The competition in Latin America encompasses four categories of players: large domestic firms, state owned enterprises, small and medium-sized businesses, and multinational firms.

LARGE DOMESTIC FIRMS: FAMILY CONGLOMERATES

The private sector development in Latin America has been the large domestic firms; most of them are family businesses. Although liberalisation of trade and investment has threatened or destroyed many, others have linked up with multinationals or been acquired by them and in turn, have developed new businesses. Many powerful Chief Executive Officers of these enterprises have embraced the need for transparency and modern business practices, whereas others cling to their privacy and traditional ways of conducting business.

The family owned domestic conglomerates occupy presently a leading role in the Latin American business world. Most were formed during the import substitution industrialisation period following the World War II, although some date to the beginning of the twentieth century, when the industrialisation process began in the more advanced countries of the region Argentina, Brazil, Colombia, Chile and Mexico.

The origin of these conglomerates centered on three strategic pillars

1. Expansion based on the development of natural resources.
2. Growth based on diversification, for the purpose of generating synergies through a core industrial base.
3. The acquisition by financial, construction and service firms of businesses in their respective industries.

Apart from the family conglomerates, there are presently new and often very powerful economic groups that came into being and began to flourish during the course of neo-liberal reform and economic restructuring in the 1980s. These new organisations resulted from the privatisation of traditional activities as well as the dynamic growth of conglomerates with
their portfolio approach to governance and management. In the second half of the 1990s, new family owned domestic organisation arose just as traditional ones were disappearing. This suggests the existence of different capabilities in strategic response to political and economic changes as well as competition between large investor groups and traditional oligopolies that had been thriving in protected markets.

Before Latin America’s opening of their economies to foreign competition, the family owned companies had started to export non-traditional products to boost their sales overseas. Other groups, the largest ones, internationalised more widely and deeply, exporting not only merchandise but also capital. They have pursued three types of strategies.

1. **Withdrawal**: This is the tendency to concentrate on the complete sale or sales of majority control of the enterprise to foreign investors rather than closing the business.

2. **Defensive**: Preventive investments; that is pre-emptive purchase of an acquisition target or purchase of a large, existing domestic competitor; the importation of the finished goods for their sale in country, thereby taking advantage of local distribution networks; a greater and more intensive orientation toward the customer, particularly in the food industry; the formation of industrial and financial groups; and the search for the profitability via access to fiscal or business incentive or sector promotion policies. One modality of defensive strategy has been the growth of industrial and service activities, motivated by market deregulation or the privileged access in competing for business opportunities, particularly the privatisation of communication, electricity distribution, and infrastructure in general.

3. **Offensive**: There are several options. One is to strengthen and expand the firm’s core business activities. Another option is moderate growth through the pursuit of diversification. The achievement of potential synergies is the basic aim of these types of business operations.

Finally, there is growth with extensive diversification, for the most part the result of participation in a number of privatisation. In these cases, one witnesses the emergence of true conglomerates, businesses that are profitable but lack synergies in production manufacturing, commercial operations, and financial management.
STATE - OWNED ENTERPRISES (SOE)

The adoption of import substitution industrialisation model, neo-mercantilist and protectionist tendencies which were part of the economic fabric of the region since colonial and post-interventionist state presence on basic industries was nourished by massive amounts of multilateral funding from development banks, bilateral aid, and sovereign lending by global financial institutions. A strong trajectory of worldwide economic growth during the first three decades following the war broadened and deepened the trend toward large state-owned companies as a key engine of development.

State-owned enterprises have shrunk dramatically, due to the privatisation wave from the early 1990s; nevertheless, many remain especially in public utilities and compete with or prevent competition with large private firms. SOEs that have not been sold off because they are not financially attractive candidates for privatisation, are cash cows for the government or for reasons of nationalism are now turning to private management and contracting out services to boost efficiency and effectiveness. Nearly two decades have passed since Latin America began to sell off its SOEs, and the benefits from this process have been well documented. Privatisations have reduced public deficits, created new productive employment, increased government revenues, and created competition and improvement in the quality of public services.

