Foreign Direct Investment in Latin America:

Perspectives of the Major Investors

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MADRID, 1998

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INTER-AMERICAN DEVELOPMENT BANK
INSTITUTE FOR EUROPEAN-LATIN AMERICAN RELATIONS

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COPYRIGHT IDB/IRELA 1998
ISBN 84-88607-30-X
DEP. LEGAL M-28690-1998

Printed at Rumagraf, S.A.
Av. Pedro Díez, 25
E - 28019 Madrid

Cover Design: Antonio Escot

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CONTENTS

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FOREWORD

Flows of foreign direct investment (FDI) have continued to increase rapidly in the past few years and have become one of the main driving forces in the process of economic and financial globalization. In Latin America and the Caribbean, inflows of FDI have risen more than fivefold since the beginning of the 1990s in an environment of increasing price stability, the implementation of reforms and the recovery of economic growth. Foreign direct investment has continued to increase even in conditions of instability and volatility in the international financial markets, and represents an increasing share of overall capital inflows to the region.

Though in many ways still linked to the process of privatization in the countries of the region, flows of FDI are a growing share of new investments that contribute to the introduction of new technologies and the improvement of production capacities. Furthermore, the intensification of regional integration and cooperation has contributed to enhance the attractiveness of foreign investment in a number of areas, while at the same time giving rise to a new phenomenon of intra-regional investment.

In an effort to contribute to the study of this most important aspect of the region's development, the Inter-American Development Bank (IDB) and the Institute for European-Latin American Relations (IRELA) jointly published two previous studies on the subject: the first one in 1993 under the title of *Foreign Direct Investment in Latin America and the Caribbean: An Overview of Flows from Europe, Japan and the United States, 1979-1990*; and the second in 1996 with the title of *Foreign Direct Investment in Latin America in the 1990s.*

As a continuation of this effort, the present publication attempts to focus in greater detail on the analysis of FDI flows to Latin America and the Caribbean from the vantage point of and on the basis of statistical sources from the main investor countries. We expect that this third publication will contribute to a better understanding of recent developments concerning flows of FDI.

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ACKNOWLEDGEMENTS

This project was carried out by a joint IDB-IRELA research and editing team, formed by Ziga Vodusek from the IDB Special Office in Europe, Alvaro Calderón (currently with ECLAC) and Jaime Crispi from IRELA, on the basis of contributions received for individual chapters. The contributors were Michael Mortimore (United States), Shikegi Tejima (Japan), Alfredo Arahuetes (Spain), Ramon Casilda (Spain), Peter Nunnenkamp (Germany), Peter West (United Kingdom), Maryse Raffestin (France), and Luis Jorge Garay and Arturo Vera (Intra-regional investment). Georg Saul was responsible for the methodology and systemizing the data base. Comments on the text were received from Robert Devlin, Valpy FitzGerald, Ricardo Ffrench-Davis and Luis Jorge Garay. Thanks go to Mary Stanier, María Dolores Azategui, Justin Byrne, Andrew Crawley, Elizabeth Joyce and Marcelo Pollack for editorial help. Acknowledgements of assistance in obtaining information and data are due to Jan Atteslander, Herbert Oberhänsli and Patrick Métral, and to all institutions that generously provided us with the latest available FDI data, including government offices, central banks and statistical agencies of the United States, European countries and Japan, as well as the OECD. Special thanks in this respect also go the Economic Commission for Latin America and the Caribbean (ECLAC).

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PRESENTATION AND SUMMARY

Introduction

Over the last five years, Latin America and the Caribbean as a whole have attracted record levels of foreign direct investment (FDI). As a result, the region now ranks second among the developing regions in terms of total FDI flows, outstripped only by South and South East Asia (largely due to the fact that China is currently the second most important recipient country in the world after the United States). FDI, therefore, is playing an increasingly important role in the economic development of Latin America and the Caribbean. This upsurge in foreign investment is closely linked to the economic stabilization and reform programmes being implemented throughout the region. The liberalization of investment regimes and the progress made towards regional integration, combined with extensive and far-reaching reforms (including privatizations and concessions for the construction of infrastructure), appear to have helped make Latin America an ever more attractive area for investment.

In the 1990s, FDI has accounted for an increasingly large proportion of all capital flows to Latin America. In 1997, the region is estimated to have absorbed some $42 billion in FDI, or around 45% of total capital flows of $93 billion. This compares, according to World Bank figures, with 20% and 38% of total capital inflows in 1980 and 1990, respectively. Given the region's considerable dependence on foreign capital, and the highly volatile nature of short-term capital flows, it should be noted that, since FDI is less vulnerable to cyclical factors and fluctuations in global financial markets, it has continued to flow to the region even though conditions have not always seemed propitious. This is confirmed by the scant impact of the Mexican financial crisis at the end of 1994 on FDI flows, as well as the apparently limited consequences of the current crisis in Asia on investment in the region.

During the 1990s, FDI flows to Latin America and the Caribbean have been on average almost five times higher than during the previous decade. According to figures by the United Nations Conference on Trade and Development (UNCTAD), FDI flows in 1995 accounted for 11% of gross capital formation in the region, while the total stock of FDI constituted 18.4% of its GDP. These figures confirm the current importance of FDI for capital formation in the region. Foreign investment, however, does not merely have a major quantitative impact on economic growth through its contribution to increasing the capital stock in

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the region's economies, but is also associated with other positive effects, including a more efficient allocation of resources, technological transfers and the improvement of productive inputs, the promotion of exports, and greater competition in the domestic, recipient market.

Since 1993, the Inter-American Development Bank (IDB) and the Institute for European-Latin American Relations (IRELA) have been collaborating in the study of FDI in Latin America. The objective of this joint initiative is to contribute to both qualitative and quantitative knowledge of an issue which is of vital importance to the region by analyzing statistics provided by the investor countries. The first general study, which was published in 1993, provided a geographic breakdown of FDI flows from the leading investor countries, particularly the United States, the main European countries and Japan. This study was updated in 1996 to include an extensive data base covering a larger number of countries, and focusing on the importance of the privatization process and regional integration in attracting FDI to the region.

This new study offers a more detailed analysis of FDI in Latin America and the Caribbean during the 1990s from the perspective of the main investor countries. It seeks, on the one hand, to quantify the phenomenon and, on the other, to examine the factors which influence the investment decisions of foreign companies operating in the region. Extensive analysis is provided of six investor countries, as well as of intra-regional investment. The six investor countries studied are the United States, Japan, Spain, the United Kingdom, Germany and France, and in each case the analysis considers the specific characteristics of each country's FDI. The quantitative analysis focuses on FDI flows and stocks in the period 1990-96, broken down by recipient country and leading economic sectors for investment, while the qualitative analysis examines the regional investment strategies adopted by the transnational corporations (TNCs) from these countries. Apart from these countries, FDI from Switzerland, Canada and Asian countries other than Japan are also examined briefly.

Contents

The chapters dedicated to the different countries share a number of features with respect to the quantitative analysis of the evolution of FDI in Latin America and the Caribbean, the geographic and sectoral distribution of investment, and the position of Latin America in comparison with other developing regions. At the same time, however, the specific characteristics of FDI from each investor country are also examined. This is reflected in the different analytical focus of each chapter, which concentrates on those aspects that are of greatest importance

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for an understanding of the evolution of FDI in the country in question. Some of the more distinctive aspects of these chapters are outlined below.

Subject matter by chapters

As its title suggests, Chapter I provides a general overview of capital flows to the region, focusing particularly on direct investments. This chapter examines Latin America's place in the global context of FDI flows, and briefly discusses some of the strategies adopted by trans-national corporations (TNCs) with investments in the region. An analysis is also provided of some of the general trends in FDI over the last few years, as well as the quantitative and qualitative effects of a number of specifically Latin American developments on FDI; these include the privatization processes, regional integration and new forms of investment such as mergers and acquisitions (M&A).

This chapter also includes four boxes which discuss a number of important issues that, given the character of the book, are not treated in detail elsewhere. Since the book concentrates essentially on FDI from the perspective of investor countries, Box 1 offers some general considerations about the potential impact of FDI on recipient countries. In Box 2, the interested reader can find a brief overview of the main theoretical issues and debates, as well as bibliographical references to a number of works exemplifying different theoretical approaches to the analysis of international business. Boxes 3 and 4 briefly examine the scale and nature of FDI from two countries which, although major investors in the region, are not the subject of specific chapters. Box 3 provides an overview of the FDI operations involving Swiss TNCs in the region and Box 4 looks at FDI from Canada.

Chapter II presents a detailed analysis of the recent pattern of FDI from the United States, the largest foreign investor in Latin America and the Caribbean. After examining the upsurge in global flows of US FDI during the 1990s, the chapter goes on to argue that US FDI in Latin America and the Caribbean has also undergone significant qualitative changes over the last few years. These changes reflect the transformation of the business environment in the region, as well as the increasing global competition facing US TNCs. Traditionally, US investment in the region (especially in manufacturing industry), was clearly oriented towards supplying the protected Latin American markets during the import substitution period. To this end, US TNCs set up replicas of their US plants in the region. These used imported inputs to produce for national or sub-regional markets. However, the structural changes which have taken place in the global economy and in the national economies of Latin America over the past few

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decades have obliged these companies to make significant changes to their strategies.

As a result, it is possible to identify two new types of investment strategies which are followed by US TNCs in Latin American and the Caribbean. The first consists of investments in manufacturing industry in order to strengthen their competitive position in the US market with respect to TNCs from other countries. The second involves participation in the privatization of the energy and service sectors in the region. In this way, US TNCs seek to ensure their share of the expanding national and sub-regional markets in the face of increasingly intense global competition from the TNCs of other countries also operating in these sectors. The importance of the first strategy is exemplified by an analysis of the investments made by US TNCs in both the Mexican automobile industry and the *maquiladora* assembly plants in the Caribbean Basin. With respect to the second strategy, data is provided on the rapid expansion of US TNCs in the tertiary and energy sectors, especially through the acquisition of stakes in privatized companies.

Chapter III examines Japanese FDI in Latin America and the Caribbean. Analyzed within the broader context of the internationalization of Japan's economy over the last two decades (not least in response to the appreciation of the yen since the 1970s), evidence shows that the region has become increasingly attractive to Japanese TNCs over the course of the 1990s. This, it is argued, reflects the combination in recent years of a series of pull factors from Latin America and push factors affecting Japanese FDI. Foremost among the pull factors are the upturn in the region's economy, the introduction and consolidation of economic reforms, the region's new investment opportunities created by privatization and concession programmes, and the progress made towards sub-regional integration. The push factors include the saturation of the Asian markets (traditionally key recipients of Japanese FDI), and the desire of Japanese TNCs to diversify their investments.

The chapter subsequently examines the position held by Latin America in the global production of Japanese TNCs. In this respect, an important finding is that a large proportion of Japanese FDI in Latin America is devoted to meeting regional demand. Some 75% of sales by Japanese TNCs are made in local or sub-regional markets, while only 4% of their production is exported to Japan. This is a very different situation from that of the Japanese-owned companies in countries belonging to the Association of South East Asian Nations (ASEAN), which export around 25% of their production to Japan. There is a clear link between the market orientation and sectoral distribution of Japanese investment in the two regions. Whereas in the ASEAN countries, 75% of Japanese FDI is

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concentrated in manufacturing industries (with relatively standardized, low-wage production), in Latin America and the Caribbean manufacturing industry accounts for only half of all Japanese FDI.

More recently, however, the sectoral distribution of investment has begun to change, with increasing Japanese investment in assembly operations, particularly in the automobile and electronics industries. Most of these investments are concentrated in Brazil and Mexico (the largest recipients of Japanese FDI in the region), where the TNCs seek to take advantage of growing markets, as a result of the integration processes in which these countries are involved – the Southern Common Market (*Mercado Común del Sur,* MERCOSUR) and the North American Free Trade Agreement (NAFTA), respectively. Here it is argued that the future expansion of this type of operation will partly depend on the ability of Japanese TNCs to establish relations with their suppliers and employees in the region of the type that exist in Japan. This is because part of their "ownership advantages" are derived from the institutional structure of Japanese labour and supplier markets. The existence of stable, long-term trade relations with both employees and suppliers gives assembly companies in Japan advantages over countries where these relations operate on a short-term basis. In a bid to recreate these conditions in Latin America and the Caribbean, Japanese TNCs have encouraged their Japanese suppliers to engage in FDI in the region (fuelling the increase in small- and medium-sized Japanese companies operating there) and tried to forge long-term relationships with local suppliers.

Spanish FDI in the region is analyzed in Chapter IV. This chapter first examines the historical background for Spanish foreign investment, which only began to acquire real significance after the restructuring of Spain's economy in the 1970s. From 1974 onwards, a major increase in FDI outflows was accompanied by significant qualitative changes in the character of investments, as well as marked differences in terms of the destination of these flows. The 1970s saw a growth of Spanish FDI in Europe and the United States, as companies developed export networks and, in the case of banks, gained a foothold in the main international markets. In Latin America, however, most FDI was intended to exploit technological advantages and secure a share of the protected markets in the region.

A second upsurge in FDI came in the wake of Spain's incorporation into the European Economic Community in 1986. For a number of years, the greater volume of Spanish investment in Latin America did not prevent the region's share of total Spanish FDI from falling. However, during the 1990s, and especially since 1994, the region has attracted an increasing proportion of total

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Spanish FDI. After analyzing in detail the geographic and sectoral distribution of Spanish FDI in recent years, this chapter goes on to consider the nature and determinants of the strategies followed by the main TNCs with investments in the region.

One important feature of recent Spanish FDI in the region is the way it is highly concentrated in the service sector (telecommunications, banking and transport). This is explained by the combination of the particular "ownership advantages" of Spanish TNCs, on the one hand and the "locational advantages" offered by the region, on the other. The former comprise intangible assets related to cultural and linguistic ties, the large scale of their operations and the oligopolistic position that some companies investing in Latin America enjoy in their domestic market. In the tertiary sector, the locational advantages are related to the size and growth of the Latin American markets in these sectors and the new regulatory framework for FDI. These factors are highlighted in three boxes which focus on Spanish investment in banking, telecommunications and oil and natural gas.

German FDI in the region is examined in Chapter V. The internationalization strategy adopted by German companies has traditionally been much more export- than investment-oriented. Thus, from a Latin American perspective, Germany seems to be a less important investor than other European Union (EU) countries or the United States. Yet from the German perspective, Latin America and the Caribbean account for a large proportion of its FDI in the developing regions. After examining the recent evolution of FDI in different sectors and countries, and the particular characteristics of German investment, the chapter focuses on two particularly significant questions. First, from the German perspective, it discusses the important issue of the potential impact of German FDI in Latin America on the domestic labour market. This is followed by an examination, from the Latin American perspective, of the possibility that the emergence of new investment opportunities in other developing regions or countries in transition (especially Central and Eastern Europe) may lead to a diversion of German FDI from Latin America.

With respect to the first question, indirect evidence suggests that German FDI in Latin America does not have a significant impact on the level of employment in Germany. German investment in Latin America (and in other regions) has mainly focused on exploiting the market rather than relocation in search of lower costs. Therefore, the effect on employment in Germany is negligible. Furthermore, the empirical evidence suggesting that there is a

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positive correlation between German FDI and exports from Germany to FDI recipient countries, appears to indicate that FDI and exports complement, rather than substitute, one another. Equally, over the last few years, the sectors with the highest levels of German FDI have also benefited from above average levels of job creation in Germany itself.

These findings are also relevant to the second question. The fact that German FDI in Latin America and the Caribbean is largely directed towards supplying local markets (concentrated particularly in manufacturing industry and in the largest countries) means that the emergence of new investment opportunities in Central and Eastern Europe and Asia is unlikely to have a very significant impact on Germany's traditional investments in the region. Nonetheless, from a Latin American perspective, the other side of the coin is that German investors have proved to be very unresponsive to the positive developments in the region; there has been very little German involvement in privatizations, for example. The explanation for this relative inflexibility appears to lie in specifically German factors. Foremost among these is the preference of German companies for exports, and the incapacity of the state-owned companies and/or those in highly regulated areas of the service sector to bid for privatized companies or concessions in Latin America and the Caribbean. This chapter also includes a box outlining the operations and strategies of German automobile companies in Latin America.

Chapter VI examines the evolution of British FDI in the region. The United Kingdom has been the second largest source of foreign investment worldwide for over two decades. Although Latin America is not a very important destination for British FDI, the latter still represents a significant proportion of all FDI in the region. After outlining the historical importance of British investment over the course of the century, the chapter goes on to analyze the recent pattern of British FDI in Latin America and to draw comparisons with British investment elsewhere. This shows that, as far as the developing regions are concerned, Asia has been the most important destination for British investment over the last few decades. During the 1980s, in particular, British investment in Latin America was almost entirely confined to companies with well-established links in the region. Moreover, British TNCs have been slower than their counterparts in other investor countries to respond to the greater political stability and new economic opportunities in the region.

Although this response has been rather slow, it is already possible to identify a number of interesting sectoral trends in British FDI to Latin America and the Caribbean. While the split between manufacturing and non-

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manufacturing sectors (approximately half and half) is similar to that of British FDI in other regions, the distribution of investment within these sectors is rather different from the general pattern. In particular, within the non-manufacturing sector, there is an unusually high concentration of investment in the energy sector, while financial services account for a smaller proportion of the total in Latin America than elsewhere.

This chapter then presents information on a number of recent investments and discusses the relatively scant participation of UK companies in the privatization processes in the region. Although Latin America has generally not been seen as a priority by British companies establishing international networks in the service sector, there is evidence that some recently privatized British companies are beginning to take an interest in the privatization processes there. Finally, the results of a British government study of companies' foreign investments are analyzed in a box. One important finding of this study is that, as in the case of Germany, the search for cost reductions does not appear to be, at least explicitly, a decisive factor for British investors. As a result, rather than leading to job losses in the United Kingdom, FDI has tended to boost employment in the country by fuelling increased demand for British products.

Chapter VII examines French FDI in Latin America and the Caribbean. Despite their historical ties with the region, French companies showed little interest in Latin America before 1996. This reflected a series of factors in France as well as in Latin America and other regions. The first causal factor is the heavy concentration of French FDI in Europe, as a consequence of the consolidation of the Common Market in the mid-1980s. A second factor is the negative impact that the political and economic instability which afflicted much of Latin America for many years had on French investors' image of the region. Finally, a third, decisive reason for the scant interest shown by French TNCs before 1996 was the competition for French capital from other developing regions (Asia and Central and Eastern Europe).

Since 1996, however, there has been a major upsurge in French investment in Latin America. This has been characterized by significant differences according to the sectors of origin. An analysis of the sectoral and geographic distribution of recent French FDI in the region is followed here by an examination of the strategies adopted by companies in the different sectors. This shows, for example, that French companies which have long been involved in the exploitation of natural resources have now modernized their operations and redirected their production towards regional markets. At the same time, the large

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French industrial groups appear to be pursuing continent-wide strategies in order to rise to the challenges created by the new regional markets and to compete for market shares from TNCs from other countries. In the service sector, on the other hand, French TNCs have taken advantage of the opportunities created by privatization processes to penetrate new markets. Finally, there has also been an increase in investment by small and medium-sized French enterprises in the region.

Despite the particular characteristics of French FDI in the different sectors, the analysis also shows that there are some common trends. Perhaps the most important of these is that French FDI has primarily been oriented towards supplying local markets rather than relocating production in an attempt to reduce costs. This is the conclusion to be drawn, for example, from the relatively low levels of intra-group trade. This chapter also includes a box analyzing the role of French companies in the privatization programmes, an appendix with details of recent French FDI operations in the region, and another which sets out the definitions, statistical sources and methodologies used in the analysis.

Finally, Chapter VIII examines the increasingly important but previously little studied phenomenon of intra-regional FDI in Latin America and the Caribbean. The chapter begins by considering some theoretical issues relating to the potential impact of regional integration on FDI, before outlining the evolution of intra-regional FDI in Latin America and the Caribbean as a whole, and analyzing some specific cases. These include investment flows between the members of MERCOSUR, investments by Chilean companies in the rest of Latin America, FDI flows within the Andean Community (*Comunidad Andina*), and Mexican investment in other countries in the region. One reason for the scant attention paid to intra-regional investment in Latin America and the Caribbean is the lack of comprehensive standardized data on the subject. This chapter makes an important contribution in this respect, by systematizing data on intra-regional investment in the 1990s from national sources in the investor and recipient countries. The inherent difficulties of this task are compounded by the scarcity of information, in some cases, and in others by the different methods used to record the data.

Nonetheless, the available data reveals that, despite the considerable growth in recent years, intra-regional investment still accounts for only a very small proportion of total FDI in the region. In terms of the destination of flows, intra-regional FDI tends to concentrate in a few sectors, particularly those in which investor companies already operate in their home markets. While FDI within MERCOSUR is largely concentrated in some branches of manufacturing industry,

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most intra-regional investment in the Andean Community goes to the service sector. Chilean FDI, meanwhile, is particularly highly concentrated both in terms of geographic areas (Argentina and Peru) and economic sectors (energy), while most Mexican investment flows go to Central America. With respect to the future prospects for intra-regional investment, the continual consolidation and expansion of sub-regional integration processes should lead to greater investment in the manufacturing industry, as well as the formation of partnerships which may eventually serve as the foundations for the development of local multinational companies. The chapter ends with an appendix which briefly outlines the regulatory framework for FDI in the region.

General themes and trends

Despite their emphasis on the particular characteristics of FDI from the different investor countries, the country-by-country analyses also reveal a number of broader, more general themes. From the Latin American perspective, macroeconomic stabilization, trade and financial liberalization, the promotion of private activity (particularly through extensive privatization programmes and the incipient concession programmes), the introduction of more liberal regulatory frameworks for foreign investment, and the regional integration initiatives, have all roused the interest of foreign investors from different regions. The new national and international environment has attracted increasing inflows of investment from companies already operating in Latin America (which have adapted, expanded, and restructured their operations), as well as from newcomers determined to take advantage of the new opportunities in the region.

Over the last few years, a significant proportion of FDI flows have consisted in the transfer of assets, first from the public sector (privatizations) and more recently among private agents (M&A). In a more competitive climate, the acquisition of companies constitutes a way of accessing markets with high growth potential. At the same time, and in response to the major financial demands posed by these operations, strategic alliances (both between foreign companies and between foreign and local firms) have become increasingly common features of the business landscape in Latin America and the Caribbean.

In terms of the destinations of FDI in the region, Brazil has replaced Mexico as the main recipient country, essentially due to the success of its economic stabilization programme, the accelerated privatization processes, and the progress made with respect to regional integration (MERCOSUR). Although the service sector has attracted most foreign investment over the last few years (mainly as a result of privatizations), manufacturing industry can be expected to

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regain momentum in the years to come. In this respect, the ambitious investment programmes currently being implemented by leading car manufacturers, and the massive M&As taking place in the food and chemical industries provide grounds to expect that the new Latin American affiliates could become important components of the integrated global production systems now being established by leading TNCs. The liberalization of the recipient economies in Latin America and the Caribbean is creating favourable conditions for the development of competitive companies in a wide range of economic sectors.

Apart from the traditional sectors, the new expanded FDI flows have gone into sectors which used to be closed to foreign capital. This is the case of the investments in mining (copper, iron, gold, silver, etc.) and hydrocarbonates (oil and natural gas) through the formation of joint ventures, tenders for new, unexploited reserves, and/or the transfer of state-owned assets. Foreign investors have also begun to play a leading role in the service sector, particularly in banking and public utilities (telecommunications, electricity generating and distribution, and water supplies).

In terms of the investor countries, the United States has retained its position as the largest investor in Latin America and the Caribbean. Recently, however, other investors, and particularly the European countries, have expanded their presence in the region. Many companies (both in manufacturing industry and the service sector) from Spain, the United Kingdom, Germany and France are restructuring or launching new operations, each with different strategies. Meanwhile, Asian investors, particularly from Japan, South Korea and Taiwan, have begun to integrate Latin America and the Caribbean into their global strategies. In highly competitive industries such as automobiles, electrical products and clothing, Asian companies have begun to invest in Mexico and some Central American and Caribbean countries in order to benefit from their proximity to the US market, as well as the tax incentives and low wage levels offered there. Much of this investment has gone into the creation of *maquiladora* assembly plants.

The analysis presented in this book, therefore, highlights that the strategies of foreign companies investing in the region vary in accordance with a number of different factors: notably, the company's country of origin, the nature of the recipient economy, the sector in which they invest, and the type of investment made. Without aspiring to offer a full analysis of all these factors, it is possible to identify a number of basic elements which shape the strategies of TNCs investing in Latin America and the Caribbean. In terms of the nature of the companies involved, most FDI in the region is made by large TNCs. Given the

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considerable concentration of FDI in the largest countries (Brazil, Mexico and Argentina), on the other hand, it is hardly surprising that their main reason for investing tends to be production for local markets.

This is an interesting finding. Traditionally, production for the local market largely involved investment in manufacturing sectors protected by high tariff barriers. Today, even though investment takes places in more open economies and in an increasingly deregulated and liberalized environment, this incentive still operates. The growth of local markets during the 1990s, their enlargement at the sub-regional level as a result of the integration processes, and intensified global competition among TNCs, is forcing them to make new investments and introduce qualitative changes in their production methods if they are to conquer new markets, or to expand – or even simply maintain – their share of the markets in which they are already established. In recent years, this type of investment has characterized the manufacturing industry, particularly in the Mexican automobile industry and MERCOSUR, in a process dominated by European, US and Asian companies.

Cost reduction, on the other hand, does not appear to constitute the main reason for investment in the region by European TNCs. Relocation to cut costs is explicitly identified as the principal incentive for investments in only a few cases, notably for US automobile companies in Mexico (and by other manufacturers in Central America and the Caribbean) and some Japanese assembly operations. Most of these involve the production of goods for export to the United States. Given the non-tradable nature of most services, FDI in this sector is also almost entirely directed towards local markets. Within the service sector, the main investments are in public utilities (telecommunications, energy, and water), banking and commerce. Spanish and French companies have been particularly prominent in these areas, accompanied to a lesser extent by US and British companies.

In terms of the impact of FDI on the investor country, the evidence presented here (particularly in the chapters on Germany and the United Kingdom), suggests that investment abroad has little effect on the level of employment in the country of origin. In fact, there are some indications that, in certain cases, FDI may actually generate additional demand for products from the country of origin, thereby increasing the level of activity and employment.

The aggressive internationalization strategy being followed by a number of leading Latin American companies (particularly from Chile and Mexico), should also be highlighted. One consequence of this is the increasing importance of

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regional capital in total FDI flows. This implies that intra-regional investment can be expected to grow in the years to come. Equally, as this process is consolidated, new regional economies (particularly the smaller ones) are also likely to participate.

A note on the statistics

It should be emphasized that, for analytical purposes, given the distinct methodologies used in different countries, the figures presented in this book have not been compiled and aggregated on the basis of a common definition, and neither do they all include exactly the same components of FDI (particularly as far as reinvested earnings are concerned). This inevitably affects the comparability of the data. Furthermore, the great volatility of FDI flows means that the data on flows in particular should be treated with caution, especially when the figures are recorded on an annual basis. Annex I in this book discusses these and other questions concerning the definitions of FDI, the methods used to measure and compile data, and the problems involved in attempting to identify the final destination of flows. This annex also examines a number of issues relating to the preparation and presentation of the data base included here. An understanding of these questions is vital in order to be able to compare the data for different countries. The reader is therefore recommended to consult this annex in order to avoid misinterpretation of the statistics provided here.

The data for FDI flows and stocks used throughout this book are given in Annex II. This includes detailed figures on FDI in Latin America and the Caribbean, broken down both by investor and recipient country, as well as the trade areas in the region. This information has been obtained from the central banks and statistical agencies in the investor countries. In the case of flows, the figures refer to net flows of FDI as reflected in the balance of payments figures of the investor countries. These figures differ from the FDI data provided by the recipient countries and published in the International Monetary Fund's Balance of Payments Statistics. These two series are not directly comparable. Where available, Annex II also provides a series of figures on the levels of FDI stock of the main investor countries. In the case of Japan and Spain, the balance of payments data are only disaggregated for a limited number of countries. Therefore, in order to complete the statistical series, an estimate was made on the basis of the records for authorized investments.

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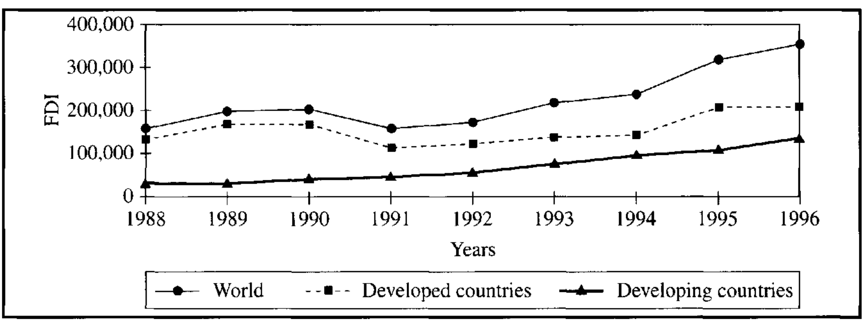
CHAPTER I

FOREIGN DIRECT INVESTMENT IN LATIN AMERICA AND THE CARIBBEAN: AN OVERVIEW*

Introduction

Foreign direct investment (FDI) has become a key aspect of the globalization process that is reshaping the world economy at the end of the 20th century. During the 1990s, there has been a major expansion in worldwide flows of FDI, which have grown from an annual average of $142 billion between 1985 and 1990 to almost $350 billion in 1996. This process has reinforced the already important role that transnational corporations (TNCs) play in most national economies, both in industrialized and developing countries (see Graph 1).[1] Their significance is such that, according to data from the World Trade Organization (WTO), trade among TNCs accounts for one- third of all world trade and their exports to other unrelated destinations represents a further 33%, while the remainder comprises transactions between national companies.

Graph 1
Global FDI Flows
(millions of US$)



Source: IRELA-IDB based on data in UNCTAD (1997).

* This chapter was prepared by Álvaro Calderón, Economic Affairs Officer in the Unit on Investment and Corporate Strategies of the Division for Productive Development of the United Nation's Economic Commission for Latin America and the Caribbean (ECLAC) and former Deputy Director of the Institute for European-Latin American Relations (IRELA), and Ziga Vodusek, Senior Economist in the Special Office in Europe of the Inter-American Development Bank (IDB).

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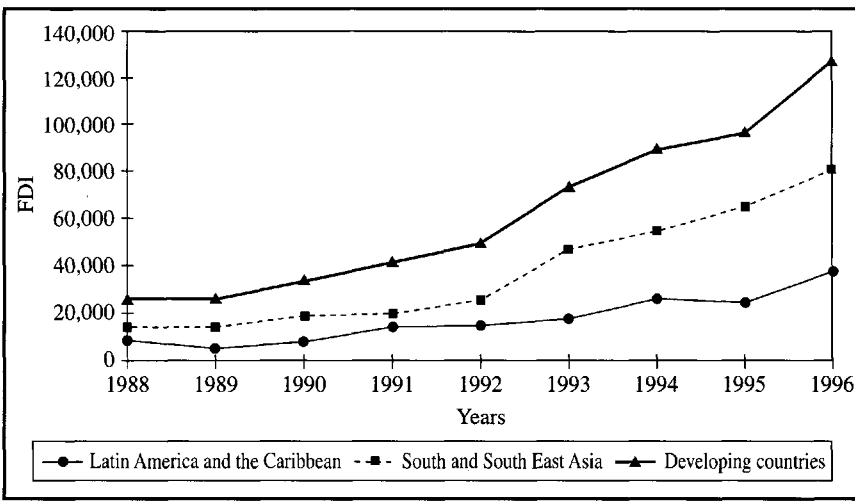
The present boom in FDI has been characterized by the increasing importance of capital inflows to the developing economies (which absorbed 16.5% of all FDI in 1990, rising to 36.9% in 1996), as well as the pre-eminence of the United States and the United Kingdom as sources of foreign investment. If the present trend continues, a growing number of countries will be incorporated into this process.[2]

Between 1991 and 1996, the developing countries received an average of almost $80 billion a year in FDI, most of which was concentrated in South and South East Asia (62.3%) and Latin America and the Caribbean (29.3%) (see Graph 2). During this period, much of this growing flow of capital went to China, which alone absorbed one-third of all the FDI in South East Asia. However, despite the increasing geographic diversification of FDI in the developing countries, the bulk of these inflows of capital still goes to a relatively small number of recipient countries. In 1996, 34.2% of all FDI in the developing countries was concentrated in just six recipient countries (excluding China): Brazil, Singapore, Indonesia, Mexico, Malaysia and Argentina.

Graph 2
FDI Flows to Developing Regions
(millions of US$)



Source: IRELA-IDB, based on data in UNCTAD (1997).

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During the 1990s, economic reforms and macroeconomic stability in Latin America and the Caribbean have significantly improved the region's image in the eyes of foreign investors. At the same time, the new opportunities in the region (especially those related to privatizations) encouraged the expansion of FDI inflows, which reached $38 billion in 1996 and topped $45 billion in 1997 (see Table 1). As a result, the region has emerged as an increasingly important market, and a key component of the global strategies being developed by the world's leading TNCs.

Turbulence in Capital Markets: the Evolution of FDI

During the 1990s, despite the uncertainties and fluctuations in the world's capital markets, Latin America has reinforced its position as an "emerging market" and gained an increasing share of the portfolio held by international investors from the developed world. The introduction of new mechanisms of external financing (particularly stocks and bonds) resolved the problem of the strict external restrictions on investment which existed in many Latin American economies.

The gradual improvement in the structural bases of the region's economies (owing to the implementation of macroeconomic adjustment programmes and major economic reforms), has strengthened their capacity to react to external shocks. The progress made in this respect was exemplified by the region's rapid recovery after the Mexican financial crisis at the end of 1994.[3] Generally speaking, the Latin American countries have made satisfactory economic progress in the more favourable international climate existing since 1995. Despite their continued foreign deficits (particularly in their current accounts), the plentiful supply of foreign capital and the major growth in exports (which has more than doubled that of the GDP as a whole) have enabled the governments in the region to maintain and extend their programmes of economic stabilization and reform.

Between the beginning of June and mid-October 1997, a number of the most important countries in South East Asia were hit by serious economic problems.[4] On 23 October, the Hang Seng index (the most important share index in the Hong Kong stock market) suffered the largest fall in ten years (10.4%), dragging most of the world's other stock markets with it.[5] The greatest losses were registered in the emerging markets in Asia and Latin America (Hong Kong, South Korea, Thailand, Brazil, Argentina and Mexico). Four days later, American shares suffered their biggest drop (7.18%) since the crash on 29 October 1987, forcing Wall Street to suspend trading early for the

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first time since president John F. Kennedy was assassinated in November 1963.[6] This critical situation was compounded by the banking crisis in Japan, which provoked the closure of two leading Japanese financial institutions on 17 and 24 November, as well as the devaluation of the Korean won at the beginning of December.

At first, with memories of the "peso crisis" still fresh, Latin America was hit quite severely by the global consequences of the crisis in Asia. This was particularly intense because the markets in the region were the last to absorb the falls in the stock exchanges of Asia, Europe and the United States, thereby increasing investors' fears. Brazil[7] was particularly hard hit, followed by Argentina, Mexico and Peru. It is still too early to gauge the full repercussions and consequences of this turbulence in the capital markets, which may undermine investors' willingness to take risks, as well as affect the value of their operations in the emerging economies. This, in turn, might disturb international financial movements.

However, despite the negative impact of the Asian crisis on both trade and external financing[8], for the time being at least, the Latin American economies have managed to administer and control the effects of this external shock. This was confirmed by the favourable macroeconomic results registered in the region in 1997 (with 5.2% GDP growth and inflation below 11%). In part at least, this situation is a consequence of the region's decreasing financial vulnerability as a result of changes in the composition of its capital inflow (with the growing importance of FDI) and the improved performance of the banking system.

Until now, the consequences of the crisis in Asia have not affected the flow of FDI to Latin America and the Caribbean. However, if the crisis continues, it is highly likely that the region will begin to feel the effects in the medium term. The devaluation of their currencies has made the Asian economies much more competitive, and will thereby help to attract investors from other parts of the world to this region. At the same time, the macroeconomic difficulties facing these countries may affect their foreign investments, as the resources available will essentially be reserved for their domestic economies. Equally, if the financial crisis deepens, the macroeconomic stability of the region, as well as capital flows, might be seriously compromised.

The new pattern of capital flows to Latin America

From May 1995 onwards, Latin America slowly regained access to the international capital markets. The net balance of capital flows to the region rose

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from $25 billion in 1995 to almost $74 billion in 1997. At the same time, the tendency towards a change in the composition of capital inflows which had first appeared at the end of 1995 became much stronger. Incoming capital increasingly consisted of FDI and investment in medium- and long-term debt, particularly bonds. This tendency developed within a favourable international climate, starting with the timely and plentiful international financial aid provided to the region (and to Mexico and Argentina in particular) during 1995, and characterized by the existence of stable interest rates in the United States, and cuts in the rates in both Germany and Japan. Nonetheless, towards the end of 1997 and at the beginning of 1998, this tendency was partially interrupted as a consequence of the crisis in Asia.

The increasing importance of FDI in Latin America is particularly significant in this context, since the instability of the stock markets has had little impact on flows of this type of investment to most countries in the region. FDI inflows which, until 1993, essentially involved privatizations, have now begun to include a significant proportion of new capital. At the same time, reflecting the tendency seen in many industrialized economies, mergers and acquisitions have accounted for a significant proportion of FDI inflows.

Recent events have not only led to changes in the relative importance of the different forms of investment, but have also affected the destination of capital flows to the region. Following the crisis in Mexico, and largely as a result of the *Plan Real*, Brazil has emerged as a major target for international investors. Since 1995, Brazil has received inflows of capital of around $30 billion a year (or almost 60% of the regional total during this period), and a growing part of this investment now consists of long-term financing, essentially in the form of FDI and bonds.[9]

On the other hand, Mexico (the most attractive economy for foreign investors in recent years) recovered rapidly from the crisis at the end of 1994. Mexico's good macroeconomic results and the positive expectations of foreign investors encouraged a major increase in capital inflows, almost half of which consisted of FDI. Moreover, although the crisis in South East Asia has affected Mexico, in early 1998 there is little indication that its consequences will be too serious. Argentina, Chile, Colombia and Peru are the other major destinations for flows of foreign capital to the region.

The great turbulence which has recently affected the stock exchanges has highlighted the essentially volatile nature of many capital inflows. This, combined with the fact that most Latin American economies are vulnerable to

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external shocks, has turned the enthusiasm generated by the massive inflow of capital into growing concern about the most appropriate way of managing these flows.[10]

Changes of Ownership: A Significant Proportion of FDI

Macroeconomic stability, trade and financial liberalization, extensive privatization programmes in the service sector (financial services and the development of infrastructure), the relaxation of regulations governing private investment (both domestic and foreign), and the processes of regional integration have all combined to transform the business environment in Latin America. Above all, there are now greater incentives for established domestic and foreign companies as well as newcomers to invest in the region.

Over the last few years, and despite the seriousness of the financial crisis in Mexico and the turbulent situation in Asia, FDI flows have continued to show sustained growth, reaching a record $45.5 billion in 1997. Despite this, Latin America and the Caribbean have lost ground in terms of the total flow of FDI to developing countries, as the region's share fell from 36.8% in 1991 to 30.1% in 1996 (see Graph 2). During the same period, the South East Asian countries attracted an increasing share of all FDI, above all due to the pull of China.[11]

During the first half of the 1990s, flows of FDI essentially responded to the privatization programmes implemented by a number of countries in the region. Over time, the revenue which governments received in the form of transfers has gradually been accompanied by further substantial inflows of direct investments to modernize these newly privatized companies. Later, massive inflows of capital reflected a new wave of privatizations, mainly involving the transfer of activities previously carried out by the state to the private sector (in the form of concessions), as well as the partial opening up of the great state-owned corporations to private foreign investment. In many cases, foreign investors have joined up with local companies in order to diversify the risks associated with this type of operation. Although, initially at least, these investments do not expand the productive capacity of the recipient country, they have led to an improvement in the quality of services (especially energy and telecommunications), which should have a positive effect on the national economy and, in particular, on the export output of manufacturing industry and mining (see Table 1).

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Privatizations accounted for a smaller proportion of total inflows of FDI in 1996 (in 1991, these acquisitions had absorbed 50% of all flows) (see Graph 3). Although the sale of state-owned companies is now drawing to a close in a number of countries (Argentina, Chile and Mexico, which obtained over $90 billion from this source), there are still some $100 billion worth of state assets in the region, concentrated mainly in Brazil.[12] A few years ago, privatization programmes were seen as a means of attracting foreign capital and helping to overcome the tight restrictions on international financing. At present, given Latin America's more positive image in international business circles, it is difficult to argue that the sale of state-owned assets still constitutes a major incentive for foreign investment.

A new phenomenon in Latin America: mergers and acquisitions

In the United States and Europe, mergers and acquisitions (M&A) have been a widely-used corporate strategy for over a decade. They are now being carried out on a global scale, and starting to become increasingly frequent in Latin America. This development could change the character of companies both in and beyond the region in the next century, as a significant proportion of direct investment from the United States has been used to finance the boom in M&A involving US TNCs.[13] In the first half of the 1990s in Latin America, this procedure was used above all by US companies in Argentina.[14] During the first six months of 1997, the M&A of companies in Latin America accounted for 13% of the world total, outstripping Asia and confirming the growing importance of this type of operation in the region.[15]

The globalization process has encouraged the tendency towards the liberalization of capital movements and the internalization of production. In this context, companies have been obliged to adapt and define their strategies in global terms, and M&A have become a mechanism used to improve a company's market position, to complement technological know-how, and to assemble the resources necessary to implement projects requiring high levels of investment. For these reasons, M&A have been concentrated above all in the most dynamic and strategic sectors, such as telecommunications, energy, financial services and the chemicals industry.

The supply of assets in Latin America and the Caribbean has increased significantly due to the economic reform programmes implemented in the region. Many business owners have been obliged to sell their companies because they lack the technology and/or capital necessary to compete in more open

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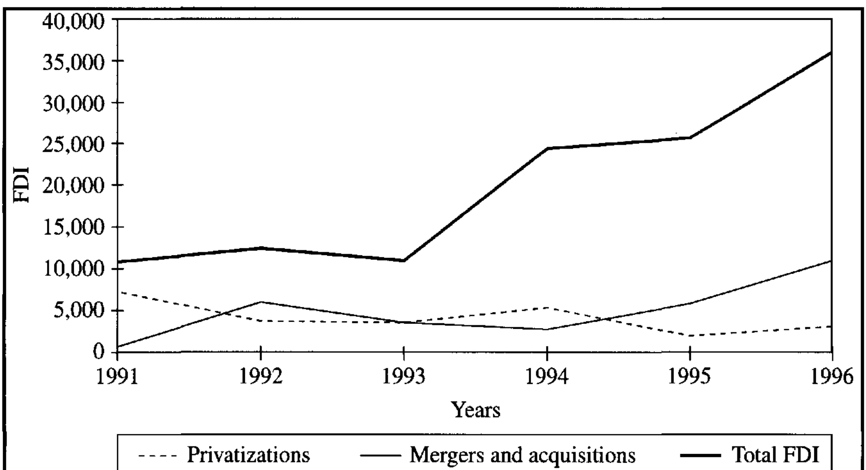
markets. In fact, many of the companies acquired by foreign investors previously belonged to conglomerates with interests in a wide variety of sectors. This suggests that local, privately-owned corporations have adopted a strategy of specialization in order to channel their resources into those activities where they believe they have a better chance of facing up to the tough competition from leading world companies.

Over the last few years, large numbers of foreign companies have seized these opportunities to enter or expand in the region.[16] Interest initially focused on Mexico, where companies can take advantage of NAFTA. Subsequently, however, with the return to macroeconomic stability in Brazil and Argentina and the expansion of the local market through the creation of MERCOSUR, both countries have also been the object of major M&A operations by foreign companies.

Graph 3
FDI Flows Through Privatizations and M&A
(millions of US$)



Source: Compiled by the authors from data provided by the Investment and Business Strategies Unit of the Division for Productive Development, ECLAC, and information in UNCTAD (1997): 353-357, and World Bank (1997):121.

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The prospect of rapidly expanding markets, particularly for manufactured goods, has attracted many foreign companies, and the acquisition of an existing company is a simple, rapid way of entering the market. Through acquisitions, companies eliminate part of the competition and inherit a market position, distribution channels, know how, and knowledge of local markets.

Some of the TNCs operating in Latin America are currently selecting assets for acquisition in their core business as a means of expanding in the regional markets. As in the case of local corporations, the TNCs are selling off their interests in less important activities in order to finance these operations. Geographic diversification has not only enabled them to increase their turnover, but also to reduce the risks associated with concentrating on a single market. Equally, thanks to their greater access to foreign financing (through international stock and bond issues), some larger Latin American companies have begun to play a key role in this process. It can be seen, therefore, that this is a time of very rapid change both in the business structure of Latin America and in the role of foreign investors in the region.

Box 1: The Potential Effects of FDI on the Recipient Economy

The effects of direct investment on recipient developing economies have been widely debated in the specialist literature. As a result, it is possible to consider the consequences of FDI in terms of both costs and benefits. Below we shall briefly outline some of the most widely recognized effects on recipient economies, as set out in the report "*A Background Note on Foreign Direct Investment in Latin America and the Caribbean*" (Garay et al., 1996) prepared by the IDB for the working group on investment in the Free Trade Area of the Americas (FTAA).

The principal acknowledged benefit of FDI for the recipient country consists of the contribution it makes to economic development through the increase in capital stock and improvements in the efficiency of investment. The latter is essential to increase competitiveness and productivity in the national economy in the context of globalization. Increased efficiency may be the result of a whole series of different factors: reductions in administrative costs; increased productivity of capital and labour; exploitation of economies of scale, and/or externalities through access to new markets; improvements in the quality of existing products or the introduction of new products; the exploitation of comparative advantages (both static and dynamic); and the adjustment of national productive structures to new market conditions.

In addition, benefits from FDI are linked to the fact that it tends to foster the development of human resources through training, and spill-over effects that improve

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the efficiency of the labour market, lead to better wages, etc. FDI often leads to improved training for workers and managers in the recipient countries. However, given that the training provided for workers is often confined to the specific requirements of a particular production line, its effect on the wider labour market may be limited.

By fuelling exports, FDI may also play an important role in the restructuring of the economies of recipient countries, helping to make them more competitive and export-oriented, and giving them greater access to international markets through the investor companies' production and distribution networks. Equally, FDI has often served to boost exports of manufactured goods. On the other hand, there is also evidence to suggest that FDI activities are more reliant on imports than local companies.

FDI may also be the most important channel for gaining access to new technologies. It may promote technological transfers, thereby helping to raise productivity, as well as changing the composition of products and exports, research and development, and encouraging organizational innovations in local companies. It may also lead to an improvement in management and training methods. Nevertheless, it is worth bearing in mind that the technological transfers associated with FDI are often determined in accordance with the strategies of the TNCs.

The creation of linkages between TNCs and local companies may also have an impact on the industrial structure of recipient countries. There may be direct linkages with local suppliers of raw materials, components and services. Interactions with respect to information, technology, specific skills and finance may also occur. Indirect ties also generate collateral effects in terms of skills and externalities related to training and innovation, increased pressure on local firms in terms of competitiveness, etc. The diffusion of these different types of links encourages intra-industry transactions, favouring vertical and horizontal integration within the recipient economy. Empirical evidence suggests that the extent to which these links are formed in local economies essentially depends on the trade regimes and industrial policies of the different national governments, as well as the global strategies of the TNCs and the specific role they assign their subsidiaries.

The social benefits of FDI tend to be lower in recipient countries with highly import substituting regimes industrialization than in more export-oriented economies, or those which are relatively open to international competition. In the case of very protected economic environments, many of the benefits of FDI may be internalized by the foreign companies operating under oligopolistic or monopolistic conditions. TNCs exposed to competition are more sensitive to production costs, and therefore have stronger incentives to maximize efficiency. As a result, there can be little doubt that the recent liberalizing reforms carried out in many Latin American and Caribbean countries will have a major impact not just on FDI flows, but also on the recipient countries themselves.

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On the other hand, FDI flows may also have costs for recipient countries. These are connected to the incentives established by national governments in order to attract foreign investment, the distortions and the loss of public revenue due to transfer pricing between subsidiaries, the restrictions imposed by parent companies on their subsidiaries in terms of the provision of inputs (in favour of foreign suppliers), the (un)suitability of the technology used, and the extent of labour training and technological transfers. Moreover, FDI may promote a division of labour based on the investor company's global interests, which may be inconsistent with the recipient country's understanding of its comparative advantages.

Finally, it should be emphasized that a definitive evaluation of the impact of FDI on recipient economies must inevitably be based on case-by-case empirical analysis, which should study in detail the costs and benefits in a wide variety of areas.

New Geographic and Sectoral Destinations for FDI

In 1996, the last year for which complete figures are available, FDI flows to Latin America were concentrated in Brazil (29%) and Mexico (20%), followed by Argentina, Chile, Peru and Colombia. However, the concentration of FDI in just a few countries at the beginning of the 1990s has weakened over the course of the decade: during the last two years, at least seven countries have attracted annual flows of over $1 billion, compared with only two in 1990.

Recently, foreign investors in Latin America and the Caribbean have shown greater interest in the service sector, especially telecommunications (Argentina, Chile and Peru), the generation and distribution of electricity (Argentina, Brazil, Colombia and Peru) and banking (Argentina, Chile, Colombia and Venezuela). There has also been major investment in the primary sector, essentially in mining (Bolivia, Peru and Venezuela and, more recently, Argentina) and oil (Argentina, Colombia, Peru and Venezuela), in manufacturing (Argentina, Brazil and Mexico, especially in the automobile industry), and in export activities (through the *maquiladora* assembly plants in Mexico and some other countries in Central America and the Caribbean).

The rapid increase in FDI in countries in the region over recent years has produced a major expansion of the accumulated FDI stock in their economies.

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According to the estimates produced by the United Nations Economic Commission for Latin America and the Caribbean (ECLAC), the stock of the principal recipients of FDI totalled some $262 billion by the end of 1996 (see Table 2). Hence about one-third of all FDI stock in the region was accumulated during the period 1990- 1996.

An analysis of the geographic distribution of stock highlights the cases of Argentina, Chile, Colombia, Mexico, Peru and Uruguay. These are countries which had an important stock of FDI at the end of the 1980s and have attracted sustained and growing flows of FDI over the course of the 1990s. The case of Peru is particularly interesting since, at the beginning of the decade it had negative stock[17], but this situation was reversed during the years that followed due to major inflows of FDI. Brazil also stands out in this context, as its stock of FDI grew by little more than 0.5% between 1990 and 1996, suggesting that the annual inflows of FDI into the economy for much of this period were insufficient to compensate for the depreciation of existing stock.

Table 1
FDI Flows to the Main Recipient Countries in Latin America
(in millions of US$)

	1990	1991	1992	1993	1994	1995	1996	1997(e)
Argentina	1,83	2,439	4,045	2,555	3,068	4,181	4,285	6,000
Brazil	989	1,103	2,061	1,292	3,072	4,859	11,112	18,000
Chile	590	523	699	808	1,773	1,668	4,091	2,600
Colombia	500	457	729	959	1,667	2,317	3,322	3,000
Mexico	2,634	4,762	4,393	4,389	10,973	9,526	7,619	8,000
Peru	41	–7	136	670	3,084	2,035	3,581	2,000
Venezuela	451	1,916	629	372	813	985	1,833	4,000
Subtotal	7,041	11,193	12,692	11,096	24,450	25,571	35,843	43,600
Regional total	7,698	11,965	13,731	12,494	26,260	27,564	38,110	45,500

Source: Investment and Business Strategies Unit of the Division for Productive Development of ECLAC, based on data obtained from the International Monetary Fund (IMF), and national sources.
(e) Preliminary estimates.

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Table 2
FDI Stock in the Main Recipient Countries of Latin America
(in millions of US$)

	1990	1991	1992	1993	1994	1995	1996	FDI/GDP[1]
Argentina	11,058	12,965	14,829	16,476	20,401	24,629	28,930	9.7
Brazil	104,557	100,650	98,252	96,031	95,488	98,839	107,544	14.3
Chile	12,332	12,262	12,418	12,783	14,074	15,547	19,259	26.8
Colombia	3,500	3,602	3,952	4,389	5,779	8,004	11,131	14.9
Mexico	37,132	40,108	42,725	45,586	55,373	62,926	69,960	20.9
Peru	-416	-403	-249	430	3,497	5,477	8,924	14.6
Venezuela	3,903	5,632	6,011	6,168	6,749	7,627	9,275	13.8
Subtotal	172,066	174,816	177,938	181,863	201,361	223,049	255,023	
Regional total	175,597	178,527	183,585	188,500	207,263	229,670	262,234	

Source: Investment and Business Strategies Unit of the Division for Productive Development, ECLAC.
1 Estimate, 1996 (in percentage).

While the largest countries in the region are also the largest recipients of FDI, by observing FDI flows in relation to the size of the economy (FDI stock as a proportion of GDP) a different picture emerges. From this perspective Chile ranks first with a stock of FDI equivalent to almost 27% of its GDP, followed by Mexico with 21%, while for Peru, Brazil, Colombia and Venezuela the percentage is around 14% (see Table 2).

On the other hand, although the smaller countries in the region receive modest revenues from foreign investment in comparison with other countries, FDI may still have significant effects on their economies. In fact, during the first half of the decade, the importance of FDI increased in a number of these countries, confirming the relatively greater dispersion of foreign investment in the region. Thus, according to UNCTAD figures:

- Between 1991 and 1995, FDI flows have made a major contribution to the formation of fixed capital in a number of smaller countries, notably Trinidad and Tobago (44.6%), Guyana (37.2%), Bolivia (19.6%), Costa Rica (17.6%) and Jamaica (11.1%) (unweighted averages).

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- In 1995, the stock of FDI as a percentage of GDP was particularly significant in Trinidad and Tobago (75.1%), Jamaica (31.3%), Costa Rica (30.2%), the Bahamas (29%), Belize (25.3%) and Bolivia (22.3%).

- The country with the highest per capita FDI in the region was Trinidad and Tobago, followed by Chile and Costa Rica (see Table 3).

Table 3
FDI Stock Per Capita
(in US$, ranked according to 1996 figures)

	1980	1990	1996e
Trinidad and Tobago	879	1,693	2,995
Chile	77	768	1.298
Costa Rica	278	477	915
Argentina	184	270	821
Mexico	115	391	772
Brazil	137	251	672
Jamaica	228	292	609
Uruguay	248	317	506
Peru	49	58	377
Venezuela	101	198	371
Latin America and the Caribbean	114	256	600

Sources: UNCTAD (1997) and IDB (1998)
Note: Excluding offshore centres and "other countries" (see Annex I)
e: Estimate

MERCOSUR and NAFTA as magnets for foreign investors

Liberalization, deregulation, and economic stability have all contributed to the renewed interest among foreign investors in the MERCOSUR countries. The redefined strategies of TNCs operating in the sub-region increasingly reveal their greater awareness of the opportunities offered by the enlarged market. This trend is particularly evident in the manufacturing sector (automobile industry) and in

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some services, such as banking, telecommunications and electricity generating and distribution. These developments will undoubtedly have a significant impact on the future competitiveness of MERCOSUR.

Brazil's economic recovery has made it the favourite destination for foreign investment in Latin America and the Caribbean. Some analysts consider that the substantial inflows of capital since 1996 (over $10 billion a year) mark just the beginning of a major expansion in foreign investment in the country. A government survey has estimated that before the year 2000, the private sector (both domestic and foreign) will invest some $220 billion in the Brazilian economy. At the same time, with the intensification of the privatization process, investments of over $60 billion are expected over the next three years in the telecommunications and electricity sectors alone. In 1997, following completion of the privatization of industrial enterprises (with the sale in May that year of Vale do Rio Doce for just over $3.1 billion) and the state-owned rail company, further privatizations occurred in electricity generating and distribution companies,[18] cellular telephone services[19] and the banking system. Foreign capital has begun to play a more active role in this final phase of the privatization process, often intervening in association with local investors.[20]

According to the Brazilian Central Bank, in 1996 some $2.3 billion of foreign capital flowed into the country through privatizations, modifying the sectoral distribution of FDI. Public utilities (electricity, telecommunications, and rail companies) absorbed 32% of this investment, while the service sector as a whole accounted for 62% of all inflows of FDI. The significance of this development can be seen from the fact that, in terms of FDI stock, the service sector accounts for less than 30% of the total. However, the data available on new investment projects suggests that manufacturing industry is likely to regain its traditional importance as a destination for FDI, particularly as a result of a number of substantial investments made or planned in the automobile industry.

In 1996, the manufacturing industry absorbed some 24% of FDI inflows. As a result of liberalization and the improved competitiveness of the Brazilian economy, over 50% of these investments went to the automobile, metal-mechanical and electrical industries. Ongoing or planned investment operations in manufacturing until 1999 are concentrated in the metallurgical industry (25%), chemicals and petrochemicals (15%), the automobile industry (10%), pharmaceuticals (7%) and foodstuffs (5%). In the primary sector, there are plans to make substantial investments (worth over $3.4 billion) over the next few years, particularly in mining.

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Argentina was not seriously affected by the Mexican crisis and is now looking forward to another period of rapid growth in capital inflows. An influx of over $23 billion is expected in the period 1995-2000, concentrated above all in manufacturing of automobile engines and parts, food and beverages, petrochemicals, construction and telecommunications. It is also anticipated that there will be a major upsurge in investment in mining, oil and energy supplies (natural gas). Investments of over $3.7 billion are forecast in mining operations in the period 1997-2000. Argentina will also carry out a further wave of privatizations, notably of the publically-owned provincial electricity and water companies; these sales are expected to generate between $5 billion and $6 billion. It should be noted that 67% of FDI flows into the country come from newcomers, that is, companies investing in the Argentine economy for the first time since 1990.

Given these developments in the two largest economies of MERCOSUR, and the progress being made in the integration process, it seems clear that a new trend is emerging in FDI flows. TNCs appear to be adapting their strategies (previously concentrated in manufacturing industry) to the new reality of the sub-region, in that they now view MERCOSUR as a unit, and are incorporating it as such into their integrated global production and management systems.

During the first half of the 1990s, Mexico was the largest single recipient of FDI in Latin America, attracting over half of all flows to the region, while it currently accounts for some 20% of the total. Mexico's membership of NAFTA helps explain its prominent position, as foreign investors took advantage of the guaranteed access to this market and preferential tariff treatment for trade with Canada and the United States.

Over the last few years, and despite the progressive liberalization of the service sector, privatizations and the high value of the peso, most FDI in Mexico has still come from leading manufacturing companies, especially US TNCs. The major devaluation of the peso at the end of 1994 made the tradable sector much more competitive, encouraging investment in export-oriented production. As a result, over the last two years, and despite the economic problems caused by the peso crisis, there has been a steady increase in investment in manufacturing, particularly in the automobile industry and *maquiladora* assembly plants.

