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Technological Innovation Studies Program

Research Report

A STUDY OF CANADIAN JOINT VENTURES

IN MEXICO

Interim Report

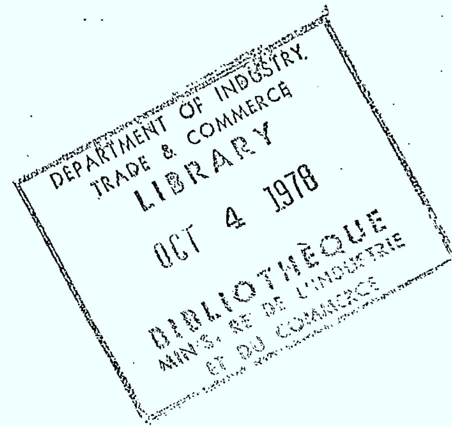
J. W. C. Tomlinson
and
M. Thompson

Rapport de recherche

Programme des études sur les innovations techniques

Industry, Trade and Commerce | Industrie et Commerce

Technology Branch | Direction de la technologie
Ottawa, Canada | Ottawa, Canada



A STUDY OF CANADIAN JOINT VENTURES IN MEXICO

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The views and opinions expressed in this report are those of the author and are not necessarily endorsed by the Department of Industry, Trade and Commerce.

INTRODUCTION

This report is based on information collected from a variety of sources in over forty interviews during 1976 and 1977. Respondents included executives of Canadian and Mexican parent firms and their joint ventures, plus other businessmen and government representatives in both countries. The sample covers virtually all firms known to be Canadian-Mexican joint ventures at the time of the study, with the exception of two or three mining companies operating in less accessible regions of Mexico. None of the joint ventures approached and only one senior executive of a parent (Canadian) firm refused to cooperate. In most cases, there were interviews with both Canadian and Mexican representatives.

The eleven joint operations fall into three industrial groups: manufacturing (7); mining (2); services (2). They range in age from one established over 25 years ago, down to one firm that had not yet commenced operations in 1976. Their size also shows considerable variation. Although the Canadian partners typically rank among the major firms in Canada, several of the newer joint ventures were formed by smaller companies. Overall there appears to be increasing interest among Canadian companies in Mexican joint ventures. In the manufacturing sector, there has recently been a trend towards the purchase of equity in existing firms, rather than the formation of new companies.

The sample was restricted to enterprises which were successful, or which offered sufficient prospects of success to warrant continuation in the face of adversity. Thus, the responses to questions concerning the Mexican economic climate and joint ventures as a vehicle for investment were overwhelmingly favourable. Clearly, a different image in both areas might well emerge if a sample of unsuccessful or aborted joint ventures were surveyed.

The motives of most of these Canadian investors in forming joint ventures were so obvious as to need little elaboration. Mining companies were seeking minerals, and Mexico has a history of mining activities that predates the Spanish Conquest in 1520. Firms in the manufacturing and service sectors wanted access to a large market with a record of growth, good prospects for the future, and relatively stable (by Latin American standards) economic and political conditions. Government regulation of foreign investment in Mexico is complex, but in recent years, official policy has been to require participation by Mexican nationals in virtually all new investment, usually in a majority position. (Legorreta, 1973, p. 37) There is also a long-standing policy of encouraging import-substitution. Thus one of the basic questions in a study of this nature, the reasons for choosing a joint venture as the vehicle for investment, appears to be answered at the outset. The Mexican government will not tolerate other forms of foreign participation in the Mexican economy, except in special circumstances.

The Law to Promote Mexican Investment and to Regulate Foreign Investment and the Law on the Registration of the Transfer of Technology and the Use and Exploitation of Patents and Trademarks provide the main body of legislation concerning foreign investment in Mexico. Patents, trademarks and licensing are further controlled by the 1976 Law on Inventions and Trademarks. Under these Laws,* control over investments is officially centralised in the National Commission on Foreign Investment which maintains the National Registry of Foreign Investment.

Foreign participation in new ventures is formally limited to 49% or less in most industries, 36% in mining operations in areas designated as national reserves. So far as mining operations are concerned in general, a law promulated in late 1975 requires a Mexican share of 60% It also defined a "net capital" concept for determining equity shares in new mining operations which is likely to be applied to other industries in the future. Under this concept, percentage shares of foreign and Mexican ownership are calculated at all tiers of ownership and prorated to

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* Ley Para Promover la Inversion Mexicana y Regular la Inversion Extranjera (May 8, 1973) and
Ley Sobre el Registro de la Transferencia de Tecnologia y el Uso y Explotacion de Patentas y Marcas (February 1,1973) and
Ley de Invenciones y Marcas (February 5, 1976).

determine the effective net ownership of the new venture.* There are only four large Mexican mining companies that can be considered as experienced and competent potential partners - Peñoles, Asarco, Fresnillo and Frisco. Of these, the first three already have significant foreign ownership. Hence if they are included in a new joint venture, the foreign pro-rated share in ownership could soon be pushed over the allowable limits.

Current lack of foreign capital and necessary new technology, or short-term reinvestment problems of local partners are situations which qualify from time to time as special circumstances where constraints may be relaxed in order to avoid frightening off the golden geese. Even in cases of these types however, a foreign investor cannot expect to maintain a dominant equity position for very long. Over the years, the Mexican record of reducing foreign-owned investments to at least a parity position for local ownership has been very effective - originating the technique known

* Thus for example, a Canadian mining firm might seek to set up a new Mexican operation with an existing local joint venture which was itself already 50% foreign-owned. It could strictly only expect to be permitted an (40 - x)% share of the overall equity in the new venture, where x is the proportion of the overall equity already assigned to foreigners through the first tier of ownership in the existing joint venture. In fact an unfortunate choice, since the joint venture itself would have trouble in qualifying for 100% of the new operation and would have to bring in more"purely" Mexican capital!

in the international business literature as "creeping expropriation - reducing foreign-owned investments to at least a parity position for freedom of management in operating a business.....increasing a nation's share of the benefits from international enterprise while allowing the firm to continue its operations." (Robock and Simmonds, 1973, p.366) The record of law and practice concerning expropriation in Mexico is examined in Lowenfeld, Expropriation in the Americas: A Comparative Law Study.

This report is organised in the following manner. After the introduction there is a brief account of the Business Climate of Mexico and its prospects. The main points which arose in the interviews are then presented in summary form, together with comments upon the issues raised, most of which have implications for Canadian firms and investors. This summary is then followed by a more detailed elaboration of the background to these issues in sections dealing with:

Control and Review Systems for Technology and Foreign Investment in Mexico.

Mexican Partners

Rates of Return

Government Incentives

Market Share

Initiation of Joint Ventures

Nationality Issues

Taxes

Division of Responsibility Amongst Partners

Dividends and Other Payments

Relations with Government

Views on Joint Ventures

Transactions Between Partners

Exports

The report itself ends with a discussion of some Conclusions and Recommendations from the study. While many of these are particularly directed toward implications for the Canadian Government, they should also be of interest, indirectly at least to Canadian business. A final section provides a first structuring and iteration of a long-term simulation model of the joint venture process in Mexico.

Business Climate of Mexico

A. might be expected, most respondents were optimistic about the business climate in Mexico, although they had reservations about the period up to the end of 1977. For them the most favourable aspects of the country were: political stability, relatively equitable and consistent treatment by government, the potential market growth created by economic expansion plus oil discoveries, and labour, which is relatively cheap, eager to learn, and seldom on strike. The negative aspects cited were: fear of devaluation (which in fact occurred three months after the interviews), rapid population growth, the shortage of skilled workers and managers, and the bureaucratic tendencies of government. Whatever their complaints, the fact that they were continuing operations in Mexico, suggested that they regarded the problems as tolerable at least.

Respondents were very positive about the medium and long-term future prospects for Mexico. They spoke of projected annual growth rates for their local activities of up to 30 per cent, due to the continued expansion of manufacturing, extension of infrastructure services, rising GNP, oil discoveries, etc. Even firms with currently unsatisfactory rates of return were quite willing to endure this situation for several years in the expectation of substantial improvements. The change in government at the end of 1976 was regarded as an especially favourable condition for business and investment. For example, where labour was regularly appeased with inflationary wage

increases and the private sector made the scapegoat of many of Mexico's social problems under President Echeverria, the situation has now changed. Unions are being asked to make sacrifices in the national interest, while private business is being wooed to provide necessary investment which the government is unable to finance.

At the same time of the interviews this optimism was generally supported by analysts of Mexico's future: "Mexico will be enjoying a golden period of its economic development during 1977-1980.....There is a ring of stability to Mexico's medium to long-range future: (B.L.A. August 1976). In the last few months however, some of the euphoria has become muted. In January of 1977, Business International's Latin American supplement began to cover itself both ways: "Recovery from the 1976 crisis seems to be going well...however, the potential for a relapse is still very much present...If the recovery process does go sour, it would not be a slight or slow development but a rush toward disaster that would make Mexico an extremely risky place to be doing business." (B.L.A. Jan.1977)

By March 9, Business Latin America seemed to have run out of optimism: "Mexico entered 1977 sliding into the worst recession in 30 years and the highest inflation since WW II, price pressures will lead to an unprecedented COL leap in 1977. Meanwhile an industrial recession is gripping the economy.....confidence may be back but the financing is not...

labour will be a main outlet for the social ferment growing out of 1977's problems....strikes will flare up in many sectors....lastly, the oil itself is both a bonanza and a potential political booby trap" (BLA May, 1977).

In this respect, despite short term problems of inflation and uncertainty caused by the change of government, there still is a noticeably more relaxed evaluation of the current problems in Mexico on the part of Canadian interests such as those interviewed in this study. "Economically the country is immensely rich in minerals, possessed of large oil reserves, more than capable of feeding itself and rapidly getting into place an industrial structure and transportation infrastructure which provides a strong base for fast growth in the future. Politically its role could be decisive in the position and alignment of the Americas in decades to come" (Robertson, 1977).

On the basis of such evidence and with confidence in the ability of the Mexican government to continue its track record of conservatively successful and pragmatic control of its economic system, the positive forecasts for the Mexican economy expressed by these respondents appear reasonable. "The government believes that its act of balancing wages and prices, spending and borrowing, political and economic pressures must continue for another two years before inflation slows, investment begins to show results and oil exports transform the country's balance of payments. The task is enormous - the IMF wants Mexico's

inflation down to U.S. standards by 1980 - but, in contrast with the improvisations of the Echeverria regime, president Lopez Portillo's economic team at least seems to know what it wants and even how to achieve it." (Economist, April 9, 1977, p.85).

Summary of Responses Concerning Canadian Joint Ventures in Mexico

This section list briefly some of the main points stressed by respondents in interviews, both in Mexico and in Canada. Each point is followed by a comment from the study team based on the overall evidence. A broader discussion of the issues follows in the main body of the report.

A. What Canadian Firms Should Look for in a Mexican Partner

1. Financial Status - one of the primary attributes mentioned was that a Mexican partner must have a sound financial status and the capability of matching capital and financing needs for the joint operation.

   Comment - clearly desirable under the matching ownership requirements imposed by the Mexican Government. It may limit the range of potential local partners in the short run, or make the government a more attractive partner if the probable capital needs are large. Other alternatives are to seek a number of local associates who can between them provide matching finance, or for the Canadian partner to organise a higher debt component in the capital structure.

