“The Impact of TNC Strategies on Development in Latin America and the Caribbean”

Michael Mortimore

Foreign direct investment (FDI) and, more generally, the activities of transnational corporations (TNC) have lost a lot of their shine recently with respect to their contribution to development. This, on the one hand, is because FDI inflows, in general, and to developing countries, in particular, have collapsed since 2000 (UNCTAD, 2003). On the other hand, empirical analyses increasingly call into question the assumptions underlying the traditionally very favorable views of FDI and TNC activities as motors of growth and development. This suggests that it is an opportune moment to review and revise our understanding of the impact of TNCs on development.

The indicators for FDI and TNC activities have taken a severe turn for the worse. For example, global inflows have fallen from a high of US$ 1,393 billion in 2000 to just 651.2 billion in 2002. FDI inflows to developing countries peaked at 246.1 billion in 2000 to reach only 162.1 billion in 2002 (52.7 billion going to China alone). As of 2002, several significant indicators of the level of international production by TNCs either declined, such as sales, gross product and employment of foreign affiliates, or stopped expanding, such as the exports of foreign affiliates. Whether this is a mere bump in the road or a secular decline is, of course, central to developing country decision making with regard to the role of FDI policies in development strategies. Unfortunately, this is not something that we can answer easily at this moment, but rather it is something that must be carefully and continually monitored. In this paper, we carry out a revision of the impact of FDI and TNCs operations on development.

The original literature on productivity spillovers can now be seen with hindsight to have been an extremely biased vision of potential FDI impacts, suggesting that the mere presence of increasing levels of FDI and TNC activities improved the productivity of the host economy, much like water spilling over the sides of a glass. In other words, it suggested that the largest quantity possible of FDI should be attracted in order to quickly surpass the threshold beyond which productivity benefits accelerated. Recently this essentially ideological premise has been questioned increasingly in terms of its utility as a guide to FDI policy in the manufacturing sector, where the empirical analyses of such have multiplied. Also, it might be mentioned that the spillovers literature has little to offer in terms of FDI impacts in services, where most FDI now goes, thus, it can be considered incomplete. This article invites the reader to think outside the existing FDI policy box dominated by the spillovers literature by offering a different perspective based more on corporate strategies in real-world settings.

This article consists of five parts. The first, examines the evolution of empirical findings on the original literature that supported the rosy view of the impact of FDI and TNC activities. It points out its shortcomings while salvaging the most useful elements in order to incorporate them into a more realistic perspective based on a clearer comprehension of the principal TNC strategies that drive FDI. The second section reviews the overall experience of Latin America and the Caribbean (LAC) from this perspective. Section three focuses specifically on the impact of efficiency-seeking FDI in the region. Section four does the same for market-seeking (services) FDI. In this manner, we arrive at a more satisfactory explanation of the impact of TNC strategies on development in LAC. Finally, the last part demonstrates that the FDI policy recommendations deriving from the new analytic perspective are considerably different from those emanating from the original spillovers literature.

1. A critical review of some of the spillovers literature

The microeconomic literature analyzing the impact of FDI and TNC activities tends to focus on manufacturing activities in particular countries. The improvement in the basic data available for this analysis has

---

1 Chief, Unit on Investment and Corporate Strategies, United Nations Economic Commission for Latin America and the Caribbean. This Unit produces the annual report on Foreign Investment in Latin America and the Caribbean. During August, 2001 thru September, 2002, Mr. Mortimore worked for UNCTAD in Geneva contributing to the thematic section (“TNCs and export competitiveness”) of the World Investment Report 2002.

2 We should widen our research interest to “transnational corporation (TNC) activities”, rather than simply FDI, in order to have a fuller appreciation of the phenomenon that we are dealing with. After all, TNCs can have a very significant impact on a developing country without investing a cent. I use FDI as shorthand for FDI / TNC activities in this text.
provoked a significant sophistication in the kind of statistical and econometric tools used to attempt to isolate the FDI impact on development and make its measurement more rigorous. This is a positive development because the dominant strand of this literature --that related to the concept of “spillovers”-- came to very powerful conclusions based on quite weak evidence and can be considered, from that perspective, to have been ideologically- more than empirically- based. The basic conclusion was that the increased presence of FDI in itself produced productivity gains in the host economy based on transmission mechanisms such as technology assimilation and transfer, human resource training, deepened production linkages and enterprise development, among other things. In other words, the more pronounced these transmission mechanisms, the more favorable the impact on host country productivity.

Table 1 provides a summary of what can be considered a representative sample of the spillovers literature. Some of the principal findings of the review of that literature are:

- the original empirical analyses tended to be methodologically questionable due to the unavailability, poor quality or limited comparability of much of the evidence upon which it rested its case. The outcome tended to be assumed where it was supposed to be proven.
- as data availability improved and the empirical analysis was extended, first, into developing countries and, later, into economies in transition, the original conclusions were challenged as more and more mixed or negative impacts were encountered and measured where positive ones had been assumed to exist. This was particularly evident with regards to economies in transition. With regards to developing countries, the case of Mexico is particularly revealing. Early studies of that country (Blomstrom and Persson, Blomstrom, Blomstrom and Wolff, and Kokko) when it was closed and had an unfriendly attitude towards FDI found spillover effects to be positive. A more recent study (Romo, 2003) of that country –now open and with a decidedly favourable attitude towards FDI -- found these effects to be questionable at best.
- it became increasingly evident that, while it was clear that FDI could favorably impact the host country --and generally did so in the more economically-advanced developed countries—that was not at all an automatic result in other host countries possessing a more limited absorptive capacity.
- although the empirical results of the spillovers literature progressively raised doubts about the initial rosy view of FDI impacts, especially in developing countries and economies in transition, the improvement in the measures being employed –transfer and assimilation of technology (TAT), human resources (HR), production linkages (PL) and enterprise development (ED) became benchmarks for more penetrating FDI impact analyses.

In other words, the spillovers literature brought into question its own original postulates by way of improved data availability and better statistical and econometric analysis. As a result, it could no longer be assumed that the best FDI policy was necessarily the one that aimed to attract the maximum amount of FDI.

**Table 1- A Summary of the Evolution and Results of a Sample of the Spillovers Literature**

<table>
<thead>
<tr>
<th>Author (s)</th>
<th>Country</th>
<th>Year</th>
<th>Data Level</th>
<th>Analysis</th>
<th>Result</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1. Developed Countries</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Globerman (1979)</td>
<td>Canada</td>
<td>1972</td>
<td>Cross-section</td>
<td>Industry</td>
<td>+</td>
</tr>
<tr>
<td>Harris and Robinson (2001)</td>
<td>UK</td>
<td>1974</td>
<td>Panel</td>
<td>Firm</td>
<td>?</td>
</tr>
<tr>
<td>Authors</td>
<td>Country</td>
<td>Year Range</td>
<td>Methodology</td>
<td>Industry</td>
<td>Comment</td>
</tr>
<tr>
<td>-------------------------</td>
<td>------------------</td>
<td>----------------</td>
<td>-------------------</td>
<td>----------</td>
<td>---------</td>
</tr>
<tr>
<td>Barry et al. (2001)</td>
<td>Ireland</td>
<td>1990-1998</td>
<td>Panel Firm</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td><strong>2. Developing Countries</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kokko et al. (1996)</td>
<td>Uruguay</td>
<td>1990</td>
<td>Cross-section Firm</td>
<td>?</td>
<td></td>
</tr>
<tr>
<td><strong>3. Transition Economies</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Konnings (2001)</td>
<td>Bulgaria, Poland, Romania</td>
<td>1993-1997</td>
<td>Panel Firm</td>
<td>-</td>
<td></td>
</tr>
</tbody>
</table>
The insights of the more recent spillovers literature based on better empirical studies can be used to arrive at even more penetrating and objective analyses of the impacts FDI and TNC operations on development. Table 2 provides an important ingredient not present in the analysis associated with the spillovers literature: corporate strategies, or why TNCs invest in host countries in the first place. Building on Dunning’s work, it is feasible to define the principal TNC motivations for investing. TNCs seek certain advantages in specific host countries in terms of natural resources, markets (for manufactures or services), efficiency or other strategic factors. At the same time, the host countries have certain expectations with regards to the benefits that the different TNC strategies will generate. It is here that the factors identified by the spillovers literature are particularly valuable (i.e. TAT, HR, PL, ED). At the same time, a significant amount of empirical research has demonstrated that host countries can be frustrated by certain kinds of endemic problems that arise—according to distinct corporate strategies—and spoil their expectations with regard to the benefits from FDI.

