478

A FOREIGN ECONOMIC POLICY FOR THE 1970'S

HEARINGS

BEFORE THE

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OF THE

JOINT ECONOMIC COMMITTEE CONGRESS OF THE UNITED STATES

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257

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CONTENTS

WITNESSES AND STATEMENTS

Monday, July 27, 1970

Tuesday, July 28, 1970

Wednesday, July 29, 1970

Thursday, July 30, 1970

SUBMISSIONS

Monday, July 27, 1970

A FOREIGN ECONOMIC POLICY FOR THE 1970'S

MONDAY, JULY 27, 1970

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON FOREIGN ECONOMIC POLICY
OF THE JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The Subcommittee on Foreign Economic Policy met, pursuant to notice, at 10:12 a.m., in room S-407, the Capitol Building, Hon. Hale Boggs (chairman of the subcommittee) presiding.

Present: Representatives Boggs, Reuss, Widnall, and Conable.

Also present: John R. Stark, executive director; John R. Karlik, economist; Myer Rashish, consultant; and George D. Krumbhaar, economist for the minority.

Chairman BOGGS. Ladies and gentlemen, and members of the subcommittee, as well as our panelists, today we open the fourth set of hearings in the continuing investigation of the Subcommittee on Foreign Economic Policy to establish policy goals for the 1970's. We have already surveyed the issues broadly, and looked intensively into U.S. trade policy toward other industrial nations and our efforts to promote economic growth in the developing countries. Now, we are turning to the implications of direct investment across national boundaries, both in the United States and throughout the rest of the world.

The rapid growth of such investment during the last decade has led to the development of what are now known as multinational corporations. These corporations do significant proportions of their business in a number of different countries rather than concentrating their activities in one single nation. While business leaders have viewed this development as a means of distributing the fruits of technology and managerial expertise more rapidly throughout the globe, spokesmen for organized labor have viewed multinational corporations as institutions exporting thousands of jobs. The U.S. Government has also become concerned that American firms might be able to avoid administrative regulations by permitting their branches abroad to engage in activities that would not be permitted here. On the other hand, some other governments have considered the attempt to impose U.S. antitrust statutes, balance of payments guidelines, and trade regulations on the foreign subsidiaries of American firms as an unjustified extension of U.S. sovereignty. It is not surprising, therefore, that corporate managers have sometimes found themselves caught between the conflicting desires of different governments.

It is these questions and the impact of multinational corporate activity on productivity, the transfer of technology and international payments flows that we shall be investigating today and in our subsequent hearings.

Today's first witness is Mr. Guido Colonna di Paliano, who has lately become a director of the Fiat Motor Co., one of the great motor companies in the world. Ambassador Colonna is former Deputy Secretary General of NATO, and until recently, a member of the Common Market Commission, responsible for internal market relations and the development of industrial policy within the European community.

I might also add that he was also responsible for a great attempt to direct the community outward rather than inward.

Second is Mr. Charles P. Kindleberger, professor of economics at Massachusetts Institute of Technology and a student of multinational corporate activities.

Next is Mr. James W. McKee, president of the CPC International, one of the great multinational corporations based in this country.

Finally, we have Mr. Judd Polk of the U.S. Council of the International Chamber of Commerce.

It is a very distingiushed panel. We are very happy to welcome you gentlemen and we will first hear from Mr. Colonna.

STATEMENT OF GUIDO COLONNA DI PALIANO, DIRECTOR, FIAT CHAIRMAN, RINASCENTE, AND FORMER ITALIAN MEMBER OF THE EEC COMMISSION RESPONSIBLE FOR INTERNAL MARKET RELATIONS AND THE DEVELOPMENT OF A EUROPEAN INDUSTRIAL POLICY

Mr. COLONNA. Mr. Chairman, it is a great privilege to be invited to participate in the hearings of your subcommittee, and I am very grateful for this honor.

I regret that I was unable to circulate, in advance, copies of my prepared statement. I beg the indulgence of the subcommittee for this omission.

Copies of this prepared statement shall be circulated in time for this afternoon.

Chairman BOGGS. We will have it in the record.

Mr. COLONNA. Thank you very much, sir. Let me also say, Mr. Chairman, that your announcement that you shall visit the commission very soon pleased me very much, and I can assure you that you will be heartily welcome in Brussels.

A great deal of specific information has already been contributed to this subcommittee by highly qualified persons on international investments and the multinational corporation.

I shall, for my part, endeavor to highlight the connection existing between this modern form of industrial organization and the process of economic integration in which we are engaged in Western Europe. Special problems arise in fact when multinational corporations are active and investment flows in States which have agreed to become eventually a single economic entity.

My views are based on my experience as member of the Commission of the European Communities: A position which I have held until a few weeks ago. More specifically, I have had in mind the findings and the proposals outlined in a memorandum on the industrial policy of the European Community which was prepared under my responsibility and presented last spring by the Commission to the Council of Ministers.

The opinions which I shall express here do not, however, commit anybody but myself.

It is important that ideas and policies developed in Brussels should be appreciated in regard to the overall objective which we want to achieve in Europe.

Members of the subcommittee are no doubt aware of the purpose for which the process of European integration was launched 20 years ago. The aim was, and still is, that Europe should acquire, through the gradual integration of the free and democratic nations of the continent, the strength required to bear its share of responsibility in the world.

It is consistent with this design that the productive structures of the member countries should take legitimate advantage of the creation of the community for facing with success larger and larger doses of international competition over the wide world.

Twenty years of efforts have had positive results. A new reality, distinct from its national components, has come into existence, which all economic operators must take into account. A custom's union has been acheieved: a network of common rules has been agreed and is being enforced.

This new reality has been beneficial not only to us but also to our trading partners in the world.

Thus, total trade between the community and the United States amounts to some $15 million, which is three times as much as in 1958.

From 1958 to 1967, the United States had a large surplus—averaging $1.2 billion per annum—on its trade account with the community.

In 1968, the very rapid expansion of domestic demand in the United States led to an exceptional growth of imports. But in 1969, the community was again in deficit with the United States in excess of $1 billion. Exports from the United States amounted to $7 billion and those from the community $5.8 billion.

Direct international investment has become a very significant alternative to visible exports for producers desirous to expand their outlets beyond the national frontiers.

Since 1958, direct investments by American firms in the community increased nearly fivefold. The capital for these investments comes now very often from issues floated in Europe; while the return on these investments has become very significant in regard to the balance of payments of the United States.

It can be stated, therefore, with objectivity that the creation of the community has been from an overall point of view beneficial not only to ourselves but also to our trading partners. We in Europe have achieved a marked improvement in our standard of living. But the internal demand resulting from this improved situation has been available also to our external competitors.

The community is indeed bound to pursue outward looking trade policies because of its structural dependence on world trade in the formation of its national product. Total trade accounts for nearly

20 percent of the gross national product of the community, while in the United States the corresponding figure is only 7 percent.

Let me now, Mr. Chairman, outline very briefly our current ideas and plans for the further development of the community.

A custom's union is not sufficient to secure a free circulation of all goods and services. This total freedom can be achieved only through the elimination of a number of nontariff barriers. These barriers can be removed only through a complex process of harmonization of national rules and regulations. It must be recognized that a great deal remains to be done in this respect.

Let me underline that we are aware that nontariff barriers, whether administrative rules and regulations, fees, sanitary prescriptions, technical norms, or public procurement procedures, affect also trade with our external partners. The community cooperates actively in the GATT to this end. Whenever possible, solutions for our own internal problems in regards to the barriers are selected which are likely to be acceptable within wider frameworks. The elimination of these barriers at world level will require considerable efforts and a good will in all countries concerned. In the meantime, our own internal efforts of harmonization shall be beneficial also to our external partners because they will be eventually faced with a single set of rules and regulations, whereas at present there can be as many as six.

A common market as outlined by the Rome treaties, is not only a market within which goods should circulate in total freedom; it is also meant as an area in which productive factors can be organized by managers with a view to achieving greater efficiency, irrespective of the political boundaries separating the member states. Labor and capital should be allowed to circulate freely, and corporations should enjoy the right of establishment in any part of the community area.

Once again this implies the harmonization of different national legislations.

Finally, the Community must consist not only of a common market but also of a set of common economic policies. The founders of the community foresaw that, lacking the required degree of harmonization in national economic policies, there could be no certainly of stability of the common market. Here again, it must be recognized that, with the exception of the agricultural policy, progress has been so far limited.

The community can, therefore, be considered as a reality which is not yet what it was supposed to be. This lack of fulfillment does not justify, however, in my opinion, the recurrent pessimism on the chances of our endeavor to succeed. We are up against real and objective difficulties; we are fully aware of them; we are determined to overcome them; but it takes time.

The elimination of nontariff barriers, the establishment of a common legal, fiscal and financial framework, the harmonization of the national economic policies cannot be carried out by the application of automatic rules such as those which have brought about the establishment of the customs union.

Every step in this direction must necessarily result from a specific agreement between the governments of the member countries. It is up to the Commission to submit proposals which are objective, realistic and reflecting the common interest, but it is up to the Council to take decisions on them.

Now, the various governments in the Council reflect necessarily the attitude in their respective countries in regard to any issue under discussion, and it is not surprising that these attitudes should very often differ. The notion of common interest is a subjective one and likely to be influenced by local considerations and preoccupations. This subcommittee no doubt appreciates the problem of reconciling the general and the local interest, the short and longer term.

It is the duty of the Commission to fight for decisions which are as immediately consistent as possible with the common interest. But sometimes imperfect compromises are better than none at all, because they can be the stepping stones for further and better decisions.

This is the way in which I look at the common agricultural policy, an area of the community activity which is subject to serious criticism in this country and elsewhere. The extension of the preference entailed in the customs union to farm products was an essential condition for the establishment of the Community, dictated by political, economic and social considerations.

However, the achievement of a common market for agricultural products meant the harmonization of six different national policies of support of agricultural prices. The outcome can be criticized at leisure, but this stage had to be reached for embarking upon the next one: The launching of the program known as the Mansholt plan, having as its objective a common European agricultural policy less costly for the taxpayer, more evenly rewarding for the producer, and more acceptable to our trading partners in the world.

Far-reaching endeavors are inevitably subject to periods of stagnation and crisis. What matters, however, is that the sense of progress should not be lost. In our case it was not.

The Community has indeed survived a series of crises, the last of which was concluded by the summit meeting held in The Hague last December. It was agreed in this meeting to hasten the process of internal consolidation of the Community, to set forth as a new objective the establishment of an economic and monetary union, and to open negotiations with Great Britain and the other applicant countries.

As a result, the Community is now in a new phase of intensive activity along four main directions:

(*a*) Discussion of the Mansholt plan for a reform of the common agricultural policy.

(*b*) Discussion on a common industrial policy.

(*c*) Discussion of a program of action to achieve economic and monetary union before the end of the present decade.

(*d*) Negotiations with the applicant countries.

These four groups of problems are, of course, closely interrelated.

In order to correct the imbalances and deficiencies of the present common agricultural policy, new industrial jobs must be created. This requires the promotion of a sustained industrial development in the Community, this development being so conceived as to permit the productive structures of the Community to keep on facing international competition in its various forms.

Since the industrial structure of the member states differs in terms of relative strength, the absence of an harmonious industrial development within the Community would hinder the achievement of an economic and monetary union and, indeed, would jeopardize the very existence of the customs union.

As concerns the enlargement of the Community, it would seem that the desire of the applicants, in particular Great Britain, to become members is proportional to the prospects of greater vitality and internal consolidation of the Community.

The problems which the present common agricultural policy creates for Great Britain are well known: hence, the importance of the Mansholt plan for a reform of this policy. The preference entailed in the participation of Great Britain to the customs union offers but limited advantages to British industry. Hence, the importance which the British industry seems to attach to a coherent industrial development strategy.

The industrial policy which the Commission suggests consists in a gradual approach that should promote European industrial and technological development with a view to a continuation of the present expansion of international trade and investment.

The Commission regards as a first and urgent step in this direction the achievement of the Common Market as a common outlet for all goods and services. This implies inter alia the liberalization of public procurement throughout the Community. Public procurement of goods produced in other member countries is at present negligible.

Government procurement is bound to increase rapidly as a result of the explosion of social demand. It is, therefore, important that the de facto preference granted by national authorities to their own industries should come to an end. The Commission no doubt has the authority and the duty to enforce the rules of the treaties against discriminatory practices. But national public procurement procedures, particularly for certain sophisticated products, are such that the enforcement of the common rules is not always easy, not even possible.

It is urgent to make a start with the products of certain technologically-advanced sectors, for which the procurement procedures allow the greatest degree of discretion to the public purchaser. Most of our nation states are anxious, for a variety of reasons, to promote within their boundaries industrial activities in the advanced, technology intensive sectors. The main motivation for this attitude is the fear that otherwise their industry would be cut off from the rewards which the industrial exploitation of technological progress holds in store for those who are capable of exploiting it and are trained to do so.

In my opinion, this is a legitimate preoccupation. However, the individual states of the Community do not have the size required for the emergence of productive structures capable to engage with ultimate success in lines of production requiring a large financial and managerial potential and for securing an internal outlet of the appropriate dimensions.

Governments tend to explain their restrictive attitude in regard to the admission to tenders of extra-national competitors, with the need of securing at least a partial return for their investment; I mean, the investment is in the form of subventions granted for research and development activities.

This is why the Commission suggests that the problem of liberalizing public procurement in these advanced sectors should be attacked at two levels: at the time when the subvention is granted, and when the goods become available.

First of all, the Commission suggests that R. & D. activities in certain technologically-advanced sectors should be financed by the Community. This would limit from the outset the inclination of the national authorities to reserve their market to their own industry. Community subventions, granted on the basis of joint selective decisions, could also be different member states to form joint ventures of long duration. This would be a very good way to exploit the availability of the Community as an area of continental dimensions.

The Commission suggests further that the cognizant national authorities should agree to compare and dovetail their medium-term purchasing programs for certain items, with a view of transferring larger and larger portions of the consolidated program of procurement from the present restrictive practices to nondiscriminatory procedures.

The response of the European firms to these proposals is still to be assessed. The choice between the short-term advantages of protectionism and the long-term advantages of free competition is always a difficult one.

Insofar as the authorities are concerned, their response appears to be generally positive but cautious; however, some time will be needed before reaching any conclusion.

Now, Mr. Chairman, the question arising in regard to the subsidiaries of the non-European corporations active in the Community seems to be the following: How will they react to these suggestions? How will they use the influence which they can bring to bear on national authorities? I feel that they have a great chance in respect of these and similar issues by playing straight in favor of the consolidation of the Community and against the present fragmentation of the market.

At present the subsidiaries of non-European corporations are in a position to share, together with the national industrial activities (when these exist) the advantages of national preference in public procurement, at the same time being part of powerful multinational organizations capable of developing worldwide strategies for the production and marketing of their technology.

This notwithstanding, I hope that these organizations do not oppose the suggested course. An accepting attitude on their part would be convincing evidence that multinational corporations are willing and capable to reconcile their efforts for maximizing their opportunities with the loyalty they owe to the policies of the host countries. In our case the host countries are members of a community.

Another problem causing concern to the Commission is the multiplication of State subsidies. These are granted to industrial sectors threatened by market modifications or by new technological processes, and to plants operating in areas facing difficulties, either because of underdeveloped or obsolescent industrial structures, or because their natural economic cohesion is cut across by political frontiers.

Chairman BOGGS. Mr. Colonna, I do not want to cut you off in any way, but would you summarize the balance of your statement so that all of the——

Mr. Colonna. Yes; I shall do so. Shall I have 5 minutes more? Is that all right?

Chairman Boggs. Yes; 5 minutes.

Mr. Colonna. Five minutes. Very well.

In many instances the powers of the Commission to resist this trend and to enforce a common discipline are limited. The risks entailed by this trend are obvious. Competition between the markets would be put in jeopardy. Needed resources would be wasted. The transition to more remunerative activities would be discouraged. Again, the question arises what would be the attitude of the subsidiaries of multinational corporations? These today can draw advantage from their bargaining power in relation to national authorities for securing facilities of this kind. It should be hoped that they would play in favor of the consolidation of the Community and against national selfishness.

Finally, the Commission suggests that the Community should have a policy of industrial structures, allowing for structures to develop in the Community which would tend to have the same strength and the same potential as their competitors throughout the world and subsidiaries of the corporation active in the Community.

There are a number of reasons why so far corporations of this kind and strength have not developed within the Community and in my statement I go into explaining why this is so. But it seems to us that this is a situation which must be corrected because otherwise in the end, in the overall relationship between the Community and the United States, there shall be a fundamental imbalance because the community is represented in foreign markets more by its exports than by its subsidiaries. The Community is in a fragile situation in relation to any restrictive policy with regard to imports that would be introduced in any of its important export markets.

We must, therefore, strive, without having any recourse to protectionist practices, to develop within the Community structures that are capable to compete with the great organizations which have emerged in the United States with their subsidiaries on the Common Market and on third markets.

I should stress in this respect, Mr. Chairman, and this is going to be my conclusive word, two points. First, that in suggesting the means to achieving this objective, the Commission has never suggested or encouraged policies that could be described as a protectionist. We know the value of American investment in the Community. We appreciate the advantages that have accrued to us from these investments. What we want is to reach a better balance and we want to achieve this better balance with a view to maintaining open the avenues to a further expansion of international investments and foreign trade.

My second point, Mr. Chairman, is that, however, the activity of multinational corporations, the flow of direct investments across the boundaries, does create a number of problems that must be attacked objectively. There are a number of these problems. I submit that because of the specific importance that both the United States and the community have in respect to these problems, it would be very advantageous if an appropriate framework would be devised where we could discuss these issues alongside with any other issue arising in the context of relations across the Atlantic.

A newspaper widely read in Europe, published by an American firm, carried a headline a few days ago indicating that the Community and the United States are at the brink of a trade war. As a man that is convinced that fundamental interests across the Atlantic run in the same direction, I do not think that we can and must speak about trade wars.

Chairman BOGGS. On that note, I must agree with you completely. A trade war——

Mr. COLONNA. That was my concluding remark.

(The prepared statement of Mr. Colonna follows:)

PREPARED STATEMENT OF GUIDO COLONNA DI PALIANO

It is a privilege to be invited to participate in the hearings of your Subcommittee and I am grateful for the honor.

A great deal of information has already been contributed to this Subcommittee by highly-qualified persons on international investments and the multinational corporation.

I shall for my part endeavour to highlight the connection existing between this modern form of industrial organization and the process of economic integration in Western Europe. Special problems do arise when multinational corporations are active in the European Community and investment flows into states which have agreed to become a single economic entity.

My views are based on my experience as Member of the Commission of the European Communities; a position which I have held until a few weeks ago. They are based largely on the findings and the proposals outlined in a memorandum on the industrial policy of the European Community which was prepared under my responsibility and presented last spring by the Commission to the Council of Ministers.

However, the opinions which I express here are my own.

(1) It is important that ideas and policies developed in Brussels should be appreciated in regard to the overall objective which we want to achieve in Europe. Members of the Subcommittee are no doubt aware of the purpose for which the process of European integration was launched twenty years ago. The aim was and still is that Europe acquire, through the gradual integration of the free and democratic nations of the continent, the strength required to bear its share of responsibility in the world.

Consistent with this design, the productive structures of the member countries should take legitimate advantage of the creation of the Community in order to meet larger and larger doses of international competition over the wide world.

Twenty years of effort have had positive results. A new reality, distinct from its national components, has come into existence. A customs union has been achieved; a network of common rules has been agreed upon and is being enforced.

(2) This new reality has been beneficial to us and to our trading partners in the world.

Total trade between the Community and the United States today amounts to some $15 billion—three times as much as in 1958.

From 1958 to 1967, the United States had a large surplus—averaging $1.2 billion per annum—on its trade account with the Community.

In 1968, a very rapid expansion of domestic demand in the United States led to an exceptional growth of imports. But again in 1969, the Community was in deficit with the United States in excess of $1 billion. Exports from the United States amounted to $7 billion and those from the Community to $5.8 billion.

Direct international investment has become a very significant alternative to visible exports for producers who expand their outlets beyond the national frontiers.

Since 1958, direct investments by American firms in the Community increased nearly fivefold. The capital for these investments comes very often from issues floated in Europe and the return on these investments has become not insignificant in regard to the balance-of-payments.

Thus the Community has been, from an overall point of view, beneficial not only to ourselves but also to our trading partners. We in Europe have achieved a marked improvement in our standard of living. But the internal demand resulting from this improved situation has been available also to our external competitors.

The Community is indeed bound to pursue outward-looking trade policies because of its structural dependence on world trade in the formation of its national product. Trade accounts for nearly 20 percent of its gross national products, while in the United States the corresponding figure is only 7 percent.

(3) Let me outline very briefly our current ideas and plans for the further development of the Community.

A customs union is not sufficient to secure a free circulation of all goods and services. Total freedom can be achieved only through the elimination of a number of non-tariff barriers. The removal of these barriers can be accomplished only through a complex process of harmonization of national rules and regulations. A great deal remains to be done in this respect.

May I stress that we are aware that non-tariff barriers, whether administrative rules and regulations, fees, health and safety standards, technical norms, or public procurement procedures, also affect trade with our external partners. The Community cooperates actively in the GATT to this end. Whenever possible, those solutions to our own internal non-tariff barrier problems are sought which are likely to be compatible with wider international frameworks. The elimination of these barriers at a world level will require considerable effort and good will. In the meantime, our own internal efforts of harmonization will also be beneficial to our external partners because they will be able to deal with a single set of rules and regulations, whereas at present there are six.

(4) A common market, as outlined by the Rome treaties, is not only a market within which goods should circulate in total freedom; it is also an area in which productive factors can be organized by managers with a view to achieve greater efficiency, irrespective of the political boundaries separating the member states. Labor and capital should be allowed to circulate freely, and corporations should enjoy the right of establishment in any part of the Community area.

Once again this implies the harmonization of different national legislations.

(5) Finally, the Community must consist not only of a common market but also of a set of common economic policies. The founders of the Community foresaw that, lacking the required degree of harmonization of national economic policies, there could be no guarantee of economic stability in the Common Market. Here again it is recognized that, with the exception of the agricultural policy, progress has been so far limited.

(6) The Community is, therefore, a reality, but it is still in the process of completion. This lack of fulfilment does not, however, justify pesimism over the chances of our ultimate success. We face real and objective difficulties; we are fully aware of these, and we are determined to overcome them.

The elimination of non-tariff barriers, the establishment of a common legal, fiscal and financial framework and the harmonization of the national economic policies cannot be carried out by the application of automatic rules, such as those which have brought about the establishment of the customs union.

Every step in this direction results from a specific agreement among the governments of the Member Countries in the Council of Ministers. It is up to the Commission to submit proposals which are objective and realistic and which reflect the common interest: but it is up to the Council to take decisions on them.

Government representatives in the Council reflect the attitude of their respective countries concerning any issue under discussion. It is not surprising that these attitudes very often differ. The notion of common interest is a subjective one and likely to be influenced by local considerations and preoccupations. This Subcommittee no doubt appreciates the problems of reconciling the general and the local interest and the short and longer term interest.

It is the duty of the Commission to fight for decisions which are as consistent as possible with the common interest. Sometimes, imperfect compromises are better than none at all for they can be the stepping stones for further and better decisions.

This is the way in which I look at the common agricultural policy, an area of Community activity which is subject to serious criticism in this country and elsewhere. Special treatment for agricultural products in the customs union was an essential condition for the establishment of the Community. It was dictated by political, economic and social considerations.

The achievement of a common market for agricultural products meant the harmonization of six different national policies in support of agricultural prices.

The results can be readily criticized: but this stage had to be reached in order to embark upon the next one—the launching of the program known as the Mansholt plan, having as its objective a new common European agricultural policy less costly for the taxpayer, more evenly rewarding for the producer, and more acceptable to our trading partners in the world.

Far-reaching endeavours are inevitably subject to periods of stagnation and crisis. What matters, however, is that the sense of progress should not be lost. In our case it was not.

The Community has survived a series of crises, the last of which was concluded by the summit meeting held in The Hague last December. It was agreed in this meeting to hasten the process of internal consolidation of the Community, to set forth as a new objective the establishment of an economic and monetary union, and to open negotiations with Great Britain and other applicant countries.