In an increasing effort to improve performance, transparency, and accountability, governments have turned to outsourcing to the private sector. The provision of services need not be the same as government production. Contracting out an entire operation or only part of it can accomplish multiple objectives. These include cost reduction, less political interference, more adaptable labor force practices, management flexibility, improved chances to innovate, and improved effectiveness of service provision through performance-based contracts themselves.

Although SOEs have been diminished markedly during the last decade, they still play a role in international commerce as large purchasers of raw materials and inputs and as exporters of commodities, manufactured goods, and services. SOEs compete with local and multinational enterprises in many instances; in many others they serve as a rich business for private-sector
suppliers of everything from energy products to engineering, construction, procurement services, information technology and telecommunications.

Despite the massive Latin American privatisations in the late 1990s, SOEs are down but not out. There have been exceptions to the selling spree; and the expectations are large. Among the top 500 biggest companies in Latin America, three biggest are SOEs; and these three have held the top spots for the last 10 years: Pemex (Mexico), PDVSA (Venezuela), and Petrobras (Brazil) all oil companies. These are globally competitive firms, to whose ranks should be added to Codelco (Chile), the world’s largest copper producer. These four firms produce about USD100 billion in revenue annually. They have not been privatised for various reasons like nationalist sentiment, political opposition, and especially, their enormous importance as revenue producers for the government.

**SMALL BUSINESS ENTERPRISES: FORMAL AND INFORMAL**

The small-business sector in Latin America, both formal and informal, accounts for nearly 90% of private-sector activity in the region. Small and medium sized enterprises (SMEs), along with micro enterprise, are engaged in a broad range of economic activities in agriculture, manufacturing, retailing, services, and transportation. The principal market for both industrial and consumer goods and services of the SME sector is the domestic market; however, macro-and micro economic reforms and trade liberalisation have energised a number of enterprises, from handicrafts and apparel to food products and industrial materials, to seek markets beyond their borders. The increased economic activity due to trade, finance, and investment integration in NAFTA, MERCOSUR AND THE ANDEAN COMMUNITY has also fostered the growth of SME suppliers to multinational firms and to large local enterprises.

The competitive challenges to SMEs have increased and intensified given the market-opening measures (unilateral, bilateral and multilateral) that have accompanied regional economic reform. Mercosur provides an excellent example. Here the integration process is having structural repercussions on the conduct of the firms in terms of production, on the definition of their future business strategies and on their investment decisions. For many SMEs, especially those who produce tradable manufacturers subjected to the influence of international technological and consumption patterns, or for producers of intermediate goods,
parts, or components for use by assembly or terminal industries, the present challenge is to redesign their businesses, rethinking both production activity and business strategies. The reason is that the condition under which these enterprises were set up and managed by their owners in the past has undergone substantial changes.

Small and medium-sized enterprises in Mercosur are concentrated in labor-intensive manufacturing activities, especially natural resources –based, agro industries, agro food industries and mature manufacturing activities (clothing, footwear, plastics, metal products and machineries). A significant part of the activities of SMEs are connected with the manufacture of intermediate products, parts, components, processes or sub assemblies incorporated in other manufactured goods.

Throughout the hemisphere, not just within Mercosur, SME entrepreneurs are faced with a number of serious business challenges. These include restructuring a firm’s business operations to respond to regional economic integration and its impacts on local markets, repositioning the firm and developing competitive strategies to ward off threats and seize opportunities brought about by internationalisation and improving technological capability. As SMEs strive to meet these challenges, they are faced with internal constraints characteristic of such firms. These include a high degree of centralisation of decision-making, a closed structure of ownership, a lack of formal operating procedures, intuition-based strategic management, and the absence of long term planning. Additionally, these firms manifest a high degree of intra firm vertical integration, few forms of collective action, and low levels of subcontracting. They tend to produce a wide variety of products and low volume of production, their sources of finance are erratic and costly, and they normally market to a restricted geographical area.

As economic reform intensifies, the role of SMEs will not diminish but increase. SME presence in the industrial structure of Latin America demonstrates that these firms are not marginal players. Although their productivity is significantly lower that of large enterprises, the gap has narrowed or closed in some countries. Since SME export very little, domestic macro economic conditions have been the principal determinants of how these enterprises have faired. The impacts of trade liberalisation have not escaped the SME sector, but the effects have not been generalised. Some SME sectors have been the winners, few others have
been losers due to their unwillingness to change to the circumstances or unable to face the challenges in competition.

