Antitrust - the 'Big Tech' Debate

Over the past decade as we have shifted into the digital economy, technology has become more ingrained in our everyday life and as consumers, we have become more reliant on technology for how we work, communicate, shop, and relax. This has created an environment that has led to technology-based companies growing exponentially, cementing themselves as market leaders, and becoming some of the largest, most powerful businesses in the world. It is no surprise then that this has attracted the attention of various regulators. Most recently the US, with the release of a 451-page report which is the product of an 18-month investigation into what they deem as anti-competitive behaviour by Google, Amazon, Apple, and Facebook.

In this month's article we look at this antitrust case, the consequences of government intervention, as well as look ahead to see what a potential outcome could be for investors.

What is anti-trust and what are the regulators worried about?

The intention of antitrust law is to prevent anti-competitive behaviour and keep markets functioning fairly for consumers. The laws prohibit collusion, anti-competitive mergers and the monopolization of industries and markets. These practices have generally led to more expensive goods and services for the end consumer.

Historically, businesses that have managed to gain significant market share and pricing power have grabbed the attention of regulators. Standard Oil (1911), IBM (1969) and Microsoft (1998) being the most well-known cases.

In the eyes of the regulators "*Google, Amazon, Apple, and Facebook have established significant market power and have used this power to dominate markets in ways that erode entrepreneurship, threaten privacy online, and undermine the free press*"[1]. According to them, the result of this is less innovation, fewer choices for consumers, and a weakened democracy.

Although the business activities of these companies are complex, regulators feel that each have significant influence over important aspects of the digital economy: Google in online search; Facebook in social networks; Amazon in e-commerce sales and delivery and Apple in smart phones and related apps.

What are regulators trying to achieve?

Their main concern is that these businesses have significant influence over consumers in their respective segments of the market which leads to a worse outcome for these consumers. To resolve this, regulators have recommended "*prohibitions of certain dominant platforms from operating in adjacent lines of business*"[2] which would essentially separate the underlying platform from the products and services sold on it.

This would mean Google could no longer own Android and offer apps like Gmail, Maps, and Chrome. Amazon could no longer own Amazon Marketplace and sell its own private-label goods. Apple could no longer own iOS and offer products like Safari and Siri; and Facebook could no longer own social-media platforms like Whatsapp and Instagram and use personal data to target ads to users.

What are the consequences of government interference?

Although antitrust regulation sets out to protect the end consumer, there is research that suggests this does not always seem to be the case and often this 'interference' can have negative effects on innovation, entrepreneurship, and competition, all of which results in a negative outcome for the end consumer.

Uncertainty

Firstly, antitrust regulation is complex, and often very open to interpretation. This makes it difficult as a corporate to know when it may be used. This can put the brakes on growth as the fear of being investigated could hinder a business's mindset about growth and their desire to innovate.

InvestSense (Pty) Ltd
Phone: +27 10 020 6777
Email: invest@investsense.co.za
Web: www.investsense.co.za

There is also uncertainty in the minds of investors, as previous examples have shown how an antitrust case can adversely affect a company. Take Microsoft as an example. Their ability to innovate and continue along their growth path was hindered by the distraction of their antitrust case between 1998 and 2001. At the time Microsoft was close to developing their own smartphone operating system, which then fell behind competitors due to the time and effort it took to defend their case.

How might this have affected the global technology industry today if we had another competitor to iOS and Android?

What if this happened in today's market? Many technology-based companies are pricing in unconstrained growth potential. An antitrust lawsuit could have a significant impact on these business models and their ability to grow at expected rates.

Not thinking long term

Often short-term benefits come at a greater long-term cost. A lawsuit now could deter future mergers and innovations that could benefit the consumer in the long-term. Consider the case against IBM which lasted 13 years before being dropped. During this time, the computer market had completely changed, and their competitors had long surpassed it. Who knows what consumer benefitting innovations IBM could have developed with the time and the resources it spent devoting to defending the case?[3]

The other side of the argument

Generally, the mindset of the regulator has been the bigger the business and the more market power or influence they have, the worse the outcome for the end consumer. This is often referred to as "The Curse of Bigness"[4]. The rationale being that these businesses have pricing power that will eventually lead to higher prices and will drive out competitors, leading to less innovation.

However, many argue that this does not seem to be the case within the technology sector as there are a number of examples showing how tech companies have benefitted consumers.

Pricing

As a result of technology, prices in many industries have fallen. For example, over the last decade prices for digital adverts have fallen by 42%[5], with these savings then flowing through to consumers in the form of lower prices for goods and services. The price for books has also fallen by more than 40%[6] since Amazon's IPO in 1997. Then there is the point that many of the services are provided at no direct cost to consumers, with Facebook and Google as an example.

Competition

One of the concerns raised by the US regulators is that these businesses have become so powerful that no new competitors dare to challenge them. However, there are several examples of businesses that have entered the market and managed to compete with the larger incumbents.

