

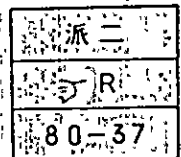
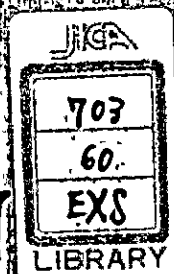
REPORT ON THE PROMOTION OF INDUSTRIAL DEVELOPMENT
BY JAPANESE INVESTMENT
IN THE STATE OF MINAS GERAIS.

Submitted to
Instituto de Desenvolvimento
Industrial de Minas Gerais

October 1980

Prepared
by
Hideo Ueki

Expert Dispatched by Japan International Cooperation Agency
Industrial Economist,
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Acknowledgment

This report is aimed to present personal observation summarized from consulting cooperation with INDI (Instituto de Desenvolvimento Industrial de Minas Gerais) for 45 days under the technical cooperation program by JICA (Japan International Cooperation Agency) on the development of industrial location in conjunction with direct investment from abroad (Japan) in the State of Minas Gerais. The format of report is principally based on the outline requested by INDI.

During the stay in Brazil, various kind cooperation for the fulfilment of working tasks was pleasantly shared with many people of the organizations such as INDI, CDI, CEMIG, CEBRAE and CEAG-MG, BDMAG, SENAI, Consulado Geral do Japão (Rio de Janeiro), JICA and JAMIC, JETRO (São Paulo and Tokyo), Câmara de Comércio e Industrial Japonesa do Brasil (São Paulo and Rio de Janeiro), in addition to many private enterprises in Brazil which generously accepted field interviews and provided relevant information. Hence, appreciation should be honored respectfully to all of the good people associated with organizations above.

However, the contents and views of this report are personal ones, and do not necessarily represent organizations where the expert is associated.

Wishing this working report to be something helpful for all of those who concern industrial development for the State of Minas Gerais through Japanese technical cooperation.

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1. Trends of Japanese Enterprises toward Investment in
Brazil

1.1 Profile of the Japanese Foreign Investment by Region,
Industry and Scale

The total amount of Japanese foreign direct investment during 1951 until 1979 (permission base) was US\$ 30,214 million, and the share of Brazil was US\$ 2,691 million (8.9% of the total). Since the share of Latin America was US\$ 5,007 million (16.7%) during the same periods, the share of Brazil occupied 53.7% of Japanese direct investment in Latin American Region.

Japanese investment in Brazil by industry is shown in the Table 1 below. It is noteworthy characteristic that manufacturing industry occupied 74.3% of the total, besides the concentration is on the manufacturing sectors such as Electric and Communication Apparatus (11%), Textile (10%), Machinery (9%), and Metals (9%).

Nextly, let us identify the Japanese investment by scale. In accordance with statistics released by Small and Medium Enterprises Agency of Japan, total permit cases of Japanese foreign investment were 2,395 in 1978, and 1,219 cases (about 51% of all) were composed by small and medium scale

Table 1. Japanese Direct Investment in Brazil by Industry
(as of December 1973)

(Unit: thousand dollars)

	J a p a n			Share by Sector(%)
	Direct Investment	Reinvestment	Total	
(1) Mining	14,576	1,107	15,683	1.12
(2) Manufacturing	947,960	94,197	1,042,157	74.26
Iron and Steel	122,750	3,309	126,059	8.98
Metals	81,628	8,626	90,254	6.43
Machinery	123,300	5,775	129,075	9.20
Electric and Communication Apparatus	140,179	20,714	160,893	11.47
Automobile	45,582	2,431	48,013	3.42
Auto Parts	7,339	-	7,339	0.52
Chemical Raw Materials	27,635	727	28,362	2.02
Oil Related Goods	18,630	183	18,813	1.34
Pharmaceutic Goods	490	9	499	0.04
Textiles	121,802	15,953	137,755	9.82
Food	32,082	8,087	40,169	2.86
Tabaco	826	24	850	0.06
Other Manufacturing	225,717	28,359	254,076	18.10
(3) Public Utility	52	11	63	0.00
(4) Agriculture	5,624	-	5,624	0.40
(5) Services	261,457	14,395	275,852	19.65
(6) Others	63,171	954	64,125	4.57
(7) Total	1,292,840	110,664	1,403,504	100.00
(8) Share by Country (%)	14.53	2.29	10.21	-

Source: Boletim do Banco Central do Brasil, (Separata), Junho de 1979.

enterprises. The main region of Japanese foreign investment by small and medium scale enterprises is concentrated on U.S. (54%), Asia (30%), and Latin America (7%).

