

National Differences in Political Economy

2

Learning objectives

- Understand how the political systems of countries differ.
- Understand how the economic systems of countries differ.
- Understand how the legal systems of countries differ.
- Explain the implications for management practice of national differences in political economy.

This chapter discusses differences in national political, economic, and legal systems, highlighting the ways in which managers in global settings need to be sensitive to these differences.

Political differences are described along two dimensions: collectivist vs. individualist and democratic vs. totalitarian. Economic systems are explored in terms of market characteristics: market economies, command economies, and mixed economies. Legal systems are discussed in terms of the protections they offer for business: intellectual property, product safety, liability and contracts.

The opening case describes the economic growth in the East African nation of Ghana over the last decade. In 2011, Ghana became Africa's newest middle-income nation, thanks to the global demand for two of its major exports—gold and cocoa—as well as the recent start-up of oil production in the country. The closing case explores the reasons why Poland has experienced strong economic growth during the recent global recession while the rest of the world has struggled.

OUTLINE OF CHAPTER 2: NATIONAL DIFFERENCES IN POLITICAL ECONOMY

Opening Case: Ghana: An African Dynamo

Introduction

Political Systems

- Collectivism and Individualism

- Democracy and Totalitarianism

Country Focus: Venezuela under Hugo Chávez, 1999–2013

Economic Systems

- Market Economy

- Command Economy

- Mixed Economy

Legal Systems

- Different Legal Systems

- Differences in Contract Law

- Property Rights and Corruption

- The Protection of Intellectual Property

- Product Safety and Product Liability

Country Focus: Corruption in Nigeria

Management Focus: Did Walmart Violate the Foreign Corrupt Practices Act?

Management Focus: Starbucks Wins Key Trademark Case in China

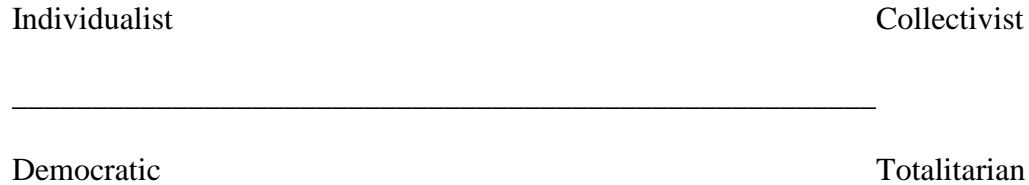
Implications for Managers

Critical Thinking and Discussion Questions

Closing Case: Poland's Economy

CLASSROOM DISCUSSION POINT

Ask students to think about the two dimensions used to describe political systems: Collectivist-Individualist and Democratic-Totalitarian. Begin by drawing the following scale on the board:



Then ask students to provide some examples of what might describe a collectivist system—where does Canada’s national healthcare system put it, which countries might be considered democratic, where should China be placed, and so on.

Finally, move to a discussion of how differences in political economy present both opportunities and threats for business. Managers must analyze each national market that they participate in and identify specific ways in which the political economy of that nation could support or threaten the company’s business model.

If there are foreign students in the class or students with foreign experience, you might draw on their observations of differences these dimensions impose on the practice of business.

OPENING CASE: Ghana: An African Dynamo

Summary

The East African nation of Ghana has emerged as one of the fastest-growing countries in sub-Saharan Africa over the last decade, becoming the continent’s newest middle-income nation. Driving this growth has been the strong demand for two of the country’s major exports—gold and cocoa—as well as the start of oil production in recent years.

Overcoming military coups and corruption, the country’s recent leaders have embraced a stable political environment, which has helped drive the country’s economic success and dramatically reduce widespread governmental corruption. Discussion of the case can revolve around the following questions:

1. How did the political and economic policies implemented over the last 20 years help Ghana prosper? What does this mean for existing and potential investors in the country?
2. How important is the privatization of state-owned enterprises to the country’s booming economy?

3. What does Ghana need to do to ensure that it continues to prosper? What steps should the country take to make it a more attractive destination for investment and economic partnerships?