(7) As a result the Community is now in a new phase of intensive activity along four main directions:

(a) Discussion of the Mansholt plan for a reform of the common agricultural policy;

(b) Discussion of the memorandum on a common industrial policy;

(c) Discussion of a program of action to achieve economic and monetary union before the end of the present decade;

(d) Negotiations with the applicant countries.

These four groups are closely interrelated.

In order to correct the imbalances and deficiencies of the present common agricultural policy, new industrial jobs must be created. This requires the promotion of a sustained industrial development in the Community. The development must be so conceived as to permit the productive structure of the Community to face international competition in its various forms.

Since the industrial structure of the member states differs in terms of relative strength, the absence of a harmonious industrial development within the Community would hinder the achievement of an economic and monetary union, and indeed would jeopardize the very existence of the customs union.

As concerns the enlargement of the Community, it would seem that the desire of the applicants, in particular Great Britain, to join is proportional to prospects of greater vitality and internal consolidation of the Community.

The problems which the present common agricultural policy creates for Great Britain are well known: hence the importance of the Mansholt plan. The advantages entailed in the participation of Britain in the customs union offers are limited for British industry. However, British industry attaches great importance to a coherent industrial development strategy from which it could benefit widely.

(8) The industrial policy which the Commission suggests consists of a gradual approach that should promote European industrial and technological development with a view to a continuation of the present expansion of international trade and investment.

The Commission regards as a first and urgent step in this direction the achievement of the common market as a common outlet for all goods and services. This implies *inter alia* the liberalization of public procurement policy throughout the Community. Public procurement of goods produced in other member countries is at present negligible.

Government procurement is bound to increase rapidly as a result of the explosion of social demand. It is therefore important that the *de facto* preference granted by national authorities to their own industries should come to an end. The Commission has the authority and the duty to enforce the rules for the Treaties against discrimination practices. But national public procurement procedures, particularly for certain sophisticated products, are such that the enforcement of the common rules is not always easy or even possible.

It is urgent to make a start with the products of certain technologically advanced sectors for which the procurement procedures allow the greatest degree of discretion to the public purchaser. Most of our nation states are anxious, for a variety of reasons, to promote within their boundaries industrial activities in the advanced, technology-intensive sectors. The main motivation for this attitude is the fear that otherwise their industry would be cut off from the rewards which the industrial exploitation of technological progress holds in store for those who are capable of exploiting it and are trained to do so.

In my opinion this is a legitimate preoccupation. However, the individual states of the Community do not have the size required for the emergence of productive structures capable to engage with ultimate success in lines of production requiring a large financial and managerial potential and for securing an internal outlet of the appropriate dimensions.

Governments tend to explain their restrictive attitude to regard to the admission to tenders of extra-national competitors by insisting on the need of securing at least a partial return for their investment: this investment is in the form of support given for R&D activities.

Thus the Commission suggests that the problem of liberalizing public procurement in these advanced sectors should be attacked at two levels: at the time when the support is provided and when the goods become available.

(9 First of all, the Commission suggests that R&D activities in certain technologically-advanced sectors should be financed by the Community. This would limit from the outset the inclination of the national authorities to reserve their market to their own industry. Community support granted on the basis of joint selective decisions, could also be used as an incentive for encouraging industrial firms of different member states to form joint ventures of long duration. This would be a very good way to exploit the availability of the Community as an area of continental dimensions.

The Commission suggests further that the cognizant national authorities agree to compare and dovetail their medium-term purchasing programs for certain items with a view of transferring larger and larger portions of the consolidated program of procurement from the present restrictive practices to non-discriminatory procedures.

The response of the European firms to these proposals is still to be assessed. The choice between the short-term advantages of protectionism and the long-term advantages of free competition is always a difficult one.

Insofar as the authorities are concerned, their response appears to be generally positive but cautious; some time will be needed before reaching any conclusion.

(10) The question that arises in regard to subsidiaries of the non-European corporations active in the Community seems to be the following: "How will they react to these suggestions; how will they use the influence which they can bring to bear on national authorities?" I feel that they have a great chance in respect to these and similar issues through the consolidation of the Community rather than in the present fragmented state of the market.

At present, the subsidiaries of non-European corporations are in a position to share, together with the national industrial activities (when these exist), the advantages of national preference in public procurement, at the same time being part of powerful multinational organizations capable of developing worldwide strategies for the production and marketing of their technology.

This notwithstanding, I hope that these organizations do not oppose the suggested course. An accepting attitude of their part would be convincing evidence that multinational corporations are willing and capable to reconcile their efforts for maximizing their opportunities with the loyalty they owe to the policies of the host countries. In our case the host countries are the members of a Community.

Another problem causing great concern to the Commission is the multiplication of state subsides. These are granted to industrial sectors threatened by market modifications or by new technological processes, and to plants operating in areas facing difficulties, either because of underdeveloped or obsolescent industrial structures, or because their natural economic cohesion is cut across by political frontiers.

In many instances, the powers of the Commission to resist this trend and to enforce a common discipline are limited. The risks entailed are obvious: competition between national markets where industry is treated differently by the authorities could become intolerable; much needed resources are wasted in support of less rewarding activities, and the transition to more remunerative ones is discouraged.

The Commission feels that this trend will be gradually reversed; industrial reconversion and regional problems should be considered as affecting the Community as a whole and solved accordingly.

It would be very desirable if subsidiaries of multinational corporations maintained policies favoring a consolidation of the Community and against national self-interest, even though this posture could reduce bilateral bargaining power with the national and local authorities.

(11) The Commission suggests also the establishment of a common policy for industrial structures. Industrial structures in highly industrialized societies tend

to oligopolistic situations, as the relevant market goes beyond the national boundaries. Industry in the six countries of the Common Market could not but follow this trend, and the creation of a customs union acts as a powerful incentive in this direction.

However, in the past concentration in the Community has, as a general rule, either been restricted to firms of the same nationality or to mergers with firms having the decisional center outside the Community. Concentration between firms belonging to different member countries has been the exception rather than the rule. This trend is inconsistent with the objective of developing a competitive industrial structure in the Community.

Concentration restricted to a national area cannot lead to the optimum conditions required in certain advanced sectors. Concentration through mergers with multinational corporations based outside the Community often tends to increase the competition to which the Community is exposed, without directly reinforcing her competitive strength through the improvement of her structural conditions.

But this is not all: the emergence of national industrial empires controlling the largest share of the national production in any given field could inevitably work against the ultimate objectives of the Community which is the fusion of its national components into a single political entity. The current trend would increase the danger that competition between firms irrespective of their nationality which is the basic principle on which the Community is based degenerates into competition, rivalry and potential hostility between member states.

This is the reason why the Commission stresses the urgency of joint decisions to establish a common legal, fiscal and financial framework conceived for a common market of continental dimensions.

There is no lack of ideas in this respect. The Commission seeks the political will required to translate these ideas into concrete action. Such a common framework is indeed an essential condition for making transnational cooperations and mergers within the framework of the Community available also to the medium-sized industries, which most of all feel the need of achieving more competitive structures.

(12) The Commission has been promoting, for years, the creation within the Community of a new "Statute of the European Commercial Corporation," which would enable companies engaged in industrial, commercial and banking activities in the six countries to be subject to identical corporation laws and also to one single jurisdiction.

The Commission recognizes, however, that the absence of a common body of laws, although an important factor, is not the only explanation for the present situation and trend. National authorities are vested with the power of deciding, on behalf of the overall national interest, whether or not a merger can take place and the conditions thereof. The Commission suggests that these discretionary powers should be gradually transferred from the national level to that of the Community.

Government are invited to start with periodical discussions on the criteria whereby they exercise these powers. The matter is not whether national authorities should have more or less discretionary powers than those which they now have in order to influence the way whereby industry can achieve more competitive structures. This is an option which is bound to remain open: policies in this respect shall be more or less liberal according to the prevailing trends in responsible public opinion.

The Commission has suggested various means to encourage transnational mergers within the Community, such as loans granted by the European Investment Bank to corporations in several different member countries—since this type of merger is more complicated and expensive than that between corporations of the same country. These loans could be supplemented as required by guarantees financed from the budget of the Community: the Bank might even be authorized to acquire, for a limited period of time, stock of the merging corporations.

The Commission does not advocate the transfer of nationalism and protectionism to the Community level, since it is firmly against nationalism and protectionism of any kind. The task of the Commission is to persuade the member states to achieve fully Community goals according to the initial design and without reservations.

(13) The Commission appreciates the invaluable contribution of non-European corporations, in particular U.S. corporations; with their investments in the Community these have, in fact, favored an expansion of our economies, an increase in our employment level, the adjustment of our regional imbalances, and

finally, the enhancement of our capacity for a rational utilization of innovation and technological progress and our disposition ot acquire modern managerial techniques.

But precisely because the benefits entailed in international investments, in particular American investment, are so attractive, the Commission is concerned lest they become the origin of disruptive forces within the Community.

Thus the Commission advocates that the Community and not national and local authorities be vested with whatever responsibility is entailed in the control of these investments.

(14) I am aware that the approach recommended by the Commission in the memorandum on industrial policy raises practical questions as to the treatment of the subsidiaries of corporations based outside the Community.

I have mentioned a few of the points where there appears to be a connection between our proposed common industrial policy and international investments; there are others, of course, for instance in the field of finance.

It seems to me that these matters are so important in the overall context of the relations between the United States and Europe, and for the further development of the European Community, that they could very well be a particular subject of discussion between the two parties within an appropriate framework.

I would like to say at this point, as a former member of the European Commission, how much I appreciate the activities of this Subcommittee and how timely they are. But a few days ago an American newspaper published and widely read in Europe carried a headline stating that the United States and the European Community are on the brink of a trade war.

This is not pleasant reading for anyone convinced as I am that there is a fundamental and indivisible identity of long-term interests between the United States and Europe. One cannot but feel that the conflicts which are at the origin of the present situation are of limited relevance when related to the global relationship across the Atlantic. I do not mean to say that these conflicts should be disregarded because they refer to limited economic sectors in the United States and Europe, representing only a marginal factor in the creation of wealth in our respective countries.

In fact, the isolated consideration of sectorial issues may reach such a level of intensity as to create new and far more serious problems. In a climate of sophisticated interdependence, one in which highly industrialized societies must secure their evolution, all issues hang together: and this goes also for international investments.

(15) I would propose that we Europeans should persuade our American friends to help redress an unbalanced situation by placing these problems in a global context.

Our industries are far more apparent on foreign markets with their visible exports than with their subsidiaries. As a result, Europe is more vulnerable to any restrictive measure of international trade which may be taken by our trading partners. This also means that we cannot, in any comparable degree, surmount tariff and non-tariff obstacles, take full advantage of public procurement, adjust our production to the specific circumstances of any given market. We cannot, in other words, benefit from the same advantages enjoyed by our American competitors.

Furthermore, earnings from international investments are a welcome contribution to the positive side of the balance-of-payments.

We are no doubt responsible for this shortcoming: we must try to correct it, making full use of our Community and without indulging in sterile protectionist practices. The final outcome would render us more competitive also at the level of international investment, thus allowing us to cooperate for a continuation of free-trade economic policies throughout the world.

We could certainly use a discussion of this kind also to exchange information and consult with each other on the problems of antitrust policies connected with international investment. In fact, the problem of political control of corporations which, because of their worldwide operation, do not fit precisely in any national legislative framework, and tend to appear—even without justification—at odds with national or regional economic development programs, cannot be but settled through negotiations between the two most industrialized areas in the world.

(16) The outcome of these talks could be an improvement of what appears to be the most efficient instrument of development in an advanced industrial society.

Multinational enterprises were born to utilize with ever increasing efficiency resources such as raw materials, capital, management, and research. But how many of these corporations can rightly be called "multinational," and how many are instead merely large enterprises which limit themselves to operating on various markets?

An enterprise is truly multinational when not only its body of stockholders is at the international level, but—all the more important—when the investment and the market strategies are set forth by decision-making organs of a multinational nature.

Only an internationalization of these top-level organs can guarantee a fulfillment of the responsibilities assumed by the multinational corporations toward the countries in which they chose to operate.

Chairman BOGGS. Now, if we may hear from Dr. Kindleberger.

STATEMENT OF CHARLES P. KINDLEBERGER, PROFESSOR OF ECONOMICS, MASSACHUSETTS INSTITUTE OF TECHNOLOGY

Mr. KINDLEBERGER. Thank you very much. I am grateful for the opportunity to put forward my views on the need for some machinery to resolve differences of viewpoints between governments, and if possible to harmonize attitudes and action, toward what is variously called the multinational, international or transnational corporation. The world has machinery for the settlement of questions regarding policy in macroeconomics, money, trade, foreign assistance, lending, and similar issues. Questions involving action by a corporation of one nationality in another jurisdiction are sometimes ignored and sometimes the subject of diverging action by two or more nations. The basic rule embodied in U.S. treaties of friendship, commerce, and navigation, that all foreign corporations shall be given national treatment except in some restricted fields such as banking, transport, communication, is frequently violated in practice.

Foreign nations discriminate against U.S. corporations on the one hand, and the United States itself is unwilling in its turn to leave American corporations to the mercies of the Calvo doctrine which holds that foreign corporations in a national jurisdiction cannot claim the support of their home governments, but must be content with local justice.

My conviction that some machinery would be useful rests to some degree on Galbraith's view of countervailing power. You will recall that this suggests that as the corporation rose from the locality to regional and national power, it was necessary for trade unions to become national and for the Federal Government to acquire strength to prevent corporate domination of the economy. I am not suggesting that the international corporation, often but by no means exclusively American in origin, is exploitive or dominant or dangerous. It is simply that there will be some number of instances, perhaps few, when private profit must be subordinate to broader considerations of national purpose, in this country and in others. Where two or more purposes clash through the corporation, or where on the contrary, the corporation is able to evade a reasonable national purpose of one country by seeking another jurisdiction, there is need, in my judgment, for machinery to work out a reasonable solution.

Note that the recommendation is for machinery, not rules. This is because in this field, as in most of industrial regulation, circumstances alter cases. To use an illustration that I have given before, it is one thing for General Electric to take over Machine Bull in France, but it would be quite different if IBM were to do so. In the one case world competition in computers is enlarged; in the other it would be reduced.

It is also for some machinery, not a great deal. There is a wide spectrum of opinion in this field. At one extreme, Seymour J. Rubin, my former colleague in the Department of State, whom you are going to hear later in the week, has argued that there is no problem likely to arise in this area that cannot be settled through the ordinary channels of diplomacy.[1] On the other hand, the distinguished former Undersecretary of State, George W. Ball, recommends a system of world incorporation which would submit international corporations to a special form of world law.[2]

My suggestion, for what it may be worth, is to steer between these extremes and to focus on a few troubled issues, but only a few, in the hope that if progress is made, and further problems arise, the machinery developed can be extended.

A vast number of problems should be excluded, especially those which fall within the national jurisdiction. I am not interested in modified or common law rules on hiring local labor, access to local means of finance, nationalization, and similar questions which involve primarily one government and one firm. The International Bank for Reconstruction and Development is concerned with working out a code of conduct in some of these areas, though with little hope of success, in my judgment. These are matters on which I am content to let competition develop standards. Any country which applies too harsh a rule will find itself unable to get access to foreign management, capital and technology in direct investment. I would expect that the less-developed countries would in the first instance be unwilling to join the organization here proposed though they would be welcome if this guess is wrong. Perhaps as in trade, with GATT and UNCTAD, there is need for a double standard, one for developed countries and one for the less-developed countries which they ultimately outgrow.

For the moment the GATT for international corporations that is envisaged might be concerned with five problem areas: taxation, balances of payments, export controls or trading with the enemy, antitrust, and the issuance of securities. In taxation a good deal of the work is done by double-taxation agreements, but these could readily be generalized so as more nearly to harmonize income definitions, if not rates which competition seems to be leading to convergence. Double taxation is one problem, in which one can expect to hear from the subject, but zero taxation where a company threads its way between jurisdictions so effectively as to escape both is less likely to be called to notice. A GATT for the international corporation might be an effective organization for bringing pressure on a few jurisdictions such as Luxembourg, the Bahamas, Panama, and some Swiss cantons, to attract business by remitting normal levies. The attraction of Delaware and Hoboken, N.J., for national corporations in this country waned as the Federal income tax took over.

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[1] See S. J. Rubin, "The International Firm and National Jurisdiction," in C. P. Kindleberger, ed., The International Corporation, Cambridge, Mass., MIT Press, 1970, pp. 179–204.

[2] See G. W. Ball, "Cosmocorp: The Importance of Being Stateless," Columbia Journal of World Business, November–December 1967.

In a world of mobility, moreover, States must protect themselves against the tax concessions of other States by offering the same terms, thus eroding the tax base. The less-developed countries receive much advice suggesting caution in tax bargaining with foreign companies lest they give away too much. Here is an area in which international consultation on a continuous basis may be useful for developed and undeveloped countries alike. And the international corporation which was subject to double taxation could use it as a forum in which to raise the question of relief.

The balance-of-payments issue is one of double jeopardy: one country such as the United States telling a firm to bring home profits, or to invest abroad, but not to take money, whereas the other has rules against profit remittances, let us say, or requires both investment and money from outside. I must confess that the problem is perhaps more theoretical than real. In a given situation it will be clear which country is in the more trying balance-of-payments difficulties, as it was when Under Secretary of State Katzenbach informed then Premier Michel Debre that the United States was about to impose foreign exchange regulations on January 1, 1968. But there may readily be difficulties in overlap between foreign exchange regulations, and there is merit in machinery to resolve them.

The trading with the enemy problem is one which has excited especially Canada, Belgium and France in the past. This occurs when the United States tries to stop subsidiaries of U.S. corporations abroad from selling to Cuba or China, when those companies come under another jurisdiction which may have a different policy. More generally, it is seeking to require foreign subsidiaries of U.S. firms to adhere to the purposes of U.S. foreign policy rather than the policies of the country where the subsidiary is located. An early and famous example was the U.S. requirement that IBM not sell a certain computer to the French atomic program since the Government of France was opposed to nonproliferation of atomic weapons. It seems evident that there will be more problems of this sort unless foreign policies converge. It would be useful to have a forum for their resolution.

The most troublesome area is in the field of antitrust. Here the United States has tried to get other countries to adopt its policies in the draft charter of the International Trade Organization of 1948, in a United Nations effort under Sigmund Timberg, in the Constitution of the Coal and Steel Community, and in the Rome Charter of the European Economic Community. Occasions arise from time to time when U.S. courts seek to subpena documents in other jurisdictions in connection with antitrust suits here. The Congress of the United States has felt strongly on this issue at many times in recent history.

But the problem does not arise soley from the fact that U.S. policy in the antitrust field has been more positive, or perhaps more negative, than that of other countries. There are real issues for the international corporation as to whether particular takeovers which reduce world competition should be allowed, or whether one country's policies in the antitrust field should reduce competition in another country. Recently a Canadian Royal Commission on Farm Machinery Prices disclosed that British law allows the farm machinery industry to forbid sales of machinery for export to Canada, not only by dealers, but also second-hand, by individuals who buy from dealers, making it impossible for Ontario farmers to buy combines in England at a saving over Canadian prices of $1,400 after paying for transportation and extra commissions.

One substantial problem which will probably need international attention relates to the tendency in many industries for various companies to feel need to be represented in every market, with the result that a number of small countries find themselves with the same eight or 10 companies that compete in the U.S. market, struggling for business in a marekt one-fiftieth the size, each plant small and each inefficient. In a number of countries and industries, steps are being taken by national policy to reduce numbers and achieve more efficient scale. whether by subsidies to one, designation of a chosen instrument, or other device. International decisions on appropriate sorts of solutions may be helpful. It concerns the United States: A recent example of the tendency of various competitors in an oligopolistic industry to want to be represented in every market is the current entry of a new set of European and prospectively Japanese firms into the U.S. market.

In the security field, a recent amendment to the Securities Exchange Act requires foreign issuers whose shares are held by 300 or more U.S. persons to register with the Commission even if their securities are traded only on the over-the-counter market, the issuer did not seek to have his securities listed, and took steps to prevent them being traded. Another question arises where foreign investment trusts operate abroad without selling to U.S. investors in an effort to avoid SEC supervision, but may transgress U.S. rules by operating as an insider—with more than 10 percent of the common stock of a single registered corporation. In the long run it may be intolerable to have securities issued in the Euro-bond market with jursidiction responsible for the protection of investors from the effects of security manipulation. At this early stage in the development of the market, the borrowers are almost entirely large corporations with an international credit rating, borrowing from sophisticated investors. As the market continues to develop, this may no longer be true.

My suggestion, which I have elaborated with a young lawyer, Philip Goldberg, in a paper to be published shortly in Law and Policy in International Business, put out by the Georgetown Law School, is that the U.S. Government take the lead in convening a conference of experts to propose agreement on a few simple principles plus machinery by applying them in particular cases which are put to it by governments or by corporations. The beginnings should be modest, but I would envisage that with time, there could develop a forum for the resolution of problems affecting the international corporation rather similar to GATT in the field of trade. The international corporation is here to stay, I believe, and it will present in the future more rather than fewer problems. I suggest it is utopian to try to answer all the problems it raises at one fell swoop, with an international code, and naive to think that all the issues can be dealt with ad hoc.

Thank you very much.

Chairman Boggs. Thank you very much.

We will now hear from Mr. James W. McKee, Jr., who is president of one of the great international corporations, CPC International, Inc. Mr. McKee has a splendid reputation in the business community and we are very happy indeed, to have you here, sir.

STATEMENT OF JAMES W. McKEE, JR., PRESIDENT, CPC INTERNATIONAL, INC.

Mr. McKEE. Mr. Chairman and members of the subcommittee, thank you for inviting me to contribute to your consideration of one of today's most important economic issues—the role and impact of the multinational corporation on the United States and the world economy.

I have a prepared statement for the record, but with your agreement, I will present only a summarized version this morning.

Chairman BOGGS. We would appreciate that so that we can go on with the panel, but the full statement will be incorporated in the record. Let me say at this time, any of you gentlemen who care to add to the record after the panel is concluded, we will be happy to have that for the record as well.

Mr. McKEE. Thank you. I have seen at first hand how the multinational company generates economic development, capital, jobs, products, services, technology, and how it creates understanding and common purpose through cultural and educational exchange in the movement of people. In so doing the multinational corporation serves not only the specific interest of the host countries but also of the base country. The United States, as the home base for most of the world's leading multinational companies, is benefitted both directly and indirectly. I made a special point of this because there is concern expressed both here and abroad about the multinational company. On the one hand, there is the fear of the host that the base country through the so-called exploitation of multinational companies committed to its different policies and laws, challenges their sovereignty. They may feel threatened with a loss of control over their economic resources or even their political destinies.

There is also the somewhat contradictory fear that the multinational company, as it divorces itself from any particular national, cultural, moral or legal code, will no longer be subject to any control.

Although there may be some exceptions, I contend that both these fears are unjustified. While any multinational company will conduct itself consciously or unconsciously according to its heritage, it must recognize that to be able to perform its economic function, it must attempt to accommodate to the policies and laws of the base and host countries to the satisfaction of each, or violating these, it will eventually be forced to limit or to cease operations in one or the other.

The aim of the multinational company is, quite forthrightly, to become more completely multinational in terms of its people, its capital, and ownership. Under these circumstances, it cannot afford to be irresponsible.

The U.S. multinational company has made a positive contribution to the United States. It has increased wealth, and the international assets of the United States. It has had a generally stimulating effect on the U.S. economy and U.S. jobs. American direct foreign investment has made substantial contributions to U.S. income through the repatriation of profits, royalties, fees for licenses, engineering and management services. The figures are well known to the subcommittee so I will not repeat them here.

It has been argued that investment abroad should be made less attractive. I do not agree. Different risks attract different types of investors and if the climate for investment in St. Louis is not right and a good profit does not seem likely for a specific investor, the fact that investment in France is made less attractive to him, does not suddenly make the investment in St. Louis more so. Furthermore, even though investment abroad by American capital may be discouraged, the investment opportunities will still exist, and will likely be taken over by other investors.

There is abroad agreement that the value of American foreign investment has been hurt by U.S. controls. Although most large U.S. multinational companies have been able to make their peace with these controls and have continued to grow abroad, there is no question that they have had a distorting and limiting influence.

It has also been argued that investment elsewhere costs American jobs. Certainly, in our own industry there is no export of jobs as a result of our investment abroad.