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The automobile industry: the driving force for FDI in the manufacturing sector

Investments in manufacturing have been concentrated above all in the automobile industry. Between 1990 and 1995, foreign vehicle manufacturers invested some $12 billion in the region, while a further $23 billion of investments are expected between 1995 and 2000, over half of which will go to Brazil. In the manufacturing sector, and particularly in the automobile industry in MERCOSUR, intra-regional trade has grown rapidly, indicating an intense level of intra-company trade dominated by the TNCs in the sector.

Within MERCOSUR, six European Union (EU) manufacturers (Fiat, Mercedes-Benz, Peugeot, Renault, Scania and Volkswagen), three American companies (Chrysler, Ford and General Motors, GM) and five Asian producers (Asia Motors, Honda, Hyundai, Mitsubishi and Toyota) have announced ambitious plans for investments before 2000 of around $13.3 billion in Brazil, and almost $4 billion in Argentina (that is, almost $18 billion in total). Some of these investments have been encouraged by the introduction of a series of special incentives, particularly in the poorer regions of Brazil, where projects worth a total of almost $2.8 billion have been approved under this special regime.[21] At the beginning of 1998, most of these projects were already under way and the TNCs involved are currently defining their strategies.

Companies already established in Latin America are currently consolidating their position in the region, modernizing, expanding, and diversifying their production capacity, and adapting it to international standards in order to export. This is the case of Ford, GM, Chrysler, Volkswagen and Nissan in Mexico.[22] A number of automobile companies with a major presence in the Latin American markets have made investments intended to defend their market shares and respond to increased demand, particularly for the lower end of the market. This is the case of Fiat, Volkswagen, Ford and GM in Brazil. At the same time, there has been an increase in the number of companies entering the regional market for the first time, or returning to it in search of "a niche in the market". This is the case of Chrysler, Renault, Peugeot, BMW and Mercedes-Benz (which has constructed only its second factory outside Germany), as well as several Asian companies (Asia Motors, Honda and Hyundai). Brazil has attracted most of these investments.

The figures available suggest that, at the beginning of 1998, and despite the difficulties arising from the Asian crisis, the large TNCs in the automobile industry are still backing Latin America, and Brazil and MERCOSUR in particular. GM has announced that its plans to invest in MERCOSUR will not be affected by

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the crisis. Between 1998 and 2000, GM intends to invest some $4.6 billion in the region ($1 billion in Argentina and the rest in Brazil). GM already has two plants in Brazil and two in Argentina; in the latter, it has invested $520 million since returning in 1994, after a 16-year absence. The Peugeot-Citroën consortium has announced that it will begin construction of a $600 million plant in Porto Real, where it expects to export some 20,000 vehicles annually over the next five years to Argentina, Uruguay and Paraguay. Volkswagen do Brasil announced an agreement with its Mexican counterpart whereby it would increase its exports of vehicles to Mexico from 7,000 in 1997 to 28,000 in 1998.

Another, increasingly important destination for investment in the manufacturing sector is the *maquiladora* or assembly industry, particularly in Mexico and some Central American and Caribbean countries. Large inflows of foreign capital have gone, for example, into the production of monitors and televisions in Mexico, computer components (Intel) in Costa Rica and, above all, the clothing industry in most of these countries, which benefit from their proximity to the US market, tax incentives, and low wage levels. The development of the *maquiladora* industry has been encouraged by US government policies which have benefited US companies above all.

Tariff rule HTS 9802 has enabled companies based in the United States to export components produced there for assembly in other countries and, when the finished products return to the United States, only the value added abroad is subject to import duty. This measure has proved very favourable to Mexico and Central American and Caribbean countries, boosting their exports and leading to a major increase in their market shares. The benefits of this regulation have affected the clothing industry above all.

Under NAFTA rules of origin, companies with operations in Mexico have benefitted from tariff reductions and exemption from import quotas for the US market. They have also been able to include their Mexican inputs as part of the North American content required under NAFTA.

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Box 2: Observations on the Theory of International Trade

The analysis of the various forces which determine the nature and scale of international business cannot be considered in a single field of academic study. In fact, the analysis of the multitude of factors that may influence a company's decision and ability to invest abroad correspond to different academic disciplines, such as the Theory of the Firm, International Economics, International Politics, Political Science and Finance, to name a few.

Given the eminently applied nature of this book, the analysis is not based on any particular theoretical model, since its contribution to knowledge of the subject is essentially based on discussion of the empirical evidence. Nonetheless, it would be impossible (and inappropriate) to overlook completely the theoretical perspective. Hence, although theoretical issues are not examined in depth, the chapters on individual countries do include some references to the theoretical elements behind the analysis. For readers interested in pursuing the theory of international business in greater depth, this box provides a table based on Grosse and Behrman (1992) which classifies the different analytical approaches in this field. The following table offers, therefore, a very selective guide to the existing theoretical approaches and debates, as well as recommending some works on the subject. In some cases, the references quoted offer rival explanations for similar phenomena; in most, however, they attempt to explain different dimensions of international business, and may therefore be considered complementary.

Theoretical approach	Functional area	Dimensions explained	Some references
International production cycle	International economics and marketing	FDI flows; impact of technology; influence of market conditions	Vernon (1966) Wells (1972) Vernon (1979)
Monopolistic competition	Theory of the firm (economics)	Strategies and competitiveness of TNCs	Hymer (1960) Caves (1971) Kindenberg (1969) Grosse (1985)
Internalization	Theory of the firm (economics)	Size and expansion of the company	Buckley & Casson (1976) Rugman (1981)
Transaction costs	Theory of the firm (economics)	Structure and function of organizational hierarchies	Teece (1986) Hennart (1982) Casson (1983)
Competitive advantages	Business strategy	Competitiveness of companies and industry	Caves (1981) Ghoshal (1987) Porter (1990)
Eclectic theory	Theory of the firm (economics)	Internalization and competitive advantages	Dunning (1977) Dunning (1988)

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Arbitration of national market	Finance	Segmentation of national markets; direction of FDI flows, international finance	Aliber (1970)
Bargaining theory	Political science, business strategy, political economy	Negotiations between governments and companies, the distribution of profits between governments and companies	Vernon (1971) Moran (1985) Gladwin & Walter (1980) Fayerweather (1969)

Source: Based on Grosse and Behrman (1992).

These local incentives have encouraged not only US companies to establish this type of export-processing operations, but also companies from elsewhere, especially Asia. Major examples of this trend are the Korean companies operating in Guatemala and Honduras, and their Taiwanese counterparts with plants in Nicaragua. In the case of Mexico, the devaluation at the end of 1994 and the subsequent exchange rate stability have encouraged a major wave of investment in the *maquiladora* industry. In 1996 alone, there was a 25% increase in the number of companies operating this system.

"Emerging" sectors for foreign capital

Favourable economic prospects in Latin America, combined with the opening up of many sectors which were previously closed to foreign capital, have changed the sectoral distribution of FDI in the region.

A growing proportion of FDI flows are destined for the traditional extraction industries, reflecting the introduction of new mining regulations in countries such as Argentina, Bolivia and Peru. South America is currently the main region in the world for investment in mining: in 1997 it attracted some \$14.3 billion, more than twice the amount invested in 1995. As a result of deregulation, Argentina expects further investments amounting to some \$3.7 billion by 2000. While in 1996 total mining output was worth some \$500 million, official information on ongoing projects in the sector predicts an increase to \$1.7 billion by 2000. At the same time, it is estimated that exports will climb from their present level of \$73 million to \$1.2 billion over the next four years.

Other major areas of investment in the primary sector include hydrocarbons and, above all, oil. Until recently under state control, these sectors have gradually been opened up to private investment, through the award of

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concessions to exploit less important reserves, joint ventures in certain major activities and, in some cases, the total privatization of the sector. Colombia and Venezuela stand out as recent examples of this trend.

The discovery of new reserves, the decision by the Empresa Colombiana de Petróleo (ECOPETROL) to sell some of its assets, the introduction of a new regime for foreign investment, and new regulations specifically governing activity in the sector, have combined to make hydrocarbons the single most important destination for FDI in Colombia over the last few years (accounting for 40% of the total). At the same time, in Venezuela, the state-owned company Petróleos de Venezuela S.A. (PDVSA) is now engaged in joint projects with foreign investors amounting to a total of $5.4 billion.[23]

The liberalization of the financial sector has attracted substantial investment in most countries in the region, particularly Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela. Among the most important operations carried out over the last few years are the acquisitions made by Spanish banks such as Banco Santander, Banco Bilbao Vizcaya (BBV) and Banco Central Hispanoamericano (BCH), involving a total investment of over $6.5 billion. Privatization of the state-owned banks in Brazil will create new opportunities for foreign investment in the sector.

At the same time, privatization programmes still being implemented in the region will continue to absorb a substantial share of FDI flows, destined both to the acquisition of existing assets and related investments. This trend will be reinforced by the forthcoming privatizations in sectors which were previously reserved for local investors (transport, telecommunications, energy, gas and oil) and are now open to foreign capital, as well as by the new wave of sales in Brazil.

Main Sources of FDI in Latin America

An analysis of the influx of investment to Latin America and the Caribbean from the perspective of the principal sources of FDI (that is, according to the data from investor countries) reveals that these flows have expanded substantially since the beginning of the 1990s. This increase involves both traditional investor countries and those which have only recently begun a process of large-scale investment in the region. During the period 1990-1996, the flow of investment (expressed as annual averages) has increased almost fivefold in comparison with the 1980s (see Table 4).

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Table 4
FDI Flows to Latin America and the Caribbean, 1980-1996
(accumulated values in millions of US$ and as a percentage of the total)

	1980-1989	Annual average	%	1990-1996	Annual average	%
Europe	12,207	1,221	46.7	25,889	3,698	30.0
— France	1,690	169	6.5	2,947	421	3.4
— Germany	2,810	281	10.7	3,780	540	4.4
— Spain	1,280	128	4.9	5,355	765	6.2
— United Kingdom	4,580	458	17.5	6,307	901	7.3
USA	11,018	1,102	42.1	57,064	8,152	66.2
Japan	2,918	292	11.2	3,201	457	3.7
Total of the three	26,143	2,614	100.0	86,154	12,308	100.0

Source: IDB-IRELA, based on Table 32 in the Statistical Annex.

A major component of FDI in Latin America and the Caribbean consists of investments made in offshore centres (see Table 5). Nonetheless, in many cases, the final destination of these investments is other countries in the region. Given that it is virtually impossible to identify the eventual geographic or sectoral destination of these investments, the present analysis does not focus on FDI investments in offshore centres. It should be noted, however, that these investments have also increased (in fact, they have almost doubled) during the 1990s, thereby contributing to the overall increase in the flow of FDI to the region. At the same time, however, the evidence suggests that their importance has decreased in comparison with the flow of capital to other Latin American and Caribbean economies. The trend observed in the 1980s, when FDI in offshore centres exceeded that in the rest of the region as a whole, was reversed in the period 1990-1996, when investment in other countries in the region was almost double that in the offshore centres.

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Table 5
FDI Flows to Offshore Centres in Latin American and the Caribbean, 1980-1996
(figures in millions of US$)

	1980-1989	Annual average	%	1990-1996	Annual average	%
Europe	11,569	1,157	32.1	10,614	1,516	23.9
— France	460	46	1.3	—	—	—
— Germany	680	68	1.9	2,268	324	5.1
— Spain	510	51	1.4	1,337	191	3.0
— United Kingdom	7,100	710	2.0	5,306	758	12.0
USA	13,286	1,329	36.9	32,533	4,648	73.4
Japan	11,194	1,119	31.1	1,184	169	2.7
Total of the three	36,049	3,605	100.0	44,331	6,333	100.0

Source: IDB-IRELA, based on Table 33 in the Statistical Annex.

The United States is still the largest investor in the region, which (including offshore centres) absorbs 17% of all US foreign investment and over 62% of its investment in countries outside the Organization for Economic Cooperation and Development (OECD). Between 1990 and 1996, US companies invested over $57 billion (some two-thirds of all FDI in the Latin America and Caribbean), while in 1995, total US FDI stock in the region amounted to $67 billion. The principal recipient countries are Brazil and Mexico, which have absorbed 63% of all US FDI in Latin America during the 1990s, and hold 59% of US FDI stock in the region. In fact, in 1996, these two economies became the most important destinations for US investment of all the developing countries. However, although many of the same investor companies are involved, they tend to follow very different strategies in the two countries. In Brazil, TNCs attempt to exploit the advantages of a vast domestic market and the opportunities offered by MERCOSUR, while in Mexico, most investment is destined for production plants which supply the US market.

During the 1990s, Canada has also emerged as a major investor in Latin America, particularly in the mining industry. In 1996, Canadian FDI stock in the region amounted to some $23.3 billion, equivalent to 13% of its total FDI, and 62% of its FDI in non-OECD countries. Argentina, Brazil,

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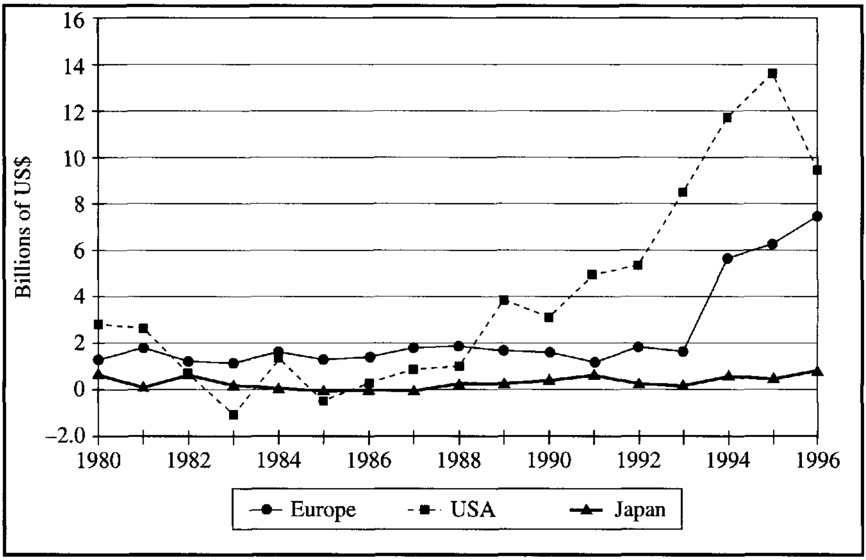
Chile, Mexico and Venezuela account for the bulk of Canadian investment in the region. At present, Canada is the second largest investor in Chile, with current or planned investments of over $7 billion. Canada has also played an important role in the recent development of mining activities in Argentina and Peru. Some 29 Canadian mining companies are now well established in Peru, where they have plans to invest more than $2 billion (see Box 4).

Graph 4
FDI Flows to Latin America and the Caribbean, 1980-96
(in billions of US$)



Source: IDB-IRELA based on tables in the Statistical Annex.

Over the last few years there has been an unprecedented increase in the flow of FDI from the EU. In contrast to the situation in the 1980s and early 1990s (with annual average flows to the region of $1.2 billion and $1.6 billion, respectively), EU companies invested an annual average of $6.2 billion in the

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region during the period 1994-1996 (see Graph 4). Indeed, in 1996 the flow of direct investment from Europe (excluding offshore centres) almost matched that of the United States.

Since 1994, the two largest EU investors in terms of flows have been the United Kingdom and Spain. In terms of stocks, the main investors in the region have been Germany, the United Kingdom and France.[24] Latin America and the Caribbean represent the main destination of investments outside the OECD for a number of European countries, notably Germany (60%), the Netherlands (55%) and the United Kingdom (44%). The flow of FDI from the EU Member States is directed above all to MERCOSUR countries, particularly Brazil (35%) and Argentina (20%), and Mexico (13%).

FDI from the EU is concentrated above all in manufacturing industry. This is the destination for 81% of investment from the Netherlands, 68% from Italy, and 67% from Germany (figures for stocks in 1995 and 1996). Especially in recent years, however, the implementation of privatization programmes in many Latin American countries has fuelled a major increase in investment in the service sector (largely by Spanish and French companies).

On the other hand, the agreements signed by the EU with MERCOSUR (15 December 1995), Chile (21 June 1996) and Mexico (8 December 1997) are expected to lead to a major increase in the flow of European FDI to the region, given that they envisage the liberalization of bilateral trade and financial relations.

Switzerland is another important source of foreign investment in the region (see Box 3). In 1995, the total stock of Swiss FDI in the region amounted to some $8 billion, over half of which was held in the MERCOSUR countries, 17% in Mexico and 16% in Chile. Since 1993, when Switzerland first published data on direct investment operations, the flow of Swiss FDI to the region has averaged $340 million a year.

Japanese investment, on the other hand, still accounts for a relatively small proportion of all FDI flows to Latin America and the Caribbean. Japanese investors in the region have tended to focus on Panama, Brazil and Mexico, mainly in the financial and insurance sectors and, to a lesser extent, in commercial services and manufacturing.[25] This is a rather different pattern from that followed by Japanese companies in the rest of the world, where they invest mainly in manufacturing industry.[26] Nevertheless, the progress made by the Latin American economies suggests that Japanese private investors may be starting to take a greater interest in the region.[27] According to some analysts,

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Brazil alone will receive Japanese FDI of around $2 billion over the next two years.

Investments by other Asian countries, essentially in response to the signing of NAFTA and the creation of MERCOSUR, have also increased considerably. A new generation of small- and medium-size companies are seeking access to the US and Canadian markets through Mexico. Recently, companies from South Korea, Taiwan and Singapore have been investing in Mexico, mainly in *maquiladora* assembly plants producing televisions, electrical appliances and automobile parts.[28] Proximity to the United States and low labour costs constitute the main attractions of Mexico, the Central American countries and the Caribbean. Brazil has also begun to receive major investments from South Korean companies.[29] In terms of the prospects for the future, it is still too early to tell how the crisis in Asia will affect these planned investments.

Over the course of the 1990s, more than half the flows of FDI from Europe and Japan to the region have gone to MERCOSUR, while US FDI has flowed to a wider range of countries. In comparison with the 1980s, and coinciding with the development of integration processes, foreign investors are currently showing more interest in the Andean Community, which suffered net disinvestment in the period 1980-1989, as a result of withdrawals by US and Japanese companies.

Box 3: Swiss FDI in Latin America and the Caribbean

Data on geographically distributed Swiss FDI have only been available since 1993. The figures are published by the National Bank of Switzerland and give a breakdown of the principal recipient countries. The lack of equivalent information for previous years means that it is difficult to produce an analysis of Swiss FDI in Latin America and the Caribbean comparable to that of the other countries covered in this study. However, this box offers some basic information on Swiss investment in the region.

Latin America and the Caribbean are important destinations for Swiss FDI. According to estimates produced by the National Bank of Switzerland, at the end of 1996 the total stock of Swiss FDI in the region (including offshore centres) amounted to $19.6 billion. This sum represents some 14% of Swiss FDI worldwide, and 70% of Swiss FDI in non-OECD countries. Most of this investment (some $11 billion) is held in offshore centres. However, even when these are excluded, Latin America was still the most important destination in terms of stock, accounting for 45% of Swiss investment in developing and transitional countries (followed by Asia, with 39%).

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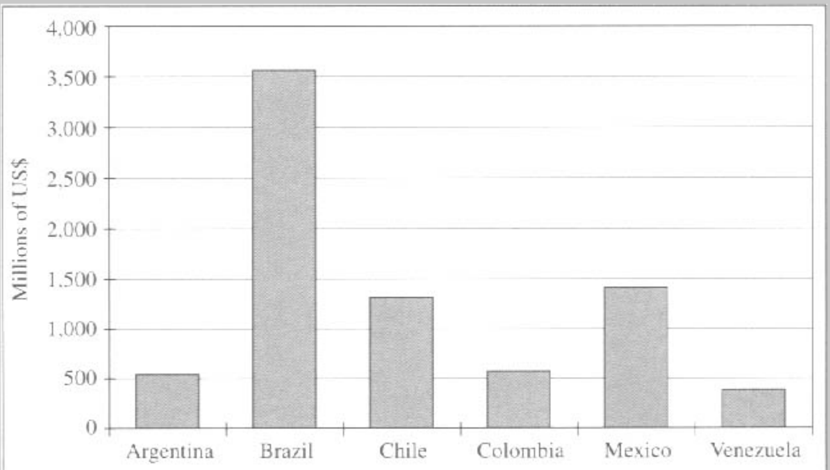
At the end of 1996, Brazil, with $3.6 billion dollars, was the ninth most important FDI destination for Swiss companies. This should be compared with the stock of Swiss investment in the most important Asian destinations, namely Japan and Hong Kong, which had total stocks of $3.3 and $1.5 billion, respectively. Swiss investment in Brazil outstripped that of Spain, Sweden and Belgium. In fact, Swiss FDI stock in Brazil accounted for 45% of its total investment in Latin America at the end of 1996, excluding offshore centres in the region. The next most important destinations for Swiss FDI were Mexico ($1.4 billion) and Chile ($1.3 billion). Taken as a whole, these three countries accounted for more than 88% of all Swiss investment in the region (excluding the offshore centres).

Stocks of Swiss FDI in selected countries, end of 1996



The information on flows of Swiss FDI shows a rather different picture. The most important destination for Swiss FDI flows in the period 1993-1996 was Asia (including the Middle East), which attracted $3.4 billion, or 54% of all flows to developing or transitional countries, followed by Eastern Europe and Latin America and the Caribbean (attracting some $1.4 billion each), and Africa with just $147 million. The main recipient countries were Singapore, India and China. In Latin America the main destinations during this period were Uruguay, with $285 million, and Mexico with $238 million

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By sectors, manufacturing industry accounted for 77% of Swiss investment in the main recipient countries (Argentina, Brazil, Chile and Mexico). In the region as a whole, including offshore centres, the service sector absorbed the bulk of Swiss investment (79%). This highlights the very different type of investment in offshore centres and the rest of the region.

At the end of 1996, the Swiss-owned affiliates in Latin America and the Caribbean employed over 147,000 people (out of a worldwide total of over 1.4 million). Most of these jobs (113,000 employees) were in the four largest recipient countries mentioned above, of which three-quarters were in manufacturing industry. With over 69,000 employees, Brazil had by far the largest number of jobs in Swiss-owned companies in Latin America, and ranked fifth in the world in this respect. Swiss affiliates employed over 20,000 people in Mexico, and some 13,000 in Chile.

A large number of Swiss companies operate in Latin America and the Caribbean. In many cases these have been present in the region for many years. In 1995, it was estimated that over 250 Swiss companies operated in Brazil alone, both in manufacturing industry (essentially in foodstuffs, chemicals and machinery) and the service sector (particularly in banking, insurance and commerce). Around 90% of Swiss companies in Brazil are located in the São Paulo area. The size of the Brazilian market is seen as the main attraction for Swiss investors. Hence the activities of these companies are essentially oriented towards supplying local markets, while the re-importation of industrial products represents only a small part of their business.

Nestle, for example, has a total of 86 factories in Latin America, with sales of around $6.5 billion. In Brazil (the company's fourth most important market worldwide, and the most important in the developing world), Nestle has 28 plants, employing 15,000 people; in 1996, sales totalled some $3.2 billion. Other Swiss multinationals, including Novartis, Roche, Sulzer, Schindler and the Swiss Banking Corporation, are also active in the region. Novartis, for example, has plans to invest $150 million to expand its factories in Brazil. Nestle has recently made a series of acquisitions, including some Bolivian companies, while the Swiss Bank Corporation has recently acquired the Grupo Banco Omega.

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Table 6
FDI Flows from Europe, the United States and Japan by Sub-region, 1990-1996
(net flows in millions of US$)

	1990-1996					
	Europe	%	USA	%	Japan	%
Argentina	4,954	19.1	5,853	10.3	188	5.9
Brazil	8,859	34.2	18,720	32.8	1,553	48.5
Paraguay	43	0.2	45	0.1	1	0.0
Uruguay	544	2.1	235	0.4	-1	0.0
MERCOSUR	14,400	55.6	24,853	43.6	1,741	54.4
Chile	1,991	7.7	4,777	8.4	83	2.6
Bolivia	68	0.3	99	0.2	—	—
Colombia	1,160	4.5	1,265	2.2	75	2.3
Ecuador	221	0.9	543	1.0	4	0.1
Peru	2,127	8.2	965	1.7	-24	-0.8
Venezuela	1,611	6.2	4,122	7.2	360	11.3
Andean Group	5,187	20.0	6,994	12.3	415	13.0
Mexico	3,547	13.7	17,344	30.4	950	29.7
Costa Rica	105	0.4	752	1.3	1	0.0
El Salvador	27	0.1	84	0.1	—	—
Guatemala	-121	-0.5	146	0.3	—	—
Honduras	9	0.0	-45	-0.1	7	0.2
Nicaragua	10	0.0	—	—	—	—
Central America	30	0.1	937	1.6	8	0.2
Latin America and the Caribbean	25,889	100.0	57,064	100.0	3,201	100.0

Source: IDB-IRELA, based on data contained in the Statistical Annex.

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Intra-regional investment

Over the last few years, the expansion and diversification of intra-regional trade has been accompanied by a major increase in investment between countries in the region. This trend is most pronounced in the Southern Cone, particularly in the São Paulo-Buenos Aires-Santiago de Chile triangle. Within MERCOSUR, there are a number of joint initiatives involving large national companies, designed to connect the member countries. This process is still in its early stages, and is very difficult to measure given the absence of full and reliable data on investment flows between these countries. Nonetheless, initial estimates suggest that the flows of intra-regional investment have topped $7.5 billion during the 1990s. Chile is the leading investor country, with outflows of $4.3 billion, followed by Brazil ($935 million) and Argentina ($900 million). The most important destinations for these intra-regional flows are Argentina and Peru (which have received some $4 billion and $1 billion respectively, from Chile).

Intra-regional investment has tended to flow to sectors in which the investor companies operate in their domestic markets, particularly in public utilities, natural resources, commerce and banking. In the case of Chile, for example, intra-regional FDI has mostly gone to the energy sector; the movement of capital between the countries in the Andean Community, especially Colombia and Venezuela, largely takes place in the financial sector and commerce; and in the MERCOSUR countries, these are concentrated in manufacturing industry: Argentine investments in Brazil are concentrated in the food and beverages industry, and Brazilian investments in Argentina in the automobile industry, metallurgy and chemicals.

Box 4: Canadian Investment in Latin America and the Caribbean

Canadian companies have centred their globalization strategies on the United States and the EU (which account for 54.4% and 21.7% of the total stock of Canadian FDI respectively). In sectoral terms, Canadian investment is concentrated in the mining, oil and financial sectors (banks and insurance companies). Latin America and the Caribbean have gradually consolidated their position as the most important destination for investment by Canadian TNCs in the developing world; the region's share of total Canadian FDI stock rose from 8.5% in 1990 to 13.7% in 1996.

According to the official figures published in *Statistics Canada*, Canadian investment in Latin America and the Caribbean has two main characteristics. First, it is overwhelmingly concentrated in the Caribbean countries, and especially in offshore centres, where companies take advantage of the tax benefits these offer. Usually,

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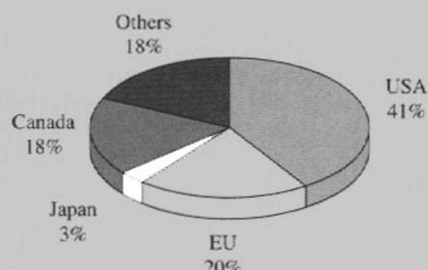
however, this capital is later channelled to another country in or beyond the region. Second, there is considerable Canadian investment in the exploitation of natural resources (mining and hydrocarbonates) in those countries which have eliminated restrictions on foreign investment in these sectors.

In spite of the distortions that investments made via offshore centres can produce in the figures, it is estimated that there is considerable Canadian investment stock in a number of Latin American countries, particularly Brazil, Mexico, Chile and Venezuela; more recently, Argentina has also attracted major investment. Brazil is the main recipient of Canadian investment in the region (with a stock of some $3.5 billion according to official figures). However, over the course of the 1990s, Brazil has been losing ground: between 1990 and 1996, Brazil's share of all Canadian investment to the region dropped from 20% to less than 12%. In a context of increasing flows of FDI, this reflects the ongoing diversification of Canadian interests in Latin America.

Chile, one of the region's main recipients of FDI, constitutes an interesting case. Canada is the second largest investor country in Chile, providing inflows on a par with those from the EU as a whole. Canada currently has ongoing or planned investments in Chile worth over $7 billion. Companies such as Falcombridge, Place Dome, Rio Algom, Cominco and Teck Corp., are involved in major prospecting operations for copper and gold in northern Chile, projects that are changing the structure and export capacity of the sector. Peru is also emerging as a major destination for Canadian mining companies. The main project involving Canadian capital is the exploitation of the mineral Antamina, in which Inmet Mining Corp. and Rio Algom Ltd. have invested some $2.5 billion.

Graph 1
Chile: Main Investor Countries, 1990-1997
(in percentages)



Source: Investment and Business Strategies Unit, ECLAC, based on data provided by the *Comité de Inversiones Extranjeras de Chile*, Santiago de Chile.

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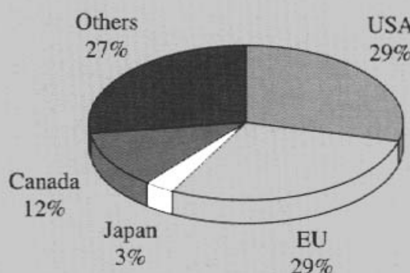
Another increasingly important recipient of Canadian investment is Argentina. According to some estimates, a number of major investments in oil and gas, mining and energy have converted Canada into the third largest investor in Argentina after the United States and Spain. At the end of 1997, most foreign mining companies were at the pre-investment stage (prospecting-exploring) in different sites, and had still not begun exploitation. Rio Algom has emerged as the largest foreign investor in the mining industry in Argentina after investing $1.2 billion in the Alumbrera copper mine over the last two years. The first shipment of mineral was made in October 1997, and exports are expected to reach $600 million a year over the next 20 years.

Graph 2
Estimates of Main Investor Countries in Argentina, 1997-2000
(percentages)



Source: Investment and Business Strategies Unit, ECLAC, based on data provided by the *Centro de Estudios para la Producción* (CEP), Buenos Aires.

Canadian investors, however, have not only acquired interests in the primary sectors. It is estimated that Canadian banks have spent more than $600 million on the acquisition of stakes in banks in Latin America. The Bank of Nova Scotia has been particularly active, imitating the strategy of the Spanish banks by embarking on an aggressive programme of expansion.

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Bank of Nova Scotia's Acquisitions in Latin America, 1990-97

Bank	Country	Equity (%)	Investment (millions of US$)
Banco Quilmes	Argentina	100	240
Sudamericano	Chile	28	30
Scotiabank of Costa Rica	Costa Rica	80	10
Banco Ahorromet	El Salvador	53	25
Inverlat	Mexico	10	31
Inverlat*	Mexico	55	143
Sudamericano	Peru	25	17
Banco del Caribe	Venezuela	25	85

Source: Investment and Business Strategies Unit, ECLAC, based on Moore, 1998.

(*) $143 million in convertible bonds when the Bank of Nova Scotia assumes control of 55% of Inverlat. The acquisition of Inverlat does not include an initial investment of $110 million to take control of an 8.4% stake.

In order to foster this process, the Canadian government has signed Investment Protection Agreements with a number of Latin American countries. These reciprocal, bilateral agreements seek to promote and protect foreign investment by granting investors the rights and obligations corresponding to national investors, and establishing mechanisms to apply measures relating to international trade (set by the WTO), the transfer of funds, transparency and dispute resolution. Canada has signed agreements of this type with Argentina, Barbados, Costa Rica, Ecuador, Panama, Trinidad and Tobago, Uruguay and Venezuela.

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NOTES

[1] In 1995 it was estimated that some 280,000 subsidiaries of TNCs sold goods and services of a total value of almost $7 billion.The growth in global sales has been 1.2-1.3 times higher than that of exports since 1987. The output of these subsidiaries tripled between 1982 and 1994, giving them a slightly larger share of total world production (6% in 1994 compared to 5% in 1982). Production by foreign-owned subsidiaries makes a more important contribution to the GDP of developing countries (9%) than to that of developed countries (5%) (UNCTAD, 1997).

[2] The relatively limited importance of developed economies as recipients of FDI is a direct consequence of the considerable rise in mergers and acquisitions involving companies in the industrialized countries, in response to the increasing protectionist pressures in some of these countries.

[3] The crisis of the Mexican peso and the so-called "tequila effect" at the end of 1994 and the beginning of 1995 seriously undermined international investors' confidence in Latin America and the Caribbean. During the first few months of 1995, there was a short-term withdrawal of capital from a number of Latin American countries, and the supply of private investment almost entirely dried up. In this context, compensatory financing by multilateral financial institutions (especially to Mexico and Argentina) enabled them to meet their short-term commitments and rapidly regain access to the international capital markets. As a result, over the course of 1995 the flow of capital in the form of FDI was maintained, or even increased, in most countries in the region, which were also able to attract increasing supplies of capital from the international bond markets towards the end of 1995 and in early 1996.

[4] Thailand, Malaysia and Indonesia were forced to abandon their fixed exchange rate mechanisms, since the effort required to maintain them ran contrary to the monetary policies they were trying to implement. On 2 July 1997, Thailand opted to float its currency, which led to an 18% drop in the value of the baht. A few days later, on 11 July, the Philippines was forced to take similar measures, which led to a 6.4% fall in the value of the peso. In mid-August, the Malaysian and Singaporean currencies slumped to their lowest levels in recent years, and Indonesia was obliged to abandon its defence of the parity of the rupee and the dollar. The Asian currencies continued to fall; this process which was accentuated by the rating that Standard & Poor gave the Malaysian and Indonesian national debts, and the latter's voluntary application for intervention by the International Monetary Fund (IMF). In mid-October, the Vietnamese and Pakistani currencies were devalued by 5% and 9% respectively. On 19 October, the resignation of the Thai Minister of Finance was followed by daily demonstrations calling for the resignation of the Prime Minister; the crisis ended with the resignation of all 48 members of the Cabinet two days later.

[5] In the wake of the Hong Kong crisis, the value of US shares fell by 2.3%, headed by some of the major multinationals (including General Electric, IBM and Exxon Corp.). At the same time, the European stock markets dropped fast, especially London (3.1%), Frankfurt (4.6%) and Paris (2.4%).

[6] The shares of the major US TNCs were the worst hit, due to predictions that their foreign profits would fall as a consequence of the crisis in Asia. As investors deserted these companies, the effects of the crisis were also felt by a number of banks. This was the case of Citicorp, one of the most globalized banks in the world, which had obtained almost 23% of its total profits in the Asian markets in 1996.

[7] Between 23 October 1997 and the end of the year, the São Paulo stock exchange lost one-third of its value, while the Brazilian Central Bank spent some $10 billion (17% of its reserves) in the currency markets in an attempt to maintain the value of the real.

[8] In terms of trade, the devaluations of the Asian currencies increased the competitiveness of these countries' exports, making competition fiercer in international markets (particularly in the industrialized countries). At the same time, Latin American products were affected by the decrease in the purchasing power of the Asian markets due to the crisis. In financial terms, the greater volatility of the capital markets increased the cost of foreign financing, which could have negative effects on growth. A report produced in March 1998 by the Analysis Department of the Bankers Trust highlighted the negative consequences of the Asian crisis for world trade. In a world in which the growing correlation between returns on currencies in global markets is reducing incentives to invest in emerging markets, the consequences of fluctuations in trade may affect the composition of portfolios,

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thereby increasing the danger of contagion. According to the report, the countries which are most vulnerable to these difficulties (as a result of the structure of their foreign trade) are Chile, Mexico and Venezuela, even though the first two have adequate mechanisms to deal with this type of situation. On the other hand, the countries which are less prepared to deal with problems of this kind (Argentina and Brazil), are also those which are less affected by the trade aspects of the crisis.

[9] This massive inflow of capital has enabled Brazil to finance its huge current account deficit. Nevertheless, the situation began to change in July 1997 as a result of the troubled situation in Asia. A halt in the inflow of capital was accompanied by a number of major withdrawals, fuelling concerns about Brazil's macroeconomic stability. Nevertheless, the situation appeared to improve in mid-March, when the Brazilian Central Bank announced record reserves of $63 billion. Much of the inflow of capital consisted of investments in the local market, as Brazilian interest rates are amongst the most attractive in the world. There has also been a constant and considerable inflow of FDI, almost $2.6 billion during the first two months of 1998: 50% up on the same period the year before.

[10] As a result, governments in the region have generally tended to tighten restrictions on short-term movements of capital. Apart from the existing rules to this effect in Chile and Colombia, Brazil has taken steps to discourage inflows of the most volatile types of capital. These measures have tended to reinforce the new pattern of capital investment in Latin America.

[11] Between 1991 and 1996, the South East Asian countries increased their share of FDI flows to the developing countries from 50.1% to 63.1%. In the same period, China's share of the flows of FDI to these Asian countries rose from 20.6% to over 50%. China is currently the largest single recipient of FDI in the developing world, and the second largest worldwide after the United States.

[12] Between 1990 and 1996, 73 public companies were sold in Brazil for a total sum of some $15 billion. The privatization process speeded up during 1997, with the sale of the Companhia Vale do Rio Dose (CVRD), the largest iron producer in the world, and part of the electricity network; in all the sell offs generated some $20 billion. During 1998, the privatization programme is expected to begin with the sale of Telebras, and to raise some $30 billion. Some observers estimate that the Brazilian government will receive more than $80 billion from privatizations over the next two years.

[13] M&A, above all in the EU and the United States, account for much of the current boom in global FDI flows: almost 50% of FDI flows involve this type of operation (UNCTAD, 1997).

[14] Between 1992 and 1997, 39% of the M&A operations in Argentina involved US companies.

[15] According to other estimates, 1997 saw a record level of M&A operations worth some $70 billion, or double the 1996 figure.

[16] TNCs have long had a strong presence in the region, benefiting from closed and relatively uncompetitive markets there. In recent years, however, the more open environment forced them to embark on a major process of restructuring and redefine their regional strategies.

[17] In statistical terms, negative FDI stock signifies that during a relatively prolonged period of time, the FDI flows to a country were insufficient to offset the depreciation in the value of capital or substitute capital re-exported to the country of origin (ECLAC, 1998).

[18] In 1997, 65.6% of the Cía. de Electricidade do Estado da Bahia (COELBA) was sold off for $1.6 billion, CCODEE for almost $1.5 billion, 90% of CNNDEE for $1.4 million, 33% of Cía. Energética de Minas Gerais (CEMIG) for $1.1 billion, and 70% of Cía. de Electricidade do Rio de Janeiro (CERJ), $587 million.

[19] In 1997, a consortium headed by the US company Bell South was awarded the licence to operate cellular telephony services in São Paulo; the operation required an investment of over $3.1 billion.

[20] Initially, the Brazilian privatization programme differed from its counterparts elsewhere in the region due to the fact that the majority of investments came from domestic pension funds and companies. This trend has changed as the programme has spread to new sectors.

[21] During 1996, Japan, Korea, the United States and the EU became concerned about Brazil's automobile policy, which establishes reduced customs duties on imports of car parts by companies producing cars with at least 60% local content. This system contravenes World Trade Organization (WTO) rules, and the countries affected are considering taking Brazil to the WTO tribunal in order to resolve their differences. However, these FDI flows are related to the long-term restructuring of the world automobile industry, and the growth of the automobile market in MERCOSUR. As a result, a number of analysts suggest that changes in Brazil's trade policy are unlikely to seriously affect this trend.

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[22] In 1996, Fiat used its Brazilian subsidiary to produce an economy model (Palio) for the Asian and Eastern European markets. Ford has adopted a similar strategy in Brazil where it makes Ka and Fiesta cars. Volkswagen has used its Mexican subsidiary to produce a Beetle (a more powerful model than the Golf) for the US market.

[23] During 1997, the opening up of the oil industry to private investment continued with the third round of the Operative Agreements involving the state-owned company PDVSA, whereby almost $2.2 billion was raised from the sale of licences to 18 groups to exploit marginal oil fields. Among the most important operations are the joint venture between PDVSA, Veba Oel (Germany) and Mobil (United States) requiring an investment of $2.4 billion dollars, and the agreement signed with CONOCO (United States), with an investment of $500 million. These are only three of the 45 private companies which have formed partnerships with PDVSA to explore and exploit the country's oil fields. The private partners are obliged to provide around 50% of the state-owned company's planned investment programme, which expects to invest some $66 billion over the next ten years.

[24] No data is available on Spanish FDI stock.

[25] Panama is the largest single destination for Japanese investment in Latin America and the Caribbean, due to the benefits that the use of "flags of convenience" offers shipping companies.

[26] In the mid-1980s, Japan emerged as a major source of FDI, encouraged by the rapid appreciation of the yen, rising local costs (particularly labour), and the tighter restrictions established in many important foreign markets (notably the United States and EU). This led Japanese companies to seek production sites abroad.

[27] Evidence for this process can be seen in the recent decisions of Japanese car manufacturers to set up operations in Argentina and Brazil, as well in the construction of a cellulose plant and an oil refinery in Brazil and in the participation in the Colombian telecommunications sector and the construction of a steel plant in Venezuela. Other major investments include the $300 million investment by Nippon Steel; the construction of Honda and Toyota assembly lines in São Paulo; Panasonic's $100 million investment plan in Manaos; the purchase of 40% of the mining company Caemi Mineração e Metalurgia (CCM) by Mitsui for $180 million; and the entry of DDI together with Motorola into the cellular telephony market.

[28] An interesting example is that of the Korean company Daewoo Electronics, which plans to invest some $159 million in Mexico in 1997 to build a plant producing television sets in the state of Sonora, and another producing refrigerators and washing machines in the state of Queretaro (70% of this production is for export).

[29] This is also the case of Goldstar, which constructed a $1.2 billion factory in São Paulo for the production of television sets. Samsung plans to invest $1 billion in a plant to produce computer monitor screens, mobile phones and refrigerators, while Asia Motors is investing $3 billion in a car assembly plant

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CHAPTER II

UNITED STATES*

Introduction

The United States has traditionally been the largest single foreign investor in Latin America and the Caribbean. Since the Second World War, the bulk of US FDI stock has been concentrated in manufacturing industry, and above all in chemicals, machinery and capital goods, and in the exploitation of natural resources. Following the wave of nationalizations in Latin America in the 1960s and 1970s, and in the current context of globalization, the pattern of US investment in the region appears to have changed. However, it is difficult to appreciate the scale and nature of these changes from the official statistics, which are distorted by the large number of investments that are channelled via financial centres. A better picture of the changing nature and destination of US FDI in Latin America can be obtained by focusing on a number of specific sectors. Hence, after commenting briefly on the global flows and stocks of US FDI in Latin America, this chapter examines a few representative examples of US investment in the region.

In particular, analysis of the automobile industry in Mexico, the *maquiladora* assembly operations in Mexico and the Caribbean Basin, and the evolution of industries such as electricity generation, transport, and communications throughout the region, offers a clearer vision of the changes in US investment strategies in Latin America over the last few years. Two different investment strategies implemented by US transnational corporations (TNCs) can be identified from this analysis. The first is based on greenfield investment in manufacturing industry, and is intended to make the TNCs more competitive in the US market in the face of tough competition from third countries. The second strategy, which is found above all in the service sector, consists of the acquisition of existing companies in order to supply local markets. This is often linked to the privatization process, and is another key element in the response of these companies to the challenge of global competition.

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A note on the statistics

Although the US government publishes abundant statistics on US FDI, they can give a distorted view of the sectorial breakdown of investment in the region.[1] This is because much of the total investment recorded in the statistics consists of capital invested in offshore banking centres. These centres are often only intermediary, stopping points for the capital, and it is very difficult to identify the final destination of such investments. The distortions this can cause are exemplified by the differences between the figures for the sectoral classification of US foreign affiliates, and those from the parent companies in the United States. The former indicate that the proportion of US FDI in manufacturing industry rose from 27% of the total in 1982 to 41% in 1989, before falling to 24% in 1995. Yet according to data from the parent companies, there has been no drop in manufacturing industry's share of US investment in the region, which has remained constant at around 55% of the total. This problem is particularly serious in the case of Latin America and the Caribbean.

Graph 1 highlights the enormous impact that operations channelled via the offshore banking centres in Latin America and the Caribbean (notably Bermuda, Panama, the British offshore centres in the Caribbean, the Netherlands Antilles, the Bahamas, etc.) have on the figures for US FDI in the region. For a period during the 1990s, for example, more US FDI flowed to these centres than to the three largest recipient countries in the region (Brazil, Mexico and Argentina) combined. This anomaly indicates that while the official statistics suggest that manufacturing industry's share of all US FDI in the region fell significantly between 1982 and 1989 (from 18% to 14%) before recovering slightly between 1989 and 1996 (when it rose to 15%), investment in manufacturing has in fact become increasingly important for US TNCs. This is explained by the fact that much of the investment in this sector was channelled via non-manufacturing affiliates in these banking centres.

This interpretation of the data for US FDI in manufacturing industry accords with the results of much of the research carried out in the region. These studies suggest that the destination of US FDI in Latin America and the Caribbean becomes much clearer when the focus shifts from the aggregate figures to certain specific industries. Representative sectors include automobile production in Mexico for the US market, and in Brazil and Argentina to supply the Southern Common Market (*Mercado Común del Sur*, MERCOSUR) as well as another area of manufacturing industry, the assembly plants (*maquiladoras*) found in Mexico and the Caribbean Basin. Significant investment operations in

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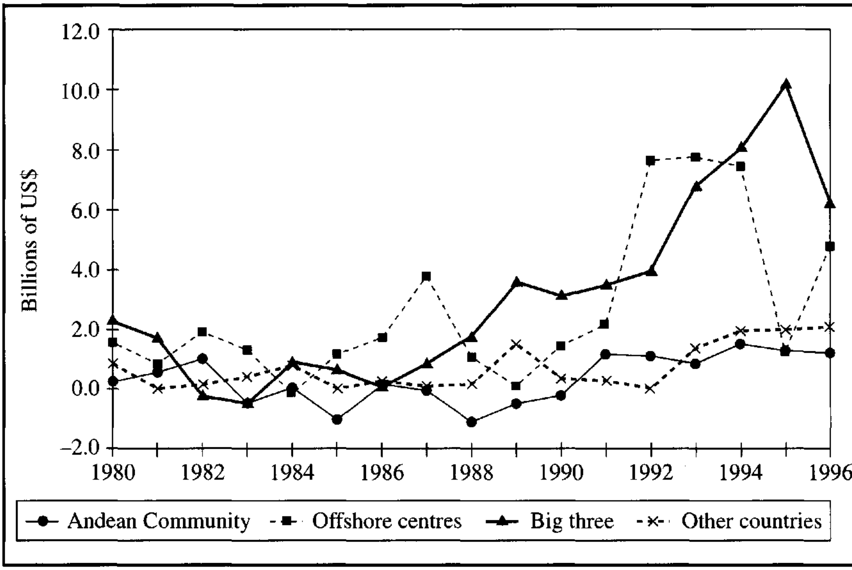
the service sector include the acquisitions made by US companies in many countries throughout the region. This line of enquiry also casts more light on the way in which US TNCs have adapted to the globalization process, thereby making it possible to offer a more profound analysis of their operations in Latin America and the Caribbean.

Graph 1
US FDI in Latin America and the Caribbean, 1980-1996



Sources: US Department of Commerce, Bureau of Economic Analysis, *Survey of Current Business* (various issues).
Note: The Big three are Argentina, Brazil and Mexico.

US FDI in Latin America and the Caribbean in the 1990s

In order to respond to the new opportunities and challenges arising in the international market, US companies investing abroad have adopted diverse strategies in different sectors. This section briefly analyzes the evolution of global FDI flows, before looking more specifically at three different types of

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investment by US companies in Latin America. This second line of analysis provides a much clearer, qualitative picture of some of the trends in US FDI in the region over the course of the 1990s.

In terms of the global flows, some significant changes can be seen in the investment strategies of US companies, traditionally the largest foreign investors in the world. According to the statistics produced by the US Department of Commerce, total FDI (expressed in historical costs) rose from $207.3 billion in 1982 to $796.5 billion in 1996.[2] Although much of this investment is still concentrated in Europe (half the 1996 total), there have been some changes in the geographic distribution of US FDI. Regions such as Latin America and the Caribbean and Asia have seen major growth. The proportion of total US FDI in Latin America and the Caribbean rose from 13% in 1982 to 18% in 1996. In Asia, Japan's share of the total rose from 3% to 5% over the same period, while the proportion received by developing countries in Asia increased from 6% to over 8%.

These increases have been offset by a reduction in the share of other, traditionally more important destinations, such as Canada, whose proportion of the total fell from 21% to 12% between 1982 and 1996. While the largest changes in Asia were due to the increased flow of FDI to Japan in the period 1982-1989, and to the newly-industrialized countries (NICs) in the 1990s, FDI in Latin America and the Caribbean has risen continuously during the 1990s (with the exception of 1996). US FDI in Latin America and the Caribbean (excluding the offshore centres mentioned above), increased from $3.2 billion in 1990 to a record $13.5 billion in 1995.

The annual average flow of US FDI to the region for the period 1990-1996 was therefore more than $7 billion higher than the average for the 1980s, although in 1996 US investment in the region dropped by around $4 billion with respect to 1995, in the context of a slump in the flows of US FDI to all the emerging markets. Even so, US FDI in Latin America in 1996 was still higher than the average for the period 1990-1996 (see Table 1), and the provisional figures for 1997 suggest that this downward tendency has already been reversed. As for the national distribution of US FDI stock in the region, the 1995 data shown in Graph 2 confirms the pattern of flows seen in Table 1. In 1995, just six countries accounted for almost 90% of the stock, while Brazil and Mexico alone held over half the total.

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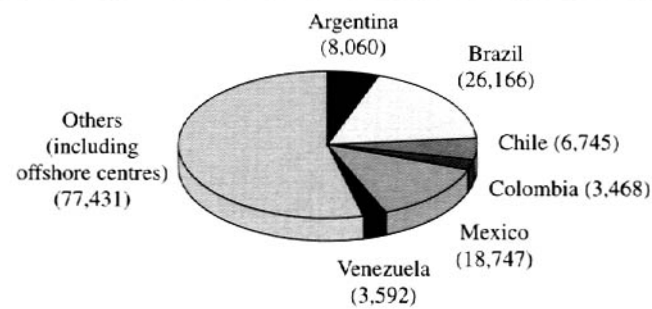
Table 1
Flows of US FDI to the Six Largest Recipient Countries and the Offshore Centres
(in millions of US$)

Country or region	Averages								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Argentina	123	836	164	415	558	1,079	931	2,291	415
Brazil	663	2,674	1,054	869	2,054	3,263	3,517	4,899	3,064
Chile	106	682	293	226	106	198	1,554	1,406	994
Mexico	357	2,478	1,949	2,183	1,320	2,516	3,674	2,955	2,747
Peru	26	247	346	26	3	8	231	317	800
Venezuela	27	589	39	1,248	692	555	644	554	390
Offshore centres	1,329	4,648	1,463	2,176	7,657	7,763	7,431	1,278	4,765
Latin America and the Caribbean	2,803	12,809	4,797	7,157	12,751	16,895	19,010	14,753	14,299

Source: IDB-IRELA, based on data from the Statistical Annex.

Graph 2
US FDI Stock in the Six Main Recipient Countries in Latin America and the Caribbean
(in millions of US$)



Source: See Statistical Annex.

These global figures confirm that Latin America and the Caribbean constitute a key area of investment for US TNCs, while the upward tendency shows that the region's role in their corporate strategies has changed over the

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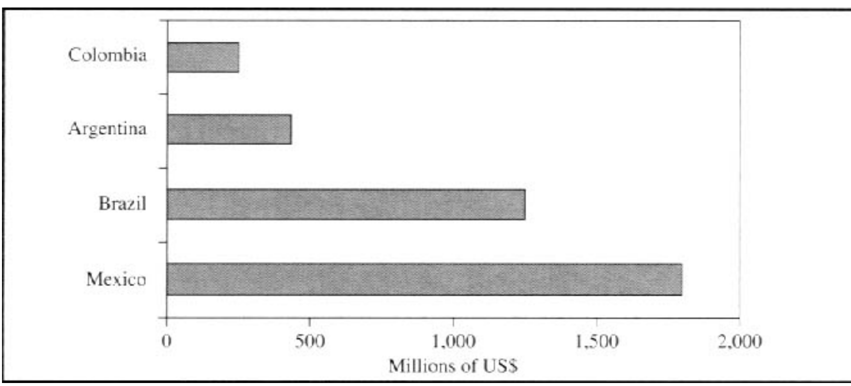
last few years. As can be seen in a number of specific sectors, there have been two main types of strategy:

— in manufacturing industry, US investment has sought to improve competitiveness in the US market, particularly against competition from Asian companies; and

— in the service sector, US companies have adopted a more aggressive strategy of market penetration, essentially by acquiring existing companies, in accordance with their overall response to globalization.

In manufacturing industry, during the phase of import substitution industrialization (ISI) US TNCs set up miniature replicas of their US plants in Latin America and the Caribbean (see Graph 3). These plants enabled them to assemble their products locally, using mainly imported components, and then to sell them in protected local markets. In order to do this they had to establish an affiliate in each market, and there was little trade between them. When restrictions were later eased on trade and FDI, the TNCs were obliged to adapt their strategies to an environment in which survival depended on achieving competitiveness at the international level. The impact of these changes can be seen from two examples: car production and the *maquiladora* assembly plants.

Graph 3
The Four Main Destinations for US FDI in Manufacturing Industry, 1996
(in millions of US$)



Source: Deloitte Research - Manufacturing Institute

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Regional integration and automobile production in the region[3]

In 1993, three of the world's largest car producers were US companies which assembled a large proportion of their passenger vehicles outside the United States. These companies were General Motors (GM), which assembled 48% of its production outside the United States, Ford (59%) and Chrysler (48%). Much of this assembly work was carried out in Latin America: GM assembled 8% of its production in the region, Ford 9% and Chrysler 17.5%.

GM, Ford and Chrysler held first, third and fifth place, respectively, in the ranking of the 50 largest TNCs in Latin America in terms of volume of sales: their combined sales accounted for 20% of total sales of the 50 largest foreign companies in Latin America and the Caribbean. In 1996 (see Table 2), the automobile industry constituted the main focus of TNC activity in the region, as 10 of the 28 largest foreign companies in terms of sales were vehicle manufacturers.

Table 2
The Ten Largest Automobile Companies Operating in Latin America
(in millions of US$ and percentages)

Position All	Position TNCs	Company	Origin	Sales	Exports	Export/ Sales
5	1	VW (Brazil)	Germany	7,003.3	n.a.	n.a.
7	2	Chrysler (Mexico)	USA	6,455.4	4,948.3	77
8	3	GM (Mexico)	USA	6,345.6	4,526.5	71
10	4	GM (Brazil)	USA	5,432.9	611.6	11
12	5	Fiat (Brazil)	Italy	4,742.9	329.9	14
18	8	Ford (Mexico)	USA	3,879.1	2,387.1	62
19	9	Ford (Brazil)	USA	3,830.1	n.a.	n.a.
49	16	Mercedes Benz (Brazil)	USA	2,130.9	249.0	12
63	20	Nissan (Mexico)	Japan	1,800.0	1,050.9	58
85	28	Ford (Argentina)	USA	1,464.6	n.a.	n.a.

Source: "Las 500 mayores empresas de América Latina", *América Economía*, 1997-1998 edition.
Note: All: in ranking of all companies; TNCs: in ranking of transnational corporations.

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Although these companies have been operating in the region for some time, the Latin American automobile industry has been radically restructured over the last few years. US FDI, channelled via GM, Ford and Chrysler, has played a significant role in this process. Table 3 gives an overview of the general situation in the industry during the 1980s, and the changes that have taken place in the 1990s. In the 1980s, Brazil led the way in terms of total production, with an output of 1,165,100 units; this was more than twice the Mexican level (490,000 units) which, in turn, almost doubled that of Argentina (281,800 units). The figures also show that most of this production was destined for domestic markets and, consequently, very little for export (in 1981, exports accounted for 14% of production in Brazil, 4% in Mexico, and just 1% in Argentina).

The Latin American debt crisis created major problems for the respective national automobile industries, whose production levels stagnated for almost a decade. During this period, the Mexican automobile industry became much more export-oriented; more recently, its counterparts in Argentina and Brazil have followed suit. In this respect, the automobile industries in these three countries exemplify some of the key features of the new corporate strategies of US TNCs.

The new national and international environment in the 1990s has brought far-reaching changes in the Latin American automobile industry. By 1996, total production was far higher than in 1980: Mexico's output was 2.5 times higher and Brazil's was 1.6 times higher, while Argentina was something of an exception, with an increase of only 10%. These changes were not confined to the spectacular growth in total production. There has also been a dramatic increase in the value of exports from these countries (which were 53.6 times higher in the case of Mexico and 29.4 times higher in Argentina, although Brazilian exports only doubled in value). At the same time, and reflecting the existence of a more competitive environment, imports made major inroads into domestic markets, absorbing 48% of demand in Argentina (1996), 22% in Brazil (1995), and 5% in Mexico (1994).

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Table 3
Mexico, Brazil and Argentina: Vehicle Production, Exports and Imports, 1980 - 1996
(in thousands of units)

	Annual average									
	1980-89	1990-96	1980	1990	1991	1992	1993	1994	1995	1996
MEXICO										
Total production	455	1,031	490	821	989	1,081	1,080	1,097	931	1,211
Exports	77	544	18	277	351	383	472	575	779	971
Imports	—	—	—	—	—	6	3	56	17	30
BRAZIL										
Total production	959	1,338	1,165	914	960	1,074	1,391	1,581	1,629	1,814
Exports	222	286	157	187	193	342	332	378	263	306
Imports	—	141	—	3	28	45	97	218	369	224
ARGENTINA										
Total production	171	264	282	100	139	262	342	409	285	313
Exports	2	36	4	1	5	16	30	39	53	109
Imports	—	—	—	—	17	106	110	1,741	101	152

Sources: Compiled by the author from data supplied by the national automobile industry associations: AMIA (Mexico), ANFAVEA (Brazil) and ADEFA (Argentina).
(-) Almost zero.

Another key dimension of the new corporate strategies in the industry has been heavy investment in modernizing plants and increasing productivity in the largest automobile markets in the region. The most innovative aspect of these investments is that, unlike in the past, they have not only been destined for national markets, but also to meet the demands of specific regional markets. That is, automobile manufacturers modernized and transformed their operations in accordance with the sectoral regulations established in the North American Free Trade Agreement (NAFTA) and MERCOSUR, which opened the door for the development of new corporate strategies. Regional integration, therefore, has played a major role in the restructuring of these companies, which now operate on a global scale.

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The restructuring of the Mexican automobile industry

A number of detailed studies have been made of the history of the transformation of the Mexican automobile industry.[4] These show, for example, that in 1996 Mexico produced 797,682 passenger vehicles, almost four times more than in 1983 (207,000), and that almost 80% of these vehicles were exported. There was almost $10 billion of FDI in the industry, which was initially invested in engine plants and subsequently in modern car plants. This FDI totally transformed the Mexican automobile industry, significantly increasing its contribution to the country's economy, particularly when the increased activity in the assembly of car components is taken into account.