Another Perspective: With sustain economic success and political stability, Ghana will need to continue its efforts to increase educational opportunities for its citizens. To learn more go to { <http://www.bbc.co.uk/news/world-africa-22607178> }

LECTURE OUTLINE

This lecture outline follows the Power Point Presentation (PPT) provided along with this instructor's manual. The PPT slides include additional notes that can be viewed by clicking on "view," then on "notes." The following provides a brief overview of each Power Point slide along with teaching tips, and additional perspectives.

Slides 2-3 and 2-4 Political Economy

The political, economic, and legal infrastructure of a nation has a major influence on the way managers make decisions. Political systems have two dimensions: the degree of collectivism versus individualism, and the degree of democracy versus totalitarianism. These dimensions are interrelated; systems that emphasize collectivism tend towards totalitarianism, while systems that place a high value on individualism tend to be democratic.

However, a large gray area exists in the middle. It is possible to have democratic societies that emphasize a mix of collectivism and individualism. Similarly, it is possible to have totalitarian societies that are not collectivist.

Slides 2-5 through 2-7 Collectivism and Individualism

Collectivism refers to a political system that stresses the primacy of collective goals over individual goals. Advocacy of collectivism can be traced to the ancient Greek philosopher Plato. In modern times the collectivist system is largely the domain of nations that have embraced socialism.

Individualism is the direct opposite of collectivism. Its central tenet is that individual economic and political freedoms are the ground rules on which society is based.

Slides 2-8- through 2-10 Democracy and Totalitarianism

Democracy, as originally practiced by several city-states in ancient Greece, is based on a belief that citizens should be directly involved in decision making. Most modern democratic states practice **representative democracy** in which citizens periodically elect individuals to represent them. **Totalitarianism** is a form of government in which one person or political party exercises absolute control over all spheres of human life and opposing political parties are prohibited (**Communist, theocratic, tribal, right wing**).

Totalitarianism denies its citizens all of the constitutional guarantees asserted by representative democracies.

Slide 2-11 through 2-14 Economic Systems

There is a connection between political ideology and economic systems. In countries where individual goals are given primacy over collective goals, we are more likely to find free market economic systems. In contrast, in countries where collective goals are given preeminence, the state may have taken control over many enterprises, while markets in such countries are likely to be restricted rather than free.

There are three broad types of economic systems: the market economy, the command economy, and the mixed economy.

A **market economy** is an economy in which all productive activities are privately owned, as opposed to being owned by the state. Production is determined by the interaction of supply and demand and signaled to producers through the price system.

A **command economy** is an economy in which the goods and services that a country produces, the quantity in which they are produced, and the prices at which they are sold are all planned by the government.

A **mixed economy** is an economy in which certain sectors of the economy are left to private ownership and free market mechanisms while other sectors have significant state ownership and government planning. India has a mixed economy.

Mixed economies were once very common throughout much of the world, although they are becoming much less so. There was a time not too long ago when Great Britain, France, and Sweden were mixed economies, but extensive privatization has reduced state ownership of businesses in all three.

Slide 2-15 and 2-16 Legal Systems

Legal systems are the systems of rules or laws that regulate behavior along with the processes by which the laws are enforced and through which redress for grievances is obtained.

There are three main types of legal systems – or legal traditions – in use around the world: common law, civil law, and theocratic law. **Common law** is based on tradition, precedent, and custom. **Civil law** is based on a very detailed set of laws organized into codes. **Theocratic law** is based on religious teachings.

Slides 2-17 and 2-18 Contract Law

A **contract** is a document that specifies the conditions under which an exchange is to occur and details the rights and obligations of the parties involved. **Contract law** is the body of law that governs contract enforcement.

Since common law tends to be relatively ill specified, contracts drafted under a common law framework tend to be very detailed with all contingencies spelled out. In civil law systems, contracts tend to be much shorter and less specific because many of the issues typically covered in a common law contract are already covered in a civil code.

