Beneath the Surface: The Impact of Radical Economic Reforms on the Outward Orientation of Argentine and Mendozan Firms, 1989–1995*

OMAR N. TOULAN AND MAURO F. GUILLÉN

Abstract. The main argument of this article is that in order to assess accurately the impact of a market liberalisation programme such as the one Argentina has undergone, one must look beneath the aggregate statistics and analyse underlying changes in critical market structure and organisational variables. While aggregate trade figures imply that the country has been successful at reintegrating itself into the world economy, two underlying trends reveal potential threats to the country's long-term development. These trends relate to the level of value added being created in the country, particularly with regard to its exports, and to changes in the composition of its trading partners.

Despite four decades of relative decline, Argentina is still the third largest economy in Latin America and ranks at the top of the region in terms of *per capita* income and most standard indicators of social development. Furthermore, since 1990 it has been the second largest destination of foreign direct investment (FDI) in the region after Mexico.[1] In spite of the impact of the recent economic reforms, however, Argentina still has one of the largest government sectors, highest average trade tariffs, and least outward-oriented economies in the region.[2] And while Argentina was home to some of the first multinationals in any developing country,[3] Brazil and Mexico currently have more firms both in Latin America's Top 500 ranking and on the United Nation's list of the largest multinationals headquartered outside the Triad (USA, Japan, European Union) economies.[4] The purpose of this article is to assess the differential

Omar N. Toulan is at the Sloan School of Management, MIT, Cambridge, Massachusetts.
Mauro F. Guillén, is at the Wharton School, University of Pennsylvania, Philadelphia.

* The authors would like to acknowledge the support of the MIT–Province of Mendoza Project, and in particular that of Donald Lessard.

1 UNCTAD (United Nations Conference on Trade and Development), *World Investment Report 1995* (New York, 1995), p. 393.
2 *América Economía Annual Edition 1995–1996*, pp. 14–20.
3 Jorge Katz and Bernardo Kosacoff, 'Multinationals from Argentina', in Sanjaya Lall (ed.), *The New Multinationals* (New York, 1983), pp. 137–219.
4 *América Economía Annual Edition 1995–1996*, p. 98; UNCTAD, *World Investment Report 1995*, pp. 30–1, 398.

impact that the radical economic reforms implemented since 1989 have had on Argentina's industries and firms both in the country as a whole and in one of its provinces: Mendoza.

Our key argument is that the foreign trade and investment trends underlying the surge in Argentine economic growth in the early 1990s indicate a less than optimal role for the country and its firms in the world economy. Exports are expanding rapidly, but a disproportionate share of the growth since 1989 is accounted for by products with a relatively low value-added content, and by markets in Mercosur – the customs union linking Argentina with Brazil, Paraguay and Uruguay – and the rest of Latin America at the expense of the more sophisticated markets of North America and Europe. The implications which these trends hold for the future competitiveness of the country are potentially severe.

One might argue that Argentina once attained high levels of wealth precisely by drawing on its natural resources and traditional sources of comparative advantage to produce and export low value-added goods. In fact, Argentina grew rich during the late nineteenth century and the first third of the twentieth century by exporting primary agricultural products, mostly to Europe. One should be reminded, however, that the development of Argentine agricultural production and export income between 1880 and World War II was far from smooth. International demand for its products was subject to sharp crises such as those taking place around 1890, 1910, and 1921 as well as during the early 1930s and the early 1940s. Conflicts between those situated upstream at the relatively less profitable stages of the value-added chain and those closer to the market (e.g. cattle ranchers versus meat-packers, or crude oil producers versus refiners and distributors), became quite virulent during the 1920s and 1930s.[5] Thus, well before structuralist or dependency critiques flourished, and before populist–nationalist economic policies became the norm, Argentina suffered from recurrent balance of payments crises as a result of its reliance on export earnings from low-value, volatile commodities to cover imports of consumer and capital goods and to service its foreign debt.[6] In a world dominated by bilateral trade deals, Argentina had large surpluses with Britain (its main export market for beef) and huge deficits with the USA (its major source of inputs, machinery and consumer goods), a triangular pattern that proved unmanageable during the 1930s and late 1940s as the British economy and Sterling declined.[7]

[5] Peter Smith, *Politics and Beef in Argentina* (New York, 1969); Carl Solberg, *Oil and Nationalism in Argentina* (Palo Alto, 1979).

[6] Paul Lewis, *The Crisis of Argentine Capitalism* (Chapel Hill, NC, 1992), pp. 13–98; David Rock, *Argentina 1516–1987: From Spanish Colonization to Alfonsín* (Berkeley, CA, 1987), pp. 162–249.

[7] Rock, *Argentina 1516–1987*, pp. 197–8, 223–5, 290–3, 321–2.

Our argument about the current situation, however, is neither a structuralist nor a dependency one.[8] In a world economy tending towards globalisation, efficiency-based competition, and a mix of multilateralism and trading blocs, the product composition of exports relative to imports is not as important as the value-added content of the exports and how it interacts with patterns of comparative advantage. It is well known that some countries have been able to develop economically on the basis of natural resources, by triggering investments in basic and capital-goods industries (e.g. Australia, Sweden, Finland, Norway). We argue that a country rich in natural resources ought to build on those advantages and direct its export effort towards sophisticated markets by focusing on such value-adding activities as product development (if not research), quality enhancement, marketing know-how, and upgraded worker skills. Our analysis shows that Argentine industrial exports have not built upon the country's natural resource advantages, are not principally destined to the more sophisticated markets, and are growing less rapidly than exports of lower value-added content. We also analyse in depth the experience of one of the country's provinces, Mendoza, which, in contrast to Argentina as a whole, has been successful at developing a capital-goods industry with high export growth. However, similar to the national trend the province has seen a dramatic reduction in agro-manufactures in favour of primary agricultural products.

Market reforms in Argentina

By the mid-1980s pressures to reform the Argentine economy became paramount. The country was falling further and further behind the rest of the world, with a string of years of negative real growth rates. Argentina's share of world exports had fallen from a high of 3.0 per cent earlier in the century to 0.3 per cent by 1990, even though the country produced more than 1.1 per cent of world output. Among the issues which needed to be addressed were a state structure which employed nearly 20 per cent of the economically active population of the country, a system of subsidies on which much of the private sector depended, hyper-inflation, an exploding foreign debt, an ageing infrastructure, and a coefficient of trade openness of only five per cent.[9]

Even though Carlos Menem won the 1989 presidential election on a traditional Peronist platform, his campaign was intriguingly un-

[8] For a review of those positions, see Robert Gilpin, *The Political Economy Relations* (Princeton, 1987), pp. 274–90.