Between 1990 and 1996, the value of exports in the Mexican automobile industry (vehicles, engines and components) increased almost fivefold, from $4.5 billion to $17 billion. Over 90% of these exports went to the US market. In 1995, Mexico supplied 8% of the passenger vehicles imported by the United States, as well as 10% of its commercial vehicles, 12% of the engines and 8% of the components. As a result, automobile exports accounted for some 20% of the total value of Mexican exports to the United States that year.[5] There has also been a major improvement in productivity, since increased output has been accompanied by a reduction in the total number of people employed in the industry.

The transformation of the Mexican automobile industry was to a large extent a response to the strong competition from Japanese companies. They reduced the European and US companies' share of the market, and created excess supply in a very competitive environment. Japan's market share of car imports to countries within the Organization for Economic Cooperation and Development (OECD) rose from 11.7% in 1971 to 26% in 1990, while most European and US companies suffered a sharp drop in sales. The strategies adopted by the three largest US car producers (Ford, GM and Chrysler) in response to this situation shared a number of key features, particularly with respect to the US market. All of them invested heavily in new engine and vehicle plants in Mexico, imported passenger vehicles into the United States, and incorporated components assembled by *maquiladoras* into their US production systems. As a result, even before the 1994 financial crisis, two-thirds or more of the passenger vehicles produced by these companies in Mexico were destined for the US market.

The changes implemented by the Ford Motor Company (see Box 1) exemplify the transformation of these companies' operations, and the way in

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which they integrated their Mexican operations into their overall production system. In the case of Ford, the company's new international strategy was based on the creation of a series of strategic alliances, including the acquisition of minority shares, with competitors with more advanced technology or greater organizational capacity. Ford acquired a 25% stake in Mazda Japan (now increased to 34%) and 50% of Mazda United States. Between 1982 and 1992, Ford invested almost $3 billion in Mexico in order to make it more competitive in the United States, and above all in the small car market.

A number of factors account for the success of this strategy. These include specialization in a smaller range of models, the introduction of Japanese production and organizational techniques, Ford's use of components made by its *maquiladora* plants in car assembly, and the new role assigned to specialist suppliers. Other US TNCs soon began to adopt similar strategies, integrating their Mexican car and component plants into their overall production system.

These strategies were reinforced by the rules established in NAFTA, which incorporated the Mexican automobile industry into the existing US-Canadian agreement on the motor industry. This has meant that US tariffs on Mexican imports have been reduced from 2.7% to 0.6% for vehicles, and from 1.7% to 0.4% for components. TNCs established in Mexico have benefited enormously from these tariff reductions, which have helped to consolidate their positions and strategies. Between 1993 and 1996[6], the three largest US TNCs in the automobile industry invested almost $3 billion in Mexico, or the equivalent of 10% of their investments in the United States.

The value of Mexican vehicle exports to the United States rose from $4.6 billion to $11.7 billion during this period, making Mexico the second largest supplier to the US market, and putting it ahead of Germany. At the same time, the value of exports of components increased from $3.6 billion to $7.1 billion, putting Mexico in second place in this sector, ahead of Japan. Mexico's market share of US automobile imports rose from 6.5% to 13.4%, and of components from 16.6% to 23.7%, while other exporting countries, including Canada, saw a drop in their market share in both sectors. Along with the textile, electronics and chemical industries, the automobile industry was clearly one of the principal beneficiaries of NAFTA.[7]

NAFTA's sectoral agreement for the automobile industry is not, therefore, simply an instrument for the liberalization of markets in member countries. More

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importantly, in certain segments of the US market, it has enabled US TNCs to use their foreign investment strategies to obtain significant competitive advantages (production costs, integrated supply chains, preferential access, etc.) over non-US competitors. Above all, they have done so by using Mexico as a base for low-cost, high-quality exports, taking advantage of their preferential access to this market. In this way, the major US automobile manufacturers have integrated NAFTA into their global investment strategies.

Box 1: The Transformation of Ford's Operations in Mexico

The first Ford factories in Mexico were built in Cuautitlan, near Mexico City, to assemble vehicles for the local market. Considered to have been relatively inefficient, these plants had a capacity of only 60,000 units a year, and were used to assemble a number of different models. Ford embarked on a new strategy in 1983, when it established its Chihuahua engine plant with a production capacity of 200,000 units for export to the company's factories in the United States. This plant has been described as "a factory with a large output, producing for export and intended to compete with the best engine plants in the world", and is said to have demonstrated that "advanced production processes can be transferred successfully to newly-industrialized countries".[8] Output was increased to 500,000 units a year in the period 1992-1993, mainly in order to supply high-tech engines to the Ford plants around the world.

Ford's second largest investment in Mexico was a car assembly plant in Hermosillo, which produced the Mercury Tracer model. Designed by Mazda, this plant was built in 1986 and enlarged in 1990 in order to incorporate production of the Ford Escort and increase its annual capacity to 160,000 units. The plant was designed to reach levels of quality and output to match or beat those of the company's international competitors. Recently, it has produced the highest quality Ford cars in North America, and was ranked fifth in terms of quality out of the 46 car assembly plants in the region.

Ford's other manufacturing operations in Mexico consist of 11 assembly plants and three joint ventures with Mexican companies producing components. The new system of production is based on the use of more specialized suppliers. The success of these flexible production techniques varied considerably in the different plants. The Cuautitlan plant was simply restructured in order to introduce the new production methods, while the Hermosillo and Chihuahua plants were specially designed to use the most advanced technology and management methods.

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The transformation of Ford's Mexican operations has been reflected in its products. Between 1978 and 1982, when ISI production techniques were used, Ford Mexico sold locally assembled vehicles. Over the next four years, these models were replaced by new models that were nonetheless still produced at the Cuautitlan plant. With just a few exceptions, annual production of the original models never rose above 20,000 units, and none were exported until 1987. In the period 1988-1992, several new models were produced for export, and annual production averaged 50,000 units. Production of these models (Tracer and Escort) for export came to constitute the core activity of Ford's Mexican plants. Through specialization, Ford was able to reach the minimum requirements of scale (100,000 units) for efficient production of the Escort. In 1996, Ford Mexico became the fifth largest company in Mexico in terms of sales, exporting vehicles and parts to a value of almost $2.4 billion, compared to just $14 million in 1985.

In short, the corporate strategy implemented by Ford during the 1980s had a major impact on the Mexican automobile industry. The key element of this strategy was specialization in producing the modern Zeta engine and two models of cars, first the Mercury and then the Escort. In 1996, Ford exported 186,249 cars, and by mid-1997 the company was responsible for 33.4% of all Mexican automobile exports.[9]

At the same time, Ford's production for the Mexican market dropped to a mere 14,780 units in 1996. Ford became the largest car importer in the country, the company's imports peaking in 1994 with 23,300 units, followed by a drop to 16,651 in 1996. Evidently, Ford's initial strategy did not include the modernization of its existing Cuautitlan plant, which was only intended to supply the domestic market; instead, it was based on the construction of a new high-tech engine and vehicle assembly plants to supply the highly competitive US market. With this strategy, and investments of $3 billion in the period 1982-1992, Ford successfully integrated its new Mexican plants into its US production system.

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Assembly of manufactured goods in Mexico and the Caribbean Basin[10]

Over the last few years, other US manufacturers have faced similar challenges to those that Japanese companies represented for US automobile TNCs in their domestic market. Between 1980 and 1995, producers from developing countries in Asia increased their share of the US market from 15% to 25% (China's share alone rose from 0.5% to 6%). The sectors that have suffered most from competition from Asia include the machinery and electronic equipment industries, clothing and footwear, games and sports equipment, as well as other low-tech sectors. In response to this challenge, US TNCs have concentrated on setting up assembly plants in Mexico and the Caribbean Basin.

The strategy adopted by these companies is based on the use of what might be called a "low wage export processing area" which, generally speaking, comprises Mexico and a number of Caribbean countries, notably the Dominican Republic and Costa Rica. In the case of Mexico, this type of operation is particularly common in the following sectors: electrical machinery and electronic equipment; equipment for the distribution of electricity, telecommunications, and electronic equipment for producing circuits and electrical machinery. In 1995, these sectors accounted for 20% of all Mexican exports to the United States, while clothing accounted for a further 4% of the total.

In the case of the Dominican Republic, however, the clothing industry accounted for almost 50% of all exports to the United States, well up on the figure of 10% in 1980. The other main exports consisted of medical instruments, electrical equipment for the production of circuits, and jewellery. Clothing is also Costa Rica's main product for the US market, accounting for 36% of all its exports in 1995 (compared to around 9% in 1980). It can be seen, therefore, that US TNCs in a number of sectors use, to varying degrees, affiliates in Mexico and the Caribbean Basin to supply electrical and basic electronic equipment and clothing to the US market.

Three factors give these TNCs special access. Firstly, they take advantage of rule HTS 9802 on tariffs, which allows companies based in the United States to export components produced in the United States for assembly abroad, and determines that they are only required to pay duty on the value added abroad (in most cases, mainly wages) when these products are reimported. Secondly, they benefit from the Caribbean Basin Initiative (CBI) which established preferential tariffs and increased the quotas for these countries in the US market. Finally, there are the benefits that NAFTA has brought to Mexico, thanks to the rules of origin included in this agreement.

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The importance of rule HTS 9802 can be seen from Table 4. Of all the developing countries, Mexico has benefited most from this regulation; in fact, almost half of all US imports under this rule come from Mexico. The Caribbean Basin countries taken as a whole have been the second main beneficiary, as their market shares have increased significantly in the period 1990-1996. Many of the US imports from Mexico (42% of the total) and the Caribbean countries - Dominican Republic (60%), Costa Rica (39%), Honduras (47%), Guatemala (35%), El Salvador (62%), and Jamaica (56%) - entered the US under HTS 9802, while the figures are much lower in the case of the Asian countries. This mechanism, therefore, gives US TNCs significant competitive advantages over their Asian rivals.

The advantages of this mechanism can be seen most clearly in the clothing industry. Asian countries used to dominate US imports of textiles and clothing; in 1990, imports from these countries to the United States were worth $20.2 billion (or 72% of the total). By 1996, however, imports of textiles and clothing from Mexico and the Caribbean Basin had risen from $2.7 billion (10% of the total) in 1990 to $10.3 billion (22% of the total), while Asia's share had dropped to 59%. During the same period, clothing imports under rule HTS 9802 increased from $1.4 billion (6% of the total) to $8.9 billion (19%). Some 95% of these imports came from Mexico and the Caribbean Basin.

In this way, US TNCs used rule HTS 9802 to obtain competitive advantages that enabled them to compete with Asian firms in their domestic market by investing in Latin America and the Caribbean. Mexico and the Caribbean Basin countries encouraged this process, establishing special areas for processing exports, as well as programmes designed to promote the creation of *maquiladora* assembly plants. Under these programmes, exporters can take full advantage of low labour costs, while also benefiting from tariff exemptions on products imported for assembly and re-export, as well as exemption from taxes on exports, earnings, and the repatriation of profits and capital. With the introduction of simpler customs procedures in these countries, administrative costs have also been reduced.

Moreover, the implementation of NAFTA has given Mexico a number of advantages which are not available to the Caribbean Basin countries. In accordance with the agreement, companies based in Mexico benefit from a six point reduction in duties, and import quotas have been abolished on a large number of articles. In addition, they have been able to include the Mexican inputs used in their products as part of the percentage of US components required under the terms of NAFTA. These advantages, combined with the major

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devaluation of the peso in 1994-1995, encouraged many US companies to invest even more heavily in *maquiladora* plants, and to relocate some of their operations from the United States to Mexico.

However, the advantages that NAFTA has brought Mexico have also led other countries to adopt different strategies, designed to enable them to compete in other industries by means of investments of this kind. For example, Costa Rica, which was losing its comparative advantage with respect to wages, has attempted to shift towards more hi-tech, precision industries. One result of this change in strategy is that Intel, which produces integrated micro-processors for computers, has decided to invest $300-$500 million in Costa Rica in the period 1997-1998.

Table 4
US Imports from Developing Countries under Rule HTS 9802, 1990 and 1995
(in billions of US$ and percentages)

Country	1990	1995	Exports to the US as % of total exports
Mexico	12.8	25.0	42
Malaysia	1.4	2.8	16
Dominican Republic	0.7	1.9	60
South Korea	2.2	1.8	8
Philippines	0.6	1.7	25
Taiwan	1.0	1.2	4
Singapore	1.3	1.0	5
China	n.a.	0.9	2
Thailand	0.5	0.8	7
Costa Rica	0.3	0.7	39
Honduras	n.a.	0.7	47
Hong Kong	0.3	0.6	7
Guatemala	n.a.	0.5	35
El Salvador	n.a.	0.5	62
Jamaica	0.2	0.5	56
Subtotal	21.3	40.5	—
All the rest	1.4	1.3	—
TOTAL	22.7	41.8	13

Source: US Department of Commerce

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Investment in assembly plants in Latin America – to benefit from rule HTS 9802 and in reaction to Asian competition in the US market – is therefore another reflection of the way in which US FDI in the region is responding to the challenge of globalization. In this case, the strategy of US TNCs is based on production in areas in Mexico and the Caribbean Basin offering special conditions for exports and relatively low wages, in order to improve competitiveness in their home market.

In terms of the recipient countries, the consequences of this type of investment will depend on the benefits they are able to offer US companies. If the only added value in the region is that obtained from the use of unskilled labour to produce exports, the impact of this investment will be largely confined to the direct employment generated by these activities and, in terms of the balance of payments, to the small proportion of the exported value that the country retains in the form of hard currency. If, in contrast, recipient countries can attract more technologically advanced activities, and provide high quality domestic inputs at competitive prices, these investments could have a greater impact, generating internal production linkages and other types of positive externalities (for example, training).

The acquisition of companies in other sectors

A third important new dimension of US FDI in Latin America and the Caribbean consists of the growing number of acquisitions in the region, particularly of former state-owned companies. Again this trend has been encouraged by the need to adopt new strategies in the face of changes in both international markets and in the economic situation in different countries. In the years leading up to the debt crisis in the 1980s, hardly any foreign companies operated outside manufacturing industry. This is explained by the fact that foreign companies were legally excluded from almost the entire service sector, while the mining and energy sectors had been the object of a wave of nationalizations and expropriations. However, this situation changed dramatically as a result of the liberalization of the economies in the region and the privatization of state-owned companies.

These two related processes are responsible for the major increase in US involvement in the exploitation and export of natural resources, as well as in the service sector, where they serve local markets. Of particular importance is US FDI in energy and communications, in which a number of US companies now play an important role. Generally speaking, their penetration of these sectors began with relatively small investments, which only later were followed by

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much heavier programmes of acquisitions. As a result, a number of US companies have become established as leading players in the increasingly competitive Latin American energy and service markets, which now constitute just another field for global competition among the TNCs. This can be seen from an analysis of some representative examples of recent operations by US companies in these sectors.

There have been several significant developments in the energy sector, which comprises a number of related activities including oil, gas and electricity production. US TNCs have begun to re-establish their presence in the oil industry in Latin America, albeit without achieving the dominance they had enjoyed before the nationalizations of the 1960s and 1970s. On privatization, various US companies acquired small stakes in the largest oil company in Argentina, Yacimientos Petrolíferos Fiscales (YPF), while the two most important companies in the region, Petróleos Mexicanos (PEMEX) and Petróleos de Venezuela (PDVSA), have still not been directly privatized. Amoco and Mobil bought some former state-owned assets in Bolivia and Peru, respectively. However, the major investments in this sector have been in the exploration and development of new oil fields in Venezuela, where a number of US TNCs have participated with local companies in projects worth over $2 billion.

The role of US TNCs in the electricity production and generation sector has been strengthened through the acquisition of state-owned companies. AES and Southern Electric have been particularly active in this type of operation. Between 1994 and 1997, these two companies invested more than $5 billion in the acquisition of privatized companies. Southern Electric began by making a small investment in state-owned assets in Trinidad and Tobago, but the scale of their operations has increased significantly since then. Major investments by the company include the acquisition of majority stakes in Light Serviçöes de Electricidade and the Cia Centro-Oeste de Distribuçäo de Energia in Brazil, and the shares acquired in Hidronor and the Empresa de Servicios Eléctricos de Buenos Aires (ESEBA) in Argentina. This programme of investments has made them major actors in the sector, competing with corporations such as Endesa from Spain and the Chilean companies Enersis, Chilectra and Chilgener.

Another area of the energy sector which has seen considerable expansion by US TNCs is the gas industry. One representative example of this tendency is Enron which, either alone or in partnership with other companies, has made acquisitions worth around $1.1 billion. Enron began rather cautiously by acquiring a stake in the Argentine Transportadora de Gas del Sur when it was privatized in 1992, but strongly reinforced its position in 1996-1997 through a

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series of acquisitions in Colombia, Bolivia and Brazil, the scale of investment increasing substantially on each occasion. Although it faces tough competition from a number of companies in the United States (Mobil, CM Energy) and Europe (Repsol in Spain, Royal Dutch Shell, and British Gas), Enron exemplifies the very aggressive strategies that a number of US companies have adopted in the Latin American market.

In telecommunications, competition in the region has become much more intense as a result of the dismantling of the traditional state monopolies. The US TNC Bell South has been one of the most aggressive operators in this sector. The company has made a number of major investments, particularly in the field of mobile telephony, investing a total of $2.8 billion in the period 1991-1997. Bell South was involved in a few small operations in Venezuela in 1991, followed by similarly modest investments in Guatemala and Peru, before embarking on a more ambitious programme of expansion, first in Brazil and then in Argentina and Bolivia. As a result, in the space of just a few years it has become one of the major telecommunications companies in Latin America, competing alongside the Spanish giant Telefónica, as well as other US companies.

It can be seen, therefore, that the liberalization of the energy and service sectors in Latin America and the Caribbean has enabled US companies to adopt new expansive strategies in the region. They have adopted these in response to economic opportunities and structural changes in these countries, as well as the behaviour of their competitors in the global markets. Latin America has therefore become an important area for global competition among the leading TNCs in these sectors.

Conclusions

Latin America and the Caribbean constitute areas of vital importance in the strategies that US companies have adopted in the face of the new challenges of globalization. Given the way in which US investment in the region's offshore banking centres can distort the aggregate figures, these offer only a rough indication of the real situation, which can be seen much more clearly by analyzing some representative examples of FDI by US companies in the region. These show how the traditional pattern of investment has changed substantially, as companies have adapted to the demands and opportunities created by the globalization process and programmes of structural reform implemented in the region.

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Two types of strategies followed by US TNCs over the past few years have been identified in this chapter. The first consists of investing in specific countries in the region in order to export to the US market and obtain competitive advantages, particularly with respect to their Asian rivals. This strategy lies behind the investments of US automobile companies in Latin America, as well as the assembly plants (*maquiladoras*) established by manufacturers in other sectors. The second strategy is intended to increase the companies' share of markets in the region, particularly in the energy and service sectors. This strategy, which has usually gone hand-in-hand with the wave of privatizations in the region, was made possible by the removal of barriers to investment in, and trade with, Latin America, and constitutes a key aspect of the overall strategy of these companies for increasing competitiveness in the global market.

NOTES

[1] See Stekler, L.E. and G.V.G. Stevens, "The Adequacy of US Direct Investment Data", *International Finance Discussion Papers* 401, Washington D.C.: Board of Governors of the Federal Reserve System, June 1991, and "A Guide to BEA Statistics on US Multinational Companies", *Survey of Current Business*, March 1995.

[2] Figures taken from "US Direct Investment Abroad: Detail for Historical Cost Position and Related Capital and Income Flows, 1996", *Survey of Current Business 77:9*; *US Direct Investment Abroad: 1982 Benchmark Survey Data*; and *1989 Benchmark Survey Data,* US Department of Commerce, Washington D.C., December, 1985 and October, 1992.

[3] This analysis is based on information and data contained in the following documents, all of which were written by the author: "The Automotive Industry in NAFTA (Mexico), MERCOSUR (Brazil and Argentina) and ASEAN (Thailand)" prepared for the UNCTAD research project on Industrial Restructuring and International Competitiveness, Geneva, 1997; "Dimensions of Latin American Integration: NAFTA and MERCOSUR Automobile Industries", prepared for *Transnationals*, 1997; and "Transforming Sitting Ducks into Flying Geese: The Mexican Automobile Industry", *Desarrollo Productivo* 26, UN-ECLAC, LC/G, 1985 Santiago de Chile, October, 1995.

[4] See,for example, Michael Mortimore, "Transforming Sitting Ducks into Flying Geese: The Mexican Automobile Industry", *Desarrollo Productivo* 26, UN-ECLAC,LG/C, 1985, Santiago de Chile, October 1995.

[5] Calculated from ECLAC's computer model on international competitiveness, CAN PLUS.

[6] Shaiken, H., and S. Herzenberg, "Automatization and Global Production: Automobile engine production in Mexico, The United States and Canada", *Monograph Series* 26, Centre for US-Mexican Studies, University of California, San Diego, 1987.

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[10] Information taken from the following studies by author: with Calderón, A. and W. Peres, "Mexico: Foreign Investment as a Source of International Competitiveness", in Dunning, J. and R. Narula (eds.), *Foreign Direct Investment and Governments,* Routledge: London and New York, 1996; with W. Peres, "Policy Competition for Foreign Direct Investment: Costa Rica, Jamaica and the Dominican Republic", report prepared for the Development Centre research project on "Policy Competition and Foreign Direct Investment", OECD, Paris, February 1997; with Duthoo, H. and J.A.

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CHAPTER III

JAPAN*

Introduction

During the 1980s, Japan emerged as the single most important investor country at the global level. This was largely a consequence of the strong rise in the value of the yen, growing domestic labour costs, and the consolidation of Japan's foreign trade relations. Japanese foreign direct investment (FDI) flows peaked in 1989 (at around $67.5 billion in declared value). After a period of decline, Japanese FDI has recovered over the last few years and topped $49 billion in 1996.

By the end of 1996, 46% of Japanese FDI was invested in the United States, while Asia's share of the total continued to rise (24%). Latin America, however, had yet to recuperate the levels of investment it had enjoyed before the foreign debt crisis of the early 1980s. Japanese investment in manufacturing industry has grown steadily over the last few years, and flowed above all to the United States, Asia and Europe. In contrast, Latin America has attracted relatively little Japanese manufacturing investment. However, the situation has shown signs of improving more recently. This chapter analyzes recent trends in Japanese FDI in the region, focusing on the strategies adopted by Japanese transnational corporations (TNCs) and their apparent impact on the development of Latin America and the Caribbean.

It should be emphasized that the statistical data on Japanese FDI flows presented and analyzed in this chapter comes from two different sources; while the information they give rarely coincides, they offer complementary images of the same phenomenon. Firstly, there is the register of notifications of foreign investments made by Japanese companies and kept by the Japanese Ministry of Finance. The second source of data consists of the information gathered by the Bank of Japan on movements of capital registered as FDI in the balance of payments. In some cases, figures from this second source have been estimated from the data available, following the method described in the Statistical Annex to this book.

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Latin America and the Caribbean in Comparison to Other Developing Regions

In the early 1970s, in a period of expanding total Japanese FDI flows, Latin America and the Caribbean (along with Asia) was one of the main recipient regions for Japanese capital (see Table 1). Many of these investments were intended to consolidate or expand the presence of Japanese companies in manufacturing industry in the host countries, many of which were following import substitution strategies. Alternatively, other investments were made in order to take advantage of the region's abundant supply of natural resources. However, with the onset of the foreign debt crisis and economic stagnation, investment in the region entered into a slump from which it would only emerge in the early 1990s. Latin America now attracts very little Japanese FDI, absorbing just under 10% of the total flow in 1996.

In the 1990s, the strongest magnet for most foreign investors was the massive wave of privatization programmes launched by the majority of Latin American governments. However, for a number of reasons these operations attracted relatively little Japanese capital:

- The foreign debt crisis had a negative impact on the way Japanese investors saw Latin America, although some did take advantage of the debt conversion mechanisms offered by Brazil and Mexico.

- Generally speaking, when Japanese manufacturing companies invest abroad they prefer to build new plants rather than acquire existing facilities.

- In some of the privatized sectors, such as energy and telecommunications, Japanese firms were not in a position to compete with their European and US rivals.

- Towards the end of the 1980s and in the early 1990s, direct investments in Asia were more profitable than those in other developing regions.

At the same time, the strength of the yen, and the frequent tensions in trade relations between Japan and the United States, Canada and the European Union (EU)[1] forced Japanese firms to relocate part of their operations to these countries, in order to overcome the growing trade barriers and maintain their market shares. Particularly in the automobile and electronics industries, these developments prompted a drop in FDI flows to the developing regions as a whole (see Table 1). This affected Asia less than Latin America, where the subsequent

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recovery was also much slower, as Japanese investors considered that there were fewer opportunities for profit in the region.

Furthermore, the strategy followed by Japanese manufacturing firms in developing countries during the 1980s was based on "efficiency-seeking" FDI. Their objective was to establish efficient foreign production centres which would allow them to export to third countries, as well as to get round the problem of the strong yen and Japan's trade conflicts with western countries. From this perspective, the export-based policies and more prudent debt management in the countries of East and South East Asia made them a more attractive destination than Latin America and the Caribbean.

However, Latin America and the Caribbean's share of total Japanese FDI did not fall significantly in this period (Table 1). This was mainly because of the major investments made in non-manufacturing sectors, such as shipping in Panama (using "flag of convenience") and banks and insurance companies registered in offshore centres (Bermuda, the Cayman Islands, Panama and the Virgin Islands). Although most of these capital flows consisted of portfolio investments, they were classified as FDI. However, for the purpose of this book, which largely excludes investments in offshore centres in the region, Japanese FDI can be said to have fallen during this period.

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Table 1
Japanese FDI in Different Regions
(in millions of US$, percentages, and yen/US$)

Period	Total (millions of US$)	North America (%)	Latin America[1] (%)	Asia (%)	Europe (%)	*Yen*/US$
1970-74	1,998	23	20	26	19	360
1975-79	3,828	27	16	29	9	297
1980-84	7,926	33	19	24	13	227
1985-89	36,493	48	13	12	20	239
1990-94	42,217	46	10	15	21	145
1995	50,694	45	8	24	17	94
1996	49,172	48	9	24	15	109

Source: IRELA-IDB, based on data for notifications registered by the Japanese Ministry of Finance.
1. Including offshore centres.

The fall in Latin America's share of Japanese FDI in manufacturing industry reveals more clearly the shift in the destination of Japanese capital. Investment in manufacturing industry, which had been quite high during the period of import substitution in the region in the 1970s, fell sharply during the second half of the 1980s (see Table 2). Since 1994, however, Japanese investors have been returning to the region, including to manufacturing industry. Although Japan seems to be acting more cautiously than the western investor countries, the emergence of a more positive attitude towards Latin America and the Caribbean among Japanese investors coincides with global investment trends.

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Table 2
Japanese FDI in Manufacturing in Different Regions
(total in millions of US$ and percentage share)

Period	Total (millions of US$)	North America (%)	Latin America[1] (%)	Asia (%)	Europe (%)
1970-74	684	16	30	40	6
1975-79	1,351	20	19	34	7
1980-84	2,236	40	15	29	10
1985-89	8,816	62	3	19	14
1990-94	12,554	41	4	29	21
1995	18,623	39	2	43	11
1996	20,829	44	7	33	14

Source: IRELA-IDB, based on information of notifications registered by the Japanese Ministry of Finance.
1. Including offshore centres.

Recent Trends in Japanese FDI Flows to Latin America and the Caribbean

General trends

Flows of Japanese investment to Latin America began to expand in the mid-1990s, mainly drawn in by so-called "pull factors". The most important of these has been the expansion of local markets in a context of major economic reforms, the opening-up of infrastructure projects to private investment, the participation of foreign capital in privatizations, and the growth of the Latin American markets as a result of the various integration processes being implemented in the region, including the North American Free Trade Agreement (NAFTA) and the Southern Common Market (*Mercado Común del Sur*, MERCOSUR).

Brazil has been the principal beneficiary of this recent upsurge in Japanese FDI, most of which has been concentrated in manufacturing industry. These investments have mainly been made by Japanese companies involved in the assembly and supply of parts and components, particularly in the automobile and electronics industries. These investments have been prompted both by the growth of the different local markets and the overall expansion of the market as a result of the creation of MERCOSUR. Along with these industries, shipbuilding and iron and steel have attracted significant investment, as have financial and insurance services.

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Table 3
Japanese FDI in Latin America and the Caribbean in Selected Years
(in millions of US$)

	1980	1985	1990	1994	1995	1996
Argentina	8.6	4.3	31	-27	86	38
Brazil	113.1	179.5	127	60	256	634
Chile	9.3	30.1	-28	4.7	—	—
Colombia	—	—	59	7.7	—	—
Mexico	539	-223.9	159	518	129	-61
Peru	-33.7	-144.4	-30	—	—	—
Venezuela	7.6	-2.3	69	3.4	21	168
Latin America and the Caribbean	661.5	-161.1	399	567.8	492	780
MERCOSUR	123.8	181.4	158	33	342	673
Offshore centres	36.3	1,251.6	488	1,082.0	370	-680
Total	697.1	1,090.5	887	1,666.9	883	96

Source: IRELA-IDB, on the basis of balance of payments data from the Bank of Japan.

The main reason for the growth in FDI flows to Mexico, particularly in 1994, was the signing of NAFTA. Although the peso crisis caused some difficulties and a temporary decline in the flows, the rapid recovery of the Mexican economy, and the fact that investment in Mexico provides a gateway to the US market will probably ensure that this flow of new investment continues. The principal destination of Japanese FDI in Mexico has been the transport equipment sector. In other countries, such as Venezuela, most Japanese investment has been concentrated in commerce, services, chemical products, and ferrous and non-ferrous metals. As far as primary products are concerned, the agricultural, forestry and fishing industries in both Argentina and Chile have also received Japanese FDI in recent years.

However, the upsurge in Japanese investment is not only a response to the "pull factors" from Latin America and the Caribbean. More recently, a number of domestic "push factors" have also encouraged the flow of Japanese FDI to the region. These include the saturation of the Asian markets, compared with the relative improvement in the performance of Japanese-owned companies in Latin America. As a result, since 1996, Japanese manufacturing companies have sought to diversify their foreign investments. The annual surveys produced by the Export-Import Bank of Japan (JEXIM), which are analyzed in detail below,

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show that this tendency has not only boosted FDI in Latin America but also in the United States and Europe.

Diversification has also been encouraged by the financial and currency crisis which hit Asia towards the end of 1997. The recent currency devaluations in a number of Asian countries, however, will make its exports more competitive and may hence pull Japanese FDI back to the region. On the other hand, with the declining competitiveness of labour-intensive production, some Asian countries are turning to the production of higher added value goods. However, their capacity to attract FDI in the future will depend on their ability to implement this change quickly and successfully; this, in turn, depends on the evolution of the current crisis in the region. Thus, the difficulties these countries are now facing could lead to an increase in Japanese FDI in Latin America.

Table 4
Main Destinations of Japanese FDI in Brazil
(in millions of US$)

	1989	1990	1991	1992	1993	1994
Total manufacturing	135	315	97	178	322	464
Chemical	5	158	0	11	38	2
Ferrous and non-ferrous metals	45	24	22	4	47	215
Electric and electronic	36	26	28	69	6	3
Transport equipment	15	42	18	20	40	215
Commerce	21	18	5	5	6	0
Finance and insurance	133	226	35	84	58	687
Other services	35	11	5	12	3	10
Total	349	615	171	464	419	1,235

Source: IRELA-IDB, based on data on notifications registered by the Japanese Ministry of Finance.

One significant characteristic of both the aggregate and sectoral flows of Japanese FDI to Latin America and the Caribbean is that, rather than consistently rising like the flows to Asia[2], they have fluctuated considerably

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over time. Moreover, very few Japanese companies have invested in the region, compared with the large number of companies operating in Asia (attracted at first by the excellent returns on their investments in large-scale assembly plants).

Table 5
Main Destinations of Japanese FDI in Mexico
(in millions of US$)

	1989	1990	1991	1992	1993	1994
Total manufacturing	21	150	154	53	19	585
Ferrous and non-ferrous metals	8	9	2	9	5	4
Electric and electronic	8	2	1	1	6	31
Transport equipment	1	105	140	17	6	538
Commerce	14	6	13	5	16	0
Other services	0	12	26	0	18	28
Total	36	168	193	60	53	613

Source: IRELA-IDB, based on data on notifications registered by the Japanese Ministry of Finance.

The main reasons for the increase in Japanese investment in Mexico are the economic recovery and Mexico's membership of NAFTA. However, the peso crisis of December 1994 provoked a short-lived but nonetheless sharp drop in Japanese FDI in Mexico. Japanese investment in Brazil has followed a similar pattern. It rose at the end of the 1980s and in the early 1990s, but has also undergone major fluctuations. Equally, in Brazil too, the growing inflows of Japanese capital have not only gone into manufacturing industry. In 1994, for example, over half of all Japanese FDI was in financial services and insurance (Table 4). Although, as in the case of Mexico, regional integration (in MERCOSUR) helps explain the increased flows of Japanese FDI to Brazil, the overriding factor seems to have been the recovery of the Brazilian economy.

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Central America and the Caribbean, in contrast, have attracted much less Japanese FDI than the larger countries such as Argentina, Brazil and Mexico. However, it seems likely that some sectors, such as electronics, will prove more attractive in the future due to the advantages these countries offer in terms of geographic position, the labour force, and local services, particularly given the existence of export incentives (*maquiladoras*).

The Strategy of Japanese Companies in Latin America

According to a survey produced by JEXIM, Japanese companies are once again considering investing in Latin America. The 1992-1994 report shows that the companies consulted considered Mexico to be one the most "promising" countries over the next ten years, although no Latin American country figured among the ten most promising countries in the medium term.[3]

In 1994, Mexico lost its place among the "most promising" countries in the long term, although it returned to the "top ten" in 1996, only to drop to 12th place the following year. In the 1997 report, Brazil was the best placed Latin American country, as well as the seventh in the global long-term ranking, and ninth in terms of its short-term prospects. The growing popularity of Latin American countries is a result both of "pull factors" in the recipient countries and "push factors" affecting Japanese companies. Since 1996, Japanese companies have followed a policy of diversifying the location of their FDI; Latin America is now seen as a region with considerable potential for growth and investment opportunities, whereas Asia is considered to be virtually saturated[4].

Another reason for the diversification of FDI is the relative increase in the profitability of Japanese-owned affiliates outside Asia, and above all in western countries and Latin America (see Table 6). Although this tendency is very recent, the substantial improvement in the performance of Japanese-owned companies in Latin America, especially in 1997, has boosted investors' confidence in the region.

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Table 6
Japanese Manufacturing Companies' Evaluation of Profits of their Affiliates by Region and Country[1]

	NIC[2]	ASEAN[3]	China	Other Asia	USA and Canada	EU	Latin America[4]
1991	3.12	3.15	—	2.81	2.27	2.93	—
1992	3.34	3.19	—	2.97	2.26	2.55	—
1993	3.31	3.15	2.88	2.97	2.26	2.29	2.61
1994	3.04	3.20	2.83	2.97	2.46	2.35	2.65
1995	3.24	3.15	2.75	2.63	2.72	2.52	2.91
1996	3.24	3.20	2.55	—	2.88	2.81	2.89
1997	3.31	3.21	2.65	—	3.07	2.99	3.16

Source: *Export-Import Bank of Japan*
1 Ranking from 1 to 5, in which 1 = poor and 5 = excellent.
2 Newly-industrialized Countries.
3 Association of South East Asian Nations.
4 Latin America and the Caribbean

In contrast to the trend in the 1980s, the flow of FDI from Japanese manufacturing companies in the 1990s has responded more sensitively and less abruptly to the changing levels of return on their investments. However, there has been a clear increase in the flows to the countries where the best results were obtained, at the expense of those showing poorer results. Japanese firms are now attempting to implement a more finely-tuned "globalization strategy"; with profit levels rising again in Latin America as a result of the greater macroeconomic stability and market liberalization, the region seems more attractive to Japanese investors. In short, the recent strategies adopted by Japanese manufacturers in Latin America are the result of a combination of improved economic results in the region, the performance of their affiliates there, and the globalization strategies[5] implemented by Japanese TNCs.

Latin America and the Caribbean in the Global Production of Japanese TNCs

The Japanese-owned affiliates in Latin America and the Caribbean account for only 3% of their parent companies' total sales, and in terms of the regional distribution of sales, the region only makes a larger contribution than the Middle

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East and Africa. Some two-thirds of the total volume of sales of the Japanese affiliates in the region are in non-manufacturing sectors. This is a very similar proportion to that for the United States, but it contrasts sharply with the figures for Asia, where manufacturing industry accounts for over half the total value of sales of Japanese affiliates.

In terms of the value of sales, the most important manufacturing sector is the transport equipment industry, followed by electronics and chemicals. The transport equipment industry is also the leading sector in the United States and Oceania, whereas in Europe and Asia the electronics industry ranks first. This may be related to the nature of production in Latin America, which is generally geared towards local markets. For reasons of costs, the transport equipment industry tends to supply local markets, whereas the electronics industry is more export-oriented.

This is certainly the case in Latin America and the Caribbean, where Japanese subsidiaries have tended to produce for local markets, generally only exporting to neighbouring countries. More recently, however, these affiliates have gradually become more export-oriented. In this respect, they are imitating their counterparts in Asia, which manufacture products for export both to Japan and third countries, particularly in the West. Nonetheless, 74.8% of the sales of Japanese affiliates in Latin America and the Caribbean are made in their respective national markets or neighbouring countries, 21% in the United States and Canada, and only 4% in Japan and other Asian countries. These figures contrast with the sales of Asian-based Japanese affiliates, only 5% of which go to western countries, and 22% to the Japanese market (see Table 7).

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Table 7
Destination of Sales of Japanese Affiliates by Region, 1997
(in percentages)

Subsidiaries in:	Export market:			
	Local market	USA/ Canada	Japan	EU
Latin America	74.8	20.5	3.9	0.6
NICs	61.4	4.7	16.7	2.4
ASEAN	60.8	3.0	22.2	1.9
China	60.6	3.0	25.9	1.1

Source: Export-Import Bank of Japan.

Incentives for Japanese Investment in Latin America and the Caribbean

Although the factors behind Japanese FDI flows in Latin America and the Caribbean are similar to those operating in Asia, the processes of regional integration appear to have had a greater influence in the case of the former. According to the JEXIM surveys, Japanese TNCs show more interest in regional integration in Latin America (10.7%) than in ASEAN (2.1%).

According to the results of this survey, the most common motives for Japanese FDI in Latin America are:

- the desire to maintain or increase market shares in the recipient countries;

- the consolidation of "export bases", which are common in main producing regions of the world, and are becoming increasingly important in Latin America (particularly in the case of Mexico, "export bases" in Latin America may help boost sales to the United States, as well as to other countries in the region, such as Brazil and Argentina); and

- the production of parts by local suppliers. This is a global trend among Japanese investors, which has been visible in Latin America since 1994. While this process is expanding in Latin America and other western countries, it is declining in the ASEAN countries and China, possibly due to the depreciation of the yen since 1995.

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Table 8
Motives for Japanese FDI in Latin American and ASEAN
(percentage of respondents identifying each motive)

A. Latin America

Motives	1990	1991	1992	1993	1994	1995	1996	1997
A	66.7	60.9	36.7	55.2	42.5	60	47.6	55.4
B	8.3	17.4	16.7	20.7	32.5	44.4	45.2	42.9
C	0	0	3.3	3.5	2.5	8.9	4.8	8.9
D	8.3	8.7	13.3	17.2	7.5	28.9	23.8	26.8
E	16.7	0	3.3	6.9	5	8.9	7.1	1.8
F	8.3	8.7	3.3	3.5	2.5	2.2	2.4	3.6
G	4.7	21.7	6.7	10.3	5	24.4	26.2	23.2
H	41.7	4.3	10	13.8	12.5	20	14.3	16.1
I	8.3	8.7	3.3	3.5	12.5	20	21.4	23.2
J	8.3	0	13.3	3.5	5	2.2	7.1	12.5
K	0	4.3	3.3	0	0	0	0	1.8
L	0	4.3	0	0	7.5	13.3	7.1	7.1
M	8.3	4.3	0	0	2.5	4.4	11.9	3.6
N	—	—	—	—	—	—	—	10.7

B. ASEAN

Motives	1990	1991	1992	1993	1994	1995	1996	1997
A	39.8	47.8	46.4	50.5	54.8	64.7	63.6	65.7
B	19.5	12.2	15.5	20	13.5	31.5	32.7	37.1
C	17.7	8.7	10.3	21	23.2	36	25.3	25
D	13.3	16.5	12.4	32.4	23.9	42.6	38.3	45
E	0.9	2.6	3.1	1	1.3	1.5	1.2	1.4
F	9.7	12.2	16.5	7.6	7.1	5.6	4.9	6.4
G	31.9	23.5	18.6	20	22.6	31	37	35.7
H	38.1	27.8	27.8	20	20.6	40.1	36.4	30
I	4.4	6.1	8.2	17.1	17.4	32.5	24.1	20.7
J	6.2	12.2	9.3	1	4.5	5.1	3.7	6.4
K	0.9	4.3	5.2	1.9	1.3	3	3.1	1.4
L	2.7	0.9	4.1	10.5	9.7	21.8	8.6	16.4
M	2.7	3.5	2.1	2.9	3.9	6.6	8.6	10.7
N	—	—	—	—	—	—	—	2.1

Source: Export-Import Bank of Japan

A: Market protection/expansion; B: development of new market; C: export to Japan; D: export to a third country; E: response to tariff or other trade regulations in the host country; F: international division of the production process; G: international division of products; H: obtain cheap labour; I: supply parts to local producers; J: guarantee inputs or natural resources; K: respond to request by host country; L: avoid exchange rate risks; M: develop products adapted to the local market; N: interest in regional integration.

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Most Japanese FDI flows to Latin America are absorbed by Brazil and Mexico, for very similar reasons to those which explain the pattern of Japanese investment in Asia. In the case of Brazil, since 1995 investment by Japanese companies has increasingly responded to the need to maintain and expand their market shares, as well as the desire to supply parts to local assembly plants. In 1997, regional integration also figured as a major causal factor for Japanese FDI. In contrast, the objective of exporting to Japan or third countries has been a less important motive for Japanese investment in Brazil than in the case of the Asian countries. In any event, the main attraction that Brazil holds for Japanese investors is its huge national market, followed in second place by the availability of cheap labour.

The principal attractions of Mexico as a destination for Japanese FDI are very different to those of Brazil. In the case of Mexico, the most important factors are the desire to take advantage of cheap labour and to establish a base for exporting to third countries. Since 1995, however, the goal of exporting has become less important, possibly because so much of Mexico's production is already geared towards the US market. The latest survey carried out by JEXIM shows that, apart from Brazil and Mexico, only two other Latin American countries were seen as likely recipients of Japanese FDI: Argentina ranked 33rd and Peru 40th in the list of the most popular countries. This apparent lack of interest in investing in Latin America is explained by a number of factors which were highlighted in the 1997 survey:

- the region's productive capacity is already sufficient to meet current demand;
- the profitability of Japanese affiliates in Latin America is not sufficient to encourage further investment by their parent companies; and
- the prospects offered by the business environment are too uncertain to warrant the creation of new companies.

This image, however, seems to reflect the situation existing in the past, as conditions in the region have changed significantly over the last few years. As a result, it is probable that the negative image reflected in this survey will gradually change, as Japanese investors become increasingly aware of the growing profitability of Japanese affiliates in Latin America, and the new stability and potential for growth in the region.

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The JEXIM survey also identified a series of more structural obstacles to increased Japanese FDI in the region. In the case of both Brazil and Mexico, these include the lack of suitable infrastructure, of local middle managers and engineers, and the difficulties encountered in obtaining high quality parts and some raw materials. The legal system is also seen as a major disincentive in Brazil, whereas Mexico is thought to suffer from a shortage of skilled labour. Macroeconomic stability alone, therefore, is not enough to ensure larger inflows of Japanese FDI. Rather, improvements must be made in the economic, social and legal infrastructure, as well as the region's education systems.

NAFTA and MERCOSUR: Magnets for Japanese Investors?

According to the 1997 JEXIM survey, regional integration constitutes a major stimulus for Japanese investment in Latin America. However, contradictions arise when the attraction of specific destinations is studied, for this suggests that regional integration is not considered to be a fundamental cause of the investments made by Japanese companies in Brazil and Mexico.

This is understandable in the case of Brazil, bearing in mind the size of the Brazilian domestic market within MERCOSUR. Nonetheless, it is more surprising in the case of Mexico, given its importance as a base for the export of labour-intensive products to the United States. Yet none of the respondents to the JEXIM survey (companies involved in the manufacture or assembly of electronic components or the production of automobile parts) considered that regional integration had a decisive influence on their decision to invest in Brazil or Mexico in the next three years.

These responses, however, appear to contradict the trends identified here. As can be seen in Table 7, 20.5% of all sales by Japanese affiliates in Latin America were made to the United States and Canada. The Japanese car companies as well as the three leading US manufacturing firms with affiliates in Mexico (General Motors (GM), Chrysler and Ford) have increased their exports to the United States, which have more than offset the slump in demand in the Mexican market following the 1994 peso crisis. This shift clearly indicates a change in the global strategies of these companies. Moreover, a number of Japanese electronics companies have relocated their plants from the United States to Mexico, a tendency which seems to confirm that Mexico offers a more effective base (particularly in terms of costs) from which to exploit the economic area created by NAFTA.

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On the other hand, although the 1997 JEXIM survey suggests there has been very little response to the regional integration processes in the Southern Cone, some Japanese firms are investing in Brazil and Argentina in anticipation of the growth of the MERCOSUR markets. Moreover, while many Japanese companies still have considerable doubts about the prospects for MERCOSUR, a number of telecommunications companies are considering expanding their operations there in order to meet the demands created by this integration process.

The Role of Small and Medium-Sized Japanese Companies

FDI by Japanese component suppliers in Latin America and the Caribbean has increased and will surely continue to do so, just as it will in other regions of the world. This type of investment is intended to exploit the particular "ownership advantages" of the Japanese automobile and electronics industries, whose production is generally characterized by the assembly of a large number of parts and components. Faced with the choice of producing in Japan and exporting, or directly producing abroad, Japanese companies have traditionally opted for the first alternative for reasons that are closely linked to their relations with local suppliers. Production inside Japan has two main advantages for assembly companies: the high quality and low cost of production, and the existence of very sophisticated assembly procedures, such as the "just-in-time" systems.

In principle, at least, with the appropriate processes of technological transfers and training, these conditions could be reproduced abroad. However, a number of other factors, essentially related to manufacturing companies, are also influential in the decision of TNCs to engage in FDI. These involve the differences between Japan and other countries in terms of relations with both employees and suppliers.

Generally speaking, these firms have to decide what proportion of the parts they require will be produced in-house (internalization) and what proportion they will purchase from suppliers. This decision depends on their assessment, on the one hand, of the transaction costs (generated when these operations are carried out through the market), and on the other, of the internalization costs (which are related to the overheads involved in producing the parts in-house). The greater the level of internalization, the lower the transaction costs. Hence, the transaction costs curve depends, among other things, on the nature of the company's relations with its suppliers and the characteristics of the market in which it operates. On the other hand, the internalization costs curve is

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influenced, among other things, by the nature of a company's labour relations.

Given the particular character of Japanese management systems, which are based on long-term employment contracts, marginal costs of internalization grow at an increasing rate as the proportion of internally-produced components and parts rises (that is, the curve is convex). Likewise, since relations with suppliers in Japan are also established on a long-term basis, marginal transaction costs decrease at an increasing rate as the level of internalization rises (this curve is also convex). This occurs because suppliers have long-term relations with their client, so they are very sensitive to the bargaining power gained by the assembly company when it increases its internal production of components. As a result, when an assembly company internalizes more production, it can obtain better conditions from its suppliers. Given the form of these two curves, the optimum level of internalization is at an intermediate position, whereby some processes are internalized while others are performed though long-term commercial relations with suppliers.

In contrast, in western countries both industrial relations and relations with suppliers are usually short-term oriented. Given the competitive labour market, internalization costs rise at a decreasing rate (that is, the curve is concave). On the other hand, since suppliers generally do not enter into long-term relations with the assembly firm, they are less sensitive to the greater bargaining power acquired by the assembly company as it increases internal production of components. In fact, a company's bargaining power with respect to suppliers drops as the volume of acquisitions in the market decreases. As a result, in theory at least, the optimum decision lies at one or other of the extremes: either to produce all components and parts internally, or to buy them all in the market place, with the company merely assembling them. The final decision depends on the relation between the internalization costs in the first case (with zero transaction costs) and the transaction costs in the second case (with zero internalization costs).

In either case, the total costs (all other factors being equal) of producing in Japan are lower than in the West. Hence, the specific advantages of Japanese firms (their "ownership advantages") are largely derived from the Japanese system of long-term relations with both suppliers and employees. As a result, since the early 1980s, Japanese companies have based their strategies of market penetration on the export of finished products rather than producing them locally in foreign markets where these conditions do not exist.

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However, the constant pressure exerted by the rising value of the yen, and the trade conflicts with western industrialized countries, have modified the strategy of Japanese companies by creating incentives to invest abroad. In response, they have established networks of hybrid international operations, which are quite different from the traditional Japanese systems of production. These operations make use of management techniques tailored to the host countries, while trying to change the attitude of local suppliers towards long-term relations. Japanese automobile companies have had some success in this respect in the United States, thanks to the creation of supplier "support centres". The TNCs have also encouraged their Japanese suppliers to follow them abroad. The growth in investment by medium-sized suppliers of parts and components in Latin America and the Caribbean is linked to this process, and can be expected to intensify in the future, as these suppliers follow the larger firms[6].

The Impact of Investments on Recipient Countries

In light of the characteristics of Japanese FDI outlined above, it is possible to draw some conclusions about the possible effect of these capital inflows on the recipient countries in Latin America and the Caribbean. Since one of the objectives of Japanese FDI is to establish international or inter-regional integrated systems of production incorporating suppliers and assembly companies (particularly in the automobile and electronics industries), one clear positive effect is technological transfers. Within this strategy, in addition to the FDI by small and medium-sized Japanese suppliers, effective use must also be made of local suppliers if the maximum benefit is to be gained from internationalization. Cooperation within these production networks is therefore mutually beneficial for the Japanese TNCs and the recipient countries.

If this type of production system is to be effective and profitable, relations between the local suppliers of parts and components and the Japanese assembly firms must be founded on trust and cooperation, and operate on a long-term basis. This, of course, does not rule out competition among local suppliers, which is in fact encouraged by the Japanese companies. They see this blend of cooperation and competition as the best way of maintaining efficient relations with their suppliers, and ensuring the availability of high quality parts and components at competitive prices.

One basic feature of Japanese-owned companies is that they "learn from experience" at all levels. This is not only true of their research and development (R&D) activities, but also of the production process itself. Generally speaking,

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Japanese companies do not use formal manuals when deciding on the best way to develop, since they believe that all procedures can be improved through experience. During the initial phases of their operations they rely on specialized Japanese workers, who are familiar with the working methods of these companies, and are therefore able to transfer Japanese know-how to the local companies. As the Japanese experience in Asia shows, this approach offers numerous opportunities to develop the skills and capacity of local companies, to increase exports from the countries in which they are based, and to promote the economic growth of these countries.

Conclusion

The recent expansion of Japanese FDI flows to Latin America and the Caribbean is a consequence of the brighter economic prospects for the recipient countries. This tendency should be further encouraged by the ongoing process of inter-regional integration. The main purposes of Japanese investments in Latin America are similar to those of investments in Asia. They are intended to give investor companies a foothold in local markets, as well as to reproduce each company's ownership advantages by constructing efficient international or regional production networks. This model of organization, based on the creation of a complementary relationship between Japanese investors and companies in the recipient countries, favours the development of local companies, their export capacity, and their potential for future expansion.

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Box 1: Other Asian Investments in Latin America and the Caribbean

Latin America and the Caribbean are less important destinations for FDI from other Asian countries, including the Republic of Korea and Taiwan. The distribution of these countries' FDI in the region is very similar to that of Japan, in that it is concentrated in the offshore banking centres (Panama and the Virgin Islands). In terms of productive investment, during the first half of the 1990s most capital was absorbed by Mexico (where companies from India, the Republic of Korea and Taiwan were particularly prominent). Mexico's appeal seems to be based on the expansion of the local market following the implementation of NAFTA. There is also some evidence that state-owned Chinese companies have been carrying out a programme of acquisitions both in Mexico and Peru since 1992.

In the future, Asian firms may follow the example of their Japanese counterparts and increase their FDI in Brazil in order to seize the opportunities created by the consolidation of MERCOSUR. As a result, the Asian-owned affiliates in NAFTA and MERCOSUR countries may set up regional production networks with local, western and Japanese companies in the area, and as such, form part of the international networks of Japanese TNCs.

Korean investment

Although the flows of Korean FDI to Latin America and Caribbean account for only a small proportion of total Korean investment, they have expanded substantially since the mid-1980s. This growth reflects both internal and global developments, such as the liberalization processes in the region, the appreciation of the won, rising domestic interest rates, trade conflicts with western industrialized countries, and the global tendency towards regional integration. Towards the end of 1996, South Korean FDI totalled $13.7 billion, a massive increase from the $500 million invested in 1985 (including offshore centres, Bank of Korea). Nonetheless, following the financial crisis in Asia, Korea has seen a major reduction in its sources of external financing, as well as a sharp fall in the value of the won. Although the consequences of the crisis are still not clear, Korean FDI flows will almost certainly be affected.

South Korean investment in Latin America took off in 1995, when it rose by 495% compared to 1994, and continued to grow the following year, with a 121% increase that took it to $219 million. By the end of 1996, Korean companies had 268 investment projects in the region, worth around $560 million, or some 4% of their total foreign investment. The bulk of this capital (59%) was invested in manufacturing industry (net figures, Bank of Korea). It should also be emphasized that the South Korean statistics do not include investments made through Korean-owned subsidiaries in other countries, such as Samsung in the United States.

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The main recipients of Korean FDI in the region are Argentina, Brazil, Chile, and above all Mexico. Investment in Mexico boomed in 1994 following the signing of NAFTA. Two of the largest Korean investors are Daewoo and the textile company Kohap Co. Approximately 70% of all Korean production in Mexico is destined for export, and only 30% for the local market. Along with their counterparts from Japan, Korean companies have spearheaded the recent wave of Asian investment in Brazil. Here, LG Electronics is constructing a $1.2 billion plant to produce television screens and tubes, while the automobile companies Hyundai, Kia Motors and Asia Motors are investing some $3 billion in assembly plants in various parts of the country.

NOTES

[1] The most precise data on Japanese investment flows are contained in the "Regional Balance of Payments Summary" published by the Bank of Japan (BJ) in its *Monthly Review of the Balance of Payments Statistics*. However, since these statistics only explicitly refer to two Latin American countries (Brazil and Mexico), the geographical breakdown of investment in the region has been calculated on the basis of the adjusted data from the Japanese Ministry of Finance. These figures have also been used to estimate the main trends in Japanese FDI in the different economic sectors in Latin America.

[2] There were also small fluctuations in Japanese FDI to all Asian countries. However, the long-term trend for most countries was upwards.

[3] "Short term popularity" reflects that companies have investment plans in the short term, while "long term popularity" means that the companies believe that prospects are good but have no specific investment plans

[4] Another option for making new investments is to expand domestic or internal investment. In fact, domestic investment in Japan did increase significantly in 1996 and 1997, boosted by the weaker yen.

[5] «Globalization strategy» signifies a strategy intended to establish a productive base, sales, purchase of parts, finance, engineering and research and development on a global basis. This is achieved through trade, international investment, licensing agreements, and strategic alliances.

[6] The transaction costs Japanese parent firms face when exporting end products differ from those in the components market. However, for simplicity's sake, here it is assumed that the nature of the transaction costs are the same in both cases

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CHAPTER IV

SPAIN*

Introduction

The comparatively late onset of industrialization in Spain, which only began in earnest in the 1960s, also determined that Spain lagged behind other more advanced economies in terms of foreign direct investment (FDI). In practice, Spanish foreign investment only acquired any real significance after Spain joined the European Economic Community (EEC) in 1986. Although the number of companies involved is still small, the level of Spanish FDI has risen considerably in the 1990s. Spain is currently in an intermediate phase in the "development path" of foreign investment, whereby the wide gap that has traditionally existed between the high level of inflows of FDI into Spain and the very small Spanish outflows of FDI is now beginning to shrink.[1]

This chapter briefly examines the evolution of Spanish FDI over the last three decades, before analyzing in greater detail some of the main characteristics of the flows of Spanish investment to Latin America in the 1990s. The analysis has two main goals: first, to identify the geographic and sectoral distribution and scale of Spanish investment in Latin America, and compare them with the pattern of Spain's investment in other areas and countries; and second to outline the strategies followed by the Spanish investor companies and the factors that determine their FDI operations in the region. Accordingly, the first part of this chapter offers a brief history of Spanish foreign investment from the 1960s to the end of the 1980s, while the second part provides a more detailed analysis of Spanish FDI in Latin America in the 1990s.

The analysis of the geographic and sectoral breakdown of Spanish FDI is based on statistical data compiled by the General Directorate for International Economics and Foreign Transactions (*Dirección General de Economía Internacional y Transacciones Exteriores*, DGEITE) of the Spanish Ministry of Economy and Finance. These figures refer to investment projects presented for

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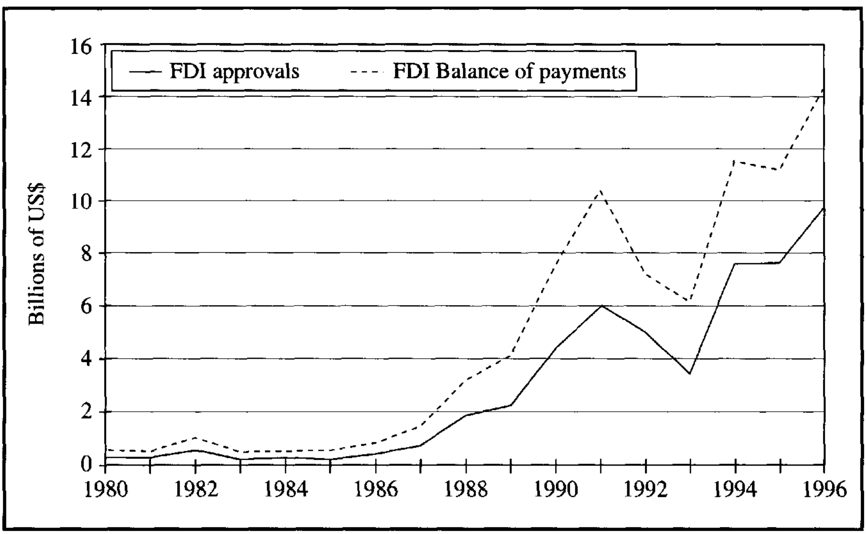
approval which have a period of six months to be made effective, but may never actually be realized. As a result, this data differs from the balance of payments figures prepared by the Bank of Spain, which are based on figures for the effective movements of capital defined as direct investments provided by the different banks for the Register of Accounts (see Graph 1). In their favour, the DGEITE figures also include: investments made by banks against their currency holdings abroad (which represent considerable amounts, and have been included in the approval figures since 1992), as well as international receipt and payment settlements, a mechanism often used to realize investments. The analysis of the breakdown of flows by sector of origin and destination, which only refers to data on approved investments, is based on the figures compiled by the DGEITE. In contrast, in some sections of the chapter the analysis of aggregate flows of FDI also incorporates the figures produced by the Bank of Spain.

