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CEPAL REVIEW
First half of 1978

Transnational corporations and export-oriented primary commodities

A general conceptual framework for case studies

*Benny Widyono**

This article presents in some detail a general conceptual framework intended to provide guidelines for the study of negotiations between governments and transnational corporations in connexion with export-oriented primary commodities. If the developing countries have greatly improved their bargaining position *vis-à-vis* the transnational corporations during the past few decades, this is due not only to changes in economic and political power relations at the world level but also to the pooling of increasingly detailed knowledge of all the factors which strengthen the hand of the governments in their dealings with the corporations.

The agreement concluded in each specific case between transnational corporations and governments depends upon a constellation of interrelated factors, pre-eminent among which are certain economic, political and administrative characteristics of the host countries, the nature of the commodity concerned and its world market, the basic features of the corporation, and the international scenario in which the negotiation is conducted. After describing these factors, the author shows the complexities of the negotiation process, the various types of pacts and agreements that have been established, the direct and indirect gains to which they give rise and the ways in which the host country can participate in these.

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A. Introduction*

In July 1977, an *aide-mémoire* was signed between Mr. Enrique Iglesias and Mr. J.B.P. Maramis, the Executive Secretaries of CEPAL and ESCAP, respectively, dealing with the possibilities for regional co-operation between the two regional commissions in the field of transnational corporations.[1] In this *aide-mémoire*, the two Executive Secretaries agreed to co-operate in the conduct of case studies on the involvement of transnational corporations in export-oriented primary commodities of interest to both regions. Provision was made for the gradual extension of this co-operation to other interested regional commissions.

It was agreed that all case studies should have a common focus and should concentrate on the specific issues surrounding the following two areas of concern:

(1) Factors determining the relative *bargaining positions* of host governments and transnational corporations;

(2) The resulting *structure of distribution of gains* between the host countries and transnational corporations.

The emphasis in the case studies will therefore be on the bargaining process between the two parties concerned. It is

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[1] *Aide-mémoire* between the Executive Secretaries of CEPAL and ESCAP on Interregional Co-operation among Regional Commissions in the field of Transnational Corporations, Geneva, 26 July 1977.

believed that the interplay of several key factors in the government's bargaining position will be very important in determining the outcome of the negotiations. These in turn will result in an agreement which determines the structure of the distribution of gains accruing from exports of primary commodities.

The dimension and complexities of the problems vary from country to country, from commodity to commodity and from project to project. Generalized policy recommendations to host governments are, therefore, difficult to formulate at the present stage and will have to await the accumulation of enough evidence from case studies being undertaken by researchers in different parts of the world and for as many commodities as possible. The underlying approach to the case studies to be carried out in this interregional project will, therefore, be that of *descriptive pragmatism* rather than *prescription*. In order to provide a common focus and aim to all the case studies, a general conceptual framework applicable to all case studies has been developed and is presented in this paper. It has been kept very broad in order to accommodate the multifarious conditions and situations which exist in the industry. It will also be applicable to renegotiations and to negotiations associated with nationalization of a given production facility operating in the country.

1. *Transnational corporations and exports of primary commodities*

In spite of the rapid increase during recent years in manufactured exports from a few selected developing countries, primary commodities continue to figure prominently in developing countries' exports.[2] For the developing countries as a whole, the share of exports of primary commodities in total exports was 84.7 per cent in 1975. Petroleum accounted for 60.9 per cent in 1975, as compared to 28.3 per cent in 1960.[3]

Concomitant with the above phenomenon has been the slow growth of primary commodity exports in relation to other exports. During 1950-1975, in terms of current prices exports showed the following annual rates of growth: foodstuffs and raw materials, 7.3 per cent; fuels, 14 per cent; and manufactures, 12.7 per cent. In terms of constant prices, the percentages are as follows: foodstuffs and raw materials, 4.2 per cent; fuels, 6.8 per cent; and manufactures, 8.3 per cent. The declining share of foodstuffs and raw materials in total exports during the period is reflected in the decreasing importance of such products in world exports. During the period, the share of food and raw materials declined from 46.4 per cent to 19 per cent, whereas that of fuels increased from 9.9 per cent to 18.6 per cent and that of manufactures from 43.7 per cent to 60.4 per cent.[4]

It is generally recognized that such factors as rapid technological progress, reducing demand for raw materials as a proportion of total demand through

[2] Throughout this paper, commodities are defined as those in SITC categories 0 to 4 (inc.) and 68 (non-ferrous metals).

[3] International Bank for Reconstruction and Development (IBRD), Report Nº EC-166/77, *Commodity Trade and Price Trends*, August 1977.

[4] These shares are for exports in current prices. Source: CEPAL, *The economic and social development and external relations of Latin America*, E/CEPAL/1024, Santiago, Chile (mimeographed text), 15 March 1977.

technological innovations, with, in advanced countries, the development of synthetic raw materials and the rapid increase of food production, rising prices of manufactured goods because of inflation and restrictive import policies, are among the most important determinants of the above trends.

Structurally, primary-exporter countries receive only a small fraction of the final prices paid for their commodities by consumers and by manufacturers in importing countries. It has been roughly estimated that final consumers pay over 200 billion dollars (excluding taxes) for the developing countries' major primary exports, excluding oil (after further processing, packaging and advertising); but the exporter countries receive only 30 billion dollars; or roughly one-seventh of the total.[5] The spread is largest for commodities requiring complicated processing techniques. For example, 4 to 5 tons of bauxite worth between 40 and 80 dollars will yield 1 ton of primary aluminum metal worth 700-800 dollars, and this in turn will yield semimanufactured products worth between 1,000 and 1,500 dollars.[6] Even for foodstuffs exports requiring little further processing, there is a considerable spread between export value f.o.b. and consumer prices. Banana-exporting countries, for instance, receive in gross export revenues between 12 per cent and 30.8 per cent of the retail consumer price in Italy and in the United States, respectively.[7]

International efforts to improve the economic performance of developing countries which rely heavily on primary commodity exports have recently been intensified in many international forums and by producer associations. The struggles of the developing countries have centred around demands for such measures as the linking of the prices of raw materials to those of manufactured goods, the stabilization of raw material prices and of the incomes of developing primary-exporter countries, the removal of tariff and non-tariff barriers and the increasing of the export price of specific commodities.

While all these international efforts directed at improving raw material prices and access to markets will undoubtedly benefit the developing countries which depend on primary commodity exports, a comprehensive and long-run solution to the problems faced by such countries will have to be found by placing primary commodity problems in the wider context of the international marketing of such commodities, and by examining the overall structure of the distribution of gains from such activities, i.e., the entire operational chain from the producer to the consumer. To this end, international efforts will have to be complemented by national efforts aimed at altering the distribution of gains[8] in favour of the developing exporter country. These national policy measures should be directed at two different

[5] See Mahbub Ul Haq, "The Third World and the International Economic Order", *Turkeyen Lectures*, Georgetown, Guyana, 1975.

[6] See Norman Girvan, *Corporate Imperialism: Conflict and Expropriation*, New York, M.E. Sharpe, 1976, p. 101.

[7] See FAO, Committee on Commodity Problems, "Review of the economic aspects of production, trade and distribution of bananas", CCP:BA 75/8, April, 1975.