Although we continue to try to increase exports, the economies of our business dictate that the only really effective way we can compete in other markets is by direct investment. We could not rely on exports to produce anything like the income—and the balance of payments contribution—that has been generated by our investment abroad.

In fact, investment abroad often generates jobs in the United States. It can create a direct and particular demand for U.S. made plants and equipment, fabricated semifinished products and parts, and U.S. raw materials. In our own case, our overseas wet milling operations result in substantial exports of corn, 50 million bushels worth $70 million in 1969 alone.

The benefits brought to its host countries and to world economic growth by the multinational company should be considered an additional benefit to the United States to the extent that our national interests are identical with those of other nations.

I can be specific in pointing out some of the benefits of a multinational operation in our company's investments in several developing countries. We entered Latin America in the late 1920's and early 1930's. We entered Pakistan only 8 years ago. Yet, there is a similarity to the pattern and the results. In all cases, our original investments were in corn grinding operations at a time when starches were becoming important adjuncts to developing industries. Our development of the corn starch industry contributed in many ways to the economies of host countries. We created jobs which had not existed. We provided cash markets for local corn. We provided trained agronomists to teach farmers more modern corn cultivation techniques and in each case, developed new hybrid seed suitable to growing conditions in the different locations. Without our 40 years' experience in Latin America, it would have been difficult to make these accomplishments in only 8 years in Pakistan.

The profitability of those investments has increased the resources of the host countries and contributed to their economic growth through payments to agriculture, through increased payments of wages and through increased payments of taxes. Through remittances, it has contributed to our total corporate resources and to the economic growth of the United States.

In my opinion, the further development of the multinational company will occur as a natural outgrowth, a result of factors operating in the world today which can only intensify in the future.

First, beyond any doubt, markets are more similar today than ever before and are becoming more so. As 19th century nationalism has weakened and countries have opened themselves to the world, cultural differences have tended to dissolve. As the world becomes more truly one market with a similar set of needs and wants, the role of the multinational company becomes indefinitely more important.

Second, as the world shrinks in size it becomes more open. This may not be readily apparent today as protectionist views are being reasserted. But, as Europeans, for example, begin to see that an enterprise in any of the six nations is good for the European Common Market as a whole, so we believe it will become more evident to all that the multinational enterprise serves the common good, and contributes effectively to total economic progress and goals.

Third, industrial output and world trade are growing in scale, and there seems little prospect that this trend will be reversed. As the world grows smaller and as the needs for capital and technology increases, multinational enterprises will increasingly be called upon to look beyond artificial economic boundaries to utilize the efficiencies generated by the diversity of their capital and technology.

Fourth, as the world becomes more open and the markets more uniform, there will still be a lag between progress in one area or country and another. These different levels of development challenge the multinational company to utilize profitably the appropriate level of technology, which it has tested in similar economies elsewhere. In this way, the world's resources are more efficiently used and market demands are met as these grow in size, and diversity.

In my opinion, the multinational company is highly desirable in the broadest sense. It is an instrument of world development, for which this Nation must assume a share of the responsibility and cost. The great inequities of economic opportunity throughout the world must be corrected as one of the important preconditions for world peace, stability, and our own growth. Governments should respect this vast potential and help create the climate in which it can be maximized. Together, business and government must find a way to resolve, by the development of harmonized international business law, the difficulties of being subjected to multiple and often contradictory sets of policies and laws.

These include such areas as antitrust, international tax policy, and securities regulation. Patent procedures should be harmonized and simplified. Common standards of weight and measure, and common food and drug standards, should be implemented more rapidly. The transfer of people should be facilitated.

When we have similar policies and laws governing corporate behavior in all countries, the fear that multinational companies could operate as a law unto themselves will disappear. Nonetheless, they will encounter many difficulties, many dilemmas, in adjusting to their increased responsibilities of world citizenship, while achieving the results expected of them.

I believe business can, in a context of sound Government policy, make a very significant step toward accomplishing these objectives.

Thank you very much.

Chairman BOGGS. Thank you very much, Mr. McKee. I might say that Dr. Longnecker, president of Tulane University in my town, told me of your extraordinary ability and I think he understated the case.

Mr. McKEE. Thank you very much.

(The prepared statement of Mr. McKee follows:)

PREPARED STATEMENT OF JAMES W. McKEE, JR.

Mr. Chairman and members of the Subcommittee, thank you for inviting me to contribute to your consideration of one of today's most important economic issues—the role and impact of the multinational corporation on the United States and the world economy.

CPC International, which some of you may remember as Corn Products Company, is a diversified food, industrial, and chemical products manufacturer. We have operated multinationally through direct investment since 1919, and our export business dates back to 1903. Today we manufacture in 99 plants in 38 nations. Our worldwide sales of $1.3 billion are about evenly divided between the U.S. and abroad.

The question at issue is whether the growth of strong multinational business organizations is in the best interest of the United States or against it.

My statement is based not only on personal, but also our corporate experience. I have seen at firsthand, how the multinational company generates economic development—capital, jobs, products, services, technology; and how it creates understanding and common purpose through cultural and educational exchange and the movement of people.

In so doing, the multi-national company serves not only the specific interest of its host countries, but also of the base country. The United States, as the home base for most of the world's leading multinational companies, is benefited both directly and indirectly.

I make a special point of this because there is concern expressed both here and abroad about the multi-national company. On one hand, there is the fear of the host that the base country through the so-called exploitation of multi-national companies committed to its different policies and laws, challenges their sovereignty. They may feel threatened with a loss of control over their economic resources or even their political destinies.

There is also the somewhat contradictory fear that the multinational company, as it divorces itself from any particular national, cultural, moral or legal code, will no longer be subject to any control.

Although there may be some exceptions, I contend that both these fears are unjustified. While any multi-national company will conduct itself consciously or unconsciously according to its heritage, it recognizes that to be able to perform its economic function, it must attempt to accommodate to the policies and laws of the base and host countries to the satisfaction of each, or violating these, it will eventually be forced to limit or to cease operations in one or the other.

This very process of accommodation, the attempt to satisfy both countries, may be irritating to one or the other, but it is only through the wildest sort of exaggeration that it can be construed as a conspiracy against either country.

The ultimate aim of the multi-national company is, quite forthrightly, to become more completely multi-national in terms of its people, its capital and ownership. Under these circumstances, the multi-national company cannot afford to be irresponsible.

I would like to first give you my views on the impact of the U.S. based multinational company on the U.S. economy and then explore some of the problems surrounding growing multi-nationalism. There are important implications that must be faced not only by U.S. policymakers and the Subcommittee, but also by counterparts in other countries, and no less so by multi-national businesses themselves. In an era in which society seems to demand a greater accountability and responsiveness to society as a whole for individual actions, we will all be required to make difficult, perhaps painful, adjustments.

The U.S. multi-national company has made a positive contribution to the United States. It has increased U.S. wealth, and the international assets of the United States. It has had a generally stimulating effect on the U.S. economy and U.S. jobs.

American direct foreign investment has made substantial contributions to U.S. income through the repatriation of profits, royalties, fees for licenses, engineering and management services.

The returns from our growing foreign investment base have been substantial. The book value of U.S. direct private foreign investment is estimated to have reached almost 70 billion dollars. In 1969, direct investment outflows from the U.S. were an estimated $2.4 billion. Income in 1969, including royalties and fees, was an estimated $7 billion, resulting in a positive balance of payments contribution for the year alone of about $4.6 billion. Though not always as large, the net contribution of the direct foreign investment activities of U.S. corporations has become greater than the net conribution of exports. It has helped in a major way to offset the continuing deficit in Federal Government transactions, which averaged nearly $7 billion annually during the last half of the 1960's.

It has been said that foreign investments are exports of capital that should be invested in the United States. Accordingly, it has been argued, investment abroad should be made less attractive. I don't agree. Different risks attract different types of investors and if the climate for investment in St. Louis is not right and a good profit doesn't seem likely for a specific investor, the fact that investment in France is made less attractive for him, does not suddenly make the investment in St. Louis more so. Furthermore, even though investment abroad by American capital may be discouraged, the investment opportunities will still exist, and will likely be taken by other investors.

There is broad agreement that the actual and potential value of U.S. foreign investment has been hurt by U.S. controls on investment abroad. Although most large U.S. multi-national companies have been able to make their peace with these controls and have continued to grow abroad, there is no question that they have had a distorting and limiting influence.

It has also been argued that investment elsewhere costs American jobs. Certainly in our own industry there is no export of jobs as a result of our investment abroad.

Although we continue to try to increase exports, the economies of our business dictate that the only really effective way we can compete in other markets is by direct investment. We could not rely on exports to produce anything like the income—and the balance of payments contribution—that has been generated by our investment abroad.

Our business generally is in high-volume, low-cost, rather perishable products. Starch made in Illinois, largely because of rail and ocean transportation costs, cannot compete with starch made in, say, Germany. Perishable food products cannot be shipped long distances without very significant loss of quality, or such measures to protect quality as would price them out of the mass market. These and other factors, quite distinct from labor costs, require direct investment.

Investment abroad often generates jobs in the U.S. These investments generally stimulate the ability—and the desire—to purchase U.S.-made goods. Moreover, they create a direct and particular demand for U.S.-made plant and equipment, fabricated semi-finished products and parts, and U.S. raw materials. In our own case, our overseas wet milling operations result in substantial exports of corn, 50 million bushels worth $70 million in 1969. We should also consider that the countries in which the U.S. has its largest investments are the best customers for its exports. Nor should we forget that while there has been a tremendous growth of the multi-national corporation in the past 20 years, there has also been a tremendous growth of U.S. production and employment.

Besides contributing to U.S. income, assets and jobs, the worldwide operations of U.S. corporations have given the U.S. economy greater resiliency and strength. We know, for example, that our worldwide operations cushion the impact on the corporation as a whole of a recession in any one country. This has, in effect, given our total operations more stability which, in turn, contributes to the strength of the U.S. economy.

The U.S. also benefits in terms of technology. We develop new technology worldwide in 12 research facilities in Japan, Europe, and the U.S. That technology is fully shared and used by our operations everywhere. The result is to introduce new efficiencies, and new products, in the most appropriate markets, and so to prosper by serving our customers.

The benefits brought to its host counrties and to world economic growth by the multi-national company should be considered an additional benefit to the U.S., to the extent that our national interests are identcal with those of other nations. But the delivery of these benefits are of primary importance if for no other reasons than that they provide us with our welcome abroad and qualify us to remain in business there, thus making possible our very direct and tangible contribution to the U.S. economy.

I can be specific in pointing out some of the benefits of a multi-national operation in our company's investments in several developing countries. We entered Latin America in the late 1920's and early 1930's. We entered Pakistan only eight years ago. Yet, there is a similarity to the pattern and the results, at least in part. In all cases, our original investments were in corn grinding operations, at a time when starches were becoming important adjuncts to developing industries. Our development of the corn starch industry contributed in many ways to the economies of host counrties. We created jobs which had not existed. We provided cash markets for local corn. We provided trained agronomists to teach farmers more modern corn cultivation techniques and in each case, developed new hybrid seed suitable to growing conditions in the different locations. Yet, it must be kept in mind that without our 40 years' experience in Latin America, it would have been difficult to make these accomplishments in only 8 years in Pakistan.

The profitability of those investments has increased the resources of the host countries and contributed to their economic growth through payments to agriculture, through increased payments of wages and through increased payments of taxes. Through remittances, it has contributed to our total corporate resources and to the economic growth of the United States. As proud as we are of these accomplishments, they would not have been possible without the loyalty and abilities of the local employees who were willing to learn our methods and techniques for our mutual benefit. We find it difficult to believe that we are unique. We are convinced that other companies have had similiar experiences.

Let me turn now to the future, and to the further development of the multinational company. In my opinion such development will occur as a natural outgrowth, a result, of factors operating in the world today which can only intensify in the future.

First, beyond any doubt, markets are more similar today than ever before and are becoming more so. As 19th century nationalism has weakened and countries have opened themselves to the world, cultural differences have tended to dissolve. As the world becomes more truly one market with a similar set of needs and wants, the role of the multi-national company becomes infinitely more important.

Second, as the world shrinks in size it becomes more open. This may not be readily apparent today as protectionist views are being reasserted. But there is a significant move in this direction with the development of regionally free trade within common markets and free trade areas. And, as Europeans, for example, begin to see that an enterprise in any of the six nations is good for the European Common Market as a whole, so we believe it will become more evident to all that the multi-national enterprise serves the common good, and contributes effectively to total economic progress and goals.

Third, industrial output and world trade are growing in scale, and there seems little prospect that this trend will be reversed. As the world grows smaller and as the needs for capital and technology increase, multi-national enterprises will increasingly be called upon to look beyond artificial economic boundaries to utilize the efficiencies generated by the diversity of their capital and technology.

As the world becomes more open and the markets more uniform, there will still be a lag between progress in one area or country and another. These different levels of development challenge the multi-national company to utilize profitably the appropriate level of technology, which it has tested in similar economies elsewhere. In this way, the multi-national company uses the world's resources more efficiently and meets market demands as these grow in size and diversity.

In my opinion, the multi-national company is highly desirable in the broadest sense. It is an instrument of world development, for which this nation must assume a share of the responsibility and cost. The great inequities of economic opportunity throughout the world must be corrected as one of the important preconditions for world peace, stability, and our own growth.

It appears to me then, that the arguments for the multinational company are contained in this larger argument for world development and the growing unification of national economies into a world community.

The multi-national corporation is not only good for the U.S., but for the world economy. Governments should respect its vast potential and help create the climate in which that potential can be maximized.

Satisfying inconsistent demands of the governments of the countries where we operate does create conflicts. Together business and government must find a way to resolve, by the development of harmonized international business law, the difficulties of being subjected to multiple and often contradictory sets of policies and laws.

These include such areas as antitrust, international tax policy, and securities regulation. Patent procedures should be harmonized and simplified. Common standards of weight and measure, and common food and drug standards, should be implemented more rapidly. The transfer of people should be facilitated. When we have similar policies and laws governing corporate behavior in all countries, the fear that multi-national companies could operate as a law until themselves will disappear.

Multi-national companies, themselves, will be the most active protagonists in bringing this about. Nonetheless, they will encounter many difficulties, many dilemmas, in adjusting to their increased responsibilities of world citizenship, while achieving the results expected of them.

The global task confronting industry throughout the world in an overwhelming one. It must utilize in the most efficient manner possible, those assets under its control to contribute to the improved well-being of the environments in which it operates, which in turn will determine its own health and progress.

I believe business can, in a context of sound government policy, make a very significant step toward accomplishing these objectives.

Chairman Boggs. Now, Mr. Polk, with the U.S. Council of the International Chamber of Commerce. He has worked with us for many years. We are very happy to have you here today. I think you certainly are one of the most knowledgeable men in the country on this subject. I would hope that you could summarize your prepared statement so that we can get ahead with the panel discussion.

STATEMENT OF JUDD POLK, U.S. COUNCIL OF THE INTERNATIONAL CHAMBER OF COMMERCE

Mr. Polk. Thank you, Mr. Boggs. The prepared statement you have. In summarizing it, those of you who are following the oral statement might look at the prepared statement.

Chairman Boggs. The prepared statement will, of course, be made a part of the record.

Mr. Polk. Thank you, sir.

The international company to me is interesting mainly for the phenomenon it is a part of rather than for itself. What it is a part of, and it contributes to, is the emergent world economy. This means that as I see it as an economist, we have entered a period where we will be allocating resources on an international basis, that is to say, that just as we are used nationally to investing—committing resources—in accordance with the best national use of those resources, we have now translated really through the superior communications of the world to a world basis for the same allocation. No use of resources is justified if the output can be achieved at a lower cost elsewhere. A corrollary of that is simply that if a cheaper means of making a given product can be found elsewhere, there is also better use of the resources here.

Now, to see how far this process has gone, I have tried with the help of some of the materials this committee has developed, to look at what the gross world output might be and the figures in my prepared statement give a summary. For the first time I have not excluded the Communist countries and here the work of this subcommittee has been helpful in getting comparable figures. Roughly in orders of magnitude like this, with output that is not really very comparable across national borders, orders of magnitude are the most that we can hope for.

The United States with an output very close to a thousand billion dollars, a trillion dollars, constitutes about a third of it. The rest of the "industrialized west"—there is not really a good term for this; it includes the other industrial countries not counting the Communist countries—account for another thousand billion dollars. Russia and the Eastern European countries and a rough estimate for China account for $650 billion and the less-developed countries account for $350 billion.

Now, this is a sort of output profile. You know the population profile which works out at about 3 billion, perhaps closer to 3½ billion now. About a third of the world is in the area that is here ticked off as less-developed and China.

We have a fair basis for inferring what may be the internationalized portion of this $3,000 billion output today. That figure I get at around $450 billion. This includes something over $200 billion, which is the output of investment activities in which the United States is engaged abroad. It includes $100 billion in our own market that is associated with foreign investment here, and it includes a very rough figure, where our indicators are not too good, of $150 billion for other countries' interproduction completely outside the United States.

This $450 billion is par of the $3,000 billion GWP. It represents about 15 percent of the total. It is growing very rapidly. It grows at about 10 percent a year, which is a very solid rate of growth compared to the rates that we are accustomed to, and one could expect that the percent of the world's output that in international would by the end of the century be equivalent to the amount that is noninternationalized.

Now, as against this, the United States like most countries, still takes a national view of its policy and we get very different results from a national view. For instance, we have been most concerned with the balance of payments. I think there are an increasing number of people who find real difficulty in the presently prevailing concepts of the balance of payments. This is an old-fashioned notion really of how to relate the accounts of one trading Nation to another. It makes no allowance, really, for how to relate the accounts of interproducing nations, or the accounts at a country doing international banking.

Concern over the balance of payments has come from a concept of deficit, which I think is fictitious. We have sought to resolve that deficit by all kinds of controls, of which the ones most inconsistent with the concept of a world economy, I think, are our controls on direct investment. We are, I think, seeing in the proliferation of American banking as well as businesses overseas the anomaly of accounting which counts on one side of the fence geographic United States. And on the other side of the fence it counts all Americans who are geographically outside the United States. So, what is counted "foreign" in our balance of payments is really increasingly within the family.

I think we must be very close to the point now where we can erect a balance of payments on a more realistic international basis. Here the focus would be on the international flow of funds. This is the kind of financial information we arm ourselves with in our efforts to analyze the national economy. We look at the sources and uses of funds. In our present balance-of-payments techniques we are failing to pick up enormous movements of the utmost importance, and on the other hand, we give crucial position to movements that relaly do not make very much difference.

For instance, the weekend convenience of a small group of banks can result in a geographic movement of funds that will appear to create a deficit of several billion dollars in the balance of payments. Here, again, I think we must be close to the point of not caring whether companies A, B, and C do their banking in New York or London or Paris or Frankfurt, particularly since they may be using the same bank throughout.

The loosest points, I think, in our interesting interproducing structure throughout the world occur in familiar areas. One is with the less-developed countries, the $350 billion in our production figures here. There is a large amount of production in the less-developed countries associated with international investment. It is historically concentrated on extractive industries more than in the case of international investment in the rest of the world, but I think we must concede that the present array of institutions has failed to provide an environment in which a corporation is fully as productive as it has been in the more industrialized West. Very briefly, it is not possible to do justice to the perplexing character of the problems here and the urgency of them. I think that the fact that we have not succeeded more than we have with the less-developed countries should make us extremely open minded, though, to the possibility of institutional arrangements that would involve on the one hand governmental planning arrangements and on the other hand, the productive corporation or group of corporations.

Similarly, we have not achieved—as yet history has not perhaps quite vouchsafed a political basis for exploration of—broad interproducing arrangements between the United States—and for that matter, the entire industrialized West—and the Eastern world. This is the other area in which the interproducing connections are not at all firm.

I think some of the recent interest shown by Russia in, for example, the arrangements with Fiat, and in the arrangements that Russia asked Ford to take a look at, though nothing has yet eventuated, indicate the possible future development, politics permitting, of the economic relations that could exist on an interproducing basis.

Well, I think the moral of all this is that the United States in seeking the best use of its own resources, must be impeccably international in its policy. It is very difficult for us to discriminate in favor of geographic United States without discriminating against ourselves in activities in which we are already heavily involved abroad.

Thank you very much.

(The prepared statement of Mr. Polk follows:)

PREPARED STATEMENT OF JUDD POLK

We have heard a lot about the international corporation in recent years: from Servan-Schreiber's rather unfair popularization of the notion as an American Challenge, by which is meant menace; to the quiet and thoughtful work of John Dunning, who turns out to be the Mr. X of the last budget speech where Parliament was left with a suggestion to bate their breath on certain aspects of tax policy pending the completion of certain current tasks of Professor Dunning; to the pervasive Canadian concerns about the big international company, particularly of course American companies. This concern reached the level of an expert parliamentary commission two years ago and produced a document that was in effect a reinterpretation of Canada's economic origins and mission in terms of making use of and preventing abuse of the international company's powers. Then there is the wide-front Harvard work in progress covering the behaviour of international companies in an encyclopeadic way.

I think, though, that all of this work is basically a lagging reaction to the impact of the international company on the world economic scene. In fact the international company itself is a reflection rather than a source of a new phenomenon, namely the internationalization of production. The state of industrial technology—and very much including instantaneous world electronic communication and computers—has created the situation in which for the first time men have been in a position to treat the world itself as the basic economic unit in pursuing that core economic problem: making the best use of its resources.

The significance of this fact, namely (to use an awkward word) the worldizing of our housekeeping is immediate, pervasive, distinctive and full of possible upheavals and new departures for our foreign economic policy (and it might be argued right here for our domestic economic policy as well). I would like to devote my brief time here to the nature of these new facts and their most important policy implications. It may be helpful at the outset to mention that many of our major policy directions appear misguided when viewed from the standpoint of the best interests of the United States in an internationalized world of production.

As we inform ourselves about this supposedly new phenomenon, the international or multinational company, we pursue its implications without reference to—in fact often inconsistently with—the really new phenomenon of which it is a part, namely the internationalization of production. The international company is old, as we have every reason to recall when standing on this ground once managed by such ancestors of our modern international company as the Hudson Bay Company and the Virginia Company of London. What is new and important is the degree of cohesion in international production. The scope of these operations inevitably implies an emergent world economy.

THE INTERNATIONALIZATION OF PRODUCTION

In the fundamental task of allocating resources to maximize or optimize yield the question of the economic area whose resources are being allocated is crucial to the question of how best to allocate them. The emergence of a national market in contrast to regional ones, in the United States is an analogous event so recent that even the youngest of us here have witnessed it at least in part. For example, we are currently in a phase of national development in which national resources are being nationally allocated in such a way that the financial capabilities, the technology, the managerial skills and the energies of all regions of the country are contributing to the distinctive pace of development in the West and Southwest. There are many examples; this is only one to suggest the feel of the thing. Any significant use of resources in this country, whether under public or private sponsorship, be it dam or computer services, embraces and answers the question. What is the most effective national, not regional or local, use of the given funds or real resources.

Yet as recently as a generation ago the nation was not the reference area for typical examinations of alternative prospective yields.

It is already the implicit suggestion, now worth putting explicitly, that our commitment to international operations in response to our communications, industrial, technological and, I think one must add, community capability requires us to assess international, not just national, competing opportunities if we are to reach a tenable resource commitment. I say community because the breadth of the borders of the community we think we belong to has a lot to do with the ultimate breadth of the real community we create for ourselves. International business expresses and consolidates a sense of international community. And the existence of our $143 billion investment stake abroad, with its product profile of $220 billion, illustrates the real force to date of the invitation, perhaps economic compulsion, to commit resources to production in an international rather than a national frame of reference.

Self-Imposed Barriers

It is an odd fact that even though we are deeply committed—I think irreversibly—to recognizing a world economic framework in our productive decisions, we are only beginning to get familiar with the implications of world economics. Our governmental policies are often ambivalent and sometimes directly inconsistent with the international character of our producing operations. Our present program of capital controls over foreign direct investment is a case in point. The general program of tightening the reins on American investment abroad began with the Interest Equalization Tax in 1963 (passed by Congress in 1964) and culminated in a mandatory control over Americans' foreign investment activities generally. A good bit of the debate over the pros and cons of these restraints, and particularly the question of whether they would help or hurt the balance of payments, was argued before this Committee and other committees of Congress. I think the Committee will recall the Administration's regular contention that the high and consistent earnings from foreign investment present a persuasive justification for it in the long run, but that particular balance of payments urgencies required some limitations in the short run. As an interested student of foreign investment I got the impression throughout these years, and particularly in connection with the mandatory program, that the Administration's cost-benefit analysis made the decision a pretty close one. An important and perhaps even deciding consideration was more political than economic. This had to do with the regularly expressed anxieties of foreign countries over the extent of American influence—the American Challenge already mentioned—in their economic affairs as implicit in the growing strength of American investment and producing operations. And I have certainly gathered from talking to foreign friends that whatever else the restraints may or may not have done they did tend to lower the American profile at a time when many of them found the sharpness of this profile disconcerting.

