Market-seeking strategies predominate in the recent FDI boom in MERCOSUR countries. In the trade performance of transnational corporation affiliates a sort of ‘asymmetric integration’ is clearly visible: they produce for the internal market and, to some extent, for the regional one, while import inputs and final goods from developed countries (and a significant part of these trade flows is intra-firm). Thus, even if affiliates obtained productivity gains in the 1990s, they have not yet been reflected in a significant increase in exports, and even less in extra-regional exports. Hence, the foreign direct investment boom seemingly has not yet contributed to a better insertion of MERCOSUR countries into the world economy.

Key words: Foreign direct investment, Multinational corporations, Regional integration, Trade

JEL classifications: F23, F21, F15

1. Introduction

The share of MERCOSUR member countries (Argentina, Brazil, Paraguay and Uruguay) in world foreign direct investment (FDI) inflows increased from 1.4% in 1984–89 to 5.9% in 1997–99. This share is much higher than that exhibited by MERCOSUR in terms of world GNP (below 4%) or trade (nearly 1.5%). Hence, it seems that one of the main assets of this new trade agreement has been its capacity to attract FDI.

As a result, transnational corporations (TNCs)¹ have become the most dynamic agents in these economies—most notably in Argentina and Brazil—displacing state enterprises (which have mostly been privatised in both countries) and, to a lesser extent, large domestic conglomerates.²

¹ In this study, TNCs are firms that have made outward direct investments, irrespectively of the number of affiliates.
² It is interesting to take into account that most domestic conglomerates that survived TNCs massive expansion in the 1990s became increasingly transnationalised themselves (see Chudnovsky and López, 2000).
This FDI boom took place simultaneously with two other major changes in the region: (1) the adoption of structural reforms programmes (including the privatisation of state enterprises, the liberalisation of trade and capital flows, market deregulation, etc.);\(^1\) and (2) the beginning and deepening of the regional integration process within MERCOSUR.

In fact, the arrival of FDI to MERCOSUR—especially in Argentina and Brazil—was mainly conceived as a fundamental factor for the success of the structural reform programmes. FDI would supposedly contribute not only to the financing of balance of payments deficits but also to the productive and technological modernisation of the host economies. This modernisation should have led, among other things, to growth in both exports and imports.

This is not the first time in the history of MERCOSUR countries that FDI has been considered a fundamental factor for economic development objectives. TNCs were key agents in the import substitution industrialisation (ISI) process, especially in Argentina and Brazil, where a significant stock of FDI and a strong presence of TNCs in the manufacturing sector were already observable well before the recent FDI boom.

Although in the ISI period TNCs showed better performance—in terms of productivity, technological assets, etc.—than domestic firms, their main investment motivation was to take advantage of the highly protected domestic markets ('tariff jump'). Not surprisingly, several studies (e.g., Sourrouille \textit{et al.}, 1984) have shown that during the ISI foreign affiliates in the region had poor export performance and used technologies which were far below the international frontier. This was to be expected, since in that period TNCs operated in an environment with relatively few incentives for technological progress and efficiency gains.

The recent FDI boom took place in a different context. Argentina and Brazil, and to a lesser extent Paraguay and Uruguay, carried out deep structural reforms in line with the recommendations of the so-called ‘Washington Consensus’. These processes began and spread differently in each country. In any case, their most notorious consequence was the formal ending of the ISI regime, which in fact had been exhausted since the beginning of the 1980s.

With the new ‘rules of the game’ in force in the 1990s, when MERCOSUR economies were more open to trade, capital and technology than in the past, TNC affiliates would supposedly show strategies and behaviours different from those exhibited during the ISI period and contribute more to the economic development of the host countries. The first objective of this paper is to find out whether these differences have been observed in practice.

At the same time, it is important to find out whether TNCs and domestic firms reacted differently in terms of strategies and behaviours in the new economic environment in MERCOSUR countries. Our second objective is to discover whether TNCs’ affiliates took advantage of their technological assets and their access to foreign markets to modify their previous mostly ‘inward-oriented’ strategies more rapidly than did their domestic counterparts.

Last but not least, TNCs’ affiliates, for the reasons mentioned above, are supposed to contribute positively to the improvement of host countries’ competitiveness, a fact which

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\(^1\) It must be noted that, even in this scenario, a few sectoral policies have been put in place. This is most notably the case of the automotive sector, which has remained relatively closed to the competition of imported vehicles. Automotive policies both in Brazil and Argentina have aimed at stimulating local production through trade-related investment measures (see Bastos Tigre \textit{et al.}, 1999, for an analysis of these regimes).
should be reflected in more exports to an increasing number of destination markets. The third objective of the paper is to analyse to what extent this expected contribution has been observed in the case of MERCOSUR countries.

On the basis of these research objectives, the main questions that are addressed in this paper are as follows:

1. What type of strategies and behaviours have TNC affiliates shown in the 1990s?
2. To what extent did these strategies and behaviours differ from those exhibited during the ISI period?
3. In what ways have TNC affiliates differed from domestic firms in their behaviour?
4. What has been the impact of TNCs' behaviour on the foreign trade patterns of MERCOSUR countries?¹

After presenting a brief background of the main features of the FDI boom in MERCOSUR² in the next section, we deal with these questions in Section 3. The main findings and their implications are presented in the final section. In answering all these questions, we make an attempt to shed light on the main differences found among the various MERCOSUR countries in relation to the issues under study. The main source of information for this paper are the findings of research projects carried out in each of the MERCOSUR countries³ in 1999 and 2000 with a similar approach: Chudnovsky and López (2001)—Argentina; Laplane et al. (2001)—Brazil; Masi (2001)—Paraguay; and Bittencourt and Domingo (2001)—Uruguay. Whenever we employ other sources, they are named explicitly.