[8] This paper will concentrate on the economic or monetary gains derived from the export trade, and will leave aside such other effects of foreign investment activities as are felt, for example, in employment and at the cultural level.

stages of the process. One is the distribution of gains from a given f.o.b. export value. The second set of policies are directed towards increasing the value added from exports, either through forward linkage operations from primary commodity exports to capture a larger share of the overall gains from such exports, or through a rise in the unit value of exports (as in the OPEC case, for example).

Since the overall gains from primary commodity exports are closely linked to the operations of transnational corporations, the key to understanding the structure of these global gains lies in an analysis of the nature and operations of these transnationals and of their impact on the economic development of producer countries.

Through their global network of subsidiaries and associated companies, linked together by an intricate system of common financial, managerial, technological and organizational services, a small number of transnational corporations continue to exercise control, directly or indirectly, over the crucial stages of the operational chain of most primary commodity exports, from exploration to production, processing, exportation, transport, marketing, distribution and financing. Complex constellations of horizontal and vertical integration have been established by transnational corporations in primary commodity exports, especially in the mining sector, often producing oligopolistic structures in the markets for these commodities.

During the past twenty years or so, there has been a marked decline in the degree and extent of the control exercised by transnational corporations over export activities in respect of many commodities. An important factor contributing to this trend is the strengthening of the bargaining power of host governments and the mutually reinforcing policies introduced by them to improve the distribution of gains in their favour.

Host governments have at their disposal a series of policy instruments with which they can attempt to shift the international distribution of gains in favour of their countries. They may renegotiate the terms of the agreement and fiscal concessions, levy royalties and taxes, or require the expansion of purchases of goods and services and of processing activities in the host country; finally, they can assert sovereignty over natural resources by partial or total nationalization of subsidiaries of transnational corporations operating in the country. It goes without saying that host governments' policy instruments are not mutually exclusive and that one policy measure may reinforce another. Internationally, the emergence of many firms independent of the oligopoly in each commodity has enabled host governments to widen their options and to purchase independently the services formerly available only in the package called direct investment. These services include technology, management, marketing and distribution.

2. *Criteria for the selection of case studies*

The selection of specific commodity-country combinations for the case studies to be carried out in the project under discussion, on the basis of the general conceptual framework developed in the present paper, is guided by the following criteria:

a) The commodity selected should be of export interest to several countries

in Latin America and preferably in Asia. If this project is extended to other regions, the criterion will naturally be expanded to include other commodities of specific interest to Africa and West Asia. Statistically, therefore, commodities selected must figure prominently in the exports of the countries concerned. Secondly, the countries selected must make an important contribution to the world supply of exports of the commodity in question;

b) The degree and extent to which transnational corporations exercise control —whether directly or indirectly— over the production and marketing of the commodity concerned must be significant. Since indirect control over the marketing of the commodity is included, most of the commodities exported by developing Asia and Latin America can qualify for selection as objects of case studies. Even if production is in the hands of smallholders, as is the case with certain agricultural export commodities, the final business of marketing and distribution in the consumer countries is conducted by a handful of transnational corporations;

c) Recent government policies *vis-à-vis* transnational corporations in respect of the commodity selected must have yielded substantial improvements in the gains accruing to the host governments concerned. This criterion is adopted because it is believed that case studies describing such successful host government action will enable other governments trying to improve the gains from primary exports to move up on the 'learning curve' of bargaining power.

Using these three criteria as a basis, case studies were undertaken by CEPAL, the possibilities of expanding them to Asia and eventually to Africa being kept in mind. The three case studies selected were; tin in Bolivia, bauxite-aluminum in the Caribbean (specifically in Jamaica, Guyana and Surinam), and bananas in Central America and Panama. In all three cases, the gains from the commodity exports concerned have been shifted substantially in favour of host countries as a result of changes in the policies of host governments. This satisfies criterion (c) outlined above. These case studies will incorporate, whenever possible and appropriate, data on the experience of South-east Asian countries exporting identical commodities and involved with the same transnational corporations. The comparison of different control relationships maintained by the same transnational corporations in various parts of the world will contribute further to the accumulation of case study evidence in this still largely unexplored area of research. Since all three commodities are exported in significant quantities by certain African countries as well, the extension of the study to that region will obviously increase the validity of the conclusions reached.

Criterion (a) was met as follows. During 1973-1975, tin represented 41.3 per cent of total Bolivian exports. The corresponding figures for bananas were: Costa Rica, 27.1 per cent; Honduras, 22.3 per cent; and Panama, 27.8 per cent; while those for bauxite were: Guyana, 19.6 per cent; Surinam, 24.2 per cent; and Jamaica, 19.4 per cent.

Another criterion is the importance of the country's exports in total world exports of the commodity. During 1973-1975, Bolivia accounted for 14 per cent of world exports of tin, being the second largest exporter of tin after Malaysia. The corresponding figures for bananas were: Costa Rica, 16 per cent; Honduras, 8.3 per cent; and Panama, 8.2 per cent. The percentages for bauxite

were: Guyana, 9.5 per cent; Surinam, 10.2 per cent; and Jamaica, 23.3 per cent. During the same period, the Latin American and Caribbean region's share in world exports of the three commodities was: bananas, 75.2 per cent; bauxite, 47.2 per cent; and tin, 15.4 per cent. The corresponding shares of developing countries in Asia were: bananas, 10.7 per cent; bauxite, 5.6 per cent; and tin, 58.5 per cent.[9]

Criterion (b) concerns the degree and extent of control exercised by transnational corporations over the commodity concerned. Although recent government policies are introducing significant changes in patterns of ownership and control, transnational corporations are still dominant in the bauxite-aluminum and banana sectors of the Caribbean and the Central American isthmus, respectively, and, for that matter, in those of South-east Asia and Africa.

Six vertically-integrated transnational corporations control the bulk of the world aluminum industry. The four largest operate in Jamaica: the Aluminum Company of America (ALCOA); the Aluminum Company of Canada, ALCAN Aluminum Limited; the Reynolds Metals Company; and the Kaiser Aluminum and Chemical Corporation, along with two others which are important in the copper industry: Revere and Anaconda. ALCOA also operates in Surinam and the Dominican Republic, whereas Reynolds is active in Haiti. In Surinam, the other important producer is Billiton, a Dutch transnational corporation which has its origin in the Indonesian tin industry and is still important in the tin industry of Thailand. ALCOA also explores for bauxite in Indonesia, while the Malaysian production is owned by ALCAN.

In the banana economy of the Central American Isthmus, three transnational corporations from the United States dominate the scene, although often operating through associate producers. These three companies are: United Brands (a merger between the United Fruit Company and AMK Corporation); Castle and Cook (parent company of Standard Fruit); and Del Monte Corporation. Together with the Japanese transnational Sumitono, they control Philippine banana exports through a system of associate producers and market control.[10]

The tin industry has been selected because of the dynamic modifications which have occurred in the control exerted by transnational corporations over the industry, especially since World War II. The tin industry has always been relatively unstructured, and has not been dominated on a worldwide basis by fully-integrated companies, as is the familiar pattern in other non-ferrous metals.

