L. Willmore (1973) "Direct Foreign Investment and Industrial Entrepreneurship in Central America", ch. 18 of Latin American Prospects for the Seventies, edited by D. Pollock and A. Ritter, Praeger, New York.

CHAPTER 18

DIRECT FOREIGN INVESTMENT AND INDUSTRIAL ENTREPRENEURSHIP IN CENTRAL AMERICA

L. N. Willmore

It is now generally recognized that direct foreign investment is more than a financial transaction, for the foreign investor provides entrepreneurial services in the form of modern technology, management, and the ability to successfully market a product. Indeed, the international corporation prides itself on supplying these services, and it is the components other than plant and equipment which justify the high rate of return for equity investments compared with investments in the form of bonds.[1] But the introduction of these entrepreneurial inputs into a developing economy can have a negative impact on human resources, even though the investment itself adds to the productive capacity of the region. By supplying management and technology and by refusing to sell shares in the local operation, the international investor may well retard the development of local institutions that could perform these functions. In the words of Felipe Pazos, "the main weakness of direct investment as a development agent is a consequence of the complete character of its contribution."[2]

The Central American Common Market (CACM), which includes Guatemala, El Salvador, Honduras, Nicaragua, and Costa Rica, provides an excellent opportunity to study the simultaneous emergence of native entrepreneurs and subsidiaries of international corporations in the manufacturing sector of a developing economy. Factories began to replace artisan methods of production during the 1940s, when the governments of the region adopted protective tariffs and offered industrial incentives to encourage import-substitution. The removal of artificial barriers to trade between the five countries, which began in the late 1950s and was completed for the manufacturing sector by 1965, has stimulated the domestic production of manufactures and has attracted a considerable amount of direct investment from abroad.

The emerging Central American industrialist feels threatened by competition from the subsidiaries of foreign corporations, and for this reason has appealed for measures to restrict direct foreign investment in existing industries. The purpose of this chapter is to examine the merits of this appeal and the overall impact of direct foreign investment on industrial entrepreneurship in the region. In particular, the study considers the change in the pattern of foreign investment which resulted from import-substitution and economic integration, the reaction of the local industrialist to this changed pattern of investment, and the policy measures which have been implemented in the CACM as a result.

Before he proceeds, the reader is asked to bear two points in mind. First, following A. H. Cole,[3] the function of entrepreneurship can be viewed as innovation, management, and adjustment to external conditions. But management alone, however essential it may be for the success of a business enterprise, is not synonymous with entrepreneurship. For the purposes of this chapter a "manager" is assumed to function as an entrepreneur only to the extent that he is given the authority—the decision-making power—to innovate and adjust to changes in the business environment. Second, there has been little research in Central American industries at the level of the firm, so many of the points in this chapter that relate to the structure of Central American enterprises must be regarded as tentative hypotheses which may be confirmed (or rejected) by subsequent empirical investigation.

THE PATTERN OF FOREIGN INVESTMENT

Direct foreign investments have a long history in Central America. In 1897 the book value of equity investments held by foreigners was calculated at about $12 million and was concentrated in the banana-growing countries of Costa Rica, Guatemala, and Honduras.[4] In recent years foreign investments have penetrated all five countries, and in a way far different from that of the "Banana Republic" type of investment.

Since the Central American countries record capital flows but not direct foreign investment in the region, a study of the pattern of foreign investment must be restricted to direct investments of U.S. firms. The task of compiling statistical evidence is made more difficult because prior to 1968 the U.S. data treated Central America not as a unit but rather as a balancing entry ("other Central American and West Indies") following Mexico and Panama.

Nonetheless, from the data published periodically by the U.S. Department of Commerce it can be estimated that the book value of U.S. investments in manufacturing increased sixfold from the time the General Treaty establishing the CACM was signed (December 1960) to the end of 1968. U.S. investments in agriculture and services

have remained largely unchanged over the same period. The increased investment in "other" activities (mostly the export sector of agriculture) shown in Table 18.1 is most likely due to the purchase of sugar plantations in the Dominican Republic following the 1965 intervention, for there is no evidence that U.S. fruit companies have increased their holdings in Central America.

