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Final Report

16100

INDUSTRIAL CO-OPERATION AND INVESTMENT POLICIES WITHIN THE REGIONAL ARRANGEMENTS IN LATIN AMERICA AND THE CARIBBEAN*

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Vienna, January 1987

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INTRODUCTION

The objective of this paper is to review different industrial co-operation and investment policies within the regional and subregional economic integration schemes in Latin America and the Caribbean.

The research was made during January of 1987 for the Regional and Country Studies Branch of the Studies and Research Division of UNIDO, in Santiago, Buenos Aires and Vienna.

In Chapter 1 to 9 the current situation of industrial co-operation and investment policies is reviewed. Emphasis is put on description more than on analysis, ad it was required. The epilogue attemtps to put some conceptual aspects of the economic integration process within the framework of the theory of the internationalization of production; this is done in a very schematic way because of time limitations. Also, some suggestions are made for UNIDO's work programme.

The Annex provide with a massive amount of basic information on the diverse economic integration schemes in Latin America and the Caribbean. Where they are not needed they would be rejected from the main body of the study.

1. REGIONAL INDUSTRIAL PROGRAMMING

Industrial growth is confronted in Latin America by serious problems, both on the demand (size and structure of the markets) and on the supply side (availability of resources, technology and inputs). One way out of these problems which Latin American countries have taken is the integration of the industrial productive sectors. The results have not been very successful to far.

(a) Central American Common Market (CACM)

The aim of Central American Common Market on this regard was to promote investments in the "integration industries", designated as such because they needed the expanded Central American Market to reach economies of scale in order to operate under competitive conditions. These industries would benefit from the unrestricted opening of member country markets and from the protection against external competition provided by a common external tariff.

Only four "integration industries" have been selected: caustic soda and chlorinated insecticides in Nicaragua; vehicle tires and tubes in Guatemala; and flat and sheet glass in Honduras. The latter was never materialized. In fact, the Integration Industries Régime lost its attraction when the general Treaty was approved in 1960, since the latter established the commitment to move on within a short period toward the full liberalization of trade and the adoption of a common external tariff.

(b) LAFTA/LAIA

The Treaty of Montevideo included a provision for the co-ordination of national industrialization policies, although the main aim of LAFTA was to form a free trade zone. Complementation agreements were established by industrial sectors, as specific programming instruments.

Most of these Complementation Agreements have been nothing else than inter-firm trade specialization by TNCs. Only one of them - No. 6, referring to the petrochemical sector, which was signed by Bolivia, Colombia, Chile and Peru in 1968 - was about new investments and it would serve as a starting point for a Sectoral Industrial programme for the Andean Group.

The LAIA Treaty does not envisage any specific instrument for integration of the industrial sector. The Agreements of Partial Scope are very alike to the old Complementation Agreements and any initiative in the direction of industrial programming within LAIA have to be undertaken through this instrument.

(c) CARIFTA/CARICOM

CARIFTA/CARICOM has a provision for region-wide industrial programming through the selection and location of industries, but this has not yet been fully defined and the application of it has been very marginal.

Efforts to programme industrial production on a regional basis have been slow and disappointing. The only practical achievement to date has been the allocation by the Eastern Caribbean Common Market (ECCM) of thirty-one industries, of which about seven have come on stream in the subregion; no other achievements were registered in the fields of joint promotion of industrial development. The feasibility study of a regional aluminium complex

still awaits final decisions by the Governments concerned. At the wider CARICOM level a technical study outlining a framework for regional industrial programming in pursuit of the objectives of Article 46 of the Common Market Annex to the Treaty has only recently been completed. The policy guidelines which were used for the study are the satisfaction of basic needs, foreign exchange earnings or savings, use of regional raw materials, promotion of employment and strengthening of the domestic and export sectors of the regional ecomony.[1/]

Recently, the CARICOM Council of Ministers has established a Regional Garment and Textile Advisory Committee of eleven persons drawn from the public and private sectors in the Region. The Committee will function as an advisory body to the Common Market Council. It is charged with examining the needs of the industry, in particular in the areas of protection, marketing and technical assistance and with making recommendations to the Common Market Council on what should be done to meet those needs.[2/]

(d) Andean Group

The Andean Group established two main instruments in this regard: the Rationalization programme, focusing on existing industry (IRP) and the Sectoral Industrial Development programmes (SIDP) for programming new investments.

Not a single IRP has been drawn up in the context of the Andean integration process, mainly because of the opposition of existing enterprises.

The SIDPs may be considered sectoral custom unions since they consolidate the expanded market for the products of the programmed sector by fixing the common external tariff for it and liberalizing reciprocal trade with regard to the particular product concerned. They are an attempt to systematically allocate industries among member countries to avoid duplication of production and unnecessary competition. Only selected industries are to be included as programs, and each program will cover one industry, with products within the industry assigned to member countries. programmes are designed to provide favorable tariff preferences and temporary monopolies and semi-monopolies over the manufacture of the products.

It was hoped that through industrial planning the ANCOM members would develop new specialized industries and improve existing ones, thus reducing the need for imports and increasing the amount of exports and employment to the benefit of overall regional development.

The Board of the Agreement drew up eight proposals for SIDPs: in the petrochemical, metal working, automotive, iron and steel, electronics and telecommunications, chemicals, pharmaceuticals and fertilizer sectors. The country members considered feasible only the first four. However, only the three first have been approved and the automotive has become obsolete as TNCs are going through an intense re-shaping of the industry on a regional and world basis.

The petrochemical and the metal working programs have experienced several technical and economic problems that have complicated their functioning to

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1/ The Caribbean Community in the 1980s, Guyana, 1981 and Caribbean Development Bank Annual Report 1985.

2/ Caricom Perspective, November-December 1985.

such an extent that changes in them are currently being negotiated. The first one has suffered from oil price fluctuations; the second one is the only one which has resulted in exchanges of certain relevance, especially from a qualitative point of view.

The participation of the private sector in the planning process of the metal working program was minimal. Indeed, some of the difficulties later encountered in finding domestic extrepreneurs willing to undertake feasibility studies and invest in the manufacture of products assigned under the program can be traced to the lack of involvement of the private sector in the evolution and implementation of the program. Ultimately it would fall to the technical experts of the Board to draft the outlines of what would become the metal working program.[1/]

Product assignation had several problems. On the one hand, high technology products were assigned to countries with the lowest technological capabilities in metal working, in order to give them a "big push". So Bolivia and Ecuador were forced to turn to TNCs not only for technology but also as partners. On the other hand, an independent evaluation of the assignations rated quite badly those made to Bolivia and Ecuador, while around half of the assignation made to Colombia, Chile and Peru were rated as positive.[2/]

Regarding the petrochemical agreement, TNCs' pressures exacerbated interstate conflicts by enhancing the nationalistic bargaining behavior of Andean negotiators eager to create national petrochemical industries based on domestic natural gas or petroleum resources. The result of this coincidence of interests and technology was a compromise in the rationality of industrial planning efforts in the petrochemical sector. The creation of six wholly integrated petrochemical complexes built in production inefficiencies right from the outset of the programme.

The Andean countries have also designed other instruments for joint industrial development. They are the Intersectoral Industrial Development programmes and the Integral Development Projects, which have not resulted in tangible results yet. The Board of the Agreement put forward a proposal for organizing programs of this kind for the electronics and telecommunications, chemicals and pharmaceutical sectors, but they were not accepted by the countries.

(e) Cauce

The Cauce Treaty between Argentina and Uruguay was signed in 1974. Its main objective is bilateral trade, but it could have some direct consequences for the industrial sector. In fact, one of its goals is to coordinate industrial activities and other, to promote binational enterprises.

In practice, Cauce has been utilized for industrial complementation only by TNCs within the car industry (Fiat and Renault).[3/]

1/ Lynn Mytelka, Regional Development in a Global Economy, Yale, 1979.

2/ Eduardo Gana, La programación metalmecánica, Cepal 1978.

3/ Pablo Bustos, El Cauce como instrumento por la integración económica de Argentina y Uruguay, Fundación Ebert, 1986.

2. PROMOTION OF REGIONAL MULTINATIONAL ENTERPRISES

(a) Andean Group[1/]

The countries' interest in encouraging the establishment of some type of mutinational enterprise can be traced back to August 1966 when Colombia, Chile, Venezuela, Ecuador and Peru signed the Declaration of Bogota. This document calls for the adoption of projects in which enterprises and capital of several Latin American countries can participate in order to facilitate the process of integration. Later, when the Cartagena Agreement was signed, it contained a provision to approve a uniform regime for multinational enterprises (Article 28); to recommend the establishment of mutinational enterprises for the implementation, expansion or complementation of certain industries in the area of industrial programming (Article 38); and to establish multinational enterprises which facilitate the development of infrastructure projects in the fields of energy, transportation and communications (Article 86). The first rules of the Andean Group on this subject were contained in Decision 46 (1971) (See the text in the Annex). However, Decision 46 was unable to stimulate the creation of multinationals: it contained complex and time-consuming rules for the formation and operation of these firms and imposed restrictions on their areas of activity. So in 1982, Decision 169 was approved in an attempt to eliminate some regidities of Decision 46; the firms are now called Andean Multinational Enterprises (AME).