[9] Coefficient of openness is defined as half the sum of imports and exports of goods and services over GDP.

programmatic. He surprised virtually everyone by appointing liberal economists from one of the leading business groups (Bunge & Born) and noted anti-Peronists to top cabinet and economic staff positions. With the failure of the Austral Plan to reduce inflation still fresh, Menem correctly understood the need to force changes in state finances and labour negotiations as well as to implement a sound currency stabilisation programme. He almost immediately succeeded in reversing the trend towards exploding public-sector deficits with a bold privatisation programme, and in splitting the labour union leadership and imposing sector-by-sector deals.[10] His first few months in office finished disastrously at the end of 1989, however, with the collapse of the Bunge & Born Plan to bring down inflation.

The year 1990 witnessed further inroads in public deficit reduction, but inflation success eluded him once again in spite of the harsh therapy of the bank deposit-bond conversion (Bonex) plan.[11] It was not until the implementation of Domingo Cavallo's convertibility plan of March 1991 that inflation finally subsided. Menem's reforms affected virtually all aspects of the economy, but those which had a significant impact on the internationalisation of economic and business activity can be classified into three broad areas: monetary policy, fiscal policy, and trade and regulatory policy.

Monetary reform

Of all the reforms adopted by the government since 1989, the one which has received the most attention and has served as the foundation for the other reforms is the Convertibility Law. It represented a major change in both the exchange rate and monetary regimes of the country. On the one hand, the Law fixed the currency to the dollar on a one-to-one basis and required that the Central Bank fully back the monetary base in the form of foreign assets. The goal was to reinstill confidence in the currency, which had been severely weakened following a decade of hyperinflation, as attested to by the growing dollarisation of local transactions. However, in addition to bolstering the credibility of the Argentine currency, the Convertibility Law played a second more critical role. It formally laid out the primary objectives of the Bank: above all to preserve the value of the peso, and only secondarily to regulate the amount of money in the economy, to control the banking system, to administer reserves, and to act as the financial agent of the government. This change in mission accompanied by the freeing of the Central Bank from the auspices of the

[10] Jeremy Adelman, 'Post-Populist Argentina', *New Left Review*, vol. 203, pp. 65–91.

[11] Paul Beckerman, 'Central-Bank "Distress" and Hyperinflation in Argentina, 1989–1990', *Journal of Latin American Studies*, vol. 27, part 3 (Oct. 1995), pp. 663–82.

executive branch (particularly the Ministry of Economy), making it accountable only to Congress, reduced the ability of the Central Bank to be used by the government as the lender of last resort, thus forcing a '*de facto* coordination between fiscal and monetary policies'.[12]

It is precisely this constraint on the Treasury, with its implications for fiscal stability, that lies at the core of the success of the Law. It is difficult to quantify its overall impact on the economy, for in addition to the direct impact on inflation it also had the indirect, but perhaps more important, effect of lending credibility to the reform process as a whole. As such, the success of subsequent reforms cannot be judged indepedently of the Convertibility Law. There are, however, certain aspects of the economy on which the Law had both a direct and immediate impact. The most visible of these was the inflation rate, which by the end of the 1980s had spiralled to levels never before seen in Argentina, reaching a peak of nearly 5,000 per cent in 1989.[13] Following the change in monetary policy in 1991, however, inflation plummeted to an annual rate of 84 per cent in 1991 and 17.5 per cent in 1992.

The drop in inflation resulted in a rapid increase in the money supply, due in large part to the return of capital which had fled abroad in the previous decade. By some estimates, the amount of investments held by Argentines outside the country during the 1980s exceeded $50,000 million.[14] The monetisation of the economy as measured by M3* (domestic and dollar denominated) increased three-fold from June 1991 to December 1994, from less than $14,000 million to more than $55,000 million. As a share of GDP, M3* increased from less than seven per cent to roughly 19 per cent during the same period. This increase in the money supply was accompanied both by an increase in lending by the domestic financial system and a reduction in interest rates. Loans to the private sector increased from $14,300 million in June 1991 to just under $55,000 million in December 1994. This increase in lending was due in part to the direct effect of the reduction of inflation on the return of capital to the country and indirectly to the increased confidence in the financial system that it instilled and which allowed for the reduction of bank reserve requirements from 79 per cent on checking account deposits to 43 per cent.

As such, from the point of view of the firm, one of the most immediate impacts of the drop in inflation was an increase in the amount of capital

[12] FIEL (Fundación de Investigaciones Económicas Latinoamericanas), *Indicadores de Coyuntura: Número Especial*, no. 350 (Oct. 1995).

[13] Ministerio de Economía y Obras y Servicios Públicos, *Argentina en Crecimiento: 1996–1990*, vol. I (1995).

[14] Felipe de la Balze, *Remaking the Argentine Economy* (New York, 1995).

in the domestic financial system available for loans. However, while the level of capital in the economy has increased, the ability to access it varies dramatically by firm. The opening of the capital markets has been accompanied by a shift in their composition. Government banks are playing a smaller and smaller role, being replaced by private lenders, both domestic and foreign. The clientèle which these private banks serve, however, tends to be different from that of the government banks. Small and medium-sized firms depend on government banks to a much greater degree, while larger and international firms tend to be customers of private banks. As such, changes in the capital markets appear to have benefited larger firms at the expense of smaller ones.

In addition to its economic impact, the reduction in inflation has had organisational effects on the way in which firms operate. Over the previous decade firms were forced to operate in an environment in which relative prices between capital and labour were constantly changing as a result of differential inflation rates. As such, even if firms were able to access funds during this period the decision on whether to invest them in labour or physical capital was not clear cut. As such, the result was that even firms which were able to access capital refrained from domestic investments. The inflationary environment of the 1980s forced firms to be short-sighted for fear of increased future instability. Following the stabilisation of prices, however, firms were able more accurately to determine relative prices and as such make the investment decisions which had previously been unclear.

Fiscal reform

On the fiscal side, two key laws were enacted to bring about structural reform. The first of these, the Economic Emergency Law (1989), suspended virtually all subsidies to the private sector and reduced extraordinary government expenditures (e.g. industrial promotion arrangements, regional subsidies). The result has been a balancing of the budget which in turn has aided the reduction of interest rates. The second of these laws, the Government Reform Law (1989), set up the regulatory framework for the transfer of firms and assets from the public to the private sector.