Japanese, German, and Mexican companies have established manufacturing plants in Central America,[5] but the United States still accounts for most of the direct foreign investment in the region. As U.S. enterprises operating public services are nationalized,[6] other companies, including United Fruit and W. R. Grace, are diversifying and investing an increasing amount in the manufacturing sector of the economy. Firms that formerly exported their products to Central America have opened plants in the region to cross the tariff barrier and retain their share of the local market.[7] The available evidence seems to support the observation made frequently in the press that the formation of the CACM has encouraged large international companies to produce consumer goods in the region, in competition with smaller Central American enterprises.* Central America thus appears to have entered a "new stage of foreign intervention"[9] which is very different from that which the region experienced in the past.

THE INTERNATIONAL FIRM AND NATIONAL ENTREPRENEURSHIP

By encouraging import substitution in the postwar period the Central American governments have fostered the emergence of a new type of entrepreneur, one who manufactures commodities for the domestic market. At the same time, foreign investment has been diverted from the export and service sectors and toward the manufacturing sector of the economy. Economic integration has accelerated this process by making production for a regional market more

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*A Guatemalan columnist, expressing a point of view which is frequently encountered in the Central American press, suggests that "the common market is nothing more than an expansion of the productive zones of the United States of America—and to a lesser extent of Japan, Germany and other countries which have incorporated some of their industries in the integration plans. And to our greater dismay, there have even been cases of prosperous industries, built by Central American entrepreneurs, which have been sold to wealthy foreign companies."[8]

TABLE 18.1

Book Value of U.S. Direct Investment in Central America and West Indies,* 1960, 1964, and 1968 (millions of U.S. dollars)

	Total	Mining and Smelting	Petroleum	Manu-fact-ures	Utili-ties	Trade	Other
1960	464	20	71	19	132	18	204
1964	589	31	139	46	142	26	205
1968	725	33	198	121	147	45	251

*Exclusive of Cuba, Panama, and Caribbean dependencies.

Note: The five Central American countries account for approximately three-fourths of the total values shown.

Source: U.S. Department of Commerce, Survey of Current Business, various issues.

TABLE 18.2

Book Value of U.S. Direct Investment in the Central American Common Market, 1968, 1969, and 1970 (millions of U.S. dollars)

	Total	Mining and Smelting	Petroleum	Manufactures	Other
1968	596	6	151	104	335
1969	630	8	154	113	335
1970*	624	10	160	73	381

*Preliminary.

Source: U.S. Department of Commerce, Survey of Current Business, various issues.

attractive to both the Central American industrialist and the large international firm. As a result of policies that protect local industry but not the local industrialist, foreign capital is increasingly competitive with local capital and a conflict has developed between the Central American industrialist and his foreign counterpart.

The Central American industrialist typically employs his local manufacturers' association as a pressure group to oppose what he considers to be "unfair" competition from abroad. A case in Honduras provides an excellent example of this type of activity. In May 1968 the Honduras Association of Timber Producers published an open letter to President Oswaldo Lopez Arelleno in which they expressed their opposition to the establishment of a large pulp and paper mill. The proposed company, Industria Papelera Centroamericana, was to be a "joint venture" with International Paper (a U.S. firm) controlling 51 percent of the stock and Standard Fruit and United Fruit an additional 15 percent each. The remaining minority shares were to be purchased by the Central American Bank of Economic Integration (BCIE), the government-owned National Development Bank, and the Luxemburg-based Adela Investment Company. The local producers argued that the proposed ten-year tax exemption and the creation of unemployment in existing mills would outweigh any benefits which might accrue to the Honduran economy.[10] In this instance the government was more interested in increasing exports to the rest of Central America than in protecting the national entrepreneurs, so the company was granted a charter as planned in February 1969.[11] Were it not for the fact that Honduras has a serious balance of payments problem, the local producers might have been more successful in influencing governmental policy.

Thus far, the industrialist has had more effect on foreign investment policy at the regional level than he has at the national level. In an important public statement published in March 1965 the Central American Federation of Chambers of Industry (FECAICA) proposed that a total of eight restrictions be imposed on foreign direct investment in the region. The most important of these proposals were: (1) certain areas of the economy should be reserved exclusively for Central American investment, (2) "joint ventures" of domestic and foreign capital should be encouraged, (3) foreign firms should employ Central American administrators and managers, (4) no fiscal incentives should be granted to foreign investors who "threaten the stability of established firms," and (5) regional and state financial institutions should give preference to Central American investors, since "foreign investors are in a better position to provide their own financing."[12]

The FECAICA declaration was apparently quite effective, for less than three months later the ministers of economics of the five

CACM countries issued a policy statement that echoed the FECAICA proposals. In their joint declaration, the ministers urged that local resources be developed whenever possible, that joint industrial ventures be encouraged when a high level of technology requires foreign participation, and that in all other cases priority be given to Central American investors.[13] This declaration is not, however, binding on the individual governments, as is evident from the case of the pulp and paper mill in Honduras.

