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the financial transfers within the Community overt and intelligible, the more so as the financial flows under the guise of financial solidarity in agricultural policy are *by no means conducive to a genuine reconciliation of interests* but warrant fears that the Community will have to cope with greater strains and stresses in future. The supporters of European integration have a special reason to work for a change in the agricultural policy lest the much applauded linchpin of the Community turns into a means for its destruction.

### To Sum Up

Nobody can at this juncture present ready-made proposals for a forward-looking agricultural policy. The immediate task is to consider what may happen if the present policy is continued and to look for vantage-points for a new approach. This certainly necessitates a journey into unknown territory. We cannot hope to move into the kind of predetermined agricultural world of full har-

mony into which Mansholt entranced us. It is our job to carry on the development of the agricultural structure which has come down to us as part of the foundation of our European civilisation and in doing so keep the larger social implications before our eyes. Just as we were unable to foresee all our present problems twenty years ago, so we cannot expect to perceive today all the factors which will determine the developments in coming decades. There is all the more reason therefore to make our agricultural policy — the market policy in Brussels as well as our structural policy — *flexible and adaptable*.

There is not much time to lose if the danger to our rural regions, the threat of economic losses and the risk to European integration are to be averted. Please regard these my remarks not so much as criticism but as *suggestion for a discussion* in which we all have the same aspirations for the development of our rural areas and the future of the European Community.

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## The Decay of the Andean Group

Sven Heldt, Kiel \*

**The creation of the Andean Group in 1969 and its ambitious program had been accompanied by optimistic expectations of its members who now have become disappointed. Regarding the conflicts within this Group the withdrawal of Chile plays a prominent part — a withdrawal which will probably have negative effects on this country, but also for the rest of the Group it represents a painful shrinkage.**

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**T**he creation of the Andean Group in the year 1969 by Bolivia, Chile, Colombia, Ecuador and Perú<sup>1</sup> was the result of the difficulties encountered within the Latin American Free Trade Association (LAFTA), due to a lack of common interests and an insufficiency of instruments designed to prevent an unbalanced distribution of the benefits expected from the integration process. It were therefore those members of LAFTA classified as having restricted markets<sup>2</sup> or whose economies were relatively less developed<sup>3</sup> that principally showed interest for a change. They were convinced that only through the creation of a close economic unit it would be possible to counterbalance the economic weight of the remaining three big members within LAFTA, namely Argentina, Brazil and Mexico, and by this way facilitate

the integration of the whole Latin American region. The essential objectives of the Andean Group were therefore defined as follows: to reach a persistent improvement of the standard of living of the inhabitants of the subregion through a process of economic integration leading to a balanced and harmonic development of the partner countries, to facilitate its participation in the process foreseen by the Treaty of Montevideo and to establish favourable conditions for the conversion of LAFTA into a common market.

The strategy of subregional economic integration of the Andean Group provided measures to be executed by specific instruments and within a fixed timetable that would touch almost every field of the economic life of the partner countries. These basic mechanisms were a harmonization of the economic policies of these countries, a common agricultural and industrial programming, the liberalization of the reciprocal trade, the adoption of a common external tariff, special measures designed to reduce the differences in the level of economic development between the partners,

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<sup>1</sup> Venezuela adhered only in the year 1973, although it participated in the initial negotiations.

<sup>2</sup> This group of countries comprises Chile, Colombia, Perú and Venezuela.

<sup>3</sup> The relatively less developed countries of LAFTA are Bolivia, Ecuador, Paraguay and with restrictions also Uruguay. But only Bolivia and Ecuador are members of the Andean Group.

the canalization of financial resources and the physical integration.

### **Special Features of the Andean Group**

The Andean integration scheme was characterized by special features like the establishment of a common treatment of foreign investments, trade marks, patents and licenses and the harmonization of economic policies as a special tool for establishing a preferential treatment towards the relatively less developed members, Bolivia and Ecuador. By the first of these measures it was intended to secure that the potential benefits generated by the integration process would be retained in the area. The purpose of the second was to distribute them adequately among the members. An additional instrument, the sectorial industrial programming, was designed for predetermining the production location of a fixed list of products, therefore subcontracting the decision of where to produce from the market mechanism. By this way, the specialization of the partner countries in certain product lines was to be determined by the way of negotiations.

