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European investment in Latin America: an overview

*Juan Alberto Fuentes K.**

The macroeconomic policies implemented during the second half of the 1980s and early 1990s to promote economic stabilization and foster changes in the region's production patterns have, in combination with the external debt renegotiation process, helped create favourable conditions for foreign investment from all sources –including Europe– in a growing number of Latin American countries. However, although the liberalization and deregulation initiatives that have accompanied these policies have opened up opportunities for foreign investment, European firms –whether already established in the region or planning to enter it– will have to make some adjustments if they are to make a genuine contribution to the enhancement of Latin America's international competitiveness. These microeconomic adjustments, which have already been accomplished in some cases but are only beginning in others, will help focus national and entrepreneurial strategies on forging a diversified position –in terms of both trade and investment– for the Latin American countries in the world economy.

The above factors constitute the backdrop for this essay, which starts out with an analysis of some important traits of foreign investment in Latin America in general. It then goes on to assess the trends observed in European investment, in particular. In so doing, the author examines the effects of macroeconomic equilibria and debt-equity swaps, European firms' contribution to exports of manufactures, the function of sectoral policies, the role of European investment in services, and its presence in privatized companies within that sector.

* The author is an Economic Affairs Officer attached to the Office of the Executive Secretary of ECLAC.

I
Adjustment and foreign investment in Latin America[1]

An examination of foreign investment as a component of total investment in each Latin American country brings to light the difficulties which these countries have in attaining satisfactory levels of investment within the framework of their structural adjustment programmes (Corbo and Rojas, 1991; Fuentes, 1991b). The familiar problem of uncertain expectations (Keynes, 1936, chapter 12; Asimakopulos, 1991, pp. 73-76) has had a major impact in this respect (Dornbusch, 1990). Against this backdrop, debt-equity swaps and privatizations may be regarded as subsidization mechanisms which help to trigger a flow of foreign investment in the face of what has been referred to as the "benevolent dictatorship of the status quo" (Dixit, 1992) –a status quo engendered by the postponement of investment decisions in situations where the level of risk (volatile yields) and discount rates are such that returns have to be above "normal" in order for investments to be undertaken at all.

In view of the investment opportunities created by the investment process itself (Scott, 1992), an increase in foreign investment may lead to an increase in total (domestic and foreign) investment. However, given the close ties which often exist among transnational corporations and between them and transnational banks, it may be supposed that foreign firms are better able to make use of swaps and privatization mechanisms, as well as of other investment opportunities, in cases where

[1] This essay could not have been completed without the valuable assistance of staff members of the Joint ECLAC/CTC Unit on Transnational Corporations. The author is especially grateful for having been given access to the information and analyses contained in research papers currently being prepared by Michael Mortimore, Alvaro Calderón and Ricardo Bielschowsky. Most of the information presented here on European investment stock and flows, in particular, has been drawn from the study being conducted by A. Calderón.

access to financing (in addition to technology) constitutes a major entry barrier.[2]

In any event, as in the case of total investment (ECLAC, 1990a, page 36), Latin America's "lost decade" was a time when it lost ground in respect of foreign investment as well. Whereas between 1980 and 1984 the region received 12% of the foreign direct investment (hereafter referred to as FDI) made by the world economy as a whole, the figure dropped to 7% between 1985 and 1987 and to 6% between 1988 and 1989 (CTC, 1991, page 4). As shown in figure 1, direct investment in the region as a whole was stagnant between 1983 and 1986 in nominal terms, which means that it declined in real terms. Portfolio investment not only diminished but actually turned into a negative flow.

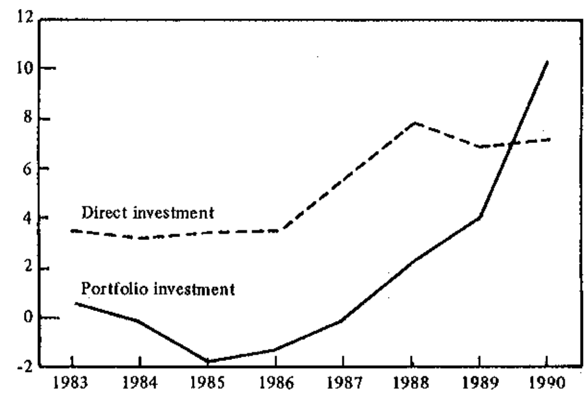
It was not until 1986 that foreign (both direct and portfolio) investment began to recover, with debt-equity swaps and the success of the stabilization and adjustment process in some countries serving as the engines for this recovery. Thus, in countries where macroeconomic imbalances were less severe during the first half of the 1980s (e.g., Brazil and Colombia), the amount of incoming direct investment during those years was greater, while in countries suffering from more severe imbalances (such as Mexico, Chile and Argentina), it was less (see figure 2, based on table 1).

During the second half of the 1980s first Chile and then Mexico managed to consolidate their stabilization processes. These countries, along with Argentina and Brazil, also engaged in a large number of debt-equity swaps while at the same time making an effort, in most cases, to liberalize the conditions pertaining to incoming foreign investment. However, whereas Chile's and Mexico's intensive use of debt swaps *triggered* a heavy inward flow of direct

Figure 1

LATIN AMERICA: FOREIGN INVESTMENT, 1983-1990

(Billions of dollars)



Source: International Monetary Fund (IMF), *Balance of Payments Statistics* (several issues), New York.

investment which –thanks to the consolidation of the stabilization process in these countries and their determined adjustment efforts– then held its own and actually increased substantially during the ensuing years, the absence of a solidly-based stabilization process in Brazil prevented the sustained growth of foreign investment.[3] In contrast, although Mexico and Chile stopped participating in debt swaps towards the close of the 1980s, foreign investment has continued to rise anyway.[4]

Argentina[5] and Venezuela,[6] on the other hand, continued to engage in swaps and started to privatize State enterprises as well, which served as another vehicle for foreign investment. Smaller countries made less use of debt-swap mechanisms, and the growth of FDI and of exports in these countries therefore depended more on the advantages which

[2] This underscores the need to give more favourable treatment to national firms and to undertake public investments that will strengthen the systemic foundations for their competitiveness in order to promote domestic investment (ECLAC, 1990a). Such treatment should be given, above all, to medium-scale and small firms through the establishment of institutional mechanisms to increase their access to financing (ECLAC, 1992a, chapter VII).

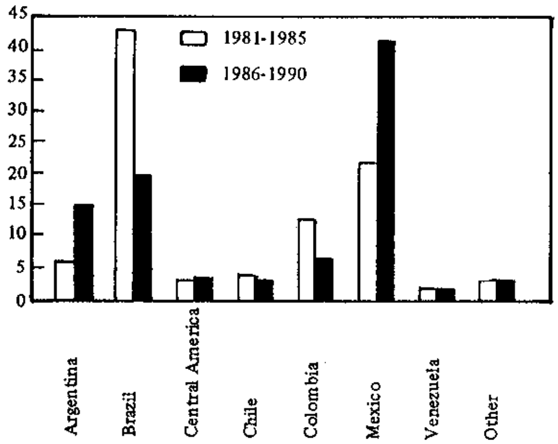
[3] In Brazil, debt swaps were carried out during the 1980s. Whereas such operations represented 27% of total FDI in 1982-1985, they accounted for 61% in 1986-1989. In Mexico this stage was shorter; most swap activity was concentrated between 1986 and 1990, and new applications were not processed after 1988. In 1987 and 1988, swaps accounted for 71% of FDI, but in 1989 and 1990, the figure was only 8% (Source: IMF, *Balance of Payments Statistics* (various issues)).

[4] This suggests that some of the swap-related foreign investment seen in these countries might have taken place even without this subsidy.

Figure 2

LATIN AMERICA: FOREIGN DIRECT INVESTMENT, 1981-1990

(Percentage of cumulative investment in each period)



Source: International Monetary Fund (IMF), *Balance of Payments Statistics* (several issues), New York.