The industrialist pressure groups are, of course, motivated by self-interest and self-preservation. A governmental or regional developmental agency that is interested in the long-run development of human resources must consider the net impact of foreign direct investment on the formation of national entrepreneurs. And foreign direct investment does have a stimulating as well as a stifling effect on the development of entrepreneurship.

Direct investment from abroad can strengthen local entrepreneurship in three distinct ways. First, the manufacture of final demand goods creates opportunities for local entrepreneurs through the effects of what Hirschman calls "backward linkages," i.e., the purchase of intermediate goods in the domestic economy. Second, international firms train national managers who may become independent entrepreneurs in the future. Third, local industrialists become more efficient as a result of competition with and imitation of foreign-owned enterprises. The relevant question is then to what extent do these positive stimuli offset the negative impact of foreign direct investment on the development of industrial entrepreneurs in Central America.

At the present stage of industrial development in Central America, the industrialist has not become a supplier to the subsidiaries of international firms and, with the exception of plants that process agricultural products, backward linkages have not formed as a result of the establishment of new factories in the region. The present pattern of industrialization has resulted in a proliferation of plants that do little more than assemble imported component parts, plants that—to paraphrase a Guatemalan economist—package imported commodities in imported containers and add the label "Producto Centroamericano."[14] Costa Rica, for example, has four automobile assembly plants that import all component parts and a number of television and radio assembly plants that operate under similar conditions.[15] In Nicaragua, to cite another example, the chemical, cosmetics, and soap industries are composed primarily of plants that handle the final blending and bottling of imported products. These industries import 86 percent of their inputs from abroad, with the result that the value added by Nicaraguan blending, packaging, and distribution amounts to only 36 percent of the final retail price.[16]

The proponents of this indiscriminate type of industrialization argue that backward linkages will form in time. This may be true for some industries, but there is always a natural resistance on the part of the manufacturer of the final product to allow these linkages to form. If the manufacturer is an international firm, the only reason for establishing an assembly plant in Central America may be to escape the high duties on final consumer goods by exporting parts rather than the finished products. In other words, the parent company may continue to regard the small Central American economy as an export market, even though it has a "manufacturing" subsidiary in the region. In addition, the manufacturer may regard a domestically produced input as an inferior and more costly substitute for the imported good.

Albert Hirschman has suggested that this resistance to backward linkages is not a serious problem when one considers that the manufacturers of final demand goods can expand vertically and thus become their own suppliers.

> The resistance is almost wholly premised on the supposition that manufacturing in the higher stages of production is going to be undertaken by entrepreneurs <u>other</u> than the already established industrialists (or other than members of his immediate family). For if he himself undertakes it, most of the listed objections to the expansion of manufacturing via backward linkage fall to the ground. Thus, the fear of unreliability and poor quality of the domestic article should abate and the fear of domination by a monopoly supplier will disappear entirely.[17]

But what happens when the manufacturer is an international corporation? On the one hand, the corporation is predisposed to supply its Central American subsidiary with inputs produced by the parent company or a low-cost producer abroad.[18] On the other hand, if the host country stimulates the formation of backward linkages by collecting a higher duty on imported inputs, the subsidiary will expand through vertical integration rather than purchase intermediate goods from local entrepreneurs. In either event, the prospect of promoting national entrepreneurship through the effects of backward linkages is not very promising.

A second way in which a subsidiary of an international firm can increase the supply of local entrepreneurs is by training managerial personnel. In the case of Central America this impact is likely to be insignificant for two reasons. First, in many cases the parent company has simply substituted the export of component parts for the export of assembled units, with the result that the scope for innovation within the subsidiary operation is probably quite limited.* Second, even if a local employee should learn the requisite skills for successful entrepreneurship, he will find it difficult to obtain financial support for an industrial venture, given the present state of the Central American capital market. The prospective entrepreneur may seek employment in a firm that allows him greater scope for his entrepreneurial talents, but this solution presupposes that such enterprises exist in the region.

For a complete picture of the development of human resources in industry, one must bear in mind that the native manufacturer is no more willing to entrust his employees with decision-making power than is his foreign rival. With few exceptions, the Central American firm is a family affair, and outsiders generally are not permitted to participate in decision making at any level. Thomas Cochran reports that in the case of the Puerto Rican firm, the owner-manager was very reluctant to delegate authority or provide information to non-relatives.