Privatisations have since affected over 60 state-owned firms, totaling $26,000 million worth of net assets, and including such 'icons' as YPF, ENTel, Aerolíneas Argentinas, and Gas del Estado. In addition to replenishing the coffers of the government and reducing the need for subsidies, it was hoped these privatisations would help raise the level of productivity of these enterprises and the economy in general. While this was not always the case, the general level of labour productivity of the

Table 1. *Argentine trade reform: tariff rates*

	Oct. 1989	Oct. 1990	Oct. 1991	Nov. 1992	April 1994	April 1995
Average tariff (%)	22.3	17.3	9.3	10.2	9.1	11.6
Dispersion[a]	12.9	5.4	8.9	5.1	5.7	7.2
Maximum tariff (%)	40.0	24.0	35.0	20.0	20.0	32.0
Most frequent tariff (%)	37.0	24.0	na	na	na	10
Average statistic tax[b]	na	3.0	3.0	10	7.2	2.4

[a] Dispersion is defined as the standard deviation of tariff rates.
[b] The statistic tax is an additional tax beyond the tariff which was originally imposed to reduce imports from Brazil but which as part of the Mercosur agreement is to be eliminated.
Source: Ministry of Economy.

economy increased by an impressive 26 per cent from 1991 to 1994, due in part to lay-offs and capital investments and in part to the application of better organising practices.[15]

Trade and regulatory reform

In the realm of trade policy many changes have been undertaken to open up the economy to foreign markets. In addition to the completion of the Mercosur agreement, which liberalised trade between Argentina, Brazil, Uruguay and Paraguay, there has been a general trend towards reduced protectionism in recent years. As can be seen from Table 1, the average and most frequent tariffs have both been reduced substantially since 1989. As one can also see, however, while the general trend has been one of reducing protectionism, this has not always been linear in its evolution, particularly in the case of the statistic tax. As such, while the economy is much more open today than in the late 1980s, signs of hesitation in tariff policy may have discouraged even further investment in the economy.

In addition to trade liberalisation, many of the internal markets in the country have also been deregulated, including energy, communications, and transportation. While changes in all three have had an impact on the competitiveness of the country *vis-à-vis* foreign markets, that which seems to have had the most immediate impact for exports is deregulation of the transport sector. With the privatisation of many of the road systems and the opening up of markets to competition, land transportation costs have dropped substantially. The cost of shipping products from Mendoza to São Paulo, for instance, fell by 30 per cent from October 1990 to January 1994.[16] Furthermore, ocean freight prices have also fallen dramatically, in

[15] FIEL, *Indicadores de Coyuntura: Número Especial*, p. xv.
[16] Ministerio de Economía y Obras y Servicios Públicos, *Argentina en Crecimiento: 1995–1999*, vol. VI (1995), pp. 30–60.

part as a result of a depressed international shipping market, but also as a result of deregulation of the port system. Taxes were reduced, ports privatised, and competition opened. This has resulted in reductions in ocean freight charges of over 50 per cent in many instances according to the Comité de Conferencias de Fletes.

The impact of monetary, fiscal, trade and regulatory reforms has begun to be felt. From 1990 to 1994 the economy grew by over 30 per cent, a growth rate outpaced only by China and Thailand. Furthermore, gross investment as a share of GDP increased from under 15 per cent in 1989/90 to 21 per cent in 1993. Concurrent with these results have been increased levels of inward FDI, challenging Mexico as the largest Latin American destination.[17]

The impact on internationalisation: the national level

The reforms discussed above have had a significant impact on the level of internationalisation of the Argentine economy. While still far below the level reached 60 years ago, the coefficient of openness of the economy has increased to nearly 9 per cent from a low of five per cent in early 1989. During the 1989–94 period, Argentine exports increased 65 per cent to reach levels of $15,000 million, and are projected to have reached levels of more than $22,000 million in 1995.[18] More dramatically, imports increased from $4,200 million in 1989 to $21,500 million in 1994 (an increase of 413 per cent), due in large part to the release of pent-up demand following the dropping of tariff barriers and the growth of the domestic economy. (Fig. 1).

While increased exports were one of the desired objectives of the market liberalisation programmes, the aggregate trade figures tend to mask certain underlying structural changes, which affect not only Argentine exports, but also the overall make-up of the economy. Among the most important changes since the opening of the economy in the late 1980s has been a redistribution of resources within the country towards what are generally considered to be lower value-added products. As a result, the nation has seen a disproportionate growth in the exports of primary products and energy in lieu of higher value-added agro-manufactured and industrial products. Whereas in 1989 products with relatively low value-added contents accounted for roughly 25 per cent of exports, in 1994 they had grown to account for 34 per cent. This trend is even seen within each general category. In energy exports, for instance, which are dominated by YPF (the formerly state-owned oil company),

[17] UNCTAD, *World Investment Report 1995*, p. 393.
[18] FIEL, *Indicadores de Coyuntura: Número Especial*, p. xviii.

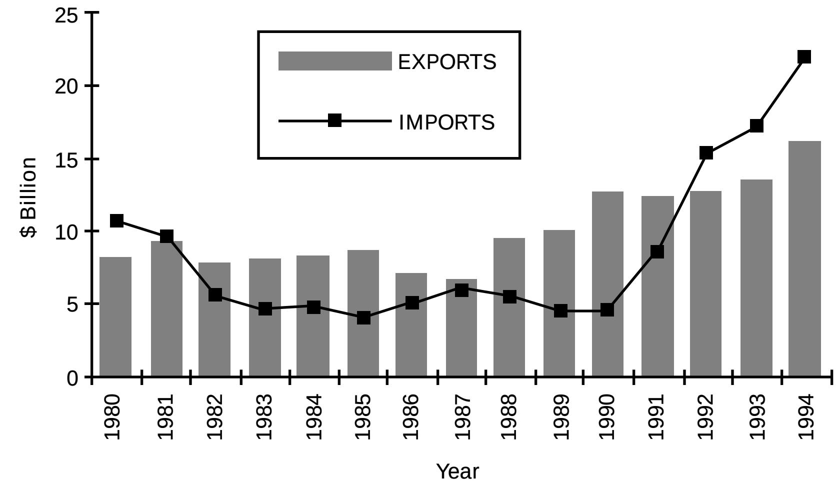

Fig. 1. *Argentine foreign trade. Source*: Ministry of Economy.

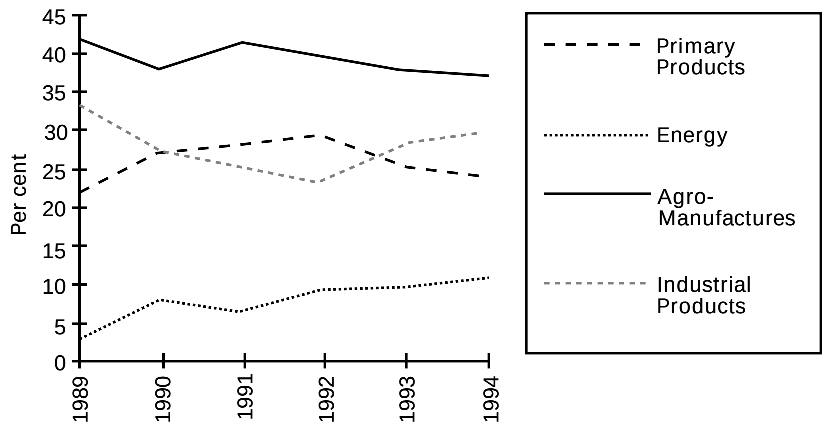

Fig. 2. *Argentine exports by type of product, 1989–94* (*as a percentage of total exports*). *Source*: INDEC.

there has been a shift from refined products to crude oil exports and natural gas. Whereas the latter represented 26 per cent of exports in 1992, by 1994 that share had grown to over 61 per cent.[19]

It is perhaps too early to tell whether this is a long-term trend, as there are signs that it may be moderating. Industrial exports did in fact make up some lost ground between 1992 and 1994, as indicated in Figure 2. Nearly 45 per cent of this recovery in industrial exports, however, is attributable to the sale of motor vehicles and parts to Mercosur, a trade promoted by a special regime requiring balanced exports and imports between the trade

[19] YPF, *Memoria y Balance, 1994* (Buenos Aires, 1995).

