Corporate Strategies for FDI in the Context of Latin America’s New Economic Model

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Summary. — The NEM in Latin America radically altered foreign direct investment inflows to the region. Previously restrictive national policies became ones that facilitated foreign direct investment (FDI) in the context of new business opportunities. Transnational corporations (TNCs) took a new look at the region in the context of their evolving corporate strategies, examples being efficiency-seeking corporate strategies in the automotive (Mexico) and the apparel industry (Caribbean Basin) and the market access strategy for services in the telecommunications and electrical energy industries (Brazil). Two interrelated problems arose: (a) TNC objectives were often attained but those linked to national development goals often were not, and (b) national policies did not channel FDI to priority development activities. © 2000 Elsevier Science Ltd. All rights reserved.

Key words — Latin America, foreign direct investment, automobile industry, apparel industry, privatization

1. INTRODUCTION

According to the NEM, foreign direct investment (FDI) in Latin America and the Caribbean was to assume a more predominant role with respect to the region’s growth and development. The statistics for FDI inflows suggest that it did. Figure 1 indicates that the volume of FDI inflows recently reached unprecedented levels. In 1997–98, the average annual inflow was approximately US$70 billion, whereas the average annual inflows previous to the 1990s never surpassed 10 billion and during 1991–95 reached only about 23 billion.

Such a rapid surge in FDI inflows made its presence felt in terms of certain economic indicators (Table 1). FDI inflows jumped from the equivalent of 1% to over 4% of Gross Domestic Product (GDP) between the 1980s and 1997. That impact was even more pronounced in the smaller countries of the region (Central America). In terms of Gross Fixed Capital Formation (GFKF), the indicator for the 1980s increased by a factor of more than 4 to 18.6% in 1997. Again, the situation was more pronounced in the smaller countries. Measured in this fashion, FDI is now playing a far more important role in the economic activities of the region.

Another interesting aspect of the new reality for FDI in Latin America is that after decades of losing ground to developing Asia—in terms of the proportion of the total FDI flow to developing countries that each region received—Latin America finally began to close the gap in the mid-1990s (Table 2). It is true that Latin America had received the lion’s share previous to the 1990s, when the volume of FDI inflows was extremely small in comparison to the 1990s. It was left behind, however, by developing Asia in the early 1990s, when inflows to developing countries became very significant (US$74.6 billion a year during 1991–95). In 1996–97, when FDI inflows to developing countries surpassed $138.6 billion a year, Latin America increased its share from 31% to 40%. While still behind developing Asia, it was rapidly closing the gap.

Making policy changes to attract much greater flows of FDI to Latin America and facilitating a much more central role for FDI in the region’s growth and development were important aspects of the implementation of the NEM in the region. The above indicators of the level and presence of FDI in the region suggest that this was the case. As shall become apparent, however, the burst of FDI in the 1990s has not generally achieved key host government goals related to converting FDI into a
significant new engine of growth and development. While the objectives of corporate strategies were for the most part met, the growth and development goals of the host countries were not. Corporate and country strategies did not seem to coincide.

This paper analyzes the new corporate strategies for FDI in Latin America. It is based on the best statistical information available on FDI in Latin America, that of the Information Center of the ECLAC Unit on Investment and Corporate Strategies, coupled with the results of an extensive research program on this subject carried out over the last decade. Generally, the research was based on formal questionnaires administered to representative samples of foreign firms in different countries of the region, especially those that had distinguished themselves in terms of improving their international competitiveness. This paper is organized in three sections. The first defines aspects of the new operating envi-

Table 1. Latin America: FDI/GDP and FDI/GFKF indicators, 1970–97 (%)a

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<tr>
<td>(1) FDI/GDP</td>
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<tr>
<td>LAIA countriesb</td>
<td>0.4</td>
<td>1.0</td>
<td>0.7</td>
<td>3.9</td>
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<tr>
<td>Central America countries</td>
<td>1.7</td>
<td>3.1</td>
<td>1.7</td>
<td>5.8</td>
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<tr>
<td>Latin American countriesc</td>
<td>0.1</td>
<td>1.0</td>
<td>0.9</td>
<td>4.2</td>
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<tr>
<td>(2) FDI/GFKF</td>
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<tr>
<td>LAIA countriesb</td>
<td>–</td>
<td>3.7</td>
<td>3.9</td>
<td>17.3</td>
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<tr>
<td>Central America countries</td>
<td>–</td>
<td>15.2</td>
<td>3.8</td>
<td>29.9</td>
</tr>
<tr>
<td>Latin American countriesc</td>
<td>–</td>
<td>4.0</td>
<td>3.8</td>
<td>18.6</td>
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</tbody>
</table>

a Source: ECLAC, Information Center of the Unit on Investment and Corporate Strategies, Division of Production, Productivity, and Management, on the basis of information from the International Monetary Fund (IMF) or the relevant country’s balance of payments.

b The 11 larger countries of the Latin American Integration Association.

c Excludes Caribbean countries.
environment, especially in terms of changes in the international market and the new national and subregional policies designed to adapt to them. The following section analyzes the responses of the transnational corporations to the new operating environment in Latin America and the Caribbean. The new strategy to use FDI to improve efficiency in the automobile and apparel industries is highlighted, on the one hand, as is that to use FDI to gain market access in services (electricity generation and telecommunications), on the other. The concluding section contains a critical evaluation of the results from the perspective of the interests of the host countries.

2. CHANGES IN THE OPERATING ENVIRONMENT

FDI inflows to Latin America have responded to changes in both the international setting, and in policies (national and subregional). The fact that a globalization process—understood as a long-term tendency toward a single universal market—is taking place and is altering the existing competitive situations in virtually all industries needs little explanation (Mortimore, 1992, 1993, 1995b,d; OECD, 1996). To comprehend this phenomenon in concrete terms, it is important to take into consideration aspects of specific international markets. This involves analyzing the structure of specific product markets, the characteristics of the principal competitors in those markets, the nature of technological change, and the effect of new international norms (GATT/WTO rules on trade, investment, intellectual property, etc.), among other factors. Clearly the globalization process intensifies competition. It does not do so, however, in the same way or at the same rate in all product markets (Mortimore, 1995a). For countries or regions not accustomed to fierce competition, as is clearly the case for Latin America and the Caribbean (Mortimore, 1996), the sudden exposure to it can be traumatic for all firms operating there, national and foreign alike. The severe challenges to the competitive situation in the international market of several representative industries will be examined in more detail below.