Graph 1
Total Spanish FDI Authorized and Registered in the Balance of Payments



Sources: Compiled by the author from Bank of Spain data, and various issues of the *Boletín de Información Comercial Española* (BICE) produced by the DGEITE, Ministry of Economy and Finance of Spain.

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Historical Background

The structural transformation of the Spanish economy during the 1960s and early 1970s dramatically reshaped the country's productive system. This process gave rise to a highly structured productive fabric, which in turn created the domestic conditions necessary for Spanish companies to embark on programmes of foreign investment. Until 1973, in the expansive phase of this process, there was relatively little FDI (amounting to an accumulated total stock of $247 million). Most of this investment was concentrated in financial and commercial services related to exports, and in the exploitation of raw materials required by the Spanish market. Some manufacturing companies also invested abroad, albeit on a rather modest scale.

In terms of the destination of Spanish FDI, 35% went to EEC countries, 29% to Latin America,[2] 16% to members of the European Free Trade Association (EFTA), and a mere 6% to the United States. Although large companies were responsible for the most substantial investments, numerous small and medium-sized enterprises (SMEs) were also active in the region. In most cases, the companies investing abroad acquired complete control of their investments; in just over half the cases, Spanish companies acquired stakes of more than 50% in the capital of the foreign company.

Spanish FDI expanded considerably after 1974; the total flow of investment during the second half of the 1970s was four times higher than during the preceding period. Latin America and the Caribbean attracted much of this expanded flow of Spanish investment,[3] absorbing more than half the total flows, while the relative shares of the EEC and the United States remained unchanged. This shift in the destination of Spanish investment reflected a change in its nature and purpose. The main objective of investments in the EEC and the United States was to develop commercial networks to secure new markets and increase exports and, in the case of financial institutions, to consolidate their position in the main international markets. In contrast, the investments in Latin America were primarily intended to exploit the technological and organizational advantages of the investing companies, by producing in markets with high protective tariffs, good prospects for growth, advantageous relative costs and abundant supplies of raw materials.

The different purposes of investments in these regions were inevitable, given the sectoral distribution of Spanish FDI flows. Almost three-quarters of all investments in the EEC and the United States were made in the financial and

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commercial sectors, while in Latin America the largest share went to manufacturing industry (especially in Mexico, Venezuela, Argentina, Brazil and Chile), followed by financial services (above all in Panama and Puerto Rico, which offered access to the United States). In third place came the primary sector (in Argentina and Mexico), followed by investment in commercial activities (in Mexico, Venezuela, Brazil and Chile).

This period saw a decline in the previously important role of SMEs, as the large companies consolidated their position as the main investors. Foremost among these were Spanish banking groups. Accounting for a quarter of all Spanish FDI, these Spanish banks sought to consolidate their presence in other markets as part of a strategy of overseas expansion. This process also involved some medium-sized banks, with the result that Spanish financial institutions as a whole had a much stronger presence in Latin America (in terms of the number of subsidiaries, branches and delegations) than their counterparts from other industrialized countries.

The introduction of a new, more liberal regulatory framework at the end of 1979 fuelled expectations of a further rise in Spanish FDI. Although Aguilar (1985) has suggested that this was not the decisive factor, Spanish investment did continue to grow over the next few years. This was explained by the support the Spanish government gave to exports, as well as the upsurge in investment in the financial sector, notably in the form of the acquisition of banks in Chile, Puerto Rico and Uruguay, and flows to offshore centres such as Panama and the Netherlands Antilles. As a result, the sectoral and geographic distribution of Spanish FDI that had appeared in the 1960s was further consolidated. Latin America and the Caribbean absorbed 60% of Spanish FDI in this period, the EEC's share fell, while that of the United States rose.

The debt crisis in 1982 seriously weakened Latin America's ability to attract FDI and resulted in a major process of disinvestment in the region. Between 1982 and 1986, the year that Spain joined the EEC (now the European Union, EU) the proportion of Spanish FDI going to Latin America slumped from around 50% of the total to just 21%. In the same period, the EU Member States absorbed 30% of Spanish investment, while the United States maintained its 15% share.

Some 60% of investment flows during this period were destined for financial institutions and services. However, a new phenomenon appeared in the form of financial operations by non-financial companies. Not only was there an

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expansion of financial activities abroad, but new groups and holdings were created by Spain's largest companies. These new forms of Spanish business activity abroad were a response to the new demands and opportunities existing in the international markets. Over half of all Spanish investments in Latin America in this period were made in the financial sector, which was followed in importance by metallurgy and precision machinery, food, beverages and tobacco, and the mining of non-metallic minerals. In contrast, very few investments were made in commercial activities, reflecting the economic difficulties facing the countries in the region.[4]

Spain's entry into the EEC in 1986 marked the beginning of a new phase of foreign investment. Between 1986 and 1990, total Spanish FDI rose to an annual average of $2 billion, significantly up on the figure for the first half of the decade. Just over half the total investment in this new period went to EU Member States, reflecting the opportunities and challenges presented by the European integration process. The United States followed in second place, absorbing some 10% of the total. In absolute terms, Latin America (excluding Panama and the offshore centres in the Caribbean) received more Spanish FDI than during the first half of the decade, but in relative terms the region's share dropped to 10%. Almost 65% of all Spanish FDI in this period was in financial activities and services, followed a long way behind by commercial activities and the exploitation of non-energy minerals.

Two different groups of countries can be identified in terms of Spanish investment in Latin America and the Caribbean (excluding Panama and the offshore centres in the Caribbean). The first accounted for some 80% of all flows of Spanish FDI to Latin America and consisted of Chile (20%), Argentina (20%), Puerto Rico (17%), Mexico (13%) and Brazil (10%). All the investment in Puerto Rico was in the financial sector, which also absorbed 75% of the total flows to Chile, and over 50% of those to Argentina, where the rest was mainly destined for the non-metallic mineral and fishing industries. In the case of Mexico, restrictions on foreign investment in the banking sector meant that 30% of all Spanish FDI was absorbed by commercial activities, while another 50% was divided between metallurgy and insurance. More than half the total flows to Brazil were concentrated in financial activities, followed by the food, beverages and tobacco sector (which accounted for around a third of the total). The second group of countries –Venezuela, Uruguay, Cuba, the Dominican Republic and Colombia– absorbed 16% of Spanish FDI in the region. The sectoral distribution of the investments in these countries varied in accordance with the character of their economies.

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The single most important category of Spanish investors were banks investing in credit institutions.[5] The scale of their operations was such that their foreign investments came to represent almost 60% of their total assets. Until 1990, the importance of this type of investment reflected the overseas expansion of Spanish banks, which was concentrated on a small group of countries.[6] Another important category of investors consisted of companies seeking to consolidate and expand their commercial activities by creating distribution networks for their products, or to ensure supplies of raw materials. Most of these companies tended to invest in the sector in which they operated, and in which they enjoyed comparative advantages. A third category of investors consisted of insurance companies, which also tended to realize operations within their own sector.

These three sectors absorbed at least 75% of all flows of Spanish FDI to Latin America. Other significant destinations for investment included the exploitation and processing of non-metallic minerals (above all in the cement industry), the energy sector (especially oil and gas) and, from 1990 (when Telefónica and Iberia began to expand in the region) communications and transport. All these companies tended to acquire a majority stake of the local companies. In fact, expansion was largely achieved through rights issues in companies in which the Spanish firm already had a stake or, albeit to a lesser extent, through acquisitions. In contrast, there was relatively little greenfield investment. The predominance of operations involving rights' issues was to a large extent explained by the prominent role played by financial institutions. These require major injections of capital to open subsidiaries and branches and meet the risk requirements set by the banking authorities in the recipient countries.

Spanish FDI in the 1990s

The growth in investment which followed Spain's entry into the EU peaked in 1991. Over the next two years, the slower growth in the EU had a negative impact on Spanish investment in the region. However, 1993 saw the beginning of a new period of expansion (see Graphs 1 and 2). According to the figures recorded in the balance of payments by the Bank of Spain, Spanish FDI flows to Latin America and the Caribbean (excluding the Caribbean offshore centres and Panama) increased from an annual average of $128 million in the 1980s to $765 million between 1990 and 1996, when it reached almost $1.6 billion. When Panama and the Caribbean offshore centres are included, the average annual

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flow in the period 1990-96 increases to $959 million, and the figure for 1996 to almost $2.2 billion.

Between 1991 and 1993, the EU was still the largest single destination for Spanish FDI, attracting some 60% of the total.[7] In second place came Latin America with 12% of the total flows.[8] A similar proportion went to Panama and the Caribbean offshore centres, although in this case it should be remembered that the final destinations of many of these investments were other countries in the region. This was the case, for example, for the $549 million invested by Telefónica Internacional de España in the British Virgin Islands, which was in fact destined for Chile and Argentina. At the same time, the United States accounted for just 6% of all Spanish FDI.

In 1994-96, Spanish FDI flows grew by 63% compared to the first three years of the decade (1991-93), and 148% in comparison to the period 1986-90. This upsurge in investment reflects the growing pull of the opportunities existing in the main Latin American economies. Although Spanish investment in EU Member States has increased in absolute terms, in relative terms it dropped from 60% of the total following Spain's entry in 1986, to 33% in 1994-96. In contrast, Latin America's share of total flows rose to 40%, Panama and the Caribbean offshore centres increased their relative share to 18%, while that of the United States fell slightly to 5%. Within Latin America (excluding Panama and the Caribbean offshore centres), just eight countries absorbed 97% of all Spanish FDI flows: Argentina accounted for some 33% of the total, Peru 28%, Chile 9%, Puerto Rico 8%, Mexico 6%, Brazil 5%, and Venezuela and Colombia 4% each.

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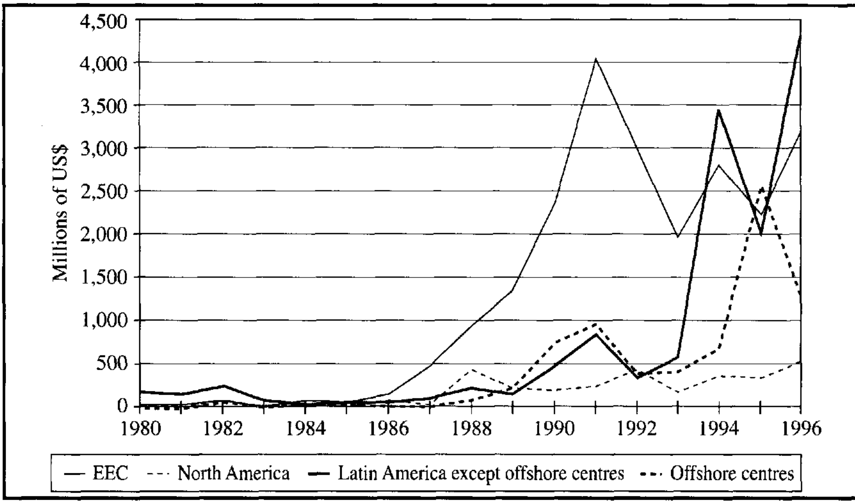
Graph 2
Spanish FDI by Region, 1980-96



Source: Compiled by the author from data in the *Boletín de Información Comercial Española* (various years), published by the DGEITE.

Holding companies: an indirect channel for Spanish investment

Holding companies play an increasingly important role as channels for Spanish FDI in the principal recipient regions. Flows of capital into holding companies are redirected in the second stage of the operation into investment projects in other sectors which constitute their final destination. Now, as in the past, since Spanish companies tend to invest in their core business, the differences (in the figures of approved investments) between the sectors of origin and destination are explained by the involvement of holding companies. In this case, in the second stage of the operation, which is not recorded, investments are made in similar sectors to those of the company's existing activity. This type of operation, involving an intermediate phase, is carried out for tax reasons.[9] It is in order to benefit from tax savings that large Spanish corporations in all sectors usually structure their overseas network through a share holding company. Hence the growing investment in holding companies reflects the international reorganization of corporate groups which use these holdings to

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channel their investments throughout the world, and above all to Latin America and the EU.[10]

In Latin America (excluding Panama and the Caribbean offshore centres), some 28% of Spanish FDI in holding companies during this period came from the transport and communications sectors, 19% from financial institutions, 14% from manufacturing industry, smaller proportions from companies in the oil sector, food, beverages and tobacco production, the paper and printing industry, and commerce, while 25% came from the share holding companies themselves. Yet in the EU countries, investments in holding companies accounted for just over half the total, thereby producing a significant distortion in the sectoral analysis. Just under one third of these investments came from the financial intermediaries, 12% from commerce, 10% from manufacturing industry, and 21% from holding companies. The distortion is even greater in the case of the United States, where 61% of flows go into the holding companies.

Once the sectors of origin of investments in holding companies have been identified, it is possible to indicate the probable character and composition of the flows. The most noteworthy common feature is the importance of financial intermediaries and insurance both in those areas which have traditionally attracted considerable Spanish investment (the EU, Latin America, Panama and the Caribbean offshore centres, and the United States), as well as in the Middle East and Asia. Some 75% of the investment in financial activities went to the EU and Latin America, while another 17% of the total in this sector went to Panama and the Caribbean offshore centres.

Latin America is a major focus for Spanish investment in the transport and communications industries, so much so that Latin America absorbs over 88% of all Spanish investment in these sectors. This is explained by the fact that the countries in the region have been, and still are, at the centre of the international expansion strategy of the two leading Spanish companies in the sector (Telefónica and Iberia). The privatization processes implemented in many Latin American countries have exerted a strong pull on foreign investors everywhere. Spanish companies have shown a particularly strong interest in these privatization programmes, attracted both by the conditions of entry, the anticipated medium- and long-term profitability of investments, as well as their own technological and organizational capacity in these sectors.

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Box 1: Spanish Banks in Latin America

Between 1990 and 1997, Spanish banks invested over \$6.5 billion in Latin America. A leading role was played by a small number of institutions, the Banco Santander with \$3.4 billion, Banco Bilbao Vizcaya (BBV) with \$2.2 billion, and Banco Central Hispano (BCH) with \$500 million. These banks have adopted different strategies according to the barriers to entry, the national legislation in the different recipient countries, and their broader corporate strategies:

- The approach followed by Banco Santander has been to acquire controlling stakes in existing institutions, and establish Spanish ownership and management control. This strategy has been successfully applied in numerous countries in the region. In Argentina, Banco Santander acquired 35% of Banco del Río de la Plata (\$594 million, merging it with Santander Argentina), thereby becoming the largest Argentine commercial bank, with assets of \$10 billion. Banco Santander also acquired 55% of Banco Bancoquia (\$13.6 million) in Colombia, 90% of the Banco de Venezuela (\$345 million) in Venezuela, 87.5% of Banco Mexicano in Mexico (\$40.6 million), 75% of Banco Osorno (\$410 million) in Chile, and the BCH network (\$235 million) in Puerto Rico. In March 1997, Banco Santander became the first Spanish bank to enter the Brazilian market when it acquired 51% of Banco Geral do Comercio (\$229 million).

- The BBV's strategy has consisted of establishing agreements with local partners which give it a majority stake and 100% management control. It has been particularly active in Mexico, where it acquired 90% of Probursa (\$495 million) and 100% of the Cremi and Oriente banks (\$18 million); in Peru, where it acquired 68.5% of Banco Continental (\$130 million); in Colombia, buying 43.5% of Banco Ganadero (\$398 million); in Venezuela, acquiring 40% of Banco Provincial, and 100% of Popular and Banco de los Andes (\$44 million); and in Argentina, where it now controls 32% of Banco Francés del Río de la Plata (\$350 million) and 52% of Banco de Crédito Argentino (\$985 million).

- BCH has followed a strategy of establishing a continent-wide alliance through the creation of an investment holding company. This has enabled it to establish itself at the head of the banking market in Chile after merging with Banco de Santiago and Banco O'Higgins. In alliance with the local Luksic group, BCH is now consolidating its presence in the Southern Cone, and above all in MERCOSUR. The BCH has adopted a similar strategy in Central America, forming an alliance with the Gilinski group to enter that market. In Mexico, BCH has a stake in the Prime group which controls 20% of Banco Internacional.

The Spanish bank Argentaria also operates in Latin America, where it has concentrated on promoting and financing trade between Spain and MERCOSUR. To this end, it has merged its subsidiaries in Chile, Argentina, Paraguay and Brazil.

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It is interesting to note that the major Spanish banks still have only a weak presence in Brazil, Latin America's largest and potentially most profitable market. There are some 200 banks in Brazil (five of which are of a similar size to the BBV, Santander and BCH), as well as a large number of very well-established foreign and regional banks. This situation appears to be explained by the tendency for the destination of investments to be determined, at least initially, by cultural affinity and cost factors: a one point share of the Brazilian market currently requires an investment of some $265 million, a sum which would be sufficient to acquire the first or second largest bank in Argentina or Colombia. Despite the presence of the Banco Santander, BBV has announced plans to spend between $800 million and $850 million to enter the Brazilian market.

Until now, Spanish banks have followed a pragmatic strategy in Latin America, choosing to invest in countries with which they have cultural and linguistic ties, and in which they can expect success to be achieved at a lower cost. Reflecting the favourable economic prospects in the region, the expanding Spanish presence is encouraging Latin American banks to embark on restructuring and modernization processes, introducing new technologies, products and management methods.

The geographic distribution of Spanish FDI in Latin America

As a result of the major investments made by Spanish companies during the 1990s, Spain is now one of the largest foreign investor countries in Latin America. Spain's position in the ranking of investors in the region could be even higher than that suggested by the figures; since it is impossible to identify the final destination of flows to Panama and Caribbean offshore centres in the form of reinvested earnings, these figures do not reflect the real volume of investment.

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Table 1
Breakdown of Spanish investment flows to Latin America by country
(in millions of US$)

	averages 1980-1989	1990-1996	1990	1991	1992	1993	1994	1995	1996
Argentina	21	206	87	18	79	27	65	555	610
Brazil	11	32	15	51	17	1	28	73	37
Chile	37	41	9	37	32	4	96	24	82
Colombia	2	68	3	10	8	28	24	30	376
Mexico	21	86	37	15	21	46	184	207	94
Peru	3	294	0	0	0	0	1,616	170	275
Offshore Centres	51	235	210	307	123	59	213	154	581
Latin America & the Caribbean	181	959	371	548	308	153	2,285	883	2,162

Source: IDB-IRELA, based on Table 5 of the Statistical Annex (balance of payments based).

Argentina has been the main destination of Spanish investment in Latin America in recent years. This is a consequence of the major programme of privatizations implemented by the Argentine government, and the leading role that Spanish companies have played in it. As noted above, the bulk of Spanish investments in the 1990s has been channelled through holding companies. However, when the data on the sectoral origin of flows are crossed with those for the final destinations of this capital, the results show that there has been a major expansion in investment in the transport and communications sectors (Telefónica and Iberia), financial services, banks and insurance (see Box 1), oil extraction and refining (see Box 3), as well as energy and water (Endesa and Aguas de Barcelona).

Spanish FDI in Peru is a recent development, as for a number of years the country's economic problems kept investors away. However, the extensive programme of reforms implemented by the Peruvian government and the return to macroeconomic stability have created good investment opportunities, thereby awakening the interest of foreign investors. Spanish companies have been prominent among these, above all through their participation in the privatization

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process; one notable example is the acquisition of the Compañía Peruana de Teléfonos and Entel by Telefónica (see Box 2).

The presence of Spanish companies in Chile is determined by the importance, both in terms of the origin and destination of investment, of the financial sector (banking and insurance), which has absorbed 87% of the total FDI flows to the country in the 1990s. The investment flows into holding companies comes from banks or insurance companies. In this sense, the sectoral distribution of investment by sectors is identical to that in the 1980s, when Chile launched its programme of structural reforms. Accordingly, the fishing, and paper and printing industries have retained their share of Spanish investment, while the construction, energy and water sectors have attracted a growing proportion of total FDI.

The sectoral breakdown of Spanish FDI in Mexico has changed dramatically during the 1990s. As noted above, before 1990 most investment was made in wholesale distribution, metallurgy, insurance and, to a lesser extent, the paper and printing industry, food, beverages and tobacco. The absence of investment in the financial sector, due to the legal restrictions then in force, should be noted. Following economic liberalization in the 1990s, and the resolution of the problems that numerous Mexican banks faced in the wake of the 1994 currency crisis, there has been an upsurge in FDI flows to this sector. In the period 1993-96, banks and insurance companies absorbed 38% of Spanish investment in Mexico, a trend which intensified in 1997 as a result of major investments by Banco Santander and BBV, many of which were channelled through holding companies.

The greater relative importance of banking and insurance activities has not reduced the traditional diversity of Spanish investment in Mexico. Food, beverages and tobacco (25%) and metallurgy and transport equipment (14%) still attract considerable inflows of capital, while tourism and the chemicals industry are absorbing larger shares of the total. Unlike in other countries in the region, Spanish companies have a strong presence in manufacturing industry. The best established Spanish companies in the country have made further investments in response to the opportunities created by the implementation of the North American Free Trade Agreement (NAFTA).

The level of Spanish investment in Brazil was traditionally relatively limited in comparison with the size of the country's economy. Moreover, the sectoral breakdown of investment in Brazil was rather different to that found in the rest of Latin America, since the financial and commercial sectors accounted

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for a very small share of the total. The sheer scale of Brazil's domestic market, combined with the existence of very high protectionist barriers, meant that most FDI was absorbed by the food, beverages and tobacco industries, metal products, electrical and electronic equipment, and parts and components for the automobile industry. Again, holding companies acted as channels for much of this investment (46%).

In the 1990s, the sectoral breakdown of investment has remained essentially unchanged, except for the increasing importance of banks and insurance companies (30%). However, 45% of Spanish FDI flows still went to manufacturing industry.[11] Through the *Plan Real*, Brazil managed to stabilize and partially liberalize its economy and, in the last two years, embark on a number of attractive privatization programmes. This helps explain the increased Spanish investment in telecommunications, electricity and infrastructure in 1997, which also saw major investment in the financial sector.

Reflecting the deteriorating economic situation in the country, Spanish investment in Venezuela has been very erratic over the last few years. The scale of the economic crisis highlighted the fragility of the Venezuelan financial system, forcing the government to open up the sector (which had traditionally been reserved to local investors) to foreign capital. Spanish companies have engaged in a number of major investment operations, including Banco Santander's acquisition of Banco de Venezuela and BBV's takeover of Banco Provincial. These operations reflected a significant change in the sectoral distribution of Spanish FDI in Venezuela. During the first half of the 1990s,[12] there was a sharp drop in investment in tourism, while manufacturing industry increased its share of Spanish investment (90% of which was channelled via holding companies). There was also increased investment in the financial sector, and above all insurance.

Spanish investment in Colombia has traditionally been concentrated in the paper and printing industry, the financial sector (mainly insurance) and commerce. In line with the general trend for the 1990s, there has been a sharp increase – to the point that they absorb almost 80% of total flows – in investment in financial services (banks and insurance companies), followed at a considerable distance by the paper and printing industry (with 6%).

In conclusion, over the course of the 1990s there has been a major increase in Spanish FDI flows to Latin America in both absolute and relative terms. These

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investments, however, have converged on a small number of companies and a few large operations. As a result, Spanish investment in the region has become even more concentrated in a small number of countries and sectors.

The strategy of Spanish companies in Latin America

At the end of the 1980s, Spanish FDI was concentrated in a handful of sectors, with just a few companies investing in each.[13] Most Spanish investors in Latin America opted to make rights' issues in existing companies, or to opt for the second, increasingly popular strategy of directly making acquisitions; by 1996 this had become the principal mechanism for investment. This tendency is similar to that followed by the leading companies in the industrialized countries, and reflects the importance of the availability of strategic assets and the need to circumvent the barriers to entering different markets. Greenfield investment accounted for a very small part of Spanish investment (even less than long-term intra-group loans). As a result, Spanish companies with interests in Latin America can be divided into two main groups.

Box 2: Telefónica's Strategic Alliances

In just a few years, Telefónica de España has developed from being a state-controlled monopoly to an increasingly efficient, diffused ownership, private company facing a number of new challenges. It has embarked on a fundamental process of transformation in order to respond to the dismantling of the telephone monopolies in Spain and the EU and to convert itself into a leading international telecommunications company. The changes seen in Latin America over the last few years led Telefónica to choose the region as the location in which to implement this strategy. Taking advantage of the privatization programmes, and the transitional monopolies granted by governments, Telefónica acquired telecommunications companies in Argentina, Brazil, Chile, Peru and Puerto Rico, and considerably expanded the existing infrastructure in the sector. Telefónica currently has 7.5 million fixed lines, almost 600,000 mobile phone clients, and some 300,000 cable television subscribers in Latin America.

Since 1988, Telefónica has held a 43% stake in Compañía de Telecomunicaciones de Chile (CTC), providing basic telephony (2 million lines), long-distance calls (via the affiliate CTC Mundo), and a mobile phone service (100,000 clients).

Since November 1990, and through its stake in Telefónica de Argentina, Telefónica has operated the telecommunications system in the south of the country, providing basic telephony, long-distance calls (through a 50-50 joint venture), and more recently

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mobile telephony. The company currently operates some 3.7 million basic lines and 130,000 cellular telephones. At the same time, it owns 75% of Telefónica Larga Distancia (TLD) in Puerto Rico.

In May 1994, Telefónica paid more than $2 billion for a 35% share of Compañía Peruana de Teléfonos (CPT) and ENTEL Peru, which it amalgamated into Telefónica del Perú. This company provides both local and long-distance telephone services, as well as having some 50,000 mobile phone clients. In January 1997, Telefónica formed part of the consortium which acquired 35% of Brazil's Companhia Riograndense de Telecomuniçacôes (CRT) for $681 million. CRT provides basic telephony and long-distance services in the state of Río Grande do Sul, where it has over 780,000 lines and 180,000 cellular phone clients.

Telefónica lost its monopoly in Spain in 1998, and it is expected that in the next few years the companies controlled by Telefónica Internacional (TISA) – essentially those in Latin America – will generate almost half the company's earnings. To date, the monopolistic position Telefónica enjoys in Latin America has brought it major profits. However, as these markets have developed, and the rhythm of growth has decreased, they have gradually been opened up to competition. There is no longer a monopoly in Chile, while the market will be opened up in Peru in 1999, and in Argentina in 2003.

Most of Telefónica's network in Argentina (71%), Chile (100%) and Peru (68%) is digitalized, enabling the company to use the network to provide other services apart from basic telephony services. As a result, it is increasingly interested in expanding into other areas, including cable television, Internet services, etc.

As part of its strategy for expansion, in April 1997 Telefónica tried to establish a joint venture with British Telecom and the US company MCI Communications Corporation. This agreement constituted a non-aggression pact in the markets where each operator was already active and gave Telefónica management of joint operations in Latin America, as well as a presence in the Mexican market, through MCI's subsidiary Avantel. However, the agreement collapsed when MCI was taken over by WorldCom Inc. in October 1997. Telefónica has continued to seek alliances with major international operators (notably AT&T Corporation).

According to analysts, these alliances will bring significant investment into the region (and above all Brazil), as well as reactivating the long-standing project to establish a Pan-American Network which would handle international traffic throughout the continent, requiring a total investment of some $1 billion. Telefónica, therefore, is coming to the end of the first phase of its new corporate strategy which, with Latin America to the fore, has transformed the company into one of the leading international telecommunications operators.

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The first group consists of large companies in oligopolistic sectors, along with publically-owned companies operating in regulated markets. This group is the source of at least 75% of Spanish investment in Latin America. The second group comprises medium-sized companies with significant ownership advantages (such as brand names, marketing, technology, organization or management). These companies invest abroad in order to promote their exports, produce in large-scale, protected markets, acquire strategic assets, or secure supplies of raw materials or products in demand in the Spanish market. This group accounts for a smaller, but growing proportion of Spanish FDI in the region (see Table 3).

Table 2
Breakdown of Spanish FDI in Latin America by Sector
(in millions of US$)

	1993	1994	1995	1996	Total 1993-1996
Industry	30	152	99	596	876
Services	262	2,428	506	1,959	5,154
— Financial	156	217	295	1,713	2,381
— Transport communications	106	2.211	163	181	2,611
Holding companies	300	755	1,239	1,621	3,916

Sources: Compiled by the author from data in the *Boletín de Información Comercial Española* (various years), DGEITE, Spanish Ministry of Economy and Finance (based on notifications).

Ownership advantages, location advantages and the benefits of internalization

Economic theory suggests that companies that engage in direct investments in order to exploit ownership advantages are attracted by the location factors of the recipient country, and opt for the advantages derived from internalizing operations instead of carrying them out via the market. Ownership advantages, therefore, compensate for the costs and disadvantages companies face when investing directly in unfamiliar environments. According to this theory, intangible assets are the main determinants of foreign investment. The empirical evidence available in the Spanish case confirms that accumulation of intangible

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assets increases FDI.[14] However, ownership advantages are a necessary but insufficient condition for FDI: this also requires the existence of location advantages.

The location advantages offered by the recipient countries represent their main attraction for investors. These advantages may consist of an abundant supply of raw materials, low labour costs, incentives for investment, tariff and non-tariff protection, the country's participation in regional integration processes, etc. The concentration of Spanish FDI in the service sector in Latin America raises the question of the existence of sector-specific location advantages.

Existing studies of investments in the service sector demonstrate that, in terms of location factors, there is a positive correlation between these capital flows and:

— the opening up of the markets in recipient countries to FDI in services;
— cultural affinity between the recipient and investor countries; and
— the size and rhythm of market growth in the recipient countries.

These studies also indicate that, in terms of ownership advantages, flows are positively linked to:

— the comparative advantages of the investor companies;
— the oligopolistic behaviour of the companies in investor countries in their domestic markets;
— the size and rhythm of growth of the service companies making the investment;
— the presence of other investor companies from the country of origin in the market of the recipient country; and
— cultural affinity.

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Table 3
Principal Spanish Investors in Latin America

Company	Sector of Activity
First Group	
Banco Santander	Financial institutions
Banco Bilbao-Vizcaya (BBV)	Financial institutions
Banco Central-Hispano (BCH)	Financial institutions
Banco Exterior de España	Financial institutions
Mapfre	Insurance company
Telefónica	Telecommunications
Gas Natural	Hydrocarbons
Repsol	Hydrocarbons
Iberia	Transport
Endesa	Electric energy
Iberdrola	Electric energy
Unión Fenosa	Electric energy
Dragados	Construction
Agromán	Construction
Empresa Nacional de Celulosa	Paper industry
Aguas de Barcelona	Water management
Second Group	
Gamesa	Aeronautical parts and components
Grupo Antolín-Irausa	Autoparts and components
FICOSA	Autoparts and components
Talleres Fabio Murga	Autoparts and components
Tableros de fibras-Tafisa	Wood industry
Acerinox	Metal transformation industry
Viscofan	Plastic wrappings
Indetex	Textile and clothing
Sol Meliá	Tourism
Homasi	Tourism
Iberco	Tourism
Hoteles Mayorquines Reunidos	Tourism
Maninvest	Tourism
Roca Radiadores	Drainage and heating
Planeta	Printing and publishing
Santillana	Printing and publishing
Salvat	Printing and publishing
Cía. Catalana de Cementos Portland	Non metallic minerals
Cía. Valenciana de Cementos Portland	Non metallic minerals
Corporación Uniland	Non metallic minerals

Sources: Compiled by the author from data in CEPAL, *Directorio sobre Inversión Extranjera en América Latina y El Caribe*, 1993, and Reuters.

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Market deregulation in Latin America has been a key element behind investments in telecommunications (Telefónica, Alcatel, Amper) and transport (Iberia). In general terms, liberalization and the favourable treatment given to FDI, combined with the attractive incentives offered in privatization programmes, have been further important major location factors for Spanish companies. At the same time, companies which enjoy ownership advantages (in particular, large corporations and those with an expansive strategy) are attracted by their cultural and linguistic affinity with the region, which gives them an edge over their competitors from other cultures, many of which already had experience of operating in these markets.

Location factors, such as access to natural resources, have also played a significant role in influencing investment in the primary sector (Repsol and Gas Natural). On the other hand, the abundant supply of raw materials, low labour costs, regional integration processes, the scale and high degree of protection of some markets, and the problems involved in supplier-client relations are also important incentives for investment in manufacturing industry. These factors have encouraged the internationalization of Spanish automobile component companies (Antolín-Irausa and Ticosa) in Mexico, Brazil and Argentina. These location advantages have encouraged some other Spanish companies, as well as some Spanish affiliates of transnational corporations (TNCs), both to export and engage in FDI (as exemplified by the way Alcatel followed Telefónica to the region).

Despite the scant information available on the subject, the advantages of internalization should also be highlighted. Foremost among these is the direct control companies acquire over all the various phases of the value chain. Given the difficulties involved in directly observing this strategy in operation, most experts suggest that its importance should be measured through a number of indicators referring to the degree of control a TNC has over its foreign affiliates. Analysis of these indicators reveals the growing tendency for Spanish companies to secure majority control of their foreign operations, above all in the EU and the United States, and to a lesser extent in Latin America.

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Box 3: The Expansion of Repsol in Latin America

Repsol was one of the first companies to be privatized in Spain, a process completed in April 1997 with the sale of the 10% stake still owned by the Spanish government. It is currently one of Spain's five largest companies. Faced by increasingly tough competition in the domestic market (which provided 80% of its revenue), Repsol has embarked on a new strategy centred around two key objectives:

- — expansion in Latin America; and
- — entry into the electricity sector.

In little over two years, Repsol has invested almost $2 billion in Latin America and plans to invest a further $3 billion over the next five years. As a result, the company anticipates that Latin America will provide some 25% of its total revenue by the beginning of the next century.

Although Repsol has established operations in Ecuador, Peru and Mexico, its strategy for expansion in Latin America has focused on Argentina. Argentina is a member of MERCOSUR and offers Repsol a potential springboard into Brazil, the most attractive market in the region. Repsol's first operation in Argentina was in oil prospecting (in association with Astra), while, following the acquisition of Gas Natural Buenos Aires Norte in 1992, the company has been involved in prospecting for, and the production and distribution of, gas supplies.

In mid-1996, Repsol stepped up its strategy of expanding in MERCOSUR. In June that year, it acquired a 37.7%, controlling stake in Astra, Compañía Argentina de Petroleo, for $360 million. Over the course of the year, Repsol increased its share in Astra to 56.7%, taking the company's total investment to $659 million.

Through Astra, Repsol has continued to increase its assets in Argentina, where it plans to invest $2 billion over the next five years. In 1997, the company acquired 45% of Pluspetrol Energy for $340 million and 67% of Mexpetrol Argentina S.A. for $204 million; both of these companies are involved in prospecting and producing oil and gas. In May that year, Repsol bought a network of 700 service stations in Argentina for $345 million, giving it a 13% share of the Argentine fuel distribution market, which is its core business in Spain. Finally, in June 1997 Repsol invested $79.2 million in the acquisition of Astra S.A., a company which distributes and stores liquid gas.

Apart from Argentina, Repsol has significant interests in Peru, Venezuela, Colombia, Bolivia, Mexico and Ecuador. In Peru, it is a member of the consortium that successfully bid for 60% of the La Pampilla refinery ($180.5 million), acquired two liquid gas bottling and distribution companies (Rimac and Solgas), and established a

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network of 30 fuel distribution points. Repsol has also announced plans to invest a further $240 million in Peru over the next five years.

In Latin America, and in accordance with its corporate strategy, Repsol has not only concentrated on oil and gas, but has also expanded into the electricity sector. In association with Iberdrola, it currently has a stake in two generating plants in Argentina, and is considering the possibility of investing in Brazil. Analysts believe that Repsol has plans to generate over 3,000 MW in Argentina and Brazil over the next five years. Everything suggests, therefore, that Repsol will continue to consolidate its presence in Latin America, operating in increasingly competitive sectors.

The second factor is the degree of internalization of exports (that is, the extent to which a company uses its own trade and distribution channels for products made in Spain and exported to other countries). A number of recent studies suggest that over the last few years the proportion of exports internalized by investor companies has increased in relation to total exports. They also reveal that the degree of internalization rises as the distances involved grow. This tendency is confirmed in the case of the three main markets for Spanish companies: the EU, the United States, and Latin America. Over the last few years, the destination of most Spanish investment in Latin America (mainly the service sector) has meant that the advantages of internalization seem to have been less significant in the region than in the case of the EU.

Conclusions

Spanish FDI in Latin America and the Caribbean has passed through two different phases during the 1990s. Between 1990 and 1993, while the EU still absorbed the bulk of Spanish FDI, the proportion of the total going to the countries in the region (including Panama and the Caribbean offshore centres) continued to rise, just as it had done since the end of the 1980s. Since 1994, Latin America has been at the centre of the major increase in Spanish FDI, and has in fact replaced the EU as the single most important destination for these flows. The importance of the region for Spanish FDI may be even greater than the figures suggest, since many of the investments channelled via Panama and the Caribbean offshore centres are in fact destined for other countries in the region. The sectoral distribution of Spanish FDI has changed over the course of the decade. Along with the financial sector, which has traditionally been the

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main focus of Spanish FDI flows and has been the object of renewed interest in the 1990s, there has been a major upsurge in investment in telecommunications and, to a lesser extent, air transport. Both trends have served to accentuate the relative insignificance of investment in manufacturing industry.

Acquisitions and rights' issues remain the preferred investment mechanism for Spanish companies. Many of these investments have been made via holding companies; this is a common feature of Spanish FDI in the EU and the United States as well as in Latin America. Ownership and location advantages have been key factors in the investment strategies followed by Spanish companies, outweighing the benefits offered by internalization. A large proportion of Spanish FDI has been made by a small group of oligopolistic companies and state-owned companies (some of which have now been sold to private investors, such as Telefónica, or are currently being privatized, such as Endesa). At the same time, however, there has also been an increase in the role played by medium-sized companies, whose international strategy is based on their significant ownership advantages.

In light of the strategies adopted by Spanish companies and the location advantages they enjoy, Latin America constitutes a very attractive destination for their FDI. This can be seen from the provisional figures for 1997, when investments were authorized in the region for a value of $6.6 billion, some 52% of Spanish FDI worldwide. The countries in the region are engaged in a process of economic modernization which will enable them to base their growth not just on an abundance of resources and low labour costs, but also on more dynamic factors such as improvements in their technological capacity, human and capital resources, and infrastructure. Foreign companies will continue to play a role in this process provided the countries in the region maintain their commitment to macroeconomic stability, advance towards regional integration, and continue to improve social conditions.

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NOTES

[1] The "development path" of foreign investment explains the gap between the level of development of a country and its FDI (Dunning and Narula, 1994). As companies develop, their competitive advantages change with respect to both their domestic as well as external markets; advantages based on privileged access to natural resources lose importance in comparison to those based on assets generated by the company (brand names, international expansion, organization and/or management, marketing). These advantages serve as the foundations for a company's international expansion, and hence foreign investment.

[2] Above all in Mexico, Argentina, Chile and, albeit to a very limited degree, Brazil.

[3] These were concentrated in Mexico (15.5%), Argentina (13.2%), Venezuela (20%), Brazil (10.5%), Chile (6.3%), Panama (8.6%) and Puerto Rico (9%). Equally, 58% of the capital invested by the 100 largest investor companies (accounting for 84% of the funds invested, but a mere 12% of all Spanish investors) was located in Latin America (Durán and Sánchez, 1981).

[4] In contrast, although the financial sector absorbed 37% of Spanish investment in the EU in this period, commercial activities attracted some 30% of the total.

[5] The profile of Spanish investor companies in this period can be deduced from the data contained in the 1986 Census of Spanish Direct Investment and the information compiled by the Economic Commission for Latin America and the Caribbean (ECLAC) and published in the *Directorio sobre Inversión Extranjera en América Latina y el Caribe* (1993).

[6] In the EU (the United Kingdom, France, Belgium, Germany, Italy, the Netherlands and Luxembourg); in the United States; in Latin America, (Puerto Rico, Chile, Uruguay, Argentina and Brazil); and in Panama and the Caribbean offshore centres.

[7] The main recipients of Spanish FDI in the EU were Portugal (22.2%), France (12.3%), the United Kingdom (11.2%) and, increasingly, Italy (13.8%). The Netherlands also stands out, since it absorbed almost 30% of these flows; however, most of these investments were essentially financial operations, mainly in holding companies, designed to exploit tax advantages in the Netherlands rather than to finance a productive activity.

[8] Almost 93% of investment in Latin America (excluding Panama and the Caribbean offshore centres) was concentrated in a small group of countries: Argentina (34%), Venezuela (15%), Chile (13.2%), Mexico (8.6%), Brazil (6.5%) and Puerto Rico (16%).

[9] International tax planning of investment projects is an important factor in investment strategies. Tax considerations not only influence the choice of the recipient country, but also the structure of a company's international network.

[10] The only exception is investment in the commercial sector, which, in the case of Spain at least, has traditionally been made to support a company's foreign trade operations.

[11] These manufacturing industries include investment in the production of automobile parts and components, electrical equipment, electronic and metallic products, paper and printing (7%) and chemicals (3%).

[12] In the 1980s, tourism accounted for almost half the total investment, while the rest went to production of metal products, the paper and printing industry, and, to a lesser extent, insurance.

[13] According to the 1986 Census, 61.5% of all Spanish Net Capital (NC) in the region belonged to the 36 companies in the financial sector (banks, insurance and holdings); the 47 companies in textiles, clothing, wood, paper and printing, and other manufacturing industries accounted for 7.6% of the NC; the 131 commercial companies accounted for a further 5.8%; the 18 companies producing metallic products (except machinery) and transport equipment held 5.2%; and the 57 companies in the fishing, food, beverages and tobacco sectors owned 5.1% of the NC.

[14] This would be the case of some companies in the second group: Gamesa and the Antolín-Irausa Group, FICOSA, Viscofan, Acerinox and Planeta. The large companies, such as Banco Santander and Telefónica, and to a lesser extent BBV, which have an established brand name and reputation, enjoy organization and management advantages, and have implemented an aggressive internationalization strategy (Durán, 1996).

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CHAPTER V

GERMANY*

Introduction

Foreign direct investment (FDI) is a widely debated issue in both Latin America and Germany. In Germany, there is considerable concern that the massive gap between the increasingly substantial outflows of FDI and the scant inflows is both symptomatic of the relatively unfavourable climate for investment in Germany and contributes to unemployment.[1] More specifically, many people believe that German FDI in developing countries reduces both the job prospects and wage-levels of low-skilled German workers. In Latin America, on the other hand, it is feared that the increasingly tough global competition for FDI will jeopardize the current boom in the inflow of capital to the region. The concern is that the Asian economies in transition (above all China) and the Central and Eastern European countries will prove more attractive to international capital, thereby diverting foreign investment away from the traditional recipient countries in Latin America. In this respect, the future of the reform processes in Central and Eastern Europe are particularly important for Germany: if they evolve favourably, many observers consider that the attractive opportunities existing closer to home may cause German FDI to be diverted from the region.

On closer examination, however, it appears that these fears are largely unfounded. From the standpoint of Germany, relocation of labour intensive production to low-wage economies does not seem to be a prime motive for German FDI. As a result, the flow of investment to Latin America says little about the state of the German economy or the need or otherwise for structural adjustments there. At the same time, from the perspective of Latin America, there is little evidence to suggest that there has been a substantial diversion of German FDI away from the region. The particular pattern of German FDI in the region in comparison to FDI from other countries seems to have two distinct implications. On the one hand, the distinctive character of German investment in Latin America appears to make it less likely that it will be diverted to other regions. On the other, it has also made German investors less sensitive to the improved economic climate which now exists in Latin America, and the investment opportunities this has created. And this, in an age of globalization, could prevent German FDI from expanding in the future.

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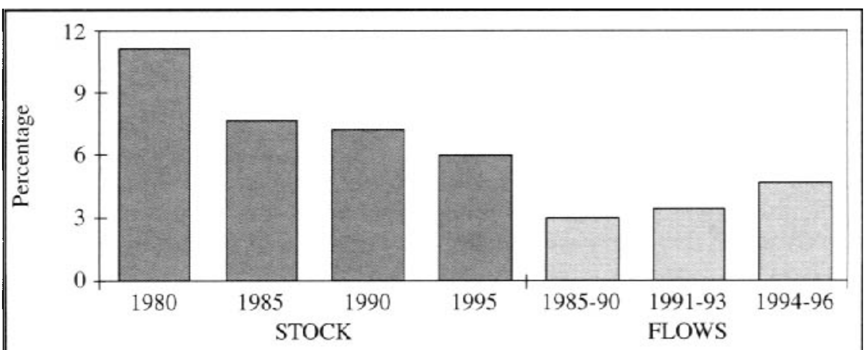
Main Tendencies of German FDI in Developing Regions

Position of Latin America and the Caribbean

Investment relations between Germany and Latin America and the Caribbean[2] look very different from the perspective of the investor and recipient countries. From the standpoint of Latin America, German FDI is relatively insignificant. Since the mid-1980s, German companies have been responsible for less than 5% of all FDI flows to Latin America, and they hold only a slightly higher proportion of all FDI stock in the region (see Graph 1).

Over the last few years, almost all the other major investor countries have overtaken Germany in terms of accumulated FDI stock in Latin America. The stocks of Japanese and US FDI, for example, were 3.5 and 4 times higher in 1994 than in 1985, while German investments in the region grew by less than 80% over the same period. As can be seen in Graph 2, Germany's comparatively poor record in this respect essentially dates from the 1980s, when flows of German FDI to the region stagnated. This suggests that German investors have reacted more slowly than their counterparts in other countries to the improved climate for investment in the region. In the 1990s, however, Germany regained ground, substantially increasing its FDI stock.

Graph 1
Germany's Share of Total FDI in Latin America, 1980-96
(in percentages)



Sources: Compiled by the author from data from the Deutsche Bundesbank; OECD (1996); UNCTAD (1997).
1. The flows are averages for the different periods.

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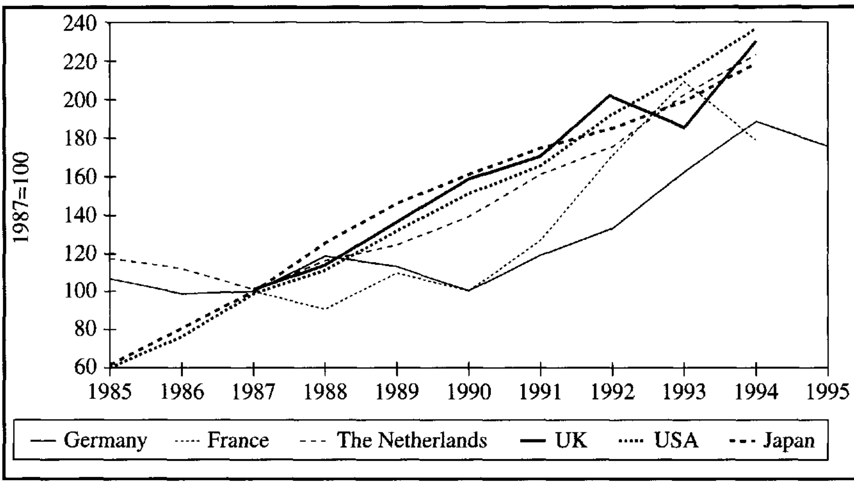
In contrast, from a German perspective, Latin America appears to be an important destination for FDI, at least in terms of German investment outside the Organization for Economic Development and Cooperation (OECD). During the 1980s, the region absorbed some 66% of German FDI in the developing countries (see Graph 3).[3] The situation has not changed significantly in the 1990s. Although this figure fell to below 50% in 1995, this was still significantly higher than Latin America's share of total FDI stock in the developing countries.

Graph 2
FDI Stock of the Main Investors in Latin America, 1985-95



Sources: Compiled by the author from data from the Deutsche Bundesbank; OECD (1996).

1. The index is based on FDI stocks in national currencies, except for Japan, whose stock is registered in US$.
2. There are no figures for France for 1985 and 1986.
3. The figures for the Netherlands do not include investments in Mexico.

German investors' preference for Latin America, as well as their relatively small share of total FDI in the region, essentially reflects the comparatively low level of German FDI in the developing countries as a whole:

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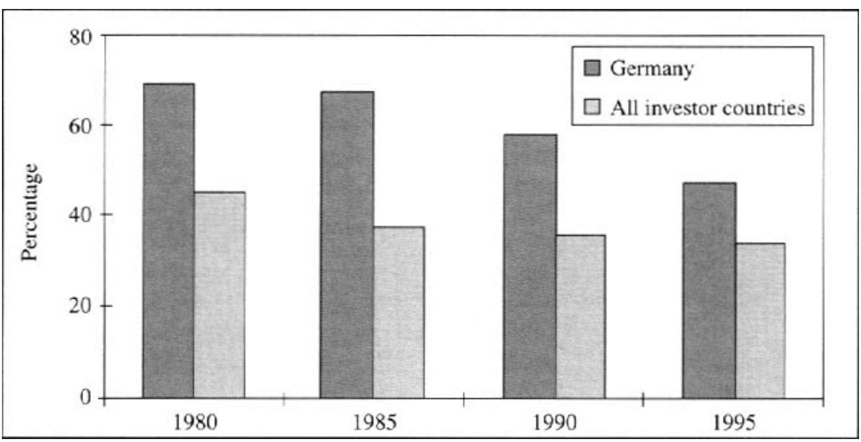
- Between 1985 and 1994, less than 10% of all German FDI flows went to non-OECD countries (including Mexico). In contrast, the non-OECD countries' share of all Japanese FDI was three times higher, and almost four times higher in the case of US FDI.

- The same is true in terms of accumulated FDI stock. In 1990, the developing countries as a whole accounted for only 10% of all German FDI stock, compared to 25% of all FDI stock from the United States, and 32% from Japan.

More recently, however, there are signs that the developing countries are beginning to attract larger flows of German FDI. In fact, the developing countries' share of all German FDI doubled in the period 1993-96, rising to an average of almost 20%. As would be expected, this new pattern of flows has had a less significant impact on the distribution of accumulated stocks of German FDI, some 13% of which were located in developing countries in 1995.

Graph 3
Latin America's Share of Total German and Other Investor Countries' FDI Stock in Developing Countries, 1980-95



Sources: Compiled by the author from data from Deutsche Bundesbank; UNCTAD (1997).
1. Including Central and Eastern European economies in transition.

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A number of conclusions can be drawn from these tendencies with respect to the fears existing in both Germany and Latin America discussed in the Introduction to this chapter:

- First, given that German FDI has traditionally been concentrated in countries with a similar level of development (essentially those in the OECD), it is unlikely that the outflow of FDI from Germany has contributed significantly to its unemployment problem. If the relocation of production to economies with lower costs via FDI had a considerable impact on jobs, this would be more marked in the United States and Japan, since both these countries have much more capital invested in low-wage developing countries.Yet, a comparative analysis of the labour market in the leading industrialized countries shows that the opposite is true. Historically, that is, the figures do not seem to support this theory. It remains to be seen, however, whether the recent upsurge in German FDI in the developing countries in general, and Latin America in particular, will have more serious implications for employment in Germany in the future.

- Second, given German companies' traditional preference for investment in Latin America, the concern that exists in the region with respect to a possible diversion to other areas is understandable. Nonetheless, given that Germany accounts for only a small proportion of total FDI in Latin America, the potential consequences would not be too serious. In any event, at present there is no evidence of a significant diversion of German FDI away from Latin America.

Latin America's main competitors

Discussion of FDI diversion is inevitably made more difficult by the fact that, unlike in the case of trade diversion (a result of discriminatory trade policies), there are no firm analytical bases for the concept. Neither Germany nor the European Union (EU) have policies that explicitly discriminate between different recipient regions. Nor is it possible to establish a direct causal relationship between German economic policy and German investors' traditional preference for Latin America, or a possible diversion towards other developing regions. Nonetheless, economic policy can indirectly influence decisions regarding the location of investments. Latin America could be in an unfavourable position when it comes to competing for German investment as a result of the close relation existing between the EU and the Central and Eastern European economies in transition. The fact that the prospective members of the EU among these countries will benefit from unrestricted access to EU markets may clearly attract German investment to the region.

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It is difficult, however, to gauge the real, empirical significance of the diversion of FDI from Latin America to Central and Eastern Europe. In the absence of a counter-factual situation, it is impossible to know exactly how German FDI would have evolved in Latin America if Central and Eastern Europe had not emerged as potential competitors for these flows. Equally, it is impossible to say whether the situation would have been different for Latin America if Central and Eastern Europe had not obtained preferential access to EU markets.

Despite these limitations, the evidence suggests that FDI diversion to these countries has not had a significant impact on the evolution of German FDI in Latin America. Table 1 shows that German FDI in developing regions is by no means a zero-sum game, in which a rise in flows to one region inevitably means a fall in flows to another. On the contrary, since the mid-1980s all the developing regions have received increasing flows of German FDI. It seems more likely, therefore, that the new opportunities for investment in Central and Eastern Europe have resulted in a net increase of German FDI as a whole in this period, rather than drawing investment away from other regions.

A comparison between the pattern of investment in Asia and Latin America between 1989-92 and 1993-96 tends to confirm this impression. If we attribute the fact that German FDI flows to Latin America increased relatively little (by a factor of 2.3) in this period to a diversion of flows to Central and Eastern Europe, it is difficult to explain why Asia received almost four times more German FDI between 1993 and 1996 than in the period 1989-92 (a similar increase to that enjoyed by Central and Eastern Europe). Any diversion of FDI towards the European economies in transition should have had a similar effect on Asia and Latin America (since both regions faced new, and to some extent privileged competition from these countries for German FDI).

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Table 1
Flows of German FDI to Developing Regions, 1985-96
(annual average in millions of US$)

	1985-88	1989-92	1993-96
Latin America	363	521	1,204
Africa	–78	165	231
Asia	522	585	2,261
Central and Eastern Europe	39	901	3,691

Source: Compiled by the author from data from Deutsche Bundesbank and OECD (1996). See also the Statistical Annex.

Nor does the evolution of the stock of German FDI in Latin America and other, competing developing regions suggest that there has been a substantial diversion of direct investment. It is important to remember, however, that changes in the value of the stock may affect the accuracy of the data, and hence the analysis too. This is particularly important in the case of investments in Latin America, where German investors were already operating in the 1970s and 1980s. Nonetheless, it is striking that the accumulated German FDI stock in Latin America had already begun to stagnate in the 1980s, that is, well before Central and Eastern Europe began to compete for German FDI (see Graph 4). On the other hand, the increase in the stock of German FDI in Latin America in the 1990s coincided precisely with the upsurge in German direct investment in Central and Eastern Europe. German FDI stocks increased at the same time in both regions, rising by some $7 billion in each between 1990 and 1995 (compared with an increase of $4.2 billion in Asia during the same period).

In short, the evolution of German FDI in Latin America suggests that this is essentially determined by changes in investors' perception of the climate for investment in the region, rather than the performance of investments in other developing regions. Hence, an analysis of the evolution of German FDI in Latin America must be based on an understanding of the factors that have shaped the way investors see the region. In this sense, an analysis of some of the structural characteristics of German FDI in Latin America may clarify the factors which influence investors' perception of the opportunities existing in the region, that is, precisely, the decisive determinant of investment there.

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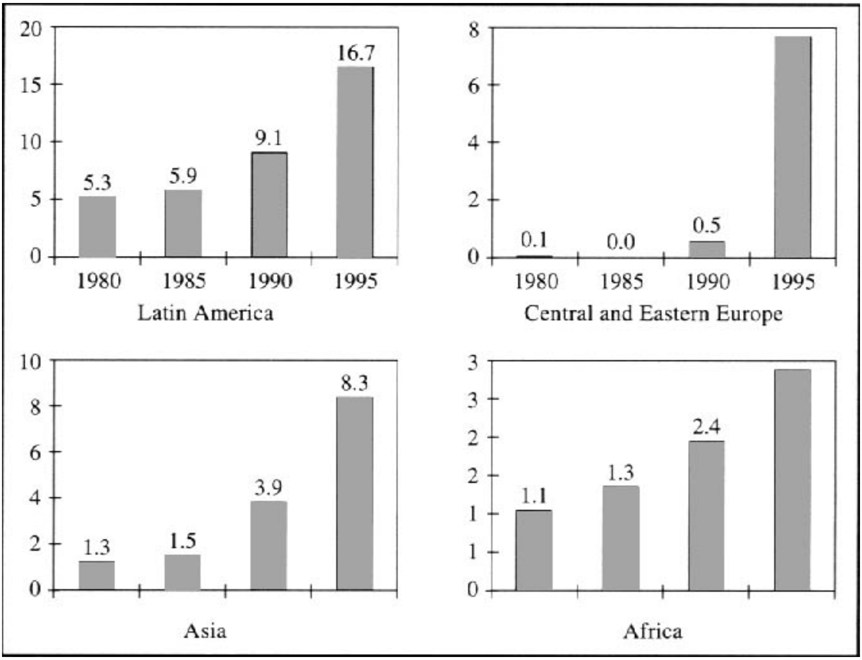
Graph 4
German FDI Stock in Developing Regions, 1980-95
(in billions of US$)



Source: Compiled by the author from data in Deutsche Bundesbank. See also the Statistical Annex.

Geographic and Sectoral Distribution of German FDI in Latin America

Main recipient countries

German investors' preference for Latin America has been accompanied by a tendency for them to focus on just a few countries in the region.[4] Both in 1985 and in 1995, Argentina, Brazil and Mexico alone accounted for more than 90% of German FDI stock in the region (excluding the offshore centres); in comparison, it is interesting to note that these three countries are the destination of only some 75% of all foreign investment in Latin America.