The nationalization of the three largest companies in Bolivia in 1952 and of the Billiton Company in Indonesia in 1957 has further significantly weakened the control of transnational corporations over the industry (Bolivia and Indonesia are respectively the second and third largest producers of tin in the world). The Indonesian State monopoly in tin, P.T. Timah, and the Bolivian mining corporation (Corporación Minera de Bolivia – COMIBOL) –which accounted for 75 per cent of Bolivia's tin exports in 1975– are now the two largest com-

[9] Source: IBRD, *Commodity Trade and Price Trends, op. cit.*, tables 19 to 22.

[10] Data obtained from annual reports of companies and government sources.

panies in the world.[11] More recently, in 1976, control over the world's remaining largest transnational corporation producing tin (the London Tin Corporation), with production in Nigeria, Malaysia, Thailand and Australia, passed into the hands of PERNAS, a holding company owned by the Government of Malaysia. This was brought about through a successful take-over bid for the parent company in London and the transfer of the company headquarters to Malaysia.[12]

Control over the smelting of tin, which in turn influences the marketing of the metal by transnational corporations, is also diminishing rapidly. The State enterprises in Bolivia and Indonesia are expanding their tin smelting capacity and will soon smelt all their domestic production. The world's largest tin-smelting transnational corporation is Amalgamated Metal Corporation (a 1976 merger between Consolidated Tin Smelters and Amalgated Metal Corporation), which owns smelting facilities in Nigeria, Malaysia and Australia. AMC is controlled by Patiño N.V., which also owns a tin smelter and production facilities in Brazil. The Williams Harvey tin smelter in England, owned by AMC, which formerly smelted the bulk of Bolivian tin, was closed down in 1974.[13]

Finally, the three commodities selected provide good examples of how co-operation and concerted efforts among producer countries can improve the bargaining position of each host government. The concerted action taken through the International Bauxite Association and the Union of Banana-Exporting Countries considerably enhanced the bargaining power of the producer countries. Although the International Tin Agreement, which is now entering upon its fifth phase with the recent ratification by Bolivia,[14] embraces both producer and consumer countries, the producer countries have frequently been able to join forces to serve their common interest in the International Tin Council, the executive arm of the Agreement. The tin agreements have above all been successful in exerting a stabilizing influence in the tin market, dominated as it is often is by speculative elements.

B. The bargaining framework

This section presents the general outline for the study. Central to this outline is the bargaining framework depicted in diagram 1, which shows the relationships among the various elements entering into the bargaining process and determining its outcome. The framework has been drawn up on simple lines so that it can be applied to all cases under study. At

[11] Excluding the People's Republic of China.

[12] Government sources for Bolivia and Indonesia. On the PERNAS take-over story, see: Andrew Davenport, "Bargaining for Vital Tin Stakes", *Far Eastern Economic Review*, April 1, 1977; "Country Profile", *Asian Finance*, April-May 1977.

[13] United States Bureau of Mines, "Tin", *Mineral Facts and Problems*, Washington, D.C., 1975; Walter Skinner's *Mining International Yearbook*, London, The Financial Times, 1975, 1976 and 1977 issues: company reports; William Fox, *Tin: The Working of a Commodity Agreement*, London, Mining Journal Books, 1974.

[14] *Metals Week*, 20 June 1977, p. 3.

Diagram 1

TRANSNATIONAL CORPORATIONS IN PRIMARY COMMODITY EXPORTS: ELEMENTS IN THE BARGAINING FRAMEWORK

A
THE BARGAINING SITUATION

The relative bargaining positions of host governments and TNCs are shaped by a process of mutual interaction among the following four sets of factors:

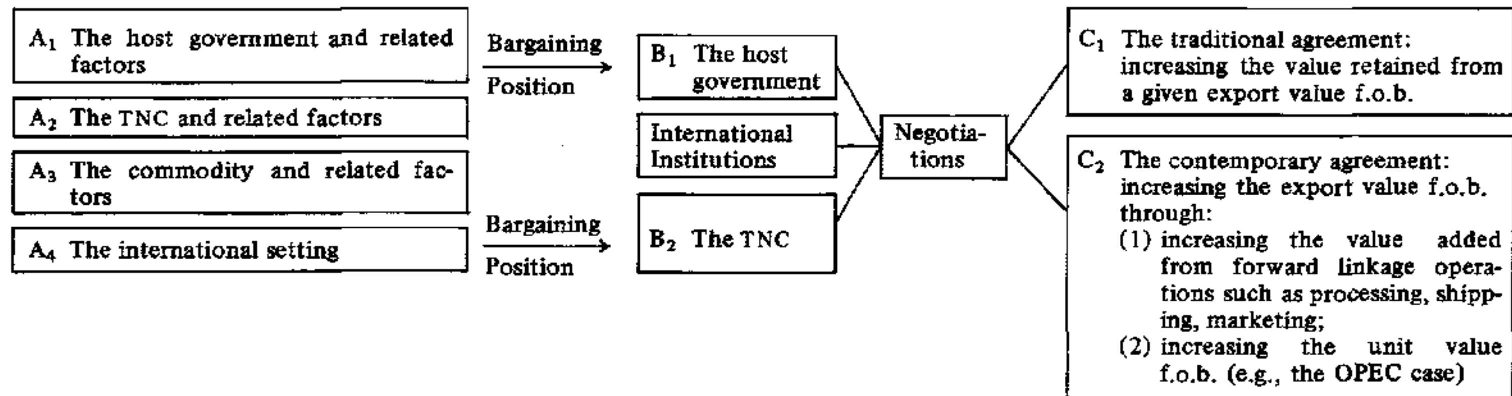
B
THE BARGAINING PROCESS

The terms and conditions of the agreement are the subject of negotiations between the two negotiating parties, influenced by international institutions.

C
THE AGREEMENT AND THE DISTRIBUTION OF GAINS

There are three types of agreements:
(a) the specific contract (e.g., mining contract)
(b) the standard contract (e.g., a forestry concession)
(c) the implicit agreement (e.g., projects operating under general investment laws).

In all cases, the host government is interested in improving the distribution of gains in its favour at the following two levels:



the same time, it introduces into the situation a dimension of continuous change which will make it possible to analyse changes in host-government/transnational-corporation relationships over time.

In the bargaining framework it is assumed that both the host government and the transnational corporation are interested in maximizing their respective gains from the potential project (or the existing project in the case of renegotiations), and that therefore the bargaining process plays an important role in the determination of the distribution of gains. The negotiations between the two parties concerned take place in a certain *bargaining situation* in which both parties are equipped with their respective bargaining capacity. The relative bargaining capacity of each party is determined by a process of mutual interaction among numerous factors, which have been grouped in four sets in box A of diagram 1. In a particular bargaining situation, *negotiations* will commence between the two interested parties, under the influence of international institutions (diagram 1, box B).

There are three types of agreements. In the case of an important mining project involving hundreds of millions of dollars, the pertinent negotiations may entail years of hard bargaining, resulting in a formal specific contract. In other cases, where the procedures have been standardized, no formal negotiations may be conducted at all and the company may start operations after signing a standard contract. Thirdly, a company may enter operation under general laws applicable to foreing investment projects, i.e., the agreement is implicit. The formal or implicit agreement concluded will form the basis of the *distribution of gains* among the transnational corporation, the host government and the other parties concerned (see diagram 1, box C).

