

Dilemma of the Developing Countries: Economic Growth and IPR Protection

By Yung Terd Lu

The ancient Chinese empire is the original producer of true porcelain. Some potters invented kilns that burned potteries at higher temperature than ordinary kilns. The potteries burned in these kilns turned into ceramics with glasslike surfaces. Soon, porcelain creation spread over China and certain provinces become famous for the types of porcelains that they created. Porcelain production was no longer only for domestic consumption, but was also available for international exports through the Silk Road to reach Europe. However, the secret behind making porcelain was still kept within China. The secret soon leaked out to Japan, Korea and along the Silk Road, and different potters created their own variations of it. Soon, porcelains with cobalt blue Arabic motif came out of Central Asia. China's may lose its creating porcelain methods but its people benefitted from innovative outside attempts in modifying porcelains. The blue and white porcelains are now widely used within China and around the globe.¹ This essay will discuss why certain countries will "steal" intellectual property from other sources and its relation with economic prosperity as well as suggested route of development.

The ancient Chinese may have increased competitions from losing out its "intellectual property", but the society as a whole benefitted from more varieties for consumption. Porcelain creation could be considered an improved form of pottery making in the past. Joseph Schumpeter's works often focused on the idea that innovation and technology are the driving force behind industrial development. He coined the term "creative destruction" to represent the replacement of old methods with newer, more efficient ways of doing things through innovation

¹ Brief history of Chinese porcelain given by Professor Bradley Farnsworth of University of Michigan during a lecture.

to support long-term economic growth. Gutterman interpreted the Schumpeter's line of thought and argues that IPR protection would increase domestic R&D, subsequently increasing the flow of new products and enhancing the value of patent rights. In return, this would increase the inward investment and technology transfer that would lead to improvements in the local knowledge base, a win-win situation for the local economy.² Yet, this is not necessarily the case if the developing countries do not have the adequate knowledge or technology to begin this cycle of R&D. Thus, influx of foreign knowledge is necessary to jumpstart the economy, often through mimicking the methods and processes from foreign intellectual sources. So, is a strict IPR protection always the better option? As the porcelain indicates, if the secret of porcelain making remained in China, some porcelain varieties would never have appeared. Keeping the secret in China would have slowed the innovative force that created diverse varieties of porcelain, a slight contradiction to the Schumpeter-championed "creative destruction".

Therefore, most developing countries do not comply with the Western standards of IPR protections. They need the technological transfer from the Western world, to build up the local knowledge bases and to develop their economies. Thus, imitations appear when local companies enter the market and reverse-engineer foreign goods. Certain industries in some developing countries consist mostly of illegal goods manufacturing. To consider the severity of IPR breach, the software market in China, for example, is made up of mostly pirated software.³ Robert L. and Ostergard Jr. found that empirically, stronger IPR protection in developing economies does not correlate to higher economic growth; the marginal benefits of stronger IPR protection are often

² Robert L. & Ostergard, Jr., *Development Dilemma: The Political Economy of Intellectual Property Rights in the International System* (New York: LFB Scholarly, 2003), 46.

³ Pat Choate, *Hot Property* (New York: Alfred A. Knopf, 2005), 5.

negligible and sometimes have negative impacts instead of promoting economic growth.⁴ Hence, the argument that strong IPR protection is essential to local economy improvement by Gutterman and others is not valid in the case of developing economies.

The East Asian miracles of the twentieth century depend on low IPR protection to fuel their economic growth. Japan, South Korea, Singapore, Taiwan and Hong Kong started out by copying or acquiring intellectual capitals from the Western industries. These governments implemented import substitution policies and encouraged the local manufacturing industries to produce these goods. Of course, the local industries lack the knowledge to produce the goods independently and resorted to imitating the imports. Through lacking IPR protection, these industries have access to foreign technologies and from them, seek to improve the local knowledge base. Japan use a different approach with high IPR protection, but the cost of purchasing these rights is so minimal because the Japanese government policies aide Japanese firms to gain access on foreign patents and knowledge.⁵ Glass argues that imitation industries in developing countries build up local knowledge, that make the cost of innovation attractive to local firms. According to Glass, it is necessary for developing countries to have higher resource accumulation as indicated by high savings rate or low IPR protection to promote innovative R&D. The East Asian tigers took both these options to build up their economies.⁶

Developing countries could develop their economies by depending on low IPR protection, but they cannot continue this for the long term. It will also stifle the growth of domestic firms within the countries. If the original producers of these products do not get any

⁴ Robert, L and Ostergard, Jr., 59 & 156.

⁵ Pat Choate, 138 – 168. Within those pages are methods of how the Japanese firms extract secrets from foreign companies.

⁶ Amy Jocelyn Glass, "Imitation as a Stepping Stone to Innovation".
<http://www.biz.uiowa.edu/econ/seminars/fall99/glass.pdf> (accessed February 12, 2010).

form of recognition such as monetary compensation from their inventions, they would be frustrated because their hard work spent on designing new products are reverse-engineered and sold by someone else. This situation will disrupts the sustainable growth of the domestic industry which otherwise can be a pillar for the domestic economy growth. Another problem associated with low IPR protection is the quality of the goods produced. The quality of imitations usually does not amount to par as the original goods because they are not subjected to the original producers' higher manufacturing standards. Plus, the main attraction of these imitated goods is their low price and the manufacturers might forgo quality for cost. In May 2004, two hundred babies died due to fake infant formula sold in Anhui and Shandong provinces. Manufactured counterfeit toys are painted with white lead base paint that is hazardous to health.⁷ The citizens in developing countries may benefit from economic improvement but it cannot be worth it if it comes at the cost of others and their health.

As the developing countries' economies grow so too should their IPR protection. The lack of IPR might jumpstart the economy, but it is not beneficial in the long run. Since the local domestic firms are also afflicted by the plight of negligible IPR protection, their own industries are also under threat from the imitation industry. Government should gradually revamp the IPR laws over time so that the market can adjust accordingly. Developed countries should not just criticized developing countries over the lack of IPR protection; instead they should help them develop their industries faster so that the benefits of tighter IPR outweigh the cost of implementing it. More FDI should be poured into the developing economies, and with this as a

⁷ Pat Choate, 6-11.

bargaining tool, negotiate for stricter IPR protection.⁸ It is ironic how the Asian tigers nowadays have some of the best IPR protection relative globally.⁹

IPR is essential for the growth of the economy. While many believe that strong IPR protection lead to better economic development, Robert et al argued that it does not make a significant impact on the economic growth of developing countries. Instead, strong IPR may have some negative effect on growth. Glass supported this through her research on the East Asian tigers' model that these countries developed because they adopted a strategy of high savings and low IPR protection to stimulate the economy. So, it is not fair to criticize developing countries for not providing enough IPR enforcement because developing countries want the opportunity to develop too. However, this should not be continued for the long term because there are negative externalities on the domestic industries and society. Some imitated goods should not be consumed for the risk of damage to the wellbeing and health of the people. To counter this, developing countries could with low IPR enforcement, but should increase it as their economy grows in order to negate the negative effects of lacking IPR. It is important to find equilibrium between safeguarding and keeping IPR loose to develop budding industries and also, to maintain a sustainable economy for the nation.

⁸ Amy Jocelyn Glass. Foreign direct investment (FDI) pushed the resource constraints outwards and permits R&D to grow, an alternative compared to low IPR protection.

⁹ According to result from Heritage Foundation, which provide an index including property rights protection.