> The fear of delegating authority helped to prevent the rise of a middle management group. Managers could not be found by advertising in the newspapers or consulting an agency. Sales managers or chief accountants had to be trained from the ranks, and unless they were relatives, the senior partner was unlikely to consult them on policy.[20]

This situation persisted in Puerto Rico in the mid-1950s, and in my opinion is characteristic of most Central American firms today.[21] The existing firms in Central America are probably not making a significant contribution to the formation of entrepreneurs, and the introduction of the international corporation into this environment is not likely to alter the picture from the standpoint of human resource development.

The third way in which direct foreign investment can stimulate local entrepreneurship is by forcing existing firms to improve the efficiency of their operations as a result of competition and demonstration effects. There is no doubt that foreign direct investment has, in

*This point—like many others in this chapter—is a tentative judgment subject to empirical investigation. But Litvak and Maule, in their study of U.S. subsidiaries in Canada, have concluded that "potential Canadian creativity is often not encouraged and in fact may be obstructed." A priori one would assume that the delegated authority to local personnel in an underdeveloped and small economy like Central America would allow even less scope for individual initiative.[19]

this sense, had an effect on the Central American industrialist. As Paul Rosenstein-Rodan has noted, "the stimulating effect is undoubtedly strong, perhaps so strong that the problem is that the patient should not be weakened (or killed) by overstimulation."[22]

The Central American industrialist has been unable to respond quickly to the stimulus of competition with the international firm, and many of his difficulties stem from the formation of the common market itself. The program of economic integration, which has given considerable impetus to Central American industrialization, is paradoxically contributing to the decline of the Central American industrialist. The industrial entrepreneur, who was accustomed to produce for the market of his own country, suddenly found himself operating in a larger regional market in the mid-1960s. Although the industries of each country were able to survive the competition of intraregional imports,[23] the industrialist has not been as successful in meeting the competition of the international enterprise.

The local entrepreneur needs time to adapt his finances, production, and marketing to the changed business environment.[24] Regional marketing requires an expanded sales organization and promotional advertising on a scale to which the national enterprise is usually not accustomed. The industrialist may also find it necessary to adapt his product line, alter his production techniques by purchasing modern equipment, or, at the very least, increase his inventory to meet the needs of a larger and more geographically dispersed market. Credit is generally available for additions to fixed plant and equipment, although the local entrepreneur may lack the technological information required for efficiency in planning capital expenditures. The major financial problem is the need for working capital to finance an enlarged inventory and sales promotion, and the small firm has little hope of obtaining credit for such purposes.

The international firm has an advantage over the local industrialist in marketing, technology, and finance. The parent company has exported its products to all five countries in the past, so it has a marketing and sales organization that encompasses the entire region. The international firm is not only aware of but is most likely an innovator with respect to technology. And financially, the international enterprise can more easily incur the expenses of initiating regional production and marketing, for it has access to both the retained earnings of the parent company and the international money market.

In short, a program of protection and encouragement of national entrepreneurship is not without merit from the standpoint of human resource development in Central America. Throughout the postwar period the five countries have made every effort to protect their "infant" industries and stimulate the process of industrialization. They are now beginning to implement measures to protect their "infant" industrialists and encourage the development of national entrepreneurship.

REGIONAL INDUSTRIAL POLICY

Although Central America does not yet have a comprehensive program of "infant" industrialist protection, the five countries have utilized the common market framework to institute a number of policy measures in favor of national entrepreneurship. These measures fall roughly into two categories: positive attempts to improve the competitive position of the local industrialist, and attempts to restrict the activity of the international firm so as to favor domestic over foreign investment.

The positive measures to improve local entrepreneurship are directed at marketing, technology, and finance—three respects in which the international firm has a distinct advantage over the local industrialist. Three new regional institutions have been created to deal with these problems. The Central American Institute of Business Administration (INCAE), which was founded under the auspices of Harvard University, is training potential independent entrepreneurs and increasing the pool of management personnel that is available to local firms. In addition, the universities in the region have added courses in business organization, marketing, and finance to the traditional accounting courses in the commerce curriculum. The Central American Institute of Research and Industrial Technology (ICAITI) provides technical advice and carries out feasibility studies for private enterprise in all five countries. This institute has no doubt improved the efficiency of existing enterprises and it provides useful information to those entrepreneurs who consider investing in a new industry. The Central American Bank for Economic Integration (BCIE) has improved somewhat the availability of credit to the industrialist. But the bulk of the funds of the bank have been received as a part of the foreign aid programs of the industrial countries, and these funds are often tied to the exports of the country that has extended the credit to Central America. Thus bank credit is restricted largely to expenditures on capital goods and does not aid the businessman who seeks to increase his inventory and extend his marketing operations.

