Chapter 3: Business for Development

Multinationals, telecommunications and development

Foreign direct investment (FDI) flows have stepped up dramatically around the world since the mid-1980s. In Latin America, the 1990s were a period of accelerated FDI inflows, led by the entry of developed-country multinationals into newly privatised or liberalized sectors.

The real change, however, is not in the game but in the players. Of worldwide FDI stocks, the share emanating from developing countries has increased by half, growing from 8 per cent in 1990 to 12 per cent in 2005. Latin American enterprises now also play away from home. Since 2006, the value of annual outward FDI flows from the major countries in the region has flirted with the $40 billion mark. This explosion of outward investment is largely the result of the rapid internationalisation of a small number of large enterprises, mainly from Brazil and Mexico. Indeed, in 2006, Brazil was a net source of FDI, with outward flows amounting to $26 billion, as compared to inflows of $18 billion.

The largest Latin American multinationals are in primary commodities and related activities; Mexico's cement producer, CEMEX, and Brazil's Petrobras, in oil, and Companhia Vale do Río Doce (CVRD), in mining, are important examples. Services and final goods have also become key areas of multinational activity by Latin American firms, first regionally, and now, for a small number of very successful enterprises, globally. While these firms' multinational growth reflects diverse corporate strategies, scopes and ambitions, it places Latin America firmly on the new global map of home countries for multinational corporate activity.

The telecommunications contribution

The telecommunications sector is at the crossroads of these new trends in multinational investment. While several multinationals from Europe and North America entered the sector aggressively in Latin America during the region's privatisation and liberalisation period in the 1990s, consolidation and competition have given the upper hand amongst these firms to Spain's Telefónica. Since 2000, successful expansion within the region by Mexico's América Móvil and its sister company Telmex has in turn created a formidable new regional competitor for Telefónica. The role of these two multinationals from opposite sides of the Atlantic, who now dominate telecommunications in Latin America, sheds valuable light on the contribution of multinational enterprise to sector-specific and broader economic development in the region.

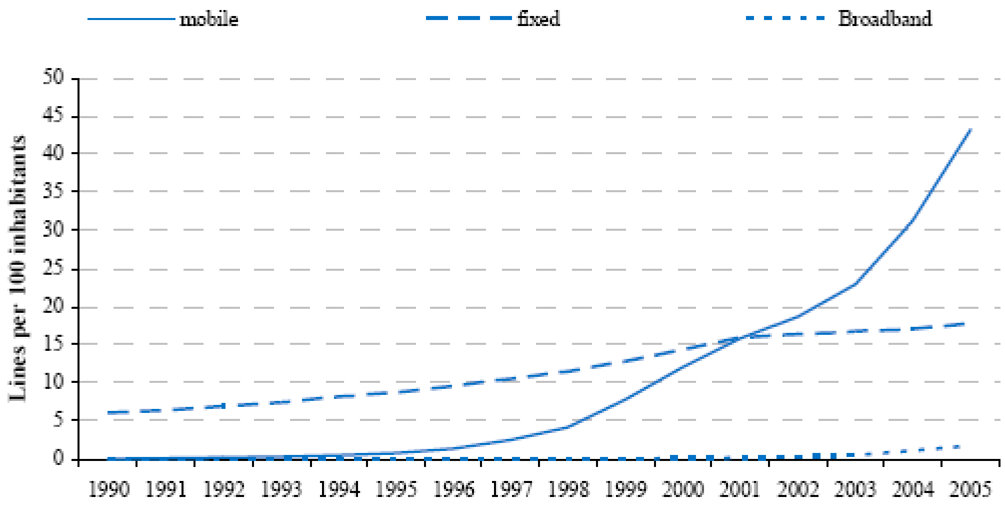
Telecommunications contribute to the economic performance of countries as a whole because of the importance of the services they provide. By increasing the availability and speed of information flows to a broad range of potential users, the sector can transform both economic and political life. For the sector to play this transformational role, however, much depends on the extent of its coverage of the population and the degree of access it provides to different segments of the population. It is precisely in its impact on coverage and access that FDI in telecommunications has played a transformational role in Latin America.

Since privatisation started in the region at the turn of the 1990s, cumulative FDI flows in the sector — including the entry of foreign enterprises through privatisations, capital expenditures and the establishment of new mobile operations — have exceeded $110 billion. FDI in this sector has thus been a major source of Latin America's total FDI inflows. Equally important is the fact that in such non-tradable services as telecommunications, where responsiveness to local conditions is crucial for success, multinational investors have pursued strategies adapted to individual host countries ("multi-domestic strategies") that have in turn generated significant employment and fiscal revenues in host countries.

FDI in this sector has also helped bring about the rapid progress of connectivity in Latin America. Telephone density (lines per 100 inhabitants) has not only increased significantly: it has increased most where the sector has received the most FDI per capita. Figure 4 shows the impressive speed at which mobile telephony has spread in the region since the late 1990s. The growth in landline density is also significant, especially during the 1990s, although it has visibly slowed since then (and at 18 lines per 100 inhabitants, remains far below universal service). By 2005, the region thus attained a combined teledensity of 61, above the world average of 54, and well above South Asia's 12 for example (although still a long way from average levels in OECD countries of 130).