The main characteristics of an AME are set forth in Articles 1 and 2 of Decision 169 and include the following:

(1) AME's must receive contributions from national investors of two or more member countries and they must total more than 80 per cent of the capital of the enterprise.

(2) Contributions from foreign investors must be less than 20 per cent of the capital of the enterprise.

(3) When the enterprise is capitalized with contributions from only two member countries, the sum of the contributions from the investors of each member country may not be less than 15 per cent of the capital of the enterprise. If there are investors from more than two member countries, the contributions from at least two countries shall meet the above-mentioned requirements. In both cases, investors from the country where the principal place of business is located shall contribute 15 per cent or more of the capital of the enterprise.

(4) The principal place of business shall be located in one of the member countries.

(5) The majority of subregional capital shall be reflected inthe technical, administrative, financial and commercial operation of the enterprise.

1/ R. Cherol and J. Nvñez del Arco, "Empresas Multinacionalos Andinas: un nuevo enfoque a las inversiones multinacionalas en al Grupo Andino, Integración Latinoamericana, 1983.

(6) AME's located in Bolivia and Ecuador may consist of subregional capital contributions amounting to 60 per cent and foreign capital contributions amounting to 40 per cent for a period of ten years from the establishments of the enterprise, or fifteen years from the time Decision 169 becomes effective.

All AME's may enjoy the following benefits:

(1) The products of an AME shall enjoy all the benefits of the trade liberalization programme.

(2) The enterprise shall receive the same tax treatment as an equivalent national enterprise.

(3) The AME shall have access to domestic credit and the same financial treatment as a national enterprise.

(4) The enterprise shall not be required to obtain prior authorization from the appropriate national agency to invest or reinvest in the same country as the principal office. Also in such cases, the net profits of the AME's shall be transferable in freely convertible currency.

(5) AME's may establish branch offices in member countries other than the one where the principal office is located.

(6) With the authorization of the appropriate national agency, the AME, or its branch, may participate in sectors reserved for national enterprises.

(7) The branches, with the authorization of the appropriate national agency, may transfer all net profits in freely convertible currency to the principal office.

(8) Foreign and subregional investors in an AME may transfer abroad, with the authorization of the appropriate national agency, all net profits in freely convertible currency.

(9) To avoid double taxation, shareholders of an AME will not be required to pay taxes on the profits received from the branch office which are redistributed to them as dividends by the main office, not will investment companies which are shareholders in AME's be required to pay taxes on the income they derive from the redistribution of the AME's profits.

(10) Member countries shall treat subregional employees of an AME as national empoyees for purposes of the application of foreign labour quotas.

(11) Member countries shall facilitate the entry into their territories of promoters, investors, and executives of such enterprises.

(12) Member countries shall facilitate the contracting of technology, patents and trademarks within the region where the AME's operate.

(b) SELA[1/]

The Sistema Económico Latinoamericano (SELA) is a vast programme of regional co-operation adopted in 1975 by most Latin American countries. The Panama Agreement for the constitution of SELA includes, as one of the objectives of the system, "to improve the allocation of human, natural,technical and financial resources of the region, through the formation and stimulation of Latin American Multinational Enterprises.....Such enterprises can be created with contributions of State, para-state, private or mixed capital, whose national character is to be granted by the Member States, and whose actibities are to be subject to their jurisdiction and control". The mechanisms for the promotion of LMA are based on the SELA "Action Committees" created for a variety of sectors. The origin of MULTIFERT S.A. is the work of the "Action Codmmittee" on fertilizers created by SELA with the purpose of exploring and promoting the creation of a commercialization mechanism jointly owned by the Latin American Countries to deal with the regional demand and supuply of fertilizers and their raw materials, with the objectives of rationalizing the trade among the countries and carry out joint imports from third countries on the basis of an increased bargaining power. MULTIFERT was created in 1978 by a treaty among the governments of Bolivia, Costa Rica, Cuba Guatemala, Mexico, Nicáragua, Panama, Peru and Venezuela. Its headquarters are in Panama and the authorized capital amounts to US $3.75 million. So far, it is the only LMA.

The basic rationale for the creation of MULTIFERT derived from the critical importance of the agricultural sector in the Latin American economies, and the need to improve its productivity through the increased use of fertilizers. In 1974, Latin American production represented only 46.9 per cent of total consumption. Such external dependence created balance of payments problems and serious vulnerability, in a market characterized by strong price oscillations frequently caused by dumping practices on the part of the industrialized countries.

1/ Eduardo White and Marcelo Halperín, Regional regimes for the promotion of joint ventures among developing countries, Cedrei, July 1985.

3. MEASURES FOR CAPITAL GOODS FOREIGN TRADE

(a) Latinequip

Latinequip is an incorporated company whose shareholders are public sector financial institutions - the Bank of the Province of Buenos Aires, the Bank of the State of Sao Peuto and the National Financiera of Mexico. Its aim is to provide assistance to the exporters of capital goods in the commercialization, financing and technology transfer operations as well as in the establishment of joint ventures. For services supplied to interested companies Latinequip charges a fee to be agreed upon in accordance with the specific characteristics of each operation.

Latin American exports of capital goods reached 2 per cent of the world total in 1982 while regional imports accounted for 7 per cent of the same total. Intra-regional trade of capital goods, on the other hand, represented something less than 5 per cent of the total market during the same year. Capital goods exports represented 12.5 per cent, 14 per cent and 12.9 per cent of the production of Argentina, Brazil and Mexico during 1982-1983. In the same year, 56 per cent of Argentina, 49 per cent of Brazilian and 8 per cent of Mexican exports of capital goods were shipped to other developing countries.

The services offered by Latinequip officially include the following:

(a) Periodical survices of regional export supply;

(b) Search and development of markets through a set of commercial offices and/or representatives;

(c) Survey of made to order capital goods' demand. This includes projects financed by multilateral credit institutions; development plants and investment programmes of large government enterprises;

(d) Constitution of consortia among suppliers;

(e) Aid to obtain financing at private and public levels;

(f) Transfer of technology and development of joint ventures;

(g) Negotiation with relevant authorities.

Latinequip entered its operative stage by the end of 1984 and since then only 10 operations for a total value of US $20 million have been fully concluded and signed. Its project portfolio, however, reaches almost 600 operations, of which only an undetermined proportion will be carried out.

One major weakness of Latinequip is that it does not operates with the "last fund" modality which is often required in order to develop a commercial operation. Potential buyer often do not know what they need and somebody has to finance preliminary studies even at the risk of losing the money if the deal is finally not closed. In order to be competitive with industrialized countries' traders this requisite has to be met.

(b) The Agreement between Argentina and Brazil

The recent Integration and Co-operation Act signed by Argentina and Brazil established a programme for bilateral economic integration which should

be characterized by its gradual character, a growing degree of policy harmonization, intersectoral specialization, progressive equilibrium of reciprocal trade and the active participation of private entrepreneurs in both countries.

The programme consists of twelve Protocols (their texts may be found in the Annex). Their subjects are the following ones:[1/]

1. Creation of a customs union in bilateral trade in capital goods with removal of all trade barriers and promotion of balanced trade.

2. Planned growth in Brazilian wheat purchases from Argentina.

3. Promotion of food security in both countries through increased trade in food products to eliminate seasonal shortages.

4. Promotion of overall trade levels between the two countries, with enphasis on eliminating trade imbalances.

5. Promotion of joint ventures between industrialists of both countries.

6. Financial support from central banks to support adjustment to trade imbalances.

7. Investment fund to be created to expand production.

8. Co-operation in energy development to expand oil and gas production in Argentina and joint electricity generation.

9. Promotion of biotechnology.

10. Creation of economic research centres to monitor the integration project.

11. Co-operation in the event of nuclear accidents.

12. Co-operation in aerospace to develop joint export potential.

Most of the Protocols could have an impact on industrial development and co-operation between the two countries. However, all of them need to be defined in a more systematic way. So far only one of them has been implemented, No. 1 on capital goods, although protocol No.7 is also involved.

Agreement could not be reached on other sectors which were also considered; petrochemical, chemical, plastic and electronics industries, as well as the automotive industry. With regard to this latter case, the merger of Ford and Volkswagen in the two countries has forced other firms in that sector to aks for protection and a schism has developed between the manufacturers and part suppliers. No agreement was reached concerning maritime transport either as the respective flag carriers were unable to develop a formula for dividing shipping.[2/]

1/ Translations were taken from the Financial Times, 1 August 1986.

2/ Business Latin America, 22 December 1986.

Protocol No. 1 on Capital Goods

For the time being the Protocol is a custom union. Both countries agreed to erase tariff and non-tariff restrictions to those goods included in the First Common List (See the Annex for a complete list of the capital goods included). The objective is to reach a bilateral trade of US $2,000 million between 1987 and 1990, starting with US $300 million during 1987 (The figure for 1985 was about US $200 million). They will also have a common external tarif regarding these goods. The national treatment can only be granted to products with less than 20 per cent of imported inputs.

Each semester the list would be increased with new items up to 50 per cent of the universe of agreed capital goods.

The expansion of the universal exchange must be both equilibrated and symmetrical. In practical terms that means that if the Brazilian annual superavit is greater than 20 per cent of the agreed value, some corrective measures are to be put into effect. According to the Protocol No.7, in that case both countries will increase the Investment Fund for the same amount of this supravit and this new funds will be invested in Argentina, in order to improve its productive and exporting capabilities. If the superavit surpasses 40 per cent of that value, according to the article 10 of Protocol No. 1, "necessary measures will be adopted, which must be compatible with the general trade situation, in order to correct such disequilibrium."

