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ECONOMIC AND POLITICAL NATIONALISM AND PRIVATE FOREIGN INVESTMENTS

HENRY LANDAU*

Recent years have seen changing attitudes toward the status and role of existing and prospective foreign investments and the rights and property of foreign investors. In the developing nations, the change was brought about in response to unfulfilled rising expectations and nationalistic fervor, as well as by desires for economic self-determination and achievement of development goals with a minimum of outside help. The attitudes of the developed nations were shaped by extensive economic penetration by foreign interests and a concomitant fear of outside control of major sectors of their economies.

DEVELOPING NATIONS

The economies of the developing nations are largely agricultural. Because they lacked technical and managerial skills and capital resources, their governments clamored for, and the international agencies urged the infusion of, private foreign investments to transform agrarian societies into industrialized nations, provide employment, increase national standards of living, and earn foreign exchange needed for infrastructure development.¹

Exploration and subsequent exploitation of natural resources required investment of substantial high-risk capital and the application of sophisticated technology, with no expectation of immediate return on the investment.² The installation and operation of large-scale public utilities called for technology, operational skills and investors willing to accept a small yield on their investment, none of which were available locally.

To attract the required capital, technology and skills the developing countries were willing to enter into long-term concession agreements, operating agreements and investment agree-

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¹ See generally *The Capital Needs of the Less Developed Countries*, Report of Secretary General, U.N. Doc. A/A.C. 102/5 (1962); *Financing of Economic Development — Promotion of Private Foreign Investment*, U.N. Doc. E/4293 (1967); International Chamber of Commerce, Public and Private Investment in Economic Development BR 179 (1955).

² It took, "almost \$150,000 to find and develop Boliva's oil and gas resources," and "it took ten years and \$95,000,000 before Gulf could export one drop of oil from Bolivia," Lumpkin, *Gulf Oil's Experience in Bolivia*, 8 HOUSTON L. REV. 472 (1971).

ments. Additionally, many offered incentives which were then thought to be commensurate with the size of the investment, the risk involved and the benefits the investment would bring to the countries. The foreign investor responded, relying upon the promises embodied in these agreements.

Fundamental socio-economical and political developments, resulting from pressures of the dissatisfied, produced an outlook unfavorable to foreign investments. Vying for popular support, the ruling groups in many developing countries identify themselves with the needs and aspirations of the people. To allay the frustrations of the populace and to divert its attention from the ruling groups' failure to solve the countries economic and political problems, they exploit the fear of foreign economic domination, brand the foreign investor an economic imperialist and blame him for nonachievement of development goals. By appeals to national pride and by use of the fashionable slogans of nationalism and economic independence,³ they take measures to abrogate or modify rights previously granted to the foreign investor and take over his property.

In countries where natural resources are the primary source of wealth, the extractive industries are the principle objects of take-overs. Natural resources, especially minerals and petroleum, are exhaustible. It is often charged that their extraction by foreign investors is not in the best interest of the country. These resources are generally the main source of export earnings. As a result there is pressure, in the face of rising nationalism, upon the governments in many developing countries to secure greater control over these industries in hopes of obtaining a larger share of the foreign exchange earnings they produce.

The trend to expropriate extractive industries became evident a decade ago when Uruguay introduced the United Nations Resolution 1803 calling on each member "to recognize the right of each country to nationalize and freely exploit its natural wealth as an essential factor of economic independence."⁴ Recently, Algeria's President Houari Boumediene was quoted as having said, "Until now the riches of the Third World have served the interests of the rich nations. It is time for those

³ Brigadier General Guillermo Rodriguez Larahas said that, "There is no political tendency in our revolution and no ideology. There is nationalism, there is the Fatherland at the beginning, the middle and the end, and there is a desire to serve the Ecuadorian people." N.Y. Times, Mar. 9, 1972, at 11, col. 1.

⁴ 7 GAOR 7 (1952), U.N. Doc. A/C2/L.165 (1952).

nations to understand that economic colonialism—like political colonialism before it—must vanish.”⁵

As a result of this trend, the foreign owned companies are continually pressured to agree to a revision of their concession agreements to provide the host country with an ever increasing share of the companies' earnings and, in addition, demands are made upon them for equity participation.⁶ To force the sale of an equity interest, the governments sometimes impose unattainable production quotas, limit the amount of exports, or subject the enterprise to harassing government regulations.⁷

⁵ Sheehan, *The Algerians Intend to Go It Alone, Raise Hell, Hold Out and Grow*, N.Y. Times, April 22, 1972, (Magazine) at 18.