Table 2. *Level of value added of exports (%): Argentina*

	1989	1994
Low value-added	24.9	33.9
Primary products	21.8	23.6
Energy	3.1	10.3
High value-added	75.1	66.1
Agro-manufactured products	41.8	36.7
Industrial products	33.3	29.4

Source: Ministry of Economy.

pact signatories. Unfortunately, the backward linkages into the general economy which the auto sector provides are relatively weak, as it is dominated by foreign players, whose Argentine facilities are for the most part production and assembly oriented. The research and development and other higher values activities of these firms are located outside of the country, thus reducing the potential benefit normally associated with industrial exports. Furthermore, an additional 15 per cent of the increase in industrial exports is due to a growth in precious metals and their transformation, a sector with relatively low levels of industrial value-added.[20]

Much research has pointed to the level of value-added of a country's exports as a sign of the degree of economic development (Table 2). Countries which are dependent on the export of raw materials and commodities not only miss out on the potential to capture value-added rents, but are also subject to the higher degree of volatility found in commodity markets. Using cross-national data for the 1970–89 period, Sachs and Warner have shown that an inverse relationship exists between GDP growth rates and natural resource exports.[21] In the case of Argentina, this is an issue of central concern, given the high degree of dependence on relatively low value-added exports. While it may be claimed that Argentina is simply adhering to a path dependency argument by exporting products based on its natural resources, it should also be noted that the country has the best educated population in Latin America, a resource which such exports do not exploit. Furthermore, even if path dependency is applicable, the point being made here is that these are changes that should be monitored as they can have a significant impact on the future structural composition of the economy.

[20] Ministerio de Economía y Obras y Servicios Públicos, *Argentina en Crecimiento: 1995–1999*, vol. IV, pp. 193–215.

[21] Jeffrey Sachs and Andrew Warner, 'Natural Resource Abundance and Economic Growth' (Cambridge, MA, 1995); also see Paul Krugman, 'The Narrow Moving Band, the Dutch Disease, and the Competitive Consequences of Mrs. Thatcher', *Journal of Development Economics*, vol. 27, nos. 1–2 (Oct. 1987), pp. 41–55.

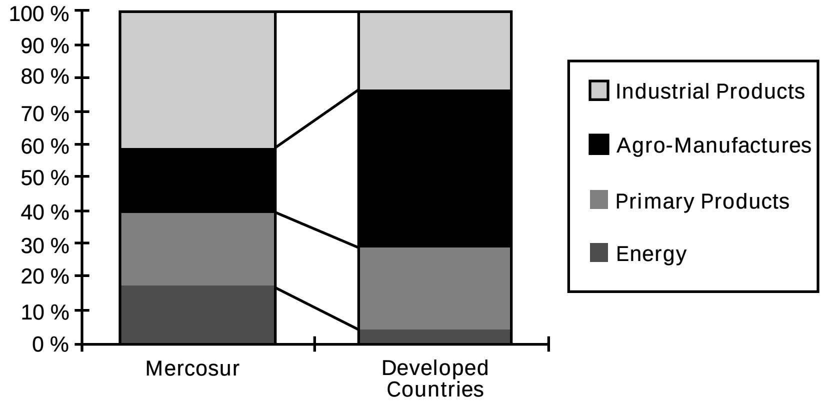

Fig. 3. *Composition of Argentine exports by area of destination. Note*: Developed countries defined as the USA, the EU and Japan. *Source*: INDEC.

In addition to the change in the composition of exports over the past five years, change in the destination of those exports has been in evidence, largely in part due to the growth in importance of Mercosur (Fig. 3). Whereas in 1989 Mercosur accounted for 15 per cent of Argentina's exports, by 1994 that figure had doubled to 30 per cent, with Brazil accounting for the lion's share. While this growth in trade with its neighbours was part of the purpose in establishing the bloc in the first place, it also entails potential drawbacks. The main threat is the fact that while Brazil is a large market with strong growth potential, it does not possess the sophisticated demand present in the United States, Europe or Japan. As such, competing in the Brazilian market does not necessarily force local firms to confront the leading edge in global competition. This trend is eventually self-reinforcing, for the longer one stays out of the leading markets the harder it will be to enter them in the future – particularly in the area of industrial exports in which technological advances are fastest. One already sees that, while in general Mercosur countries import more lower value-added products from Argentina than the developed economies, the one exception is industrial products. Again, much of these industrial exports relate to intra-firm transfers of the auto industry. And, while the developed markets still represent 39 per cent of Argentina's exports, that share has been decreasing with the growth in trade since 1989.

Although one should not ignore the economic incentives which compel firms to increase sales within Mercosur, one should also be conscious of what is occurring outside the bloc. One approach is to adopt a tapping procedure of selecting more advanced markets. By directly participating in these markets one can extract knowledge and information which can then be used to improve one's position in home and bloc markets. Such an approach differentiates the role each market serves in the firm's overall strategy. The importance of Europe, the USA, and East Asia, therefore, may not be due to their overall market size potential, but rather the learning which can arise through operating in those markets. It is for this reason that withdrawing from the more advanced markets could be harmful in the long run.

Certain researchers, including some economic growth theorists, claim that regional trading blocs can serve as testing grounds for eventual global integration, as they allow firms gradually to develop internationalisation skills. In many ways this argument is similar to the infant industry protectionist argument, in which barriers are used to protect domestic industries until they develop the skills necessary to compete internationally.[22] Unfortunately, such policies have a fairly poor record in Latin America. The same potential fate could lie in store for firms operating under the protection of Mercosur, wherein their level of competitiveness is confined to the demands and pressures of the Mercosur market, rather than the global one.[23] While it is still too early to tell whether firms are in fact viewing Mercosur as a launching pad, interviews with managers do not reveal such tendencies.

Another trend which has intensified over the past five or six years is the increased concentration of exports in the hands of a smaller number of firms. This is due in part to the general increase in concentration in Argentine industry as a result of enhanced, efficiency-based competition. However, the degree of consolidation in the export markets far surpasses that of the economy as a whole, implying that the trend towards concentration has been much more prevalent in the tradeable sectors.

For the economy as a whole, the largest 500 firms' share of GDP increased from 23.4 per cent in 1990 to 30.4 in 1994. By contrast the proportion of exports controlled by the 30 largest exporters increased from 32.6 per cent to 55.0 per cent during the same time period.[24] One of

[22] For further reading on this issue see: Richard Baldwin and Anthony Venables, 'Regional Economic Integration', in Gene Grossman and Kenneth Rogoff (eds.), *Handbook of International Economics*, vol. 2 (Amsterdam, 1995), pp. 1597–1644; Elhanan Helpman and Assaf Razin, *International Trade and Trade Policy* (Cambridge, MA, 1991); John Tomer, 'A New Rationale for Industrial Policy: Developing the Capabilities of the Learning Firm', *International Review of Applied Economics*, vol. 7, no. 22 (1993), pp. 208–22.