Box C of diagram 1 distinguishes between two levels of agreements: *the traditional agreement,* which concerns itself with the distribution of the proceeds from gross value of exports alone; and the *contemporary agreement,* which is concerned with the overall distribution of benefits from commodity exports, i.e., from the final consumer value of such exports, including the margins accruing to shipping, processing, manufacturing, distribution and marketing. The distribution of gains can also be improved by simultaneously raising the unit value of exports and the retail consumer price. Both the producer country and the transnational corporation will gain at the expense of the consumer, as, for example, in the OPEC case.

As the name suggests, the contemporary agreement evolved from the traditional agreement. However, as the process of change is not uniform for all commodities and all countries, there are countries today which still allow transnational corporations to operate under a traditional agreement.

The actual distribution of gains depends on the process of implementation of the project, in which the transnational corporation executes the project and the government exercises its regulatory and control functions. A further complication is that the actual distribution may differ considerably from what was agreed on paper. In the case of an implicit agreement, automatic renegotiations will take place to adjust the provisions originally agreed upon. Where a formal contract is involved, however, renegotiations are more com-

plicated and will result in a new agreement.

Since the evolution of the different types of agreements and the implications for the distribution of gains are closely associated with the changes in the bargaining power of the two parties concerned, it is useful at this stage to examine in greater detail the four sets of factors which appear in diagram 1, box A.

1. *The bargaining situation (box A)*

A tabulation of the main elements entering into each of the four sets of factors that determine the bargaining situation is presented below. The list is by no means exhaustive, but it includes what are considered to be the important elements in each set.

(a) *The host government and related factors (A_1)*

(i) *Political factors*

- Degree of independence and links with politico-economic groupings;
- Political philosophy of the government, especially its attitude towards foreign capital investment;
- Stability and strength of the government and the extent of its authority throughout the country;
- Foreign penetration and control over various sectors of production in the country concerned.

(ii) *Administrative factors and legal framework*

- Quality of the bureaucracy: skills and efficiency; the role of education and training;
- Skills and experience in negotiations with transnational corporations;
- Qualifications of technical cadres for running corporate functions independently;
- Extent of information available to the public administration on the industry and the corporation concerned, as well as on terms and conditions imposed by other host governments;
- Extent of information available on the relationship of the transnational corporation with the home government and institutions like the Overseas Private Investment Corporation (OPIC) or the Export-Import Bank (EXIMBANK);
- The laws and regulations of the country, especially those pertaining to foreign investment.

(iii) *Economic factors*

- Dependence on foreign exchange earnings from exports in general, and from the commodity concerned in particular; the degree of export diversification;
- Position of the country in world trade in the commodity concerned;
- Position of the country in world production and reserves of the commodity concerned;
- The proportion of the commodity exported in relation to the host country's production;

- Relationships with international economic systems;
- Economic and financial dependency; balance of payments and debt position, etc.

(b) *The transnational corporation and related factors (A_2)*

(i) *International control relationships*

- Structure of the oligopoly: degree of vertical and horizontal integration and control over production and exports, shipping, processing, marketing and distribution;
- Existence of cartel arrangements, including gentleman's agreements, in the industry;
- Oligopoly dynamics: weakening of the oligopoly through emergence of independent firms in the industry;
- Position of the particular transnational corporation in the industry: share in markets, raw material supplies, production and processing capacity;
- Corporate strategies in respect of global control over raw material supplies;
- Necessity of securing a 'hurdle rate' of return; i.e., a risk-adjusted minimum acceptable internal rate of return.

(ii) *Relationships with the host country concerned*

- Structure of the transnational corporation in the host country:
  - status of subsidiary (–ies) in the system);
  - related and associated companies through interlocking directorships and management and technology contracts;
- Transnational mobility of the corporation:
  - dependence on raw materials from the particular host country and possibilities of shifting to other sources of supply;
  - debt/equity factors in the investment project;
  - investment planned or already placed in host country concerned;
- Home country support for the corporation.

(c) *The nature of the commodity (A_3)*

(i) Trends in demand and supply, including projections of such trends. Importance of trade in world production of the commodity;

(ii) Trends in demand for and supply of substitutes;

(iii) Income- and price-elasticities and elasticity of substitution;

(iv) Market structure. Importance of formal markets and of arm's-length trading versus intra-company transactions;

(v) Geographic concentration of countries in production, processing, trading and consumption of the commodity;

(vi) Nature and structure of the industry. Proportion represented by export value of primary commodities in final consumer value in importing country;

(vii) Dynamics of resource discovery and, in the case of minerals, trends in reserves related to current production;

(viii) The trend towards massive size in mining projects: increasing capital investment required per metric ton of production of the specific commodity concerned.

(d) *The international setting (A_4)*

(i) *World political order: post-world-war political emancipation and decolonization.*

(ii) *World economic order*

- The calls for economic emancipation to accompany political independence, culminating in demands for a New International Economic Order; and on the other hand, the steadily-growing power of transnational corporations in all spheres;
- The role of international institutions: United Nations agencies (especially UNCTAD), IMF, IBRD, etc.;
- International commodity agreements, e.g., the International Tin Agreement;
- Producers' associations, e.g., Organization of Petroleum Exporting Countries (OPEC), International Bauxite Association, Union of Banana-Exporting Countries, Association of Natural Rubber-Producing Countries;
- Multipolarization of the world economy;
- Preferential schemes extended to a particular group of countries by certain importer countries and other policies imposed by consumer/importer countries;
- Potential or real sanctions imposed by home governments and/or international institutions on countries which embark on policies such as expropriation.

(e) *Shaping the bargaining situation*

It would be difficult, if not impossible, to assign meaningful values or weights to the above factors, most of which are qualitative in nature. Moreover, although in the short run many factors are assumed to be constant, in the long run they all vary, which creates a climate of continuous change and often tension in the bargaining situation.

Until a more rigorous general theory on the bargaining framework including both qualitative and quantitative factors has been developed, the most reasonable approach would appear to be to carry out case studies, which is the methodology adopted in this project.[15] The foregoing catalogue will then act purely as a checklist. Thus, an appreciation of what matters might be formed by looking at otherwise very smilar cases in different countries or industries or in the same industry at different points of time. It is believed that the accumulation of such case study evidence will enable other host governments to apply similar strategies in respect of transnational corporations operating in their countries.

Although as a general rule the improvement of a host government's

[15] Of course, many rigorous bargaining models exist, in which the non-qualitative factors are ignored or assumed to be constant. None of these will have an operational value in the approach presented in this paper.

bargaining power will automatically weaken the other party, there are cases where the zero sum of game theory does not apply, as both parties can increase the gains to be distributed through jointly-conceived strategies. The petroleum price hike is, of course, the most obvious example, whereby both host governments and transnational corporations increased their benefits by jointly capturing the consumer surplus.

Broadly speaking, transnational corporations are almost by definition able to capture a larger share of profits through their structural and inherent characteristics. Their unique advantages include their transnational mobility and their control over vital resources, which in turn gives them control over the crucial stages in the export of primary commodities; their strong point is their very 'transnational-ness', a characteristic which governments in particular do not possess.

