



Why do countries export fakes?

The role of governance frameworks, enforcement and socio-economic factors



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Context

Trade in counterfeit and pirated goods poses a serious and growing risk to economic growth, undermining good governance, the rule of law and citizens' trust in government.

In order to provide policy makers with reliable empirical evidence about this threat, the OECD and the European Union Intellectual Property Office (EUIPO) joined forces to develop an understanding of the scale and magnitude of the problem. The results published in previous reports, *Trade in Counterfeit and Pirated Goods: Mapping the Economic Impact* (2016) and *Mapping the Real Routes of Trade in Fake Goods* (2017), show that trade in counterfeit and pirated goods amounted to up to 2.5% of world trade in 2013. Counterfeit and pirated products originate from virtually all economies on all continents, although middle-income and emerging economies tend to be relatively prominent players.

This report offers an opportunity to further analyse these findings to assess what are the drivers that will make an economy more likely to become active in the trade in fake goods, which can serve in designing efficient policy responses to close the governance gaps. The results show that governance, production facilities, the existence of free trade zones, as well as the way that trade facilitation policies are implemented, are all factors that are impacting an economy's propensity to trade in counterfeit goods.

Executive summary

Trade in counterfeit goods is a longstanding – and growing – socio-economic threat to effective governance, efficient business and the well-being of consumers worldwide, and is becoming a key source of income for organised criminal groups. It also damages the engine of economic growth, by destroying firms' revenues and undermining their incentives to innovate.

Existing empirical studies, including the recent OECD-EUIPO studies *Trade in Counterfeit and Pirated Goods: Mapping the Economic Impact* and *Mapping the Real Routes of Trade in Fake Goods* have found that counterfeit and pirated products originate from virtually all economies on all continents, although their intensity of involvement varies. Some tend to be important producers or transit points in trade in fake goods, whereas their neighbours play only marginal roles.

This report seeks to answer the question of why some economies are more involved in counterfeit trade than others. It draws on large datasets to quantify the various socio-economic conditions that determine an economy's propensity to become an active actor in the trade in fake goods. The analysis finds five main drivers:

Five main drivers

- 1. Governance:** high levels of corruption and poor quality of intellectual property protection are factors that affect the degree of exports of fake goods from an economy.
- 2. Free trade zones (FTZs):** FTZs offer a relatively safe environment for counterfeiters, with good infrastructure and limited oversight. The share of fake goods from economies hosting the 20 biggest FTZs is twice as big as from economies that do not host any FTZs.
- 3. Production facilities:** low labour costs and poor labour market regulations are important drivers of trade in counterfeit and pirated goods. Improving working conditions, by raising the minimum wage or increasing paid leave, could decrease the share of counterfeit and pirated products exported, especially by economies with weak governance.
- 4. Logistics capacities and facilities:** the ability to trace and track consignments is the key factor for reducing the share of counterfeit and pirated products in exports. However, other

factors increase this trade, including low shipping charges; fast, simple and predictable customs formalities; and good quality trade and transport related infrastructure (e.g. ports, railroads, roads or the information technology). These factors tend to increase counterfeit trade in economies that are highly corrupt.

5. Trade facilitation policies: The way of implementing trade facilitation matters. Enhancing transparency is likely to reduce economies' likelihood to export fakes: availability of detailed information on trade flows, degree of involvement of an economy in the trade community; transparent and regular review of fees and charges imposed on imports and exports; and sound internal co-operation between border agency and other government units. Other factors, tend to encourage counterfeit trade, such as advance rulings (i.e. where the administration asks traders about the classification, origin, valuation methods etc. applied to specific traded goods), and the possibility to appeal administrative decisions of the border agencies. Importantly, the factors that potentially encourage counterfeit trade tend to be particularly pronounced in highly corrupt economies.

Of these five drivers, gaps in governance, especially high levels of corruption and gaps in intellectual property rights enforcement, are the crucial factor for trade in fakes, multiplying the effects of FTZs, logistic facilities or trade facilitation policies. The presence of FTZs is a particularly strong driver of trade in counterfeit and pirated goods in economies with weak governance, high corruption levels and a lack of IPR enforcement.

