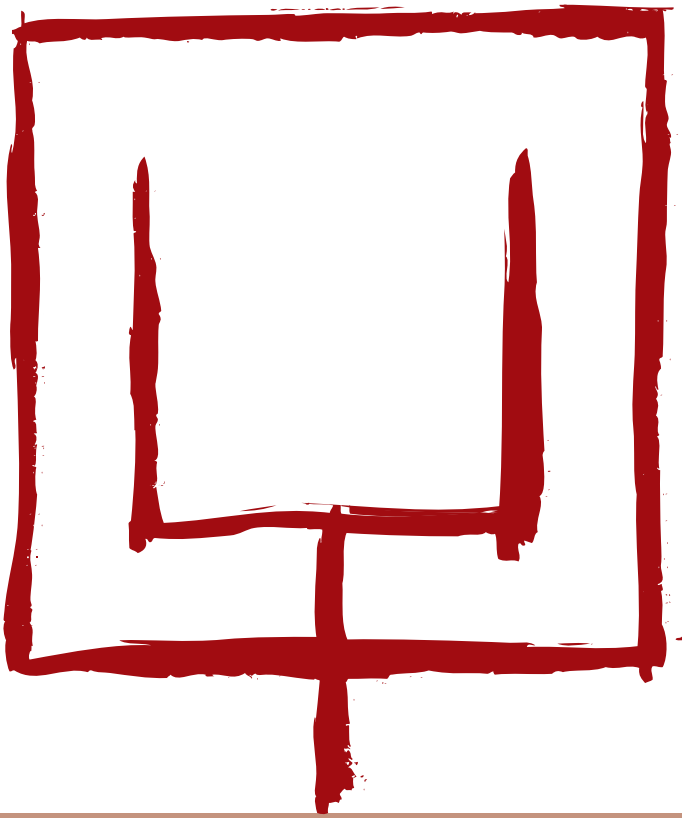
2015

Briefing paper



Foreign Direct Investment
in Latin America and the Caribbean

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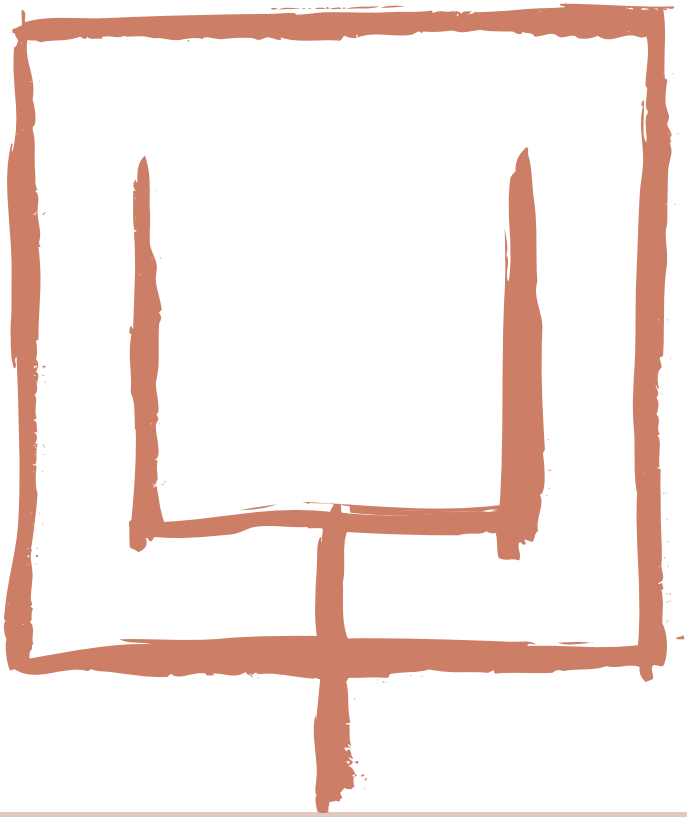

Foreign Direct Investment
in Latin America and the Caribbean

UNITED NATIONS

ECLAC

Alicia Bárcena
Executive Secretary

Antonio Prado
Deputy Executive Secretary

Mario Cimoli
Chief, Division of Production, Productivity and Management

Ricardo Pérez
Chief, Publications and Web Services Division

The 2015 version of *Foreign Direct Investment in Latin America and the Caribbean* is the most recent edition of an annual series published by the Unit on Investment and Corporate Strategies of the Division of Production, Productivity and Management of the Economic Commission for Latin America and the Caribbean (ECLAC). This year's edition was prepared by Olaf de Groot and Miguel Pérez Ludeña, under the coordination of Giovanni Stumpo. The database was built by Leandro Cabello.

Carol Fernández Delgado, Caroline Gomes, Michael Milligan and Ramon Padilla provided substantive contributions for the work. Comments and suggestions were received from Mario Cimoli, as well as staff from the Sustainable Development and Human Settlements Division (especially Carlos de Miguel, Joseluis Samaniego and Marcia Tavares), the subregional headquarters of ECLAC in Mexico (particularly Jorge Mario Martínez), and Port of Spain (in particular Dillon Alleyne and Michael Hendrickson).

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In previous editions of *Foreign Direct Investment in Latin America and the Caribbean*, the year given on the cover and in the title was the year for which data were presented. Starting with this edition, however, the title carries the year in which the report is published, consistently with the practice for the other flagship reports published by ECLAC. As a result, there is no 2014 edition of *Foreign Direct Investment*.

Any comments or suggestions concerning the contents of this document should be addressed to Giovanni Stumpo (Giovanni.stumpo@cepal.org) and Olaf de Groot (olaf.degroot@cepal.org).

Notes and explanations of symbols

The following symbols have been employed in this edition of *Foreign Direct Investment in Latin America and the Caribbean:*

- Three dots (...) indicate that data are missing, are not available or are not separately reported.
- A dash (-) indicates that the amount is nil or negligible.
- A blank space in a table indicates that the concept under consideration is not applicable or not comparable.
- The use of a hyphen (-) between years (e.g. 2008-2013) indicates reference to the complete number of calendar years involved, including the beginning and end years.
- A slash (/) between years (e.g., 2010/2011) indicates that the information given corresponds to one of these two years.
- The world "dollars" refers to United States dollars, unless otherwise specified.
- Individual figures and percentages in tables may not always add up to the corresponding total because of rounding.

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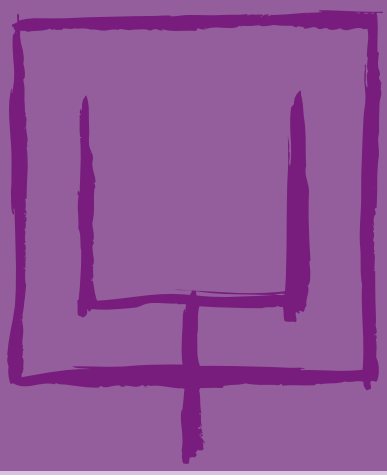


Summary and conclusions

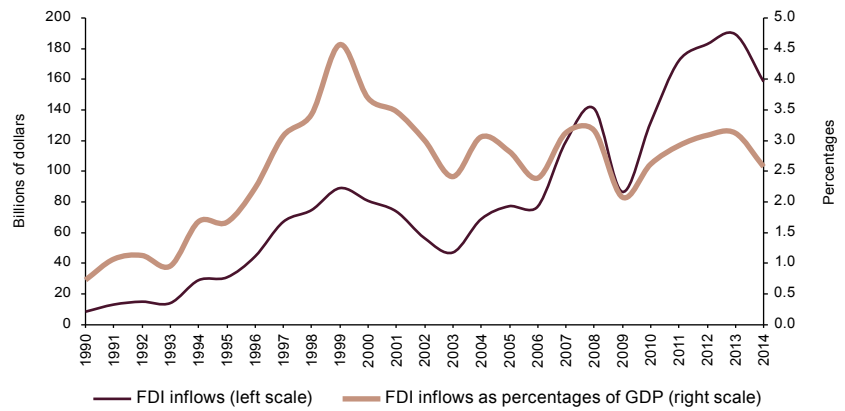
Foreign direct investment (FDI) in Latin America and the Caribbean fell by 16% in 2014 to US$ 158.803 billion. Outflows of FDI from the region were also down, by 8%. Both these trends were driven by the decline in prices of export commodities and the economic slowdown in the region. Nevertheless, FDI remains very important for the economies in the region, especially for smaller Caribbean economies.

A. Foreign direct investment in Latin America and the Caribbean

Global FDI flows were down by 7% in 2014, but flows to developing and developed economies differed significantly. Flows to the developed economies fell by 14%, as FDI to North America plummeted by 54%, owing principally to a single divestment in the United States. The Russian Federation faced sanctions, among other economic challenges, which led to a 51% fall in inflows to the transition economies in 2014, while inflows to the developing economies rose by 5%. Decreased flows to both Latin America and the Caribbean (16%) and Africa (2%) were offset by a substantial increase to developing Asia (15%).

As a share of GDP, FDI inflows in Latin America and the Caribbean stood at 2.6%, which is somewhat lower than the region's long-term average, although this proportion also varies significantly throughout the region. Smaller economies generally have high FDI-to-GDP ratios, with economies in the Caribbean regularly reaching levels as high as 10% of GDP. Larger economies typically have much lower ratios, for instance 1.5% of GDP in Brazil[1] and 2.0% of GDP in Mexico.

Figure 1
Latin America and the Caribbean: foreign direct investment inflows and FDI inflows as a proportion of GDP, 1990-2014 [a]
(Billions of current dollars and percentages of GDP)



Source: Economic Commission for Latin America and the Caribbean (ECLAC) on the basis of official figures and estimates as of 18 May 2015.

[a] Figures do not include flows into the main financial centres of the Caribbean. FDI figures indicate inflows of foreign direct investment, minus disinvestments (repatriation of capital) by foreign investors.. These figures differ from those set out in the 2014 editions of the Economic Survey of Latin America and the Caribbean and the Preliminary Overview of the Economies of Latin America and the Caribbean because these publications show the net balance of foreign investment, that is, direct investment in the reporting economy (FDI) minus outward FDI.

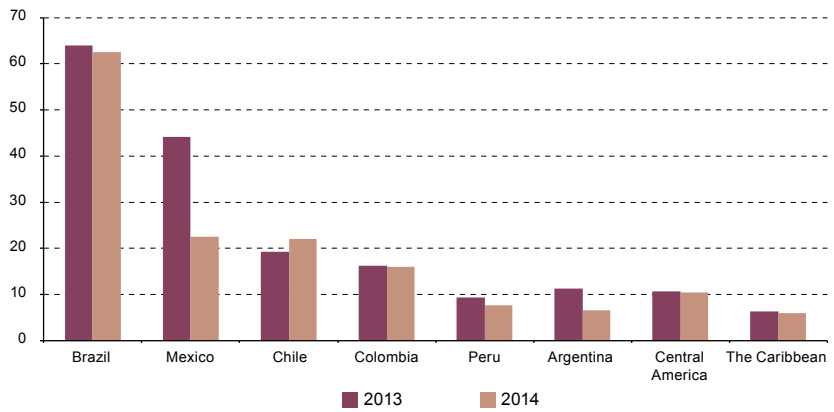
Among the larger economies, Mexico recorded the steepest fall in inflows, with a drop of 49% to US$ 22.795 billion. This can be explained by a number of one-off factors, including the fact that the 2013 FDI figures were inflated by the US$ 13.249 billion acquisition of beer maker Grupo Modelo by a European firm. Also significant was the divestment by United States-based AT&T of its holdings in América Móvil, worth US$ 5.57 billion. Brazil continues to be the largest recipient of FDI in the region, though inflows slipped by 2% to US$ 62.495 billion. Chile remains the third

[1] The Central Bank of Brazil has recently changed its data collection methodology (see chapter 1). Estimates included in this summary use the previous methodology, which is comparable with previous years.

largest recipient of FDI with US$ 22.002 billion, up 14% on 2013. FDI to Central America fell by 2%, while FDI to the Caribbean fell by 5%. The biggest increases in the region were reported by Barbados (5,119%), Paraguay (230%) and Antigua and Barbuda (66%), while the greatest decreases were seen in Suriname (97%), the Bolivarian Republic of Venezuela (88%) and Grenada (64%).

The sectoral distribution of FDI in 2014 also differed substantially from previous years. The share of natural resources in FDI inflows fell to 17%, compared with an average of 24% in 2009-2013. The share of manufacturing dipped to 36%, thus strengthening the dominant position of the services sector, which received 48% of inflows in 2014, compared with 38% in 2009-2013. In some economies, such as Colombia, Ecuador and the Plurinational State of Bolivia, the natural resources sector continues to receive a large share of FDI, but even in these economies that share is waning. The reason for this is the decline in the prices of minerals, which has been occurring since 2012, but is only now starting to affect FDI inflows. The price of oil dropped by half in the latter months of 2014, after remaining stable for several years.

Figure 2
Latin America and the Caribbean (selected countries): inward foreign direct investment, 2013-2014
(Billions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC) on the basis of official figures and estimates as of 18 May 2015.

There is some evidence that the technology intensity of FDI in the region is increasing: FDI in medium-high and high technology sectors now accounts for some 60% of total inflows, although with large differences between countries. Mexico receives the highest share of such FDI, followed by Brazil, owing mainly to large investments in the automotive sector (medium-high technology), which is having a transformative impact on those economies.

With respect to the source countries of investment, the Netherlands is now the largest investor country in Latin America, accounting for 20% of inflows that can be attributed to source countries. This chiefly reflects the Netherlands' position as by far largest investor in Brazil, since it is the source of 29% of flows into that country. The United States was responsible for 17% of inflows during 2014. Its investments account for a large share of total FDI in Mexico (29%), Colombia (14%) and Central America (33%). Spain is the third largest investor in the region, having nearly quadrupled its share to 10%. Spain has a particularly strong presence in Mexico (18%), Colombia (13%) and some of the Central American economies. Two large acquisitions by Spanish companies in 2014 are evidence of the recovery of Spanish inflows after several years of weak inflows. Official FDI from Asia to the region is minimal, accounting for some 6% of total flows in 2014, of which one sixth comes from China.

Outward FDI decreased for the second year in a row, falling by 8% to US$ 29.628 billion in 2014. The same factors behind the overall drop in FDI inflows to the region also explain the lower FDI outflows since the vast majority of trans-Latin corporations invest within the region. Outflows from Colombia and Mexico dropped markedly in 2014, whereas outflows from Chile increased. Brazil's FDI outflows have been negative for four years running, owing to large inter-company loans that seek to bypass the high cost of capital in the country. Despite the fall in outflows from Mexico, Mexican trans-Latins continue to dominate the list of cross-border acquisitions. Peru became the third largest investor abroad in 2014, with outflows of US$ 4.452 billion.

The proportion of profits that transnational corporations reinvest in the same economy remained more or less stable at 50%, while they repatriate the rest. The downtrend in the average profitability of FDI seen since 2008 continued, reaching 5% in 2014. Total FDI income declined by 16% to US$ 103.877 billion, as the economic slowdown and lower prices of export commodities reduced profits across most countries.

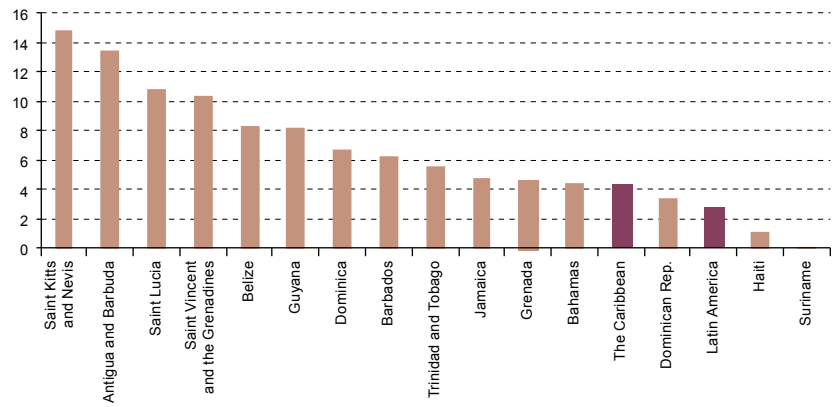
Despite this drop in 2014, FDI income is still the largest negative item in the current account for most economies in the region. This has become a source of concern because over the previous decade the trade account has deteriorated significantly, generating growing current account deficits that in 2013 and 2014 reached 2.7% of GDP for the region as a whole. This deficit has to be financed through capital inflows, of which FDI has been the largest and most stable type. In fact FDI is now the largest external liability in the region and as such it will continue to generate large flows of FDI income in the near future. In other words, FDI is not a free form of capital and countries should therefore attempt to direct these flows to projects with the capacity to transform their production structure.

FDI flows into Latin American and the Caribbean will likely decline again in 2015. The region's slack economic growth —projected at around 1% for the year— will continue to act as a brake on domestic-market-seeking investments. This will drag down FDI inflows to Brazil, in particular. Conversely, Mexico could well receive more investment in 2015 thanks to the large number of projects announced in manufacturing and to regulatory changes making it easier for foreign firms to enter certain segments of the services market. Investment is expected to continue slipping in mining, regardless of international price trends, and in hydrocarbons, owing to the drop in the oil price in the latter months of 2014. Accordingly, ECLAC estimates that inflows to the region overall will be down by as much as 10%.

B. Foreign direct investment in the Caribbean

FDI is very important for the Caribbean, where FDI inflows in many economies make up a much larger share of GDP than in Latin America. In 2014, FDI inflows in the subregion fell by 5% to US$ 6.027 billion. The Dominican Republic and Trinidad and Tobago are the largest recipients in the Caribbean, absorbing 37% and 23% of total inflows, respectively. At the other extreme, Cuba and Haiti receive only small amounts of FDI, despite their large populations.

Figure 3
The Caribbean (selected economies): inward foreign direct investment as a proportion of GDP, 2014
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and estimates as of 18 May 2015.

Of the economies in the Caribbean, the Dominican Republic's FDI inflows are the most balanced in terms of distribution between natural resources, manufacturing, tourism and other services. The inflows of many other economies typically depend more heavily on a particular sector. The Bahamas and the members of the Organisation of Eastern Caribbean States (OECS), for example, receive the bulk of investment in the tourism sector, while inflows to Guyana, Suriname and Trinidad and Tobago are driven primarily by natural resources. In 2014, Haiti and Jamaica

received the majority of FDI in the transport and telecommunications sector on the back of significant investments in the expansion of telecommunications services.

The tourism industry is a key sector, attracting the bulk of investment in many countries in the Caribbean. The transformative impact of tourism investment is constrained by the limited capacity of many economies to provide the inputs required by the tourism value chain. To address this constraint, governments should encourage home-grown investment in secondary services, as well as agriculture and small-scale manufacturing, to increase spillovers from the tourism industry. Countries in the Caribbean should also remain vigilant regarding the fast rise in tourist numbers to other regions, which may leave some ambitious expansion plans without the market necessary to support them.

Significant FDI takes place in the hydrocarbons sectors of Trinidad and Tobago and Suriname, where oil is an important export product. The mineral that attracts most FDI in the region's mining industry is gold. Guyana and Suriname have substantial operations in the gold mining industry, but the largest mining investment in the Caribbean is the Pueblo Viejo gold mine in the Dominican Republic. The construction of the mine has been completed, so it is not currently receiving significant inflows of FDI, but it has had a positive impact on the country's current account and may open the door to further investment in the future.

The Dominican Republic, being the largest economy in the region, also attracts significant investment in the export-oriented manufacturing sector, particularly from the United States. Haiti is also slowly entering this market, but from a very low base. Export-oriented services play a much larger role in the rest of the Caribbean. Business process outsourcing (BPO) is a key export-oriented service in several economies, while others focus on higher value financial services. A unique export-oriented service in the Caribbean is offshore education. There are currently 40 educational institutions that target the North American education market, with significant spillover benefits for local economies.

One major constraint on market-seeking FDI is the small size of the subregion's markets. However, some firms manage to operate profitably by treating the Caribbean as a single market, rather than a collection of small markets. This strategy is apparent in the telecommunications and financial services markets. In other sectors, much of the market-seeking FDI is from small firms seeking niches in the different economies. Several major trans-Caribbean conglomerates are also actively vying for share in the different markets. These companies use their conglomerate structure to reduce risk by taking on different product and geographical markets. While these trans-Caribbean conglomerates have typically focused mainly on the Caribbean, the sluggish economic growth in the subregion is now pushing them to look further afield and seek investment opportunities in South, Central and North America.

The subregion's ability to attract significant FDI is attributable in part to a generous set of FDI promotion policies. Currently, such policies target four areas: active promotion by an investment promotion agency; improving the overall business climate; reducing obstacles that are specific to foreign investors; and providing financial incentives, such as tax holidays. Most governments focus on providing financial incentives since they are easily granted, while it is much harder to introduce structural improvements to the business climate. Nonetheless, the complicated fiscal situation in many Caribbean countries should prompt governments to rethink their focus on such incentives. This will be challenging, however, since competition between taxation regimes is used to attract the largest investments, and Caribbean governments will therefore have to work together to coordinate such policy changes across the subregion.

It is not clear whether existing FDI promotion policies have a positive or negative impact on economic development. FDI certainly can have a transformative impact on a country's economic situation, but only if the conditions are right for encouraging local spillovers by integrating FDI with local value chains. This is not currently the case for the Caribbean. Furthermore, FDI may promote growth in a country's capital stock or help sustain temporary current account deficits, but since the relationship between FDI and capital stock growth is weak and outflows of FDI income have been increasing, neither of these potential effects would seem to be of benefit to the subregion.

While the Caribbean has attracted significant FDI over the years, it is not clear that the region has fully leveraged that investment. Most governments could do more to harness existing FDI to encourage economic growth, while some economies, particularly Cuba and Haiti, which have to date received very small FDI inflows, would first have to attract those flows in order to perceive any significant positive impact.

C. Transnational corporations and the environment

Despite the recent weakening of FDI inflows, transnational corporations have a very significant —and still growing— presence in Latin American and Caribbean economies, and their environmental footprint is therefore large as well. Transnational corporations played a major role in establishing certain consumption and production patterns (including the rise in car ownership) which have long-term implications for the region's environmental sustainability. Their investment strategies can therefore have very significant implications regarding the environmental impact of economic activity.

It is not possible to measure the exact environmental impact of FDI, but since different sectors affect the environment in very different ways, the ecological impact of FDI depends to a large extent on its distribution across sectors. Mining, for example, is one of the sectors that attracts most FDI to Latin America and the Caribbean, but it also has major environmental implications, emitting five times more greenhouse gases per dollar of output than the economy-wide average, while generating significant environmental liabilities that have sparked conflicts with local communities throughout the region. Mining activities in Latin America have also become more energy-intensive during recent years because of declining ore grade in ageing deposits. Some heavy industries also have a large environmental footprint, whether in terms of their greenhouse gas emissions or the average pollution abatement costs that they incur. By this last measure the steel, paper and pulp, and chemical industries are the heaviest polluters. Lastly, agriculture is another sector with a large environmental impact (it is, in fact, the largest source of greenhouse gas emissions in the region), although it is not an FDI-intensive sector.

Foreign direct investment can thus be expected to have a more serious environmental impact in countries where it is concentrated in mining and heavy industry, though the actual impact of each investment is contingent on government regulations (and their enforcement) and the actions taken by companies.

Large international corporations are increasingly considering their environmental footprint and taking steps to mitigate it, over and above local regulatory requirements. On average, they engage in more initiatives of this type than Latin American companies and could lead by example in this regard. However, it is difficult to gauge the impact of such voluntary actions, and many of them are in fact little more than marketing strategies. Many of the initiatives that have a real impact on the environment are those that also bring financial benefits to companies, such as actions to improve energy efficiency. In any case, voluntary actions cannot substitute for public regulation.

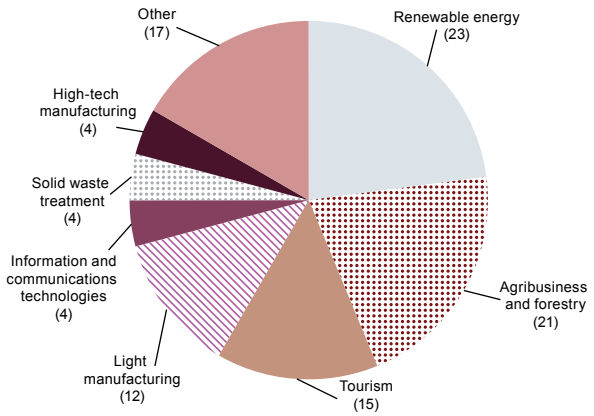
Looking to the future, substantial investments will be required to make the economies of Latin America and the Caribbean more environmentally sustainable. Worldwide, it is estimated that current investment falls as much as US$ 1 trillion short of that needed to meet the sustainable development goals on climate change and water and sanitation services. To cover this gap, the private sector will need to make a larger contribution in developing countries and transnational corporations will be key stakeholders in this process, since they hold considerable assets in Latin America and the Caribbean and have the technological and institutional wherewithal needed to enhance sustainability.

FDI has great potential to supplement domestic investment, but opportunities will need to be translated into workable business models. Investments in infrastructure are crucial for improving the region's environmental sustainability, but experiences to date have had mixed results. For example, many foreign investments in water and sanitation services had negative outcomes; on the other hand, the governments of the region have managed to attract large investments to the renewable energy sector.

FDI is also one of the key mechanisms for transferring green technologies to Latin America and the Caribbean and other developing regions. Most of the research and development that leads to the creation of such technologies is carried out by transnational corporations based in developed countries, though some innovation also takes place in the region. The development of second-generation ethanol (by domestic and foreign companies in Brazil, with the support of the government) is an example of a homegrown technology with the potential to reduce the environmental impact of transport.

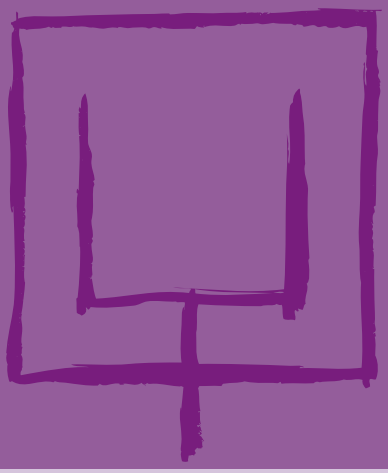
All the region's countries have environmental policies, but they are seldom coordinated with investment promotion efforts. Still, almost two thirds of investment promotion agencies claim to consider the environmental impacts of FDI and, despite limited room for manoeuvre, many have programmes to attract FDI based on green criteria, with a strong focus on renewable energy (see figure 4). Governments should aim to ensure consistency between FDI promotion policies and other policies that have a bearing on the environment, such those on energy, transport, industry and urban development.

Figure 4
Latin America and the Caribbean:[a] target sectors for attracting green investment
(Percentage of total responses)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the respective countries.
[a] Includes responses by investment promotion agencies in 19 of the region's countries, out of a possible total of 31, to a survey conducted between October and December 2014.

Chapter I



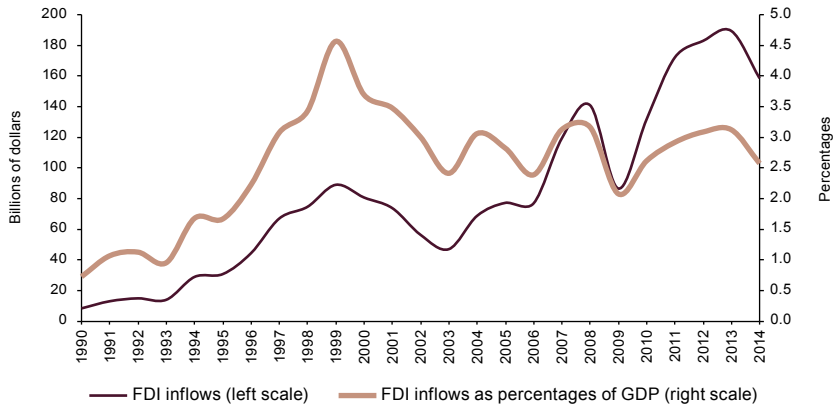
Overview of foreign direct investment in Latin America and the Caribbean

Introduction

Foreign direct investment (FDI) in Latin America and the Caribbean fell by 16% in 2014 to US$ 158.803 billion,[1] reversing a growth trend that had lasted more than a decade (aside from brief dips in 2006 and 2009). Business conditions deteriorated and the profits of transnational corporations did not reach the heights of previous years. FDI outflows (or foreign investments by trans-Latin corporations) were also down in 2014, totalling US$ 29.162 billion.

As a proportion of the size of the regional economy, FDI inflows in 2014 were in line with the previous decade's average of 2.6% of GDP. This indicator shows that, after a short spell of very high inflows around the turn of the century, FDI has stabilized in relation to GDP, despite growing significantly in nominal terms, peaking at a record high of US$ 189.951 billion in 2013 (see figure I.1).

Figure I.1
Latin America and the Caribbean: foreign direct investment inflows and FDI inflows as a proportion of GDP, 1990-2014 [a]
(Billions of current dollars and percentages of GDP)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures as of 18 May 2015.
[a] Figures do not include flows into the main financial centres of the Caribbean. FDI figures indicate inflows of foreign direct investment, minus disinvestments (repatriation of capital) by foreign investors. These figures differ from those set out in the 2014 editions of the Economic Survey of Latin America and the Caribbean and the Preliminary Overview of the Economies of Latin America and the Caribbean because they show the net balance of foreign investment, that is, direct investment in the reporting economy (FDI) minus outward FDI.

In 2014, FDI inflows suffered from sluggish economic growth across the region and lower export commodity prices. The same factors were in play in 2013, but a single exceptionally large transaction (the acquisition of the Mexican brewer Grupo Modelo for US$ 13.249 billion) inflated the FDI figures for that year, masking the effects of the two factors. The drop in FDI outflows is attributable to the same factors since trans-Latin corporations tend to invest mainly within Latin America and the Caribbean, where the investment conditions were unfavourable.

The adverse conditions hit the natural resources sector hardest, in particular mining. The lower profits recorded by this sector were partially responsible for the overall drop in FDI inflows, as the value of reinvested earnings fell. Even though the returns on FDI declined across the region, FDI income remains the largest negative item in the current account and is therefore a source of concern for many countries with large current account deficits.

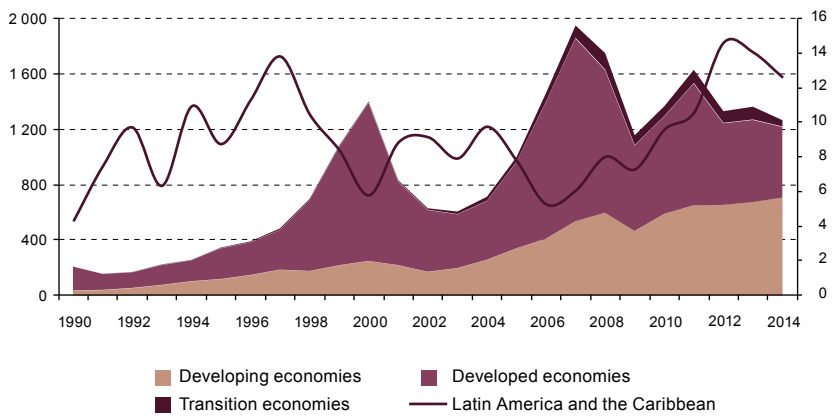
[1] The Central Bank of Brazil recently changed its accounting methodology from that prescribed by the fifth edition of the IMF *Balance of Payments Manual* to that of the sixth edition. This has resulted in a substantial increase (55%) in its recorded FDI inflows. However, at the time of publication, only the 2014 figures are available under the sixth edition methodology, meaning that changes in the data over time cannot be identified. For that reason, in this chapter, all data concerning Brazil are represented by the fifth edition methodology unless otherwise specified. The subsection specifically on Brazil includes and compared the results from both methodologies.

A. Overview of foreign direct investment worldwide

In 2014, global FDI inflows decreased by 7% to approximately US$ 1.27 trillion, reversing the slight uptick of the previous two years. However, the drop is less striking when the largest divestment of 2014, valued at US$ 130 billion, is excluded. In that transaction, United States-based Verizon Communications reacquired the 45% share in Verizon Wireless previously held by the United Kingdom's Vodafone in order to take full control of the mobile telecommunications carrier. Without this transaction, global FDI flows would have been practically stable in nominal terms.

Consistently with the recent trend, developing countries increased their share of global FDI inflows to 56% in 2014 (see figure I.2). Transition economies saw FDI inflows fall by 51%, accounting for a mere 3.6% of global FDI inflows. The primary culprits of this stark decrease were the political uncertainty in Ukraine and the Russian Federation's weakening economic performance, compounded by the sanctions against it. Developed economies saw a small decrease of about 14% in inward FDI, attributable primarily to the Verizon deal, which caused a two-thirds fall in inflows to the United States. If that deal had not taken place, inflows to North America would have decreased only marginally. Inflows to the European Union, on the other hand, rose by 14% to US$ 267 billion, although this is still equivalent to only about one third of the inflows before the financial crisis. Both France and Germany posted negative FDI inflows in 2014, owing primarily to intercompany loans and, in the case of France, to a single divestment.

Figure I.2
Global flows of foreign direct investment by group of economies and the share of Latin America and the Caribbean in those global flows, 1990-2014
(Billions of dollars and percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations Conference on Trade and Development (UNCTAD), *Global Investment Trends Monitor*, No. 18 ((UNCTAD/WEB/DIAE/IA/2015/1), Geneva, 2015 and World Investment Report 2014 (UNCTAD/WIR/2014), Geneva, 2014.

FDI inflows to developing countries increased by 5% in 2014 relative to the previous year, with Asian economies receiving the largest share (US$ 492 billion). The two largest FDI recipients worldwide are both located in Asia: China, which received US$ 128 billion in 2014; and Hong Kong Special Administrative Region of China, which received US$ 111 billion. In 2014, inbound FDI to Africa fell by about 3%, with a 17% decline in North Africa and a marginal uptick in Sub-Saharan Africa. According to UNCTAD (2015), a 41% increase in mergers and acquisitions (M&As) indicates growing interest in African consumer markets. Latin America and the Caribbean saw the largest fall in inflows among developing economies, with a 16% drop. However, this was expected after the spike in inflows in 2013 (see table I.1). [2]

[2] For the first time, in this edition the figures in table I.1 do not include the Caribbean financial centres, which partly explains why the overall numbers for all years reported are lower than those published in previous years. Yet, even excluding the financial centres, developing economies were able to increase their proportion of global FDI inflows from 50% to 56%, the highest share ever recorded.

Table I.1
Global foreign direct investment inflows, variation and distribution by region, 2005-2014 [a]
(Billions of dollars and percentages)

Region grouping	Investment flows (billions of dollars)						Variation rate (percentages)						Investment flows (percentages)					
	2005-2009	2010	2011	2012	2013	2014	2005-2009	2010	2011	2012	2013	2014	2005-2009	2010	2011	2012	2013	2014
World	**1 449**	**1 347**	**1 613**	**1 329**	**1 363**	**1 266**	**9**	**-7**	**20**	**-18**	**3**	**-7.1**	**100**	**100**	**100**	**100**	**100**	**100**
Developed economies	**917**	**703**	**880**	**590**	**594**	**511**	**8**	**-23**	**25**	**-33**	**1**	**-14.0**	**63**	**52**	**55**	**44**	**44**	**40**
European Union	574	384	490	282	235	267	-2	-33	28	-42	-17	13.6	40	28	30	21	17	21
North America	259	226	263	213	302	139	24	-13	16	-19	42	-54.0	18	17	16	16	22	11
Transition economies	**74**	**71**	**95**	**84**	**92**	**45**	**31**	**-4**	**34**	**-11**	**10**	**-51.1**	**5**	**5**	**6**	**6**	**7**	**4**
Developing economies	**470**	**590**	**653**	**655**	**676**	**710**	**10**	**26**	**11**	**0**	**3**	**5.1**	**32**	**44**	**40**	**49**	**50**	**56**
Latin America and the Caribbean	99	132	172	183	190	159	8	33	31	6	4	-16.4	7	10	11	14	14	13
Africa	47	47	48	55	56	55	17	1	2	15	2	-1.8	3	3	3	4	4	4
Developing Asia	323	409	431	414	427	492	10	27	5	-4	3	15.2	22	30	27	31	31	39
Errors and omissions	**-12**	**-17**	**-15**	**0**	**1**	**0**	**-**	**-**	**-**	**-**	**-**	**-**	**-1**	**-1**	**-1**	**0**	**0**	**0**

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations Conference on Trade and Development (UNCTAD), *Global Investment Trends Monitor,* No. 18 ((UNCTAD/WEB/DIAE/IA/2015/1), Geneva, 2015 and World Investment Report 2014 (UNCTAD/WIR/2014), Geneva, 2014.

[a] In Global Investment Trends Monitor No. 18 (UNCTAD, 2015), UNCTAD introduced a methodological change by excluding data for the financial centres in the Caribbean and elsewhere, which has resulted in significant changes for global totals and regional distributions for past years. As fully revised data are not yet available, regional shares for past years have been corrected only for the inclusion of the Caribbean financial centres. Other updates implemented by UNCTAD for those years for which full data are not available have been aggregated in the errors and omissions category.

B. Inward foreign direct investment in Latin America and the Caribbean

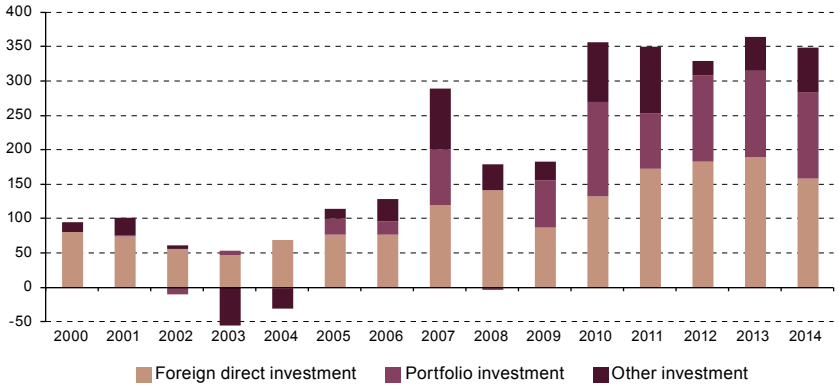
1. General trends

FDI inflows reached US$ 158.803 billion in 2014, a 16.4% drop compared with 2013 and similar to the level recorded in 2011, in nominal terms. This is only the third drop in FDI inflows since 2003 and the previous two, in 2006 and 2009, were quickly turned around by large increases in the following year.

FDI inflows grew from less than US$ 50 billion in 2003 to a peak of US$ 189.951 billion in 2013 (in nominal terms) on the back of high commodity prices, which boosted FDI in natural resources, and steady GDP growth across most of the region, which increased FDI in services and manufacturing for the domestic market. Prices of the region's key export commodities started to decline in 2012 and economic growth slowed in 2013, but FDI inflows continued to reach new highs in those years, in part because of the extraordinarily large acquisition of the Mexican brewer Grupo Modelo by Anheuser-Busch InBev for US$ 13.249 billion in 2013. Excluding this single transaction, FDI inflows would have been flat in 2013.

The decline in inward FDI is taking place in a context of relative financial stability and stable capital flows in Latin America and the Caribbean (ECLAC, 2014b). In 2014, risk premiums remained stable and capital inflows held firm on the back of increased other investment inflows (typically bank loans and deposits) (see figure I.3). For the past five years, portfolio investment and other investment have grown in importance and remained relatively stable. Over this period, FDI accounted for just 47% of cross-border capital inflows, compared with almost 70% during the preceding decade. Nevertheless, since portfolio inflows are concentrated in the largest economies, many smaller economies in the region rely more heavily on FDI for their capital needs.

Figure I.3
Latin America and the Caribbean: inward cross-border capital flows, 2000-2014
(Billions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official sources as of 18 May 2015.

In 2014, the dollar continued to appreciate against most other currencies. This trend was sparked by the United States Federal Reserve's 2013 announcement of its intention to begin withdrawing quantitative easing, and it continued throughout 2014, accelerating towards the end of the year. The faster dollar appreciation was attributable to the falling oil price, which affected several economies in Latin America, as well as the United States' improving economic performance and expectations of a hike in the interest rate set by the Federal Reserve.

Not all currencies were affected in the same way, however. Of the major currencies in Latin America, the Argentine and Colombian pesos suffered the greatest depreciation with respect to the dollar in 2014, falling by 31% and 24%, respectively. The currencies of Brazil, Chile and Mexico depreciated by between 12% and 15% against the dollar, while remaining more or less stable against the euro. Peru is an exception since the sol depreciated only slightly (7%) against the dollar and appreciated by a similar amount against the euro.[3]

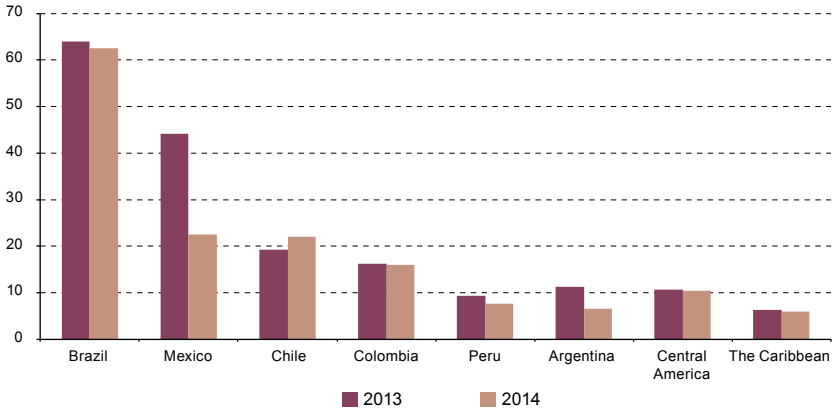
The impact of such currency devaluations on FDI inflows is somewhat ambiguous. On the plus side, they can reduce the cost of investments, particularly greenfield investments, that are expressed in local currencies. Meanwhile, mergers and acquisitions, which are generally denoted in dollars, have become more expensive for European investors, but cheaper for investors from the United States. A third consideration is that devaluation tends to reduce the returns on market-seeking investments, whose profits are expressed in dollars, and increase returns on export-oriented investments.

In short, the impact of currency fluctuations is uncertain and depends on several factors, including the type of investment, the origin of the investor and the specific local situation of the investment destination. Overall, in the short term, devaluations are most likely to have a marginal effect, as FDI investment decisions are typically driven by long-term considerations.

The decline in inward FDI was concentrated in the largest economies. Of the region's six largest economies, only Chile recorded increased FDI inflows, while in Colombia they remained stable. Brazil remains the largest recipient country in the region, having received US$ 62.495 billion in 2014, marginally less than in previous years. Mexico, the second largest economy in Latin America, was also the second largest FDI recipient. However, at US$ 22.568 billion, its recorded inflows fell short of the average for the previous decade, even in nominal terms. On the other hand, the two-year average of US$ 33.384 billion is the highest ever recorded. Chile received US$ 22.002 billion, more than in 2013, but still less than at its peak in 2012. At US$ 16.054 billion, inflows to Colombia were the same as for 2013. Peru recorded a drop in FDI inflows for the second year running. While flows of FDI to South America, as well as Mexico, ebbed in 2014, flows to Central America and the Caribbean were practically unchanged (see annex table I.A.1).

[3] Before 2014, the Bolivarian Republic of Venezuela maintained an official fixed exchange rate of 6.3 bolívares to the dollar which was significantly out of step with the parallel market rate. In 2014, the government introduced two alternative exchange rates, which stood at 11.3 bolívares to the dollar and 50 bolívares to the dollar in November 2014. The use of different types of exchange rates is limited to specific groups of importers and investors (ECLAC, 2014a). Early in 2015, another regime was introduced with an exchange rate of 192 bolívares to the dollar.

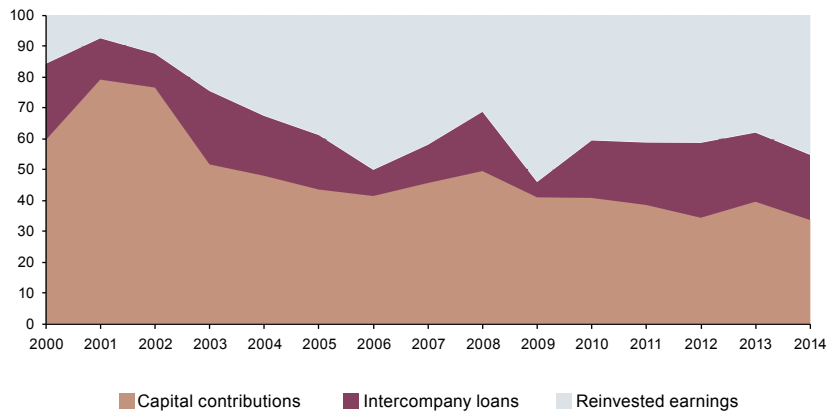
Figure I.4
Latin America and the Caribbean (selected countries): inward foreign direct investment, 2013-2014
(Billions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and estimates as of 18 May 2015.

In absolute terms, all three components of FDI inflows were lower in 2014 than in previous years. Capital contributions fell the most relative to the other components, owing in part to their larger-than-usual share in 2013 following the Grupo Modelo acquisition mentioned above. Intercompany loans and reinvested earnings dropped relatively less and therefore their share in the region's FDI inflows edged upwards (see figure I.5 and annex table I.A.4).[4]

Figure I.5
Latin America and the Caribbean: foreign direct investment by component, 2000-2014
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and estimates as of 18 May 2015.

The share of reinvested earnings in FDI inflows had grown over the previous decade, owing to a significant rise in FDI income (ECLAC, 2013b). Since 2010, however, FDI income has grown only modestly and the share of reinvested earnings in the region's FDI inflows has stabilized at around 40% of total inflows.

Across the region, transnational corporations tend to reinvest approximately 50% of their earnings within the same subsidiary and repatriate the remaining 50%. The proportion of earnings that is reinvested has remained almost unchanged over the years. In 2014, 53% of FDI income was reinvested in the economies with information available.[5]

FDI income, the profits reported by transnational corporations in the region, totalled some US$ 103.877 billion in 2014, 16% less than in 2013. Most countries in the region registered a drop in FDI income, including Brazil (-9%),

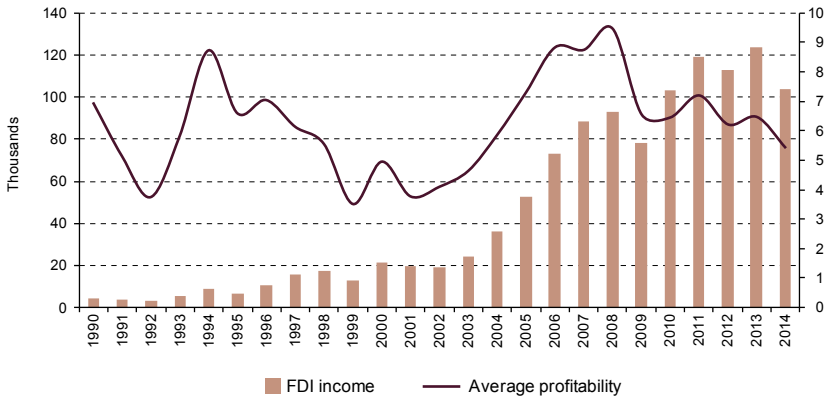
[4] The breakdown of FDI by component is calculated on the basis of information from 32 countries, representing 66% of FDI in the region. Under the fifth edition of the *IMF Balance of Payments Manual* methodology, Brazil did not include reinvested earnings in its calculation of FDI and it is excluded for this reason.

[5] Calculations on the basis of data from Chile, Dominican Republic, Peru, Plurinational State of Bolivia and Uruguay.

Colombia (-10%), Chile (-12%) and Peru (-14%). In the last two countries, the profit downturn was concentrated in the mining sector. In Brazil the heaviest drop in FDI income was in the automotive sector, which was hit especially hard by the worsening economic conditions and limited access to credit. This sector had yielded particularly high profitability rates in Brazil over the past decade. The largest drop was registered in Mexico (-38%), but this was due to extraordinarily high FDI income registered in 2013.

Average profitability, measured as FDI income divided by FDI stock, fell to 5%, which is slightly lower than the average for the previous two decades and represents a sharp reduction from the highs of over 9% reached between 2006 and 2008 (see figure I.6).

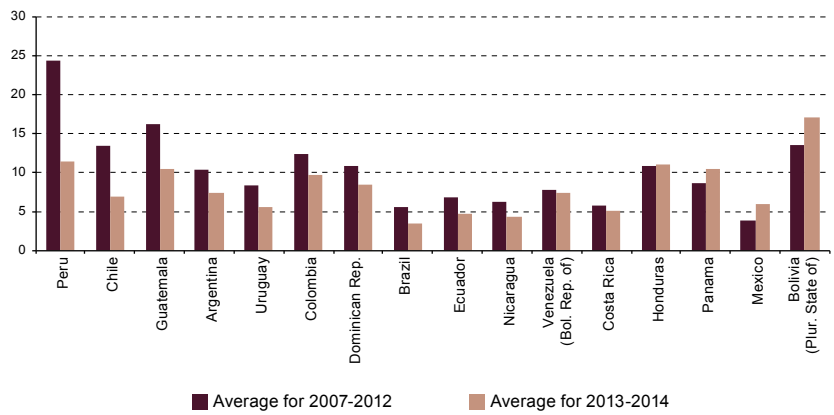
Figure I.6
Latin America and the Caribbean: FDI income and average profitability of FDI, 1990-2014
(Billions of dollars and percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and estimates as of 18 May 2015.

The decline in average profitability since 2012 was especially marked in countries with large FDI stocks in mining. From 2006 to 2011, average annual profitability reached 25% in Peru and 15% in Chile, but since 2012, as prices of metals have declined and costs have risen, these profitability levels have reverted to more reasonable rates (see figure I.7). Average profitability also declined, albeit less, for countries in which FDI is not concentrated in natural resources. By contrast, transnational corporations in Panama have reported a rise in average profitability, and so did companies in Mexico, although from a low base.

Figure I.7
Latin America and the Caribbean (selected economies): FDI income as a proportion of FDI stock, averages 2009-2012 and 2013-2014
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and estimates as of 18 May 2015.

Thanks to the continuing rise of FDI stocks in the region, the considerable drop in average profitability over the past two years has led to only a small decline in FDI income. FDI stocks are defined as the assets owned by transnational corporations in the host economy at the end of the year. FDI stocks grow with new investments (either greenfield or acquisitions) and shrink with asset divestments or depreciation. In nominal terms they have risen considerably over the past few years, reflecting the fact that FDI is the largest external liability for most economies.

FDI stocks have grown relative to GDP over the last decade, indicating that transnational corporations now have a larger footprint than ever before in the region. This has not been the case, however, for Argentina, the Bolivarian Republic of Venezuela, Ecuador, Guatemala and the Plurinational State of Bolivia, which have prioritized national investments over FDI (with the exception of Guatemala) (see annex I.A.5).

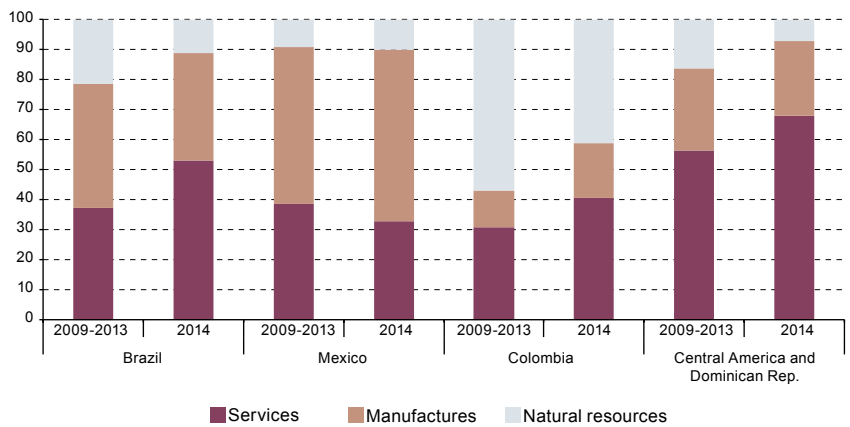
2. Distribution of FDI by sector

For those countries with FDI data disaggregated by sector, the biggest change in 2014 was the slump in flows to the natural resources sector, which recorded its lowest share in FDI in the last 10 years at 17% of total inflows, down from 24% in 2009-2013. Since manufacturing's share remained at the same level as in previous years (36%, compared with 39% in 2009-2013), the greatest expansion took place in the services sector. For those economies with data available, the services sector received 48% of inflows in 2014, compared with 38% in 2009-2013. These averages obscure the large differences between the economies, which are shown in figure I.8. In 2014, services exceeded a 50% share in Brazil's total FDI for the first time, reaching 53%. This was explained in part by the relatively large fall in the share of the natural resources sector, which shrank from 21% to 11% of inflows. In Mexico, manufacturing absorbed more than 50% of FDI, owing largely to flows to the automotive sector, while the share of the services sector fell to 33%. Services were also important in Colombia (41% of FDI inflows, up from 31% in 2009-2013), the Dominican Republic (74%, up from 47%) and the rest of Central America (66%, compared with 61%) (see figure I.8). The major economies that do not report data disaggregated by sector include Argentina, Chile and Peru. The last two of these have typically received significant inflows of FDI to the natural resources sector, but tentative information suggests that those flows also diminished in 2014 (see annex table I.A.2).

Figure I.8

Latin America (selected countries and subregions): sectoral distribution of foreign direct investment, 2014 [a]

(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and estimates as of 18 May 2015.
[a] The figures for Central America exclude Panama.

