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Any comments or suggestions regarding this publication should be addressed to Michael Mortimore (e-mail: michael.mortimore@cepal.org).

Explanatory notes

The following symbols are used in tables in this Study:

Three dots (...) indicate that data are not available or are not separately reported.

A dash (–) indicates that the amount is nil or negligible.

A point (.) is used to indicate decimals.

Use of a hyphen (-) between years (e.g., 2001-2005) indicates reference to the complete period considered, including the beginning and end years.

The word "tons" means metric tons and the word "dollars" means United States dollars, unless otherwise specified.

References to annual rates of growth or variation signify compound annual rates, unless otherwise specified.

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Abstract

In 2005, foreign direct investment inflows to Latin America and the Caribbean (not including financial centres) amounted to over US\$ 68 billion, almost 11% more than in 2004. These inflows greatly exceed the figures recorded between 2001 and 2003, but they still fall short of the volumes observed during the FDI boom of the late 1990s. The region also continues to see its share in world flows decline, which suggests that it has yet to realize its true potential for attracting such investment. This is at least a two-fold problem.

On the one hand, the region has certain policy-related and institutional weaknesses that hinder its efforts to face up to the strong competition for FDI. To gain a better understanding of this situation, the Economic Commission for Latin America and the Caribbean (ECLAC) carried

out a study on the role and practices of 15 investment promotion agencies. The findings of that study are presented in chapter II.

On the other hand, success in taking advantage of FDI and the presence of transnational corporations depends, to a large extent, on the extent of local companies' absorptive capacity. The second part of this year's report provides a detailed analysis of the competitive positions and internationalization processes of a large number of emerging Latin American transnational corporations, referred to in the study as "trans-Latins". This information was compiled on the basis of interviews with executives from major trans-Latins in Argentina, Brazil, Chile and Mexico. The conclusions reached on the basis of this analysis are presented in chapters III through VI.

Summary and conclusions

The US\$ 68 billion in inflows of foreign direct investment (FDI) received by Latin America and the Caribbean¹ in 2005 were about 11% higher than the level of FDI it posted in 2004. In terms of the growth of those inflows, however, Latin America and the Caribbean were outperformed by other world regions. The good news was that many emerging transnational corporations (TNCs) from the region (here referred to as “trans-Latins”) continue to deepen their internationalization processes through FDI, although starting from a comparatively small base. In addition, a large part of Latin American and Caribbean countries’ outward FDI (OFDI) goes to other nations in the region, thereby reinforcing inward FDI flows as well. In this respect, the region is positioning itself more advantageously with regard to OFDI, even while it continues to exhibit weaknesses in attracting new inward FDI from outside of the region, especially the higher-quality FDI that would generate more profound multiplier effects in host countries. This year’s report examines the competitive situation of Latin America and the Caribbean in terms of its ability to attract FDI and offers a number of recommendations concerning the types of more active policies needed to do so. The bulk of this year’s edition focuses on trans-Latins.

¹ These figures do not include inflows to financial centres in the region.

A. Overview of FDI in Latin America and the Caribbean

1. FDI inflows to Latin America and the Caribbean

As in earlier editions of *Foreign Investment in Latin America and the Caribbean*, two data sets will be used to analyse the profiles of TNCs in the region. One set comprises balance-of-payments information on FDI inflows, while the other focuses on company-level information on sales and exports. This combination of statistical information provides a basis for a more incisive analysis of the presence and operations of TNCs in the region than would otherwise be possible.

Table 1 shows FDI inflows to Latin America and the Caribbean (excluding financial centres) during the past 15 years. Three major trends stand out. First, total inflows rose from an annual average of US\$ 20.2 billion in 1991-1995 to US\$ 70.6 billion in 1996-2001 before falling sharply thereafter. Then, in 2004, they began to rebound, surpassing the US\$ 68 billion mark. An important aspect of this trend was the shift in the composition of these flows away from privatizations. Second, South America has traditionally received more FDI than Mexico and

the Caribbean Basin, but it has also experienced much more volatility, in part because much of its inward FDI has been related to one-off privatizations. Between 1991-1995 and 1996-2000, South America's annual average FDI inflows rose by a factor of five—from US\$ 11.8 billion to US\$ 53.2 billion—before falling back to about US\$ 34.7 billion. Mexico and the Caribbean Basin only managed to double their average annual inflows during this period (from US\$ 8.4 billion to US\$ 17.5 billion) but were able to maintain them at roughly the US\$ 24 billion level thereafter. Third, the winners and losers for 2005 (compared to 2004) are clear: the Andean Countries (especially Colombia, but excepting Bolivia), Argentina, the Dominican Republic, Nicaragua and Uruguay are in the first category, while Bolivia, Brazil and Honduras are in the latter. In other words, the absolute level of FDI inflows continues to be variable and its distribution is uneven, although, when weighted by GDP, there is clearly a convergence between the subregions in this respect.

Table 1
LATIN AMERICA AND THE CARIBBEAN: NET FDI INFLOWS, BY SUBREGION, 1991-2005^a
(Millions of dollars)

	1991-1995 ^b	1996-2000 ^b	2001-2005 ^b	2004	2005 ^c
Mexico	6 804.6	12 608.8	18 805.8	18 244.4	17 804.6
Central America	659.2	2 340.2	2 250.7	2 728.8	2 745.0
Caribbean	945.1	2 519.1	2 857.9	2 861.2	2 971.3
Subtotal - Mexico and Caribbean Basin	8 408.9	17 468.1	23 914.4	23 834.3	23 520.8
MERCOSUR	6 445.2	36 757.1	19 883.1	22 822.1	20 398.5
Andean Community	3 685.5	10 746.7	9 701.1	7 674.0	16 918.5
Chile	1 666.2	5 667.0	5 087.7	7 172.7	7 208.5
Subtotal - South America	11 797.0	53 170.7	34 671.9	37 668.8	44 525.4
Total - Latin America and the Caribbean	20 205.8	70 638.9	58 586.2	61 503.2	68 046.3

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of statistics from the International Monetary Fund and official figures.

^a Excludes financial centres. Net FDI inflows are defined as FDI inflows to the reporting economy minus capital outflows generated by the same foreign companies. These FDI figures differ from those published by ECLAC in *Preliminary Overview of the Economies of Latin America and the Caribbean* because in that study, FDI was defined as the inflows to the reporting economy minus outflows from residents.

^b Annual averages.

^c Data available as of 24 April 2006.

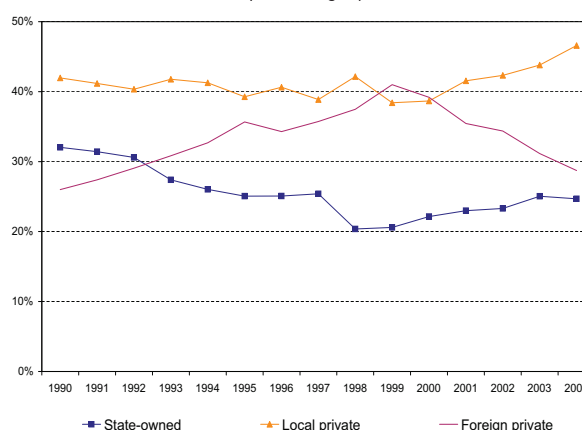
Both major subregions of Latin America and the Caribbean —Mexico/the Caribbean Basin and South America— receive FDI of all types, but there have traditionally been important differences in emphasis. Mexico and the Caribbean Basin tend to receive proportionately more efficiency-seeking FDI aimed at establishing export platforms for manufactures, while South America receives a larger proportion of market-seeking FDI in both services and manufactures. Although an incipient trend towards more efficiency-seeking operations has been observed in Brazil in the electronics and automotive industries, it remains to be seen whether this trend will persist, given the revaluation of the Brazilian *real*. As regards geographical origin, more FDI in Mexico and the Caribbean Basin comes from the United States, whereas in South America, the largest share comes from European countries. There are also some important differences within these subregions.

These characteristics of inward FDI are also reflected in the international competitiveness of the two subregions, although FDI is clearly not the only factor involved. On the one hand, Mexico and the Caribbean Basin experienced solid growth in their international market shares in 1980-2004, especially with regard to non-resource-based manufactures, although this trend has weakened somewhat since 2002. FDI in export platforms for the electronics, automotive and apparel industries accounts for much of this export success, even though these investment flows are also associated with some of the recent difficulties that have arisen as FDI export platforms in China crowd out some of this subregion's sales on the United States market. South America, on the other hand, has specialized in natural resources and natural-resource-based manufactures, in which FDI is not so important a factor. The long-term international market shares of South America have not increased nearly as much as those of Mexico and the Caribbean Basin, although the high international prices of several commodities (petroleum, copper, gold, soybeans) did have the effect of expanding the international market shares of South America in 2002-2004. Thus, FDI plays a very important role in relation to the Mexican and Caribbean Basin subregion's international competitiveness but is less influential—but by no means unimportant—with regard to the international competitiveness of South America.

The evolution of TNCs in Latin America and the Caribbean is reflected in their position on the list of the 500 top enterprises by sales and the top 200 principal exporters. TNCs' share of the sales of the 500 largest companies in Latin America and the Caribbean rose from 26% to 43% between 1990 and 1999 before falling back to 29% in 2004. Interestingly, both private local firms and State enterprises, which have enjoyed high international prices

for the commodities that they produce, have improved their positions relative to foreign firms within the top 500 during the last few years. Meanwhile, the TNC share of the main 200 exporters' foreign sales climbed from 19% to 47% between 1990 and 2000, before declining to 36% in 2004. Thus, the operations of TNCs in Latin America and the Caribbean, measured as a proportion of the total sales and exports of the largest firms in this region, swelled during the FDI boom years and have shrunk during the 2000s, but are still significantly higher in absolute terms than they were before the boom.

Figure 1
LATIN AMERICA AND THE CARIBBEAN: TOTAL SALES OF THE
TOP 500 FIRMS, BY OWNERSHIP, 1990-2004
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the Special Studies and Projects Department of *América economía* magazine, Santiago, Chile, 2005.

According to the latest information available, consolidated sales of the principal subsidiaries of the 50 largest TNCs operating in the region amounted to US\$ 258.6 billion in 2004. United States companies still lead the list, with 22 firms, although European companies, taken together, have 24 affiliates. Three Asian companies and one Australian firm make up the balance. In all, 31 of the companies are manufacturers, 11 are service providers and 7 specialize in natural resources. One is a diversified conglomerate. The manufacturers are concentrated in the automotive industry (9), food products and beverages (7) and electronics (6). The service providers deal mainly in telecommunications (4), electricity (3) and retail trade (3). Five of the seven natural-resource-based companies are petroleum/gas producers, while the other two are mining companies. Five of the top ten companies are either United States enterprises (General Motors, Delphi and Ford) or German (Volkswagen and DaimlerChrysler) firms operating in the automotive industry. Three of the top ten firms are Spanish or Italian companies operating in the telecommunications industry (Telefonica, Telecom Italia) and electricity (Endesa)

sectors. Most of the affiliates of the top 50 TNCs in terms of consolidated sales operate in the three largest markets, that is, Mexico, Brazil and Argentina.

No major changes took place in relation to the presence of transnational banks in the region in 2004. Two Spanish banks (BSCH and BBVA) and one United States bank (Citicorp) still top the list of the principal transnational banks (in terms of assets) operating in the region.

In short, TNCs have maintained a significant presence in Latin America and the Caribbean, but their position has been slipping somewhat over the last few years.

Thus, the Latin American and Caribbean region's experience with FDI can be summed up as follows. During the 1990s, Latin America and the Caribbean were quite successful in attracting large amounts of FDI based on new economic models that focused on opening up the economy, liberalizing business activities and implementing strong horizontal incentives in the form of the deregulation of services and the privatization of State enterprises. Those initiatives attracted mostly market-seeking and natural-resource-seeking FDI. The region did not perform as well in attracting efficiency-seeking and, especially, strategic or technological asset-seeking FDI, which are associated with the globalization of TNC activities.

A debate has arisen about the benefits of the FDI received by Latin America and the Caribbean. On the one hand, FDI inflows have played an important role in transforming the region by modernizing industry and improving services and infrastructure. This effect is evident in the upgraded telecommunications network in Brazil, financial services in Argentina, road and airport services in Chile and the export platforms in Mexico and Costa Rica that assemble competitive motor vehicles and microprocessors, respectively. On the other hand, serious problems have arisen in different parts of the region with regard to FDI. Natural-resource-seeking FDI is criticized for creating enclave industries entailing few of the types of processing activities that would help integrate these investments into the national economy, as well as for generating low fiscal revenues from non-renewable resources and polluting the environment. Market-seeking

FDI is often regarded as creating higher-cost industrial activities that, although not internationally competitive, sometimes crowd out local firms, as well as services prone to regulatory problems that at times trigger formal investment disputes. Efficiency-seeking FDI is criticized because it often results in a low-value-added trap based on static rather than dynamic advantages, has only weak production linkages with the local economy, crowds out local firms and can lead to a "race to the bottom" in terms of production costs (wages, social benefits) and a "race to the top" with regard to incentives (taxes and infrastructure). Finally, technology-seeking FDI (which is almost non-existent in the region) can stagnate at a low level of scientific and technological development and can come into tension with national scientific and technological policy goals. In other words, the FDI boom in Latin America and the Caribbean produced mixed results and, as FDI inflows decline, criticism of those results increases.

The Latin American and Caribbean experience illustrates the fact that while FDI by TNCs can lead to increased productivity and exports, it does not necessarily boost the domestic sector's competitiveness, which is what ultimately determines long-term economic growth. Economic liberalization allows TNCs to tap into existing capabilities more freely but does not, in itself, provide growth opportunities unless the domestic industrial sector has the necessary absorptive capacity to profit from externalities generated by TNC activity. As a consequence, over time, FDI inflows from TNCs rise in countries where local capabilities are strengthened and new capabilities are created, but they stagnate or fall in economies where this does not happen. For this reason, it is essential to connect the competitive advantages of TNCs to the improvement of the domestic absorptive capacity of host economies. The Latin American and Caribbean countries require improved FDI policies in the context of more coherent development strategies to derive long-term benefits from FDI by TNCs. This suggests that governments in the region have a major policy role to play in attracting more and better FDI that will contribute to the industrial and technological upgrading of the host economy and the improvement of its international competitiveness.

2. More active FDI policies

While FDI can be attracted in a number of different ways, recent experience suggests that the more successful countries employ active or integrated strategies to do so. Active policies are based on prioritizing certain kinds of

FDI and then creating the necessary conditions to attract them (availability, cost and quality of factors of production), whereas passive policies rely mainly on the natural resource base, on macroeconomic, legal and institutional conditions,

and on certain types of measures (non-discrimination, guarantees and legal protection, horizontal incentives) to facilitate FDI. The former usually target higher-quality (often efficiency-seeking or strategic asset-seeking) FDI within a coordinated policy framework focusing on productive development. By contrast, the latter policies tend to attract natural-resource- or market-seeking FDI and to be independent of other policies. An integrated approach in this area, on the other hand, involves linking FDI and other productive development strategies directly to the national development strategy.

Governments around the world are now tending to move towards the use of more active and more focused investment policies. These policies are aimed at promoting both foreign and national investment by providing more effective ways to compete for higher-quality FDI, on the one hand, and by improving the domestic absorptive capacity of the host economy, on the other. This trend is evident in developed countries (mainly European nations, such as Ireland, the Nordic countries, France, United Kingdom), transition economies (e.g., Hungary, Czech Republic) and developing Asian countries (e.g., Singapore, Republic of Korea, China, Malaysia, Thailand). More recently, there is evidence of a further shift from active to integrated FDI policies, that is, the harmonization of FDI policy within overall development policy. National investment promotion agencies (IPAs) often play a central role in helping countries to reach their policy goals, especially in terms of attracting higher-quality FDI.

The situation in Latin America and the Caribbean does not, however, reflect these global trends; instead, FDI policy in this region seems to have remained in its infancy, in the sense that FDI policies are primarily passive and most of the national IPAs are new and lack experience. While the mere existence of an IPA is no guarantee of success, the experiences of the above-mentioned European, Asian and transition economies suggest that an effective IPA can be a critical element in attracting higher-quality FDI and deriving greater benefits from existing FDI, assuming that other crucial elements for TNC investment decisions are in place, such as sufficient domestic absorptive capacity as reflected in a suitable business environment and the availability of qualified workers and local input suppliers. In order to better understand the actual status of IPAs in Latin America and the Caribbean, ECLAC has undertaken a detailed survey whose results are presented in chapter II. The focus here, briefly, is on the nature of FDI promotion in the region, especially the use of incentives and targeting strategies.

FDI promotion calls for marketing efforts in the potential host country and measures designed to facilitate investments by overcoming information asymmetries and reducing installation costs. Successful recipient countries

usually possess well-established IPAs that can compete effectively in this area. IPAs in Latin America and the Caribbean, with few exceptions, tend to have inadequate budgets and few professional staff, very few foreign offices, limited coordination with subnational offices, and a weak outward orientation. This makes it very difficult for them to compete effectively with IPAs in other regions, especially those in Europe, Asia and certain transitional economies. Latin American and Caribbean IPAs need to strengthen their budgets and staff and to position themselves more advantageously at the national and international levels in order to develop a more coordinated, outward-oriented FDI promotion capacity.

The more competitive IPAs of Europe, Asia and some transition economies often use targeted incentives to make their economies more attractive, in particular to the efficiency-seeking and strategic or technological asset-seeking FDI that they prioritize. The most common incentives take the form of fiscal measures (tax relief) or financial benefits (direct subsidies to reduce set-up costs). In Latin America and the Caribbean, in contrast, existing incentives are primarily fiscal in nature and tend to be general, horizontal and automatic measures, usually involving export processing or maquila services and corporate tax rates. Moreover, there appears to be little evaluation in the region of how effective these incentives are in terms of their stated objectives. The IPAs of Latin America and the Caribbean recognize the importance of incentives, especially to both promote local investment and attract higher-quality FDI, but they have little experience with targeted incentives. This suggests that governments in the region that are not satisfied with the quality of the FDI that their countries have received might want to re-evaluate the use of FDI incentives in today's more competitive international environment and to consider shifting from horizontal to targeted ones. The experience of other regions suggests that more active policies utilizing targeted incentives could improve the quality of the FDI that the Latin American and Caribbean region attracts and the benefits that it derives from these investments.

Many countries employ FDI targeting strategies to make better use of their limited resources and to achieve specific objectives by focusing in a proactive way on identifying and engaging certain kinds of investment projects. These projects may be targeted by sector (e.g., the automotive industry, biotechnology), function (manufacturing, logistics, R&D), type of project (investment amount, technology-intensive ventures), type of investor (Fortune 500, brand name, "winners"), or source country (United States, neighboring countries). In Latin America and the Caribbean, with very few exceptions (Costa Rica, Chile), FDI policies are not linked to targeting

strategies, however, and where targeting does exist, it is very broad and relatively unfocused. The Latin American and Caribbean region's performance in attracting FDI for R&D from TNCs has been particularly dismal compared to other regions.

More active policies do not guarantee success in attracting higher-quality FDI or improving the benefits for the host country, however. This has been clearly demonstrated by the incentives war waged among various Brazilian states in an attempt to attract the major new FDI projects being launched by automotive TNCs during the 1990s, to cite just one example. Poorly designed and badly implemented active policies may, in fact, prove to be more costly than passive ones, especially if local authorities do not possess a clear idea of their country's FDI potential in the context of its absorptive capacity or of the differences between the social and private costs and benefits of large FDI projects. Governments contemplating such policies would therefore do well to ensure that their FDI strategy sets out clear objectives and is realistic in terms of domestic absorptive capacity.

Governments considering the use of more active policies to attract higher-quality FDI must determine whether or not they possess what the TNCs that they are targeting are looking for (e.g., access to export markets, good quality and low-cost human resources, physical infrastructure, local inputs, and service logistics in the

case of efficiency-seeking FDI, or the requisite scientific base, scientific infrastructure and intellectual property protection in the case of strategic asset-seeking FDI). They will also have to offer a conducive business environment, in which stable rules and solid institutions are crucial. Any shortfalls in these areas will have to be addressed by means of policy solutions within the context of a concrete development strategy.

National institutions also need to be up to the task. It is particularly important for them to generate both the conditions and capabilities required for the FDI they want to attract. In order to do so, these institutions must understand TNC motivations and behaviour in today's more competitive environment and, in particular, the factors that determine which host countries will survive the TNC decision-making process as regards site selection and will thus make it onto their shortlists of potential investment sites. At the same time, it would be prudent to look beyond the transition from passive to active FDI policies and begin to lay the groundwork for a future shift towards integrated policies by harmonizing the role of FDI policy within the overall development strategy. This would enable Latin American and Caribbean countries to begin to close the policy gap with competing host countries, especially those that have been most successful in attracting higher-quality FDI and benefiting more from it. In this field, policy definitely matters.

B. Trans-Latins

Emerging TNCs from developing and transition economies are an increasingly important phenomenon for the world economy which is not adequately captured by OFDI statistics. OFDI from developing countries started long ago, but did not become a full-scale boom until the 1990s. In the process, developing Asian TNCs have far surpassed their Latin American and Caribbean counterparts. Be that as it may, emerging Latin American TNCs—trans-Latins—have become a factor in FDI inflows and are attempting to position themselves better in national, regional and international markets. ECLAC interviewed 45 trans-Latins in four different countries of the region—Argentina, Brazil, Chile and Mexico—in order to gain a better perspective on this phenomenon.

The developing Asian OFDI boom must be distinguished from the Latin American and Caribbean one, especially in terms of the factors driving them and

the types of productive specialization that have resulted. Case studies suggest that developing Asian TNCs are more likely to internationalize into world markets in general based on efficiency- and strategic asset-seeking strategies, while the emerging TNCs of Latin America and the Caribbean and a number of other regions (transition economies, Africa) tend to move into neighboring markets, usually on the basis of natural resource- and market-seeking strategies. In the case of Latin America and the Caribbean, the focus is primarily on Latin American and North American markets.

Case studies also suggest that the main push factors in the recent Asian experience were a relative scarcity of natural resources, these nations' cumulative (and positive) OFDI experiences, the need to lower production costs and acquire strategic assets, and sophisticated government promotion of OFDI by way of a reduction in exchange-rate

restrictions, institutional support, financial support and, in some cases, special OFDI agencies. By contrast, the Latin American experience and, to a certain extent, that of other regions have been driven more by macroeconomic instability (boom/bust cycles in domestic demand and exchange-rate volatility), truncated (and sometimes negative) experiences as outward investors, the need to diversify risk and the opening up of these economies to foreign competition, in conjunction with the increased competition brought by deregulation and privatization, as well as much more limited government promotion of OFDI (mainly in the form of reductions in exchange-rate restrictions). Interestingly, State-owned enterprises are playing an important role in both regions, but in the case of developing Asia, these ventures tend to cut across several activities, while in the Latin American countries, such enterprises are mainly concerned with petroleum.

The main pull factors influencing developing Asian OFDI, meanwhile, have been centred more on gaining access to third markets for host-country export platforms; making use of the availability of technology, organizational practices and management skills, and connections to China's overseas network; acquiring the means to improve logistics, reduce production costs and avoid trade restrictions; converting national brands into global ones; following clients; associating with TNC clients (in the electronics industry, for instance, in order to integrate more fully into supplier networks); and obtaining trade preferences in host countries. In the case of Latin American OFDI, on the other hand, the chief pull factors have revolved around other (Hispanic) networks, privatization and deregulation opportunities in neighbouring countries, improving distribution systems, converting national brands into regional ones, associating with TNC partners (e.g., food products, beverages, auto parts, white goods), and obtaining preferential access to host markets via subregional integration (Argentina and Brazil) and free trade (Mexico and Chile) agreements and, possibly, via more extensive legal guarantees for foreign investments under the terms of national, bilateral and multilateral agreements.

The trans-Latins come primarily from just four Latin American countries: Argentina, Brazil, Chile and Mexico. Some of the factors that have supported the internationalization of the Argentine trans-Latins include their large domestic market shares, improved positions in the value chain (e.g., Arcor), alliances or associations with TNCs (Arcor with Danone), improved logistics or distribution systems (Arcor), the possibility of capitalizing upon similar consumption patterns in neighbouring countries (Quilmes), experience and capacity for large-scale infrastructure projects in developing-country settings (Impsa) and the opportunity to lower production costs by

bargaining more successfully with suppliers and by making use of competitive technical and managerial capacity (Techint). Radical changes in the Argentine economic model that helped to stabilize the economy and open it up to increased foreign competition starting in the early 1990s have represented an important driver as well. So too have host-government policies that have opened up other economies within the region and, especially, new opportunities arising from deregulation or privatization (Techint, YPF, Perez Companc) as well as, possibly, the trade preferences made available through the MERCOSUR integration scheme.

Two characteristics of Argentine OFDI stand out among all others. First, it has been concentrated in a few industries (petroleum, steel, food products) dominated by a small number of large enterprises (YPF, Perez Companc, Techint, Arcor). For example, in 1997, during the peak of Argentine OFDI, three companies accounted for almost two thirds of total OFDI from Argentina: Pérez Companc, YPF and Techint. Second, many of the companies in this select group no longer exist as Argentine trans-Latins. YPF and Perez Companc—both from the oil and natural gas industry—were subsequently acquired by foreign companies (the first by the Brazilian trans-Latin, Petrobras, and the second by the Spanish TNC, Repsol). The transnationalization of these major Argentine trans-Latins, in conjunction with the sale to TNCs of significant equity or assets by others (Quilmes, Macri and Mastellone), is one of the defining aspects of the Argentine experience.

Brazilian OFDI has been based mainly on natural-resource-seeking and market-seeking strategies. Early on, OFDI was carried out to diversify sources of petroleum or to support exports of mainly primary products. The initial investors were State-owned firms, such as Petrobras and CVRD, as well as others that had based their growth, to a great extent, on serving as suppliers to the State and that were obliged to look for new markets when the crisis in public finances broke out in the 1980s (Odebrecht). Since the 1990s, trade liberalization, deregulation and privatization have, on the one hand, generated a number of push factors that have prompted companies to look to foreign markets: greater competition in the domestic market, the need for greater scale to ensure competitiveness (Embraco) and increasingly modern and professional management in both former State-owned (CVRD, CSN) and family-owned groups (Gerdau, Camargo Correa). This shift in orientation has also led to a refocusing on core strengths. The main pull factors have been supplier relationships with transnational clients (Embraco), economic reforms (including privatizations) in other markets, especially within the region (Petrobras, Usiminas) and, more recently, the crisis in Argentina, which opened up opportunities

for several acquisitions (Petrobras, Camargo Correa). A distinctive characteristic of Brazilian OFDI is that Brazilian companies appear to be more concerned than firms in other countries with the diversification of risk and the possibility of using OFDI as a tool for risk management by ensuring greater diversity in the location of assets (and therefore lower capital costs) and for hedging against adverse trends in macroeconomic variables (exchange-rate volatility and fluctuations in demand). Considering the size of the Brazilian economy, the internationalization of its trans-Latins has been rather limited.

The investments of Chilean trans-Latins have been concentrated in a small number of activities linked to comparative advantages in natural resources (forestry), natural-resource-based manufactures (metals) and services (temporary advantages in the cases of electricity and pension funds, and more permanent ones in the cases of retail trade, beverages and air transportation). The early timing (1970s) of Chile's economic reforms (including the privatization of State-owned enterprises), the accumulated experience of operating in an open and competitive economy, and geographical and cultural proximity provided Chilean trans-Latins with competitive advantages that enabled them to seize opportunities arising in neighbouring countries. Thus, initially, the early reforms gave Chilean trans-Latins an advantage over competing TNCs that possessed little knowledge of how to function in the Latin American environment; however, those advantages soon waned, and some of the Chilean companies that were most active in the internationalization process were taken over by international operators (Enersis, Gener, pension funds). Retail companies (Falabella, Cencosud, FASA, Ripley) made up a new wave of internationalizers, following upon the experience of mainly natural-resource-based manufacturers (Arauco, CMPC, Masisa, Molymet, CCU, Embotelladora Andina, Madeco). In every instance, the internationalization of Chilean trans-Latins has been closely focused on neighbouring countries, especially Argentina and Peru. Many Chilean trans-Latins experienced difficulties in the course of their internationalization processes and were obliged to retrench after substantial losses. As a result, with the exception of FASA and Masisa, the internationalization of Chilean trans-Latins has not been very extensive.

The success of the large Mexican trans-Latins has depended on a variety of factors, even though most of these companies have implemented similar market-seeking investment strategies. The principal push factors have been the impacts of changes in home-government policy based on the new economic model (opening the national economy to increased trade and investment competition), new access to other markets (especially in North America) through free trade agreements, and the new corporate strategies that emerged from the increased competition and

the changed domestic business environment that emerged in the early 1980s. Mexican companies, whether operating in mature industries or in dynamic global sectors, were obliged to react. CEMEX was the only one to become a global TNC. Some attempted to become regional players by stepping up their internationalization processes on a relatively independent basis (Alfa, San Luis Rassini, Bimbo, IMSA, TELMEX) or through a TNC-linked model (America Movil, Gruma, Coca Cola FEMSA, Mabe). The key pull factors have related to host-country locational advantages (growth opportunities, geographical proximity, Hispanic networks) that tie in with corporate objectives (new markets, consolidation of existing export markets, improved position in the value chain) and impacts of changes in host-government policies (especially free trade agreements). Many of these companies have experienced difficulties at one time or another during their internationalization process but, fortunately, have been able to learn from their mistakes.

In general, there are relatively few trans-Latins for a region the size of Latin America and the Caribbean. Developing Asia, by comparison, has many more emerging TNCs. In fact, in 2003, only 7 of the top 50 emerging non-financial TNCs from developing countries, measured by assets, were from Latin America and the Caribbean, whereas 40 were from developing Asia. This situation is a far cry from the state of affairs in 1977, when 14 of the top 30 developing-country TNCs were from Latin America. In other words, Latin America soon lost its early lead in internationalizing business ventures. Undoubtedly, the number of emerging TNCs generated by a region is related to its long-term growth rate. Sectoral considerations are also central, however.

The principal trans-Latins are found mainly in three broad sectors: basic industries, food and beverages and certain services. Many trans-Latins are concentrated in basic industries, that is, petroleum and natural gas, mining, steel and cement. Most got their start as local suppliers of natural resources. In many cases, the State has played an important and active role in the creation and promotion of such enterprises. In fact, many of these businesses are or began as State enterprises (Petrobras, CVRD, YPF, Usiminas, CSN, ENAP) or have been closely linked to State industrial development policies (Gerdaul, Techint). With the exception of América Móvil, founded in 2000, the largest, most geographically dispersed and most competitive of the trans-Latins are concentrated in basic industries.

Many of the more traditional trans-Latins in sectors other than basic industries deal in mass-market manufactures, such as soft drinks (Coca-Cola Femsa, Andina), beer (AmBev, Quilmes, Bavaria, CCU) and food products (Bimbo, Gruma, Arcor). These firms have generally been

more regional or less international than those in basic industries. These trans-Latins have competed against TNCs in their own national or regional markets, and their distribution systems have been their principal competitive asset. Sooner or later, most have been obliged to find some sort of way of coping with TNC competitors by focusing on niches, undertaking licensing arrangements, or selling them a minority or majority equity stake. Those that have attempted to retain greater independence have often sought out sector or market niches (Bimbo, Arcor), sometimes in the context of licensing arrangements (AmBev, Bavaria, CCU, Quilmes). Others have come to depend on TNC partners, even though they may not necessarily be formally controlled by them (Coca-Cola Femsa, Gruma, Andina, CCU). Others eventually became actual components of TNC networks (AmBev's transformation into InBev, Bavaria's sale to SABMiller).

Many of the more modern trans-Latins in non-basic industries have been active in services, such as telecommunications (América Móvil, TELMEX), retail trade (Elektra, Cencosud, Falabella, Ripley, FASA), airlines (Lan, Varig, TAM) and electricity (Enersis, Gener, ISA). In general, these firms have faced very stiff competition from TNCs. Two different types of situations have emerged in this respect, however. In some cases, successful trans-Latins have been able to take advantage of TNCs whose incursion into the Latin American market did not meet their expectations and that sold off those assets to trans-Latins (América Móvil, Cencosud, Falabella). In others, trans-Latins experiencing difficulties have sold some or all of their assets to TNCs (Enersis, Gener, Macri, Impsat). Some of the more traditional trans-Latins got their start by supplying engineering services to the large infrastructure projects of the import-substituting industrialization period (Brazilian engineering firms such as Oderbrecht and Andrade Gutierrez; Impsa from Argentina and ICA from Mexico) and were then obliged to seek foreign projects when governments in the region scaled back their State-financed infrastructure works.

Overall, trans-Latins that have grown out of basic industries associated with local natural resources have exhibited greater longevity and competitiveness. These firms, which first established a strong national base upon which to expand within the region, have eventually been able to generate a more enduring international presence outside of the region. The kind of State promotion that assisted these basic-industry trans-Latins was absent in the food and beverages and services sectors, which in part explains their more limited expansion within the region and their virtual absence beyond. The trans-Latins in these latter industries have faced much tougher competitors in national and regional markets, including, in particular, TNCs that maintain a presence in most or all major global

markets. As a consequence, they have tended to turn out to be "shooting stars", that is, national companies that grow and internationalize within the region but eventually end up as components of TNC systems, once their regional systems are acquired. Often, when these trans-Latins' regional production systems have reached a certain critical mass, they have become attractive to the TNCs that are constantly scanning regional markets for such opportunities.

This overview of the largest trans-Latins contrasts with the available information on the relative mobility of the 500 largest firms, by sales, in Latin America and the Caribbean, which indicates that as of 1999 the presence of TNCs in that group started to decline (falling from 43% to 29% by 2004) while that of local private firms has increased (from 37% to 46%) over the same period. Assuming that these figures are compatible with the data on trans-Latins, it would appear that the less internationalized companies on the list of the region's top 500 firms are doing better than the trans-Latins. This poses somewhat of a quandary for the Latin American business model.

A comparison of the very successful group of emerging TNCs from developing Asia with the less successful group from Latin America and the Caribbean suggests that the basic issues affecting their integration into the international market are quite profound and include such factors as entrepreneurship, domestic absorptive capacity and the role of home governments.

Latin America's integration into the international market continues to be fragile and to be based on the less dynamic activities in international trade. Moreover, many of the region's firms—even the most successful ones—seem to be at a significant disadvantage in terms of the competitive strengths required to prosper in global markets, particularly in activities that generate the most forceful multiplier effects. The two principal types of firms leading the region's integration into the global market are State-owned exporters of basic commodities, such as petroleum and copper, and TNCs with assembly plants (automotive and electronics plants, as well as other relatively more technology-centric activities). Given the focus on extractive and, generally, unprocessed natural resources, in the first case, and the high level of dependence on imported components, in the other, these firms' impact on domestic absorptive capacity in the form of knowledge creation, technology transfer, human resource training and locally-based supplier networks is limited. Consequently, the absorptive capacity of the region's domestic economies and the role of private national firms remain relatively weak by comparison to other regions. Even in the case of the principal trans-Latins (with the significant exception of several of the ones in basic industries), their internationalization is focused primarily on less competitive niches or neighbouring

countries, not the global market. As a result, the Latin American and Caribbean region does not possess anything even remotely similar to the Asian electronics industry, which has evolved into a world-class high-tech activity that incorporates national companies and has generated very strong multiplier effects for the developing Asian region as a whole.

Finally, for decades now, Asian home governments have been cultivating closer business/government interfaces in order to promote a greater affinity between business strategies and government development objectives. Home-government horizontal policies focused on improving the local business environment are often combined with selective ones aimed at assisting emerging TNCs to internationalize in strategic activities or priority sectors

(usually knowledge-based ones). The impact of those policies is reflected in the experiences of many of the faster-growing developing Asian economies, which have become hyper-competitive in producing manufactures. Many of these products require the use of complex technologies, state-of-the-art organizational practices and global supply chains. These kinds of policies and their effects are virtually absent in Latin America and the Caribbean.

In other words, in order to generate more trans-Latins, to improve their potential for becoming global TNCs and to augment their impact on the local economy, it is necessary to reevaluate certain fundamental aspects of the region's integration into international markets, such as the competitive ability of its entrepreneurship, domestic absorptive capacity and the role of home government policy.

Chapter I

Regional overview of foreign direct investment in Latin America and the Caribbean

In 2005, foreign direct investment (FDI) in Latin America and the Caribbean (excluding financial centres)¹ amounted to over US\$ 68 billion, which means the level of inflows was 11% higher than the previous year. The region saw a decline in its share of worldwide flows and those directed at developing countries, however. In terms of companies, an overview of the 500 largest enterprises in the region continues to show the trends seen in previous years: transnational corporations losing ground to local companies. This chapter analyses the current situation in terms of FDI inflows and the presence of transnational corporations (TNCs) in the region.

A. Recent FDI trends

1. The international situation

In 2005, worldwide FDI flows (including financial centres) shot up once more, to reach almost US\$ 900 billion, which is 29% up on the previous year. In a break from recent trends,

developed countries, developing nations, South-East Europe and the Commonwealth of Independent States (CIS) all received significantly higher inflows of FDI (see table I.1).

¹ Since there is limited information as to the proportion of FDI received by financial centres, which is effectively invested in the region, except where otherwise indicated, it is not included in the analysis.

Table I.1
GLOBAL DISTRIBUTION OF NET FDI INFLOWS, 1991-2005^a
(Billions of dollars)

	1991-1995 ^b	1996-2000 ^b	2001-2005 ^b	2004	2005 ^c
Worldwide total	231.7	814.1	754.3	695.0	896.7
Developed countries	148.8	601.2	514.6	414.1	573.2
United States	39.3	191.9	97.9	95.9	106.0
Europe	93.2	364.5	377.6	258.2	449.2
15 original members of the European Union	83.3	332.8	345.4	231.4	407.7
United Kingdom	14.9	67.7	80.2	77.6	219.1
10 new members of the European Union	7.2	16.6	24.2	27.8	37.7
Developing countries	80.4	203.2	212.4	243.1	273.5
Africa	4.9	9.4	19.6	18.7	28.9
Latin America and the Caribbean ^d	22.4	83.0	65.7	68.9	72.0
Asia and Oceania	53.1	110.7	127.2	155.5	172.7
China	22.8	42.7	54.8	60.6	60.3
South-East Europe and the CIS	2.5	9.7	27.1	37.2	49.9
Russian Federation	1.0	3.2	9.1	12.5	26.1

Source: United Nations Conference on Trade and Development (UNCTAD), Foreign direct investment database [online] (www.unctad.org/fdistatistics). For figures for 2003 to 2005, United Nations Conference on Trade and Development (UNCTAD), "Data show foreign direct investment climbed sharply in 2005", Press release, Geneva, 23 January 2006.

^a In 2005, the United Nations introduced a new geoeconomic classification of countries. The main difference is the incorporation of the 10 new members of the European Union into the category of developed countries and changes to the categories of Central and Eastern Europe. Data from previous years were therefore reorganized to provide a series in keeping with the new criteria. For further details, see UNCTAD (2005b, p. 6).

^b Annual averages.

^c Preliminary figures.

^d Includes financial centres, unlike the totals shown in figure I.2 and tables I.2 and I.3.

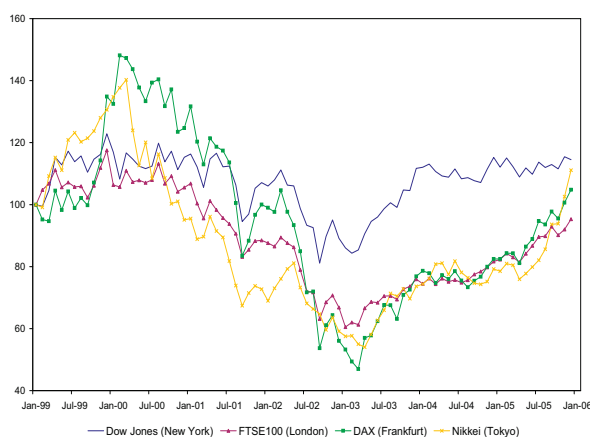
In 2005, FDI in developed countries grew for the second year in a row, to stand at US\$ 573 billion. The European Union as a whole was the main recipient of FDI at the global level, with most of the US\$ 445.4 billion total going to the 15 original member countries. The United Kingdom was the largest individual recipient, receiving the highest amount ever recorded by a European country, although a large share of this was the result of a single company's internal restructuring.²

FDI in all developing regions increased to US\$ 273.5 billion, which represents 31% of worldwide flows. The amount received by African countries almost doubled in 2005 to US\$ 30 billion, while China was the world's third largest recipient and accounted for 22% of all FDI going to developing countries.

The world economy continued to expand in 2005, although at a more moderate rate than in 2004 (ECLAC, 2005b; IMF, 2005a). The prospects for the expansion of global FDI continue to look positive, partly thanks to

good performances in the financial and corporate spheres. Sales of the world's top 500 firms climbed by 13% in 2004 and profits rose by 27%, which means that those companies have greater resources available to finance new projects. Moreover, with interest rates relatively high, companies sought financing on the main stock exchanges, which accounts for the expansionary cycle initiated at the beginning of 2003 (see figure I.1). Stock markets thus remain a significant option for borrowing and highly rated companies have been able to raise capital from financial institutions on better terms.

Figure I.1
STOCK MARKET INDEX TRENDS, NEW YORK, LONDON,
FRANKFURT AND TOKYO, 1999-2005
(Index: January 1999=100)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by Bloomberg.

Mergers and acquisitions are still the main channels for FDI and are estimated to have represented around two thirds of total worldwide FDI between 1995 and 2004. Mergers and acquisitions are expected to be the main form of investment worldwide in 2006, although developing regions with lower production capacity will probably see more greenfield investment (UNCTAD, 2005a).

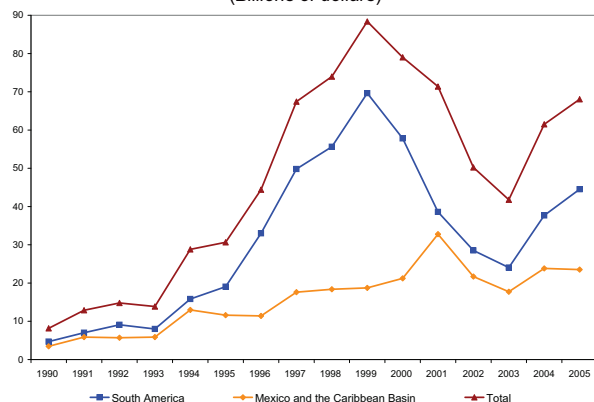
Around 60% of global FDI is channelled into service sectors, while a third goes to manufacturing and the remainder to natural resources. This pattern applies to both developed and developing countries, although manufacturing accounts for a slightly larger proportion of flows to the latter (UNCTAD, 2005b).

² In November 2004, the Royal Dutch/Shell Group announced the creation of a new company, Royal Dutch Shell Plc, resulting from the merger of Shell Transport and Trading Company Plc and Royal Dutch Petroleum Company. Listed on the London and Amsterdam stock exchanges, the new company has its head office in The Hague, Netherlands, and its capital structure is simpler. The operation was valued at US\$ 100 billion and the merger was completed on 20 July 2005.

2. The situation in Latin America and the Caribbean

In 2005, FDI flows to Latin America (not including financial centres) amounted to US\$ 68,046,000,000 or 11% more than the year before (see figure I.2). Following the FDI boom at the end of the 1990s and the subsequent decline at the beginning of this decade, the region seems to be displaying a less volatile pattern. In the short term, FDI in the region is expected to remain at the same levels as in the recent period, with a slight upward trend but less buoyancy than in other developing regions (UNCTAD, 2005a).

Figure I.2
LATIN AMERICA AND THE CARIBBEAN: NET INFLOWS OF FDI, BY SUBREGION, 1990-2005^a
(Billions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information from the International Monetary Fund (IMF), "Balance of Payments Statistics" [CD-ROM] and official data.

^a This does not include financial centres. The FDI figures shown correspond to inflows of FDI minus capital outflows generated by foreign investors. The figures differ from those presented in the *Preliminary Overview of the Economies of Latin America and the Caribbean*, as the latter shows the net balance of foreign investment, i.e., direct investment in the reporting economy minus direct investment abroad. Figures updated to 24 April 2006.

Factors that could affect inflows of FDI to the region include:

- **Economic growth:** GDP in Latin America and the Caribbean and the United States (the region's main investor) has continued to grow, and is expected to expand at similar rates in 2006 (ECLAC, 2005b; OECD, 2005a).
- **Commodity prices:** Demand for natural resources has increased steadily in the recent period, driven especially by China, and this has pushed commodity prices up to record levels. Companies working in related activities have thus enjoyed a substantial boost to their income, which could lead to future investments. However, the rise in the price of petroleum (which

is an input for many industries) may hurt investment in manufacturing and other branches of economic activity over the next few years.

- **Mergers and acquisitions:** Following the FDI boom recorded at the end of the 1990s, linked mainly to cross-border privatizations, mergers and acquisitions in the region, there has been a systematic decline in such flows, although an upturn has been observed in the last two years (see table I-A.1). There is also evidence that an increasing proportion of FDI is taking the form of greenfield investments (UNCTAD, 2005a).
- **Political and institutional changes:** The rationale of the economic reforms carried out in Latin American and Caribbean countries during the 1990s has been increasingly questioned in recent times. Although the reforms created the conditions for an FDI boom, the benefits did not bear out expectations. Albeit with different nuances, this is reflected in the renewal of political leaderships in many countries, which could lead to some changes in the nature of relations with TNCs (especially in the area of natural resources).
- **Business environment:** According to various global competitiveness indicators, its environment for conducting private business still places Latin America and the Caribbean at a disadvantage vis-à-vis developed countries and some emerging economies in Eastern Europe and the Asia-Pacific Region. This is to the detriment of the region as regards locational investment decisions (see box I.1).

In 2005, Latin America and the Caribbean saw the continued consolidation of a new pattern of FDI. As far as the source of capital is concerned, the United States has become more entrenched as the largest investor, accounting for almost 40% of total investments (see figure I.3 and table I-A.2). Spain, which was a key country during the FDI boom, has slipped to third place, providing only 6% of total inflows. In second position is the Netherlands, which represents almost 12% of FDI in the region.³ Although not fully reflected in the figures, an increasingly significant proportion of investment is coming from other countries in the region, in the form of capital flows linked to the operations of trans-Latin corporations (see table I-A.1 and chapters III to VI). In terms of the target sectors for FDI inflows, manufacturing has increased its share at the expense of services, although these are still preferred by foreign investors (see figure I.4 and table I-A.3).

³ A degree of caution must be exercised regarding these figures, since many companies use their subsidiaries in the Netherlands to redirect financial resources to other destinations around the world in order to lock into tax benefits.

Box I.1

THE BUSINESS ENVIRONMENT IN LATIN AMERICA AND THE CARIBBEAN

A suitable business environment is crucial for decision-making in the private sector. Competitively speaking,^a the conditions prevailing in Latin America and the Caribbean in terms of financial systems, intellectual property rights, taxes, bureaucratic hurdles, commercial codes and State intervention in the economy, among other factors, place Latin America and the Caribbean far behind the developed countries and the Asia-Pacific region. The indicators used to assess the quality of the country's business environment include the following:

- Index of Economic Freedom (Heritage Foundation): This measures 50 independent variables divided into 10 broad factors of economic freedom, such as trade policy, tax burden, government intervention, monetary policy, foreign investment, banking, wages and prices, regulation, rights of ownership and degree of market informality.
- Doing Business (International Finance Corporation): This measures ease

of conducting business, based on a number of variables that are important for business start-ups, including the simplicity of company registration procedures, licensing arrangements, property registration and credit application; labour conditions; tax payment; and facilities for closing a business.

- Corruption Perceptions Index (Transparency International): A tool based on expert assessments and opinion surveys, aimed at measuring the perceived level of corruption in each country. It does not provide an objective measure of corruption based on quantifiable dimensions, but is merely a subjective gauge of opinions about a country's degree of corruption.
- Globalization Index (A. T. Kearney): An index that assesses performance in four key components of global integration. Economic integration is measured by trade and FDI inflows and outflows. Technological connectivity is gauged

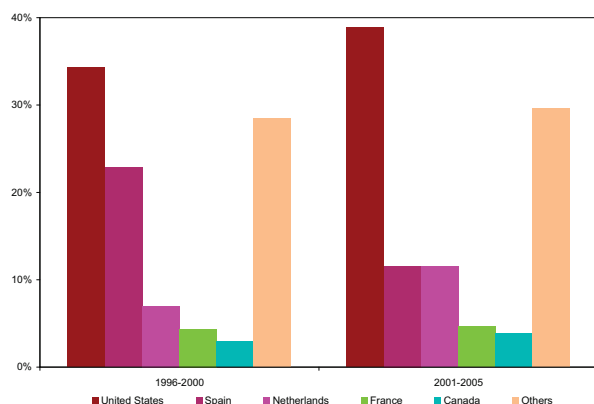
by the number of Internet users. Political engagement includes each country's membership in international organizations and involvement in United Nations peacekeeping missions. Personal contact tracks aspects such as international travel and tourism, international telephone traffic, and so on.

Latin American and Caribbean countries tend not to score very highly as regards any of the indicators mentioned, which places them lower in the respective index ranking than some countries in other developing regions. Only Costa Rica and Chile score well on certain indicators, whereas the other countries figure in the bottom two quintiles of each index. The region is facing a major challenge: attracting quality FDI not only requires clear national development objectives matched by a concomitant promotion effort (see chapter II), but also a culture and institutional environment in which national or foreign investors can readily set up and successfully run productive concerns.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information from The Heritage Foundation [online] <<http://www.heritage.org>>; International Finance Corporation, "Doing Business Database" [online] <<http://www.doingbusiness.org>>; Transparency International [online] <<http://www.transparency.org>> and A. T. Kearney [online] <<http://www.atkearney.com>>.

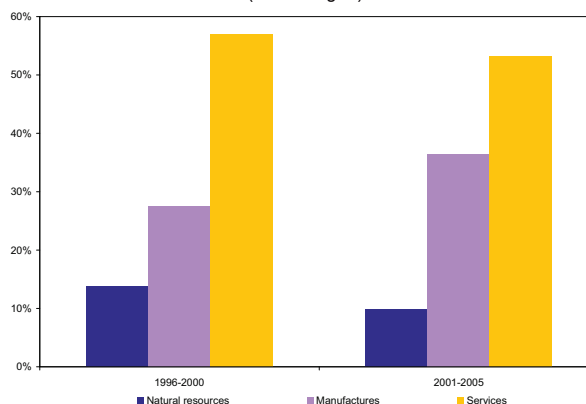
^a The concept of competitiveness refers chiefly to institutional conditions for setting up in business within a given country or region. Countries with more robust institutions, that facilitate business, are more competitive from this perspective. This should not be confused with the concept of international competitiveness, which refers to the region's share of world imports.

Figure I.3
LATIN AMERICA AND THE CARIBBEAN: FDI BY COUNTRY
OF ORIGIN, 1996-2005
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official statistics.

Figure I.4
LATIN AMERICA AND THE CARIBBEAN: FDI BY TARGET
SECTOR, 1996-2005
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official statistics.

A number of points warrant discussion in relation to the main recipient countries. First, Mexico was the country of choice for foreign companies in 2005, while Brazil continued in second position. Mexico's FDI inflows have been remarkably stable and voluminous, with a significant proportion going to manufacturing. Second, there has been a notable upturn in inflows to Colombia, mostly owing to the sale of the Bavaria brewery to SABMiller (see chapter V). Third, there has been a significant recovery in flows to the Bolivarian Republic of Venezuela and, to a lesser extent, to Peru. The fourth point is that Chile has continued to be a popular country for FDI, thanks to the stability and buoyancy of its economy. Generally speaking, the performance of the smaller economies has been relatively stable and has not exhibited any major variations.

Over the last few years, South America has received larger volumes of FDI in absolute terms than Mexico and the Caribbean Basin. Flows to South America have been less stable, however: annual average FDI inflows increased fivefold, from US\$ 11.8 billion in 1991-1995 to US\$ 53.2 billion in 1996-2000, only to fall back to US\$ 34.7 billion thereafter. Investment in Mexico and the Caribbean Basin, on the other hand, doubled from US\$ 8.4 billion in the first of these periods to US\$ 17.5 billion in the second, and has held steady at around US\$ 23.9 billion since then. However, the ratio of foreign investment to GDP has tended to converge in the two subregions, although the Caribbean countries differ in this since, as small economies, they tend to have a higher FDI-GDP ratio. Between 2001 and 2005, investment in South America ranged from 0.8% of GDP (Guatemala) to 6.1% (Chile). In Mexico, the average was 2.8% of GDP. In 2005, Colombia was the region's largest recipient of FDI in relation to GDP, with 8.4%. After Colombia and not including the Caribbean countries, Chile, Jamaica and Panama have received the largest amounts of FDI in relation to their GDP in the past year.

As FDI has become more stable in terms of amounts and geographical distribution, its relative significance within national economies has also become fairly constant.

Be that as it may, the Latin American and Caribbean region continues to receive a shrinking proportion of global FDI flows. The region took in 12% of global inflows during the 1980s, compared with 10% in the 1990s. Since 2000, it has received just over 8% worldwide FDI. This could indicate that the region is being gradually sidelined from FDI in the current pattern of globalization.

(a) Foreign direct investment in Mexico, Central America and the Caribbean

Net inflows of FDI to this subregion amounted to US\$ 23.52 billion in 2005. This was 1.3% lower than the previous year, reflecting a decline in inflows to Mexico (see table I.2).

Table I.2
MEXICO AND THE CARIBBEAN BASIN: NET INFLOWS OF FDI,
1991-2005^a
(Millions of dollars)

	1991- 1995 ^b	1996- 2000 ^b	2001- 2005 ^b	2004	2005 ^c
Mexico	6 804.6	12 608.8	18 805.8	18 244.4	17 804.6
Central America	659.2	2 340.2	2 241.2	2 728.8	2 701.0
Costa Rica	257.1	495.2	583.5	617.3	609.2
El Salvador	19.0	309.5	373.0	465.9	477.0
Guatemala	93.5	243.7	203.9	154.7	167.8
Honduras	42.2	166.1	219.7	293.0	190.0
Nicaragua	37.9	229.2	194.2	185.6	230.0
Panama	209.4	896.5	666.8	1 012.3	1 027.0
Caribbean	945.1	2 519.1	2 857.9	2 861.2	2 971.3
Jamaica	126.1	349.6	603.8	601.6	601.6
Dominican Republic	227.0	701.5	853.2	758.4	898.8
Trinidad and Tobago	308.3	681.5	681.7	600.0	600.0
Others	283.7	786.5	719.1	901.2	870.9
Total	8 408.9	17 468.1	23 904.9	23 834.3	23 476.9

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information from the International Monetary Fund (IMF) and official figures.

^a This does not include financial centres. FDI inflows are equal to inflows of FDI minus capital outflows generated by foreign investors. The figures differ from those presented in the *Preliminary Overview of the Economies of Latin America and the Caribbean*, as the latter shows the net balance of foreign investment, i.e. direct investment in the reporting economy minus direct investment abroad.

^b Annual average.

^c Data available as of 24 April 2006.

In 2005, FDI flows into Mexico continued to go mainly to manufacturing.⁴ Much of manufacturing FDI in Mexico is channelled into the maquila industry, which depends heavily on economic performance and industrial activity in the United States. The economic upturn in its northern neighbour has therefore impacted positively on investment in Mexico. According to figures from the Mexican Ministry of Economic Affairs, manufacturing accounted for 58% of total FDI inflows, and services, 41%. Two thirds of that FDI comes from the United States, with Spain—which played a major role in restructuring the banking sector—following far behind with 10% (see table I-A.2).

The automotive subsector has been the fastest-growing and has received much of total FDI. The leading vehicle assembly companies (Ford Motor Company, General Motors, Nissan Motor Company, Volkswagen and DaimlerChrysler) and several parts manufacturers have invested in expanding and modernizing plants

⁴ Exceptionally, inflows into Mexico between 2001 and 2003 were channelled mainly into the services sector, specifically reflecting major changes in ownership of the largest local banks.

and introducing new models with a view to increasing production capacity and improving the range and quality of products. Investment by Japanese companies is beginning to gather momentum following the conclusion of a free trade agreement between Mexico and Japan aimed at diversifying the market and reducing Mexico's dependency on the United States market (ECLAC, 2005c, Mortimore and Barron, 2005). Prominent examples are Nissan's US\$ 1.3 billion investment to produce a new compact model for sale in the United States and Toyota's US\$ 160 million invested to expand its first Mexican assembly plant, which makes the Tacoma pick-up model in Tijuana. Lastly, the Bridgestone tyre company invested US\$ 220 million in setting up a plant in Nuevo León, with 95% of its production destined for export to Canada and the United States. This plant is the first outside Japan to incorporate the Bridgestone Innovative and Rational Development (BIRD) production system, which is distinguished by its fully automated production process.

In other manufacturing activities, the Argentine conglomerate Techint purchased 42.5% of the Hylsamex steel company from the local Alfa group, for US\$ 2.56 billion. This acquisition fitted into Techint's strategy of building up its position as a major producer of flat and long steel in Latin America (see chapter IV). In addition, Electrolux of Sweden transferred its operations in Michigan, United States, to Juárez, where it opened its plant in mid-2005 after a \$ 100 million investment. The Juárez plant will make refrigerators for export to North America, Europe and the rest of Latin America.

In the services sector, a number of developments warrant mention in the retail segment, in which Wal-Mart was consolidated as the leading chain. The United States company invested over US\$ 740 million to open 70 new stores and refurbish others. In March 2005, the French chain Carrefour announced its intention to pull out of Mexico and sold its assets to Chedraui, a local operator. This was part of a plan launched the year before to shed non-strategic or underperforming assets.

In 2005, FDI in the Caribbean Basin⁵ amounted to US\$ 5.67 billion, which represented a 1.5% increase over the previous year. Nonetheless, the subregion continues to receive high levels of FDI, outstripping even the

volumes recorded in the second half of the 1990s (see table I.2). Most of this FDI has gone to manufacturing. Attracted by the tax incentives and relatively cheap labour available in the Caribbean Basin, foreign companies have established bases for assembling goods that range from clothing to microelectronics. Many of the subregion's countries have thus become export platforms (with varying degrees of sophistication), supplying the United States market in particular.

At the beginning of the new decade, the downturn in the United States economy deprived the subregion of major investment projects. Especially after the recovery of the United States economy, however, most manufacturing investment has consisted of reinvestment of profits, aimed at expanding the production capacity of firms operating in export-processing zones. In 2005, one such was investment by Componentes Intel in Costa Rica (Central Bank of Costa Rica, 2006). In addition, the Dominican Republic–Central America–United States Free Trade Agreement (CAFTA-DR) could boost efficiency-seeking investment geared towards the United States market.

In contrast with the slowdown in FDI in manufacturing, investment in services was particularly buoyant in the Caribbean Basin, as two retail and telecoms giants in the Americas expanded their presence in Central America. First, the United States retail chain Wal-Mart purchased 33% of the Central American Retail Holding Company (CARHCO)⁶ from Royal Ahold of the Netherlands, which gave it an instantaneous, significant presence in Guatemala, El Salvador, Honduras, Costa Rica and Nicaragua. Second, in December 2004 the Mexican trans-Latin América Móvil acquired a further 42% of Compañía de Telecomunicaciones de El Salvador (CTE)⁷ for US\$ 295 million —bringing its share in the company to 94%— and announced a US\$ 160 million investment plan to consolidate its presence in the region.

FDI in the Caribbean subregion strongly reflects the buoyancy of petroleum activity in Trinidad and Tobago. In mid-2005, Repsol-YPF acquired three oilfields (Teak, Samaan and Pou) and one gasfield (Onyx) from British Petroleum (BP) in Trinidad and Tobago, at a cost of US\$ 229 million.⁸ Repsol-YPF plans to invest

⁵ The Caribbean Basin encompasses the countries of the Caribbean and Central America, and Panama.

⁶ Royal Ahold formed a joint venture with La Fragua of Guatemala, which owned operations in El Salvador and Honduras. It later expanded the partnership to include Corporación de Supermercados Unidos (CSU) of Costa Rica, thereby creating the subregion's largest supermarket chain, Central American Retail Holding Company (CARHCO). Thus, Royal Ahold gained a 33.3% share in CARHCO which, in turn, owned 85% of La Fragua and 100% of CSU. In 2005, CARHCO operated 363 stores: 120 in Guatemala, 57 in El Salvador, 32 in Honduras, 124 in Costa Rica and 30 in Nicaragua.

⁷ In 2003, América Móvil bought France Telecom's share in CTE.

⁸ Following the completion of this US\$ 229 million transaction, the State-owned Petroleum Company of Trinidad and Tobago Limited (PETROTRIN) is to acquire a 15% share in the fields. The transaction is subject to approval by the Government of Trinidad and Tobago (Repsol-YPF news [online], 19 July 2005).

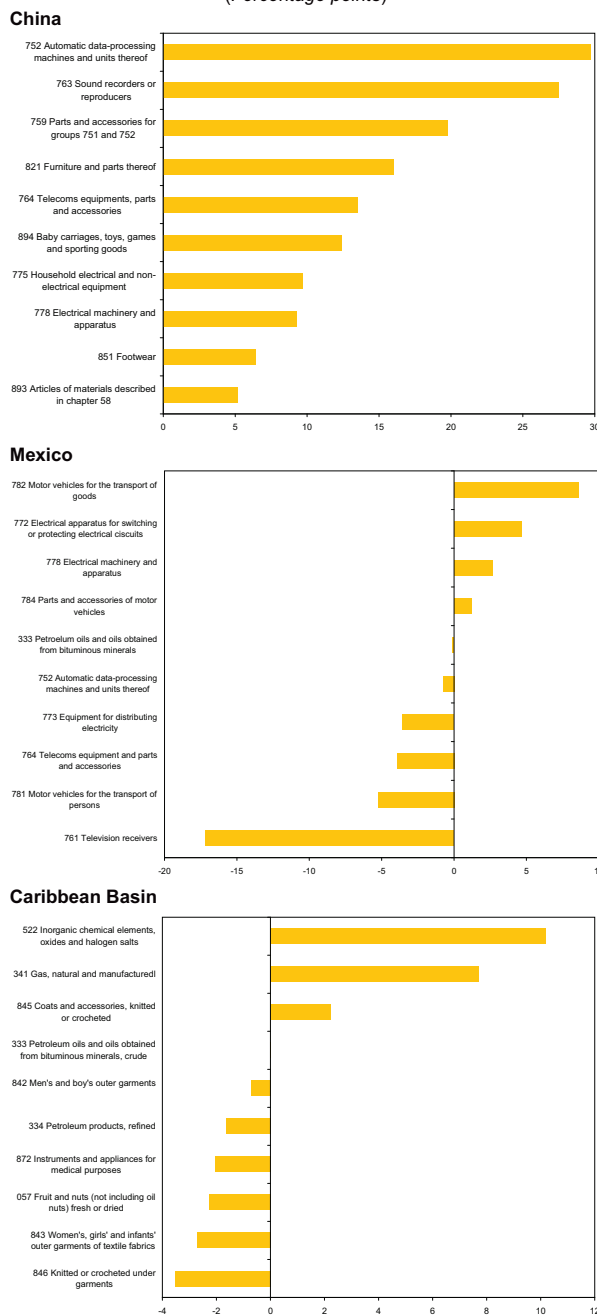
US\$ 500 million in developing oilfields and natural gas deposits up to 2025 (Repsol-YPF news, 19 July 2005). In December 2005, Repsol-YPF announced the coming on stream of the world’s largest liquefied natural gas plant, Train 4 of the Atlantic LNG project.⁹ This US\$ 1.2 billion investment makes Trinidad and Tobago the top liquefied natural gas exporter to the United States. The Spanish company has thus consolidated its leadership in the Caribbean hydrocarbons sector, in accordance with the growth strategy set out in its Strategic Plan 2005-2009, which included upstream exploration and drilling among its top priorities. Repsol-YPF plans to invest more than US\$ 2.2 billion in the Caribbean subregion during the period covered by its Strategic Plan, with US\$ 1.25 billion of this amount earmarked for Trinidad and Tobago (Repsol-YPF, news [online], 16 December 2005).

In addition to the major projects under way in the hydrocarbons sector, new investments have been announced in other areas of activity. In September 2005, ESSAR of India signed an agreement with the National Energy Corporation of Trinidad and Tobago to build an integrated iron and steel complex, with an investment estimated at US\$ 1.2 billion (*India Infoline News*, 12 September 2005, <http://www.indiaonline.com>). This investment will be used, among other things, to produce flat steel for manufacturing tubes, in what will represent a major step forward for the local steel industry (*The Trinidad Guardian*, 28 September 2005, <http://www.guardian.co.tt>).

As mentioned earlier, because of the way Mexico and the Caribbean Basin have developed as export platforms, the pattern of their FDI inflows is largely determined by the performance of the United States economy, particularly its manufacturing activity. Recently, the structural vulnerability arising from this almost exclusively single-market focus has been worsened by the emergence of China as an extremely powerful competitor.

Between 2000 and 2004, Mexico’s share in United States imports dropped from 10.9% to 10.3%, while the share of Caribbean Basin countries has remained practically unchanged at around 1.8%. This is in contrast to the proportion accounted for by China, which climbed from 8.6% to 13.8% in that period. In other words, while Mexico’s share fell by 0.6 percentage points, the Caribbean Basin’s remained the same and China’s rose by 5.2 percentage points. However, a closer examination of those countries’ 10 main export products to the United States reveals an even more alarming pattern (see figure I.5).

Figure I.5
CHINA, MEXICO AND CARIBBEAN BASIN: CHANGE IN MARKET SHARE OF 10 MAIN EXPORT PRODUCTS^a TO THE UNITED STATES, 2000-2004
 (Percentage points)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations, Commodity Trade Database (COMTRADE), 2005.

^a According to the Standard International Trade Classification (three-digit SITC code, Rev. 2). Main ten exports to the United States by each of these countries or group of countries in 2004, and the variation in their share in relation to 2000.

⁹ The partners in Atlantic LNG are Repsol-YPF (22%), BP (38%), BG Group (29%) and the State-owned National Gas Company of Trinidad and Tobago (11%). Repsol-YPF also has a 20% share in Train 1 of the Atlantic LNG liquefaction plant and a 25% share in each of Trains 2 and 3 (Repsol-YPF news [online], 16 December 2005).

- Mexico has lost market share in 6 of the 10 product groups, most of them in medium- or high-technology segments.
- Like Mexico, the Caribbean Basin countries have lost market share in 6 of their own 10 main exports (mainly natural resources and low-technology manufactures).
- China, on the other hand, has increased its market share in all 10 of its main export products to the United States (all non-resource-based manufactures).

Challenging times therefore lie ahead for Mexico, Central America and the Caribbean, since their strong dependence on the United States market is now exacerbated by tough competition from China. These countries should therefore deepen their capacity for attracting FDI, not only by ensuring they remain cost-competitive, but also by better harnessing the advantages of proximity and of their trade agreements with the United States and other world regions.

(b) Foreign direct investment in South America

In 2005, FDI flows to South America amounted to US\$ 44,525,400,000 which was 18% higher than the previous year (see table I.3). The increase was largely accounted for by investment inflows to the Andean Community, excluding Bolivia, which soared by 120% over the previous year. The total for MERCOSUR came to US\$ 20,398,500,000 or 10.6% less than in 2004.

The drop in FDI flows to Brazil does not represent a dramatic change in the recent pattern. Indeed, the year before had been atypical, because of an especially large inflow caused by the acquisition of the trans-Latin Ambev by the Belgian company Interbrew (see chapter V). In 2005, FDI in Brazil amounted to US\$ 15.2 billion, with no large-scale acquisitions and a higher proportion going to new projects. As far as the origin of FDI is concerned, the European Union continued to be the largest bloc investor and the United States the main single country investor in Brazil. Mexico accounted for a larger share than before, mainly thanks to telecoms operations (see table I-A.2 and chapter VI). In terms of target sectors, manufacturing regained a prominent place among FDI preferences, since it attracted almost as much as services, which had dominated the agenda of foreign investors for almost a decade (see table I-A.3).

The retail trade industry has continued to consolidate with the emergence of a new major player: the United States company Wal-Mart, the world's largest retail corporation. Wal-Mart has recently increased its hitherto small presence in the Brazilian market by acquiring assets from some of its main global competitors. In March 2004, it bought the Bompreço chain from Royal Ahold of the

Netherlands for about US\$ 300 million, thereby gaining 118 stores in the north-east of Brazil. In December 2005, Wal-Mart paid US\$ 750 million for the Brazilian operations of Sonae of Portugal. As a result, Wal-Mart has become Brazil's third-largest retail chain, with 295 stores in 17 of the 26 States, behind the French chain Carrefour and the Pão de Açúcar group, which is partly owned by the French chain Casino (*The Wall Street Journal Americas*, 15 December 2005).

Table I.3
SOUTH AMERICA: NET FDI INFLOWS, 1991-2005^a
(Millions of dollars)

	1991- 1995 ^b	1996- 2000 ^b	2001- 2005 ^b	2004	2005 ^c
MERCOSUR	6 445.2	36 757.1	19 883.1	22 822.1	20 398.5
Argentina	3 781.5	11 561.1	2 980.6	4 273.9	4 662.0
Brazil	2 477.4	24 823.6	16 480.7	18 145.9	15 066.3
Paraguay	103.8	185.1	53.9	69.9	69.9
Uruguay	82.5	187.2	367.9	332.4	600.3
Andean Community	3 685.5	10 746.7	9 701.1	7 674.0	16 918.5
Bolivia	158.4	780.2	271.1	62.6	-279.6
Colombia	911.9	3 081.1	3 946.2	3 117.0	10 192.1
Ecuador	368.1	692.4	1 370.1	1 160.3	1 530.2
Peru	1 304.2	2 000.8	1 794.0	1 816.0	2 518.8
Venezuela (Bolivarian Republic of)	943.0	4 192.2	2 319.8	1 518.0	2 957.0
Chile	1 666.2	5 667.0	5 087.7	7 172.7	7 208.5
South America	11 797.0	53 170.7	34 671.9	37 668.8	44 525.4
Total - Latin America and the Caribbean	20 205.8	70 638.9	58 586.2	61 503.2	68 046.3

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information from International Monetary Fund (IMF) and official figures.

^a This does not include financial centres. FDI figures are equal to inflows of FDI minus capital outflows generated by foreign investors. The figures differ from those presented in the *Preliminary Overview of the Economies of Latin America and the Caribbean*, as the latter shows the net balance of foreign investment, i.e., direct investment in the reporting economy minus direct investment abroad.

^b Annual average.

^c Data available as of 24 April 2006.

FDI in Argentina was up by 9.1% in 2005 to stand at US\$ 4.662 billion (see table I.3). Against a backdrop of stabilization, expansion of exports and economic growth, the country's investment prospects have improved substantially and some companies now view Argentina as an opportunity to expand their international presence. One example is the Brazilian conglomerate Camargo Corrêa, which bought cement producer Loma Negra for US\$ 1.025 billion, thereby gaining control of 48% of the Argentine cement market. This share could increase as the group implements its announced investment plans, which amount to some US\$ 100 million (see chapter IV).

Domestic demand has rallied, prompting some manufacturing firms with a strong presence in the country to expand their production capacity in order to supply the domestic market and boost exports. The automobile sector has staged a strong recovery, following contractions in 2001 and 2002. Since 2003, automobile production has grown by 75%, to 300,000 units in November 2005. This

buoyancy is reflected in new projects announced by some of the main assembly plants: Peugeot Citroën will invest US\$ 125 million in making new export models and DaimlerChrysler will spend some US\$ 50 million on the production of a Mercedes Benz utility vehicle, which will be sold exclusively to non-Latin American markets.

