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The Myth of Diversification

**Moorad Choudhry and
the Treasury Team at
Europe Arab Bank discuss
Modern Portfolio Theory**

Bridging Boundaries for Shared Solutions

Preview of the Fifth Global Congress on Combating Counterfeiting and Piracy

The Role of Competition Policy in the
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The Challenge Is Now

When the global downturn recedes and the world gets back to normal it is not going to be the normal the west is used to. The collapse of the western banking system has changed perceptions. Global economic power has shifted east and the structures and legal systems the west created will inevitably change.

Will capitalism look like it did six months ago? Or is a new economic model emerging? A new configuration of geopolitical forces is emerging. China, India and the G20 are gaining power at the dawn of a new US administration. Continental Europe, having been hit hard by the financial crisis, will distance itself from the Anglo Saxon capitalism of the last three decades. A new agenda, with its multilateralism and global institutions to protect the entire world, is emerging, with the choice to be made at the summit of the Group of 20 in London in April.

Whatever model develops will need to accept the economic realities of today and not fight the protectionist battles of yesterday. The developing economies of the east do not need to accept western labour rules, environmental standards and the like. Those politicians calling for global standards to ensure the status quo should be aware of the consequences. There is still economic growth in the emerging giants of the east whilst the west is saddled with the consequences of the myopia of their politicians and regulators. The wealth is drifting eastwards.

It will not be possible for the west to have exclusivity at the international financial meetings that govern the world economic order. A meeting without the BRICs involved is a meeting with the wrong people involved. A system that imposes western rules and practices to the exclusion of all else will not be effective or acceptable.

The priorities for the summit of the Group of 20 countries in London in April will be to form the agenda for the global economy in 2009-10. The banking system has to be treated to enable normal trade to resume. Then a new financial architecture needs to be established. If everyone could calm down and adopt a more measured view of the likely long-term damage to bank balance sheets, much of the crisis would be over and the appropriate measures could be taken to build a new financial regulatory environment.

A Downing Street briefing paper on the London summit calls for "visionary leaders" to act as one. "This crisis is an opportunity," it says. "The world's leading economies can come together and lay the foundations not just for a sustainable economic recovery, but also for a genuinely new era of international economic partnership, a global deal, in which all countries have a part to play and all will see the benefits."

Let us hope that the west sees sense. The challenge is now. ■

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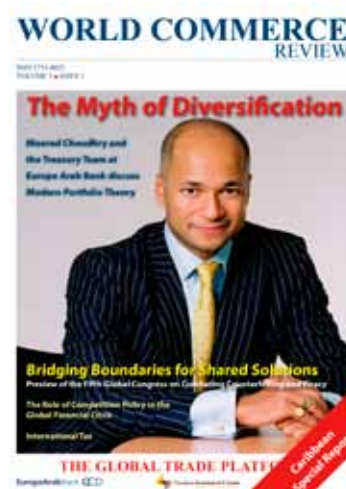
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The Role of Competition Policy in the Global Financial Crisis

Principal contributors: Calvin Goldman and Navin Joneja of Toronto, Canada; significantly assisted by members of the Competition Committee of the Business and Industry Advisory Committee to the OECD (BIAC), including Rufus Ogilvie Smals (United Kingdom), Pascal Durand-Barthez (France), Paul Lugard (Netherlands) and John Taladay (United States)¹

The following article summarises the recent statement of the BIAC Competition Committee submitted to the ongoing OECD discussions regarding competition policy and the financial crisis

In the OECD Strategic Response to the Financial and Economic Crisis, it is stated that the “world is currently facing the most severe financial and economic crisis in decades” and further emphasised that “competition policy considerations should play an important role not only in financial sector bailouts and restructuring but also in the subsequent recovery.”²

This article discusses the appropriate role of competition policy and the likely challenges that competition authorities will face going forward as a result of the global financial crisis. In assessing the appropriate role of competition policy in this context, governments should try to achieve an effective balance between appropriate regulatory oversight on the one hand and the continued reliance on normative competition principles on the other. In the latter part of this article, we offer specific suggestions, principally directed toward competition law and other regulatory agencies, that will help facilitate this balance in practice. In doing so, we focus on the relationship between competition authorities and other government regulators and make specific proposals as to how the agencies might effectively interact with each other in addressing critical issues that arise out of the global financial crisis. Finally, we note that the OECD, and in particular its Competition Committee, is well positioned to play a leading and constructive role in this area.

The need for balance between prudential/regulatory oversight and normative competition principles

Various views have been expressed as to the causes of the global financial crisis. Many commentators suggest that the crisis has some footing in a lack of proper regulatory oversight by financial sector authorities in various countries in relation to certain key areas (eg, inadequately regulated housing mortgage distribution markets and related security products, and failure to apply adequate risk management practices).³ Notwithstanding the debate over the precise nature of the cause of the crisis, there is a broad consensus that the global financial crisis was not a result of a failure of effective competition policy. As such, there is no good reason to exclude competition and market considerations from decisions that will need to be made in this crisis concerning the restructuring of industries and economic sectors going forward. Accordingly, the challenge for governments is to find the right balance between financial sector regulation directed towards ensuring prudential and fiscal viability on the one hand and applicable norms of competition policy on the other hand, in order for industries and sectors to have the maximum opportunity to grow over the longer term.

In this respect, it is important that we distinguish between regulatory failures and market failures. The global financial crisis was caused or contributed to by a series of regulatory failures both at national and international levels, as well as a series of risk management failures within the private sector. Our many years of experience and learning all suggest that faith in a market-based system should not be eroded as a result of this crisis. Competitive markets produce more wealth and efficiency, as well as economic stability and security, than any other system. Excessive economic controls by central governments have proved largely to be less efficient and less wealth maximizing. In short, competition policy should not be ignored or temporarily set aside; rather it must be utilized as a tool or necessary input within the overall economic and financial policy framework applicable to decisions made in the context of the financial crisis. Furthermore, as history has shown, competition policy can serve to act as a stabilizing force and provide legal certainty in uncertain economic times.⁴ Accordingly, in formulating policy measures to address the economic crisis, governments should strive to the extent realistically

possible to have competition norms be part of the decision-making process.

Nobel Prize winning economist Joseph Stiglitz explained that even Adam Smith, who is often regarded as a staunch proponent of free markets, recognized that some regulation is necessary:

“Adam Smith, the father of modern economics, is often cited as arguing for the ‘invisible hand’ and free markets: firms, in the pursuit of profits, are led, as if by an invisible hand, to do what is best for the world. But unlike his followers, Adam Smith was aware of some of the limitations of free markets, and research since then has further clarified why free markets, by themselves, often do not lead to what is best..”

Government plays an important role in banking and securities regulation, and a host of other areas: some regulation is required to make markets work...

The real debate today is about finding the right balance between the market and government...Both are needed.”⁵

Indeed, in his Inaugural Address, President Obama stated:

“Nor is the question before us whether the market is a force for good or ill. Its power to generate wealth and expand freedom is unmatched, but the crisis has reminded us that without a watchful eye, the market can spin out of control...”⁶

However, rather than see the pendulum swinging to excessive regulation and intrusion on an overly draconian basis, we suggest there should be a careful and well-thought out balancing of the principles applicable to crisis management and prudential regulation on the one hand, and the

maintenance of normative competition, free market principles on the other. Debates about lessons to be learned from the financial crisis must not be about the “end of capitalism” or the “failure of the market economy.” In this regard, we can and should draw upon lessons from the past. For example, we certainly have much more learning at this stage regarding the importance of such competition norms and the


dangers of protectionism than had been the case during the early part of the Great Depression.⁷

As a result, policy discussions concerning the appropriate scope of regulation need to be based on facts and not be driven by ideology or opportunism. For example, empirical evidence and analysis should continue to guide the policy action and the implementation of solutions. Markets should be kept open and transparent but subject to appropriate regulatory supervision. No matter how tempting it may be to protect and promote “national champions”, increased state intervention in the economy should be treated with care. The process of deregulation and increased reliance on competition policy should continue in relation to markets that are presently excessively regulated especially in newly industrialized nations. Finally, a certain degree of risk-taking is necessary in order to promote and foster innovation.

Specific suggestions concerning competition law enforcement policy going forward

Competition law agencies will have an increasingly important role to play in achieving a sensible balance between regulatory oversight and normative competitive principles on a going forward basis. We offer the

“...the challenge for governments is to find the right balance between financial sector regulation directed towards ensuring prudential and fiscal viability on the one hand and applicable norms of competition policy on the other hand”



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following suggestions:

First, competition authorities should work in tandem, right from the outset, with sector specific regulators, especially in relation to critical issues in the financial services sector. Financial regulators should apply their expertise in regulating standards of prudence, while competition authorities should apply normative competition provisions and their wealth of experience in the review of business conduct, significant acquisitions and major restructurings. In order to achieve this, mechanisms need to be in place to allow for close coordination of their respective teams on the ground, right from the beginning of the matter. In essence, competition authorities should be included in the decision-making process concerning the overall framework resolution; in other words, competition law agencies should be invited to join the public sector discussions, and should accept the invitation to be at the table as early as possible.

In addition, practical experience suggests that effective coordination between two or more public sector bodies necessitates full information sharing between them. Such information sharing must be done in a manner that protects the confidential and competitively sensitive information that either or both statutory authorities need to respect; if necessary, waivers and other regulatory protection should be established to allow for this full sharing of such information. Experience in parallel merger reviews among domestic competition authorities from different nations has shown that the best way to avoid contradictory conclusions, which can produce uncertainty and delay, is to have teams on the ground (preferably experienced analysts and case officers) who could work together from the beginning of the process. This will significantly reduce the potential for conflicts and ought to give rise to the greatest likelihood of properly informed decision-making.

A second recommendation directed towards competition law enforcement agencies is that they need to have tools available to operate with sufficient speed and flexibility to complete even large and complicated reviews in an expeditious timeframe when the circumstances warrant, particularly in the area of mergers and restructurings. We note by way of example the new emergency rescue powers that European Commissioner Neelie Kroes has referred to recently as an important adjunct to her powers to decide mergers regulating financial institutions in a very short timeframe.⁸ We also note in this context that representatives of the United States Department of Justice are able to work expeditiously with representatives of the United States Federal Reserve Bank and share requisite information on an expedited basis when necessary. In our view, these are both examples of

the kind of timely and procedural flexibility that competition authorities need to have available in order to be able to contribute to the decision-making process in the context of a financial crisis. In essence, we suggest that competition authorities should have in place a framework for such situations so that they can play an effective role in what are often very limited timeframes. We therefore suggest that national competition authorities consider crafting not only substantive criteria (which may include failing firm principles) but also procedural criteria that will allow decision-making to be done in an expedited and orderly manner.

Third, we suggest that the OECD can play a leading and constructive role on a going forward basis having regard to its relevant experience and areas of expertise. The Competition Committee of the OECD has a history of developing Recommendations and Best Practices in areas such as exchange of information between competition authorities, merger reviews and anticompetitive practices affecting international trade. We would suggest that the OECD Competition Committee could work towards establishing guidelines or best practices for cooperation between competition law authorities and financial sector regulators. This would ultimately establish a suggested framework for procedures allowing representatives of the two agencies to confer as early as possible and share all relevant financial and market related information, all under the umbrella of respecting all appropriate confidentiality protections. These procedures would ultimately assist in coordinating and expediting reviews and, as mentioned earlier, should also assist in avoiding potential conflicts.

We also suggest that the OECD Competition Committee could develop guidelines or best practices directed toward the substantive and procedural criteria applicable by the competition authorities in evaluating business practices during critical industry or economic crisis situations (eg, situations where a firm is failing or in danger of failing). By way of examples, these best practices could try to establish considerations relevant to determining likely insolvency without having to wait for actual insolvency; or the criteria and timelines that should be applicable to any "search" for a competitively preferable purchaser. Some of these criteria are already incorporated in national guidelines.⁹ The same would apply to procedural best practices directed toward trying to ensure that the competition authority is able to contribute, on an expedited basis, its input into the decision-making process.

Business remains committed to the application of competition norms in the context of the financial crisis and looks forward to continued engagement with governments and other relevant stakeholders on these issues. ■

1. Founded in 1962 as an independent organisation, the Business and Industry Advisory Committee to the OECD (BIAC) is the officially recognised representative of the OECD business community. BIAC's members are the major business organisations in the OECD member countries and a number of OECD observer countries, www.biac.org.
2. OECD Strategic Response to the Financial and Economic Crisis at pages 6 and 10 (paragraph 13). 2009. This OECD publication is issued under the responsibility of the Secretary-General of the OECD. It is available at www.oecd.org.
3. See E Andrews, Greenspan Concedes Error on Regulation, *The New York Times*, October 23, 2008 (source: <http://www.nytimes.com/2008/10/24/business/economy/24panel.html>); A Faiola, E Nakashima and J Drew, What Went Wrong?, *The Washington Post*, October 15, 2008 (source: <http://www.washingtonpost.com/wp-dyn/content/article/2008/10/14/AR2008101403343.html>); and T Donohue (President and CEO, US Chamber of Commerce), Reforming Financial Regulations, *uschamber.com* magazine, December 2, 2008 (source: <http://www.uschambermagazine.com/content/081202.htm>). In a January 13, 2009 speech, Ben S Bernanke, Chairman of the Federal Reserve, stated "High on the list, in light of recent events, are strengthening regulatory oversight and improving the capacity of both the private sector and regulators to detect and manage risk." (source: <http://www.federalreserve.gov/newsevents/speech/bernanke20090113a.htm>). See also D Gerard, Managing the Financial Crisis in Europe: Why Competition Law is Part of the Solution, Not of the Problem, *Global Competition Policy*, December 2008 (source: www.globalcompetitionpolicy.org).
4. See D Gerard, Managing the Financial Crisis in Europe: Why Competition Law is Part of the Solution, Not of the Problem, *Global Competition Policy*, December 2008 (source: www.globalcompetitionpolicy.org).
5. See Daniel Altman, Managing Globalization. In: Q & Answers with Joseph E Stiglitz, Columbia University and The International Herald Tribune, Oct 11, 2006.
6. See Text of Inaugural address by President Barack Obama (Jan 20, 2009) available at <http://www.whitehouse.gov/blog/inaugural-address/>
7. See paper by John Fingleton, CEO, UK Office of Fair Trading, entitled "Competition Policy in Troubled Times", January 20, 2009 (source: http://www.oft.gov.uk/shared_of/speeches/2009/spe0109.pdf) where he states, inter alia: "The credit-crunch raises a more general risk that the emphasis on open, competitive markets and the benefits that they deliver is reduced or even lost as part of an over-regulatory response. The suspension of competition rules by the Roosevelt administration in 1933 is argued to have added to the duration of the Great Depression, and government intervention to restrict competition in 'structurally depressed industries' prolonged the Japanese recession in the 1990s. On top of the clear evidence that competition contributes positively to productivity growth and competitiveness, these episodes should serve as a warning against the attractive sirens of reduced competition."
8. For example, Neelie Kroes, the European Commissioner of Competition, has stated: "The College of Commissioners has granted new powers to ensure that rapid decisions are made to protect our future...Using these powers, I am able to decide favourably on emergency rescue measures of financial institutions within a very short timeframe, including over the weekend, to protect our future." See Competition policy and the financial/banking crisis: taking action (source: http://ec.europa.eu/commission_barroso/kroes/financial_crisis_en.html) (as displayed Jan. 20, 2009). See also The Enforcer: Can Neelie Kroes, Europe's competition chief, stand up to governments as well as companies?, *The Economist*, January 10th, 2009, p 59, which highlights the importance of flexibility in these circumstances.
9. For example, several jurisdictions, such as the European Union, the US and Canada, have a "failing firm" doctrine whereby antitrust authorities will take into consideration whether a firm is failing (eg, by examining the firm's financial statements, projected cash flows, indebtedness) in determining the competitive effects of a merger. See Part VIII of the EU's Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, Official Journal C 31, 05.02.2004, p 5-18 (source: <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2004:031:0005:0018:EN:PDF>). See section 5.0 of the US 1992 Horizontal Merger Guidelines (source: <http://www.usdoj.gov/atr/public/guidelines/hmg.htm#5>). See also subsection 93(b) of Canada's Competition Act and part 9 of the Merger Enforcement Guidelines regarding failing firms (source: [http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/vwapj/2004%20MEGs.Final.pdf/\\$file/2004%20MEGs.Final.pdf](http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/vwapj/2004%20MEGs.Final.pdf/$file/2004%20MEGs.Final.pdf)).

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Keeping Borders Open During the Global Downturn: What are the Policy Options?



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No one blames international trade in goods and services, supply chains and outsourcing, and migration for getting the world economy into its current state, but that doesn't mean that any profound policy shift away from open borders won't have systemic consequences in the shorter to medium term (affecting the depth of the recession and the speed of any eventual recovery) and over the longer term (influencing the future viability of export-led development strategies and jeopardizing the potential for international trade cooperation for decades to come).

There is a lot at stake here—and the purpose of this piece here is to tackle head-on any complacency and to describe several government policies which could form the basis of a package of measures that the G20 governments could adopt at their April summit in London, UK. In principle nothing would prevent other governments doing likewise. Indeed, the governments of the world could extend any measures worldwide and possibly codify them in accords at the World Trade Organization (WTO).

Four forms of complacency

Some policymakers and analysts, even those well versed in trade, seem to be taking a nonchalant view towards international commerce in the current severe global downturn. Some reckon the lessons of the 1930s - when trade restrictions deepened the Great Depression - are well known and that protectionism won't regain its hold. Paradoxically, others are more jaded about political leaders, believing the latter will take mercantilist steps to promote exports and discriminate against foreign commerce, irrespective of any commitments made in trade accords including the "binding" agreements of the World Trade Organization.

Meanwhile, after the machinations of the Doha Round negotiations (launched in 2001 and still nowhere near finished) with its adverse impact on the credibility of trade negotiators, trade ministers, and the WTO, others are sceptical that even if government leaders knew the right thing to do, they couldn't get their acts together. Finally, some (typically generalists) in government reckon commercial policy is easy to fathom, unlike the complexities of international finance where expert advice is frequently sought, and so there is little need for new policy thinking.

Discussions of the possible steps to keep borders open during these troubled times need to take account of these four perspectives. In what follows, I draw upon very recent evidence to address some of these points, making the case that it is unwise to take the relatively open world trading system for granted.

Don't take open borders for granted

Fortunately, to date, no major trading nation has raised trade barriers across the board. Still, this has not prevented slews of unfair trade cases, reductions in export taxes and taxes on imported intermediate goods, and outright tariff increases from happening in certain sectors. No doubt these steps plus the souring mood accounts for the alarming rise in the frequency with which terms associated with protectionism are being reported in the world's newspapers. As the chart shows, mentions of the infamous 1930s Smoot Hawley tariff were eight times as frequent in the last quarter of 2008 than in 2007. Mentions of devaluation, bailouts, "Buy America" measures, and protectionism are all up. While not every such mention relates to a protectionist act, collectively the world's journalists are reporting a clear shift in discussions on commercial policy away from the era of globalization and open borders that we have become accustomed to.

Discrimination against foreign commerce can take many forms. Malaysia, for example, recently instructed its firms to layoff foreign nationals first.¹ This is a big concern for the 300,000 Indonesians working in Malaysian factories, especially as recent estimates suggest a third of them will be fired soon. Migrant workers, such as these, sent home collectively \$251 billion in remittances in 2007 alone, which financed much consumption of essentials and investment in the world's poorer na-

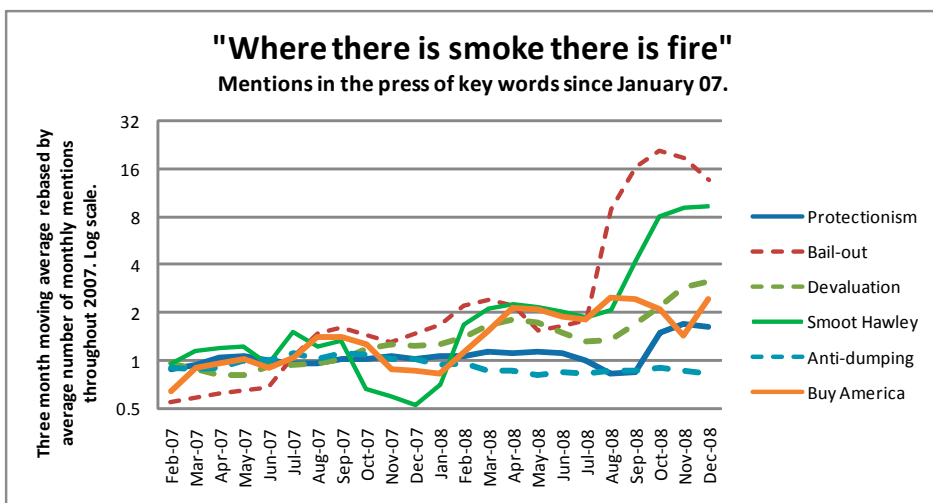
tions. Greater flows of people, parts, components, and investments across borders have substantially expanded the ways governments can discriminate against foreign commerce and its adverse impact. The knock-on effects are much more complex than in the post-war world of tariffs and quotas. Plus governments can be very good at disguising protectionist measures as benign domestic policy changes, such as altering health and safety standards in a way that is more costly for foreign firms to comply with than domestic firms.

Another cause of concern is that national living standards are dependent increasingly on sales to foreign markets, whether it be direct through exports or indirectly through supply chains and subsidiaries established overseas. The latest annual report of the US Council of Economic Advisers stated that in 2006 twenty percent of American manufacturing jobs were generated directly and indirectly by exports. Moreover, US exporting firms have per worker productivity levels a quarter higher than firms that do not engage in international trade and the former pay their workers 13-18 percent more. Given most other economies are far more export dependent than the USA, the contribution of exports to national living standards around the globe is considerable. Protectionism puts this contribution at risk.

In addition, while experts can debate the finer points of East Asia's emergence, almost every account points to the importance of export-led growth. Sophisticated supply chains organize production and sometimes design throughout East Asia, all with goal of ultimately shipping goods to North America, Western Europe, and Japan. This crisis has been brutal on international supply chains, such as those operating in clothing and apparel. The number of apparel suppliers filing shipping manifests to US Customs fell from 22,099 in July 2008 to 6,262 in October 2008, a 70 percent fall. Among the 70,000 foreign apparel suppliers tracked by one company, 40 percent had seen year-on-year drops of export volume to the US of 75 percent or more.² This is particularly worrying as many suppliers establish their credentials in the fourth quarter of each year in the rush up to Christmas.³

What affects exports soon affects jobs. According to the Chinese Ministry of Human Resources and Social Security 4.85 million jobless migrant workers had returned home by the end of November 2008, raising the total number of migrants out of work to over 10 million. One advisor to the Chinese State Council (cabinet) said that 670,000 firms had closed in 2008 because of the financial crisis and that 6.7 million jobs had been lost. One in eight recent graduates, totally 1.5 million, were expected to be without jobs at the end of 2008.⁴

But rising unemployment is not confined to China. Indonesian business associations estimate that 1.5 million jobs there will be lost in 2009.⁵ Recently, the Federation of Indian Export Organisations estimated that up to 10 million jobs could be lost in the first quarter of 2009 in its labour-intensive export industries.⁶ Fears have been expressed in both Beijing and New Delhi that rising jobless will lead to social unrest.





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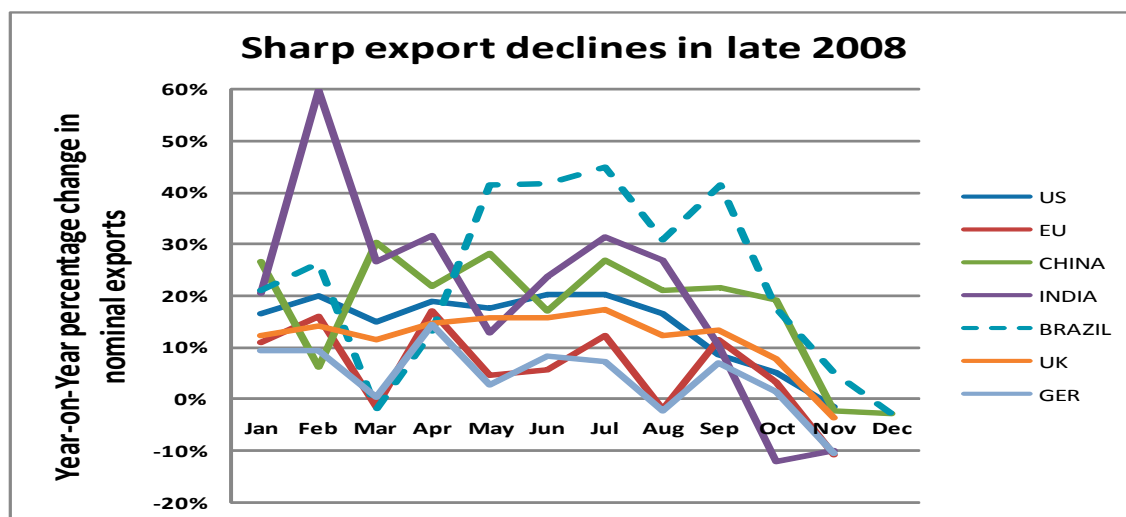
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All in all, the sharp downturn in exports witnessed in the latter part of 2008 and confirmed in recent press reports and the chart below is a source of major concern, not just because of its immediate contractionary effect but also because it calls into question the viability of a path to development that some say has lifted a billion people out of poverty.

Worse is still to come

The last quarter of 2008 may have been awful, but most commentators expect economic performance to deteriorate further during the first half of 2009. Given the bank bail-outs of last October and November have not restored lending to the private sector, firms are finding themselves under enormous pressure to conserve cash, reduce outlays, and inevitably this will push up unemployment. Those governments that can afford to do so - and it is worth remembering that many emerging market governments cannot - are effectively lending money to the private sector directly. All manner of bail-outs have been announced.



Leaving aside for the moment whether governments can continue to finance all these subsidies, concerns have been raised about the eligibility for and strings attached to this financial support and whether associated bailouts tend to discriminate against foreign firms. So concerned was the *Financial Times* about this matter that it has called for an international accord on state support for business during the downturn.⁷

The sheer scale of the fiscal stimuli and bail-outs being offered has also raised questions as to whether they will be voluntarily financed by private investors, even those governments with excellent credit ratings. On their current plans governments plan to issue over three trillion dollars in debt in 2009, three times the 2008 total.⁸ Nasty policy choices could arise should governments find their funding plans dashed because the alternative means for helping national firms tend to come at the expense of impoverishing others: deliberate currency devaluation, imposing tariff and non-tariff barriers, and resorting to the many loopholes in WTO agreements.

Even if financing isn't a problem, questions will arise inevitably as to whether the vast number of new government contracts are being deliberately funnelled away from foreign firms, including the subsidiaries of foreign firms. All this adds to the potential for some pretty unpleasant international trade disputes. Indeed, 2009 may well be the year when the apparent consensus in favour of open borders faces its greatest test. The temptation to turn inwards will surely be greater than at any time in the recent past.

Keeping borders open: some policy options

The fear that parochial concerns might trump long-standing commitments to open borders and the worrying parallels to the 1930s have motivated more and more analysts to warn not only of the perils of protectionism but also to call for international initiatives to stop the clock being turned back. Indeed, concerns about resurgent protectionism were mentioned in the communiqué of the G20 leaders at the November 2008 summit.

A number of collective measures were contained in an electronic book of contributions from over 15 leading trade analysts that Richard Baldwin and I edited and circulated last December.⁹ The reaction to that book and subsequent debate has identified a number of policy options worthy of consideration. Before enumerating those options, it may be worth reflecting on what the ultimate goal of any international initiative might

be that the G20 countries might undertake at their London summit this coming April.

Seeking to prevent any discrimination against international commerce will no doubt be appealing to some. But do more pragmatic considerations lead to different goals, such as limiting the form of protectionism imposed, limiting the conditions under which such measures are taken, or constraining the time they are in place? Or should the focus be on improving the transparency of government decision-making or assuring procedural safeguards? Should consultation mechanisms by trading partners be established and employed before any trade measures are imposed, as is the case in many free trade agreements? Figuring out the ends of any future G20 trade initiative will have considerable implications for the appropriate means.

The following six policy options, many of which are complementary with one another, are worthy of serious consideration.

1. Some have proposed that a surveillance mechanism be established to quickly identify any new discriminatory trade measures taken by governments, whether or not they are consistent with WTO accords. Given the lousy track record of governments reporting to the WTO the more sensitive aspects of their trade policies, questions arise as to which body or bodies have the capability to undertake this surveillance function. It may be the case, as some contend, that its current mandate allows the WTO could undertake this function,

but will it pull its punches? Whichever body undertakes this function needs to be tough enough to stand up to national governments and credible enough to be taken seriously by them.

2. Others have argued that governments' commitments to open borders could take the form of a collective pledge to a standstill on imposing certain, specified trade measures for the duration of the global economic downturn. Given the many forms that protectionism can take an immediate question arises as to what state measures will be restricted for the duration of the downturn. Plus, acceptability may require that any standstill be balanced across trading partners,¹⁰ that is, imposing a comparable degree of restraint on all major trading partners. This might involve developing countries committing not to raise their tariffs on manufactured goods while industrial countries commit not to expand payments to farmers. What constitutes "balance" and are their different formulas that assure "balance"? Plus, what legal form would any standstill take and how would it be enforced?

3. An initiative to limit the potential for discrimination in the application of financial support-or bailouts-from governments to firms has been mentioned before. To use European parlance could collective action to limit the use of state aids during the economic downturn be desirable, or indeed part of a standstill? What would this involve?

4. Bearing in mind that in many jurisdictions government procurement contracts are not that open to international competition, what steps can be taken to ensure that the large stimulus packages don't erode what little room there is for foreign bidders for state projects? Can the avowed desire of governments to move fast in implementing spending increases be reconciled with any practical measures on keep open state contracts to a modicum of competition? Is the case for such competition, on value for money grounds or bang-for-the-buck, greater during a downturn?

5. Taking steps to reduce the red tape that can bedevil international trade might offer another tangible way to demonstrate a commitment to open markets. In this regard some have argued that the well-advanced WTO negotiations on trade facilitation be completed and implemented immediately, with financial support provided to developing countries facing any roll-out difficulties. Since such a WTO accord will likely require more reforms by developing countries than by



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industrialized countries, should the latter take additional steps (such as accelerating the implementation of duty-free quota-free market access for the least developed countries) to equalize contributions to such an initiative?

6. Some have also argued that the best possible expression of the world's collective desire to retain and further open borders is to complete the Doha Round negotiations. Given the potential for substantial backsliding by both developing and industrialized countries, backsliding that is all the more tempting during a sharp recession; ironically the appeal of completing the Doha Round may have grown

as the downturn has worsened. But is it feasible - especially given the considerable bad blood and missed deadlines experience since this round of negotiations was launched in 2001? ■

Dr Evenett has published nine books and edited volumes, 25 academic articles and 40 book chapters. His research focuses on the factors determining the intensity of competition in emerging markets, on the effects of competition law and policy on firms' behaviour, and on the analysis of existing and proposed agreements at the World Trade Organization. His research is taught at dozens of universities around the world.

A version of the editorial was previously published on VoxEU.org

1. "Malaysia bans foreign hiring for factories, stores," Associated Press 22 January 2009

2. Suppliers to clothing trade in US fall by 70%," Financial Times, 10 December 2008; "Factory Evaluator Panjiva Readies Home Rankings," Home Textiles Today, 15 December 2008.

3. An initiative to limit the potential for discrimination in the application of financial support-or bailouts-from governments to firms has been mentioned before. To use European parlance could collective action to limit the use of state aids during the economic downturn be desirable, or indeed part of a standstill? What would this involve?

4. "Millions Face Job Losses in Asia," Asian News Desk, 22 December 2008.

5. "Millions Face Job Losses in Asia," Asian News Desk, 22 December 2008.

6. "Indian business warns on loss of 10m jobs," Financial Times, 7 January 2009.

7. "Not a time for a one-man band. A global financial crisis requires global co-operation," Financial Times, 22 January 2009.

8. "Confident tone as UK debt sale nears," Financial Times, 22 January 2009.

9. "What should leaders do to halt the spread of protectionism?" Available at <http://www.voxeu.org/index.php?q=node/2651>. Soon after the publication of this book Richard Baldwin and I offered some thoughts on "Restoring the G20's credibility on trade: Plan B and the WTO trade talks," which generated a number of comments, all of which are available at: <http://www.voxeu.org/index.php?q=node/2692>

10. See, in particular, the contents of a letter by the Indian Ambassador to the WTO in The Financial Times, "Standstill must avoid unequal burden on countries," 12 January 2009.

The Role of SWFs and the Santiago Principles

Thomas Ekel is an Investment Director with the Asset Management Department of the Norwegian Ministry of Finance, which is responsible for the management of the Norwegian sovereign wealth fund

Much has been written about Sovereign Wealth Funds (SWFs) over the past two years. What started out as alarmist cries about SWFs threatening national security and financial stability gradually transformed into a more nuanced discussion about their activities and effects. The recent drop in asset and commodity prices and economic downturn have even led some to question the significance of SWFs altogether. While the outlook for the size of these investment vehicles may be uncertain, they will nonetheless be important participants in the international monetary and financial system. A general insight into the framework and activities of SWFs, as well as the Santiago Principles that the funds endorsed in October 2008 (see box), therefore remains important.

