

Effects of fdi in the dominican republic



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Introduction

Background and purpose

The Dominican Republic has done a major shift in its economy, coming from an agricultural economy, to one based on services. An estimate of the sectors contribution to the country are, 60. 2% in services (tourism, transportation, communications, finances, others), 15. 5% in industry (manufacturing), 11. 5% in construction, 11. 3% in agriculture, and 1. 5% in mining (CIA fact book). As of right now only tourism leads the service industry, but is soon to be challenged by the investment of contact centers. Because of this shift in its economy the Dominican Republic has become home to various foreign investments, but the one this study will focus on is on the foreign direct investment in contact centers, or call centers as they are also known. It is important to explore the advantages the Dominican Republic offers to attract such foreign investment, as well as to analyze the fact that although there are benefits, it could also lack the necessary infrastructure to sustain this rapidly growing industry.

Due to the ongoing world financial crisis, many international companies are struggling to keep their business afloat and looking to establish their contact centers outside of their home based countries. Saving money and reducing operational cost are some of the main reason companies move and do foreign direct investment (FDI) abroad. Investing and conducting operations overseas seems to be the answer that foreign contact centers are looking for in order to meet such goals. It can be said that the Dominican Republic offers an answer to the difficulties contact centers companies are experiencing and continue to confront back at home. Some of the solutions given to these

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companies are a great business climate for foreign direct investment (FDI), incentives and good geographical location, among other compensations. As a result of moving abroad contact centers gain a particular advantage over their competitors. These advantages can range from cheaper operational cost, strategic location and skilled personnel, to a variety of options which may or may not be available in the Dominican Republic. But like everything in life not everything is perfect, the country also needs to confront a sad reality, which is that although it offers “ good things” to investors, it also lacks of other “ good things”.

This study will provide the key aspects of contact center FDI in the Dominican Republic in order to present some of the weak and strong points the country has on this industry. By doing this the report looks at what the country has to offer to current and future investors in the contact center industry. It will also provide-from the investors’ point of view-what makes the Dominican Republic an attractive place to invest foreign capital in contact centers, as well as some of the problems encountered throughout the business venture. Although information provided by the governmental institutions in charge of spreading information about this industry say “ the country is capable, suited and ready to meet all the requirements of international investors”, it is a fact that no system is perfect. This is where facts will be laid down in order to show what truly attracts, keep or loses these investments on the island. Based on those previously mentioned facts the study will look at what improvements can be made by the country in order to keep a competitive edge on the rapid growing industry.

With this information the reader will comprehend the flaws in the system, and what measures are needed in order to correct them and generate a more positive investment climate. Along with this positive investment climate the study will show the impact call center FDI has had in the country. An efficient and effective investment climate can only be produced by pointing out the pros and cons of what the Dominican Republic has to offer to its investors. The conclusion of the study wishes to convey that these improvements can be achieved by taking action upon the recommendations given. Being that this study is based mostly on empirical knowledge, some of the observations made will be presented based on the industry expertise of the writer of over 7 years or working experience in this field.

Research questions

Is the Dominican Republic a good place for FDI?

Have contact centers FDI created a real impact in the Dominican Republic?

Research methodology

In order to answer the questions mentioned above, this paper we will use a mixture of methodologies in order to analyze if the country is truly a good place for contact center FDI and if the industry has had an impact in the Dominican Republic. These methodologies include interviews, qualitative research and quantitative data.

Organization of paper

This document will be composed of four chapters, the first one being its introductory part. The first chapter will provide a brief introduction and background of the Dominican Republic and what sectors comprise the FDI in <https://assignbuster.com/effects-of-fdi-in-the-dominican-republic/>

the country, along with the research questions and research methodology. The second chapter will present an overview of foreign direct investment, inflows, trends, performances and investment climate that pertains the country, as well as the promotion agency in charge of FDI in the country. This information will be in comparison with selected economies from the Caribbean, Latin America and others. The third chapter will cover a more in-depth analysis of contact centers in the Dominican Republic, flaws and investor perspective. The study will also look at a specific company from which the study will depict the impact this specific center has had in the country. The concluding and fourth chapter will provide key findings from the study and recommend future improvements based on those findings.