Investment in the petroleum sector has been rather flat, owing in part to a 45% levy on oil exports, which severely erodes the profits that companies would otherwise stand to gain from the higher international prices for crude. In order to encourage investment in this sector, in June 2005 the Government launched its 2004-2008 Energy Plan, which provides for preferential tax treatment for new investments in oil and natural gas. In addition, the Government has continued with the deregulation of the natural gas market steered by the Ministry of Energy. This involves decontrolling the prices that producers charge to large consumers, who can thus negotiate prices directly, while distributors still sell at controlled rates. Lastly, the Venezuelan State-owned company *Petróleos de Venezuela* (PDVSA) has announced that it will buy the oil refining and distributing company *Rutilex Hidrocarburos Argentinos Sociedad Anónima* (RHASA) and the Argentine distribution network of the Uruguayan State-owned company *Administración Nacional de Combustibles, Alcohol y Portland* (ANCAP). PDVSA is also planning to build a gas pipeline through Bolivarian Republic of Venezuela, Brazil and Argentina. This project will help to capitalize on existing synergies to increase electricity integration in the region, for which the diversification of sources and economies of scale will be particularly important in the long term (ECLAC, 2005c).

Although a degree of normality now prevails, a number of conflicts remain between the Government and TNCs, especially in the utilities sector. In 2005, the French company *Suez*, a majority shareholder in the drinking water and sanitation company that services several Argentine provinces (including Buenos Aires), announced its intention to pull out of Argentina, having been unable to reach an agreement with the Government on rates (the company followed through on this decision in March 2006). *Électricité de France* followed suit and, in both cases, the intention is for local investors to take over the operations (see box I.2).

Uruguay continued to receive relatively significant FDI inflows in 2005. In the period since 2000, its inflows have been almost twice as high as during the regional FDI boom (see table I.3). This is partly attributable to the Government's efforts to improve the business environment in the country. The pulp and paper sector has been a prominent destination for investment flowing into the country. The project spearheaded by *Botnia* of Finland to build a wood pulp plant near the city of Fray Bentos, on the banks of the Uruguay river, is now in the implementation phase. With an investment of US\$ 1.1 billion, this is the biggest industrial investment in the history of Uruguay and Finland's largest private-sector investment abroad (*Botnia*, 2005). The Spanish company *Ence* has launched a similar project, also on the banks of the Uruguay river, worth a total projected value of US\$ 728 million (*Papermarket*, 2005). These projects are, however, fiercely opposed by a number of local and Argentine groups, which protest they may contaminate the river and hurt tourism, one of the area's foremost economic activities. In March 2006, the Governments of Argentina and Uruguay agreed to request a goodwill gesture, in which road blocks would be lifted in exchange for a 90-day suspension of plant operations to conduct an independent environmental impact assessment (*Diario Financiero*, 23 March 2006).

In 2005, Chile received US\$ 7.208 billion in FDI inflows, which was equivalent to a 0.5% increase over the preceding year. The country is continuing to evidence a level of stability that is welcomed by foreign investors. A major portion of the inflows recorded are reinvestments. The main FDI-receiving sectors in Chile were mining, transport and communications, and electricity. Infrastructure concessions (motorways, airports, ports, and so on) have also generated large FDI inflows.¹⁰ In 2005, the different concession projects brought in investment of close to US\$ 1 billion (*Chile Investment Review*, February 2006, p. 8). Prominent in the electricity sector are the investments carried out by the Australian company *Pacific Hydro*. This company is going ahead with the construction and operation of the 155 MW *La Higuera* hydroelectric plant, which is valued at US\$ 270 million. This project is part of an active investment plan, which includes the construction of eight power plants with a total capacity of 1,000 MW over a period of ten years.

¹⁰ Between 2000 and 2006, the Ministry of Public Works of Chile brought in a total of US\$ 7 billion in investments in 50 concessions to build and operate infrastructure projects (*Chile Investment Review*, February 2006, p.8).

Box I.2

ARGENTINA: NEW OPPORTUNITIES FOR LOCAL INVESTMENT IN UTILITIES

Following the crisis of 2001 and 2002, the Argentine economy is showing clear signs of an upturn, as evidenced by high rates of growth and investment, rallying employment and wages, sound fiscal accounts and the normalization of relations with international lending institutions. TNCs have again begun to view Argentina as a target for foreign direct investments. Utility companies, however, are still feeling the effects of the crisis and of the devaluation that ended the peso's one-to-one dollar parity. At the beginning of 2002, rates were converted into local currency at a one-to-one parity and then frozen. Consequently, these companies saw their revenues slashed by the devaluation. Rate rises were made conditional upon renegotiation of the contracts signed in the 1990s and fulfilment of investment plans. Little headway has been made in such negotiations, however, because of the socio-political implications of a rate rise. Several of the firms affected brought cases against Argentina before international bodies, such as the World Bank's International Centre for Settlement of Investment Disputes (ICSID), claiming entitlement to damages arising from the measures taken by the Government. In response, the Government altered its strategy and made the withdrawal of complaints brought before ICSID a condition for renegotiating contracts. At the same time, the Argentine Government approached the Governments of France and Spain (the countries of origin of most of the claimant firms), urging them to intervene on its behalf. The firms have reacted in different ways. Some companies that have strategic interests in the country have found it to their advantage to withdraw their complaints. This is the case of Edesur, AES Corp., Pioneer National Resources, Camuzzi, Gas Natural BAN, Edenor and Unysis. Conversely, firms that opted to pull out of Argentina have persisted with their suits, as have companies that see the legal action as a form of defence (Mortimore and Stanley, 2006). Local investment groups better placed to renegotiate contracts or

obtain financing have emerged to take over the operations left by TNCs.

Suez of France is one of the firms that chose to pull out. In September 2005, Suez announced its withdrawal from the Aguas Argentinas concession, a drinking water and sanitation company that serves some 11 million people in the Buenos Aires metropolitan area. Aguas Argentinas was the largest concession operated by Suez anywhere in the world. In negotiations lasting several years, Aguas Argentinas (of which Suez controlled 40% and Aguas de Barcelona of Spain, 25%) lobbied for a 60% rate hike in order to finance its infrastructure investment plans. The Government offered 16%, along with resources for the company's investment plans. Aguas Argentinas demanded in response that the Government also assume part of its liabilities, including debt of US\$ 650 million. The Government finally agreed to the rate hike, but not until 2007, and refused to assume the firm's loan liabilities, prompting Suez's eventual decision to withdraw from Aguas Argentinas. In May 2005, Suez had pulled out of its Aguas de Santa Fe concession too, following the failure of negotiations that also involved claims and counter-claims for rate hikes and breach of investment commitments, respectively. Unlike these two cases, Suez will not be giving up its Aguas Cordobesas concession, since the venture has performed well and negotiations with the provincial government have been successful.

Both the concessions Suez has exited will be left in the hands of local firms. The Aguas de Santa Fe operations will be taken over by the provincial government and later reprivatized. In the case of Aguas Argentinas, a private Argentine group is interested in assuming control. In March 2006, the Argentine Government finally rescinded the contract with Suez; the State has now assumed control of the utility through a new corporation called Agua y Saneamiento Argentina, S.A. The Government of France lodged a vehement complaint in response to this development (*El Clarín*, 23 March 2006).

Électricité de France (EDF) had a similar experience to its compatriot firm Suez. EDF owns Edenor, an electricity company which supplies the northern part of Buenos Aires. In this case, too, the negotiations revolved around a hike in rates that have been frozen since 2002. The Government refused to agree to any such hike and Edenor's financial performance suffered. Stating its intention of focusing on its European operations, EDF sold off 65% of Edenor, in which it had a 90% controlling interest, to the local investment group Dolphin, for the sum of US\$ 100 million. Following the sale, EDF now maintains a 25% interest and will provide technical assistance to the new owners over the next five years. Dolphin has reached an agreement with the Government that includes an increase in rates in exchange for the withdrawal of the complaint before ICSID and the provision of soft Government loans for new investments.

The case of Telefónica of Spain is rather different. This company, which controls the operator Telefónica de Argentina, brought a suit before ICSID for US\$ 2.8 billion, the highest ever brought against Argentina. As in the previous cases, Telefónica is claiming damages caused by the freezing of rates and the impact of devaluation. However, parallel negotiations being conducted with the Government suggest that the suit will be withdrawn once an agreement has been reached on fixed telephony charges and a regulatory framework is established for the sector.

In short, Argentina's economic performance is improving, although negotiations are continuing with utility companies over the alteration of rate structures. The outcomes have been varied and are not yet definitive. Telefónica of Spain and Dolphin, the controlling shareholder in Edenor, have withdrawn or are likely to withdraw their complaints before ICSID. Others, such as Suez and EDF, have opted to pull out, leaving the task of pursuing the negotiations to the new investors.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

In the telecoms subsector, Endesa sold its mobile telephone subsidiary Smartcom to América Móvil de Mexico for US\$ 472 million. This operation gives one of Latin America's telecoms leaders access to the Chilean market, which is largely dominated by Telefónica of Spain (the other regional leader) and by ENTEL, whose respective market shares may be affected as a result.

TELMEX has obtained a concession for operating the local wireless loop service in the country.

In addition to the electricity subsector, medium-term investments will go chiefly to mining, especially copper, thanks to new investment options opened up by the free trade agreement signed recently with China, Chile's second largest trading partner. Of particular interest is

the agreement between the Chinese mining company Minmetals and Chile's State-owned Codelco, under which Minmetals will pay Codelco US\$ 2 billion for a long-term copper supply. Codelco, for its part, has given Minmetals an option to buy a minority shareholding in the company that will work the Gaby deposit, should Codelco bring that project on stream.

Chile has developed a good position as a target for investments in "new services" (ECLAC, 2005c). The Chilean Association of Call Centres hopes to triple this segment's revenues and employment by 2008. It also plans to bring together the public and private sectors in an effort to make Chile one of the world leaders in this business, on a par with India and Costa Rica (Cinver, 2005). The US\$ 23 million purchase of Comicrom, a Business Process Outsourcing (BOP) company, by Tata Consultancy of India was a significant transaction in this regard in 2005.

FDI in the Andean Community, which comprises the Bolivarian Republic of Venezuela, Bolivia, Colombia, Ecuador and Peru, increased by more than 120% in 2005, to US\$ 16,918,500,000. This reflected an increase in all the countries of the Community, except Bolivia, which has recorded successive declines in FDI since 2003.

Colombia is the leading FDI recipient in the Andean Community, with an amount in excess of US\$ 10 billion. Much of this—31% in 2005—was invested in the extraction of natural resources (see table I-A.3). The government's efforts were geared mainly towards the hydrocarbon sector, seeking to attract investments that could expand reserves and hence increase Colombia's energy independence. The stability and security that the government has sought to guarantee foreign investors has generated a virtuous circle around the hydrocarbon sector (Coinvertir, 2005). Indeed, a sound business environment, together with the continuing presence and new development plans of TNCs in the country, is Colombia's best advertisement and accounts for its status as one of the few Latin American and Caribbean countries that have shown a strong rate of FDI growth in the present decade. Consequently, numerous companies invested in oil and natural gas exploration and production during the first half of 2005, running up a total of over US\$ 500 million. The largest transaction, however, was in the brewing industry, where the South African firm SABMiller completed the acquisition of Bavaria in October. This operation, worth US\$ 7.806 billion, will place it among the top 10 beverage companies in the world (see chapter V). In the tobacco sector, the purchase of Coltabaco by Philip Morris, for US\$ 300 million, was the largest business deal transacted on the Colombian stock exchange.

Abundant natural resources have attracted foreign investors to the other Andean Community countries too.

In Ecuador, the largest operation was led by a Chinese company, China National Petroleum, which formed the conglomerate Andes Petroleum and bought the Canadian firm EnCana's crude oil reserves and pipelines in Ecuador. The acquisition, valued at US\$ 1.42 billion, is part of China's strategy to secure energy reserves in different parts of the world. Andes Petroleum has access to proven reserves of 143 billion barrels of oil and a 36% share in a pipeline that transports 450,000 barrels per day.

In Peru, the operations of mining company Southern Peru Copper Corp, a subsidiary of the trans-Latin Grupo México, were merged with another group subsidiary, Minera México (see chapters III and IV). The merger is valued at US\$ 4.6 billion and makes Grupo México the holder of the second largest copper reserves in the world after Chile's State-owned Codelco. The hydrocarbon subsector in Peru will maintain the intense activity it has seen in recent years, thanks to the Camisea natural gas project. The Peruvian State and Perú LNG, the consortium that operates the oilfield, signed an agreement officially launching the Camisea II project, which involves an investment of US\$ 3.3 billion. The first step will be to build a liquefaction plant for natural gas, which will then be shipped and exported. The first plant of its kind in Latin America, this plant will entail a US\$ 1.3 billion investment. In addition, US\$ 1.2 billion will be invested in expanding and developing new drilling sites and in extending the gas pipeline to the coast. The remaining US\$ 800 million will be invested in the transport of liquefied natural gas to the international market.

Investment in the oil subsector in the Bolivarian Republic of Venezuela has been influenced by the high prices of crude oil and the Government's efforts to secure larger benefits from this development. At the end of 2005, the Government started to apply the 2001 Hydrocarbon Act more strictly. This Act prohibits private firms, whether local or foreign, from owning a majority shareholding in a deposit. Consequently, the Government took control of 32 extraction fields, which had been in the hands of private companies and which accounted for approximately 17% of the country's daily extraction capacity. The Government intends that private companies wishing to continue operating in Bolivarian Republic of Venezuela should sign joint ventures with PDVSA, which may control up to 70%. When the deadline for signing new contracts expired on 31 December 2005, only smaller companies and ExxonMobil (which transferred its shareholdings to Repsol-YPF) had opted to pull out of the country. The larger stakeholders, such as ChevronTexaco, British Petroleum, Royal Dutch/Shell, Petrobras and Repsol-YPF signed contracts with PDVSA since, even under the current regulations, Venezuelan oil operations remain profitable thanks to the abundance of reserves and low drilling costs.

The political and social instability prevailing in Bolivia in recent years has impacted on new investments and accounts for the constant decline in FDI inflows since 2000. In 2005, Bolivia was the only country in the region to experience net outflows of FDI, amounting to US\$ 280 million. The new Government has promised to implement far-reaching reforms in the hydrocarbons sector, where TNCs have a large presence. The reforms will be directed towards nationalization and industrialization of the resource, but the companies' existing operations will be respected under a new regulatory framework. In fact, in March 2006, President Evo Morales announced his

intention of nationalizing the country's natural resources by decree before mid-year. The nationalization decree would cover not only hydrocarbons, but also mining and water (*El Diario* [online], 23 March 2006 <http://www.eldiario.com>).

In the wake of the FDI upturn that followed a period of turbulence, the subregion is now faced with a situation in which new political leaderships could change relations between countries and TNCs, with negative implications for some types of investment, due to the legal uncertainty generated by shifts in the "rules of the game".

B. Presence of TNCs among the region's major firms¹¹

The analysis of the 500 largest companies and 200 leading export firms operating in the region provides an overview of business trends in Latin America and the Caribbean. The sales of the former stood at

46% of regional GDP in 2004 while the exports of the latter were equivalent to approximately 58% of total exports from Latin America and the Caribbean that year.

1. Regional corporate map

While the 1990s were marked by a growing presence of TNCs, reflecting unprecedented growth in FDI, especially towards the end of the decade, that trend has tended to be reversed in the present decade. Indeed, private local firms account for an increasing proportion of the largest corporations operating in the region (ECLAC, 2005c).

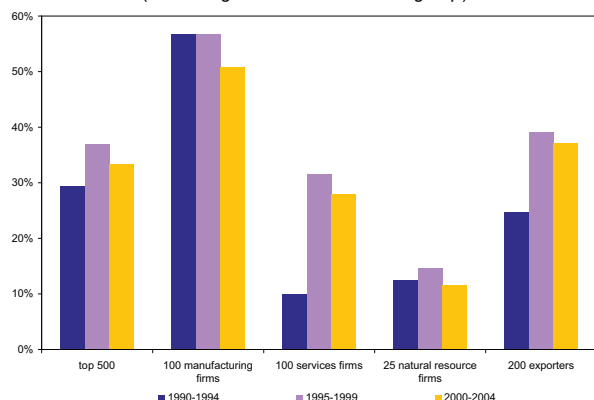
Figure I.6 shows the proportion of sales accounted for by non-financial foreign firms in different categories. In the 1990s, this proportion rose across all categories, especially among the top 500 firms, the top 200 exporters and, even more significantly, the group of the 100 largest services firms, whose share of sales increased from 10% of that category between 1990 and 1994 to 32% in the

following five-year period. The period 2000-2004 saw a generalized reduction in the sales share of transnational firms in each of the categories.

This state of affairs is hardly surprising, in view of the type of investment that TNCs usually bring into the region. Generally speaking, the investments of efficiency-seeking export firms go to the Mexican and Caribbean Basin subregion. This is in addition to investments channelled into various subsidiaries in Brazil, which have been reoriented towards export activities. The investments of utility companies largely reflect the voluminous inflows of FDI attracted by the privatization and divestments of domestic public and privately-owned firms.

¹¹ At the time of writing, sales data for the major firms were available up to 2004. This section is based on information provided by the Department of Studies and Special Projects of the journal *América economía*, supplemented with information from the reviews *Expansión* (Mexico) and *Exame* (Brazil). As on previous occasions, adjustments are made for data of subsidiaries that are duplicated in the records of the parent company. This occurs with PEMEX (Mexico) and PEMEX Petroquímica, PEMEX Refinación, PEMEX Gas and Petroquímica Básica, PEMEX Exploración y Producción, and PMI Comercio Internacional; Bunge Brasil and Bunge Alimentos and Seara Alimentos; and Wal-Mart of Mexico and Bodega Aurrerá, Sam's Club, Wal-Mart Supercenter, Superama and Suburbia.

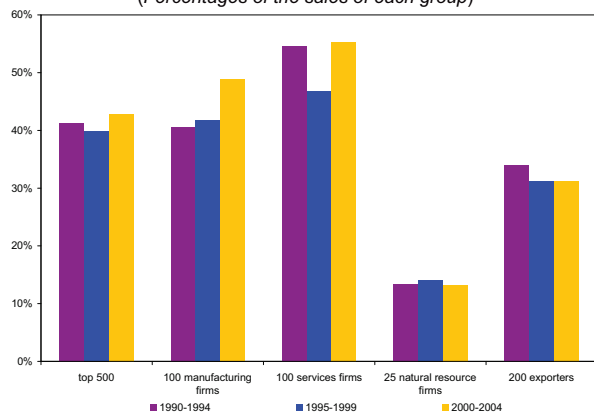
Figure I.6
**NON-FINANCIAL FOREIGN FIRMS: SALES AND EXPORT SHARE
 IN DIFFERENT CATEGORIES OF FIRM, 1990-2004**
 (Percentage of the sales of each group)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the Special Studies and Projects Department of *América economía* magazine, Santiago, Chile, 2005.

Latin American-owned firms generally gave a fairly stable performance during the past decade, as reflected in figure I.7. Local companies within the 100 largest services firms were an exception however, since their sales share dropped in the frenzy of buying and selling of local firms which, as noted earlier, resulted in a stronger presence of TNCs.

Figure I.7
**NON-FINANCIAL LOCAL PRIVATE FIRMS: SALES AND EXPORT
 SHARE IN DIFFERENT CATEGORIES OF FIRM, 1990-2004**
 (Percentages of the sales of each group)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the Special Studies and Projects Department of *América economía* magazine, Santiago, Chile, 2005.

Between 2000 and 2004, the corporate map was redrawn. In this period, the sales of private local firms grew at an average annual rate of 11%, while State enterprise sales expanded by 9%. Sales of foreign private companies, on the other hand, fell by an annual rate of 2% over the same period.

Approximately 85% of the sales of TNCs within the top 500 in Latin America are generated in Mexico, Brazil and Argentina. Consequently, these firms' earnings and, by extension, their overall performance in the region are a direct function of the situation in these countries. From this perspective, there are factors in each of the three countries that can help to interpret the falling market share of TNCs in recent years.

The first of these factors concerns the slow growth of the United States economy in the early years of the decade and resulting impact on Mexican exports, of which a large proportion are generated by TNCs. This has been compounded by the growing influx of Chinese exports to the North American market, squeezing these firms' market shares.

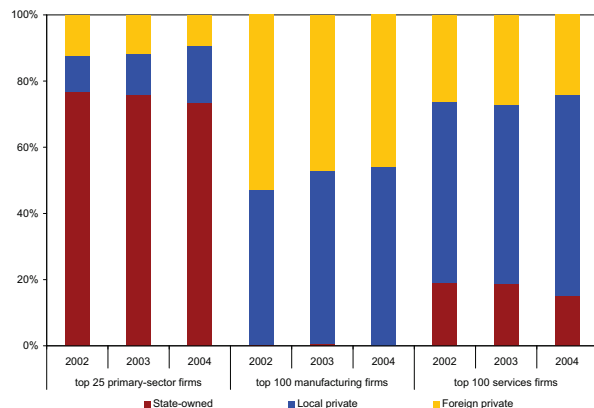
A second factor is the crisis in Argentina and the impact on TNCs of the Government's decision to freeze utility rates after converting them to pesos in the wake of the currency devaluation. This prompted several companies to scale down or even withdraw from their Argentine operations, owing to the poor results caused by weakened domestic demand and revenues being received in a severely devalued local currency (see box I.2).

Lastly, the third factor is the difficult situation Brazil faced, with investor uncertainty over the new Government, coupled with waning confidence in emerging markets (which was partly attributable to the Argentine crisis). The devaluation of the Brazilian real undermined the dollar earnings of TNCs in different sectors and, hence, their motivation to continue investing or even, in some cases, to remain in the region at all.

These factors help to shed light on the dip in the relative presence of TNCs and the expansion of that of local private firms. Much of the ground gained by these local firms is also due to their own merit, however, as will be discussed in the following section and in the later chapters of this report.

America and the Caribbean in 2004. Other major State-owned corporations in this sector, with combined sales of approximately US\$ 15 billion, are Corporación del Cobre (Codelco) of Chile, Empresa Colombiana de Petróleos (Ecopetrol), Empresa Nacional de Petróleo (Enap) of Chile and Empresa Estatal Petróleos del Ecuador (Petroecuador). Private companies with a similar level of sales include the privatized former State enterprise Companhia Vale do Rio Doce (CVRD) of Brazil, Companhia Brasileira de Petróleo Ipiranga, also of Brazil, Grupo México and a number of foreign firms, including Repsol-YPF of Spain, Royal Dutch/Shell of the Netherlands and ExxonMobil of the United States.

Figure I.8
TOP 500 FIRMS: SALES OF THE TOP 100 MANUFACTURING FIRMS, THE TOP 100 SERVICES FIRMS AND THE TOP 25 PRIMARY-SECTOR FIRMS BY CAPITAL OWNERSHIP
 (Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the Special Studies and Projects Department of *América economía* magazine, Santiago, Chile, 2005

Clearly, these are, for the most part, petroleum and mining enterprises, whose performance reflects the high international prices for those commodities. Indeed, copper prices soared by 30% in 2004, while silver and gold prices were up by 12.4% and 6.9%, respectively (Cochilco, 2006). The price of iron, which is fixed once a year, stood at 37.9 cents per dry metric ton unit (dmtu), compared with 32 cents in 2003 (IMF, 2005b). At the end of 2004, the price of petroleum was over US\$ 43 per barrel, 26.3% more than at the start of the year, a trend which continued throughout 2005 and is set to carry over in 2006.

The local private firms increased their presence among the 100 leading manufacturing firms, at the expense of private foreign enterprises (see figure I.8).¹² In 2004, the sales of these 100 companies expanded by 26% to US\$ 303

billion, of which 54% corresponded to private local firms and the rest to foreign companies. The automobile, iron and steel and agribusiness subsectors account for almost half of this group's total sales. Much of the increase in local private firms' share is attributable to the expansion of Brazilian firms operating in the iron and steel sector—namely Companhia Siderúrgica Nacional (CSN), Gerdau and Usiminas—and agribusiness (Sadia and Perdigão). Argentine firms in these sectors, prominently Aceitera General Deheza and Tenaris, also saw an upturn. Conversely, private Mexican firms' sales declined or remained flat in agribusiness, beer and soft drinks, cement and electronics. These trends reflect the comparative advantages of the region's countries in resource-based manufactures. In fact, it was in these categories, as well as in the primary sector, that the trans-Latins stood out at the global level.

The smaller share of the private foreign firms is mainly a reflection of the virtual stagnation of sales by subsidiaries established in Mexico, which grew by a mere 2%. Electronics and the automobile industry are the main subsectors in which TNCs are represented in Mexico and in which sales diminished or remained unchanged. In the electronics sector the principal TNCs are LG (Republic of Korea) and Siemens (Germany) and in the automobile sector, General Motors (United States), DaimlerChrysler and Volkswagen (Germany), and Nissan (Japan). The situation was different in Brazil, where the sales of foreign companies increased owing, to a large extent, to the performance of automobile companies such as DaimlerChrysler (Germany) and Ford (United States), electronics firms such as Nokia (Finland) and Siemens, and chemical manufacturers, such as BASF (Germany).

The top 100 non-financial firms in the services sector recorded US\$ 276 billion in sales in 2004, or 20% more than in 2003. This sector is dominated by private local firms (61 companies, which account for 61% of sales), followed by foreign companies, with one quarter of sales, then State-owned enterprises (see figure I.8). The commerce, telecoms and energy subsectors report by far the largest sales volumes and the highest number of firms. This pattern of specialization is reflected among the private firms, while State enterprises tend to be found mainly in the energy segment, with a smaller role in transport and other public services. Local private firms recorded sales increases in Chile, Brazil and Mexico, especially in telecoms (Telemar of Brazil and the Mexican trans-Latins América Móvil and Teléfonos de México); retail (D&S and the Chilean trans-Latins Cencosud and Falabella); and electricity (Companhia Paulista de Força

¹² As noted earlier, the State maintains only a marginal presence in the manufacturing sector. It accounted for as little as 0.5% among the 100 leading manufacturers in 2003, and did not figure at all in 2004.

e Luz (CPFL) of Brazil). Several of these companies are trans-Latins, which have benefited from the sound local economic environment and reaped the benefits of their expansion into other countries of the region (see chapters III, IV, V and VI).

The foreign firms have seen their share in this group decline substantially. As indicated, their share shrank to 24% in 2004, down from 36% in 2000 and 40% in 1999. The most striking case is that of the foreign companies in Argentina: there are now almost no foreign firms among the heavyweights in the services sector, unlike the situation in the 1990s. Conversely, in Brazil and Mexico there has been little change with respect to the situation in earlier years, with major TNC subsidiaries prominent in commerce, energy and telecoms. This is the case of the subsidiaries of supermarket chains Wal-Mart of the United States, Carrefour of France and Sonae of Portugal (which sold its Brazilian assets to Wal-Mart in 2005); power companies AES Corp of the United States, Electricité de France, and Iberdrola of Spain in Brazil's electricity sector; and Telefónica of Spain, Portugal Telecom, Telecom Italia and the Mexican trans-Latin América Móvil in Mexico's telecoms sector.

In short, the data show an increase in the relative presence of private local firms in all three sectors of activity, which is due in some cases to their own growth and success, and in others to the withdrawal of TNCs.

(b) The top 200 exporters

Following a modest performance at the beginning of the decade, exports from Latin America and the Caribbean rallied strongly in 2004, climbing by more than 21% over the 2003 figure. Exports of natural resources and resource-based manufactures were up 28%. Recovering external demand was reflected in excellent international prices for these products. Primary resources led the region's exports, accounting for 47% of the export mix. Exports of non-resource-based manufactures climbed by 17%, driven by mid-level technology manufactures, although this was not enough gain a higher share in the export basket (United Nations, 2005).

The region's export performance is defined to a great extent by the leading export firms of Latin America and the Caribbean. Shipments abroad by the top 200 exporters totalled US\$ 256 billion in 2004, accounting for 58% of total exports and representing a 23% increase over the figure for 2003.

The sectors in which these firms operate also largely reflect the region's export pattern. As may be supposed, natural resources, especially oil, gas and mineral products, account for half of exports by the 200 leading export companies. Agribusiness goods represent a smaller

proportion, followed by automobiles, autoparts, electronic and computer products, and other manufactures with different levels of embodied technology.

In terms of ownership of these companies, State-owned enterprises control exports in the primary sector (petroleum and minerals), although a number of large private firms, such as the mining company Companhia Vale do Rio Doce (CVRD), also operate in this category. Two thirds of the exports of private local companies, or 19% of the total, are manufactures (see table I.5). These companies are Brazilian, such as Sadia (agribusiness), Embraer (aerospace), Gerdau and Companhia Siderurgica Nacional (steel), or Mexican, such as the Imsa Group (steel), the Bimbo Group and the Maseca-Gruma Group (agribusiness), and Mabe (electronics). Private foreign enterprises are also represented in the manufacturing sector in Brazil and Mexico, albeit in different segments. The region's leading export firms, besides the State oil companies, are Mexican subsidiaries of the United States companies General Motors, Delphi, Hewlett-Packard, Lear and General Electric and of DaimlerChrysler and Volkswagen of Germany, and Brazilian subsidiaries of Cargill and Bunge of the United States.

Table I.5
EXPORTS OF THE TOP 200 EXPORT FIRMS, BY SECTOR
AND OWNERSHIP, 2004
(Percentages)

	State-owned	Private local	Private foreign	Total
2004				
Primary	36.0	4.7	8.8	49.5
Manufactures	0.0	18.9	27.6	46.5
Services	0.0	4.0	0.0	4.0
Total	36.0	27.6	36.4	100.0
2000				
Primary	14.8	5.5	4.5	24.8
Manufactures	0.0	23.4	41.2	64.7
Services	0.0	8.8	1.7	10.5
Total	14.8	37.8	47.5	100.0
1995				
Primary	32.2	6.7	4.9	43.8
Manufactures	1.2	20.9	26.2	48.3
Services	0.0	7.2	0.6	7.8
Total	33.4	34.9	31.7	100.0

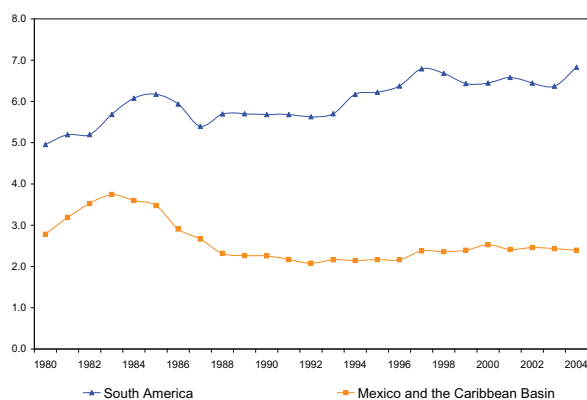
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the Special Studies and Projects Department of *América economía* magazine, Santiago, Chile, 2005.

The role played by TNCs in the region's exports has had an impact on the international position of the subregions. As shown in figure I.9, South America's exports of natural resources and resource-based manufactures, which are dominated by State enterprises, represent a larger share of the world market than those of Mexico and the Caribbean Basin (see figure I.9). These two subregions' market shares did not change significantly between 1980 and 2004. On the other hand, Mexico and the Caribbean Basin export a larger world share of non-

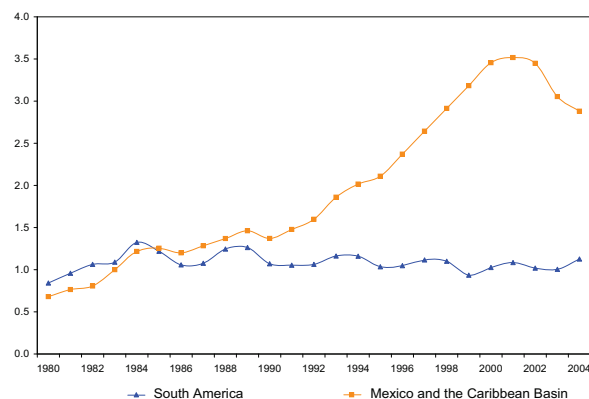
resource-based manufactures than South America does. Foreign firms have had a very substantial presence in this sector, especially in automobiles, electronics and clothing. Also noteworthy is the dip seen since 2002 in the Mexican and Caribbean Basin world share, which is partly attributable to competition from China. This represents one of the main challenges in the near future. Another factor is that exports from TNCs operating in Brazil in these sectors trended upwards until 2004 (ECLAC, 2005c), although the competitiveness of Brazil's exports has suffered since then as a result of the currency revaluation.

Figure I.9
LATIN AMERICA AND THE CARIBBEAN: MARKET SHARE OF WORLD IMPORTS OF NATURAL RESOURCES AND RESOURCE-BASED AND NON-RESOURCE-BASED MANUFACTURES, ^a 1980-2004
 (Percentages)

Natural resources and resource-based manufactures



Non-natural resource-based manufactures



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations "UN Comtrade Database [online database], Statistics Division, Department of Economic and Social Affairs, 2005. Merchandise categories based on the Standard International Trade Classification (SITC 3 digits, Rev.2). The data are annual and not three-year moving averages, as used in TradeCAN.

^a The natural resource category contains 45 simply processed commodities, including concentrates, while resource-based manufactures are made up of 65 groups: primarily agricultural and forestry products and metals, except steel, petroleum products, cement, glass, and others. The category of non-resource-based manufactures contains 120 groups of products: 44 low-technology products (garments, textiles, glass manufactures, steel, jewellery), 58 mid-level technology products (the automobile industry, the processing industry and engineering) and 18 high-technology products (electronics, pharmaceutical products, turbines, aircraft, instruments).

(c) The major transnationals

The consolidated Latin American and Caribbean sales of the 50 largest non-financial TNCs totalled US\$ 259 billion in 2004, which meant a 12% rise over the previous year's figure (see table I-A.5). The share of subsidiaries of United States firms in this group has declined to 45%, down from 52% in 2003 (see figure I.10). This was due mainly to the drop in sales of the Delphi subsidiary in Mexico and the purchase by Telefónica of Spain of BellSouth's Latin American assets. This acquisition has boosted the Spanish company's sales in the region, and it remains the second largest TNC in Latin America, after General Motors. The higher sales volumes recorded by the power companies Endesa and Iberdrola (which entered Mexico in 2004) has upped the share of these Spanish companies in the group's sales from 12% to 14%. The German corporations had a similar experience: these companies, mainly in the automobile sector, also increased their share in the sales of the 50 leading TNCs (to 13%), thanks to the higher sales figures of the Volkswagen and DaimlerChrysler subsidiaries in Brazil, Mexico and, to a lesser extent, Argentina. Bayer's chemicals subsidiary in Brazil also contributed to the robust performance of the German companies.

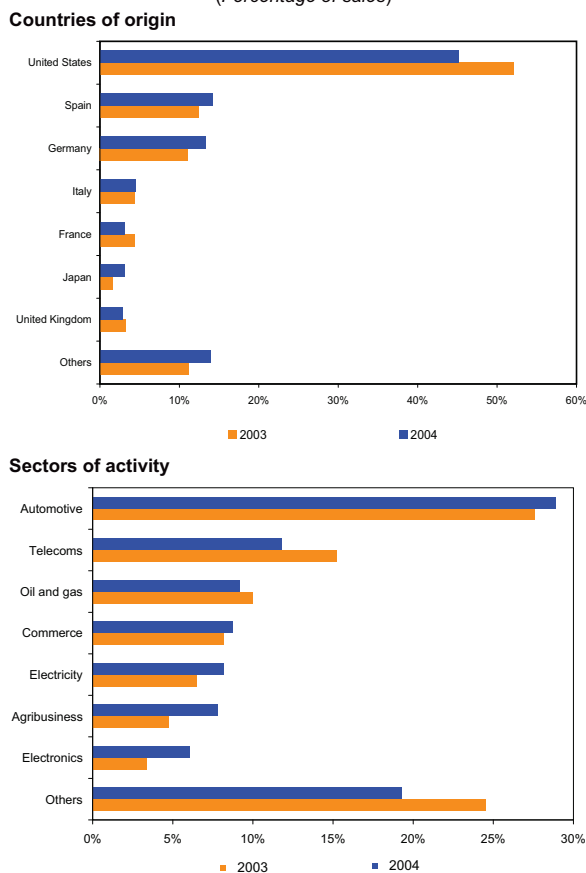
As a result of the stronger growth in the sales of TNC subsidiaries, Brazil now has more TNCs than any other country in the region, replacing Mexico, which held the lead in 2003. These two countries account for 80% of the Latin American sales of the subsidiaries of major global conglomerates, while the remaining 20% is divided up among Chile, Argentina and a few other South American countries.

The region's banking sector continues to be dominated by the Spanish banks Santander Central Hispano (SCH) and Bilbao Vizcaya Argentaria (BBVA) and by Citicorp of the United States. Thanks to the sound economic climate, which has been reflected in a credit boom and the stabilization of the financial system, the 250 largest banks in the region have increased their assets by 30% and their profits by 69%.

The 50 major non-financial TNCs operating in the region reflect the profile of the FDI inflows into Latin America and the Caribbean in terms of countries of origin and destination sectors. The incipient investment by developing countries is still far from altering the traditional pattern of investment in the region.

The business sector in Latin America and the Caribbean is still in a state of flux. In the 1990s, the region observed an increasingly strong presence of foreign firms, which took over large State-owned or local private companies. Currently, however, the advance of the latter and the slowdown in the expansion of foreign firms have altered the regional corporate map.

Figure I.10
**TOP 50 NON-FINANCIAL TNCs BY CONSOLIDATED SALES IN
 LATIN AMERICA, 2003-2004**
 (Percentage of sales)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the Special Studies and Projects Department of *América economía* magazine, Santiago, Chile, 2005.

In conclusion, FDI trends in Latin America and the Caribbean may be summarized as follows: in the 1990s, Latin America and the Caribbean attracted significant sums of FDI through new economic models based on open economies, liberalization of trade activities and the implementation of attractive horizontal incentives, namely, deregulation of services and privatization of State-owned enterprises. These initiatives attracted mainly market-seeking and natural-resource-seeking FDI. Latin America and the Caribbean was less successful in attracting efficiency-seeking FDI and even less so in securing strategic or technological asset-seeking FDI.

Whether such FDI inflows into Latin America and the Caribbean have been of benefit to the region is now the subject of discussion. Admittedly, FDI flows have played an important role in transforming the region by modernizing industry and upgrading services and infrastructure. This is especially evident in the modern telecommunications network in Brazil, financial services in Argentina, the road and airport network in Chile and export platforms in Mexico

and Costa Rica, which assemble competitive motor vehicles and microprocessors, respectively. Serious problems have surfaced in different parts of the region in relation to FDI, however. Resource-seeking FDI is criticized for creating enclaves with few processing activities that can be integrated into the local economy, generating low fiscal returns from the exploitation of non-renewable natural resources and causing environmental pollution. Market-seeking FDI is often regarded as creating higher-cost industries that are not internationally competitive, as well as crowding out local manufacturers and inviting regulatory problems that have led to formal investment disputes. Objections are raised to efficiency-seeking FDI on the basis that it frequently leads to stagnation in the low value added trap, since it is based on static, non-dynamic advantages, has very weak links with the local economy, crowds out local firms and can lead to a reduction in standards in terms of production costs (wages, social benefits) and to pressure for greater incentives (for example, in the area of tax and infrastructure). Furthermore, strategic-asset-seeking FDI—which is, in any case, almost non-existent in the region—can lead to stagnation at a low level of scientific and technological development and may be incompatible with the objectives of national scientific and technological policies. In other words, the FDI boom in Latin America and the Caribbean produced conflicting results and, as flows have declined, criticisms of its outcomes have mounted.

The experience of Latin America and the Caribbean illustrates the fact that, although the FDI brought in by TNCs can increase productivity and exports (UNCTAD, 2002), it will not necessarily improve the competitiveness of the domestic sector, which, in the final analysis, is what determines long-term economic growth (Lall and Narula, 2006). Economic liberalization enables TNCs to exploit existing capacities more freely, but does not in itself provide growth opportunities, unless there is a domestic sector with the necessary absorptive capacity to benefit from the externalities produced by the TNC activity. Such capacity is determined by a set of factors, including the level of education of the population and the training of the workforce, the existence of sound institutions and of physical, scientific and technological infrastructure. Consequently, FDI flows increase over time in countries where local capacities are being strengthened and new capacities are being created, and stagnate or diminish in the opposite case. For this reason, the competitive advantages of TNCs must be matched by an improvement in the absorptive capacity of the recipient countries.

In order to obtain long-term benefits from the FDI brought into the region by TNCs, the countries of Latin America and the Caribbean require better FDI policies that are part of more coherent development strategies. Chapter II looks at the experiences of investment promotion agencies in Latin America and the Caribbean.

Annex

Table I-A.1
LATIN AMERICA AND THE CARIBBEAN: ACQUISITIONS OF PRIVATE FIRMS OVER US\$ 100 MILLION, 2005
(Millions of dollars and percentage of share acquired)

Firm or assets sold	Country	Buyer	Buyer's country of origin	Amount	Percentages
Bavaria S.A.	Colombia	SABMiller Plc	United Kingdom	7 806.0	71.8
Hylsamex	Mexico	Techint Argentina S.A.	Argentina	2 565.8	42.5
Petroleum Reserves and Pipelines	Ecuador	Andes Petroleum	China	1 420.0	100.0
Loma Negra S.A.	Argentina	Constructora Camargo Corrêa	Brazil	1 025.1	100.0
Companhia Brasileira de Distribuição	Brazil	Casino Guichard Perrachon	France	858.6	11.6
Sonae assets	Brazil	Wal-Mart	United States	764.0	...
Smartcom PCS	Chile	América Móvil	Mexico	510.4	100.0
TIM Perú SAC	Peru	América Móvil	Mexico	502.9	100.0
Unión de Cervecerías Peruanas					
Backus & Johnston	Peru	SABMiller Plc	United Kingdom	468.0	20.3
Granahorrar	Colombia	BBVA	Spain	424.0	98.8
Real Seguros S.A.	Brazil	Millea Holdings Inc.	Japan	380.1	100.0
Sociedad Minera Cerro Verde	Peru	Sumitomo Metal Mining Co. Ltd.	Japan	265.2	21.0
Dixie Toga S.A.	Brazil	Bemis Company	United States	251.2	64.4
Reposo SAIC	Brazil	United Phosphorus Ltd.	India	218.4	100.0
Tubos del Caribe S.A.	Colombia	Maverick Tube Corp.	United States	186.6	100.0
Cervecería Leona	Colombia	SABMiller Plc	United Kingdom	176.0	31.0
Banco Bradesco S.A.	Brazil	Banco Espirito SantoReg	Portugal	159.8	3.2
Banco Salvadoreño	El Salvador	Banistmo	Panama	145.5	60.0
Interbanco S.A.	Colombia	Société générale	France	135.6	50.0
Votoceel Filmes Flexiveis	Brazil	Arcor	Argentina	119.5	100.0
Cruz del Sur S.A.	Chile	Royal & Sun Alliance Ins Grp	United Kingdom	118.1	100.0
Consorcio Siderurgia Amazonia	Venezuela (Bol. Rep. of)	Techint Argentina S.A.	Argentina	107.4	4.5
Total				18 608.2	

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of corporate information, Bloomberg and specialized press reports.

Table I-A.2
LATIN AMERICA AND THE CARIBBEAN: MAIN INVESTOR COUNTRIES, 1996-2005
 (Percentages)

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	Total
Argentina	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	...	100.0
Spain	14.4	22.8	15.1	74.8	64.9	31.1	-13.9	-37.6	25.4	...	43.7
United States	31.5	33.6	18.5	15.7	11.0	1.0	18.8	-8.8	17.1	...	1.4
France	7.2	2.5	18.3	6.4	6.4	79.5	-18.7	-28.6	4.0	...	7.8
Netherlands	2.2	10.4	13.5	-0.2	0.7	6.4	-12.5	36.1	15.8	...	4.8
Italy	3.8	4.8	6.8	2.1	6.8	-6.0	-4.0	26.3	-0.3	...	3.8
Others	40.9	26.0	27.7	1.2	10.3	-12.0	130.2	112.6	38.1	...	21.5
Bolivia	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	...	...	100.0
United States	30.8	30.1	34.7	33.6	44.2	40.0	28.9	33.4	...	...	34.6
Argentina	1.6	11.1	21.5	10.5	9.7	11.4	3.1	3.6	...	...	10.0
Brazil	8.9	8.0	3.4	13.8	4.9	8.2	18.2	10.8	...	...	9.6
Italy	32.4	17.4	10.7	6.4	6.3	7.2	2.7	4.7	...	...	9.6
Spain	3.3	9.7	4.5	1.0	5.5	6.7	26.8	11.1	...	...	8.9
Others	23.0	23.7	25.2	34.8	29.3	26.5	20.3	36.5	...	...	27.2
Brazil	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
United States	25.8	28.6	20.2	29.3	18.1	21.2	13.9	18.5	19.6	21.2	21.5
Spain	7.7	3.6	22.0	20.7	32.1	13.1	3.1	5.5	5.2	3.9	14.2
Netherlands	6.9	9.7	14.5	7.4	7.5	9.0	18.0	11.2	38.0	16.7	13.9
France	12.7	8.1	7.8	7.2	6.4	9.1	9.7	6.4	2.4	8.7	7.4
Portugal	2.6	4.4	7.5	8.7	8.4	8.0	5.4	1.6	2.8	1.2	5.8
Others	44.4	45.6	28.1	26.7	27.6	39.5	49.9	56.9	31.9	48.3	37.2
Chile	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	...	100.0
Spain	10.1	28.9	14.8	49.9	21.2	7.7	7.3	12.4	80.0	...	30.0
United States	47.2	17.3	23.2	15.8	26.1	36.2	16.3	29.0	2.3	...	22.5
Canada	12.1	20.3	16.5	5.0	24.5	2.8	27.0	14.6	7.3	...	12.7
United Kingdom	6.2	10.4	11.6	3.6	5.5	8.9	44.9	10.5	2.0	...	9.8
Australia	2.6	3.5	6.3	0.1	1.1	13.1	3.8	4.0	2.7	...	4.0
Others	21.8	19.7	27.5	25.6	21.6	31.3	0.7	29.4	5.6	...	20.9
Colombia	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	...	100.0
United States	25.1	30.1	-3.1	20.4	43.5	22.5	-13.7	326.0	38.6	...	22.8
Spain	16.6	2.4	41.8	-2.1	-54.4	33.4	31.3	46.7	25.6	...	18.2
Netherlands	2.3	1.0	3.7	21.7	66.7	7.1	6.5	11.6	22.2	...	10.3
Panama	11.9	8.2	36.2	0.2	-198.9	4.6	-107.7	8.8	1.3	...	5.6
Germany	2.4	2.4	1.1	2.5	35.0	0.6	11.3	3.7	1.5	...	2.5
Others	41.6	56.0	20.4	57.3	208.0	31.8	172.4	-296.8	10.9	...	40.5
Costa Rica	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	...	100.0
United States	61.9	74.9	79.5	55.7	68.4	56.8	50.1	62.3	65.7	...	63.4
Mexico	7.8	5.3	3.5	14.9	7.2	6.7	4.5	6.6	4.7	...	6.8
Netherlands	1.5	0.9	0.1	0.1	0.0	0.6	34.8	5.2	4.0	...	6.2
Canada	1.8	2.0	5.6	5.8	-0.7	7.9	-1.5	3.0	8.4	...	3.7
El Salvador	2.5	3.4	0.1	2.4	3.7	3.6	3.6	4.4	1.0	...	2.7
Others	24.5	13.5	11.3	21.2	21.4	24.5	8.5	18.4	16.1	...	17.2
Ecuador	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
United States	44.8	40.0	41.8	35.5	32.7	23.8	30.7	13.1	26.7	18.7	28.2
Canada	2.5	15.1	23.8	20.5	23.7	32.3	27.6	21.1	26.1	34.2	24.4
Italy	0.2	1.4	9.8	9.9	9.3	6.6	8.6	3.5	4.2	4.6	5.9
Spain	3.7	3.6	0.1	0.0	11.9	6.4	6.9	3.1	4.2	8.5	5.0
Argentina	2.8	4.2	3.2	13.5	3.5	4.8	4.6	1.3	2.1	1.6	3.8
Others	45.9	35.6	21.2	20.5	19.0	26.1	21.7	57.8	36.6	32.4	32.8
El Salvador	...	...	...	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
United States	...	...	...	33.7	36.3	36.5	35.8	36.3	32.6	31.7	34.5
Venezuela (Bolivarian Rep. of)	...	...	...	16.5	15.7	13.7	12.6	11.8	9.9	9.6	12.3
Mexico	...	...	...	3.7	3.4	3.1	3.0	3.2	19.8	19.3	9.2
France	...	...	...	11.8	10.8	9.5	8.7	8.2	0.2	0.2	6.2
Spain	...	...	...	3.8	3.5	5.4	6.5	6.2	6.3	6.0	5.5
Others	...	...	...	30.5	30.4	31.8	33.5	34.3	31.2	33.2	32.3

Table I-A.2 (concluded)

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	Total
Honduras	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	...	...	100.0
United States	48.8	41.4	35.8	47.3	18.0	31.3	82.4	60.9	...	...	44.8
Canada	1.6	3.3	12.2	21.9	6.4	9.7	12.4	8.9	...	...	10.4
Netherlands	...	...	0.0	2.7	47.2	7.6	-32.8	1.4	...	...	6.9
El Salvador	10.2	21.0	9.2	6.0	3.4	-0.6	8.6	2.7	...	...	6.2
Italy	10.0	5.9	12.0	-1.5	6.0	6.3	1.8	0.1	...	...	4.0
Others	29.4	28.4	30.8	23.7	19.0	45.8	27.6	25.9	...	...	27.8
Mexico	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
United States	67.3	61.1	65.5	53.5	71.1	77.4	66.0	55.4	42.5	66.4	63.4
Spain	0.9	2.7	4.1	7.8	12.3	2.5	4.2	13.8	38.2	10.3	10.3
Netherlands	6.3	2.9	12.8	8.1	15.0	9.3	6.9	4.0	2.2	8.9	7.7
United Kingdom	1.0	15.2	2.1	-1.4	1.6	0.4	6.8	8.3	0.7	0.6	3.3
Canada	6.9	2.0	2.6	4.6	4.0	3.6	1.2	1.9	2.1	2.5	3.0
Others	17.5	16.1	13.0	27.5	-4.0	6.7	15.0	16.7	14.3	11.3	12.2
Paraguay	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	...	...	100.0
United States	20.5	46.1	42.0	13.6	37.5	4.8	35.9	37.8	...	...	34.5
Argentina	13.3	11.1	16.7	21.8	7.4	12.5	8.2	9.9	...	...	11.2
Brazil	4.2	7.5	13.8	6.7	17.2	13.9	10.6	7.7	...	...	9.8
Netherlands	13.2	10.4	7.1	22.1	3.2	5.2	10.7	9.1	...	...	9.7
United Kingdom	9.1	1.6	1.5	0.1	3.4	4.2	4.6	4.7	...	...	3.9
Others	39.8	23.4	18.9	35.7	31.3	59.4	30.0	30.9	...	...	30.8
Peru	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	...	100.0
United Kingdom	21.6	23.2	34.5	52.9	11.1	25.2	48.3	25.4	30.8	...	30.1
United States	31.9	25.0	21.7	18.7	8.1	-12.5	-19.7	21.3	35.3	...	14.4
Netherlands	4.0	14.3	1.9	7.8	15.6	33.2	29.2	19.1	25.8	...	14.2
Spain	18.6	-5.7	3.9	1.7	52.3	-3.7	6.1	1.4	0.0	...	12.9
Chile	5.3	2.1	5.9	7.1	1.4	16.9	4.7	2.3	0.0	...	5.2
Others	18.6	41.2	32.0	11.8	11.5	41.0	31.4	30.5	8.1	...	23.2
Venezuela (Bolivarian Republic of)	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
United States	26.0	17.4	17.2	28.3	17.5	33.5	38.8	0.7	35.4	40.5	21.8
Spain	2.7	15.7	6.9	3.9	9.9	5.8	5.5	4.0	4.2	3.4	8.0
France	3.1	5.3	3.1	4.8	4.9	10.0	9.5	0.1	10.2	0.4	5.0
United Kingdom	3.8	8.9	3.2	6.6	0.4	1.8	2.2	0.5	...	0.3	3.7
Argentina	6.2	4.8	4.5	6.9	0.2	1.0	2.8	0.5	...	0.0	3.2
Others	58.2	48.0	65.1	49.6	67.0	47.9	41.1	94.3	50.2	55.4	58.4

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official statistics.

Table I-A.3
LATIN AMERICA AND THE CARIBBEAN: DISTRIBUTION OF FDI BY SECTOR, 1996-2005
 (Percentages)

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	Total
Argentina	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	...	100.0
Manufactures	39.9	36.1	15.7	8.1	14.3	2.3	46.0	69.3	28.6	...	20.7
Natural resources	24.9	1.9	18.2	74.4	26.3	41.5	52.7	-16.8	53.0	...	40.9
Services	30.2	53.4	50.0	13.1	45.6	58.2	-21.5	32.6	2.9	...	29.4
Others	5.0	8.6	16.1	4.3	13.9	-1.9	22.8	14.9	15.6	...	9.0
Bolivia	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	...	...	100.0
Manufactures	7.7	2.9	1.6	15.1	11.2	9.9	9.1	11.0	...	...	8.5
Natural resources	17.1	38.5	56.7	46.8	53.0	64.5	47.5	47.7	...	...	48.7
Services	75.2	58.6	41.7	38.2	35.8	25.5	43.4	41.4	...	...	42.9
Brazil	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Manufactures	22.7	13.3	11.9	25.4	17.0	33.3	40.2	34.9	52.8	47.5	28.2
Natural resources	1.4	3.0	0.6	1.5	2.2	7.1	3.4	11.5	5.3	4.5	3.7
Services	75.9	83.7	87.5	73.1	80.9	59.6	56.4	53.6	41.9	48.0	68.1
Chile	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	...	100.0
Manufactures	19.0	12.0	8.8	9.0	7.9	16.1	6.2	18.2	8.5	...	11.2
Natural resources	22.6	33.8	41.9	15.0	11.6	23.0	59.3	31.4	7.0	...	25.6
Services	58.5	54.2	49.4	76.0	80.4	60.9	34.5	50.4	84.5	...	63.2
Colombia	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Manufactures	24.4	16.6	11.6	36.5	82.2	5.9	17.7	0.3	14.0	18.9	19.3
Natural resources	32.3	32.1	18.5	3.4	29.6	10.0	2.7	-24.1	1.8	67.0	21.3
Services	43.2	51.3	69.9	60.1	-11.9	84.1	79.6	123.8	84.2	14.1	59.4
Costa Rica	...	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	...	100.0
Manufactures	...	68.1	71.6	59.1	75.3	51.6	73.7	68.8	74.5	...	68.1
Natural resources	...	9.4	6.9	8.1	-2.7	0.2	-1.3	-6.3	2.3	...	2.0
Services	...	22.0	21.2	32.3	27.2	47.7	27.5	36.5	20.8	...	29.2
Others	...	0.6	0.3	0.5	0.2	0.5	0.0	1.0	2.3	...	0.7
Ecuador	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Manufactures	4.7	6.2	3.5	1.2	1.3	4.4	4.4	4.6	3.2	3.0	3.8
Natural resources	61.4	77.6	88.3	93.3	94.7	85.6	84.5	56.4	81.4	93.4	80.7
Services	33.9	16.2	8.2	5.5	4.0	9.9	11.1	39.1	15.4	3.6	15.6
El Salvador	...	...	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Manufactures	...	...	26.6	24.6	25.0	25.9	26.0	28.3	26.4	26.3	26.2
Natural resources	...	...	2.3	1.2	0.5	1.8	2.0	2.0	2.5	2.5	1.9
Services	...	...	71.1	74.3	74.5	72.3	72.0	69.7	71.1	71.2	71.8
Mexico	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Manufactures	61.4	60.3	61.5	67.2	56.0	22.3	39.8	43.1	49.9	58.0	47.8
Natural resources	1.5	1.2	0.9	1.6	1.6	0.3	1.9	0.8	0.8	0.7	1.1
Services	37.1	38.5	37.6	31.3	42.4	77.4	58.3	56.1	49.3	41.3	51.1
Peru	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	...	100.0
Manufactures	27.9	19.6	16.4	9.2	4.8	22.9	19.3	5.1	0.5	...	15.0
Natural resources	11.1	8.5	20.2	21.0	2.5	0.7	0.4	0.5	6.3	...	9.6
Services	61.0	71.8	63.4	69.8	92.6	76.4	80.2	94.4	93.2	...	75.5
Venezuela (Bolivarian Rep. of)	...	...	...	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Manufactures	...	...	...	49.3	33.6	38.4	40.7	14.0	84.5	50.6	40.2
Natural resources	...	...	...	3.2	0.7	0.1	1.3	1.4	0.1	0.0	0.9
Services	...	...	...	47.4	65.7	61.5	58.0	84.6	15.3	49.3	58.9

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official statistics.

Table I-A.4
LATIN AMERICA: MAIN SECTORS AND OWNERSHIP OF TOP 500 COMPANIES, 2000-2004
 (Percentages)

Sector	2000	2001	2002	2003	2004
State-owned					
Hydrocarbons	16.9	16.0	16.1	18.1	19.1
Energy	3.0	4.0	4.2	3.8	3.5
Mining	0.4	0.5	0.6	0.5	0.8
Public services	0.3	0.2	0.3	0.3	0.7
Transport	0.1	0.3	0.4	0.4	0.3
Others	1.3	2.0	1.7	2.0	0.2
Total State-owned	22.1	23.0	23.3	25.0	24.7
Local private					
Commerce	7.3	7.9	8.3	8.3	7.8
Telecommunications	2.8	3.8	4.0	4.1	4.4
Steel	2.6	3.3	3.8	4.2	4.4
Soft drinks/beer	3.1	3.5	3.8	3.6	3.1
Hydrocarbons	1.0	1.0	1.1	1.5	3.1
Agribusiness	3.1	3.2	3.5	3.5	3.0
Mining	1.8	1.6	1.8	2.0	2.5
Cement	1.1	1.4	1.5	1.3	1.4
Petrochemicals	1.3	1.2	1.4	1.9	1.3
Energy	0.7	0.9	0.7	0.9	1.3
Others	13.9	13.8	12.6	12.5	14.2
Total local private	38.7	41.6	42.3	43.8	46.6
Foreign private					
Automobile	7.3	6.7	7.3	6.5	6.0
Telecommunications	6.5	4.0	3.4	3.9	3.0
Hydrocarbons	3.6	3.2	2.9	3.2	2.7
Commerce	3.1	3.2	3.1	3.0	2.5
Electronics	4.2	3.9	4.4	2.6	2.1
Energy	2.6	2.8	1.9	2.1	2.0
Agribusiness	1.6	2.0	1.9	2.1	1.8
Autoparts	2.4	1.5	2.1	1.0	1.6
Mining	0.4	0.4	0.8	0.9	1.5
Chemicals	0.9	1.1	1.0	0.8	1.3
Others	6.6	6.7	5.6	5.0	3.6
Total foreign private	39.2	35.4	34.4	31.2	28.7
Total 500 companies	100.0	100.0	100.0	100.0	100.0
Total 500 companies (sales in billions of dollars)	852 361	830 433	734 710	831 772	1 073 755

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the Special Studies and Projects Department of *América economía* magazine, Santiago, Chile, 2005.

Table I-A.5
LATIN AMERICA: TOP 50 NON-FINANCIAL TRANSNATIONALS, BY CONSOLIDATED SALES, 2004
(Billions of dollars)

Position in 2004	Firm	Country of origin	Sector	Sales	Percentages of global sales (%)	Main subsidiaries
1	General Motors Corp.	United States	Automobile	18 800	10.0	Mexico, Brazil, Colombia, Argentina
2	Telefónica de España SA	Spain	Telecoms	17 136	45.0	Brazil, Chile, Peru, Mexico, Argentina
3	WalMart Stores	United States	Commerce	14 440	5.0	Mexico, Brazil, Argentina, Guatemala
4	DaimlerChrysler AG	Germany	Automobile	13 984	8.0	Mexico, Brazil, Argentina
5	Volkswagen AG	Germany	Automobile	11 846	11.0	Mexico, Brazil, Argentina
6	Bunge	United States	Agribusiness	10 677	42.0	Brazil, Argentina
7	Endesa	Spain	Electricity	9 710	44.0	Chile, Brazil, Argentina, Peru
8	Ford Motor Co.	United States	Automobile	8 668	5.0	Mexico, Brazil, Argentina
9	Telecom Italia SpA	Italy	Telecoms	8 524	22.0	Brazil, Argentina, Chile, Bolivia
10	Delphi Automotive Systems Corporation	United States	Auto parts	6 969	24.0	Mexico, Brazil
11	AES	United States	Electricity	6 860	72.0	Brazil, Venezuela (Bolivarian Republic of), Chile, Argentina
12	Repsol-YPF	Spain	Oil/gas	6 666	15.0	Argentina, Chile, Peru, Ecuador, Bolivia, Colombia
13	Carrefour Group	France	Commerce	6 570	7.0	Brazil, Argentina, Mexico, Colombia
14	Royal DutchShell Group	Netherlands/United Kingdom	Oil/gas	6 430	2.0	Brazil, Chile, Argentina, Mexico
15	Unilever	Netherlands/United Kingdom	Hygiene/ foodstuffs	5 151	10.0	Brazil, Mexico, Argentina, Chile
16	ExxonMobil Corporation	United States	Oil/gas	4 925	2.0	Brazil, Colombia, Argentina, Chile
17	Cargill, Inc.	United States	Agribusiness	4 854	7.0	Argentina, Brazil
18	HewlettPackard (HP)	United States	Computing	4 850	6.0	Mexico, Brazil, Argentina
19	Nissan Motor	Japan	Automobile	4 760	6.0	Mexico, Brazil
20	Nestlé	Switzerland	Agribusiness	4 705	7.0	Mexico, Brazil, Colombia, Chile
21	BHP Billiton Plc	Australia/United Kingdom	Aluminium	4 705	21.0	Chile, Peru, Brazil, Colombia
22	General Electric	United States	Various	4 636	3.0	Mexico, Brazil
23	Lear Corporation	United States	Auto parts	4 550	27.0	Mexico, Brazil
24	Arcelor	Luxembourg	Steel	4 441	12.0	Brazil, Mexico, Argentina
25	ChevronTexaco	United States	Oil/gas	4 199	3.0	Brazil, Colombia, Argentina, Venezuela (Bolivarian Republic of)
26	Siemens AG	Germany	Electronics	3 625	4.0	Mexico, Brazil
27	Sony	Japan	Electronics	3 177	5.0	Mexico, Brazil
28	Bayer	Germany	Chemicals	3 116	8.0	Brazil, Mexico, Argentina
29	Iberdrola SA	Spain	Electricity	3 047	24.0	Brazil, Mexico, Bolivia
30	Fiat Auto	Italy	Automobile	2 995	5.0	Brazil, Argentina
31	Anglo American Plc	United Kingdom	Mining	2 985	12.0	Chile, Brazil, Argentina, Venezuela (Bolivarian Republic of)
32	British American Tobacco Plc. (BAT)	United Kingdom	Tobacco	2 901	12.0	Brazil, Mexico, Venezuela (Bolivarian Republic of), Chile
33	Phelps Dodge Corporation	United States	Mining	2 855	43.0	Peru, Chile, Brazil, Venezuela (Bolivarian Republic of)
34	Portugal Telecom	Portugal	Telecoms	2 838	35.0	Brazil
35	The CocaCola Company	United States	Beverages/beer	2 788	13.0	Mexico, Brazil, Argentina, Chile
36	Whirlpool	United States	Electronics	2 744	21.0	Brazil, Mexico
37	PepsiCo	United States	Beverages/beer	2 724	9.0	Mexico, Argentina, Brazil
38	Koninklijke Philips Electronics N.V.	Netherlands	Electronics	2 640	6.0	Mexico, Brazil, Argentina, Chile
39	Visteon Corporation	United States	Auto parts	2 115	11.0	Mexico, Brazil, Argentina
40	Verizon Communications	United States	Telecoms	2 039	3.0	Venezuela (Bolivarian Republic of), Dominican Republic
41	Dow Chemical	United States	Chemicals	1 959	5.0	Brazil, Argentina, Mexico, Colombia
42	E.I. Du Pont de Nemours	United States	Chemicals	1 840	7.0	Mexico, Brazil, Argentina
43	LG Electronics Inc.	Republic of Korea	Electronics	1 819	5.0	Mexico, Brazil
44	KimberlyClark Corporation	United States	Wood pulp/paper	1 776	12.0	Mexico, Brazil
45	Nokia	Finland	Electronics	1 730	5.0	Brazil, Mexico
46	BASF AG	Germany	Chemicals	1 683	4.0	Brazil, Mexico, Argentina
47	Sonae SGPS	Portugal	Commerce	1 631	18.0	Brazil
48	Électricité de France	France	Electricity	1 539	3.0	Brazil, Argentina
49	Procter & Gamble	United States	Hygiene/cleaning products	1 500	3.0	Mexico, Argentina, Brazil
50	BP Amoco Plc	United Kingdom	Oil/gas	1 478	1.0	Argentina, Colombia, Venezuela (Bolivarian Republic of)
	Total			258 594		

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the Special Studies and Projects Department of *América economía* magazine, Santiago, Chile, 2005.

Chapter II

Active policies to attract foreign direct investment in Latin America and the Caribbean

A. Introduction

Although many different strategies have been employed to attract foreign direct investment (FDI), the countries that have been most successful in this regard are those that have adopted more active investment attraction policies. In the process, the countries also generate know-how that enables them to develop increasingly complex policy frameworks. At a theoretical level, these frameworks can be grouped into the three categories outlined below.

- **Passive policies:** these are built essentially upon a country's comparative advantages or macroeconomic conditions. They may be sufficient to attract TNCs that are seeking markets or natural resources, which are attractions intrinsic to a particular country. On this basis, countries may establish policy frameworks designed to facilitate inflows of FDI, through non-discrimination, legal FDI protection mechanisms, general incentives and so forth. This type of investment attraction policy is not normally integrated with the country's development policy and its success is measured mainly by the volume of FDI inflows.
- **Active policies:** developing an active FDI attraction policy involves, first, defining the types of investment needed to achieve the desired benefits then, within the options available, creating the conditions to attract such investment, over and above the market or endowment of natural resources. Generally speaking, such strategies aim to attract efficiency-seeking firms that produce goods and services for export and which can generate additional benefits, such as production linkages. In this type of promotion, micro variables (such as factor costs and availability) are more important and competition among countries is stiffer.
- **Integrated policies:** FDI brings the greatest benefits when the respective investment-attraction policies are integrated with development policy. When the two are coordinated and integrated, a country can generate or enhance the conditions that make it attractive to investors, on the one hand, and make the most of the potential benefits of FDI, on the other. In special cases, such as

Ireland and Singapore, FDI has become a development axis around which the country's other policies are aligned. In less exceptional cases, FDI has helped to develop sectors that are strategically important for the country's productive development plan.

Governments may find it useful to consider which policy category suits their respective country best, depending on where its advantages and aspirations lie. In view of the mounting and increasingly sophisticated competition among countries to attract FDI, however, a more active strategy to attract investment is usually the best means to secure FDI with the most powerful multiplier effects and extract the maximum benefit from existing investments. Even though this is a relatively recent phenomenon, countries are making increasingly proactive and determined efforts to attract foreign firms' best investment projects. The changes occurring in the institutional structure of FDI promotion and facilitation clearly reflect this new situation. Although institutional arrangements vary from one country to another, a common denominator of successful investment promotion has been the creation of an agency or department specifically for the task (Loewendahl, 2001). In 2004 there were at least 160 national investment promotion agencies (IPAs) and over 250 at the subnational level (OECD, 2005). The newness of this trend is apparent in the fact that two thirds of these agencies were created in the final decade of the

twentieth century, between 1990 and 2000 (UNCTAD, 2001). Such agencies are working in an increasingly competitive international environment, in which they need to become "professional sales machines for their country or region" (MIGA/GDP Global, 2005).

The countries of the region are no exception in this regard. Indeed, 30 of the region's 33 States have now set up IPAs or equivalent institutions to centralize their promotion activities. Nevertheless, compared to the policies implemented by developed countries, economies in transition (such as Hungary and the Czech Republic) and the developing Asian countries (namely Singapore, Republic of Korea, China, Malaysia and Thailand), the efforts made in the Latin American and Caribbean countries have been weaker in terms of definition of explicit policies, integration with other development policies, promotion exercises, facilitation mechanisms and targeting of activities.

This chapter analyses the state of play as regards investment attraction policies in Latin America and Caribbean, particularly their degree of proactivity in attracting FDI. The analysis is based on a set of surveys and interviews conducted with 15 IPAs in the region,¹ in three relevant areas: (i) promotion policies, (ii) incentives policies, and (iii) targeting strategies. The rest of the chapter further examines these policies and sets out conclusions and recommendations.

B. Promotion policies: investment promotion agencies (IPAs)

One of the countries' main challenges in attracting FDI is potential investors' lack of familiarity with the attributes and advantages of a particular location or country. This translates into: (i) information asymmetries as regards the features of a location and the criteria defined by investors;

and (ii) high learning and set-up costs for firms newly arrived in the country. The usual means of addressing these problems is for countries, or even provinces and regions, to establish investment promotion agencies, departments or programmes.

¹ For the purposes of this enquiry, the IPA (or equivalent) in each country was taken as the main contact and source of information. In the 33 Latin American and Caribbean States, 30 IPAs were identified operating at the national level (excluding Haiti, Suriname and Saint Kitts and Nevis). All these IPAs were invited to take part in the research and 15 accepted. The study included a survey and an interview, consisting mainly of open questions. The methodology has certain limitations: since only the main IPA in each country was contacted, the survey does not necessarily reflect the complexity of the institutional structure of investment promotion; this is particularly true in the case of countries with federal forms of government.

1. A changing institutional structure

Since investment promotion is a fairly incipient activity in the region, it is interesting to look at how the institutional structure of promotion agencies has changed, especially in the last five years (see table II.1).

Table II.1
MAIN INSTITUTIONAL CHANGES IN 2000-2005, BY COUNTRY

Type of institutional change	Number of countries	Countries
Creation of investment promotion agency	3	El Salvador, Guatemala, Saint Vincent and the Grenadines
Creation of investment promotion functions or programmes	3	Ecuador, Chile, Saint Lucia
Creation of new institutional structure by merger or absorption	2	Peru, Colombia
Internal restructuring and/or changes in reporting structure	4	Jamaica, Panama, Paraguay, Uruguay

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of surveys of investment promotion agencies.

Interestingly enough, of the 15 agencies included in the study, 12 were created during this period, have undergone major changes or are in the process of institutional reorganization. In Uruguay an inter-ministerial commission was recently created to streamline the different institutions working in activities related to investment promotion. Paraguay is processing a new decree that will shift the National Department of Export and Investment Promotion (ProParaguay) from the Ministry of Foreign Affairs to the Ministry of Trade and Industry. And Panama's Ministry of Trade and Industry has undertaken an administrative restructuring that will affect its National Production and Investment Promotion Department. In all three countries, these changes were occurring while this research was under way. The Government of Saint Lucia reorganized its National Development Corporation (NDC), focusing its activities on FDI and local investment, and developed a new strategic plan for 2005-2008. The Jamaica Promotions Corporation (JAMPRO) was heavily restructured between 2001 and 2003 in terms of organization and staff.

Guatemala, El Salvador, Saint Vincent and the Grenadines, Ecuador and Chile have all created investment

promotion agencies or programmes in the last five years. The Guatemalan agency Invest in Guatemala started up only in 2004. In 2000, El Salvador launched Promoting Investment in El Salvador (PROESA), which was rolled with the export promotion agency EXPORTA into the National Exports and Investments Promotion Commission (CONADEI) in 2004, although it has retained an autonomous image. In Saint Vincent and the Grenadines, National Investment Promotions Incorporated (NIPI) was created in 2003 to foster investment and exports.

