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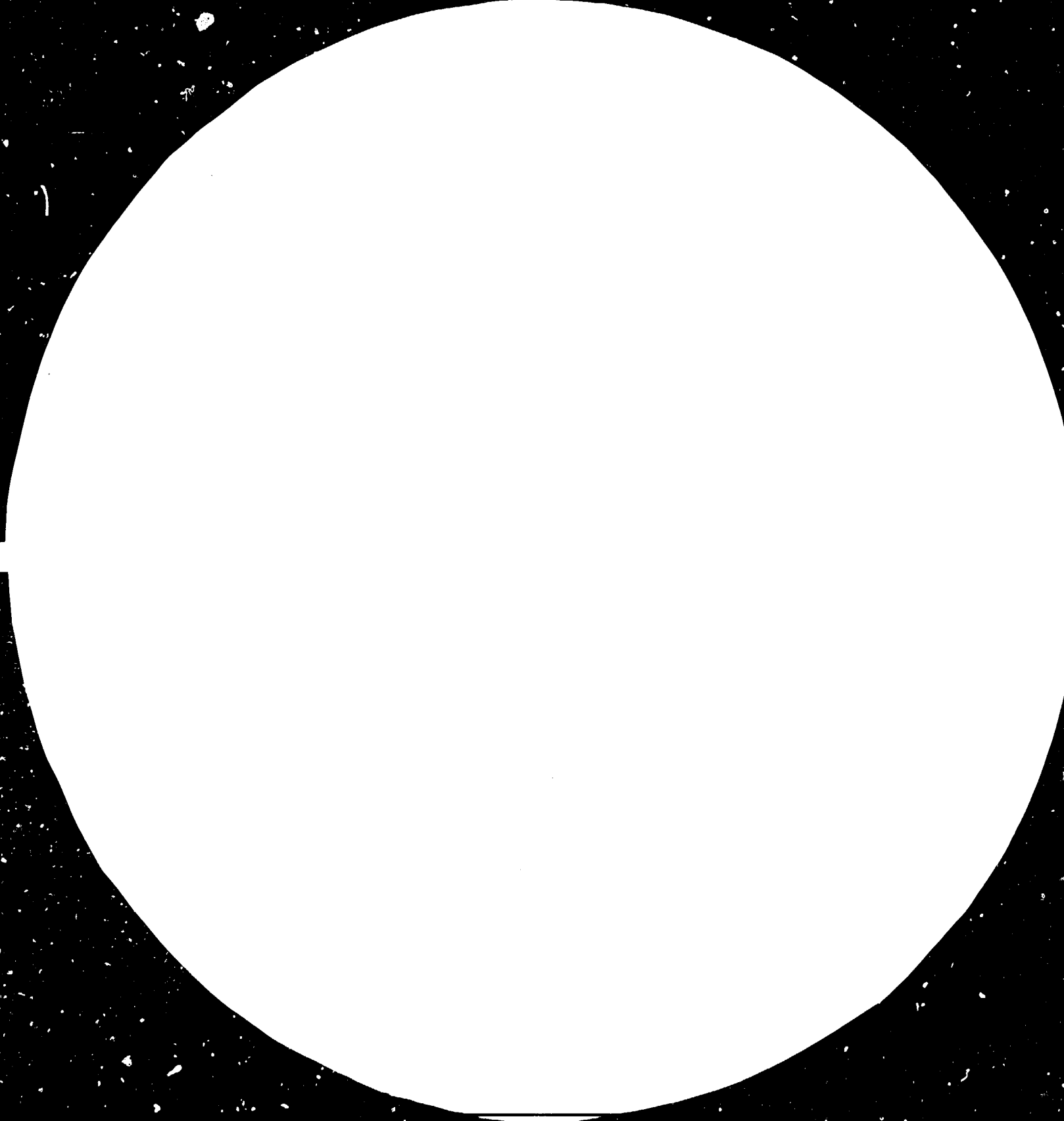
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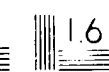
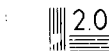
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Tripartite Forms of Industrial Co-operation*

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** IDC: Institute for Developing Countries.

Tripartite industrial co-operation (TIC) is a relatively recent form of trade creation for enterprises with different economic and social systems and at different levels of development. TIC projects are accordingly to be found in countries in three distinct regions: the socialist countries of Eastern Europe; the industrialized nations of Western Europe and North America; and the developing countries, which are often referred to as "east", "west" and "south" in the context of TIC.