These unusually far reaching measures adopted by the Andean countries were only possible as a result of a strong commitment of the governments of the participating countries in favour of regional cooperation. The leading personalities of that time were the presidents of Colombia and Chile.

When the agreement was signed in 1969 and during the first years of functioning the governments in power were characterized by strong nationalistic attitudes<sup>4</sup>. The majority of the member countries, namely Bolivia, Ecuador, Chile, Colombia and Venezuela were following a traditional development strategy, with priority for industrialization through an import substitution process under intermediate levels of protection. Perú, on the other side, favoured a planned development strategy, where the integration was thought as a vehicle for a national autonomous development. According to this strategy the trade liberalization process within the region received less importance compared to the regional industrial programming under relatively high and differentiated tariffs to develop strategic industries, reserving for the foreign capital a restricted and regulated role. This position received additional backing when President Allende assumed power in Chile in 1970.

### **Economic Implications of the Integration Instruments**

The effects of a trade liberalization program like that of the Andean Group upon the individual partners depend basically on the degree of in-

dustrial development of each country, the size of the import coefficient and the dependence of the State on tariff revenues. The liberalization process is then most favourable for those countries which can successfully reduce the production costs through economies of scale and a better allocation of production resources. The size of the import coefficient is decisive for the immediate possibilities to export to the regional market, a low coefficient being an indicator of an advanced import substitution process. Countries with a high import coefficient might therefore be forced to import now goods from partner countries which they formerly imported from third countries most probably at a lower cost. This development has an impact on the tariff revenues of the State, depending upon the degree that the subregional imports substitute third country imports or national production. According to these considerations the potential benefits of the liberalization process were expected to be greatest for Colombia and Chile<sup>5</sup>.

The setting of a common external tariff determines the general incentive given to the production destined to the subregion and indirectly also determines the stimulation granted to the exports going to third countries. The structure of this tariff decides upon the relative protection given to the different types of products. The bigger the similarity of the present tariff level and structure of a member country to that proposed for the integration community, the bigger will be its benefit from it. According to the minimum common external tariff already adopted, Colombia was closest, while Bolivia and Ecuador had practically no benefit. Their national tariffs on manufactured goods were significantly lower than the common tariff showing almost no home production in intermediate, capital, and some durable consumer goods. The latest proposition of the Junta of the Treaty of Cartagena for a definite common external tariff structured according to the labour intensity of production and fixing lower rates is, therefore, a more acceptable solution.

In relation to the joint regional planning of dynamic industries, it is important to avoid that foreign competitive pressures are completely eliminated so to prevent excessive regional costs for these industries. It is, therefore, a question of the price the Andean countries are willing to pay for having a more diversified industrial structure, since inefficiencies in these industries, especially

<sup>4</sup> Specially the presidents Allende in Chile, Torres in Bolivia, Velasco in Perú and Rodríguez Lara in Ecuador.

<sup>5</sup> The intra-subregional trade has developed very dynamically, from US \$ 86 mn to 468 mn between 1969 and 1974, but still represents only about 6 p.c. of the total foreign trade of the region. Chile and Colombia have maintained their share of about 55 p.c. in total regional exports in this period, if we subtract the exports of crude petroleum of Ecuador in the year 1974, which started to grow dramatically.

in intermediate and capital goods industries, will affect the efficiency of all other Andean industries that need these products as inputs. Coupled with this question arises the problem of a fair distribution of the new industries among the partner countries, since inefficient infant industries will be to the benefit of those countries where they are located at the expense of the other partners, as long as the exporting country does not subsidize these exports by the amount of the higher production costs. And this conflicting situation will persist until these new industries mature and thus make regional protection superfluous. In order to avoid this risk, regional import substitution should then only be promoted in those activities where acceptable levels of efficiency through learning by doing can be reached after a reasonable number of years.

If costly trade diversion arises for those countries which have traditionally had lower levels of protection (Bolivia, Ecuador and Venezuela) attempts to offset this disadvantage by locating inefficient investments in these countries in the framework of regional industrial programming will not encourage growth in the subregion. In effect, the Andean subregion needs an expanding volume of exports to the rest of the world for guaranteeing a rapid and efficient growth and, consequently, for financing a rising amount of imports of capital and intermediate goods whose production in the subregion may still be uneconomical<sup>6</sup>.