In late 2001, Ecuador created a Foreign Investment Department as part of its Export and Investment Promotion Corporation (CORPEI), following a structural analysis carried out with the support of the United Nations Conference on Trade and Development (UNCTAD). Chile abandoned its passive stance on FDI in 2000, when the Foreign Investments Committee (CINVER) took a more active role in investment promotion and the functions of the Production Development Corporation (CORFO) expanded to include investment promotion organized around geographically and sectorally targeted programmes.

In Peru and Colombia, the new institutional structure was shaped by mergers and absorptions. Peru's private investment promotion agency PROINVERSION was created in 2002 with the merger of three agencies working on investment-related activities. In early 2005, the semi-public agency Invest in Colombia (COINVERTIR) was absorbed into the public export promotion institution PROEXPORT, which thus acquired new investment promotion functions.

Brazil has also made significant changes² to its investment promotion machinery in recent years. The existing Investment Attraction Programme was established after a series of institutional changes at the national level, and its promotion component has been implemented by the Export and Investment Promotion Agency (APEX) since 2005, while the business facilitation aspect of the programme is conducted by the Investments Bureau, which reports to the Office of the President. The two institutions coordinate with the different subnational IPAs, which have taken on an important autonomous role in attracting investment into their respective States.

² Although Brazil is not covered in this chapter, it must be mentioned here because it is one of the region's largest FDI recipients.

2. Organization and financing of IPAs

As may be appreciated from table II.2, the countries examined exhibit a wide variety of institutional arrangements for investment promotion. Only five of these countries —Bolivarian Republic of Venezuela, Costa Rica, El Salvador,³ Guatemala and Peru— have agencies whose sole function is to promote foreign investment. In the other countries, this function is generally combined with export promotion⁴ (except in the case of Chile).⁵

From the point of view of ownership and administration, nine of the agencies examined are public institutions, four are mixed or semi-public and only two, those of Costa Rica and Ecuador, are private non-profit organizations. The forms of financing of these IPAs are also varied: some are funded from the public budget, some by voluntary or mandatory contributions from firms or donors, by returns on their own assets and investments, services lent or a combination of the above.

3. Main functions, activities and resources of IPAs

The IPAs surveyed carry out quite a broad spectrum of functions, including those considered primary (analysis of opportunities, country image, targeted marketing, investor services, post-investment follow-up and services), as well as complementary activities (improvement of business climate, advising authorities, administering incentives, and enhancing local firms' competitiveness), as shown in table II.3.

The agencies' responses were more varied with regard to the frequency of those functions, which is a better way to

measure promotion efforts. Investor services is, on average, the most frequently performed function and administration of incentives is the least frequent. Notably, administration of incentives by the agencies consists only of support for firms applying for the benefits on offer, since none of those surveyed has a mandate to deliver any sort of incentive directly. This is the responsibility of other institutions, except in the case of Chile, where CORFO manages two programmes to attract and promote investments, through which it can provide targeted incentives to investors.

³ In the case of El Salvador, although PROESA has been part of CONADEI since 2004, it is grouped in this category because it maintains a separate image.

⁴ Although it might appear efficient to pool the functions of export promotion and investment attraction, especially in view of work with external markets and firms and the temptation to share resources, they are two totally different matters. Best practice indicates that the two functions should be dealt with separately (MIGA, 2005). This research did not inquire how the different agencies separate these functions in practice (beyond having two separate departments in their organigrams), however; attention is merely drawn to the point.

⁵ Chile's CINVER is the institution officially responsible for investment promotion. However, its main function is to administer the legal mechanism, which affords signatory foreign firms stability in a range of investment-related aspects. In addition, jointly with CINVER, CORFO implements two programmes to attract and promote investment. One of these (*Todo Chile*) takes a geographical approach to attracting investment into the regions and the other takes a sectoral focus, seeking to attract technology-intensive investments. For methodological reasons, CINVER was considered as the sole informant, but mention will be made of CORFO programmes where relevant.

Table II.2
ORGANIZATION AND FINANCING OF IPAs

Country / Institution	Ownership	Form of funding	Notes
Agencies that promote investment only			
Costa Rica Costa Rican Development Initiatives Coalition (CINDE)	Private (non-profit)	Mixed (assets and donor contributions)	
El Salvador Promoting Investment in El Salvador (PROESA)	Public	Public budget (including the rust fund used to set it up)	PROESA was created in 2000 and retains an independent image, but was absorbed in 2004 the National Export and Investment Promotion Committee
Guatemala Invest in Guatemala	Public	Public budget (World Bank)	Created in 2004
Peru Private Investment Promotion Agency (PROINVERSIÓN)	Public	Self-funded (autonomous funding)	Main function is to administer the public tender process, which provides it with an income
Venezuela (Bolivarian Republic of) (CONAPRI)	Mixed (Public-private)	Mixed (public-private assets)	
Agencies that promote exports and investment			
Colombia PROEXPORT Colombia	Semi-public	Self-funded (assets)	COINVERTIR became part of PROEXPORT in early 2005
Ecuador Export and Investment Promotion Corporation (CORPEI)	Private (non-profit)	Mixed (public-private)	FDI department set up in 2001
Jamaica Jamaica Promotions Corporation (JAMPRO)	Public	Mixed (public, services)	Around 17% of the budget is funded by revenue-generating projects
Paraguay National Department of Export and Investment Promotion (ProParaguay)	Public	Public budget	Reporting hierarchy of ProParaguay now being moved from Ministry of Foreign Affairs to the Ministry of Trade and Industry
Saint Vincent and the Grenadines National Investment Promotions Incorporated (NIPI)	Semi-public	Self-funded (assets, services)	Publicly-owned enterprise, part of whose budget is funded by income from services
Uruguay Export and Investment Promotion Institute (URUGUAYXXI)	Semi-public	Public budget	Inter-Ministerial Commission created to propose measures to streamline the different promotion institutions
Other types of investment promotion institutions			
Chile Foreign Investment Committee (CINVER) (1)	Public	Public budget	In 2000, CORFO created targeted investment promotion programmes
Mexico National Bank for Foreign Trade (BANCOMEXT) (2)	Public	Self-funded (autonomous financing)	
Panama Ministry of Trade and Industry (3)	Public	Public budget	The National Production and Investment Promotion Department, which reports to the Office of the Under-Secretary for Foreign Trade, was considered an IPA
Saint Lucia National Development Corporation (NDC) (4)	Semi-public	Self-funded (assets and investments)	Restructured in 2005 to focus on investments

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

Note: The main function of the institution is: (1) to administer the legal framework of foreign investment; (2) promotion and financing of foreign trade; and (3) and (4) economic development, including export promotion.

Table II.3
FUNCTIONS OF IPAs

Functions	IPAs		Average frequency of each function ^a	Average staff allocation ^b
	Number	Percentage		
Investor services (assistance in assessing and selecting location, legal requirements and procedures, and so forth)	15	100	4.6	20.0%
Marketing programmes (missions, fairs, meetings, and so on)	15	100	4.2	16.7%
Analysis of opportunities (management of business intelligence, databases, sectoral analyses, etc.)	15	100	4.1	15.7%
Country image (advertising or other broad scope actions)	15	100	3.9	12.5%
Post-investment follow-up and services (after care, problem-solving, and so forth)	15	100	3.7	11.4%
Design, consultancy services for authorities and/or policy advocacy	15	100	3.6	8.5%
Improvement of local business climate	14	93	3.5	8.3%
Development and enhancement of local firms' competitiveness.	12	80	2.7	4.8%
Administration of incentives (evaluation, allocation and/or disbursement)	7	47	1.4	2.2%

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

^a Scale: 5: very high, 4: high, 3: medium, 2: low, 1: very low, 0: nil. Out of a total of 14 responses.

^b Of 13 IPAs which supplied data.

In relation to promotion activities as such, investor reception and services is the function IPAs report conducting most frequently. It also accounts for the largest proportion of their resources (see table II.4). This is positive to the extent that it reflects evaluation visits to the country by

potential investors, but it also shows most agencies are tending to adopt a receptive rather than a proactive stance. Promotional activities abroad, such as visits to foreign firms, seminars or participation in fairs or events, are less frequent and command fewer resources.

Table II.4
MAIN MARKETING AND INVESTOR SERVICES ACTIVITIES

Activities	IPAs		Average frequency of function ^a	Average resource allocation ^b
	Number	Percentage		
Reception and assistance for missions of potential investors	15	100.0	4.7	2.5
Generation of promotional information and products de (brochures, documents, etc.)	15	100.0	4.5	2.7
Administration of a website	15	100.0	4.2	2.2
Visits to firms and meetings with executives abroad	15	100.0	3.8	2.3
Participation (exhibitions) at fairs abroad	15	100.0	3.8	1.9
Missions abroad	11	73.3	3.4	1.8
Mailing or telemarketing campaigns	13	86.7	2.9	1.6
Organization of promotional events abroad (seminars, breakfasts, and so on)	13	86.7	2.8	1.8
Advertising in international media	11	73.3	1.7	1.0
Contract with public relations agency abroad	6	40.0	0.8	0.8

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

^a Scale: 5: very high, 4: high, 3: medium, 2: low, 1: very low, 0: nil. Average of 15 responses.

^b Scale: 3: high, 2: medium, 1: low, 0: nil. Average of 12 IPAs which supplied data.

The individual information, however, reveals a group of countries (Chile, Costa Rica, Mexico, Paraguay and Saint Vincent and the Grenadines) that afford priority to activities abroad, which they carry out very frequently. The agencies in Chile, Costa Rica and Mexico also have the highest budgets of all the countries examined. CINDE in Costa Rica has a total staff of 27 and over 20 years' experience in investment promotion. Mexico's investment promotion effort is built mainly on the structure of the National Bank for Foreign Trade (BANCOMEXT), whose investment promotion management has access to the Bank's broad international network. And Chile has launched a broad range of promotion programmes with the help of representatives abroad and has created 12 regional agencies throughout the country. The CORFO investment promotion staff (handling both local and foreign investments and including the regional agencies) and the CINVER personnel combined number 72. At the other extreme is Paraguay, with the lowest budget and smallest staff endowment of all the agencies examined. Although this research did not directly evaluate the effectiveness

of the agencies' work, it would be hard to imagine that this agency could operate above minimum thresholds, given the high costs involved in conducting promotion activities abroad.

Colombia and Ecuador are the two least outward-looking countries. Both have afforded priority to internal, receptive activities, such as investor services, promotion by means of a web page or the generation of information, rather than proactive activities conducted abroad.

An agency's capacity for action is determined, among other factors, by the size of its budget and human resources endowment. The findings of a recent study (Morisset and Andrews, 2004) suggest that agencies with a small budget have no significant impact in terms of securing investment. Moreover, minor budget increments also fail to produce any great effect in this regard.

In general, except for Chile, Costa Rica, Mexico, El Salvador and Peru, the budgets and human resource endowments of the IPAs analysed are below the world average (see table II.5 and box II.1).⁶

Table II.5
IPAs BY RELATIVE PROACTIVITY OF PROMOTION ACTIVITIES AND BUDGET

		Proactivity of promotion activities ^a Relative position of IPAs										
		Least proactive						Most proactive				
		5	6	7	8	9	10	11	12	13	14	15
Budget	More than US\$ 2 million	O Peru (177) ^b						O El Salvador (29)		O Chile (32) ^c		
	US\$ 1 million - US\$ 2 million							O Guatemala (10)		O Costa Rica (27)		
	US\$ 500,000 - US\$ 1 million	O Colombia (14)		O Uruguay (6)		Venezuela (Bolivarian Republic of) (17)						
	Less than US\$ 500,000	O Ecuador (5)			O Saint Lucia (19)	O Jamaica (6)	O Panama (11)		O Saint Vincent and the Grenadines (9)			
		O Paraguay (3)										

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of surveys of investment promotion agencies.

() Indicates the total number of employees devoted to FDI promotion.

^a The surveyed agencies' reports on the frequency of their promotion activities abroad were used to establish comparisons of proactivity. The matrix shows their relative positions.

^b Around 80% of the agency's human and financial resources are devoted to administration of the public tenders process.

^c Estimate of staff and budget of CINVER and of central and regional CORFO offices and CORFO representatives abroad working on investment promotion. Including promotion of national investments, the total would be 72 staff.

^d Refers to the central office only. BANCOMEXT has 80 staff in its 31 overseas offices, whose functions include investment promotion.

⁶ A number of difficulties and limitations arise in the comparison of budgets and staff endowments among IPAs, since only four of these agencies are devoted solely to investment promotion.

Box II.1

COMPARATIVE ANALYSIS OF BUDGET AND STAFF ENDOWMENT OF IPAs

A survey conducted by UNCTAD (2001) indicates that in 1999 the average annual budget of an IPA was US\$ 1.1 million, and it was funded mainly by the public sector. Budget varies considerably from one agency to another, however: 8% of agencies, mainly in least developed countries, have a budget of less than US\$ 100,000, while 21% operate with a

budget of over US\$ 5 million. With regard to staff endowments, the UNCTAD survey reports that agencies in OECD countries employ an average of 22 people; least developed countries, 33; economies in transition, 26; and other developing countries, 29.

A more recent study (Morisett and Andrews, 2004) surveyed 75 IPAs in 58

countries in early 2002. It found that the average budget for FDI promotion was US\$ 2.6 million per year, but 50% of agencies have a budget of no more than US\$ 650,000. A typical agency in a developing country has an annual budget of less than US\$ 450,000 and employs a team of 10 professional staff.

IPA BUDGETS BY COUNTRY INCOME LEVEL, 2001

(Dollars)

	Income level		
	Low	Middle	High
Average	548 500	1 237 000	9 382 100
Minimum	28 404	33 300	283 155
Maximum	1 488 833	5 593 000	27 300 000
Median ^a	287 421	569 574	9 316 800

Source: Jacques Morisett and Kelly Andrews-Johnson, "The effectiveness of promotion agencies at attracting foreign direct investment", *Foreign Investment Advisory Service Occasional Paper*, No. 16, Washington, D.C., World Bank, 2004.

^a Median: 50% of agencies have a budget below the median.

In relation to resource endowment, Morisett and Andrews found that agencies in the highest-income countries employ 18 professional staff on average; those in upper-middle-income countries employ an average of 22 professional staff; those in lower-middle-income countries 15; and those in low-income countries only 11.

The medians for these groups are 10, 8, 7 and 8, respectively. In terms of standards and best practices, the Multilateral Investment Guarantee Agency (MIGA) (2005) proposes that an IPA should have a minimum endowment of 25 staff (in the central office alone).

Countries seeking to increase the

amount of FDI flowing into their respective economies need to ensure that the resources and staff devoted to FDI policy are adequate to meet its objectives. In this regard, it is useful to refer to the experiences—successful or otherwise—of neighbouring countries and others that have faced similar challenges.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations Conference on Trade and Development (UNCTAD), "The world investment promotion at a glance: a survey of investment promotion practices", ASIT Advisory Studies, No. 17 (UNCTAD/ITE/IPC/3), New York, 2001; Jacques Morisett and Kelly Andrews-Johnson, "The effectiveness of promotion agencies at attracting foreign direct investment", *Foreign Investment Advisory Service Occasional Paper*, No. 16, Washington, D.C., World Bank, 2004 and Multilateral Investment Guarantee Agency (MIGA), "Developing an investment promotion agency" [online] FDI Promotion Center, World Bank, 2005 <<http://www.fdipromotion.com/toolkit/>>.

4. Benefits of promotion activities

Agencies have a varied perception of which activities have yielded the largest returns in terms of attracting investors (see table II.6).⁷ Costa Rica's CINDE, for example, affords much importance to investment aftercare, as a source of reinvestment and information on other firms with plans to invest. As well, the existence of satisfied firms willing

to pass on their experiences greatly facilitates the task of promoting a country or region. The experience and know-how built up over years of participation in trade fairs and shows have also helped the agency to extract greater benefits from these events, enabling it to work in a more aggressive and targeted manner.

⁷ Little information is available on the effectiveness of IPA work. One recent study (Morisett, 2003) attempted to measure the impact of IPA work, or the cause-and-effect relationship between this work and FDI flows, and found a positive correlation in both cases. The study also found, however, that agencies' effectiveness depends on the setting in which they operate, i.e., an agency in a country with a poor investment climate is less effective in attracting investments.

Table II.6
**COSTA RICA, CHILE AND COLOMBIA: THREE MAIN ACTIVITIES
 OR FUNCTIONS THAT HAVE PROVIDED GREATEST RETURNS
 IN TERMS OF FDI ATTRACTION**

Costa Rica (CINDE)

1. Aftercare: for the expansion projects of firms that ave already invested and the referrals these generate
2. Participation in trade fairs
3. Visiting missions to firms abroad

Chile (CINVER)

1. Generation, compilation and dissemination of clear, concise and accurate information, in English, mainly in the form of publications, brochures, documents and websites
2. Organization of events in Chile and abroad, with the participation of local businesspeople, seminars, and conferences
3. Reception and services for missions of potential investors

Colombia (COINVERTIR-PROEXPORT)

1. Preparation of promotional material
2. Investment facilitation
3. Investment climate

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of surveys of investment promotion agencies.

CINVER of Chile has expended great efforts to compile, generate and divulge information on the country to meet the needs of foreign investors. Given that Chile's more proactive stance on investment promotion is recent (2000), as part of its earlier efforts the agency prepared a register of what the country had to offer and made this information available in different formats (brochures, documents, website, and so forth). CINVER also began to promote Chile abroad, by organizing promotional events (seminars, workshops, and so on) with the help of local businesspeople.

Colombia's COINVERTIR has tended to adopt a more inward-oriented stance (though this might change now that it forms part of PROEXPORT), having found that its best returns in terms of FDI attraction are provided by its promotional materials, investment facilitation and efforts to enhance the business environment.

5. Investment promotion offices abroad

A permanent presence close to potential investors, through offices or representatives abroad, greatly facilitates promotional activities. However, given the high costs involved in maintaining an office abroad, especially in a developed country, few countries have overseas offices devoted exclusively to investment promotion.⁸

Six of the agencies surveyed have overseas offices that combine investment promotion with other responsibilities (which are afforded greater importance). This is the case of the overseas branches of the IPAs in Colombia, Ecuador, Guatemala, Mexico and Paraguay, whose main function is export promotion. The largest overseas office network is that of BANCOMEXT of Mexico, with 31 offices, eight of which are located in the United States.

Guatemala created a programme of commercial attachés for investment and tourism (PACIT), with the aim of promoting exports, investment and trade liberalization and providing support services for international marketing by Guatemalan businesses. This programme is described as the pooling of efforts by the public and private sectors to provide export firms

with access to the services of a network of commercial offices abroad. PACIT encompasses five ministries, a bank and nine business organizations.

Chile, Costa Rica and Saint Lucia have developed models based exclusively on investment promotion. Through CORFO, Chile has devised a representation-based scheme by means of contracts with firms that take on its promotion functions. It has such representatives in Spain (Barcelona), Sweden (Stockholm) and the United States (Boston) and is considering the possibility of securing representation in Italy and Germany. CINDE of Costa Rica has an office in New York devoted solely to investment attraction. Both Chile and Costa Rica had offices in Silicon Valley in the United States, but neither is now operational. The other IPAs report neither offices nor representation abroad.

All the countries coordinate in some way or other with their embassies or diplomatic representatives. In some cases, specific agreements are drawn up or training is conducted to help diplomatic staff undertake investment promotion functions.

⁸ OECD countries had an average of seven such offices in 2001 (UNCTAD, 2001). Countries where FDI promotion is one of the main pillars of development policy have the largest networks of investment promotion offices abroad. Ireland, for example, has 13 overseas offices, of which 5 are located in the United States alone.

6. Subnational offices

IPAs exist at the subnational level, in States, regions, provinces or departments, for at least two main reasons: (i) just as countries compete to attract investment, different locations within a country compete to secure those investments; (ii) investors need detailed and specific information on the different locations within a country. The work of assessment is facilitated by skilled staff based in those locations.

IPAs form part of a wide variety of types of institutional arrangements. In some cases, subnational agencies report to a central office. This is the case of CORPEI in Ecuador (with three offices); BANCOMEXT in Mexico (26 offices), though investment promotion is not this institution's main function; PROINVERSION in Peru (2 offices);⁹ and JAMPRO in Jamaica (1 office).

In other cases, the States or provinces themselves create agencies or set up teams to facilitate investment. It might be supposed that this is more common in more spread out and federally structured countries such as Mexico, especially since Guatemala, Costa Rica and Saint Lucia do not have regional offices. Countries such as Uruguay, Paraguay and Chile do report having promotion offices at the regional level, however.

The cases of the agencies in Paraguay and Chile are interesting, since both have agreements with regional governments. ProParaguay signed an agreement of cooperation and assistance on export and investment

promotion with the 17-member Council of Governors. In Chile's case, the CORFO regional investment promotion programme was established in the framework of a joint funding agreement between CORFO and the 12 regional governments, enabling investment promotion teams to be set up in each of the country's regions. The offices report to CORFO, but are partly funded by the regional governments. The Bolivarian Republic of Venezuela, Colombia and Uruguay have autonomous subnational offices, which report to regional or State governments.

In short, the IPAs examined exhibit a broad variety of institutional arrangements, both in terms of their legal set-up and administrative accountability and their funding. Their functions and activities are similar to those performed by such institutions in other parts of the world. Generally speaking, however, their stance is more receptive and domestically-oriented than proactive and outward-looking. This is illustrated by the fact that very few countries have overseas offices devoted solely to investment promotion. Of course, the institutional fabric of investment promotion is relatively young and still being consolidated, so institution-building remains to be done. Consequently, in combination with the scarce resources generally available to IPAs, it may be supposed that their capacity to perform efficiently and effectively is compromised.

C. Incentives policy

From the point of view of a country wishing to attract FDI, the ideal situation is one in which the country can offer conditions that will meet the expectations of a potential investor and better those offered by its competitors (including incentives). In such a situation, no incentives need be offered. It is uncommon for one

location to be so clearly superior to another, however. The countries and cities that have secured a place on the shortlist are usually quite similar, competitively speaking. Hence, the possibility of securing incentives can influence a firm's decision on where to locate its operations.

⁹ In addition, as a result of the new legislation on decentralized promotion, each of Peru's 24 regions will soon form its own promotion agency.

The rationale and justification for incentives is that they can correct market failures and harness positive externalities for the host country's benefit. The right incentives can alleviate the risk and uncertainty facing a new investor, whether local or foreign, as well as the additional costs that those factors represent, which might otherwise be a barrier to investment. In the case of foreign investors, incentives can also be used to increase a country's cost-attractiveness vis-à-vis other regions competing for a particular project. The benefits that the investment will bring, whether in such general terms as technology transfer or job creation, or in more specific terms such as the positive impact of the first

foreign firm to set up in business in the country,¹⁰ justify the provision of incentives provided that the cost does not exceed the anticipated social returns.

Incentives take different forms, but may generally be classified as fiscal or financial. Fiscal incentives are temporary or permanent reductions in or exemptions from different kinds of taxes. Financial incentives consist of direct subsidies that help to lower the cost of setting up or operating a project—fixed assets, training, utilities, and so on—in the form of grants, reductions in the cost of factors of production or services, or provision of the necessary infrastructure.

1. Incentives offered in Latin America and the Caribbean

The incentives countries use to attract FDI are available to local investors as well although, in general, foreign investors make greater use of them. Most of the countries examined use mainly fiscal instruments,¹¹ through which they aim to attract investments by efficiency-seeking, export-oriented firms (see table II.7). The effectiveness of fiscal instruments in securing this type of FDI is not proven, however.

Table II.7
MAIN INCENTIVES FOR FDI

Type of incentive	Number of countries for which this is the main incentive
Duty-free regime (including exemptions from income tax)	6
Tax exemptions (from tax on corporate profits)	5
Maquila legislation	1
Subsidies (targeted)	1
Others	2

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of surveys of investment promotion agencies.

Colombia, Costa Rica, Ecuador, El Salvador and Guatemala have duty-free regimes as their main incentives for investment. These regimes allow the free passage

of goods without payment of import and export duties, in addition to a series of tax benefits, which in general include cuts in or exemptions from corporate tax and levies on profit remittances. Uruguay also has a duty-free law (which provides for income tax exemptions), but URUGUAYXXI finds that its temporary goods admission scheme has brought the greatest returns.

Paraguay promotes export-oriented investment on the basis of maquila legislation, which regulates the establishment of local and foreign commercial activities producing for export through outsourcing, using local labour and raw materials. Firms that operate under this scheme are subject to a single tax rate of 1% levied on the maquila contract and related activities. Given that the purpose is to export, no more than 10% of the goods produced may be distributed on the domestic market.

In Bolivarian Republic of Venezuela, Jamaica, Panama, Saint Lucia and Saint Vincent and the Grenadines, the main incentives are tax-based, with the size of the cut or exemption (mainly in corporate taxes) depending the sectors to be supported.¹² For example, the main incentive for investors in Saint Lucia is an exemption from corporate tax for up to 15 years. The number of years' exemption depends on the contribution the company makes to the economy, measured as local value added. Other factors are the amount of capital invested and the

¹⁰ The strategy of "follow-the-leader" is common with regard to FDI. A number of firms are known as "pioneers" because they seek out locations that offer good opportunities. Once they have set up, others follow. The pioneer firm assumes the learning costs of being the first foreign investor.

¹¹ For the purposes of comparison, this section sets out a simplified account of the incentives that reporting agencies found to have the greatest impact. Each country offers a broader range of incentives which is more complex to compare and thus beyond the scope of this work.

¹² Bolivarian Republic of Venezuela and Jamaica also have duty-free zones.

export orientation of the investments. This benefit is available for investments in the productive sectors of the economy and is extended especially to firms that export manufactures. In the Bolivarian Republic of Venezuela, income tax law provides for an investment incentive in the form of tax discounts on a percentage of the new investment. Investments in industrial and agribusiness sectors, construction, electricity, telecommunications, and science and technology qualify for a reduction of 10% of the amount invested. Investments in tourism enjoy a markdown of 75%; those in agriculture, fishing and fish farming, 80%; and investment in hydrocarbons and related sectors, 8%. The President of the Republic may also fully or partially excuse from payment of income tax profits obtained in sectors that are considered particularly important for national development, generate higher employment capacity or set up in particular regions of the country. Export-oriented investment is not specifically promoted in the Venezuelan scheme.

Mexico, Chile and Peru are special cases, for different reasons. Unlike the other countries, Mexico offers no income tax cuts or exemptions, although it does use other means to promote investment. Legislation on the promotion and operation of the maquila industry allows the temporary importation of goods to be used in the conversion, manufacture or repair of merchandise for export, without payment of general import duty, value-added tax or countervailing duties, as the case may be. This mechanism offers no special incentives but, like similar regimes in other countries, allows the temporary entry of goods without payment of the corresponding taxes.¹³ In Mexico, the main incentives are offered by States and municipalities, which have the autonomy to promote their respective regions and negotiate special conditions with investors. Generally speaking, this sort of incentive includes local tax cuts or exemptions, the supply of access infrastructure, provision of land free or at low cost, and cuts in utility rates.

Chile has a mixed scheme, based on tax cuts and financial incentives to promote targeted investment.¹⁴ Chile has no generalized mechanism of tax exemptions for attracting FDI (which has been a frequent topic of discussion in Government, academic and business circles), having opted for a strategy based on promotion of its structural advantages. However, it does have some mechanisms for tax exemptions and cuts and financial incentives for new investors, intended to foster the development of geographically isolated or economically

depressed areas, and of specific sectors in those areas. The Government is also promoting a programme to attract investment in technology-intensive ventures, offering non-refundable financial incentives to co-finance fixed assets, long-term rentals and human-resource building for such projects. Peru has adopted a similar stance to Chile's, since it extends fiscal incentives for two sectors only —agribusiness and aquaculture— and maintains duty-free regimes that are not significant from the point of view of attracting FDI.

The most significant incentives in each country can be categorized by the way they are allocated and the scope of the objective at which they are aimed.

(a) Allocation of incentives

Incentives can be allocated in one of two ways: automatically or on a case-by-case basis. Where they are allocated automatically, a firm whose investment project meets the established requirements (for which it has to submit a proposal for individual assessment), will qualify for pre-defined benefits. This is the system employed in most of the countries whose incentives are based on duty-free areas, maquila legislation or sectoral tax exemptions. The role of decision makers is to approve or reject applications for subsidies.

Where incentives are allocated on a case-by-case basis, the subsidy is granted as a function of the investment project's merits, with certain evaluation criteria being established in advance. The amount of the subsidy depends on the outcome of the evaluation. The advantage of managing subsidies in this fashion is that support can be targeted on the basis of expected impacts, which optimizes the use of public resources. The disadvantage is that the need for ad hoc evaluation makes the subsidies more expensive to administer and can invite difficulties with corruption.

In turn, case-by-case allocation of incentives is managed in two different ways: either the subsidy mechanism is regulated and institutionalized, with clear and transparent reporting criteria, or it not institutionalized or regulated and incentives are allocated as part of an individual negotiation with no pre-set conditions. Chile's programme to attract technology-intensive investments and Saint Lucia's tax exemption mechanism come into the first of these two categories. The second is more common in countries whose States or municipalities have the autonomy to custom-assemble incentive packages for individual firms.

¹³ The great success of the maquila industry in Mexico is due mainly to the country's cost advantages with respect to the United States, and to the effort and special treatment Mexico has expended on developing this industry.

¹⁴ Chile has two duty-free zones, but they are not export-oriented. On the contrary, their main function is to store imported goods for subsequent distribution on the domestic market or re-export.

(b) Scope of incentives

Incentives can be general in scope (such as support for new investment in duty-free areas) or they can target a particular sector or be provided to meet a specific objective (such as subsidies for human resource training in Chile's technology-intensive investment programme).

General incentives tend to coincide with automatic allocation, while targeted incentives are more commonly allocated on a case-by-case basis.

Countries planning to include incentives in their investment promotion strategy need to establish, among other things, the type of incentives that are best suited to their objectives. Generally, the more sophisticated the type of investment they aim to attract, such as investment in research and development, the more targeted the incentives have to be. For example, Ireland has an attractive rate of taxation (12.5%, the lowest among the European Union and OECD countries), which is combined with a range of financial incentives directly operated by IDA Ireland. In its negotiations with potential investors, IDA can offer a package of incentives including grants for hiring, training, research and development (R&D), and fixed assets. The main criteria for defining the size of grants are the quality of the employment created and the project's location. Where incentives are targeted in this way, it is important to define the requirements and size of the subsidy clearly and transparently, in order to reduce the risk of unleashing

an "incentives war" between countries or even between States within a country,¹⁵ or of offering an incentive that outweighs the project's social returns.

Another example is the Czech Republic, which created an incentives programme in 2004 to attract investment in technology centres that could feed into productive activities. To facilitate this type of activity, whether locally- or foreign-owned, the Government subsidizes as much as 50% of the investment costs in the first five years or up to two years' of the new employees' wages, as well as up to 35% of specific training costs and 65% of general training.

Incentives need not necessarily take the form of standardized financial subsidies like the above examples, since, among other reasons, there may not be a sufficient budget for such an approach (in 2004, IDA had a budget of over 65 million euros for incentives). Sometimes countries devise incentives which are neither initiatives favouring a single firm nor broad enough to be categorized as general policies, but nevertheless help to enhance specific features and narrow the gap between the conditions available and the requirements of foreign investors. For example, Costa Rica and El Salvador have instituted training programmes to meet the growing demand for skilled personnel (bilingual technicians) in the international services sector, and Chile has prepared a register of fluent English-speakers in order to facilitate the recruitment process for firms that need bilingual staff.

2. Effectiveness of incentives

Questions that often arise are whether incentives really influence investors' decisions, whether a firm was afforded more incentives than it needed and whether an investment would have gone ahead anyway, with or without the subsidy. It is difficult to answer these questions precisely, given the information asymmetries in this area.¹⁶

The empirical evidence compiled by a host of researchers suggests that incentives are not particularly important to firms at the first stage of the country selection process. During this stage, when the longlist of investment options is being drawn up, the choice

revolves around structural advantages. Incentives do become more important, however, especially for efficiency-seeking investments, when firms are assessing and comparing shortlisted countries. Thus, incentives are not the main factor in the decision, but they do appear to have an influence on the final choice of one location over another.

None of the countries surveyed provided information on ex post assessments of the impact generated by projects they had subsidized. A few countries had information relating to the number of projects, jobs created and value of exports.

¹⁵ A classic example of this was the competition between Brazilian States to attract automobile manufacturers, which is studied in Oman (2000) and Charlton (2003).

¹⁶ The assessment methodology employed by countries such as Ireland (on which Chile based its investment project assessment model), explicitly includes an adjustment factor that takes into account the possibility that the grant was not necessary.

Although it is a complex undertaking to establish the real need for incentives and the outcomes of investments that have benefited from them, it is important to attempt such an exercise in order to ensure the best possible results within the limitations of the scarce resources available to the region's countries.

In short, the ideal situation from the point of view of overall gain would be one in which the countries could compete on the basis of their structural advantages, without offering incentives. Given, however, that countries have a strong motivation to offer incentives (whether fiscal or financial) as a means of making

themselves more attractive to potential investors, in practice, incentive-free competition does not occur. Having decided to offer incentives, whether to local or foreign firms, a country should review its existing schemes in relation to the type of investment it wishes to attract. As the competition for better quality investments mounts, incentive schemes need to become more complex and sharply focused. Countries that propose to attract high-quality investment should therefore develop more targeted mechanisms, always ensuring that the social returns on the investment are greater the costs associated with the incentives.

D. Targeting strategies

The third type of active policy reviewed here is targeting. This is understood to refer to the decision of a country (or IPA) to prefer a particular type of investment, on the basis of certain criteria. Countries adopt targeting strategies for at least two reasons. The first is shortage of resources or need to use them efficiently. In this case, the emphasis is on the practical aspect; given that resources for investment promotion are scarce, efforts must be targeted in order to rise above the threshold needed for effectiveness. The second reason is the need to achieve a specific objective. Here, the investment projects selected must represent a significant contribution towards the chosen objective and be capable of generating the desired effects. For example, targeting efficiency-seeking firms can help to develop local supply chains and integrate them into international trade networks. Where reasons are formally given, they usually consist of a combination of both types, and are generally underpinned by the idea that some projects are "better" than others. The evaluation of a project's outcome will depend on the specific factors to which countries afford priority.

In selecting an objective, a country usually uses one or both of two criteria: (i) its own interests (the chosen objectives are those that will contribute most to the aims of the FDI promotion policy); and (ii) traits of the country (objectives are selected on the basis of advantages the country already has that are attractive to potential investors). The ideal situation is when the two criteria coincide, that is, when the country possesses advantages

or conditions that enable it to attract FDI in areas it is keen to develop. When interests far exceed real possibilities, in other words, when a country wishes to attract FDI for projects whose conditions (including incentives) are not attractive for potential investors, those "interests" are better described as "wishes" that have no basis in reality, and it runs the risk of using resources for activities that will not yield the desired outcomes.

For the purposes of this study, five forms of targeting were defined: by sector or industry, by function or activity, by type of project, by type of firm,¹⁷ and by country or geographical area (see table II.8).

Table II.8
TYPES AND EXAMPLES OF TARGETING

Targeting	Examples
By sector	Information technologies, automobile segment, biotechnology, agribusiness, tourism, and so on
By function	Manufacturing, logistics, commerce, R&D, back-office, etc.
By type of project	Large investments, employment generating, technology-intensive, export-generating, and so on
By type of firm	Fortune 500, leading brands, "winners", ^a etc.
Geographical area	Latin America, neighbouring countries, United States, Asia, Japan, Europe

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

^a Mortimore and Vergara (2005) showed how Costa Rica was able to attract semiconductor leader Intel by means of an active, targeted policy, while Mexico failed to attract the automotive leader Toyota because it did not employ such policies.

¹⁷ In general, survey responses indicate that the respective countries have not defined targets by type of firm (beyond belonging to the target segment), and so this is not included in the later analysis in this chapter.

1. Targeting in Latin American and Caribbean countries

(a) Sectoral and functional targeting

From the sectoral point of view, the preferences of 14 of the 15 countries covered by the survey showed that the region's countries are specifically aiming to attract investment in tourism and agribusiness. In other words, they are targeting traditional industries, not modern businesses that typically deploy efficiency- or technology-seeking strategies.

ICTs, including software development, ranked third in the countries' preferences. Fourth came ICT-enabled services, such as call centres, shared services, back-office services and business process outsourcing (BOP) (see table II.9). Countries are thus aware of the opportunities presented by the rapid growth of those sectors and functions and have set about attracting investments by firms looking to transfer their operations to lower-cost locations. Globally, UNCTAD (2004) estimates that the fastest-growing offshore services will be those enabled by ICTs. Exports of such services are anticipated to grow from US\$ 1 billion in 2002 to US\$ 24 billion in 2007.

Table II.9
FIVE MAIN SECTORS OR FUNCTIONS TARGETED FOR
INVESTMENT BY THE COUNTRIES SURVEYED

Sector or function	Positive responses	
	Number of countries	Percentage
Traditional		
Tourism/hotel infrastructure	14	93
Agribusiness/processed foods	14	93
Modern		
ICTs/software development	10	67
ICT-enabled services (contact centres, shared services, back office, business process outsourcing)	8	53
Logistics	6	40

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of surveys of investment promotion agencies.

Logistics occupies fifth place among the preferences. Six of the countries surveyed wished to attract investment to enhance regional product distribution. The other preferences

expressed were quite specific to the individual countries and exhibited varying degrees of targeting.

Costa Rica exhibits the most highly targeted promotion of foreign investment, since its efforts are directed mainly at services (contact centres, shared services and software design, engineering and development) and manufacturing of electronics and medical devices. The fourth sector that CINDE aims to promote in the future is tourism. These sectors were selected for the "revealed competitive advantages" that firms operating there have generated through successive investments. For example, the set-up of Intel's electronics operations, Abbot's medical devices and Procter & Gamble's shared services in Costa Rica revealed advantages that would also benefit other firms and were thus worth promoting. Costa Rica, as will be discussed further on, also has the most tightly focused geographical strategy, since its promotion activities are concentrated in the United States, where CINDE has its only overseas office.

Saint Lucia, Bolivarian Republic of Venezuela and Colombia follow Costa Rica in terms of the degree of targeting. In Saint Lucia, as well as the four sectors mentioned above, NDC also promotes investment in the entertainment industry. Saint Lucia too focuses on a small number of countries, with its main targets being the United States, India and the Caribbean. NDC finds that focused work has helped to secure a number of major projects that a more general approach might not have attracted. Bolivarian Republic of Venezuela is working to attract investment in petrochemicals, mining, and iron and steel.

Although the Venezuelan agency CONAPRI has been operating for almost 15 years, its efforts to target its promotion work are more recent. At first, CONAPRI focused strongly on overseas promotion of the country in general. It was not until 2003 that it adopted a more targeted approach and began to move away from the previous strategy. CONAPRI has found investment targeting to be crucial to the success of its FDI promotion policy.

Colombia, too, is shifting from a passive to a proactive stance on foreign investment, working with international consultants to identify specific firms by industry and by country. Paraguay's approach is also becoming quite targeted, concentrating investment promotion efforts on three specific sectors (apart from the three most popular

preferences indicated in table II.8): meat, cotton and textiles, and clothing. Together with Chile and Panama, Colombia and Paraguay are the only countries seeking to attract FDI in R&D.

Ecuador, Uruguay and Peru have devoted part of their efforts to securing investments in natural resources. Like the Venezuelan agency, Ecuador's CORPEI has found the identification of priority sectors to be one of the keys to the success of its FDI promotion policy. In this effort, Ecuador received technical assistance from UNCTAD in 2000, which identified a gap between potential and materialized FDI, based on unexplored advantages, particularly the country's rich natural-resource endowment (biodiversity, fishing, aquaculture, petroleum and mining) and ideal climate for tropical agriculture. Uruguay has identified a number of industries in the natural resource sector in which it would like to generate greater value added and is thus promoting investment in the rubber, pulp and metallurgy industries. Peru has signalled agribusiness, aquaculture and forestry as its priorities, based on its comparative advantages. However, over 80% of the promotion activities conducted by PROINVERSION concern infrastructure projects being tendered to private operators. Unlike the other sectors, this reflects the need to rectify internal shortcomings the country suffers. Jamaica is seeking to add projects in mining and metallurgy to its investment portfolio.

El Salvador, too, targets the first four preferences mentioned in table II.8, but has also identified a number of poles in manufacturing, such as electronics, textiles and clothing, and autoparts. Saint Vincent and the Grenadines is seeking projects in light manufacturing, the film industry and international financial services to add to its portfolio. And Panama proposes to improve the Canal by attracting investments in logistics, transport and business services.

Chile exhibits a mixed pattern, as a result of its institutional arrangements for investment promotion. CINVER is responsible for promoting Chile as a business platform in general, through the programme *Chile País Plataforma*, which advertises the opportunities arising from trade agreements already signed or being negotiated. CORFO has focused its efforts on three well-defined sectors: the food industry, with the purpose of strengthening regional clusters; technology (ICT-enabled services, software development and biotechnology), in order to diversify the production base by developing new high-potential sectors; and, recently, the carbon credits market, for which it has devised specific incentives, with a view to capitalizing on emerging opportunities.

Guatemala and Mexico are the countries with the loosest degree of sectoral targeting. Guatemala has defined

sectors in a very general way (assembly, manufacturing and services) and Mexico has a great diversity of target sectors and no particular geographical focus. Mexico's interest in its chosen sectors is to complement and strengthen local industry and the domestic market, in order to substitute imports and satisfy the country's need for goods.

(b) Investment targeting by project type

Job creation was the most frequently cited objective and the most desirable feature of an FDI project, with a mention in the responses of 11 of the 15 IPAs surveyed. Next in the order of priorities came technology-intensiveness, which was sought by ten of the IPAs examined, and export orientation, which was cited by eight (see table II.10). Although there is interest in attracting investments with a large technology-transfer component, efforts to promote FDI in R&D are limited (see box II.2). Initiatives such as duty-free zones or maquila regimes in most of the countries are an indication of efforts to attract projects to expand or diversify the export base. Firms usually have to meet export targets in order to qualify for these incentives. The schemes must also meet the standards of the World Trade Organization (WTO) and conform to international agreements. Some countries focus on projects above a threshold investment figure, usually US\$ 1 million. This is the practice in Ecuador and Saint Lucia in general, and in Chile for technology projects. Other aspects used to differentiate projects include positioning in the production chain, contribution to the country's development strategy or the strengthening of a cluster, although these variables are a little more difficult to evaluate.

Table II.10
INVESTMENT TARGETING BY TYPE OF PROJECT

Type of project	Positive responses	
	Number	Percentage
Creates jobs	11	73.3
Is technology-intensive or transfers technology	10	66.7
Generates exports	8	53.3
Involves a large investment ^a	5	33.3
Contributes to the country's regional development	1	6.7
Is strategically important for the country	1	6.7
Is important within the production chain	1	6.7
Adds value to products	1	6.7
Strengthens food industry clusters	1	6.7
Conforms to Kyoto Protocol ^b	1	6.7

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of surveys of investment promotion agencies.

^a For Chile (in technology), Ecuador and Saint Lucia, a large investment is defined as an investment of over US\$ 1 million.

^b Carbon credits market.

Box II.2

ATTRACTING FDI IN RESEARCH AND DEVELOPMENT

The recent UNCTAD report on global investment flows, the World Investment Report 2005 (WIR05), gives a detailed account of the tendency for transnational enterprises to internationalize their R&D activities.

This segment of corporate value chains, which is the least internationalized, is now the fastest growing. Although comprehensive data are not available, the statistics show that:

- In 1995-2003, the foreign proportion of R&D spending by leading Swedish firms increased from 22% to 45% and amounted to US\$ 2.47 billion.
- Between 1995 and 2002, Japanese firms' external spending on R&D rose from US\$ 1.9 billion to US\$ 3.3 billion, which represented 4% of Japan's total R&D investment.

- German firms' external spending on R&D increased by 130%, to US\$ 12 billion, between 1995 and 2001.

The bulk of world spending on R&D is carried out by transnational firms. In 2002, the 700 companies that spend most on R&D (of which at least 98% are transnationals) accounted for 69% of total R&D spending by firms worldwide which, in turn, represented 46% of all spending on R&D in the world. To put these figures in context, Ford Motor spends more on R&D than Spain or Switzerland, Siemens spends more than Belgium or Israel, and Toyota more than Finland or Austria. Of these firms, 80% are based in five countries—the United States, Japan, Germany, the United Kingdom and France—and represent three main industries, IT hardware,

automobiles, and pharmaceuticals and biotechnology.

R&D investment has traditionally gone to developed countries, and they continue to account for much of it. TNCs are increasingly locating R&D activities in developing countries, however. China and India are the principal Asian beneficiaries of R&D investments and Brazil is the largest Latin American recipient. Despite the opportunities this trend represents, however, as a rule the countries of the region have not actively promoted this type of investment. A recent survey conducted by UNCTAD (2005b) indicated that only 11% of IPAs in Latin America and the Caribbean promote investments in R&D, as against 79% in the developed countries and 94% in the developing countries of Asia and Oceania.

DO IPAS ACTIVELY PROMOTE R&D-RELATED FDI?

Region	Number of responses	
	YES	NO
Developed countries	15	4
South-East Europe and CIS *	5	4
Developing countries		
Africa	9	13
Latin America and the Caribbean	2	16
Asia and Oceania	15	1

Source: United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2005: Transnational Corporations and the Internationalization of R&D*, Geneva, 2005. United Nations publication, Sales No. E.05.II.D.10.

* UNCTAD classification. CIS: Commonwealth of Independent States (Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Russian Federation, Tajikistan, Turkmenistan and Ukraine).

SELECTED COUNTRIES: UNCTAD INNOVATION CAPABILITY INDEX, 2001

	Innovation capability		Technological activity		Human capital	
	Position	Index	Position	Index	Position	Index
Sweden	1	0.979	1	0.976	2	0.982
Japan	11	0.885	5	0.935	21	0.835
Ireland	21	0.814	22	0.781	18	0.848
Hungary	32	0.725	28	0.692	35	0.758
Czech Republic	36	0.690	30	0.680	38	0.701
Argentina	37	0.685	37	0.603	33	0.767
Chile	42	0.576	47	0.544	47	0.609
Brazil	49	0.529	52	0.478	52	0.579
Uruguay	52	0.506	71	0.298	37	0.715
Costa Rica	58	0.472	49	0.526	71	0.419
Mexico	59	0.469	54	0.461	65	0.477
Venezuela (Bolivarian Republic of)	62	0.460	56	0.468	64	0.482
Peru	63	0.425	74	0.289	57	0.561
Jamaica	67	0.395	68	0.315	67	0.475
Colombia	68	0.393	70	0.311	66	0.476
Ecuador	78	0.319	83	0.235	74	0.404
El Salvador	84	0.279	88	0.204	82	0.354
Paraguay	93	0.213	106	0.075	83	0.351
Guatemala	101	0.135	109	0.055	96	0.215
Angola	117(last)	0.019	117	0.000	118	0.025

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2005: Transnational Corporations and the Internationalization of R&D*, Geneva, 2005. United Nations publication, Sales No. E.05.II.D.10.

Box II.2 (concluded)

As with other types of investment, facilitation of R&D investment requires certain basic conditions to be met. It calls for stability and an investment-friendly business environment, infrastructure endowment (especially as regards information and telecommunications), protection of intellectual property and so on. By far the main pull factor, however, is the availability of adequate numbers of knowledgeable researchers at an attractive cost. Such human resources are usually to be found in an innovation-friendly environment, as reflected in the existence of an advanced national innovation system (NIS).

UNCTAD (2005b) has developed an "innovation capability" index, built on two

indicators: one measuring technological activity (which takes number of research staff, patents granted and scientific publications as proxies, all deflated by the number of inhabitants); and the other measuring human capital (whose proxies are the literacy rate and enrolment in secondary and tertiary education). The innovation capability index gives an indication of a country's capacity to attract FDI in R&D. The following table shows the indices of the countries examined. Countries that UNCTAD ranks as having a medium innovation capability are shown in bold typeface.

Only four of the countries covered in this study (Chile, Costa Rica, Panama and Paraguay) explicitly identified investment

in R&D or in highly complex technology as a particular investment target. The first two countries would be in a position to rise to the challenge, but Paraguay would be well advised to redefine its strategic focus. The UNCTAD report did not furnish information on Panama.

It is no simple undertaking to promote investment in R&D, and not all the countries have the advantages they would need to do so successfully. Nevertheless, transnational enterprises are increasingly inclined to make their R&D investments abroad. The countries of the region should at least be abreast of this trend and, where possible, try to capitalize on the opportunities arising in this area.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2005: Transnational Corporations and the Internationalization of R&D*, Geneva, 2005, United Nations publication, Sales No. E.05.II.D.10; and ECLAC/UNCTAD seminar entitled "Globalization of R&D by Transnational Corporations – Policy Challenges and Opportunities for Latin America and the Caribbean", Santiago, Chile, 17-18 January 2006.

(c) Geographical targeting of investment

From the geographical point of view, most IPAs target the United States, which accounted for 10 preferences. Other activities are aimed at geographical areas, such as Europe, Asia and Latin America, with no single country fielding more than 20% of the responses. Costa Rica has the most targeted strategy in geographical terms, mentioning only the United States as its main focus. At the other extreme are Mexico, Peru and Saint Vincent and the Grenadines, which did not indicate geographical target areas. Saint Vincent and the Grenadines expects to embark on a targeting strategy in 2006. Table II.11 gives a schematic summary of the different countries' strategies, based on a series of sectoral and geographical targeting criteria.

As well as pointing up the fact that all investment is not the same, targeting enables countries to make more efficient use of the generally scarce resources available for promotion activities. With a few exceptions, the countries of the region target investment quite loosely, focusing on broad sectors such as tourism and agribusiness or on multiple objectives. IPAs should ensure that specific

objectives are defined in keeping with the resources available and with the objectives and strategies of the national development policy.

Table II.11
TARGETING STRATEGIES

	Geographical targeting		
	A small number of countries	A small number of countries and some geographical areas	Many countries and/or several geographical areas
Sectoral targeting	A few well-defined sectors	Costa Rica	
	A few well-defined sectors and other more general ones	Colombia Saint Lucia El Salvador	Venezuela (Bolivarian Rep. of) Chile Jamaica Panama
	Many well-defined sectors and/or several general ones		Uruguay Paraguay Peru Guatemala Ecuador Mexico Saint Vincent and the Grenadines

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of surveys of investment promotion agencies.

E. Conclusions and recommendations

At a theoretical level, there is a broad consensus regarding the potential benefits of FDI. Although many different strategies are used and different objectives pursued in promoting FDI, it is apparent that, especially in Europe, Asia and some economies in transition, the countries that have been most successful in securing this type of investment and harnessing its benefits are those that have adopted more active and targeted policies (UNCTAD, 2004, 2005b).

With the exception of a few special cases, FDI alone cannot resolve problems associated with a country's level of development and economic growth. It can, however, provide powerful leverage for solving such problems provided that it is consistent with the country's overall development strategy. More active policies increase the possibilities not only of attracting the kind of investment best suited to national objectives, but also of harnessing its potential benefits in an effective manner. The global tendency is towards increasingly complex policy frameworks integrated with the whole array of development policies, which also translates into stiffer competition among countries to attract FDI.

Generally speaking, the development of policies to attract FDI is in its infancy in Latin America and the Caribbean. The countries are now beginning to move away from the passive stance on investment, in which inflows are based on comparative advantages and policy success is measured mainly by the amount of investment received, towards a more active approach reflected in more proactive policies on investment promotion in which horizontal strategies to attract investment are combined with more targeted efforts in sectors and projects that are of particular interest.

This research has found that the institutional structure of investment promotion is relatively incipient and still being consolidated (in 50% of the cases studied, the IPAs were set up after 2000), indicating that institutional learning remains to be done. Considering, moreover, the shortfalls in budget and human resources (which are, on average, below the international benchmarks) and limited coordination and integration with other policies, it may be supposed that IPAs have little capacity to implement FDI promotion policies in an efficient and effective manner.

From a positive standpoint, the Latin American and Caribbean countries are advancing along the right road. They are generating changes aimed at consolidating the

institutional fabric of investment promotion. There is an awareness of the benefits this can bring and of the need to target promotion work, and steps are being taken in this direction. The IPAs surveyed report that progress will be made towards more active policies in the short term. Given the substantial head start of the developed countries and developing Asia in this regard, it is to be hoped that the region can make rapid enough progress to tie FDI in with its industrial development objectives and technology-building aspirations in order to enhance its international market integration.

In the light of the analysis of the countries' policies on investment promotion, incentives and targeting strategies, the following aspects should be carefully reviewed:

- **Coordination and integration with development policies:** It is important to ensure that the objectives of FDI promotion are compatible with the country's broader development aims and to take into consideration the importance of active policies of FDI promotion. These policies need to be coordinated and integrated with the whole range of productive and economic development policies, which includes endowing the institutions responsible for FDI promotion with adequate human and financial resources.
- **Promotion:** Generally speaking, the functions and activities that Latin American and Caribbean IPAs report performing are similar to those carried out by such institutions in other parts of the world. Their stance tends to be more receptive and domestically-oriented than proactive and outward-looking, however. Given the tough competition for FDI, agencies have to "go out and look" for investment rather than waiting for it to come to them. Since this approach is more costly and requires better qualified personnel, it would be beneficial to examine budgets and resources allocated to those activities (which, as noted earlier, are still below the international benchmarks).
- **Incentives:** Incentives play a role in competition among countries. They have more impact on certain categories of investment (efficiency-seeking) and at the shortlist stage of the selection process. The countries examined tend to use mainly fiscal incentives, with tax exemptions directed mainly towards exports in the form of duty-free zones and maquila regimes. As priorities are defined and efforts are made to attract more specific types of investment, the countries

should consider replacing their incentive frameworks with more targeted models. There is all the more reason to revise incentive frameworks given that the countries will have to adapt their duty-free regimes to WTO subsidy regulations in the near future. It is also advisable to improve ex ante and ex post evaluation mechanisms to ensure that investment incentives are awarded only when the anticipated benefits outweigh the respective costs, and when the best possible evaluation indicates that the investment would not be made otherwise.

- **Targeting R&D:** Although the countries are making headway with the development of more targeted schemes, on average, their strategies are still quite broad. Special mention was made of a number of countries' efforts to attract FDI in R&D. The tendency for transnational companies to look for new locations to invest in R&D is quite recent and represents an opportunity for countries that can

offer the necessary conditions. Given that heavy investment in R&D may contribute to national development objectives, it is worth the countries' effort to assess whether they are in a position to attract such investment, identify niches in which they could make an attractive offer and strengthen their national innovation system.

In conclusion, by all accounts competition to attract FDI is becoming ever more intense and the countries that are enjoying most success are those which, apart from having the necessary conditions, are designing and implementing active policies to attract and harness the benefits of such investment. The countries to benefit most will be those that have targeted their investment promotion efforts to tie in with their national development aims both as they are now and with regard to competitive positioning in the future. The international experience is broad and varied enough to offer valuable references for individual countries in this undertaking.

Chapter III

“Trans-Latins”: an overview

“Trans-Latins”, emerging Latin American transnationals that have made direct investments outside their home countries, have become an increasingly important phenomenon, particularly since the mid-1990s. Indeed, outward foreign direct investment (FDI) by trans-Latins is accounting for an increasing share of total FDI in Latin America. This chapter provides an overview of the situation, covering the global, regional and local context of the trans-Latins’ international expansion, their motivations, their competitive advantages and some of the difficulties they have had to face. To take the measure of this phenomenon, a combination of different information sources has been used (since none can provide a satisfactory explanation on its own), including official balance-of-payments statistics, studies by academics and institutional investors, press items, company reports and, most importantly, interviews with high-level executives from the largest trans-Latins in Argentina, Brazil, Chile and Mexico.¹

Later chapters will provide more in-depth and detailed analyses of a group of activities in which many of the leading trans-Latins are involved: basic industries (hydrocarbons,

extractive mining, iron and steel, cement, metal processing, paper and cellulose), food and beverages, and services (engineering, telecommunications, electricity, retail).

¹ Executives from about 45 of the largest trans-Latins in Argentina, Brazil, Chile and Mexico were interviewed between May and November 2005. In making the selection for the study, preference was given to the largest of the internationalized companies in each of these countries.

A. The global background to the expansion of the trans-Latins

1. The history of outward FDI from developing countries

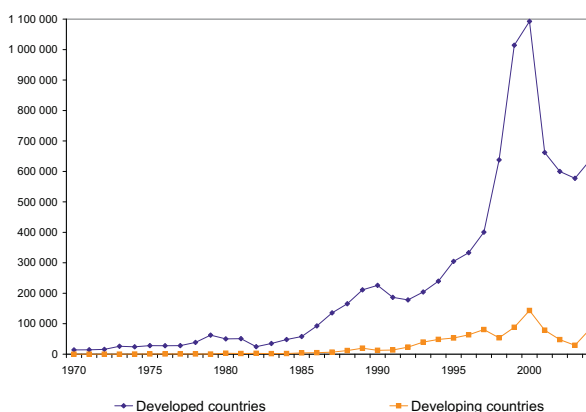
Few outward FDI statistics are available for developing countries (particularly by comparison with inward FDI data) and the quality of those that do exist is highly questionable. There are several reasons for this.

First, the existence of tax havens makes it hard to correlate outflows from investor countries with the inflows reaching the recipient countries. By contrast with incoming FDI, this problem is not corrected by the statistical information of the Organisation for Economic Co-operation and Development (OECD) countries, because most investors are from countries which are not members of that grouping. Furthermore, the statistics do not distinguish between local firms and subsidiaries of transnational companies (TNCs), which makes the parent company difficult to identify. Lastly, in many cases, and particularly in developing countries, governments do not make an effort to produce statistics of this type.

Despite these shortcomings, the statistical information available does reveal some of the global and regional trends in outward FDI.

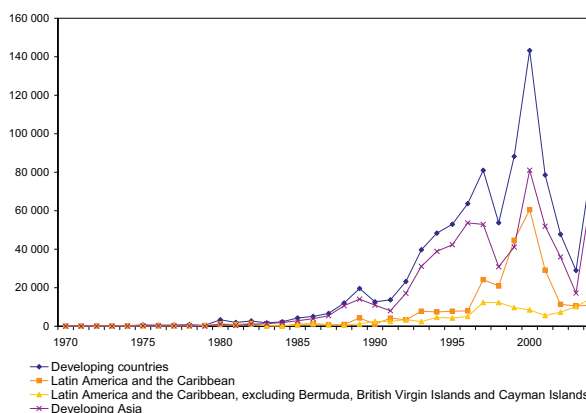
According to the information available from the United Nations Conference on Trade and Development (UNCTAD), outward FDI by developing countries increased from an annual average of US\$ 106 million in the 1970-1974 period to some US\$ 9.5 billion between 1985 and 1989, and then to US\$ 76.4 billion in the five-year period 2000-2004 (see figure III.1). In this way, the stock of outward FDI from developing countries rose from US\$ 89.5 billion to just over US\$ 1 trillion between 1985 and 2004. As these figures plainly show, direct investment from developing countries has been on the rise, particularly in the last few years. Some authors have spoken of “waves” of outward FDI from developing countries. The first began in the 1960s and ended in the late 1970s, while the second coincided with the 1980s (Chudnovsky and López, 2000). In retrospect, comparing these first two “waves” with the investment boom of the 1990s gives them more the appearance of ripples (see figure III.1). The fact is that investment flows from developing countries began to grow at unprecedented rates in the mid-1990s, although there was a sharp slowdown after 2000 (see figure III.2).

Figure III.1
OUTWARD FOREIGN DIRECT INVESTMENT: DEVELOPING AND DEVELOPED COUNTRIES, 1970-2004
(Millions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by United Nations Conference on Trade and Development (UNCTAD).

Figure III.2
OUTWARD FOREIGN DIRECT INVESTMENT: DEVELOPING COUNTRIES, BY REGION, 1970-2004
(Millions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by United Nations Conference on Trade and Development (UNCTAD).

In the 1970s, foreign investment by firms headquartered in developing countries took on a degree of importance as Latin American and Asian firms began to invest more heavily abroad. Around the early 1980s, when the amounts were small, a substantial proportion of FDI flows from developing countries originated in Latin America and the Caribbean. Since then, and especially during the boom period, the situation has been reversed and leadership has shifted to the developing countries of Asia; this shows up particularly clearly when foreign investments made from tax havens are excluded from the statistics (see figure III.2).

According to the statistics available, outward FDI from Latin America and the Caribbean leaped from an annual average of some US\$ 52 million between 1970 and 1974 to US\$ 1.7 billion in 1985-1989, and then to US\$ 24.5 billion between 2000 and 2004. Excluding the main financial centres (Bermuda, British Virgin Islands and

Cayman Islands), the annual average was US\$ 9.2 billion in this last period. By contrast, outward FDI originating in developing Asia increased from an annual average of US\$ 3 million in 1970-1974 to US\$ 7.4 billion between 1985 and 1989, and then to US\$ 51.1 billion in 2000-2004. Between 1985 and 2004, the outward FDI stock of the Latin American and Caribbean countries rose from US\$ 51 billion to US\$ 271.7 billion (or US\$ 147.4 billion when the main financial centres are excluded), whereas in developing Asia it leaped from US\$ 27 billion to US\$ 718 billion. In 1977, 14 of the 30 largest developing-country transnationals were from Latin America and the Caribbean and just 10 were from East and South-East Asia (Heenan and Keegan, 1979). By 2003 the situation had been reversed, as 40 of the top 50 developing-country transnationals were Asian and just 7 Latin American, all of them from Brazil and Mexico (see table III.1).

Table III.1
DEVELOPING COUNTRIES: THE TOP 50 NON-FINANCIAL TRANSNATIONAL CORPORATIONS, 2003
(Billions of dollars)

Company	Country	Sector	External assets
1 Hutchison Whampoa Ltd.	Hong Kong SAR of China	Diversified	59 141
2 Singtel Ltd.	Singapore	Telecommunications	17 911
3 Petrolim Nasional Bhd (PETRONAS)	Malaysia	Petroleum	16 114
4 Samsung Electronics Co., Ltd.	Republic of Korea	Electronics	12 387
5 Cemex S.A.	Mexico	Cement	11 054
6 América Móvil	Mexico	Telecommunications	8 676
7 China Ocean Shipping Co.	China	Transport	8 457
8 Petróleo Brasileiro (Petrobras)	Brazil	Petroleum	7 827
9 LG Electronics Inc.	Republic of Korea	Electronics	7 118
10 Jardine Matheson Holdings Ltd.	Hong Kong SAR of China	Diversified	6 159
11 Sappi Ltd.	South Africa	Paper	4 887
12 Sasol Ltd.	South Africa	Chemicals	4 226
13 China National Petroleum Corp.	China	Petroleum	4 060
14 Capitaland Ltd.	Singapore	Real estate	3 936
15 City Developments Ltd.	Singapore	Hotels	3 879
16 Shangri-La Asia Ltd.	Hong Kong SAR of China	Hotels	3 672
17 Citic Pacific Ltd.	Hong Kong SAR of China	Diversified	3 574
18 CLP Holdings	Hong Kong SAR of China	Basic services	3 564
19 China State Construction Engineering Corp.	China	Construction	3 417
20 MTN Group Ltd.	South Africa	Telecommunications	3 374
21 Asia Food & Properties	Singapore	Food	3 331
22 Flextronics International Ltd.	Singapore	Electronics	3 206
23 Companhia Vale do Rio Doce (CVRD)	Brazil	Mining	3 155
24 YTL Corp. Berhad	Malaysia	Basic services	2 878
25 Hon Hai Precision Industries	Taiwan Province of China	Electronics	2 597
26 China Resources Enterprises	Hong Kong SAR of China	Petroleum expl./ref./distr.	2 364
27 Oil & Natural Gas Corp.	India	Petroleum expl./ref./distr.	2 328
28 Neptune Orient Lines Ltd.	Singapore	Transport and storage	2 266
29 United Microelectronics Corporation	Taiwan Province of China	Electronics	2 251
30 Singapore Airlines Ltd.	Singapore	Transport and storage	2 118
31 Metalúrgica Gerdau S.A.	Brazil	Metals	2 056
32 Barloworld Ltd.	South Africa	Diversified	1 957
33 Quanta Computer Inc.	Taiwan Province of China	Computing	1 934
34 First Pacific Company Ltd.	Hong Kong SAR of China	Electronics	1 910
35 Hyundai Motor Company	Republic of Korea	Motor vehicles	1 780
36 Taiwan Semiconductor Manufacturing Co. Ltd.	Taiwan Province of China	Computing	1 539
37 Benq Corp.	Taiwan Province of China	Computing	1 497
38 China National Offshore Oil Corp.	China	Petroleum and natural gas	1 467
39 Fraser & Neave Ltd.	Singapore	Food and beverages	1 395
40 Swire Pacific Ltd.	Hong Kong SAR of China	Business services	1 387
41 Keppel Corporation Ltd.	Singapore	Diversified	1 361
42 Yue Yuen Industrial Holdings Ltd.	Hong Kong SAR of China	Textiles and leathers	1 317
43 Acer Inc.	Taiwan Province of China	Electronics	1 244
44 Delta Electronics Inc.	Taiwan Province of China	Electronics	1 219
45 Grupo Bimbo S.A. de C.V.	Mexico	Food	1 156
46 China Minmetals Corp.	China	Mining and metals	1 150
47 The MUI Group	Malaysia	Hotels	1 135
48 Gruma S.A. de C.V.	Mexico	Food	1 086
49 Hongkong Electric Holdings Ltd.	Hong Kong SAR of China	Electricity, gas, water	1 074
50 Nan Ya Plastics Corp.	Taiwan Province of China	Petrochemicals	1 030

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2005: Transnational Corporations and the Internationalization of R&D*, Geneva, 2005. United Nations publication, Sales No. E.05.II.D.10.

In the 1970s and 1980s, the leading Latin American countries in terms of outward FDI were Argentina, Brazil, Colombia and Mexico. Most investments from these countries went to other developing countries, particularly neighbouring ones, and the main sectors involved were natural resource extraction, engineering and construction services, and manufacturing operations set up to avoid trade restrictions in the recipient countries. Often partnerships were formed with local companies and investments were oriented primarily towards markets in the recipient country, except where they were natural resource-seeking investments whose purpose was to supply markets in the home country (Chudnovsky and López, 1999a). Argentine and Brazilian companies were the leaders and their direct investments beyond their borders were largely market-seeking, the intention being to exploit competitive advantages (product design or adaptation capabilities, and commercial and productive management) in less sophisticated markets (Chudnovsky and López, 1999b).

In the mid-1980s, developing Asia caught up with and then outstripped Latin America and the Caribbean. Hong Kong Special Administrative Region of China, Singapore, the Republic of Korea and Taiwan Province of China were the main investors, along with other South-East Asian economies. These economies had grown quickly on the back of outward-oriented strategies in which exports and outward FDI were crucial. Direct investments beyond their borders were motivated by a combination of factors: the appreciation of local currencies, higher labour costs, a growing scarcity of natural resources, a need for greater proximity to customers and a requirement for new technologies and brands to enhance competitiveness, among other things. Broadly speaking, individual investments were larger than they had been in the first wave, they were intended to reduce production costs, and they were generally oriented towards third-country markets. A growing proportion were in the markets of developing countries (Whitmore and others, cited in Chudnovsky and López, 1999a).

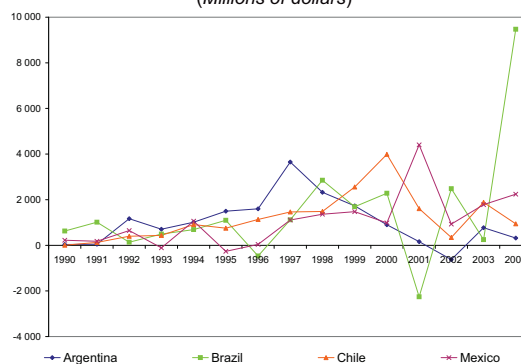
In the 1980s, Latin American and Caribbean investment felt the negative impact of the debt crisis and the drop-off in domestic economic activity, and the continent accordingly lost ground to developing Asia as a source of direct investment. Some existing investments became unsustainable and many manufacturing companies that had grown up in the shelter of the import substitution industrialization (ISI) model, particularly in the car parts, metallurgy, steel and textile sectors, closed down or were taken over by TNCs (Chudnovsky and López, 1999b). Thus, much of the direct investment undertaken by Latin American countries in the first two waves could not be sustained over time.

In the 1990s, outward FDI flows from developing countries grew at unprecedented rates, although they fell off considerably after 2000 owing to the numerous shocks

experienced by emerging economies (see figure III.2). In developing Asia, the main actors were the Republic of Korea, Singapore, Taiwan Province of China, Hong Kong Special Administrative Region of China, and China. In the Republic of Korea, regulatory changes and policy measures favourable to investment abroad, including tax and financial incentives, contributed to the internationalization of large conglomerates (*chaebols*) in the areas of electronics and machinery, and of smaller firms in the areas of textiles, wearing apparel and footwear. For the Republic of Korea and Taiwan Province of China, internationalization was a mechanism for raising efficiency and preserving competitiveness in labour-intensive sectors by transferring operations to low-wage countries, and for obtaining access to new markets (Mathews, 2005). The opportunities that were beginning to open up in China also attracted ever growing amounts of FDI from other countries in the region, especially Singapore and Hong Kong Special Administrative Region of China (Goldstein, 2006). In addition, much Asian investment spread beyond the region itself, with greater and greater amounts going to industrialized economies.

In Latin America in the 1990s, economic liberalization, deregulation and privatization policies exposed local companies to the challenge of competing in the local market (often a captive one) and pursuing foreign investment opportunities. Nonetheless, the bulk of outward FDI from Latin America and the Caribbean stayed within the region, with only a few global actors investing in other continents. These investments went to sectors as diverse as hydrocarbons, mining, cellulose and paper, steel and other metals, cement, food and beverages, engineering and construction, household electrical appliances, car parts, aircraft manufacture, electricity, telecommunications and retail, among others. Because of the high volatility of their outward FDI (largely the result of macroeconomic crises), leadership in the region has alternated between the main countries (Argentina, Brazil, Chile and Mexico) (see figure III.3).

Figure III.3
LATIN AMERICA AND THE CARIBBEAN: OUTWARD FOREIGN
DIRECT INVESTMENT, 1991-2004
(Millions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by United Nations Conference on Trade and Development (UNCTAD).

Even so, Latin American and Caribbean companies have lost ground in this process, whose scale and geographical reach have increased strikingly in recent years. At present, only a handful of firms from the region's largest economies

are among the 50 leading developing-country TNCs: four from Mexico (CEMEX, América Móvil, Bimbo and Gruma) and three from Brazil (Petrobras, CVRD and Gerdau) (see table III.1).

2. General trends

Because of the shortcomings of the statistics on outward FDI flows, different sources of information have to be used. One particularly good source is a set of national case studies on emerging transnationals conducted in 2005 by the United Nations Conference on Trade and Development (UNCTAD), from which some general conclusions can be drawn (see table III-A.1):²

- Despite the great diversity of internationalization experiences among developing countries, there are many common factors within regions, especially when Latin America and the Caribbean is compared with developing Asia.
- Recently, outward FDI has been more concentrated in high-technology manufactures and in services, whereas older studies showed these capital flows centring more on natural resource extraction (hydrocarbons and mining), natural resource-based manufactures (steel, cement, cellulose and paper, food and beverages) and some services (electricity).
- Efficiency-seeking and strategic asset-seeking strategies are far commoner in developing Asia than in Latin America and the Caribbean and other regions, where natural resource- and market-seeking strategies have predominated.
- Direct investment from developing Asia has tended to spread around the world, while investment from Latin America and other regions is largely confined to neighbouring countries, with the exception of some natural resource-seeking investments, chiefly in the areas of hydrocarbons and engineering services.

It is also possible to identify the main factors driving the internationalization processes of these countries and of the largest emerging TNCs (see table III-A.2). Once again, there are factors common to all the countries: (i) push factors, such as the desire to open up new markets and the need to secure access to export markets and consolidate

there, and (ii) pull factors, such as the prospect of access to the recipient country market and the availability of natural resources. There are large differences between regions, however.