The Ministers of Finance and Economy of both countries must co-ordinate their politics on foreign exchange rate in order to achieve an stable exchange rate between both countries. Exchange rate policy should be neutral with regard to the relative competitiveness of exports and imports.

There are significant differences between incentives, benefits, imports price and protection vis-á-vis third countries in Argentina and Brazil. Both governments would compensate for their "asymmetries". The idea is to isolate the purely competitive aspects of the final price. This "pampered" trade is a new concept in the region. Another characteristic of the Agreement which is also something new is that the private sector played a very active role in Argentina, although the Brazilian list was made by bureaucrats. The Argentinian list was completely put together by private firms and in fact is has some ad-hoc flair in it.

The main issues involved for the Argentinian firms were the following ones:

(a) Wage differentiation. Studies specially made confirmed that qualified labor is more expensive in Brazil, while the opposite is true about unqualified labor. On the other hand, wages represent a small fraction of total costs;

(b) Financial costs of production. This has not been discussed with Brazil. In the meanwhile, they are higher in Argentina and the government is looking for some way to correct it;

(c) Export promotion schemes. Here the Brazilians have a problem because the Argentinian scheme is more favourable than CACEX's; and

(d) Financing of the trade operation. Here some changes are needed in both countries in order to put them in line with each other.

It has been suggested that this Agreement could open a new stage of the Latin American integration process which would be characterized by a slower, more gradualistic approach and by its emphasis on bilateral links. In fact, ALADI led the way already in 1980. What seems really new in the Agreement is the active participation of the private national firms; the emphasis which has been put on the capital good sector and the active participation of Brazil. In the past it has been said that the process of economic integration needed a strong locomotive: maybe Brazil will provide that driving force.

Akwardly, worries about the future of the industrial aspects of the Protocols are concentrated in the evolution of the Brazilian economy and not on the expectations of the private Argentinian sector.

So far Uruguay has only approved a special agreement with Brazil, which is basically a wheat-and-meat for industrial products exchange. The same country had already signed CAUCE with Argentina in 1974.

One interesting point came out in Argentina with regard to the financing of the compensation for the steel price to be paid to local manufacturers of final products. In the end the Argentinian Chamber of Capital Goods Producers will pay one third of the total and the public sector will pay the rest.

All promotional regimes should not keep going for ever. It remains to be seen how fast could they be withdrawn.

4. FOREIGN INVESTMENT POLICIES

(a) The Andean Group[1/]

Competent national agencies. These are responsable for authorities, registering and monitoring direct foreign investment and approving contracts on transfer of technology and on patents, as well as for signing and monitoring agreements on the conversion of foreign enterprises as provided in the Common Regime for Foreign Capital and Technology (the text of Decision 24 may be found in the Annex).

One important point which has not been settled in the AP is whether policies of foreign investment should be administrated by one single agency - which would thus have a multidimentional approach - or by many different agencies. Both alternatives have problems; the first one, because it would require a high degree of specialization and it should be very powerful in order to be efficient. The second one, on the other hand, could reduce the policy of foreign investment to a discrete series of bureaucratic registrations and make the achievement of more general goals impossible.

Authorization of FI. There are no criteria for restricting the flow of direct foreign investment, other than those established by Decision 24 itself and its related provisions and amendments. The general atmosphere is one of openness to foreign capital and there is clearly a willingness to be flexible or, in some cases, to refrain from applying the rules set forth in the Common Régime.

The member countries have not established a clear set of priorities for authorizing foreign investment. The social and economic impact of a project or of a foreign enterprsies is used as a point of reference or for purposes of information, but not as a standard for rejecting direct foreign investment. In this regard, there are no specific standards for restricting the setting up of foreign enterprises whose international operations show deficits, despite the fact that the goal of the Andean Pact is to substitute imports and promote exports.

Most of the member countries have exempted enterprises engaged in the exploitation of basic commodities, insurance, banking, financing, transport, tourism and mass communications media from the scope of the Common Régime. The exceptions allowed for the article 44 of Decision 24 have been made the general rule. In practice, the Régime is mainly and almost only applied to the manufacturing industry.

There is no discrimination as regards incentives to investment according to the source of the capital concerned. In all the member countries, foreign investors receive the same treatment as nationals, and when it comes to taxation and/or exchange arrangements, differences are not taken into account. National agencies have not followed common criteria for the authorization of reinvestments by foreign enterprises.

There is no uniform standard with respect to the positive application of agreements providing for the conversion of foreign enterprises; in practice,

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1/ See a special study on this subject in the Annex.

the mechanism is hardly ever used. This was considered a fundamental rule of Decision 24 but different developments - not only oposition from the TNCs - have made it almost conpletely obsolete for new investments.

Registeration of direct foreign investment. There are no major differences among member countries as regards the criteria they apply for registration of direct foreign investment. All the countries allow the registration of capital investments in foreign or national currency, capitalization of loans, valuation of tangible goods, reinvestments and capitalization of resources in general. Except in one country the competent national agencies have issued explicit regulations concerning procedures for registration of direct foreign investment. These list in detail the documentation which is required for this purpose. In general terms, all the procedures are very similar.

TNCs' operations and the national economy. The member countries have not regularly applied restrictions on the granting of medium- and long-term internal credit to foreign enterprises, and there is a tendency to eliminate the restrictions established in the Common Régime on this subject. On the other hand, all countries have specific criteria and mechanisms for regulating the arrangement by foreign corporations of external loans from financing agencies or parent companies and/or subsidiaries. However, the compliance of these regulations leave not been evaluated.

Although, historically, transfers of profits of foreign corporations they have not reached the ceiling of 20 per cent above the amount of investment registered with the competent national agencies, there is a general tendency among the member countries to have the regulation of this aspect up to national legislation.

The member countries have not been fully enforcing the criteria established in Decision 24 with regard to authorization and monitoring of the right to re-export capital.

There are no specific agreements with foreign enterprises in connexion with the purposes, objectives or programmes of global and/or sectoral policies, although some member countries have legal mechanisms for implementing such policies. There are no common mechanisms for regulating new types of contracts with foreign enterprises ("turn-key" contracts, for example). Some member countries have signed document which violate the provisions of the Common Régime with respect to the application of criteria of extraterritoriality in the settlement of possible conflicts or disputes with foreign corporations.

There are no specific criteria for monitoring the majority participation of national investors in national or mixed enterprises and ensuring that this participation is reflected in the management of production, administration, marketing and finances of these firms.

Changes in Decision 24 made by the Commission of the Cartagena Agreement. From its inception Decision 24 has undergone several changes as a result of decisions taken by the Commission of the Cartagena Agreement. The most significant changes were made in 1976, as the five other signatories tried to prevent Chile from withdrawing from the Andean Group. By Decision 97, the Government of Chile was authorized to sell stock in State enterprises belonging to CORFO to foreign investors. The most important modifications were made by means of Decisions 103, 109 and 110, as follows:

- Creation of special categories of capital: subregional capital is to be considered as national capital when certain specific requirements are met, and neutral capital, in the case of international public financing agencies or governmental agencies concerned with co-operation for economic development. This category of capital is not to be taken into account in determining the nature of the firm.

- Conversion agreements: the date on which the conversion of foreign firms was to begin was postponed from 30 June 1971 to 1 January 1974. Authorization was also given for the incorporation of new direct foreign investment to national or mixed enterprises provided the enterprise remained at least a mixed one.

- Remittance of profits: the ceiling for transfer was raised from 14 per cent to 20 per cent of registered direct foreign investment. Undistributed gains may be invested as direct foreign investment.

- Reinvestment of capital: the rate of reinvestment permitted was increased from 5 per cent to 7 per cent.

- Access to domestic credit: foreign enterprises were allowed access to long- and medium-term credit on the local financial market. The provision concerning the regulation of short-term credit by each country was eliminated.

The Board of the Cartagena Agreement has not proposed any amendments to Decision 24. In 1983 the Commission, for its part, approved a plan for the reorientation of the Andean integration process, in which eight areas were selected for priority action, with a sectoral strategy being formulated for each area. Several of these have to do with direct foreign investment and the transfer of technology, but Decision 24 is not mentioned not is its current sphere of application affected, even indirectly. In the strategy for the area of financing, investment and payments, it is proposed that efforts should be made to attract external investment "within the framework of Andean legislation" and on terms that are suited to the needs and development priorities of the member countries.

As regards the strategy on science and technology, two policies are included which are relevant to the case of direct foreign investment. On the one hand, reference is made to the need to exercise a joint bargaining capacity and, to this end, to develop evaluation and selection methodologies, including "new techniques for the analysis of technology contracts". On the other hand, reference is made to the need to update regulations regarding patent rights currently in force in the subregion.

Changes in Decision 24 adapted unilaterally by the countries. There are significant differences in the way member countries of the Andean Group conceive and apply Decision 24. Several of these differences actually entailed ad hoc amendments to Decision 24.

Conversion agreements are being applied less and less and some countries have stopped signing them and enforcing them. The countries have been more and more willing to accept the idea - even though it is contrary of Decision 24 - that these contracts are to be applied solely to those firms which wish to benefit from the expanded Andean market.

