Distr.
GENERAL

UNCTAD/COM/30
21 April 1994

ENGLISH ONLY

UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

COUNTRY STUDY

ANALYSIS OF NATIONAL EXPERIENCES IN HORIZONTAL AND VERTICAL DIVERSIFICATION, INCLUDING THE POSSIBILITIES FOR CROP SUBSTITUTION

COLOMBIA

GE. 94-51724

CONTENTS

FOREWORD

1. The Committee on Commodities, at its fourteenth session, in November 1990, decided that priority should be given to the study of the impact of market conditions in importing and exporting countries with regard to diversification, including government policies, structural adjustment, forms and methods of trading, and technical assistance.[1] The Standing Committee on Commodities, at its first session, in October 1992, decided, in the same vein, that national experiences in horizontal and vertical diversification, including the possibilities for crop substitution, should be analysed, and that an examination should be made of the best ways of achieving diversification, taking into account competitiveness, market trends and opportunities

2. In accordance with these mandates, a number of country studies are being undertaken, in Cameroon, Colombia, Fiji, Senegal, Solomon Islands and the United Republic of Tanzania. The experience of these countries in the diversification of their commodity exports (including increased processing and diversification into commodity-related marketing activities) as well as the conditions influencing this are analysed. These conditions fall in two broad areas: the macroeconomic and international environment (including market access conditions), and the commodity-specific supporting framework (in terms of services supplied by the government or otherwise, infrastructure, market promotion support, etc.).

3. The approach attempts to identify the key factors that gave rise to commodity export diversification, or prevented the exploitation of diversification possibilities. It includes questions as to which were the important factors that led to and facilitated the establishment of new export-oriented productive activities; what were the problems these new activities encountered, and, if they were overcome how was this done; or, if they were not overcome, were there gaps in the supporting environment, and, in particular, government policies. No attempt is made to decide whether macroeconomic policy is more important than microeconomic policy, or vice versa; or whether cheap credits are more useful for an exporting company than good market information networks. Rather, an attempt is made to describe which package of conditions is necessary to make export diversification viable, and which package of policy measures seems to enhance the chances of export diversification efforts.

4. The goal of these studies is not to formulate specific policy recommendations for the countries under study. Rather, it is to draw conclusions on the sorts of policies that would facilitate diversification, the support services that are absolutely necessary to enable local entrepreneurs to make use of existing possibilities, and the ways in which a country can reap greater benefits from the marketing of its commodities. At the present time, many countries are in the process of policy reform; and diversification of exports is usually one of the envisaged outcomes. However, the resources available to stimulate such diversification are scarce, and in general countries do not have the information necessary to determine how their resources can be used optimally. These studies will, it is hoped, support the process of policy formulation in developing countries in this area.

---

[1] TD/B/C.1/L.96, 21 November 1990, para. 12.

[2] "Establishment of the work programme of the Standing Committee" (TD/B/CN.1/8), 3 February 1993.

SUMMARY AND CONCLUSIONS

5. Colombia's economy has traditionally been rather a closed one. It still is - but an "opening up" is already perceptible. Whereas Colombia's per capita exports in the early 1980s equalled one third of the average for Latin American countries, by the late 1980s this proportion had increased to two thirds. In value terms, its exports doubled during the past decade, with most of their growth taking place in the second half of the 1980s. This growth was based on products other than coffee, Colombia's traditional main export, and the share of coffee in exports more than halved. However, as fuel exports, virtually absent at the beginning of the decade, have now outstripped exports from the coffee sector, Colombia was more dependent on its four main exports in 1990 than it was in 1981.

6. The economy's export diversification should be evaluated in terms of the increase in the range of products exported and in non-traditional exports. In both respects, Colombia has done quite well. From 1986 (when economic policy was liberalized) to 1990, a wide range of products - commodities, in raw or processed form, and manufactures - which were formerly not exported found their place in the list of significant export products, and non-traditional exports more than tripled in volume.

7. Among the primary commodities that increased considerably in export importance during the 1980s were crude oil, coal, flowers, fishery products, and fruit and vegetables. Crude oil and coal exports were developed through large-scale investments financed to a great extent by transnational companies or by foreign lending. Consequently, much of the export proceeds from this sector are lost through debt reimbursement, profit repatriation, etc. The strong expansion of flower exports - Colombia is now the world's second largest flower exporter - was made possible by the capacity of the local private sector to invest important sums in the development of this export item. For fishery products and fruit and vegetables, a combination of local private capital and government support made the development of exports possible.

8. There has been a strong expansion in Colombian exports of processed commodities as well. Again, a major part of this trade was developed during the 1980s. The exports of most of the products involved - among others leather and leather goods, white sugar and citric acid - were developed by domestic private enterprises; only in the development of ferronickel production has the Government played a major role.

9. Marketing of commodities is to a large extent in Colombian hands. Sales operations of the State coal and fuel enterprises are well developed, as are the operations of coffee exporters - this has been an important factor in Colombia's increasing share of the world market in these sectors. Enterprises in the banana and flower sectors have diversified vertically into distribution networks in the USA and EC, and into worldwide marketing operations. Foreign involvement in marketing is substantial for a few processed commodities only - ferronickel and, to some extent, coffee extracts. In their case, the involvement of transnationals in marketing has been essential for securing market access.

10. The diversification of the economy has helped to create employment and to increase export earnings. Moreover, export-related commodity diversification has had important linkage effects. For example, the infrastructure created primarily for flower exports has played a significant role in making fruit exports possible. Backward linkages have resulted in the creation of companies producing, for example, packaging materials, and art and graphics firms - essential for further diversification into brand name products. Diversification has also had learning effects, creating both the managerial and the marketing skills needed for entering into yet other activities.

11. This diversification has taken place in an environment that has not been altogether conducive to an expansion of export-oriented production. A lack of financial resources and the underdevelopment of the domestic capital market limits both the ability of the Government to finance support services such as research institutes, market identification services, and mineral prospecting, and the capacity of the private sector to finance large-scale projects. The setting of priorities was thus essential for an optimal use of such financial capacities as existed. Moreover, the inward-looking policy of the past meant that the Colombian economy was not well structured for a rapid reorientation towards exports: road, railway and waterway infrastructure are domestically oriented, and ports are poorly organized; most industries are located inland, far from seaports; Colombian entrepreneurs have not yet had time to build up the skills and organizational structure necessary for exporting; and support structures, such as specialized export houses or experienced export consultants, are still rare.

12. Government policies have been important for the diversification of commodity exports. Diversification out of coffee has been a long-term goal of Colombian economic policy, dating from the 1940s. Earmarking of the necessary funds was an important aspect of this policy. The association of coffee producers drew up its first five-year diversification plan in 1960, funnelling resources from coffee into the development of other products. In the 1980s, the fuel sector was also taxed to finance the development of other mineral exports. Taxes on imports were used to fund a large-scale programme of government support to the export sector. The resources from a tax on major exports and import taxes were used, among other purposes, to finance research and development on alternative production and export possibilities; to support the adaptation of existing production facilities to the requirements of the world market; to finance processing factories; to make subsidized credits available to non-traditional export sectors; to provide other financial rebates, in the form of import tax exemptions and domestic tax rebates, to non-traditional export sectors; to identify potential markets and fund promotion campaigns; and to create export marketing companies. A number of export industries created during the 1980s, such as silk production, shrimp farming and passion fruit production, were the direct result of this government support. The Government adapted its support to the needs of each sector: for example, when anti-dumping actions taken by the United States became the main obstacle for flower exports, lawsuits to counter these anti-dumping actions were financed out of the government-administered Diversification Fund.

13. But a real expansion of exports only took place after macroeconomic policy changed in the mid-1980s. While the macroeconomic adjustment has caused problems because of its speed, leaving little time for enterprises to adapt, and policy has not always been as predictable as exporters would wish, its general effects have been to support the export structure - partly because macroeconomic policy is now

determined in close cooperation with the various associations of exporters. The Colombian peso is kept at a level that ensures the competitiveness of Colombian exports; exporters have access to the imports they need for efficient production; the liberalization of investments has made it possible to tap both foreign finance and know-how; and infrastructure policies are helping to overcome the transport barriers of the past. The emphasis in government support has shifted from a series of discretionary measures on the output side (export subsidies; marketing support) to the provision of support at the beginning of the production chain, among other things, to manpower training, technology development and the relocation of industry closer to seaports.

14. The diversification of Colombia's commodity exports seems to have been the result of five factors:

- the existence of a relatively well developed private sector, having at its disposal a well trained labour force with many of the specific skills necessary for adapting to export-oriented activities
- a supportive macroeconomic environment from the mid-1980s onward, with government policies often decided in cooperation with the private sector;
- a general framework of government support services that enabled private entrepreneurs to initiate new exports, and, that, during the early 1980s, protected specific export sectors against a poor macroeconomic environment by compensatory subsidies;
- the willingness of the Government to undertake specific, focused activities to support new export sectors at critical moments;
- access to foreign capital, technology and marketing know-how.

15. However, government policy can be still further improved. Policy changes may have taken place too quickly, not allowing enough time for the private sector to adapt, and without a government 'safety net' to ensure that, to the extent possible, exporters can make the transformation from domestically-oriented production to production for export. Moreover, exporters suffer from the credit squeeze and the difficulty of exchanging dollars into pesos, which are a result of monetary policy. These elements of economic policy need attention in order to ward off negative consequences, especially for smaller companies that are less able to adapt to changing conditions than larger enterprises.

Chapter I

THE DEVELOPMENT OF DIVERSIFICATION POTENTIAL, AND DIVERSIFICATION EXPERIENCE

16. Colombia, with a population of 34 million and a gross domestic product of US$ 40 billion (in 1989), is one of Latin America's larger economies. It was also traditionally a rather closed economy, oriented at import substitution rather than open to the international market, with, in the early 1980s, per capita exports of just a little over one third the average for Latin American countries (see table 1).

Table 1
Per capita exports
(US$)

	Average Latin America	Colombia	Brazil	Chile	Mexico	Peru	Venezuela
1981	318	112	191	345	283	183	1,312
1989	277	184	232	639	260	163	661

Source: Based on data in UNCTAD, *Commodity Yearbook* and *Handbook on International Trade and Development Statistics*, 1991.

17. The 1980s showed the first signs of change, however, with Colombia beginning to strengthen its links with the international economy. Whereas exports in most of Latin America contracted, in Colombia they expanded, at a rate second only those of Chile. Exports are still relatively low, but are bound to expand further when the investments and policy changes of the 1980s start to bear fruit. In Colombia's current economic programme, export-oriented activities, especially non-traditional ones, receive high priority. But there have been difficulties in the shift from import substitution to different export orientation. Colombia's policies, problems and results in effecting the shift, which are discussed in the following chapters, may prove of relevance to other countries wishing to restructure their economies.

A. Export experience

18. Exports of goods account for about two thirds of Colombia's official foreign exchange earnings, exports of services for one fifth, and capital transfers for the remainder. These capital transfers do not include those related to the export of illicit drugs, which are illegal and therefore unreported. Estimates on the amount of foreign currency repatriated of by drug traffickers vary between US$ 2.8 billion and US$ 3.5 billion for the early 1990s, equal to half of the earnings of official exports of goods (and two and a half

times as much as the export revenues from coffee).[3] Taking into account the fact that a certain proportion of exports of emeralds and gold is also unregistered, the official figures that are used in this report therefore reflect only a part of Colombia's export experience.

19. Colombia's registered exports increased very rapidly during the 1970s, from US$ 0.7 billion in 1970 to US$ 3.3 billion in 1979. Coffee exports more than quadrupled during that period, to reach US$ 2 billion in 1979. After peaking in 1980, a year with exceptionally high coffee prices, exports then remained fairly stable in the early 1980s, but showed a strong growth in 1986 when coffee prices were again at a very high level (see graph 1). When coffee prices fell again in 1987, fuels took over as an engine of export growth. The period after 1986 also shows a strong growth by manufactured exports, and by exports of agricultural products other than coffee. Overall, exports continue to increase, and Colombia's current account shows a growing surplus. In effect, the surplus on Colombia's current account, coupled with the supply of dollars obtained by illegal exports, has started to become a problem for the Government: as they push the exchange rate up, and therefore threaten the viability of regular export activities.

Graph 1

Colombian exports by commodity group, 1970-1990

Source: UNCTAD and INCOMEX data. Minerals include gemstones and gold; manufactures include cotton

[3] It is estimated that a further US$ 1.2 billion is invested abroad annually. See "Colombia: resilient, but for how much longer ?", *Latin American Economy & Business*, January 1993.

B. Commodity-related diversification experience

20. The share of coffee in Colombia's export earnings was very high until the late 1960s (when coffee accounted for about 61 per cent of exports). Dependency on coffee remained high during the 1970s, and until 1986 coffee continued to account for more than half of export earnings (see graph 2). By 1990, this percentage had declined to as little as 20 per cent, and since 1989 fuel exports have been larger than coffee exports.

Graph 2

Composition of Colombian exports: traditional and non-traditional exports as percentages of total exports, 1970-1990

21. Colombia's declining dependency on its traditional main export should not hide the fact that, in relative terms, it became more dependent on a few commodities only during the 1980s. As graph 2 shows, the share of coffee, fuels, gold and bananas in total exports was higher in 1990 than in 1981.

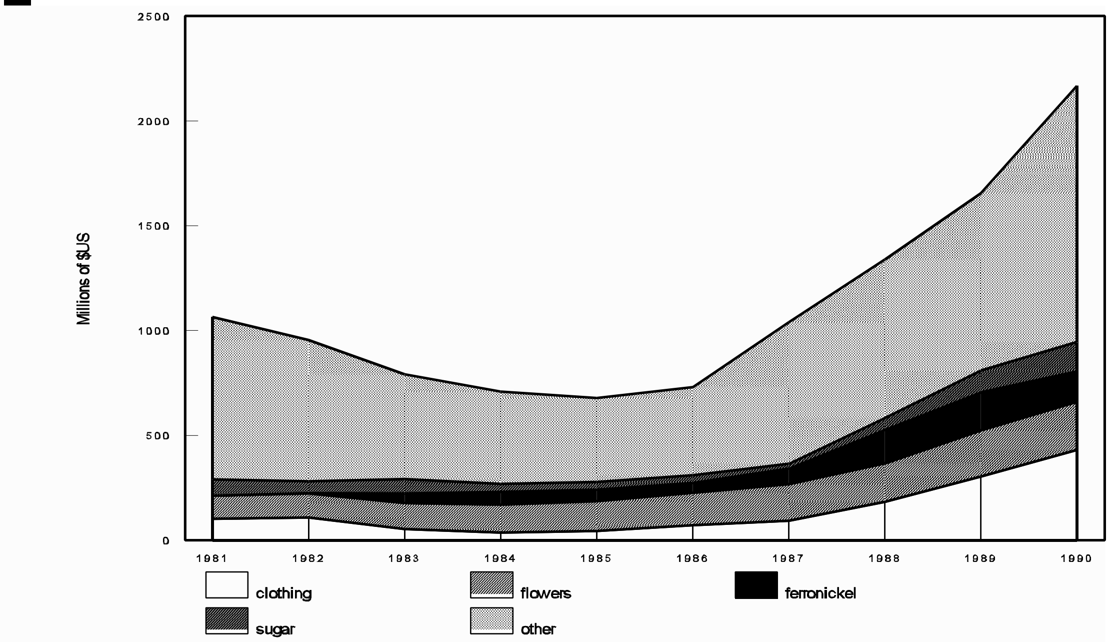
22. Thus, Colombia's diversification experience is visible only when absolute export figures are considered. Graph 3 shows the growth of non-traditional exports during the 1980s. In 1990, non-traditional exports were more than twice as high as in 1981, and triple their level in 1986.[4] Table 2 tracks

[4] The strong growth of textile exports is somewhat misleading. A large part of Colombia's clothing exports is produced by 'assembly' factories, that do not use the cotton and cotton yarn produced in

the record of growth for Colombia's commodity exports, and, again, the growth of non-traditional exports is evident, including the introduction of commodities that were previously not exported, such as cocoa, white sugar and passion fruit juice.