Where push factors are concerned, outward FDI from developing Asian countries appears to be driven by a relative scarcity of natural resources, the need to lower production costs and acquire strategic assets, and sophisticated governmental promotion of these capital outflows in the form of currency regulations, institutional and financial support and, in some cases, direct support from organizations created for this purpose. In Latin America and the Caribbean, meanwhile, and to some extent in other regions as well, investment is determined by the need to find markets for their raw materials and diversify their sources, macroeconomic instability (boom and bust cycles in internal demand, and currency instability), abortive experiences as foreign investors, the need to diversify risks, the rapid opening of domestic markets and the growth of outside competition owing to deregulation and privatization, and a far more limited supporting role for government (chiefly in the form of currency regulations). It is also significant that initiatives by State enterprises have been important in both regions. However, initiatives in developing Asia are diversified across a number of activities, whereas those in Latin America are mainly confined to basic industries (see table III-A.2).

In the case of pull factors, companies from developing Asia have been motivated more by considerations of access to third-country markets for their export platforms, the availability of technology, organizational practices and management skills, utilization of the overseas Chinese network, the need to improve logistics, the desire to reduce production costs and avoid trade restrictions in third countries, the globalization of national brands, the ability to follow their clients, and the drive to become

² In December 2005, UNCTAD held an Expert Meeting on Enhancing Productive Capacity of Developing Country Firms through Internationalization at its headquarters in Geneva, Switzerland. Fourteen national case studies were presented, including three prepared by ECLAC. The following were consulted: Bonaglia and Goldstein (2005), Brimble (2005), Calderón (2005), Erdilek (2005), Giroud (2005), Moon (2005), Mortimore (2005), Rumney (2005), Svetlicic (2005), Tavares (2005), UNCTAD (2005d), (2005e) and (2005f) and Yusof (2005).

customers of TNCs (in electronics, by becoming better integrated into provider networks) and obtain trade preferences in recipient countries. In Latin America and the Caribbean, on the other hand, and also in other regions to some extent, the main factors have been: ethnocultural networks (Hispanic immigrants in the United States), opportunities resulting from privatization

and deregulation in neighbouring countries, improvements to distribution systems, the regionalization of national brands, associations with TNCs (food and beverages), preferential access to recipient markets thanks to subregional integration agreements (Argentina and Brazil), free trade agreements (Mexico and Chile) and investment promotion and protection agreements (see table III-A.2).

B. Trans-Latins

In Latin America and the Caribbean, most trans-Latins are from four countries: Argentina, Brazil, Chile and Mexico.³ When it comes to the factors driving their outward FDI, these countries have a great deal in common. National peculiarities need to be borne in mind, however, for the dynamic of these capital flows to be fully understood.

Chronologically speaking, Argentina and Brazil were the pioneers, driving the first waves of outward FDI,

while Mexico and Chile entered the process later and were important during the boom period. At present, while Brazil has sustained its pattern of internationalization and Argentina has virtually disappeared as an external investor, it is companies from Mexico and Chile that have taken up the running, increasing their presence in external markets with new production and service activities.

1. Argentina: foreign investment pioneers, but few survivors

Argentina is often cited as one of the first developing countries to undertake outward FDI (Chudnovsky and López 2000, United Nations 1993). Among the first companies to carry out investments outside the country were: Alpargatas, a textile maker that set up a manufacturing subsidiary in Uruguay in 1890 and then another one in Brazil; S.I.A.M. di Tella, an engineering company; and Bunge & Born, a diversified agricultural conglomerate which set up production plants in neighbouring countries in the first half of the twentieth century (see box III.1). Later, however,

Alpargatas became a minority shareholder in its main operations in Brazil, S.I.A.M. di Tella was nationalized after a period of major losses and Bunge & Born moved its headquarters out of the country (United Nations, 1993). This tendency has been repeated even by some of the Argentine companies that have invested abroad most recently, such as Yacimientos Petrolíferos Fiscales (YPF) and Pérez Companc, which were taken over by foreign companies. Thus, although Argentina was a pioneer in Latin America, many of its foreign assets were lost over time (UNCTAD, 2005g).

³ Some firms are also coming to prominence in Colombia (Grupo Bavaria, Cementos Argos, Industrias Alimenticias Noel and Interconexión Eléctrica S.A. (ISA)), Venezuela (Petróleos de Venezuela S.A. (PDVSA), Grupo Cisneros) and some of the Central American countries. The analysis presented in the chapters that follow will include some of these companies.

Box III.1

BUNGE & BORN: AN ARGENTINE TRANS-LATIN?

Although Bunge & Born (now Bunge) is often cited as one of the first Argentine companies to invest abroad, its nationality is not easy to determine, as the location of its headquarters has changed several times over its history. The company was founded in Holland in 1818, soon after which it moved to Belgium and then Argentina. It was in Argentina that it really expanded, becoming one of the world's leading marketers of agricultural

commodities. It was also one of the first Argentina-based companies to start investing outside the country. In the 1970s the company moved again because of political instability, this time to Brazil.

By the following decade, Bunge & Born had diversified into numerous activities up and down the food production chain throughout the American continent. In 1999, after

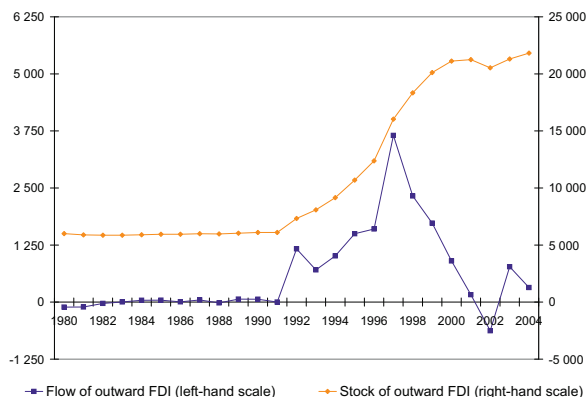
undergoing a deep restructuring and refocusing on its core business (agriculture), the company changed its "nationality" yet again and set up its headquarters in New York, United States, where Bunge began to trade its shares on the stock exchange in 2001. Thus, it is hard to determine whether this company is still Argentine, and what the local implications of its transnationalization might be.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

In the early twentieth century, Argentina was the most economically advanced country in Latin America and the Caribbean. However, the severe macroeconomic crises it went through, often accompanied by radical transformations of the dominant economic model (from the export agriculture approach to import substitution industrialization (ISI) and then the introduction of different variants of the market economy model), resulted in long periods of slow growth, with episodes of great macroeconomic instability, despite its exceptional wealth of natural resources. The largest local companies had to operate in a very shifting and highly uncertain business environment. The effect on outward FDI was variable. Early investments were encouraged under the export agriculture model; during the ISI period many of these investments became dormant; and with the advent of liberalization and economic opening, outward investment was once again stimulated.

In the 1990s, Argentina was once again one of the largest external investors in Latin America (see figures III.3 and III.4), largely owing to the restructuring of local industry in the face of the growing foreign competition that resulted from the new economic model (Kulfas, 2001). This situation did not last long, however. In an initial phase, the changes (trade and financial liberalization, deregulation, privatization and stabilization programmes) offered good growth prospects, and these were seized upon by the dominant local groups and foreign investors. This process was then extended to the country's neighbours, where some of the largest local business groupings made direct investments. However, the stabilization plan, based as it was on a fixed exchange rate in a context of excessive external borrowing, ultimately undermined the economic model, triggering a profound crisis.

Figure III.4
ARGENTINA: STOCK AND FLOWS OF OUTWARD FOREIGN DIRECT INVESTMENT, 1980-2004
(Millions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by United Nations Conference on Trade and Development (UNCTAD).

From 1998, Argentina's outward FDI went into steady decline, with a slight recovery in 2003. From a peak of US\$ 3.7 billion in 1998, investment abroad had turned negative by 2002. These figures show that the business groupings which had flourished in the upturn experienced severe setbacks that forced them to withdraw from many activities, both locally and abroad. Although the stock of outward FDI reached US\$ 21.8 billion in 2004 (only exceeded in the region by Brazil), these data conceal a very different reality. Owing to the way the economic reforms were implemented and the subsequent crisis, Argentine trans-Latins were unable to sustain their original impetus and ended up selling most of their assets, both in Argentina and abroad (see table III.2).

Table III.2
ARGENTINA: THE LEADING TRANS-LATINS AND THEIR OPERATIONS ABROAD, 2004-2005
 (Millions of dollars)

Company	Sector	Sales	Operations in regional markets ^a					Internationalization category ^b			
			LA	NA	EU	AP	OT	TNC	>50%	>25 <50%	<25%
YPF ^c	Petroleum	6 666	x	x			x	x			
Techint	Steel	6 421	x	x	x	x	x	x			
Pérez Companc ^c	Petroleum	2 332	x							x	
Arcor	Food	929	x							x	
Quilmes ^d	Beverages	765	x							x	
Mastellone ^e	Food	463	x					...	...	...
Impsa	Engineering	...	x	x		x		x			
Bagó	Pharmaceuticals	...	x							x	
Grupo Macri ^e	Diversified	...	x					...	...	...
Bunge ^f	Food	...	x	x	x	x	x	...			

Source: Economic Commission for Latin America and the Caribbean (ECLAC) on the basis of information provided by the companies and *América economía* magazine, "500 mayores empresas de América Latina", Santiago, Chile, 15 July-18 August 2005.

^a LA: Latin America and the Caribbean, NA: North America, AP: Asia Pacific, EU: Europe, OT: other.

^b Calculated as a percentage of sales (or employment) accounted for by subsidiaries outside Argentina.

^c Argentine trans-Latins taken over by TNCs.

^d Argentine trans-Latins controlled by TNCs.

^e Argentine trans-Latins that have sold their main assets to TNCs.

^f Argentine trans-Latins that have moved their headquarters to another country.

With the exception of the very largest trans-Latins, the international expansion of Argentine companies has been confined to Latin America and, to a far lesser degree, North America and Europe. Between 1990 and 1996, some 84% of all flows of Argentine outward FDI went to Latin American countries, chiefly Brazil (31%) and Venezuela (28%) (Kosacoff, 1999). On the whole, this geographical pattern has continued up until the present. The main areas of activity have been natural resources and natural resource-based manufacturing. In the 1990s, outward FDI went mainly into hydrocarbons, iron ore and steel, and the food sector (Kosacoff, 1999). Nonetheless, the most significant characteristic of this group of trans-Latins in the present decade has been the unresisting ease with which they have been sold off, wholly or in part, to their main competitors, almost all of them TNCs.

Since the late 1990s, the main Argentine petroleum companies that invested abroad (YPF and Pérez Companc) have been sold to foreign companies (Repsol of Spain and Petrobras of Brazil). A large equity stake has been taken in the beer company Quilmes by a Brazilian company in the same sector, AmBev (now InBev). Other companies, such as Mastellone and Grupo Macri, remain under Argentine control but have sold many of their foreign assets, along with some of their most valuable local possessions. As of now, only three Argentine trans-Latins (Techint, Arcor and, to a lesser extent, Impsa) have come through the traumatic experiences of the 1990s intact. Indeed, there are no Argentine companies in the list of the top 50 non-financial developing-country TNCs (see table III.1).

Among the push factors driving Argentine trans-Latins to carry out outward FDI were their high domestic market share (Techint, Arcor, Quilmes) and chronic macroeconomic instability. The need to increase and diversify reserves (essential in the oil industry) led YPF and Pérez Companc to make natural resource-seeking investments. Many companies sought to internationalize their competitive advantages (Techint, Mastellone, Arcor, Pérez Companc) and capitalize on the international experience and presence they had built up as exporters (Arcor). Also important was the need to improve product quality (Arcor) and increase minimum scale to maintain existing capacity (Impsa). Some companies sought to improve their competitiveness by obtaining advantages through internationalization, such as access to new markets (Arcor and Techint), and by incorporating higher-skilled human resources (Techint). Some built up special advantages, such as the networks and industry knowledge bequeathed to them by the original founders of the company, generally European immigrants (Techint).

Where the impact of changes in Argentine government policy is concerned, opening up the economy to outside competition placed heavy pressure on all companies, particularly since these transformations were very swift and far-reaching. Deregulation and privatization in the energy sector were very important in this regard. The Argentine Government did not promote outward FDI in any significant way; indeed, currency regulations in periods of crisis often discouraged it.

As for the pull factors influencing outward FDI by Argentine trans-Latins, the main ones included the

opportunities arising in other countries' privatization programmes, access to new markets, geographical and cultural proximity (investments by Quilmes in Paraguay and Uruguay and by Techint in Italy), the availability of natural resources (YPF and Pérez Companc) and the host countries' potential to become platforms for exports to third-country markets (Impsa, Techint). Policy changes by recipient country governments were very important, particularly the new opportunities opened up by deregulation and privatization (Techint, YPF, Pérez Companc) and the trade preferences that became available because of integration within MERCOSUR. The outward investment policies of the recipient countries were not a determining factor.

Some of the competitive advantages secured by these trans-Latins and exploited by their international operations consist in the learning experience provided by the gradual growth (in size, quality, diversification and the sophistication of production) of their home market (Arcor), the establishment of alliances or partnerships with TNCs (Quinsa with AmBev and Arcor with Danone),

improved logistics and distribution systems (Arcor), the opportunity to turn local brands into regional ones (Arcor and Quilmes), the technological sophistication of their infrastructure in a developing market (Impsa) and the consolidation of centralized procurement, which increased negotiating power vis-à-vis suppliers (Techint).

In conclusion, two characteristics of Argentine outward FDI should be highlighted. First, it is largely confined to a few industries, which are dominated in turn by a handful of large companies. In 1997, for example, during the upsurge in these capital flows, almost two thirds of all outward FDI from Argentina was the work of three companies, Pérez Companc, YPF and Techint (Kosacoff 1999). Second, many of these companies no longer exist as trans-Latins. Of the largest, two, in the hydrocarbons industry, were subsequently taken over by foreign companies. Among the leading trans-Latins, transfer of ownership abroad and the sale of large equity or asset holdings to other companies (Quinsa, Macri and Mastellone) are some of the defining features of the Argentine experience.

2. Brazil: investment abroad as a hedge against internal risk

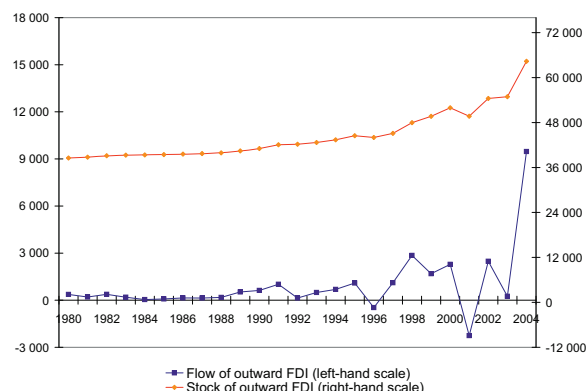
In the 1960s and 1970s, the Brazilian ISI strategy was accompanied by export promotion policies. This combination defined the characteristics of the first wave of Brazilian outward investment between the 1970s and early 1980s: natural resource-seeking initiatives, particularly in the case of petroleum (Petrobras), or export support systems (distribution, marketing and assembly). Manufacturing investment was still low and largely confined to food products, steel and electronics. Proprietary advantages included the "tropicalization" of technologies, production experience and the availability of raw materials (López, 1999).

In the 1980s, which were a time of instability and uncertainty, productive investment (both domestic and external) contracted because economic agents preferred to increase their liquidity (López, 1999). Nonetheless, some large Brazilian enterprises did make major investments abroad. This was the case with engineering and construction companies, whose domestic market opportunities diminished as public investment fell, and the Companhia Vale do Rio Doce (CVRD), which started investing, in partnership with foreign companies, to secure markets and processing capacity for its main export product, iron ore. There was also substantial manufacturing investment from the mid-

1980s until the early 1990s, chiefly in car parts, metallurgy, textiles and steel. Companies were seeking markets first and foremost (essentially to overcome tariff and non-tariff barriers), together with some strategic assets, using just-in-time techniques in the car manufacturing and parts industry (López, 1999). In the late 1980s, the bastions of ISI began to be dismantled, leading in the early 1990s to trade liberalization, deregulation and privatization.

Spurred by these reforms, Brazilian firms were restructured in a process that involved intensive technological and organizational innovation and improved product quality. This provided an incentive for internationalization, something that began to be reflected in the trend of outward FDI (see figure III.5). The reforms also set in train a vigorous process of consolidation, however, with mergers and acquisitions and numerous plant closures and cutbacks, while in some cases companies dismantled their international operations and withdrew or sold out to TNCs (López, 1999). Many of the large family groups were restructured as professional management was brought in and ownership was diversified by floating equity on the stock market. State companies were privatized or, as in the case of Petrobras, partially opened up to private capital.

Figure III.5
BRAZIL: STOCK AND FLOWS OF OUTWARD FOREIGN DIRECT INVESTMENT, 1980-2004
(Millions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by United Nations Conference on Trade and Development (UNCTAD).

While the tendency of restructuring at some large companies was towards greater specialization, as they divested themselves of assets that were not part of their core business, others diversified into other segments. International investments were important instruments in both reorganization strategies. CVRD took the first course, liquidating non-strategic assets and beginning to diversify into other minerals with investments outside Brazil. Petrobras, meanwhile, went further in its early natural resource-seeking investments and began to invest internationally in the refining, distribution and marketing of petroleum

derivatives. This market-seeking movement enabled it not only to overcome the limitations of the Brazilian market, but also to protect itself from its fluctuations.

Stability in the second half of the 1990s meant that companies were able to adopt a medium-term planning horizon, but they still had great difficulty in obtaining financing. Again, the first two years of stabilization generated opportunities in the internal market that brought about a temporary interruption in internationalization efforts, especially those whose purpose was to support exports. For many companies, indeed, outward FDI was a second step in the internationalization process, after exports (Iglesias and Motta Veiga, 2002).

In the early years of the present decade, macroeconomic instability and economic and political uncertainty led many companies to increase their investments abroad. What drove investment flows in this new phase was the desire to diversify the risk associated with operations in the domestic market.

In 2004, investment flows from Brazil to other countries totalled some US\$ 9.5 billion, although a single transaction, the merger between Interbrew and AmBev (see chapter V), accounted for about US\$ 4.5 billion of this. The stock of outward FDI that year was estimated at some US\$ 69 billion, the highest figure in Latin America and the Caribbean (see figure III.5). Most of the companies that have internationalized have invested in Latin America, although many of them have also invested in at least one other continent (see table III.3). As for the distribution of investment by economic activity, it has largely remained concentrated in hydrocarbons, metal processing and construction.

Table III.3
BRAZIL: THE LEADING TRANS-LATINS AND THEIR OPERATIONS ABROAD, 2004-2005
(Millions of dollars)

Company	Sector	Sales	Operations in regional markets ^a					Internationalization category ^b			
			LA	NA	EU	AP	OT	TNC	>50%	>25 <50%	<25%
Petrobras ^c	Petroleum	40 763	x	x	x	x	x				x
CVRD ^c	Mining	10 377	x	x	x	x	x				x
Gerdau ^c	Steel	7 383	x	x	x						
Usiminas	Steel	4 607	x								x
AmBev ^d	Beverages	4 523	x	x						x	
EMBRAER	Aircraft	3 854		x	x	x					x
CSN	Steel	3 692		x	x						
VARIG	Air transport	3 337	x								x
Camargo Correa	Cement and textiles	2 796	x								x
Norberto Odebrecht	Engineering and construction	2 205	x	x	x	x	x				
Votorantim Cimentos	Cement	1 733		x					x		
TAM	Air transport	1 703	x								x
Andrade Gutierrez	Engineering and construction	1 372	x		x	x		x			x
Klabin	Paper and cellulose	1 028	x								x
WEG	Motors	830	x		x	x				x	
EMBRACO ^d	White goods	799	x	x	x	x				x	
Queiroz Galvão	Engineering and construction	...	x								
Marcopolo	Car parts and vehicles	605	x		x	x				x	
Tigre	Tubes and connections	437	x								x
Sabó	Car parts	...	x	x	x					x	

Source: Economic Commission for Latin America and the Caribbean (ECLAC) on the basis of information provided by the companies and *América economia* magazine, "500 mayores empresas de América Latina", Santiago, Chile, 15 July-18 August 2005.

^a LA: Latin America and the Caribbean, NA: North America, AP: Asia Pacific, EU: Europe, OT: other.

^b Calculated as a percentage of sales (or employment) accounted for by subsidiaries outside Brazil.

^c Brazilian companies listed by UNCTAD among the top 50 non-financial developing-country TNCs (see table III.1).

^d Brazilian trans-Latin taken over by a TNC.

With the notable exception of the Empresa Brasileira de Aeronáutica S.A. (EMBRAER) (see box III.2), the main Brazilian trans-Latins specialize in natural resources or natural resource-based manufactures. Of the ten leading Brazilian trans-Latins, six were formerly State-owned (some still are in part), which is indicative of the influence of public policies on their creation and development (see table III.3). Furthermore, Odebrecht, a family conglomerate, developed largely as a provider of services to the State, particularly until the 1980s, as did other engineering and construction companies. The largest firms also include a number of iron and steel enterprises: a

national family business (Gerdau) and two formerly State-owned companies (Usinas Siderúrgicas de Minas Gerais S.A. (Usiminas) and Companhia Siderúrgica Nacional (CSN)). The pace of these companies' internationalization and the reasons for it vary greatly, but it is undeniable that the protection of industry was crucial to the development of what are now the largest operators. The combination of State support (or ownership) and dynamic, professional management in the post-privatization period was crucial to the current success of many of these companies, including EMBRAER (see box III.2).

Box III.2

EMBRAER: A HIGH-TECHNOLOGY TRANS-LATIN

The Empresa Brasileira de Aeronáutica S.A. (Embraer) is a rare example of a trans-Latin in a technology-intensive sector. The company is now the world's largest manufacturer of commercial aircraft with less than 110 seats. Embraer is one of Brazil's leading exporters and has a workforce of some 16,000 people, 2,500 of them outside the country. The company was founded in 1969 with majority State ownership, and the emphasis on technological development was always present. Production began in the 1970s, with aircraft for agricultural and military purposes and for passenger transportation. The Brazilian armed forces and local airlines were the earliest and largest customers. However, Embraer quickly began to sell to armed forces (Uruguay was the first case) and commercial airlines in other countries. From the outset, exports were seen as a way of financing the company's research programmes. As the years went by, close collaboration grew up between the company, the armed forces and domestic and foreign firms involved in production. Embraer also benefited from export promotion policy instruments, including some tied specifically to military procurement. The company's interaction with local research and development institutions has also been a dominant factor in its growth. In the late 1970s, Embraer invested in technical and commercial support assets in the United States and Europe.

Following a severe financial crisis, Embraer was streamlined and, in 1994, privatized. Foreign ownership was limited

to 40%. The company was acquired by a consortium that included United States investors (Wasserstein Perella and Bozano Simonsen), one of Brazil's largest financial conglomerates and the pension funds of Banco do Brasil and Telebras (both of them State-owned at the time). The State kept 6.8% of the equity and a golden share with the power of veto over any change in company control or objectives and any alteration in its defence programmes. Following privatization, its operations were rationalized, particularly with the development of the ERJ-145, a commercially successful passenger plane which returned the company to profit in 1998 after eight years of losses. In 1999, Embraer established a strategic partnership with a group of European aerospace companies comprising the European Aeronautic Defence and Space Company (EADS), Dassault, Thales and Snecma, which acquired 20% of the company's voting shares.

Embraer's sales abroad have been essential to its growth, representing 90% of the total in 2002. To sustain them, it has had to establish sales representatives and maintenance centres all over the world and, more recently, assembly operations. Furthermore, the company has forged a number of joint ventures with foreign companies for new product development and maintenance purposes. The motives behind Embraer's investments in manufacturing operations abroad have been high tariffs on assembled products and military procurement policies favouring local producers.

In the early part of the present decade, the company began a new phase of foreign investment aimed at breaking into the promising markets of China, the United States and Europe. In 2001, Embraer set up a parts storage operation with the China Aviation Supplies Import and Export Corp. (CASC). In 2002 it formed a joint venture with AVIC II to produce the ERJ-145 in China, and the Harbin Embraer Aircraft Industry (HEAI) was set up, with the Brazilian firm taking a 51% stake. HEAI produces some components and is to carry out assembly and testing operations. The operations in China have revealed the complexities of doing business in that country, partly because of high tariff barriers and partly because of requirements and conditions imposed by the government. In 2002, Embraer made new investments in maintenance and other services in Nashville, United States. In 2004 it invested in the conversion of a former military base in Florida into an aircraft assembly operation so that it could bid for United States military contracts. That same year, the company acquired OGMA-Indústria Aeronáutica de Portugal S.A., a formerly State-owned aircraft maintenance firm.

In addition to its high-technology profile, Embraer is the only trans-Latin that combines the commercially oriented culture of the post-privatization era with the technological, productive and management capacity developed under Brazilian State ownership.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of Todd Benson, "Corporations in Brazil shed stay-at-home tradition", *New York Times*, 10 December 2004; *Valor econômico*, "No turbulence in sight. Brazil's top 200", year 1, No. 1, October; Andrea Goldstein, "The political economy of industrial policy in China: the case of aircraft manufacturing", *William Davidson Institute Working Paper*, No. 779, July 2005; Andrea Goldstein, "EMBRAER: from national champion to global player", *CEPAL Review*, No. 77 (LC/G.2180-P), August 2002; Defesanet, "Embraer: principais eventos em 35 anos" [online] 19 August 2004 <<http://www.defesanet.com.br/embraer/35eventos>>; EMBRAER, official site [online] <<http://www.embraer.com>>; Brazilian Aircraft Corporation (EMBRAER), "Embraer", document prepared for the Conference on Investment for Development: Making It Happen, Rio de Janeiro, 25 to 27 October 2005.

Nonetheless, Brazilian trans-Latins have been subject to many of the same problems as their counterparts in other Latin American countries. In the recent period, many companies that internationalized early (car parts) have been taken over by foreign enterprises. The beer producer AmBev, which was absorbed by a TNC, is the most recent and significant case (see chapter V). At the same time, for all its size, the Brazilian economy displays a very low degree of internationalization. Of the largest trans-Latins, only one might be regarded as having an advanced level of internationalization (over 50% of sales or employment outside Brazil), eight as being moderately internationalized (over 25% but less than 50% of sales or employment outside Brazil) and most (11 firms) as displaying limited internationalization (less than 25% of sales or employment outside Brazil) (see table III.3). This can be accounted for, among other factors, by the size of the domestic market, the fact that it was opened up only quite recently, and the “psychological” gap that distances many businesses from opportunities abroad —something that seems to be changing rapidly (Da Rocha, 2003).

The main push factors for the earliest Brazilian hydrocarbon investments abroad were uncertainty about

the size of domestic reserves and the risks associated with this activity, which make diversification of sources a necessity. In engineering and construction services, the decline of public spending on infrastructure works forced companies to look for external markets if they were to survive and grow. As was mentioned earlier, trade liberalization, deregulation, privatization and other reforms in the 1990s increased both the need to search aggressively for growth opportunities abroad and the management capacity for doing so. Lastly, and to a greater degree than in other cases analysed, the risk of doing business in Brazil has been one of the main push factors for FDI, as investing abroad has enabled companies to reduce the impact of currency volatility on export competitiveness and to balance local and foreign currency revenue and outlays (see box III.3). For a number of Brazilian companies, owning assets abroad has meant improved risk ratings and given them access to financing on better terms. Thus, if there is one push factor that stands out as characteristically Brazilian in the Latin American outward investment process, it is the inherent risk of doing business from a Brazilian base and the effects of this on the cost of capital.

Box III.3

MARCOPOLO: ASSEMBLY AND THEN PRODUCTION ABROAD TO ESCAPE AN UNSTABLE CURRENCY?

Founded in 1949, the Brazilian company Marcopolo is the largest bus manufacturer in Brazil, accounting for more than half of all units produced there. It exports to over 60 countries and is an important player in the Middle East.

In the 1990s, Marcopolo began to set up assembly plants outside Brazil as a way of facilitating exports of components manufactured in the country since the cost of transporting finished vehicles was high, especially to markets where they could not be moved overland. In 1990 it set up a plant in Portugal to sell to the European market. By 2002 this was still a small operation (10 units a month), but it was restructured and output doubled. In 1997 Marcopolo set

up a plant in Argentina and achieved good results in the early years, achieving output of 100 units a month. It was very hard hit by the Argentine crisis, however, and suspended production until 2005. The lessons learned in Portugal and Argentina contributed to the success of the Mexican operation, which was established independently in 2000 and then became a joint venture with Daimler-Chrysler. In 2001, plants were set up in Colombia and South Africa. According to the company, its greatest growth potential lies in developing-country markets. One of the most promising for the near future is China, where Marcopolo is considering the best way to go about setting up a competitive

operation and taking advantage of low production costs, while gaining access to the local and regional market.

The recent strengthening of the Brazilian currency has affected Marcopolo's operations abroad, as they are based on parts and components produced in Brazil. Against this background, the company is restructuring these operations in order to incorporate a larger local production component. In this case, outward FDI has provided the solution to a problem and helped the company to continue growing, which is obviously good news for Marcopolo. It also illustrates, however, how currency instability is affecting industrial activity and jobs in the home country.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

As for the pull factors, these included opportunities in neighbouring markets as a result of privatization, of competition policy constraints on the expansion of firms in these same countries (asset swap between Petrobras and Repsol-YPF), and of the crisis in Argentina (the takeover of Pérez Companc by Petrobras). Some companies followed transnational customers to other regions (car parts). Asymmetrical trading conditions were also behind

many market-seeking investments. Indeed, protectionism persists in certain sectors, such as steel and orange juice, and this has been a spur to investment, especially in the United States. The absence of bilateral trade agreements with markets that are important for Brazilian exports, such as the United States, has been a vital incentive to invest in those countries, either directly or by using third countries as export platforms.

To sum up, Brazilian companies have only a modest record when it comes to internationalization. Although Brazil is one of the largest economies in the developing world and the largest in Latin America, its internationalization dynamic is centred on just a few economic activities with limited geographical coverage. In other words, the process has

been controlled by a handful of large companies. Because of the enormous size of the local economy, the number of companies seeking growth opportunities outside the country is not great. Nonetheless, persistent instability and uncertainty have forced some of the largest local conglomerates to invest abroad as a risk diversification mechanism.

3. Chile: the last to join the trans-Latin club

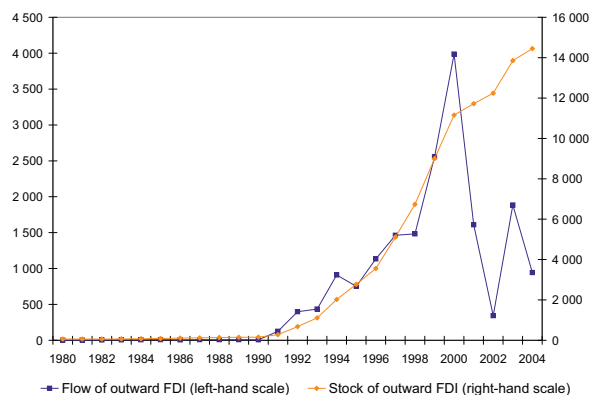
Chile was a pioneer of economic reform in Latin America. In the early 1970s, the authorities of the time charted a radically new course for the economic model, the main elements of which (the opening up of the economy to outside competition, trade and financial liberalization, deregulation, privatization, the lessening of the size and role of the State, and the predominance of the market economy) served as an inspiration for the reforms that would be implemented years later by most of the region's countries. Following a rather chaotic initial period of high inflation, excessive external borrowing and economic recession, the country entered upon a path of high growth that has made it the best-performing economy in Latin America.

In addition to growth and macroeconomic stability, the country integrated rapidly into the international market by signing numerous free trade and bilateral investment agreements with countries in Latin America, North America, Europe and Asia. Chile became a large recipient of FDI and vastly expanded its trade links. In microeconomic terms, a high degree of concentration began to appear in some of the main areas of the Chilean economy and, in the face of growing external competition and domestic market saturation, some of the largest of the emerging business groups began to invest heavily abroad. Between 1985 and 2004, the stock of Chilean investment abroad grew from US\$ 100 million to some US\$ 14.5 billion (see figure III.6).

In the early 1990s, a group of Chilean firms were proving quite competitive in the local market, something they had achieved in part because of their exposure to the policies implemented in the country some years before. Important competitive advantages were built up in a number of sectors, such as telecommunications, electricity generation and distribution, retail, some branches of manufacturing, and pension fund administration. In these circumstances, Chilean companies were able to obtain large amounts of financing on very good terms. Furthermore, the early reforms gave them a valuable competitive edge over other countries in the region where the economic changes were only just beginning. Thus, while Chilean trans-Latins were not as large as some

of their competitors in other Latin American countries, their experience enabled them to embark upon ambitious internationalization plans.

Figure III.6
CHILE: STOCK AND FLOWS OF OUTWARD FOREIGN DIRECT INVESTMENT, 1980-2004
(Millions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by United Nations Conference on Trade and Development (UNCTAD).

In the 1990s, the pace of outward investment growth was faster in the case of Chile than in that of other Latin American countries (ECLAC, 1998, p. 142). The dominant investment strategies of the Chilean trans-Latins were focused on breaking into new markets for services (electricity generation and distribution) and manufactures (paper and cellulose) and on securing natural resources (hydrocarbons and forestry). The great bulk of the earliest outward FDI flows went to neighbouring countries, especially Argentina, to buy up assets that were being privatized. Much of this investment was in the electricity sector, where the main agents in the process were Enersis, Empresa Nacional de Electricidad (ENDESA) and Chilgener (subsequently Gener and now AES Gener).

Chilean investments abroad gradually diversified in their geographical and sectoral scope (Calderón, 2005). The large investments in the electricity sector were joined by others in service activities (Cencosud, Falabella, Ripley

and a number of pension fund administrators (AFPs) and some areas of manufacturing (Madeco, Lucchetti).⁴ In the case of the industrial sector, internationalization was most intensive among business groups that had clear natural comparative advantages. In most cases, the activities concerned were associated with natural resources, examples being food, soft drinks and beer, cellulose and paper, and mineral manufactures. Other countries, particularly Peru and then Colombia and Brazil, also became recipients for these investments, the great majority of which followed market-seeking strategies and took the form of purchases of existing assets.

As Chilean investments expanded they took in other activities, a notable example being the AFPs. In the early 1980s, the Chilean authorities undertook a far-reaching reform of the pension system, moving from an unfunded system to one of individual accounts in which private companies were the fund managers.⁵ The Chilean AFPs built up a wealth of experience in the local market, which they then used to internationalize their operations as reforms of this type spread to other countries in Latin America. As greater synergies arose between pension fund administration and other financial activities, the major international operators began to take an interest in the Chilean AFPs. In 1998, the Spanish company Santander Central Hispano (SCH) bought AFP Summa and a year later Banco Bilbao Vizcaya Argentaria (BBVA), also of Spain, took over the leading fund administrator in the Chilean market, Provida.⁶ Thus, the international presence of the Chilean AFPs declined and the two Spanish banks, together with the United States finance company Citicorp, came to dominate the regional market for pension funds. In this case, as with the electricity sector, the regional networks created proved to be a valuable asset for international operators wishing to quickly establish a solid presence in Latin America.

In the late 1990s and the early part of the present decade, some of the largest Chilean trans-Latins with a regional presence were taken over by TNCs, a situation that coincided with a sharp deterioration in the economies that had received these investments (Argentina, Brazil and Peru). In an environment of great uncertainty, Chilean

firms sought to bolster their position in the local market and postponed their plans for investing outside the country.⁷ In Peru, and especially in Argentina, contingency plans were implemented and in some cases radical productive and financial restructuring was undertaken to cope with the enormous losses.

Not to be put off by this experience, Chilean trans-Latins have expanded afresh in the present decade. Favourable economic conditions in Chile and its neighbours have facilitated new investment, so that the historical pattern of these capital flows has been re-established. For some of these companies, such as retailers, competitive advantages acquired at home have translated into great potential for regional expansion (Calderón, 2005).

Nonetheless, apart from electricity and pension funds, investment by Chilean trans-Latins has remained concentrated in a small number of natural resource-related businesses, services and natural resource-based manufacturing (see table III.4). With a few exceptions (ENAP, Lan Airlines, ENTEL and MOLYMET), the international expansion of these trans-Latins has been confined to Latin America. The level of internationalization, again with a few exceptions (Farmacias Ahumada, Falabella, Ripley and Madeco) has fallen short of 25% of total sales. Looked at in this way, Chilean trans-Latins would seem to have internationalized rather cautiously. However, many have encountered difficulties along the way (Falabella, CENCOSUD, Ripley, Madeco) and others were taken over by TNCs when they overextended or built up regional networks that turned them into very attractive targets (Enersis, Gener, Masisa, pension funds). Still, there are no Chilean firms among the leading developing-country transnationals (see table III.1).

The push factors that explain the internationalization of Chilean trans-Latins can be grouped into four categories. First, there are certain constraints associated with the domestic business environment, such as high market shares in a small, saturated market (ENAP, Lan, Arauco, CMPC, Madeco and Farmacias Ahumada). Another group comprises the competitive advantages that are peculiar to individual companies (telecommunications, energy, retail, pension funds) or arise naturally (cellulose, paper, minerals),

⁴ In 1996, Lucchetti, part of the Luksic group, decided to build a pasta production plant in Lima, Peru. Shortly after construction began, the Municipality of Lima questioned the viability of the plant, which was sited in a nature reserve. In 2003, after operating for five years, the plant was shut down, and a long drawn-out legal process ensued. The Chilean investors had lost more than US\$ 150 million, leading them to file a claim for compensation with the International Centre for Settlement of Investment Disputes (ICSID).

⁵ In May 1981, the individually funded pensions system began to operate with 12 pension fund administrators (AFPs). After a consolidation process involving numerous mergers, there are now six: Summa Bansander, Cuprum, Habitat, PlanVital, BBVA Provida and Santa María.

⁶ At the time of the takeover, Provida had 2.4 million subscribers, US\$ 10.2 billion under management and five subsidiaries abroad (Colombia, Ecuador, El Salvador, Mexico and Peru). It had 40% of all pension system subscribers in Chile (Calderón and Casilla, 1999, p. 25).

⁷ Indeed, it has been estimated that Chilean companies lost about US\$ 10 billion because of their high exposure to Argentina and Peru (interview with Guillermo Tagle of Santander Inversiones on the Radio Duna programme "Hablemos en Off", Santiago, Chile, 26 September 2005).

enabling them in many cases to internationalize early. Other aspects of their corporate strategies stem from the need to open up new export markets and consolidate old ones, to increase scale (Cencosud, FASA, Ripley, Falabella) and to obtain international financing (Enersis, Gener, Cencosud, Madeco, Embotelladora Andina and CCU). Other push factors include early shifts in government policy which gave Chilean trans-Latins a considerable advantage over their neighbours and over TNCs with little experience

of Latin America, particularly in environments of recent deregulation and privatization. Chilean trans-Latins took advantage of the access to MERCOSUR provided by the association agreement. Although the Chilean authorities have signed numerous free trade treaties, however, they have not been very important to these companies' operations. Lastly, the promotion of Chilean outward investment has not been a major factor, although the lifting of many currency restrictions has facilitated capital outflows of this type.

Table III.4
CHILE: THE LEADING TRANS-LATINS AND THEIR OPERATIONS ABROAD, 2004-2005

Company	Sector	Sales	Operations in regional markets ^a					Internationalization category ^b			
			LA	NA	EU	AP	OT	TNC	>50%	>25 <50%	<25%
Enersis ^c	Electricity	4 863	x					...	...	...
ENAP	Petroleum	4 704	x					...	...	...
Falabella	Commerce	2 885	x							x	
Cencosud	Commerce	2 477	x							x	
Lan Airlines	Air transport	2 034	x	x				...	...	...
Arauco	Cellulose and paper	2 075	x					...	...	...
CMPC	Cellulose and paper	1 935	x							x	
CGE	Electricity	1 276	x							x	
ENTEL	Telecoms	1 243	x	x						x	
FASA	Commerce	1 087	x					x			
MOLYMET	Metallurgy	975	x		x			...	...	...
Ripley	Trade	909	x							x	
CCU ^d	Beverages	755	x							x	
Embotelladora Andina ^d	Beverages	743	x					...	...	...
AES Gener ^c	Electricity	702	x					...	...	...
Madeco	Metallurgy	582	x							x	
Masisa ^c	Cellulose and paper	398	x					x			

Source: Economic Commission for Latin America and the Caribbean (ECLAC) on the basis of information provided by the companies and *América economía* magazine, "500 mayores empresas de América Latina", Santiago, Chile, 15 July-18 August 2005.

^a LA: Latin America and the Caribbean, NA: North America, AP: Asia Pacific, EU: Europe, OT: other.

^b Calculated as a percentage of sales (or employment) accounted for by subsidiaries outside Chile.

^c Chilean trans-Latin bought by a TNC.

^d Chilean trans-Latin controlled by a TNC.

The main pull factors were location advantages in recipient countries, consisting essentially in opportunities for growth and access to the markets of Chile's neighbours, particularly Argentina, Peru, Brazil and Colombia. The main competitive results were to turn national brands into regional ones (CMPC, Masisa, Lan Airlines, Farmacias Ahumada, Falabella, Cencosud, Ripley), improve logistics and distribution systems (ENAP, Masisa) and forge alliances or partnerships with TNCs (ENAP, CCU, Embotelladora Andina). Policy changes in the recipient markets were very important, especially market opening in neighbouring countries, deregulation and privatization. At the same time, significant difficulties for the internationalization of these companies were created by the deterioration of the economic situation in Argentina (CGE, Falabella, Cencosud, Madeco) and, to a lesser extent, Brazil (Madeco).

Chilean trans-Latins, then, are fairly small and have only a limited international reach, and their initial success was due in large part to their primary advantages. As their

competitors in the region and elsewhere gained experience and access to the same markets, their initial advantages were eroded. In many cases, these companies' regional assets made them attractive targets for TNCs (Enersis, Gener, Masisa, and pension funds). However, there are examples of Chilean trans-Latins that have defended their own market against dominant transnationals (Cencosud, Ripley, Falabella), even buying up many of their assets in Chile (ENTEL, Falabella) and abroad (Cencosud). Chilean trans-Latins that have learned from experience and became more competitive, both locally and in neighbouring countries, have gradually consolidated their internationalization.

To sum up, the internationalization of Chilean firms has centred on Latin America. Early reforms, the privatization of State enterprises and the acquired experience of doing business in an open, competitive economy, together with geographical and cultural proximity, gave them an important competitive edge

when they sought to expand internationally and take advantage of the opportunities that were arising in neighbouring countries, particularly at a time when Chile had access to external financing that it could redirect into foreign investments (Calderón and Griffith Jones, 1995). During the initial phase, when the environment was highly uncertain, this experience was crucial for

competing with TNCs that did not know Latin America well. However, these advantages were rapidly eroded, their competitors found their way, and some of the Chilean companies that had been most active in this process were absorbed by international operators. Now, following a period of stagnation, Chilean investment abroad has picked up again, reinforcing historical patterns.

4. Mexico: taking advantage of proximity to the United States

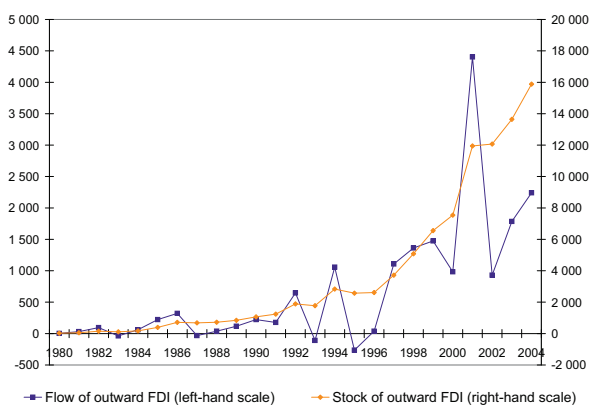
Mexico's economic model, like that of other Latin American countries, changed many times in the twentieth century. In the late 1980s, before it had even emerged from the rigours of the external debt crisis, the country implemented a radical reform that basically consisted in opening up the economy to foreign trade and investment and reducing the role and size of the State.⁸ Thus, policies were brought in to liberalize the economy, deregulate many services, privatize State assets and drastically reduce incentives for local businesses. The new model, which revolutionized the domestic business environment, also involved measures to attract and create export platforms for manufacturing assembly operations in the country (*maquila*).

The new economic policy slowly began to produce results, as creditor countries finally recognized. In 1994, Mexico formalized a free trade agreement with the United States and Canada, with a view to consolidating the reforms begun some years earlier. Mexico subsequently negotiated similar agreements with a number of Latin American countries, the European Union (1999) and Japan (2004). These drastic economic policy changes were also recognized by the main investor countries when they admitted Mexico to the General Agreement on Tariffs and Trade (GATT) (1986) and the OECD (1994).

The shift in economic conditions and the new competition from TNCs in the domestic market forced Mexican firms to revise their corporate strategies, particularly when the North American Free Trade Agreement (NAFTA) came into force. The urgency increased with the 1994 financial crisis, as Mexican firms had to alter their defensive stances and seriously rethink their corporate strategies to adapt to the new conditions. Thus it was that, from an almost non-existent base, Mexican companies began to invest outside the country, hesitantly at first and then with great enthusiasm (see figure III.7). A great

deal of financing was available to them for this purpose, from both local and international sources. This foreign investment drive was concentrated in the United States and Central America, extending in some cases to South America and other more distant regions such as Europe and Asia (Mortimore, 2005).

Figure III.7
MEXICO: STOCK AND FLOWS OF OUTWARD FOREIGN DIRECT INVESTMENT, 1980-2004
(Millions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by United Nations Conference on Trade and Development (UNCTAD).

Because Mexican balance-of-payments procedures do not make outward FDI registration compulsory, the statistics do not seem to fully reflect the scale and tendency of these capital flows. Even on the information available, however, it is clear that Mexico has a significant stock of outward FDI (some US\$ 16 billion in 2004) and that there was a very strong upsurge in the early years of the twenty-first century (see figure III.7).⁹

⁸ Two of the most important areas of the Mexican economy, petroleum and electricity, were not opened up to FDI.

⁹ This figure certainly falls short of the reality. In a speech delivered at ECLAC headquarters in Santiago, Chile on 26 January 2006, President Vicente Fox put a figure of US\$ 23 billion on total Mexican investment in Latin America (Presidencia de la República de México, 26 January 2006).

Table III.5 shows the main Mexican trans-Latins that have generated a large part of the direct investments made outside Mexico (Grosse and Thomas, 2005). Concerning their level of internationalization, these companies can be classified into four groups:

- Cementos Mexicanos (CEMEX) is the only Mexico-based company that can be said to be a major TNC at the global level, given the percentage of its sales generated outside the country and the degree of geographical coverage its operations have attained.¹⁰

- Companies with an advanced degree of internationalization (over 50% of sales or employment outside Mexico), such as América Móvil, Gruma, San Luis Rassini and Grupo Alfa.
- Firms with a moderate degree of internationalization (over 25% but less than 50% of sales or employment outside Mexico), such as Coca Cola FEMSA, Grupo IMSA, Grupo Bimbo, TELMEX and Mabe.
- Companies with a limited degree of internationalization (less than 25% of sales or employment outside Mexico), a category that includes a further nine companies.

Table III.5
MEXICO: THE LEADING TRANS-LATINS AND THEIR OPERATIONS ABROAD, 2004-2005
(Millions of dollars)

Company	Sector	Sales	Operations in regional markets ^a					Internationalization category ^b			
			LA	NA	EU	AP	OT	TNC	>50%	>25% <50%	<25%
TELMEX	Telecoms	12 443	x	x						x	
América Móvil ^c	Telecoms	12 086	x	x					x		
Grupo FEMSA	Beverages	8 426	x							x	
CEMEX ^c	Cement	8 142	x	x	x	x		x			
Grupo Alfa	Diversified	5 275	x	x	x				x		
Bimbo ^c	Food	4 623	x	x	x						x
Grupo México	Mining	4 359	x	x							x
Grupo IMSA	Metallurgy	3 325	x	x						x	
Grupo Elektra	Trade	2 350	x								x
Grupo Vitro	Glass	2 348	x	x	x						x
Gruma ^c	Food	2 242	x	x	x				x		
Grupo DESC	Car parts	2 138	x	x	x						x
Grupo Xignux	Diversified	1 954	x								x
Grupo Mabe	White goods	1 841	x							x	
Grupo ICA	Construction	1 175	x		x						x
Grupo CIE	Media	699	x	x	x						x
San Luis Rassini	Car parts	...	x	x					x		
Grupo Posadas	Tourism	401	x	x							x
Jugos del Valle	Beverages	378	x	x							x

Source: Economic Commission for Latin America and the Caribbean (ECLAC) on the basis of information provided by the companies and *América economía* magazine, "500 mayores empresas de América Latina", Santiago, Chile, 15 July-18 August 2005.

^a LA: Latin America and the Caribbean, NA: North America, AP: Asia Pacific, EU: Europe, OT: other.

^b Calculated as a percentage of sales (or employment) accounted for by subsidiaries outside Mexico.

^c Mexican companies listed by UNCTAD among the top 50 developing-country transnationals (see table III.1).

Most of the 19 Mexican trans-Latins have their international operations concentrated in Latin America and North America. Eight have operations in the European Union. Just one, CEMEX, has operations in Asia, although Gruma is in the process of initiating operations in that region. Almost half these companies produce natural resource-based manufactures such as cement, glass, food and beverages, petrochemicals, etc. Two other activities are important, however: car parts and telecommunications. In most of

these areas, international expansion has been motivated primarily by the search for new markets. The case of car parts is rather different in that Mexican suppliers operate in what is an extremely competitive industry in Mexico, and this is forcing them to raise their efficiency and set up some plants near the main assembly operations in the United States and Europe. Generally speaking, these trans-Latins have expanded internationally by buying existing assets and not through greenfield investment (Garrido, 1999, 2001).

¹⁰ As used here, the concept refers to a trans-Latin (CEMEX, the sole example) which not only has a high level of sales abroad and possesses an international network, but that has also attained very significant coverage in the world market —i.e., a market share that makes it one of the leaders in its field. Only on these terms can a TNC be deemed "major".

These internationalized Mexican companies have clearly moved beyond the defensive strategies they employed to survive the first few years after the change of economic model. They have now adopted aggressive internationalization strategies (América Móvil, CEMEX, Bimbo) and, as a result, a small group of large Mexican companies have consolidated their presence in international markets (Salas-Porras, 1998; Garrido, 2001).

Mexican trans-Latins have responded to a number of push factors. First, many of these companies faced limited long-term opportunities in the domestic business environment because local markets were saturated (mobile telephony, cement, food and beverages) and were affected by medium-term problems such as volatile domestic demand (car parts, white goods). A second group of factors were the corporate strategies adopted by these firms to improve their competitive situation. Many of the trans-Latins have tried to internationalize their competitive advantages (the GPS technology used by CEMEX, the distribution systems of Gruma and Bimbo, the homogeneous mobile telephony network of América Móvil) to open up new markets and consolidate existing export markets and, in general, to improve their position in the value chain. A third element is the impact of local policy changes by the country's government, as the decision to open up the Mexican economy to foreign competition, including privatization and the deregulation of services, had a very significant effect in forcing these companies to adopt more aggressive strategies.

The pull factors also encompass four elements. First, there are the location advantages of the host countries. Mexican trans-Latins have concentrated mainly on the

United States and Latin America, showing that geographical proximity and ethnic networks (language/culture) or national ones (Mexicans living outside their country) have weighed heavily in the context of the renewed growth in opportunities in these markets. A second group of pull factors are the advantages, both strategic (raising market share, forming alliances with TNCs, following local customers) and competitive (improving products and logistics and distribution systems, and turning national brands into regional ones), that internationalization can bring. Alliances with TNCs have been very important for companies like América Móvil, Gruma, San Luis Rassini, Coca Cola FEMSA and Mabe. The impact of policy changes by host governments constitutes the third group. Mexican firms took advantage of the many free trade agreements concluded to obtain preferential access to their partners' markets.

In summary, economic reforms and increasing integration into the North American market led to substantial changes in the corporate strategies of large Mexican companies. Thus, growing domestic competition and greater access to other markets encouraged Mexican businesses to abandon their passive, defensive strategies and adopt more active, aggressive ones in quest of new opportunities abroad. In an initial phase they concentrated on the United States and Central America, but then ventured into South America and other regions. At the same time, most of these companies experienced difficulties either before or while internationalizing, but fortunately succeeded in learning from their mistakes (Thomas, 2005). In a very short period of time, Mexico has succeeded in positioning several of its companies among the ranks of the largest developing-country transnationals (see table III.1).

C. Conclusions

The official statistics do not fully reflect the scale of outward FDI. Nonetheless, it is clear that a process of growing internationalization is in progress among some Latin American firms, on a scale that had no precedent in earlier cycles (first and second waves).

In Latin America, the process is largely confined to a few companies in certain countries, chiefly Argentina, Brazil, Chile and Mexico, and in a limited range of economic activities. This reflects the production structure of the region and the growth dynamic of these countries and their enterprises.

Argentina and Brazil have accrued the most experience over time. Much of this effort has gone to

waste, however, particularly in Argentina, most of whose trans-Latins have been taken over by foreign companies. In Brazil, the size of the market has discouraged greater internationalization. Nonetheless, prolonged periods of instability and uncertainty have forced the largest companies to look abroad for "insurance" against country risk. The macroeconomic conditions have meant that most companies have preferred liquidity, so investments abroad have been confined to a few large firms. Mexico and Chile, for their part, came later to the process, spurred essentially by the competitive pressures that the largest local firms were feeling in their domestic markets as a result of economic reform.

In terms of economic sectors, basic industries (hydrocarbons, mining, cement, cellulose and paper, iron and steel), some mass consumption manufacturing (food and beverages) and certain services (electricity, telecommunications, air transport, retail) account for a large proportion of internationalization initiatives. In most cases, companies' investments have been market-seeking and involved purchases of existing assets.

In a number of sectors, some Latin American companies now have a global presence. On the whole, though, this is in niches that have been neglected or ignored by the most dynamic transnationals in the world economy. The geographical coverage of trans-Latins is fairly limited, being usually restricted to neighbouring countries or the region. Outside of the basic industries, very few have operations in other continents. In the whole group, only a handful have high percentages of their sales abroad. CEMEX is the only trans-Latin that might be regarded as a transnational company of truly global reach.

This process has gone forward without any explicit support from the countries' governments. However, many of the companies that are now among the leading trans-Latins were sponsored by the State, particularly in basic industries and public services. In most cases, though, internationalization was not part of national authorities' thinking at the time these industries were fostered and developed.

The success stories have been studied, but there is probably a far greater number of cases in which internationalization failed or was cut short. There have also been successes that were beset with many difficulties along the way, or that were broken off when the companies concerned were taken over by larger global investors. The regional networks built up have proved a very valuable asset for TNCs wishing to achieve high market coverage in Latin America in a short time. Many of the companies that invested abroad in the second half of the 1990s were subsequently taken over by transnationals.

Analysis of national experiences shows that in certain areas of activity Latin American firms have succeeded in expanding their operations beyond their borders, and this is a development of great interest at a time when most global industries are undergoing powerful processes of consolidation and concentration. There are markets with few dominant global operators where trans-Latins have comparative advantages deriving from the natural resources of their home countries, the production or management capabilities developed over their history, or other assets. In other sectors, particularly those that have displayed Latin American characteristics in their consumption patterns, trans-Latins have exploited certain "niches" or gaps that have opened up. These activities are dealt with in the chapters that follow.

Annex

Table III-A.1
NATIONAL CASE STUDIES: THE CHARACTERISTICS OF INTERNATIONALIZATION
(Millions of dollars and percentages)

Country	FDI stock 2004	Percentage GDP	Percentage gross fixed capital formation 2002-2004	Main activities	Geographical distribution	Investment strategy focus
1. Developing Asia						
Singapore	101 000	94.5	24.4	Finance (57%), transport (8%), communications (7%), manufacturing	Asia, Europe, tax havens, North America	Market-seeking, efficiency-seeking, strategic asset-seeking (access to technology)
China ^a	39 000	2.4	0.2	Manufacturing (including high technology: information technology and communications equipment, other electronics) (33%), trade (20%), mining and other natural resources (18%)	Hong Kong SAR (33%), North America, Asia, Europe	Market-seeking, natural resource-seeking, strategic asset-seeking (access to technology)
Republic of Korea	39 000	5.8	2.0	Manufacturing, trade	Asia, North America, Europe	Efficiency-seeking, market-seeking, natural resource-seeking, strategic asset-seeking
Malaysia	14 000	11.7	7.7	Services (44%), hydrocarbons (36%), agriculture (9%), manufacturing	Asia (ASEAN) (36%), tax havens (25%), Europe (9%), North America (8%)	Natural resource-seeking, market-seeking (services)
Thailand	3 000	2.1	0.8	Manufacturing (33%), trade (15%)	Asia (33%), Europe (8%)	Market-seeking, natural resource-seeking
India	7 000	1.0	1.0	Services (software), manufacturing	Europe, North America, Asia	Market-seeking, strategic asset-seeking
2. Latin America and the Caribbean						
Brazil	64 000	10.7	3.7	Manufacturing (natural resource-based, car parts, aeronautics), hydrocarbons, mining, services (engineering and construction)	Latin America, Europe, North America, Africa, Asia	Market-seeking, natural resource-seeking
Argentina	22 000	14.4	...	Manufacturing (natural resource-based), hydrocarbons, services (engineering)	Latin America, Europe, Asia	Market-seeking, natural resource-seeking
Mexico	16 000	2.3	1.3	Manufacturing (natural resource-based, except car parts), services (information technology and telecommunications)	North America, Latin America	Market-seeking
Chile	14 000	15.4	6.5	Services (electricity, retail, financial services) (50%), manufacturing (mainly natural resource-based) (30%)	Latin America (Argentina-51%, Brazil-14%, Peru-14%)	Market-seeking, natural resource-seeking
3. Other						
South Africa	29 000	13.5	1.5	Natural resources (mining, hydrocarbons), manufacturing (beverages), services (information technology and telecommunications)	Europe (75%), Africa (9%), North America (9%)	Natural resource-seeking, market-seeking
Egypt	700	1.1	0.6	Services (telecommunications), manufacturing (textiles)	Middle East, Asia	Market-seeking
Turkey	7 000	2.3	1.2	Services (financial, retail) (53%), natural resources (hydrocarbons) (27%), manufacturing (household electrical appliances, electronic equipment, petrochemicals) (20%)	Tax havens, Middle East, Asia, Europe	Market-seeking, natural resource-seeking
Slovenia	2 000	7.5	5.5	Manufacturing (chemicals, machinery and equipment, food, pharmaceuticals) (33%), services (retail, financial services, management) (18%)	Former Yugoslavia (57%), Europe (25%), tax havens (11%)	Market-seeking
Russian Federation	82 000	14.0	9.1	Natural resources (hydrocarbons, mining), manufacturing (metals), services (transport, telecommunications, construction)	Europe (50%), Asia (Commonwealth of Independent States) (20%), North America (20%)	Natural resource-seeking, market-seeking (services)

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of case studies presented at the Expert Meeting on Enhancing Productive Capacity of Developing Country Firms through Internationalization, United Nations Conference on Trade and Development (UNCTAD), Geneva, 5 to 7 December 2005.

^a Excludes the outward FDI of Hong Kong Special Administrative Region of China.

Table III-A.2
NATIONAL CASE STUDIES: THE FACTORS BEHIND INTERNATIONALIZATION

Country	Push factors	Pull factors	Leading companies ^b
1. Developing Asia			
Singapore	Well-established outward investor, small domestic market, need to acquire technology, need to acquire skilled human resources, government promotion, initiatives by State enterprises	Access to external markets, following customers, improving logistics, availability of strategic assets, access to the overseas Chinese network	<i>Singtel, Capital Land, City Developments, Asia Food and Properties, Flextronics International, Neptune Orient Lines, Fraser and Neave, Keppel, Singapore Airlines</i>
China ^a	Opened up to foreign competition, initiatives by State enterprises, government promotion, scarcity of natural resources	Access to external markets, availability of natural resources, initiatives by State enterprises, access to strategic assets, access to the overseas Chinese network, avoiding trade restrictions, turning national brands into global ones	<i>China Ocean Shipping, CNPC, China State Construction Engineering Corp., CNOOC, China Minmetals Corp., Sinopec, CNCC, China Mobile, CPNG, China Resources, Haier, Huawei Technologies, Lenovo, Shanghai Enterprises</i>
Republic of Korea	Well-established outward investor, saturated domestic market, need to reduce labour costs, appreciation of local currency, scarcity of natural resources, government promotion	Availability of cheaper labour, availability of strategic assets, avoiding trade restrictions, availability of natural resources, turning national brands into global ones	<i>Samsung Corp, LG Electronics, Hyundai Motor, Daewoo, Hyundai, SK, POSCO, Samsung Electronics</i>
Malaysia	Government promotion, initiatives by State enterprises	Access to external markets, availability of natural resources, regional integration (ASEAN), access to the overseas Chinese network	<i>Petronas, YTL Corp., MUI Group, Kulim, Kumpulan Guthrie, Sime Darby, Amsteel Corp, Genting, Berjaya, Hume Ind., Telekom Malaysia, Malaysia Airline, Malaysia Int'l Shipping</i>
Thailand	Government promotion, small domestic market, need to reduce labour costs	Access to external markets, access to third-country markets via trade privileges (Generalized System of Preferences), availability of natural resources	<i>Charoen Pokphand, Banphu Group, Saha Union Group, Amata, Loxley, CP Group, Siam Cement Group, PCS Machine Group, Modern Plastic & Pkging, Jasmine</i>
India	Government promotion	Access to external markets, availability of strategic assets, availability of brands	<i>Wipro, Infosys, Tata, Ranbaxy, EsSEL Propak, Usha Beltran, Core Healthcare, Ramco Systems, NIIT, Larsen and Toubro</i>
2. Latin America and the Caribbean			
Brazil	Risks and high market share in domestic market, competition policy constraints on domestic market expansion, threats in the domestic market because of market opening and deregulation, need to break into new markets	Attractive external markets, opportunities created by privatizations and new openness to foreign competition in neighbouring countries, availability of natural resources, following customers	<i>Petrobras, Companhia Vale do Rio Doce, Gerda, Ambev, Odebrecht, Votorantim Cimentos, Usiminas, CSN, EMBRAER, VARIG, Camargo Corrêa (and Santista), TAM, Andrade Gutierrez, Klabin, EMBRACO, Marcopolo, Tigre, Sabo, WEG</i>
Argentina	Saturated domestic market, scarcity of some natural resources, growing foreign competition because of deregulation and privatization, initiatives by State enterprises, appreciation of local currency	Attractive external markets, opportunities created by privatizations and new openness to foreign competition in the countries of the region, availability of natural resources	<i>Techint (Tenaris and Ternium), Arcor, YPF (now Repsol-YPF), Pérez Compan (now Petrobras Energía), Quilmes, Impsa</i>
Mexico	New openness to foreign competition, growing external competition because of deregulation and privatization, low domestic demand, macroeconomic instability, need to consolidate export markets	Access to external markets, access to third-country markets via free trade agreements, proximity to North American market, Hispanic network in United States, improvements to logistics and distribution systems, deregulation of services, new partnerships with transnationals	<i>CEMEX, America Móvil, Bimbo, Gruma, TELMEX, Alfa, Coca Cola FEMSA, San Luis Rassini, Mabe</i>
Chile	Early economic reformer, small national market, saturated domestic market, availability of local financing for investment abroad, greater foreign competition because of deregulation and privatization, initiatives by State enterprises	Access to external markets, access to third-country markets via free trade agreements, privatizations in neighbouring countries, economy opened up to foreign competition, availability of natural resources, deregulation of services, availability of international financing (ADRs)	<i>ENAP, Falabella, Cencosud, Lan Airlines, Arauco, CMPC, CGE, ENTEL, Farmacias Ahumada, MOLYMET, Ripley, CCU, Embotelladora Andina, Madeco</i>
3. Others			
South Africa	Initiatives by State enterprises, government promotion, saturated domestic market, macroeconomic instability	Availability of natural resources, access to external markets, privatizations in neighbouring countries, access to United Kingdom network	<i>Sappi, Sasol, MTN, Barloworld, Billiton, Anglogold Ashanti, Old Mutual, South African Breweries, Dimension Data, Eskem Holdings, Vodacom, Naspars</i>
Egypt	Saturation of domestic market	Access to external markets, access to the Islamic network	<i>Prascam, Oriental Weavers</i>
Turkey	Economy opened up to outside competition, deregulation, macroeconomic instability, saturated domestic market, increase in domestic tax burden, need to reduce labour costs	Access to external markets, access to third-country markets (customs union with the European Union), availability of natural resources, privatizations in neighbouring countries, availability of subsidiaries, Turkish network	<i>TPAO, Koc Holdings, Sabanci Holdings</i>
Slovenia	Hostile business environment, small domestic market, need to increase scale	FDI "legacy", recapture of "lost" markets, access to external markets	<i>Govenje group, Mercator group, Krka d.d. Novo mesto, Prevent group d.d. Slovenj Gradec, Ultra, Petrol group</i>
Russian Federation	Initiatives by State enterprises, more flexible currency regulations, macroeconomic instability, need to diversify risks	Availability of natural resources, access to external markets, former Soviet Union network	<i>Lukoil, Norilsk Nickel, Novoship, RusAl, Primorsk Shipping, Mechel, Far East Shipping, Alrosa, Yukos, Gazprom, RAO UES, Severstal, Rosneft, MTS, OMZ</i>

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of case studies presented at the Expert Meeting on Enhancing Productive Capacity of Developing Country Firms through Internationalization, United Nations Conference on Trade and Development (UNCTAD), Geneva, 5 to 7 December 2005.

^a Excludes the outward FDI of Hong Kong Special Administrative Region of China.

^b The companies whose names are shown in italics are among the top 50 non-financial developing-country corporations (or the 10 largest in South-East Europe/Commonwealth of Independent States in the case of the Russian Federation).

Chapter IV

Trans-Latins in basic industries

A first group of trans-Latin corporations are engaged in primary activities, producing natural-resource-based manufactures and supplying basic inputs to the industrial sector. They include not only the largest companies, but also firms that were pioneers in making direct investments outside of Latin America and the Caribbean.

These enterprises' growth has generally been strongly influenced by the State. Especially in the mining and hydrocarbons sectors, some of the largest enterprises are, or used to be, State-owned. Others have flourished in protected environments or with the help of State incentives aimed at promoting specific key activities. In many other cases, private companies (that usually got

their start as family-run businesses) have attained their present scale through the purchase of State assets. These companies have invested extensively in Latin America and elsewhere in their search for natural resources and markets and are mainly involved in the hydrocarbons, mining and metal processing, cement, and pulp and paper subsectors.

A. Hydrocarbons: from resource-seeking to market-seeking strategies

Some of the first and most active Latin American companies to engage in outward foreign direct investment were hydrocarbons (petroleum and

natural gas) enterprises. This is mainly a consequence of the business logic inherent in the petroleum industry.¹

¹ Historically, technology, capital and demand have been concentrated in the United States and Europe, while the natural resources have been in Asia, Latin America and the Middle East. At the beginning of the twentieth century, Standard Petroleum and its European rivals, including Royal Dutch/Shell and Burma Petroleum (subsequently British Petroleum (BP)), were contending for the Asian markets and for the resources of the Middle East. In addition to the asymmetrical geographical distribution of reserves and consumption, uncertainty concerning the amount of reserves existing within national borders obliged the companies to diversify their investments geographically. By controlling the reserves, the main transnational petroleum corporations acquired significant positions in the petroleum product refining, distribution and marketing segments throughout the world, even in markets with significant local players (often under State control), as in the case of Latin America (Odell, 1968; Penrose, 1968).

As in the case of the first transnational petroleum corporations, the trans-Latins in the sector invested in exploration and production in places as varied as Asia, Latin America, the Middle East and the North Sea as a way of reducing the risk associated with their operations. More recently, they have also begun to invest in downstream activities in order to diversify their operations.

Two main groups currently predominate on the world market: (i) transnational corporations (TNCs) based in the major consuming countries; and (ii) State-owned enterprises in developing producer countries. This second group of corporations is particularly important because its members own about 80% of the world's known hydrocarbon reserves. The State-owned enterprises have most of their capacity in the exploration and extraction (upstream) segment, while the TNCs are net purchasers of petroleum on the world market and focus on refining, distribution and marketing (ECLAC, 2002, p. 135). Latin America is well represented among the world's largest petroleum companies in both of

these groups (see table IV.1). *Petróleos de Venezuela S.A. (PDVSA)* and *Petróleos Mexicanos (PEMEX)* are State-owned enterprises from the two countries in the region that have the largest known reserves. They are followed by the Brazilian company *Petróleo Brasileiro S.A. (Petrobras)*, which has the largest holdings of assets abroad (see table III.1), and the Argentine *Yacimientos Petrolíferos Fiscales (YPF)*, which was acquired by the Spanish company *Repsol* after being privatized in the 1990s. Further down the list are the State-owned petroleum enterprises of Colombia, Chile and Ecuador. Most of these Latin American companies have made substantial outward foreign direct investments

Many Latin American petroleum companies are or were State-owned. This does not mean that the role of the State has been the same throughout Latin America or that TNCs have not played an important role. In fact, various models for the relationship between the State and private companies (local and foreign) have been adopted and implemented, and these models have determined which firms have engaged in outward FDI.

Table IV.1
LEADING INTEGRATED PETROLEUM COMPANIES, 2004^a
(Millions of dollars and ranking)

Rank ^b	Enterprise	Country	Total sales	Reserves		Production		Refining	
				Petroleum	Gas	Petroleum	Gas	Sales	Capacity
1	Saudi ARAMCO	Saudi Arabia	116 000	1	4	1	7	7	8
2	Exxon Mobil	United States	270 772	12	14	4	2	1	1
3	NIOC	Iran	28 400	2	2	2	6	10	14
4	PDVSA	Venezuela (Bol. Rep. of)	63 200	5	6	5	12	8	4
5	BP	United Kingdom	285 059	17	15	9	4	3	3
6	Royal Dutch-Shell	Netherlands and United Kingdom	268 690	21	17	6	3	2	2
7	Chevron Texaco	United States	147 967	19	22	11	9	4	9
8	Total	France	152 610	20	21	14	8	6	6
9	PEMEX	Mexico	63 691	9	28	3	15	12	13
10	Petrochina	China	...	14	18	10	20	11	12
11	Petrobras	Brazil	36 988	18	32	13	23	9	11
12	Repsol-YPF	Spain	44 858	40	23	32	16	15	16

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of *Petroleum Intelligence Weekly*, December 2004; and *Fortune*, "The 2005 Global 500" [online] 25 July 2005, (<http://www.fortune.com/fortune/global500>).

^a The shaded lines correspond to Latin American companies.

^b Ranked on the basis of a combination of petroleum and natural gas reserves and output and of production capacity and sales of refined products.

The following general trends—although with significant interruptions—have been observed in the region (except in Mexico): (i) an important role was played by TNCs in the early twentieth century; (ii) later, State-owned enterprises were founded and petroleum assets were nationalized under the terms of different participation agreements, some of which provided for no more than a very limited role for TNCs in the industry; and (iii) since the 1990s, many corporations have been privatized, and all the various segments have been opened up to new competitors. Now, the State is beginning to take on a significant role once again in some countries. This is the case in Bolivia, where efforts are being made to reactivate Yacimientos Petrolíferos Fiscales Bolivianos (YPFB). In Argentina, the company Energía Argentina Sociedad Anónima (ENARSA) has been created, and in the Bolivarian Republic of Venezuela, the idea of establishing a State agency at the regional level for the industry is being considered. Some thought is also being given to the possibility of a joint purchase of Repsol-YPF by these enterprises (*Valor Futuro*, 2006).² It is not yet clear how these enterprises will operate in the market or how they will influence the industry's regional prospects, however.