2. Business Capability - local partners should be competent businessmen especially with respect to marketing, administration, and financial management.

Comment - this would be particularly true if the local partner were to be directly responsible for managing the joint venture. In fact, it rarely appeared to be the case that partners actually ran the operation. Usually, however, they were instrumental in recruiting or seconding suitable personnel who were then trained in the technical side of the business by the Canadian partner. In any case, the underlying concern here was the potential quality of the interaction between partners which would be enhanced if they had a common familiarity with and appreciation of business problems.

3. Common Goals - there must be clarification and compatibility of the objectives which the local partners seek in the joint venture.

Comment - this is well worth stressing as one of the most important issues to be clarified in the feasibility and pre-negotiation stages of the association. All too often, clarification is skated over without sufficient effort to verify congruence of objectives with respect to issues of dividend levels, technical assistance payments, growth rates, organisational structure and operating responsibilities. It is also important to establish pre-determined methods of resolving potential conflicts. Once the joint venture is set up, unexpected fundamental conflicts in objects are more difficult to resolve. This in fact is one of the pargmatic reasons underlying the concern of Mexican

respondents that Canadian partners should be SIMPATICO.

4. Ability to negotiate with government - or to provide contacts who can negotiate with adequate impact on behalf of the interests of the joint venture.

   Comment - a universal and usually justified concern of foreign investors whose own nationality is felt to preclude them from the local corridors of power. Clearly however, there are trade-offs here. Locals, especially members of the elite, are familiar with the system and know how to access it (the "know-whom" role). On the other hand, the economic and technical status of a larger foreign investor carry sufficient weight to at least gain the serious attention of government decision makers. Again, the main issue is the quality and effectiveness of the interaction. A sensible solution, as one of the respondents indicated, may be for the Canadian investor to approach the government jointly with a suitable local partner or contact.

5. Compatibility in ethics - in terms of what is considered acceptable business behaviour and what activities are legitimate or tolerable in "manipulating the system" in Mexico.

   Comment - the first of these is difficult to pre-determine without the kind of comprehensive discussion which is also required for objectives and this is another good reason

for stressing this aspect of pre-negotiation. So far as "bribery and corruption" are concerned, it is important to distinguish the political, societal or organisational level involved. Triumphant virtue doesn't get imported components off the docks and conforming to universal local custom in persuading a longshore foreman or customs clerk to cooperate will probably not destroy the fabric of local society. Attempting to bribe a high-level government official may however, destroy the credibility of the briber and creates for both parties grave long-term risks of the type of exposure which is currently internationally fashionable. Once a Mexican partner's compatibility in business objectives and behaviour is established, this is one area where their guidance,both to the spirit and the execution of the practice of local mores,is particularly appropriate.

B. What Mexican Firms Look for in Foreign Partners.

1. Financial Resources - sufficient to create the necessary capital investment in Mexico.

   Comment - in the short term, a very important consideration. Both the nation and its businessmen are currently in a capital squeeze. In the longer run, perhaps six to ten years, foreign capital will probably become far less vital as oil revenues percolate through the Mexican system.

2. Technology and Experience in its Application - sufficient to bring a new technological package on-stream in Mexico, to trouble shoot and upgrade it as suitable.

   Comment - currently an important determinant, in the future probably the critical determinant, as foreign capital loses its attractiveness. In the past this has been an area of comparative advantage of the major multinational corporations. It is argued in this report that appropriate technology is becoming a major potential advantage of medium, even small firms wishing to invest in Mexico and that this creates opportunities for many Canadian companies.

3. International Status - visibility and reputation simplify local evaluation of a prospective foreign partner in a very imperfect market for information. From this limited perspective, the bigger the foreigner, the better.

   Comment - still a reassuring criterion for Mexican interests, but two things are happening. First, disillusion is creeping in, especially in Mexico, with the cost of the MNC's technology. Second, most of the MNCs already have Mexican operations and Mexican associates. Uncommitted new Mexican interests are looking elsewhere for suitable partners. Both these reasons are also linked with the comment above on

technological attractiveness in their impact upon the potential opportunities for Canadian firms.

4. <u>Commitment to the Mexican Joint Venture</u> - which should be perceived as a significant part of the foreign firm's global operations and organisation, preferably in tangible form such as using the joint venture as an export base for Latin American markets. Canadian firms should also avoid trying to manage their end of the joint venture directly from Canada.

   <u>Comment</u> - the depth of the joint commitment is of concern to all parties in the joint venture. However, even though they may themselves have other irons in the fire, the venture is more likely to be important to the Mexican interest, while it may be a relatively small part of the foreigner's international activities. Here again is an apparent potential advantage of Canadian firms with limited international activities.

5. <u>International Experience</u> - which is more than having a distribution or sales branch abroad. Respondents stressed that this was a desirable but not a necessary condition if other potential contributions were very attractive.

   <u>Comment</u> - almost by definition, another potentially limiting criterion in considering the majority of Canadian firms- who happened to be internationally inexperienced. However, it is likely to be subordinate to the technological carrot. In any case many domestically operating Canadian firms have internationally trained or experienced executives who

create for them a potential relative advantage in comparision with a similar Mexican partner.

6. Depth in Management

   Comment - in itself not a critical consideration since most Mexican Canadian joint ventures are managed by Mexicans. However, good top executives seconded from the Canadian partner are highly valued. Further, the availability of Canadian technical managers for limited tours of duty clearly adds to the probability of success of a joint venture. A less obvious aspect of this issue is that Mexican partners are again looking for evidence of a Canadian partner's potential commitment as indicated by the availability of senior Canadian executives to participate in decision making in Mexico. An active Board of Directors is also an important feature of Mexican business organisation.

7. Ability to Communicate - desirably this means the ability of the Canadian partner's executives to speak Spanish and the need for understanding of the Mexican environment.

   Comment - although it may appear to be an unnecessary sophistication when English is a universal language of business and technology, this accomplishment was repeatedly stressed by respondents. Our conclusion is that it is necessary for Canadians who are likely to be operating in Mexico on a continuing basis, even if the importance of this capability is perhaps peculiar to Mexico amongst Spanish-speaking countries. However, while fluency in

Spanish undoubtedly smooth the passage of negotiations, it is not as vitally important during the stage of negotiation of an agreement.

C. Specific Canadian Strengths and Weaknesses Identified by Respondents.

1. Strength in Technology - although a number of potential areas of comparative strength for Canadian firms have been identified in this report, only one was explicitly stressed by Mexican respondents. This was the fact that, in their experience, Canadian firms possessed excellent technical knowledge, especially in mining and associated technology.

   Comment - it may be optimistic to talk of other areas of strength so much as possible factors which could be developed into positive advantages on the part of Canadian investors. These would include, compatibility in size, acceptable nationality, empathy as a fellow host nation to dominating MNC investment, managerial and technical skills, all of which are discussed in later parts of the report.

   Weaknesses cited included:

2. Fear of Offending Latin Sensitivities - Canadians are unnecessarily afraid of insisting upon competent planning and performance. They should be tougher with their partners when necessary.

3. Lack of Local Autonomy - Canadian firms do not give their local executives and managers enough autonomy.
4. Lack of Openness to Local Customs and Mores - Canadians are less open-minded about local customs and mores than are other foreign investors in Mexico, including Americans.
5. Inability to Work with the Mexican Bureaucracy- Canadians must understand and respect the power of the Mexican Government and be willing to negotiate areas of conflict. They must be patient with the bureaucracy and must not be afraid to seek local aid in order to overcome apparent stumbling blocks created by bureaucratic rigidities.
6. Lack of Appreciation of Mexican Laws - Generally Canadians do not know or understand Mexican laws and do not either do their homework, or retain competent local counsel. As a result they miss out, for example, on tax concessions and other incentives.
7. Failure to Use Available Informational and Other Facilities - Canadian firms do not use promotional and advisory bodies such as the Canadian Association for Latin America, Canadian Export Association, various joint Canada-Mexico Business interest groups.

Comments - there are clearly elements of contradiction between several of the complaints listed above. They do however provide an indication of potential problem areas,

about which prospective Canadian investors in Mexico should be forewarned. On the issue of information sources, it is also worth listing some of the main groups who were described as being helpful in finding local Mexican partners. They included:

i) Canadian and Mexican banks. The latter clearly know the population of local business interests, while the former are becoming more knowledgeable about the Mexican environment and its potential.

ii) Canadian embassy and consulate officers were said to be particularly active in Mexico and effective in establishing contacts for Canadian businessmen.

iii) Mexican law firms, many of whose personnel were U.S. trained in business as well as law.

iv) Mexican subsidiaries of multinational accounting firms such as Price Waterhouse.

v) Canadian and other consulting companies, a group with more experience in Mexico than all but a few Canadian firms.

vi) Other Canadian firms; in this context, the report discusses later a cumulative impact, combining demonstration effects and growth in trusted information sources, which could be put to use in stimulating the growth of Canadian firms' serious interest in Mexico.

D. Additional Major Points Cited by Mexican Respondents.

1. Professional Advice - should be thoroughly sought out from a number of sources by potential Canadian investors. One cannot effectively go it alone in Mexico.

2. Authority of Negotiator - joint venture negotiations are likely to be more successful if they are carried out by top level executives, preferably at the level of the President, Chairman of the Board, or at least the VP International of the Canadian firm.

   Comment - the Mexican end of the negotiations is almost always carried out by the owners or top executive of the Mexican interest. Their status and potential commitment to a joint venture opportunity are therefore on the line. When the chief Canadian negotiator, either because of limitations upon his authority, or as a bargaining procedural tactic, has to refer back to head office, the perceived importance of the project from the Canadian end is seen by the Mexicans as downgraded and with it their own status. They are in any case anxious to establish a sound personal relationships with their Canadian opposite numbers as the strongest underlying basis for effective business relationships in Mexico. If they withdraw from direct participation in the negotiations, two things may happen - both unfavourable. Either they will withdraw their interest in the project which is then doomed

from the point of view of their partnership and difficult to re-establish with another partner if they feel sufficiently slighted to pass the word around. Alternatively, negotiations will be left to lower-echelon Mexican executives who will certainly have to refer back even trivial issues for approval, thus delaying negotiations considerably-possibly even beyond Canadian tolerance.

3. Mexican Chairman - it is desirable, for the local image of the joint venture, to appoint a Mexican chairman, either from the local partner or a mutually acceptable senior Mexican.

   Comment - at the same time many of the Mexicans interviewed were strongly in favour of assigning a Canadian, or other competent foreigner, as the joint venture's top executive officer. As a result, the favoured combination is a well-connected and effective Mexican corporate head (preferably not just a figurehead) coupled with a capable Canadian to run the operation.

4. Government as Partner - try to avoid taking the Mexican Government as a partner. Its goals were seen by respondents as oriented towards social development rather than profit maximisation.

   Comment - a reasonable basic preference but probably not a strong enough criterion to jeopardise an attractive

project for which there are no other suitable local takers. As discussed later, the Mexican Government's agencies value profits themselves and have rarely proved as undesirable as the folk-lore of business might suggest.

5. Acceptable Rates of Return - Mexican investors can get 12-15% on term deposits and bonds with very little risk. Therefore, they are not interested in low rates of return and look for 15-30% net of tax from investments in other activities such as manufacturing.