When contract disputes arise in international trade, there is always the question of which country's laws apply. Many countries including the United States have ratified the **United Nations Convention on Contracts for the International Sale of Goods (CIGS)**. The CIGS establishes a uniform set of rules governing certain aspects of the making and performance of everyday commercial contracts between sellers and buyers who have their places of business in different nations.

Another Perspective: The United Nations Commission on International Trade Law provides a detailed overview of the United Nations Convention on Contracts for the International Sale of Goods at {http://www.uncitral.org/uncitral/en/uncitral_texts/sale_goods/1980CISG.html}.

Slides 2-19 through 2-22 Property Rights

Property rights refer to a resource over which an individual or business holds a legal title; that is, a resource that they own.

These rights can be violated through private or public action. **Private action** refers to theft, piracy, blackmail, and the like by private individuals or groups. **Public action** violations occur when public officials, such as politicians and government bureaucrats, extort income or resources from property holders.

Another Perspective: The U.S government's web page on intellectual property rights, {<http://www.uspto.gov>}, contains a wealth of information on intellectual property rights including information on international intellectual property rights treaties and protecting trademarks.

In the United States the **Foreign Corrupt Practices Act** makes bribing a foreign government official in order to obtain or maintain business over which that foreign official has authority a violation of United States law, and requires all publicly traded companies to keep audit records.

Slides 2-23 and 2-24 Intellectual Property Rights

Intellectual property is property that is the product of intellectual activity, such as computer software, a screenplay, a music score, or the chemical formula for a new drug. Ownership rights over intellectual property are established through **patents, copyrights, and trademarks**.

Another Perspective: The World Intellectual Property Organization's web site contains extensive information on various treaties and agreements between countries regarding the protection of intellectual property. The site is {<http://www.wipo.int/portal/index.html.en>}.

Another Perspective: The World Intellectual Property Organization offers suggestion on how exporters can avoid common pitfalls when exporting intellectual property. More details can be found at {http://www.wipo.int/sme/en/documents/wipo_magazine/9_2004.pdf}.

Slides 2-25 and 2-26 Product Safety and Liability

Product safety laws set safety standards for products and manufacturing processes. **Product liability** involves holding a firm and its officers responsible for product safety standards.

Slide 2-27 Determining a Market's Overall Attractiveness

All else being equal, countries with democratic political institutions, market-based economies, and legal systems that protect property rights and limit corruption will be more attractive than nations that lack these characteristics.

CRITICAL THINKING AND DISCUSSION QUESTIONS

QUESTION 1: Free market economies stimulate greater economic growth, whereas state-directed economies stifle growth. Discuss.

ANSWER 1: In a market economy, private individuals and corporations are allowed to own property and other assets. This right of ownership provides a powerful incentive for people to work hard, introduce new products, develop better advertising campaigns, invent new products, etc., all in the hopes of accumulating additional personal capital and wealth. In turn, the constant search on the part of individuals and corporation to accumulate wealth enriches the entire economy and creates economic growth. In contrast, in a command economy, private individuals and corporations are not allowed to own substantial quantities of property and other assets. The objective of a command economy is for everyone to work for "the good of the society." Although this sounds like a noble ideal, a system that asks individuals to work for the good of society rather than allowing individuals to build personal wealth does not provide a great incentive for people to invent new products, develop better advertising campaigns, find ways to be more efficient, etc. As a result, command economies typically generate less innovation and are less efficient than market economies.

QUESTION 2: A democratic political system is an essential condition for sustained economic progress. Discuss.

ANSWER 2: Although you can always find examples of totalitarian regimes that have achieved rapid economic growth, it seems fair to say that sustained, decades-long periods of economic growth are quite rare under totalitarianism. There is a widespread belief in the West that democratic principles are more conducive to long-term economic growth than are totalitarian ones. One of the contributing factors is that democratic systems allow for the stable transfer of power through elections, and thus provide political stability, which is an essential prerequisite for rapid economic growth.