The economic reforms of the 1990s had two significant effects on outward FDI by this industry (Campodónico, 2004). First, privatizations opened up investment opportunities for companies from other countries, including Latin American neighbours. For example, the sale of State-owned assets in Peru and Bolivia enabled Argentine and Brazilian firms to enter the petroleum and natural gas segments, while the restrictions that the Argentine authorities placed on the acquisition of YPF by Repsol created opportunities for Brazilian investors in Argentina. Second, the behaviour of companies in this industry, including State-owned enterprises, has changed, as they now give priority to profits and efficient management, as well as taking a more aggressive approach in seeking out business opportunities.

TNCs and State-owned enterprises thus dominated the industry, leaving relatively little space for the development of local private companies. Many of these companies prospered as subcontractors in support activities such as engineering and construction, however (see chapter VI). In Argentina, policies on outsourcing and the way in which YPF was privatized enabled some of these enterprises to acquire substantial reserves and begin operating as petroleum companies (Pérez Companc, Astra, Pluspetrol and Bidas). As they went through their expansion process, all of these companies made outward investments, especially Pérez Companc, and later on they were all acquired by foreign companies.

The dynamics of the internationalization of Latin American petroleum companies has largely been determined by the distribution of reserves (see table IV.2).³ In this connection, there are two general trends:

- Countries with extensive hydrocarbons reserves, including the Bolivarian Republic of Venezuela, have concentrated their outward investments in refining capacity in order to secure marketing channels (in the United States and Europe) for locally-produced petroleum (see table IV.2). In contrast, PEMEX has not made any significant investments abroad (see box IV.1).
- Countries with smaller reserves see internationalization as a way of securing their supply. Enterprises from Argentina (YPF and Pérez Companc), Brazil (Petrobras) and Chile (ENAP) have made varying investments (depending on the level of domestic reserves) in exploration and production in Asia, Latin America, the Middle East and Europe. In a second phase, they have gone on to add market-seeking operations and to invest in refining, distribution and marketing, mostly in neighbouring countries, to take advantage of opportunities arising from privatization and deregulation (see table IV.2).

² Press reports indicated that ENARSA, in partnership with PDVSA and Petrobras, and with the participation of Bolivia, might be considering the possibility of making a bid for the Spanish company Repsol-YPF, or at least its facilities and production capacity in Argentina (*Ámbito financiero*, 3 March, 2006).

³ Latin America and the Caribbean is responsible for approximately 10% of the reserves, 14% of the production and only 8% of world petroleum consumption. Nevertheless, the regional distribution is unequal, as the Bolivarian Republic of Venezuela and Mexico account for approximately 80% of the reserves, 70% of output and only 37% of consumption (BP, 2005).

Table IV.2
TRANS-LATIN HYDROCARBONS CORPORATIONS: MAIN OPERATIONS, BY SEGMENT AND GEOGRAPHICAL DESTINATION

	Latin America ^a									Others	
	AR	BO	BR	CH	CO	EC	MX	PE	VE		
PDVSA											
Exploration and production	x									x	
Refining						x				x	x
Distribution and marketing	x	x	x			x				x	x
PEMEX											
Exploration and production							x				
Refining							x				x
Distribution and marketing							x				
Petrobras											
Exploration and production	x	x	x		x	x		x		x	x
Refining	x	x	x								
Distribution and marketing	x	x	x		x			x			
ENAP											
Exploration and production	x			x	x	x		x		x	x
Refining				x							
Distribution and marketing				x		x		x			

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

^a AR: Argentina, BO: Bolivia, BR: Brazil, CH: Chile, CO: Colombia, EC: Ecuador, MX: Mexico, PE: Peru, and VE: Bolivarian Republic of Venezuela.

Box IV.1

PEMEX: IS FOREIGN INVESTMENT A SOLUTION FOR THE FUTURE?

Mexico and the Bolivarian Republic of Venezuela both have abundant petroleum reserves, and their State enterprises (PEMEX and PDVSA, respectively) are among the 10 largest petroleum companies in the world (see table IV.1). PEMEX, however, has no significant investments abroad. As in the case of the Bolivarian Republic of Venezuela, Mexico's national reserves are so abundant that it has had no incentive to invest in hydrocarbons exploration and extraction abroad, and these activities have therefore been concentrated within

the country. In contrast to the PDVSA strategy, however, refining capacity has also been concentrated in Mexico, which allows it to take advantage of its proximity to the United States.

In recent years, legal restrictions on the participation of private companies in the Mexican petroleum industry have limited the capacity of PEMEX to invest in greatly-needed refining capacity, since it cannot engage in joint ventures. The situation is similar for exploration and production activities, and PEMEX has been

unable to secure sufficient investment on its own to renew its reserves and maintain its high production rate. One partial solution has been a joint investment with Royal Dutch/Shell in a Texas refinery, an operation which is controlled by the British-Dutch firm. Possible new partnerships between the two companies are now being considered for exploration projects in the Gulf of Mexico—on the maritime border of Mexico and the United States—and in Peru. Joint refining projects have also been undertaken in Central America.^a

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of *Expansión*, "5 medidas para sanear PEMEX", 26 October 2005; and *EI Universal*, "PEMEX Internacional", 11 November 2005.

^a In addition to these investments, PEMEX owns 4.8% of Repsol-YPF.

1. PDVSA: in search of a market for its petroleum products

The Bolivarian Republic of Venezuela has the largest petroleum reserves in Latin America. Foreign companies were the first to drill petroleum commercially in this country, and they dominated production until the petroleum industry was nationalized and PDVSA was founded in 1975. Since then, both local and foreign private petroleum companies have participated in the industry through various mechanisms. At present, PDVSA takes part in a number of partnership agreements as a majority shareholder. In the 1980s, the internationalization of PDVSA was seen as a way to market locally-produced petroleum independently of the TNCs whose assets had been used to form the company. Accordingly, in order to secure control of distribution channels, PDVSA began to acquire refinery assets abroad—giving priority to partnerships with other international operators—first in Europe and then in the United States. This allowed it to expand its share of the world market, especially in the heavy petroleum trade, and to gain valuable experience in higher-value-added segments of the industry (Baena, 1999; Campbell, 2005).

In 1983, PDVSA set up a joint venture with the German company Veba Öl AG through which it controlled 50% of the Ruhr Öl refinery. PDVSA was to provide crude petroleum while Veba Öl was to provide the marketing channels in Germany and advanced refining technology. The agreement was successful for the first few years, despite the fact that the modifications needed in order for the refinery to have the capacity to process heavy petroleum from the Bolivarian Republic of Venezuela were not made. Instead, an exchange agreement was made with Russia whereby lighter Soviet petroleum was processed in the German refinery, while PDVSA sent heavy petroleum to Cuba. When the Soviet Union's support for Cuba came to an end, PDVSA had to buy lighter crude petroleum for processing in Germany.

In the mid-1980s, falling petroleum prices prompted PDVSA to try to increase its market share. Between 1983 and 2002, it spent about US\$ 4.4 billion to purchase refining, storage and marketing assets outside the Bolivarian Republic of Venezuela, including US\$ 250 million to lease

the refinery in Curaçao. Over the same period, additional contributions to affiliates abroad reached about US\$ 2 billion, for a total expenditure of about US\$ 6.5 billion (Boué, 2004). The investments associated with the PDVSA internationalization programme are probably one of the largest international capital flows to ever move from South to North (Boué, 2004).

Initially, PDVSA acquired a number of assets in the United States and Europe, including the CITGO Petroleum Corporation. In 1986, it bought 50% of CITGO in partnership with Southland Petroleum Corporation, thus gaining access to the ninth largest refinery network in the United States, which significantly increased its interests in that country.⁴ In 1989, PDVSA acquired the remaining 50% of CITGO with a view to making that company the centre of its operations in the United States.

Over the 1990s, PDVSA continued to expand its presence abroad, especially in the United States through CITGO. In 1993, CITGO increased its share in the Lyondell-CITGO refinery in Houston, Texas. In 1997, PDVSA acquired the remaining 50% of UNO-VEN, of which CITGO already owned 50%, and purchased 50% of a refinery in Louisiana in partnership with Mobil. In 1998, PDVSA bought 50% of the Amarada Hess refinery in the Virgin Islands. Early in this decade, PDVSA made some investments in South America (Argentina, Brazil, Chile, Paraguay and Uruguay), mostly in distribution. Although the results have been variable, its operations in the United States—especially through CITGO—have brought substantial profits for PDVSA (Campbell, 2005).

PDVSA has also headed up a move to reactivate the State's role in Latin America's petroleum industry by encouraging the creation of regional agencies. The role of the State has taken on greater importance since India and China have begun to work through State entities to increase their external supply sources and have begun to compete for reserves in other economies, where the status of State-owned enterprise is a significant asset. PDVSA has begun to establish itself commercially in China in order to tap into the potential of this market, where its own status as a State-owned enterprise could be an advantage.

⁴ CITGO is currently the main PDVSA affiliate abroad. With its headquarters in Houston, Texas, the company owns refining capacity—distributed among eight refineries—of over 1 million barrels/day, which are sold in the United States market. In addition, it owns a network of over 13,000 service stations in the United States and Puerto Rico which represents 10% of this market and places it among the top five gasoline distributors. It is also the fourth-largest jet fuel distributor and the largest distillate distributor.

The PDVSA internationalization process has drawn criticism from many groups, and it is currently restructuring its international assets. This overhaul includes the sale of some refinery assets in the United States and Europe as well as new projects that may involve other Latin

American State-owned enterprises and their governments. These projects include investments by PDVSA in refining capacity in north-eastern Brazil and by Petrobras in petroleum exploration and extraction in the Bolivarian Republic of Venezuela.

2. Petrobras: the integrated energy company of the Southern Cone?

In the early 1970s, Petrobras' foreign investments rapidly picked up momentum as petroleum prices climbed and as the idea gained sway that access to reserves was needed. By the end of the 1970s, the outlook for petroleum production on a significant scale in Brazil was dim. The company signed a number of technical assistance agreements, obtained tracts for exploration and coordinated Brazil's trade relations with other petroleum-producing countries, including Algeria, Colombia, Egypt (in association with Mobil Petroleum), Iran, Iraq, Lebanon and Madagascar. The Iran-Iraq conflict forced Petrobras to leave Iran. In the 1980s, Braspetro —the international subsidiary of Petrobras— continued its operations but gave priority to lower-risk areas, such as the Gulf of Mexico (in United States territory) and the North Sea, while Petrobras focused its exploration and production efforts on Brazil. Towards the end of the decade, the domestic crisis made it necessary to cut back on investment both inside and outside the country.

In the early 1990s, investment began to recover both in petroleum exploration and production in various parts of the world and in the search for new types of energy sources. In line with the Brazilian government's efforts to diversify the country's energy sources, Petrobras invested in the development of natural gas reserves, transport infrastructure and marketing channels (including thermoelectric power plants), especially in Bolivia. In 1991, Petrobras signed an agreement with the Bolivian State-owned company Yacimientos Petrolíferos Fiscales Bolivianos (YPFB) in order to obtain natural gas supplies for Brazil. Through its subsidiary Gaspetro, it also began the construction of a Bolivia-Brazil gas pipeline in association with private partners. At the same time, the federal and state authorities worked to promote the use of natural gas by increasing thermal generation capacity —mostly through Petrobras investments— and encouraging the development of gas distribution networks in metropolitan areas.

In 1997, when fundamental changes were made in Brazil's legislation concerning this sector, Braspetro still had partnerships with more than 70 petroleum companies

and had 140 exploration contracts in nine countries: Angola, Argentina, Bolivia, Colombia, Ecuador, Lebanon, Peru, the United Kingdom and the United States. Recently, the company has begun to invest in Iran (after 20 years outside the Middle East), Tanzania and other countries. During this process, Petrobras has managed to develop significant competitive advantages, including the sophisticated deep-water drilling technology it uses in a number of its foreign exploration and production operations. Its status as a State-owned enterprise has also been a significant asset in some cases.

Petrobras has continued to increase its presence in the gas and petrochemicals markets in neighbouring countries. It invested in gas pipelines to supply gas to thermal power plants on the border with Uruguay, purchased a share of Companhia Mega S.A., a joint venture with YPF and Dow Investment Argentina (28%), and reached an agreement with the National Administration of Fuel, Alcohol and Cement (ANCAP) of Uruguay for the exploration of natural gas and the operation of a lubricants plant.

The regulatory changes in Brazil and the prevailing uncertainty regarding what role Petrobras would play in a market open to new competitors ushered in a new phase in its internationalization process. The company increased its operations in the fuel refining, marketing and distribution segments in neighbouring countries. These investments were also intended to achieve vertical integration in the local market in order to manage the risk associated with fluctuations in the different segments in which it participated. Many of these initiatives were made possible by privatizations and other institutional and regulatory reforms in the countries of the region. Between 1999 and 2002, Petrobras invested in refineries and in fuel distribution in Bolivia. In 2000, Repsol-YPF and Petrobras negotiated an asset swap, whereby Petrobras acquired the network of 700 Eg3 service stations in Argentina and a refinery in Bahía Blanca in exchange for a 10% stake in the Albacora Leste field, 30% of the REFAP refinery and exclusive distribution rights for 250 service stations (Petrobras, 2001). This agreement, which was undertaken

in response to restrictions that the Argentine competition protection authorities placed on the purchase of YPF by Repsol, enabled Petrobras to acquire approximately 12% of the Argentine fuel market and helped to generate synergies with its assets in the south of Brazil and Bolivia.

In 2002, Petrobras consolidated its interests in Argentina with the purchase, for US\$ 1.125 billion, of a majority share in Pecom Energía (PECOM), part of the Argentine conglomerate Pérez Companc. With this operation, Petrobras strengthened its position in Latin America in terms of hydrocarbons reserves and production, in downstream activities such as refining, distribution, marketing and petrochemicals, and in gas transport and energy generation assets. At the time of this purchase, Pecom Energía was the largest independent petroleum company in Latin America, with operations in Argentina, the Bolivarian Republic of Venezuela, Bolivia, Ecuador and Peru (see box IV.2). Petrobras also acquired Petrolera Santa Fe, the Argentine affiliate of Devon Energy Corporation, a company engaged in the exploration, development and production of petroleum and natural gas reserves, for which it paid about US\$ 90 million.

The Brazilian petroleum company has recently made significant progress in diversifying its energy sources and its presence in the region. Over the period 2002-2005, Petrobras invested in gas processing and transport assets in

Uruguay in an effort to integrate electricity generation into its operations (Petrobras, 2002). In 2005 it entered the gas distribution business in Uruguay (Petrobras, 2005). The natural gas from reserves outside Brazil is transported through its gas pipelines to the domestic market in order to fuel its generators, as well as to provide an energy supply for other activities. The strategic purchase of Pecom Energía has given it access to all segments of the electricity business in Argentina, which serve to complement its reserves in that country.⁵

Like other companies, Petrobras has taken advantage of the restructuring of the British-Dutch firm Royal Dutch/Shell in order to continue expanding its interests in downstream segments (see box IV.3). In December 2005, the Brazilian company acquired its fuel businesses in Colombia and all of its operations in Paraguay and Uruguay for an approximate total of US\$ 140 million. These assets are an excellent complement to its existing Latin American assets and offer good opportunities for growth and synergy.

In short, Petrobras has followed an internationalization strategy in which it combines the expansion of its hydrocarbon reserves with a growing diversification of its business. Initially, the scarcity of reserves in Brazil prompted the company to start up exploration and production activities abroad. Subsequently, with

Box IV.2

PÉREZ COMPANC: FROM LARGEST REGIONAL PRIVATE PETROLEUM COMPANY TO AFFILIATE OF THE MOST INTERNATIONALIZED STATE COMPANY IN LATIN AMERICA

The experience of Pérez Companc, although brief, is the most significant case in terms of the internationalization of a private petroleum company. The company entered the petroleum industry as a service provider for YPF and subsequently began to operate abroad as a subcontractor in the late 1970s. In the early 1990s, it made a strong entry into the petroleum business in the Argentine domestic market and soon afterward expanded its activities abroad, concentrating on exploration

and production in Brazil, Bolivia, Ecuador, Peru and Venezuela (Gadano, 1990; Campodónico, 1998; and ECLAC, 2004).

In 1996, Pérez Companc, together with YPF and PlusPetrol, purchased shares in Andina, a company resulting from the capitalization of YPFB. In 1999, it took a step towards integrating its activities in Bolivia by acquiring, in association with Petrobras, two refineries with a joint capacity of

60,000 barrels/day. In 2000, as part of an asset swap with Repsol-YPF, it gave up its stake in Andina S.A., as well as 50% of the gas fields in the San Jorge gulf in southern Argentina, in exchange for the Repsol-YPF share of the natural gas deposits of Santa Cruz I (30%) and Santa Cruz II (62.2%), also in southern Argentina (ECLAC 2002).^a As in the case of YPF, this brief experience with internationalization proved to be an extremely attractive asset when the company was sold to Petrobras in 2002.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

^a Pérez Companc also invested in petrochemicals (Innova Project) in Rio Grande do Sul, in Brazil.

⁵ Petrobras now generates 6.5% of the country's electricity through Generación Eléctrica Buenos Aires (GENELBA) and the Piedra del Águila and Pichi Picún Leufú hydropower plants. It also shares joint control of Transener, the main transmission company, and owns a significant share of EDESUR (controlled by the Spanish company ENDESA), the distributor for the central and southern sections of the City of Buenos Aires.

deregulation of the sector on the horizon and the need to diversify the Brazilian energy grid, Petrobras embarked upon a new phase in which it gave priority to integrating the different segments of the industry. In addition to continually increasing its hydrocarbon reserves, it expanded its fossil fuel refining, distribution and marketing activities and extended its vertical integration into the natural

gas/electric power chain. Petrobras is thus becoming an important link in energy integration in the Southern Cone of Latin America (ECLAC, 2005, chapter III). On a smaller scale, the internationalization process of Petrobras—whereby it has shifted from upstream to downstream activities—has been emulated by other companies in the region (see box IV.3).

Box IV.3

ENAP: INTERNATIONALIZATION BASED ON COMPETITIVE ADVANTAGES DEVELOPED IN THE DOMESTIC MARKET

The Empresa Nacional del Petróleo (ENAP) of Chile has gone through an internationalization process similar to that of Petrobras, but on a smaller scale. Sipetrol, the exploration and production affiliate of ENAP, created in 1990, has made investments in Argentina, Colombia, Ecuador, Egypt, Iran and Yemen. In 2004, 86% of the company's output was produced abroad, mostly in Argentina. The first investments were typically minority interests in partnerships with international companies, and their main objectives were to add value to the company by expanding its petroleum and natural gas reserves, develop technical competencies in areas of the Middle East which were seismically and geologically similar to Chilean petroleum fields, and gain technological knowledge and expertise in offshore operations.

ENAP recently took advantage of its experience in the local market to redefine its internationalization strategy so as to focus on markets for refining and sales of petroleum products. It was very difficult to enter these segments of the local market

for two main reasons: (i) local and foreign companies were already well-established; and (ii) these companies were ENAP's main clients for its refined products, especially gasoline. An opportunity to enter this market arose in Peru and Ecuador, and the second stage in the internationalization of the company was under way.

In August 2004, ENAP purchased the Peruvian affiliate of the British-Dutch Royal Dutch/Shell company, which included a network of 165 service stations in Lima and in the coastal region of Peru, as well as its wholesale and lubricants distribution businesses. Once the operation was concluded, the acquired company merged with Romero Trading, a consortium with extensive experience in the fuel wholesale business. The new company, known as Primax SA, became the leader in the Peruvian fuel and lubricant market with a 27% market share.

In December 2005, ENAP repeated the Peruvian experience and, through Primax SA, acquired the fuel distribution business of Royal Dutch/Shell in Ecuador. The Shell Ecuador

assets include a network of 60 service stations that represent about 10% of the retail market.

With these operations, ENAP intends to establish a leading position in refining, logistics and marketing on the Pacific coast of South America. These new markets will also be a major destination for exports of refined products produced in Chile.

In short, ENAP, like Petrobras, began its international expansion by seeking out reserves that were scarce in its home country. The company gradually expanded its geographical coverage, which was initially concentrated in Argentina, to more distant locations such as Egypt and Yemen. Its exploration experience in the south of Chile and Argentina enabled it to develop significant competitive advantages in offshore operations, which it used in its subsequent projects abroad. Most recently, it has taken an important step in diversifying its internationalization strategy by incorporating the advantages gained in the domestic refining market through the acquisition of Royal Dutch/Shell assets in Peru and Ecuador.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

3. The Argentine trans-Latin petroleum corporations: a tasty morsel for TNCs

As mentioned earlier, Argentina stands out among the Latin American countries because of the opportunities offered by its hydrocarbon policies, which have paved the way for the emergence of private local companies in different segments of the industry. Many of them made outward foreign direct investments, but later on they were all purchased, either entirely or in part, by foreign companies. The smaller petroleum companies that made such investments included Pluspetrol and Astra, both part-

owned by Repsol-YPF, and Bidas, controlled by British Petroleum (BP). The most significant experiences were those of YPF (now Repsol-YPF) and Pérez Companc (now known as Petrobras Energía) (see box IV.2).

In the early 1990s, YPF was partially privatized (the State kept a large share) and restructured, and in 1999 it was sold to the Spanish company Repsol, forming Repsol-YPF. In between those two landmark events, in 1995, it acquired the company Maxus Energy, based in Dallas,

United States, and through that company, assets and rights in petroleum and gas fields in the Bolivarian Republic of Venezuela, Bolivia, Ecuador, Indonesia, Peru and the United States. Subsequently, YPF purchased 50% of the Bolivian company Andina (one of the two enterprises which resulted from the capitalization of the Bolivian State-owned petroleum company YPFB) in partnership with Pérez Companc and Pluspetrol (Gadano, 1998). Some of these investments were made in partnership with its future purchaser, Repsol. From the late 1980s on, the two companies went ahead with a number of joint exploration projects, including ventures in Bolivia, Indonesia and Peru.

In the mid-1990s, the company began to move into refining and marketing outside Argentina. In 1996, YPF and Repsol made a joint investment in Refinadores del Perú (REFIPESA), owner of 60% of the La Pampilla refinery, which accounted for about 50% of the country's refining capacity. Subsequently, YPF invested in service station networks in Brazil, Chile, Ecuador and Peru and in refineries in Brazil and Peru (Gadano, 1998).⁶

The substantial presence of YPF outside Argentina was highly valued by Repsol when it decided to buy the company. In addition to the strong complementarity of the two enterprises' assets, the acquisition of YPF automatically gave Repsol a solid position in Latin America and assets in other parts of the world. When this operation was completed, Repsol-YPF embarked on a plan to sell off some of its non-strategic assets in order

to concentrate on the regions with the most potential. In fact, geographical diversification is one of the pillars of its strategic plan for 2003-2007. Repsol-YPF now has interests in Africa, Europe, Latin America, the Middle East and the United States. In 2007, about 44% of production is expected to take place outside Argentina (Repsol-YPF, 2004).

In short, Latin American petroleum companies have been significant outward direct investors. Many of them are still State-controlled, and their governments have therefore had a central role in defining their strategies. Companies that were privatized have quickly been snapped up by international operators. Generally speaking, the nature of the internationalization process has been determined by the characteristics of national reserves. The companies of reserve-rich countries, in particular the Bolivarian Republic of Venezuela, have invested mainly in refinery capacity and in other downstream activities such as distribution and marketing. The aim of this strategy has been to obtain external markets for the petroleum produced by the country. In contrast, for the companies based in countries with smaller reserves, internationalization has been a mechanism for securing a supply for the domestic market. Nevertheless, in a subsequent phase, the most successful companies have moved downstream into refining, distribution and marketing in order to extend their strong vertical integration in the domestic market into the international arena, especially in neighbouring countries.

B. Mining and metal processing: a costly wager

The mining industry's course of development has been similar to that of the hydrocarbons sector, although its concentrative effects have been stronger. In the 1990s, the proliferation of liberalization and privatization policies, together with an upswing in the demand for minerals and metals, encouraged the leading mining companies to embark on ambitious plans to expand production capacity and invest in exploration and the mining of new deposits. The financial requirements of the mining industry's expansion marked a sharp contrast with the slowdown seen in other economic activities, however.

Starting in the second half of the 1990s, in particular, mergers and acquisitions became more frequent and contributed to the concentration of the mining industry. TNCs sought to increase their profitability by generating productive and management synergies, thereby improving their capacity to capture investment funds on international capital markets and boost their relative share of world trade. As a result, a small group of Australian, British, Canadian and United States companies, together with a few from Latin America, now dominate the industry (see table IV.3).

⁶ At the end of the 1990s, YPF had 147 service stations in Peru, amounting to 7% of the market, and 107 service stations in Ecuador, a market share of 12% (Repsol-YPF, 2000).

Table IV.3
LEADING MINING COMPANIES IN THE WORLD, BY SALES, 2004^a
(Millions of dollars)

Company	Home country	Main products	Sales	Regions where operating outside of the home country ^b				
				NA	LAC	EU	AS	OT
1 BHP Billiton	United Kingdom, Australia	Copper, coal, iron silver and nickel	29 587	x	x		x	x
2 Anglo American Plc	United Kingdom	Coal, gold, copper and nickel	24 930	x	x	x	x	x
3 Rio Tinto Group	Australia	Iron, cooper	11 799	x	x	x	x	x
4 Phelps Dodge	United States	Cooper, molybdenum and coal	8 287	x	x	x	x	x
5 Corporación Nacional del Cobre de Chile (CODELCO)	Chile	Copper, molybdenum	8 204					
6 Companhia Vale do Rio Doce (CVRD)	Brazil	Iron, manganese, copper and nickel	8 066	x	x	x	x	x
7 Mining and Metallurgical Company Norilsk Nickel	Russia	Nickel, copper, gold silver	7 033	x				
8 Newmont Mining	United States	Gold, coal and iron	4 524	x	x		x	x
9 Inco Ltd.	Canada	Nickel	4 278				x	
10 Grupo México	Mexico	Copper, molybdenum, silver and gold	4 206	x	x			
11 Barrick Gold Corporation	Canada	Gold and silver	1 932	x	x		x	x

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the companies.

^a The shaded lines correspond to Latin American companies.

^b NA: North America (United States and Canada), LAC: Latin America and the Caribbean, EU: Western and Eastern Europe, AS: Asia, OT: Others.

Latin America has played a significant role in the changes seen in this industry. In view of its abundant and diverse endowment of mining resources, the region has become the main destination for investment in exploration, with the activities in this area concentrated in five countries: Argentina, Brazil, Chile, Mexico and Peru. This process has also spurred large inflows of FDI, which have considerably increased the presence of private capital—especially from the large mining TNCs—and consolidated the local companies as relevant actors in the sector.

National governments have played an important role because of their position as asset holders. TNCs have, in general, played a significant part as well, but local firms have been the most important players in their domestic markets. Examples include the Companhia Vale do Rio Doce (CVRD), which produces iron ore in Brazil, and the Corporación Nacional del Cobre (CODELCO) and Grupo México, which are engaged in copper mining in Chile and Mexico, respectively. With support from explicit government policies, processing and refining companies have emerged and formed industrial clusters, such as the following:

- Brazilian iron and steel companies – Gerdau, Usiminas, Companhia Siderúrgica Nacional (CSN) and Companhia Siderúrgica de Tubarão (CST).
- The Argentine company Techint and the Mexican company IMSA, which are leaders in the segments of seamless tube fabrication and galvanized sheets, respectively.
- Madeco and Molymet, Chilean companies whose operations have been boosted by the development of the copper mining industry, have become major producers of copper and molybdenum rods.

With a well-established position in their home countries, some of these companies began to make outward investments, mainly by taking advantage of the opportunities offered by privatization programmes. In most cases, these firms used the internationalization of their operations as a mechanism to gain access to natural resources and diversify their production or to enter protected markets and harness production and management advantages. Thus, a significant part of the FDI outflows from Latin America and the Caribbean have come from companies in the mineral and metal extraction and processing industry.

1. Mining: a capital-intensive and highly uncertain activity

As mining is capital-intensive and subject to strong uncertainties, the industry can develop only through financially sound companies having sophisticated technical capacities. In Latin America, a great deal of mining activity has been conducted with substantial State support and/or differing degrees of participation by private groups, both local and foreign. Internationalization processes have been few in number, but significant in terms of the financial resources involved, especially in the cases of the Companhia Vale do Rio Doce (CVRD) and the Grupo México.

In the first case, State involvement was vital in implementing an early vertical integration strategy aimed at securing markets for the iron ore produced in Brazil. When CVRD was privatized, its priorities in relation to its international expansion began to change. The company began to concentrate on its main activity—mining—and sought greater diversification within this activity. In contrast, the internationalization experience of Grupo México is much more recent and has entailed a reorganization of its controlling shareholders' equity positions. The Mexican company has succeeded in positioning itself as one of the world's leading copper mining enterprises (see table IV.3).

(a) CVRD: from verticalization to international expansion of its core business

Brazil has extensive reserves of iron ore (the most heavily mined and used mineral on the planet) and has become the world's second-largest producer, after China. CVRD is the leading company in this sector in Brazil and Latin America. It is also the largest exporter of iron ore and pellets at the global level and sells its products to the iron and steel industry in five continents. Based on this leadership position, the State-owned CVRD got an early start on its international expansion drive.

In the first phase of this process, during the 1980s, the company tried to secure markets for Brazilian exports of iron ore by means of the vertical integration of its operations. The State's ownership of the company served as the framework for this strategy's implementation. The Brazilian State was also the owner of Companhia

Siderúrgica de Tubarão (CST), a slab producer. In 1984, CVRD, in partnership with a Japanese firm, acquired California Steel Industries (CSI), one of the main sheet steel producers of the United States.⁷ With this acquisition, the Brazilian State gained control of three vertically integrated segments. Through subsequent privatizations and the purchase of CST shares by CVRD and CSI, this level of integration was maintained until 2005.

In 1992, CVRD acquired 35% of the French company Société Européenne D'Alliage pour la Siderurgie (SEAS). Later in the same decade, CVRD bought the remaining part of SEAS and changed its name to Rio Doce Manganése Europe (RDME), thereby securing a market for its manganese.

Once it was privatized, CVRD embarked on the second phase of its internationalization process while maintaining the strategic orientation of the first phase. During this second phase it extended its geographical coverage to the Middle East and strengthened its interests in Europe. In October 2000, CVRD and the Gulf Investment Corp. (GIC) jointly acquired a company located in Bahrain, Gulf Industrial Investment Co. (GIIC), whose main asset was an iron pellet plant. CVRD began to process raw materials brought from Brazil and to supply pellets to the steel industry in the Middle East.

In 2003, CVRD acquired Elkem Rana, a Norwegian ferrochromium producer, which it renamed Rio Doce Manganese Norway (RDMN) and converted into a ferromanganese plant. With this acquisition, CVRD gained access to the European market for the manganese extracted in northern Brazil (which had previously been considered to be a waste product) and managed to avoid the trade sanctions imposed by the United States on ferro-alloys produced in Brazil. This operation turned CVRD into the European market's leader in manganese alloys, with a share of close to 40%.

The third stage in the company's internationalization process nearly paralleled the second one. This new cycle was triggered by the consolidation of the global iron ore industry starting in 2001. This trend stemmed, to a large extent, from the long-term price outlook (even though demand in China had pushed prices up to record levels between 2000 and 2005) and the need to cut costs and

⁷ In order to carry out this operation, good relations between CVRD and Kawasaki Steel were essential. From the second half of the 1970s on, in addition to being one of the company's largest clients, Kawasaki Steel partnered with CVRD and other State-owned enterprises in various projects in Brazil. Kawasaki Steel and NKK merged in 2001 to form JFE Steel.

boost production. The three largest producers (CVRD, Rio Tinto and BHP Billiton) increased their share of the world market from 48% to 58% between 1996 and 2000, and by 2004 their share had expanded to 74% (De Paula, 2002, 2005a). CVRD turned its attention back to mining (its main business) and began to reverse the diversification and vertical integration process that it had set in motion earlier. Between 2000 and 2005, it overhauled its corporate structure and began to sell off assets in areas that it no longer considered to be strategic. These assets included its shares in CSN, Açominas and especially CST, which was sold to the steel industry's world leader, ARCELOR (see table IV.4). Moreover, In May 2005, the CVRD Board of Directors recommended the sale of the company's stake in CSI.

CVRD was also one of the companies whose assets were the most heavily concentrated in a single geographical area (90% in Brazil) and one of the least diversified in terms of products (see table IV.3). The company therefore needed to improve its ability to compete with its main rivals. It thus began to plot out a new strategy of geographical and product diversification with a view to improving its management of the risks associated with operations in Brazil and the cycles of the iron ore industry. The sector's high degree of concentration limited the number of options available for achieving further growth (any acquisition would have been very expensive), and this situation was compounded by the administrative difficulties resulting from the restrictions established by competition authorities in Brazil and abroad.

Given the iron ore industry's advanced stage of organization and consolidation in Brazil, and with surpluses generated by the rise in international prices, CVRD embarked upon new outward investments, mainly in mineral prospecting, exploration and production. Until the early years of this decade, all of the investments made by CVRD in prospecting had been in Brazil. In 2002, the company began exploring for copper and gold in Chile and Peru. In 2003, it launched a manganese project in Gabon, and the following year it began coal and copper exploration projects in Mongolia. By 2005, approximately 37% of the company's prospecting budget was invested abroad. CVRD currently has exploration offices in Angola, Argentina, Australia, Bolivarian Republic of Venezuela, Chile, Gabon, Mozambique, Peru and South Africa. This new strategy has included a special role for one particular mineral: coal.

Despite the fact that some of its main competitors (BHP Billiton and Rio Tinto) were already producing coal, this mineral offered an excellent opportunity for

CVRD, since it is an important input for the steel industry, including the company's main clients. To date, CVRD has initiated a number of projects, basically through greenfield investments, although acquisitions are not excluded from its plans. The locations of the projects include Mozambique and China.

In November 2004, CVRD acquired a coal exploration concession in Mozambique for US\$ 123 million. The company controls 95% of the project, while the United States company American Metals and Coal International (AGCI) owns the remaining 5%. This venture calls for US\$ 1 billion in investments and will entail development of the deposit and the construction of a port. Operations are expected to begin in 2009. It is currently the largest CVRD project outside Brazil.

Also in 2004, CVRD launched two projects with some of the largest coal producers in China. First, it formed a consortium with Yankuang and the Japanese company Itochu to produce coal and methanol in Shandong province. It then set up a partnership with Yongcheng Coal & Electricity Group, another major Chinese producer, and Shanghai Baosteel, China's main steel maker, to produce coal. In both cases, it has acquired a minority interest as a way of becoming more knowledgeable about the coal market and gaining access to natural resources that it can use in its Brazilian operations.

Given the currently high level of iron ore prices, CVRD will probably continue to increase its outward foreign investments while extending and consolidating the main components of its internationalization strategy's third phase, which focuses on further geographical and product diversification. The company estimates that the portion of its assets located outside Brazil will increase from 8% to 30% of the total within about 10 years.

(b) Grupo México: buying out the controlling company

At the beginning of the twentieth century, the United States company Americas Smelting and Refining Company (ASARCO) began mining in Mexico. In the mid-1960s, it was reorganized to form ASARCO Mexicana, which was 51% Mexican-owned. During this period, the company expanded under the wing of policies implemented by the Mexican Government to develop the mining industry. In 1974, ASARCO Mexicana was renamed Industrial Minera México (IMMSA) and ASARCO reduced its share to 34%. Two years later, IMMSA was reorganized to form Grupo Industrial Minera México (GIMMEX). In the late 1980s and early 1990s, GIMMEX capitalized on the privatization

of State assets to incorporate Mexicana de Cobre and the Cananea deposit in Sonora.⁸ In 1994, Grupo México was created to replace GIMMEX, and a new phase of expansion began with the acquisition of cathode and concentration plants, smelters and refineries.

By the end of the 1990s, Grupo México had become Mexico's largest mining cluster. It was vertically integrated and based on copper mining, with numerous rail transport assets. At that time, all of its operations were in Mexico and ASARCO still owned part of the cluster. The company began to look at expanding its operations abroad, and began by acquiring the company that had created Grupo México's predecessor some one hundred years earlier, and with which it had a longstanding relationship.

In September 1999, Grupo México launched a hostile takeover bid for ASARCO, which it acquired for over US\$ 2.2 billion. This conduct of this operation required an elaborate financial strategy which, at the time, drew criticism from analysts and investors, who regarded it excessively risky given the situation of ASARCO as a low-profit, high-cost operation facing a large number of suits over environmental issues.⁹ Grupo México's real interest, however, lay in the 54.2% share that ASARCO owned in the Peruvian company Southern Peru Copper Corporation (SPCC), one of the world's most profitable copper mines.

Any uncertainties involved in Grupo México's wager were soon dispelled by the rise in copper prices and a far-reaching restructuring process that considerably improved

the company's financial results. Grupo México split SPCC off from ASARCO as part of the restructuring, and made it an independent company. The SPCC assets formerly owned by ASARCO were transferred to the Americas Mining Corporation (AMC), a subsidiary of Grupo México that controlled all the group's mining assets.¹⁰

This reorganization enabled SPCC to continue expanding its operations in Peru. Concentration plants (Cuajone and Toquepala) were modernized, the Cuajone mine was expanded, which increased its reserves from 10 to 40 years, and a world-class metallurgy complex is now being built in the coastal city of Ilo. Operations in the United States were cut back rapidly and substantially.¹¹

At the end of 2004, SPCC and Grupo México merged their operations to form the second-largest producer of copper and the second-largest copper company in terms of market capitalization. The merged company also owns the world's second-largest reserves of copper. By contrast with CVRD, Grupo México has a well diversified portfolio in terms of mining products and geographical areas, which should help it to hedge risks and increase the scale of production.

In short, in a very capital-intensive and highly uncertain industry, the main Latin American companies, CRVD and Grupo México, have sought to build up their presence in an increasingly concentrated global market. They have deepened their product specialization and abandoned some of their efforts to move up the value chain in order to focus on mining activities.

2. The iron and steel industry: jostling for position in a consolidating international industry

As noted earlier, unlike mining activities, the bulk of capacity for making iron ore into steel is located close to consumer markets, in other words, in developed countries. Nevertheless, as part of the industrialization processes that took place in the twentieth century, some industrial clusters also grew up to take advantage of proximity to the iron ore. In Latin America, explicit industrialization

policies, the creation of large State-owned enterprises, the strength of local family groups and early partnerships with foreign investors (mainly in Brazil) have helped to create a powerful steel industry. Brazil and Mexico are the region's largest steel producers today, ranking eighth and fifteenth, respectively, in the world. Brazil is also the world's fourth largest exporter of steel.

⁸ In 1988, investors linked to GIMMEX acquired 95% of Mexicana de Cobre for US\$ 690 million, at public tender. Two years later, a consortium consisting of Mexicana de Cobre (76%) and ACEC Union Minière of Belgium (24%) acquired 100% of the Cananea mine at public tender for US\$ 524 million. In 1997, Grupo México acquired the Belgian company's 24% share in the Cananea complex.

⁹ To make this acquisition, Grupo México had to more than double its liabilities, to take control of a company twice its own size.

¹⁰ AMC purchased SPCC assets from ASARCO for US\$ 765 million, thereby alleviating the precarious financial situation of ASARCO.

¹¹ In August 2005, ASARCO, now consisting of all of Grupo México's assets in the United States (other than those of SPCC) filed for bankruptcy after a six-week strike by workers at the Arizona mines and a Texas refinery. Grupo México's controlling shareholders remained optimistic, however, as the bad news coming from this relatively small investment in the United States had shrunk the company's value.

Although Latin American producers are not among the industry's largest companies, they do possess significant competitive advantages, given their access to high-quality, low-cost iron ore (especially in the case of integrated companies), low costs of other inputs and their management capacity. In the last few years they have climbed up in the ranks, mainly through mergers and acquisitions and very often by seizing the opportunities offered by privatization programmes (see table IV.4). In part, this trend has been a response to the consolidation of the industry, especially in Europe, and companies' drive to emulate their global rivals in terms of scale and competitiveness.¹²

In this context, companies faced an imperative to expand. Domestic markets were too limited, so they began to seek new opportunities abroad. Indeed, the circumscription of the domestic market was a barrier to reaching a threshold scale for efficiency, and this was worsened by the competition authorities' reluctance to approve fresh domestic acquisitions. Like in other industries, international expansion was also a means

of hedging risks through geographical diversification of assets and helped to overcome the protectionist barriers established in the main export markets.

The divestment of State assets was one of several factors that were crucial to the process of internationalization of Latin American iron and steel companies. In Brazil and Argentina, Gerdau and Techint expanded locally through such privatizations, giving them a solid domestic position to begin investing abroad, initially by bidding in other privatization processes and acquiring private assets. Privatization also helped formerly State-owned companies, such as CSN, to develop profit-seeking forms of management, improve administrative practices and enhance their capacity for seeking business opportunities around the world.

The Brazilian steel industry was one of the first to open up to foreign investors. In 1921, the Luxembourg iron and steel group ARBED (now part of ARCELOR) acquired shares in Belgo-Mineira. In the 1950s, Mannesmann of Germany was producing steel in Brazil and Japanese TNCs such as Nippon Steel and Kawasaki, as well as

Table IV.4
WORLD'S LARGEST STEEL COMPANIES, BY OUTPUT AND SALES, 2004^a
(Millions of metric tons and millions of dollars)

	Company	Country of origin	Output	Sales	Regions in which the company has foreign operations ^b				
					NA	LA	EU	AS	OT
1	Arcelor	Luxembourg	46.9	41 160	x	x	x	x	
2	Mittal Steel N.V.	Netherlands	42.8	22 197	x	x	x	x	x
3	Nippon Steel	Japan	32.4	27 696	x	x		x	
4	JFE	Japan	31.6	23 416	x			x	
5	POSCO	South Korea	30.2	23 158	x	x		x	x
6	Shanghai Baosteel	China	21.4	19 524	x	x		x	
7	US Steel	United States	20.8	13 969			x		
8	Corus Group	United Kingdom	19.0	17 891	x				
9	Nucor	United States	17.9	11 376				x	
10	ThyssenKrupp	Germany	17.6	11 401	x	x	x	x	x
11	Riva Acciao	Italy	16.7	9 572	x		x		x
12	Internacional Steel Group (ISG) ^c	United States	16.1	...					
13	Gerdau	Brazil	14.6	6 952	x	x	x		
44	Companhia Siderúrgica Nacional (CSN)	Brazil	5.5	3 084	x		x		
49	Techint	Argentina	5.2	11 325	x	x	x	x	
53	Usiminas	Brazil	4.7	4 594		x			

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of International Iron and Steel Institute, *World Steel in Figures, 2005*, Brussels.

^a The shaded lines correspond to Latin American companies.

^b NA: North America (United States and Canada), LA: Latin America and the Caribbean, EU: Western and Eastern Europe, AS: Asia, OT: Others.

^c In April 2005, ISG merged with Mittal Steel.

^d Includes sales of the steel segment only; corresponds to fiscal year 2004-2005.

¹² Between 1984 and 1997, 37 steel companies in 22 countries were privatized, resulting in a high level of country-concentration and large volumes of FDI. An intense wave of mergers also helped to consolidate the industry at the global level. Prominent among these mergers were: Thyssen and Krupp, which formed ThyssenKrupp Stahl (1997); British Steel and Hoogovens, which merged to form Corus (1999); Outokumpu and Avesta Sheffield, which established Avesta Polarit (2000); and Usinor, ARBED and Aceralia, which formed ARCELOR (2001), the largest company in the industry (see table IV.4).

Finsider of Italy, were key partners of the Brazilian State in establishing large foundries, first Usiminas in 1956, then Companhia Siderúrgica de Tubarão (CST) in 1976. New foreign investors moved in after the privatization, one such being NatSteel, which bought part of Aço Minas Gerais (Açominas). This situation limited the international expansion strategies of a number of Brazilian companies that were partially controlled by leading global operators. This was the case of Belgo-Mineira, controlled by ARCELOR, and Usiminas, whose holding group's largest shareholder is Nippon Usiminas, which is led by Nippon Steel. This could explain why these firms' internationalization efforts have been limited to minority shares in partnerships with other Latin American firms.

Gerdau and Techint are the largest steel companies in Brazil and Argentina, respectively, and they have the most significant international interests. Both companies have longstanding international experience, which is particularly interesting in a context of intense consolidation of the global iron and steel industry.

(a) Gerdau: keeping close to inputs and consumers and internationalizing its business with a structure of mini-mills

In the second half of the twentieth century, Gerdau grew rapidly within the Brazilian market, through acquisitions, greenfield investments and the expansion of existing plants. In the 1990s, it was actively involved in the privatization programme, in which it acquired a number of companies (Cimetal, Usiba, Piratini and Cosinor). In 1996, in partnership with NatSteel, it bought shares in Açominas, which had been privatized in 1993. Gerdau later went on to purchase a majority stake in Açominas and, in 2003, restructured all of its local operations under the name Gerdau Açominas.

At the beginning of the 1980s, while it was consolidating its position in Brazil, Gerdau acquired the Uruguayan steel producer LAISA. This small-scale, low-risk operation served as a valuable learning experience for subsequent investments and operations abroad. Nevertheless, Gerdau's process of international expansion was not to gather momentum until almost ten years later. Between 1989 and 1998, Gerdau complemented its domestic growth with acquisitions of relatively small operations, usually mini-mills specializing in long steel products.

Gerdau's early international expansion consisted of the acquisition of a number of operations in the Southern Cone (Argentina, Chile and Uruguay), which enabled

it to take advantage of an extensive and consolidating market to substitute exports and establish a structure based mainly on mini-mills. In 1997, Gerdau decided to focus its internationalization process on Argentina, where a large portion of its exports went. At the end of that year, the company bought a controlling share in Sociedad Industrial Puntana S.A. (SIPSA), a rolling mill in the province of San Luis. A few months later, Gerdau purchased a 33% share of SIPAR Laminación de Aceros in exchange for 33% of SIPSA. With the two companies, Gerdau had acquired around 20% of the long steel market in Argentina. At that time, SIPAR was supplied by Gerdau, Açominas and Acindar so, with the acquisition, Gerdau and Açominas (in which the Brazilian firm already owned shares) became its sole suppliers. In this way, Gerdau's share in Açominas opened the way to the Argentine market without having to set up a whole new operation. In 2004, it expanded its interests in Latin America by acquiring a majority share in the Colombian companies Distribuidora de Aceros Colombianos (DIACO) and Siderúrgica del Pacífico (SIDELPA), which together controlled around 45% of the local market. In this case, the attraction was the potential of the Colombian market, which at that time was a net importer of steel products.

In North America, Gerdau conducted a series of large-scale acquisitions, beginning with Courtice Steel (1989) and Manitoba Rolling Mills (1995) in Canada. In 1999, it acquired 75% of AmeriSteel, located in Florida, for US\$ 262 million.¹³ In December 2001, through AmeriSteel, Gerdau bought Birmingham Southeast with a view to supplying the south-eastern United States market and expanding its supply of products in North America. At the end of 2002, AmeriSteel, Co-Steel, Gerdau Courtice Steel and Gerdau MRM Steel were merged to form a new entity, Gerdau AmeriSteel, the second-largest mini-mill network in North America, with operations worth about US\$ 382 million.¹⁴ In April 2004, Gerdau upped its share in Gerdau AmeriSteel from 69% to 72%, with an outlay of US\$ 100 million. At the end of 2004, the company sought to expand its geographical coverage in the United States and Gerdau AmeriSteel bought shares in North Star Steel, which had plants in Iowa, Kentucky, Minnesota, Tennessee and Texas. These operations enabled Gerdau to continue expanding while avoiding trade restrictions on steel imports.

Lastly, Gerdau expanded across the Atlantic to enter the European Union market. In January 2006, the firm bought 40% of SIDENOR of Spain, the country's largest producer of forged, cast and special long steel. In addition,

¹³ Gerdau later increased this share to 85%, with an investment of US\$ 36 million.

¹⁴ With this operation, Gerdau also acquired 50% of Gallatin Steel. The remaining 50% remained in the hands of the Canadian company Dofasco.

SIDENOR owns 58% of Aços Villares, a long steel producer in São Paulo, Brazil. Over 90% of SIDENOR production goes to the European market. Gerdau is thus on the way to establishing an important link with large motor vehicle producers in Europe, whose relationship with SIDENOR it has inherited, and to locking into the production, administrative and industrial management know-how of one of the largest producers in the steel industry.

In short, Gerdau has pursued a gradual, cautious strategy of outward investment, which has allowed it to grow steadily by capitalizing on opportunities in the Latin American, North American and European markets. Gerdau's strategy has usually been to test markets through exports, then to invest directly, drawing on its domestic market experience to successfully restructure its newly acquired assets. Most of the companies acquired have been mini-mills—which helped to avoid the problems of shortcomings in transport infrastructure or long distances—specialized in the long steel segment. Gerdau has thus expanded its geographical scope and product range to become the largest long steel producer in the Americas.¹⁵

Gerdau's internationalization has enabled it to reduce its financial costs, thanks to enhanced corporate risk assessment. It has played an active part in consolidating the global steel industry and has managed to achieve more stable economic results thanks to the geographical diversification of its operations and access to foreign-currency income. In 2004, Gerdau's non-Brazilian operations accounted for 43% of its crude steel production, 47% of its sales and 33% of its employees. Company representatives consider that overseas sales could come to represent 50% of the total by 2010.

(b) Techint: from the global seamless tube business to the new challenge of flat and long steel

Latin America's abundant endowment of mining resources and the broad production base of its processing industries, especially in the iron and steel industry, have enabled some companies to explore specific niches for products with greater value added. After becoming the vanguard of their domestic markets, these companies have set about internationalizing their businesses, with varying degrees of intensity and geographical coverage. Among the most successful are the Argentine firm Techint, which manufactures steel tubes and focuses on the iron and steel industry, IMSA of Mexico, which produces galvanized sheets and metal structures and panels, and Madeco of Chile, a copper wire manufacturer (see box IV.4).

Techint set up in Italy at the end of the Second World War. Soon afterwards, its founders moved the company to Argentina, similarly to the story of Bunge & Born (see box III.1). Almost immediately after the move, Techint began to provide engineering and construction services to various Latin American and European countries (see chapter VI). Within a short time, the company's activities had expanded to include energy infrastructure, manufacture of steel structures and equipment and parts for heavy machinery, especially in Argentina.

Techint's engineering services formed the basis for its steel industry activities. In the 1950s, the first plants for its "star product", seamless steel tubes, were built in Mexico and Argentina (SIDERCA). At the end of the 1960s, Techint established a steel cold-rolling facility in Argentina. As of the mid-1980s, it built up its activities in the steel business, mainly in the manufacture of seamless and soldered tubes, and expanded its international calling by acquiring a new set of assets outside Argentina.

Between 1993 and 2004, Techint expanded its seamless tube production capacity almost five-fold, mainly through acquisitions and exclusively via international operations (see figure IV.1). Techint has thus established an extensive distribution network and gained proximity to its clients. In 1993, Techint took control of the Mexican company Tubos de Acero de México S.A. (TAMSA), one of whose main clients was the Mexican State-owned petroleum company PEMEX. In January 1996, Techint acquired control of Dalmine SpA, a maker of tubes, tubing and related products and supplier of services for the mechanical, motor vehicle, petrochemical, chemical, petroleum and energy industries. It serves the European market through its Italian operations, which account for about 30% of its seamless tube production capacity. In 1998, Techint bought 70% of Tavas, the only seamless tube plant in the Bolivarian Republic of Venezuela, catering mainly to the domestic petroleum industry. In 1999 Techint acquired the Brazilian soldered steel tube manufacturer CONFAB, to supply the local hydrocarbons industry. In 2000, the Techint Group purchased 51% of NKK Tubes in Japan—of which JFE owned the remaining 49%—to serve the Japanese market. Also in 2000, it bought the Algoma Tubes of Canada, specifically to serve the energy industry there. In 2004, Techint stepped up its European interests with the acquisition of Silcotub in Romania.

Although Techint has been producing flat steel since the 1960s, it has only more recently afforded more emphasis to that line of business, especially through its international operations, all located in Latin America. The starting point

¹⁵ Gerdau now has a market share of 50% in Brazil (long steel), 50% in Chile, 80% in Uruguay, 20% in Argentina and 22% in North America.

Box IV.4

MADECO: POORLY TIMED INTERNATIONAL EXPANSION?

While the growth of Techint in the steel tubes market was driven by the petroleum industry, Madeco's development was fuelled by the telecommunications sector. At the beginning of the 1980s, the Luksic group—which controlled CCU (see chapter V)—acquired a majority share in Madeco, a producer of copper and aluminium cables, tubes, sheets and profiles. Madeco went through a period of rapid growth and diversification on the back of the expansion of the construction sector, particularly the upgrading and expansion of utility networks, among others in telecoms and electric power. First, it bought a number of local firms, then launched an ambitious internationalization plan with acquisitions in Argentina, Brazil and Peru.

Madeco began its international expansion at the beginning of the 1990s, focusing on Argentina and Peru, first in making cables, and then in other activities (flexible packaging). In Argentina, it bought the cable manufacturer Indelqui and the largest copper tube maker, Decker. These were subsequently merged to form Decker-Indelqui, which began making cables, tubes and sheets. In Peru, Madeco bought Triple-C, which later merged with Indeco, the largest local cable producer, retaining the name of the latter company.

In 1997, Madeco entered Latin America's largest market, Brazil, by acquiring Ficap, the second-largest cable producer there. In 1999, it established Ficap Optel as a joint venture with Corning Inc. (a global fibre optic provider) to produce, sell and distribute fibre optic telecoms wires. Madeco thus became a major player in this segment in Brazil and Argentina. The economic downturn in Brazil and Argentina led to a slump in the demand for telephone cables, however, badly hurting the Chilean company, which recorded losses of US\$ 204 million between 1999 and 2001 (Madeco, 2004a). In these circumstances, Madeco temporarily suspended Decker-Indelqui operations in Argentina and reduced its fibre optic cable operations in Brazil to a minimum, which distanced it from Corning.

In the light of these developments, Madeco devised a plan to restructure its liabilities and enhance the profitability of its assets and interests, especially in Brazil. In 2003, Madeco concluded financial restructuring with its creditor banks and increased its capital (by US\$ 140 million) to raise additional resources to pay off debts—mainly through bond redemption and prepayment of 30% of its bank debt—and to make operational changes to its

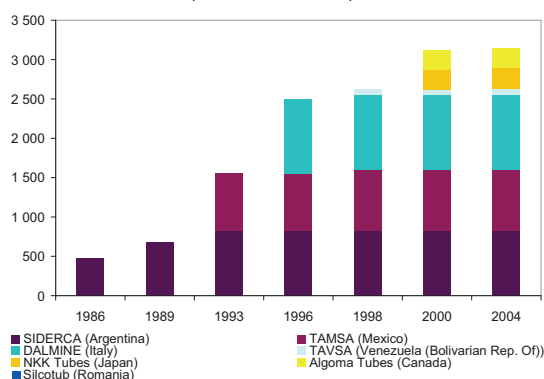
various productive units (Madeco, 2004b, p. 6). The financial restructuring gave the company manoeuvring room to take measures aimed at increasing sales and enhancing operational efficiency.

At the end of 2003 Decker-Indelqui re-started operations, after copper tube exports from Chile had performed well and Argentine demand for these products has risen. At this time Madeco was also focusing on its cables business unit and its largest operation, Ficap in Brazil, aiming to make it into an export platform for the European market (Madeco, 2005, p. 22).

In short, Madeco is a leader in virtually all the markets and segments it has entered. This position has not been achieved without difficulty, however. After a deep financial crisis caused by a worsening economic situation—particularly as regards demand for telephone cable—in Brazil and Argentina, the company undertook a broad financial and productive restructuring. At present, the market for Madeco's main operations is improving, and its substantial idle capacity, mainly in Argentina, is expected to be taken up once again. Some of its operations have focused on exports, including units producing tubes and sheets in Chile, cables in Brazil and flexible packaging in Argentina, much of whose output is sold to Brazil.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

Figure IV.1
TECHINT: SEAMLESS TUBE PRODUCTION CAPACITY
(Thousands of tons)



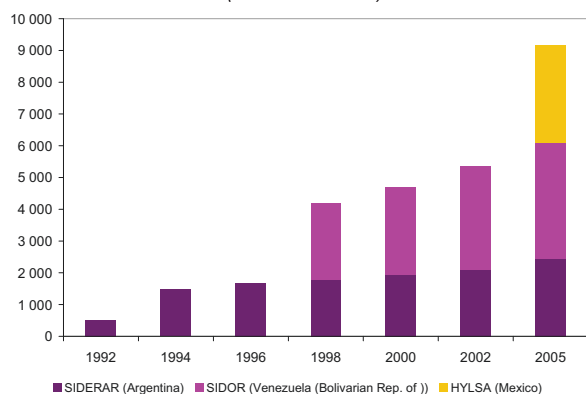
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by Techint.

for this new phase of its strategy was the purchase of a majority share in the privatization of Sociedad Mixta Siderurgia (SOMISA), Argentina's largest integrated

flat steel plant, now known as SIDERAR. Techint later led the consortium that submitted the winning bid for 60% of SIDOR, the largest steel company in the Bolivarian Republic of Venezuela. In 2005, it acquired the Mexican company Hylsamex from the Alfa Group. Hylsamex had made investments outside Mexico, one of which was in the SIDOR privatization. With these two acquisitions, Techint quickly doubled its production capacity to become Latin America's largest manufacturer of long and flat steel products (see figure IV.2).

In 2005, seeking clearer definition for its two main lines of business, Techint created Tenaris, which groups its steel tube activities, and Ternium, an umbrella for its flat and long steel operations. Tenaris is a global company, through which the Techint Group has secured an important market niche. Ternium has a more regional focus and will pose a significant challenge for the Group over the next few years in an increasingly concentrated and competitive market.

Figure IV.2
TECHINT: FLAT AND LONG STEEL PRODUCTION CAPACITY
(Thousand of tons)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by Techint.

In summary, the Techint Group has had a strong international leaning since its beginnings. It was established in Italy and moved to Argentina, from where it expanded to the rest of the world. Although it initially provided engineering and construction services, it rapidly expanded into other activities, especially those related to the steel industry. Capitalizing on growing demand from the petroleum industry, it made strategic purchases to become the provider of major petroleum companies, especially State enterprises. This strategy gave Techint very valuable experience, enabling it to grow into one of the largest seamless tube manufacturers. At the same time, it built up its steel-related interests and, through the privatization of key assets, became the largest regional producer of long and flat steel products. This outcome of all this is paradoxical, since Techint has become a major global player in a sophisticated product (seamless steel tubes), but its greatest challenges lie at the regional level in a lower-value-added segment (long and flat steel).

(c) IMSA: expanding internationally to increase value added

IMSA, a contemporary of Techint, became one of Mexico's largest steel manufacturers, operating mainly in the galvanized steel segment.¹⁶ In the 1990s, the company adopted a strategy of moving into segments with greater value added and high-productivity processes, and has focused more on this strategy as difficulties in obtaining raw materials—basically steel and aluminium—for its business have mounted. In this regard, it has been essential

to expand internationally in order to find new market niches. At first, IMSA focused its strategy on the United States, through relatively small operations in different segments, including vehicle batteries, pre-fabricated buildings, panels and so forth.

In the 1990s, IMSA also looked for opportunities in Latin America. In 1994, it bought a share in IPAC S.A., a Chilean galvanized products company. In 1997, it acquired Industria Galvanizadora de Guatemala (INGASA), which owned plants in Costa Rica, Guatemala and Honduras, thereby increasing its Central American interests and its exports to North and South America. IMSA Acero and CSN also established a joint venture to set up a finished product plant in Brazil, which was abandoned in 1999.

In the current decade, IMSA has refocused on North America. In 2000, it acquired Steelscape, Inc., a manufacturer of galvanized, coated and painted steel products for the construction market in Canada and the United States. It also owns plants in Alabama, California, Louisiana and Washington, supplying the galvanized steel market. In 2004, through Steelscape, IMSA acquired the galvanized steel producer Polymer Cpetroleum Coaters of Fairfield in Alabama, through which it became the main provider for this segment in the United States.

IMSA also built up the panel business it had begun a few years earlier in the United States and Chile. In 2005, through Metl-Span, the company opened a new steel panel plant in Nevada, increasing its total production capacity by 30%. With plants in Nevada, Texas and Virginia, the group currently has access to most of the United States market. Taking into account its Mexican and Chilean operations, IMSA is the leading player in this market in the Americas. In 2002, with a view to producing fiberglass-reinforced plastic panels, IMSA bought Lightfield (now Stabilit Europa), the second-largest manufacturer in Europe, and became the largest manufacturer in the European Union.

In summary, in a consolidating market—with the heart of the action in Europe—and with abundant mineral reserves, Latin American firms such as Gerdau have taken advantage of the opportunity to expand. Gerdau has created a substantial network of mini-steel mills that bring it close to the main consumer centres, especially in the North American and South American markets, and it has thus become a supplier of inputs for a large number of industries throughout the Americas. Some companies, including Techint, IMSA and MADECO, have entered segments offering greater value added, with varying degrees of success.

¹⁶ Hot immersion galvanization is the application of a zinc protection layer to prevent corrosion. Galvanization consists of submerging the steel in a vat of zinc smelted at 450 degrees centigrade. Iron and zinc have a strong affinity at this temperature, allowing the alloy to form with pure zinc predominating on the surface.

C. Cement: the building material of the first global trans-Latin

In the vast majority of the countries, the cement industry has developed under the wing of the State and in step with industrialization processes. Nevertheless, it has also been strongly linked to the performance of domestic economies. The low value added of this commodity means that its market is regional. By nature, cement cannot be transported over long distances at competitive prices. The high cost of transport in relation to the product's value means that exports are not an economically viable option, and internationalization therefore depends on outward foreign direct investments.

In the last few decades, the cement industry has undergone an intense process of concentration and consolidation, with a large number of mergers and acquisitions in the global market. In the 1970s, having strengthened their position in their domestic markets and encouraged by broader access to financing, some of the main European producers began to expand geographically—mainly into North America—in order to offset the risks associated with local-market business cycles. This

international expansion continued in the second half of the 1980s, focusing now on Latin America. In the 1990s, the spotlight was again on the United States, later moving to Central and Eastern Europe. Lastly, some of the industry's largest companies acquired true global status by seizing upon the opportunities that arose from the Asian crisis in 1997.

In this decade, the world's largest cement company is Lafarge, after many acquisitions on all five continents, including the British company Blue Circle. The cement industry is now controlled by a small number of large global operators, mostly of European origin, led by Lafarge of France, then Holcim of Switzerland. One Latin American company—Cementos Mexicanos (CEMEX) of Mexico—has powered its way into this select group to challenge the hegemony of the European corporations (see table IV.5). This is no isolated case, however. Other Latin American companies have recently embarked on international expansion strategies, including Votorantim Cimentos (VC) and Carmargo Corrêa of Brazil and Argos of Colombia.

Table IV.5
WORLD'S LARGEST CEMENT-MAKING COMPANIES, BY OUTPUT AND SALES, 2004^a
(In millions of tons and billions of dollars)

	Company	Country of origin	Output	Sales	Regions in which the company has foreign operations ^b				
					NA	LA	EU	AS	OT
1	Lafarge	France	151	19 633	x	x	x	x	x
2	Holcim	Switzerland	150	11 695	x	x	x	x	x
3	CEMEX ^c	Mexico	98	8 149	x	x	x	x	x
4	Heidelberg Cement	Germany	80	8 689	x		x	x	x
5	Italcementi	Italy	61	6 158	x		x	x	x

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the companies.

^a The shaded lines correspond to Latin American companies.

^b NA: North America (United States and Canada), LA: Latin America and the Caribbean, EU: Western and Eastern Europe, AS: Asia, OT: Others.

^c Data prior to incorporation of the assets of RCM of the United Kingdom.

1. CEMEX: the only Latin American TNC

In the 1970s, CEMEX significantly increased its local-market share in Mexico on the back of economic growth fuelled by policies of import substitution industrialization. It grew from a local company in north-east Mexico into a national enterprise. At this time the firm extensively modernized its production processes, increased its vertical integration (by stepping up activities in the pre-mixed concrete market) and began to export to the United States to supply the rapidly growing markets in the States of Arizona, California and Texas.

The crisis of the 1980s, combined with early steps towards more open and deregulated local markets and the growing interest of leading European companies in acquiring interests in the Americas, forced CEMEX to take an active stance in relation to the incipient changes on the international stage. Between 1987 and 1989, it acquired two of its main Mexican market competitors (Cementos Anáhuac and Empresas Tolteca), which strengthened its export profile and expanded its production capacity in the concrete segment, in addition to weakening the presence of foreign groups in Mexico.¹⁷ CEMEX established an extensive distribution network and purchased some of its client firms (concrete plants) in the south of the United States (Arizona, California, Florida, Kentucky, Minnesota, New Mexico and Texas).

The company's main competitors in the United States reacted strongly to this strategy and filed an antidumping complaint against cement imports from Mexico. After the imposition of countervailing duties,¹⁸ CEMEX exports to the United States contracted sharply. With the danger of an export strategy focused on a single market so patently revealed, the company's management sought to diversify its export markets and to consolidate in the United States as an autonomous business, independent of Mexican cement imports. This was the point at which CEMEX began to actively and resolutely internationalize its production activities, seeking opportunities in emerging or potentially high-growth markets.

Interestingly enough, the opportunity did not arise in the United States but in Europe. In 1992, CEMEX

acquired Spain's two largest cement companies, Compañía Valenciana de Cementos Portland and La Auxiliar de la Construcción S.A. (LACSA), for some US\$ 1.84 billion.¹⁹ Within a short time, CEMEX had restructured its new assets, increased productivity, and become the world's fourth largest cement company.

Nevertheless, instead of deepening its expansion strategy in developed countries, CEMEX turned towards other emerging economies, first in Latin America and the Caribbean, then in Asia (see figure IV.3). In 1994, CEMEX acquired Corporación Venezolana de Cementos (Vencemos) for US\$ 320 million, and the Panamanian State enterprise Cemento Bayano. The crisis of December 1994 and the severe contraction of Mexico's domestic market further convinced the CEMEX management of its international expansion strategy and the merits of expanding it further (Barragán and Cerutti, 2003, p. 22). Indeed, the profits of its Spanish enterprises were essential to keep the company afloat. In 1995 and 1999, CEMEX acquired new assets in Chile, Colombia, Costa Rica and the Dominican Republic.²⁰ As it had done in Spain, CEMEX invested in modernizing production and management in its new Latin American affiliates, achieving a dominant position in most of the respective domestic markets.

Meanwhile, CEMEX began to explore markets further afield, first through exports then by purchasing a number of assets (see table IV.6 and figure IV.3). In 1997, the company acquired 30% of Rizal Cement Company in the Philippines. The Asian crisis provided the opportunity for expansion in that region. Over the next two years, CEMEX purchased Indonesia's largest cement company, PT Semen Gresik, another 40% of Rizal Cement Co. and 100% of APO Cement Corporation in the Philippines, for which it paid out over US\$ 640 million. In 2001, CEMEX entered the Thai market with the acquisition of 99% of Saraburi Cement Company. In 1999 it paid US\$ 417 million for Assiut Cement, the largest cement producer in Egypt, thus extending into North Africa.

¹⁷ At the beginning of the 1990s, CEMEX launched a US\$ 1 billion investment plan to extend and upgrade production capacity in Mexico, and secured a market share of 68%. CEMEX thus became Mexico's strongest global company (Barragán and Cerutti, 2003, p.15).

¹⁸ CEMEX lost the anti-dumping suit and had to pay a 52% tax on products exported to the United States.

¹⁹ Most of the financing for this operation came from a syndicated bridging loan of US\$ 1.143 billion, which was paid off in mid-1993 with a US\$ 1 billion issue of Eurobonds.

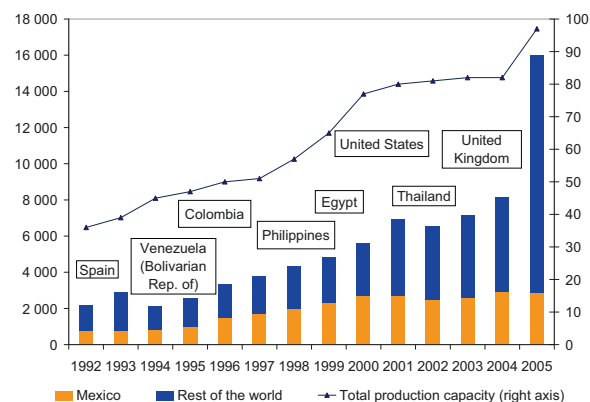
²⁰ In 1995, CEMEX bought Cementos Nacionales in the Dominican Republic for US\$ 111 million followed, a year later, by Cementos Diamante and Cementos Samper of Colombia, for US\$ 700 million. In 1999, CEMEX acquired 95% of Cementos del Pacifico, the leading producer in Costa Rica, and 12% of Cementos Bío Bío in Chile. In 2002, it bought the Puerto Rican Cement Company for US\$ 176 million.

Table IV.6
CEMEX: GEOGRAPHICAL AND PRODUCTION DIVERSIFICATION, 1998-2004
 (Millions of tons per year and number of plants)

	Production capacity			Cement plants		Concrete plants	
	1998	2000	2004	1998	2004	1998	2004
Mexico	28.5	27.2	27.2	21	18	214	211
United States	1.1	12.6	14.3	1	17	48	97
Spain	10.4	10.4	11.0	8	8	73	77
Venezuela (Bolivarian Republic of)	4.3	4.3	4.6	3	3	42	35
Colombia	5.1	4.8	4.8	6	5	28	22
Central America and the Caribbean	1.3	1.1	4.0	5	11	5	36
Philippines	2.8	5.8	5.8	2	3	-	0
Indonesia	3.2	5.0	4.4	-	4	-	9
Thailand	-	-	0.7	-	1	-	0
Egypt	-	4.0	4.9	-	1	-	3
Total	56.7	77.2	81.7	50	71	410	490

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by CEMEX.

Figure IV.3
**CEMEX: INTERNATIONALIZATION OF OPERATIONS,
 MAIN ACQUISITIONS, SALES IN MEXICO AND
 THE REST OF THE WORLD, AND TOTAL
 PRODUCTION CAPACITY, 1992-2005**
 (Millions of dollars and millions of tons per year (right axis))



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by CEMEX.

CEMEX has thus become established as an international corporation with well diversified revenue sources. The combination of investments in potentially high-growth, but higher-risk emerging economies and ventures in more stable industrialized countries providing revenues in hard currency gave CEMEX the flexibility it needed to continue expanding. However, the high level of volatility in the developing countries in the late 1990s led the company to seek new options to strengthen its activities in developed economies.

Accordingly, at the beginning of the present decade CEMEX shifted its growth strategy again, focusing now on developed countries. In 2000, it acquired Southdown Inc.,

the second-largest cement company in the United States, for some US\$ 2.8 billion. With this transaction, CEMEX became the largest cement producer in North America and the third-largest in the world. The Southdown acquisition reduced the vulnerability of CEMEX in emerging markets and provided it with a significant income in dollars, in which the bulk of its debt is also denominated. In 2004, CEMEX paid some US\$ 5.8 billion for RMC Group of the United Kingdom, the world's largest supplier of construction materials and associated services, in the largest purchase ever made by a Mexican firm (ECLAC, 2005c, p. 44). CEMEX thus strengthened its presence in the United States and Europe, entering new markets such as the United Kingdom, France and Eastern Europe and shortening the lead of the two largest cement producers at the global level (see table IV.6). The company's sales in developed countries increased from 41% of its total sales in 2003 to 68% in 2005 and it became the largest trans-Latin among TNCs from developing countries (see table III.1).

