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UNITED NATIONS INDUSTRIAL DEVELOPMENT ORGANIZATION
Vienna International Centre, P.O. Box 300, 1400 Vienna, Austria
Tel: (+43-1) 26026-0 · www.unido.org · unido@unido.org

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REGIONAL CO-OPERATION AMONG INDUSTRIAL DEVELOPMENT FINANCING INSTITUTIONS 1/

by

Tulio de Andrea
Consultant, Latin American
Association of Development
Financing Institutions (ALIDE)

1/ The views and opinions expressed in this paper are those of the consultant and do not necessarily reflect the views of the Secretariat of UNIDO.

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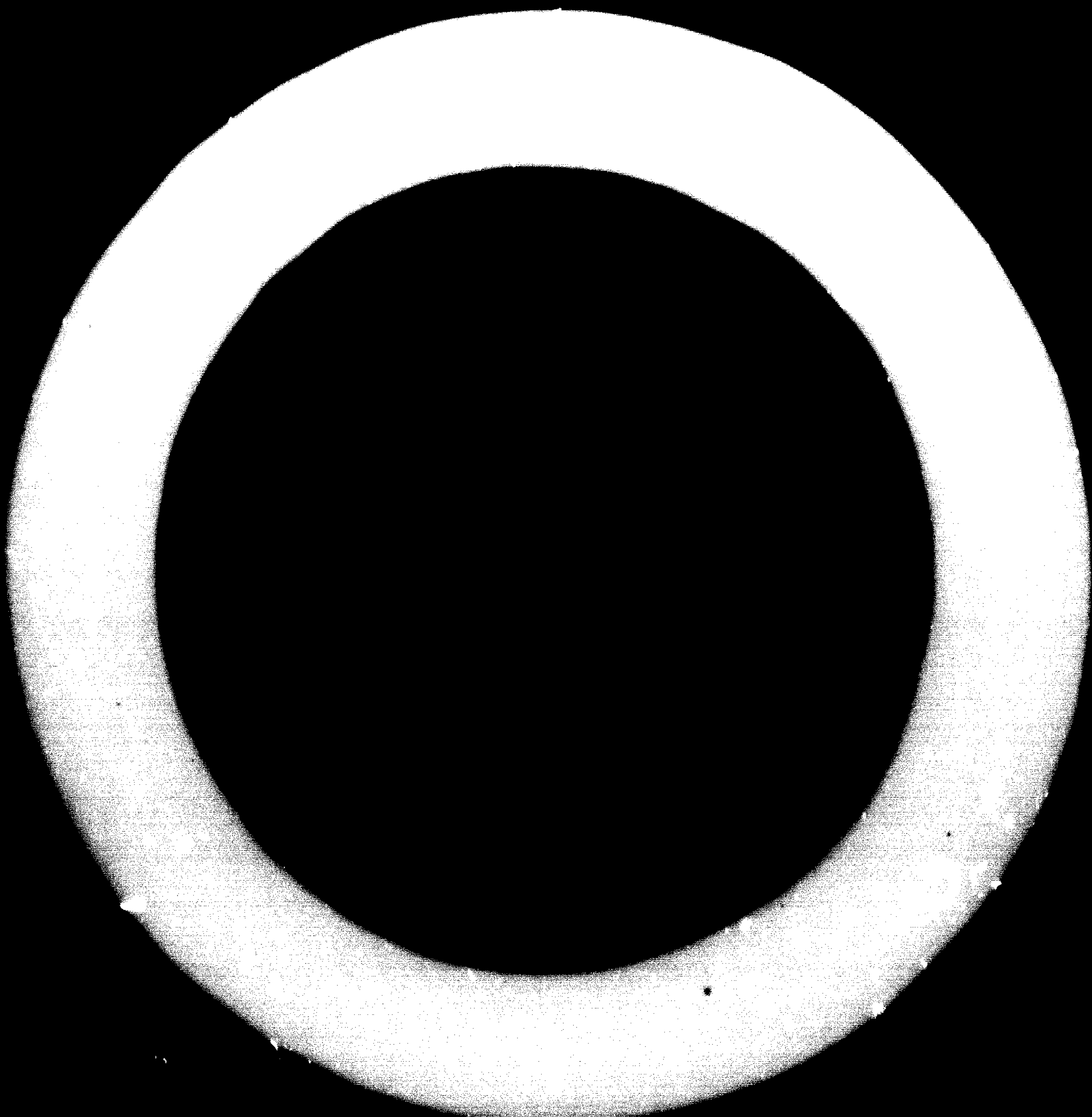

[illegible] CO-OPERATION AMONG [illegible]
DEVELOPMENT FINANCING I[illegible]

I am very pleased to participate as the representative of ALIDE in the Fourth Meeting on Co-operation among Industrial Development Financing Institutions, organized by the United Nations Industrial Development Organization (UNIDO), and to deliver a paper on regional co-operation among industrial development financing institutions. This paper attempts to discuss certain aspects of this interesting subject in a concise manner, in accordance with the outline proposed by UNIDO.