Graph 3

The growth of non-traditional exports, 1981-1990



23. Colombia's diversification was not limited to the export sector. In effect, export diversification is an expression of both the diversification of the domestic economy, and of a growing export orientation of sectors traditionally oriented towards the domestic market. As is evident from table 3, both the mining and manufacturing sectors clearly became more export oriented during the 1980s. In the manufacturing sector, exports in 1989 were equal to one sixth of production, compared to one ninth in 1980. In the case of the

---

Colombia, but cloth imported from the United States, which is cut according to patterns designed in the United States, and then re-exported there. Some Colombian clothing enterprises have started to integrate backwards, though, and more Colombian materials are now being used, mainly for the production of simply designed clothing. See "Industry profile/Colombian textiles: tackling US protectionism", *Latin American Economy & Business*, January 1992.

mining sector, while its share in GDP more than doubled, its share in exports increased more than fivefold. The apparent decline in the export orientation of the agricultural sector is to a large extent the result of the base year chosen, a year when prices of agricultural exports were very high. In 1981, agricultural exports were equal to only one third of agricultural production.

Table 2

Main registered commodity exports, 1970, 1975, 1981, 1984, 1987, 1990
(mn US$, f.o.b. value)

	1970	1975	1981	1984	1987	1990
Coffee:						
- beans	467.0	672.0	1,423.26	1,764.50	1,650.65	1,414.72
- extracts	N.A.	N.A.	38.57	37.22	51.19	58.14
Fuels:						
- crude oils	64.1	-	-	-	942.36	1,539.69
- fueloils	12.1	98.3	32.32	445.16	334.64	354.58
- coal	-	-	6.26	33.81	245.54	536.95
- briquettes	-	-	3.12	4.03	6.35	7.78
- gasoil	-	-	-	-	12.93	27.77
- other fuels	-	-	-	-	49.07	27.27
Gold	N.A.	N.A.	239.00	245.00	384.00	374.00
Bananas	18.1	31.6	122.43	197.92	210.33	317.98
Ferronickel	-	-	-	62.36	75.90	146.31
Sugar:						
- raw	14.0	95.1	76.88	37.07	15.83	126.59
- white	-	-	-	-	5.23	13.85
- confectionery	N.A.	N.A.	4.27	2.54	3.73	6.10
- citric acids	-	-	3.80	5.04	7.61	7.92
Precious stones	3.5	12.7	63.88	24.48	57.41	111.50
Flowers:	1.0	19.3				105.95
- carnations			60.76	64.16	71.08	50.56
- roses			13.45	23.33	38.07	38.68
- pompons			20.08	25.68	33.06	6.07
- chrysanthemums			N.A.	N.A.	N.A.	
- other fresh flowers			15.31	20.13	31.62	27.24
Fisheries:	4.7	11.6				
- frozen fish			1.14	1.75	4.79	32.00
- frozen prawns			14.79	14.45	11.16	11.25
- other frozen crustaceans			2.93	24.40	43.38	68.03
Cotton	34.6	76.1				
- raw			93.42	48.10	46.70	46.61
- yarn			17.76	11.53	11.75	8.30
- cotton fabrics			29.47	27.13	42.01	32.55
Cement:	3.3	11.9				
- Portland			28.92	9.45	19.20	25.58
- clinkers			1.34	8.38	11.63	14.41
Cocoa:						
- beans	-	-	0.13	8.24	16.24	11.50
- butter	-	-	5.52	7.26	11.16	11.14
- chocolate	-	-	N.A.	7.08	2.34	N.A.
Hides & Leather:	6.7	16.5				
- hides & skins			0.63	1.18	9.01	10.01
- bovine leather			2.65	7.34	9.99	19.98
- leather handbags			9.80	4.18	10.94	16.65
- leather shoes			14.94	15.67	19.72	69.27
- other leather products			19.03	8.74	43.20	63.49
Rice	-	22.9	9.34	-	-	18.85
Bovine meat	21.8	56.8	25.71	10.07	21.64	13.01
Passion fruit juice	-	-	-	-	8.76	10.73
Tobacco	7.2	12.8	19.12	19.13	15.10	19.28
Platinum	-	-	-	8.90	10.44	14.00
TOTAL NET EXPORTS	**735.6**	**1,465.2**	**2,930.29**	**3,848.97**	**4,939.58**	**6,855.65**

Source: INCOMEX data, based on Colombian National Administrative Statistics Department (DANE) Customs documents. Total exports adjusted for re-exports. N.A.: data not available.

Table 3

The role of different sectors in GDP and exports and their export orientation, 1980 and 1989.

Sector	Share in GDP		Share in exports		Exports relative to gross production a/	
	1980	1989	1980	1989	1980	1989
Agriculture	19.4	18.0	77.2	40.8	65	42
coffee	3.5	N.A.	59.8	21.4	69 b/	86
Mining	2.3	6.4	7.2	39.9	51	115
crude oil	0.2	2.4	0.6	28.5	-	41
coal	0.1	0.7	0.1	7.9	5	80
gold	0.8	1.0	4.1	5.4	51 c/	85
Manufacturing d/	23.3	21.1	15.6	19.3	11	17

Sources: Ministry of Mines and Energy, *Estadisticas minero-energeticas 1940-1990*, Bogota, 1990; ECLAC, *Statistical Yearbook for Latin America and the Caribbean,* Santiago de Chile, 1990; INCOMEX data.

a/ Estimates, based on gross values for agriculture, mining and manufacturing, and volume figures for the separate commodities. The figure is higher than 100 per cent for mining in 1989 because of the high volume of mining imports (gross domestic production = consumption + investments + exports - imports).

b/ Domestic consumption amounted to 11 per cent of production, the rest was added to stocks.

c/ Until the mid-1980s, gold was not considered an export commodity, but as a way to boost the Central Bank's reserves. A major part of production was therefore retained within the country.

d/ Ferronickel production and exports are included in 'Manufacturing'.

24. At the same time that it diversified its exports, Colombia also diversified the market for its coffee exports (see table 4). Nevertheless, its dependency on only a few clients for all other main commodities remains remarkably high.

C. The benefits of commodity diversification

25. Commodity diversification has had benefits for Colombia other than making the economy less dependent on the vagaries of the coffee market. For one thing, commodity export diversification has created an important number of jobs and increased export earnings. After 25 years in operation, by the late 1980s, the diversification programme of the coffee association (Federacafe) in the coffee producing zones had resulted in the creation of 628,000 jobs and in additional exports worth US$ 306 million a year.[5] The flower sector, which appeared in the 1960s, had by 1991 generated 40,000 direct jobs (of which 70 per cent are held by women), and 25,000 indirect jobs.

---

[5] "La diversificación en la economía cafetera y el desarrollo nacional", (Diversification of the coffee economy and national development) *Nueva Frontera*, Special document, "25 años diversificando las zonas cafeteras", (25 years diversifying the coffee areas) June 1988.

Table 4

Market diversification for main commodity exports

Commodity	Country of destination	Percentage distribution			
		1981	1984	1987	1990
Coffee beans	Western Germany	36.3	30.5	32.2	32.1
	USA	18.9	23.9	20.2	18.3
	Japan	4.5	5.2	6.7	7.3
	Netherlands	8.8	6.1	5.7	5.5
	Eastern Germany	1.4	-	2.3	4.6
	Sweden	5.5	4.8	4.4	4.2
	Ten main clients	88.6	86.5	82.2	82.8
	Fifteen main clients	96.0	95.1	92.1	92.3

Coffee extracts	United Kingdom	21.9	10.1	44.1	23.3
	Japan	16.4	39.8	18.0	22.3
	USA	25.7	22.2	12.0	15.2
	Western Germany	19.3	4.9	6.0	8.2
	USSR	-	-	-	7.1
	France	1.8	3.5	1.4	3.6
Crude oil	USA			74.1	80.6
	Chile	-	-	6.6	5.5
	Puerto Rico			6.2	4.7
Bituminous coal	United Kingdom		-	4.3	17.8
	France		-	11.5	14.7
	Denmark	-	-	27.1	14.6
	Netherlands		-	5.8	13.4
	USA		10.6	10.2	6.2
	Puerto Rico		38.6	3.8	1.8
Precious stones	Japan	57.3	92.4	90.7	79.9
	USA	35.3	4.5	7.4	13.1
Raw sugar	USA	81.5	82.0	88.3	89.7
	Venezuela	-	12.5	-	7.5
	USSR	7.4	0.3	11.7	-

Source: INCOMEX data, based on Colombian National Administrative Statistics Department (DANE) Customs documents.

26. Moreover, export-oriented commodity diversification has had important linkage effects. The infrastructure created for diversification activities can also be used for other activities - the improvement of airport facilities to facilitate flower exports, for instance, has also helped exports of fruit. Backward linkages are strong - to take again the case of the flower industry, the demand for inputs has resulted in the establishment of companies for the supply of plastics, cardboard, fertilizers and refrigeration equipment, and in the creation of art and graphics firms, and has furthermore stimulated the development of transport companies and freight forwarders. Diversification also has learning effects, creating both the managerial and marketing skills necessary to enter into yet other activities (see Box I).

BOX I

THE LEARNING EFFECTS OF EXPORT EXPERIENCE

The skills necessary for exporting have to be learned. And there is no method as effective as actually trying to export. Once an exporter has learned, for a certain product, how to organize his contacts with a foreign market, he is often able to use this experience for the export of other, new products.

Several experiences in Colombia show how exporters are able to build on their existing production and export know-how to enter into new fields. Private banana exporters, organized in companies such as BANACOL, PROBAN and Turbana, have developed an extensive knowledge of fruit markets, and have used this to develop important exports of fresh fruits such as mangoes, melons and strawberries; in the Magdalena region, the main banana producing zone, these fruit now occupy 4,000 ha, compared to 12,000 ha for bananas. Flower exporters as well are diversifying into fruit, using, like banana exporters, their knowledge of export logistics and of how to find importers to develop new markets for products that they can grow under glass, such as artichokes, strawberries and asparagus.

The coffee sector, which has also tried to build on its exports to develop new activities, has had more problems. Not only is the fruit market completely different from that of coffee but it suffers from a lack of infrastructure such as cold storage or means of transport; banana and flower exporters could profit from the facilities already created for traditional exports. In several cases, such as the promotion of silk production and exports, exporters had to rely on

27. Commodity export diversification has not occurred at the cost of selling the country's national resources to foreign transnationals; most of Colombia's industry and agriculture remains in domestic hands. In primary production, the only substantial foreign involvement is in the crude oil and coal sectors, with a large number of transnationals (the largest being Shell, Occidental Oil and British Petroleum) active in crude oil exploration and exploitation, and Exxon, via its subsidiary Intercor, active in coal exploration and exports. However, in most cases foreign interests in these sectors are in the form of joint ventures with Colombian state companies. Outside the fuels sector, foreign participation in the primary sector is rare - the only two major cases seem to be in the flower sector, where an Argentine firm owns Floramerica, Colombia's largest flower producer and exporter, and in the production of raw silk, where Republic of Korea firms are heavily involved. Even the marketing of primary commodities is to a large extent in Colombian hands (see section B.).

28. In commodity processing and the marketing of these processed products foreign involvement is stronger. The production and marketing of ferronickel, instant coffee, and canned pineapples are all partly controlled by foreign companies (see chapter IV, sections B and C).

D. Bottlenecks for commodity export

diversification

29. Colombia's bottlenecks for commodity export diversification stem partly from the limits imposed by its scarce financial resources and partly from economic policy decisions taken in the 1970s. Natural resource availability is not a real bottleneck: the country's mineral and agricultural resource base is vast, and the climate is sufficiently varied enough from one region to another to allow a wide gamut of products to be grown.[6]

30. However, scarce financial resources limit the extent to which production possibilities can be identified and exploited. The government services responsible for land evaluation, crop research and mineral prospecting have always suffered from a lack of means. In agriculture, land is poorly developed outside the coffee zone, and even if a production possibility is identified, a follow-up mechanism to realize it is lacking. In the coffee zone, land evaluation is well developed, thanks to funding by the Diversification Fund (see chapter III, section B.1). The Fund also finances pilot projects in its zone of operation[7]; elsewhere in Colombia, only the former government export promotion agency, Proexpo, which had very limited means, was able to finance pilot projects. Part of Proexpo's mandate was to identify and elaborate export possibilities even when domestic production was not well developed or nonexistent, and was prepared to support such a new sector until it had grown up or was shown to be a failure. This potential for a long-term commitment has been realized fairly successfully in a number of cases.

31. In the minerals sector, a lack of funds for prospecting is a major problem, given the size of the country and the difficulty of the terrain. Nevertheless, the responsible agency, Ingeominas, has produced a sizeable number of regional maps of mining potential (often as subcontracting agency for private investors), and undertakes physical and hydrological prefeasibility studies when certain mineral resources are deemed potentially attractive.

32. Technological levels in most sectors of the economy are still quite low. Although importance of technology for the international competitiveness of a country has increased, and an active government policy to stimulate research and development and to facilitate access to foreign technologies is necessary, resources to pursue such a policy are scarce.

33. Colombia's capital market is underdeveloped. Finance for both investment and working capital can be difficult to obtain and expensive. For many projects, the domestic financial market is simply too small, and access to foreign capital is necessary. For working capital credits, the inflow of capital from abroad hinders access to credit for domestic entrepreneurs, as the government tries to limit the growth of the domestic money supply by credit rationing (which hits hardest companies that cannot give guarantees -

---

6 See, for minerals, H.R. Ensminger, "The mineral industry of Colombia", US Bureau of Mines, *Minerals Yearbook, 1987*.

7 See, for instance, "Colombia se alista para entrar al mapamundi de la fruticultura", (Colombia gets ready to join the world's fruit growers), *Nueva Frontera*, January 1990.

mainly smaller enterprises in new sectors) and by keeping interest rates high.

34. Added to this is the general problem of setting up new export activities; this requires initial investments in several activities, all of which are very expensive. "Piggy-backing" on activities already undertaken by others is difficult when one is the first to enter a certain market, and for private entrepreneurs the costs of market identification, developing or adapting technology, and training personnel can be prohibitive.