   Comment - in spite of their high opportunity benefits, the evidence from the study indicates that Mexican partners are more sophisticated than the simplistic form of this argument would suggest. While the majority of Mexican investors prefer early dividend pay-outs, they are increasingly prepared to accept both limited earnings in the short term and reinvestment for growth where the longer-run potential of a project is attractive.

6. Investing in Growth Sectors - proposed projects are more likely to be acceptable in areas and sectors of economic growth or where socio-economic growth will be created.

   Comment - even to the extent that acquisitions of Mexican operations by foreigners or entry into a market dominated by existing Mexican firms are virtually obstructed by the Mexican Government, unless they are the only means of

salvaging a desirable local project.

7. Avoid Prestanombres - the Mexican Government reacts strongly against the use of local paper partners or Prestanombres. They insist upon a genuinely joint operation with commitment of joint financial resources.

   Comment - a dangerous strategy to circumvent local ownership regulations with stiff penalties for all parties if convicted. However, as discussed later, there are a number of acceptable alternative short-term expedients in genuine cases of necessity, including Fideicomisos and other trust-based arrangements.

E. Potential Problem Areas Listed by Respondents in Mexico

1. Inflation - the rate of inflation will probably be a problem.

   Comment - this is certainly a problem in 1976 and will remain so into 1978. However, the Mexican Government's track record in controlling inflation since World War II has been good. Its present objective is to bring inflation down to an annual rate of 5-6% within two years. As of mid-1977, its strategy of restricting wages and prices while encouraging investment to increase local supplies of goods and materials under the Alliance for Production programme seems reasonable.

2. Stability of the Peso- even after devaluation, the stability of the value of the peso is likely to be uncertain.

Comment - short-term fluctuations of up to 15% may continue through 1977, but the long-term strength of the currency is more important to foreign investors. Mexico's balance of payments, in spite of the I.M.F.'s rather conservative perspective, is likely to move strongly into surplus by 1980-1982 as oil and gas revenues reach projected values (B.L.A. May 11, 1977, p.150) In comparison with the prospects for the Canadian dollar over the same period, a Canadian flight into Mexican pesos might even seem justified!

3. Price Controls - these currently affect over 250 products for the Mexican domestic market.

   Comment - under 1974 and 1976 Presidential Decrees these controls are aimed mainly at subsistence goods and consumer necessities and only really affect import substituting industries in a sector where Canadian interest is limited In the short-term, they do not in any case affect the price of new products to the Mexican market. As the Mexican economy recovers, these controls are likely to be relaxed. In fact a Presidential Decree of June 20, 1977 has just removed price controls in the Mexican auto industry, which have existed in one form or another since 1962. This was a direct inducement to increase exports to $1.10 for every $1.00 of imported components by June 1981. It is also the first specific step by the Lopez Portillo Government to free price controls from all non-basic goods.

4. Import Restrictions - on components and equipment for various industries.

Comment - there was little evidence that these had effected new technology projects or the sectors in which Canadian firms are involved. On the other hand, several cases were cited where the Mexican Government had moved remarkably quickly to approve the import of equipment and components needed by Canadian-associated ventures in emergency situations.

5. Unemployment - has been rising, "800,000 young people become 16 every year and only 300,000 new jobs are created."
   Comment - while this is clearly a potential source of socio-political friction, it is also a strong reason for the encouragement of foreign investment which can create jobs and economic development - an argument clearly recognised by President Lopez Portillo's government.
6. Class Structure and Regional Problems - the Mexican Government is going to be under pressure to deal with regional disparities and the demands of the peasants. These problems are not likely to affect a joint venture directly but may have indirect effects through directive and distributional policies for the government.
   Comment - there are unlikely to be any desperate efforts at re-distribution similar to those in the last throes of the Echeverria regime. The present government seems more likely to work for steady, soundly-based industrial growth as a solution, providing incentives to investors who locate in less-developed zones. More dramatic amelioration of income and employment disparities may be made in the early

1980 by using oil revenues.

7. Labour Unrest - unions are still not militant in Mexico, although some older union leaders are experiencing more trouble than before in controlling their younger, more radical members.

   Comment - again, the government appears prepared to hold the line in the short-term, as indicated by the Alliance for Production programme. In the medium term, it should be able to make acceptable concessions to satisfy labour.

8. Bureaucratic Inflexibility - the workings of the bureaucracy are laborious and inefficient. Relatively simple paper work which would only take 3 days to complete in Canada can take 3 months in Mexico. Doubts were also expressed about the honesty of the bureaucracy at lower and middle levels.

   Comment - while the complaints may be true, one is tempted to wonder how long a respondent has been away from Canada who remembers a turn-around time of 3 days for any transactions with federal or provincial governments, or any transactions involving Postes Canada!

9. Lack of Skilled Personnel - of the quality needed, both in terms of technical and engineering skills and in terms of capable managers.

   Comment - one of the main attractions which a Canadian firm has to offer may well be its ability to train Mexican personnel in technical skills and their application. This may be little consolation to a small Canadian firm looking for what is virtually an expanded licensing operation based on competent Mexican personnel. However the allowable

ratios of foreign (Canadian or third country nationals) to local personnel can be as high as one in ten which leaves some room to manoeuvre in the short-run.

Control and Review Systems for Technology and Foreign Investment in Mexico.

The main clearing house for approval of technology transfers is the National Registry of the Transfer of Technology, controlled by the Ministry of National Properties and Industrial Growth, with technical advisement from the National Council of Science and Technology. Local beneficiaries, whether Mexicans, foreigners resident or subsidiaries located in Mexico, from any of the following activities are required to register all documents related to the relevant contracts or agreements:

licensing use of patents or trademarks

provision of technical assistance or expertise of any kind

provision of managerial, engineering and operating services

Notification to the Registry through the Ministry of Industry and Commerce must be made not more than 60 days after an agreement or modification to an agreement has been signed. Registration can also be requested by the foreign supplier of technology and this is probably a desirable precaution to avoid possible manipulation of the Registry's terms of acceptance by a local licensee. Unregistered agreements are unenforceable in law and dependent production programmes are not approved by the Mexican Government.

For its part, the National Registry must officially act on such applications within 90 days or permit acceptance automatically. In practice, the Registry automatically rejects all submissions it cannot process in time, forcing re-submission and a further

90 day delay. However, such cases are not prejudiced by the need for re-submission. In the first two years of its activities it dealt with about 5,000 agreements and contracts. Nearly 75% of these were approved. Most of the rejections were based upon excessively high costs or long terms, price maintenance clauses, restrictions on production levels or exports, and grant-back clauses. Other causes for rejection were limitations on licensees' R&D activities or procurement sources, exclusive sales contracts, obligation to submit disputes to foreign courts and contracts relating to transfer of technology which is already freely available in Mexico.

The national Commission on Foreign Investment includes representatives, usually at the Undersecretary or deputy level, from the Ministries of Finance, Industry and Commerce, Foreign Affairs, Patrimony, Labour and the Office of the Presidency. An Executive Secretary of the Commission, appointed by the President, and at least two Commission lawyers constitute an Advisory Board which is in turn assisted by an Economic Analysis Section.

Potential foreign investors send notification of a project and a request for approval and for a permit to incorporate to the Commission. Upon approval by the Commission, the Ministry of Foreign Affairs issues a permit authorising acquisition of property. (Prior to the 1973 Law, the Ministry ruled directly on the acceptability of proposals by foreign

investors.) After approval, incorporation follows a common procedure: preparation of articles and other papers by a lawyer or notary, verification of these documents by a local commercial court, authorisation for the project to proceed, registration of the project with the National Registry of Foreign Investment.

Once joint ventures are established the foreign investment regulation laws treats further expansion into new sites or products as new investments which have to be approved and registered. This rule was originally intended to provide leverage to control wholly foreign owned operations existing in Mexico in 1973, by forcing them to accept new conditions, notably Mexicanisation of ownership, if they wished to expand a successful operation. Indirectly, it appears to offer a threat to the freedom of any foreign-associated joint venture to expand. In effect however, there is no evidence that it has been, or is likely to be, applied in this way to ventures which have a Mexican equity majority - or an acceptable reason why such an ownership situation is impossible. Further, the Commission approved in its first three years over 400 of roughly 600 requests for expansion or new product lines from foreign majority owned companies which had been established in Mexico prior to 1973.

Past experience with the processing of new applications suggests that an applicant would normally know within 60 days if a proposal is acceptable - although the maximum period,

especially in mining projects, can be a year. This average elapsed period did not include dalays caused by project modifications, or by initial rejections followed by re-submissions.

Mexican Partners

All respondents agreed that the choice of a partner is a crucial variable in the success of a joint venture. Since pu public ownership of joint stock companies is rare (no Canadian company was listed on the Mexico City Stock Exchange in 1976), individual investors tend to have a large share of the equity in a firm. However, relatively few Mexicans have enough money to invest in a large joint venture and many potential partners are already involved in so many firms that new joint ventures may post conflict of interest problems. Consequently the government is at least a potential partner in many joint ventures. Two main classes of local partners were present in joint ventures involving Canadian interests - wealthy individuals and families or government agencies. It also appears to be the case in Mexico that when several individuals hold equity in firms, they do not usually vote their shares as a common local bloc.

Most firms in the sample have private partners. These are often individuals with investments in many industries and close ties with one or more of the major banks. Persons in these circumstances in Mexico have a variety of alternative possibilities, with a high opportunity cost for any specific investment, and hence demand a generous rate of return, one

which will at least provide repayment of their investment within five years. Admittedly, they are conservative investors, but with reason, since they are unable to diversify as readily as large corporations. Only a few will take really substantial risks, although such individuals do exist. A number of firms had experienced difficulties in their history because original local partners had been unable or unwilling to produce additional capital to finance expansion. In these cases, the proportion of Mexican ownership fell, or new investors had to be found. While the government's preference is for the latter alternative, in order to maintain relative shares in ownership, locating supplementary new investors can be difficult, since they have to adapt to existing practices in the joint venture.

Both Canadian executives and Mexican respondents in this study generally agreed that one of the most serious problems in the formation of joint ventures in Mexico at the moment is the apparent lack of readily available and suitable private capitalists to meet legal requirements for Mexican ownership. This is a common difficulty in establishing joint ventures in developing nations, even one as relatively advanced as Mexico. One result is that the limited number of such potential partners which are clearly visible and well qualified are probably over-extended because of the extent of their participation in joint ventures with foreign firms on top of their commitments to their own "original" Mexican operations.

Companies such as Penoles, for example, already have a full complement of joint ventures and are therefore, extremely reluctant to enter into any new agreements.

This has in the past led to a dangerous strategy which a few foreign firms (none in this sample) have relied upon. This involved creating dummy partners, whereby a block of shares were held in escrow to be purchased later by assigned "partners" with profits from the venture itself, in order to evade the intent of the law. The government knows of these practices and disapproves of them. Since 1973, legislation has provided firm penalities (up to nine years imprisonment and fines of up to $4,000) against Mexicans who act as fronts (PRESTANOMBRES) for foreign capital,plus fines of up to confiscation for the firm and up to $8,000 for employees of the firm. A further risk in this practice is that the "dummy" partners have occasionally been able to bilk both their foreign partners and the joint venture with impunity because of the lack of formal public recourse in such marginally legal situations.