In the large–market countries of Latin America, foodstuffs, textiles and apparel, chemicals and plastics, and machinery and equipment weigh heavily in total SME production. In all countries in the region, foodstuffs occupy an important place in SME production, due to the industry’s labour intensiveness and natural comparative advantages with low economies of scale. Given the fact that these two industries are aimed almost exclusively at the local market, domestic demand is far more important than trade liberalisation in affecting the competitiveness of these SMEs.

As for micro enterprises, their profile is distinct but not unrelated to that of SMEs. Among the principal features of these business-informal as well as formal- are that they are owner operated, employ 10 or fewer people, are financed out of personal savings, and have fixed assets of less than USD20,000. These small firms have a high percentage of female owners, depend on members on their family as workers, and have limited access to financing. Additionally, micro enterprise workers are not able to avail themselves of technical or management or business assistance services. For micro enterprises in the region, the many serious business challenges seem un daunting from complex tax and registration procedures to the lack of services. The four basic areas in which such obstacles are found are: the policy and regulatory environment, access to financing, access to business development services, and access of resources to the sector as a whole.

For every country in the region, access to capital ranks as the most serious barrier to business survival, let alone expansion, among SMEs as well as micro enterprises. Multilateral lending institutions and government have been involved in SME and micro enterprise lending for the past two decades. Commercial lenders are dedicating resources to this sector as well. In Mexico, companies and entrepreneurs can receive USD10,000 to 200,000 in loans to purchase raw materials, machinery, and other capital equipment. In Brazil, the nation’s largest bank, Banco do Brazil, offers its services through local post offices and supermarkets to target low-income customers, SMEs and micro enterprise entrepreneurs. Other banks, such as Bredesco, are considering to pursue similar strategies. The Chilean loan program will help SMEs train hundreds of thousands of employees.
THE INFORMAL ECONOMY

These businesses include, most prominently, street vendors and home workers, but run the gamut from building trades (electricians, carpenters, plumbers) to beauticians, mechanics, maids, and caregivers. One may say that underground activities are those that have legal ends but employ illicit means. That is, they are activities that do not intrinsically have a criminal content but must be carried out illicitly, even though they are illicit and desirable activities for the country. The most important characteristic of informal activities in that those involved in them directly as well as society in general benefit more if the law is violated than if it is not.

Small business, both formal and informal has been affected by the changing economic and political landscape in the Americas. Many firms have benefited from market liberalisation policies, trade opening, deregulation, and administrative reform; many others have been affected negatively, unwilling to change or unable to meet the challenges of increased competition from both within and outside the markets. Evidence to date indicates that there will be winners and losers from the ongoing process of globalisation and that SMEs will continue to play an important role in the economic growth and development of Latin America.

MULTINATIONAL FIRMS (MNEs) AND CORPORATE STRATEGIES

The 1990s will long be remembered as the decade during which Latin America experienced a major turnaround, in its economic orientation and undertook a major transformation to come into its own.

Following several decades of stagnation, countries throughout the region took decisive action to begin realising their immense economic potential. The reform programs initially adopted by Mexico and Chile and subsequently by Argentina, Brazil and several Andean countries, have enhanced the area’s investment appeal in the eyes of international investors. Consequently, Latin America has become a major destination for direct investment by many of the world’s leading multinationals. Out the world’s five largest emerging countries (Russia, India, China, Indonesia and Brazil), Brazil has covered the most ground in economic reform and is by far the most attractive business destination. Brazil’s role as the locomotive of Mercosur only reinforces its attractiveness.
Multinational Companies (MNCs) are uniquely well equipped to seize opportunities in the new, liberalised economic environment. Their global reach, capabilities, particularly technology, financial power, product design, range, quality, function and scale provide them with distinct competitive advantages vis-à-vis local firms. However, some multinationals are encountering internal obstacles in translating their global advantages into superior local performance—difficulties not uncommon to business entry in many emerging markets. As the new economic model of neo liberal reform dramatically altered the business landscape in Latin America, MNCs mobilised to commit to and actively pursue new ventures. Accordingly, these firms have designed and implemented strategies appropriate to achieving their objectives in the region.