TikTok - a social media business that competes with Instagram and Snapchat, has just surpassed Instagram, as US teenagers' second favorite social media app[7]. Another example is Zoom, a subscriptions-based company that competes against 'Google Meet', 'Microsoft Teams' and 'Skype', has dominated the videoconferencing market this year, growing from 10 million users in December 2019 to 300 million users in April 2020. It has left its competitors behind as they scramble to enhance their existing offering to compete.

In fact, the number of startups in the US has seen a significant increase over the past 15 years and in 2019 there were four times more venture capital deals compared to 2006[8].

Entrepreneurship

Another concern by regulators is that 'Big Tech' has had a negative effect on entrepreneurship. Again, this does not seem to be the case in the technology sector. In fact some argue that these large platform businesses like Amazon Web Services and Shopify, have

InvestSense (Pty) Ltd
Phone: +27 10 020 6777
Email: invest@investsense.co.za
Web: www.investsense.co.za

reduced the barriers to entry for entrepreneurs and have leveled the playing field by enabling companies of any size to access the tools they need to run their businesses online, which is in turn lowering the costs of starting and scaling a business.[9]

So where to from here?

The biggest challenge US regulators face is that current antitrust legislation was written for a tangible world and has not been updated to reflect the new intangible economy. This makes it very difficult to prove anti-competitive behaviour given the nature of the digital business model, as existing legislation requires regulators to prove that consumers have been negatively impacted due to higher prices. This is difficult in a world where many businesses have reduced prices (digital adverts) or offer products/services at no cost.

To resolve this there would need to be changes to the anti-trust legislation, which would require the same bill to be passed by majority in both the House of Representatives and the Senate. With the current nature of US politics this provides a challenge, as although both the Democrats and Republicans agree 'Big Tech' power is a concern, they do not agree on *what* the exact issues are and *how* they should be addressed[10].

The need for regulation in the technology sector is something that most investors agree on. However, the way in which it is being done, by focusing on anti-competitive behaviour and using outdated antitrust regulations, does not seem to be the correct way to go about it, and given the current legislative and political environment in the US, the probability of anything happening in the near future seems unlikely.

However, another very important aspect of this regulation debate is finding a way to regulate the way in which social media platforms influence and control the flow of news and information to suit a certain view or political rhetoric. This is arguably more crucial than the current focus on anti-competitive behaviour as it involves influencing the human psyche which has the ability to change our behaviour and opinions.

The outcome of this 'Big Tech' debate is important for investors as many have benefited hugely from tech stocks globally and locally through Naspers. As discussed, regulation can create uncertainty which is negative for share prices and can potentially limit long term growth rates and returns. However, letting these companies grow in an unconstrained manner will likely create the commercial environment regulators are aiming to avoid, so a confrontation appears inevitable. Given all this and where valuations stand today, investors need to be mindful that looking ahead, past performance will be extremely difficult to sustain.

---

[1] Investigation of Competition in Digital Markets - Subcommittee on Antitrust, Commercial and Administrative Law

[2] Investigation of Competition in Digital Markets - Subcommittee on Antitrust, Commercial and Administrative Law

[3] https://www.ben-evans.com/benedictevans/2020/8/10/would-breaking-up-big-tech-work

[4] The Curse of Bigness: Antitrust in the New Gilded Age: Tim Wu

[5] https://www.progressivepolicy.org/issues/regulatory-reform/the-declining-price-of-advertising-policy-implications-2/

[6] Federal Reserve Bank of St Louis – Economic Research

[7] Piper Sandler – Taking Stock with Teens annual survey

[8] PitchBook - Venture Monitor Q2 2020

[9] 'Scale as a Service' – Baillie Gifford

[10] Ninety One Asset Management

InvestSense (Pty) Ltd
Phone: +27 10 020 6777
Email: invest@investsense.co.za
Web: www.investsense.co.za