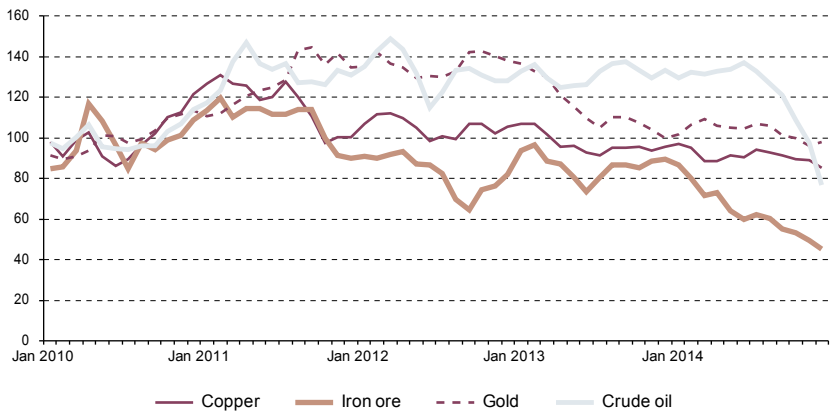
The natural resources sector consists of two components, each following a separate trend. The first is oil and gas exploration and exploitation, which is mostly conducted through State-owned enterprises in Latin America, although the industry also receives large inflows of FDI. The second is mining, which, owing in part to its more diversified product base, involves far more players, though —with the exception of CODELCO in Chile— none are large State-owned companies.

Oil and natural gas prices had been very stable from 2011 to mid-2014, when they dropped by 40%. By the fourth quarter of 2014, the fall in global oil prices led to a 12% reduction worldwide in upstream capital expenditure (EIA, 2015), which is the fastest-responding segment in the oil sector and also the segment in which the bulk of capital investment takes place. In fact, Anglo-Dutch supermajor Royal Dutch Shell announced a 40% cut in planned investments for 2015[6] and the United Kingdom's BP intends to cut its investment budget by 20% (Adams and Energy Editor, 2015). A significant decline in investment can therefore be expected in Latin America and the Caribbean in 2015 as projects are put on hold. However, the rapid decline in oil and gas prices did not have an impact on the FDI figures for 2014.

The fall in prices in the mining sector began much earlier and, by contrast with hydrocarbons, mining investments tend to have long run-up times. A global slump in mining activity was therefore foreseeable and, indeed, in 2014, all aspects of mining saw global declines. Exploration budgets dropped by 26% between 2013 and 2014, down by 47% from 2012, although Mexico and Chile are still among the top five for global exploration (SNL Metals & Mining, 2015). Far fewer global milestones, such as the opening of new mines, were reached in 2014 than at the industry's peak in 2010: 96 compared with 389.

Figure I.9 shows price movements for some key minerals, as well as crude oil. The impact of commodity cycles depends on each country's specific minerals base. Copper is the most important mineral in Latin America and has suffered the largest and most consistent slump in recent years. Chile, as the world's leading copper exporter, should expect to be hit hard by this trend. The price of gold, a major export from Chile, Mexico, Peru and Suriname, peaked between early 2011 and mid-2013, but has been stable since then. The price of iron ore, produced mostly by Brazil in this region, plummeted by 50% between January and November of 2014. Notwithstanding, the United Kingdom's Anglo American completed its first shipments of ore from the new US$ 8.8 billion Minas-Rio operation in October (Walker, 2015).

Figure I.9
Global prices for selected commodities, 2010-2014
(Index: 2010=100)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

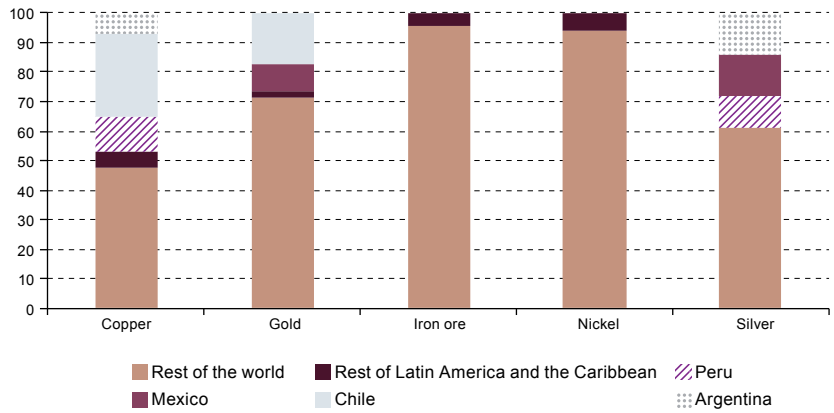
Figure I.10 shows the distribution of major mining projects —at any stage of development, from pre-feasibility to construction— around the world at the end of 2014. Latin America clearly dominates in the copper sector, with more than 50% of projects (by value) under way in the region. Chile is the largest single player, but Peru also has several large projects under development. The region is also very active in gold and silver mining, with approximately 30% and 40% of worldwide projects, respectively. By contrast, its involvement in iron ore and nickel projects is only marginal. Projects in the pipeline are an important consideration, since they will be the target of investment in the coming years.

While the manufacturing sector may have seen a small drop in its share of FDI, it continues to be very important for many economies. This is particularly the case since manufacturing investment tends to be less capital-intensive than natural resources investment and can thus create more employment per dollar invested (see chapter III of ECLAC, 2014b). Manufacturing is a sector with two different identities. On the one hand, it can be market-seeking, which is the case in large markets and for specific products, such as cement, food and beverages and others. These

[6] See BloombergBusiness (2015).

products have limited tradability and investments in such subsectors thus seek to take advantage of local markets. On the other hand, investment in export-oriented manufacturing makes use of local strengths, such as low-cost labour, to produce products for export. This type of manufacturing is particularly prevalent in Central America, Mexico and the Dominican Republic, from where many products are exported to North America. Export-oriented manufacturing tends to materialize through greenfield projects undertaken by transnational corporations, whereas market-seeking investment more often takes the form of mergers and acquisitions.

Figure I.10
Latin America and the Caribbean (selected countries) and rest of the world: distribution of major mining projects,[a] late 2014
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of on the basis of S. Walker, "Pulling back across the board", *Engineering and Mining Journal*, 16 January 2015.
[a] These figures represent the value of mining projects that are currently under way, but at different stages of development. There is no guarantee that these projects will be completed.

The automotive sector can be the recipient of either type of investment. It is a sector dominated by transnational corporations: all the assemblers in the region and the largest auto parts makers are foreign-owned. Most production takes place in Mexico and Brazil and FDI inflows into the sector in both economies have grown significantly since 2012. From 2003 to 2011, inflows into the automotive sector in the two countries combined averaged US$ 2.909 billion per year, rising to US$ 4.028 billion in 2012, US$ 5.791 billion in 2013, and a record high of US$ 8.031 billion in 2014.

Mexico's automotive plants are deeply integrated with those of the United States and Canada, its co- signatories in the North American Free Trade Agreement. Mexico exports 82% of its production, compared with only 11% for Brazil. Brazil's automotive industry is integrated with its neighbouring Southern Common Market (MERCOSUR) members. More than 57% of Brazil's automotive exports go to other MERCOSUR members. More than 80% of automotive exports from Argentina, Paraguay and Uruguay are within MERCOSUR, mostly to Brazil. Argentina is the only other MERCOSUR country to have a sizeable automotive industry (which has been growing in recent years). Uruguay exports assembled vehicles to Brazil and Paraguay has specialized in the production of tyres, exports of which have averaged US$ 17 million a year since 2009. Several companies announced new investments in Paraguay recently (in tyres and other auto parts), suggesting growth potential in the auto parts industry there in the coming years (see section D.2 for details).

For the first time in three years, services are again the largest recipient of FDI, absorbing 47% of inflows in those countries that report data disaggregated by sector. The services sector is relatively diverse, and includes financial services, business process outsourcing (BPO), electricity generation, infrastructure and tourism. Each of these receives significant FDI inflows, although the distribution differs significantly in each economy. In the Caribbean, for example, BPO and tourism are particularly important, although disaggregated data are often not available. These two sectors, which are not particularly capital-intensive, are pivotal for the Caribbean because of their capacity to create employment. Chapter II addresses the Caribbean in more detail and explores some of the key features of BPO and tourism in the subregion.

The financial services sector is not generally considered to be capital-intensive, but it is a very valuable sector and one in which many mergers and acquisitions take place. In 2014, for example, Chile's Corpbanca acquired

Helm Bank of Colombia for US$ 1.32 billion, only to be taken over itself subsequently by Brazil's Itaú Unibanco for US$ 2.2 billion. In recent years, other large takeovers have also attracted significant attention, and in general there is a trend towards consolidation in the sector. At the same time, European and North American banks have announced divestments from the region in recent years, capitalizing some of their more profitable assets.

Transport infrastructure in general does not receive much FDI, with the exception of port- and shipping-related projects and a very small number of highways, mostly in Chile. However, there appears to be a trend towards growing foreign investment in airports, as discussed at length in box I.1. Telecommunications are another area of infrastructure that receives substantial investment. In fact, the gradual roll-out of fourth-generation (4G) technology requires a large and continuous stream of investment from international telephone operators. In Brazil, telecommunications was the second largest services category in 2014, after commerce. Mexico reported a significant negative inflow to the sector in 2014, owing to a single, one-off divestment by the United States' AT&T, as discussed in more detail in section D.3. In many Central American and Caribbean economies, some of the most significant investment announcements in 2014 concerned the expansion of 4G coverage.

Lastly, electricity generation was the fourth largest services sector in Brazil, with inflows of US$ 2.291 billion. In Mexico, by contrast, inflows to the sector remained low, but a significant legislative change is likely to open up the sector to major investment in the coming years, including an announced US$ 5 billion investment by Spanish electricity giant Iberdrola. In other economies, particularly in Central America, Chile and Uruguay, it is the renewable energy sector that is at the centre of attention, with numerous new wind farms and solar plants under construction.

Box I.1

Landing investments in Latin America

Air traffic to Latin America and the Caribbean is on a solid growth path, with recent figures showing that the region has the second highest growth of any region at an annual rate of 8.2%. Although Brazil has not posted the same robust economic growth as several other economies in the region, including Chile, Colombia and Peru, in recent times, all these countries are expected to see persistently strong growth in air traffic. In the long term, Brazil is expected to rise from tenth to fifth position in the global ranking of most important airline markets. Air freight growth is somewhat slacker, but still significant.

This is reflected in the number of airport construction projects in the region: 318, according to the Centre for Aviation, in Latin America alone, which is 13.6% of all projects worldwide. In terms of capital expenditure, however, the figures for Latin America are much less impressive: only 6.3% of total expenditure is scheduled to take place in the region, for an estimated total of US$ 34.2 billion. This implies that the projects taking place in Latin America are relatively small-scale. The region's share in new airports is 12.7%, ahead of the Middle East (6.9%) and North America (2.4%).

Airports are an important category of infrastructure, since they require large investments and support other types of FDI and development. Furthermore, airport infrastructure projects receive a relatively larger share of foreign investment than other infrastructure projects. Traditionally, airports were run by the State, but the past 20 years have seen privatizations and the introduction of public-private partnerships and other forms of shared ownership. One common practice is to award concessions lasting several decades to private operators. However, the situation differs significantly between countries. For example, in Mexico most airports are managed by one of three large government-owned corporations: Aeropuertos y Servicios Auxiliares (ASA), with 19 airports; Grupo Aeroportuario del Pacífico (GAP), with 12 airports; and Aeropuertos del Sureste (ASUR), with 9 airports. In Brazil, the largest airports are run by consortiums of domestic and foreign companies.

Brazil has seen a wave of investment in airports owing to the 2014 World Cup and the 2016 Olympic Games. The State operator Infraero has awarded concessions to consortiums for some of the country's largest airports, while maintaining a minority stake in each of the concessions. Inframérica, which includes Argentina's Corporación América as one of the two consortium members, has maintained and operated Brasilia international airport since 2012 on a 25-year concession that included significant upgrades before the World Cup. The same consortium also built and now operates the new airport at Natal, the only airport in Brazil in which Infraero does not have a stake in the concession. São Paulo's Guarulhos Airport was reopened in 2014 after a US$ 1.3 billion upgrade by its operators, consisting of South Africa's Airports Company South Africa (ACSA) and a local investment fund. Belo Horizonte's 30-year concession was awarded in 2014 to a consortium that includes the operators of the international airports of Zürich and Munich, which has pledged to invest US$ 660 million. Finally, Rio de Janeiro's airport is operated by Brazil's Odebrecht and Singapore's Changi Airport, which will invest a further US$ 888 million before the start of the Olympic Games in 2016.

While Brazil is the dominant air market in Latin America, other countries also receive significant investment in their airports. Bogota's El Dorado Airport is the third busiest in Latin America (after São Paulo Guarulhos and Mexico City International Airport) and is currently undergoing a US$ 1.26 billion reconstruction scheduled for completion in 2016. El Dorado is operated by a consortium consisting of several local firms and Switzerland's Flughafen Zürich. Lima's Jorge Chávez International Airport is currently in the first phase of a US$ 1 billion expansion plan to be completed by 2030. The consortium operating the airport is led by Germany's Fraport (70%), together with the International Finance Corporation (20%) and a local investment fund (10%). Finally, the concession for the international airport of Santiago was awarded in early 2015 to a consortium consisting of France's Aéroports de Paris (45%), France's VINCI Airports (40%) and Italy's Astaldi (15%). Investments of approximately US$ 700 million are planned by 2030 to triple the airport's capacity. The table below shows some of the largest investments in airports currently under way.

Box I.1 (concluded)

Latin America: major airport expansions

City and country	Estimated cost *(millions of dollars)*	Current capacity *(millions of persons)*	Future capacity *(millions of persons)*	Planned completion date
Belo Horizonte, Brazil	666	10	20	2016
Rio de Janeiro, Brazil	888	17.5	30	2016
Santiago, Chile	700	9.5	29	2030
Bogota, Colombia	1 260	14	20	2016
Punta Cana, Dominican Republic	100	5	10	2015
San Salvador, El Salvador	490	1.6	6.6	2032
Cancún, Mexico	750	15	25	2016
Mexico City, Mexico [a]	321	32	n/a	2018
Panama City, Panama	840	9	18	2026
Asunción, Paraguay	264	1.2	2	2017
Chiclayo, Peru	128	...	...	2015
Lima, Peru	1 000	10	...	2030
Piura, Peru	231	...	...	2023
Barquisimeto, Bolivarian Republic of Venezuela	413	...	...	2015

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on basis of Centre for Aviation, "Latin America airport construction and investment activity continues - but Brazil slows" [online] http://centreforaviation.com/analysis/latin-america-airport-construction-and-investment-activity-continues--but-brazil-slows-193981.

[a] Excludes the planned US$ 13 billion outlay for a new airport in Mexico City.

Not all the investments in the table above are funded through FDI, but many of the airports in question are operated by transnational consortiums. Taking into account the projected rate of growth in Latin American air traffic, the sector can expect to see further international investment, but only if governments are willing to relinquish control of national airports. Airports are strategic assets and cooperation between the private and public sectors can help to boost FDI in airport infrastructure.

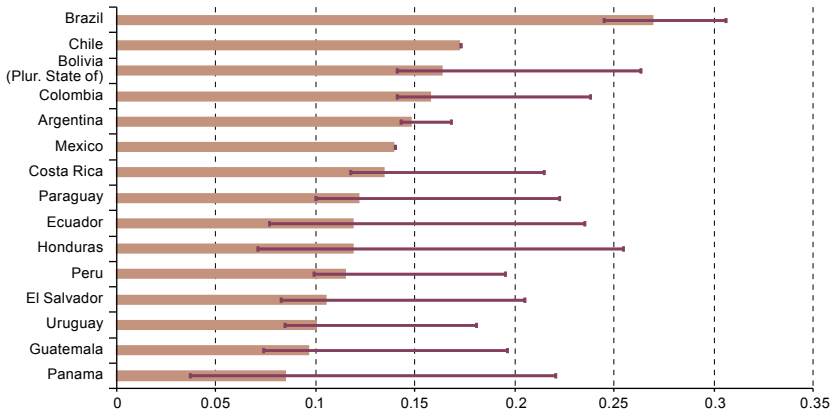
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on basis of Centre for Aviation, "Latin America airport construction and investment activity continues - but Brazil slows" [online] http://centreforaviation.com/analysis/latin-america-airport-construction-and-investment-activity-continues--but-brazil-slows-193981.

3. Technology intensity of investment

The structure of the region's economies varies greatly in terms of relative intensities of capital and labour. This structure is largely the result of fortune and past economic policies. For example, countries that are rich in natural resources are more likely to be capital-intensive than countries whose focus is on services. The respective growth rates relating to labour and physical capital thus partly determine the growth rate of an economy. However, another factor that drives economic growth is the capacity to improve productivity, primarily through innovation. The different elements that contribute to the capacity to innovate can be measured and expressed as a share of GDP, as for physical capital. This measure is referred to as innovation capital and by this indicator Latin America lags significantly behind many Organization for Economic Cooperation and Development (OECD) countries.

Figure I.11 shows estimated innovation capital as a share of GDP for selected countries in Latin America. Due to limitations in data availability, it is not always possible to estimate the exact figures for each economy and upper and lower bounds for each country are therefore indicated. Brazil is far ahead of the other economies with respect to capacity to innovate, while Panama has the lowest level of innovation capital. The factors used to measure innovation capital include investments in software and hardware, expenditure on research and development, expenditure on tertiary education and other forms of training, and number of patents filed. Even though the data are standardized by economy size, larger economies tend to have more innovation capital. The figure also shows that Central American countries have relatively low levels of innovation capital compared with South American countries.

Figure I.11
Latin America (selected economies): estimated innovation capital as a share of GDP, 2010
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of O. de Groot, "Innovation capital in Latin America: A first attempt at analyzing the region's competitive strengths in innovative capacity", Santiago, Chile, ECLAC, 2014, unpublished.

Note: The bars indicate point estimates for the size of innovation capital, while the whiskers indicate the uncertainty of the estimation, providing a lower and upper bound of the estimates.

Just as an abundance of natural resources can attract investment in natural resources, an abundance of innovation capital can help attract investment in high-technology sectors. A wealth of innovation capital is, in fact, one of the factors that contributes to the potential productivity of high-technology investment. This relationship can be investigated by looking at the technology intensity of announced investment projects as recorded by the Crossborder Investment Monitor (fDi Markets) published by the Financial Times.[7]

Figure I.12 shows the technology intensity of FDI for selected Latin American economies. Medium-high- and high-technology investments make up a large share of announcements in both Brazil and Mexico. The automotive sector captures a large share of these inflows, primarily in these two countries (see boxes I.2 and I.4 of ECLAC, 2014b). At the other extreme, medium-high- and high-technology investments account for less than 40% of the value of investments announced in Colombia, Panama and Peru. This difference has to do with the structure of the economies —for example, the Panamanian economy is very services-centred— and it has implications for the impact of FDI. Aside from Brazil and, to a more limited extent, Mexico, single investments can have a large impact on the total figures since the number of projects per country is limited.

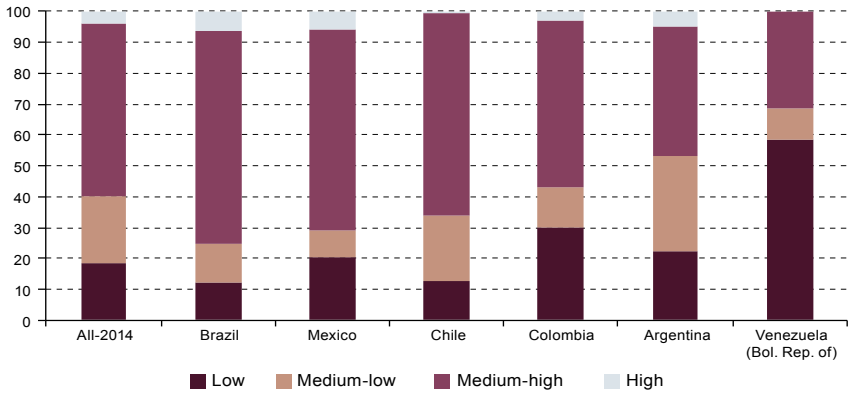
The new Audi plant in Puebla, Mexico, illustrates the impact that more technology-intensive FDI can have. Following the inauguration of a new, highly advanced plant some years ago, Germany's Volkswagen Group, which owns the Audi brand, worked together with the local government and a local university to create a new training centre to be completed in 2015. Since the plant employs some of the most advanced production techniques used within the multinational enterprise, it was decided to build a training centre in order to ensure that the staff would be qualified to use the most up-to-date new technologies. Furthermore, in order to optimize efficiency, producers of intermediate suppliers are also trained at the centre. As a result, Audi's incorporation into the production structure will help raise the skill level of a large share of workers in the region. In addition to the Volkswagen Group, the project also involves another German company, Siemens, which produces some of the electronics for Audi vehicles.

Lastly, figure I.13 shows the technology intensity of investment projects in the region as a share of the total value of all investment announcements for different time periods. This figure again highlights that there are very few high-technology investments in Latin America, with the share holding steady at around 4% of the total value of announced investments from 2008 to 2014, according to fDi Markets. However, an encouraging pattern can be seen in the growing prevalence of medium-high-technology projects, whose share rose from 38% in 2008-2010 to nearly 56% in 2014.

[7] fDi Markets is a database of investment announcements, and there is therefore no certainty that the announced projects will be completed. Analysts from fDi Markets estimate the costs of investment projects when these are not published, which is both a strength and a weakness of this database. It is a strength since it makes the database significantly more comprehensive than it would otherwise be. It is also a weakness since the estimates are occasionally unrealistic. The database categorizes each project under one of 53 sectors and one of 18 activities, with each of these combinations classified by technology intensity.

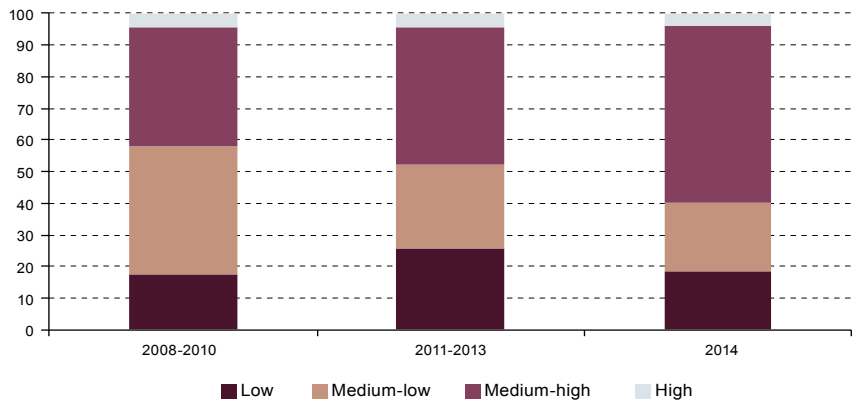
The especially large share recorded in 2014 is attributable to the great number of announcements in the automotive sector, particularly in Mexico. Such a large number of announcements in a single year is somewhat uncommon and 2015 may be expected to bring a return to the lower average of previous years. The share of medium-low-technology investment projects has dropped from 40% in 2008-2010 to 21% in 2014, owing largely to reduced investment in some heavy industries in certain large countries. Finally, the low-technology category displays no clear trend, varying between 18% and 26% in the periods covered by the figure.

Figure I.12
Latin America (selected economies): technology intensity of announced investments, 2011-2014
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of Financial Times, fDi Markets.

Figure I.13
Latin America and the Caribbean: technology intensity of announced investments, 2008-2010, 2011-2013 and 2014
(Percentages)



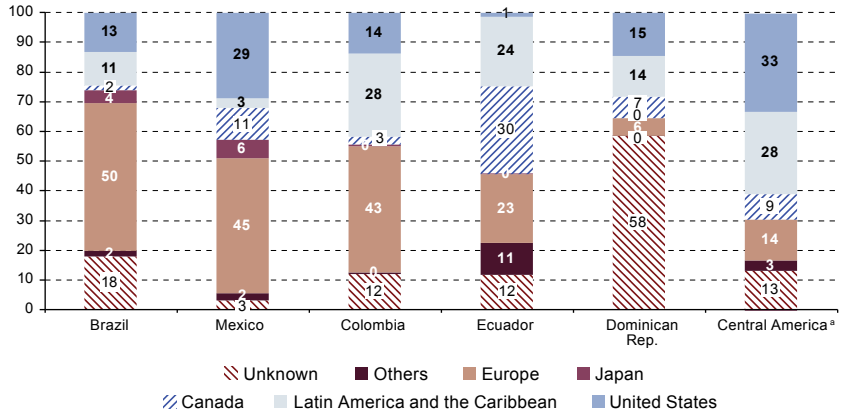
Source: Economic Commission for Latin America and the Caribbean (ECLAC) on basis of Financial Times, fDi Markets.

4. Largest investor countries

The Netherlands has now become the largest single investor in Latin America and the Caribbean, accounting for 20% of all attributable[8] inflows, up from 14% in 2013. The share of the United States in FDI inflows, meanwhile, fell to 17%, down from 20% in 2013 and 25% in 2012. Naturally, this hides a large degree of intraregional variation. In Mexico, for example, the United States regained its position as top investor despite its share slipping from 30% to 29%. In 2013, it had lost its top position to Belgium, owing to the takeover of Grupo Modelo by Belgium's Anheuser-Busch Inbev. In Brazil, the United States' share of investment shrank to 13%, making the country the second largest investor after the Netherlands at 29% (see figure I.14).

[8] Not all countries provide a disaggregation of FDI inflows by country of origin. Data in this section is based on those countries included in figure I.14

Figure I.14
Latin America (selected countries and subregions): origin of foreign direct investment, 2014
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and estimates as of 18 May 2015.
[a] Central America includes Costa Rica, El Salvador, Guatemala and Honduras.

The dominant position of the Netherlands reflects its prominence in the Brazilian market, whereas in other countries, it plays a much smaller role. Instead, Spain, which nearly quadrupled its share to 10% in 2014, is the largest European investor in other economies. In Mexico and Colombia, Spain is responsible for approximately 18% and 13% of inflows, respectively. Two of the largest M&As in 2014 were carried out by Spanish companies: Gas Natural Fenosa acquired 54% of Chile's Compañía General de Electricidad for US$ 3.3 billion and Banco Santander expanded its share in Banco Santander Brasil by 14% for US$ 3.199 billion (see table I.2). The third large European investor, with 8% of total inflows, is Luxembourg, which is also particularly important in Brazil (10% of inflows). Not typically renowned as economic powerhouses, the Netherlands and Luxembourg act as conduits for investment from other countries. Ideally, these investment flows should be attributed to their original source countries, but this is not always possible. The data available therefore show that these two countries, and Ireland to a lesser extent, continue to play a large role.

FDI from Asia increased in 2014, although this FDI cannot always be tracked easily or directly because some countries in Latin America and the Caribbean do not keep records on the origin of investment. For example, table I.2 shows that three of the largest M&As in 2014 were completed by Chinese companies, including the largest acquisition recorded during the year. However, two of these took place in Peru, whose central bank does not track the origin of investment. This leads to a significant underestimation of China's role in FDI in Latin America and the Caribbean. ECLAC estimates that the region received FDI inflows of US$ 10 billion per year from China between 2010 and 2013. This figure was probably even higher in 2014 in view of the aforementioned acquisitions. Overall, FDI from Asia increased from 5% to 6%, with China's share in recorded inflows to Latin America and the Caribbean increasing to 1% (see annex table I.A.3).

Table I.2
Latin America and the Caribbean: 20 largest mergers or acquisitions, 2014

	Company	Country of origin	Assets acquired	Asset location	Seller location	Sector	Amount *(millions of dollars)*
1	MMG Limited and partners	China	Glencore Las Bambas copper deposit	Peru	Switzerland	Mining	7 005
2	Royal Dutch Shell	Netherlands and United Kingdom	Repsol liquefied natural gas (LNG) portfolio	Peru, Trinidad and Tobago, Spain	Spain	Oil	4 100
3	Gas Natural Fenosa	Spain	Compañía General de Electricidad (54%)	Chile	Chile	Electricity	3 300
4	Banco Santander	Spain	Banco Santander Brasil (14%)	Brazil	Brazil	Finance	3 199
5	China National Petroleum Corporation (CNPC)	China	Petrobras Energía Perú	Peru	Brazil	Oil	2 600
6	PPG Industries	United States	Consorcio Comex	Mexico	Mexico	Manufacturing	2 300
7	Lundin Mining Corporation	Canada	Candelaria and Ojos del Salado mines (80%)	Chile	United States	Mining	1 800

Table I.2 (concluded)

	Company	Country of origin	Assets acquired	Asset location	Seller location	Sector	Amount (millions of dollars)
8	Global Logistics Properties	Singapore	34 industrial properties	Brazil	Brazil	Real estate	1 368
9	Corpbanca	Chile	Helm Bank	Colombia	Colombia	Banking	1 320
10	Millicom	Sweden	Telecommunications business of EPM (50%)	Colombia	Colombia	Telecommunications	1 300
11	Eutelsat Communications	France	Satélites Mexicanos	Mexico	Mexico	Telecommunications	1 142
12	American Tower Corporation	United States	BR Towers	Brazil	Brazil	Telecommunications	1 012
13	Mubadala Development and Trafigura Beheer	United Arab Emirates and the Netherlands	MMX Porto Sudeste de Brasil (65%)	Brazil	Brazil	Infrastructure	971
14	Brookfield Asset Management	United States	VLI (27%)	Brazil	Brazil	Transport	845
15	Celsia	Colombia	Seven power plants	Costa Rica and Panama	France	Electricity	840
16	Pearson	United Kingdom	Grupo Multi	Brazil	Brazil	Education	829
17	Mitsui & Co.	Japan	Jirau hydropower plant (20%)	Brazil	France	Electricity	750
18	Partners Group	Switzerland	Fermaca	Mexico	United States	Infrastructure	750
19	Alliance Boots (Walgreens and KKR)	United States	Farmacias Ahumada	Chile and Mexico	Mexico	Commerce	740
20	China Construction Bank	China	Banco Industrial e Comercial (72%)	Brazil	Brazil	Banking	725

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by Bloomberg.

Table I.3 shows that there were also several major divestments in 2014, which may be defined as acquisitions by national companies of assets held by foreign investors. The largest of these took place in Argentina. In 2012, the Government of Argentina introduced legislation to partially renationalize YPF, which was owned by Spain's Repsol. The compensation was decided only in 2014, with the Government of Argentina paying US$ 5 billion for Repsol's 51% share. Repsol later sold a further 12% for US$ 1.311 billion. The second largest divestment came from the United States' AT&T, which sold its share in América Móvil to Inmobiliaria Carso. More details about this transaction can be found in section D.3. Other divestments took place in several other countries, including Brazil, Colombia and Mexico.

Table I.3
Latin America and the Caribbean: 10 largest divestments, 2014

	Selling company	Seller location	Assets divested	Buyer	Country	Sector	Amount (millions of dollars)
1	Repsol	Spain	YPF (63%)	Government of Argentina	Argentina	Oil	6 311
2	AT&T	United States	América Móvil (8%)	Inmobiliaria Carso	Mexico	Telecommunications	5 570
3	TRG Management	United States	Transportadora de Gas Internacional (32%)	Empresa de Energía de Bogotá	Colombia	Infrastructure	880
4	Apache	United States	All local assets	YPF	Argentina	Gas	852
5	Carrefour	France	Carrefour Brazil (10%)	Península Participações	Brazil	Commerce	678
6	Newmont	United States	Penmont gold mine (44%)	Fresnillo	Mexico	Mining	450
7	BP	United Kingdom	Polvo oil field (60%)	HRT Participações em Petróleo	Brazil	Oil	135
8	Iberdrola	Spain	Itapebi Geração de Energia (23%)	Neoenergia	Brazil	Electricity	134
9	Prudential Financial	United States	Centro Bancomer	Fibra Uno Administración	Mexico	Real estate	125
10	Petrobras	Brazil	Transierra (45%)	Yacimientos Petrolíferos Fiscales Bolivianos (YPBF)	Plurinational State of Bolivia	Infrastructure	107

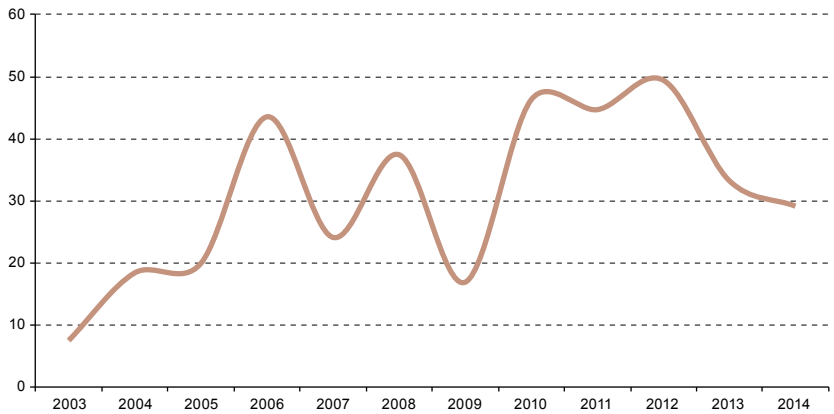
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by Bloomberg.

C. Outward foreign direct investment

FDI outflows from Latin America and Caribbean countries fell substantially for the second year in a row to US$ 29.162 billion in 2014, down by 12% with respect to 2013. These flows averaged US$ 46.800 billion per year between 2010 and 2012 and have fallen by a cumulative 42% to the current level. FDI outflows have always been volatile because they are concentrated in a handful of countries and a limited number of large trans-Latin corporations, making them very sensitive to individual acquisitions or large projects (see figure I.15 and annex table I.A.6).

The drop in 2013 and 2014 can be explained by the same factors that have eroded FDI inflows. Since most outward investment from Latin American and Caribbean economies remains within the region, any worsening of investment prospects in the region also affects FDI outflows. Furthermore, many of the largest trans-Latin corporations are in the extractive industries, which are reducing capital investment in response to lower commodity prices.

Figure I.15
Latin America and the Caribbean: outflows of foreign direct investment, 2003-2014
(Billions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC) on basis of official figures and estimations as of 18 May 2015.

Traditionally, most of the largest trans-Latin corporations come from just four countries: Brazil, Chile, Colombia and Mexico. These four countries account for 90% of total outflows from the region over the previous decade (see table I.4). The drop in outflows in 2014 was concentrated in Colombia and Mexico. In Colombia, the bulk of outflows are invested in the extractive industries (46% of total), followed by manufacturing (21%). Unfortunately, comparable data for Chile and Mexico are not available.

Table I.4
Latin America and the Caribbean (selected economies): outward foreign direct investment, 2000-2014
(Millions of dollars)

	2000-2005 [a]	2006	2007	2008	2009	2010	2011	2012	2013	2014
Argentina	533	2 439	1 504	1 391	712	965	1 488	1 055	1 097	2 117
Brazil	2 513	28 202	7 067	20 457	-10 084	11 588	-1 029	-2 821	-3 495	-3 540
Chile	1 988	2 212	4 852	9 151	7 233	9 461	20 252	20 555	10 308	12 052
Colombia	1 187	1 268	1 279	3 085	3 505	5 483	8 420	-606	7 652	3 899
Mexico	2 909	5 758	8 256	1 157	9 604	15 050	12 636	22 470	13 138	7 610
Venezuela (Bolivarian Republic of)	809	1 524	-495	1 311	2 630	2 492	-370	4 294	752	1 024
Latin America and the Caribbean	**10 632**	**43 447**	**24 134**	**37 440**	**16 911**	**46 276**	**44 686**	**49 439**	**33 251**	**29 162**

Source: Economic Commission for Latin America and the Caribbean (ECLAC) on the basis of official figures and estimate as of 18 May 2015.
[a] Simple averages.

Brazil has the largest stock of FDI abroad in the region, but for the fourth year running it reported negative FDI outflows in 2014 according to the methodology of the fifth edition of the IMF *Balance of Payments Manual*.[9] This does not mean that Brazilian companies are abandoning their investments abroad. Indeed, in 2014 Brazilian companies invested US$ 19.556 billion in capital contributions, which is the highest figure since 2011, but received US$ 23.096 billion in net loans from subsidiaries abroad. The result is a negative inflow of US$ 3.540 billion, similar to last year's figure. New investments in 2014 primarily targeted the financial services sector and telecommunications.

In 2014 Peru became the third largest investor country, behind Chile and Mexico, with outflows of US$ 4.452 billion. Some of the largest Peruvian companies have been investing abroad since 2006, benefiting from strong economic growth in their domestic market, macroeconomic stability and better access to finance (Peru acquired investment grade status in 2008). From 2006 to 2013 outflows averaged only US$ 1.4 billion a year, but several large acquisitions and projects in 2014 drove up outflows to a record high.

There is no official data on the sectoral distribution of FDI outflows from Peru, but the largest companies are chiefly in mining and food manufacturing. Hochschild Mining specializes in underground mining for silver and gold and has subsidiaries in Argentina, Mexico and Chile, where it has recently acquired a project that will require investments of around US$ 1 billion. Another large mining transnational is Minsur, part of Grupo Breca, which specializes in tin mining. Its largest operation outside Peru is Mineração Taboca in Brazil. In food manufacturing the largest companies are Aje, Gloria and Alicorp, which have a presence in many Latin American markets. In 2014 there were two large cement acquisitions: UNACEM bought a plant in Ecuador for US$ 517 million and Grupo Gloria bought a plant in the Plurinational State of Bolivia for US$ 300 million. Peruvian companies follow a similar strategy to their counterparts in Colombia or Chile of seeking out markets in neighbouring countries.

Outflows from Argentina surged to US$ 2.117 billion, double the amount of the previous year; and outflows from the Bolivarian Republic of Venezuela totalled US$ 1.024 billion. The State-owned Petróleos de Venezuela, S.A. (PDVSA), the largest company in the Bolivarian Republic of Venezuela, was rumoured to be looking for a buyer for its subsidiary in the United States, which operates three refineries with a capacity of 750,000 barrels per day (bpd). The transaction, should it occur, would be worth several billion dollars.

FDI outflows from other economies are much more modest, although this is largely due to underreporting: almost half of the economies in the region do not report on outward FDI and many who do fail to record substantial flows. Official figures from Central American countries are particularly low, with the partial exception of Costa Rica which registered outflows of US$ 218 million in 2014. Still, there is evidence that some companies are expanding considerably in other countries, generally within Central America (see box I.2). In 2014, Promerica Financial Corporation from Panama bought a majority share in Banco de la Producción in Ecuador for US$ 130 million. In early 2015, Banco Ficohsa of Honduras acquired the assets of Citibank in Guatemala, having acquired its Honduran assets in 2014. Chapter II contains a more detailed analysis of outward FDI from the Caribbean economies.

Box I.2
Central American trans-Latins

Between 2011 and 2013, investment by transnational corporations in Central American countries outside their home country represented only 1% of total Latin American and Caribbean investment abroad. However these investments are growing and are important for the subregion's economies.

According to information provided by fDi Markets and Thomson Reuters (see Padilla and Gomes, 2015), Central American companies made 271 foreign investments between 2003 and 2013. Panama, Costa Rica and El Salvador were the main investor countries and the largest number of transactions were recorded in business and financial services, the wholesale sector and food and beverages.

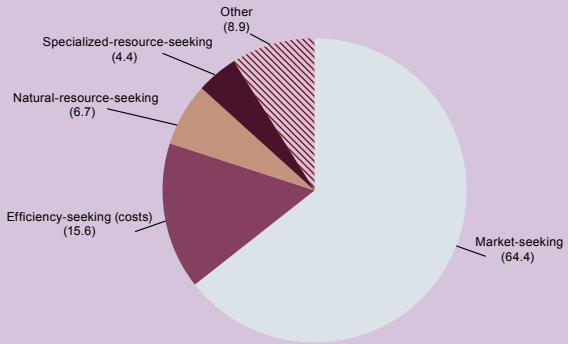
Interviews conducted in the context of a case study with representatives of a significant sample of transnational corporations in Costa Rica found the following:

(i) Two thirds of investments are primarily market-seeking, with a view to expanding operations and taking advantage of economies of scale or to establishing a regional presence (see figure).
(ii) Although large and medium-sized enterprises predominate (70% of Costa Rican transnationals have more than 51 employees), there is also scope for the participation of small businesses and even micro-enterprises.
(iii) In some economic activities, such as logistics and business services, internationalization is a necessity: large clients see Central America as a single market and expect services at the subregional level, which requires investment and a physical presence in different countries.
(iv) Costa Rican trans-Latins are highly concentrated in the countries of the subregion: two thirds operate exclusively in other Central American countries and only 22% of the companies surveyed had invested outside Latin America (typically in the United States, Europe or Asia).

[9] Under the methodology prescribed in the six edition of the IMF Balance of Payments Manual, Brazil's outward foreign direct investment in 2014 is actually US$ 25.736 billion, primarily owing to a large change in the way intercompany lending is accounted for.

Box I.2 (concluded)

Costa Rica: distribution of companies by main foreign investment strategy
(Percentages)



Source: R. Padilla and C. Gomes, "Determinants and home-country effects of FDI outflows in Latin America", Mexico City, ECLAC subregional headquarters in Mexico, 2015, unpublished.

The Costa Rica case study also sought to identify the main consequences of businesses internationalizing in a small economy. The quantitative effects include the creation of new jobs, more activities with a higher technology content and greater productivity, while the qualitative effects include technology transfer and improved goods and services.

Source: R. Padilla and C. Gomes, "Determinants and home-country effects of FDI outflows in Latin America", Mexico City, ECLAC subregional headquarters in Mexico, 2015, unpublished.

The two largest corporate acquisitions by Latin American companies in 2014 were in the telecommunications sector. Oi from Brazil carried out its announced merger with Portugal Telecom (valued at US$ 8.056 billion) and América Móvil increased its stake in Telekom Austria for US$ 6.110 billion (see table I.5).

Table I.5
Latin America and the Caribbean: 15 largest cross-border acquisitions by trans-Latins, 2014

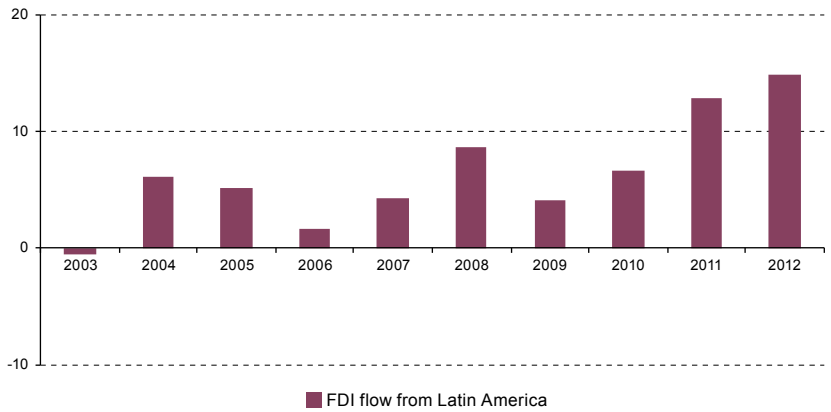
	Company	Country of origin	Assets acquired	Asset location	Seller location	Sector	Amount *(millions of dollars)*
1	Oi	Brazil	Portugal Telecom	Portugal	Portugal	Telecommunications	8 056
2	América Móvil	Mexico	Telekom Austria (33%)	Austria and elsewhere	Austria	Telecommunications	6 110
3	Grupo Bimbo	Mexico	Canada Bread	Canada	Canada	Food and beverages	1 497
4	Corpbanca	Chile	Helm Bank	Colombia	Colombia	Banking	1 320
5	Celsia	Colombia	Seven power plants	Costa Rica and Panama	France	Electricity	840
6	Cementos Argos	Colombia	Cement and concrete businesses in Florida	United States	United States	Cement	720
7	Falabella	Chile	Maestro	Peru	Peru	Retail	712
8	Mexichem	Mexico	Dura-Line	United States	United States	Chemicals	630
9	Alsea	Mexico	Food Service Project (72%)	Spain	Great Britain	Real estate	298
10	Mexichem	Mexico	Vestolit	Germany	United States	Chemicals	293
11	COPEC	Chile	Proenergia Internacional	Colombia	Colombia	Retail	287
12	Finaccess	Mexico	IBM Headquarters	Spain	United States	Real estate	189
13	SONDA	Chile	CTIS Tecnologia	Brazil	Brazil	Information technology	169
14	Alfa	Mexico	Campofrio (19%)	Spain	Spain	Food and beverages	167
15	Promerica Financial Corporation	Panama	Banco de la Producción (56%)	Ecuador	Ecuador	Banking	130

Source: Economic Commission for Latin America and the Caribbean (ECLAC) on basis of Financial Times, fDi Markets.

Outward direct investments by companies in Latin America and the Caribbean are still largely concentrated within the region, but as companies grow and develop a significant number of them are starting to invest in other regions. Most of the largest trans-Latin companies from Mexico invest in the United States, as do some of the largest corporations from Brazil and Colombia. In recent years many companies have also been increasing their investments in Europe. According to data from the European countries, FDI from Latin American countries has increased notably since 2009 (see figure I.16), reflecting the more readily available financial resources of Latin American companies relative to their European counterparts. The first reflection of this shift was the divestment by European companies of valuable assets in Latin America in order to improve cash flows, but as the situation develops Latin American companies are also entering the European market. Investment by trans-Latin corporations in other developing regions remains rare.

Figure I.16 shows the nearly continuous increase of FDI inflows into European Union member States. Only between 2008 and 2009 was there a significant drop in inflows from Latin America, but this was consistent with the downturn in global flows. Since 2003, approximately 31% of the incoming investment from Latin America went to Spain, while Belgium and Luxemburg accounted for another 25% and 15%, respectively. The most important remitting countries are Brazil and Mexico, although this differs significantly between host economies.

Figure I.16
European Union: [a] foreign direct investment inflows from Latin America and the Caribbean, 2003-2012
(Billions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of data from the Organization for Economic Cooperation and Development (OECD).
[a] Data are unavailable for Bulgaria, Croatia, Cyprus, Latvia, Lithuania and Romania.

D. Foreign direct investment inflows by country

In Latin America, as in the Caribbean, just over half of all countries saw decreases in their inflows of FDI, while the rest experienced increases of varying degrees. The largest increases occurred in El Salvador, and Chile, while the sharpest contractions took place in the Bolivarian Republic of Venezuela, Mexico and Argentina. These two sets of countries epitomize the cyclical nature of FDI, with two of the three main risers belonging to last year's largest fallers, and this year's sharpest fallers making up last year's fastest risers. In other words, at the country level, extreme swings are common and often counteracted immediately. Table I.6 shows total FDI inflows by country and by subregion from 2004 to 2014.

Brazil's share in total FDI inflows increased to 38%,[10] somewhat above the long-run average of one third. Mexico and Chile ranked second and third, with approximately 14% each. FDI inflows in Latin America and the Caribbean were even more concentrated than in 2013, with just five economies receiving some 80% of total FDI in 2014. That top five include Colombia, which continues to receive large amounts of FDI, and Peru, where FDI inflows have dropped off somewhat from previously high levels.

[10] Under the methodology of the sixth edition of the *Balance of Payments Manual*, Brazil's share is even larger: approximately half of total inflows for the region.

Table I.6
Latin America and the Caribbean: foreign direct investment inflows by receiving country and subregion, 2004-2014
(Millions of dollars and variation in percentages)

	2004-2007 [a]	2008	2009	2010	2011	2012	2013	2014	Absolute variation 2013-2014 *(amount)*	Relative variation 2013-2014 *(percentages)*
South America	**50 074**	**95 388**	**59 194**	**95 113**	**133 487**	**146 901**	**128 322**	**119 502**	**-8 821**	**-7**
Argentina	5 350	9 726	4 017	11 333	10 840	15 324	11 301	6 612	-4 689	-41
Bolivia (Plurinational State of)	111	513	423	643	859	1 060	1 750	648	-1 102	-63
Brazil	21 655	45 058	25 949	48 506	66 660	65 272	63 996	62 495 [b]	-1 501	-2
Chile	9 174	16 604	13 392	15 510	23 309	28 457	19 264	22 002	2 738	14
Colombia	7 247	10 565	8 035	6 430	14 648	15 039	16 199	16 054	-146	-1
Ecuador	449	1 058	308	163	644	585	731	774	43	6
Paraguay	95	209	95	210	619	738	72	236	165	230
Peru	3 284	6 924	6 431	8 455	7 665	11 918	9 298	7 607	-1 691	-18
Uruguay	1 001	2 106	1 529	2 289	2 504	2 536	3 032	2 755	-277	-9
Venezuela (Bolivarian Republic of)	1 713	2 627	-983	1 574	5 740	5 973	2 680	320	-2 360	-88
Mexico	**25 734**	**28 574**	**17 644**	**25 962**	**23 560**	**18 998**	**44 627**	**22 795**	**-21 832**	**-49**
Central America	**4 891**	**7 406**	**4 442**	**5 863**	**8 504**	**8 864**	**10 680**	**10 480**	**-200**	**-2**
Costa Rica	1 255	2 078	1 347	1 466	2 176	2 332	2 677	2 106	-571	-21
El Salvador	547	539	294	-230	218	482	140	275	96	53
Guatemala	535	754	600	806	1 026	1 244	1 295	1 396	100	8
Honduras	686	1 006	509	969	1 014	1 059	1 060	1 144	84	8
Nicaragua	290	627	434	490	936	768	816	840	25	3
Panama	1 578	2 402	1 259	2 363	3 132	2 980	4 654	4,719	65	1
The Caribbean [c]	**4 818**	**9 616**	**5 281**	**4 809**	**6 637**	**8 284**	**6 322**	**6 027**	**-296**	**-5**
Total	**85 517**	**140 984**	**86 561**	**131 746**	**172 190**	**183 047**	**189 951**	**158 803**	**-31 149**	**-16.40**

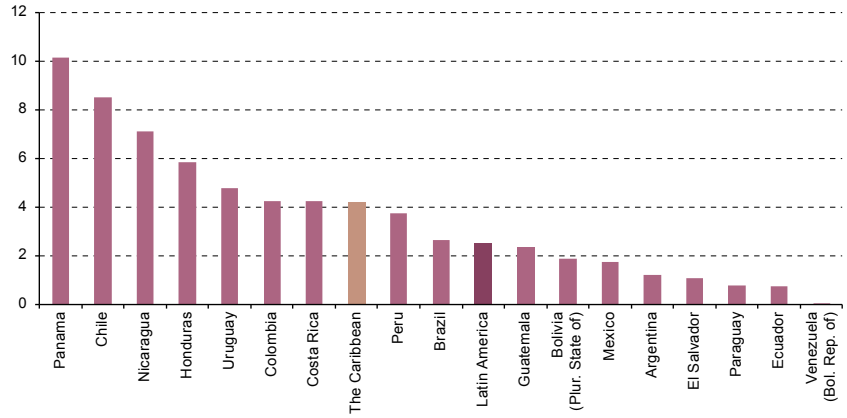
Source: Economic Commission for Latin America and the Caribbean, on the basis of official figures and estimates as of 18 May 2015.
[a] Simple averages.
[b] The 2014 figure for Brazil is calculated according to the methodology of the fifth edition of the IMF Balance of Payments Manual for purposes of comparison. Under the methodology of the sixth edition, which Brazil has recently adopted, the country recorded FDI flows of US$ 96.851 billion.
[c] See chapter II for FDI inflows from the Caribbean are disaggregated by country and discussed in more detail in chapter II.

Relative to the size of their economies, smaller economies tend to receive proportionally more FDI, which confers a particularly important role on transnational corporations. FDI inflows are equivalent to as much as 10% of GDP in Panama, Chile and Nicaragua (see figure I.17). Individual, one-off transactions can have a huge impact on inflows in different economies, particularly smaller ones. The effects are more marked for mergers and acquisitions than for greenfield investments since M&As tend to take place at a single point in time, whereas large greenfield investments are more likely to span several years. Caribbean economies have high FDI-to-GDP ratios on average, and are reviewed separately in chapter II.

1. Brazil

As noted earlier, the central bank of **Brazil** changed its data collection method recently from the fifth to the sixth edition of the IMF *Balance of Payments Manual*. The most important change this has entailed is that approximately US$ 24 billion of intercompany lending that was previously considered a negative outflow has been reclassified as a positive inflow, increasing both net inflows and net outflows by that amount. Second, the inclusion of reinvested earnings, which Brazil did not previously treat as FDI, increases its incoming FDI by a further US$ 10.698 billion and its outgoing FDI by US$ 6.010 billion. Other changes have only a small impact. Unfortunately, so far, the data calculated under the sixth edition methodology is available only for 2014, which precludes long-term comparisons with preceding years. To accommodate comparisons over time, so far this chapter has used the data according to the fifth edition. According to those data, FDI inflows into Brazil slipped to US$ 62.495 billion in 2014, down by 2% on the previous year and lower still than the totals for 2012 and 2011. Under the sixth edition definition, however, Brazil received US$ 96.851 billion in 2014, which implies that Brazil actually received approximately half of all inflows into the region as a whole.

Figure I.17
Latin America and the Caribbean: foreign direct investment as a proportion of GDP, 2014
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and estimates as of 18 May 2015.

