HOW DO TRADEMARKS AFFECT FIRMS’ INCENTIVES TO INNOVATE?

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Research question

- Purpose of trademarks is not to stimulate innovation

- Yet innovating firms extensively use trademarks
  - (but so do non-innovative firms)

- Exploratory paper: How do trademarks affect firms’ incentives to innovate?
  - How important are these effects?
Theoretical background

- Economic function of IPRs
  - e.g. Maskus, 2000, Landes & Posner, 2003

- Economic function of trademarks

- Economics of innovation incentives
  - E.g. Antonelli, 2003, Scotchmer, 2004

- A few studies: relationship between TMs and innovation
  - Nicholson, 2000, Mendonca et al., 2004
Economic function of trademarks

- Differentiate products or services
- Signal of quality/good will
- Reduce consumer search costs
- Also signal to other firms
Patents and trademarks differ in important ways

- **Patent**
  - Exclusive rights in return for disclosure of the details of the invention, thereby facilitating the diffusion of new knowledge

- **Trademark**
  - Exclusive rights to a distinctive word, symbol, shape, etc.
How are trademarks linked to innovation?

(1) Direct incentives to incremental innovation
- Thus “innovation” can comprise product differentiation
- Most such innovations cannot be patented

An example:
(2) Supplements to other appropriability strategies

<table>
<thead>
<tr>
<th>Means of appropriability</th>
<th>How trademarks can enhance appropriability</th>
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<tbody>
<tr>
<td>Patent</td>
<td>Raise imitation costs</td>
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<td></td>
<td>Appropriability after patent expiry</td>
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<tr>
<td>Lead time</td>
<td>Delay competitors from catching up</td>
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<td></td>
<td>Enable appropriability even if lose first position</td>
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<tr>
<td>Secrecy</td>
<td>Raise imitation costs</td>
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<td>Enable appropriability even if secret disclosed</td>
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To what extent do trademarks block innovation?

- Might lead to more incremental innovation at expense of basic innovation
- Barrier to entry to a more innovative firm
- Supplement to patent (which can block innovation)
How important are the effects of TMs on innovation?

- Fewer effects (both positive and negative) than patents
  - Limited monopoly power
  - Trademark-based licensing does not involve innovation

- Much depends on consumer perceptions
  - TM may signal innovativeness for a particular product, but this does not necessarily apply to other products, or the firm more generally
Trademarks most important where firms cannot appropriate returns by other means

- Design-based product differentiation

- Services
Trademarks can even help to protect "the unprotected"

- Red Hat has developed a successful business model fully based on Open Source Software applications
  - Red Hat gets Linux source code free, tests and improves the software, and distributes applications that can be downloaded without charge from the Internet
  - But most customers prefer to buy an original copy, and they are also covered by Red Hat’s guarantee and offer of technical support
Concluding remarks

- More attention should be paid to the effects of trademarks on innovation
- How strong should trademark protection be?
- What types of innovation are encouraged by TMs?
- What are the effects when TMs strengthen other appropriability strategies?

- Implications for SMEs?
Further research:
(1) Innovative effect of Internet domain names

- Only one name can be registered under each top-level domain
- Dissatisfied consumers can also use DNs to subvert the company
(2) Innovative effect of geographic indications?

- Identify a good as originating in a particular place

- But how far should this protection go?
  - Some say: Producers have the right to preserve the reputation and quality of traditional goods
  - Others: Protectionism; supports inefficient production