The TNC subsidiary's strength lies in the large central expenditure borne by the corporation as a whole, and not necessarily by a particular subsidiary. Through their heavy expenditure (on exploration, advertising and marketing, or on research and development),[16] TNCs control most turnstiles of entry to the industry. Depending on where the key scale factors are, and where heavy expenditure is made, the crucial turnstiles of entry will be located either after the production stage, as in the case of bananas (and other tropical agricultural products), tin, bauxite and iron ore, or else at the production and exploration stage, as in the case of petroleum, copper, nickel and natural gas.

Accordingly, the oil and copper companies that are challenged by economic nationalism in the countries where the wells and mines are located cannot easily capture oligopoly control at a later stage. In the cases where oligopoly control is strong at the post-production stage, on the other hand, TNCs may continue to maintain it even if production facilities are nationalized.[17]

Despite the difficulty of assigning values or weights to the factors in the list above, one can make certain generalizations about the magnitude and intensity of the impact of each factor on the relative bargaining power of host governments and transnational corporations.

Ceteris paribus, from the standpoint of the structure of transnational corporations, a country owning a resource for which substitutes are readily available is *de facto* in a weaker position than the owner of the sole source of a material, and the latter's position is stronger if it does not depend on that resource alone for its export revenue.

In a given host country, a transnational corporation which depends to a large extent on raw materials from that country will be in a weaker position than other corporations which have a more diversified resource pattern. The ability of host governments to play off one company against another will depend on the oligopoly dynamics, which differ from commodity to commodity. In commodities in which the control of the few dominant companies is constantly being challenged by the proliferation of new independent companies, host go-

[16] Paul Streeten, "Policies Towards Multinationals", *World Development*, vol. 3, no. 6, June 1975, pp. 393-397.

[17] Theodore H. Moran, "Transnational Strategies of Protection and Defense by Multinational Corporations: Spreading the risk and raising the cost for nationalization in natural resources", *International Organization*, vol. 27, no. 2, Spring 1973.

vernments will be in a better position to bargain than in cases where a handful of companies control the crucial technology or marketing of the commodity.

Host governments possessing few bargaining skills or first-hand experience, owing to the absence of qualified personnel and lack of information about the market, will be able to take advantage of the knowledge and experience of other countries which have been successful in concluding contracts favourable to them or in renegotiating existing contracts. Concerted action and solidarity among host countries will automatically strengthen individual positions, whereas lack of solidarity will allow corporations to play off one country against another.[18] Although all transnational corporations are by definition able to move easily across national boundaries, when it comes to mineral exploitation the corporations with mineral reserves in many parts of the world will be placed at an advantage over companies with limited resource mobility. In this connexion it should be remembered that in both the successful instances of concerted action by producer countries, i.e., in respect of petroleum and bauxite, the initiative was taken by a group of countries with similar problems and interests: the Arab countries in the case of oil and the Caribbean countries in the case of bauxite.

[18] After having succeeded in raising revenues from bauxite exports by 600 per cent in 1974, the Jamaican Government sent out missions to other bauxite-producing countries, which introduced similar levies. Solidarity benefited all parties. The other countries took advantage of Jamaican skills and knowledge in planning their strategies, while Jamaica's position was strengthened by concerted action on the part of other producers.

The market structure of the commodity is an important determinant of the bargaining power of host governments. In the absence of an open market for the commodity concerned, host governments, even after nationalization, will have to sell their output to the handful of transnational corporations controlling the industry. If nationalization does not take place, the export price is essentially a tranfer price between two subsidiaries of the same company. It can, therefore, be arbitrarily set by the company, which is aiming at profit maximization at the global rather than at the subsidiary level.

Finally, information is a very important source of strength. For example, if a government knows the 'hurdle rate' of return to the company it can impose heavy taxation on profits in excess of this return, as they represent economic income. Unfortunately, this hurdle rate is often a closely-guarded secret, although instances can be cited of successful renegotiations due mainly to the information on it possessed by the host government (e.g., the case of the Jamaican bauxite levy).

To move from essentially static to medium-term conditions, the changes over time in bargaining positions can be discussed at two levels: the project level and the general level.

At the project level it is generally observed that the bargaining position of host governments is weakest before the project starts. This is especially the case in big mining projects, as the first stage involves risk capital for large-scale exploration expenditure which the trasnational corporation can supply. Once the corporation has sunk substantial amounts of capital, which is frozen over the short term, the bargaining position tilts in favour of the host governments,

to which the original terms of the agreement may come to appear excessively generous. They may then introduce new tax laws, or tighten the control and regulation provisions within the existing agreement, or demand the renegotiation of the original contract. The balance of bargaining power may eventually swing back in favour of the transnational corporation at the time when it is considering a further large investment outlay, until the new bargain again becomes obsolete. This cyclical pattern of the bargaining process has been described by Raymond Vernon as the "obsolescing bargain".[19]

Analysing the dynamic changes which have taken place at the global level, one can observe that the cyclical trend described above oscillates around a secular trend in which host governments have continuously managed to strengthen and improve their bargaining position *vis-à-vis* the transnational corporations. This is reflected in the ability of host governments to conclude agreements with increasingly better terms and conditions or to apply to existing projects policy measures such as renegotiations or nationalization, all of which have shifted the distribution of gains unmistakably in favour of the governments concerned.

Among all the factors listed above, three in particular have contributed to this trend: the improving international climate in favour of Third World participation in global economic activities; the improvement in the negotiating skills of host countries; and the emergence of new industrial powers with their own independent corporations challenging the supremacy of the handful of companies controlling each commodity. These three factors are discussed below.

In the past, it was taken for granted that colonies and peripheral countries should specialize in the production of raw materials and cheap foodstuffs for the metropolitan countries. The dynamism generated by commodity flows from the peripheral countries and colonies was felt mostly in the metropolitan countries where the whole decision-making process with respect to processing, manufacturing and marketing of the commodities was concentrated, while the commodity-producing countries were relegated to the position of dependent entities. Whatever dynamism trickled down to them was very often confined to the foreign-oriented export-enclaves.

Private capital investment played an all-important role in this international division of labour between the metropolis and the periphery. Until the late nineteenth century, Western Europe's main interest in the colonies was as a source of cheap foodstuffs and agricultural materials. Private companies, some of them possessing in embryo the characteristics of today's giant corporations, developed the plantation economy and the trading facilities to satisfy these metropolitan needs. At the beginning of the twentieth century a new dimension was introduced into this typical relationship. As the industrial sector in Western Europe and Japan expanded rapidly and domestic sources of fuels and minerals

[19] Raymond Vernon, *Sovereignty at Bay*, New York, Basic Books, 1971, pp. 46 *et seq.* For a distinction between the bargaining power of host governments at the pre-exploration, pre-exploitation and post-execution stages of a mining project, see Rex Bosson and Bension Varon, *The Mining Industry and the Developing Countries*, World Bank Research Publication Series, Oxford, University Press, 1977, pp. 137-139. See also Theodore Moran, "Economic Nationalism and the Copper Industry", *Development Digest*, vol. XIV, no. 3, July 1976.

were swiftly depleted, these countries embarked upon an aggressive overseas search for fuels and minerals.

In this search, too, private companies played a major part, and the era witnessed the birth of the fully-integrated company with the establishment of Royal Dutch Shell in 1907, followed by other petroleum companies and companies engaged in prospecting for all the major metals of those days: copper, tin, bauxite and iron ore. Although the United States had always been relatively self-sufficient in these basic materials, to the extent that the country did require overseas supplies its companies not only participated in this worldwide hunt for fuels and minerals but were often in the lead.