The inability of the Central American industrialist to finance his expansion into a regional market undoubtedly accounts for much of the weakness of domestically owned enterprises. In this respect it is significant that in El Salvador, where some industrialists have been quick to seize the opportunities of the CACM, many of the local manufacturers have extensive interests in financial institutions.[25]

In general, however, the absence of a capital market of any importance in the region means that there is no mechanism by which savings are allocated to entrepreneurs who have investment opportunities. As a result, a considerable amount of savings is invested abroad or held by Central Americans as liquid assets in financial institutions outside the region.[26]

To strengthen the local capital market, a Costa Rican economist has suggested that the CACM form a "public investment corporation" which, in the manner of a mutual fund, could channel private savings to local industry.[27] But this increase in the demand for equity shares would have little effect on the level of investment unless an increased supply of industrial shares is forthcoming. At the present time neither the international corporation nor the family-owned firm is eager to sell equity shares in the local market. The international firm generally avoids issuing any significant number of shares in a subsidiary company, for there may be a conflict between maximization of global profits and maximization of profits in any single region, or there may be a conflict of interest, with the local shareholder preferring to maximize short-run profits and the parent company long-run profits.* The family firm, like the international enterprise, is adverse to issuing shares out of fear of losing some control of the company. Thus most domestically owned firms prefer to expand gradually through debt financing and reinvested earnings rather than seek outside shareholders who are willing to hold equity in the firm.[28]

Even with an effort to develop a strong Central American capital market, improve the technology of existing plants, and train business managers, the Central American industrialist needs time to adapt to his changed environment, and this requires governmental action to restrict direct foreign investment and protect the "infant" industrialist. No single country in the region is able to impose meaningful restrictions on foreign investment for fear that the international enterprise will simply move its subsidiary to another CACM country. At the same time, the national governments are reluctant to delegate to a regional body the authority to make decisions with respect to industrial investments, decisions which are of vital importance to any national economy. After several years of negotiations, the Central American governments have agreed to harmonize their fiscal incentives to industrial development, but an international firm can still "play off" one country against another to obtain a right to majority ownership and effective control of a subsidiary company. The CACM councils

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*Sears Roebuck is a notable exception, but it is not an industrial corporation.

can suggest guidelines but cannot, in most cases, make these guidelines binding on the member states.

The Central American Economic Council, which is made up of the five ministers of economics and is responsible for the overall direction of the CACM, is prepared to use its persuasive powers on behalf of the local industrialist. On the occasion of the visit of Governor Nelson Rockefeller in the spring of 1969, for example, the council emphasized that "direct foreign investment cannot be regarded as a substitute for international transfers destined to finance development projects in the public sector" and urged that direct investment be "channelled to priority sectors of the economy in such a way as to strengthen Central American entrepreneurship."[29]

Under the terms of the General Treaty of Economic Integration and the various protocols to that treaty, the Economic Council can do little more than encourage governments to favor domestic investors. The body can advise, but cannot decree, the composition of investment capital in almost all cases—with one important exception. This exception occurs when a company seeks to be declared an "integration industry" and thus obtain a privileged and protected position within the CACM for a period of ten years or more.[30]

When the ministers of economics drafted the 1963 protocol which designated the first two "integration industries," they were careful to restrict foreign participation in the enterprises.[31] The first "integration" enterprise—the GINSA tire and tube plant in Guatemala—had been established in 1957 with predominantly (94.2 percent) Central American capital.[32] The General Tire Company of Akron, Ohio, supplies technical assistance in exchange for minority participation and a contractual fee. As a condition of "integration" status, GINSA is required to issue a majority of any new shares to Central Americans. Similarly, a minimum of 40 percent Central American participation was required in the second "integration industry"—a new caustic soda and insecticide plant in Nicaragua.