An acceptable strategy adopted by some foreign investors who were unable to find local partners when they established operations in Mexico was to enter into an agreement with Mexican fiduciaries empowered by the government to set up trusts, known as <u>fideicomisos</u>,as a means of complying with the law. Strictly speaking these were originally real estate

trusts authorised by Presidential Decree in April 1971. They created a method whereby foreign investors could lease real estate to set up industrial or tourist activities which were perceived as desirable operations for national development in border areas such as Monterrey. This mechanism was necessary to compensate for Mexican restrictions against foreign ownership of real estate within 50 kilometres of the coasts or 100 kilometres of the borders. These trusts cannot exceed 30 years and leases are for terms of not more than 10 years. It is also worth noting that under Mexican Law, a lease to a foreigner is treated as an acquisition of assets by the latter and such requests are ruled upon by the National Commission on Foreign Investments.

In application the procedure has been extended to cover situations where suitable local partners for a new foreign investment are not readily available. The partner in such cases then becomes a local bank, which acts as trustee for a majority of the shares until the success or potential of the investment attracts a local partner,or the earnings record is favourable enough to justify a successful public share issue. In these cases, the bank has voting, but not dividend rights and disposal of the shares must meet with the foreign partner's approval. Such arrangements are not uncommon and seem to meet with government approval provided that efforts to secure active partners are vigorous

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* The Mexican Securities Exchange Commission(COMISION NACIONAL de VALORES) requires, amongst other things, that the company must have profits from its operations before making a public offering (ESCOBEDO, 1975, p.60).

and sincere. Whatever the strict legal correctness of the strategy, the advice of local experts is that it is acceptable "if it is done with a big bank and kept upfront". In other words, if the government is shown that the trust is a genuine short-term expedient because of lack of local partners or funding, possibly when an existing firm goes public, or develops a "fade-out" joint venture.

This relative shortage of recruited local private capital has led the government into direct participation to achieve national developmental goals. It stresses the point that the economy is a mixed system, including both public and private objectives and sectors. Its own part in this system is seen as including the provision of strategic or basic industries like steel or petrochemicals, as well as infrastructure and social capital. This role is also seen to involve the need for government to enter other private sector activities if a local company is about to fail, at the very least in order to prevent any resulting unemployment. "The result is often a three-way partnership among foreign investors, Mexican investors and the government-with government officials thereby gaining valuable exposure to business problems and procedures". (Robinson and Smith, 1976, p.14).

Two of the joint ventures in the sample involved government agencies as partners, while two had a partner which was a state-owned corporation. One of the firms with a government partner actually acquired the latter during the period of the interviews,

so that no information on their experience was available because of the current sensitivity of the issues involved. While there was little evidence of any detrimental activities by government partners, firms which currently had private sector partners wished to avoid government equity participation altogether if possible, but would reluctantly accept minority holdings if necessary. The two Canadian firms with direct government partners accepted this situation out of necessity, as the actual or projected rate of return on their Mexican projects by themselves was too low to interest local private investors. Both recognised that government influence in their industries was so extensive in any case that partial public ownership had little additional impact upon their autonomy.

The majority complaint by these Canadians concerning their Mexican government partners was the lack of a profit motive on the part of the latter and their willingness to sacrifice profits for social ends. Officials from two government financed development banks, who were the partners involved, admitted that their organizations would accept lower returns than private investors; in fact the divergence between social and private benefits in some of the projects they sponsored was one of the basic justifications for their own existence. These officials denied however, the suggestion that they were unconcerned with earnings and indicated that they clearly recognised the role of profits as a partial measure of efficiency in resource allocation. They further stated that they only invested in the private sector

by invitation, except where legislation specifically regulated the form of investment.*

In view of the relatively low potential rate of local return on these particular projects, the Canadian complaints hardly seem justified in these cases. "Although state companies are often guided by social considerations, the government also wants them run profitably and in a business-like manner. For the past six years the government budget has demanded that state enterprises operate self-sufficiently, without support from Mexico's treasury. As of September 1976, 70% of the 740 state-owned companies produced profits. Profits are however, believed to suffer somewhat from bureaucratic inefficiency," (I.L. & T. Mexico, March 1977).

In the same context, managers from the two firms with state-owned corporations as partners also stated flatly that the Canadian and Mexican partners were equally interested in profits and that political considerations were not important in corporate decisions.

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*There is the possibility in this context, that they may be "invited" into a joint venture, virtually by default, when the local private sector loses interest. Examples of this kind were cited for Heinz and for Philip Morris, where private shareholders dropped out and the government decided the operations were important to the national interest so sent in NAFINSA to replace local partners.

Rates of Return

The rate of return which was acceptable to Mexican and Canadian investors was a subject of considerable discussion and concern, both to the partners and to their bankers. In general, Mexicans expect around 20 percent return net of tax on their investment in an established firm, although they will accept lower rates (or even no return) while a firm is becoming established. As one Mexican respondent said, "I can get 15 per cent from high quality industrial bonds, so why should I bother with managing a firm for less than a premium over that?" The rate of return actually achieved by joint ventures in the sample varied from 3 per cent to 31 per cent, but the norm was in the 18-20 per cent range, after Mexican taxes. Some of the Canadian investors in this group were prepared to accept a lower rate of return on their investment in joint ventures, in fact a level closer to Canadian standards, but stated that they had found no Mexican partners willing to join in such a venture and no Mexican banks which were prepared to lend them money.

It should be emphasized however, that the large family or bank groups which have provided most of the Mexican capital in local joint ventures are prepared to accept lower dividend pay-outs, even for several years, in order to increase the equity base in these investments. To some extent this appeared to be a direct contradiction of the argument often cited in the literature, that local partners in joint ventures in developing countries are reluctant to reinvest earnings for the sake of long-term

growth. This was in spite of the fact that attractive short term alternative investments clearly existed for these Mexican partners.

Government Incentives

Few Canadian joint ventures appeared to have received any significant government incentives to invest in Mexico. Basically such incentives are not directed at foreign investors in Mexico in any case although firms which have not more than 49% foreign equity can qualify. Firms falling into a "new and necessary" industrial category, or which invest in Zones II or III* are exempt from payment of up to 40% of income tax, plus 100% of stamp tax, local sale tax and import duties, for tax holidays of up to 10 years. Low-interest loans may be granted to firms which are considering new projects of high priority to the government. Such funds are usually channelled by NAFINSA or Banco de Mexico through their subsidiaries such as FOMIN, FOGAIN, FONEP, FONEI OR FOMEX, or through private banks. The only special treatment cited by respondents as available in the service sector was in the facilities of the tourism development bank, which will make loans at preferential rates for the construction of tourist facilities.

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* Zone I covers the Federal District and most municipalities in the state of Mexico, plus Monterrey and Guadalajara. Firms in these areas are excluded from the government's incentives programe. Zone II covers the municipalities of Tlaquepaque and Zapopan in Jalisco; Lerma and Toluca in the state of Mexico; Cuernavaca and Jiutepec in Morelos; Queretaro; Cualtancingo, Puebla and Cholula in Puebla. Companies operating in these areas are eligible for slightly less generous incentives than those for firms in the rest of Mexico, designated as Zone III (I.L. & T. Mexico, March, 1977).

Other incentives in the form of CEDIS, or tax rebates tied to manufactured exports were available to firms which exported a specified part of their total output. This incentive was later dropped when the peso was floated in September, 1976. It has not yet been restored, although the government promised to do so when the export tax was dropped in October, 1976. However,none of these particular joint ventures appeared to have been able to continue to meet the fairly substantial export targets of the CEDI system in any case. Further, one firm commented that even when they had earned CEDIS on past exports, they had not received the refund of taxes involved for five or six months because of bureaucratic delays.

A number of joint ventures had actually received some form of incentive benefits in the past, but even in these cases the Canadian partners stated that the incentives had not been a major factor in their decision to invest in Mexico.

A separate fiscal situation exists for the mining industry. Taxes on mining operations are theoretically so high that no company can develop a property without negotiating a "fiscal agreement" (convenio fiscal) with the Federal Government These agreements vary, but the starting point is usually 50 per cent rebate of export and production taxes for firms with majority Mexican ownership. In national reserve areas the prescribed level of this majority is 64% ownership by the Mexican partner. More generous treatment can be negotiated.

The terms of the agreements vary, but usually run initially for 5 years and are renewable twice. However, at least one Canadian company backed out of a joint venture because it could not secure a fiscal agreement from the outset for 15 years. Taxes involved are actually collected and then returned to the company, which gives the government both an additional control mechanism in the threat of permanent withholding and a short-term source of interest-free revenue for the period until the taxes are repaid.

Market Shares

As in the case with most Mexican industries in which foreign firms are involved (Robinson & Smith, 1976, p.91) Canadian joint ventures typically enjoy a dominant position in the product markets in which they participate. The lowest market share reported for the joint ventures in this sample was 35 per cent, while the highest was 90 per cent (except for those firms which reported no competition at all in one or more of their Mexican product lines). The average market share for the manufacturing ventures was around 50 per cent. While the Mexican economy has many oligopolistic industries, the firms in this sample seemed to enjoy large market shares even by local standards. One Mexican partner observed that joint ventures generally are formed in sectors of the economy where competition is not strong. This would appear to be partly a result of the government's efforts, both to protect local

firms in industries where the latter have become established and to direct foreign investment into sectors which local interests lack capability or interest in entering.

Another indication of the position of these firms is the level of their annual sales. Eight firms provided useable sales data, and their average annual sales were $37 million per year, ranging from $100 million down to slightly more than $1 million. Several of the ventures at the lower end of the range were new and anticipated substantial sales growth in 1976-1977. The average level of annual sales for these Canadian-associated joint ventures is considerably higher than the figure of $20 million reported for 229 non-Canadian foreign-affiliated companies in 1974 (Robinson & Smith, 1976, p.74).

Initiation of Joint Ventures

There appeared to be no general pattern for the initiation of the joint ventures in this study. Few of these Canadian companies now operating in Mexico seemed to be there as the result of a well-developed overall corporate strategy, although some of the more recent ventures may have come out of more deliberately planned initiatives. This was markedly different from the case of other foreign investments in Mexico. Over 80% of the latter were said to have been initiated by their foreign parent companies as part of specific overall

corporate objectives including:

- penetration into a growing market 83%
- relative stability of Mexico (for diversification) 64%
- expected higher profits or lower labour costs 56%
- substituting local manufacture for exports in the face of tariffs 29%
- application of corporate technology to new opportunities 31%
- Integrative or competitive strategies [i.e. export base for neighbouring markets (10%); offshore manufacture (5%); matching or forestalling competitors 15%)] 30%

(Source: Robinson and Smith, 1976,p.137)

Several Canadian ventures in fact began after chance encounters. Canadian executives, either on holidays, or as an offshoot of other business relationships, came to know Mexicans who were in the same industry or were customers and someone suggested a joint venture. Usually, the Canadian firm already had other foreign operations, so that establishing an operation in Mexico was not a significant departure from normal practice even though the country may have been a new investment milieu and joint ventures an unfamiliar structural format for investment abroad.