As shown by the Table 2 below, 727 cases (30.4% of the total cases in 1978) were composed of manufacturing industries and 290 cases of them were composed of small and medium scale enterprises (39.9% of all manufacturing cases). As a trend of Japanese manufacturing investment, machinery (electric and ordinary) and metal working sectors are increasing recently.

1.2 Most Attractive Sectors in Brazil

In accordance with recent questionnaire survey conducted by Small Business Corporation of Japan, 294 small and medium enterprises among 869 samples showed interests in foreign direct investment. Although about 128 enterprises (70%) of those candidates consider Asia as investment location, the numbers of candidates which selected Latin America as suitable location is only 13 (4.4%). Accordingly, these 13 enterprises which might be mostly interested in Brazil are the following sectors.

- Transportation Machinery Equipments
- Electric and Ordinary Machinery
- Metal and Non Ferrous Metal Works (Molding)
- Wood Processing and Furniture Works

- Rubber Products
- Fertilizer

In addition to the sectors aforementioned, the following attractive sectors could be added for the State of Minas Gerais from the local observation and field investigations through interviews with industrialists in Minas.

- Electric and Electronics Components
- Extraction and Smelting Process of Mineral Resources
- Motor Cycles (and Bicycles)
- Machinery Equipments for Process Controle
- Measuring Gauges and Tools
- Packaging Machinery
- Plating and Heat Process
- Agro-industries (Food, Soybeen Processing, Biomas Energy, etc.)

Table 2. Trends of Japanese Foreign Direct Investment by Industries

(Unit: Cases, %)

	1 9 7 6				1 9 7 8			
	Total		M.S. Enterprise only		Total		M.S. Enterprise only	
		(%)		(%)		(%)		(%)
Agriculture and Fishery	78	4.7	33	6.1	104	4.3	42	3.5
Mining	36	2.2	1	0.2	27	1.1	2	0.2
Manufacturing								
Food Processing	44	(10.7)	18	(13.4)	67	(9.2)	37	(12.7)
Textiles	38	(9.2)	12	(9.0)	65	(8.9)	37	(12.7)
Wood Processing and Paper Pulp	20	(4.8)	6	(4.5)	17	(2.3)	NA	-
Chemical	59	(14.3)	12	(9.0)	67	(9.2)	14	(4.8)
Steel and non Ferrous Metals	44	(10.7)	11	(8.2)	141	(19.4)	19	(6.6)
Ordinary Machinery	57	(13.8)	21	(15.7)	92	(12.7)	35	(12.1)
Electric Machinery	67	(16.2)	24	(17.9)	143	(19.7)	73	(25.2)
Transport Machinery	26	(6.3)	3	(2.2)	23	(3.2)	5	(1.7)
Others	58	(14.0)	27	(20.1)	112	(15.4)	70	(24.2)
Sub Total	413	25.0 (100.0)	134	24.7 (100.0)	727	30.4 (100.0)	290	24.2 (100.0)
Construction	58	2.5	19	3.5	64	2.7	13	1.1
Commerce	476	26.0	221	40.8	654	27.3	363	30.3
Finance & Insurance	41	1.9	1	0.2	25	1.0	-	-
Services & Others	357	15.3	115	21.2	412	17.2	202	16.8
Real Estates & Branches	193	13.6	18	3.3	382	15.9	287	23.9
Total	1,652	100.0	542	100.0	2,395	100.0	1,199	100.0

Source: Small and Medium Enterprises Agency, April 1980 (Survey data was compiled by Small Business Corporation from original statistics of Central Bank of Japan as of October 1979).