Economic growth slowed from 2.5% in 2013 to 0.1% in 2014, but FDI inflows were affected little, reflecting the long-term confidence of foreign investors. Still, the slowdown did cause FDI income (the profits made by transnational corporations in the country) to fall to US$ 25.105 billion, down 9% on 2013, according to the fifth edition methodology. Under the newer methodology, FDI income reached US$ 35.803 billion, but again, there is no comparable number available for the preceding years. The drop in profits was especially heavy in the automotive sector, which has traditionally been among the most profitable for foreign companies. FDI income in this sector alone plummeted from US$ 3.29 billion in 2013 to only US$ 884 million in 2014, reflecting declines in vehicle registrations (7%), production (15%) and exports (40%). This contraction was due mainly to more restricted access to credit and lower demand in Argentina, the sector's leading export market. The National Association of Motor Vehicle Manufacturers of Brazil (ANFAVEA) expects a similar performance in 2015.

Despite these troubles, the automotive sector received FDI inflows worth US$ 4.221 billion in 2014,[11] a new record high, as most auto assemblers went ahead with the expansion plans announced in previous years (see box I.2 of ECLAC, 2014b). In manufacturing, the coke, oil derivatives and biofuels sector was the largest recipient of FDI with inflows worth US$ 17.278 billion. Other major manufacturing sectors include steel (US$ 4.692 billion) and chemical products (US$ 3.916 billion).

In services, the sectors that received the most FDI were retail (US$ 6.943 billion), telecommunications (US$ 4.167 billion) and financial services (US$ 3.170 billion). The largest transaction in financial services was the acquisition by Banco Santander of a 14% stake in its subsidiary Banco Santander Brasil. The Spanish bank made use of the opportunity provided by a depressed share price.

This operation by Santander, as well as increased investments by Iberdrola in electricity services, is behind the sharp rise in FDI flows from Spain, which reached US$ 6.356 billion. In 2014, Spain was Brazil's second largest FDI source country after the United States, excluding the Netherlands and Luxembourg, which act as a conduit for sizeable FDI flows from third countries. In 2014, FDI from China climbed to US$ 1.161 billion on the back of increased investments in oil, electricity distribution and manufacturing.

In natural resources, FDI increased in mining, but dropped substantially in oil and gas exploitation. In the successful auction of the Libra field in late 2013, Total (from France), Shell (United Kingdom/the Netherlands), the China National Offshore Oil Corporation (CNOOC) and China National Petroleum Corporation (CNPC) acquired rights to a 40% stake in the field and paid a signing bonus of US$ 7 billion. The consortium (led by the State-owned Petrobras with its 60% stake) committed to invest US$ 400 million between 2014 and 2016. Still, the effect of lower oil prices has been felt in Brazil, and foreign companies have grown more reluctant to increase investments in oil exploration and exploitation.

[11] The sectoral figures are calculated on basis of the sixth edition methodology, but exclude reinvested earnings. The inflows for which sectoral distribution is available total US$ 86.153 billion.

2. Other South American countries

FDI inflows to **Chile** increased by 14% to US$ 22.002 billion, despite falling investment in the mining sector, which is crucial to the Chilean economy. A number of large M&As in other sectors compensated for the fall in mining investment. The largest takeover in 2014 was the acquisition of Compañía General de Electricidad by Spain's Gas Natural Fenosa for a total of US$ 3.3 billion, making the Spanish company the largest player in the Chilean electricity market with a 40% market share. Abbott Laboratories of the United States announced a US$ 2.9 billion takeover of CFR Pharmaceuticals, a Chilean pharmaceuticals company with assets in several Latin American countries. Furthermore, Brazil's Itaú Unibanco acquired a controlling stake in Corpbanca for an estimated US$ 2.85 billion, although the deal is still subject to regulatory approval. Alliance Boots, which is controlled by Walgreens and KKR of the United States, acquired Farmacias Ahumada, which operates in both Chile and Mexico, for US$ 740 million. The acquisition of Bupa Chile by the British United Provident Association was valued at approximately US$ 497 million.

The electricity sector, in particular renewable energy, received large investments in 2014. Some 982 megawatts (MW) of renewable energy projects came online in 2014, compared with 244 MW in 2013, resulting in a total of 2,097 MW of installed capacity. While wind energy accounts for the largest share of installed capacity with 836 MW, solar power is the fastest-growing area, surging from 4 MW at the end of 2013 to 402 MW at the end of 2014. The foreign investments announced in this sector in 2013 included a US$ 1.4 billion investment in wind and solar by Mainstream Renewable Power of Ireland and a US$ 1.2 billion investment in hydropower by United States-based AES Corporation. In 2014 Spain's Abengoa announced a US$ 750 million investment in solar energy. A number of other operators also announced plans in 2014 to build wind farms or solar plants, but not all of these plans will materialize, especially given the slump in international oil prices, which makes investments in electricity generation less attractive.

Despite the slowdown in mining investment in 2014, the sector remains extremely important for Chile. The US$ 1.97 billion investment by Australia's BHP Billiton in the Escondida mine announced in 2013 continued to be disbursed throughout 2014. Similarly, the Sierra Gorda mine, controlled by Poland's KGHM (55%) and Japan's Sumitomo (45%), has accumulated some US$ 4.156 billion in investments in order to start operations, a significant portion of which was disbursed in 2014.

FDI inflows to **Colombia** totalled US$ 16.054 billion in 2014, a similar figure to 2013. FDI in Colombia continues to diversify, with the natural resources sector taking a decreasing share of investment for five years in a row, reaching 40% in 2014. Industry, communications, transport and business services received 45% of inflows, with the remaining 15% going to commerce, hospitality and other sectors. The National Hydrocarbons Agency, however, forecasts that in 2015, some US$ 8 billion will be spent on exploratory drilling (Reuters, 2014), primarily by foreign companies, which would push up the share of natural resources in total FDI again. Outgoing investment from Colombia fluctuates more than incoming investment, dropping by 49% in 2014.

Several sizeable M&As were announced or completed in Colombia in 2014. For example, the US$ 1.32 billion takeover of Helm Bank by Chile's Corpbanca, announced in 2012, was finally completed in 2014. Norwegian fertilizer firm Yara International acquired OFD Holding, whose primary assets are in Colombia, for US$ 377 million. In telecommunications, Sweden's Millicom expanded its assets in Colombia when its local telephone operator Tigo merged with UNE Telecom in 2014. Equity International (United States) partnered with the local Terranum Group to acquire Decameron Hotels & Resorts for US$ 490 million, but since Decameron's assets are spread throughout the region, this acquisition will not have a great impact on FDI inflows in Colombia. On the other hand, TRG Management of the United States divested its 32% share in Transportadora de Gas Internacional to Empresa de Energía de Bogotá for US$ 880 million, thus creating a significant negative inflow of FDI.

In a market-seeking investment proposition, Chile's CCU, which is partially owned by Heineken of the Netherlands, announced an investment of US$ 400 million to start producing beer and non-alcoholic beverages in Colombia. This is a direct challenge to the United Kingdom's SABMiller, which has dominated the Mexican beer market since its 2005 takeover of Bavaria. Box I.3 discusses the Latin American beer market in more detail.

FDI inflows in **Peru** declined for the second consecutive year to US$ 7.607 billion, 18% less than in 2013 and 36% lower than the record of 2012. To keep this decline in perspective, it should be mentioned that Peru has received very high levels of FDI in recent years relative to its previous trend and also to the size of its economy.

There is no official data on FDI by sector in Peru, but the mining sector seems to account for much of the decline. In 2014 investment in mining (both domestic and foreign) fell by 11%, the first drop since 2007 after years of very rapid growth. The fall was particularly marked in the acquisition of equipment and infrastructure. Copper production was flat in terms of quantities and dropped by 12% in dollar terms, while gold production declined. FDI had also increased over the previous decade in services and other market-seeking activities, but the slowdown in GDP growth in 2014 may make the domestic market less attractive for investors.

Lower metal prices, production problems at the mines and slacker economic growth combined to reduce FDI profitability in Peru. FDI income earned by foreign companies in the country dropped to US$ 7.964 billion, the lowest level since 2007. About half of these profits were reinvested, a similar proportion to previous years. Reinvested earnings were the largest component of FDI (totalling US$ 3.978 billion), followed by intercompany loans (US$ 2.278 billion) and capital contributions (US$ 1.342 billion), which were significantly lower than in previous years.

Box I.3

"Big Beer" market dominance in Latin America and the Caribbean

Beer is an interesting product: it is almost ubiquitous and relatively easy to produce, but bulky and thus expensive to export. Even the least developed economies produce it, since there is no lack of demand. At the global level, however, the market is extremely concentrated, with only five companies —led by Anheuser-Busch InBev (Belgium), SABMiller (United Kingdom) and Heineken (the Netherlands)— responsible for over half of the world's beer production (Barth-Haas Group, 2014). Each of these companies is the result of multiple mergers and acquisitions as organic growth into new markets is almost impossible. Anheuser-Busch InBev is the product of the takeover of United States-based Anheuser-Busch by Belgian-Brazilian InBev in 2008. InBev itself has its origins in a 2004 merger of Belgium's Interbrew and Brazil's AmBev.

In Latin America, many of the largest M&As in recent years have been associated with beer. The 2013 takeover of Grupo Modelo in Mexico by Anheuser-Busch InBev (valued at US$ 13.249 billion) was one of the largest ever recorded in Latin America and the Caribbean. The table below ranks the largest mergers and acquisitions in the beer market in the last 20 years. It shows that the global trend towards consolidation in this market led to two waves of large takeovers in Latin America and the Caribbean: around 2005-2006 and in 2010-2013.

Latin America and the Caribbean: largest mergers and acquisitions in the beer sector, 1995-2014

Year	Company	Country of origin	Assets acquired	Location	Nominal amount *(billions of dollars)*	Real value in 2014 [a] *(billions of dollars)*
2004	Interbrew	Belgium	AmBev (52%)	Brazil	11 732	14 196
2013	Anheuser-Busch InBev	Belgium	Grupo Modelo (50%)	Mexico	13 249	13 381
2010	Heineken	Netherlands	FEMSA beer operations	Mexico	7 325	7 838
2005	SABMiller	United Kingdom	Bavaria (97%)	Colombia	4 717	5 566
2013	Constellation Brands	United States	Compañía Cervecera de Coahuila	Mexico	2 900	2 929
2011	Kirin Holdings	Japan	Aleadri-Schinni Participações e Representações	Brazil	2 523	2 649
2005	Interbrew	Belgium	AmBev (5%)	Brazil	1 274	1 503
2011	Kirin Holdings	Japan	Jadangil Participações e Representações	Brazil	1 354	1 421
2006	Anheuser-Busch InBev	Belgium	Quinsa (34%)	Argentina	1 200	1 368
2012	Anheuser-Busch InBev	Belgium	Cervecería Nacional Dominicana (42%)	Dominican Republic	1 000	1 030

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of figures provided by Thomson Reuters.
[a] Real values in 2014 were calculated using the United States GDP deflator as provided by the United States Bureau of Economic Analysis.

As a result of these two waves of takeovers, local brewers play a significant role in very few countries in the region. Only in the Bolivarian Republic of Venezuela, Costa Rica, Guatemala, Nicaragua and some Caribbean countries do locally owned enterprises have the largest market share. That is not to say that there are no locally controlled brands in other markets, but they often play second or even third fiddle to the large international enterprises. The map below shows the top beer company in each economy in the region.

In addition to the global top five companies, local independent (often family-owned) enterprises are the market leaders in a small number of countries, the United Kingdom's Diageo has the largest market share in Jamaica, and Trinidad and Tobago's ANSA McAL holds the largest market share in three smaller economies in the Caribbean. These last two companies are not traditionally considered brewing companies, although Diageo does have significant experience in this area through its Guinness brand.

Box I.3 (concluded)

Latin America and the Caribbean: top beer company in each market, 2014

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of Barth-Haas Group, "Beer Production - Market Leaders and their Challengers in the Top 40 Countries in 2012", 2013 [online] http://www.barthhaasgroup.com/johbarth/images/pdfs/report2013/Barth_Beilage_2013.pdf.

Note: The boundaries shown on this map do not imply official endorsement or acceptance by the United Nations.

As the map clearly shows, Anheuser-Busch InBev is the dominant player in the Latin American market, while SABMiller is the market leader in a several economies in northern South America and Central America. The takeover of Bavaria in 2005 was significant because it gave SABMiller the largest market share in several medium-sized beer markets. In Colombia, Ecuador and Peru, SABMiller's market share was 98%, 95% and 94%, respectively, in 2012 (Barth-Haas Group, 2013). This dominance goes far beyond that of the other companies in other markets, varying from Anheuser-Busch InBev's 69% market share in Brazil, 56% in Mexico and 77% in Argentina to Heineken's[a] 88% market share in Chile. It is typical for single brewers to dominate national beer markets in developing economies. The largest players in Angola (SABMiller with 89%), Turkey (Efes with 83%), Nigeria (Heineken with 70%) and Thailand (Singha with 67%) all hold a dominant market share. By contrast, in developed economies, market shares above 50% are very rare. Some exceptions include Belgium, in which the domestic Anheuser-Busch InBev has a market share of 56%, Denmark (Carlsberg with 54%) and Republic of Korea (Oriental Brewery with 53%).

The implication of this intense market dominance in Latin America and the Caribbean is that competition is relatively stifled. Since organic growth is difficult, existing market dominance practically guarantees a future market for a product, though this may not hold true as strictly for some larger markets. Heineken, for example, announced a new US$ 480 million brewery in Mexico in early 2015. However, as a general rule, the lack of competition shields companies from the pressure to innovate, which may not benefit consumers in the long term. The advantage gained by the buyer is also reflected in the high valuations of beer companies. A list of the top 10 largest M&As of any type in Latin America and the Caribbean in the last 20 years would include several of those listed in the table above. The value, and profitability, of these beer companies is incomparable with any other sector.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of Barth-Haas Group, "Beer Production - Market Leaders and their Challengers in the Top 40 Countries in 2012", 2013 [online] http://www.barthhaasgroup.com/johbarth/images/pdfs/report2013/Barth_Beilage_2013.pdf; and information provided by Thomson Reuters.

[a] Heineken shares control of Compañia Cervecerías Unidas (CCU) with the local Luksic family: a unique blend for a large brewer in Latin America of local control and international experience.

Peru hosted three of the five largest corporate acquisitions in Latin America in 2014, but these were ultimately transfers of ownership between foreign companies and had no net effect on FDI flows. Two Chinese companies increased their footprint in Peru: China Minmetals Corporation bought the Las Bambas copper mine from Glencore of Switzerland for US$ 7.005 billion and the China National Petroleum Corporation (CNPC) acquired the assets of Brazil's Petrobras Energía Perú for US$ 2.6 billion.

FDI inflows to **Argentina** dropped by 41% to US$ 6.612 billion —the smallest amount the country has received since 2009. The main reason for this decline was the nationalization of YPF, which took place in 2012, but was not

settled until 2014. The government paid US$ 5.000 billion to Spain's Repsol as compensation for the expropriation of 51% of YPF. Repsol subsequently sold its remaining 12% share. With the return of the majority share to Argentina, in practice, this implies a negative inflow in the balance of payments. If it were not for this transaction, inflows into Argentina would have remained at a similar level to previous years. Reinvested earnings make up the bulk of inflows and totalled US$ 7.365 billion. In mining, Canada's Yamana Gold is in the process of investing US$ 450 million in the Cerro Moro project near Puerto Deseado. Although recent data are not available, the sectoral distribution of FDI in Argentina seems balanced between natural resources, manufacturing and services. The share of services has increased in recent years, but manufacturing is likely to have gained ground in 2014.

Several automotive manufacturers have expanded their production facilities in Argentina recently. In October, Japan's Toyota announced it had completed 60% of its US$ 800 million investment plan announced in 2013, while General Motors of the United States announced in 2014 that it would increase its earlier investment of US$ 450 million to US$ 720 million. Lastly, Italy's Fiat Chrysler announced the construction of a new engines plant in Argentina in 2013 at a cost of up to US$ 300 million.

According to industry specialists, Argentina has great potential for oil exploration, with the Vaca Muerta formation touted as a particularly abundant source of both shale gas and shale oil. The government has announced several special benefits to oil companies willing to invest more than US$ 1 billion. Since then, United States-based Chevron signed an agreement with YPF to invest US$ 1.6 billion to explore the Vaca Muerta formation and Russia's Gazprom is rumoured to have offered US$ 1 billion of investments. The Vaca Muerta exploration is expected to require a total investment of some US$ 15 billion. In December, Malaysia's PETRONAS committed US$ 550 million to shale gas cooperation with YPF (Mander, 2014). Finally, the Anglo-Dutch company, Royal Dutch Shell and France's Total announced an investment of US$ 550 million together with Gas y Petróleo de Neuquén, a local oil and gas company, in a different field.

In 2014, the **Bolivarian Republic of Venezuela** witnessed a significant reduction in FDI inflows. Total inflows fell by 88% from US$ 2.680 billion to US$ 320 million. In previous years investment had increased owing to restrictions on foreign exchange: foreign enterprises were unable to repatriate their profits and therefore sought investment opportunities within the country. This resulted in a property boom in Caracas as many foreign companies reinvested their profits in real estate. The estimated 3% contraction in GDP growth in 2014 likely caused a concomitant drop in transnationals' profits and thus a subsequent reduction in reinvested earnings.[12]

The oil industry continues to require significant investment and the government-owned Petróleos de Venezuela, S.A. (PDVSA) works with its foreign partners on operating production facilities. In the automobile industry, where the Bolivarian Republic of Venezuela was until recently among the major players in Latin America, production slumped by about 75% between 2013 and 2014 owing to the limited availability of parts and a lack of access to foreign exchange (*The Wall Street Journal*, 2014).

FDI inflows to **Uruguay** totalled US$ 2.755 billion in 2014, 9% lower than in 2013. Uruguay has received significant investment in its renewable energy sector —testament to this was the completion of several large wind farms in 2014. The country is scheduled to source 90% of its energy from renewable sources in 2015 and is among the global leaders in the field, particularly with respect to wind energy. Recent large investors in wind farms include Argentina's Corporación América (50 MW), Spain's Abengoa (50 MW and 70 MW), Germany's SOWITEC (81 MW) and Italy's ENEL (50 MW).

Manufacturing does not play a major role in Uruguay. Nevertheless, a new pulp mill was completed in 2014, representing the largest single investment the country has ever received. The mill, a joint venture between Chile's Arauca and Swedish-Finnish Stora Enso, cost US$ 2.27 billion, plus US$ 230 million for the related port, and has taken several years to complete.

Some large plans are on the table in Uruguay. A project by United Arab Emirates-based Zamin to develop an iron mine for a cost of up to US$ 3 billion has been under discussion for several years. In direct relation to this, the Government of Uruguay has been promoting the idea of constructing a new US$ 1 billion port on its Atlantic coast, for which it is looking for investors.

[12] Valuing the existing FDI stock is complicated by the existence of alternative exchange rates. Individual companies, such as Spain's Telefónica, have devalued their Venezuelan assets by moving from the official exchange rate to alternative ones, but the Central Bank of Venezuela continues to use the official exchange rate. Telefónica has devalued its assets in the country by 7.450 billion euros over several years (El País, 2015).

After two years of very large inflows, FDI inflows to the **Plurinational State of Bolivia** fell by 63% to US$ 648 million. In recent years, much of the investment in the country has gone to natural resources, particularly in the oil and gas sector. In 2014, for example, PDVSA announced that it would invest US$ 200 million in a number of exploration and production projects. Outside the natural resources sector, Peru's Holding Cementero acquired full control of the Plurinational State of Bolivia's largest cement maker, Soboce, by purchasing the remaining 51% stake in the company for an estimated US$ 300 million in December.

Several nationalizations and divestments have taken place in the Plurinational State of Bolivia in recent years. Brazil's Petrobras and France's Total divested their stake in the major gas pipeline Transierra for US$ 133 million. The buyer, Bolivian State-owned energy company YPFB, now controls a great majority of the gas pipeline. The Malku Khota mine was nationalized in 2012 and its former owner (TriMetals Mining of Canada) is seeking US$ 386 million in compensation in an international arbitration court. India's Jindal Steel and Power was awarded US$ 22.5 million by an international court for its share in the El Mutún project and it is seeking a further US$ 100 million in damages. Such nationalizations and divestments are considered to be negative inflows of FDI, thus leading to a reduction in FDI.

FDI inflows to **Ecuador** increased by 6% to US$ 774 million, over two thirds of which was invested in the natural resources sector. Manufacturing's share shrank to only 14% of FDI inflows during 2014, while services fell from 43% to only 18% of inflows. Oil exploration is currently undergoing a small boom in Ecuador. In October, contracts were awarded to a number of international companies to work with state-owned Petroamazonas in order to explore for new oil supplies. The government expects that US$ 2.1 billion will be spent on such exploration over the next five years.

The Ecuadorian food and beverage market has attracted significant interest from foreign firms. Holding Tonicorp, a dairy products company, was acquired by Mexico's Arca Continental, in a deal also involving Coca-Cola of the United States. This acquisition was valued at US$ 400 million and Coca-Cola announced other plans in 2014 to invest up to US$ 1 billion in Ecuador over the next five years. Arca Continental also announced its intention to invest a further US$ 80 million in a new industrial plant.

In the financial sector, Panama's Promerica Financial Corporation, which already operated a bank in Ecuador, acquired 56% of Banco de la Producción, the country's fourth largest bank. This could benefit the sector by raising professional standards. Promerica already operates banks in many Central American countries, as well as in the Cayman Islands and the Dominican Republic.

Paraguay more than trebled its inflows, from US$ 72 million to US$ 236 million. The country is making efforts to attract more investment and particularly to diversify away from infrastructure and agriculture, its traditional sectors. One of the largest growth areas is the automotive industry, in which Paraguay takes advantage of its MERCOSUR membership to supply Brazilian and Argentine car factories. Japan's Fujikura is among the leading car parts manufacturers in the country, but recent investment announcements have also been made by Japan's Sumitomo (US$ 15 million), Republic of Korea's THN Corporation (US$ 40 million) and Italy's Pirelli (exploratory stage).

Several Brazilian companies also announced expansions in 2014, including plastics manufacturer X-Plast with US$ 26 million. However, the largest Brazilian investments are in the agricultural sector: meat processing company JBS announced a US$ 100 million investment in the construction of a new slaughterhouse in Paraguay, and Bunge has long been a major investor in the country.

3. Mexico

In 2014, FDI flows to Mexico fell by 49% to US$ 22.795 billion. While this may seem like a very large drop, it is important to remember that the figures for 2013 were inflated by the takeover of Grupo Modelo by Belgium's Anheuser-Busch InBev (see box I.3) for US$ 13.249 billion. This was compounded by a US$ 5.57 billion divestment in the telecommunications sector (completed for regulatory reasons) in 2014, which is discussed in more detail below. Without these two extraordinary events, FDI inflows in Mexico would have been above those of the previous decade and the two-year average inflow of FDI is in fact the highest ever recorded. Aside from the telecommunications takeover, M&As actually played a relatively small role in 2014. United States-based PPG Industries acquired Consorcio Comex for US$ 2.3 billion in order to expand its coatings business into Mexico and Central America; and France's Eutelsat Communications acquired Satélites Mexicanos for US$ 1.142 billion.

United States-based AT&T was responsible for the divestment that resulted in a negative inflow in 2014 and was also involved in some of the other large transactions affecting Mexico in 2014. In May, the company announced its intention to acquire DirecTV, the United States' leading satellite television provider, for US$ 48.5 billion. Since DirecTV is a major player in several countries, including Mexico, the acquisition had to be approved by regulators in these different countries. In Mexico, regulatory approval was complicated by the fact that AT&T also held an 8.3% stake, and 24% of the voting shares, in América Móvil, another company that provides satellite television services. AT&T therefore sold its stake to Inmobiliaria Carso, América Móvil's holding company, for US$ 5.57 billion. AT&T maintained its faith in the Mexican market, however, as demonstrated by its November agreement with Grupo Salinas to acquire Iusacell, Mexico's third largest mobile network, for US$ 2.5 billion. This acquisition was completed in January 2015 and was therefore not included in the annual FDI inflows for 2014, whereas the US$ 5.57 billion divestment was. All of this goes some way in explaining the fall in investment in Mexico, where the transport and telecommunications sector posted a negative inflow of US$ 3.753 billion in 2014.

The heightened activity in the telecommunications sector in Mexico is partially driven by new anti-monopoly legislation, under which the regulatory body may impose asymmetrical regulations and obligations on the "preponderant agent", defined as a party with market dominance. América Móvil is such a company, controlling 68% of the mobile telecommunications market. The company can either reduce its market share by selling some of its assets or continue to be the preponderant agent. In the first case, Bank of America estimates that such an operation could yield US$ 10 billion (Telegeography, 2014) and could give a platform to a new (foreign or local) player. In the second case, the anti-monopoly legislation may make it more attractive for new players to enter the market anyway, as it did for AT&T.

In manufacturing, the automotive industry is key (see box I.4 in ECLAC, 2014b), with Mexico now the world's seventh largest car producer. Of all the branches of manufacturing, the automotive industry was the largest FDI recipient in 2014, absorbing US$ 4.308 billion of the US$ 12.87 billion total. Mexico was the subject of a wave of new investment announcements from car makers from all over the world in 2014. Among the largest were investments by the United States-based Ford and General Motors for US$ 2 billion and US$ 3.6 billion respectively, and by the Republic of Korea's Kia Motors (largely owned by Hyundai Motors) for US$ 1 billion. In a joint venture, Germany's Daimler and Japan's Nissan are building a US$ 1.36 billion factory. Other expansion plans are under way from Sweden's Volvo and Japan's Honda.

Inflows in the electricity sector are still small, totalling US$ 580 million in 2014, although this was higher than the average of US$ 253 million per year in the five previous years. Spain's Iberdrola announced investments of US$ 5 billion, of which it has already disbursed US$ 1.5 billion, including US$ 950 million in wind farms with 2,000 MW of capacity. Furthermore, on the back of the reforms to the energy sector, IEnova, which is co-owned by United States-based Sempra Energy, plans to invest US$ 3.2 billion in domestic infrastructure projects over two years, while Canada's TransCanada is involved in a US$ 1 billion pipeline construction project.

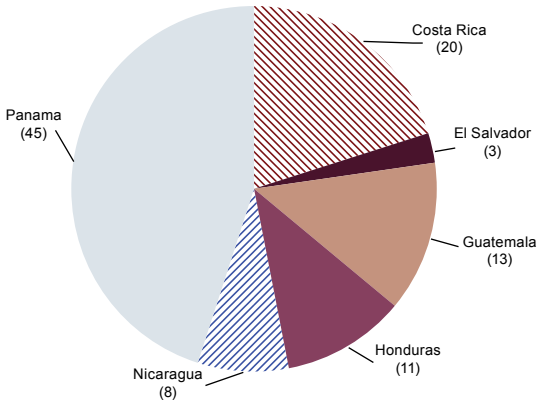
The services sector received approximately one third of all FDI inflows into Mexico in 2014, with financial services being the dominant subsector, attracting 25% of all FDI inflows. The other services subsector with significant inflows was hospitality, which received some US$ 825 million in FDI in 2014, primarily in the hotel sector.

4. Central America

FDI inflows to Central America, unlike those to South America, held relatively steady in 2014. In total, the subregion recorded inflows of US$ 10.480 billion, 2% less than the year before. Once again, Panama was the largest recipient of FDI, accounting for more than 45% of the Central American total. The largest rate of growth was observed in El Salvador, whose inflows nearly doubled between 2013 and 2014. Costa Rica was the only country with decreased inflows in 2014, though it continues to be the second largest recipient (see figure I.18)

Central America hosts a great deal of activity in the renewable energy sector. According to consulting company IHS Technology, photovoltaic capacity in Central America rose from 6 MW in 2013 to 22 MW in 2014 and is expected to jump to 243 MW in 2015, with Honduras leading the way. Investments in renewable energy, primarily by foreign investors, are already having an impact on the region's energy balance, even though solar energy still makes up a very small portion of current electricity generation capacity. Hydropower continues to be the pre-eminent renewable resource, wind energy also far outstrips solar energy, and even geothermal energy plays a part. Nevertheless, investment in solar energy is increasing rapidly.

Figure I.18
Central America: distribution of FDI inflows by country, 2014
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and estimates as of 18 May 2015.

In the other sectors, services continue to be the leading recipient of FDI, though mining has been making strides in certain countries. As discussed in box I.4, the expansion of the Panama Canal and the proposed construction of the Nicaragua Canal are spurring investment in logistics facilities and ports throughout Central America and the Caribbean.

FDI flows into **Panama** increased marginally to US$ 4.719 billion, which is the highest ever recorded and continues a nearly unbroken uptrend since 2009. FDI income has also increased substantially over the same period and it too reached a new record in 2014. Panama has the highest FDI-to-GDP ratio in Latin America and is positioned to continue receiving significant investment inflows (box I.4 below discusses the impact of the Panama Canal on investment in the country). The share of natural resources in FDI has grown with the development of the Cobre Panama project. Since this concession was acquired by Canada's First Quantum Minerals in a hostile takeover, investment has continued, including approximately US$ 600 million in 2014. The open-pit mine is expected to start operations in 2018 and total investment is estimated to be US$ 6.4 billion. Even though specific data are not yet available, this single investment by First Quantum Minerals is solely responsible for increasing the share of natural resources in Panama's FDI flows, which are traditionally dominated by services (90% of inflows between 2009 and 2012).

The expansion of the Panama Canal currently under way is leading to a further inflow of investment in the logistics sector. Newly announced projects in logistics include warehouses and distribution centres by the ESKE Group (Peru), Hutchison Whampoa (Hong Kong Special Administrative Region of China), Deutsche Post (Germany), PSA International (Singapore) and the CEVA Group (United Kingdom). Beyond the logistics sector, Panama is consolidating its role as a financial centre, attracting significant inflows and outflows of FDI in that sector. Colombia's Bancolombia is one of the major foreign players, strengthening its position through its 2013 takeover of HSBC Panama. Since the country is involved in many offshore financial activities, it is no surprise that Panama hosts the regional or global headquarters of many international companies.

Lastly, Panama also attracts investment in its renewable energy sector. InterEnergy, for example, which is incorporated in the Cayman Islands, announced a US$ 427 million investment in a Panamanian wind power project with a total capacity of 270 MW.

FDI flows into **Costa Rica** shrank by 21% to US$ 2.106 billion in 2014. The share of the manufacturing sector has been in decline for several years and received only 20% of FDI inflows in 2014. The largest receiving categories were services and real estate, with 35% and 36% of inflows, respectively. In 2014, both Mexico's América Móvil and Spain's Telefónica announced expansions of their 4G networks in the country. These roll-outs tend to be expensive, but exact cost estimates are not available. According to the Costa Rican Investment Promotion Agency (CINDE), companies committed to US$ 474.4 million of new investments in 2014, including US$ 127 million in the life sciences sector, which is a profitable sector for Costa Rica. A sizeable new project has been announced by United States-based American World Clinics, which plans to construct a US$ 100 million health-care complex aimed at attracting medical tourists.

Box I.4

The impact of the Atlantic-Pacific canal(s?)

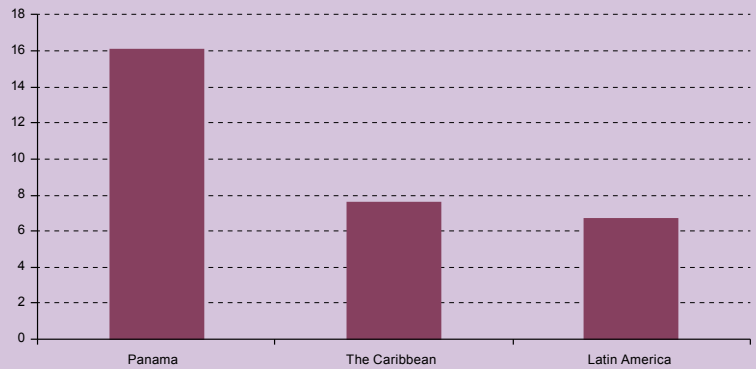
The 77.1-kilometre Panama Canal, which celebrated its centenary in 2014, has had an immense impact on international trade. By virtue of its vital role in international trade, the size of the locks on the Canal imposed a practical maximum size limit on the ships used in transport, known as Panamax. The Canal's role in enabling trade between the Pacific and Atlantic cannot be overstated. Today, around 5% of global maritime trade passes through the Panama Canal.

For Panama, the impact has been even larger. As shown in the figure below, the Panamanian economy relies much more heavily on transport, storage and communication than the rest of the region. This is attributable to the large harbour, warehousing and transport industry related to the Panama Canal, which is responsible, directly and indirectly, for some 100,000 to 120,000 jobs. The Canal is the driving force behind much investment in Panama. It continues to be the largest recipient of FDI relative to the size of the economy in Latin America and only a small number of Caribbean economies outperform it by this measure.

According to fDi Markets, Hutchison Whampoa (Hong Kong Special Administrative Region of China), Deutsche Post (Germany), PSA International (Singapore) and the CEVA Group (United Kingdom) announced investments in warehousing and storage projects in 2014 for a combined total of more than US$ 700 million. This success has been an important driver for the robust economic growth recorded in Panama in recent years, leading some analysts to refer to Panama City as "the Singapore of Central America" (*The Economist*, 2011).

Latin America and the Caribbean: share of the transport, storage and communications sector in total GDP, 2012

(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of the CEPALSTAT database.

However, the limitations of the Panama Canal have grown increasingly clear. The Panamax standard has become a severe constraint as many modern ships are too large to fit through the Canal. In 2006, the Panama Canal Authority (PCA) estimated that by 2011, 37% of cargo ships would be too large (PCA, 2006). In order to remain fit for purpose, a plan was proposed to add a third set of larger locks to allow larger ships to pass through the canal. The US$ 5.25 billion project was originally due for completion in 2014, but is still under construction. Completion is now scheduled for the end of 2015. The project is financed primarily through loans from international partners, including the Japan Bank for International Cooperation, the European Investment Bank and the International Finance Corporation. Although this is not an FDI project as such, many foreign companies are involved as contractors in the construction process.

Meanwhile, the Government of Nicaragua has plans to construct a competing canal,a which, with a length of 259 kilometres, will be more than three times as long as the Panama Canal. If completed, it will be able to handle ships that are significantly larger than those that can fit through the expanded Panama Canal. Discussions about a possible Nicaragua Canal date back to 1825, but the Hong Kong Nicaragua Canal Development Group (HKND), based in the Hong Kong Special Administrative Region of China, was only recently founded in 2012 for the purpose of building the Nicaragua Canal. Officially, work started in December 2014 and is scheduled for completion by 2020 at an estimated cost of US$ 50 billion. Several major Chinese companies will participate in the project, which is not, as yet, fully funded. The project remains uncertain, but its completion would have a huge impact on the shipping industry.

In view of the expansion of the Panama Canal and the possible construction of the Nicaragua Canal, shipping in the Caribbean has a bright future. These prospects have led to a large number of new projects throughout the Caribbean, with several economies seeking to set themselves up as logistics hubs in competition with Panama. In 2014, Cuba opened the Port of Mariel, which was largely funded by Brazil, at a cost of nearly US$ 1 billion. The port's proximity to the canal(s) and to the United States could create opportunities, as long as the United States lifts its sanctions on Cuba. The China Harbour Engineering Company (CHEC) is involved in the preliminary studies regarding the possible construction of large new port terminals in Jamaica (Goat Islands at an estimated cost of US$ 1.350 billion) and broke ground on a transhipment port in the Bahamas in 2014 at a cost of US$ 39 million. Finally, in Trinidad and Tobago, a consortium of companies from China committed in 2014 to the construction of both a new port (costing around US$ 500 million) and several new industrial parks (US$ 250 million).

Owing to their key role in international transport, the Panama Canal and, if it is completed, the future Nicaragua Canal have transformative potential, not just for the individual countries involved, but for the entire region.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of Panama Canal Authority (2006), "Third set of locks project fact sheet" [online] http://www.pancanal.com/esp/plan/documentos/propuesta/acp-proposla-relevant-information.pdf; Financial Times, fDi Markets and *The Economist*, "A Singapore for Central America?", 14 July 2011 [online] http://www.economist.com/node/18959000.

[a] The potential construction of the Nicaragua Canal has drawn much criticism with respect to the decision-making process, the environmental impact and the overall desirability of the new canal. An overview of the sceptics' point of view can be found in Confidencial (2015).

Costa Rica is recognized globally for its efforts to reduce the use of hydrocarbons in energy generation. In 2014, the country generated approximately 80% of its electricity through hydropower and, in 2015, it was lauded for having produced all its electricity from renewable sources in the first 75 days of the year, thanks to abundant rainfall. In 2014, the Costa Rican Congress approved a US$ 958 million geothermal project, financed largely through loans from Japanese and European investment banks. For the most part, electricity generation is controlled by government-owned ICE, but there are also several small private players. The Orosí wind project, developed by the United Kingdom's Globeleq, will have 50 MW of generation capacity and is currently under construction for at least US$ 109 million. Other investors include Spain's Gas Natural Fenosa, which is constructing the 50 MW Torito 1 hydropower plant, to be completed in 2015, and Italy's ENEL, which is involved in the 50 MW Chucas hydropower plant completed in 2014.[13]

In manufacturing, Canada's Gildan Activewear is investing an undisclosed sum in a new textile factory in Guanacaste, as part of a US$ 300 million expansion plan. Finally, Sysco Corporation of the United States announced that it had acquired 50% of the privately held food distributor, Mayca Distribuidores, for an undisclosed sum.

FDI flows into **Guatemala** increased by 8% to US$ 1.396 billion in 2014, the highest level ever recorded. For several years, the natural resources sector has received the largest FDI inflows, but this year the energy sector outperformed natural resources, receiving 24% of inflows compared with 23%, respectively. Manufacturing's share slipped to 13% and retail received 15% of total inflows.

Solway Group (the Russian Federation) is constructing a ferronickel mine at an estimated cost of close to US$ 300 million and has received permission to explore for other opportunities. Meanwhile, Tahoe Resources of Canada operates the Escobal mine in San Rafael Las Flores, which also requires significant investments. Finally, Canada's Quattro signed an exploration and exploitation contract for a block in the North Petén basin in 2014.

Grup Marítim TCB of Spain broke ground on a US$ 252 million port enlargement in preparation for the expansion of the Panama Canal (see box I.4). Finally, through its Tigo brand, Sweden's Millicom acquired Cablefusión, one of its main competitors in the pay television market, to become a sector leader.

In **Honduras**, the inflow of FDI increased by 8% to reach a new record of US$ 1.144 billion, despite a significant divestment by Citibank of the United States, which sold its Honduran operations to local financial group Banco Ficohsa in 2014. Banco Ficohsa also acquired the Guatemalan assets of Citibank, also for an undisclosed sum, in 2015. Telecommunications operators in many countries in the region are upgrading their networks to make them 4G compatible. In Honduras, for example, the Russian Federation's VimpelCom is investing in expanding the 4G network of its subsidiary Wind Telecom.

Like other countries in Central America, Honduras is actively expanding its electricity generation capacity from renewable sources. By 2018, Honduras is expected to install a cumulative 499 MW of new solar capacity. To this end, SunEdison of the United States started construction in 2014 on a US$ 146 million, 82 MW photovoltaic plant in Choluteca. Upower, another United States-based independent power producer, also started construction in 2014 on a US$ 190 million, 100 MW photovoltaic plant in La Gaceta. Nevertheless, there is also ongoing investment in traditional electricity generation. Guatemala's Cementos Progreso is working with a local partner to build a US$ 125 million, 60 MW, coal-operated power plant both to supply its own factory and to sell electricity to the national electricity company.

In **Nicaragua**, FDI edged up from US$ 816 million to US$ 840 million from 2013 to 2014. A project that could have a significant impact on future FDI inflows is the Nicaragua Canal (the continuing debate on that topic is covered in box I.4). One of the largest investments in 2014 was the rapid expansion of Xinwei Telecom of China, which was awarded six licences to provide different services in the country, leading to expected investments of US$ 300 million. As announced in 2013, Canada's B2Gold is continuing to explore new mining options in order to expand its existing operations, which represents a continuous investment by the company. Until now, Nicaragua has received less FDI in renewable energy generation than other Central American nations, though the United States-based Viaspace has invested in a 12 MW biomass power plant. However, in 2014, the Government of Nicaragua announced that it aims to have 90% of its electricity generated by renewable sources, particularly wind and hydroelectric power. The construction by a Brazilian conglomerate of the 253MW Tumarín dam is getting underway, but with ownership of the project shared between the State-owned electricity companies and foreign investors.

[13] The largest project is the Reventazón dam, which is expected to cost up to US$ 1.4 billion and to have generating capacity of more than 300 MW. However, this project is being developed by the State-owned Grupo ICE and is therefore not FDI.

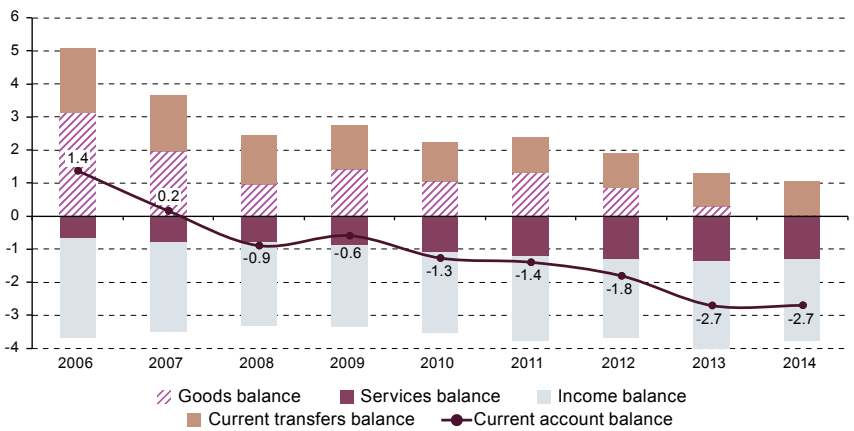
FDI inflows to **El Salvador** increased by 53% from US$ 179 million in 2013 to US$ 275 million in 2014. A portion of that investment came from the ongoing investment by Sensity Systems of the United States, an LED manufacturer that committed in 2013 to building a US$ 490 million factory to supply the region. Colombia's Procaps acquired Laboratorios López, which is the country's largest pharmaceuticals laboratory. Hyatt Hotels of the United States announced that it would invest US$ 36 million in its first hotel in El Salvador, which is scheduled to open in 2016.

Italy's ENEL, through its subsidiary Enel Green Power, announced a deal in December to sell its 36.2% stake in the La Geo geothermal joint venture to its State-owned partner INE for US$ 280 million. This large negative inflow is offset by some major investments in the telecommunications sector, where inflows totalled US$ 334 million in 2014. The year's largest telecommunications investment came from Sweden's Millicom, through its local Tigo brand. Also in telecommunications, Jamaica's Digicel announced a US$ 45 million upgrade of its network in early 2014.

E. FDI and the current account balance

Over the past two decades, Latin America and the Caribbean posted a current account surplus for just five years (from 2001 to 2005). Throughout the 1990s and from 2006 to 2014 the region registered cumulative current account deficits, which have widened a great deal in the past five years. Figure I.19 shows the changes in the different components of the current account over the last decade. The greatest variation was in the goods surplus, which shrank from 3% of GDP in 2006 to 0.3% of GDP in 2013 and virtually disappeared in 2014. The other components have been more stable: the current transfers balance has been consistently positive, deteriorating only slightly over the decade, and both the income balance and the services balance have posted long-standing deficits.

Figure I.19
Latin America and the Caribbean: current account structure, 2006-2014
(Percentages of GDP)



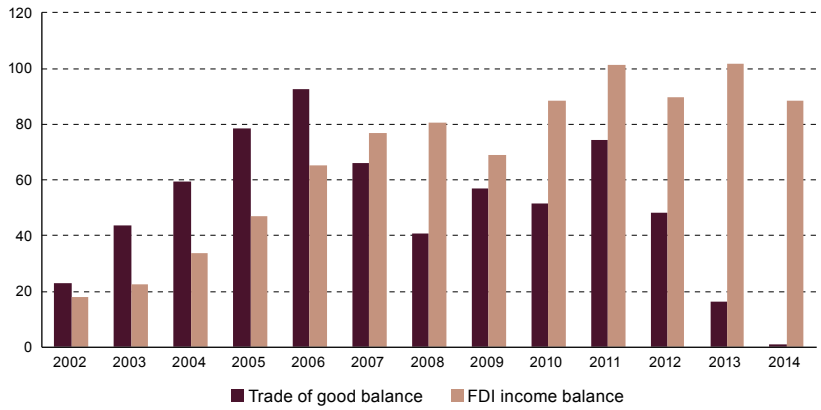
Source: Economic commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and estimates.

The current account deficit deteriorated markedly in 2013 owing mainly to a sharp reduction in the goods surplus from 0.8% to 0.3% of GDP as imports grew more rapidly than exports. The slowdown in export growth, which began in 2012, was caused by weak international demand from both developed economies and emerging markets (ECLAC, 2013a). That weak demand drove down the prices of the region's export goods (mostly commodities) to the extent that even higher export volumes could not offset the fall. The deficit remained stable in 2014 because the drop in FDI income mentioned above was compensated by an equal drop in the goods trade surplus (ECLAC, 2014a).

A look at the data for the past decade reveals that the growth of FDI income has been possibly the strongest driver of the deterioration of the region's current account balance. The profits of transnational corporations in the region rose from US$ 19.011 billion in 2002 to US$ 103.379 billion in 2010 and they have remained at these high levels ever since, reaching a record in nominal terms of US$ 123.798 billion in 2013. That last amount represented 83% of total investment income from the region and more than double the value of the services balance.

From 2002 to 2007 the rapid growth of FDI income was offset by an equally large rise in exports. In fact both trends were determined by the surge in commodity prices, which boosted both exports and the profits of transnational corporations in the extractive industries. That dynamic changed substantially in the subsequent years. The global economic crisis of 2008-2009 hit exports much harder than FDI income in the region, and the disparity between the two has grown even more apparent in the past three years. While the goods balance declined from US$ 75 billion in 2011 to only US$ 1 billion in 2014, the FDI income deficit[14] has held steady at around US$ 100 billion (see figure I.20). Other current account items, such as trade in services, remittances and other types of investment income, are certainly important in many economies, but the widening FDI income deficit and the deteriorating surplus on the goods balance have been the largest single factors contributing to the region's growing current account deficit.

Figure I.20
Latin America and the Caribbean: selected current account items
(Billions of dollars)



Source: Economic commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and estimates as of 18 May 2015.

A large current account deficit can jeopardize economic growth if it cannot be funded on the international market (ECLAC, 2013b). The growth rate to which countries can aspire without coming up against this external constraint depends on four variables: (i) the net exports of each economy; (ii) the terms of trade; (iii) capital flows between the economy and the rest of the world; and (iv) net payments to non-resident factors of production. The capacity of each country to finance its current account deficit depends on its level of reserves, sovereign funds (if any) and degree of access to international markets, which is mainly determined by its credit history.

It is also important to analyse the dynamics of FDI inflows and FDI income in relation to the economic cycle. While FDI is now the largest external liability of most countries in the region, it is not a liability on which the creditor can demand repayment, as opposed to loans and bonds. This is one reason why FDI inflows are much less volatile than portfolio and other investments and very rarely turn negative in a crisis. At the same time, FDI income expands with economic growth and contracts during downturns, producing a countercyclical effect on the host economy. Events that can trigger a balance-of-payments crisis, such as terms-of-trade shocks, are likely to reduce FDI income as well.

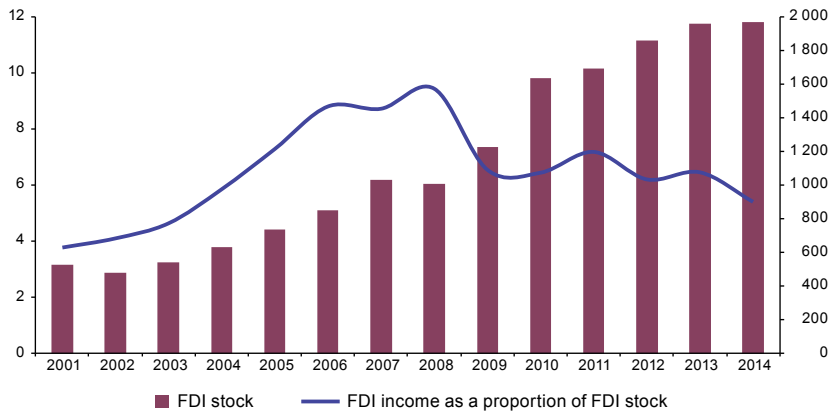
However, this automatic adjustment is far from perfect. While the prices of export commodities started to decline in 2012 and economic growth contracted in 2013, FDI income continued to reach new highs and declined only in 2014. Although the average profitability of FDI in Latin America and the Caribbean declined since 2008, as the FDI stock continued to grow, total FDI income actually rose, reaching its highest level in 2013 (see annex table I.A.5). In other words, the size of the assets that transnational corporations have in the region and their continuing growth guarantee that the profits of transnationals remain large, despite a potential drop in profitability (see figure I.21).

The impact of FDI income on the external accounts varies significantly by country. On the whole, the countries with FDI concentrated in the mining sector, such as Chile and Peru, posted the highest returns on FDI as commodity prices rose. However, Brazil is one example of a country that has seen a notable rise in FDI income even though the transnational corporations operating there are not concentrated in the extractive industries. Chile and Brazil are

[14] Net FDI income is equivalent to the profits made by transnational corporations in countries in the region minus the profits made by trans-Latin corporations abroad.

among the few economies for which there are data on FDI income by sector. In terms of average profitability across sectors, the mining sector in Chile stands out for its returns of up to 25% in 2010. But other sectors have also been very profitable, including public utilities (electricity, gas and water), which have achieved returns of 10% that same year. In Brazil, mining and oil were not among the most profitable sectors for transnational corporations; rather, automotive manufacturing and cement production reached return levels above 10%.

Figure I.21
Latin America and the Caribbean: FDI stock and average profitability of FDI, 2001-2014
(Billions of dollars and percentages)

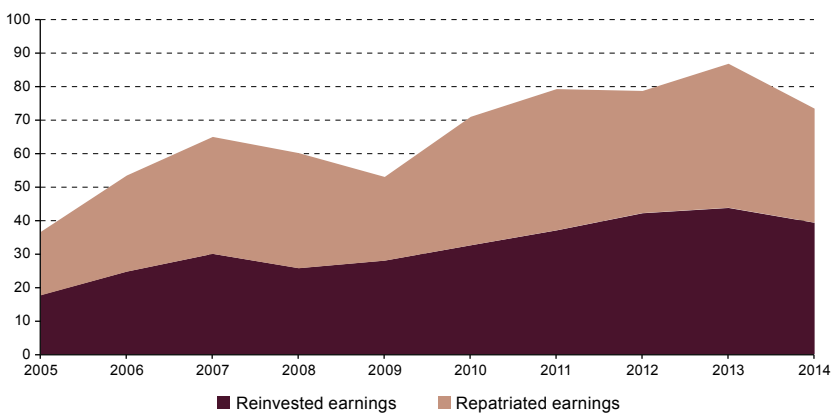


Source: Economic commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and estimates as of 18 May 2015.

While the earnings generated in the extractive industries are higher, the effects on the balance of payments may actually be milder if these income flows are offset by increased exports of commodities. Export-oriented FDI can compensate for the profits it repatriates with the value of the exports it generates. By contrast, FDI income in market-seeking activities may put more pressure on the current account as they are not offset by exports.

It is important to note that not all FDI income recorded as a debit in the current account leaves the country. In fact, about 50% of FDI income is reinvested in the same economies —a proportion that has remained relatively stable over the years. In 2009, when the financial crisis had an impact on FDI income, transnational corporations maintained their level of reinvested earnings and reduced profit repatriations (see figure I.22).

Figure I.22
Latin America and the Caribbean: [a] reinvested and repatriated FDI income, 2005-2014
(Billions of dollars)



Source: Economic commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and estimates as of 18 May 2015.
[a] The figures shown here do not include Brazil, since that country did not report reinvested earnings under the fifth edition Balance of Payments Manual methodology it used until recently.

Reinvested earnings are recorded as both a debit on the current account and as a liability on the capital account. This alleviates the pressure on the external accounts, but only at the cost of accumulating a higher liability in the form of FDI stock. In fact, most countries in the region have been financing their current account deficits with large inflows of capital, mainly FDI.

As noted above, the ever-burgeoning FDI stock will have a long-term impact on the current account as FDI income swells. In fact, taking into account capital inflows and profit outflows, FDI is already having a negative impact on the balance of payments in some countries in the region. Over the past decade, outflows of FDI income from Chile, Colombia, Peru and the Plurinational State of Bolivia have exceeded the FDI inflows received.

Of course, in the same way that transnationals' profits in the region are marked as debits on the current account, the profits made by trans-Latin corporations abroad are registered as credits. This should offset the negative effect on the current account of the repatriated earnings flowing out of the region, but so far it has had a limited effect: FDI income outflows total some US$ 100 billion, whereas FDI income inflows have yet to exceed US$ 15 billion and are concentrated in only a few countries.

Overall, the current account deficits posted in most Latin American and Caribbean economies and the role that FDI income has played in them highlight the fact that FDI, as is the case for other forms of external capital, carries a cost. While FDI has been praised for its stability (it rarely turns negative), its persistent effects on the current account are significant. In order to offset these effects, FDI should promote changes in the production structure that could boost exports in the future. Even in industries where large FDI flows have clearly increased production capacities (such as the automotive industry), the shallowness of local value chains turns these industries into net importers as well.

F. Conclusions

FDI inflows into Latin America and the Caribbean fell by 16% in 2014. That fall was somewhat larger than expected and has been amplified by a number of one-off events, mostly the Grupo Modelo acquisition in Mexico, which inflated the FDI figures in 2013, and the nationalization of YPF in Argentina, which was settled in 2014 and represented a large divestment.