2. FDI and TNCs in the MERCOSUR countries in the 1990s: main features

The FDI boom took place in a context where stabilisation plans and market-oriented structural reform programmes were applied in the region (specially in Argentina and Brazil). The latter comprised trade liberalisation, privatisation of state-owned firms and the deregulation of several economic activities. Reforms included actions aimed at eliminating restrictions and conditions for FDI arrival and the deregulation of TNCs' affiliates' activities. At present, there are few sectoral restrictions for FDI entry into the MERCOSUR countries (it is mainly in Brazil where restrictions for FDI in some services sectors still remain).

Both in Argentina and Brazil the regulatory regime of the ISI period disappeared, giving place to new rules of the game with higher degrees of competition in each domestic market and a reduced role for the state. In turn, reforms were slower in the smaller countries. Although Paraguay and Uruguay liberalised their trade and capital accounts, the privatisation of state-owned firms has not been as relevant as in the bigger partners of MERCOSUR.

Argentina and Brazil had started the regional integration process by the mid 80s, and were joined by Paraguay and Uruguay in 1991, when MERCOSUR was officially created with the aim of creating a customs union in 1995. Although some restrictions to intra-zone

¹ The estimates for foreign trade activities of TNC affiliates correspond to the period prior to the devaluation of the real in 1999, which had a strong impact on the trade patterns of MERCOSUR countries.
² In this paper the impact of regional economic integration within MERCOSUR on FDI volume and patterns (i.e., the kind of study made in Dunning, 1997) is not dealt with. However, when analysing TNCs' strategies, attention will be paid to the role played by MERCOSUR in the definition of those strategies.
³ These studies have been published in a book form (Chudnovsky, 2001). They were carried out within the MERCOSUR Economic Research Network with the financial support of the International Development Research Center of Canada.
trade still exist, and the trade policies of the member countries are not always consistent (that is why experts consider MERCOSUR an ‘imperfect’ customs union) the integration process has led to a substantial increase in intra-regional trade flows. However, the difficulties in facing the ‘deep integration’ issues and the absence of macroeconomic coordination and of a dispute settlement system introduced turbulence into the relationship among partners, especially since the Brazilian devaluation in 1999.

In this scenario, a significant growth in FDI inflows took place. From almost U$S1600 million in 1984–89, MERCOSUR received more than U$S40 billion on annual average between 1997 and 1999. As a result, the FDI/GDP ratio strongly increased in all MERCOSUR countries.

While Argentina was the main destination country until the mid 1990s, Brazil took the lead from then on. These trends were mainly related to the different timing of the privatisation process. In Argentina this process took place almost entirely in 1990–93, while in Brazil most privatisations occurred in the late 1990s. In both countries, mergers and acquisitions (M&As), not only related to public but also to domestic private firms, was the main form of entry of FDI in the 1990s.

In the 1990s, there was a shift in the destination of the investment flows vis à vis what happened during the ISI stage. The main change in this connection is that the manufacturing industry lost share vis à vis the services sector. While the manufacturing sector received almost 50% of FDI inflows between 1976 and 1989 in Argentina, its share fell to 32% between 1992 and 1999. In Brazil, while the share of the manufacturing sector in the FDI stock in 1989 was 71%, that sector attracted only 20% of FDI inflows between 1996 and 1999.

Within the manufacturing sector, some industries—such as automotive, chemicals, food, beverages and tobacco—prevail both in Argentina and Brazil, though FDI in machinery and equipment was also relevant in Brazil during the 1990s. These sectors were also those receiving most FDI in manufactures during the ISI period in both countries. In turn, Paraguay and Uruguay exhibit a strong concentration of manufacturing FDI in food, beverages and tobacco.

The increasing share of services in FDI inflows is explained not only by the privatisation of utilities and other state companies, but also by: (1) sectoral deregulation and/or lifting of previous FDI entry barriers in areas such as banking and insurance; (2) the increasing importance of private supply in health and education; (3) the changes in the pension systems; (4) the fall of the share of the manufacturing industry in the GDP of MERCOSUR countries vis à vis services sectors.

As a logical consequence of the massive arrival of FDI to the economies of the region, the presence of TNCs in those economies increased strongly in the 1990s. Between 1990 and 1998, the share of foreign affiliates in sales increased from 34 to 59% in Argentina (considering the 1,000 largest firms), from 41 to 51% in Brazil (considering the 500 largest private firms), from 36 to 51% in Paraguay (considering total sales) and from 26 to 38% in Uruguay (considering 300 largest firms).1,2 We also observe the same trend when analysing other economic variables, such as valued added, investment and employment. In this way, Argentina and Brazil have reached very high levels of TNC presence, only comparable with

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1 Only non-financial firms were considered in all cases, except for Paraguay. It is worth noting that foreign presence in the banking system has significantly increased in the four countries under study.

2 The sales of the 1,000 largest firms in Argentina represented 49% of GDP in 1998. In Brazil, the 500 largest firms represented 40% of Brazilian GDP in 1997, while the corresponding figure in Uruguay for 1998 was 59%. These data clearly show that the samples employed for these estimates are highly representative.
those found in some East Asian countries which are wide open to foreign investment, such as Malaysia and Singapore.

TNCs have also increased their share in foreign trade flows. While in 1990 TNCs’ affiliates absorbed 32% of total exports in Argentina, their share reached 54% in 1998. In Uruguay, the TNCs’ share passed from 26 to 30% between 1992 and 1998, in Paraguay from 32 to 54% in the same period and in Brazil from 48 to 53% in 1989–97.¹ We find a similar trend in the case of imports. TNCs increased their share in imports from 62 to 72% in Argentina, from 53 to 63% in Brazil, from 6 to 11% in Paraguay and from 22 to 24% in Uruguay.²

3. TNCs’ strategies in the 1990s

3.1 A taxonomy of TNCs’ strategies

Our analysis of TNCs’ strategies in MERCOSUR during the 1990s is mainly based on the framework derived from the so-called ‘eclectic paradigm’ of FDI (Dunning, 1988, 1994). According to this paradigm, FDI is classified into four types, according to its main motivation: resource seeking, market seeking, efficiency seeking and strategic asset seeking. The abundance, cost and/or quality of natural and human resources attract resource-seeking investments. The availability of these factors is, in this case, the main locational advantage of the host countries. These investments are generally export-oriented and they often operate as enclaves within host countries.