35. The problems for the export sector have been compounded by the inward-looking economic policy that was adopted in the early 1970s. One result of this is that Colombia's infrastructure and location of industry are still very internally oriented. Most industries are located near the main towns, inland and far from seaports. Road, railway and waterway infrastructure connecting the main towns with the ports is poor, and over the last two decades existing facilities were allowed to deteriorate. The regulations that were introduced to control air and rail traffic and the operation of the ports reflected this inward-looking orientation, and were thus not very supportive of the competitiveness of export transactions. There were some exceptions, e.g. the infrastructure for the flower industry (see Box II), but the role of the Government in these has been minimal.

BOX II

THE GENESIS OF THE TRANSPORT INFRASTRUCTURE NECESSARY FOR FLOWER EXPORTS

When flowers exports from Colombia started, exporters could only use passenger airplanes. But as the sector expanded, capacity problems quickly appeared. Flower exporters were, however, already well organized, and were able, through their association, to begin chartering aircraft. This resulted in a large reduction in transport costs, which made flower exports even more attractive. The supply of flowers thus increased, it became an interesting market for airline companies and some started to offer charter services. Competition among these companies for the lucrative flower market was strong, and they soon began to make efforts to attract flower exporters by better services; as, for instance, when, one by one, they built their own cold storage rooms at the airports. Transport infrastructure for flower exports is now very good, without any major investments by the government, and without the producers having been forced to pay for the whole infrastructure themselves. However, without the cooperation of the exporters in the initial phase the whole process of infrastructure improvements would never have taken place.

36. Another result of the inward-looking policy of the past is that Colombian entrepreneurs have not yet had the opportunity to build up the skills and the organizational structure necessary for exporting. For example, exports of many non-traditional products are still small, and Colombian entrepreneurs are not yet able to offer quantities that are interesting for international buyers (a problem which limits the development of an independent textile sector in particular).[8] Colombian entrepreneurs often lack the necessary international contacts;[9] have little knowledge of how to organize the logistics of exports; do not yet have the requisite bargaining power and skills to penetrate new markets effectively (countries like Japan

---

8 The Colombian Chamber of Commerce created an international trade company in 1991 to enable small companies to combine their export supplies in order to attain larger export volumes.

9 For example, palm oil producers, until recently, did not know how to set about finding clients abroad. They set up a joint marketing company in 1991 to overcome this problem.

require negotiation techniques that are quite different from those commonly used in the United States and Europe - Colombia's traditional main markets); and so far do not know how to convince foreign partners to transfer technology and skills, including marketing know-how. Support structures, such as specialized export houses or experienced export consultants, are rare, and this forces most companies to rely on themselves instead of being able to delegate export development to more experienced enterprises.

37. Many of these problems are being overcome. With the improvement of Colombia's political climate, and the perception abroad of this climate (which often hampered Colombia's exports in that Colombian exporters were seen as too vulnerable to terrorist attacks, which were apt to disturb the flow of goods and thus hinder the just-in-time production process of the importer), as well as the possibilities created by technological advances,[10] Colombia's export potential should increase.

E. Illicit drugs and export diversification

38. It has been often argued that for more than a decade, illicit drugs have been one of Colombia's major foreign exchange earners. Initially the drugs sector was based on cocaine, but lately it has started to diversify into the more capital-intensive production of heroine.

39. Most of the raw materials for these drugs - coca and papaver plants - are not grown in Colombia, but in neighbouring countries; most of the primary processing of coca leaves, to produce coca paste which is much less bulky and therefore easier to transport, also takes place in those countries.[11] Virtually all production is by small-scale farmers, each cultivating on average about two hectares; in Colombia, farm employment for some 61,000 people is created in this way. The coca plant is an ideal crop for these small farmers: the first harvest can take place six months after planting; four to six consecutive harvest are possible; and much family labour is required. The processing of coca leaves or paste, or in some cases only the logistics of commercialization, are arranged in Colombia.[12]

---

[10] A technological innovation that may have a large impact on Colombian flower and fruit exports to Europe is the recent introduction of so-called Freshtainers, containers which provide total control of temperature and humidity. Whereas before exports of this kind to Europe had to be sent by plane, these containers have made it possible to export by sea, at a lower cost, thus freeing scarce airfreight capacity (see "Colombian flower power booms", *Financial Times*, 19 September 1991).

[11] In 1992, in Colombia, coca was cultivated on around 25,000 hectares, compared to 200,000 ha in Peru, and 50,000 ha in Bolivia; another 15,000 ha was used for the cultivation of papaver, which is hardly grown in Peru and Bolivia. See F. Hurtado Pascual, 1992.

[12] It is reported that the domestic value added of cocaine only accounts for a minor part of its final sales price. The Colombian f.o.b. price for cocaine is normally within a price range of US$ 1,500 to US$ 2,000 per kg (of which farmers receive around 40 per cent), compared to the United States c.i.f. price of $14,000 to $18,000, and a retail value of $60,000 to $120,000. For a description of coca processing and value added in the industry, see F.E. Thoumi, 1992.

40. It appears that this has resulted in major foreign exchange inflows into the Colombian economy. It has been suggested that a part of drug earnings has been invested in land and property construction and part has been invested abroad. In 1987, an estimated 250,000 people, or 3 per cent of the workforce, were employed in drug-trade related activities;[13] up to 1.7 per cent of Colombia's domestic product could be directly based on the drug trade.[14] A recent report by the Universidad Nacional de Colombia claims that the drug trade allows Colombia to import and invest more than other Latin American countries,[15] although most of Colombia's exports of non-traditional products were initiated before drug exports became important.

41. At the same time, Colombia's regular exports were affected. The violence engendered by the battle for drug money has led to the death of a number of competent businessmen and politicians, and has created problems of image for the country in the eyes of some importers and potential foreign investors. Colombian exports are often exposed to more scrutiny, and therefore more delayed, than exports of other countries. Drug-related violence has caused the Government to devote a substantial level of resources to military purposes. The production and processing of drugs has resulted in deforestation and the pollution of many rivers, causing major environmental problems in some regions.[16]

42. Activities to promote crop substitution in coca and papaver growing zones face serious problems. Firstly, they are costly and difficult, because most of these zones are fairly inaccessible and often affected by guerrilla activity. If the farmers who produce drugs are driven out of these zones, they can easily move crop production to other mountainous regions that are difficult of access - a large part of Colombia's land surface falls in this category.[17] Therefore, force needs to be combined with more positive interventions (see Box III). Drug production will be difficult to stop as long as its economic rationale remains, that is as long as prices for illicit drugs in the developed countries maintain their present high level. Perhaps even more importantly, as is mentioned above, a major part of Colombia's illicit drug activities involve processing and

---

[13] "Colombia: resilient, but for how much longer", Latin American Economy & Business, January 1993. This should be compared to 600-700,000 jobs generated in Bolivia (with 6.5 million inhabitants), and 900,000 jobs in Peru (with 21 million inhabitants). According to Colombia's director of agrarian reform, drug syndicates have bought one third of the country's best agricultural land (Tom Quinn, "Colombia - still under siege", *Time*, 1 March 1993.

[14] According to the country's President, Cesar Gaviria (*Time*, 1 March 1993).

[15] This study was reported in *Time*, 1 March 1993.

[16] Thoumi, *op. cit.*.

[17] Colombia has some 7.5 million hectares of land situated at a height of between 2,000 and 3,000 metres, the ideal level for coca and papaver production; most of this land is difficult of access, and at present less than half a per cent is used for illicit drug cultivation. Coca processing as well can easily be moved from one region to another, as it is a relatively cheap, technically simple operation (see Thoumi *op. cit.*).

marketing foreign-grown raw materials.[18] Consequently, even if crop substitution activities in Colombia would reduce the amount of coca and papaver grown locally, additional efforts would be needed to put an end to marketing and distribution.

[18] The amount of money earned by Colombian drug gangs is estimated to have been US$ 4 to 4.7 billion a year in the beginning of the 1990s (Latin American Economy & Business, January 1993; Thoumi, *op. cit.*). A large part of the money is not repatriated to Colombia, but invested abroad. These drug earnings can be compared to the f.o.b. value of the exports of cocaine produced from Colombian-grown coca leaves, which is only about US$ 240 million (assuming an f.o.b. price of US$ 2,000/tonne).

BOX III

HOW TO PROMOTE CROP SUBSTITUTION IN THE ANDEAN REGION

As is well-known, the fight against drugs should be fought at different levels - primary production, processing, marketing, and final consumption. A research project recently undertaken by the International Trade Centre UNCTAD/GATT, for the United Nations Drug Control Programme, throws some light on how farmers could be stimulated to substitute coca leaves by other crops.

The project set out to identify potential agricultural crops, for both the domestic and the export market, which could replace coca leaf production in Bolivia, Colombia, Ecuador and Peru. It did this by taking into account the circumstances under which those producing coca leaves live, the prices they receive for coca, and the prices that they could receive for other possible crops with due regard to international market conditions and transport costs.

The project found that, in the current situation of very low international prices for most commodities, no single crop could effectively compete with coca. Coffee, the main crop grown in the same mountainous regions as coca, even engenders losses when labour time is fully taken into account. An intensification of production does not change this: for the major substitute crops, it would only increase real losses, while, for coca, intensification is a profit-making proposition.

Rather, the project proposes to build on the major disadvantage of coca production, namely its high labour intensity. It found that a well planned production mix would allow farming families to optimize the use of their labour time and thus increase their total income; this would provide sufficient incentive to stop producing coca. Such a production mix should include crops for self-consumption, for the domestic market and for export.

Coca is mainly cultivated in isolated regions, by farmers with little experience in producing for an exigent market. Therefore, a major effort is needed to make alternative crops marketable, by putting into place a good physical infrastructure and by setting up a proper organizational framework for farm exports. In Peru, for instance, it was found that small farmers, once organized and brought into contact with export companies, could readily access the export market.

The investments required to provide the necessary preconditions for successful crop substitution are high for the countries in question, but low compared to the costs of cocaine use to the economies where consumption is widespread. This is linked to the fact that farmers get only a minor part, 1-5 per cent, of the final price that consumers pay for their cocaine. The ITC UNCTAD/GATT project estimates that total costs to restrict coca production strictly in the four countries it covers would be US$ 10 billion, spread out over 10 years; such an investment would create legitimate exports of US$ 250 million a year.

Sources: F. Hurtado Pascual, International Trade Centre UNCTAD/GATT, 1992 and 1993.

Chapter II

ECONOMIC POLICY ENVIRONMENT

A. Introduction: economic orientations during the 1980s

43. During the 1970s, the economic model followed by Colombian policy makers was growth through import substitution, with heavy protection for domestic industries and little attention paid to exports. On the early 1980s, problems built up. The balance of payments became more and more negative, exhausting international reserves. The Government reacted by imposing quantitative restrictions on imports. Expansionary government policies had resulted in a large fiscal deficit, which, after 1982, was financed for the most part by printing money. This resulted in a fast growth of inflation and aggravated the overvaluation of the peso. The competitiveness of Colombian exports on the international market was considerably eroded. Economic growth fell to a historic low and savings and investment declined.

44. In 1984, Colombia implemented a major economic adjustment programme, for which it received substantial international support (in 1985, external credits provided 90 per cent of the financing needs of the public sector). The main elements in the programme were the reduction of the fiscal deficit, the devaluation of the peso and a reduction in import controls. Economic performance indeed started to improve during the second half of the 1980s.[19]

45. The 1985-1986 trade reform programme did not essentially alter the inward orientation of production incentives; rather, it terminated the protectionist policies of the early 1980s. Import liberalization mainly concerned non-competing inputs for locally manufactured goods. Only after 1986 did the Government really open up the economy. Since then, a series of measures have been taken in rapid succession with fast liberalization beginning in late 1990, and in 1991 a new economic programme was adopted, called the 'Apertura' ("opening" of the Colombian economy to world market competition). Among other things, import taxes are being rapidly reduced, import licences abolished and export subsidies eliminated, foreign investment is being made easier, and red tape has been reduced.

46. The 'Apertura' does not imply that the Government has ceased to support the private sector. However, the modalities are clearly different at present:

(a) Support will basically be at the first stage, instead of the end, of the production chain; it will chiefly concern manpower development (mainly at a very specialized level for which foreign support will be indispensable), and technology (improving the links between existing research institutes and private enterprises, and stimulating R and D activities of these enterprises themselves).

---

[19] See Jose Antonio Ocampo and Eduardo Lora, *Stabilization and adjustment policies and programmes; country study: Colombia* (WIDER, Helsinki, 1987).

(b) Government support for a particular enterprise/sector will be temporary (1 to 4 years), not for an indeterminate length. The Government will provide long-term capital only as minority participation in a project and for a clearly limited period.

(c) Government support will be automatic, following general rules, and no longer discretionary on the basis of case-to-case decisions by government officials.

(d) Actual government intervention in the production stage will consist mainly of promoting certain actions by enterprises, not of directly intervening to ensure that enterprises undertake these actions. For instance, the Government will stimulate the private sector to adhere to international quality norms and will try to make it clear to private enterprises that developed country markets have a preference for environmentally "clean" products.

47. Government policy is also formulated in such a way that distortions from the past are addressed: special incentives are created to promote a relocation of industries towards the seaports and to raise the technological level of small and medium-scale industries.

B. Infrastructure and transport policies

48. For much of the 1980s, infrastructure and transport policies tended to be dirigiste, but in 1990 they started changing along the same lines as macroeconomic policy, i.e. instead of direct government intervention the Government merely ensures that the necessary conditions exist for the development of the private sector.

49. These changes can be seen in both port and railway policy. The State railway company, Ferrocarril, has been broken up, with the Government remaining responsible for the maintenance of the railway lines, but the private sector assuming responsibility for the operation of the rolling stock. Similarly, the Government is privatizing the ports: for every port two companies are formed, with the Government maintaining control over the physical harbour facilities and the private sector responsible for loading and unloading operations.

50. Transport regulations are also being adapted. New port regulations make it possible for companies that own their own loading facilities also to handle third parties' loading, which will help exporters to cope with the often completely congested government-controlled loading facilities.[20] Labour regulations, which now add considerably to loading and unloading costs, are also being changed. The obligation on exporters from and importers to Colombia to use Colombian vessels for at least half of the quantity transported has been abolished; ships from countries that allow Colombia to compete are now free to compete for transport

---

[20] In the past, several companies, confronted with problems in government-controlled ports, invested in their own port infrastructure: Carbocol and Ecopetrol have their own ports, and a large number of other companies (such as Carbones de Caribes, the main private coal exporter, and enterprises exporting cement, petroleum, banana, sugar, steel products and petrochemical products) have their own loading facilities. Until recently, when these companies rented their loading facilities to others, they had to pay to the port authorities the equivalent of what the loading would have cost at the government-controlled loading facilities.

to and from Colombia. In road transport, some further regulatory changes may be necessary; for example, the potential of the Venezuelan market can still not be fully exploited because of regulations that require local means of transport to be used in both Colombia and Venezuela, that is, goods have to be loaded from one truck into another after passing the frontier.

51. In air transport as well there are important changes. Air transport used to be monopolized by some large Colombian companies, but in 1991 an "open sky" agreement was signed with Venezuela. This helps Colombian fruit and flower exporters considerably, as Venezuela has too heavy an import load and not enough volume for exports, the opposite problem to that of Colombia. To give an example: demand for air transport to the EC is about 1,000 tonnes a week, mainly flowers and fruit and some textiles. Availability is only 500-600 tonnes. With the additional offer of airfreight space from Venezuela, Colombian exporters will be able to take full advantage of the tariff concessions offered to their flower and fruit sectors by the EC.