The drop in commodity prices, which began in 2012 for metals and spread to oil in the second half of 2014, led to a sizeable reduction of FDI in natural resources in the region. This represented an important change in the cycle, as FDI had been responsible, to a large extent, for the reprimarization of some economies in the region in the previous decade. Falling investment in the natural resources sector was partially offset by increasing investment in the services sector, especially in market-seeking services. Manufacturing received significant FDI inflows, but mainly in the larger economies.

FDI outflows also decreased significantly from US$ 33.251 billion in 2013 to US$ 29.162 billion in 2014. The great majority of outflows still originate in a few Latin American countries and are directed towards other economies within the region. Developed countries receive some investment from the trans-Latins, but the outflows to developing countries outside the region are very small. Overall, trans-Latin corporations are not sufficiently diversified geographically to avoid being affected by the adverse economic environment in the region.

Although the average profitability of FDI has declined in recent years, FDI income is having an ever greater negative impact on the balance of payments. FDI income was responsible for a large share of the current account deficit in 2014, which reached 2.7% of GDP. Addressing that growing deficit requires a large capital account surplus, which can be partially funded through FDI itself.

In a context of subdued economic growth and lower international demand for its key exports, Latin American and Caribbean economies will need to attract FDI projects that can raise production capacity and help diversify their economies.

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Annex

Table I.A.1

Latin America and the Caribbean: inward foreign direct investment by country, 2001-2014

(Millions of dollars)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Antigua and Barbuda	112	80	179	95	238	361	341	161	85	101	68	138	101	167
Argentina	2 166	2 149	1 652	4 125	5 265	5 537	6 473	9 726	4 017	11 333	10 840	15 324	11 301	6 612
Bahamas	234	238	292	532	641	843	887	1 032	753	960	971	575	410	374
Barbados	87	81	167	127	240	342	476	464	247	290	384	436	5	275
Belize	61	25	-11	111	127	109	143	170	109	97	95	189	95	141
Bolivia (Plurinational State of)	706	677	197	85	-288	281	366	513	423	643	859	1 060	1 750	648
Brazil	22 457	16 590	10 144	18 146	15 066	18 822	34 585	45 058	25 949	48 506	66 660	65 272	63 996	62 495
Chile	4 200	2 550	4 334	7 241	7 482	8 798	13 178	16 604	13 392	15 510	23 309	28 457	19 264	22 002
Colombia	2 542	2 134	1 720	3 116	10 235	6 751	8 886	10 565	8 035	6 430	14 648	15 039	16 199	16 054
Costa Rica	460	659	575	794	861	1 469	1 896	2 078	1 347	1 466	2 178	2 332	2 677	2 106
Dominica	21	21	32	27	32	29	48	57	43	25	14	29	26	36
Dominican Republic	1 079	917	613	909	1 123	1 085	1 667	2 870	2 165	2 024	2 277	3 142	1 991	2 209
Ecuador	1 330	783	872	837	493	271	194	1 058	308	163	644	585	731	774
El Salvador	0	0	0	0	512	227	1 447	539	294	-230	218	482	179	275
Grenada	61	57	91	66	73	96	172	141	104	64	45	34	114	40
Guatemala	499	205	263	296	508	592	745	754	600	806	1 026	1 244	1 295	1 396
Guyana	56	44	26	30	77	102	152	178	164	198	247	294	214	255
Haiti	4	6	14	6	26	161	75	29	55	178	119	156	186	99
Honduras	304	275	403	547	600	669	928	1 006	509	969	1 014	1 059	1 060	1 144
Jamaica	614	481	721	602	682	882	866	1 437	541	228	218	413	654	699
Mexico	30 029	24 027	18 888	25 127	24 694	20 901	32 213	28 574	17 644	25 962	23 560	18 998	44 627	22 795
Nicaragua	150	204	201	250	241	287	382	627	434	490	936	768	816	840
Panama	405	78	771	1 012	1 027	2 498	1 777	2 402	1 259	2 363	3 132	2 980	4 654	4 719
Paraguay	70	6	25	28	35	95	202	209	95	210	619	738	72	236
Peru	1 144	2 156	1 335	1 599	2 579	3 467	5 491	6 924	6 431	8 455	7 665	11 918	9 298	7 607
Saint Kitts and Nevis	90	81	78	63	104	115	141	184	136	119	112	110	139	120
Saint Lucia	63	57	112	81	82	238	277	166	152	127	100	78	95	75
Saint Vincent and the Grenadines	21	34	55	66	41	110	121	159	111	97	86	115	160	139
Suriname	-27	-74	-76	-37	28	-163	-247	-231	-93	-248	70	121	138	4
Trinidad and Tobago	835	791	808	998	940	883	830	2 801	709	549	1 831	2 453	1 995	1 394
Uruguay	297	194	416	332	847	1 493	1 329	2 106	1 529	2 289	2 504	2 536	3 032	2 755
Venezuela (Bolivarian Republic of)	3 683	782	2 040	1 483	2 589	-508	3 288	2 627	-983	1 574	5 740	5 973	2 680	320

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of estimates and official figures as of 18 May 2015.

Table I.A.2
Latin America and the Caribbean: inward foreign direct investment by destination sector, 2006-2014
(Millions of dollars)

	2006	2007	2008	2009	2010	2011	2012	2013	2014
Argentina [a]									
Natural resources	272	546	426	-37	1 148	930	708	902	…
Manufactures	1 291	1 698	3 249	2 307	2 511	4 063	4 354	3 692	…
Services	5 837	5 310	7 505	1 082	6 741	5 662	7 721	7 648	…
Belize									…
Natural resources	12	9	37	7	13	29	100	22	16
Manufactures	0	0	0	0	0	0	0	0	0
Services	83	101	117	93	79	59	90	64	116
Other	14	34	16	9	5	5	6	9	9
Bolivia (Plurinational State of) [b]									
Natural resources	390	486	859	420	530	622	1 166	1 550	1 558
Manufactures	67	164	154	74	274	240	119	317	390
Services	126	303	290	193	132	171	220	162	164
Brazil									…
Natural resources	1 542	4 806	15 085	7 487	18 358	6 296	9 044	16 782	7 046
Manufactures	8 462	16 074	15 796	12 796	20 416	31 664	25 612	21 140	22 228
Services	12 702	13 147	13 704	6 334	9 509	28 493	30 454	26 001	33 138
Chile									
Natural resources	3 283	6 495	4 599	7 125	5 196	17 913	12 852	2 317	…
Manufactures	1 154	-657	1 570	421	595	942	2 095	671	…
Services	2 617	6 481	8 725	3 933	6 927	4 249	8 491	10 089	…
Other	244	215	256	1 409	3 008	339	5 104	7 181	…
Colombia									
Natural resources	3 797	4 452	5 176	5 672	4 976	7 336	7 970	8 385	6 618
Manufactures	815	1 760	1 696	1 364	210	1 214	1 985	2 590	2 928
Services	2 138	2 673	3 693	1 000	1 244	6 098	5 084	5 224	6 508
Costa Rica									
Natural resources	59	33	467	73	31	38	-17	-5	7
Manufactures	439	689	555	407	966	737	634	306	419
Services	961	1 170	1 031	845	446	1 401	1 715	2 375	1 680
Other	10	4	26	22	23	2	0	0	0
Ecuador									
Natural resources	-69	-77	265	58	189	380	243	279	528
Manufactures	90	99	198	118	120	122	136	138	109
Services	250	173	595	132	-143	142	207	314	137
El Salvador									
Natural resources	29	10	5	1	1	-1	-3	6	1
Manufactures	17	21	28	56	-65	149	-47	285	87
Services	182	1 315	480	165	-166	70	531	-112	187
Other (maquila)	-0	101	26	72	0	0	0	0	0

Table I.A.2 (concluded)

	2006	2007	2008	2009	2010	2011	2012	2013	2014
Guatemala									
Natural resources	0	70	174	139	120	325	418	335	324
Manufactures	0	210	175	51	299	150	145	186	183
Services	0	437	369	401	363	544	636	707	824
Other	0	28	36	9	23	7	46	67	65
Honduras									
Natural resources	86	30	4	10	84	62	41	70	65
Manufactures	228	384	267	98	341	392	438	325	347
Services	356	513	736	402	545	560	579	665	733
Other	0	0	0	0	0	0	0	0	0
Dominican Republic									
Natural resources	107	30	357	758	240	1 060	1 169	93	-39
Manufactures	-168	184	574	280	566	355	1 257	404	607
Services	1 146	1 453	1 938	1 128	1 218	862	716	1 494	1 640
Mexico									
Natural resources	485	1 891	4 549	1 350	1 453	846	3 006	5 443	2 299
Manufactures	10 232	12 901	8 662	6 613	13 918	10 099	7 830	29 595	12 870
Services	10 183	17 421	15 362	9 680	10 591	12 615	8 163	9 161	7 399
Nicaragua									
Natural resources	15	11	57	47	77	191	123	272	199
Manufactures	63	121	122	70	108	226	302	234	270
Services	209	250	447	318	323	550	347	346	189
Other	0	0	0	0	0	0	22	129	182
Panama									
Natural resources	1	-59	-59	-34	77	94	1 164	31	…
Manufactures	129	161	161	104	-114	298	520	364	…
Services	1 765	2 106	2 106	1 190	2 760	2 761	1 296	4 259	…
Other	2	-11	-11	0	0	0	0	0	…
Paraguay									
Natural resources	-36	-2	3	8	-6	14	35	43	5
Manufactures	60	8	149	-109	53	105	290	-36	76
Services	70	196	56	195	163	500	413	65	155
Uruguay									
Natural resources	328	338	604	253	329	383	220	378	…
Manufactures	96	263	261	242	131	190	340	240	…
Services	594	592	1 003	962	1 010	1 360	1 536	1 642	…
Other	476	136	238	71	820	572	440	770	…

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of estimates and official figures as of 18 May 2015.
[a] Data from the Central Bank of the Republic of Argentina.
[b] Gross foreign direct investment flows, excluding divestments.

Table I.A.3
Latin America and the Caribbean: inward foreign direct investment by country of origin, 2006-2014
(Millions of dollars)

	2006	2007	2008	2009	2010	2011	2012	2013	2014
Argentina [a]									
United States	1 375	737	2 562	1 751	2 081	2 854	3 445	5 045	…
Netherlands	616	583	1 171	-120	-44	639	2 105	1 506	…
Spain	1 520	1 161	-2 709	1 237	1 247	-459	-918	1 186	…
Germany	258	363	328	312	635	267	617	999	…
Canada	67	629	885	-186	644	434	1 453	775	…
Brazil	437	847	1 436	-152	1 667	1 883	1 580	699	…
France	133	872	368	48	158	132	471	538	…
Italy	-7	271	227	78	201	336	186	436	…
Bolivia (Plurinational State of) [b]									
Spain	4	50	25	145	271	246	364	676	537
United Kingdom	17	24	48	70	11	2	111	309	442
Peru	26	35	26	40	82	12	56	102	442
France	38	13	36	22	89	55	73	220	200
United States	272	322	295	162	85	76	89	61	140
Brazil [c]									
Netherlands	3 317	7 634	3 916	4 260	2 736	17 908	12 003	13 120	24 591
United States	2 784	3 744	5 007	1 963	5 348	5 572	13 509	8 742	11 505
Luxembourg	397	5 864	6 292	-483	9 132	2 452	7 648	9 311	8 679
Spain	749	1 787	2 572	3 262	313	9 779	2 073	2 307	6 356
Switzerland	0	0	0	0	6 547	1 415	5 017	3 303	4 688
France	555	1 015	2 231	2 231	3 029	4 383	2 760	2 964	3 947
Japan	826	81	4 316	1 709	2 426	7 387	1 255	3 193	3 548
Germany	0	0	0	0	498	1 434	1 171	1 539	2 670
Chile									
United States	111	3 726	2 272	763	2 962	2 746	3 332	5 084	…
Spain	822	1 088	2 210	1 870	1 507	2 063	1 335	3 689	…
Canada	498	2 612	1 667	308	2 716	3 961	6 471	3 422	…
Japan	159	236	-28	1 116	207	1 559	545	1 696	…
Netherlands	327	805	824	1 377	79	716	641	984	…
Colombia									
Switzerland	65	122	140	166	180	994	698	2 084	2 814
Panama	330	839	1 141	789	1 368	3 508	2 395	2 055	2 453
United States	2 636	2 697	2 874	2 343	1 593	2 155	2 476	2 861	2 213
Spain	671	572	1 040	830	113	1 164	628	951	2 155
United Kingdom	906	1 580	1 505	1 400	949	1 408	1 357	1 416	1 080
Bermuda	396	82	404	645	624	924	367	846	1 070
Costa Rica									
United States	821	962	1 328	1 022	1 031	1 376	1 051	1 216	1 004
Spain	13	57	141	79	28	247	318	214	212
Mexico	22	71	20	7	40	183	346	147	182
Panama	28	-3	20	22	31	-3	12	283	120
Canada	345	97	64	33	49	42	8	42	100
Colombia	-3	30	50	6	101	152	112	69	88

Table I.A.3 (continued)

	2006	2007	2008	2009	2010	2011	2012	2013	2014
Dominican Republic									
United States	662	536	360	455	1055	499	252	374	321
Mexico	84	-124	1055	273	433	73	-32	6	244
Canada	142	113	383	773	696	1126	851	143	158
Netherlands	41	54	-73	96	50	28	10	83	70
Venezuela (Bolivarian Republic of)	17	53	11	31	208	70	55	47	44
Ecuador									
Canada	-252	49	58	65	105	252	59	28	229
China	12	85	47	56	45	80	86	94	79
Spain	7	85	190	51	-17	52	50	71	77
Netherlands	38	8	-8	-4	11	7	11	48	76
Uruguay	15	2	-37	-13	40	3	6	115	62
Switzerland	7	1	34	24	6	8	18	9	28
El Salvador									
Luxembourg	0	0	0	0	-309	-41	85	42	157
Spain	0	0	0	0	-41	-0	18	170	141
United States	13	499	129	74	-124	23	6	-72	101
Guatemala									
United States	4	326	229	151	343	127	227	212	358
Canada	198	25	54	74	114	305	290	269	188
Mexico	0	76	76	50	97	81	96	114	157
Colombia	0	3	15	21	22	155	48	167	136
United Kingdom	83	63	66	58	-25	121	74	-19	107
Russian Federation	0	0	0	0	0	13	134	187	86
Spain	0	13	22	6	43	4	29	17	55
Honduras									
Mexico	38	92	30	168	124	154	192	266	201
United States	339	460	449	92	185	141	173	128	154
Luxembourg	0	0	0	171	133	149	124	150	147
Canada	107	139	51	-39	159	187	132	114	115
Panama	16	22	16	1	14	16	22	63	109
Guatemala	17	15	44	14	61	44	52	37	73
Mexico									
United States	13 263	13 000	11 678	7 340	6 994	12 196	9 417	13 141	6 516
Spain	1 461	5 458	4 998	3 004	4 185	3 446	-781	-218	4 093
Canada	966	835	3 438	1 832	1 856	1 400	1 768	4 351	2 421
Germany	751	649	657	-32	334	378	946	1 773	1 546
Netherlands	2 805	6 656	1 900	2 633	9 222	2 783	1 460	5 257	1 490
Japan	-1 434	440	519	483	536	916	1 816	1 643	1 434
Belgica	69	228	142	346	38	164	0	13 290	1 262

Table I.A.3 (concluded)

	2006	2007	2008	2009	2010	2011	2012	2013	2014
Nicaragua									
United States	53	84	126	88	88	159	121	244	…
Mexico	53	128	164	48	90	115	149	125	…
Venezuela (Bolivarian Republic of)	0	47	132	147	29	45	210	108	…
Panama	101	5	4	1	1	34	78	77	…
Spain	10	45	59	25	33	116	-19	74	…
Panama									
Colombia	70	134	60	135	82	486	429	1125	…
United States	117	163	224	-19	1120	652	-16	789	…
Belgium	0	0	0	0	11	23	-130	428	…
Switzerland	132	146	122	301	444	216	139	379	…
Japan	44	60	-50	4	26	6	-4	281	…
South Africa	17	13	19	26	879	191	612	246	…
Mexico	51	60	69	154	-9	171	-146	217	…
Paraguay									
United States	84	107	190	111	255	354	59	-128	141
Brazil	52	41	42	-26	29	90	177	83	135
Netherlands	2	-30	20	-28	4	11	34	79	25
United Kingdom	-1	1	-2	3	2	19	50	25	20
Spain	7	19	11	16	19	-10	63	-9	17
Trinidad and Tobago									
United States	627	574	403	469	363	488	560	1272	361
India	27	21	16	17	13	2	1	2	348
Canada	3	3	2194	4	3	994	1586	357	248
United Kingdom	150	159	146	152	118	64	25	21	31
Uruguay									
Argentina	282	373	534	432	588	809	975	672	…
Brazil	56	86	183	110	108	170	178	255	…
Netherlands	-18	10	14	110	-2	172	78	171	…
Spain	81	153	232	55	75	194	136	132	…
France	7	25	17	23	35	-132	4	118	…
United States	67	43	144	167	-36	77	88	87	…

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of estimates and official figures as of 18 May 2015.
[a] Data from the Central Bank of the Republic of Argentina.
[b] Gross foreign direct investment flows, excluding divestments.
[c] The data for 2014 are standardized according to the methodology of the sixth edition of the *Balance of Payments Manual* of the International Monetary Fund (IMF).

Table I.A.4
Latin America and the Caribbean: inward foreign direct investment by component, 2006-2014
(Millions of dollars)

	2006	2007	2008	2009	2010	2011	2012	2013	2014
Antigua and Barbuda									
Capital contributions	335	328	149	79	96	61	110	65	137
Inter-company loans	18	0	0	1	1	2	6	29	23
Reinvested earnings	9	12	12	5	5	5	22	7	7
Argentina									
Capital contributions	2 166	2 578	4 552	2 133	2 504	4 508	4 861	2 784	-1 184
Inter-company loans	263	1 846	4 777	-1 010	3 507	2 600	3 120	1 601	0
Reinvested earnings	3 108	2 050	396	2 894	5 322	3 732	7 343	6 916	7 365
Bahamas									
Capital contributions	843	887	1 032	753	960	971	575	410	374
Inter-company loans	0	0	0	0	0	0	0	0	0
Reinvested earnings	0	0	0	0	0	0	0	0	0
Barbados									
Capital contributions	265	420	339	140	222	218	225	112	185
Inter-company loans	49	24	80	94	41	178	53	-43	63
Reinvested earnings	28	32	45	13	27	-12	158	-64	27
Belize									
Capital contributions	98	100	141	80	80	103	193	98	134
Inter-company loans	-15	13	8	6	2	1	0	0	0
Reinvested earnings	25	30	21	23	15	-8	-4	-6	7
Bolivia (Plurinational State of) [a]									
Capital contributions	11	27	45	1	1	5	19	17	313
Inter-company loans	306	654	850	177	141	130	282	331	889
Reinvested earnings	266	272	407	509	793	899	1 204	1 682	910
Brazil									
Capital contributions	15 373	26 074	30 064	19 906	40 117	54 782	52 838	41 644	47 303
Inter-company loans	3 450	8 510	14 994	6 042	8 390	11 878	12 434	22 352	15 192
Reinvested earnings	...	...	...	...	...	...	...	...	...
Chile									
Capital contributions	1 980	2 622	7 775	1 905	4 662	10 921	8 532	4 679	10 347
Inter-company loans	-325	374	2 232	967	2 985	3 162	10 841	8 329	7 248
Reinvested earnings	7 143	10 182	6 597	10 519	7 863	9 226	9 085	6 256	4 406
Colombia									
Capital contributions	5 193	7 462	7 827	4 907	3 741	8 282	9 088	9 737	9 394
Inter-company loans	-31	-396	461	731	-635	1 872	1 239	2 368	2 493
Reinvested earnings	1 495	1 983	2 332	2 396	3 325	4 494	4 712	4 094	4 167
Costa Rica									
Capital contributions	1 034	1 377	1 594	1 050	818	959	721	1 644	1 199
Inter-company loans	25	-2	39	-174	150	711	759	187	467
Reinvested earnings	410	521	446	471	497	509	853	845	440
Dominica									
Capital contributions	5	28	39	24	9	5	16	13	22
Inter-company loans	19	9	9	13	13	7	9	8	8
Reinvested earnings	5	10	9	6	3	2	4	5	5

Table I.A.4 (continued)

	2006	2007	2008	2009	2010	2011	2012	2013	2014
Dominican Republic [b]									
Capital contributions	765	1 616	2 199	704	1 333	1 342	1 900	1 036	...
Inter-company loans	-394	-446	278	1 096	614	468	904	471	...
Reinvested earnings	714	498	394	365	351	464	780	401	...
Ecuador									
Capital contributions	136	151	229	278	265	252	227	424	653
Inter-company loans	-260	-368	530	-226	-315	64	57	-3	-193
Reinvested earnings	395	411	298	256	213	328	301	310	314
Grenada									
Capital contributions	71	140	128	97	56	39	29	109	35
Inter-company loans	12	17	1	2	3	1	0	0	0
Reinvested earnings	12	15	12	5	5	5	5	5	5
Guatemala									
Capital contributions	87	260	198	94	265	198	446	208	131
Inter-company loans	-21	-30	75	19	-102	58	219	416	316
Reinvested earnings	526	515	482	488	643	770	580	672	949
Honduras									
Capital contributions	204	220	568	84	29	284	310	174	174
Inter-company loans	46	203	-40	65	378	56	52	240	355
Reinvested earnings	419	505	479	360	562	674	697	645	615
Mexico									
Capital contributions	6 574	17 761	12 305	11 204	15 160	9 396	4 325	21 622	4 235
Inter-company loans	6 221	5 992	7 298	1 545	5 880	4 730	6 114	7 134	5 565
Reinvested earnings	8 106	8 460	8 970	4 895	4 921	9 433	8 559	15 443	12 769
Panama									
Capital contributions	1 929	719	918	898	948	759	1 561	1 340	1 402
Inter-company loans	364	178	136	105	540	1 224	682	540	340
Reinvested earnings	205	879	1 348	257	874	1 150	737	2 773	2 977
Paraguay									
Capital contributions	60	43	20	173	-9	391	439	242	126
Inter-company loans	-11	129	132	-102	129	300	61	-322	4
Reinvested earnings	46	30	57	23	91	-73	238	151	106
Peru									
Capital contributions	874	733	2 981	1 828	2 445	896	5 393	2 460	1 342
Inter-company loans	240	924	656	-782	693	2 117	-508	3 075	2 287
Reinvested earnings	2 353	3 835	3 287	5 385	5 317	4 652	7 033	3 764	3 978
Saint Kitts and Nevis									
Capital contributions	107	135	178	132	116	107	106	137	118
Inter-company loans	5	3	3	1	1	1	2	0	0
Reinvested earnings	2	2	2	2	2	4	1	1	1
Saint Lucia									
Capital contributions	220	254	135	135	109	80	54	76	53
Inter-company loans	6	8	21	13	13	15	16	10	11
Reinvested earnings	11	15	11	3	4	5	8	9	11

Table I.A.4 (concluded)

	2006	2007	2008	2009	2010	2011	2012	2013	2014
Saint Vincent and the Grenadines									
Capital contributions	94	102	142	100	91	79	112	157	136
Inter-company loans	3	8	8	8	2	2	2	2	2
Reinvested earnings	13	11	9	2	4	4	1	1	1
Suriname									
Capital contributions	0	0	0	0	0	0	0	0	0
Inter-company loans	-163	-247	-231	-93	-248	-51	113	71	-21
Reinvested earnings	...	...	...	...	...	121	11	69	27
Trinidad and Tobago									
Capital contributions	497	554	2 322	426	309	0	1	0	0
Inter-company loans	-20	-21	-16	-12	-11	136	698	1 040	661
Reinvested earnings	406	297	495	296	251	1 696	1 754	954	732
Uruguay									
Capital contributions	576	550	1 012	990	1 617	1 412	1 665	1 866	2 111
Inter-company loans	699	448	540	82	8	263	94	306	-79
Reinvested earnings	219	331	554	457	664	828	777	860	722
Venezuela (Bolivarian Republic of)									
Capital contributions	-134	-806	302	-3 348	-1 319	-495	-307	-79	...
Inter-company loans	-2 323	773	-11	367	1 457	2 752	3 292	1 784	...
Reinvested earnings	1 949	3 321	2 336	1 998	1 436	3 483	2 988	975	...

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of estimates and official figures as of 18 May 2015.
[a] Gross foreign direct investment flows, excluding divestments.
[b] Data standardized according to the methodology of the fifth edition of the *Balance of Payments Manual* of the International Monetary Fund (IMF).

Table I.A.5
Latin America and the Caribbean: inward foreign direct investment stock by country, 2001-2014
((Millions of dollars and percentages of GDP)

	2001	2005	2011	2012	2013	2014	2001	2005	2011	2012	2013	2014
	(millions of dollars)						*(percentages of GDP)*					
Argentina	79 504	55 139	93 199	100 821	111 361	114 076	25	25	17	17	18	21
Bolivia (Plurinational State of)	5 893	4 905	7 749	8 809	10 558	11 206	72	51	32	33	35	33
Brazil	121 949	181 344	696 408	743 964	747 891	754 101	22	20	27	31	31	32
Chile	43 482	78 993	175 753	205 999	214 378	224 573	60	63	70	78	77	87
Colombia	15 377	36 987	97 364	112 926	128 182	141 667	16	25	29	31	34	38
Costa Rica	3 185	5 417	16 225	18 811	21 789	24 309	19	27	39	42	44	49
Dominican Republic	2 752	8 866	22 129	25 143	26 660	29 035	11	25	38	42	44	45
Ecuador	6 876	9 861	12 501	13 086	13 817	14 591	28	24	16	15	15	15
El Salvador	2 252	4 167	8 120	8 789	8 918	9 358	16	24	35	37	37	37
Guatemala	3 918	3 319	7 751	8 938	10 255	12 102	21	12	16	18	19	21
Haiti	99	150	784	963	...	...	3	4	10	12	...	...
Honduras	1 585	2 870	7 965	9 024	10 084	11 228	21	29	45	49	55	57
Jamaica	3 931	6 919	11 110	11 988	12 457	13 159	43	62	77	81	87	93
Mexico	157 305	234 149	338 975	366 564	391 879	337 750	23	27	29	31	31	26
Nicaragua	1 565	2 461	5 617	6 385	7 200	8 040	29	39	58	61	66	68
Panama	7 314	10 167	23 875	26 762	31 413	35 917	58	62	72	71	74	77
Paraguay	1 016	1 127	3 947	5 288	5 076	5 381	13	13	16	21	18	18
Peru	11 835	15 889	50 641	62 559	71 857	79 429	23	21	30	32	36	39
Suriname	...	...	742	866	1 006	1 012	...	...	17	17	19	18
Uruguay	2 406	2 844	15 147	17 407	19 564	...	12	16	32	34	34	...
Venezuela (Bolivarian Republica of)	39 074	44 518	44 576	49 079	55 766	...	32	31	14	13	14	...

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of estimates and official figures as of 18 May 2015.

Table I.A.6

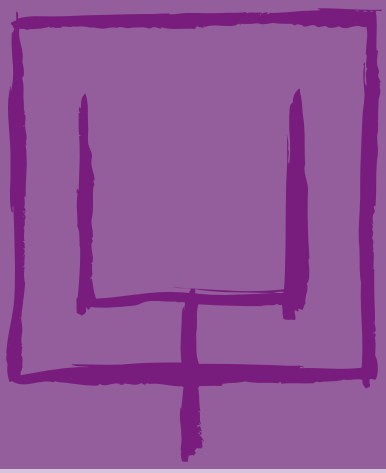
Latin America and the Caribbean: outward foreign direct investment flows by country, 2001-2014

(Millions of dollars)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Antigua and Barbuda	13	14	13	15	17	2	2	2	4	5	3	4	6	6
Argentina	161	-627	774	676	1 311	2 439	1 504	1 391	712	965	1 488	1 055	1 097	2 117
Bahamas	42	28	46	86	78	136	141	171	89	88	304	49	28	122
Barbados	1	0	1	4	9	44	82	-6	-56	-54	301	-129	106	93
Belize	0	0	0	0	1	1	1	3	0	1	1	1	1	3
Bolivia (Plurinational State of)	3	3	3	3	3	3	4	5	-4	-29	0	0	0	0
Brazil	-2 258	2 482	249	9 807	2 517	28 202	7 067	20 457	-10 084	11 588	-1 029	-2 821	-3 495	-3 540
Chile	1 610	343	1 709	2 145	2 135	2 212	4 852	9 151	7 233	9 461	20 252	20 555	10 308	12 052
Colombia	16	857	938	192	4 796	1 268	1 279	3 085	3 505	5 483	8 420	-606	7 652	3 899
Costa Rica	10	34	27	61	-43	98	262	6	7	26	58	428	290	218
Dominica	4	1	0	1	13	3	7	0	1	1	0	0	2	2
El Salvador	0	0	19	0	113	0	95	80	0	5	-0	-2	3	1
Grenada	2	3	1	1	3	6	16	6	1	3	3	3	3	...
Guatemala	10	22	46	41	38	40	25	16	26	24	17	39	34	31
Honduras	3	7	12	-6	1	1	1	-1	4	-1	2	55	26	...
Jamaica	89	74	116	60	101	85	115	76	61	58	75	24	73	...
Mexico	4 404	891	1 253	4 432	6 474	5 758	8 256	1 157	9 604	15 050	12 636	22 470	13 138	7 610
Paraguay	6	6	6	6	6	7	7	8	8	7	0	0	0	0
Peru	237	-522	773	258	868	1 327	987	-200	3 176	1 038	1 450	2 330	1 154	4 452
Saint Kitts and Nevis	2	1	2	7	11	4	6	6	5	3	2	2	2	2
Saint Lucia	4	5	5	5	4	4	6	5	6	5	4	4	3	3
Saint Vincent and the Grenadines	0	0	0	0	1	1	2	0	1	0	0	0	0	0
Suriname	0	0	0	0	0	0	0	0	0	0	3	-1	0	0
Trinidad and Tobago	58	106	225	25	341	370	0	700	0	0	1 060	1 681	2 061	1 055
Uruguay	-6	-14	-15	-18	-36	1	-89	11	-16	60	7	3	5	13
Venezuela (Bolivarian Republic of)	204	1 026	1 318	619	1 167	1 524	-495	1 311	2 630	2 492	-370	4 294	752	1 024

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of estimates and official figures as of XX May 2015.

Chapter II



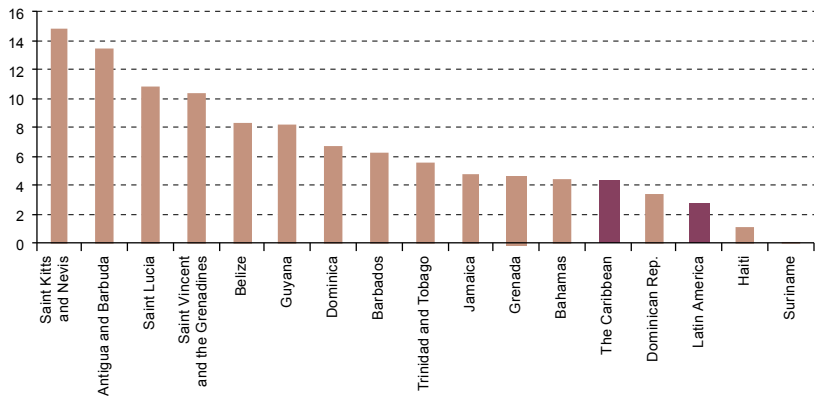
Foreign direct investment in the Caribbean

Introduction

Foreign direct investment (FDI) is very important for the Caribbean. These economies receive substantial FDI flows relative to their size, and a large share of their economic activity is conducted by transnational corporations. The ratio of inward FDI to gross domestic product (GDP) last year was 4.2% for the whole subregion and over 10% in several economies (see figure II.1). By way of comparison, the ratio is 2.6% in Latin America and lower, if anything, in other developing regions. Even compared with other small economies such as Pacific island States, Caribbean economies receive particularly high levels of FDI in relation to their economic size.

This chapter reviews the current state of affairs with respect to Caribbean FDI flows. The next section provides some background on the Caribbean context, and it is followed by a section detailing medium- and short-run trends in FDI flows into the region on a country-by-country basis. After this comes an analysis of some of the sectors that are most important for the Caribbean. This chapter then discusses the extensive and costly use of FDI promotion policies in the region before addressing the importance of trans-Caribbean enterprises and drawing some conclusions in its final section.

Figure II.1
The Caribbean (selected economies): inward foreign direct investment as a proportion of GDP, 2014
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures as of 18 May 2015.

A. Background

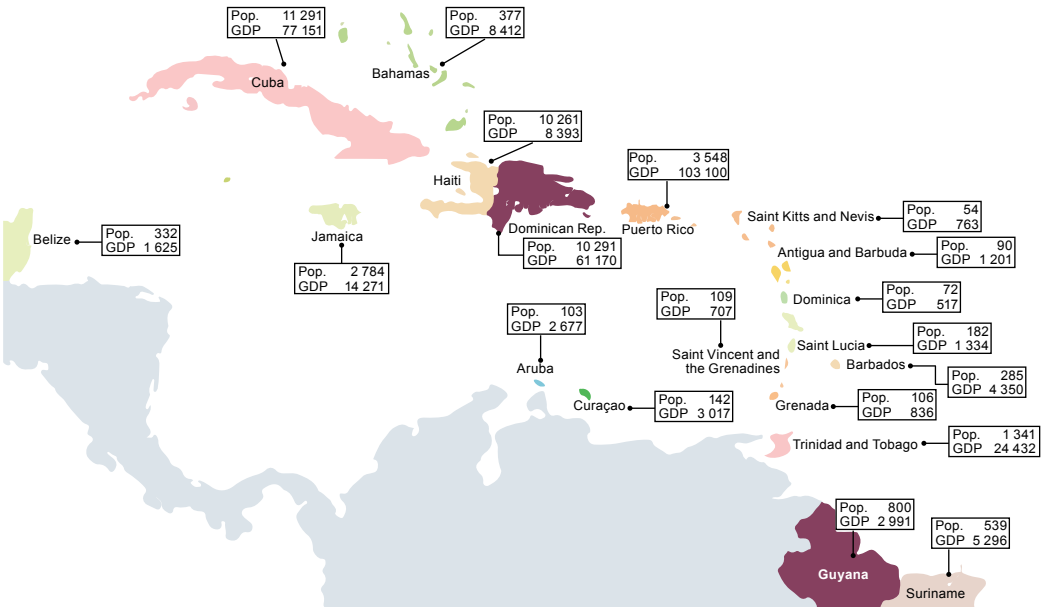
The Caribbean subregion discussed in this study comprises the following ECLAC member States: Antigua and Barbuda, the Bahamas, Barbados, Belize, Dominica, Dominican Republic, Grenada, Guyana, Haiti, Jamaica, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Suriname and Trinidad and Tobago. This chapter also treats the Dominican Republic and Haiti as part of the Caribbean subregion, although in other analyses these economies are usually dealt with separately from the English- and Dutch-speaking Caribbean because of their large populations and different historical background. Haiti is included because the small size of its economy and its economic vulnerability make it similar to other Caribbean countries. The Dominican Republic also shares features with the other Caribbean countries, even if its economic size is disproportional to that of any of the other economies in the region (see map II.1). Cuba is discussed in box II.1, but not included in the rest of the analysis owing to a lack of comparable data.

In addition to these countries, there are 13 other economies in the Caribbean that are associate members of ECLAC but not fully independent States. They are: Anguilla, Aruba, Bermuda, the British Virgin Islands, the Cayman Islands, Curaçao, Guadeloupe, Martinique, Montserrat, Puerto Rico, Sint Maarten, the Turks and Caicos Islands and the United States Virgin Islands.[1] Information on FDI inflows into most of these economies is very incomplete. The Cayman Islands and the British Virgin Islands operate as offshore financial centres for transnational corporations and, as a consequence,

[1] There is a final group of economies that are not members or associate members of ECLAC. This includes some of the Dutch Caribbean and some of the overseas regions and collectivities of France.

register huge inflows and outflows of FDI that have little relation to productive activities in those economies. Puerto Rico is the largest economy in this group and attracts large flows of FDI (more than the entire Caribbean subregion in some recent years), while many other countries do not record FDI inflows at all (see also De Groot and Pérez Ludeña, 2014, box 1).

Map II.1
The Caribbean (selected economies): population and GDP, 2013
(Thousands of inhabitants and millions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
Note: The boundaries and names shown on this map do not imply official endorsement or acceptance by the United Nations.

Most economies in the subregion have experienced economic stagnation in recent years. From 2008 to 2013, only Guyana, Haiti and Suriname had positive rates of per capita GDP growth (see table II.1). Severe budget deficits in nearly all Caribbean economies have limited the policy space available for improving the economy through government action. While Saint Kitts and Nevis had a budget surplus of 2.7% of GDP in 2014[2] and Jamaica nearly achieved a balanced budget, all other governments ran significant budget deficits, ranging from 1.3% of GDP (Haiti) to 7.7% (Saint Lucia). The average national debt reached 78.6% of GDP in 2014, exceeding 100% in Jamaica and coming close to this figure in other economies such as Antigua and Barbuda, Barbados and Saint Kitts and Nevis. Moreover, the private-sector response to the crisis was weak, leading to sluggish domestic investment. This highlights the importance of FDI as a source of investment financing in Caribbean-type economies, where domestic private investment is strongly driven by public investment.

An important characteristic of Caribbean economies is vulnerability. The report by the United Nations Conference on Trade and Development on small island developing States (UNCTAD, 2014) on the occasion of the third International Conference on Small Island Developing States in 2014 discusses the challenges of attracting FDI to such economies. Most of the economies included in its analysis are located in the Caribbean, and the challenges identified are very real, with many Caribbean economies vulnerable not only to natural disasters and climate change but also to international economic fluctuations. FDI inflows into the subregion are very large for the size of its economies, making them sensitive to variations in these inflows, with the additional implication that their productivity depends on the productivity of the FDI concerned. Next, in most of them, FDI is highly concentrated in specific sectors, such as natural resources in some countries and tourism in others, which increases exposure to sector-dependent shocks. Finally, FDI is narrowly based in terms of origin, with a great portion coming from a limited number of countries, especially Canada and the United States. As a result, shocks that affect these countries of origin are quickly transmitted to the Caribbean.

[2] In 2013, Saint Kitts and Nevis had a surplus of 14.0%, which it was forced to accumulate as part of its consolidation effort to bring down its towering debt.

Table II.1
The Caribbean (selected economies): summary statistics

	Per capita GDP, 2013 *(dollars)*	GDP growth, 2014 *(percentage annual growth rates)*	GDP growth, 2008-2013 *(percentage annual growth rates)*	Inward FDI, 2014 *(millions of dollars)*	Gross fixed capital formation, 2013 *(percentages of GDP)*	Fiscal balance, 2014 *(percentages of GDP)*	Gross public debt, 2014 *(percentages of GDP)*	Unemployment, 2014 *(percentages)*
Antigua and Barbuda	13 342	3.2	-2.8	167	24.6	-1.9	95.0	...
Bahamas	22 323	1.0	-0.4	374	26.3	-3.4	61.8	14.3
Barbados	15 264	0	-0.4	275	13.9	-7.1	97.7	11.6 [a]
Belize	4 894	3.6	2.4	141	17.8	-1.7	75.9	11.1
Dominica	7 177	2.4	0.8	36	12.0	-1.7	72.2	...
Dominican Republic	5 944	7.3	3.8	2 209	14.4	-3.0	36.4	6.8
Grenada	7 891	3.8	-0.7	40	18.6	-6.3	89.9	...
Guyana	3 739	4.5	4.2	255	18.6	-4.9	60.9	...
Haiti	818	3.5	1.9	99	15.7	-1.3	30.4 [a]	...
Jamaica	5 126	1.2	-0.8	699	21.0	-0.7	128.1	13.6
Saint Kitts and Nevis	14 133	6.3	0.0	120	29.1	2.7	95.7	...
Saint Lucia	6 486	-1.6	0.4	75	23.3	-7.7	80.2	...
Saint Vincent and the Grenadines	7 328	0.5	-0.3	139	25.2	-5.8	72.2	...
Suriname	9 826	3.5	3.9	4	41.2	-5.7	29.9	...
Trinidad and Tobago	18 219	1.8	-0.1	1 394	14.0	-2.7	62.6	3.7 [a]
The Caribbean	4 934 [b]	4.4 [b]	0.1	6 027	21.1 [b c]	-3.9	78.6	...

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of *Economic Survey of Latin America and the Caribbean 2014* (LC/G.2619-P), Santiago, Chile, 2014; and United Nations, "National Accounts Main Aggregates Database", Statistical Division, 2015.
Note: Averages for the Caribbean do not include the Dominican Republic or Haiti, unless otherwise indicated.
[a] 2013 data.
[b] Includes the Dominican Republic and Haiti.
[c] Simple average.

The activities of transnational corporations have much more impact on Caribbean economies than on those of large countries like Brazil, Chile or Mexico, even if the absolute amounts of FDI are small in comparison. Investment decisions made in Europe, the United States or Asia can have large effects on the levels of investment, employment or tax receipts in Caribbean economies because of the relative size of individual companies in those economies. Policies designed to maintain or attract FDI, including those aimed at making it easier to do business, are thus particularly important there because policy changes may affect individual companies' decisions, directly impacting local economies.

B. Trends in FDI

Taken as a whole, the Caribbean's inflow of FDI shrank from US$ 6.322 billion to US$ 6.027 billion between 2013 and 2014, a decrease of 4.7%, compared with a decrease of 16% in Latin America. However, this overall trend hides the fact that the Caribbean is a highly varied region where the different economies follow their own trends. While most economies are highly dependent on services (tourism in particular), others, such as Belize, Guyana, Suriname and Trinidad and Tobago, are primarily based on natural resources. This section discusses the medium-term trend for each of the economies, using the most recent data from 2014.Table II.2 displays the latest figures for the economies included in this chapter.

Table II.2
The Caribbean (selected economies): foreign direct investment inflows by receiving country or territory, 2008-2014

	2008	2009	2010	2011	2012	2013	2014	Absolute change, 2013-2014 *(millions of dollars)*	Relative change, 2013-2014 *(percentages)*
Antigua and Barbuda	161	85	101	68	138	101	167	66	66
Bahamas	1 032	753	960	971	575	410	374	-36	-9
Barbados	464	247	290	384	436	5	275	270	5 119
Belize	170	109	97	95	194	95	141	46	48
Dominica	57	43	25	14	29	26	36	9	36
Dominican Republic	2 870	2 165	2 024	2 277	3 142	1 991	2 209	218	11
Grenada	141	104	64	45	34	114	40	-73	-64
Guyana	178	164	198	247	294	214	255	41	19
Haiti	30	55	178	119	156	186	99	-87	-47
Jamaica	1 437	541	228	218	413	654	699	45	7
Saint Kitts and Nevis	184	136	119	112	110	139	120	-19	-13
Saint Lucia	166	152	127	100	78	95	75	-20	-21
Saint Vincent and the Grenadines	159	111	97	86	115	160	139	-21	-13
Suriname	-231	-93	-248	70	121	138	4	-134	-97
Trinidad and Tobago	2 801	709	549	1 831	2 453	1 995	1 394	-601	-30
Total	9 618	5 281	4 809	6 637	8 289	6 322	6 027	-302	-5

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures as of May 2015.

1. Hispaniola

The **Dominican Republic** is the largest economy in the Caribbean after Cuba and the largest recipient of FDI. All sectors are open to FDI and there is a strong presence of transnational corporations in most of them, with the partial exceptions of financial services and agriculture. FDI inflows peaked at more than US$ 3 billion in 2012, when the country's largest beer company was acquired for US$ 1.2 billion. Inflows were just shy of US$ 2 billion in 2013 and increased by 11% in 2014.

Tourism was the largest recipient of FDI for many years, and although investments declined after the 2009 financial crisis, they picked up again from 2013. Around the year 2000, the country also received large investments in public utilities in connection with a privatization programme that, at least in the electricity sector, was recently reversed. FDI has also been important in developing export manufacturing, although the sums invested have never been very large. The largest investment of the past few years has been in the Pueblo Viejo gold mine, acquired by Barrick of Canada. Almost exclusively because of this project, FDI in natural resources averaged over US$ 700 million between 2008 and 2012, while the mine was being developed. Transnational corporations' profits have been high in the Dominican Republic as a consequence of strong economic growth and new mining exports. At over 10% in the last decade, average returns are the highest in the Caribbean and the fifth-highest in Latin America. Income from FDI was US$ 2 billion in the past three years, putting it almost on a par with FDI inflows.

Mexico's América Móvil started to roll out a 4G mobile service during 2014; this has cost US$ 225 million to date, with a further US$ 750 million expected over the coming years. Mexico is one of the largest investors in the Dominican Republic, with CEMEX opening a 1.5 MW solar energy complex to power its San Pedro cement plant and investing a further US$ 20 million in various other elements of the plant. Another development in the electricity sector is that AES of the United States is planning to expand its power generation capabilities from 210 MW to 324 MW at a cost of around US$ 260 million.

In tourism, several hotels were opened or reopened by operators that included the United States-based Gansevoort Hotel Group, which opened a high-end property on the north coast for an investment estimated by fDi Markets at

more than US$ 200 million. A US$ 85 million investment in the Amber Cove port by British-American cruise company Carnival was also completed in 2014. Furthermore, Spain's Tradebe Port Services announced an expansion of its terminal for fuel oil and distillate products, estimated to require US$ 200 million of investment.[3]

Finally, Australian gold miner PanTerra warned that the performance of its Las Lagunas mine had been unsatisfactory, but stated that it was planning to undertake exploration in other areas as well. The performance of PanTerra contrasts with that of the Pueblo Viejo mine mentioned earlier, which is operating as expected.

Haiti is one of the countries that receive the least FDI in the Caribbean, both in absolute terms and in relation to the size of the economy. FDI inflows in 2014 dropped to US$ 99 million after four years in which they had averaged US$ 150 million.

There are many important sectors of the economy in which FDI is almost absent, for various reasons. The extractive industries have never been developed, although Newmont Ventures of Canada and other foreign companies are currently doing exploration work. There is also no heavy industry in the country, although the size of the economy (and its growth potential) would support a cement manufacturing plant. The financial sector is dominated by local banks, and electricity production and distribution are handled by a State-owned company. There is also very limited investment in agriculture by formal enterprises, whether local or foreign.

The sector that has received the largest amount of FDI in the past few years is telecommunications. Two foreign companies, Digicel of Jamaica and Netcom of Viet Nam, have invested substantial amounts in expanding their networks and now offer both fixed-line and mobile telephony and Internet services. Another large foreign investor is Heineken of the Netherlands, which bought local brewer Brana in 2011 and has invested in upgrading its facilities to meet the growing demand for beer and soft drinks.

FDI inflows into export processing manufacturing have averaged only US$ 6 million a year over the past decade, but are very important in terms of job creation. The sector is focused on garment production for the United States market, and most investors are from Asia. Tourism is another sector with great potential, but so far investments have been limited. The largest project registered has been the construction of a Marriott hotel in the capital, estimated at US$ 50 million. There are several projects to build large resorts in the country, including one recently announced by Carnival Cruise Lines for the construction of a port on Latortue island at a cost of US$ 70 million.

2. The southern Caribbean

FDI inflows into **Trinidad and Tobago** totalled US$ 1.394 billion in 2014, 30% less than the previous year. This continues a downward trend from 2013, when FDI inflows shrank by 19% compared with 2012. The hydrocarbons sector has traditionally attracted the bulk of FDI in the country (over 80% since 2011). The fall in oil prices since mid-2014 has created an uncertain environment in this sector, but major projects have continued despite these concerns. The United Kingdom's BP began construction of its Juniper offshore gas project in the fourth quarter of 2014, and this is expected to be completed in 2017. Total capital expenditure for the project may be as high as US$ 2.1 billion. Australia's Range Resources announced a significant investment in oil extraction at the Beach Marcelle site in 2013. The estimated US$ 100 million to US$ 150 million investment was supposed to start in 2014, but was postponed. In the same sector, France's Total divested a US$ 473 million share of its oil-producing fields to the National Gas Company (NGC) of Trinidad and Tobago in 2013, and this represented a significant negative inflow during that year.

Outside the extractive sector, Japan's Mitsubishi announced the construction of a new methanol plant in 2013 for a total cost of US$ 850 million. The original 2014 date for construction has since been postponed to 2015 at the earliest, and it is unclear whether the project will take place. A US$ 63 million clay block factory, a collaboration between local firm ANSA McAL and Italian company SACMI, was opened in 2014. Furthermore, the Government of Trinidad and Tobago signed an agreement with China in 2014 for the construction of a port in south-west Trinidad and for the development of seven industrial parks throughout the country. The industrial parks are meant to service both the manufacturing and the services sectors. The projects, which are expected to cost US$ 500 million for the port and US$ 250 million for the industrial parks, are subject to the approval of concessional funding from the Export-Import Bank of China. On the island of Tobago,

[3] See [online] http://www.fdimarkets.com/.

tourism is the most important sector, but there has been relatively little investment in recent years. Bermuda-owned Coco Reef spent US$ 9 million upgrading its properties during 2011-2012, but no other major foreign investments were recorded.

Trinidad and Tobago is responsible for approximately 90% of all outgoing FDI in the Caribbean. In 2013, for example, NGC acquired a 39% share in a Phoenix (United States) gas processor from ConocoPhillips for US$ 600 million.[4]

Suriname received only US$ 4 million in FDI in 2014 compared with US$ 138 million the year before. 2014 saw the long-awaited start of construction at the Merian gold mine by Newmont Mining Corporation of the United States, which is expected to invest approximately US$ 1 billion before operations can start in late 2016. National oil company Staatsolie also has a 25% stake in the Merian gold mine. Canada's IAMGOLD continues to operate the Rosebel gold mine, and in 2014 it also took an option on the nearby Sarafina mine. On top of that, IAMGOLD has also completed the largest solar energy project in Suriname to date, a 5 MW project costing between US$ 12 million and US$ 14 million. Alcoa, the United States-based aluminium producer, on the other hand, has reduced its operations in Suriname recently and is expected to divest its operations in 2015. Downstream, Kaloti Jewellery Group of the United Arab Emirates has set up a mint house and refining facility, which opened in 2014 at an estimated cost of US$ 20 million.

Outside the mining industry, very little FDI arrives in Suriname. There is investment in real estate, primarily from the Netherlands, which has a large Surinamese diaspora. Otherwise, the agricultural sector attracts the largest share of investment, such as the takeover of 90% of the national banana company by Belgium's Univeg for some US$ 30 million in 2014. Two former plantations, Brokopondo and Victoria, have gone through several rounds of unsuccessful privatization and development over recent decades, but there are signs that the Investment and Development Corporation Suriname (IDCS) will soon be able to identify a foreign investor that may be able to exploit the land successfully in a joint venture. In 2009-2010, Atlantic Tele-Network of the United States invested an estimated US$ 60 million in a fibre optic cable to Suriname. In other sectors, such as services or manufacturing, it is difficult to see any improvement in the immediate future unless the country addresses its challenges in governance, ease of doing business and international connectivity.

FDI to **Guyana** increased by 19% in 2014 to US$ 255 million, contributing to a lower balance-of-payments deficit. With 28% of inflows, the mining sector is the largest in Guyana, and in the bauxite, gold and diamond industries are particularly prominent players. Although FDI in gold mining is expected to fall owing to lower prices, FDI in bauxite is expected to increase, with continued investment by companies based in China and the Russian Federation. Bosai Minerals (China) has invested several hundred million dollars in recent years, but its relationship with the Government of Guyana has worsened recently, with US$ 100 million of planned investments not materializing.[5] In 2013, RUSAL committed to investing US$ 20 million in the Kurubuka-22 bauxite mine. Guyana Goldfields of Canada has invested heavily in the Aurora gold mine, which is expected to start production in 2015. Total expenditures are estimated at US$ 240 million. Outside of the mining sector, investors, particularly from China, have also made significant inroads into the distribution of consumer goods, for example with Haier Electronic Appliances' US$ 10 million plant, opened in 2012. As a result, the manufacturing industry received 12% of inflows in 2014. The tourism industry, which is relatively small in Guyana, received 11% of inflows in 2014. The sector should benefit from the opening of a US$ 51 million Marriott hotel, under construction since 2011 and due to open in 2015. One of the largest planned projects of recent years has been the Amaila Hydro Power Project, estimated at US$ 850 million, but with the withdrawal of Sithe Global of the United States in 2013, its future is unclear. The government is still committed to its eventual completion nonetheless.

3. The western Caribbean

Inward FDI in the **Bahamas** was somewhat lower than the previous year, with a 9% decrease to US$ 374 million. However, this was well below the annual inflows of earlier years, with a range of between US$ 750 million and US$ 1.05 billion from 2006 to 2011. The country showcases some of the most ambitious tourism plans anywhere in the Caribbean, but also faces many of the associated challenges. With 4,000 rooms, the Atlantis Resort is one of the largest resorts in the Caribbean. Kerzner International of South Africa had to sell the property to Canada's Brookfield Asset Management in 2012 after

[4] See [online] http://www.businesswire.com/news/home/20130816005664/en/ConocoPhillips-Announces-Sale-Trinidad-Tobago-Asset#.VNzCLObF8t1.