A matter of trust

The more nuanced perception of SWFs that gradually developed through 2008 was partly aided by the efforts on the part of SWFs through the Santiago Principles to demonstrate that they are properly set up and that their investments are made on a financial basis. Such confidence building measures, combined with characteristics such as little leverage and a focus on long-term investment returns, helped support the fundamental recognition that sovereign investors and recipient countries alike have a common interest in a stable financial system, reducing protectionism and maintaining an open and stable investment climate.

The Santiago Principles cover three areas: (i) sound objectives and legal framework to facilitate the formulation of an appropriate investment strategy; (ii) a sound institutional and governance framework that separates the functions of the owner, governing body (bodies) and management to facilitate accountability and operational independence; and (iii) a clear investment and risk management framework to promote a disciplined investment process and sound investment operations.

While the government ownership of the assets gave rise to the SWF-label, it is worth remembering that these funds differ in some fundamental respects: age, institutional arrangements, fund design, assets under management, and investment philosophy to name just a few. Given the heterogeneity and the size of the group, as well as the technical complexity of the subject matter, the successful drafting of the Santiago Principles in a relatively short time frame was met with general recognition.

Who are they?

The Santiago Principles define SWFs as follows: special-purpose investment funds or arrangements that are owned by the general government and created for macroeconomic purposes to manage assets

to achieve financial objectives and where the investment strategies include investing in foreign financial assets. This means that the definition excludes foreign currency reserves held for balance of payments or monetary policy purposes, state-owned enterprises and pension funds. Typically, SWFs have been established by balance of payments surpluses, official foreign currency operations, privatization proceeds, fiscal surpluses and/or commodity exports.

Several SWFs have been undertaking cross-border investing for many years. In their home countries SWFs can have a key role in improving the management of public finances and achieve macroeconomic stability. They can also bring important diversity to financial markets through their ability in many circumstances to take a long-term view in their investments and ride out the business cycle - a characteristic that can be extremely beneficial during periods of financial turmoil.

Is there an after-life?

When the Santiago Principles were published, the SWFs recognized that it also would be useful to follow up on the work. By being able to review the principles and facilitate the dissemination, proper understanding, and implementation of the principles, SWFs could continue the confidence building measures and improve their asset management practices. By having a forum for exchange of views among themselves and with recipient countries one would be better able to achieve the objective of helping maintain a stable, global financial system and free flow of capital and investments. We may therefore hear more from SWFs in the times to come.

While the threat of protectionism aimed at SWFs that prompted the writing of the Santiago Principles may seem to have receded, the economic downturn can again change the climate. Furthermore, other challenges remain. In the same way that sovereign investors and recipient countries alike have a common interest in a stable financial system and an open and stable investment climate, the financial crisis has been a reminder that they also have a common interest in well-functioning markets and well-run companies. It would therefore seem sensible that SWFs as long-run investors with large pools of assets should support regulatory reform of the market place aimed at better regulation, not just more regulation or regulation disguised as protectionism. Similarly, SWFs would seem well placed to reiterate the fundamental corporate governance principle of aligning the interests of the administration with the long-term interests of the owners. Long-term investing has again become fashionable. Now it is important that reform efforts also embrace long-term value creation. ■

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The Santiago Principles

1. The legal framework for the SWF should be sound and support its effective operation and the achievement of its stated objective(s).
 - 1.1. The legal framework for the SWF should ensure legal soundness of the SWF and its transactions.
 - 1.2. The key features of the SWF's legal basis and structure, as well as the legal relationship between the SWF and other state bodies, should be publicly disclosed.
2. The policy purpose of the SWF should be clearly defined and publicly disclosed.
3. Where the SWF's activities have significant direct domestic macroeconomic implications, those activities should be closely coordinated with the domestic fiscal and monetary authorities, so as to ensure consistency with the overall macroeconomic policies.
4. There should be clear and publicly disclosed policies, rules, procedures, or arrangements in relation to the SWF's general approach to funding, withdrawal and spending operations.
 - 4.1. The source of SWF funding should be publicly disclosed.
 - 4.2. The general approach to withdrawals from the SWF and spending on behalf of the government should be publicly disclosed.
5. The relevant statistical data pertaining to the SWF should be reported on a timely basis to the owner, or as otherwise required, for inclusion where appropriate in macroeconomic data sets.
6. The governance framework for the SWF should be sound and establish a clear and effective division of roles and responsibilities facilitating accountability and operational independence in the management of the SWF to pursue its objectives.
7. The owner should set the objectives of the SWF, appoint the members of its governing body(ies) in accordance with clearly defined procedures, and exercise oversight over the SWF's operations.
8. The governing body(ies) should act in the best interests of the SWF and have a clear mandate, and adequate authority and competency to carry out its functions.
9. The operational management of the SWF should implement the SWF's strategies in an independent manner and in accordance with clearly defined responsibilities.
10. The accountability framework for the SWF's operations should be clearly defined in the relevant legislation, charter, other constitutive documents, or management agreement.
11. An annual report and accompanying financial statements on the SWF's operations and performance should be prepared in a timely fashion and in accordance with recognized international or national accounting standards in a consistent manner.
12. The SWF's operations and financial statements should be audited annually in accordance with recognized international or national auditing standards in a consistent manner.
13. Professional and ethical standards should be clearly defined and made known to the members of the SWF's governing body(ies), management, and staff.
14. Dealing with third parties for the purpose of the SWF's operational management should be based on economic and financial grounds, and follow clear rules and procedures.
15. SWF operations and activities in host countries should be conducted in compliance with all applicable regulatory and disclosure requirements of the countries in which they operate.
16. The governance framework and objectives, as well as the manner in which the SWF's management is operationally independent from the owner, should be publicly disclosed.
17. Relevant financial information regarding the SWF should be publicly disclosed to demonstrate its economic and financial orientation, so as to contribute to stability in international financial markets and enhance trust in recipient countries.
18. The SWF's investment policy should be clear and consistent with its defined objectives, risk tolerance, and investment strategy, as set by the owner or the governing body(ies), and be based on sound portfolio management principles.
 - 18.1. The investment policy should guide the SWF's financial risk exposures and the possible use of leverage.
 - 18.2. The investment policy should address the extent to which internal and/or external investment managers are used, the range of their activities and authority, and the process by which they are selected and their performance monitored.
 - 18.3. A description of the investment policy of the SWF should be publicly disclosed.
19. The SWF's investment decisions should aim to maximize risk-adjusted financial returns in a manner consistent with its investment policy, and based on economic and financial grounds.
 - 19.1. If investment decisions are subject to other than economic and financial considerations, these should be clearly set out in the investment policy and be publicly disclosed.
 - 19.2. The management of an SWF's assets should be consistent with what is generally accepted as sound asset management.
20. The SWF should not seek or take advantage of privileged information or inappropriate influence by the broader government in competing with private entities.
21. SWFs view shareholder ownership rights as a fundamental element of their equity investments' value. If an SWF chooses to exercise its ownership rights, it should do so in a manner that is consistent with its investment policy and protects the financial value of its investments. The SWF should publicly disclose its general approach to voting securities of listed entities, including the key factors guiding its exercise of ownership rights.
22. The SWF should have a framework that identifies, assesses, and manages the risks of its operations.
 - 22.1. The risk management framework should include reliable information and timely reporting systems, which should enable the adequate monitoring and management of relevant risks within acceptable parameters and levels, control and incentive mechanisms, codes of conduct, business continuity planning, and an independent audit function.
 - 22.2. The general approach to the SWF's risk management framework should be publicly disclosed.
23. The assets and investment performance (absolute and relative to benchmarks, if any) of the SWF should be measured and reported to the owner according to clearly defined principles or standards.
24. A process of regular review of the implementation of the GAPP should be engaged in by or on behalf of the SWF.

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Modern Portfolio Theory and the Myth of Diversification

Moorad Choudhry, Stuart Turner, Gino Landuyt and Khurram Butt are in the Treasury Team at Europe Arab Bank plc



The year 2008 was an *annus horribilis* for investors in financial markets. Not one investor was protected against the downfall in asset prices. Even the stars of the last decade, the wizards of Greenwich who promised investment portfolios to be immune against this correction by adding “portable alpha” to their portfolios, had to admit that there was no safe haven. Diversification across several different asset classes didn’t work either, since every major asset class appeared to be under attack.

What the credit crunch and recession has taught us was that diversification and the efficient portfolio theory is a myth. Those challenging the diversification principle are entering Nobel Prize territory and Professor Markowitz himself. The view we posit in this article is that a cornerstone of modern finance, the Modern Portfolio Theory (MPT), did not withstand the test during the market crisis of 2007-2008. If our view is correct then it places a large question mark beside the fee-driven business of the professional fund management industry. Because why would a less-sophisticated investor pay X% per annum in fees to a professional investment manager if that manager is not creating any value? Moreover, in a bear market it can be demonstrated that diversification to hedge or spread risk destroys rather than creates value, because it merely magnifies the existing risk exposure for no reward.

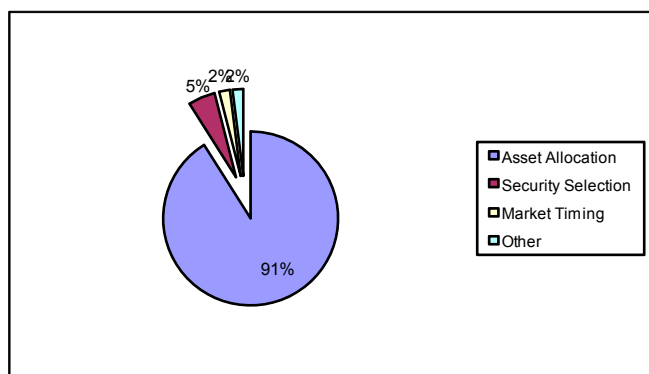
We begin the article with a summary introduction to the basics of MPT. We then consider the weaknesses inherent in the model as they appear, and link those weaknesses empirically to the current market environment. We conclude the paper with policy recommendations.

A summary introduction to MPT

Modern Portfolio Theory as formalised by HM Markowitz is based upon four major components, which we summarise below.

1. Investors are risk averse. Investors are more concerned with risk than with reward. Given the choice of two securities which offer the same return, the investor will choose the security which offers less risk. Therefore rational investors will not accept additional risk unless the level of return compensates them for this risk.
2. Security markets are efficient. The Efficient Market Hypothesis states that while the returns of different securities may vary as new information becomes available, these variations are inherently random and unpredictable. Assets are re-priced literally every second of the day according to what news is immediately available. As new information enters the market it is quickly reflected in the prices of securities, and thus temporary pricing discrepancies are extremely difficult, if not impossible, to exploit for profit. Advanced information dissemination technology and increased sophistication on the part of investors are causing the markets to become even more efficient, further complicating attempts to exploit price fluctuations arising from inefficient dissemination of information.

Figure 1. Determinants of portfolio performance



Source: Brinson, G, Hood, LP, G Beebower, “Determinants of Portfolio Performance”, *Financial Analysts Journal*, August 1986

3. Focus on the portfolio as a whole and not on individual securities. The risk and reward characteristics of all of the portfolio’s holdings should be analysed as one, not separately, with assumptions that equities offer higher returns than bonds, small-company equities offer higher returns than large-company equities and value equities offer greater returns than growth equities, all with their respective commensurate risk levels. An efficient allocation of capital to specific asset classes of equities and bonds is far more important than selecting the individual securities.

This is illustrated in Figure 1, reproduced from Brinson, Hood and Beebower (1986). As shown, asset allocation can determine over 90% of the performance variation of an investment portfolio. How one’s investment dollars are allocated far outweighs the potential effects of individual security selection and market timing.

4. Every risk level has a corresponding optimal combination of asset classes that maximises returns. Portfolio diversification is not so much a function of how many individual stocks or bonds are involved, but rather the lack of correlation of one asset to another. The higher a correlation between two investments, the more likely they are to move in the same direction. A portfolio of many different oil company stocks is highly correlated but poorly diversified. In this example, a disruption in oil supply will likely have a similar effect on all of these stocks. A portfolio of oil company stocks and alternative energy stocks is not as correlated and an oil supply disruption would probably have a different effect on oil company stocks than alternative energy company stocks. A higher lack of correlation equates to a greater level of diversification.

Figure 2. The efficient frontier



Source: Brinson, G, Hood, LP, G Beebower, “Determinants of Portfolio Performance”, *Financial Analysts Journal*, August 1986

The “efficient frontier” represents the range of hypothetical portfolios that offer the maximum return for any given level of risk. Portfolios positioned above the range are unachievable on a consistent basis; portfolios below the efficient frontier range are too risky based on the amount of reward offered and thus inefficient. The goal is to find the point along the efficient frontier which offers the maximum return at the risk level appropriate to an investor’s risk tolerance (see Figure 2).

The portfolio represented by point A in Figure 2 is inefficient because portfolios exist with the same value but less risk (Portfolio B) and portfolios with the same risk but more value (Portfolio C) as well as portfolios with a combination of these two conditions (Red Area). The Efficient Frontier, as originally defined in MPT, is a line that represents the continuum of all efficient portfolios relative to risk and value. (HM Markowitz, 1991)

The Efficient Market Hypothesis is at odds with traditional investment strategies. However, it has been supported by numerous academic studies, both theoretical and empirical. These studies show, among other things, that the risk-adjusted returns achieved by most professional investment managers are no better than those of the market as a whole, and many

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times inferior. This is primarily due to expenses and taxes incurred with active management. That's the bad news for active fund managers and investors.

The implications of the Efficient Market Hypothesis are profound for investors. In essence, we should be sceptical of anyone who claims to know how to "beat the market." One cannot expect to consistently beat the market by picking individual securities or by "timing the market".

Flaws in the model

The Markowitz paper on portfolio diversification, Sharpe's Capital Asset Pricing Model (CAPM) and the Modigliani-Miller theorem¹ were ground-breaking works and became the cornerstones of modern corporate finance. Modigliani-Miller was more a debate on the fundamental nature of debt versus equity. But all of them made similar assumptions to develop their model, which are (from WF Sharpe, 1964 and HM Markowitz, 1952):

- A. Volatility as a measure of risk
- B. Exclusion of correlation of 1.00
- C. No transaction costs
- D. Liquidity is infinite
- E. Investors act rationally
- F. Investors as a group look at risk-return relationships over the same time horizon
- G. Investors as a group have similar views on how they measure risk
- H. All assets can be bought and sold in the market
- I. Politics and investor psychology have no effect on the markets

Note that both papers were written during a time of extreme market stability. MPT was written in 1959, Modigliani-Miller's paper is spread over three articles in 1958, 1961 and 1963 and Sharp's paper was published in 1964. All the theories, MPT in particular, have been seen to have their merits in a bull market environment and this explains why they were so brilliant at the time. In the current market environment however the MPT model shows clearly weaknesses. This is best represented by the Dow Jones performance shown at Figure 3.

Figure 3. Dow Jones Index Annual Evolution: Dec 1959 – Dec 2008



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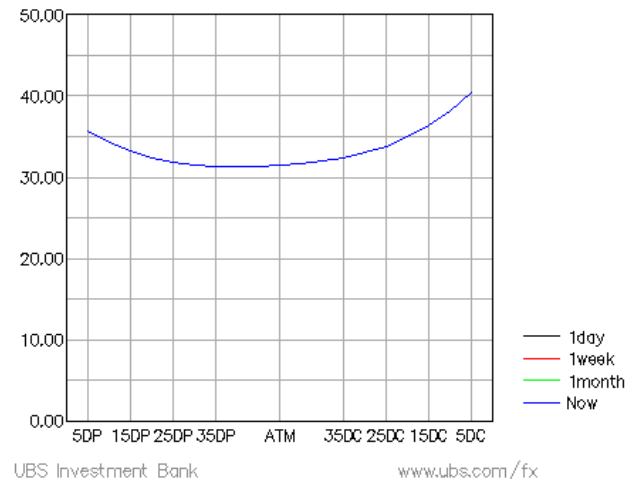
Both Markowitz and Sharp needed a proxy for risk and used volatility (in terms of standard deviation or *beta*) to define it. Consequently the assumption was made that the higher the volatility of an investment, the higher the risk. However, is volatility the right parameter for risk? Neither Markowitz nor Sharp did research on this matter. Probably this assumption was made building further on the Efficient Market Theory which in turn made the assumption that investors are risk-averse and act rationally. This assumption was accepted by the market without challenge.

We suggest that it is viable to argue that investors are more concerned about downside volatility than upward moves. The volatility approach in MPT and Sharpe's model values both of these equally. But such an approach is flawed in the current market environment. During the 1970s research was done on this matter, however a decade later Markowitz and Sharpe received Nobel Prizes for their work on portfolio theory and CAPM, having never reviewed their assumptions on risk.

We argue that high volatility does not give better results, and nor does lower volatility give poorer results. This thesis is supported by for example

Murphy (1977) who stated "realised returns appear to be higher than expected for low risk securities and lower than expected for high risk securities...or that the risk-reward relationship was far weaker than expected. Other important studies have concluded that there is not necessarily any stable relationship between risk and return, and that there often maybe virtually no relationship between return achieved and risk taken." (JM Murphy, 1977)

Figure 4. XAU/USD Volatility Smile



UBS Investment Bank

www.ubs.com/fx

Source: UBS. Used with permission

Another major problem in the volatility concept is the assumption that it is constant over time. Skewness of the volatility curve is completely ignored in the model although it is not ignored by option market makers. An option trader does not quote the same volatility every day, but rather adjusts prices to take volatility skew into account for in-/out- or at-the-money options.

Figure 4 shows the skew of the volatility of a 6-month option of XAU versus USD. One can clearly see that the volatility for Calls compared to Puts is higher and rises for far out-of-the money options. So the assumption of constant volatility is a fundamental weakness in the orthodox theory.

The major reasons why a volatility curve shows a smile are:

- Supply and demand amongst hedgers and speculators
- Directional view of the market
- Implied volatility usually goes up when the spot price moves
- Exotic options: market makers use OTM options to statically hedge exotic risk which means that they are unwilling to short OTM options

There is also empirical evidence of irrationality. A good example of the current irrational behaviour of investors is the price of certain holding stocks. At the time of writing (January 2009) some of these shares are trading at a lower price than the capitalized amount of cash these holdings have in their accounts. A good example is RHJ International, trading at a market cap of €311.39m but with over €500m in cash on account at its bankers. More such anomalies can be found in the credit and fixed income market; for example we note the high number of negative basis trade opportunities currently available for financial-sector companies. The credit crisis, which started in the summer of 2007, was triggered by the fall in confidence amongst investors for the US commercial paper (CP) and asset-backed CP (ABCP) markets. According to the academic theory of risk, this should not have been the case, as equities are considered to be a more risky investment than CP. It is outside the scope of this article to consider the irrationality of investors although there is recent literature on this subject. For instance Kahneman (2003) clearly supports the thesis that rational decision taking is often not feasible due to the restricted resources each individual has available to him.

Other assumptions behind MPT, such as infinite access to liquidity, have clearly been proved to be a misjudgement during the 2007-2008 crisis. On its own this one flawed assumption renders the theory unworkable. Other assumptions on the neutral impact of investor psychology and politics are also flawed given that these two factors do have an effect on the markets.

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Figure 5. Credit Suisse Tremont Hedge Fund Index performance 2008

	Currency	Index Value		Return		
		Dec 08	Nov 08	Dec 08	Nov 08	YTD
Credit Suisse/Tremont Hedge Fund Index	USD	351.08	351.2	-0.03%	-4.15%	-19.07%
Convertible Arbitrage	USD	221.62	223.82	-0.98%	-1.88%	-31.59%
Dedicated Short Bias	USD	88.94	90.46	-1.68%	3.04%	14.87%
Emerging Markets	USD	264.49	263.92	0.22%	-1.87%	-30.41%
Equity Market Neutral	USD	225.47	224.54	0.41%	-40.85%	-40.32%
Event Driven	USD	395.52	400.56	-1.26%	-3.21%	-17.74%
Distressed	USD	452.18	463.96	-2.54%	-5.00%	-20.48%
Multi-Strategy	USD	371.03	372.86	-0.49%	-2.17%	-16.25%
Risk Arbitrage	USD	277.63	273.26	1.60%	-0.02%	-3.27%
Fixed Income Arbitrage	USD	166.79	168.13	-0.80%	-5.60%	-28.82%
Gobal Macro	USD	582.69	576.3	1.11%	1.54%	-4.62%
Long/Short Equity	USD	401.98	397.78	1.06%	-1.41%	-19.76%
Managed Futures	USD	284.19	277.61	2.37%	3.22%	18.33%
Multi-Strategy	USD	275.79	280.04	-1.52%	-4.63%	-23.63%

Source: Credit Suisse /Tremont Hedge Funds Index

Empirical evidence

We suggested above that in the current environment investors have not acted rationally. That is, the current anomalies in the stock and fixed income markets, and also the concept of volatility, has given investors some false guidance.

An important element in Markowitz theory is the issue of correlation. In his paper he argues that the risk of a portfolio could be reduced and the expected rate of return increased when assets with dissimilar price movements are combined. Such diversification reduces risk only when assets are combined whose prices move inversely with each other. In other words the lower the correlation the better for the risk-reward profile on the efficient frontier.

If we look at the Credit Suisse Tremont Hedge Fund Index at Figure 5 we see that this is clearly not the case. All the strategies shown (except for dedicated shorts and managed futures) showed a negative performance for 2008. We can argue that both dedicated shorts and managed futures are pure directional plays, like betting in a casino, and anticipate a negative downturn, and so would always perform positive in the current environment. Such strategies cannot be said to represent the application of MPT.

The problem is that MPT and the diversification argument, like so many supposedly good investment ideas, only works in a bull market, when investors pay at least lip-service to "fundamentals" and apply some logic in share valuation (and even then they don't always; for example, the dot.com crash). In a bear market, or in any period of negative sentiment, all asset prices and markets go down. And in times of crises, as we have observed during 2007-08, correlation between asset classes is practically unity.

It does not matter what industry, country or level of managerial expertise is being considered, all prices go down and all credit spreads widen in a bear market such as the one we have observed now. In this crisis, everyone has lost money: banks, hedge funds, volatility traders, private equity, long-short investors, and traditional long-only fund managers have all registered losses².

More significantly if we look closer at the Credit Suisse Tremont Index we notice that even the "long-short" equity index is down in this period as well, by over 30%. This refutes the claim that these strategies generated "alpha".

On paper, diversification sounds like a great thing but where modern portfolio theory suffers the greatest weakness is in its assumption that in every market correlation is below 1.00. What we have observed over the last five years, whether it is managed on the basis of fundamental factors, momentum, arbitrage or any other rationale, is that everything tends

to end up on the same side of the trade at the same time. Believers in portfolio theory are convinced that (for instance) alternative investments are somehow negatively correlated with basic equities. During 2007-08 they have learnt the hard way that this is simply not true. Bonds, equities, commodities and currencies aren't asset classes in their own right.

The same argument applies to banks that diversified by branching out and operating globally. The rationale was that moving into different geographical regions spread and diversified risk. In fact all this did was magnify risk across economies so that when the credit crunch came it hit them everywhere. While the ultimate global bank, HSBC, appears to have weathered the storm fairly well, possibly due more to its vast size than its geographical dispersion, some of the largest losses, in relative terms, have been registered at global players such as Citibank, RBS and UBS.

Only a small minority of fund managers ever outperforms the index or benchmark. Given that they charge a fee to their clients, those that fail to do so are failing to create value. Most investors would be better off simply tracking their benchmark index. We believe diversification only ever applies in a bull market. In a bear market, all prices go down and correlation is effectively unity. Recognising this, the justification for charging fund management fees disappears. To continue to market an ability to generate alpha, to claim that one can outperform the market over anything other than the very short-term, has a touch of charlatanism about it.

Summary and conclusions

The Markowitz Modern Portfolio Theory clearly had its merits over the last 30-35 years. It was the basis for an investment and banking model that generated significant returns from the 1980s onwards. However in a severe bear market the model has clearly been seen to be flawed, and contributed to the development of a banking business model that suffered large losses. The assumptions on which it is based clearly prove that a paradigm shift in economics needs to take place that modifies or completely replaces MPT.

Portfolio diversification only makes sense if one has the possibility to pick out assets which are uncorrelated. Unfortunately in a severe recessionary environment correlation tends to go to one among every asset class, so this is a non-starter for anything other than a very short term (less than five year) investment horizon.

In this respect the fund management industry will need to restructure its operating model and also review performance fees, since we can see that in a bear market it cannot add value to portfolios. Adding "alpha" to a portfolio in this type of market is a myth. Showing positive returns in a bear market is just a matter of shorting the markets, which is a directional play and has nothing to do with MPT or diversification.



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Our suggestion is that the paradigm shift in financial economics should be a reversion to “traditional” markets. Not only does diversifying across asset classes and geographical regions not spread risk, we have seen how in a bear market it amplifies risk. The clear lesson from the crisis is to “know one’s risk”, and that is best served by concentrating on assets and sectors that one is familiar with. Diversifying in the name of the MPT will only erode value.

Our policy recommendations are:

- Restructure the business model to concentrate assets and regions for

which one has genuine understanding and expertise;

- Secure liquidity to allow for times of market corrections and illiquidity. To this end we further recommend ensuring a maximum of only 20% of funding requirement in less than the one-month maturity, and avoiding over-leveraging on the capital base over fifteen times.

A paradigm shift that results in a greater concentration on familiarity and an acceptance of lower average returns will do much to prevent largescale losses at the time of the next market correction. ■

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1. To quote: “With well-functioning markets (and neutral taxes) and rational investors, who can ‘undo’ the corporate financial structure by holding positive or negative amounts of debt, the market value of the firm – debt plus equity – depends only on the income stream generated by its assets. It follows, in particular, that the value of the firm should not be affected by the share of debt in its financial structure or by what will be done with the returns – paid out as dividends or reinvested (profitably)”; Modigliani and Miller (1958).

2. An investor who held only risk-free sovereign securities such as Treasuries, Gilts and Bunds would not have lost money. But if this was done for risk-averse reasons then it is not actually a “strategy” as such, merely the base risk-free option. If it was done as a directional play on interest rates, again this is not a value-added fund management strategy but rather the tactics of the casino. Either way, the fact that investors in risk-free sovereign securities made money reinforces our argument.

Don’t Panic! Banks Have Always Failed...

Dr Adrian R Bell, Professor Chris Brooks and Dr Tony Moore of the ICMA Centre, University of Reading

This article will highlight an episode from medieval Europe that has many parallels with today’s financial situation¹. The financial crisis of 1294 featured sub-prime borrowers, liquidity disappearing, recriminations, the seizure of foreign owned assets and runs on the bank. While the study of history cannot provide us with a toolkit of how to fix the current seizure in bank lending, by identifying some common elements in both crises, we can place current events in a wider perspective that may assist today’s market commentators and policymakers in forming their own views.

Medieval credit

Our study centres on the relationship between the English king, Edward I (1272-1307), and an Italian merchant society, the Ricciardi of Lucca. Between 1275 and 1294, the Ricciardi and Edward entered into a sophisticated financial relationship that could be compared to a modern current account incorporating extensive overdraft facilities. The Ricciardi managed certain sources of royal income; most notably the customs on wool exports but also the periodic taxes on property granted to the king by parliament and other extraordinary income. In return, the Ricciardi would disburse payments on the king’s behalf as and when required. These payments would be made in part from the monies collected by the Ricciardi, but also from their own resources and from loans advanced by other merchant societies brokered by the Ricciardi.

This relationship had great advantages for the king. It allowed Edward to anticipate his income and to smooth the seasonal fluctuations in royal revenues. Perhaps more importantly, the Ricciardi extended credit to Edward (the overdraft), allowing him to respond to unexpected events or undertake expensive projects without having to maintain a large cash reserve. The conquest of Wales, for example, was largely funded by the Ricciardi. Surviving accounts for this period show that the royal overdraft generally stood at around £20,000, although this includes an element of interest and ‘bank fees’. Although the payment of interest is disguised in the sources because of religious disapproval of usury, it has been possible to calculate some figures and these suggest that the king was able to borrow from the Ricciardi (or from other merchant societies via the Ricciardi) at between 10-15% per annum.²

The merchants also benefitted from this relationship. It is clear that they received some form of financial compensation, as described above.



L-R: Dr Tony Moore, Professor Chris Brooks, Dr Adrian Bell

Furthermore, the Ricciardi could benefit from royal favour in their business dealings. For instance, they were allowed to sue their debtors before the king’s own exchequer court. Perhaps most significantly, the Ricciardi were able to build on their relationship with the king to expand their share of the profitable wool export market. Many merchants sought to secure their supplies of wool by entering into advance contracts for wool with producers, most notably the great religious houses. During their time as royal bankers, between the years 1272–1294, the Ricciardi were counterparties in almost half of all wool forward contracts.³

Looking at the wider economic background, such financial dealings were made possible because the 1270s and 1280s were a period of abundant liquidity. Just as Western banks, at least until recently, benefitted from the ‘Asian savings glut’, the Ricciardi and other Italian merchant societies managed large sums of papal taxation, collected in England and across Europe in support of a proposed crusade. In 1292, the Ricciardi took over 100,000 marks (£66,666) of papal taxation granted to Edward by the pope. Like modern banks, the merchant societies would have used this opportunity to make profits by loaning this money at interest or by investing in trade. Figure 1 shows the position of the merchant at the centre of a pan-European network of trade and credit:

Although this meant that, at any one time, most of their own capital was committed in various ventures, both modern bankers now and the Ricciardi then could look to other banks or merchant societies respectively for short-term injections of liquidity. The current ‘credit crunch’ arguably started with the ‘sub-prime crisis’ in the US, as a result of which banks were unwilling to lend to each other, thus removing liquidity from the market. In the early 1290s, there was a similar process as the pope called in much of his funds deposited with the merchant societies, and then the French king levied a heavy tax on the Italians in France. This had the effect of sucking liquidity out of the system, leaving the Ricciardi particularly vulnerable should Edward seek to make a large withdrawal at short notice.

The ‘credit crunch’

Unfortunately, this was precisely the situation that arose in 1294, when war broke out between England and France. Although the Ricciardi should have been well-capitalised at that time, it seems that much of this was tied up and they found themselves needing to find a very large sum of money

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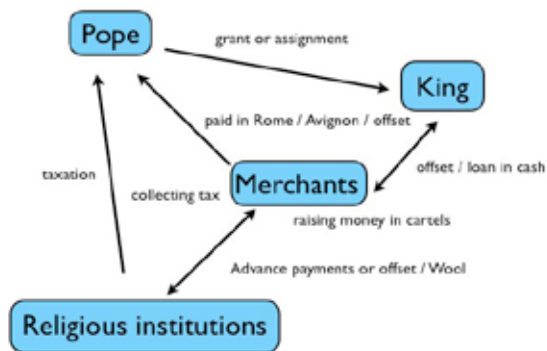


Figure 1 – The merchant as money manager

very quickly to meet Edward's demands for money to fund his armies.

Previously, the Ricciardi would have looked to their fellow merchant societies for short-term loans to buy time for them to realise their own assets. However, the other merchant societies were also affected by the wider lack of liquidity and seem to have been unable or unwilling to advance the necessary sums. These difficulties were compounded by the Anglo-French war, which effectively cut communications between Italy and England. Unable to update the account books of their various branches across Europe, the Ricciardi and their fellow merchants could not manage their money effectively. The following quotes from the Ricciardi's internal letters may sound familiar:

"everyone to whom we owed money ran to us and wanted to be paid, and because of this we were held very tight everywhere";

"it seems that money has disappeared";

"we used to have credit and could borrow 100,000 and 200,000 livres tournois (£25,000-50,000 sterling) and even more, we are now reduced to such a point that if we wanted 100 livres tournois (£25 sterling) we could not find them";

"we do not find anyone willing to give us credit of even £10 of Lucca".⁴

Overall, the Ricciardi, like some banks today, argued that their difficulties were merely a short-term mismatch and that their assets matched their liabilities. Unfortunately, owing to the uncertainty caused by the conflict between England and France, the Ricciardi were unable to collect on debts owed to them while their own creditors sought to withdraw sums deposited with or loaned to the Ricciardi. As a result, they were unable to provide the English king with the financial support that he desperately needed. In response, Edward removed the Ricciardi from their position as collectors of the customs on wool and, in an attempt to recover some of his losses, ordered the seizure of the assets (mainly wool but also debts owed to the merchants by private individuals) held by the Ricciardi and other merchant societies. This dealt a major blow to their finances and marked the end of the long-standing relationship between the Ricciardi and the English crown.

Lessons from 1294?

From the bankers' perspective, the Ricciardi sought to recover their position by a series of 'credit swaps' and netting between their creditors and debtors. They sought a new accounting with Edward in the belief that his 'overdraft', combined with money that they had lent to the king's brother and the proceeds of the wool and debts seized by the king, would offset the bulk of the papal taxation that they owed him. Their other main creditor was the pope, and the Ricciardi sought to persuade him to take over the debts owed to them in France and in Italy, which the Ricciardi themselves were unable to collect, but which the pope, with his political and religious authority, could call in. In some ways, this is similar to the concern of modern banks to reduce their liabilities and perhaps to the intervention of governments to exchange Treasury-backed bonds for more difficult to collect assets held by the banks. Unfortunately for the Ricciardi, they were unable to convince either Edward or the pope to support them, and the society eventually folded.