C. Investment policy

52. In line with decisions taken in the Andean Group, Colombia has gradually liberalized its policy towards private investment since 1987. While, before 1987, foreign companies were required to become national or mixed enterprises, since that year most sectors of the economy (except those linked to national security) have been fully opened to foreign interests. The provisions of the new investment legislation allow, among other things, for 100 per cent foreign ownership, equal treatment for foreign and Colombian investors, and a profit remittance of up to 25 per cent (higher in the mining sector). This new attitude towards foreign investment is also reflected in the Government's investment promotion activities. For instance, in the case of identified mining possibilities, the Ministry of Mines offers the project to the private sector, both domestic and foreign. When Colombian enterprises are interested, they are allowed to try to identify foreign joint venture partners in order to gain access to capital or expertise.

53. As a result, foreign investment inflows peaked in 1988 and 1989, with major new investments in the coal mining sector in particular. The fuel sector and the manufacturing sector also profited considerably from this new investment policy. Investment in agriculture, on the other hand, is very limited, less than one per cent of total foreign investment.

54. Further liberalization followed. Up to 1991, contract negotiations with foreign investors were discretionary, and there were no general rules on the concessions (the level of allowable profit repatriation, etc.) that could be offered. Such general rules have now been drawn up as part of the Apertura, and became law in 1991. The new regulations are based on equal treatment of foreign and national enterprises, and also equal treatment across economic sectors, with the exceptions of coal and nickel mining and of fuel exploration, for which conditions are somewhat more favourable.[21]

---

[21] See "Régimen legal de la inversión extranjera en Colombia (Legal regime for foreign intestment in Colombia)", *Colombia Exporta*, June 1991.

D. Exchange rate policy

55. Since 1984, the nominal exchange rate of the Colombian peso is adjusted daily by the authorities, under a system linked to a basket of foreign currencies. Before this system was adopted, the adjustment of the peso was more haphazard. During the 1970s and part of the 1980s the Colombian peso was overvalued by 30 to 40 per cent, which made exports rather unattractive. This was the result of a high domestic inflation rate, but the difference between domestic and world market inflation was not compensated by a lower exchange rate for the peso.

56. By late 1984, however, the pace of the daily mini-devaluations started to accelerate at a rate greater than the domestic and foreign inflation differential, making exports much more attractive. From late 1984 to late 1986, the real exchange rate was devalued by 39 per cent. Since then, policy has been to maintain the real exchange rate at the level attained in late 1986 (as graph 3 shows, exports of non-traditional commodities began to grow from 1986 onwards). This is only one of the policy goals, though: other goals include maintaining Colombia's level of foreign exchange reserves and keeping Colombia's overall balance of payments stable. The latter goal resulted in a 4 per cent appreciation in 1990, which was reversed again in 1991 after pressure from exporters. Overall, the goal of retaining export competitiveness seems to play a major role in exchange rate policy.

E. Monetary policy

57. Since late 1986, monetary policy has been used mainly to control the balance of payments, or more specifically, to retain purchasing power parity with Colombia's main export clients. This has become more of a problem since 1991. In the past, exporters were obliged to remit the receipts of their exports within a certain time limit. Since 1991, however, exporters may keep accounts in foreign currencies, and convert these to pesos when they want. This implies that the Central Bank has less control on the timing of currency conversions and thus has more problems to keep domestic inflation in check. Additionally, direct measures to control the balance of payments such as export subsidies or import taxes are being abolished. Credit policy is one of the direct policies left: in times of high foreign exchange inflows (the present situation in the Colombian economy), the Central Bank can give, for instance, cheap credits to enterprises that want to import capital goods, thus upgrading the technological level of the company, and reducing the amount of domestic currency in the economy. The other main instrument of monetary policy is intervention on the foreign exchange markets: massive purchases or sales are made to reach the desired exchange rate.

58. This use of monetary policy to control the balance of payments can prejudice exports. As mentioned, the main issue in Colombia's balance-of-payments account is the large inflow of foreign exchange, which puts pressure on the peso. However, a revaluation would make exports less competitive. To absorb the extra money supply, the Central Bank needs to follow a deflationary policy, which means that short-term credits can at times be very difficult to obtain, and companies get into liquidity problems. Exporters normally only receive the receipts of their sales after a fairly long time; nevertheless, they need money to bridge the waiting period so this block on short-term finance has hit them hard. In 1991, the decision was taken that exporters would only be able to obtain short-term loans by selling their "long-term" titles to the Central Bank at a considerable discount. This amounts to an implicit devaluation for companies

with a low level of liquidity, in all likelihood smaller companies active in the export of non-traditional commodities.

F. Policies for improving market access

59. Colombia, like the great majority of developing countries, is confronted with market access problems for most of its export products, including primary commodities. Import barriers are still in force in the largest industrial countries for coffee, tobacco and bananas. For flowers, Colombian exporters are regularly confronted with anti-dumping duties in their main market, the United States of America. Phytosanitary restrictions limit the export potential of products such as pineapples. In addition, for several of its export products (such as meat and sugar) Colombia is affected by the subsidies given in major industrial country exporters. Non-traditional exports such as textiles, clothing, footwear and leather articles are subject to high tariff and non-tariff barriers.[22] Nevertheless, exporters do not consider these to be the main barrier to an expansion of exports (domestic factors are thought to be more important), and in recent years market access has improved in several respects.

60. Since the late 1960s, Colombia has had preferential agreements with a number of other countries in Latin America. Despite this, until the mid-1980s, Colombia's trade with these countries did not expand faster than its total merchandise trade. However, the process of regional economic integration has accelerated considerably in the past few years and is likely to provide new opportunities. Within the framework of the Latin American Integration Association, Colombia has signed several bilateral cooperation agreements and others are being negotiated. These bilateral agreements include preference margins for tariffs as well as total elimination of levies for some products. In the Andean Pact (with Bolivia, Ecuador, Peru and Venezuela), which has been in force since 1969, good progress was made towards liberalization in 1989. Negotiations in the Andean Pact resulted in 1990 in the decision to set up a customs union among the largest members by 1993, and a complete customs union by 1995.[23] In the Group of Three, with Mexico and Venezuela, Colombia has drawn up liberalization schemes embodying large tariff reductions for a long lists of products.[24] In February 1993, a free trade agreement was signed with Venezuela and a number of Central American states.

61. The impact of such regional integration efforts can be considerable, as is shown by the experience of Colombian sugar exports. Colombia is traditionally a raw sugar exporter to the world market. When tariff barriers within the Andean Pact were reduced and then abolished, a large market for white sugar was opened up. Exports of white sugar almost tripled from 1989/90 to 1990/91, and then tripled again the year after, while raw sugar exports to the world market virtually disappeared. As the main market access

---

22 GATT, *op.cit.*, pp. 41 and 183-184.

23 Ministry of Economic Development, *Reglas de juego para la Apertura* (Rules of the game for the Opening), Bogota, 1991, p. 23.

24 The Group of Three is set to become the Group of Four with the inclusion of Ecuador. It is intended to liberalize most trade between these four countries by 1994.

obstacles that remain in force concern agricultural products (except sugar, where there is little competition between the countries), regional integration schemes should especially benefit the manufacturing sector (including commodity processing), and to some extent the fuels sector.

62. Market access is improving at an international level as well. For instance, in 1990, the EEC decided to give tariff concessions to Colombian exports for four years as part of a programme to combat the export of illegal drugs. The United States of America has a similar programme: in November 1989 the Government announced the Andean Initiative, which consisted of a number of unilateral concessions for a period of 10 years to support the economies of Colombia, Peru and Bolivia. It would cover less than half of Colombia's exports, while most Colombian exports are still threatened by the probable loss of their Generalized System of Preferences status in 1993. Of interest for the longer term is the Enterprise for the Americas Initiative, launched by the United States of America in 1990, with the aim of creating a free trade zone in the medium term. The process envisaged is one of a series of bilateral negotiations between the United States of America and firstly Mexico, then Chile; Colombia is not a priority in this respect for the United States Government.

G. The implications of the Colombian economic policy environment for commodity export diversification

63. During the 1970s and the first half of the 1980s, the Colombian economic policy environment tended to discourage commodity export diversification, owing to the high rate of inflation, the overvalued exchange rate, regulations that hindered efficient exports, and the lack of appropriate policies in the area of infrastructure and transport. On the other hand, import substitution was encouraged. The export diversification that took place was mainly possible because specific sectors were shielded by the Government from this generally discouraging macro-environment, as will be discussed particularly in chapter III. However, as the tables in chapter I indicate, the success of export diversification during this period was rather limited.

64. Since the policy changes of 1984-1986, Colombia's economic policy environment has been rather favourable for exports, and commodity export diversification has taken place at a much faster pace. The continuing dialogue between the Government and the well-organized private sector ensures that the macroeconomic decisions taken are, as far as possible, in keeping with the interests of the export sector. Colombia's Association of Exporters and its Chamber of Commerce are consulted on all major economic policy decisions, and, at the sectoral level, the associations of sugar, cocoa and coffee exporters have a considerable influence, extending so far that the Government appoints the leaders of these associations as its representatives in international commodity negotiations.

65. Naturally, exporters have some problems with particular aspects of general economic policy. To the extent that policy changes result in improved opportunities in the short run, the private sector is not well prepared to profit from these; for 30 years, the Colombian market was protected, and now has difficulty

in adapting.[25] Their short-term problems are therefore likely to weigh more heavily. Exporters object in particular to the credit squeeze and difficulties experienced in exchanging dollars into pesos, which are a result of monetary policy (necessarily so because of the inflow of foreign exchange - largely related to drug exports), and the sometimes rapid abolition of subsidies. These elements of economic policy are likely to have negative consequences, especially for smaller companies which are less able to adapt to changing conditions than larger ones, partly because they lack financial reserves of their own.

66. At the sectoral level, exports of non-traditional products seem to have benefited most from the policy changes of the mid-1980s. In the past, only a few large sectors managed to overcome the barriers imposed by macroeconomic policy. Infrastructure was well developed only for the coffee, fuel and banana sectors, and for the two largest coal export companies. However, recent changes in infrastructure and transport policies have facilitated exports of, among other things sugar, flowers, fruit, clothing and leather goods.[26] Improvements in regional market access are of particular interest for exporters of manufactures, coal and some food products such as sugar.[27] Steps taken to improve access to the markets of the EC and United States, on the other hand, have mainly benefited the flower and fruit exporters, and the exporters of products such as clothing and leather. The liberalization of investment policies has been of most benefit to the fuel, mining and manufacturing sectors. It has ensured that Colombia will remain a large fuel exporter until well into the next century, and that coal exports will continue to expand. Foreign investment in the manufacturing sector should also help Colombia to reach the technological levels required to participate in international trade in these goods.

---

[25] One expression of this is that Colombian entrepreneurs make less than full use of the tariff concessions given by the EC and United States as well as those arising from regional economic free trade programmes.

[26] An improvement of the railway infrastructure benefits the export of bulk goods, specifically, sugar, coal, cement, coffee and paper. Better functioning of the ports also mainly stimulates the export of bulk goods, although when containers become easier to use through the improvement of port operations, other export commodities will also profit. The "open-sky" arrangement is mainly of importance for exporters of high value products like fruits, vegetables, clothing and leather goods.

[27] For example, the association of sugar exporters signed a contract with Venezuelan refiners in 1991, whereby Colombia supplies the raw sugar, and both countries (in a fifty-fifty joint venture) sell this and refined sugar in the frontier area; similar deals are being negotiated with Peruvian and Mexican refiners.

Chapter III

GOVERNMENT POLICIES FOR HORIZONTAL DIVERSIFICATION, AND HORIZONTAL DIVERSIFICATION EXPERIENCE

A. Policy formulation

67. Diversification, as a long-term objective, has been part of the economic programmes of all the Governments in power since the 1940s. The goal has always been very general - to move away from overdependence on coffee, and the question of which specific sectors should be supported has been left more to tactical decisions than to strategic guidelines. Specific policies have been formulated to support diversification - these have been more or less effective, depending not only on the policies themselves but also on the macroeconomic environment in which they were being applied. The specific policies for horizontal commodity diversification, and the concomitant development of non-traditional commodity sectors, will be discussed in this chapter. Vertical diversification, and policies specific to this, are discussed in chapter IV.

B. Policy experience

68. The diversification-specific policy measures discussed in this section include the earmarking of finance; the creation of specific support structures; the adaptation of general regulation and pricing policy to stimulate diversification; the provision of financial incentives; and the provision of credit on favourable terms.

1. The earmarking of funds for diversification: the Diversification Fund of the coffee sector

69. Colombia has considerable experience in the use of earmarked diversification funds. The main primary commodity industries are taxed, directly or indirectly, to finance diversification. This is the case for the coffee sector, the fuel sector, and the coal sector.

70. To support the agro-industrial and manufacturing sectors, including companies envisaging export-oriented commodity processing, there are two special funding agencies. The largest is the Industrial Promotion Institute (Instituto de Fomento Industrial, IFI). In the area of primary commodities, IFI has invested in coal exploration, gold mining, and fisheries (shrimp and fish).[28] The second organization is the Export Development Fund (Fondo de Promoción de Exportaciones), which has invested in coal (it has a 38 per cent share in Carbocol, Colombia's largest coal exporter), and the international banana trade

---

[28] *Reglas de Juego para la Apertura, op. cit.*, annexes 1A, 1B.

(through its participation in Comunbana).[29]

71. The Colombian coffee sector was organized at an early stage: its association, Federacafe, was created in 1927. It was soon confronted with the need to make arrangements to avoid an oversupply of coffee: during the early 1940s, it was cut off from the European market and it was necessary to install an export quota. A National Coffee Fund was created to finance this policy. Diversification out of coffee became an explicit goal in 1943, when Federacafe decided it was necessary to promote exports other than coffee. In 1960, Federacafe's first five-year Diversification Programme was drawn up. To finance this programme, the Fund for Development and Diversification was created in 1963. It was financed by taxes on coffee exports, other contributions from coffee producers, direct support from the Government, and large loans from the World Bank and other donors.

72. The goals of this programme were to identify viable alternatives to coffee, to determine ways to reduce the risks of farmers entirely dependent on coffee, and to find crops that would make use of the available labour supply outside the peak times of the coffee season. These same goals remained in the later programmes; at present, the sixth- five year Diversification Programme, 1991-1995, is under way. In these Programmes, the economic possibilities of different coffee zones were identified as a function of soil characteristics, climate, distance from urban markets and ports, and human resource availabilities. The promotion of new products then took place through research and development, extension work, special credit programmes,[30] subsidized input supply, and the creation of price information networks for fruit, vegetables and roots and tubers (including price forecasts for the season to come, to allow farmers to make better investment decisions), and, after the initial phase, the creation of commercialization networks as well. Large investments were also made in the improvement of infrastructure.