[5] See [online] http://www.guyanatimesgy.com/2014/04/07/govt-rescinds-bosais-block-37-concession/.

failing to run it profitably. Brookfield has promised to continue investing US$ 50 million per year there, but this shows the difficulty of guaranteeing profitability for such a large venture. Baha Mar, another mega project, is scheduled to open in the spring of 2015 after a US$ 3.5 billion investment, the largest share of which has been financed by the Export-Import Bank of China. The project will add another 2,200 rooms to the inventory and will further saturate the market in the Bahamas; it is not immediately clear whether this can sustain two mega hotel projects right next to each other.[6]

The Bahamas has had several run-ins with promising investments that turned out to be failures. United States-based Glasslam opened a new location for small-scale high-tech manufacturing in 2009, but it was closed soon afterwards, something the CEO of Glasslam attributed to the difficulty of doing business and bad relations with Grand Bahama Power Company.[7] Another purported manufacturing investment, by the now defunct Pegasus Wireless Corporation of the United States, finally turned out to be a scheme to defraud investors.[8] On the other hand, the Bahamas is one of the few countries in the region with substantial outgoing investments as well. Cable Bahamas, for example, acquired four separate cable operators in Florida for close to US$ 100 million in 2013. A final investment worth noting is the expansion of Cable & Wireless, which owns 51% of Bahamas Telecommunications Company and upgraded its network at a cost of some US$ 100 million in 2012 and 2013. It originally acquired a majority share in 2011 for US$ 210 million. The 2010 transfer for US$ 1.36 billion of a Bahamian oil refinery from First Reserve to Buckeye Partners, both based in the United States, did not represent a new inflow of capital, but can be considered a vote of confidence in the country.

Jamaica received FDI inflows worth US$ 699 million, 7% more than in 2013 and the largest amount since 2008. The sector classified as "other"received the most FDI in 2014, but tourism saw the largest increase, jumping from US$ 6 million in 2013 to US$ 104 million in 2014. The rise in FDI could be considered a positive signal from investors in response to the government's commitment to financial reform and its signing of an Extended Fund Facility with the International Monetary Fund (IMF). A major point of discussion in the country is the development of the Goat Island Port by China Harbour Engineering Company (CHEC). The project, estimated to require an investment of US$ 1.35 billion, is opposed by environmentalists but supported by both the government and much of the population. A decision is expected in 2015 (see also box I.4 in chapter I). CHEC is also the main force behind Highway 2000, a US$ 600 million project for a north-south highway which has been ongoing for about 10 years and is now projected to be completed by 2016.

Investments in mining, most relating to bauxite, have been declining over the past few years, dropping from a high of US$ 336 million (38% of FDI inflows) in 2006 to a mere US$ 26 million (4% of inflows) in 2014**.** In the latter year, the Russian Federation's RUSAL committed to building a coal-fired power plant in exchange for a two-year bauxite levy concession. At the same time, China's Xinfa Group has been in extensive discussions with the Government of Jamaica to invest up to US$ 3 billion in the redevelopment of Reynolds mines, together with an alumina plant and another coal-fired power plant. The negotiations between Xinfa Group and the government have not yet been concluded. One of the largest inflows of FDI in recent years is associated with the decision by Italy's Campari Group to acquire the spirits business of Lascelles deMercado for US$ 415 million in 2012.

Tourism was the major recipient of FDI a decade ago, when a series of investments by Spanish companies increased capacity in the sector substantially. After the financial crisis, the industry suffered from overcapacity and new investments declined to as little as US$ 6 million in 2012, picking up again only very recently. The Moon Palace Golf & Spa Resort is reopening after an estimated US$ 100 million refurbishment by Mexico's Palace Resorts. Playa Hotels and Resorts invested an estimated US$ 150 million in refurbishments and construction at the former Ritz Carlton, which reopened in late 2014. The Royalton White Sands reopened in late 2013 after Canada's Blue Diamond Hotels & Resorts spent US$ 50 million upgrading and updating it. The United States-based Apple Leisure Group, which already operates two hotels on the island, is among companies rumoured to be considering new investments. In addition to foreign investors, Sandals Resorts is investing in its home market by upgrading and modernizing existing properties.

The inflow of FDI into **Belize** increased significantly in 2014, rising by 48% to US$ 141 million, with real estate being the most important sector with 35% of inflows, followed by tourism with 21%. Since 2005, tourism has been responsible for 28% of inflows, followed by real estate with 19% and financial services with 10%. Since the country has a relatively small economy, individual investments can cause large swings in inflows, so that next year will

6 See [online] http://www.wsj.com/articles/chinas-bahamas-project-hits-hurdles-1412092767.
7 See [online] http://www.dwmmag.com/index.php/glasslam-to-open-three-new-locations-close-one-in-2010/.
8 See [online] http://www.bahamasb2b.com/news/2011/08/another-of-christies-big-investors-turns-out-to-be-a-crook-10826.html.

probably see a reversion to the mean. The two sectors of primary importance to Belize are tourism and agribusiness. In the latter category, the country is one of the few in Latin America and the Caribbean to receive FDI inflows that are significant relative to the size of the economy. One example of an international investor is United States-based TexBel Agricultural Investments, which is in the process of putting an estimated US$ 45 million into the development of coconut farming. In another example, American Sugar Refining of the United States acquired a majority share in Belize Sugar Industries for US$ 100 million in 2012. In retail, Jamaica's GraceKennedy acquired the remaining third of its Belizean subsidiary for an undisclosed amount in 2012.

In tourism, Norwegian Cruise Line's US$ 50 million investment in an environmentally friendly port will soon be forthcoming, while several other far-reaching plans for cruise terminals or resorts have occasionally been floated in the media, but without a clear path towards realization. In 2014, Caye Chapel, an island which had been part of a bankrupt estate and ended up in the possession of Belize Bank, was finally sold for US$ 11.5 million to an unnamed Mexican hotel group and is expected to be developed into a new luxury resort. On Ambergris Caye, a range of developments are at different stages of realization, but local critics say that several of them do not adhere to local and national regulations. Environmentalists also worry about the speed at which Belize's sensitive coastal range is being developed. In 2011, large property on Long Caye Island was sold to Amble Resorts, which was planning to develop it into an eco-resort, but progress has been slow and it is unclear whether any investment has taken place.

Box II.1
Foreign direct investment in Cuba

Cuba is the largest country in the Caribbean in terms of population, and the only economy in the region that does not report FDI data. Despite the absence of exact FDI figures, it is possible to examine some of the major policy issues relating to FDI.

The most important development was the introduction of the Foreign Investment Act in 2014, which updated legislation dating from 1995. The aim of this legislation is to diversify the production structure, access advanced technology, substitute imports (especially of food) and promote integration into international value chains. Another of the government's objectives is to change the energy matrix through investments in renewable energy —a strategy that has been pursued in several economies in the Caribbean and Central America. The law allows FDI in all sectors except education, health and defence. More importantly, it establishes legal safeguards for investors, allows foreign investors to hold a majority share in an investment and introduces tax incentives such as an eight-year income tax waiver for investments in joint ventures with local institutions.

Compared with other investment regimes in the region, the law maintains several major restrictions. First, all investments and divestments must be approved individually by the government. Second, although most sectors are open to investment, the government produces a portfolio of priority projects, including, for example, joint ventures with local institutions (which receive special tax treatment). Finally, all workers must be hired through State-owned employment agencies. It is still too early to assess whether the introduction of this legislation has incentivized FDI inflows to Cuba.

Investment opportunities may also be created by the ongoing changes in the relationship between Cuba and the United States. United States President Obama's announcement of a détente between the two countries on 17 December 2014 is likely to encourage investment in Cuba by enterprises based in the United States. More importantly, it is also likely to lead to a large influx of foreign tourists to the island and to the investment in accommodation infrastructure this will require. Toro (2015) shows that some 1.1 million Canadian tourists visit Cuba each year (out of a total of 2.9 million tourists), while most Americans have so far been debarred from visiting. The number of tourists from the United States is likely to be even greater owing to its larger population and proximity to the island. Cuba was a major destination for United States tourists in the 1950s, before the Cuban Revolution.

At present, the largest foreign investments are State-sponsored, such as the port facilities at Mariel, costing nearly US$ 1 billion, funded through the Brazilian Development Bank (BNDES) and constructed by Odebrecht (BBC, 2014).

Many of the other significant projects that have been undertaken in recent years are tourism-related. Two Spanish hotel groups, Melia Hotels International and Hotusa, announced investments in new hotels in 2013, according to fDi Markets. It is not clear whether those investments have actually taken place, however. In general, information on investment in Cuba is not readily available, although it appears that activity is now on the increase. A good example of the growing importance of the Cuban market is the opening of a sales office (for an estimated capital investment of US$ 19 million) by Spanish winery Bodegas Fernando Castro.

Spain is the leading investor in Cuba at present, followed by several other European countries, Canada and the BRIC countries (Brazil, the Russian Federation, India and China). The newly opened Mariel port is likely to increase the involvement of Brazil in particular, while the fall in global oil prices will reduce the involvement of the Bolivarian Republic of Venezuela in the Cuban economy. The United States could soon become a large source of foreign investment, not least from the Cuban diaspora. Large hoteliers such as Marriott and Apple Leisure Group have expressed interest in the development of new properties in Cuba once the investment embargo is lifted.

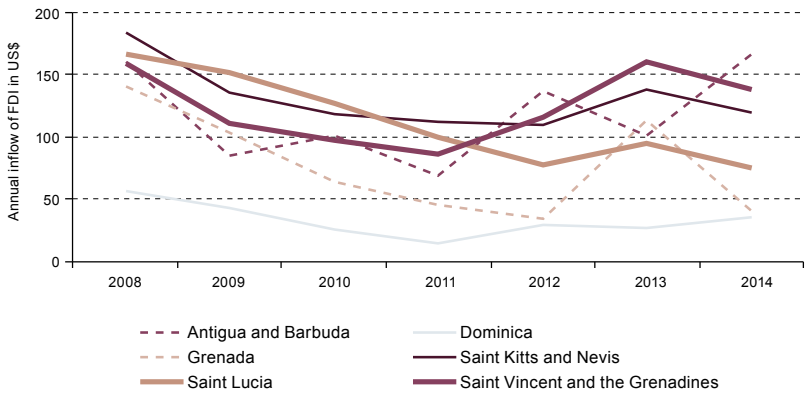
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of BBC, "Brazil-funded port inaugurated in Cuba", 27 January 2014 [online] http://www.bbc.com/news/world-latin-america-25920580; and F. Toro, "Cuba is hoping to replace Venezuelan oil with American tourists", *FiveThirtyEight*, 16 January 2015 [online] http://fivethirtyeight.com/features/cuba-is-hoping-to-replace-venezuelan-oil-with-american-tourists/.

4. The Organisation of Eastern Caribbean States and Barbados

The Organisation of Eastern Caribbean States (OECS) as a whole experienced a small decline in FDI between 2013 and 2014, although the total inflow was still the second-highest since 2010. Most OECS member States saw small drops, with Grenada being a negative exception and Antigua and Barbuda a positive one (see figure II.2).

This set of economies is strongly dependent on tourism, with very little inward FDI in other sectors. OECS members commonly rank as the economies with the highest FDI to GDP ratios in the world (see figure II.1). Citizenship by investment (CbI) programmes are an important instrument in several OECS member States. This is a type of programme whereby investors can obtain citizenship in exchange for a significant investment in the country (in most cases around US$ 400,000, sometimes less). This method is appreciated by many investors, who use it to attract individual participants in large tourism projects. CbI programmes are not unique to the Caribbean, but their use is more developed there than in other locations.

Figure II.2
Organisation of Eastern Caribbean States: total foreign direct investment (FDI), 2008-2014
(Millions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

In 2014, **Antigua and Barbuda** saw a 66% increase in inward FDI, bringing inflows to the highest level since the beginning of the financial crisis. The most significant announcement of 2014 related to the sale of some 1,522 acres of land to China's Yida International Investment Group for US$ 60 million. The company reportedly plans to construct several luxury hotels, 1,300 residential units, the largest casino in the Caribbean and many more facilities. Estimates for outlays over 10 years vary between US$ 740 million and US$ 2 billion. The project is expected to have an enormous impact on the island, both economically and environmentally. Also in 2014, the United Kingdom's Cable & Wireless Communications announced a plan to spend US$ 14 million upgrading the local telecommunications network operated by its regional subsidiary LIME.

Much of the investment that took place in Antigua and Barbuda before 2014 was also in the tourism industry. The Jamaican giant Sandals Resorts International owns several properties, including the Grand Pineapple Beach resort, originally acquired in 2008. This resort is to receive a US$ 125 million makeover to become a Beaches Resort, this being another brand operated by Sandals. Since 2012, Pearns Point has been under development as part of a plan that should eventually cost around US$ 250 million. Pearns Point is backed by developers from the Netherlands and is being primarily funded through Antigua and Barbuda's CbI programme, which has helped with the effort to market it as a destination for overseas property buyers. In 2012, Bau Panel Systems of Gibraltar, United Kingdom, held a groundbreaking ceremony for a factory that was to supply materials for a social housing project, but no progress was made thereafter. In 2014, the new Antiguan Prime Minister decided to withdraw the government's support for the project.

Saint Vincent and the Grenadines experienced a 13% drop in FDI inflows to US$ 139 million. Continuing time and cost overruns at Argyle International Airport, under construction since 2008 and set to be completed in 2015 at a cost of US$ 240 million, according to the most recent estimates, have been a burden on the overall economy. However, once the airport is finally completed, it will improve the islands' attractiveness to foreign investors, particularly in the tourism

sector. Among the largest current investments, Ireland's International Investment & Underwriting (IIU) entered into a joint venture to operate and further develop the former Raffles Resort in 2010 at a cost of approximately US$ 120 million. This property became the ultra-luxurious Pink Sands Hotel and opened in 2014. The US$ 250 million Buccament Bay Resort opened in 2011 and was by far the largest resort at that time, with 368 rooms. Its developer, Harlequin Hotels and Resorts of the United Kingdom, has since filed for bankruptcy, adversely affecting the individual small-scale investors behind it but not affecting operations at the hotel. The government continues to hold out against the introduction of a CbI programme in the country on principle, despite the success of such programmes in other jurisdictions.

Looking to the longer term, Saint Vincent and the Grenadines has welcomed investment in alternative energy sources in order to reduce its dependence on the import of diesel. The fall in oil prices has lessened the need for such substitution, but the government is committed to continuing work on existing projects. Iceland's Reykjavik Geothermal and Canada's Emera are still aiming to develop geothermal energy sources in Saint Vincent and the Grenadines, with the aim of having a first plant operational by 2017-2018. Finally, Cyprus-based currency trader Exness moved its operations from New Zealand to Saint Vincent and the Grenadines in 2014, an investment estimated by fDi Markets at US$ 31 million.

Saint Kitts and Nevis receives some of the most stable FDI flows of any OECS member state. 2014 saw a small drop of 13% from US$ 139 million to US$ 120 million. The country makes successful use of its long-standing CbI programme compared with neighbouring States. A number of projects are currently under construction, nearly all of them funded at least partially through the CbI programme. The use of this programme means that it is not possible to identify the exact origins of the funds, but projects do tend to be driven by specific development groups. Kittitian Hill, on which construction started in 2010 and whose first stage opened in 2014, has cost approximately US$ 90 million in total and is backed by investors from Switzerland and Trinidad and Tobago. Koi Resort and Residences, the first phase of which is to be completed in 2016, is backed by a United States-based developer, as is Christophe Harbour, a large project that includes residences, a marina, facilities and several hotels. The total investment committed to this group of projects is more than US$ 1 billion, of which some US$ 350 million had been spent by the end of 2014. The first hotel in Christophe Harbour is the Park Hyatt St. Kitts, under construction by the United Arab Emirates' Range Developments and scheduled for completion by late 2015. The largest employer on Nevis is the Nevis Four Seasons (Canada), which was damaged by hurricane Omar in 2008. It reopened in late 2010 after a refurbishment costing some US$ 100 million.

Besides tourism, Saint Kitts and Nevis aims to attract investment in several other sectors, including international education, agriculture, financial services and renewable energy. In this last sector, a second solar plant was opened in January 2015, funded jointly with the Government of Taiwan Province of China. Speedtech Energy of Taiwan Province of China opened a US$ 1.5 million solar panel manufacturing plant in 2013. Finally, Saint Kitts and Nevis also plays an important role in international education, with four universities using the United States curriculum currently located in the country. The best-known of those is Ross School of Veterinary Medicine, which, together with its sister University of Medicine in Dominica, was acquired by DeVry University of the United States for US$ 310 million in 2003.

Saint Lucia has shown a consistent downward trend in FDI inflows since 2008, with an average annual drop of 12% and a larger fall of 21% to US$ 75 million between 2013 and 2014. Most investment has traditionally taken place in the tourism sector, and a CbI programme is under consideration. As in other economies, many transactions taking place in Saint Lucia are not treated as new FDI inflows. For example, the acquisition of Hess Oil Saint Lucia by Buckeye Partners of the United States in 2013 as part of a larger US$ 850 million package was a transfer of ownership between foreign parties: while it was a commitment to the island, it did not represent a new inflow of FDI.

The bulk of investment takes place in the tourism sector, in the form of new construction, acquisition and upgrading of existing infrastructure or gradual expansion of a property. Examples of the first include the Harbor Club Hotel and dive centre, currently under construction by a Swiss investor at a total cost of some US$ 45 million, and Hotel Chocolat, completed in 2013 at a similar cost. The second group includes the Rodney Bay Marina, purchased in 2006 by Island Capital Group of the United States and upgraded for an estimated US$ 40 million, and the Capella Marigot Bay Resort and Marina, which reopened in 2014 after a multi-million dollar refurbishment by its new United States-based owners. An example of the final group is Windjammer Landing, owned by Canada's EllisDon since 1989. This resort is currently investing close to US$ 50 million in expanding and upgrading its facilities in order to be able to continue competing with other offerings in the region.

The large inflow of FDI into **Grenada** in 2013 appears to have been an anomaly, with inflows in 2014 dropping back by 64% to US$ 40 million, historically a more normal figure and the lowest of any OECS member State. Like other

OECS members, Grenada is primarily dependent on investment in tourism. This means that individual projects, whether new developments or refurbishments, can have a significant impact on FDI inflows. In late 2013, for example, Sandals LaSource Grenada Resort was reopened after a US$ 100 million refurbishment, which probably contributed to the surge of FDI recorded in 2013. Grenada also provides a good example of the market power of large players such as Jamaica's Sandals. In return for its investment, Sandals received a 29-year corporation tax waiver and 25-year waivers on property taxes, customs duties on capital inputs and alcohol duty. These concessions seem particularly generous given that Grenada is in partial default, having most recently defaulted on its debts in 2005.

Like other islands, Grenada is using its CbI initiative to attract investment, but it is not clear whether the grand ambitions of certain investors are realistic. For example, British-Grenadian property developer Peter de Savary has been working for several years on a property development called Port Louis, which is expected to cost between US$ 500 million and US$ 700 million. The marina has now been successfully developed, but it is not clear yet whether the rest of the grand plan to put Grenada "on the global luxury map" is ever going to be completed.[9]

Consistently at the bottom of the ranking of OECS member States when it comes to FDI inflows, **Dominica** actually saw a 36% increase in FDI during 2014 to US$ 36 million. With GDP declining in four years out of six recently (ECLAC, 2014c), the island is looking to FDI to move the economy forward. News reports from December 2013 implied that China's ASCG and the Government of China were looking to invest some US$ 300 million in Dominica, including a US$ 70 million international hotel, hospital facilities and an international airport, but it is uncertain whether any of these investments will actually take place. Even if they do, it is not immediately clear that the construction of an international airport is a worthwhile investment for the Dominican economy.

The Government of Dominica has been at the forefront of efforts to attract investment in geothermal energy generation. Several companies have been close to committing to a definitive investment in recent years, but nothing has so far come of this. A major challenge for the island is that its market is probably too small to make geothermal energy a worthwhile option unless it links its electricity grid to those of other islands, which would significantly increase the projected costs.

Jamaica's Digicel acquired Dominican cable television and Internet provider SAT Telecom for an undisclosed sum during 2014 after buying the mobile network of France's Orange in 2009. Finally, an agreement was signed with the United Arab Emirates' Range Developments on the construction of a 125-room luxury hotel, with the country's CbI programme being used to fund the investment. So far, the island's relatively liberal CbI programme has not led to a significant inflow of FDI.

Between 2013 and 2014, **Barbados** saw FDI inflows increase from US$ 5 million to US$ 275 million. The Central Bank of Barbados provides fairly disaggregated data which show that in the long run more than 60% of FDI is invested in real estate. This is higher than elsewhere in the region, and is associated with the country's attractions as a second residence. Where other tourist accommodation is concerned, the island is at the mercy of international tourism flows. One of the largest resorts on the island, Almond Beach Village, ended up in the hands of Massy of Trinidad and Tobago when it purchased Barbados Shipping & Trading between 2008 and 2012. The property was close to bankruptcy and was finally taken over by a government agency in 2013 for US$ 53 million. It was eventually resold for the same price to Sandals, which performed a US$ 65 million upgrade in 2014 in order to reopen in January 2015. This is illustrative of the complicated relationship between hotel operators and the Government of Barbados.

Since Barbados is a financial centre, it can be difficult to differentiate transactions by enterprises that are truly based there from those that are only nominally Barbadian. There was a good example of this in 2014 with the purchase of Columbus International, an international telecommunications operator based in Barbados, by Cable & Wireless Communications of the United Kingdom for more than US$ 3 billion. At the same time, the slippage in Barbados' sovereign debt rating may put its role as a financial centre at risk. Barbadian behemoth Sagicor announced in early 2015 that it planned to move its headquarters because of the downgrading of Barbados sovereign debt by Standard & Poor's. In 2010, on the other hand, Canada's RBC Wealth Management announced the construction of a new wealth management office at an estimated cost of US$ 31 million.

Many firms have made plans for Barbados, although with varying degrees of certainty. For example, Guernsey-based Cahill Energy has announced the construction of a US$ 240 million waste-to-energy plant that aims to meet about 25% of Barbados' electricity demand. Furthermore, a range of hotels are scheduled to break ground in 2015, but while the investments involved total several hundred million dollars, it is not clear how certain they are to materialize.

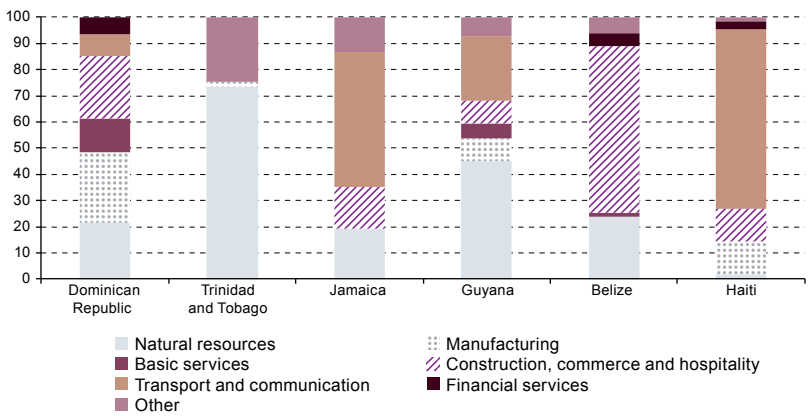
[9] See *Forbes* [online] http://www.forbes.com/sites/marcbabej/2013/02/01/the-700-million-vision-to-put-grenada-on-the-global-luxury-map/.

C. Sectoral analyses

The Caribbean consists of several groups of economies, each with its own economic story reflecting its strengths and weaknesses. There are some sectoral trends that are common to the whole subregion, and this section deals with those segments that attract the most FDI to it. For many economies, the tourism sector is the largest earner of foreign exchange and the primary destination for investment. The second most important sector is natural resources. In some economies, particularly Belize, Guyana, Suriname and Trinidad and Tobago, natural resources (in the form of agriculture, mining or oil and gas exploration) are the most important attractors of FDI, while in others (the Dominican Republic and Jamaica) the natural resources sector plays an important but less dominant role. The third category is export-oriented FDI.[10] This is not a single sector, but includes both export-oriented manufacturing and various export-oriented services, such as offshore education and business process outsourcing (BPO). The final category discussed in this section is market-seeking FDI.[11] This also encompasses various sectors, mostly in services (banking, retail, energy) but also in small-scale manufacturing.

A sectoral breakdown of FDI inflows is possible in only a few economies. Figure II.3 shows the average sectoral breakdown over a five-year period for those countries for which disaggregated data are available. As expected, natural resources are particularly important in Guyana and Trinidad and Tobago, but play a smaller role in the other economies. Only in the Dominican Republic does manufacturing account for a large proportion of FDI, while transport and communications are particularly important in Haiti and Jamaica. In recent years, these countries have received large investments in the telecommunications sector, corresponding to both network expansion and the setting-up of new networks.

Figure II.3
The Caribbean (selected countries): average breakdown of FDI inflows by sector for the most recent five-year period [a]



Source: Economic Commission for Latin America and the Caribbean (ECLAC) on basis of official sources.
[a] The data for Jamaica are for 2008-2012; Belize, 2009-2013; Trinidad and Tobago, 2007-2011; Guyana, 2009-2013; and the Dominican Republic and Haiti, 2010-2014.

A final observation is that the construction, commerce and hospitality sector accounts for a large proportion of FDI inflows to Belize, and for a slightly lesser but still significant proportion to the Dominican Republic and Jamaica. As this sector is a a major driving factor behind tourism, it could be expected to play a key role in Barbados and the member States of OECS, however, this cannot be confirmed as data for those economies are limited. The Bahamas, which is a larger economy than many of the OECS member States, is a major recipient of tourism-related investment flows, as supported by the figures concerning the contribution of tourism to Bahamian GDP.

[10] Both natural resources and tourism are considered export-oriented sectors as well, but are dealt with separately because of their particular importance.
[11] A standard framework for the analysis of foreign investment incentives includes resource-seeking, efficiency-seeking and market-seeking FDI. This chapter, however, uses the perspective of FDI-receiving economies, where market-seeking and export-oriented FDI is a more logical dichotomy. As an example, investments in the natural resources sector are resource-seeking from a corporation's perspective, but would be considered export-oriented FDI from the perspective of the host country.

1. Tourism FDI [12]

The Caribbean is famous for its tourism, but the tourism industry in the subregion has struggled in the past few years. According to the World Tourism Organization (UNWTO, 2014), the number of arrivals in the Caribbean has increased only modestly in recent years. Table II.3 shows a disaggregation of tourist arrivals and tourism receipts per Caribbean economy. Not shown, however, is the growth of tourism in the rest of the world. Between 2010 and 2013, the number of arrivals worldwide increased by 16.3% and tourism receipts by 26.5%. In the Caribbean,[13] on the other hand, these growth rates were only 8.6% and 9.0%, respectively. As a result, the Caribbean's global market share of arrivals fell from 2.2% to 2.1% and its share of receipts from 2.6% to 2.2%. From 2008 to 2013, more than half the economies included in our analysis saw reductions in visitor numbers.

The differences between economies are very large, however. To illustrate this, figure II.4 shows the tourism share of total foreign-exchange receipts and the ratio of tourism earnings to GDP. The countries shown can be divided into three groups. The first includes Barbados, the Bahamas and all OECS member States except Saint Kitts and Nevis: in these countries, tourism is responsible for more than 30% of foreign-exchange earnings, and in many of them tourism receipts equal more than 20% of GDP. These are economies for which tourism is a pivotal sector. The second group of economies includes Belize, Jamaica and Saint Kitts and Nevis, where tourism receipts make up between 20% and 30% of total foreign-exchange earnings and a substantial share of GDP. These are economies in which tourism plays a significant role, but less so than in the first group. The third group consists of Haiti, Guyana, Suriname and Trinidad and Tobago, where tourism receipts make up only a very small portion of total earnings. These are economies in which tourism currently plays a much smaller role. Three of the four countries generate significant revenue from natural resources. The Dominican Republic is an unusual case and not included in any of these three country groups. Tourism expenditures there represent 8% of GDP but nearly 25% of foreign-exchange earnings, partly because its economy is much larger and more diversified than others in the subregion. At the same time, the industry supports some 200,000 jobs in the country (UNWTO, 2014) and plays an important role in its image.

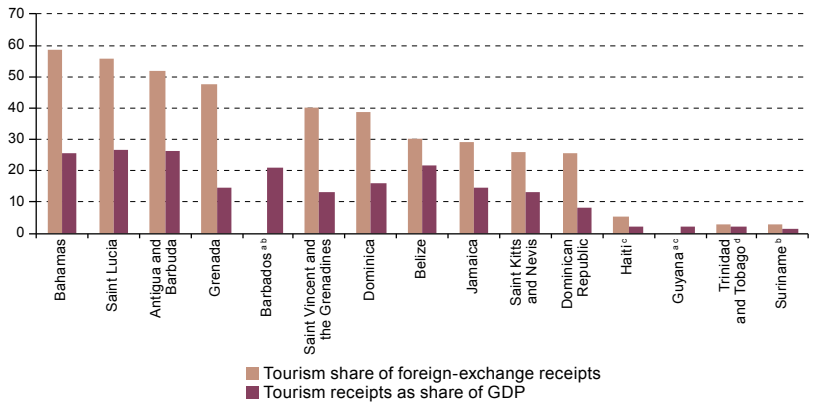
Table II.3
The Caribbean (selected countries): international tourist arrivals and international tourism receipts, 2010-2013

Country	International tourist arrivals (thousands)				Average annual change (percentages)	International tourism receipts (millions of dollars)				Average annual change (percentages)
	2010	2011	2012	2013		2010	2011	2012	2013	
Antigua and Barbuda	230	241	247	244	2.0	298	312	319	299	0.2
Bahamas	1 370	1 346	1 422	1 363	-0.1	2 163	2 142	2 311	2 162	0.2
Barbados	532	568	536	509	-1.3	1 034	963	907	912	-4.0
Belize	242	250	277	294	6.7	249	247	298	351	12.5
Dominica	77	76	78	78	0.4	94	106	76	82	-2.5
Dominican Republic	4 125	4 306	4 563	4 690	4.4	4 209	4 436	4 736	5 118	6.7
Grenada	110	118	112	116	1.9	112	117	122	120	2.4
Guyana	152	157	177	...	8.0	80	95	64	...	-6.9
Haiti	255	349	349	420	19.1	169	162	170	...	0.4
Jamaica	1 922	1 952	1 986	2 008	1.5	2 001	2 000	2 070	2 074	1.2
Saint Kitts and Nevis	98	102	104	107	3.0	90	94	95	101	3.9
Saint Lucia	306	312	307	319	1.4	309	321	337	354	4.6
Saint Vincent and the Grenadines	72	74	74	72	0.0	86	92	94	92	2.3
Suriname	204	220	240	249	6.9	61	61	71	84	11.6
Trinidad and Tobago	388	402	...	...	3.6	450	472	...	...	4.9
Total	10 083	10 473	10 472	10 469	1.3	11 405	9 620	11 670	11 749	2.1

Source: World Tourism Organization, *UNWTO World Tourism Highlights: 2014 Edition*, Madrid, 2014; and official figures.

12 Tourism was also one of the topics of chapter III of ECLAC (2009).
13 This refers to the World Tourism Organization definition of the Caribbean, which includes all of the islands located in and around the Caribbean Sea.

Figure II.4
The Caribbean (selected countries): inbound tourism expenditure as share of total foreign-exchange receipts and total GDP, 2013
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of World Tourism Organization, *UNWTO World Tourism Highlights: 2014 Edition*, Madrid, 2014; and official figures.
[a] Data unavailable for the tourism share of foreign-exchange receipt.
[b] 2010 figures.
[c] 2012 figures.
[d] 2011 figures.

Forecasts for global tourism (UNWTO, 2011) show that the Caribbean is expected to continue losing market share in the future. The main reasons for this are saturation of the Caribbean market and the entry of more and more areas of the world into the tourism market. The global growth rate of tourism between 2010 and 2030 is forecast at about 3.3% per year (down from 3.9% between 1995 and 2010), but the growth rate of tourism in the Caribbean is expected to decrease from 2.4% to 2.0% over the same period. Only western Europe, northern Europe and North America are expected to do worse between 2010 and 2030. So far, primarily thanks to the Dominican Republic's strong performance, the region has been able to slightly exceed expectations. In any case, relatively gloomy forecasts have not stopped FDI in the tourism sector from increasing significantly in recent years. For the foreseeable future, the Caribbean can expect to see a significant increase in tourism-related investment, with the potential exception of the Dominican Republic (UNWTO, 2011).

There are many different types of tourism in the Caribbean, reflected in the various kinds of accommodation. In terms of total amounts spent, mega projects make up a large share of investment in the sector. The largest project in the region, Baha Mar in the Bahamas, scheduled to open in the first half of 2015, includes five different hotels and involved a total investment of approximately US$ 3.5 billion, largely financed by the Export-Import Bank of China. In Jamaica, there may not be such large individual projects, but a major inflow of investment into the accommodation sector a decade ago has created a very large supply in resorts and resort-style hotels. Many hotels in Jamaica are operated under management contracts by large international players. This modus operandi is less common on other islands, although the Bahamas' enormous Atlantis Resorts is another example. The Dominican Republic is obviously the giant of Caribbean tourism when it comes to the number of tourists attracted. Canada's Blue Diamond Resorts opened a new 323-room luxury hotel in December 2014, while there are several very large combinations of resorts. The Gran Bahía in Punta Cana, for example, has several thousand rooms spread over different hotels. The regional giant is Jamaica's Sandals Resorts International, which has branches on several islands. Recently opened resorts include those in Barbados (reopening in 2015 after a US$ 65 million upgrade), Grenada (2013), the Bahamas (2010) and Antigua and Barbuda (2008).

Luxury and ultra-luxury accommodation is an interesting sector in which there is a great deal of investor interest. Many of the new operations in the luxury or ultra-luxury market are operated by individuals or small outfits. That applies to new firms such as Koi Resorts (whose primary backer is based in the United States) in Saint Kitts and Nevis, where an estimated US$ 200 million will be spent, Saint Lucia's Windjammer Landing (a subsidiary of Canada's EllisDon) and the Crane Resort in Barbados (reopened in January 2015 after a US$ 45 million upgrade and owned by a Canadian investor), as well as to the long-established Jade Mountains Resort in Saint Lucia, whose original backers were from Canada. Accordingly, many governments in the Caribbean focus on developing unique properties to attract high-spending tourists. Some of these hotels charge up to US$ 2,000 per room per night.

Ecotourism has led to relatively recent additions to the Caribbean accommodation stock. The concept of ecotourism is not particularly well defined and can encompass anything from eco-conscious microenterprises to large international corporations developing large resorts. This type of accommodation has many advantages for investors and host countries alike. First, higher prices can be charged for ecotourism, which benefits investors. Second, the negative impacts (see also chapter III) of tourism are reduced because of the increased environmental awareness. Third, ecotourism also encourages increased engagement with the local economy (through suppliers and job creation), which can increase the local economic benefits of tourism inflows.[14]

The third type of tourism where FDI can play an important role is in the conferencing sector. In Saint Lucia, for example, the Harbor Club Hotel is currently under construction by a Swiss investor spending at least US$ 40 million with the aim of creating the best business hotel in the Caribbean (and the only one in Saint Lucia). This is also a field in which multinational corporations play an important role. Among the top conferencing destinations are Hilton hotels in Port of Spain and Montego Bay (Jamaica) and the Sheraton Hotel in San Juan (Puerto Rico). The advantages of this type of tourism are that it includes high-spending customers, which increases its impact, and that it may help to introduce destinations to potential future visitors. The disadvantage is that spillover into the local economy is more limited, particularly where international chain hotels are concerned.

The fourth type of tourism is primarily FDI-driven: residential investment, whereby individuals from outside the region purchase property there.[15] On some islands, this makes up a large share of FDI inflows. Unfortunately, disaggregated data are not always available. In Barbados, 71% of FDI inflows between 2001 and 2010 were from real estate sales.[16] The only other economies reporting figures look at land sales only, with figures ranging from as little as 5% in Dominica to as much as 63% in Saint Kitts and Nevis (2007-2011 average), giving an average of about a third of all flows in reporting economies. Real estate investment is different in some ways from other tourism investment: beyond the construction phase, it may not have the same kind of spillovers in terms of job creation, for example. However, in Barbados, for example, an active effort is under way to make sure that owners contribute their vacation homes to the accommodation market when they are not occupying them. This real estate can thus still attract tourists who will make use of auxiliary services on the island. Finally, in certain projects, such as Christophe Harbour (Saint Kitts and Nevis), holiday homes are part of a larger effort to make the overall project, which also includes luxury hotels, secondary services and a marina, financially viable.

In addition to the aforementioned types of investment in accommodation, two other forms of tourism FDI are important in the region, namely FDI relating to non-stay tourism and auxiliary services. Non-stay tourism primarily involves people arriving on cruise ships and yachts. On many islands, non-stay arrivals far exceed the number of overnight visitors, but the impact on the local economy is much lower. The islands are attempting to capture more of these tourists' spending power through State investment in port and shopping facilities. In certain cases, though, this also involves private investment. In Belize, for example, Norwegian Cruise Line is scheduled to open a new eco-friendly cruise terminal in 2015 at a cost of US$ 50 million. In other economies, investment is mostly channelled into yachting facilities, as reflected by significant investments in, for example, the Rodney Bay Marina in Saint Lucia and marinas associated with hotels on various islands (such as Capella Marigot Bay and Marina in Saint Lucia and Christophe Harbour in Saint Kitts and Nevis).

FDI in auxiliary services is limited. Restaurants, tour services and other hospitality businesses tend to be locally run, for example. The airline industry is, of course, an exception, and a highly integrated and integral part of the tourism industry (see box II.2). Airlines also create their own secondary services. Goddard Enterprises of Barbados, for example, provides airline catering services at many airports throughout the region. While this is not capital-intensive FDI, it creates significant employment.

A lack of airline capacity in the region is frequently cited as a reason for high transport and shipping costs and an obstacle to further developing some industries, such as tourism, and is due to limited economies of scale in the region and high per-unit operating costs. Caribbean Airlines, the national airline of Trinidad and Tobago and by far the largest regional airline, was incorporated in 2006, replacing its predecessor, British West Indies Airlines. The airline has an alliance and code-sharing programme with British Airways. Given the worldwide trend in airline mergers,

[14] UNCTAD (2010) discusses the example of the Lao People's Democratic Republic, which has specific guidelines on the use of local products and the employment of local people. The discussion identifies guidelines that can be potentially useful for ecotourism in the Caribbean as well. See [online] http://unctad.org/en/Docs/diaepcb200916_en.pdf.

[15] For clarification, the term "residential investment" does not imply that the purchasers make the location where the investment is made their primary residence. More often than not, this is not the case.

[16] According to official estimates from the Central Bank of Barbados.

it is not surprising that various airlines in the Caribbean have also merged; this has often involved large amounts of merger and acquisition FDI. In the 2000s, State-owned Air Jamaica, another large regional carrier, experienced severe financial difficulties and the Government of Jamaica began looking abroad for solutions. After discussions with the Government of Trinidad and Tobago, in 2011 Caribbean Airlines acquired routes operated by Air Jamaica as well as the airline's fleet. It also took on Air Jamaica's debts and many of its assets, and rehired many of its employees. The Government of Jamaica retains 16% ownership of Air Jamaica. This acquisition makes Caribbean Airlines now the flag carrier of three Caribbean countries: Guyana, Jamaica and Trinidad and Tobago. Another important regional airline, especially for the countries of the eastern Caribbean, is Leeward Islands Air Transport (LIAT). This airline is jointly owned by 11 Caribbean nations and services 22 destinations with a fleet of 16 mostly small aircraft. In 2007, LIAT acquired Caribbean Star airlines, based in Antigua and Barbuda.

Box II.2

The relationship between airline capacity and accommodation

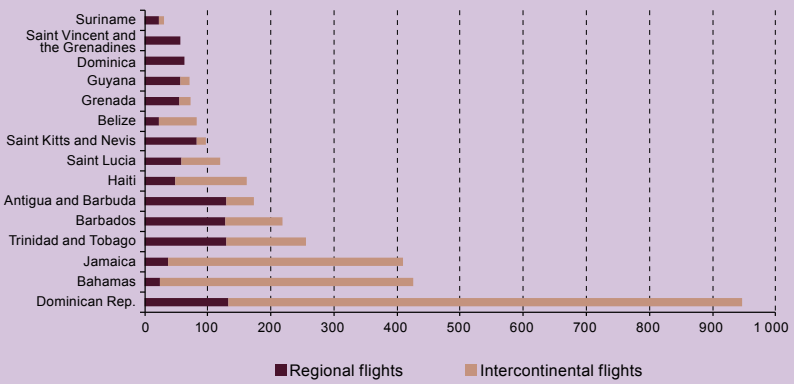
Market size is a primary concern for any business. The size of the tourism market in the Caribbean is directly dependent on the number of flights available to the different islands. Particularly for some smaller markets, an additional daily flight can have a significant impact on the demand for accommodation. At the same time, airlines only offer flights to destinations for which there is demand from travellers, which are those where there is sufficient accommodation to host tourists.

This phenomenon is familiar to the authorities, who make a great deal of effort to encourage both airlines and resorts to expand their businesses simultaneously. Individual investor decisions can thus have a large impact on a country's tourism capacity. For example, Sandals' recent expansion into Barbados is leading to an increase in air travel from Europe and North America because there is more accommodation available. Other resorts, such as the Coconut Bay Beach Resort and Spa on Saint Lucia, work closely with airlines (in this case British Airways) to sell package deals that include both flight and accommodation.

However, not all air travel has the same impact. A one-week sample of the number of flights from different destinations to the Caribbean shows, first, that certain places receive a disproportionate share of incoming flights. The Dominican Republic, the Bahamas and Jamaica receive 29.8%, 13.5% and 12.7% of all incoming flights, respectively.[a] Nonetheless, intercontinental flights have a particularly large impact because they bring tourists from far-away locations (primarily Europe and North America), but also because those flights tend to use larger aircraft. Saint Lucia, where more than half of all incoming flights are intercontinental, benefits more than Saint Kitts and Nevis, where a mere 18% of flights are intercontinental.

The Caribbean (selected countries): international air travel to different Caribbean destinations, one-week sample, 14 to 20 January 2015

(Numbers of incoming flights)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of FlightStats [online] http://www.flightstats.com/go/Home/home.do.
Note: Domestic flights are excluded. Regional flights include all flights from other Caribbean economies, while in the case of Belize they also include flights from other Central American countries.

An unusual aspect of the relationship between the airlines and Caribbean economies is that, although airlines such as Delta Air Lines, United Airlines, American Airlines and British Airways have a great impact on the latter, they do not usually make significant investments there themselves.

Haiti is an interesting case. It is the fourth most popular destination in the subregion for non-regional flights, mostly from the United States. This is primarily because Haiti has a large population and a large diaspora, but it suggests that there may be an opportunity to further develop tourism. Flight bottlenecks, often a problem in developing tourism, would not be an obstacle for Haiti.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).
[a] While the Dominican Republic has a large economy, the number of flights to some places such as the Bahamas and Barbados is particularly disproportionate to the size of their economies.

From a theoretical point of view, the nature of the impact of FDI on recipient economies is not clear (De Groot, 2014a). There are differences between tourism-related FDI in the Caribbean and overall FDI elsewhere. First, the region is very dependent on inflows of foreign capital because it has a relatively low investment capacity itself, something that is exacerbated by risk avoidance among local banks and a shortage of entrepreneurs to seek out new productive activities. Second, many Caribbean economies rely on the tourism industry for job creation, and without foreign investment it would not be so well developed.

A major transformative impact from foreign investment in tourism can be found in training and education. In many of the economies, access to education is limited and investors find it challenging to hire workers with the required skills. One exception is Barbados, which has a particularly good education structure. Workers in other countries, including the members of OECS, do not have a similar level of access to education. As a result, many of the larger investors in the Caribbean have extensive training programmes for their staff. For example, the Coconut Bay Beach Resort and Spa on Saint Lucia, realizing that young people are not able to afford higher education after finishing secondary school, hires many local students for internships or as part-timers, providing full training in the hard skills that will enable these workers either to become a valuable part of the resort's workforce or to go on to higher education after a few years. Other examples of training provided by employers include extensive safety training, food and beverage service training, and soft skills. While such training may not be equivalent to higher education, it has a substantial impact on the employability of workers. Local investors may be willing to offer similar types of training. However, foreign-owned businesses tend to be larger and have a stronger focus on consistently high service quality.

There may be limited spillovers for local establishments from large foreign-owned resorts. Since many such resorts and hotels are full-service, tourists often tend not to venture away from them; they may be encouraged to participate in excursions, but since these are often run by the hotel, they have a limited impact on the rest of the economy. Other businesses such as restaurants and local tour operators capture only a small fraction of tourists' spending. Of course, the resorts themselves require many inputs, including construction materials, furnishings, agricultural products and public services. However, in many cases local sourcing of such products (with the obvious exception of public services) is very limited. This is partly due to inconsistent product supply and quality and, in the case of technical equipment, partly a matter of preference, furnishings being a possible example, and partly due to the high costs of local production. It should be a matter of concern to governments, however, that investors import agricultural products even when the same product is produced locally. This happens in cases when local production cannot compete cost-effectively with imports or, more commonly, local goods of a consistently high quality are not available.

Governments should focus on improving the ability of domestic producers to supply the inputs required by large investors. While the situation differs between countries, the capacity of local producers is often considered to be very low. If local producers can develop the capacity to supply the tourist infrastructure sustainably, this can significantly increase local spillovers and the benefits an economy derives from tourism investment. In some cases, a regional approach to scaling up production of agricultural and other products might be able to make them cost-competitive. Another important consideration for governments is guaranteeing the quality of the workforce. Finding qualified employees can be hard in the Caribbean, even if job types are relatively standardized. This raises questions concerning the quality of the hospitality-oriented educational institutions that should provide the necessary basic qualifications. Currently, the subregion relies on investors to provide training even when there is an opportunity for governments to take responsibility in this field.

2. FDI in natural resources

The primary sector is much less important in the economies of most Caribbean countries than in those of South America, but there are some major exceptions. Belize, Guyana, Suriname and Trinidad and Tobago are very dependent on natural resources, while the Dominican Republic and Jamaica are more diversified but still host important operations in the extractive industries. Furthermore, limited local capabilities mean that most investments in the extractive industries (this is less the case in agriculture and forestry) are conducted by transnational corporations.

The largest investments in natural resources are in oil and gas extraction in Trinidad and Tobago. The country produces 81.3 thousand barrels per day (tbd), and the sector contributed 45% of GDP in 2014. There are two State-

owned companies in the sector, Petronin and NGC, but the majority of investments are carried out by foreign companies. These have been present in the country since the 1940s, and currently the largest are BP, BG and BHP Billiton, all of the United Kingdom, and Repsol of Spain. Foreign companies negotiate separate production-sharing agreements with the government for each concession. In recent years, 90% of total FDI in Trinidad and Tobago has been in the oil and gas industry.

Oil and gas is far less important in other countries of the Caribbean. Still, there is production in Barbados (1 tbd), Belize (1.8 tbd) and Suriname (15 tbd) that is significant for the size of these economies, especially in Suriname. There have also been substantial exploration efforts. Suriname's State-owned oil company signed contracts with Apache and Tullow Oil of the United States in 2012, while Repsol is carrying out exploration in Guyana.

Mining is currently very important for Guyana and Suriname. In Guyana, large-scale mining is concentrated in bauxite extraction, with Bosai Minerals of China and RUSAL of the Russian Federation both having large investments. Gold mining is usually carried out through small-scale operations, although the large Aurora mining project, owned by Canadian investors, is currently under construction, with an estimated initial capital investment of US$ 249 million. In Suriname, bauxite production has lost ground relative to both oil and gold. IAMGOLD of Canada is the largest player in the industry. The Economist Intelligence Unit forecasts total investment inflows of between US$ 1 billion and US$ 1.5 billion in gold mining, targeting both the expansion of existing operations and the opening of new mines.

Jamaica produces bauxite and limestone. RUSAL and CEMEX are the largest companies, but investments have decreased in recent years. In 2013, Nippon Light Metals began a US$ 3 million exploration for rare earths which, if successful, could lead to large FDI inflows.

The largest mining investment in the Caribbean has been the Pueblo Viejo gold mine in the Dominican Republic, owned by Barrick of Canada. The company has invested a total of US$ 4.3 billion over several years. During the construction phase of the mine in 2011 and 2012, FDI inflows in the sector reached over US$ 1 billion per year. The mine started to produce in January 2013, but while there are plans for expansion, the company has shelved them due to the fall in the gold price and is currently focusing on cost reduction. This single project has been significant for the country in terms of investment, exports and fiscal revenue. In fact, the government demanded a renegotiation of the fiscal agreement with the company, which was finally completed in 2012. This reduced some of the privileges previously granted to it and therefore raised the revenue the government will receive.

Agriculture is a sector that receives relatively little FDI in any country (see ECLAC, 2013, chapter III), and most countries in the Caribbean are not land-abundant. Belize and Guyana are exceptions, and both have attracted the attention of investors from neighbouring countries like Barbados, Guatemala and Trinidad and Tobago looking to produce rice, sugar and other products. Asian investors are interested in producing sugar and palm oil on large plantations, mostly in Guyana and Suriname. In 2007, Complant Sugar of China acquired assets in the Jamaican sugar industry for US$ 92 million. In 2012, State-owned Belize Sugar Industries was sold to American Sugar Refining in a deal that may involve up to US$ 100 million of investment. Another example from Belize is the investment by United States-backed TexBel Farms in the production of both oranges and coconuts with a view to exporting to the United States.

Lastly, there are many foreign companies, particularly from Brazil and Asia, in the Guyana logging industry, but very little information is available on their operations.

While agriculture and logging are carried out mostly by local investors, extractive industries have largely been developed by foreign companies. FDI in oil and gas has transformed the economy of Trinidad and Tobago, and mining investments have had a large impact on the Dominican Republic, Guyana and Suriname. It is partly because of these sectors that this group of economies has outperformed the rest of the Caribbean subregion over the past decade. With the reversal of the commodity cycle, FDI in natural resources is likely to fall over the coming years. Alcoa's announcement in March 2015 concerning the rapid divestment of its Surinamese assets supports this thesis.

3. Other export-oriented FDI

Export-oriented FDI is a form of FDI that seeks to exploit local production advantages in order to supply an external market. The most common advantages that host markets display include low costs, connectivity and trade relations. By and large, the Caribbean does not enjoy such benefits, so export-oriented FDI is relatively limited.

Tourism affects the balance of payments much as export-oriented businesses do, since it is a locally produced service sold primarily to foreign customers (namely tourists). Thus, tourism brings an inflow of capital during the investment stage, but also during the operational stage. This sets it apart from market-seeking FDI, as discussed below. Leaving aside tourism and mining, two forms of export-oriented FDI remain: manufacturing and services. Export-oriented manufacturing is important in few Caribbean economies, primarily the Dominican Republic and Haiti. Export-oriented services, on the other hand, play a more important role in a larger range of economies. This sector is able to make use of the relative cost advantage of labour in the Caribbean as compared with the United States and the fact that a large part of the Caribbean is English-speaking. Specific sectors include finance, business process outsourcing (BPO) and education.

(a) Manufacturing

Manufacturing exports from the Caribbean economies covered in this chapter are very modest, the primary exception being the Dominican Republic. Manufacturing exports from the Bahamas, Guyana, Suriname and Trinidad and Tobago are largely confined to some processed natural resources (oil, pearls, sugar), as discussed in the previous section, and only in Barbados are there a few modest exports of pharmaceuticals and optical equipment. Manufacturing exports from Jamaica have declined significantly over the past two decades.

The Dominican Republic, on the other hand, has a large export processing industry which was originally built around the production of apparel and has slowly diversified, mostly into the production of medical and pharmaceutical devices. Some 78% of accumulated investment in the country's export processing zones (EPZs) is foreign (CNZFE, 2014), coming mostly from the United States, and recorded FDI in the sector has averaged US$ 150 million in the past three years.

Investment, production and employment in this industry declined significantly from 2005 to 2010 as a consequence of Chinese competition in apparel manufacturing and the financial crisis in the United States. Employment dropped by 41% between 2004 and 2009, and the industry reacted by diversifying away from apparel and increasing the value added of local operations, for example by providing complete packaging. There has been a partial recovery since 2010, with employment growing but still significantly below the level of a decade ago.

Haiti is the other country in the Caribbean with an export processing industry, focused almost exclusively on garments. The country suffers from low capacity and particularly high non-labour costs, but the garment industry remains competitive because of the advantage provided by the Haitian Hemispheric Opportunity through Partnership Encouragement (HOPE) Act of 2006 in the United States. This legislation offers free access to the United States market for garment products manufactured in Haiti irrespective of the provenance of the textiles.[17] This advantage has been granted until 2020 but may be extended on the basis of humanitarian considerations. Almost all investments in EPZs in Haiti are foreign, predominantly from Asia but also from the Dominican Republic. FDI in EPZs in 2013 was US$ 12 million, a significant increase over earlier years but still indicative of the modest size of the industry.

Overall, the scope for attracting large amounts of FDI into export-oriented manufacturing in the Caribbean is limited. In different degrees, all the economies suffer from high energy costs, poor infrastructure and low capabilities. Wages are generally higher than in Central America or Asia, and the generous tax concessions awarded to these industries are matched elsewhere. The Dominican Republic has been the largest recipient of investments in this sector, but even there industry is struggling to accommodate the rise in wages that comes

[17] By comparison, garments produced in the Dominican Republic or any Central American country have to be made with inputs from those countries or the United States. In practice this means that manufacturers based in Haiti can source their textiles directly from Asian countries.

with economic growth. If the specific advantages of the HOPE Act are maintained, Haiti has the potential to attract more investments in this sector.