The international climate was heavily weighted against the colonies and peripheral countries. The 'host governments' in the colonies were colonial administrations having the same objective as the transnational corporations: namely, to ensure the regular, orderly and cheap flows of raw materials and foodstuffs needed by the metropolis, with little regard for the economic needs of the local population in the colonies. Even in the case of the independent peripheral countries of Latin America, the bargaining position of transnational corporations, often backed by powerful home governments, was very strong and, at the same time, that of host governments very weak. The second factor explaining this weakness in those days was the complete ignorance of host governments regarding their natural resources, and their lack of experience in dealing with complicated issues such as mining contracts. Host governments had to rely entirely on company reports on the nature and extent of their natural wealth, to their obvious disadvantage, and corporations could virtually dictate the terms and conditions of the contract.

The international climate has changed considerably, especially since the Second World War. The political emancipation and decolonization which took place in the 1950s and 1960s have created independent countries out of erstwhile colonies. Transnational corporations now have to deal with host governments instead of colonial administrations.

However, the new nations very soon found out, as had their fellow Third World countries in Latin America long before, that political independence did not automatically bring about economic independence. Improved international communications, coupled with the increasing skills of bureaucratic machinery and the growing awareness of the intelligentsia in the Third World, fed by a swelling flow of university graduates (often from universities in the home countries of the transnational corporations), have stepped up the collective bargaining power of host governments. The countries of the Third World realize that economic independence cannot be achieved if they plod on in their marginal role of providers of raw materials for the metropolis and continue to receive only a minute portion of the total gains derived from their commodity exports.

Third World solidarity and awareness, as demonstrated in the many existing international forums, have contributed significantly to these changes in the international climate. In addition, improvements in international communications have enabled host countries to learn from one another's experience so that new agreements will have better terms and conditions than old ones. The successive waves of nationalizations and

renegotiations are mutually reinforcing, and often have repercussions on relationships in the same industry elsewhere or even in other industries.

An important factor in the decline of oligopoly power has been the emergence of numerous independent companies, some of them fully-integrated transnational corporations, others purveyors of separate services such as technology, and still others State enterprises. This is a consequence of the multipolarization of world economic power among the countries of Western Europe, the Socialist countries and Japan in the 1960s and 1970s, with its challenge to the post-war economic supremacy of the United States. This does not mean, of course, that the older companies have declined in absolute importance. On the contrary, through continuous mergers, consolidation and vertical and horizontal integration, these companies have individually all become statistically stronger. However, there is no doubt that the relative share of the oligopolies in production and exports of most commodities has declined over time.

2. *The bargaining process (box B)*

Given the bargaining situation, the success of a government in maximizing gains derived from primary commodity exports will largely depend on the skill with which it exploits its bargaining position. Several stages can be distinguished in the bargaining process between the transnational corporation and the host government. Stage one takes place prior to the initiation of a new project. Here the bargaining process will establish the terms and conditions of the agreement, which in turn will determine the distribution of gains from the project. In contemporary agreements, the terms and conditions agreed upon include such issues as transfer prices, the kind of technology to be used and its cost, tax and royalty rates and tax reporting techniques, concessions and the time limit involved, management and patent fees, the structure of debt and ownership, including the extent of local participation, local processing requirements and local purchases of goods and services.

Once the project is in process of execution by the transnational corporation, the government, exercising its regulatory and control functions, will attempt to ensure that the actual gains derived are in accordance with previously agreed-upon terms and conditions. It may pass new tax or other laws affecting the distribution of gains, within the confines of the original agreement. If, however, it demands significant changes, such as the imposition of a new production levy or equity participation in the companies concerned, or other issues are raised requiring changes in the original provisions of the agreement, the bargaining process enters its second stage, i.e., the renegotiation of the agreement. Renegotiations are nowadays quite common in the relationship between host government and transnational corporation, in view of the changing bargaining position described at length in the previous section.

When renegotiations break down, the government may decide to nationalize the facilities owned by the transnational corporation. Nationalization may occur without previous attempts at renegotiation, which is the case if a government decides to resort to it either as a matter of principle, or on an *ad hoc* basis at

the prompting of given events. Unless nationalization is accompanied by confiscation, it will entail a certain type of negotiations as well, which may be labelled stage three of the process; they will centre on the issue of compensation payments, but will often also include negotiations on a new relationship between the two parties, i.e., the signing of management, technology or marketing contracts. Nationalization of a dependent "cell" or subsidiary will not necessarily be followed by a severance of all ties with the transnational corporation network.

3. *The agreement and the distribution of gains (box C)*

Turning now to the *volume of distribution of gains* itself, this study will employ the concept of *retained value* as a basis for measuring the distribution of gains. Under this concept, the gains to the host country are measured as the sum total of all components of foreign-exchange export earnings which are retained in the country. Table 1 shows that in the case of the traditional agreement, the most important components are: (a) wages and salaries; (b) domestic purchases of goods and services;[20] (c) the government's share of revenues (royalties, taxes, levies, dividends); (d) reinvested profits.

Table 1 also shows that the contemporary agreement has two components. One is the gross value of exports (XR), where the distribution of gains problems are of course, identical with those of the traditional agreement, i.e., XR = RV + OP. The second component deals with the gains from forward linkage activities. If the government succeeds in transferring the later-stage processing activities —refining, smelting and eventually manufacturing— to the host country, but continues to rely on transnational corporations for the operation of the activities in question, additional distributive implications emerge. Here again, the components of retained value become important. Governments are also interested in securing shares in lucrative operations such as shipping, marketing and distribution, which are carried on outside the host country and would presumably yield foreign exchange revenues. The important magnitudes are not the gross margins accruing from these operations, but the net surplus gains that the host country can earn from engaging in such activities.[21]

The concept of retained value employed in this study has been applied by Mikesell in case studies on copper, petroleum and other products.[22] It is by no means the only way to calculate the nation's benefits; it is perhaps not even the best, as it suffers from various defects such as the inability to compute social opportunity cost and the social rate of discount. Nevertheless, from the standpoint of host government policy, it is a useful approach for comparing alternative means of developing a project. Furthermore, estimation problems at the case study level due to lack of data would prevent the use of a more

[20] Defined net of import content of local purchases. Import content may be very large, especially in small countries with a narrow industrial base.

[21] See the introduction to this paper.

[22] See Raymond F. Mikesell, *Foreign Investment in the Petroleum and Mineral Industries,* Resources for the Future, Inc., The Johns Hopkins Press, Baltimore, 1971; and by the same author, *Foreign Investment in Copper Mining,* Resources for the Future, Inc., The Johns Hopkins Press, Baltimore, 1975.

