INDUSTRIAL COMPETITIVENESS POLICIES:
THE LOCAL DIMENSION

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ABSTRACT

The local dimension has been given only secondary, peripheral importance in the debate on policies to promote competitiveness and has been relegated to the sidelines or ignored in policy design and implementation. The main thesis of this paper is that the time has come to integrate these two areas of thought and action. If such integration were achieved, policies to promote competitiveness would gain in terms of specificity and implementation by giving a central place to the territorial and local dimensions. By the same token, policies that have developed within the tradition of analysis at the regional or local level could achieve a much greater degree of realism by drawing on the major elements of the debate on policies to promote competitiveness. The time is ripe for a synthesis that would be highly positive for both analytical approaches.

In support of this thesis, this paper first describes the current situation of policies to promote competitiveness in Latin America and the Caribbean (LAC), that is to say, what policies are being discussed, designed and implemented in the region in the second half of the 1990s. It then examines aspects of that situation which can contribute to a better design of local-level policies. Lastly, it presents a number of pending issues under the heading of “The current debate”.

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1 In this paper, the terms “region” and “regional” may refer, depending on the context, to Latin America and the Caribbean or to regions of a given country.
1. Policies to promote industrial competitiveness

Why should we start this analysis with a description of the current situation of competitiveness policies in the region? The answer is that, just as most of the policies to promote competitiveness now being implemented in LAC are strongly influenced by macroeconomic policy, it is also extremely unlikely that any country will adopt local policies of a major significance that may conflict with its overall approach to the promotion of competitiveness. It is essential to bear this in mind if significant policies of local or regional scope are to be implemented.

As it is shown by Peres (1997), most of the LAC countries have moved away from sector-based industrial policies towards policies to promote industrial competitiveness. This step has important implications, since it signals a shift of emphasis away from the creation of new production sectors and towards the quest for efficiency in already existing production sectors. In the import-substitution policies of the past, as well as in the local policies aimed at the creation development poles, the focus was always on the creation of new production sectors. Today, however, the main emphasis in the LAC region is on raising efficiency in existing industries and service sectors.

This is an important issue that will affect the content of local policies in LAC. As reported by Katz and Stumpo (1996), the majority of the large and medium-sized countries of the region are gradually restructuring their industrial sectors, reorienting them towards industries engaged in the exploitation or processing of natural resources; the most important exceptions to this trend being north-central Mexico, Central America and the Caribbean, where the focus tends to be on low value-added assembly-line, manufacturing activities which are conducted by firms in export processing zones (maquiladoras) assembling goods for the US market. The emphasis on natural resources and natural resource-based products is relevant because it limits the degrees of freedom for the development of new competitive advantages and affects one of the touchstones of policies of local scope: the development potential of small enterprises. This question is dealt with later on in more detail.

Another important aspect of current developments regarding policies to promote competitiveness is that, until a decade ago, too much emphasis was placed on the distinction between interventionist and non-interventionist governments in LAC. By the mid-1990s, even governments with little or no inclination towards interventionism have been led to adopt policies that frequently go beyond the mere reinforcement of market mechanisms in order to exploit static comparative advantages. There are two reasons for this. In some cases, the depletion of specific natural resources—one example is coal in Chile—has had local consequences that have forced non-interventionist governments to adopt policies to promote competitiveness. In other cases, trade integration has brought about changes in the basic rules of competition—between Mexico and the United States, Venezuela and Colombia, and Brazil and Argentina, for example—which have led governments with no interventionist leanings to design policies to offset the negative consequences of integration or maximize its positive outcomes.
It may well be that trade integration has been the single most important factor in galvanizing the region into the discussion and designing of policies to promote competitiveness. The contrast between the situation as it stood when such policies were absent from decision-making in the region, prior to the commencement of negotiations on the North American Free Trade Agreement (NAFTA) in 1990, on the one hand, and the rich experience that has grown out of NAFTA, the Southern Common Market (MERCOSUR), the revitalized Central American Common Market (CACM) and trade integration between Venezuela and Colombia, on the other, clearly indicates that trade liberalization and integration have played a decisive role in reawakening interest in the design of industrial competitiveness policies.

To conclude this description of the current policy context in the region, it is important to note that the countries are now mounting an effort to set aside the practice of drawing up long lists ("laundry lists") of necessary conditions for competitiveness and are instead trying to identify a limited number of conditions that would be sufficient for its achievement. Less than a decade ago it was still the case that a paper on competitiveness would typically dwell on a large list of all the factors involved in increasing national or enterprise competitiveness; this type of approach has paralyzed decision-making and policy implementation. Although some progress has been made since then, this inability to establish priorities for policy and action is still one of the region’s main weaknesses.