Table 1

LATIN AMERICA:[a] FOREIGN DIRECT INVESTMENT FLOWS, 1981-1990

(Millions of dollars)

Countries	1981-1985	1986-1990
Argentina	1 239.7	4 766.0
Bolivia	97.6	58.6
Brazil[b]	8 720.1	6 255.0[b]
Colombia	2 716.5	2 273.0[c]
Costa Rica	260.3	475.8
Chile[c]	881.4	1 154.0
Ecuador	238.0	387.0
El Salvador[d]	47.9	73.8[d]
Guatemala[d]	299.1	624.9[d]
Honduras[d]	77.7	153.0[d]
Mexico	4 518.2	13 033.0
Dominican Republic	209.0	487.9
Panama	144.7	-59.4
Paraguay	63.9	106.1
Peru	80.5	173.0
Venezuela	515.3	790.0
Total	**20 109.9**	**30 751.7**[d]

Source: International Monetary Fund (IMF), *Balance of Payments Statistics* (several issues), New York.

[a] Uruguay is not included owing to lack of data for a number of the relevant years.

[b] The figure shown for the period 1986-1990 includes only an estimate of FDI for 1990.

[c] Does not include debt-equity swaps valued at US$3.161 billion during the period 1985-1989.

[d] Does not include data for 1990; the figures for these three countries and the total for the period 1986-1990 are therefore underestimates.

normally attract foreign investment to any given country, such as the supply of natural resources, inexpensive manpower, and preferential access to the United States market (Buitelaar and Fuentes, 1991), although it was usually contingent upon the prior implementation of a stabilization programme.

The significant increase in net capital inflows (to around US$36 billion) observed in 1991 (ECLAC, 1991b) probably marked the end of the downward trend in Latin America's share of the world's total foreign investment. There are a number of reasons for this, including short-term or cyclical factors, such as portfolio investment's response to the prevailing interest rate spreads and the attractiveness of the undervalued shares being traded on Latin American stock exchanges. Above and beyond these cyclical reasons, however, it is feared that, in the absence of economic stabilization, countries have found it necessary to provide large subsidies via debt swaps or low-priced privatizations in order to attract foreign investment that they would otherwise not receive.

There are other factors, however, unrelated to subsidies or short-term considerations, such as well-established stabilization processes, external debt renegotiations and the institution of a clearly-defined development strategy, that undoubtedly help to foster more lasting expectations of a sort that will encourage economic agents to invest in the region. The resumption of growth and of a net positive flow of resources, in particular, could well have a decisive influence on European direct investment in the region (Pio, 1990).

[5] In 1986 the mechanism set up by the Central Bank in its Directive A-532 of September 1984, which paved the way for an exchange subsidy and covered US$219.5 million of FDI during that year, probably had a major impact in this regard. In 1988 and 1989, a decisive factor seems to have been the mechanism set in motion by Directive A-1109 of 27 October 1987 (a discount on the public external debt along with a commitment to contribute 30% in the form of own resources) covering US$1.039 billion in direct investment, at least one fourth of which was domestic investment. In addition, directive A-1194 of May 1988 (for Central Bank loans and rediscounts) permitted the conversion of US$488 million of debt, at an average discount of 66%, into direct investment, and another US$40 million in FDI was generated through the programme established by Directive A-1056 of July 1987, which was implemented during the second half of 1988. (Source: Joint ECLAC/CTC Unit on Transnational Corporations.)

[6] Swaps accounted for 86% of inward FDI in 1989; in 1990, the figure was 67%. (Source: Central Bank of Venezuela.)

II

European direct investment and how the crisis has influenced it[7]

In view of the gradual emergence and increasing importance of a triad composed of the United States, Western Europe (or the European Community) and Japan –which was the source of around 80% of the world's total stock of FDI in the late 1980s– it is worth undertaking a fairly detailed analysis of the geographic origins of these capital flows (CTC, 1991). In 1990, Europe provided 10% less direct investment in Latin America than the United States did, but six times as much as Japan, and the situation had been much the same throughout the preceding decade (see table 2).

During the 1980s Germany generally maintained its position as the largest European source of investment in Latin America, accounting for about a quarter of total European investment in the region (see figure 3). While the smaller countries and those with a shorter history of foreign investment –particularly Switzerland and, to a lesser extent, Sweden– adopted what might be described as a more "reserved" attitude towards crisis-shaken Latin America (see table 3 and figure 3), both the United Kingdom and France increased their share of total European investment. A major reason for this, in both cases, was these countries' intensive use of mechanisms for converting external debt paper into direct investments. These swap mechanisms enabled them to transform a high-risk asset whose returns were uncertain into a lower-risk, higher-yield asset (Ffrench-Davis, 1989).

As a result of the above factors, during the latter half of the 1980s the level of European direct investment came to depend upon the extent of European banks' exposure in the region and reflected the availability of debt paper in the countries where European firms were located. Thus, the United Kingdom, whose creditor banks were most heavily involved in Chile and Mexico, became the largest European investor in these countries during the period in question (see table 4).

[7] The figures cited in this section should be regarded as no more than very rough estimates, since they are based on country sources which use differing definitions of FDI.

Table 2

LATIN AMERICA: BREAKDOWN OF FDI STOCK, BY GEOGRAPHIC ORIGIN, 1980-1990 [a]

(Percentages)

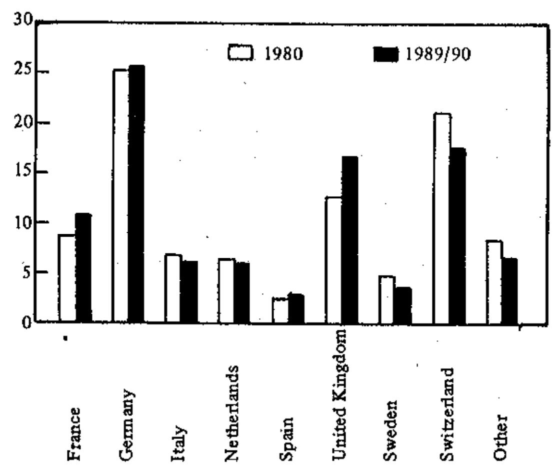
Origin	1980	1985	1989/1990
Western Europe	38.7	35.5	636.4
United States	43.5	46.1	45.9
Japan	6.3	6.4	6.0
Other	11.5	12.0	11.7
Total	**100.0**	**100.0**	**100.0**

Source: Joint ECLAC/CTC Unit on Transnational Corporations.
[a] The data shown are estimates based on information for Argentina (figures for 1989 are used in the place of data for 1990), Bolivia, Brazil, Colombia, Chile (1979 figures take the place of 1980 data), El Salvador, Guatemala (does not include 1990), Honduras (does not include 1980 or 1985), Mexico (1989 is used instead of 1990), Paraguay (does not include 1980), Peru, Dominican Republic (does not include 1980 or 1985) and Venezuela.

Figure 3

LATIN AMERICA: EUROPEAN DIRECT INVESTMENT, BY SOURCE, 1980 AND 1989/1990

(As percentages of stock of European FDI)



Source: Joint ECLAC/CTC Unit on Transnational Corporations.