73. Products such as sugar, cocoa, cereals, livestock, poultry, fish, wood, rubber, honey, bananas, other fruit vegetables and ornamental plants have been promoted. Through the Diversification Fund the development of over 15,000 ha of high-yielding cocoa plantations has been financed - 15 per cent of the total surface under cocoa in Colombia. More than a 100 agro-industrial enterprises received financial support (up to three quarters of total investments). These included companies that process fruit, vegetables, milk, leather, sugar, wood and silk. In the case of the sugar sector, for instance, support from the Diversification Fund included soil studies, ground levelling, technical assistance to sugar cane growers, co-financing of several sugar factories (among others, Colombia's fourth largest sugar factory), and the co-financing of several factories for the production of confectionery. The promotion activities in the fruit sector are described in Box IV. A large number of cooperatives were set up, as well as an export company. As can be seen from Box V, the Diversification Fund was also used to finance part of the costs of market

---

[29] *Ibid*, annex 2.

[30] Credit conditions are very favourable compared to those in many other countries. For instance, for farmers wishing to enter into a new activity, up to 90 per cent of total costs (including working capital) can be financed at a strongly subsidized rate, and with a relatively long pay-back period (seven years, after a two-year grace period). See "El crédito para diversificación" (Credit for diversification), *Nueva Frontera*, January 1990.

BOX IV

THE PROMOTION OF FRUIT EXPORTS BY THE ASSOCIATION OF COFFEE EXPORTERS

In the fifth Diversification Programme, 1984-1989, fruits was identified as a major area for future export-oriented growth. After intensive market studies, a number of kinds of fruit, both those known on western markets (such as oranges, pineapples and mangoes) and those hardly known (such as pitaya and passionfruit) were chosen for active promotion.

Over one quarter of the total resources of the Diversification Fund for this period was used to finance the development of some 15,000 ha of new fruit production. An effort was made to place Colombia firmly on the market, with exports through Comercafé (International Marketing Company for the Export of Coffee Products), a company created by Federacafé.

In the late 1980s, several projects for the processing of fruit were also partly financed by the Diversification Fund: a company to produce passionfruit juice, a hitherto unknown export for Colombia, with exports now valuing over US$ 10 million a year; and a company to

BOX V

WHO PAYS THE BILL FOR PENETRATING A NEW MARKET ?

The difficulties faced in penetrating a new market are often underestimated. Having small exports is often not a problem; but once one acquires a larger market share, competitors, including competing producers in the importing country, start to react. A typical reaction of United States producers on competition with foreign suppliers is recourse to the law: anti-dumping and compensatory rights suits to ensure that the foreign supplier gets hit with an additional tax and thus becomes less competitive.

These kinds of lawsuits have been a major problem for Colombian flower exporters who depend strongly on the United States market. Without government support they would in all likelihood not have been able to overcome the legal pressure from United States producers.

To counteract protectionist tendencies, the Colombian association of flower exporters, Asocolflores, retains a permanent lobbying representative in Washington, who also represents exporters in lawsuits. Between 1982 and 1991, there have been 17 anti-dumping and compensatory rights suits against Colombian exporters, which have cost, in lawyers' fees alone, US$ 3.5 million. The cost of representation in Washington is paid for by the producers themselves, but the legal costs have until 1992 been paid out of the Diversification Fund. In this way, Colombian flower exporters avoided anti-dumping margins until 1986; and when in 1986 such a margin was put in place, the lobbying activities of Asocolflores resulted in a change of the methodology used in

penetration by flower exports. Most of these diversification activities took place during the second half of the 1980s.

74. The present five-year Diversification Programme has three main elements:[31]

- The further promotion of non-traditional crops, and of livestock and poultry holdings; 90 per cent of total investment under the Diversification Programme is destined for these activities;
- Commercialization activities: these have been given a relatively large place in this Five-Year Plan. In November 1990, Federacafe created for this purpose the Fund for Investment and Commercialization, to participate in commercialization activities undertaken by groups of producers in the coffee zones, to undertake research into packaging and handling techniques necessary for exports, and to help producers in identifying foreign clients;
- Agro-industry, oriented towards the production of fruit pulp and juices, meat, milk and wood

[31] Federacafe, VI Plan Quinquenal de Diversificación Cafetera (Sixth Five-Year Coffee Diversification Plan), internal note, 3 July 1991.

products; over 60 enterprises are to be set up.

The budget for this five-year plan is around US$ 400 million.

75. It has become more urgent to undertake this programme in the present situation of oversupply and low prices in the world coffee market. In 1992, a plan was adopted to take 30,000 ha out of coffee production during 1993, and 100,000 ha within the next few years - this represents about 10 per cent of land now under coffee. Regional coffee committees have undertaken not to promote new sowings of coffee or the modernization of plantations. In these conditions, diversification becomes the only way for coffee farmers to improve their living conditions.

2. Support structures

76. The private sector, to be able to diversify, needs access to certain services such as the following: services to alert entrepreneurs to market possibilities, product adaptation support, insurance, banking, repairs, consultancies, market information networks and market promotion. These services can be supplied in part by the private sector, but it often sees no interest in doing so - as is especially the case in countries with an economy that is a not yet fully developed. The Government will then have to provide them.

77. In a number of respects the Colombian private sector is sufficiently developed to provide itself with a number of support services, such as repairs, telecommunications and, to a certain extent, R and D (although they have concentrated on product development rather than pure research). In most other areas, however, the role of the Government has been very important. In Colombia, the main government organization providing support to export-oriented activities was, until late 1991, the Fondo de Promoción de Exportaciones de Colombia (Proexpo). Most of the support services provided by Proexpo were absorbed by a new Ministry of Foreign Trade on 1 January 1992, while Proexpo's role in providing export credits has been taken over by a new Bank for Foreign Trade (Bancoldex).[32]

78. Proexpo had an active role. It did not wait for requests for support from the private sector, but anticipated that sector's needs, and played an important role in making it aware of export possibilities. It operated export promotion offices in over a dozen countries. Proexpo's total budget in 1991 was over half a billion dollars financed from import taxes and loans from the World Bank and other international organizations.[33] Most of these funds were used for Proexpo's credit programme (see section 5).

79. Government policy, as regards support structures, has been most highly developed in the area of <u>export market promotion</u>. This was, for a long time, one of Proexpo's principal activities. Among its activities were:[34]

- direct support to exporters, through subsidizing the participation of private enterprises in trade fairs

---

32 The exact distribution of labour is not clear. Bancoldex' mandate covers commercial promotion of exports: including provision of information services and establishment of contacts between exporters and potential buyers. In order to do this, Bancoldex maintains the foreign trade bureaus which Proexpo used to manage.

33 *Reglas de Juego para la Apertura*, *op. cit.*, pp. 14-15.

34 See Proexpo, "Servicios de promoción externa de PROEXPO", Bogota, 1990.

abroad, financing foreign sales missions of Colombian entrepreneurs, and arranging visits of potential foreign buyers to Colombia;

- provision of market information: gathering information on products and distributing this information among potential suppliers in Colombia; identifying possible markets for products offered by Colombian enterprises; and doing general market studies on non-traditional markets;
- support to generic promotion campaigns, e.g. for Colombian fruit.[35]

80. In the case of export insurance, the Government's possibilities were limited. Proexpo was able to give export insurance, contracting it out with a private company, but its exposure ceilings did not permit it to do this on a large scale. The Bank for Foreign Trade is to strengthen activities in this area: part of its mandate is "to establish or become a partner of institutions offering export credit insurance or hire them to provide such services; or to finance such institutions or those they serve."[36]

81. The functioning of services to identify diversification opportunities was discussed in chapter I, section D. In general, the private sector is informed of various production potentials, be they in the agricultural or the mining sector.

82. The main government organization active in the area of product adaptation was again Proexpo, supporting export-oriented companies that had problems in their production, quality control procedures or packaging. In this respect, Proexpo could organize study missions abroad for local producers, recruit foreign specialists to advise domestic producers, import improved seed varieties, and do studies on improved cultivation techniques. Sectors in which Proexpo has been active include cotton, where it started a number of pilot projects to counteract the effects of 30 years of technological stagnation; shrimp farming, where it financed the acquiring of the expertise to make this activity successful; the promotion of Colombian flowers on the Japanese market by identifying the new harvesting and treatment techniques that would be necessary to meet Japanese market exigencies and bringing in Japanese experts to teach these to Colombian producers; fruit and vegetables, in which Proexpo, together with the Ministry of Agriculture, is cooperating with the United States Department of Agriculture to overcome problems in the area of physosanitary requirements.

83. Support activities in the area of market information include seminars to make entrepreneurs aware of the possibilities of the world market (which is necessary, as years of internally oriented growth have created an attitude among private enterprises that is not very dynamic) and the creation of market information networks. Most of these activities are the work of the Chamber of Commerce and Proexpo (now the Bank and the Ministry of Foreign Trade), although, as mentioned above, Federacafe has also financed the creation of a market information network for fruit. The Chamber of Commerce in particular

[35] Generic promotion campaigns for flowers seem to be mainly financed by the private sector; e.g., in 1992, the Colombian Flower Council supported the promotion activities of the American Floral Marketing Council with a gift of US$ 300,000.

[36] Carlos Caballero Argáez, "From PROEXPO to the Bank of Foreign Trade", *Colombia Exporta*, December 1991.

has made a major effort to ensure that enterprises become more export-oriented. It organizes seminars on, among other topics, how to profit from international market possibilities and how to adapt to the requirements of international trade. It operates a market information network, in cooperation with the Chambers of Commerce of other countries and it has set up a export marketing company to facilitate the exports of small and medium-sized companies.[37]

84. Quality control is not the responsibility of a government department, unlike the situation in some other countries. The supreme body for trade policy, the Foreign Trade Council, has a mandate to establish standards concerning quality, packaging, marking and other requirements aimed at ensuring the best conditions for the marketing of Colombian products abroad,[38] but it has chosen to limit its role to the distribution of information on international norms to Colombian companies, and when there are problems, to help them to overcome these. Although exports are prejudiced by frequent problems with the quality supplied, especially by smaller enterprises (which damages Colombia's image abroad), no sanctions are taken against companies that ignore international quality standards.

3. Pricing policy

85. Pricing policy has not been particularly important for Colombia's diversification. Price controls did exist; prices for main consumer goods such as cereals and sugar were kept low, and a number of domestic industries were protected against foreign competition by keeping domestic prices high. Diversification has only been a goal in one case. From the late 1970s on, the Government, by adjusting consumer prices, shifted domestic demand away from exportable products like fuel oil and kerosene towards more abundant sources of energy, such as natural gas, hydroelectric power, and coal.[39]

4. Financial incentives

86. Financial incentives have been an important tool for the promotion of commodity export diversification. During the 1980s, the most important means were a scheme for reimbursement of indirect taxes (Certificados de Reembolso Tributario - CERT),[40] and the Plan Vallejo, a programme to provide

---

[37] Chamber of Commerce of Bogota, *Servicios de Promoción Commercial y Posibilidades de Cooperación* (Trade Promotion Services and Possibilities of Cooperation), Bogota, October 1991.

[38] GATT, *Trade policy review - Colombia 1990*, Geneva, 1990, p. 16.

[39] (Ministry of Mines and Energy), *Memoria al Congreso Nacional, Anexo histórico* (Report to the National Congress, Annex on past developments), Bogota, 1990, p. 156.

[40] Other financial incentives, such as direct export subsidies, foreign exchange retention schemes (which allow exporters to retain part of their foreign exchange earnings) or parallel exchange rates, have been of no relevance in Colombia since 1980. Differential exchange rates, used to tax the coffee sector, were in existence until 1967, and a similar system, using exchange certificates but again taxing the coffee sector, was used between 1977 and 1980. Non-traditional exports received preferential exchange rates during much of the 1960 and 1970s.

exporters with access to duty-free imported inputs. In effect, these incentives, together with subsidized credits, were seen as a way to compensate the export sector for disadvantages resulting from the import-substitution oriented character of macro-policies. As President Gaviria of Colombia stated in late 1990: "This mechanism did not result in an export model, but rather in an exporting enclave inserted in a generally hostile environment, and surviving on the basis of transfers and preferential treatment."[41]

87. The tax reimbursement certificate (CERT) is used to compensate exporters of all products other than coffee, cocoa, raw cattle hides, ferronickel or petroleum and petroleum products for indirect taxes paid. This certificate can be used to pay national taxes of any kind. The CERT programme replaced in 1983 a similar scheme introduced in the 1960s. CERT is paid on the f.o.b. value of exports for exporters not receiving duty-free imports under the Plan Vallejo; those receiving duty-free imports only obtained a CERT for their domestic value added.

88. CERT rates are established by product and are not directly related to indirect taxes paid. Initially, manufactured exports were favoured, but since a general scaling back of the programme took place in the early 1990s several non-traditional exports fall under relatively high CERT rates. After this scaling back, the CERT has been retained, at a lower level, solely for most non-traditional products, and for some traditional products when exported to non-traditional markets (for instance, drawbacks for sugar and bananas have only been abolished for exports to the United States). This financial incentive for exports to new markets is general: exports to Asian countries get a CERT 50 per cent higher than the normal one for the relevant commodity, while exports to most Latin American countries are entitled to one that is 30 per cent higher. In general, CERT rates are higher for the more processed forms of a commodity.[42]

89. Since the mid-1950s, the import content of certain exports, mainly manufactured goods, has been exempted from import duties. This was systematized under the Plan Vallejo, introduced in 1959. During the 1980s most exports other than coffee, raw cattle hides, gold, gemstones, crude oil and fuel products were eligible for import duty drawbacks. In addition, exporters who were approved by INCOMEX were freed from a range of other obligations, such as some bureaucratic procedures, licences, and customs or consular fees. Some non-traditional sectors did not receive any duty drawbacks, for various reasons. For example, the flower sector voluntarily gave up export subsidies, subsidized credits and duty drawbacks in the early 1980s as a result of pressure from the United States of America.[43]

90. Import duty drawback levels were abolished in 1991. One way in which this has been

---

[41] Quoted in Carlos Caballero Argáez, "Economic opening and export policy", *Colombia Exporta*, March 1991.

[42] See Proexpo, "CERT", *Boletín del Exportador*, No. 33-34, 1991.

[43] In theory, enterprises only needed to give up these advantages for the part of their production that they exported to the United States. In practice, however, regulations made in that country make it impossible for companies to receive any financial support if they do not want their exports to the United States to be hit with extra taxes.

compensated is a streamlining of procedures for export-linked imports. Since 1987, import licences for capital goods and spare parts have been granted almost automatically. This is partly the result of United States pressure, partly a logical element in Colombia's new macroeconomic policy (see chapter II, section A).

5. Credit policies

91. When credit is scarce, the existence of special credit lines to promote non-traditional sectors can have a strong influence on diversification, and, indeed, access to credit - a general problem in Colombia. For instance, sugar producers complain that limited access to credit has resulted in lower automatization of the sugar industries, outdated technologies, and lack of means to invest in, for instance, water treatment plants.

92. Real interest rates in Colombia are higher than in surrounding countries, and obtaining loans can be difficult. To combat the problem of high interest rates, credits for selected, non-traditional activities used to be subsidized, with a larger subsidy for small firms and pilot projects than for large firms. This practice was discontinued in 1990. As a way to reduce the problems of access to credit, several special credit lines have been set up and are still operational.[44] The main ones are:

- investment credits, to finance investments in the production, quality control, preservation and marketing of exportable goods. The credit amount is fixed in accordance with the share of exports in total sales of the project, and can reach 90 per cent of total investment costs if the share of exports is over 50 per cent;
- credit term is five years; and
- working capital credits of two kinds:
    * pre-shipment credit to finance the working capital of firms producing or marketing export goods. Credit terms vary between six months and a year;
    * post-shipment credit to finance the credit granted by the exporter to his foreign buyers. This credit can cover up to 100 per cent of the credit granted by exporters. It has a term of one year for consumer goods and five years for capital goods.