Overview of FDI in the Dominican Republic

FDI trends and performance in Dominican Republic

The Dominican Republic, like many other developing countries, is actively seeking to attract FDI. They are not only seeking FDI as an important factor in creating employment opportunities and additional source of income, but rather for the reason of potential spillovers of knowledge and technology. The strong public support for FDI in the Dominican Republic is expressed through the creation of the Center for Exports and Investment of the Dominican Republic, institution in charge of all exports and investment, along with other measures taken by the government. Some of these measures include simplification of administrative procedures, aid from the CEI-RD in logistics and information, subsidies, tax breaks, exemptions and other instruments that facilitate FDI. Before addressing the question of whether FDI in the Dominican Republic has led to development, spillovers of

knowledge and technology, as well as, if it is a good place for contact centers to establish and invest, the study will provide an overview of FDI inflows and trends in the Dominican Republic.

FDI inflows in the Dominican Republic have made a miraculous recovery from 2004 to 2008 according to the data by the World Bank (World Bank, World Development Indicators). As any other developing country, the inflow of foreign capital was affected by the political environment, which reflected in an average loss of almost 200 million dollars per year during the 2000-2004 governmental period. During this period the collapse of a major bank caused financial turmoil and many investors were forced to leave the country. After a change of government and the macro stability was placed back in track by the new authorities, the country received an average foreign capital inflow of 450 million dollars a year, to earn a total of over two billion dollars in FDI inflows (See figure below). This great recovery happened during the 2004-2008 period, as it was first mentioned, and it is still improving as the country keeps positioning itself as a preferred destination for FDI. Although contact centers are not the main reason for this fast recovery in the FDI, the new rapid industry of contact centers are playing a very important role as it continues to evolve into a leading industry in the service field.

In President Fernandez first governmental period (2004-2008) the country recovered from the worst financial crisis in many years. During 2005 the country predicted a GDP growth of 9.3% and inflation to be brought under control at 7.3% throughout the 2004-2008 years. By managing these issues President Fernandez said “ We have rescued the confidence of investors by

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achieving macroeconomic stability” (Leonel Fernandez, 2004). Having achieved macroeconomic stability, the Dominican Republic received US\$1 billion worth of foreign direct investment (FDI) in 2005, up 40% from 2004, and U. S. investment accounted for around 40% of the total (CEI-RD, 2006). This led to an improvement of FDI inflows and mechanisms to continue attracting and sustaining this newly found investments. Below are the net inflows of FDI for various Latin American and the Caribbean countries, including the Dominican Republic.

Investment climate

When one thinks of the Dominican Republic, images of tropical beaches and all-inclusive resorts may come to mind, but this ten million-strong nation, occupying two thirds of the Caribbean island of Hispaniola, also has one of the Americas’ fastest growing economies and diverse scenery in the Caribbean (BusinessWeek, 2006). The briefing paper “ Foreign Investment in Latin America and the Caribbean”, 2008 is one of the latest editions of a series issued annually by the Unit of Investment and Corporate Strategies of the Economic Commission for Latin America and the Caribbean (ECLAC) Division of Production, Productivity and Management. This report presents-in a very detail manner-the foreign investment done in Latin American and Caribbean countries, showing their relative differences and investment climate among other indicators. This report also touches on the contact center industry, which has contributed greatly to the ever increasing FDI inflow of the Dominican Republic. Comparing to other countries the Dominican Republic shows one of the best FDI inflows by reflecting a relative difference of 83%. What this means is that FDI activities has been constantly

growing in the country, thus reflecting good initiatives from the country and a positive improving investment climate (see image below).