Table 3

LATIN AMERICA: EUROPEAN INVESTMENT, BY SOURCE, 1980 AND 1989/1990

(Percentages)

Countries	Germany	Italy	Switzerland	France	United Kingdom	Other[a]
Argentina						
1980	12.4	16.6	16.6	13.2	10.3	30.9
1989	14.6	17.6	17.3	14.5	8.7	27.3
Bolivia						
1980	48.1	2.9	1.5	28.2	2.2	17.1
1990	50.9	2.2	5.0	19.6	1.9	20.4
Brazil						
1980	29.6	5.8	21.4	8.5	13.5	21.2
1990	30.4	7.1	17.5	10.5	14.7	19.8
Colombia						
1980	11.8	1.5	38.0	10.4	14.2	24.1
1990	11.6	0.5	28.9	8.7	22.0	28.3
Chile						
1980	7.9	6.4	22.5	10.9	28.9	23.4
1990	5.1	0.6	6.2	9.6	29.1	49.4
Mexico						
1980	34.6	1.3	24.2	5.2	13.0	-
1989	24.7	0.7	17.7	11.3	26.6	-
Peru						
1980	6.6	3.4	30.5	9.8	15.3	41.0
1990	8.5	7.0	30.5	6.4	14.8	32.8
Venezuela						
1980	2.5	3.5	32.4	9.0	21.3	31.3
1990	7.2	7.9	23.5	14.2	20.7	26.5

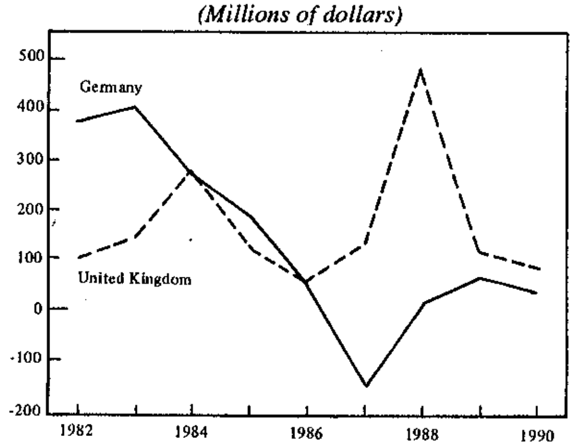
Source: Estimates based on information derived from national statistics by the Joint ECLAC/CTC Unit on Transnational Corporations.
[a] Includes the rest of the European countries (Netherlands, Sweden, Spain, Finland, etc.).

Brazil provides an especially good example of this phenomenon during the second half of the 1980s. France was the chief European user of swap mechanisms in Brazil because that was the country in which its banks' exposure was the greatest. The second heaviest user was the United Kingdom –Brazil's main European creditor. The fact that Germany, on the other hand, made only limited use of such mechanisms –despite its position as the largest European investor in Brazil and in the region– was in keeping with its banks' more limited exposure in Latin America. It is true that German law imposed some restrictions in this regard, but there also seems to have been less pressure to change those laws than there was in other creditor countries (CTC, 1992a). Figure 4 shows how the trend of British investment in Brazil, which was largely based on the use of swap mechanisms, compares with that of Germany, whose dependence upon these mechanisms was much less pronounced.

Figure 4

BRAZIL: EUROPEAN DIRECT INVESTMENT, 1982-1990[a]

(Millions of dollars)



Source: Joint ECLAC/CTC Unit on Transnational Corporations.
[a] Annual flows.

Table 4

LATIN AMERICA (FOUR COUNTRIES): SHARE OF EUROPEAN FDI IN TOTAL DEBT-FDI SWAPS

(Cumulative data for 1985-1989 and percentages)

Source	Argentina		Brazil		Chile		Mexico	
	%		%		%		%	
Europe	44		40		34		32	
United Kingdom	2	(16)	6	(17)	14	(15)	14	(17)
Germany	2	(7)	2	(7)	1	(3)	6	(2)
France	5	(6)	11	(12)	4	(0)	3	(6)
Spain	7		1		7		3	
Switzerland	8	(4)	6	(3)	5	(2)	2	(2)
Italy	11	(4)	2	(1)	2	(1)	0	(2)
Benelux	6		4		0		2	
Other	3		8		1		2	
Rest of world	56		60		66		68	
Total	**100**	**(100)**	**100**	**(100)**	**100**	**(100)**	**100**	**(100)**

Source: Estimates based on figures supplied by the Joint ECLAC/CTC Unit on Transnational Corporations.

Note: The bracketed figures refer to the percentage of each Latin American country's total commercial bank debt with the banks of each European country. The data (for 1987) correspond to commercial bank debt in the United Kingdom, Germany and France, and to Swiss and Italian commercial banks. (Source: *World Debt Tables 1989-90*, vol. 2, Washington, D.C., 1989; and World Bank, *Financial Flows to Developing Countries. Current Developments*, Quarterly Review, Washington, D.C., December 1991.)

In line with various European countries' pre-existing patterns of direct investment, European FDI was more heavily concentrated in the manufacturing sector than was FDI from other regions during the period in question (1980-1991). In fact, a negative correlation has been observed between German investment in developing countries and its natural-resource imports (Juhl, 1979). Furthermore, the United Kingdom's oldest investments in Latin America tend to be concentrated in public services and to be associated with a subsequent disinvestment, although in some countries (including Brazil), it has retained its interest in the British-Netherlands oil company, Shell (Abreu, 1988). Even Swedish firms, which hail from a heavily natural resource-based manufacturing sector, have invested in Latin American electronics, metal products and machinery, and chemicals rather than in its mining sector (Blomström, Giorgi, Tansini and Zejan, 1987; García, 1989).

Thus, during the 1980s European direct investment's share of total investment, when measured on a *country-by-country basis*, either held steady (Argentina and Brazil) or increased (Mexico and Venezuela) in those countries where the lion's share of FDI had been concentrated in the manufacturing sector in the past (see tables 5 and 9). In countries where there was a larger and growing percentage of total FDI in the mining sector (e.g., Chile, Colombia and Bolivia), European direct investment was concentrated in the secondary sector and –increasingly– in the services sector; [8] it did not, however, attain the same degree of dynamism as displayed by the rest of FDI in these countries' primary sectors, and therefore lost ground in these cases. This is why European direct investment continues to be concentrated in the countries that have the largest manufacturing sectors.

[8] It is significant that the percentage of total European direct investment in the primary sectors of Chile and Peru (about 10% in both countries at the start of the 1990s) is much smaller than the percentage of total foreign direct investment in this sector (35% in Peru and 51% in Chile). (Source: Joint ECLAC/CTC Unit on Transnational Corporations.)

The distribution of European direct investment among the countries of the region has also changed according to the speed of each country's growth, thereby corroborating the positive correlation between growth and European investment or, in other words, the latter's procyclical character. While Brazil remained the main destination for European direct investment, receiving over half the total stock of FDI, Mexico nudged Argentina out of second place as Argentina's share shrank from 20% in 1980 to around 10% in 1989-1990 while Mexico's climbed from about 14% to nearly 23%. Venezuela and Chile also increased their shares of inward European direct investment, although not as dramatically (see figure 5).

In keeping with Europe's tendency to channel its FDI towards the more industrially developed countries rather than towards countries that rely more heavily on the extraction of their natural resources (note, in table 5, the steep drop in the percentage of Chile's total FDI corresponding to European direct investment), only a very slight decline was observed in the percentage of European direct investment in Argentina, Brazil and Mexico (the three most highly industrialized countries in the region), which were receiving around 90% of the total stock of European direct investment by the close of the 1980s.[9] The fact that this percentage has remained more or less constant can also be taken as an indication that there have been no major changes in European investment in the region, which, once established, has favoured the maintenance or modernization of existing plants over the implementation of new projects. Some studies on FDI in general appear to show that investment in the manufacturing sector –especially when directed towards a large market– tends to generate inertial forces that perpetuate the established pattern (Langhammer, 1991). Thus, just as the presence of risk may lead to the postponement of investment decisions (entry), in this case it would seem that the prospect of future returns on an existing investment discourages disinvestment (exit) even when there is a possibility of present losses (Dixit, 1992).

[9] Although investment from other countries also continued to exhibit this type of concentration, it changed more than European investment did. The concentration of direct investment from the United States in these same three countries was reduced by six percentage points (from 81% to 75%) and the concentration of Japanese investment was five points lower (dropping from 97% to 92%). (Source: Joint ECLAC/CTC Unit on Transnational Corporations.)