Table 2- Determinants, Benefits and Problems of FDI, by Corporate Strategy

<table>
<thead>
<tr>
<th>A. Key host country determinants</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Natural resource-seeking FDI</td>
<td>Abundance of natural resources</td>
</tr>
<tr>
<td></td>
<td>Access to natural resources</td>
</tr>
<tr>
<td></td>
<td>International commodity price movements</td>
</tr>
<tr>
<td>Market-seeking FDI</td>
<td>Market size, growth and purchasing power</td>
</tr>
<tr>
<td>(national or regional)</td>
<td>Level of tariff protection</td>
</tr>
<tr>
<td></td>
<td>Barriers to entry</td>
</tr>
<tr>
<td></td>
<td>Market structure (competition)</td>
</tr>
<tr>
<td></td>
<td>Local regulatory and supervisory requirements</td>
</tr>
<tr>
<td>Efficiency-seeking, export-oriented FDI</td>
<td>Access to export markets</td>
</tr>
<tr>
<td></td>
<td>Quality and cost of human resources</td>
</tr>
<tr>
<td></td>
<td>Cost of physical infrastructure (ports, roads, telecom)</td>
</tr>
<tr>
<td></td>
<td>Logistics</td>
</tr>
<tr>
<td></td>
<td>Quality of suppliers, clusters, etc.</td>
</tr>
<tr>
<td></td>
<td>International trade and investment commitments</td>
</tr>
<tr>
<td>Strategic asset-seeking FDI</td>
<td>Presence of firm-specific assets</td>
</tr>
<tr>
<td></td>
<td>Science and technology base</td>
</tr>
<tr>
<td></td>
<td>Logistics</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>B. Key benefits expected by host countries</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Natural resource-seeking FDI</td>
<td>Exports of natural resources</td>
</tr>
<tr>
<td></td>
<td>High local content</td>
</tr>
<tr>
<td>FDI</td>
<td>Employment in non-urban areas</td>
</tr>
</tbody>
</table>
Market-seeking FDI (national or regional)  
Local activities  
Systemic competitiveness  
Increased local content  
New production linkages  
Enterprise development  
Efficiency-seeking, export-oriented FDI  
Export competitiveness for manufactures  
Transfers of technology  
Improved human resources  
Deeper production linkages  
Enterprise development  
Advance from assembly to manufacturing  
Strategic asset-seeking FDI  
Science and technology infrastructure  
Logistics development  
C. Principal problems that have arisen  
Natural resource-seeking FDI  
Enclave activities not integrated into local economy  
Low level of local processing  
Cyclical in relation to international prices  
Market-seeking FDI (national or regional)  
Higher cost production or service provision  
Weak international competitiveness  
Not world class  
Regulatory problems for services  
Crowding out of national companies  
Efficiency-seeking, export-oriented FDI  
Getting stuck in low wage assembly, no upgrading  
Focus on static not dynamic advantages  
Limited production linkages: import dependent  
No advance toward clustering  
Crowding out of national companies  
Strategic asset-seeking FDI  
Stagnates at certain level  
Can be out-competed  

In this context, it makes sense to complement the more recent and defensible findings of the spillovers literature with this new perspective focusing on the impact of TNCs with similar strategies, especially where those strategies are the dominant form of FDI in a given host country. The experience on LAC suggests so. After a brief review of the LAC experience with FDI and TNC activities, the following sections focus on the distinct situations of the new and dominant TNC strategies in that region: efficiency-seeking FDI and market-seeking (services) FDI. This will demonstrate that, at a minimum, identifying distinct TNC strategies allows on to classify those different situations in order to compare like ones, thereby producing greater clarity on the more direct impacts of FDI and TNC operations in developing countries.

1. FDI and TNC experiences of Latin America and the Caribbean

The history of LAC has been marked by foreign interventions since the end of the 15th century when Spanish colonization began. During the last century foreign investment has been a central factor in defining the nature of the integration of the region into the international economy, both in the form of external financing and direct investment. The stop-and-go nature of external finance has been a constant challenge to policy makers (ECLAC, 1971, Ffrench-Davis and Griffith-Jones, 1995), particularly during the boom and bust of syndicated lending by transnational banks in the 1970s (Mortimore, 1989 and 1991) that ultimately led to the “lost” decade of the 1980s (ECLAC, 1994). Lost, in this context, means that it did not contribute to the achievement of developmental goals. The recent collapse of FDI inflows raises the specter that something similar might take place with regard to FDI (Chart 1).
Chart 1: Latin America and the Caribbean: net transfer of resources (NTR) a/

a/ The net transfer of resources is equivalent to the net inflow of capital (including net errors and omissions) less the balance in the factor payment account (profits and net interest payments). Negative figures indicate transfers to the exterior. B/ Equivalent to the net inflow of FDI less profit remittances. C/ Equivalent to the net inflow of other capital, different from FDI, less the net payment of interest. D/ Preliminary estimates.
Source: ECLAC

Table 3
Latin America and the Caribbean: Net Inflows of FDI by subregions, 1990-2002 a/

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Mexico, Central America &amp; the Caribbean</td>
<td>6,846</td>
<td>15,229</td>
<td>17,984</td>
<td>18,263</td>
<td>29,465</td>
<td>17,409</td>
</tr>
<tr>
<td>2. South America</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>-Southern Cone</td>
<td>8,956</td>
<td>45,375</td>
<td>70,236</td>
<td>57,320</td>
<td>39,555</td>
<td>28,032</td>
</tr>
<tr>
<td>-Andean Community</td>
<td>6,114</td>
<td>35,590</td>
<td>61,881</td>
<td>48,468</td>
<td>30,723</td>
<td>19,969</td>
</tr>
<tr>
<td>3. Financial centers</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>18,308</td>
<td>69,518</td>
<td>108,030</td>
<td>94,438</td>
<td>84,013</td>
<td>57,441</td>
</tr>
</tbody>
</table>

Source: Information Center of the Unit on Investment and Corporate Strategies, ECLAC. a/ Net inflows (gross inflows – capital remittances by the same foreign enterprises) b/ Annual average c/ Estimates

Table 3 indicates the evolution of FDI inflows to LAC during 1990-2002. The annual averages tripled from over US$ 18 billion in 1990-94 to almost $ 70 billion in 1995-99, peaking at over $ 100 billion in 1999. Between 1999 and 2002 the inflows fell by half. Mexico, Central America and the Caribbean more than doubled their average annual inflows from $ 6.8 billion in 1990-94 to $ 15.2 billion during 1995-99 and generally remained slightly above that average thereafter (2001 was an exceptional year in which the $ 12.5 billion purchase of a Mexican bank by Citigroup much elevated the annual figure). South America experienced more of a roller coaster ride when average annual inflows of about $ 9 billion during 1990-94 were multiplied by a factor of five to $ 45.4 billion during 1995-99 before declining steeply to $ 28 billion in 2002. These figures for South America hide two separate realities. On the one hand, the Andean Community tripled its average annual FDI inflows between the first and second period and
generally maintained that level thereafter. On the other hand, the Southern Cone (Mercosur plus Chile) experienced
the roller coaster ride multiplying average annual inflows by six from $ 6.1 to $ 35.6 billion before seeing those
inflows fall to below $ 20 billion in 2002. Financial centers in the Caribbean experienced strong and growing FDI
inflows until the bottom started to fall out during 2001-2 in association with an OECD initiative to curtail the tax
evasion facilities of those countries. Thus, distinct subregional realities underlay the general picture described above.

Four well-defined focal points of TNC activities / FDI in the region during the 20th century are evident
(Mortimore, 2000). Each indicates a distinct corporate strategy with regards to the essential purpose of the
investment within the context of the TNC organization. Table 4 assists in interpreting the logic of the corporate
strategies driving FDI in LAC.