2. The State of Minas Gerais as an Industrial Location for Japanese Enterprises

2.1 Main Advantages

- (1) There are abundant endowments of mineral resources and agricultural products.
- (2) Industrial districts developed by CDI (Compania de Distritos Industriais) are available as new industrial location, and the land cost is relatively cheaper.
- (3) Cheaper labours are available.
- (4) Technical support of INDI and CEMIG are available.
- (5) Financial support such as Fondo de Apoio Industrial, Banco de Desenvolvimento de Minas Gerais, Minas Gerais Participações S.A., etc. are available.

2.2 Main Constraints

- (1) Related supporting industries are insufficient, especially there are difficulty of subcontracting with local small and medium scale industries due to constraints of technology and quality of their products.
- (2) Level of Labour skills is considered as lower than

São Paulo, hence more training at enterprises is necessary.

- (3) Attitudes of mineiro are considered to be a little conservative and less innovative compared with Paulista and Carioca due to their fewer experiences of international transactions with foreigners from the frank point of view by Japanese industrialists.
- (4) There are educational problems for the children of Japanese families in the State of Minas Gerais.
- (5) Electric and communication infrastructure is not completely sufficient due to the exhausted parts of equipments of electric relay and systems, despite of sufficient capacity of electricity by CEMIG.

2.3 Ways to Improve Conditions

Appropriate remedies for the betterment of constraints aforementioned are required in general. For example, in order to solve the constraints of few supporting industries as subcontractors, not only the technical help of CEAG (Centro de Apoio a Pequena e Média Empresa) under CEBRAE (centro Brasileiro de Apoio a Pequena e Média Empresa) but also direct technical and financial assistance from large enterprises to local small and medium enterprises are indispensable. Hence, Japanese experiences and know-how to improve the problems might be effective when applied appropriately in Brazil through

Japanese technical cooperation.

As for the up grading of labour skills, the role of SENAI is of vital importance. Accordingly, Japanese technical assistance for SENAI's new courses on electric and electronics through JICA cooperation program under implementation would be expected to improve the constrained conditions. However, effective Japanese technical training programs at Japanese affiliated enterprises in Brazil should be continued and also reinforced by using existed Japanese official cooperation programs for Brazilian technical training.

2.4 Evaluation of existing industries in Minas Gerais

Most of Japanese affiliated enterprises are facing the phase of expansion of production capacity as well as diversification of their products lines. That is why it might be necessary for INDI and CDI to provide additional updated information and appropriate support upon their interests of expansion plan.

3. The Investment Decision in Japan

3.1 Motivation and Process for Investment Decision

The Main Motivation of foreign direct investment by the foreign business oriented Japanese small and medium enterprises is mostly reinforcement of sales in local market (37%), and utilization of local labour (24%). Besides, other motivation such as utilization of plant equipments or technology (19%), and export to third country (17%) is also significant as shown in Table 3.

Table 3. Motivation of Foreign Direct Investment

(Unit: Number of Enterprises)

	Yes	(%)
(1) Reinforcement of sales in local market	109	37.1
(2) Utilization of plant equipments or technology	57	19.4
(3) Export to third country market	49	16.7
(4) Reinforcement of competitiveness by international subcontracting	48	16.3
(5) Reinforcement of collecting foreign business information	47	16.0
(6) Security of Raw materials supply	23	7.8
(7) Utilization of company personnels	21	7.1
(8) Utilization of capital	16	5.4
(9) Risk management against variation of foreign exchange	14	4.8
(10) Harmonization of trade conflicts	9	3.1
(11) Others	4	1.4
(12) Not available	69	23.5
Total	294	100.0