⁶ In 1969 Chile and Zambia took over more than 70% of profits of the copper extracting companies and leading oil producing countries including Libya, Iran, Kuwait, Saudi Arabia and Venezuela received more than five billion dollars in tax revenues. On September 4, 1970, the government of Sierra Leone acquired a majority interest in diamond mining operations in Sierra Leone. In 1972 the Organization of Petroleum Exporting Countries, consisting of Saudi Arabia, Iran, Iraq, Kuwait, Qatar and Abu Dhabi demanded a 20% participation in the Persian Gulf concessions as the only alternative to nationalization. In 1961 Mexico passed a new mining law restricting foreign capital in mineral development thereby compelling Asarco Mexicana S.A. and Industrias Penoles S.A., subsidiaries of American Smelting and Refining Company, to sell 51% interest to Mexican nationals. On May 18, 1972, the Mexican government announced the “Mexicanization” of the country's sulphur industry with the acquisition of Azufrera Panamerica, 34% owned by Pan American Sulphur Company, of which the government will own 80% and private individuals 20%.

Under the Chileanization program, foreign-owned copper companies were initially compelled to sell a portion of their 100% interest.

After the passage of a new mining law on February 7, 1961, which provides for fading-out of majority foreign interests, Mexican interests acquired a majority interest in Asarco Mexicana S.A., formerly a 100% owned subsidiary of American Smelting and Refining Company, and of Industrias Penoles, a subsidiary of American Metal Climax. Algeria converted its minority interest into a majority interest in a number of oil and gas companies. Kenya acquired a 50% interest in a petroleum refining company owned by a foreign consortium. The Bolivian Government announced the nationalization of the nitrate industry by its acquisition of the 49% equity interest of Eequimich from Anglo Lautara, 51% of which was already owned by the Government. In 1971, a state-owned Chilean steel company acquired Bethlehem-Chile Iron Mines Company, an iron mining concern, wholly-owned by Bethlehem Steel Corporation. Guyana took over Demerara Bauxite Company, a subsidiary of Aluminium Company of Canada. Haiti cancelled a refining concession agreement held by Haitian Petroleum Company, a subsidiary of Valentine Petroleum and Chemical Corporation. Peru expropriated the refinery complex and oil fields of International Petroleum Company, Ltd. Algeria nationalized or intervened in a number of natural gas, oil and pipeline companies and refineries. Libya nationalized the petroleum import and distribution facilities of Standard Oil of New Jersey, and Gulf Oil Company was compelled to relinquish its exploration concession. Uganda nationalized a number of foreign-owned oil and mineral companies. Zaire (formerly Congo, Kinshasa) took over the concessions and facilities of Union Miniere du Haut Katanga. Burma nationalized Burmese Oil Corporation. Ceylon nationalized distribution facilities and related equipment of Standard Oil Co. (New Jersey) and California-Texas Oil Co.

⁷ Iraq's demand for a 20% participation was accompanied by an increase in the production quota. The sale by Compania Azufrera Mexicana, S.A., a subsidiary of Pan American Sulfur Incorporated of its 43% interest to the Mexican government and of its 43% interest to private

The threat of nationalization is often sufficient to induce the sale of the enterprise at a price below that ordinarily obtainable.

The chairman of Pan American Sulphur Company, which in May 1972, sold its interest in Azufrera Panamerica to the Mexican Government said, "This was not an expropriation at all. It was a voluntary arms length transaction."⁸ However, Pan American Sulphur Company was reportedly happy to sell out because it was displeased with some government regulations. The sale followed an anti-dumping investigation by the U.S. Treasury Department, and Horacio Flores de la Pana, Mexico's National Properties' Secretary, told a news conference, "The less share we have of U.S. markets, the less reason there is to share our sulphur earnings with U.S. investors."⁹

In several countries, there was outright expropriation and in others the take-over followed the acquisition of equity participations of petroleum and mining companies. To keep these basic natural resources completely under local control, the expropriating governments abrogated or annulled even recent concessions and took over the enterprises' properties, machinery, distribution and other facilities in the belief that they could successfully operate these companies and thus obtain funds for their development programs.¹⁰ In a number of countries the

Mexican nationals, and the sale by Compania Explotadora del Istneo, S.A., a subsidiary of Texas Gulf Sulfur of its 66% interest to Mexican nationals followed the Mexican government imposition of quotas limiting their exports.