In addition to increasing its geographical coverage and reducing exchange-rate risk, with this latest purchase CEMEX has showed a clear inclination towards greater diversification within the cement business, by becoming the largest maker of concrete in the world (*Expansión*, 27 October-10 November 2004, p. 55). This being so, the company was able to open a secure and efficient distribution channel to sell cement in developed countries, where it is sold mainly in the form of pre-mixed concrete. The acquisition of RMC brought CEMEX know-how in the area of ready-mixed cement, which was important in view of the large infrastructure and construction projects starting up in Mexico and the fact that the

firm's international competitors were increasing their presence there. Lafarge is building a new plant in the State of Hidalgo and Holcim is rapidly increasing its Mexican sales.²¹

With the strengthening of its operations in Europe and the United States, the next stage in the expansion of CEMEX will most probably be to enter two of the most dynamic emerging markets in the world economy, China and India.

2. Votorantim Cimentos and Camargo Corrêa Cimentos: new trans-Latins in the cement industry

While CEMEX was consolidating its global interests, Votorantim Cimentos (VC) and Camargo Corrêa Cimentos, cement producers in two of Brazil's largest industrial conglomerates, were beginning to expand internationally. Both companies are just starting out along this road, however, each in a very different manner.

VC was created in 1997 and, since it was an umbrella for all the enterprises in the conglomerate making cement, concrete and related products, it moved into the lead, controlling close to 40% of the domestic market. Thus strongly positioned in Brazil, and in view of contracting domestic demand, VC began to seek opportunities abroad. Internationalization was seen as a way to enhance access to external financing and escape from "Brazil cost", while diversifying income and protecting its domestic market position against the possible entry of one of the industry's major global leaders. In addition, the efforts that VC had made to enhance its production processes had left it better placed to undertake an international expansion, by bringing its operations to world class level. In short, VC had learned much from the experience of CEMEX.

The VC production system was the firm's main competitive advantage. It therefore began to seek assets with which it could replicate its success in Brazil, by adding value to improve the operational performance of the acquired company. VC did not intend to internationalize its business too rapidly, however, and began to seek new markets cautiously. In view of the volatility seen in many emerging markets, the firm opted to focus its international expansion strategy on North America.

The opportunity that VC had been seeking arose as a result of negotiations between the competition authorities of the United States and Canada with the French firm Lafarge.²² In August 2001, VC acquired Saint Mary's Cement in the Great Lakes region on the United States-Canada border, for some US\$ 720 million. With

this foothold in the United States, VC continued to seek new opportunities. In early 2003, Suwannee American Cement, located in Florida, was looking for a large cement industry operator to manage its activities. This was a very attractive opportunity for VC, which purchased 50% of the company for US\$ 104 million. Thereafter, VC set about vertically integrating its United States assets in order to supply products with higher value added.

- In 2004, VC acquired the concrete company S&W Materials in Florida, with the intention of setting up new plants and improving its distribution system. By 2006, it controlled 25% of the Florida market, by building on synergies with the Suwannee cement factory. In 2005, VC formed a partnership between Anderson Materials and S&W Materials with a view to consolidating a production cluster in the south of the United States.
- In September 2003, through Saint Mary's, VC acquired the assets of Badger Cement Products in the Great Lakes region, thus increasing its presence in Wisconsin and in northern Illinois. In February 2005, it purchased two cement factories and a number of CEMEX distribution terminals in the Great Lakes region in the United States, for US\$ 389 million.²³ With this operation, VC strengthened its United States interests and created an integrated operation in the Great Lakes region, gaining a lead position with a market share of close to 30%.

With these new investments VC consolidated a regional pattern of internationalization, centered on North America, and entered the select group of the world's ten largest cement producers. Between 2001 and 2004, Votorantim Cimentos invested about US\$ 1 billion in the United States and Canada, building its international operations from nil to 24% of the company's total sales. In 2007, its outward investments are expected to amount to US\$ 1.8 billion,

²¹ CEMEX now controls 51% of the Mexican market, followed by Holcim with 23%, Cruz Azul with 15% and Lafarge with 5% (*Business Latin America*, 25 July 2005).

²² In 1997, Saint Mary's Cement had been acquired by the British company Blue Circle, which was subsequently purchased by Lafarge. The Canadian and United States Governments ruled that if Lafarge were to take control of Blue Circle, it would have to divest some assets, including Saint Mary's.

²³ This sale was part of a CEMEX restructuring plan aimed at lowering its indebtedness by almost US\$ 6 billion.

through which VC intends to triple its sales in North America (*Gazeta Mercantil*, 2005), which would mean that close to 50% of the company's total sales would be generated by its subsidiaries abroad.

VC will probably continue to focus its international expansion strategy on North America, either by either expanding the current production structure or by acquiring new assets in order to lock into the market expansion driven by economic stability. VC does not discount the possibility of further geographical diversification, however. Latin America could be an option, since expansion into Europe or emerging economies such as China or India appears less probable. There are fewer opportunities for VC in the territories of the industry's largest companies, but establishing a European platform would give it a more substantial international presence, with significant potential for local synergies. Moreover, expansion in Asia—despite the high growth prospects—would also pose significant cultural challenges for VC.

At the end of 2004, Votorantim considered the possibility of buying the company Loma Negra in Argentina, in order to strengthen a possible regional

strategy for the Americas. However, a Brazilian competitor, Camargo Corrêa Cimentos, finally acquired Loma Negra.

The cement division of the Camargo Corrêa group is the fifth largest producer in the Brazilian market. In April 2005, Camargo Corrêa bought Loma Negra for US\$ 1.025 billion, in what was the largest investment in the group's 65-year history. In addition to the market in Argentina and other Southern Cone countries, one of the big advantages Loma Negra brought was rapid access to ports through the rail network. In contrast to the situation in Brazil, the management of Camargo Corrêa considered that cement could feasibly be exported to African markets such as Angola, Mozambique, and Nigeria.

The cement industry in Latin America is still being consolidated. There is apparently still manoeuvring room for the leading companies, CEMEX and Holcim, to make fresh moves and for the emergence of new players, some of them potential trans-Latins. In this regard, Camargo Corrêa's recent purchase of Lomas Negras and acquisitions by Argos of Colombia are prominent developments (see box IV.5).

Box IV.5

ARGOS: CEMENT KING OF THE CARIBBEAN

With 48% of the market, Argos is the cement industry leader in Colombia and the fifth-largest cement producer in Latin America. At the end of the 1990s, Argos began internationalizing with investments in the Bolivarian Republic of Venezuela, Dominican Republic, Haiti, Panama and the United States, in addition to exports to 18 countries.

In 1998, through Cementos del Caribe, Argos acquired Corporación Cemento Andino in the Bolivarian Republic of Venezuela and entered into partnerships to invest in Cementos Colón in the Dominican Republic, Cimenterie

Nationale d'Haiti and Corporación Incem in Panama. Thus, Argos established a strong geographical presence in the Caribbean, from which it could supply virtually all the subregion's markets.

Faced with mounting competition in its home market, where CEMEX and Holcim were operating, Argos began to deepen its internationalization process. In mid-2005, Argos acquired two concrete companies in the United States for US\$ 258 million, which was the largest investment ever made by a Colombian firm there. This acquisition brought the Colombian

cement group's total outward investment to almost US\$ 500 million. The larger of the two new acquisitions, Southern Star Concrete (Dallas, Texas) was bought for US\$ 245 million and produces 4 million cubic metres of concrete in 46 plants, which is more than the annual total of the entire Colombian industry. The other new company, Concrete Express (Conex), is smaller and headquartered in Savannah, Georgia. With these operations, Argos has moved closer to its main clients, which it used to supply through exports, and is climbing up the industry's value chain.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

The natural disasters which have recently hit the United States, including Hurricanes Katrina, Rita and Wilma, could create enormous business opportunities for the reconstruction of devastated cities. Indeed, an estimated five million tons of cement and three million cubic metres of concrete will be needed over the next five years. Latin American companies with plants in the south of the United States, such as CEMEX, Votorantim and Argos, stand to benefit from such opportunities.

In short, CEMEX pursued a pattern of internationalization very similar to that of most successful TNCs. First, it consolidated its position in the domestic market, which allowed it to gain size and power to negotiate with the

international capital markets. Second, it built up know-how in other markets through exports. Lastly, it began to expand into other countries. Between 1985 and 2005, CEMEX expanded its cement production capacity from 10 million to almost 100 million tons per year, with growth particularly strong in the last decade. After investing over US\$ 11.3 billion in acquisitions, CEMEX has deepened its geographical and product diversification to become the largest private company in Latin America, apart from petroleum companies. In this process, CEMEX was able to add value to the companies it acquired and thus increase the group's overall profitability. Its ability to take the best of the management tools of the companies it bought and

absorb them into its own best practices is perhaps the key to the Mexican company's successful expansion. At present, CEMEX has over 50,000 employees around the world (39% in North America) and sales of US\$ 16 billion, of which 37% are in Europe (mainly in Spain and the United Kingdom), followed by the United States (26%), Mexico (22%) and Central and South America (9%). Together with Lafarge of France and Holcim of Switzerland, CEMEX is part of a triumvirate that dominates the world cement market.

CEMEX is not the only Latin American example of successful expansion, however, and its experience has served as inspiration for other companies. The dependence

of the cement industry's performance on business cycles, as traumatically experienced by CEMEX, prompted other firms to undertake selective internationalization strategies in order to reduce their vulnerability and hedge the risks associated with their domestic market operations. This is the case of Votorantim and Argos, which focused their internationalization strategies on North America. While CEMEX was growing internationally and adding value to the companies it acquired, Votorantim concentrated on improving its production processes to bring its operations up to world-class level, then seized opportunities as they arose.

D. Forestry, pulp and paper: internationalizing a natural comparative advantage

At the end of the nineteenth century, new techniques for producing pulp from wood made it possible to manufacture paper on a large scale at low cost, thus leading to its use on a massive scale. Changes in consumer habits in the 1950s brought explosive growth in demand for paper products. Pulp thus became one of the most common commodities for everyday products used by people across the world.

The main producers of pulp today are the United States, Canada, China, Finland, Japan and Sweden, which are home to the industry's largest integrated companies (dealing with timber, pulp, paper, panels, etc.), led by three United States firms (see table IV.7). The forestry and paper industry remains fairly fragmented, however, since the leading 100 companies account for only 25% of global production (PriceWaterHouseCooper, 2005). As in other industries that process natural resources, the forestry, pulp and paper products industry is capital intensive and uses advanced technology, which makes the cost of raw materials—mainly timber—fundamental. Over the last few years, several developing countries (Brazil, Chile, Indonesia, South Africa and others) with natural advantages have considerably increased their share in world production and trade. In this group of countries, public policies were crucial to the development and growth of the industry. In Latin America, Brazil and Chile have secured a place among the world's leading producers (in seventh and tenth position, respectively) and exporters (ranking third and fifth, respectively).

Chile's forestry sector has major natural competitive advantages (climate, soil, geographical location of the forests and proximity to transport infrastructure). In the 1970s, the Government promoted the activity by

offering large tax benefits to companies in the sector. Accordingly, the leading companies devised ambitious investment plans to increase their forestry base and to expand, modernize and diversify their productive capacity—mainly for exports—and to move into products of greater value added, such as pulp, paper, sawn timber and panels. Two companies in this sector, Celulosa Arauco y Constitución (Arauco) and Compañía Manufacturera de Papeles y Cartones (CMPC), became significant global players (see table IV.7).

To complement their growth in the domestic market, CMPC and Arauco embarked on extensive plans to internationalize their business, initially through exports, then through direct investment, buying local companies or building their own facilities in neighbouring countries with natural environments similar to Chile's. The Brazilian firms remained at the first stage of this process, since they did not continue internationalizing beyond their export concerns. International expansion was seen as a way to expand and diversify product ranges, in order to lessen vulnerability to commodity business cycles (Feller-Rate, 2004, p. 3; BCI, 2004, p. 5). Another factor driving this expansion was the growing shortage of land for new plantations and stricter requirements in Chile regarding environmental matters and indigenous communities. At the beginning of the 1990s, Chilean enterprises began to expand their forestry assets abroad, mainly in Argentina (Misiones and Corrientes provinces) and, to a lesser extent, in Uruguay and Brazil.

With these first investments in plantations and forested areas, the Chilean firms moved into new productive concerns with quite distinct profiles. While Arauco concentrated on producing pulp, processing timber and manufacturing

Table IV.7
WORLD'S LARGEST WOOD, PULP AND PAPER COMPANIES, BY SALES, 2004^a
(Millions of dollars)

	Company	Country of origin	Sales	Regions in which the company has foreign operations ^b				
				NA	LA	EU	AS	OT
1	International Paper	United States	25 548	x	x	x	x	
2	Weyerhaeuser Co.	United States	20 170	x	x	x	x	x
3	Georgia-Pacific Corp.	United States	19 656	x		x		
4	Stora Enso	Finland	15 417	x	x	x	x	x
5	Kimberly-Clark	United States	15 083	x	x	x	x	x
6	Svenska Cellulosa	Sweden	12 245	x	x	x	x	x
7	UPM-Kymmene Corporation	Finland	12 213	x		x	x	
8	Nippon Unipac	Japan	11 030	x			x	x
9	Oji Paper Co.	Japan	10 917	x	x		x	
10	Metsälitto	Finland	10 639	x		x		
42	Celulosa Arauco y Constitución	Chile	2 075		x			
46	Compañía Manufacturera de Papeles y Cartones	Chile	1 933		x			
52	Kimberly-Clark México	Mexico	1 754					
64	Aracruz Celulose	Brazil	1 167					
69	Votorantim Celulosa e Papel	Brazil	1 010					
71	Klabin	Brazil	1 001		x			
76	Suzano Papel e Celulose	Brazil	902					
83	Grupo Industrial Durango	Mexico	725					

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of PriceWaterHouseCooper, *Global Forest and Paper Industry Survey, 2005 Edition*, 2005 and information provided by the companies.

^a The shaded lines correspond to Latin American companies.

^b NA: North America (United States and Canada), LA: Latin America and the Caribbean, EU: Western and Eastern Europe, AS: Asia, OT: Others.

panels, CMPC focused on making paper products. In addition, a new player—Masisa—emerged to carve out a niche in products with greater value added.

In 1996, Arauco bought the plantations and production facilities of Alto Paraná in the province of Misiones, Argentina, which made it the main producer and only exporter of pulp in that country. It also bought two sawmills and two wood processing plants in Argentina, which helped it to become established as the third-largest pulp enterprise in the world and the main producer of sawn wood in Latin America and in the southern hemisphere (Arauco, 2004). In January 2004, Arauco acquired the forestry assets of Pérez Companc, which were also located in Misiones province.

By contrast, although CMPC continued to expand its plantations—in order to build up enough forestry assets to set up a pulp plant (though not before 2007)—its international expansion strategy was based on paper manufacturing, first tissue-paper products (tissue paper, napkins, paper towels, facial tissues and disposable handkerchiefs), then disposable diapers, to supply the markets in Argentina, Uruguay and Peru, and possibly to export. With a view to this, CMPC acquired a number

of existing plants and built new ones. Today, CMPC leads the tissue-paper markets in Chile, Argentina and Uruguay, and ranks second in Peru. In January 2006, CMPC acquired a tissue-paper factory in Mexico, from where it plans to expand into the United States, Central America and the Caribbean.

Starting from a much smaller base, another Chilean company began to expand in the forestry business, mainly in the timber boards segment, until it acquired considerable dimensions at the regional level (Calderón, 2005). In 1994, Masisa opened the first particleboard plant in Argentina and, a year later, another plant to manufacture medium density fiberboard (MDF) there. Encouraged by good results in Chile and Argentina, the company then entered the more demanding markets of Brazil and Mexico. At the end of 2000, Masisa opened the Ponta Grossa industrial complex in Brazil, with an MDF plant and Latin America's largest and most modern oriented strand board (OSB). Masisa invested US\$ 118 million in this project (Feller-Rate, 2004a, p. 2). In 2002, it acquired a particleboard plant in Durango, Mexico and soon afterwards took over full management of the operations of Fibranova C.A., a subsidiary of Terranova, S.A. in the Bolivarian Republic

of Venezuela. The firm also expanded and diversified its operations in Argentina. Masisa thus significantly increased its production capacity to become one of the lowest-cost producers in the world and the leading board producer in Latin America, making it highly competitive in little-differentiated products (Feller-Rate, 2004a, p. 8).

The positive outlook for this segment led to the emergence of competitors. Arauco entered the panel fabrication business, seeking to take advantage of a growing supply of timber from its own plantations, manufacture more products with higher value added and complement its main activity of pulp-manufacturing (COPEC, 2002). In 1997, it began producing in Chile and subsequently acquired the facilities of Trupán S.A. and Maderas Prensadas Cholguán S.A., thus expanding the production of plywood, MDF and hardboard. In 2001, Arauco built an MDF plant in Misiones, Argentina, adjacent to the sawmill it owned there. In March 2005, it entered Brazil and built up its interests in Argentina by acquiring the assets of the French company Louis Dreyfus in both countries for some US\$ 300 million. With an annual production capacity of over one million cubic metres of panels, Arauco has grown into one of largest panel manufacturers and the largest plywood producer in Latin America, as well as Masisa's main competitor in Chile and Argentina (Arauco, 2004).

Over the years, Masisa has worked to complement its manufacturing business by strengthening distribution channels, as the main pillar of its commercial policy (Terranova, 2004, p. 29). It has developed an extensive distribution network for its products in all the countries where it owns operations and in another where it has trade offices. In 1992, Masisa opened the first of its specialized

stores, known as Placacentros, in Chile. By the end of 2004, it had 215 Placacentros stores in 12 Latin American countries, mainly in Chile, Mexico and Brazil, and expected to have 290 such stores by 2005 (Masisa, 2005, p. 20).

Masisa's rapid growth aroused the interest of the Swiss entrepreneur Stephan Schmidheiny. Through Forestal Terranova, he acquired Masisa's controlling group, Pathfinder. In April 2005, Masisa was merged with Terranova to form one of the region's largest forestry groups, with 368,000 hectares of forest in Argentina, the Bolivarian Republic of Venezuela, Brazil and Chile and an annual production capacity of 531,000 cubic metres of sawn timber and 2.3 million cubic metres of panels. The merger was intended to consolidate a position in markets where the companies were already operating, with Terranova's position in the United States benefiting Masisa products, and Terranova's products locking to Masisa's lead position in Latin America, sales volume and product distribution logistics. Masisa thus replicated the experience of other Chilean companies which consolidated abroad but could not then stand up to the heavyweights and were ultimately absorbed by a global operator with larger financial capacity (Calderón, 2005).

In summary, the Chilean forestry companies have been expanding their assets abroad, particularly in Argentina and, more recently, Brazil. With the supply of inputs thus secured, they began manufacturing in different subsectors, thereby averting the rivalry that occurred in the Chilean market, especially in pulp production, between Arauco and CMPC. Arauco deepened its specialization in pulp and sawn timber, to contend with Masisa for the lead position in the panel business, whereas CMPC internationalized its business based on the manufacture of paper products.

E. Conclusions

The earliest and largest Latin American companies to engage in substantial outward FDI include trans-Latin commodity firms, in other words, companies supplying basic inputs for industry. These firms' activities range from extraction (hydrocarbons and mining) to operations involving different degrees of processing (steel, cement, pulp and paper). They have also exhibited the greatest geographical expansion, either because of the location of the natural resources or because the trans-Latins' global competitiveness in these sectors has enabled them to invest in getting their products into major markets.

Generally speaking, the State has played a key role—either directly or through public policies—in the development and subsequent international expansion of many of the large hydrocarbons, mining, cement, steel and pulp companies. The largest of the internationalized mining and drilling companies are either State-owned or recently privatized. In other cases, such companies have grown up in sheltered environments or have benefited from incentives as part of State policy for promoting certain key activities. Those private firms among the group (usually originally family-owned) often expanded by acquiring former State assets.

Recently, the industries in which these companies operate have been undergoing intensive consolidation. Rather than a matter of opportunity, therefore, internationalization has been necessary for survival. This is because access to markets and, especially, to raw material reserves are vital assets for competitiveness. In most cases, international expansion has taken place in the Americas, with neighbouring countries and

the United States the priority destinations for direct investments. Such activities have also produced what is perhaps the only Latin American TNC —CEMEX of Mexico. The future of this group of trans-Latins hinges to a large extent on their ability to achieve a good competitive and dynamic position in their largest markets, while becoming more sophisticated and adding value to their products.

Chapter V

Trans-latins in the food and beverages industry

A. Introduction

The world food and beverages industry has undergone significant change during the last decade, driven by shifts in consumption patterns, technological advances and increased competition. The leading transnational corporations (TNCs) in this industry have responded by following strategies based on the extension and improvement of their product line-ups and the diversification of their geographical markets, often by acquiring assets from competitors. These companies have built competitive advantages based on strong and internationally recognized brands, scale economies, research and development capacity and efficient global distribution systems. The achievement of scale economies in production, marketing, management and, above all, distribution has been crucial to the competitiveness of food and beverage companies and this, in turn, has determined their ability to dominate this industry.

Some of the region's most prominent Latin American transnational corporations, or "trans-Latins", have emerged in the food and beverages industry and their experiences form the subject of this chapter. Such trans-Latins are finding it increasingly necessary to link up with major TNCs as part of their internationalization process; several of them, however, especially in the beverages industry,

have found themselves subsumed into the global systems of TNCs in the process, usually by way of acquisitions. After a brief introduction to the major TNCs in both industries, this chapter will examine the experiences of trans-Latins, first in the beverages industry, which has undergone major changes in the last few years, then in the food industry.

Tables V.1 and V.2 provide an overview of the largest global TNCs by sales in the food and beverages industries. These tables must be interpreted with caution, since the division between the two industries is increasingly blurred. On the one hand, one of the two principal soft drinks producers, PepsiCo, has diversified into the food industry, which explains why it figures as a major player in both industry lists. On the other hand, several of the dominant food companies, too, have increasingly diversified their product mix and have entered or expanded into the beverages market, taking advantage of the consumer patterns noted earlier. For example, in 2004 Danone's beverage sales reached US\$ 4.7 billion, which was equivalent to

25% of its total sales (Danone, 2005). Likewise, Nestlé's bottled water sales amounted to US\$ 1.9 billion in 2004, accounting for approximately 10% of its total sales that year; while sales of other beverages, including soluble drinks, accounted for another 15%. Thus, it is difficult to establish a clear-cut definition of the market leaders in each separate industry.

Trans-Latins have played an important role in the transformation of these industries in Latin America and the Caribbean. This chapter analyses the way the trans-Latins have developed in those two industries, their internationalization and their interaction with world-leading TNCs.

Table V.1
LARGEST FOOD COMPANIES, BY SALES, 2004
(Billions of dollars)

	Company	Country of origin	Main activity	Sales	Regions in which the company has foreign operations ^a				
					NA	LAC	EU	AS	OT
1	Nestlé S.A.	Switzerland	Diversified	69.826	X	X	X	X	X
2	Unilever Plc	United Kingdom	Diversified	49.961	X	X	X	X	X
3	Archer Daniels Midland Co. (ADM)	United States	Agricultural products	36.151	X	X	X	X	
4	Kraft Foods Inc.	United States	Food products and soft drinks	32.168	X	X	X	X	X
5	PepsiCo	United States	Snacks and soft drinks	29.261	X	X	X	X	X
6	Tyson Foods Inc.	United States	Processed meats	26.441	X	X ^b		X	
7	Bunge	United States	Agricultural products	25.168	X	X	X	X	
8	Sara Lee Corporation	United States	Processed meats and bakery products	19.566	X		X		
9	ConAgra Foods	United States	Diversified	18.179	X				
10	Groupe Danone	France	Milk products	17.040	X	X	X	X	X

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of *Fortune*, "The 2005 Global 500" [online], 25 July 2005 <<http://www.fortune.com/fortune/global500>> and *Food Engineering*, "Top 100 food and beverage companies", October 2004.

^a NA: North America (United States and Canada), LAC: Latin America and the Caribbean, EU: Europe, AS: Asia, OT: Others.

^b Operates solely in Mexico.

Table V.2
LARGEST BEVERAGE COMPANIES, BY SALES, 2004
(Billions of dollars)

	Company	Country of origin	Main activity	Sales	Regions in which the company has foreign operations ^a				
					NA	LAC	EU	AS	OT
1	PepsiCo	United States	Carbonated soft drinks	29.261	X	X	X	X	X
2	The Coca-Cola Company	United States	Carbonated soft drinks	21.962	X	X	X	X	X
3	Coca-Cola Enterprises Inc.	United States	Soft drink bottler (Coke)	18.158	X		X		
4	Diageo Plc	United Kingdom	Spirits/alcoholic beverages	16.163 ^a	X	X	X	X	X
5	InBev	Belgium	Beer	16.209	X	X	X	X	
6	Anheuser-Busch Inc.	United States	Beer	14.934	X	X	X	X	
7	Asahi Breweries Ltd.	Japan	Beer	14.007	X		X	X	
8	Heineken N.V.	Netherlands	Beer	13.647		X	X	X	X
9	SABMiller	South Africa	Beer	12.901	X	X	X	X	X
10	Kirin Brewery Co. Ltd.	Japan	Beer	11.745	X		X	X	X

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of *Fortune*, "The 2005 Global 500" [online], 25 July 2005 <<http://www.fortune.com/fortune/global500>>; annual reports from the companies and information provided by *América economía*, 2005.

^a Diageo's sales are for 2005.

B. Trans-latins in the beverages industry

The global soft drinks industry is extremely concentrated and features a complex network of licensing and equity relationships that originate primarily with the two United States-based beverage TNCs that dominate this industry: Coca-Cola and PepsiCo (Scheinman, 2004a). A distant third place was held by the global soft drinks corporation Cadbury-Schweppes, but it no longer figures among the top 10 beverage TNCs (see table V.2), having sold off much of its assets in the beverage business (the European division) in 2006.

Trans-Latins are prominent in both main segments of the beverages industry: carbonated soft drinks and beer. They have been and remain important allies of the undisputed world market leaders, Coca-Cola and PepsiCo, in maintaining the dominance of these two corporations' global brands in the region. For that reason, the internationalization of soft drinks trans-Latins must be analysed in the context of the distinct corporate strategies of these two global producers. Coca-Cola has sought a more direct influence over its core bottlers than PepsiCo has done. At the same time, some local bottlers of Coca-Cola and PepsiCo also market their own soft drinks brands (as well as beer, especially in the case of PepsiCo's associates). Local bottlers have therefore played somewhat distinct roles in the networks of the two global corporations.

In the beer industry, local companies have traditionally been dominant to global TNC brewers, both in Latin America and the Caribbean and elsewhere. Local, not global, brands lead the market, in contrast to the soft drinks industry. Regional and global beer brands are only recently making headway in the region, as specialty products in the context of the opening of local markets to imports or to licensing of local bottlers. At first, the internationalization of Latin American beer firms to form trans-Latins strengthened regional brands and, with few exceptions, was carried out independently of the dominant global corporations. In the last few years, however, the largest trans-Latin brewers have been absorbed into global brewers by way of large mergers and acquisitions, which has truncated the emergence of Latin American transnationals in this industry.

Given the way the two segments of the beverages industry are interrelated, it is necessary to examine the main trends in both in order to assess the prospects for emerging Latin American TNCs in this business. In the 1990s, particularly in the North American and European markets, per capita consumption of the more traditional drinks, such as carbonated

soft drinks and beer and certain other alcoholic beverages, began to come to a standstill, with consumer tastes changing in favour of other beverages. The main shifts have been from: (i) spirits to beer and wine; (ii) alcoholic- to non-alcoholic beverages, especially bottled water; and (iii) carbonated to non-carbonated beverages. This has put pressure on carbonated soft drinks manufacturers and brewers to diversify their products to keep up with these trends and to increase their range of non-carbonated soft drinks, such as juices, bottled waters and "light" beverages. Similar trends have developed in Latin America and the Caribbean, with an additional shift to low-price products (see box V.1).

These changes have created both opportunities and challenges for beverage companies. Many have reacted by bringing more new products on stream in the framework of "total beverage company" strategies aimed at satisfying changing consumer tastes by offering a more comprehensive product line-up. For example, the growth of wine consumption prompted such different companies as Australia's Foster and Chile's Compañía Cervecerías Unidas (CCU) to enter the wine segment. There are examples in the distilled spirits segment too, since Guinness UDV started producing liqueurs, vodka and whisky as well as beer, Pernod Ricard began to make liqueurs, distilled spirits and wines (Jacob's Creek), and Allied Domecq acquired leading wine brands in California. Even non-beverage companies, such as Nestlé, Unilever and Danone, are expanding their businesses into ready-to-drink beverages, especially bottled water (Wilkinson, 2004a). In order to extend their product line-ups, global TNCs have often sought out takeover targets that would bring them new products. The drive to acquire existing assets has had a greater impact than the entry of new competitors into the different segments of the beverage industry, which has led to the industry's consolidation in the hands of a few global players.

As well as extending their product line-ups, global TNCs have looked for ways to improve the position of their brands in both traditional and faster-growing, non-traditional markets. In terms of geographical expansion, TNCs took advantage of newly-opened markets in Eastern Europe, Asia and Latin America. In 2003, China overtook the United States as the largest consumer of beer; however, the United States was still the largest market in carbonated soft drinks, followed by Mexico and Brazil. In terms of positioning their brands in new and traditional markets, TNCs also searched for acquisition targets, further consolidating the industry.

Box V.1

CHANGES IN THE BEVERAGE INDUSTRY IN LATIN AMERICA: CHALLENGES TO COCA-COLA AND PepsiCo AND OPPORTUNITIES FOR REGIONAL COMPANIES

The existence of a large, young population in Latin America and the Caribbean offers promising growth prospects for beverage companies in the medium and long terms, with Brazil and Mexico being among the world's most attractive markets. Consumer trends are putting pressure on traditional players Coca-Cola and PepsiCo, while some smaller regional corporations have been able to move into market niches and expand internationally, independently of these two companies.

The first challenge to the dominant soft drinks TNCs comes from non-carbonated beverages. Although, like in other emerging markets, carbonated soft drinks sales still have potential for growth, Brazil and Mexico are reflecting global consumption patterns, with a rise in the consumption of bottled water and other non-carbonated beverages, such as juices. The established carbonated soft drinks producers are therefore facing competition both from transnational companies that have traditionally focused on food products, such as Nestlé, Danone, Parmalat, Bunge, Unilever and Kraft, and from local players such as Mexican trans-Latin Jugos del Valle.

Jugos del Valle has managed to conquer the region's main consumer markets: its native Mexico, where it has a 32% domestic market share, and Brazil, where it has a domestic market share of 37%. Unlike the large beverage companies that have sought diversification, Jugos Del Valle has concentrated on a niche market and on consolidating its brand name. The company started its international expansion

through exports, progressively acquiring knowledge of the Latin American market and, in 1999, building a plant in Brazil, from which it exports to other South American countries, the Middle East, Australia, New Zealand, Japan and China. Leading edge technology in the Brazilian plant and the company's strategic position within the region has helped Jugos Del Valle overcome the effects of the revaluation of the Mexican peso, which would otherwise have jeopardized its exports. In Bolivarian Republic of Venezuela and Peru, the company invested in partnerships with local producers in a system similar to that of the global soft drinks producers, whereby it sells concentrate to its partner companies, which add water and sugar, bottle the product and distribute it on the local markets. Between 1993 and 2001 the company operated a subsidiary in Puerto Rico in a similar fashion. Jugos Del Valle also has a Texan subsidiary that imports and distributes products, like many of the Mexican food companies targeting the Hispanic community in the United States.

The second major challenge to the dominant soft drinks TNCs comes from low-price products such as *tubainas* in Brazil and Kola Real in Peru. *Tubainas* are inexpensive carbonated soft drinks manufactured by a large number of local or regional firms, most of which are small or medium-sized. From the mid-1990s onwards, sales of *tubainas* grew steadily and strongly in Brazil, gaining large market shares in their respective regions. Coca-

Cola has responded by cutting costs, lobbying for better control of tax evasion, which it claims accounts for much of the cost advantages of the *tubainas*, and entering this market itself, for example by acquiring the Jesus brand, which is estimated to represent approximately 20% of the market in the northern Brazilian State of Maranhão.

This low-cost segment has given rise to another trans-Latin: Ajegroup. This corporation produces Kola Real, a low-priced beverage that has captured 20% of Peru's soda market. Kola Real was first sold in Bolivarian Republic of Venezuela and Ecuador in 2001, rapidly gaining over 10% of each market. In Mexico, where the company has production plants, the beverage was introduced as Big Cola and quickly gained 4% of the market. The brand became popular even in high-income segments. A 5% share of the Mexican market, which is the company's target for Kola Real, would be equivalent to its existing sales at home in Peru and in Bolivarian Republic of Venezuela and Ecuador (Scheinman, 2004a) and would thus double its total sales. Moreover, in February 2006 Ajegroup announced an investment in Thailand as a first foothold in the Asian market, where it also sees potential for its product (*América economía*, 2006).

It remains to be seen whether these trans-Latins will be able to sustain their challenge to the transnational players. Much will depend on their strategy as regards low-income markets, which is as yet not clearly defined in the region.

Source: John Wilkinson, "O setor de bebidas no Brasil. Processos de concentração e transnacionalização e o papel do capital nacional", Rio de Janeiro, June 2004, unpublished; Marc N. Scheinman, "Latin American corporate strategy in the soft drinks industry: for Coca-Cola and Pepsi-Cola Mexico is the crown jewel", Santiago, Chile, 2004, unpublished; David Gertner, Rosane Gertner and Dennis Guthery, *Coca-Cola's marketing challenges in Brazil: the Tubainas war*, Thunderbird, The Garvin School of International Management, 2004; *Folha de São Paulo*, "Receita amplia vigilância de grande empresa", 27 December 2005; *Beverage World*, "Latin America heats up", 15 February 2004; *Revista Recall*, "Tubainas mudam de cara e já controlam 32% do mercado", No. 49, 2002; official information from Jugos del Valle and *América economía*, "Empresa peruana de refrescos invierte en Tailandia", 24 February 2006.

These shifts in corporate strategies in search of wider product portfolios and access to new markets are accompanied by an unrelenting quest for scale economies in production, marketing and, in particular, distribution, all in a bid to improve efficiency. In other words, broader product line-ups, stronger presence in new markets and an ongoing effort to heighten efficiency are the main determinants shaping the global consolidation process in both the soft drinks and the beer sectors. These motivations are driving the internationalization of the main players,

which is taking place through a number of different modalities, especially exports, licensing agreements and foreign direct investment (FDI).

Table V.3 shows the main beverage companies in Latin America and the Caribbean. The list is headed by three trans-Latins, FEMSA, Ambev and Modelo, which all have annual sales of over US\$ 4 billion. These are followed by Bavaria, with almost US\$ 2 billion in sales, and CCU, Quilmes and Andina, whose sales range from US\$ 400 million to US\$ 700 million.¹ Latin America's

¹ Other similarly-sized beverage companies, such as Coca-Cola bottlers Arca and Contal, are not included in this ranking because they have not initiated a significant internationalization process.

largest beverage companies have taken on several different functions, acting as: (i) carbonated soft drinks bottlers and distributors for Coca-Cola or PepsiCo; (ii) soft drinks syrup producers, bottlers and distributors of their own products; and (iii) brewers. Some have specialized in a single role, while others combine several. Of these larger companies, only Modelo and Andina do not operate in both the soft drinks and beer industries. Most of these Latin American beverage companies have undertaken significant internationalization processes during the last decade or so and have thus grown into some of the largest trans-Latins. In 2003, three of the top 25 trans-Latins

by sales were beverage companies (ECLAC, 2005c). All of the beverage-producing trans-Latins listed in Table V.3 are linked to the industry's dominant TNCs by way of licences or foreign ownership, although the degree of TNC influence in their operations varies appreciably.

The rest of this section will examine the internationalization processes undertaken by these companies, first in the carbonated soft drinks segment, then in the beer segment, before drawing some conclusions about the future of trans-Latins in the beverage industry.

Table V.3
THE MAIN TRANS-LATINS IN THE BEVERAGES INDUSTRY, BY SALES, 2004
(Billions of dollars)

Company	Country of origin	Total sales	Soft drinks affiliation	Foreign brewer affiliation (licence)	Present foreign ownership
FEMSA: Coca-Cola FEMSA and FEMSA Cerveza	Mexico	8.4	Coca-Cola	Molson Coors, Heineken	The Coca-Cola Company holds 39.6% of Coca-Cola FEMSA, which is FEMSA's soft drinks division. Labatt held 30% of FEMSA Cerveza until 2004
AmBev	Brazil	4.5 ^a	PepsiCo	Interbrew	Now part of Inbev. Interbrew has controlled the company since 2004
Modelo	Mexico	4.1	-	-	Anheuser-Busch holds 50.2%
Bavaria	Colombia	1.9	PepsiCo	-	SABMiller has controlled the company since 2005
CCU	Chile	0.7	PepsiCo	Anheuser-Busch, Guinness, Heineken, Paulaner	Anheuser Busch holds 11% of CCU Argentina. Heineken owns approximately 31% (50% of the control group) ^b
Quilmes	Argentina	0.5	PepsiCo ^c	AmBev/Interbrew	AmBev holds 50.4%. Heineken held minority stakes from 1984 to 2002
Andina	Chile	0.4	Coca-Cola	-	The Coca-Cola Interamerican Corporation holds 10.7%

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the corporate websites and FEMSA, "Presentación a inversionistas", June 2005.

^a Includes Quinsa (Quilmes holding company) sales for Latin America.

^b Schorghüber was part of the controlling group until 2003.

^c Coca-Cola in Paraguay from 1965 to 2000.

1. Trans-Latin soft drinks producers

The trans-Latins in the soft drinks industry have to be analysed in the context of the production and distribution systems of the principal global TNCs to which they are affiliated. Coca-Cola and PepsiCo sell concentrates (flavouring ingredients used to prepare beverage syrups or finished beverages) and syrups (beverage ingredients composed of concentrate, sweetener and water) to authorized bottlers and fountain wholesalers. The authorized intermediaries combine these ingredients into finished carbonated soft drinks, which they bottle and sell under

the Coca-Cola and PepsiCo trademarks (Scheinman, 2004a).² The marketing of standardized global brands is central to their success. Despite the simplicity of the basic business concept, the manufacturing process and distribution services involved in the bottling operation make it a capital-intensive activity, requiring specialized, high-speed production lines, large truck fleets and other assets (Yoffie, 2004). While global brands are dominant in the carbonated soft drinks markets, as bottlers, the local firms are often crucial partners for the beverage TNCs.

² Net sales and profits of Coca-Cola and PepsiCo trademarked beverages are reported through their country bottlers and consolidated at the corporate level. Therefore, it is necessary to examine the major bottlers' financial reports filed with the United States Securities and Exchange Commission (SEC) in order to understand the performance of Coca-Cola and PepsiCo in specific countries (Scheinman, 2004a).

It is in this framework that soft drinks trans-Latins have emerged in the soft drinks industry, in association with the two dominant soft drinks TNCs. The international expansion of these trans-Latins has to be seen, therefore, in the context of worldwide competition between the dominant players in this industry.

From the mid-1970s up until the late 1990s, Coca-Cola and PepsiCo grappled mainly with each other, in an aggressive competition that was referred to as the “Cola Wars”.³ Coca-Cola and PepsiCo invested billions of dollars in their key bottlers to enforce uniform advertising, branding, marketing and quality standards throughout their global distribution systems (Scheinman, 2004a). In tandem with these new investments, Coca-Cola and PepsiCo made increased demands on their bottlers’ performance and imposed changing contractual terms with regard to the development of new flavours, cost saving measures and advertising. The reorientation of their corporate strategies with regard to their global networks resulted in improved performances for both of these two dominant beverage TNCs. From 1975 to 1995, the two corporations averaged annual growth rates of approximately 10% in the soft drinks business both in their largest market, the United States, and worldwide (Yoffie, 2004). In most regions, Coca-Cola led the market, but PepsiCo held a strong second place. Notable exceptions were certain Middle Eastern and South East Asian countries, countries of the former Soviet Union and the Bolivarian Republic of Venezuela, where PepsiCo fared better. From the late 1990s onwards, PepsiCo focused increasingly on emerging markets and performed very well in India, China and the Russian Federation. By 2004, sales outside North America had come to account for 70% of total sales in the case of Coca-Cola (Coca-Cola, 2005) and 34% for Pepsi (PepsiCo, 2005), compared to 62% and 9%, respectively, in 2000 (Yoffie, 2004).

In the 1990s, the shift in consumer tastes away from carbonated soft drinks posed a new challenge for both Coca-Cola and PepsiCo, because it obliged them to compete in wider product markets with other competitors. Both companies developed new non-carbonated products, diversified their cola flavours by adding lemon twists and other ingredients and incorporated local flavours—such as guaraná in Brazil, or Inca Kola in Peru—into their portfolios.⁴ Both companies have also invested substantially in bottled waters and other drinks in their drive to become total beverage companies (Wilkinson, 2004a). PepsiCo has traditionally been a more diversified company than

Coca-Cola and, although this was once considered a liability (Scheinman, 2004a; Hartley, 1998), in the context of recent market trends it has been increasingly viewed as an asset. In fact, PepsiCo overtook Coca-Cola in terms of market capitalization in 2005 (*The Economist*, 2005b). One industry commentator went so far as to suggest that losing the cola wars was the best thing that could have happened to PepsiCo, as it forced the company to transform itself from a beverage company into a food company that sells beverages (*Fortune*, 2006).

These soft drinks companies also diversified into new markets which offered better growth prospects. In contrast to the trends described in traditional markets, in emerging markets carbonated soft drinks still showed significant potential for growth. Throughout the 1990s, Coca-Cola and PepsiCo competed fiercely for market shares in countries whose per capita consumption levels were still considerably below those of North America (such as China, India and Eastern European countries). Latin America, especially its larger countries, such as Brazil and Mexico, was also viewed as promising, given the high consumption rates in Mexico and the potential for growth in these rates in other countries, coupled with a young population. Latin America represents approximately 20% of global soft drinks sales (including non-carbonated drinks). Mexico alone accounts for nearly 50% of the region’s consumption. From the vantage point of market size, Mexico ranks second in volume after the United States, with Brazil fifth and Argentina fifteenth. Mexico leads the world in per capita consumption, however, with an average of 342 litres per year, compared with 327 in the United States. By contrast, Brazil and Argentina consumed only 96 and 88 litres per capita, respectively, which was less than a third of Mexico’s total. Mexico and Brazil are also ranked among the world’s fastest growing markets, in fourth and eighth place, respectively (Scheinman, 2004a).

Economic crises in the late 1990s in East Asia, the Russian Federation and Latin America caused the sales of Coca-Cola and PepsiCo to deteriorate and their profits to wane, although PepsiCo’s smaller overseas presence made it less vulnerable to these crises (Yoffie, 2004). Both companies restructured their operations, largely by consolidating their bottling operations, based on the concept of “anchor bottlers”. This concept had first arisen during the 1980s after Coca-Cola’s less competitive bottlers had been weakened by tougher performance demands and new contractual relationships imposed as

³ This is the title of a 1980 book by J.C. Louis and Harvey Yazizjian (Everest House).

⁴ In Brazil, Coca-Cola expanded the output of Guaraná Kwat, renovated production facilities and planted 200 hectares of guaraná. Further expansions followed. Kwat secured 11% of the guaraná market in 2002, against Antarctica’s 28%. Coca-Cola also expanded Fanta’s mix by incorporating new flavours such as citrus and strawberry (Scheinman, 2004a). In Peru, Coca-Cola entered a partnership with JR Lindley, holders of the Inca Kola brand.

part of the new strategy the corporation had introduced in 1978. Coca-Cola therefore acquired some of these weaker companies, which it restructured through capital injections and sold on to other, better-performing bottlers. In the mid-1980s Coca-Cola acquired two of its largest bottlers, which brought one third of the volume sold in the United States under company-owned bottlers. These companies were later unified under Coca-Cola Enterprises (CCE), consisting of 51% publicly-owned shares and 49% owned by Coca-Cola (Yoffie, 2004). Coca-Cola thus restructured its bottlers' network to consist of more anchor bottlers in which it owned a large minority stake and a position on the board of directors. One of the key advantages of the anchor bottler system was that it heightened Coca-Cola's control over a smaller group of larger and more geographically diverse bottlers with more efficient operations and higher investment capacity. By 2000, CCE handled 70% of Coca-Cola's North American sales.

PepsiCo also started acquiring a number of large bottlers in the late 1980s. By the mid-1990s, bottlers in the United States numbered less than 200, compared to more than 400 in the mid-1980s. PepsiCo owned approximately half of these and had equity stakes in most of the rest (Yoffie, 2004). Eventually, as described below, the anchor bottler system spread beyond the United States. In Latin America, anchor bottlers became the most prominent soft drinks trans-Latins.

The large local beverage manufacturers in Latin America and the Caribbean are affiliated with either Coca-Cola or PepsiCo as franchised bottlers and, in some cases, through minority ownership. The section below will analyse the main Latin American carbonated soft drink producers that have invested outside their home countries, i.e., the soft drinks trans-Latins, by affiliation to either Coca-Cola or PepsiCo. An important distinction to bear in mind is that some companies produce primarily or exclusively the beverages of one of the two dominant beverage TNCs, while others have brands of their own whose sales outweigh those of the Coca-Cola or PepsiCo products they also make. As a consequence, these companies' outward investments have been undertaken in two distinct manners: (i) by acquiring other soft drink bottlers, in the context of the global strategies of their licensors (Coca-Cola or PepsiCo); or (ii) by acquiring other bottlers, in the context of their own internationalization strategies and usually led by the beer segment, thus relegating their licensing arrangement (usually with PepsiCo) to a secondary position in their overall sales.

(a) The Coca-Cola bloc

Two trans-Latins stand out among Coca-Cola's bottlers in Latin America: (i) Coca-Cola FEMSA (Mexico), the

soft drinks division of the FEMSA group, which also owns a major trans-Latin brewer, FEMSA Cerveza (see section 2); and (ii) Andina, the main bottler of Coca-Cola in Chile. The experiences of two smaller Coca-Cola bottlers in Chile —Embonor and Polar— will also be examined. Quilmes of Argentina is a special case, as a trans-Latin which held a Coca-Cola bottling concession in Paraguay for several decades until it shifted its bottling operations to PepsiCo products. Figure V.1 shows the internationalization patterns of these companies.

(i) Coca-Cola FEMSA: Coca-Cola's major player in Latin America

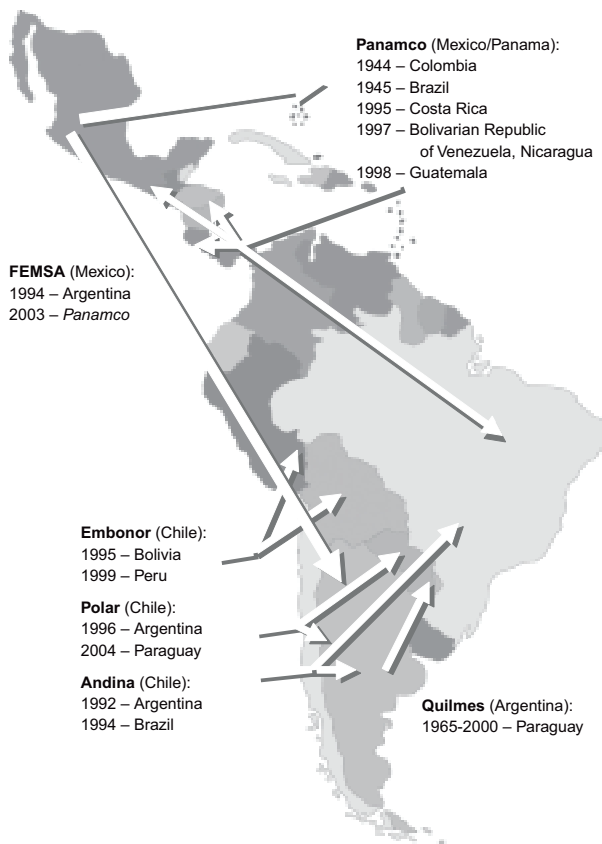
The FEMSA group was founded as a brewer in Mexico in 1890 and entered the soft drinks business in the late 1970s. It acquired several Coca-Cola bottling franchises for Mexico City and other Mexican regions in 1979. In the early 1990s, The Coca-Cola Company bought a 30% stake in FEMSA's soft drinks division, Coca-Cola FEMSA. This stake was later increased to 39.6% in view of the company's success in the Mexican market, including its achievements in local production and distribution, which increased its potential to contribute to the restructuring of the Coca-Cola system in Latin America.

In view of its position as the leader of a market that already had a high per capita consumption of soft drinks, Coca-Cola FEMSA began to look for growth opportunities outside Mexico, in an initiative that was strongly supported by Coca-Cola. It acquired the Coca-Cola bottling franchise for the city of Buenos Aires, Argentina in 1994. Although this experience was initially a challenge for Coca-Cola FEMSA in terms of production practices and managerial capacity, it also taught the company how to adapt to changing circumstances, which stood it in good stead during the Argentine crisis shortly after the turn of the decade. Coca-Cola FEMSA adopted a number of measures to improve its performance, such as the development of cheaper products, the segmentation of metropolitan markets by purchasing power and the use of returnable bottles, which heightened consumer loyalty. These strategies were then successfully applied to other regions. The challenges presented by the Buenos Aires operation and the company's efforts to overcome them brought Coca-Cola FEMSA to a new level of efficiency and sophistication.

The next internationalization initiative undertaken by Coca-Cola FEMSA was the acquisition of Panama-based Panamerican Beverages Inc. (Panamco) for US\$ 3.7 billion in 2003. Panamco was particularly attractive, because it had been a Coca-Cola anchor bottler for Latin America since 1995 and, through extensive internationalization, had come to own bottling operations in a large number of

countries in the region: Mexico, Guatemala, Nicaragua, Costa Rica, Panama, Colombia, Bolivarian Republic of Venezuela and Brazil. Panamco had been weakened by a series of crises in the countries of the region, such as those experienced by Bolivarian Republic of Venezuela in the late 1990s; the aftermath of the local-currency devaluation in Brazil in 1999; and episodes in Colombia and Central America (BBC, 2003). By 2003, Panamco's difficulties were affecting Coca-Cola's performance.

Figure V.1
THE INTERNATIONALIZATION OF LATIN AMERICAN COCA-COLA BOTTLERS



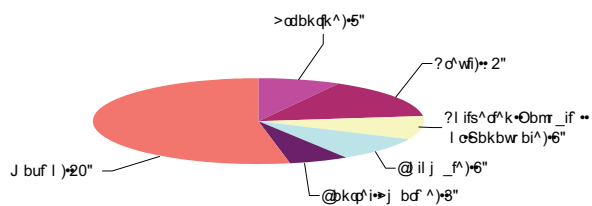
Source: Economic Commission for Latin America and the Caribbean (ECLAC).

Coca-Cola FEMSA, supported by Coca-Cola, decided to purchase Panamco as a means to expand its presence in markets with promising growth prospects. Coca-Cola FEMSA proceeded to close down Panamco's redundant plants: eleven out of seventeen plants were closed in Colombia and, of the nine plants in Bolivarian Republic of Venezuela, five were made into distribution centers. Coca-Cola FEMSA applied practices that had been successful in its Mexican and Argentine operations to its newly acquired assets. These included marketing strategies tailored to different purchasing power segments within the franchised territories, the elimination of

certain intermediaries in the distribution process, the improvement of data collection on consumption patterns and the introduction of new technology for data processing, which allowed the company to develop and implement its market segmentation strategies efficiently.

Coca-Cola FEMSA is now the second largest bottler of Coca-Cola products in the world, the largest soft drinks company in Latin America and the largest bottler of Coca-Cola products outside the United States (Scheinman, 2004a). Market diversity also gave the company greater revenue stability by balancing out seasonal differences in consumption and contributed to its overall efficiency by significantly scaling up its operations. The company's sales are currently distributed as shown in figure V.2.

Figure V.2
FEMSA SALES BY COUNTRY, 2004 (Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of FEMSA, "Presentación a inversionistas", June 2005.

In summary, the internationalization process of Coca-Cola FEMSA was forged by the company's need to secure space for growth beyond its domestic market, combined with Coca-Cola's support based on its own anchor bottler strategy and the opportunity created by the financial troubles of other bottlers in the Coca-Cola network. Through its investment in Argentina and its acquisition of Panamco, Coca-Cola FEMSA gained footholds in key metropolitan areas of South America, such as Buenos Aires and São Paulo. The company's experience with these foreign investments pushed it towards more efficient practices and turned it into a highly competitive player in the Latin American soft drinks industry.

(ii) *Andina and other Chilean bottlers: subregional expansion*

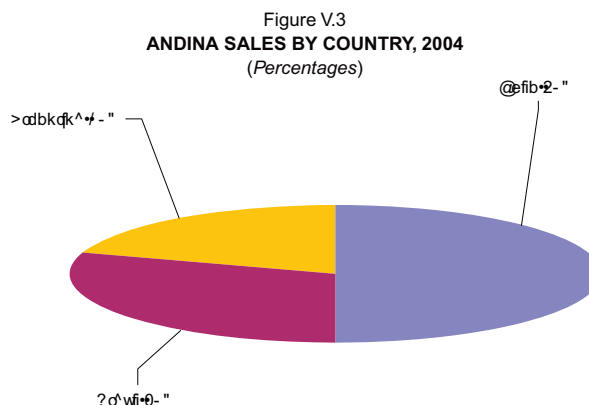
Three Coca-Cola bottlers —Andina, Embonor and Polar— operate on Chilean territory and have all expanded internationally into neighbouring and other countries. Andina alone is among the region's largest beverage companies (see table V.3) with annual sales in the order of US\$ 0.4 billion, which is, however, less than 5% of the sales of the FEMSA group (Coca-Cola FEMSA and FEMSA Cerveza combined). Embonor and Polar are interesting, if marginal, cases.

Andina was established as a Coca-Cola bottler in Chile in 1946. It started its international expansion in the 1990s, focusing on Argentina and Brazil. In Argentina, it acquired a minority share in INTI SAIC, a Coca-Cola bottler in the city of Córdoba. In 1992, it increased its holding to a controlling stake. In 1995, Andina gained control of Embotelladora del Atlántico S.A. (EDASA), a Coca-Cola bottler for the Rosario and Mendoza areas. Greenfield investments were subsequently undertaken in Córdoba, where Andina concentrated its Argentine production from 2002 onwards, closing down other plants. Cost savings made through this restructuring and other measures, such as the reintroduction of returnable bottles, helped Andina survive the aftermath of the severe crisis in Argentina in the early years of the new decade.

Andina's Brazilian operations began in 1994, when it purchased Rio de Janeiro Refrescos Ltda., whose franchise area covered part of the State of Rio de Janeiro, part of the State of Minas Gerais, and the State of Espírito Santo. In 2000, it acquired Coca-Cola Nitvitgov Refrigerantes S.A (NVG) which expanded its franchise zone within Rio de Janeiro State. Lastly, in 2004, it undertook a swap with Coca-Cola's Brazilian subsidiary Recoforma Indústria do Amazonas Ltda., through which it exchanged its Minas Gerais franchise for other areas, again in Rio de Janeiro State, all with a view to achieving economies of scale (Feller-Rate, 2005b). Thus, Andina was able to restructure its Brazilian operations to make its distribution network more efficient.

Currently, as shown in figure V.3, half of Andina's sales are made outside Chile, which underscores the importance of internationalization in the company's growth strategy. Andina's Argentine and Brazilian territories account for almost 80% of the total population covered by the company's franchising contracts. Moreover, these territories have a lower per capita consumption than Chile and therefore possess greater potential for growth (Feller-Rate, 2005b). As regards franchise areas, in a manner of speaking, Andina has positioned itself immediately behind Coca-Cola FEMSA, having obtained the second most important licence areas (in terms of the population they serve) in both Argentina (provinces of San Juan, Mendoza, Entre Rios, Córdoba, San Luis, and large parts of Santa Fe and Buenos Aires, while Coca-Cola FEMSA holds the metropolitan area of Buenos Aires) and Brazil (Rio de Janeiro, with Coca-Cola FEMSA covering São Paulo). Andina thus combines a solid foothold in the relatively stable Chilean market with operations that embody higher potential (but also higher risk) in Argentina and Brazil. Coca-Cola has supported Andina's internationalization efforts by acquiring minority equity ownership (11%) in Andina itself in 1996, then by supporting bottler acquisitions and the 2004 franchise swap that enabled Andina to

maximize operational and managerial efficiency. As in the case of Coca-Cola FEMSA, productive restructuring catalysed by the Argentine crisis also helped to enhance the company's overall efficiency.



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of Feller-Rate, "Informe de clasificación: Embotelladora Andina S.A.", Santiago, Chile, May 2005.

Chile's smaller Coca-Cola bottlers, Embonor and Polar, have internationalized their business following similar patterns to that of Andina, that is, starting from relatively secure footholds in Chile, they have invested in the acquisition of bottlers in key regions in neighbouring or nearby countries. Embonor, which possesses approximately 35% of the domestic market by volume, expanded northwards from its Chilean franchise areas in the north of the country towards Bolivia and Peru. In 1995 and 1996, it acquired Embotelladoras Bolivianas Unidas (Embol) and now sells approximately 96% of Coca-Cola products in Bolivia. In 1999 it acquired the British group Inchcape's bottling assets in Peru, consisting of the Coca-Cola bottler Embotelladora Latinoamericana S.A. (ELSA), and in Chile. In the deal, The Coca-Cola Company acquired a 42.5% stake in Embonor. In January 2004, the company sold its stakes in its Peruvian assets to JR Lindley, the makers of Inca Kola, with whom Coca-Cola had been allied since 1999 (Feller-Rate, 2006). At present, 20% of Embonor's sales come from Bolivia, which has a lower per capita consumption than the Chilean market and therefore potential for growth. Internationalization has helped Embonor position itself to develop this potential, while its base in Chile—whose market offers higher margins (Feller-Rate, 2006) and greater stability—helps to offset the additional risks of operating in Bolivia.

In contrast to Embonor and Andina, Polar, the smallest of the three Chilean Coca-Cola bottlers, started in 1971 as a brewer. The group held brewing assets until 2000, when they were divested—in line with The Coca-Cola Company's strategy for its bottlers—to enable the company

to concentrate on its core business. In Chile, Polar expanded by acquiring two Coca-Cola bottlers in 1979 and 1981. It began to internalize its business eastwards in 1996, when it undertook a series of acquisitions of Argentine Coca-Cola bottlers, covering certain provinces of central and southern Argentina. In 2004, it acquired Paraguay Refrescos S.A. (Paresa), the exclusive Coca-Cola bottler for Paraguay (Feller-Rate, 2005c). Coca-Cola owns 29.4% of Paresa, through the Coca-Cola Interamerican Corporation (Feller-Rate, 2005c). Polar followed the same pattern as the other Chilean bottlers, in the sense that it expanded with support from The Coca-Cola Company, from a secure base in Chile to larger but riskier markets (its Argentine and Paraguayan operations account for 86% of the total population living in all Polar's franchised territories).

The experience of the Chilean Coca-Cola bottlers thus reflects the advantages of a stable home-country market as a base from which to internationalize into neighbouring countries. With support from The Coca-Cola Company, these bottlers have been able to expand internationally into markets that offer promising growth prospects, while managing the additional risks involved in such a venture.

(iii) Quilmes: jumping ship

Argentina's Quilmes group was founded in the late nineteenth century, originally to supply the European beer industry with agricultural inputs. It later became a brewer and this is now its main activity. Quilmes had a strong presence in Paraguay through its beer operations (see section 2), which gave it an advantage as a soft drinks bottler. It held a monopoly over Coca-Cola product distribution in Paraguay from 1965 up until 2000, having purchased a controlling interest (57.97%) in Paraguay Refrescos (the company that was later acquired by Polar of Chile) and acquiring certain assets of Refrescos del Parana S.A., which controlled approximately 10% of the Paraguayan territory. Apparently not satisfied by its relationship with Coca-Cola, in 2000 Quilmes withdrew from the Coca-Cola franchise in Paraguay to join the larger PepsiCo network there.

To summarize, then, the Coca-Cola bloc is built on the operations of two principal trans-Latins—Coca-Cola FEMSA and Andina—with bases in Mexico and Chile, respectively. The large scale operations of Coca-Cola FEMSA in Mexico provided it with the experience and financial resources to undertake huge acquisitions all over Latin America, most notably in Argentina and Brazil, even before it embarked upon the largest operation of all, the acquisition of Panamco, which greatly expanded its presence in the region. Andina and the other, smaller Chilean bottlers internationalized their business on a

more modest scale in keeping with their sales volume and the size of their base market. They largely limited their international expansion to neighbouring or nearby markets in the Southern Cone.

In all cases, the support of Coca-Cola has been essential to the success of these trans-Latins and that support must be interpreted in the context of Coca-Cola's global consolidation strategy. The operations of The Coca-Cola Company are set apart by the significant equity interest it tends to have in its partners: 39.6% of Coca-Cola FEMSA, 11% of Andina, 45.5% of Embonor, 29.4% of Polar and, in the past, 25% of Panamco. Another defining trait of these Coca-Cola associates is the fact that their core business is soft drinks, not other beverages. For example, the revenues of Coca-Cola FEMSA accounted for 49.6% of the FEMSA group's total revenues in 2004, compared to only 26.4% from FEMSA Cerveza. The Chilean bottlers, Embonor, Andina and Polar, sell only soft drinks. This is consistent with Coca-Cola's traditional strategy of focusing on its core business. The nature of the business, with bottlers using inputs imported from The Coca-Cola Company to produce Coca-Cola products that account for much or all of their income, coupled with The Coca-Cola Company's significant minority equity holdings in these trans-Latins, means that Coca-Cola wields a strong influence over its anchor bottlers. The exception of Quilmes, which decided to withdraw from Coca-Cola franchise in Paraguay, suggests that the possibility of combining beer interests with a PepsiCo franchise in Paraguay offered more independence of action.

(b) The PepsiCo group

One major feature that distinguishes PepsiCo's main Latin American associates—Quilmes, AmBev and Bavaria—from the trans-Latins in the Coca-Cola bloc is that PepsiCo's products usually account for a minority of its associates' total sales and its influence over their overall operations is smaller. For example, in 2005, Ambev's own soft drinks brands—Guarana Antarctica, Sukita, Soda Limonada Antarctica and Guarana Brahma—accounted for 68.4% of its soft drinks sales. Another important characteristic is that the core business of most of the PepsiCo trans-Latins is brewing, not soft drinks. For example, beer represents 83% of the sales of both AmBev and Bavaria, and 66% of Quilmes' total sales. It would seem that, whereas the Coca-Cola system tends to build on the advantages of its principal bottlers' focus on core products, the PepsiCo network relies more on synergies among different products within single distribution systems. Figure V.4 shows the flows of international investment made by PepsiCo's trans-Latin associates in the soft drinks industry.

Figure V.4
THE INTERNATIONALIZATION OF LATIN AMERICAN PEPSICO
BOTTLERS



Source: Economic Commission for Latin America and the Caribbean (ECLAC).

(i) *Quilmes: the Argentine soft drinks leader*

Quilmes gained international experience in the soft drink bottling segment through its Coca-Cola franchise in Paraguay in 1965-2000 and its brewing interests in the Uruguayan market as of 1965. For this reason, the main owners of Quilmes, the Bemberg family, were well placed to take over the operations of Buenos Aires Embotelladora (Baesa) in Argentina and Uruguay (see box V.2). In December 1999 Quilmes acquired what remained of the largest PepsiCo bottler in Argentina and the only one in Uruguay. Subsequently, Quilmes acquired a 99.21% interest in Embotelladora del Interior S.A. (EDISA), the second largest PepsiCo producer and bottler in Argentina. In this manner, Quilmes came to control an estimated 84% of the production and sale of PepsiCo carbonated soft drinks in Argentina and 100% in Uruguay, where it also holds 98% of the beer market.

Quilmes' internationalization as a PepsiCo bottler was thus confined initially to Uruguay. With the Baesa acquisition, Quilmes increased its total soft drinks volume (including Argentina and Uruguay) nearly threefold (Quinsa, 2001) and began to capitalize on the synergies created by merging its soft drinks and beer distribution networks. Quilmes' affiliation with PepsiCo was, moreover, a good combination with its subsequent (2002) alliance with AmBev, which also acquired some of the Baesa assets and was PepsiCo's bottler in Brazil.

Box V.2

BAESA: A SOURCE OF ASSETS FOR PEPSICO-ASSOCIATED TRANS-LATINS

Buenos Aires Embotelladora (Baesa) was founded in 1990 in Argentina and held the Pepsi and Seven-Up franchise for the metropolitan area of Buenos Aires and other regions of Argentina. Shortly thereafter it initiated its international expansion supported by PepsiCo and eventually became its largest bottler outside the United States. By 1994, it had acquired other assets in Uruguay, Chile—a partnership with CCU in Embotelladoras Chilenas Unidas S.A. (ECUSA)—and Argentina. The following year, it attempted to enter the Brazilian market.

The rapid international expansion of Baesa soon encountered problems. It had overinvested in a number of ways, building four plants and acquiring a fleet of over 700 trucks, investing in specific products for the Brazilian market (such as refrigerating equipment for exclusive retailers) and running up huge marketing expenses. To finance all this, the company

incurred excessive debt in both Brazil and Argentina. Coca-Cola's aggressive reaction to the Argentine firm's move into Brazil caused Baesa to lose many of its smaller and most lucrative retailers there. Moreover, a change in the tax legislation in Argentina (allegedly influenced by Coca-Cola) favouring colas and disadvantaging other soft drinks hurt Baesa, most of whose profit came from non-cola beverages. By 1996, the Baesa plants were operating at one third of capacity, some had to be shut down (Hartley, 1998) and PepsiCo had to intervene in the company. By 1997, Baesa was forced to withdraw from the Buenos Aires and New York stock exchanges.

During that same year, Baesa attempted to restructure by selling its Brazilian subsidiary to Brahma. In this operation Brahma repurchased the bottling license for Pepsi and Seven-Up (which it had sold to Baesa in 1994) and acquired five of the Baesa industrial plants and

related assets. Subsequently, Baesa sold its Chilean assets to CCU and its Argentine and Uruguayan holdings to Quilmes. Early in 1999 (when PepsiCo was still its largest shareholder, with 23.5%), the ownership of Baesa was transferred to its main creditors: PepsiCo, Citibank, BankBoston and VVB Bank. At that time, Baesa owed US\$ 735 million in outstanding debt (*Clarín*, 1997, 1998). Thus, the firm's internationalization proved to be its undoing and its foreign assets were acquired by other trans-Latins in the PepsiCo network.

The rapid internationalization process of Baesa appears to have surpassed its financial and managerial capacity, resulting in the accumulation of large volumes of debt unsupported by its operational performance, somewhat similarly to the experience of Panamco of the Coca-Cola bloc. Baesa failed in part because it did not have the benefit of a home market with Mexico's volume or Chile's economic stability.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information provided by CCU, Quilmes and AmBev; Robert F. Hartley, "Fracasos de marketing", *Executive Digest*, No. 42 [online] 1998 <<http://www.centroatlantico.pt.>>; *Clarín*, "La embotelladora de Pepsi vuelve al ruedo", 7 December 1998 and "Brahma compró la Pepsi en Brasil", 24 October 1997.

(ii) AmBev: PepsiCo's major player in Latin America

AmBev—the American Beverage Company—was created through the merger of Brazil's largest beverage companies, Brahma and Antarctica, in 1999. Before the merger, in 1997, Brahma had purchased the Brazilian assets of Baesa (see box V.2) and signed a 20-year franchise agreement to distribute PepsiCo products in Brazil. Like Quilmes, however, AmBev was first and foremost a brewer, and much of its new competitiveness was based on the synergies of distributing both beer and soft drinks, which is why the affiliation to PepsiCo made more sense than its previous Coca-Cola licence.

The franchising agreement brought benefits to both PepsiCo and AmBev. With AmBev as its distributor, PepsiCo products gained access to new sales points in Brazil, especially restaurants, where AmBev had established a strong position. For AmBev, the launch of Pepsi Twist in Brazil in 2003 gave a fresh boost to PepsiCo's performance there (Gertner, Gertner and Guthery, 2004) and the alliance with PepsiCo helped promote AmBev products abroad, for example, in 2001 PepsiCo began producing Guarana Antarctica in Europe.

AmBev's internationalization as a PepsiCo bottler began a little later, following a wave of outward investments by the company in its main business, beer (see section 2). In 2003, AmBev acquired Embotelladora Rivera, the PepsiCo franchise holder in the north of Peru and Lima, and in 2004 it took over 51% of Embotelladora Dominicana, the PepsiCo franchisee in the Dominican Republic. These transactions aided further expansion into the beer market, on the back of the established soft drinks distribution networks. In Guatemala this was carried out through a joint venture with CabCorp, PepsiCo's Guatemala-based anchor bottler for Central America, whereby CabCorp maintained its independence in the soft drinks operations. By 2004, through its Brazilian, Peruvian and Dominican Republic operations, AmBev had become the largest Pepsi-Cola bottler outside the United States. The internationalization of AmBev's soft drinks business has therefore been largely a vehicle for its regional expansion as a brewer.

(iii) Bavaria: Andean expansion

Bavaria, Colombia's largest beverage company, does not distribute PepsiCo products in its home country, where it concentrates on its core businesses of beer, malt, water and soft drinks. In 1995 it acquired the PepsiCo franchise in Panama, however, and, as a consequence of its acquisition of Backus & Johnston in Peru, it inherited Embotelladora Frontera, which held the PepsiCo franchise for the northern Peru until July 2004. In January of that year, through its Panama subsidiary, Bavaria had also acquired 49% of Grupo ECSA (Embotelladora Centroamericana S.A.), the PepsiCo bottler in Costa Rica. Lastly, Bavaria purchased Corporación Boliviana de Bebidas S.A. (CBB), the PepsiCo bottler in Bolivia, which held 25% of the soft drinks market there. CBB was also part owned by Backus & Johnston, the brewer in which Bavaria had owned a controlling stake since 2002. Backus & Johnston had acquired CBB in 2000, when it bought Cia. Cervecera del Sur, then the owner of Embotelladora Frontera in Peru and of CBB in Bolivia. As was the case for AmBev and Quilmes, Bavaria's internationalization as a PepsiCo bottler is intrinsically tied to its international expansion as a brewer.

In short, the PepsiCo network in Latin America is different to that of Coca-Cola in several key ways. These differences include the core businesses (beer or soft drinks) of the associated trans-Latins, the importance (secondary or central) of the TNC products in the trans-Latins' product line-ups and the geographical base of the principal bottlers (Argentina/Brazil/Colombia versus Mexico/Chile). In general, the PepsiCo soft drinks network allowed its bottlers greater independence of action. This aspect will become clearer with the analysis of the beer market in Latin America and the Caribbean (see section 2).

The analysis of these two soft drinks TNC-associated networks in Latin America suggests that knowledge of local market traits in the region is a significant competitive advantage possessed by the soft drinks trans-Latins. This is reflected in the FDI of the Latin American bottlers allied to Coca-Cola and PepsiCo, which is exclusively intra-regional in nature. At the same time, it is important to look at the brewing operations of PepsiCo's associates in order to comprehend the overall nature of their corporate strategies.

2. Trans-Latin brewers

One characteristic that sets the beer market apart from that of soft drinks is that, traditionally, local or, more recently, regional players have dominated national markets with local brands. Most foreign brands have evolved as pricey,

specialty products that still enjoy only marginal market shares. The structure of the global beer industry, which is much more fragmented and complex than the soft drinks business, led the largest TNC brewers (see table V.4) to

focus on consolidating their home markets and positioning their brands in other large markets before turning their attention to emerging economies. In the meantime, local and regional players positioned themselves in the emerging regions. One emerging market brewer —South African Breweries— was even able to develop into a TNC based on its ability to operate in difficult business environments (see box V.3). The leading TNC brewers have not been able to control their local operations and mould consumer tastes to the same extent as the carbonated soft drinks TNCs. Instead, they have been obliged to employ a number of different modalities (exports, licences and FDI) to link up with local players in order to position their products in those national markets. The experience of the beer industry in Latin America and the Caribbean illustrates this.