The relatively unplanned nature of Canadian investments in Mexican joint ventures is also in contrast to the motivations described in an earlier study of Canadian investments abroad. The latter examined the way in which 312 foreign affiliates of 54 Canadian firms were set up. Basic criteria stressed for establishing this global sample included:

- market penetration and potential 84%
- geographical diversification 81%
- relative stability of host country 72%
- expected higher profits 70%
- using corporate technology 67%
- matching competitors 51%
- local manufacture because of tariffs 36%

(Source: Tomlinson and Himmelsbach, 1973).

This difference in the basis for initiation of joint ventures in Mexico as compared to Canadian foreign direct investment in general is probably partially due to the relative lack of importance ascribed to opportunities in developing nations by corporate decision makers in Canada. Of the larger sample described above, over 73% of the affiliates were in the U.S.A., U.K., E.E.C., or Australia, only 11% were in Latin America. It could therefore be argued that the difference in degree of corporate attention is perhaps just a reasonable result of larger, more-established and relatively stable markets in developed as compared with developing countries.

This may be part of the answer, but does not fully explain the similarity between Canadian firms' criteria with respect to a largely developed set of host nations, as described in the listing immediately above, and the criteria of non-Canadian investors in Mexico, described earlier. A further explanation probably lies in the fact that the latter include many of the world's largest multinational (or trans-national) corporations, whose resources, experience and scope of activities are greater than those of most Canadian firms. In terms of what might be called "decision budgeting", Mexico may be perceived, rightly or wrongly, as a marginal opportunity for the capabilities of Canadian firms, but well within the normal range and purview of larger MNCs. In terms of policy implications, this suggests that if increased Canadian

investment in Mexico is desirable, whether to Canadian or Mexican governments, either opportunities in Mexico have to be made to appear much more attractive, or the capabilities and decision range of Canadian firms have to be expanded.

A number of other companies became established in Mexico through their export sales or licensing agreements there. When the government began to restrict imports, these firms had the choice of manufacturing in Mexico or losing the market completely. Since they did not want to be shut out of a lucrative and growing market, most firms elected to stay and begin local production. Because of formal Mexican legislation and informal governmental pressure, this meant setting up a local joint venture.

In recent years, the formation of a joint venture has in itself often been one of the initial objectives of the parties concerned. Mexican companies wishing to expand their product lines have sought foreign partners which were not already tied to one of their competitors in Mexico. Canadian firms on the other hand have sought quick access to the Mexican market or mineral resources. When these goals coincide, the result has frequently been the purchase of a significant share of the equity in an existing local firm by Canadian interests, or the formation of a new joint venture in which the Mexican partners have been an established Mexican company. Several Canadian mining companies have adopted the latter strategy. Firms with a serious commitment to investment in Mexico start

exploration companies, using their own capital. After locating a viable property they seek out a Mexican partner, usually (though not always) a local mining company with operating experience.

A number of successful joint ventures have been formed through Canadian purchase of shares in an existing Mexican operation. As stated earlier, this strategy of acquisition of a going Mexican concern by foreign interests is frowned upon by the government unless it is clearly a necessary salvage operation. Nor does the government usually object to such purchases when the capability of the Mexican firm will be raised by the infusion of capital and technology and especially if the firm will export or compete with majority foreign-owned companies. In fact it is an additional partial indication of the government's firmness and capability of imposing effective direction upon foreign investment that: "...analysis of acquisitions in Mexico.....have not demonstrated that take-overs have constituted denationalization in Mexico. When a small or moderate-sized firm of any nationality is floundering, acquisition by a resource-rich MNC may be the only way to keep it from going under....................go on to make important contributions to the economy as it builds up the acquisition" (May, 1975, p. 49). In the cases described here therefore, it is expected, by both the Mexican government and the

Canadian interests that the infusion of capital, plus Canadian expertise, has permitted or will stimulate growth of the Mexican acquisition. Eventually it is expected that it will be possible to achieve resale of the shares at a price high enough to recover most, if not all, of the original investment, while the Canadian partner retains substantial minority holdings.

Occasionally, a joint venture in Mexico arose out of other foreign operations. One Canadian company bought a U.S. firm in a different industry as part of a diversification plan. Part of the purchase turned out to be minority interest in a Mexican firm. Apparently, the Mexican operation was very much an inadvertent acquisition for this Canadian investor, but the joint venture has proven to be extremely profitable. In another case, a Canadian firm set up a subsidiary in Mexico to supply components to a major U.S. multinational corporation with which it had dealings in Europe. Subsequently, a Mexican government agency bought into the local subsidiary and the now-joint operation expanded to supply a wider market.

Newer joint ventures, for which information was more readily available, normally have substantial initial direct investments by the Canadian partner, either through loans it arranged, or cash. The Canadian parent firm usually provides critical technology, technical services and know-how, which are not capitalized but charged against revenues of the venture

when it begins operations. Mexican partners frequently, but not always, made proportionate contributions to the capital of the venture. In none of the cases surveyed did the contribution of this the Canadian partner consist of machinery, new or used. Occasionally, the Canadian parent company sold machinery to the Mexican firm, but local managers were careful to note that prices were competitive, the transaction was carried out at arms length, and there was no obligation to buy from a particular source. In one case, used machinery was actually given to the Mexican joint venture, even though the technical assistance agreement did not strictly require such a contribution.

When joint ventures involve the establishment of completely new enterprises, the time necessary for setting up the operation can be substantial. In the mining industry, one knowledgeable executive estimated that 10 years might pass between the opening of an office in Mexico and the commencement of mineral extraction. Much of the intervening period would of course be taken up with exploration, but other steps in the process can also be time-consuming. A manager in the service sector reported spending over a year in fulfilling legal requirements to establish a joint venture. In fact, necessary documents are three or four times as long in Mexico as in Canada. In theory, if all the necessary preliminary work is done carefully and suitable legal assistance is retained, legal requirements can be met in a few weeks. However, in spite of the claims of the legal profession, such as achievement appears to be the exception rather than a common event.

Nationality Issues

Both Mexican and Canadian executives believed that Canadians have a good reputation as potential business associates in Mexico, although there is some doubt about the value of this reputation. Part of this favourable reputation of Canadians is simply due to the fact that they are not Americans. In the words of one of President Lopez Portillo's predecessors, "POBRE MEXICO, TAN LEJOS DE DIOS, TAN CERCA DE LOS ESTADOS UNIDOS". The government and Mexicans generally are eager to diminish their reliance upon U.S. investment and they see Canadians as alternatives to Americans with equal technical expertise. Canadian expertise in mining and geology in particular is known and respected. One or two Mexicans observed that Canadians seem to understand Mexican government policies and fears of foreign control better than do Americans.

Whether this is in fact true or not, it appears a reasonable initial assumption in the light of the common situation of Canada and Mexico as hosts to U.S. investment. It therefore generates perceived empathy that could provide potential benefits for Canadian investors in Mexico, which nation has itself been much more resolute than Canada in resisting dependence upon U.S. investment (probably at considerable cost in terms of the relative stimulus to development of the two host countries over the lst 30 years). This situation has been strengthened by successful contacts between Mr. Trudeau and President Echeverria and between the Trade Missions of Ministers Gillispie and Jamieson and their Mexican counterparts,

in which the latter have consistently promoted a theme concerning "the need to by-pass our great common neighbour." As a result of these initiatives and the underlying good will, Mexican government agencies generally appear especially happy to deal with Canadians.

However, a number of executives noted that Canadians have been hurt by their inexperience in Mexico. U.S., Japanese and German companies have executives with almost a lifetime of experience in Latin America, but there are very few Canadians with that kind of background. Several Canadian firms have in fact had to overcome this shortage by hiring third country nationals to represent them. As another indication of inexperience, a number of mining companies attempted to finance their operations through promotional activities (a practice the Mexicans will not tolerate), thereby giving all Canadian mining companies a bad name. Other companies tried to manage their Mexican activities from Toronto, or failed to allow enough time for satisfactory negotiations or for getting their operations started.

A few firms have failed to master the rather complex immigration regulations and got into difficulties through minor violations. At least one firm attempted to by-pass the processing of visa applications by sending executives into Mexico as tourists for short-term visits, with the result, as might be expected, of considerably extending the period of delay before eventual processing. In such cases the individual is lucky if he is not "thirty-threed" by the President under Article 33

of the Constitution, or expelled by the Minister of the Interior under the LEY GENERAL de POBLACION, as being INCONVENIENTE for the nation. Over the last five years Mexican immigration law has been administered progressively more restrictively. The categories of permits for foreign businessmen are clearly laid out as:

a) Six month VISITANTE - effectively for conference, inspection, feasibility studies, technical trouble shooting or shareholders meeting.

b) Eighteen month VISITANTE - necessary for negotiating or executing contracts, for direct employment in Mexico, or for board of directors' meetings of Mexican firms.

c) IMMIGRANTE EMPLEADO-for acting in principal executive, or long-term technical roles.
(Austin, 1973)

In general Canadian investors have lacked personnel who know Mexico well. For instance, they have also been deceived by the letter of Mexican law, failing to appreciate the potential flexibility in its interpretation and administration. On other occasions they have failed to prepare their arguments and clarify their requirements sufficiently before signing preliminary agreements with Mexican partners. Mexicans involved with foreign investors noted that most Canadian businessmen do not appear to avail themselves of the opportunities for becoming acquainted with Mexico, through Conference Board meetings or through the offices of the Canadian Association for Latin America, or the Canada-Mexico Committee, or business groups (although the Canadian Government is well represented).

One of the major disadvantages cited with respect to Canadian investors was their lack of reputation and status in international business circles. Many of the Mexican investors interviewed said they preferred to deal with large, well known partners - the "Fortune 500" companies - which had substantial international experience. One of the basic reasons for this conservatism is that even institutional investors lack the capability to conduct a sophisticated analysis of prospective partners' non-Mexican operations. Since few Canadian companies fall into the category of major multinational companies, this attitude would seem to suggest that smaller firms are likely to have difficulty in establishing themselves in Mexico.

On the other hand there are some saving features in the situation. In the first place most of the major multinational corporations are already located in Mexico and tied up with various local partners. Any Mexican interest which is not already matched with an MNC partner will probably prefer not to become a junior (because most recent) partner to other Mexican firms. It will tend to look for a new foreign match where its local status and potential influence over a joint venture are likely to be greater. This in turn has the effect of increasing the opportunities available for competent but internationally less-prominent firms. In fact it was repeated by several respondents that there are many family-owned local firms that need additional capital or

know-how and provide good potential opportunities for joint ventures to Canadian investors. Secondly, in an international investment environment where governments of developing nations indicate increasingly vociferous concern over the threat of economic imperialism by large MNCs, there are some intrinsic benefits in being capable but small - and therefore relatively unthreatening (Farmer, 1975).

Perhaps the situation with respect to benefits of Canadian nationality is best put into perspective in that no respondent could point to specific advantages in being Canadian, aside from a friendly reception from the government. Moreover, two of the large Canadian firms in Mexico actually had difficulties with associated Mexican joint ventures in 1976 - one venture was terminated, another suffered long delays in its establishment. In neither case was the local government prepared to extend special consideration to the Canadian partner and it even used a strike to eliminate one Canadian-owned firm from a market where the latter competed with a state-owned company. Clearly these firms obtained no benefits from being Canadian. The argument in the previous paragraph above might suggest that the government's antagonism was provoked by the threatening size and competition of these two foreign interests. If so, then size, as might be expected, is likely to prove dominant over nationality as a determinant of governmental attitudes towards foreign investors in Mexico (Tomlinson, 1977).