A good investment climate is not created by simple marketing; it takes hard work, good economic policies and first-class governance on behalf of the government and its Head of State. Because many countries offer desirable investment conditions companies frequently ask themselves, where they should invest their capital. The answer needs to be provided by the country that wishes to be the host of the foreign investments these companies wish to make. The Dominican Republic has characteristics that make it a desirable place to make an investment of any kind, but the question that still lingers around is if the country can really sustain an investment of great magnitude. Offering the right investment climate in the Caribbean is something that the country wishes to achieve, but is not always successful on doing so. With a long history of attracting considerable FDI in a variety of sectors, the Dominican Republic is a regional leader in attracting contact center foreign investment. Longstanding political stability and a diversifying economy have led many foreign firms to choose the Dominican Republic as an investment destination. Recent success in attracting FDI is due to the country's investor-friendly legal regime, generous incentives, and infrastructure capable of supporting new technologies, including information technology (FDI Magazine. Financial Times Magazine. August 2005). As mentioned earlier, this success is fairly new and the Dominican Republic still faces the challenge of maintaining and attracting this foreign investments.

A great way to see how well positioned is the country and the investment climate it offers is to do a comparison of economies. “ Doing Business 2010:

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Reforming Through Difficult Times” is the seventh in a series of annual reports investigating regulations that enhance business activity and those that constrain it. The report presents quantitative indicators on business regulations and the protection of property rights that can be compared across 183 economies, from Afghanistan to Zimbabwe, over time (Doing business, 2010). Looking at this specialize report the Dominican Republic reflects its ranking in ease of doing business and other important world ranking criteria’s that foreign investors consider necessary to know before investing in any. Although this report is using specific economies, the data compares the Dominican Republic to the economies of countries around its region, as well as others from a distant hemisphere and much more developed than the island.

One basic criterion for investment is the ease of doing business, the chart below reflects a clear weakness for the Dominican Republic in this area by ranking lower than a Puerto Rico and Jamaica. Puerto Rico and Jamaica are much smaller countries, which may contribute to more agile processes, but the fact that they are neighboring countries there should be a bigger similitude among them in terms of how business is handle. This is a clear sign that depending on how a country handles its business will reflect how efficient their mechanisms are, therefore providing a bigger ease of doing business. Another factor that should not be of much importance is the fact that Jamaica and Puerto Rico receive assistance, guidance and at times are regulated by developed countries. This should not be an excuse for why the Dominican Republic is falling behind in such a basic and important principle. (Doing business, 2010).

The chart below, which has also been extracted from the “ Doing Business 2010: Reforming Through Difficult Times” Report, touches on another very important factor for investors when they consider making an investment abroad. The ranking given in this chart is compared to the selected economies of Haiti, Puerto Rico, Singapore, Rwanda and others. This comparison is done once again in order to show how the Dominican Republic presents itself as a favorable investment location. Yet again this favorable climate for investors is not providing the best climate because is falling behind to neighboring economies which only advantage seems to be a more organize and efficient system. The Dominican Republic continues to improve, but is weak in its bureaucratic process, which as a result continues to slow down its progress.

Dominican Republic’s ranking in doing business

(Doing business, 2010)

Once an investment is done, one of the biggest-if not the main concern of any investor-is how secure is their investment in a foreign country, meaning how are they protected from any unwanted situation. The Dominican Republic has recently passed a new legislation which provides a greater protection to its investors, thus providing investors with a contingency plan if anything happens. The graph below shows the global ranking of the Dominican Republic in terms or protecting its investors, which is a great improvement from other areas already mentioned. Although this is a very important concern for investors, it still addresses a post-investment situation. What this mean is that it does not really provide an immediate impact in attracting a foreign investment if the other factors are

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encouraging, but it does boost investors confidence in the country they plan to invest as well as adding to a better investment climate.