From the perspective of the English government, in the short-term, Edward had dealt with the Ricciardi decisively and, as a result, he was able to recover a small part of the papal taxation promised to him. However, the fall of the Ricciardi had significant costs in the medium-term, since Edward still needed to raise huge sums of money to pay for his armies,

now fighting in Gascony, Scotland and Wales, as well as the subsidies that he had promised to his allies in the Low Countries and Germany. As a result, Edward was forced to turn to moneylenders who both lacked the resources of the Italians and charged much higher rates of interest (40%-80% per annum). He also found it necessary to impose unprecedentedly heavy taxation on England, ultimately precipitating a baronial rebellion in 1297. Moreover, much of Edward's expenditure was met in the form of wardrobe bills, effectively government IOUs, and as much as £200,000-worth of these may have been outstanding in 1307.

Applying this argument to the current crisis, it is clear that taking punitive action against the banks today would further reduce access to credit and, given the greater reliance of the modern economy on credit, this would have much more serious consequences for the country as a whole. Edward himself may subsequently have come to the same conclusion. By 1299, he had entered into another long-term financial relationship with an Italian merchant society, in this case the Frescobaldi of Florence. In 1302, the Frescobaldi wrote to Edward (see Figure 2), complaining that:

"...they are damaged in that owing to the aforesaid advance that they have made you, they have not been credited by other merchants, nor have they been able to carry on trade in the time aforesaid, and were obliged to deliver back 200,000 gold florins (roughly equivalent to £33,333 sterling) that they had in deposit from honest men, of which the damage is so great that they dare not write it".⁵

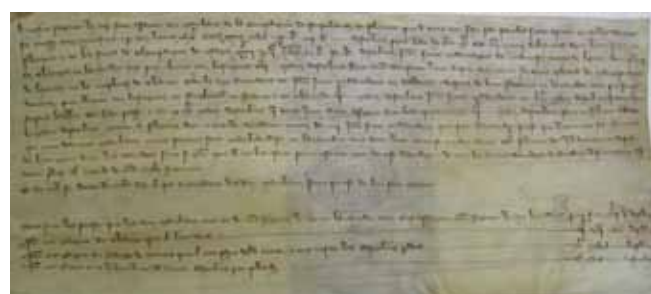


Figure 2 – Letter of the Frescobaldi to Edward I (c.1301-2) – (TNA SC 1/47 no.120, Crown Copyright)

In contrast to his treatment of the Ricciardi, Edward recognized the justice of the Frescobaldi's claim and promised them £10,000 in compensation. Although far smaller in absolute terms, in comparison to annual government income of about £40-50,000, this commitment is relatively greater than the initial £50 billion recapitalisation promised to the banks by the British government in 2008. It suggests that Edward recognised that his initial hard-line policy towards the Ricciardi had in fact proved counter-productive.

There was an alternative policy. Edward's opponent, Philip the Fair of France, sought to fund his armies by debasing/devaluing the French currency. He ordered repeated recoinages throughout the 1290s, in each of which the silver content of the coinage was reduced, possibly by as much as two-thirds in total. As a result, the pound sterling and the gold florin both gained between 50% and 100% in value against the livre tournois. The income (seigniorage) gained from these recoinages paid for much of the cost of the war and meant that the French king did not have to resort to direct taxation to the same extent as his English counterpart or incur the same level of debt. It is likely, however, that the long-term consequences for the French economy of the weakening of the currency were more damaging than the medium-term pain of high taxation and debt in England. This issue will surely have considerable modern resonance as governments begin to grapple with the problem of how to pay for the obligations that they are currently undertaking. ■

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The Climate Principles - Tackling the Challenge of Climate Change

Financial institutions that spend the green dollar are key to crisis recovery, argues Emily Farnworth of The Climate Group

Type 'Green Dollar Bill' into Google and the first link that bounces back is a Wiki answer to a slightly ironic question – why is the dollar bill green? One theory put forward is that bureaucrats of the day thought green would best represent the strong and stable credit of the US government.

How times have changed.

Once the heart of the global economy, a build up of toxic lending by US banks has led to cardiac arrest. The financial blood stream that inextricably links global economies to local businesses was invisible until it failed. Billions of dollars are being pumped in to resuscitate and the need for a lifestyle change is starting to come into focus.

But the recovery will be under the shadow of an even greater threat to our survival. The climate crunch is looming and requires a change now to avoid harm to both our physical and fiscal environments. The International Panel on Climate Change (IPCC) has recommended that developed countries reduce their greenhouse gas emissions by 25-40% (on 1990 levels) by 2020 and by 80-90% by 2050 in order to avoid dangerous climate change.

To meet these targets, the finance industry has an intrinsic role to play in delivering money to flourishing green industries whilst supporting the exchange of carbon credits on global carbon markets.

In December 2008, five of the world's largest and most successful financial institutions launched *The Climate Principles* to outline exactly what this means for the sector. Credit Agricole, HSBC, Munich Re, Standard Chartered and Swiss Re worked with over twenty global financial institutions to develop a document that is somewhat equivalent to the finance sector's five point plan for a low carbon lifestyle.

The Climate Principles address every part of the finance sector's broad remit, making them relevant to anything a financial institution is doing, anywhere in the world. They go far beyond addressing operational carbon emissions or investment in low carbon technology – they are about incorporating an analysis of the risks and opportunities of climate change into everything a financial institution does. And as part of their commitment to reducing their climate impacts, adopting institutions must educate their business clients and consumers, develop products and services that enable them to make the best choices, be transparent about the decisions they make and publicly disclose their progress.

So the finance industry is beginning to understand and deliver on its role in preventing dangerous climate change.

Thus far insurers have borne the brunt of increased extreme weather events – hurricanes, flooding, drought all cause damage that costs money to repair. In huge sums.

Swiss Re is one of the world's leading re-insurance companies with a keen focus on the costs that a changing climate will bring. The financial impact of severe weather events is the most obvious area for scrutiny but they also recognise a change in temperatures around the world will influence the spread of pests and disease which then impacts on health and life expectancy. There is also a need to dispel the misconception that climate change is just about global warming. Due to the complex role the oceans play in determining weather patterns, winters in Europe are likely to be colder and more severe. The Swiss Federal Institute of Technology (ETHZ) in cooperation with Swiss Re indicate that more frequent and severe storms in Europe will mean average annual losses can be expected to increase from 16 to 68% by the end of the century. For a global reinsurance company, this means continuously updating underwriting and risk management approaches to minimise financial losses.

Investment in renewable energy is another area that the finance sector has been quick to develop. Public offerings, mergers and acquisitions all require the involvement of private sector finance and the size of these deals are now comparable with other mainstream business areas. For

example, Iberdrola Renovables completed the world's fourth largest IPO of 2007 raising USD \$6.6 billion. It significantly boosted the total funds raised by the low carbon energy sector on the public markets in 2007 to around 17%. Scottish and Southern Energy (SSE) quickly followed Iberdrola and moved ahead with the acquisition of renewable firm Airtricity for €1.8 billion (USD \$2.6 billion) increasing SSE's renewable energy generation portfolio by 400 MW of wind in operation, another 200 MW in construction and a 10,000 MW global pipeline of wind projects in various stages of development.

Views on the potential growth of renewables may continue to differ and while the sector is repeatedly beating all forecasts, the challenge is certainly not for the faint-hearted due to the scale of investment and development needed.

Investment in clean energy is only a small piece of the overall investment opportunity. Consultants McKinsey & Co recently published version 2 of their Global Greenhouse Gas Abatement Cost Curve which gives a picture of CO₂ and cost savings versus the investment required for 200 climate change solutions, across ten sectors and twenty-one regions, between now and 2030. They conclude that the technical potential exists globally to reduce greenhouse gas emissions by 70% by 2030, keeping us relatively healthy according to the IPCC.

But let's talk costs.

“...the finance industry is beginning to understand and deliver on its role in preventing dangerous climate change”

The additional investments that would be required amount to \$690 billion (€530 billion) in 2020 and over a trillion dollars (€810 billion) in 2030, which is only around 5-6% of the total expected investment in global fixed assets each year. Costs are potentially less than 1% of global GDP (\$260/€200

- \$390/€300 billion annually by 2030, compared to global GDP in 2030 of about \$80/€60 trillion).

So, our high-carbon diet is a big problem but we still have the time and potential to change habits of a lifetime, we can afford it, and what's more, there is profit to be made in solving it.

In September 2007, HSBC launched their *Global Climate Change Index*. This is the first, fully tradeable index tracking 300 companies worldwide who make money from fighting climate change.

Benchmark Index new composition as of September 2008

Description	No. of stocks	Wtg. (%)
Low Carbon Energy Production	207	61.35
Bio-energy	31	2.75
Diversified renewable	17	2.34
Gas	3	2.03
Hydro/geothermal/marine	13	1.37
Integrated power	46	26.31
Nuclear	25	13.03
Solar	48	8.46
Wind	24	5.06
Energy efficiency & management	109	26.80
Buildings efficiency	23	4.09
Energy storage	11	0.92
Fuel cells	12	0.80
Industrial efficiency	41	14.67
Transport efficiency	22	6.32
Water, waste & pollution control	70	11.63
Pollution control	3	0.22
Waste	21	4.06
Water	46	7.35
Financials	4	0.22
Carbon trading	2	0.14
Investment company	2	0.08
Total	390	100

Based on data as of 05 September 2008

Source: HSBC

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Opening of the Sinan solar power plant, Korea © Standard Chartered Bank

At the time of launch, the *Financial Times* reported that the 300 companies in the index had sharply outperformed other stocks in a clear sign of the growing demand from investors for securities that fight global warming. They also reported that since January 2004, the 300 companies in the index had produced nearly twice the profits or returns of other stocks. Kevin Bourne, global head of equities execution at HSBC commented, "We have produced this index because there is investor demand for it and we want to make money from it. People want a good guide to how these stocks are performing".

One year on and HSBC believe that the green investment agenda has "deepened and broadened". The latest composition of the index, as of September 2008, shows that high fuel prices have convinced many of the virtues of energy efficiency, whilst investment in low carbon energy production is the most attractive.

One country determined to detox is China. Now the largest emitter of carbon dioxide in the world, China has quietly embarked on a calculated low carbon plan. The Chinese government has set its country the most ambitious targets in the world and it is ahead of schedule in reaching these goals. All this without giving up its day job as the factory of the world.

So what are the vital statistics? China is number one producer of renewable energy (*Renewables 2007 Global Status Report*). China is the second for absolute dollar amount invested in renewable energy in 2007 (over \$12 billion). China is the second largest manufacturer of solar PV, behind Japan (1% of market share in 2003 has risen to 18% in 2007). And China is set to become world number one manufacturer of wind turbines by 2009 (Global Wind Energy Council).

As leading financiers in the largest photovoltaic (PV) solar power plant in Asia, Standard Chartered bank is already cashing in on low carbon growth in South Korea. Just like the Chinese government, the Koreans are also incentivising renewable energy, passing regulations to aid the growth of wind and solar capacity. Standard Chartered has now made a

commitment to finance \$8-10 billion of renewable and clean technology projects by 2012.

Asia is showing the strongest growth rates in low carbon industries, creating jobs and generating profits in the process. Something Obama is keen to replicate in the US.

In January, the House introduced an \$825 billion package, with about \$550 billion in new government spending and \$275 billion in new tax cuts. To get started towards Obama's goal of creating five million new "green-collar" jobs over the next 10 years, \$54 billion of this new spending will go to promote the production of renewable energy, modernise the electricity grid and increase energy efficiency in government buildings and homes. These kinds of projects fall into what Mark Fulton of Deutsche Bank calls the "green sweet spot," because they address climate change, increase energy security and create jobs.

During his campaign, Obama promised to break the country's past energy policies and addiction to foreign oil. Alongside the economic stimulus package, Obama is likely to champion a comprehensive energy policy and a national cap and trade programme.

The first dollar bill was issued in 1862 as the industrial revolution began. Momentum is now building for green revolution and a prosperous low carbon economy. Perhaps financial institutions and governments globally would do well to return to the founding psychology of their 'green dollar bills' for inspiration. Making them readily available for green investment could ensure the future strong and stable credit of the world. ■

To find out more about *The Climate Principles* visit www.theclimateprinciples.org or email principles@theclimategroup.org

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Preview of the Fifth Global Congress on Combating Counterfeiting & Piracy

Cancun, Mexico 2-4 June 2009

Bridging Boundaries For Shared Solutions



Ronald K Noble, Secretary General of INTERPOL, addressing the 4th Global Congress on Combating Counterfeiting and Piracy in Dubai

THE GLOBAL TRADE PLATFORM

We Make Life Authentic

Instant Authentication On-line



THE ONLY WAY TO COMBAT COUNTERFEITING IS TO UNDERMINE ITS ECONOMICS

HOW? – By refusing to buy fake produce.
HOW? – By being able to tell an original from a fake.
HOW? – By using the DINTAG System offering
instant naked-eye authentication to anyone
who cares: brand owner, end-consumer,
law enforcer.

USE DINTAG – SAY NO TO FAKES!

Bridging Boundaries For Shared Solutions



Joseph Clark is the Executive Director of the Global Congress Secretariat

The Global Congress on Combating Counterfeiting and Piracy is a unique public-private partnership based on a mutual commitment and a recognition that the public sector and private sector must work together to find solutions to this growing global problem.

The Fifth Global Congress on combating Counterfeiting and Piracy will be held in Cancun, Mexico 2-4 June 2009.

Background on the Congress

The Global Congress on Combating Counterfeiting and Piracy represents a unique, international public private sector partnership that is united in its efforts to identify solutions and facilitate their implementation against the growing menace of the illegal trade in counterfeiting and piracy.

In 2003, the need to address the rapidly growing global problem of counterfeiting and piracy had emerged as a key priority for national governments and intergovernmental organizations concerned about the myriad adverse costs to social welfare and economic development that were resulting from the rampant theft of intellectual property. Notably, trade in counterfeit goods was rising dramatically worldwide and had spread to almost every conceivable type of product. Billions of dollars in revenues were being lost to the black economy. Counterfeit drugs were putting lives at risk. And there was growing evidence that transnational organized crime networks were using profits from trade in counterfeit and pirated goods to fund their activities.

It was clear that better strategies – based on more effective cooperation between stakeholders at national and international level – were needed to combat the multiple threats posed by this damaging trade. To this end, the first Congress was convened by the World Customs Organization (WCO) and INTERPOL with the support of the World Intellectual Property Organisation (WIPO).

A Global Congress Steering Group was formed after the First Global Congress hosted by the World Customs Organization (WCO) at its headquarters in Brussels in May 2004. The Steering Group is chaired, on a rotating basis, by INTERPOL, the World Customs Organization and the World Intellectual Property Organization. The private sector is represented on the Steering Group by the International Chamber of Commerce (ICC) through its BASCAP initiative, the International Trademark Association (INTA) and the International Security Management Association (ISMA).

INTERPOL, the WCO and WIPO are the key international inter-governmental organizations involved in the fight against counterfeiting and piracy, and their views and voice on the issue with their member states and world governments is critical to finding and implementing solutions. The ICC, INTA, and ISMA are global business organizations actively engaged in the fight against counterfeiting and piracy. All three embody the principle that business and governments must work together to achieve more effective protection of intellectual property.

The key focus areas of the Steering Group are as follows:

1. Raise awareness on the problems associated with counterfeiting and piracy
2. Promote better legislation and enforcement
3. Enhance cooperation and coordination
4. Build capacity
5. Promote solutions, particularly in the key focus area of health and safety risks related to counterfeit products

To date, the Steering Group has convened four Global Congresses and four Regional Congresses that have brought together global political and business leaders and experts from law enforcement, the judiciary, academia and the private sector to share strategies, program concepts and identify priorities for action. An "outcomes statement", capturing the recommendations and suggestions, has been produced following each of the eight Congresses.

The Global Congress has become the premier international forum for shaping practical strategies to combat counterfeiting and piracy as evidenced by the prestigious speakers and growing numbers of delegates attending each successive Congress. Both the Third Global Congress (Geneva, January 2007), and the Fourth Global Congress (February 2008) were attended by over 1,000 people representing about 100 countries from around the world.

A look forward – The Fifth Global Congress on Combating Counterfeiting and Piracy

The Fifth Global Congress will be held in Cancun, Mexico on 2-4 June 2009, the first time a Global Congress will be staged in the Americas. It is being hosted by INTERPOL and the Mexican Government agency Instituto Mexicano de la Propiedad Industrial (IMPI).

The Fifth Global Congress will build on the successes of the first four Global Congresses. It will be focussed on developing tangible solutions to the current challenges in fighting counterfeiting and piracy globally, and will include special sessions devoted to the increasing problems in Mexico, Central and South America.

A look back – The Fourth Global Congress on Combating Counterfeiting and Piracy

The Fourth Global Congress was held in Dubai, UAE 3-5 February 2008. Hosted by Dubai Customs, the Congress was convened by the WCO, INTERPOL and the World WIPO in partnership with the International Chamber of Commerce (ICC), the International Trademark Association (INTA), and the International Security Management Association (ISMA).

Underscoring the importance of counterfeiting and piracy, both globally and across the Gulf region, the Congress was held under the patronage of His Highness Sheikh Mohammed bin Rashid Al Maktoum, Vice President and Prime Minister of the United Arab Emirates and Ruler of Dubai.

The Congress attracted over 1,200 delegates representing 90 countries from around the world. Notably, roughly one-third of the participants represented companies and organizations from Dubai and the GCC region.

Heads of international organizations and government leaders, senior representatives of customs and police, business executives and experts from around the world shared their experiences and identified concrete actions and solutions to more effectively combat counterfeiting and piracy.

The Fourth Global Congress was organized around five themes that consistently have emerged as the key focus areas for concrete actions to combat counterfeiting and piracy. In addition, the Fourth Global Congress also featured special sessions on the challenges facing free trade zones and transshipment countries, and counterfeiting and piracy over the internet.

In the course of the presentations and discussions, a number of dynamic suggestions and proposals were made on how the various stakeholders might more effectively combat counterfeiting and piracy. These suggestions and proposals were prioritized and incorporated into the following Recommendations for Action.

Fourth Global Congress Recommendations for Action

I. Cooperation and coordination

Not surprisingly, Congress participants once again reaffirmed that the global problems of counterfeiting and piracy are too great to be solved by individual governments, enforcement authorities, business sectors or companies. While some progress has been made, and there are an increasing number of achievements, the consensus was that more can, and should be done to improve cooperation and coordination among and between government authorities and the private sector.

Key recommendations:

1. Customs and police authorities, and where appropriate, the private sector, should participate more fully in developing and using existing tools to collect and share information including:

WCO Customs Enforcement Network (CEN)
INTERPOL Database on International Intellectual Property (DIIP) Crime

2. Companies are encouraged to adopt INTERPOL's Minimum Global Standard for the Collection of Information on Counterfeiting and Piracy in order that the information can be readily assimilated into INTERPOL's database and thus improve its operational capabilities against organized criminal networks.

3. The private sector should make better use of cross-industry anti-counterfeiting-related associations to improve cooperation among all stakeholders and with service provider organizations.

4. WCO, WIPO, INTERPOL and private sector stakeholders should convene a forum to identify a process for accelerating the integration of multi-disciplinary IP crime-related training to reduce redundancies, improve efficient use of resources and more fully leverage the collective strength of the organizations represented on the Global Congress Steering Group partnership or which are involved in training activities.

5. Led by members of the Global Congress Steering Group, all organizations involved in the fight against counterfeiting and piracy need to significantly enhance the timely exchange of information. It was noted that more information is needed on the business practices of counterfeiters and pirates and how to exploit their weaknesses.

6. National and international enforcement organizations should take the lead in identifying effective ways for the private sector to create support and determination from policy makers to take the needed actions to stop counterfeit products including, in particular, those that threaten the health and safety of consumers.

7. Dubai Customs is encouraged to follow-through on its offer of support to other Customs administrations in the GCC Countries and Arab world to share experience and knowledge.

II. Legislation and enforcement

Speakers and delegates called on governments to further improve legislation dealing with the enforcement of IP rights, streamline procedures and implement already existing international obligations. They also recommended that a new set of standards be developed at the national and regional levels with the aim of making available more effective civil and criminal remedies and border measures. There was broad acknowledgment that even if good laws are in place, they are often poorly enforced. In order to update national and regional IP protection regimes and to make the enforcement of intellectual property rights more efficient, decision-makers in the public and private sectors need to be made aware of the requirement to allocate additional human and financial resources.

Key recommendations:

1. All participants should use their influence and resources to encourage national governments to regularly update civil, criminal and border measures legislation taking into account new international and regional standards or to implement recent decisions by the national authorities on more effective intellectual property protection and enforcement.

2. Members of the Global Congress Steering Group partnership should work within their organizations, with each other and with other interested parties to encourage international governmental organizations and national governments to develop a holistic strategy on the negotiation and revision of international conventions and treaties related to counterfeiting and piracy. This will help to ensure that agreements at the international level such as the Palermo Convention (fighting organized crime), and the WHO IMPACT Initiative (preventing the distribution of counterfeit medical products) are complementary. The strategy must also take into account the project work of the G8 and initiatives aiming at higher standards in the field of IP enforcement such

as the WCO SECURE Initiative, and preparations for the conclusion of an Anti-Counterfeiting Trade Agreement (ACTA).

3. WIPO, ICC/BASCAP, INTA, national brand protection groups and IPR organizations should continue and increase their efforts to educate government leaders and the public on the value of intellectual property in economic development and the attendant need to introduce and maintain control measures to reduce counterfeiting and piracy. This balance is a crucial pre-condition for controlling the expected sharp rise in counterfeit and pirated goods.

4. Members of the Steering Group and other committed organizations and companies should work with WHO to identify the best ways to encourage implementation of the "Principles for National Legislation against Counterfeit Medical Products," adopted by the International Medical Products Anti-Counterfeiting Taskforce (IMPACT) in December 2007, including the recommended responsibilities of governments, manufacturers, operators

in the distribution chain, retailers and other relevant parties. The suggested criminal sanctions should also be implemented.

III. Capacity building

The Congress recognized that a country's effectiveness in protecting IP rights is partially dependent upon its capacity to enforce them. Therefore, in addition to prescriptions for better legislation, stronger enforcement and penalties, speakers also suggested methods for improving knowledge, enhancing training and developing skill capacities.

Key recommendations:

1. ICC/BASCAP, INTA and other business organizations should identify ways to share private sector experiences and knowledge in risk management techniques related to counterfeiting and piracy, particularly with most at risk countries.

2. The Global Congress Steering Group should look for opportunities to engage the newly-formed associations of companies involved in the development and use of detection, verification and technology systems to foster an exchange of information on appropriate technologies and systems that are proven to work in the detection and deterrence of counterfeiting and piracy.

3. Through INTERPOL, the WCO and WIPO as well as other organizations directly involved in enforcement, identify opportunities for better coordination of donor efforts and support for training and capacity building for law enforcement officials, focused on building real capabilities region by region and sector by sector.

4. Extend the efforts to combat counterfeiting and piracy to other regions around the world including, in particular, to Africa by organizing an event, under the auspices of the Global Congress Steering Group, in one of the African countries in which counterfeit goods are an emerging problem.

IV. Awareness raising

Many speakers and delegates addressed the need to increase public and political awareness and understanding of counterfeiting and piracy activities and the associated economic and social harm. They also agreed that as a matter of priority, young consumers should be educated about the dangers and consequences of the counterfeiting and piracy trade. Greater steps in raising awareness can lead to informed consumers that better understand the harm associated with purchasing and consuming counterfeit and pirated goods; likewise, well-informed policymakers are in a better position to make appropriate decisions, implement policies and allocate resources.

Key recommendations:

1. The business community must continue to take the lead in raising awareness and educating the public and decision makers on the harms and costs of counterfeiting and piracy, including increased investments to reach broader audiences with more frequent delivery of targeted messaging.

2. The business community should work with IGOs and national governments to collect and exchange communications materials

"...the global problems of counterfeiting and piracy are too great to be solved by individual governments, enforcement authorities, business sectors or companies"

aimed at increasing awareness and education. ICC/BASCAP and WIPO have each initiated a process to collect current programs and research and are working together to share this information with each other and other relevant organizations.

3. National governments must do more to warn consumers about the harm of counterfeit products, building on successful government and government/business sponsored public education campaigns such as those on seat belt safety as well as prevention of AIDS, drug abuse, and other broad social dangers.

4. The business community should seek to inspire a sense of global collective responsibility and action in order for all economic actors to fight against counterfeiting and piracy. The ICC has agreed to invest in developing messages which move consumers to action, and to develop a globally recognized symbol and other elements that could be used by all interested parties to create a common, global awareness and education effort. INTA is developing a web site specifically for educating youth about the value of IP and its protection.

V. Health and safety risks

The Congress widely recognized that counterfeiting and piracy harm society in many ways that are not immediately obvious. This is particularly true for counterfeit medicines and over-the-counter drug products and consumer goods that are not tested to the same safety standards as genuine products. These fake products can seriously injure or even kill consumers, and at a minimum, do not deliver the expected and promised health benefits of the real products. In addition to health hazards presented by foods, beauty and health care products, agricultural products, fake auto parts and electrical goods, speakers addressed the growing problem of counterfeit pharmaceuticals and drew particular attention to the fact that persons in need of medication often acted in good faith and were not aware of, and therefore not in a position to assess, the risk.

Key recommendations:

1. Develop national working groups, comprised of law enforcement, health ministries and the private sector, to develop strategies and programs to combat counterfeit drug, food and beverage and other consumer products such as auto parts, toys and electrical components containing dangerous or sub-standard, unsafe components. This effort should include national public awareness programs to educate and warn consumers about the potential dangers of counterfeits, including the risks of purchasing medicines and food from unapproved sources. As appropriate, this initiative should be promoted and supported by the members of the Global Congress Steering Group, working with the WHO, consumer groups, standards organizations and others involved in consumer safety.

2. Have the Global Congress Steering Group seek opportunities to engage the WHO in the Global Congress process to build synergies with the new IMPACT initiatives and other WHO programs related to counterfeit drugs.

3. Use the Global Congress events to share information on advances in the development and use of covert and overt markers and other detection and verification technologies, and other techniques and standards being created to protect the health care products supply chain against the introduction of counterfeit goods.

4. Encourage the private sector to register trademarks with Customs, and provide the appropriate follow-up training, education and support of Customs officials to enable them to fight the trade in counterfeit goods including, in particular, those which may cause health and safety risks.

5. Build more effective partnerships between law enforcement agencies and the private sector with a particular focus on intelligence sharing, awareness and product identification training and sample sharing.

VI. Free trade zones and transshipment countries

The Congress recognized the legitimacy and benefits of free trade zones and the use of countries for transshipment purposes, but noted there is abuse by counterfeiters and organized criminal networks facilitating the movement of counterfeit and pirated goods into third countries. Speakers and delegates encouraged countries to develop and/or apply required legislation, appropriately enforce the legislation, develop risk assessment procedures and criminally punish traffickers of counterfeit and pirated goods.

Key recommendations:

1. Encourage national governments to enact new, or more effectively apply, legislation prohibiting transshipment and transit of counterfeit and pirated goods at least in cases in which intellectual property rights are infringed in the country of importation and/or the country of final destination.

2. Permit and encourage customs administrations to control shipments into and out of free trade zones and transshipment countries.

3. Assure that customs officials and local law enforcement conduct regular and targeted risk assessment operations to profile and cause disruption to movement of counterfeit and pirated goods.

4. Encourage national governments to punish trafficking of counterfeit and pirated goods through free trade zones with effective deterrent sanctions including fines and incarceration.

VII. Sale of counterfeit and pirated products over the internet

Participants overwhelmingly recognized the importance and urgency of finding concrete and practical solutions to this challenge. Congress speakers emphasized that the internet is not “the Wild West” and there is an urgent need to implement concrete practical solutions to eliminate or at least significantly disrupt counterfeiting and piracy transacted over the internet. This was considered a collective responsibility, requiring action by intermediaries and government authorities to enforce IP rights.

Key recommendations:

1. Intermediaries (eg, registrars, internet access providers, web hosts, search engines and online advertising providers, trade boards, auction sites, online payment providers and credit card companies, courier and shipping companies) should undertake immediate actions to prevent and deter counterfeiters and pirates from accessing their services for the purposes of illicit trade and distribution. These measures should include, in particular: reasonable pre-contractual due diligence (eg, client’s identity verification, legitimacy of business conducted); providing a mechanism for receipt of notices from rights owners and prompt responses thereto, filtering of illegal digital content by internet Service Providers (ISPs), refusing to host sites with counterfeit and pirated content, removing such sites from search results, supporting efforts for increased transparency of data.

2. Governments should: (a) partner with IP owners, ISPs and control authorities to develop methodologies and measures/sanctions to prevent and disrupt illegal activities; (b) strengthen legal frameworks to protect IPRs in an online environment; (c) increase the resources to law enforcement agencies that are engaged in the battle against internet piracy and counterfeiting; (d) establish efficient mechanisms for international cooperation between law enforcement agencies in response to widespread multi-territories fraud schemes.

3. Following the recent government initiatives in France (Olivences report), the UK and South Korea, cooperation and coordination at the international, regional and national levels should be strengthened in order to explore possibilities of controlling access to, and the availability of, counterfeited or pirated material, and techniques for filtering illegal content.

4. Support the further development of INTERPOL’s IPR program ‘Dedicated Internet Anti-Piracy Capability’ by encouraging meaningful partnerships with governments, piracy affected industries and all other stakeholders to maximize opportunities to intervene in the internet piracy related activities of transnational organized criminals.

5. Encourage and support the Universal Postal Union’s (UPU) efforts to implement measures to prevent shipments of counterfeit and pirated products through postal traffic, such as including counterfeit products in the List of UPU Prohibited Articles; developing electronic information to carry out risk-assessment of counterfeit products; raising awareness of postal employees about counterfeit products; and informing postal users about the consequences of sending counterfeit products through the mail. It was noted that these efforts would require external expert help of right holders and appropriate legislation in some cases. ■

Information on the Fifth Global Congress in Cancun and on previous Global and Regional Congresses can be found on the Congress website – www.ccapcongress.net



INTERPOL

John Newton is IPR Programme Manager, Intellectual Property Rights Programme at the International Criminal Police Organization – INTERPOL

The relevance of counterfeiting and piracy to INTERPOL

The International Criminal Police Organization – INTERPOL has been focused on combating intellectual property (IP) crime¹ since 2002 and a significant amount of resources are committed to the cause. The reason IP crime is given priority by INTERPOL is the clear involvement of transnational organized criminals who manufacture and distribute counterfeit and pirate products on an industrial scale on a regional and increasingly global basis. It seems that no industry is exempt from the attentions of these persistent and unremitting international criminals who derive significant illicit profits from their activities.

This is evidenced by the wide breadth of industries who work in partnership with INTERPOL and other stakeholders in an effort to take on and disrupt the activities of the counterfeiters. Industries currently working with the INTERPOL IPR Programme include: agrochemicals; baby milk; battery; beverages; business software; certification (product health and safety); chemicals; condoms; electrical; games software; food; household goods; image consumables; luxury goods; recording; medical product; motion picture; motor vehicle manufacturers; plastic; pharmaceutical; shoe polish; skin care; spirits; telephone; tobacco; toys; and, watch manufacturers. Many more are indirectly involved through their membership of national organizations such as the US Chamber of Commerce.

Of central concern to these industries are the almost infinite trademark and copyright infringements that adversely affect their commercial interests. However, INTERPOL does not expend much energy focusing on definitions or discussions about the relative importance of trademarks over copyright and vice versa. On the contrary, emphasis is placed on doing something about it. The reason for this approach is that modern day organized criminals are effectively commodity brokers who do not distinguish between counterfeiting and piracy, but concentrate on manipulating any illegitimate commodity to generate massive profits. Consequently INTERPOL efforts centre on the common denominator in all types of counterfeiting and piracy, and increasingly illicit trading - the transnational organized criminals themselves.

Against this background INTERPOL consistently delivers three main international functions. The first is raising government policy maker and chief police officer awareness about the links between IP crime and transnational organized criminals. Customs agencies, by the very nature of their work at national borders, have always been involved in the interception of incoming shipments of counterfeit and pirate products. Typically national police forces have not been involved to any degree and INTERPOL is at the forefront of efforts to encourage chief officers to dedicate more resources to fighting transnational IP crime.

The second core function is collecting intelligence about international criminals at the core of organized counterfeiting and piracy. The INTERPOL Database on International Intellectual Property (DIIP) crime is designed to identify criminal organizations that attack more than one industry sector or a group of industries. When links are discovered INTERPOL leads proactive regional cross-industry law enforcement interventions to disrupt these criminal conspiracies.

Facilitating and coordinating these international enforcement operations is the third activity. INTERPOL is an international organization and does not have the power to make these interventions within the territorial jurisdictions of its member countries. The actual enforcement work is done by national police and customs officers in target countries. INTERPOL's role is to identify an 'intervention point' for collective efforts and then bring together the enforcement agencies, IP crime affected industries, cross-industry associations and other stakeholders to make meaningful interventions happen.