QUESTION 3: What is the relationship between corruption in a country (i.e., bribe-taking by government officials) and economic growth? Is corruption always bad?

ANSWER 3: In the United States we show public contempt for the practice of bribery although evidence suggests that bribery is not uncommon in the United States. When government officials engage in corruption, they subordinate the interest of their country to their personal gain. They also reduce the level of transparency in business interactions. Many nations with rampant bribery appear to be among the most economically underdeveloped, yet the inflexible generalization that corruption is always bad oversimplifies the role of culture and its influence on meaning-giving. There are many cultures that accept the role of bribes far more openly than we do in the United States. That managers are aware that some countries – France, Germany and Japan for example – recognize that bribes play an important role in some parts of the world and allow their corporations to expense bribes (deduct bribes as a legal corporate expense) is important.

QUESTION 4: You are the CEO of a company that has to choose between making a \$100 million investment in Russia or Poland. Both investments promise the same long-run return, so your choice is driven by risk considerations. Assess the various risks of doing business in each of these nations. Which investment would you favor and why?

ANSWER 4: When assessing the risks of investment, one should consider the political, economic, and legal risks of doing business in both Russia and Poland. The political risk in Russia is still high but it is undergoing continual governmental changes under Putin's leadership, and courting foreign investment. Relatively, Poland is more stable, but it may have less potential. On the economic front, both countries have inflation and economic turmoil as unproductive factories are still struggling in Russia, and migrant workers returning from Western Europe are swelling Poland's ranks of the unemployed. From the legal perspective, Poland is making steady progress, while the situation in Russia is unclear. Thus at this time, the risk in Russia would clearly be higher. (For discussion or to modify this question, you might want to substitute other countries into this question depending on current events and the countries with which your students will be most familiar.)

QUESTION 5: Read the Country Focus on Venezuela under the leadership of Hugo Chávez, then answer the following questions:

- a. Under Chávez's leadership, what kind of economic system was put in place in Venezuela? How would you characterize the political system?
- b. How do you think that Chávez's unilateral changes to contracts with foreign oil companies will impact upon future investment by foreigners in Venezuela?
- c. How will the high level of public corruption in Venezuela impact future growth rates?
- d. Currently Venezuela is benefitting from a boom in oil prices. What do you think might happen if oil prices retreat from their current high level?
- e. In your estimation, what is the long run prognosis for the Venezuelan economy? Is this a country that is attractive to international businesses?

ANSWER 5:

- a. Chávez claimed to be a democratic socialist. During his 1998 presidential campaign, Chávez blasted the notion of global capitalism. Most students will probably agree that Chávez followed his ideals since winning the election in Venezuela. Chávez ensured that his powers as president were stronger than before, and he extended government control of the media. In addition, Chávez made a number of moves to increase state ownership of key industries like oil, and turned ranches and farms into workers' cooperatives. Chávez also used some of the profits from the country's oil revenues to increase government spending on various social programs, some of which are modeled after programs in Cuba.
- b. In the oil industry, which the country depends on for some 70 percent of its exports, Chávez pushed out foreign companies and expanded the hold of the state run company. Most students will recognize that by making it more difficult for foreign investors to do business in the country, in the oil industry or otherwise, Chávez threatened the country's future economic growth. In fact, the country's dependency on oil and lack of diversification into other industries has already had an impact: Inflation is running at more than 25%, and the country has had to expand its budget deficit as the government spent heavily to support its social programs that were once funded by oil revenues. The country's future without Chávez remains unclear.
- c. Corruption in Venezuela is rampant. In 2012, Transparency International ranked the country to 165 out of 174, making it one of the most corrupt countries in the world. Government officials are permitted to demand bribes in return for permission to expand operations or enter new lines of business. Many students will recognize the challenges of operating in an environment like the current situation in Venezuela. Some students will probably suggest that firms may reassess their investments given the new political and economic risks present in the country. Many students will probably conclude that a market that is considered to be only partly free, with rampant corruption and privatization taking place, is no longer a worthwhile destination.