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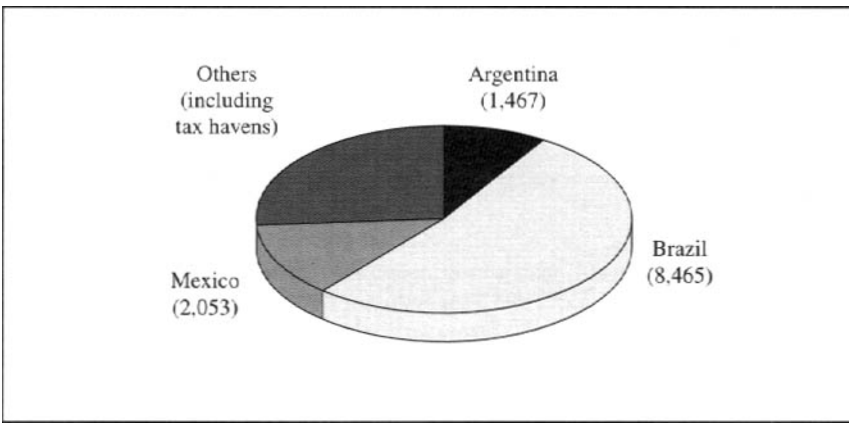
Brazil is the single most important destination in the region for foreign investment from all investor countries, but the concentration of German FDI there is even more pronounced. Despite the relative shift in FDI stock from Brazil to Mexico since 1985, in 1995 there was still four times more German investment in Brazil than in Mexico, which is the second largest recipient of German FDI in the region.[5] Even in per capita terms, in 1995 the stock of German FDI was higher in Brazil (followed by Argentina, Chile and Mexico) than in any other Latin American country. In contrast, it is interesting to note that the smaller countries (Chile and Costa Rica) where among the first in terms of per capita FDI stock from the investor countries as a whole, while Brazil ranked fifth in this respect.

The data on FDI flows reveal that German investors have continued to show a marked preference for Brazil, which absorbed more than 66% of German flows to Latin America between 1993 and 1996. At the same time, the data on flows do not suggest that Mexico is attracting a larger share of German investment in the region. In fact, Mexico's share of accumulated flows of German FDI dropped to around 3% during the same period.

Graph 5
Distribution of German FDI Stocks in Selected Countries, 1995
(in millions of US$)



Sources: See Statistical Annex.

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In 1995, apart from the three main recipients of German FDI in Latin America, only Chile and Colombia accounted for a significant share of German FDI stock in the region. In per capita terms, however, the German presence in Colombia was relatively weak in comparison to that of the other important investor countries. Equally, Chile attracted a smaller proportion of German investment than of all foreign investment. In the same year, the other countries in the region accounted for a very small proportion of German FDI. Moreover, most of them saw their relative shares drop between 1985 and 1995, and this despite the ongoing integration of sub-regional markets. This would seem to suggest that, until now at least, regional integration in Latin America has not had a significant impact on the smaller economies' capacity to attract German FDI.

Sectoral distribution

German FDI in Latin America is not only concentrated in just a few recipient countries, but also in a small number of sectors; although European FDI as a whole has tended to concentrate in manufacturing industry, this pattern is even more evident in the case of German investment (see Table 2):

- In 1995, despite the relative decline registered since 1985, manufacturing industry still accounted for two-thirds of German FDI stock in Latin America.

- The concentration of German investment in manufacturing was most pronounced in the three main recipient countries.

- While manufacturing industry's share of German FDI stock in the region has fallen, this decrease is much less significant than for foreign investment as a whole; in 1995, for example, the service sector in Mexico accounted for 45% of all FDI stock, but less than 10% of German stock.[6]

Equally, German FDI has been concentrated in just a few manufacturing industries. Both in 1985 and 1995 four industries accounted for more than 80% of German FDI stock in manufacturing in Latin America (see Table 2). In the case of Mexico, the combined share of chemicals and transport equipment rose from 69% in 1985 to 76% in 1995. In Argentina and Brazil, the proportion of German investment in these two industries was consistently higher than in the case of foreign investment as a whole.

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The lower level of geographic, sectoral, and industrial diversification of German FDI in Latin America, suggests that German investors have adopted different strategies in the region to those followed by companies from other countries.

Table 2
Sectoral Breakdown of German FDI in Latin America[1] in 1985 and 1995
(in percentages)

	Manufacturing (total %)		Main industries (percentage of manufacturing sector)							
			Chemical products		Electric equipment		Machinery		Transport equipment	
	1985	1995	1985	1995	1985	1995	1985	1995	1985	1995
Latin America	71.8	66.6	29.4	29.8	15.4	15.2	10.8	10.7	25.6	27.5
Argentina	80.5	75.7	35.8 (22.4)	37.8 (24.3)[2]	14.8	12.4	7.4	0.7	23.6 (21.5)	28.3 (29.6)[a]
Brazil	91.3 (74.7)	86.2 (58.1)[3]	22.5 (23.7)	21.0 (24.9)[3]	16.0	17.4	12.9	15.8	28.4 (18.5)	27.5 (19.1)[3]
Mexico	88.1 (77.8)	90.0 (53.5)	48.9	36.1	14.9	10.9	3.8	0.9	20.3	40.1

Source: Compiled by the author from data from Deutsche Bundesbank; see also the Statistical Annex.
1. In brackets: equivalent share of FDI stock of all investor countries, when it exists.
2. 1992.
3. 1993.

The Strategy of German Companies in Latin America

Different internationalization strategies

Before examining the main determinants of German FDI in Latin America, it should be noted that FDI has not been German companies' preferred mechanism of internationalization. The predominance of exports over FDI in all large investor countries is more accentuated in the case of Germany (see Table 3). The

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coefficient of FDI/exports was two to three times higher in the case of the United States, France, Japan and the United Kingdom than in that of Germany. For all the industrialized countries, except France, internationalization through FDI was a more significant element of their economic relations with Latin America than with the rest of the world. The higher FDI/exports coefficient in the case of Latin America is probably due to the existence of import restrictions which have limited opportunities for foreign companies to implement internationalization strategies via exports to the region. However, it is surprising that German companies lagged so far behind their main competitors in the use of FDI as a means of expanding in Latin America.

The marked preference for exports over FDI, which is a characteristic of the strategy followed by German companies, may have undermined their capacity to respond to the new investment opportunities in Latin America. Their preference for exports also suggests that the relocation of manufacturing operations in Latin America has been a secondary consideration for German companies. And this, in turn, provides further, indirect evidence that FDI in Latin America should have less impact (if any) on the labour market in Germany than that in the United States, Japan or the United Kingdom.

Table 3
FDI/Exports Coefficient of Main Investor Countries[1], 1985-95
(in percentages)

	Latin America	World
Germany	8.4	4.8
France	3.8[2]	9.6
Japan	42.5[2]	8.2
United Kingdom	63.7[2]	15.5
USA	20.4[2]	10.0

Sources: Compiled by the author from data from Deutsche Bundesbank; OECD (1996); IMF (1996); UN (various editions).
1. Accumulated global FDI flows to Latin America in relation to accumulated global exports to Latin America.
2. 1985-94

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Determinants of German FDI

An analysis of the determinants of German FDI[7] also challenges the widely held view that FDI has been a major contributing factor to the problems in the German labour market. Negative consequences could be expected for low-skilled German workers if FDI essentially involved the relocation of relatively standardized and labour-intensive production lines, in which case cost factors would be more important than market motives as stimuli for FDI. In practice, however, the opposite is true of German FDI. Above all in Latin America, German companies invest in order to gain access to the large, and often protected markets in the recipient countries. Cost factors seem to be of secondary importance. This interpretation is confirmed by a number of findings:

- First, German FDI in Latin America has consistently been concentrated in chemicals, electrical equipment, machinery, and transport equipment. In all these sectors, the evolution of German employment levels has been relatively favourable in comparison with the average variations in employment in manufacturing industry as a whole between 1980 and 1994.

- German FDI in Latin America also seems to be relatively capital intensive. In the absence of other more satisfactory data, the ratio of employees to sales may be used as an indicator of the comparative intensity of the factors of production of German and US FDI in different regions (see Table 4). According to this indicator, US FDI in Latin America is slightly more labour intensive than German investment in the region.[8] Moreover, German FDI in Central and Eastern Europe, as well as in the developing countries in Asia, is more labour intensive than in Latin America. This suggests that international differences in labour costs have been a less important determinant of German FDI in Latin America.

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Table 4
Size and Labour Intensity of German and US Companies in Latin America[1]
(averages)

	Latin America	Argentina	Brazil	Chile	Mexico	Asiatic DCs[2]	Econ. in trans.[3]
Sales by company							
- Germany[4]	126	111	211	39	107	57	39
- USA[5]	61	..	..	..	..	52[6]	..
Employees by company							
- Germany[4]	232	154	403	81	209	120	139
- USA[7]	135	..	217	..	296	99	..
Employees/sales							
- Germany[4]	185	141	193	207	196	215	363
- USA[8]	205	138	190	163	283	128	..

Sources: Based on data from Deutsche Bundesbank; US Department of Commerce.
1. In all indicators German or US FDI worldwide has been assigned a value of 100. The proxy variable for labour intensity is the ratio of employees to sales.
2. Except China in the case of German FDI.
3. Including China.
4. 1995.
5. Acquisitions and establishment of non-banking subsidiaries in 1994.
6. Including Australia, Japan and New Zealand.
7. 1993; non-banking subsidiaries.
8. 1991; non-banking subsidiaries.

- Third, the essentially market-oriented character of German investment in the region is confirmed by a simple correlation analysis. As in the case of other investor countries, the stock of German FDI (per inhabitant of the recipient country) is generally higher in the Latin American economies with relatively high levels of per capita incomes. However, in contrast to total FDI in the region, German investment is highly concentrated, even in terms of per capita FDI stock. The correlation between per capita FDI stock and the size of the population of the recipient Latin American countries was insignificant for foreign investors as a whole, but very strong (and positive) in the case of German investment.

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Box 1: Determinants of FDI and its Impact on Employment in Germany

A number of company surveys and econometric analyses have shown that German FDI essentially responds to market-related factors. Two-thirds of the German companies analyzed in 1995 stated that they had invested abroad in order to take advantage of new markets. More than half identified the desire to consolidate their position in traditional markets and to participate in the growth of the recipient economy as two of the main incentives for FDI. There was also found to be a strong positive correlation between German investments and exports to recipient countries, which means that investments and exports tend to be complementary elements of companies' internationalization strategies. The substitution of FDI by exports seems to be the exception rather than the rule.

These same studies found that cost-related factors have played a secondary role in FDI, although their importance has increased over the last few years. According to some experts, a 1% real appreciation in the value of the German mark – indicating a decline in the international competitiveness (in terms of prices) of the German economy – is associated with a 2.5% rise in outflows of German FDI. According to these studies, small- and medium-sized German companies have increasingly resorted to FDI as a means of cutting production costs, above all by relocating labour-intensive production to Central and Eastern Europe.

However, the theory that German FDI has a negative effect on employment can be refuted by examining the correlation between the stock of FDI (as a percentage of all German capital assets) and the variation in employment in the manufacturing sector in Germany during the period 1980-94. If FDI was mainly driven by cost factors, job losses would be concentrated in those industries that invested most heavily abroad. Significantly, however, the employment figures in almost all manufacturing industries with significant levels of FDI were comparatively good. These industries include chemicals, electrical equipment, machinery and the transport equipment sector, precisely the most important destinations for German FDI in Latin America.

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Box 2: German Automobile Companies in Latin America

There a number of similarities between the international operations of the main German automobile companies and the overall pattern of German FDI. First, in both cases, the main location is Latin America, which accounts for nearly 66% of Volkswagen car production in non-OECD countries. The proportion of Volkswagen and Mercedes-Benz lorries and buses produced in Latin America is even higher (85%). Second, vehicle production is also concentrated in just a few countries. Argentina, Brazil and Mexico account for the bulk of the output of both Volkswagen and Mercedes-Benz in the region. In 1995, almost 70% of the total Latin American production of these companies took place in Brazil. Third, the main incentive for these companies' investments has been to supply the local, protected markets.

Import restrictions made it less profitable to export finished vehicles to Latin America and also meant that it was difficult to supply affiliates in the region with competitively priced components and spare parts. This reduced the international competitiveness of vehicle parts produced in Brazil. In this light, it is hardly surprising that the Latin American affiliates of German producers are not very tightly integrated into the global production and supply networks of their parent companies. German imports of parts made in Brazil and Mexico (measured in units produced by the German companies in these countries) were the equivalent of only a fraction of German imports of parts from Spain (see figures below). A similar, albeit less pronounced, pattern existed with respect to German exports of vehicle parts to Brazil, Mexico and Spain.

Trade of vehicle parts between Germany and a group of German FDI recipient countries, 1995

(US$ per unit produced by German companies in the respective recipient country)

	Brazil	Mexico	Spain
German imports of vehicles and parts	523	525	8,500
German exports of vehicles and parts	1,821	3,248	7,567

Source: VDA (1996).

A number of automobile producers, including Volkswagen and Mercedes-Benz, have announced ambitious plans to expand their FDI in Latin America. The largest project, the construction of a Volkswagen plant in Mexico for $1 billion, will enable the production of the "Beetle" to restart this year. Volkswagen is also investing $500

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million in the construction of a plant in San José dos Pinhais, in Paraná (Brazil), which will be completed in 1998 and should reach full production at the end of 1999. These two projects made Volkswagen the largest investor in the Latin American automobile industry last year. Two other projects confirm the increasingly strong German presence in the region: a new $750 million Audi-Volkswagen plant in Paraná and an engine plant for Chrysler (US) and BMW ($500 million).

Although it is likely that German automobile producers will continue to focus on the main economies in the region, investments now being made appear to suggest a change of tactic. Automobile producers are coordinating their strategies in Argentina and Brazil, and the development of MERCOSUR seems to be leading to a heightened division of labour at the sub-regional level. Volkswagen's new investment in bus and lorry production in Rosende seems to have radically changed the company's modular production methods in Brazil, in that the company has established very close relations with parts and components suppliers. Local investment conditions could play a decisive role in ensuring that Latin America becomes an integral part of German automobile manufacturers' global networks of production, thereby changing the traditional function of German FDI in the sector.

Response of German investors to new opportunities in Latin America

The limited diversification of German FDI in Latin America may explain why German companies have been relatively slow to take up the new investment opportunities in the region. It seems likely, for example, that German investors' preference for larger countries helps to explain their weak response to Chile's economic reforms. The traditional weight of investment in manufacturing industry may also have contributed to the low level of German investment in Chile, where the primary sector has been the destination for an increasing proportion of all FDI stock. Nor do differences in the rhythm of growth in the region appear to have had an immediate impact on German FDI. In 1995, and unlike in the case of FDI as a whole, the correlation between the per capita stock of German FDI and the average annual increase in per capita incomes in the Latin American recipient countries was insignificant.

German investors have also been slower than their counterparts in other investor countries to respond to the important investment opportunities created by the privatization programmes in many Latin American economies, above all in the service sector (telecommunications, transport, financial services and electricity supply). In countries like Argentina, Peru and

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Venezuela, the privatization programmes account for a large part of all foreign investment.Yet significantly, all these countries' relative share of German FDI stock actually shrank between 1985 and 1995, while their share of the total FDI stock of all the investor countries rose during the same period. Equally, German FDI flows to Brazil fell from just under $1.2 billion in 1995 to $157 million in 1996, precisely when Brazil's position as a recipient of European FDI was boosted by the sale of a large number of state-owned companies.[9]

These figures confirm that German investors have played a strictly secondary role in the privatization process in Latin America, not least in comparison to their counterparts in other investor countries. It is interesting to examine the explanation for their apparent lack of flexibility. An exogenous factor that is worth considering is the possibility that German investors suffer from competitive disadvantages with respect to the new opportunities in Latin America in comparison to US companies, which benefit from lower transaction costs because of their geographic proximity to, and institutional links with, some countries (especially Mexico). However, a number of factors suggest that the scant flexibility shown by German investors cannot be attributed to exogenous factors alone:

- Latin American countries do not discriminate against FDI from countries other than the United States. Indeed, some of them are particularly interested in diversifying their FDI sources in order to reduce the predominance of US investors.

- For a number of years, German FDI has grown more slowly than US and even Japanese investment, and the latter at least could hardly have benefitted from lower transaction costs (see Graph 2).

- A number of investors from other European countries have successfully taken advantage of the privatization process in the region.

Hence the lack of flexibility shown by German investors appears to be a consequence of specifically German factors. On the one hand, and regardless of the structural features of German FDI, the central role that exports play in German companies' internationalization strategies may have limited their capacity to seize new opportunities for investment. The emphasis traditionally placed on exports certainly appears to have affected German participation in the expansion of the non-tradable sector of the Latin American economies.[10]

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At the same time, several branches of the service sector in Germany are still highly regulated or in the hands of inefficient public companies. This may mean that few German companies are capable of putting in tenders for state-owned companies in Latin America. Finally, the scale of German FDI projects in Latin America is quite large in comparison to those of US companies in the region as well as German companies in other developing regions (see Table 4). This means that a few big companies dominate German investment in Latin America. The scant presence of small- and medium-sized companies could have also reduced the capacity of German investors as a whole to exploit the new opportunities existing in the region.

Conclusions and Prospects

The pattern of German FDI in Latin America differs from that of other countries, as well as from German investments in other developing regions. These differences are significant both for Germany itself and the Latin American recipient countries. With respect to Germany, one important conclusion is that FDI flows to Latin America could hardly have contributed to the country's employment problems. In fact, it would be interesting to know why German investors have taken less advantage than their competitors of the new opportunities in Latin America, as this may not only inhibit the development of investment relations, but also, in the long term, trade relations too. The empirical evidence suggests that, generally speaking, FDI and exports are complementary forms of international trade and production. If the trend towards the liberalization of foreign trade and the deregulation of FDI continues, they will become increasingly complementary, rather than alternative, elements of companies' internationalization strategies.

The concerns of Latin American countries regarding a possible diversion of FDI to other developing regions appear equally unfounded. There is little evidence that the exceptional interest German companies have shown in investing in Central and Eastern Europe has had a significant impact on German FDI in Latin America. Instead, it seems that German investments in different regions complement each other, and reflect different strategies. However, it should be noted that the pattern of German FDI in the past is no guarantee for the future in the context of changes in Latin America and the world.

On the other hand, it is reasonably likely that German investment in the region will focus less on local markets in the future. The current trend towards globalized production and trade is changing the form and purpose of FDI.

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Increasingly, the geographic dispersion of production and the combination of markets and resources by means of investment and trade constitute key features of the world economy. This means that one of the traditional determinants of FDI has lost much of its importance: the scale of national markets. At the same time, differences in costs at the local level, the quality of the infrastructure, the facilities provided for businesses, and the availability of skills and human capital have become more important factors. Although the response of transnational corporations (TNCs) in different countries to the changing international environment will vary in both degree and speed, sooner or later German FDI will be affected if strategies shift from the search for markets to the search for efficiency, as seems to be already occurring in some sectors (e.g. the automobile industry).

More specifically, trade liberalization has weakened the role of FDI as a mechanism to overcome import restrictions. This poses a critical dilemma for Latin America, where traditionally FDI was drawn in by the prospects of market access rather than efficiency. In the long term, the move towards trade liberalization and the deregulation of FDI will encourage the integration of the Latin American economies into the TNCs' global networks of production and trade, on the basis of specialization in accordance with different countries' comparative advantages. In the short term, however, the difficulties involved in integrating Latin America into companies' corporate strategies could make exports more attractive than FDI. This would affect German FDI, since German companies have a strong preference for exporting. Meanwhile, recent trade trends indicate that Latin America still suffers from a lack of international competitiveness in industries in which German investors have traditionally been most active. The revealed comparative advantage in 1994 was negative for the chemicals, machinery and transport equipment industries.[11]

In short, future investment relations between Germany and Latin America will depend on the ability of the recipient countries to improve their competitiveness in those industries with the highest levels of German investment. The revitalization of the regional integration processes could have mixed effects. On the one hand, it might result in a more efficient division of labour at the sub-regional level, and hence attract investment from companies with defined regional or sub-regional strategies. Regional integration, on the other hand, may not be sufficient to ensure continued inflows of German FDI, given that this investment is largely market-oriented and tends to converge on the largest and most advanced member states of regional organizations. Latin America's chances of attracting efficiency-oriented FDI may even decrease if regional integration takes place in a way that clearly discriminates against

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non-member countries. Opening up to world markets seems to be the most effective way of securing integration into global systems of trade and production.

NOTES

[1] For a recent analysis of FDI trends and investment conditions in Germany, see Nunnenkamp (1996), Klodt and Maurer (1996) and Jost (1997).

[2] Henceforth in this chapter, and unless otherwise stated, the term Latin America includes the Caribbean.

[3] Central and Eastern Europe are considered here to be part of the developing world.

[4] This section essentially refers to FDI stock. FDI inflows, particularly in the smaller recipient countries, tend to be volatile, and the details are often not released for reasons of confidentiality.

[5] The total FDI stock of all investor countries in Brazil was only 1.5 times higher than in Mexico.

[6] The sectoral breakdown of German FDI stock provided by Deutsche Bundesbank (1997a) is incomplete. In 1995, commerce (including maintenance and repairs), banks, other financial institutions and insurance companies accounted for 23% of the stock of German FDI in Latin America. In 1994, these service sectors' share of German FDI was 8.4% in Brazil and 4% in Mexico.

[7] See, for example, Klodt and Maurer (1996), Jost (1997), Deutsche Bundesbank (1997).

[8] However, it should be noted that this difference is solely due to the relatively labour-intensive character of US FDI in Mexico.

[9] There is no direct evidence for participation of German investors in the privatization process in Latin America. However, investors from other countries seem to have been the main players in the largest FDI projects within this process.

[10] The service sector generated 55% of Latin America's GDP in 1995. Between 1990 and 1995, the sector grew by a yearly average of 3.8%, while manufacturing industry expanded by only 2.5%. At the same time, the service sector's share of total FDI stock rose significantly in a number of Latin American countries.

[11] The revealed comparative advantage (RCA) is calculated in the following way: RCA $= (X_i - M_i) : (X_i + M_i)$, where X = exports, M = imports, *i* = manufacturing industries. The RCA can vary between -1 (no exports) and 1 (no imports). In 1994, the RCA was - 0.41 for chemicals and - 0.35 for machinery and transport equipment (calculated on the basis of United Nations' figures, several editions). The RCA was also negative (0.13) for cars, although the imports in this sub-sector of the machinery and transport equipment industries were subject to severe restrictions in a number of Latin American countries.

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CHAPTER VI

UNITED KINGDOM*

Introduction

The importance of the United Kingdom as a foreign investor in Latin America and the Caribbean can only be understood in the context of the country's traditionally very prominent role as a source of FDI worldwide. Although its position as an economic power has steadily declined over the course of the century, the United Kingdom is still one of the most important international investors. Between 1971 and 1995 it was the second largest source of FDI outflows in the world. The United States held first place for most of this period, but in the 1980s it was overtaken by both Japan and, once again, the United Kingdom (see Table 1). Equally, the United Kingdom has consistently ranked second in the league table of FDI recipient countries, outmatched only by the United States. In terms of foreign investment, therefore, it is probably the most internationalized economy in the world.

Since FDI outflows from the United Kingdom have generally been larger than the inflows, the book value of British assets held abroad is higher than that of the assets of foreign registered companies in the United Kingdom. After peaking at $43.6 billion in 1995, British FDI dropped slightly to $34.4 billion in 1996. At the end of 1996, the total stock amounted to almost $355 billion. Inflows, in turn, reached $25 billion in 1996, close to the previous high in 1990. The total stock of foreign investment in the United Kingdom was $237.7 billion, well below the level of British capital invested abroad. This is the general context in which FDI in Latin America and the Caribbean should be analyzed.

* This chapter was written by Peter J. West, Chief Economist, BBV Securities, London. The author would like to thank María Caro for her help with the chapter.

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Table 1
FDI Flows of the Main OECD Countries, yearly averages

	Outflows			Inflows		
	Billions of US$			Billions of US$		
	1971-80	1981-90	1991-95	1971-80	1981-90	1991-95
USA	13.4	17.6	60.5	5.6	36.5	42.0
United Kingdom	5.5	18.6	25.3	4.6	13.0	17.3
Japan	1.8	18.6	20.4	0.1	0.3	1.0
Germany	2.5	9.0	22.0	1.4	1.8	3.6
France	1.4	8.6	14.7	1.7	4.3	12.6
TOTAL	24.6	72.3	142.9	13.4	56.0	76.5
	% of the total			% of the total		
USA	54.5	24.3	42.3	42.0	65.2	54.8
United Kingdom	22.4	25.7	17.7	33.9	23.3	22.6
Japan	7.3	25.7	14.3	1.1	0.6	1.3
Germany	10.1	12.5	15.4	10.4	3.2	4.8
France	5.7	11.8	10.3	12.6	7.7	16.5
TOTAL	100.0	100.0	100.0	100.0	100.0	100.0

Source: OECD, *International Direct Investment Statistics Yearbook 1996*, Paris (1997).

Historical Background

Before the First World War, the United Kingdom was the single largest source of foreign capital in Latin America, both in the form of bonds and FDI. It has been estimated that the total stock of FDI in the region in 1914 was $7.6 billion, 47.4% of which was held by British companies.[1] Investment was concentrated in the railways, a sector which accounted for 46% of all British FDI in Latin America, followed by public utilities (15%). The outbreak of the First World War in 1914, however, triggered a decline in the flow of capital from the United Kingdom to Latin America. Although direct investment picked up after the war, it did not return to pre-1914 levels. As a result, the United States became the main source of foreign capital in the region. The Second World War only accentuated the further decline in the position of the United Kingdom.

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After the Second World War, a number of Latin American governments nationalized companies in sectors in which British companies were still very prominent. The best known operation of this type took place in 1948, when the Argentine government paid no less than $600 for the British interests in the country's railway system.[2] This policy of nationalization helps explain why for most of the post-war period Latin America was not a priority area for British FDI, even though the United Kingdom's pre-eminent position in global direct investment meant that it remained an important investor in Latin America. In recent years, however, there have been clear signs that this situation is changing. Following the radical structural reforms and liberalization programmes carried out in most of Latin America since the mid-1980s, British investors have begun to show a renewed interest in the region. This suggests that British companies will play a more active role in the future development of Latin America.

Recent UK FDI in Latin America

For the past 25 years or more, the United Kingdom has consistently been the second largest source of foreign investment flows worldwide. Its share of the accumulated FDI stock in Latin America, however, has been somewhat lower. Indeed, according to the available figures (which, while not always very up-to-date, probably offer an accurate picture of the overall situation) the United Kingdom's share of FDI in some countries in the region is in fact relatively small (see Table 2). Nonetheless, in almost all cases, the United Kingdom ranks among the main investor countries: it is the second most important investor in three of the eight largest Latin American countries, the third in another three, and the fourth in one. Equally, in the mid-1990s, the United Kingdom was still the third largest investor in Brazil (with 9% of the total stock), the largest economy in the region. Argentina is the country in which the United Kingdom occupies the lowest position in the ranking of investor countries, although even here it accounts for 5% of the total FDI stock. Moreover, these figures refer to the situation in 1994, and probably still reflect the impact of the Falklands/Malvinas War on British investment in Argentina. Following recent major investments in sectors such as gas distribution and banking, the United Kingdom now probably holds a larger share of FDI stock in Argentina.

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Table 2
UK FDI in Latin America
(position and percentage of total)

	Year	Position	% of the total
Argentina	1994	8	4.9
Brazil	1994	3	9.0
Chile	1996	4	5.2
Colombia	1995	2	4.3
Ecuador	1994	2	4.5
Mexico	1995	2	6.7
Peru	1997	3	13.5
Venezuela	1994	3	4.9

Sources: IDB-IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid (1996); Secretaría de Programación Económica del Ministerio de Economía, *Inversión Extranjera Directa en Argentina 1992-1995*, Buenos Aires (1996); Comité de Inversiones Extranjera, *Informe Anual 1996*, Santiago de Chile (1997).

Although, from a Latin American perspective, the United Kingdom's position as a major international investor makes its participation in FDI in the region significant, from the perspective of the investor countries the situation is rather different. Latin America accounts for a significantly lower proportion of all FDI from the United Kingdom than from the other large investor countries, such as Canada, the United States, Japan and most Western European countries, particularly Spain.[3] In fact, Latin America is only of less importance to France and Sweden than to the United Kingdom (Table 3).

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Table 3
Latin America's Share of FDI from Selected OECD Countries, 1994

	% of the total
USA	15.5
United Kingdom [1]	3.6
Japan	11.3
Germany	5.4
France	2.6
Switzerland	13.9
Canada	12.9
Italy	5.9
Sweden	0.0
Spain [2]	45.7

Sources: OECD, *International Direct Investment Statistics Yearbook 1996*, Paris (1997); United Kingdom: Office for National Statistics, *Business Monitor MA4 1995: Overseas Direct Investment*, London (1997); Spain: Banco Bilbao Vizcaya.

1. Figures for 1995, excluding offshore centres; when they are included in the figures, the United Kingdom's share rises to 8.4%.
2. Figures for 1996.

Table 4 presents a more detailed breakdown of UK FDI flows over the last few years. This shows that Latin America's share has risen slightly, from 2.4% of the total at the end of the 1980s to 3.7% in the period 1991-96. Among the developing regions, and above all more recently, Asia has benefitted most from the overseas expansion of British-registered companies. However, the developed countries continue to attract the bulk of British FDI. The figures also show that the European Union (EU) has replaced the United States as the main destination for FDI from the United Kingdom during the 1990s.

Given the recent revival in British interest in Latin America, however, the average figure for the 1990s is probably not an accurate indicator of the current situation. Despite the currency crisis in Mexico in 1994-95, there has been a major increase in UK investment in Latin America over the last few years. After falling to almost insignificant levels in 1991 and again in 1993, British FDI in the region grew strongly over the following three years (see Table 5). In 1996, the last year for which official figures are available, Latin America attracted nearly 7% of all British FDI. These figures are by far the highest in the period analyzed

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here. Moreover, as noted below, new, major investments were announced in 1997, suggesting that this resurgence in British investment in the region has continued.

Table 4
FDI Flows from British Companies, by Region
(percentage of the total)

	1985-90	1991-96
Developed countries	88.0	82.1
USA	49.5	26.4
EU	25.4	42.5
Other	13.1	13.2
Developing countries	12.0	18.0
Africa	1.6	1.4
Asia	2.9	8.3
Latin America	2.4	3.7
Offshore centres	3.7	2.0
Other	1.4	2.6

Sources: Office for National Statistics, *Business Monitor MA4 1995, Overseas Direct Investment*, London (1997); *First Release Overseas Direct Investment* 1996, London (1997).

These trends in British FDI in Latin America are explained by a number of factors, some of which are specifically domestic developments, while others are related to the evolution of the situation in Latin America itself. As one would expect from a country with such a high level of foreign investment, British investors have always taken an interest in Latin America, regardless of the ups and downs in the region's economy. Some large companies that have been operating there for many years have maintained their commitment to it during prolonged periods of economic and political turbulence in many countries. However, despite these historical links and the dominant position of British FDI at the beginning of the century, for most of the post-war period Latin America has not been a favourite area for new investments, even in terms of the developing countries. In fact, Latin America became a region in which only specialist investors with established relations maintained an active interest.

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This reluctance to invest in the region is a consequence of historical and cultural factors, as well as purely economic and financial considerations. On the one hand, UK companies have understandably been drawn to the developed markets, especially the English-speaking countries (the United States and Canada) and the United Kingdom's EU partners. In the developing world, on the other hand, the greater British interest in Asia is explained by a number of factors. Apart from its better economic performance (until recently at least), Asia was seen as being geographically closer, and also benefitted from the existence of strong links dating back to the days of the British Empire. Given its generally weak economic development, Africa has also attracted a disproportionate share of UK FDI. Again, this is probably best explained by the United Kingdom's strong historical and cultural ties with the region. In the case of Latin America, in the light of the prolonged economic and political instability in the region, combined with the fact that, until recently, many countries actively rejected foreign investment, it is hardly surprising that many potential UK investors avoided the region.

Table 5
Evolution of FDI Flows of British Companies, by year
(in millions of US$ and percentages)

	Total	Latin America[1]	% of the total	Offshore centres[2]	Latin America[3]	Percentage of the total
1985	11,181	327	2.9	454	780	7.0
1986	17,308	540	3.1	483	1,022	5.9
1987	31,400	834	2.7	1,319	2,154	6.9
1988	37,260	837	2.7	1,124	1,961	5.3
1989	35,239	494	0.4	687	1,181	3.4
1990	18,040	493	3.0	1,497	2,213	12.3
1991	16,462	69	0.4	-409	136	0.8
1992	17,844	542	3.0	1,414	2,528	14.2
1993	26,073	222	0.9	777	1,032	4.0
1994	32,225	1,365	4.2	1,205	2,942	9.1
1995	43,573	1,645	3.8	393	1,799	4.1
1996	34,379	2,968	5.7	425	2,399	7.0

Sources: Office of National Statistics, *Business Monitor MA4 1995; Overseas Direct Investment*, London (1997); *First Release: Overseas Direct Investment 1996*, London (1997); data provided directly by the Office for National Statistics.

1 Excludes offshore centres.
2 Offshore centres and other flows/countries (see Statistical Annex).
3 Includes other countries.

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Following the so-called "lost decade" of the 1980s, the implementation of radical market reforms and rigorous financial policies has led to a major improvement in the macroeconomic data and prospects for Latin America. At first, British companies proved slow to react to the profound transformation of the region's economies. This may have reflected the continued influence of the region's negative image mentioned above, which meant that investors were more impressed by the upheavals of the past than the good prospects for the region in the present. On the other hand, some investors were still shaken by their experience in the 1980s when, attracted by the brief economic revival, they had invested in the region, only to suffer the full consequences of the debt crisis and the subsequent period of paralysis and macroeconomic instability. This helps account for their reluctance to increase their investments, and their initially cautious response to the new economic climate in the region. This situation seems to be changing today. The recent growth in funds channelled by UK companies into new and existing operations in Latin America suggests that their investment strategies are conditioned by their growing awareness of the prospects for expansion in the region.

Based on the latest available data, Table 6 gives a detailed country-by-country breakdown of UK FDI stock in Latin America in 1996. This shows that Brazil absorbed the largest share of British investment in Latin America, as befits its position as the largest economy in the region. It was followed by Colombia and Chile, which relegated Mexico and Argentina (the second and third largest economies) to fourth and fifth places respectively.

Table 6
British FDI Stock by Main Recipient Countries, 1996
(in millions of US$ and as percentage of total)

	Millions of US$	%
Argentina	813	7.7
Brazil	4,107	39.0
Chile	1,138	10.8
Colombia	2,163	20.5
Jamaica	598	5.7
Mexico	941	8.9
Venezuela	319	3.0
Other	462	4.4
Total Latin America	10,541	100.0

Source: Office for National Statistics

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The overall distribution of British FDI between the manufacturing industry and non- manufacturing sectors is similar in Latin America to the rest of the world. However, some interesting differences can be seen within the general pattern at the end of 1995. In manufacturing industry, the proportion of UK investment in the chemicals industry was substantially higher in Latin America than in the rest of the world. The same was true of the food, beverages and tobacco industries. In contrast, the paper industry and mechanical and electrical engineering accounted for a smaller share of UK industrial investment in Latin America than in other regions.

Table 7
Stocks of British FDI in Latin America by country and sector, 1996
(in millions of US$)

	Argentina	Brazil	Chile	Colombia	Mexico	Jamaica	Venezuela
Manufacturing sector	661	2,669	761	97	710	7	153
Metals	—	—	—	—	..	—	—
Chemical products	302	681	105	53	34		48
Mechanical machinery	..	53	—	—	2		—
Electric machinery	..	31	..	..	12		..
Transport	7	105	0	7	25		..
Food, beverages and tobacco	204	914	126	19	312		90
Paper	—	14	..	—	..		—
Other	106	873	528	..	14		..
Non Manufacturing sector	153	1,440	377	2,066	231	591	165
Agriculture	—	..	..	—	—		—
Energy	..	1,071	205	2,005	12		..
Construction	—	..	..	—	..		..
Distribution	17	102	24	..	192		19
Transport	—	..	..	..	..		—
Financial services	42	248	17	..	..		..
Other services	58	15	0	5	8		2
All sectors	813	4,107	1,138	2,163	941	598	319

Sources: Office for National Statistics

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The differences in the composition of investment outside manufacturing industry are much more pronounced. At the end of 1996, the energy sector accounted for a much larger share of British FDI in Latin America than in other recipient regions. In contrast, the financial sector and other services, accounted for a much smaller proportion of the total. This probably reflects the effective prohibition on the entry of foreign banks that existed in many Latin American countries in the past. This situation is likely to change in the future, since many of these barriers to investment have been removed over the last few years within the general context of economic liberalization, but also because the financial crises made fresh injections of capital essential. British banks have been among the first financial foreign institutions to enter the Latin American banking market, seizing the opportunities created by these developments.

Table 8
Net Book Value of British FDI Stock by Sector, 1996
(in millions of US$ and percentages)

	Latin America		World total	
	millions of US$	%	millions of US$	%
Manufacturing sector	5,208	47.1	153,261	43.2
Metals	—	—	2,165	0.6
Chemical products	1,616	14.6	40,013	11.3
Mechanical machinery	56	0.5	8,290	2.3
Electric machinery	85	0.8	12,918	3.6
Transport	148	1.3	7,062	2.0
Food, beverages and tobacco	1,722	15.6	37,789	10.6
Paper	15	0.1	14,574	4.1
Other	1,566	14.1	30,450	8.6
Non Manufacturing sector	5,856	52.9	201,819	56.8
Agriculture	..	—	694	0.2
Energy	3,532	31.9	45,135	12.7
Construction	..	—	5,534	1.6
Distribution	355	3.2	18,698	5.3
Transport	1,355	12.2	5,150	1.5
Financial services	447	4.0	58,263	16.4
Other services	124	1.1	68,345	19.2
All sectors	11,064	100.0	355,081	100.0

Source: Office for National Statistics

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Some recent British investments

Although the official British figures for 1997 are not yet available, when published they will probably show that the upward trend that started in 1994 has continued, as a large number of, in some cases quite considerable new investments have recently been announced. Table 9 gives details of some of the most significant investments made by UK companies in Latin America since the end of 1996. The list essentially refers to acquisitions and, while not exhaustive, does give a general idea of the most recent trends in investment.

Even if not all the planned investments announced are actually made in the immediate future, there can be no doubt as to the notable increase in interest in Latin America among British investors. The financial sector stands out, above all as a result of the series of acquisitions of Latin American banks by the London-based group, HSBC.[4] This confirms the prospects for increased British investment in the financial sector as a whole noted above. Another important destination for investment is the food industry. Here, Unilever's acquisition of the largest ice-cream producer in Brazil constitutes the most important single investment by the Anglo-Dutch corporation outside Europe and the United States. This operation represents a decisive step forward in Unilever's strategy of expansion into Latin America, which included the acquisition of the second largest Argentine ice-cream company in 1997.[5]

These investments are clearly intended to enable these corporations to benefit from the new economic situation in Latin America and the anticipated expansion of the regional markets. In the case of both HSBC and Unilever, their investment strategies appear to be guided by the better prospects for sales growth in Latin America than in their traditional, maturer markets. This, at least, is the conclusion to be drawn from the explanation the companies themselves have given for these investments. Sir Willie Purves, chairman of the HSBC Group, considers that Asia and Latin America offer the bank the greatest potential for growth, while neither Europe nor the United States are attractive regions for acquisitions: "we see Europe and the United States as mature markets. It is not very easy to see how we will be able to increase the shareholders' capital with the prices in these markets".[6] Unilever chairman Niall Fitzgerald echoed this argument when explaining the company's recent acquisition in Brazil; this, he maintained "opens up good opportunities for growth, that will lead to a sustained increase in the value of these assets". This point was confirmed by the president of Unilever's Latin American operation, who described the region as an area of high growth potential for the company.[7]

Until now, direct British involvement in the privatization programmes in Latin America has been limited compared with that of other industrialized

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nations. Nevertheless, some British companies have made major investments in former state-owned assets. These include the stake British Gas acquired in one of the natural gas distributors in Buenos Aires, and the acquisition by Cable and Wireless of a majority stake in the Panamanian telecommunications operator. Anglian Water has also acquired part of the equity capital of the state-owned water company, Aguas Argentinas, while Shell took a significant stake in the gas and oil transport division of Yacimientos Petrolíferos Bolivianos.

Table 9
Some Recent British Investments in Latin America

Company	Date	Country	Investment	Value (US$m)	Sector
HSBC	Mar 97	Brazil	Banco Amerindus	1,000	Commercial bank
HSBC	Mar 97	Argentina	Control of Banco Roberts	600	Commercial bank
Cable & Wireless	May 97	Panama	49% of INTEL	652	Telecoms
British and American Tobacco	Jul 97	Mexico	La Cigarrera tobacco company	712	Tobacco
Lasmo	Jul 97	Venezuela	Oil concession	450	Oil
BBA Group	Nov 97	Brazil	Bidim	40	Non-yarn textiles
Robert Fleming	Nov 97	Brazil	100% of Banco Graphus	n.a.	Investment bank
Unilever[1]	Nov 97	Brazil	Kibon	930	Ice cream
Royal & Sun Alliance	Nov 97	Chile	40% of Insurance Company La Construcción	128	Insurance
Standard Chartered	Nov 97	Colombia, Peru, Venezuela	67.3% of Extebandes	165	Foreign trade bank
Inchcape	Nov 97	Peru	Majority stake in Coca-Cola bottling plant	65	Drinks
Lucas Varity	Jan 98	Brazil	66% of Freios Varga Varga	115	Autoparts
HSBC	Jan 98	Mexico	19.9% of Grupo Financiero Serfin	145	Commercial bank

Sources: Compiled by the author on the basis of information from the *Financial Times*, Reuters, and Bloomberg.
1. A mixed Anglo-Dutch company

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Generally speaking, however, British investors have not been the most active in acquiring state-owned assets in the region. Significantly, for example, British companies have been virtually absent from the massive programme of privatizations in Brazil, in which their only major investment has been Shell's acquisition of a 20% stake in the São Paulo gas distribution company, Comgas. This is surprising in light of the fact that the United Kingdom pioneered the sale of state-owned companies to private investors in the 1980s. The explanation for British companies' scant involvement in the privatization process in Latin America is not that the recently privatized state companies and manufacturing companies in the United Kingdom have concentrated exclusively on restructuring their domestic operations, but rather that their international expansion has been focused on other regions. National Power, the largest electricity generating company in the United Kingdom, for example, is involved in projects in Australia, China, the United States, Indonesia, Pakistan, the Czech Republic and Turkey. As in the case of other UK companies, Latin America has simply not been a priority for the foreign operations of this new privatized company.

Box 1: A Study of British investment

In a report on competitiveness presented in 1994, the British government commissioned a study of foreign investment by British companies in order to identify forms of support, given their corporate strategies. The result was the *Competitiveness White Paper: Study on Outward Investment Final Report*, published by the Department of Trade and Industry in 1996.

The study was based on an analysis of the results of a questionnaire circulated to 900 companies, proportionately divided between small, medium and large companies. Most companies declared that most of their investments were concentrated in Western Europe. A larger proportion of major corporations had investments in non-OECD countries, including those in Latin America. Of the companies surveyed which had trade or investment relations with non-OECD countries, 36% had interests in Latin America. Most companies said the main reason for investing abroad was to exploit market potential (this was the case of 41% of the manufacturing companies), 27% to penetrate a new market and 11% to establish a regional base, while only 3% identified lower costs or greater profitability as the main reason for their FDI. Nonetheless, once a company has decided to invest in a given region, lower costs were mentioned as a key factor when choosing between different countries.

This report suggests that companies manufacturing high-tech products invest abroad in order to exploit or internalize ownership or technological advantages. In the service sector, many companies invest abroad because their product is non-tradable, and

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hence must necessarily be generated in the local market. Equally, the investment strategies of service companies are often determined by the financial regulations existing in the recipient countries.

The report also revealed that both in OECD and non-OECD countries, FDI has a basically neutral, or slightly positive effect on employment levels in the United Kingdom. The report found that investment abroad, even in non-OECD countries, tends to increase production in the United Kingdom, thereby disproving the widely-held idea that companies transfer production from the United Kingdom to another country in order to obtain higher levels of productivity and take advantage of cheap resources. The largely positive results of FDI are explained by the fact that investments in marketing and sales also generate demand for goods produced in Britain. However, some of the largest companies in the service sector did report reduced employment in the UK; in these sectors, foreign investment is less likely to generate demand in the country of origin since investments in services tend to be more self-sufficient.

There are signs, however, that some privatized British companies are beginning to take an interest in the final stages of privatization process in Latin America. They have left it rather late, however, since most countries are now reaching the end of this process. Nonetheless, some opportunities do still exist, above all in Brazil, where major privatizations in telecommunications and electricity generating will be carried out in 1998-99.

Prospects

A number of UK companies are currently engaged or planning to engage in major new investments in Latin America. In Brazil, now that the state oil company Petrobras has lost its 44-year old monopoly, both British Petroleum (BP) and Royal Dutch Shell plan to tender for concessions in the oil sector. In Peru, Shell has acquired almost a 58% stake in the huge Camisea oil field, which could require an investment of as much as $3 billion. Shell is waiting for final approval of plans to construct a $350 million pipeline in the south of the country. BP, in turn, has a strong presence in Venezuela, where the oil industry has been opened up to foreign investment as part of an ambitious expansion plan. At the same time, the independent producer Lasmo intends to invest $750 million in a project to develop the oil fields for which it obtained a concession in 1997.

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In the manufacturing sector, the automobile company Rover has announced that it will invest $150 million in Brazil to assemble its four-wheel drive Land Rover, following in the steps of its US, German and Japanese competitors who are already producing there. The retail giant Marks and Spencer plans to open a network of department stores throughout the region. National Power and one of its smaller competitors, PowerGen, intend to bid for some of the Brazilian power companies to be privatized in 1998-99.

Thus, although, there are still some obstacles to investment, there are good grounds to believe that the renewed interest shown by British investors in Latin America is not a passing phenomenon, but rather that it will intensify over the next few years. Although there may be occasional setbacks, on the whole the prospects for growth in the reformed economies in the region are very promising. In this light, and given the current economic difficulties in South East Asia, it seems more than likely that Latin America will improve its position with respect to the Asian countries as a destination for British companies seeking opportunities for growth in emerging markets.[8]

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NOTES

[1] ECLAC, *External Financing in Latin America*, New York: United Nations, 1965.

[2] Victor Bulmer-Thomas, *The Economic History of Latin America Since Independence*, Cambridge: Cambridge University Press, 1994.

[3] As a region, Latin America and the Caribbean account for a much larger share of all UK FDI if investments in offshore centres such as Bermuda and the Cayman Islands are taken into account. Often, however, inflows of capital registered in these offshore centres are destined for holding companies whose productive activities are carried out elsewhere. It is almost impossible to tell the final destination of such investments. Hence, they are not generally included in the analysis of FDI flows (as is the case in this book), since to do so would seriously distort the real scale of UK investment in Latin America.

[4] The HSBC Group developed from the Hong Kong and Shanghai Banking Corporation, which was founded in Hong Kong in 1865. In the early 1990s, HSBC acquired Midland Bank, one of the four UK clearing banks, and changed its country of registration to England. The Group's headquarters has been in London since 1993.

[5] John Willman, "Unilever Enjoys Growing Taste for Ice-Cream", *Financial Times*, 11 November 1997.

[6] G. Graham, "HSBC up 15% in First Half", *Financial Times*, 5 August 1997.

[7] LATAG, "Unilever in Major Ice-Cream Scoop", *Latin America Today*, November 1997.

[8] Julian Amey, Managing Director of Canning House, believes that UK companies can no longer base their strategy for the emerging economies on investment in Asia, as many of have done until now. See, Julian Amey, "Wounded Tigers", *Latin America Today*, September 1997. Some large UK investors share this view; during a speech delivered in London on 1 December 1997, Phil Watts, managing director of Shell, commented that "Latin America is becoming the new frontier; today we can see the potential of the Latin American pumas rather than of the Asian tigers".

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CHAPTER VII

FRANCE*

Introduction

"Until recently, little real interest was taken in events". This comment by the managing director of a French industrial group quoted in J.G. Berthommier's[1] report for the French Ministry of Economy and Finance faithfully reflects the hesitant response of French companies to the new business opportunities that have appeared in Latin America. Although France's strong historical ties with the region make Latin America a privileged area for expansion, in the early 1990s French companies in practice tended to concentrate on the rapidly growing economies of Asia, and on Eastern Europe, when considering new destinations for future investments. However, in 1996, when Asia was still seen as the most promising destination for investment, there was a major resurgence of interest in Latin America.[2] Does this flow of capital into the region, which is still too recent to be fully captured in the statistics, constitute a real change in the attitudes and strategies of French companies?

This chapter analyzes the place that Latin America occupies in the internationalization strategies of French companies. The data used here has been drawn from a number of different sources. The Banque de France records the flows of French foreign direct investment (FDI) in the balance of payments, and publishes annual figures for French FDI stock. The Department for Foreign Economic Relations (*Direction des Relations Economiques Extérieures,* DREE) of the Ministry of Economy and Finance also produces an annual survey of French foreign affiliates. Finally, in 1994 the Statistical Service of the Ministry of Industry (SESSI) compiled data on the level and nature of trade between affiliates within the same group as part of a study of the globalization of French companies. These different sources offer a complementary vision of the internationalization strategies currently being adopted by French companies.

The second part of this chapter provides a brief historical overview of French FDI in Latin America, along with aggregate data for the last two decades. These are accompanied by an examination of some of the main factors

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determining French investment in this period. The third part of this chapter offers a more detailed breakdown of investment patterns in the 1990s by sector and country. Particular attention is paid here to the impact that the structural reforms and processes of regional integration have had on French investment. The final section of this chapter examines the factors that have influenced this investment, and the role it plays in the regional and global strategies of French companies in a variety of economic sectors.

Factors Determining French FDI in Latin America

Taken as a whole, Latin America and the Caribbean[3] constitute the principal recipient region for French FDI in the developing world: in 1995, the region was the location for 39% of all French investment stock outside the Organization for Economic Cooperation and Development (OECD).[4] Most of these investments were not new. Indeed, the region has long been an important destination for French foreign investment, as a number of major companies have been active in Argentina and Brazil since before the Second World War. Yet Latin America represents a low proportion of global French FDI stock (accounting for just 4% of the total in 1995). Latin America began to lose ground in this respect at the end of the 1970s. For years after, the economic crisis affecting the countries in the region brought French investment virtually to a standstill. Even when the situation in the region improved in the early 1990s, French companies tended to look elsewhere when defining their foreign investment strategies. As a result, before the mid-1990s, the region rarely attracted more than 1% of all French FDI flows.

Table 1
French FDI Stock at the End of 1995

	Millions of US$	% of non OECD	% of total FDI
Latin America	7,346	39	4.0
Africa	4,692	25	2.5
Asian NICs	3,309	17	1.8
Eastern Europe	1,629	9	0.9
Non OECD countries	18,980	100	10.3
EU	100,963	—	55.0
World	184,380	—	100.0

Source: Banque de France.

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The situation has changed significantly during the last two years, however. In fact, the new investments made during this period appear to reflect a radical shift in the attitude of French companies towards Latin America. The massive increase in French investment in the region has been most spectacular in Brazil, which alone absorbed 3.6% of all flows of French FDI in 1996, and almost 10% of the total during the first ten months of 1997. This resurgence of French FDI in Latin America has also included Argentina, Mexico, and Colombia, and has gradually spread to the less economically developed countries in the region.

Table 2
French FDI Flows to Latin America

Years	Millions of US$
1980-1984 (annual average)	232
1985-1990 (annual average)	107
1990	283
1991	-14
1992	145
1993	332
1994	101
1995	59
1996	2,037
January-August 1997 (estimate)	1,500

Source: Banque de France.

Three main factors shaped the evolution of French FDI in Latin America in the period before 1995:

- The first was the "Eurocentric" orientation of French FDI: when this came to an end, capital which had previously been invested in OECD countries, and above all in Europe was released for investment in developing countries.

- The second was French companies' perception of, and reaction to, the changing political and economic situation in the region. In this respect, it should be noted that while a number of major disinvestment operations affected the balance of FDI flows, they did not affect the overall trend of flows to the region.

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- The third, and final factor was the impact of competition from the dynamic economies of Asia, and the economies in transition of Central and Eastern Europe, on the global location and nature of French direct investment.

Examination of these issues is followed by a brief analysis of the massive increase in French FDI in the region since 1996.

The impact of "Eurocentrism"

After a period of considerable uncertainty as to how best to respond to the challenge of globalization, in 1985 French companies embarked on a major programme of foreign investments. However, this was largely concentrated on the countries in the developed world and, with the consolidation of the Common Market, Europe in particular. As a result, in 1990, when this was still the predominant tendency, the OECD countries absorbed 97% of all French FDI flows. This period of "Europeanization" of flows substantially changed the geographic distribution of French FDI, so much so that only 8% of all French FDI stocks were located in developing countries in the early 1990s.

While the tendency for investment to be concentrated in Europe seems to have ended in 1990, French companies only appear to have become seriously interested in the emerging markets after the consolidation of the Single Market (see Graph 1). The onset of what seems to be a new geographic pattern of French foreign investment emerged in 1993. This can be seen in the substantial increase in flows of FDI to developing countries, while the flows to the OECD countries dropped to 1987 levels.

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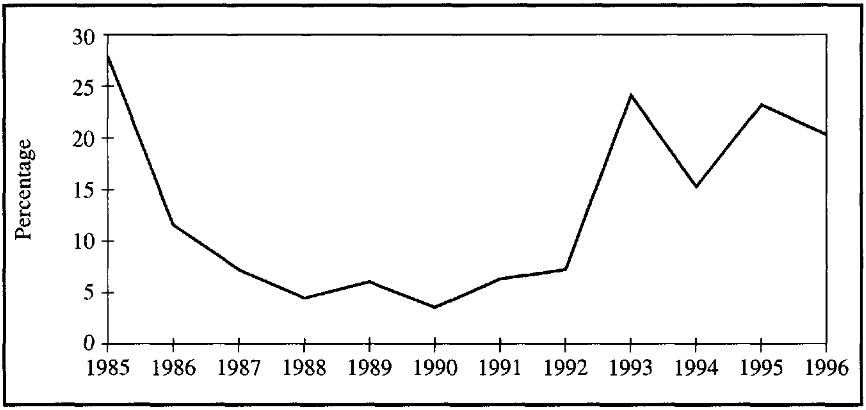
Graph 1
Non-OECD Countries' Share of Net Flows of French FDI



Source: Banque de France.

The tendency for French FDI to converge on Europe had a particularly strong impact on Latin America.[5] Flows to the region slumped in the period 1985-89 (from an annual average of $232 million in the period 1980-84 to $107 million in the second half of the decade), before showing signs of recovery in 1990 and then rising very rapidly in 1996. This sharp increase was confirmed and consolidated in 1997, and does not seem to have been affected by the new dynamism acquired by the European integration process in the build up to monetary union.

French investment and changes in the region

The economic and political climate

A second factor which appears to have had a major influence on the evolution of French investment in Latin America involves investors' perceptions of the political and economic instability in the region. It is clear that French investors were very reluctant to invest in the region during the difficult years of the 1980s. This can be seen from the overall drop in FDI flows to Latin America, as well as from the reduction in the number of affiliates set up there; in fact, the number of new French affiliates

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established in this period fell by over 50% in comparison to the previous decade. It is also apparent that this slump was not simply a consequence of the diversion of French FDI towards the European Union mentioned above: the drop in investment in Latin America was much more pronounced than in the non-OECD countries as a whole.

Generally speaking, French companies were rather slow to react to the return of political and economic stability and the adoption of structural adjustment and liberalization policies in Latin America. Between 1988 and 1993, while France was still trying to make up for lost ground with respect to investment in Europe, and beginning to take an interest in Asia, almost 600 state-owned companies were sold in what was the first major wave of privatizations in the region. While a number of French companies were involved in a few major operations (contributing to the aggregate increase in French investment in the region in 1990), as a whole they were virtually absent from the privatization process (see Box 1). Thus, the flow of investment to Latin America during the first half of the 1990s essentially consisted of a small number of major operations rather than a mass influx of French companies into Latin America.

Specific disinvestment operations which affected the general trend

In this respect, it is also interesting to consider the pattern of investment flows which emerges once a number of specific, large-scale operations have been excluded. This shows that the apparent fluctuations in net French FDI in recent years (see Graph 2) obscure the fact that the gross flows (that is, the new investments made each year) remained relatively constant, within a slightly upward trend. In fact, closer examination of the figures reveals that the drop in the net flow of French FDI to Latin America between 1993 and 1994, and to a lesser extent in 1991, was not a consequence of a broad diversion of capital, but rather of a small number of major disinvestment operations which, despite involving significant sums, appear to have constituted relatively isolated cases.

A structural-type explanation could be put forward for these outward flows of capital, namely that a connection exists between the major investment flows seen in 1990 and 1993 and the reductions seen in the years immediately afterwards. If this were so, the latter would reflect the sale of part of the assets acquired during the previous years. However, closer examination shows that the disinvestment did not occur in those sectors and countries which had received inflows of investments immediately beforehand (see the analysis of the

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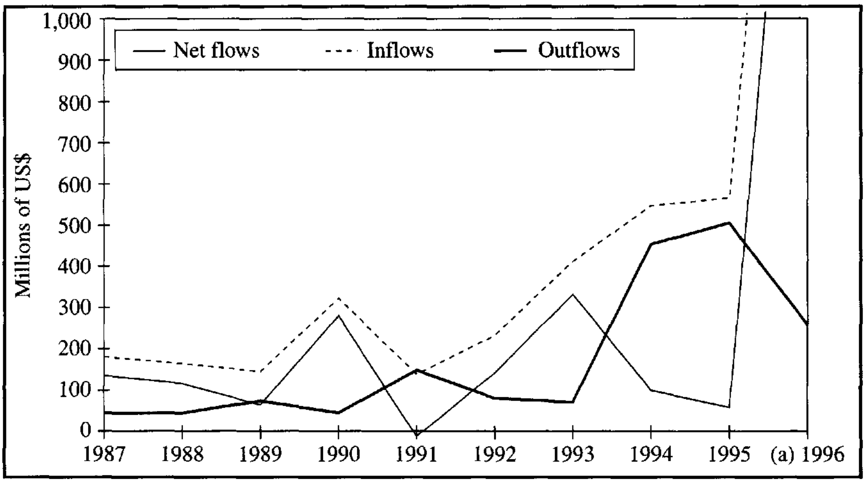
geographic and sectoral distribution of French investments below).[6] Moreover, we also find that this disinvestment was highly concentrated: in each of the three years considered here (1991, 1994, 1995), just two or three major operations accounted for the bulk of the outward flows of investment from the region.

Graph 2
Breakdown of French Investment Flows to Latin America



Source: Banque de France.
Note: (a) Inflows: $2.3 billion - Outflows: $255 million - Balance: $2 billion.
Short-term loans between companies in the same group have been included in the figures since 1996, thereby interrupting the homogeneity of the series. However, in the case of Latin America these loans are of little significance (they accounted for just 2% of the total flows during the first eight months of 1997).