An example of the dramatic changes in national and subregional policy can be captured by the treatment of FDI, something that can be referred to as the Rip Van Winkle effect when comparing the situation in the 1970s with that of the 1990s. During the 1970s in Latin America the official attitude toward foreign investment was generally restrictive, as exemplified by the 1973 Mexican Law to regulate foreign investment and the 1969 Decision 24 of the Andean Group which established an Andean foreign investment code. The restrictive nature of these initiatives is captured in four aspects. In terms of the right of entry and establishment, foreign investors were required to seek previous authorization from national officials and were obliged to register their investments for balance of payments purposes (subsequent profit remittances or capital repatriation). Several notable sectoral restrictions were in place. In natural resources, the trend was to exert national control, usually in the form of state enterprises. In the petroleum sector, expropriation or the use of association contracts were increasingly common. In services, FDI was generally prohibited. In the manufacturing sector, a transition from foreign to mixed companies was promoted in general and specific reservations held in certain sectors (auto parts, petrochemicals, the Andean sectoral programs of industrial development, etc.). Restrictions on operations were common, such as performance requirements (obligatory levels of national content and exports, import compensation requirements, etc.), preferences for joint ventures and creating a favorable environment for national firms in their negotiations with foreign ones in order to obtain technology by way of licenses. Financial restrictions included limits on the repatriation of capital, profit remittances, and royalties, and the exclusion of foreign firms from access to the national financial market.

The situation with respect to national policy on foreign investment in the 1990s could hardly have been more different. Its aim was now to promote and give guarantees to FDI. At the national level, representative examples of this are the explosion of bilateral Investment Promotion and Guarantee Agreements in the region, and the sharp increase in activities of national foreign investment promotion agencies. At the international, regional, or subregional level, examples are the attempt by Latin American countries to gain access to the Multilateral Agreement on Investment of the OECD, the work of the Negotiating Group on Investment of the Free Trade Area of the Americas (FTAA) initiative, and the invest-
ment chapter incorporated into the North America Free Trade Area (NAFTA) integration initiative.

Thus, the new view on TNC entry and establishment incorporated universal access and automatic or liberal establishment, and this tended to become the norm for negotiations. The existing rules excluding or limiting FDI in specific sectors underwent a “stand still.” Incentives for FDI replaced restrictions on it. Existing performance requirements were rolled back in keeping with new international norms, and new rules for the protection of and guarantees for FDI generally replaced the previous limits on the operations of transnational corporations (TNCs). Foreign firms acquired direct access to local capital markets. Thus, national policy with regard to the treatment of FDI did a complete about-face between the 1970s and the 1990s for the purpose of converting transnational corporations into more active agents of growth.

3. THE RESPONSES OF TRANSNATIONAL CORPORATIONS

The NEM evident in Latin America and the Caribbean during the 1990s has affected the competitive situation of TNCs. For existing affiliates operating in the region, particularly in the manufacturing sector, the opening up of national economies of Latin America exposes them to increased competition from imports and FDI inflows from competitors. The deregulation and liberalization of government policy at a sectoral or company level changes their basic operating conditions. They are forced to react to the new competitive pressures by adapting their corporate strategies. For new entrants, the new operating conditions, combined with the privatization of state assets, provide opportunities to expand and consolidate their international systems of integrated production (ISIP), or to consolidate their market access in services. FDI has been a very important factor in the transformation of Latin American economies, but to comprehend fully that phenomenon one must go beyond the numbers to analyze the objectives of the investing TNCs.

Historically, FDI in Latin America had been concentrated in infrastructure (during the first part of the 20th century) and natural resources (until the 1970s). Much of that investment was later nationalized. During the period between the Great Depression and the Debt Crisis of the 1980s, much of the new FDI sought to gain market access in the context of the import-substituting industrialization process. This FDI, mainly from US corporations, was concentrated in the chemical, machinery and transportation equipment sectors. Local operations in the region tended to be of a stand-alone nature and were not generally integrated into the ISIP of the headquarters’ corporations.

The experience with debt crisis in the 1980s and the policy changes inherent to the NEM brought about a complete change of operating conditions in Latin America, and that is reflected in the new focal points of FDI in the 1990s. Table 3 provides a synoptic overview of the focal points of FDI inflows to Latin America and the Caribbean during the 1990s, viewed from the perspective of the corporate investment objectives. In essence, Dunning’s well-known scheme (Dunning, 1993) was applied to Latin America and the Caribbean using the database of the Information Center of ECLAC’s Unit on Investment and Corporate Strategies. The shortcomings of FDI statistics were compensated for in large part by generating complementary information. Such information included that related to FDI modalities (mergers and acquisitions, privatizations and new assets), changes in international competitiveness (the CAN computer software) and the extensive research program of specific new focal points (automotive, apparel, electronic, etc. industries) in specific countries. No single set of FDI information is capable of producing Table 3, rather it is the outcome of numerous sources of information combined with a significant research program based on company interviews.

TNCs looked for four principal benefits in the region during the 1990s. Moving from the simpler to the more complex, they are: increased access to natural resources; greater access to markets for manufactures; new access to markets for services; and improved efficiency of their international systems of integrated production. The new objectives in the NEM period are the search for efficiency and the entry to previously closed, or severely restricted, service activities in the local market. A short explanation of each focal point is followed by a more detailed analysis of the most important ones as applied to particular cases (ECLAC, 1998).

The interest in gaining increased access to natural resources mainly concerned new
entrants enticed by the liberalization and deregulation of the petroleum and mineral sectors. Often they took advantage of the opportunities made available by way of the sale of state assets, be that in the form of the privatization of state companies or the concession of petroleum or mineral rights. This was particularly pronounced in Venezuela, Colombia and Argentina with respect to petroleum and gas, and in Chile, Peru and Argentina with respect to minerals.

In Venezuela and Colombia, the concession of petroleum rights was central to FDI inflows. In 1995, the state petroleum company of Venezuela—PDVSA—established a 10-year investment program in the order of $65 billion. It was premised on the sale of concessions (Mobil, Dupont-Conoco, Enron, Amoco, Elf Aquitaine, British Petroleum, among others) and the establishment of joint ventures (ARCO, Phillips Petroleum and Texaco) with major transnational corporations operating in the petroleum industry. In the case of Colombia, as well as concessions it is of interest to note that three of the top foreign firms in the country, by sales, are petroleum companies (Mobil, Exxon, and Texaco).