d. During the years when oil prices were rising, Venezuela, one of the world's largest producers of oil, became very rich. Chávez funded various social programs using the oil profits. Most students will probably recognize that the recent drop in oil prices probably spells trouble for these programs. Some students may wonder whether falling oil prices could spell disaster for Venezuela's oil industry. Chávez maximized the state's share of oil revenues by pushing out foreign companies and increasing the hold of state-run Petroleos de Venezuela SA.

e. A recent World Bank study puts Venezuela as being one of the most regulated economies in the world. The move to take various enterprises under state control is also impeding economic growth. In the oil industry, for example, Chávez reduced the stakes owned by foreign companies to give the state run company a bigger position. Most students will probably conclude that given the levels of corruption and regulation, the country is just too risky to consider as a destination for international companies. Some students may also note that Freedom House's 2012 assessment that the country was only "partly free" would also deter potential investors.

Another Perspective: The U.S. Department of State maintains a web site covering the political and economic situation in Venezuela. For more details, go to {<http://www.state.gov/r/pa/ei/bgn/35766.htm>}.

QUESTION 6: Read the Management Focus feature: Did Walmart violate the Foreign Corrupt Practices Act? What is your opinion? If you think they did, what do you think the consequences will be for Walmart?

ANSWER 6: Student opinions will vary on this topic. Despite spending more than \$230 million on its own internal investigation so far, Walmart still may incur a substantial fine from the US Department of Justice. The case is still pending. For more details, go to {<http://www.forbes.com/sites/nathanvardi/2012/04/22/why-wal-mart-is-in-big-trouble-for-hushed-up-mexican-bribery-allegations/>}

CLOSING CASE: Poland's Economy

Summary

The closing case describes Poland's economic success story. Poland, unlike most countries in Europe, weathered the recent global recession better than most countries. Decisions made early in the decade and during the 1990s helped Poland develop a stable economic policy and a stable political system. The country has benefitted from its free market and free trade policies as well as its efforts to privatize state-owned businesses. Today, Poland is working to make the country even more attractive to foreign investors by simplifying tax laws, reducing tax rates, and removing bureaucratic barriers to doing business in the country. A discussion of the case can revolve around the following questions:

QUESTION 1: How was Poland able to avoid the worst effects of the economic crisis that gripped most of Europe during 2008–2009?

ANSWER 1: In 1989, Poland elected its first democratic government after more than four decades of Communist rule. Since then, like other Eastern European countries, Poland has embraced market-based economic policies, opened its markets to international trade and foreign investment, and privatized many state-owned businesses. In 2004, the country joined the European Union, giving it easy access to the large consumer markets of Western Europe. All of these steps help transform Poland into a major exporter. As a result, Poland recorded the highest sustained growth in the region from 1989 through 2010, helping keep the country stable during the 2008–2009 economic crisis.

QUESTION 2: What lessons can be derived from the Polish experience during 2008–2009?

ANSWER 2: In addition to maintaining a strong export business during the crisis, Poland has also maintained a fiscally conservative government, keeping public debt in check, and not allowing it to expand during the recession as many other countries did. The country also got lucky. A tight monetary squeeze in the early 2000s, which was designed to curb inflation and ease Poland's entry into the EU, headed off the asset price bubble, particularly surging home prices that hurts so many other economies around the world.

QUESTION 3: From the perspective of international business, what is attractive about the Polish economy? What are the weaknesses and risks associated with doing business there?

ANSWER 3: Poland's transition from a Communist country to a democratic one is a work in progress. Steps are being taken to simplify tax laws, reduce tax rates, and remove bureaucratic hurdles to doing business in the country. The Entrepreneurship Law dramatically reduced the number of health, labor, and tax controls that companies had to comply with, making it much easier to start a business in the country. In addition, the country continues to privatize state-owned enterprises, which has helped increase the country's GDP, making it attractive for foreign investment.

QUESTION 4: Even though Poland has been committed to liberalizing its economy since the collapse of communism in 1989, significant vestiges of the old system still remain. Why do you think it has taken Poland so long to transform its economic, political, and legal system?