Traditionally, it was the search for natural resources that explained the presence of foreign activities,
beginning with the Spanish conquistadores search for gold and silver and now manifest in huge investments for the
extraction of other minerals (especially, copper) and the exploration and extraction of hydrocarbons (petroleum and
natural gas). For most of the 20th century FDI by TNCs following natural resource seeking strategies was the
principal kind of FDI in the region. This kind of investment was typically an enclave type of activity characterized
by “extract and export” operations with little local processing. It took place wherever the natural resources were
found. The TNC usually captured the lion’s share of the benefits outside of the host country. In terms of national
benefits, usually they did not extend much beyond the Government’s take from royalties and export taxes and the
relatively high wages of the “labor aristocracy” linked to the extraction process itself (ECLA, 1949; Rodriguez,
1980; Girvan, 1973). This situation led to a wave of nationalizations / expropriations in the petroleum (Peru,
Venezuela, Ecuador) and mining (Chile) sectors during 1968-76 (Pinelo, 1973; Moran, 1974; Petras et al., 1977). In
the last quarter century FDI has been focused mainly on the new access to petroleum and natural gas fields in the
Andean countries and Argentina, and the big mineral projects in Chile, Argentina and Peru. Governments now tend

<table>
<thead>
<tr>
<th>Corporate Strategy / Sector</th>
<th>Raw materials-seeking</th>
<th>Market (national or regional) access-seeking</th>
<th>Efficiency-seeking</th>
<th>Strategic element-seeking</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Goods</strong></td>
<td><strong>Petroleum /natural gas:</strong> Argentina, Venezuela, Colombia, Bolivia, Brazil, Trinidad &amp; Tobago <strong>Minerals:</strong> Chile, Argentina and Peru</td>
<td><strong>Auto industry:</strong> Brazil and Argentina <strong>Agro-industry:</strong> Argentina, Brazil and Mexico <strong>Chemicals:</strong> Brazil <strong>Electricity generation:</strong> Argentina, Chile</td>
<td><strong>Auto industry:</strong> Mexico <strong>Electronics:</strong> Mexico and Caribbean basin ** Apparel:** Caribbean basin and Mexico</td>
<td></td>
</tr>
<tr>
<td><strong>Services</strong></td>
<td></td>
<td><strong>Financial Services:</strong> Brazil, Mexico, Chile, Argentina, Venezuela, Colombia and Peru <strong>Telecommunications:</strong> Brazil, Argentina, Chile and Peru <strong>Retail trade:</strong> Brazil, Argentina, Mexico and Chile <strong>Electricity distribution:</strong> Colombia, Brazil, Argentina and Central America <strong>Gas distribution:</strong> Argentina, Brazil, Chile and Colombia <strong>Tourism:</strong> Mexico, Caribbean basin</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
to capture a larger share of the benefits from FDI in petroleum and natural gas operations due to new modalities (i.e. association contracts, etc.). The fiscal take from the mining projects tends to be smaller, however, do to the intense competition for projects that has led host countries to allow the deduction of the interest payments of these highly leveraged projects before taxes are paid (ECLAC, 2002, Chapter 4; Moguillansky, 1999).

Historically, the second major focal point of TNC activities / FDI in the region was that of market-seeking (manufactures) TNCs during the import-substituting industrialization (ISI) process in the region that generally spanned the 1930-80 period. Governments tried to promote industrialization by establishing high tariff protection against imports (often 100% or more of the price of imports) and offering special benefits to certain sectors. In order to avoid being excluded from growing markets, TNCs responded with a burst of FDI in the automobile, machinery, chemical and agro-industrial sectors of the larger markets of the region, such as Brazil, Mexico and Argentina (Newfarmer and Mueller, 1975; Evans, 1994; Chudnovsky, 1974). This effort did result in the establishment of new manufacturing activities where they did not previously exist, however, it was achieved in an inward-looking and overprotected manner that meant that the new industry was not internationally competitive (Baer, 1972; Hirschman, 1968; Cardoso and Faletto, 1979; Gereffi and Evans, 1981; Newfarmer, 1985, Jenkins, 1984). This produced the unsavory result that, in the automobile industry, for example, the vehicles were overpriced, poor quality, and technologically obsolete (Jenkins, 1974; Mortimore, 1998a and 1998b, Bennett and Sharpe, 1985). Instead of leading the industrialization process as was the case in East Asia, these higher-tech activities dragged it down, especially from a balance of payments perspective due to the high level of imports of components and weak exports (Fajnzylber, 1983; Chudnovsky, 1974; Sunkel et al, 1980; Vaitsos, 1974). This created growing tensions between host governments and foreign investors. The former resorted to a host of performance requirements (minimum local content levels, export obligations and trade balancing) while the latter complained that they could not “export by decree” (Mortimore, 1985 and 1991). The result was a kind of truncated and dependent industrialization process that contrasted sharply with the success of East and South-East Asia (Fajnzylber, 1983; Mortimore, Bonifaz and Duarte, 1997-8). The tensions produced in the local environment were manifest in the new, more restrictive, foreign investment regulations enacted in countries, such as Mexico (1973) (Sepulveda and Chamacero, 1973, Dussel 2000, Mortimore, 1998, Mortimore, Buitelaar and Bonifaz, 2000) and the members of Andean Pact (1969) (Vaitsos, 1974-1980; Rodriguez, 1980; Dos Santos, 1970); and those that understood it as imperialism or exploitation (i.e. Caputo y Pizarro, 1970; Frank, 1977).

The disputes over the nationalization / expropriation of petroleum and mining subsidiaries, the rising tensions with the subsidiaries of manufacturing companies in the context of the exhaustion of the ISI process, and the disinterest of transnational banks to continue placing syndicated loans in the region combined to produce a severe and chronic economic crisis. These negative experiences fueled the dependencia debate in Latin America, one that blamed most of the region’s ills on external factors, especially TNCs, and recommended inward-looking, independent developmental models.3 Events soon left this debate behind.

Sooner or later, in the face of a chronic net external transfer of resources, virtually all countries of the region jettisoned their inward-looking, nationalistic orientations in the course of the 1980s and embraced the central tenets of the Washington consensus designed by the principal national and international organizations located in Washington (US Government, IMF, World Bank, IDB) (Gore, 2000). Those tenets were: the reduction in the size and role of the State, the implementation of a more private sector-based economic model, an opening up of the economy to trade and foreign investment, and a sustained effort to raise export performance, etc. This led to a proliferation of FDI-friendly policies in the region that coincided with the global boom in FDI flows that produced the huge increase in FDI inflows to LAC.

This boom was driven by different corporate strategies that those of the past. Although the FDI inflows are not that large in terms of the overall capital formation in the region, the new neo-conservative outlook to

---

3 The dependency school of thought had at least three variants, those that identified dependency with external vulnerability (i.e. Furtado, 1970; Cardoso and Faletto, 1979); those that saw it as a structural phenomenon related to the international expansion of transnational corporations (i.e. Sunkel, 1973, 1980, 1993; Sunkel and Mortimore, 2001; Rodriguez, 1980; Dos Santos, 1970); and those that understood it as imperialism or exploitation (i.e. Caputo y Pizarro, 1970; Frank, 1977).
policymaking and the absence of defined developmental strategies often produce the effect that these new dominant corporate strategies of principal foreign investors (efficiency-seeking and market-seeking for services) often became the de facto focus of the host economic model. In this changed policy environment in Latin America, the new TNC activities and inflows of FDI driven by different corporate strategies (efficiency-seeking, market-seeking for services) have now surpassed those motivated by the older or more traditional ones (natural resource-seeking, market-seeking for manufactures) (Mortimore 2000).

2. Efficiency-seeking FDI and TNC operations in LAC

The efficiency-seeking TNC activities in the region are manifest in export platforms established mainly to form part of international or regional systems of integrated production of the TNCs (Mortimore y Peres, 2001; Mortimore, Vergara and Katz, 2001; UNCTAD 2002a). These have attained a higher or more sophisticated level in the form of the automotive and electronics platforms in Mexico (Mortimore, 1998a and 1998b; Dussel, 1999 and 2000) and a lower or less sophisticated level in the form of the apparel platforms in Central America and the Caribbean (Mortimore 2002 and 1999). It is relevant to distinguish between these two kinds of export platform because their developmental impacts in LAC are distinct.