[23] José Bekinschtein, 'Apertura Externa y Patrón de Comercio: El Comercio Exterior Argentino y su Consistencia con el Escenario Global', in Bernardo Kosacoff (ed.), *Hacia una Nueva Estrategia Exportadora* (Buenos Aires, 1995), pp. 113–14.

[24] Calculations based on data published by *Mercado*: 'Ranking de las 500 Empresas Líderes' (Aug. 1991), pp. 41–64; 'Las 250 Empresas que Más Exportan' (May 1992), pp. 51–8; 'Las Empresas que Más Exportan' (April 1994), pp. 100–21; 'Las 1000 que más venden' (June 1995), pp. 119–79.

the potential explanations of exporter concentration is that while the economy is in the process of opening and exposing its firms to competitive forces to improve quality and costs, it is not a pressure which is felt uniformly throughout the country. There are still many sectors, insulated from the direct stimuli of tradeable markets, which have been slower to reform. The competitiveness of the non-tradeable sector, however, also has implications for the tradeable sector, as it provides many of the service inputs. As such, lack of integrated reform may inhibit the ability of the tradeable sector to expand its exports in the future.

A second reason for the rising concentration of exports is the disproportionate growth of primary and energy exports, which are typically accounted for by relatively few and large firms. The top 30 exporting firms are involved in one of four areas: petroleum, foodstuffs, steel products or motor vehicles.[25] In most cases, little value is added to the raw material being exported, with the only exceptions being certain steel products (e.g. seamless tubes), and motor vehicles and parts, whose recent export booms have much to do with a new requirement that imports be compensated by exports.[26] With the exceptions of YPF and the vegetable oil producers, the top 30 exporting firms are either controlled by foreign capital or by diversified local groups, in many instances with the assistance of foreign partners. The important trade in agricultural commodities, for instance, has become increasingly dominated by business groups and foreign multinationals because of their access to export market information and cheaper financing.[27]

Local business groups have clearly benefited from the process of economic reform. Their ability to take advantage of market, information and financing imperfections and to capitalise on their project execution capabilities, as suggested by the established theories of business group success in developing countries, has probably been enhanced, at least temporarily.[28] New opportunities have become generally available, but business groups have found themselves in a better structural and financial

[25] 'Ranking de Exportadores', *Prensa Económica*, no. 210 (June 1995), pp. 38–79.

[26] Roberto Bisang and Bernardo Kosacoff, 'Tres Etapas de la Búsqueda de una Industrialización Sustentable: Exportaciones Industriales Argentinas 1974–1993', in Bernardo Kosacoff (ed.), *Hacia una Nueva Estregia Exportadora: La Experiencia Argentina*, *el Marco Regional y las Reglas Multilaterales* (Buenos Aires, 1995), pp. 66–9, 78.

[27] Graciela Gutman, 'Cambios y Reestructuración Recientes en el Sistema Agroalimentario en la Argentina', in Bernardo Kosacoff et al. (eds.), *El Desafío de la Competividad* (Buenos Aires, 1993), pp. 337–78.

[28] N. Leff, 'Industrial Organization and Entrepreneurship in Developing Countries: The Economic Groups', *Economic Development and Cultural Change*, vol. 26 (1978), pp. 661–75; Alice Amsden and Takashi Hikino, 'Project Execution Capability, Organizational Know-How and Conglomerate Corporate Growth in Late Industrialization', *Industrial and Corporate Change*, vol. 3, no. 1 (1994), pp. 111–47.

position to exploit them. Most importantly, they have entered into numerous alliances with foreign firms, frequently as a result of becoming partners in privatised companies. Overall, 40 per cent of privatised equity has gone to foreign firms, generally in conjunction with an Argentine business group acting as the local partner.[29] These and other renewed contacts with foreign firms have helped the groups acquire technology, equipment and organisational and marketing know-how.[30] Not surprisingly, they are ardent supporters of the new, overtly liberal regulation (or lack thereof) concerning foreign investment.[31] The groups have seen their shares of total Argentine exports surge from about 15 per cent in the mid-1970s to more that 25 per cent in the early 1990s.[32] They are also among the most active Argentine firms in terms of outward foreign investment.[33] Unfortunately, several of the groups are active in low value-added activities such as oil (e.g. Pérez Compac, Astra, Bridas, Comercial del Plata) or agricultural commodities (Bunge & Born), while those active in manufacturing consumer goods are trying to reorganise and refocus (Alpargatas, Arcor, Macri). Some firms such as Techint (steel and seamless tubes) and IMPSA (heavy machinery), however, have shown that they can be successful at exporting high value-added products.

Foreign multinationals have also benefited from economic reforms, but one should differentiate between those linked to natural resources for export and others engaged in manufacturing for the domestic market. Overall, the multinationals' share of total Argentine exports has remained stable at around one third since the mid-1970s.[34] In a recent survey, Kosacoff and Bezchinsky[35] determined that the average manufacturing multinational in Argentina imports three times as much as it exports. Unfortunately, only five per cent of their imports have to do with capital equipment, with the rest evenly divided between inputs and final goods

[29] Adelman, 'Post-Populist Argentina'; Bernardo Kosacoff and Gabriel Bezchinsky, 'New Strategies of Transnational Corporations in Argentina', *CEPAL Review* (April 1994), pp. 135–9.

[30] 'El Poder de los Grupos Económicos en la Argentina', *Prensa Económica* (June 1994), pp. 35–66.

[31] Fundación Invertir Argentina, *Foreign Direct Investment in Argentina 1994–1995* (Buenos Aires, 1995).

[32] Bisang and Kosacoff, 'Tres Etapas de la Búsqueda de una Industrialización Sustentable: Exportaciones Industriales Argentinas 1974–1993', p. 85.

[33] Roberto Bisang, Mariana Fuchs, and Bernardo Kosacoff, 'Internacionalización de Empresas Industriales Argentinas', in Bernardo Kosacoff (ed.), *Hacia una Nueva Estrategia Exportadora: La Experiencia Argentina, el Marco Regional y las Reglas Multilaterales*, (Buenos Aires, 1995), pp. 175–229.

[34] Bisang and Kosacoff, 'Tres Etapas de la Búsqueda de una Industrialización Sustentable: Exportaciones Industriales Argentinas 1974–1993', p. 85.