### Differing Aspects of Foreign Direct Investments

With respect to the role of foreign direct investments (FDI) opinions are very divergent as to the benefits they may bring to the host countries. The common measures toward FDI adopted by the Andean Group<sup>7</sup> actually reflected a rather sceptical view of these benefits. They comprised a limitation for the remittance of profits up to a maximum of 14 p.c. of the invested capital per annum, a forced divestment policy within a period varying between 15 years for Chile, Colombia, Perú and Venezuela and 20 years for Bolivia and Ecuador, a prohibition to invest in certain sectors like transport and communications, limited access to domestic credit, the elimination of prohibitive export clauses, limitations for licensing agreements, a prohibition for the acquisition of existing industries and others.

These rules were the reflection of the results of some investigations undertaken by that time in Latin America to measure the effects of direct foreign investments<sup>8</sup>. They supported the conviction of many politicians and technocrats that these effects were in many cases negative. It was, nevertheless, not intended to cut the flow of FDI, but to control it and direct it to those activities

where economic benefits were expected, the rationale being the sharing of the rents originated by the creation of the common market.

The promoters of FDI commonly stress the following benefits: positive employment effects, transfer of technological knowledge and managerial skills without lengthy negotiations, a rapid transfer of capital to capital-scarce regions, positive balance of payments effects through either export promotion or import substitution, the introduction of new products, the achievement of economies of scale and the stimulation of additional domestic investment through forward and backward linkages.

But in fact one can find on account of numerous examples a quite different picture, the employment effect being quite limited due to the utilization of rather capital intensive technologies<sup>9</sup>, the remittance of profits being excessive and channelled through the way of transfer pricing for inputs coming from the parent firm, the net inflow of new capital being reduced, since the greater part of the investments is commonly financed by the reinvestment of local profits and local credits, the payment for patents being excessive, registering even payments for not utilized technologies, the net effect on the balance of payments being rather weak on account of high import contents in import substituting activities and weak export promoting effects, which even in successful cases tend to increase dependency on export markets<sup>10</sup>, the introduction of new products tending to satisfy the limited demand for conspicuous goods of the high income classes and thus preventing the achievement of economies of scale.

On top of it, a conflict of interests was visualized between the host country and the foreign investor mainly due to the fact that foreign investors follow policies that tend to maximize the benefits of the whole multinational company, not always leading to the maximization of the benefits of the particular subsidiary. Although the defenders of an international *laissez-faire* system point out that the negative experiences with FDI are the result of the application of wrong economic policies in the host countries, the experience in the Andean countries does not confirm this in numerous cases.

<sup>6</sup> The only tariffs that can be so far considered as rather high are those fixed for some productions assigned to Bolivia and Ecuador and those under discussion for the automobile industry.

<sup>7</sup> The common rules toward foreign direct investments are contained in Decision 24 of the Commission of the Treaty of Cartagena, adopted as early as 1971.

<sup>8</sup> See f.e. C. Vaitzos, Patents revisited: their functions in developing countries, in: Journal of Development Studies, Vol. 9, Oct. 1972, No. 1, and Intercountry income distribution and multinational enterprises, Oxford 1974.

<sup>9</sup> This tendency is supported by distorted factor prices for labour due to minimum wage legislation and other measures.

<sup>10</sup> See H. W. Valle, Las industrias de exportación, in: Desarrollo Económico, Vol. 14, No. 54, July-Sept. 1974.

The Common Foreign Capital Statute was, therefore, designed to prevent these negative effects as well as to improve the bargaining position of these countries vis-à-vis foreign investors, seeking to attract only those investments that are in accordance with the national interests of the host country. For this purpose, the external tariffs and the direct allocation of industries to particular countries according to the sectorial programs of industrial development (SPID) are important additional tools. In exchange for the restrictive clauses, stable investment rules, a guarantee against unforeseen expropriations and an expanded protected regional market were offered to potential foreign investors. It was then a question of how foreign investors would react to these unprecedented behaviour of a group of countries, how powerful their lobby would be in an attempt to liberalize these rules and how attractive the Andean market would be for investors in relation to alternative investment opportunities.