While all the factors identified above matter, it is important to note that none of the factors outlined above *alone* can explain the intensity of exports of fakes from a given economy – it is the combination of numerous factors that allows important nodes in counterfeit trade to emerge. Another key aspect to note is the fact that many of the factors presented above can actually be extremely beneficial for trade in general, such as good logistics facilities. It is the *misuse* of these facilities that can result in higher flows of trade in fake goods. The degree to which this misuse occurs depends greatly on the level of governance in an economy, particularly corruption and IPR enforcement. The challenge from the perspective of policies is to reduce the scope for misuse, while keeping open the possibility to benefit from trade.

Why do some countries export fakes?

POOR GOVERNANCE

Corruption, bribery, poor IP legislation and weak enforcement create favourable conditions for counterfeiting.

Governance factors, in addition to their direct effect, also multiply the influence of other factors on trade in fakes. Good governance is a catalyst that greatly deters the effects that logistics, trade measures or FTZs have on illicit trade in counterfeits.

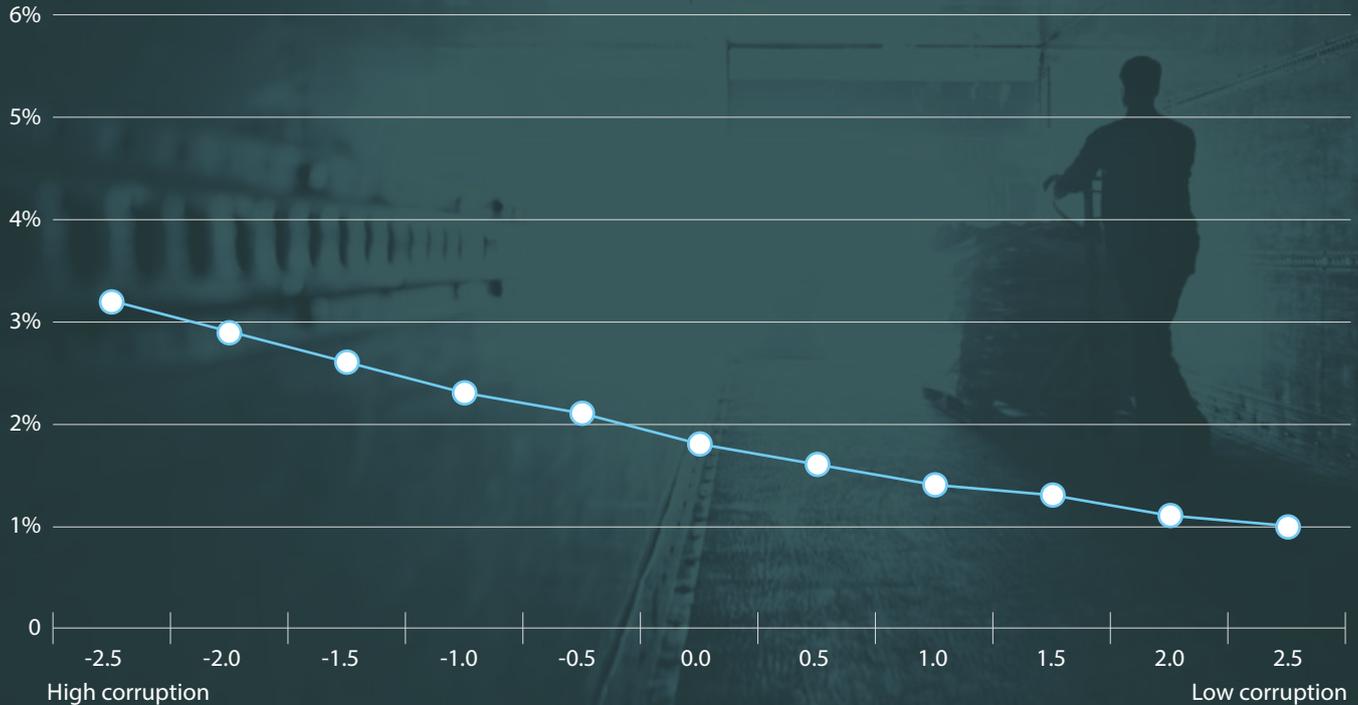
Governance aspects that affect export of fakes:

Bribery	Enhances
Sound Intellectual property protection	Reduces
Control of corruption	Reduces



Predicted share of fake exports depending on the level of corruption control

Share of exports of counterfeit and pirated goods

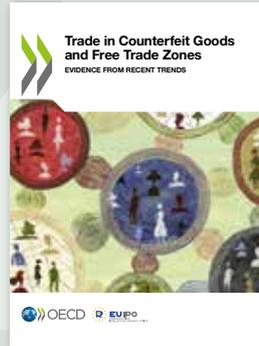


Why do some countries export fakes?

