEC producers agreed to reduce oil output in 2016 in an effort to stabilize prices, which had fallen due to an excess of supply. However, because different nations have diverse economic and political interests, maintaining output limits and gaining agreement among member countries has occasionally proven to be difficult.

Geopolitical Dynamics: In addition to its member countries, other significant oil-producing countries also have an impact on the functioning of OPEC. Geopolitical concerns, such as Middle East conflicts, sanctions against specific OPEC members, and political disagreements within member nations, can affect oil supply and prices. For instance, the capacity of OPEC to agree on production limits and other policy decisions has recently been hampered by conflicts between certain of its members, such as Saudi Arabia and Iran. Relationships between OPEC and non-member nations like the US, Russia, and China, which have a big impact on the world oil market, are also influenced by geopolitical factors.

Climate Change and Technological Advancements: OPEC's activities have been impacted by technological developments in the energy sector, such as the creation of shale oil and renewable energy sources. The surge in shale oil production in the United States has lowered oil prices by increasing the quantity of oil on the market and complicating OPEC's efforts to control prices through output quotas. Concerns about the long-term demand for oil have also been raised by the growing worldwide attention on climate change and the shift to renewable energy sources, which may have an effect on OPEC's market share and earnings. OPEC has taken action to diversify its revenue sources and invest in renewable energy technology in response to the need to adapt to shifting energy landscapes.

Market Share and Revenue: Market share is a crucial factor in the strategies of OPEC member nations because they significantly rely on oil exports for their economic profits. In the past, OPEC sought to keep a sizeable portion of the global oil market in order to guarantee steady income for its member nations. However, OPEC has struggled to hold onto its market share due to escalating competition from non-member nations, technological developments, and shifting international energy regulations. To increase their revenue streams, OPEC has responded by imposing output quotas, market diversification initiatives, and investments in downstream operations like refining and petrochemicals.

OPEC still has a substantial impact on the world oil market despite the difficulties and possibilities it faces. Through production limits, agreements, and diversification initiatives, the organization has attempted to address challenges connected to oil price volatility, geopolitical dynamics, technological improvements, and market share. OPEC will probably continue to modify its policies as the global demand for oil changes and the energy landscape changes.

Conclusions

Unexpectedly, cartels are a touchy subject. Although cartel dynamics are not a mystery, they are insufficient to explain any specific organization. The volume of research to date has an emphasis on why cartels fall apart rather than their enduring power. More study of cartel internal organizational dynamics that incorporates political, organizational, and economic theory is required.

The rise and fall of cartels serve as a reminder that international trade and collaboration are absolutely necessary for a flexible division of labor based on comparative advantage and competition. Given the experience of the 20th century, when increasing nationalism distorted international markets and frequently forced businesses to cooperate to survive, economic cooperation among businesses was gradually eliminated thanks to international collaboration. Because of the fierce competition that constrained the market's size, cartels emerged as a disappointing but probably sensible second-best solution.

The intriguing question of whether competition is crucial for effectiveness and creativity is finally raised by the study of cartels. The cartel dilemma draws attention to difficult-to-resolve conflicts between the costs of capitalism's stop-go, boom-and-bust instability and the advantages of moderate stability and risk management, between price and quality, between consumers and producers. One place to think about when and how cooperation might be effective and inventive is through cartels.

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