

Cipla Case

- The Setting

- Key Players

- Strategic Options

Exhibit 6 AIDS Infection and Treatment Rates for Selected Regions, 2002

	# of People Infected	% of All People Infected, Worldwide	Deaths in 2002
North America	980,000	2%	15,000
<i>United States</i>	670,000	2%	8,963
Western Europe	570,000	1%	8,000
Latin America and Caribbean	1,940,000	5%	102,000
Sub-Saharan Africa	29,400,000	70%	2,400,000
<i>South Africa</i>	4,950,000	12%	360,000
North Africa & Middle East	550,000	1%	37,000
Eastern Europe & Central Asia	1,200,000	3%	25,000
Asia & Pacific	7,200,000	17%	485,000
<i>India</i>	3,970,000	9%	310,000
<i>China</i>	1,000,000	2%	17,000
Australia & New Zealand	15,000	0%	100
Total	41,855,000		3,072,100

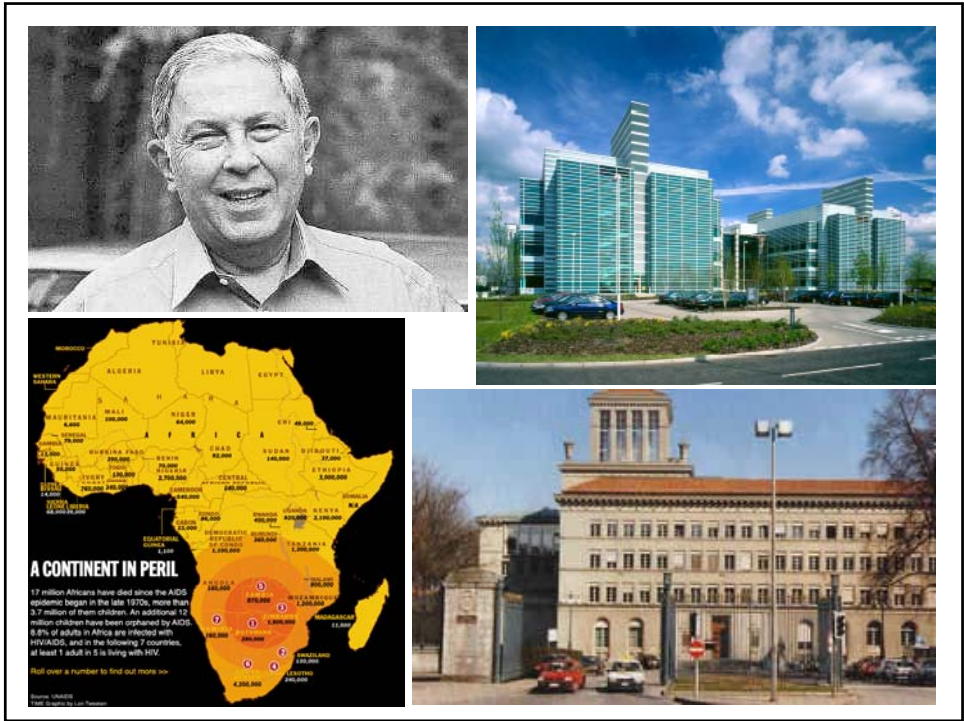


Exhibit 4 Financials for Top Multinational Pharmaceutical Corporations and Cipla, 2001

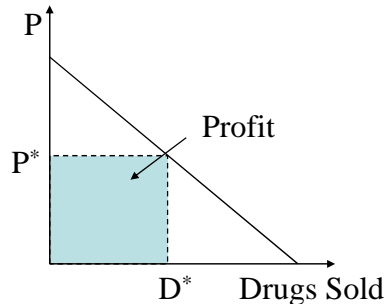
Company	Corporate Headquarters	Net Sales (in US\$ millions)	Selling, General and Administrative	R&D	Material and Production Costs	Pre-tax Profit
GlaxoSmithKline	UK	29,504	36%	12%	22%	30%
Boehringer Ingelheim	Germany	7,360	na	15%	18%	13%
Bristol-Myers Squibb Company	US	19,423	27%	12%	29%	27%
Merck and Co., Inc.	US	21,199	27%	12%	17%	47%
Cipla	India	221	8%	0.2%	48%	22%

Source: Company annual reports, 2001.