MISUSE OF FREE TRADE ZONES (FTZs)

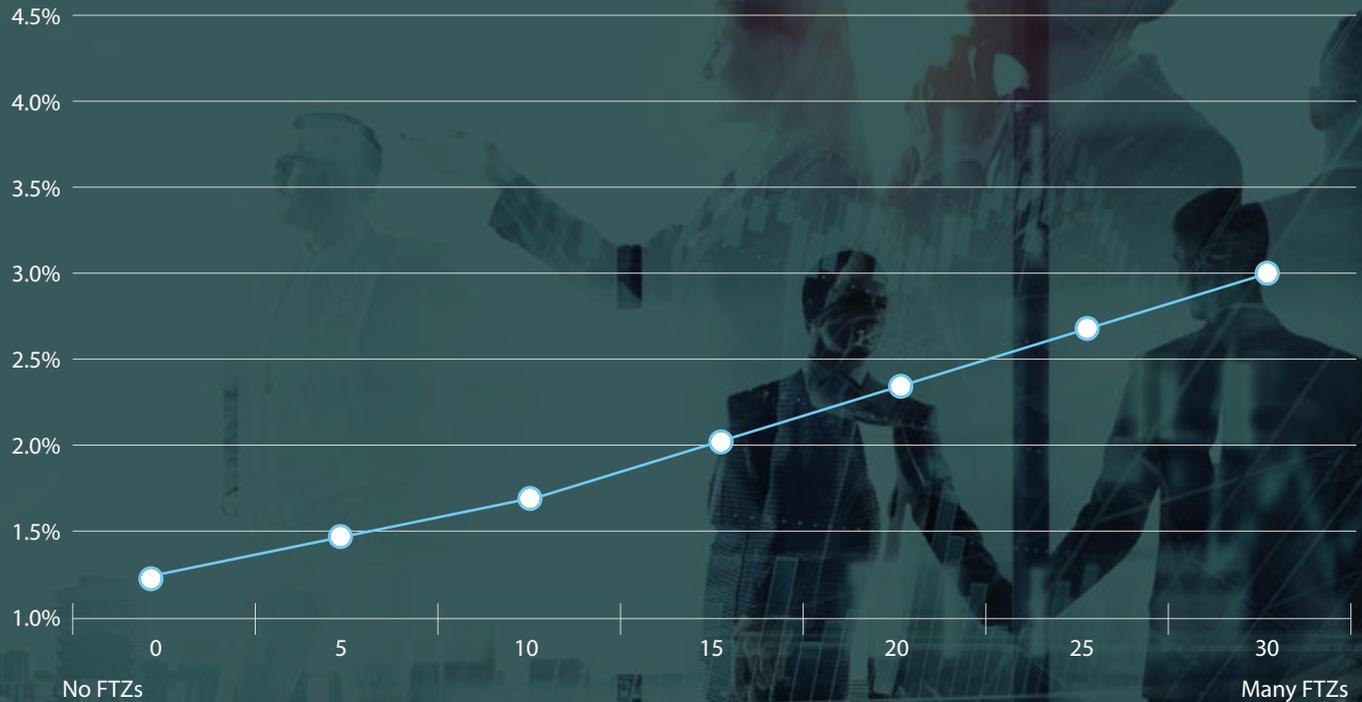
Lightly regulated zones, especially in countries with poor governance, offer a relatively safe environment with good infrastructure and limited oversight; they can spur trade in counterfeit and pirated products.

See *Trade in Counterfeit Goods and Free Trade Zones*, OECD/EUIPO (2017) that confirms the links between FTZs and trade in counterfeit products.



Predicted share of fake exports depending on the number of FTZs

Share of exports of counterfeit and pirated goods



Why do some countries export fakes?

