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Colombia's lesson in economic development

A faster pace of economic development calls for microlevel reforms to help specific sectors and companies become more competitive in global markets.

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Many developing countries are frustrated because better macroeconomic conditions haven't led to faster economic growth. Clearly, earning an investment-grade rating on sovereign debt isn't enough. Our work in Colombia creating and implementing an economic-development program, with a model focused on improving specific industry sectors, could provide useful lessons for a number of developing countries.

Colombia has enjoyed a surprising political and economic turnaround over the past decade. Nonetheless, many economists assert that the improvements in the business environment are necessary but not sufficient to ensure sustainable economic development. The country's government concluded that to achieve enduring success, it would have to focus on making specific business sectors more competitive. Its Productive Transformation Program,[1] launched in 2007, created a novel public–private partnership engaging eight industry sectors. Early results suggest that tighter collaboration has not only removed investment barriers but also built competitive advantages.

The country has come a long way since 2000, when some economists and political analysts were saying that it was becoming a failed state. The government has reclaimed territories it had abandoned to drug traffickers and rebel armies, crime rates have fallen drastically, investor confidence is high, and unemployment has dropped. Growth slowed during the 2008–09 global recession, but Colombia has fared better than the rest of Latin America: from 2005 to 2009, the economy grew at an annual rate of 4.6 percent, compared with 3.6 percent for the whole region.

One big issue as Colombia tries to achieve sustained economic growth is its reliance on commodities. The country has a diversified industrial base focused on the internal market—the result of the import substitution model it (like most of Latin America) pursued from the 1950s until the early 1990s. Most of its industries failed to develop enough to become competitive globally; many of them underwent a painful restructuring once the country started opening its economy, in the 1990s. Some of the stronger sectors, taking advantage of newly signed free-trade agreements, worked hard to export manufactured goods to other Latin American countries. These efforts, however, haven't reduced Colombia's dependence on commodities, such as oil, coal, coffee, and fresh-cut flowers, which still collectively represent about 70 percent of its exports (exhibit).

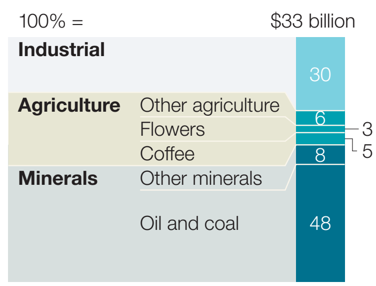
The commodity sector is important, and Colombian officials rightly concluded that it should be nurtured, much as some high-income countries (for instance, Australia and Canada) have done to support economic development. But these officials also decided that other measures should be undertaken as well. To generate better-paying jobs for Colombians, the Productive Transformation Program seeks to accelerate the growth and competitiveness of higher-value-added sectors.

[1] For more information, see www.transformacionproductiva.gov.co.

Exhibit

Colombia's economy continues to rely heavily on commodities

Composition of Colombian exports, 2009, %



Source: Banco de la República; Colombia's National Bureau of Statistics (DANE)

A keystone of the program is closer collaboration between the government and the business community. Rather than choose winners, as some developing countries have, Colombia invited all sectors to participate in the program. Given the government's limited resources, it organized a contest to decide which ones to work with first. It did set preconditions: subsidies or protection would not be granted, so any improvement in competitiveness would have to occur under market conditions. In exchange, the government agreed to work with private businesses to educate and train the workforce in pertinent skills, to improve the regulatory environment, to help promote industries in foreign markets, and to develop the required infrastructure.

The government based its selection on not only the potential of a sector but also the willingness of its leaders to commit money and people to the effort (see sidebar "Expanding the focus"). The first chosen were a mix of emerging high-potential sectors (business process outsourcing and offshoring, software, cosmetics, personal-care products, and health tourism) and established ones (textiles and clothing, electricity, auto parts, and printing and graphic arts).

After choosing a sector, the government worked with businesses in it to create and implement a strategic agenda. The overall goal was to build an understanding of the sector's position in the global marketplace and in Colombia, as well as to define initiatives required to increase the sector's competitiveness.