In Mexico, the efficiency-seeking TNC activities stemmed primarily from greenfield investment in new export platforms usually operating via the maquiladora scheme for export assembly. Some of the favorable impacts of this FDI were to greatly increase exports and improve export competitiveness to the extent that Mexico became one of the ten winner countries associated with the new international systems of integrated production (UNCTAD 2002). These export platforms provide employment to more than 1 million Mexicans and represent the dynamic part of the manufacturing sector, although the recession in the US market has taken some of the shine off them. The automotive cluster is particularly impressive, providing exports of $31.7 billion in 2001 (or 20% of Mexico’s total exports) and generating a favorable balance of payments in the order of $8.9 billion (Bancomext, 2002). In 1994, automotive exports had amounted to only $10.8 billion and the automotive industry then generated a deficit of $0.7 billion. Seventy percent of the current exports are vehicles and thirty percent are auto parts. Although 93.8% of the exports go to one sole market—the North American one—in the context of the North American Free Trade Agreement (NAFTA) signed in 1994, the Free Trade Agreement signed in 2000 with the European Union promises to diversify them. Evidence on production impacts is limited, however, it seems that the configuration of the automotive cluster has produced significant production linkages and the upgrading of human resources (Carillo, 1995; Lara and Carillo, 2003, Romo, 2003). The effects in terms of transfer of technology and enterprise development are less noteworthy. Another positive factor is found in the apparel industry where the effect of the NAFTA rules of origin is generating production linkages and some “full package” providers in terms of enterprise development related to new organizational practices (Bair and Gereffi, 2003; Gereffi and Bair, 1998). Thus, many of the export platforms in Mexico have produced very significant results, especially in terms of export competitiveness of the automotive and apparel industries.

Some negative impacts have also been attributed to the export platforms in Mexico. For example, the dynamism of the export sector has not been transmitted to the rest of the economy, suggesting that it is not well integrated into the economy as a whole (Dussel, 1999). While exports grew at almost 18% a year over the 1994-2002 period, the GDP grew at only 3% a year (CEPAL, 2002). In other words, the link between FDI inflows and GDP growth was not clear. The extreme dependence on the NAFTA market introduced a cyclical element to export performance. The electronics industry (dominated by Asian TNCs) possessed few of the production advantages—production linkages and enterprise development—associated with the automotive and clothing industries (dominated by US TNCs) and even the latter were mainly limited to foreign not Mexican suppliers (Carrillo and Zarate, 2001; Contreras, 2001; Dutrenit and Vera-Cruz, 2001; Gomis, 2001; Gonzalez and Barrajas, 2001; and Jaen and Leon, 2001). Finally, the NAFTA itself and many of the bilateral investment agreements signed by Mexico contained elements that put limitations on future policy choices to deal with some of these shortcomings. The opportunity afforded foreign investors to litigate against State policy outside of Mexico produced uncertainty about the space for and effectiveness of national policy. The number of performance requirements prohibited by NAFTA was much greater than the Trade Related Investment Measures (TRIMs) agreement of the World Trade Organization (WTO) and represented a harsher environment for policy makers dealing with production effects. Finally, the maquiladora format used by many exporters severely reduced the taxes paid by them, weakening the fiscal link between the export platforms and the National Treasury (Dussel, 2001). Thus, in spite of their evident successes with regard to
export competitiveness the effect on the overall production apparatus was muted and the ability to deal with these shortcomings was limited by international agreements.

In the case of Central America and the Caribbean (CAC) the situation was somewhat distinct. The apparel industry was the focus of TNC activities operating in host country export processing zones (EPZ), usually in the context the US production sharing mechanism. The apparel industry produced over half of the exports of many of these countries. A significant amount of new exports were generated by way of these TNC activities, both through FDI in new, more efficient plants and through buyers’ contracts with foreign and local assemblers. The export competitiveness of the subregion demonstrated a marked improvement as a result. Other positive effects were the generation of new jobs (especially for women in non-urban settings), some upgrading of human resources, and some enterprise development as local companies bid for and won assembly contracts. Thus many of the export platforms in CAC generated a surge in exports from the apparel industry and this considerably improved the export competitiveness of the subregion.

Many negative impacts have been attributed to these export platforms. Unlike the situation in Asia where EPZs often were converted into industrial zones and become linked to science and technology parks (ESCAP, 1994), the EPZs in CAC often get stuck in a rut. On the one hand, the US production sharing mechanism effectively limited the CAC contribution to an assembly stage of production utilizing US inputs since tariffs are applied to all value added outside of the US upon entry to the US market. This leads the TNC activities in this industry to focus primarily on low wages in CAC (Mortimore, 1999 and 2002). On the other hand, the intense competition for plants and contracts in the context of US import quotas can lead to a “race to the bottom” in terms of competitive devaluations, wage repression, and reduced social security benefits, and a “race to the top” with respect to (over dimensioned) incentives, both of which severely reduce the national benefits deriving from such operations (Mortimore and Peres, 1997 and 1998). Very little in the way of production linkages or technology transfer is forthcoming. CAC does not have the benefit of anything similar to the NAFTA rules of origin that work in favor of the further integration of the Mexican apparel industry, since physical inputs for NAFTA can come from the US, Canada or Mexico. The Caribbean Basin Trade Partnership Act of 2000 attempted to face up to that problem by doing away with some quotas, allowing for the incorporation of a certain amount of locally-produced cloth and permitting some further local processing (cutting, stone washing, etc.). Furthermore, it is hoped that the Central American Free Trade Agreement currently under negotiation will provide NAFTA-like rules of origin for the apparel industry; however, the US textile industry seems set on maintaining the existing restrictions. To date, nonetheless, the CAC apparel export platforms have been limited to one market—the United States—and one function—simple assembly of US-made components. Any possible upgrading of these operations will have to take place very fast to be feasible as the last part of the WTO Agreement on Clothing and Textiles will kick in as of 2005 and that will mean that CAC apparel producers will face a much harsher competitive environment in the US market do to the increased presence of Asian, especially Chinese, competitors. Thus, the apparel export platforms enjoyed success with regard to export competitiveness, however, the effect on the overall production apparatus was truncated by the primary mechanism used to gain access to the US market (Mortimore and Zamora, 1998; Mortimore, Vicens and Martinez, 1998; Mortimore, Duthoo and Guerrero, 1995). Recent alterations in bilateral and international agreements appear not to be sufficiently comprehensive or rapid to make much of a difference.

This evaluation of the main efficiency-seeking TNC activities in Latin America—those in Mexico and CAC—suggests that the indicators of success in terms of new exports and export competitiveness are truly impressive and much superior to the rest of Latin America (Table 5) (ECLAC 2001 and 2002). Nonetheless, this success does not square with the reality of Mexico and the CAC at the level of production. Evidently, the impacts of the transmission belts associated with the transfer and assimilate of technology, the construction and deepening of production linkages, the upgrading of human resources and enterprise development are smaller or different from what is generally assumed in terms of the spillovers literature. Moreover, there is a huge difference between the situation of Mexico and that of CAC in the sense that the national benefits of the latter associated with the apparel industry are exceptionally small and vulnerable. It would appear that, in the absence of a host country development strategy, the benefits generated from these kinds of TNC activities based on efficiency-seeking considerations accrue primarily to the TNCs themselves and not the host countries. While the situation in Mexico is qualitatively superior to that of Central America and the Caribbean, it is still not good enough.