Two oddities illustrate the ambivalence of our policy position. In lowering the profile by inhibiting investment we also mobilized investment to respond to Washington directives in just the way that those abroad who were anxious over the profile had as the center of their anxiety. The most notable feature of the program here is the establishment of targets for repatriation of earnings—a directive that went from Washington parent to foreign subsidiary involving the disposition of funds eventuating completely outside of the United States' jurisdiction, and in the hands of companies whose "citizenship" was strictly local, though of U.S. parentage. Neighboring Canada, ever sensitive to pressure from the South, was a case in point for a few days before Canada was exempted from the mandatory controls. One Canadian economic expert, Melville H. Watkins (who also was chairman of the group of experts previously mentioned) referred to this period in the dramatic terms that for a moment Canada saw the power grid light up. The mobilization of any country's subsidiaries abroad raises most touchy issues and, to say the least, does not contribute to a lowering of profile.

The other oddity is somewhat similar. As I have previously testified before this Committee, the artificiality of our balance of payments reckonings, and in particular the calculation and publicization of large scale balance of payments deficits, have seemed wrong to me as an economists. Nonetheless the objective of reducing these deficits has been the main reason throughout the '60s for the various controls over American citizens' business operations arboad. The oddity lies in.the fact that one conventional and perhaps the most usual basis for calculating the alleged deficit counts all of our banking liabilities to foreigners as direct increases in the deficit *without* offset by current accumulations of short term assets. The rationale for this view turned on the fact that our assets, being private in a private system, could not be marshalled to meet our liabilities. The mandatory program demonstrated the ease with which very massive short term holdings of Americans could be marshalled.

Updating Balance of Payments Analysis

Actually balance of payments technique has moved somewhat beyond this point. The balance of payments expert Review Committee's recommendations in 1965 led to a second calculation, a deficit on official accounts. This went part of the distance in balancing the onesidedness just mentioned. But we have now passed pretty much beyond the relevance of this kind of calculation too. Existing balance of payments techniques show up best for a kind of closed national economy related to other economies primarily by limited trade transactions, with bills for any net purchases requiring settlement in an international money. When, however, a country becomes involved as the United States has in very extensive international banking, when its producers have substantial operations all over the world in a variety of currencies, when its own currency is widely used throughout the world for all monetary purposes, then the standard highly selective trade-oriented balance of payments accounting fails to measure these international relations in any meaningful way. The old-fashioned accounting tosses up enormous deficits that are really without meaning and, at the same time, fails to note international credit movements that merit the deepest concern. The minuses and pluses of these balance of payments calculations do not reflect some useful "net" of American transactions with foreigners but rather mix transactions with foreigners together with debts and credits within the American international circle of companies and banks.

The unreality of the balance of payments was everywhere apparent in the lengthy correspondence that my organization, the United States Council of the International Chamber of Commerce, has just conducted with a group of companies on the impact of the investment controls on their operations. The Council has recently reported at length on this interesting correspondence, and I have copies here available for this Committee. The report is concerned primarily with the cumulative difficulties the controls have brought in the way of maintaining the competitive soundness of companies' operating structures abroad and the disadvantageous financial arrangements forced into the corporate design. A persistent note that recurred throughout the correspondence was the sense that the national balance of payments as geographically conceived is very remote if not fictitious to American companies whose branches abroad figure significantly as buyers of exports from geographic United States and sellers of imports to it.

Beyond this, actual experience with the program has displayed to businessmen the mere bookkeeping character of the balance of payments "advantages" alleged as the raison d'etre of the controls. Under the controls the government makes a crucial distinction between liabilities of a bank's New York headquarters and those of its branches in London and Paris, and similarly between dollar funds available to a company in the United States and dollar funds available to it abroad. These largely fictitious distinctions are maintained at the cost of the noted disadvantages to business operations abroad and close to crippling disadvantages to the normal further development and continued functioning of the United States' international capital and money markets. They have also advanced the dubious arts of window dressing down to the level of company accounts.

Meanwhile the balance of payments technicians struggle to log in and out the billions, even tens of billions, in funds transferred back and forth between banks and their foreign branches. We have gotten to the stage where a weekend's banking convenience to a single group of banks can create the appearance of a deficit larger than any of the deficits registered in recent years in the struggles of the pound, the French franc and the lira, not to mention the dollar itself.

One way of bringing greater realism to the balance of payments would be to bring into its purview the whole structure of business assets which have so changed our orientation to the world. I think members of this Subcommittee will find in the table I have appended to my remarks here that the investment information compiled by the Department of Commerce yields a most interesting and basic underlying picture of United States assets and liabilities. It would not be difficult to evolve from this sort of data a relatively complete international balance sheet, and then to devise an income statement which would, as in all classical accounting, reconcile changes in the balance sheet from the beginning to the end of the period. I think it is most likely that this approach would give a far more coherent and accurate piture of the country's basic ability to discharge its existing liabilities to foreigners as banker, as trader and as producer. I think this effort should be made.

At the same time we should not delude ourselves that a strictly geographic accounting can successfully portray the intricacy of our involvements in the world economy. It has been noted already that Americans appear on both the domestic and foreign side of the balance of payments fence. It hasn't been noted here yet, but this Subcommittee is aware that on the monetary side an extraordinary market in non-resident dollars, commonly called the Eurodollar market, has grown up over the last 15 years. We have not yet exhausted the meanings of this new and unpredicted financial phenomenon. Looking back it seems that the Eurodollar and Eurobond markets provided a crucial link that internationalized banking in a way that reflects and gives financial expression to the growing internationalization of the world's basic producing structure.

I think we must be close to the point where we should stop worrying about whether companies A, B and C are keeping their funds in a New York bank or its branch in London, or Paris, or Frankfurt, or Tokyo; or what the exact national distribution of the companies' equity structure may be. We are close to the point where the meaningful questions, such as whether the companies are in reasonably liquid shape or not, can be faced in dollar terms without making the separate determination in a variety of national currencies.

In the case of our highly developed national market we are not concerned with state or regional balances of payments. The financial facts from which we try to derive an impression of the state of the financial health in the country belong to the national flow of funds data. I think we are very close to the point where we could and should turn to analogous international sources and uses of funds to read the true state of international financial affairs. If we are not close to that point, one of our immediate tasks should be to determine why not.

How Far Has World Output Been Internationalized?

There is nothing startling about the process of internationalization of production, which is here taken to mean simply the state of affairs that exists when an entrepreneur of one country organizes production of "his" product in another country, usually as an alternative to producing it in his country and exporting it. Students of the motives for such activity, including myself, have been surprised at the now familiar variety. In the post World War II world a common occasion for producing abroad was the barriers imposed by national authorities to imports thought to be wasteful of chronically scarce foreign exchange. The typical post-war problem was to reconstitute war-damaged-destroyed-distorted resources as the appropriate means of ultimately achieving acceptably high standards of consumption, in contrast to an alternative possibility of spending (that is squandering) precious foreign exchange merely to establish foreign sources of supply for consumers. The existence of barriers and the special situation pertaining after World War II somewhat obscured the fact that even in the absence of these special conditions economics would have provided crucial reasons in terms of higher product availabilities for internaional production. The same economic factors that have led to the establishment of bigger national markets in contrast to earlier regional and local markets would prevail for the still wider market possibilities that exist as national barriers are lowered or withdrawn.

We do not have precise figures on the extent to which actual international investment trends have led to the establishment of an internationalized producing and marketing system in the world. But our indicators are quite good enough to demonstrate emphatically that American entrepreneurs are involved in production activities abroad that result in well over $200 billion a year in sales. In the same spirit of internationalizing our perspectives, we can note here that something like a tenth of the production in geographic United States is to be associated with foreigners' investment activities here. Both of these estimates of international activity are based on U.S. figures. Not covered are the investing and producing activities of other countries in foreign areas other than the United States. For these the available information is very sketchy. Nonetheless an order of magnitude can be inferred on the basis of general considerations such as achieved levels of GNP, trade and aggregate scraps of information on investment. I think $150 billion would be a minimal guess for this category of other (foreign) international production. Taken altogether—that is, U.S. producing activities abroad, foreigners' here, and foregners' in other foreign countries—we get an order of magnitude of $450 billion. This figure does not take into account the product of communist countries producing operations abroad, a figure which though presumably very limited at present may well grow.

U.S. policy for its international activities has fallen far behind the world that these activities have done so much to create. By far the most important economic fact of this generation is the rapid rise of international production.

As a basic foundational fact, what we are wanting here is a figure for a gross world product (GWP). This lack is not fatal; we can make aggregate national product figures serve the purpose. But the lack illustrates the interesting point that when we need to be considering the consequences of operating an emergent world economy on the basis of national policy perspectives, we are driven to draw a picture of those activities from figures rooted in national rather than world perspective.

A world production figure can be approximated as follows:

	Billions of dollars
U.S. GNP	$1,000
Rest of industrial "West"	1,000
Russia, Eastern Europe, and China	650
Less developed countries	350
Total	3,000

Sources: These order-of-magnitude estimates have been elicited from information on national GNP or per capita production, as provided for different areas by U.S. Department of Commerce, The International Bank, the United Nations' *Yearbook of National Accounts*, O.E.C.D. National Accounts, and Joint Economic Committee's *Soviet Economic Performance*.

The figure of $450 billion, representing international production, when read against the aggregate GWP level of about $3,000 billion reveals that this internationalized component of aggregate world production amounts to a sixth of all activity. I think it may be accepted that at this level of relative importance, internationalized activities suggest not just a special area of overlap among national economies but rather the solid underpinning of an emergent world economy.

BROAD POLICY IMPLICATIONS

As I see it there are two broad policy implications for us in this picture of world production:

1. The primary international economic interest of the United States is in the correct international allocation of resources. What it does is to translate to the world economy the key features of competiveness and efficiency that guide our national development. Note: As a matter of economics, it should be noted that the production gains obtained from better allocation of resources take the place formerly held by the law of comparative advantage i.e. national specialization, as the rationale of the gains from international trade.

2. The internationalization of production has been concentrated in the industrialized market economies. How to achieve comparably productive relations with the other third of the world, which clearly has not yet been integrated in the world economy, is a major problem, economic and political, for our future policy.

In regard to the first of these—the United States' interest in international production—the nation's primary interest and probably the only tenable basis for policy is in achieving the most productive world usage of resources. This objective will doubtless raise many intricate issues, particularly in a world whose economic integration appears to be running distinctly ahead of its political integration. Only international perspectives are valid in a world in which the factors of production move competitively to their ever more effective uses: yet these perspectives must nonetheless be read and implemented from the limited vantage points of national governments.

The economic corollaries of the principle of the international optimizing of resource uses are exacting. Wherever resources are used in a less productive and therefore more costly way than they could be in an alternative use elsewhere, real product is sacrificed. Worse, the less efficient use cannot survive the effective range of international competition.

At the moment we are preoccupied with some of the special international problems which have arisen in selected industries. Our sense of our long run interest gets obscured in our concern either to shore up the faculty competitive position of a given industry or to offset the comparable shoring-up actions of others.

These hearings as I understand it are designed to restore the sweep of at least a decade to our policy deliberations. With the steadily growing consolidation of production in the world as a spatial context and the basic time-accounting in terms of a decade. I think it is not open to any country—not even to this one with its incomparably variegated and developed market—to validate any use of resources, that is of manpower, machines, technique and management, less efficient than elsewhere obtainable. As a practical matter it is doubtful that any area of national economic life can be effectively protected against the competitive power of greater efficiency. If this were not so, the prospect for our further growth and that of other countries would be unpromising. This is the inexorable benefit, hard though its terms from time to time may be, of competition. And we have not allowed ourselves to dissipate this benefit in our national development.

For the United States the achievement of adequate perspective and conviction for the next decade of international development should come readily out of our experience with the successful merging of regional interests in a pattern of overall national development. The nature of this development and its eventuation were happily foreseen in the constitutional provision of an Interstate Commerce Clause. At least as confirmed in the nation's growing experience, the economic advantages of free movement of goods and materials and capital were seen to outweigh any local gains from interrupting that freedom of movement.

Unfortunately on the international front we do not have that sort of constitutional assurance nor do we have the same sense of community. But we have it incipiently perhaps in the seemingly hard-won principles of international cooperation that have been in the course of building over the years since World War II. The General Agreement on Tariffs and Trade was initially a limited international treaty on trading principles preserved from the wreckage of the proposed International Trade Organization nations were unable to agree upon in 1945. The GATT carries great authority with us and with all its members, unquestionably beyond anything originally intended. Perhaps even more dramatic has been the high degree of monetary cooperation achieved in and beyond the International Monetary Fund—more dramatic because of the extreme sensitivity of sovereign states to sharing with others any degree of monetary jurisdiction.

What is called for now by our real long range economic interest is unqualified support of all international initiatives that extend rather than limit the freedom of movement of goods and capital. This policy we should approach with the assurance that when given resource commitments are challenged by lower cost operations elsewhere, this is merely the economic verdict that a better use exists here for the resources in question. It is our task to find that use.

I do not want to gloss over the truly difficult problems created by the product of apparently substandard competitors. Our national notions of allowable competition have been forged in a long struggle to incorporate concepts of decent living standards and working conditions into production. In the case of the less developed countries the desperate character of their needs can virtually be defined in terms of their failure to achieve comparable standards. The effect of international competition can and should be in the direction of making decent standards prevail. This sort of problem, very analogous to problems of fair competition within the nation, is probably among the most difficult to be resolved if a satisfactorily working world economy and its enormous productive benefits are to prevail. Difficult though the problems are, there seems to be no reason to assume that they are beyond the same means of solution that have proved effective nationally, solutions in which labor unions and social legislation have been the key elements. It should be mentioned that the free movement of goods and capital is structurally essential to the effectiveness of an economy, and as in the case of our country fair labor standards must be achieved without sacrificing the freedom essential to productivity.

In this same sense the context of a world economy suggests that the key issues for the future are likely to echo those that have proved crucial in large national economies. Here again our own history I think is a good guide and finds considerable corroboration in the experience of other developed countries. In addition to the key problem of fair labor standards, three other areas that are predictably important are: (1) the harnessing of excessive bigness and influence of companies (international antitrust); (2) the internationalizing of responsibility for monetary and credit policy (an international Federal Reserve); and (3) international tax policy. Progress in these areas is familiarly a contest between international experience and national habit and the issues will not be easily or quickly disposed of. But our international experience in each of them is growing rapidly and I think it is far easier to be hopeful of a satisfactory outcome now than it was 25 years ago when we first faced the urgency of international solutions to the problems which had previously been played close to the national chest, so to speak.

The other of the two broad policy areas mentioned above has to do with our relations with the less developed countries and the centrally planned ones. In this overview of policy it is not possible to do justice to the host of problems that make up the package we identify as relations with the less developed countries or the intricacies of political and security problems that override our economic relations with the communist countries. Neither of these big areas, which account for about a third of the world's output, can be excluded from the concept of an emergent world economy. Yet in neither case has the interplay of local institutions yielded a pattern of dynamic production so dramatically characteristic of the economic relations among the countries of the other two-thirds of the producing world.

In the case of the less developed countries it should also be kept in mind that in terms of output alone international activities loom very large in the total production picture—perhaps $150 billion, or well over a third of the total $350 billion aggregate GNPs. This is a product picture in which extractive industries play a large part on the international side. In short, the LDCs constitute an area in which international activity has played a long traditional and very specialized role.

The recalcitrance of the development problem in the face of a long history of intensive relations with the more developed West suggests that the emphasis in the period ahead should be on the possibilities of new departures with new cooperative institutions that bring together the entrepreneurial skills of the international community and the developmental responsibilities of the local communities. As for the United States, its position as the most developed country and as the chief international banker of the world gives it a crucial role in the process of maintaining a net flow of investment resources adequate to bring the LDCs into a more dynamic relationship with the developed world. All studies appear to indicate that their developmental potential is consistent with that more dynamic result.

Just a word more on perspectives. In the context of the entire output of the world today the United States, at $1,000 billion, represents about a third. This fraction is more than just a manner of showing the level of U.S. production; it expresses that production in relation to the entity it is part of. The clear implication of the international production trends we have looked at is that United States production is a part of world production. We have seen that a tenth of this U.S. production of $1,000 billion is directly to be associated with the investment of foreigners and similarly about a tenth of the $2,000 billion produced outside the U.S. is to be directly associated with American investment in producing activities. But beyond these designations of product as "internationalized", our growing knowledge of the methods of international companies gives a clear sense of the internationality of the whole process.

Beyond sheer size, the international sector of world production is a very dynamic one, growing steadily at an annual rate of close to 10%—a pace almost double the basic economic growth rates we are familiar with in the various national economies. The implication of these rates of growth is that world production continues to be internationalized at a fairly brisk pace. Projections of the rate suggest that within a generation a majority of production will have been internationalized. Moreover if the dynamism of the international sector can be maintained it will as it grows exert a more and more powerful influence on general growth rates, putting within reach fairly hopeful answers to both the capital and consumption requirements of the world's rapidly growing population.

This is all subject to a big IF—we all have reservations to make whenever the game of growth rates is being played. If only the right things are produced, if only reasonably equitable distribution is achieved—and above all if international politics do not force an economic fragmentation of the world. These and doubtless many other ifs are all relevant. But I would say the most important one, and one directly within the political capability of the United States, is *if* the United States follows an economic policy that is impeccably international.

I think the country has reached the point in its international orientation where such a policy is in its best national interest regardless of what other countries do. This is reminiscent of the classic moment in economic history when in 1846 England repealed the Corn Laws, thereby removing protection of its agriculture and improving the international cost position of its industry. Special circumstances, including especially famine conditions, gave urgency to their decision, but it is taken historically as the moment when England recognized its fundamental industrial structure had become irreversibly international.

The United States' economy, though larger, more varied and probably more selfsufficient than England's, is in a similarly irreversible position. One simple way to illustrate the point is to recall the growing extent to which foreign production includes the productive activities of Americans abroad; to discriminate against foreigners is to discriminate against ourselves. In a subtler but I think more meaningful sense the effective operation of the American economy depends on the world setting of which it is so large a part.

VALUE OF U.S. INVESTMENTS ABROAD AND FOREIGN INVESTMENT IN THE UNITED STATES, 1959–69

[In billions of dollars]

	1950	1960	1964	1965	1966	1967	1968	1969 estimate
U.S. assets (investments abroad), total	31.5	68.0	99.1	106.3	111.8	122.7	135.3	143.4
Direct investment (book value—mainly subsidiaries of U.S. companies)	11.8	31.9	44.4	49.5	54.7	59.5	64.8	69.8
Other long-term private (market value—mainly portfolio; including investments where U.S. equity is less than 10 percent)	5.7	12.6	20.5	21.6	21.0	22.2	24.2	24.1
Total long-term private (with yields typically above 10 percent)	17.5	44.4	64.9	71.0	75.7	81.7	88.9	93.9
Short-term private	1.5	5.0	10.9	10.2	10.6	11.9	13.0	13.6
Total private	19.0	49.4	75.8	81.2	86.3	93.6	101.9	107.5
Government short-term (including monetary)	1.7	4.4	4.5	4.8	4.5	5.4	7.4	7.6
Other government (f.e. Eximbank, IBRD)	10.8	14.1	18.8	20.3	21.0	23.6	25.9	28.2
Total government	12.5	18.5	23.3	25.1	25.5	29.0	33.3	35.8
U.S. liabilities (foreign in United States), total	17.7	41.2	56.9	58.7	60.4	69.7	81.1	91.2
Direct investment	3.4	6.9	8.4	8.8	9.0	9.9	10.8	12.1
Other long-term	4.6	11.5	16.6	17.6	18.0	22.1	29.5	29.8
Total long-term	8.0	18.4	25.0	26.4	27.0	32.0	40.3	41.9
Private short-term	6.5	12.0	17.5	18.2	20.8	23.0	27.0	37.5
Government short-term	3.1	10.8	14.4	14.2	12.6	14.8	13.9	11.8
Total short-term	9.7	22.8	31.9	32.4	33.4	37.8	40.9	49.3
U.S. creditor position (assets-liabilities)	13.8	26.8	42.2	47.6	51.4	53.0	54.2	52.2

Sources: U.S. Department of Commerce, Survey of Current Business, various issues; Federal Reserve Board of Governors, Federal Reserve Bulletin, April 1970; U.S. Council of the International Chamber of Commerce.

Chairman BOGGS. Thank you very much.

We will proceed now to a panel discussion and I would like first, to direct some questions to Mr. Colonna.

Mr. Colonna, there is great fear in our country that the European Common Market is looking more inward than outward and that fear is accentuated now by the prospective entry of the United Kingdom, Denmark, Norway, and Ireland into the Community.

For my own part I have looked upon the Community as one of the great developments of modern times, not only in hours of its economic implications, which are manifold, but also its political implications. The idea that the animosities which have divided Western Europe are being resolved in a fashion somewhat similar to what happened on this continent when we were a new nation is one that fires the imagination of mankind everywhere. But if, on the other hand, with the accession of the United Kingdom and the others, the Common Market merely becomes an inward-looking, protectionist trading bloc, then I am afraid that an international trade war, which would be devastating beyond comprehension, could actually come to pass.

I would be very, very interested as the other members of this panel would be in this.

I wonder if you would respond to my inquiry.

Mr. COLONNA. I shall be glad to do so, Mr. Chairman, very briefly.

Chairman BOGGS. You do not have to be too brief.

Mr. COLONNA. Mr. Chairman, I submit that the record to date of the external economic policy of the Community is such that this policy cannot be regarded as inward-looking and——

Chairman BOGGS. Would you say that in agricultural policy as well?

Mr. COLONNA. I was coming to that.

Chairman BOGGS. Go right ahead.

Mr. COLONNA. I would say that this is true from an overall point of view and I offer as evidence the Kennedy round as a result of which in 1972, the external tariff for the Community will be, I believe, the lowest of any other industrialized area in the world. I would also offer as evidence the open door policy to foreign investments in the Community, investments which, of course, have been beneficial to us, but they have also been very beneficial to the investors, albeit, of course, they can create certain problems also for the countries of origin of these investments, as we have just heard. That is an open argument.

Insofar as agriculture is concerned, Mr. Chairman, in absolute terms the volume of imports has very considerably increased between 19——

Chairman BOGGS. Ambassador, you are referring to the past. I want to look to the future.

Mr. COLONNA. Yes, but we have to know where we are in order to see where we can go.

Chairman BOGGS. I agree with that.

Mr. COLONNA. Up to now, in agriculture there has not been, in fact, any diminution of the percentage of American imports in the growth of consumption in the Community. Now, looking at the future——

Chairman BOGGS. Just let me amend your statement just to one extent. If you look at America in the continental sense, not as the geographic limits of the United States, there has been, in my judgment, vast discrimination against the tropical products of Latin America as a result of the preferential treatment accorded to the African nations.

Mr. COLONNA. Mr. Chairman, this is, I would say, politically speaking, a different problem. When the Community was created, it was faced with the problem of the former colonies of certain countries, members of the Community. The decision was made to extend to those countries a preferential treatment within the framework of an association agreement. We realized—the countries members of the Community realized that for certain tropical products, this preferential agreement would hurt other producers throughout the world, in particular our Latin American friends, and certain concessions were made unilaterally in order to offset to a certain extent, the impact of this preference. I accept, Mr. Chairman, that this was a difficult decision to make for the Community.

Chairman BOGGS. Well, now, let us look to the future. Let me first state the fear and you give me the answer, if you will, please.

Mr. COLONNA. Yes, sir.

Chairman BOGGS. The fear is that with the accession of the United Kingdom and the other nations to the Treaty of Rome that the common agricultural policy will be even more discriminatory and to be even more specific, the producers of such agricultural commodities as soybeans and feed grains in the United States are very much concerned about what may transpire. Some say that we should take retaliation in the form of restrictions on industrial products. They say, if this is really going to happen in the Common Market, then we had better take a look at how many Volkswagens, Fiats, et cetera, come into the United States.