Tripartite industrial co-operation evolved during the past decade from various bilateral forms of East-West and North-South industrial co-operation. In view of the increasing number of TIC contracts concluded, this form of co-operation would now appear to have passed the experimental stage and to have become an accepted form of inter-enterprise relations at the international level. The total number of tripartite projects, estimated to be around 100 in the early nineteen-seventies, has probably now exceeded 200 in the early nineteen-eighties.

Increasing attention has been paid at both bilateral and multilateral levels to this new and promising form of business relations. At the bilateral level, all East-West industrial co-operation agreements of the intergovernmental

type concluded since 1974 include provisions that define those forms of co-operation of particular interest to the contracting states. Many agreements include third-market co-operation, and include projects involving developing countries in other regions, among the forms mentioned. Indeed, many of the projects which were examined during preparation of this paper were either initiated or formulated, sometimes both, in the context of formal trade, payments and industrial co-operation agreements between the Governments of the partners. At the multilateral level, the importance of tripartite co-operation has been stressed in a number of resolutions of the United Nations General Assembly and of UNCTAD. Since 1975, the UNCTAD secretariat has been dealing on a regular basis with issues pertaining to tripartite co-operation, with a view to fostering this type of economic relations among countries with different economic and social systems and at different levels of development.

In order to cast additional light on this new phenomenon in international economic relations, a number of empirical studies have been undertaken by both individual researchers and international organizations during the last ten years or so. Although a considerable amount of factual knowledge has been accumulated in this way, much remains to be done to bridge the wide gaps which still exist in our understanding of this phenomenon. These deficiencies are to a large extent explained by the absence of precise and comparable information on the number of projects, their value, time-span and geographical and sectoral distribution.

For the purpose of this paper and in conformity with usually accepted practice, the term "tripartite industrial co-operation" is used to refer to a project in which an enterprise from a third (developing) country takes an active part, together with an enterprise from a socialist country and a firm from a market-economy country. For true TIC to operate, the developing-country partner should be not only a recipient, client, purchaser or beneficiary of the project but also an active participant. Should a developing country be merely a client and the partners come from Eastern and Western countries, then the term "co-operation in third countries" is considered to be more appropriate. Tripartite co-operation, therefore, as defined by the ECE, is an industrial arrangement which should be clearly distinguished from so-called "triangular" financial arrangements between oil producing surplus countries (providing capital), industrialized market economies (providing technology) and developing countries (acting as recipients of the above technology).

This paper is based upon specific study of some tripartite projects. The enterprises interviewed by the ECE secretariat can be divided into three broad categories depending on whether they are domiciled in Eastern, Southern or Western Europe. All these firms operate in energy and energy-related sectors - a field of activity in which largest number of tripartite projects are to be found. Out of twenty-one firms interviewed, fifteen are domiciled in Western Europe and three each in Eastern and Southern Europe.

The Western firms which were interviewed are among

the leading (usually transnational) firms in their respective industrial sectors, in terms of manufacturing output and exports, during the period when most of the tripartite projects examined here were completed.

Although the share of deliveries to third countries under tripartite arrangements was, on the whole, rather limited owing to the cyclical character of the power-plant sector, it nevertheless constituted an important share of the deliveries to developing countries in the years when these plants were being built.

All the East European enterprises interviewed in connection with this inquiry enjoy an international reputation and their Western counterparts can also be regarded as leading firms in their respective fields of activity. All have engaged in various forms of industrial co-operation for many years in both developed and developing countries - including TIC in more recent years. These enterprises have the status of Foreign Trade Organizations (FTOs) and are domiciled in Hungary and Romania, respectively - two centrally-planned-economy countries.

For reasons of geographical proximity and economic complementarity, Southern Europe is a region where a relatively large number of tripartite projects are to be found. The countries with more intensive experience in this respect are Greece, Turkey and Yugoslavia. The country which was selected for the purpose of conducting interviews is the last-named. This choice was motivated by two reasons: the first is that, as a developing country, Yugoslavia has been the recipient of a number of tripartite projects; the second is

that, as a socialist country with a well-developed industrial and technological base in such key sectors as energy, construction and plant engineering, this country has been actively involved - together with firms in developed market - economy countries - in a large number of projects in developing countries within as well as outside the European region.