The only country in Latin America in which the efficiency-seeking TNCs activities are dominant and in which a new national developmental strategy has been implemented to improve upon the existing shortcomings is
the exceptional case of Costa Rica (Salazar, 1998). This country had a developmental trajectory very similar to other countries of CAC in which the apparel export platform represented its principal link to the international economy (Mortimore and Zamora, 1998). With the end of the civil wars in other parts of Central America higher wage Costa Rica came under considerable competitive pressures. Instead of opting for the “low road” to export competitiveness encompassing competitive devaluations, repressed wages, reduced social security benefits, and never-ending incentives, Costa Rica chose to design and implement a new development strategy based on attracting FDI to upgrade into more technologically-sophisticated activities (Robles, 2000). A considerable amount of success was achieved in electronics, medical devices and logistics. The attraction of the much fought-over Intel microprocessor assembly and testing plants worth $500 million boosted Costa Rican exports by about 30% and greatly improved its export competitiveness (Spar, 1998; ECLAC, 2000). Beyond that, the Intel investment also stimulated advances in other fields especially services, where Costa Rica is developing into a significant exporter of software (UNCTAD, 2002b). Some of the major decisions that backed up the new developmental strategy were those related to investing heavily in education (6% of GDP), emphasizing technical and English language capabilities, an active FDI policy based on setting national priorities, identifying the TNCs to be targeted and negotiating firm-level packages, and designing and implementing industrial policies to deal with some of the problems which arise (Egloff, 2001). Of particular importance is the fact that these policies are in tune with the development strategy (A. Gonzalez, 2002) and that the TNCs activities are evaluated in that light. In this sense, Costa Rica’s development strategy possessed elements found in well-known success stories, such as Singapore and Ireland.

Efficiency-seeking FDI / TNC activities have redefined the integration of Mexico and the Caribbean basin into the international market. The spillovers literature identifies the transmission belts that are most relevant for measuring and evaluating this impact in the form of transferring and assimilating technology, upgrading human resources, building production linkages and promoting local enterprise development, however, it does not separate country situations according to the distinct corporate strategies that drive that FDI or the different policies needed to ensure that the benefits are also enjoyed by the host country, as well as the investing TNC. Thus, the spillovers literature is relevant but not that useful unless like situations –such as the countries playing host to major components of the international systems of integrated production of efficiency-seeking TNCs—are compared.4 This brief analysis of aspects of the electronics, automotive and apparel industries in their real-world settings in Mexico and the Caribbean basin demonstrates the usefulness of this methodology. Costa Rica stands out as an example of what can be achieved by successfully combining the correct policy framework—one that reflects the priorities of the national development strategy—with the dominant corporate strategy.

4. Market-seeking (services) FDI and TNC activities in LAC

Unlike the situation with manufacturing activities—especially those associated with efficiency-seeking FDI—the spillovers literature remains uncharacteristically silent on the subject of FDI in services. Here, the TAT, HR, PL and ED variables are less relevant and harder to measure. Another analytical focus is needed.

The most important market-seeking TNC activities in the region are those associated with the opening up of services previously closed to FDI, such as telecommunications and other infrastructure (sanitary services, distribution of gas and electricity, airport administration, etc.), financial services, and retail commerce, among others (ECLAC 2001 and 2003). The FDI linked to this corporate strategy comes mainly in the form of acquisitions (including privatizations), primarily involves European TNCs, and takes place principally in the larger economies of the region, such as Brazil, Mexico, Argentina and Chile. This FDI has contributed significantly to the modernization of these economies and the improvement of their systemic competitiveness (that is, it makes exporting easier but does not directly generate exports), however, with the exception of Mexico, the huge increase in profit and capital remittances has often created severe balance of payments constraints—especially in countries with weak international competitiveness (Table 5) and low export / GDP ratios, such as Brazil and Argentina—once the original investment is concretized. The crowding out of private national companies has often been a problem as well. The design and implementation of national policies and regulations have been critical factors in dealing with some of the problems that have arisen. The subsequent analysis will deal with the situation of two of the principal services contrasting the experiences of Argentina and Brazil. Mention will be made of new FDI policy initiatives in Chile aimed at improving on or complementing the market-seeking (services) mold.

4 It might be mentioned that there exists a large and growing literature on global value chains that also is very useful in this regard. See http://www.ids.ac.uk/globalvaluechains/
### Table 5

Latin America and the Caribbean: international competitiveness in world imports, 1985-2000  
(import market shares in percentage)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>MEXICO AND CARIBBEAN BASIN</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Overall market shares</td>
<td>2.39</td>
<td>1.96</td>
<td>2.40</td>
<td>3.35</td>
<td>40.2</td>
</tr>
<tr>
<td>1. Natural resources</td>
<td>5.01</td>
<td>3.56</td>
<td>3.28</td>
<td>3.54</td>
<td>-29.3</td>
</tr>
<tr>
<td>2. Manufactures based on natural resources</td>
<td>2.09</td>
<td>1.82</td>
<td>1.86</td>
<td>2.10</td>
<td>-</td>
</tr>
<tr>
<td>3. Manufactures not based on natural resources</td>
<td>1.34</td>
<td>1.55</td>
<td>2.33</td>
<td>3.57</td>
<td>166.4</td>
</tr>
<tr>
<td>- Low technology</td>
<td>1.25</td>
<td>1.53</td>
<td>2.48</td>
<td>3.92</td>
<td>213.6</td>
</tr>
<tr>
<td>- Medium technology</td>
<td>1.27</td>
<td>1.64</td>
<td>2.51</td>
<td>3.68</td>
<td>189.8</td>
</tr>
<tr>
<td>- High technology</td>
<td>1.66</td>
<td>1.40</td>
<td>1.91</td>
<td>3.19</td>
<td>92.2</td>
</tr>
<tr>
<td>4. Others</td>
<td>2.06</td>
<td>2.01</td>
<td>2.37</td>
<td>3.27</td>
<td>58.7</td>
</tr>
<tr>
<td><strong>SOUTH AMERICA</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Overall market shares</td>
<td>3.40</td>
<td>2.76</td>
<td>2.76</td>
<td>2.62</td>
<td>-22.9</td>
</tr>
<tr>
<td>1. Natural resources</td>
<td>6.82</td>
<td>7.16</td>
<td>8.33</td>
<td>8.50</td>
<td>24.6</td>
</tr>
<tr>
<td>2. Manufactures based on natural resources</td>
<td>5.55</td>
<td>4.66</td>
<td>4.93</td>
<td>4.93</td>
<td>-11.2</td>
</tr>
<tr>
<td>3. Manufactures not based on natural resources</td>
<td>1.24</td>
<td>1.14</td>
<td>1.12</td>
<td>1.03</td>
<td>-16.9</td>
</tr>
<tr>
<td>- Low technology</td>
<td>1.96</td>
<td>1.75</td>
<td>1.66</td>
<td>1.42</td>
<td>-27.6</td>
</tr>
<tr>
<td>- Medium technology</td>
<td>1.20</td>
<td>1.21</td>
<td>1.34</td>
<td>1.27</td>
<td>5.8</td>
</tr>
<tr>
<td>- High technology</td>
<td>0.47</td>
<td>0.36</td>
<td>0.29</td>
<td>0.45</td>
<td>-4.3</td>
</tr>
<tr>
<td>4. Others</td>
<td>2.10</td>
<td>2.11</td>
<td>1.35</td>
<td>1.56</td>
<td>-25.7</td>
</tr>
</tbody>
</table>

Source: Based on the ECLAC, TradeCAN 2002 Edition, computer program on international competitiveness.  
Merchandise trade groups defined according Lall (2000) using the Standard International Trade Classification (SITC Rev. 2).

The telecommunications industry in Latin America was one of the first services to be opened to foreign investment. In many ways it became a test case of the region’s ability to attract FDI. Some governments started from the premise that the sale of State assets to private, usually foreign, investors was in itself the solution to the problems of inefficiency, poor service, low investment and high debts often associated with State service providers. In fact the privatization of State assets often simply transformed a public monopoly into a private one. The original policy goals often never went beyond attracting foreign investment and getting the highest price for State assets. The regulatory framework for the sector was often drawn up after the privatization had taken place. Rarely was the principal objective a conscientious and well thought-out telecommunications policy aimed at national developmental goals. Argentina and Brazil represent extreme examples in this regard.