The Economic Council's desire to protect Central American entrepreneurship was most evident during a dispute that developed between GINSA and the Firestone Tire and Rubber Company. GINSA was successful in substituting its own brand for some of the imports, and requested an increase in the tariff in the hope of supplying virtually all of the Central American demand for tires and tubes.[33] In reaction to the competition of GINSA in the regional market, Firestone decided to cross the tariff barrier and establish an "integration" plant in Costa Rica. This was legally permissible, for the 1963 protocol (Article 27) allows the executive council of the CACM to designate, by majority vote, additional "integration" plants for tires provided that 60 percent of the capital stock is offered to Central Americans and that at least 30 percent is actually purchased by them.

Firestone, however, was willing to sell a maximum of 25 percent of the initial shares in the local market, so Costa Rica's application for a second "integration" tire plant was referred to the Economic Council in February 1965. The council ruled that foreign participation could not exceed 30 percent—far less than the 75 percent requested by Firestone—and that the tires produced by the plant would have to carry a Central American brand name rather than the well-known Firestone insignia.[34]

Firestone could not accept the conditions imposed by the Economic Council, so built a plant without "integration" status in order to supply the Costa Rican and (by special arrangement) Panamanian markets. Under the terms of the Regime of Integration Industries, the tariff in the other four countries will be reduced by 10 percent each year, with free trade in tires at the end of ten years. Costa Rica cannot protect her industry from Guatemalan imports, so Firestone will undoubtedly incur losses during this transitional period. It is alleged, however, that Firestone intended to retain its share of the Central American market and was therefore not concerned with the fact that the plant would not be a profitable investment.[35]

The Central American tire and tube industry should provide an interesting case study of duopolistic competition during the present decade. If economies of scale are important in the industry, GINSA, which has three times the installed capacity of the Firestone plant, should have substantially lower costs per unit of output. However, competition between the two companies will most likely take the form of increased expenditures on advertising, and in this nonprice competition Firestone has the initial advantage of a well-established brand name. When Firestone began production in 1967, GINSA conducted an extensive advertising campaign to make Costa Ricans aware that GINSA, unlike Firestone, is a Central American company with a large number of shareholders throughout the isthmus. For several months the Costa Rican press and radio carried announcements of a promotional contest in which the prizes were shares of GINSA stock. As tariff barriers are removed for Firestone tires this type of advertising will undoubtedly increase throughout Central America. Ultimately the two companies will have to reach some type of tacit agreement regarding division of the market, or continue to face expensive outlays for promotional purposes.[36]

The inability of the Economic Council to prevent Firestone from investing in one of the CACM countries on its own terms is a direct consequence of the lack of a clearly defined agreement on foreign direct investment in the region. Nor does there exist a comprehensive policy on foreign ownership at the national level. The ministers of economics, acting jointly, have suggested some policy guidelines; but the party (or military junta) in power in each country has failed to formulate a similar statement of policy. Cabinet ministers are appointed by the president in each country, so one might conclude that silence on the issue is a weak approval of the ministerial statements. But in considering any particular case the national governments invariably ignore the appeals of local industrialists and accept foreign investment of any type so as to improve the balance of payments and stimulate the process of industrialization.

CONCLUSION

Economic integration and the substitution of imports in Central America has encouraged the development of the modern indigenous industrialist and, at the same time, threatens his existence. Direct foreign investment in the manufacturing sector is often competitive with the existing enterprises of local entrepreneurs. For this reason the Central American industrialist, through FECAICA and other pressure groups, is attempting to restrict foreign investment to areas that are not competitive with his own activities.

Thus far, the Central American industrialist has not been able to restrict the penetration of the international firm, which has an advantage in marketing, technology, and finance, and sufficient mobility to bargain with five independent republics. If Central America is to protect and favor national entrepreneurship, there must be an increased effort to improve the competitive position of domestically owned enterprises and there must be a common foreign investmental policy throughout the region.

Economists now generally accept the concept of an "infant" industry, and are beginning to admit the need for protection of national ("infant") entrepreneurship in a developing economy. It is very likely that Central America, like Mexico[37] and Peru[38], will begin to restrict direct foreign investment and promote national entrepreneurship.

Native industrialists, intellectuals, and common market officials increasingly share the opinion that most of the benefits of integration are accruing to "certain migratory birds,"[39] to international corporations rather than to local entrepreneurs. If the members of the Central American Common Market do not agree to a uniform policy with respect to foreign investment, individual governments may well find themselves under pressure to adopt more radical measures, such as the nationalization of foreign-owned subsidiaries.

CHAPTER 18

1. In underdeveloped countries as a whole, equity investment now forms 90 percent of private international investment, with a 10 to 15 percent return after taxes, compared with a 5 to 6 percent rate of return for bond credit. Paul N. Rosenstein-Rodan, "Multinational Investment in the Framework of Latin American Integration," in Inter-American Development Bank, *Multinational Investment in the Economic Development and Integration of Latin America* (Bogota, Colombia, 1968), pp. 54-55.