In the case of Argentina, Repsol of Spain followed up on a $1 billion dollar series of purchases of local firms (EG3, Pluspetrol, Mexpetrol Argentina, Algas, etc.) in 1999 with the $15 billion purchase of YPF (ranked 13th in Latin America by sales in 1998). In other words, the FDI in the petroleum sector had several distinct dimensions. With respect to mining, the FDI during 1990–97 was primarily concentrated (about 80%) in new projects in Chile (Stallings and Peres, 1999). Subsidiaries of mining TNCs, such as Escondida, Minera El Abra, Disputada Las Condes, Candelaria, Mantos Blancos, Zaldivar, Quebrada Blanca, Mantos de Oro and El Indio, all figured in the 1997 list of the 30 biggest foreign firms in Chile. These petroleum and mining investments almost by definition resulted in strong export streams.

Those corporations seeking greater market access in manufactures tended for the most part to be ones that had existing operations in the Mercosur countries (mainly Brazil and Argen-

### Table 3. Focal points of FDI in Latin America and the Caribbean during the 1990s

<table>
<thead>
<tr>
<th>Sector/objective</th>
<th>Primary Manufacturing</th>
<th>Services</th>
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<tbody>
<tr>
<td>Natural resource seeking</td>
<td><strong>Petroleum and gas:</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Venezuela, Colombia,</td>
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<td></td>
<td>Argentina; <strong>Minerals:</strong></td>
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<tr>
<td></td>
<td>Chile, Argentina, Peru</td>
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<tr>
<td>Market access seeking: manufactures</td>
<td><strong>Automotive:</strong> Mercosur;</td>
<td></td>
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<td></td>
<td><strong>Chemicals:</strong> Brazil;</td>
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<td></td>
<td><strong>Agro-industry:</strong> Argentina, Brazil, Mexico</td>
<td></td>
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<tr>
<td>Market access seeking: services</td>
<td><strong>Financial services:</strong> Brazil, Mexico, Chile, Argentina;</td>
<td></td>
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<tr>
<td></td>
<td><strong>Telecommunications:</strong> Brazil, Argentina, Chile, Peru;</td>
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<td></td>
<td><strong>Electrical energy:</strong> Colombia, Brazil, Argentina, Central America;</td>
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<td></td>
<td><strong>Gas distribution:</strong> Argentina, Brazil, Chile, Colombia</td>
<td></td>
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<tr>
<td>Efficiency seeking</td>
<td><strong>Automotive:</strong> Mexico;</td>
<td></td>
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<tr>
<td></td>
<td><strong>Electronics:</strong> Mexico and Caribbean Basin;</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Apparel:</strong> Caribbean Basin and Mexico</td>
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</table>

*Source: For the typology of objectives see Dunning (1993), for its application to Latin America-ECLAC (1998).*
tina). These TNCs were adapting to the new competitive situation that derived from the opening of the national markets to increased import competition. Mergers and acquisitions (M&A) by companies operating in these mature oligopolies, such as chemicals, food products, beverages, and tobacco, were pronounced. Over 60% of the number of M&A in Latin America during 1990–98 and 52.2% of their total value corresponded to the cases of Brazil and Argentina. For example, Colgate Palmolive bought Kolynos (Brazil), Unilever acquired Kibon (Brazil), ICI bought Tintas Coral (Brazil) and Alba (Argentina), Nabisco purchased Modelo Terrabusi (Argentina) and Parmalat acquired Industria Alimenticia Batavia (Brazil). In other words, the sale of private assets in the competitive shake-out was evident. Exports generally did not play an important role in these activities, the focus of which was primarily to defend existing market shares.

One of the major concentrations of FDI in the mid- to late-1990s was founded on seeking new market access in services. Given that the service sector had previously been closed to FDI in most of the region, new entrants predominated. They often took advantage of the opportunities presented by the privatization of state companies (in telecommunications and energy distribution) or the sale of private sector assets through mergers and acquisitions (financial services, especially banks). This was most noticeable in Brazil. Many other countries of the region, however, were incorporated in this manner in the process of international expansion of certain TNCs.

During the early to mid-1990s, the most forceful expansion of TNCs in the region came in the form of FDI seeking to improve the efficiency of their ISIP by extending them to certain countries in Latin America. Sometimes this involved TNCs that already possessed foreign affiliates in the region; however, the aim usually was to restructure the existing operations to convert them into an export platform, as was the case for the automobile industry in Mexico. In other cases, new assets were created in the export processing zones, for example, to establish assembly operations for auto parts, electronics and apparel in Mexico and the Caribbean Basin.

It is noteworthy that there is little evidence of strategic asset seeking by TNCs in Latin America, especially in terms of research and investment to develop world class technologies. While this is an activity more common to TNC operations in the OECD countries, some evidence of this was apparent in developing Asia, especially in the electronics industry. In Latin America, the only activity of this nature had more to do with marketing, not technology development, and was not considered significant enough to merit a separate entry.

In what follows, we focus on what we consider to be the two most important objectives of FDI in the recent period. First, we analyze some of the most notable corporate strategies aimed at improving the efficiency of their ISIP by way of FDI (most notably in Mexico and the Caribbean Basin). Then we examine those focused on gaining market access for services by way of FDI (most evident in Brazil). These objectives are important for two reasons: the proportion of the total FDI inflows that they represent and, in the case of the efficiency seeking FDI, the very significant trade flows produced as a consequence. The analysis of the corporate strategies behind these new objectives is based on the results of an extensive research program that for the most part utilized company interviews and formal questionnaires to gather the relevant information.

(a) Using FDI to improve the efficiency of international systems of integrated production

One of the major examples of the impact of the NEM is found in a few sectors of certain countries and involves TNCs that attempt to gain efficiency by setting up new operations or restructuring their existing operations in Latin America. Two of the principal examples in Latin America are automobiles in Mexico and apparel in the Caribbean Basin. Though they share common elements—a challenge in the international market, a more accommodating national policy and new corporate strategies—they also have important differences, therefore it is better to treat them separately.