93. Additionally, there were credit lines aimed at quality management; design, packaging and training programmes; export promotion such as pre-investment studies, market studies and advertisement; etc..

94. These credit lines were administered by Proexpo until 1991, and since then by the new Bank of Foreign Trade "Banco Colombiano de Comercio Exterior" (Bancoldex). There are credit lines for most export sectors, with the exception of coffee beans, coffee products, unprocessed leather, gold, gemstones, crude oil and oil products.[45] Conditions to be met for obtaining these credits are rather severe. For every peso lent, the equivalent of several pesos have to be returned to the country within a limited period of

---

[44] GATT. *op.cit.*, pp. 144-145.

[45] See Proexpo, (Preshipment credit line - regulations), Circular P-SDC-002, 19 April 1991.

time.[46] In addition, lending charges for loans denominated in pesos are very high (in late 1992 they stood at some 42 per cent on an annualized basis); for this reason, large companies with access to the international banking system (and thus lending in other currencies) are far more privileged than to smaller ones.

C. Diversification experience - major developments

95. Colombia has added a considerable number of new primary commodities to its exports, and expanded the exports of formerly minor ones. Among the commodities that have thus increased in importance during the 1980s are crude oil; coal; platinum; flowers; shrimps (see Box VI)[47]; lobsters; tuna; and a variety of fruits and vegetables.

BOX VI

SHRIMP FARMING

Shrimp farming is a fast growing export sector. For years exports of shrimp caught at sea have been a significant source of foreign exchange, but possibilities for expansion in this area are limited. Compared to this, the potential for shrimp farming is large.

A number of isolated shrimp farming attempts were undertaken in the 1970s, with little success. After the government's export promotion fund, Proexpo, began to support this activity things changed. Proexpo promoted and financed the building of more than 90 per cent of the country's shrimp farms and hatcheries, organized study trips for Colombian businessmen and experts, and financed the acquisition of foreign expertise and technologies. The Government continues to back this sector in the adaptation of up-to-date processing technologies: before export, frozen

96. Colombia used to export crude oil from the 1920s until 1976, when growing internal demand overtook stagnating production. The Colombian Government reacted by opening up the sector to foreign involvement in exploration and by improving domestic prices for fuels. This started to pay off by 1980 and in 1986 a major new oil field was brought into exploitation. Since then, Colombia has become a crude oil exporter again.[48]

97. The development of this sector has relied on close cooperation between the Government and foreign transnationals. Most of the new developments took place in joint ventures between the State oil company, Ecopetrol, and one of a dozen transnationals (with Shell, Occidental Oil and BP as the most important).[49] In these joint ventures, the duration of foreign involvement is clearly limited, with the foreign

---

[46] This ranges from 1.4 times the amount lent for loans for strawberry production, to ten times the amount for the sugar industry. The difference reflects the normal speed of turnover of working capital in these industries.

[47] *Colombia Exporta*, March 1989.

[48] See Ministry of Mines and Energy, Memoria al Congreso Nacional, Anexo Histórico, *op. cit.*, Bogota, 1990. On the other hand, the country is a large importer of refined products, mostly petrol. Ecopetrol is preparing to build a new refinery which will make the country mostly self-sufficient in oil products.

[49] In early 1993, less than one quarter of Colombia's crude oil production (91,000 barrels/day out of a total of 434,000 barrels/day) originated from fields wholly owned by Ecopetrol. Almost 300,000

partner usually losing its share after 20 years. The development of the fuel sector is highly capital intensive and, without foreign investment, the Colombian Government would have had to borrow considerable sums abroad. Naturally, the foreign involvement implies that part of the benefits of the increase in oil exports is lost as profit repatriation.[50]

98. Domestic fuel consumption continues to rise and, at present levels of production, Colombia will become a net importer again by the end of the century. However, exploration continues and some important new oilfields have been discovered in recent years. When these fields become operational, Colombia will be able to maintain its crude oil exports at levels similar to or higher than current levels.

99. In the late 1980s, there were 35 different minerals exploited in over 7,000 mines. Most of these minerals are destined for the local market. Until the recent past, this was also the case for the main mineral, coal. Only from 1985 on did coal exports become important. The development of the largest deposit, El Cerrejón, was started in 1976 as a US$3 billion joint venture between a State company, Carbocol, and an Exxon subsidiary, Intercor (later, Ecopetrol also took a large ownership share, in order to raise the necessary additional development capital without selling out to foreign investors). While the small and medium-sized coal mines export about one fifth of their production, practically all of El Cerrejón's production is exported.[52] As in the case of the crude oil sector, development was expensive, and a large part of the gross export proceeds is lost through profit repatriation (see Box VII).

---

barrels/day came from joint ventures between Ecopetrol and foreign companies, with the balance produced in concessions fully owned by foreign companies. Eighty-five per cent of Colombia's known oil reserves have been discovered by foreign companies. See C. Brogan, "Colombia - Casanare oilfields prepare for start-up", *Petroleum Economist*, July 1993.

[50] Ecopetrol's President estimated in early 1993 that foreign oil companies, even on the assumption of a low oil price of US$ 18, would make a net profit of US$ 2.65 a barrel on every barrel they produced in Colombia. This would imply a total net profit for foreign oil companies of over US$ 300 million yearly. (The Government and Ecopetrol obtain US$ 10.35 a barrel; the remainder goes to exploration, development, production and transportation costs.) See C. Brogan, *op. cit.*.

[51] "Colombia: more discoveries", *Latin American Economy & Business*, March 1992, and "Colombia: a bit of a boom", *idem*, August 1992; "Colombia: more gushers", *idem*, July 1993. The newly discovered field are expected to become operational by 1996, allowing Colombia to strengthen its position as an exporter.

[52] *Idem*.

BOX VII

NET FOREIGN EXCHANGE INCOME FROM THE COAL SECTOR

Developments in the energy sector tend to be very expensive. The internal capital market of countries such as Colombia is not large enough to generate the necessary resources, so it is necessary to rely on foreign sources, be it as investors or lenders. This implies heavy lending abroad: Carbocol, Colombia's main coal company, accounted in 1990 for 10 per cent of Colombia's external debt, Ecopetrol, the State oil company, for another 15 per cent. Moreover, the development and operation of production in this sector is often complicated in terms of the machinery and installation of spare parts, and qualified people for certain jobs are not always available domestically. The result of these two factors is that a large part of the gross foreign exchange revenues from the energy sector leaves the country again in payment for production-related costs. As an indication, the currency flows linked to Colombia's coal sector are as follows:

Net currency earnings from the coal sector, 1986-1989 ($US mn)

	1986	1987	1988	1989
Gross export earnings	201	263	311	600
Related imports	138	169	53	39
Related service payments	15	19	6	19
Profit repatriation	94	121	150	168
Long-term debt repayments	11	31	80	100
Net proceeds	- 57	- 77	22	274

Source: Based on Ministry of Mines and Energy, Memoria al Congreso Nacional; Anexo historico (Report to the National Congress; Annex on past developments), Bogota, 1990, p. 135. Note that repayments of short-term debt are not included.

The situation in the fuel sector is not very different. These figures indicate that in terms of net export earnings, coffee has not yet lost its predominance. Of course, coffee production also requires some imports, mainly fertilizers and pesticides, but these do not account for a major part of production costs. As an illustration: in the flower sector, imports of chemicals in 1991 were valued at about one eighth of the gross earnings from flower exports.

100. Small-scale private coal producers obtain support from a special promotion fund, the Fondo Nacional de Carbon, which is financed by a 5 per cent tax on production (therefore, most of the income of this fund comes from the large-scale Carbocol coal mining). Exploration as well as infrastructure development are financed from this fund. Additionally, Carbocol promotes the regular usage, month by month, of coal by electrical installations, which helps to provide a secure market outlet for small-scale coal miners.

101. Gold exploitation was, until 1974, mainly in the hands of a foreign transnational, the International Mining Co. In that year, IMC was sold to national private interests. Shortly afterwards, gold prices rose strongly, and as a result Colombian gold production, both by this private company and by small, independent miners, increased rapidly. The Government reacted by paying more attention to this sector. Among other companies, Ecopetrol invested, together with the Government, in the exploration for gold. In 1988 the Government also set up a promotion fund for precious metals for small and medium-scale producers (who account for virtually all precious metal production).

102. Emerald mining was, at least officially, a government monopoly until 1968. Then, the Government decided to create a State enterprise, Mineralco (which now covers all minerals) to explore, exploit and manage the country's emerald deposits in cooperation with the private sector. There are now 17 emerald mines, and a large number of illegal small-scale operations. It is estimated that nearly half a million Colombians make their living in the emerald sector, from exploration and extraction to transformation, marketing and exporting, making this sector one of the country's largest employers. The Government tries to promote the sector by, in particular, improving the export marketing system so that producers get a fairer share of the final price.

103. Flower production in Colombia was started on a small scale during the early 1970s, when private entrepreneurs invested in the adaptation of cultivation techniques and the necessary infrastructure. The quality of the flowers grown around Bogota was such that it attracted the interest of foreign buyers. This stimulated other investors to become involved. Both the volume and variety of flowers exported increased steadily. Flower exports are now the fifth largest source of export revenues and some 20 different species are exported. Markets are being diversified as well: in 1991, 15 per cent of Colombian flower exports went to Europe compared to 7 per cent the year before, mainly as a result of a reduction of EC tariffs on Colombian exports.

104. The success of the flower sector is due to a number of factors:

- geographical and physical conditions that are very favourable. The climate around Bogota (lying at a height of some 2,000 m) is moderate, the number of hours of sunshine is high, and production is possible all year round;
- the availability of cheap labour, mainly women. By repressing labour union activity, the flower sector has managed to keep wage costs low;[53]
- the availability of the technical skills necessary to adapt foreign techniques to local circumstances. Most of this has been done without foreign support. The expertise gained by Colombian entrepreneurs in this area has now become an exportable commodity: they have become involved in joint ventures for flower exports in Mexico, Central America and Ecuador;
- the existence of a dynamic enterprise sector, with money to spare and a willingness to take risks, not only in launching the activity but also in constantly experimenting with a view to diversifying production. This last element is necessary to keep up with market demand, which often changes rapidly.

105. The involvement of the Government in the flower sector has been limited, but may have come at crucial moments. Initially, the Government subsidized flower exports (see section B.5); and has continuously supported export promotion, including efforts to secure market access (see for instance Box V).

---

[53] See "Colombia's flower industry grows up", *Latin American Economic Bulletin*, May 1992.

106. Fruit and vegetable exports have profited from strong support by the Government. Promoted by public assistance, 25 new tropical fruit export companies were created in 1988 alone.[54] Government support included subsidies, support to promotion campaigns, and investment in fruit marketing information networks and fruit marketing companies (in particular through the coffee diversification fund - see Box IV).

107. Other export sectors have not really grown, despite government efforts. For example, a major credit line of 150 million pesos was set up by the Banco de la Republica in the late 1980s to support investment in precious stone mining. This credit line, however, has not been used because the private enterprises concerned cannot provide the necessary guarantees. Several minor sectors in which the Government showed interest, financing research and development, proved not to be viable - e.g. the breeding of frogs in the Amazon area to supply the gourmet market for frog legs was found not to be feasible for environmental reasons and, for some fruit, no viable production techniques could be identified, despite years of experiment.

D. Marketing experience

108. The marketing of unprocessed primary commodities has, in general, proved to be within the reach of Colombian exporters (see table 5). Only for some small non-traditional exports have there been problems. For example, palm oil exporters have had serious problems in finding clients and in the case of tuna exports, cooperation with a transnational (Star-Kist) became necessary to obtain marketing access.[55]

109. The fact that the marketing of primary commodities is mainly in the hands of Colombian companies does not necessarily imply that these companies fully absorb the margins of international trade. In most cases commodities are sold on a spot basis and f.o.b.: beyond the country's ports, and the Colombian exporter has no share in marketing margins. Notable exceptions are the banana and flower sectors (see Box VIII), and Carbocol's coal exports which take place mainly through long-term contracts. Sometimes the f.o.b. sale of commodities is a well-considered economic decision - as in the cases of Federacafe's and Ecopetrol's exports. Until 1993, Federacafe owned, indirectly, a coffee fleet, but considered that to maintain the competitiveness of Colombian coffee it had to expose its national fleet to international competition. Ecopetrol has decided to stay out of fuel transport because of the financial risks linked to oil spills.[56] But in other cases, as, for instance, sugar exports, which are almost entirely sold by tender to

---

[54] GATT, *Trade policy review - Colombia*, Geneva, 1990, p. 154.

[55] Early in 1992, the United States banned tuna imports from a number of countries, including Colombia, because these countries are fishing tuna in such a way that too many dolphins are killed. This cuts the Colombian tuna industry off from its main market. Moreover, Colombia's fisheries industry is threatened by growing pollution of coastal waters.

[56] One of the other two oil exporters, Occidental Oil, sells, like Ecopetrol, only spot, f.o.b.. Shell sells mainly under long-term contracts and arranges the transport itself.

international trade houses, Colombian exporters are looking for ways of increasing their involvement.

Table 5

The marketing organization of main primary commodity exports, 1989-1990

Commodity	Export marketing structure
Coffee	About half of the value of exports passes through Federacafe, the association of coffee producers, and about half through private traders. Of these, the largest, a Colombian company, had a share of 9 per cent of exports in 1989 (the same company also controlled 60 per cent of Colombia's tobacco exports). One of the other two large exporters is owned by a German coffee company.
Crude oil	About 53 per cent of exports are by Ecopetrol, the rest by Shell and Occidental Oil.
Coal	Half of the exports of the Cerrejón Mine (90 per cent of total exports) are by Carbocol, the other half by Intercor (EXXON). To avoid competition, they agreed to supply different markets. The remaining 10 per cent is divided among a number of private exporters.
Bananas	All exports are through cooperatives, which took over production when, in the 1970s, the American banana transnationals withdrew from production. The largest is UNIBAN, which accounted for 52 per cent of Colombia's banana exports in 1989; two others, PROBAN and BANACOL, accounted for 17 and 13 per cent respectively.
Gold	Exports of gold were a monopoly of the Central Bank until 1991.
Flowers	There are around 350 companies exporting flowers, the largest of which accounts for about 7 per cent of Colombia's flower exports (this is also the only large foreign-owned flower company, part of an Argentine consortium). This fragmentation of the export sector is entirely different from the situation in the other main flower exporting countries, where exports are highly centralized.
Cocoa	Around 15 private traders, all of which, except one small company, are in Colombian hands, export over 90 per cent of cocoa beans; the remainder is exported by a trading company set up by the cooperatives of cocoa farmers. Concentration is high: one trader accounted for 30 per cent of exports in 1989, two others for 23 and 16 per cent respectively.
Emeralds	There is a multitude of small private exporters, and one export cooperative, the Federación Nacional de Productores y Exportadores de Esmeraldas. The Government is considering the creation of a national export-oriented emerald exchange.
Sugar	Some 90 per cent of exports are sold through a sugar trade company, CIAMSA, set up by the mills that are members of the Colombian sugar producer association. The remaining 10 per cent is sold by the sugar mills themselves.