Market-seeking investments are aimed at exploiting the host country’s market (and, eventually, neighbour countries’ markets). The size and growth prospects of the market, the existence of physical barriers and/or high transport costs, and the host country’s economic policies—including especially, but not only, the degree of protection for domestic production—are key influences for this type of FDI, which became the predominant motivation for TNCs during the ISI process.

Sequential investments made by already established TNC affiliates aimed at increasing the efficiency of their activities by integrating assets, production and markets the better to exploit economies of scale and scope are called ‘efficiency-seeking’ (or ‘rationalised’) investments. These investments usually take place as a result of changes in the competition conditions within host countries (due to trade liberalisation, economic integration with neighbour countries, the appearance of new competitors, etc.), but can also be the fostered by changes in the global or regional strategies of TNCs. According to the received literature, this kind of investments has an increasing relevance vis à vis the traditional forms of FDI (i.e., resource or market-seeking) (Dunning, 1994). Regional integration processes, the reduction in transport costs and new developments in telecommunications and information systems favour this type of strategy, since they are usually effected through productive, technological and commercial complementation within the network of affiliates of each TNC.

¹ In the case of Argentina, the figures were estimated for the 1,000 largest exporters, which amounted to 90% of total exports in 1998. In Brazil, the data were obtained from a sample of the 500 largest firms, which contributed with nearly half total exports in 1997. Both in Paraguay and Uruguay, the figures are based on data from the country’s total exports.

² The basis and time periods for these estimates are the same as those used for export share estimates in Brazil, Paraguay and Uruguay. In the case of Argentina, the 1,000 largest importers were taken into account, which amounted to 63% of the country’s total imports in 1998. The time period considered in this case was 1995–98.
Finally, an increasingly widespread form of FDI is termed ‘strategic asset-seeking’. Its main purpose ‘is to acquire resources and capabilities that an investing firm believes will sustain or advance its core competences in regional or global markets. These assets may range from innovatory capability and organisational structures to accessing foreign distribution channels and better appreciation of the needs of consumers in unfamiliar markets’ (Dunning, 1994, p. 36).

Changes in FDI aims and strategies have modified the role of affiliates within TNC structures. In the past, market-seeking strategies occurred in ‘stand alone’ affiliates, which were to some extent a lower-scale replica of the parent firm organisation—with the exception of R&D activities which tended to concentrate in the country of origin of the firm (UNCTAD, 1994).

As competition over costs becomes widespread in certain industries, national consumption patterns converge and transport costs fall, many TNCs adopt ‘simple integration’ strategies. In these cases, the affiliates specialise in certain segments of the value chain (in the case of affiliates in developing countries, those segments are usually labour intensive) under intra-sourcing arrangements defined by the corporation. This strategy tends to increase foreign trade flows generated by FDI in developing countries, not only through affiliates’ exports, but also because those kinds of affiliates often operate with a low degree of local vertical integration.

A third type of strategy is termed ‘complex integration’ (UNCTAD, 1994). In this case, TNCs search for more effective ways of organising and governing the wide range of assets they own in different locations. This shift to a more complex corporate integration scheme requires a breakdown of the value chain into discrete functions—assembly, procurement, finance, research and development, etc.—and their location wherever they can be carried out most effectively in the light of the overall needs of the firm as a whole.

What has happened with TNCs’ strategies in MERCOSUR in the 1990s? We have established a taxonomy of affiliates’ strategies based on their foreign trade performance (see Table 1 for details of the samples employed in each country to build this taxonomy).

Market-seeking strategies prevailed in Argentina, Brazil and Paraguay in the 1990s (Table 1). In contrast, in Uruguay resource-seeking strategies were predominant in terms of investments amounts, although market-seeking strategies have prevailed if one considers the number of foreign firms involved in each kind of strategy and their market shares. We have not identified FDI operations as being mainly motivated by efficiency-seeking or strategic asset-seeking objectives, although both kinds of objective are present, to some extent, in many recent investments in MERCOSUR countries.

In certain cases—mostly in the services sector—market-seeking strategies have been ‘pure’, in the sense that foreign affiliates do not export (or if they do, exports are not made on a regular basis). This type of strategy is, in relative terms, dominant both in Argentina and Uruguay, while it was less relevant in Brazil. This is a reflection of the fact that most recent FDI inflows in MERCOSUR have gone to the services sector. With the exception of Paraguay, TNCs operating in these sectors exhibit lower import coefficients than the average for the whole of foreign affiliates; in fact, in the case of Brazil, the affiliates in these

1 This finding is consistent with the fact that different surveys made to foreign affiliates operating in the region show that the size and dynamism of domestic markets have been the key factors of attraction for FDI in both Argentina and Brazil.