The Yugoslav enterprises involved in tripartite projects, whether as recipient of such projects or as suppliers of equipment and technology to developing countries, are usually referred to as "organizations of associated labour" (OALs) - a term which designates enterprises which operate within the framework of a socialist system based on the concept of social property and workers self-management.

At the time the interviews were conducted, all the above-mentioned enterprises were involved in the supply of equipment, technology and services to developing countries under various organizational arrangements. Several macro- and micro-economic motives induce firms from the three regions to take part in TIC the most obvious of which is that the scope of most projects commonly found in developing countries is too wide for a single company or enterprise to handle on its own. It is therefore compelled to rely on the participation of other firms, including those located in the recipient country. Moreover, many of the labour-intensive components of a project, such as civil engineering and construction work, are more economically achieved by relying on local undertakings and their ability to mobilize large amounts of labour and materials. Despite the similarity of a number of basic motives, a distinction should be made between

the aims pursued by various types of enterprises and their underlying motivations.

Most projects in the energy (or, at least, an energy-related) sector, particularly primary energy processing, power generation plants and mining complexes, are usually of very large scale in terms of their capital requirements and the variety of technologies which they employ. As many of these projects are sited at remote locations, often distant from Western firms' traditional markets, the tripartite formula has several attractive features for the firms which may explain some of these firms' principal motivations when entering tripartite projects. Among these advantages are the following: (1) access to new markets: many of the project sites mentioned in the previous section are located in developing countries which have a large volume of trade with Eastern countries; by joining with Eastern enterprises, which may already be established in these markets, and forming consortia to carry out these large-scale projects, Western firms can obtain important orders; by combining its financing facilities with the bilateral clearing arrangements between the host government and the government of its Eastern partner, the Western firm is in a position to obtain orders that would otherwise be lost if the firm was a member of a consortia consisting solely of Western firms; (2) gaining maximum advantage from available concessionary financing: the combination of concessionary financing with project finance made available under bilateral clearing arrangements usually gives a Western company a substantial edge over its Western competitors; if the Western company has, in addition, licensed

its Eastern partner to manufacture a substantial portion of the equipment required for the project, which can be purchased by the client under the existing clearing account, then the consortium is likely to win the contract because the amount of foreign exchange required by the project will be that much less; and (3) fulfilling existing reciprocal purchase obligations to their Eastern partners.

Since the Yugoslav enterprises interviewed were involved in the supply of equipment and the provision of services together with their West European counterparts, the motives of these enterprises are usually consistent with those of the latter. The Yugoslav OALs interviewed cited four principal motives for their participation in tripartite projects: clients' requirements; interest of the main contractor; necessity of co-operation owing to the size and nature of a specific project; and terms of financing.

The motives cited by East European FTOs involved in tripartite co-operation do not differ basically from those of the Yugoslav firms referred to above. In addition to promoting the export of capital equipment and other goods, TIC assures regular sources of imports of basic commodities, such as crude oil and phosphates. TIC projects often help East European partners to become more familiar with Western technology. A motive often cited is access to new sources of finance which TIC offers Eastern enterprises, either from Western banks or through their Western partners. TIC projects are an additional means for Eastern partners of finding new markets and obtaining materials through the utilization of existing bilateral clearing agreements with developing coun-

tries.

A more precise and detailed analysis of enterprises' motives when entering into tripartite co-operation would require that these be related to the specific organizational scheme which is used for carrying out TIC and the role played by a given enterprise in these schemes. If one leaves aside a few production (and marketing) joint ventures, the quasi totality of TIC is constituted by co-operative schemes for the execution of a project of which the client is domiciled in a third (usually a developing) country. It consists of the delivery of production lines or complete plants and the construction of infrastructure objects. Joint projects are achieved through a variety of institutional arrangements which at the risk of over-simplification can be classified as follows:

Joint projects

Based on purely contractual arrangements		Based on consortia-type arrangements	
Based on contractor/sub-contractor relationship	Based on contractor/contractor relationship	Based on simple consortium relationship (without risk- and profit-sharing)	Based on complex consortia arrangements (involving risk- and profit-sharing)

Empirical studies carried out indicate that all the formulae indicated are encountered in tripartite arrangements and depend on the nature of the project for which a co-operative arrangement is sought.

Arrangements based on contractor/sub-contractor relationships are characterized by the fact that one of the

partners is the prime contractor and signs separate agreements with each of the sub-contractors. Thus, two sets of legal relationships are always present: between the bidders/suppliers themselves, and between the bidder and the client. Both sets of relationships are of the debtor-claimant type in which the partners do not assume risks jointly or share profits.