Source: Based on interviews.

BOX VIII

DIVERSIFICATION INTO MARKETING

Both the banana and flower sectors offer examples of exporting companies that have taken over some distribution activities within the countries to which they export.

A banana company created in 1969, UNIBAN, created a subsidiary, Turbana, to handle its banana imports and marketing in the United States, as a way to get around the control of the three large United States banana companies. Turbana has since become the world's fourth largest fruit trader. Colombia's two other large banana export companies, Proban and Banacol, have also increased their control over international marketing. These companies now trade, apart from fruit and bananas from Colombia, bananas from Ecuador, Costa Rica, Nicaragua, Venezuela and Peru.

The five largest flower exporters have also diversified into providing marketing services and, since

E. Conclusion

110. Table 6 below gives an overview of the specific sectoral policies of the Government and of the involvement of domestic and foreign private sectors in the diversification of primary commodity exports away from coffee. As can be seen, the role of the Government has been dominant or substantial in the cases of crude oil, coal and fruit, while in two other sectors, flowers and fisheries, it has given important support at crucial moments. Like fruit, flowers and fisheries, other sectors have also profited their period of initial growth from the general supporting framework for non-traditional exports: tax reimbursements, preferential exchange rates during a short period of the 1960s, import duty drawbacks and preferential credits. In addition, the Government has in many cases promoted the development of these sectors by financing R and D and extension activities, often through the Diversification Fund.

111. The role of the private sector was predominant or important, however, for all exports other than crude oil and coal. In many cases, the private sector took the initiative and its initiatives were then supported by the Government. A dynamic entrepreneurial sector thus seems to be an essential ingredient for successful export diversification.

112. Foreign investors played a major part in the development of the capital-intensive and know-how intensive crude oil and coal sectors. In other sectors, know-how can, in general, be acquired by Colombian interests, sometimes with government support, but in most cases through private initiative.

Table 6

The role of the Government, domestic private sector and foreign investors in the development of selected primary commodity exports

	Role of the Government	Role of the domestic private sector	Role of foreign investors
Crude oil	Dominant role. All oil is exploited in joint ventures between the Government and foreign transnationals.	No role of significance.	Large role. Transnationals provided a major part of exploration and exploitation finance, and technical expertise.
Coal	Large role. The major coal producing company is a government-transnational joint venture. Small private producers also receive government support.	Small, albeit increasing, role.	Large role. Transnationals provided a major part of exploitation finance, and technical expertise.
Gold	Minor role. The Government has undertaken some limited gold exploration activities, and created a fund for small and medium-scale producers.	Large role. Most gold mining is in the informal sector, by small, independent miners.	Minor role. Foreign companies were the initial investors in the gold sector, but their production remained low.
Bananas	Minor supporting role. The Government has a small share in a banana marketing company.	Large role. Banana companies are mainly in private hands or cooperatives, which have undertaken their expansion programme mainly by their own efforts.	Minor role. Banana plantations were set up by foreign transnationals, but the sector was developed strongly only after Colombian domestic interests took over.
Raw sugar	Supporting role. The Government has invested on a minor scale in sugar cane milling and refining, and provided support to the development of the sector through the Diversification Fund.	Dominant role. Colombia's sugar sector is mainly set up by and in the hands of the domestic private sector	No role of significance.
Flowers	Important supporting role. The Government intervened at key moments, for market promotion and to protect existing markets against protectionist measures.	Dominant role. Colombia's flower sector has mainly been developed by local private entrepreneurs.	Minor role. A few foreign companies invested in the Colombian flower sector.
Fisheries	Important supporting role. The Government invested in the creation of fisheries and shrimp companies, and financed the acquiring of expertise to make shrimp farming successful.	Large role. Most of the actual production is by private companies.	Minor role. One transnational provides marketing support for frozen tuna.
Fruits	Large role, especially through the Diversification Fund, which financed market studies and a major part of research and development and extension activities in the fruit sector, and was used to provide special credits and create commercialization companies. Also, support to generic promotion campaigns.	Large role, in the case of fruit exports promoted by the banana companies, and in the case of some minor fruit exports (such as strawberries) initiated by private flower growers.	No role of significance.
Cocoa	Supporting role, including through the Diversification Fund.	Dominant role. The cocoa sector has mainly been developed by the Colombian private sector.	Minor role.

Source: UNCTAD secretariat. Products are ranked in order of size of exports in 1990. Only activities of direct relevance to the promotion of the different sectors are included.

Chapter IV

GOVERNMENT POLICIES SPECIFIC TO VERTICAL DIVERSIFICATION AND THEIR RESULTS

A. Policies for vertical diversification

113. Colombia has never had a specific policy to promote domestic pre-export transformation of raw materials. The processing of commodities is seen as just another economic activity that may or may not be worth while supporting. There are no special facilities such as tax benefits, or preferential access to risk capital for pre-export processing. There was a special credit line for transformation activities, under the administration of the government export promotion agency, Proexpo, but no use has been made of it. Government activity was mainly limited to participation in some specific commodity processing projects: the petrochemical industry, the production of ferronickel and silk production.

1. The earmarking of funds for vertical diversification

114. Although the Government has invested directly in some processing industries, in particular petrochemicals, no funds have been specifically earmarked and used for vertical diversification. However, IFI, the main funding agency for the promotion of industrial and other export-oriented activities has financed, among these, part of the development of Colombia's ferronickel industry, and has also invested in cement production, textiles and agro-industry (silk production, shrimp farming, citric acid production, and the production of printing materials from sugarcane bagasse).[57] The other large government funding agency, the Fondo de Promoción de Exportaciones, has invested in sugar cane milling and refining.[58]

115. In 1992 a new fund was created, the Fondo de Modernización Económica, receiving its resources from a 6 per cent tax on imports. These funds are to be used to pay some remaining financial incentives (see chapter III, section B.5), and to support the modernization of the industry sector (including commodity processing and the upgrading of the quality of entrepreneurship). Because financial incentives will gradually be scaled back, an increasing part of the funds will be used for industry conversion.

2. Diversification-specific regulation

116. Marketing regulation can have considerable consequences for diversification, especially into processing. The case of Indonesia, which has considerably strengthened its exports of processed wood through the ban of raw timber exports is well known. Several other countries have tried to do the same, with more or less success. In Colombia, the Foreign Trade Council, the supreme body dealing with trade policy, is empowered to establish the degree of working or processing which specific products must have

---

[57] *Reglas de Juego para la Apertura*, *op. cit.*, Annexes 1A, 1B.

[58] *Idem*, annex 2.

in order to be exported.[59] In practice, however, regulation has not been used as a means to promote commodity processing. An export quota did exist until 1991 for essential products such as sugar, cotton and rice (with corresponding company-level export quotas), but this was basically to protect processors producing for the domestic market against a shortage of supply of raw materials. The levels of export quotas in general (except for cotton) exceeded exportable quantities. Now, only an export ban on wood for ecological reasons is in force.

117. In the case of cotton, until 1991 the Government used to set not only an obligatory domestic sales quota (for sales to the textiles sector), but also prices. From the early 1970s to 1988 there were two different cotton prices, one fixed price for cotton used in domestically-oriented textiles production, and a variable price, linked to world market prices, for cotton used in exported textiles.[60] In 1988, the Government decided to shift to one, government-determined price. As domestic cotton prices were below international prices in most years, this pricing policy discouraged Colombian cotton growers and favoured textile producers, giving them a comparative advantage over foreign competitors.[61]

3. Financial incentives

118. Processed commodities receive much the same treatment, in terms of financial incentives, as primary commodities. Only in a few cases were financial incentives specifically used to promote processing. One special case was that of leather products; there were no import duty drawbacks for hides and leather whereas such drawbacks existed for exports of leather products.

B. Vertical diversification experience

119. The list of processed commodities exported by Colombia in the late 1980s has little in common with that of the beginning of the decade. During the 1980s, and especially the second half of the decade, many non-traditional processed commodities began to be exported (see table 7). Most of these activities have been developed by private initiative, without much government support.

120. Foreign participation in commodity processing is not limited to involvement in ferronickel. Transnational companies (Nestlé and Mitsubishi) are involved in or control the production of coffee extracts (see Box IX); silk (see Box X);[62] citric acid; and canned pineapple. In all these cases, the processing factories were set up with the explicit goal of servicing the international market. During the 1970s, TNCs also became involved in a number of domestically-oriented processing industries, which were promoted by the Government as part of its import-substitution policy: namely paper, milk powder,

---

[59] *Idem*.

[60] The share of cotton used for export-oriented production of textiles was, until 1987, fixed at 37.5 per cent by the Government; in 1987 it was reduced to 25 per cent.

[61] G. Castro Guerrero, *Perspectivas del cultivo de algodón en Colombia* (Prospects for cotton cultivation in Colombia), Confederación Colombiana del Algodón, Conalgodón, Bogota, August 1990.

[62] "Sericulture in Colombia", *Colombia Exporta*, Proexpo, Year IX, No. 30, June 1991.

fertilizers, synthetic fibres, tyres and glass.[63]

BOX IX

DEVELOPING NEW OUTLETS FOR COFFEE

Japan is traditionally a tea-drinking nation. Brazilian and Colombian exporters understood that to replace tea by coffee could prove rather difficult. Instead, they decided to create a new market, for tinned, cooled coffee, which would not compete with tea but with soft drinks, and would be sold mainly through vending machines. In Colombia, private exporters set up a joint venture with Mitsubishi (which has access to the distribution networks), and a promotion campaign was started. This new product proved a direct hit, allowing Colombian coffee exporters to tap an important new market. The Japanese canned coffee business is now worth some US$ 5 billion, and an expansion into other Asian

BOX X

THE INTRODUCTION OF SILK PRODUCTION

In 1970, as part of its diversification programme, Federacafe started a study on the cultivation of silkworms. With financing from the Diversification Fund, a small pilot plant was set up in 1985, which began exporting on a small scale soon afterwards. A visit by the President of Colombia to the Republic of Korea in 1987 resulted in a joint venture with a Korean enterprise for the production of raw silk thread. This was soon followed by two other Korean enterprises, while a number of Colombian silkworm breeders also set up their own processing plants. The Colombian Government promotes production by financing all technical assistance to silkworm breeders and by providing cheap credit. When all these projects are operative (expected by 1993), Colombia will be one of

121. Colombian private enterprises dominate in the processing of leather, cotton yarn, cement, white sugar, cocoa and some of the minor products (although transnationals are involved as well - for instance, Nestlé has a small cocoa processing operation). In most cases, processing was set up to supply the domestic market, and later expanded to exports. Only in the case of leather (see Box XI) can it really be argued that the Government has played an important part in encouraging exports.

BOX XI

THE PROMOTION OF THE EXPORT OF LEATHER PRODUCTS

Leather products have long been considered to have a large export potential, and this sector has therefore received considerable government support. As leather accounts for half the costs of manufactured leather products, this support was targeted both at the improvement of the production of hides and skins, and at the manufacturing of leather and leather products. Moreover, export marketing is complicated, and thus received specific attention.

With support from the EC, the government export promotion agency, Proexpo, has worked on improving quality and raising productivity at all levels of production. They also brought small and medium-sized producers (responsible for over half of production) into contact with foreign clients. All exporters profited from the targeted credits.

The government support has been successful. Leather products have been one of Colombia's fast growing export sectors. Exports from this sector increased from $ 47 mn in 1981 to $ 93 mn in 1987, and to $ 179 mn in 1990. Some new export products, such as leather dog toys (now valued as over $ 9 mn in exports) have been developed from

---

[63] ECLAC, *Las empresas transnacionales en el desarrollo Colombiano* (Transnational corporations in Colombia's development), Santiago de Chile, 1986, p. 14. The 10 main transnationals accounted for around 10 per cent of total manufactured production in Colombia in the early 1980s.

Table 7

Exports of major processed commodities

Product (a)	Value US$ million 1990	Remarks
Fueloils	355	Exports are mainly to the US market, because the nickel and asphaltite contents are too high for the European market. Prospects for expansion are very limited.
Leather & Leather products *	179	See Box IX.
Ferronickel *	146	Produced by a Billiton-Government joint venture and exported by Billiton. Studies are under way on the further transformation of the ferronickel. A plan to double the capacity of the nickel smelter was abandoned in early 1993 because of low world market prices.
Coffee extracts	58	Federacafe has a factory producing some 4 million tonnes of soluble freeze-dried coffee and some 2 million tonnes of frozen coffee extracts. The private sector has two such factories (of which one is a joint venture with Mitsubishi, see Box IX), and one factory producing 6 million tonnes of soluble coffee made by evaporation, partly owned by Nestlé. Exports are only a small part of production, in the case of all of these factories.
Cotton yarn and fabrics	41	Production and exports are stagnating. The technological level of the sector has been allowed to deteriorate vis à vis the world market. Moreover, domestic textile processors need an increasing quantity of yarn and fabrics for their production (and have even started importing these products since 1990); a decline of yarn and fabrics exports can therefore be expected, while textile exports will increase. Some 32,216 MT of cotton were also exported in the form of textiles; at international market prices, this amount of cotton would have a value of approximately US$ 61 million.
Cement	40	While more than 80 per cent of production is still for the domestic market, exports of cement have almost doubled in volume in the 1980s, with three factories in the North of the country becoming mainly export oriented. Exports are expected to expand, with investments in port facilities being made by these three private factories, and sales efforts undertaken in non-traditional markets.
Gasoils	28	Exports of surplus production with strong year-to-year fluctuations.
White sugar *	14	This sugar is of a lower quality than the white sugar normally traded internationally. All is exported to regional markets. Further expansion is expected.
Cocoa butter*	11	Exports are only a small and declining part of total production.
Passionfruit juice *	11	First factory set up by Federacafe, with exports starting in 1986. In 1990, Colombia had become the world's second largest exporter, after Brazil, with plans for a strong further expansion of exports.
Citric acid *	8	Factory set up by sugar refineries in cooperation with a US company.
Briquettes *	8	An expansion is expected. The State coal mining enterprise, Carbocol, is setting up a test facility for the production of briquettes to replace the use of firewood, especially by industrial installations (such as sugar mills). It is hoped to expand production, and supply other Latin American countries such as Brazil and Haiti.
Confectionery	6	Exports are only a small part of total production.
Silk	N.A.	Created in the mid-1980s. Most production is in joint ventures with Korean companies and is strongly export oriented.
Molasses	N.A.	Exports of this by-product of sugar are only a small part of total production. The bulk is used domestically for the production of animal food.
Chocolate*	N.A.	Exports are only a small and declining part of total production, due to fast growing local demand.
Petrol	N.A.	Export of occasional surpluses.
Canned hearts of palm *	2	Created in the early 1980s. Four canning plants are now active, and export 90 per cent of their production.
Canned pineapple *	N.A.	Produced and exported by Chiquita.
Canned asparagus *	N.A.	

Source: UNCTAD secretariat, based on a large variety of sources.
a/ Exports of products indicated with an asterisk were initiated during the 1980s.
N.A. Data not available.