The comments relate to the Latin American experience. It was felt, however, that they were also pertinent to other developing regions which are doubtless confronted by the same problems. In fact, the differences which do exist are more of degree than of substance.

1. <u>Importance of regional co-operation in the industrialization of the developing countries</u>

Industrialization and development were in the past considered almost synonymous terms. It used to be said that where the industrialization process gained momentum, economic growth and, in general, social progress also occurred. Nowadays, conversely, it is accepted that while industrialization is an essential condition for the economic development of countries, it alone is not sufficient to guarantee that process.

The industrial development model based on national import substitution was termed "inward-oriented growth". It typified the process of the industrialization of most Latin American countries, particularly between the depression years of the thirties and the early sixties. It was a response to external instability and its backdrop was the domestic market of each country.

In the initial stage of this process, geared towards the production of finished consumer products, the model of national substitution for imports proved reasonably successful. Industry participated in the formation of the GNP of the countries and generated increased employment in the manufacturing sector, although to a lesser degree than in industrial production. But the consequences of unco-ordinated growth began to be felt, both in other branches of the economy and within the industrial [illegible] agriculture [illegible][1] [illegible], the [illegible] between the industrial sector and [illegible] consumer goods industry [illegible] increasingly strongly felt.

In some cases, export capacity [illegible] exports of primary products, which were the main earners of foreign currency, slowed down, while imports of foodstuffs, which impeded rational development in the agricultural sector, increased. Without a basic industry to rely on, industrial development became largely tied to imported raw materials and semi-finished goods which in turn created a dependency on foreign markets and a dangerous lack of flexibility in the balance of payments of Latin American countries.

The artificial and sometimes undesirable development of industry described above derived principally from the limited domestic markets and the poorly developed economic structure of so many developing countries. These did not permit rational integration either horizontally (integration of industry with other sectors of production) or vertically (of various activities within the industrial sector itself).

Towards the beginning of the sixties, it became essential for several Latin American countries to find a new industrial development model. In these countries, the process of providing substitutes for imported consumer goods was losing momentum, since saturation point had almost been reached as regards imports for which substitutes could be provided. The field left for the expansion of suitable industries was relatively limited since it was not linked to population growth, increased earnings and income distribution. Furthermore, carried forward by the inherent momentum of

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1/ By contrast, experience shows that developing countries which have been most successful in balancing their agricultural and industrial development are those which have strengthened the agricultural sector as a basis for the expansion of the industrial sector, since in the long run, investments in agriculture yield dividends in industrial growth.

2/ In some cases, basic industries were set up for political reasons, without regard to the needs of the industrial sector of the country and in the absence, both at the time and subsequently, of intermediate industries which would enable basic industries to function economically.

the development process, countries were forced to [illegible] in increasingly complex industrial activities which required a high level of technology and intensive capital investment but were not economical unless they could benefit from economies of scale.

It became essential to replace this model of "inward-oriented growth" in "water-tight compartments", which was operating slowly and increasingly inefficiently, by a concept of "outward-oriented growth", which would take advantage of the expanded market provided by all countries of the region and would permit both the rationalization of existing industry and the economical establishment of new industries. As a result, there were established in turn the Treaty on Central American Economic Integration, the Latin American Free Trade Association, the Andean Regional Group and the Caribbean Free Trade Area, most of them during the sixties.

Nowadays, co-operation between the countries of the Latin American region - whether in the form of expanded markets or industrial complementarity and economic integration agreements - is a prerequisite for the achievement of broader and more ambitious goals in the shorter term. Such co-operation will make it possible to overcome national restrictions to development, will transcend the limitations of domestic markets and will provide opportunities for large industrial installations, as well as consolidating the bargaining power of participating countries and improving their access to technology.

2. Development financing institutions and the regional integration process

The impetus achieved in the process of Latin American economic integration in the coming years will largely depend on the efforts made by the development financing institutions of that area. There are only few agencies whose sense of responsibility is such that integration would benefit capital, the entrepreneur and the economies of these countries in general.

In the task of establishing new enterprises or expanding and modernizing existing enterprises or rationalizing their production in order to take advantage of the benefits of reductions in customs tariffs or industrial complementation agreements, it would be possible to ensure by the combined action of development financing institutions and Latin American entrepreneurs and the harnessing of domestic savings in the region that these advantages would mainly and preferentially benefit Latin American countries. However, at present it is the large foreign corporations and not the Latin American industrialists who show themselves to be most aware of the significance of the lowering of trade barriers in the region or of the possibility of complementation between related manufacturing activities.