Can Intl Pharma Charge Low Prices in Poor Countries?

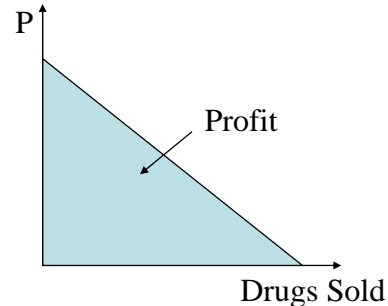
Single World Price

- Choose single worldwide price to maximize profit
- Assume zero marginal cost to make drug



Price Discrimination

- Now choose different price for each buyer: capture their entire willingness to pay



- Price discrimination possible only if: (1) know different buyers' willingness to pay; (2) buyers can't resell good to each other; (3) different prices will be "allowed" by public

Cipla's Strategic Options

- Option #1: Give up
 - Shift away from copying patented drugs
- Option #2: Influence "rules of the game"
 - Remake TRIPS (and/or its interpretation) to preserve existing business model
- Can Cipla win?

The WTO

- What is the WTO?
- The Operation of the WTO
- Firm Strategy & the WTO

The WTO

- What is the WTO?
 - The Bretton Woods Institutions
 - The GATT
 - The Uruguay Round and the Birth of the WTO

The Bretton Woods Institutions

- At close of World War II, view that war was partly caused by economic desperation of the Great Depression
- View that Great Depression was exacerbated by terrible international economic coordination through the 1930's
 - e.g. Smoot-Hawley act of 1930 in USA
- Result: A “three-legged stool” of international institutions negotiated in 1944 to support international economic prosperity
 - the International Monetary Fund (IMF)
 - the World Bank
 - the International Trade Organization (ITO)

Bretton Woods, New Hampshire, 1944



↑
Henry Morgenthau
(US Treasury Secretary)

↑
John Maynard Keynes

The GATT

- Unlike the IMF and World Bank, the ITO was never ratified
- The General Agreement on Tariffs and Trade (GATT)
 - Negotiated in 1947
 - Provided rules for negotiating future free trade agreements
 - Only covered trade in goods -- not services
 - Many exceptions (e.g. textiles, agriculture)
- GATT the organization
 - When ITO failed, GATT also became a formal organization based in Geneva
 - GATT the organization had no real enforcement powers

The GATT: Two Key Principles

- The “most-favored-nation” (MFN) principle
 - Any tariff concession made to one GATT member must also be made to all other GATT members (but exceptions)
- The “national treatment” principle
 - Once imported through customs, a foreign good cannot be taxed or regulated differently from domestic goods
- These principles intended to force large-scale negotiations among nations, prevent retaliation against individual nations, and encourage transparency
- These principles survive at the core of the WTO

The Birth of the WTO

- Uruguay Round negotiated from 1986-1994
- GATT the *organization* eliminated, replaced by the WTO
 - WTO has real power to enforce agreements
- GATT the *agreement* remains, with significant new tariff reductions worldwide
- Plus massive expansion of scope of trade agreements
 - GATS – Trade in services (banking, insurance, tourism, etc)
 - TRIPS – Intellectual property protections
 - TRIMS – reduce obstacles to foreign investment
 - Many others (new agreement runs 22,500 pages!)

The WTO

- The Operation of the WTO
 - The Dispute Settlement Body
 - Examples

The WTO's Dispute Settlement Body

- Unlike the GATT, the WTO can enforce its trade agreements
- The Dispute Settlement Body (DSB) in Geneva adjudicates
 - A *country* files a complaint with the DSB
 - DSB forms a panel of experts, who make a finding
 - If complaint found valid, petitioning country may impose equivalent tariff penalties *on whatever goods they want* as long as offending country does not change behavior
- Any country can appeal DSB decision to Appellate Body
 - 3-member panel formed to make final determination
- Whole process must take less than 15 months

Example: U.S. Steel Tariffs

- U.S. employs “safeguard” provisions of WTO
 - Claims increased imports causing damage to domestic steel industry
 - Enacts temporary protections in 2002
- EU, China, Japan, etc, file complaint with DSB
 - DSB rules against US, and Appellate Body supports ruling
 - US refuses to eliminate protections at first
 - EU and other countries allowed to retaliate
 - EU allowed \$2Billion in tariff retaliation annually
 - Eventually targets Florida exports
 - U.S. repeals steel tariffs