2 However, it must be taken into account that this analysis is based on 1997 data for Brazil, while privatisations undertaken between 1998 and 2000 might have considerably increased the incidence of this strategy.
### Table 1. TNCs’ strategies in MERCOSUR\(^a\) (%)

<table>
<thead>
<tr>
<th>Country</th>
<th>% of total TNC sales(^b)</th>
<th>Resource seeking</th>
<th>Pure market seeking</th>
<th>Market-seeking with low export orientation</th>
<th>Market-seeking with moderate export orientation</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argentina 1997</td>
<td>12.2</td>
<td>38.1</td>
<td>23.4</td>
<td>25.8</td>
<td>100.0</td>
<td></td>
</tr>
<tr>
<td>Brazil 1997</td>
<td>1.6</td>
<td>20.1</td>
<td>25.7</td>
<td>52.6</td>
<td>100.0</td>
<td></td>
</tr>
<tr>
<td>Paraguay 1998</td>
<td>25.5</td>
<td>29.6</td>
<td>44.9</td>
<td>–</td>
<td>100.0</td>
<td></td>
</tr>
<tr>
<td>Uruguay 1998</td>
<td>21.2</td>
<td>45.8</td>
<td>18.1</td>
<td>14.9</td>
<td>100.0</td>
<td></td>
</tr>
</tbody>
</table>

\(^a\)Data in this table are based on samples which include the leading 140 and 154 TNCs operating in Paraguay and Uruguay, respectively. In the case of Argentina and Brazil, the samples include TNCs belonging to the top 1,000 and 500 firms operating, respectively, in each country. Information on sales was obtained from specialised publications in each country, except for Paraguay, where they were provided by the Central Bank. Information on foreign trade was obtained from different official as well as private sources in each country. The sales of the 1,000 leading firms in Argentina represented almost 50% of the GDP in 1997. In Brazil, the sales of the leading 500 firms represented 41% of GDP in the same year. In Uruguay, the 154 TNCs selected contributed 90% of the investments made by all the TNCs operating in the country. In Paraguay, the TNCs whose data are included in this table represent the bulk of the foreign investment made in the country.

\(^b\)The share of each group in total TNC sales in each country.

\(^c\)Exports (imports) to (from) MERCOSUR over total exports (imports).

\(^d\)Exports to non-MERCOSUR countries over total sales.

sectors make almost no imports. The differences between countries may be accounted for by the different sectoral composition of the investments included in this category. In the case of Paraguay, a great part of pure market-seeking investments corresponds to commercial affiliates which distribute imported goods from MERCOSUR but mainly from non-MERCOSUR countries; hence, they exhibit a very high import coefficient. In Argentina, besides privatised public utilities—which make significant capital goods and inputs imports—there are many TNC affiliates that distribute imported electronics products, computers, telecommunications equipment, etc. that are not made in the country. In contrast, Brazil has managed to build up an electronics industry; hence, those TNC affiliates do not appear in this category, which is mainly composed of firms operating in the retail and wholesale trade as well as in sectors such as construction, transport, etc.

In any case, evidence indicates that stand-alone schemes prevail within this group of firms in the four countries under study, and that strong inter-affiliate integration or specialisation strategies (neither intra nor extra-regional) are not usual (or at least, those strategies, if they exist, do not materialise through foreign trade flows of goods).

Market-seeking strategies also prevail in the manufacturing industry, although foreign affiliates in industrial sectors, even if primarily oriented towards domestic markets, also undertake export activities. We have divided market-seeking strategies within the manufacturing sector in two groups: i) low export-orientation: we include in this category those sectors whose export/sales ratios are lower than the average of the host economy. ii) moderate export-orientation: we include in this category those sectors whose export/sales ratios are higher than the average of the host economy. It is important to highlight the fact that even within the latter group, it is hard to find firms with export coefficients above 25%. In other words, TNC affiliates within the manufacturing sector have not engaged in ‘export-oriented’ investments in these countries.

It is important to highlight the fact that the sectoral composition of each group is not the same in all countries. Sectors such as information technology equipment and telecommunications and non-metallic minerals have a low export orientation both in Argentina and Brazil. Likewise, the rubber, plastics and automotive sectors show a moderate export orientation in both countries. In contrast, the production of food, beverages and tobacco has a low export orientation in Argentina, but a moderate one in Brazil. The converse occurs for clothes, machinery and electrical equipment (low export orientation in Brazil and moderate in Argentina). This suggests that sectoral dynamics has a direct influence on TNC strategies in some cases, but that national environments also play an important role in that connection.

Foreign affiliates operating with market-seeking strategies with low export orientation exhibit an export coefficient much lower on average than their import propensity. Hence, it is not surprising that this group of affiliates, as a whole, operates with strong trade deficits in the four countries under study. Sectors linked to high-tech activities (electronics, information technology and telecommunications equipment) tend to show the highest import coefficients and/or the larger difference between import and export propensities, at least in Argentina and Brazil.

MERCOSUR is a significant destination for this group’s exports; extra-zone exports represent only 2.3% of the sales of market-seeking TNCs with low export orientation in Argentina, 2.6% in Brazil and 1.8% in Paraguay. In turn, MERCOSUR is much less important as a region of origin of imports than as an exports market (Table 1).

On the basis of this evidence, we can conclude that foreign affiliates within this group have a type of ‘asymmetrical’ integration with the international market—and also within
their corporations. While there is strong integration on the imports side (acquiring inputs, components, equipment and final products from non-MERCOSUR countries, and especially from developed countries—see below), integration seems to be much weaker on the side of exports, which are strongly concentrated within MERCOSUR.

The ‘market-seeking with moderate export orientation’ strategy accounted for more than 50% of TNC sales in Brazil; in contrast, their sales were hardly over 25% of total TNC sales in Argentina and around 15% in Uruguay. Since Brazilian industry is the most competitive among MERCOSUR countries, it is no surprise to find that TNCs in that country are more export oriented than those of Argentina and Uruguay.

