

Fakes and status in China

China is known for "malinvestment". Its consumption habits are also pretty dodgy



MOST shop windows proudly showcase what can be bought inside. The window of the Silk Street Market, a touristy shopping centre in Beijing, is a bit different. It displays a pair of official notices advertising what cannot be bought inside. These non-offerings include luxury brands such as Prada, Louis Vuitton and Burberry. The notices are meant to save customers from buying fakes unwittingly. But many still buy them wittingly. You could almost say that counterfeits remain Silk Street's trademark, despite the market's efforts to stamp them out. On the ground floor, a purple "Paul Smith" polo-shirt from a Guangzhou factory was offered to your correspondent for 1,285 yuan (\$200), a price which eventually fell to 150 yuan. It is not easy to walk away from such bargains. Especially when the stall holder will not let go of your coat.

Economists and policymakers around the world want China to consume more. They are eager for it to reduce its dependence on investment, which amounted to almost half of GDP last year. No economy that invests so heavily can possibly invest it all wisely. Economists therefore worry about a widespread misallocation of capital, or "malinvestment". But some of China's consumption is also a bit questionable.

Fake goods are rife. Researchers once stopped every fifth person in a Shanghai mall and asked them about their buying habits. Of the 202 who completed the survey, almost three-quarters admitted to buying knock-off luxury goods. The resulting paper* by Ian Phau and Min Teah of Curtin University of Technology in Australia was titled "Devil wears (counterfeit) Prada". Some people buy luxury brands as an act of self-expression. Others buy them as an act of social emulation. They want to wear the same brands as the people they aspire to be. The Chinese are more likely to be this second type of buyer, according to Lingjing Zhan of Hong Kong Polytechnic University and Yanqun He of Fudan University. And, other studies suggest, such status-seeking consumers are more likely to buy counterfeits.

A Prada handbag is a bundle of two things: a well-made product and a well-marketed brand. But some consumers value prestige, not quality. Fakes allow shoppers to "consume" the prestigious brand without buying the high-quality good, as Gene Grossman of Princeton and Carl Shapiro, now of the University of California, Berkeley, pointed out in a seminal 1988 paper. This unbundling no doubt drives Prada and others mad, but it would seem to be a boon to consumers.

Or is it? As Messrs Grossman and Shapiro also point out, a luxury brand confers status only because it is exclusive. It has to be “widely popular but not widely accessible”, as one marketing professor puts it. People who buy Prada are paying for exclusivity. The devils who wear counterfeit Prada erode that exclusivity, imposing an “externality” on owners of the genuine article.

As counterfeiters rush to replicate a brand, the brand owners fight to distinguish themselves from the fakes. In a recent paper, Yi Qian of Kellogg School of Management studies the response of branded Chinese shoemakers to an influx of fakes after the government shifted its enforcement efforts to more urgent things, such as stamping out counterfeit food, drugs and alcohol. Many shoemakers reacted by improving the quality of their footwear, importing Italian pattern-pressing machines and using pricier materials, such as crocodile skin. Their response contradicts the popular notion that fakes inhibit innovation and investment. But firms also raised prices by more than was warranted by their extra costs. Buyers of fakes therefore impose a cost on people who want to buy the real thing. They make brands less exclusive—or more expensive.

But it is possible that buying genuine luxuries imposes an externality of its own. Status, after all, is a “positional” good. To be top of the social heap, it is not enough to have fine things. Your things need to be finer than everyone else’s. Someone who buys a more expensive watch or car to climb up the social ladder forces other social climbers to spend more to stay ahead. In making their purchase, they will carefully weigh how much prestige their big spending will buy. But they will not take into account how much extra everyone else will now have to spend to preserve their social position. As a result of these “arms races”, China may be overspending on luxury goods. Its shoppers account for only 6% of the world’s consumer spending, but, according to figures released by Bain Consulting last month, they now account for 20% of global sales of luxury goods.

Sympathy for the devil

These wasteful status games are not confined to China’s finely dressed elites. In China’s villages, people cement their position in the local pecking order by hosting expensive weddings, funerals and other ceremonies for their own family and buying costly gifts for other people’s. Xi Chen and Ravi Kanbur of Cornell University, and Xiaobo Zhang of the International Food Policy Research Institute, have studied the “gift-books” kept by households in 18 poor villages in the mountains of Guizhou, a southern province. They found that the poorest households (those living on less than \$1 a day at purchasing-power parity) spent about 30% of their budgets on gifts and festivals, twice as much as similarly impoverished Indians. When a household enjoyed a sudden windfall—such as compensation for requisitioned land—they would spend more, forcing everyone else to keep pace. Economists fret that Chinese investment is marred by wasteful prestige projects, orchestrated by local bigwigs seeking to outdo one another. Perhaps its consumption is not that different.

Fonte: The Economist, London, v. 403, n. 8790, p. 79, June 23th-29th, 2012.