On a smaller scale, there are interesting examples of export-oriented manufacturers operating outside of the Dominican Republic and Haiti. One is Lenstec of the United States, which has had a high-tech production facility for intraocular lenses in Barbados since 1996. This can be seen as the poster child for FDI, creating relatively highly paid jobs and making use of Barbados' high levels of education and relatively low costs and the fact that the population is English-speaking. Another example is Nucor of the United States, which reassembled a mothballed steel plant from Louisiana in Trinidad and Tobago in 2005 and has since expanded it several times, producing steel for export. Each of these cases involves investments that are small by international standards but substantial by those of the recipient economies. Another distinguishing feature is that they focus on very specific strengths in these economies, whether they be the highly educated population base of Barbados or the availability of affordable gas upon which steel production depends in Trinidad and Tobago.

(b) Business process outsourcing (BPO)[18]

By and large, BPO is the most important type of export-oriented service in the Caribbean. BPO is an appealing sector in economies where wages are competitive but capital investment is relatively expensive. It is also attractive for the host country because it creates a large number of jobs per million dollars invested (see ECLAC, 2014a, chapter III). It is a broad sector that can include a range of segments of varying degrees of sophistication. At the low end, there are call centres, but at the high end it includes technical support, accounting and even management. The primary issue in attracting FDI in services is the ability to provide a product cost-efficiently, but worker education levels take on more importance when it comes to moving up the BPO value chain. Thus, several companies in Suriname provide call centre services for the Netherlands, benefiting from linguistic and cultural familiarity and a relative cost advantage. Similarly, Guyana provides primarily low-level call centre services to companies in the United States, again benefiting from a common language. Somewhat higher up the value ladder, the Dominican Republic has several operators that offer bilingual services in English and Spanish and are thus able to capture a larger share of the market. Jamaica's BPO sector employs some 14,000 people, not only in call centres but also in firms providing extensive financing and accounting services (JAMPRO, 2014). Cost, language and proximity to the United States are the primary attractions for investors.

One of the primary operators in this business-to-business sector is KM² Solutions of the United States. Within the Caribbean, the firm has operations in Barbados, the Dominican Republic, Grenada and Saint Lucia. Having originally started in Saint Lucia, it encountered physical capacity issues there and expanded internationally. In Barbados, it employs around 750 people in a rapidly expanding business. It benefits from the highly educated workforce in Barbados, as well as the language and cost advantages mentioned earlier. At the highest end of BPO, although this goes beyond traditional BPO operations, Canada's Gildan Activewear has substantial management operations in Barbados, where it has been running back office finance, marketing, production planning and international sales since 1998. This is different from traditional BPO in several ways: first, the company is not outsourcing the services to another company, but simply operates its divisions from Barbados. Second, it creates high-quality jobs that are well paid and make use of the highly educated local population. Finally, while operators such as KM² are flexible when it comes to downscaling and upscaling (being willing to recruit and shed staff as needs require), Gildan's commitment to the local economy is more permanent. Altogether, such an investment thus yields significant benefits to the Barbadian economy.

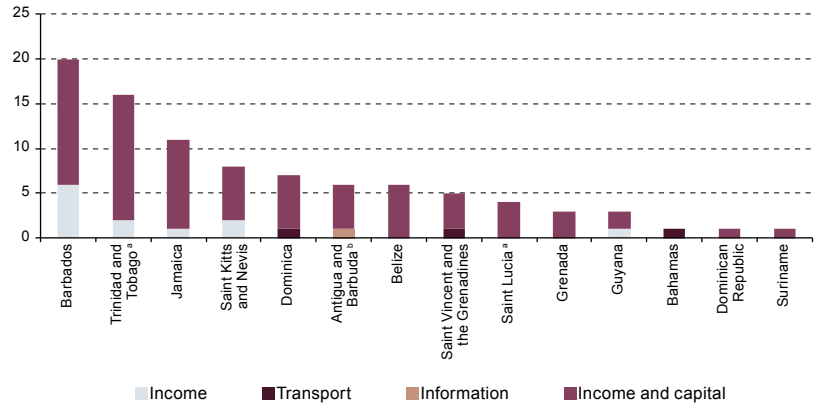
(c) Financial services

Financial services are important throughout the Caribbean region. While some economies, such as those of the British Virgin Islands and the Cayman Islands, are especially renowned for their financial services industry, others also attract significant investment. This is not a capital-intensive sector, of course, so the total quantity of investment may not be large, but the quality and quantity of employment are substantial. The existence of an active financial services sector may also have positive spillovers for human capital accumulation. With respect to employment, the financial services industry is at the high end of BPO, so it is not surprising to see that the major players once again include Barbados, as well as some of the territories not covered in this chapter (such as those of the Dutch-speaking

[18] The topic of BPO is discussed extensively in ECLAC (2009), chapter II.

Caribbean). A necessary condition for the development of a successful financial services sector is a strong tax treaty network. Figure II.5 shows that Barbados leads the region with respect to different types of tax treaties, though certain jurisdictions, such as the Bahamas, do not levy any income tax and thus do not require double taxation agreements.

Figure II.5
The Caribbean (selected economies): international tax treaties per jurisdiction, 2011
(Number of tax treaties)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations Conference on Trade and Development (UNCTAD), "Country-Specific Lists of Double Taxation Treaties" [online] http://unctad.org/en/Pages/DIAE/International%20Investment%20Agreements%20%28IIA%29/Country-specific-Lists-of-DTTs.aspx.
[a] 2010 figures.
[b] 2008 figures.

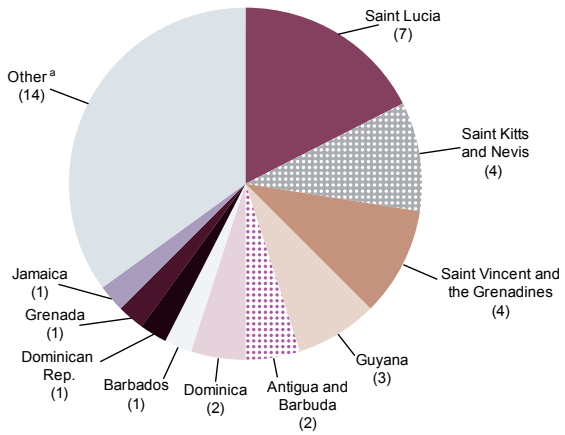
(d) Offshore education

Another non-traditional export-oriented service sector is offshore education. Since the 1980s, in response to the rising costs of (particularly) medical education in the United States, offshore schools have been set up, primarily in the Caribbean. These schools focus mostly on the North American market and attract students by their relatively low costs and attractive locations. They only have a marginal presence in the local education market and are generally operated as profit-making businesses. Today, medical schools still make up the great majority of such establishments, although there are also offshore schools for dentistry and veterinary medicine. Most schools have programmes that encourage local students to enrol as well, although the latter's share of total enrolment remains low. In secondary education, there are some foreign-owned establishments, such as the International School of Port of Spain, but these are not export-oriented, focusing instead on the domestic market.

As shown in figure II.6, Saint Lucia hosts the largest number of medical schools, with seven institutions. The other OECS member States also host a substantial number (13 in total), while Guyana has two and a few other economies just one. As evidence of the value of such establishments, Canadian private equity firm Atlas Partners LP and pan-Asian firm Baring Private Equity Asia spent US$ 750 million to acquire a majority stake in Grenada's St. George's University in 2014.[19] Offshore education is a sector that offers many advantages to economies: it is not capital-intensive, but it does create relatively good jobs and attracts consumers who spend a significant amount of time and money on the island, benefiting the balance of payments. According to the newly established (2011) American University of Barbados School of Medicine, there are also significant spillovers for tourism establishments, both from visits from family and friends and from the holding of medical conferences. Governments do not have many incentive programmes for offshore education, even though these have the potential to attract more investment into this potentially beneficial sector, especially in economies that are not currently involved in it. DeVry University Group of the United States is one of the largest players in offshore education, having acquired the Ross University School of Medicine (Dominica) and School of Veterinary Medicine (Saint Kitts and Nevis) in 2003 for US$ 310 million and the American University of the Caribbean (Sint Maarten) in 2011 for US$ 235 million.

[19] See *The Wall Street Journal* [online] http://blogs.wsj.com/atwork/2014/08/08/st-georges-university-lands-750m-investment-deal/.

Figure II.6
The Caribbean: numbers of offshore medical schools per jurisdiction, 2015



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of Foundation for Advancement of International Medical Education and Research (FAIMER), "International Medical Education Directory", 2015 [online] https://imed.faimer.org/.
[a] "Other" locations are primarily in the Dutch-speaking Caribbean.

4. Market-seeking FDI

Market-seeking FDI is defined as FDI whose purpose is to produce and sell a product in a specific market, rather than export it. This is one of the main types of FDI around the world. Usually, market-seeking FDI focuses on large markets and promising growth prospects. The first of these conditions is not applicable in the Caribbean, while the second only applies to a limited number of economies. However, two strategies make the Caribbean attractive for market-seeking FDI. First, certain companies do not see the individual economies as their markets, but operate throughout the region, thus achieving an economy of scale that makes investment worthwhile. This is particularly the case in the banking and telecommunications sectors. Second, low levels of competition in individual markets make profit margins relatively high. In many markets, there are only a few firms that offer certain products. This applies not only to telecommunications, but also to building materials and certain basic foodstuffs. Moreover, some market-seeking FDI in banking and food and beverages, for instance, centres on mergers and acquisitions to consolidate a market position.

In the Caribbean, the banking sector is controlled almost completely by market-seeking FDI, primarily from banks based in Canada. The largest player is Scotiabank, which has been operating in the subregion since 1889, when it opened a branch in Jamaica. It is now active in countries throughout the subregion, including the Dominican Republic and Haiti, and also has branches in Asia, Europe and North and South America. As Scotiabank has a large banking network in the Caribbean, improved financial integration could be partially achieved by improving interoperability between its branches, which do not currently cooperate much across countries. Conversely, local banks are dominant in the Dominican Republic and Haiti.

In telecommunications, there are just three primary players in the entire Caribbean. The United Kingdom's Cable & Wireless Communications descends from the original monopolist in most jurisdictions, where it now operates through its subsidiary LIME. LIME is active in all OECS member States, as well as Barbados and Jamaica. Furthermore, it owns shares of around 50% in operations in the Bahamas and Trinidad and Tobago. LIME is in the process of expanding its network coverage, which involves significant investment flows. Digicel, based in Jamaica, has operations in most economies as well, including Haiti since 2006, although the Dominican Republic is a notable exception. Barbados' Columbus Communications has significant operations in Barbados, the Bahamas, Grenada, Jamaica and Trinidad and Tobago through its subsidiaries Flow and Cable Bahamas. During 2014 it was taken over by Cable & Wireless Communications for US$ 3 billion. Finally, América Móvil is the largest player in the Dominican Republic through its Claro subsidiary, but it withdrew from the Jamaican market in 2011 by selling its assets to Digicel.

The energy market in the Caribbean is relatively fragmented, which is troublesome because of the small size of the individual markets. Particularly in the eastern Caribbean, integration of the different networks would have the potential to yield significant scale advantages. Several international players have Caribbean operations, although these are primarily focused on the larger markets. In 2007, Japan's Marubeni purchased 80% of JPS of Jamaica for US$ 553 million, of which half was later resold to Korea East-West Power. Marubeni also has significant assets in Trinidad and Tobago. Interenergy (co-owned by the International Finance Corporation) is a large player in both the Dominican Republic and Jamaica. AES Corporation of the United States also owns a large power plant in the Dominican Republic. One international investor that is also involved in smaller markets is Canada's Emera, which controls significant assets in the energy markets of the Bahamas, Barbados, Dominica and Saint Lucia.

Other small-scale market-seeking investment can also be seen in individual economies. Caribbean Grains, a grain-processing company operating in several parts of the Caribbean, is one example. It recently started operating a new flour and feed mill in Saint Lucia, in addition to existing assets in the French-speaking Caribbean. For the company, operating in Saint Lucia has the advantage that it is the only grain mill in the country and can corner the market thanks to its first mover advantage. Similarly, Trinidad and Tobago-based TCL Group has a number of subsidiaries in different Caribbean economies to supply cement to those individual markets. Subsidiaries include Arawak Cement in Barbados and TCL Guyana.

Only a few economies in the Caribbean can claim to have markets large enough on their own to attract significant investment. The Dominican Republic, Haiti, Jamaica and Trinidad and Tobago are among those that occasionally attract substantial amounts of purely market-seeking investment. One example of a highly internationalized sector is the beer sector. Of the leading beer producers, only Carib Brewery (Trinidad and Tobago) is still locally owned. Cervecería Nacional Dominicana was sold to Anheuser-Busch Inbev in 2012, Brana of Haiti was sold to Heineken of the Netherlands in 2011 and Diageo of the United Kingdom has owned a majority shareholding in Jamaica's Desnoes & Geddes since 1993 (see also box I.3).

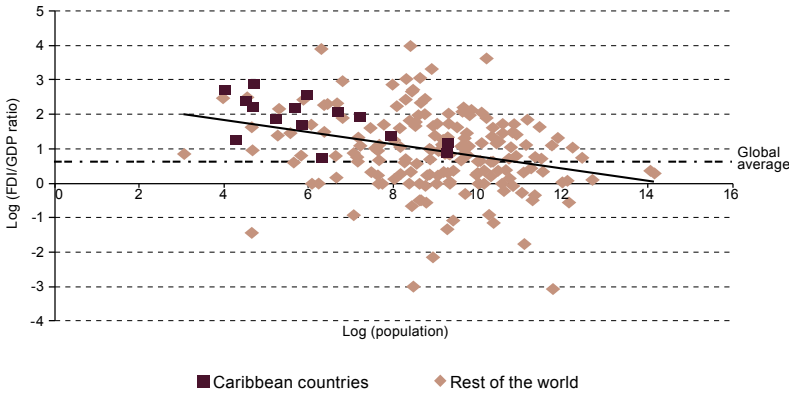
Market-seeking FDI can bring significant benefits to local economies. By increasing competition, it improves service delivery and reduces prices, thus increasing consumer surplus. Although beneficial in principle, such investment has a cost. As discussed below, Caribbean investments are often associated with significant fiscal and non-fiscal benefits, the costs of which are borne by taxpayers. Market-seeking FDI is intended to take market share from other (possibly locally owned) companies, and it is thus more likely than other kinds to crowd out domestic entrepreneurs, which makes the long-term impact on the balance of payments less clear. While the immediate capital account inflow benefits the country, outflows of income from FDI in subsequent years can represent a permanent burden on the current account. Looking beyond the impact on the balance of payments, market-seeking FDI can have positive impacts on the local economy through its effects on secondary suppliers, as well as the lower prices already mentioned.

D. FDI promotion policy[20]

As noted above, the level of incoming FDI in the Caribbean is relatively high by comparison with other regions. Caribbean nations have an average FDI to GDP ratio of 4.2%, as compared with 2.6% in Latin America. Small economies generally tend to have somewhat larger FDI ratios, as can be seen in figure II.7, but the Caribbean has attracted particularly significant amounts of FDI, even if there has been a decrease in inflows since the financial crisis. Only the two worst-performing Caribbean nations, which in 2014 were Haiti and Suriname with ratios of 1.1% and 0.1 respectively, lag the global average of 1.9% (for 2013). One of several reasons why the Caribbean is able to attract such large amounts of FDI is because of FDI promotion policies, both financial and non-financial. It is difficult to quantify such policies precisely, but they appear to be more generous than in other regions.

[20] This section is partly based on De Groot and Pérez Ludeña (2014) and De Groot (2014b).

Figure II.7
The Caribbean and the rest of the world: foreign direct investment (FDI) to GDP ratio in relation to population size, 2013



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations, "National Accounts Main Aggregates Database", Statistics Division, 2015 [online] http://unstats.un.org/unsd/snaama/dnllist.asp; United Nations, "World Population Prospects: The 2012 Revision", 2014 [online] http://esa.un.org/unpd/wpp/index.htm; and United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2014* (UNCTAD/WIR/2014), Geneva, 2014.

Putting these two facts together could be construed as saying that the Caribbean's policy of attracting FDI has been very successful, but such causality cannot be assumed without further proof. After all, FDI inflows cannot necessarily be tied to the generosity of the incentives. Moreover, even if there is a causal relationship between FDI promotion policies and FDI inflows, this does not in itself say anything about the impact of FDI. Whether that impact is positive is a matter of ongoing debate, as discussed in De Groot (2014a). Finally, even if incoming FDI does have a positive impact, a cost-benefit analysis would be required to determine whether the region's generous FDI promotion policies are justifiable.

De Groot (2013) outlines a methodology for analysing the impact of FDI promotion policies in the Caribbean.[21] The first step is to determine the objectives of the policy (UNCTAD, 2012b). These may be to increase employment or the capital base, but may also reflect a desire to improve the level of technology used in an economy. To achieve these objectives, a policymaker may propose certain FDI promotion policies. Different types of such policies are discussed below, but in principle they can include anything aimed at increasing the level or quality of FDI. These policies exercise an influence on the level or quality of FDI, which then links back to the policy objectives. Even though some policies (reducing unnecessary regulation, increasing judicial efficiency) may have positive non-FDI side effects that seem to justify them, only once all the corresponding linkages are confirmed is an FDI promotion policy truly justified.[22]

1. Different types of FDI promotion policies in the Caribbean

Bartels and De Crombrugghe (2009, p. 2) argue that FDI promotion policies "…are meant, at best, to shape —or even distort— the economic environment of the host country in order to attract and retain higher levels of value-adding FDI". FDI promotion policies can include a range of measures, which may be separated into four different types:

- Policies that focus on improving the overall business climate, benefiting both domestic and foreign producers. Examples of such policies include reducing bureaucratic hurdles to setting up a business, improving the judiciary by guaranteeing property rights, and increasing the level of security in regions that require this.
- Policies that focus on removing or reducing obstacles specific to foreign investors. They may include, for example, liberalizing migration policies for foreign workers, guaranteeing non-discrimination in government procurement between domestic and foreign suppliers or concluding double taxation agreements with other countries.
- Active investment promotion by an investment promotion agency, focused on resolving information asymmetries between foreign and domestic investors. Examples include the opening of trade offices in foreign countries, both to provide potential investors with marketing information and to assist such investors in overcoming the challenges of investing in a new area.

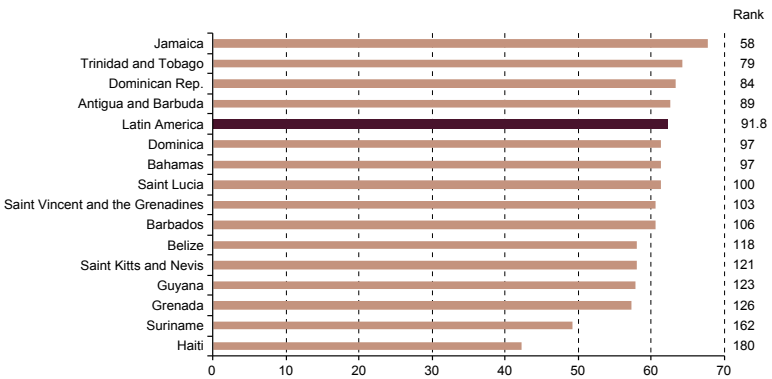
[21] That model is inspired by Blomström and Kokko (2003), who discuss the conceptual framework in which FDI operates. It differs somewhat from the outline provided by UNCTAD (2012b), which focuses more strongly on policy coherence and the sustainability of development.

[22] This linkage has been the subject of many academic contributions, including Harding and Javorcik (2011) and Lim (2005).

- Policies that use financial measures to stimulate FDI, primarily tax holidays of different types or exemptions from import and export duties. However, financially costly measures can also include generous grants or subsidies for the initiation or continuation of certain investments.

The first of these (improving the overall business climate) is likely to have the strongest impact on economic growth, since it stimulates both domestic and foreign investment. This approach has long been used in the Caribbean and as a result many economies have very low corporate and income tax rates (there is, for example, no income tax in the Bahamas), but has rarely moved beyond the financial aspect of the business climate. According to the *Doing Business 2015* report (World Bank, 2014), most Caribbean economies do not rank high for ease of doing business. Figure II.8 shows that only Jamaica, ranked fifty-eighth in the world, performs substantially better than the Latin America average, with some economies ranking among the worst in the world. The rankings of Haiti (180th) and Suriname (162nd) can be put in perspective by considering the rankings earned by war-torn nations such as Iraq (156th), Sudan (160th) and the Syrian Arab Republic (175th). Clearly, the Caribbean is lagging the rest of the world in its efforts to lower bureaucratic hurdles and improve judicial efficiency.

Figure II.8
The Caribbean (selected economies): distance to the frontier [a] on ease of doing business and global ranking, 2015



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of World Bank, *Doing Business 2015: Going beyond efficiency*, Washington, D.C., 2014.
[a] The Doing Business indicator is a composite of subindicators, each of which is maximized at 100 for the best-performing country: the frontier. A score of 60 thus implies that a country scores 40% below the top performer on the average subindicator.

The quality of governance in the Caribbean is relatively high compared with other regions at a similar stage of development. Of the elements of governance discussed by Kaufmann, Kraay and Mastruzzi (2009), regulatory quality should be a particular area of focus for Caribbean governments since it directly influences the business environment in which foreign investors thrive.

Owing to the relatively small size of Caribbean economies, individual policy actions can make a significant practical difference in the day-to-day operations of foreign investors. Thus, monitoring investor experiences and attempting to ameliorate the bottlenecks identified by investors continues to be an important task for investment promotion agencies. Governments can also do more to encourage the building of local capacities. Foreign investors are often attracted to locations where local markets can provide the inputs they need; and Caribbean economies tend to fall short in this respect. While the level of education is relatively high, workers' skills are not sufficiently developed to meet the needs of the labour market. Similarly, many economies lack local producers of the intermediate inputs needed by investors. In addition to increasing an economy's attractiveness for investors, encouraging the production of intermediate goods also deepens the quality of local value chains and thus greater benefits are derived from FDI.

The second type of FDI promotion policy relates to foreign investors only. In 1994, all Caribbean Community (CARICOM) members except Suriname signed a double taxation agreement between themselves. As discussed above (see figure II.5), the size of tax treaty networks differs by country. Although most countries have concluded double taxation agreements with their primary investment partners (the Netherlands, the United Kingdom and the United States), further strengthening the network of double taxation agreements could provide additional incentives for investors to consider certain investment locations. With respect to migrant worker policies and non-discrimination

clauses in government procurement, the region still lags. Only Belize has specific regulations that allow foreign investors to benefit from eased migration restrictions. Similarly, few of the subregion's governments provide equal opportunities to foreign and domestic companies in government procurement. Volosin (2012) compares procurement procedures throughout Latin America and the Caribbean. She finds that only 38% of countries in the Caribbean stipulate competitive processes as a fixed rule, while elsewhere in Latin America some 58% do so. The evaluation criteria used in public procurement are unspecified or insufficiently specified in 10 of 13 Caribbean countries, as against just 5 of 19 other countries. The positive exceptions in the Caribbean are Antigua and Barbuda, Grenada and Jamaica.

Improving these non-financial features of FDI promotion policies could help to stimulate investment in, for example, infrastructure, which has benefits that are particularly likely to spill over into the rest of the economy. Non-financial FDI promotion policies have the added benefit that they are less costly than financial ones. Citizenship by Investment (CbI) programmes are another interesting example of a non-financial FDI promotion policy aimed specifically at foreign investors. First pioneered by Saint Kitts and Nevis in 1984, and later adopted by both Dominica and Antigua and Barbuda, these programmes provide investors with citizenship in the target country in exchange for a relatively small investment (or donation). In Saint Kitts and Nevis, this is a primary means of financing much investment in tourism infrastructure, with interested persons purchasing US$ 400,000 shares in new developments in exchange for usage rights and citizenship. This programme is considered to have been very successful in attracting both short- and long-term investors, largely from Asia, the Middle East and the Russian Federation.

CbI programmes have some potential downsides as well. Since citizenship of OECS and CARICOM countries brings with it certain mobility rights in other States, such programmes can attract some ire from nearby neighbours, although these other nations may also benefit from such investments. Second, one of the advantages of being a citizen of Saint Kitts and Nevis (or other CARICOM countries) is visa-free travel to many countries, particularly the United States. The United States thus frowns upon the granting of citizenship to individuals who may pose a threat to the country. Thanks to what are claimed to be careful background checks, there have not been many problems so far, but if the United States were to withdraw visa-free access for CARICOM citizens, this would be a great blow to the region.[23] Finally, as shown by the launch of Antigua and Barbuda's and Dominica's CbI programmes, the benefits are so apparent that the market for citizenship has attracted competition from other jurisdictions, driving down prices. Dominica, for example, only requires an investment of US$ 100,000, the cheapest in the world. Grenada used to have a CbI programme that required investment of as little as US$ 40,000, but it was abolished after the attacks of 11 September 2001 in the United States. Grenada's new programme, introduced in 2013, is supposedly limited to investors who are specifically invited to apply. A potential problem with CbI programmes may be that land purchases in small, land-scarce islands puts prices beyond the reach of the local population.

The third type of FDI promotion policy involves the role played by investment promotion agencies (IPAs). This is a challenging aspect of promotion policy, since many of the economies involved are relatively small and thus cannot afford large information campaigns and may have trouble attracting qualified staff. This is unfortunate, since the literature (for example, Harding and Javorcik, 2011) argues that the use of IPAs may be the most cost-efficient way of increasing FDI. The approach taken to this by the Caribbean Forum of African, Caribbean and Pacific States (CARIFORUM) could be considered a blueprint for similar regions. In 2007, it created the Caribbean Association of Investment Promotion Agencies (CAIPA), a single body that promotes the interests of all its 19 members. This is done through two primary channels: first, in thus combining, its members can build capacity more effectively by jointly purchasing important inputs (such as informational databases) and holding training sessions; second, CAIPA takes a regionwide approach to promotion, recognizing that organizations often choose a region before settling on a specific country. In this way, local IPAs do not have to take such a broad approach in their own activities.

Unfortunately, as in other regions, and some limited academic literature aside, there is little evidence from formal analysis of these agencies' effectiveness and real impact on inward FDI. Many of the economies are too small to be able to sustain IPAs with sufficient capacity to manage all the duties performed by these agencies in

[23] The United States has given a warning to Saint Kitts and Nevis to this effect and Canada has instituted visa requirements for the country's citizens due to an incident involving one of its passport holders.

more developed countries. There is also great variation between different economies in investor appreciation for the IPA. An organization such as SKIPA (Saint Kitts) is a true one-stop shop that is able to provide the full range of investment-related services and is highly appreciated by the investors making use of it. At the other extreme, there are countries where IPA services are merely an afterthought for another State agency.

The fourth and most important channel for FDI promotion policies are financial incentives. Here, Caribbean governments are very active. Among the most typical financial incentives are the following:

- Income taxes: All economies provide some relief from income taxes (except for the Bahamas, which does not levy income tax), but do so under very different regimes, with a 15-year full exemption being most common. While some economies limit exemptions to specific sectors and others such as Belize allow exemptions only in special free zones, in other economies these exemptions are provided without reservations.
- Dividend taxation: Most of the economies that have any sort of withholding tax on dividends also provide an exemption for foreign investors, although this is usually limited to the first 10 to 20 years after investing.
- Duties on imported materials: Nearly all the economies provide some sort of reduction or exemption for the imported goods and materials required by a new investment. OECS member States, in particular, tend to provide full exemptions without time limits. Some economies have very specific regulations for vehicle importation that may benefit specific individuals or businesses. In Jamaica, for example, there is a tax exemption for the import of agricultural vehicles.
- Property taxes: Property tax regimes differ greatly between economies. In Guyana, for example, no property tax concessions are available. In many OECS member States, on the other hand, investors are eligible for a 15-year full exemption.
- Other financial incentives: In addition to the above, there are several other regulations in particular countries aimed at making economies more attractive to foreign investors. Where they are in place, foreign investors are often exempted from exchange controls, and stamp duty on land purchases is also often reduced or waived. Some of the economies in the region also provide specific training grants or research and development (R&D) subsidies (for example, Jamaica and Grenada), or even subsidies for renting office space (Barbados). Accelerated depreciation allowances are also offered to investors.

It is clear that the incentives available in the region are very generous; moreover, the conditions for qualifying for them are often not strict. While they are sector-specific in certain countries (often focusing on tourism, manufacturing or agriculture), only a few economies have strict qualifying regulations. Barbados, for example, requires financing sources to be external, while Belize requires companies to create employment, transfer skills and earn foreign exchange if they are to be eligible for any subsidies. Many governments do state "preferences" with regard to foreign investment, although these are not necessarily hard requirements, and most have stated goals for employment creation or the generation of foreign-exchange inflows.

Many Caribbean economies provide a full tax holiday for investors in export-oriented activities. The BPO industry is practically exempt from any income tax. Even the extractive industries, which in most other regions are subject to stricter tax regulations that often include royalties, benefit from incentives in the Caribbean. The bauxite mining industry in Jamaica enjoys tax advantages. Guyana levies a modest royalty (5%) on gold mining and none on bauxite. The only major exception is the oil industry in Trinidad and Tobago, where private companies (most of them foreign) enter into revenue-sharing contracts with the government; these are negotiated case by case and provide the government with substantial income. In Suriname, the national oil company, Staatsolie, also continues to play an important role in the exploitation of the country's reserves, and any foreign participation is strictly under its leadership.

Besides the generous tax exemptions formalized in law, governments add discretionary waivers for individual companies. As a result, there is often great uncertainty about the kinds of incentives available to investors and significant flexibility for decision-makers that does not necessarily enhance the effectiveness of incentive schemes. In Haiti, this has been identified by investors as their foremost concern about the investment climate. Increasing transparency in the allocation of financial incentives should be a goal in itself, since it would also lead to a more efficient distribution of scarce resources (Goyal and Chai, 2008). The Government of Jamaica, for example, has taken a step in this direction with the Omnibus Tax Incentive Act, passed in December 2013, which replaces all existing tax incentives and bans further discretionary waivers. Despite liberal incentives, FDI in the region has often shifted to locations outside it when these expire.

2. The impact of FDI promotion policies

The impact of FDI promotion policies is complex to analyse. It is beyond the scope of this chapter to scrutinize the entire system, but it is worth looking at whether the FDI promotion policies in place are having the desired impact. Of course, this is contingent on knowing what impact is being sought by governments in the region. The following are the most important reasons identified by policymakers for pursuing such policies:

- FDI is sought to decrease unemployment. Unemployment rates are very high in some economies such as Saint Lucia, and in those cases the primary concern of policymakers is to reduce the unemployment rate, particularly for the young.
- Policymakers in the region are worried that there is a degree of underinvestment in their economies as a result of their low investment capacity. However, data from the United Nations Statistics Division (United Nations, 2015) show that the rate of gross fixed capital formation (GFCF) in the Caribbean is actually somewhat above that of comparable economies. Moreover, as shown in figure II.9, the correlation between FDI and GFCF is very weak in most economies. In only four economies is there arguably a statistically significant relationship between the two.
- A third reason for attracting FDI is the hope that there will be technological spillovers from these investors in the local economy. Such spillovers can help companies or even entire economies to climb up the global value chain.
- The final major reason is that in the Caribbean, whose primary product is tourism, investments on the scale needed to keep accommodation up to the constantly rising standards of international rivals and thereby stay competitive require the participation of large international investors. This also applies to the extractive industry, which in the Caribbean is likewise dependent on FDI inflows.

The question then becomes whether the FDI promotion policies currently in place actually address these issues. Policymakers often believe that investment would quickly dry up without them. However, investors do not rank financial incentives among the top reasons for investing in the region (CAIPA, 2013). Rather, they are attracted by its strategic location, its educated and English-speaking workforce or the availability of a relatively large pan-Caribbean market. At the moment, there is little hard evidence for the impact on FDI and economic growth of the generous incentives given by Caribbean governments. It seems likely that policies to enhance the overall investment climate would have more success, and they would benefit domestic and foreign investors alike. Also, given high levels of debt in the region, the opportunity cost of these incentives in terms of foregone public investment in infrastructure, human capital and the business environment can be quite high.

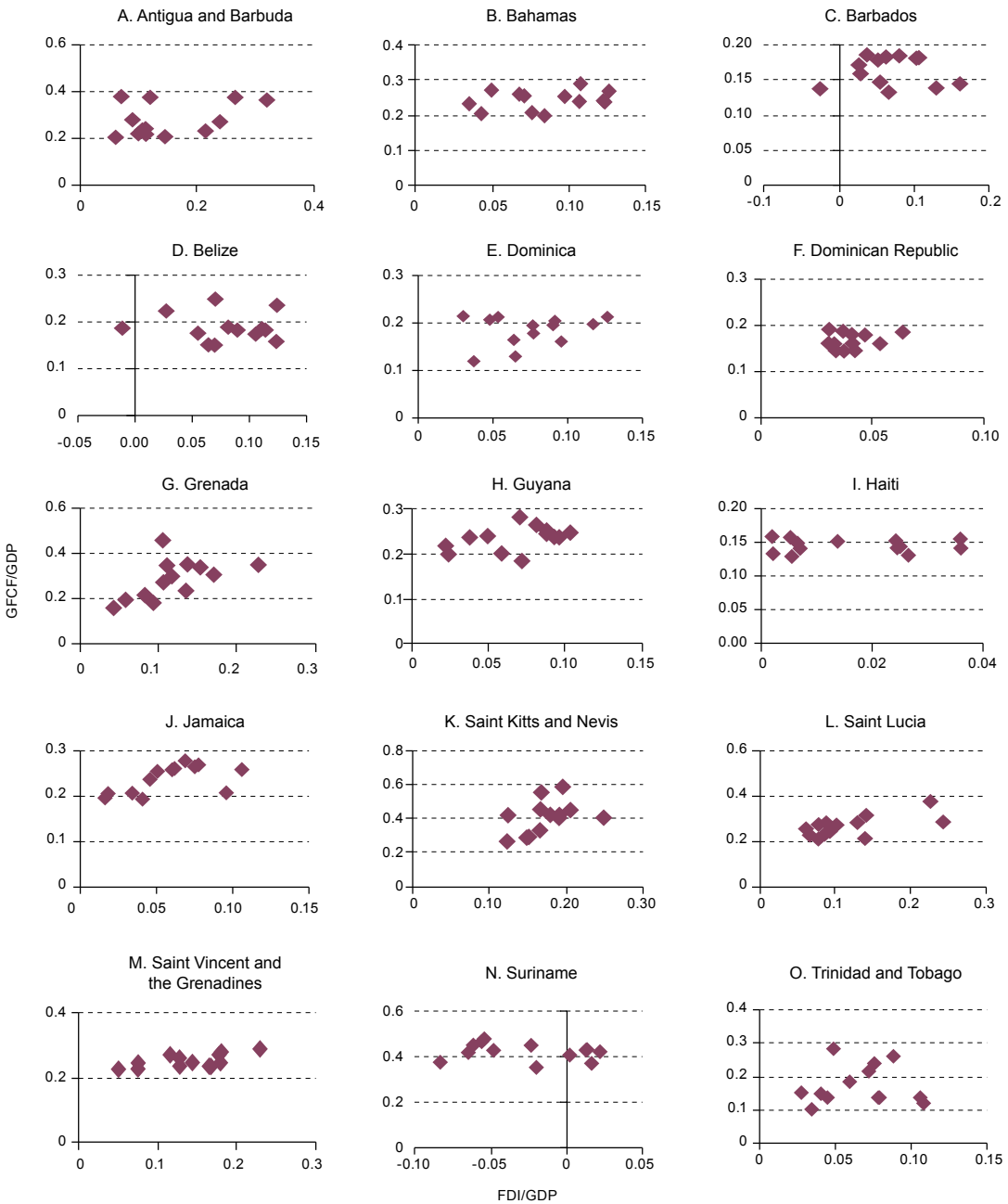
Goyal and Chai (2008) are among the few academics to have looked at tax incentives in the Caribbean, analysing tax regimes in different OECS members. According to these authors, countries forego some 9.5% to 16% of annual GDP in tax incentives, without much noticeable impact. They believe that investors are, in fact, not very price-sensitive, and that the removal of generous financial subsidies could yield potential revenue of between 7% and 13% of GDP. This research only deals with firms outside the all-important tourism sector. Nonetheless, on the basis of these results, it seems unlikely that positive spillover effects from FDI justify the cost. Over and above, the use of tax policy to favour certain foreign-driven sectors over domestically run ones results in a cost transfer to these domestic investors, putting them at a competitive disadvantage.

The situation is made worse by the stressed public finances of most Caribbean countries, as seen in table II.1. ECLAC (2014c) reports that the average budget deficit in 2014 was 3.9% of GDP (excluding the Dominican Republic and Haiti), with six countries having deficits of over 5%. The total national debt reached close to 100% of GDP in Antigua and Barbuda and Barbados and 127% of GDP in Jamaica, further increasing these economies' vulnerability. At a time when many Caribbean countries are reducing their fiscal deficits, the incentives granted to foreign investors have to come from higher taxes on other constituencies. These raise the costs of doing business in the economy and may even be pushing many local companies into the informal economy. The impact of FDI promotion policies and the size of the benefits from FDI overall are the subject of a lively academic debate, as summarized in De Groot (2014a).

Exemptions from import duties are a special case, however. Import duties in the Caribbean are relatively high and, combined with the high costs of transportation to the region, impose a significant burden on business. Particularly in the early-stage development of new projects, when many inputs are required, import duty waivers are critically important. It is not clear, however, why a distinction should be made between local and foreign investors when these

waivers are granted. Rather, CARICOM ought to pursue cuts in common tariffs to reduce the need for waivers. This is particularly the case when duties are levied on products that have clearly positive spillover effects, such as solar power generating equipment. One complicating factor is that import duty waivers reduce incentives for local sourcing, which is among the primary benefits of investment. However, when local companies are able to deliver consistently high product quality, they should be able to compete with imported products on this rather than on price alone.

Figure II.9
The Caribbean (selected countries): foreign direct investment (FDI) to GDP and gross fixed capital formation (GFCF) to GDP ratios, 2001-2013



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations, "National Accounts Main Aggregates Database", Statistics Division, 2015 [online] http://unstats.un.org/unsd/snaama/dnllist.asp [date retrieved: 7 January 2015].

Tax competition is leading to a race to the bottom in which tax advantages offered by one jurisdiction are matched by others competing for FDI. This is more problematic in the Caribbean than in other regions because economies are often competing for the same projects, particularly in tourism and BPO. It is difficult for governments to differentiate their own product offering in these markets. Klemm and Van Parys (2012) analyse this form of strategic interaction in taxation rates and find that it is particularly marked in Latin America and the Caribbean.

In CARICOM, there are currently proposals to harmonize incentives that, if approved, will cap these at a common level to reduce the burden of financial FDI promotion policies without negatively affecting the level of overall FDI. This could go a long way towards addressing the problem in the Caribbean region whereby the costs of attracting FDI may be larger than the benefits from such investment. Bird (2000) argues that "[w]hy so many governments opt for incentives in the absence of any solid evidence that they produce economically significant results remains a puzzle to many economists" (p. 201). He believes that with tax coordination across the region (admittedly a challenge), overall welfare could be increased. The World Economic Forum (WEF, 2013, p. 8) describes investment subsidies as "a coordination failure among governments [that] are, like most subsidies, inefficient". Additionally, it argues that they divert attention away from truly hard decisions about measures to improve the overall business climate. While doing so could help domestic and foreign investors alike, it is usually more difficult than offering incentives. Furthermore, even if policymakers were eager, it is not certain that many of the economies in the subregion actually have the institutional capacity to make such changes.

3. FDI and economic development in the Caribbean

The relationship between FDI and economic development is ambiguous and the subject of much academic debate. One of the most relevant questions is: how does FDI impact economic development? The previous subsection showed that thereis no clear causal link between FDI and increased fixed capital formation and that the Caribbean is not suffering from a lack of capital investment. Furthermore, FDI may lead to the creation of jobs for the local population or value chains from which local enterprises can benefit. One last hypothesis is that FDI may simply be necessary to compensate for the large current account deficits in the Caribbean countries.

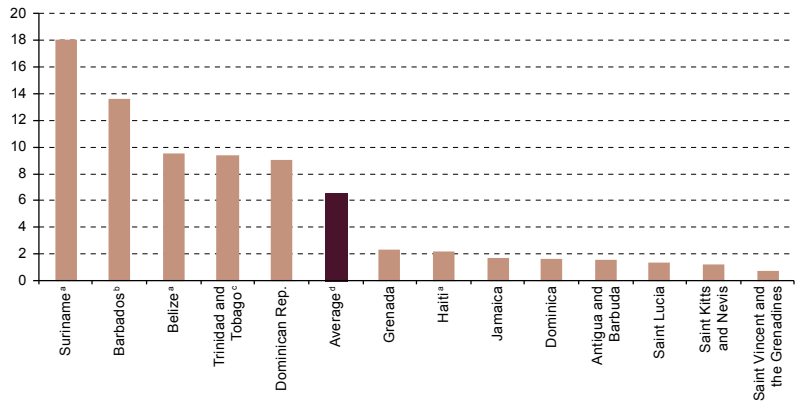
Since unemployment is a serious issue in many Caribbean economies, jobs created by foreign investment would theoretically have a beneficial impact in terms of economic development. However, it is not clear that foreign investors are better job creators than local investors. Indeed, foreign investors are more likely to use foreign staff for the best-paid jobs and local investors may be better able to make optimal use of local labour market conditions. This leads to a second point: the skills of many workers in the Caribbean do not match the needs of employers. As a result, large employers, which tend to be foreign, are required to provide extensive training in order to build the skills they need in their workforce. In this regard, therefore, FDI can be considered to impact positively on economic development since it works as a channel to improve the skill level of local workers.

Local value chains do not tend to attract much attention in the Caribbean, even though policy can play an important role, for example, in connecting local goods producers and foreign investors. Currently, many foreign investors import a large share of their inputs, despite the high cost of doing so in the Caribbean. They do so because of limited local capacity to provide those inputs. While it is understandable that not every country can manufacture high-tech inputs, it would perhaps be feasible for these economies to aim to provide the agricultural inputs required by large hotels and resorts. Investors argue that the local producers are not able to deliver goods of a sufficiently high and consistent quality, which should be a call to action for the governments of the subregion. Policies that focus on improving the capacities of local producers to enter the value chains of these different industries would significantly enhance the benefits derived from inward FDI.

With respect to the balance of payments, as discussed earlier in this chapter, the impact of FDI can be ambiguous. When the initial investment is made, whether in the form of a greenfield project or an acquisition, there is an inflow of foreign exchange into the country and an improvement in the capital account. The long-term effect on the current account is more complicated, however. As the company makes profits, they are recorded as a debit in the current account (income from FDI). Some of this is repatriated and some reinvested, whereupon it will be accounted for as a capital inflow again.

Capital outflows in the form of income from FDI can be quite substantial, although central bank data show that profitability is relatively low in the subregion. Figure II.10 shows average profitability in recent years for foreign investors in the Caribbean. Profits are highest in Suriname, where they average around 18%, having been particularly strong during 2011 and 2012. Barbados does not have complete data available, but profitability is also strikingly high for the years in which it does. Investors in Belize, the Dominican Republic and Trinidad and Tobago also make healthy returns of between 9% and 10%. All other countries for which data are available, however, have very low profitability, particularly by Latin American standards (see chapter I). This is partly down to the economic cycle, since tourism, the most important industry in many economies in this group, has been in decline in recent years.

Figure II.10
The Caribbean (selected economies): returns on FDI, 2008-2013 average
(FDI income divided by the stock of FDI, in percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2014*, Geneva, 2014; and official figures.

Note: Data on stocks are taken from UNCTAD to ensure that figures are consistent across countries.
[a] All investment income is taken rather than only income from FDI. FDI stock data in Suriname are imputed on the basis of official figures for the period from 2008 to 2010.
[b] Data only cover the period from 2008 to 2010.
[c] In 2012 and 2013, all investment income is taken.
[d] Excludes the Bahamas, Barbados, Guyana and Suriname.

The values in figure II.10 are FDI income divided by the stock of FDI in the country. Thus, economies with very large stocks can have low rates of return but still register large outflows of foreign reserves. Table II.4 shows FDI income in recent years. The final column shows how average FDI income compareS with inflows of FDI in recent years. In Belize, Suriname and Trinidad and Tobago, more foreign exchange leaves the country in the form of FDI income than is received as FDI inflows, while in Barbados and the Dominican Republic, FDI is almost neutral for the balance of payments.

E. Trans-Caribbean enterprises

Inflows of FDI into the Caribbean get far more attention than outflows. While nearly every country reports FDI inflows in its balance of payments, many countries do not consistently report the amount of outward FDI, so it is difficult to assess net FDI flows from the Caribbean. Nonetheless, some Caribbean countries are sources of FDI as well, with companies investing not only in their home markets, but also in other Caribbean economies and countries outside the region.

Indeed, this outbound FDI has been ongoing for some time and has often had significant consequences. The Massy Group conglomerate began investing in Guyana, Jamaica and Barbados in the 1970s. The foreign subsidiaries of some trans-Caribbeans are very large and make their own investments in turn. In early 2014, for example, Sagicor Group Jamaica signed an agreement to fully acquire RBC Jamaica from Royal Bank of Canada. This also shows that FDI from the region can involve the acquisition of assets from parties based in developed countries.

Table II.4
The Caribbean (selected economies): FDI income and inflows of FDI, 2008-2013

	FDI income (millions of dollars)						Average FDI income as a share of FDI inflows (percentages)
	2008	2009	2010	2011	2012	2013	2008-2013
Antigua and Barbuda	40.6	35.5	33.3	36.5	50.3	28.7	35.3
Barbados	264.5	310.9	249.8	...	...	...	89.7
Belize [a]	164.8	89.3	137.4	97.7	118.3	117.8	102.6
Dominica	12.5	13.4	7.8	5.0	5.1	15.2	37.7
Dominican Republic	1 668.5	1 518.1	1 528.4	1 802.0	1 836.0	2 397.6	77.8
Grenada	31.7	55.4	30.8	20.6	18.8	13.2	40.2
Haiti [a]	22.5	18.3	10.4	3.2	4.0	15.0	23.8
Jamaica	376.2	231.8	127.0	111.8	125.7	135.5	37.5
Saint Kitts and Nevis	23.4	20.3	18.2	18.7	12.7	19.4	15.1
Saint Lucia	52.5	35.3	31.7	12.0	23.3	15.7	23.1
Saint Vincent and the Grenadines	18.1	12.4	11.0	7.4	5.6	1.4	8.1
Suriname [a]	21.8	25.0	130.4	278.3	218.5	149.2	133.6
Trinidad and Tobago	903.6	781.0	827.0	3 068.6	3 387.3 [a]	2 254.5 [a]	119.3
Total [b]	3 336.2	2 835.7	2 893.4	5 461.9	5 805.5	5 163.1	64.5

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
[a] Data for total investment income rather than FDI investment income only.
[b] Excludes Barbados.

Table II.5 lists four of the largest Caribbean-based companies or conglomerates, all of which have significant operations in the Caribbean outside their home country. All four derive very substantial proportions of their revenue from other countries, although revenue data broken down in this way are not available for all companies.

Table II.5
Data on selected large trans-Caribbean conglomerates

Home country	Massy Group	ANSA McAL Group	Sagicor Group	Goddard Enterprises
	Trinidad and Tobago	Trinidad and Tobago	Barbados [a]	Barbados
Total revenue in 2013 (dollars)	9.4 billion	6.2 billion	1 billion	962 million
Approximate share of revenue from outside home country (percentages)	47	-	60	-
Principal areas of business	Automotive, distribution, energy and industrial gases, finance, industrial equipment, insurance, property, retail and technology	Automotive, beverages, distribution, financial services, manufacturing, services, property	Finance, insurance	Aerosols and liquid detergents, airline catering, automotive, baking, beverages, general trading, ground handling, industrial and restaurant catering, insurance, investments, meat processing, packaging, pharmaceuticals, printing, property, shipping agents, stevedoring and tours, water purification and bottling
Primary foreign investment destinations	Antigua and Barbuda, Barbados, Guyana, Jamaica, Saint Lucia, Saint Vincent and the Grenadines, the United States and others	Barbados, Guyana	Jamaica, the United States and other Caribbean countries	Antigua and Barbuda, Bolivarian Republic of Venezuela, Colombia, El Salvador, Grenada, Guatemala, Honduras, Jamaica, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Uruguay, and other Caribbean countries

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of annual and quarterly reports from the respective companies.
[a] In January 2015, Sagicor Group announced its intention of redomiciling elsewhere to avoid the impact of Barbados' financial instability. What prompted this move was a downgrade of Sagicor Life's bond rating by Standard & Poor's as a result of the downgrading of Barbados sovereign debt.

Overseas investments are important for a company's bottom as well as top lines. For example, Massy Group derives 41% of its before-tax profits from outside Trinidad and Tobago, with nearly all of this coming from Barbados, Guyana and Jamaica.

Most of the FDI undertaken by large trans-Caribbean companies is in the form of mergers and acquisitions. This often leads to restructuring and streamlining of the existing operation, usually resulting in job cuts and other revenue-saving measures. When a gap in the market exists, a greenfield investment is more likely. For example, Sagicor Group made greenfield investments in subsidiaries in Belize and Panama to expand its insurance operations.

Large transnational Caribbean companies tend to be conglomerates, that is, groups of several corporations, some operating in entirely different businesses. This structure is important for the Caribbean, which, even as a whole, is a small market. Because of its economic and geographical properties, the Caribbean is especially prone to economic and environmental shocks. Operating as a conglomerate is thus an important way of smoothing risks, since if one corporation's business is severely affected in a downturn, it can be supported by other parts of the conglomerate operating in different industries. When several corporations operate in related fields, conglomerates can also provide opportunities to form value chains. Of course, this structure has its dangers too —if a conglomerate does not divest failing enterprises, its successful branches may be burdened by the need to support them in perpetuity. This contributed to the collapse of Colonial Life Insurance Company of Trinidad and Tobago in 2009.

Sandals Resorts is exceptional in the region in that it is not a conglomerate but a highly focused enterprise. It is a giant trans-Caribbean company operating all-inclusive resorts throughout the region. Based in Jamaica, the firm began operating in 1981 and continued adding resorts there before opening its first international resort in Antigua in 1991. Now the company has 15 all-inclusive couples-only resorts in 6 countries. Sandals also operates the family- and singles-friendly Beaches Resorts in Jamaica and the Turks and Caicos Islands.

Sandals caters to international visitors, especially from the United States. The opening of a resort can be a major boost for the local economy, stimulating tourism development and even bringing an increase in air travel as airlines respond to increased demand. Investments can take the form of acquisitions, renovations and expansions of existing resorts, sometimes saving them from closing entirely, with all the negative impact this would have on the local economy. Resorts also provide highly coveted jobs; when one opened recently in Barbados, about 5,000 people applied for 600 positions.

The Dominican Republic has no major foreign investments, despite being the largest economy in the Caribbean. There are no official data on FDI outflows, but the few known foreign investments by companies from the country are in Haiti. Grupo M, for example, has garment manufacturing plants employing 9,000 workers, while Grupo Estrella has several construction projects in Haiti.

1. Investments beyond the Caribbean

Economic growth in the Caribbean has been modest at best in recent years, as the subregion continues to recover from the 2008 drop in asset prices and resulting recession. Jamaica, now undergoing a fiscal restructuring in close cooperation with the IMF, has been having particularly severe problems. It is an important target market for many trans-Caribbeans, and its economic woes have negatively impacted businesses in the region. Massy, for example, reported a 24% drop in its Jamaica-based business in 2013 due to both falling consumer demand and currency depreciation (see box II.3).

These economic factors, along with a drive to explore new and larger markets, have helped push Caribbean companies to invest outside the region, particularly in Latin America. Goddard Enterprises is an example of a company with a significant amount of its business based outside the Caribbean. The conglomerate has substantial catering and ground handling operations in several Caribbean countries and in Latin America, including the Bolivarian Republic of Venezuela, Colombia, Ecuador, El Salvador, Guatemala, Honduras and Paraguay. Massy Group rebranding decisions have been influenced by a desire to broaden its activities in Latin America, as discussed in box II.3.

Of course, investing in Latin America has its own problems. The Bolivarian Republic of Venezuela is seemingly a natural target market for trans-Caribbean companies. It is geographically close and has developed strong ties to many countries through bilateral agreements, the PetroCaribe arrangement[24] and trade. However, the country has recently been in an economic slump (like the Caribbean region itself), which could make it less attractive for FDI from the Caribbean. Furthermore, the risk of currency devaluation combined with government currency controls can make it difficult for companies operating in the country to trade Venezuelan currency for United States dollars or another currency that serves for international trade or profit repatriation, and this has been reported as a problem by some Caribbean enterprises attempting to operate in the Bolivarian Republic of Venezuela (McLean and Khadan 2014; bkp Development Research & Consulting, 2014).

[24] The PetroCaribe Energy Cooperation Agreement is an arrangement between the Bolivarian Republic of Venezuela and a number of nations in the Caribbean and elsewhere whereby subsidized petroleum is supplied for cash or the equivalent in goods and services. There are questions about the future of the programme because of the fall in oil prices, which has had a large impact on the Venezuelan budget. All the economies discussed in this chapter except Barbados and Trinidad and Tobago are parties to the PetroCaribe arrangement.