ANSWER 4: Even after 20 years, Poland's transition from a socialist economy to a market-based system is not complete. The government continues to dismantle the bureaucratic socialist structure that was in place for more than 40 years. Its ability to keep exports strong helped Poland weather the recent economic crisis. It still needs to address the high unemployment rate of migrant workers who returned from Western Europe

countries during the European recession. Simplifying government regulations will demonstrate to foreign investors that the country is ready to do business.

Another Perspective: Information on doing business in Poland is available at {<http://www.doingbusiness.org/data/exploreeconomies/poland/>} and {<http://www.worldbiz.com/poland-c-108.html?osCsid=f4dcfe39fee3398472c8a39d15aab83b>}

INTEGRATING iGLOBES

There are several iGLOBE video clips that can be integrated with the material presented in this chapter. In particular, you might consider the following:

Title: Fate of Eurozone: Back on the Brink?

Run Time: 4:55

Abstract: This video explores the potential fate of the euro as voters in Greece reject current austerity programs, and economic and political problems continue to threaten the future of the European Union's monetary integration.

Key Concepts: globalization, European Union, euro, economic development, protectionism, global capital markets, national trade policy, currency values

Notes: European markets are in turmoil once again thanks to the growing realization that the trillion euros injected into European banks by the European Central Bank in an effort to increase liquidity in the system was in fact not a cure for the problems plaguing some countries, but instead was little more than an anesthetic. The problems in Europe have reemerged in part because of the troubles in Greece, but also because of economic and political issues across the European Union bloc.

For some time, Greece in particular has struggled to get its economy back on track, yet so far its efforts have had little effect. Now, its problems are at the forefront of the issues threatening the longevity of the euro, and indeed the viability of the European Union in general. Voters in Greece made their preferences regarding the situation overwhelmingly known at the country's recent elections where those who supported the current austerity program were soundly defeated by those who do not. In fact, additional elections are now being organized that will essentially determine whether the troubled economy will continue to remain a part of the Euro Zone. While the problems in Greece are headlining much of the focus on the future of the euro, the lack of economic growth within the European Union in general, and especially in countries like Spain, has also contributed to the uncertainty regarding the longevity of the single currency system. Unemployment remain high throughout much of the bloc, and lingering debt problems are making it

difficult to pull out of the recession that gripped the region after the global financial meltdown that began in 2008. Not surprisingly, many Europeans are unhappy with the state of affairs. Some, like the Germans, are in favor of continuing with the current austerity policies, but others like the French, believe that there may be better alternatives. Regardless, there is a common belief that something needs to be done to get the region back on track.

At one time, the notion of a country actually leaving the Euro Zone was unthinkable. Now though, some people like Zanny Minto Beddoes, editor for the *Economist*, believe that it could become a self-fulfilling prophecy. However, what will happen if Greece does leave the Euro Zone is anyone's guess. Zanny Minto Beddoes suggests that should Greece opt out, the remaining European Union countries will have to integrate their economies more quickly and to a greater extent than currently planned. Only time will tell however, whether this would be possible, or whether other countries would simply follow Greece's lead and also opt out.

Discussion Questions and Answers

1. Discuss the impact of the recession in Europe on the U.S. economy. What do the European Union's troubles mean for the United States?

Answer: A number of countries within the European Union are on the edge of economic chaos. Students may note for example, that in addition to Greece, other countries including Spain and Portugal are also in economic disarray. Most students will probably voice some concern that the troubles in these countries could spill over into other countries causing widespread economic distress. This of course would have a negative impact on the fragile economic recovery currently underway in the United States. Moreover, students may suggest that even if the status quo persists, the impact could be quite troubling for the United States.

2. Reflect on the economic and monetary discord in Europe. Should U.S. companies be concerned? Does your response change if a company does not have any direct interests in Greece? Why or why not?