Argentina was still in the throes of a severe economic crisis characterized by fierce hyperinflation at the beginning of the 1990s when the new government decided to make the sale of the State telecommunications company a showcase for attracting FDI (ECLAC 2001). Argentina’s policy in this sector during the following 10 years can be referred to as “cashing in”. The sale of the State telecommunications company –Entel—was to convince foreign investors that Argentina was open for business. Entel was divided into two monopoly operations, one in the north of the country and the other in the south. The privatization rules permitted payment with discounted government debt paper which meant that, with hindsight, the assets were sold cheap and in very favorable conditions for the two winner groups: Telefonica / Citibank in the south and France Telecom / Telecom Italia in the north. These operators were given 7 years of exclusivity (followed by a two year extension) and beneficial operational guidelines that demanded far less in terms of investment and price reductions than their efficiency gains generated (Abeles, Forcinito and Schorr, 1999; Azpiazu, 1999). The regulatory authority was established after the fact by decree rather than by way of an Act of Congress. When the regulators began to take their job seriously the government stripped away many of their powers. In both fixed-line and mobile services government policy favored the two dominant operators. Only in 2000 was a significant degree of competition introduced into the industry. There is no denying that a huge amount of new investment went into the sector, that customer costs dropped considerably (but still remained comparatively high) and most service performance indicators improved noticeably...
(although not as fast as those of most other countries of the region). However, the cost of such can be considered exceedingly and excessively high.

The Brazilian policy for opening up the telecommunications sector demonstrated that their policy makers had learned from the experiences of others. Their policy might be referred to as “getting a boost”. In 1995, the Brazilian Federal Constitution was modified to allow for the licensing of service provision to private sector agents. Two years later the Telecommunications Act was enacted to provide a regulatory framework for telecommunications, including the industry’s regulatory authority, ANATEL, in association with the competition authority, CADE. During 1994-97, the majority State-owned telecommunications company –Telebras—invested over $20 billion to prepare the company to be privatized in a rational and orderly fashion. In 1998, Telebras, was privatized by auction along with a host of other assets for $26.7 billion. The interesting aspect here is that Telebras was divided into 12 different pieces (one long distance provider, 3 fixed line providers, 8 mobile operators) which, together with the mirror companies, ensured a reasonable degree of competition during the short transition, 1998-2001, until fuller competition came into force. The principal foreign investors were Telefonica España, Telecom Italia, Portugal Telecom, BellSouth and MCI Worldcom. This process stimulated a huge amount of greenfield investment in extending the existing infrastructure. This posterior investment was guided by developmental goals established by the telecommunications policy, such as universal service, better performance and lower costs (Herrera, 1998). The result was that the telecommunications policy and the Brazilian economy were given a significant boost by the opening up of the sector to telecom TNCs.

The relative performance of the telecom industry in Argentina and Brazil is demonstrated in Table 6. Each and every of the five separate indicators suggests that the performance of the telecoms industry in Brazil was superior to that of Argentina over the same period.

<table>
<thead>
<tr>
<th>Indicator</th>
<th>1990</th>
<th>1995</th>
<th>2002</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Main lines per 100 inhabitants</td>
<td>Argentina 9.3</td>
<td>15.9</td>
<td>21.8</td>
</tr>
<tr>
<td></td>
<td>Brazil 6.5</td>
<td>8.5</td>
<td>22.3</td>
</tr>
<tr>
<td>2. Cellular telephone subscribers per 100 inhabitants</td>
<td>Argentina 0.04</td>
<td>0.98</td>
<td>17.7</td>
</tr>
<tr>
<td></td>
<td>Brazil 0.02</td>
<td>0.83</td>
<td>20.1</td>
</tr>
<tr>
<td>3. Complaints per 100 main lines</td>
<td>Argentina 42.4</td>
<td>29.5</td>
<td>17.3</td>
</tr>
<tr>
<td></td>
<td>Brazil 4.7</td>
<td>3.2</td>
<td>3.8</td>
</tr>
<tr>
<td>4. Charge for residential line connection (dollars)</td>
<td>Argentina 2155</td>
<td>500</td>
<td>150</td>
</tr>
<tr>
<td></td>
<td>Brazil 1215</td>
<td>43</td>
<td></td>
</tr>
<tr>
<td>5. Charge for business line connection (dollars)</td>
<td>Argentina 5338</td>
<td>750</td>
<td>150</td>
</tr>
<tr>
<td></td>
<td>Brazil 1215</td>
<td>43</td>
<td></td>
</tr>
</tbody>
</table>

Source: based on ECLAC, (2001) and International Telecommunications Union, www.itu.int

With regard to financial services, the principal aims of Latin American policy makers were to bring in transnational banks (TNBs) to avoid the perennial financial crises that have characterized the region and to improve the efficiency of the sector (ECLAC, 2003, Chapter 3; Stallings and Studart, 2000). This took place in two phases across the region. The first phase encompassed the attraction of TNBs by way of opening up the sector, offering State guarantees and capital injections to make the sector more attractive, and reducing the role of State banks and easing controls over interest rates and credit allocation. The second phase represented an attempt to improve the regulatory and supervision aspects of financial services (capital reserves, risk analysis, transparency, institutional development, etc.). The effect was immediate as the TNB share of total financial sector assets in the region jumped from about 10 to over 50 percent. Three universal banks led the wave of acquisitions in the region. The Santander group ($16.4 billion), the Banco Bilbao group ($9.6 billion) and Citigroup ($12.5 billion) investments during this period surpassed $38 billion. The 2001 market shares for loans of Santander (10.4%), BBVA (9.3%) and Citigroup (9.1%) accounted for over half of the total share for foreign banks (63.8%) in Latin America. Other major players in more traditional activities or specific segments included FleetBoston, Scotiabank, HSBC, ABN Amro and Lloyds. In other words, a very small group of TNBs spearheaded the entry of foreign direct investment in the financial services sector of Latin America (Calderon and Casilda, 2000). An analysis of the first decade of heightened TNB activity in Latin American financial services (ECLAC, 2003) finds that the increased competition from the larger foreign
presence in the sector has produced microeconomic benefits in the form of improved efficiency and more liquidity, however, has not led to the hoped-for macroeconomic benefits, that is, the availability of more credit at lower cost, improved systemic stability of the sector and the TNBs playing a role of lender of last resort to it affiliates in the region. Moreover, many TNBs feel discontent because their costly positioning in the region coincided with the spread of financial crises. The experiences in the region vary considerably in terms of the national policies applied to this sector. Argentina and Brazil again represent polar examples in this regard.

The Argentine experience with huge FDI inflows into the financial services sector might be referred to as ‘blind faith’. The 1994 financial crisis in Argentina was comparable in magnitude and effects to those that took place in Mexico, Russia and the Asian NICs. Argentine policy makers put their faith in the massive entry of foreign banks to correct this weakness by way of privatizing the dominant state bank sector and otherwise attracting foreign ones. Over 11% of the $75.5 billion of FDI inflows that entered the country between 1992 and 2000 went to the financial services sector (ECLAC 2002, Chapter 2). Between 1994 and 2001 the foreign bank share of financial sector assets rose from 18 to 61 percent. The principal market shares (assets) belonged to Santander (8%), FleetBoston (8%), BBVA (7%), Citigroup (6%), HSBC (4%) and Scotiabank (3%) and the highest exposure in terms of Argentine assets in their Latin American assets belonged to FleetBoston (30%), HSBC (27%) and Scotiabank (16%) (ECLAC 2003, Chapter 3). As a consequence, local banks were crowded out. The regulatory and supervision situations were murky at best. The presence of foreign banks produced many positive impacts in terms of modernizing the sector, however, there have been no dramatic differences in microeconomic efficiency demonstrated to date by foreign banks in comparison to local ones. With regard to macroeconomic effectiveness, the indicators were rather dismal as the new financial crisis set in as of 2000: the growth in the availability of credit fell from 1.4% to –17.6% between 1997-2000 and 2000-2001, the cost of such credit to users rose from 11 to 27% and system stability broke down with foreign banks offering no guarantees to savers and no assurances against possible runs. The “pesification” of debts coupled with a 70% devaluation of the peso and the freezing of bank accounts pushed many banks to the wall (ECLAC 2002, Chapter 2). Scotiabank and Credit Agricole bailed out of Argentina as a result. This experience exploded the myth that TNBs by definition represented bulwarks against further financial crises do to their better risk management, the effect of their home country regulatory and supervisory institutions and the headquarters firms’ obligations to their own subsidiaries. At the same time, the Argentine regulatory and supervisory institutions did not perform as expected.