2. "The Role of International Movements of Private Capital in Promoting Development," in John H. Alder, ed., *Capital Movements and Economic Development* (London: Macmillan, 1967), p. 196. Quoted in A.O. Hirschman, "How to Divest in Latin America, and Why," *Princeton Essays in International Finance*, No. 76 (November 1969).

3. Arthur H. Cole, "An Approach to the Study of Entrepreneurship," *Journal of Economic History*, Vol. VI (Supplement, 1946), pp. 1-15.

4. Cleona Lewis, *America's Stake in International Investments* (Washington, D.C.: Brookings Institute, 1938). Cited in UN Economic Commission for Latin America (ECLA), *External Financing in Latin America*, E/CN.12/649/Rev.1 (New York, 1965), p. 15.

5. Mexican direct investment is usually in the form of a "joint venture." One recent project involving both Mexican and Costa Rican businessmen is a dehydrating plant for fruits and vegetables. See *La Republica* (San Jose), June 11, 1971, pp. 1, 17.

6. The process of nationalization of public utilities and railroads is still continuing in Central America. "Costa Rica Completa Nacionalizacion de Energia Electrica," Secretariado de Integracion Economico Centro American (SIECA), *Carta Informativa*, Vol. LXXXV (November 1968), p. 14; "Guatemala Declara Caducidad de la Concesion a Ferrocarriles Internacionales de Centroamerica," SIECA, *Carta Informativa*, 87 (January 1969), pp. 6-8.

7. See "Central Americans Lift Trade by Tariff Cuts; Arrow Shirt, Other Firms Rush In," *Wall Street Journal*, March 10, 1965, p. 1; Sheldon L. Schreiberg, "The United States Private Investor and the Central American Common Market," in U.S. Congress, Joint Economic Committee, *Latin American Development and*

Western Hemisphere Trade, Hearings (Washington, D.C., 1965), pp. 260-285.

8. Alvaro Contreras Velez in Prense Libre, 1965. Quoted by Francisco Villagran Kramer in Integración Económica Centroamericana: Aspectos Sociales y Políticos (Guatemala: Universidad de San Carlos, 1967), p. 235. My translation.

9. This phrase is borrowed from Eduardo Lizano F., "El Problema de las Inversiones Extranjeras en Centroamérica," Revista del Banco Central de Costa Rica, 67 (September 1966), p. 59.

10. "Honduras: the 78 Million Dollar Question," Latin America (London), May 31, 1968, pp. 170, 172.

11. SIECA, Carta Informativa, 89 (March 1969), pp. 22, 23.

12. "Pronunciamiento de la FECAICA en Relación a las Inversiones Extranjeras en el Área Centroamericano," March 25, 1965, in Villagran Kramer, Integración Económica Centroamericana, pp. 237-239.

13. "Declaration of the Ministers of Economy of Central America," June, 21 1965, in Inter-American Economic and Social Council, The Role of Foreign Private Investment in the Development of Latin America (Washington, D.C.: Pan American Union, 1969), pp. 168, 169.

14. Raul Sierra Franco, "La Industrialización en Centroamérica," in Seminario de Historia Contemporánea de Centroamérica (San Salvador: Editorial Universitaria, 1964), p. 25.

15. Roger D. Hansen, Central America: Regional Integration and Economic Development (Washington, D.C.: National Planning Association, 1967), pp. 87-89. (The 1969 ECLA Survey of Latin America notes that "several projects for the assembly of motor vehicles" have been initiated in Guatemala.)

16. Ibid., pp. 48-49.

17. Albert O. Hirschman, "The Political Economy of Import-Substituting Industrialization in Latin America," Quarterly Journal of Economics, Vol. LXXXII (February 1968), p. 21.

18. See Judd Polk, "U.S. Exports in Relation to U.S. Production Abroad," in Bela Balassa, ed., Changing Patterns in Foreign Trade and Payments (rev. ed., New York: Norton, 1970), pp. 61-71.

19. See I.A. Litvak and C.J. Maule, "Canadian Entrepreneurship and Human Resource Development: The Effect of Direct Foreign Investment," Business Quarterly, Spring 1972.

20. Thomas C. Cochran, The Puerto Rican Businessman: A Study in Cultural Change (Philadelphia: University of Pennsylvania Press, 1959), p. 86.

