Abstract

This paper examines the effects of intellectual property rights (IPR) protection on foreign direct investment (FDI) and innovation. Northern firms develop quality improvements and may shift production to the South through FDI. Due to weak protection of IPR in the South, Southern firms may then copy the product designs of multinationals. This risk of imitation shortens the expected duration of profits for multinational firms. But an increase in aggregate expenditure and the North-South relative wage makes multinational profits larger while they last, and this effect dominates. Hence imitation encourages FDI, which releases Northern resources from production, and thus increases innovation.

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1. Introduction

Intellectual property rights (IPR) protection is the subject of heated debate in international policy negotiations. Many developing countries feel that the Trade-Related Aspects of Intellectual Property (TRIPs) agreement signed in the Uruguay round benefits rich countries at the expense of the poor. McCalman (2002) finds evidence sympathetic to their view: his calculations indicate that the United States is the major beneficiary and developing countries are major contributors. Consequently, developing countries are now pushing to have