⁸ N.Y. Times, May 19, 1972, at 49, col. 1.

⁹ *Id.*

¹⁰ On November 15, 1963, by Decree 743-45, Argentina annulled petroleum exploration and development contracts awarded to seven companies, some of which continued operating in Argentina. In 1969 Bolivia nationalized all assets of Bolivian Gulf Oil Company. In 1971 the government of Juan Jose Torres Gonzalez abrogated International Metals Processing Corporation's dredging concession, granted in 1965, and the twenty-year lease of zinc, cadmium, lead, silver and gold granted in 1966 to Mina Matilde Company, owned by U.S. Steel and Mineral & Chemical Corporation. In 1972 the disputes concerning the International Metal Processing and Mina Matilde confiscations were resolved by the government of Col. Hugo Banzer Suarez, by the creation of mixed enterprises under private management. In May 1970 the Bolivian Government announced the nationalization of the nitrate industry by acquisition of 49% equity interest of Soquimech, of which it then owned 51%. In 1971 a state-owned Chilean steel company acquired Bethlehem-Chile Iron Mines Company, an iron mining concern, wholly-owned by Bethlehem Steel Corporation. Guyana took over Demera Bauxite Company, a subsidiary of Aluminum Company. Haiti cancelled a refining concession agreement held by Haitian Petroleum Company, a subsidiary of Valentine Petroleum and Chemical Corporation. Peru expropriated the refinery complex and oil fields of International Petroleum Company, Ltd. . Algeria nationalized or intervened in a number of natural gas, oil and pipeline companies and refineries. Libya nationalized the petroleum import and distribution facilities of Standard Oil of New Jersey, and Gulf Oil Company was compelled to relinquish its exploration concession. Uganda nationalized a number of foreign-owned oil and mineral companies. Zaire (formerly Congo, Kinshasa) took over the concessions and facilities of Union

outlook regarding basic utilities and essential services resulted in similar measures with respect to foreign owned communication and power industries,¹¹ as well as banks¹² and insurance companies.¹³

The nationalistic urge to eliminate or reduce foreign influence is not confined to basic industries. Even as U.N. Resolution 1803 reflects the desire to preserve control over natural resources, U.N. Resolution 2158 (XXI) recognizes "the right of all countries and particularly of the developing countries to secure and increase their share in the administration of enterprises which are fully or partly operated by foreign capital and to have a greater share in the advantages and profits derived therefrom on an equitable basis."¹⁴ The policy enunciated in Resolution 2158 was given a fuller expression in the message of Mexico's President Gustavo Diaz Ordaz to the Mexican Congress on September 1, 1966.

Those who would like to open the door to foreign investments without limit or protection forget that through our economic development we strive to consolidate national independence as quickly as possible. With reference to direct foreign investment, we propose that they be associated in minority partnership with local capital. Far from granting preferential treatment, we try to limit their field of activities by proposing exclusiveness of the Nation in basic industry and require a majority of Mexican capital in certain secondary industry closely linked with basic industries.¹⁵

The policies thus expressed were carried out by excluding foreign interests from new and existing stipulated industries and activities deemed vital to national economies, and by con-

Maniere du Haut Katanga. Burma nationalized Burmese Oil Corporation. Ceylon nationalized distribution facilities and related equipment of Standard Oil Co. (New Jersey) and California-Texas Oil Co.

¹¹ Brazil, Costa Rica, Colombia and Mexico took over the properties of American Foreign Power Company, and Chile acquired a 70% interest in South American Power, a Boise Cascade subsidiary. Brazil, Chile, Ecuador and Peru expropriated telephone and cable facilities owned by subsidiaries of International Telephone & Telegraph Company. Somalia took over the Italian-Somali Electric Co.

