Foreign Investment in Latin America Rises

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Figures for 2004 show that the long-term decline in foreign direct investment (FDI) into Latin American countries has turned around for the first time since 1999. The Economic Commission for Latin America and the Caribbean (ECLAC), a regional UN agency based in Santiago, Chile, found that the turnaround could portend a surge in sustained investment.

While economic analysts generally welcomed the FDI increase, the figures are still lower relative to other regions and heavily dependent on export commodities, which have the potential for volatility. The figure is also 20% lower than the 1999 figure for the region.

Meanwhile, regional poverty has dropped by a single percentage point, lagging far behind the hopes of millions and rendering the best regional economic growth in seven years worthless for many. A 44% increase to US$54 billion in 2004 Foreign capital inflows topped US$ 54 billion in 2004, far exceeding the US$37 billion registered in 2003 and representing a 44% increase. This contrasted sharply with the 2003 19% decrease in FDI, which represented the fourth consecutive annual decrease (see NotiSur, 2004-06-04).

Much of the increase of foreign investments in Latin America was because of the expansion of the world economy, which led US and European companies to increase production in developing countries. Overall, foreign investment in developing countries grew by 79% last year. ECLAC officials said they welcomed the change in capital inflows, claiming it could mean the beginning of a new sustained investment boom. But ECLAC stated that it does not mean that the Latin American and Caribbean countries have "solved their problems with regard to the limited benefits they receive from the presence of transnational corporations (TNCs) within their borders."

The Santiago-based organization also stated that FDI is set to continue rising in the region, where the number of leftist governments has increased a fact that does not seem to faze investors, according to the agency's executive secretary, Jose Luis Machinea.

ECLAC's annual report on capital flows in the region warns of "evident weaknesses in competing for newer, higher-quality investments." Machinea said at a March 15 presentation of the report in Santiago that China poses a threat as a competitor to Mexico and Central American countries that are keen on drawing investment in technology, but it is also an opportunity for South American nations that depend on exports of basic commodities. Chinese demand for soy, for example, has radically transformed the agriculture industry in Argentina and Brazil (see NotiSur, 2004-02-27, 2003-10-03).

Rise of the "Translatinhas"
Privatizations are no longer the main attraction in the region for foreign investors, who are now purchasing assets from the private sector, say ECLAC researchers. At the same time, the presence of transnational corporations has diminished, giving way to companies known as translatinas - local firms, especially based in Mexico and Brazil, that have also set up shop in a number of other countries in the region. These include Petrobras, Telmex, America Movil, Cemex, Companhia Vale do Rio Doce, Femsa, Odebrecht, and Carso Group.

Much of the foreign investment in Latin America last year did not come from outside the region but from the translatinas. They often buy struggling companies in the absence of higher bidders from the US or Europe. The report looked closely at the energy crisis in the Southern Cone (see NotiSur, 2004-04-30), suggesting a "subregional approach" to developing the energy sector and attracting FDI from new stakeholders like petroleum companies. The energy sector went to market for investments in the boom of the 1990s, but the investment "failed to redress existing capacity shortages and the industry went into crisis."

**Weaknesses evident**

"In general," said the ECLAC report, "existing FDI inflows are not of the quality that is required. If the region's countries are to increase the benefits they reap from the presence of TNCs, the national policies and institutions they have put in place to deal with international commitments regarding investment, establish incentives to attract FDI and evaluate the results of FDI policies will need to be improved."

Compared to the rest of the world, the region's percentage of foreign capital inflows has fallen steadily in recent years, reflecting "evident weaknesses in competing for newer, higher-quality investments" like high-tech manufacturing, research and development centers, and new services such as those related to shared back-office activities, software, and regional headquarters. The countries with the greatest increase in foreign capital were Brazil (79%) and Chile (73%). Brazil was the largest recipient with over US$18 billion, followed by Mexico with almost US$17 billion.

Argentina rose over the previous two years. Trinidad and Tobago, El Salvador, and Colombia also saw FDI rise, while Panama and Venezuela experienced a downturn. The US remained the region's largest investor (32% of flows), given the decline in European investment, especially from Spain. Asian investment remained low.

In line with trends worldwide, between 2002 and 2003 the service sector received most FDI (51%), although these were mostly traditional services and not those with a higher technological content, which ECLAC says is preferable. Manufacturing (36%) came next, followed by the primary sector (13%).

China has emerged as a serious rival for FDI flows for some of the region's countries. For Mexico and the Caribbean, the Asian country represents major competition for efficiency-seeking investment. In contrast, for South America, China offers opportunities as a destination for its natural-resource exports. ECLAC studies find that FDI does not automatically offer benefits to receiving countries and that these vary depending on the strategies applied by transnational
firms (search for natural resources, local markets, efficiency in conquering third markets, and technological assets). The body therefore recommends that receiving countries more clearly define what they expect from FDI, and assign it a role within the framework of their national strategies for developing production.

Unlike Europe and Asia, Latin America and the Caribbean still have few efficient institutions that evaluate the policy in this area to determine whether it achieved the desired effects. Many nations saw rising economic growth in the past year, with Argentina registering a 9.1% growth rate and Chile seeing 6.1% growth, its highest since 1997.

Chile's Banco Central reported that per capita GDP had gone up 9.5% to US$5,900 per person. Chilean sectors that led the economic growth were fishing at 21.3%, agriculture and forestry up 7%, and industry with 6.9%. The region's GDP grew by 5% last year and is projected to grow by more than 4% this year. Exports have grown by an average of 10% over the past five years, and inflation is under control in most places. These are "very positive signs," although the region cannot forego making badly needed economic reforms to keep growing in the future, Machinea claimed.

China, East Asia, and Eastern Europe are widening their lead in the world race for foreign investments. While Latin America drew more than 50% of the world's investments in developing countries in the 1970s, it now attracts only 22%. More than 60% of the foreign investment in the region goes to utilities and about 30% to manufacturing plants. "There is a clear limitation in the regional capacity to compete for better quality investments, including those for the production of advanced technology, research and developing centers," which generate much higher-paying jobs, the report says.

Poverty shows very slight decrease

Another troubling point that reduces optimism regarding increasing FDI and waxing GDP is the minimal decline in poverty and extreme poverty. An ECLAC report released three months prior to the FDI analysis showed that regional poverty had dropped a mere percentage point. Economic inequality in Latin America is the world's most pronounced, and the trickle down of steady economic growth has indeed been only a trickle.

John Williamson of the Institute for International Economics (IIE) said that if ECLAC projections were correct, "it suggests that income distribution is still worsening. This is profoundly depressing." Williamson suggested countries adopt packages of more progressive taxation and public expenditure, along with closing loopholes that shortchange tax-revenue collection. Even with the highest economic growth in the region since 1997, the agency foresaw a 1% decrease in poverty relative to 2003 numbers. That meant an estimated 2 million would leave ECLAC's definition of poverty behind, while 224 million would remain poor and 98 million people would be indigent, or extremely poor.

Percent of populations living in extreme poverty (according to ECLAC):

Honduras 53.8
Nicaragua 42.4 * Bolivia 37.0
Paraguay 33.3
Guatemala 32.3
Colombia 25.2
Ecuador 24.0
El Salvador 22.9
Venezuela 22.7
Peru 21.7
Argentina 21.0
Panama 16.0
Brazil 14.2
Mexico 13.1
Costa Rica 7.5
Chile 4.3
Uruguay 3.0

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