As regards national jurisdiction over disputes relating to direct foreign investment, two countries have signed agreements with OPIC which, in practice, go beyond this principle established in Article 51 of Decision 24.

The ceilings on the remittance of profits established by Article 37 have been overlooked in several countries, either as a general rule or in specific cases.

The principle of not authorizing direct foreign investment in activities for which the demand is already sufficiently covered (Article 3) has not been generally applied.

As regards the existence of sectors to which the access of direct foreign investment is restricted (Articles 40-44), there have been significant exceptions.

The least controversial areas are the registration of direct foreign investment and the transfer of technology, although there are significant differences in the way the relavent rules are applied from one country to another.

Technology. Decision 24 stipulates that all contracts on the importation of technology and on patents and brands - whether or not they involve payment - must be examined and submitted to the competent national authority for approval. This agency is responsible for evaluating the real contribution of the imported technology by estimating its potential profitability and, the price of goods which incorporate it or establishing some other specific quantification of the impact of the imported technology.

Decision 84 adds some criteria for evaluating applications for the importation of technology, including the following:

- its impact on local technological development;
- its impact on technology in employment;
- its contribution to national or subregional development plan;
- its impact on the balance of payments and on the generation of income;
- its impact on the environment.

Under Decision 24, clauses providing the following information must be included:

- identification of modalities of transfer of technology;
- contractual value of each element involved;
- determination of the period during which it shall be in force.

In addition the authorization of certain types of clauses, is forbiden including those which would entail on obligation to purchase capital goods, intermediate products, raw materials or other technologies from a given source; those which would reserve for sellers the right to fix prices; those which would restrict the volume or structure of production; those which would prohibit the use of competing technologies; those which would establish option to buy - total or partial - in favour of the supplier or the technology, which would require the buyer of technology to transfer to the suplier any inventions or improvements resulting from the use of such technology; those which would make it obligatory to pay royalties for unused patents; and those

which would prohibit or limit the export of products made with the technology concerned, except in exceptional cases, excluding those falling within the sphere of subregional trade or the export of similar products to third countries.

A transfer of technology may not be considered a capital contribution and, in an intra-firm transaction, it does not give rise to a right to receive royalties or tax deductions.

Decision 24 provides that contracts for the licensing of brands may not include any restrictive clauses which would for example, prohibit or limit the right to export or sale in certain countries of products made with the brand name; require the use of raw materials, intermediate goods and equipment supplied by the owner of the brand or its affiliates; fix sale or resale prices; require the payment of royalties for unused brands, or require the use, on a permanent basis, of personnel supplied by, or designated by, the owner of the brand.

Registration of technology contracts. Not all contracts on the importation of technology are registered. In several countries, public sector contracts are either not registered or only partially registered, despite the large number of contracts involved. The acquisition of technology incorporated in to capital goods is not systematically registered, evaluated or controlled in any country of the Andean Group. This type of transfer of technology undoubtedly accounts for the bulk of payments for technology made by these countries.

In general, it may be said that clauses which are expressly prohibited by Decision 24 have been eliminated from contracts, although there are some exceptions. As regards intra-firm payments, there are no uniform criteria in the subregion for establishing the existence of a dependency relationship between a parent company and a subsidiary. The criteria used generally refer to the holding by the parent company of stock in the subsidiary, and this varies from country to country.

There are very few cases in which technology contracts have been rejected. Several countries provide for a domestic recourse vis-à-vis the authority which is responsible for registering contracts.

Evaluation of contracts and technology. Countries which do register contracts systematically tend to focus their attention on formal aspects, while they only consider the actual purpose of the contract in vague general terms. Up to now, the emphasis of policies on technology has been more quantiative than qualitative in all the countries which do apply registration. Contracts are normally analysed in terms of their cost in foreign exchange, while their actual technological content, in connexion with which Decision 24 and 84 establish clear and explicit evaluation guidelines is not analysed in detail, often because the necessary technical means are not available.

Pyament for technology. The modalities and magnitudes of payments made abroad for technology contracts vary considerably from country to country. The practice of basing payments on a percentage of net sales, accounts for more than half of all cases in one country and almost two-thirds in other; in a third, it only represents 12 per cent. A second option is that of paying a fixed amount; this has been adopted to varying degrees in the different

countries and accounts for one-third of all cases in one country, 19 per cent in other and only 4 per cent in a third. In 1981 these payments ranged from a very low percentage of the countries' exports to 0.6 per cent. This difference may be explained by the different degrees to which the process is centralized in the various countries.

Intra-firm payments for technology imports were not interrupted with Decision 24, although they are prohibited. The publications of the United States Department of Commerce attest to this.

There are no subregional criteria concerning the range of payments allowed in connexion with the various economic sectors. In the case of one country, for example, it amounts to between 2 per cent and 3 per cent for the engineering and metal products sector and 2 per cent for the pharmaceutical sector, whereas payments usually are not authorized for the food sector.

In some cases, larger payments are authorized as a means of promoting exports. There is no technological justification for this criterion.

Monitoring. There is no evidence of regular and systematic monitoring, in any of the countries, of the performance of obligations. This is particularly true in the case of the actual transfer of the technology concerned. This does not mean that some countries do not closely follow the development of a given number of contracts each year, as in Colombia, for example. In general, no fines have been imposed for non-compliance with contracts.

Extensions of contracts show a certain tendency to reduce their duration, although there are a large number of long-term contracts.

None of the Andean Group countries have conducted long-term evaluations of the effectiveness of the Andean régime for the transfer of technology.

(b) Caricom

The Common Market Annex of the Treaty of Chaguaramas includes on article calling for a regional policy on foreign investment . According to article 44 market states "recognize the need for continuing inflows of extra-regional capital and the urgent necessity to promote development in the less developed countries" and declare that they "shall keep under review the question of ownership and control of their resources with a view to increasing the extent of national participation in their economies and working toward the adoption as far as possible of common policy on foreign investment ".

A Draft Agreement on foreign investment and the development of technology - inspired on Decision 24 of the Andean Group - was proposed for adoption at the Special Heads of Governments Conference held in St. Lucia in July 1974, but it was not accepted.

(c) Central Americal Common Market

The 1960 Treaty does not contain any reference to the treatment of FS within the CACM. In 1976, a High Level Committee submitted to the different Governments of the area a draft of the Central American Economic and local Community, which included specific regulations on foreign investment . However, this new treaty has not been approved as of today.

5. SPECIAL TREATMENT FOR LESS DEVELOPED COUNTRIES

All integration schemes in Latin America grant special treatment to the relatively less developed countries (LDCs). The rationale for this is the acknowledgement of the broad economic difference that exist among the different country members of each regional arrangement and the belief that integration should serve to reduce their disparities. If it there were no support programmes for LDCs it is very probable that these countries would not be able to offset the costs generated by trade diversion stemming from their participation in the integration process. On the other hand, external economics favor the more industrialized countries as the site for integration investment. In order to ensure their continued will to participate in the integration process they have to visualize that the distribution of costs and benefits among the members of the integrations group corresponds to their expectations. It is not easy to formulate a precise definition of what constitutes an LDC, but the socio-economic indicators most often used to compare relative development are the gross domestic product, the degree of industrialization, the degree of urbanization and life expectancy at birth.

The tools most frequently used by the integration schemes in Latin America to benefit the LDCs include the following:

(a) Trade instruments (lists of non-extensive concessions, privileged access to the markets of the more developed countries, exclusive margins of preference, and temporary exemptions from the Common External Tariff);

(b) Industrial planning (integration industries, exclusive production rights in sectoral programmes for industrial development, and industrial modernization and streamlining);

(c) Financial instruments (preferential allocation of resources through subregional and regional banks);

(d) Tax instruments (special tax incentives for industries that locate in LDCs);

(e) Preferential treatment in the agricultural sector (assignment of investment priorities and margins of preference for LDC agricultural products); and

(f) Physical infrastructure and communications planning (measures to stimulate highway and telecomunications systems).

How these instruments are employed in each scheme is discussed in more detail below.

(a) CACM

In the Central American Common Market, the principle of balanced development has been affirmed in a series of declarations and resolutions by the integration organizations and in secondary instruments of the General Treaty of 1960, although it was not specifically mentioned in the basic agreement.

In September 1966 a Protocol to the Central American Agreement on Fiscal Incentives for Industrial Development was signed, known as the Protocol on Preferential Treatment for Honduras, which went into effect in March 1969 - three months before the unfortunate rupture in diplomatic relations between Honduras and El Salvador. This Protocol is the only instrument expressly written and ratified within the CACM to benefit a reltively less developed country.

In January 1971 Honduras withdrew from the Central American Free Trade Zone, reestablishing tariff barriers for its subregional trade and unilaterally modifying the Central American Agreement on Import Duties and some of its protocols. Honduras switched from its original multilateral commitment with the reap of the Common Market countries to bilateral trade agreements with the three countries with whom it maintained deplomatic relations during the 1970's and with El Salvador after 1981. Through these bilateral agreements, Honduras is receiving, at least in part, the preferential treatment sought when it was part of the Free Trade Zone.

The Central American Bank for Economic Integration, created to facilitate financing for projects emerging from the integration process, gives relative priority to projects located in honduras, thus becoming the most successful of the above measures favouring LDCs in the Central American Common Market.