Table 5

SHARE OF EUROPEAN FDI IN TOTAL STOCK OF FDI IN EACH COUNTRY

(Percentages)

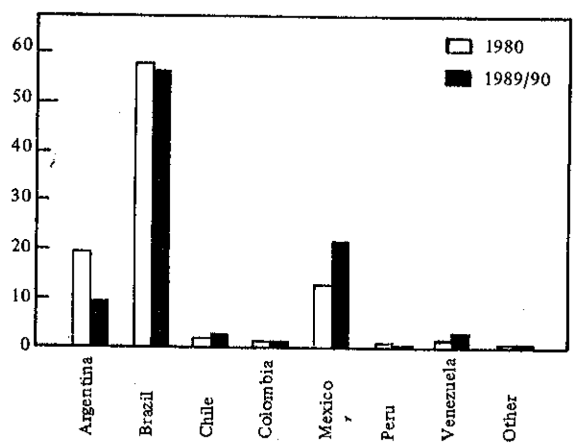
Countries[a]	1980	1985	1989/90
Argentina	52.8	48.9	48.0
Bolivia	13.7	11.6	10.3
Brazil	47.3	42.9	49.6
Chile	40.6	32.1	17.8
Colombia	23.7	21.6	17.1
El Salvador	14.2	17.8	17.5
Mexico	23.1	23.8	26.3
Peru	22.0	23.0	22.5
Venezuela	17.4	24.3	28.5

Source: Joint ECLAC/CTC Unit on Transnational Corporations.
[a] See footnote a of table 2.

Figure 5

LATIN AMERICA: TOTAL EUROPEAN DIRECT INVESTMENT, 1980 AND 1989/1990

(Percentage breakdown of stock)



Source: Joint ECLAC/CTC Unit on Transnational Corporations.

The relative lack of growth in European direct investment in the region, as well as its increase in the United States and within the European Community itself, was also reflected in a steady decrease in the percentage of the total stock of such investment that was directed to Latin America during the period starting in the second half of the 1970s and ending at the close of the 1980s (see table 6). This points up a relative decline in the Latin American economies' importance to Europe, in contrast to their growing importance for the United States, and suggests that this situation could foreshadow a process of inter-American integration involving an expansion of United States investment and a decrease in European investment. Europe's trade profile has also weakened, with Latin America's percentage of the European Community's total trade dropping from 6.7% in 1980 to 5.7% in 1990 (ECLAC, 1992b).

Table 6

LATIN AMERICA: SHARE OF TOTAL FDI FROM EUROPE AND UNITED STATES, 1974-1989

(Percentages)

Source	1974-1979	1980-1985	1986-1989
European Community	9.4	5.2	2.2
Germany	13.8	7.5	4.0
Spain	50.8	30.0	13.5
France	14.0	7.5	2.1
Italy	7.7	9.9	6.8
Netherlands	8.5	4.1	2.1
United Kingdom	5.6	2.7	0.8
United States	11.6	19.6	10.2

Source: Ministry of Economic Affairs and Finance of Spain and Spanish Agency for International Cooperation (AECI), *El vínculo Iberoamérica-Comunidad Europea. Planes, políticas y estrategias de desarrollo*, Madrid, March 1992 (table 6, p. 14).

III

The adjustment of European investment in Latin America

1. *Global factors*

Just as in the case of exports, FDI, too, can be expected to exhibit a certain degree of specificity based on each source-country's competitive strengths (Porter, 1990). Aside from the specific types of characteristics attributable to differences in the quality and availability of natural, human and financial resources, there is some evidence to suggest that three "models" of entrepreneurial development are emerging (one for each of the three members of the investment triad mentioned earlier) which may be influencing corporate processes of adjustment and innovation in each of the corresponding countries or regions (Ostry, 1990). According to this view, when the European model, in particular, found that competition from the United States and, especially, Japan was threatening it with possible stagnation and recession at the start of the 1980s, its response took the form of an aggressive technological policy and the 1992 Single European Market (Ostry, 1990, pp. 70-72). The climate created by this uncertain transition in Europe and the crisis in Latin America affected the performance of European firms having investments in the region during the 1980s. The following analysis of the position of the main goods-producing European companies in Latin America will use these firms' export performance as an indicator of their degree of adjustment and of their contribution to Latin America's efforts to carve out a place for itself within the world economy.[10]

This analysis is based on information concerning the 500 largest firms in terms of sales and the region's 100 largest exporters, and has been supplemented with data on major Argentine, Brazilian and Mexican companies (*América Economía*, 1990a and 1991b). This information provides further evidence of the oligopolistic nature of European investment in the region, its concentration in Brazil, and

[10] A more exhaustive analysis –which would go beyond the bounds of this article– would call for an assessment of their contribution in terms of scarce inputs such as technology, management expertise, marketing know-how and capital, as well as their costs (Helleiner, 1989). Within this framework, such firms' export performance would serve as a rough indicator –within certain limits– of their contribution to any increase in the competitiveness of each host country.

Germany's position as the leading European source country. In 1989, more than half (34) of the 60 European firms with the largest sales were concentrated in Brazil, and a significant number of them (18) were to be found in Argentina, whereas only five were located in Mexico and just three were in Chile. Moreover, one-third (21) of these companies were German, 10 were from the United Kingdom, 8 from Italy, 5 from Switzerland, 5 from France, 4 from Sweden and the remainder from Spain, Finland and the Netherlands (*América Economía*, 1990a).

However, although 16 of the 100 national and foreign firms with the largest *sales* in Latin America in 1989 were European affiliates and these firms accounted for nearly 14% of the total value of this group's sales, in 1990 there were only seven European affiliates among the 100 largest *exporters* and those seven accounted for less than 4% of the group's total exports in terms of value (see table 7). In contrast, 22 of the 100 largest exporters were United States subsidiaries, and these companies contributed over 12.5% of the total value of the group's exports (*América Economía*, 1991b).

There are three possible reasons for the European firms' poorer showing in terms of exports. First of all, as became clear when the information on FDI was analysed at a more aggregated level, Europe's lack of a competitive edge in natural resources and staple foods has been reflected in the limited nature of its foreign investment in these sectors, which have traditionally been export-oriented. Of the 60 main affiliates founded by European transnationals in the region, in 1989 only one was engaged in mining and two in drilling for oil (see table 8), while the producers of processed foods (including Nestlé) and tobacco were primarily oriented towards supplying the local market.

The European companies' more limited involvement in natural resource-based activities may also be reducing their chances of forming strategic alliances with large Latin American export and foreign investment firms, most of which tend to be based in the mining and petroleum industries. Nevertheless, the presence of at least some room for cooperation is demonstrated by the fact that CEMEX (Cementos Mexicanos) and CODELCO (Corporación Nacional del Cobre de Chile) have investments in Europe and by the existence of what could be regarded as a strategic alliance between Petróleos de Venezuela S.A. (PDVSA) and British Petroleum in connection with the development and marketing of fluidized coal (*América Economía*, 1990b and 1991a).

The second possible reason for European firms' poorer export performance is that Mexico, where the scale and percentage of United States investment is greater, made more rapid progress in terms of stabilization, trade liberalization and export growth during the period 1988-1991 than did countries such as Argentina and Brazil, where there are relatively more European companies. Given the geographic make-up of FDI in Mexico, more United States than European firms would have been both stimulated and pressured into competing and boosting their exports.

Specifically, the trade liberalization programme launched in Mexico during the second half of the 1980s was accompanied by a drive to liberalize the terms and conditions pertaining to incoming FDI. FDI in the *maquila*, or in-bond assembly, industry had been encouraged since 1973; in fact, at first this was the only sector in which 100% foreign ownership was permitted. Then, in 1985, the authorities began to take a more flexible attitude towards the application of laws relating to FDI in general, and in the following years investment was given a particularly strong stimulus in the form of debt-equity swaps. In 1989 and 1990 authorization for 100% foreign ownership was broadened to include a wide range of sectors within the Mexican economy. Similar steps were taken in other countries as well, such as Argentina and Venezuela, which, along with Chile, were the first countries to eliminate major restrictions on the repatriation of profits and capital.

