

Modern Day Merchant Guilds: Supply Chains and Informal Property Rights Enforcement

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Property Rights under “Anarchy”

Expectation: Markets generate informal property rights enforcement

Mechanism: Firms “punish” states for violating other firms’ rights

But expropriation sometimes happens

When do market pressures deter expropriation?

- When will one firm help enforce another firm’s contract?

Argument

Firms will enforce contracts that provide them an indirect economic benefit

Historical: Merchant guilds linked economic interests of their members

Modern day: Supply chains link firms in the chain

Model Primitives

Players: Host government, target firm, and partner firms

Uncertainty about host's temptation to break a contract with target

Partner firms benefit when the target is protected

Partner firms invest effort in protecting the target

Model Results

Parameter	Impact on Breach
Economic links	Decrease
Government capacity	Increase
Value of target firm	Decrease
Number of partner firms	Increase

Multi-Method Empirics

Observational data: Intra-firm trade and investment arbitration

Expert survey of US MNCs in Russia (October 2013)

Case studies of MNCs in Azerbaijan

Expert Survey: Dependent Variables

Prompts: “Sometimes, government actions ...

- ... **lower the value** of foreign investments in ways that violate contractual obligations or general expectations of fairness.”
- ... **transfer ownership** of foreign investments to the state or state-owned entities.”

Responses:

- Past experiences
- Beliefs about future experiences

Expert Survey: Explanatory Variables

Parameter	Measure
Economic links	Russian suppliers Joint venture with a Russian entity
Government capacity	Interactions with SOEs Foreign-owned market share
Value of target firm	Size of Russian investments Sales in Russia

Results: Current and Future Concerns about Breach

	Lowers value	Transfers ownership	Total breach
<u>Firm Economic Links</u>			
Proportion of Russian suppliers [†]	(+) ^{***}	(+) ^{***}	(+) ^{***}
Joint venture with Russian entity	(-)	(-)	(-)
<u>Government Capacity</u>			
Interactions with SOEs	(+) ^{**}	(+) ^{**}	(+) ^{**}
Foreign-owned market share	(-)	(-) ^{***}	(-) ^{**}
<u>Value of Target Firm</u>			
Size of Russian investments [†]	?	(+) ^{**}	(+) ^{**}
Sales in Russia	(-)	(-)	(-)
Observations	47	49	47

† Expected sign reversed because of excluded category
Control variables: immobile industry, years in Russia

Results: Breach and Deterrence in Azerbaijan

BP and Barmek: Major investors into immobile assets

BP has *krisha* (roof) established by local suppliers

- Stable contract (1994-present)

Barmek “tried to act independently” – Baku official

- Stable contract (2001-2005)
- Expropriation, criminal cases (2006)

Conclusion

Supply chains as modern day guilds: Link economic activities

Incentive for outsourcing

MNCs do not always protect each others' rights