Box II.3
The Massy rebrand

Massy Group, the largest Caribbean conglomerate, had its beginnings in 1923 with the founding of the Neal Engineering Company. In 1932, this merged with Massy to form Neal and Massy Engineering Company. The firm continued to grow into a conglomerate, eventually becoming Neal & Massy Group, with more than 60 companies operating in the region. Some of its most important acquisitions as it grew included Cannings & Company (of Trinidad and Tobago) in 1975 and Barbados Shipping & Trading Company in 2008.

International expansion and the diversification of industries under the group's umbrella led executives to believe a rebranding campaign was needed. In order to build brand image and recognition, in 2014 the different firms within the Neal & Massy Group were rebranded to Massy, and Neal & Massy Group itself changed its name to Massy Group. Massy Group is a conglomerate of various subsidiaries operating in the automotive, distribution, energy and industrial gases, finance, industrial equipment, insurance, property, retail and technology sectors. These encompass dozens of different businesses and brand names now relabelled as Massy. For example, Hi-Lo Food Stores is now Massy Stores, while Neal & Massy Automotive, Nealco Motor Mart, Neal & Massy Auto Rentals and Tobago Services have now been rebranded under the single name of Massy Motors.

Some of these names are iconic in Trinidad and Tobago and the Caribbean. During the rebranding process, many in the region have been learning for the first time how many brands and businesses are in fact part of Neal & Massy, now Massy. The choice of the conglomerate's new name, Massy, was made after consideration of thousands of candidate names. It was chosen because it was familiar —many people already referred to some Neal & Massy companies simply as "Massy". The heritage reflected in the original name is captured by the company's new symbol, which includes both an "N" and an "M".

In terms of strategy, the decision to bring all group businesses under the umbrella of a single name directly relates to the growth strategy of this pan-Caribbean conglomerate. It increases synergies between the different components of the business, while retaining the risk-spreading strengths of the diversification strategy. Elsewhere in the world, large companies tend to become more specialized with size, since they benefit more from dominating a single product than they do from winning a smaller share of more different markets. The situation in the Caribbean is different in that even complete dominance in a single product market still produces only a very small base for a company. Thus, spreading across different product markets increases potential market size while at the same time reducing risk.

The unification of the company's businesses extends beyond the use of a common name. Massy is also taking steps to increase cooperation and improve integration between its different components and to encourage subsidiaries to work together. For example, companies under the Massy umbrella sold automobiles (Neal & Massy Automotive), provided vehicle insurance (United Insurance) and provided finance for vehicle purchases (General Finance Corporation). Now all these companies have been rebranded under the Massy name and steps have been taken to ensure that they communicate and cooperate with each other. This could result in both increased revenues for Massy Group and more convenient shopping for customers.

The decision by Massy Group to brand all its products under the Massy name is also related to its intention to continue to focus on expanding into Latin American markets. In Spanish, "más sí" means "more yes" or perhaps "More? Yes!". This was a factor in management's decision to choose the name Massy as its branding focus.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

The third major destination for FDI by Caribbean companies, after other Caribbean countries and Latin America, is the United States. The United States is the world's largest FDI source and destination. Much FDI going from the Caribbean to the United States is designed to take advantage of Miami as a major goods and services distribution port. Because transport and travel between Caribbean countries remains underdeveloped, Miami is an important hub for intraregional trade. FDI in the United States can thus facilitate increased trade and investment with countries in the Caribbean. Some FDI is also for access to markets in services such as insurance.

Digicel Group is an excellent example of a company that has used its strength in the Caribbean to learn and develop a new business model that can be applied elsewhere as well.[25] The company now operates in most Caribbean markets and has aggressively pursued investments in markets outside the region, with operations in several countries of Central and South America. It was in discussions to develop telecommunications networks in Myanmar, but failed in its bid to obtain one of two licences offered by the government. Digicel's expertise in developing mobile phone networks in small island countries has allowed it to branch out and operate in some South Pacific island economies as well, including Fiji, Nauru, Papua New Guinea, Samoa, Tonga and Vanuatu. It has even used its reach to fill a financial-sector niche: Digicel mobile money allows users to send and receive money and pay bills through their phones.

2. The advantages and disadvantages of intraregional FDI

Outbound FDI is sometimes portrayed negatively by the media and other institutions, particularly when it goes to developed countries. It can be seen as the relocation of jobs and productive enterprises out of the home country, to the latter's detriment. Nonetheless, outbound FDI has several advantages for both employment and economic growth in the source country, and some of these advantages are particularly relevant to small island developing States.

[25] Digicel's operations are mostly in the Caribbean, with its headquarters in Jamaica; however, the founder is from the Republic of Ireland.

Investing in foreign countries can be a way for Caribbean companies to cope with the problem of small markets and the resulting low demand at home. Expansion can lead to economies of scale, and thence increased production and distribution. These economies of scale would be more difficult to achieve in a single Caribbean country or even the whole Caribbean region.

Caribbean economies are well known to be susceptible to both economic and environmental shocks. Geographical diversification can make them more sustainable at home. A company which restricts itself to a small domestic market with wide fluctuations in supply and demand is unlikely to survive. This is especially true in Caribbean economies, which have fairly open trade; domestic companies must compete with large, international ones, whether at home or abroad.

When a Caribbean company makes foreign investments, it opens up to a larger market than its domestic one. This can directly lead to an expansion of production and employment in the home country if the company uses inputs from there. Although trade is most commonly seen as a way for Caribbean nations to tap world markets through exports, FDI can achieve the same goal.

FDI within the region has, at least initially, zero net effect on the region's balance of payments as a whole, something that has both positive and negative aspects. With intraregional FDI, there is no initial transfer of capital to the region (although of course there is between countries within the region). Similarly, profits, even if repatriated, stay within the Caribbean; for the region as a whole, this prevents a continued drain on the current account from profit repatriation. Of course, that does not preclude a disparate share-out of FDI returns, depending on the capacity of individual countries to invest competitively in others.

Caribbean transnational companies may be more committed and better positioned to contribute to community development in the Caribbean than other sources of FDI. Goddard, for example, highlights its contributions to the Caribbean in its annual report; these include a donation in pursuit of UNESCO World Heritage Site status for several areas in Saint Vincent and the Grenadines and support for athletic activities in a number of Caribbean countries. Sagicor has also funded community development projects throughout the Caribbean, focusing on education, health, community and youth involvement and sports. ANSA McAL funds awards to recognize Caribbean achievements in key fields and maintains a foundation which champions various social causes in the Caribbean. Massy Group sponsors activities to promote innovation, youth development, education, women's empowerment, physical fitness and other goals. Caribbean Airlines is involved in a number of community and charitable activities including, for example, backing for a paediatric cancer patient support organization. This is not to say that foreign firms cannot contribute to social development in the Caribbean as well; BP, for example, contributes to several projects in Trinidad and Tobago.

Caribbean transnationals, as large companies which must compete internationally, can also be important for the development of human capital in the region. They are probably more likely to train and hire local staff as managers than investor companies from outside the region. Nonetheless, their ability to hire locals for some positions is limited by human capital constraints. For example, there are few formal insurance education programmes in the Caribbean, so actuarial experts must often be hired from outside the region.

The choice of where to invest in the Caribbean may be strongly influenced by bureaucratic obstacles and the time required to set up a new business. The region is subject to various economic and environmental risks, which investors must also take into account. Furthermore, most of the markets are small, so industries with high entry or fixed costs may struggle to attain profitability.

F. Conclusions

There is no doubt that FDI is playing a major role in the economic development of the Caribbean. FDI inflows are very large compared with the size of local economies, many of which suffer from large current account deficits that governments are trying to compensate for with inflows of FDI. In tourism particularly, the role of FDI cannot be overstated, since many projects require such substantial investments that local investors would not be able to defray them. A similar argument can be made in the natural resources sector, although joint ventures between local and international enterprises are more common in that field. Cuba and Haiti are the two exceptions in the Caribbean, receiving very little FDI for the size of their economies.

Since 2008, FDI inflows into the Caribbean have decreased by 37% to US$ 6.027 billion. The experience of the region's different economies has varied greatly, however. The likes of the Dominican Republic, Jamaica and Trinidad and Tobago receive substantially larger amounts of FDI than smaller economies, which reflects their economic size. Over time, Guyana and Haiti have seen significant increases in FDI inflows, while the Bahamas and Barbados have experienced the largest falls.

With respect to the balance of payments, the impact of FDI is ambiguous. While it is true that economies with temporary current account deficits may be able to offset them with a capital account surplus, many economies in the Caribbean have permanent current account deficits, and the continuous inflow of FDI that would be required to offset them would lead to a large build-up of foreign capital. Furthermore, such inflows are then associated with outflows of capital in the form of income from FDI. On average, outflows of income from FDI are equivalent to more than three quarters of FDI inflows in the Caribbean, and they are particularly substantial in Barbados, Suriname and Trinidad and Tobago.

The degree to which FDI crowds out local investment also affects its impact on the balance of payments. A local investment will not give rise to an influx of capital at the time the initial expenditure is carried out and does not lead to significant outward current transfers compared with a similar amount of FDI. Export receipts can rise whatever the source of the investment. Although local investment may seem more likely to have a beneficial long-term impact on the balance of payments than a similar amount of FDI, it is important to remember that FDI is often sought by countries because local firms do not have the resources to make the same types of greenfield investments that large multinational corporations do.

Besides the impact on the balance of payments, there is potential to positively affect economic growth in the different economies. Many Caribbean economies have long been suffering from a lack of competitiveness, and FDI could help to transform them. However, evidence for a transformative impact is limited. Empirically, it has not been shown that inflows of FDI lead to subsequent economic growth. There are exceptions: particularly in the case of investments too large to be borne by local economies, such as in mining, the absence of FDI would hamper economic development. In other cases, likewise, foreign investors may be able to invest larger sums within a shorter period, quickly providing employment opportunities. In certain economies, furthermore, inward FDI has the potential to yield significant benefits. This is particularly true of Cuba and Haiti, as developing countries that receive very little FDI. In these cases, inbound FDI has the potential to be truly transformative in terms of employment creation, technological spillovers and economic growth. However, both these economies are clear exceptions within the Caribbean context.

The impact of the extensive use of FDI promotion policies in the Caribbean is a subject of debate. The effectiveness of different policies of this type has not been sufficiently researched in the Caribbean context, making them difficult to justify at a time when many governments in the subregion are suffering from significant revenue shortfalls. Exacerbating the harmful impact of FDI promotion policies is the arbitrary way they are applied in many jurisdictions. At present, investment incentives are too often granted on the basis of individual negotiations between investors and policymakers. Unfortunately, this is not always a relationship between equals in the Caribbean, with investors having substantially more bargaining power.

The result of such unbalanced relationships and of the fact that many Caribbean economies offer very similar products has been a race to the bottom between the different governments, which match one another's incentive offers. Caribbean governments should thus be encouraged to cooperate more energetically on reducing the FDI promotion policies available to investors, particularly those that do not seem to directly affect the variables which governments wish to act upon, such as employment creation. Only if governments cooperate closely through forums like CARICOM and OECS can they stand up to the market power of some of the larger corporate players in the region. If they achieve this, they will be in a position to use their resources more productively. In particular, rather than having blanket fiscal subsidies, they could target specific sectors with reforms that can increase the local benefits of FDI. With respect to tourism, for example, this means encouraging local companies to produce a consistent supply of high-quality inputs for the sector.

An underlying challenge is that FDI promotion policies would not be so necessary in the Caribbean if it were able to improve its business environment. Investors are looking to optimize their overall business, and it is not uncommon for them to say that higher taxes would not be a problem if the business environment were better. More effective government, less bureaucracy, better public services, a faster judicial system, better contract enforcement: all these would make it easier to do business, benefiting domestic and foreign investors alike. If such improvements were to take place in the region, the call for further FDI promotion policies would not be as strong and would anyway be easier for policymakers to ignore.

FDI inflows into the Caribbean are likely to increase moderately in the near future, once economies are able to return to growth. Since the region's overall FDI figures are primarily driven by large investments in the natural resource sector, the future of the headline FDI figure largely depends on what happens to commodity prices in the international market. Much also hangs on the degree to which Cuba and Haiti are able to start attracting significant investment. These two economies are large by Caribbean standards and their entry into the FDI arena could have a large impact. For individual economies, it is important to remember that what truly matters is not the quantity of FDI but its transformative impact.

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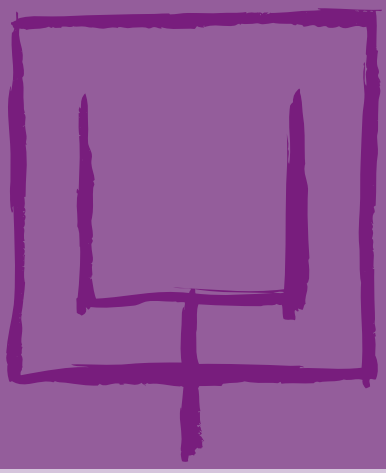
Chapter III



Transnational corporations and the environment

Introduction

At the United Nations Conference on Sustainable Development (Rio+20), the participating countries agreed on the need to move towards a new form of consumption and production that does not endanger the environmental balance of the planet. In this regard the success of efforts to reduce poverty and inequality, and to promote development, will be contingent on ecological constraints and environmental degradation.

In Latin America and the Caribbean, environmental problems are complex and encompass several dimensions (ECLAC, 2012). The region is highly urbanized, with more than 80% of people living in cities. While this is beneficial to the quality of life of much of the population, it has also created significant social and environmental problems, such as inadequate basic services and air and water pollution in many urban areas. Despite considerable progress, solid waste management remains a critical issue in many neighbourhoods owing to the poor management of economic incentives, low collection coverage and a shortage of sites for final disposal.

Latin America and the Caribbean is also home to the planet's greatest biodiversity, but this wealth is at risk of being lost. The world failed to meet the 2010 Biodiversity Target adopted by the Convention on Biological Diversity, mainly owing to land-use changes and the consequent reduction, fragmentation and loss of habitats. Large-scale export agriculture, tourism and unplanned coastal development all have a major impact on this process. Deforestation is another key issue for in the region, which accounts for one third of global forest losses. Having accelerated in South America between 1990 and 2005, the phenomenon has since slowed thanks to a number of steps taken in the Brazilian Amazon. The degradation of desert and arid land is also causing biodiversity loss and is detrimental to the economic productivity of agriculture and related activities.

The region has plentiful water resources, but they are unevenly distributed and their quality may be degraded by urban growth and the expansion of certain economic sectors. Chemical production is partly responsible for this degradation, since neither the industry nor consumers are willing to pay for the proper disposal of chemicals. Although some institutional progress has been achieved in this sphere, and most countries have adopted strategies for the management of these products, some implementation problems remain.

The region is also experiencing the same climate change impacts as the rest of the planet, with the Caribbean and other coastal territories particularly affected. In fact, addressing climate change is one of the priorities of the Programme of Action for the Sustainable Development of Small Island Developing States. The region's per capita greenhouse gas emissions are slightly higher than the world average, and are largely accounted for by the energy sector (42%), agriculture (28%) and changes in land use (21%) (ECLAC, 2014b).

The post-2015 development agenda is structured around sustainable development goals (SDGs) which mainstream the concept of environmental sustainability. The agenda also emphasizes that all actors, including the private sector, need to be included in efforts to achieve the SDGs. In Latin America and the Caribbean, transnational corporations are a key actor: on some occasions they have been almost entirely responsible for the development of sectors with major environmental impacts, while also making a decisive contribution to the introduction of unsustainable consumption patterns (for example, private vehicle use), which will be difficult to reverse in the near term. However, many transnational firms have the capacity to help introduce more sustainable practices, thanks to their experience in countries with stricter environmental regulations, more advanced technology, or greater exposure to civil society and international financial markets.

This chapter explores how business strategies can help or hinder the transition towards a more environmentally friendly production structure, with a particular focus on foreign direct investment (FDI). Increased social and political demand for environmental protection has recently led to change in the relationship between FDI and the environment. Technological advances have also expanded the range of solutions to many environmental problems, with transnational corporations the main proprietors of these technologies. Lastly, FDI inflows into Latin American and Caribbean economies have increased over the past decade, and in some countries have been channelled more intensively into the natural resources sector, which has a potentially high environmental footprint.

Measuring the environmental impact of FDI is beyond the scope of this chapter, although the influence of production structures on these impacts, and the conditions needed to make best use of positive contributions by transnational

corporations, are examined. The chapter also reviews the environmental impact of transnational corporations from a broad vantage point, as well as how public policies are channelling this impact. Consideration will be given to past actions (pollution and environmental liabilities, among others) and future prospects (how FDI can make the region's production structure more sustainable). Government policies are also analysed, with special reference to the convergence or divergence of environmental and investment policies. Several boxes included in the chapter give a detailed account of recent environmental developments and corporate performance in specific sectors.

A. Production structure, corporate strategies and the environment

As chapter I explained, despite weaker FDI flows in 2014, transnational corporations have been increasing their presence in most of the region's countries for the past decade: it is only natural that their environmental footprint should increase too. However, the magnitude of that impact, whether positive or negative, will not be directly proportional to the amount of investment received, but will depend on the production structure and regulatory framework of the country in question, and on business strategies relating to the location of investment, the development of clean technology or the adoption of other environmental measures.

Environmental impacts differ greatly according to economic sector. Accordingly, transnational corporations are likely to have a limited impact in countries where FDI is concentrated in services or light manufacturing, and a significant direct impact in countries that attract FDI to heavy industries or the development of natural resources.

Transnational corporations have the capacity to situate polluting operations in countries with laxer environmental regulations. In the same way as some transnational firms are accused of locating their activities in certain countries so as to minimize their tax burden or labour costs, so they stand accused of attempting to minimize their environmental protection costs by transferring their dirtiest operations to countries with more permissive environmental regimes (see section 2).

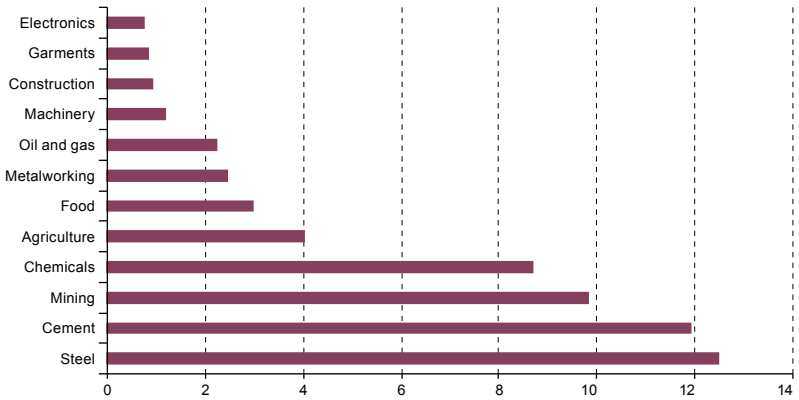
Transnationals can also use their greater technological expertise to promote environmental sustainability by introducing cleaner modes of production and helping to build local capacity in that sphere. They can also make a positive contribution by showing greater willingness to undertake voluntary initiatives in favour of sustainability.

1. Sectoral distribution and the environmental impact of FDI

It is estimated that 42% of all inward FDI in Latin America and the Caribbean goes to the services sector, while manufacturing receives 32% and natural resources the remaining 26%. However, countries differ significantly owing to their varied comparative advantages and production patterns. Since these activities affect the environment in different ways, the ecological consequences of FDI are primarily contingent on the production structure of each country.

There are many dimensions to the environmental impacts of different economic activities, and therefore it isn't possible to quantify them using a single variable. Golub, Kauffmann and Yeres (2011) define the following environmentally relevant sectors: agriculture, extractive industries, manufacturing, construction, transport, and electricity, gas and water services. This extremely broad definition only excludes services whose ecological impacts are mainly indirect, such as retail and banking. By focusing on a single variable, it is possible to gain a more specific measurement of impacts on certain sectors. For example, the sectors with the largest impact in terms of energy intensity (as an approximation of their potential contribution to greenhouse gas emissions) were paper manufacturing, steelmaking, cement production and mining. Figure III.1 shows energy intensity by sector in the United States in 2011.

Figure III.1
United States: energy intensity in selected sectors, 2011
(Thousands of British thermal units (BTUs) per dollar of output)

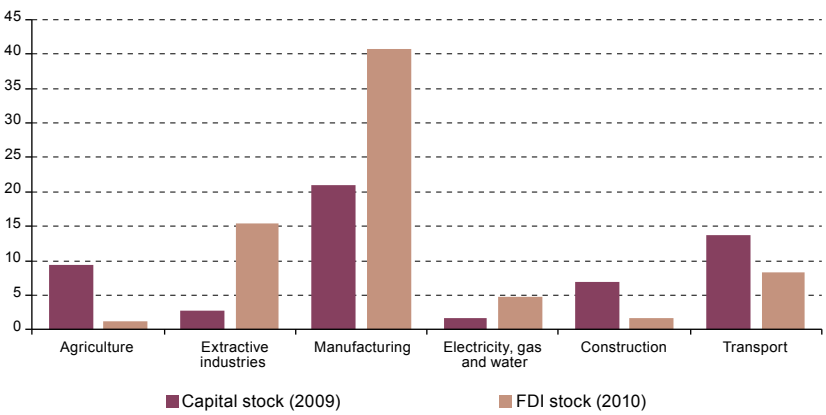


Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of the United States Department of Energy, "Energy Intensity Indicators", 2015 [online] http://www1.eere.energy.gov/analysis/eii_index.html.

Environmental degradation —often caused by mining or heavily polluting industries— is not necessarily a consequence of FDI, and would still exist if these activities were performed by local firms. Moreover, in many economies (particularly small and medium-sized ones) transnational companies are the only enterprises with the capacity needed to develop certain industries, with the result that there is no way of distinguishing the environmental impact of the sector from that of FDI.

The sectoral concentration of FDI in a given production structure may be observed by comparing each sector's share of the cumulative stock of FDI with its share of total capital. In general, transnational corporations will tend to dominate sectors that have large economies of scale, are capital intensive, or which allow them to exploit their technological advantages, brands or patents. Figure III.2 shows this comparison for Brazil, the only country in the region for which there is an estimate of capital stock broken down by sector. Taking into account only the most polluting sectors, and compared with total investment, FDI was more highly concentrated in extractive industries, electricity, gas and water, and manufacturing, and less so in construction and agriculture.

Figure III.2
Brazil: FDI stock and total capital stock in environmentally sensitive sectors, 2012
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and Marcel P. Timmer (ed.), "The World Input-Output Database (WIOD): contents, sources and methods", *WIOD Working Paper*, No. 10, 2012 [online] http://www.wiod.org/publications/papers/wiod10.pdf.

The observations presented in figure III.2 cannot be extrapolated to all of the region's countries, though some trends are indeed comparable. Local investors predominate in agriculture, construction and transport in almost all countries. Conversely, the relative importance of FDI in extractive industries varies greatly, being larger in Argentina,

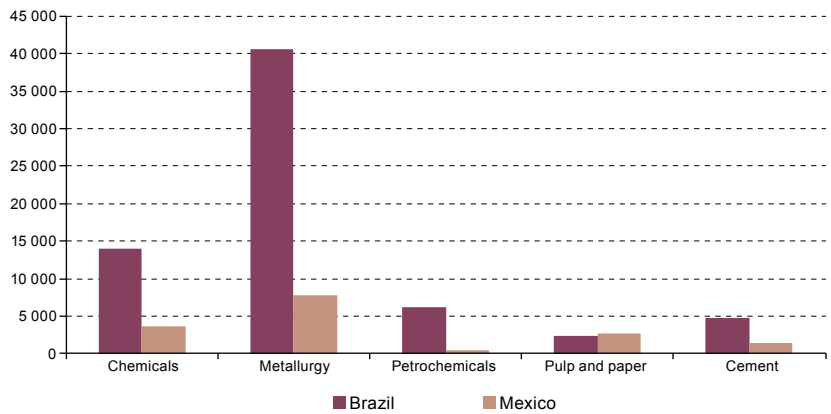
Chile, Peru and Trinidad and Tobago than in Brazil and Mexico. The relative magnitude of FDI in the electricity and manufacturing sectors is also highly variable.

It is estimated that these six sectors account for 41% of FDI worldwide, 46% of FDI in developing economies (Golub, Kauffmann and Yeres, 2011) and 62% of FDI in Latin America and the Caribbean. In other words, the sectoral distribution of FDI in the region means that the potential impact on the environment is high (in comparison with the world average).

Different manufacturing industries have diverse environmental impacts. One way of measuring them is to study the pollution abatement costs incurred by corporations (per unit of output, in the United States economy) (Mani and Wheeler, 1997). According to 2005 data, six industrial sectors were identified as producing the most pollution: iron and steel, pulp and paper, industrial chemicals, leather, petrochemicals and non-metallic minerals (cement) (EPA, 2008). Almost all are fairly intensive in capital, energy and land, and have high fixed costs. By contrast, the manufacturing of textiles, garments, machinery, transport materials and professional and scientific instruments are subsectors that are deemed to have low environmental impacts.

By this criterion, the region's two largest economies exhibit very different patterns. In Brazil, natural-resource processing industries have developed most, while in Mexico labour-intensive and medium-high-tech industries such as machinery, automobiles and electronics have dominated. For this reason, FDI flows to the most polluting industries are much stronger in Brazil, although total FDI in the manufacturing sector (US$ 17 billion per year in the past decade) is comparable to that received by Mexico (US$ 12 billion per year). In Mexico, the polluting industries accounted for just 15% of FDI, compared with 49% in Brazil. Much of the difference is due to the enormous investment inflows in the Brazilian steel industry in recent years (see figure III.3), though Brazil receives much more FDI than Mexico, both in absolute and relative terms, in almost all of the most polluting sectors.

Figure III.3
Brazil and Mexico: cumulative FDI in polluting manufacturing industries, 2007-2013
(Percentage of total FDI in manufacturing)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

Disaggregated data are not available for Central America and the Caribbean, but the absence of steelmaking and other heavy industries and the specialization in labour-intensive export manufacturing suggests that the environmental impact of industrial FDI in those countries is equal to or less than that of industrial FDI in Mexico.

These comparisons between countries are based on overall environmental impact patterns and might not reflect the impact of individual investment projects in these countries. Even within the same industry, processes may have different (positive or negative) environmental impacts depending on national regulations, natural or social circumstances at the location, and individual corporate decisions. One example is that of CO_2 emissions per unit of electricity generated: in power systems that mainly rely on fossil fuels (for example, those of northern Chile or Mexico), electricity-intensive industries will generate many more indirect emissions than they would in countries where electricity is mainly generated from renewable energies (such as Brazil or Colombia).

Classifying environmental impacts in the services sector, which accounts for half of the region's FDI, is more difficult since effects tend to be more indirect. A good example is the retail trade, a service sector whose FDI inflows are among the strongest in the region.[1] While its operations are not especially dirty, this sector can exert significant influence over the value chain of many other products. In 2009, the Brazilian subsidiary of United States retailer Walmart signed a sustainability pact with other companies, designed to achieve specific internal targets such as increasing the energy efficiency of stores by 25% and reducing the use of plastic bags by 50% (a target that was reached in 2012). Other goals involved the requirement that wood, livestock and soybean suppliers hold certificates guaranteeing that their production processes do not contribute to the deforestation of the Amazon.

The financial services sector also has significant potential to influence the rest of the economy. For example, the "Equator Principles"[2] were designed by international public banks to be applied in major infrastructure projects, but commercial banks have increasingly applied them to all large and medium-sized loans. The 80 banks that adhere to these principles include the main foreign banks operating in the region (Citigroup, Santander, BBVA) and many of the region's major financial institutions, notably those of Brazil (Itaú, Caixa Econômica Federal, Bradesco, Banco do Brasil and Pine). In that country, a new regulation requires that banks assume responsibility for environmental impact studies in the projects they finance, thereby adopting the practice of the principal international banks.

For many of the region's economies, mining and oil companies are likely to have the greatest environmental impacts. Worldwide, the percentage of FDI allocated to natural resources stands at less than 10%, while in Latin America and the Caribbean it is 26% (Golub, Kauffmann and Yeres, 2011) and in countries such as Chile, the Plurinational State of Bolivia and Trinidad and Tobago, the figure exceeds 50%. This trend has intensified with the reprimarization process of the past decade, which in many cases has been spurred by high levels of FDI in extractive industries, especially mining (see the section in chapter I on sectoral distribution).

Extractive industries are voracious energy consumers and are therefore responsible for considerable indirect greenhouse gas emissions. In the north of Chile, mining firms have increased their power consumption by 33% in the past eight years, drawing electricity from a grid that is 83% coal-powered.[3] At the same time, these companies have increased their direct greenhouse gas emissions from 3 million to over 5 million tons of CO_2 equivalent in the past 10 years, largely owing to the increased use of trucks in open-pit mining. These growing environmental impacts reflect the more intensive use of energy because of declining ore grade in working deposits. Many of these corporations (both domestic and foreign) are striving to improve their energy efficiency and increase the use of renewable energies in their operations; however, this has not yet managed to reverse the underlying trend.

Environmental liabilities caused by extractive industries pose a more local, but no less important problem. The management of these liabilities is at the heart of many of the disputes concerning heavy industrial operations by transnational corporations in the region. Particularly problems have arisen in operations that changed hands without a sufficiently clear attribution of this responsibility to one of the parties, as in the dispute between Ecuador and Chevron. More recently, Barrick Gold faced similar problems following a case of water pollution at its mine in the Dominican Republic.

In short, mining, hydrocarbons and other primary sectors such as forestry have a considerable environmental impact at the global and local levels (see box III.1), and in many countries these activities have taken place thanks to foreign investment. For as long as the extractive industries dominate the Latin American and Caribbean production structure, foreign (and domestic) investment will continue to have a significant bearing on the environment.

1 During the past decade, the services sector's annual FDI inflows exceeded US$ 1.0 billion in Mexico and US$ 3.0 billion in Brazil.
2 The Equator Principles are an environmental and social risk management framework for developing countries, adopted by financial institutions, which provides a minimum standard for due diligence to support responsible risk decision-making.
3 See Mining Council [online] http://www.consejominero.cl/ambitos-estrategicos/energia-y-cambio-climatico/.

Box III.1

Mining in the spotlight: governments and civil society demand better environmental performance from mining corporations

Mining is one of the sectors that attracts most FDI to Latin America, but it also generates one of the largest environmental impacts. In fact, environmental impact management is often a decisive factor when undertaking investment projects, beginning with the initial operating permit that is granted after the environmental impact assessment and continuing throughout the useful life of the mine. In recent years there has been a proliferation of cases in which mining operations have been suspended and even cancelled because of protests by the directly affected communities or by national civil society. The most common causes of contention are environmental (pollution, water use and the accrual of environmental liabilities), but complaints have also been made of human rights abuses, the displacement of communities, unfulfilled expectations of shared mining royalties and negative impacts on traditional production activities (Saade Hazin, 2013).

Such conflicts —which vary somewhat from one country to the next— abound all over the world, although Latin America accounts for a disproportionate number even taking into account the magnitude of the sector in some of the region's countries.

In Chile, most conflicts have been confined to legal action. The largest —in terms of investment— was the Pascua Lama case, in which Canada's Barrick Gold Corporation called a halt to its mining operation on the Argentine-Chilean border in April 2013 after a court ruled that the company was responsible for reducing indigenous communities' access to water. The setback proved so serious for the company that it was forced to take an asset write-down of US$ 5 billion, although Barrick Gold is confident that it will be able to resume the project in future.

In Peru, communities and groups opposed to mining projects have more commonly opted for direct action, which in one case in 2013 paralysed the Yanacocha mine, under the majority ownership of Newmont of the United States, for several months and caused Peruvian gold exports to fall by 25%. In Colombia, the Government halted coal exports by the Drummond Corporation, again from the United States, for reasons of marine pollution, and protests by residents have delayed several major projects such as those run by AngloGold Ashanti in Tolima department and Eco Oro in Santander department (*The Economist*, 2014). In the Dominican Republic, another legal claim has been filed against Barrick Gold for use of public spaces in its Pueblo Viejo project.

One of the reasons for the increased number of conflicts is that mining investment in the region has boomed in the past decade. As well as expanding their presence in traditional mining countries, corporations are seeking new opportunities elsewhere, leading to social conflicts with the potential to derail major projects. In Uruguay, the Zamin mining company plans to invest more than US$ 1.0 billion to develop the Aratirí iron ore mine, but the determined opposition to the project from society could make it difficult to implement. In Panama, in 2012 the Government cancelled mining concessions in the territory of the Ngöbe-Buglé ethnic group after a number of protests, although the Cobre Panamá project in the province of Colón remains on track. In Costa Rica, environmental concerns have led to a near-total ban on large-scale mining.

Quite apart from the surge in mining investment, the number of complaints has risen because the affected communities are increasingly well informed and have more and more avenues open to them to make their voices heard. Moreover, Governments are taking steps to improve access to information and justice and to increase participation in environmental issues by undertaking institutional reforms such as Chile's General Environmental Framework Law of 2010 (ECLAC, 2014d). At the regional level, ECLAC is leading the process for the application of Principle 10 of the Rio Declaration, which recognizes the right to public participation in environmental issues, and which already counts 19 of the region's countries as signatories (see [online] http://www.cepal.org/rio20/principio10). Provisions on rights of access to information may also be included in international agreements such as the bilateral investment treaty signed between Uruguay and the United States.

Another legal instrument that has facilitated citizen participation is International Labour Organization (ILO) Convention No. 169 concerning indigenous and tribal peoples, which stipulates that consultations with indigenous communities must be held before mining projects affecting them can be carried out. Fifteen countries in the region have so far signed up to the Convention, which has been instrumental in at least one important case, when in 2013 a Chilean court suspended work at the El Morro gold mine, owned by Canada's Goldcorp and for which investments to the tune of US$ 3.9 billion had been planned, on the grounds that the consultation process did not comply with the Convention.

Mining companies will be forced to adapt to civil society empowerment and growing environmental awareness, which are structural trends that will not change in the short or medium term. Change is, however, taking place in the economic climate in which projects are implemented. Over the past decade, FDI in mining has returned extraordinarily high profits, which in Chile stood at 25% per year between 2007 and 2011 (see ECLAC, 2013, chapter II). It is possible that the perception that mining companies have reaped a windfall has fuelled the demands of civil society, though it is also true that the strong profitability of mining projects has allowed corporations to make real efforts to accommodate these demands, despite the additional cost involved.

In the current context of falling mineral prices and declining investment (see chapter I), corporations might adopt another strategy to cope with the rising number of environmental complaints, and ecological concerns —and alternative livelihoods to mining— may come into conflict with the need to save jobs in the sector. Governments should mediate in these conflicts, with the ultimate goal of promoting responsible mining investments and penalizing those which do not respond to expectations of sustainable development in the region.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

2. Foreign direct investment and the relocation of polluting activities

Transnational corporations may have different strategies to national ones, since they have the ability to transfer production processes between countries, with one possible reason being the avoidance of costly environmental regulations. This is known as the pollution haven hypothesis, and could be significant since almost half of FDI in the aforementioned dirty industries flows from developed to developing countries. While environmental controls and restrictions in developing countries will presumably converge with the standards of developed countries, the asymmetry in environmental regulations will remain significant in the near term.

Proving or disproving this hypothesis is a complex task, given the multitude of factors that determine the location of investments. While most studies, including those by Rezza (2014), Sanna-Randaccio and Sestini (2011), Smarzynska and Wei (2001), and Mani and Wheeler (1997), have found no evidence for the phenomenon, Wagner and Timmins (2009) found evidence to support the hypothesis in the case of the German chemicals industry, as did Dean, Lovely and Wang (2009) in relation to investments in China by companies based in the Hong Kong and Macao Special Administrative Regions and Taiwan Province of China.

The gulf between the environmental regulations found in different countries, as well as in their application and in conflict resolution mechanisms, does not explain the location of pollution-intensive activities (or only does so partially). There are several reasons for this, the first of which is that the costs incurred by corporations in controlling environmental damage are relatively modest. According to the Pollution Abatement Costs and Expenditures Survey, for manufacturing as a whole, current environmental costs in 2005[4] amounted to less than 0.5% of sales, while investments in treating or preventing pollution accounted for 4.6% of total investment (EPA, 2008).

In the case of energy-intensive industries, offshoring may be indirectly motivated by environmental policies. Such industries include that of aluminium production in the European Union, in which climate change mitigation regulations increased production costs by 8% between 2002 and 2012 (Oliver, 2014). Since 2007, almost half of European plants have closed and aluminium producers may have some incentive to relocate smelters to countries with lower energy costs. This production shift may reflect intrinsic competitive advantages in energy production and help reduce global CO_2 emissions if the plants relocate to countries with a range of renewable energies available (especially hydropower, as in many Latin American countries). However, the relocation could also reflect disparities in countries' climate-change-mitigation regulations, and could cause increased emissions if production were transferred to locations more reliant on dirtier energy sources.

Corporations wishing to take advantage of more permissive environmental regulations should consider that the existence of different production systems within the same enterprise entails extra coordination costs. While it is difficult to generalize, transnational firms tend to homogenize modes of production among their subsidiaries in order to gain flexibility and economies of scale. This would require that the most exacting environmental standards be applied in all countries (UNCTAD, 2010b).

Another important factor is that pollution-intensive industries such as steel, petrochemical and cement production also happen to be the least mobile, since they have high fixed costs and investments are recovered over long periods (Ederington, Levinson and Minier, 2005). The cost of transporting cement is so high compared with the value of the product that its international trade is negligible. The industry therefore responds exclusively to domestic demand patterns, with no space for expanding or reducing capacity according to environmental regulations.

Among these polluting industries, a trend has been observed whereby production is displaced from developed to developing regions, mainly Asia but also Latin America. Relocating production in this way, which could also indicate a preference for avoiding the strictest environmental regulations, should primarily be understood as a response to demand, which is stagnant or weakening in developed countries and strengthening in emerging economies (see box III.2).[5] In fact, the prospect of burgeoning demand has led to major investment in Latin America's heavy industries, which in turn will determine the intensity of emissions and other pollutants from these industries in the coming decades. For example, the fastest growth in the region's steel production capacity has been recorded at Brazil's integrated plants, which emit six times more CO_2 than semi-integrated plants. Projects such as the steel mill Companhia Siderúrgica do Atlântico opened in 2010 by ThyssenKrupp with a production capacity of 5 million tons per year, have contributed to inertia in the emissions intensity of the steel industry.

[4] Includes the operating and maintenance costs of equipment for the mitigation of air and water pollution, as well as solid waste management payments to the public and private sectors.

[5] This trend is examined in detail in chapter III of ECLAC (2010), on the steel industry.

Box III.2

Heavy industry and emission reduction strategies

Industrial CO_2 emissions, which account for 19% of the total, are highly concentrated in a handful of sectors, led by steel (30%) and cement (26%), followed by chemicals and petrochemicals (17%), pulp and paper (2%) and aluminium (2%) (IEA, 2014). Despite continual improvements to reduce its carbon intensity, heavy industry is expected to be a major emitter in future, and emissions will be a decisive factor in business strategies.

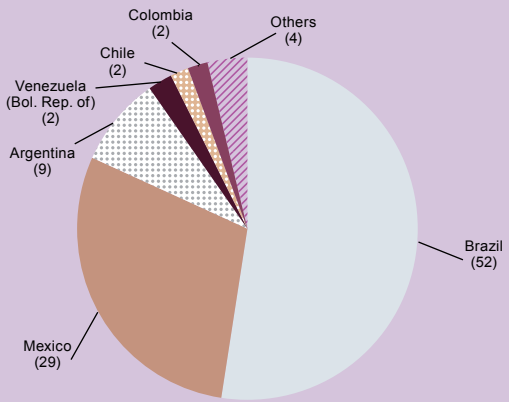
The steel and cement industries are highly transnationalized. Many European and some Asian companies operate in the region, notably the steelmakers ArcelorMittal, ThyssenKrupp, Vallourec, Nippon Steel and Posco, and the cement manufacturers Lafarge and Holcim. Trans-Latin corporations, some with genuine global presence, also operate in these sectors and include the steelmakers Techint (Argentina), Gerdau and CSN (Brazil), and the cement producers Cemex (Mexico), Argos (Colombia) and Votorantim (Brazil).

While Brazil and Mexico account for 79% of the region's total steel production, nearly all countries produce cement and little international trade is carried out this subsector. Foreign direct investment figures show that steel production capacity is concentrated in Brazil, which has received the lion's share of FDI in the industry in recent years (see figures 1A and 1B).

Figure 1A

Latin America and the Caribbean: distribution of steel production, 2014

(Percentages)

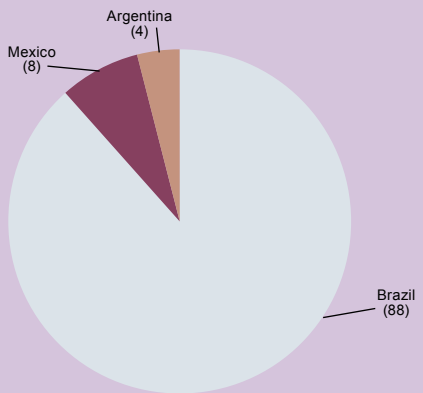


Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information from the World Steel Association (WSA).

Figure 1B

Latin America and the Caribbean: cumulative FDI inflows in the steel sector, 2005-2013

(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

Demand for cement in the region increased by 6% and 5% in 2011 and 2012 respectively (the most recent years with data available), while demand from Europe fell; steel consumption followed a similar trend. For that reason, European steel firms (ArcelorMittal, ThyssenKrupp and Vallourec) and cement makers (Lafarge and Holcim) have stepped up their investment in the region. Companies certainly face different environmental regulations in Europe and Latin America, especially in terms of emission reduction commitments, but the clear displacement of demand to emerging economies makes it difficult to determine whether environmental regulations are responsible for the transfer of production capacity.

Although the corporations operating in Latin America and the Caribbean are not yet subject to any formal emission reduction obligations, they should now be preparing for future controls. As in other industries, iron and steel companies have

Box III.2 (concluded)

argued for a sectoral agreement that gives them a measure of control over how they reduce emissions and which guarantees similar competitive conditions for all companies (WSA, 2014). They have also urged governments to adopt a life-cycle approach when considering CO_2 emissions, rather than focusing only on the industry that manufactures the product: this would allow the extra CO_2 emitted in producing lighter steels to be offset against the reduced emissions from vehicles made from such steels, which would consume less fuel. Through this strategy, the industry aims to guarantee its growth towards higher value-added products, even in a context of significant emission restrictions. The European cement industry has also published a road map proposing a 32% reduction in its CO_2 footprint compared with 1990 levels, using conventional technology. With the application of more radical methods, such as carbon capture and storage, this reduction could be as high as 80%.[a]

The scale of the emission reductions that Latin American steel and cement firms will be required to make, and their time frame for doing so, remain to be decided. Nevertheless, there is little doubt that their future will be determined by their ability to adapt to a less carbon-intensive world. Aside from upgrades to existing plants, which could reduce global emissions by an estimated 9% to 18% (IEA, 2007) there will be a trend towards investment in plants that use less carbon-emitting processes.

Accordingly, a long-term shift in production capacity is expected away from high carbon-emitting coke blast furnaces towards gas-based direct reduction modules (whose emissions are lower), and semi-integrated plants (whose emissions are much lower). This will be no easy transformation and the process will be slow and incomplete, even if it were accompanied by strong incentives, such as taxes on CO_2 emissions, carbon intensity-based barriers to trade in steel or direct subsidies on investment in new plants. This adaptation will also depend on each country's relative abundance of coal, natural gas or electricity, as well as iron ore and scrap. In Latin America there is a relative abundance of iron ore and a lack of scrap (with the exception of Mexico, which imports it from the United States), hampering the expansion of semi-integrated plants.

Efforts to reduce steel-industry emissions in Latin America and the Caribbean have been much more limited than those proposed in Europe, for example. In Brazil, the Sectoral Plan for the Reduction of Steel Industry Emissions focused on the sustainable use of charcoal.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
[a] See European Cement Association [online] http://www.cembureau.be/post-2020-climate-and-energy-legislation-proposal-european-cement-industry.

3. Transnational corporations, green technology and clean modes of production

One area where FDI can benefit the environment is through the transfer of clean technologies. Shifting Latin America's production patterns towards sustainable alternatives, as well as replacing certain industries and products, will require the development and dissemination of new technologies. Transnational corporations are key actors in creating and distributing this technology, and their investment strategies will determine the pace of adoption by the region's economies.

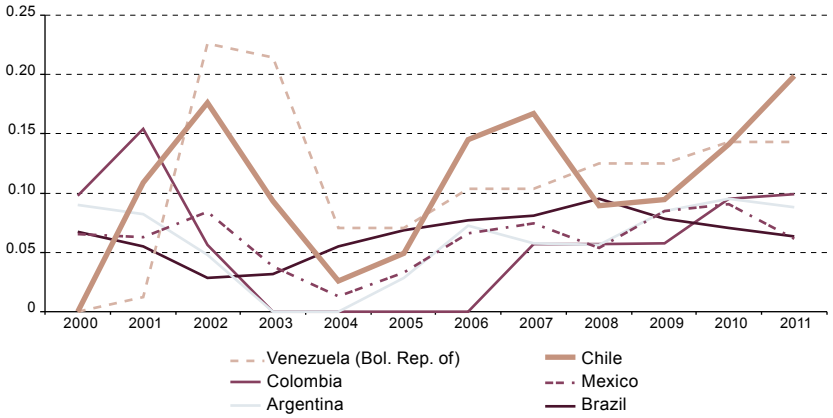
There is no precise definition of a green technology, since different activities require different technological solutions. Existing indicators are limited to measuring progress in the areas of energy and pollution mitigation and control (OECD, 2014) and, although useful for illustrating trends, they exclude innovations in other sectors, especially those with cross-cutting applications such as information and communications technologies and the development of new materials, which can be hugely effective in reducing the environmental footprint of economic activities.

Regardless of how they are measured, most of these technologies are still being created in developed economies and despite some progress by developing countries, they still lag behind (Krishna, 2009). Between 1978 and 2005, a very small number of countries (Germany, Japan and the United States) accounted for most patents in climate change mitigation technologies (Dechezleprêtre and others, 2011).

Latin America and the Caribbean has limited capacity for creating these technologies. According to the Organization for Economic Co-operation and Development (OECD), between 1999 and 2011 the region's six largest economies (Argentina, the Bolivarian Republic of Venezuela, Brazil, Chile, Colombia and Mexico) filed fewer than 300 patents for green technologies, out of a total of 4,300. Figure III.4 shows the percentage of green patents registered in each country. While this percentage is increasing slightly, reflecting the growing importance of the environment as a focus of research efforts, both the percentage and the total number of green patents remain at very low levels.[6]

[6] Brazil registered 2,503 patents, of which 170 were considered green technologies. Colombia registered 112 (6.5 of which were green), Argentina 575 (33.5 green), the Bolivarian Republic of Venezuela 70.5 (4 green), Mexico 780 (47.5 green) and Chile 299 (37 green).

Figure III.4
Latin America (6 countries): patents in green technologies, 2000-2011[a]
(Percentage of total patents in each country)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of data from the Organization for Economic Co-operation and Development (OECD).
[a] Data refer to averages of two consecutive years, in order to smooth out shocks.

With technical capacity thus divided, it is no surprise that international technology flows tend to run in a North-South direction. Some 22% of recorded transfers of climate-change mitigation technologies were from OECD countries to developing economies;[7] for technology transfers in general the figure stood at 16% (see table III.1). South-South technology transfers accounted for no more than 1% of the total. The question remains: what role does FDI play in these North-South technology transfers?

Table III.1
World: distribution of exported technologies in general and climate-mitigation technologies, 2000 to 2005
(Percentages)

Origin	Destination	
	OECD	Non-OECD
Exports of all technologies		
OECD	77	16
Non-OECD	6	1
Exports of climate-mitigation technologies		
OECD	73	22
Non-OECD	4	1

Source: Antoine Dechezleprêtre and others, "Invention and transfer of climate change-mitigation technologies: a global analysis", *Review of Environmental Economics and Policy*, vol. 5, No. 1, 2011.

It may be supposed that transnational corporations generally have a superior level of green technology to local firms, if only because of their size and the sectors in which they operate. Several studies have confirmed that in developing economies, foreign-owned companies are more energy efficient than their domestic counterparts (Peterson, 2008). Many transnational firms base their competitiveness strategy on the ownership of clean production technologies, especially in medium-high-tech manufacturing sectors such as component manufacturing (Siemens, Alstom).

Some of these companies may exploit their advantages through the manufacturing and export of components —such as the Danish firm Vestas, a worldwide exporter of wind turbines produced in Denmark— but many others are obliged to invest in their destination markets. For example, the power company Enel wishes to leverage its expertise in smart grids (acquired in Italy, where it has installed a large number of smart meters) by investing in

[7] Data from European Patent Office, Worldwide Patent Statistical Database (PATSTAT) [online] http://www.epo.org/searching/subscription/raw/product-14-24.html.

its distribution subsidiaries in Latin America. In such instances FDI has a direct positive environmental impact on the region's economies.

Foreign direct investment can also have an indirect positive impact where the introduction of cleaner technology is be transferred to local firms through production linkages. There is little evidence of such technology spillovers in Latin America and the Caribbean, and the few studies carried out on green technologies confirm that potential is limited at present (Zarsky and Gallagher, 2009).

Transnational corporations' superiority in green technology may reawaken perennial concerns over the region's technological dependence. If cleaner production systems are ultimately imposed (either by market forces or by government regulation), and these systems include advanced technologies owned by foreign firms and governments, then technological dependence will increase. To avoid this situation, increased efforts should be made and mechanisms established to build local capacity in environmental technologies. While multilateral climate change negotiations always mention the transfer of technology to developing countries, a method for implementing such transfers has not yet been developed beyond some specific and limited efforts, such as the request by some countries (notably China) that Clean Development Mechanism projects contain a technology transfer component.

One way of creating local capacity is through the research and development (R&D) activities undertaken by transnational corporations in the region. Although on a much smaller scale than in the firms' home countries, these activities are still significant: at least 20% of the "green" patents filed in Brazil in 2014 belonged to transnational firms such as Dow, Fiat and Whirlpool.

Specific examples of foreign investment in the development of clean technologies include the Alstom centre of excellence in geothermal energy in Morelia, Mexico, and the development of second-generation ethanol in Brazil by a combination of domestic and foreign corporations (including Shell). In both cases, the transnationals are carrying out research on technologies that exploit the specific natural advantages of the host country: Mexico's abundant geothermal energy and Brazil's vast sugarcane crop.

Private investments in clean technologies generally respond to specific government incentives. If the region's governments do not set environmental targets in certain key sectors (as they do in Europe and the United States), then foreign and domestic companies will not invest in developing the technologies needed to meet these targets. The automotive sector provides a clear illustration of the relationship between environmental regulations and standards and investment in new technologies (see box III.3).

Box III.3

The automotive industry: technological efforts and environmental standards

The automotive industry is one of the region's most crucial sectors (in Brazil it accounts for 5% of GDP) and is currently in a growth phase (see section B.2 of chapter I). The sector is dominated by transnational corporations: all of the region's vehicle assembly firms and the largest auto parts manufacturers are foreign owned.

The industry's environmental sustainability is under scrutiny because of the direct impact of the vehicles it produces, rather than that of its operations. In Latin America, road transport generates 32% of CO_2 emissions, double the global average (Lee Schipper, Deakin and McAndrews, 2010), and is one of the main causes of unacceptably high pollution levels in Lima, Rio de Janeiro (Brazil), Santiago and the continent's other major cities. Of the many dimensions to environmental sustainability in vehicles, the most important is the reduction of CO_2 and other pollutant emissions per kilometre travelled. Various alternative technologies seek to address this: reducing the vehicle's weight, improving its mechanics, developing more efficient internal combustion engines, increasing the use of biofuels and introducing electric engines. Automakers are allocating much of their huge research and development budgets to the design of vehicles that produce fewer and fewer emissions, though it is not yet known which technological solutions will ultimately prevail.

Automotive firms have two main technical objectives: to make vehicles more efficient and to meet the emission standards set by governments. These standards were introduced for the first time in the United States and Europe in 1987 and 1992 respectively, have been updated several times, and are now applied in most of the world's countries.

Governments may have different motivations for adopting emission standards, from fulfilling their emission reduction commitments to alleviating local pollution in cities. Another reason relates to industrial policy: developing countries with automotive sectors that receive FDI have shown much greater inclination to set standards for polluting emissions than those that do not have an automotive industry. This is because setting standards incentivizes innovation by the enterprises operating in the country. Brazil, China, India and Mexico have all seen a jump in the number of patents filed by the sector after emission standards were introduced (Saikawa and Urpelainen, 2014).

To what extent has industrial policy has played a part in the adoption of emission standards in Latin America? The two countries that account for the bulk of the region's vehicle production —Mexico and Brazil— receive extremely high levels of foreign investment in their respective auto industries. While

Box III.3 (concluded)

Mexican production is geared towards supplying the United States and Canadian markets, in Brazil the sector is largely focused on domestic consumption and, to a very limited extent, exports to South America. The Mexican automotive industry is therefore largely insensitive to domestic environmental regulations and highly attuned to those of the United States. Consequently the Mexican Government has little scope for influencing the technological development of its industry through emission standards, and has been unable to close the gap with United States standards.

By contrast, Brazil is noteworthy for an original policy based on the uptake of technologies that enable the use of ethanol in vehicles. Between 2002 and 2005, in response to fiscal incentives, the country's main automakers launched flexible-fuel or "flex-fuel" vehicles capable of running on either gasoline or ethanol. This technology has been highly successful and is now incorporated into nearly all of the cars sold in the country, creating a boom in ethanol consumption. However, in recent years the policy has been sidelined by the Government's decision to keep gasoline prices below the cost of production as a means of controlling inflation. This policy has had a heavy impact on ethanol producers, who decided to suspend their expansion plans as a consequence of falling demand. Moreover, the latest incentives for the automotive industry are designed to strengthen local capacity and increase value added, rather than making cars less polluting; this contrasts with the State assistance that the industry received after the crisis in Europe and the United States.