A second explanation for the fall in net flows in the period 1994-95 could be that French investors withdrew capital from the region in response to the financial crisis in Mexico in December 1994. However, this hypothesis can also be discarded, since none of the major cases of disinvestment in the region during this period affected Mexico. Rather, the evolution of FDI flows shows that neither the financial crisis itself nor the recession that followed deterred French investment projects in Mexico. If the major devaluation of the Mexican peso did have any impact, it was on the value of the stock[7] of French investment in

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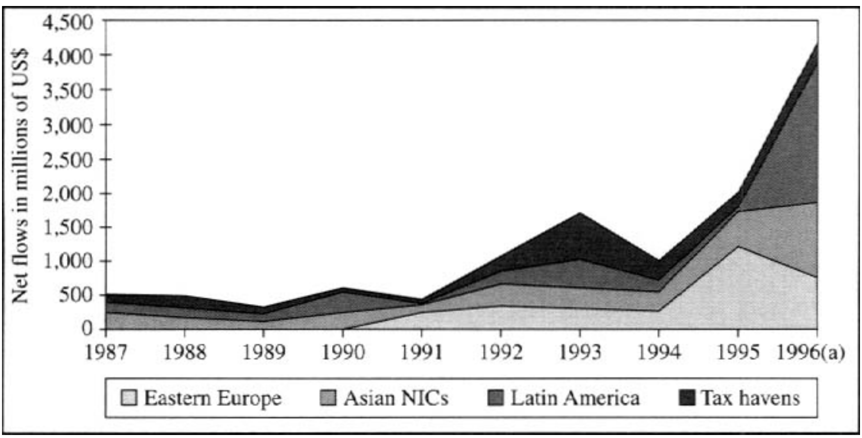
Mexico, which affected the value of the stock of French FDI in the area as a whole from the end of 1994 onwards.

The position of Latin America compared to other developing regions

The rapid economic growth in Asia over the last few years has made it one of the principal destinations for foreign investment outside the OECD countries. Despite their historical ties with Africa, and to a lesser extent with Latin America, French companies have been no exception to this rule. Thus, while the flows of French FDI into Asia have been relatively modest in comparison to those from other industrialized countries, they have nonetheless led to a steady increase in the French presence in the most dynamic economies in the region (Graph 3).

Graph 3
Geographic Breakdown of French FDI Flows to Developing Regions



Source Banque de France.

On the other hand, the geographic distribution of French investment since 1991 also confirms the increasing pull of Central and Eastern Europe. The implementation of structural reforms and liberalization processes in the region, the prospect of integration into the European Union (EU) and, of course, geographic proximity, have all added to the attraction of this region for French

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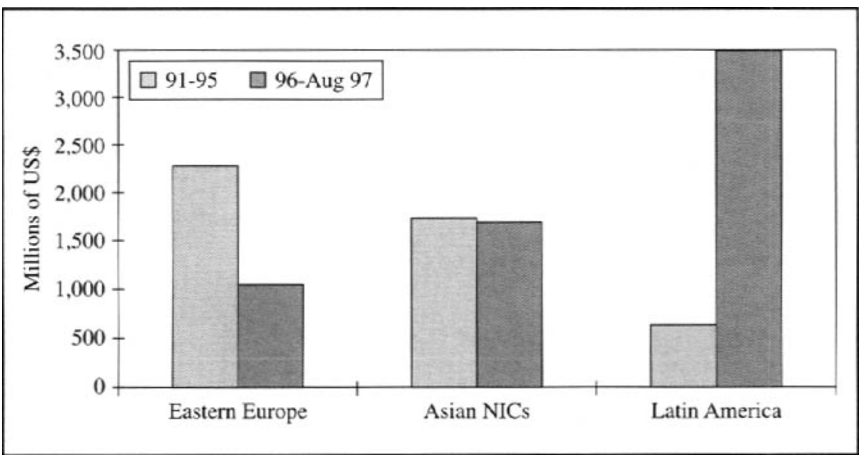
investors, and above all medium-sized companies. This is a similar situation to that which occurred when Spain opened its doors to foreign investment. Moreover, the Central and Eastern European markets became increasingly attractive precisely when the medium-sized companies were embarking on the internationalization of their operations. Nonetheless, these flows of investment are relatively modest in scale, and almost insignificant in comparison with those made by the large corporations.

Although French companies have long been aware of the need to penetrate the Asian markets (as reflected in the volume and regularity of the flows to the region), when capital became available for investment in other developing countries in 1991-95, priority was given to Eastern Europe (see Graph 4). For a number of years, Latin America, a more distant region which has often been associated with hyperinflation and instability, suffered the consequences of this competition. However, this situation began to change in 1996, when Latin America reestablished its leading position and French companies began to react to the more secure and dynamic political and economic situation in the region.

Graph 4
Accumulated French FDI flows



Source: Banque de France.

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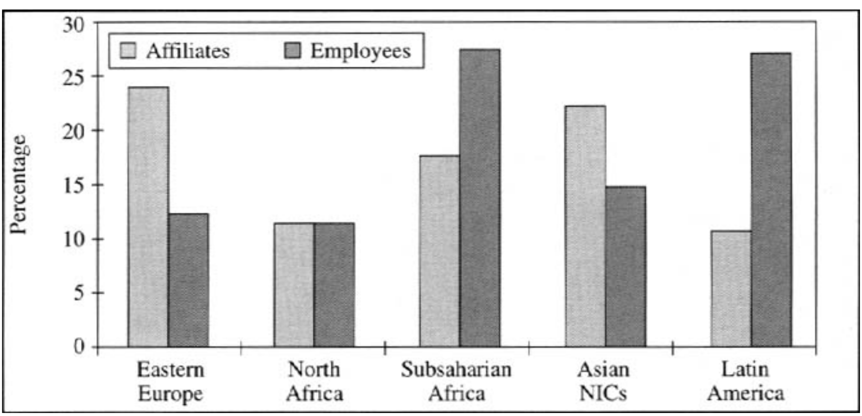
However, the pull temporarily exerted by other developing regions did not undermine Latin America's position in terms of the total stock of French FDI. This is explained by a number of factors. Firstly, the French presence in Asia and Eastern Europe largely took the form of growing numbers of small and medium-sized operations, which have little real impact on the value of stocks. Secondly, the proportion of French FDI in developing regions is still relatively limited, and the amounts involved are small. As a result, despite the unprecedented annual volume of FDI flows, over the last five years the number of employees in French affiliates in non-OECD countries has risen by little more than 25%.

Latin America's reduced capacity to attract French investment during and immediately after the years of economic and political crisis in the region can be seen even more clearly by analyzing new investments and the number of personnel employed by French affiliates in the region. In 1980, the total number of French affiliates in Latin America (around 500) was similar to that in Asia, while there were only some 100 French-owned affiliates in Central and Eastern Europe. At that time, the French presence was strongest in Sub-Saharan Africa, where there were around 1,000 French-owned companies. Yet by the end of 1995, the geographic distribution of French investment in the developing regions had changed dramatically, and almost entirely to the benefit of Asia and Central and Eastern Europe (Graph 5).

Graph 5
French Affiliates and Personnel Employed in Developing Regions at the end of 1995



Source: DREE, *Enquête filiales*, 1996.

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Closer examination of French-owned subsidiaries and their personnel reveals that the French presence in Latin America consists mainly of a small number of large-scale operations. This level of concentration, which reflects the traditional sectoral distribution of investment (above all in basic industries), has not declined in recent years. French investment has traditionally converged around a core group of large companies with strong roots in Latin America, rather than a broader range of French firms. Nonetheless, the recent resurgence in interest in the region, which has attracted French industry as a whole and is strongest among small and medium-sized enterprises (SMEs), should soon be reflected in the statistics.

French companies rediscover Latin America in 1996

Regardless of the explanation for the somewhat erratic fluctuations seen in the past (within an overall context of moderate growth), the spectacular increase in investment in 1996 and 1997 appears to indicate a more lasting change in the attitude of French companies towards Latin America. A number of factors combine to suggest that this new found impetus is not merely the product of a few isolated operations; instead, it appears to reflect a more fundamental shift in their investment strategies. In fact, all the indicators of French investment activity in the region show substantial increases since 1996. Along with the expansion of investment flows, which have increased at least threefold and been channelled towards an ever larger number of sectors, there has been a notable decrease in the number and scale of disinvestment operations in the region. The rate of new investments (5% growth), and the reversal of the downward trend in the number of personnel employed by French subsidiaries since 1995, provide further grounds for optimism. The slight increase in these companies' exports, which rose by 10% in 1996 and is undoubtedly linked to the larger flows of FDI, should also be noted.[8]

This growth in FDI continued in 1997, which also saw considerable diversification in investment albeit with national variations. During the first eight months of the year, there was a truly spectacular upsurge in French investment in Brazil, with an influx of nearly $1 billion (making France the fourth largest investor in the country after the United States, the United Kingdom and Germany). Colombia also experienced a major increase in French investment, above all in the form of long-term loans from French companies to their affiliates. On the other hand, the level of investment in Argentina remained relatively stable.

Within this general pattern of intensified activity, French investment in different sectors has responded to very different logics. As will be seen below,

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the development plans of the large French industrial corporations form part of continent-wide strategies intended to meet the challenges created by the emerging regional markets in Latin America. In the utilities and infrastructure sectors, French companies have taken advantage of their strong position to seize the opportunities presented by the second wave of privatizations. At the same time, there has been a significant increase in the number of government-backed initiatives to raise awareness among French SMEs of the business opportunities now existing in Latin America. All these tendencies suggest that Latin America has regained its ability to attract French companies, in comparison with other developing regions.

Box 1: French Companies and the Privatization Process

The Berthommier Report, which was compiled for the Ministry of Economy and Finance in October 1997, analyzes the role played by French companies in the privatization-concession processes in Latin America, and the opportunities that can be expected to appear over the next few years. This report confirms, firstly, that French companies played a relatively small role in the first wave of privatizations: only 50 of over 700 state-owned companies sold between 1990 and 1994 were acquired by French investors. According to the same report, the sectoral breakdown of the companies sold to French firms between 1973 and mid-1997 was as follows: water and sanitation (31%), electricity (15%), oil-gas (15%), finance (27%), transport-civil engineering (8%) and telecommunications (4%).

The French presence is weakest in the industrial sector. French companies certainly appear to have taken little interest in the opportunities for investment in this sector (mines, iron and steel plants, etc.). In the banking sector, French involvement appears to have been very limited, generally consisting of consultancy contracts which do not require significant investment. Thus, French banks have not kept pace with their American, British, or Spanish competitors in terms of their penetration of Latin American markets.

In the telecommunications sector, France Telecom's operations in Mexico and Argentina generated investments which have had a major impact both on the company's traditional suppliers and sub-contractors and on its European partners. The company's experience in this field undoubtedly means that it is well-placed to participate in future operations, as exemplified by the cellular telephone contract signed in Paraguay at the end of 1997. In the energy sector, Electricité de France has been awarded concessions in Mexico and Argentina. French companies are currently interested in electricity generation, and are beginning to win contracts to build and operate power stations. Gaz de France has been very active since 1993, participating in a number of different operations involving the transport and distribution of gas supplies. French oil companies have obtained concessions for the extraction of resources, but so far have shown no interest in acquiring local privatized companies.

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Regardless of the nationality of the beneficiary, the award of concessions and the sale of state-owned companies in the energy and telecommunications sectors have major consequences for France, since it is widely recognised that French companies have great expertise and know-how in these areas. As a result, and independently of the acquisitions made by French companies, French specialists in oil prospecting and mining (such as the Compagnie Générale de Géophysique) and electrical equipment suppliers (Cegelec, Alsthom, Schlumberger) have benefitted significantly from the new opportunities for foreign investment.

French companies still have only a weak presence in the field of air and land transport and in the construction and operation of the infrastructure this requires (airports, highways, bridges); Systra, Aéroports de Paris, and Lafarge are exceptions to this rule. In contrast, French companies have outstripped their competitors in the field of water supplies. The two main French operators (Lyonnaise and Générale des Eaux) have been awarded concessions in six countries (Brazil, Mexico, Chile, Colombia, Bolivia and Argentina). In this sector (which includes sewage disposal), there are good prospects for further development in the future, above all in Mexico and Brazil. If these expectations are fulfilled, they would also have major consequences for French suppliers and sub-contractors.

During the first wave of privatizations, French involvement was limited to a small number of countries and companies. More recently, however, French companies have shown greater dynamism and initiative in the region. The variety of ongoing projects and the larger number of tenders put forward by French companies suggest that there has been a generalized change in attitude. Thus, the prospects are encouraging, above all in the light of the fact that most of the privatizations still to take place involve sectors (such as infrastructure, services, the environment, health, education) in which French companies have widely recognized expertise and experience.

French FDI in Latin America in the 1990s

A breakdown of the annual flows of French FDI by recipient country and sector reveals that investments have tended to be both highly concentrated and to fluctuate over time. In fact, a small number of major operations account for over 75% of the flows of capital to the region as a whole over the last decade. The sectoral and geographic distribution of investments has not changed significantly during this period. However, this situation could change as French companies begin to respond to the regional integration processes and the opportunities created by the programmes of privatizations and concessions currently being implemented in a number of different countries.

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Distribution by sectors

Despite their still limited overall presence in the region, French companies have consolidated their position in certain industries (car manufacturing, chemicals, agribusiness), as well as in some areas of the service sector (telecommunications, electricity, water supply and sanitation, and the operation of infrastructure). The bulk of French FDI stock is still held in the industrial sector, which accounts for 46% of all assets, compared to 35% in the service sector.[9]

Table 3
Sectoral Breakdown of French Investment in Latin America in 1994[1]

	Millions of US$	% of the total
Agriculture and agribusiness	322	4
Energy and water	177	2
Industry	3,386	46
— of transport eq.	435	6
Construction and civil engineering	64	1
Services	2,549	35
— financial[2]	1,266	17
Holding companies	848	12
Total	7,346	100

Source: Banque de France.
1. Includes offshore centres.
2. Includes banks and financial institutions.

Despite the continued predominance of the industrial sector in terms of total stock, since the resurgence in investment at the beginning of the decade the flow of French capital into the region has largely reflected the internationalization strategies of companies in the service sector. Commercial services (banks and insurance, retail distribution, tourism, transport and telecommunications) account for 43% of French FDI flows.[10] The rapid expansion seen in the service sector over the last two years should continue, if the planned investment operations are put into practice and French companies are able to take advantage of their expertise in the development and administration of public utilities and infrastructure (see Box 1).

In the manufacturing sector, investment flows since 1990 (which account for just 22% of total flows) largely reflect the consolidation of companies

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already established in the region rather than the arrival of newcomers. A number of large French electrical and mechanical engineering groups installed plants in the region in the 1960s and 1970s, while in mining and the chemical industry the French presence dates from even earlier. More recently, the current or planned expansion of production (above all in the automobile industry) is closely related to the ongoing processes of regional integration. This suggests that, with the return of a favourable economic and political climate, the ongoing processes of regional integration through customs unions may prove to be a key factor for the revitalization of industrial investment.

Agribusiness constitutes another major focus of French industrial investment in Latin America. The potential for growth in this sector is illustrated by the Danone group. Following a number of major acquisitions, in less than two years Danone has emerged as the market leader in three important areas (biscuits, dairy products, and mineral water) in Argentina. At the same time, and alongside the traditional presence of oil companies, major French groups have taken advantage of new opportunities in the energy sector, and above all in electricity generating and related activities. Thus, in 1996 the electricity, gas and water sector absorbed at least 25% of all capital flows to the region.

Geographic distribution

Brazil, Argentina and Mexico are the undisputed leaders in terms of the geographic distribution of French investment in the region. This reflects the size of their populations and the scale of their economies, as well as the advantages which their membership of free trade areas offers potential investors. As can be seen in Graph 6, in 1995 these three countries alone accounted for 90% of all French FDI flows to the region.

Brazil has traditionally been the most important destination for French investment in Latin America. By the end of 1995, 60% of all FDI stocks in the region were concentrated there. The operations which have been completed, initiated or announced since then have only confirmed Brazil's preeminence in this respect; so much so that Brazil is now not only the preferred destination for French FDI in the region, but also a major magnet at the global level: in 1996 it absorbed 3.6% of all French FDI, making it the eighth most important recipient country in the world, ranking only behind the United States and the six most important EU Members States.

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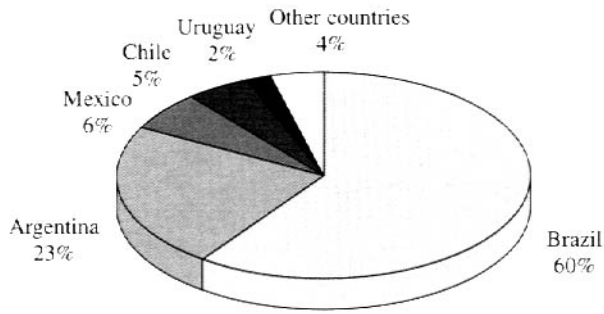
Graph 6
Stock of French Investment in Latin America and the Caribbean at the End of 1995



Source: *Banque de France.*

The recent upsurge in investment has only reinforced Brazil's share of French FDI stocks worldwide. By the end of 1995, Brazil ranked ninth (immediately behind Italy) with 2.1% of all French FDI. Brazil is by far the most important Latin American country in terms of the number of people employed by French affiliates; in this respect, it holds seventh place in the global ranking, ahead of Switzerland and the Netherlands. With some 120,000 employees, the French affiliates in Brazil account for almost half the total for Latin America. Brazil's striking preeminence in terms of French FDI in Latin America is not matched in other developing regions of the world, where French investment tends to be spread more evenly. Moreover, within Brazil itself, French companies are operating in an increasingly wide range of sectors. Despite the presence of a number of well-established industrial groups, such as Saint-Gobain, Rhône-Poulenc and Pechiney, more jobs now exist in French companies in other sectors. The largest single French employer is the Carrefour retail distribution group, which currently employs some 20,000 people in Brazil.

During the first half of the 1990s, while countries such as Argentina and Mexico eased the conditions for foreign investment and embarked on privatization programmes, Brazil continued to impose a number of restrictions. As a result, the former benefitted from increased influxes of foreign investment, while the flows to Brazil remained relatively stagnant. As a result, there was a temporary diversion of

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French FDI to other Latin America countries between 1989 and 1995, Argentina receiving 31% of all flows that year, while Brazil received just 20%. This tendency changed radically in 1996 as a consequence of French participation in the privatization of LIGHT in Rio (EDF) and Aguas de Limeira (Lyonnaise des Eaux), as well as the investments made first by Renault and then Peugeot.

Argentina is the Latin American country which has seen the sharpest and most consistent increase in French investment since the early 1990s. In terms of the French FDI stock, it now ranks fourteenth at the global level and second among the developing countries. Between them, the French affiliates in Argentina employ almost 50,000 people. Many of these jobs are connected to new investments or recent acquisitions outside manufacturing industry, in particular by groups such as Danone, Carrefour, France Telecom and Lyonnaise des Eaux. The latter two companies' involvement in the privatization-concession process has opened the door to the Argentine market to their traditional partners, and put them in a very strong position with respect to future bids in the public utilities sector at the provincial level. The scale of their investments has also had an appreciable impact on the balance of French FDI flows.[11] This is certainly the case of the largest single operation by a French company, France Telecom's acquisition of a 9.9% stake in Telecom Argentina when this was sold for a total price of almost $2.4 billion.

The French presence in Mexico is more recent and still relatively limited, particularly in comparison to that of some other European countries. In 1995, Mexico accounted for less than 6% of all French FDI stock in Latin America, although it should be remembered that the value of this stock may have been affected by the devaluation of the peso over the course of the year. Nevertheless, almost 35,000 people are employed by the French subsidiaries in Mexico. Around 70% of these jobs are in manufacturing industry, compared to the average of just 32% in the region as a whole. At the same time, the average number of employees per unit of production (over 500) is much higher than in other countries, reflecting the predominance of French investment in labour-intensive activities. The indicators also suggest that, in common with their European counterparts, French manufacturers use Mexico as a platform for production destined for the US market. French companies have also invested heavily in the service sector, as in the case of France Telecom in Telmex, CGE in Aguas Calientes, GEC-Alsthom, and Club Mediterranée.

Traditionally concentrated in the exploitation of natural resources, the French presence in the other Latin American countries is now strongest in the service sector, and located above all in Colombia, Venezuela, Chile, Uruguay

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and Peru. Groups such as Sodexho (restaurant chains), AGF (insurance) or Carrefour (retail distribution), for example, have significantly expanded and diversified their operations in South America. However, privatizations and concessions in the public utilities sector and the modernization of infrastructure are responsible for bringing most French companies to these countries, and offer the best opportunities for geographic diversification in the future.

Table 4
Main Activities of French Affiliates in Latin America

Countries	Sectors[1]
Brazil	Tourism Retail, distribution Minerals, glass and cement Chemicals and plastic
Mexico	Electric and electronic eq. Tourism Pharmaceutical and perfumes Water, gas and electricity Telecommunications
Argentina	Automobile Retail, distribution Foodstuff Water, gas and electricity Telecommunications
Venezuela	Construction, civil engineering Minerals, glass and cement Chemicals and plastic
Chile	Insurance Tourism Automobile
Colombia	Water, gas and electricity Automobile Electric and electronic eq.

Source: DREE
1. Listed in order of the number of people employed in each country.

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The Strategies of French Groups

FDI *as the principal vehicle for French presence in Latin America and the Caribbean*

For many years, French companies did not include Latin America and the Caribbean in their commercial strategies (precisely those strategies which are most important in the first phase of the internationalization process). To some extent, the protectionist policies which many Latin American countries had adopted since the 1950s obliged the major French groups to skip this phase and directly establish manufacturing plants in the region. At the same time, exports by smaller, independent French companies to Latin America have been insufficient to generate a flow of trade with a direct impact on productive investment.[12]

As a result, Latin America has been much more important as a destination for French investment than as a trading partner: in 1996, Latin America (including the offshore centres) absorbed 7.9% of the net flow of FDI, compared to just 2.1% of French exports. However, the low ratio of French exports/FDI flows to the region is not simply a legacy of protectionism; according to figures from the International Monetary Fund (IMF), rather than increasing, France's market share has actually fallen since the onset of liberalization in the region, dropping from 4.7% in 1990 to 3.8% in 1996.

Intra-group trade

At the same time, however, FDI tends to generate international trade within groups investing abroad, either because the creation of a foreign subsidiary is intended to secure easier access to a market, or because part of the groups' production is carried out abroad.

In the first case, the parent company exports finished products for resale by the affiliate. However, the existence of protectionist barriers, or the weak purchasing power of the local market may hinder the use of this type of strategy. This is confirmed by the results of the SESSI "Industrial Globalization" survey (see Graph 7). Its analysis of French foreign trade in 1993 clearly shows that strictly commercial intra-group trade accounted for a remarkably low proportion (just 7%) of all French exports, which themselves were very low compared with FDI stock.[13] Until very recently, therefore, trade-related investment has constituted a relatively insignificant part of the total. Nevertheless, the removal of protectionist barriers and the stronger economic growth in Latin America have improved the prospects for trade in general, and should bring this type of trade to levels closer to the

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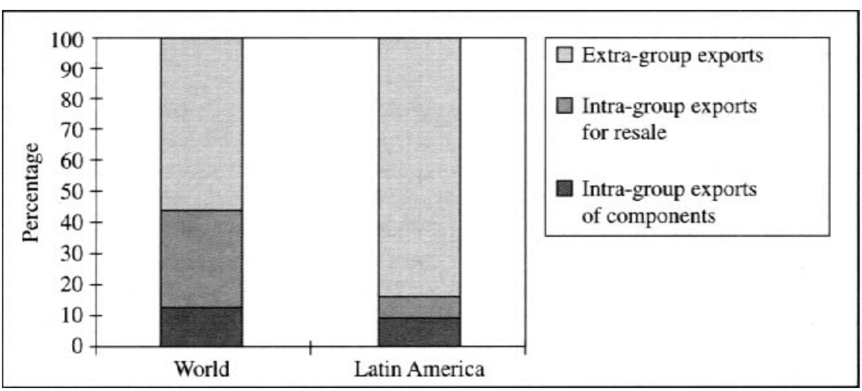
average as the commercial phase of internationalization, which was skipped by the large industrial groups, may now be left behind by other foreign investors.

In the case of affiliates in manufacturing industry, intra-group trade generally takes the form of sales of factors of production (raw materials, machinery, components). Exports of this type account for some 10% of all French exports to Latin America. This figure is much lower than that of France's main industrial partners (in Spain, for example, which is an important productive base for French groups, this figure is around 30%), but twice as high as for South East Asia or North Africa. This type of trade is essentially limited to sectors in which French companies have long been established in Latin America, notably in the chemical-pharmaceutical and transport equipment industries. Both have traditionally been characterized by a considerable international division of production, and hence intense intra-group trade, as exemplified by that between France and Spain.

However, the distances involved, combined with some governments' policies of restricting investment in low added value production (especially in the automobile industry) necessarily limit the potential growth of this type of trade. As a result, a foreign company's customary suppliers and sub-contractors are often forced to set up a manufacturing base near the site of production, generally in partnership with a local firm. In other sectors, such as retail distribution, transport costs, customs tariffs, and import taxes are often considered to be prohibitive. As a result, for example, nearly 90% of all Carrefour's sales consist of locally produced goods.

Graph 7
Breakdown of Exports of French Companies



Source: SESSI, *Globalization Survey*, 1993.

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Investments intended to secure a reduction in production costs often generate the resale of finished products by the subsidiary either to the parent company or to another company in the same group. Hence, the existence of a large volume of intra-group trade of this type would indicate that certain phases of the production process have been relocated. In Latin America, however, this type of strategy appears to be extremely rare and of minimal importance insofar as French companies are concerned. Intra-group trade of this type is very limited and largely restricted to components for the automobile industry. The reimportation rate (defined as the ratio between intra-group imports for resale and intra-group exports of components) is much lower than in other developing regions.

Table 5
Reimportation Rate of French Companies by Region

Regions	percentages
Latin America	7
South East Asia	91
North Africa	90
Central and Eastern Europe	127

Source: SESSI, *Globalization Survey*, 1993.

Thus, the French-financed operations in Latin America operate relatively autonomously of the parent company. The pull that French FDI has on foreign trade is mainly felt outside the investor groups which, without necessarily being manufacturers, resort to their traditional suppliers for complex products (as in the case of EDF, Lyonnaise des Eaux, or SNCF-RATP, which use them for occasional orders which do not require suppliers to set-up production on-site).[14]

Strategies: From the extraction of natural resources to the penetration of expanding markets

The low level and peculiar nature of intra-group trade reflects the way in which, over the course of the century, French companies have responded to the changing economic and political conditions in France and Latin America. The brief analysis which follows shows that their responses have varied in accordance with the specific characteristics of the different economic sectors.

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The extraction of natural resources

French foreign investment in Latin America was traditionally driven by the search for natural resources. Thus, the first companies to invest in the region were characterized by their great dependence on raw materials and agricultural products. This type of investment still accounts for the bulk of French investment in the petrochemical and chemical industries (Total, Elf, Rhône-Poulenc, Pechiney), mining (Saint-Gobain, Lafarge) and rubber (Michelin).

Nonetheless, major changes are now taking place in these sectors. Given the prospects for the expansion of the local market and the development of regional markets, there is a need to expand, modernize, and introduce qualitative improvements in the production process. As a result, Total, which is participating in a massive project for oil extraction in the Orinoco Basin in Venezuela, has plans for major growth in Latin America. Michelin, in turn, considers that rising rubber production in Brazil will lead to an increase in its tyre production, fuelled by intensified car production. Having recently acquired a number of local firms, Lafarge is now the third most important producer of cement in Brazil, the single largest producer of concrete, and the only plasterboard manufacturer in the country. The Saint-Gobain group has also stepped up its programme of acquisitions in Latin America, and now owns seventy factories in six countries. In most cases, the absence of significant intra-group imports and exports in these sectors confirms that the main objective of these companies is to supply the Latin American market.

Manufacturing industry and national markets

The second main stimulus for French investment in Latin America has been the consolidation of its share of national, and more recently regional, markets. Encouraged in the past by the existence of protectionist barriers to imports, investment in the automobile industry, as well as in the production of capital and consumer goods, has been revitalized by the creation of sub-regional customs unions and hence larger markets. The North American Free Trade Agreement (NAFTA) attracted major investment in the chemical industry, automobile production and the agribusiness in Mexico. However, since 1995 French manufacturers appear to have shifted their attention from Mexico to the members of the Southern Common Market (*Mercado Común del Sur*, MERCOSUR). This is apparent from the way in which French groups operating in these industries have now intensified their investment in both production and trade in order to supply MERCOSUR.

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Developments in the automobile industry exemplify this type of strategy. French investment in the 1970s, based on the acquisition of minority stakes in companies, are no longer sufficient to meet the rapid expansion in demand or guarantee their market share in the face of very intense international competition. Thus, the French automobile companies Renault and Peugeot Citroën decided to make greenfield investments in Brazil, acquiring majority stakes of 60% and 68% respectively. The Renault plant, which is due to start production at the end of 1998, has the capacity to produce 110,000 vehicles a year. In January 1998, Peugeot Citroën signed a contract to build a similar sized factory (with a capacity for 100,000 vehicles a year), at the same time as it announced plans to pull out of China and India.

These operations not only reflect these two groups' plans to expand their existing manufacturing capacity in Latin America, and more specifically in Argentina, but also a fundamental change in strategy. And this, in turn, confirms that MERCOSUR, and South America as a whole, now represent key areas of development. However, it is still too early to say whether these French manufacturing investments respond to a new trend in the inter-continental division of labour, whereby different countries specialize in different areas of the production process in function of the complementarity of neighbouring countries. It should also be noted that in these oligopolistic industries, the slow response of French companies in comparison to their competitors means that their investments are often essentially defensive in character, in that they are intended simply to maintain their market share. And in order to do this, they are obliged to imitate their international competitors.

Penetration of new markets in the service sector

In contrast, in other sectors French groups seem to have adopted more offensive strategies (designed, in other words, to secure or increase their market share). This is true above all in those sectors requiring investment in real estate, where market access is dependent on investing near consumers, as in the case of public utilities, the construction and operation of infrastructure, tourism, and retail distribution (hypermarkets). French companies now hold a strong position in these sectors in Latin America, having achieved market coverage which extends beyond the boundaries of the existing customs unions. A new dynamism has been visible in these sectors for two years or more, as demonstrated by the proliferation of French tenders for concessions and major contracts.

The search for direct access to local markets has also been the main impetus for the rapid expansion of groups such as Danone (which in 1997 acquired the

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largest dairy group in Argentina, Mastellone) and Sodexho, which has gained a foothold in the tourism industry and the provision of collective services in six countries. In the consumer goods sector, the Mexican crisis of 1994-95, and the subsequent relatively swift economic recovery, have had a reassuring, rather than unnerving, effect on investors. In fact, the crisis has had very varied consequences. The Carrefour group, for example, which in recent years has expanded in Latin America at the rate of some fifteen new hypermarkets a year, responded to the loss of purchasing power among Mexico's middle classes by cutting prices, thereby increasing its customer base. In the light of the relatively competitive position of these French groups in Latin America, it seems likely that local investment, which still represents a minimal proportion of all French FDI stock at present, will increase substantially in the near future. In those industries with low levels of international trade in finished products, all the Latin American countries are potential recipients at both the national and provincial level.

Minimal relocation in search of efficiency

In contrast, there are few signs that the advancing process of globalization has encouraged any significant relocation to Latin America of the labour-intensive, standard-technology, light industries, as would be expected if comparative advantages were the principal incentive for such investments. In terms of French investment at least, this does not seem to be a decisive factor, since Latin America lacks the advantage of geographic proximity offered by Central and Eastern Europe or North Africa.

To conclude, it can be seen that, compared to their competitors, French industrial groups have been relatively slow to respond to the new investment opportunities existing in Latin America. However, the recent resurgence in French investment in the region has involved a large number of sectors and responded to different logics. Yet in most cases, and regardless of the nature of the investment, these operations are generally intended to supply the Latin America market itself. This, in fact, constitutes the best guarantee that the major flow of French capital to the region seen over the last two years will continue in the future.

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Annex 1:
Recent French FDI Operations of Over 100 Million Francs

Country	Type of Flow		Year	Flows in millions of US$
Argentina	Investment	Insurance	1993	27
			1994	19
		Retail distribution	1993	33
			1994	24
			1996	53
		Electricity, gas and water	1992	36
			1993	26
			1994	39
			1996	179
		Financial services	1993	48
			1994	39
			1996	57
		Commercial and property development	1994	192
			1996	130
		Oil, gas	1989	25
		Food poducts	1995	48
		Chemical products	1995	20
			1996	137
		Telecommunications	1990	30
	Disinvestment	*Retail distribution*	*1993*	*28*
			1996	*24*
		Electricity distribution	*1996*	*104*
		Financial services	*1995*	*73*
		Oil and gas	*1989*	*23*
			1992	*20*
		Secondary oil products	*1996*	*20*
Brazil	Investment	Automobile	1996	34
		Electricity, water and gas	1996	400
		Financial services	1988	25
			1996	34
		Commercial and property development	1990	57
			1992	35
			1995	23
			1996	342
		Food products	1990	19
			1995	41
		Chemical products	1994	28
			1995	33

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**Annex 1 (cont.):
Recent French FDI Operations of Over 100 Million Francs**

Country	Type of Flow		Year	Flows in millions of US$
		Mineral products	1988	21
			1990	21
			1996	191
Brazil	*Disinvestment*	*Retail distribution*	*1991*	*123*
		Financial services	*1987*	*22*
			1990	*33*
			1995	*325*
		Mineral products	*1988*	*18*
		Textiles and clothing	*1989*	*23*
Chile	Investment	Construction and civil engineering	1990	20
			1996	23
		Financial services	1988	25
	Disinvestment	*Retail distribution*	1992	24
		Financial services	*1995*	*47*
Colombia	Investment	Retail distribution	1996	65
		Oil, gas	1993	112
			1994	82
			1995	73
	Disinvestment	*Oil and gas*	*1994*	*292*
Mexico	Investment	Automobile	1987	73
			1995	52
		Retail distribution	1996	25
		Financial services	1990	29
			1995	32
		Communications equipment	1993	18
		Property and commercial development	1994	21
			1996	224
		Food products	1995	53
		Chemical products	1995	21
	Disinvestment	*Retail distribution*	*1996*	*28*
Peru	Investment	Financial services	1995	42
			1996	22
	Disinvestment	*Financial services*	*1994*	*25*
			1995	*33*
Uruguay	Investment	Textiles and clothing	1990	26
			1991	21
Venezuela	Investment	Mineral products	1989	19
		Oil derivatives	1996	200
	Disinvestment	*Mineral products*	*1994*	*79*

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Annex 2: Definitions, Statistical Sources and Methodology

Direct investment flows

French FDI flows are recorded in the balance of payments compiled by the Banque de France, and published each year in an annex of the Annual Report of the Balance of Payments, broken down by sector and country. Insofar as Latin America is concerned, this report specifies the figures for the costs and annual balances of investments in three countries (Argentina, Brazil, and Mexico), but further data are available from the Banque de France. The investment flows are calculated in French francs, according to the exchange rate on the day the investment was made. These figures are then converted into dollars, using the average annual exchange rate in the year in question. In accordance with international recommendations, the term "direct investment" includes:

- — equity stock of at least 10% of the total;
- — investment in real estate;
- — Long-term loans (of more than a year) between a parent company and subsidiaries, and only since 1996; and
- — short-term loans and accounting operations between associated companies. Unlike the other EU countries, these loans represent only a fraction of French flows to Latin America (2% during the first eight months of 1997). Hence their inclusion does not present a serious problem for the homogeneity of the series.

Since 1996, earnings reinvested by subsidiaries have been included in the overall figures, but not in the geographic or sectoral breakdown of flows. Investments by French foreign subsidiaries which involve internal financing or loans from local banks are not included, since they do not imply the transfer of capital from France to the recipient country.

The exclusion of reinvested earnings could result in the underestimation of French flows in comparison to those of other countries which do include them in their figures, especially in the case of large companies with substantial foreign earnings. This is the case, for example, of the French group Carrefour, which now owns some 50 hypermarkets in Brazil. While in 1996 the group invested $300 million there, hardly any of this flow of capital was registered in the balance of payments, since the investment was partly financed by earnings obtained in Brazil ($185 million in 1996, or one-quarter of the groups's total earnings).

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The method used to record flows, which is based on the immediate rather than the final destination of the capital, also inflates the figures for flows towards those countries in which companies have established holding companies, to the detriment of the final recipient of the investment. This means that it is impossible to say, for example, how much of the flow registered to the Netherlands, the United States, or holdings in offshore centres, is actually destined for Latin America.

Direct investment stock

Since 1989, the Banque de France has compiled annual data on the total stock of French FDI. This data is obtained by means of a survey distributed to companies, and referring to subsidiaries in which French groups own at least a 10% of the capital. The results are published 15 months after the end of the financial year in question (in April 1997 for stock held on 31 December 1995) and in the Annual Balance of Payments Report which includes a detailed breakdown of the figures by sector and country, including five Latin American countries (Argentina, Brazil, Chile, Mexico, and Venezuela).

The figures refer to the investor's share of the capital in the companies in which the investment has been made, including the total amount of reinvested earnings, as well as any loans or credits made to the affiliate. The geographic breakdown of the stock is calculated in book value, that is, in accordance with the total sum recorded in the company's accounts, while the flows are calculated according to the commercial value on the day the investment was realized. As a result, the figures do not include what is known as "goodwill" (trade, intangible assets, prospects for growth).

The figures have been converted from the local currency into French francs according to the exchange rate at the end of the financial year. This means (as, for example, in the case of Mexico in 1994-95) that a devaluation of the local currency may make it appear that the value of the stock has collapsed. The value in dollars is based on the figures provided by the Banque de France, calculated in accordance with the exchange rate at the end of the financial year.

The variations in the nature of the operations considered here, and in the method used to measure and convert the figures, means that it is very difficult to compare the flows with the annual variations in stock. Thus, these results should be seen as complementary, insofar as they offer different perspectives of a single reality.

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Foreign affiliates

The DREE's network of 170 economic development offices provide it with very detailed information on French foreign affiliates. Each year, it produces a survey of the number of French affiliates and their employees. The *Affiliates 1996* survey, which was published in August 1997, refers to the French presence abroad at the end of 1995 and in early 1996.

Intra-group trade

In 1994 the SESSI produced its first *Globalization Survey*, which provides information on imports and exports between subsidiaries within the same parent group. This data has been compared with that contained in the Annual Survey of Companies, as well as with the customs data on foreign trade as a whole at both the company- and group-level. The resulting data base includes figures on the volume, nature, and type of intra-group trade in 1993, making it possible to analyze the geographic distribution of production, as well as information on the strategies followed by the groups concerned.

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NOTES

[1] *France and Privatizations in Latin America,* report presented to the French Ministry of Economy and Finance.

[2] This can be seen from the results of the survey of 311 executives of multinational companies and international experts compiled by Arthur Andersen and the French Ministry of Economy and Finance.

[3] Henceforth, and unless indicated to the contrary, the term Latin America is used to refer to both Latin America and the Caribbean.

[4] Data on French FDI stock are published 15 months after the end of the financial year. The figures used here correspond to 31 December 1995. The data for 1996, referring to the stock on 31 December 1996, will be available in April 1998.

[5] Excluding offshore centres in the region.

[6] These readjustments were made, although they did not always imply the sale of assets. This can be seen in the fact that the number of people employed by French subsidiaries in Latin America fell by 5% between 1994 and 1995.

[7] The French FDI stock in the different geographic areas is expressed in book value. Figures are calculated in the currency of the recipient country, converted into dollars according to the exchange rate at the end of the financial year.

[8] A sixth of all industrial exports to Latin America take the form of intra-group exports.

[9] Nonetheless, French-controlled subsidiaries in the manufacturing sector employ fewer people than those in the service sector.

[10] Some 60% of the disinvestment in this period was in commercial services. This sector was particularly heavily affected in 1995, due to the disinvestment by Credit Lyonnais and the Banque National de Paris (BNP).

[11] These operations are often partially reflected in the flows of direct foreign investment registered in the balance of payments. Even in the case of operations unconnected to privatizations, there are often significant differences between the official figures for FDI flows and the actual investments made by French companies. Among other reasons, this is a consequence of financial operations involving holdings based in third countries, as well as the fact that reinvested earnings are not included in the calculation of the geographic breakdown of flows.

[12] In the industrial sector, independent SMEs account for only 6% of French exports to Latin America.

[13] More than half of these exports involved non-French groups (above all in North America and other European countries).

[14] The effect is sometimes indirect. An interesting example is that of the Carrefour group, which sells more local than French products in Latin America, yet has nonetheless helped introduce its traditional European suppliers into Brazil.

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CHAPTER VIII

CHARACTERISTICS AND RECENT EVOLUTION OF INTRA-REGIONAL FDI*

Introduction

This chapter has a number of different objectives. First, it aims to provide a brief outline of some theoretical arguments concerning the effects of economic liberalization and regional integration on the flow of FDI to recipient countries, and especially those in the developing world. Second, it analyzes the trends and sectoral breakdown of FDI in Latin America, particularly in the Southern Cone countries and the Andean Community (*Comunidad Andina*). Third, it considers the importance and nature of intra-regional investment in the region, as well as the significance of a number of questions concerning the regulations governing intra-regional investment and the way in which capital flows are recorded.

Given the serious shortcomings of the information on foreign investment in the region (resulting from the variety of different recording methods used, and the absence of registers of capital flows in some countries), the figures given here are inevitably only illustrative of the scale and sectoral distribution of intra-regional investments. This chapter, therefore, does not pretend to draw definitive conclusions, but merely seeks to offer a preliminary analysis of the subject which may serve as the basis for a more informed understanding of the situation.

Latin American Integration and the Treatment of Foreign Capital

The general background

The integration process in Latin America in the 1970s and early 1980s formed part of a model of development based on expanding the market through the implementation of a sub-regional policy of import substitution and export promotion. The basic mechanisms in this model included the drive to ensure that foreign capital effectively contributed to development in the region, thus helping to reduce its technological dependency. At the same time, the recipient countries attempted to guarantee that the repatriation of earnings, royalty payments, and

* This chapter was written by Luis Jorge Garay and Arturo Vera, Integration, Trade and Continental Affairs Division of the Inter-American Development Bank (IDB).The authors would like to thank Robert Devlin for his comments on a first draft.

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the re-export of capital would not have a major negative effect on their balance of payments. In practice, the existence of a series of restrictions, economic instability in the region, and the absence of well-defined "rules of the game" served to discourage the desired foreign investment.[1]

In the years that followed, the persistence of certain endemic problems in Latin American countries, the debt crisis, and advancing economic globalization, were all decisive factors in the switch to a new model of development, designed to reintegrate the region into the world economic system. The scale and extent of the reforms required to achieve this structural transformation made it necessary to define a new approach to regional integration. This emphasized the role of market forces and private initiative, in the context of increasingly deregulated domestic markets and the removal of restrictions on both foreign trade and capital flows. All this has altered the nature of the integration process. This is no longer "inward looking" and based on import substitution, but rather looks "outwards" in order to participate in both international trade and foreign investment (which, as shown in the Annex to this chapter, is based on the principles of equal, automatic and practically universal access to FDI).

The more favourable economic, legal and institutional environment for private initiative is expected to prove highly attractive to foreign investors. The region offers foreign companies opportunities to expand in larger, more dynamic markets (which are no longer limited to the population of the individual country). These markets offer companies the chance to streamline their production at the global level, exploit "location advantages", generate competitive advantages, diversify risks, improve profit margins, consolidate their distribution and service networks, and reinforce financial relations between the capital markets of the countries in the integrated economic area. In principle, these opportunities are most likely to be seized by countries which are "natural partners", in that they complement each other and have geopolitical and cultural ties.

The effects of regional integration on foreign investment

Traditional economic theory treats all foreign inflows in the same way; from a neo-classical perspective capital is seen as homogeneous and essentially responds to variations in the rate of return in different countries. Accordingly, this theory recognizes that a preferential agreement between countries *may* encourage investment both from partner countries and from the rest of the world (intra- and extra-regional investment), since such

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agreements reduce the distortions between member countries and increase the size of the market.

Modern theoretical approaches to FDI and transnational corporations (TNCs) offer a more realistic vision of their basic characteristics, particularly in the context of economic globalization. One of the most important questions here is the so-called "monopolistic advantages" enjoyed by some TNCs as a result of "market failures" in the generation, dissemination and exploitation of intangible assets, such as technology, organizational skills and marketing. Thus, in the light of high transaction costs for technological transfers by other means (for instance, licensing agreements[2]), some companies engage in direct investment to create specific "ownership advantages", benefit from "location advantages" and exploit "intangible assets".[3]

On the other hand, there are good reasons to believe that changes in the nature of the regional integration process will provide greater scope for the development of location advantages and specialization between member countries, and hence make them more attractive to both intra- and extra-regional foreign investors.[4] Therefore, apart from the potential effects of economic integration on FDI described above, intra-regional investment may also be affected by a number of specific factors relating to the nature of the integration process. Recently, a number of these factors have been identified as decisive; these include the fact that integration tends to reduce the level of uncertainty with respect to present and future trade policies, the macroeconomic situation, and the political climate.[5]

Regional integration can also have negative effects on FDI, however. A free trade area with strict, selective rules of origin that discriminate against third countries may generate disincentives for extra-regional foreign investment. If the rules of origin offer advantages to investors from the member states of the regional organization, and discriminate against foreign investors which would benefit from the use of extra-regional inputs, foreign investment may be diverted to other regions. Clearly, this could have negative consequences for both the competitiveness of companies and member states, as well as the development of the region.[6]

These, potentially negative effects must be weighed against the advantages of integration in terms of attracting extra-regional FDI. One very important advantage is the expansion of the potential market. Integration agreements facilitate the stability and transparency of preferential access to all markets of the member states. This offers advantages to foreign companies when defining

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their investment strategies in the region, as they can take advantage of specialization and complementary processes, and even supply the largest market from other member states.

Generally speaking, the processes of liberalization, deregulation and privatization and "outward looking" regional integration tend to create favourable conditions for different types of extra- and intra-regional foreign investment, and for partnerships between domestic and transnational capital. A number of different types of investment should be highlighted in this context.

The privatization of state-run public utilities may benefit companies in the region which, either individually or in association with foreign companies, can invest surplus capital and apply their administrative and management skills in these operations. Among other factors, the profitability of investments in privatized companies increases when the cost of acquisition is lower, and when the prospects for expansion of the local market are better, as well as with more liberal public utility tariff policies (i.e. weaker state regulation). The advantages of privatization for the recipient country depend on the conditions of sale, the net capital revenue, and the extent to which the quality of the service improves; ultimately, this means the extent to which its social profitability increases in the medium and long term.[7] Generally speaking, much the same is true of the sale of state-owned companies exploiting natural resources, and the access given to foreign companies in this sector.

The liberalization of the financial sector and the removal of restrictions on foreign capital in this field often lead to the acquisition or creation of new banks and insurance companies by institutions in the region, third countries, or joint ventures formed to exploit "ownership advantages", "organizational advantages", or "intangible assets". The social benefits for the recipient countries will depend, among other factors, on improvements being made in the quality and variety of the services provided, on the transfer of "know-how", and on the extent to which liberalization promotes competition, reduces segmentation and lowers intermediary costs in the financial sector.

Economic liberalization and regional integration also tend to create opportunities for manufacturing companies to exploit competitive and location advantages in larger markets. In this case, companies can benefit, for example, by developing complementary, specialized systems of production and economies of scale, by internalizing "strategic assets"[8] and forming strategic alliances

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throughout the chain of production, from suppliers to distributors. Given the relative deficit in technology and "know-how" and the lower level of industrialization in most developing countries, intra-regional initiatives of this kind are likely to develop more slowly and have a less significant impact than in other areas. In the short term at least, extra-regional companies are likely to lead the field in this type of initiative, sometimes in association with companies from the member state in order to exploit "location and socio-cultural advantages". This is particularly likely to occur in non-traditional, technologically advanced industries, or in sectors which are heavily dependent on natural resources found in the region.

It can be seen, therefore, that just as the consequences of regional integration for intra-regional investment are determined by a number of different factors, so too are the benefits of investments between members states. In the case of the latter, these factors include the conditions prevailing in the host economy; the type of investment (national, regional or in alliance with transnational capital); the destination of the investment (production, financial services, public utilities or speculation); the duration of the investment (short or long term); and, finally, the extent to which competitive advantages are exploited, and competitiveness improved.

Intra-regional Investment in Latin America: Some Empirical Evidence

Regional investment trends

Any analysis of intra-regional investment in Latin America is inevitably conditioned by the limitations of the information available. The absence of complete registers of capital flows in a number of countries in the region, combined with the different recording methods used by the various sources mean that the data available is partial and fragmentary, and that the figures for intra-regional investment[9] may offer a distorted vision of reality. In the case of Chile, for example, the Banco Central only records outflows of capital, while Mexico does not record its own investments overseas. In other countries, such as Argentina and Costa Rica, it is not even a legal requirement to register movements of capital. The following, therefore, is merely a tentative analysis of the scale, evolution and sectoral distribution of direct investments between countries in the region during the first half of the 1990s.[10]

Intra-regional investment has shown the same rapid growth as total FDI in Latin America and the Caribbean (see Table 1). The total stock of investments

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held by Latin American countries in other countries in the region increased almost fourfold between 1990 and 1995, when it amounted to $4.1 billion. Despite this growth, however, intra-regional investment still represents a relatively small proportion of the total FDI in Latin America. In 1995, it accounted for an average of just 3.5% of all foreign investment stock in eight Latin American countries. Almost half of this intra-regional investment stock was held in Argentina, followed by Chile, Colombia and Brazil.[11] This pattern contrasts with the distribution of total foreign investment, which is concentrated in Brazil (32.6%), Mexico (29.9%) and Argentina (13.2%).

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Table 1
Stock of Intra-regional and Total FDI in Latin America, 1990, 1995 and 1996
(in millions of US$ and as percentages of the total)

Destination	1990	1995	1996	1990	1995	1996	1997[1]
Argentina	166 (2.4%)	2,064 (8.4%)	n.a.	6,942	24,630	27,352	30,210
Bolivia	58 (7.2%)	n.a.	200 (10.1%)	806	1,715	1,985	2,340
Brazil	114 (0.3%)	535 (0.9%)	n.a.	38,965	58,083	63,720	74,400
Chile	164 (2.6%)	521 (3.3%)	673 (3.3%)	6,423	15,691	20,270	21,560
Colombia	197 (5.6%)	542 (8.1%)	643 (7.7%)	3,500	6,480	8,363	10,315
Ecuador	108 (7.9%)	138[2]	n.a.	1,370	3,015	3,285	3,435
Peru	51 (3.8%)	282 (5.8%)	470[3] (7.0%)	1,330	4,825	6,058	6,751
Venezuela	10 (0.3%)	73 (1.1%)	n.a.	3,581	6,749	7,940	11,245
Sub-Total	868 (1.4%)	4,155 (3.5%)	n.a.	62,917	121,188	138,973	160,256
Mexico	n.a.	n.a.	n.a.	30,309	65,591	67,780	68,210
Total[4]	n.a.	n.a.	n.a.	93,226	186,779	206,753	228,446

Source: Compiled by the authors from data in SELA (1997); IDB and IRELA (1996); CEPAL (1997 a.); Ministry of Economy of the Argentine Republic (1996); Banco Central do Brasil (1996); Chilean Foreign Investments Committee; Banco de la República de Colombia; Peruvian Board of Foreign Investments and Technologies.

1. Preliminary estimate.
2. 1994.
3. 1997.
4. This line refers only to the total for these countries and not for the entire region.

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As can be seen in Table 2, until 1995 at least there were major differences in the level and nature of intra-regional investments. In 1995, the balance of accumulated investments between the countries in the Southern Common Market (*Mercado Común del Sur*, MERCOSUR) accounted for just 0.15% of the sub-regional GDP, and 0.3% in the case of the Andean Community. However, in the case of MERCOSUR, the proportion of total FDI corresponding to investments between member states increased from 0.5% in 1990 to 1.3% in 1995, while in the case of the Andean Community, this figure remained around 2%. On the other hand, total Chilean investment stock in MERCOSUR was 40% higher than all the investments among its member states in 1995, while accumulated Chilean investment in the Andean Community accounted for less than half the total intra-Andean investment stock in the same year.

Despite these variations and the lack of complete, detailed data on intra-regional FDI, the fragmentary empirical evidence available can nevertheless be used to illustrate a number of interesting tendencies in investment between different Latin American countries.

Intra-regional investments in MERCOSUR

The liberalization, deregulation and consolidation of MERCOSUR have made it a major magnet for investment.[12] Although no detailed information is available on the breakdown of FDI flows (except in the case of privatizations), indirect evidence does exist on the general tendencies. This shows, for example, that the sectoral pattern of intra-regional investment in MERCOSUR varies considerably in the different recipient countries. According to Bouzas[13], 89% of Argentine investment in Brazil is concentrated in the industrial sector, while in the case of Brazilian investment in Argentina, only 50% goes into manufacturing industry and 37% into the service sector.

In terms of the evolution of flows over time, very few Brazilian companies invested in Argentina before 1989. However, there was a steady increase in Brazilian investment after the creation of MERCOSUR in 1991 and during the economic upturn that followed the introduction of the convertibility programme. The implementation of the Brazilian stabilization programme (the *Plan Real*) and the opening-up of the economy attracted Argentine investments to Brazil. By mid-1995, the combined stock of Argentine, Paraguayan and Uruguayan investments in Brazil amounted to $457 million; a 500% increase compared to 1990, when it totalled $84 million. Meanwhile, total Brazilian investments in other MERCOSUR countries during the same period rose to approximately $530 million.

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Table 2
Intra-regional Investment in Latin America in the 1990s[1]
(in millions of US$ and percentage share, calculated to the nearest million and decimal point)

Host Country / Investor Country	Argentina		Brazil		Chile		Colombia		Ecuador		Peru		Venezuela	
	1989	1995	1990	1995	1990	1996	1990	1996	1990	1994	1990	1997	1990	1995
Argentina			34 30%	116 22%	36 22%	314 47%	2 1%	19 3%	14 13%	15 11%	4 8%	59 13%	2 7%	6 8%
Brazil	76 46%	455 22%			76 47%	159 24%	2 1%	56 9%	9 8%	21 15%	4 8%	28 6%	1 3%	3 4%
Uruguay	50 30%	51 3%	50 44%	296 56%	24 15%	97 14%		35 5%	3 3%	3 2%	24 47%	80 17%	20 67%	12 16%
Paraguay				44 8%	1	1	2 1%	3 1%						
Mercosur	126 76%	507 25%	84 80%	457 85%	136 85%	571 85%	6 3%	113 18%	26 24%	39 28%	32 63%	167 35%	23 77%	21 29%
Chile	5 3%	1473 71%	1 1%	30 6%			1 1%	52 8%	13 12%	15 10%	1 2%	257 55%		
Colombia	22 13%	16 1%		1	14 9%	17 3%			18 17%	27 20%	9 18%	8 2%	2 7%	38[2] 52%
Ecuador						1	28 14%	117 18%			1 2%	9 2%		
Peru	1				3 2%	7 1%	6 3%	14 2%	3 3%	3 2%			3 10%	3 4%
Venezuela	11 7%	18 1%	10 9%	17 3%	5 3%	47 7%	82 42%	314 49%	39 36%	42 30%	7 14%	10 2%		
Andean Community	34 20%	34 2%	10 9%	19 4%	22 14%	73 11%	116 59%	445 69%	60 56%	72 52%	17 33%	27 6%	5 17%	41 56%
Mexico	1 1%	50 2%	18 16%	30 6%	3 2%	29 4%	11 5%	34 5%	8 7%	11 8%		20 4%		10 14%
Latin America	166 2%	2063 8%	114	535 1%	161 3%	673 3%	197 6%	643 8%	108 8%	138 5%	51 4%	470 10%	30 1%	73 1%
L. America and the Caribbean	412 6%	3826 16%	1942 5%	5100 9%	451 7%	1441 7%	393 11%	1298 16%	345 25%	439 16%	246 19%	526 11%	305 9%	743 11%
Total	6942	24630	38965	58083	6424	20270	3500	8363	1370	2708	1330	6751	3581	6749

Source: Compiled by the authors from the sources listed in Table 1.
1. A blank indicates there is no investment or that investment amounts to less than $500,000.
2. According to the Banco de la República de Colombia, Colombian investment amounted to $ 118 million.

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As noted above, almost 90% of the stock of Argentine investments in Brazil is concentrated in manufacturing industry. The food and beverages industry accounts for the bulk of this investment (almost 75%), textiles for 14%, and the chemical industries 5%. In contrast, Brazilian investments in Argentina are more diverse; although manufacturing industry absorbs almost 60%, the remainder is divided between the service sector (37%) and commerce (3%). The breakdown of investment within manufacturing industry is as follows: automobile production and parts 43%, metallurgy 18%, food and beverages 9%, and chemicals 8%. In the service sector, banks account for half the total investment, while the rest is divided almost equally between insurance and financial institutions. As Bouzas explains, "while there is considerable Brazilian investment in the service sector in Argentina, the opposite is not true. This difference is partly due to the different conditions of access to the sector in Brazil".[14]

Finally, Brazilian investments in Paraguay, like Paraguayan and Uruguayan investments in Brazil, are concentrated in the service sector (banks and insurance companies in the case of the former, and real estate and retail distribution in the latter). While almost all Brazilian investment in Paraguay has centred on financial services (banks, financial and trust institutions), in Uruguay, Brazilian companies have interests in a broader variety of sectors. Even though total intra-regional investments flows are still relatively small, the expansion and diversification of intra-regional trade has been accompanied by a growing number of operations in distribution and retailing, as companies attempt to consolidate their position in the larger market.

More recently, a number of joint investments have been made by companies in the MERCOSUR countries, and between these and their counterparts in Chile. Although no exact information is available, the value of these operations can be seen from the number of alliances between Argentine and Brazilian companies. Most of these projects are in manufacturing industry (45%). As in the case of total intra-regional flows, a large proportion of these joint ventures are in the service sector (41%), while commerce accounts for another 14% of the total. Within manufacturing industry, the principal sectors for these joint investments include food and beverages (12%), followed by vehicle parts (8%), and automobile engines, chemical products, agricultural machinery and equipment, with 4% each. The breakdown of operations in the service sector is as follows: banks (11%), telecommunications (6%), information technology (4%), and press and communications, advertising, and insurance with 3% each.[15]

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Chilean investment in Latin America

By mid-1994, Chilean foreign investments amounted to over $8.6 billion.[16] Over 75% of all Chilean FDI stock was held in the four Southern Cone countries. Argentina received the highest proportion (53%), followed by Peru (17.4%), Brazil (3.6%) and Bolivia (2.6%) (see Table 3).

The scale of Chilean FDI is explained by a number of factors, the most important being the early liberalization, deregulation and privatization of the Chilean economy; this process has allowed the country to expand its foreign economic relations earlier than its neighbours. Throughout this period, Chilean investments have been closely linked to the privatization of state-owned companies. According to the Chilean Foreign Investment Committee, Chilean companies that invest abroad tend to do so in sectors in which they already have extensive experience in the domestic market. In general, Chilean investment in Latin America takes the form of strategic alliances with foreign companies in sectors in which the Chilean investors are familiar with the economic environment. Hence, the most recent Chilean investments in electricity, communications, mining, banking and pension funds have all been made through partnerships with multinationals or Latin American companies.[17]

For example, the largest Chilean electricity companies, Enersis and Endesa, operate in the Latin American market in a number of different ways: in partnership with foreign companies; autonomously (Endesa operates 16% of the installed capacity in Argentina, 27% in Peru, and 6% in Colombia);[18] or in association with local companies in each market, as in the case of the consortium Enersis formed with Argentine and Peruvian companies to generate and distribute electricity in Argentina, Chile and Peru.