In the case of the business-process-outsourcing sector, studies reviewed the experience of India and the Philippines, given their success serving the English-language market. Other studies looked at Morocco to understand its approach to the French-language market, which is similar in size to the Spanish-speaking one, where Colombia has a natural

Expanding the focus

Colombia's business-process-outsourcing sector could expand its market focus gradually from voice services to knowledge-based services.

	Differentiation	Geographic focus	Segments
High-level strategy	*'Nearshore'* *Better cost and service levels than other Latin American countries*	*Domestic market* *Spain* *US Hispanic market* *Multinationals in Latin America*	Develop leadership position in Spanish-language voice services Migrate gradually to data-processing and knowledge-based services in Spanish and English Focus on services to sectors with strong base in Colombia (eg, government, health care, and financial services)

advantage. The studies found, for example, that Colombia had lower costs than other Latin American countries and could serve the US Hispanic market and multinationals in the region competitively. Diagnostics also concluded that the sector could account for more than 300,000 jobs in Colombia by 2019 (see sidebar "Creating jobs").

To date, the program's results are encouraging, although it's too early to claim success. There seems to be an important new working dynamic, based on a shared and clear agenda, between the public sector and the business community. As an illustration, here is a summary of some steps already taken in the business-process-outsourcing sector.

- Developing human resources. The government has set up a national registry for people with certified proficiency in the English language (www.ispeak.gov.co) to make it easier for business-process-outsourcing companies to find qualified employees. The city of Bogotá, in partnership with several companies, has created a program to finance English-language education for call center employees.

Creating jobs

Colombia's business-process-outsourcing sector could provide more than 300,000 jobs by 2019.

	2008–12	2012–19	2019–32
Projected number of jobs created	155,000 by 2012	305,000 by 2019	600,000 by 2031
Market focus	Establish leadership in Spanish-language voice services; locate facilities in major cities Build capabilities in basic and rules-based data in Spanish and English	Maintain leadership in Spanish voice services; gradually transfer facilities to midsize cities Migrate gradually to data- and knowledge-based services in facilities located in large cities	Focus on data- and knowledge-based services in which employee skills can have beneficial spillover effects on rest of economy
Share of service mix	Spanish- and English-language services: 98% and 2%, respectively	Spanish- and English-language services: 75% and 25%, respectively	Spanish- and English-language services: ~50% for each

- Taxation and regulation. By eliminating the value-added tax on business-process-outsourcing service exporters, in May 2010, the government gave them the same conditions that goods-exporting industries enjoy and eliminated a disincentive to the creation of offshoring services in Colombia. In the second half of 2010, Congress is expected to approve a new data protection ("Habeas Data") bill, which would align Colombian law with stricter European and US data security requirements, making the country a more attractive business-process-outsourcing destination. Finally, Colombia adopted International Financial Reporting Standards, which will support the development of financial and accounting services, since Colombian professionals must be certified in the standards. This is important because financial accounting is one of the processes developed countries are offshoring.

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- Industry promotion. Colombian executives in the sector have established a local chapter of the International Association of Outsourcing Professionals—the first in Latin America—which will help managers stay connected to their peers abroad and to become up to date on global trends. In addition, a partnership between exporters and the government will promote foreign investment in a variety of sectors, including business process outsourcing.

- Infrastructure. Local governments are developing two free-trade zones, near Bogotá and Medellín, respectively, specializing in business process outsourcing. State-of-the-art infrastructure and services will be available to companies that settle there. In addition, the government has already granted free trade–zone status to three new business-process-outsourcing facilities, in Bogotá, Manizales, and Pereira. Three others are under consideration, in Bogotá, Medellín, and Popayán.

The leaders of Colombia's business community and public sector are committed to accelerating the pace of the country's economic development. This goal will require not only sustained improvement in the business environment, security, and fiscal policy but also microlevel reforms to ensure that specific sectors and companies become more competitive in global markets. The Productive Transformation Program is an important element in this process. Colombia's new government, which takes office in August, has promised to continue it; in the second half of 2010, the program will be extended to the agribusiness sector. We think this approach offers lessons for other developing nations looking for ways to spur economic development.

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