Importance of the Global Congress process

INTERPOL was a founder member of the Global Congress Steering Group together with the other two international organizations, the World Customs Organization (WCO) and World Intellectual Property Organization (WIPO). By the three international organizations standing together to tackle counterfeiting and piracy in partnership with the private sector organizations represented on the Steering Group, it sends a



strong message of intent and provides the foundation for the deployment of a whole range of collective activities to make a difference.

Given that INTERPOL is a police organization, it is natural that its role within the partnership is to champion the cause of IP crime at a national, regional and global level. Ronald K Noble, the Secretary General of INTERPOL, highlighted this function at the Second Global Congress on Combating Counterfeiting and Piracy hosted by INTERPOL in November 2005. He also confirmed that the defining characteristic of IP crime for INTERPOL is the involvement of transnational organized criminals.

All four Global Congresses held to date have provided the Steering Group member organizations with an opportunity to review progress and determine strategic priorities for the Steering Group cycle leading up to the next Global Congress. The INTERPOL IPR Programme has steadily evolved over the last five years while at the same time the Global Congress on Combating Counterfeiting and Piracy has developed into the predominant event of its kind in the world. The Fifth Global Congress co-hosted by INTERPOL and the Instituto Mexicano de la Propiedad Industrial (IMPI) in partnership with the Global Congress Steering Group to be held in Cancun, Mexico on 2-4 June 2009 will be a significant milestone as it coincides with the INTERPOL IPR Programme becoming truly global in its outreach.

Evolution of the IPR Programme

In 2002 one police officer was committed to IP crime. In 2009 there are five full-time officials comprising of police officers and other officials who drive the programme forward. Their efforts are enhanced by an ability to generate support from national police agencies in INTERPOL's 187 member countries using the I-24/7 Global Police Communications System. As of February 2009, 89 member countries (48 per cent) from every INTERPOL region have provided intelligence on counterfeiting and piracy and are actively working with the IPR Programme to combat transnational IP crime.

Raising awareness about the nature and extent of transnational organized IP crime among policy makers and chief police officers in member countries has contributed to the increased momentum. However, the real driver for the growth has been leadership and the proactive stance taken by the IPR Programme. This has manifested itself in the four important interconnected outputs. These are the collection of information for action; bespoke IP crime training; coordinating and facilitating regional cross-industry law enforcement interventions into transnational organized IP crime; and, bridging the gap between police and the public health

sector to combat counterfeit medicines in the context of the World Health Organization (WHO) International Medical Products Anti-counterfeiting Task Force (IMPACT).

Database on International Intellectual Property (DIIP) crime

The INTERPOL Database on International Intellectual Property (DIIP) crime was established in 2007 with the active support of the United States Chamber of Commerce. The database has become a unique central point of reference for private industry worldwide to provide information on IP crime. One of its functions is to maintain reliable data on the scale of counterfeiting and piracy to determine more clearly the nature of crimes against brand integrity. The IP Crime Unit analyses the data to identify possible links between IP crimes across different industry sectors to ensure that scarce collective resources can be directed where they will be most effective. The database is now used systematically to support all INTERPOL IPR Programme operational deployments on a regional and global basis.

Apart from making investigations more efficient the database is becoming a valuable tool for informing the strategic development of the IPR Programme. For example, analysis of information has confirmed transnational organized criminals in Southeast Asia are responsible for the flow of counterfeit anti-malarial medicines into parts of Africa. While this was suspected for some time the analysis has enabled police forces in both regions to coordinate their efforts on the same criminal organizations. It is expected these advances will lead to proactive investigations and operational successes in 2009 and beyond.

IP crime training

Raising police awareness about the nature and extent of transnational organized IP crime has led to a tremendous increase in demand for training from INTERPOL member countries. This is especially so in countries where the IPR Programme acts as a catalyst for collective law enforcement interventions in the activities of these criminals. The IP Crime Training Programme initially started in South America to prepare police officers to participate in anti-counterfeiting operations in the Tri-border Area at the junction of Argentina, Brazil and Paraguay.

While these sessions were useful in themselves it was recognized that a more systematic approach was needed. It was decided to aim INTERPOL training efforts at the needs of police middle managers with responsibility for investigating IP crimes. Beginning in 2008, the INTERPOL and Italian Guardia di Finanza co-hosted one-week courses have been attended by over 100 middle managers from 63 member countries. Another 138 customs, drug regulatory body and police middle managers from 26 Eastern and Southern Africa countries received the same training at the INTERPOL and Kenya Police co-hosted IP Crime Training and Operational Workshops held in Kenya in November 2008. Over 120 other drug regulatory body and police managers in Africa and Southeast Asia received similar training on counterfeit medical products to prepare them for operational interventions that took place as part of the IMPACT Programme.



INTERPOL briefing Ugandan Police officers during Operation Mamba, the first combined INTERPOL-IMPACT operation in Africa

Providing 358 operational middle managers with quality training on all aspects of transnational organized IP crime in one year is a considerable achievement and it is hoped to emulate this in 2009. However, a characteristic of policing is that there is often a rapid turnover of staff as officers are either promoted or assigned to other duties. In an effort to counter this loss of expertise and provide consistent learning opportunities, INTERPOL is working with private sector organizations represented on its advisory body, the INTERPOL Intellectual Property Crime Action Group (IIPCAG), to develop an interactive modular IP crime training course which will be accessed through the internet.

It is expected that a working model will be on-line by September 2009. Once the course has been quality-assured the intention is to identify a police IP crime training coordinator in each INTERPOL member country to ensure the training materials on the Internet are made widely

available and are an integral part of national police training. It is expected that this will lead to a better level of awareness about transnational organized IP crime and an increased willingness by police officers to target this criminality.

Coordinating and facilitating regional cross-industry law enforcement interventions

IP crime intelligence and training are only valuable if they are used to support proactive operations. This is an area which has seen steady growth since the First Global Congress in 2004. The first INTERPOL and WCO-led Operation Jupiter – South America pilot deployment in the Tri-border area achieved modest results in the three participating countries with seizures of counterfeit and pirate goods valued at circa US \$10 million. Argentina, Brazil and Paraguay were joined by Chile and Uruguay in the second Jupiter deployment which resulted in seizures of US \$35 million. The experience and lessons learnt in the formative years combined with better coordination led to seizures in excess of US \$121 million and 185 arrests in Operation Jupiter III in early 2008. Jupiter IV, with the operating area extended to include Bolivia and Peru, was concluded in late 2008 and the results exceeded those achieved in Jupiter III.

The working partnership developed between INTERPOL, WCO, the customs, police and IP crime affected industries in South America has been very productive and enabled the Operation Jupiter model to be refined. It has now been successfully applied in all four INTERPOL regions - Africa, the Americas, Europe and Asia - targeting transnational organized criminals involved in manufacturing and distributing a diverse range of counterfeit and pirate products. For example, in Operation Storm in 2008, police across Southeast Asia made a series of arrests and seized fake drugs worth over six million dollars in an operation supported by INTERPOL, the World Health Organization (WHO) IMPACT Programme and the World Customs Organization (WCO).

The operation targeted individuals and groups involved in the manufacture and distribution of four classes of counterfeit medical products identified as posing a significant public health risk – anti-malarials, anti-tuberculosis medicines, anti-HIV medicines and antibiotics, specifically those for pneumonia and child-related illnesses.

Operation Storm confirmed the unique ability of INTERPOL to coordinate such operations. This was recognized by the world renowned PLoS medical journal which commented, "...it is universally accepted that the involvement of INTERPOL was crucial, acting as a bridge between the health sector (including the World Health Organization and the physicians and scientists) and national police agencies to act as a catalyst for action?"

International Medical Products Anti-counterfeiting Task Force (IMPACT)

Since its inception, the IPR Programme has been broad-church in the sense that every effort is made to work with all industries affected by IP crime. However, the last two years has seen more emphasis placed on counterfeit products which have the potential to adversely affect the health and safety of consumers. Some 25 per cent of available resources are dedicated to these activities. The most obvious example of this is the full-time secondment of an IPR Programme crime intelligence officer to the WHO IMPACT Programme.

IMPACT is a global coalition of stakeholders, created in 2006, that aims to develop international collaboration between WHO member states, international organizations, NGOs, law enforcement agencies and health professional groups. The aim is to raise awareness of the dangers of

counterfeit medical products and curb their manufacture and distribution.

The purpose of the secondment is to assist the health sector to offset the damage caused to patients by fake medicines which often contain no active ingredients. Public health authorities and drug regulatory bodies frequently encounter fake medicines for life threatening diseases such as malaria, tuberculosis and HIV aids. However, they do not have the investigative capacity or knowledge to identify sources or intervene in the distribution networks for fake medicines. This is especially so in cases involving transnational organized criminals.

The INTERPOL role is to collate available information and encourage national police forces to intervene. For example, Operation Mamba, the first combined INTERPOL-IMPACT operation in Africa targeted over 230 outlets suspected of selling counterfeit pharmaceutical products throughout Tanzania and Uganda in September 2008. The operation resulted in the seizure of some 100 types of unregistered and suspected counterfeit products. Among the confiscated drugs were anti-malarial, anti-fungal, multivitamin, cardiac, hormonal, multivitamin, skin and veterinary medicines. 2009 will see INTERPOL-led enforcement operations systematically deployed throughout Eastern and Southern Africa.

Private sector and other stakeholder dimension

INTERPOL is proud of its achievements in combating transnational organized IP crime. However, there is one other common denominator which the IPR Programme does not take for granted. That is the constant

support it receives from all IP crime affected industries and other stakeholders working together in partnership with the three international organizations to make a difference. All involved recognize they cannot hope to operate successfully in a vacuum.

There has always been a collective determination to share knowledge and expertise for the common good. This is evident in the commitment shown to the Global Congress Steering Group process by the International Chamber of Commerce (BASCAP), International Trademark Association (INTA) and International Security Management Association (ISMA).

Nevertheless, with the current economic downturn there is an even greater need for all stakeholders to have a common purpose and work towards agreed objectives if the momentum gained since the First Global Congress hosted by WCO in 2004 is to be maintained and enhanced. This will be uppermost in the minds of the Global Congress Steering Group as we work with delegates at the Fifth Global Congress "Bridging Boundaries for Shared Solutions." ■

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1. Intellectual property (IP) Crime is a generic term used by INTERPOL to describe all types of counterfeiting and piracy
2. Source: PLoS Medicine - www.plosmedicine.org - February 2008/ Volume 5/ Issue 2/ e32/ pp.0001-000111



World Customs Organization... Combating Fakes Through Stronger Enforcement and Focused Capacity Building

WORLD CUSTOMS ORGANIZATION

No country can escape the scourge of counterfeiting and piracy, which can have severe financial, economic, health and safety consequences for all. More so in developing and less developed countries whose economies are more vulnerable and poverty more pronounced. And in the current global financial crisis which has caused revenue security fears to surface in many of these countries as they feel the effects of the economic downturn, the counterfeiting and piracy trade adds to their woes. These illegal goods are now being produced on an industrial scale and evidence suggests the active involvement of trans-national organized crime syndicates in this trade. Anything that can be bought and sold is now being counterfeited which means that the health and safety of consumers is now being compromised on a daily basis. Governments therefore expect customs, as a frontline border agency, to protect the community from all forms of dangerous trade by ensuring that they comply with all regulatory requirements.

To ensure that customs is in a position to service its mandate and to enhance the effectiveness of customs anti-counterfeiting and piracy initiatives at the national and regional level, the WCO and its 174 members have focused their attention on strengthening customs border enforcement through innovative capacity building programmes. These programmes include targeted operations or training seminars followed by practical groundwork. As an example, in June 2008 the WCO launched 'Operation Vice-Grips' which rallied the forces of six customs administrations in North and West Africa to conduct simultaneous inspections of imported consignments that could potentially contain counterfeit and pirated goods. The operation involved principal ports in Africa known to be used by counterfeiters and pirates as destinations for their illicit goods, whether destined for the African market or in transit to other parts of the world. Forty-seven maritime containers were inspected by customs officials after they had received specific training in risk analysis and targeting by WCO IPR specialists. Several tons of goods representing globally trusted brand names and consisting of 1.4 million items were intercepted, including fake car accessories, clothing, mobile phone batteries, soft drinks, ink cartridges, gas filters, skin care products, electronic appliances, and even baby hygiene products! This operation revealed a veritable "supermarket" of goods with no product or brand escaping unscathed.

The operational capacity of customs is significantly enhanced through the use of the WCO's secure communication structure – known as CENCOMM – which enables customs and others participating in operations, including anti-IPR operations, to share information and intelligence in a secure environment within the WCO Central Enforcement Network (CEN). In addition, a fully equipped facility located within the premises of the WCO Secretariat called the 'Operation Coordination Unit' (OCU) is available as a central point for the overall steering and coordination of individual operations. This broad range of tailor-made applications and the flexibility of CENCOMM convinced the G8 Heads of Government to select this system for an on-going pilot project among its members which focuses on the exchange of information on seizures of IPR infringing goods among G8 countries.

At the international level, the WCO has continued to enhance its cooperation with intergovernmental organizations and the global business community, whom it recognizes as valuable partners in the fight to combat counterfeiting and piracy. Spurred on to work with others, the WCO joined forces with the European Commission, under the framework of their EU Customs 2013 Programme, to host an international conference in May 2008 on combating the fake goods trade. Solutions proposed for concrete action included: the need for real acceptance at the highest political level of the dangers posed by counterfeiting especially to consumers; the need for improved and adaptable legislative and operational measures; the need for customs to have practical tools that would enable them to distinguish between genuine and fake goods; the need to concentrate resources and intensify efforts at the operational level; the critical need to improve exchanges of information between the public and private sectors; the need to improve customs-to-customs intelligence flows; and the need to find practical solutions to counter fake goods being traded via the internet.

In recognizing that more still needs to be done to stop the deluge of counterfeit goods reaching world markets, the WCO's anti-counterfeiting and piracy efforts will be invigorated during 2009 by enhancing its partnership approach, by ensuring that more use is made of new technology, by promoting innovative approaches to IPR border

enforcement, and by encouraging even more national and regional participation. But this is not all, the WCO's current action plan includes implementing initiatives to assist customs in meeting their obligations under the WTO TRIPS Agreement, creating extra tools to enhance customs operations, making sure relevant information and intelligence is at the disposal of WCO members, promoting more exchange of information and customs best practice, ensuring that the WCO becomes a forum for discussing IPR issues in a transparent manner; and introducing a dynamic and responsive IPR capacity building programme which is consistent with the policy objectives of WCO members and which will truly enhance the skills and competencies of customs officials on the frontline.

Customs operational activities will be stepped up and will include those targeting major international sporting events such as the 2010 FIFA World Cup in South Africa as experience has shown that these sporting

events are a major 'business opportunity' for counterfeiters across the globe. Also, the WCO will begin discussions on the challenges posed by internet sales of counterfeit products which have grown enormously over the last few years. Our commitment to finding a solution to internet sales of counterfeit goods, especially fake pharmaceuticals and foodstuffs, is unflinching. There is no doubt that tackling this issue is going to be difficult and will require Herculean efforts and creative action on the part of the WCO, its members, and its international stakeholders.

The WCO's plans for this year are already in motion and the organization is ready to actively work with its Global Congress partners to challenge counterfeiters head on and deal a mighty blow to this dark trade! ■

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Enforcement Takes Centre Stage on the International Agenda

Michael Keplinger is a Deputy Director General of the World Intellectual Property Organization



**WORLD
INTELLECTUAL
PROPERTY
ORGANIZATION**
**ORGANISATION
MONDIALE
DE LA PROPRIÉTÉ
INTELLECTUELLE**

While counterfeiting and piracy are age-old concerns, the recent escalation and alarming growth in the scale and scope of these illegal activities and their corrosive impact on economic development and social well-being is obliging policy-makers across the globe to find creative, durable, and effective solutions and strategies to tackle this challenge. In spite of the difficulties encountered in accurately measuring the extent of this illicit and clandestine trade, empirical data suggests that the trade in fake goods affects all economic sectors and is prevalent in all economies. It is no longer the unique concern of the major luxury goods manufacturers – trade in fakes is increasingly troubling for businesses, consumers and policy-makers operating in all sectors in all countries. All economic sectors that are driven by creativity and innovation - from consumer and household goods-based industries to the creative industries (eg. film, music) - are under threat from this illicit trade. The risks to the health and safety of the general public resulting from the sale of fake pharmaceuticals and sub-standard mechanical and electrical appliances are perhaps of greatest concern.

Counterfeiting and piracy, the industrial scale of which points to the involvement of organized crime rings, stifle local industry, threaten employment, tax revenues and the services they support, discourage international trade and foreign direct investment, present significant health and safety risks, cultivate a negative international image for countries hosting these operations, place a heavy burden on law enforcement authorities, and can potentially foster corrupt practices within government. The effects are many, and are felt at all levels of the society.

The startling growth and increasing sophistication of counterfeiting and piracy have been fuelled by a number of factors: at core, this illicit trade is driven by the prospect of high and quick profits and a low risk of sanctions. On top of this, the widespread availability of copying technologies has enabled the production of clones. Increased global market integration, the creation of free trade zones and the proliferation of the internet have also spawned new and improved distribution channels. These factors have all contributed to the emergence of a complex global challenge which threatens the future economic growth and prosperity of all countries and for which global solutions and the active engagement of all stakeholders is essential.

Central to the challenge of effectively combating counterfeiting and piracy is a strong political commitment to supporting the development of effective and appropriate solutions. This requires a better understanding of the dimensions of the challenge, the problems and difficulties encountered by different countries around the world, as well as closer cooperation between the various stakeholders (government agencies, the private sector and consumers).

While we all have - whether as right holders or as consumers - a role in supporting respect for IP rights and their enforcement, in most

circumstances we do not need to develop new laws. Governments can achieve a great deal in the battle against IP crime by updating, where needed, and effectively implementing the legislative frameworks that are already in place, and by giving real meaning and adequate support to the enforcement mechanisms currently at their disposal. Little can be achieved, however, without raising general awareness, particularly among members of the judiciary, as well as the general public, of the destructive consequences of IP crimes, and the need to mete out effective penalties under national law.

The Geneva-based World Intellectual Property Organization (WIPO) – a specialized agency of the United Nations - is the global body charged with promoting the protection of intellectual property (IP) for economic, social and cultural development. As such, the Organization is well placed to play a leading role in coordinating IP enforcement activities at the international level. Through its Advisory Committee on Enforcement (ACE) and in line with requests from its member states, WIPO is actively engaged in the process of identifying stumbling blocks to effective enforcement and working with global partners to reach workable solutions. Together with a diverse group of stakeholders, WIPO's Enforcement and Special Projects Division is supporting efforts to develop effective government and industry anti-counterfeiting and piracy strategies. Such strategies focus on legislative assistance, improved coordination, capacity building, and awareness-raising. Many efforts are being undertaken to coordinate activities at the international level and to strengthen cooperation between intergovernmental (IGO) and non-governmental organizations (NGO) in combating counterfeiting and piracy.

The ACE also provides a forum for international review and discussion of IP enforcement issues with a view to identifying opportunities for improved coordination and cooperation among stakeholders. At its November 2007 session, the ACE focused on cooperation and coordination at different levels for effective enforcement of IP rights under criminal law and considered issues such as the scope and definition of IP crimes, investigation and initiation of criminal proceedings, jurisdiction, means of streamlining proceedings, evidentiary issues, sentencing options and level of penalties. This body takes a balanced approach to IP enforcement, including in the context of broader societal interests and development-oriented concerns. The ACE is a further indication of the clear commitment of WIPO and its member states to join forces, with public and private sector stakeholders, in developing effective strategies to counter the insidious problems of counterfeiting and piracy.

The Organization also provides countries, at their request, with legal advice on the protection and enforcement of IP rights. In this respect, countries are placing a much greater emphasis on enforcement than before. Effective enforcement requires active involvement of attorneys, judges, customs, police, prosecutors, and administrative authorities. WIPO supports the efforts of all countries to combat counterfeiting and piracy through, for example, the organization of training programs for

judges and other actors in this field. In promoting better coordination and cooperation with organizations actively engaged in combating IP-theft, the Organization is committed to facilitating an informed and balanced global debate on adequate responses to the challenges to IP enforcement caused by counterfeiting and piracy and the economic consequences of inefficient IP protection and enforcement.

WIPO is also a key member of a unique public-private sector coalition known as the Global Congress on Combating Counterfeiting and Piracy, which is united in its efforts to identify solutions to effectively combat counterfeiting and piracy and to facilitate their implementation.

The Fourth Global Congress on Combating Counterfeiting and Piracy, which was held in Dubai in 2008, called on national and international political leaders to engage in the battle against counterfeiting and piracy. More than 50 speakers from 25 countries delivered proposals for more effectively combating counterfeiting and the so-called Dubai Declaration¹, which emanated from the Fourth Congress, outlines concrete recommendations and offers a visible expression of the international community's united efforts to tackle the scourge of counterfeiting and piracy.

The Global Congress was previously hosted by WIPO in January 2007 in Geneva; by INTERPOL in 2005 in Lyon, France; and by WCO in 2004 in Brussels. These international gatherings provide a valuable forum for representatives from both the public and private sectors to pool their experience, raise awareness, enhance cooperation and identify strategies to deal more effectively with the global problem of counterfeiting and piracy.

In the five years since the first Congress was convened, significant progress has been made in terms of galvanizing global awareness, particularly among top policy-makers and leaders as well as members of the public, about the gravity of the multiple challenges presented by the trade in counterfeit goods along with the need to join forces in implementing effective and practical countermeasures. This is further evident from recent developments in various frameworks, such as the G8 Declaration on the World Economy, and multi-country discussions on a draft Anti-Counterfeiting Trade Agreement (ACTA).

On the day-to-day operational level, WIPO provides a number of IP services that are designed to help businesses around the world obtain international protection for their trademarks, patents and designs, and to better guard themselves against infringement. Whereas all IP rights are territorial, and extend only to the border of the country in which they are recognized, WIPO's international filing and registration systems offer a timely and cost-effective means of obtaining IP protection in multiple countries. WIPO's Arbitration and Mediation Center provides a range of alternative dispute resolution services which offer considerable advantages in certain IP disputes by offering a single, rapid, cost-effective and neutral procedure. The Center is also one of the main architects of the Uniform Domain Names Dispute Resolution Policy (UDRP) which is a cost-effective and rapid way to resolve disputes relating to the abusive registration of trademarks as domain names, a phenomenon known as cybersquatting.

WIPO is committed to ensuring that all of its 184 member states are aware – and make full use – of the enormous potential of the IP as a tool to create value and enhance economic growth. Companies and governments around the world are increasingly recognizing the strategic importance of IP in promoting national and commercial interests. The establishment of an IP culture in which there is broad-based understanding of the role and potential of the IP system, – one of WIPO's principle objectives – is a key ingredient in promoting greater respect for IP rights. Well functioning enforcement mechanisms are an excellent means to deter IP-related violations and to ensure that right holders and society as a whole can fully reap the benefits from the IP system.

While the challenges associated with the battle against the global trade in counterfeiting and piracy are formidable, there are important signs of broader awareness, and a greater and more widespread political will and readiness to cooperate and to take concerted action. It is heartening to see a growing, deep-rooted concern to uphold and respect IP rights. Enforcement has clearly moved up the global political agenda. This is witnessed by a growing willingness to take concerted action and bolster national and regional efforts to ensure effective enforcement. Just as in today's knowledge-based economy, the possibility of achieving sustainable economic growth depends on effective use of the IP system, so too, the credibility of the IP system depends on the enforceability of IP rights and the effectiveness of those who carry out this important task. ■

1. see <http://www.ccapcongress.net/archives/Dubai/Files/Final%20Dubai%20Outcomes%20Declaration.pdf>



Mobilizing Business in the Fight Against Counterfeiting and Piracy

Jeffrey Hardy is the BASCAP Coordinator at the International Chamber of Commerce

Business Action to Stop Counterfeiting and Piracy – BASCAP – was launched by the International Chamber of Commerce to:

- Connect and mobilize businesses across industries, sectors and national borders in the fight against counterfeiting and piracy.
- Pool resources and expertise – creating greater critical mass than any single company or sector could do alone.
- Amplify the voice and views of business to governments, public and media – increasing both awareness and understanding of counterfeiting and piracy activities and the associated economic and social harm.
- Compel government action and the allocation of resources towards strengthened intellectual property rights enforcement.
- Create a culture change to ensure intellectual property is respected and protected.

The challenge

Counterfeiting and piracy impact virtually every product category. The days when only luxury goods were counterfeited, or when unauthorized music CDs and movies DVDs were sold only on street corners are long past.

Today, counterfeiters are producing fake foods and beverages, pharmaceuticals, electronics and electrical supplies, auto parts and everyday household products. And, copyright pirates have created multi-million networks to produce, transport and sell their unauthorized copies of music, video and software. Millions of fake products are being produced and shipped around the world to developing and developed markets at increasingly increasing alarming rates.

Millions of consumers are now at risk from unsafe and ineffective products, and governments, businesses and society are being robbed of hundreds of billions in tax revenues, business income and jobs.

The drain on the global economy is significant and the longer term implications of the continuing growth in this illicit trade are enormous. The OECD has reported that "international trade in counterfeit and pirated products could be up to US\$ 200 billion". Taken together with the value of domestically produced and consumed counterfeits, the significant volume of digital and fake products being distributed via the Internet, and the loss of economic development, harm to health and safety, reduced technology transfer, and innovation, the total magnitude of counterfeiting and piracy worldwide is well over US\$ 600 billion.



BASCAP Global Leadership Group, New York March 2008

The enormous impact of counterfeiting and piracy

- Loss of business – perhaps most obvious to business is lost sales, diminished reputations and loss of good will suffered by legitimate right holders. For example, about a quarter of small to medium sized businesses in Europe report lost sales resulting from customers purchasing counterfeit items. According to the toy industry, counterfeiting was responsible for lost sales of almost 11% in Spanish companies, rising to just below 50% amongst a group of very small companies.
- Loss of employment – the loss of legitimate jobs among trademark owners and their supply chain partners is real and significant. In 2004 French Finance Minister Nicolas Sarkozy (now President) said that counterfeit goods were costing France some 30,000 jobs a year through lost sales suffered by affected companies. The US Chamber of Commerce estimates that counterfeiting and piracy costs the US 750,000 jobs annually. The motion picture industry reports 141,030 jobs are lost to piracy annually. The US auto industry estimates 10,000 jobs per year lost to counterfeit auto part markets. It is estimated that a 10% reduction in computer piracy in the US would lead to an additional 105,511 jobs.
- Damage to reputation and image – the presence of fake products in the marketplace confuses consumers and eventually destroys consumer trust in branded products. This becomes an even more significant problem for pharmaceutical, over-the-counter drugs and other products that have serious health and safety implications. Counterfeits eventually can damage the reputation of an entire company.
- Risks to health and safety – an increasingly alarming aspect of the counterfeit problem is the increase in fake drugs and other goods that present public health and safety risks. Substandard counterfeit products already have caused injuries and deaths in developing and developed markets and there is evidence these problems are escalating. The World Health Organization (WHO) estimates that counterfeit drugs account for 10% of all pharmaceuticals. That number can rise to as high as 60% in developing countries. And, it is not just fake drugs that are of concern. Among the other reported cases involving serious health and safety ramifications: fake vodka with lethal doses of methanol in the UK; counterfeit airplane parts in Russia; counterfeit toys found to cause suffocation and strangulation; 3,000 doses of counterfeit blood pressure drugs administered to patients in Siberia; 10% of pharmacies in Taiwan found selling counterfeit sleeping pills containing harmful substances; and the European toy sector reporting products that do not comply with basic safety standards and contain toxic substances or be made from hazardous materials; and counterfeit fake brake pads, brake shoes and steering linkages in the auto parts segment.
- Loss of tax revenues – significant tax revenues may be lost to the country or region in which the abuse occurs. Tax losses include unreported and unpaid corporate profits taxes, value-added taxes uncollected when items are purchased, and payroll taxes from undocumented workers. These losses deprive governments of revenues needed for other social priorities. The associated Chambers of Commerce and Industry of India found that counterfeiting and piracy has robbed the Indian government of \$31.25 billion in lost tax revenue.
- Stifling innovation, entrepreneurship and business initiatives – Innovation and creativity suffer in markets where counterfeiting and piracy are present. Companies become cautious about investing in R&D or decide to locate a manufacturing plant or research facility somewhere else. A European survey of small and medium sized companies found that 25% of decisions to invest in R&D or production were adversely influenced by considerations of IPR abuses.
- Links to organized crime – attracted by high profits, low risk of detection and minimal penalties for IP crimes, organized criminals

increasingly are moving into the manufacture and distribution of counterfeits. The US Federal Bureau of Investigation (FBI) and Interpol have both reported that organized criminal groups have moved into IP crime and that they are using the profits generated from these crimes to facilitate other illegal activities.

A brief history of BASCAP

BASCAP was launched in early 2005, with a strategy of engaging CEOs and other top executives from multiple sectors and industries directly in the fight against counterfeiting and piracy. A Global Leadership Group (GLG) made up of CEOs and senior executives was formed to provide strategic direction, set priorities and act as the voice of BASCAP with senior government officials and the media.

Membership at the CEO level has grown and the GLG now includes 25 core members. Each company is also represented by a senior executive who serves on a Steering Committee that directs the day-to-day activities and priorities of BASCAP. The Steering Committee shapes the BASCAP message and program direction, formulates products and missions and establishes implementation priorities.

Overall, BASCAP has included participation by some 150 companies and trade associations that have championed the initiative through various degrees of participation, contributions of expertise and/or financial support. BASCAP is supported by a dedicated and experienced group of experts at the ICC charged with implementing the strategies, direction and priorities identified by the GLG and Steering Committee.

BASCAP programs and activities

- Public policy and advocacy – BASCAP's long term goal is to press governments to take concrete action to reduce and ultimately eliminate counterfeiting and piracy. Shorter term, BASCAP's priority is to push for significantly higher benchmarks for government performance at the national, regional, multi-lateral and international level.
- Communications and education – greater public awareness and education are essential in the fight against counterfeiting and piracy. BASCAP communications capitalize on ICC's strong and broad media "assets" including materials production staff, editorial writers, global mailing lists, email alerts, website featuring 300,000 page views per month, and a worldwide network of media contacts. Hundreds of BASCAP news reports have appeared on television and radio and in wire services, newspapers, magazines, and e-publications. Major international media have covered BASCAP meetings, events and press releases. National television, radio and press reports have appeared in over 30 countries throughout the world. Our messages have repeatedly reached at 350 million households worldwide. Additionally, a cornerstone of BASCAP activities is the creation of educational content aimed to help governments better understand the value of investing in stronger IP enforcement.

The initial focus of BASCAP was the development of a set of core information products and a wider portfolio of tools and intelligence that would provide the base upon which to build a full and forceful engagement in the fight against counterfeits and pirates. BASCAP subsequently moved forward with direct interventions to deliver the positions of the business community to governmental bodies such as the G8 and EU, and intergovernmental organizations, including WIPO, WCO and Interpol. BASCAP also has spoken out through news conferences and news releases to the international media on important developments in the battle against counterfeits and piracy, and initiated a public education and media campaign to reach consumers and government leaders.

BASCAP's key priorities moving forward include setting standards for global performance by governments and companies; framing decisions for policymakers; pushing for the allocation of resources at the highest levels in national governments; and, improving awareness on a global basis.

BASCAP – through its member companies and their CEOs and other senior executives and its dedicated support staff – will continue to look for new and creative ways to deliver the strongest and most compelling case for priority action by governments and enforcement officials. BASCAP's mission is to change the policy and legal climate on counterfeiting and piracy by – calling local, national and international enforcement officials to action, petitioning for the reallocation of resources, and pressing for results. ■

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Protecting and Promoting the Rights of Trademark Owners



International Trademark Association

The International Trademark Association (INTA) is a not-for-profit membership association of more than 5,800 trademark owners and professionals, from more than 190 countries, dedicated to the support and advancement of trademarks and related intellectual property as elements of fair and effective national and international commerce.

The Association was founded in 1878 by 17 merchants and manufacturers who saw a need for an organization "to protect and promote the rights of trademark owners, to secure useful legislation and to give aid and encouragement to all efforts for the advancement and observance of trademark rights." After 130 years, INTA continues its mission to represent the trademark community, shape public policy and advance professional knowledge and development through education and training, information and publishing as well as policy development and advocacy.

With worldwide expertise on trademark issues, INTA regularly engages with public policymakers who value the Association's insights into trademark issues and trends. The Association, often in cooperation with national, regional and international intellectual property organizations, encourages adoption of and adherence to trade agreements and multinational treaties, acknowledging that trademark protection encompasses broad trade concerns. INTA promotes these efforts and carries out its public policy mission through a number of vehicles, including, but not limited to, amicus briefs, advocacy, reports, and model laws and examination guidelines.