¹² Chile, Libya, Somalia, Sudan, Uganda and Burma nationalized foreign-owned banks. Peru restricted foreign ownership in domestic banks to 25%, and Decision 24 of the Andean Subregional Common Market Commission limited foreign interest in domestic banks to 20%. Venezuela restricted banking functions of banks having a foreign interest until 80% of the capital shall be owned by Venezuelans.

¹³ Libya, Uganda, Indonesia and Iraq took over foreign owned insurance companies. Tanzanian Insurance (vesting of interest and regulation) Act of 1967 provides for compulsory sale to National Insurance Company of foreign owned shares of insurance companies operating in Tanzania. Sudan ordered all foreign owned insurance companies to cease writing new business.

¹⁴ G.A. Res. 2158, 21 U.N. GAOR, at 29, U.N. Doc. A/6316, Supp. 16 (1966).

¹⁵ Creel, *Mexicanizations: A Case of Creeping Expropriation*, 22 Sw. L.J. 281, 294 (1969) [hereinafter cited as Creel].

trolling and regulating foreign investments in other, even small, established and prospective enterprises.¹⁶

Foreign participation in new projects is controlled by insisting upon, or encouraging, substantial local participation,¹⁷ restricting foreign wholly owned enterprises¹⁸ and by offering incentives to enterprises owned jointly by foreign and local interests.¹⁹

The extent of foreign ownership and control of existing enterprises is regulated by provisions of investment laws or investment agreements, which confer upon the government the right of participation in enterprises,²⁰ and by laws and decrees which call for a fade-out of the foreign interest through the sale of fixed percentages of equity within prescribed periods of time.²¹

¹⁶ Brazil excludes foreigners from ownership and operations of domestic air lines, coastal shipping, newspapers and telecommunications. Mexico reserves control of radio and television broadcasting, production, distribution and export of motion pictures, transportation, fish hatcheries and fishing, publishing and publicity, production, distribution and sale of aerated beverages, manufacture and distribution of rubber products, and insecticides and basic chemical products. In Indonesia, foreigners are excluded from telecommunications, production and transmission of electricity, aviation, ownership of railroads, mass media and other industries considered vital. El Salvador reserves enterprises with capital of \$40,000 or less for persons born in El Salvador or other Central American countries. The Ghanaian Business (Promotion) Act of 1970 transferred foreign owned small and medium sized retail and wholesale businesses to Ghanians.

¹⁷ Mexican Decree No. 4990 (D.O. 2nd July 1971) provides for Mexicanization of oil, steel, aluminum, cement, glass, fertilizer and cellulose industries. In India, a majority foreign ownership is not permitted except where the enterprise will contribute needed technology, or require a substantial amount of foreign exchange or produce substantial export earnings. Ceylon and Thailand prefer joint enterprise. Philippines prefers joint ventures and limits foreign interest to 40% in certain areas and in industries developing natural resources. In Nigeria at least 55% government equity is required in iron, basic steel, petrochemical and fertilizer production industries. At least 35% private participation is required in some small businesses even though local investment capital is not available for such participation.

¹⁸ In several Latin American and African countries control is exercised through initial screening and approval which among other things affects remission of profits and repatriation of invested capital.

¹⁹ In the Dominican Republic, El Salvador and Malaysia investment incentives are available only to joint enterprises, with substantial local participation.

²⁰ In Congo (Brazzaville) the government reserves the right to take equity participation. In Ghana large scale enterprises are required to offer to the government participation in new issues.

²¹ Mexico requires a reduction of the majority foreign interest within five years in important industries and ten to fifteen years in others. Also, sales of stock to foreigners in Mexican companies which will result in a foreign owned majority are discouraged. See Creel, *supra* note 15. Ceylon requires a gradual transfer of majority interest to its nationals. In the Philippines, pioneer industries must list their stock on the exchange within ten years and sell 60% of the equity to Philipinos within twenty years. Zambia's President Kaunde proposed that the state should take a 51% interest in 25 companies engaged in the manufacturer and sale of building materials, road transportation, brewing and wholesale and retail trade. Peru requires all foreign owned concerns to enter into