(i) Improving efficiency in the automobile industry of Latin America

The automobile industry in Latin America is where the biggest foreign firms by sales are found in the region. In 1998, seven of the 10 largest foreign corporations, by consolidated sales, operating in Latin America were auto TNCs (GM—Mexico, VW—Brazil, GM—Brazil, Chrysler—Mexico, VW—Mexico, Fiat—Brazil and Ford—Mexico). The automobile industry was a central focus of US and
European (but not Japanese) FDI in Latin America during the 1990s (Mortimore, 1998b; ECLAC, 1998, chapter 4). A brief examination of the intersection of the three mentioned groups of factors (international market, national policy and corporate strategies) will provide the information necessary to understand the new competitive situation of this industry and the role of FDI in the automobile industry of Mexico.

Mexico is the best example in Latin America of a country that has undergone a very significant structural transformation in the context of the globalization process (Mortimore, 1998c; Calderón, Mortimore & Peres, 1994, 1996). This is most evident in the automotive (Mortimore, 1995c), electronic (Carrillo, Mortimore & Alonso, 1998; Carrillo & Mortimore, 1998) and apparel sectors. The changes are most apparent in terms of the import market shares gained in major markets, such as the North American one, where Mexico's performance rivals and even exceeds most of developing Asia's (Mortimore, Bonifaz & Duarde de Oliveira, 1998). By far the most significant example is the automotive industry.

Since at least the 1970s the major Japanese automobile producers have been challenging the US and European auto TNCs that had dominated the industry (Mortimore, 1997). The competitive prowess of the Toyota system based on an integral “lean” production, flexible organization, defect prevention and just in time delivery of inputs produced major import inroads for Japanese producers in the US and European markets. The application of restrictive trade policies obliged the Japanese auto TNCs to set up local production facilities first in the United States and later in Europe. That represented the first phase of the expansion of the international systems of integrated production of Toyota and other Japanese auto TNCs. During 1987–91, the Japanese auto TNCs increased their market share in the United States to 25% (Datton, 1991). By 1989, the ranking of auto TNCs in terms of their competitiveness put Japanese auto TNCs operating in Japan in first place, Japanese auto TNCs operating in the United States in second place, US firms operating in the United States in third place and European firms in Europe in fourth place. This Japanese challenge in the global automobile market produced sharp reactions from competitors, especially the US ones that sought to compete better in the US market by seeking to establish more efficient production facilities in neighboring Mexico.

National policies in the United States and Mexico facilitated the new corporate strategies of US auto TNCs (Mortimore, 1998d). There were at least two elements involved: auto parts and vehicle assembly. The use of the US production-sharing mechanism (Harmonized Tariff System 9802) allowed US-based companies to export components for assembly while the imported final product was charged tax only on the value-added (mainly wages) outside of the United States. This benefit was combined with the Mexican maquila program that offers tax-free operations similar to export-processing zones. Taken together, this produced great cost reductions in the assembly of labor-intensive auto parts. With regard to vehicle assembly, the previously restrictive Mexican national automobile policy was refurbished to facilitate the implementation of new export-oriented plants in northern Mexico, close to the US border. For example, Mexican authorities permitted the assembly of “export models” that incorporated much higher levels of imported components (70% as compared to 40% for models sold in the national market). Finally, the North American Free Trade Agreement contained a special chapter that provided preferences for US auto TNCs in the integration of a continental automobile industry. The regional (United States, Canadian, Mexican) norms of origin (62.5% of production costs) in particular were influential in this respect. All this produced a burst of FDI in the Mexican automobile industry by auto TNCs as well as their parts suppliers beginning in the mid-1980s.

The corporate strategies behind the huge increase in FDI in the Mexican automobile industry reflected the reaction of the US Big Three auto TNCs (General Motors, Ford and Chrysler). The US Big Three sought to compete better in the North American market vis-à-vis the Japanese transplants by establishing what they considered to be world class vehicle assembling plants in Mexico. During 1990–96 the US Big Three invested over $5.5 billion in new plants in Mexico. This came on top of considerable FDI during the 1980s, when, for example, the famous Ford plant at Hermosillo was established (Carrillo, 1995). The structural transformation of the Mexican automobile industry during the 1990s with respect to its level of production, productivity, trade orientation and balance-of-payments effect can be
seen in Table 4. During the 1990s it became an emblem of Mexico’s new export orientation.

The central role of US auto TNCs in the transformation of the Mexican automobile industry is demonstrated in Table 5. By 1998, the Mexican automobile industry was producing almost one and one-half million vehicles, and the US Big Three were responsible not only for two-thirds of the production but, more importantly, for about 70% of the exports. Chrysler and Ford, in particular, exported over 84% of the vehicles that they produced in Mexico. They had established export platforms in Mexico to assist them in meeting the Japanese challenge in the North American market. This is reflected in the fact that Japan’s import market share for vehicles (SITC 781 and 782) in the North American market dropped from 41.5% in 1985 (38.9 in 1990, 31.7 in 1994) to 26.1% in 1996. Mexico’s share rose from 0.6% in 1985 (3.6 in 1990, 7.6 in 1994) to 11.6% in 1996. Furthermore, in terms of the structure of Japan’s overall exports to the North American market, vehicles fell from 30% of the total value in 1985 to 18% in 1996. In the case of Mexico, vehicles jumped from less than 2% of total value of exports to North America in 1985 to almost 15% in 1996. The FDI and trade links of auto TNCs operating in Mexico became one of Mexico’s principal means of integration into the international economy.