(Doing business, 2010)

In an interview to CEI-RD Minister Eddy Martinez in the renowned Dominican daily show “ Hoy Mismo”, transmitted by channel 9, he talks about the investment climate in the Dominican Republic and mentions key factors that make the country a great place to invest-compared to other countries in the region. He talks about establishing incentive mechanisms in order to attract those capitals which appraise the value of the investment not only for the amount, but for the impact these investments will have in terms of technology transfer, creation of employment, type of employment, quality of products produced in the country and if they will carry out Research & Development activities. Although this mechanism is something the country wishes to implement, it is still not fully incorporated, thus leaving room for error. The institution is still trying to educate and integrate the contact center community so they can share these incentives and goals with other investors who want to do future business based on the country incentive structure.

To disseminate this information the CEI-RD has done seminars concerning these incentives, and is moving forward to the implementation of those incentive policies. During the interview CEI-RD Minister mentioned that many investments come through different ministries, therefore many investors are not sure who and how their investment are handle. This reflects a clear disorganization in the governmental mechanisms, which translates into a

weakness. Minister Martinez suggests the government creates an “integrated mechanism of investment”. What this means is that no matter the origin of the investment or ministry, it will end up in a single place. This will allow proper follow up of the investment, and in case a project gets stuck, the institution can determine where being detained due to bureaucracy or lack of project handling. Based on that integrated mechanism the country can increase its FDI inflows by having all projects in a single place, thus providing one more reason to invest in the Dominican Republic.

Promotion agency (CEI-RD) and incentives offered

The Dominican Republic’s government has implemented a liberal framework for attracting FDI. It makes no distinction between foreign and local companies in terms of ownership restrictions and ability to qualify for investment incentives. Foreign investment is permitted in all sectors except those related to public health and the environment (such as storage and disposal of hazardous or radioactive waste), as well as national security. The Dominican Republic government also offers full exemption from all taxes, duties, charges, and fees that affect production and export activities in free trade zones, which it introduced in 1969. The free trade zones aim to attract high-tech manufacturing (including electronics and electrical components) as well as more traditional manufacturing-such as of automotive parts, medical devices and pharmaceuticals, plastics, metals, injection molding, textiles and footwear, jewelry, tobacco and of course contact centers. The incentives offered last up to 25 years for zones on the Haitian border, and up to 15 years for all other zones. In May 2006 there were 59 industrial parks and free trade zones in the Dominican Republic, hosting more than 600 companies,

providing over 190, 000 direct jobs, and occupying 2. 1 million square meters. Although there are no performance requirements for foreign investors, few sector-specific incentives are offered to them. (World Bank Group, MIGA, Snapshot of the Caribbean, 2007)

All of the benefits mentioned above and the continuing inflow of investment is happening thanks to efforts from the government and the institution in charge of carrying out FDI promotion. The institution carrying out this very important task is the Dominican Republic's Export and Investment Center (CEI-RD), which is headed by Eddy Martinez, as the Minister and Executive Director of this government institution that promotes national strategic export and foreign investment opportunities and works hands-on with local and foreign enterprise to facilitate business activity. Because the institution knows the importance of investment they are aggressively targeting investors through offices in New York, Miami and California, and because of the nation's entry into the Central American Free Trade Agreement, or CAFTA-DR. The Centro de Exportación e Inversión de la República Dominicana (CEI-RD) as it is called in Spanish, is the country's one-stop investment promotion intermediary. It has three main departments: Export Promotion, Investment Promotion, and a Training Center. The CEI-RD aims to strategically promote the valuable conditions that the Dominican Republic offers as an investment destination and foreign trade developer, by pursuing priority areas as defined by the Government, to increase employment, technological transfer and the social welfare of the Nation. The agency organizes and participates in trade missions both overseas and locally as

well as provides tools to assist investors, such as an export directory. (World Bank Group, MIGA, Snapshot of the Caribbean)