This is the overall policy framework for the majority of the countries of the region. For purposes of illustration, it may be useful to examine the most significant developments in this connection that took place in 1996. First, four countries—Colombia, Bolivia, Peru and, more recently, Venezuela—have based an important part of their policy design efforts on Michael Porter’s methodology for analyzing the competitive advantage of nations (Porter, 1990). 2 Central American countries are also moving in the same direction.

In those countries, recommendations based on Porter’s methodology serve as the starting point for the debate on policies to promote competitiveness. This is important, for this framework offers a new approach for the analysis of the local or regional dimension. Indeed, in Colombia, where work on proposals based on that approach began in 1990, a National Competitiveness Council was established in August 1994 to draw up a detailed national strategy for the attainment of that goal, and one of the committees set up by that Council was precisely aimed to developing local- or regional-level policies.

A different approach has been adopted in Chile and Argentina, where the emphasis is on promoting and responding to business demand for technology diffusion, human resource training, export promotion mechanisms, etc., and, in particular, on fostering the development within civil society of bodies such as chambers of commerce and other intermediary organizations that can help to implement horizontal policies of this kind. Chile has made more progress in this area; in Argentina, the idea has gained a certain currency at the proposal level but its implementation lags somewhat further behind.

2 This work was usually carried out with the financial assistance of the Andean Development Corporation (CAF).
Still other approaches have been adopted in the region’s two biggest countries, Brazil and Mexico; industrial policy programs were issued in both countries in 1996. In Mexico in particular, the hallmark of the new policy is that it fully incorporates the experience gained from working within NAFTA. It is clear from Mexico’s growth pattern, which has been shaped by its trade integration with the United States, that opening up the economy has raised the efficiency of certain manufacturing sectors considerably but, at the same time, has severed production linkages. Ultimately, the formation of efficient production chains—a phrase that smacks strongly of the 1970s and early 1980s—is what will constitute the basic thrust of Mexico’s industrial policy through the end of the decade.

In addition to the above-mentioned approaches, three other policies have come to prominence in Latin America, albeit to differing degrees, since in some countries they well established, while in others they are only just beginning to become a focus of serious analysis. These policies are: i) privatization, a process which is widespread and is nearing completion in a few countries, but is just getting under way in others; ii) deregulation, where progress has also been very uneven; and iii) competition policies, which, with the exception of one or two countries, is still on the drawing board stage or at a low level of implementation. The incorporation of a gender approach into competitiveness policy design and implementation is just beginning.

2. Building bridges

So, local- and regional-level policies must be designed and implemented in a Latin America where a number of elements interact: policies based on Porter’s methodology, an emphasis on promoting private sector demand for services, a renewed interest in stronger linkages within production chains, and an interest in privatization, deregulation and competition. In these framework, there are five factors that may help to bridge the gap between local and competitiveness policies.

First, it is important to give serious thought to the problematic relationship between local policies and local participation. Some confusion has arisen between the notions of decentralized and participatory policies because it is assumed that decentralized government agencies are more democratic and allow more participation than centralized ones, but there is very little evidence to support this assumption in Latin America and the Caribbean.

In this respect it is helpful to divide policies into three groups: i) centralized policies with a local impact, i.e., traditional industrial policies that are handed down from the central government but have a significant impact at the local level; ii) decentralized, non-participatory policies, since the fact that a policy is decentralized and that power has been transferred from the center to an intermediate body such as a state or a municipality is no a priori guarantee of a greater degree of participation; and iii) the area of greatest interest for future analysis and action, which is the potential scope of genuinely participatory—i.e., bottom-up—policies, as part of a truly democratic approach to industrial policy, as suggested in Cowling and Sugden (1994).
The second factor is the actual impact of the new economic model in place in the region. In opposition to import-substitution industrialization which was clearly based on large urban markets supplied by large companies, it is hoped that export-led growth based on small enterprises—that is being encouraged under the new model—will permit a more rapid local development.