Anti-counterfeiting a top issue for INTA

Counterfeiting is one of the most important issues INTA and its members face. As an international leader in discussions and efforts to enhance public and private sector efforts that combat counterfeiting, INTA believes strongly that nations must work together and exchange information and ideas that will eliminate the threat posed by cheap, fake goods that have potential to harm consumers and play on the good name of legitimate marks. ■

INTA approach to anti-counterfeiting

Global Partnerships	International Policy Advocacy
<p>Global Congress on Counterfeiting and Piracy As part of the Global Congress Steering Group, INTA supports and lends industry expertise to the development of a high-level strategic forum design to create and strengthen public-private sector partnership in enhancing cooperation, capacity and public awareness on anti-counterfeiting and anti-piracy.</p> <p>ACTA Business Response Group In partnership with the International Chamber of Commerce (ICC) Business Action to Stop Counterfeiting and Piracy (BASCAP), INTA created an informal business response group to monitor and provide industry-wide perspectives on the Anti-Counterfeiting Trade Agreement – a trade agreement that INTA hopes will truly raise the standards of IP protection globally.</p>	<p>Through INTA's Anti-Counterfeiting and Enforcement Committee (ACEC), INTA works with members to outreach to national governments around the world to strengthen anti-counterfeiting laws and regulations, enforcement practices, and industry partnerships. The seven Subcommittees in the ACEC evaluate treaties, laws regulations, procedures and other enforcement measures; develops and advocates policies to advance protection against counterfeiting and infringement; and provides anti-counterfeiting and enforcement education.</p>

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INTA - Representing Trademark Owners Since 1878



INTERNATIONAL SECURITY MANAGEMENT ASSOCIATION

The Worldwide Organization of Chief Security Officers

Enhancing Professional and Business Standards Worldwide

The International Security Management Association (ISMA), founded in 1983, is a premier international security association of senior security executives from major business organizations located worldwide. ISMA's mission is to provide and support an international forum of selected security executives whose combined expertise will be utilized in a synergistic manner in developing, organizing, assimilating, and sharing knowledge within security disciplines for the ultimate purpose of enhancing professional and business standards.

ISMA provides opportunities to network with other senior security executives and to establish a leadership forum to provide personal and professional growth opportunities. Members benefit from semi-annual workshops held in major cities around the world. Workshops focus on security, business, and leadership issues to include a members' forum which generates open discussion on a variety of security, management and other relevant topics. One of the greatest benefits of ISMA membership is

the opportunity to develop professional and personal relationships with other leaders in the international security community. These relationships benefit the company as well as the member. ■

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Instituto Mexicano de la Propiedad Industrial



The Mexican Institute of Industrial Property (IMPI) is the administrative authority in charge of industrial property matters in Mexico. It was created by presidential decree on December 10, 1993 and is a decentralized body with legal authority and with its own assets, including its own budget.

The general objectives of IMPI are: to protect industrial property rights through patents, utility models, industrial designs, trademarks, trade names, advertisement slogans, appellations of origin and trade secrets; to prevent acts that infringe intellectual property rights or that constitute unfair competition; and, to establish the corresponding sanctions and penalties to such acts. Another objective is to promote and encourage inventive activity that has industrial applications and technical improvements, as well as disseminating technological knowledge within productive sectors.

Since its creation, IMPI has faced significant changes regarding the volume of IP issues provided. They are highlighted as follows:

- With regard to inventions, in 1994 the institute received 11,627 applications and in 2008 it received 20,198 applications. From 1994 to December 2008, it had received a total of 220,089 invention applications.
- With regard to marks, in 1994 the institute received 34,253 applications and in 2008 it received 77,574 applications. From 1994 to December 2008, it had received a total of 799,416 mark applications.

IMPI human resources increased from 250 employees in 1994 to 895 employees this year with the aim of providing and solving the growth in demand of application services.

This has resulted in the allocation of IMPI's officers in two central buildings located in Mexico City as well as five regional offices strategically located within the country of Mexico.

IMPI is more than an institution only in charge of protection procedures and/or inventions and marks registrations. In 1997, IMPI was granted the faculty to punish copyright infringements on trade related commerce foreseen in Article 232 of the Federal Copyright Law. This responsibility was given to IMPI as a result of the acquired experience by officers in charge of sanctions to infringements on industrial property matters. This was possible because of IMPI's advantage of having an enforcement infrastructure.

In this respect, concerning enforcement, IMPI is an institution where the protection of intellectual property rights is managed in a *sui generis* way. This is because IMPI is the only industrial property office that deals, in a direct way, with all intellectual property infringement matters. It is a kind of specialized mini-court on IP matters. This ensures that the force of the law provisions work rapidly and promptly in favour of those acquired rights. Since 1994 to December 2008, the institute has received 30,068¹ administrative declaration applications; performing 41,822 inspection visits and seizing 67,484,916 products that presumed to infringe intellectual property rights, with a monetary value of approximately USD\$12,000,000².

Likewise, Mexico has consistently tried to strengthen intellectual property rights (IPR) protection and it has revised its laws to comply with global standards. Furthermore, IMPI will continue to promote its anti-counterfeiting and anti-piracy policies, especially regarding legislation, education and public awareness.

Besides Mexico's national legal framework, in order to align its legal framework with international IP regulations Mexico is currently a member

of the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) administered by the World Trade Organization (WTO), complies with 17 treaties and conventions administered by the World Intellectual Property Organization (WIPO), including UPOV and those two WIPO treaties dealing with internet and digital era, and has signed 12 Free Trade Agreements (FTAs) that include chapters or provisions regarding IPR.

Mexico is aware of the problem concerning the illegal economy, specifically piracy and counterfeiting, which needs to be attacked through the participation of the public sector, industry, federal authorities, consumers, since it is a problem that affects everybody and there is a need of joint collaboration among these stakeholders.

It is important to stress that on June 15, 2006, the National Agreement Against Piracy was signed by Mexican federal authorities, including Mr Vicente Fox, President of Mexico, as an honour witness.

The general objective of this Agreement is to develop sustainable and permanent strategies, performed by the public and private sectors, to defend intellectual property rights against illegal actions and with the aim of recovering the loss of market because of these crimes.

Within this framework, an inter-institutional Committee for the Attention and Protection of Copyright and Industrial Property works with the aim of fighting against the illegal market in order to retrieve the national and international market, as strategic keys. They constitute compelling factors for the enhancement of the national public heritage since, as a result of actions, more and more economic recovery will be realized, the reactivation of productive plants will arise and the fostering of legal establishments will make a financial contribution to the state wealth.

Furthermore, IMPI is signing State Agreements Against Piracy with three action lines: i) recovery of internal market, ii) fight against illegal actions, iii) public awareness and education.

Currently, Mexico is carrying out actions to fight piracy and counterfeiting, divided into these main categories: i) measurement; ii) international cooperation, iii) public awareness.

The best way to know the impact of public awareness and knowledge among the public and consumers is that of measurement in order to establish next steps for future actions about consumers' perception concerning counterfeiting and piracy.

Regarding international cooperation, IMPI is actively participating in different regional, multilateral and international forums for combating counterfeiting and piracy among all authorities in charge of the protection of IPR.

A very important element in combating piracy and counterfeiting is public awareness with the aim of providing the general public continuous campaigns emphasizing IPR, the importance of these rights and helping people realize the negative effects of this particular form of economic crime. It is important to stress that IMPI has been involved in raising the awareness of IP among the judiciary.

IMPI has been active in strengthening and fostering of IPR, with regard to promotion and training events (training courses, tradeshow, among others), as well as carrying out several campaigns addressed to the general public and to specific stakeholder groups. The campaigns are jointly organized by IMPI, the private sector, non-governmental organizations and government agencies such as the Attorneys General Office (PGR), the National Institute of Copyright (INDAUTOR), the Ministry of Finance (SHCP) through customs and the judiciary, among others. ■

1. 26,457 solved procedures
2. \$172,018,642 pesos



Anti-Counterfeiting In Challenging Times



Stuart Adams and Jeremy Newman are Directors of Rouse, a global intellectual property consultancy

So, here we are. In a recession. Again.

You would need to have been working in the early 90s to have experienced a serious downturn in the global economy. But even that, by all accounts, was pretty gentle compared to what we are facing now and which many commentators are comparing to the Depression of the late 20s/early 30s. This is uncharted territory in the world of anti-counterfeiting.

How do, and will, these tough economic times impact upon counterfeiting and rights holders' ability to do something about it?

We are already seeing some very obvious effects as rights holders look to cut costs in order to maintain profit or keep losses to a minimum. Production lines are closing. Head offices are instituting head count freezes and imposing dramatic budget cuts. Non-essential travel is being cut. Marketing/advertising spend is being cut. And in many companies we have already seen cuts to the budgets of legal/intellectual property (IP) teams.

More counterfeiting?

Such cuts are coming at a time when the temptation to counterfeit, and even knowingly purchase counterfeits, has rarely been higher. Far from cutting anti-counterfeiting budgets, most rights holders would be well advised to increase them or risk losing whatever hard won advances they may have made against counterfeiters in recent years. Here are just some of the factors leading to this conclusion.

- Cutting production of genuine goods in response to reduced demand inevitably leaves factories sub-contracted by brand owners with empty order books...but also with all the expertise and tooling required to continue production. Those factories may have been producing finished goods, or branded components/spare parts.
- Take the simple example of a factory in China which for some years has been producing genuine goods under contract to a major multinational. Now the major multinational is suffering massively reduced sales and has terminated the contract with the Chinese factory. Hundreds or even thousands of jobs will be lost at the Chinese factory. What an enormous temptation for the factory owner to turn to the production of counterfeits.

As an aside, this is also a very good example of the need for carefully drafted contracts with such suppliers in the first instance which should, ideally, provide for the return of tooling upon termination and a right to conduct audits post termination.

- Just as worrying is the sub contractor whose order books are less full but has not been terminated completely. Such manufacturers are perfectly placed to engage in 'back door supply' whereby production in excess of that which the rights holder is now ordering is sold to anyone who will come and buy it.

Again this shows the importance of carefully drafted supply contracts with, for example, provisions allowing for regular unannounced factory visits and audits. But whilst these days such provisions are common, one has to ask how often rights owners exercise their rights. And when rights owners are cutting costs and cutting staff, how many will even be able to exercise such rights? At the very time when extra vigilance is required there must be every prospect of rights owners actually becoming less vigilant.

- In a similar vein, those providing services to customers using branded goods are now under extreme pressure to supply counterfeits.

A good example of this would be a car service/repair business. It could be anywhere in the world. That business now has fewer customers as drivers make the inevitable decision to extend service intervals. To try to eek as much profit as possible out of dwindling customers, the temptation to fit counterfeit parts and use counterfeit oil and other such materials must be huge. Even the customer themselves may well be tempted to ask for 'non-genuine' parts and lubricants, choosing to

turn a blind eye to the risks and convince themselves that these will be 'good enough' given the cost saving.

- In addition distributors, whether to end users or customers such as the service/repair business mentioned above, may be tempted, and are ideally placed, to trade in counterfeits to try to increase margins on decreased sales and thus maintain a level of profitability.

To take a simple example, think of the supplier of office stationery. How tempted that trader must now be to supply counterfeit consumables such as toner to his customers. Alternatively, rather than knowingly buying and selling counterfeits they might instead go to the grey market for stock, turning a blind eye to the risks and inevitably purchasing a proportion of counterfeits.

- At an individual level, unemployment around the world is starting to rise at a very worrying rate. Of course this is disastrous for all concerned. But inevitably, one of the means which some will turn to in order to maintain a level of income is by trading in counterfeit goods. The internet has made this a pretty simple exercise. We have, for example, seen a recent significant increase in offensive auctions on popular Chinese trading sites. Following up on these has led to the conclusion that many of these are not typical 'traders' but simply the work of individuals trying to supplement declining/disappearing incomes.

- Following on from this, some consumers are now, of course, far more likely to be willing to purchase counterfeits. We have already alluded to this above, but envisage the problem becoming most acute in respect of those goods where consumers do not believe there is any harm in the counterfeits. Clothing, footwear and luxury items such as handbags and watches are obvious examples. Rights holders, governments and other agencies have tried very hard to persuade consumers against counterfeiting but would appear to have had only a modicum of success. If our arguments don't work when consumers feel relatively affluent what chance have we got as recession bites?

And so on. We can all think of countless similar examples of how and why counterfeiting is likely to get worse during this recession. Worse still, surely, if affected rights holders spend less tackling the problem.

More difficult to enforce rights?

All this is happening at a time when tackling counterfeiting is likely to get more difficult. For example:-

- Traders will be more desperate today than they were a few months ago to avoid/evade detection and punishment. They will quite simply be more difficult to find.
- And if you are able to find them they are likely to be much smarter about how they do business, making it more difficult to obtain evidence of sufficient weight to convince rights holders, and then the requisite authorities, that action is warranted. For example, traders will be even more likely to keep production runs and stocks to an absolute minimum. Such stock as there is will be more likely to be kept in multiple unmarked warehouses held in the names of multiple individuals. Seeing the big picture will be more difficult than ever.

- If you are able to find a target and obtain good evidence, enforcement will be more difficult. The very people you most look to for assistance (administrative enforcement bodies, the police and the courts) are all acutely aware of the increased social impact at this time of striking out at someone's ability to earn a living and employ fellow citizens. This fear was brought starkly to light in a news report which appeared recently in Hong Kong's South China Morning Post revealing that law enforcement officials in Guangdong Province (China's 'factory', and the Chinese province most affected by the recession so far) were being urged by the Ministry of Public Security to turn a blind eye to minor offences committed by key business people and technical personnel. There is no guidance on what might constitute 'minor offences' but the risk to anti-counterfeiting efforts is clear.

Similarly, the Supreme Court in China has issued guidance to lower courts advising them to be extra cautious when considering applications for property preservation orders. Such orders have become a vital tool for Plaintiffs in China since enforcement of awards of damages is so difficult. Anything which limits the availability of asset preservation orders will be a huge setback for civil litigation.

- Furthermore government spending on anti-counterfeiting enforcement is surely going to be squeezed leading inevitably to prioritisation. Combined with the difficulty of persuading the enforcement officials to help you, it is likely to become increasingly difficult to get sufficient evidence to persuade administrative authorities to take action, or to persuade civil courts to impose sufficient awards of damages to act as a deterrent. Also, of course, it is going to be more difficult to persuade criminal courts to impose sufficient penalties when faced with a defendant arguing that his 'victimless crime' was committed only in an attempt to feed his family.

- Budget reductions/reduced activity could easily reduce the opportunity for collaboration. This is a huge shame. We have seen considerable movement over the years from a mentality where collaborating with competitors was unthinkable in many/most industries to recognition that acting in concert is likely to lead to enforcement which is both more effective and more cost effective. Now if one or more members of a loose coalition simply don't have the budget to participate any more (or, worse still, have gone out of business completely), enforcement for the remaining members will become more expensive and less effective.

More funding?

All of which surely indicates that now is most definitely not the time to be cutting anti-counterfeiting budgets. To do so would significantly risk losing any hard won gains over previous years, making it still more difficult to get on top of the problem when the recession ends.

Prioritisation

Whether or not the argument within rights holding companies for an increase in anti-counterfeiting budget is won, it will be more important than ever to prioritise resources where they are most likely to have the most significant impact.

This, as ever, will require rights owners to look carefully at where they can spend precious resources to have the most impact. This will vary from industry to industry, company to company. Inevitably China will figure

large in most rights holders' budgets as will crucial choke points such as busy transit ports and free trade zones.

One area in particular, however, stands out in the opinion of the authors as requiring dedicated attention even in times of restricted budget – customs. Customs continues to be the area where most impact has been made over recent years and which still has so much to offer. Vast amounts of the counterfeit goods produced travel the globe. We have opportunities to not only seize them, but in doing so obtain vital information about production and supply chains as they pass through borders (and, we should add, whilst passing through transit ports and free trade zones).

But we need to be smarter about how we work with customs. We need to spot trends and react to them. To take one example, statistics released by the European Commission last year showed an increase in the number of individual customs detentions in the EU (from 37,334 to 43,671 cases) but paradoxically a drop in the total quantity of items seized (from 128 million to 79 million). Whilst it's difficult to spot long term trends as annual figures can be skewed by a few very large cases, these numbers reinforce our experience that counterfeiters are now less keen to send goods in large shipments and are increasingly turning to smaller consignments and postal traffic. Customs and rights holders need to adapt systems that worked well in the days of forty containers arriving at Rotterdam port, to deal with the multitude of smaller consignments now being utilised.

Working with customs, lobbying for better rules/regulations where required and lobbying for additional manpower (a tough ask at present!) has never been more necessary. And at a time when the World Customs Organisation has never been more committed to the fight, this could be the ideal time to seek to further engage with customs.

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Consumer-Oriented Brand Protection: No Charity – Just a Well-Calculated Business Strategy

Inga Daugeliene is the CEO of Dintag Corp. Oy

In spite of the huge efforts being undertaken by national and international anti-counterfeiting organizations, law enforcement agencies and regulatory authorities the seizures of counterfeit goods still count in thousands, while their worldwide sales count in millions of items and billions of dollars. Production of fakes has become a form of organized crime with its own experts specializing in production in the industrial sectors concerned, its own financiers, logistics experts, importers, wholesalers and distributors, right up to the end consumer.

This business is so profitable that the only effective way to stop it is to make it not economically worthwhile.

How? By enabling the end consumer to choose whether to buy, or not to buy.

Given a chance to tell an original from a fake, the consumer can finally refuse buying counterfeits – especially those raising health and even life hazards, like fake medicines, alcohol, tobacco, foods, perfumeries, car parts or toys.

Thus it is the billions of end-consumers who are the final decision-makers: by refusing to buy fakes they are in a position to undermine the whole idea of counterfeiting. The elaborate schemes and networks set up by organized criminal groups become useless: no demand, no supply.

Measures are being taken. Are they worth the investment?

Manufacturers are investing millions in investigations and raids on counterfeiters, building and prosecuting cases, devising systems and putting in place teams to increase their chances of at least controlling the growth of counterfeiting of their brands. They also turn for help to law enforcement – customs, police – and regulatory authorities.

Detection and detention of counterfeit goods has joined the list of customs functions in the last ten years, when counterfeiting got into gear and began to be taken seriously both by the IP right holders and authorities. Customs officers who still have to deal with 'good old' smuggling, drug, human and arms trafficking, etc, must now check thousands of items daily and try to recognize fakes within the huge cross-border flow of goods.

The manufacturers' anti-counterfeiting strategies are focused mainly on tracking and tracing the supply chain. They use costly and time-intensive tools based on sophisticated techniques – latent taggants, markers, machine-readable inks, DNA-based marks, micro-threads, etc., that can be 'seen' only with the help of special devices, like readers, scanners, microscopes. They also supply customs with lists of distinctive features that are meant to help tell a genuine product from a counterfeit. The question is: can a customs officer carry around a backpack of various devices and at each check of suspicious (or not suspicious) goods effectively use descriptions of products that cross the border in thousands of containers?

Moreover, the vulnerability of most existing brand protection systems is that all the information necessary to authenticate the product is contained within the protection means itself – which makes it easier for an evil-thinker to replicate these protection means. Thus, the wealthy and well-organized counterfeiter does not take long in catching up with the most advanced techniques and manages rather sooner than later to clone any sophisticated gadget.

The brand owner is unable to stop unfair competition from illegal trade sources – even well-protected 'civilized' supply chains are penetrated by counterfeiters. Besides, 'intra-corporate' measures do not protect from those fakes that enter the market from beyond the legal supply chain – through the Internet, so-called 'suitcase imports', street markets, abusive retailers and pharmacies, etc. Meanwhile, the unprotected end-consumer goes on buying fakes and ensuring profits not for the IP-right holder, but for the IP-right offender. The customs/police officer still does not have a reliable instrument to detect counterfeits. The procedure of obtaining legal evidence on counterfeit goods through specialized laboratories is

time-taking and costly – at the taxpayers' expense.

Core strategy: a reliable and simple brand protection technology

The market did not take long in responding to this gap between the needs of counterfeit-affected industries and their consumers. The solution was found – and it is to *divide* the protection means in two, and to place a part of the information necessary for authentication *not* on the product itself, but *separately*. Such systems are known as the "call-in-the-numeric-token", or CNT systems. The 'numeric token' – or an identification number – is located on the protection means, while the information related to this ID number is located in a database. This system enables any interested party to authenticate the product. This interested party can be the end-consumer (patient or doctor), the manufacturer, the wholesaler, the customs officer, or any other representative of a regulatory authority.

The ID number on the product is read with a naked eye and forwarded via a telephone or the internet to the database, which responds with the information necessary for the product authentication. The CNT approach allows the creation of a system that is counterfeit-proof – to fake a distributed system is actually impossible. The system should allow the *authenticator* himself to make a conclusion on the product authenticity – by comparing the information given out by the system to the information on the product being authenticated. If this information coincides, the product is authentic, and if not, the product is counterfeit. Along with being counterfeit-proof, in order to maintain fair competition, an effective technology should be inexpensive and easy to implement. It should allow minimal changes to manufacture process by using standard equipment and incurring minimal personnel training and minimal implementation time.

It is vital that an effective system be also cross-industry – that is, applicable on all kinds of products. The more unified the system, the less confusion for the users, the easier consumer education, the less time and expense on advertising.

Protected products gain marketing advantages over their competitors by enabling the consumer to make sure he is

buying the genuine product. And last but not least, through the use of such an online system the brand owner and/or law enforcer are able to receive reliable feedback from the consumers. The archived data on the checks executed through the system can be also used as evidence in court.

A unified authentication system would offer the same authentication procedure for all kinds of products, making it easily applicable by all stakeholders:

- End-consumers,
- Branded goods manufacturers,
- Manufacturers of parts & components,
- Manufacturers of materials & substances,
- Wholesale and retail distributors,
- Customs officers, other law enforcers,
- Regulatory authorities.

A unified brand protection system offering reliable authentication with the naked eye is the major 'missing link' in the struggle against counterfeiting. It is a mighty weapon – a Kalashnikov that can help join the effort and eventually put an end to counterfeits.

Equipping the stakeholders with an authentication instrument: a well-calculated business strategy

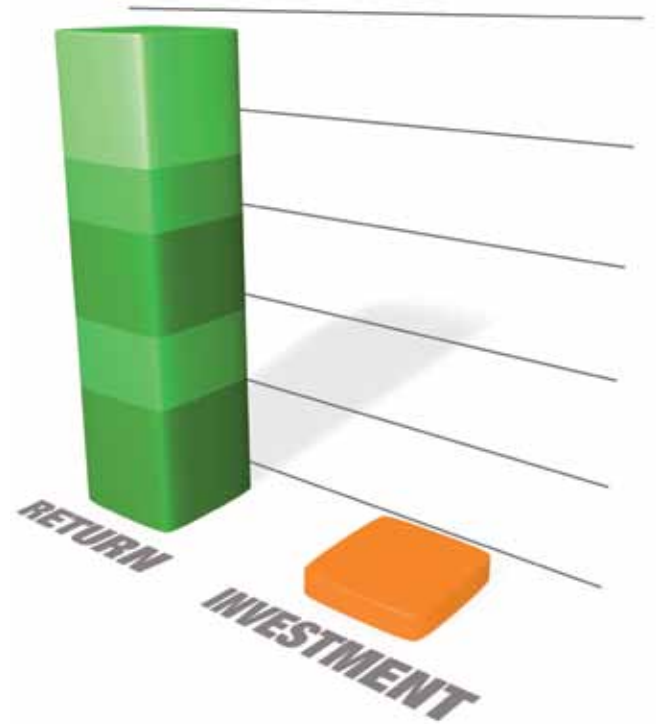
The main factors that can be used to calculate cost-effectiveness of implementing a consumer-oriented authentication system are given in the graph below.

As can be seen from the graph, the benefits for a branded goods manufacturer from implementing such a system would be as follows:

Royalty growth due to effective control of licensed production. By supplying protection marks (tags, labels) to the licensee, the brand owner ensures

WHERE IS THE MONEY?

- Royalty growth due to effective control of licensed production
- Increased company value due to the value of protected brands
- Elimination of the counterfeits' dumping price pressure
- Sales growth due to increased consumer trust
- Market share growth due to squeezing counterfeiters out
- Investment into consumer-oriented brand protection technology



that the licensee produces strictly the quantity of products as envisaged by the license agreement. Thus the brand owner ensures that his royalties are paid in full and that no “third shift” products will appear on the market.

Elimination of the dumping price pressure posed by counterfeit goods. The competitiveness of fakes is more often than not based on their low prices. Appearance of cheap fakes or lookalikes on the market causes brand owners to lower the prices for authentic products. Squeezing counterfeits out of the market will help carry out more flexible pricing strategies, free from outer pressures.

Sales growth due to increased consumer trust. Today the counterfeit goods (mostly substandard, low quality) deteriorate the brand by disrupting its image, its ‘promise of quality’. Once the consumer gets an instrument to tell an original from a fake, the producer or seller of fakes will be no longer able to deceive the buyer and cast a shade on the brand – be it newly born or well established.

Increased company value due to the value of protected brands. Brand is a complex of the consumer’s concepts and expectations concerning the branded product. The better consumer’s expectations are met, the higher the brand value and its contribution to the overall company value.

Due to all the above, there will be a growth in market share of protected branded goods.

Anti-counterfeiting strategy = anti-crisis strategy

The global financial crisis has hit most industries in most regions of the world. Production volumes are shrinking, people are losing jobs, and consumer spending is slowing down. Globalization leaves no stone unturned...

Meanwhile, another product of globalization, ‘the plague of the 21st century’ – counterfeiting – is coming to the forefront. Organized criminal groups producing counterfeits are not concerned with the banking crisis – as they do not keep their capital in the banks. Organized criminal groups producing counterfeits are getting an unprecedented chance to infiltrate the legal supply chain: while legal production is shrinking, distributors, wholesalers and retailers are looking for ways to maintain their profits. As a result, they are more willing than ever before to allow counterfeits, which are much cheaper than genuine goods, into their supply chains.

And this is where an anti-counterfeiting technology can help. Protection of branded goods through a technology that can be used by anyone, without any special skills or devices, with the naked eye, through widely-

available communications like the internet or mobile phone, is a mighty barrier to the penetration of counterfeits into the crisis-weakened market. A unified and widely available anti-counterfeiting technology can be a very effective tool against counterfeits.

In the current economic climate global companies seeking to cut costs are more motivated than ever before to transfer their production premises to third-world countries. And it is common knowledge that the main problem with remote plants – be they proprietary or licensed – is output volume control. The notorious ‘third shift’ has long been a headache for many brand owners manufacturing their products abroad.

And again, a technology based on marking each and every item with a protection means based on the CNT principle described above can help establish precise control over the production volume on licensed manufacturing facilities. A reliable instrument of production volume control allows safe production transfer to cheaper regions. This measure is effective in stable economic conditions (see the graph) – but currently it can become a crucial one.

Reliable instrument of production volume control allows safe production transfer to cheaper regions.

Conclusion

During all economic conditions the implementation of an effective brand protection strategy can mean an extremely satisfactory return on investment. Taking care of the consumer may be rewarded – especially when the consumer is turned into the main agent of getting back the markets lost to counterfeiters.

There are 6.5 billion consumers. Among them, there are millions prepared to check authenticity – especially of those products that raise health issues. There is little chance that even a counterfeiter would knowingly give his kids fake medicines or install a fake brake pad on his car.

There are also law enforcers who are in charge of detecting and seizing counterfeits – and their work efficiency would increase many times if they are given a simple instrument to check. There are lots of counterfeit-related cases in courts where the origin of products is so hard to prove.

Given an instrument to tell an original from a fake, we can all join the effort against counterfeits that have flooded our life. Given an instrument to tell an original from a fake, we can refuse buying those fakes, thus blowing up the very economics of counterfeit production. No demand – no supply. ■

Deploying Technology to Fight Counterfeiting

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Introduction

Counterfeiting and piracy have become high technology industries in themselves. The sophistication used to copy products often means that fakes are ostensibly identical to the originals. This presents a huge problem for all of the stakeholders; from the brand owner, through the supply chain to the end consumer.

More importantly the problem cuts across every sector causing specific issues in specific markets. Copied luxury handbags may not present a health risk to the end consumer, but the revenue generated from sales often promotes illegal child labour in third world countries¹. Fake apparel and sportswear may last just as long as the real thing, but almost certainly finances terrorist activity somewhere in the world². Then there are products that really do cause health and safety issues – from bogus car parts that can contribute to road accidents, fake wines and spirits that contain harmful ingredients, to counterfeit medicines that either provide no medication at all or give the wrong medication³.

When it comes to piracy; the copying of music, software, and other copyrighted media, the problem is compounded by the ethereal nature of the digital product⁴. Media can be replicated with various levels of quality, but in many cases up to the level of the original with relative ease. This presents its own technological challenges to overcome, as digital media can be supplied without packaging and without importation through a customs agency.

Despite the fact that public awareness of the problem is growing, few consumers or indeed employees of brands are fully conversant with the extent of the problem⁵. There are several contributory factors to this; the reluctance of many brands to discuss the problem for fear of losing trust and reputation within their consumer base, the difficulty in measuring the extent of counterfeits as they travel alongside legitimate products within the supply chain, and the fact that consumers are barraged daily with news and advertisements, and so any message about counterfeits barely peaks above the background noise. This lack of awareness can also make the effective implementation of a brand security technology more difficult, because some form of education or marketing is usually required to ensure that the technology is recognized and used properly.

A diverse problem

There are numerous published statistics about the extent of counterfeiting, and there are many organizations around the world attempting to combat the crime⁶. But it is always instructive to look at these facts and reflect on how technology might be deployed to have an effective impact on the problem.

Firstly, headline figures quoted by reputable sources such as Interpol, the World Customs Organization (WCO) and the International Chamber of Commerce (ICC) put the annual value of counterfeit goods as being equivalent to about 5-7% of world trade or (US\$500 to US\$650 billion)^{7,8}. This is a sizeable figure (more than the annual revenue of world's largest retailer Wal-Mart, which for the financial year ending January 2008 had sales revenues of just under US\$375 billion)⁹. As such, it would seem reasonable to make investments in sophisticated technology to reduce the problem. The difficulty many brand owners face is quantifying the losses so that they can gauge the likely return on such an investment.

Counterfeiting is also a rapidly growing industry, and has increased unabated for many years^{10,11}. The recent credit crunch and economic downturn may have adversely affected legitimate manufacturers, but there is evidence that this has fuelled trade in fake products. Partly because low cost fakes are more appealing to the cash-strapped consumer¹² and also because in this industry cash flow is governed more by criminal activity than lines of credit from high street banks¹³.

In the fashion industry, the impact of the problem is difficult to gauge because the argument goes that people who buy fakes would not usually buy the much-more-expensive genuine products. There is bound to be some element of truth to this, but ultimately, the lower cost fakes are being sold in lieu of mainstream products from lower-end brands, and so revenue is still being made illegitimately whilst taxes and duties are almost certainly being evaded¹⁴. Fashion and luxury is also a very broad market sector, with products including clothing, suits, shoes, sportswear, handbags, watches, perfumes, cosmetics and jewellery for example. The manufacturing and distribution practices for these different product

lines are also diverse and so universally protecting a brand, either with improved business practices or through the use of technology, can be a major challenge.

Looking at another very different sector by way of example, the Motoring Equipment Manufacturers Association (MEMA) in the US estimates that counterfeiting costs the global automotive parts industry US\$12 billion per annum with US manufacturers losing about US\$3bn in annual sales¹⁵. The problem has lurked in this industry for years and has not yet been satisfactorily addressed¹⁶. Much of the problem stems from the fact that cars require replacement parts during their life and the fitting of these is often trusted to workshops and mechanics, sourcing goods from a complex international supply chain. Moreover, parts range in shape, size and operating requirements which can present challenges when deploying a technological brand protection solution; particularly if it is to protect a part directly rather than the packaging.

Perhaps the most alarming market sector in which counterfeit goods are rampant is that of pharmaceutical and medical products¹⁷; to the extent that respected academic journals have also reported the problem^{18,19}. The World Health Organization (WHO) International Medical Products Anti-Counterfeiting Taskforce (IMPACT) is cautious in stating the size of the problem²⁰, although in the past the WHO has reported estimates of as much as US\$35 billion of counterfeit medicines being sold globally per year. The medical supply chain is complicated; local legislation in different territories requires repackaging and relabeling, and in recent years the sale of medicines over the internet has rapidly increased. All of these problems present serious difficulties in preventing fake products entering a market, and unfortunately it is the developing countries with malaria, AIDS, and relatively poor healthcare in general that suffer the most from the scourge.

More information, resources and news about counterfeiting in these and other sectors is available at the BASCAP website (www.bascap.com) and at the No to Fakes website (www.notofakes.com).

Deploying technology

Brand owners and manufacturers have often resorted to technology involving marking their product packaging to try to thwart the menace of counterfeiting. Probably the most common and most overt technique is the use of a hologram, once a high-technology solution that was deemed difficult to replicate. Today, holograms and similar optical-effect labels can be reproduced passably and with relative ease, and counterfeit products have even sported holograms where the original does not!

This fact provides an insight into a major issue relating to counterfeit prevention. The consumer is difficult to educate, and highly unlikely to tell a genuine hologram from a crude imitation. Not only that, but to a consumer, holograms are synonymous with security so counterfeiters can leverage this understanding to sell more product.

Engineering components and spare parts have often relied on serialization to provide some level of counterfeit protection. This is particularly so in the aviation industry; the argument here being that individually numbered items will have a paper-trail of traceability demonstrating the pedigree of the part. However, copying and altering numbers is a relatively straightforward task, even when they have been shot-peened or laser marked using capital-intensive equipment. This results in confusion, as the original and fake with the same serial number cannot easily be distinguished and depending on which one gets checked first, a fake may pass into use ahead of the genuine one.