A brief comparison of the corporate strategy of the US auto TNCs in Mexico with that of the principal resident auto TNCs in the Mercosur market 7 serves to clarify certain important differences (Mortimore, 1998a,b). International market challenges and new national and subregional policy packages forced firms to react by way of new corporate strategies. Generally, firms chose one of the 3 “R”s: retire, rationalize or restructure. Some retired—that is, they sold their assets, licensed local firms or simply ceased to operate. Others rationalized their operations—that is, without making major new investments, they tried to maintain their market shares by reducing

<table>
<thead>
<tr>
<th>Vehicle assembler</th>
<th>Production</th>
<th>%</th>
<th>Exports</th>
<th>%</th>
<th>Exports/production (%)</th>
</tr>
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<tbody>
<tr>
<td>Chrysler</td>
<td>360.6</td>
<td>25.3</td>
<td>301.1</td>
<td>31.0</td>
<td>83.5</td>
</tr>
<tr>
<td>Ford</td>
<td>213.7</td>
<td>15.0</td>
<td>174.8</td>
<td>18.0</td>
<td>81.8</td>
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<tr>
<td>General Motors</td>
<td>314.2</td>
<td>22.0</td>
<td>198.8</td>
<td>20.5</td>
<td>63.3</td>
</tr>
<tr>
<td>(US Big Three)</td>
<td>888.5</td>
<td>62.2</td>
<td>674.7</td>
<td>69.4</td>
<td>75.9</td>
</tr>
<tr>
<td>All othersb</td>
<td>539.5</td>
<td>37.8</td>
<td>297.3</td>
<td>30.6</td>
<td>55.1</td>
</tr>
<tr>
<td>Total</td>
<td>1427.6</td>
<td>100</td>
<td>972.0</td>
<td>100</td>
<td>68.1</td>
</tr>
</tbody>
</table>

Table 5. Structure and export propensities of the Mexican automobile industry, 1998 (thousands of units and percentage)a

Source: Information from the Mexican Vehicle Manufacturers Association (AMIA).

b Mainly Volkswagen and Nissan.
operational costs through downsizing, streamlining, etc. Some restructured by making significant new investments to reorient the role of the existing plants within the new global strategy of the headquarter corporation, usually in terms of its international system of integrated production.

As we have seen, the affiliates of the US auto TNCs in Mexico chose the latter strategy. The response by Mercosur auto TNCs, however, was quite different. The principal auto TNCs operating in the countries that formed the Mercosur market (Fiat, VW, Ford, GM, Renault, and PSA) are mainly European. In fact, even the US assemblers' (Ford and GM) links are mainly to the European operations of their particular headquarter’s corporation. In the 1980s, in Brazil and Argentina most of these companies reacted by retiring (Renault and Fiat began to operate through local licensees in Argentina) or rationalizing production (Ford and VW merged their operations in Autolatina until 1995). Faced with the NEM in its Mercosur setting in the 1990s, most of these auto TNCs did attempt to restructure. The less competitive European (and US) auto TNCs announced substantial FDI to improve the competitiveness of their operations in Mercosur. They did it, however, in a defensive manner. Their goal was not to establish export platforms of importance to their international systems of integrated production. Rather, they were attempting to defend their existing Mercosur (especially, Brazilian) market shares in the face of increased import competition, in the context of the transition period toward the full implementation of the auto agreement within Mercosur (ECLAC, 1998, chapter 4; de Quadros Carvalho, 1997).

Compared to Mexico, the principal constituents of the Mercosur market (Brazil and Argentina) possessed neither the geographical proximity to a major market, the capacity to produce labor-intensive auto parts in export-processing zones, nor the same degree of liberalization or deregulation (no comparable “export” model facilities for assemblers). Moreover, they still had relatively high levels of import protection for vehicles (not parts) and high levels of obligatory subregional content (without compensating maquila auto parts inputs). The essence of corporate strategies in this context was to maintain market access in order to defend their presence in the context of the NEM. In sum, the impact on the local economy of the defensive FDI in Mercosur can be considered less positive than the efficiency-seeking FDI in the Mexican automobile industry from the perspective of exports, balance of payments, and, most notably, the quality of the vehicle produced. With regards to corporate strategies—though not necessarily national development priorities—the efficiency-seeking option in Mexico appeared to produce much better results than the market defense one in Mercosur.

(ii) Improving efficiency in the apparel industry of Latin America and the Caribbean

US apparel TNCs also sought to improve the efficiency of their operations in Latin America and the Caribbean in order to compete better in their own home market in the face of an Asian challenge (Gereffi, 1997). A small group of Asian producers had come to dominate North American imports of apparel, accounting for almost two-thirds in 1985. Table 6 indicates the dimension of that dominance and how Latin American countries, especially those of the

| Table 6. Import market shares for apparel in the North American market, 1985–96 (% of total imports) |
|---------------------------------------------------------------|------------|------------|------------|------------|
| Asian NICs | 66.4  | 61.4  | 47.4  | 45.4  |
| Caribbean Basin | 3.4  | 7.1  | 12.5  | 13.1  |
| Mexico | 1.6  | 2.6  | 6.7  | 7.6  |
| All others | 28.6  | 28.9  | 33.4  | 33.9  |
| Asian NICs | 69.4  | 43.3  | 23.4  | 21.3  |
| Caribbean Basin | 7.0  | 20.5  | 30.8  | 31.5  |
| Other Latin America | 4.0  | 5.5  | 15.0  | 15.8  |
| All others | 19.6  | 30.7  | 30.8  | 31.4  |

*a Source: Based on ECLAC’s CAN PLUS computer software on international competitiveness.*
Caribbean Basin, gained market share. This reflected the way that the Caribbean Basin apparel operations—both through the subsidiaries of US apparel TNCs and the contracting of national firms for apparel assembly—helped US apparel TNCs compete better in the North American market (Mortimore, 1999, Section IV). During 1985–96, the import market share of apparel (SITC 84) of the principal Asian exporting countries (Hong Kong, South Korea, Taiwan and China, among other newly industrializing countries—NICs) to the North American market saw their import market share fall from 66.4% to 45.4%. At the same time, Latin American exporters to that market (mainly Caribbean Basin countries and Mexico) sharply increased their import market shares for apparel (from 6.8% to 22.5%).

The apparel industry includes a host of trade and investment relationships between producers/assemblers and buyers, many of which are based on subcontracting arrangements as well as FDI. Given this complication and the number and diversity of the activities included in the apparel industry it is better to focus on a more defined segment, such as the knitted and crocheted underwear industry (SITC 846). It is in this segment that the role of subsidiaries is more pronounced. The operations of subsidiaries of the big US apparel TNCs (such as Sara Lee, Warnaco, Lovable, etc.) are predominant in this segment of the apparel industry, and change in Latin America’s exports has been most dramatic. In 1985, the North American imports of knitted and crocheted underwear came principally (69.4%) from the Asian NICs. But, by 1996, only a little more than one-fifth did so. Conversely, the North American imports of knitted and crocheted underwear from Latin America rose from about 11% in 1985 to over 47.3% in 1996. Caribbean Basin countries provided the lion’s share (31.5% in 1996) of those imports, with Mexico providing about 13%. Viewed in this manner, the Asian challenge to the US apparel industry had been defused largely by Caribbean Basin and Mexico suppliers.