This having been said, some thought needs to be given to the kind of industries or sectors in which Latin America is specializing. As mentioned before, with the exception of Mexico and those countries where maquiladora industries are strongly present, the countries of the region are specializing in exports of paper and pulp, edible oils, petrochemicals, mineral resources that have undergone a minimum of processing, and products of other large-scale, continuous-process industries, that is to say, non-labor-intensive activities. Thus, the expansion of large-scale industries, which underpin the region’s export development, will not have much impact either on the level of employment or on the its geographical distribution. Indeed, the activities that are leading growth and exports in the 1990s are among the ones that have the least impact on these variables.

The assumption underlying many local policies in Latin America and the Caribbean is that small enterprises will be the driving force of the export-led growth model, or, more specifically, small metalworking companies members of subcontracting chains that serve large-scale assembly industries. Yet this is not the case in such sectors as pulp, soybean oil, iron ore or petrochemicals. That kind of situation is found, on the other hand, in the automotive industry, consumer electronics and telecommunications equipment, and that is why significant changes in the regional structure of industry are taking place in countries such as Mexico, where, thanks to the importance of industries that lend themselves to the formation of links between small enterprises and export development, the new model is bringing about a much more significant shift in the localization of production. This is a key point: due account needs to be taken of the sectors in which Latin America is specializing in order to forecast what form development is likely to take.

A third factor is that today, whenever the issue of policies to promote competitiveness is raised, the question of the restrictions imposed by the World Trade Organization (WTO) regime also arises. The WTO regime allows for subsidies in only three groups of activities (categorized as “green”): environmental protection, support for pre-competitive technological research and promotion of regional development. The fact that WTO accords “green” status to activities in support of regional development is of high importance to countries or economic agents interested in defending their capability to provide or receive direct support in the form of subsidies. On this point, it should be taken into account that, although in some countries even to mention subsidization is regarded as almost “sinful”, others regard subsidies as a normal and self-evident practice.

A useful illustration of the shift that has taken place in the approach to local development policies and instruments is to be found in the divergence between what could be called the “old-style” and “new-style” approaches to local policies from the standpoint of the promotion of competitiveness. The “old-style” view is exemplified by the policy Mexico issued in 1983,
whose very name was quite revealing: industrial localization policy. Its objectives and instruments were typical of the “old-style”.

The 1983 policy was designed and adopted by central decision-makers, who afterwards negotiated it with states and municipalities, as if unaware that whoever wrote the first draft and set the agenda would largely determine the outcome. At the time, however, it was claimed that the policy was a participatory one merely because other levels of government had been consulted.

The major instruments of this policy were public-sector investment in infrastructure and industrial parks, which would stimulate employment and attract investment to the regions. Naturally, fiscal and credit incentives were also taken into account. Fiscal support took the form of relocation incentives (as also occurred in many other countries of the region), while credit was accessible, as always, only for medium-sized or larger enterprises. In addition, companies were offered another very powerful incentive, which in many cases tipped the balance: in order to encourage industries to locate their facilities in a particular area, land-use regulations were eased, water and energy charges were reduced and, explicitly or implicitly, the enforcement of environmental regulations was relaxed. This type of relocation policy was typical 10 or 15 years ago, when a precise industrialization model was predominant, which included an well-defined local policy component.

The “new-style” approach — as exemplified by Mexico’s 1996 industrial policy, to which reference was made earlier — incorporates some interesting changes. In the first place, the new policy does not address regional or local development as a specific policy area. Yet it is far more realistic on this score than the 1983 policy was. Why? Because it is based on the idea that the changeover to a new development model will lead to the establishment or emergence of clusters of firms, whose local impact will be different from that prevailing under the earlier model. In other words, the aim is not to tamper with the industrial location patterns generated by the new model, but rather to be aware from the start of the pattern that will take shape and, in the light of that awareness, use development instruments to shorten the adjustment time and reduce transition costs.

Rather than taking local objectives and goals as the bases for deciding which industries to attract, the new approach is more realistic: it determines what industries are being stimulated by the new economic model, and then assesses what the local impact of that dynamic will be and how adjustment times and transition costs can be minimized.

The effects of the new model are sure to vary widely from country to country in LAC. The local dimension is likely to develop in completely different ways even among very small countries such as El Salvador and Costa Rica (which specialize in the assembly of manufactures for export by maquiladora industries that have only tenuous links with the activities supplying domestic markets), and Uruguay (which specializes in processing agro-industry products that have strong linkages with the country’s production structure). Thus, the most intelligent approach is to decide where the economic dynamic is leading to and then anticipate its impact at the local level.
In much the same way as the Mexican policy does, approaches based on Porter’s methodology also regard clusters of industries in particular location as hubs of competitiveness. An example is provided by the work done by the Monitor Company on Cali’s printing and graphic industry or Arequipa’s textile sector. Such work bridges the gap between the analysis of the conditions that prevail in each local context and the analysis of the cluster that may exist in that context. There is much to be learned from studies that have adopted this approach.