Globalisation, national and sub regional policies, and new developments in virtually all industries and sectors have precipitated changes in the operating environment in Latin America. Existing competitive positions are shifting rapidly, and one clearly notes a long-term tendency towards a single universal market. The quest for international markets requires, first, an analysis of the structure of specific product markets, competitor analysis within those markets, the basis and form of technological change, and the impact of new international norms, such as World Trade Organisation (WTO) rules on trade, investment, intellectual property, services and agriculture.

During the 1970s in Latin America, government policies and positions toward foreign investment were generally restrictive. Two decades later, Latin American leaders and policy makers had done a 180-degree turnaround, recasting their view of MNCs to one of “engines of growth” and implementing measures to promote and provide guarantees to FDI and MNC operations. Consequently, there has been a flurry of bilateral investment promotion and guarantee achievements, interest in gaining access to the OECD (Organisation for Economic Cooperation and Development) multilateral agreement on investments.

The responses of MNCs have been varied, across industries, sectors, and countries. For existing affiliates, opening up national economies pits them against increased competition from imports and FDI inflows from competitors. The deregulation and liberalisation of government policy at a sector or company level changes their basic operating conditions. In essence, they are compelled to adapt their corporate strategies to the new environment. For
new entrants, new operating conditions combined with the sale of state-owned enterprises unleashed opportunities to grow and consolidate their international systems of integrated production.

The strategic motivations of MNCs have been to increase their access to natural resources and markets for manufactures, gain new access to markets for services, and improve the efficiency of their international systems of integrated production. In the case of new entrants, access to natural resources, through the liberalisation and deregulation of the mining and energy sectors have been the drivers.

For firms striving for greater market access in manufactures, their strategies aimed to adapt to the new competitive situation that derived from the opening of the national markets to increased import competition. These companies generally were ones that had existing operations in the Mercosur countries, mainly Brazil and Argentina. Rather than seeking to boost their business via exports, these firms were interested principally in defending their market positions, mainly by merging or acquiring prominent local firms in mature industries such as chemicals, food products, beverages, and tobacco.

The service sector is another area where FDI has been vigorous, especially since the sector had been off-limits prior to market opening reforms. New entrants predominated in this sector, taking advantages of opportunities in telecommunications and energy distribution, mergers and acquisitions, and financial services, especially banks, and particularly in Brazil. Other services that took off at this time included consulting, construction and engineering, law and accounting, logistics, and franchising. The vigorous expansion of MNCs in the region in the early 1990s centered on FDI aimed at boosting the efficiency of globally integrated production and distribution systems. An important component of this strategy was the restructuring of existing options to convert them into an export platform. The automobile industry in Mexico provides a good example, as well as newly created asset bases in auto parts, electronics and apparel.

Strategic asset seeking by MNCs in Latin America, especially in terms of research and investment to develop world-class technologies, did not weigh heavily as a factor in FDI strategies. However, in the future R&D in selected countries could become a driver. The public sector was the financial source and performer of R&D activities. Chile is dominant
competitor in Latin American R&D. The nation maintains three national funds that support basic research, applied research, and innovation in production.

Unquestionably, the two most important objectives of FDI in recent years have been improving the efficiency of their globally integrated systems of production and distribution and gaining market access for services by way of FDI. The importance of these objectives is attributed to the proportion of the total FDI inflows that they represent and the very significant trade flows produced as a consequence.

The automobile sector provides a vivid example of how FDI (through firms setting up new operations or restructuring existing ones) can improve the efficiency of globally integrated production and distribution systems. It is this sector where the biggest foreign firms by sales are found in the region, accounting for seven of the 10 largest foreign corporations by consolidated sales: General Motors-Mexico, Volks Wagon-Brazil, General Motors-Brazil, Chrysler-Mexico, Volks Wagon-Mexico, Fiat-Brazil, and Ford-Mexico. The case of Mexico is the best example of a country that has undergone a very significant transformation in the context of the globalisation process, especially in the automotive sector.