[35] Kosacoff and Bezchinsky, 'New Strategies of Transnational Corporations in Argentina', pp. 142–4.

for sale inside Argentina. Thus far, economic reforms seem to have failed at stimulating changes in the traditional roles that multinationals have played in Argentina: exporters of low value-added primary commodities or manufacturers of price-inflated goods for the domestic market.[36] The evidence is that they devote few resources to technology development,[37] worker training,[38] or process and product quality enhancement, as indicated by the few multinational operations in Argentina which have obtained an ISO 9000 certification. It is, perhaps, too demanding to ask either the business groups or the foreign multinationals to totally revamp their long-standing managerial and organisational practices within three or four years of the inception of reforms. However, our point is that the changes in the economic behaviour of business groups and foreign multinationals since 1991, with a few exceptions, could constrain the long-term well-being of Argentina in the world economy.

The internationalisation of the Mendozan economy

While the trends discussed above are evident at the national level, they are more clearly identified at the provincial level: differences in geographic specialisation that might confound the results are reduced. Furthermore, there are a number of other advantages to not focusing solely on the national level, which tends to be dominated by Buenos Aires. The first benefit stems from the fact that the economic mix of Mendoza is more representative of the typical region in Latin America than is that of Buenos Aires. Firm size in Mendoza is also more characteristic, in the sense that the majority of the economy is comprised of small to medium-sized firms. Given the growing concentration of exports in the hands of fewer and fewer firms, it is important to understand how these smaller firms are adapting to changes in the market and the regulatory environment.

The Province of Mendoza occupies over half of the Cuyo region at the foot of the Andes to the North of the Colorado river, and accounts for about four per cent of Argentina's population and GDP.[39] The City of Mendoza's one million inhabitants make it the fourth largest in Argentina. Founded in 1561 by Spanish colonisers arriving from Chile, it lies about 600 miles west of Buenos Aires and 130 miles east of the border with

[36] Paul Lewis, *The Crisis of Argentine Capitalism*.

[37] Kosacoff and Bezchinsky, 'New Strategies of Transnational Corporations in Argentina', p. 147.

[38] Mariana Fuchs, 'Calificación de las Recursos Humanos e Industrialización: El Desafio Argentino de los Años Noventa' (Buenos Aires, 1994), CEPAL *Documento de Trabajo*, no. 57.

[39] CRECER, *Anuario 1992–1993: La Economía de Mendoza* (Mendoza, 1994).

Chile. A class of middle-sized farm and vineyard owners emerged in the second half of the nineteenth century occupying the flat, arid lands stretching east from the Andean sierra. The railroad reached Mendoza in 1885, allowing for increased immigration and improved transportation of goods to the markets in and around Buenos Aires. Wine production increased rapidly at the turn of the century, displacing alfalfa growing and extensive cattle breeding. The provincial government played a key role at this time in establishing the first technical training institutions and chemical testing laboratories for wines as well as improving basic irrigation infrastructure. The first mineral water, soft drink and beer bottling plants were established in the 1890s, while the mechanisation of vineyard and bottling activities resulted in the growth of metal-mechanic repair shops.[40]

New industries developed between the two world wars: processing and canning of fruit, vegetables, and olive oil; petroleum drilling; cement; and industrial alcohols. Glass and tin factories followed in the 1940s. By the 1950s Mendozan agroindustry and railways had generated a sizeable metal-working and machinery industry, which started exporting food-processing equipment by 1960. Contacts made with foreign firms allowed Mendozan firms to improve their designs of machinery.[41] A large petroleum refinery and petrochemical complex and several chemical plants, were established during the years of import substitution. By the mid-1980s primary agricultural activities accounted for a mere six per cent of Mendozan GDP, with industry/mining and services each representing about 46 per cent.

As with 22 of Argentina's 24 other provinces, Mendoza has experienced an impressive growth in trade in recent years. However, it still remains below the national average relative to its economic size. Mendoza saw its exports increase from $152 million in 1988 to $452 million in 1994.[42] This growth of almost 200 per cent, however, has been somewhat erratic, with exports rising rapidly until 1990, before falling for two years and eventually recovering in 1993. This drop in exports can be partly explained by the upturn in the economy in 1991 and the ensuing increase in domestic demand.

In relation to the rest of the country, Mendoza improved its export ranking among the provinces during this period from seventh to fifth place. However, exports are still below what might be expected on the

[40] José Antonio Borello, *From Craft to Flexibility: Linkages and Industrial Governance Systems in the Development of a Capital Goods Industry in Mendoza, Argentina, 1895–1990* (Buenos Aires, 1994), Working Paper no. 12, pp. 27–40. [41] *Ibid*. p. 78.

[42] Ministerio de Economía y Obras y Servicios Públicos, *Argentina en Crecimiento: 1995–1999*, vol. IV.

basis of the provinces show of national production. In this sense, Mendoza still lags behind the average, by nine percent when measured on a straight provincial average basis, and by 28 per cent when weighted by GDP.

While there has been an overall growth in Mendozan exports, this growth features many of the same underlying characteristics identified at the national level, among these the shift towards lower value-added products (Table 3). In the case of Mendoza, this trend has been more dramatic in one sense, but at the same time tempered by the growth of industrial exports. The province has always been, as has much of the country outside of Buenos Aires, an exporter of relatively low value-added products. However, in recent years, this trend has been accentuated still further. Whereas the relative share of low value-added exports has increased by nine percentage points in the country as a whole, they have experienced a growth of nearly 15 percentage points in Mendoza and now account for over half of the province's exports.

In contrast to the country as a whole, the province has witnessed a substantial growth in industrial exports, increasing from 19.5 per cent of the total in 1989 to 26.3 per cent in 1995. While this is encouraging news, if one looks behind the figures, one realises that another phenomenon is occurring. Much of this growth in industrial exports can be attributed to the export growth of one or two large firms in the metal-mechanic sectors, and not necessarily to increased exports by the entire Mendozan industrial sector. On the other hand, the production of these leading firms has been moving towards increased subcontracting. As a result, while these smaller suppliers may not export on their own, they participate in the internationalisation process indirectly through supplying intermediary components to exporting firms. Even though final goods exports may be concentrating, it does not necessarily mean that fewer firms are reaching international standards. In fact, this situation may prove to be a better internationalisation model than one in which all factors try to export, as it allows for greater product specialisation.[43]

While industrial exports have grown, the other group of higher value-added products, agro-manufactured products, have witnessed not only a relative but also an absolute decline in exports. From a high of $135 million in 1990, agro-manufactured exports dropped to barely $100

[43] Alberto Delgobbo and Hugo Kantis, 'Competitividad e Internacionalización de las PyMES Metalmecánicas, Estudios de Casos en la Provincia de Santa Fe' (Buenos Aires, 1991), CEPAL *Documento de Trabajo*, No. 27; Virginia Moori-Koenig, Gabriel Yoguel, and Francisco Gatto, 'Reflexiones Sobre la Competitividad de las Empresas PyMES en el Nuevo Escenario de Apertura e Integración, la Situación de Firmas Metalmecánicas' (Buenos Aires, 1993), Ministerio de Economía, *Documento de Trabajo*, no. IE/03.