MISUSE OF PRODUCTION FACILITIES

Developed and cheap production facilities, and poor working conditions are factors that seem to favour trade in fake goods.

Aspects of production that affect export of fakes:

Higher minimum wages

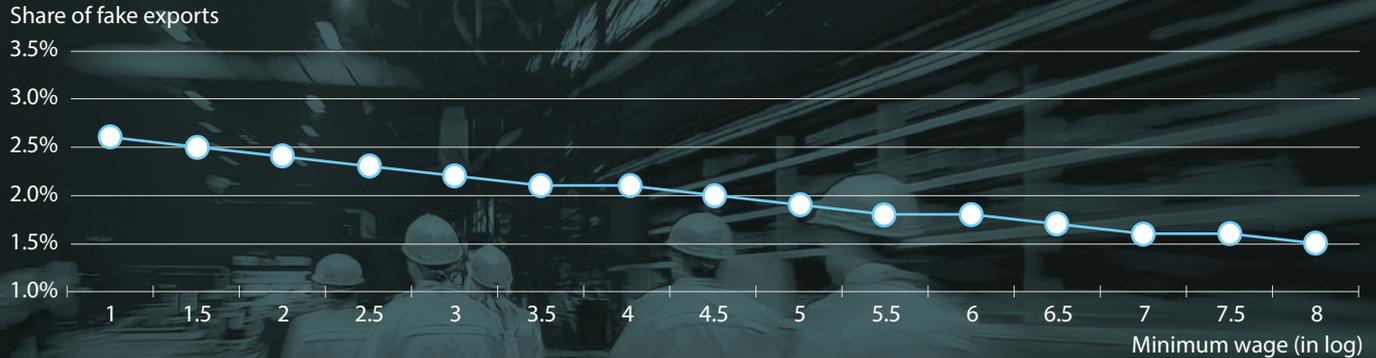
Reduces

Increased annual paid leave

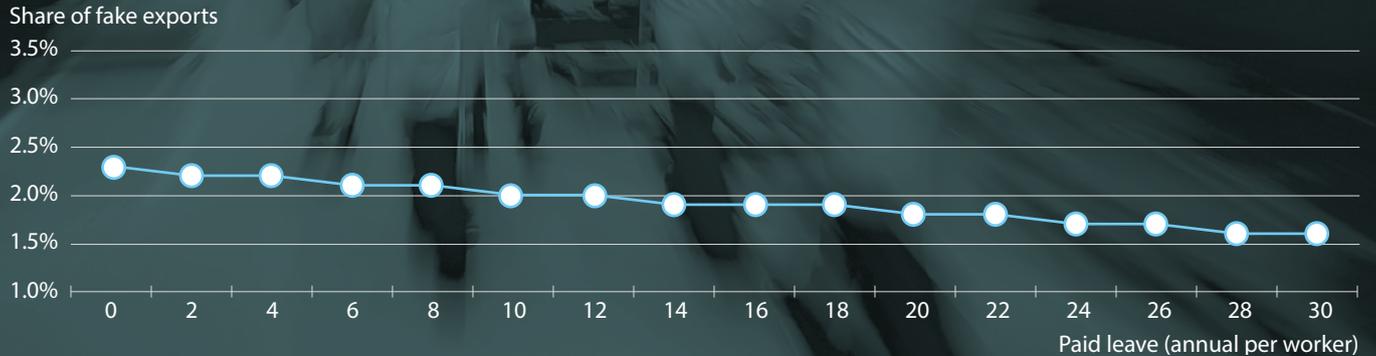
Reduces



Predicted share of fake exports depending on the value of minimum wages



Number of annual days of leave per worker



Why do some countries export fakes?

LOGISTICS CAPACITIES AND FACILITIES

In **corrupt countries** with weak IPR protection, the ease of management of both inbound and outbound materials, parts, supplies and finished goods also facilitates trade in fakes.

Transparency is the key! The ability to trace and track shipments reduces trade in fakes even in economies that are corrupt.

Logistics capacities related to exports of fakes:

Ability to track and trace consignments

Reduces

Competitively priced shipping

Enhances

Speed, simplicity and predictability of customs clearance process

Enhances

Quality of transport infrastructure

Enhances



Impact of the ability to trace and track consignments on the share of counterfeit and pirated exports

Share of fake exports



Why do some countries export fakes?