National policies played an important role in this process. The dynamism of Latin American exports of apparel to the North American market came from three principal aspects of national or subregional policy associated with low wages, the use of export processing zones, and special access to the US market. The low wages came as a consequence of the devaluation of national currencies. This was initially related to the debt crisis of the 1980s, later to the particular case of the currency crisis of Mexico in 1994. These devaluations were large (usually on the order of 50%), and produced a severe reduction in local wage rates measured in terms of dollars. The sharp decline in wages made the use of export-processing zones in the Caribbean Basin much more attractive. These tax-free operations were originally intended to have a duration of a fixed period of time (around 10 years). They gradually became permanent, however, as a consequence of the escalating war of incentives among Caribbean countries trying to attract FDI (Mortimore and Peres, 1998a,b).

Finally, Caribbean Basin assemblers acquired a special access to the US market by way of HTS 9802 combined with the US Caribbean Basin Initiative, as did Mexican assemblers by way of HTS 9802, replaced in 1994 by the NAFTA benefits. The importance of this mechanism is shown in that over 1987–96, the share of US textile and apparel imports being funneled through HTS 9802 rose from 6% to 19%. Mexico (35%) and the Caribbean Basin countries (56%) accounted for over 90% of that use of the HTS 9802 mechanism (USITC, 1997). Mexico later improved its competitive situation vis-à-vis the Caribbean Basin countries by way of NAFTA’s norms of origin (coupled with the 1994 devaluation).

Again, as in the case of the automobile industry, it was not the entry of the hyperefficient Asian producers that produced the burst of Caribbean Basin and Mexican apparel exports to the North American market. Rather, it was the US manufacturers of knitted and crocheted underwear that adapted their corporate strategies to the new competitive situation in the international market and the opportunities available in the Caribbean Basin and Mexico by establishing subregional systems of assembly. In this manner they could supply the US market more efficiently than producing the final product in their US plants. Those US plants now produced the inputs ready to be assembled in the Caribbean Basin plants.

The more successful Caribbean Basin plants were usually wholly-owned subsidiaries in order to control the operation and maintain quality standards. Often the US apparel TNC set up assembly plants in several Caribbean Basin countries and Mexico in order to adapt more easily to the changing competitive situations of individual assembly sites. Thus, if local
exchange rates appreciated, or wage and social security costs increased substantially, or transportation or infrastructure problems arose in any particular site, the headquarter corporation could adapt by closing a local assembly line and adding another one in a more convenient location (Mortimore, 1999; Mortimore & Zamora, 1998; Mortimore, Duthoo & Guerrero, 1995; Vicens, Mortimore & Martinez, 1998). This gave optimum flexibility to the corporate strategies of the US apparel TNCs.

The analysis of the nature of the FDI in Latin America and the Caribbean by TNCs seeking to improve the efficiency of their ISIP throws light on one of the central aspects of the New Economic Model in the region. For many Caribbean Basin countries (Table 7), these operations became one of the principal elements of their incorporation into the international economy (the North American economy) by way of trade.

In the case of both autos in Mexico and apparel in the Caribbean Basin, the examination of the intersection of the competitive situation in the international market, new national and subregional policies, and the new corporate strategies of the principal foreign investors demonstrated that the new FDI was primarily from US TNCs reacting to distinct Asian challenges in their home market. It is not the most competitive Asian TNCs investing in the region to extend their ISIP but rather their US competitors trying to win back US or North American market shares. This has produced solid results for the TNCs but not so clearly for the host countries. From a host country developmental perspective, this FDI tends to result in export platforms which possess little contact with the host economy, thereby truncating or limiting the national industrialization process. The situation of Mexico, in this regard, is superior to the Caribbean Basin because of the level of technological sophistication of the industries involved and the more positive impact on local supplier networks due to the effect of the NAFTA norms of origin (Mortimore, 1998a, 1999; Gereffi & Bair, 1998; Sunkel & Mortimore, 1997). In this sense, there seems to be more of a coincidence of interests between the corporate strategies of many US apparel TNCs and some of the developmental preoccupations of Mexican policy-makers, unlike the situation in the rest of the Caribbean Basin (Mortimore, 1999, ECLAC, 1999, chapter 4).

(b) Using FDI to gain market access for services: the privatization of electricity generation and distribution, and of telecommunications

The largest share—more than one-half according to balance of payments information from national sources—of FDI inflows to Latin America during 1995–98 has been that attracted by the NEM through the liberalization and deregulation of services. While these inflows do not usually generate significant trade flows, as was the case for FDI from efficiency seeking TNCs in the manufacturing sector, the increased competition permitted by the new national regulations can strongly affect the systemic competitiveness of an economy. By far the most important case in the region during the last few years is that of Brazil.

During 1990–95, Brazil was not a very important recipient of FDI inflows. That changed during 1996–98, however, when it became the principal recipient in Latin America, displacing Mexico. Inflows jumped from about $11 billion in 1996 to over $31 billion in 1998. In the process, the role of FDI in the Brazilian economy was increased and transformed. During 1990–97, the share of foreign firms in the total sales of the 500 largest companies in Brazil rose from 31% to 36.3%. The stock of FDI in 1995 was mainly in manufacturing activities (55%), but by 1997 it had shifted to services (56.6%). TNCs seeking market access for services did so primarily by purchasing existing assets (not creating new ones), either by way of the privatization program in the electricity and telecommunications sectors or the private acquisition of banks and other financial institutions. Given that 28%

Table 7. Relative importance of apparel (SITC 84) and underwear (SITC 846) in total exports of main Caribbean Basin assemblers to North American Market, 1996 (%)

<table>
<thead>
<tr>
<th>Assembly site</th>
<th>% Apparel (SITC 84)</th>
<th>% Underwear (SITC 846)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Haiti</td>
<td>65.3</td>
<td>24.8</td>
</tr>
<tr>
<td>El Salvador</td>
<td>63.9</td>
<td>20.8</td>
</tr>
<tr>
<td>Honduras</td>
<td>63.7</td>
<td>25.4</td>
</tr>
<tr>
<td>Jamaica</td>
<td>50.6</td>
<td>35.7</td>
</tr>
<tr>
<td>Dominican Republic</td>
<td>49.6</td>
<td>13.0</td>
</tr>
<tr>
<td>Costa Rica</td>
<td>35.0</td>
<td>12.3</td>
</tr>
<tr>
<td>Caribbean Basin average</td>
<td>43.0</td>
<td>14.0</td>
</tr>
</tbody>
</table>

a Source: USITC.
of all FDI inflows to Brazil between 1991 and July 1998, entered through the privatization program, the discussion will be limited to that phenomenon. Again, the analysis of the intersection of a changing competitive situation in international markets, altered national policies, and new corporate strategies throws light on the subject matter.