Table V.4
WORLD'S LARGEST BREWERS BY PRODUCTION VOLUME, 2004
(Millions of hectolitres and billions of dollars)

Company	Country of origin	Beer production (Millions of hectares)	Beer sales (Billions of dollars)	Main brands
InBev	Belgium	202	10.1	Stella Artois, Brahma, Beck's, Staropramen, Bass, Leffe, Hoegaarden
SABMiller	South Africa	138	11.3	International Brands: Pilsner, Urquell, Peroni Natro Azzuro, Miller Genuine Draft, Caste Large
Anheuser-Busch	United States	136	12.2	Budweiser, Michelob, Busch
Heineken	Netherlands	98	11.8	Heineken, Amstel
Molson Coors ^a	Canada/ United States	60	6.0	Molson Canadian, Molson Dry, Coors Light, Carling, Zima

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information provided by the companies.

^a Before the sale of Kaiser to FEMSA Cerveza.

Box V.3

SABMILLER: GLOBAL COMPETITIVE ADVANTAGES BASED ON HOME COUNTRY INSTITUTIONAL VOIDS

Khanna and Palepu (2005) demonstrate that, in developing countries, local firms that are able to overcome the challenges created by institutional voids —defined as “the absence, or poor functioning, of the specialist intermediaries needed to bring buyers and sellers together in markets”— can gain significant competitive advantages, even vis-à-vis transnational corporations. SABMiller is an example of a company that overcame institutional voids in its native South Africa and, in doing so, developed competencies

that enabled it to become a successful transnational corporation. South African Breweries (SAB) came into existence at the end of the nineteenth century. Under apartheid, it developed a distribution system through which it was able to sell beer through traditional beer-drinking outlets (shebeens) to the black population. The expertise the company acquired in dealing with the complexities of such a distribution system enabled it to conquer markets in several African countries (especially Angola, Mozambique, the United Republic

of Tanzania and Zambia) and later in India, China (where it is now the second largest brewer), Honduras and El Salvador. SAB was then catapulted into the premier league of TNC brewers when it acquired Miller in the United States in 2002 and the Colombian company Bavaria, one of Latin America's largest brewers, in 2005. SABMiller utilized the competitive advantages of its experience in operating in difficult business environments to become a beer-producing TNC, something that no trans-Latin brewer has accomplished.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of Tarun Khanna and Krishna Palepu, *Emerging Giants: Building World-Class Companies in Emerging Markets*, Harvard, Harvard Business School, 2005 and *The Economist*, “Beer – Andean thirst”, 29 October 2005.

The growth rate of Latin America's beer market is not among the highest; however, the region's young population and the relatively low per capita consumption in most countries (see table V.5) make for promising middle- and long-term growth prospects, especially in comparison to the traditional markets. Per capita consumption in the United States is estimated at approximately 84 litres, and in Europe between 80 and 140 litres (Agriculture and Agri-Food Canada; Brewers of Europe), which makes Brazil and Mexico look very attractive markets. For global players, one implication of the growing importance of emerging markets, including Latin America, is that local know-how as regards effective operation in developing country business environments becomes increasingly significant as a competitive advantage.

Table V.5
LARGEST CONSUMERS IN LATIN AMERICA, 2004

Country	Beer market (Millions of hectolitres)	Per capita consumption (Litres)
Brazil	84.5	47
Mexico	54.8	52
Venezuela (Bolivarian Republic of)	14.8	57
Colombia	14.0	31
Argentina	13.2	34
Peru	6.4	24
Chile	4.3	27

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of AmBev 2004 Annual Report, São Paulo and FEMSA, “Presentación a inversionistas”, June 2005.

Companies have used a mixture of strategies, ranging from exports through licensing agreements to FDI (both acquisitions and greenfield investments), to meet the

challenge of conquering new geographical markets, in general, and Latin American ones, in particular. In some cases, these three forms of entry into foreign markets have been employed in succession, but for the most part, companies—TNCs and trans-Latins alike—have combined strategies not necessarily sequentially, but with one of these three forms of entry predominating or strategically more important than the others.

Beer exports to, from or within Latin America have not been very significant, except for Mexican brewers FEMSA Cerveza and Modelo, whose expansion towards the North American market was exports-based. TNCs have enjoyed little success in exporting beer to the region and most of the largest brands, such as Anheuser-Busch, Miller, Heineken, Carlsberg and others, have ventured into the Latin American market by way of licensing agreements or strategic alliances with local companies whereby, typically, the local partners produce and distribute the international brands in the national market, and sometimes regionally, as specialty or premium beers. These alliances have often been strengthened by the acquisition of minority stakes in the Latin American partner. Most of the trans-Latin brewers, facing more limited TNC competition than their counterparts in the soft drinks industry, became trans-Latins primarily by expanding through licensing and by acquiring and controlling other Latin American firms. This strategy has been employed by the larger brewers based in Argentina (Quilmes), Brazil (AmBev), and Colombia (Bavaria). However, the last decade has witnessed huge growth in FDI, especially by way of mergers and acquisitions, which has radically altered the configuration of the beer map in Latin America and the Caribbean.

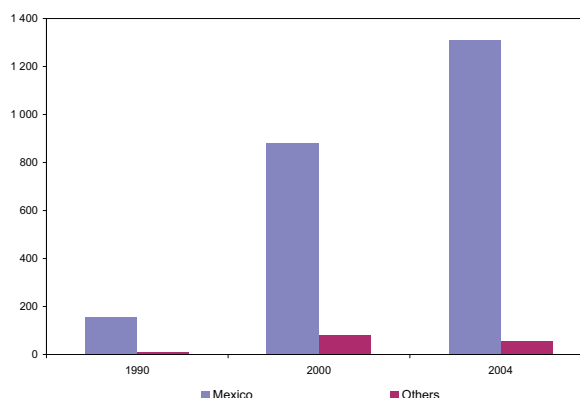
There follows an analysis of these three modalities of internationalization—exports, licensing and FDI—undertaken by the largest companies in the Latin American beer industry. Each of the three subsections below provides an analysis of the internationalization experiences of specific trans-Latins.

(a) Exports

Globally, exports from the main European brewing countries, and to a lesser degree from the United States, increased substantially from 1990 onwards but were never the principal modality of international expansion for the major TNC brewers. Exceptionally, Mexican brewers FEMSA Cerveza and Modelo, took a different route, using exports as the main basis on which to internationalize their Sol and Corona brands into the North American market. In 2004, United States and European beer exports to Latin America and the Caribbean were equivalent to less than 8% of the trade value of Mexican beer exports to the

United States alone, which represented over US\$ 1.1 billion (United Nations, w/d). Exports from other Latin American and Caribbean countries, however, were negligible (see figure V.5). Recently, with the global launch of the Brazilian Brahma brand by the InBev group, Brazilian beer exports jumped from US\$ 12.6 million in 2004 to US\$ 28.4 million in 2005 (AliceWeb, 2006), which is very significant for Brazil but still far below the volume of exports by Modelo or FEMSA Cerveza. Beer is exported from Latin America by other companies, including Quilmes and CCU (mostly within the Southern Cone), Bavaria and Polar, but these exports represent small fractions of the companies' sales and target markets and pale in comparison to the volume of Mexico's beer exports. Modelo and FEMSA Cerveza are the region's most significant exponents of the export modality of internationalization.

Figure V.5
BEER EXPORTS FROM LATIN AMERICA AND THE CARIBBEAN
(Millions of dollars)



Source: United Nations, "Commodity Trade Database (COMTRADE)", Statistics Division.

Modelo was established in 1922 in Mexico and grew into a conglomerate of over 150 companies encompassing packaging, malt, real estate, transportation and other services, as well as seven breweries. The company had exported marginal amounts since the 1930s (with the end of the Prohibition in the United States) and much greater volumes from the late 1970s onward. Its international expansion began in the southwestern United States, where its marketing campaign associated the Corona brand with United States tourists' memories of sun and sand during their vacations on Mexican beaches. In 1993, the United States-based TNC brewer Anheuser-Busch recognized this competitive advantage and invested in Modelo, acquiring a 17.7% equity interest, which it built up over the years to its current 50.2%. Between 1993 and 2000 Anheuser invested more than US\$ 1.8 billion in Modelo equity, the value of which more than doubled to US\$ 4.4 billion. The Corona brand has become the top-selling imported beer in the United States. Although management control

has apparently remained in the hands of five Mexican families, 10 of the Modelo group's 21 board directors are from Anheuser-Busch (Scheinman, 2004a). The first of the beer trans-Latins is, therefore, tied to a TNC through this very significant ownership share.

Modelo's other main competitive advantage for Anheuser-Busch was the potential of the Mexican market. The two companies complemented each other, since Modelo enjoyed economies of scale and competitive advantages in Mexico similar to those of Anheuser-Busch in the United

States (Scheinman, 2004b). For Modelo, the partnership with the owners of the Budweiser brand helped it to meet the challenges of globalization and to take advantage of the North American Free Trade Agreement (NAFTA), which was then under negotiation. Ironically enough, however, Anheuser-Busch did not acquire distribution rights for Modelo's brands in the United States, and the success of these in the North American market eventually caused friction with the Anheuser-Busch bottlers, which were hungry for a share of Modelo's success (see box V.4).

Box V.4

ANHEUSER-BUSCH'S MEXICAN BEER DILEMMA

The relationships between brewers and their distributors are much less monolithic than they might sometimes appear and this can lead to strategic dilemmas as brewers expand their influence over other companies. Since it owns over 50% of Modelo, it could be expected that Anheuser-Busch would promote the Corona brand energetically in the United States. Preexisting contracts, however, prevent Corona from being carried

by Anheuser-Busch distributors. With the brand's fast growth in the United States, Anheuser-Busch distributors began to put pressure on the company to bring Corona into their portfolio, which would have required a costly contract buyout. Instead, the company attempted to adapt by introducing other "Mexican-inspired" beers, such as Azteca in California, Tequiza in New York and the south-west and Rio

Cristal in southern Florida and Virginia. Serious promotion of these products would have harmed Anheuser-Busch's Corona business, however. Modelo has expressed an intention to either acquire the company that manages the distribution of its Corona brand in the United States or end the contract. This decision led to an arbitration process that remained unresolved in January 2006.

Source: Kotler Marketing Group, 2000 and *Modern Brewery Age*, "Gambrinus and Modelo maneuvering for advantage", 7 February 2005.

During the period 1998-2005 Modelo turned in an impressive performance. Net revenues from its seven breweries more than doubled. The major contributors to this growth were surging exports and increased domestic demand, coupled with efficiency gains (yield per hectolitre averaged over US\$ 80). By 2004, 28.6% of sales corresponded to export markets, with the overwhelming majority coming from Mexico's NAFTA partners, the United States and Canada, where Modelo's beer was sold at premium import prices. In contrast to Mexico's almost non-existent market for imported brands, these labels accounted for around 12% of the United States market in 2003. It was precisely this import segment that grew fastest in the United States, particularly among well-heeled consumers who preferred foreign beers for their cachet and superior taste. Another factor was the huge influx of Mexicans to the United States, which further fuelled Modelo's growth in that market (Scheinman, 2004b). Corona now sells approximately 50% more than Heineken in the United States, which it overtook in 1997 as the number one imported beer.

FEMSA Cerveza is the beer subsidiary of the FEMSA group. Together with the group's soft drinks subsidiary (Coca-Cola FEMSA), FEMSA is the largest Latin American beverage company. It is, however, still second to Modelo in beer sales and beer exports. This situation is nevertheless changing fast, due to two factors. The first

is that FEMSA Cerveza is gaining on Modelo thanks to an agreement with Heineken allowing it to distribute its Sol, Dos Equis and Tecate brands in the United States market (*Business Week*, 2005). The second is recent its FDI ventures in Brazil. Both factors demonstrate FEMSA Cerveza's renewed interest in complementing its export initiatives with licensing and FDI arrangements, in terms of its internationalization modalities.

FEMSA Cerveza was obliged to shift its corporate strategy because it was not achieving the performance outcomes it expected. From 1994 to 2004 it was associated with the Canadian TNC brewer Labatt, which owned 30% of its stock. Operationally, this partnership combined Labatt and FEMSA beer import businesses in the United States to form the second largest specialty beer company there, Labatt USA, in which Labatt held 70% and FEMSA Cerveza the other 30%. This relationship was stretched to breaking point when the Brazilian brewer AmBev acquired Labatt as part of the transactions leading up to Interbrew's acquisition of AmBev. By that time, relations between FEMSA Cerveza and Interbrew were already conflictive because of Interbrew's attempt to sell its Beck's brand in the United States through the Labatt/FEMSA Cerveza joint venture, without first obtaining the consent of FEMSA Cerveza, which considered that this arrangement would harm the sale of its own brands (Scheinman, 2004b). As a result, Labatt sold its 30%

stake in FEMSA Cerveza in August 2004 and FEMSA Cerveza entered into the agreement with Heineken to distribute Sol, Dos Equis and Tecate in the United States. In what has been viewed as the first move in an emerging beer war between FEMSA Cerveza and InBev, in 2006, FEMSA Cerveza began an FDI-based internationalization process by acquiring Kaiser in Brazil, while maintaining its export-based strategy for the North American market (*America economía*, 2006).

As a result of these transactions, FEMSA Cerveza is now the only trans-Latin brewer that does not have foreign shareholders, though this does not signify that the FEMSA group is independent of the leading TNCs in the beverage industry. Its agreement with Heineken is central to its export-based internationalization strategy in the beer industry. Furthermore, its connection with the Coca-Cola soft drink system, by way of Coca-Cola FEMSA, is crucial to its soft drink network in Latin America. This gives further weight to the assertion that the trans-Latins in the beverage industry are, without exception, associated with transnational corporations.

In summary, among the trans-Latins, exports-based internationalization has been a significant strategy only for two Mexican brewers, Modelo and FEMSA Cerveza. Unlike other trans-Latin brewers, these Mexican firms enjoy geographical proximity and preferential access to the North American market, where they can also build on their cultural affinity with Mexican Americans. A distinctive trait that helps these brands to internationalize through exports is that they occupy a specific niche in the North American market, consisting of United States tourists who have visited Mexico. The great majority of the other TNC brewers and trans-Latins have preferred to establish production facilities in the different markets, either through licensing arrangements or through FDI.

(b) Licensing agreements

Licensing agreements are the principal instrument by which TNC brewers have entered new markets. This modality allows them to establish relatively small scale operations and benefit from partnerships with national, regional or transnational brewers who have built up distribution networks and local knowledge. Globally, licensing agreements form an extensive network of contractual arrangements that tie the major TNC players together (see table V.6). In some cases, these agreements

involve brewing, marketing and distributing; in others, they are confined to the distribution and marketing of imported products.

Licensing agreements among TNC brewers are common in traditional markets. For example, Anheuser-Busch brews Kirin Ichiban in California while Kirin brews both Heineken and Anheuser-Busch brands in Japan; Anheuser-Busch brands are brewed by Carlsberg in Denmark and by Guinness in Ireland; SABMiller bottles Kronenbourg in Italy and Carlsberg in the Canary Islands; and Miller distributes Fosters in the United States market. Licensing agreements with local producers became a common first incursion into emerging markets for TNC brewers, as was the case with the huge Chinese market in the 1990s. Many of these licensing agreements in emerging countries were originally coupled with the acquisition of equity, usually minority stakes; however, more recently, the TNC brewers have become more aggressive direct investors, either acquiring control of local brewers or establishing completely new plants in emerging markets, as the experience of Latin America and the Caribbean aptly demonstrates.

In the case of Brazil, the initial success of the macroeconomic stabilization programme known as the Real plan paved the way for a host of new licensing arrangements between different beer-producing TNCs and the leading national brewers, Brahma and Antarctica. In 1995, Miller Brewing Company and Brahma entered a joint venture to produce the Miller Genuine Draft brand locally. A year later, Carlsberg licensed its brand to Skol (a Brahma company) and Anheuser-Busch entered an agreement with Antarctica to produce and sell Anheuser-Busch brands locally.⁵ In 2002, Heineken licensed its brand to Kaiser, with whom it had a longstanding technology transfer partnership and in which it held a minority interest.

In the cases of Argentina and Chile, CCU became the key player for the licensing of foreign beer brands. It developed into a pivotal company for a number of TNC brewers that preferred to enter the South American market by way of licensing agreements. It became a rare example of a relatively independent, multi-brand, cross-border brewer. CCU quickly grew into Chile's largest brewer, with a domestic market share of close to 90%. Reflecting global trends in the beverages industry, CCU has diversified its activities not only into carbonated and non-carbonated non-alcoholic beverages but also into wine and *pisco* (grape liquor) and, more recently, confectionery and biscuits. Among brewers, CCU is nothing if not atypical (see box V.5).

⁵ This agreement ended with the AmBev merger in 1999, when Anheuser-Busch turned to the Chilean company Compañía Cervecerías Unidas S.A. (CCU) to produce its brands for the Southern Cone markets.

Table V.6
LICENSING AGREEMENTS BETWEEN LATIN AMERICA'S LARGEST BREWERS AND GLOBAL BREWERS

Licencees (brewers and/or distributors)								
	Inbev (including AmBev)	Anheuser-Busch	SABMiller	Heineken	Molson Coors	FEMSA	CCU	Quilmes
Licensors	Inbev							
	Anheuser-Busch	Anheuser-Busch brands are brewed by InBev companies Labatt and Oriental Breweries in Canada and South Korea. The company's agreement with Antarctica in Brazil came to an end in 1999, with the AmBev merger		Anheuser-Busch brands have been brewed in Italy by Heineken since 2003 ^a		CCU brews and sells Budweiser in Chile, Argentina, Paraguay and Brazil		
	SABMiller	AmBev distributes Miller in Brazil						
	Heineken	Heineken's Murphy's brand is distributed in the UK by InBev; Heineken and Diageo bought a 28.98% stake in InBev-controlled Namibian Breweries, which will now distribute Heineken as well as InBev brands		SAB brewed Amstel in South Africa (until 2005)	Molson Coors distributes Heineken in Canada. Heineken is distributed in Brazil by Kaiser, formerly a Molson Coors company	Kaiser (formerly Molson Coors) distributes Heineken in Brazil	CCU has distributed Heineken in Chile since 2003	Quilmes distributed Heineken in Argentina from the early 1980s up to 2002
	Molson Coors	Molson brewed for Miller in Canada		Heineken distributes Molson Coors brands in Europe	Coors/Molson alliance since 1985 to distribute Coors in Canada. Joint venture since 2001 to import, market, sell and distribute Molson brands in the United States	FEMSA distributes Coors Light in Mexico		
	Paulaner							CCU distributes Paulaner in Chile
	Guinness				Heineken brews Guinness in some Central American and Caribbean countries	CCU distributes Guinness in Chile and Argentina		
	Carlsberg	AmBev distributes Carlsberg in Brazil. Labatt distributes Carlsberg in the United States	Anheuser-Busch distributed Carlsberg in the United States from 1985 up to 1998					
Modelo							CCU imports Corona into Argentina	
FEMSA Cerveza				Heineken distributes FEMSA in the United States	FEMSA entered a licensing agreement with Kaiser, a Molson company, in 2004. Kaiser was subsequently acquired by FEMSA			

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the companies.

^a Peroni had brewed, packaged and distributed Budweiser in Italy since 1995, but the partnership ended when the company was acquired by SABMiller.

Box V.5

CCU: THE ATYPICAL TRANS-LATIN BREWER

CCU is quite exceptional within the Latin America beverage industry and its experience warrants closer examination. In the early 1990s, CCU entered an agreement to brew and distribute Paulaner beer (a brand of the German brewer Schörghuber) in Chile. In the mid-1990s, CCU invested directly in minority stakes in breweries in Croatia (Karlovacka Pivovara) and Peru (Backus & Johnston), which it subsequently sold. It then turned to Argentina, which possessed advantages in terms of geographical proximity, cultural affinity and size (the company estimated the Argentine market to be three times the size of the Chile's market at the time). The CCU move into Argentina was promising as a way of growing beyond the limits of the Chilean market from a well-grounded base in Chile. In the mid- to late 1990s, CCU acquired Compañía Industrial Cervecera S.A. de Salta, Cervecería Santa Fé S.A. and Cervecerías Córdoba in Argentina. CCU is now the second largest brewer

in Argentina after Quilmes, with a market share of approximately 15% (Feller-Rate, 2005). The distinguishing factor is that CCU focused on Argentina to brew both local and foreign brands, the latter under licensing agreements with TNCs (Heineken and Anheuser-Busch).

In 1995, in parallel to its first acquisition in Argentina, CCU reached an agreement with Guinness which gave it distribution rights over that brand in Chile and Argentina. The same year, Anheuser-Busch entered an agreement with CCU to produce and sell its brands through the CCU Argentina subsidiary. With the end of the agreement between Anheuser-Busch and Antarctica/AmBev in 2000 (see above), CCU began to export Budweiser from Argentina to Brazil, Paraguay and Chile and, in 2001, Anheuser-Busch acquired a 20% equity stake in the company. In 2001, a dispute between CCU and Heineken resulted in a court ruling that engendered a new arrangement among CCU, Heineken and

Schörghuber giving CCU exclusive brewing and distribution rights over the Heineken brand in Chile and Argentina. In response to this new agreement, Anheuser-Busch sold its 20% stake in CCU, but permitted CCU to continue brewing and distributing Budweiser in Chile and Argentina.

In effect, this rather singular internationalization process, which combined exporting from a host country, licensing arrangements and FDI, has resulted in CCU atypically brewing and distributing the global brands of rival TNC brewers—Anheuser-Busch, Guinness, Heineken and Carlsberg—in both Argentina and Chile, as well as other countries in the case of Anheuser-Busch, and thus establishing a niche within South America. In a similar fashion to the Chilean soft drinks trans-Latins, CCU has benefited from its strong financial base in Chile to expand into a larger market with higher risk but also better growth prospects, combining local brands with well-known global names.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of Feller-Rate, "Informe de clasificación: Compañía Cervecerías Unidas", Santiago, Chile, May 2005 and official information from Compañía Cervecerías Unidas (CCU).

The most obvious example of a trans-Latin brewer that has used licensing to expand internationally is the American Beverage Company, AmBev. In 2002, AmBev entered an agreement with Quilmes whereby the latter brewed and distributed AmBev's brands in Argentina, Chile, Bolivia, Paraguay and Uruguay, while AmBev retained the option of brewing and distributing Quilmes' brands in Brazil. In common with many of the licensing agreements seen in the industry, alongside this alliance AmBev acquired a minority equity shareholding in Quilmes. As will become apparent, this agreement was part of a more complex transaction that has to be viewed in the context of, first, AmBev's original internationalization process and, second, its current position as part of the Interbrew network. Similarly, in 2004 FEMSA Cerveza entered into a licensing agreement with Kaiser to produce Sol beer in Brazil (SEAE, 2004; Bloomberg, 2004), which must now be interpreted as part of a more ambitious internationalization strategy in the light of FEMSA Cerveza's acquisition of Kaiser in 2006.

As can be appreciated from this analysis, licensing is a widely used modality for TNC brewers entering the Latin American beer market. Licensing arrangements enabled several national brewers to expand and to enhance

their competitiveness enough to internationalize thereafter through FDI, and thus develop into trans-Latins.

(c) Foreign direct investment

Evidently, the internationalization processes of brewers in Latin America took place in a context of global consolidation of the beer industry. In 2002, the top ten brewers in the world represented 50% of global beer sales by volume; and 69% of output was generated in only eleven countries. Within a few years, the global beer industry had been transformed by major FDI flows in the form of acquisitions. South African Breweries (SAB) purchased the second largest United States-based TNC brewer, Miller, for US\$ 5.6 billion in 2002 and Italy's Peroni for nearly US\$ 800 million in 2003; and Heineken bought Austria's BBAG for US\$ 2.4 billion in 2003 (Scheinman, 2004b). By 2003, the eight largest brewers, led by Anheuser-Busch (United States), SABMiller (South Africa/United Kingdom), Heineken (Netherlands) and Interbrew (Belgium), accounted for 53% of world beer sales by volume. Subsequently, Interbrew acquired AmBev in 2004. Molson and Coors merged, also in 2004, and in 2005 SABMiller acquired Colombia's Bavaria. Whereas, until recently, it could safely

⁶ Based on estimated total beer sales of 1.484 billion hectoliters (Euromonitor International, 2005).

be said that the beer industry was much less concentrated than the carbonated soft drinks industry (in which the top five companies make one half of global sales), that difference is rapidly diminishing. Presently, the top five players hold approximately 43% of total sales in terms of volume (Euromonitor International, 2005).⁶ Table V.7 shows the main mergers and acquisitions in recent years in the beer industry. Latin America figures on this list through the acquisitions of AmBev and Bavaria, which are both consolidated trans-Latins with large international networks of their own.

Table V.7
MAIN MERGERS AND ACQUISITIONS IN THE BEER INDUSTRY,
2002-2005

Acquirer/ merging party	Acquired company/ merging party	Resulting corporation	Year	Value (US\$ billion)
South African Breweries	Miller Brewing (USA)	SABMiller	2002	5.6
Heineken (Netherlands)	BBAG (Austria)	--	2003	2.4
Molson (Canada)	Coors (United States)	Molson Coors	2004	3.4
Interbrew (Belgium)	Ambev (Brazil)	InBev	2004	11.0
SABMiller (United Kingdom)	Bavaria (Colombia)--		2005	7.8

Source: Prepared by the author on the basis of information provided by the companies.

This wave of acquisitions, which took place against a mosaic of worldwide licensing agreements, has generated a number of conflictive situations in the industry, with companies finding themselves party to agreements whose other partners that have been acquired by rival firms. Two global and two Latin American examples serve to illustrate this point. In Italy, Heineken ended its licensing agreement with Peroni when the latter was acquired by SABMiller. In Canada, Miller filed a suit against Molson Coors to end an agreement that allows Molson to brew and sell Miller brands there. When Molson and Coors merged, Miller saw there would be little incentive for the merged Molson Coors to promote Miller brands in Canada, since these would compete with the Coors brands. In Latin America, Labatt withdrew from FEMSA Cerveza, and Schorghüber left CCU, as noted earlier.

Three principal trans-Latins—Quilmes, AmBev and Bavaria—stand out among the largest foreign direct investors in the Latin American beer industry. FEMSA Cerveza's very recent acquisition in Brazil could make it a newcomer to this group. The internationalization patterns of these trans-Latin brewers is shown in figure V.6 and their development process is examined in the following section.

(i) *Quilmes: the Argentine beer industry leader*

Quilmes was established in the late nineteenth century and was officially registered in Paris, France. Originally, it imported barley produced in Argentina for the French and German beer industries. Throughout the twentieth century it expanded in Argentina, through both acquisitions and greenfield investments. Quilmes now controls 64.5% of the Argentine beer market, even after losing a few percentage points of its market share to imported beers. Part of the company's success is attributable to its capacity to interpret consumer tastes and expectations, which has been crucial to its ventures outside Argentina, as well as its solid, broad distribution network based on its own agents in large urban areas, its independent distributors in other parts of the country and its significant degree of vertical integration (for example, the company still produces basic inputs, such as barley).

From the early 1980s up until 2003, Heineken held a 15% stake in Quilmes, which it sold after Quilmes entered into a strategic alliance with AmBev in 2002. This alliance gave Quilmes licensing rights over production and distribution of AmBev brands in Argentina, Bolivia, Chile, Paraguay and Uruguay, as well as the possibility of having AmBev distribute its own brands in Brazil (which has not taken place to date). AmBev transferred control over its plants in Argentina, Bolivia, Uruguay and Paraguay to Quilmes, in exchange for 36.09% of Quilmes' shares.

As a minority stakeholder in Quilmes, Heineken opposed this transaction, which imposed upon it a sudden partner (in the Quilmes venture) who was a direct rival to its expansion plans in Latin America. Heineken sold its stakes in Quilmes to AmBev (which now holds 50.4% of the company) and turned to Chile where it acquired 50% of the firm that controls Chilean beverage company CCU, which is also the second largest brewer in Argentina (see above). For Quilmes, this meant the loss of the Heineken brand and the need to redesign its business model accordingly.

Quilmes stands out among the region's beer-making trans-Latins (and among trans-Latins in general) in that it started investing outside Argentina more than 70 years ago. Foreign direct investments began with plants in Paraguay in 1932, followed by others in Uruguay in 1965. These investments took advantage of the proximity and similarity of the Paraguayan and Uruguayan markets to Argentina's. Today Quilmes has market shares of approximately 95% and 98%, respectively, in these two countries. In 1991, Quilmes acquired a plant in Chile, on the assumption that market similarities would yield the same success it had enjoyed in

Paraguay and Uruguay; however, the results were not as favourable as expected and by 2004 Quilmes had only 11% of the market, despite having held the licence for Heineken. In 1996, the company invested in two breweries in Bolivia and in 2000 it acquired control of Cervecería Boliviana Nacional (CBN), a market leader, which gave it a total market share of 98%. This strong grip on Southern Cone markets represented a significant competitive advantage from the standpoint of its strategic alliance with Ambev, by means of which Quilmes is also expanding its sales in the Chilean market through the Brahma brand.

Figure V.6
THE INTERNATIONALIZATION OF THE TRANS-LATIN BREWERS



Source: Economic Commission for Latin America and the Caribbean (ECLAC).

Quilmes' international expansion has thus been based on FDI, which has resulted in control of its target markets in the Southern Cone, with the exception of Chile. Its international presence was strengthened through the alliance with AmBev, which transferred its assets in these countries to Quilmes, along with licences to brew and distribute its key products. Interbrew's acquisition of AmBev brought Quilmes into the InBev network, however,

so it can now no longer be considered an emerging Latin American TNC.

(ii) *AmBev: the Latin American heavyweight brewer*

Brahma and Antarctica, the forerunners of AmBev, had both beer and soft drinks operations before their merger. Their beer exports from their Brazilian base were of marginal importance. In terms of FDI, Brahma had made certain investments in Argentina (Compañía Cervecería Brahma Argentina and Maltería Pampa) and Bolivarian Republic of Venezuela (Compañía Cervecería Nacional); however, the real momentum came with the merger with Antarctica in 1999. The new entity controlled over 70% of the domestic beer market, which generated a response from the Brazilian competition authorities,⁷ particularly with respect to its Bavaria brand.

Stronger efforts to internationalize the business and develop AmBev into a transnational corporation began after the merger. AmBev's outward expansion began in the Southern Cone market with two operations in Uruguay in 2000. In one of these, a joint venture with Danone, AmBev acquired controlling stakes in Salus, a brewer and mineral water market leader in Uruguay. In the other, AmBev bought 95.4% of the Uruguayan brewer Cervecería y Maltería Paysandú S.A. (Cympay). The following year, the company acquired the Paraguayan firm Cervecería Internacional, the producer of the Krone brand and distributor of Brahma and Ouro Fino, which are imported from Brazil and Argentina, respectively (Wilkinson, 2004a). To consolidate its position in the Southern Cone market, AmBev entered the strategic alliance with Quilmes in 2002, as noted above.

AmBev then turned to Central America. In 2002, it entered a joint venture with Central American Bottling Corporation (CabCorp), PepsiCo's anchor bottler in Central America, to produce and distribute beer in Guatemala and other Central American countries. One of CabCorp's most appealing assets for AmBev was its vast distribution network for soft drinks in the region (Wilkinson, 2004a). In 2004, AmBev acquired 51% of Embotelladora Dominicana (Embodom), the leading soft drinks (PepsiCo) bottler in the Dominican Republic, with plans for building a new brewery.

Soon thereafter, in 2003, AmBev set its sights on the Andean region. It began building a plant in Peru and acquired assets belonging to Embotelladora Rivera, taking over the PepsiCo distribution franchise in the north of Peru and Lima and two industrial units. A direct distribution system was established in Peru in 2004. It also acquired 80% of Ecuador's

⁷ AmBev had to divest its Bavaria brand and provide open access to its distribution network for at least one small brewer in each of five regions of Brazil, as well as the company (Molson) that acquired the Bavaria brand in 2000 (Wilkinson, 2004a).

second largest brewer, Cervecería Suramericana. In common with other trans-Latins, AmBev has encountered bureaucratic hurdles to its internationalization in Latin America, in the form of local regulations (see box V.6).

Lastly, in 2004, AmBev acquired Labatt Brewing Company Ltd, one of Canada's two leading brewers, with eight breweries in Canada and the Budweiser licence there, as well as a large import operation in the United States in partnership with FEMSA Cerveza (which was subsequently dismantled). Labatt was part of Interbrew and this transaction must be viewed in the context of the Interbrew's acquisition of AmBev. This provided Ambev with a 42% share of the Canadian market (Labatt's 2003 share), which was second only to Molson's 44%, as well as a tariff-free export platform to the United States, and access to cheaper capital (Wilkinson, 2004b).

Having established itself as a solid regional player with dominant market shares in the Southern Cone and promising operations in the other subregions, Ambev was an attractive takeover target for expanding TNC brewers in the context of the industry's global consolidation. On 3 March 2004, Interbrew (Belgium) and Ambev (Brazil), the world's fourth and sixth largest brewers, respectively, announced their intention to combine forces. The agreement entailed a complicated swap of equity and debt and was referred to in the media as a merger; financially, however, it may be argued that it was effectively a takeover of AmBev by Interbrew,⁸ since JP Morgan, one of two investment banks hired by Ambev to evaluate the transaction, revealed on 29 March 2004 that AmBev had agreed to cede 57% of its economic capital to Interbrew (Wilkinson, 2004b). The beer industry's largest trans-Latin was now part of a global TNC brewer.

Box V.6

THE BOTTLENECK IN PERU, MEXICO AND BOLIVARIAN REPUBLIC OF VENEZUELA

Access to bottles can be a significant barrier to the entry of new competitors to a market. Beer has traditionally been distributed in Peru in amber-coloured 620 millilitre bottles. When AmBev moved into the Peruvian market in 2004, it intended to use similar bottles to launch its Brahma brand, and imported bottles from Ecuador. In a series of decisions, INDECOPI, Peru's consumer protection and intellectual property rights agency, arrived at different rulings regarding brand ownership rights over this type of bottle held by Backus & Johnston's, the country's largest brewer. Although the latest ruling favors AmBev, a number of court decisions, some of

them unappealable, prevent AmBev from using the traditional bottles, thus raising its entry costs in the Peruvian market. With Backus & Johnston's integration into the SABMiller system (resulting from the acquisition of its controller, Bavaria, by the South African company), a negotiated solution may follow.

Mexico's beer market is dominated by giants FEMSA and Modelo. Peruvian beverages company Ajegroup, which has already gained a 5% share of the cola market in Mexico, has plans to launch its Big Chela beer there in 2006, thereby contesting the long-standing duopoly. In what has been interpreted as a protectionist measure,

Mexico's Congress passed a law setting lower taxes for beer sold in returnable bottles than for beer sold in cans and disposable bottles. This will tend to raise entry costs since new brewers must either pay higher taxes or invest in complex bottle distribution and collection systems.

In the Bolivarian Republic of Venezuela, the dispute over bottles involves established brewers Cervecería Regional (Cisneros group) and Cervecería Polar. In 2002, the two companies lodged mutual accusations of bottle retention and destruction. The competition authority, Procompetencia, prohibited each company's distributors from collecting or receiving competitors' bottles.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of *The Economist*, "AmBev's combative Peruvian market entry", 19 December 2005 and "Regulatory watch: AmBev's sobering venture in Peru", 4 July 2005; *Business Latin America*, "Food, beverages, tobacco – Mexico", 5 December 2005 and *Producto*, "Polar-Cisneros, guerra sin fronteras", November 2002.

(iii) Bavaria: the Andean beer leader

Bavaria is Colombia's largest brewer (with over 90% of the market) and beverage company. Its beer brands include Cerveza Águila, Costeña, Cerveza Clara Pilsen, Poker, Club Colombia, Cerveza Águila Light, Águila Imperial, Leona Cerveza and Cerveza Bahía. The Águila, Cristal, Pilsener and Atlas brands are leaders in many Andean countries, including Colombia, Peru, Ecuador and Panama.

Bavaria began internationalizing in the early 1980s, focusing first on the Andean region and later on Central America. In 1982, Bavaria acquired an equity stake in Compañía de Cervezas Nacionales S.A. (CCN) and Cervecería Andina in Ecuador. Its upped its equity share in these two companies in 2002 and 2004, respectively. Almost another decade elapsed before Bavaria's next major acquisition, which was Panama's largest brewing company, Cervecería Nacional S.A. Between 2002 and 2004, it acquired 74.9% of the voting rights (and 39.9%

⁸ One of the aspects of the transaction that set it apart from a straightforward acquisition, however, is the fact that several of AmBev's executives took on key positions within the merged entity, Inbev, in what has been referred to as a "reverse takeover". As of 1 January 2006, former AmBev staff occupied the positions of Chief Executive Officer (to which Carlos Brito was appointed in December 2005), Chief Financial Officer, Chief Information and Services Officer, Zone President for Latin America and Chief Buying Officer (www.inbev.com).

of the total equity) of Backus & Johnston, Peru's largest beverage company. Bavaria spent almost US\$ 1.5 billion on its acquisitions in Panama and Peru.

As a result of this process, Bavaria secured the beer markets on the Pacific coast of South America, with the exception of Chile (Beverage World, 2004). In 2005, it controlled 83% of the market in Panama, with Heineken as its main competitor, and 92.4% in Ecuador, where InBev is its strongest rival (Bavaria, 2005). In Peru, it controls approximately 90% of the market through Backus & Johnston.

In 2005, Bavaria was bought by SABMiller for US\$ 7.8 billion. Bavaria's attractiveness to SABMiller lay in its regional presence, as well as its recent strategy of portfolio expansion through product differentiation and differential pricing strategies for different market segments. Analysts have interpreted SABMiller's move as necessary to ensure the group's position in Latin America—it had invested in El Salvador and Honduras—in view of its rivalry with the InBev bloc. Like AmBev, Bavaria had expanded aggressively within the region, taking advantage of its strong domestic position, neighbouring country market similarities and, where possible, synergies in its soft drink distribution networks. Also like AmBev, it is now part of a global TNC brewing company.

(iv) FEMSA Cerveza: beginning to internationalize its business

As noted earlier, FEMSA Cerveza has only recently embarked upon an internationalization process beyond exports and licensing. In January 2006, it paid Molson Coors US\$ 68 million for 68% of Brazilian brewer Kaiser, which owns the Kaiser and the Bavaria brands (unrelated to the Colombian brewer Bavaria) (Valor, 2006). Compared to the internationalization of Quilmes, AmBev and Bavaria, the acquisition of Kaiser is relatively small; nevertheless, it does bring FEMSA into the category of a trans-Latin beer producer, as opposed to a mere exporter, and it makes FEMSA Cerveza the only company with substantial brewing interests in both Mexico and Brazil. Most notably, after the recent TNC acquisitions of existing trans-Latins, FEMSA Cerveza is the only trans-Latin brewer not controlled by a TNC, even though Heineken and Molson Coors still possesses equity stakes (17% and 15%, respectively) in Kaiser.

Kaiser had a long experience with foreign investors. It had started out in the early 1980s in association with Coca-Cola bottlers in the state of Minas Gerais. Coca-Cola held a 10% stake in the company until 2002. Heineken also acquired a 10% stake in 1983, which it gradually increased to 20%, before licensing the Heineken brand to Kaiser in 2002. Its share later fell back to 17%

after Kaiser's acquisition by FEMSA Cerveza. Molson acquired the Bavaria brand in Brazil in 2000 as a result of restrictions imposed on the AmBev merger. In March 2002 it gained control of Kaiser (80%) for US\$ 765 million. It united the two brands under Kaiser, with Heineken maintaining a 20% share. Molson's experience in the Brazilian market was sobering in that it acquired the Bavaria and Kaiser brands with market shares of over 8% and 14%, respectively, which dropped precipitously to a combined market share of 8.7% by December 2006 (Valor, 2006). Pressure to sell Kaiser mounted after the Molson Coors merger. Its poor performance was reflected in the sale price, which was less than 10% of the amount Molson had paid for Kaiser alone (without Bavaria) in 2002 (although it entailed the transfer of a large volume of debt and other potential liabilities).

FEMSA Cerveza was a natural candidate to buy Kaiser, since it was a brewer with strong brands but as yet very little presence in the Latin American market outside Mexico. As well, it was Heineken's partner in the United States and intrinsically tied into the Coca-Cola system, both as the owner of a sizeable share of Coca-Cola's Brazilian distribution network and through the Coca-Cola FEMSA subsidiary. FEMSA Cerveza filled a vacuum left by a TNC brewer that was clearly unsuccessful in its Latin American venture and it remains to be seen whether its know-how on beer distribution in developing country settings and, more importantly, its links with Coca-Cola will be able to turn around Kaiser's market shares. Success in this venture would leave FEMSA Cerveza well structured, because it would encompass substantial export sales in the traditional North American market, which offers low growth but high volume and stability, a solid base in the Mexican market, where there is still room for expansion in per capita beer consumption, and a foothold in the region's other large market, Brazil. It combines different kinds of TNC partnership arrangements: a distribution agreement with Heineken in the United States, shareholdings in Kaiser and the link with Coca-Cola through the FEMSA group's soft drinks subsidiary. It is one of the few remaining trans-Latins in the brewing industry.

In summary, the internationalization of the beer industry in Latin America and the Caribbean has to be seen in the context of changing consumption patterns, the consolidation of the global market and the interactions between regional and transnational players. Unlike what occurred in the soft drinks segment, TNCs came late into the brewing industry in Latin America and the Caribbean and local brands therefore still account for the bulk of beer consumption in the region. In this setting, a small group of large trans-Latin brewers, all of which had some sort of significant alliance with transnational groups, were built up through corporate strategies based

on a combination of exports, licensing agreements and FDI. The transnational corporations' were involved first through licensing agreements with established local and regional firms. More recently, however, global TNCs, such as Anheuser-Busch, Interbrew and SAB Miller have acquired majority stakes in (or control of) such regional heavyweights as Modelo, AmBev, Quilmes and Bavaria and have thus established a direct presence in the mass-consumption beer market in Latin America and the

Caribbean. With the exception of FEMSA Cerveza, which is just beginning to internationalize its business through FDI, and CCU, which represents a very particular and unique case, the trans-Latin brewers as such have now died out, since they are all now part of world-leading TNC brewer networks. The relative independence of the beer trans-Latins in the internationalization process, as compared with the soft drinks companies, has come to an end.

C. Trans-latins in the food industry

Within the context of the transformation that has come about in the food industry, in which TNCs have broadened their product mix as they expand internationally, the successful trans-Latins (see table V.8) have used their strong domestic-market positions as a base to secure tranches of niche markets. Like the beer-producing trans-Latins, these firms started out independently and have increasingly important partnerships with food industry TNCs, although they have maintained greater independence.

The Mexican producers of traditional products such as bread and biscuits (Bimbo) or typically Mexican foods (tortillas, among others, made by Gruma, Alfa and Desc) are prominent examples. Like the Mexican brewers, these companies have tapped into demand for Mexican food products among Mexican immigrants in the United States in order to gain a foothold in the market there, from where they have expanded into other markets. Apart from producers of Mexican food products, the industry's

Table V.8
TRANS-LATINS IN THE FOOD INDUSTRY

Company	Country of origin	Sales (Millions of dollars)	Regions in which the company has foreign operations ^a				
			NA	LAC	EU	AS	OT
1 Bimbo	Mexico	4 623	X	X	X		
2 Gruma	Mexico	2 242	X	X	X	X	
3 Grupo Alfa	Mexico	1 220	X	X	X		
4 Arcor	Argentina	929		X			
5 Grupo Desc (Food Division)	Mexico	395	X				

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the corporate websites and *América economía* magazine.

^a NA: North America (United States and Canada), LAC: Latin America and the Caribbean, EU: Europe, AS: Asia, OT: Others.

trans-Latins include Arcor, which is a large regional player and a worldwide exporter of confectionery and chocolate, which it produces mainly in MERCOSUR. The following sections describe the experiences of Bimbo, Gruma, and Arcor.

1. Bimbo: the packaged bread leader in the Americas

Bimbo is a major bread producer in a very fragmented industry. It has positioned itself among the world leaders in terms of sales, production volume, and brands (see figure V.7). It is Mexico's largest food company, producing a broad range of goods including bread, biscuits, maize and wheat tortillas, confectionery, chocolate, and processed food. In the 1960s and 1970s, Bimbo expanded within Mexico and built up brand recognition of its principal makes: *Bimbo* and

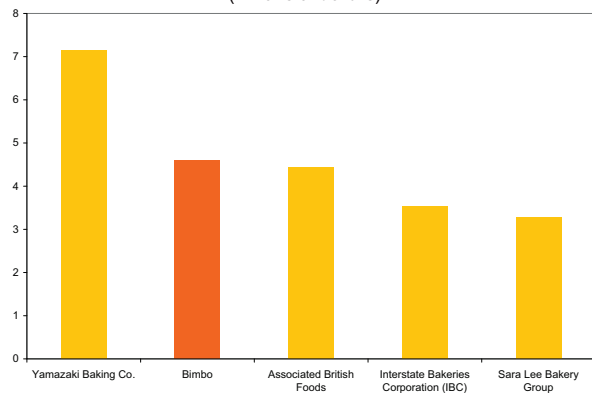
Marinela. In the 1980s it began to internationalize, first by exporting and soon after by opening production plants in the United States. In the 1990s, Bimbo began a rapid process of parallel expansion in the United States, which now accounts for 30% of its sales, and in the Central and South American markets.

Bimbo began its exports to the United States using a two-pronged strategy: (i) to meet demand among Mexican immigrants; and (ii) to raise entry barriers to potential

United States competitors aiming to enter the Mexican market. In the 1990s, the company decided to establish productive capacity of its own in the United States, rather than relying solely on exports, and embarked upon an aggressive strategy of buying ailing firms, mainly in the States of Texas and California, which are home to nearly half of the Hispanics living in the United States. The company spent nearly US\$ 1 billion on these acquisitions. Between 1994 and 1999, the most prominent acquisitions were Fabila Foods, C&C Bakery, Pacific Pride, Mrs. Baird's (the leading company in Texas) and Four-S Baking of California, all which were consolidated under Bimbo Bakeries USA. The company thus rapidly gained a leading position in the segments of packaged bread and maize and wheat tortillas in the regions that were closest to the border and had the largest Latin American immigrant population.

In 2002, Bimbo acquired the bakery operations of the Canadian company George Weston Ltd in the west of the United States, at a cost of US\$ 630 million. The assets complemented Bimbo's operations well, especially given their location in California and Texas. This operation gave Bimbo access to leading brands and products in the United States market, such as Oroweat, Entenmann's, Thomas' and Boboli, as well as five plants in Texas, Colorado, California and Oregon. This acquisition doubled Bimbo's United States subsidiary in size, making it the country's third largest baked goods company after Interstate Bakeries Corporation (IBC) and Sara Lee Bakery, the biggest food company in the world (see figure V.7).

Figure V.7
**WORLD'S LARGEST BAKED GOODS PRODUCERS,
 BY SALES, 2004**
(Billions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the companies.

The complex restructuring undertaken in the wake of this acquisition took place in a difficult context, including a drop in consumption as consumer patterns were influenced by low-carbohydrate diet trends, among other factors. Like other companies, Bimbo recorded losses in several segments. The company responded by creating a more efficient information system to monitor inventory, delivery of fresh produce and the collection of past-fresh bread from retailers to reuse in other products. Bimbo also introduced new products that were richer in fibre and lower in calories, to adapt to the new demand patterns in the United States market.

These shifts in business strategy and new product lines enabled Bimbo to extend its internationalization process to other countries in Central and South America. In 1990, it acquired a bread producer in Guatemala, thus creating Bimbo Central America. This opened the doors to new markets in this subregion and the company soon established plants in Costa Rica and El Salvador and distribution centres in Honduras and Nicaragua. Between 1992 and 1995, Bimbo expanded in Latin America by combining acquisitions, such as Ideal in Chile and Panificador Holsum in the Bolivarian Republic of Venezuela, with the construction of new plants in Argentina. In the second half of the decade, the company continued its expansion into Colombia and Peru, in both cases through alliances with large local food companies, Alimentos Noel and Alicorp, respectively. In 2000, Bimbo entered Brazil via the acquisition of Plus Vita, one of the country's largest packaged bread producers, for US\$ 64 million. In 2005, Bimbo bought 30% of Alimentos Fargo, an Argentine business that controlled close to 50% of the packaged bread market there. Bimbo has thus acquired leading market shares of 87% in Peru, 86% in Costa Rica, 77% in the Bolivarian Republic of Venezuela and 71% in Chile.

With solid footholds in both the United States and Latin America, Bimbo recently began to expand into Europe, with the acquisition of a company in Ostrava, Czech Republic, where it has built on the opportunities arising from the increasing penetration of packaged bread and the still fragmented industry structure.

In summary, little more than a decade into its ambitious expansion scheme, Bimbo has established a solid presence in the United States and in Latin America's main markets. In an industry that is undergoing significant transformation, leading to the decline of many large and consolidated players, Bimbo has responded successfully by adapting its product mix and improving production and distribution processes.

2. Gruma: the tortilla king

Gruma S.A. de C.V. is one of the world's main producers of maize flour and tortillas. After consolidating a strong position in the Mexican market (with a market share of over 70%), Gruma, like Bimbo, looked for opportunities elsewhere. It too began with the culturally similar markets of Central America and Hispanic immigrants in the United States. More recently, Gruma has built its expansion on the growing popularity of Mexican food, particularly tortillas.

Gruma began expanding internationally in the early 1970s, when it set up a plant in Costa Rica. It later invested in other Central American countries. It moved into Honduras in 1987 and El Salvador and Guatemala in 1993. By 2004, its Central American business represented 5% of Gruma's total sales. The acquisition of two more companies in the Bolivarian Republic of Venezuela gave the company a leading position there.

Gruma entered the United States in 1977, focusing much of its effort on this market thereafter. Attracted by the size of the Hispanic market, Gruma started up in the United States by acquiring, modernizing and vertically integrating traditional tortilla producers. The company established operations to buy maize, produce maize flour, develop products, machinery and brands, and actually make the produce. It also set up an extensive distribution network. The United States market was fragmented and under-explored when Gruma started up there, but the firm's favourable outturn aroused the interest of other businesses. American companies Archer-Daniels-Midland (ADM), ConAgra Foods Inc. and Cargill, as well as Minso of Mexico, soon entered the maize flour market. Similar developments occurred in the tortilla segment, with the arrival of American companies Tyson Foods Inc., General Mills, Fiesta Foods and, more recently, Bimbo, as noted above.

In 1996, in response to this mounting competition and to strengthen its presence in the United States market, Gruma entered a partnership with ADM, one of the world's largest food companies, specializing in maize refining, processing maize oil, and producing wheat flour (see table V.1). This joint venture brought Gruma into the wheat flour market in Mexico and gave it some of the ADM operations in the United States, while ADM received 22% of Gruma's shares and 20% of Gruma's United States maize flour business. The partnership enabled both companies to exploit changing—and converging—consumption patterns in the two countries. Between 2000 and 2004, sales in the United States market increased at an average annual rate of 9%. Today Gruma has six maize flour production plants in Texas, Indiana, Kentucky and California, in addition

to 13 plants producing tortillas and other products in the west and south-east of the United States.

At the same time as it was building up its presence in the United States and Central America, Gruma also entered the maize flour market in the Bolivarian Republic of Venezuela. Between 1993 and 1994, Gruma bought a 50% stake in Derivados de Maíz Seleccionados, C.A. (DEMASECA). In 1999, it acquired Molinos Nacionales, C.A. (MONACA) for US\$ 94 million. Gruma's current operations in the Bolivarian Republic of Venezuela—five plants producing maize flour, four producing wheat flour and four others processing rice and oats—have transformed the company into the second largest producer of maize and wheat flour in the world and contribute 14% of its total consolidated sales.

Encouraged by its experience in North America, Gruma began to envision its growth prospects on a global scale, including more distant and culturally different markets. In 2000, through its American branch, Gruma opened a plant in the United Kingdom, as a stepping stone to the European market. In 2004, it undertook two new European acquisitions: Ovis Boske, a tortilla plant in Holland, and 51% of Nouva De Franceschi & Figlu, an Italian maize flour company. With increased productive capacity in Europe, Gruma began to supply other markets there, including Germany, France and Poland, as well as Scandinavian countries, among others. Gruma's United States and European operations now represent close to 51% of its total consolidated sales.

In parallel with its international expansion, the company sought to diversify its product range by moving into wheat-flour-based goods. In 1998, Gruma entered the bread market through the Breddy brand in the north of Mexico. The results fell short of expectations, however, and the company decided to concentrate on activities with greater growth prospects. In 2001, Gruma sold its bread producing interests in Mexico, the United States and Costa Rica to the trans-Latin Bimbo (see above) for US\$ 70 million. At the same time, it began to prepare the next step of its international expansion, Asia.

First, Gruma began to export maize flour to Asia, principally to the Republic of Korea and Indonesia, for the production of nachos and wheat tortillas, which were in high demand in these countries. Shortly thereafter, capitalizing on the growing international popularity of Mexican food, the company moved into other markets, such as Japan and China. In 2005, Gruma consolidated its entry to Asia with the construction of its first plant in China, which is to come on stream in 2006. Gruma currently has an investment programme of US\$ 500 million for China over the next five years.

Box V.7

THE ALFA AND DESC GROUPS: MEXICAN FOOD AS A MEANS OF RISK DIVERSIFICATION

A number of the larger Mexican groups have implemented diversification strategies in order to compensate for the natural fluctuations of business cycles and thus reduce the risks associated with their investments. The Alfa and Desc groups have gone into food manufacturing to offset market vagaries in such activities as petrochemicals, autoparts, and real estate. These groups viewed the mounting demand from Mexican immigrants in the United States and the growing international popularity of Mexican food as an interesting business opportunity. They acquired local companies, started to export, and soon installed productive capacity in foreign markets.

The Alfa Group, through Sigma (which accounts for 25% of the group's sales), is the leading producer of refrigerated and frozen food in Mexico, particularly as regards cold meat and dairy products. In the last few years, Sigma has tried to replicate its local success by entering the Central American and Caribbean markets, buying a number of businesses in Costa Rica, El Salvador and the Dominican Republic. In 2001, Sigma Food ("Sigma Alimentos") and ConAgra Foods (see table V.1) formed a joint venture to market frozen convenience foods in the United States, Canada, Mexico and Central America. ConAgra brought to the alliance its experience in product development and manufacturing, together with its distribution

network in the United States and Canada, and Sigma contributed its know-how in authentic Mexican food preparation, productive capacity and distribution network in Mexico and Central America.

The Desc Group has diversified internationally into the food business in the United States only (with a single plant in California), but with a wider range of products. The company produces and distributes a large variety of products, including traditional goods such as tomato purée, powdered coffee, vegetables and vegetable oil, as well as "ethnic" products such as ingredients for spicy dishes and chilli. "La Victoria" brand has a solid position in the traditional foods segment, as does "Embasa" in ethnic foods.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

3. Arcor: the confectionery maker

Arcor is one of the world's leading confectionery manufacturers and the main confectionery exporter in Argentina, Brazil and Chile. It is also the largest producer of biscuits in South America. The company focuses on the production of confectionery, chocolate, biscuits and processed foods, but it has undergone a gradual vertical integration encompassing strategic inputs such as milk, sugar, and packaging. Arcor has twenty-two plants in Argentina, four in Brazil, three in Chile and one in Peru, as well as a broad network of commercial offices to support its export strategy.

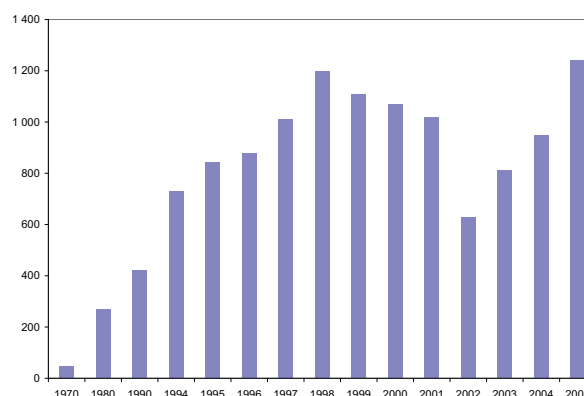
From its origins near Cordoba, Argentina, Arcor gradually expanded both its product mix and its geographical coverage. The company first exported in the late 1960s, when it already held approximately 50% of the Argentine market. Its growth during this period was based mainly on increasing the scale of production and consolidating distribution networks. At the beginning of the 1970s, while continuing to expand its product mix through acquisitions as well as organic growth, Arcor stepped up its exports and embarked upon a process of international expansion with investments in Paraguay (1976), Uruguay (1979) and Brazil (1981). The fact that Arcor's early export strategy focused on competitive markets, such as the United States and Latin America, was a distinguishing trait of its corporate development and pushed it to adopt best practices to meet the quality requirements of highly competitive markets.

In the 1980s, despite instability and stagnation in the Argentine economy, Arcor continued to expand its activities and modernize its production and management processes. Its levels of indebtedness grew considerably, as it sought to finance investments in a period of high financial costs. This left the company well placed for the recovery of domestic demand in the 1990s, however, which set it apart from its competitors. In fact, in the 1990s, the challenges posed by economic liberalization and institutional reforms led to many companies in Argentina being closed down or taken over by foreign companies, but Arcor was among of the few that successfully maintained their positions. Moreover, it did so using exclusively Argentine capital and it continued to expand its regional presence with new investments in Brazil (1999) and Chile (1998), while its productive operations in other countries enabled it to increase its presence in higher value added products (Kosacoff and others, 2002). Arcor thus became the main manufacturer of confectionery and chocolate in Latin America, with an increasing share in markets outside the Southern Cone through exports.

Arcor's international presence helped the company survive the economic crisis in Argentina in 2001 and 2002. It was one of the few companies that were able to come through the crisis, recover and even increase sales levels in relation to the late 1990s (see figure V.8). Its strong orientation towards foreign markets also enabled Arcor to profit from the competitive advantage created by the

devaluation of the Argentine peso. Even though local sales decreased considerably, exports grew and the company's access to currencies and markets not affected by the crisis gave it a natural hedge. This also enabled Arcor to defend its position in the domestic market, where it competed successfully with world class TNCs, such as Cadbury, Adams, Nestlé and Kraft-Suchard, and to consolidate its position in MERCOSUR and Chile (see table V.9). From Brazil, Arcor also has easier access for its exports to Africa and Europe. From Chile it sells to the Andean Community and Asia. Although other companies too turned to the international market, Arcor's advantage was that its internationalization strategy had matured over a long period of time and it was already a recognized international player. For example, in 2003, Wal-Mart nominated Arcor as one of its 50 worldwide strategic providers and the best in Argentina (Arcor, 2005, p. 13).

Figure V.8
ARCOR: CONSOLIDATED SALES, 1970-2005
(Millions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of Arcor, "Todo sobre Arcor" [online] 2005 <<http://www.arcor.com.ar>>.

Table V.9
ARCOR: PRODUCTION PLANTS OUTSIDE ARGENTINA, 2005

Country	Company	Location	Main product	Year established or entered market	Type of investment		
					Acquisition	Greenfield	Alliance
Brazil	Arcor Do Brasil	Piracicaba, São Paulo	Confectionery	1981	X		
	Arcor Do Brasil	Bragança Paulista, São Paulo	Chocolate	1997		X	
	Bagley Latinoamérica ^a	Campinas, São Paulo	Biscuits	2005			X
	Bagley Latinoamérica ^a	Aymoré, Belo Horizonte, Minas Gerais	Biscuits	2005			X
Chile	Alimentos Indal S.A.	Los Andes	Canned products, sauces and jams	1989		X	
	Industria de Alimentos Dos en Uno	Santiago	Confectionery and chocolate	1998	X		
Peru	Arcor Peru	Chancay	Confectionery	1996		X	
Mexico	To be determined	To be determined	Confectionery and chocolate	2005			X

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of Arcor, "Todo sobre Arcor" [online] 2005 <<http://www.arcor.com.ar>>.

^a Plants operated by Arcor in the framework of its strategic alliance with Danone. Arcor owns 51% of the property and Danone the remaining 49%.

Arcor has now reached a new phase in its global positioning strategy, in which alliances with transnational corporations are crucial. In April 2004, Arcor entered a strategic alliance with the French company Danone, thus moving into the business of biscuits, alfajores and cereal bars for Argentina, Brazil and Chile. This joint venture is managed by Arcor and represents the largest producer of biscuits in South America, with its products being sold under the "Bagley" brand name. In September 2005, Arcor also signed an agreement with Bimbo (see above) to produce and distribute confectionery and chocolate in the North American market. This agreement made Bimbo the sole distributor of Arcor confectionery products (Bon

o Bon) in Mexico. In addition, an investment agreement was signed for the construction of a plant in Mexico, which will manufacture Arcor and Bimbo products jointly.

In summary, Arcor's success has come of its ability to adapt to a turbulent macroeconomic environment, which included making large investments when other companies were retrenching. Arcor expanded gradually, basing its strategy on its competitive advantages: experience, technical know-how, technology and resources. The early internationalization process was crucial to this strategy and helped protect Arcor from the wave of takeovers that began to flood the Argentine business environment in the 1990s.

D. Conclusions

Both the food and beverages industries are being transformed by shifts in consumer tastes, technological change and increased competition. Moreover, the two industries are increasingly converging as food producers move into beverages and vice versa. As a result, the global TNCs and their trans-Latin counterparts in the region are implementing new corporate strategies.

The global TNCs are using their competitive advantages in brand management, scale economies and global distribution systems to increase their global presence. Corporations in the two industries have clearly differed in the timing and nature of their arrival in Latin America and the Caribbean. In the beverage industry, the carbonated soft drinks TNCs moved in earlier and their global brands are now dominant in the region, while the TNC brewers arrived later and local brands have prevailed up until now in the beer market.

The trans-Latins relied on their knowledge of local markets and the establishment of efficient national distribution systems, expanding internationally to build up a regional or subregional presence beyond simply exporting. The expansion of these trans-Latins on a regional scale and of the TNCs on a global scale soon made it necessary for the two to link up in the food and beverages industries.

The links between the TNCs and the trans-Latins consisted of licences to distribute TNC brands in local markets and minority or majority equity holdings. In carbonated soft drinks, Coca-Cola preferred to develop anchor bottlers as an integral part of its corporate strategy, whereas PepsiCo maintained looser links with its bottlers, which were mainly local brewers. In the beer industry, a number of the large and flourishing brewers

whose regional or subregional networks reached a certain critical mass were acquired by the dominant global TNC brewers. In the food industry, strong partnerships with TNCs (Gruma) occurred as well as weaker associations (Arcor). Mexican food-producing trans-Latins were better placed to benefit from the United States market in their internationalization process.

The experiences of trans-Latins in the food and beverages industries suggests that, unlike firms in basic industries, emerging Latin American TNCs are obliged to link up with the global corporations that dominate their particular industry. This type of association has led to three main outcomes. First, some trans-Latins, such as Bimbo and Arcor, have been able to compete with the global TNCs by specializing in niche and regional markets. Second, other trans-Latins have become closely integrated into global TNC networks (Coca-Cola FEMSA, Andina, CCU, Gruma), but have maintained majority equity control. Third, a number of trans-Latins have become formally integrated into global TNC networks, which hold an outright majority in their equity (AmBev, Quilmes, Bavaria).

In summary, the trans-Latins in the food and beverages industries faced tough competition in national and regional markets, especially from TNCs with a presence in most or all of the major global markets. The result was a number of “shooting stars”, or national companies that expanded and internationalized within the region, only to end up as components of TNCs that acquired their regional systems. Trans-Latins whose regional production systems reached a certain critical mass often became attractive targets for global TNCs scanning regional markets for opportunities.

Chapter VI

Trans-Latins in the services sector

Trans-Latins in the services sector can be divided into three major groups. The first consists of engineering and construction companies which got their start during the industrialization and infrastructure development processes that took place in their home countries during the second half of the twentieth century. Following the slowdown in those processes and the decline in the corresponding national governments' investment capacity, these firms began to seek out opportunities in other markets. The second group comprises public utilities that were transferred over to the private sector as part of the reforms of the 1990s. A third group, made up of retailers and other firms, developed in the wake of economic deregulation and liberalization as local enterprises responded to the new competitive environment and the arrival of TNCs seeking to capitalize upon the specific characteristics of Latin American markets.

A. Engineering and construction: a first generation of trans-Latins in the services sector

In the engineering and construction industry, there is no clear line between FDI and services exports. Inflows may be recorded as an export by the parent company in some cases and, in others, as sales made by a foreign subsidiary. Be this as it may, in most instances the intensive interaction

between these companies and economic agents in the host country is akin to what occurs in the case of FDI, with the firms' physical presence taking the form of asset and job creation, interaction with local authorities, and adaptation to local laws, regulations and customs.

Companies in this sector in Latin America and the Caribbean generally grew up against a background of industrialization and infrastructure development in their home countries during the second half of the twentieth century. They faced little competition from TNCs owing to the market-reserve policies prevalent at the time. When many States' financial capacity began to weaken in the 1980s, companies sought to diversify their activities, which often included public utilities that had recently

been privatized or opened up to private capital, and to expand into other geographical markets, moving towards internationalization. Prominent among these companies were the Brazilian conglomerates Odebrecht and Andrade Gutierrez and, to a lesser extent, Camargo Corrêa and Queiroz Galvão. Engineering was the basis for the diversification and development of other manufacturing and service activities by companies such as Techint and Impsa (Argentina) and the ICA group (Mexico).

1. Brazilian conglomerates

In the second half of the twentieth century, Brazil's engineering and construction companies burgeoned, thanks to the stimulus provided by the development of infrastructure such as roads, bridges, drinking-water and sanitation systems, industrial plants, oil platforms and airports. Having diversified into other industries and geographical markets, Odebrecht, Andrade Gutierrez, Camargo Corrêa and Queiroz Galvão were some of the country's largest conglomerates and major investors in foreign countries. Odebrecht and Andrade Gutierrez—Brazil's two strongest international players—are the only Latin American companies on the list of the world's top 100 international contractors, measured by revenues from projects outside the home country. In 2005, Odebrecht and Andrade Gutierrez were ranked in 21st and 82nd place, respectively (ENR, 2005).

In the 1980s, when economic conditions deteriorated in Brazil and the State's investment capacity began to decline, the country's engineering companies started to diversify in search of new businesses and geographical markets. Making use of the experience acquired in their home country, some of them—mainly Odebrecht and Andrade Gutierrez—embarked upon an active internationalization effort.

Odebrecht's first major project outside Brazil—a hydroelectric plant in Peru—was launched in early 1979. It also broadened its activities to include oil drilling services, with projects in Africa and India. In 1988, Odebrecht acquired the Portuguese contractor José Bento Pedrosa & Filhos and became involved in public utility concessions in Portugal. In the early 1990s, Odebrecht entered the United States market and while it was building up its activities there, it also undertook a number of projects—from shopping centres to hydroelectric plants—in Argentina, the Bolivarian Republic of Venezuela, Bolivia, Chile, Colombia, Ecuador, Mexico and Peru. In the oil drilling business, Odebrecht acquired a leading British offshore construction company, and formed partnerships with a number of other firms,

thereby acquiring considerable technical experience. This was followed by several projects in Africa.

In 1983, Andrade Gutierrez signed its first international contract. In 1988, it acquired the Portuguese firm Zagope, through which it undertook a number of airport, road and other construction projects in Portugal, including in the Madeira Islands, and participated in public-utility concessions for roads and sanitation works. With the contraction of the Portuguese market, Zagope began to bolster its internationalization strategy, focusing on North Africa (Algeria, Morocco and Tunisia), the European market and the Middle East. It also worked on road-building projects in Mauritania.

In the late 1990s, both companies restructured their activities, withdrawing from less profitable markets but maintaining a strong international presence. Odebrecht pulled out of Germany and South-East Asia, but remained in Angola. Andrade Gutierrez consolidated its presence in Latin America. In 2004, Odebrecht and Andrade Gutierrez generated about 80% and 60%, respectively, of their overall engineering and construction revenues outside Brazil.

Despite some bumps in the road, they have now successfully consolidated their status as major players in the world market, thanks to the competitive advantages afforded by a combination of technical know-how, flexibility and low costs, the ability to operate in unstable regulatory and economic environments, and cultural and linguistic links with countries where demand for infrastructure projects is high.

The internationalization of the Brazilian companies Camargo Corrêa and Queiroz Galvão followed similar, albeit less ambitious, paths, with investments focused on Latin America. Camargo Corrêa has pursued an internationalization strategy in other sectors, such as textiles, through Santista Têxtil, and more recently, the cement market, with the acquisition of Loma Negra in Argentina (see chapter IV).

In general, these Brazilian conglomerates emerged during the import-substituting industrialization (ISI) era, and their internationalization was a product of the subsequent ISI crisis.

2. Other engineering and construction companies

Techint was established as an engineering company based on its founders' know-how and experience (see chapter IV). It then grew to its current market position in flat steel and steel sheets and pipes. Almost immediately after it was set up in Italy, following the Second World War, the company began to provide engineering services to customers in Latin America and Europe; its first major project was a network of pipelines in Argentina and Brazil. It was involved in civil engineering and electric-power infrastructure works in the 1950s, and in the 1960s and 1970s it expanded into the market for turnkey plants in various industries, including steel and petrochemicals. The companies belonging to this group have worked on over 3,000 projects in 50 countries, mainly in Latin America, Africa and the Middle East. Techint is currently one of the world's largest corporations in the field of oil and gas pipelines. In addition to its engineering and construction activities in the steel industry, the group has expanded into other services, as have other companies in the same sector, especially since the reforms of the 1990s. About 82% of its engineering and construction activities are currently outside Argentina (see chapter IV).

Founded in 1947, the Mexican ICA group also based its growth on large-scale State projects such as the

construction of hydroelectric power stations, particularly from the 1950s onward. Beginning in the 1980s, like other companies, it diversified into other segments, such as water distribution and environmental services, and began seeking markets outside Mexico. In the 1980s and 1990s it worked on water distribution projects in El Salvador and the United States, an airport in Belize, gas pipelines in Argentina and civil engineering works in the United States. Since 1994, it has been involved in major gas-pipeline projects in Argentina, Bolivia and Chile, transport projects in Puerto Rico and road construction in Panama. Through its subsidiaries Rodio and Kronsa, it has taken part in various projects in Europe, especially Portugal and Spain. Its international sales currently make up 15% of the total.

The competitive advantages of this group of trans-Latins include a combination of technological capabilities, operational flexibility and low costs. The ability to operate in complex regulatory, legal and economic environments, together with linguistic and cultural links to certain countries, have given these companies an edge over global competitors in some markets, particularly those of developing countries, and their international experience has in turn helped them penetrate other markets, including the United States and Europe.

B. Public utilities in the hands of private enterprise

The economic and regulatory reforms implemented first in Chile and then in most of the other countries of Latin America and the Caribbean made room for the expansion of local private enterprises, which often competed or collaborated with TNCs. Having consolidated their positions in local markets, some of these companies began to see internationalization as an opportunity for further growth.

Chile's electric power companies led the way, achieving strong positions in a number of Latin American

countries, but were later taken over by TNCs. The Colombian firm ISA is an exceptional case, in that it is still State-controlled and has entered the international scene mostly through its activities in electric power transmission and telecommunications services (see box VI.1). In the telecommunications sector, the Mexican firms Teléfonos de México (TELMEX) and América Móvil both belonging to the Carso group. Examples in the airline industry include the Brazilian airline companies and the Chilean company Lan Airlines.