The globalisation of Mexico’s automobile industry had its roots in the 1970s when Japanese automobile producers began challenging the USA and European auto MNCs. By investing in lean production technologies, flexible organisation, defect prevention, and just in time delivery of inputs—not to mention fuel efficiency at a time of two global oil shocks—the Japanese auto MNCs came to pose a serious threat to USA and European competitors. The Big Three USA auto companies (GM, Ford, and Chrysler) assumed a defensive position through an offensive move: improving their competition in the USA market by establishing more efficient production facilities in neighboring Mexico.

The repositioning, in fact the transforming, of the USA auto companies was abetted by national policies in the United States and Mexico; new corporate strategies were developed to boost efficiency, sales, market share, and financial performance. Two principal elements were involved in corporate strategic responses: auto parts and vehicle assembly. By using production-sharing arrangements, USA firms could export components for assembly while the imported final product was charged tax only on the value-added (mainly wages). At the same time, Mexico vigorously promoted its maquiladora programme, offering tax-free
operations similar to export-processing zones. Taken together, this produced great cost reductions.

Mexico clearly saw the advantages in abandoning its previously restrictive national automobile policy and developing one aimed at facilitating the implementation of new export-oriented plants. This policy was complemented with NAFTA (North American Free Trade Agreement) provisions that gave preferences to USA auto producers in integration of the continental automobile industry. The regional (USA, Canadian, and Mexican) norms of origin (62.5% of production costs) in particular were influential in this respect. As a consequence of the synergistic policies of the USA and Mexican governments, FDI in the Mexican automobile industry by auto MNCs as well as their parts suppliers skyrocketed. This response, a reaction of the Big Three USA auto companies, led to the creation of world-class vehicle assembly plants in Mexico. During 1990-1996, the Big Three invested over USD5.5 billion in new plants in Mexico on top of considerable FDI during the 1980s.

By 1998, Mexico’s automobile industry was producing 1 to 1.5 million vehicles, and the Big Three were responsible not only for two-thirds of the production but more important for about 70% of the exports.

Chrysler and Ford exported over 84% of the vehicles that they produced in Mexico. The linkage between FDI and trade in auto MNCs operating in Mexico became one of Mexico’s principal means of integration into the international economy.

If one compares corporate strategies in Mexico’s automobile industry with Mercosur’s, sharp differences emerge. The challenges of international markets and new national and sub-regional policy packages forced firms to react by way of new corporate strategies-some phased out, selling their assets, licensing local firms, or shutting down all together. Others rationalised their operations; that is, without making major new investments, they tried to maintain their market shares by reducing operational costs through downsizing, streamlining, and so on. Some chose restructuring, undertaking major new investments to recast the role of the existing plants within the new global strategy of corporate headquarters, usually in terms of its international system of integrated production.
Affiliates of USA auto firms in Mexico chose the latter strategy; the response by Mercosur auto MNCs was quite different. The principal auto MNCs in the Mercosur market (Fiat, GM, Renault, and PSA) are mainly European. Interestingly, USA assemblers’ (Ford and GM) links are mainly to the European operations of their particular Head Quarter’s corporation. In the 1980s, in Brazil and Argentina most of these companies reacted by pulling back/pulling out (Renault and Fiat began to operate their local licensees in Argentina) or rationalizing productions (Ford and VW merged their operations in Autolantina until 1995).

When less competitive European and USA auto firms announced substantial FDI to improve the competitiveness of their operations in Mercosur, the reasons were “defensive”; they did not do so to establish export platforms. They were attempting to defend their existing Mercosur market shares. Recognisably, the Mercosur market possessed neither the geographical proximity to a major market, the capacity to produce labour-intensive auto parts in export processing zones, nor the same degree of liberalisation of deregulation. Additionally, they had relatively high levels of import protection for vehicles and high levels of obligatory sub-regional content. In essence, the impact on the local economy of the defensive FDI in Mercosur has not been as positive or far-reaching as the efficiency-seeking FDI in the Mexican automobile industry in terms of exports, balance of payments, and especially, the quality of the vehicle produced. A strategy that opted for the efficiency-seeking option in Mexico appeared to produce much better results than the market defense-based strategy in Mercosur.

As mentioned earlier, another objective of FDI is to gain market access for services, for example through the privatisation of electricity (generation and distribution) and telecommunications. Over half the FDI inflows to Latin America during 1995 – 1998 came about due to the liberalisation and deregulations of services. Although these inflows do not usually produce significant trade flows, the increased competition permitted by the new national regulations can have a significant impact on the overall structural competitiveness of an economy.

