

Costa Rican democracy reaps FDI rewards

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Costa Rica was once thought of simply as a 'banana republic', but in the past decade it has attracted impressive flows of foreign investment which have transformed its economy. Costa Rica now attracts about \$517bn., or 53 per cent of the total foreign investment in Latin America. Schuler and Brown (1999) argue that a major factor in attracting multinational corporations has been the country's political and institutional stability. Costa Rica has established a strong democracy with transparent institutions, competitive elections and a solid social welfare state. The Citizens' Audit on the Quality of Democracy 1998–2001 has produced evidence on the experience of democracy by citizens from all walks of life within the country (O'Donnell et al., 2004). The audit revealed high spots such as the electoral system, but also weaknesses, such as poor treatment of citizens by bureaucrats. In general, it brought to light that democracy is deeper than simply electing governments, but is about human rights, accountability of those in power and the rule of law. It highlighted the importance of social and economic inequalities in assessing the quality of political participation.

Costa Rica's biggest FDI success story has been Intel, whose chip factory now accounts for 37 per cent of the country's exports. Costa Rica was competing against Mexico for the factory, and both governments offered incentives. The Costa Rican government offered Intel tax-free status for eight years, followed by a 50 per cent discount for another four; a commitment to invest more in infrastructure and education; and a favourable regime on energy prices. Mexico offered enhanced incentives and had the advantage of lower wages than those in Costa Rica. Notwithstanding, Intel opted for Costa Rica. This evidence suggests the decisive role played by a strong democracy, along with membership in a number of international accords (such as GATT and WTO).

Schuler and Brown (1999) also argue that democracy seems to influence the way multinationals behave once they have settled in the host country. Lively democratic institutions and interest groups which represent and channel citizens' views can provide valuable feedback to the company and aid it in developing beneficial relationships with the community. For example, Ston Forestal, a US company which invested in a reforestation project in Costa Rica, changed the location of its planned chipping factory after environmental groups, mainly Greenpeace, had lobbied the government. The company then set up a multiparty watchdog group to monitor its operations. This development is indicative of Costa Rica's approach to conservation of its biodiversity through decentralized decision-making and localized management of protected areas.

How does Intel benefit Costa Rica? The company enjoys a tax holiday for eight years, and it brings 90 per cent of its supplies from abroad, as there is no local electronics industry. Still, the enthusiastic workforce at the new factory see the benefits of a constant education in the new economy. The agreement between the government and Intel provided for cooperation in developing new programmes for worker training. One twenty-something employee says chips are far more challenging than bananas, the country's other major export: 'Bananas will be bananas today and bananas tomorrow. When you're making chips ... you always learn something new.'


The Intel experience in Costa Rica indicates that the existence of robust democratic political institutions gave Costa Rica significant advantages in attracting investment. While the multinational company possesses significant bargaining power in its relations with governments, in that it has geographical mobility and ownership of the technology, states are in a position to build 'institutional comparative advantage', as Costa Rica has successfully shown.

Programme (UNDP) (2002) Human Development Report 2002; UNDP (2002) Human Development Report 2003; O'Donnell, G., Cullell, J. and Iazzetta, O. (eds) (2004) The Quality of Democracy (Notre Dame, IN: University of Notre Dame Press).

Case questions

Why does democracy reduce political risk for foreign investors in Costa Rica?

What specific lessons can multinational organizations learn from Intel's experience in Costa Rica which can be applied in assessing locations globally?

 Intel's website is at www.intel.com. The section on corporate responsibility details some of their Costa Rican links.