Mind you, I consider this to be a very dangerous situation. Would you mind commenting on it?

Mr. COLONNA. Yes, Mr. Chairman. I would say that an evolution such as the one that you indicated at the end would be a catastrophy from the point of view both of the United States and Europe and I permit myself to consider that in this our interests are common. I can here, of course, only express personal opinions. I am neither the British Government nor the Government of the member countries of the Community.

Chairman BOGGS. Well, your personal opinion carries great weight because in my judgment, you have made as great a contribution to the Community as Jean Monnet himself made.

Mr. COLONNA. Oh, Mr. Chairman, thank you very much. On this point I shall permit myself not to agree with you but I accept your statement. [Laughter.]

However, I would be very surprised, Mr. Chairman, if as a result of the disadvantages that the present agricultural policy has on the economy of Great Britain and on British finances—I am speaking from the overall economic point of view, and from the point of view of the Treasury, not of the agricultural producers, I must underline this point. I should be really surprised if as a result of this fact and as a result of the fact that we ourselves in the Community are bearing the brunt of the cost both for the taxpayer and the consumer of our present level of prices, there would not be over the years to come a fairly profound modification of the current policy.

In expressing this view, I can base myself on the initiative taken by my eminent former colleague, vice president of the Commission, Mr. Monsholt, a Dutchman, who is the author of a plan for a reformation of the agricultural policy calling precisely for these objectives.

Were we to achieve these objectives, a great deal of the difficulties that have arisen in the relationship between the United States and us would be on their way to a solution. But, Mr. Chairman, the percentage of active population in the United States which is active in agriculture is around 4 or 5 percent. I address myself to my economist neighbors. Our percentage, Mr. Chairman, is still in the neighborhood of 15 percent and in certain countries it reaches—in certain areas of certain countries it goes up to 30 percent.

Now, a new type of agriculture, one that would eliminate all kinds of uncompetitive production that secures at the present level of prices an insufficient but livable income entails what? A very powerful industrial development. You have to create jobs in order for millions of people coming from the farms to find a new and better way of living, and this is precisely what we are trying to do, but we cannot do that nationwide, because our nations are too small. Even Germany, I submit, which is obviously the most strong member country, is too small for such a purpose. Italy certainly could not do it and I am an Italian and I can speak for my own country. So, we must look at a joint effort and we come back to the achievement of the community which has been too slow, unfortunately, for reasons which I consider to be objective, but which now seem to go more rapidly than here now.

Chairman Boggs. Well, would you agree with this sort of summation? There are a number of distinguished members of this committee here and I do not want to monopolize the time. The greatest Common Market on earth are the 50 States of the American Union and the wisdom of our Founding Fathers manifested itself when they prohibited the erection of any barrier between the respective States. The truth of the fact, the greatest inadequacy of the Articles of Confederation which preceded our Constitution arose because of the lack of political institutions to prevent the competition which arose in the 13 Original States.

Now, in our country we have many industries that, because of internal competition, either technological or geographical, ceased to exist. The migration of the textile industry from New England to the South is a good example that comes to mind. There are so many others. And in internal competition in the private enterprise system we say, well, it is too bad, but the automobile took the place of the horse and buggy, and so on.

Mr. Colonna. Precisely.

Chairman Boggs. Now, rather than erect all kinds of barriers between us and the Common Market and you and us and Japan—I am talking now about industrialized parts of the earth—is not there enough ingenuity in these three great developed areas to recognize the problem that Mr. McKee has pointed out here, namely, that we do not produce anything like enough food to feed mankind today in all of these countries and we do not produce enough textiles to clothe them. Why is it not possible for the great emerging United States of Europe and the United States of America and now this magnificent industrial empire in Japan, and it is magnificent, it is a new industrial complex—they can put steel down in my town cheaper than they can from Birmingham because they have got a more modern industry—why cannot we organize ourselves to do that? Why cannot we evolve a sort of common policy and in the process make some real contribution to mankind, and maybe avert some of the tensions that are creating war and famine all over the earth? Would you respond?

Mr. COLONNA. Mr. Chairman, insofar as agriculture is concerned, the problem of food, we in the Community during the Kennedy round negotiations, indicated our preparedness to discuss with our major partners in the producing world to enter into discussions in order to arrive in the first place at an agreed policy of support of prices which is always the trouble in establishing (*a*) a good trade relationship between producing countries, and (*b*) a reasonable balance between supply and demand on the world market.

Of course, I am perfectly aware, Mr. Chairman, and I totally subscribe to your cry of alarm in relation to the hunger in the world but we have to think, of course, also to what happens in relation to solving demand and it is in relation to solving demand that producers must have to find between themselves reasonable equilibrium so as to have the strength to answer the unsolved demands.

Chairman BOGGS. I understand. Just one or two final questions to which you can respond quite readily. Do you envisage a common currency for the EEC down the road?

Mr. COLONNA. I envisage a common currency or a common monetary policy which is precisely the same thing——

Chairman BOGGS. Right.

Mr. COLONNA (continuing). At the end of this decade, or else there will not be any more Common Market.

Chairman BOGGS. Now, one final question. Is it possible to maintain the Economic Community without ultimately coming some day to the political instrumentalities that must enforce the economic arrangements?

Mr. COLONNA. The answer is, no.

Chairman BOGGS. Thank you very much.

Just one question now for Mr. McKee. We create in a bill presently before the Ways and Means Committee a Domestic International Sales Corporation called DISC. What is your feeling about that?

Mr. MCKEE. We think that DISC is one of the possible answers to encouraging more exports from the United States and assisting on the balance of payments.

Chairman BOGGS. So you approve of it?

Mr. MCKEE. Yes.

Chairman BOGGS. Now, one other question. I was greatly interested in your remarks about Pakistan. Just a cursory examination would show that the United States carries on its greatest trade with the developed nations, Canada, the Common Market, Japan. Our least trade is with the less-developed countries, our trade varies almost directly with the degree of prosperity of our trading partners.

Is it not a fact that you and your multinational corporations, that your corporation plus similar corporations, are making direct contributions to the increase in per capita income of these developing nations?

Mr. MCKEE. Well, this is certainly our contention. We believe from our general policies that we do contribute and increase their local income, which will in turn increase their total economic——

Chairman BOGGS. One final question and then I yield to Mr. Reuss, who is an expert on this subject.

Today, the biggest plus in balance of payments is return on American investment abroad; is that not correct?

Mr. McKEE. Yes.

Chairman BOGGS. Mr. Reuss, I yield to you.

Representative REUSS. Thank you. Oh, Mr. Widnall?

Representative WIDNALL. Thank you, Mr. Reuss. I certainly would like to join in welcoming all of you members of the panels here this morning. I missed some of the testimony because I was not able to get here right on time, but I have read it and I think you have made an outstanding contribution to the work of this committee.

Mr. McKee, I would like to ask you this question. In your prepared statement you note that the actual and potential volume of U.S. foreign investment has been hurt by U.S. controls on investment abroad. Can you give some specific examples of the impact the controls have had upon the international operations of CPC?

Mr. McKEE. Could I give the example without mentioning specific countries if that would be agreeable?

Representative WIDNALL. I am sure that would be satisfactory.

Mr. McKEE. When these controls were first put into effect, guidelines were given to U.S. corporations for financing and the repatriation of profits generated abroad, as well as new investments in these countries. We felt at that time that the practices we had been following as a corporation were very close to the ones that were set up by the Department of Commerce.

What happened subsequently is that where we had been prepared to increase our investment in certain countries, we then had to go out and borrow either in the Eurodollar market, as an example, or in a particular local currency, which was not the appropriate one at that time from an availability viewpoint. This slowed down the making of the investment and increased our interest costs which in turn reduced the total profitability of our investments.

Now, there are two or three examples that we have of just this sort of a situation but as I say, we have still been able to find the funds abroad. It has just reduced the profitability of our investment.

I am not sure if that is sufficient to answer your question, but it has happened.

Representative WIDNALL. Then, how do you feel it can be expedited?

Mr. McKEE. Again, it has been our feeling that one of the methods for improving the balance of payments is, of course, through exports. We have heard a lot about the decline of U.S. exports. Even though we recognize that agricultural products have been one of the primary exports from the United States, we find that the best effort has not been made to export industrial commodity type products many of which are sold strictly on price.

Where they have had the best result is where the export is selling on the basis of its technology and the purchaser abroad is willing to pay for that technology in this product. This is really where we have seen the slowdown in the last few years from the United States and its effect on the export balance.

Representative WIDNALL. Then, I take it, you feel these controls have had a major impact on the balance of payments.

Mr. McKEE. Yes, sir. Negatively so.

Representative WIDNALL. What do you think would be the effect of the immediate loosening of controls?

Mr. McKEE. I have difficulty in answering that question in the general sense. I know for our own company that there would be very little impact right now, because we have made other arrangements which we would be very reluctant to break down right now. We might slow down some of the remittances in order to get some of our debt equity balance sheets in proportion again in certain countries. In some of the countries, they are putting more pressure on us, asking that our borrowings in those countries be in line with our capital. In some of these specific areas we think we might make some adjustment but the effect on our total contribution to the balance of payments would be very small.

Representative WIDNALL. Mr. Colonna, according to a recent article in the Economist magazine, there is a worldwide liquidity crisis which could be sparked by further Penn Central-type instances in the United States. In your conversations with European business and financial leaders, do you find this to be a matter of concern with them?

Mr. COLONNA. Yes; Mr. Widnall. Our business enterprises in general are facing a great deal of pinch in securing the means necessary for securing their development. There is a shortage of finance available. This is due to a number of factors. The increasing demand for social services which induces our governments to dispose of a large portion of the resources available: And here we come to the subject matter of this meeting, the competition in which our firms find themselves in regard to the subsidiaries of the multinational corporations, American based, which for the reasons that were just discussed right now are forced to borrow either in the local markets when there is means available, or in the Eurodollar, which is composed as we all know, to a certain extent of the savings of the European countries themselves.

In other words, hoping that I have answered the question that you wanted to put to me, we are having right now a situation in which the liquidity of the enterprises is the more difficult because also our costs are rising. We are having a very rapid increase in costs in Europe, specifically labor costs. Labor costs have increased and are increasing over the last 2 years to an extent that does not still bring them in line with average American salaries, even taking into account the purchasing power of the dollar in the United States and in Europe, which is different, but they are growing very much and the enterprises in Europe could face this very rapid increase in the cost of labor only by enormous efforts for increasing their productivity, but this entails easy access to financial means and that is where the pinch is felt.

Representative WIDNALL. You have the same problem, then, that we have here, the relationship of productivity to increase.

Chairman BOGGS. I think Mr. Polk wants to comment.

Mr. POLK. Mr. Widnall, the U.S. Council, for which I work, just completed a survey of companies and the impact of the controls on their operations. I referred to this survey in my prepared statement. We are having a press conference tomorrow and it is scheduled for release tomorrow but with the chairman's permission, I would like to give it to you subject——

Chairman BOGGS. You can release it right now, as far as I am concerned.

Mr. POLK. I would like to release it to you, sir, but not to the public.

Chairman BOGGS. OK, fine. Release it to Mr. Widnall, too, and the other members of this committee.

Mr. POLK. Yes, sir; I might say——

Chairman BOGGS. That is the first time we ever got anything ahead of time. [Laughter.]

Mr. POLK. In a couple of words, naturally you do not except the companies to like controls. But their concern is based both on a feeling that the controls are both edged toward nonbusinesslike, noneconomic means of financing and on concern for the future state of their liquidity. The correspondence was, I felt, rather eloquent on these points and there is an annex in the report that quotes at length from the correspondence.

Representative WIDNALL. Thank you, Mr. Polk. One more question. Mr. Colonna, in the July issue of the Morgan Guaranty survey, Robert Triffin describes the Common Market's plan to achieve monetary integration as including a common currency within 10 years. He notes this push for integration is now being accelerated by the feeling that it may offer the only practicable way to regain monetary sovereignty already lost to the United States. I am quoting from his article.

What do you feel would be the impact on the dollar if such a plan comes off on schedule?

Mr. COLONNA. Mr. Widnall, I would say that these plans should be looked at not as an act of aggression on the dollar, if I may speak quite bluntly. That is not at all the way in which most Europeans at least, look at this issue. These plans must be looked at in terms of the requirements of the Common Market, the Community, to come to its ultimate achievement and also in terms of creating a better relationship that the one existing at present between the United States and Europe. It is quite clear, and the events in 1968 and 1969, can be indicated as evidence of this, that if the monetary relations between the six countries continue to be dominated by individual policies which are incoherent between themselves, there is no great hope for the Common Market to remain in being and to progress. While very big corporations like those that we have been discussing this morning can develop appropriate strategies in order to take into account the disparity of these monetary policies and also the risks entailed in certain changes of parities between them, the mass of the business enterprises in our countries, which is still of a medium or small size in comparison with yours—we are very far from the oligopolistic situation which you have achieved already since a long time—could certainly not face these risks and the result would be a withdrawing, a further withdrawing within the national boundaries both economically and politically.

Therefore, one should look at the establishment of a monetary union in Europe in the first place as a normal consequence of the endeavor which we have entered into 20 years ago of integrating for political and economic reasons the nations of Europe, Europe having been for so long the source of major conflicts throughout the world.

What then would be the ultimate result if these efforts would be crowned with success? Well, I do not think these efforts would mean to do anything else than the creation for Europe of a negotiating position with the United States in relation to the evolution of the international monetary system. This would be evidently a change in the relations to the situation existing 20 years ago for the very simple reason that at that time no European country, let alone no group of European countries, would have had any voice in that matter, but I do not think that this should be interpreted, once again, as a program entailing aggressive intentions in regard to the dollar.

Chairman BOGGS. Mr. Reuss will inquire.

Representative REUSS. Thank you, Mr. Chairman, your panel has been in general quite optimistic concerning the multinational corporation and American foreign investment. This subcommittee has had testimony from representatives of the American labor movement recently to the effect that——

Chairman BOGGS. I might add we are going to have some more tomorrow.

Representative REUSS. And there will be some more. Their position is very briefly this. In former times, it is said, American labor could withstand a good deal of competition from foreign labor which was paid very much less and whose working conditions were markedly inferior to those in this country, because American technology was so much better that, therefore, we overcame the labor cost differential and our productivity came out on top.

Recently it is said, with the development of the international corporation, American technology has been exported in a whole variety of areas—Korea, Hong Kong, Taiwan, and Mexico. Perhaps some European countries are mentioned from time to time. There the technological gap between the United States and those countries has been markedly narrowed and hence the wage differential turns out to be much more of a governing factor than it was.

Such at least runs the argument and I would like to ask anyone who wants to comment on that proposition. First, perhaps Mr. Kindleberger?

Mr. KINDLEBERGER. That is the kind of question we international trade economists spend our time answering all the time. I am glad to do so, Mr. Reuss. In fact, this generally comes at a very early stage of the economics courses we teach.

The fact of the matter is, the Japanese and the Mexicans cannot supply it all to us and if they could supply our total standard of living that would be a very happy thing. We could play golf, and go sailing.

No; I think the labor theory that cheap labor abroad is taking jobs away from Americans is wrong. In the first place, we export more than we import right now in terms of value, so on that showing it is not true at all that we do not create jobs through foreign trade.

Chairman BOGGS. May I interrupt you there?

Mr. KINDLEBERGER. Yes, sir.

Chairman BOGGS. Is it not also a fact that more and more of our people engage in service enterprises for which there is no competition from abroad?

Mr. KINDLEBERGER. Exactly, except when our tourists go abroad and stay at the Meurice, and so on.

Chairman BOGGS. Where do they stay?

Mr. KINDLEBERGER. Some of them stay at the Meurice.

Chairman BOGGS. That is where you stay?

Mr. KINDLEBERGER. I had in mind the congressional trips myself. [Laughter.]

Representative REUSS. Can we change the subject? [Laughter.]

Mr. KINDLEBERGER. It is entirely right that some people in some industries are affected by imports and it may be true that cotton textiles will go the way of Christmas tree ornaments and that automobiles are the cotton textiles of tomorrow. But we move on and we have got to move on and if we just spend all our income for imported products, then the foreigners quickly find themselves in inflation.

The Japanese are very much worried about inflation today because they are exporting so much to this country. It is quite clear the Japanese cannot feed, clothe, furnish with electronics themselves and ourselves without finding it expensive. They do not want to earn just money. They too, want to buy things.

I think what some of my labor friends are worried about is we may have to adjust our economy but that certainly, sir, is what happens all the time. Nobody likes to adjust. In my field no literary economists like to have these mathematicians take over.

Chairman BOGGS. Do they?

Mr. KINDLEBERGER. They are moving up fast and just in the same way the established unions do not like. The fact is that there are some lines of work in which we had better import and move on to something where we have a greater efficiency, a comparative advantage.

Representative REUSS. You have not, however, quite, I think, addressed yourself fully to the point made by the unions which is that there has been this great upsurge in the export by the United States of technological advance and that to the extent that this has happened, the old factor which used to make American labor competitive with a handful of rice labor, figuratively speaking, tended to wash out. What about that? Is that an untrue account of what has been going on or——

Mr. KINDLEBERGER. It may change the pace to some extent and I believe it has. But it does not seem to me to change the basic principle, which is that we have an advantage in certain things and they have an advantage in others. We claim, for example, we have an advantage in the production of soybeans. Very well paid farm labor produces soybeans and we have a big advantage in land. In steel it is remarkable how well the Japanese are doing, but the Europeans all the time complain that we have such cheap and abundant coal. It is to be understood that Americans worry about labor just as the foreign producers think about our cheap interest rates. From an overall point of view, the labor theory that we are going to be ruined by cheap imports just cannot be accepted.

Representative REUSS. Let me ask Mr. Polk to comment on two interesting items in the table which he appended to his prepared statement entitled, "Value of U.S. Investments Abroad and Foreign Investment in the United States." Your last column there refers to the U.S. creditor position, assets minus liabilities, and that U.S. creditor position went up remarkably from 1950 when it was $13 billion. By 1960 it was $26 billion. By 1964 it was $42 billion. By 1966 it was $51.4 billion. But, then occurred a leveling off and today, your most recent figures show that it is only $52.2 billion or about what it was in 1966.

How do you account for that sharp leveling off after 1966? And what are the implications of that leveling off for our balance of payments in the future?

Mr. POLK. I believe, Mr. Reuss, that it is reflecting an improper policy on our part. You will notice that in the U.S. assets, the top line, there is a basic deceleration of growth. I did not actually calculate it out except in hand notes on my own copy. This is true also in the direct investments which we subjected to control. We have treated this not as a national asset that should not grow but rather as a balance-of-payments cost that ought to be minimized.

I think it is a fundamental economic error and one we should correct.

The net effect shows up in our net creditor position, and is, I think, more interesting than any of the balances that are calculated in our balance of payments. To the extent that we have to continue with balance-of-payments accounting on a national basis, I would prefer taking these net creditor figures as being the thing that is to be explained by the year's operations—the exports, imports, investments, banking changes. I would try as in a bank or business accounting to try and reconcile this basic change in our asset position.

Now, 1969 shows what seems to me to be a change for the worse. We have slightly weakened our asset structure in relation to liabilities. Commenting very briefly, I think actually when you open these books you get into reasons to feel as I do that in spite of poor policy—I have not been happy about it—the dollar has gained great strength because of this movement toward internationalization and the strength of international production that underlies it. The dollar is now relatively strong but I think we are getting warning signals here from figures like these, that we need to adapt our policy away from present calculations of the deficit and on to a basis of maximizing the benefits from international production.

Representative REUSS. Thank you very much, Mr. Chairman.

Chairman BOGGS. Thank you very much, Mr. Reuss.

Mr. Conable?

Representative CONABLE. Thank you, Mr. Chairman.

Mr. Colonna, when we had a quiet talk earlier this year I expressed some fears about the rise in protectionism in the United States and those fears seem to be somewhat realized in the bill that is emerging from another committee on which I serve. I realize you are not here to threaten and I do not want to put you on the spot about this, but, of course, one of the major restraints on those who are concerned about imports is fear of what may happen to exports if we go to the route of trying to shut our door here. Inevitably in the light of our great trade with Europe, we are concerned about what may happen there.

Your own country of Italy—I realize you are a citizen of the world, sir, in a very real sense and I subscribe to the comments that the chairman made about your influence in the European Economic Community —but your own country of Italy is one of the inevitable targets of import quotas of footwear. Italy would have to retaliate if it were to do so through the European Economic Community as a unit.

The chairman has expressed some concern about your agricultural policies and we are well aware of the tremendous agricultural surpluses you have in the European Economic Community. We sell you there over half a billion dollars worth of soybeans, for instance, at this point, used largely for margerine and quite obviously, that would be a tempting target for retaliation.

Now, I would like to ask you several questions. First of all, is not the form of retaliation likely to emerge from Europe, if we go this disastrous route of getting into a trade war, likely to be a restraint on investment because of the frustrations you will have in trying to impose trade restraints other than agricultural in the light of our many multinational corporations there in Europe?

I found some optimism in Brussels about developing agricultural policy even though you do have 15 percent of your people engaged in agriculture in the European Economic Community made up of countries with very closely divided governments which are, of course, politically sensitive to the bloc vote of the farmer. Do you see any possible ray of light in agriculture there resulting in some reduction of your surpluses and your subsidized exports? And do you have any general comments to make on this issue of retaliation, assuming that, as I think we must assume at this point, we are embarked on a course looking toward a less free trade here in this country.

Mr. COLONNA. Mr. Conable, I have to be very careful how I answer because——

Representative CONABLE. Yes, I realize that, sir.

Mr. COLONNA. Not at all because I would feel personally embarrassed but because I must say that there is nothing I would consider more catastrophic than seeing our two respective countries and areas embark into a course of mutual retaliation. I do not have to say who and where in the world would benefit from this coming up of this situation between us. This being said, we have to be, of course, realistic and recognize that there are several areas in which interests in the United States and Europe could come in collision between themselves for a number of reasons that can be understood and justified from an impartial point of view, but which are not very easily accepted by the groups concerned on one side and the other. This is really the difficulty.

There is no use going to explain to a farmer in Europe what is the result on the overall relationship with the United States of a certain policy when, after all, from a certain level of price of milk or of grain or whatever it is, depends after all for the present time, his life and the life of his family. This is really the source of the trouble.

My view, my personal view, but it is a view which is increasingly shared by others, is as follows: We shall not get out of our present difficulties, you, American friends, and ourselves, if we shall continue to consider the various facets of our trade relations in isolation. All these issues hang together. Visible trade, investment, and invisible trade, all the various sectors concerned, should be looked at within some kind of global framework. I heard Professor Kindleberger referring, for instance, to the possibility of some kind of GATT for investments. I believe that investments, direct investments, have now become so important as an alternative to visible trade that they cannot be excluded from a discussion between great areas of the world such as the United States and Europe. On the contrary, they must be included so that a certain balance can be reached, overall balance can be reached, which can be presented to our respective people and accepted.

You see, when you—when one hears reference to, for instance, the shaping as a result of the activities of the multinational corporations of a world economy, one tends intellectually to agree with this concept, but evidently the question comes up what shall be, in this world economy, the position of a group of countries such as the one I have been the servant of, both individually and as a group?

Well, to sum up, I would say, (a), we are not yet in this trade war and we do not have, therefore, to be so despondent about possibilities of avoiding it. I feel that one way to avoid it would be to face these difficulties jointly, globally, within an appropriate framework. I submit that the United States and the Community are for the present time the two most important areas from the point of view of international trade. I do not want to exclude anybody else, but I say that a discussion between these two parties would be certainly beneficial if it could be pursued, as I say, on a global basis.

(b) Insofar as agriculture is concerned, I can repeat what I have already said. We are getting more and more convinced that we cannot carry on on the present level and that we shall therefore, embark upon a reform of our agriculture, the result of which will be beneficial to our interests.

Incidentally, the so dreaded soybeans tax has not been introduced by the Community so far. Well, shall be say it has not. Well, that indicates that we are responsive to global interests in the United States. But we would like the United States to be responsive to our global interests, both economic and political, and for the Community, the continuation of its integration process has also political consequences.

Representative Conable. Does not the existence of the Common Market at this point reduce the probability of a trade war in that its member nations who may be especially affected by possible limitations and access to the American market will have to subordinate their interests to the overall interest which continues to be one of facilitation of world trade rather than a closing of world trade?