TNCs within this group operate with much lower export coefficients in Argentina and Brazil (16 and 13% respectively) than in Uruguay (24%). In turn, affiliates in Argentina and Uruguay exhibit much higher import propensities (29% and 25% respectively), than in Brazil (10%). Hence, affiliates within this group operate, as a whole, with a strong trade deficit in Argentina (and to lesser extent in Uruguay), but with a surplus in Brazil. Although affiliates operating with this kind of strategy often show a great degree of integration with their counterparts in other MERCOSUR countries (this is most notably reflected in the automotive sector), they also exhibit a far higher extra-MERCOSUR export-ratio vis à vis those affiliates with a low export orientation (Table 1). The fact that these affiliates do not only export more than those in the ‘low export orientation strategy’ but are also more prone to export to non-MERCOSUR countries would suggest that they have attained higher competitiveness levels vis à vis the other group.

Furthermore, the type of integration between these affiliates and the rest of the world is less asymmetric than in the case of the group with low export orientation, particularly in Brazil’s case. Additionally, the import coefficient is lower for Brazilian foreign affiliates than for Argentinian ones. This might be a consequence, among other factors, of the fact that the Brazilian industrial complex is more articulated (i.e., linkages are more widespread) than the Argentinian one and/or that the import de-substitution process has been more intense, in the 1990s, in Argentina than in Brazil. However, in spite of the apparent higher competitiveness of the Brazilian affiliates, their exports of those products pertaining to high-tech sectors, or for which quality and technological requirements are more significant, are still concentrated in Latin America (see below).

Have trade liberalisation and MERCOSUR contributed to reduce the weight of the market-seeking orientation of foreign affiliates in the manufacturing sector? To answer this question, we only use information on the Argentinian case. Foreign manufacturing affiliates in that country increased their average export coefficients between 1992 and 1997. However, the ratio of extra-zone exports on sales actually fell in the same time period.1 This means that, in fact, those affiliates are more market seeking than in the past, since they have partly reoriented their sales towards Brazil (where, as a consequence of the creation of MERCOSUR, they enjoy a tariff preference vis à vis extra-zone competitors), at the expense of extra-zone as well as of purely domestic sales.

Regarding resource-seeking strategies, their weight is low in Brazil, while they are relatively more important in Argentina, Paraguay and particularly in Uruguay (in these three countries, agricultural resources account for the bulk of these investments but, in Argentina, oil and mining investments have also been very important in the 1990s). Resource-seeking TNCs operate in the four countries with high export propensities (more

1 Although a composition effect might be influencing this result, the available data show that it cannot be the main determinant, since extra-zone exports coefficients fell in 11 out of the 13 manufacturing sectors into which the foreign affiliates sample was classified in Argentina.
than 70% in Argentina and Uruguay\(^1\) and almost 50% in Brazil) and low import coefficients. Exports are mainly directed to extra-zone markets. In turn, imports from MERCOSUR countries are not significant.

As already mentioned, TNCs investments in the 1990s have included both efficiency as well as strategic asset-seeking components. However, in both cases these components have almost always been a complement of the primary motivation, i.e., market seeking. We analyse efficiency-seeking strategies of TNC affiliates in MERCOSUR below (see subsection 3.2).

In turn, asset-seeking objectives have been present in M&As, mainly in Argentina and Brazil. In general, TNCs have looked for the domestic market share of the acquired firm, rather than its equipment, human resources or technological capabilities. This means that TNCs in MERCOSUR countries seek assets that are strategic in relation to the firm’s performance at the national or regional level (i.e., brands, distribution channels, consumers loyalty, etc.), but they are rarely seen as strategic for the corporation’s global performance. We observe the exception to this rule in Brazil, where TNCs have acquired domestic firms that had already gone through significant learning processes which not only resulted in the possession of valuable technological assets and high efficiency and quality levels, but had also allowed some Brazilian firms to install production facilities in the US and Europe to attend those markets—the cases of the automobile part makers Metal Leve and Cofap, both acquired by TNCs in the 1990s, are the most important in this regard.\(^2\)

3.2 What is new in TNCs’ strategies?

Are there any differences between the strategies adopted by TNCs in the 1990s and those prevailing during the ISI period?

During the ISI, TNCs main investment motivation was to exploit the domestic market through stand-alone subsidiaries which were small-scale replicas of their headquarters. Import propensities were low, since high tariffs and local content requirements induced TNC affiliates to buy from local suppliers. In turn, export propensities were also low and generally lower than import propensities. A survey made to 42 TNCs in different Latin American countries in 1981 showed that only eight of them exported more than 10% of their sales (Sourrouille et al., 1984). Hence, these affiliates were not closely integrated with the rest of the corporation.

Furthermore, since TNC affiliates in the ISI stage operated in markets which were highly protected, even if they were more efficient, on average, than domestic firms, they often had technologies and scales which were far from the international frontier, especially in Argentina.

What happened in the 1990s? As already noted, the main motivation for FDI has been the same as that in the ISI, i.e., market seeking. However, there are three significant differences between these two periods.

First, trade liberalisation has allowed TNC affiliates significantly to increase their imports of capital goods, inputs and final goods. Hence, TNCs’ domestic linkages are less than in the ISI stage. In turn, affiliates have been able to gain economies of specialisation

\(^1\) Excluding the tourism sector, which can be considered, at least in Uruguay, as part of the resource-seeking strategy.

\(^2\) The perception that Brazil may offer valuable strategic assets for TNCs is in line with the findings of a survey whose results are reported in Dunning (1996), who points out that Brazil has been considered by several TNCs as a source of ‘created’ assets (both technological and managerial), which might contribute to maintaining or improving the corporation’s competitive position at the international level.
(since they now complement local production with imported final goods), upgrade their plants (thanks to the access to modern foreign capital goods) and reduce their costs (by replacing local suppliers by foreign ones—this replacement may also allow quality gains).