Box VI.1

THE ISA GROUP: INFRASTRUCTURE SERVICES IN THE ANDEAN COMMUNITY

Interconexión Eléctrica S.A. (ISA), a corporation controlled by the Government of Colombia, plays a major part in electric power transmission in Colombia and interconnections with neighbouring countries. It began its internationalization process in 2001 within the Andean Community, and in 2002 it bought stakes in two electric power companies in Peru, Red de Energía del Perú S.A. (REP) and Interconexión Eléctrica ISA Perú S.A. It owns 30% of REP directly and another 30% indirectly through its subsidiary Transelca, Colombia's second-largest electric power transmission company. It has a 28% direct shareholding in ISA Perú, and an indirect stake of 55%, also through Transelca. In 2003 it invested

in Bolivia's electric power transmission sector and set up Interconexión Eléctrica ISA Bolivia S.A. (ISA Bolivia). With these investments, the company now operates 48% of the Andean Community's power transmission networks with voltage levels of 220 kV and above. It runs 84% of such networks in Colombia, 79% in Peru, and 53% in Bolivia.

ISA has also invested in Ecuador's telecommunications sector. INTERNEXA, its telecommunications subsidiary, has a 50% share in TRANSNEXA SA, which is the main operator, and has exclusive control of the fibre-optic network between Ecuador and Colombia. Over a time span of several decades, ISA's activities in Colombia have enabled it to build up technological and

management capabilities, including the ability to integrate processes and products from local and foreign companies for the development, construction, operation and maintenance of electric power and data distribution networks. This has facilitated its work in other countries of the region. The firm has also benefited from the Andean Community's energy integration agreements, particularly Decision 536, which contains the "General framework for subregional interconnection of electric power systems and intra-Community exchange of electricity."

Currently, 17% of the group's sales and 15% of its assets are outside Colombia. It hopes to raise those figures to 50% in the coming 10 years.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

1. Electric power: shooting stars?

A number of Chilean firms have achieved considerable growth and a substantial regional presence in a relatively short time. Perhaps the electric power company Enersis provides the most outstanding example. Between 1992 and 1997, it carved out a strong position in electric-power generation and distribution markets in Argentina, Brazil, Colombia and Peru and became Latin America's largest electric power conglomerate, valued at US\$ 5 billion (ECLAC, 2000, p. 150). This process took place during a period when there were no large global operators, the world market was very fragmented, and the domestic market was dominated by State corporations.

Chilean electric power companies made their first foreign investments in Argentina, taking advantage of the privatization of Servicios Eléctricos del Gran Buenos Aires (SEGBA). In March 1992, a 60% shareholding in Central Puerto was awarded to Chilgener (49.5%) and Chilquinta (10.5%) for US\$ 92 million. Soon after that, 60% of the Costanera power plant was sold to a consortium of companies including Endesa (30%), Enersis (9%) and Chilectra (9%) for US\$ 90 million. Then the same consortium acquired 51% of Empresa Distribuidora Sur S.A. (EDESUR) for US\$ 511 million. Thus, SEGBA was divided up into four companies, three of which were controlled by Chilean corporations.

Enersis subsequently expanded its position in the region, acquiring new assets in Argentina, Brazil, Colombia and Peru. In Brazil, it bought a share of Companhia

de Electricidade do Rio de Janeiro (CERJ) and in the Cachoeira Dourada hydroelectric power plant. In Colombia it acquired shareholdings in the Betania and EMGESA power plants and the CODENSA power distribution company. In Peru, Enersis owned a share of Empresa de Generación Eléctrica de Lima (EDEGEL) and the EDELNOR distribution company.

Nonetheless, its rapid growth brought to light financial shortcomings which limited its ability to take part in new international competitive bidding for companies in the electric power sector. Faced with this problem, Enersis considered the possibility of bringing in a new shareholder with a controlling interest which could provide the capital needed for its future expansion. At that point, Endesa-Spain —its main competitor in the electric power business in Latin America— expressed an interest in forming a long-term strategic alliance. In late 1997, the Spanish corporation acquired 29% of Enersis for US\$ 1.179 billion, but that stake was not large enough to control the Chilean firm. Relations between the two companies deteriorated, and Endesa-Spain sought to gain control of the company. In March 1999, Endesa made a successful bid for 32% of Enersis for US\$ 1.45 billion, which gave it a 64% stake in the Chilean firm and control of its management.

Much the same thing soon occurred with Gener and Endesa, which were bought by AES Corporation of the United States and Endesa-Spain (through Enersis),

respectively. The acquisition of the Chilean electric power companies enabled international corporations that were competing for regional leadership to strengthen their positions in Latin America.

Chile's electric power companies are no longer the most active internationalizers, having instead chosen to confine themselves to certain specific industry niches in neighbouring countries. One such example is Compañía General de Electricidad S.A. (CGE), which has focused mainly on the distribution of electric power, natural gas and liquefied natural gas (LNG) in north-western Argentina. In 1992, through a competitive bidding process, a consortium (50% of which was owned by GASCO, a Chilean natural gas producer and distributor in which CGE has a 57% shareholding) was awarded the concession for the supply of natural gas in Salta, Tucumán, Jujuy and Santiago del Estero provinces. In 1995, CGE was part of a consortium that successfully bid for Empresa de Distribución Eléctrica de Tucumán S.A. (EDET), the electric power distribution company for Tucumán province. The following year, CGE and EDET joined another consortium that acquired a majority stake in Empresa Jujeña de Energía S.A. (EJESA) and Empresa Jujeña de Sistemas Energéticos Dispersos S.A. (EJSEDSA), which operated in Jujuy province. In 1999, with the acquisition of Empresa Eléctrica Emec S.A. (EMEC), CGE took control of Aguas Negras, the company that controlled Energía San Juan, the electric power distribution firm for San Juan province.

CGE currently distributes electric power to about 640,000 customers, covering the whole of Tucumán, Jujuy and San Juan provinces, with a market share of over 4% in terms of energy supply and 5% in terms of customers (CGE, 2005, p. 48). The difficulties affecting the Argentine economy have, however, caused problems for the company in that country. In November 2004, following unilateral changes to the legal and contractual regimes, CGE decided to take its case to the International Centre for Settlement of Investment Disputes (ICSID), requesting arbitration in its dispute with Argentina. The company was calling for recognition of the losses it sustained as a result of the measures adopted by Argentina, which have altered the pricing structure for electric power distribution (CGE, 2005, p. 48). Further issues arising from restrictions on exports of natural gas from Argentina were problematic for the company's operations in Chile. Consequently, CGE is facing serious difficulties at the international level.

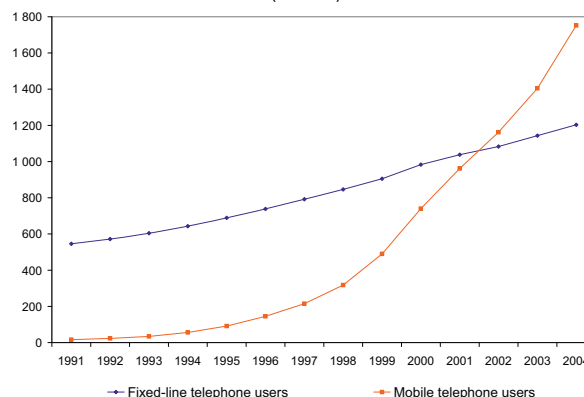
In short, Chile's electric power companies were pioneers in the recent internationalization of Latin America's largest corporations. Although it was a rapid and intense process, it was also relatively brief, and the leading companies were acquired by foreign corporations wishing to find a quick way of entering the Latin American market, which were attracted by the Chilean firms' broad regional coverage, particularly in the Southern Cone.

2. Telecommunications: the Teléfonos de México (TELMEX) and América Móvil phenomenon

Telecommunications have undergone sweeping changes in recent years, becoming one of the most dynamic sectors of the economy. Private enterprise is playing an increasingly important role, competition is intense, the mobile telephone industry is making inroads, and the sector is one of the driving forces of the globalization process.

Traditional telecommunications operators have been wholly or partly privatized in the great majority of countries. Where this has not yet occurred, private companies have a growing share of the sector. This is particularly true in the mobile telephone segment, which such firms have entered by obtaining service-provider licences. This has contributed to rapidly intensifying competition among the various segments and agents in the sector. Mobile telephones have been gaining ground swiftly and are increasingly replacing fixed-line telephones. In many countries, mobile phone users now outnumber fixed-line users (see figure VI.1).

Figure VI.1
TOTAL NUMBERS OF FIXED-LINE AND MOBILE TELEPHONE
USERS IN THE WORLD, 1991-2004
(Billions)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the International Telecommunication Union (ITU).

In the telecommunications sector, the globalization process has at least four very clear dimensions. First, most day-to-day activities are touched by telecommunications and information and communications technology. Second, governments have implemented their market liberalization and openness strategies in the framework of international, regional and multilateral agreements, particularly within the context of the World Trade Organization (WTO) Agreement on Basic Telecommunications Services.¹ Third, technological progress has contributed to format convergence and to the likelihood of improved flexibility and range in service delivery. The emergence and rapid growth of mobile-

phone and Internet services have dramatically changed the ways in which people communicate with one another. Third-generation (3G) mobile services will operate on a worldwide, rather than local or national, scale and will offer integrated multimedia services. Fourth, international firms that operate in several countries at once have appeared on the scene, and this development has given rise to an active consolidation process based on partnerships, mergers and acquisitions. A small group of companies is now present in all the world's largest markets, and it is difficult to find a country where the main telecommunications service provider is not a foreign investor (see table VI.1).

Table VI.1
THE WORLD'S LEADING TELECOMMUNICATIONS COMPANIES, BY SALES, 2004-2005
(Millions of dollars)

Company	Country of origin	Main activities	Total sales	Regions where operating, other than country of origin ^a				
				NA	LAC	EUR	AS	OTH
1 Nippon Telegraph and Telephone (NTT)	Japan	Fixed-line, mobile, data	100 545			x	x	
2 Deutsche Telecom AG (Telekom)	Germany	Fixed-line, mobile	71 989	x	x ^b	x	x	x
3 Verizon Communications Inc.	United States	Fixed-line, mobile, data	71 563		x ^c	x ^d		
4 Vodafone Group Plc	United Kingdom	Mobile	62 971	x		x	x	x
5 France Télécom	France	Fixed-line, mobile, data	58 652	x	x ^e	x	x	x
6 SBC Communications ^f	United States	Mobile, data	41 098					
7 Telecom Italia SpA	Italy	Fixed-line, mobile, data	39 228		x	x		x
8 Telefónica S.A.	Spain	Fixed-line, mobile, data	38 188		x	x		x
9 BT Group Plc	United Kingdom	Fixed-line, mobile, data	34 673			x		
10 AT&T Corp. ^{f g}	United States	Mobile, data	30 537					

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information from *Fortune*, "The 2005 Global 500" [online] <http://www.fortune.com/fortune/global500> and information provided by the companies.

^a NA: North America (United States and Canada), LAC: Latin America and the Caribbean, EUR: Eastern and Western Europe, AS: Asia, OTH: others.

^b Operations in Brazil only.

^c Verizon Communications has shareholdings in telecommunications companies in the Bolivarian Republic of Venezuela (28,5% de CANTV), the Dominican Republic (100% of Verizon Dominicana) and Puerto Rico (52% of Puerto Rico Telephone).

^d Verizon Communications has shareholdings in telecommunications companies in Italy (23.1% of the Italian subsidiary of Vodafone) and in the territory of Gibraltar (50% of Gibraltar NYNEX Communications (GNC)).

^e France Télécom has interests in Brazil (25 % of Intelig) and the Dominican Republic (85% of Orange Dominicana).

^f In 2005, AT&T Inc. (formerly SBC Communications), came into being when SBC purchased AT&T Corp. for some US\$ 16 billion, creating the largest telecommunications corporation in the United States. (Following the merger, SBC adopted the name AT&T Inc.) SBC had earlier combined its mobile telephone assets in the United States with those of BellSouth, forming Cingular Wireless. The assets of AT&T Wireless, acquired in 2004, were then added, making the company the country's largest mobile telephone operator, with more than 50 million subscribers, and the leader in the provision of broadband Internet services, with some 6 million subscribers.

^g On 5 March 2006, AT&T Inc. announced that it had reached an agreement to purchase the BellSouth corporation for some US\$ 67 billion. With that acquisition, AT&T became the company with the greatest market value, about US\$ 150 billion. Of approved by the regulatory authorities, the agreement will give AT&T full control over Cingular Wireless, a joint venture of SBC and BellSouth. AT&T plans to eliminate the Cingular brand and transfer its assets to the AT&T brand.

These changes have had a considerable impact in Latin America. In the 1990s, practically all State telecommunications corporations were privatized, and a few private companies—most of them foreign—became the largest operators in the sector. After an initial bout of enthusiasm, the lack of competition and deteriorating economic conditions in many of the countries of the region dampened investment, particularly in fixed-line services.

Nonetheless, growing demand for telecommunications services led to swift development of the industry's most dynamic segments, especially wireless phones and the Internet. From 1995 to 2004, the number of mobile telephone subscribers in Latin America soared from 3.5 million to 177 million. As the number of subscribers overtook traditional fixed-line customers in most countries, the profile of the regional market began to change rapidly

¹ February 1998 saw the entry into force of the WTO agreement liberalizing trade in basic telecommunications services, with 69 States parties representing more than 90% of the sector's worldwide income. The parties to this agreement undertook to apply, wholly or partly, a set of regulatory principles relating, in particular, to interconnection, transparency and the protection of competition.

and an intense process of consolidation began among the main operators. While some withdrew from Latin America in the face of intense international competition (especially from United States firms), others took the opportunity to strengthen their positions in the region. Prominent examples of firms in this group include Telefónica de España and the Mexican firm América Móvil, which are vying for the leadership of the regional market, with the Italian company Telecom Italia² lagging quite some distance behind in third place (see table VI.2).

Table VI.2
LEADING OPERATORS IN LATIN AMERICA: AMÉRICA MÓVIL,
TELEFÓNICA AND TELECOM ITALIA, SEPTEMBER 2005
(Thousands of customers)

Country	Telefónica de España		Telecom Italia		América Móvil	
	Fixed	Mobile	Fixed	Mobile	Fixed	Mobile
Argentina	4 477	7 395	3 500	5 400	-	5 555
Bolivia	-	-	52	1 400	-	-
Brazil	12 446	28 841 ^a	-	18 300	-	17 401
Chile	2 462	5 230	-	-	-	1 792
Colombia	-	5 171	-	-	-	11 334
Ecuador	-	1 624	-	-	-	3 546
Paraguay	-	-	-	-	-	139
Peru	2 302	3 199	-	-	-	1 596
Uruguay	-	322	-	-	-	111
Venezuela (Bol. Rep. of)	-	5 319	-	1 300	-	-
South America	21 687	57 101	3 552	26 400	-	41 474
Mexico	-	5 976	-	-	-	33 572
El Salvador	69	494	-	-	804	755
Guatemala	44	924	-	-	939	1 750
Honduras	-	--	-	-	346	-
Nicaragua	-	337	-	-	229	627
Panama	-	788	-	-	-	-
Central America	113	2 543	-	-	1 971	3 478
Total	21 800	65 620	3 552	26 400	1 971	78 524

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information from Telefónica, official site [online] <http://www.telefonica.es>; Telecom Italia, official site [online] <http://www.telecomitalia.it> y América Móvil, official site [online] <http://www.americamovil.com>.

^a Joint venture with Portugal Telecom, in which Telefónica owns a 50% shareholding.

América Móvil took the lead in a remarkably short time. In 1990, as a central part of the economic reforms undertaken by the Mexican authorities, TELMEX was privatized and sold as a vertically integrated company. One of the aims for this sale was to create a “national champion” capable of competing with foreign companies (Mariscal and Rivera, 2005). A consortium consisting of the Mexican financial conglomerate Carso and two international operators—the United States firm Southwestern Bell and the French company France Telecom—acquired 51% of

TELMEX for US\$ 1.7 billion. From 1990 to 1995, with the regulatory situation yet to be consolidated, the new owners operated as a monopoly. In mid-1995 the Federal Telecommunications Act was adopted, opening up all segments to competition. Although TELMEX enjoyed a monopoly in fixed-line telephones until the late 1990s, international operators began to challenge its position in other segments of the market, particularly in the case of its subsidiary TELCEL in the mobile telephone segment. TELMEX invested over US\$ 13 billion to modernize, expand and diversify its telephony facilities in Mexico.

Faced with increased competition in Mexico, TELMEX decided to compete on its potential rivals’ markets, and it rapidly made internationalization a central element in its growth and consolidation strategy. The company’s approach in this regard has a great deal in common with the strategy used by Telefónica a number of years earlier (Mariscal and Rivera, 2005). In 1995, TELMEX began the process of applying to operate in the United States, but it took three years for it to receive the necessary authorization after forming a partnership with the United States company Sprint. Given the difficulty of entering the United States market, TELMEX began to look at alternatives and, beginning in 1997, it acquired Telecomunicaciones de Guatemala (TELGUA) and a number of mobile telephone and Internet assets in Brazil, Ecuador and the United States.

Meanwhile, in Mexico, TELCEL was finding new ways to bring more customers into the mobile telephone market. Its payment-system innovations enabled it to capitalize upon that segment’s burgeoning growth, especially after its adoption of prepayment (1997) and “caller pays” (1999) systems. Aware that scale is very important on the mobile telephone market, TELCEL used prepayment mechanisms to attract low-income customers.

Taking advantage of its solid position on the Mexican market, TELMEX decided to place greater emphasis on its internationalization strategy, especially in the area of mobile telephones. In September 2000, it split off some of its own assets to create América Móvil as a spin-off.³ The new company began developing its own strategy to replicate the success it had achieved in Mexico by taking advantage of the low market penetration of mobile telephones in the rest of Latin America to achieve growth outside the country.

América Móvil benefited from favourable circumstances when it entered the telecommunications business. First, the company had some US\$ 2 billion in reserve for the

² Telecom Italia has focused on the mobile telephone market in Brazil, where it is competing for second place with América Móvil.

³ TELCEL in Mexico, TELGUA in Guatemala, Consorcio Ecuatoriano de Telecomunicaciones S.A. (CONECEL) in Ecuador, and Algar Telecom Leste (ATL) in Brazil.

acquisition of additional assets. Second, it pioneered the development of a new form of financing on the Mexican market based on stock certificates known as CEDEVIS, which enabled it to raise the additional capital needed to finance its aggressive international expansion strategy.⁴ In addition, the international telecommunications sector was facing an acute crisis, and a number of its main operators were seeking to sell off non-strategic assets in Latin America, providing attractive opportunities for new acquisitions.

From the beginning, the company's internationalization process focused on Latin America, and particularly the Brazilian and Colombian markets. From that starting point, the company has expanded into Argentina, Central America (El Salvador, Guatemala, Honduras and Nicaragua) and, more recently, Chile, Paraguay and Peru.

Initially, the newly-founded company sought to establish alliances with other international operators in order to acquire the necessary experience and diversify the risk involved in its ventures outside Mexico. In November 2000, together with Bell Canada Inc. and SBC Inc., América Móvil set up Telecom Américas to strengthen its expansion in Latin America. In a series of transactions between 2000 and 2002, Telecom Américas acquired four mobile telephone companies in Brazil: Algar Telecom Leste (ATL)⁵ (Rio de Janeiro and Espiritu Santo), Americel (seven states in the central-western and northern regions), Telet (Rio Grande do Sul) and Tess (São Paulo). Through the creation of Telecom Américas, América Móvil acquired a stake in the Colombian company Comunicación Celular S.A. (COMCEL), in which Bell Canada had a large shareholding.

Nonetheless, although this alliance had started out with great enthusiasm, it proved to be short-lived owing to differences in the participants' strategic outlooks. In 2002, América Móvil bought out its partners' shares,

restructured Telecom Américas and turned its attention entirely on Brazil.⁶ At that point the firm began to buy other companies and licences, including the assets of BellSouth in Brazil (BSE and BCP), and expanded its stakes in companies in which it already had interests, thereby achieving nationwide coverage. In late 2003, América Móvil brought together its regional operators under a single brand name, Claro. By September 2005, having invested more than US\$ 5 billion, América Móvil had succeeded in establishing a strong position on the Brazilian market (17.4 million customers and 22% of the national market), although it was still far behind its main rival in the region, Telefónica (28.8 million customers and 36% of the market).⁷

Thus, as a result of the restructuring of Telecom Américas, América Móvil ended up with the operation in Colombia. It later acquired a number of other companies that were then merged under the name COMCEL in December 2004. COMCEL currently provides mobile telephone services to 80% of Colombia's population.

Having taken over the assets of Telecom Américas in Colombia and Brazil, América Móvil adopted an active acquisitions strategy elsewhere in Latin America, capitalizing on the opportunities opened up by other distressed operators. Between 2003 and 2005, América Móvil purchased France Telecom's stake in Compañía de Telecomunicaciones de El Salvador (CTE); the Peruvian subsidiary of Telecom Italia; Smartcom, a company created in Chile by Endesa-Spain; and an asset of Verizon in Argentina, the Compañía de Teléfonos del Interior (CTI).⁸ As of September 2005, América Móvil had almost 45 million mobile telephone customers outside Mexico (57% of the total number) and had gone a long way towards closing the distance between itself and Telefónica on the Latin American market (65.6 million customers, or 70% of the total) (see table VI.2).⁹

⁴ Financing on the local capital market was particularly brisk in 2002-2003. In 2004, América Móvil sought additional financing on international markets through the issue of bonds. Given the company's good results, those issues were very successful, with rates of return equivalent to those of any "blue chip" in the United States. Between 2000 and 2005, América Móvil invested US\$ 3.1 billion in the United States and 13.75 billion pesos on the Mexican Stock Exchange.

⁵ In late 2001, América Móvil had a 59% indirect stake in ATL through Telecom Américas. In January 2000, América Móvil had acquired a minority shareholding in ATL for US\$ 248 million, and in May 2001, it purchased an additional 41% from the United States company Williams Communications Group Inc. for US\$ 400 million.

⁶ In July 2002, América Móvil bought Bell Canada's shares for US\$ 370 million and acquired those of SBC Inc. in exchange for 50% of Cellular Communications of Puerto Rico Inc.

⁷ In September 2005, second place in the Brazilian market was held by the Italian firm TIM, with a market share of 23%, and a local company, Telemar, trading under the brand name Oi, was in fourth place.

⁸ In Argentina, América Móvil negotiated directly with CTI's creditors, having committed itself to investing the necessary resources to make its investment profitable. Between 2003 and 2004, in a series of transactions, it acquired 92% of CTI, for which it paid US\$ 239 million, and secured debt instruments issued by CTI operating subsidiaries for about US\$ 600 million. In July 2004, América Móvil purchased the remaining 8% of the company's shares from the Techint group. In December 2004, CTI had a market share of 26%, and 67% of its subscribers were in the interior of the country, the remainder being in or near Buenos Aires.

⁹ In September 2005, Telefónica had 19.6 million customers in Spain, 4.5 million in the Czech Republic and 3.8 million in Morocco.

In addition to its sizeable market share, the fact that América Móvil had built up a homogenous mobile telephone network based on GSM technology has given it a notable advantage over its main competitors in Latin America. This choice of technology would enable the company to implement new advances in the industry more easily while also giving it a sufficient scale to facilitate negotiations with technology suppliers. Telefónica, its main competitor, has an equivalent number of customers in a similar number of countries, but its network incorporates several different technologies (see table VI.2).

Although América Móvil and TELMEX currently operate as independent companies, the former's experience has provided inspiration for the latter. In 2004, TELMEX acquired the assets of AT&T in Latin America, the shares of the United States firm MCI in the Brazilian long-distance telephone company EMBRATEL, the telephone companies Tectel and Metrored in Argentina, and the Chilean firm Chilesat. From 2003 to 2005, TELMEX invested some US\$ 4.75 billion in Latin America (*Latin Trade*, December 2005, p. 39), acquiring a direct share in the fixed-line, long-distance and data transmission segments of some of South America's leading markets. TELMEX does not face strong competition in the mobile telephone segment, but this is not the case in the other sectors, where it must contend with competitors such as Telefónica, which controls 38% of the market in Brazil and 80% in Chile. Like América Móvil, TELMEX will seek to bolster its presence in Brazil by consolidating its assets in that market and using its share of the cable television network (Net Serviços de Comunicação) to offer broadband Internet services (see table VI.3). In March 2006, TELMEX announced its intention to purchase Verizon's assets in Latin America for about US\$ 4 billion. The negotiations are thought to involve the purchase of 28.5% of CANTV in the Bolivarian Republic of Venezuela, 52% of Puerto Rico Telephone, and 100% of Verizon Dominicana (formerly CODETEL) (*El Universal*, 3 March 2006).

Thus, in a little under five years, América Móvil has become a considerably larger and stronger firm than what had been expected when it was founded. It now shares regional leadership with Telefónica, which has a bigger fixed-line customer base. América Móvil is among the

region's leading companies and one of the five largest in the world in terms of subscribers (see figure VI.2). As of late 2005, it had operations in 14 countries in the Americas (including Mexico and the United States) and was serving 78.5 million mobile-phone clients and 2 million fixed-line subscribers in Central America, a subregion where it has become the largest telecommunications service provider. Like Telefónica, América Móvil owes its success to its competitive performance in the context of the "national champion" policy.

Table VI.3
TELMEX: OPERATIONS IN LATIN AMERICA

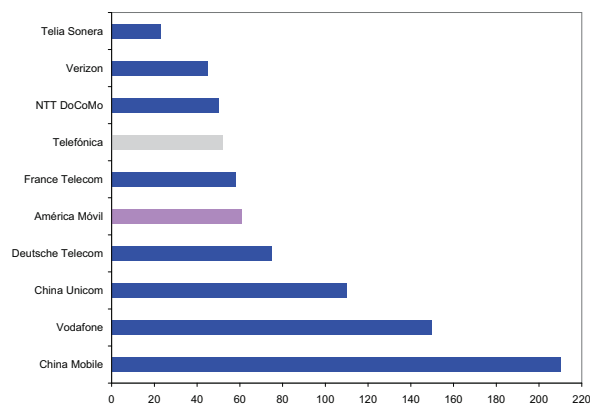
Country	Company	Market share	Date acquired	Amount
Argentina	TELMEX Argentina ^a	100.0	24/02/2004	200 ^b
	Tectel	93.3	19/04/2004	113
	Metrored	93.3	30/06/2004	...
Brazil	TELMEX do Brasil ^a	100.0	24/02/2004	^b
	EMBRATEL	63.9	23/07/2004	400
	Net Serviços de Comunicação	37.1	31/01/2005	...
Chile	TELMEX Chile ^a	100.0	24/02/2004	^b
	TELMEX Corp. (Chilesat)	99.3	08/06/2005	131
Colombia	TELMEX Colombia ^a	100.0	24/02/2004	^b
Peru	TELMEX Perú ^a	100.0	24/02/2004	^b

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

^a Assets acquired from AT&T Latin America.

^b In February 2004, TELMEX purchased the assets of AT&T Latin America in Argentina, Brazil, Colombia, Chile and Peru for a total of US\$ 196 million.

Figure VI.2
MOBILE TELEPHONE SERVICES: THE 10 LEADING OPERATORS,
BY NUMBER OF CUSTOMERS, DECEMBER 2004
(Millions of subscribers)



Source: Economic Commission for Latin America and the Caribbean (ECLAC).

3. Trans-Latins in air transport: operating in heavily regulated territory

In the airline industry in Latin America and the Caribbean, as in other world regions, foreign airlines are subject to various restrictions. These restrictions deal with aspects

ranging from the nationality of pilots and flight attendants to limits on how large a share of the company can be held by foreign interests and barring such companies from

running domestic flights. The privatization of State airlines in the 1990s and the somewhat more flexible rules adopted by some countries since then have created opportunities for the internationalization of airline companies. There have been two generations of international ventures by airline transport companies in the region. The first was led by the major Brazilian airlines, and the second by the Chilean company Lan Airlines.

In the second half of the 1990s, Brazil's traditional airlines Varig, Viação Aérea São Paulo (VASP)—both State-owned—and TAM invested in neighbouring countries. Varig acquired 49% of the Uruguay's Pluna airline. However, the company's problems in the domestic market were reflected in Pluna's performance and held back any other movements Varig might have made towards internationalization. In 2005, Varig announced its intention to sell its shareholding in Pluna.

In 1995, VASP acquired 50% of Lloyd Aéreo Boliviano (LAB), a company that was going through a serious crisis. Also in the mid-1990s, VASP bought 51% of Ecuatoriana de Aviación. As in the case of Varig, the financial problems experienced by VASP in Brazil were an obstacle to the success of its international operations. VASP sold its share of LAB in 2001, and in the same year Ecuatoriana de Aviación's operations were suspended and its routes were transferred to LAB.

TAM focused its internationalization on MERCOSUR. In 1994 it set up ARPA Líneas Aéreas Paraguayas and in 1996, it acquired 80% of Líneas Aéreas Paraguayas, a shareholding which had belonged to Cielos de América, an Ecuadorian consortium. The operations run by TAM in Paraguay have been consolidated under the name Transportes Aéreos del Mercosur (TAM Mercosur). TAM owns 95% of this company, with the remainder belonging to the Government of Paraguay. TAM Mercosur operates between Buenos Aires, Montevideo, Ciudad del Este, São Paulo, Santa Cruz, Cochabamba, Santiago and Curitiba, among other destinations.

Towards the end of the 1990s, the introduction of greater flexibility in Brazil's airline industry paved the way for the appearance or growth of new airline companies, including Gol Airlines. In just a few years' time, this "low-cost, low-price" airline has seen remarkable growth in Brazil, where it has carved out a market share of about 30% in less than five years, as well as in terms of international routes in Latin America. Despite the discouraging results of the major Brazilian airlines, in July 2005 Gol announced that it was embarking on an

internationalization drive involving the creation of a similar company in Mexico. The Mexican market is the second largest in Latin America after Brazil, and its per capita incomes, distances and relatively high prices open the way for the introduction of a "low-cost, low-price" model. The new company is expected to start operating in 2006.

The Synergy group, which owns a small airline in Brazil, Ocean Air, acquired stakes in Vipsa (Ecuador) and Taxi Aero and Wayra (Peru), then, in 2005, it acquired 100% ownership of the Colombian airline Avianca. These investments have given the group a larger presence in the airline industry outside Brazil than within the country.

The most interesting experience of all, however, is that of the Chilean company Lan Airlines. Privatized in 1989, it has been thoroughly restructured. This process has involved various national acquisitions, capital restructuring and changes in ownership and, beginning in 1994, a reorientation of its strategy with a view to becoming South America's largest airline and one of the 10 biggest in the world.

Following a wide-ranging search for a new corporate identity, the management of Lan Airlines began to develop the LAN brand without restricting it to the Chilean market, realizing that the only way to grow would be through an international expansion drive involving the creation of a network of companies based in various Latin American countries, rather than the addition of more routes within Chile. To that end, Lan Airlines has set up Lan Perú, Lan Ecuador, Lan Dominicana and, more recently, Lan Argentina to operate domestic routes along with some international destinations.

Lan Airlines took a decisive step towards the regionalization of its operations when it successfully concluding negotiations with the Government of Peru for the creation of Lan Perú in 1999. Under the terms of that country's legislation, the Chilean company undertook this initiative jointly with Peruvian investors, who retained a 51% stake in the airline, with Peruval holding 30% and Inversiones Aéreas 21%.¹⁰ Thus, Lan Airlines owned 49% of the new company, which provided international services between Chile, Peru and the United States, as well as operating domestic routes between cities such as Arequipa, Cuzco and Lima.

Nonetheless, the capital structure of Lan Perú gave rise to numerous difficulties and legal disputes. First, although Inversiones Aéreas was incorporated under Peruvian law, it was directly linked to Lan Airlines. This meant that 70% of Lan Perú was in Chilean hands, in contravention

¹⁰ Under Civil Aviation Act No. 27,261, at least 51% of an airline must remain in Peruvian hands. The Act's implementing regulations, adopted in December 2001, provide that the 49% limit on foreign ownership of the company's capital remains in force for the first six months from the beginning of operations. After that period, foreign shareholdings may increase to a maximum of 70%.

of the Civil Aviation Act. Second, there was considerable tension between Lan Airlines and Peruval. As a result, Lan Perú's international flights were suspended in November 2000, as were its domestic services the following month. The situation began to improve in early 2001, when 30% of the company was transferred to a local entrepreneur who then became the president of the Peruvian affiliate. Domestic flights were then restarted, and a month later international services were resumed.

In 2002, Lan Airlines set up Lan Ecuador, and in August of that year authorization was obtained from the Ecuadorian National Civil Aviation Council for the operation of international services from the country's two main cities, Quito and Guayaquil, to five foreign destinations (Buenos Aires, Madrid, Miami, New York and Santiago). In December 2002, having invested US\$ 250 million to purchase two Boeing 767-300 aircraft and one Airbus A-320, and US\$ 100 million to recruit 500 staff, Lan Ecuador began its commercial operations. It is currently the country's largest operator, with a 20% market share (BCI, 2004a, p. 7).

In mid-2003, Lan Airlines began to operate regular flights between Santo Domingo and Miami, with three flights per week on Boeing 767-300 aircraft. In order to do so, it set up Lan Dominicana, in which Lan Airlines has a 49% shareholding, with the remainder in the hands of Dominican investors. The service was later extended to major tourist destinations in the Dominican Republic, such as Punta Cana.

In March 2005, after a number of unsuccessful attempts, efforts to enter the Argentine market began to bear fruit. Lan Airlines reached an agreement with the Government of Argentina to operate the State-owned company Líneas Aéreas Federales (LAFSA) and to establish a new airline,

Lan Argentina. To put its initiative into effect, Lan Airlines acquired Aero2000, a local company that held a licence from the Secretariat of Transport to operate some of the main local and international routes, but was not operating any flights and had no aircraft of its own. Since, under Argentine legislation, domestic investors must hold a majority interest in airline companies, Lan Airlines took a 49% stake in Lan Argentina and local partners acquired the other 51%. The arrival of Lan Airlines in Argentina raised some difficulties, including strong opposition from the LAFSA trade unions. Lan Argentina had modest plans initially, but expectations are high. The airline was set up with just US\$ 4 million, but in two years it plans to control 40% of the Argentine market, which is twice the size of Chile's.

Lan Airlines is currently the largest domestic and international passenger airline in Chile, Ecuador and Peru. It has also expanded the scope of its air cargo operations by acquiring stakes in such airlines as Aerolinhas Brasileiras S.A. (ABSA) in Brazil, MasAir in Mexico and Florida West in the United States and by setting up an operations centre in Miami. This strategy has turned Lan Airlines into the region's principal air cargo carrier.

Further advances in the internationalization process will require not only determination and the necessary capabilities on the part of the firms in question, but also greater flexibility in policies and restrictions applying to the participation of foreign investors. Any such change is likely to be influenced, positively or negatively, by the performance of the first few internationalized companies and their impact on competition and prices in domestic markets. It will also depend on what kinds of alternatives to the entry of foreign capital may be found for addressing the serious financial problems facing some of the region's principal airlines.

C. Retail trade: a new business model ushers in an exceptional success

The evolution of retail trade in Latin America has paralleled its growth in Europe and the United States, although it occurred several decades later. In the early twentieth century, department stores began to appear in the region's main cities. Later, following the United States model, the first supermarkets appeared, then hypermarkets and shopping centres. The retail trade sector has traditionally been in the hands of local family-owned groups, and its growth has generally been quite fragmentary.

At the worldwide level, unlike other industries, the internationalization of retail trade companies has been slower. Until the 1960s, most companies had focused their growth and diversification strategies on their local markets. Traditional markets, however, began to show signs of saturation and this, together with regulatory changes and greater openness to FDI, prompted some large firms to seek new growth opportunities abroad. In the supermarket segment, European companies were the

pioneers, particularly the French company Carrefour and the Netherlands firm Royal Ahold (see table VI.4).

In the 1990s, the internationalization of companies in the sector became more dynamic—particularly with the arrival of the United States chain Wal-Mart—and Latin America has in recent years become one of the main

targets of those major operators. Through a strategy based on the acquisition of local chains, Wal-Mart, Carrefour and Royal Ahold rapidly built up a solid position in the region's major markets (Argentina, Brazil and Mexico) and soon became some of the largest TNCs operating in Latin America.

Table VI.4
THE WORLD'S LEADING RETAILERS, BY SALES, 2004
(Millions of dollars)

Country	Home country	Main activities	Total sales ^b	Regions where operating, other than home country ^a				
				NA	LAC	EUR	AS	OTH
1 Wal-Mart Stores Inc.	United States	Supermarkets, hypermarkets, convenience stores	287 989	X	X	X		
2 Carrefour S.A.	France	Supermarkets, hypermarkets, convenience stores	90 389	X	X	X	X	
3 The Home Depot Inc.	United States	Home improvement	73 094	X	X ^c			
4 Metro AG	Germany	Supermarkets, home improvement, department stores	70 165		X	X	X	
5 Koninklijke Ahold N.V.	Netherlands	Supermarkets, hypermarkets, convenience stores	64 681		X			
6 Tesco Plc	United Kingdom	Supermarkets, hypermarkets, convenience stores	62 505		X	X	X	
7 Kroger Co.	United States	Supermarkets, convenience stores	56 434					
8 Rewe Group	Germany	Supermarkets, home improvement, convenience stores	50 749		X			
9 Costco Wholesale Corp.	United States	Convenience stores	48 107	X	X ^c	X	X	
10 Target Corp.	United States	Department stores	46 839					

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information from *Fortune*, "The 2005 Global 500" [online] <http://www.fortune.com/fortune/global500>; *Stores*, "2005 Global powers of retailing. The top 250 global retailers", section 2 [online], Deloitte Touche Tohmatsu, January 2005, <http://www.stores.org>; Chain Store Age, "Top 100 global retailers" [online] December 2004, <http://www.chainstoreage.com>.

^a AN: North America (United States and Canada), LAC: Latin America and the Caribbean, EUR: Eastern and Western Europe, AS: Asia, OTH: others.

^b Refers to the group's overall sales and may therefore include sales not related to retail trade.

^c Operations in Mexico only.

Table VI.5
LATIN AMERICA: LEADING INTERNATIONAL RETAIL CHAINS, BY SALES
AND MARKET POSITION, 2004
(Millions of dollars)

Country	Leading global/regional chains				Emerging chains			
	Wal-Mart Stores		Carrefour		Cencosud		Falabella	
	Sales	Position	Sales	Position	Sales	Position	Sales	Position
Argentina	300	...	1 457	1	792	2	144	...
Brazil	2 298	3	4 562	2	-	-	-	-
Chile	-	-	-	-	1 684	2	2 337	1
Colombia	-	-	560	4	-	-	-	-
Mexico	12 598	1	^a	-	-	-	-	-
Peru	-	-	-	-	-	-	404	3

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

^a In March 2005, Carrefour sold its assets in Mexico to the local chain Chedraui for an estimated US\$ 500 million.

During this period, expansion into the smaller Latin American economies was more limited, with Royal Ahold being almost the only significant participant. The Netherlands chain achieved a strong position in Chile, Paraguay, Uruguay and Central America. In 1999, Royal Ahold entered into partnerships with firms in Costa Rica and Guatemala, creating Central America's largest

supermarket chain, Central America Retail Holding Company (CARHC). Nonetheless, in early 2003, Royal Ahold ran into serious financial difficulties and publicly admitted to accounting irregularities. The company's announced intention to withdraw from Latin America created new openings for other companies wishing to expand their presence in the region. Its most valuable Latin American

assets were acquired by just two companies: Wal-Mart and the emerging Chilean group Cencosud.¹¹

As can be seen from the experience of Royal Ahold, it has not been easy for large retailers to expand into foreign markets, and good results at home are no guarantee of success abroad (Bianchi and Ostalé, 2004, p. 3). Royal Ahold has not been the only example of this in Latin America; other transnational corporations with subsidiaries in the region that have pulled out of certain countries include The Home Depot (Argentina and Chile) and Carrefour (Chile and Mexico). In most such situations, the international chains in question have been unable to adapt their formats and practices to the characteristics of local markets and have faced

unexpected difficulties with suppliers, the accommodation of consumer preferences, and strong competition from established local chains.

The Chilean experience is a particularly interesting one. Local chains put up a fierce resistance to leading international corporations, reinforced their positions on the domestic market, and then explored new business opportunities in neighbouring countries. This last development is especially noteworthy, since not even the big Mexican chains (Organización Soriana, Controladora Comercial Mexicana, Grupo Gigante and Grupo Elektra), which have been strong competitors of Wal-Mart, have succeeded in expanding their activities abroad to any significant degree (see box VI.2).

Box VI.2

IN SEARCH OF A COMPETITIVE FORMAT: THE ELEKTRA GROUP'S BANK/STORE COMBINATION

The largest retailer in Mexico is the United States firm Wal-Mart, followed at some distance by a series of local operators, such as the supermarket chains Organización Soriana, Grupo Comercial Mexicana and Grupo Gigante; the Puerto de Liverpool department stores; and Grupo Elektra, an electronics and white-goods chain. In most cases, when businesses are faced with the possible arrival of new international operators, they have focused their strategies on defending their domestic market shares. Only a few companies have seen expansion outside the country as the answer to the challenges of growing competition, but Grupo Elektra is one of them.

In the late 1990s, this group adopted an ambitious internationalization strategy, seeking to enter the great majority of Spanish-speaking markets in Latin America and the Caribbean. Initially, Elektra sought to replicate the strategy it had developed in Mexico, and in less

than three years it opened almost 100 establishments in the Dominican Republic, El Salvador, Guatemala, Honduras and Peru, while also offering direct credit facilities through its commercial division (Credifácil in El Salvador and Elektrafin in other countries). Nonetheless, the company encountered many legal restrictions on its financial activities that limited its ability to provide credit to its stores' customers. The combination of commercial and financial activities has been the key to Elektra's success on the domestic market, as well as that of other emerging corporations, such as the Chilean firms Falabella and Ripley. In 2002, its poor results forced Elektra to close down its operations in the Dominican Republic and El Salvador and to rethink some aspects of its business strategy.

The new strategy was aimed at strengthening the financial dimension of the group's businesses. To that end, Grupo Elektra obtained a licence to operate a commercial bank—the first

granted to a Mexican entity since 1994—and created the Banco Azteca. The group took advantage of Elektra's large network of stores, turning them into both retail shops and bank branches. This was an innovative strategy for Mexico, and in record time the Banco Azteca became the country's largest banking institution in terms of the number of branches and geographical coverage. With this new business model, the Grupo Elektra has sought to reactivate and strengthen its international expansion. The idea has been to first set up a bank branch office and then to expand commercial activities by opening up new stores. In March 2005, the Grupo Elektra began operating in Panama, establishing its first branch outside Mexico, and it plans to expand this strategy to other Latin American countries in the future. Elektra plans to spend some US\$ 400 million to open about 60 new shops in Mexico and Central America in 2005-2006 (*Business Latin America*, 14 November 2005).

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

Retail trade is one of the most dynamic sectors of the Chilean economy, has been steadily growing stronger and is highly competitive. In recent years there has been a marked trend towards consolidation of the sector's different commercial formats—supermarkets, specialized chains (pharmacies, home improvement and building materials) and department stores—which compete aggressively to attract consumers. There has

also been greater diversification in sources of income. This has been accomplished, essentially, through the provision of customer credit and the sale of a broader range of products at the same location in order to attract more customers (banking services, insurance and travel agencies). Many of these changes have occurred against the backdrop of profound transformations in the sector's largest companies as they have made the transition from

¹¹ Wal-Mart acquired the Brazilian chain Bompreço and Royal Ahold's shares in the Central American supermarket chain CARHCO. Cencosud bought the Santa Isabel chain in Chile and the Disco supermarkets in Argentina.

family firms to professionally-managed firms and then into public companies whose shares are traded on stock markets in Chile and abroad.

With a more open economy and growing competition with the arrival of the first international operators, retail companies adopted a defence strategy which yielded good results. First, they studied the top international retailers. They then took some of those retailers' business models and practices, pinpointed and eliminated their shortcomings, and proceeded to adapt them to the local market. They also hired executives who had ties with those corporations and then added new products and services. For their part, the foreign corporations underestimated the local firms' ability to react and ultimately had to withdraw from the Chilean market (Bianchi and Ostalé, 2004).¹² Thus, a number of companies emerged in this sector whose competitive advantages have enabled them to establish a strong position on the domestic market, to block international competitors' attempts to enter the Chilean market and to begin to expand into neighbouring countries (see table VI.6).

Table VI.6
CHILE: LEADING RETAILERS, BY MARKET SHARE, 2005
(Percentages)

Group	Department stores	Home improvements	Supermarkets	Pharmacies
Falabella	40	21	3	-
Cencosud	29	5	25	-
Ripley	31	-	-	-
D&S	-	-	35	4
Farmacias Ahumada (FASA)	-	-	-	30
Salcobrand	-	-	-	27
Cruz Verde	-	-	-	34
Other	0	74	37	5
Total	100	100	100	100

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

Financial activities within the context of retail trade are quite widespread in Chile.¹³ The development of the sector has been closely linked to the provision of customer credit and has been boosted by retailers' creation of financial entities of their own, such as Banco Falabella (1998), Banco Ripley (2003) and Banco París (2004). Meeting the demand for customer credit has become an additional source of income and a key factor in these companies' profit structures. Consumer credit activities

strengthen the retail side of the business, and good results there, in turn, boost credit levels, thus generating a strong synergy between the two activities (Falabella, 2004b, p. 27). It also provides retailers such as Falabella, Ripley and Cencosud with information on their customers that helps them to define marketing strategies and optimize the composition of their merchandise and promotional activities. Changes in the regulatory framework and greater market restrictions could affect these firms' capacity to generate operating flows, and their ability to adapt to a more restrictive environment will therefore be of vital importance for its future growth.

Cencosud has been a pioneer in international expansion. During the 1980s it opened two shopping centres with Jumbo hypermarkets in Buenos Aires, where Unicenter was the largest of its kind in Argentina. These initial incursions marked what was to become the pattern for Cencosud's internationalization drive, which involved a combination of real estate development—construction and operation of shopping centres—with retail trade, particularly supermarkets, to which it would later add home improvement stores. In 1993, the company introduced a new line of business simultaneously in Argentina and Chile, opening the Easy home improvement and building materials stores. From then until 1998, Cencosud's growth in Buenos Aires was particularly rapid, as it built and ran seven new shopping centres, all of which included Jumbo and Easy stores. The company's market penetration strategy was even broader in the case of Easy, as it located almost half of these stores away from the shopping centres run by Cencosud. This strategy was designed to generate synergies between the company's different lines of business, especially in Argentina.

During the same period, the department store chain Falabella also moved into Argentina, but with a rather more conservative strategy than the one used by Cencosud. In 1993, the firm opened its first store in the town of Mendoza, where people were already familiar with Falabella because of the busy tourist traffic between the two countries. The company saw Mendoza as offering a opportunity for growth with less risk than would have been involved in moving into Buenos Aires (Bianchi, 2002, p. 6). With this initial operation, Falabella became the only department store chain operating in the Argentine market (Falabella, 2004b, p. 37).

Despite this privileged position, the results were not up to expectations. Falabella had to deal with a complex environment in which legal standards, consumers' preferences

¹² In 1999, after operating for five years without making a profit, the largest United States department store chain, J.C. Penney, sold its assets to its local competitor Almacenes París. In 2001, three years after it had begun doing business, the world's biggest home improvement store, The Home Depot, decided to sell its operations to its local partner Falabella. In 2003, after five years in the country, the world's largest supermarket chain, Carrefour, sold its premises to the local operator D&S. Lastly, in the same year, Cencosud acquired the operations of Royal Ahold in Chile.

¹³ This strategy had already been applied by companies in the United States. In Chile, however, it was particularly successful, given that the targets of the big stores' credit card facilities were lower-income consumers, a segment not covered by traditional banking.

and habits, and import facilities were very different from those in Chile. Nonetheless, the company continued its expansion into Argentina, opening two new shops in San Juan (1994) and Córdoba (1997) while seeking to generate economies of scale that could make the venture profitable (Bianchi, 2002, p. 6). Its real opportunity to consolidate its position in Argentina came a little later, however, when Cencosud remodelled Unicenter. Falabella then came in as the second anchor store at Unicenter, alongside Jumbo, and established itself in Buenos Aires. As a means of promoting its department store sales, it also introduced its CMR credit card and other services such as a travel agency. When it began to provide credit, the company's performance began to pick up, and Falabella now has high expectations for its future growth in Argentina (Falabella, 2000, p. 17).

In light of its experience in Argentina and the difficulties it had encountered there, Falabella reformulated its strategy for entering other markets and began to pay special attention to local characteristics. In 1995, encouraged by the Peruvian economy's growth prospects, it entered that market by acquiring the department store chain SAGA (Sociedad Andina de Grandes Almacenes), a Colombian company which was well known locally and which had two stores in the city of Lima. The company began operating under the name SAGA Falabella, retaining local management and incorporating processes and best practices applied in Chile (Bianchi, 2002, p. 7). Thus, the strong position of the SAGA brand, the existing managers' knowledge of the market, the presence of a culture of shopping in department stores, and the fact that Falabella was regarded as a local company by Peruvian consumers enabled it to begin turning a profit very quickly (Falabella, 2004b, p. 38). As in Argentina, those results were boosted by the introduction of the CMR credit card, the company's travel agency and the sale of insurance.

In view of Falabella's success, one of its main Chilean rivals, Ripley, began to expand into Peru in 1997. The new competitor, applying the same strategy it had used in the Chilean market, opened its first shop in Lima at the Jockey Plaza shopping centre, where Falabella also had a store. In Peru, Ripley sought to build up its corporate image among higher-income consumers before approaching lower-income segments.

In a bid to cope with this new situation, between 1996 and 1998 Falabella expanded and remodelled its existing facilities, opened two new shops in Lima and set up a distribution centre. The company also worked to maintain good relations with its domestic suppliers (almost 50% of its purchases were local), while at the same time ensuring close coordination with the purchasing department in Chile, as a way of creating synergies in volume purchases from foreign suppliers (Bianchi, 2002, p. 8).

Table VI.7
NUMBER OF RETAIL STORES, BY BUSINESS SEGMENT
AND COUNTRY, 2000-2005

	Falabella			Cencosud			Ripley		
	1998	2000	2004	1998	2000	2005	1998	2000	2004
Department stores									
Chile	26	29	33	-	-	21	14	23	29
Argentina	4	5	5	-	-	-	-	-	-
Peru	4	4	8	-	-	-	1	4	7
Home improvement									
Chile	2	5	54	2	3	16	-	-	-
Argentina	-	-	-	8	14	25	-	-	-
Peru	-	-	1	-	-	-	-	-	-
Colombia	-	-	8	-	-	-	-	-	-
Supermarkets									
Chile	-	-	8	3	4	119	-	-	-
Argentina	-	-	-	8	10	248	-	-	-
Peru	-	-	3	-	-	-	-	-	-

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information from Falabella, Cencosud, Ripley and Farmacias Ahumada.

The economic situation began to deteriorate, affecting the balance sheets of the two Chilean firms' Peruvian subsidiaries. In response, both Ripley and Falabella launched new expansion drives involving major changes in their strategies. In 2000, Ripley introduced a new low-price, self-service format (Max). This strategy enabled it to work with segments of the Lima population that its competitor had not yet reached. Meanwhile, Falabella was opening smaller stores (SAGA Falabella Express) in an effort to explore the company's potential market in other parts of the country. Using smaller shops and a tailor-made selection of products, the company sought to identify the needs and preferences of consumers in the northern part of the country and to introduce the CMR credit card. Falabella soon opened premises in Trujillo—the largest city in northern Peru—and in Chiclayo, Piura and Arequipa.

Coming on top of the difficulties in Peru, the sharp downturn in the Argentine economy destabilized Falabella's and Cencosud's plans. Falabella put a freeze on new investment and announced that it would not open any more new stores in Argentina, but would instead concentrate on improving the commercial management and efficiency of its operations (Falabella, 2001, p. 19 and *El Mercurio*, 5 April 2002). One of the major measures implemented by the Chilean firm was a sharp cutback on imported merchandise, which is replaced with local products that were more suited to Argentine tastes. This gave it a considerable competitive advantage (Falabella, 2004b, p. 37). Falabella also sought to improve its communications strategy and capitalize on the economies of scale generated by its joint operations in Chile and Peru (Falabella, 2001, p. 19). The department store format also proved to be highly convenient and advantageous for Argentine consumers during the economic recession because they could use the CMR credit card for their purchases (Falabella, 2004a, p. 14).

Unlike Falabella, Cencosud continued to grow but focused its efforts on expanding into other parts of the country, expanding its activities into the real estate business and locating its stores in somewhat smaller shopping centres (Neuquén and Mendoza), as well as extending its Easy chain. In 2002, Cencosud bought the four stores that the United States chain The Home Depot had owned in Argentina for US\$ 105 million (Cencosud, 2003, p. 15). Cencosud succeeded in becoming one of the largest shopping-centre management companies and the leader in Argentina's home-improvement and building-materials sector.¹⁴ The devaluation of the peso forced Easy to substitute local products for imports and use a greater number of local suppliers.¹⁵ This situation also provided an opportunity to add new products in its stores in Chile and thus activate scale-based purchasing synergies (Cencosud, 2004, p. 36).

The troubled economic situation in Argentina and Peru in the early 2000s held back the international growth of Chile's largest retailers, but they did succeed in growing and strengthening their positions in the Chilean market while introducing major changes in their business development

strategies. Given the small size of their domestic market, they realized that they could not expand enough if they confined their businesses to a single segment, so they began to broaden and diversify their product ranges in order to create synergies among different lines of business. Thus, while global operators were specializing and standardizing their formats, a new variant—integrated retail—began to emerge in Chile's retail trade industry.

It was Falabella that took the first steps in this new direction. In the late 1990s it moved into the home-improvement segment in partnership with the United States firm The Home Depot and acquired 20% of the Farmacias Ahumada (FASA) chain, a specialized company with an interesting growth strategy (see box VI.3). In 2001, Falabella bought out its partner, The Home Depot, and created HomeStore. Two years later, it merged HomeStore with Sodimac, Chile's largest company in that segment. This transaction indirectly boosted Falabella's internationalization campaign, thanks to Sodimac's presence in Colombia.¹⁶ Falabella subsequently expanded into the supermarket segment, initially in Peru, through the creation of the Tottus hypermarket chain, and then quickly extended that venture into Chile.¹⁷

Box VI.3

FARMACIAS AHUMADA (FASA): FROM A NEIGHBOURHOOD PHARMACY TO THE LARGEST PHARMACY CHAIN IN LATIN AMERICA

In less than 35 years, FASA has grown from a traditional pharmacy to the biggest chain of pharmacies in Latin America and one of the world's 10 largest, with operations in Brazil, Chile, Mexico and Peru (FASA, 2005, p. 7; *Chain Drug Review*, December 2002). It is also one of the few companies to have successfully implemented an internationalization strategy in this particular retail market, in which the market leader is the British company Boots Group PLC.

In recent years, Chile's pharmacies have been undergoing an intensive consolidation process in a highly competitive atmosphere, with the three largest chains together covering more than 90% of the market. Unlike its Chilean competitors, FASA realized that the independent pharmacies' shrinking market share and the growth of pharmacy chains would translate into fewer opportunities for growth within Chile. The company therefore embarked upon an active internationalization process, seeking new markets that would bring profitable growth and enable it to benefit from the synergies generated by its size and experience (FASA, 2005, p. 7). Entering highly fragmented

and dispersed markets, FASA was able to expand its market share rapidly, thanks to cost advantages resulting from its greater volume of business, the implementation of technological and logistical improvements, and marketing campaigns (FASA, 2002, p. 29; FASA, 2003, p. 49).

FASA began its internationalization drive in 1996 when it entered the Peruvian market, where, jointly with local investors, it set up the pharmacy chain Boticas FASA S.A. In 2000, together with AIG Capital Partners Inc., it acquired 77% of Drogamed, the largest pharmacy chain in the Brazilian state of Paraná, for US\$ 25 million. The following year, in order to take full control of its affiliates in Brazil and Peru, FASA acquired 15% of Boticas FASA and, jointly with AIG, 23% of Drogamed. In early 2005, FASA bought the remaining 35% of Drogamed from AIG, thereby converting it into a wholly-owned subsidiary.

In 2002, FASA acquired a majority interest in the Mexican company Far-Ben S.A. de CV by subscribing to a US\$ 45 million capital increase. In 2003, FASA strengthened its operations, taking over Farmacias

Benavides, which operated in the north of the country, with very good results. This doubled the size of the business in terms of sales, customers and numbers of stores.

Thus, using different internationalization strategies tailored to each market, from entirely new operations in Peru (Boticas FASA) to the takeover of chains in Brazil and Mexico (Drogamed and Farmacias Benavides), FASA has been able to boost its operations in record time. As of now, after more than eight years of international expansion, over 60% of the company's consolidated earnings come from abroad and over 71% of its customers are outside Chile.

This international expansion effort was not trouble-free, however, particularly in Brazil. In January 2006, following five years of losses, FASA sold its Brazilian subsidiary to local investors. Complicated regulations, high taxes and commissions, the level of informality and the difficulty of adapting to local idiosyncrasies had turned its operations in Brazil, the world's sixth-largest consumer of pharmaceutical products, into a nightmare (*Qué Pasa* magazine, No.1818, 11 February 2006).

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

¹⁴ The Argentine shopping-centre market basically comprises two large operators, Cencosud and IRSA-Alto Palermo Centros Comerciales, which cover 60% of the gross rentable space in commercial premises of that type.

¹⁵ Before then, some 30% of the products sold in their shops were of foreign origin.

¹⁶ In 1994, the original owners of Sodimac formed a joint venture with the local group Corona to introduce the HomeCenter franchise into Colombia. Falabella currently owns 35% of the joint operation and runs eight stores, achieving nationwide coverage and consolidating its position as the leader of the sector in Colombia (Sodimac, 2005, p. 25).

¹⁷ In 2004, Falabella entered the supermarket business in Chile by acquiring 88% of Supermercados San Francisco, the country's third largest chain, for US\$ 62.5 million.

Cencosud then began to implement a similar strategy. First, it sought to extend the geographical coverage of its supermarket chain in Chile and diversify its format. To that end, it bought local chains such as Santa Isabel, Las Brisas and Montecarlo (Cencosud, 2005, p. 13). Then, in March 2005, Cencosud made its boldest play, taking over Almacenes París, Chile's third-largest department store chain after Falabella and Ripley.¹⁸ As a result, like Falabella, Cencosud established a broad base in retail trade that enabled it to generate synergies and coordinate the company's assets, especially in the non-banking credit business—Cencosud (Jumbo) and Almacenes París together have about 4 million credit card holders—and in Banco París.

Cencosud and Falabella have thus made considerable progress in developing an integrated model of supermarkets and department stores (a strategy which has also been very successfully implemented by the Spanish chain El Corte Inglés). The integrated retail concept had been applied most intensively on the domestic market, but when the economic situation in a number of Latin American countries began to take a turn for the better, this new strategy began to be applied to operations outside Chile as well, and Falabella and Cencosud have shown great interest in continued expansion into relatively undeveloped market segments or niches in other countries in the region.

- In less than two years, Falabella has very successfully replicated its business model in Peru, opening three Tottus hypermarkets, two Sodimac Home Center home improvement stores, and it plans to open up six more in the next two years (Sodimac, 2005, p. 24), along with four new Saga Falabella department stores. Its plans for expansion in Argentina include the launch of two new department stores in Florida Street, in central Buenos Aires (*La Nación*, 17 December 2005). In Colombia, using a format that hardly exists at all in that country, it plans to open three new Sodimac stores and four Falabella department stores.¹⁹ The company is also looking closely at new opportunities

in Ecuador and the Bolivarian Republic of Venezuela (*Business Latin America*, 14 November 2005).

- When the first signs of a recovery in Argentina began to appear, Cencosud saw a chance to increase its market share and expand the geographical coverage of its operations in that country by buying the Disco supermarket chain, the second largest in Argentina, from Royal Ahold, an operator which was in serious difficulties.²⁰ It soon began to show its strength in Argentina, where it was competing with two worldwide market leaders, Wal-Mart and Carrefour, achieving a 22% market share. Furthermore, following the acquisition of Almacenes París, the company decided to step up its internationalization drive by taking advantage of the shopping-centre platform it already had in Argentina.²¹ Almacenes París plans to open stores in Colombia and Peru in 2006 (*Business Latin America*, 14 November 2005).
- Ripley has also continued to seek opportunities for diversification and may follow Falabella's lead in the supermarket segment in Peru before turning to the Chilean market. The company has announced that it will give a new boost to its international expansion. To that end, it is targeting other Latin American countries which are accessible in terms of potential and size, such as the Bolivarian Republic of Venezuela, Colombia and Ecuador (*El Mercurio*, 19 June 2005).

Chile's top retail-trade companies may continue to expand their geographical and segment coverage. Ambitious investment plans for the coming years have already been announced, especially by Falabella and Ripley, each of which intends to invest over US\$ 550 million in 2005-2007 (*Estrategia*, 18 July 2005, and *El Mercurio*, 28 July 2005). These companies' expansion plans, both past and future, have involve a complex feat of financial engineering that has combined internal cash generation, bank loans, bonds and equity issues in order to finance such operations. Even so, the corporations

¹⁸ On 31 August 2005, shareholders' meetings of both companies approved the merger of Cencosud and Almacenes París, the latter being taken over by the former.

¹⁹ To that end, Falabella, together with the Corona group, its partner in Sodimac, intends to invest some US\$ 100 million (*El Mercurio*, 28 July 2005).

²⁰ In early 2004, Cencosud successfully completed its first issue of shares and American Depositary Receipts, equivalent to 21% of its value, thereby raising US\$ 332 million. Using these funds, it concluded an agreement with Royal Ahold one month later, acquiring an 85% share in the country's second largest supermarket chain, Disco SA, for close to US\$ 315 million. The successful completion of this transaction occurred only after a number of legal battles, however, and the attempt to merge with Jumbo was unsuccessful (*El Clarín*, 29 April 2005). Nonetheless, and even during the especially difficult period that followed the purchase of Disco and the remodelling of the Jumbo stores (where it invested over US\$ 500 million), Cencosud became the second largest supermarket operator in Argentina, with close to 22% of the market (Cencosud, 2005, p. 63 and *Estrategia*, 2 November 2004).

²¹ As with Easy and Jumbo, Cencosud plans to open an Almacenes París store in each of its shopping centres in Argentina. This process will begin in early 2006 with the opening of an Almacenes París store at Unicenter in Buenos Aires, to compete with Falabella (*La Nación*, 17 December 2005).

show acceptable and well-defined levels of indebtedness. Cencosud has experienced the greatest difficulties in that respect, and its level of indebtedness was very high following its recent expansion, but it has been able to turn the situation around quite rapidly.²²

In sum, Chilean retailers have achieved solid competitive advantages using a business model based on the synergies among related activities, a strong customer orientation and a powerful financial dimension. The development of this integrated retail formula has been the direct result of the intense competition existing in the Chilean market, whose size makes it very difficult to run a profitable operation in just one segment of retail commerce. The key to success has therefore been to combine local knowledge with the best international practices, a diversified product range that includes banking services, and a strategy for surviving in a highly competitive market. These companies have thus consolidated broad local coverage with a growing presence abroad, mainly in Argentina and Peru.

The Chilean companies have applied the central elements of their home-market strategies in their

international expansion, but they have also made some changes in order to tune into local consumers' tastes and habits and to win acceptance. To this end, they have worked with local partners, established long-term relationships with local suppliers and recruited local staff in the countries where they are investing. Many of these changes have been implemented during economic crisis in those countries. Then, as the economic outlook has improved, the Chilean companies have accelerated the internationalization of their operations.

As a result, for the first time ever, two Chilean corporations are now listed among the world's top 250 enterprises in this sector: Falabella (228th) and D&S (239th) (Deloitte, 2006). Cencosud is set to join them on the list, with total sales estimated at over US\$ 3.2 billion following its merger with Almacenes París.

This business model also has some limitations in terms of international growth, however, especially in larger markets. It is therefore expected that their international expansion will continue gradually, but will be restricted to markets of a size that makes them accessible to the Chilean companies.

Box VI.4

ENTERTAINMENT AND THE MEDIA: EXPORTING LATIN AMERICAN CULTURE?

Outdoor entertainment: CIE

The Corporación Interamericana de Entretenimiento, S.A. de CV (CIE), founded in 1990, is Latin America's largest provider of outdoor entertainment for the Spanish- and Portuguese-speaking markets. It produces events such as live concerts, theatrical productions, sporting events and games, as well as managing amusement parks, advertising these events and running ticket sales. Vertical integration, a strong capacity for coordinating suppliers, a sophisticated information management system and access to facilities for holding such events are among the company's advantages in relation to its competitors, which are mostly smaller, local companies. Its internationalization drive began in the late 1990s, and it now promotes events in Argentina, Brazil, Chile and the United States. It also operates entertainment centres in Argentina and Brazil, amusement parks

in Colombia and the United States, and the Buenos Aires zoo.

The company has call centres in Colombia and Panama for ticket sales. Until 2004 it was also operating in Spain, but it left that market in the face of fierce competition and the high cost of obtaining permits and access to entertainment facilities. Its varied activities give its customers an advantage in terms of contacts and relations with entertainers, for whom transaction costs are lower when they deal with a single company. Like other trans-Latins, CIE is a vehicle for Latin American products (cultural products, in this case) in the United States, as well as for United States products in Latin America and the Caribbean. Also like other trans-Latins, CIE has sought to diversify its activities and geographical markets as part of its risk-reduction strategy. Currently, 15% of its sales and 20% of its assets are outside Mexico, whereas the corresponding figures stood at 30% five years ago. Mexico has nonetheless been a

higher-growth market than its other areas of operation, and the company expects this to continue to be the case.

Indoor entertainment: the Televisa and Cisneros groups

In addition to their activities in other sectors, the Mexican group Televisa S.A. and the Venezuelan Cisneros group are active in the indoor entertainment segment, which includes the production and distribution of music and of content for television and radio. Like CIE, these companies have taken advantage of cultural similarities within the region and among Spanish- and Portuguese-speaking communities in Europe and the United States. They also broadcast content from other countries, mainly the United States, on paid or open television channels in the region via satellite or cable and, increasingly, on the Internet. They also broadcast content from Latin American countries in the United States.

²² In January 2005, an increase in the company's capital was agreed, to pay for part of the purchase of Almacenes París. In March 2005, including the liabilities of Almacenes París, Cencosud's financial debt stood at US\$ 1,156,000,000, 40% of which was short-term borrowing (Feller-Rate, 2005, p.2). In June the same year, Cencosud sold 38.6% of Disco and Jumbo to various institutional funds for US\$ 130 million, and the company subsequently adopted a debt refinancing plan worth US\$ 530 million.

Box VI.4 (conclusion)

Televisa group

The Televisa group first moved into the international sphere in 1988, transmitting news programmes in Spanish to the United States, Central and South America, Western Europe and North Africa. In 1992, in partnership with the Cisneros group and the entrepreneur Andrew Jerrold Perenchio, it acquired an unconsolidated shareholding in Univisión, the largest Spanish-language television company in the United States, where it broadcasts about 70% of its content during prime time. Through Televisa Estudios, which has affiliates in Europe and the United States, it markets television content worldwide. Through Innova, the result of a strategic alliance among Televisa, News Corporation, Liberty Media and Globopar (Brazil's

largest television and media group), it also does business in the direct-to-home (DTH) satellite television sector.

Cisneros group

The Venezuelan Cisneros group is involved in various activities in the entertainment sector, where it has a large proportion of its assets. It has a stake in Venevisión, the country's leading television channel. In 1992 it acquired a shareholding in Univision Communications Inc., the largest Spanish-language content provider to the Hispanic audience in the United States, and in that same year it purchased Chilevisión. In 1994 it acquired Caribbean Communications Network, a leading media company based in Trinidad and Tobago, and in 1996 it

set up the Cisneros Television group to distribute Latin American television content internationally. Since 1997 it has owned a stake in Caracol Television, Colombia's leading network and the country's main content producer. Through Venevisión Continental, established in 2000, it distributes programmes from Caracol, Venevisión, Univisión and Chilevisión throughout the continent via satellite. In the direct broadcast ("direct-to-home") satellite television segment, it established DirecTV Latin America in 1996, in partnership with GM Hughes Electronics. The Cisneros group holds the Blockbuster franchises for Puerto Rico, as well as music labels and other television- and music-related businesses. Through Venevisión International Theater, it is also becoming involved in the outdoor entertainment segment.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

D. Conclusions

A first generation of companies in the services sector began to internationalize their operations in response to the contraction of their domestic markets. Others have seen opportunities in the privatization and deregulation of traditional sectors and in the development of new services. While the customers of the first generation were companies and governments in various parts of the world, the main market for the others has been Latin America and the Caribbean.

One of the principal competitive advantages for the first generation of companies in the engineering and construction sectors was their management's ability to operate in the economically, financially and legally complex environments characteristic of many developing countries, which have the greatest shortfalls in infrastructure and therefore the greatest potential demand for such projects. These companies moved on from their projects in emerging markets to do business in developed countries. For Brazilian companies, which are prominent in that group, growth on the domestic market as government suppliers (as well as supplying private enterprises) played an essential role in allowing them to attain the size and experience needed for successful internationalization. This has in turn contributed to their growth and helped them to reduce the risk associated with limiting their operations to a single, often turbulent, market.

In the public utilities sector, the reforms in Chile, which preceded the reform process in other countries,

gave that country's electric power companies an initial advantage for their expansion in the region, since they were able to combine their knowledge of markets that were relatively similar to their home market with their expertise in post-reform operations. Those advantages were relatively short-lived, however, and the great majority of Chilean firms in that sector became "shooting stars" that were taken over by foreign companies.

In telecommunications, the Mexican firms TELMEX and América Móvil have met with notable success, even when competing with transnational giants. These companies' strong positions in Mexico, backed up by State policies, have been crucial for their international expansion. In retail commerce, fierce competition on the Chilean market caused companies to seek solutions that would leverage synergies among different segments. The resulting model, with some modifications, has been exported to neighbouring countries and has generally met with success.

A common characteristic of those last two groups of companies, which also include enterprises in the airline transport, retail commerce and entertainment sectors, is that their business is almost entirely limited to the region or to bringing services to Latin Americans living abroad. As in the food and beverages sectors, there appears to be a set of Latin American consumer habits that gives a competitive advantage to the region's companies.

* * *

In summary, the Latin American and Caribbean region can be said to have produced a relatively small number of emerging TNCs which are less internationally competitive than their Asian counterparts. The largest and most competitive trans-Latins having the greatest international presence are concentrated in basic industries. Their competitiveness generally derives from the comparative advantages of their home countries, strong initial support from the State and the experience they have gained along the way. Trans-Latins involved in non-resource-based manufacturing or services have not achieved such good results relative to the size of their companies, their international presence and their competitiveness, although there are some significant exceptions, such as América Móvil.

This last group of more technically sophisticated companies has had to deal more directly with the major TNCs in their sectors, and this has forced them to react in the face of stronger competition. Some companies have avoided this competition by occupying market niches or obtaining greater protection from the governments of their home countries. Others have sought to associate with TNCs without losing control over their operations, while still others have been absorbed by TNCs through acquisitions.

Aside from the relative scarcity of major trans-Latins in the sectors of non-resource-based manufacturing and services, the region has had a considerable number of “shooting stars”: trans-Latins which have the potential to become TNCs but which have lost that potential following their acquisition by international operators. This trend has been especially notable in certain manufacturing industries, such as food and beverages, vehicle parts and public utilities such as electric power supply. In many cases, once trans-Latins in these sectors have reached a certain size and geographical coverage, they have become priority targets for TNCs seeking a quick way to build a strong presence in the region or subregion.

After two decades of economic reforms designed to liberalize and open up the economies of Latin America and the Caribbean, trans-Latins weak international competitiveness and the proliferation of “shooting stars” have revealed some shortcomings in that process. The main problems are rooted in local private firms’ limited capacity to incorporate modern technologies and organizational practices and to form profitable links with TNCs while still retaining control over their operations. In order to overcome these problems, local private enterprises will need to strengthen their capacity to absorb new technologies and to increase their negotiating power, and the region will have to attract higher-quality FDI.

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