Table 3. *Level of value added of exports (%): Mendoza*

	1989	1994
Low value-added	36.7	51.5
Primary products	15.0	22.7
Energy	21.7	28.8
High value-added	63.2	48.5
Agro-manufactured products	43.7	22.2
Industrial products	19.5	26.3

Source: Ministry of Economy.

million in 1994, with most of the decline coming from reduced processed fruit and vegetable exports. By contrast, exports of unprocessed fruits and vegetables have increased by a similar dollar amount, implying that the agro-industrial sector in particular has reacted to the market changes of the last five years by moving to lower value-added products, thereby revealing potential weaknesses in the international competitiveness of the sector. Even within agro-manufactured exports there appears to be a move towards lower value-added, witnessed by the growth of table wines over fine wines.[44]

The changes in export composition discussed above have taken place in the context of (and in some ways more pronounced) structural changes in the composition of Mendozan GDP. Since the mid- to late-1980s, the Mendozan economy has witnessed a considerable shift away from industry and mining towards what are generally classified as service industries (commerce, transportation, financial services, and social services). Together they have increased from roughly 40 per cent of GDP in 1986 to nearly 57 per cent in 1993. While agriculture has maintained its share of roughly 5.5 per cent, industry and mining have seen not only their share (from 46 to 29 per cent) but also their absolute value decrease.

During the 1989–93 period, the economy of Mendoza grew by 17 per cent in real terms. By contrast, the industrial and mining sector shrunk by 25 per cent and agriculture by 15 per cent. Even though the economy has seen a shift away from tradeable goods, as was mentioned earlier, exports have increased substantially, implying that the export intensity of the tradeable sector has increased even more than might be apparent at first glance. As Table 4 shows the export intensity of the agricultural sector has increased by a factor of 1.61 since 1989. Even more revealing is the increase in industrial export intensity, whose level in 1993 was 3.21 times that in 1989. Despite this relative growth in the export intensity of the industrial and mining sector, it still lags far behind that of the agricultural sector, which in 1993 had an export share of production more than nine

[44] Data provided by the Ministry of Exterior of the province of Mendoza.

Table 4. *Mendozan index of export intensities (1989 = 1.0)*

	Production (A)		Exports (B)		Export intensity (B/A)	
	1989	1993	1989	1993	1989	1993
Industry	1.00	0.75	1.00	2.41	1.00	3.21
Agricultural	1.00	0.85	1.00	1.37	1.00	1.61
Agriculture/industry	0.16	0.19	2.52	1.78	15.4	9.6

Source: Ministry of Foreign Trade, Province of Mendoza.

Table 5. *Top 10 exports from Mendoza ($ million)*

	1991	1992	1993	1994
Fresh garlic	54.1	36.3	48.0	48.0
Canned olives	21.7	15.1	22.7	26.5
Dried plums	9.4	6.6	9.2	15.0
Polypropylene	9.2	6.9	9.8	10.2
Leather	8.9	6.8	8.6	9.6
Bulk fine wine	7.6	7.5	8.7	8.6
Valves	0.0	0.7	0.4	8.0
Bulk table wine	0.9	1.1	3.1	6.1
Crane parts	1.8	0.2	19.9	5.7
Ethyl alcohol	3.5	2.5	4.9	5.4

Source: Ministry of Foreign Trade, Province of Mendoza.

times higher than that in the industrial sector (down from more than 15 times in 1989).

The implications which follow from this analysis support the conclusions arrived at earlier that the Mendozan economy, while in the process of changing, is still disproportionately dependent on the agricultural sector, and is moving towards lower value-added products for its export performance.

An analysis of Mendozan exports by product reveals a greater intertemporal consistency than alluded to when one looks only at the industry versus agriculture split (Table 5). If one excludes energy, the leading five or six exports have been relatively consistent in their ranking over the last four years. From 1991 through 1994 the leading export of the province was fresh garlic, followed by canned olives and dried plums. The variability which was mentioned earlier appears to come in large part from non-core exports of the province which have either made temporary inroads, such as crane parts in 1993, or others which have lost importance such as *mosto* (unfermented grape juice).

Another notable observation is that although the province is the heart of the Argentine wine industry (the world's fifth largest), exports of all kinds of wine products totalled less than $20 million in 1994. Furthermore,

Table 6. *Leading importers of Mendozan exports*

Products in which Brazil is the no. 1 importer	Products in which the USA, Japan, or Europe is the no. 1 importer
Fresh garlic	Fine wine
Canned olives	Retention valves
Dried plums	Parts for cranes
Canned peaches	Ferrous alloys
Onions and shallots	Apple juice
Fresh plums	Silicon manganese
Pears	Leather
Fresh apples	Calcium silicon
Olive oil	Bottled wines
Fresh grapes	Grape juice
	Tartaric acid

Source: Ministry of Foreign Trade, Province of Mendoza.

the majority of the modest growth during this period came in the form of increased low-quality table wine exports to countries such as Paraguay, as opposed to finer wines whose main export markets are the United States and Japan.[45]

With regard to country of destination for exports, Mendoza is even more dependent on the Mercosur market than the nation as a whole, with 45 per cent of exports heading for other Mercosur nations (versus 30 per cent heading to the United States, Europe and Japan). (Table 6). In contrast to the nation as a whole, however, one sees that many of Mendoza's higher value-added products are sold primarily to more advanced economies, implying that the industrial base which the province has is in fact competitive at international and not just regional levels. While Brazil is the leading importer from Mendoza of a whole host of raw or semi-processed agricultural products, the more sophisticated exports such as machine valves, crane parts, ferrous alloys and other metals have the USA, Japan and Europe as their main markets. Wine is another good example, in which the fine and bottled segments have the USA and Japan as their main markets while the growing segment, table wine, has Paraguay as its leading destination. Given the composition of exports, this trend towards increased trade with Mercosur will only serve to strengthen the shift towards lower value-added products and potentially weaken a currently competitive industrial base.

As alluded to in the title, the objective of this article is to probe beneath the aggregated trade statistics and observe the second-order trends whose impacts will be felt later. Until now, the discussion has been focused primarily at the industry and in some cases product level of analysis.

[45] *Ibid.*

Table 7. *Survey variables*

Category of variables	Specific variables	Definition
Internationalisation	EXPORT	Firm engaged in exports
	EXPORT%	Exports as a % of total sales
Firm demographs	LARGE	Over 80 employees
	FAMILY	Family ownership
	FOREIGN	Some foreign ownership
	FIRMAGE	Firm age in years
	MACHIND	Machinery-related industry
	AGIND	Agro-related industry
	CHEMIND	Chemical-related industry
Strategy variables	NQC	No quality control systems
	NOEDUC	Workers without qualifications (%)
	PROPDES	Possesses proprietary designs
	SUPPLY	Uses suppliers outside Mendoza
	COST	Future strategy: reduce costs
	QUALITY	Future strategy: improve quality
	CUSTOMER	Dependent on 1–2 customers
Government programmes	GOV1	Participation in commercial missions
	GOV2	Participation in credit programmes
	GOV3	Participation management training

However, in order to confirm the trends identified at these levels it is necessary to assess the changes in outward orientation at the firm level. To do so we rely on information from a survey conducted in 1995 by the Ministry of Culture, Science, and Technology of the Government of Mendoza covering roughly 200 firms in the province. The survey was undertaken as an effort to highlight common attributes of Mendozan firms and identify those factors which can impact on competitiveness.[46]

The survey included firms from all the major industries present in the province and covered a wide range of issues relating to firm demographics and strategies. Of more than 200 variables, a subset was selected for its potential relevance to a firm's internationalisation capacity. Two indicators of internationalisation were chosen. The first, EXPORT, states simply whether or not the firm exports any of its production. The second dependent variable, EXPORT%, is used only for the sample of firms which do in fact export, and is a measure of the export intensity of the firm (exports over total sales).