At times, political motives for the elimination of the foreign interest loom as large as the economic motives. In the preamble to the Bolivian Supreme Decree G.O. 474 of the 17th of October 1969, the stated reason for the expropriation of Gulf Oil is that "[T]he Bolivian Gulf Oil Corporation has grown into a new superstate economically and politically more powerful than the Bolivian State." Libya nationalized the properties of the British Petroleum Company for "colluding" in Iran's invasion of the Arab island in the Persian Gulf. The United Arab Republic threatened to nationalize the properties of West German companies should West Germany establish formal diplomatic relations with Israel. The effect of moves such as these is that "foreign investments are the most exposed targets of frustration, irrational policies and misguided nationalism."²²

The efforts to rid the country of real or imagined foreign domination may satisfy national pride and serve political interests, but only at the expense of the country's economic interest. Most of the developing countries have not reached a stage of technical and managerial expertise which can provide a sustained efficient operation of the expropriated industries. Absent such expertise, there will be no earnings for self-sustained growth and for upgrading of the standard of life. For example, Chile's labor and technical problems limited copper production from the expropriated mines to 750,000 tons instead of the planned one million tons.²³ Bolivia exports one-third of the tin it exported prior to expropriation.²⁴

Perhaps in recognition of their own limitations, some developing countries have reversed the trend toward economic nationalism. Guinea, which in 1961 took over Bauxites du Midi, a subsidiary of Alcan, was unable to fulfill its contractual obli-

fade out agreements providing for the sale of its shares to reduce the foreign ownership to 85% by July 1974, to 55% by July 1981 and to 49% by July 1986. In December 1970 the Commission of the Cartagena Agreement on Andean Subregional Integration published its Decision 24, later superseded by Decision 37, proposing uniform rules to exclude foreign investments in Bolivia, Chile, Colombia, Ecuador and Peru and to reduce foreign participation to a minority interest in the future, by subjecting existing companies to divestment of equity and management through mandatory fadeout agreements in key industries and depriving other industries of the Central American Common Market benefits if they do not avail themselves of the option to enter into fadeout agreements. (See Schliesser, *Restriction on Foreign Investment in the Andean Common Market*, 5 INT. LAW 586, (1971).

²² President Nixon's "State of the World Message," 116 Cong. Rec. 3821 (1970).

²³ N.Y. Times, July 2, 1971.

²⁴ *Expropriation, Why They Do It*, FORBES, July 15, 1971, at 36.

gation to mine and export bauxite, and by 1963 was compelled to turn over the operation to a new enterprise in which the government holds a minority interest. On May 1, 1971, President Amin of Ghana reversed the policy of former President Obote to require a 60% Ghanaian ownership in commercial banks, mining, transportation and other important private companies by reducing the government's participation therein to a 49% interest. Cambodia, which nationalized the petroleum industries in 1967, at first granted a twelve year grace period to Standard Oil Company (N.J.) and to California Texaco Company, and in 1970 repealed the Nationalization Act. In October 1967, Sierra Leone revoked the "Non-Citizens Trade and Business Act of 1966" which excluded non-citizens from certain industries. In 1970 the assets of Sterling Drug Company were nationalized and subsequently denationalized.

Bolivian President Hugo Banzer Suarez, referring to the transfer of the previously confiscated tin dredging operation of International Mining and Processing Company and of the Matilde Zinc Mine, to mixed companies under private management, stated, "[T]here is no need now for major nationalization and we want foreign capital to develop our resources on a fair basis. We have enough problems making the already nationalized mines work efficiently."²⁵

An in-flow of advancing technology as well as a large amount of foreign capital is essential if the industrial development of the developing countries is to continue at a desirable pace. The pursuit of policies grounded on economic and political nationalism will impede that flow.

The Executive Committee of the International Chamber of Commerce was prophetic when it issued its statement that it feared

the overall effect of Decision 24 (of the Commission of the Cartagena Agreement) will be: to deter rather than to attract the transfer of technology, to adversely affect the balance of payments and to result in a wasteful utilization of local capital resources. The ICC further fears that Decision 24, instead of contributing towards the attainment of its stated objectives, will impede rather than promote progress toward development, national participation and regional integration.²⁶

The restrictive investment policies of the Andean group caused 56 companies to hold up 84 definitive or potential projects in 1971.²⁷

²⁵ N.Y. Times, Feb. 9, 1972, at 7, col. 1.