While international market factors were not the principal motivation behind the FDI in services in Brazil, they were nonetheless very important secondary factors. The opening up of Brazil, and other Latin American countries previous to Brazil, provided opportunities for major players in other markets and newcomers within and without the region to position themselves in Latin America. The annexes of the General Agreement on Trade in Services (GATs) relating to telecommunications and financial services set a promising environment. Unlike the operations of TNCs in the manufacturing sector in which the consolidation of ISIP can provide very significant competitive advantages, the primary goal in the service sector is usually to gain access to the national market. In most services, integrated operations of an international nature are not a principal feature in the TNCs competitiveness. That being said, the telecommunications and electricity sectors are among the services in which integrated operations can provide advantages, especially in limiting the possibilities for expansion of competitors.

In the case of Brazil, the principal initiative for the hugely increased FDI inflows came as a result of major changes in national policy. In a general sense, it appeared that Brazil was breaking out of its chronic macroeconomic instability. In 1995, the Brazilian Constitution was modified to facilitate foreign investment in previously reserved sectors. The liberalization and deregulation of services in telecommunications, electricity, financial services, and retail commerce attracted huge inflows of FDI. In the case of telecommunications and electricity, this was principally via the privatization of public sector (federal or state) assets or the concession of public sector rights (such as cellular phones). Inflows of FDI of $27,164 million accounted for 41% of the total privatization program from 1991 through July 1998, while 59% came from Brazilian investors.

The telecommunications sector received $15,897 million of FDI from the sale of existing assets, mostly Telebras, and in the form of cellular phone concessions. Over 80% of the FDI received by way of these privatizations came from investors of only three countries: Spain (31.7%), Portugal (26.6%) and the United States (22.9%). The principal Spanish investor also purchased 77% of Cia. Riograndense de Telecomunicacões. Thus, the FDI was very much concentrated in a few operations and came from relatively few countries of origin.

The electricity sector received $9,493.9 million of FDI from the sale of electricity generating and distributing companies during 1996–98. As with telecommunications, privatization in the electricity sector was very concentrated in a few operations that had the participation of relatively few investing countries. Two of the privatized companies were among the largest foreign-owned companies in Brazil, by sales, in 1997. Most of the FDI was concentrated in only nine operations. Over one-half of the FDI received by way of these privatizations came from only one country, the United States (57.3%). Other important investing countries were Spain (17.8%), Chile (10.6%) and France (6%).

In terms of corporate strategies, a similar situation was found in both telecommunications and electricity where a single company dominated the FDI in the sector. The difference was that in telecommunications that firm was a relative newcomer, while in electricity it was a well-established one. In the telecommunications sector, Telefónica de España was most active in the Brazilian privatization process as well as others in Latin America. Telefónica had already established joint ventures in Chile, Peru, and Argentina, among others, and evidently was attracted by a Brazilian market possessing 17 million fixed lines (plus a waiting list in 1997 of 13 million more), four million cellular phones and 400,000 public telephones. For that reason, Telefónica took the lead in the privatization process, investing over $5 billion and accounting for almost one-third of the total FDI involved. The strategy of Telefónica was to achieve a critical mass in its international operations by operating in all aspects of the industry, and in the case of Latin America it foresaw foreign investments of about $19,825 million in joint ventures in markets with growth potential during 1998–2001 (Goldero Sánchez, 1998). Telefónica was pulling out all the stops to become a major player in Latin America and, presumably, the world.

At the other extreme, the US telephone giant, MCI, a world player in telecommunications, made significant investments in its core activi-
ties, long-distance telephone calls. It made a major investment of $2,273 million for the purchase of Embratel, a fixed line company with international operations. Earlier, it had set up Avantel during the privatization of Telmex in Mexico. Telefónica and MCI later entered into a strategic alliance for the creation of an integrated system of telecommunication among Latin America, North America and Europe.

In the electricity sector it was a US company that dominated the privatization process in Brazil. Founded less than 20 years ago, AES Corp. established a global system of 35 electricity generation and distribution operations with assets of over $8 billion in the United States, Europe and Asia before setting its sights on Latin America. During 1993–98 it invested $2,222 million in constructing or acquiring electricity generation and distribution facilities in Argentina. It also invested some $734 million doing the same in Puerto Rico, Mexico, Dominican Republic and El Salvador during 1997–98. But, its principal operations during that period were in Brazil, where it invested $3,222 million, 94% through the privatization program. Clearly, the principal interest of AES in Latin America was to assemble an integrated network in the Mercosur countries.

The opening up of Brazil to foreign investment in services thus provided the opportunity for relative newcomers to position themselves in the Brazilian market. While gaining access to the national market for services such as telecommunications and electricity was the principal strategic goal of the foreign investors, the possibility of assembling regional networks in these sectors was also a significant factor for the relatively few major investors. The central aspect of these services is to supply the local market and in that sense, this FDI did not have a direct impact on Brazil’s trade performance. The improvement of the provision of local services, however, does have a direct and significant impact on the systemic competitiveness of the host country.

Nevertheless, some concerns have been raised about the downside of this kind of FDI in Brazil. One has to do with its concentration of the sale of existing assets in the hands of few corporations, some of which seem to be extremely adventurous in their international expansion. Another is the apparent weakness of the national regulatory environment, and a third is the state’s financial dependence on the sale of its limited assets. Again, there seemed to be a certain discontinuity in the attainment of goals associated with corporate strategies and the lack of such in respect of national developmental goals.