A third possible reason for the export performance of European companies is that they have generally been slower than other transnational corporations to set up in-bond assembly activities in other countries or to incorporate new technologies as a means of adapting to today's more competitive world –a world in which Japanese and South-East Asian corporations increasingly hold sway (Mortimore, 1992). Latin America's remoteness, the ready supply of cheap labour to be found in North Africa and large-scale immigration probably account for the absence of European *maquila* operations in the region. This situation stands out in sharp contrast to the active involvement of United States and Japanese firms in northern Mexico and to the Republic of Korea's recent concentration of investments in the *maquila* industry in Central America, particularly

Table 7

LATIN AMERICA: SALES AND EXPORTS OF THE LARGEST UNITED STATES AND EUROPEAN FIRMS LOCATED IN THE REGION [a]

(Percentage share in sales and exports of 100 largest companies)

Major companies	1989		1990	
	Number of firms (%)	Sales	Number of firms (%)	Exports
European firms	16	14	7	4
United States firms	11	11	22	13

Source: "Ranking 500," *América Economía,* Nº 44, Santiago, Chile, October 1990; "Ranking 100 exportadores". *América Economía,* Nº 54, Santiago, Chile, September 1991.

[a] Includes only those companies that were among the top 500 firms in terms of sales in 1989. The weighting of companies in each country may vary due to exchange rate variations.

Table 8

LATIN AMERICA: SECTORAL DISTRIBUTION OF AFFILIATES OF LARGEST COMPANIES WITH EUROPEAN CAPITAL, 1989

Sector	Germany	Italy	United Kingdom	France	Nether-lands	Switzer-land	Sweden	Spain	Finland	Total
Mining									1	1
Tobacco and food			2	1		3				6
Textiles			1							1
Construction		2								2
Petroleum			2							2
Chemicals	8	1	4	1		2				16
Iron and steel	1	2								3
Heavy equipment	3					1				4
Motor vehicles	6	2		2			2		1	13
Tyres	1		1							2
Electronics	2	1			2		2			7
Telecommunications								1	1	2
Airlines						1				1
Total	**21**	**8**	**10**	**4**	**2**	**7**	**4**	**1**	**3**	**60**

Source: Calculated on the basis of "Ranking 500", *América Economía,* Nº 44, Santiago, Chile, October 1990.

Guatemala (Choi, 1992). As for the idea that European companies are slower to incorporate new technologies, if this is true, then in view of each European country's differing comparative advantages, the impact of this characteristic can be expected to vary from one sector to another. For example, a technological lag would tend to be more noticeable in the automobile and computer industries than in the chemical industry.

In short, the combined effect of lower European investment in natural resources; certain Latin American countries' more rapid progress in terms of stabilization, liberalization and export promotion; and, possibly, slower technological rationalization and adjustment on the part of European firms has been reflected in a smaller percentage of large companies (in terms of sales) which have at the same time figured among the largest exporters, in the cases of Brazil

and Argentina, and, inversely, a larger percentage of firms among the major exporters in countries such as Mexico, Colombia and Chile. Thus, whereas only seven of the 500 largest corporations of Latin America (in terms of sales) in 1989 were in Mexico, this country had 13 of the region's 100 largest exporters in 1990. The corresponding figures for Colombia are 2 and 8, respectively, and for Chile, 2 and 5. And of Mexico's 13 major exporters, only two were European (Volkswagen and Renault), while Colombia and Chile had only one each (Shell and Río Tinto Zinc) (*América Economía*, 1991b and 1990a).

2. *The impact of sectoral policies*

The sectoral policies adopted by some Latin American countries in the 1980s illustrate the interrelationship which, as the region's integration into the world economy increases, arises between the behaviour of foreign investment and various policy tools, including foreign-exchange requirements, public-sector hiring, restrictions on the percentage of foreign ownership, rules of origin and regulations concerning promotion activities. These policies have been of particular importance in the chief sectoral destinations of European direct investment, such as the automobile, chemical and electronics industries.

Brazil's automobile industry was the first to begin to export on a significant scale, thanks at least in part to a government incentive programme (Fritsch and Franco, 1991, p. 115), but its export growth flattened out in 1990 and 1991, precisely at the time that just the opposite was occurring in Mexico. Ever since 1983 the Mexican Government had been pursuing a programme designed to strengthen the automobile industry by ensuring its self-sufficiency in terms of foreign exchange and reducing the number of models produced (Peres, 1990, pp. 116-117). This reinforced an ongoing process of investment in and rationalization of existing factories in Mexico; at the same time, new plants were being built which, at first, were run by United States subsidiaries (Chrysler, Ford and General Motors). These enterprises benefited from their special ties to the United States market and, in particular, from the potential for intra-firm trade, while European (Volkswagen and Renault) and Japanese (Nissan) corporations lagged somewhat behind or encountered other difficulties.

By 1987, the Mexican subsidiaries of Chrysler, Ford and General Motors were already exporting between 44% and 61% of the motor vehicles they produced, whereas Nissan was exporting only 18.7% and Volkswagen only 0.1% (Peres, 1990, pp. 5-6). Consequently, the sector's promotion policy tended to favour investment from the United States, which was in a better position to meet the challenges facing it. It is likely that the trade liberalization policy, which was made more comprehensive in 1987-1988, had a similar effect. The European firms' rationalization process did make headway, however, as was evidenced later on by the increased exports of Volkswagen, which became one of the region's 20 largest exporters and was selling 34.3% of its output to buyers outside Mexico by 1990 (*Expansión*, 1991a). Meanwhile Renault, which had given up producing automobiles in Mexico in 1986, concentrated on exporting 100% of the motor vehicle parts it produced there.

Thus, European firms had to adapt to a set of rapidly changing circumstances which included heavy investment by their main competitors, macroeconomic stabilization and trade liberalization policies, and sectoral requirements. This suggests that the trends observed in the automobile industry in Mexico are probably a reflection of a process of integration with the United States; it is also quite possible that United States investment may have played a predominant role in promoting that integration process (CTC, 1992b, p. 42).

In Brazil, on the other hand, European subsidiaries were the automobile industry's top-ranked exporters in the mid-1980s. Nevertheless, United States firms do seem to have made some inroads during the decade, since they expanded their share of the major companies' exports from 25.6% in 1980 to 34% ten years later.[11] However, this all took place in the presence of severe macroeconomic imbalances (including an overvalued currency) which prompted a steep drop in exports of both trucks and automobiles despite their guaranteed access to some external markets. For example, notwithstanding their preferential access to a captive market (Italy), the Fiats produced in Brazil in 1990-1991 were less competitive and the firm's ability to export those vehicles was therefore reduced. In this case, it is clear that, despite pre-existing investments, the absence of a stable economy ultimately cancelled out any stimulus which a sectoral policy could have generated.

[11] The corporations taken into consideration here are the United States Big Three and Volkswagen, Fiat, Mercedes-Benz, Scania and Volvo. (Calculated on the basis of data supplied by the Joint ECLAC/CTC Unit on Transnational Corporations.)

Macroeconomic disequilibria and differing long-term perspectives have also hindered the utilization of sectoral complementarity agreements between Argentina and Brazil. The significant level of direct investment from European sources in both countries –about half of the total stock of FDI in each case– could pave the way for both policy-led and investment-led economic integration (CTC, 1992b, pp. 35-36). In particular, Volkswagen's and Ford's joint venture in AUTOLATINA and the subregional perspective adopted by Nestlé (CTC, 1992b, p. 26) could serve as examples of convergent sectoral policies (in this case, involving the automobile and agribusiness sectors) and of investment-led integration, provided that trade and investment flows between the two countries are truly liberalized. In addition to the existing macroeconomic imbalances, differences among the governments of MERCOSUR member countries with regard to regulations on and protection from competition from non-members (especially in relation to the automobile industry) have hampered efforts to arrive at common solutions (Worcel, 1992).

The chemical and electronics industries, for their part, illustrate the effects of policies that place varying degrees of restrictions on FDI access. In 1989, European enterprises played a leading role among the major corporations in the chemicals and petrochemicals sectors, particularly in Brazil and Argentina, but not in Mexico, where FDI –especially in petrochemicals– was restricted for strategic reasons. Even so, there were a considerable number of Mexican firms among the country's main exporters, and they had a high export coefficient (an unweighted average of 50.4%) (*Expansión*, 1991a). Unlike the computer industry in Brazil, the technology required by the petrochemicals sector was neither overly complex nor captive, and firms' competitive positions depended primarily on the supply of one natural resource: petroleum.