Fourth, another promising, although fairly recent, step towards bridging the gap between these two approaches is the fact that, in various regions in a number of Latin American countries, business associations have taken the initiative in designing and promoting a strategic model for action at the local level. There are many examples of this trend, but two are of particular interest. One is the Foundation for the Development of the Cauca Valley, an organization that operates in parallel with the Cali Chamber of Commerce. The Foundation has devised a development strategy whose value lies not only in its intellectual merits, but in the fact that the work required to develop a strategy for that region was planned and funded by a business association. Another very interesting initiative is under way in Valencia, Venezuela, where the Industrial Association of the Carabobo State intents to address a number of issues that are generally regarded as being far removed from the local dimension, but that nonetheless have a significant impact on the Association’s members. Of particular note are the internal organizational changes which the Association has programmed so that it can make effective use of information on dumping and unfair trade practices that might affect its region’s export products. Since it felt that such information was not going to be managed adequately by the central government, the Association decided to take on the job of preparing analyses and submitting proposals for the defense of fair trade practices in its members’ sectors of activity.

Experiences such as these need to be taken into account, for they are examples of clusters in action, with cities, firms and industries all taking part in the work of designing policies that will meet their needs.

A fifth consideration is that, in order to make progress towards an approach that will integrate the promotion of competitiveness with territorial development policies, it may be useful to recall, as pointed out by Alburquerque (1997), that the concepts of endogenous development (based on the territorial dissemination of technologies rather than purely on innovation per se), responsibility of regional governments, promotion of small firms and provision of local production services are at the heart of the concept of systemic competitiveness, which has been one of the touchstones of modern approaches to competitiveness. These concepts may help to bridge the gap between policies designed to promote competitiveness and policies for dealing with local issues.

Nevertheless, this should not obscure the fact that there are at least three points on which the two approaches differ significantly. One is the emphasis on small and medium-sized enterprises based on the assumption that they are more flexible. While this is indeed an attribute of some firms of small size, it is primarily exhibited by firms that have the capacity to move forward towards flexible production or specialization models. However, in Latin America —as mentioned in Abramo (1996)— firms that work under flexible production are still the exception, even in São Paulo and Mexico City. At present, flexible production does not appear to be the
direction in which most Latin American companies are moving, even in the region's more developed geographic areas.

The second point concerns a fact already mentioned in this paper. If the Latin American countries are giving priority to such industries as paper and pulp, mineral processing or soybean oil, then it is very difficult to see how high expectations on small businesses would fit into this overall scheme.

Lastly, perhaps the most important objection to the usual sorts of local policies has to do with the definition of the level at which policies should be targeted; a question that is considered in the literature on the subject. Generally, local-policy goals and instruments focus on a particular region, on individuals or, in many cases, both. They seek to give support to different regions for geopolitical reasons, national solidarity or other similar considerations; or they provide support to individuals through training subsidies, unemployment insurance or other means to reduce the costs of adjustment. There are not many cases in which the emphasis is on the firm. This is the point where the two approaches presented in this paper diverge the most. Enterprises are necessarily going to be the link between people and regions. A policy that is closely geared to the region as a political entity or strongly oriented towards individuals may prove ineffective if it fails to take into account the constraints affecting enterprise activity.

3. The current debate

In essence, what is the current debate really about? In response, one can pinpoint five areas that usually arise in the analyses of this matter.

First, it is not clear to what extent governments are truly involved in an effort to further the scope of democratization or to what extent they are simply “making a virtue of necessity” based on a recognition that their capability for designing and implementing policies on a centralized basis is poor. This issue is important since the answer will, in large part, determine whether the strongest and most immediate (ideological) position to be adopted will be for or against these policies. Naturally, if one believes that current decentralized policies are the outcome of a process of democratization, then one's initial assessment will be totally different than if one believes that governments are just recognizing that they lack qualified staff for policy design and that, on the rare occasions when such staff are available, they lack the capacity to put those policies into practice, which would mean that they were merely passing on their responsibilities and the pressures exerted by society. This might, in the long run, strengthen the democratization process, but it is not the same thing as a genuine attempt to design participatory policies. This is an important point, and one must always attempt to determine to what extent there is a true commitment to democratization and to what extent there is merely a lack of capacity underlying the decision to pass the problem on to another level of government.