Second, for TNC affiliates the ‘domestic market’ is not just the market of the country in which they operate (as happened in the ISI), but MERCOSUR as a whole. Regional integration agreements like MERCOSUR facilitate the search for economies of specialisation and scale—and therefore for efficiency gains—through efficiency-seeking strategies. This opportunity is particularly important for foreign affiliates in Argentina and Uruguay, and to a lesser extent for Brazilian foreign affiliates, given the differences among the respective domestic markets.

Third, since MERCOSUR economies are currently more open to international trade than during the ISI stage, market-seeking strategies must include ‘rationalisation’ initiatives, aimed at reducing costs and improving the productivity of TNC affiliates through vertical disintegration, outsourcing, personnel reduction, etc.

These pro-efficiency actions will not necessarily materialise as ‘efficiency-seeking’ strategies in the sense of Dunning’s eclectic paradigm, since those actions do not always include arrangements aimed at taking advantage of the common governance of productive and commercial facilities in different countries through complementation and specialisation of the TNC affiliates. However, strictu sensu ‘efficiency-seeking’ strategies are also gaining importance, especially at a MERCOSUR level.

In fact, in the 1990s many TNCs operating in tradable sectors adopted strategies in which each MERCOSUR affiliate tends to specialise in certain products or production lines, exporting the resulting products to the other MERCOSUR countries and importing inputs and final products from those countries or from other locations. Exports and imports of this kind are usually of an intra-firm nature.

Efficiency-seeking strategies are more widespread in sectors such as electrical domestic appliances, petrochemicals, food and beverages, pharmaceutical, cleansing and personal care products, tyres and, most notably, in the automotive industry. Those strategies are generally deployed within MERCOSUR, and especially between Argentine and Brazilian affiliates, which have tended to specialise in certain complementary product lines. Specialisation has thus led to increasing trade flows between affiliates in both countries. In contrast, MERCOSUR affiliates have seldom integrated within efficiency-seeking networks with other affiliates in developed countries.

The spread of efficiency-seeking strategies goes hand in hand with the gradual abandonment of the ‘stand-alone’ model that was typical of the ISI stage, and the adoption of simple and, less frequently, complex integration schemes. The available evidence suggests that, unlike what happens with affiliates in developed countries, the reinforcement of integration schemes within the TNCs networks have hardly ever involved the transfer of corporate strategic functions to affiliates in MERCOSUR countries. For instance, MERCOSUR affiliates rarely undertake R&D or product and process design activities (in general, they only carry out adaptive tasks, and these are mainly concentrated in Brazilian affiliates), since these functions are centralised in their parent company or in affiliates located in developed countries. The same goes for activities such as market development and marketing.

Nonetheless, even at the MERCOSUR level, the adoption of efficiency-seeking strategies and of intra-corporation integration schemes still seems to be in its infant stage, and is still very dependent on macroeconomic fluctuations in Argentina and Brazil. In fact, it is only in the automotive industry—which, as already mentioned, was favoured by
specific sectoral policies that have been in force both in Argentina and Brazil—that the adoption of efficiency-seeking strategies has led to the establishment of ‘strong’ integration schemes. The international strategies of automotive industries are increasingly based on the settlement of sub-regional production and distribution centres, where vehicles, parts and pieces are mutually exchangeable among the different affiliates. MERCOSUR has become one of these centres. As a consequence, investment projects are envisaged for the regional market as a whole, and production plans articulate the activities of the different affiliates of the corporation through complementary specialisation schemes. Firms seek to reduce the number of platforms used in each plant and assign only one or two models to each plant, usually as a ‘product mandate’ for the MERCOSUR region, to reach efficient scale ranges. They complement domestic supplies through intra-firm trade. Imports and exports flows among MERCOSUR TNC affiliates in this industry have thus grown considerably.

What happens with TNC affiliates in the smaller MERCOSUR countries? Uruguayan foreign affiliates—specially those created during the ISI—are being relegated to a marginal position in the regional structure of the corporations as a consequence of the spreading of efficiency-seeking strategies. Hence, they are gradually turning into commercial affiliates—importing final products from other MERCOSUR countries and from other affiliates—or have even been dismantled in some cases.

3.3 TNC and domestic firms export/import propensities

In Argentina, TNC affiliates import and export more than domestic firms in relation to their respective sales. However, the exports/sales ratio of domestic firms is higher than their imports/sales ratio, while we find the opposite for TNCs (Figures 1 and 2). While TNCs as a whole exhibit negative foreign trade balances (and this is specially visible in the
manufacturing and services affiliates), domestic firms as a whole generate a positive contribution to the country’s trade balance.

In Brazil, export propensities are similar for TNCs and domestic firms, while the import propensity of TNCs is higher and has grown faster *vis à vis* those of domestic firms. Foreign affiliates as a whole exhibit positive trade balances, but the same does not happen with industrial affiliates, which passed from a surplus in 1989 to a deficit in 1997. Both in Argentina and Brazil, trade deficits are relatively more important in research-intensive manufacturing branches (information technology, telecommunication equipment, pharmaceuticals) as well as in the automotive sector.

In the case of Uruguay, we found a decrease in both the import as well as in the export propensities of TNCs. While in 1992 the export propensity of foreign affiliates was higher than their import propensity (and TNC affiliates as a whole exhibited a positive trade balance), both things had changed by 1998. The above-mentioned consequences of the implementation of efficiency-seeking strategies for Uruguayan affiliates could be one of the reasons for this change.\(^1\) In turn, domestic enterprises operate with positive trade balances in both years and with higher propensities to export than to import. Thus, while in 1992 TNC affiliates’ export propensity was significantly higher than that of domestic firms, this difference had almost disappeared by 1998.

We carried out statistical exercises based on the ‘matched pairs’ technique in Argentina, Brazil and Uruguay with data for 1997. These exercises showed that the differences found between TNCs and domestic firms in relation to their import propensities were statistically significant, while no statistical significance was found when analysing the differences in their export propensities.