In Brazil's electronics industry, European corporations turned in a better export performance than United States or Japanese firms did, even though the latter lead the field at the international level (Cantwell and Dunning, 1991). This is probably due to the fact that most of the European electronics firms were in the telecommunications subsector (Ericsson, Siemens and Pirelli), where, by mounting joint ventures which increased their percentage of Brazilian capital enough to meet the Brazilian Government's standards regarding national ownership, they were able to win large contracts from TELEBRAS (Fritsch and Franco, 1991, p. 93). These contracts enabled them to generate economies of scale and, thus, to export.[12] Faced with a partial restriction on FDI, European corporations were rewarded for their flexibility with attractive public-sector contracts. In the computer industry, on the other hand, strict requirements which staked out the entire domestic market for wholly Brazilian-owned firms limited the operational possibilities of such corporations as IBM while, at the same time, exacting technological requirements and protectionist policies limited Brazilian companies' export opportunities.

Mexico's electronics industry illustrates the potential importance of assembly (*maquila*) activities, where the prospects for greater integration and for endogenous technological development are uncertain when foreign firms holding an absolute technological advantage team up with weak national companies (Cantwell and Dunning, 1991). In this case, European corporations have lagged somewhat behind in terms of both their exports and their progress in making a maquila-based adjustment, whereas the three United States corporations have had a noticeably higher exports/sales coefficient (between 65.9% and 31.5%), as well as figuring among the 500 largest companies of Latin America and among Mexico's principal exporters. In contrast, the only European corporation that has been ranked in both of these groups has had a much lower coefficient (4.5%). Furthermore, three Japanese exporters of television sets and other home electronics were also among Mexico's five largest *maquiladoras* in 1990 (*Expansión*, 1991c).

3. *New sectoral policy directions*

As the process of deregulating and promoting foreign investment that was begun in Latin America in the latter part of the 1980s has proceeded, the traditional sorts of policies for regulating this type of investment at the sectoral level have begun to decline in significance. Two trends relating to European investment in the region are to be observed, however, that could take on increasing importance in respect of sectoral policy: the application of standards that discriminate against capital from specified geographical sources –as, in fact, rules of origin may well do– and sectoral FDI promotion.

[12] The Philips corporation, for its part, was involved in the production of home electronics and had greater flexibility and access to imported inputs through its operations in the Manaus customs-free zone.

In spite of the possibility of having to make a difficult choice between exportation and national integration (Peres, 1990, chapter 3), in the case of Mexico's participation in NAFTA (North American Free Trade Agreement), [13] it is ironic that the rules of origin are having much the same effect on Japanese and European firms as yesteryear's national-content regulations did, with the difference that in this case they are discriminatory in nature. Generally speaking, they may have conflicting effects, and may give rise to any one of three different scenarios. First, given the need to export, the imposition of such standards could, within certain limits, contribute to the development of greater competitiveness, which would be reflected both in more exports and in more integrated and more efficient industrial sectors; [14] this would tend to occur in the more industrialized countries. Second, they may promote the formation of enclaves of sectors that become integrated via intra-firm trade among foreign subsidiaries in the relevant countries; this would tend to occur in sectors where the technological lag separating national enterprises from foreign enterprises is considerable.

Third, the fact that such rules present obstacles or entail added costs may discourage export-oriented FDI and thereby promote its concentration in the larger markets. This may be of importance in the light of the Enterprise for the Americas initiative, under which national origin rules, when applied to capital, would in effect discriminate against countries where there is more non-United States FDI. Thus, there is a risk that national origin rules could become an increasingly restrictive and discriminatory sectoral policy tool, when what is wanted is just the opposite (Fuentes, 1991a). Furthermore, the growing use of rules of origin for protectionist purposes provides a valid argument for setting common external tariffs as a way of reducing their impact. A danger also exists that other investment rules may be applied in a discriminatory manner, as in the case of mergers and acquisitions (*Inside US Trade*, 1992); given the absence of a multilateral framework in this area, however, regional agreements may serve as the foundation for subsequent multilateral accords (CTC, 1992b, pp. 44-45).

Even the largest corporations do not really examine the entire array of investment situations or opportunities that exist worldwide, however, but instead tend to follow in the steps of their competitors (Bélot and Weigel, 1991, p. 53). This constitutes an argument for the types of programmes which various developed countries (including a number of European countries and the European Community) have for promoting foreign investment. The European Community's programme, in particular, provides assistance in the identification of sectors, countries and firms which may be suitable sites for projects and financing for research, investment and training (Commission of the European Communities, 1991). Nevertheless, the desirability of targeting promotion efforts, the existence of economies of scale in these activities, and the successful experiences of some countries (e.g., Costa Rica and the Dominican Republic) in attracting FDI to such sectors as textiles and electronics all point to the advisability of having *sectoral* promotion programmes for specific countries while, at the same time, linking and coordinating the promotion programmes of international agencies, developed nations and developing countries (Bélot and Weigel, 1991, pp. 56-57 and 64-65).

IV

Services, privatization and European investment

When the manufacturing sector's growth began to slow to a standstill or even go into reverse in the 1980s, its relative share of FDI diminished in the vast majority of the region's countries (see table 9). This was coupled with an increase in the share of investment going to services in the larger countries (Argentina, Brazil, Peru and, especially, Mexico). In addition to a larger amount of foreign investment in its tourism industry, Mexico –along with Argentina, Chile and Venezuela– received a considerable flow of foreign investment in telecommunications as a

[13] Signed by Canada, Mexico and the United States.

[14] This was the thrust of the investment decisions taken in Mexico by Nissan, when it expanded its local production of automobile parts, and by Volkswagen, when it boosted its national content from 60% to 80% (*Expansión*, 1991b).

Table 9

LATIN AMERICA: SECTORAL DISTRIBUTION OF TOTAL STOCK OF FDI, 1980 AND 1990

(Percentages)

Countries	Primary	Secondary	Tertiary	Total
Argentina				
1980	14.9	62.8	22.3	100.0
1989	14.0	60.4	25.6	100.0
Bolivia				
1980	67.2	14.8	18.0	100.0
1990	71.4	13.2	15.4	100.0
Brazil				
1980	3.7	74.4	21.9	100.0
1990	2.9	69.3	27.8	100.0
Chile				
1983	41.2	25.3	33.5	100.0
1990	50.6	19.8	29.6	100.0
Colombia				
1980	6.1	70.7	22.9	100.0
1990	45.9	42.4	11.6	100.0
Costa Rica				
1980	45.8	43.2	11.0	100.0
1990	51.8	36.4	11.8	100.0
El Salvador				
1980	1.7	52.8	45.5	100.0
1990	1.3	54.2	44.5	100.0
Mexico				
1980	5.1	77.5	17.4	100.0
1990	1.9	62.3	35.8	100.0
Panama				
1980	14.3	50.3	35.4	100.0
1990	9.0	25.1	65.9	100.0
Peru				
1980	43.8	34.3	21.9	100.0
1990	34.7	34.2	31.1	100.0
Venezuela				
1980	1.8	61.7	29.3	100.0
1990	5.0	70.7	16.3	100.0

Source: Joint ECLAC/CTC Unit on Transnational Corporations.

result of the privatization of enterprises in this sector. The expansion of FDI in these countries' services sectors is in keeping with trends worldwide, particularly in the case of European FDI (CTC, 1991, pp. 18-20). In the remaining countries –including Bolivia, Chile, Colombia and Costa Rica– the concentration of FDI in the primary sector became more pronounced, in line with the nature of their position in the international economy (i.e., a position based on the utilization of the region's natural comparative advantages).

Investors' interest in the services sector has been heightened in recent years by the region's movement in the direction of deregulation and privatization, which has major implications in terms of competition, technological performance and discrimination. Within services, the subsector of *telecommunications* has been a favourite destination for foreign investment because the privatization process in this industry has been coupled with large-scale investments in which the level of risk is lower and the returns higher thanks to regulatory frameworks that ensure some degree of monopoly control (exclusive or restricted licenses) along with high, predictable rates, while penalties are confined to withdrawal of the license (ECLAC, 1991a). In addition, there is the possibility of making a profit by obtaining part of the discount at

which external debt paper is swapped, in cases where such instruments are involved. Yet another attraction is the strong possibility that the shares of privatized companies will rise in value on both national and international stock exchanges. Accordingly, European investment in the privatization of telecommunications enterprises has been significant (see table 10).