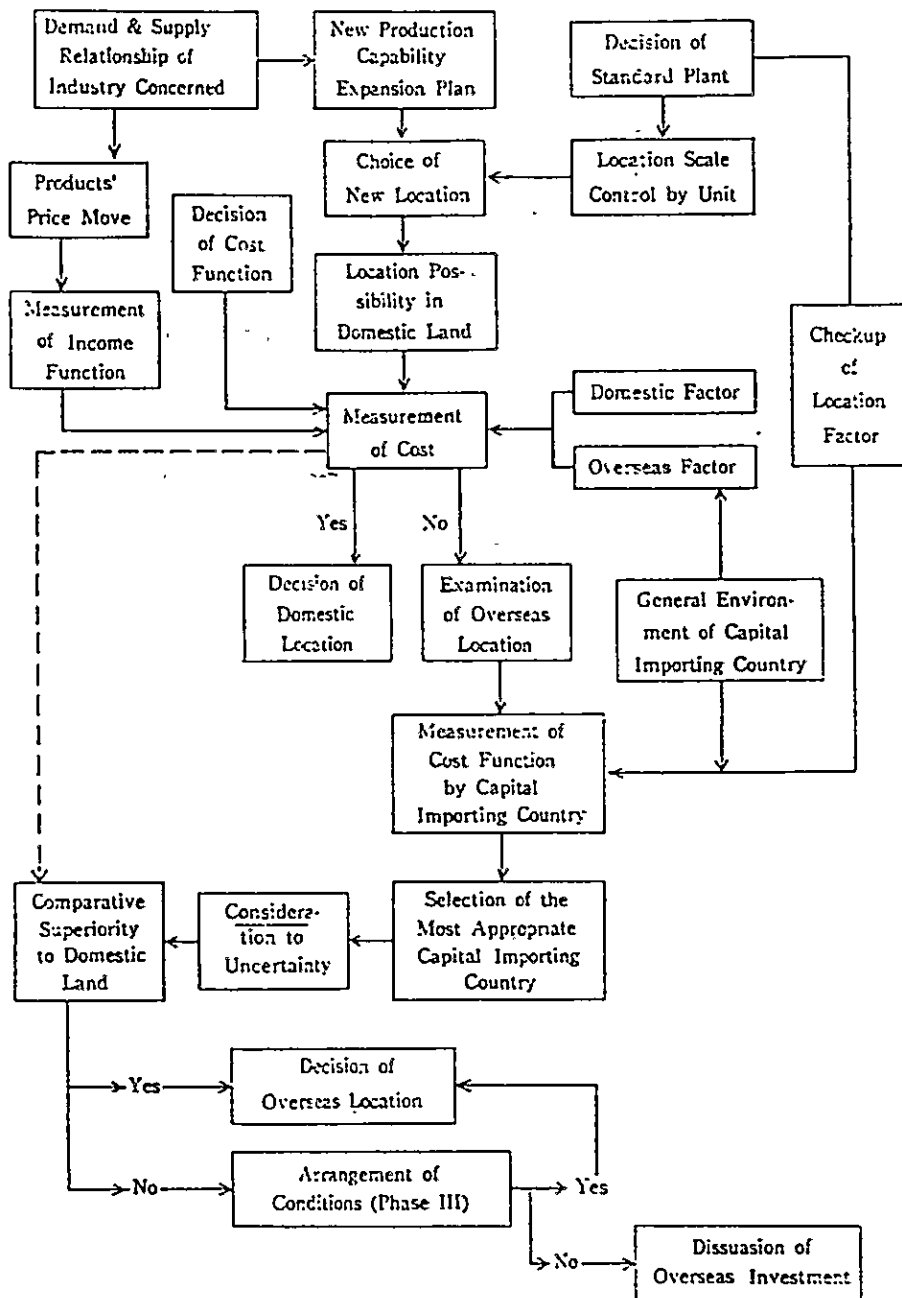
Source: Small and Medium Enterprises Agency of Japan, April 1980
(Survey was conducted by Small Business Corporation).

The typical process of Decision Making for Japanese foreign investment is shown as Figure 1 below. During the screening of the foreign investment, Japanese enterprises face the difficulty to get the following qualitative and quantitative information:

- (1) Investment policy, taxation, and legal systems toward enterprises by host governments,
- (2) Commercial and social customs and practices,
- (3) Credibility of local partners,
- (4) Economic and industrial trend,
- (5) Education and technological standard of labour,
- (6) Marketability,
- (7) Standard of living and consumption behavior,
- (8) Related supporting industries,
- (9) Infrastructure and industrial estates, etc.

The planning and research for the foreign investment project is usually initiated by the middle management at Japanese enterprises, and authorized by the top management after long terms of checks through organizational bottom-up concensus system, so called "Ringi". Hence, it is required to keep contacts on the industrial investment consulting and/or negotiations with right functions of the candidates' organizations.

Figure 1. Decision Making Process for Foreign Investment



Source: MRI, Evaluation of International Development of Industry. March 1972, p.4.