To date efforts in the CACM to benefit the LDCs have been rather limited, and the results have not been satisfactory, as SIECA has noted in its evaluation of the first decade of the integration process. According to SIECA, the Common Market "did not permit the principle of balanced development to be put fully into practice", which has contributed, among other things, to the current decline of the integration system.

(b) LAIA

The specific mechanisms established by the Treaty of Montevideo of 1980 to benefit the LDCs are the following:

(a) opening the markets of the medium and more developed countries to LDC products, preferably of an industrial nature;

(b) the negotiation of Special Co-operation programmes; and

(c) establishment of the Office for Economic Promotion within the Secretariat to encourage the full participation of the LDCs.

Furthermore,the LAIA system provides for special treatment through the regional tariff preference and the automatic extension of the concessions granted in the trade agreements on specific topics.

With regard to measures designed to increase exports of goods from the LDCs - point (a) - regional agreements were signed containing lists of products from the LDCs whose entrance to the markets of the integration group would be facilitated in compliance with Article 18 of the Treaty of Montevideo of 1980.[1/] These

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1/ This Article stipulates that market opening lists will be composed preferably of industrial products, for which total exemption from import duties and other restructions set by the other nations of the Association, will be granted without reciprocity; market opening lists, in contrast to LAFTA's earlier lists of non-extensive concessions, are irrevocable.

agreements include 212 products from Bolivia, 154 from Ecuador, and 242 from Paraguay, 70 per cent of which may be generally considered traditional industrial products (foodstuffs, te tiles, leather and wood manufactures, ceramics, and vegetable oils). These lists will be progressively broadened according to procedures and at times to be determined by the member countries.

Special Co-operation programmes - point (b) - may include:

(a) marketing, pre-feasibility, and feasibility studies for new business ventures or the expansion of existing firms;

(b) the promotion of Latin American multinational enterprises for the production and marketing of products included in the market opening lists;

(c) co-operation in technology and management; and

(d) collaboration on projects of common interest in the areas of financing, technical assistance, the acquisition of machinery and equipment, and access to third country markets.

The Office for Economic Promotion in the General Secretariat of the Association - point (c) - was created with the primary goal of providing LDCs with the necessary information and adequate technical alternatives to take advantage of the opportunities offered by the market opening lists for expanding their productive activities. Similarly, it should be noted that an evaluation of the support system for the LDCs and the adoption of measures for its more effective application are included as part of the specific functions of the Evaluation and Convergence Conference.

LAIA is still in the process of formalizing the special mechanisms in support of the LDCs envisaged by the Treaty. In fact, in 1983 regional market opening agreements were signed and went into effect. In addition, two special co-operation programmes for Bolivia were also ratified. Similarly, the Office for Economic Promotion now has a co-operation programme for Bolivia, Ecuador, and Paraguay consisting of studies emphasizing the identification fo export, industrial complementation and financing projects.

(c) CARICOM

The principle elements of this preferential treatment granted to LDCs are the following:

(a) the LDCs were granted greater flexibility in adopting the instruments for intra-regional trade liberalization - that is, more time and fewer requirements to reduce their tariffs with respect to intra-regional trade;

(b) the level of external protection applied by the relatively less developed countries was taken into account in the formulation of the Common External Tariff of the Community in order not to damage the economies of these countries when they joined the community;

(c) special regulations were adopted to protect certain industries in the LDCs;

(d) it was stipulated that the exclusionary clause could not be applied to goods from the LDCs (this clause permits the adoption of temporary restrictions on intra-regional imports when a member country is experiencing balance of payments difficulties);

(e) LDCs were granted preferential funding from the Caribbean Development Bank; and

(f) similarly, they were given special consideration in CARICOM 's sectoral programs.

In addition to receiving the above preferential treatment, the LDCs have their own institutions for mutual co-operation and co-ordination of their activities vis-à-vis the rest of the Community. The Organization of East Caribbean States (OECS), founded in 1981, is the principal organ of the relatively less developed islands of the Caribbean Community and supersedes the West Indies Associated States (WIAS). The main areas of OEAS activity are:

(a) the promotion of economic integration through the East Caribbean Common Market, in which mechanisms for intra-regional trade liberalization and the co-ordination of external tariffs have been developed;

(b) the issue of regional currency through the East Caribbean Currency Authority (ECCA), as well as the establishment of a regional central bank;

(c) the co-ordination of judicial institutions through the Supreme Court of the West Indies Associated States;

(d) the co-ordination of civil aviation through the Directorate of Civil Aviation (DCA);

(e) the establishment of joint embassies and trade offices; and

(f) co-operation in production and in the provision of joint services.

The LDCs have certainly profited from their participation in CARICOM, especially in the areas of functional co-operation, such as health, education, nutrition, meteorology, technical and cultural training, etc. Similarly, these countries have received the benefits of co-operation from the co-ordination, both commercial and diplomatic, of the foreign affairs of the CARICOM nations. Moreover, the LDCs benefit from the services of regional organizations for air and maritime transport and agricultural and industrial promotion, as well as the Caribbean Development Bank. It should be noted that during the 1970's, the LDCs received six times more resources per capita from the Caribbean Development Bank than the more developed countries.

Furthermore, the subregional institutions created by the LDCs have been somewhat successful. In addition to the joint services rendered by these institutions, the adoption of a subregional industrial programme should be mentioned, in which 31 industries have been identified, 7 of which are now in operation.

(d) Andean Group[1/]

The Cartagena Agreement stipulates the promotion of a balanced and harmonious development of its member countries. To achieve this goal the Agreement conceives a package of mechanisms designed to make possible the equitable distribution of integration's benefits in order to bring about a gradual reduction in the existing differences in development among its member countries. Thus, the Agreement contains a Special Regime for Bolivia and Ecuador to help these countries attain a faster rate of economic development.

The Special Regime provided for by the Andean countries includes the following:

(a) a set of trade regulations designed to establish temporary margins of preference favouring both countries, in order to stimulate trade with the rest of the Group;

(b) a set of preferential regulations in the industrial area, reserving to Bolivia and Ecuador the exclusive rights over goods not currently produced in other member countries, as well as more favourable treatment in the sectoral programmes for industrial development and the industrial modernization and streamlining programmes;

(c) a commitment to joing action in negotiations with the Andean Development Corporation (CAF) and other national and international organizations regarding technical assistance and financing for projects in Bolivia and Ecuador; and

(d) The granting of concessions and the consideration of special circumstances in the harmonization of policies (such as the handling of foreign capital and regulations for multinational Andean enterprises), and other areas of the integration process.

The Special Regime for the Andean LDCs has had very little effect and has not lived up to initial expectations. In the area of trade, the total abrogation of tariffs by Colombia, Peru, and Venezuela on a series of products of special interest to the LDCs and the total exemption from duties for both countries with regard to all other tariffs - except for products included in the mechanisms for industrial planning - had a positive impact on both countries' exports to the Group; nevertheless, Ecuador benefitted substantially more. In fact, in 1982 Ecuador became one of the main exporters of traditional and non-traditional products to the subregion.

Industrial planning, which had held great promise as an equalizer of cost and benefit distribution, specifically for the LDCs, had minimal effects in Ecuador and virtually none in Bolivia. A decade after the Cartagena Agreement went into effect, only two of the eleven projects assigned to Bolivia and six of the fifteen projects planned for Ecuador in the metal-working programme were in operation.

1/ This section is based on Junta de Cartagena, "Lineamientos por un plan de reorientación del proceso de integración Andina", JUN/di 743, August 1983.

With regard to special financial treatment, even though the Andean Development Corporation and the Andean Reserve Fund (FAR) channeled their resources preferentially to assist those two countries, the results were barely significant, due to the limited capital resources of both institutions.

In order to facilitate the implementation of Bolivia's sectoral programmes for industrial development, the Cartagena Agreement Commission approved a Special Assistance programme for Bolivia; this programme was to have been carried out through five major projects, but these have not yielded satisfactory results either.

The Commission in its document on a reorientation plan for the Andean integration process,[1/] points to the following as the principal causes for the limited application of the Special Regime:

(a) the inability of the productive structure of the five countries to assimilate the changes required by the integration process and put the principles of regional solidarity into practice;

(b) the fragmentary application of the mechanisms comprising the Special Regime and the delay in the application of the preferential measures;

(c) the failure of the other members of the Agreement to follow through on their commitments, which adversely affected the exclusivity of the concessions granted to Bolivia and Ecuador;

(d) the limited capacity to develop, start up, and administer projects in the two countries;

(e) the economic and financial difficulties of the subregion, aggravated by the international crises; and

(f) the limited infrastructure and transport services within the subregion, expecially in Bolivia.

After evaluating the results of the assistance programme for Bolivia and Ecuador, the Cartagena Agreement Commission proposed a new system of subregional co-operation, based on the development of specific integration profects in both countries and aimed at increasing and diversifying exports to both the subregional and third country markets. At the same time special measures to aid Bolivia, as well as other steps to guarantee compliance with commitments made by the larger countries were taken.

1/ See Cartagena Agreement Commission, "Plan de Reorientación del Proceso Andino de Integración," (Reorientation Plan for the Andean Integration Process), COMXXXV-E/dt.3/Rev.2.