Available data indicate that many projects (more than one-third in the case of the Western firms interviewed) would appear to fall within this category. In most of the projects reviewed here which used this form of co-operation, the Western firms served as sub-contractors, even though many of them supplied as much as one-half of the services and deliveries required by the projects. As a rule, this type of co-operation implies sub-deliveries in the form of equipment and components.

Arrangements based on contractor/contractor relationships are preferred for the execution of more complex projects, especially when the question of industrial property rights arises and/or when the suppliers are required to grant separate credits. In this case, the partners may prefer that each of the two contractors be directly responsible to the client for supplies or for performance of the work entrusted to him under the terms of the order-contract which links him to the latter.

Despite the existence of separate - legally independent - contractual relationships, this form of co-operation implies that the partners co-operate informally, in a loose form of association by which each signs a separate

contract with the client for its part of the work. This form of co-operation is generally practised when each partner is paid separately by the client under different arrangements. Whilst the Eastern partner's deliveries are usually covered by a bilateral clearing agreement, those of the Western firm are paid in convertible currency.

Formed by tripartite industrial co-operation partners to carry out a specific project, a simple consortium arrangement does not constitute a legal entity; as such, it denotes a "loose" grouping of complementary resources and capacities for a limited duration, primarily designed to facilitate co-ordination of the partners' contributions to a project. A simple consortium may have the legal form of an "association momentanée" or that of "die einfache Gesellschaft".

Such a grouping has three principal features: there is no intention to incorporate; it is based on debtor-claimant relationships, not on risk and profit sharing; and its members do not have joint liability. Being constituted for a single project, the life of a simple consortium is fixed in duration. Moreover, it is based on a double set of legal relations: on the one hand, between the consortium members and the client, embodied in the order-contract; on the other hand, between the consortium members and governed by the contract drawn up at the time when the consortium is established. A simple consortium may also include various sub-contracting arrangements with parties which may not have acceded to the main consortium contract.

Also known as unincorporated partnerships or contractual non-equity joint ventures, the principal feature of

arrangements based on risk- and profit-sharing mechanisms is risk and profit sharing. Even though it is not considered to be a legal entity, i.e. it does not possess a juridical personality, such an association nevertheless does have joint liability, despite its lack of corporate formalities.

According to the enterprises interviewed, the joint venture formula is seldom used in practice. In fact, it would appear that the needs of the partners can be met by the simpler consortium arrangements described above which make it possible for the co-operating firms to define in advance their respective contributions to the project and the ensuing liabilities.

Once it has been decided to carry out a project by using the tripartite approach, a much broader range of financing possibilities becomes available from the point of view of the client. The financing mechanisms commonly employed when the project contractors are exclusively of Eastern and Western origin correspond to the resources which these contractors are capable of mobilizing for the client country. In other words, a tripartite project permits the partners to mobilize a wider variety of financing resources than if only Western firms or Eastern enterprises were to execute the project on their own.

The principal sources of financing to which Eastern and Western partners generally have access for tripartite projects include the following: (i) borrowing from the capital markets of the industrialized market economies on commercial conditions; (ii) bilateral (and multilateral) capital assistance programmes; and (iii) bilateral clearing

agreements.

Most tripartite project in energy-related and other basic industrial sectors make use of commercial financing arrangements for a substantial portion of the cost of capital equipment, services and other charges billed in convertible currencies. Commercial financing sources are generally relied upon by Western firms for that part of their deliveries which is not covered by preferential credits, financing being made available under various loan agreements between the client and one of the international development banks of the bilateral clearing arrangements of the Eastern partner. As a general rule, it may be stated that the larger the cost of a tripartite project the greater the share of non-commercial financing, particularly if the Eastern partner is supplying a large share of the equipment under bilateral clearing arrangements. When the share of project credits granted by governmental capital assistance programmes and multinational credit institutions, such as the World Bank, is added to the amount covered by bilateral clearing arrangements, the percentage of commercial financing may amount to only a minor share of the total cost of a project.

The availability of government-assisted concessionary financing for tripartite projects is mainly determined by the status of the recipient country, i.e. whether it qualifies for financing on preferential terms, and if it is in no way affected by the tripartite nature of consortia. Many Western governments offer financing for large-scale projects in developing countries on favourable terms as part of these governments' development assistance programmes. Since many

projects carried out on a tripartite basis generally include Western partners from countries that have such programmes, a share of these partners' contributions to such projects makes use of preferential financing, such as low-cost direct loans, mixed credits and subsidized credit insurance against political and commercial risks.