The study for Paraguay only provides information on export and import propensities for TNCs and for the country as a whole. TNC affiliates; export-sales ratio is higher than their import one. The opposite occurs for the country as a whole. TNCs generated foreign trade surpluses during the 1990s, in contrast to what happened at the country level. However, if

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\(^1\) It is worth noting that the tourism industry, where TNCs play a relevant role, generates significant income for Uruguay. This income has not been taken into account for these estimations (since they are based on trade in goods only) but should be considered when analysing TNCs’ contribution to Uruguay’s balance of payments.
we exclude affiliates in agricultural sectors, the remaining TNCs exhibit, as a whole, a trade deficit.

3.4 The geographical pattern of TNCs’ foreign trade

To what extent have TNCs contributed to increasing the diversification of exports market (and specially the access to markets in developed countries) of the MERCOSUR countries?

In Brazil, TNC affiliates’ exports are more concentrated in MERCOSUR countries than Brazilian exports as a whole. Of the exports of TNC affiliates, 28% were directed to MERCOSUR in 1997 (Table 2), while sales to MERCOSUR reached 17% of total Brazilian exports in the same year. In contrast, MERCOSUR has been the origin of 13% of

Table 2. Exports and imports: geographical pattern. 1997 (%)

<table>
<thead>
<tr>
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<th>Argentina</th>
<th>Brazil</th>
<th>Paraguay</th>
<th>Uruguay</th>
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<td>TNCs</td>
<td>Total</td>
</tr>
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<td></td>
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<tr>
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</tr>
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<td>2.8</td>
<td>n.a.</td>
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<tr>
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</tbody>
</table>

\[a\] Latin American Integration Association (excluding MERCOSUR countries and Mexico).

\[b\] China, Hong Kong, Indonesia, Japan, Malaysia, Philippines, Singapore, South Korea, Taiwan and Thailand.


\[1\] Data on this section are based on estimations for all foreign affiliates in Uruguay and Paraguay and on samples in the cases of Argentina and Brazil. Argentina’s sample includes 140 affiliates whose exports represented 33% of total exports and 21% of total imports in 1997. Additionally, the sample represented 71% and 36% of TNCs total imports and exports, respectively, in the same year. The sample for Brazil is composed of 100 affiliates whose total sales represented 20% of Brazilian international exchange, 48% of the international exchange of the 500 largest firms in the country and 84% of total the international exchange of those TNCs included in the 500 largest firms.
total TNC imports, against 16% for Brazil’s total imports. Hence, foreign affiliates show a trade surplus with MERCOSUR and the rest of Latin America, and a deficit with NAFTA and the European Union.

In the case of Argentina, the geographical pattern of TNC foreign trade is quite similar to that of the country as a whole. In both cases, a significant increase in MERCOSUR’s presence takes place, both as origin of imports as well as a destination for exports, over the decade. In fact, TNC exports show a higher concentration in MERCOSUR than Argentinean exports as a whole (we observe the inverse situation in the case of developed countries’ markets). It is important to note that TNC affiliates’ exports to their home countries are very low, while their imports tend to be strongly concentrated in their home countries and/or regions.

In the case of Uruguay, in 1998 half of TNCs imports and exports were carried out within MERCOSUR. However, and contrary to what happens in Argentina and Uruguay, the concentration of exports in MERCOSUR is slightly below the national average (the opposite occurred in the case of imports). While imported inputs originate mainly in developed countries, final products are imported mostly from Argentina and Brazil. As we found in the cases of Argentina and Brazil, the share of home countries/regions in the foreign trade flows of TNC affiliates is higher in the case of imports than for exports. However, the trade pattern of TNCs is less related to the home countries/regions of the affiliates than in Argentina and Brazil. This finding is attributed to the fact that most Uruguayan affiliates operate as subsidiaries of Argentinian affiliates.

In turn, TNC affiliates in Paraguay have reoriented their sales towards MERCOSUR during the 1990s. This reorientation has been more pronounced than in the case of domestically owned firms. Contrary to what has been found in the other three countries under study, MERCOSUR is more important as the origin of imports than as an export destination for Paraguayan TNC affiliates. This could be related to the fact that many affiliates have their headquarters in Argentina and Brazil, and operate mainly as distribution centres for products exported from those countries.

Summing up, TNC affiliates have not contributed to a substantial improvement in access to new exports markets for MERCOSUR countries. In fact, TNCs exports are more concentrated in MERCOSUR markets than domestic firms’ exports in the cases of Argentina, Brazil and Paraguay, while their exports to developed countries markets are mostly made by TNC affiliates operating in natural resource-intensive branches.

Comparing TNC affiliates’ foreign trade flows among the four countries under study, we find that MERCOSUR is less relevant as an export market (and as an import origin) for Brazilian TNCs, while their relevance is highest in Paraguay and Uruguay. In turn, it is in Brazil that the share of manufactured products within TNCs exports is highest. The weight of manufactured products is lowest in the case of Paraguay.

In this regard, we must note that in the four countries under study TNC affiliates export manufactured products (and specially those scale or R&D intensive) to MERCOSUR as well as to other Latin American countries, while they mostly sell primary and agro-industrial products to developed countries, from where they import inputs, final goods, parts, etc. which are not produced locally owing to technical and/or scale restrictions.

In this scenario, within MERCOSUR a ‘hierarchy’ is visible among the four countries, with Brazil being the location chosen by TNCs for producing and exporting those products where scale economies or R&D activities are more relevant. Brazil has also attracted most recent FDI operations in those sectors. This trend may be explained by the fact that Brazil already was, prior to the creation of the MERCOSUR, the country where
the industrialisation process had advanced furthest, both in quantitative as well as in qualitative terms.