Radio-frequency identification (RFID) is the latest way to serialize items; making use of a silicon chip to store the unique number and in some cases additional information. However, RFID is not without its problems; it is still relatively expensive compared to simple numbers and barcodes, it comes in a variety of formats with very different levels of security, clones can be made to broadcast the same number, and in some instances the metallic or liquid environment makes RFID unreliable. However, RFID is here to stay as a logistics tool, and certainly helps raise the hurdle of counterfeiting. Used alongside other security technologies, it can be a very powerful tool.

When a brand owner considers a technology for brand protection, many questions need to be addressed, as illustrated in Exhibit 1. The strategy needs to be considered throughout the supply chain and the product

lifecycle. A risk analysis needs to be conducted on how and when products should be authenticated, but it also needs to address the necessary action if an authentication fails. At the end of a product's life, there must be no danger that the security feature can be unscrupulously reused on an illegitimate product.

In addition, the brand owner needs to know if a solution should be used in isolation or as part of a layered security system. Money and passports, for example, have long been issued with multiple layers of security; because if one layer is compromised, there is a strong likelihood that others will remain intact. There are also different solutions for different types of authentication: the look and feel of the banknote is often enough for a consumer to be confident that the money is genuine; the shopkeeper may resort to ultraviolet light to verify a watermark; whereas a bank will use other machine readable technology to provide yet higher levels of confidence in the process. The same approach should be used to protect products.

The next step is to consider the means of authentication at each level; particularly if human observation is to be relied upon (usually less expensive in terms of equipment out in the field being unnecessary, but certainly less secure as consumers and officials alike are easily duped). Where a reader is to be deployed, whether it is a simple "filter" to change the appearance of a genuine label or a more sophisticated scanner to read a tag, consideration needs to be given to the cost and the location. Verification at the actual point of sale is usually the most powerful approach, but the vendor needs to be incentivized and the consumer needs to expect it as part of the service. Exhibit 2 highlights some of the considerations and drivers that exist along a supply chain.

As such, one of the principal hidden costs in the use of any technology deployed to thwart counterfeiting is in educating the consumer to know what to expect and how to discern genuine products from fake. Brand owners often overlook this fact, and sophisticated technology may provide a disappointing return on investment if an education plan has not been rolled-out in parallel.

The specific requirements of different sectors also challenge how a technology might be successfully deployed. For example, fashion items are often limited editions or bespoke products made using high-quality materials in novel and distinctive designs. The product range is often diverse and delivered in a high mix of low volume. The anti-counterfeiting technology must not impact on the aesthetic design of the item, whilst still providing a means of security that can ideally be authenticated by the consumer. Genuine fashion items often become collectables, and although the brand owner may not wish to promote resale, an authentication technology that can last the lifetime of an item brings value to the end-user and ultimately respect for the brand. Analyzing these different drivers helps to establish where value is likely to be perceived in a deployed system. Ideally, value needs to be derived at each point in the supply chain, as highlighted in Exhibit 3.

Spare parts are usually carefully engineered to work in aggressive environments. For example, replaceable items like gaskets, plugs, filters and pumps might need to operate at elevated temperatures, in high humidity or in oily conditions. This is not just the case for cars, but also for public transport, aircraft, industrial applications such as power stations, in refrigerators, etc. Brand owners often make most of their revenue on after-sales servicing, and so there is a need to protect the supply chain to safeguard business as well as the reputation of the brand. As such, brand owners will realize that a suitable technology often needs customization to work favourably with the nuances of a particular product.

For pharmaceuticals, the primary packaging (such as the blister pack) is the most useful part to protect, because outer cartons are often replaced

in different markets to cater for differences in language and label legislation. Some technologies even exist to directly mark the tablet, but there are limitations as to the ease of verifying such markings in the supply chain. However, another consideration is the sheer volumes of products that are produced each year. A suitable anti-counterfeiting technology needs to be cost-effective for very low-cost but high-volume items. Protecting the high-end medicines is not enough, because even low-cost generic painkillers such as Aspirin are found to be lucrative products for counterfeiters.

Materials solutions and an integrated approach

A powerful approach to brand protection is through the use of materials and chemicals to provide the equivalent of a "fingerprint" or "DNA" for a product. A number of techniques have been researched and developed to achieve this, including the use of the unique fibre arrangements in paper²¹ and packaging²² and the use of composite materials²³. As a result, these technologies can be deployed in the form of a label, tag or by embedding the identifier in the product itself. Often these technologies work synergistically with serial numbers, barcodes and RFID chips, because the ease of reading a number helps make the authentication step quicker. This is analogous to checking a passport photograph in a database by first using the passport number as an index to find the correct entry quickly.

The power of this approach is that each product then has its own unique identifier, often constructed from very small and complex features, such that they are prohibitively difficult to reproduce. Ideally, the arrangement of the features is left entirely to nature and not directed by a predefined pattern, mask or design. If the features being measured are invisible (rather than being optical features), then the standard tools for photocopying or lithographically reproducing the "fingerprint" do not apply, and this raises the bar to duplication yet further. As the size scale drops in to the micrometer and nanometer regime, so the security rises yet further.

Solutions such as these are often fully integrated with a remote database so that the original "fingerprint" can be verified against one read later in the supply chain. This has become possible because telecommunications links are now widely available in the form of the internet, wireless connectivity and mobile phone systems. This means a remote database can be contacted quickly and inexpensively so that not only the authenticity of a product can be checked, but additional information such as expiry date can also be disseminated. This brings value beyond anti-counterfeiting, because if embraced by the supply chain, it also provides track and trace information that can improve efficiency and lower costs in other areas.

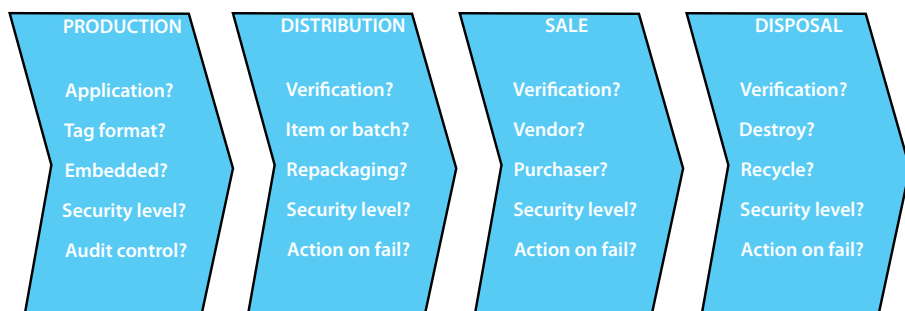
Exhibit 4 illustrates the concept, showing the components of this kind of high-end brand security technology. The product is protected with a tag, a scanner authenticates the tag and takes away any subjectivity of the authentication process, and a database not only provides authentication information, but also a fully updated audit trail capable of disseminating information in real time.

Outlook and conclusions

Deploying ever more sophisticated anti-counterfeiting technology is likely to be the only near-term solution to reducing the prevalence of fake products. Moreover, these solutions will need to be fully integrated to enhance security as well as bring value to each stakeholder in the supply chain. Because counterfeiting affects virtually all product sectors, and different products have specific forms, modes of use and customer expectations, the technology to provide the brand security is likely to require some level of customization to be effective.

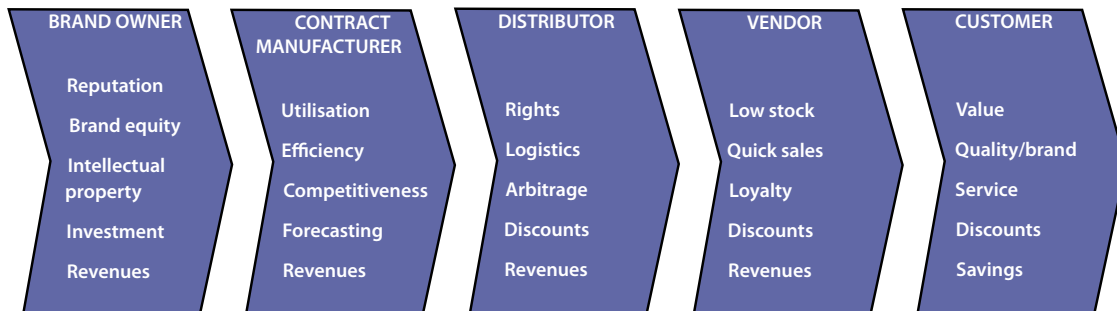
The author (adrian.burden@singular-id.com) acknowledges his colleagues at Bilcare Technologies for input and discussion during the writing of this article; particularly Peter Moran, Praful Naik, Raman Nanda, and Jessica Williams. For more information please visit www.singular-id.com

EXHIBIT 1



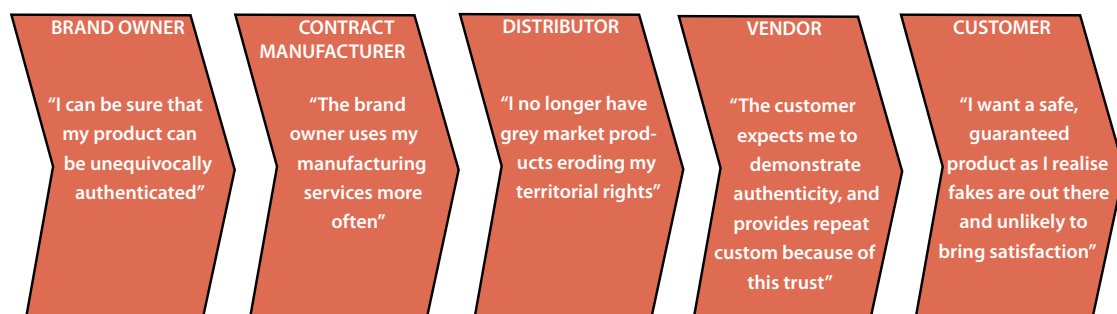
Some of the questions relating to how a deployed brand security technology should be used and moderated throughout the product lifecycle.

EXHIBIT 2



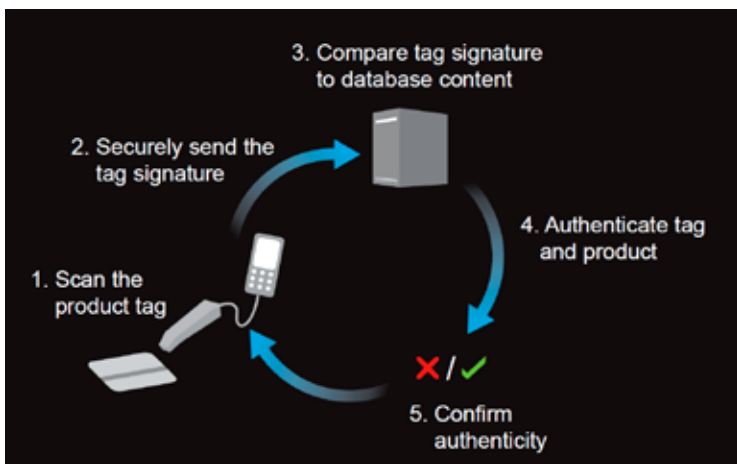
Some of the drivers and considerations of the parties across the supply chain. Unfortunately, many are in conflict with the notion of full-priced genuine products being preferential to lower cost fakes, and few encourage an authentication step.

EXHIBIT 3



Identifying the value an anti-counterfeiting solution brings to each stakeholder is paramount. Often there is a need to offer more value than simply 'anti-counterfeiting', such as supply chain management, warranty management or preventing product diversion.

EXHIBIT 4



Making use of a scanner and remote database to authenticate a materials-based "fingerprint" and prevent the counterfeiting of products.

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Energy Efficiency – The Invisible Solution



Scott Petersen is Marketing Director – Energy Solutions at Honeywell Building Solutions, Europe, Middle East, Africa and India

It is almost universally agreed that climate change is making an impact on the world we live in and action is needed to mitigate its potentially harmful consequences. So far, governments, companies and individuals have tended to focus on 'supply side' initiatives to reduce carbon emissions, promoting a "greener" way of generating electricity – primarily through renewable and nuclear sources – in hope that it will have less of an impact on the environment. The notion has caught on so well that EU member states have recently agreed to increase the renewable energy component of the EU's energy mix to 20% by 2020.

However, the greenest energy is the energy you don't use in the first place. Reducing energy consumption - or the demand for energy - reduces the total amount of required power generation capacity and the corresponding carbon and other harmful greenhouse gas emissions it produces.

Today, Europe collectively represents 17% of total global energy consumption. Although this is less than the US, which at 22% is the world's largest energy consumer, Europe still ranks significantly high as the second-largest energy consumer globally, surpassing China in third place by three percentage points. And of this, more than half of Europe's energy is consumed in the developed countries of North Western Europe.

Perhaps surprisingly for many, the overall demand for energy in Europe will continue to grow - despite the clamour around the negative impact of climate change. According to a recent energy-demand study conducted by the McKinsey Global Institute, the demand in Europe will grow by an average 1.2% a year to 2020, without any changes in current policy. This is less than the global demand increase figure of 2.2% a year but because developed nations have more services than industry in their composition, Europe already starts from a higher baseline than the global average. So in practical terms, this means we could see energy demand increasing by nearly a quarter by 2020.

The need to curb energy consumption has been flagged as a pressing issue by the European Commission. This is highlighted by Europe's poor energy efficiency performance where EC estimates indicate that European countries currently waste at least 20% of the energy they use. Consequently, the European Action Plan was drafted to set Europe's Energy Efficiency target to a 20% saving by 2020 in order to specifically negate this waste. This equates to a saving of more than €100 billion and around 780 million tonnes of CO₂ a year by 2020. However, while the intentions may be good, this initiative is not a binding target and is reliant on member states taking individual action. This raises questions as to whether the target will actually be achieved by 2020.



The opportunity lying in Europe's buildings

In the European Community, buildings account for 40% of all carbon emissions and of this, commercial buildings account for a third. In financial terms, the 20% inefficiency figure equates to an astounding €270 billion wasted every year in buildings through a lack of basic energy efficiency measures and poor energy efficiency habits by the occupants.

Despite the current downturn in the construction industry and a slowing in the number of new buildings, energy demand is still predicted to grow by 1.2% per annum and in the absence of reduction measures will increase 53% on a compound basis by 2030.

So, if we are to address this major issue where should we focus to get the biggest 'bang for our buck' and who should lead by example?

Take, for example, the UK's National Health Service which is responsible for

3% of England's total emissions. Its environmental impact is equal to that of a small country. But building new, energy efficient hospitals won't solve the problem. In fact, focusing most of our efforts on new build should be viewed as a distraction.

While building more economically-friendly buildings will obviously contribute, they will represent only a small percentage of Europe's overall building stock. As a result, new 'green' buildings will only tackle around 10% of the challenge. Retrofitting existing buildings is the real solution that will address energy inefficiency.

Europe's leaders have agreed to carbon emission reductions of at least 60% by 2050, and recently the UK's Climate Change & Energy Secretary, Ed Miliband, committed the country further by raising this to 80% by 2050. If this target is ever going to be met, governments need to be aware that 80% of the buildings we will be occupying in 2050 are already standing today and, on top of this, 90% of the targets can be achieved now by retrofitting these buildings using existing technologies.

The role of legislation

And governments need to take a lead as market forces alone will not address the challenge of reducing the 20% of energy we waste every year. The public sector is responsible for around 7% of European electricity consumption and so is a good area to focus on and provide a lead. But are public sector buildings a good target?

On October 1 2008, under the Energy Performance in Buildings Directive, most public buildings over 1000m² in the UK were required to have a Display Energy Certificate which provides a rating of the actual energy performance of the building. This is the A to G energy rating that you see on electrical appliances. Of the first 3,200 public sector buildings assessed, a quarter were rated either F or G. And this wasn't just old buildings. The Imperial War Museum built in Salford in 2002 has the same rating as its sister museum in London which was built in 1815!

A second piece of relevant new energy legislation is the Energy End Use and Energy Services Directive which commits EU member states to reduce energy consumption by 1% per year by 2016. The same legislation has tasked the public sector to take a leading role to promote and deploy this initiative. Their challenge looks daunting but the good news is that energy efficiency solutions do exist.

Where should you focus?

Where can organisations focus their efforts to achieve their energy efficiency targets and make the biggest impact?

The International Energy Agency, the IEA, estimates that for every euro spent reducing energy demand, two euros of investment in new energy supply plant and infrastructure is avoided. Recent research has also found that investing in energy efficiency delivers greater carbon reductions and a better financial return than investing in renewable energy generation.

However, we still need to battle the perception that supply-side energy management is a more tangible investment. After all, you can see a

wind turbine, you can touch it and you can see the blades turning and generating energy. In contrast, demand-side management – or specifically energy efficiency measures – is often called the invisible solution as improvements are on an individual basis and tend to be small or fragmented. Amory Levins, cofounder and chairman of prominent US based non-profit research organisation the Rocky Mountain Institute, says that "increasing energy end-use efficiency is generally the largest, least expensive, most benign, most quickly deployable, least visible, least understood, and most neglected way to provide energy services". New energy efficient lamps still light the office just as the inefficient ones did.



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One area of differentiation though is that demand-side energy management is a saved overhead which contributes straight to the bottom line. Even though the improvements on an individual basis are small and fragmented, collectively they can make a huge difference to the business outcome.

Energy efficiency solutions exist today

There are many solutions that individually address energy efficiency concerns but few can address it better as a single solution than Energy Performance Contracting (EPC). Energy Performance Contracting has actually been around for many years but it's still relatively new in Europe. It's recommended explicitly in the Energy End Use and Energy Services Directive as a measure that the public sector should use to meet its 2016 energy reduction target and overcome funding issues. But, to date, most government departments including those responsible for implementing the Directive don't know what EPC is! It's not surprising that EPC is not well known or promoted throughout the public sector.

EPC is used extensively in the USA and is the preferred process promoted and implemented by the Department of Energy (DOE) to curb its annual \$17 billion energy bill. In fact at the end of December 2008, the DOE announced the award of 16 EPCs that could result in up to \$80 billion in energy efficiency, renewable energy, and water conservation projects at federally-owned buildings and facilities.

In late November 2008, European Commission President, Jose Manuel Barroso, issued the European Economic Recovery Plan, which was a tool box of recommendations that included addressing energy efficiency in buildings and specifically called on member states to "urgently implement measures such as energy performance contracting".

Energy Performance Contracting has specific advantages

We have seen that most buildings have the scope for improvement. Current building owners are wasting 20% of the energy they purchase - money that is escaping out of windows, radiating from badly insulated pipes, lost in poorly performing plant or by reckless habits such as lighting unoccupied rooms.

Energy Performance Contracting is a collective solution that looks to make use of this wasted money and adds a financial element that enables building owners to upgrade their buildings with modern, reliable and energy efficient technologies without the need for up-front capital. Improvements, upgrades or retrofit work are funded by the projected energy savings guaranteed by the Energy Services Company (ESCO) installing them.

The innovative aspect - and key benefit - of Energy Performance Contracting is that if the ESCO doesn't deliver on the required savings, they pay the difference and if they exceed the target saving, the customer takes the surplus. This means that all operational and financial risk is transferred to the ESCO. It's an elegant solution that ensures whilst energy targets are delivered, the building owner's funding and risk issues are overcome.

But more than a funding model, it is a programme that includes practical, engineered energy efficiency measures that are implemented in buildings to deliver real energy savings. Measures can include optimization of heating, lighting, controls, HVAC and building fabric improvements.

In summary, Europe is a major energy consumer and buildings are a major contributor to energy waste. If we address their inefficiency using practical and collective solutions on the demand side, such as energy performance contracting, we can make a major impact on reducing carbon emissions, reducing energy costs, meeting legislative targets and making buildings comfortable environments to visit, live and work in.

As McKinsey & Company quotes in its report 'Pathways to a low-carbon economy', published in January 2009, "It is one thing to have the potential to make deep cuts in Green House Gas emissions; it is another for policy makers to agree on and implement effective emission reduction policies, and for companies, consumers and the public sector to take action to make this reduction a reality".

Solutions and companies that offer the solutions already exist so if the will is there, the way is sure to follow. ■

OECD Draft Notes About Comparability and Transactional Profit Methods

Oliver Wehnert is a Partner at Ernst & Young AG, Germany

Introduction

The OECD released the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (hereinafter referred to as "the TP Guidelines") in 1995. Monitoring the implementation of those guidelines is one of the OECD's responsibilities. If economic developments and especially the practical experiences gained in applying the TP Guidelines require an update of those the OECD takes action. Against this background the OECD called the business community's attention to two inherently linked areas, namely comparability issues and the application of transactional profit methods (ie. the transactional profit split methods and the transactional net margin method). In both areas the OECD invited the business community and countries to comment on a series of notes¹. Recently, in November 2008, both were invited by the OECD to a consultation on comparability issues and the application of the transactional profit methods².

This article will discuss selected OECD Draft Notes³ referring to comparability and transactional profit methods and thus provide an update on the TP Guidelines' development in those areas. Additionally the positions Ernst & Young (hereinafter referred to as "E&Y") took in its responses referring to the single notes are summarized from time to time. For further and detailed information about all OECD Draft Notes please refer to E&Y's comments on the respective notes⁴.

Comparability

The 2006 OECD Draft Notes on comparability identify and discuss a wide range of practical problems that taxpayers and tax administrators have encountered when applying the current TP Guidelines in their comparability analysis. The OECD Draft Notes document attempts to address these issues by suggesting more detailed analysis or proposing further guidance on the application and/or selection of the most appropriate transfer pricing method. In the following a range of important OECD Draft Notes shall be discussed.

Note 1: Putting a comparability analysis and search for comparables in perspective


According to this Note the primary drivers for conducting a comparability analysis are for taxpayers to determine how transfer prices should be established and for the tax administrations to determine whether the chosen transfer prices need to be adjusted. The comparison required in Article 9 of the TP Guidelines is a comparison of conditions that is broader than merely comparing prices and margins. However, according to this Note many tax administrations and practitioners are relying primarily on a comparison of prices or margins in order to determine the arm's length nature of a transaction.

Although transfer pricing comparability analysis cannot be reduced to a mere search of comparables, the common practice of both tax administrations and multinational enterprises to conduct mechanical comparisons of financial indicia only, cannot be ignored. This behaviour is understandable given the difficulties and costs associated with obtaining information on independent companies engaged in comparable transactions. To illustrate this, taxpayers often question the point of a detailed analysis of the related party transaction, in particular the intercompany terms and conditions, when nothing like the same information is available to evaluate potential third party comparables.

In its response E&Y thus emphasized the importance for the TP Guidelines to recognize these practical difficulties and the costs associated with comparability analysis and identify, evaluate and provide guidance on alternative analytical frameworks that can be used when reliable comparables are not available.

Note 2: Determination of and making comparable adjustments where appropriate

Although the current TP Guidelines stress the need to adjust comparables



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in order to improve comparability, the particular circumstances under which such adjustments should be made and how such adjustments should be calculated has been unclear.

Even when such adjustments can be reliably made and will improve comparability, application of the current TP Guidelines can raise residual concerns that such adjustment may be inappropriate where the adjustments are either relatively large or small. Additionally, comparability adjustments should only be considered where they can be expected to increase the reliability of results.

Note 3: Internal comparables

Consistent with the “natural hierarchy of methods” and the presumed better reliability of information, the current TP Guidelines appear to indicate a general preference for the use of internal comparables over external ones. Although there is a strong bias for the use of internal comparables, the search for potential internal transactions should be limited to the parties involved in the transaction and to other members of the multinational enterprise having substantially similar transactions (volumes, products etc.) with third parties in the same or similar markets.

Note 4: Determination of available sources of information and their reliability

The current TP Guidelines recognize the difficulties taxpayers and tax administrators often have receiving adequate information to apply the arm's length principle.

Although the issues associated with the use of limited and asymmetric information are well recognized, the discussion of this issue in the OECD Draft Notes appears to be unbalanced. While it suggests that taxpayers should not use private information, tax authorities using secret comparables are simply encouraged to apply safeguards.

E&Y believes that the OECD should roundly reject the use of non-public domain information that is not equally available to taxpayers and tax authorities.

Note 5: Multiple year data

The current TP Guidelines provide little guidance to how multiple year data should be used in a comparability analysis.

There is discrepancy in approaches related to the use of multiple year data for transfer pricing analysis. Particularly the question arises whether it is the purpose of multiple year data to gain a better understanding of the controlled transaction and the use of that data for statistical purposes or to smooth results. Thus, further definitive guidance should be provided as to when, and how, the use of multiple year data would be appropriate in a comparability analysis. Such guidance should particularly include settlements about circumstances in which multiple year data, including subsequent year data, may be appropriately used in a comparability analysis and about how to multiple year data should be used (eg. screening of comparables, setting a range or both?)

Note 6: Definition of the arm's length range, extreme results, methods to enhance reliability, loss-making comparables

Since transfer pricing is not an exact science, there are many occasions when the application of the most appropriate method or methods produces a range of results. The current TP Guidelines do not provide adequate guidance as to how to address the selection of the most appropriate point(s) in a comparable range.

The OECD Draft Notes identify comparability considerations in relation to extreme results, approaches to enhance reliability of the arm's lengths range and loss making comparables.

Transactional profit methods

Having received an impression about the TP Guidelines' status quo referring to comparability issues it is to conclude that the current TP Guidelines provide relatively little guidance about comparability issues. Thus, in this regard, it is important to provide the business community with some clarity. As indicated in the introduction, the OECD focuses on updating both, parts of the TP Guidelines related to comparability issues and parts of the TP Guidelines related to the application of the transactional profit methods. Therefore, in the following the contents of the OECD Draft Notes regarding transactional profit methods shall also be described and briefly discussed.

Note 1: Review of transactional profit methods: status as last resort method

In the TP Guidelines, traditional transaction methods are regarded as preferable to other methods. Transactional profit methods are described

as last resort methods and its use should be limited to those exceptional situations where no data is available or where the available data is not of sufficient quality to rely solely on the traditional transaction methods⁵. However, since the publication of the TP Guidelines in 1995, an increasing number of countries indicates that in practice transactional profit methods are being used in far more cases than would be expected from their last resort status. The 2008 OECD Draft Notes propose that the exceptional status of transactional profit method should be replaced by an approach using the most appropriate method in a particular case. As it is often not possible to apply the traditional transactional methods this approach reflects the practical reality of implementing the arm's length principle.

E&Y believes that abolishing the exceptional status of transactional profit methods and introducing a “most appropriate method” analysis is a welcome step towards the alignment of the TP Guidelines with the practical realities of implementing the arm's length principle.

Note 2: Use of more than one method - “sanity check”

This note reaffirms the existing guidance that the application of more than one method is not required although it might be useful in some cases. Additionally the note explores circumstances in which the application of a transactional profit method together with a traditional transactional method may be useful. Finally the use of a “sanity check” is discussed to verify the primary method's results.

In its response, E&Y recognized that applying a transactional profit method to corroborate or “sanity check” the results of applying a transactional method is helpful, particularly for large and complex transactions. However, E&Y argued that applying multiple methods should not be required.

Note 3: Access to the information to apply or review the application of a transactional profit method

This note considers two points relating to the difficult question of information availability. First it considers requests by the tax administration for information on a foreign associated enterprise for the purpose of reviewing the application of a transactional profit method and, particularly if tax authorities should be able to request more information than would be available to the domestic entity if the parties were unrelated. Secondly, this note considers requests by tax authorities for information on management or cost accounting.

It is understandable that tax authorities need, within reasonable limits, to have access to qualitative financial information to the extent that this is necessary to review the application of a transactional profit method. The OECD Draft Notes recognize that access to information may not always be needed and that there are practical issues concerning availability. Further it is understandable that segregated accounting information and information on cost allocation is often necessary to successfully review transactional profit methods.

Note 4: Application of transactional profit methods and unique contribution

This note considers when a transactional profit split method is appropriate in cases involving unique contributions and how to apply the transactional profit split method in such cases. Further it considers when the transactional net margin method (“TNMM”) may be the most appropriate method and discusses the use of TNMM to price a license fee for an intangible.

Further discussion is needed about how to implement the transactional profit split method. Particularly a consensus is needed on how to deal with very complex cases with multiple non-routine contributions for which no obvious objective allocation key exists. Due to limited information available on royalty rates for third party transaction, it is inevitable that TNMM will play an important role in settling license fees when only one party of the transaction is making a non-routine contribution.

Note 5: Application of the TNMM: standard of comparability

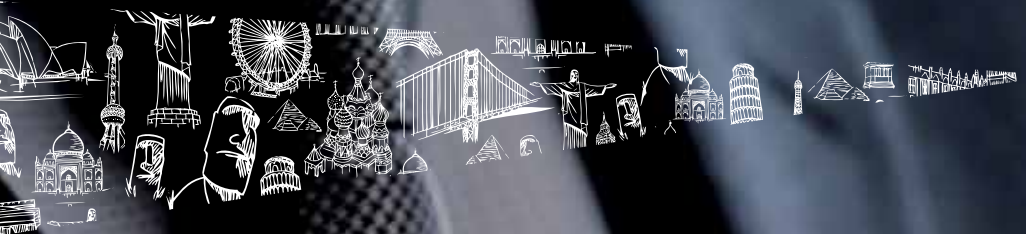
This note considers comparability issues in relation to the application of TNMM including the use of company wide data to generate financial benchmarks.

In its response, E&Y recognized that when the traditional transactional methods cannot be reliably applied and only one party is making a non-routine contribution, TNMM is likely to be the most appropriate method. In applying TNMM reasonable endeavours should be used to undertake comparability analysis. However, it must be recognized that only limited information is often available. If comparability standards are set too high, no OECD method will be capable of being reliably applied.

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Closing remark

As indicated and discussed above the current TP Guidelines provide little guidance about comparability issues and little consideration of the practical relevance of transactional profit methods. Against this limited clarity and little consideration the concluding words of Ms de Ruiter, heading the working party being responsible for the TP Guidelines, at the end of the OECD's recent consultation with the business community shows promise and shall be quoted to conclude this discussion: "...we had a very constructive dialogue about what the practical implementation

of the arm's length principle, of the comparability standard and of the rules for selecting and applying a transfer pricing method mean for taxpayers and tax administrations... The finalization of the guidance will require a delicate balance between a theoretically sound framework and workable guidance on application..."⁶ Additionally, a balance instead of further division of the positions of the two major stakeholders being the taxpayer and the tax administration exercising the TP Guidelines is highly desirable and thus should generally be considered in any update of the TP Guidelines. ■

1. OECD, *Comparability: Public Invitation to Comment on a Series of Draft Issues Notes*, May 10, 2006, available via <http://www.oecd.org/dataoecd/59/38/36651642.pdf> and *Transactional Profit Methods: Discussion Draft for Public Comment*, January 25, 2008, available via <http://www.oecd.org/dataoecd/18/48/39915180.pdf>.
2. <http://www.oecd.org/dataoecd/27/40/41689023.pdf>.
3. "Selected" refers to those OECD Draft Notes which were primarily discussed at the OECD Consultation Meeting on Comparability and Transactional Profit Methods in Paris, November 17 and 18, 2008. Hence the number and order of the OECD Draft Notes subject to this discussion may not be in line with the number and order of the OECD Draft Notes subject to the respective discussion draft.
4. Referring to Comparability: <http://www.oecd.org/dataoecd/54/40/37859809.pdf>, referring to Transactional Profit Methods: <http://www.oecd.org/dataoecd/11/27/40580595.pdf>.
5. TP Guidelines para. 2.49, 3.49, 3.54.
6. http://www.oecd.org/document/49/0,3343,en_2649_33753_41697585_1_1_1_100.html.

Islamic Finance Securitisation in Luxembourg

Vassilijan Zanev is a Senior Associate at Loyens & Loeff Luxembourg

Islamic finance constitutes one of the fast-growing fields in today's global financial markets. The involvement of Islamic investors in the securitisation industry and the development of Shari'a compliant securitisation transactions during recent years is an affirmation of the success of the marriage between securitisation and Shari'a compliant finance. Several Islamic securitisations have been implemented in Luxembourg, which has gained recognition as an international securitisation and structured finance hub.

Islamic securitisation follows the same principles as the conventional securitisation. However, several restrictions arising under Shari'a principles will apply, notably the prohibition of interest ("riba") and speculation, the exclusion of the industries involving alcohol, pork and gambling, etc. As Islamic finance rules prohibit interest-based financing, investors are allowed to support or invest on the basis of partnership, but not on the basis of interest.

It has now been almost five years since the law of March 22, 2004 on securitisation (the Securitisation Law) was adopted by the Luxembourg parliament, creating a flexible, lightly-regulated and tax-efficient regime for securitisation vehicles (the SVs). Alternatively, the investors may opt for a non-regulated ordinary commercial company (ie., what is often referred to as a *société de participations financières* or Soparfi). Both regimes have offered solutions suitable for Islamic investors.

Nature of Islamic securitisation and sukuk

"Sukuk" is the Arabic name for a financial certificate and can be analysed as the Islamic finance equivalent of bond. However, interest bearing instruments are not permitted and there cannot be a guarantee on fixed return. Sukuk is a kind of asset-backed security representing a common share in the ownership of the investment assets. The sukuk holders share the return generated by the sukuk assets and bear the losses in proportion to the certificates owned by them. Unlike conventional securitisations, Islamic securitisation and sukuk will require a higher connection with the securitised assets.