The comparable Brazilian experience might be referred to as “spreading the risk”. The Brazilian economy in the mid-1990s was suffering a bout of hyperinflation that was faced up to by way of the Plan Real. Brazilian policy makers thought that the entry of foreign banks to compete with local banks would consolidate that process. Over 15% of the FDI inflows that entered the country between 1996 and 2002 went to the financial services sector. The foreign bank share of financial sector assets rose from 14 to 49 percent. The principal market shares (assets) belonged to Santander (4%), ABN (4%), HSBC (3%), BBVA (2%), and Citigroup (2%) between 1994 and 2001 (ECLAC 2003, Chapter 3). Unlike the case of Argentina, local banks were crowded out only temporarily as they are presently making a strong comeback during difficult times (ECLAC 2003, Chapter 1). The stricter regulatory and supervision practices were part of the reason why this took place. The presence of foreign banks forced local banks to improve their performance, particularly in terms of microeconomic efficiency. With regard to macroeconomic effectiveness, the indicators improved from a weak base: the growth in the availability of credit fell from 11.4% to 14.4% between 1997-2000 and 2000-2001, the cost of such credit to users fell from 67 to 46% (although still outrageously high). Although the Brazilian financial system came under great stress, especially once the Argentine crisis began, it weathered the storm. Two of the largest private local banks in Brazil (and Latin America) –Bradesco and Itaú – reversed the regional trend toward crowding out and denationalization by way of their acquisitions of local banks (including some foreign banks) often by way of privatizations. In other words, the nature of policy making in Brazil including managing the bout of hyperinflation, introducing more competition in financial services, establishing a strict regulatory framework under competent supervision, and not putting all their eggs in the TNB basket, led to a better outcome.

Table 7 offers some indicators on the performance of the financial services sector. One must interprete these indicators with great care as both countries suffered severe financial crises during the period under analysis. The figures on the real variation suggest that Brazil’s overall performance was appreciably better than that of Argentina during 1997-2001. The other four indicators offer an added dimension by differentiating the results by nationality of bank. Here, the bottom line is that in Brazil the financial performance indicators of foreign banks are superior to those of local banks, the opposite of the situation in Argentina. To the extent that these figures reflect on the nature
of opening up of the financial services sector to foreign banks, Brazil’s results were clearly better than those of Argentina.

Table 7
Indicators of Financial Sector Performance, 1997-2001
(percentages)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Real variation in credit&lt;sup&gt;a&lt;/sup&gt;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Argentina</td>
<td>1.4</td>
<td>-17.6</td>
</tr>
<tr>
<td>Brazil</td>
<td>11.4</td>
<td>14.4</td>
</tr>
<tr>
<td>2. Profitability&lt;sup&gt;b&lt;/sup&gt;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Argentina</td>
<td>0.8</td>
<td>0.3</td>
</tr>
<tr>
<td>Brazil</td>
<td>0.9</td>
<td>0.7</td>
</tr>
<tr>
<td>3. Liquidity&lt;sup&gt;c&lt;/sup&gt;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Argentina</td>
<td>84.5</td>
<td>91.9</td>
</tr>
<tr>
<td>Brazil</td>
<td>95.2</td>
<td>201.5</td>
</tr>
<tr>
<td>4. Efficiency&lt;sup&gt;d&lt;/sup&gt;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Argentina</td>
<td>268</td>
<td>190</td>
</tr>
<tr>
<td>Brazil</td>
<td>143</td>
<td>158</td>
</tr>
</tbody>
</table>

<sup>a</sup>/ Figures in constant 1998 values.  <sup>b</sup>/ Return on assets.  <sup>c</sup>/Loanable funds as percent of total deposits.  <sup>d</sup>/ Overdue loans as percent of loan loss reserves

Even this very compressed analysis of the experiences of two of the principal country recipients of market seeking (services) FDI in Latin America permits the differentiation of those experiences in terms of impact. In both the telecommunications and financial services sector, the outcome in Brazil was far superior to that of Argentina. The key features distinguishing those results were the role played by national policy in terms of defining developmental goals in each industry and the guidance provided by regulatory and supervisory authorities.

Before concluding, it makes sense to refer the recent policy initiatives of another principal recipient of market seeking (services) in Latin America: Chile. This country was a pioneer in much of the opening up to FDI that took place in the region. It opened up telecommunications and financial services much before other Latin American countries and with a considerable degree of success in terms of the amount of FDI attracted, and its impact in modernizing many services. Chile has one of the best telecommunications infrastructures in the region and has the best record for avoiding financial crises since the late 1980s. It also has come to appreciate the limitations of policies based exclusively on attracting FDI by way of horizontal policies (ECLAC, 2000, Chapter 1) and is now attempting to define what it considers the priority areas for targeting FDI attraction at the national (information technology, electronics, biotechnology and new materials) and subnational levels, and new more proactive instruments (direct contacts, strategic offices, incentives, etc.) to carry it out. During the last two years, Chile has implemented a two track policy initiative of a more focused or targeted nature to attract FDI to these more technologically-sophisticated activities and services in which Chile can serve as a platform to access the rest of South America. As part of this initiative, Chile’s President Ricardo Lagos opened a promotion office in Silicon Valley and has proposed Valparaiso as the country’s new technology capital. This new effort has produced results in the form of Motorola’s development center for wireless solutions, Ericsson’s regional development center, Santander’s regional development center, Santander’s regional technology center and Delta’s regional client contact center. The new policy initiative is based on making Chile’s role in Latin America similar to that of Ireland in Europe or that of Singapore in Asia. This represents the first attempt in South America to move from the easy stage of attracting FDI by way of horizontal instruments –where more FDI is better—to a more difficult stage based on selective instruments and FDI targeting –where the quality more than the volume of FDI is the focus.
This section on FDI driven by market-seeking (services) corporate strategies in Latin America demonstrates that the spillovers literature has virtually no relevance for measuring and evaluating impacts of FDI driven by this corporate strategy. In fact, the impacts vary from service to service and country to country. The brief analysis of FDI in telecommunications and financial services in Argentina and Brazil demonstrated that a clear definition of developmental goals in the context of reliable regulatory and supervisory norms and institutions are critical to obtaining national benefits. Argentina and Brazil were polar examples in this regard.

5. Conclusions and Policy Recommendations

The critical analysis of the spillovers literature allowed us to question the original findings that suggested that a “the more, the better” FDI policy was a host country’s best option. Even the more recent empirical studies of that line of analysis suggest that, increasingly, negative or mixed not positive impacts are encountered in the analysis of developing countries and transition economies. One very useful aspect of that kind of analysis was the identification of the principal transmission belts of FDI and TNC impacts, those associated with the transfer and assimilation of technology, improving human resources, establishing and deepening production linkages and enterprise development. However, even these useful aspects of the spillovers literature were limited basically to FDI and TNC operations in the manufacturing sector.

We used the analysis of these transmission belts in LAC in the context of one dominant TNC strategy in the manufacturing sector: the efficiency-seeking one. The analysis of the cases of Mexico and the Caribbean basin demonstrated the usefulness of that approach. It demonstrated that in the absence of a development strategy the benefits of this category of FDI tend to accrue primarily to the investing TNCs, not the host countries. The case of Costa Rica indicated that an active FDI policy that targeted the TNCs employing efficiency-seeking FDI strategies deemed most coherent and coincident with the host country development strategy produced far better results than a “the more, the better” FDI policy, such as that which was common until recently in Mexico and still persists in most of the Caribbean basin.

With regards to the market-seeking (services) FDI strategy of TNC in LAC, the spillovers literature did not offer much in order to analyze the impacts on development. Here, the TAT, HR, PL and ED transmission belts were less relevant and difficult to measure. In order to get a clearer understanding of the impact of such corporate strategies in the countries in which that FDI strategy is dominant, it was necessary to incorporate another kind of analysis more pertinent to the reality of services, such as telecommunications and financial services. Argentina and Brazil provided two polar cases with regard to FDI and TNC impacts in those services. While many of the relevant factors were specific to the separate services, it was found that the existence of a sectoral development strategy on the part of host country authorities and their responsibility in liberalizing those sectors were two central aspects in defining development impacts. In particular, the establishment of a responsible regulatory framework and consequential sectoral institutions were critical to success. Argentina implemented a “the more, the better” FDI policy with disastrous results. Brazil did much better with a more focused and careful liberalization process in which the quantity of FDI was not the principal priority. In this respect, the more appropriate FDI policy was an active one in terms of understanding the corporate strategies of the TNCs demonstrating interest in the sale of local assets (State or private sector) in order to establish the best contingent investment requirements in association with regulatory and competition authorities.