²⁶ 37 ICC INFORMATION 9 (1971).

²⁷ *Learning to Live with Expropriation*, BUSINESS WEEK, July 10, 1971, at 34.

Overseas Private Investment Corporation insured only \$8 million of new U.S. investments in Latin America during the last quarter of fiscal 1971 against an average level of \$100 million for each quarter of the preceding four years.²⁸ The gain in national pride and the short term political advantages are a high price to pay for the economic and social advantages which would have resulted from the abandoned and lost projects.

DEVELOPED COUNTRIES

Foreign investors no longer have an unrestricted access to the economies of all developed countries. There is a growing concern that some sectors of their economies will be dominated by U.S. and other foreign interests.²⁹ Governments and business communities are particularly disturbed by the role of the giant international corporations and their impact on the local social and economic conditions.³⁰ They are concerned that decisions affecting production, employment and marketing are made outside the country and are influenced by the business and national interests of the foreign parent company rather than those of the local operating company.³¹

Several developed countries have adopted, or are contemplating adopting, measures to control or to curb foreign investments. Japan weighs the competitive effect of new ventures on existing Japanese industry and does not permit the entry of a competitive enterprise. All agreements between Japanese and foreign business concerns must be approved by the Ministry of International Trade. There is insistence that management be in the hands of Japanese, and there must be a Japanese majority equity interest if government approval is required for remission of earnings and repatriation of capital.³²

The European Economic Community Commission prefers enterprises within the Community, capitalized by nationals of the Community's members and whose centers of decision will be within the Community. In France, Law #66-1008 conferred upon the government the power to regulate foreign invest-

²⁸ OVERSEAS PRIVATE INVESTMENT CORPORATION, ANNUAL REPORT, at 6 (1971).

²⁹ See generally S. SCHREIBER, THE AMERICAN CHALLENGE (1968).

³⁰ Valery Gisard d'Estaing, French Minister of Finance, has said, "Multi-national companies are growing out of all proportion with national firms. This is a problem with which the government must be concerned."

³¹ Louis Camu, president of the Bank of Brussels, has said, "Make the power of decision coincide with operational activity." London Financial Times Symposium, 1970.

³² AMERICAN MANAGEMENT ASSOCIATION, Report No. 428-429, April 30, 1965; E. LANG, *Doing Business in Japan — A New Look at Licensing and Joint Ventures*, BUSINESS ABROAD (1970).

ments.³³ Foreign investments are screened, and special permits are required for large investments. Under Decree #67-78 all acquisitions or increases of control must have the approval of the Ministry of Finance.³⁴

The problem of foreign investments, particularly U.S. investments, are important issues in Canada and Australia. Canadians are perturbed by a high percentage of foreign ownership and by their belief that some foreign owned industries are run like branches of the parent companies with little or no sensitivity to local conditions.

In 1971, the First National City Bank of New York, which was the only foreign owned bank in Canada, sold, under pressure, its 75% interest in the Mercantile Bank. In 1972, in response to the Grey Commission Report, which dealt with the influence of foreign investments, acquisitions of existing companies will be under the control of the Canadian government.

United States investments in Australia are attacked by politicians and economic nationalists, and the government is examining the role that the large foreign enterprises play in the Australian economy. John Douglas Anthony, Deputy Prime Minister and Minister of Trade and Industry, said that the government intends to police foreign investments and hinted at a requirement for a higher percentage of Australians in ownership and management.

Economic nationalism exists in all parts of the world. Its intensity, the manner in which it is expressed, the way in which it operates and its impact on foreign investments varies from country to country. However, it is generally related to the country's political and economic maturity and stability. The foreign investor must, therefore, conform to the national goals, aims and economic policies of the host country.³⁵

³³ Torem and Craig, *Developments in the Control of Foreign Investment in France*, 70 MICH. L. R. 285, 286 (1971).

³⁴ *Id.*

³⁵ To promote "collaboration between partners which is so vital if the economic growth of the Third World is to be accelerated" the Commission on International Investments and Economic Development of the International Chamber of Commerce is preparing a guide for international private investment which will contain recommendations addressed to the investors, as well as to the governments of host countries and of the countries of the investors.