4. Conclusions

The recent FDI boom in MERCOSUR took place under very different conditions from those prevailing during the ISI, when TNCs, specially in Argentina and Brazil, became the leading agents of the industrialisation process.

At the international level, the spreading of so-called globalisation led to a rapid growth in cross-border capital and merchandise flows. At the regional level, instead of the typical economic policy regime of the ISI—inward oriented and with a strong presence of the state—MERCOSUR economies have been substantially liberalised and deregulated.

Nevertheless, when analysing TNCs’ strategies and behaviours in the 1990s, a déjà vu impression appears, since the basic determinants for FDI have been, as in the ISI period, the domestic market and their growth perspectives, although national market attractiveness is now enhanced by the perspectives of accession to other MERCOSUR countries.

The domestic market has been a decisive factor, not only for services—which have at吸取 most FDI flows in the 1990s—but also for the bulk of the FDI in manufacturing industry. Hence, market-seeking strategies have prevailed.

Although the predominance of market-seeking strategies introduces an element of continuity with the ISI, it is true that these strategies are now combined with pro-efficiency measures aimed at competing in the new regional and global scenario. This new approach has in some cases been effected through what is termed in the received literature as ‘efficiency-seeking’ strategies (in which TNC affiliates integrate their assets and coordinate their activities to better exploiting economies of scale and scope).

However, an ‘asymmetric integration’ is visible: MERCOSUR’s TNC affiliates produce for the internal market and their exports are generally low. Furthermore, only in some natural resource intensive manufacturing branches are these exports directed towards developed countries’ markets, while the rest of the affiliates export mainly to MERCOSUR and, to a lesser extent, to the rest of Latin America. In turn, TNC affiliates import inputs and final goods from developed countries; in this regard, we must highlight the fact that trade liberalisation has facilitated TNC affiliates to incrementing their imports both by replacing local suppliers for foreign ones as well as for complementing their local production with imported goods. Besides, note must be taken that a significant part of both export and import flows is ‘intra-firm’.

Thus, even if affiliates have obtained productivity gains through specialisation and restructuring (partly at the expense of reducing their linkages with the host economies), these gains have not yet been reflected in a significant increase in TNC affiliates exports, and even less in an increase in their exports destined towards the markets of developed countries.

Regarding ‘strategic asset-seeking’ strategies, only in Brazil, and in certain specific cases, do TNCs seek assets that are important for the corporation’s global competitive position. In turn, even if M&As in MERCOSUR countries were partly undertaken with asset-seeking motivations, the kinds of assets that TNCs look for when they acquire domestic firms are mostly related to the market share of the domestic firm that is bought (i.e., brands, distribution channels, etc.). This suggests that, within MERCOSUR, only Brazil—to some extent—is seen by TNCs as a host country where they may have access to valuable assets for competing worldwide.
Finally, only in Uruguay have natural resource-seeking investments, which are highly export oriented, had a prevailing role in the recent FDI boom, although they have also been important in Argentina and Paraguay. In this regard, we must highlight the fact that no labour-intensive export-oriented FDI has been found within MERCOSUR countries, a key difference vis à vis FDI destined for Mexico or Central America and the Caribbean in the 1990s.

In relation to the linkages between FDI and foreign trade, our findings show that TNCs do not seem to have made a greater contribution than national firms to the growth of exports in the countries of the region, although they have a higher propensity to import compared with local enterprises. Neither have they contributed to expanding the diversification of their export markets (in fact they are more ‘MERCOSUR oriented’ than are national firms).

It is important to note that the FDI sectoral distribution and the TNCs trade patterns reflect the existing structural differences between MERCOSUR countries. Brazil clearly appears as the country that attracts more FDI to scale-intensive and high-tech sectors (and this is consistent with the above-mentioned finding regarding the role of Brazil as a host country where strategic assets may be found by TNCs). However, the bulk of goods with higher value added and/or technological sophistication are exported to MERCOSUR—and to the rest of Latin America. At the same time, similar, but presumably more complex, goods are imported—as parts, components, capital goods, inputs or final goods—by Brazilian TNC affiliates from industrialised countries.

In this scenario, we can conclude that the FDI boom to MERCOSUR in the 1990s has not yet generated a significant contribution to the enhancement of the competitiveness level and the upgrade of the trade structure of the host countries. In turn, TNC affiliates seemingly has fewer linkages with the local economy (as revealed by their higher import propensity) than domestic firms. Hence, it comes as no surprise to find that, especially in the manufacturing and services sector, significant trade deficits result from their operations in MERCOSUR countries.

The findings of this paper suggest that FDI cannot be, per se, a tool for economic development if other and more fundamental conditions are not present in the host countries. In fact, we can think that the sequence goes from domestic policies aimed at ‘creating assets’ in host countries (i.e., human capital, technological infrastructure, etc.) to the attraction of FDI inflows that, in this hypothetical and more favourable environment, could eventually contribute more to the economic development of MERCOSUR countries, both by enhancing their export capabilities and by creating more linkages with the host economies. In other words, FDI is not a substitute for the lack of good domestic development policies.

Regarding further research issues, the various factors accounting for the trade performance of the TNCs studied in this paper are worth exploring more deeply. A more detailed examination of the strategies of the TNC affiliates taking into account the different sectors in which they operate, the technological gaps with overseas facilities, their country of origin, age, the intra-corporation markets allocation strategy, etc. should shed more light on the endogenous factors accounting for the high reliance on imports and the relatively poor export performance of TNC affiliates. In turn, evaluating the various domestic policies in force which may have an impact on TNC affiliates’ foreign trade as well as the consequences of some events that took place after the period considered in this paper—such as the devaluation of the real in Brazil in 1999 and the current crisis in Argentina—should contribute to the analysis of the influence of exogenous factors. Finally, we should
assess both exogenous and endogenous factors more adequately with a longer time frame than that covered in the present paper.

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