

# The Economist

## Knock-offs catch on

Fake goods are proliferating, to the dismay of companies and governments

IMITATION is supposed to be the sincerest form of flattery, but that is not how most brands see it. On March 1st Philip Morris, a tobacco giant, sued eight American retailers for selling counterfeit versions of its Marlboro cigarettes. Thanks to the rise of the internet and of extended international supply chains, and more recently, to the global economic downturn, counterfeit goods are everywhere. Fake Porsches and Ferraris zoom along the streets of Bangkok. A German bank has discovered an ersatz gold ingot made of tungsten in its reserves, according to a German television channel investigating persistent reports that many of the world's financial institutions have been similarly hoodwinked. NASA, America's space agency, has even bought suspect materials.

Counterfeiting “used to be a luxury goods problem”, says Therese Randazzo, who is in charge of protecting intellectual property at America's customs service.

Now people are trying to traffic counterfeit items that have a “wider effect on the economy”, she says, such as pharmaceuticals and computer parts. A new study by America's Department of Commerce shows that fakes have even infiltrated the army. The number of counterfeit parts in military electronics systems more than doubled between 2005 and 2008, potentially damaging high-tech weapons.

The OECD estimates that the international trade in counterfeit and pirated goods was worth around \$250 billion in 2007. The International Anti-Counterfeiting Coalition (IACC), a lobby group, says the true figure is actually closer to \$600 billion, because the OECD's estimate does not include online piracy or counterfeits that are sold in the same country as they are made. Counterfeit goods make up 5-7% of world trade, according to the IACC.



Several factors have contributed to the growth of counterfeiting in recent years. The shift of much of the world's manufacturing to countries with poor protection of intellectual property has provided both the technology and the opportunity to make knock-offs. The internet in general, and e-commerce sites like eBay in particular, have made it easier to distribute counterfeit goods. MarkMonitor, a firm that helps companies defend brands online, estimates that sales of counterfeit goods via the internet will reach \$135 billion this year.

The recession in the rich world may also have given a boost to counterfeit goods. Frederick Mostert of the Authenticity Foundation, an anti-counterfeiting group, has noticed a “spike” in knock-offs this recession, as consumers short of money trade down from the real thing. Cost-cutting measures may also have made firms' supply chains more vulnerable to counterfeit parts. In 2008 the value of fake goods seized at America's borders increased by nearly 40% over the year before. It subsequently fell by 4% last year—far less than the 25% decline in imports overall (see chart). In Europe in 2008 customs services confiscated more than double the previous year's haul of counterfeit goods.

Businesses, which feel the revenues lost to counterfeiters all the more acutely in a downturn, are making an even greater effort to root out impostors. Complaints from Louis Vuitton, a luxury-goods firm, for example, led to nearly 9,500 seizures of knock-offs last year, 31% more than in 2008. Lawsuits brought by companies against manufacturers and distributors of counterfeits are at an all-time high, says Kirsten Gilbert, a partner at Marks & Clerk Solicitors, a British law firm.



The technology used to counter pirates is also becoming more sophisticated. Holograms are a cheap way to distinguish real items from fakes, although counterfeiters are getting better at copying them. Special inks, watermarking, and other “covert” technologies (meaning those invisible to the naked eye) are becoming more popular as a result. Many “brand protection” firms have also started to peddle radio-frequency identification (RFID) technology to help companies track shipments. This allows firms to tag boxes and crates with chips which send out signals identifying them as authentic.

The most foolproof technique for identifying genuine goods involves incorporating materials with special genetic markers into the packaging or product itself. Firms or officials can then literally check an item’s DNA to ensure that it is real. This is more expensive than other anti-counterfeiting measures, but companies with very valuable wares, such as the grandest wineries, are splurging on it. James Hayward,

the boss of DNA Applied Sciences, which sells such technology, insists that new clients are “knocking down our door”, in spite of the recession.

Online brand-protection services, which track counterfeiters on the web for their clients, are also thriving. OpSec Security, which provides physical and online brand protection, has seen revenues from its online monitoring business grow by more than 20% annually for the past two years, even as revenues for its shipping services declined (because companies are shipping fewer items). MarkMonitor raised the price of its online brand-protection service by 18% last year because demand was so high. America’s biggest firms spend \$2m-4m a year to combat counterfeiting on average—a figure that is growing along with internet shopping.

Governments are also boosting their efforts to crack down on counterfeiting, which deprives them of tax revenue in addition to harming legitimate businesses. Counterfeiting and piracy cost G20 economies €62 billion (\$85 billion) a year in lost taxes and higher spending on unemployment benefits, according to a study by Frontier Economics, a consultancy. For every dollar invested in the fight against counterfeiting in America, the government receives \$5 in extra tax revenue, estimates the US Chamber of Commerce, a business lobby. In recent years France and Italy, among others, have enacted laws that threaten consumers who buy fake goods with steep fines and even imprisonment.

America appointed its first “IP tsar” last autumn and is developing a new enforcement strategy. The European Union has formed an anti-counterfeiting “observatory” to collect better data and disseminate tips on how best to detect fake goods. The EU, America and Japan, among others, are also discussing a new treaty, called the Anti-Counterfeiting Trade Agreement (ACTA), that would strengthen international controls on counterfeits and piracy. It is expected to be launched later this year.

But in China, where 80% of the world’s fake goods are thought to be produced, officials are loth to crack down on a thriving local business. China is not expected to sign ACTA—undermining it before it has even been unveiled. Perhaps China could make a just-as-good fake treaty instead.

The  
Economist