A complement to Decision 24 on the regional basis was Decision 46, which provided a uniform regime for the creation of regional multinational companies and common rules for the treatment of subregional capital. There, capital coming from the subregion is treated as being national and not subject to the restrictions for foreign capital<sup>11</sup> and projects where cost, magnitude or technological complexity surpass the possibilities of a single country are encouraged through the creation of regional multinational companies. These would commonly take the form of public Andean enterprises.

The Andean multinational enterprises could at least partially replace extraregional transnational companies and they would be closely related to the sectorial programs of industrial development where import substitution on a regional scale was planned in such sectors as important as metal working, chemical products, petrochemicals, fertilizers, automobiles and electronics.

Through the creation of these companies it was also hoped to help the relatively less developed members, Bolivia and Ecuador, to utilize the special customs concessions and to build up factories under the sectorial programming agreements. But it should be kept in mind that through the creation of Andean multinational companies the errors committed at the national level with import substitution policies are not repeated at an international level and under the cover of integration and joint enterprises<sup>12</sup>.

### Changing Political and Economic Conditions

The ambitious program of the Andean countries needed a strong political leadership and a high measure of consensus and solidarity to advance

significantly. And this was not present anymore when important political changes had occurred in almost every member country and the new political leadership realized the implications of the Treaty of Cartagena for the new economic policies followed thereafter by some of them.

The most important event was the overthrow of the Allende-government in Chile in September 1973, after President Torres of Bolivia and President Rodríguez Lara of Ecuador had also been replaced by conservative military governments. Thereby the nationalistic element strongly present in the first years after the creation of the Andean Group, favouring industrial programming and strict control over foreign investments, was decisively weakened. Further, the conditions in the world economy have radically changed, reversing the political interest in favour of the primary sector. In view of a growing scarcity of these goods, a tendency towards the formation of cartels of primary products producing countries developed including some of the countries forming the integration community. And finally, the admission of Venezuela to the Andean Group changed the dimension of the Community through its enormous oil wealth, providing it with a strong financial power seeking a corresponding political influence in the subregion.

### Conflicts within the Andean Group

The adoption of an extremely liberal economic policy by the military government in Chile signaled the beginning of serious conflicts within the Andean Group. Chile began to contemplate regional integration as a second best, favouring low and uniform common external tariffs, giving preference to the market mechanisms for the assignment of resources and behaving sceptical about the SPIDs and finally adopting an ideologically founded position against any regulation for FDI. This behaviour was, therefore, in strict opposition to the nationalistic spirit of the founder years of the Andean Group.

First difficulties arose when Chile promulgated in the year 1974 a decree (Decree-law 600) pertaining FDI which secured no discrimination against foreign investors and which was in contradiction with the most important provisions of Decision 24. Only the strong and close opposition of the other member countries, specially in view of the fact that Chile would be in a better competitive position to attract foreign investors by having adopted more liberal measures, that even

<sup>11</sup> The rules pertaining to the transfer of capital remain subject of each individual country.

<sup>12</sup> For example the joint public enterprises Monómeros Colombo-Venezolanos have been facing continuous difficulties. See C. F. Díaz Alejandro, *Inversión extranjera directa por latinoamericanos*, in: *Integración Latinoamericana*, Vol. 1, No. 4, July 1976, p. 8.

gave MNCs a more favourable treatment than national enterprises, forced Chile to promulgate a second decree (Decree-law 746) securing the full implementation of Decision 24. In exchange for it, a discussion about Decision 24 was foreseen, specially about those subjects pertaining to the repatriation of benefits and the fading out principle, as well as about the problem of the big differences in the application of these rules in the individual countries, which diminished the effectiveness of this mechanism to create a stable investment climate.

In fact, the problem of interpreting the clauses and concepts of Decision 24 uniformly was acknowledged by the Junta of the Treaty of Cartagena as early as 1972, but the discussions about its harmonisation were interrupted and delayed first by the constitutional crisis in Colombia in 1972, later by the entry of Venezuela in 1973 and finally by the submission of the controversial Decree 600 by Chile in 1974.