Table 1

THE DISTRIBUTION OF GAINS UNDER THE TWO TYPES OF AGREEMENT

The traditional agreement[a]	*The contemporary agreement*[a]
A. Components of gross export revenues (XR):	Components of the distribution of gains from final consumer value (FCV)
1. *Components of retained value of exports* (RV)	A. *Components of gross export revenues:* same as under the traditional agreement (XR)
(a) Wages and salaries (W)	
(b) Domestic purchases of goods and services (DP)[b]	XR = RV + (OP) (1)
(c) Government's share of revenues (GR).	
(d) Reinvested profits (RP)	
2. *Components of outflow payments* (OP)	B. *Components of forward linkage activities* (FL)
(a) Imports of goods and services, including invisibles such as patents and licences (MGS)	(a) Refining and smelting (or ripening in the case of foodstuffs such as bananas)
(b) Salaries of expatriates accruing abroad (SE)	(b) Manufacturing
(c) Loan repayments abroad, including interest (LP)	(c) Shipping and insurance
(d) Corporate profits transferred abroad (TP)	(d) Marketing and distribution
XR = RV + OP (1)	FCV = XR + FL (2)

[a]See diagram 1 for an explanation of these two types of agreement.
[b]DP is defined net of the import content of domestic purchases.

sophisticated measure of the distribution of gains, such as the concept of net present value of the investment project developed by Mikessell, McKern and Kindleberger.[23] In the latter concept, the time element is taken into account by introducing an appropriate social rate of discount. In addition, the equation includes such measures as the social value of external economies and the social opportunity cost of domestic inputs, all of which are difficult to estimate.

Table 1 simplifies the picture in that it assumes an ongoing project earning foreign exchange from exports. This makes it possible to calculate, on an annual basis, how the export earnings are

[23] Charles P. Kindleberger, "Direct Foreign Investment in Economic Development", in *Direct Investment in Asia and the Pacific* (Peter Drysdale, ed.), University of Toronto Press, 1972. For further elaboration of the concept, see Raymond F. Mikesell, "Foreign Direct Investment in External Financing", paper presented at the Conference on External Financial Policies, sponsored by OAS and the Central Bank of Chile, Santiago, March 1977. See also Bruce McKern, *Multinational Enterprise and Natural Resources*, Australia, McGraw Hill, 1976, pp. 23-33.

distributed among the various agents: the transnational corporation, the host government and others.

A key element in the negotiations is the determination of *direct gains,* or gains in the narrower sense of the word, i.e., the surplus accruing from the project. Since surplus is the difference between revenue and cost, its size will depend on the method by which the various items determining these two magnitudes are calculated. The methods of calculation are often a major source of conflict. Primary export projects involve complicated inflow and outflow transactions between various subsidiaries of the transnational corporation, and the calculation of cost and revenue therefore depends very much on the corporation's transfer pricing practices.

In order to obtain a better understanding of the relationship between the investment of the transnational corporation and the surplus generated by the project, the project's balance-of-payments flow must be traced from its beginning. This is done in table 2, which distinguishes between the two phases of each project: the initial investment or pre-exportation period and the sustained-exportation period. In both periods inflow payments are equal to the retained value plus outflow payments (IP = RV + OP (1)).

The pre-exportation period varies from project to project. In the mining and petroleum sectors, it will include the exploration period, during which the corporation brings in equity or loan capital for high-risk activities which may turn out to be unsuccessful. On this investment, therefore, the company expects a higher than normal rate of return, which it will recover in the form of profits when the project starts production. Even if the activity is less risky, as in the case of banana plantations, there will be an initial period in which expenditure is made and nothing is earned. Very often the inflow is in the form not of cash but of heavy machinery, drilling equipment, etc., so that the inflow item is automatically offset by the import item. During this period, the main components of retained value are wages and salaries (W) and domestic purchases of goods and services (DP).

In Phase II, the sustained-exportation period, the problem of the distribution of gains will loom up in earnest, as there are foreign exchange earnings from exports to be divided. Corporations often justify their high rate of profits, or returns, on the grounds that they have to write off expenditure incurred in Phase I and take into account the high-risk activities undertaken during that phase. While this may be true, it is difficult in practice to estimate the magnitudes of a just return for risks undertaken in Phase I, because of the use of transfer pricing and because the corporation maximized returns on a global scale. A government will find it hard to understand that against earnings from exports of its own country's products a company will write off unsuccessfull investment in another country.

Conceptually speaking, the ability of governments to capture the direct gains from export activities is related to the various categories of economic returns within the overall gains. It is useful to distinguish between three types of economic returns which accrue from primary commodity exports:

1. Resource income, first introduced by Ricardo many years ago in agriculture. Today this concept is much more applicable to mining, especially when differences in the quality and in the

Table 2

DISTRIBUTION OF GAINS DURING THE TWO PHASES OF THE INVESTMENT PROJECT

Inflow payments (IP)	*Retained value (RV)*	*Outflow payments (OP)*
Phase I: The initial investment period		
1. Transfers from transnational corporation's headquarters (THQ)	1. Wages and salaries (W)	1. Imports of goods and services, including designs, blueprints, etc. (MGS)
(a) equity capital (EC) (cash and subordinated loans)	2. Local purchases of plant, equipment goods and services[a] (DP)	2. Salaries of expatriates accruing abroad (SE)
(b) debt (foreign loans) (DE)	3. Changes in cash balances in local banks (CLB)	3. Changes in cash balances in foreign banks (CFB)
		4. Interest payments (IP)
Phase II: The sustained-exportation period: operating results in year i		
1. Export revenues (XR)	1. Wages and salaries (W)	1. Imports of goods and services, including royalties, patents, licences, etc. (MGS)
2. Transfers from transnational corporation's headquarters (THQ): same as 1 (a) and (b) under Phase I	2. Local purchases of goods and services (DP)	2. Salaries of expatriates accruing abroad (SE)
	3. Government's share of revenues (GR)	3. Profits and depreciation transferred abroad (TP)
	4. Retained earnings and depreciation reinvested or in local banks (RP)	4. Debt amortization (DA)

[a]Defined net of import content.
Note: In both periods: IP = RV + OP (1).

accessibility of mineral deposits produce differential resource incomes;

2. Quasi-income. This type of income is earned by factors of production brought into combination by the transnational corporation, such as capital and technology. It also includes the services of experts, which, owing to the oligopolic position of managers, are not readily available;

3. Monopolistic and monopsonistic income accrued. Since perfect competition does not exist in primary-commodity trade, oligopolies controlling the barriers to entry earn these types of income on the buyer and seller sides.

In practice, it is difficult for a host government to identify the three kinds of income and demand a share of each type. Usually, quasi-income is shown

among the cost items of the transnational corporations and will be part of the outflow payments. Attempts to capture such forms of income are difficult, but a tax on licence fees, for example, has been introduced successfully by some countries.

For obvious reasons the differential resource incomes are the most easily captured by host governments earning them. Finally, the burden of the recent successes of governments in demanding a larger share of the gains from oil and bauxite has been shifted by the transnational corporations on to the consumers, allowing both host governments and transnational corporations jointly to maximize the monopolistic income gained in these industries.[24]

Nowadays, the distinction between the two types of agreement is rapidly disappearing. Between the two extremes —i.e., a host government receiving a minimal share of earnings under a traditional type of agreement and a government which participates in all activities, including forward linkage, in the shape, for example, of a fully-integrated nationalized firm—, a wide range of variations on the basic theme has come into existence, especially with the proliferation of new types of agreements replacing the traditional foreign-direct-investment package, such as joint ventures, turn-key operations, management or technology contracts, production-sharing agreements, etc.