In terms of the sectoral distribution of Chilean investment, by the end of July 1996 the electricity sector accounted for 37% of the total, followed by manufacturing industry, with almost 30%, and commerce and banking, with over 4% each. Despite this relatively high level of concentration in the electricity sector, there has been some diversification of Chilean interests in recent years. Chile is also a major investor in MERCOSUR. This essentially reflects the very active role played by Chilean companies in the privatization processes in Argentina, especially in the tertiary sector (financial and other services).[19] On the other hand, Argentina is the main Latin American investor in Chile. Argentine companies supplied almost half of the capital inflows to Chile from Latin America, and 1.5% of the total FDI in the country in the period 1974-96. Argentine investments are concentrated in the transport and storage sector,

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electricity, and construction. However, despite this strong Argentine presence in Chile, the accumulated stock of Argentine investment there was much smaller than the total Chilean investment in Argentina ($315 million compared to almost $1.5 billion).

As for Chilean investment in the Andean countries, Peru is by far the most important recipient (with 70% of all Chilean investments made in the Andean region before 1995), essentially because of the privatization of its electricity companies.[20] Another interesting case is that of Colombia, where the Chilean electricity companies Endesa Chile and Codensa formed a partnership with the Spanish company Endesa España at the end of 1997, in order to acquire the Empresa de Energía Eléctrica de Bogotá for almost $2.1 billion. This single operation represented four times the accumulated value of all Latin American investments in Colombia during the previous six years, thereby converting Chile into the largest Latin American investor in Colombia in the period 1992-97, with a share of almost 75% of the total, followed by Venezuela (12%) and Ecuador (5%).[21]

Table 3
Chilean Investment Worldwide[1], 1990 - July 1996

Country	Total Investments (in millions of US$)	Share (%)	Total value of projects (millions of US$)	Share (%)
Argentina	4,554	52.7	8,106	49.3
Peru	1,498	17.4	3,100	18.8
Brazil	340	3.9	1,305	7.9
Panama	312	3.6	315	1.9
Bolivia	228	2.6	240	1.5
Russia	153	1.8	153	0.9
Mexico	119	1.4	1,176	7.2
Caribbean	634	7.3	752	4.6
Others	797	9.3	1,304	7.9
Total	8,634	100.0	16,451	100.0

Source: Compiled by the authors from data provided by the Chilean Foreign Investment Committee.
Others: Includes 28 countries whose individual investments account for less than 1% of the total.
1. As well as Chilean FDI, the figures include loans to subsidiaries and other forms of finance. The Central Bank of Chile only records the capital outflows defined in Section XII of the International Currency Act. This explains the significant discrepancies in the figures for the value of the investments in the different sources.

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Intra-regional investment in the Andean Community

Another interesting question is the relative intensity of investment flows between the Andean countries. The most important flows are as follows: the acquisition of Colombian financial institutions by their Venezuelan counterparts (accounting for 70% of all Venezuelan investments in Colombia) following the deregulation of the sector; Colombian investments in Venezuela, mainly in wholesale distribution (55% of the total) and financial and other services;[22] and Ecuadorian investments in Colombia, which are also concentrated in the financial sector (83%) and, to a lesser degree, transport (17%).[23] Another interesting feature of intra-Andean investment (which, according to the Banco de la República de Colombia, amounted to an accumulated total of almost $720 million in 1996), is the way that the flows are very unevenly distributed between the different countries in the region. Investments between Colombia and Venezuela accounted for almost two-thirds of the total, those between Colombia and Ecuador for another 20%, and those between Ecuador and Venezuela for 8%.

Judging by the evolution of the flows between Colombia and Venezuela, which amounted to $32 million between January and August 1997, this pattern may have been consolidated more recently. Almost two-thirds of all Latin American (excluding Panama and the Caribbean) investment in Colombia in the period 1992-97 came from Venezuela and Ecuador, whereas the main recipient of Colombian investments in Latin America was Venezuela (78%).

However, these figures must be seen within the broader context of global FDI. Despite the major upsurge in Colombian investment in Venezuela since 1992 (almost 85% of the accumulated stock dates from after 1991), Colombia was the source of only around 2% of all FDI stock in Venezuela before 1996.[24] And although Colombian investment is no longer confined to wholesale distribution (it now also includes timber and chemical products), it still involves a relatively small number of investor companies. As Iturbe has noted "investments are highly concentrated; for example, 85.6% of recorded investments came from nine investors, on average investing some $4.1 million, while there is also a very large number of small investors, 92 of which account for only 14% of total investment...of these, 64 have average investments of less than $20,000".[25]

Likewise, in 1996 Venezuela was the source of only 3.9% of all foreign investment stock in Colombia.[26] The Colombian financial sector absorbed most of this capital, accounting for 67% of Venezuelan investment in the period 1992-97; in fact, Venezuela provided 41.3% of all foreign investment in this sector in

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1993 and 33% in 1995.[27] As for manufacturing industry (which represented a quarter of Venezuelan investments in Colombia between 1992 and 1997), the largest investment operations have been in the chemical, rubber and plastics industries and, albeit to a lesser extent, beverages and electrical equipment. Companies from the two countries have also formed strategic alliances to complement and distribute their products (including axles, drive belts, and shock absorbers).

A note on Mexican foreign investment

Even less information is available on Mexican foreign investment, since Mexico does not record capital outflows. However, there are a number of reports which offer some insight into the general characteristics and evolution of Mexican investment in Latin America.[28] They suggest that the strategy of Mexican investors mainly involves the acquisition of companies in the region (and even in global markets) in order to improve their competitive position, penetrate new markets, and assure their economic integration with the rest of Latin America.[29] Mexican foreign investment has been closely linked to privatization programmes, particularly in Central America, as well as some branches of manufacturing industry and the service sector. Investments have tended to be concentrated in just a few countries, especially the United States.

A number of factors explain why Mexican investment has been concentrated in the United States. The most important of these have been the rapid liberalization of the Mexican economy since the second half of the 1980s, and the implementation of the North American Free Trade Agreement (NAFTA) this decade, which has reinforced the traditional trade links between the two countries (over 70% of Mexican exports go to the United States). Within Latin America itself, until 1989 Mexican investments were concentrated in Central America. In the 1990s, however, this pattern has changed, with a considerable expansion of flows towards South American countries such as Argentina and Colombia.

The fact that Mexican investment is concentrated in relatively few sectors reflects the existence of large Mexican conglomerates operating in these areas, such as Cementos de México (CEMEX), Teléfonos de México (TELMEX), Grupo Alfa and Vitro. In practice, Mexican foreign investment has tended to flow above all to non-metallic minerals (cement and glass), telecommunications and, albeit to a lesser degree, other activities such as construction. In 1989, for example, Vitro (the world's third largest glass manufacturer), acquired a US

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company for an estimated $900 million, as well as a number of other companies in Central America, Bolivia, Colombia and Peru. More recently, Vitro has formed an alliance with a Brazilian company to supply the MERCOSUR market. At the same time, CEMEX (the fourth largest cement manufacturer in the world) has acquired plants in Spain, the United States, Central America and Colombia, for an estimated total value of $1.8 billion. More recently, TELMEX, Grupo Alfa, and Grupo Banacci have acquired US telecommunications companies worth more than $1.65 billion.[30]

Conclusions

The increase in FDI flows to Latin America and the Caribbean over the course of the 1990s has been closely linked to the emergence of a more attractive economic, regulatory and legal framework for investment in the region. This favourable situation is the result of the macroeconomic reforms and privatization processes, as well as the changes in regional integration, towards a more "outward looking" model of development. In these circumstances, the potential benefits of FDI (such as technology transfers, higher productivity, employment, training, and the expansion and diversification of exports) can be expected to be considerably greater than those obtained in a more restrictive environment of the type that existed in the region during years of import substitution-based development.

Although there has been a notable increase in direct intra-regional investment in Latin America, it is still relatively modest. While the total stock of intra-Latin American investment increased fivefold during the first half of the 1990s, it still accounted for little more than 3.5% of the total FDI accumulated in eight Latin American countries since 1995. Intra-regional investment has tended to be concentrated in just a few sectors, generally those in which investor companies are already operating at home, particularly in public utilities, natural resources and banking. Nonetheless, there are major differences both in the intensity and nature of intra-regional investments in Latin America.

In 1995, the accumulated balance of intra-MERCOSUR investments amounted to just 0.15% of sub- regional GDP. In the Andean Community, on the other hand, intra-regional FDI was worth twice as much (in terms of its contribution to the combined GDP of member states). The greater dynamism of the Andean Community is largely a result of the flows of investment between Colombia and Venezuela, which have been concentrated in the financial sector and wholesale distribution. In contrast, intra-MERCOSUR investments were

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mainly concentrated in the manufacturing industry, and involved Argentina and Brazil above all. There is a tendency towards specialization in both these countries: most Argentine investment in Brazil is in the food and beverages industry, while the automobile, automobile parts, metallurgical and chemical industries absorb most Brazilian investments in Argentina.

Chile, the regional pioneer in terms of exporting capital, exemplifies the tendency for intra-regional investment in Latin America to concentrate in relatively few countries and sectors. Almost three-quarters of all Chilean foreign investment stock in mid-1996 was located in Argentina (53%) and Peru (17%), and in both countries the energy sector accounted for the bulk (over 50%) of the total value of stock. The main reason for this is that the initial phase of investments in the region was closely linked to the privatization process, in which many Latin American firms joined forces with foreign companies to acquire former state-owned enterprises.

Regardless of the recent pattern of investment, there is likely to be an increase in the number of intra-regional and extra-regional corporate alliances, given the greater certainty regarding preferential access to the enlarged markets formed by members of regional organizations; this trend is likely to continue as these organizations develop in the future. Exploiting assets such as location advantages, specialization and complementary processes, among others, these alliances should promote increased investment in manufacturing industry and, in time, form a platform for the development of truly multinational Latin American companies. This, at least, is suggested by the range of joint manufacturing operations now being planned by companies in a number of countries throughout the region.

Finally, it should be stressed that this analysis is based on partial and fragmentary data; given the shortcomings of the capital flow records kept by various countries in the region, this is the only information available. This problem, which has been exacerbated by the opening of the capital accounts, inevitably frustrates any attempt to analyze the economic consequences of foreign investment and its potential costs and benefits. Moreover, the differences in the methods used to record data tend to distort the figures for intra-regional investment. Latin American countries would do well to make improvements in this area. In a favourable climate of liberalization and deregulation of foreign investments, records of this kind would be no obstacle to foreign investment inflows, and would make it far easier to monitor and evaluate investment trends. The availability of more accurate and complete statistical data, and the possibility of carrying out more reliable empirical studies, would benefit both

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investors and those responsible for macroeconomic planning and regional integration.

Annex:
Foreign Investment Regimes in Latin America

Since the late 1980s, the main attractions for FDI in Latin America have been economic reform and liberalization, and the privatization process. During the 1990s, the liberalization and deregulation of investment regulations has constituted a further incentive for investment.

According to technical studies drawn up for the Free Trade Area of the Americas (FTAA) Investment Working Party,[31] the legal and institutional framework for foreign investment in Latin America and the Caribbean is characterized by its increasing homogeneity; this is a reflection of the measures taken by the countries in the region to create a stable legal climate for foreign investment. The most noteworthy features of these changes are the introduction of laws and regulations to protect both investors and investment, and the progressive liberalization of different sectors of the economy that had been closed to FDI during the years of policies based on import substitution. These changes were reinforced by the proliferation of bilateral and multinational investment agreements in the 1990s, which were explicitly designed to promote investment, either autonomously or as part of agreements on free trade or regional economic integration.

Bilateral integration agreements establishing legal measures to facilitate investment include the agreements signed by Mexico and Chile, Costa Rica and Bolivia and, more recently, Chile and Canada. The most important sub-regional agreements in this respect are NAFTA, the Free Trade Agreement between Mexico, Colombia and Venezuela (the Group of Three or *Grupo de los Tres*, G-3), the Andean Community and MERCOSUR. These sub-regional integration agreements include rules standardizing the treatment of foreign investment between the member states. All the treaties dictate equal treatment for foreign and national investors through rules conceding "national treatment" and the status of most favoured nation, as well as guaranteeing investment transfers, protecting against expropriation, applying appropriate compensation measures, and resolving disputes. In some cases, however, these treaties also establish implementation requirements or define reserved sectors (G-3, for example).

In general, there is a broad tendency for legislation to reinforce the protection and promotion of foreign investment in Latin America and the

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Caribbean. However, there are still considerable variations in the type and extent of regulations, and in the degree of liberalization in different sectors of the economy. A recent comparative analysis of bilateral investment agreements[32] concluded that, in the American hemisphere, there are two different models in terms of coverage, the extent of regulations, and degree of liberalization of investment. First, NAFTA and similar agreements promoted by the United States and more recently Canada, which have stricter regulations, and include the right of entry for investors into all sectors except those explicitly mentioned in the agreements. Second, the traditional European model, which is used more frequently in Latin America and allows the recipient state to decide whether or not to allow the entry of foreign investments.

NOTES

[1] The balance of foreign investment rose by barely 50% during the first half of the 1980s, compared to the twofold increase during the first half of the 1990s, when the process of economic liberalization was in full swing.

[2] See, amongst others: J.H. Dunning (1993); M. Blomstrom, M. and A. Kokko, "How Foreign Direct Investment affects Host Countries", *Policy Research Working Papers* No. 1745, Washington D.C.: The World Bank, March 1997.

[3] J.H. Dunning, *The Theory of Transnational Corporations*, vol. 1, London: UNTLNC, 1993.

[4] M. Blomstrom and A. Kokko, "Regional Integration and Foreign Direct Investment", Washington D.C.: The World Bank (unpublished manuscript), 1997.

[5] One of the models developed along these lines can be found in: W.J. Ethier, "Regionalism in a Multilateral World" (unpublished manuscript), 1996.

[6] A.L. Winters, "Assessing Regional Integration Agreements", Washington D. C.: The World Bank, June 1997, p. 35; and C.E. Barfield, "Regionalism and US Trade Policy", in: J. Bhagwati and A. Panagariya (eds.), *The Economics of Preferential Trade Agreements*, AEI Press, Washington D. C., 1996, p. 42.

[7] For an analysis of Latin American privatizations, see: R. Devlin and R. Cominetti, *La crisis de la empresa pública, las privatizaciones y la equidad social*, Serie Reformas Política Pública 26, Santiago de Chile: CEPAL, 1994.

[8] J.H. Dunning, "Re-evaluating the Benefits of Foreign Direct Investment", *Transnational Corporations* 3:1, 1994.

[9] Any analysis of intra-regional investments in Latin America faces the serious problem of the lack of comparable information. Recent ECLAC and SELA reports indicate that the information available on investment flows is at best fragmentary and, at worst, anecdotal.

[10] The main sources of information used here are publications of ECLAC and central banks and, in particular, the SELA document, "Financiamiento externo, deuda externa y flujos de capital intraregional en América Latina y el Caribe", SP/XXIIIO/Di, No. 7, 1997.

[11] When the Caribbean is included, the distribution is as follows: Brazil, 33.8%; Argentina, 25.4%; Colombia, 12.2% and Chile, 9.1%.

[12] See C. Sepúlveda and A. Vera, "Mercosur: Logros y Desafios", Washington, D.C.: BID, May 1997.

[13] R. Bouzas, *Informe MERCOSUR*. 1, July-December 1996, Buenos Aires: INTEL, 1997, pp. 15-16.

[14] R. Bouzas, (1997), *ibid.*, p. 16.

[15] The Argentine Embassy in Brazil, "Argentina-Brazil. Comercio, inversiones e integración física. Hacia una nueva relación en la construcción de un espacio competitivo común", Brasilia, August 1995.

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[16] Comité de Inversión Extranjera, "La inversión de capitales chilenos en el mundo", Santiago de Chile, August 1996, p.2. (unpublished manuscript). The Santiago Chamber of Commerce estimates that accumulated Chilean investment down to the first semester of 1996 amounted to over $10.7 billion.

[17] For a relatively detailed list of recent Chilean strategic alliances with multinationals, see J.M. Benavente, "Antecedentes generales sobre la inversión extranjera en Chile", 1997. Report produced for the "MAI and the dynamic emerging economies" Workshop, OECD, Mexico, 10-11, December.

[18] SELA (1997), *ibid.*, p. 9.

[19] Accumulated Chilean investment in Argentina amounted to almost $1.5 billion at the end of 1995.

[20] And, to a much lesser extent, the acquisition of some existing companies, including some in the food industry.

[21] Equally, the electricity sector would be the main destination, with a share of 74%, overtaking the financial (15%), manufacturing (6%) and transport (2%) sectors.

[22] Accumulated Venezuelan investments in Colombia amounted to $314 million in 1996. There is some doubt as to the accumulated Colombian investment in Venezuela: according to the records of the Venezuelan Foreign Investment Office, they total $38 million, whilst the Banco de la República maintains that they amount to $146 million.

[23] Total Ecuadorean investment in Colombia amounted to $117 million at the end of 1996.

[24] Based on figures published by the Banco de la República de Colombia.

[25] E. Iturbe de Blanco, "Las relaciones de comercio e inversiones entre Colombia y Venezuela", *Serie Intal, Documento de Trabajo* 3, Buenos Aires, October 1997, p.20.

[26] According to the Banco de la República's figures for Venezuelan investment in Colombia.

[27] Iturbe de Blanco (1997), p. 23.

[28] See, among others, Griffith-Jones, S. et al., "Financial Flows for Regional Integration", paper prepared for the FONDAD Conference on "Regional Integration and Global Co-operation. The case of Latin America and the Caribbean", Santiago de Chile, March 1995 (unpublished manuscript).

[29] Griffith Jones (1995), p. 19.

[30] SELA (1997), ibid..

[31] See, among others; BID, *Regímenes de Inversión Extranjera en las Américas. Un Estudio Comparativo*, Washington D.C.: BID, August 1997; and OEA, *Acuerdos de Inversión en el Hemisferio Occidental: Un compendio*, Washington, D.C., April 1997.

[32] A. González, "Las negociaciones internacionales sobre inversión extranjera. Elementos para la posición de los países de América Latina y el Caribe", SELA, November 1997, p. 11.

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ANNEX I

FDI STATISTICS: METHODOLOGICAL ISSUES*

Introduction

Given the substantial growth of FDI flows over recent years, FDI statistics have become increasingly important both for economic analysis and for policy analysis. Since FDI constitutes an important element of international financial flows, FDI statistics are essential in order to measure the internationalization of economic activities. At the same time, the attractiveness of a particular country as an investment location is often evaluated using data on its stock and/or inflows of FDI.

It should be borne in mind, however, that FDI statistics suffer from a number of limitations. The use of distinct methods and criteria to register and keep track of FDI operations makes it difficult to compare the data from different countries. This incomparability is essentially due to four factors. Firstly, the definition of what actually constitutes FDI varies from country to country. Secondly, the items included in national FDI statistics also vary. Thirdly, the systems for compiling figures are different and only make it possible to calculate certain types of FDI, or different time frames are used when recording FDI. Finally, national statistics may not reflect the real final destination of FDI.

Despite the attempts of the International Monetary Fund (IMF) and the Organization for Economic Cooperation and Development (OECD) to achieve international harmonization on recording and reporting practices, many of the available statistics on direct investment are still not compiled in accordance with international guidelines. The preliminary results of an IMF/OECD survey on the methodology used for measuring FDI suggest that there are a number of shortcomings in the national systems used to compile FDI data. The information collated from the regular FDI questionnaire circulated by the European Commission's Statistical Office (EUROSTAT) also shows that no European Union (EU) Member States supplies all the standard items in accordance with the recommendations of the IMF and the OECD (EUROSTAT, 1997). Differences in FDI definitions, measurement and recording methods limit the comparability of FDI statistics and can lead to misinterpretations of the data.

* This chapter and the tables were prepared by Geog Saul, Consultant, Madrid.

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This Annex highlights the discrepancies in the definitions, the statistical coverage, and the recording methods used by the countries for which data is presented in this study. It also discusses the problems involved in obtaining data on the geographic distribution of FDI, and the resulting statistical problems. The sources are also examined, along with the procedures used to estimate the FDI data for Japan and Spain. Finally, a number of technical notes are presented.

Definition of FDI

The IMF and the OECD are the principal sources for guidelines on the definition of FDI and the procedures that should be used to measure FDI. The fifth (1993) edition of the IMF *Balance of Payments Manual* (BOPM5) and the third (1996) edition of the *Detailed Benchmark Definition of Foreign Direct Investment* (BD3) contain the most widely used definitions of FDI. The BD3 is fully consistent with the BOPM5, although it provides further information in the form of an operational guide so that professional statisticians can standardize the different methods used to calculate FDI.

Generally speaking, FDI refers to the category of international investment made by an incorporated or non-incorporated resident entity in one economy in order to obtain a lasting interest in an enterprise in another country (the resident entity is the direct investor and the enterprise is the direct investment enterprise). A lasting interest implies the existence of a long-term relationship between the direct investor and the enterprise, as well as that the investor has a significant degree of influence on the management of the enterprise. Direct investment comprises not only the initial transactions establishing the relationship between investor and the enterprise, but also all subsequent transactions between them and among affiliated enterprises, both incorporated and unincorporated.

On Portfolio Investment

In contrast to direct investment, *portfolio investment* covers financial transactions (other than those included in direct investment and reserves) in the form of equity or debt securities. Debt instruments include bonds and notes, money market instruments and financial derivatives. One notable characteristic of portfolio investment is that the securities are usually issued and traded in organized financial markets, implying that portfolio investors do not acquire greater influence over the company in which they invest. *Other investments* includes commercial credits, long and short-term loans, cash and deposits, and other accounts receivable or payable (inter-company transactions of the same type but related to direct investment are not registered in this category).

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The most important feature in defining FDI is the relative degree of influence of the investors in management. Usually the investor obtains an effective voice in the management of a direct investment enterprise through a lasting interest. In BOPM5, lasting interest is defined as ownership of 10% of the equity of a direct investment enterprise. In practice this may be contradictory, since an investor could own more than 10% without having a lasting influence in management, or own less than 10% and have effective decision-making powers. A number of countries adopt a flexible attitude to the 10% minimum stake, and Germany and the United Kingdom have fixed the threshold at 20%.

The definition distinguishes between three types of foreign investment companies. Affiliates are defined as companies in which the direct investor has a stake of more than 50%; associated companies are those where the stake is between 10% and 50%; and branches are those companies which are fully or partially owned by the parent company. FDI also includes the stake held indirectly by the direct investor in affiliates of the direct investment company. A number of countries do not include this type of FDI, with the result that there is a danger of underestimating total FDI flows and reinvested assets. The OECD has recommended that these countries should require companies to produce consolidated accounts of their operations world-wide.

Components of FDI Statistics

FDI statistics have three main components: share capital, inter-company debt transactions, and reinvested earnings. However, not all countries include all these items in their statistics.

Equity capital includes outflows of capital that occur when a direct investor company increases its investment in any of its existing foreign subsidiaries or makes a new investment in a foreign company, either by acquiring an existing business or by establishing a new one. In accordance with the recommendations of the IMF (1993) and the OECD (1996), the statistics should not only include contributions of capital, but also the provision of machinery or the financing of assets through loans from local entities.

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Differences in the Definition and Reported Components of FDI by Country of Origin (end of 1996)					
	Percent of ownership	Components of FDI			
		Equity capital	Inter-company debt transactions	Reinvested profits	Others
Austria	10%	Yes	Not included	N.a. by country	Excludes non-cash transactions
Belgium	No minimum threshold	Yes	—	Not included	Excludes non-cash transactions
Denmark	10%	Yes	Includes inter-company loans	N.a. by country	—
Finland	10%	Yes	Includes inter-company loans	N.a. by country	Excludes trade credit between parent and affiliate
France	10%	Yes	Includes short-and long-term loans	N.a. by country	Excludes FDI financed through local borrowing
Germany	20%	Yes	Excludes short-term loans	Included	Excludes trade credit between parent and affiliates
Italy	20%	Yes	—	Not included	Excludes FDI in real estate
Japan	No minimum threshold	Yes	Excludes short-term loans	Not included	Excludes trade credit and equity without payment
Netherlands	No minimum threshold	Yes	Not included	Included until 1995	Excludes FDI via *holdings* in the Netherlands
Portugal	10%	Yes	Includes short- and long-term loans	Included	Excludes trade credit between parent and affiliate
Spain	10%	Yes	Includes short- and long-term loans	Not included	Excludes non-cash transactions
Sweden	—	Yes	Excludes short-term loans	N.a. by country	Excludes trade credits and non-commercial real estate
Switzerland	10%	Yes	Includes inter-company loans	Included	—
United Kingdom	20%	Yes	Included, but in net values	Included	—
United States	10%	Yes	Includes inter-company loans	Included	—

Source: Compiled by the author from EUROSTAT (1997) and OECD (1997) and information obtained from central banks and statistical agencies.

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Inter-company debt transactions are those which take place when an affiliate receives a loan from the parent company, or when the direct investor receives a loan from its affiliate. These loans cover the borrowing and lending of funds including debt securities and trade credit. Some countries include certain types of inter-company debt flows, while others do not. These flows include both short and long-term loans. In 1996, inter-company debt transactions from the United States, for example, accounted for almost 10% of US capital outflows (Bargas, 1997).

Reinvested earnings refer to the direct investor's participation in the undistributed profits of its foreign affiliates. They are calculated after corporate tax has been deducted from total earnings and represent the difference between the direct investor's share of its affiliate's current earnings and the dividends paid by the affiliate to its parent company. Reinvested earnings are negative when the affiliate makes a loss or the parent company receives higher dividends than its share of current earnings.

Reinvested earnings currently constitute an important component of direct investment. They accounted for over 65% of the total flows of FDI registered in the United States in 1996, compared to an average of 36% in the period 1982-94. These figures indicate the increasing importance of this component of FDI. Reinvested earnings also accounted for 50% of all Swiss FDI in 1995.

Reinvested earnings are not treated in the same way in all national statistics. The main differences are generally due to different allocation periods or the use of different methods of calculation. Some countries allocate reinvested earnings according to the period in which they are going to be used (Germany, for example), rather than the period in which they are obtained (as the United Kingdom does). Reinvested earnings are generally not included in the statistics of those countries which use settlement registers of theirs central banks statistics as the primary data source. In any case, even when earnings are registered, the data may not necessarily be complete, as the statistical information systems may not capture all the foreign activities of national companies, nor all those of foreign companies in their own economy. In many cases, companies seek to minimize tax payments by manipulating the figures for the earnings of their affiliates. This detracts from the value and significance of FDI statistics.

One of the most common difficulties in any attempt to measure FDI is the lack of information on reinvested earnings. In this study, while six source countries of FDI include reinvested earnings in their FDI figures, the other nine do not.

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Measurement and Collection of FDI Statistics

Statistics on FDI are obtained from three primary sources of data collection: the international transactions reporting system, enterprise surveys, and investment notifications and approvals (IMF, 1995).

Statistics based on data obtained from an international transaction reporting system generally only cover flows of equity capital which are registered by settlements. Much of the necessary information is available in banking records. However, non-cash transactions (such as those involving reinvested earnings, equity in the form of machinery, and inter-company debts) are not reflected in these figures. This is because, unlike flows of equity capital, these movements do not involve foreign currency transactions which are recorded in the registers of the central bank.

Most countries use a combination of data collection systems when compiling their FDI statistics. Those countries that base their balance of payments statistics on an international transactions reporting system often supplement the information with declarations from enterprises and/or information from annual enterprise surveys.

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FDI Collection Systems of Investor Countries				
	International Transactions	Company surveys	Notifications or Approvals	Description
Austria	X	X		The National Bank of Austria collects balance of payments data and conducts annual surveys on the stock data.
Belgium	X	X		Until 1994, the figures were based on bank settlements. Since 1995, the system has changed, and now includes the use of surveys.
Denmark	X	X		The National Bank of Denmark compiles balance of payments statistics using bank settlements. Stock surveys are undertaken irregularly.
Finland	X	X		The information consists of data on payments abroad, monthly reports on assets and liabilities and annual FDI reports.
France	X	X		The collection system is based on bank liquidations/statements and company declarations. The stock of information is recorded in annual reports.[1]
Germany	X	X		The information on flows is based on reports of transactions from companies and banks. The stock of data is recorded in annual reports.
Italy	X			The *Ufficio Italiano dei Cambi* registers foreign currency declarations. The figures for the stock are obtained from the accumulation of flows since the previous stock.
Japan	X		X	The Bank of Japan publishes FDI data for balance of payments purposes. The Finance Ministry compiles figures from notifications.
Netherlands	X	X		Data on FDI is obtained through declarations of external transactions. The information on the stock is based on annual reports.
Portugal	X			The information is obtained from statistical declarations, bank liquidations/statements and direct reports from economic actors.

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	International Transactions	Company surveys	Notifications or Approvals	Description
Spain	X		X	The Bank of Spain compiles data based on bank liquidations/statements. The Ministry of the Economy and Finance collates figures from notifications.
Sweden	X	X		The Bank of Sweden compiles information for balance of payments purposes. Annual reports on stocks are also produced.
Switzerland	X	X		The National Bank of Switzerland collects information for its balance of payments statistics. Annual reports are also produced on the stock.
U. Kingdom		X		The Office for National Statistics produces quarterly and annual surveys on FDI, which are completed with data from the central bank.
USA		X		The Bureau of Economic Analysis publishes quarterly and annual FDI reports.

1 As well as the Bank of France, the Department for Foreign Economic Relations of the Ministry of Economy and Finance also publishes FDI information in the form of an annual report on the economic activities of French-owned foreign subsidiaries.

Source: Based on EUROSTAT (1997) and OECD (1997), and from central banks and statistical agencies.

The FDI statistics based on company surveys are compiled from data obtained from government surveys. The main purpose of these surveys is to collate detailed information on the financial and operational data of direct investors. Company surveys supply the most complete record of FDI transactions and stock data. They also provide information on other economic activities relating to FDI, such as sales (domestic and foreign), earnings, employment, and the contribution of value added of foreign affiliates. Most countries which have significant flows of FDI use company surveys to obtain information on the different dimensions of foreign investment.

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FDI Data from Latin American and Caribbean Sources

FDI data reported by Latin American and Caribbean countries, which are also used in this publication, contain some additional factors, which limit the reliability and quality of these statistics. A recent ECLAC analysis focuses on the deficiencies of FDI statistics prepared by the authorities of Latin American/Caribbean countries. Above others, the following problems are highlighted. A) FDI registers are lacking or incomplete. This is particularly caused by an insufficient institutional development and missing resources. B) In some countries there is more than one organism collecting FDI data mainly for one specific economic sector. Thus, FDI figures can show high disparities between the different national sources. A central co-ordination entity often does not exist. C) Several conceptual and methodological differences exist from country to country limiting the comparability of data between countries.

The user should bear in mind, that FDI statistics from Latin American and Caribbean countries contain serious limitations affecting the reliability of the data and should therefore be interpreted with caution.

Data on investment approvals/notifications is collected by government agencies, in accordance with the national regulations on FDI. The approval/notifications system is rarely set up according to balance of payments requirements. FDI statistics are often a by-product of this collection system. In general reinvested earnings, inter-company loans and liquidations of investment are not recorded. There could be significant time lags between approval and actual investment, and the approved investment may never be realised. Information on non-equity transactions, such as lending and inter-company accounts, is limited.

The countries analyzed in this study generally use figures on international transactions and/or company surveys to compile FDI statistics. A variety of different sources can be used to trace a single component of the balance of payments accounts. Japan and Spain also provide data for approvals and notifications, which contain more detailed information than the balance of payments data.

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An example: The German Data Collection System

The FDI data collectiòn system used by the German Federal Bank (Deutsche Bundesbank) combines information from an international transactions reporting system with company surveys. The Federal Bank receives reports from German companies and banks on their direct investment abroad. The direct investor must present payment reports when the investment is made. The Federal Bank uses this information to compile statistics on FDI flows. The data are then complemented with information obtained from annual company reports. In particular, these annual reports provide figures on reinvested earnings which are added to the FDI flows.

The annual reports of German direct investors are used to compile information on FDI stock. These reports include information on changes in the valuation of stocks, as well as reinvested earnings. However, it should be noted that the figures for reinvested earnings are based on a company's operational balance sheet, and do not include the revaluation of stocks. The data on stocks published by the German Federal Bank include reinvested earnings for the year in which the profits/losses are obtained. In contrast, the reinvested earnings which are included as a component of FDI flows are registered when the company calculates profit flows. This occurs one year after the figures are presented in the stock statistics.

German FDI in Brazil and Mexico
(in millions of DM)

	Brazil				Mexico			
	Stock	Flow of FDI	Of which:		Stock	Flow of FDI	Of which:	
			Equity + other capital	Reinvested earnings			Equity + other capital	Reinvested earnings
1993	10,586	-203	47	-250	4,118	2	52	-50
1994	14,404	733	308	425	3,089	129	179	-50
1995	12,134	1,699	699	1,000	2,943	-25	575	-600
1996	n.a.	237	423	-186	n.a.	32	-73	105

Source: Deutsche Bundesbank, *Zahlungsbilanzstatistik*, October 1997, Frankfurt; Deutsche Bundesbank, *Kapitalverflechtung mit dem Ausland*, May 1997, Frankfurt.

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Between 1993 and the end of 1994, the stock of German FDI in Mexico declined from some 4.1 billion DM to around 3.1 billion DM, largely as a result of the devaluation of the peso and company losses. The 600 million DM of reinvested profits (losses) which were reported in 1995 were actually made in 1994 and included in the FDI stock that year. However, the 600 million DM of losses were registered in the 1995 figures for FDI flows, when in fact new FDI totalled 575 million DM. This resulted in a negative FDI flow in 1995 of 25 million DM. In 1995, reinvested earnings included in FDI flows from Germany to Brazil totalled 1 billion DM. This profit was obtained in 1994 (and included in the FDI stock statistics that year), but it was registered in the FDI flow statistics in 1995. Therefore, in order to avoid misinterpretations when analyzing German FDI figures, the difference between the year when the profits are made and the year they are earnings must be taken into account.

Geographic Distribution of FDI

The interpretation of FDI statistics is further complicated by a problem involving the geographic destination of investments. The OECD recommends that FDI flows should only be calculated on the basis of the immediate recipient country, due to the difficulties involved in obtaining information on FDI flows to the ultimate recipient. Changes in the stock of FDI, however, give some indication of the scale of the flows to the final destination country. This guideline is necessary and practical for the purposes of the balance of payments, but it does not meet the needs of either academic research or policy-making, both of which often require information on the precise geographic distribution of FDI.

In practice, FDI statistics do not always reflect the final destination country. If a foreign investment is channelled via a holding company which is itself a subsidiary of the direct investor, then the total investment may be assigned to the country in which the subsidiary is based, rather than its final destination.

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IMF/OECD: Survey of the Implementation of International Methodological Standards for Direct Investment

In May 1997, the IMF and the OECD launched the *Survey of Implementation of International Methodological Standards for Direct Investment.* The survey is a study of data sources, collection methods, and methodological practices for FDI statistics (IMF 1997c).

The Survey sets three objectives:

- To discover the extent of adoption by the member countries of the recommendations on FDI statistics depicted in BOPM5 and the Benchmark Definition;
- To obtain standardised information on data sources, collection methods, availability, periodicity, timeliness, revision policy, and breakdowns;
- To facilitate the exchange of information between reporting countries.

Consequently, the survey form was designed with a view to providing a set of easily comparable metadata (information about data) on FDI statistics.

Preliminary results identify the most significant sources of discrepancy:

- The report identifies the failure of many countries to compile data on reinvested earnings as the most important source of the discrepancy in global direct investment data.
- Contrary to the international guidelines, many countries do not include short-term financing between affiliated enterprises in their direct investment data.
- Many countries do not consider *Special Purpose Entities* (SPEs) of multinational enterprises to be residents of their economy for balance of payments transactions. SPEs are offshore enterprises that engage primarily in international transactions and do little or no business in the host economy. Types of SPEs include *financing subsidiaries*, which are set up abroad to channel capital to their parent company and *holding companies*, which are set up mainly to hold investments in their countries.
- Mismeasurement of cross border purchases and sales of real estate investment.
- Mismeasurement of investments by affiliates in their parent companies. The preliminary 1997 survey results indicate that only a few countries record such financial transactions in strict conformance with international guidelines.
- International manuals recommend that 10 percent or more of the ordinary shares or voting power establishes a direct investment relationship - the so-called "10 percent rule."

Finally, the report urged compilers to prepare and exchange information on the geographical breakdowns of direct investment flows, following the method of geographical allocation recommended in BOPM5.

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The accurate geographic distribution of FDI flows or stock data is particularly difficult to identify in the case of FDI channelled via Special Purpose Entities (SPEs). These include holding companies, corporations in offshore centres, financial affiliates, regional headquarters, etc. These entities are usually located in offshore centres with relatively low tax rates and high levels banking and commercial confidentiality, modern communication facilities, no exchange controls, and no need to provide financial statements to regulatory or statistical authorities. SPEs are usually located in offshore centres such as the Bahamas or Panama (see the technical notes for a complete list of offshore centres in Latin America and the Caribbean), although some also operate from relatively high tax countries such as the Netherlands.

A significant proportion of FDI flows from a number of investor countries goes to offshore centres in Latin America and the Caribbean (this is the case, for example, of 47% of the total US FDI stock in the region in 1996). When a US investor sends funds to a holding in Panama which, in turn, transfers the money to the United Kingdom to build a plant, the movement and stock of capital are registered in US FDI statistics as going to Panama, since this is the country with which the US company makes a direct investment transaction. Equally, when a Spanish company transfers funds to the British Virgin Islands, the investment is registered as going to the Virgin Islands, even if the final destination may be Argentina. Almost all countries register flows and stock of capital investment on the basis of the first country of destination.

Another problem is that the authorities in offshore centres frequently fail to record inflows of FDI. The balance of payments statistics kept in offshore centres normally include only a very small proportion of FDI inflows. Some OECD countries also supply incomplete information. For example, FDI via intermediary holding companies in the Netherlands (Special Financial Institutions) are not included in Dutch FDI figures.

The problems surrounding the geographic distribution of FDI flows affects the comparability of data from different countries. When interpreting the data presented in this book, it should be borne in mind that the final destiny of FDI flows to offshore centres in Latin America and the Caribbean may in fact be a country outside the region.

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FDI Flows and Stock Statistics

Further problems arise when attempting to compare figures for FDI flows, on the one hand, and stocks on the other. The table on German FDI in Brazil and Mexico shows that, in the case of Brazil, German FDI stock shrank by more than 2.2 billion DM between 1994 and 1995. In contrast, the FDI flows were positive and amounted to some 1.7 billion DM over the same period. The differences between FDI flows and the change in the FDI stock are a result of the diverse ways of measuring statistics for flows and stocks. As noted above, one reason is the use of different time periods in which reinvested earnings are recorded in the statistics for FDI flows and stocks. Another factor explaining the discrepancy is that the figures for stock include capital depreciation and the effects of exchange-rate movements, while the figures for flows do not take these elements into account. The principal characteristics of the statistics on FDI flows and stock are outlined below.

Generally speaking, **FDI flows** measure the movement of capital from parent companies (the direct investor) to their affiliates abroad. The flows are usually registered for balance of payments purposes. Normally, flows data are available before those for stock data (which are based on company balance sheets). FDI flows include equity capital, inter-company debt transactions and reinvested earnings. The figures on investment flows usually provide limited information. Detailed information on the geographic or sectoral breakdown of investment is often lacking.

It should also be noted that investment flows are often highly volatile. The volume of FDI flows can vary substantially from year to year. These fluctuations may be attributed to methodological issues as well as to exceptional one-off investments which have a considerable impact on annual FDI figures. In other words, variations in figures FDI flows do not necessarily reflect changes in the attractiveness of a location.

The **FDI stock** data generally provide a better indication of the geographic and sectoral distribution of FDI. They also include historic FDI. Information on stock is normally obtained from company surveys. The information registered in surveys includes the total value of assets attributable to foreign ownership at a given time. These figures are for net capital stock, since the depreciation of the stock of capital is also registered, besides disinvestments (solely reported in data on net FDI flows). FDI stocks include the following components: the value of shares and reserves attributed to the direct investor, plus short- and long-term loans, trade credit, debt securities

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and dividends which have been declared but not yet paid to the direct investor (OECD, 1996).

The OECD recommends that FDI stock should be measured in market value but, in practice, it tends to be recorded in book values. This limits its usefulness in terms of analysis, since it reflects the prices from various years. The data on FDI stock reflect accumulated values, which are obtained from the balance sheets of the direct investors, while the book values of each investor are recorded in different years. Hence, book values cannot be interpreted as constant or current values in any given year. A problem arises when the market value has increased significantly over time (as may be the case with land and real estate, for example), whereas the registered book value of the FDI stock has not risen. However, FDI figures can be revalued in the accounts of the direct investors in order to reflect the current position. The annual change in the stock is the sum of the FDI flows and valuation adjustments. The latter reflect changes in the stock more than in capital flows (for example, increases and decreases in prices or exchange rates).

Nearly all countries with FDI outflows also provide information on the stock as it is presented in company surveys and registered in book values. Italy, however, publishes information on the FDI stock based on accumulated flows, as do almost all Latin American countries.

Conclusion

This analysis has highlighted the existence of a number of problems which limit the reliability and quality of FDI statistics. The statistical components of FDI figures can vary considerably from country to country and from year to year. This can directly affect the quality of the information, and limit the comparability of FDI figures between different countries.

The fact that important components frequently go unrecorded can result in a significant underestimation of FDI. Certain elements of equity capital often go unrecorded, including indirect ownership of FDI, non-capital contributions, and FDI financing through borrowing in the recipient country. The main consequence of this is that total FDI and reinvested earnings can be considerably underestimated. Moreover, information on reinvested earnings and inter-company debt is often underrepresented, although it is the absence of reinvested earnings which is particularly important, since when they are registered, they often account for a large proportion of the total. Given the importance of

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reinvested earnings in FDI statistics, their more comprehensive inclusion would improve the analysis of FDI, while giving a somewhat different picture and leading to different conclusions.

The extent of coverage of the FDI components which are reported and recorded is almost directly linked to the data collection systems employed. Those countries that use company surveys provide more complete information than those which register FDI transactions data via bank settlements. Generally speaking, the systems of international transaction information do not include non-cash transactions, such as reinvested earnings or FDI financed through local borrowing.

Data obtained from approvals/notifications are generally overestimated. On the one hand, they include investments that are approved but never actually made and, on the other hand, they do not include the liquidation of investments. In this book, approvals/notifications data is only used as a supplementary source.

FDI data often contain inconsistencies with respect to the geographic distribution of investment. The FDI channelled via offshore centres is registered in the offshore centres, although the final destination is often another country. Information on FDI flows/stock to/in offshore centres is generally overestimated, while figures for FDI flows to other countries are proportionately underestimated.

Another problem is that of the time differences in the registration of specific components. Some countries record reinvested earnings in the year when they are made, while others do so in the year when they are actually used. Moreover, in the case of Germany, the stock statistics include reinvested profits in the year in which they are made, while they appear in the FDI flow statistics the following year. The differences in the time of registration can have a major impact on statistical information.

The reader should also bear in mind the differences between FDI flow and/or data on FDI stocks. The figures on FDI flows are often volatile. The changes in FDI stock from one year to the next are not the sum of the stock from the previous year and the value of FDI flows during that same year. The stock statistics also include the depreciation and revaluation of capital.

As a result of all these problems, the reader should bear in mind the shortcomings of the data when analyzing and interpreting it. Unfortunately, any

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study on FDI inevitably encounters these problems, and considerable inconsistencies in the statistics are to be expected.

* * *

Data Sources and Processing of the Statistics

For this study, the statistical data in IDB/IRELA (1996) has been updated to include the period 1990-96 for almost all the countries. The central banks and statistical agencies have provided information on FDI flows and, in part, on FDI stocks. The information sources are:

Source of Information (the previous years are based on IDB/IRELA, 1996)		
Austria:	*Österreichische Nationalbank* – National Bank of Austria	(1992-96)
Belgium:	*Banque Nationale de Belgique* –National Bank of Belgium	(1990-96)
Denmark:	*Danmarks Nationalbank* – National Bank of Denmark	(1993-96)
Finland:	*Suomen Pankki* – Bank of Finland	(1990-96)
France:	*Banque de France* – Bank of France	(1990-96)
Germany:	*Deutsche Bundesbank* – German Federal Bank	(1990-96)
Italy:	*Ufficio Italiano dei Cambi* – Italian Exchange Bank	(1990-96)
Japan:	Bank of Japan (Totals have been taken from OECD-DCD)	(1995-96)
Netherlands	*De Nederlandsche Bank* – Bank of the Netherlands	(1990-96)
Portugal:	*Banco de Portugal* - Bank of Portugal	(1992-96)
Spain:	*Banco de España* - Bank of Spain	(1990-96)
Sweden:	*Sveriges Riksbank* – Bank of Sweden	(1990-96)
Switzerland:	*Schweizerische Nationalbank* – National Bank of Switzerland	(1992-96)
U. Kingdom:	Office for National Statistics	(1990-96)
United States:	Department of Commerce/Bureau of Economic Analysis	(1992-96)

These bodies provided FDI data on net capital outflows registered for balance of payments purposes. It should be noted that this information is different from the data on capital inflows registered by recipient countries and published in the IMF balance of payments statistics. The figures for FDI outflows, as registered in the countries of origin of FDI, and the figures for FDI inflows registered by recipient countries are not directly comparable.

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The data were processed in a number of steps: a) the flow data were harmonized by using a homogenous geographic breakdown; b) estimation of the missing figures, particularly in the case of Japan and Spain; c) conversion of the values in local currency to US$ using the average IMF exchange rate for the period; and d) grouping of the countries and calculation of the corresponding values.

A range of FDI stock statistics was also prepared to complete the data on FDI flows. The stock figures are based on the information provided by respective central banks and statistical agencies. The stock figures were converted into US$ using the IMF year-end exchange rates.

Estimates for Japanese and Spanish FDI data

Available balance of payments data for Japan and Spain include FDI flows for only limited number of recipient countries. In both cases, however, there are sources of information on FDI which provide data on notifications and approvals, giving more detailed information than the balance of payments statistics. Some FDI outflows have been estimated for the purpose of this study. The procedures followed are described below.

The data on Japan for the period 1980-94 are based on information contained in IBD/IRELA (1996). The information for 1995 and 1996 comes from the Bank of Japan's Financial Account, which includes a breakdown of the most important regions and countries (the total for Latin America, Brazil and Mexico). The total FDI flows for Latin America were compared and adjusted in line with total inflows for Central America and the Caribbean and for South America from the OECD/DCD (in accordance with the country's balance of payments figures). Estimates were made for other countries and groups using a weighted structure based on the geographic distribution of FDI outflows, reconstructed from notifications provided by the Japanese Ministry of Finance.

A similar method was used to estimate the data for Spain. For the period 1990-96, the Spanish FDI data were provided by the Bank of Spain. The Bank publishes balance of payments figures with a limited geographic breakdown. The information in this study includes figures for Argentina, Brazil, Chile, Colombia, Mexico, Venezuela, Central and South America, and totals for Latin America and the Caribbean. The estimates for other countries and groups of countries have been calculated using the data on the geographic breakdown of approvals, provided by the Ministry of Economy and Finance. Initially, the figures for notifications were adjusted on the basis that the time lag between the verification

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and realization of an investment is usually around six months. The method of calculation involved including half the annual figures in the information for the following year. Hence, the estimates are calculated on the basis of the weighted structure of notifications and applied to the difference between the total for Latin America, and the six Latin American countries mentioned above.

Data Conversion

To facilitate comparisons among countries, all data are expressed in US dollars. Data from the central banks have been converted from national currencies into US dollars, using average annual exchange rates for FDI flows and year-end rates for stock data, as given in the IMF *International Financial Statistics Yearbook.*

Net FDI values

The information in this study refers to net values of FDI abroad. In the balance of payments, FDI is treated on the basis of assets-liabilities (an asset for the economy of the direct investor and a liability for the recipient country). But this is not complete, since the direct investor and the direct investment company also share financial assets and/or liabilities. Thus, FDI is registered separately for assets and liabilities. Generally, the direct investor has more assets and the direct investment company more liabilities.

Net FDI abroad includes the assets and liabilities of the direct investor of the reporting country with the company in the recipient country (net outward FDI). The net FDI in the reporting economy includes the assets and liabilities of the companies of the direct investor in the reporting country with the direct investor of the country of origin (net inward FDI). In this sense, disinvestment (when the direct investor sells the stake in the direct investment company) is treated as a liability of the direct investor to the company of direct investment.

Rounding up of figures

Most data are expressed in millions or billions. Because of the calculation methods used, rounding differences may appear between an aggregate and the sum of its components.

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Sign Conventions

A dash (-) means there are no data available, no flows have been reported for reasons of confidentiality, or the values are zero or insignificant.

A zero (0) means the amount is less than half the minimum value registered, but more than zero.

Negative values refer to disinvestment: the liquidation of investment or repatriation of capital.

Geographic classification

Andean Community:	Bolivia, Colombia, Ecuador, Peru and Venezuela.
Central America:	Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua.
European Union:	In this study, the EU includes Austria, Belgium (with Luxembourg), Denmark, Finland, France, Germany, Italy, the Netherlands, Portugal, Spain, Sweden and the United Kingdom. Ireland and Greece do not record FDI flows by country of destination.
Europe:	The EU and Switzerland.
Group of Three:	Colombia, Mexico and Venezuela.
Latin America/Caribbean:	Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Paraguay, Peru, the Dominican Republic, Suriname, Trinidad & Tobago, Uruguay and Venezuela.
MERCOSUR:	Argentina, Brazil, Paraguay and Uruguay.
Offshore centres:	Anguilla, Netherlands Antilles, Bahamas, Barbados, Bermuda, Cayman Islands, Panama, St. Vincent &

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the Grenadines, Turks & Caicos Islands and British Virgin Islands. This classification could differ from those used by other international organizations.

Other flows: Antigua & Barbuda, Aruba, Belize, Cuba, Dominica, Grenada, Montserrat, St. Kitts-Nevis, St. Lucia, and unspecified or unallocated flows to the region.

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ANNEX II

STATISTICAL TABLES

CONTENTS

FDI flows to Latin America and the Caribbean by Investor Countries

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15. FDI flows from Europe to Latin America and the Caribbean, 1980-96

16. FDI flows from the USA to Latin America and the Caribbean, 1980-96

17. FDI flows from Japan to Latin America and the Caribbean, 1980-96

18. Total FDI flows from Europe, the USA and Japan to Latin America and the Caribbean, 1980-96

FDI flows to Latin America and the Caribbean by Recipient Countries

19. FDI flows to Argentina, 1980-96

20. FDI flows to Brazil, 1980-96

21. FDI flows to Chile, 1980-96

22. FDI flows to Colombia, 1980-96

23. FDI flows to Jamaica, 1980-96

24. FDI flows to Mexico, 1980-96

25. FDI flows to Peru, 1980-96

26. FDI flows to Venezuela, 1980-96

27. FDI flows to the Andean Group, 1980-96

28. FDI flows to Central America, 1980-96

29. FDI flows to the Group of Three, 1980-96

30. FDI flows to MERCOSUR, 1980-96

31. Total FDI flows to Latin America and the Caribbean (including offshore centres and other flows), 1980-96

32. FDI flows to Latin American and Caribbean Countries, 1980-96

33. FDI flows to Latin American and Caribbean Offshore Centres, 1980-96

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FDI stock of Selected Investor Countries in Latin America and the Caribbean

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FDI flows to Latin America and the Caribbean by Investor Countries

1. FDI flows from Austria to Latin America and the Caribbean, 1980-96
(net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	—	8	—	—	5	3	20	20	7
Argentina	—	1	—	—	1	—	3	—	5
Bolivia	—	—	—	—	—	—	—	—	—
Brazil	—	6	—	—	3	3	18	19	1
Chile	—	0	—	—	—	—	—	0	1
Colombia	—	0	—	—	1	—	—	—	—
Costa Rica	—	—	—	—	—	—	—	—	—
Dominican Republic	—	—	—	—	—	—	—	—	—
Ecuador	—	—	—	—	—	—	—	—	—
El Salvador	—	—	—	—	—	—	—	—	—
Guatemala	—	—	—	—	—	—	—	—	—
Guyana	—	—	—	—	—	—	—	—	—
Haiti	—	—	—	—	—	—	—	—	—
Honduras	—	—	—	—	—	—	—	—	—
Jamaica	—	—	—	—	—	—	—	—	—
Mexico	—	0	—	—	—	—	—	0	0
Nicaragua	—	—	—	—	—	—	—	—	—
Paraguay	—	—	—	—	—	—	—	—	—
Peru	—	—	—	—	—	—	—	—	—
Surinam	—	—	—	—	—	—	—	—	—
Trinidad y Tobago	—	—	—	—	—	—	—	—	—
Uruguay	—	—	—	—	—	—	—	—	—
Venezuela	—	0	—	—	1	—	—	—	—
Andean Group	—	0	—	—	2	—	—	—	—
Central America	—	—	—	—	—	—	—	—	—
Group of Three	—	0	—	—	2	—	—	0	0
MERCOSUR	—	7	—	—	4	3	20	19	6
Offshore Centres	—	—	—	—	—	—	—	—	—
Other flows / Countries[1]	4	35	36	10	—	—	—	—	201
Total	4	43	36	10	5	3	20	20	208

Source: IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s,* Madrid 1996; updates based on data provided by *Österreichische Nationalbank* - National Bank of Austria.

[1] Includes FDI flows to Latin America/Caribbean (Bolivia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Guyana, Haiti, Honduras, Jamaica, Nicaragua, Peru, Paraguay, Suriname, Trinidad & Tobago and Uruguay) not located by Country and also flows to Offshore Centres and Other flows/Countries.

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2. FDI flows from Belgium to Latin America and the Caribbean, 1980-96
(net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	15	110	59	36	71	-91	-61	178	579
Argentina	-2	16	-1	-14	8	-19	-34	2	171
Bolivia	0	2	—	0	0	0	-1	1	15
Brazil	11	27	37	-16	10	-16	-91	-13	280
Chile	2	10	3	-1	1	4	2	5	59
Colombia	0	1	0	-2	-2	-1	11	—	0
Costa Rica	0	0	-1	1	—	0	2	-3	1
Dominican Republic	0	1	—	—	—	8	0	0	—
Ecuador	1	1	4	5	7	-12	3	—	-1
El Salvador	—	0	0	—	0	—	0	—	0
Guatemala	—	0	-1	-1	-2	0	—	3	3
Guyana	0	0	—	1	0	—	—	—	—
Haiti	—	0	0	0	0	—	0	—	—
Honduras	0	1	1	0	0	—	—	1	5
Jamaica	0	0	0	0	—	—	0	—	—
Mexico	-2	47	21	53	40	-23	17	182	43
Nicaragua	0	0	1	0	0	0	—	0	0
Paraguay	0	1	0	0	0	0	3	1	0
Peru	1	1	2	7	0	0	1	0	0
Surinam	0	0	—	—	0	—	0	0	0
Trinidad & Tobago	—	—	—	—	—	—	—	—	—
Uruguay	0	2	-1	1	10	-31	38	1	0
Venezuela	4	-2	-5	2	-3	-1	-12	1	2
Andean Group	6	3	0	12	3	-15	2	1	17
Central America	0	1	-1	1	-2	0	2	1	10
Group of Three	1	46	15	53	36	-25	16	183	45
MERCOSUR	9	47	35	-29	29	-66	-84	-10	451
Offshore Centres	115	-15	-6	9	94	1	-59	-135	-9
Other flows / Countries	0	12	10	-6	74	-1	2	9	-2
Total	129	107	63	39	239	-91	-119	53	568

Source: Figures for 1980-1989 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid, 1996; data for 1990-1996 provided by *Banque Nationale de Belgique*.

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3. FDI flows from Denmark to Latin America and the Caribbean, 1980-96
(net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	1	20	15	2	—	25	3	43	49
Argentina	—	1	—	—	—	2	1	—	3
Bolivia	—	0	—	—	—	0	—	—	—
Brazil	0	6	1	2	—	-2	8	9	21
Chile	—	—	—	—	—	—	—	—	—
Colombia	—	0	—	—	—	0	-2	—	1
Costa Rica	—	—	—	—	—	—	—	—	—
Dominican Republic	—	—	—	—	—	—	—	—	—
Ecuador	—	—	—	—	—	—	—	—	—
El Salvador	—	—	—	—	—	—	—	—	—
Guatemala	—	—	—	—	—	—	—	—	—
Guyana	—	—	—	—	—	—	—	—	—
Haiti	—	—	—	—	—	—	—	—	—
Honduras	—	—	—	—	—	—	—	—	—
Jamaica	—	—	—	—	—	—	—	—	—
Mexico	1	9	14	—	—	3	-4	34	19
Nicaragua	—	1	—	—	—	4	—	—	—
Paraguay	—	0	—	—	—	1	—	—	—
Peru	—	—	—	—	—	—	—	—	—
Surinam	—	—	—	—	—	—	—	—	—
Trinidad & Tobago	—	—	—	—	—	—	—	—	—
Uruguay	—	—	—	—	—	—	—	—	—
Venezuela	—	3	—	—	—	17	—	—	6
Andean Group	—	3	—	—	—	17	-2	—	7
Central America	—	1	—	—	—	4	—	—	—
Group of Three	1	12	14	—	—	20	-6	34	25
MERCOSUR	0	7	1	2	—	1	9	9	24
Offshore Centres	—	2	9	0	—	4	—	—	—
Other flows / Countries	17	22	—	—	47	-1	11	25	73
Total	18	44	23	2	47	28	15	68	123

Source: Data for 1980-1992 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid, 1996; data for 1993-1996 provided by *Danmarks Nationalbank* - National Bank of Denmark.