4. CONCLUSION

The New Economic Model in Latin America has undoubtedly been a significant factor in changing transnational corporate strategies with respect to Latin America and the Caribbean. The dimension of those changes is manifest in the explosion of FDI directed at the region, rising from $14.2 billion a year during 1990–92 to about $70 billion a year during 1997–98. It was possible to make sense of the sheer mass of these FDI operations by organizing them according to the goals of the corresponding corporate objectives (efficiency-seeking, market access for services or manufactures, and seeking secure supplies of primary materials). It was then possible to analyze the most important examples according to the intersection of three sets of factors (the competitive situation in the international market, changes in national policy, and the nature of corporate strategies).

For US TNCs seeking to gain efficiency in their automobile or apparel assembly operations in Mexico and the Caribbean Basin, the explanation came in the intersection of different groups of factors, such as the Asian challenge in the US market, the new national and US policies to accommodate the new corporate strategies, and the specific competitive situations of individual corporate systems of integrated production. With regard to TNCs seeking access to the Brazilian market for services, the relevant factors had to do with the strategic positioning of firms made possible by the liberalization and deregulation of telecommunications and electricity generation and distribution, and the particular situations of corporations such as Telefónica de España and MCI, in telecommunications, and AES Corp. and Endesa/Enersis, in electricity.

This analysis permits some interesting insights into the new corporate strategies for FDI in the context of the new economic model in Latin America and the Caribbean. Latin America is attracting mainly the reactive FDI of second and third-rate TNCs seeking to improve the efficiency of their regional systems of integrated production, not the FDI of the first-rank international market conquerors. Moreover, the way that US TNCs successfully
organize their production to meet the different Asian challenges in their home market implies certain costs, as well as benefits, for the host countries of their FDI in the region. In the case of Mexico, the norms of origin of NAFTA are producing many positive results in both automobiles (Mortimore, 1998a,b) and apparel (Gereffi & Bair, 1998) because Mexican physical inputs now count as “NAFTA content” in the North American market. On the other hand, the organization of offshore assembly of apparel in the Caribbean Basin is a clear example of some of the costs involved, measured in terms of the national industrialization process (Mortimore, 1999). Local physical inputs do not count as “NAFTA content,” although parity has been sought for years in the US Congress, and they are taxed as value added outside of the US market upon entry. This naturally truncates the national industrialization process and produces a severe competitive challenge for national firms.

The analysis of the massive new FDI in services in Brazil also offers certain insights. A large proportion of the new inflows corresponds to the purchase of existing assets rather than the creation of new ones. This is not necessarily a problem, since the new owners usually invest significant resources into modernizing the facilities in order to make them more competitive, and this has a favorable impact on the systemic competitiveness of the host economy. But when the investment is highly concentrated in a small number of huge operations, when some of the principal new investors are adventurous newcomers (Telefónica de España, Telecom Portugal, Endesa/Enersis, etc.) that are possibly out of their depth, when the regulatory environment is weak and the state seems to depend financially on the sale of its limited assets, then caution is warranted. For example, whereas Telefónica’s investment strategy in Latin America was said to rest essentially on good telecommunications regulations combined with a strong macroeconomic stability in the host country, it jumped in with both feet in Brazil, a country that clearly did not seem to fulfill either requirement. Furthermore, from the FDI recipient perspective, how long can privatization programs sustain FDI inflows before the state runs out of attractive assets to sell?

All in all, several of the governments of Latin America and the Caribbean should be congratulated for reestablishing the region as a destination for significant inflows of FDI—a vast improvement over the situation during the lost decade of the 1980s. At the same time, it must be pointed out that there seems to be no direct or clear connection between the increased inflows of FDI and the growth of economic activities in those economies. In the rush to attract FDI, most governments of the region do not seem to have very clear long-term objectives, except a vague idea that somehow investment, especially foreign investment, produces growth, exports, employment, etc. Yet we have seen that there is often a down side for the host economies. For example, there was quite a difference between expectations and reality in the apparel industry in the Caribbean Basin. In the services sector of Brazil, most of the FDI inflows went to the purchase of existing assets undergoing privatization. Doubts could be raised about the concentration in those industries and the supervision of the modernization of those existing assets. Perhaps it is the moment to turn national policy from simply attracting FDI to defining the results expected for the national economy, so that national developmental objectives, as well as corporate ones, can be attained.

NOTES

1. A relatively large amount of statistical and other information on FDI is available. There is balance-of-payments information from international institutions, such as the International Monetary Fund, source countries, especially the OECD countries, recipient countries, such as their central banks. There is also information from other national institutions, such as those that promote FDI, and private sources, such as business associations, the specialized financial press, and company reports, among others. For reasons of coverage, definitions and methodologies, it is a very complicated task to make use of it. The Information Center of the Investment and Corporate Strategies Unit of UN-ECLAC undertakes the difficult task of trying to make sense of all this information. It does so by way of its research program and the results are evident in its two principal publications: the annual *Report on Foreign Investment in Latin America and the Caribbean* and the intermittent *Directory on FDI in Latin America and the Caribbean*. 
2. It might be recalled that this nursery tale character fell asleep for years and awoke to a radically changed world that he could not understand. It is suggested that the policy changes in Latin America and the Caribbean with respect to FDI are of that dramatic nature.

3. The Competitive Analysis of Nations (CANs) computer software measures the revealed comparative advantages of 89 countries over 1980–96 in five major import markets (OECD, North America, Europe, Japan and Latin America) at three and four digits of the SITC Rev. 2.


5. The NAFTA norms of origin also obliged non-US auto TNCs, such as Volkswagen and Nissan to make significant investments in local suppliers so as not to be locked out of the NAFTA market (chapter 4 of ECLAC, 1998).

6. All import market shares were calculated using ECLAC’s CAN PLUS program on international competitiveness.

7. The founding members of MERCOSUR were Argentina, Brazil, Paraguay and Uruguay.

8. Mainly in Brazil ($11,250 millions as of 1995) and Argentina ($3,796 millions as of 1996), on top of that invested in the early 1990s.

9. The following discussion is based on ECLAC (1998), chapter 2.

10. The companies in which Telefónica had invested were the largest foreign companies by sales in Argentina ($2,994 million) and Peru ($1,426 million) and the fourth largest in Chile ($1,437) in 1997.

11. A competitor with similar goals was the association formed by Endesa (Spain) and Enersis (Chile). While clearly not possessing an international network of the stature of AES Corp., this association was very active in establishing a Latin American network, mainly in the Southern Cone countries but also in Colombia, Peru, Venezuela and the Dominican Republic.

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