C. Comparative analysis of diversification experience

122. Table 8 gives, for a few commodities, an impression of the extent of commodity processing in Colombia compared to that in other countries. Several products that can be exported in raw or processed form are not included - ferronickel because the data for an international comparison are lacking; cotton because a large proportion of cotton clothing exports are produced from imported materials; and cocoa because the Colombian cocoa industry is primarily domestically oriented, and exports of cocoa butter and chocolate consist only of occasional surpluses.

Table 8

The extent of commodity processing in Colombia: An International Comparison

Product	Value of a product's exports in processed form relative to the value of its exports in unprocessed form (average 1987-1989)	
	Colombia	Other countries
Coffee extracts/ coffee beans	0.04	Brazil 0.12; Côte d'Ivoire 0.23; Nicaragua 0.07
Fuel products/ crude oil	0.37	Ecuador 0.15; Malaysia 0.11; Mexico 0.06; Nigeria 0.02; Peru 13.76; Venezuela 0.71
White sugar/raw sugar	0.09	Argentina 0.06; Brazil 0.97; Cuba 0.06; Dominican Republic 0.01; Guatemala 0.00; Mexico 0.07

Source: Calculations based on UN COMTRADE data base.

123. Pre-export processing of coffee seems rather low in comparison to some other countries. However, the potential for further domestic processing of coffee is rather limited. Investment costs are very high, due to the capital and knowledge-intensive production techniques used in coffee processing; too high for Colombian investors or, for that matter, the Colombian capital market. Moreover, there is a limited market for processed pure Colombian coffee, as distinct from beans, which means that it would be necessary to import coffee from other countries for blending. Other technical factors (such as the shorter shelf life of ground coffee as compared to coffee beans) also hinder further processing. Finally, there would be marketing problems (see section D).

124. Exports of fuel products are relatively low compared to those of neighbouring Venezuela and Peru. There are also persistent imports of refined petroleum, due to a shortage in domestic refining capacity. However, the investments necessary to enhance processing in the fuel sector are enormous, and it is doubtful whether they would be economically justified.

125. In sugar, the degree of pre-export processing is not exceptionally low. Nevertheless, the sugar sector is trying to upgrade its sugar exports, and to sell semi-refined sugar, especially to the regional market. For this purpose it is entering into cooperation projects with the sugar industry in neighbouring countries.

D. Marketing experience

126. Marketing processed commodities is much more complicated than marketing unprocessed ones, because the markets are more segmented, with more scope for market power, and a strong brand name differentiation for consumer goods. There are serious market access problems for those trying to penetrate these markets without the support of established companies. In Colombia, the importance of transnationals to secure market access can be seen from the fact that foreign companies are important in or dominate the export trade in several processed commodities, including ferronickel, coffee extracts, silk, citric acid and canned pineapple (see table 7).

127. Mitsubishi accounts for about one quarter of exports of coffee extracts, the rest being in the hands of domestic enterprises. About 15 per cent of the coffee produced in Colombia is processed domestically. Exports used to be a secondary activity for most coffee processing plants. However, subsidies to domestic coffee sales were reduced from 1987 on and completely eliminated in November 1990. As a result domestic demand declined by 30 per cent between 1988 and 1990. There thus is an increasing pressure on instant coffee factories to export. Marketing problems will make this very difficult. Strong brand names already dominate in many markets, and the costs of entering markets are high. For example, the right to put a product on the shelves of a United States supermarket chain costs some US$ 5 million. An expansion of instant coffee exports will only be possible by giving up some of the profits of marketing; that is, coffee will not be exported under a Colombian brand name, but under the name of the importer (as is already the case for exports to the EC). Colombia is making an effort to actively promote its exports of instant, freeze dried, extract, semi-processed and roasted grounded coffee. A ban prohibiting the export of semi-processed coffee originally destined for the domestic market was lifted and projects are under way to start processing decaffeinated coffee. Nevertheless, it has proved difficult, to expand exports and these have been insufficient to compensate for the decline in domestic demand. In the first half of 1991, coffee processing was down 27 per cent compared to the first half of 1990.[64]

128. In ferronickel, the Government entered a joint venture with Billiton and, until this company sold its shares, Hanna Mining, to secure its access to the international market. The market for ferronickel is strongly concentrated and it is difficult for an outsider to penetrate it. In fact, the lenders for the project, including the World Bank, demanded to be shown sales contracts before they were willing to deblock their loans. Billiton is now solely responsible for marketing, and is not even obliged to inform its Colombian partner of the prices it receives.[65]

---

[64] "Colombia: the gains start to show", *Latin American Economy & Business*, November 1991; José Gemeil, "Colombia: aiming for new highs", *Coffee & Cocoa International*, No. 3, 1991.

[65] Billiton now pays its partner a price based on the prices quoted on the London Metal Exchange (LME), after deducting a sales commission, while Colombia exports a higher quality of nickel than the quality that acts as a reference for the LME contract.

E. Conclusion

129. As table 9 shows, the roles of the government and of foreign transnationals in the development of processed commodities for export have been substantial, much more so than for primary commodities. The domestic private sector has played no part at all, or only a minor one, in the development of the petroleum products, ferronickel and silk sectors. This is to a large extent due to the financial requirements for the development of these sectors. On the other hand, private investors have taken the initiative in the development of smaller-scale activities, in particular textiles and leather products. The role of the Government in these cases has largely been limited to providing a support framework.

130. In the cases of coffee extracts and citric acid, the investments required for setting up a factory were so large that this was only possible with access to important sources of finance. In the case of citric acid, much of these funds came from the Government and a foreign investor, while the remainder were provided by relatively well-capitalized sugar factories. These sugar factories were also able to finance the construction of white sugar factories themselves. For coffee extracts, the cooperative coffee sector was also well-capitalized, as were some of the large private coffee growers and exporters. This made the investment in four coffee factories possible. In the case of sugar and coffee extracts, the fact that a major share of production was destined for the domestic market, not for exports, provided investors with the necessary security.

Table 9

The role of the government, domestic private sector and foreign investors in the development of exports of selected processed commodities

	Role of government	Role of domestic private sector	Role of foreign investors
Petroleum products	Major. The petrochemical industry is controlled by Ecopetrol, the State oil company.	No role of significance.	No role of significance.
Ferronickel	Major. The sole ferronickel producing company is a Government-Billiton joint venture.	No role.	Major role. Billiton has provided a major part of investment capital and expertise, and is still responsible for marketing.
Cotton textiles	Supporting role, ensuring, among others things, cheap inputs to textile producers.	Major role. A large part of textile production is relatively small scale and, to a large extent, owned by Colombian private investors.	Minor role. Some foreign companies invested in textile factories during the 1960s and 1970s.
Hides and leather products	Strongly supporting role, including through programmes specifically targeted at this sector.	Major role. The production of leather products is relatively small scale, and mainly owned by Colombian private investors.	No role of significance.
Coffee extracts	Supporting role.	Major role. All coffee plants are set up by Federacafe or the private sector.	Important role. Mitsubishi and Nestlé both have coffee processing interests.
White sugar	Supporting role. There are no specific government support measures for white sugar exports, but negotiations for regional free trade have helped to open up a very important market to private exporters, allowing them virtually to replace exports of raw sugar by those of white sugar.	Major role. Most of the investments in white sugar production have been made by private investors, with small investments by the Diversification Fund.	No role of significance.
Citric acid	Important role, providing part of the necessary investment capital.	Large role, taking the initiative for the set up of a citric acid plant, and carrying part of the necessary investment.	Major role. Colombia's citric acid plant was set up as a joint venture with a US company.

Silk	Major role. The Diversification Fund was used to finance a pilot project for silk production.	Minor role. Private investors only entered the sector after several plants had already been set up by the Government together with foreign investors.	Major role. Several Korean enterprises initiated large-scale silk production in Colombia.
Source: UNCTAD secretariat. Products are ranked in order of size of exports in 1990. Only activities of direct relevance to the promotion of the different sectors are included.			

SOURCES

- Asocaña, Aspectos Generales del Sector Azucarero, 1990-1991, Bogota, 1991.

- Asocolflores, Revista de la Asociación Colombiana de Exportadores de Flores, No. 27, June 1991.

- Chris Brogan, "Colombia - Casanare oilfields prepared for start-up", Petroleum Economist, July 1993.

- Camara de Comercio de Bogota, Servicios de Promoción Comercial y Posibilidades de Cooperación, Bogota, October 1991.

- Gustavo Castro Guerrero, Perspectivas del Cultivo de Algodón en Colombia, Confederación Colombiana del Algodón, Conalgodón, Bogota, August 1990.

- "Colombia se alista para entrar al mapamundi de la fruticultura", Nueva Frontera, January 1990.

- Comisión Económica para America Latina y el Caribe (CEPAL), Las Empresas Transnacionales en el desarrollo Colombiano, Santiago de Chile, 1986.

- "El crédito para diversificación", Nueva Frontera, January 1990.

- "La diversificación en la economía cafetera y el desarrollo nacional", Nueva Frontera, Documento especial: 25 años diversificando las zonas cafeteras, June 1988.

- H. R. Ensminger, "The mineral industry of Colombia", US Bureau of Mines, Minerals Yearbook, 1987.

- Federacafe, VI Plan Quinquenal de Diversificación Cafetera, internal note, 3 July 1991.

- Financial Times, various issues.

- GATT, Trade Policy Review - Colombia, Geneva, 1990.

- José Gemeil, "Colombia: aiming for new highs", Coffee & Cocoa International, No. 3, 1991.

- Fernando Hurtado Pascual, Plan de Acción para el Desarrollo de Cultivos de Susticutión de la Hoja de Coca en la Región Andina; Desarrollo Alternativo en Bolivia, Colombia, Ecuador y Peru, International Trade Centre UNCTAD/GATT, 16 September 1992.

- Fernando Hurtado Pascual, Estrategía para la Ejecución de una Política de Desarrollo Alternativo a la Coca para la Región Andina en la Decada de 1990, International Trade Center UNCTAD/GATT, January 1993.

- Latin American Economy & Business, various issues.

- Ministerio de Desarrollo Económico, Reglas de Juego para la Apertura, Bogota, 1991.

- Ministerio de Minas y Energía, Memoria al Congreso Nacional, 3 vols., Bogota, 1990.

- *Idem*, Estadísticas Minero-Energéticas 1940-1990, Bogota, May 1990.

- Jose Antonio Ocampo and Eduardo Lora, Stabilization and adjustment policies and programmes; country study: Colombia, WIDER, Helsinki, 1987.

- Proexpo, "CERT", Boletín del Exportador, No. 33-34, 1991.

- Proexpo, Colombia Exporta, various issues.

- Proexpo, Export Directory Colombia 1991-1992, Bogota, 1991.
- Proexpo, Linea de crédito de pre-embarque - reglamentación, Circular P-SDC-002, 19 April 1991.

- Proexpo, Servicios de promoción externa de PROEXPO, Bogota, 1990.

- "Sugar in Colombia", Sugar y Azúcar, April 1993.

- Francisco E. Thoumi, "Why the illegal psychoactive drugs industry grew in Colombia", Journal of Interamerican Studies and World Affairs, vol. 34, No. 3, Autumn 1992.

INTERVIEWS IN BOGOTA AND CALI, DECEMBER 1991

<u>Bogota</u>

Fondo de Promoción de Exportaciones de Colombia (PROEXPO)
Constanza Laignelet de Palomino, Jefe, Dpto. de Oficinas Comerciales y Regionales
Carlos José Rincón, Jefe, Dpto. de Desarrollo Agropecuaria

Instituto Colombiano de Comercio Exterior (INCOMEX)
Armando Perdomo, Jefe, División de Organismos Internacionales
Miguel Michaels Urbina, Jefe, Sección de Otros Organismos
Lucy Repas L., División de Organismos Internacionales

Ministerio de Relaciones Exteriores
Carlos E. Hernandez, Viceministerio Económico, Cancilleria

Ministerio de Agricultura
José E. Macias Medina, Subdirector de Comercio Externo
Martha Elena Escandón G., División de Exportaciones
Carlos Enrique Pardo Hoyos, Secretario Técnico del Fondo de Estabilización del Cacao

Ministerio de Minas y Energia
Olga Escobar Molano, Jefe, Oficina de Planeación
Oscar Eduardo Rojas Bonilla, Jefe, División de Programación
Miriam de Gechem, Jefe, Sección Cooperación Técnica Internacional

Instituto de Investigaciones en Geociencias, Mineria y Quimica (INGEOMINAS)
Jorge E. Valdiri Wagner, Jefe, División Cooperación Téchnica Nacional y Internacional

Minerales de Colombia S.A. (MINERALCO)
Luis Eduardo Castro, Director

Carbones de Colombia S.A. (CARBOCOL)
Mauricio Estrada M., Director Mercadeo
Patricia Gómez Méndez, Juridica
David Reinstein B., Jefe, Dpto. de Planeación Evaluación y Negociación

Asociación de Exportadores de Café (ASOEXPORT)
Magdalena Pardo, Secretaría General

Ministerio de Desarrollo Economico
Eduardo Muñoz, Director de Comercio Internacional
Jaime Baragas Ortiz, Jefe de Político y Estrategia de Comercio Internacional

Departamento Nacional de Planeación
Luis H. Gutiérrez R., Jefe, División Política Industrial, Unidad de Desarrollo Industrial y Tecnológico
Diana Ruiz, Jefe, División Comercialización Agropecuaria

Banco de la República
Roberto Rubio P., Director, Departamento de Cambios Internacionales

Camara de Comercio de Bogota
Ana R. de Anchique, Jefe, Dpto. Comercial
Alejandro Galofre, Vicepresidente Comercial

Luz Mery Muñoz, Coordinadora Red Aico

Empresa Colombiana de Petróleos (ECOPETROL)
Enrique Lee Baron, Foreign Trade Manager

Asociación Colombiana de Exportadores de Flores (ASOCOLFLORES)
Juana Maria Unda Bernal, Gerente General

Federación Nacional de Cacaoteros (FEDECACAO)
Jairo Verano Fajardo, Director Técnico
Jorge Barrios Kidd, Agrotrade

Asociación de Cultivadores de Caña de Azúcar de Colombia (ASOCAÑA)
Ricardo Villaveces Pardo, Presidente
Juan Pablo Cabal Cabal, Director Bogotá

Fondo de Promoción de Exportaciones de Colombia (PROEXPO)
Jaime Fernandez Roa, Jefe, Dpto. de Desarrollo Industrial

Federación Nacional de Cafeteros de Colombia (FEDERACAFE)
Hernan Uribe Arango, Subgerente General
Ignacio Umaña Mallarino, Director, División de Mercadeo y Agroindustria
Roberto Pizarro Mondragón, Subgerencia General Técnica

Asociación Nacional de Exportadores (ANALDEX)
Javier Diaz Molina, Vicepresidente Técnico

Cali

Asociación de Cultivadores de Caña de Azúcar de Colombia (ASOCAÑA)
V. Izquierdo B., Asesor Técnico y Económico

Sociedad de Comercialización Internacional de Azucares y Mieles S.A. (CIAMSA)
Juan Manual Orozco G., Dpto. Exportaciones

Azucerara del Valle Ltda.
Luiz Augusto Jaramillo P., Gerente

Ingenio Riopaila S.A.
Augusto Solano Mejia, Gerente General