The various financing institutions have an important role to play in activating not only trade within the region and with other countries but also the movement of capital and highly skilled technical staff and the transfer of technology.

The subregional corporations and banks are the financial institutions that are specially competent to promote the process of integration between the countries within which they function. Such institutions, in Latin America, are the Central American Bank for Economic Integration (BCIE), the Caribbean Development Bank and the Andean Development Corporation (CAF).

The CAF, for example, "places the main emphasis on identifying and promoting projects, co-ordinating the action of various countries and entrepreneurs, seeking within and outside the area for appropriate opportunities, technical assistance, technology and patents, external partners and foreign capital contributions. In this respect, it must fundamentally be oriented towards projects whose impact will be particularly important in relation to the task of integration that has been entrusted to it"3/.

National financial institutions are also beginning to participate in the task of integration. The Industrial Bank of Peru acted until recently as the technical secretariat for the activities of public and private sectors with regard to the Andean Group, which was set up under the Cartagena Agreement. The Production Development Corporation of Chile (CORFO) has included in its organization a department for zonal and regional integration, whose functions are:

- To co-ordinate the work of CORFO with regard to integration, and to propose guidelines;

- To ensure that the industrial development programmes of CORFO are formulated in the light of the new conditions prevailing in the Andean market;

3/ Ingº. Adolfo Linares: "El financiamiento de la CAF en los planes de desarrollo de la Subregión" (Financing by the CAF in the development plans of the subregion). La Paz, Bolivia, June 1972.

- To represent CORFO vis-à-vis international and national organizations, both in the public and the private sector, in so far as the Andean sub-region, the Andean Development Corporation and LAFTA are concerned 4/.

3. Practical experience gained in the financing of regional projects, both by national banks and regional financial institutions

The activities of Latin American development finance institutions, both multilateral and national, have been concentrated on the financing of national projects. Not much attention has been devoted so far to regional projects, except, possibly, in the fields of physical infrastructure and power, in which some results have been achieved.

The Inter-American Development Bank (IDB), for example, has given technical and financial assistance for projects for the integrated development of frontier zones, by means of joint efforts by neighbouring countries, as is the case with the frontier studies for Colombia and Venezuela, Colombia and Ecuador, Argentina and Chile, and Argentina and Bolivia; for the identification of development projects for common geo-economic zones, as in the case of the riparian countries of the River Plate basin; and for the study and financing of specific integration projects, as in the case of the Acaray hydroelectric power station in the zone of the frontier between Paraguay, Argentina and Brazil.

In the middle of the sixties, the IDB set up the Preinvestment Fund for Latin American Integration, which was intended to finance studies and the preparation of the projects that would contribute towards accelerating the process of Latin American integration. The Bank applies these resources to financing preinvestment studies concerning the infrastructure, the integrated development of geo-economic zones that cover areas belonging to two or more countries, the establishment of basic industries on a regional scale, the joint exploitation of natural resources, research and the interchange of scientific and technical knowledge, the training of technical personnel and, in general, the mobilization of human resources.

4/ Production Development Corporation: Manual de Organización y Funciones (Organizational and Operational Manual) 1970.

In the industrial sector, [illegible] -exports [illegible] within the context of the [illegible] region. The most important results [illegible] related to industrial complementation. Colombia and Chile, for example, [illegible] the policy of considering any parts or assemblies produced in the LAFTA area as national inputs in the production of automobiles, provided that the value of the parts and assemblies imported and those exported offset one another. Thus, an important automobile parts industry has been growing in these countries; Chile exports gear boxes to Colombia and imports assembled engines from Colombia. Similarly, through their respective industrial development finance institutions - the Industrial Promotion Institute of Colombia (IFI) and the Production Development Corporation of Chile (CORFO), both countries have negotiated the joint and co-ordinated execution of a project for the manufacture of telephone switchboards and handsets. In Colombia, a caprolactam plant for the manufacture of nylon has commenced production, the investment having been financed by the Colombian Industrial Promotion Institute, the Venezuelan Petrochemicals Institute and foreign capital supplied by the proprietor of the technology. The capacity of the enterprise, Monómeros Colombo-Venezolanos S.A., is to be expanded to 45,000 tonnes/year in order to meet the needs of the Andean sub-region.

A more common example is the case of association between one or more financial institutions and domestic private savings in a country and a foreign enterprise for the installation of industries capable of serving the market of two or more countries. That is the case, for example, with the Industrial Bank of Peru, which associated itself with Bayer Químicas Unidas S.A. of Peru and Bayer A.G. of the Federal Republic of Germany to establish the Bayer Industrial S.A. enterprises, which produce acrylic fibres (Dralon) for the countries of the Andean Group.