In the meantime the deadline (December 1975) set for implementing a common external tariff and such important industrial programs as petrochemicals and automobiles was fast approaching. The discussions encountered serious difficulties on account of the Chilean desire for freer trade and as by the end of 1975 only an agreement for the petrochemical industry could be reached, after the first one on metal-mechanical industries was signed in 1971, and the election of a new three-man Junta, also due for that time, had to be postponed by another six months, the Andean Group faced its gravest crisis.

Intense negotiations ended in April 1976 with a compromise (Decision 100) in the form of a protocol modifying the Treaty of Cartagena. Thereafter, agreements on products to be included in the industrial programs and the implementation of the common external tariff were postponed by two years to 1977 and the trade liberalization process between the partners was extended by two years till 1982, reducing the annual tariff cuts from 10 p.c. to 8 p.c. Also the unanimity rule in the decision making pertaining to industrial programming was abolished, so that now only four members were needed to implement such a program unless no other partner categorically vetoes it, the non-signatory members having the option to join the program in the future. While the slowing down of the trade liberalization program was a concession on the part of Chile and Colombia, which were in favour of a rapid tariff cutting, the reform on the side of the industrial programming was a concession of the other partners particularly toward Chile. Finally, an additional decision authorizing the Chilean Government to sell public sector companies to foreign

investors legitimized the Chilean policy followed so far and signaled that the region was ready to be flexible in the discussion about foreign investments.

So far the crisis seemed to be overcome. But when the XX ordinary session period of the Commission of the Treaty of Cartagena took place in August 1976 in Lima, Chile was the only country that did not sign the protocol modifying the Treaty on the ground that an agreement on the reform of Decision 24 should be reached first. The expected division of the member countries in two opposed groups did not become true and Chile was confronted with the united front of the other five partners who gave it a time limit of 60 days to sign the protocol.

In the meantime the other five partners met in Colombia, where they discussed a loosening of the rules concerning foreign investments as a gesture of good will toward Chile. The so-called Sochagota Declaration provided that capital coming from Andean partners and other Latin American countries should be considered as national for the classification of industries, that capital coming from international organizations be classified as neutral, that the remittance of profits be increased from 14 p.c. to 20 p.c. of the invested capital annually and that the automatic reinvestment limit be widened from 5 p.c. to 7 p.c. Also the upper limit for the external tariff was fixed at about 80 p.c.

But these results were not enough for Chile, since it was asking full liberty for the transfer of profits and a limit for the common external tariff between 10 p.c. and 30 p.c., stating its unwillingness to finance further protection for the regional industry. The negotiations went on, and it was proposed to offer Chile a leave period of about two years from the obligations of the Treaty. Finally on October 5, the six members constituted a special commission to elaborate rules for a settlement of the problems. It was agreed that if till October 30 no agreement could be reached, Chile would withdraw from the Andean Group and this was what happened. Only those particular agreements pertaining to double taxation (Decision 40), Andean multinational enterprises (Decision 46), international traffic agreement (Decision 56) and road network in the Andean region (Decision 94) were to remain in force.

#### **Motives for the Chilean Withdrawal**

One may ask about the motives Chile had to revise its position with respect to foreign investments in the year 1974 (Decree-law 600) and to adopt such a firm standing against the position of the other five partners in the year 1976. Did it hope for support from at least one partner or had

the economic and political conditions improved so much that a possible withdrawal from the Andean Group could be risked or even wanted?

In favour of the first supposition speak the words of President Lopez Michelsen from Colombia shortly after the Declaration of Sochagota, who expressed understanding for the position of Chile and proposed fundamental changes in the rules pertaining to foreign investments and in the common external tariff, as a way to solve the conflict. In favour of the second supposition speaks the slowly improving economic situation of Chile, especially reflected in better international payment conditions and in rising exports of non-traditional goods to third countries. But more than this, it was the consequent following of economic ideas leading to a better use of comparative advantages on a world scale and away from a model of accelerated industrialisation that determined this decision<sup>13</sup>. These ideas embodied, consequently, free access for foreign capital to the Chilean market and low protective barriers.