Mr. Colonna. If I may say so, it is a very good point, Mr. Conable. Certainly, the fact that we belong to a Common Market shall reduce the danger of sudden and irrational and emotional reactions that would create serious risks for escalation. But, at the same time, the fact that the interests of the six countries are not necessarily the same in regard to any restrictive measure introduced by the United States—you mentioned shoes and Italy, for instance—means that if you would be pressing very hard in the direction, divisive forces might be created in the Common Market because of lack of consideration of the lesser partners by the one who would be hit the most. That is also a political angle not to be lost sight of.

Representative Conable. My time is up.

Chairman Boggs. Thank you very much, Mr. Conable, Mr. Widnall, Mr. Reuss, and members of the staff. I consider this one of the best panels we have had in our series of discussions and on behalf of the subcommittee, I express our gratitude. Thank you, gentlemen.

The subcommittee will adjourn until 10 o'clock tomorrow morning.

(Whereupon, at 12:10 p.m., the subcommittee was recessed, to reconvene, at 10 a.m., Tuesday, July 28, 1970.)

A FOREIGN ECONOMIC POLICY FOR THE 1970'S

TUESDAY, JULY 28, 1970

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON FOREIGN ECONOMIC POLICY
OF THE JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The Subcommittee on Foreign Economic Policy met, pursuant to recess, at 10:04 a.m., in room S-407, the Capitol Building, Hon. Hale Boggs (chairman of the subcommittee) presiding.

Present: Representatives Boggs and Widnall.

Also present: John R. Stark, executive director; John R. Karlik, economist; Myer Rashish, consultant; and George D. Krumbhaar, economist for the minority.

Chairman BOGGS. The subcommittee will come to order.

I welcome all you gentlemen and the others who are here with us this morning.

Today we enter the second day of our hearings on the multinational corporation and international investment. Yesterday's witnesses provided an excellent summary of the problems raised by the exceptionally rapid growth of direct investment over the past decade. Today we are concentrating upon the implications of this investment for employment, productivity, the transfer of technology, and the growth of real incomes both in the nations that are the source of such investment and countries that are the recipients of direct investment from abroad.

Again, I am very pleased to say, we have an exceptionally qualified panel of witnesses. First is Prof. John H. Dunning of the University of Reading in Berkshire, England. Professor Dunning has studied extensively the economic effects of foreign direct investment in Britain.

Next is Paul Jennings, president of the International Union of Electrical, Radio & Machine Workers, and also chairman of the Committee on World Trade of the Industrial Union Department, AFL-CIO, an old friend of mine. Very happy to have you.

Then, we have another labor spokesman with a somewhat different point of view—Heribert Maier, director of the Economic, Social and Political Department of the International Confederation of Free Trade Unions.

Last, but certainly not least, Mr. Jacques Maisonrouge, president of one of the largest and most dynamic of multinational companies, IBM World Trade Corp.

Gentlemen, we are very happy to have all of you here. I might say in the beginning that the Committee on Ways and Means, which is the legislative committee handling trade problems, is having its markup session this morning, so that I will only be able to stay with you for a few minutes. However, either another member of the subcommittee or Mr. John R. Stark, executive director of the committee, will preside and the panel will move right ahead, probably much more expeditiously with me not here.

Our first witness is Mr. Dunning.

I wonder if all of you would summarize your prepared statements and that would give the staff members as well as the subcommittee members an opportunity to examine in detail, and we also proceed in this fashion, that you can ask one another questions and this all becomes a matter of record.

Also your prepared statements will be made part of the record and the record will be kept open after the panel discussion this morning to give each one of you an opportunity to add to the discussion that has occurred here today. We find these records to be most invaluable.

If you will proceed, Mr. Dunning.

STATEMENT OF JOHN H. DUNNING, PROFESSOR OF ECONOMICS, UNIVERSITY OF READING, BERKSHIRE, ENGLAND

Mr. Dunning. Thank you, Mr. Chairman. I wonder whether I might highlight what I would think to be the main points of my prepared statement.

Chairman Boggs. By all means.

Mr. Dunning. I think we are entering into a new phase about our thinking on the role of the multinational enterprise in the world economy. We have gone beyond the stage of asking black and white questions like: Is the multinational enterprise a good or bad thing? Is it a force for free trade and economic liberalism or an agent for world imperialism?

To start with, we now recognize that it is not very helpful to talk about the multinational enterprise as if this was a homogeneous phenomenon. The most we can hope to do is to identify particular forms of multinational enterprises, according, for example, to the economic activity in which they are engaged, the size and scope of their foreign operations and the way in which they are financed and organized.

Much, of course, rests on exactly how one likes to define the multinational enterprise. There are some economists who take a very broad view and figure any enterprise which operates producing units in two or more countries, or three if one wants to be strictly correct, as being multinational. Others like Prof. Jack Behrman feel that the name should be confined to the type of company which organizes its worldwide operations in a closely integrated way and is strongly centralized in its decisionmaking.

I have a certain amount of sympathy with this latter approach as it pinpoints one of the main areas which distinguishes today's type of international firm from its predecessors, although I believe that there are other ways in which one might delineate the boundaries of the multinational enterprise which makes just as much economic sense.

I think, Mr. Chairman, it depends to quite a large extent from which or from whose viewpoint one is examining the question. On the global level, for example, there are three main interests which are likely to be affected and affected differently by the operations of the multinational enterprise; they are, the economy of the investing country, the economy of host countries, and the world economy in general. At a microlevel, the main participants are the investing firm, its competitors, and its suppliers and customers, both in the investing and host countries. But it does not stop there. There are in addition, distributional effects to be considered. For example, multinational enterprises may, and do, influence the prosperity of different parts of countries in which they operate more than others; their impact on labor and employment may be different from that on capital and profits. Small wonder then that particular economic sections differ in their views about the merits of multinational enterprises.

The point, I think, which I would stress at this point is that a lot of the discussion about the economic effects of multinational enterprises is very inconclusive, if not arid, simply because the discussion fails to properly specify the particular criteria on which these consequences are to be judged. This, I believe, is particularly the case when we come to look at the current controversy between the objectives of multinational enterprises and the nation states of which they are a part. Broadly speaking, multinational enterprises are motivated only by private economic objectives. Nation states are much more complex in their goals.

The primary economic aims of most industrial nations are fairly straightforward viz the maximization of GNP and the rate of growth of GNP. The achievement of these two primary aims, however, not only implies the satisfaction of a host of subsidiary economic aims, but is circumscribed by the need to meet particular social, cultural or strategic goals.

In some cases, the nature of the economic system and the interpretation of what is the social good may be such as to outlaw the participation of foreign-owned enterprises altogether. Obvious examples here are the Communist bloc countries. For similar reasons, other countries may allow foreign concerns only a limited equity in local firms. At the other extreme, there are economies which are politically very liberal and impose the fewest possible restriction on either inward or outward investment.

In between, as we all know, there are a vast spectrum of attitudes and policies toward multinational enterprises. Not only do these differ between countries but also within particular countries, and within particular sectors of particular countries, depending, for example, on the extent to which foreign companies, in general, or those of one nationality in particular are able to influence the achievement of that country's—or that sector's—economic objectives.

Now, I think this explains, in part at least, why up to the late 1950's there was very little concern in Britain about U.S. direct investment. After the last war, Britain, like the rest of Western Europe, needed all the capital and know-how she could get. Even in 1957, American firms in Britain were responsible for less than 6 percent of the total British manufacturing output and only about 7 percent of the total profits. Since then, however, the rate of new American investment in Britain has risen three times that of her GNP and I believe would have risen a great deal more had Britain gone into the Common Market in 1958.

Last year, for example, I estimate that U.S. subsidiaries in Britain accounted for about 14 percent of the output and nearly a fifth of the fixed capital formation in manufacturing industry and sold about a quarter of Britain's manufacturing exports.

I have estimated elsewhere that on current trends something like a fifth to a quarter of Britain's manufacturing output will be in the hands of American-controlled enterprises by the end of this decade.

Moreover, this investment is very concentrated. The largest 50 American finance firms in Britain account for more than four-fifths of the total capital stake and about three quarters of this is directed to four industries, oil refining, motor cars, chemicals, and electrical engineering, which also happen to be the most research-intensive industries.

In my prepared paper, I have an appendix which I compiled a couple of years ago estimating the contribution of American-financed firms to the production of certain products in the United Kingdom.

It is, I think, the prospects of this growing participation of foreign and in particular American capital which is causing, in some sectors of the British economy, at least, some cause for concern, though this concern—perhaps unease would be a better word—is rarely spelled out and in some cases amounts to a little more than xenophobia. Very often it is triggered by an isolated happening in an American-controlled firm like the labor troubles of Roberts Arundel in 1967, or the takeover of a technologically advanced United Kingdom firm by a U.S. company which subsequently removes part or all of its R. & D. activities to the United States, or the transfer of part of Remington Rand's production from its Scottish factory to the continent in 1969.

In spite of these cases being very few and far between in Britain, I think it is the possibility that they may be more prevalent in the future, as American capital penetrates even more deeply into United Kingdom industry, which has led to some rethinking on the role of foreign-owned multinational enterprises in Britain, typified best, I think, Mr. Chairman, by a chapter which was devoted to this topic in the latest Trades Union Congress Economic Review and a statement issued earlier in the year by the Ministry of Technology.

Other reasons for concern toward foreign direct investment and the impact of the multinational enterprise on host countries have been well discussed in the writings of Harry Johnson and Charles Kindleberger and I do not propose to reiterate these this morning, except to emphasize that attitudes toward multinational enterprises by host nations, though often formulated in economic terms, are usually in my opinion political at root, and will differ inter alia according to the extent to which the activities of these companies are likely to affect the promotion of domestic economic and social goals.

For the rest of my submission, I propose, if I may, to confine my remarks to economic issues, and I would like further to hypothesize that the host country has two basic aims, the maximation of real output and the rate of growth of real output per head over a period of time. The question is, to what extent are the operations of the subsidiaries of foreign multinational enterprises likely to provide a first best solution in advancing these aims?

Can one formulate this question in terms in which it can be tested? I think one can—even though in practice the testing is an extremely difficult thing to do—provided that, and this is an important proviso, one makes some assumption about what would have happened had the multinational enterprises not been operating in the host country, or if the output which they had supplied by then was rather less or rather more than it actually is.

Now, conceptually the testing of this proposition falls into two parts. The first is concerned with the measurement of the actual economic contribution of foreign-owned companies. This, in itself, involves not only calculating the value added of these concerns but the effect which their presence has had on the productivity of other economic agents in the domestic economy.

Second, we need to estimate the value of output which would have been produced in the absence of these firms or if such firms had been differently organized or differently financed, or the output these firms might have contributed had Government policy or institutional arrangements been different than they actually were.

There is a further complication. That is to isolate the contribution of foreign subsidiaries which is a contribution specifically the result of their multinational origin. For example, it may be that the large American subsidiary in Britain performs better than its indigenous competitors not because it is an offshoot of a multinational concern but simply because it is bigger than its competitors and that in this particular case size confers an economic advantage. If one is really interested in getting to the roots of the distinctive contributions of foreign-owned enterprises in relationship to indigenous firms, then I think we must pay particular care to compare like with like.

Can I briefly summarize at this point. From the viewpoint of the host country, the contribution of any foreign-owned multinational enterprise must be judged in the light of the extent to which it assists that country in achieving its economic objectives. Within the framework of any particular economic policy, this can be best assessed by evaluating its contribution to net output or growth of net output compared with the next best use of resources. On the other hand, it may be that multinational enterprises are not contributing the most to the economic welfare of host countries because these same countries are operating only second or third best economic policies.

For example, in its own interests the multinational firm will attempt to minimize its international tax burden by a variety of devices such as shifting profits from high tax to low tax countries. As a result, high tax countries might well find that their tax receipts from multinational enterprises fall; hence, so will the contributions of these enterprises to the community of which they are part. My argument here is that if this were shown to be the case, this would not be an argument for restricting the flow of inward investment but, rather, for tightening up loopholes in the domestic economy's tax regulations.

I now turn, Mr. Chairman, to illustrate some of the points which I have just made from the viewpoint of U.S. multinational enterprises operating in Britain. Excluding the effects of multinational enterprises on the terms of trade, I think there are two ways in which such foreign companies may affect the real income of host nations.

First, by their effect on the level of demand for resources, second, by their effect on the allocation of these resources.

As regards the first, I have estimated elsewhere that American firms have added about 0.3 percent to the GNP of the United Kingdom simply by locating their activities in areas of above-average unemployment and using resources which would have otherwise remained unused. I reckon that upward of 125,000 new jobs are being created in what we term the development areas in the United Kingdom by American-based companies, although it is possible that some of these extra jobs represent the movement of migrants from other parts of the country.

But most of the gains to Britain's real output arising from the presence of U.S. companies has, I believe, been due to the impact which they have had on resource allocation. This has occurred both because of the concentration of the activities of these companies in the more productive sectors of the economy, and because, in most cases, where they compete side by side with British companies, they seem to do rather better.

We looked, for example, at the labor productivity within 23 industrial groups in the United Kingdom in 1963, and we found that in 18 of these groups, foreign firms—these included firms of other nationalities than those of the United States—the foreign companies had a better record than all producing concerns. The mean productivity difference in the mid-1960's was about 20 percent, equivalent to a gain of something like 0.6 percent of GNP.

This differential, I think, is probably less today than it was some years ago because what evidence we have suggests that the productivity gap between foreign and United Kingdom firms is narrowing.

Equally important has been the split over or the spinoff effects of inward investment, that is, the impact on productivity within the domestic economy on all economic agents other than the investing companies, which is specifically the results of the presence of multinational enterprises. On these questions, there is a great deal of piecemeal evidence, hearsay and casual impressions, but I think that the data, both in respect of the United Kingdom and elsewhere, is sufficiently impressive to suggest that the spread of knowledge and entrepreneurship by multinational companies, particularly those of American parentage, is one of the most, if not the most, valuable contributions they have to make to host countries.

While I think it would be extremely difficult to attach a figure of the productivity gain to the United Kingdom of the kinds which I have just described, if I had to make a guess, it would be between a half and 1 percent of GNP. This, with the other two benefits, would give a total measurable benefit to the United Kingdom resulting from the presence of American companies of between 2 and 2½ percent of GNP. This, incidentally, compares with the figure of around 4 percent, which has been estimated by Canadian economists to be the net gain of American investment in Canada. My hunch, however, is that the figure I have just given for the United Kingdom is probably on the low side.

May I just remind you again that the share of American companies in the operations of United Kingdom manufacuring industry is increasing. In 1957 as I said earlier, less than 6 percent of the manufacturing sales were supplied by American companies. By 1966, this had risen to 10½ percent and I reckon that today the figure would be about 14 percent. Most of this expansion has been within American companies operating in Britain at this earlier date, between 1955 and 1967, the capital of the largest 100 American companies in Britain more than doubled while those of the leading United Kingdom public companies in similar industrial sectors rose by only two-fifths.

In research intensive sectors, American firms grew nearly four times the rate of their indigenous competitors and, as far as one can judge, in most industries, although not all, foreign companies have maintained or expanded their share of the local market.

Up to this point, Mr. Chairman, I have simply been concerned with giving some broad indications of the actual contribution of American investment to the United Kingdom economy over recent years. I have suggeested, I think, that this has been very much to the United Kingdom's benefit. But in view of the points which I raised earlier, I think host countries, and the United Kingdom is one of these, are now looking beyond the kind of assessment which I have just made, and asking whether subsidiaries of multinational enterprises are contributing the most they can to the local economy. That is to say, accepting foreign subsidiaries add to the economic welfare of the host country, are they adding to it as much as they possibly could, and could the benefits which undoubtedly accrue as a result of the presence of multinational enterprises nor have been achieved now cheaply by other means?

Now, let me stress that, in an economic context at least, this is not a question of whether foreign-owned enterprises are a good or a bad thing for host countries. I am simply trying to establish in which conditions they are most likely to be the first best way a country can obtain the ingredients for its prosperity. From the economist's viewpoint I would suggest the question is mainly one of price. To give a rather simple analogy: If consumers in Britain choose to buy Spanish rather than Florida oranges, this is not to argue that Florida oranges are, in any sense, bad—simply that, compared to Spanish oranges, British consumers think them to be too expensive.

Similarly, in some instances some nation states may conclude the price they are having to pay for the presence of some ultinational enterprises is, in some sense, too high: too high—that is, compared to the benefits which might be obtained from an alternative use of their resources. If the price is too high, then they will simply seek ways and means of reducing the price or try to buy the benefits more cheaply elsewhere.

In my prepared paper, Mr. Chairman, I have illustrated some possible Government policies toward susidiaries of multinational enterprises so that they can minimize this price and maximize the net benefits. I believe that this kind of strategy should in no way be interpreted as being antagonistic toward foreign investment, particularly where it is aimed at neutralizing certain advantages which multinational enterprises may enjoy over national enterprises. It is simply an attempt by the buyer of a group of products and services—in this case the Nation—to obtain these on the best possible terms.

Again, in my prepared paper, I have sought to distinguish between different types of policies to achieve this particular end, particularly those which we might term unilateral and those which we might term multilateral.

Now, as to the net benefits of the alternatives to foreign direct investment, I think I would argue we know very little. Indeed, as far as the United Kingdom is concerned we have not really been asking this question at all. Up to this point, as I have said, we have mainly been interested in assessing whether or not American investment in the United Kingdom has added to economic welfare, and the answer I have suggested is "Yes." But we are now starting to ask the question whether or not we might obtain these benefits in other ways. We certainly know that from the viewpoint of the investing businesses, foreign direct investment is generally preferred to licensing or joint ventures as a means of exploiting overseas markets, but form the host economy's viewpoint the choice is, by no means, as clear cut.

It may be asked whether or not there really is a problem here. Why cannot it be left to market forces to decide the issue? If the Government creates the right kind of economic environment then surely decisions of this kind are best left to the private sector.

Mr. Chairman, I think possibly there are three reasons why this is not the case, and all arise due to imperfections in the market. The first imperfection is the imperfection of information flows between countries and the relatively high cost of obtaining know-how at least, in research intensive industries. Second, is the fact that, at least, part of the cost of producing knowledge, and we have suggested that knowledge in one form or another is one of the most valuable contributions multinational enterprises have to offer host economies—is financed by the public sector. In other words, the public sector is already interfering—interfering perhaps is a rather loaded word here—but the public sector is already causing a pattern of resource allocation which is different from that which women arise in a free market.

Thirdly, there are important external or social costs of benefits associated with foreign investment, which do not fully enter into the calculation of multinational firms when deciding whether or not they should invest overseas or whether or not they should conclude licensing agreements or establish joint ventures. In my opinion, for these reasons host countries do require to carry out some sort of cost-benefit analysis of multinational enterprises and their alternatives.

Mr. Chairman, my time is finished, although I could say a great deal more. May I make just three points in summary?

Firstly, in studying the effects of multinational enterprises on host countries, I think it really is important—and this is not simply an academic arguing for more rigorous ways of presenting an argument—for us to try and specify exactly what one's objectives are, where possible separating the economic from the political aims. Unless one can, in some way or another, very precisely define what is one's attitude to such issues as economic independence, avoidance of foreign control, and terms pejorative as this, it is very difficult for the economist even to get to first base in his assessment of the contribution of multinational enterprises.

Secondly, assuming that one can specify a nation-state's economic goals, then it is only possible, to say very much about the contribution of foreign-owned companies if one makes some assumption of what would have happened in their absence or if their participation was less or greater, and this means that one has to make certain hypotheses about Government policies and institutions.

The final step is to assess whether the actual contribution of foreign-owned companies is the first best solution.

This involves, as I have just said, both estimating whether the net benefits arising from multinational enterprises are as high as they might be and also an evaluation of the net benefits of the alternatives which might be possible.

I suggest, Mr. Chairman, all of these latter issues involve positive and testable hypotheses. They do not involve value judgments. These come in later. They come in where one has to balance economic gains against, for example, loss of political sovereignty, and where there may be some sort of conflicts between particular economic objectives. Here I would argue that while the economist can try to evaluate the cost of benefits of alternative actions, in the end the final decision may well have to be taken on other than economic grounds.

I really do think that in our present stage of discussion of the multinational enterprise that we are not yet sure as to which of the type of propositions I have outlined this morning we are trying to test.

Thank you very much indeed, Mr. Chairman.

(The prepared statement and prepared paper, entitled "The Multinational Company and U.K. Economic Interests," of Mr. Dunning follow:)

PREPARED STATEMENT OF JOHN H. DUNNING

(A) INTRODUCTION: MULTINATIONAL ENTERPRISES AND NATION STATES

Mr. Chairman, I think we are entering a new phase about our thinking on the role of the multinational enterprise in the world economy. At least, the questions we are asking are changing. We have got beyond the stage of asking black and white questions, like—is the multinational enterprise a good or a bad thing; is it a force for free trade and competition or an agent for economic imperialism? To start with, we now recognise that it is not very helpful to talk about *the* multinational enterprise—as if this was a homogeneous phenomenon. The most one can hope to do is to identify particular forms of multinational enterprises—according, for example, to the economic activity in which they are engaged, the size and scope of their foreign operations and the way in which they are financed and organised—as these will greatly influence their impact on nation states of which they are part. For example, the balance of payments consequences to the U.S. of an investment by one of its petroleum companies in an oil drilling venture in the Far East may be totally different from an investment, of a similar amount, by a vehicles concern in new car assembly plant in Brazil. To the U.K., as a host country, the effects on real income of a 100% take-over of a U.K. firm by a fully integrated U.S. enterprise in a high technology industry, may be quite unlike an equivalent investment, jointly financed by U.S. and French interests, to produce (say) cigarettes or cotton textiles.

Much, of course, rests on exactly how one defines the multinational enterprise. There are some economists who take a very broad view, and think of any enterprise which operates *producing* units in two or more countries (three if one wishes to be strictly correct) as being multinational. On the other hand, there are those e.g. Professor Jack Behrman, who feel that this nomenclature should be confined to the type of company which organises its world wide operations in a closely integrated and harmonised way—and is strongly centralised in its decision taking. While I have a certain sympathy with this latter view as it pinpoints one of the main areas which distinguishes today's international firm from its predecessors, I believe that there are other ways in which one might delineate the boundaries of the multinational enterprise which make just as much economic sense.

It depends, in part, from *which* or from *whose* viewpoint one is examining the question. At a *macro*-level, for example, there are three main interests which are likely to be affected by the operations of the multinational enterprise—the economy of the investing country, the economy of host countries—and the economy of other countries, or the world economy as a whole. At a *micro*-level, there are the interests of the investing firm, its competitors, both in the investing country and in the host countries; and its suppliers and consumers. It doesn't even stop there. There are distributional and time effects to be considered. The multinational enterprise may influence the prosperity of different parts of countries in which it operates more than others—or of certain types of labour more than others; or the distribution between profits and wages. The short and long run effects of inward investment of a country's balance of payments needs to be carefully distinguished. My point here, Mr. Chairman, is that a lot of the discussion about the consequences of the multinational enterprise is very inconclusive simply because it fails to properly specify the particular criteria on which these consequences are to be judged.

This is particularly seen to be the case in the multinational enterprise/nation state controversy. Broadly speaking, multinational, like national, enterprises are interested only in private economic objectives. These may be quite complicated but all contain the ingredients of profitability and growth in a substantial measure. Nation states are much more complex in their goals. While the primary economic aims are fairly straightforward viz the maximisation of gross national product (g.n.p.) and rate of growth of g.n.p., their achievement, on the one hand, implies the satisfaction of a variety of subsidiary economic goals and, on the other, is circumscribed by the need to meet certain social, cultural or strategic targets.

In some cases, the nature of the economic system and the interpretation of the social "good" may be such as to exclude the operations of foreign owned enterprises altogether. Obvious examples are the communist bloc countries. For similar reasons, other countries may allow foreign companies to own only a limited equity of local enterprises. At the other extreme, there are nations which are politically very liberal and impose the fewest possible restrictions on either inward or outward investment. In between—as we well know—there are a vast spectrum of attitudes and policies towards the multinational enterprise. Not only do these differ between countries, but also within particular countries, depending, for example, on the extent to which foreign companies in general, or those of one nationality in particular, are likely to influence the achievement of that country's objectives.