Although Brazil was not a major recipient of FDI inflows during the first half of the 1990s, by 1998 it had replaced Mexico as the primary destination of foreign investment. At the same time, manufacturing was edged out by services as the principal stock of FDI went to service sectors (56%). Those MNCs seeking market access did so primarily by purchasing existing
assets, via the privatisation programs in the electricity and telecommunications sectors or the private acquisition of banks and other financial institutions.

Admittedly, international market factors were not the principal motivation behind the FDI in services in Brazil; however, they were very important secondary factors. Market openings in Brazil provided opportunities for major players in other markets and new entrants within the region, as well as outside, to position themselves in Latin America. Multilateral agreements, such as the General Agreement on Trade in Services (GATS) relating to telecommunications and financial services enhanced the attractiveness of establishing a presence in the region. Although globally integrated operations are not a crowning feature of MNC competitiveness in the services sector, they can, in fact, provide advantages, especially in limiting the possibilities for expansion of competitors in two key sectors: telecommunications and electricity. Again, Brazil serves as a prime example. Laws were changed to permit foreign investment in previously reserved sectors. The liberalisation and deregulation of services in telecommunications, electricity and financial services, and retail commerce attracted huge inflows of FDI.

As Latin American nations and the companies operating there local, multinational and state-owned-strive to compete in the rapidly changing global environment, productivity will be paramount. During the 1990s, the region made progress in improving productivity; nevertheless, its performance, in the aggregate, vis-à-vis industrialised nations remains sub-par. In a Latin American labour productivity study by McKinsey, examining steel, food processing, telecommunications, and retail banking in the five largest economies (Argentina, Brazil, Colombia, Mexico, and Venezuela), researchers found productivity levels to be only around 30% of world-class levels in three of the four cases. (Only telecommunications boosted a much higher level). Disappointingly, the World Economic Forum’s most recent global competitiveness report reveals that with the exception of Mexico, these nations have actually experienced declines in productivity during the past five years.

Although economic liberalisation has had a hugely positive impact and productivity-inhibiting factors such as protectionism and over-regulation are disappearing, bureaucratic inertia, non-tariff barriers, and rigid labor rules are mitigating against greater gains in productivity. Recognisably, the productivity gap widened between industrialised nations and developing ones after World War II, with the former group’s widespread and faster-paced
adoption of new methods of work organisation, technology, and production methods. Still, the productivity gap is not uniform but varies across industries and within sectors. For Example, in petroleum refining and oil derivatives, Latin American performance approximates that of the United States and Europe. Moreover, given the fast cycle life of information and production technologies, a number of Latin American sectors and industries can make quantum leaps from systems that were obsolete decades ago to state-of-the-art systems.

While the transfer of technology and know-how to Latin America and significant financing and investment are essential for nations and firms to improve their productivity and competitiveness continuously, they are by no means the most determining factors. In fact, in a study of Brazilian productivity, researchers found that under-investment in technology did not account for a large part of the gap; a large portion of the gap, about 35 percent, could be closely by improving the way work is organized, and another 30 percent by making modest capital improvements with payback periods of less than two years. Simply to optimise existing processes without investing any new capital would increase GDP growth by almost 2 percentage points.

Countries and firms that need these lessons are sure to experience marked gains in productivity. As globalisation spreads and intensifies, they will need to do so merely to hold their own, let alone achieve a sustainable competitive advantage vis a vis their competitors, domestic as well as foreign.

This is the current business landscape in Latin America, one fraught with both challenges and opportunities for multinational firms, their suppliers and financiers, and for governments in the region and the vast majority of consumers. The globalisation process is accelerating neo liberal economic reforms, including trade, investment, and financial liberalisation and the deepening of regional and sub-regional integration. Multinational firms in key sectors of the economy are positioning themselves to maintain and expand their competitive advantages through the development of networks, technology, and management savvy. They will also need to concentrate simultaneously on three key, interrelated disciplines: the design of the organisational structure; management processes for allocating resources and measuring/rewarding performance; and the culture, values, and behavior espoused.