21. Warren Dean in The Industrialization of Sao Paulo (Austin: University of Texas Press, 1969), pp. 176-178, reports that Brazilian industrialists, whether immigrant or native, "demonstrated almost no interest in the technical training of their manpower pool." He notes that "it was true in a narrow sense that importing technicians was cheaper than training them, and yet of how little use to Brazil was an industrial system that condemned its citizens to unskilled labour." Very often criticisms of the international corporation apply with equal force to the family firm in Latin America.

22. Rosenstein-Rodan, "Multinational Investment," p. 64.

23. See L. N. Willmore, "Free Trade in Manufactures among Developing Countries: The Central American Experience," Economic Development and Cultural Change, (Chicago: University of Chicago Press, July, 1972).

24. This argument and the discussion which follows draws heavily on Lizano F., "El Problema de las Inversiones Extranjeras en Centroamerica," pp. 57-58.

25. Robert T. Aubbey, "Entrepreneurial Formation in El Salvador," Explorations in Entrepreneurial History, Vol. VI (Spring 1969), pp. 268-285.

26. The "Comision ad hoc para el Estudio del Mercado de Valores en Centroamerica" reports that liquid Central American assets held by the United States totalled U.S. $45.4 million in 1963, and U.S.$50.5 million in 1964. Banco Centroamericano de Integración Economica (BCIE), Un Mercado de Capitales Centroamericano: Dos Estudios (Mexico: Centro de Estudios Monetarios Latinoamericanos, 1967), p. 12.

27. Lizano F., " El Problema de las Inversiones Extranjeras en Centroamerica," p. 61.

28. This is apparently true even for El Salvador, whose entrepreneurs are reputedly the most progressive of the isthmus. See Guillermo Atilio Lopez Z., "Problemas de Desarrollo Industrial en El Salvador," Bacen, Vol. V (May 1966), pp. 19-23.

29. "Exposición del Consejo Económico al Gobernador Nelson A. Rockefeller," SIECA, Carta Informativa, 92 (June 1969), pp. 4-7.

30. See "Convenio sobre el Régimen de Industrias Centroamericanas de Integración" in Escuela Superior de Administración Pública (ESAPAC), Los Instrumentos del Mercado Común Centroamericano (San Jose, 1965), pp. 111-116. An English translation of the agreement is in Joseph Pincus, The Central American Common Market (Mexico: U.S. Agency for International Development, 1962), pp. 171-176.

31. "Protocolo al Convenio sobre el Régimen de Industrias Centroamericanas de Integración," in ESAPAC, op. cit., pp. 117-131.

32. GINSA is an atypical firm in that its ownership is widely dispersed throughout the five Central American countries. David E. Ramsett, Regional Industrial Development in Central America: A Case Study of the Integration Industries Scheme (New York: Praeger, 1969), p. 46.

33. GINSA has an installed capacity of 300,000 tires, but its annual production was less than 180,000 in the mid-1960s. The company thus requested the CACM to increase the tariff on standard tires from U.S.$0.90 specific and ten percent ad valorem to U.S. $2.00 specific and ten percent ad valorem. Ibid., pp. 60-73.

34. Consejo Económico, Cuarta Reunión Ordinaria, San Salvador, February 5-9, 1965. Cited in Ramsett, Regional Industrial Development, p. 51.

35. Conversation with Manuel Noriega Morales, Director of the Central American Institute of Research and Industrial Technology (ICAITI), July 14, 1970.

36. Ramsett, who has made an extensive investigation of GINSA, suggests that "the most probable occurrence would seem to be a [geographic] splitting of the market between the two firms." In his Regional Industrial Development, p. 74.

37. For an assessment of Mexico's policy on foreign investment, see I.A. Litvak and C. J. Maule, "Foreign Investment in Mexico: Some Lessons for Canada," Behind the Headlines, Vol. XXX (July 1971).

38. Peru's current industrial policy is discussed in L.N. Willmore, "Estrategia Peruana de Desarrollo Económico," Problemas del Desarrollo, Universidád Nacionál Autonomo de México (U.N.A.M.), 9 (October-December 1971), pp. 97-109.

39. Celso Gamboa, "Ante Imperdonables Fallas del Congreso Jurídico Sobre la Integración Economica Centroamericana," La Nación (San José), November 27 and 28, 1964. Quoted in Lizano F., "El Problema de las Inversiones Extranjeras en Centroamerica," p. 61.