Chapter 5 PRODUCTION AND INVESTMENT RELATED COUNTERTRADE

5.1. The Problem of Insufficient Availability of Exports

A common problem experienced by many developing countries, and many countries in sub-Saharan Africa in particular, is the lack of availability of products for export other than a very limited range of traditional export items. This is a general trading problem and also arises as a particular difficulty in countertrade matters. This may be illustrated by the example of Nigeria, which has been involved in a number of large oil barter deals and, at one time, suggested that some non-traditional export items might also be sourced by countertraders; but oil accounts for well over 90 per cent of total exports from the country and relatively few alternative products at the requisite quality, quantity and price levels were available for procurement. In many other countries the situation is considerably more difficult, and, therefore, even if the developing country in question is prepared to embrace the idea of countertrade, there may be no suitable products available for export. This has led a number of commentators on the subject to suggest that countertrade for such countries is unlikely to be successful unless it is combined with production/investment programmes. When it is remembered that countertrade is often considered not to be worthwhile at a transaction value of less than $1 million, it reinforces the point that sufficient export products must be available before countertrade even becomes a realistic policy option.

5.2. Production and Investment Opportunities

We have already noted in Chapter 3 that buy-back and direct offset forms of countertrade involve production and, sometimes, technology transfer elements. There are also, of course, many non-countertrade avenues which can be pursued for encouraging the production and development of export products, including aid programmes, direct investment in overseas subsidiaries by multinational companies, BOT (build, operate, transfer) schemes and so on. In addition to these, and the buy-back and offset forms of countertrade, there are also other countertrade-related opportunities.

An idea that is gradually emerging is that countertrade partners, very often Western multinational companies, will assist a country (either through the rehabilitation of an existing project or the creation of a new project) to produce exportable goods, the foreign exchange revenues of which will be allocated to the import of the multinational's products. The new or rehabilitated project may have no connection at all with the usual business of the multinational company.

To give a hypothetical example, a Western vehicle manufacturer wants to export trucks to African country X which desperately needs the trucks but has neither foreign exchange nor access to credit to pay for them. Country X does not even have exportable goods available which it can offer for countertrade. The vehicle manufacturer, therefore, agrees to provide investment funds and some technical assistance to rehabilitate an oil palm processing project which was lying dormant, on condition that the government of Country X enters an agreement whereby some of the foreign exchange funds earned from palm oil exports enter an escrow account held in London and are used to pay for Country

X's imports of trucks. The arrangement is beneficial to all parties concerned because the vehicle manufacturer obtains export orders it would not otherwise have obtained and Country X receives trucks it could not otherwise have afforded as well as the employment and other benefits of a rehabilitated project.

There are only a limited number of examples of such ideas being put into practice but a few are given below. The examples not only include cases resulting in the production of export commodities but also export services and some instances of investment in trading/procurement organisations. In short, they include any countertrade deal which actually involves the foreign partner in contributing, through investment or other means, to the exporting operation of the developing country partner.

(i) In 1984, Motors Trading, the countertrading arm of General Motors, helped to establish a data processing facility in Jamaica by installing a computer and employing local workers at a considerably lower wage rate than equivalent American operators. Raw data were flown down from the USA, processed and returned. The purpose of the exercise was to earn foreign exchange because Jamaica, at that time, faced a problem in paying for General Motors' vehicles in hard currency. The arrangement worked on the basis that the foreign exchange earnings from the data processing company were recorded in an evidence account and were allocated to the import of vehicles.

(ii) The Ford Tractor Company has engaged in imaginative countertrade deals in a number of countries. One particular deal involves a South American country which had no foreign exchange to pay for tractors and no export products to offer for countertrade. Ford Tractor searched for opportunities and found that oranges and other citrus fruits were being grown in the country but were only sold on the domestic market. The company used its contacts in North America to find export markets and also put in some technical assistance to improve standards of packaging and presentation. After some successful trial shipments, the Ford dealer in the country invested in packaging machinery, recruited staff and organised supply from citrus growers on a contract basis. The foreign exchange revenues are used to fund the import of tractors.

Other known examples include a major international chemical company which has invested in cotton by-products in an African country in order to supply agricultural chemicals in return, and an international commodity trading house which invested in food (frogs' legs) exporting facilities in Bangladesh in return for supplying various commodities.

5.3. Difficulties

Although the ideas outlined in this chapter have many points to recommend them, there are also a number of associated problems and pitfalls, both from the point of view of the foreign partner and the developing country.

The developing country will gain nothing from such schemes if the production/ investment project would have happened in any case. This would only result in the foreign exchange earnings of the project being unnecessarily tied. The only real benefit arises if the production/investment project would not have happened without the countertrade deal in question and can be shown, therefore, to have resulted in incremental exports. Also, it is important that the project chosen should have a low foreign exchange input component; there is clearly little point in developing countries pursuing such schemes if the net earnings of foreign exchange are low.

From the point of view of the foreign partner, such schemes are likely to be viewed as highly risky. In the first place, the time period for making any profit out of the deal may be quite long. (This is one reason why foreign companies are more likely to be attracted to low cost/fast response schemes, such as rehabilitation projects or the establishment of procurement/trading companies, rather than embarking on high cost production projects.) Secondly, it often (but not necessarily) involves entering an area of business in which the company has no experience. Thirdly, the project selected for the production/investment component must be highly profitable in order both to repay the investment and to have foreign exchange left over for countertrade purposes. Fourthly, the sort of countries where these schemes are likely to be the most necessary are also the sort of countries for which it is difficult to obtain loans and credit insurance cover. In fact, it has often been suggested, and there are some signs that progress is being made, that aid agencies could be particularly instrumental in the supply of loans and credit insurance cover if they were prepared to take a more enlightened view of schemes involving countertrade.

It is difficult for developing countries to develop a general policy on production and investment-related countertrade because each case needs to be judged on its merits. However, it is possible for developing country governments to at least express a willingness to consider suggestions for such schemes so that the onus is put on foreign partners to draw up proposals.