Answer: When the financial crisis that began in the United States in 2008 swept around the world its impact was also felt in Europe where the economy declined in a similar way to the U.S. economy. Today, the United States is clinging to a weak economic rebound, and many companies are displaying optimism about a continued economic recovery. In contrast, while some countries within the European Union appear to be back on track, others like Greece remain in a state of economic distress. For companies, this could spell trouble. At the moment, Greece's problems are threatening to spill over into other European Union countries including Spain and Portugal. Should this occur, the entire bloc could be thrown into an economic tailspin. Because the European Union represents a large market for many U.S. companies, the problems in Europe, and in Greece in particular, are a real cause for concern. Most students will probably suggest that all U.S.

companies including those that do business directly with Greece must carefully follow the events that are still unfolding in Europe, and consider the potential implications of the situation for their business.

3. Why are voters in Greece and in some other countries so opposed to the austerity programs that have been put in place to help restore the bloc's economic stability? How, if at all, do the conservative fiscal policies affect other European Union countries?

Answer: Recently, voters in Greece overwhelmingly rejected those who believed that the current economic austerity program should continue. These voters are gaining additional support from other countries within the European Union as voters question whether the policies actually lead to stagnation of the economy and further economic distress. Indeed, in France, some are questioning whether the policies have actually made people worse off rather than better off, and whether a better alternative might exist. Many worry that the conservative approach could result in plummeting consumer confidence that could spill over into other markets creating economic chaos across the region. Now, some are pushing for a more united approach to resolving the crisis, one in which consumer confidence is restored by issuing European Union debt instruments, providing cheaper sources of funds to troubled governments, and creating Europe-wide safe assets.

4. Consider the threats to the future of the euro and the role of Greece in particular. What might European leaders learn from the current situation? How might this affect future members of the European Union?

Answer: Most students will probably suggest that the current challenges to the future of the euro and monetary union in Europe will prove to be helpful to leaders as they consider admitting new members to the bloc. In particular, students may wonder whether leaders will welcome countries that are at a different level of economic development. Students may note for example, that the economy and standard of living in general in Greece are significantly different from those of some other European Union members, especially countries like Germany and France. These differences have led to problems in the past and created controversy over policy decisions. Even now, Germany is still promoting severe austerity as a mechanism for overcoming Greece's unresolved debt problems despite the fact that Greek voters have rejected the approach. Some students may also wonder whether European Union leaders will make a stronger effort to develop greater fiscal integration as insurance against future threats to the system.

INTEGRATING VIDEOS

There are also several longer video clips that can be integrated with the material presented in this chapter. In particular, you might consider the following from *International Business DVD Volume 6*:

Title: Counterfeiting

Learning Objectives

The purpose of this video is to help you:

- ❖ Understand the nature of intellectual property.
- ❖ Explore the growth of counterfeiting and why it is more rampant in some countries.
- ❖ Examine the implications of counterfeiting and product piracy on companies.
- ❖ Recognize why it is important for firms to protect their intellectual property and identify how to limit the potential for product piracy.

Key Words

- ❖ Intellectual property
- ❖ Product piracy
- ❖ Counterfeiting
- ❖ Legal systems
- ❖ Globalization

Synopsis

Shoppers in New York City's Canal Street or Santee Alley in Los Angeles have their choice of a host of designer goods all at rock bottom prices. The only problem is that the goods are all fakes. Business in counterfeit goods like Coach purses, Louis Vuitton bags, Ray Ban sunglasses, and more is booming. Today, the market in counterfeit goods is a multi billion dollar international business that affects every industry and most products. Caroline Joiner, an executive with the U.S. Chamber of Commerce claims that product piracy and counterfeit goods is a \$250 billion per year problem for the U.S. economy. Furthermore since counterfeiters are focused on profits, and not the welfare of buyers, it is an industry that can put consumers at risk. Joiner notes for example that today's producers of fake purses could be producing fake car parts or airplanes tomorrow. In fact, counterfeit car parts are already a big problem for the auto industry. Counterfeit brake pads made of sawdust are being sold on the market as the real thing, and could be unknowingly used in taxi cabs, school buses, or semi trucks. Ford estimates that product piracy costs the company about \$1 billion per year.