A closer cooperation with the countries of the southern zone, especially Argentina and Brazil, which also corresponds more to the geographical location and the traditional trade flows of Chile, and the fact that only about 20 p.c. of the exports going to the Andean market were subject to customs preferences, were additional official arguments. This would imply that the bulk of the trade with the Andean countries would take place anyway in the future without any preferential agreement. But looking at the figures<sup>14</sup> one can see a quite different picture, namely that of the Chilean export increase to the Andean partners between 1969 and 1974, nearly 60 p.c. was covered by products included in the automatic liberalization list and that in the year 1974 nearly 74 p.c. of the products exported were manufactures. Consequently, one can legitimately expect that as a result of the withdrawal from the Andean Treaty it will be the exports of manufactures with preferential access to the Andean market that will be most seriously affected<sup>15</sup>. In 1975 the exports to the Andean countries increased by another 40 p.c. and it can be assumed that the export pattern did not change.

Compared to the total exports of manufactures, those going to the Andean countries still played a minor role (1974: 19 p.c.) and this relation was

<sup>13</sup> The Economist described the division of the Andean Group as follows: "The gangrenous limb of a Chicago-university-advised Chile has fallen off the Andean Pact", The Economist, London, Nov. 13, 1976.

<sup>14</sup> See Junta des Acuerdo de Cartagena, Evaluación de la marcha del proceso de integración, March 1976, published in: Integración Latinoamericana, Vol. 1, No. 5, Aug. 1976, tables No. 4 and 6, p. 68-69.

most probably maintained during 1975, since total manufactured exports increased by almost the same rate as the exports to the Andean Group. But if we take into account the dynamic evolution of the trade exchange within the Andean Group and considering the prospects for developing key industrial sectors by the way of industrial programming in a more efficient way, one may come to the conclusion that the potential benefits forgone are not negligible.

It is true, that the traditional trade connections with Argentina and Brazil are far more important than those with the Andean countries<sup>16</sup> and they should continue to receive high priority. This is intended through a closer participation in the River Plate Basin System<sup>17</sup>, by bilateral agreements with these countries as well as through a stronger participation in the complementarity agreements of LAFTA. The question is, if this strategy would have necessarily been in conflict with a participation in the Andean Group. And the answer is no, since we have the example of Bolivia, which is member of both communities.

#### Negative Effects of Chilean Decision Probable

Even thinking about the proposition for a common external tariff of up to 75 to 80 p.c. which Chile rejected with the argument of bearing too high levels of inefficiency, we can see that countries like Brazil or Argentina, with relatively wide domestic markets and good export performance, have external tariffs also ranging around 80 p.c. in many cases. Therefore, the Chilean withdrawal cannot be founded on these arguments, taking into account that those sectors, where Chile has comparative advantages on a world scale, are limited, e.g. mining, forestry and related industries, food processing and temporarily some labour-intensive production processes on account of the depressed real wage level.

Considering the bulk of the export potential, the two most important sectors, namely mining and forestry, were subject to exceptions in Decision 24 so that for these sectors no restrictive rules were foreseen for foreign investments. Also banking and insurances were eligible for more

<sup>15</sup> Colombia recently (February 2, 1977) introduced customs tariffs for the traditional agrarian exports coming from Chile, with the effect of increasing on the average the prices by 20 p.c. in the Colombian market for these products. Consequently, the export volume is expected to decline in the future.

<sup>16</sup> In 1974 the exports to and imports from Argentina and Brazil amounted to US \$ 169 mn and US \$ 324 mn, and US-\$ 144 mn and US \$ 85 mn respectively, compared to exports of US \$ 59 mn and imports of US \$ 166 mn for the Andean region, excluding Venezuela.

<sup>17</sup> This community was created in the year 1969 by Argentina, Bolivia, Brazil, Paraguay and Uruguay and focuses on the common use of the resources of the River Plate Basin as well as on projects of common interest.

favourable treatment and foreign investments in those activities exporting more than 80 p.c. of their production to third countries were also not subject to restrictions. Therefore the other important argument that Decision 24 hinders the flow of foreign capital so much needed for the economic development of Chile would only apply to food processing and some labour intensive processes, since investments in chemical, petrochemical or metal working industries would be uninteresting without the access to the Andean market and without a certain degree of protection. Further, the Comité de Inversiones Extranjeras approved between October 1974 and May 1976 foreign investments totalling US-\$ 314 mn, while between 1964 and 1973 investments to the amount of only US-\$ 261 mn were registered. In the other Andean countries it was also observed that the flow of FDI continued, showing even an increase in comparison to the past <sup>18</sup>.