6. TECHNOLOGICAL COOPERATION[1/]

The Cartagena Agreement covers technological policy for the subregion and provides for the establishment of the Andean System of Technological Information (SAIT) and the Andean programmes of Technological Development (PADT). SAIT functions as a clearing house in the subregion for the exchange of technological information whereas PADT aims at promoting assimilation and development of technology relevant to or appropriate for the subregion.

PADT has since developed a few signigicant technological programmes for the subregion. First, the Andean Project for Technological Development in Copper Hydrometallurgy was approved. This was designed to step up the transfer and adaptation of technologies for copper extraction by acid solution and by bacterian-acid process, and recuperation through ion exchange and electrode position. The project was also involved in the training of qualified personnel a well as in adapting and integrating the advanced equipment and technology from the transnational corporations for regional application. The main beneficiaries of this project are the copper-producing members, Bolivia and Peru.

Secondly, the Andean Forest Project was set up with a view to conducting research and disseminating knowledge in regard to the timber and other forest resources in the subregion. Work on testing various forest species has been carried out and new technology for timber exploitation has been developed. Specifically the Andean Laboratory of Wood Engineering was founded in Lima and the Andean System of Classification of Structural Wood was developed.

Thirdly, the Andean Project of Food Technology was approved by Decision 126 of the Agreement. The project has five programmes designed to carry out research on the production, marketing and consumption of food in the subregion with a view to developing food of high nutritional value and low cost for groups such as children and pregnant women.

Finally, a programme for promoting social and economic development of the rural environment has been set by PADT. The programme is charged with the generation and transfer of technology related to the development of a sound rural environment.

Apart from activities within the two formal organizations, SAIT and PADT, regional technological co-operation as provided by the Cartagena Agreement also includes appropriate legislations for marketing technology, patent rights and the legal aspects of technology transfer from outside the subregion.

1/ UNIDO, Regional industrial co-operation: experiences and perspectives of Asean and the Andean Pact, 1986.

7. INVESTMENT FINANCING

There are four multinational development banks in the region. The Inter American Development Bank (IDB), the Central American Bank for Economic Integration (CABEI), the Andean Development Corporation (CAF) and the Caribbean Development Bank (CDB).

CAF

The CAF has approved credit operations for US $572 millions Since 1971, when it initiated its activities, up to December 1985. It is by far the most important channel for joint subregional investment and its authorized capital has been recently increased from US $400 to US $1,000 million. During 1983 the CAF approved credits for US $121 millions corresponding to 20 operations. With regard to the project distribution by sectors, to industry corresponded something less than a third of the total. The rest of it went to energy (30 per cent), agriculture (16 per cent), transportation (14 per cent) and mining (10 per cent).

CABEI

The Constitutive Agreement of CABEI went into effect in 1961. The CABEI went through a liquidity crisis during the past years and also had political problems, as the country members would not agree on the person of the President of the Bank. In fact, at the end of the 1982-1983 period was not possible to financy the meeting of the Board of Governors. In February 1985 the Ordinary Assembly decided to create a Fund for the Economic and Development of Central America, with capital for US $250 million.

CDB

The CDB operations declined in 1985 up to the 1978 level and the total approved lending reached only US $41 millions, all of them to the public sector and 90 per cent for the development of infrastructure. The industrial sector got 18.5 per cent of that total. Additionally the CDB lent US $7.8 million for new projects in the LDCs of Caricom.

IDB[1/]

In 1983 the IDB decided to create the Inter-American Investment Corporation, thus providing the region with a complementary mechanism to supply the necessary investment for the private sector's production activities.

Since 1969 the IDB has undertaken a variety of initiatives to implement such a mechanism. At its XXII Annual Meeting, held in 1981, the IDB Board of Governors considered Venezuela's proposal to establish a Multinational Trust Fund for equity inestments, and the Board Committee was asked to study the plan and consult with member countries interested in the initiative.

Since then the Committee has met several times, because a large number of member countries demonstrated their willingness to participate in the initiative. The negotiations culminated in a meeting of interested parties held in Rome on November 3-4, 1983, during which the text of the Constitutive

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1/ INTAL, The Latin American Integration Process in 1983, 1984.

Agreement of the Inter-American Investment Corporation was signed. All IDB borrowing countries signed the document, as did the United States and Italy, among the Bank's developed member countries. The other member countries had until February 29, 1984, to sign the document if they wished to be included as founding members of the Corporation.

The purpose of the Corporation is to promote the economic development of its developing regional member countries by stimulating the establishment, expansion, and modernization of private enterprise, giving priority to small- and medium-scale operations, in a manner that will complement the activities of the Inter-American Development Bank. Also eligible for financing are enterprises whose shareholders include the government or other public entities with activities that strengthen the private sectors of the economy.

In order to do this, the Corporation will exercise the following role: to help finance the establishment, expansion, and modernization of enterprises; to stimulate investment opportunities; to provide technical co-operation; and to promote the development of Latin America's capital markets.

In addition, the Corporation will encourage participation by other sources of financing and/or technology, recurring to the most appropriate modes - among which are consortia for obtaining loans and the acquisition of stock by the Corporation in such companies, as well as joint enterprise, and other forms of association, such as licensing agreements, marketing or management contracts, and the like. The Corpoation will also attempt to cofinance local financial institutions and, in general, work together with them and other international and bilateral investment institutions.

The goals of the Corporation will be the following: project identification; direct investment in viable private enterprise; financing and strengthening of development financy entities that serve small enterprises; the creation of interest in direct investment opportunities in Latin American enterprises; the promotion of capital-market expansion; and the provision of advisory assistance on ways of encouraging a healthy climate for the expansion of private investment.

The Corporation's principal financial instruments will be long-term loans (from five to twelve years) with grace periods, equity investments in suitable enterprises, and the concession of partial or total guarantees when appropriate.

The investment activities of the Corporation will concentrate chiefly on medium-sized enterprises. The size of these firms, measured by such criteria a total assets, net worth, number of employees, and so forth, will vary from one country to another, and over time. Investment may be made in association with local, regional, and international financial institutions and may be carried out through consortium operations or other catalyzing mechanisms, as deemed appropriate. This focus on medium-sized enterprisesis what distinguishes the Corporation from other similar international financial institutions that operate in the region.

The Corporation also considers the promotion of small-scale enterprises in the developing countries as a matter of prime importance in terms of social and economic development. However, the experience of other international financial institutions and the evaluation of other forms of operation applicable to the small-scale enterprise indicate that it is not possible to

provide backing for these businesses directly or individually from Corporation headquarters. The activities of the Corporation in this respect would primarily consist of financing (debt or equity) and/or providing technical co-operation to private or semi-private financial intermediaries, funds, or programmes designed to promote small-scale enterprises. With this goal in mind, the Corporation will also attempt to co-ordinate its activities with respect to small-scale enterprises and cofinance these projects with other international, regional or subregional institutions that can commit themselves to providing assistance to such enterprises.

One ot the basic criteria for determining the possibility for investment will be a consideration of the economic impact of the eligble projects and enterprises. Project sponsors will provide a considerable part of the capital for the enterprises and, generally speaking, the Corporation's financing through equity capital, quasi-equity capital, and/or debt instruments should complement local resources and beutilized, insofar as possible, to mobilize additional funding from other sources.

The maximum financial commitment form the Corporation for a given project or enterprise will not exceed 40 per cent of the total cost, or this same percentage of the company's total stock. The total of these commitments may not exceed 10 per cent of the net capital of the Corporation in any given case. For equity investment, the Corporation's share in the total capital of a business may not exceed 33 per cent nor be less than 15 per cent.

The initial authorized capital of the Corporation will be US $200 million, distributed in 20,000 shares of US $10,000 each, underwritten by the IDB member countries that have agreed to join the institution. This capital may be increased by the Corporation's Board of Governors. Once the authorized capital has been totally paid in, the Board may also authorize the issue of callable capital. The Latin American countries, as a group, have stated their intention to underwrite 45 per cent of the capital. The other 45 per cent would be supplied by the United States, Italy, and other developed member nations of the IDB.

Other funding for this entity will be derived from bond issues, debt papers and stock certificates; dividend income, commissions, interest, and other funds derived from the Corporation's investments; loan recovery; sales of business investments; and any other contributions and funds entrusted to its administrations.

The Corporation will be a separate and distinct entity from the IDB. Therefore, its resources and operations will remain autonomous, and its basic organization will be independent. However, it is hoped that the Corporation will reach agreement with the IDB regarding the use of certain Bank facilities.

8. HARMONIZATION OF FICAL INCENTIVES FOR INVESTMENT

Within the Caricom it was agreed by 1973 a special Regime of Fiscal Incentives for Investment. Its more important instrument is the granting of additional incentives to LDCs within the area; and the same thing happened with regard to labour-intensive industries.

The results, however, have been disappointing as fiscal incentives did not prove to be enough to induce new investment.[1/] In the meanwhile another institution - the Caribbean Investment Corporation - just ceased to exist.

Since 1983 a new programme has been developed, the Caricom Enterprise Regime (CER), but it has not been put in practice. Its aim is to promote a regulated movement of capital, as well as entrepreneurial and managerial skills between the countries of the area.[2/]

1/ Laurence Mann, "Una evaluación de la Comunidad del Caribe: perpectivas y problemas en 1983", Integración Latinoamericana, July 1984.