The pharmaceutical industry has also been a frequent target for counterfeiters. Fake drugs are being sold over the Internet and have even made their way into mainstream outlets like pharmacies. The World Drug Organization estimates that about 10 percent of all drugs sold worldwide are counterfeit. At a government warehouse, shelves are crowded with confiscated products like fake Lipitor, fake surgical mesh, fake razor blades, and even fake toothbrushes. While the counterfeit drugs look the same as the real thing, they often lack active ingredients or are watered down versions of the real drug. These pirated products can cause allergic reactions or worsen a patient's medical condition. In some cases, they are toxic.

Counterfeiters have even infiltrated markets for everyday household products. Products like electrical cords and surge protectors are readily available, but like counterfeit drugs, they can be dangerous. A counterfeit iron for example burst into flames when it was tested in a lab. Identifying exactly which product is a fake and which is real can be difficult for consumers. To protect themselves, consumers should pay attention to prices. Prices that seem too low could be a warning signal that the product is a fake. Consumers should also try to shop at reputable businesses and avoid buying at flea markets. In addition, consumers should inspect product packaging. Products that lack a serial number or do not have a country of origin label could be counterfeit.

Discussion Questions

1. Discuss the explosive growth of the counterfeit goods industry in recent years. What factors have facilitated its expansion?
2. Reflect on the implications of product piracy for companies. How can companies protect themselves from counterfeiters?
3. Consider the challenges involved in stopping product piracy. Why is it so difficult for countries to crack down on counterfeiters?
4. Product piracy is especially prevalent in the global pharmaceutical industry. Reflect on why intellectual property rights are so important to pharmaceutical companies.

INCORPORATING globalEDGE™ EXERCISES

Use the globalEDGE™ site {<http://globalEDGE.msu.edu/>} to complete the following exercises:

Exercise 1

The definition of words and political ideas can have different meanings in different contexts worldwide. In fact, the *Freedom in the World* survey published by Freedom House evaluates the state of political rights and civil liberties around the world. Provide a description of this survey and a ranking (in terms of “freedom”) of the world’s leaders and laggards. What factors are taken into consideration in this survey?

Exercise 1 Answer

Search phrase: *Freedom in the World* or *Freedom House*

Resource Name: Freedom House Surveys

Website: <http://www.freedomhouse.org/reports>

globalEDGE Category: [Publications](#)

Additional Info:

Published annually since 1972, the survey ratings and narrative reports on 195 countries provide insight into an assessment of global political rights and civil liberties in each

country. Political rights ratings are based on an evaluation of three subcategories: electoral process, political pluralism and participation, and functioning of government. Civil liberties ratings are based on an evaluation of four subcategories: freedom of expression and belief, associational and organizational rights, rule of law, and personal autonomy and individual rights.

Exercise 2

As the chapter discusses, differences in political, economic, and legal systems have considerable impact on the benefits, costs, and risks of doing business in countries around the world. It also has a considerable impact on how easy it is to do business in these countries. The *World Bank Doing Business Indicators* measures the extent of business regulations in countries around the world. Compare the United States, France, Japan, Brazil, and Nigeria in terms of how easily contracts are enforced, how property can be registered, and how investors can be protected. Identify in which area you see the greatest variation from one country to the next.

Exercise 2 Answer

Search phrase: *World Bank Doing Business Indicators*

Resource Name: World Bank: Doing Business Indicators

Website: <http://www.doingbusiness.org/>

globalEDGE Category: [Statistical Data Sources](#)

Additional Info:

The World Bank's Doing Business Project provides objective measures of business regulations and their enforcement across 189 economies and selected cities at the subnational and regional level. To construct the indicators, two types of data are utilized: First, the relevant laws and regulations in each country are reviewed in detail. Second, official fee schedules and expert respondents' estimated of time each procedure takes is taken into account.