While the major part of the newly approved foreign investments in Chile went into the mining sector, a considerable amount was in chemical, petrochemical and metal working industries, where despite the restrictions imposed by Decision 24 they were attracted by the access to the Andean market. Unless industrial cooperation agreements are signed between Chile and other countries of the La Plata Basin, these investments run the risk to be lost and it is difficult to say if they can be compensated by others in those sectors where Chile has a comparative advantage. Investments destined to the national market are at least in the short run also unlikely on account of the depressed market situation.

The loss of the Andean market will also affect very strongly some existing industries in the metal working sector which already depend very highly on the subregional exports. One way to tackle this problem is by going into the Andean market using the open door of the Andean multinational companies (Decision 46), replacing trade flows, with the result of losing working places in Chile, where the unemployment rates are running at high levels. Further, Chile will be getting in the future only limited financial resources from the Andean Development Corporation (CAF), which was founded by the six Andean countries in the year 1968 to support the integration effort <sup>19</sup>.

On the balance, adding the loss of influence on political and economic matters within the sub-

region and through its participation as a group vis-à-vis third parties, one may be inclined to say that the Chilean decision will have negative effects. Through the participation in the Andean Group Chile was also linked to the only two remaining democracies of South America, Colombia and Venezuela, and to its neighbours, Bolivia and Perú, towards which latent conflicts resulting from the armed conflict of 1879 still are present. The cut with the Andean Group represents finally an interruption in the long integration tradition of Chile which can be hardly replaced by a loose participation in the group of the La-Plata-States, where Chile has to compete with such economic and political giants like Argentina and Brazil.

### Prospects for the Reduced Andean Group

For the rest of the Andean Group the withdrawal of Chile represents also a painful shrinkage. Indeed, the immediate conflicts have been so far settled and the protocol to the Cartagena Treaty as well as the reforms of Decision 24 are already in force. But difficult decisions lie still ahead, like the sectorial industrial programming, the redistribution of the products assigned to Chile under the metal mechanical and petrochemical agreements and the reorientation of the preferential trade flows coming duty free from Bolivia and Ecuador to the Chilean market, which will exert more pressure on the markets of Perú, Colombia and Venezuela.

And depending on the future Chilean experience with foreign investors, especially Bolivia <sup>20</sup>, which also participates in the La Plata Basin, and to a lesser extent Colombia, may be tempted to follow the same way. But as the investment climate for foreign capital is becoming in general more favourable in Latin America, it is unlikely that a country like Chile will be in a better competitive position than Argentina or Brazil in its race for attracting investments. Therefore, the conditions for the reduced Andean Group to attract foreign investors, despite some restrictions which are at least partially equated by stable investment rules and access to a preferential regional market, are not bad. But it is unlikely that the Andean Group will ever regain its former dynamism, not least, because a possible rejoining of Chile may become very difficult and be subject to costly negotiations, the only link being the constitution of a mixed Andean-Chilean Commission.

<sup>19</sup> A recent decision (Decision 29) of CAF provides that credits will be given only to members of the Andean Group.

<sup>18</sup> This constitutes an evidence that Decision 24 did not impede the flow of FDI but contributed to regulate it. While it apparently has so far failed to reduce "dependency" it seems to have been a good instrument to review and renegotiate technology contracts. See L. K. Mytelka, Direct foreign investment, technology transfer and the Andean integration, paper prepared for the International Political Science Association Meeting, Edinburgh, Aug. 15-20, 1976.

<sup>20</sup> Bolivia has been continuously expressing its disappointment with the results of a membership in the pact. In January 1977 it announced that a company manufacturing oil drilling bits with foreign assistance, a product assigned to Bolivia under the sectorial agreement for the metal-mechanical industry, will have to be closed down since similar industries have been started in Venezuela and Perú. Consequently, exports to the Andean countries have been impossible.