These privatization processes have a number of noteworthy characteristics. First, with the exception of Techint, all the European firms that appear in table 10 are government-owned, which creates somewhat of a paradox in cases of privatization. Second, assuming that ownership of around 20% of a company's stock can be taken as a meaningful indicator of controlling interest when dealing with consortia involving a number of participants, [15] the presence of European firms would appear to be decisive in five of the seven cases of privatization considered. Third, Telefónica de España's role in these processes has been considerable, since it has been involved in five of the seven cases, although with no more than a clearly minority interest in CANTV of Venezuela. Fourth, the segmentation of these markets has not always stimulated competition, at least not via the opportunity it would give to the Government to compare the performances of companies in the same sector. Argentina did manage to do this by dividing up the market geographically, but Chile's vertical division of the market between local and long-distance calls failed to ward off the danger of some degree of monopolistic control by Telefónica de España.

Finally, the privatization of telecommunications companies has altered their relationship with their traditional –usually European– equipment suppliers, and increased competition in this sector is anticipated. In Brazil, the end of the State monopoly on such services as data transmission, cellular telephones and the installation of telecommunications infrastructure has sparked competition among a wide array of Japanese, United States and European firms. In Mexico, too, the possibility exists that Telmex will discontinue the practice of purchasing most of its equipment from Swedish and French companies and will give more business to Japanese or United States enterprises in the future (*Business Latin America*, 1991).

In view of the fact that access to financing can constitute a significant entry barrier, there is a danger that this factor will overshadow a company's technological advantages in the minds of corporate decision-makers when they are weighing the pros and cons of entering new markets. In the case of Argentina (and of ENTEL in Chile), for example, the privatization process has been associated with debt-equity swaps. This has limited the number of offers, since bidders have to be able to acquire a considerable amount of debt paper; indeed, the entrepreneurial groups whose offers were accepted had to join forces with two banks (Morgan and Citibank) in order to accomplish this.

Another services industry which has been influenced by deregulation and privatization is the *airlines*. Apart from SAS, the Scandinavian airline, the only other European line with direct investments in Latin American airlines as of the beginning of 1992 was the Spanish airline, Iberia. As part of a determined strategy for consolidating its presence in the region, where it was serving 18 destinations in early 1992, Iberia acquired shares through regular commercial transactions in privately-owned companies that were not the leading airline in their respective home countries (Austral and Ladeco) while it became the major shareholder in others (Aerolíneas Argentinas and VIASA) through its participation in the privatization of these concerns (see table 11). The role of access to financing as an entry barrier was illustrated in the Argentine case, where the privatization operation involved cash payments, installment payments and the purchase of external debt paper; a number of subsequent delays and complications were indeed encountered owing to the consortia members' difficulties in obtaining the necessary financial resources.

[15] In Argentina, Telefónica de España and Techint are part of the Cointel group (in which Citicorp also has an interest), which controls 60% of the stock of Telefónica de Argentina. Meanwhile, a local group, J. P. Morgan, France Telecom and STET of Italy own 60% of the shares in Telecom Argentina.

In Mexico, France Telecom, together with a United States company (Southwestern Bell), forms part of a consortium which includes a local group and which, as a result of the privatization process, now owns 20% of the stock.

In Venezuela, Telefónica de España is part of a consortium which also includes two United States firms (GTE and AT&T) and local companies and which, thanks to the privatization process, now owns 40% of the stock.

Table 10

LATIN AMERICA: PARTICIPATION BY EUROPEAN CORPORATIONS IN THE PRIVATIZATION OF TELECOMMUNICATIONS ENTERPRISES IN FIVE COUNTRIES

Telecommunications company and year of privatization	European corporations	Percentage of shares
1. Telefónica de Argentina (1990)	Telefónica de España Techint (Italy)	20 6
2. Telecom Argentina (1990)	France Telecom STET (Italy)	18 18
3. Cía. de Teléfonos de Chile (1986-1988)	Telefónica de España	43
4. ENTEL, Chile (1986-1988)	Telefónica de España	20
5. Teléfonos de México (Telmex) (1990)	France Telecom	5
6. CANTV, Venezuela (1991)	Telefónica de España	6
7. PRTC, Puerto Rico (1991: long distance service)	Telefónica de España	100

Source: *Latin Finance*, N° 36, Miami, Florida, April 1992; *América Economía*, N° 59, Santiago, Chile, March 1992.

Table 11

LATIN AMERICA: EUROPEAN AIRLINE INTERESTS IN LATIN AMERICAN AIRLINES

Latin American airline	European airline	Percentage share in capital	Sum paid [a] (millions of dollars)
1. Ladeco (Chile)	Iberia	35	10.5
2. Austral (Argentina)	Iberia	100	20
3. Lan Chile	SAS	37	
4. Aerolíneas Argentinas	Iberia	49	600
5. VIASA (Venezuela)	Iberia	45	145

Source: *América Economía*, N° 57, Santiago, Chile, December 1991/January 1992; Joint ECLAC/CTC Unit on Transnational Corporations; *Latin Finance*, N° 26, Miami, Florida, May 1991; Salomon Brothers, *Private Capital Flows to Latin America*, 12 February 1992.

[a] Estimates. Include conversion of discounted debt in the case of Argentina and the total value of the operation in the cases of Aerolíneas Argentinas and of VIASA, which, in addition to Iberia, involved Crédit Suisse and First Boston in Venezuela as well as other participants in the consortium headed by Iberia in Argentina.

Iberia's expansion has made it one of the two highest-profile airlines in what appears to be the beginning of a concentrated regional oligopoly whose formation raises the spectre of possible bankruptcies, alliances or mergers among Latin American airlines in the future. Judging from the United States' experience with the deregulation of its airlines, this is a sector subject to significant economies of scale and entry barriers; these factors constitute valid grounds for the application of a policy on competition aimed

at regulating horizontal agreements concerning routes and vertical links between airlines and travel agencies (Bradburd and Ross, 1991). Moreover, in view of the transborder nature of the concentration process in this case, consideration should be given to the possibility of harmonizing or coordinating policies on deregulation and competition at the regional level. Events such as Japan's investment in Costa Rica's tourism industry and in its airline, Lufthansa's conclusion of a cooperation agreement with Aerovías de México and its investment in a major tourism consortium in that country, and Iberia's establishment of a regional office in the Dominican Republic could mark the beginnings of a gradual vertical integration of the airline and tourism industries (hotels, automobile rentals, domestic transportation) in the region, although this trend has not yet taken definite form.

In the case of *tourism*, two situations warrant discussion. First, Mexico and Cuba appear to have been the preferred destinations of tourism investment in recent years; part of the reason for this in the case of Mexico is the effect of debt-equity swaps in which British and Spanish investors have been deeply involved; Cuba, meanwhile, has seen an increase in Spanish investment in its hotel industry. Second, the growth of FDI in Cuba illustrates the extent to which Latin America (including Cuba) has relaxed the laws on foreign investment.

Foreign *banking* in the region has probably been the sector of foreign investment most severely affected by the external debt crisis (ECLAC, 1989), as well as by a wave of bank nationalizations that began in Nicaragua in 1979, continued on to Mexico in 1982 and culminated in Peru in 1989. These processes were later reversed, but they none the less account for the absence of large-scale foreign banking operations on a regular basis in these three countries in the early 1990s. Meanwhile, the renegotiation of debt commitments with the commercial banking system and the relaxation of certain restrictions [16] have opened up opportunities for some degree of expansion by foreign commercial banks in the rest of the countries.