3.2 General Constraints and Concerns of the Japanese Enterprises in Brazil

- (1) Communication problems due to language difficulty restrain initial business contacts as well as initial periods of joint operations until both parties understand well each other.
- (2) Higher inflation in Brazil and current economic stagnation of the world restrain new industrial investment, unless high return on investment is expected.
- (3) There are few multiple channels to find out credible local entrepreneurs on joint ventures, besides there are difficulty of the management operations of joint ventures due to the lack of enough preparatory feasibility studies and experiences for the joint projects.
- (4) Import restriction of intermediate materials and parts due to the balance of payment deficit of Brazil caused many divestment cases during the last few years, hence the uncertainty image is still remained with foreign enterprises, although this import restriction law was amended by the new economic policy as of December 1979. Hence if this kind of legal information is more properly disseminated among Japanese enterprises, decision maker of industrial investment can find more immediately

that it will be easier for exporting makers to keep export more competitive except special cases and area based on the amendment of the law.

- (5) It has been usually difficult to get authorization from INPI for the payment of foreign technical loyalty incurred from joint ventures with foreign licencer (including Japanese partner).
- (6) The new law for foreigners seems to restrain motivation for new industrial investment in Brazil. Hence, more flexible amendment for the foreign entrepreneurs is expected.

3.3 General Constrants in Minas Gerais

- (1) The supply of investment information toward Japanese enterprises and industrial associations in Brazil and Japan are not sufficient from Minas Gerais in general.
- (2) Local supporting small and medium industries has not been developed sufficiently as yet.
- (3) There are fewer settlements of Japanese immigrants in Minas Gerais compared with São Paulo, Rio de Janeiro, and Parana State. Hence, the role of immigrant entrepreneurs as a motivater for new industrial settlement in Minas from Japan is still limited. However, 3 Japanese restaurants and

cultural society facilitate Japanese industrial settlement as a transitional stage of accommodation until they are accustomed to Brazilian culture and way of living. More cultural exchange and bilingual language institution between Japan and Minas should be promoted through the international cooperation by both official and private sectors for the mutual benefits. Promotion of sister States friendly relationship between Yamanashi and Minas Gerais might be desirable in order to encourage mutual transactions.

4. The Promotion Strategy to Japan

4.1 The Most Effective Means to Establish Contact with Japanese Enterprises

The following alternative and/or some combination approach should be taken into consideration.

- (1) Establishment of a representative in Tokyo. The possibility of setting up a common representative office with other interested states may be also recommended to minimize direct cost. (It is noteworthy that there are already 34 states or country based representative offices in Japan from 12 foreign countries.)
- (2) It is effective approach to use Japanese consulting agent and/or investment consultants for the promotion of investment and trade transactions between Brazil and Japan.
- (3) It is required to have frequent opportunities for direct visiting and meeting with Japanese businessmen and associations by such as industrial missions (both official and private enterprises level).
- (4) It is necessary to provide foreign investment seminars to arouse interests on direct investment opportunity and joint ventures with local enterprises in São Paulo and Japan.

4.2 Promotion strategies of INDI for Japanese industries

- (1) More systematic promotion approach is necessary. Representative office of INDI at São Paulo and Rio de Janeiro must be more effectively coordinated.
- (2) More supply of appropriate information exchange with Japanese enterprises is necessary in order to attract industrial investment in Minas Gerais. Investment information must be effectively disseminated to the Japanese enterprises through appropriate PR media and languages.
- (3) The promotion approach is relatively taken from the interests of the State of Minas Gerais and INDI side, hence it is required to have more knowledge and information on the investment interests from the side of Japanese industries.
- (4) Up to now fewer attention and promotional efforts have been taken for Japan compared to Europe and U.S.A.. Accordingly, mailing contact lists of INDI should be added much more with Japan, and appropriate pamphlets on investment, which are translated in Japanese must be prepared.
- (5) Since direct mail approach is not always effective unless interests of both parties are justly met. Therefore, it will be more recommended for INDI to develop face to face communication contact with Japanese enterprises and associations, and to follow-up consulting activities for them.