There is a worldwide trend towards more efficient vehicles which, though potentially endangered by the recent fall in oil prices, will push corporations to innovate in this area. For example, in 2014 Italy's Pirelli announced that it was investing US$ 210 million in a "green tyre" plant in Brazil, which will produce tyres that help reduce fuel consumption. However, explicit public policies are required if countries are to attract investment in innovative technologies such as flex-fuel engines.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

4. Codes of conduct and voluntary initiatives by transnational corporations

Investment strategies may include various actions in response to price signals and public regulation, but beyond such actions, corporations have considerable scope for decision-making that involves a greater commitment to looking after the environment.

One of the first things that firms can do is to compile and publish information about their environmental footprint. The organization Global Reporting Initiative (GRI) registered a total of 4,102 sustainability reports in 2013, a tenfold increase on 2005. In fact, there are now few large enterprises that do not publish these reports and, though they remain voluntary, efforts are being made to require companies to report significant aspects of their activity. GRI also manages specific reporting criteria, which are used for the grading of corporate sustainability reports.[8]

Many firms are also choosing to count and report their greenhouse gas emissions. In fact, most of the major transnational corporations already do so, albeit to different levels of detail.[9] More than 4,500 corporations from 80 countries report their emissions through the Carbon Disclosure Project (CDP), in which 80 of the largest firms in Latin America were asked to participate, although only 42, mostly from Brazil, responded (PriceWaterhouseCoopers, 2014). Of these corporations, only eight were included among the world's most transparent companies (according to the Climate Disclosure Leadership Index). None of them figured in the Climate Performance Leadership Index that recognized 187 businesses in 2014, almost all of which were from developed countries, although one was from China, five from India and six from South Africa.

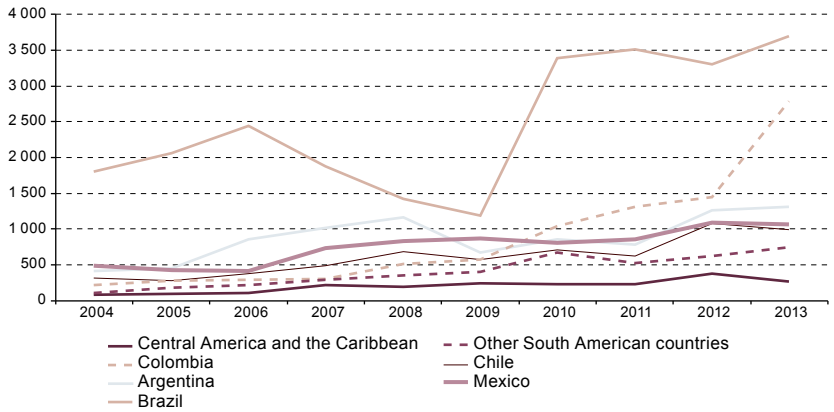
There are several reasons for businesses to calculate and report their carbon footprint, perhaps the most important of which is growing demand from financial markets. CDP was set up on behalf of 767 institutional investors, representing US$ 92 trillion in assets, who wished to receive insight into companies' climate performance. Many businesses understand that the need to quantify, report and —in all likelihood— reduce emissions will soon be an inescapable legal obligation. In the European Union, some 6,000 enterprises will be required to publish specific information on their environmental, social and governance performance as part of their financial reporting to investors. In China, the Government will require that more than 20,000 businesses provide information on their greenhouse gas emissions. It will not be long before Latin American companies are obliged to participate in this worldwide trend.

[8] For further information, see Global Reporting Initiative, Sustainability Disclosure Database [online] http://database.globalreporting.org/.

[9] Emissions may be quantified in three "scopes". Scope 1 includes emissions from company-owned facilities; Scope 2, those generated in the production of the electricity used by the company; and Scope 3, indirect emissions released at any point in the value chain as a result of the company's activity (PriceWaterhouseCoopers, 2014).

Another increasingly common practice is ISO 14001 certification. This management tool, designed to help companies identify and control their environmental impacts,[10] was employed by almost 11,000 businesses in the region in 2013, as compared with 3,000 in 2004. Brazilian firms have been most active in seeking this certification, while Colombian businesses have shown the fastest rate of uptake in recent years. Mexico has relatively few certified companies (see figure III.5).

Figure III.5
Latin America and the Caribbean: ISO 14001 certifications, 2004-2013
(Number of firms)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of data from International Organization for Standardization (ISO) [online] http://www.iso.org.

There are no data on the prevalence of ISO 14000 certifications among the subsidiaries of foreign enterprises in the region, although in other developing countries it has been observed that firms from developed countries are more likely to obtain this certification (Tambunlertchai, Kontoleon and Khanna, 2012). As with other corporate practices, the presence of foreign firms that have obtained ISO 14000 certification may serve as an incentive for local firms to follow suit (Prakash and Potoski, 2007). Leadership by foreign enterprises was also found to have been a factor in the growth of sectoral certifications such as Responsible Care[11] in the chemical industry (Garcia-Johnson, 2001) and the forestry sector's commitment to fighting deforestation (CDP, 2014a).[12]

In many cases, companies are motivated to join these initiatives simply to improve their image, as part of their marketing strategy. This kind of strategy will carry more weight in certain sectors, for example tourism, since it will help the company gain market share among the increasing number of consumers who are sensitive to such concerns.

Another reason is to facilitate funding. Many institutional investors require that corporations reveal their exposure to environmental risks, sometimes because of ethical concerns, but increasingly because they believe that activities that are incompatible with the preservation of the environment are also financially unsustainable, since sooner or later governments will encumber them with taxes or restrictions. In recent years and in view of falling oil prices, oil firms have seen some of their main investors deciding to divest[13] in the belief that the hydrocarbons business could be rendered unviable by future climate-change mitigation activities. One notable initiative in Latin America and the Caribbean is that of the São Paulo Stock Exchange, with the support of the World Bank and the Business Administration School of São Paulo at the Getulio Vargas Foundation (FGV-EAESP), which has prepared an index of

[10] There are various certifications within the ISO 14000 family. ISO 14001 and ISO 14004 relate to environmental management systems, while other standards focus on specific approaches such as life cycle analysis, communications and audits.

[11] Launched in 1985, Responsible Care was the chemical industry's response to the Bhopal disaster in India, when a gas leak at a pesticide plant owned by Union Carbide, a transnational corporation, caused the worst industrial accident in history. Five hundred thousand people were directly affected, thousands of whom died.

[12] One hundred and sixty-two of the world's largest forestry companies (including the 10 leading firms) heeded the call of the Carbon Disclosure Project by making a commitment to reduce deforestation and to share information about their activities, even where the reporting finds significant inconsistencies in many of these actions. The initiative met with little response from Latin America's main forestry companies: only one of the region's seven largest firms (Brazil's Klabin) agreed to participate.

[13] According to estimates by Arabella Advisors (2014), 180 institutions and hundreds of individuals, representing more than US$ 50 billion in assets, have pledged to divest from fossil fuels.

the 40 corporations with the best performing sustainability indicators of the 200 firms with the most liquid stocks on the market. The resulting index is highly valued by many institutional investors and therefore by the corporations themselves (Macedo and others, 2012).

As well as the advantages to be gained in their client and investor relations, corporations also mention cost savings as one of the main reasons for reducing their environmental impact. In this regard, most actions taken by companies involve lowering their consumption of inputs or energy, which undoubtedly requires a management effort and an attitude change, but which delivers an immediate —and long-term— cost reduction. The projects undertaken by the 187 leading companies in emission reduction enjoyed very high internal rates of return (CDP, 2014b).

In summary, there is a broad spectrum of voluntary activities whereby corporations can diminish their environmental footprint, and more and more firms are signing up to such initiatives. While it is impossible to quantify their actual impact, an effort to standardize and oversee corporate carbon footprint accounting could provide sound data on CO_2 emissions. Until then, it will be difficult to avoid the suspicion that many such activities are public relations strategies without any real benefit for the environment. Even where voluntary initiatives might have a material impact, or be used as a benchmark in policy design, they should never be taken as substitutes for public regulation.

Box III.4
Sugarcane: at the nexus of land, water, energy and food

Agriculture is a major driver of greenhouse gas emissions in Latin America and the Caribbean. The sector is responsible for 28% of the region's total emissions (as against 13% of global emissions), while changes in land use, often associated with agricultural activity, account for further 21% (compared with 5% of global emissions). Although emissions from changes in land use have fallen in the region over the past two decades, those from agriculture have risen by 20% (ECLAC, 2014b).

The presence of FDI in the agriculture sector is small. In the countries that reported data, FDI in agriculture stood at less than 2% of the total, with only Uruguay (22%), Guatemala (13%) and Belize (9%) posting higher figures (ECLAC, 2013). Nonetheless, some subsectors, such as the sugarcane industry in Brazil, have attracted sizeable investments.

Originally developed under a State energy security policy, the Brazilian sugarcane industry was deregulated in the 1990s, leading to a deep restructuring of the production chain. Larger enterprises, including many transnationals, entered the market and integrated its agricultural (the sugarcane harvest) and industrial dimensions (the production of sugar, ethanol and biomass electricity). In 2008, foreign firms accounted for 23% of output, a percentage that has certainly increased since then. The largest producers currently include energy companies including Shell and BP, and agricultural concerns such as Cargill and Tereos, often in strategic partnerships with local companies. The industry has also attracted FDI in countries such as Colombia, Guatemala and Nicaragua, albeit on a much smaller scale.

For transnational corporations —and energy companies in particular— sugarcane was a means of diversifying from fossil fuels, since controls on greenhouse gas emissions threatened their future development. From this perspective, investment in Brazil would increase the global sustainability of biofuel production, since sugarcane ethanol is much more efficient than other types of biofuel (BNDES/CGEE, 2008).

The prospect of expansion also raised environmental concerns, since the levels of sugarcane production that some studies suggested were needed from an emission-reduction perspective would also create a demand for land and water that would be incompatible with other sustainability criteria (United Nations, 2014). Moreover, a change in energy policy, which in recent years has prioritized low gasoline prices, led to a profitability crisis in the sector and halted its growth.

The Government of Brazil and the companies themselves have responded, through various initiatives, to environmental criticism of sugarcane expansion. First, to reduce the potential impact of sugarcane crops on biodiversity, an agro-environmental zoning system was launched in 2008 to allow sugarcane plantations in certain areas (Secretariat of Environment/São Paulo State Government, undated). Second, to reduce environmental costs, in 2007 sugarcane companies signed a voluntary agreement to mechanize 90% of the harvest in the State of São Paulo (Brazil's largest producer). This target was met in the harvest of 2013/2014, dramatically reducing the environmental impact (mechanization eliminates the need for pre-harvest burning) and improving working conditions. Away from Brazil, other corporations are taking steps to mechanize production, including Grupo Pantaleón, a Central American company that has measured its CO_2 emissions since 2012.

Another significant initiative for enhancing the industry's sustainability is the development of second-generation ethanol. This is an innovation in the industrial process that enables the extraction of ethanol from sugarcane cellulose, thus increasing productivity per cultivated hectare and reducing emissions. The first second-generation ethanol plant was opened in September 2014 by the firm GranBio (the Brazilian Development Bank (BNDES), which is promoting the development of this technology, holds a 15% share in the company). The second plant was opened shortly afterwards by Raizen (50% owned by Anglo-Dutch energy company Shell).

Sugarcane production in Brazil and other countries has potential for expansion but can also lead to severe environmental impacts. This has led to scrutiny of the sector by governments and ecological organizations, and leading to positive changes such as mechanization and second-generation ethanol. Foreign direct investment, along with the development of national firms and the participation of public-sector organizations such as BNDES, has helped build the requisite capacity for making these improvements.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

B. Looking to the future: foreign direct investment and sustainable development

Reducing the environmental impact of activities will require a behavioural shift among companies and consumers, as well as plentiful investment. Many of the necessary adjustments can be made with the current endowment of capital and infrastructure, but others will require radical changes in transport and energy infrastructure, irrigation systems and industrial plants. Some of these changes involve significant investments in fixed assets that will only be recovered in the long run, while other solutions (for example, carbon capture and storage) are still in a development or pilot phase, requiring large outlays on research and development. This section will explore the possible role of foreign direct investment in covering these requirements in the region.

Calculating the investment needed to make society's activities more environmentally sustainable is difficult in the extreme. Even when agreement exists over a specific goal (for example, reducing greenhouse gas emissions to a certain level, or extending sanitation services to a certain population), there is no single way of achieving that objective, with different paths requiring different levels of investment. Moreover, some facilities are still at the edge of technical capacity and the cost of their mass installation is highly uncertain.

One effort to quantify global investment needs for sustainable development (in all its dimensions) was recently made by United Nations Conference on Trade and Development (UNCTAD) in its publication *World Investment Report 2014* (UNCTAD, 2014). The report estimated that the investment required to meet the sustainable development goals (SDGs) in developing economies amounted to US$ 3.9 trillion per year, with the countries currently facing an annual gap of US$ 2.5 trillion. The report also highlighted three specific environmental goals in which investment needed to be found: climate change mitigation and adaptation, biodiversity and ecosystem maintenance, and water and sanitation services. Table III.2 summarizes these investment estimates.

Table III.2
World: annual current investment and estimated investment needs to meet the sustainable development goals on the environment, 2015-2030
(Billions of dollars and percentages)

Goal	Investment *(billions of dollars)*			Private-sector participation in current investment *(percentages)*	
	Current investment (latest available year)	2015-2030			
		Estimated investment required	Investment gap	Developing countries	Developed countries
Climate change mitigation	170	550-850	360-680	40	90
Climate change adaptation	20	80-120	60-100	0-20	0-20
Ecosystems and biodiversity [a]		70-210			
Water and sanitation	150	410	260	0-20	20-80

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2014. Investing in the SDGs: An Action Plan*, Geneva, 2014.
[a] The investment gap relating to ecosystems and biodiversity is not included owing to an overlap with other goals.

Huge investment is needed to achieve these goals. Worldwide, the estimated annual gap between current investment and the investment needed to meet the environmental SDGs by 2030 ranges from US$ 680 billion to US$ 1 trillion. While the public sector will always retain a key role, there is room for more private investment to help meet the sustainable development goals. The private sector currently contributes 40% of investment in climate change mitigation in developing countries, though this figure may be expected to rise (in developed countries it stands at 90%).

Different sources of funding are available within the private sector. Banks and pension funds hold total cumulative assets of US$ 8.8 trillion and US$ 1.4 trillion, respectively, in developing countries, while the assets of transnational corporations are in the same order of magnitude: US$ 7 trillion (US$ 2 trillion in Latin America and the Caribbean), plus US$ 5 trillion in cash holdings (UNCTAD, 2014). Foreign direct investment also has a number of potential advantages as a source of financing for projects to enhance the sustainability of economies. First and foremost, this type of investment

is accompanied by knowledge, which is particularly important in investments that require capacity-building. The region's greatest success story of recent years relates to investment in power generation from renewable sources (see box III.5).

Box III.5

Power from renewable sources: policies, markets and foreign direct investment

Power generation from renewables is a sector that is enjoying worldwide growth. At present, just 22.1% of the world's electricity is generated from renewable sources, mainly hydropower. Wind power accounts for about 3% and solar photovoltaic energy less than 1%, though both are growing much faster than conventional energy sources. In the past five years, investment in renewable energy has outstripped investment in fossil fuels, with wind and photovoltaic the fastest growing destination sectors. In Latin America, hydropower is much more important (supplying over half of electricity), while the proportion and the growth rate of wind and photovoltaic power are in line with the rest of the world.

In Latin America and the Caribbean, the countries that invested most in renewable energies in 2013 (not counting large hydropower plants) were Brazil (US$ 3 billion), Chile (US$ 1.6 billion) and Mexico (US$ 1.5 billion) (Frankfurt School/UNEP, 2015). In mid-2014, the generating capacity of Brazil's wind power sector topped 5 GW, while estimated investment stood at US$ 7 billion, more than double the 2013 figure and comparable with 2011 and 2012 levels. This increase in capacity was the outcome of a system of auctions in which wind power proved most competitive, thanks to steady winds in the south and north-east of the country.

Considering the size of their economies, notable investment efforts were also made in Uruguay (US$ 1.1. billion), Costa Rica (US$ 600 million) and Nicaragua (US$ 100 million). In 2014, Uruguay's wind capacity stood at 490 MW, a sixth of total power generation, and is likely to reach 1.2 GW by the end of 2015. The Government of Uruguay has boosted the sector through subsidies, public-private partnerships and long-term agreements with the domestic electricity distributor.

Solar photovoltaic is now the fastest-growing source of energy. GTM Research estimates that 805 MW of new photovoltaic capacity was installed in the region in 2014 (compared with 131 MW in 2013 and a projected 2,313 MW in 2015). At present, the most active country in photovoltaic power generation is Chile, which installed 308 MW of capacity in 2014 and is projected to add a further 1 GW in 2015; however, GTM Research forecasts that Mexico will be the leading market in the future. The largest project under construction is Luz del Norte in Copiapó, Chile, operated by First Solar of the United States, and which will have a capacity of 141 MW when it comes online in December 2015. Other significant operators include SunEdison, which has 155 MW currently in operation and a further 163 MW under construction in South America. In Chile, SunPower is the market leader, while Italy's Enel also has projects with a combined capacity of 169 MW pending completion.

Rising investment in new renewable energies has been driven by a combination of State support, favourable market conditions and foreign direct investment. Most Latin American governments have now set renewable energy targets (shown in the table below).

Latin America and the Caribbean: renewable energy targets

(Percentage of total electric power generation)

Country	Current share (2012)	Target		Notes
		Percentage	Year	
Antigua and Barbuda	0	10 15	2020 2030	
Argentina	-	8	2016	Target excludes large hydropower.
Bahamas	0	30	2030	
Barbados	-	29	2029	
Bolivia (Plurinational State of)	-	None		
Brazil	85	42.7 GW	2021	19.3 GW in bioenergy. 7.8 GW in small hydropower. 15.6 GW in wind. Current share includes large hydropower.
Chile	38	20	2025	Target excludes large hydropower. Current share includes large hydropower.
Colombia	81	6.5 and 20	2020	Current share includes large hydropower. Targets refer to grid-connected and off-grid respectively, and do not include large hydropower.
Costa Rica	92	100	2021	
Dominican Republic	14	25	2025	
Ecuador	55	None		
El Salvador	62	None		
Guatemala	64	80	2027	

Box III.5 (concluded)

Country	Current share (2012)	Target		Notes
		Percentage	Year	
Haiti	-	None		
Honduras	44	60 80	2022 2038	
Jamaica	5	15 20	2020 2030	The Government is considering raising the target to 30% in 2030.
Mexico	15	35	2026	
Nicaragua	43	74 90	2018 2020	
Panama	-	None		
Paraguay	-	None		Renewable sources already provide more than 100% of the country's electricity.
Peru	55	66	2024	
Saint Kitts and Nevis	0	20	2015	
Saint Lucia	-	15 30	2015 2020	
Saint Vincent and the Grenadines	17	30 60	2015 2020	
Trinidad and Tobago	-	5	2022	
Uruguay	60	90	2015	
Venezuela (Bolivarian Republic of)	64	None		

Source: Renewable Energy Policy Network for the 21st Century (REN21), *Renewables 2014 Global Status Report,* Paris, 2014.

State aid (modest by comparison with that provided in Europe) has coincided with a sharp decrease in the cost of renewable energy. In the past five years, the cost of solar photovoltaic energy has plummeted by 50%, while wind power became 15% cheaper thanks to technological advances and expanded input production capacity. Latin America's excellent resources make the region particularly suitable for the development of these technologies, as do the presence of geothermal energy (especially in Mexico and Central America) and biomass energy (associated with sugarcane production).

Foreign direct investment has played a central role in the rapid development of wind and solar photovoltaic energy in the region. This would not have been possible without the technical and financial capacities that were developed in the United States and especially Europe, and then brought to the region by transnational corporations. On the other hand, the growth of these industries in Latin America and the Caribbean provided a business opportunity for European (chiefly Spanish) companies at a time when European investment in renewables was on the wane. Latin America has also had the opportunity to avoid the mistakes that some European countries made in the design of incentives.

Not all activities by transnational corporations in this sector are recorded as foreign direct investment. For example, Spain's Aljaval is building a 33 MW solar farm in Chihuahua, Mexico, to be operated by local firm Rancho El Trece Solar PV. The Spanish company's contribution will be counted as imported goods and services. In the wind power sector, many facilities are installed and operated by foreign firms, but are mostly funded by local banks through project finance. For example, SunEdison of the United States is to build a 69.5 MW installation, with a total investment of US$ 130 million, part-funded by Corpbanca of Chile and BBVA of Spain. Most investments in Brazil, including by foreign companies, are mainly funded by loans from the Brazilian Development Bank (BNDES).

The electricity sector is dominated by three types of company: State-owned enterprises, private corporations (either foreign or national) and small businesses (again, either foreign or national) that operate in specific subsectors. The latter are particularly active in power generation from renewable sources, and include many foreign investors.

Some of the region's countries are taking advantage of the investment boom to develop industrial capacity in the sector. The most remarkable case is Brazil, where access to credit from BNDES (practically the only source of funding for energy projects) is contingent on compliance with local requirements. This policy has applied to the wind power sector for several years and is now being implemented in the solar photovoltaic sector. Meanwhile, Trinidad and Tobago is planning to commence the production of photovoltaic panels.

In the Caribbean, electricity usage from renewable sources is currently much lower than in Latin America (as the table shows), despite inferior access to non-renewable energy sources and higher energy prices than the Latin American subregion. Saint Vincent and the Grenadines and Saint Lucia adopted new national energy policies in 2009 and 2010, respectively. Some economies are interested in developing sources of geothermal energy, although doing so effectively may require the installation of electricity interconnectors between countries.

Source: Economic Commission for Latin America and the Caribbean (ECLAC).

Much of the investment needed to ensure sustainability will be channelled into infrastructure. Power-generation, transport and irrigation infrastructure will all have a profound impact on the sustainability of the region's economies. All of these sectors require substantial upfront investments that will be recouped over a lengthy period, with the result that foreign direct investment (and all private investment) is highly sensitive to current regulations and to investors' perceptions of their long-term stability.

Almost all of the region's governments are working to promote FDI in infrastructure projects, but in practice few countries have regulatory frameworks and markets with the potential to attract these inflows. Foreign direct investment in infrastructure has been relatively limited in the region, except in some specific segments (such as airports and ports in general, and highways in Chile). Foreign enterprises fulfil an important role in the construction of many major infrastructure projects such as the Panama Canal expansion (carried out by a consortium led by Spain's Sacyr Vallehermoso and Italy's Impregilo), but this does not extend to ownership or management once the projects are completed.[14]

In any case, it is governments that are responsible for designing sustainable transport infrastructure, although foreign firms may provide technological solutions in order to mitigate environmental impacts during construction. Railway construction and management has significant potential for FDI and can contribute to enhancing the sustainability of the region's transport system. However, efforts to attract foreign companies to this sector, especially for the high-speed lines planned in Brazil and Mexico, have not yet borne fruit.

In terms of energy infrastructure, besides the renewable power installations mentioned in box III.5, there is potential for increased investment in smart grids and energy storage; these are relatively new technologies whose uptake has been limited in Latin America and the Caribbean. Worldwide, investment in these sectors has amounted to almost US$ 34 billion per year since 2011, almost half of which has been spent on research and development (Frankfurt School/UNEP, 2015).

The need for a smaller environmental footprint has also led to the emergence of new business opportunities in the transport and water-management sectors. One recent study found that investment in clean technologies in developing economies could amount to US$ 6.4 trillion over the next decade (infoDev, 2014). To make their economies more sustainable, the region's governments must encourage FDI in these sectors, and should consider local capacity-building in new industries and sectors whose markets are expected to grow vigorously in the coming decades. In Latin America, biofuels and water and sanitation are sectors with particularly interesting prospects.

Water and sanitation services is one of the sectors that has received least FDI in Latin America and the Caribbean, despite many countries having implemented privatization programmes that induced some foreign firms to enter the market. Compared with other regions, Latin America and the Caribbean has achieved good drinking water and sanitation coverage. In urban areas, which are most likely to receive foreign investment in this sector, the only countries where less than 90% of the population has access to drinking water are the Dominican Republic and Haiti. There are greater shortcomings in sanitation coverage, which is still at very low levels in Haiti, Nicaragua and the Plurinational State of Bolivia (see table III.3).

Table III.3
Latin America and the Caribbean: share of urban population with access to basic services in countries with the lowest coverage, 2012
(Percentages)

Drinking water	Percentage	Sanitation	Percentage
Haiti	75	Haiti	31
Dominican Republic	82	Bolivia (Plurinational State of)	57
Peru	91	Nicaragua	63
Ecuador	92	Jamaica	78
El Salvador	95	Panama	80

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information from CEPALSTAT.

[14] Infrastructure projects by foreign firms are usually recorded as goods and services imports. Only when the foreign enterprise undertakes to operate the infrastructure (usually through a time-limited concession) is it counted as FDI.

The social return from covering these needs is clearly positive and more than justifies the investment, yet it remains difficult to find business models that are socially acceptable and which attract investors, particularly in the case of sanitation infrastructure. In fact, a goodly number of the foreign firms that invested in the sector in the late 1990s withdrew in the 2000s, which illustrates the difficulty of finding a balance between public and private interests in a sector that is extremely sensitive to social and political pressures (Ducci, 2007).

When promoting investment in these activities, consideration should be given to the balance between the liberalization of goods and services and the regulation needed for investments to achieve their public policy goals. It will also be very important to find the right combination of private financing and State support (either financial or regulatory). In Latin America and the Caribbean, many governments have found a successful way to attract investment in power generation from renewable sources, and such efforts should be expanded to the other types of investment needed to meet the sustainable development goals. Foreign direct investment has considerable potential in this regard, and the next section will review the status of the policies designed to capture it.

C. Environmental policy and investment promotion policy

All countries have environmental protection policies, as well as institutions that promote and regulate foreign direct investment. Yet despite the potential environmental impact of the activities carried out by transnational corporations, there is still little coordination between these two areas of public policy. This section first examines the environmental dimension of FDI policies, and then reviews some case studies in which other policies have a direct impact on FDI promotion.

1. Investment promotion agencies and environmental sustainability

This section is based on information from a survey of the region's investment promotion agencies,[15] who were questioned on the importance they attach to environmental issues in their work, the specific instruments that they use, and their outlook for the short and medium term.

Ninety per cent of agencies indicated that climate change mitigation was important in their FDI promotion policies. One a scale of one to five, with five being the most important, climate change mitigation received an average score of 3.7 points. Other environmental considerations (local pollution, deforestation and others) were regarded as more important, returning an average score of 3.9 points.

The percentage of agencies that attributed maximum importance to climate change mitigation shot up from 17% in 2010 to 33% in 2014.[16] Moreover, the percentage of agencies that attached little importance (2 points) to climate change mitigation in their policies more than halved, from 17% in 2010 to 8% in 2014.

Sixty-one per cent of agencies stated that they were actively seeking to attract foreign investments with a low environmental impact. This is an improvement in comparison with 2010 when only 50% declared that they were actively seeking to secure low-carbon foreign investment.

None of the agencies that claimed to be trying to attract green FDI had prepared any specific policy document on the environmental impact of foreign investments.[17] However, the Colombian agency had a document setting out out sustainability guidelines (including on environmental sustainability) (MCIT, 2012), while the export, tourism

[15] A questionnaire was sent to 31 national investment promotion agencies in the region between October and December 2014. Some of the questions were the same as those included in a questionnaire prepared by UNCTAD in 2010 (UNCTAD, 2010a). The response rate to the questionnaire was 61%, thanks to the participation of agencies from the following 19 countries: Antigua and Barbuda, Argentina, Barbados, Belize, Bolivarian Republic of Venezuela, Chile, Colombia, Costa Rica, Dominica, Dominican Republic, El Salvador, Grenada, Guatemala, Guyana, Montserrat, Nicaragua, Peru, Saint Kitts and Nevis and Uruguay.

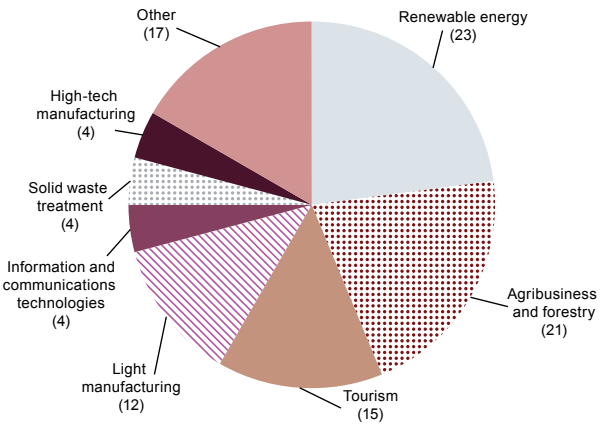
[16] The same agencies responded to a similar survey in 2010 (UNCTAD, 2010a).

[17] The document mentioned by the Peruvian agency was actually prepared by the Zofnass Program for Sustainable Infrastructure at Harvard University and refers only to a case study on the La Chira wastewater treatment plant and marine outfall (see Gúzman, 2013).

and investment promotion office, Proexport Colombia,[18] prepared its first Sustainability Report in 2013 (Proexport Colombia, 2013), which detailed its main achievements in relation to different sustainability objectives, including environmental sustainability.

Figure III.6 shows the target sectors in which, owing to their positive environmental impacts, countries aim to attract investment. The most important target sectors are power generation from renewable sources (23% of responses), agribusiness and forestry (21%), tourism (16%) and manufacturing (16%).

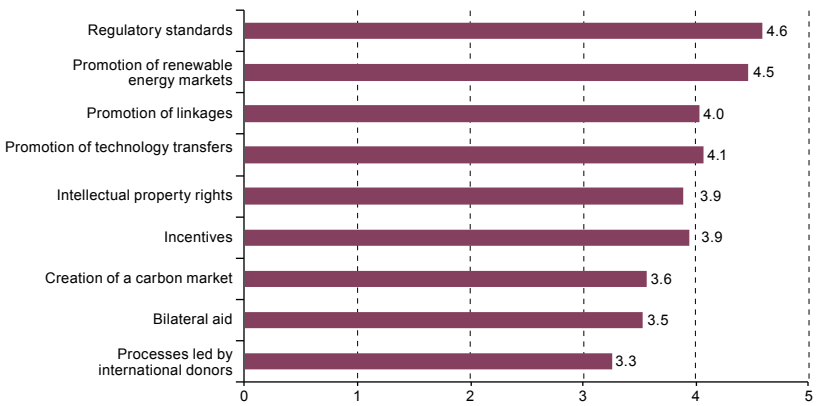
Figure III.6
Latin America and the Caribbean:[a] target sectors for attracting green investment
(Percentage of total responses)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the respective countries.
[a] Includes responses by investment promotion agencies in 19 of the region's countries, out of a possible 31, to a survey conducted between October and December 2014.

Regulatory standards and the promotion of renewable energy markets were the policy areas that investment promotion agencies considered most important in terms of the environmental impact of foreign investments (see figure III.7). On average, the areas deemed least important were processes led by international donors (3.4 points), bilateral aid (3.6 points) and the creation of a carbon market (3.6 points).

Figure III.7
Latin America and the Caribbean:[a] importance of policy areas in relation to the environmental impact of foreign investments
(Scores from 1 to 5, where 5 indicates the greatest importance)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the respective countries.
[a] Includes responses by investment promotion agencies in 19 of the region's countries, out of a possible 31, to a survey conducted between October and December 2014.

[18] Proexport Colombia was renamed ProColombia in November 2014.

The most important policy instruments used by investment promotion agencies to attract environmentally sustainable foreign investment were specific investment missions and the mapping of investment opportunities (both received an average score of 4.3 points), as well as the targeting of specific transnational corporations (4.2 points). On the other hand, specific advertising was seen as least important in attracting environmentally sustainable FDI (3.4 points).

Most agencies expressed the view that the environment would gain importance as an issue in the medium term (in the next three years). Only 26% of agencies said that it would be very important (score of 5) in the short term, although the figure rises to 47% in the medium term. Conversely, the percentage of agencies that see environmental issues as less important (3 points) falls from 37% in the short term to 11% in the medium term.

Despite the seemingly evident trend towards increased environmental consideration in FDI promotion, investment promotion agencies are in fact severely constrained in their scope for action. Environmentally sound FDI promotion activities are not necessarily coordinated with other policy areas, so that governments might incentivize power generation from renewable sources while simultaneously subsidizing fossil fuels, for example.

2. Environmental policies and implications for FDI promotion: some case studies

The region's countries differ greatly in terms of the importance attributed to the environmental aspects of FDI promotion policies. That said, some countries have clear policies that are focused on supporting the activities of firms with better environmental management. This section provides information on the environmental policies of some of the region's investment promotion agencies.

(a) Brazil: environmental aspects of industrial policy

Brazil's investment policy is primarily determined by the Plano Brasil Maior ("Bigger Brazil Plan"), which establishes specific industrial development targets in a number of sectors, one of which is renewable energy. Systemic, cross-sectoral measures, such as those on sustainable production, form the basis of efforts by the Brazilian Export and Investment Promotion Agency (Apex-Brasil) to promote the renewable energy sector. As box III.5 notes, in recent years these efforts have focused on wind power, a sector that has received substantial FDI inflows in both generation and equipment manufacturing. The first auction exclusively for solar photovoltaic energy projects was held in 2014, following the same structure as the auctions for wind power. Apex-Brasil is presently in the early stages of considering investment promotion in the environmental goods and services sector.

Besides the activities of Apex-Brasil, many aspects of environmental policy have a bearing on domestic and international investments. One of Brazil's hallmarks is its high level of decentralization, with States and even municipalities having a significant say in environmental decision-making (one such example is the agreement between the State of São Paulo and the sugarcane industry, as mentioned in box III.4). Another feature particular to Brazil is the power invested in the Public Prosecutor's Office, which is independent of the other three branches of government and has the authority to bring charges over possible crimes. On several occasions it has revoked environmental permits previously granted by the executive branch.

Environmental policy in Brazil places special emphasis on preserving biodiversity, particularly as regards the need to halt the deforestation of the Amazon. Environmental zoning, established in 2008, was a highly significant development for companies operating in the agriculture and forestry sectors.

Investment policy has generally prioritized industrial capacity-building over environmental criteria. For example, the measures launched in 2013 to boost the automotive sector (see box I.2 in ECLAC, 2014a) proposed to develop local capacity, but passed up the opportunity to strengthen environmental standards in the sector. On other occasions, the two objectives have been combined, as in the case of ethanol. Based on its competitive advantage in sugarcane production, for decades Brazil has pursued a policy that supports the use of sugarcane bioethanol in road transportation. This policy led to the development of flexible fuel vehicles, a homegrown technology that allows most new vehicles to be fuelled with either gasoline or ethanol. Moreover, in Brazil the ethanol blend in gasoline stands

at 25%. Combined with the fact that 85% of electricity is generated from renewable sources, it may be concluded that Brazil has the least carbon-intensive energy mix of any major world economy.

As in other areas of economic policy, the Brazilian Development Bank (BNDES) plays a crucial role. Two instruments are particularly relevant: environmental subcredits, which are compulsorily added to all large loans and which must be used to mitigate environmental damage, and the National Climate Change Fund, which is financed from oil revenues and is jointly managed by BNDES and the Ministry of Environment. The bank is also very active in technology policy and has assumed a prominent role in the development of second-generation ethanol (see box III.4).

(b) Chile: supporting opportunities in renewable energy

Chile's Foreign Investment Committee (CIEChile) endorses environmentally friendly activities, mainly electric power generation from renewable sources. In this sector, CIEChile promotes investment opportunities in hydropower and non-conventional renewable energies such as wind, solar, geothermal and biomass, underpinned by the clean power generation targets set by the Government. At present, hydropower accounts for 26.6% of the electricity produced in Chile, while only 6.3% comes from non-conventional renewables. The National Energy Strategy 2012-2030 aims to increase hydropower generation to between 45% and 48% by 2024, while Law No. 20698 encourages the expansion of the energy mix to include non-conventional renewable sources, stipulating that 20% of the electricity sold in the country should come from these sources by 2025.

Beyond the power sector, CIEChile promotes the growth of environmental activities that are sustainable but which as yet account for a small proportion of the country's economic activity, such as sustainable tourism and organic winemaking. The Chilean wine industry has developed the world's most comprehensive and ambitious sustainability accreditation system, and is seeking to position itself as the world leader in sustainable wine production by 2020.

(c) Colombia: indicators for measuring the environmental impact of FDI

A document prepared by the Ministry of Commerce, Industry and Tourism (MCIT) of Colombia establishes guidelines for its sustainable investment promotion policy, including criteria in relation to environmental sustainability. In this sense, the document states that "the goal is to attract sustainable investment and enhance the sustainability of inward investment in the country" (MCIT, 2012, page 4). These sustainability guidelines are intended for the use of the country's export, tourism and foreign investment promotion agency, Proexport Colombia (now ProColombia), and recommend the creation of a system of corporate sustainability indicators so that the agency will be able to identify investors that build sustainability into their operations. Suggested criteria include: (i) respect for cultural and historical heritage; (ii) respect for biodiversity; (iii) responsible investment policies in developing countries; and (iv) responsible environmental and social management policies. The document also outlines desired criteria for Proexport Colombia to take into account in relation to the nature of investor companies. These should be: (i) enterprises with cutting-edge green technologies; (ii) enterprises that promote clean production and sustainable consumption; (iii) enterprises that encourage sustainable production linkages; and (iv) enterprises in possession of environmental and social certifications.

The agency should also evaluate whether foreign direct investment projects abide by minimum environmental sustainability criteria, which include: (i) full compliance with environmental legislation; (ii) the exclusion of unsustainable business development from national parks, nature reserves, uplands and wetlands; and (iii) transparency in the environmental and social impact assessments carried out in respect of investments (MCIT, 2012, pages 29 and 30).

The above guidelines are proposed as part of a vision of the FDI initiatives that the country wants to attract in the context of its sustainable development, and are not binding on foreign firms wishing to launch operations in Colombia. The document stresses that "Colombia does not apply any selection process in relation to inward foreign direct investment (FDI), and foreign investment does not require prior authorization save in sectors such as financial services, mining and hydrocarbons, in which prior authorization is required for both national and international investments" (MCIT, 2012, page 5).

(d) Costa Rica: ban on mining activity

Costa Rica provides a clear example of inconsistency between domestic environmental sustainability policies and the FDI policy applied by the investment promotion agency. The Government is strongly committed to environmental issues, has set a target of 100% power generation from renewable sources, and aims for Costa Rica to be a carbon neutral economy by 2021. The country has also established a moratorium on open-pit mining and oil exploration and production, with the result that investment has ground to a halt in these sectors even as FDI in mining is booming in the rest of Central America.

On the other hand, the country's investment promotion agency, which claims to be actively seeking green investments, does not yet have any policy document establishing guidelines in this regard. Neither were any "green sectors" mentioned among the industries that the agency does most to promote (information and communications technology services, high-tech manufacturing and light manufacturing).

(e) Mexico: a climate change law that promotes renewable energies

As in Chile, Mexico's investment promotion agency, ProMéxico, focuses its sustainability efforts on promoting renewable energies. Mexico has taken various steps to encourage these investments in order to diversify its energy mix. In 2012, the General Law on Climate Change entered into force with the primary goal of cutting greenhouse gas emissions by 50% by 2050, compared with 2000 levels. In 2013, the Mexican Congress approved a tax on carbon emissions caused by fossil fuel use, which along with a national emissions registry will form part of a future carbon market.

More specific legislation largely falls under two laws: (i) the Law for the Development of Renewable Energies and Energy Transition Financing (LAERFTE), and (ii) the General Law on Climate Change (LGCC) of 2012. Both laws set targets: the first relating to proportion of electricity generated from fossil fuels, which will be limited to 65% by 2024, 60% by 2035 and 50% by 2050, while the second sets out the percentage that will be generated from clean sources, which should stand at 35% in 2024. These targets will guide policies for the promotion of renewable energies, so that the requirements established under these laws can be met in good time.

To achieve the above goals, the Government is offering several incentives to domestic and foreign investors. According to ProMéxico and the Secretariat of Energy (SENER, 2013), these include the following:

- Auctions for small-scale producers under a fixed-price system that ensures long-term revenue.
- An energy bank, to enable producers to accumulate excess energy under a self-supply scheme, to be used in the future or sold to the Federal Electricity Commission.
- A preferential rate for energy transmission. A service charge for renewable energy transmission or efficient cogeneration of 0.14 pesos per kWh, instead of the rate of 0.30 to 0.40 pesos per kWh that is charged for traditionally sourced energy.
- Accelerated depreciation of fixed assets.
- Exemption from paying general import or export taxes on anti-pollution equipment and parts, as well as on machinery, equipment, instruments, materials and other items for technological research or development related to renewable energy sources and clean technologies.

(f) Peru: improving water treatment and relaxing environmental controls on mining

In Peru, the activities of the Private Investment Promotion Agency (ProInversión) are coordinated with the National Environmental Action Plan (PLANAA) Peru 2011-2012 of the Ministry of Environment. The document *Guía de Negocios e Inversiones en el Perú 2014-2015* includes a comprehensive chapter on environmental sustainability. ProInversión aims to attract and deliver investment in accordance with environmental objectives in six priority areas: water, air, biodiversity, forests and climate change, solid waste and mining and energy.

Some notable investment promotion activities have focused on water treatment, especially the construction of the Taboada and La Chira wastewater treatment plants in 2009 and 2010, respectively.

In August 2009, Proinversión awarded Spain's Grupo ACS a 25-year concession to design, build, operate and maintain the Taboada wastewater treatment plant. The facility became operational in 2013 and now treats 72% of wastewater from the cities of Lima and Callao. Previously only 16% of Lima's wastewater was treated.

With the aim of raising this figure to 100%, on 18 November 2010 ProInversión awarded a design-build-operate contract for the La Chira treatment plant to a consortium comprised of Spain's Acciona and Peru's Graña y Montero. Construction commenced in June 2013 and is expected to last for 24 months. The initial operating contract is for 25 years, with the option to extend the concession to 60 years. Upon entering service, this second plant is expected to improve sanitary conditions in the neighbouring residential districts while helping to reduce greenhouse gas emissions and energy consumption (Guzmán, 2013).

Peru is also striving to attract investment in the petrochemical industry, through incentives and tax benefits for the development of petrochemical complexes in the south of the country. These initiatives underscore the importance of finding the right balance between development and production on the one hand, and the environment on the other. For example, article 9 of Law No. 29163, promoting the development of the petrochemical industry, sets forth that "the basic and intermediate petrochemical industry shall use new equipment and components that comply with international standards on safety, the environment and resource-use efficiency".[19]

In the mining sector —the main destination for FDI in Peru— notable legislation includes Law No. 3627 of July 2014, which is essentially designed to boost private investment in the country, specifically in hydrocarbon and mineral extraction, by cutting red tape and awarding tax benefits. The Law was approved in a context of falling mineral prices and deteriorating investment prospects, and has been strongly criticized by ecological groups for relaxing environmental regulations and curtailing the powers of the Ministry of Environment and its attached institutions, the Agency for Environmental Assessment and Enforcement (OEFA) and the National Service of Protected Natural Areas (SERNANP).

In particular, the Law stipulates that the environmental fines applied by OEFA will be halved for a period of three years, during which time the Agency will prioritize the prevention and modification of environmentally harmful behaviours over the application of penalties. Moreover, article 19 states that the proceeds of fines will be paid directly to the Treasury rather than to the enforcement agency, in order to avoid the perverse incentive that can arise in the imposition of monetary penalties.

The Law also simplifies the protocols and reduces the period for environmental impact assessments, stipulating that where the organization responsible for approving the environmental impact study requires binding or non-binding opinions from other public-sector bodies, these must be issued within 45 days. Should the required opinion not be issued in time, the official at fault will be fined and the body responsible for approving the environmental impact study should allow the approval process to continue without taking the requested opinion into consideration (article 20).

Article 22 deprives SERNANP of the power to decide on processes of land-use planning and ecological economic zoning in Peru, which must henceforth be approved by Supreme Decree. The article also sets forth that "land use may not be designated or excluded under ecological economic zoning or territorial planning", a provision that leaves open the possibility of mining or drilling in ecologically protected areas.

Lastly, article 23 revokes the Ministry of Environment's authority to change maximum permissible pollution and emission limits and environmental quality standards. Again, the approval of changes to these guidelines will be subject to the issuance of a Supreme Decree.

(g) Uruguay: environmental indicators for regulating incentives

Uruguay offers an interesting case study, since it is the only country in the region that uses an environmental indicator to award tax benefits to corporations. Decree No. 455/007 of 26 November 2007 states that foreign investments must be in keeping with the country's strategic objectives, including that of cleaner production, in order to be eligible for the tax benefits laid out under Law No. 16906 on investment promotion and protection.

Furthermore, Decree No. 002/012 of 2 February 2012 sets out a new methodology for the evaluation of FDI projects based on specific criteria. One of these is investment in cleaner production, defined by United Nations

[19] The same provision is included under article 6 of Law No. 29690 promoting the ethane-based petrochemical industry.

Environment Programme (UNEP) as "the continuous application of an integrated preventive environmental strategy to processes and products so as to reduce the risks to humans and the environment" (UNDP, 1999). Under the evaluation methodology, investors are assigned one point for every 5% of the total investment that is allocated to cleaner production.

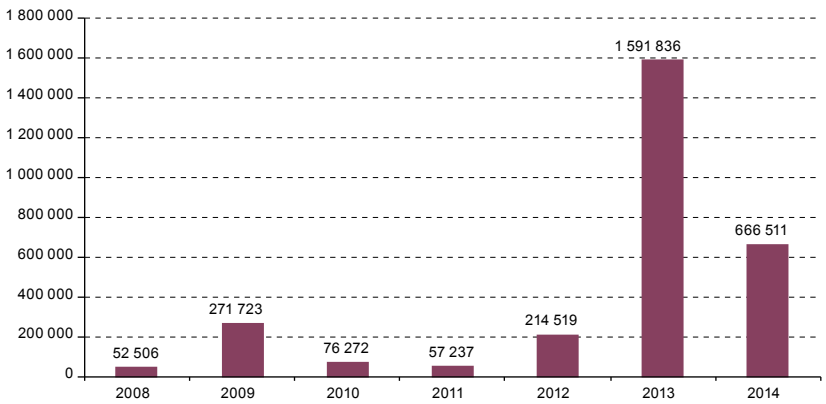
Depending on the nature of the proposed investment project, companies may also opt for a sectoral indicator. For example, in the agricultural sector, one of these indicators is investment in climate change adaptation and/or mitigation. Again, the methodology gives one point (up to a maximum of 10 points) for every 5% of the total investment that is allocated to climate change mitigation.

In 2014, the Private Sector Support Unit (UnASeP) prepared a case study to assess compliance with these targets by the companies that applied for tax benefits under Law No. 16906 on investment promotion and protection.[20]

As regards the cleaner production indicator, of the 56 companies that took this option, only 51 were included in the case study, owing to availability of information. Compliance with the indicator was high, since on average the companies were revealed to have implemented 89% of pledged investment in cleaner production. Notable investments were made in professional, scientific and technical activities; financial activities; manufacturing and the supply of electricity, gas, steam and air conditioning.

Since the issuance of Decree No. 002/012 in 2012, investment in cleaner production and in climate change adaptation and mitigation has rocketed. Data from UnASeP (2014b) show that investment in cleaner production rose from an annual average of US$ 154 million between 2009 and 2012 to an annual average of US$ 1.129 billion in 2013 and 2014 (see figure III.8). Much of this increase was brought about by the entry of wind power companies into the market. As for the sectoral indicator on climate change adaptation and mitigation, also introduced under Decree 002/012, investment rose from US$ 3million between January and August 2013 to US$ 74.2 million in the same period in 2014.

Figure III.8
Uruguay: investment in cleaner production, 2008-2014
(Thousands of dollars)



Source: Private Sector Support Unit (UnASeP), "Inversión recomendada e indicadores asociados", Ministry of Economic Affairs and Finance, 2014 [online] http://www.mef.gub.uy/unasep/documentos/201408_Inversion_recomendada _e_indicadores_asociados.pdf.

3. Spaces for integrating sustainability into investment promotion policy

Investment promotion agencies in Latin America and the Caribbean have acquired a greater awareness of the importance of environmental sustainability and are carrying out more and more activities in this area, though these efforts are still on a modest scale. Moreover, their room for manoeuvre is limited in terms of providing incentives or improving the

[20] The analysis looked at a total of 2,346 projects submitted to the Law No. 16906 Application Commission (COMAP) of the Ministry of Economic Affairs and Finance (MEF), between January 2008 and 31 December 2013.

investment climate in certain sectors, so that in practice their work is reduced to supporting environmental policy decisions with some specific programmes to attract FDI with positive environmental impacts. The only country in the region that has consistently applied environmental criteria in allocating incentives is Uruguay, and its experience is still too recent to gauge its success.

In most cases, the main investment initiative designed to improve economic sustainability is the promotion of investment in power generation from renewable sources. Chile and Mexico are the main examples of this approach, which has achieved some success in many countries, largely because it has been coupled with energy policies that favour renewable sources. The challenge is to identify new sectors and segments that can contribute to environmental sustainability and which are capable of attracting FDI. Other infrastructure sectors, such as transport, may provide opportunities in future.

All of the region's countries have environmental policies, which have generally been gaining ground in recent years, but their relationship with investment policies is still uncertain and varies significantly among the cases examined. Environmental targets are usually combined with other policy objectives to create specific initiatives. In Brazil, the most noteworthy environmental actions are combined with efforts to build industrial capacity, for example in the manufacture of renewable energy components. Peru has strived to attract infrastructure investments, including environmental investments, while Costa Rica has prioritized the protection of natural spaces, leading to a near-total ban on mining activity. In many countries, the incentives granted to renewable energies tend to stem from an interest in reducing energy dependency, rather than enhancing sustainability.

Beyond national policies, international agreements with a bearing on FDI —from bilateral investment treaties to trade pacts such as the North American Free Trade Agreement (NAFTA)— may narrow the space in which governments are able to implement environmental policies. On several occasions, transnational corporations directly affected by environmental policy decisions have appealed against them on the grounds of clauses contained in international agreements. It is therefore important that the language used in these agreements leaves sufficient space for the adaptation of environmental legislation (UNCTAD, 2010b).

D. Conclusions

Adapting the region's economies to counter environmental degradation, which has many dimensions in Latin America and the Caribbean, is a complex task. Transnational corporations are key actors in these economies and unquestionably must participate in this effort. Unfortunately, it is impossible to estimate the environmental impact of these companies' activities, although some conclusions may be drawn from the experience of recent years.

The first is that the environmental impact of FDI is heavily contingent on each country's production structure. Those countries that receive greater FDI flows in more polluting sectors must expect a more severe environmental impact, and will face difficulties in mitigating said impact through the application of tighter regulations and standards.

Public regulations remain crucial and cannot be substituted for voluntary initiatives on the part of industry. Such initiatives have taken large strides in recent years, and many are driven by transnational corporations that have introduced practices to the region that they originally applied in other countries. The real impact of these combined initiatives cannot be measured, but they may generate better results in segments where private incentives are aligned with public ones (for example, improvements in energy efficiency).

Besides reducing FDI in polluting sectors and mitigating impacts through regulations, countries in the region should also seek to attract extra investment in projects that contribute to achieving the sustainable development goals. Such investment has huge potential, but opportunities must be translated into sustainable business models for enterprises and countries alike. In previous decades, sizeable investments in water and sanitation yielded negative outcomes, leading to the abandonment of projects after serious social conflicts. Conversely, some of the region's countries have managed to design a policy framework that attracts FDI to the renewable energy sector.

Governments in the region should pursue synergies between these initiatives and public policy goals, while favouring channels for the imitation and learning of best practices. In this regard, sectoral agreements (such as the one signed by the sugarcane industry in the State of São Paulo) are an example of how to transfer a good business practice to an entire sector.

Reducing the environmental impact of productive sectors in Latin America and the Caribbean will also require the introduction of new technologies —most of which originate in developed countries— in a process that is fundamentally driven by transnational corporations. As with other types of technology, technology transfer through FDI is uncertain, difficult to measure, and constrained by the underdevelopment of production linkages with transnational corporations.

Governments should also identify key sectors and segments for introducing cleaner modes of production, and seek to attract FDI accordingly. The priority is to ensure consistency between FDI promotion policies and other policies that affect the environment, such as those on energy, transport, urban planning and agriculture.

In these and other areas, FDI must be regarded as an instrument for local capacity-building. It is ultimately local firms that will realize much of the transition towards a green economy, and they should have the incentives and capacities needed to achieve that end.

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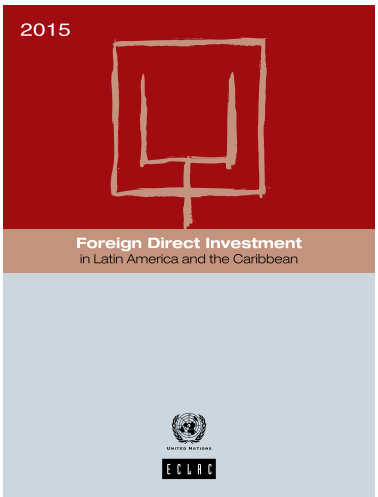

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