Taxes

Mexico, like other nations with sophisticated governments, has an elaborate system of taxation. However, like other developing nations, the specific interpretation or application of tax regulations and the efficiency of tax collection are somewhat inconsistent. There are in fact eight types of federal taxes:

Income Tax
Commercial Revenues Tax
Excise Taxes on Manufacturing, Commerce and Services
Excise Taxes on the Exploitation of Natural Resources
Import and Export Duties
Stamp Tax
Contributions to: Social Insurance
National Housing Fund
Employees' Profit Sharing
Payroll Tax
Inheritance and Gift Taxes (which hardly ever effect firms).

and four (less important) types of state, territory and federal district taxes:

Tax on Income from Capital
Real Estate Levy
Real Estate Transfer Tax
Surtax

Details of these taxes require interpretation by a tax consultant specialising in the Mexican tax system, although useful non-technical exeuctive summaries are available (ZAMARRIPA and CHEVEZ, 1973).

The focus of discussion in this study was not upon details but upon some of the general reported impacts of taxation upon joint ventures in Mexico. By law and in general practice, joint ventures with over 50 per cent Mexican ownership are treated on the same basis as companies without any

foreign ownership. There is a special sub-set of tax regulations applying to the mining industry which actually caused most Canadian and other foreign-owned companies to "Mexicanize" (i.e. change their capital structure into joint ventures with majority ownership by Mexican partners) even before more specific regulations to that end were introduced.

Another issue which concerned Canadian partners was the tax on charges for technical services by foreign firms to joint ventures. These are charged at 42 per cent (the corporate income tax rate on earnings of 1,500,000 pesos or more), so that in effect all charges are treated as net profits. As a result, foreign firms cannot charge for these items at a level which would create a normal profit on such transactions without imposing excessive costs upon a client joint venture which would tend in turn to cripple the latter's profitability. To cope with this situation, Canadian partners normally send individuals to work in a joint venture and simply charge the latter for their employee costs without attempting to make a profit from the transaction. Overall, Canadian managers reported that Mexican taxes were high but tolerable under the circumstances, since rates of return upon investment in Mexico were generous enough to compensate for local tax levels.

Division of Responsibilities Among Partners

In virtually every joint venture surveyed, the Canadian partner avoided any major involvement as a corporate entity in

the management of the organization. This condition prevailed when management was exclusively Mexican, as well as in the cases where one or more senior executives were Canadian or third country nationals. The Canadian partners exerted influence through the boards of directors, meetings with local managers, and through technical leverage. Mexican partners were even less active as a rule, confining their intervention to directors' meetings. Meetings of boards of directors are more akin to executive committee meetings; they are usually frequent with few, if any, formal votes.

A comment repeated very often by respondents of all types was that Mexican investors expect foreign partners to be represented by senior executives with considerable authority, preferably sufficient to commit their own firms with little or no reference to corporate head-quarters. They also prefer situations where the foreign executives are suitably simpatico for them to form close personal ties. Such ties are felt to be a much sounder basis for trust than simple mutuality of corporate interests and a much more civilised and suitable basis for doing business. When the subject came up, all respondents agreed that the exact division of ownership and its implied impact upon control was not important to the success of an enterprise. As one Canadian executive put it, " a good partner is a good partner, whether we hold 60 per cent of the shares or 40 per cent."

The broad functional area in which the respective partners exercised the greatest influence were relatively clear.

Canadian partners were usually most interested in and had the greatest authority in financial matters. This situation arose from the level of provision of capital by Canadian interests and their virtually universal practice of guaranteeing loans made to the joint venture (frequently by Canadian banks with whom the parent firm normally dealt, although some loans were obtained through some of the more aggressive U.S. banks). Thus Canadian partners were frequently able to exercise a virtual veto over major expansion, development of new products, purchase of other firms, major capital acquisitions, etc., because of the importance of their role as providers of capital. In fact several respondents stated that in the early stages of a joint venture, management was expected to provide extensive financial reports to the foreign partners in order to reassure them that funds were being properly and carefully expended. As the venture and, perhaps even more importantly, the relationship between the partners, became established, less detailed reports were necessary.

The importance of the role of the foreign investor in Mexico described here as a provider of capital and foreign exchange for local operations, especially in a developing host country, is consistent with some of the traditional theories of foreign direct investment and development (Nurkse, 1953). Foreign capital is currently still a basis for leverage in Mexico, since the nation's savings coefficient is around 18% and its investment coefficient just over 20% (I.D.B.,1973).

These fall well below the levels of 24% and 26.5% respectively, calculated by Prebisch as necessary for significant reduction of unemployment and increase in the rate of growth of GDP for Latin American countries (Prebisch, 1970). However, the recent verification of Mexico's large reserves of Petroleum (BLA, May 11, 1977 p.150) suggests that the country's development may well change from being primarily capital-limited to being technology-limited. This in turn will alter significantly the rules of the game for foreign investors in Mexico. Their value will tend to be judged by the government almost entirely in terms of the technology, skills and export market access which they offer and less on the capital they provide or have invested in the past.

Fortunately therefore, the second major area of Canadian influence was technology, defined broadly here to include not only patents and trade marks, but also managerial or technical skills and resources. Virtually all this sample of joint ventures deal in products or services which were developed in Canada and licensing arrangements leave control over the use of these commodities in Canadian hands. In industries where Mexican expertise or experience are limited, this situation is further controlled through a management contract between the joint venture and the Canadian parent firm. In board of directors' meetings, Mexicans typically defer to the Canadians when these issues are discussed. Technology is transmitted in several ways. Many joint firms

send key personnel to Canada for training. Normally the joint venture pays their salaries, but no further charges are made by the Canadian partner. Canadians or other foreign technicians are also sent to Mexico, especially for start-up or trouble-shooting roles, but typically only for short periods and rarely in large numbers.

Areas of Mexican responsibility are also clear and predictable. As one Mexican director stated, "The Canadians have the 'know-how', we have the 'know-who'." Thus Mexicans tend to direct the critical areas of relationships with the government, industrial relations, decisions about plant location, market assessment, etc. A foreigner, no matter how familiar with Mexico,cannot deal very effectively directly with the government on major issues, but must be represented by a Mexican. One of the respondents with a twenty five year career in Mexico,said that he would never go to the government alone but would either send a knowledgeable, well-connected Mexican, or at least have one along with him. Since most Mexican partners have close ties with at least one Mexican bank, they are able to rely upon these connections to influence the local decision-making elite and bureaucrats as well as in assisting the joint venture with local financing.

A number of other functional areas are handled jointly or else vary in their treatment. Some of the joint ventures participate with other affiliates of the Canadian parent firm

in purchasing or sales, where such arrangements are appropriate. In a number of manufacturing firms, local managers proudly noted that the Mexican venture had even contributed to technological innovation in Canadian-designed products. Most of these developments were adaptations in processes designed to accommodate the relatively short production runs appropriate to the Mexican market, or were products designed to meet special conditions encountered in Mexico with respect to climate, terrain, etc. In a few cases, items developed in Mexico complemented the parent firm's product line and were sold in third countries. Despite these occasional exceptions, there appeared to be little R and D capability developed in any of the joint ventures in the sample. They will continue to rely on imported technology for many years.

Mexicans predominate in the management of the joint ventures studied. In no case were more than two Canadians permanently employed, and in several firms there were no foreigners. In some cases parent companies with extensive Latin American operations had posted third country nationals from other Spanish-speaking nations to executive positions in Mexico for fixed periods while Mexican replacements were being trained (in Mexico or elsewhere). Both Mexicans and Canadians generally agreed that competent managers could be hired or developed in Mexico, though not without some difficulty. Immigration laws restrict the percentage of foreign

employees a firm may hire (Austin, 1973), although, as discussed earlier they are flexible enough to permit temporary assignment of foreign personnel for starting a new plant, maintenance, troubleshooting, training, etc.

The law itself is merely the formal mechanism for achieving an important national goal. Both the government and Mexican partners want to see Mexicans in some of the senior management positions of a local operation, or at least evidence of plans for developing such people. However, Mexicans do not apparently object to a succession of foreign chief executives in local joint ventures, although they judge their performance by high standards. This not really evidence of inconsistency in Mexican attitudes. It is more an indication of sensible pragmatism for several reasons. First, whatever the dictates of national pride, they are also served by success and a joint venture is more likely to be successful if run by the most capable top executive available. If such a man is a foreigner, so be it. Secondly, there is likely to be a positive correlation, recognised in fact by several of these respondents, between the nationality and corporate links of a top executive in a local affiliate and the degree of commitment of a foreign parent company to the success of that affiliate. In other words, a top-level expatriate executive will have direct ties to headquarters. Thirdly, development of competent Mexican executives is an important goal and has at least greater possibility of fulfilment

the better and more experienced the chief executive officer.

One aspect of business relationships in Mexico which came out very strongly and frequently in these interviews was the importance of language as a prerequisite for a foreigner's success in local business operations. English is universally recognised as the lingua franca of technical aspects of business and many commentators on international communications stress the primary importance of empathy over linguistic fluency. In Mexico like France however, empathy is apparently not enough. It is important to Mexicans, even though they may themselves be fluent in English, that foreign businessmen be able to speak Spanish and such an ability is probably a necessary lubricant for effective continuing business contacts. The implication therefore is that, while it may be tolerable, though a second-best situation, for a foreigner to rely upon Mexican skills in English for a short introductory period, Mexicans clearly expect foreign managers to be able to speak Spanish soon after their arrival in the country - as well as being open to and forming with local mores.

Most firms reported that relations between the partners were informal, at least after a running-in period while the relationship developed. Many examples were cited of services or contributions provided by or for a given joint venture beyond the requirements of the formal agreement between the

partners. Typically, these "extras" were not even assigned a cost, and no charge was aked or compensation offered.

Overall, it appeared that Canadians were able to direct the broad policies of the ventures to the extent they felt necessary through their control of funds and technology. There was no indication from these interviews that this situation was expected to change. However, as discussed above, the generation of revenues from successful exploitation of Mexico's oil reserves and the resulting availability of Mexican capital may change this underlying balance of power in the long run. "Mexico may be relatively far from God, but it is providentially close to large amounts of petroleum" (Fagen, 1977, p.697).

Dividends and Other Payments

The most important type of returns to the Canadian partner in these Mexican joint ventures was dividends. Except for a few companies where no dividends had yet been paid, in no case were earnings on licensing or technical assistance agreements as important as dividends. The Mexican government regulates carefully the payment of fees and royalties for technical assistance agreements and the use of patents or trademarks. The 1976 industrial patents law in particular will regulate the use of trademarks and patents.* In fact

* Ley de Invenciones y Marcas (February 5, 1976).

this law eliminates patenting altogether in pharmaceuticals, food processing, agricultural, agrichemical, nuclear energy and antipollution industries. In these industries firms can apply for "inventors' certificates" (certificados de invencion) which permit royalties to be paid, but make the technology concerned available to any Mexican firm that requires it.

The government does not usually permit such payments to exceed three per cent of sales and frequently requires lower charges to be levied. Basically the royalty level permitted seems to be a function of the value the government places on the technology in Mexico. Moreover, sophisticated Mexican investors, individuals and institutions, believe that foreign corporations have charged too much for technical expertise in the past and are wary of such agreements now.