2/ The Nassau Understanding, paragraph 40. The text may found in the Annex.

9. GOVERNMENT PROCUREMENT ON A REGIONAL BASIS

Although no systematic research has been done on the subject, state participation within Latin America imports could reach about 40 per cent of the total.[1/]

Political support for the promotion of some kind of preference for retional suppliers has been expressed in different ALADI meeting and also in the Latin American Economic Conference of Quito. The subject has been in fact included in the agenda of the ALADI .ound of negotiations.

The Secretary of ALADI is requesting the following operative elements in this regard: (a) incentives and preferences; (b) information systems; (c) supply and demand organization; (d) financial conditions; and (e) periodical evaluations.[2/]

1/ ALADI estimate.

2/ ALADI/SEC/Etudio 29, Canalitación regional de la demanda importada por el sector, August 1983.

EPILOGUE: SOME THOUGHTS ON THE PROCESS OF THE INTERNATIONALIZATION OF PRODUCTION AND THEIR IMPLICATIONS FOR UNITO'S WORK PROGRAMME

(a) Economic integration and the internationalization of production

The subject of economic integration is normally included within the analytical framework of foreign trade. Of course this is correct as far as trade plans are considered, but regional industrial co-operation, investment policies, the promotion of multinational protective enterprises - not only trade-oriented ones - and other related topics do not really belong in the analytical context of foreign trade, but of the process of the internationalization of production (IP).

The current - mistaken - consideration of the aspects of the internationalization of production within the conceptual framework of external trade has very significant theoretical and practical implications. Very often the very specificity of the phenomena is overlooked and its dynamics is not adequately grasped. This, of course, induces descriptions and policy options which are often irrelevant. On the other hand, the lack of an adequate analytical framework forbides the consideration of different ongoing processes: this is the case, for example, of foreign direct investment by private firms within the region and beyond. There is no theoretical or practical justification for the split of the same phenomenum - the internationalization of production - according to whether it takes the form of a purely private initiative or if it is made within some legal and publicly endorsed regime. Some advocates of economic integration could argue that state imported IP is, theoretically at least, more efficient. But this has nothing to do with the argument.

For some time now foreign direct investment by developing countries has been increasing and this process has evolved with little direct involvement from the Governments. This process has included firms from the NICs, but also from other, smaller countries. Part of this process is reflected in the very uncomplete statistics on intra-Latin American direct investments gathered by INTAL[1/] (see Table). According to, again, uncomplete figures there were

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1/ The same force explains that
"for several reasons, it is very difficult to determine the magnitude and relevance of these capital flows. First, DIFI statistics leave much to be desired, since in many cases there are neither official records nor contracts showing government involvement. Second, the record that do exist lack homogeneity; thus, some countries count authorized investments, while others count investments recorded or investments actually carried out, etc. While producing similar statistics, these different definitions of DIFI make comparative studies difficult. Third, estimation of DIFI involves determination of the national origin of the capital, since investments by transnational subsidiaries with capital from different countries may be classified in various ways.... (This figures) do not include unrecorded investments, which have been very important in some countries, for example, in the real estate sector in Uruguay. In general, investments made by private individuals are recorded only in countries that practice strict exchange control, which makes inter-country comparisons more difficult." (INTAL, Economic and Social (Progress in Latin America, 1984 report, 1985, p.137.

Direct foreign investment in LAIA member countries at December 31, 1982, by country of origin
(million of dollars)

Country of origin	Receiving countries												
	Argentina	Bolivia	Brazil	Colombia	Chile	Ecuador	Mexico	Praguay	peru	Uruguay	Venezuela	Total	Percentage
Argentina	...	2.9	33.0	1.4	21.2	13.2	1.3	16.2	5.0	10.0	6.6	110.8	16.9
Bolivia	2.6	...	0.1	0.3			7.7		1.7		0.1	12.5	1.9
Brazil	52.6	1.3	...	3.0	44.1	7.7	1.6	52.8	2.8		0.5	166.4	25.4
Colombia	22.0		0.2	...	12.6	21.8	12.1		1.5		1.8	72.0	10.9
Chile	2.7	0.3	1.6	0.2	...	13.9	0.4	2.1	3.0		0.2	24.4	3.7
Ecuador			0.2	20.8		...			1.9			22.9	3.5
Mexico	0;8		13.3	5.7	3.5	5.6	...		3.9		3.0	35.8	5.5
Praguay					0.2			...			0.1	0.3	0.0
peru	0.5	0.6	0.1	0.5	0.1	11.3	0.4		...		3.4	16.9	2.9
Uruguay	13.9		35.2	1.6	12.2	0.1	5.8	0.9	5.1	...	2.7	77.5	11.8
Venezuela	11.0		16.8	49.6	5.9	23.7	3.1	1.6	5.2		...	116.9	17.8
Costa Rica					0.5	0.2	0.5				0.6	2.0	0.3
El Salvador			0.2		0.3	0.1	1.2		0.1			1.7	0.3
Guatemala	0.2						0.2				0.1	0.5	0.1
Nicaragua				0.1								0.1	0.0
Total	106.3	5.1	100.7	83.2	100.6	97.6	34.3	73.6	30.2	10.0	19.1	660.7	
Percentage	16.1	0.8	15.2	12.6	15.2	14.8	5.2	11.1	4.6	1.5	2.9		100.0

Source: INTAL.

almost 600 cases of direct investment by private firms in other Latin American countries in 1982; more than 200 of them were joint ventures with local firms.[1/] It is safe to conclude that there were more than that, although the subsequent economic crisis must have reduced their actual numbers.

This field of research remains unexplored, except for INTAL's figures. The research for the last good study related to this subject was made more than a decade ago and, besides, it only deals with the joint venture kind of foreign direct investment.[2/] So far, no comprehensive study on the budget has been ever attempted. It is my conviction that the explanation of this fact is to be found in a wrong approach to the subject which has been hitherto predominant. This conceptual problems have to be cleared in order to get a sharper focus on the problem.

(b) The process of internationalization of production

In simple terms, the internationalization of the productive process is the organization by an economic agent of production across national frontiers. There are three different impulses which further this process:[3/]

(i) Private foreign direct investment. Its main agents are the transnational corporations, especially those which have their strategic decision-making centres in the developed market economies countries, but also others where central management is located in developing countries.

(ii) Public economic integration schemes for productive purposes. The systems of complementation of production existing in the Eastern European Countries are important examples of this second case. But it also includes supranational productive arrangements by the public sector or by public enterprises of different countries, like those in Latin America (see supra).

(iii) Mixed forms of internationalized production. This third impulse to the IP process stems from the economic integration efforts aiming at some kind of international specialization of the productive system.

The three kinds of IP have important differences among them. They arise mainly from the type of economic agent which is involved - public, private or a mixture of them - and from the characteristics of the economy where the matrix is situated. But all of them aim at international specialization in order to attain higher productivity levels, higher profits, or both.

1/ Bruno Raddaverro, "Posibilidas de empresas conjuntas en el ámbito ibenoamericano", Comercio Exterior, February 1985.

2/ Jaime Campos, Guillermo Ondarts and Edwardo White, Las empresas conjuntas Latinoamericanas, INTAL, 1978. Field research was ended by December 1976 (see p.XII).

3/ See Eugenio Lahera, "The transnational corporations and Latin America's international trade", Cepal Review, No.23, 1983.

Regarding private firms participation in the IP process, the starting point of the analysis is the recognition, as a main condition for this process, of the different resource endowment of each enterprise, which includes a better knowledge of production, capacity for product differentiation, underutilization of entrepreneurial and managerial capacity, and other assets - generally intangible - susceptible of generating profits.

This different endowment of some enterprises is associated with that of resources, with the economic cycles and with the features of the markets of the countries of origin. Frequently this is also associated with the size of the enterprise and its performance in oligopolistic markets.

The second condition for this type of internationalization relates to hte advantages acquired by a firm thanks to production in antoerh country, since if these advantages did not exist there would be a preference for straight forward foreign trade or the granting cf a license, as other ways of entry into foreign markets. The imperfections of the markets are of crucial importance, since they give a powerful impetus to the enterprises able to internationalize their output, thereby avoiding the disadvantages or making use of the advantages of the imperfections existing in the mechanisms of resource allocation.

These imperfections can be due to the type of market in question - barriers against entry, high cost of transactions, or difficulty in achieving economies of interdependent operation (all aspects which affect the resulting system of prices) - or to interventions by the public sector. In the latter case mention may be made of the differences between the economic policies of the different government - as regards taxation or the exchange rate, for example - or the systems of protection of ownership of technological knowledge.

There are undoubtedly other factors which condition the internationalization of production, such as government policies as a whole, both in the countries of origin of the investment, and in the host countries. Some policies have a negative impact, such as exchange control, double taxation, difficulties for profit remittance, etc. However, governments have also been concerned with the promotion of multinational firms, usually joint venture.