The host government, during the negotiations, will not merely confine itself to the narrower question of distribution of direct gains, i.e., of how to capture its share of surplus or economic returns. It will also be concerned with increasing indirect gains, i.e., the shares falling to the other domestic agents (wages and salaries and domestic purchases of goods and services), and, under the contemporary type of agreement, with the forward-linkage effects of the project. In other words, the total impact on development depends not only on the magnitude of the retained value, but also, to a more important extent, on its composition, which determines the strength of the various linkages described in the following pages.

Better control and regulation of existing stipulations in the agreement as to proportions of local personnel, of domestic purchases of goods and services, and of processing in the host country, will often yield considerable increases in indirect gains, i.e., in the country's share of the gains accruing from various components of retained value of exports. If the agreements is of the traditional type or is strongly biased in favour of the corporation, only drastic renegotiations of the contract or nationalization can resolve the problem of increasing the host country's primary-export earnings.

It is useful to clarify further the impact of distribution of gains on economic development. This is important in view of the fact that discussion on gains from transnational corporations is often coloured by conceptual con-

[24] The income concepts are from a paper by Helen Hughes, "The Distribution of Gains from Foreign Direct Investment in Mineral Development", Southeast Asia Development Advisory Group, *Papers on Development Problems in Southeast Asia*, New York, The Asia Society (mimeographed) 1974. For an analysis of the incidence of new taxes or levies introduced by governments, see Malcolm Gillis and Charles E. McLure, Jr., "The Distributional Implications of the Taxation of Natural Resources", *Rice University Studies*, Houston, Texas, vol. 61, no. 4, Fall 1975.

fusion, which renders it meaningless to policy-makers.

Since this paper deals with an export-oriented sector, the discussion should logically concentrate on the financial gains derived from export projects. It would be beyond the scope of this paper to introduce issues such as effect on employment, income distribution, choice of investments, or environment, all of which are, of course, of great importance in the actual repercussions of projects on economic development. Nevertheless, it seems useful to dwell on the various development effects of the investment project, as its global impact on development depends on their strengths and weaknesses. In this regard, the system of generalized linkages worked out by Hirschman and others will be a useful guide.[25] The concepts of forward and backward linkages of investment introduced by Hirschman are now well-know in economic development literature.[26] The linkage effects of a given product line have been defined by Hirschman as investment-generating forces that are set in motion through input-output relationships. Backward linkages refer to purchases of domestic goods and services on the part of an investment project, leading to new investments by the suppliers.[27] Forward linkages refer to investment in output-using facilities, or the downstream integration of the project in processing, manufacturing, marketing and distribution.[28] These may be called production linkages, and are of the greatest concern to host governments in negotiations with transnational corporations.

In addition, host governments should take into consideration what Hirschman calls the consumption and fiscal linkages of the investment project. Both of these relate to the income aspect of the export-oriented project. The consumption linkage works as follows: new incomes generated by the production and export of primary commodities may initially be spent on imports, but a consumption linkage is considered positive if these imports, once they have grown to a sufficient volume, can eventually be replaced by domestic manufactures. Of course, the consumption linkage may be negative if imported consumer goods compete against domestic products and price them out of the market.

The fiscal linkage relates to the fiscal revenue generated by exports of primary commodities. While host governments are primarily interested in increasing their share of the economic returns on exports of primary commodities, the ultimate impact on economic development will depend upon whether the government spends the revenue on productive investment, i.e., upon the existence of the fiscal linkage. Of course, the bigger the pie, the more likely it is that at least part of it will go to feed productive investment.

It often happens that one kind of linkage is to be had only at the expense of another. Thus, fiscal linkages have made a strong showing in mining and petroleum activities which have all the

[25] The following discussion draws heavily on Albert O. Hirschman. "A Generalized Linkage Approach to Development, with special reference to Staples", *Economic Development and Cultural Change,* vol. 25, Supplement, 1977.

[26] Albert O. Hirschman, *Strategy of Economic Development,* New Haven, Connecticut, Yale University Press, 1958.

[27] DP in tables 1 and 2.

[28] FL in table 1.

earmarks of an "enclave". If the enclave is defined as the absence of involvement with the rest of the economy, it automatically implies absence of the consumer and production linkages.

A small country receiving huge amounts of tax revenue from petroleum exports, for instance, will be less concerned with promoting forward and backward linkages. The consumption linkage may also be absent if the high propensity to import proves self-sustaining and no encouragement is afforded to domestic industry. The only consumption linkage may be the improvement of port and highway facilities to cope with the astronomical rise in imports.

It would exceed the scope of this paper to follow through in greater detail the workings of the various linkages. With exception of those relating to production, i.e., forward and backward linkages, which are of direct concern in negotiations with transnational corporations, the other linkages are more closely connected with domestic policies and with the multiplier effect.

C. Summary

The broad conceptual framework set forth above will serve as a general guide for case studies in this field of enquiry. In each case study, modifications will have to be made in the broad terms of reference propounded in this paper. Nevertheless, certain common hypotheses developed in this framework will have to be tested in all the case studies, so that a comparative study can be made in the future. The basic hypotheses presented include the following:

1. During the past twenty-five years, there has been a significant change in the distribution of gains in favour of host governments and countries;
2. The improvement in the distribution of gains is a direct result of the strengthening of the relative bargaining position of host governments;
3. The relative bargaining position is determined by the mutual interaction of four sets of factors, namely, (a) the host governments, (b) the transnational corporations, (c) the nature of the commodity and (d) the international climate;
4. The list of the four sets of factors tabulated in the paper should be used as a checklist by researchers undertaking the case studies. The use of a common checklist for these studies will enable general conclusions about the relative importance of certain factors to be drawn;
5. Basically, the government can influence the distribution of gains in its favour through negotiations with the transnational corporations;
6. Negotiations take place at various points in time. Before the initiation of a project, negotiations are conducted to conclude an agreement. After the project has been executed, renegotiations may take place to alter the terms and conditions of the contract. Finally, should the government decide to nationalize the subsidiary of the transnational corporations, negotiations may take

place regarding compensation and perhaps marketing or other arrangements;

7. There exist considerable variations of the basic model above. In the case of small projects, negotiations may not take place at all, as corporations may execute a project under a standard contract or an implicit agreement. Automatic renegotiations will take place from time to time if governments decide to alter the basic contracts and the rules and regulations governing foreign investment;
8. With regard to the content of the agreement, two types of agreement can be distinguished: (a) the traditional agreement, which is concerned with the distribution of a given f.o.b. export value, and (b) the contemporary agreement, which is concerned with increasing the export value through forward linkage effects;
9. A distinction can be made between (a) direct gains, i.e., the surplus generated by export activities, and (b) indirect gains, i.e., the retained value accruing to domestic agents of the export project other than the government (domestic purchases of goods and services, and wages and salaries, as well as profits reinvested by the corporation);
10. Direct gains: governments are interested both in their percentage share and in the volume of the surplus, since the latter is determined by such negotiable factors as transfer pricing and depreciation practices;
11. Indirect gains: governments can influence the value of indirect gains by introducing laws requiring more extensive use of local personnel and of local goods and services, or others requiring government and host-country participation in forward-linkage activities associated with its primary commodity exports (such as processing, marketing, shipping, distribution and financing).