The CEI-RD is the official organization responsible for the promotion of international trade and Foreign Direct Investment (FDI). It was created as a product of the fusion of the Center for the Promotion of Exports of the Dominican Republic (CEDOPEX) and the Office for the Promotion of Investments of the Dominican Republic (OPI-RD), according to Law 98-03, effective on June 17, 2003. The CEI-RD is comprised of two main operational areas, export promotion and foreign investment promotion and its functions include many promotions, but some of the more relevant to this study are promotion of the country's advantages to attract foreign investment, coordination with other government institution related to foreign trade in the interest of achieving an expedient and efficient flow of exports and investments in the country, promotion and development of FDI and business from the CEI-RD offices abroad, currently in Miami, New York and Chicago, participating actively in trade negotiations and administration of resulting agreements, contribute to the improvement of the legal framework and its proper application. Also throughout the Foreign Service network, new offices will be opening soon in Puerto Rico and Silicon Valley

The institution services are available for local and foreign companies to facilitate the exports and investments of the country which is an advantage to any investor. Among the services the CEI-RD offers, and which are relevant to this study, they have specialized consulting, technical assistance in meeting the regulations and norms required for the export of goods and services, which is helpful to new investor who are not familiar with the legal

framework. They also have validation of certificates of origin, technical assistance relating to trade agreements, recommendations for improving the production process and benefiting from tariff preferences. The new investor can also benefit from visits on behalf of the CEI-RD specialized staff to their companies in order to evaluate the production process under trade agreements and preferential programs. One very important service the CEI-RD offers is that they ensure the correct application of norms relating to export and investment procedures by administrating Law 84-99 on the reactivation and promotion of exports and Law 16-95 on foreign investment. Other services, although not specific to the industry, offered by the CEI-RD and from which investors could benefit are product profiles and market analysis, business intelligence, legal and economic information, registration of exports and foreign direct investment, facilitation of a network of representatives abroad and foreign trade documentation center.

As any other promotion agency the CEI-RD has several promotion programs that make the Dominican Republic attractive for FDI. These programs include National and International Trade shows and expos where it presents companies, local and foreign, can showcase their products. The CEI-RD also coordinates trade missions in order to ensure a successful transaction as well as training programs relating to international trade. In these specific programs-relating to international trade-local companies can get educated and learn how to export their products and foreign investors can learn about the local market and opportunities. Another very important promotion program-and the one of the most significant-is the coordination of business meetings to present what the country's has to offer, as well as to contact

potential investors and exporters. With this two-way program, foreign and local investors will have a mutual gain by making the necessary contacts to get their business started, thus generating future FDI. (CEI-RD, 2010)

Contact center FDI in Dominican Republic

Overview of contact center FDI

As it was previously mentioned, this study looks at the pros and cons of contact center FDI from various angles, one been from the host country point of view and the other the investor's point of view. From the host country the study takes into consideration a report created by the economist Jonathan Aragonéz, from the Center of Export and Investment of the Dominican Republic (CEI-RD), as well as other documentation of contact centers from the CEI-RD. These documents will provide the necessary data to point out the country's benefit and disadvantages. Do to the lack of published papers that truly criticize or analyze the contact center industry, this study will support many of its facts on three things. These three key contributions are empirical knowledge of the writer, interview conducted to the economist previously mentioned, and interview with a contact center owner who is doing FDI in the Dominican Republic.

The Dominican Republic has had strong export services for many years, and as a result there are 40 to 50 call centers registered with the Dominican Call Center Association. Investors currently operating in the country cited skilled workers, most of whom are bilingual, as their main reason for choosing it as their investment location (Dominican Republic Contact Center Association, 2010). The country has a large, well-trained labor force and although Spanish

is the country's official language, investors can find workers that also speak English.

“ Apart from the stable, fast growing economy, attractive cost structure and “ near shore” location, it can be said that people are the primary competitive advantage in the Dominican Republic. Investors in the Dominican Republic always emphasize the Dominicans high learning ability and proficiency in English”. (Eddy Martinez, 2006).