This explains, in part, why up to the late 1950's there was very little concern about U.S. investment in Britain. After the last war, Britain (like the rest of Europe) needed all the capital and knowledge it could get. Even in 1957, U.S. firms were responsible for only 5.7% of the total U.K. manufacturing output and earned only 7.3% of the total profits. In the last decade, the rate of new American investment has risen by three times that of g.n.p.—and would have risen a great deal more had the U.K. gone into the E.E.C. Last year, U.S. financed firms accounted for about 12% of the output and nearer 20% of the net fixed capital formation in manufacturing industry, and about one-quarter of manufacturing exports. On present trends, something like 20–25% of manufacturing output will be in the hands of U.S. controlled enterprises by 1980.

Moreover this investment is very concentrated. The largest 50 U.S. subsidiaries account for more than four fifth of the total capital stake, and about three-quarters of the investment is concentrated in four industries viz oil refining, motor cars, chemicals and electrical engineering—which also happen to be among the most research intensive industries. In my written statement, I append a table I compiled some two years ago on the contribution of U.S. firms to the production of certain products in the U.K.

It is the prospect of growing participation of foreign and particularly U.S. capital, which is causing—in some sectors of the United Kingdom at least—some cause for concern. Though this concern—perhaps unease would be a better word is rarely spelled out, and is in some cases little more than xenophobia. Very often it is triggered off by an isolated happening in a U.S. controlled firm like the Roberts Arundel affair in 1967, or the transference of part of Remington Rand's production from a British factory to the Continent in 1969—or the take-over of a technologically advanced United Kingdom firm by a U.S. firm, where some of the research and development activities are subsequently removed to the United States. In spite of these cases being rare, the possibility of their being rather more widespread in the future than in the past has led to some rethinking of the role of the foreign owned multinational enterprises in the United Kingdom—typified best I think by the chapter devoted to this topic in the latest Trades Union Congress Economic Review.

Other reasons for the dislike of foreign investment by host countries have been well discussed in writings of Professors Harry Johnson and Charles Kindleberger and I do not propose to reiterate these this morning—save to agree with both these distinguished economists that, from an economic standpoint, most of these are second best arguments. The point I wish to emphasise is that attitudes towards multinational enterprises by nation States, though often formulated in economic terms, are often political at root and will differ inter alia according to the extent to which foreign participation is likely to affect the goals of domestic policy.

Here I think all the economist can do is to estimate the economic consequences of alternative attitudes and policies. Rarely are political and economic aims precisely defined. The British, for example, have as a declared policy, the development of an indigenous electronics industry. What this means in terms of the extent to which foreign participation will be allowed no one knows. Presumably a 40 percent stake is acceptable but a 90 percent stake would not be. Where the proportion becomes unacceptable is a moot point and, I would have thought, could not be rationally determined a priori, without a thorough examination of costs and benefits not only of the additional foreign investment, but of its possible alternatives.

(B) The Economic Issues Involved: The Host Country's Viewpoint

For the rest of my submission, I would like to confine my remarks to the economic issues. In other words, I will assume the sole criteria of a host country's attitude towards foreign owned multinational enterprises is whether or not they contribute more to its economic objectives than any other pattern of resource usage. I will further suppose the host country has only two aims—the maximisation of real output and rate of growth of real output. The question is to what extent are the operations of the subsidiaries of foreign multinational enterprises likely to provide a first best solution in advancing these aims.

Can one formulate this question in terms which can be tested? I think one can (even though, in practice, the testing is a very difficult thing to do) *provided that*, and this is an important proviso, one makes some assumption about what would have happened in the absence of inward investment—or if it were $x\%$ less or more than it is. The proposition is—if the addition to the community's real output supplied by resources used by multinational firms (less any part of this output remitted to the investing country) is greater than those same resources could have produced, if used differently or under different ownership, then, multinational firms are advancing economic objectives.

Now, empirically, the testing of this proposition falls into two parts. The first is to measure the actual contribution of foreign firms: this, in itself, involves not only estimating their net output or value added, but the effect which their presence has had on the net output and productivity of other firms in the economy. Second, we need to estimate the net output which would have occurred in the absence of such firms—*or* if such firms were differently organised and/or financed, *or* these firms would contribute, if Government policy on institutions were different.

There is another problem. That is to isolate the contribution of foreign subsidiaries, which is due *specifically* to their multinational origin. For instance, it may be that a large U.S. subsidiary performs better than its U.K. competitor—not because it is an offshoot of a multinational company, but because it is bigger than its competitors and that, in this instance, size confers an economic advantage. If one is interested in the distinctive contributions of foreign owned enterprises, vis a vis indigenous firms, then it is important to compare like with like.

Let me briefly summarise at this point. From the viewpoint of a recipient country, the contribution of *any* multinational enterprise must be judged in the light of the extent to which it assists that country in achieving its economic objectives. *Given* a particular economic policy, then this can be assessed by evaluating its contribution to net output, or growth of net output, compared with the next best use of resources (which itself may be difficult to specify). On the other hand, it may be that multinational enterprises are not contributing the most to the economic welfare of host countries because of second best economic policies or regulations. (An obvious case in point is that, in its own interests, a multinational firm will attempt to minimise its international tax burden by various devices e.g. shifting profits from high tax to low tax countries. As a result, high tax countries find that their tax receipts from the multinational company fall—hence its value to the community. This, however, is not a case for restricting the flow of investment—but for tightening up loopholes in the tax regulations.)

(C) Empirical Evidence

I now turn to illustrate some of the points I have made from the viewpoint of U.S. multinational enterprises operating in the U.K.

EFFECT OF INVESTMENT ON THE U.K.'S REAL INCOME

Excluding the effects on the terms of trade, there are two main ways in which multinational enterprises may affect the real income of host countries. First, by their effect on the level of demand for resources; second by their effect on the allocation of these resources. As regards the first, I have elsewhere estimated[1] that U.S. firms have added about 0.3% to the g.n.p. of the U.K. simply by locating their activities in areas of above average unemployment (in the North East, Scotland, Wales etc.) and using resources which would have remained unused (in spite of the Government's attempts to create full employment in these areas.) Upwards of 100,000 new jobs are being created in these areas—though admittedly some of these are possibly migrants from other parts of the country.

Most of the gain to real income arising from the presence of U.S. firms in the U.K. economy is, however, due to their beneficial impact on resource allocation. This has occurred both by the concentration of their activities in the more productive sectors of the economy and because, where they compete side by side with indigenous firms, they do better. (In 1963, for example, of 22 industrial groups, *all* foreign firms had a higher labour productivity than all producing firms in the U.K. in 17 cases.) The mean (total) productivity differential in the mid 1960's was about 20%—equivalent to a gain of about 0.6% of g.n.p. The differential is probably rather less today as such evidence we have suggests that the productivity gap is narrowing.

Equally important has been the spillover or spin off effects of inward investment i.e. the impact on resource utilisation and productivity of firms other than the investing firms, which is specifically due to their presence *and* foreign affiliations. On these questions, there is a great deal of piecemeal evidence, hearsay and casual impressions. But in general, data both in respect of the U.K. and elsewhere is impressive enough to suggest that the dissemination of knowledge and entrepreneurship by multinational firms (particularly those of American parentage) is one of the most—if not *the* most—valuable contribution they have to make to host countries.

Such a contribution may be *vertical*—e.g. knowhow passed on to suppliers and customers of U.S. firms; or *horizontal*—e.g. the stimulus given to competitors—regional or industrial. More generally, information is disseminated by the mobility of personnel, by the informal interchange of ideas among executives, by the publicity of various management and administrative practices. However much it may be possible to protect innovations in product or process technology, "human technology", e.g. advances in management, marketing, labour relations, capital budgeting etc. and so on, are very difficult to keep quiet. In a variety of ways such as these, U.S. knowhow penetrates the local economy. No less important is the added competitive stimulus afforded by these firms, the parent companies of which are likely to be among the most dynamic in the U.S.

It would be extremely difficult to attach a figure of the productivity gain to the U.K. economy of the kind just described—but my best guess is that it would be in the region of ½% and 1% of g.n.p. This would give a total (measurable) benefit to the U.K. economy resulting from the presence of U.S. firms of between 2 and 2½% of g.n.p. My hunch, however, is that this is on the low side.

[1] *The role of American investment in the British economy,* Political and Economic Planning, Broadsheet No. 507, February 1969.

Improvements in productivity over time largely reflect the rate at which advances in resource usage and efficiency are taking place. As we have said, such improvements may arise from a switch of resources from less to more productive sectors (or a concentration of new resources in these latter sectors) or an increased flow of resources towards more productive firms within particular sectors; or simply an increase in efficiency in any particular firm. This latter, in turn, may be brought about by the introduction of superior production or management techniques or by a better utilisation of existing techniques. It may also reflect economies of large scale production.

The share of the subsidiaries of U.S. and other foreign controlled multinational firms in the g.n.p. of the U.K. is increasing. As we have said, in 1957, about 5% of the sales of manufacturing industry were supplied by American subsidiaries. By 1966 this had risen to 10.5% today the figure would be nearer 14%. Most of this expansion has been within U.S. affiliates already operating in 1955. Between that date and 1967, the net assets of the largest 100 American manufacturing subsidiaries in the U.K. more than doubled, while those of the leading U.K. public companies rose by only two-fifths. In the research-intensive stecors, U.S. firms grew nearly four times the rate of their indigenous competitors. In most (but not all) industries, foreign firms have maintained or expanded their share of the local market.

Our time series data are insufficient to allow us to make and *productivity* growth comparisons, but until the mid 1960's, at least, this favoured American subsidiaries—even though, relative to domestic competitors, their profitability has been falling since 1955.

(D) Is the Multinational Enterprise a First Best Solution?

Up to this point, Mr. Chairman, I have simply been concerned with giving some broad indications of the actual contribution of U.S. investment to the U.K. economy, given the environment in which it was made. But, in view of the points I raised earlier, I think host countries are now looking beyond this kind of assessment and asking whether (a) subsidiaries of multinational enterprises are contributing the most they can to the local economy and (b) whether the benefits which they confer could have been obtained in other (and cheaper) ways.

Let me stress that—in an economic context at least—this is not a question of whether foreign owned multinational enterprises are a "good" or a "bad" thing for host countries—simply in which conditions are they likely to be the cheapest way a country can obtain the ingredients for its prosperity. From the economist's viewpoint the question is mainly one of *price*. To give an analogy, if consumers choose to buy Spanish rather than Florida oranges—this is not to argue that Florida oranges are "bad"—simply that in relation to Spanish oranges they are thought to be too expensive.[2] Similarly, in some instances, some nation states *may* conclude the price they are having to pay for the presence of some multinational enterprises is too high i.e. in relation to some alternative use of resources. They then either seek ways and means of reducing the price or "buy" the benefits elsewhere.

In my prepared paper, I have illustrated some possible Government policies towards subsidiaries of multinational enterprises to minimise this price or maximise the net benefits. *Such a strategy should, in no way, be interpreted as antagonistic towards foreign investment*—particularly, where it is aimed at neutralising certain advantages which multinational enterprises may enjoy over national enterprises. It is simply an attempt by the buyer of a group of products and/or services to obtain these as cheaply as possible. In my written statement I have sought to distinguish between various types of policies to achieve this end—particularly those which we might term unilateral and multilateral. Only multilateral policies, for example, can resolve the difficult problem of extraterritorality.

As to the net benefits of the alternatives to foreign investment, we still know very little indeed. We do know that from the viewpoint of the investing businesses foreign direct investment is generally preferred to licensing or joint ventures as a means of exploiting overseas markets. From the host economy's viewpoint the choice is by no means as clear cut.

[2] Let it also be said that the producers of oranges may reasonably wish to obtain the maximum price for their produce. If the producers of Florida oranges can get a better price in Canada than in the U.K. then they will sell their supplies to the former market.

It may be asked where there is a problem? Why cannot market forces decide this issue? If the Government creates the right kind of economic environment, surely decisions of this kind can be left to the private sector.

I think there are three reasons why this is not the case—and all arise due to imperfections in the market. The first is the imperfection of information flows between countries and the relatively high cost of obtaining knowhow. Second, is the fact that at least part of the cost of producing knowledge (and we have already suggested that knowledge of one form or another is one of the most valuable contributions multinational enterprises have to offer the U.K. economy) is financed by the public sector, where market considerations may be secondary to others. Third, there are important external or social costs and benefits associated with inward investment which do not fully enter the calculations of multinational firms when deciding their investment programmes. For these reasons, host countries require to do some kind of cost/benefit analysis of multinational enterprises and their alternatives.

Mr. Chairman, my time is finished—although I could say a great deal more.

In summary I would like to make three points:

(1) In studying the effects of multinational enterprises on host economies, one must try and specify exactly what one's objectives are, where possible, separating the economic from the political aims. Unless one can, in some way, define one's attitude to issues such as "economic independence", "avoidance of control" and so on—it is very difficult for the economist to get even to "first base."

(2) Supposing that one can specify a nation state's economic goals, then it is only possible to say much about the contribution of foreign owned multinational enterprises if one makes some assumption about what would have happened in its absence. This means one has to make certain hypotheses about Government policies and institutions.

(3) The final step is to assess whether the actual contribution of multinational enterprises is the 'first best solution' (from the viewpoint of the host economy). This involves both estimating whether the *net* benefits (=gross benefit less costs) of the multinational enterprise are as high as they might be—and an evaluation of the alternatives which might be possible.

All of these later issues involve positive and testable hypotheses. They do not involve value judgments. These come in later when one has to balance economic gains against loss of sovereignty, etc., and when there may be certain conflicts of economic objectives. Here, while the economist can try to evaluate the costs and benefits of alternative actions (e.g. the marginal net benefit [or loss] of an increased U.S. stake in U.K. car industry from 30–45% cf. 49–64%) in the end the final decision may have to be taken on other than economic grounds.

In our present stage of discussion of the multinational enterprise, I am not sure we are yet clear as to which of the propositions I have just mentioned we are trying to test.

PREPARED PAPER OF JOHN H. DUNNING

The Multinational Company and U.K. Economic Interests

THE U.K. AS A HOST TO INTERNATIONAL COMPANIES

The U.K. has always adopted a welcoming attitude towards inward direct investment and, subject to certain safeguards, now rather more explicitly laid down than in the past, official policy is still cordial. Nevertheless, in certain sectors of Government (e.g. the Ministry of Technology) and in the economy as a whole, warning voices have been raised, that the benefits of foreign participation in U.K. industry are not quite so unequivocal as was once thought.

The basic concern arises not so much from the size of the present stake of foreign participation but, by certain of its characteristics, notably its very marked concentration in certain industries, its market structure, its geographical origin and its very fast rate of growth.

The facts have been documented elsewhere [1] and need only be very briefly summarised here. About 70% of the value of the direct foreign capital stake in the U.K. (which, at the end of 1968, totalled £3,500 m.) is U.S. owned. More

[1] J. H. Dunning "Foreign investment in the United Kingdom" in I. A. Litvak and C. J. Maule *Foreign investment: the experience of host countries* Praeger, New York, 1970.

than one-half of this amount is accounted for by the largest 50 subsidiaries and about three-quarters by the largest 100. The investment is strongly concentrated in the technologically advanced industries, in motor vehicles and in oil refining and distribution. In most of these industries, which also tend to be dominated by a few large firms—foreign subsidiaries are among the leading three producers—and, in several, they supply more than one-half the total output. Since these are the fastest growing industries in the economy, and, within them, foreign firms are growing faster than their competitors, the stake of these companies in the national economy is increasing.

So much for the basic facts. What of their implications for U.K. Government policy? Does it matter if a large proportion of U.K. output is supplied by subsidiaries of international companies? Are not these subsidiaries subject to the same laws and economic sanctions as their domestic counterparts? Is there any need for specific Government policy to either stimulate or curb the operation of these firms—or to control their behaviour?

To answer these questions we need first to distinguish the ways in which foreign owned enterprises are economically different from their indigenous competitors and the extent to which they react differently to government policies. We shall discuss three possible areas of differences under the general headings of objectives, organisation and operational impact.[2]

OBJECTIVES

First, *objectives*. However much a subsidiary of a multinational enterprise may seek to identify itself with the U.K. economy, its primary responsibility is to the management and shareholders of its parent company. Where it is in their best interests to raise the efficiency and stimulate the growth of the U.K. subsidiary, then, generally speaking, "what will be good for Wall Street will be good for the U.K. economy". On the other hand, whereas in the final analysis, the foreign firm will judge the succes of its subsidiary in terms of the return on the capital invested, the U.K. economy is best served when the *local* value added by the subsidiary is maximised; here income remitted represents a price which has to be paid for the resources provided by the investing company. What is regarded as a reasonable price may well vary according to the type of investment made and the country in which it is made. It will also partly depend on the price offered (e.g. in the form of tax rebates, investment allowances, etc.) by other countries. But, basically, host Governments can do little about influencing the objectives of foreign companies, except in so far as, by providing a favourable economic environment, they can orientate behavior towards growth and stability.

ORGANISATION

Second the *organisation* of foreign subsidiaries. Even a *national* multiplant firm has certain advantages over a single plant firm. It has, for example, the choice of whether to produce similar products in the separate plants or to engage in vertical specialisation; it may also be better placed to gain from local market conditions—both in its buying and selling operations. As one widens the locational choice across national boundaries, so the character of economic environments becomes more distinctive; hence the especial advantage of the international producing firm to increase its product or process specialistion.

Such evidence we have suggests this kind of international division of labour exists more in high technology than in low technology industries. A classic example is that of I.B.M. In 1957 I.B.M. abandoned the idea of making complete product lines for each separate European markets. Nowadays computers for sale in the U.K. are assembled in France from discrete segments or subassemblies made in different parts of Europe.

The economic implications of this type of multinational vertical or horizontal integration on the operation of foreign subsidiaries in the U.K. are numerous and far reachng. From a functional viewpoint, the most significant is it usually requires highly centralised and carefully harmonised decision taking (whatever contribution to this decision taking representatives from the subsidiaries may make).

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[2] Parts of the following paragraphs are taken from an article written by the author in *Government and Business* June 1970 (obtainable from Economists Advisory Group, 33 Southampton Street, London W.C. 2.)

Apart from products produced for local markets, the decision on what and how much each subsidiary should produce, where new factories are to be located and, very often, the amount and form of intra-group trading, are taken with global needs and opportunities in mind. To an extent, all international trade is similarly conducted; but the fact that *production* is internationalised inroduces a completely new dimension.

The other main implication of the internationalisation of production is that economic inter-dependence between nations is increased. Such inter-dependence is obviously implicit in division of labour; but its success largely depends on the unhampered movement of goods and services—including factor inputs—*within* the international company. Indeed, it may well be that the single most important contribution of the international company to world economic welfare is that, more than any other institution, it is helping knit together national economies, and, in doing this, it is succeeding where Governments have failed.

In theory, of course, a company should buy from the cheapest and sell in dearest world markets. In practice, it does not operate like this partly because it is not physically present in these markets, and partly because of the constraints imposed on the trade between two (or more) parties across national boundaries. But the international company is better able to get over both these difficulties, as it is able to transfer resources across national boundaries without actually engaging in trade. Since, in this respect, it will generally act as a cost minimiser, this means that it helps to introduce an element of "perfection" in world markets. For example, the shifting of funds between subsidiaries in order to take advantage of lower interest rates, tends to make a more, rather than less, efficient world capital market; the specialisation of foreign operations in labour or capital intensive activities according to the factor price structure of the recipient countries, narrows rather than widens the international differential of factor prices. By increasing the supply of goods to where they are most highly priced relative to other markets makes for a better, rather than a worse deal for consumer.

There are, however, costs involved in these intra-group activites which not all national economies are prepared to accept. Foremost of these is the surrender of a certain degree of control over national economic policy. However much the movement of capital between the U.K. and another country by the international company might help world capital markets, it may also weaken the impact of domestic monetary policy—and possibly, too, exert pressure for exchange rate adjustment. It has, for example, been estimated that speculative movements of capital by international companies into Germany in 1969 accounted for one-half of the total capital inflow in that year; the transference of research laboratories of a U.S. electronic subsidiary from Britain to Italy might be a sensible strategy both from the viewpoint of the investing company and world economic welfare, it may also weaken attempts to build up indigenous research facilities in the U.K. Similarly for the XYZ motor company to produce a different range of components of a particular motor car in half a dozen countries, but the final product in only one country, may well be a highly profitable thing to do, but it will hardly be welcomed by countries who wish (rightly or wrongly) to have their own motor car industries.

In other words, the more completely fully multinational companies take advantage of differences in national economic environments, provided they operate in a competitive market, the nearer they will come to maximising world real output. But, in so far as national policies are inconsistent with this end (and/or each other's objectives), conflicts are bound to arise. There may also be conflicts as to the best distribution of output, both within particular countries and between capital and labour.

This is then the first reason why Governments find themselves concerned about the multinational company. In one sense it is no new story; it is a continuation of an old story about the relationship between national and world economic welfare. Having said this, however, we must now enter a caveat. Even accepting that, if left to its own devices, the multinational company would help to distribute resources more efficiently—from a world viewpoint there are two reasons why the market as it is at present organised cannot fully ensure this. The first arises from the action of *Governments* and the second is *externalities* or *spillover effects* of multinational companies.

Actions of Governments to advance economic welfare of their citizens affect the behaviour of international companies in a variety of ways. We shall illustrate three of these. The first is the way in which they tax the income of foreign firms, and generally treat foreign investment. One aim of all international companies is to minimise their total tax burden. If it were feasible it would pay an multinational enterprise to *record* profits only in the lowest tax country in which it operates. As a general rule, however, the greater the differential the tax rates between countries in which the international company operates (including the "home" country), the greater the incentive of tax avoidance in high tax countries by the manipulation of intra-company transfer prices. And the more efficiently this is done, the more the high tax countries lose. Enterprises may also wish to sell at other than arms length prices, to insure against possible exchange rate changes, divided restrictions, nationalisation etc.

Second. Governmental policies towards trade, e.g. as shown in its tariff structure, exchange controls, export credits etc. can and do affect the flow of goods and services both traded between international companies and other economic agents and transferred *within* international companies—indeed the structure of their operations. One recent example is the effect which the formation of the EEC has had on the distribution of U.S. investment between Britain and the EEC countries.

Third, there is the question of extra-territorality. This arises wherever the investing country imposes rules and regulations which apply not only to companies operating in its boundaries but to the foreign subsidiaries of these companies. The most quoted examples of extra-territorality, operating against the interests of recipient countries, are controls exerted by the U.S. Government on the external trade of U.S. subsidiaries and U.S. anti-trust legislation, which may outlaw mergers which would be in the best interests of the host country. There is, however, little evidence that either of these instances has been an important constraint on the behaviour of U.S. subsidiaries in the U.K.

OPERATIONAL IMPACT

The second issue, surrounds the question of the externalities, "spill-over" or "spin-off" repercussions of inward investment. In our present context, this is the effect which U.S. subsidiaries have on the efficiency and growth of other firms in the U.K. economy and is part and parcel of the third possible area of conflict, which arises from the operational and economic impact of international companies. Assume, for the moment, that this contribution can be measured directly or indirectly by the contribution of U.S. subsidiaries to the gross national product (g.n.p.) of the U.K. Again, we are interested in the consequences which follow *specifically* as a result of the American ownership of the firm. To estimate this, it is best to suppose that in their absence, the resources released would have otherwise been used; clearly, however, the "American" contribution to national output will differ according to the "alternative position" assumed.

The key contribution of the U.S. subsidiaries to the U.K. economy is the package deal of American entrepreneurship, capital and knowledge they make available. If this, when added to local resources, produces a contribution to the g,d,p, greater than that of any other use of these resources (after deduction of any income remitted) then their economic worth is justified.

Such information we have, from a variety of sources, suggests that U.S. firms in the U.K. have indeed made a very valuable contribution in this respect. They are concentrated not only in the technologically advanced industries; but also in ones where comparative innovating advantage of the U.S. is probably the greatest. These subsidiaries not only have access both to research and development facilities of the group but also to its cumulative management experience. In view of this, it is not surprising that the productivity of U.S. subsidiaries is, on average, about 20% higher than their U.K. competitors. No less valuable, however, are the spillover effects of the imported expertise on competitors, suppliers and customers of U.S. firms, and on management and labour practices in the U.K. economy in general. Though quantitatively extremely difficult to assess, these effects are known to have been very far reaching. Indeed, almost certainly, the assimilation of improved production and management techniques has been instrumental in lowering the profitability gap between U.S. and U.K. subsidiaries by more than one-half since 1955.