Several joint ventures were phasing out their technical assistance contracts. In some cases this was because the Mexican firm had become capable of making some contribution itself to the Canadian partner's technological capabilities. In others the initial investment in necessary technical assistance had been made and the mature joint venture was paying generous dividends. In the mining industry, the normal practice is to charge exploration costs against the first revenues of the operation, and to grant one of the partners a "non-profit" management contract. Dividends are then considered to be the means of generating a return on investment. In contrast to its

treatment of technical assistance, the Mexican government has no restrictions on the payment of dividends, although they are subject to a 21% withholding tax if paid to a foreign corporation or individual or to local residents.

Predictably, all joint ventures contacted had clearly established, or were in the process of formulating, a policy regarding dividends. Several respondents observed that it was most important that these policies should be spelled out specifically at the time when the partners are forming the joint venture. As mentioned earlier, given the relatively high normal rate of return on fixed return investments in Mexico, local investors expect dividend rates that are generous by Canadian standards. Comprehensive return on investment data were not sought as part of this study. Some indication of the levels of such returns is available from U.S. Department of Commerce figures, which show that U.S. firms earned over 17% (including royalties) on the book value of their investments in Mexico in 1975.

However, it is not uncommon to find agreements between partners to delay the payment of any dividends from a joint venture for several years in order to provide funds for reinvestment. Differences in viewpoints between the partners in Mexican joint ventures appear to be diminishing in general as the local partners gain greater appreciation of the long-term benefits to themselves arising from reinvestment and equity growth. Interestingly enough, at the same time

Canadians are becoming more interested than formerly in dividends from their Mexican investments. In no case did the dividend policy call for payments to exceed 55 per cent of the earnings of the joint venture and in no case the requirement was that the firm should only distribute 20%.

Relations with Government

Much of the information for this study was gathered during the final six months of President Echeverria's term of office. Not one respondent, Mexican or Canadian, spoke favourably of his government's policies towards business and investment (foreign or domestic), although several praised the improvement in the quality of the bureaucracies in several ministries during Echeverria's presidency. Businessmen were hopeful that President Lopez Portillo, who took office on December 1, 1976 would be more sympathetic to the private sector and generally seek to improve the business climate.

One of the first policies of the Lopez government was to create an "Alliance for Production" under which government business and labour would operate in harmony "for the good of the country." In their relief at the end of the Echeverria regime, business representatives made a commitment in December 1976 to invest $5 billion during the six year term of President Lopez. In March 1977, President Lopez signed another $4.5 billion combined public and private sector

investment programme. There are already signs of strain in the "Alliance for Production" however. In spite of an extensive price freeze on over 270 products, unions are claiming that prices are not being effectively controlled.

Government regulation of business in Mexico, by law and administrative direction is extensive. Several specific aspects of this regulation affect joint ventures. A number of industries, radio and telephone communications, oil and petrochemicals, power generation, rail transport, for example, are virtually reserved to the state and are closed to all foreign investment. Activities reserved exclusively for Mexicans include road and air transport, gas distribution, land ownership in coastal and border zones. Other industries where foreign investment is already prominent or Mexican capabilities are deemed sufficient, such as chain store retailing, appear to be closed to further foreign participation by government ruling. Canadian firms operating in Mexico, however, did not find these restrictions particularly onerous. Many are clearly stated in the law, while others are well known to lawyers, consultants, Embassy personnel, etc. Thus no foreign investor need waste large sums preparing for a joint venture where there is no chance of receiving government approval.

Moreover, there are benefits from official regulation. The government protects Mexican firms in a variety of ways, through taxes, export benefits, tariffs, etc. These protections

extend to joint ventures with majority Mexican ownership on a par with completely Mexican firms. A number of firms in the sample have no domestic competition in one of their product lines. They are also effectively protected from any foreign competition through import restrictions and tariffs.

Management views of government on an operating level varied somewhat according to the ministry most often faced. In general, the government was described as pragmatic in dealing with business. Most respondents spoke highly of the competence and diligence of the Ministries of Industry and Commerce and Treasury (Hacienda). Senior officials there are involved in daily problems and deal knowledgeably with issues raised by the firms. At least two of these Canadian managers prefer dealing with the Mexican government ministries to dealing with their Canadian counterparts. However, routine procedures, such as incorporation or merger are much slower and involve more paperwork in Mexico than Canada. Many transactions involve negotiation rather than strict application of a law or administrative regulation. Most firms were subject to price controls, and price changes were customarily negotiated with the government. However, when emergencies arose, the need to import spare parts after a breakdown for instance, government response was sympathetic and rapid.

Mining companies appeared to have less favourable views of government. For one thing, they deal with three ministries

(Industry and Commerce, National Patrimony and Treasury) who do not always agree among themselves. Moreover respondents gave the impression that Patrimony, like a number of smaller agencies with whom they dealt,were not as competent as Finance or Industry and Commerce.

Smaller firms contacted reported that they had few dealings with the government and their foreign ownership did not provoke special attention. In at least one case, the firm did not have the requisite level of Mexican ownership, but its efforts to find local partners were well known, so there are no pressure from the government, direct or indirect, to Mexicanize.

News of bribes paid by foreign corporations in several nations was fresh at the time of the interview, and the subject arose frequently. All respondents agreed that bribery is unnecessary and even foolish to contemplate in dealing with federal ministries or major issues. Import permits, for instance are normally issued without extra consideration. Many firms have never paid any bribes for any purpose. Others admitted that payoffs occur, but only on petty matters such as parking, municipal services, labour negotiations, etc. Large sales to government bodies apparently involve some payoffs. A few Canadians have come to Mexico expecting to pay off everyone and have earned a reputation of being involved in bribery, which insults some Mexicans and tempts others who

might not otherwise expect payment. Several respondents stated that partners contemplating a joint venture should agree in advance on a policy in this area.

In most cases, as described earlier in this report, agencies of the Mexican Government apparently make an assessment of the value of any proposed foreign investment to the nation. If the assessment is positive, then official treatment is generally favourable,pragmatic and flexible, though often slow. If the assessment is negative, the venture is probably doomed unless substantial changes occur. Basically however, "the Mexican Government wants to discuss and wants to find a way to accomplish what the foreign investor wants. Of course there are certain limits in the Foreign Investment Law beyond which they cannot go. But normally, they have a dialogue, they are amicable, and they would like to find a way by which both parties can come to a reasonable solution" (Escobedo, 1975, p.69).

Views on Joint Ventures

In practical terms, there is no alternative to the joint venture form of investment for most firms seeking to become established in Mexico. Firms organized before the law required Mexican ownership are not required to increase Mexican participation unless they wish to expand their product lines or physically expand beyond the boundaries of

present plant sites. However, a number of respondents discussed their views of joint ventures as separate considerations apart from the legal requirements they faced.

On the whole, they found joint ventures at least satisfactory. One or two expressed a strong preference for maintaining full Canadian ownership if this were possible. Several other managers stated however, that they actually preferred joint ventures because of the assistance which good Mexican partners could provide, indicating they would opt for joint ventures even in the absence of any requirement. No firm contacted reported serious problems arising from the fact of having partners from two nations. Several persons with experience in other joint ventures reported that where problems and failures arose in these firms they were really caused by normal risks of business, such as insufficient markets, low quality ore deposits, poor management, etc. One Mexican partner recalled an unsuccessful joint venture in which each partner assumed the other was familiar with the market to be entered. When they realized that neither of them understood the circumstances to be faced, the joint venture was quickly terminated.

Perhaps the strongest indication of the acceptability of joint ventures to these Canadian firms lay in the fact that several firms in the sample had plans to undertake other joint operations in partnership with a Mexican firm, sometimes with

another foreign company. This positive and pragmatic response is consistent with the argument that business folk-lore concerning joint ventures is inconsistent. Firms with actual experience of this mode of operation are generally more inclined to consider objectively future joint venture opportunities. The most inhibited firms are usually those which have never actually been involved in joint ventures themselves. (Tomlinson, 1970). Typically, the new ventures would be set up in order to enter a new market, permit vertical integration, or develop a newly discovered ore body in Mexico. One firm planned in fact to establish joint ventures elsewhere in Latin America, relying on its Mexican experience. One of the more unusual cases involved a Canadian partner, which expressed a preference for full ownership of its foreign activities. This firm had a subsidiary in Mexico (which was actually a third tier company based in a third nation) and the Mexican operation had successfully resisted local pressure to convert to joint venture status in Mexico.

Transactions Between the Partners

A number of the parent firms in the sample conducted transactions of various types with their Canadian or Mexican partners or with third-country enterprises associated with the partner. One of the Canadian mining firms sells ore from its international sources to its Mexican partners. Local manufacturing firms often purchase components abroad from companies

with which they are affiliated in joint operations in Mexico. At least one Mexican manufacturing company sold minor quantities of several products to the U.S. member of the Canadian-owned corporate group.

In all cases except the last one cited above, respondents maintained that the transactions were conducted as if they were on an arm's-length basis, that is, prices were competitive and each partner had the option of buying or selling elsewhere. The exception was the firm selling in the U.S., where selling prices of the imported goods were above levels at which the items could actually have been produced there. This situation was reconciled by a number of special circumstances. On the one hand the American affiliate was described as purchasing the goods in order to assist the Mexican firm in meeting its export quotas. In any case, the quantities involved were insignificant in terms of the U.S. market and this supply strategy avoided the need for the U.S. affiliate to set up additional production facilities of a marginal nature itself.

Exports

The Mexican Government encourages exports of manufactured and processed goods, and firms with foreign ownership are often under a degree of pressure to export some of their production. Amongst the specific incentives offered for exports, the cases of CEDIS and other tax and tariff-related incentives were

discussed above. A similar effect is sought through the practice of linking import quotas for certain finished goods, which may be otherwise prohibited, to the quantity of finished goods exported by a firm. Further, the qualifying conditions for incentives include the provision that the Mexican firm must prove that they are not involved in any contracts which limit their ability to export.

Some of the more recently involved Canadian partners had agreed to try and achieve export targets for a joint venture when they were negotiating for permission to commence operations in Mexico. Virtually all the mining and manufacturing joint ventures had sold some products abroad, although the manufacturers had seldom been able to export more than 10 percent of their output. The main difficulty they faced was meeting price competition abroad, even though certain raw materials (principally mineral ores) were sold to local manufacturers below market prices in order to stimulate exports. This condition is not universal for all raw materials (some being more costly in Mexico than elsewhere), and does not seem to have had much impact.

Production costs in Mexico were said to be influenced by relatively short production runs and until late 1976 by an overvalued currency. A number of respondents reported that exports had been higher in the past, but that recent Mexican inflation had made foreign sales impossible. The most frequent destinations for exports were the Central American countries,

followed by the Caribbean, Northern South American and Asia. Two joint ventures sold goods in the Southern U.S.. In general, no problems were cited with respect to product quality or acceptance in foreign markets, except in terms of price.

Conclusions and Recommendations

In the course of this report, and especially in the comments in the section, Summary of Responses Concerning Canadian Joint Ventures in Mexico, a number of specific, mainly company-oriented, suggestions have been made or implied. This final section covers briefly some recommendations which are of a more general nature, many of which are seen as being of more direct concern for the Canadian Government.