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4. FDI flows from Finland to Latin America and the Caribbean, 1980-96
(net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	3	30	27	37	34	15	17	52	25
Argentina	—	—	—	—	—	—	—	—	—
Bolivia	—	—	—	—	—	—	—	—	—
Brazil	3	10	15	27	15	9	-3	9	—
Chile	—	19	9	11	18	6	20	43	24
Colombia	—	—	—	—	—	—	—	—	—
Costa Rica	—	—	—	—	—	—	—	—	—
Dominican Republic	—	—	—	—	—	—	—	—	—
Ecuador	0	—	—	—	—	—	—	—	—
El Salvador	—	—	—	—	—	—	—	—	—
Guatemala	—	—	—	—	—	—	—	—	—
Guyana	—	—	—	—	—	—	—	—	—
Haiti	—	—	—	—	—	—	—	—	—
Honduras	—	—	—	—	—	—	—	—	—
Jamaica	—	—	—	—	—	—	—	—	—
Mexico	0	1	3	0	—	—	0	—	2
Nicaragua	—	—	—	—	—	—	—	—	—
Paraguay	—	—	—	—	—	—	—	—	—
Peru	0	—	—	—	—	—	—	—	—
Surinam	—	—	—	—	—	—	—	—	—
Trinidad & Tobago	—	—	—	—	—	—	—	—	—
Uruguay	—	—	—	—	—	—	—	—	—
Venezuela	—	—	—	—	—	—	—	—	—
Andean Group	0	—	—	—	—	—	—	—	—
Central America	—	—	—	—	—	—	—	—	—
Group of Three	0	1	3	0	—	—	0	—	2
MERCOSUR	3	10	15	27	15	9	-3	9	—
Offshore Centres	11	67	80	29	109	-13	19	62	187
Other flows / Countries	—	2	82	2	-75	6	1	1	0
Total	14	99	189	68	67	8	38	114	211

Source: Data for 1980-1989 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid 1996; data for 1990-1996 provided by *Suomen Pankki* - Bank of Finland.

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5. FDI flows from France to Latin America and the Caribbean, 1980-96
(net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	169	421	283	-12	146	332	101	59	2,037
Argentina	46	137	50	19	31	92	310	35	424
Bolivia	0	2	0	—	1	1	1	10	0
Brazil	37	133	82	-81	41	43	37	-223	1,028
Chile	7	6	19	6	-2	8	-3	-31	44
Colombia	9	12	11	-14	38	110	-195	64	68
Costa Rica	0	0	—	—	1	2	0	-1	1
Dominican Republic	0	1	—	0	—	3	1	—	—
Ecuador	3	8	7	7	5	7	9	10	15
El Salvador	0	0	—	—	—	—	—	0	—
Guatemala	36	0	—	—	—	—	0	—	—
Guyana	—	3	8	12	—	—	—	—	—
Haiti	0	-1	0	—	—	—	-1	-5	—
Honduras	—	0	3	—	—	—	—	—	—
Jamaica	—	1	3	—	—	1	—	—	—
Mexico	13	81	56	11	22	33	34	180	232
Nicaragua	0	—	—	—	—	—	—	—	—
Paraguay	1	1	1	1	—	1	2	4	-2
Peru	0	1	—	0	1	13	-27	9	9
Surinam	1	0	1	—	—	—	—	—	—
Trinidad & Tobago	—	3	4	5	4	4	2	—	1
Uruguay	4	12	30	19	3	12	1	4	13
Venezuela	13	21	8	3	1	3	-71	2	205
Andean Group	24	44	26	-4	45	134	-284	94	297
Central America	36	1	3	—	1	2	1	-1	1
Group of Three	34	114	75	-1	61	146	-232	246	504
MERCOSUR	89	282	163	-42	75	148	351	-180	1,463
Offshore Centres	46	—	—	—	—	—	—	—	—
Other flows / Countries	1	246	62	46	109	717	316	214	261
Total	216	667	344	34	255	1,049	417	273	2,298

Source: Data for 1980-1989 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid 1996; data for 1990-1996 provided by *Banque de France* - Bank of France.

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6. FDI flows from Germany to Latin America and the Caribbean, 1980-96
(net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	281	540	322	549	256	36	873	1,898	-156
Argentina	60	51	-9	209	-83	50	142	313	-266
Bolivia	0	1	—	—	3	1	1	1	1
Brazil	143	308	108	193	182	-123	452	1,186	157
Chile	3	27	8	5	33	10	99	184	-152
Colombia	1	29	19	23	-3	52	25	92	-2
Costa Rica	0	6	2	6	17	4	6	3	6
Dominican Republic	0	3	2	2	1	4	-2	4	8
Ecuador	0	11	1	4	5	1	1	56	8
El Salvador	-1	4	—	—	—	1	—	24	—
Guatemala	-1	1	—	-1	5	—	—	1	—
Guyana	0	—	—	—	—	—	—	—	—
Haiti	0	0	-1	—	—	—	—	—	—
Honduras	0	0	—	-1	—	—	—	—	1
Jamaica	0	0	—	3	-4	-10	11	1	-1
Mexico	60	64	172	86	106	1	79	-17	21
Nicaragua	-1	—	—	—	—	—	—	—	—
Paraguay	1	2	2	1	4	1	1	1	2
Peru	3	0	8	-5	-38	26	-1	-1	13
Surinam	0	—	—	—	—	—	—	—	—
Trinidad & Tobago	0	12	1	14	3	1	54	37	-26
Uruguay	1	5	12	1	4	2	2	4	8
Venezuela	10	17	-4	10	20	16	3	9	65
Andean Group	14	58	24	31	-13	96	29	157	85
Central America	-2	11	2	5	22	5	6	29	7
Group of Three	71	111	188	118	123	70	108	84	84
MERCOSUR	205	365	114	403	107	-70	596	1,504	-99
Offshore Centres	68	324	51	54	24	460	243	248	1,189
Other flows / Countries[1]	0	47	12	278	15	2	2	2	20
Total	349	911	385	882	295	498	1,118	2,148	1,053

Source: Data for 1980-1989 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid 1996; data for 1990-1996 provided by por *Deutsche Bundesbank* - Federal Bank of Germany.

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7. FDI flows from Italy to Latin America and the Caribbean, 1980-96
(net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	97	59	56	123	-48	-13	-2	111	183
Argentina	9	43	14	65	5	9	22	63	123
Bolivia	0	0	—	0	—	0	—	0	0
Brazil	79	2	30	35	12	-71	-62	45	25
Chile	1	4	0	17	2	2	1	2	4
Colombia	0	1	1	-1	1	1	1	0	2
Costa Rica	1	1	0	-1	-1	1	3	2	2
Dominican Republic	0	1	1	0	0	1	1	2	3
Ecuador	0	0	1	0	0	0	—	0	0
El Salvador	—	0	0	1	—	—	0	0	0
Guatemala	0	0	—	—	—	—	0	—	0
Guyana	—	0	—	0	—	—	—	0	—
Haiti	—	0	—	—	—	—	—	0	0
Honduras	0	0	—	—	—	-1	0	—	—
Jamaica	0	1	1	0	—	4	—	0	0
Mexico	3	-9	1	-1	-79	8	7	-12	12
Nicaragua	—	0	0	—	1	—	0	0	0
Paraguay	0	-1	1	-8	—	—	0	0	0
Peru	1	1	—	—	-1	3	2	2	0
Surinam	—	0	—	—	—	3	0	0	—
Trinidad & Tobago	-2	0	—	—	-2	—	—	—	0
Uruguay	0	2	1	0	0	0	2	5	5
Venezuela	4	13	7	14	14	26	20	2	6
Andean Group	6	15	8	14	14	31	23	5	9
Central America	1	1	1	1	0	0	4	3	2
Group of Three	8	4	8	13	-64	35	28	-9	20
MERCOSUR	88	46	45	92	17	-62	-38	112	152
Offshore Centres	103	120	-24	174	1	677	8	-26	28
Other flows / Countries	0	16	16	37	-1	58	1	1	2
Total	201	195	47	334	-48	722	7	87	213

Source: Data for 1980-1989 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid 1996; data for 1990-1996 provided by *Ufficio Italiano dei Cambi.*

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8. FDI flows from the Netherlands to Latin America and the Caribbean, 1980-96
(net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	70	565	258	194	653	481	1,056	891	425
Argentina	15	145	116	14	244	39	260	328	14
Bolivia	0	—	—	—	—	—	—	—	—
Brazil	45	198	-73	143	193	403	524	-136	334
Chile	1	29	20	-15	22	—	56	118	—
Colombia	2	54	31	15	42	35	134	121	—
Costa Rica	0	—	—	—	—	—	—	—	—
Dominican Republic	0	—	—	—	—	—	—	—	—
Ecuador	0	—	—	—	—	—	—	—	—
El Salvador	0	—	—	—	—	—	—	—	—
Guatemala	0	—	—	—	—	—	—	—	—
Guyana	0	—	—	—	—	—	—	—	—
Haiti	0	—	—	—	—	—	—	—	—
Honduras	0	—	—	—	—	—	—	—	—
Jamaica	—	—	—	—	—	—	—	—	—
Mexico	2	77	139	29	102	2	-3	230	41
Nicaragua	0	—	—	—	—	—	—	—	—
Paraguay	—	—	—	—	—	—	—	—	—
Peru	2	—	—	—	—	—	—	—	—
Surinam	-1	—	—	—	—	—	—	—	—
Trinidad & Tobago	0	—	—	—	—	—	—	—	—
Uruguay	1	—	—	—	—	—	—	—	—
Venezuela	1	62	26	6	51	3	86	229	36
Andean Group	6	116	57	21	92	37	220	351	36
Central America	0	—	—	—	—	—	—	—	—
Group of Three	5	193	196	51	195	39	217	581	77
MERCOSUR	61	343	43	158	437	442	784	192	348
Offshore Centres	48	—	—	—	—	—	—	—	—
Other flows / Countries	35	103	12	15	25	86	91	216	279
Total	153	669	270	209	678	566	1,147	1,107	704

Source: Data for 1980-1989 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid 1996; data for 1990-1996 provided by *De Nederlandsche Bank* - Bank of the Netherlands.

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9. FDI flows from Portugal to Latin America and the Caribbean, 1980-96
(net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	—	51	7	1	2	-1	3	34	308
Argentina	—	0	—	—	—	—	—	2	0
Bolivia	—	—	—	—	—	—	—	—	—
Brazil	—	50	7	1	2	-1	3	31	308
Chile	—	0	—	—	0	—	—	—	—
Colombia	—	0	—	—	—	—	—	—	0
Costa Rica	—	—	—	—	—	—	—	—	—
Dominican Republic	—	—	—	—	—	—	—	—	—
Ecuador	—	—	—	—	—	—	—	—	—
El Salvador	—	—	—	—	—	—	—	—	—
Guatemala	—	—	—	—	—	—	—	—	—
Guyana	—	—	—	—	—	—	—	—	—
Haiti	—	—	—	—	—	—	—	—	—
Honduras	—	—	—	—	—	—	—	—	—
Jamaica	—	—	—	—	—	—	—	—	—
Mexico	—	0	—	—	—	0	—	0	0
Nicaragua	—	—	—	—	—	—	—	—	—
Paraguay	—	—	—	—	—	—	—	—	—
Peru	—	—	—	—	—	—	—	—	—
Surinam	—	—	—	—	—	—	—	—	—
Trinidad & Tobago	—	—	—	—	—	—	—	—	—
Uruguay	—	—	—	—	—	—	—	—	—
Venezuela	—	0	—	—	—	—	—	—	0
Andean Group	—	0	—	—	—	—	—	—	0
Central America	—	—	—	—	—	—	—	—	—
Group of Three	—	0	—	—	—	0	—	0	0
MERCOSUR	—	51	7	1	2	-1	3	34	308
Offshore Centres	—	—	—	—	—	—	—	—	—
Other flows / Countries	—	17	—	—	57	-29	26	10	58
Total	—	68	7	1	59	-30	29	43	366

Source: Data for 1980-1989 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid 1996; data for 1990-1996 provided by Bank of Portugal.

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10. FDI flows from Spain to Latin America and the Caribbean, 1980-96
(net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	128	765	155	236	185	93	2,072	1,037	1,577
Argentina	21	206	87	18	79	27	65	555	610
Bolivia	—	0	0	0	—	—	—	—	2
Brazil	11	32	15	51	17	1	28	73	37
Chile	37	34	9	37	32	4	96	-24	82
Colombia	2	68	3	10	8	28	24	30	376
Costa Rica	0	1	0	0	—	—	—	—	6
Dominican Republic	4	1	0	3	1	—	—	0	3
Ecuador	2	7	0	0	0	0	36	3	9
El Salvador	—	0	0	0	—	—	—	—	—
Guatemala	6	0	0	0	—	—	—	—	—
Guyana	—	—	—	—	—	—	—	—	—
Haiti	—	—	—	—	—	—	—	—	—
Honduras	—	0	0	—	—	—	0	0	0
Jamaica	—	—	—	—	—	—	—	—	—
Mexico	21	86	37	15	21	46	184	207	94
Nicaragua	—	0	0	—	—	—	—	—	—
Paraguay	5	1	0	1	6	1	—	—	—
Peru	3	294	0	0	—	—	1,616	170	275
Surinam	—	—	—	—	—	—	—	—	—
Trinidad & Tobago	—	1	—	—	—	—	0	-2	6
Uruguay	7	10	0	2	12	3	15	5	35
Venezuela	9	23	4	97	7	-16	8	19	42
Andean Group	16	393	7	107	16	12	1,684	223	704
Central America	6	1	0	1	—	—	0	0	6
Group of Three	33	178	44	121	37	58	216	256	511
MERCOSUR	44	249	102	73	115	31	107	633	682
Offshore Centres	51	191	210	307	123	59	213	-154	581
Other flows / Countries	1	2	6	5	1	1	1	0	3
Total	181	959	371	548	308	153	2,285	883	2,162

Source: Data for 1980-1989 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid 1996; data for 1990-1996 provided by Banco de España - Bank of Spain.

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11. FDI flows from Sweden to Latin America and the Caribbean, 1980-96 (net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	-2	37	38	-6	20	37	16	14	144
Argentina	1	5	—	-3	36	2	—	—	—
Bolivia	—	—	—	—	—	—	—	—	—
Brazil	0	21	5	7	-12	10	14	-18	140
Chile	1	2	23	-3	1	—	-10	-1	1
Colombia	0	—	—	—	—	—	—	—	—
Costa Rica	0	—	—	—	—	—	—	—	—
Dominican Republic	0	—	—	—	—	—	—	—	—
Ecuador	0	—	—	—	—	—	—	—	—
El Salvador	—	—	—	—	—	—	—	—	—
Guatemala	—	—	—	—	—	—	—	—	—
Guyana	—	—	—	—	—	—	—	—	—
Haiti	—	—	—	—	—	—	—	—	—
Honduras	—	—	—	—	—	—	—	—	—
Jamaica	—	—	—	—	—	—	—	—	—
Mexico	-5	8	—	-9	-6	25	12	32	3
Nicaragua	—	—	—	—	—	—	—	—	—
Paraguay	—	—	—	—	—	—	—	—	—
Peru	0	0	—	1	—	—	—	—	—
Surinam	0	—	—	—	—	—	—	—	—
Trinidad & Tobago	—	—	—	—	—	—	—	—	—
Uruguay	—	—	—	—	—	—	—	—	—
Venezuela	1	1	10	—	—	—	—	—	—
Andean Group	1	2	10	1	—	—	—	—	—
Central America	0	—	—	—	—	—	—	—	—
Group of Three	-4	10	10	-9	-6	25	12	32	3
MERCOSUR	1	26	5	4	24	12	14	-18	140
Offshore Centres	6	-1	—	—	-9	—	3	—	—
Other flows / Countries	46	—	—	—	—	—	—	—	—
Total	50	37	38	-6	11	37	19	14	144

Source: Data for 1980-1989 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid 1996; data for 1990-1996 provided by *Sveriges Riksbank* - Bank of Sweden.

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12. FDI flows from the United Kingdom to Latin America and the Caribbean, 1980-96 (net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	458	901	493	69	542	222	1,365	1,645	1,968
Argentina	40	82	18	25	97	156	100	46	136
Bolivia	—	4	—	—	—	—	3	—	28
Brazil	289	439	377	158	214	57	446	747	1,076
Chile	41	127	34	142	-39	152	116	347	139
Colombia	8	-20	36	-467	—	-368	312	194	156
Costa Rica	4	2	—	—	—	—	—	3	8
Dominican Republic	—	5	—	—	—	—	—	36	-3
Ecuador	7	-8	-52	-7	—	—	—	3	—
El Salvador	—	—	—	—	—	—	—	—	—
Guatemala	—	0	—	—	—	—	—	-2	3
Guyana	2	2	—	—	—	2	5	—	6
Haiti	—	—	—	—	—	—	—	—	—
Honduras	—	—	—	—	—	—	—	—	—
Jamaica	6	63	4	—	23	51	222	82	59
Mexico	34	108	48	69	201	66	64	125	181
Nicaragua	—	0	—	—	—	—	—	2	2
Paraguay	0	3	—	—	—	—	6	13	—
Peru	2	4	9	—	-7	48	-21	—	—
Surinam	0	—	—	—	—	—	—	—	—
Trinidad & Tobago	1	9	-2	-5	11	6	41	6	8
Uruguay	1	6	4	2	—	-11	14	17	16
Venezuela	24	73	18	154	42	63	57	25	153
Andean Group	41	54	11	-320	35	-257	351	223	337
Central America	4	2	—	—	—	—	—	3	13
Group of Three	66	161	102	-244	244	-239	433	344	490
MERCOSUR	329	530	398	184	311	203	565	822	1,228
Offshore Centres	710	758	1.497	-409	1,414	777	1,205	393	425
Other flows / Countries	93	206	223	476	572	33	372	-239	6
Total	1,261	1,864	2,213	136	2,528	1,032	2,942	1,799	2,399

Source: Data for 1980-1989 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid 1996; data for 1990-1996 provided by the Office for National Statistics.

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13. FDI flows from the European Union to Latin America and the Caribbean, 1980-96 (net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	1,221	3,504	1,711	1,228	1,865	1,139	5,462	5,981	7,145
Argentina	189	688	274	333	419	358	868	1,344	1,219
Bolivia	0	10	0	0	4	2	3	11	47
Brazil	619	1,231	603	519	676	313	1,372	1,729	3,406
Chile	93	257	125	199	69	185	379	643	201
Colombia	23	145	100	-436	85	-145	311	502	601
Costa Rica	5	10	1	7	17	7	11	5	24
Dominican Republic	5	12	3	6	3	16	1	43	10
Ecuador	13	19	-40	8	18	-3	49	72	32
El Salvador	0	4	0	2	0	1	0	25	0
Guatemala	40	1	-1	-1	3	0	1	2	7
Guyana	2	5	8	13	0	2	5	0	6
Haiti	0	-1	0	0	0	—	-1	-4	0
Honduras	0	1	4	0	0	-1	0	1	6
Jamaica	7	64	8	3	19	46	233	83	59
Mexico	128	473	490	252	407	161	390	961	647
Nicaragua	0	1	1	0	1	4	0	2	2
Paraguay	7	6	4	-5	10	3	13	18	1
Peru	12	302	19	4	-46	90	1,569	180	297
Surinam	1	1	1	—	0	3	0	0	0
Trinidad & Tobago	0	25	3	14	16	11	97	41	-10
Uruguay	14	37	46	25	29	-24	72	36	76
Venezuela	65	213	63	286	134	111	91	288	514
Andean Group	113	689	142	-139	195	56	2,023	1,053	1,491
Central America	45	18	5	7	21	10	12	34	38
Group of Three	215	831	653	102	626	128	792	1,750	1,762
MERCOSUR	829	1,962	927	872	1,135	650	2,324	3,127	4,702
Offshore Centres	1,157	1,446	1,817	164	1,755	1,965	1,632	389	2,400
Other flows / Countries	197	712	459	863	824	873	823	239	902
Total	2,575	5,662	3,987	2,256	4,445	3,977	7,917	6,609	10,447

Source: IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid, 1996; updated based on data provided by European Central Banks and statistic information agencies (see tables 1 to 12).

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14. FDI flows from Switzerland[2] to Latin America and the Caribbean, 1980-96
(net flows, millions of US$)

	annual average								
	1980-89	1990-96[2]	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	—	340	—	—	—	487	176	304	391
Argentina	—	*35*	—	—	—	31	34	24	49
Bolivia	—	—	—	—	—	—	—	—	—
Brazil	—	*60*	—	—	—	208	-39	107	-36
Chile	—	*47*	—	—	—	72	20	30	67
Colombia	—	*36*	—	—	—	13	66	6	58
Costa Rica	—	*8*	—	—	—	-2	-12	38	8
Dominican Republic	—	—	—	—	—	—	—	—	—
Ecuador	—	*22*	—	—	—	10	3	9	64
El Salvador	—	—	—	—	—	—	—	—	—
Guatemala	—	*-33*	—	—	—	13	-4	3	-142
Guyana	—	—	—	—	—	—	—	—	—
Haiti	—	—	—	—	—	—	—	—	—
Honduras	—	—	—	—	—	—	—	—	—
Jamaica	—	—	—	—	—	—	—	—	—
Mexico	—	*60*	—	—	—	83	61	-3	97
Nicaragua	—	—	—	—	—	—	—	—	—
Paraguay	—	—	—	—	—	—	—	—	—
Peru	—	*4*	—	—	—	1	7	16	-10
Surinam	—	—	—	—	—	—	—	—	—
Trinidad & Tobago	—	—	—	—	—	—	—	—	—
Uruguay	—	*71*	—	—	—	27	41	78	139
Venezuela	—	*31*	—	—	—	31	-1	-4	97
Andean Group	—	*92*	—	—	—	55	75	27	209
Central America	—	*-25*	—	—	—	11	-16	41	-134
Group of Three	—	*126*	—	—	—	127	126	-1	252
MERCOSUR	—	*166*	—	—	—	266	36	209	152
Offshore Centres	—	*123*	—	—	—	12	323	70	86
Other flows / Countries	360	506	2,523	1,062	539	1,175	-930	-216	-609
Total	360	770	2,523	1,062	539	1,674	-431	159	-133

Source: Data for 1980-1989 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid 1996; data for 1990-1996 provided by *Schweizerische Nationalbank* - Swiss National Bank.

[2] Figures in italics refer to four-year averages, since geographically distributed data is available only for the 1993-1996 period. Thus, individual figures and subtotals in that column do not add up to the Total and are not comparable with Switzerland figures in the next tables, which are based on seven-year averages.

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15. FDI flows from Europe to Latin America and the Caribbean, 1980-96
(net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	1,221	3,698	1,711	1,228	1,865	1,626	5,638	6,285	7,536
Argentina	189	708	274	333	419	389	902	1,368	1,268
Bolivia	0	10	0	0	4	2	3	11	47
Brazil	619	1,266	603	519	676	521	1,333	1,836	3,370
Chile	93	284	125	199	69	257	399	673	268
Colombia	23	166	100	-436	85	-132	377	508	659
Costa Rica	5	15	1	7	17	5	-1	43	32
Dominican Republic	5	12	3	6	3	16	1	43	10
Ecuador	13	32	-40	8	18	7	52	81	96
El Salvador	0	4	0	2	0	1	0	25	0
Guatemala	40	-17	-1	-1	3	13	-4	5	-135
Guyana	2	5	8	13	0	2	5	0	6
Haiti	0	-1	0	0	0	—	-1	-4	0
Honduras	0	1	4	0	0	-1	0	1	6
Jamaica	7	64	8	3	19	46	233	83	59
Mexico	128	507	490	252	407	244	451	958	744
Nicaragua	0	1	1	0	1	4	0	2	2
Paraguay	7	6	4	-5	10	3	13	18	1
Peru	12	304	19	4	-46	91	1,576	196	287
Surinam	1	1	1	—	0	3	0	0	0
Trinidad & Tobago	0	25	3	14	16	11	97	41	-10
Uruguay	14	78	46	25	29	3	113	114	215
Venezuela	65	230	63	286	134	142	90	284	611
Andean Group	113	741	142	-139	195	111	2,098	1,080	1,700
Central America	45	4	5	7	21	21	-4	75	-96
Group of Three	215	903	653	102	626	255	918	1,749	2,014
MERCOSUR	829	2,057	927	872	1,135	916	2,360	3,336	4,854
Offshore Centres	1,157	1,516	1,817	164	1,755	1,976	1,955	459	2,486
Other flows / Countries	558	1,218	2,982	1,925	1,363	2,047	-107	24	292
Total	2,935	6,433	6,510	3,318	4,984	5,650	7,487	6,768	10,314

Source: IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s,* Madrid 1996; updates based on data provided by European Central Banks and statistic information agencies (see tables 12 and 14).

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16. FDI flows from the USA to Latin America and the Caribbean, 1980-96 (net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	1,102	8,152	3,217	4,970	5,444	8,525	11,831	13,548	9,529
Argentina	123	836	164	415	558	1,079	931	2,291	415
Bolivia	—	14	—	—	-4	66	76	118	-157
Brazil	663	2,674	1,054	869	2,054	3,263	3,517	4,899	3,064
Chile	106	682	293	226	106	198	1,554	1,406	994
Colombia	-116	181	115	39	406	4	368	195	138
Costa Rica	—	107	—	—	-147	38	263	261	337
Dominican Republic	—	65	—	—	131	217	-19	55	71
Ecuador	23	78	-19	-46	12	253	182	136	25
El Salvador	—	12	—	—	1	22	32	-29	58
Guatemala	—	21	—	—	5	31	21	22	67
Guyana	—	—	—	—	—	—	—	—	—
Haiti	—	3	—	—	10	3	3	1	7
Honduras	—	-6	—	—	-16	-51	40	13	-31
Jamaica	-9	154	57	66	137	173	220	150	275
Mexico	357	2,478	1,949	2,183	1,320	2,516	3,674	2,955	2,747
Nicaragua	—	—	—	—	—	—	—	—	—
Paraguay	—	6	—	—	2	15	3	4	21
Peru	26	138	-346	-26	-3	-8	231	317	800
Surinam	—	17	—	—	44	17	-13	21	47
Trinidad & Tobago	-44	69	-89	-4	55	122	71	120	211
Uruguay	—	34	—	—	81	12	33	59	50
Venezuela	-27	589	39	1,248	692	555	644	554	390
Andean Group	-94	999	-211	1,215	1,103	870	1,501	1,320	1,196
Central America	—	134	—	—	-157	40	356	267	431
Group of Three	213	3,247	2,103	3,470	2,418	3,075	4,686	3,704	3,275
MERCOSUR	786	3,550	1,218	1,284	2,695	4,369	4,484	7,253	3,550
Offshore Centres	1,329	4,648	1,463	2,176	7,657	7,763	7,431	1,278	4,765
Other flows / Countries	373	9	117	11	-350	607	-252	-73	5
Total	2,803	12,809	4,797	7,157	12,751	16,895	19,010	14,753	14,299

Source: Data for 1980-1991 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid, 1996; data for 1992-1996 provided by the US Department of Commerce/Bureau of Economic Analysis.

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17. FDI flows from Japan to Latin America and the Caribbean, 1980-96
(net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	292	457	399	561	270	132	568	492	780
Argentina	10	27	31	90	8	8	-27	40	38
Bolivia	0	—	—	—	—	—	—	—	—
Brazil	203	222	127	276	89	110	60	256	634
Chile	8	12	-28	56	—	0	5	50	—
Colombia	3	11	59	0	—	—	8	8	—
Costa Rica	0	0	-1	2	—	—	—	—	—
Dominican Republic	0	—	—	—	—	—	—	—	—
Ecuador	0	1	3	1	—	—	—	—	—
El Salvador	0	—	—	—	—	—	—	—	—
Guatemala	0	—	—	—	—	—	—	—	—
Guyana	0	—	—	—	—	—	—	—	—
Haiti	0	—	—	—	—	—	—	—	—
Honduras	-2	1	6	1	—	—	—	—	—
Jamaica	0	1	4	—	—	—	—	—	—
Mexico	84	136	159	92	101	12	518	129	-61
Nicaragua	—	—	—	—	—	—	—	—	—
Paraguay	1	0	1	—	—	—	—	—	—
Peru	-21	-3	-30	—	5	0	1	—	—
Surinam	1	—	—	—	—	—	—	—	—
Trinidad & Tobago	0	—	—	—	—	—	—	—	—
Uruguay	0	0	-1	—	—	—	—	—	—
Venezuela	5	51	69	42	67	2	3	10	168
Andean Group	-13	59	101	43	72	2	12	17	168
Central America	-1	1	5	3	—	—	—	—	—
Group of Three	92	198	287	134	168	14	529	146	107
MERCOSUR	214	249	158	366	97	118	33	296	673
Offshore Centres	1,119	169	488	385	-223	-238	1,082	370	-680
Other flows / Countries	1	5	—	—	—	0	17	21	-4
Total	1,412	631	887	946	47	-107	1,667	883	96

Source: Data for 1980-1994 from IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid 1996; data for 1995-1996 are own calculations based on information provided by the Bank of Japan.

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18. Total FDI flows from Europe, the USA and Japan to Latin America and the Caribbean, 1980-96 (net flows, millions of US$)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Latin America/Caribbean	2,614	12,308	5,327	6,759	7,579	10,283	18,037	20,325	17,844
Argentina	322	1,571	469	838	985	1,476	1,806	3,699	1,722
Bolivia	0	24	0	0	0	68	79	129	-110
Brazil	1,485	4,162	1,784	1,664	2,819	3,894	4,910	6,991	7,068
Chile	207	979	390	481	175	455	1,958	2,129	1,262
Colombia	-90	357	274	-397	491	-128	752	710	797
Costa Rica	5	123	0	10	-130	43	262	304	369
Dominican Republic	5	77	3	6	134	233	-18	98	81
Ecuador	36	110	-56	-37	30	260	234	217	121
El Salvador	0	16	0	2	1	23	32	-4	58
Guatemala	41	4	-1	-1	8	44	18	27	-68
Guyana	2	5	8	13	0	2	5	0	6
Haiti	0	3	0	0	10	3	2	-3	7
Honduras	-2	-4	10	0	-16	-52	40	14	-25
Jamaica	-2	219	69	69	156	219	453	233	334
Mexico	568	3,120	2,598	2,527	1,828	2,772	4,643	4,041	3,430
Nicaragua	0	1	1	0	1	4	0	2	2
Paraguay	8	13	5	-5	12	18	16	22	22
Peru	17	438	-357	-22	-44	83	1,808	513	1,087
Surinam	1	17	1	—	44	20	-13	21	47
Trinidad & Tobago	-44	94	-86	10	71	133	168	161	201
Uruguay	14	111	45	25	110	15	146	173	265
Venezuela	42	870	171	1,575	893	699	737	848	1,169
Andean Group	6	1,799	32	1,120	1,369	982	3,611	2,417	3,064
Central America	43	139	10	10	-136	61	352	342	335
Group of Three	521	4,348	3,043	3,706	3,212	3,344	6,133	5,599	5,397
MERCOSUR	1,829	5,856	2,303	2,522	3,927	5,403	6,877	10,885	9,076
Offshore Centres	3,605	6,333	3,768	2,725	9,189	9,501	10,468	2,108	6,571
Other flows / Countries	931	1,232	3,099	1,936	1,013	2,654	-342	-29	293
Total	7,150	19,873	12,194	11,420	17,781	22,438	28,164	22,404	24,709

Source: IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s*, Madrid 1996; updates based on data provided by European Central Banks and statistic information agencies (see tables 15, 16 and 17).

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FDI flows to Latin America and the Caribbean by Recipient Contries

19. FDI flows to Argentina, 1980-96

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	1	—	—	1	—	3	—	5
Belgium	-2	16	-1	-14	8	-19	-34	2	171
Denmark	—	1	—	—	—	2	1	—	3
Finland	—	—	—	—	—	—	—	—	—
France	46	137	50	19	31	92	310	35	424
Germany	60	51	-9	209	-83	50	142	313	-266
Italy	9	43	14	65	5	9	22	63	123
Netherlands	15	145	116	14	244	39	260	328	14
Portugal	—	0	—	—	—	—	—	2	0
Spain	21	206	87	18	79	27	65	555	610
Sweden	1	5	—	-3	36	2	—	—	—
United Kingdom	40	82	18	25	97	156	100	46	136
European Union	189	688	274	333	419	358	868	1,344	1,219
Switzerland	—	20	—	—	—	31	34	24	49
Europe	189	708	274	333	419	389	902	1,368	1,268
USA	123	836	164	415	558	1,079	931	2,291	415
Japan	10	27	31	90	8	8	-27	40	38
Europe+USA+Japan	322	1,571	469	838	985	1,476	1,806	3,699	1,722

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20. FDI flows to Brazil, 1980-96

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	6	—	—	3	3	18	19	1
Belgium	11	27	37	-16	10	-16	-91	-13	280
Denmark	0	6	1	2	—	-2	8	9	21
Finland	3	10	15	27	15	9	-3	9	—
France	37	133	82	-81	41	43	37	-223	1,028
Germany	143	308	108	193	182	-123	452	1,186	157
Italy	79	2	30	35	12	-71	-62	45	25
Netherlands	45	198	-73	143	193	403	524	-136	334
Portugal	—	50	7	1	2	-1	3	31	308
Spain	11	32	15	51	17	1	28	73	37
Sweden	0	21	5	7	-12	10	14	-18	140
United Kingdom	289	439	377	158	214	57	446	747	1,076
European Union	619	1,231	603	519	676	313	1,372	1,729	3,406
Switzerland	—	34	—	—	—	208	-39	107	-36
Europe	619	1,266	603	519	676	521	1,333	1,836	3,370
USA	663	2,674	1,054	869	2,054	3,263	3,517	4,899	3,064
Japan	203	222	127	276	89	110	60	256	634
Europe+USA+Japan	1,485	4,162	1,784	1,664	2,819	3,894	4,910	6,991	7,068

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21. FDI flows to Chile, 1980-96

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	0	—	—	—	—	—	0	1
Belgium	2	10	3	-1	1	4	2	5	59
Denmark	—	—	—	—	—	—	—	—	—
Finland	—	19	9	11	18	6	20	43	24
France	7	6	19	6	-2	8	-3	-31	44
Germany	3	27	8	5	33	10	99	184	-152
Italy	1	4	0	17	2	2	1	2	4
Netherlands	1	29	20	-15	22	—	56	118	—
Portugal	—	0	—	—	0	—	—	—	—
Spain	37	34	9	37	32	4	96	-24	82
Sweden	1	2	23	-3	1	—	-10	-1	1
United Kingdom	41	127	34	142	-39	152	116	347	139
European Union	93	257	125	199	69	185	379	643	201
Switzerland	—	27	—	—	—	72	20	30	67
Europe	93	284	125	199	69	257	399	673	268
USA	106	682	293	226	106	198	1,554	1,406	994
Japan	8	12	-28	56	—	0	5	50	—
Europe+USA+Japan	207	979	390	481	175	455	1,958	2,129	1,262

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22. FDI flows to Colombia, 1980-96

	annual average									
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	0	—	—	1	—	—	—	—
Belgium	0	1	0	-2	-2	-1	11	—	0
Denmark	—	0	—	—	—	0	-2	—	1
Finland	—	—	—	—	—	—	—	—	—
France	9	12	11	-14	38	110	-195	64	68
Germany	1	29	19	23	-3	52	25	92	-2
Italy	0	1	1	-1	1	1	1	0	2
Netherlands	2	54	31	15	42	35	134	121	—
Portugal	—	0	—	—	—	—	—	—	0
Spain	2	68	3	10	8	28	24	30	376
Sweden	0	—	—	—	—	—	—	—	—
United Kingdom	8	-20	36	-467	—	-368	312	194	156
European Union	23	145	100	-436	85	-145	311	502	601
Switzerland	—	20	—	—	—	13	66	6	58
Europe	23	166	100	-436	85	-132	377	508	659
USA	-116	181	115	39	406	4	368	195	138
Japan	3	11	59	0	—	—	8	8	—
Europe+USA+Japan	-90	357	274	-397	491	-128	752	710	797

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23. FDI flows to Jamaica, 1980-96

	annual average									
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	—	—	—	—	—	—	—	—
Belgium	0	0	0	0	—	—	0	—	—
Denmark	—	—	—	—	—	—	—	—	—
Finland	—	—	—	—	—	—	—	—	—
France	—	1	3	—	—	1	—	—	—
Germany	0	0	—	3	-4	-10	11	1	-1
Italy	0	1	1	0	—	4	—	0	0
Netherlands	—	—	—	—	—	—	—	—	—
Portugal	—	—	—	—	—	—	—	—	—
Spain	—	—	—	—	—	—	—	—	—
Sweden	—	—	—	—	—	—	—	—	—
United Kingdom	6	63	4	—	23	51	222	82	59
European Union	7	64	8	3	19	46	233	83	59
Switzerland	—	—	—	—	—	—	—	—	—
Europe	7	64	8	3	19	46	233	83	59
USA	-9	154	57	66	137	173	220	150	275
Japan	0	1	4	—	—	—	—	—	—
Europe+USA+Japan	-2	219	69	69	156	219	453	233	334

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24. FDI flows to Mexico, 1980-96

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	0	—	—	—	—	—	0	0
Belgium	-2	47	21	53	40	-23	17	182	43
Denmark	1	9	14	—	—	3	-4	34	19
Finland	0	1	3	0	—	—	0	—	2
France	13	81	56	11	22	33	34	180	232
Germany	60	64	172	86	106	1	79	-17	21
Italy	3	-9	1	-1	-79	8	7	-12	12
Netherlands	2	77	139	29	102	2	-3	230	41
Portugal	—	0	—	—	—	0	—	0	0
Spain	21	86	37	15	21	46	184	207	94
Sweden	-5	8	—	-9	-6	25	12	32	3
United Kingdom	34	108	48	69	201	66	64	125	181
European Union	128	473	490	252	407	161	390	961	647
Switzerland	—	34	—	—	—	83	61	-3	97
Europe	128	507	490	252	407	244	451	958	744
USA	357	2,478	1,949	2,183	1,320	2,516	3,674	2,955	2,747
Japan	84	136	159	92	101	12	518	129	-61
Europe+USA+Japan	568	3,120	2,598	2,527	1,828	2,772	4,643	4,041	3,430

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25. FDI flows to Peru, 1980-96

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	—	—	—	—	—	—	—	—
Belgium	1	1	2	7	0	0	1	0	0
Denmark	—	—	—	—	—	—	—	—	—
Finland	0	—	—	—	—	—	—	—	—
France	0	1	—	0	1	13	-27	9	9
Germany	3	0	8	-5	-38	26	-1	-1	13
Italy	1	1	—	—	-1	3	2	2	0
Netherlands	2	—	—	—	—	—	—	—	—
Portugal	—	—	—	—	—	—	—	—	—
Spain	3	294	0	0	—	—	1,616	170	275
Sweden	0	0	—	1	—	—	—	—	—
United Kingdom	2	4	9	—	-7	48	-21	—	—
European Union	12	302	19	4	-46	90	1,569	180	297
Switzerland	—	2	—	—	—	1	7	16	-10
Europe	12	304	19	4	-46	91	1,576	196	287
USA	26	138	-346	-26	-3	-8	231	317	800
Japan	-21	-3	-30	—	5	0	1	—	—
Europe+USA+Japan	17	438	-357	-22	-44	83	1,808	513	1,087

Source: IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s,* Madrid 1996; updates based on data provided by Central Banks from investor countries.

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26. FDI flows to Venezuela, 1980-96

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	0	—	—	1	—	—	—	—
Belgium	4	-2	-5	2	-3	-1	-12	1	2
Denmark	—	3	—	—	—	17	—	—	6
Finland	—	—	—	—	—	—	—	—	—
France	13	21	8	3	1	3	-71	2	205
Germany	10	17	-4	10	20	16	3	9	65
Italy	4	13	7	14	14	26	20	2	6
Netherlands	1	62	26	6	51	3	86	229	36
Portugal	—	0	—	—	—	—	—	—	0
Spain	9	23	4	97	7	-16	8	19	42
Sweden	1	1	10	—	—	—	—	—	—
United Kingdom	24	73	18	154	42	63	57	25	153
European Union	65	213	63	286	134	111	91	288	514
Switzerland	—	18	—	—	—	31	-1	-4	97
Europe	65	230	63	286	134	142	90	284	611
USA	-27	589	39	1,248	692	555	644	554	390
Japan	5	51	69	42	67	2	3	10	168
Europe+USA+Japan	42	870	171	1,575	893	699	737	848	1,169

Source: IDB/IRELA, *Foreign Direct Investment in Latin America in the 1990s,* Madrid 1996; updates based on data provided by Central Banks from investor countries.

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27. FDI flows to the Andean Group, 1980-96

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	0	—	—	2	—	—	—	—
Belgium	6	3	0	12	3	-15	2	1	17
Denmark	—	3	—	—	—	17	-2	—	7
Finland	0	—	—	—	—	—	—	—	—
France	24	44	26	-4	45	134	-284	94	297
Germany	14	58	24	31	-13	96	29	157	85
Italy	6	15	8	14	14	31	23	5	9
Netherlands	6	116	57	21	92	37	220	351	36
Portugal	—	0	—	—	—	—	—	—	0
Spain	16	393	7	107	16	12	1,684	223	704
Sweden	1	2	10	1	—	—	—	—	—
United Kingdom	41	54	11	-320	35	-257	351	223	337
European Union	113	689	142	-139	195	56	2,023	1,053	1,491
Switzerland	—	52	—	—	—	55	75	27	209
Europe	113	741	142	-139	195	111	2,098	1,080	1,700
USA	-94	999	-211	1,215	1,103	870	1,501	1,320	1,196
Japan	-13	59	101	43	72	2	12	17	168
Europe+USA+Japan	6	1,799	32	1,120	1,369	982	3,611	2,417	3,064

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28. FDI flows to Central America, 1980-96

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	—	—	—	—	—	—	—	—
Belgium	0	1	-1	1	-2	0	2	1	10
Denmark	—	1	—	—	—	4	—	—	—
Finland	—	—	—	—	—	—	—	—	—
France	36	1	3	—	1	2	1	-1	1
Germany	-2	11	2	5	22	5	6	29	7
Italy	1	1	1	1	0	0	4	3	2
Netherlands	0	—	—	—	—	—	—	—	—
Portugal	—	—	—	—	—	—	—	—	—
Spain	6	1	0	1	—	—	0	0	6
Sweden	0	—	—	—	—	—	—	—	—
United Kingdom	4	2	—	—	—	—	—	3	13
European Union	45	18	5	7	21	10	12	34	38
Switzerland	—	-14	—	—	—	11	-16	41	-134
Europe	45	4	5	7	21	21	-4	75	-96
USA	—	134	—	—	-157	40	356	267	431
Japan	-1	1	5	3	—	—	—	—	—
Europe+USA+Japan	43	139	10	10	-136	61	352	342	335

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29. FDI flows to the Group of Three, 1980-96

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	0	—	—	2	—	—	0	0
Belgium	1	46	15	53	36	-25	16	183	45
Denmark	1	12	14	—	—	20	-6	34	25
Finland	0	1	3	0	—	—	0	—	2
France	34	114	75	-1	61	146	-232	246	504
Germany	71	111	188	118	123	70	108	84	84
Italy	8	4	8	13	-64	35	28	-9	20
Netherlands	5	193	196	51	195	39	217	581	77
Portugal	—	0	—	—	—	0	—	0	0
Spain	33	178	44	121	37	58	216	256	511
Sweden	-4	10	10	-9	-6	25	12	32	3
United Kingdom	66	161	102	-244	244	-239	433	344	490
European Union	215	831	653	102	626	128	792	1,750	1,762
Switzerland	—	72	—	—	—	127	126	-1	252
Europe	215	903	653	102	626	255	918	1,749	2,014
USA	213	3,247	2,103	3,470	2,418	3,075	4,686	3,704	3,275
Japan	92	198	287	134	168	14	529	146	107
Europe+USA+Japan	521	4,348	3,043	3,706	3,212	3,344	6,133	5,599	5,397

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30. FDI flows to the MERCOSUR, 1980-96

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	7	—	—	4	3	20	19	6
Belgium	9	47	35	-29	29	-66	-84	-10	451
Denmark	0	7	1	2	—	1	9	9	24
Finland	3	10	15	27	15	9	-3	9	—
France	89	282	163	-42	75	148	351	-180	1,463
Germany	205	365	114	403	107	-70	596	1,504	-99
Italy	88	46	45	92	17	-62	-38	112	152
Netherlands	61	343	43	158	437	442	784	192	348
Portugal	—	51	7	1	2	-1	3	34	308
Spain	44	249	102	73	115	31	107	633	682
Sweden	1	26	5	4	24	12	14	-18	140
United Kingdom	329	530	398	184	311	203	565	822	1,228
European Union	829	1,962	927	872	1,135	650	2,324	3,127	4,702
Switzerland	—	95	—	—	—	266	36	209	152
Europe	829	2,057	927	872	1,135	916	2,360	3,336	4,854
USA	786	3,550	1,218	1,284	2,695	4,369	4,484	7,253	3,550
Japan	214	249	158	366	97	118	33	296	673
Europe+USA+Japan	1,829	5,856	2,303	2,522	3,927	5,403	6,877	10,885	9,076

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31. Total FDI flows to Latin America and the Caribbean (including offshore centres and other flows)

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	4	43	36	10	5	3	20	20	208
Belgium	129	107	63	39	239	-91	-119	53	568
Denmark	18	44	23	2	47	28	15	68	123
Finland	14	99	189	68	67	8	38	114	211
France	216	667	344	34	255	1,049	417	273	2,298
Germany	349	911	385	882	295	498	1,118	2,148	1,053
Italy	201	195	47	334	-48	722	7	87	213
Netherlands	153	669	270	209	678	566	1,147	1,107	704
Portugal	—	68	7	1	59	-30	29	43	366
Spain	181	959	371	548	308	153	2,285	883	2,162
Sweden	50	37	38	-6	11	37	19	14	144
United Kingdom	1,261	1,864	2,213	136	2,528	1,032	2,942	1,799	2,399
European Union	2,575	5,662	3,987	2,256	4,445	3,977	7,917	6,609	10,447
Switzerland	360	770	2,523	1,062	539	1,674	-431	159	-133
Europe	2,935	6,433	6,510	3,318	4,984	5,650	7,487	6,768	10,314
USA	2,803	12,809	4,797	7,157	12,751	16,895	19,010	14,753	14,299
Japan	1,412	631	887	946	47	-107	1,667	883	96
Europe+USA+Japan	7,150	19,873	12,194	11,420	17,781	22,438	28,164	22,404	24,709

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32. FDI flows to Latin American and Caribbean Countries, 1980-96

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	8	—	—	5	3	20	20	7
Belgium	15	110	59	36	71	-91	-61	178	579
Denmark	1	20	15	2	—	25	3	43	49
Finland	3	30	27	37	34	15	17	52	25
France	169	421	283	-12	146	332	101	59	2,037
Germany	281	540	322	549	256	36	873	1,898	-156
Italy	97	59	56	123	-48	-13	-2	111	183
Netherlands	70	565	258	194	653	481	1,056	891	425
Portugal	—	51	7	1	2	-1	3	34	308
Spain	128	765	155	236	185	93	2,072	1,037	1,577
Sweden	-2	37	38	-6	20	37	16	14	144
United Kingdom	458	901	493	69	542	222	1,365	1,645	1,968
European Union	1,221	3,504	1,711	1,228	1,865	1,139	5,462	5,981	7,145
Switzerland	—	194	—	—	—	487	176	304	391
Europe	1,221	3,698	1,711	1,228	1,865	1,626	5,638	6,285	7,536
USA	1,102	8,152	3,217	4,970	5,444	8,525	11,831	13,548	9,529
Japan	292	457	399	561	270	132	568	492	780
Europe+USA+Japan	2,614	12,308	5,327	6,759	7,579	10,283	18,037	20,325	17,844

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33. FDI flows to Latin American and Caribbean Offshore Centres, 1980-96

	annual average								
	1980-89	1990-96	1990	1991	1992	1993	1994	1995	1996
Austria	—	—	—	—	—	—	—	—	—
Belgium	115	-15	-6	9	94	1	-59	-135	-9
Denmark	—	2	9	0	—	4	—	—	—
Finland	11	67	80	29	109	-13	19	62	187
France	46	—	—	—	—	—	—	—	—
Germany	68	324	51	54	24	460	243	248	1,189
Italy	103	120	-24	174	1	677	8	-26	28
Netherlands	48	—	—	—	—	—	—	—	—
Portugal	—	—	—	—	—	—	—	—	—
Spain	51	191	210	307	123	59	213	-154	581
Sweden	6	-1	—	—	-9	—	3	—	—
United Kingdom	710	758	1,497	-409	1,414	777	1,205	393	425
European Union	1,157	1,446	1,817	164	1,755	1,965	1,632	389	2,400
Switzerland	—	70	—	—	—	12	323	70	86
Europe	1,157	1,516	1,817	164	1,755	1,976	1,955	459	2,486
USA	1,329	4,648	1,463	2,176	7,657	7,763	7,431	1,278	4,765
Japan	1,119	169	488	385	-223	-238	1,082	370	-680
Europe+USA+Japan	3,605	6,333	3,768	2,725	9,189	9,501	10,468	2,108	6,571

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FDI stock of Selected Investor Countries in Latin America and the Caribbean

34. France: FDI stock in Latin America/Caribbean by Country, 1995

	Millions of US$	% share
Argentina	1,463	19.9
Brazil	3,813	51.9
Chile	332	4.5
Mexico	378	5.1
Uruguay	112	1.5
Other LAC countries	218	3.0
Latin America/Caribbean	6,310	85.9
Offshore Centres / Other	1,036	14.1
Overall Total	7,346	100.0

Source: Own calculations based on data provided by *Banque de France* - Bank of France.

35. France: FDI stock in Latin America/Caribbean by Sector, 1995

	Millions of US$	% share
Agriculture	322	4.4
Energy	177	2.4
Industry	3,386	46.1
Construction	64	0.9
Trade services	2549	34.7
Holdings	848	11,5
Total	7,346	100.0

Source: Own calculations based on data provided by *Banque de France* - Bank of France.

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36. Germany: FDI stock in Latin America/Caribbean by Country, 1995

	Millions of US$	% share
Argentina	1,467	8.8
Brazil	8,465	50.8
Mexico	2,053	12.3
Offshore Centres / Other	4,692	28.1
Overall Total	16,677	100.0

Source: Own calculations based on data provided by *Deutsche Bundesbank* - Federal Bank of Germany.

37. Germany: FDI stock in Latin America/Caribbean by Sector, 1995

	Millions of US$	% share
Total industry	11,113	66.6
Chemical Industry	3,310	19.8
Manufactures	1,191	7.1
Electronic, electrical equipment	1,694	10.2
Transport equipment	3,061	18.4
Other industry	1,857	11.1
Trade	556	3.3
Banking, Finance and Insurance	3,212	19.3
Others	1,795	10.8
Total	16,677	100.0

Source: Own calculations based on data provided by *Deutsche Bundesbank* - Federal Bank of Germany.

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38. Italy: FDI stock in Latin America/Caribbean by Country, 1996

	Millions of US$	% share
Argentina	1,711	24.9
Brazil	2,408	35.0
Mexico	70	1.0
Venezuela	181	2.6
Other LAC countries	235	3.4
Latin America/Caribbean	4,605	67.0
Offshore Centres / Other	2,266	33.0
Overall Total	6,871	100.0

Source: Own calculations based on data provided by *Ufficio Italiano dei Cambi.*

39. Italy: FDI stock in Latin America/Caribbean by Sector, 1996

	Millions of US$	% share
Agriculture & Fishing	7	0.2
Manufacturing	3,126	67.9
Food Products	385	8.4
Textiles, Apparel	20	0.4
Chemical Products	718	15.6
Mechanical Products	231	5.0
Metal Products	735	16.0
Motor Vehicles	109	2.4
Other Manufacturing	928	20.1
Energy	235	5.1
Trade	62	1.4
Transport, Communication	270	5.9
Financial Intermediation	724	15.7
Other Services	149	3.2
Others	30	0.7
Total	4,604	100.0

Source: Own calculations based on data provided by *Ufficio Italiano dei Cambi.*

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40. Netherlands: FDI stock in Latin America/Caribbean by Country, 1995

	Millions of US$	% share
Argentina	1,270	24.4
Brazil	2,142	41.2
Chile	274	5.3
Venezuela	485	9.3
Offshore Centres / Other	1,026	19.7
Overall Total	5,196	100.0

Source: Own calculations based on data provided by *De Nederlandsche Bank* - Bank of Netherlands.

41. Netherlands: FDI stock in Latin America/Caribbean by Sector, 1995

	Millions of US$	% share
Industry	3,040	81.0
Services	715	19.0
Total	3,755	100.0

Source: Own calculations based on data provided by *De Nederlandsche Bank* - Bank of Netherlands.

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42. Switzerland: FDI stock in Latin America/Caribbean by Country, 1996

	Millions of US$	% share
Argentina	433	2.2
Brazil	3,630	18.5
Chile	1,275	6.5
Colombia	472	2.4
Mexico	1,370	7.0
Other LAC countries	824	4.2
Latin America/Caribbean	8,006	40.8
Offshore Centres/ Other	11,639	59.2
Overall Total	19,645	100.0

Source: Own calculations based on data provided by *Schweizerische Nationalbank* - Swiss National Bank.

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43. United Kingdom: FDI stock in Latin America/Caribbean by Country, 1996

	Millions of US$	% share
Argentina	813	3.4
Brazil	4,107	17.4
Chile	1,138	4.8
Colombia	2,163	9.2
Jamaica	598	2.5
Mexico	941	4.0
Other LAC	2,433	10.3
Latin America/Caribbean	12,193	51.7
Offshore Centres / Other	11,394	48.3
Overall Total	22,587	100.0

Source: Own calculations based on data provided by Office for National Statitics.

44. United Kingdom: FDI stock in Latin America[1] by Sector, 1996

	Millions of US$	% share
Total no-manufacturing	5,856	52.9
Energy	3,532	31.9
Distribution	355	3.2
Transport	1,355	12.2
Banking, finance and insurance	447	4.0
Other Services	124	1.1
Total manufacturing	5,208	47.1
Chemical Industry	1,616	14.6
Electronics, electrical equipment	85	0.8
Transport equipment	148	1.3
Food Products, Tobacco	1,722	15.6
Other manufacturing	1,566	14.1
Total	10,315	100,0

Source: Own calculations based on data provided by Office for National Statitics.

[1] Covers countries included in the definition of Latin America used by the Office for National Statistics. These are Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Cuba, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay and Venezuela.

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45. USA: FDI stock in Latin America/Caribbean by Country, 1996

	Millions of US$	% share
Argentina	8,060	5.6
Brazil	26,166	18.1
Chile	6,745	4.7
Colombia	3,468	2.4
Mexico	18,747	13.0
Venezuela	3,592	2.5
Other LAC	9,005	6.2
Latin America/Caribbean	75,783	52.6
Offshore Centres / Other	68,426	47.4
Overall Total	144,209	100.0

Source: Own calculations based on data provided by the US Department of Commerce / Bureau of Economic Analysis.

46. USA: FDI stock in Latin America/Caribbean by Sector, 1996

	Millions of US$	% share
Petroleum	6,488	4.5
Manufacturing	40,611	28.2
Wholesale trade	7,686	5.3
Banking	5,632	3.9
Finance (except banking)	69,181	48.0
Services	3,512	2.4
Other industries	11,1	7.7
All industries	144,209	100.0

Source: Own calculations based on data provided by the US Department of Commerce / Bureau of Economic Analysis.

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ANNEX III

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ABBREVIATIONS

ASEAN Association of South East Asian Nations

BBV *Banco Bilbao Vizcaya*

BCH *Banco Central Hispano*

BJ Bank of Japan

CCM *Caémi Mineracão e Metalurgia*

CNNDEE *Companhia Norte-Nordeste de Distribução de Energia Elétrica*

CNNDEE *Companhia Centro Oeste de Distribução de Energia*

COELBA *Companhia de Electricidade do Estado da Bahia Elétrica*

CPT *Compañía Peruana de Teléfonos*

CRT *Companhia Riograndese de Telecomunicações*

CTC *Compañía de Telecomunicaciones de Chile*

CVRD *Companhia Vale Do Rio Dose*

DM *Deutsche Mark*

DFER Department for Foreign Economic Relations of the French Ministry of Economy and Finance

DGEITE *Dirección General de Economía Internacional y Transacciones Exteriores (Ministerio de Economía y Hacienda, España)*
General Directorate for International Economy and Foreign Transactions, Spanish Ministry of Economy and Finance

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ECLAC	Economic Commission for Latin America and the Caribbean
EEC	European Economic Community
EFTA	European Free Trade Association
FDI	Foreign Direct Investment
FTAA	Free Trade Area of the Americas
GDP	Gross Domestic Product
GM	General Motors
IDB	Inter-American Development Bank
IMF	International Monetary Fund
IRELA	*Instituto de Relaciones Europeo-Latinoamericanas* Institute for European-Latin American Relations
INTAL	*Instituto para la Integración de América Latina y el Caribe* Institute for the Integration of Latin America and the Caribbean
IS	Import Substitution
JEXIM	Export-Import Bank of Japan
JETRO	Japan External Trade Organization
M & A	Mergers and Acquisitions
MERCOSUR	*Mercado Común del Sur* Southern Common Market
NAFTA	North American Free Trade Agreement
NICs	Newly-industrialized Countries

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OECD	Organization for Economic Cooperation and Development
PEMEX	*Petróleos Mexicanos*
R & D	Research and Development
SESSI	Statistical Service of the French Ministry of Industry
SME	Small and Medium-sized Enterprises
TISA	*Telefonía Internacional*
UNCTAD	United Nations Conference on Trade and Development
PDVSA	*Petróleos de Venezuela Sociedad Anónima*
SOBEET	*Sociedade Brasileira de Estudos de Empresas Transnacionais e da Globalizacão Económica*
TNCs	Transnational Corporations
VW	Volkswagen
WTO	World Trade Organization
YPF	*Yacimientos Petrolíferos Fiscales*

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Global flows of foreign direct investment (FDI) have increased rapidly in recent years, becoming a driving force in the process of economic and financial globalization. In the context of consolidating structural reforms and the return to higher rates of growth, annual FDI flows to Latin America and the Caribbean have risen fivefold in this decade in relation to the average of the 1980s. This book, the third in a joint effort by the Inter-American Development Bank (IDB) and the Institute for European-Latin American Relations (IRELA), analyzes this issue from the perspective of the countries that invest in the region. Separate chapters discuss in quantitative and qualitative terms the FDI of six main investing countries (France, Germany, Japan, Spain, the United Kingdom and the United States), while an additional chapter discusses intra-regional FDI, a phenomenom of growing significance in the region. The book also includes a comprehensive statistical annex on FDI flows and stock, and another on methodological issues related to the quantification of FDI.

The only timely, objective and detailed source on recent direct investment flows to Latin America. The comparison of the motivations of investors from the US, Japan and Europe, and the attraction of Latin America as opposed to other regions of the world is particularly useful. Foreign Direct Investment in Latin America and the Caribbean: Perspectives of the Major Investors *is an indispensable source for policy makers, international investors and academic researchers. IRELA and the IDB should be congratulated on a valuable contribution which should help promote investment in the region.*

Professor E.V.K. FitzGerald, Director of Financial Studies, University of Oxford

The IDB and IRELA have taken a new and important step in the study of foreign direct investment in Latin America. This new book provides a complete quantitative examination of recent FDI flows and offers a valuable analysis for understanding the behaviour and determinants of the main international productive investors. The careful selection of the authors of the various country chapters provides an excellent combination in one volume of the general elements of the FDI phenomenon and of aspects specific to the different source countries. The text also includes an innovative chapter on intra-regional investment.

Ricardo Ffrench-Davis, Regional Advisor,
Economic Commission for Latin America and the Caribbean (ECLAC)

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