In both cases, the analysis of development impacts of FDI and TNC in LAC was facilitated by comparing like corporate FDI strategies in the countries where those strategies represented the dominant FDI strategy by TNCs, that is, Mexico and the Caribbean basin with regard to efficiency-seeking FDI and Argentina and Brazil in terms of market-seeking (services) FDI. In the first case, the transmission belts identified by the spillovers literature were relevant, but that was the case for FDI in services. In both cases, the original FDI policy recommendation emanating from the spillovers literature—“the more, the better”—was way off base. An active and targeted FDI policy aimed at achieving priority goals defined in the national development strategy would seem to work much better.
Bibliography


Barry, F., Gorg, H. and E. Strobl. (2001), “Foreign direct investment and wages in domestic firms: productivity spillovers vs. labor market crowding out”, mimeo, University College Dublin and University of Nottingham;


Cardoso F. and E. Faletto (1979), *Dependency and Development in Latin America*, University of California Press;


Contreras, O. (2001), ‘ empleo, estructura ocupacional y salarios en las maquiladoras del televisor’, seminar on ‘Challenges and Perspectives of the Mexican maquiladoras: local settings and global processes’, organized by the University Center for Social Sciences and Humanities (CUCSH) and the College of the Northern Frontier (COLEF) in Guadalajara, Jalisco, 30-31 October;


Dutrenit, G. and A. Vera-Cruz (2001), ‘Las PYMEs antes las redes de proveedores de la maquila ¡reto o utopía?’, seminar on ‘Challenges and Perspectives of the Mexican maquiladoras: local settings and global processes’, organized by the University Center for Social Sciences and Humanities (CUCSH) and the College of the Northern Frontier (COLEF) in Guadalajara, Jalisco, 30-31 October;

Evans, P. (1994), Dependent Development: the alliance of multinational, State and local capital in Brazil, Princeton University;

Fajnzylber, F. (1983), La industrialización truncada de América Latina, Editorial Nueva Imagen, México;


Fuentes, N. and S. Martinez-Pellegrini (2001), ‘Sistemas productivos locales en BC’, seminar on ‘Challenges and Perspectives of the Mexican maquiladoras: local settings and global processes’, organized by the University Center for Social Sciences and Humanities (CUCSH) and the College of the Northern Frontier (COLEF) in Guadalajara, Jalisco, 30-31 October;


Gomis, R. (2001), ‘La generación de ventajas competitivas a partir de la adopción y la aplicación de las tecnologías de la información: el sector de la electrónica de la industria de maquiladora de exportación en Tijuana’, seminar on ‘Challenges and Perspectives of the Mexican maquiladoras: local settings and global processes’, organized by the University Center for Social Sciences and Humanities (CUCSH) and the College of the Northern Frontier (COLEF) in Guadalajara, Jalisco, 30-31 October;


Gonzalez, G. And M. Barrajas (2001), ‘Los procesos de aprendizaje en la industria electrónica maquiladora, ¿Una senda predefinida?’, seminar on ‘Challenges and Perspectives of the Mexican maquiladoras: local settings and global processes’, organized by the University Center for Social Sciences and Humanities (CUCSH) and the College of the Northern Frontier (COLEF) in Guadalajara, Jalisco, 30-31 October;


Hualde, A. and R. López Zámano (2001), "Instituciones y maquiladores en la frontera norte de México: dinámicas locales, desafíos globales", seminar on 'Challenges and Perspectives of the Mexican maquiladoras: local settings and global processes', organized by the University Center for Social Sciences and Humanities (CUCSH) and the College of the Northern Frontier (COLEF) in Guadalajara, Jalisco, 30-31 October;

Jaén Jimenez, B. And M. Leon Sánchez (2001), 'Escalamiento industrial de la industria electrónica de Jalisco en la década de los noventa: el papel de IBM', seminar on 'Challenges and Perspectives of the Mexican maquiladoras: local settings and global processes', organized by the University Center for Social Sciences and Humanities (CUCSH) and the College of the Northern Frontier (COLEF) in Guadalajara, Jalisco, 30-31 October;

Jenkins, R. (1977), Dependent Industrialization in Latin America: the automotive industry in Argentina, Chile and Mexico, Praeger, New York;


Keller, W and S. Yeaple (2002) "Multinational enterprises, international trade and productivity growth: firm level evidence from the United States", Economics Department, Brown University;


Lall, S. (2000), "Export performance, technological upgrading and FDI policies in the Asian NICs with special emphasis on Singapore", Serie Desarrollo Productivo, No. 88, Santiago, October;


Markusen, J. and A. Venables (1999), "Foreign direct investment as a catalyst for industrial development", European Economic Review, No. 43;

Moguillansky, G. and R. Bielschowsky (2001), Investment and Economic Reform in Latin America, ECLAC, Santiago;

Moguillansky, G. (1999), La inversión en Chile: ¿el fin de un ciclo de expansión?, Fondo de Cultura Económica / CEPAL;

__________ (1998a), "Corporate Strategies and Regional Integration Schemes Involving Developing Countries: the NAFTA and MERCOSUR automobile industries", Science, Technology and Development, (Volume 16, Number 2) University of Strathclyde, Glasgow, August;
__________ (1998b), "GETTING A LIFT: modernizing industry by way of Latin American integration schemes. The example of automobiles", Transnational Corporations (Geneva), Volume 7, Number 2, August;
__________ (1991), Transnational Banks and the International Debt Crisis, United Nations Center on Transnational Corporations, New York;
__________ and W. Peres (2001), “Corporate Competitiveness in Latin America and the Caribbean”, CEPAL Review, No. 74, Santiago, Chile, August;


Nakata, M. (2001), 'El futuro de la inversión japonesa en México', seminar on 'Challenges and Perspectives of the Mexican maquiladoras: local settings and global processes', organized by the University Center for Social Sciences and Humanities (CUCSH) and the College of the Northern Frontier (COLEF) in Guadalajara, Jalisco, 30-31 October;


_______ (2003b), “Patterns of interactions between foreign and domestic firms and technology spillovers; A comparison of three industries from Mexico”, Department of International Studies, ITAM;

Ruiz, J. (2001), “Transición escuela-trabajo: prácticas organizacionales, institucionales e individuales para la inserción de la fuerza de trabajo universitaria en la industria electrónica de Jalisco”, seminar on ‘Challenges and Perspectives of the Mexican maquiladoras: local settings and global processes’, organized by the University Center for Social Sciences and Humanities (CUCSH) and the College of the Northern Frontier (COLEF) in Guadalajara, Jalisco, 30-31 October;


Saggi, K. (2001), “Trade, foreign direct investment and international technology transfer: a survey”, Department of Economics, Southern Methodist University, Dallas, USA;


Sepulvida, B and A. Chumacero (1973), La inversión extranjera en México, Fondo de Cultura Económica, Mexico;


Sunkel, O. (1993), Development from Within: toward a neostructuralist approach for Latin America, Lynne Riener Publishers, Boulder, Colorado;


_______ et al. (1980), Transnacionalización y dependencia, Ed. Cultura Hispánica del Instituto de Cooperación Iberoamericana, Madrid;

Te Velde, D. (2002), “Foreign direct investment and income inequality in Latin America, Experience and policy implications”, mimeo, Overseas Development Institute, October;


United Nations Economic Commission for Latin America and the Caribbean (ECLAC) (1994), Open Regionalism in Latin America and the Caribbean: economic integration as a contribution to changing production patterns with social equity, Santiago;

_____ (1999), Foreign Investment in Latin America and the Caribbean, 1998, United Nations, Santiago;

_____ (2000), Foreign Investment in Latin America and the Caribbean, 1999, United Nations, Santiago;

_____ (2001), Foreign Investment in Latin America and the Caribbean, 2000, United Nations, Santiago;

_____ (2002), Foreign Investment in Latin America and the Caribbean, 2001, United Nations, Santiago;

_____ (2003), Foreign Investment in Latin America and the Caribbean, 2002, United Nations, Santiago;


Xu, B., and J. Wang (1999), “Multinational enterprises, technology diffusion and host country productivity growth”, mimeo;