1. Suitable Rates of Return

A suitable rate of local return on a foreign investment is difficult to specify for particular cases and almost impossible to generalise accurately for a given country, except in simplistic or arbitrary terms. It varies with the nature of the local operation, its degree of integration into the Canadian investor's global operations, the stage of the technology involved, its significance and the level of Canadian commitment-all coupled with various aspects of the risks involved. There was little evidence that these factors had been evaluated in systematic fashion by Canadian firms for their Mexican investments. Efforts were certainly made in some cases to hedge in various ways against exchange rate risks to existing investments when the dangers of such risks became obvious, as was the case in 1976. None of these Canadian investors appeared to have developed or applied to the Mexican cases any of the organised techniques or models of risk evaluation readily available in

the literature of the field (Hertz, 1964; Robock and Simmonds, 1973; Radford, 1975). The level of sophistication in such decision analysis was limited to analogues of the "Go or No Go" or the rough "Premium for Risk" types of procedure (Stobaugh, 1969).

In such circumstances, it is difficult, even for the firms themselves, to determine accurately either the desirability of a particular investment opportunity, or its performance once undertaken, unless the latter is evaluated on an integrated global return on investment basis. As a result, while a commonly cited figure is over 20% net of tax, it appears inappropriate on the evidence available to attempt to indicate a suitable rate of return for Canadian joint ventures in Mexico. Nor is it very useful to comment upon their performance, except in the relatively subjective terms of the firms' own level of reasonable satisfaction with the returns from their Mexican joint ventures. Further, it is virtually impossible to indicate comparative values between Mexico and other potential or existing investment locations, except in similarly subjectively-derived terms.

While far from unique to the case of Canadian firms (Stobaugh, 1969), this particular limitation has been described in other studies of Canadian foreign investment (e.g. Tomlinson and Himmelsbach, 1973). Development of appropriate risk evaluation models and sectoral R.O.I. studies for potential host countries such as Mexico on a comparative basis is probably a necessary condition to increase the effectiveness of Canadian operations abroad. Ideally, this would involve three groups of protagonists.

Government, through the Department of Industry, Trade and Commerce, to provide stimulus, joint funding and centralised staff services, plus data inputs through field officers in embassies and consulates abroad. Firms, to recognise a need for commitment of resources to resolving the problem, provide data inputs, test and evaluate models and results. Academics and consultants, to provide data inputs, develop, refine and test models.

2. Availability of Local Partners

With respect to the availability of local partners for Canadian investors in Mexico, the study has indicated that there is considerable untapped potential. In terms of their international status and reputation, few Canadian firms can automatically attract a crowd of local suitors. However, less-developed nations, especially Latin American nations, are becoming increasingly concerned and selective over the costs and limitations of technology transferred by the major multinational corporations. This was indicated most recently in the 18 month Conference on International Economic Cooperation - the "North-South Dialogue" - which ended in June, 1977, and in the recent policy recommendations of the U.N.'s Economic Commission for Latin America (ECLA) at its Guatemala conference in May 1977. These nations are also concerned over other aspects of potential economic control and dysfunctional dominance by large foreign

firms. For both these reasons, the climate for smaller firms with appropriate technology to offer, a description which fits many Canadian firms which have not yet even ventured abroad, has become much more sympathetic.

In any case, so far as potential Mexican private investors in joint ventures are concerned, most of the attractive MNCs which are interested in Mexican investment opportunities are already tied up with local partners. At the same time, as BANAMEX respondents pointed out in the course of the study, the Mexican business environment is dominated, in numbers at least, by small firms. An interesting additional argument here is the finding in an earlier study that smaller firms appear to show a higher level of profitability in Mexico (Good, 1972). The combination of these factors appears to stress the importance for Canadian firms to seek out small and medium-sized local firms, especially family-owned interests, in Mexico as a promising source of potential joint venture partners.

3. Development of Reliable Information on Local Opportunities.

A theory of convergent polarity would perhaps suggest that in this situation, the favourable sea change in the environment, coupled with a cumulative impact of highly-rated information form trusted sources such as existing Canadian interests in the country would, if left to themselves, lead

to a growth in the number of Canadian joint ventures in Mexico. The presence of one such joint venture becomes a stimulus or focus for others, especially in terms of trusted information vis-a-vis suitable potential partners. There was evidence in the study of considerable spill-over effects of this type, both before and after investments were made. Canadian firms in, or interested in, Mexico naturally tend to look for help and advice from Canadian consultants, banks, or other Canadian firms.

If however, this type of development is considered desirable in Canadian and Mexican interests, the natural unstimulated process of growth may not operate fast enough. If either of the two governments wishes to speed up the process, directed intervention is necessary. While incentives, the first recourse of governments in such a situation, are attractive, the respondents to this and other studies suggest that they are rarely a primary, critical decision criterion. More important are accurate, reliable, comprehensive information regarding opportunities, together with a generally perceived consistency in environmental conditions.

Local Canadian Government representitives in Mexico stated that they spent a considerable amount of time in dealing with what turned out to be trivial requests for information and contacts from uncommitted potential Canadian investors. This time was said to be taken at the expense of developing other promising Mexican contacts and opportunities. Often

the Canadian businessman appeared to be doing little more than justify his expenses or PEMD subsidies for a trip to Mexico. Yet some of these relatively cold canvassing sorties do generate markets or opportunities and must not be thrown out with the bathwater. There must therefore be a better system of pre-instructing interested businessmen and screening the needs of Canadian firms, possibly before they even leave Canada.

If the Canadian Government wishes to stimulate investment and trade abroad by Canadian firms, there is need for greater precision in its informative role. The spectrum of information available through the multiplicity of sources and services may be adequate - it is certainly voluminous. The apparent ignorance on the part of Canadian investors concerning information and services available, or more importantly, how to utilise them, suggests two things. First, that the information may not be precisely matched to its potential user's needs. Second, that procedures for accessing and utilising services effectively are either not clearly organised, or are not clearly understood.

Resolution of this problem will not be achieved just by an expensive review and macro-recommendations by high-level O and M consultants. A more effective approach would probably be to generate a series of country-specific studies by combined teams of government, corporate and academic representatives.

Their mandate would be to:

i) verify the adequacy and accuracy of existing information or sources with respect to each country,

ii) devise effective procedures for interfacing information with potential users,

iii) work with the promotional services of the government to improve the impact of presentation,

iv) continue in an advisory and generative role to monitor and improve information transmission between Canadian interests and their countries of responsibility.

Many suitable potential components of this organization are already in place, in government departments or field offices and in bodies like C.A.L.A., C.E.A. or the Canada-Mexico businessmen's groups. Their current activities are however, too diffuse and their resources too limited to effectively carry out the role envisaged here. However, C.A.L.A. in particular is already planning a more ambitious programme of activities: "one special feature.....is to find ways of identifying investment opportunities in Latin America at earlier stages of any project's conception than is generally possible by using normal channels of information... and being able to unearth a possible joint venture project while it is still only a 'gleam in the eye'. " (Lubbock, 1976).

4. Importance of Personal Contacts

The emphasis in some of the above points has been upon possible activities by the Canadian Government and its representatives. An underlying theme however, is the importance of personal contacts in developing successful

projects, a major feature of the Mexican business culture. In this context a circularity problem arises. New Canadian candidates for Mexico need personal contacts to make negotiations effective, but, almost by definition, lack such contacts because of their inexperience in Mexico. Mexican executives in a similar situation with an unknown Canadian suitor seek information from other Canadian firms or other foreign related groups (such as the Price Waterhouse Alumni network) who are already trusted members of the informal web of business contacts in Mexico.

This type of informal network is probably difficult for the Canadian Government to penetrate effectively. Participation and development of such contacts are easier for Canadian banks, accounting firms and consultants, who should be encouraged to increase their own role as potential marriage brokers or counsellors for joint venture opportunities in Mexico. Amongst other possible mechanisms, they should develop a well-organised referral service. A possible supporting and facilitating role for the Canadian Embassy might be for example, to encourage, even host, regular weekly lunch meetings of Canadian businessmen in Mexico, to aid the development of a Canadian sub-network.

5. Seminars and Case Studies Relevant to Mexico.

Intensive case studies of successful and unsuccessful Canadian joint venture experiences in Mexico are lacking in the

business literature in Canada. These would be particularly valuable as inputs to seminars for Canadian businessmen on negotiating and operating such joint ventures. A programme of such seminars to be offered across Canada would serve three useful purposes.

a) They would help to sensitise businessmen to joint venture opportunities in Mexico.

b) Interested Canadian firms would have available a model of entry strategies and sequential programming for the development of such ventures, which could even be tailored on sector, industry or firm-specific bases.

c) Examination of past problems, failures and errors should help to avoid the costs of their recurrence and repetition.

A fourth purpose might well be added if the audience were changed to a Mexican environment. From a Canadian point of view it should be beneficial if Mexican executives also became more aware of actual events that had occurred, coupled with a better understanding of Canadian perceptions of the impact and significance of those events. Both seminars and case studies would, in other words, provide a better basis for mutual understanding prior to future negotiations and to on-going operations of Canadian joint ventures with Mexicans.

A by-product of this study will be the preparation of cameos, or brief cases which could become the introductions

to more intensive cases of the type described here. A more generalised account of the negotiation process with respect to joint ventures in the Latin American context is developed in the companion report on Canadian joint ventures in Brazil. Because of the many similarities in the negotiating process for Mexican and Brazilian situations and in the interests of brevity, the latter account has not been repeated in this report. Since however, this report has already stressed most of the Mexico-specific issues, creation of a Canada-Mexico version of the negotiating process on demand would be a relatively simple transformation and can readily be made available.

6. Mexican Trade Missions to Canada

From a simplistic point of view, sponsorship of trade missions of Mexican businessmen to Canada clearly serves the interests of those businessmen and could be seen therefore, as purely a Mexican responsibility. Pursuing the theme of improving inter-nation business contacts however, they are also likely to create a basis for increasing awareness and familiarity between businessmen of the two nations. This, in turn, is likely to serve Canadian interests in terms of the growth of personal contacts, with the potential benefits described in other recommendations above.

This argument leads to the suggestion that the Canadian Embassy offices in Mexico and business or industry groups in Canada should encourage, perhaps even sponsor jointly with Mexican interest groups, the growth of such missions to Canada. The assumption, is made, in parenthesis, that steady growth in Canadian missions to Mexico is already being encouraged and would be further stimulated by the type of activity proposed in several of these recommendations. As a preliminary format, it is further suggested that Mexican missions to Canada should be organised on a combined industry/region basis.

7. Scholarships for Mexicans in Canada.

In the long run both inter-nation familiarity and the creation of a potential cadre of trained Mexicans, oriented towards working with or for Canadian-associated firms, are likely to be encouraged by exposing more young Mexicans to the Canadian environment. This type of familiarity has already worked very successfully for U.S. interests in Mexico. It is therefore recommended that a number of Canadian scholarship programmes for Mexicans should be created. Sponsorship should be by Federal and Provincial Governments and by Canadian business groups. Various levels of programme and degrees of specificity of exposure should be envisaged. On the one hand, these could range across in-firm, local college, undergraduate or graduate levels. On the other they could be focussed upon general, technical, operational, professional and even R & D.

as areas of concentration. A detailed proposal for the structure, scope and administration of such a programme can be prepared by the Division of International Business at U.B.C. if required.

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