Figure 4. **Mobile, Landline and Broadband Penetration**

Latin America population weighted average

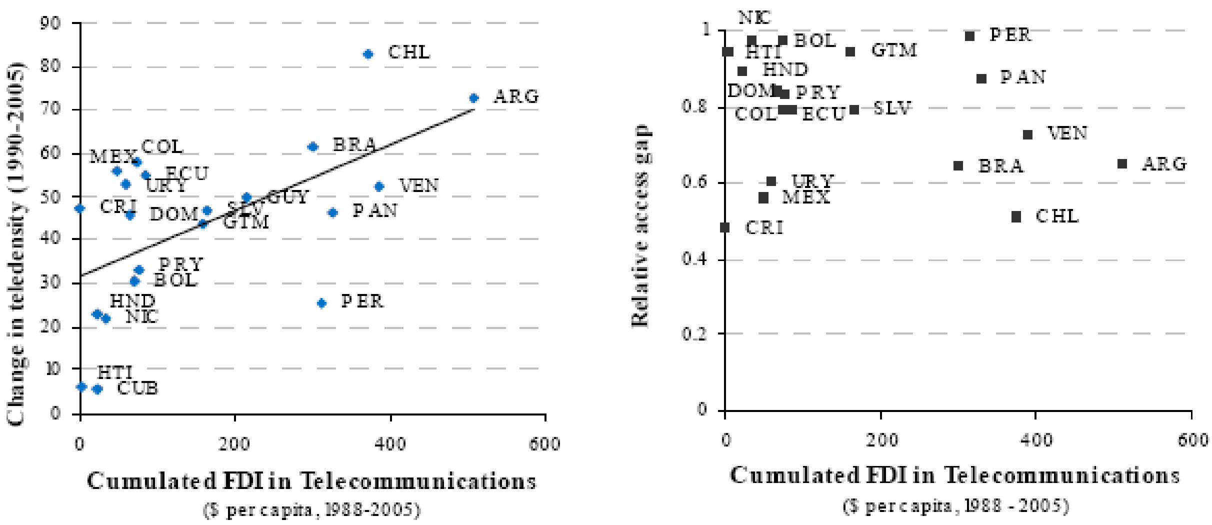


Source: OECD Development Centre (2007); based on ITU (2006) data.
StatLink http://dx.doi.org/10.1787/121327185628

Privatisations, sizeable flows of market-seeking FDI and competition amongst investors in the sector have combined to play a key role in bringing about this growth in connectivity. Also important has been the rapid spread of mobile technology — sizeable investments have gone into telecommunications infrastructure, especially linked to the spread of mobile technologies — together with process innovation (e.g. pre-paid phones) and regulatory innovation (e.g. calling-party-pays charging). Figure 5 confirms that teledensity has increased the most in countries that have received the most FDI per capita in the sector.

Figure 5 also shows, however, that this impressive growth in connectivity has not significantly lowered the access gap between the rich and the poor in most countries of the region. The increase in service initially benefited mostly the better-off, while the poor remained underserved. Inequality — as measured by the difference in the proportions of rich and poor people who have telephones at home — remains high. For the region as a whole, an individual in the highest income quintile is more than three times more likely to have a phone than one in the lowest income quintile.

Figure 5. **FDI Impact on Telecommunications Outcomes**



Source: OECD Development Centre (2007); based on ITU (2007), IADB (2007), SEDLAC (2007) and World Bank PPI Database (2007) data. 12http://dx.doi.org/10.1787/121701322488

The importance of regulatory frameworks

In countries with a particularly dynamic telecommunications sector, such as Brazil or Chile, some reduction in inequality occurred more recently (e.g. a rich Brazilian was 10 times more likely to have a phone than a poor one in 1997, but only 2.5 times by 2004). Contributing to this reduction in inequality have been moves by government regulators in these countries to supplement market mechanisms in the telecommunications sector with universal-access obligations on incumbent suppliers, or to constitute funds for the promotion of universal access. Chile's innovative project-selection mechanisms are an important example.

The most successful regulatory models for telecommunications in Latin America, in terms of increasing coverage and simultaneously lowering inequality of access between rich and poor, have ensured competitive behaviour in the sector through careful but determined regulation. While the performance of public monopolies ranges from good to dismal in countries where those monopolies still exist, even the better performers are less responsive to the new opportunities offered by mobile technologies. The privatisation of those same monopolies or the granting of long exclusivity periods to incumbents, as in Mexico, Nicaragua and Peru, while attractive in terms of revenue generation, has created uncompetitive markets that are seriously underperforming for users, especially in landline coverage.

The gap in access to telephone services between rich and poor thus remains substantial in most countries in the region, and while the provision of voice service can go a long way towards strengthening social ties and increasing mobility, it is only the first step in bridging the communications and digital divide between rich and poor. Undeveloped telecommunications networks will also remain a bottleneck for broadband access, notwithstanding the value of communal approaches to providing internet access, which are helping internet services outpace landline expansion.

The bottom line is that the spectacular progress of mobile telephony constitutes an important opportunity to reach (including through mobile banking) major segments of Latin America's population hitherto largely excluded from productive integration into the modern economy. Only a regulatory framework that ensures contestable-market behaviour by the suppliers of telecommunications services can ensure the affordability of those services for large numbers of poor households and small enterprises. The combination of such a regulatory framework, technological innovation, and competition by multinational investors for local consumers holds a significant potential for enhancing the productivity and living standards of large numbers of people.