At the start of the 1990s, the largest European banks in Latin America were from France and the United Kingdom, which were the most active European participants in the debt-equity swaps of the latter half of the 1980s. Table 12 ranks the largest foreign banks in the region according to the total amount of loans granted by their affiliates in each Latin American country. It will be noted that the list includes many European banks, in particular banks from: the United Kingdom (Lloyds Bank), France (Crédit Lyonnais), Spain (Santander), France and Italy (Sudameris) and Germany (Deutsche Bank). As of the early 1990s, these five banks all had large branches in Argentina and Brazil. In addition to the above banks, mention should be made of the presence maintained by banks from the Netherlands (Algemen Bank Nederland (ABN) and Nederlandsche Middenstands Bank (NMB)) in various countries of the region and the importance of Italian banks (Banca N. del Lavoro, Banco di Napoli) in Argentina.

Spanish banks have also been playing a dynamic role in the region in the early years of this decade. In the aftermath of the debt crisis, these banks adopted a position which places greater emphasis on secondary-market debt conversions than on rescheduling, and as a result have reduced their exposure in the region to one- sixth of its former level (*América Economía*, 1989). The Spanish banking system also increased its investments in financial services in Mexico and turned Spain into the second-largest source (after the United Kingdom) of investment in financial services in Chile since 1974. [17] The privatization of the banking system in Mexico did not spark an influx of foreign banks, although a Spanish bank does hold a minority interest in one of its newly privatized banks. Generally speaking, an intraregional liberalization of financial services in Latin America would find European banks in a particularly good position to take advantage of their presence in the region, although their degree of concentration would, on the other hand, justify considering the possibility of implementing a regionwide supervisory policy.

The importance of European banks in the region notwithstanding, United States banks have remained

[16] In the case of Brazil, for example, an increase in the number of branch offices was authorized (see Bodin de Morães, 1990).

[17] The United Kingdom was the source of 39% of the investment made in financial services between 1974 and 1991 while Spain accounted for 28% (Source: Foreign Investment Committee (CIE) of Chile.)

Table 12

LATIN AMERICA: MAIN FOREIGN COMMERCIAL BANKS, 1989 AND 1990

1989			1990		
Rank [a]	Name	Home country	Rank [a]	Name	Home country
1	Citibank	United States	1	Citibank	United States
2	Sudameris	France/Italy	2	Sudameris	France/Italy
3	Lloyds [b]	United Kingdom	3	Boston	United States
4	Boston	United States	4	Crédit Lyonnais	France
5	Santander	Spain	5	Santander	Spain
6	Deutsche Bank	Germany	6	Lloyds [b]	United Kingdom
7	Chase Manhattan	United States	7	Deutsche Bank	Germany

Source: *América Economía*, Santiago, Chile, October 1990 and October 1991.

[a] The ranking shown here is a tentative one inasmuch as it is based on estimates and incomplete information for Argentina, Brazil, Chile, Colombia, Ecuador, Mexico, Peru, Uruguay and Venezuela.

[b] The information for 1989 covers Lloyds' operations in both Argentina and Brazil, whereas the information for 1990 includes its Brazilian operations only; hence its descent from third place to sixth place in the ranking.

in the lead (ECLAC, 1989), with first-ranked Citibank's exposure being double that of Sudameris, the next largest lender. Moreover, if foreign banking operations in each country are considered separately, Citibank of Brazil and Citibank of Argentina turn out to be the largest foreign banks, followed by Sudameris and Lloyds in Brazil and Santander in Chile (*América Economía*, 1991b). Three of the five largest foreign financial institutions in Mexico in 1988 were European, but the overwhelming predominance of one United States enterprise in this group was attested to by the fact that the European institutions accounted for only 15% of the total value of the five enterprises' operations for that year (ECLAC, 1990b).

V

Conclusions

There is some concern in Latin America about the possibility of European investment being diverted to other destinations. The causes for this concern are the creation of the Single European Market, the reunification of Germany, the support being provided to Central and Eastern Europe, and the move made by member countries of the European Free Trade Association (EFTA) to join the European Community. Nevertheless, an analysis of FDI trends overall and particularly in countries such as Mexico and Chile up to 1991 actually points to a possible upturn and the gradual emergence of an increasingly favourable outlook for investment from Europe and the rest of the world in Latin America.

From a schematic viewpoint, this trend's point of departure is a stage marked by the subsidization of FDI via debt-equity swaps. In this case, the subsidy incorporated into such swaps tends to offset the perception of crisis-generated risk and can help to trigger a flow of FDI, especially from countries whose commercial banks are heavily exposed in the Latin American nation participating in the swap. Such FDI source-countries are attracted by the prospect of converting a low-yield, high-risk asset (debt paper) into a lower-risk and potentially higher-yield one (direct investment).

There will, of course, be less of a need to resort to such a subsidy in order to attract foreign investment as the region stabilizes its economies and consolidates its advances through fiscal reforms and successful external debt renegotiations, since this will make other investment opportunities more

attractive. For example, if share prices climb on the stock exchange in response to expectations of future growth, this will encourage inflows of foreign portfolio investment. Privatizations also help to attract portfolio investment and additional direct investment, not only because of the returns they themselves offer but also because of the signals which they send out regarding the relevant country's development strategy.

It is possible that special treatment for domestic investment could also help to spur this type of investment, and both domestic and foreign investment could help open up other new investment opportunities. In any event, if a new, clearly-defined development strategy is seen to have taken hold, longer-term expectations of a sort conducive to foreign investment (particularly in new, longer lead-time direct investment projects) could be generated. As expectations continue to brighten, the region's economic integration –whether at the hemispheric, subregional or bilateral level– could further reinforce movement in this positive direction.

As part of this process –which is either only just beginning or still incomplete in the great majority of Latin American countries– the nature of European investment in the region has been changing. First of all, European corporations (particularly British firms in Mexico and Chile, and French companies in Brazil) made considerable use of debt-equity conversion mechanisms during the second half of the 1980s. This fact, when considered in conjunction with German enterprises' limited use of these mechanisms, indicates that the level of European commercial banks' exposure in Latin America, rather than the returns to be had on direct investment *per se*, has been the chief determinant of the extent to which each European country has engaged in swaps and, hence, of the investments each has made in the region in the past.

Based on this dynamic, and with the aid of their pool of technological resources, European investors have followed a policy of holding their investment in Latin America's rather sluggish manufacturing sectors at more or less constant levels. The status of these sectors, the predominance of European investment in countries (e.g., Argentina and Brazil) which made relatively less headway than others in carrying forward their stabilization and adjustment programmes during the second half of the 1980s, and the implementation of what have in some cases been discriminatory sectoral policies compounded the situation created by the slower pace of modernization and export promotion programmes in European firms as compared to other foreign enterprises in the region. These firms' export performance has begun to improve as policies designed to stabilize the economy and to change production patterns have promoted a more rapid rationalization of business enterprises in general, as in Mexico, or as a result of expectations that a progressive integration of all the Latin American countries into the world economy is inevitable.

In addition, European investment largely stayed away from natural resources –a major destination for foreign investment in many countries of the region– and its share of total FDI in these countries, and particularly in Chile, therefore declined. However, European capital subsequently increased its involvement in the services sector through debt swaps and, especially, privatizations. Noteworthy aspects in this last regard include the participation of government-owned European corporations and the expansion of Spanish investment in telecommunications, air transport and financial services. In view of the inflow of foreign investment which generally accompanies deregulation and liberalization drives in Latin America, the need arises to examine the questions of supervision and of regionwide policies on competition.

The Latin American countries are laying the groundwork for changes in their production patterns and for the entry of foreign investment by modifying their sectoral policies as well as their macroeconomic and trade policies. This process may be hampered, however, if restrictive investment regulations are put into effect which discriminate against certain geographic sources of capital, as may be the case with rules of origin; under such circumstances, the conclusion of free trade agreements or the formation of regional trade blocs may discourage European investment. It is hoped that transnational corporations' progressive globalization of their activities will facilitate the harmonization of regulations on foreign investment so that they will serve as a foundation, rather than constituting a stumbling block, for a transparent economic order in which multilateral arrangements are the predominant force (CTC, 1992b, p. 45).

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