4. Suggestions and recommendations for future action by financial institutions in the developing and developed countries to promote regional co-operation in industry. Problems and possible solutions

With regard to the regional or sub-regional integration processes towards which the economic co-operation efforts of developing countries such as those in Latin America should be aimed, the most important role to be played by development financing institutions will be that of promotion of multinational enterprises. Obviously, this is an ambitious and very challenging task, which lies within the purview not only of [illegible] ...in, [illegible] ...it has not been possible [illegible] to plan a large-scale operation [illegible] in Latin America. [illegible] must come when Latin American [illegible] ...have the right to [illegible] and can be shareholders of enterprises in any [illegible] region, just as they now own of enterprises in their own countries. As long as there is not a two-way road for investments among the Latin American countries with movement along it impeded by nothing more than rules establishing appropriate machinery for reciprocity, it will be said over and over again, just as it has hitherto, that an intra-regional economic bloc must be established, but rather little progress will in the final analysis have been made towards a deep-rooted and stable integration.

It is true that the integration process does not lead in the short term to the establishment of multinational enterprises with regional capital. The system for setting up such enterprises must be established little by little on the basis of agreements on multinational investments in the region or the sub-regions, whose gradual development will lead to the creation of Latin American multinational enterprises based on a uniform statute for the whole region.

The multilateral and national development financing institutions should prepare the ground for this important task. If they changed their attitude, they could exercise a decisive influence on the economic integration of countries.

Multilaterial institutions such as the International Bank for Reconstruction and Development and the Inter-American Development Bank have done very little in the field of regional co-operation in industry. On the contrary, remaining ever faithful to the policy of responding to the needs brought before them by each country - the same policy laid down by the World Bank when it started operating some 30 years ago, when the situation of the developing countries was so different from what it is today - they are now working against the very process of industrial integration. In fact, using multilateral funds made available to national financing institutions in the form of lump-sum loans, countries are trying to promote their own markets to the utmost, and it matters little if the projects are sometimes of scant benefit to [illegible] national institu- [illegible] integration projects.

[illegible] financing institutions [illegible] for promoting and executing integration projects. [illegible] on the national scale industrial [illegible] which [illegible] integration projects should at least [illegible] using their [illegible] or funds from other sources, but should not commit funds which [illegible] belong to all the countries of the region.

And if a change in the policy of the multilateral institutions is essential, it is also to be hoped that national institutions will adopt a fresh attitude. The time has come for them to stop turning their backs on one another and to act in unity and on a large scale.

One practical way of achieving this might be through the establishment of sub-regional funds for multinational projects with contributions from national development financing institutions and international agencies. These funds, which would take over from the Preinvestment Fund for Latin American Integration, would be operated by the sub-regional financing institutions, which would use the funds' resources, in consultation with countries and technical integration bodies (e.g. the Board of the Cartagena Agreement) to make multinational industrial investments in the countries of the sub-regions. It would be understood that State and private capital in each country where a project is implemented would provide the appropriate additional contribution. In the case of private capital, this would be done through broad-based public subscriptions. Foreign capital, when indispensable, could have a place in this scheme in keeping with the existing rules in each country or sub-region.

There is little doubt that the task ahead for development financing institutions is to bring about investment at the regional or sub-regional levels, going beyond the narrow limits of national boundaries. They must lay the foundation for future Latin American multinational enterprises and prepare the ground over which State-owned enterprises and private investors in the Latin American region or the sub-regions will move.

To conclude, there [illegible] development financing institutions in the regional industrial integration process, [illegible] that the officials of development financing institutions [illegible] not [illegible] fully [illegible] of the urgency of this co-operation. Frequently, they have an incomplete [illegible] of the problems arising out of isolated action by individual countries and of the advantages offered by the industrial integration process at the regional or sub-regional levels.

It is urgent to overcome the above-mentioned limitations, since the immediate present, which is a springboard for the achievement of effective integration, is the most difficult period to get through. This lack of awareness is the main reason why there continues to be sympathy for and a favourable attitude towards projects which would have to be rejected if they were judged from the regional point of view. This is a point to which programmes for the training of officials of development financing institutions should devote priority attention.

If there is any conclusion to be drawn from this paper, it is that close co-operation between development financing institutions in Latin America for the execution of large-scale regional integration projects, above all in the industrial field, is a matter of importance.

An important step was taken in this direction when the Latin American Association of Development Financing Institutions (ALIDE) was set up. The work which ALIDE has done in the few years of its existence to make the financing institutions throughout the region better acquainted with one another and to ensure that they co-ordinate their efforts in technical assistance, training and study programmes at the regional level deserves to have attention drawn to it. If it carried on with the same task and activity, it can transform itself into the driving force of co-operation posited by this paper, and this would be one of the most fruitful contributions which any Latin American institution has made for the benefit of Latin America.

[redacted]

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