Governments have different reasons to promote region-wide multinational firms. One of them is to reap economies of scale. According to this argument the complete structure of average and marginal costs, even if increasing in a static sense, falls as production proceeds. The downward displacement of the cost structure is caused by technological gains, increases in productivity, and improvements in human capital, which can be achieved only through learning by doing and cannot be separated from the production process. An additional element plays an important role: the indivisiblity of plant size. Individual country markets may be large enough to ensure efficient primary import substitution, but further import substitution involving intermediate imports, consumer durables, and capital goods requires a larger market if a dynamic comparative advantage is to be attained. The reason is that, in many sectors, minimum plant sizes are a pre-requisite for the start up of production at reasonable costs, and such production in turn requires larger outlets than the individual national markets. Therefore, in their efforts to enlarge the scale of import substitution, developing countries are constrained by limited national markets that do not allow the establishment of plants of a size

conducive to subsequent improvemetns in productivity and competitive production costs. In this view, economic integration is a way of overcoming the limitations of the national market by allowing the establishment of economically efficient plants designed to produce for larger union markets.

This dynamic approach to customs unions does not mean the rejection of the classical doctrine of comparative advantage but rather its application to a protectionist context. Since a vigorous export promotion policy is not discarded, members of the union are expected to specialize in industrial activities in which they have intra-union comparative advantage because of their different resource endowments.

(c) The forms of internationalization

The internationalization of production can take place in two ways: (a) through horizontal expansion of the enterprise to produce mainly the same goods in the country receiving the investment; and (b) through vertical integration - backwards or forwards - which incorporates the plant of the host country into the global process of production. The prototype of horizontal integration corresponds to total local production, with local inputs, of a final good. The opposite pole is internationally integrated production, with inputs which are generally imported, of a product that in its turn complemetns the production on the international plane of a good marketed in different national marekts.(see figure).

There are various intermediate types, such as the internationally integrated production of final goods in various countries and the local production, with local inputs, of goods which in turn complement the international production of a final good. There are also combinations of both types of integration, both for the products of a single transnational coporation - some of which may correspond to horizontal integration and others to vertical integration - and by branches of a single transnational corporation, in the case of conglomerates which include various lines and types of products.

The modes of internationalization of production adopted will depend on various factors, such as: (a) the economic sector in which the enterprise operates; (b) the type of resource which gives its uperiority over local enterprises; (c) the government policies in the economic area which affect the allocation of resources and the international trade carried out; (d) the greater or lesser degree of specificity of its inputs; and (e) the peculiarities of the different economies in which such corporations work, both as regards the resource endowment and the characteristics of their markets.

(d) The consequences for the host economies

The growing internationalization of production has important effects, - both on the structure and dynamism of various aspects of the international economy, and on the countries - where the transnational corporations operate. Internationalization not only affects the directly productive processes at the national and international level - with all the imaginable consequences regarding resource allocation and international specialization - but also the financial and capital flows, as well as international trade.

Figure

POSSIBLE FORMS OF ORGANIZATION, PRODUCTION AND SALES OF INTERNATIONALIZED PRODUCTION

Ownership	Direction	Inputs	Supplier	Productive process
Total Majority Shared	Centralized) By rpoducts Decentralized) and/or regions	Local Imported	The same firm Another affilitate A transnational enterprise National firm Combination	Local Integrated

Degree of integration	Financing	Product	Market	Purchaser
Complete Partial Joint with the parent with other affiliate With other transnational enterprises	Local External Within the trans-national enterprise Outside the trans-national enterprise	Final good Input	Local External Combination	National Another affiliate Another transnational enterprise

The implications for the host economies will vary according to the type of internationalization practiced by the transnational corportions. The different forms and combinations of organization, production and sales they use will have special effects on the host economy and particularly on its foreign trade.

The fact that the imperfections of the market help to foster internalization means that the transationals do not automatically tend to eliminate them, since they are often a source of profit. These enterprises tend to provoke imperfections in the allocation of resources, since they frequently operate in oligopolistic markets, whose characteristics they reproduce, and they have the capacity to overcome the market mechanisms and the restrictions imposed by public regulations. Again, the exploitation of the imperfections of the market by the transnationals means that the ensuing benefits will not necessarily remain in the receiver countries unless the latter apply policies to achieve this end. In the regional or subregional integration initiatives taken by governments it can be seen that every process designed to homogenize the national economic spaces gives preferential treatment to those enterprsies which can undertake international specialization, operating from several countries simultaneously. It is another matter, of course, if the firms installed to supply the local market are interested in interationalizing their production.

Certain types of specialization promoted by the transnationals tend to be detrimental to the host countries, along with various aspects of their production, external trade, marketing and technology transfer strategies. They have also been criticized in their countries of origin for their effects on the balance of payments, employment, levels of prices, productivity and income.

With regard to justicly defined IP schemes, there are also significant problems. On the one hand, it is necessary

> "to solve the location problem, one of the sources of inequity in the distribution of costs andbenefits, and from the emphasis the Andean Group gives to protection in order to enable import substitution to be continued at a regional level. The purpose of industrial polanning is to avoid the market process and directly determine the location of new industries. The objective is to maximize the benefits, for the region as a whole, of the establishment of new industries and, at the same time, to distribute those benefits equitably. These two objectives may not be consistent since maximinzation of benefits presupposes the full exploitation of intra-regional comparative advantage, which may not satisfy regional equity considerations. In addition, industrial planning is largely biased in favour of producers and disregards the implied costs for consumers and the distribution of those costs. If those costs are unevenly distributed, pressures to stall such planning are certain to mount.
>
> The potential conflict between efficiency and distributive equity may threaten the viability of industrial planning. It may be argued that, since the purpose of industrial planning is to assure a more equitable distribution of costs and benefits from integration, the efficiency criterion should be eschewed in favour of higher intra-regional equality. Since such a policy could mean very high costs

and a waste of resources, mechanisms that allow the separation of location from ownership may be more appropriate. The new industry could be owned by multinational corporations formed by all the member countries, the distribution of dividends being linked to the level of benefits and to some agreed criteria for distributing them equitably.

Two additional difficulties related to regional industrial planning are the delegation of authority to a multinational entity and labour mobility. With the first, the difficulty is similar to that with the common external tariff. If the long-term development approaches of the member countries do not coincide, the sectoral priorities of the national development strategies may clash with those of regional industrial planning. Since acceptance of the principles underlying the regional programmes implies the submission of national planning to more global consideations, it also implies the surrender, at least in part, of the power to determine the patterns and characteristics of industrial development. The long-term implications of thse considerations make the surrender of power in this area politically impossible."[1/]

In a classical-type argument it might be pointed out that a contradiction arises between the development of the productive forces induced by the internationalization of production and the mechanisms of decision-making, appropriation and assignment of the surplus by their agents. The mere geographical expansion of this internationalization increases and gives poweer to both local and international trade. The imbalances and transfers of resources which it produces are also of great importance.

(e) Implications for UNIDO's work programme

A thorough examination of the process of internationalization of production in Latin America has never been attempted, mainly because of the traditional split of the subject between TNCs, on the one hand, and economic integration, on the other. The first - TNCs within the industrial sector has never been systematically researched for the region and the latter is usually visualized as a derivative from foreign trade. Completely lost in the analysis is the private foreign direct investment made by local firms.

There is no doubt that UNIDO is the logic agency to do the necessary research on this important subject. The project should include the following aspects:

First part. The internationalization of industrial production

1. The concept of the internationalization of production;

2. Economic integration efforts aiming at some form of international specialization of the productive system.

1/ Mario Blejer "Economic Integration: an analytical overview" in INTAL, Economic and Social Progress in Latin America 1984 Report, 1985. On this see also H. Hughes and G. Ohlim "The role of integration" in J. Cody, H. Hughes and D. Wall (eds.), Policies and industrial progress, Oxford, 1980 and Alicia Puyanz "La planificación industrial sectorial en el grupo Andino: en espuerto integrel de cooperción" in INTAL, El Pacto Andino, America Latina y la CEE en las 80s, 1984.

3. Foreign direct investment by local investors: characteristics, dynamics, preconditions and results. The special case of joint ventures;

4. Foreign direct investment by TNCs within the industrial sector in Latin America and the Caribbean.

Second part. Conclusions and policy options.

1. Simlilarities and differences among the diverse channels for the internationalization of production;

2. Differential success of private and public promotion of this process. Some explanations for it;

3. Convergency or divergence of the these channels? What governments could do, different options.

The study would require a 6-months research period, research assistance and some travel funds. The report would be written in 3 months making the total duration of the project 9 months. Probabaly the UNIDO-ECLAC Joint Division would be interested in organizing a regional seminar on the subject.

ANNEX

LAFTA/ALADI

1. Montevideo Treaty, 1980.

2. Final Report of the Acapulco Conferent, 1986.
Andean Group

3. Agreement on subregional Integration, 1970.

4. Decision 24, 1970.

5. Decision 46, 1971.

6. Decision 169, 1982.
Caricom

7. The Nassau Understanding, 1984.
Argentina-Brazil

8. Protocols of 1986.

9. Capital goods external trade data for Argentina and Brazil.

10. Industrial inputs: some cost comparison between Argentina and Brazil.

11. Capital goods in Argentina and Brazil: production, consumption and foreign trade.

12. Compensation for trade asymmetrics in Argentina.

13. Common list for protocol No.1.

Other material

14. Business Latin America: Investment Reputations in Latin America and the Caribbean, 1982, 1983 and 1986.

15. Eugenio Lahera and Fernando Sanchez, Comparative Study on the Association of Decision 24 in the Andean Group Countries: Current Situation and Prospects, ECLAC, LC/R.422, 1985.

16. IDB, Regional arrangements in Latin America and the Caribbean: an overview.