4.3 Multipliers in General as a Channel of Contact

(1) In Brazil

- São Paulo:
- * JETRO (Organização Oficial de Comércio Exterior do Japão)
 - * Câmara de Comércio e Indústria Japonesa do Brasil
 - * Japan Overseas Enterprises Association
- Rio de Janeiro:
- * Câmara de Comércio e Indústria Japonesa do Rio de Janeiro
 - * Consulado Geral do Japão

(2) In Japan

- * JETRO
- * Japan Chamber of Commerce
- * Japan Overseas Development Corporation (The liaison officer is stationed at JETRO office of São Paulo.)

5. Evaluation and Suggestions

5.1 General Evaluation

For the sound industrial development of the State of Minas Gerais, which are endowed with abundant mineral and agricultural resources, it is vital concerns to foster the secondary manufacturing industries which will contribute to the creation of employment and income for Brazilian people by grading up the finished products with more value added.

However, manufacturing industries are not yet well developed in Brazil mostly due to the technological and managerial constraints and lacks of related industries as supporting subcontractors and customers as well. That is why, the Third National Development Plan (1980 - 1985) emphasizes the reinforcement of small and medium scale enterprises.

Although CEAG-MG and CEBRAE has undertaken this task of reinforcing national small and medium enterprises and of promoting subcontracts between these enterprises, the effects of these challenging activities are still unfortunately limited due to the bottlenecks of their dislinkages with large national and foreign affiliated enterprises. This vital necessity was also supported from most of large scale existed enterprises.

5.2 Suggestion

From the results of observation and evaluation based on the field investigations, the following pragmatic step by step approach is suggested as problem solving.

- (1) It is necessary for INDI to continue the program of promotion with Japan side. Since it usually takes a long periods for the Japanese enterprises to take into consideration and make decision for the direct investments in Brazil, it has more importance to have a Japanese representative or consultants as effective multipliers to keep contacting with Japanese enterprises in Japan, so that these business information will be feedbacked with the promotional activities and technical supports from INDI, hence Japanese direct investments in Minas will be more appropriatly coordinated.

- (2) It is desirable for INDI and JICA to undertake the joint study on the fostering of industrial subcontracting enterprises in the State of Minas. Accordingly it is necessary to conduct preparatory feasibility study on Japanese direct investment in the appropriate industrial sectors aforementioned from the standpoints of fostering subcontracting enterprises as supporting industries through linkages effects between existed large industries and national

small and medium scale enterprises.

- (3) In order to follow up the Japanese cooperation program suggested above, the following alternative cooperation step is recommended.

Alternative (A)

Since the periods of dispatching an expert from JICA was so short this time, it is necessary for INDI to request the expert again from JICA next year, in order to follow up the investment promotion for the suitable sectors of Japanese industries as mentioned before and conduct pre-feasibility studies on Japanese direct investments in Minas Gerais together with relevant staff of INDI.

It is desirable to conduct preparatory research at related Japanese industrial associations and enterprises in Japan. After then, expert dispatched by JICA will be necessary for two or three months of joint work with INDI as the second phase of cooperation program. The results of this working reports and summarized pamphlets on investment guidance should be translated in Japanese to disseminate among Japanese related associations and private enterprises,

Alternative (B)

When the coverage of industrial sectors is diversified into several fields, and comprehensive

but technical feasibility studies including industrial linkages studies and demand forecasting of marketability in Brazil are required, JICA cooperation team composed of several technical experts might be helpful upon request from INDI to JICA.

- (4) It is recommended that after the joint studies aforementioned INDI will organize seminars on investment promotion in São Paulo and Japan, so that the fruits of joint F/S reports and recommendations offered from JICA expert could be effectively utilized for the investment promotion and implementation. When the investment decision is made after the F/S studies and promotion seminars, relevant joint venture enterprises with small and medium scale can use another Japanese cooperation program to ask technical specialists from Japan Overseas Development Corporation in Japan through JETRO center in São Paulo. JODC can also offer financing assistance with only 0.75% commissions for these joint ventures under the conditions which Japanese partner will be minority ownership position within several years of operations so that local Brazilian entrepreneurs and managers will be fostered through appropriate transfer of technology and managerial know-how from Japanese enterprises at the local joint venture enterprises.

JICA