TRADE FACILITATION POLICIES

If a country is corrupt, specific trade facilitation measures can enhance trade in fakes, instead of boosting the ease of doing business and the fight against counterfeit trade.

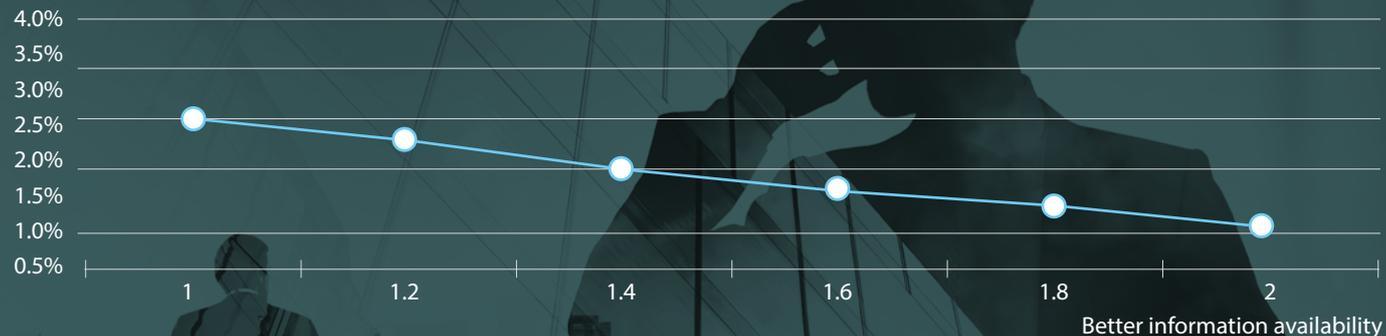
Four aspects of trade policies can significantly reduce the extent of illicit trade in fakes:

1. Greater availability of trade information
2. Deeper involvement in the world trade community (i.e. structure for consultations with traders; established guidelines for consultations; publications of drafts; existence of notice-and-comment frameworks).
3. Disciplined, transparent and regularly reviewed fees and charges imposed on imports and exports
4. Sound internal co-operation between various border agencies.



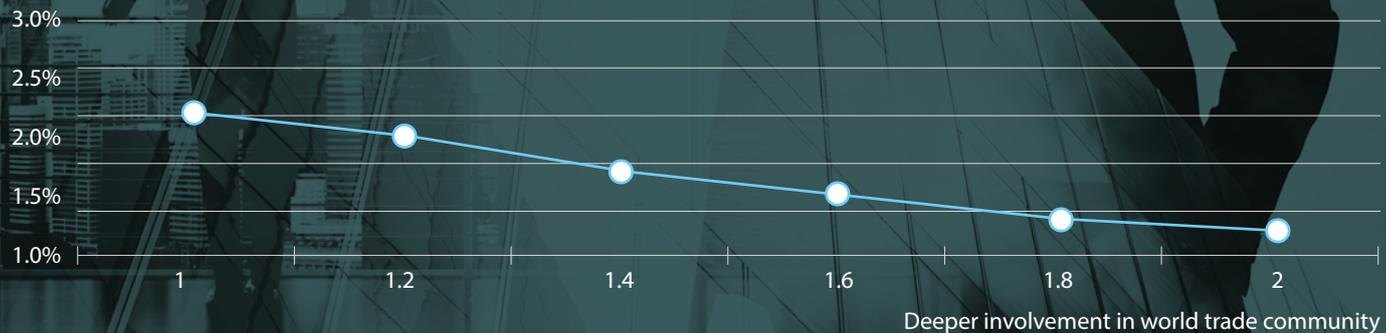
Predicted impact on exports of fakes depending of trade information availability

Share of fake exports



Involvement in the world trade community

Share of fake exports



Important!

1. None of the factors outlined above *alone* is responsible for trade in fakes. It is the *combination* of these factors that allows important hubs in trade in counterfeit and pirated goods to emerge.
2. Many of the factors that contribute to counterfeit trade are also very beneficial for general trade flows. For example, good logistic facilities are desirable from the trade perspective in terms of efficiency and their welfare-enhancing effect. It is the *misuse* of these facilities, usually in the context of corruption and other governance-related failures, that is the problem.



