

INTELLECTUAL PROPERTY PROTECTION AND OFFSHORE
SOFTWARE DEVELOPMENT: AN ANALYSIS OF THE U.S.
SOFTWARE INDUSTRY

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Abstract

Most writers who have examined the role of intellectual property protection in developing countries have argued that better protection generally has positive economic effects, whether measured in terms of increased foreign direct investment or rates of modernization and development. These studies suffer from one or more of the following limitations:

- 1) they fail to differentiate between the impact of intellectual property protection on different industry sectors;
- 2) they mistake a correlation in the data for a causal connection between intellectual property protection and foreign direct investment, and;
- 3) they ignore other factors that affect investment decisions such as software firm and market structures, intellectual property protection strategies of US companies, information costs and the business practices of local suppliers.

This project examines the impact of the level of intellectual property protection of a developing country on the level of overseas investments in software research and development. The data collected shows that there is at best, a very weak relationship between levels of intellectual property protection (as measured by software piracy rates and US Trade Representative designations) and levels of foreign direct investment in

software development for any particular country. This paper advances the following explanations for this state of affairs:

First, organizational and market considerations act as inhibiting factors of overseas investments in software research and development. At the firm level, companies concentrate their human capital involved in research and development to maximize collective learning and stimulate innovation. At the market level, the overwhelming weight of the US market encourages software companies to locate their research and development activities in this country. This facilitates effective and timely response to changes in market conditions.

Second, intellectual property protection is viewed by US software companies as a means of protecting and recouping research and development costs, but considered only as one of a number of factors influencing overseas investment decisions. This goes some way towards explaining why some countries with weak protection are leading recipients of foreign direct investment by US software companies.

The weak relationship between intellectual property protection and overseas investments jeopardizes developing country commitment to improve public enforcement. It is plausible that public enforcement can be improved if local software suppliers spearhead efforts to improve intellectual property protection.

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