The second concern relates to the problems that decentralization can cause. There are few new developments to discuss in this regard, since the problems are “out in the open” and are not about to disappear. The experience of the European Union shows that, from the 1950s up to the early 1970s, there was a trend towards the economic convergence of the various regions within
Europe, although, it seems now clear that this trend has stalled or even been reversed. In this respect, there are no features of the current process of integration and productive specialization in Latin America that would suggest that the difference between its various regions are going to diminish as a direct result of growth. It may be that the right thing to do is to leave each region to follow its own course of development and to grow in line with its own potential, but it must not be forgotten that even greater differences will ensue.

If the different regional or local agents are allowed to compete for investments only on the basis of their relative strengths, the outcome may be a negative-sum game. Brazil is the classic, but not only, example in Latin America. In order to attract a specific investment, one state may offer a potential investor an exemption from property taxes, another may offer this incentive plus cheap energy supply, and still another may offer him a property-tax exemption and cheap energy and, in addition, may suggest that it will not strictly enforce environmental regulations. If the states or lower administrative units (municipalities or cities) use this kind of incentives to compete for a given investment, in the end the country as a whole will have received the same amount of investment, but may see a decrease in local tax receipts, the income of public utility companies, its capacity for environmental control, etc. A “fiscal war” — in the widest sense of the word “fiscal” — may be an undesirable side-effect of the competition for investments because of local empowerment, and this should always be borne in mind.

Third — and this does not relate only to local policies but mainly to policies for promoting competitiveness — very often, countries use instruments that are ineffectual. In other words, governments generally declare that their objective is country’s competitive integration within the global economy, participation in “the third industrial revolution” or a change in the territorial distribution of industry. However, one may well wonder what instruments they intend to use to achieve these objectives. Very often, their reply is that they will lower interest rates on financing for training or technology development by one or two percentage points or spend a few extra tenths of a point of GDP on technological development nation-wide.

Under these circumstances, there are only two realistic options: either one believes that the current growth dynamic is the right one, or one makes substantive changes in the allocation of resources for the promotion of competitiveness. As one Latin American president pointed out in the early 1990s, “to announce programs without the corresponding budgetary appropriations is just demagogy”. One point that emerges clearly from the European Union’s experience is that the impact of regional policies actually increased when the European Commission decided that a substantial part of the development credits would be channeled through the governments of the regions rather than through the national governments. The level at which decision-making takes place regarding those instruments that actually make a difference is where results are going to be achieved. Thus, it should come as no surprise that, where this form of participation is missing or weak, decentralization is not going to be achieved.

Fourth — and this is what leads local economies to diverge from one another — modern development theory teaches that capital is mobile, natural resources can be bought, and technology (except the most sophisticated, which is not the case for Latin America), too, can be bought; the only thing that distinguishes one region’s long-term competitive capacity from that
of another is the capabilities of its population. And the quality of local management is a crucial component of these capabilities. In this respect, there are either vicious circles or virtuous circles. If, for example, a region has good universities, this will make professionals want to live there, which means that more highly skilled people will remain in the region; this, in turn, leads to better-quality jobs, etc. The reverse is also true. Therefore, if there is one element that ought to receive priority attention, it is development of local management capacity. This is not a new idea, but it may be a pivotal element in changing vicious circles into virtuous ones, as various regions in Latin America have already at least partially demonstrated (e.g., the Araucania region in southern Chile).

Fifth, if the idea outlined above hold true, then the central question is how to tie these considerations in with the development model prevailing in the region. The best link may be a cluster-based approach, which pays attention to benchmarking cluster experiences at different points along their development path, as suggested in Ramos (1996). Ultimately, both in terms of industrial organization analysis and from the viewpoint of local policies, the main variable in bringing about a change in the distribution pattern of investment, employment and technical progress is the location of specific clusters. And, if we know anything about clusters, it is that they are not uniformly distributed throughout a territory but instead tend to be concentrated in specific sections. Consequently, a cluster-based approach to policy should be in the core of the efforts to link the territorial and the industrial competitiveness approaches.

In conclusion, the basic thrust of this paper is that the time has come to incorporate considerations based on a local perspective as a central concern in thinking about policies to promote competitiveness and thus to resist the tendency to think and act primarily with regard to competitiveness at the national level and, only later, to consider, the local impact of such an approach.
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