Example: US-China IP Dispute (Counterfeiting)

- U.S. based copyright-oriented industries estimating \$2-4 Billion in losses annually in China, pressing US government to act
- U.S. brings WTO case in 2007, alleging TRIPS violation
 - Primary complaint: criminal penalties too weak in China
 - Minor complaint: China auctions off seized counterfeit goods
- DSB rules January 2009
 - US wins on minor complaint. Now China will have to destroy seized goods (comply by March 2010)
 - US loses main element of case. Suggests that WTO is unwilling to intervene strongly on criminal codes

Summary: The DSB

- Relatively Powerful
 - Decides whether domestic laws/policies are valid within international trade system
 - Application of penalties left to parties involved
 - No further appeal: Appellate Body has last word
- Relatively Active
 - 399 disputes filed, 1995 to end of 2009
 - 122 of these disputes seen through to formal ruling
- Stakes are rising with TRIPS, etc
 - DSB may ultimately rule on who gets access to life-saving medications

The WTO

- What is the WTO?
- The Operation of the WTO
- **Firm Strategy & the WTO**

The WTO

- Firm Strategy & the WTO
 - WTO Impact Strategies
 - Example: Textiles
 - Example: The TRIPS agreement
 - Strategy & Ethics

WTO Impact Strategies

- *Change the “rules of the game”*
 - Can you change the international system of trade?
- Strategy #1: Clarify existing rules in your favor
 - e.g. DSB cases
 - e.g. Domestic law
- Strategy #2: Keep sectors outside the WTO
 - e.g. Clothing/textiles
 - e.g. Agricultural products
- Strategy #3: Force sectors into the WTO
 - e.g. IP-intense industries and TRIPS
 - e.g. Service industries and GATS

Example: Textiles

- History
 - 1950: US cotton apparel firms fear Japan, create barriers
 - 1961: Short Term Arrangement on Cotton Textiles
 - 1974: “Multifiber Agreement” (MFA)
 - Expands to other textile products
 - Complicated web of country-specific import quotas
 - Renewed and expanded, again and again...
 - 1995: WTO born, agreement to kill MFA over 10 years
- January 1st, 2005
 - The MFA is dead...did U.S. notice?

Example: the TRIPS Agreement

- Initiated largely by IP industries in developed countries
 - Pharmaceuticals, agro-chemicals, entertainment, computer software, luxury consumer goods
- Existing international organization (WIPO) had no teeth
- Strategic method = *coalition building* = create maximal political leverage to force change
 - Build coalition of industry associations across countries
 - Profit incentives aligned across firms and industries: more IP protection is better
 - Powerful enough to help draft text in Uruguay Round
- TRIPS is born with birth of WTO

Key Provisions of the TRIPS Agreement

- TRIPS harmonizes international IP law
 - Common standards on what is patentable
 - + “national treatment”
 - = foreign firms have equivalent rights in your jurisdiction
 - Patents receive at least 20 years of protection
 - Copyrights receive at least 50 years of protection
- Developing countries implement with a delay
 - 2005 for most developing countries (e.g. India)
 - 2016 for 49 poorest developing countries

Why did Developing Countries agree to TRIPS?

- Log-rolling in Uruguay Round
 - TRIPS initially blocked by developing countries
 - But later gave way in exchange for concessions elsewhere
- Developing countries distracted by GATS
 - Concerned about foreign banks and other service industries entering their domestic markets
 - GATS also largely driven by industry associations
- Technology development strategy
 - Some poorer countries realized IP protection encourages foreign high-tech entry, domestic firms to adapt/innovate

Last Word: Strategy & Ethics

- TRIPS is direct result of significant non-market efforts by western IP-oriented industries
 - TRIPS brings increased profits to these industries
- What about social benefits?
 - Is TRIPS about the “gains from trade”?
 - Tradeoff between innovation incentives and short-run market access: How big of a market needs to be protected?
- Ethics & Strategy: Reducing barriers vs. Increasing barriers
 - GATS vs. TRIPS
 - Tariff jumping vs. Anti-dumping petitions