Securitisable assets

The collateral which is securitised in conventional securitisations comprise frequently of interest-bearing receivables and debt securities. Islamic finance does not permit the use of interest and as a consequence, interest-bearing assets would not normally be eligible for an Islamic securitisation. Shari'a compliant assets would include real estate, equity participations, ijara and murabaha contracts.

One of the driving factors of the popularity of the Securitisation Law is the wide range of eligible assets (other than interest-bearing assets) which can be securitised. Under the Securitisation Law, risks relating to the holding of assets, whether movable or immovable, tangible or intangible, as well as risks resulting from the obligations assumed by third parties or relating to all or part of the activities of third parties, may be securitised. During recent years the securitisation transactions in Luxembourg included diverse asset classes, such as residential loans, lease receivables, equity participations, real estate, commodities, whole businesses etc. Since March 2004, the use of Luxembourg SVs with a view to the securitisation

of real estate have become increasingly popular.

In its 2007 Report, the Luxembourg Supervisory Commission for the Financial Sector (the CSSF) clarified the legal environment applying to SVs, by accepting inter alia:

(a) the possibility to securitise and repackage shares or units in UCIs, hedge funds, limited partnerships or other companies holding the securitised risks, provided that the SV is not actively involved in the management of the entities in which it has a participation (direct or indirect), and the SV does not provide services of any nature to such entities;

(b) the possibility for an SV to acquire goods or equipment and to make them available to an operational company against the payment of a rent, provided that such transaction is structured in a way similar to a leasing operation and that its purpose is the financing of the operational company.

Structuring

The Securitisation Law provides a high degree of structuring flexibility and a lightly-regulated regime. Luxembourg SVs are unregulated entities and are not subject to any authorisation. Only SVs issuing securities to the public on a continuous basis must be approved by the CSSF.

The acquisition of the securitised risks by a Luxembourg SV has to be financed through the issuance of securities (*valeurs mobilières*), the value or yield of which is linked to such risks. Both equity and debt securities may be issued in bearer or registered form. However, interest-bearing securities, as used in conventional securitisations, are not allowed under Shari'a. Sukuk shall represent a common share in the ownership of the investment assets. The holders have to share the return and bear the losses in proportion to the certificates owned by them.

A Soparfi and an SV can be formed as a corporate body having a legal personality separate from that of their investors, whereas an SV may in addition be organised as a co-ownership of assets (without legal personality) - a so-called securitisation fund. The Soparfi and SV acronyms do not refer to specific legal forms, but merely to a specific set of legal, regulatory and tax provisions with the actual securitisation entity being formed either as: (a) a public limited liability company, (b) a private limited liability company, (c) a partnership limited by shares, (d) a cooperative company in the form of a public limited liability company, and (e) solely in respect of an SV, a securitisation fund. An SV formed as a corporate body or a securitisation fund may be compartmentalised, meaning that each compartment represents a distinct part of the assets and liabilities of the SV.

The securitisation fund deserves special attention. It is organised as a co-ownership, the joint owners of which are only liable up to the amount they have committed or contributed. The securitisation fund does not have legal personality and has to be managed by a Luxembourg-based management company in accordance with its management regulations. It may also be set up under a fiduciary arrangement, whereby the assets are being held by a fiduciary for the account of the investors. Given that securitisation funds constitute co-ownership(s) of assets, they provide a

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higher connection to the securitised assets and easily ensure compliance with Shari'a principles.

A securitisation fund governed by the Securitisation Law is transparent for tax purposes and will not be subject to corporate income tax, trade tax or net wealth tax in Luxembourg. Distribution of profits is not subject to Luxembourg withholding tax (except distributions falling within the scope of EC Savings Directive). Due to the lack of legal personality of the securitisation fund, investors may, where applicable, in principle (directly) claim treaty benefits from the jurisdictions in which the securitised assets are located.

A corporate type SV is subject to Luxembourg corporate income tax and municipal business tax. Obligations (engagements) vis-à-vis its investors and other creditors ((future) dividends, interest, etc.) are considered to be deductible "interest payments" for income tax purposes. The SV is exempt from the annual net wealth tax. Payments of dividends or interest are not subject to withholding tax (except payments falling within the scope of EC Savings Directive).

Listing of Sukuk

The Luxembourg Stock Exchange (LuxSE) is one of the key European stock exchanges for sukuk listings. The LuxSE announced on March 13, 2008 that it listed its 14th Sukuk. The Luxembourg Stock Exchange has been listing Sukuk instruments since 2002 for a total amount issued of around US\$5.5 billion.¹ The listed sukuk issuers are from various jurisdictions, notably the United Arab Emirates, Bahrain, Cayman Islands, Pakistan, Qatar and Malaysia.

The LuxSE has two segments: (i) the EU regulated market (the Regulated Market) and (ii) a multilateral trading facility designated as Euro MTF (Euro MTF). Issuers admitted to trading on the Regulated Market may avail themselves of the passport procedure under the Prospectus Directive to

have their securities listed on a regulated market of another EU member state. The Euro MTF was created in July 2005 following the adoption of the Luxembourg law of July 10, 2005 on prospectuses for securities (the Prospectus Law) implementing the Prospectus Directive, in order to offer an alternative market to issuers interested to list their securities outside the scope of the Prospectus Directive and the Transparency Directive.

Listing on the Euro MTF has been the "market of choice" for many foreign issuers. It is easier to list on this market and the LuxSE, which is the regulator approving the prospectus, is known to be very diligent in helping issuers to list expeditiously. The reporting and disclosure obligations (both financial and transparency) are not as stringent as the regulations arising under the Prospectus Directive and the Transparency Directive do not apply to securities listed on Euro MTF.

Sukuk have been listed both on the Regulated Market and Euro MTF.

Conclusion

It is not just the innovative legal corporate framework that has positioned Luxembourg as a key jurisdiction for the set up of securitisation structures but also the Luxembourg tax regulations, which are flexible enough to encourage investors.

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1. Luxembourg Stock Exchange Press Release, March 13, 2008

Tax Measures to Combat the Economic Crisis

Outi Ukkola is a Tax Partner at Deloitte Finland

Several countries have recently introduced measures to address and mitigate the effects of the global economic crisis. The stimulus action list is impressive: the tax measures include extensions of tax holidays, implementations or expansions of R&D tax regimes, carry back regimes for tax losses, extensions to tax payment deadlines and many more. The countries that have acted include large and small nations alike worldwide. Newsletters on tax developments cross the globe come in mailboxes almost daily.

In Finland Matti Vanhanen's second government is half way of its term. In February the government had extensive discussions to determine the way forward. There are many measures that the government has outlined, with the increase of the general pension age getting the most public attention.

In the big picture the productivity and competitiveness of Finland's business sector are the core foundations of the nation's economic success and living standards. Key components to current productivity and competitiveness are research, development and innovation, with the value added to a business increasingly generated through these functions rather than through traditional manufacturing or other capital incentive measures. Although Finnish R&D expenditure when compared to the country's gross national product is high by international standards, a number of recent studies show that Finnish high-end businesses are less keen on seeking rapid growth when compared to other countries with high R&D, know-how and similar economic infrastructures.

To improve competence building and innovations in particular the government announced the following measures in its statement on 24 February:

- Public resources are increased in this area
- There will be further emphasis on commercialization of research, business know how and internationalization
- It will be investigated whether innovation activities of small and medium sized companies can be fuelled by introducing a tax regime for R&D expenditure
- The conditions and economic climate for growth-companies will be improved by making the tax treatment for venture capitalists more favourable

Results of international comparative surveys, as well as the experience of a number of OECD and EU countries, on tax incentives directed at innovative businesses are encouraging. According to OECD studies, tax incentives appear more effective than direct subsidies. Despite this, by far the majority of the countries that have introduced tax incentives also maintain frameworks for providing direct subsidies. A well-designed combination of these two measures will complement each other and produce the best results.

Over 70% of OECD member countries and more than half of the EU member states have tax incentives to support R&D&I activities. Although these systems are typically designed to increase activities within the relevant country, the most recent international research notably shows that the increased tax competition targeted at R&D&I activities is resulting in certain activities being transferred from one country to another as companies seek competitive benefits.

In our view it is essential that Finland adjust its tax legislation to both encourage employment in the short-term and generate long-term overall economic success for the economy to create the necessary revenue to satisfy public sector needs. We believe any incentives created for innovative growth-companies must satisfy the following conditions:

- Subsidies must be targeted through carefully selected measures to R&D&I activities that increase positive spill-over effects throughout Finland's economy;
- The system must support the growth of innovative companies, in both their absolute number and their revenue growth, to create new jobs; and
- The system must be designed so that it will actually increase the profitability of the companies and, through this, the success of the Finnish economy in general.

I strongly recommend that international companies keep a close look on Finnish tax developments. The public debate will now start and hopefully by the summer there will be some guiding principles already drafted for the R&D activities, business angels and venture capitals operating in the Finnish market. ■

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Data Recovery and Business Continuity in Bermuda

An e-conversation among market leaders outlines Bermuda's readiness to cope when things go wrong

Data recovery (DR) and business continuity (BC) rank among the most important practices in the world of information technology. It is said that you are only as good as the state in which you emerge from the next catastrophe.

Not coincidentally, services in these areas are a core competence of a Bermuda ICT market that competes — with great efficiency — head-on with others in larger business centres. The BC/DR sector in Bermuda is vibrant with specialized hosting facilities, hot spots, and security professionals who make it their business to ensure businesses stay resilient, whatever the challenge.

To assess the state of Bermuda's capabilities in DR/BC, an e-dialogue was held among four of the Island's leading ICT and consulting practitioners. The participants in this debate were:

- Michael W Branco, President & Managing Consultant, Fireminds Ltd (www.fireminds.com)
- David Ciera, Senior Manager, Advisory, KPMG Advisory Limited (www.kpmg.bm)
- Stephen Davidson, Chief Marketing Officer, QuoVadis (www.quovadisglobal.bm)
- Chris Maiato, Senior Manager, Risk Advisory Services, Ernst & Young Ltd (www.ey.com/global/content.nsf/Bermuda/Home)

Do international standards, formal or otherwise, exist for DR? How do you meet or exceed them?

Davidson: There are many different standards for DR. There are specific "targets" such as the PAS56/BS25999 standard. DR is also incorporated into other more general IT security standards such as the ISO/IEC 27000 series.

In addition, there are specific industry codes (such as the BITS Framework for Managing Technology Risk for IT Service Provider Relationships in the financial services sector) and regulatory requirements (such as Sarbanes-Oxley for corporate governance and accountability). Generally speaking, the goals and overall approaches of these standards are pretty consistent.

QuoVadis clients adopt an array of DR methodologies, depending on their business and demands from customers, auditors, and regulators. Supporting those efforts, QuoVadis undertakes in its own audits, certifications of aspects of our operating environment and practices, including our own DR provisions. This provides evidence to customers and those to whom they are responsible of the reliability of our services.

Ciera: Formal standards have to be considered at a base level and tailored to suit the organisation. In my opinion, the starting point should be best practice, tailored down to where the organisation wants to be. The general rule of thumb, however, is that a recovery strategy will only be as good as the level of resource and expenditure an organisation is prepared to put into formulating its recovery capabilities.

Branco: Companies such as Fireminds, Logic and other top-end consulting companies use IT Governance frameworks (ITIL, COBIT) to ensure that client-company DR needs are being met. The international companies in Bermuda do this by requirement of their regulatory body (eg. the SEC). Smaller companies insist that their IT professionals earn a qualification such as the CISSP, so that they have a good understanding of securing and ensuring the continuity of their IT systems.

Maiato: Yes, there are many standards and guidelines for BC and DR, such as BS 25999-1:2006 and NFPA 1600). There are standards for the actual BCP and standards for the backup data recovery facilities. Bermuda has several local service providers that provide work area recovery services, secondary data storage facilities, and offsite computer processing facilities. These facilities all subscribe and endeavour to meet internationally recognised standards for disaster recovery facilities/data centres, and bunkers.

In addition to the physical space and technology requirements, advisory firms such as Ernst & Young provide services to assist clients developing and analysing their BC plans. Such plans are required to outline the steps necessary to resume a company's business operations in the event of a disaster — eg. how do you operate, in the event of a disaster, to provide critical services to your clients and staff? This question goes well beyond the technology realm.

What resources do you offer businesses operating in Bermuda for DR, and how do they compare with the level you would expect to find in New York, London or other international business centres?

Consensus: The top-end consulting companies in Bermuda use the same benchmarks and standards as those located in other international business centres.

Branco: Bermuda-based consultants simply work with fewer resources, or leverage partnerships with companies in larger jurisdictions in order to provide the same level of service to their Bermuda-based clients. Fireminds partners with top-end BCP Consultants (such as SunGard) to provide a complete business continuity plan with implemented IT DR infrastructure built on VMware and using real-time replication to ensure maximum uptime.

Maiato: Ernst & Young has a dedicated BCP practice that provides global services to assist organisations with all aspects of BCP. We provide assistance in developing BCPs, determining if current BCPs will meet business needs, assessing if BCPs were developed correctly, and assisting with testing of BCPs and the selection of a data centre provider.

Ciera: KPMG provides BC and DR advisory services to international and local businesses. We remain independent of any workplace or technology recovery suppliers. We assist clients to determine their recovery requirements prior to determining the required recovery strategies. These may be translated into requests for proposals for workplace and/or technology facilities. We also assist with the management and implementation of the selected vendor, whether technology- or workplace-related.

The next logical step is documentation of the crisis management, BC and DR recovery plans prior to educate the organisations' personnel on the recovery strategies to be invoked. KPMG also assists our clients by facilitating the testing of recovery strategies to ensure they meet the business requirements.

Davidson: In recent years, there has been significant interest in DR in Bermuda, as well as our international companies' need to comply with international regulatory and governance requirements. Reflecting the broad reach of many of Bermuda's international companies, Bermuda is just one component of their global business continuity needs. As a result, they are frequently looking for very specific services rather than broad-ranging DR support.

For the large companies, QuoVadis has a strong business providing work-area recovery facilities for companies that need short-term support during an interruption while their overall DR plan kicks into gear, as well as remote data backup-and-restore services for their Bermuda operations. For the small- to mid-sized companies, we also provide secure hosting for both live and fail over systems in our SecureCentre facility — allowing them to access top infrastructure without the significant capital expenditure and management overhead it would require to duplicate that in-house.

“Formal standards have to be considered at a base level and tailored to suit the organisation”

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Can you offer some success stories?

Ciera: For obvious reasons we cannot mention our clients' names — but it is fair to say that some of the strategies we have devised have been tested successfully in anger.

Branco: During a 2005 Island-wide blackout (while working for QuoVadis, before founding Fireminds), I managed the VMware environment hosted at SecureCentre and was able to assist customers by ensuring their backup systems were online, provisioning new virtual servers on the fly and responding quickly to customer needs as they worked through the business disruption. QuoVadis worked around the clock to ensure that generator was fuelled, servers were running and IT support was available 24/7 as customers managed their international businesses.

Maiato: Our offices in Bahamas, Bermuda and Cayman have been subjected to many weather-related incidents over the past few years. In all instances our Emergency Response Teams have successfully invoked our BCP plans to ensure the safety of our people, and the continuity of our business. In all instances, our business was not disrupted, and our data was secured and transferred in a timely manner, within our recovery objectives. In most instances, our teams were up and operational at their alternative sites before the hurricanes hit the islands.

Davidson: There is a growing recognition that — given Bermuda's limited size — some aspects of IT continuity are difficult to do properly, based solely on local resources. This is why, for example, QuoVadis teams with Incentra, which is based in the US, to operate and provide 24-hour support for our DataVault remote backup service. Incentra specialises in this area, working with telecom and infrastructure providers in several countries, and so has the critical mass of customers and expertise in this complicated area. QuoVadis brings the Bermuda secure hosting, coordination with the local network providers, and customer management.

Are there examples of lessons that you have learned about reliability in your or other companies' DR/BC planning?

Branco: Generally active-active DR systems are the best route for a reliable and robust DR infrastructure. The ability to failover to the DR site and resume critical IT operations within two hours is a measurable benefit that justifies the investment. In comparison, those companies who opt for traditional backup to tape, storage offsite and recovery timeframes of 48 hours do not inspire confidence in their customers.

Today's IT systems are expected to be available around the clock, around the globe and so most companies are moving to hot DR sites. Furthermore, using technology such as VMware, the costs of maintaining a DR site are much less; thus the investment in DR buys much more functionality today.

Maiato: A BCP that is not tested on a regular basis will not provide value to a firm experiencing a disaster. At the completion of developing a BCP, an organisation should test it so they can work out the kinks, validate the assumptions made at the beginning of the exercise, and then make the modifications as needed. It also provides the company's people with valuable training (similar to a fire drill) that will provide familiarity with the steps required in the BCP.

Davidson: Even using DR planning frameworks, there is sometimes a tendency to underestimate the risks facing a business. For example, it used to be that local companies focussed totally on short-term disruptions caused by wind storms. But the blackout that Mr Branco mentioned proved that disruptive events can come from totally different angles. Sometimes, companies need to step back in the DR planning to brainstorm "what if" scenarios that are outside their previous thinking.

In your experience, what mix of DR/BC planning is carried out in Bermuda, as opposed to in other locations? What drives that decision?

Maiato: The attention given to BC/DR planning is very different for each organisation. In general, however, it is often approached with a high priority after a significant incident has occurred, or the threat of one has been announced. The priority and resources assigned to the completion of the planning exercises often falls off after the incident and business resumes normal operations, thus resulting in organisations never fully completing their BC planning documents and exercises.

IT is one piece of the puzzle not the whole puzzle. For example, many insurance companies have redundant IT systems, but do not have detailed plans on how to receive clients that are submitting and reporting claims

after a hurricane or other natural disaster. They do not consider the potential that their building may be damaged or inaccessible after an incident.

Ciera: The key difference between Bermuda and other locations from a BC/DR perspective is the worst case scenario is the risk of a major hurricane. Most other locations' worst case scenarios are terrorism, fires and major systems failures.

Branco: I agree that general observation shows that most companies in Bermuda focus on IT DR and give less attention to formal business impact analysis and business continuity planning. This disproportionate focus on IT usually stems from the fact that most companies feel the pain when their e-mail server goes down, so IT managers can easily solicit funding to put backup systems in place.

Davidson: For most international companies, DR is coordinated globally so the efforts are pretty consistent. I think the major difference occurs among local companies, who may not be driven by the same regulatory pressures, or simply do not have the financial wherewithal to conduct thorough DR planning. In many cases, their response is driven by the cumulative experience of the family or management in responding to Bermuda situations. It often works well, but can fail horribly when those individuals are not available or totally "off-the-wall" events occur.

In their planning, are companies identifying the same systems as 'hot' or simply recoverable, or have you experienced that different industries select different systems?

Davidson: Companies that are serious about business continuity realise that they need to prioritise their continuity and availability options. With increased pressure on budgets, it is usually not feasible to have everything with 'hot' failover. A key part of DR planning is to identify which systems are most vital in day-to-day operation — and build discussions on recovery times and recovery points from there.

Maiato: Most organisations and companies (correctly or incorrectly) identify their e-mail system as one of the most critical systems required for the recovery of normal business operations. That said, companies in different industries do have industry-specific business applications that are selected. In an insurance company it will be the claims system, for banking it is usually the retail banking and ATM systems.

Branco: Bermuda-based companies have definitely moved towards hot DR systems in order to ensure maximum uptime. Using virtualisation and given the lowering cost of bandwidth in Bermuda, companies can now setup virtual snapshots of their primary servers in a robust colo facility such as QuoVadis, BTC or Cable & Wireless. Hot standby systems are more affordable now, so more systems are being setup in this manner.

Ciera: Companies we have worked with have implemented a range of solutions from hot, warm or cold recovery capabilities. The driver is primarily the impact of the outage from a financial or regulatory point of view.

How realistically do Bermuda companies test their DR/BC systems?

Consensus: Some are very good at it and others do not have any plans at all. Many of the largest insurance customers with regulatory compliance requirements regularly and religiously carry out full-blown, "shut the office down" DR/BC tests of different aspects of their DR provisions every month, year round.

Smaller, privately held companies tend to take a less rigid approach, though their smaller size allows them to react to DR situations a little easier.

An extra wave of activity in DR testing is experienced right before hurricane season — and then again whenever the first major Atlantic storm starts spinning.

How capable and resilient are Bermuda companies of dealing with unexpected events?

Consensus: Bermuda companies do a good job at reacting to incidents as the Island experiences hurricane and weather threats on an annual basis, although a greater degree of proactivity is needed in some cases. ■



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GOVERNMENT OF BERMUDA
Ministry of Energy, Telecommunications and E-Commerce
Department of E-Commerce

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The Mediterranean Conference Centre – 30 Years On

Located on the periphery of the historical city of Valletta, Malta, and overlooking the Grand Harbour, the Mediterranean Conference Centre is a 16th century building formerly known as the 'Sacra Infermeria' of the Order of St John. The Mediterranean Conference Centre is undoubtedly firmly established as one of the most impressive conference centres in all of Europe. The centre's historic background and imposing architecture no doubt play a very important role in securing the position it enjoys today.

Constructed in the latter part of the 16th century, this architectural landmark has had a fascinating history during which it was subject to various transformations as it changed to accommodate the needs of the day.

The building was fully restored in 1979 and converted into a modern conference centre which earned it the coveted 'Europa Nostra' Award for its 'superb restoration' and tasteful blending of ancient and modern.

The 30th anniversary of the transformation of the Holy Infirmary into an excellent conference centre, like any anniversary, is an occasion to reflect how we can ensure that this unique place in Malta continues to strengthen itself and the product 'Malta'. The way how the historical elements entwined themselves with the state-of-the-art conference facilities contributed towards the making of this place inimitable and distinctive, while attracting towards our shores high level multinational companies conferences and talents.

Since its inception as a conference centre, an ongoing restoration and maintenance programme has kept the unique historical character of this national monument, while providing a modern venue able to handle major international conferences, exhibitions, banquets and theatrical events. The MCC, the flagship of conference venues on the Island, is now renowned for its outstanding services and facilities. The range of events that can be held at the conference centre is rather wide.

The Mediterranean Conference Centre boasts a total of ten halls and eight syndicate rooms over an area of 7,000 square metres. The halls vary in size and are therefore suitable for a range of events. The largest and most impressive, Republic Hall, seats 1,400 in theatre style whereas the smallest, La Cassiere caters for 60 persons.

Each meeting hall is equipped with its own independent sound, lighting and climate control. Conference facilities include permanent installations for simultaneous interpretation for up to six languages, audio/visual equipment and WiFi throughout.

Rosette Micallef, Head of Sales and Marketing of the Mediterranean Conference Centre said "we have grown steadily over the years with a successful track record, boasting an impressive long list of satisfied clients. The Conference Centre has also contributed in no small way towards the evolvments of the conference business in Malta providing state-of-the-art facilities for both the international and local markets".

The main marketing thrust for the MCC is definitely its historic aspect. Over the years, the MCC has offered the clients a venue which is completely different from the normal concrete & steel structures. The architecture and the environment all around MCC seem to transmit a very positive feeling.

Adding value to the product Malta

The Mediterranean Conference Centre adds value to the selling points of Malta as a location for major corporate events. Ericsson, IBM, Pfizer, Philips, Glaxo Wellcome, Pharmacia, Janseen Cielac, Nortel Astra Zeneca, Baume and Mercier, Boehringer, Inhelheim, Bolton, AGIP, Aventis, Nestle Waters, Novo Nordisk, Perfetti, Sony BMG, Perfetti, Fedex and Deutsche Bank are some of the prestigious brands which the MCC managed to attract towards our shores for their corporate events.

The same can be said in the name of entertainment.

Further testimony to the centre's reputation and long experience, which stretches thirty years, is its membership in the Historic Conference Centres of Europe, HCCE, a leading historic conference centre marketing alliance.

Way ahead

The Mediterranean Conference Centre has potential and its uniqueness contributes towards it. The vision for the next years is to consolidate its

position as one of the leading service providers of its genre on the island. The recent announcement of the regeneration of the area adjacent to the conference centre will add to the value of the location. This makes the next 30 years look even more promising and exciting. ■



Sacra Infermeria, the main exhibition hall with an area of 1,700m²



La Valette Hall, the main banqueting hall at the centre, seating 900 guests



Republic Hall, Malta's largest auditorium, with a seating capacity of 1,400



David Bruce Hall, one of the small halls available at the centre



The Largest Conference Centre on the Island of Malta



The Mediterranean Conference Centre on the Island of Malta is a historical building situated within the capital city, Valletta. The Centre boasts a total of nine halls over an area of 7,000 square metres. The halls vary in size and are therefore suitable for a range of events.

Each meeting hall is equipped with its own independent sound, lighting and climate control. Conference facilities include permanent installations for simultaneous translation for up to six Languages as well as audio/visual equipment. The Centre can accommodate over 2,200 delegates in all the conference halls.

No matter what the size of the event being organised - from a small presentation to a large conference, a product launch or an exhibition, a convention or even a theatrical performance - the Mediterranean Conference Centre can cater for all your requirements.



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Cape Town International Convention Centre - Africa's Top Conference Destination

Cape Town, Africa's number one conference destination, will be home to the continent's first six-star green building when Cape Town International Convention Centre (CTICC) expands in 2012.

CTICC, which has welcomed more than three million delegates and visitors since opening in 2003, sits on Cape Town's northern foreshore, beneath Table Mountain, and provides flexibility and world-class amenities. Its impressive modern structural design is prominently located alongside the main highway into Cape Town and its convenient location at the gateway to the city provides delegates with easy access to transport terminals and major road networks.

The flexible facility provides a variety of sub-divisible and adaptable convention and exhibition venues.

CTICC currently offers 11,200m² of dedicated exhibition and trade show space, two raked auditoria seating for 1,500 and 620 delegates and a 2,000m² grand ballroom which can dine up to 1,200 people. It also has a special roof terrace meeting room with spectacular views of Table Mountain for dinners and special events as well as more than 33 break-out rooms varying in capacity from 25 to 330 people each. In the centre there are three different restaurant facilities and a popular new café that is fast becoming the hub of delegate networking.

CTICC2 is due to be constructed to the requirements set by the Green Building Council of South Africa and will be designed to use 40% less energy per square metre than the present CTICC, 95% less potable water and 25% less waste to landfill.

The new 30,000m² development, of which 9,500m² will be exhibition space, will incorporate water and energy saving technologies including special wind turbines to harvest electricity, while simultaneously ventilating the parking garages.

In the context of climate change, sustainable business development and being in a competitive industry, CTICC's focus is on minimising its carbon footprint and the environmental impact of the planned expansion. CTICC Phase 2 is due to be constructed to the requirements set by the Green Building Council of South Africa and will be designed to use 40% less energy per square metre than the present CTICC, 95% less potable water and 25% less waste to landfill.

CTICC's expansion will not only propel Cape Town into the forefront of sustainable building design and management, but will continue to drive the city's rise as one of the leading business tourism destinations worldwide.

The CTICC is within walking distance of the city's major hotels and just 20 minutes drive from Cape Town International Airport. Nearby hotels provide more than 3 500 rooms of three-star quality or more, including the 483-room five-star Westin Grand Cape Town Arabella Quays, which faces CTICC across Convention Square. CTICC is close to Cape Town's leading recreational amenities, shopping areas and cultural attractions, among which is the internationally acclaimed Victoria and Alfred Waterfront.

After five years of operation, CTICC has continued to attract the very best in conferences and conventions and is widely regarded as the leading convention centre in the southern hemisphere, with two thirds of all international meetings taking place in South Africa being held in Cape Town and one out of every three international meetings in Africa taking place in Cape Town.

While the 2007/2008 financial year saw CTICC far surpassing its revenue target, the business is built on the principles of a triple bottom line, and also measures its effectiveness through the criteria of its environmental and social performance. CTICC recognises that the sustainability of its operation relies heavily on its efforts to minimise the impact it has on the environment.

Since inception, CTICC has contributed more than R9.5 billion to the South African economy. Projections are that by 2012 the centre will also have contributed some R3 billion in tax revenue to the South African government.

CTICC's has a diverse and expanding workforce with much effort and money invested in the development of both permanent and part-time staff.

At the core of the centre's ethos is a policy of local procurement, with the bulk of its supplies and products being sourced from companies based in and around Cape Town.

CTICC obtains goods and services from 390 suppliers of which 87% are based in the Western Cape. Local expenditure amounts to R42m.

With a strong commitment to encouraging local enterprise, CTICC has enabled many Small and Medium Enterprises (SMEs) to develop along with it, perceptibly stimulating small-business growth in the province.

CTICC also constantly seeks to uplift the communities in which it operates



UNCONVENTIONAL

It may be called a convention centre, but there's nothing conventional about it.

The Cape Town International Convention Centre is designed to adapt to your exact requirements. From conferences hosting thousands of delegates and consumer exhibitions or trade shows, to executive business meetings and intimate social functions, the CTICC has played host to them all, memorably.

So, the next time you need a unique space in which to make a lasting impression, why settle for the conventional?

For more information call +27 21 410 5000, email info@ctconvention.co.za or visit our website on www.capetownconvention.com

Cape Town International Convention Centre

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■ Up to 10 000 m² of sub-divisible, column-free exhibition space ■ A grand ballroom that seats 1 500 ■ 2 large auditoria ■ 33 meeting and function rooms ■ A roof-top terrace ■ 3 exquisite restaurants ■ 1500 secure parking bays ■

CTICC



organisers when selecting a venue, but also because the centre recognises its responsibility to address issues like climate change and the preservation of the environment for future generations.

CTICC recognises and understands the responsibility it has to use its resources wisely, minimise its impact on the environment and, wherever possible, reduce its carbon footprint for the good of the planet. From the first day of construction, the centre has paid careful attention to its environmental impact. As a direct result, a recent evaluation by Green Buildings for Africa revealed that CTICC has achieved 77.1% compliance with the South African Energy and Demand Efficiency Standards. On completion of its new extension, the centre intends applying for a Six Star rating from the Green Building Council of South Africa.

Ultimately, it is the desire of CTICC that, through its actions and operations, it will not only limit its impact on the environment, but also serve as a benchmark against which the South African events and hospitality industry will measure the environmental friendliness of its operations.

International accolades

CTICC continues to scoop international accolades in both the local and international arena. In 2008, CTICC coveted the prestigious "Best of Cape Town Certificate of Excellence" in the category "Creative Cape Town". CTICC continues to enjoy international recognition for its services and facilities and was recognised in 2008 by the *Business Britain* publication as its "Convention and Exhibition Venue of the Year 2008".

Earlier this year the international magazine *European CEO* also named the CTICC its "Convention Centre of the Year 2008". At the Meetings and Incentives Travel Awards held in London, the centre was also awarded the bronze medal in the "Best Overseas Conference Centre" category.

CTICC's inclusion this year among the Top 500 companies in South Africa is further testament to the centre's service excellence. The Top 500 Companies list recognises South Africa's leading businesses.

"If you can imagine it, we can host it" so choose Cape Town and CTICC as your premier conference business destination. ■

and has formalised a Corporate Social Investment Programme, focusing on various charities to which the centre contributes through donations of excess produce and equipment.

The past financial year saw the revenue generated by CTICC rising by 28.5% to R129 million, which is a clear demonstration of the attractiveness of the centre as a venue for national and international conferences and other events. Having established a solid foundation over the past five years, CTICC is well positioned to continue growing its bottom line for the benefit of all stakeholders, and maximise the financial contribution of the centre to the ongoing growth of the provincial and national economies.

The centre presently has a well-filled portfolio of 134 international congresses booked for the next eight years until 2016.

Going green

CTICC considers the effective reduction of its carbon footprint to be of immense strategic importance. This is partly because environmental considerations are increasingly becoming an important factor for event



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Caribbean Special Report

ECCU - Regional Response to a Global Crisis

**Regional Trade Agreements - Repositioning the
Caribbean in the Global Economy**

Towards an Economic Union

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Opportune Summit

Edwin Carrington is Secretary-General of the Caribbean Community (CARICOM)



The Fifth Summit of the Americas is just a few weeks away — it will take place April 17-19 in Port of Spain, Trinidad and Tobago — and it comes at a critical juncture for the Caribbean Community and indeed for the entire Western Hemisphere. This meeting of 34 heads of state and government was always going to be important; now, with the global financial crisis upon us, it is even more urgent that our nations' leaders engage with each other on the most pressing issues of our time.

The economic uncertainty felt throughout the region and the world underscores the relevance of the theme of the Fifth Summit: "Securing Our Citizens' Future by Promoting Human Prosperity, Energy Security and Environmental Sustainability." Our governments must work together diligently to ensure that the economic crisis is resolved as quickly as possible, to make the future more secure for everyone. The people of the Americas need to know that their elected leaders are taking steps, in both the short and long term, to address their needs.

During the past few months, the countries of the region have begun to negotiate the Declaration of Commitment that the leaders will adopt in Port of Spain. The discussions on human prosperity have focused on issues related to equity, inclusion and social development, encompassing concerns as diverse as reducing infant mortality, promoting job opportunities and strengthening food security.