Western suppliers of power plants from industrialized countries whose governments make available these preferential credits obviously can offer prices to their clients that are more competitive than those of manufacturers from countries which do not have such bilateral capital assistance programmes. The fact that an increasing number of industrialized countries have adopted such programmes in recent years has helped to intensify competition among suppliers from these countries.

One of the most effective means of reducing the convertible-currency component of a large power station project has been the inclusion of an Eastern partner in a Western consortium, which makes it possible to supply many equipment items and various services for payment under the terms of an existing bilateral clearing account. Since Western equipment suppliers increasingly compete on the basis of prices determined by governmental capital assistance programmes that offer similar preferential terms to developing-country clients, the tripartite approach often turns out to be the only means available for many Western suppliers to gain a competitive edge in their offers. Indeed, the availability of bilateral clearing arrangements for financing

part of a power plant project is often a crucial factor in the decision of a Western consortium to include an Eastern enterprise as a partner.

The majority of the projects examined involved the financing of part or the whole of the deliveries through existing bilateral clearing arrangements. In most cases, the deliveries of the Eastern partner were paid under such arrangements although in a few projects the Western partner also received payment through the clearing account of its Eastern partner. An analysis of tripartite projects reviewed here for their bilateral clearing elements tends to support the conclusion that the existence of such a payment mechanism often explains why an East European partner is included in a consortium by the Western partners who have the leading role. In other words, if the initiative for a tripartite project comes from the Western side, it is usually dictated by the favourable payment arrangement afforded by an existing bilateral clearing account between an Eastern country and the country of the client. Although many reasons other than financing considerations may persuade firms to enter tripartite arrangements, this factor appears to have been the decisive motive in quite a few instances.

In a view of the complexity of tripartite arrangements, it is not surprising that many problems of a managerial nature are encountered at the project preparation and project implementation stages. Some problems of a general nature reported by various enterprises in Eastern and Western countries concern the difficulty in finding partners whose

whose capabilities complement each other. Others are due to the intricate organizational and financial procedures required to bring about a project to its successful completion. These problems which may explain why many proposed undertakings never reach the project stage are briefly reviewed below.

The nature of problems encountered at the project preparation phase depends on whether the enterprise acts as a sub-contractor or a full consortium member. Several of the firms which limited their third-market co-operation to sub-contracted deliveries often could not include components and equipment from their prospective partner because of the late arrival of the quotations they had requested. In other cases, even though the quotations did arrive on time they had not been adapted to the partner's specific technical requirements, a fact which often resulted in higher costs. In cases when firms were willing to serve as consortium members in their own right, the firms were unable to take part in the tender because their respective governments' export credit guarantees did not provide cover for the countries in which the proposed project was to be located. Indeed, according to several enterprises interviewed, of all problems listed those involving financing arrangements were considered to be the most important.

A wide variety of problems was reported to have arisen at the project implementation phase. According to the majority of Western enterprises interviewed by the secretariat, most tripartite projects experienced substantial delays of one type or another. These delays were due to a wide variety of causes; most of them can be attributed to lack of experience

on the part of the firms' partners in working to tight project schedules during the manufacturing and erection phases. Delays during the planning stage were often occasioned by problems in obtaining the necessary import permits for components which, some governments contended, could be manufactured locally at equal cost. Many of the firms interviewed were confronted by the need to assign more of their specialists during the erection and start-up phases of a project than they had anticipated because locally-available personnel often did not possess the necessary skills. In addition to these problems, smooth co-ordination was reported to be often hindered by lack of flexibility in quickly-changing production schedules of the enterprises supplying equipment to tripartite projects.

In the various cases when a project was partly financed (directly or indirectly) through counter-purchases and related reciprocal trading arrangements between the Eastern and Western partners, the North-South direction of deliveries was sometimes affected by lack of agreement on counter-purchases in the East-West direction. Often the usual counter-trade obligations of the Western partner had to be considerably increased when a third-country project suddenly entailed additional purchases by an Eastern enterprise from its Western partner. In a number of instances, the total cost of particular projects had to be raised in order to compensate for unforeseen delays, increases in equipment and material prices, and additional personnel.