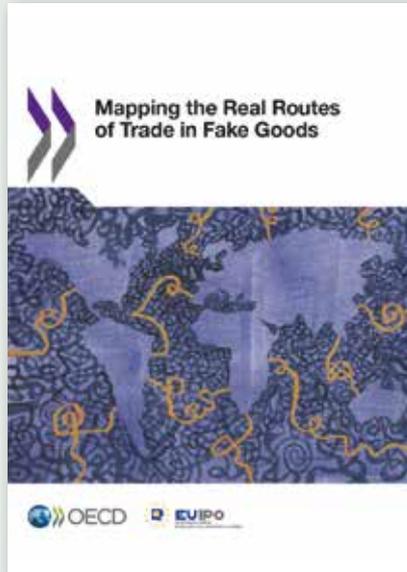


For further research

Some exporters of fakes for example Hong Kong (China) and Singapore, have excellent profiles. Great logistics and trade policies, excellent governance, low corruption and respect for IP. More research is needed to understand why these economies are such important nodes for the trade in fake goods.

There are also economies, such as Senegal or Pakistan that are significant sources of fakes, and are among the poorest performers in terms of governance quality, quality of trade and logistics infrastructure etc. Further investigation could provide more information about the nature of counterfeit trade in these economies, and help to identify “low hanging fruit” in terms of policy solutions to counter this threat.

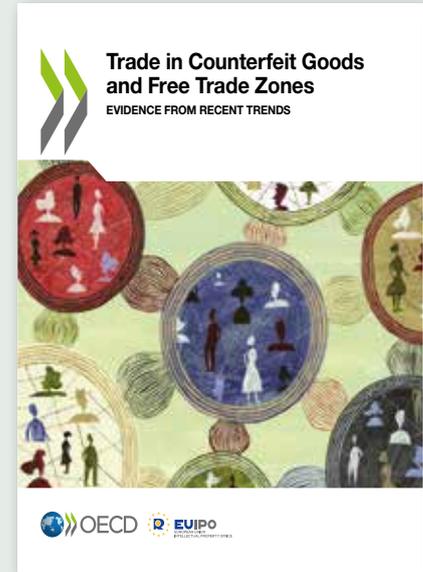
Further reading



Mapping the Real Routes of Trade in Fake Goods



2017 Situation Report on Counterfeiting and Piracy in the European Union



**Trade in Counterfeit Goods and Free Trade Zones:
Evidence from Recent Trends**





THE ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

The OECD is a unique forum where the governments of 35 democracies work together to address the economic, social and environmental challenges of globalisation. The OECD is at the forefront of efforts to understand and to help governments respond to new developments and concerns, such as corporate governance, the information economy and the challenges of an ageing population. The Organisation provides a setting where governments can compare policy experiences, seek answers to common problems, identify good practice and work to co-ordinate domestic and international policies.

www.oecd.org

The OECD Task Force on Countering Illicit Trade (TF-CIT) convenes governments and a wide range of stakeholders to map and analyse the underlying dynamics of illicit trade. Its evidence-based research and advanced analytics draw attention to the convergence of criminal networks that operate illicit trade, from counterfeits to narcotics, from excise goods to the trafficking of persons and wildlife. The goal of the TF-CIT is to foster public policies, international cooperation and public private partnerships that deter and reduce illicit markets.

<http://oe.cd/tfcit>



Managed by the EUIPO, THE EUROPEAN OBSERVATORY ON INFRINGEMENTS OF INTELLECTUAL PROPERTY RIGHTS is a network of experts and specialist stakeholders.

The Observatory's objectives are to:

- Provide evidence-based contributions and data to enable EU policymakers to shape effective IP enforcement policies and to support innovation and creativity;
- Provide data, tools and databases to support the fight against IP infringement;
- Provide knowledge and learning programmes for IP and enforcement authorities as well as for businesses and IP practitioners;
- Develop initiatives to help innovators, creators and businesses (especially SMEs) protect their IP rights;
- Design campaigns to raise awareness of the value of IP and the negative consequences of IP infringement.

<http://euiipo.europa.eu>

For other reports:

<http://euiipo.europa.eu>