In the coming months, delegations of the member states will turn to the

sections on energy and the environment, which also go to the heart of securing our future. Through this negotiating process, the member states are seeking to forge consensus on the central goals that will help shape policy decisions throughout the region. From the beginning, Trinidad and Tobago has stressed that the mandates that come out of the Summit need to be concrete, measurable and achievable. This call to be focused and practical becomes even more urgent in a time of crisis.

Given its size and economic weight, the United States will continue to exercise substantial influence throughout the region, and its involvement in the Summit of the Americas is a key element that sets this process apart from other inter-American meetings. The Fifth Summit will provide an opportunity for the region to get to know President Barack Obama early on in the new administration and for the US leader to develop a more complete and nuanced understanding of our priorities and concerns. For the Caribbean, as well as for the other sub-regions of the Americas, this presents an invaluable opportunity to be heard.

In fact, the Fifth Summit will give all of our countries the chance to turn the page in our relationship with the United States. With all the challenges facing the world today, we need the United States to be fully engaged with the Americas, and this can begin to happen in Trinidad and Tobago. ■



FIFTH SUMMIT OF THE AMERICAS

Port of Spain, Trinidad & Tobago, April 17, 18, 19 2009

The ECCU – A Dynamic and Resilient Economy

Sir K Dwight Venner is the Governor of the Eastern Caribbean Central Bank



The international economy and community is at an historic turning point. Current events have and will continue to affect all countries including those in the OECS and the Eastern Caribbean Currency Union.

The financial and economic crisis which is now unfolding has been declared by the International Monetary Fund as the worst that the global economy has faced in 60 years.

Its impact and ramifications have been so massive that most analysts and institutions are not prepared to forecast when it will bottom out and the recovery likely to begin.

Impact of the crisis on the ECCU

Given our openness and integration into the global economy, the channels of transmission of this crisis into our economies are through the real sector and the financial sector.

In the real sector there are three areas in which we are affected:

- Tourism;
- Foreign direct investment; and
- Remittances.

Tourist arrivals and expenditure have fallen, and the bookings going forward are not promising. Tourism is now our major foreign exchange

earner and the challenge we now face would be if the recovery in the international economy does not come in 2009, we would then face two weak back to back tourist seasons.

This would have, in the absence of vigorous counter measures, a very depressing effect on our economies.

Foreign direct investment has shown significant declines, manifested in the slowing down or outright stoppage of major real estate and tourism projects.

These stoppages will have an impact on construction with its significant employment possibilities and on the capacity of the tourist industry, through the number of rooms and properties available to add to the current stock.

In the case of remittances, hard data is not easy to come by, but available information would seem to suggest that there is some slowdown in this area.

The other channel of transmission, the financial sector, is being affected through the availability of lines of credit and correspondent relationships with foreign banks which are now having difficulties of their own.

In the circumstances outlined above, we now have to come up with both

short term and long term responses to these challenges.

National and regional responses to the crisis

Our governments have been addressing these matters with some urgency, and their first responses can be found in the Budget Addresses delivered in December 2008 or by the statements made by those whose budgets did not fall in this period.

As a currency union, there have been consultations at this level including the ministers of tourism, ministers of finance and representatives of the banking sector.

These culminated in an historic meeting between the OECS Authority of heads of government and the ministers of finance who make up the monetary council of the ECCB.

It was unanimously agreed that the meeting was very constructive in carrying out an objective analysis of the situation from the individual member states and currency union perspectives, and in coming up with short and medium term responses to the situation which now confronts us.

The short term responses include:

- Attempting to maintain the level of ongoing economic activity by supporting the tourism industry in their cost reduction and marketing strategies;
- Engaging in targeted public sector investment programmes to stimulate economic activity; and
- Providing efficient and effective social safety net programmes to address the needs of the poor, the indigent and the vulnerable.

With respect to the financial sector, the decision was taken to complete the regulatory framework for the entire financial system and to construct money and capital market arrangements to facilitate the provision of liquidity and investment finance.

We have been very fortunate that the Canadian banks which are the largest banks in the currency union, are well regulated in their home jurisdiction and have been rated number one in the world. Notwithstanding, we have been maintaining very close contact with the Bank of Canada, the Office of the Superintendent of Financial Institutions (OSFI), and the headquarters of the banks in Toronto and their senior regional representatives.

In the case of the domestic banks, they are well capitalised and we have strengthened our oversight over them.

We have established a contingency team at the ECCB, with senior and experienced staff to maintain constant oversight over the situation and develop contingency plans, should a crisis arise.

We are advising our governments to complete the establishment, with some urgency, where they have not already done so, of the Single Regulatory Units (SRUs), to regulate those institutions in the financial system which are not supervised by the ECCB. Such institutions as insurance companies, credit unions, building societies, money services institutions, all need to be properly regulated in normal times, much less in times of crisis.

There is an old saying *"When your neighbour's house is on fire throw water on yours"*. We are therefore putting in place a regulatory framework and capability which is comprehensive, sophisticated and sensitively balanced between rules, regulations, prudential guidelines and self regulation.

The public can be assured that everything that is humanly possible is being done to preserve the safety and soundness of our financial institutions.

Discussions are on-going with the ministries of finance and the broker dealers to enhance the effectiveness of the Regional Government Securities Market to provide financing to the governments for recurrent and capital expenditure on a regular basis and at a reasonable cost.

We are also very well advanced in creating an Eastern Caribbean Enterprise Fund (ECEEF) to facilitate investment in the productive sectors.

These initiatives in the financial sector are important to facilitate the transformation of our economies into highly competitive and diversified

entities which can take advantage of the opportunities that will present themselves when the recovery comes.

The low growth scenarios which confront our economies are due in great measure to our small land and population size and limited technical capabilities.

The OECS Authority, in recognising this fundamental impediment, has taken the decision to move to the status of an OECS Economic Union by December 2009. There is an urgent need to create the critical minimum scale and a broader economic and financial base to achieve our economic goals.

The decision was taken to establish a transition team to address the current crisis and to align the responses with the achievement of the goal of economic union.

The team comprises:

- The Honourable Prime Minister of St Vincent and the Grenadines, Dr the Honourable Ralph Gonsalves;
- The present Chairman of the OECS Authority, the Honourable Tillman Thomas;
- The present Chairman of the Monetary Council, Dr the Honourable Errol Cort;
- The Director General of the OECS Secretariat, Dr Len Ishmael; and
- The Governor of the ECCB.

Other heads of government and ministers of finance are expected to assist this core group to tackle these challenges during the course of the year.

The group will coordinate and monitor the implementation of the short term and long term policy responses to the crisis which were agreed to at the joint meeting on the 15th and 16th of January 2009.

The meeting identified three critical sectors which could be instrumental in effecting the transformation of our national and regional economies, namely:

- Tourism;
- Construction; and
- Fisheries.

Work will start immediately by teams drawn from the national and regional public services and the private sector on strategies for carrying out this decision.

The team will also meet with regional and international countries, institutions, and private sector groups to access resources and technical assistance for implementing our short and long term responses to the crisis.

While the crisis has international origins, we have the responsibility as sovereign countries to decide on our own appropriate responses.

This particular crisis is so deep and far reaching that it requires a concerted and strategic response by a conscious and mobilised population. This means that every segment of the population, politicians in government and opposition, public servants, the private sector, the trade unions, civic society, the professions including teachers, doctors, lawyers, engineers, accountants, nurses, police, community organisations, families and individuals must take responsibility for our current and future prospects and the goals of achieving a better standard of living and quality of life in the OECS.

In the final analysis a country must depend on its citizens to work hard, to cooperate with each other, to be objective in their judgments and to be prepared to make sacrifices for the good of their country.

In this time of international crisis each and every one of us must perform the role of citizen to the best of our abilities to ensure the welfare of present and future generations.

I end with this memorable quotation:

*There is no "them and us"
In a world this size there can only be "we" -
All of us working together. ■*

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Regional Trade Agreements as a Tool for Repositioning Small and Vulnerable Economies: The Case of the CARIFORUM-EC Economic Partnership Agreement

Natasha Ward is the Trade Consultant with the Barbados Private Sector Trade Team (PSTT) and Joel Richards is the Trade Research Officer with the PSTT. Email: Natasha.ward@tradeteam.bb and joel.richards@tradeteam.bb. The PSTT is the trade research division of the Barbados Private Sector Association

Introduction

The recently concluded Economic Partnership Agreement (EPA) provides a vehicle for CARIFORUM¹ countries to strategically reposition themselves in a global environment in which trade relations are increasingly based on reciprocity. In order to buffer the transition from preferential trade arrangements to a more liberalised framework, the EPA maintains access for traditional CARIFORUM exports while providing enhanced market access for goods and new opportunities for the provision of services. It is particularly in the latter area that most CARIFORUM states feel a sense of optimism given that there is tremendous export potential. The EPA therefore facilitates a transitioning towards a more pro-competitive trade regime in terms of the restructuring of productive capacity while establishing mechanisms for the provision of technical assistance and development financing.

Main gains from the EPA

Market Access

- Manufactured and agricultural products

As noted before, the EPA allows for continued predictability in access to the European Union (EU) market for CARIFORUM goods. In essence, the CARIFORUM region would be granted duty-free, quota-free access to the EU market for all goods meeting qualifying rules of origin with the exception of rice and sugar exports which would have duty and quota restrictions until 2010. This access allows the CARIFORUM region to enjoy continued preferences in the EU market relative to other countries that face duty and quota restrictions.

Furthermore, given that the EPA is a free trade agreement (FTA), CARIFORUM has granted the EU preferential access to its own market for approximately 92 per cent of exports. However, the CARIFORUM region was able to secure a measure of asymmetry in this regard as exports from the EU would be granted preferences on a phased basis ranging from ten to twenty-five years. Moreover, most CARIFORUM produced goods and revenue sensitive imported manufactured goods were excluded from the scope of liberalisation as well as almost all agricultural produce. As such, a number of CARIFORUM manufacturers and agricultural producers continue to receive a significant level of protection.

Beyond the enhanced market access, the EPA makes provision for the granting of resources to CARIFORUM manufacturing and agricultural based companies for innovation and development. There has also been a commitment on the part of the EU to provide development support aimed at promoting private sector and enterprise development, enhancing the international competitiveness of CARIFORUM firms and enhancing the technological and research capabilities of CARIFORUM states to facilitate development of and compliance with, internationally recognized agricultural health and food safety requirements and technical standards. Undoubtedly, CARIFORUM stands to gain significantly from such measures.

- Services and investment

Prior to the EPA, CARIFORUM did not have guaranteed access to the EU services market. Therefore, the region seized the opportunity to gain commercially relevant market access in services and to provide a legal framework to govern investment and the activities of investors.² Under the EPA, the EU has liberalised more than 90 per cent of its services sectors on the WTO W/120 list. The EU made commitments on the cross-border supply of services and the establishment of commercial

presence in the business, communications, construction and related services, distribution, education, environmental, financial, health and social services and transport services as well as in some new sectors such as spa services. The labour mobility commitments were hailed as some of the most valuable gains. Specific commitments include the temporary entry and stay of key personnel and graduate trainees in the areas of business, construction, distribution, education, financial, health, tourism, recreational and transport services. With respect to Contractual Service Suppliers, the EC has made commitments in 29 subsectors in the business, education, environmental, tourism and entertainment services. CARIFORUM has a strong competitive advantage in the latter two services. In addition, market access was granted to independent professionals in 11 subsectors of the business services sector.

In terms of investment, the commitments cover both services and non-service activities. Specifically, the EC has liberalised investment in agriculture; hunting and forestry; fishing and aquaculture; mining and quarrying; manufacturing; and production, transmission, and distribution on own account of electricity, gas, steam and hot water.

Challenges

It is clear that CARIFORUM states must now seek to put in place measures to ensure that they fully enjoy the benefits of the new and enhanced access to the European market. For example, more needs to be done to boost the export capacity of the private sector and diversify the range of products to effectively penetrate the EU market under the EPA. In the case of Barbados,

2006 trade data indicates that exports of sugar and rum accounted for well over half of total exports to the EU.³ Moreover, there has also been a heavy concentration of exports to the United Kingdom (UK) market in particular.

Additionally, several of the key elements required to complete the construction of the regional integration initiatives at both the CARICOM and CARIFORUM levels remain outstanding. These include the CARICOM Financial Services Agreement, the CARICOM Investment

Code and the CARICOM Public Procurement Regime. It is interesting to note that CARICOM countries made commitments in these areas under the EPA before concluding regional arrangements amongst themselves. Hence, to fully benefit from these aspects of the EPA, it would be useful for CARICOM countries to act swiftly to resolve such issues amongst themselves. In addition, the FTA between CARICOM and the Dominican Republic remains incomplete in relation to services, investment and non-reciprocity with respect to the Dominican Republic's access to CARICOM Less Developed Countries' (LDCs) markets. Now that both parties have afforded the EU much more beneficial treatment under the EPA than they afforded themselves under their bilateral agreement, they now have to refashion their FTA to reflect something as comprehensive as the EPA. The EPA indicated that CARICOM More Developed Countries (MDCs) and the Dominican Republic should offer each other the same preferences as granted to the EU one year after signature of the EPA whilst the CARICOM LDCs and the Dominican Republic were to do so, no later than three years subsequent to signing the EPA.

Development support is another critical aspect of the EPA for CARIFORUM countries. It will be important to ensure that such support is targeted towards building strong regional enterprises, creating a more facilitative business environment, improving trade logistics and facilitation as well as in enhancing product quality.

The EPA also has implications for CARICOM countries at the multilateral level. These countries have largely maintained a defensive posture at

“It is clear that CARIFORUM states must now seek to put in place measures to ensure that they fully enjoy the benefits of the new and enhanced access to the European market”

the World Trade Organisation (WTO) with respect to the liberalisation of goods and services. Given that CARICOM has entered into this very comprehensive agreement with a developed country trading partner and has made extensive commitments to eliminate tariffs over a twenty five year period as well as significant liberalisation in the area of services, the grouping's defensive posture at the WTO could very well be undermined. It is also likely that in other bilateral agreements with other trading partners such as the United States and Canada, CARICOM countries may be required to grant EPA parity. The EPA therefore could become the de facto standard by which the region's subsequent trade agreements are measured.

Other challenges include the regional co-ordination of the implementation process. This represents a critical element for the region to take advantage of market access openings and development co-operation and financing.

There are several levels of activities to be undertaken in this regard. These activities include the designation of an institution to co-ordinate the implementation process across the region to facilitate the making of joint decisions such as those pertaining to the Caribbean Development Fund as well as the co-ordination of national activities among domestic stakeholders to avoid the duplication of efforts.

Also to be addressed are mechanisms to overcome hurdles which prevented CARIFORUM from accessing the European market such as sanitary and phytosanitary requirements. Although a number of suppliers have been Hazard Analysis and Critical Control Point (HAACP) certified,

market entry has in some instances been prevented by the application of private standards. In this regard, the EPA contains a number of technical assistance provisions to assist CARIFORUM countries in dealing with these constraints.

The negotiation of Mutual Recognition Agreements (MRAs) for regulated professions is another area which must be expedited in order to take the maximum advantage of a number of the EU's commitments. The CARIFORUM states must first at a national level and then at the regional level agree to the recognition of qualifications. This will require a remarkable level of co-ordination by the business support organisations and the industry associations. These organisations and associations will then be expected to negotiate MRAs with their EU counterparts. The CARIFORUM region can also anticipate technical assistance from the EU with respect to the MRAs.

Conclusion

The EPA is by far the most comprehensive trade agreement signed between CARICOM countries and a third country or region to date. The agreement generated much debate and controversy during the negotiation process and in the months leading up to its official signing. It is anticipated that the region will move swiftly beyond the divisive tensions to delineate a strategy for taking maximum advantage of the FTA. While the EPA may not be a perfect agreement, it does offer the region the opportunity to strategically reposition itself not just in the EU market, but in the wider global economy. ■

1. CARIFORUM consists of the Dominican Republic and 14 member states of CARICOM (Antigua and Barbuda, the Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines, Suriname and Trinidad and Tobago)
2. For a more comprehensive discussion of the services and investment component of the EPA, refer to Pierre Sauvé and Natasha Ward, "Services and Investment in the EC-CARIFORUM EPA: Innovation in Rule Design and Implications for Africa," *The European Union's Economic Partnership Agreements with Africa: New Panacea for Development?* Ed. Gerrit Faber and Jan Orbie. (Routledge, 2009); and Pierre Sauvé and Natasha Ward, "The EC-CARIFORUM Partnership Agreement: Assessing the Outcome on Services and Investment," *ECIPE Discussion Paper*, (Brussels: European Centre for International Political Economy, 2009)
3. Barbados Statistical Service, 2006

Towards an Economic Union: The Organisation of Eastern Caribbean States

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The OECS: the reality of small size

The countries of the Organisation of Eastern Caribbean States (OECS)¹ have embarked on a journey towards establishment of an OECS economic union. This may be viewed as a natural culmination of a long history of cooperation that stretches as far back as colonial times. At the very core of this journey, is the confluence of fate, geography, geology and history, all of which have conspired to shape these islands, and place them in close proximity one to the other - setting the stage for the sharing of challenges, aspirations and a sense of common purpose. This close proximity and the small size of these islands have in many ways defined the personality of this space and its people, and have defined as well the persona of the entity referred to as the OECS.

Perhaps one of the most defining characteristics of the islands in the OECS is that of their small size, even within the Caribbean where other Small Island Developing States abound. The combined regional population of 584,000 persons, is less than the population of the urban areas of many countries within and outside of the Caribbean region. Small size brings with it an array of special challenges in the ability of small islands such as the OECS member states to mobilize domestic savings for investment, to produce goods and services at competitive prices, to equip scarce human resources with the full array of skill sets needed to build modern societies, to allocate even scarcer financial resources to the process of development, to use, apply and absorb technology, to supply social services and infrastructure at affordable prices, to police borders, fight drugs, crime, and HIV AIDS, to deal with the volatility of both external markets and the price of energy, to accommodate increases in the cost of food, to deal with the fallout of the global credit crisis, and to accommodate the politics of the world economy.

The reality of these challenges – and the strategic response engineered by



the OECS - has received world wide acclaim. In this home-grown approach to the issue of small size, the OECS model in which member states pool resources - human and financial - in an ambitious strategy of institution-building and service provision through functional cooperation, is unique, allowing these islands to exert far more political leverage than would otherwise obtain and to weather potentially debilitating situations as a group.

A historical perspective

A characteristic of the early history of the OECS has been common administration in a range of areas. This approach started with the formation of the Leeward Islands Federation between 1670 -1720, followed by the ill-fated West Indies Federation of 1958-1962, the establishment of a Free Trade Association in 1965 and the Caribbean Free Trade Agreement (CARIFTA) in 1968. In 1966, the West Indies Council of Ministers (WISA) was established between the Windward and Leeward Islands to provide a forum for discussions and actions leading from the colonial period of "self rule", to the achievement of independence. In 1968, this same group of islands established the Eastern Caribbean Common Market (ECCM).

These initiatives, which gave primacy to the establishment of joint institutional architecture at the regional level in response to individual human and financial constraints, sowed the seeds of the OECS model of integration. The institutional structure that now makes up the organization began to take shape in 1950 when the then British Caribbean Currency Board (BCCB) was established, later evolving into the Eastern Caribbean Central Bank (ECCB), following the withdrawal of British Guiana, Trinidad and Tobago and Barbados from the arrangement. The Directorate of Civil Aviation (DCA) - now known as the Eastern Caribbean Civil Aviation Authority (ECCAA) - was added in 1957, followed by the Eastern Caribbean

Supreme Court in 1967. These were all established to provide specialized services in the areas of monetary policy, civil aviation and the judiciary across the OECS region.

On 18 June, 1981, the Treaty of Basseterre was signed by six member states and one territory² in the capital of St Kitts and Nevis, giving birth to the Organization of Eastern Caribbean States. Two more countries (British Virgin Islands and Anguilla) satisfied the requirements of the Treaty in November 1984 and May 1995 respectively and became associate members. By 1981, several of the member states in the region had either achieved independence, or were well on their way to doing so. As newly emerging sovereign nations - small and vulnerable, responsible for all of their affairs for the first time - they felt that it was imperative that they establish formal relations at the highest level to guide joint activities.

Since concluding the Treaty of Basseterre, the OECS countries embarked on a process of functional cooperation through integration to reduce their social, economic, environmental and political vulnerabilities and increase their resilience. The countries have amplified the regional institutional architecture by adding to the ECCB, ECCA and Supreme Court, the OECS Secretariat, Eastern Caribbean Telecommunications Authority (ECTEL), the Pharmaceutical Procurement Services Unit (PPS) and the Eastern Caribbean Securities Exchange. Moreover, the OECS now boasts joint Diplomatic Missions to Ottawa and Brussels, a joint technical mission to the World Trade Organisation (WTO) in Geneva, an office in Puerto Rico, a Regional Security System in which it partners with Barbados, and a major initiative at the Secretariat to assist in the fight against HIV/AIDS.

Through the PPS, member states have been able to reduce the price of medicines by as much as 37% over the last 15 years. In 2007, the PPS returned to the nine countries savings amounting to over \$3M on pharmaceutical purchases of \$14.5M. Through ECTEL, competition has been introduced into the OECS, drastically reducing the cost of overseas calls, allowing for the entry of new providers, reducing the cost of doing business and in the process making the cell phone perhaps the most ubiquitous personal item on the region's streets.

Joint diplomatic missions have allowed these islands, as a group, to represent their strategic interests in different parts of the world, at a far lower cost than if each member state were to operate independently. Through the ECCB, the monetary union of the OECS has achieved significant levels of fiscal stability. The OECS HIV AIDS program offers direct support to the ministry of health in each member country in scaling up the treatment of persons who are HIV positive, and provides through an arrangement with Brazil, free doses of anti-retroviral drugs for 500 OECS persons. The regional security system provides for the patrol of the OECS air and sea space; and for every \$1 contributed to the OECS Secretariat member states receive at least \$3 and sometimes more, in technical support and direct benefits.

From the perspective of the region's partners the OECS arrangement is also expedient: in 2008, Brazil opened a diplomatic mission to the OECS and to St Lucia; Venezuela appointed a special ambassadorial envoy to the OECS and Spain executed a memorandum of understanding with the secretariat to support the recently launched OECS School of Protocol and Diplomacy. Other prospective partners have also made overtures to the OECS which are premised on engagement as a single region rather than as individual countries.

The OECS member states have worked together on the development of an OECS strategy and approach to negotiating trade agreements, presenting common positions at various negotiating theatres on key areas such as services, development, and special and differential treatment for small island states. OECS trade ministers, in recommendations to feed into the broader regional negotiating Brief for the upcoming CARICOM-Canada negotiations for a free trade agreement, placed strong emphasis on a special and differential carve out for the OECS, given the small sizes and capacity constraints of member states. They stressed that the carve out should be commensurate with OECS levels of development and should, among other things, be guided by sustained trade capacity building measures and development support similar to what has already been secured in the Economic Partnership Agreement (EPA) with the European Union. The

OECS through a joint mission in Geneva present common positions to the World Trade Organisation, and through similar joint representation in Brussels speak with one voice to the European Union.

Continuing the process

Notwithstanding its achievements to date, the OECS has undertaken to engage in a deeper form of integration. A primary justification for this is the perceived need for the OECS to continue to advocate, champion and pursue its own interests and build strategic alliances even while maintaining the important relationships which it has with the Caribbean Community (CARICOM) and other groupings at the regional, hemispheric and global levels.

As part of the integration process, the countries are currently elaborating a new treaty which consolidates their achievements to date, makes provision for the establishment of an economic union as a single economic and financial

space and, arguably of equal significance, addresses some of the challenges of policy implementation traditionally faced by the region, through the introduction of a new governance structure with attendant legislative and executive procedures.

The draft new treaty takes cognizance of the continuing challenges posed by the region's peculiar vulnerability and sets out among the organisation's purposes, that of being an institutional forum to discuss and facilitate constitutional, political and economic changes which would be necessary for the successful participation of the member countries in the regional and global economies.

Of the OECS' endeavours, as set out in the draft treaty, it is perhaps the economic union that has received most attention. This may be justified by the gamut of issue areas which it comprises - ranging from the movement of goods, services, workers and the right of establishment, to sectoral development and harmonization (agriculture, tourism, transportation, energy, telecommunications, *inter alia*) not to mention the further elaboration of such areas as human and social development, environmental sustainability, marine resources and the marine environment, disaster response and risk reduction.

It is important to bear in mind, however, that the proposed Economic Union will not be a miracle pill that can magically cure all of the ills which challenge the OECS. It is nevertheless a step in the right direction. It will require significant adjustments including in respect of national sovereignty, as the single economic space is attained, but the relinquishing of some measure of sovereignty is not anathema to the region: many of OECS' greatest achievements were only possible because member states pooled their sovereignty. The imperatives that dictate a closer and deeper integration in the OECS are as real today as they were forty or fifty years ago, if not more urgent and the OECS cannot but take the bold steps necessary to ensure their peoples' social, economic and political security. ■

“..the OECS has undertaken to engage in a deeper form of integration. A primary justification for this is the perceived need for the OECS to continue to advocate, champion and pursue its own interests and build strategic alliances even while maintaining the important relationships which it has with the Caribbean Community (CARICOM) and other groupings at the regional, hemispheric and global levels”

1. The full members of the OECS are the independent countries of Antigua and Barbuda, Dominica, Grenada, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines and the non-independent territory of Montserrat. Associate members are Anguilla and the British Virgin Islands, which are also non-independent territories
2. Antigua and Barbuda, Dominica, Grenada, Montserrat, St Kitts and Nevis, St Lucia and St Vincent and the Grenadines

Grenada - Open and Ready To Do Business

In a world characterized by an uncertain business environment, effervescent markets, and evolving technologies, Grenada offers a unique climate where businesses are allowed to grow and prosper. Investors have found a friendly, educated workforce that is adaptable to the changing needs of a global clientele.

The government of Grenada recognizes that private enterprise is the engine of the Grenadian economy and has taken steps to improve the climate for doing business on the island. Its overarching policy is to encourage increased private investment and to foster the development of existing investments through sound macro-economic policies, a conducive-enabling environment and an efficient and modern public sector.

“We are building a new economy where government and investors will work together to ensure benefits to both sides”

Prime Minister Tillman Thomas

Investors are encouraged in all fields of lawful economic activity

There is minimum entry requirement, no restriction on foreign ownership, no restrictions on foreign currency transactions, easy movement of capital, profit and dividends and attractive fiscal incentives.

Foreign investors are given equal treatment to domestic investors.

Investors in Grenada can benefit from a stable democratic style of government; stable economy; developed infrastructure, reliable investment support services, low crime rate and good quality of life.

Investment opportunities can be found across a wide range of sectors

Priority areas for investment in Grenada include tourism (hotels, villas, condominiums/time share property, attractions, marinas); manufacturing (film production, publishing and printing, handicraft, agro-processing, light-manufacturing), information communications technology; international financial services; health services (retirement homes, hospitals, health clinics and medical facilities) and educational services.

Grenada continues to demonstrate its economic resilience by an increasingly steady growth rate, despite contending with the devastation wrought by two major hurricanes during the ten month period September 2004-July 2005. Over the past four years, the Grenadian economy experienced real growth, averaging almost 4% annually. For 2007, the economy grew at a rate of 3.1 %, while a growth rate of 4.3% is projected for 2008. This compares quite favourably with growth experienced in other destinations in the region and is being led domestically by the construction sector (which currently continues to grow as a direct result of increasing development of tourism and residential properties), wholesale and retail trade, electricity and water, sea transport, communication and real estate and housing.

The inflation rate continues to average at 3.4% annually, stemming mainly from the effects of rising prices on the international market and the hike in wages for all categories of labour in the construction industry in the domestic market. Unemployment, which continues to be a challenge, declined significantly from a record high of 40% after the aftermath of the hurricanes, to 18.5% in 2005.

Grenada's appeal as an investment location is significantly enhanced by its open door policy to all bona fide investors, both foreign and local.

There are no restrictions prohibiting investment, and investors are encouraged to establish and operate business in all fields of economic activity with the exception of those prejudicial to national security, detrimental to the natural environment, public health or national culture.

Among its key features, Grenada boasts of excellent hotel sites, diverse tropical attractions such as white sand beaches, natural bays, exotic reefs, historic dive sites, waterfalls, volcanic lakes and ponds, rainforest, national parks, tropical flora and fauna, mangrove forest and more than 100 species of bird. Among the bird species is the Grenada Dove (*Leptotila wellsi*), which is Grenada's national bird. The island has an English-speaking population, modern sporting facilities, easy access by air via a 9,000 sq ft international airport, and by sea via modern port and cruise ship facilities.

Investment flows/activities

The tourism industry continues to be the main contributor to the country's economic growth and development and has created a plethora of untapped investment potential, particularly in those areas which create linkages to the sector such as entertainment facilities, handicraft, film, video and sound production, to name a few.

Grenada's growing reputation as an untouched, unspoiled and safe destination for tourists is serving another purpose. The attention of the rich and famous are drawn to the country as several major tourism related projects dot the landscape. The fact that Camper Nicholson, a world renowned marina operation, has set up in St George's instils investor confidence. The administration of Prime Minister Tillman Thomas views the sector as one of the main drivers for the creation of jobs and for the resuscitation of the island's economy, battered by two hurricanes and the global economic crisis.

Foreign direct investment has increased by over 300% since 2004 and over the next five years, well in excess of US\$2 billion will be invested in the tourism sector, providing over 4,000 new jobs. Among the tourism projects to come on stream, is the 120 room Four Season Resort, while currently there are other major high end tourism resort facilities being developed. The following is a selection of the same:-

- The Levera Development Project - a US\$112 million project involving a 40-room boutique hotel, spa and 135 luxury villas housed on a 360 acres site.
- Port Louis Marina and Creole Village - an EC\$1.5 billion resort spa and maritime village to include a world class marina, 120-room 5-star hotel, world class spa and well-being lifestyle centre.
- Paradis Ltd - a US\$54 million project involving 20 luxury villas and yacht berthing on an island measuring 74.1 acres.
- Virgin Beach development - an EC\$74 million project involving a residential marina to accommodate 250 berths with a maximum capacity to accommodate 20 mega yachts, a 30-room hotel and 60-room condominium.

However, Grenada's untapped investment potential is not limited to the tourism industry. Potential opportunities also exist in the agricultural sector to meet the growing demands of the tourism sector, as well as in ICT sector services, retirement homes, health and wellness facilities, hospitals and medical facilities, recreational, entertainment, cultural and sporting facilities. The government of Grenada remains committed to undertaking relevant changes to support and improve the investment climate and have already invested in state-of-the-art telecommunication and road network infrastructure, port expansion and cruise ship terminal to support current and anticipated economic developments.

The Grenada Industrial Development Corporation provides "One Stop Investment Facilitation" service for all investors. The services offered by the corporation include business and investment advice on doing business in the country; processing of applications for fiscal incentives; assisting investors to secure all required approvals, certificates, work permits, land for projects' realization, and such other support and assistance as investors may require to establish and to operate their projects; business support services including technical assistance for business diagnostics and the preparation of business plans and access to affordable factory space.

Through the GIDC, a full programme of investment incentives is available to investors. Such incentives includes accelerated depreciation with provisions for losses carried forward for a period of ten(10) years, investment allowances, deductible expenditure and customs duty exemptions. Detailed information on doing business and investing in Grenada can be obtained from GIDC website at www.grenadaworld.com

It's a Fact: Business Aviation Makes Economic Sense

When a public uproar erupted over how and when airplanes are used by companies seeking government loans, the story told in the news media was often a one-sided account lacking voices of support for business aviation. Now the time has come to speak up for the tens of thousands of cost-conscious businesspeople who consider business aviation an essential tool.



"At a time when we are facing almost unprecedented economic challenges, US businesses need tools that will help them enhance productivity, maximize flexibility, and maintain strong communications," said NBAA President and CEO Ed Bolen. "No Plane No Gain will underscore why business aviation is critical to tens of thousands of cost-conscious companies fighting to succeed in a difficult market."

Two General Aviation (GA) associations launched a campaign dedicated to defending the value of business aviation in response to the increasingly negative stereotype of business aviation.

The National Business Aviation Association (NBAA) and General Aviation Manufacturers Association (GAMA) recently a comprehensive new joint advocacy campaign with a familiar name: No Plane No Gain.

No Plane No Gain will reinforce the value of business aviation to American workers, policymakers, companies and communities across the United States through a multi-faceted, multimedia approach. Backed by dedicated financial resources from NBAA and GAMA, this campaign will include: A dedicated No Plane No Gain web site at www.noplanenogain.org studies and surveys from respected sources, placement of paid advertising, and new media like webinars, podcasts, and online videos at YouTube.

Tens of thousands of well-managed US companies use business airplanes because they have proven their value in multiplying the productivity and efficiency of their business operations. In this tough economy, businesses need to reach as many customers in as little time as possible.

Business aviation is part of a productive engine for the wider economy as well. General aviation contributes more than 1 million jobs and \$150 billion annually to the US economy, including thousands of good-paying manufacturing jobs and positive contributions to the balance of trade.

The new initiative will take full advantage of the changing ways people receive and process information today while building on proven advocacy techniques. ■

Learn more at www.noplanenogain.org





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