The model developed includes three sets of variables thought to affect firm internationalisation behaviour: firm demographic variables, strategic choice variables, and finally government programme variables (see Table 7). A logistic version of the model was estimated for the first dependent internationalisation variable, EXPORT, and a similar model was then

[46] We are grateful to Javier Espina and Verónica Linares for permission to use this database.

Table 8. *Regression results*

Variable	Parameter	Standard Error
Dependent variable: EXPORT		
LARGE	−2.8424	0.6621***
MACHIND	−0.2063	0.8199
CHEMIND	0.6893	0.9671
AGIND	2.9770	0.8787***
FIRMAGE	0.0026	0.0116
FAMILY	−0.1170	0.5541
FOREIGN	2.5256	1.3968*
NQC	−1.1883	0.9332
SUPPLY	0.8090	0.7062
NOEDUC	−0.0149	0.0090*
PROPDES	0.6903	0.5768
COST	0.0148	0.7080
QUALITY	0.5570	0.5693
CUSTOMER	0.7450	1.5413
GOV1	1.4529	0.5737**
GOV2	0.5646	0.6225
GOV3	1.3995	0.6183**
Constant	−2.3769	1.3980
Dependent variable: EXPORT%		
LARGE	−14.6727	6.6798**
MACHIND	20.4580	13.5978
CHEMIND	4.8518	16.6289
AGIND	2.8230	14.2533
FIRMAGE	−0.2890	0.1343**
FAMILY	−8.4044	7.3452
FOREIGN	−21.7632	13.6508
NQC	−19.3055	13.1205
SUPPLY	−13.4565	9.0760
NOEDUC	0.1148	0.1248
PROPDES	0.2246	8.0501
COST	−20.4774	8.0328**
QUALITY	3.1652	7.3884
CUSTOMER	35.4255	18.9230*
GOV1	9.0272	6.7040
GOV2	−15.5120	7.7381*
GOV3	9.6548	6.3568
Constant	52.8098	18.4071

$^{*}p < 10\%$, $^{**}p < 5\%$, $^{***}p < 1\%$.

estimated for the independent variable EXPORT% using linear regression.

As can be seen from Table 8 there were a number of variables that were statistically significant in predicting whether or not a firm would export. Oddly enough it turns out that large firms in the province are actually less likely to export than small or medium-sized firms as witnessed by the negative sign on the LARGE coefficient. This may be due to the fact that they have a dominant presence in the domestic market and do not see the need to go abroad, while smaller, less domestically entrenched firms see foreign markets as offering greater potential. Alternatively, what are classified as large firms here are in reality medium-sized ones that have neither the scale of truly large firms nor the niche markets of smaller ones.

Another key variable in predicting whether a firm will export is if it is part of the agrosector, in which case it will have a much greater likelihood of exporting. Mendozan-based firms in certain agriculture-related areas do enjoy a comparative locational advantage over firms in machinery, chemicals, or other industries: hence the positive effect. Other variables which tend to have a significantly positive effect on export likelihood include partial foreign ownership of the firm, and participation in government-sponsored commercial missions and management training. By contrast, firms with high percentages of uneducated workers are less likely to export, pointing to the importance of an educated workforce, even in low value-added industries. Two other variables, which are not statistically significant but which appear to be exerting an influence are the possession of quality control measures (NQC) and product research or design (PROPDES) capabilities. As might be expected, firms with no formal quality control systems tend not to export while those with design capabilities do. Taken together, these results tend to support the points highlighted earlier using industry-level statistics regarding the importance of value-added (associated with quality and education/training levels) in a firm's ability to be successful in international markets.

Similar results were found using EXPORT% as the dependent variable. Once again, large firms tended to export less on average than smaller firms, a result confirming the commonplace inverse relationship between firm size and export intensity. Older firms also tended to export less, a finding that reinforces the impression that the more embedded firms are in the domestic environment, the worse their export performance. Furthermore, firms in the machinery industry, if they do export, export more on average than firms in other industries, supporting the hypothesis that certain segments of Mendoza's industrial sector are in fact very competitive at the international level. By contrast, the agro-sector includes many firms which export due to the comparative advantage of the region but not many which export a lot, implying few competitive or firm advantages.

Conclusions

The main argument of this article has been that in order to assess completely the impact of a market liberalisation programme such as that which Argentina has undergone, one must look beneath the aggregate statistics and analyse underlying changes in critical market structure and organisational variables, changes whose impact will only be felt in the long term. On the surface, Argentina's liberalisation programme appears to have been quite successful. Comprehensive reforms of the nation's monetary, fiscal, trade and regulatory regimes have been undertaken, resulting in considerable growth in GDP. Furthermore, the objective of reintegrating the country into the world economy appears to be well underway. Trade levels have increased substantially, outpacing GDP growth in the 1990s.

The central argument being made here, however, is that while this growth has been beneficial for Argentina, it has been accompanied by certain other underlying trends which could potentially prejudice the country's long-term development prospects. The two main trends which are of greatest concern relate to the level of value-added being created in the country, particularly with regards to its exports, and the change in composition of its trading partners. As has been shown, there has been a trend in recent years towards greater reliance on exports with lower value-added content.

The second trend discussed in the article poses a similar threat to the long-term competitiveness of the Argentine economy. Growth in trade with its Mercosur neighbours, primarily Brazil, holds potential drawbacks, the main one being trade diversion away from more developed markets. As has been pointed out by other authors,[47] the level of competitiveness of a firm is directly related to the sophistication of the demand it serves. By moving more and more away from the leading edge markets, Argentina runs the risk of damaging its long-run competitiveness, as the demand pressures to improve quality and performance are weaker in these secondary markets.

Each of these trends was shown to operate both at the national and provincial levels in Argentina. Furthermore, firm level data provided additional support for the claim that those sectors which rely primarily on comparative advantage in natural resources are more likely to participate in foreign markets. The case of Mendoza also provides encouraging news in that its high-value added sector does in fact appear to be competitive at the international level. However, the challenge it will encounter, and one which the country as a whole has been failing to meet, is whether in the fact of changing trading pattern it will continue to maintain its level of competitiveness.

[47] Michael Porter, *The Competitive Advantage of Nations* (Newark, 1990).