The country's large size means that land is available for green field investment-if one was to be done-although most investors opt to rent or lease a work space for their operations. The country also offers great access to all markets being that is one of the six countries in the world that has a free trade agreement with the U. S. and Europe. Some of the other countries that have such a privilege are Israel, Jordan, Chile and Mexico (Office of the United States Trade Representative, 2010). Other favorable investment factors included the country's well-developed, affordable telecommunications infrastructure which is the only one in the Caribbean with access four international cables through the Americas Region Caribbean Optical-Ring System Cable (ARCOS-1). What this means is that the Dominican Republic connection to the U. S. or any other country is redundant, thus ensuring contact center businesses to always be connected.

Contact centers in the Dominican Republic generate 25, 000 direct jobs, from the 57 companies registered and operating in the country. In the next two years those centers are expected to create 30, 000 additional jobs, which when added to the indirect ones are more than 150, 000 in. This information

comes from the CEI-RD, which also says almost all of the data and information technology centers have been installed in the country in the past three years, meaning this great progress has been done in record time. This year alone-and not including centers outside of free trade zones-Contact Centers constituted 15% of approved companies in the free trade zones of the Dominican Republic, being matched only by textile companies (Approved companies by the Free Trade Zone and Export Committee, 2010). In previous reports the committee also shows how these companies add to the country's GDP year after year, reflecting in a steady and secure growth of this industry.

Companies approved in 2010

Free Trade Zone and Export Committee, 2010)

The contact center industry in the Dominican Republic is one that has maintained a steady and significant growth. By doing so it has provided a great deal of jobs in the Dominican labor market, citing that for the year 2009 the industry counted with 22, 000 jobs. Taking into consideration that the growth of this industry will be of about 27% and 36% annual growth during the next five years, it means that by 2014 the number of jobs can grow to an astonishing 150, 000 jobs if the average annual growth rate is of only 27%. If the industry grows at an average of 37% annually, we are talking about having 250, 000 jobs, which is almost double of the previous projection. (Jonathan Aragonéz, 2010)

Strengths, weaknesses and investors perspective of contact centers FDI

Deciding whether to invest or not in a country is a decision which is influenced by what the country has offered and showed you, and what other investors say their experience has been. Investors will most likely take other investors input as the reality of how business works in a country. With that being said, one of the biggest disadvantages mentioned by investors is that the Dominican Republic doesn't count with a large enough English speaking community to hold growing operations. This statement comes from the interview with Mr. Blake Janover, contact center owner who has experienced the lack of English speaking representatives. He mentions that the Dominican Republic is a great place to invest, but not the best in the world due to some more important flaws than not enough English personnel. The main weaknesses mentioned by this contact center owner are banking, finance, and overall infrastructure, which is why he runs everything through an external company abroad instead of legally constituting a Dominican company. He also says that it takes time to get things rolling in the country, but he likes the Dominican Republic because " it offers a huge tax benefit, as the US offers almost none" (Blake Janover, 2010). Further details given by Mr. Janover can be seen in the Appendix.

As for the interview with Mr. Jonathan Aragonez, an economist for the Center of Export and Investment of the Dominican Republic, he explains that the Dominican Republic offers contact center investors a great deal of benefits. In his interview he mentions some of the exclusivity of Dominican Republic, its treaty and skilled labor force. The most significant interpretation I could

gather from the interview was that an investor is usually winning when investing in a contact center.

“ This is an industry that is expected to grow at a steady 27 to 36 percent in average in the next 5 years, so the investor is bound to make a great profit in the business”.(Jonathan Aragonez, 2010)

Both the investor and the host country agree in one thing, the Dominican Republic offers advantages that many other countries don't have, and that is why the country is becoming a leader in the industry. These advantages are not only extended to the country and the investor, but are also transferable to the workforce. The average starting salaries in the contact centers are between RD\$18, 000 to RD\$22, 000 pesos. This amount is three times more than the average salary of RD\$6, 000 pesos-established by law-for people working office jobs such as law clerk, assistant or financial analyst (Ministry of Labor of the Dominican Republic, 2007). The contact center salaries are only matched by those of Doctors or Engineers in production plants, which is very demanding professional field in comparison with being a contact center agent. Although this is good for an individual whose only skill may be to speak English, it affects other labor markets due to the fact that the salary is so much