InvestSense

November 2020

data provided by Reuters and Datastream

30 Nov 2020

		3m	YTD	1yr	3yr pa	5yr pa	10yr pa	5yr Vol1	10yr Vol1
LOCAL MARKET INDICES									
FTSE/JSE All Share Index (ALSI)	ZAR	3.6%	2.7%	6.0%	1.6%	5.1%	9.8%	15.1%	13.3%
FTSE/JSE SA Listed Property	ZAR	4.3%	-42.4%	-43.6%	-22.9%	-11.9%	2.4%	24.7%	20.1%
SA All Bond Index (ALBI)	ZAR	4.1%	6.1%	8.1%	10.0%	8.4%	8.2%	8.9%	7.9%
SA Cash Index (SteFI)	ZAR	1.0%	5.1%	5.7%	6.7%	7.0%	6.4%	0.3%	0.3%
Balanced Benchmark	ZAR	1.9%	5.3%	6.8%	4.6%	6.4%	10.6%	10.4%	8.8%
SA Inflation (1 month lag)	ZAR	0.6%	2.9%	3.3%	4.1%	4.7%	5.1%	1.3%	1.3%
GLOBAL MARKET INDICES BASED TO USD									
Global Equity (Datastream World)	USD	5.7%	11.7%	15.1%	10.1%	11.5%	10.8%	15.1%	14.1%
Emerging Markets Equity (Datastream EM)	USD	9.8%	10.5%	18.8%	5.3%	11.1%	4.0%	17.4%	17.8%
Global Property	USD	3.4%	-6.4%	-5.2%	3.4%	5.8%	7.4%	14.8%	14.8%
Global Bonds (Barclays Global Bond Index)	USD	1.2%	8.6%	8.9%	4.5%	4.7%	2.4%	5.3%	5.0%
Global Cash	USD	0.1%	0.6%	0.8%	1.8%	1.5%	0.9%	0.2%	0.2%
MAJOR INDICES BASED TO RANDS									
FTSE/JSE All Share Index (ALSI)	ZAR	3.6%	2.7%	6.0%	1.6%	5.1%	9.8%	15.1%	13.3%
Global Equity (Datastream World)	ZAR	-3.5%	23.6%	21.6%	14.8%	13.1%	19.8%	17.1%	14.8%
Emerging Markets Equity (Datastream EM)	ZAR	0.3%	22.3%	25.5%	9.8%	12.7%	12.4%	14.6%	13.4%
Global Property	ZAR	-5.6%	-1.9%	0.1%	7.8%	7.3%	16.2%	17.0%	14.7%
SA All Bond Index (ALBI)	ZAR	4.1%	6.1%	8.1%	10.0%	8.4%	8.2%	8.9%	7.9%
Global Bonds (Citigroup)	ZAR	-7.6%	20.2%	15.1%	9.0%	6.2%	10.7%	16.6%	14.7%
COMMODITIES									
Gold (US Dollars)	USD	-9.8%	16.7%	21.4%	11.5%	10.8%	2.5%	13.3%	16.0%
Gold (Rands)	ZAR	-17.6%	29.2%	28.2%	16.3%	12.4%	10.8%		
CURRENCIES									
Rand / Dollar	ZAR	8.6%	-10.7%	-5.6%	-4.3%	-1.4%	-8.1%	17.2%	15.8%
Rand / GBP Pound	ZAR	8.9%	-11.5%	-9.0%	-3.8%	1.0%	-6.5%	17.8%	15.2%
Rand / Euro	ZAR	8.6%	-17.9%	-14.6%	-4.4%	-4.0%	-7.2%	15.9%	14.0%

Spot Rates		30-Nov-20	Latest Quarter	1 Year Ago	5 Years Ago	10 Years Ago	20 Years Ago
CURRENCIES							
Rand/US$	Rand	15.48	16.68	14.65	14.42	7.09	7.74
Rand/GBP	Rand	20.65	21.57	18.95	21.70	11.04	10.98
Rand/EUR	Rand	18.51	19.56	16.16	15.23	9.23	6.74
RATES							
Libor 6m $	US$	0.26	0.26	1.90	0.66	0.46	6.64
Repo Rate	Rand	3.50	3.50	6.50	6.25	5.50	12.00
Prime	Rand	7.00	7.00	10.00	9.50	9.50	14.50
All Bond Index Yield	Rand	9.86	10.20	9.70	8.97	8.31	9.74
COMMODITIES							
Gold ($/oz)	US$	1,774.39	1,899.84	1,461.54	1,063.68	1,385.18	268.55
Platinum	US$	979.00	884.00	894.00	831.00	1,658.00	605.00
Oil (Brent Crude) $	US$	47.70	40.99	62.62	44.11	86.26	32.52
INFLATION							
SA Inflation	%	3.3	3.0	3.6	4.7	3.5	9.4

Fundhouse is a leading investment adviser specialising in fund research, ratings and portfolio construction services. We help clients manage investments on behalf of the end investor. Our experienced team understands the complexities of the fund management world. We apply this knowledge alongside a client first mindset to improve the outcome for the end investor.

Fundhouse was founded in 2007 by professionals from the investment management industry. We currently operate from offices in the United Kingdom and South Africa, where we cover the local and global fund industry first hand. Our business is 100% independent and owner managed which means we can offer objective advice and services in the best interests of our clients.

INVESTMENT WEEK INVESTMENT RESEARCH AWARDS 2016 WINNER BEST RATINGS AND RESEARCH SERVICE

INVESTMENT WEEK INVESTMENT RESEARCH AWARDS 2016 WINNER BEST INDEPENDENT RESEARCH SERVICE

Professional Adviser 2017 awards WINNER Best Ratings/Research Service for Advisers

INVESTMENT WEEK INVESTMENT RESEARCH AWARDS 2018 WINNER BEST OVERALL INVESTMENT RESEARCH SERVICE