Improved productivity is undoubtedly a benefit to the U.K. economy. What about the costs? There are some which might occur. First, it is possible that foreign firms may lead to a less efficient and/or less competitive industrial structure. There is no reason to suppose that this has occurred. It is true that American firms have encouraged a more oligopolistic type structure in U.K. industry but this has generally aided, rather than retarded the rationalisation in U.K. industry. Second, the production methods of foreign firms may not always be suitable to the resource and/or market structure of the recipient country. U.S. subsidiaries tend to be more capital intensive than their U.K. competitors, but usually this is to their advantage. In the case of foreign participation in some of the less developed countries this is likely to be a more important issue: not always do such firms appear to make the best use of the most plentiful local resources. Third, foreign investments may bring with it possible technological drawbacks. We have dealt with some of these in more detail elsewhere,[3] but much of the problem arises because U.S. firms are able to buy U.K. knowledge below the appropriate "social" price.

POLICY IMPLICATIONS

These, then, are some of the important issues surrounding the participation of foreign firms in the industry. What do we conclude are the policy implications for Government? Empirically, the evidence is that foreign subsidiaries of multinational companies have considerably benefited the U.K. economy *operationally* and that from an *organisational* viewpoint there is little immediate cause for concern: this is not to deny that, in certain instances, considerable friction has arisen but most of the concern so far expressed arises from possible rather than actual situations.

Suppose that, at any given moment of time, the U.K. authorities wish to maximise the national output from the resources available and that, over time, they aim to maximise the rate of growth of national output, subject to some overall social welfare constraint (e.g. a "fair" distribution of income). How can the authorities encourage foreign firms to behave so as to best meet these objectives? Policy in other countries varies from outright discriminatory action against foreign investors (Japan) to controlling the amount of foreign participation (India), to laying down broad guidlines of behavior for U.K. firms (Canada). At present, as we have seen, apart from certain safeguards required from foreign firms about e.g. the amount of local capital they wish to raise, policy towards exports etc. the U.K. Government's attitude is relatively free and easy.

But with the growing role of foreign firms how long can this last? The following paragraphs consider this question in relation to several distinct types of policy. The first distinction is between policy decisions taken by authorities in individual countries—or sectors of these countries—which we might call *unilateral* policies and those which involve more than one country—i.e. *bilateral* or *multilateral* policies. Secondly, we need to differentiate between *general* policies—which affect all firms including foreign subsidiaries—and *specific* policies—directed only to foreign subsidiaries. Third, there is the type of policy which may be desirable to undertake, irrespective of the effect which foreign investment has on the economy. We call this *unconditional* policy, to distinguish it from *conditional* policy, the character of which will vary according to the nature of the impact made by the foreign company. Finally, there is policy which is directed to altering the behaviour of foreign subsidiaries to conform to some stated objectives—and policy, the purpose of which is to change the economic environment in which foreign firms operate. Let us briefly illustrate the relevance of these types of policies to the U.K. situation.

UNILATERAL POLICIES

Of *general and unconditional unilateral policies* the first essential is to create a market environment, such that foreign firms should not be able to exploit their economic power to the detriment of the U.K. economy. In some cases, this may involve the Government assisting native firms to rationalise their businesses even to the extent of backing intra-European mergers (e.g. the Dunlop/Pirelli case). It also implies that Governments should try and see that when one firm takes over another it pays a fair "social" price; that enough information is published about the operations of firms—including foreign companies—to help firms make the right decisions; that it should minimise the barriers to the dissemination of knowledge; and that it should encourage the provision of information to U.K. firms on the alternatives to inward investment (e.g. licensing agreements, etc.)

Specific and unconditional unilateral policies arise because of differences

[3] J. H. Dunning and M. Steuer, "The effects of United States investment in Britain on British technology" *Moorgate and Wall Street,* Autumn 1969.

between the economic impact of foreign and domestic firms. To allow for these and to counteract any imperfection in market conditions which might result, use may be made of discriminatory fiscal, monetary or direct controls. It has been argued, for example, that foreign companies have certain technological and financial advantages over U.K. firms: if this is so, it may be questioned whether some of the incentives given to companies e.g. to go to development areas, are really necessary. Similarly, because of the loss of income to the community which arises from income remitted, it may be desirable for the Government to introduce selective measures that would reduce this outflow. *Inter alia* this implies that the authorities should keep a watchful eye on all international transactions of foreign firms to see that they are not remitting income through "unfair" transfer pricing. Less desirable, in my opinion, is any *general* attempt to lay down a code of "good" corporate behaviour—partly because it is difficult to determine what this is, as it varies between firms and over time, and partly because it may encourage actions on the part of foreign firms which may not be in the country's best interest.

Of the *specific and conditional unilateral policies*, these by definition, assume that either it is felt that there is too much or too little foreign investment in the U.K. economy, and/or that certain actions of foreign companies should be stimulated or curbed. Various aspects of the operational impact of the international company come to mind—the effects on the balance of payments, the ability of the company to circumvent certain policies introduced by national Governments and so on. One of the reasons commonly given for introducing a code of good behaviour is to minimise these effects.

Of course, in response to the effects of foreign direct investment, it may be preferable that *general* policy should be changed. Such a *general and conditional policy* is particularly appropriate where foreign investment makes an important marginial impact on certain areas of *macro*-economic policy, e.g., the balance of payments. Rather than discourage this investment where if it has an adverse balance of payments effect, it may make better economic sense to alter general economic policy, so as to make it unimportant whether it has these effects.

MULTILATERAL POLICIES

We now turn to illustrate bilateral and multilateral policies. Sometimes these involve two or more *investing* countries; but more usually, insofar as inward investment is concerned, investing and recipient countries and/or two or more recipient countries. Again, it is possible to classify policy according to the headings earlier used but here we shall content ourselves with one or two broad observations.

Most issues of extra-territorality involve investing and recipient countries, and can only be settled by bilateral general or specific unconditional policies. On the other hand, attempts to prevent recipient countries from using "unfair" practices with respect to encouraging (or discouraging) foreign investment, require multilateral general policies. Outside the economic sphere, there is a need for harmonisation of policy with respect to legal and accounting procedures. The concept of a "European" company is already firmly established; the possibility of a world company is no longer a pipe dream. Accompanying this, there may well be need for a parallel to the International Court of Justice to deal with international disputes arising from the operations of international firms.

Finally, mention should be made of a group of problems arising out of the international company, which only a sectoral unilateral or multilateral policy can resolve. Of these, the best example of the attitude of labour to the international company. There are two issues here. First, trades unions may well seek for a general harmonisation of wage rates in all countries in which the company operates; second, there is the question of the effects of the operations of the international company on employment. Each of these issues could raise serious problems in the not too distant future; a glimpse of these is shown in the T.U.C. Economic Review for 1970.

SUMMARY AND CONCLUSIONS

To summarize: the international company is a powerful force in helping to break down economic nationalism between countries. Simply because of this it poses real problems for those countries which wish to retain complete control over their destinities.

There is an inherent conflict between the objectives of the international company and the nation states of which they are part.

From a purely economic standpoint, any host country has to pay a price for buying the services of a foreign company. But as with trade, both parties may benefit from the exchange. The question is what is the "right" price? As far as possible this should be a competitive "social" price i.e. the market price adjusted for the spill-over effects and Government action. In international trade, the General Agreement on Tariffs and Trade exists to control "unfair" trading practices between countries. There is reason to suggest that something similar may eventually be needed in the field of international direct investment. But, in my opinion, it is up to Governments—rather than international companies—to take the initiative in this respect—and also to encourage the international harmonisation of law, accounting and tax procedures.

The object of both unilateral and multilateral Governmental policy to the international company should then be to assist it in its world competitive role. Countries which are nationalistic in outlook will, however, find this suggestion disturbing, as the international company does run counter to this philosophy. For the U.K., the issue is a vital one. *Par excellence* this country is a two-way international investor. Its combined income received and paid on foreign direct investment, as a proportion of its g.d.p., is considerably greater than any other advanced country. In my opinion, it cannot afford the (dubious) luxury of economic nationalism—and this it is in its best interests to pursue as liberal a policy to both inward and outward investment as it possibly can.

APPENDIX

It has been possible to compile a list, from a number of sources, of the approximate share of the total production by all U.K. enterprises, of various products, accounted for by foreign-financed companies at the end of 1966. In some cases their share of the global goods bought by U.K. consumers will be less, due to the contribution of imports.

80% or more

Boot and shoe machinery, carbon black, color films, custard powder and starch, sewing machines, tinned baby foods, typewriters.

60–79%

Agricultural implements, aluminum semi-manufactures, breakfast cereals, calculating machines, cigarette lighters, domestic boilers, electric shavers, instant coffee, potato chips, razor blades and safety razors, refined petroleum produces, soaps and detergents, spark plugs, tinned milk.

50–59%

Cake mixes, cosmetics and toilet preparations, electric switches, ethical proprietaires (drugs sold to National Health Service), frozen foods, foundation garments, pens and pencils, motor cars, pet foods, petroleum refinery construction equipment, refrigerators, rubber tyres, tractors, vacuum cleaners.

15–29%

Computers, locks and keys, photographic equipment, printing and typesetting machinery, watches and clocks.

30–39%

Abrasives, commercial vehicles, dental equipment, floor polishers, elevators and escalators, portable electric tools, washing machines.

15–29%

Greeting cards, industrial instruments, materials handling equipment, medical preparations, soft drinks, mining machinery, paperback books, petro-chemicals, synthetic fibres, telephones and telecommunications equipment, toilet tissues.

Foreign firms are also important producers of specialized automatic transmission equipment, copper tubing and nickel alloys, cork products, electric blankets, chocolates and candies, kitchen apparatus, laundry machinery, ophthalmic products, plastic semi-manufactures, radio and television apparatus, refined platinum, specialized machine tools, and vegetable oils and fats. Outside manufacturing industry, U.S. credit and financial reporting, market research and the production and distribution of films. Foreign firms account for about 20 per cent of the bank deposits in Britain. Two of the leading car rental companies are U.S. owned, as are several publishing companies, hotels and supermarkets.

Representative WIDNALL (presiding). Now, we will hear from the next witness, Mr. Paul Jennings, president of the International Union of Electrical, Radio and Machine Workers.

Before you start, Mr. Jennings, may I just add to the welcome that was given to you by Mr. Boggs earlier and I want to join in welcoming you and acknowledge the fact that you are going to give some very valuable testimony to this committee. Proceed.

STATEMENT OF PAUL JENNINGS, PRESIDENT, INTERNATIONAL UNION OF ELECTRICAL, RADIO & MACHINE WORKERS

Mr. JENNINGS. Thank you, Mr. Chairman. My name is Paul Jennings and I am appearing here today as chairman of the Committee on World Trade of the Industrial Union Department of the AFL-CIO. I am president of the International Union of Electrical, Radio and Machine Workers, AFL-CIO.

I want to express my appreciation for the committee's invitation to appear before it and to address myself to the questions of the multinational corporation and international investment.

1. U.S.-based multinational corporations were expected to spend $12.7 billion on foreign plant and equipment in 1970, an increase of 20 percent, or $2.1 billion, above the estimated $10.6 billion in 1969. In 1968, direct investments of U.S. firms in foreign subsidiaries, plants and other facilities amounted to $9.3 billion. In 1960, the figure was $3.8 billion. Such investments are financed partly by U.S. capital outflows, partly by retained profits and depreciation of foreign subsidiaries, partly by foreign-raised capital.

Outlays of U.S. companies for new plant and equipment in foreign manufacturing facilities—exclusive of oil, mining, and other activities—jumped from $1.4 billion in 1960 to $4.5 billion in 1967. Outlays reached $5 billion in 1969, according to a McGraw-Hill business survey, and should reach $5.6 billion this year. Between 1967 and 1969, investment in foreign plant and equipment in the electrical-electronics industries alone totaled more than $1 billion.

The figures on plant and equipment outlays are a mere token of the total size and scope of the changes now taking place even for direct investment. But these figures have shown a growth of at least 10 percent yearly for the past 10 years. As a recent issue of the Journal of Marketing (July 1970) explained—

> A development of this magnitude will inevitably shape the international environment for business in the seventies and beyond. Its implications for academicians, businessmen and government policy makers have not yet been fully appreciated.

The figures on U.S.-based outlays are reportedly better than those multinationals based in other countries. The spread of U.S.-based multinationals abroad has been called the American Challenge. This term is a misleading label. The multinational corporation's planning is not necessarily American. It is related to the firm's advantage, not to the advantage of the Nation. (What's good for General Motors is not necessarily good for the United States of America. What's good for Mitsubishi or Toshiba is not necessarily good for Japan. What's good for Lever Brothers is not necessarily good for the United Kingdom. What's good for SFK is not necessarily good for Sweden. What's good for Massey-Ferguson is not necessarily good for Canada. In fact, the new developments these changes bring about may show that General Motors does not know what is really good for General Motors, et cetera, much less for the United States of America, et cetera.)

2. In the past 25 years, U.S.-based multinational firms established an estimated 8,000 foreign subsidiaries, mostly in manufacturing. The annual foreign output of these multinational firms ranges between $120 billion and $200 billion, a total greater than the total output of any nation on the globe, with the exception of the United States, the Soviet Union, and possibly now, Japan.

Let me cite output and sales statistics of three of the largest multinational firms with whom my union has collective bargaining relationships: In 1969 annual sales of the foreign subsidiaries of the General Electric Co. were about $1 billion. General Motors, which makes electrical appliances and equipment, as well as cars and trucks, reported 1969 sales of its foreign subsidiaries as $3.4 billion. The 1.4 million of its cars and trucks—out of 7,160,000 sold in 1969—were manufactured in its overseas plants. In 1968, 40 percent of corporate sales, about $1.5 billion, of the ITT Corp. were made by its foreign subsidiaries, other than those in Canada.

Other U.S.-based corporations share this kind of output and sales. In 1969, IBM had $2.5 billion in sales outside the United States, for example.

(The U.S. Government has no access to meaningful data on these firms. The public has less. The latest published survey of sales of foreign affiliates of U.S. firms is based on 1964 figures. A new report, according to the U.S. Department of Commerce, will not be available until 1971 or 1972. The data will be from a 1966 survey.)

These are only a few of the several hundred well-known U.S. names involved in the new world of global conglomerates, multinationals and conglomerate-multinationals.

3. The figures, dramatic, startling as they may be, therefore, do not fully explain what is actually occurring now. There seems to be a kind of speedup on the part of multinational firms to transfer plants, production, products, and technology—and jobs—outside the borders of the United States. Entire industries, growth industries, in fact, badly needed here, and many thousands of urgently needed jobs, are exported. To many of us in the labor movement it portends a mass exodus.

For, despite the reluctance of firms to disclose facts, the trend is marked and it is accelerating. Fortune, in its April 1970 issue, reports that U.S. food processing companies that have moved into Mexico are exporting frozen strawberries into the United States, 88 million pounds of them, worth close to $15 million last year. Afraid of protectionist sentiments in the United States, the companies will not "admit to freezing a single strawberry south of the border." A major reason for their reticence is that "imports of Mexican frozen strawberries have seriously depressed the Louisiana strawberry industry," and "nearly half the acreage planted to strawberries * * * has had to be shifted to other uses."

In my own industry, and in industries closely related, we have seen plant after plant shut down in recent years, their production discontinued, products, technology and jobs exported to offshore manufacturing facilities of the same multinational firms.

Zenith, Admiral, Ford-Philco, RCA and others, for example, have recently shifted monochrome and color TV set production to Taiwan. Last year, Westinghouse closed its Edison, N.J. TV plant and transferred production to one of its Canadian facilities as well as to Japanese firms. It imports sets now for distribution under its own label.

Emerson Radio and Phono Division of National Union Electric also discontinued production of TV sets, closing down its Jersey City, N.J. plant, and transferring production to Admiral, which, in turn, transferred production of major TV product lines to Taiwan. Warwick Electronics transferred production from its Arkansas and Illinois plants to its Mexican facility. The rush to relocate outside the United States is on. At this time, practically all radio sets, tape recorders, and cassettes sold in this country are produced abroad, and before long the same may be true of black and white and color TV sets. Currently, about half the black and white sets and about 20–25 percent of the color sets sold here are produced abroad. Some growth products, such as home video tape recorders, will not even be produced in this country because patents held by Ampex Corp. have been licensed to Japanese firms.

About a year ago, General Instrument Corp. transferred TV tuner and other component production to its Taiwan and Portuguese plants, shutting down two New England plants and most of a third. Between 3,000 and 4,000 workers were permanently laid off. General Instrument increased its employment in Taiwan from 7,200 to over 12,000. General Instrument is that nation's largest employer, with more workers employed there than in all its U.S. operations combined.

A few months ago, Motorola shut down its picture plant, selling its machinery and equipment to a General Telephone and Electronics subsidiary in Hong Kong. A second picture tube firm commenced operations in Mexico, taking advantage of item 807 of the Tariff Schedules. Friden, a division of Singer Corp., and Burroughs, both discontinued production of electronic desk calculators. Their desk calculators are now made for them in Japan by Hitachi and other Japanese firms. The calculators are sold in the United States by their former manufacturers under the latter's label. So, here we have another growth industry that U.S. based multinational firms have abandoned as producers—becoming importers of the products they once made.

The household sewing machine is but one more item in the growing list of product casualties, though as a casualty, it can probably claim seniority over others. Of each three machines sold in the United States under Singer's label, two are made in its foreign based plants.

Still another product line to be added to the casualty list is typewriters, portables and larger models. A decade ago, Sperry Rand closed out typewriter production in its Ilion, N.Y., plant, shifting production to its European plants. Now, the company's Remington typewriters are made in Japan under the Remington label by the Brothers firm. Just recently, Litton Industries shut down Royal typewriter plants, transferring production to a Japanese firm. After acquiring Royal McBee, Litton acquired Imperial Typewriters, Ltd., in Great Britain, and, later Triumph and Adlerwerke in Germany, acquisitions the Justice Department's Antitrust Division felt merited its attention.

These examples are proliferating and unnoticed. Names that have fixed meaning among economists and the public press alike—Sears, Roebuck, Union Carbide, for example—should have new meaning as multinationals are better understood. Sears, Roebuck reportedly manufactures shoes in Spain, and Union Carbide processes shrimp in India—for sale in the U.S. market—according to a recent Fortune magazine story. Food processing names like H. J. Heinz and General Foods are worldwide. Genesco, Interco, and other well-known shoe industry names are not only multinational, but conglomerates. Glass manufacturing companies like Libby-Owens-Ford. Owens Corning, Pittsburgh Plate, for example, have foreign affiliates. And well-known names in the paper industry, like Kimberly Clark, have worldwide units.

Du Pont and Monsanto—chemical firms in the public eye—are makers of synthetic fibers and yarns, nylon and chemstrand. Machinery names like Cutler-Hammer, U.S. toy names like Mattel, turn out to be global conglomerate multinationals, too.

4. Several hundred U.S. firms, it is estimated, have set up plants in Mexico, below the border under the program advertised as a "Twin Plant" concept. Under this concept, plants on the Mexican side of the border assemble parts and components shipped to them by their U.S. parent, and then return them for final processing to a twin plant somewhere in the United States. Duty is paid only on value added.

In actual practice, work and jobs are transferred from the United States to Mexico in order to take advantage of the cheap labor available at 30–40 cents an hour. In transferring production of TV lines from Warwick Electronic's Illinois and Arkansas plants, approximately 2,000 U.S. jobs have disappeared. Advance Ross Electronics transferred 250 jobs to Juarez, Mexico, from El Paso, then set up a U.S. facility with about 15 employees. Transitron has 1,500 workers in its Laredo, Mexico, plant and only management personnel in Laredo, Tex.

Let me quote from an advertisement that appeared in the Wall Street Journal on January 26, 1970: "Mr. President: Don't be embarrassed at your next board meeting," it reads, "when the question-asker on the board asks:

"What's going on in Tucson, Ariz., that caused Motorola, Control Data, Kimberly-Clark, Lear Jet Stero, and Philco-Ford to establish plants there?"

The straight-to-the-point answer is: "Twin plant in Nogales, Mexico, only 1 hour away * * * 30 cents per hour labor * * * more profitable than Japan, Hong Kong, or Taiwan."

The executive director of DATE (Development Authority for Tucson's Expansion), which inserted this ad, is quoted in a letter from former columnist, Inez Robb, published on February 18, 1969, in the Arizona Daily Star, as publicly stating (though in connection with the apparel industry):

> We are not referring to the labor supply in Tucson or the wage rate here. That mailing was directed to some 700 apparel companies that we have reason to believe may be looking for a location outside the United States.

The impact spreads across both Mexico and the United States. More than 1,000 U.S. firms are in Mexico proper—and no one knows whether the twin plant is really part of a set of quintuplets or a population explosion of multinational subsidiaries.

More recently, evidence that the twin plant concept is already worldwide shows in reports about Korea, Taiwan, and more recently Haiti (whose labor rates are advertised as below those in the Far East). Barbados and other Caribbean countries are increasingly involved with firms using those new labor-export concepts ranging from multinationals to tiny plants, but an increasing number turn out to be interrelated with multinationals. Thus, a small plant in Alabama is a "twin plant" with Japanese production and a small plant in Texas turns out to be a subsidiary of a global conglomerate which is merely adjusting its costs worldwide. "Imports from Brazil now include office machinery parts"—again under the so-called "twin plant" arrangement.

5. The electrical-electronics industries have spawned and nourished a very considerable number of our multinational giants and conglomerates. The growth of the industry, particularly its electronics segment, has been spurred by heavy Government support. More than half of this year's $25 billion in sales of electronics instruments, devices and equipment is to the Federal Government's Defense Department, NASA and FAA. Government contracts have likewise sustained the computer industry. This year's total awards to this industry have been reported as over $2 billion.

The Federal Government has been a substantial and generous customer down through the years. Additionally, it has contributed very significantly to the industries' technological growth through initiation and support of the industries' research and development programs. More than two-thirds of the $22–$23 billion R. & D. outlays in electronics and communications equipment between 1957 and 1965 were Federal funds—that is, taxpayers' money. Annual R. & D. outlays have since increased but the Federal Government's portion has not declined.

The technological lead of American electronic firms was made possible only through Government support. As the OECD Directorate for Scientific Affairs points out, "Semiconductors, numerical control, electronic computers, * * * as well as a host of other less significant innovations owe their development to Federal support." A great many of these basic, Government-subsidized, privately patented inventions have been licensed to foreign, especially Japanese, competitors. The latter pay royalties to the U.S. multinational firms holding these patents.

General Electric, for example, has licensed Japanese companies to produce parallel phase detector circuit for TV receiving sets; optical gunsights; transistors and semiconductor elements; lamps, including mercury and infrared lamps; television receiver converter circuitry, color photographic camera systems; steam turbine electric generators, et cetera.

RCA has licensed Japanese firms in the following components, products, and processes, among others: magnetic memory cores; electron microscopes; electrostatic cameras; color picture tubes; photoconductors and photoconductive elements; loudspeaker devices; monolithic integrated circuits; et cetera.

Other multinational U.S.-based corporations that have licensed Japanese firms include: Westinghouse, IBM, Sperry-Rand, CBS, Bendix, Zenith Radio, Fairchild Camera and Instrument, Allis Chalmers, Singer Co., Texas Instrument, et cetera. Licensing agreements cover color picture tubes, video tape recorders, computer data processing devices, navigational instruments, planer semiconductors including integrated circuitry, microelectronic equipment, et cetera, et cetera.

Similar licensing agreements exist in almost every major industry—machinery, chemicals, steel, rubber, et cetera, as well as in soft goods industries as apparel, shoes, or even hats. Stetson hats have been licensed or franchised for foreign production for years.

An advertisement in the Wall Street Journal on July 15, 1970, seeks the U.S. patent holder with a U.S. market for a license to produce the patented product in Mexico.

The same U.S.-owned firms, however, now argue they must transfer production—and jobs—from U.S. plants to offshore plants in Taiwan, Korea, Hong Kong, Singapore, Mexico, Europe, and elsewhere if they are to be able to meet Japanese and other non-U.S. competition. In all these offshore countries, it should be noted, wage costs are far below the wage levels in Japan—indeed, anywhere from less than 20 percent to 40 percent of Japanese wages.

This kind of interchange is often analyzed as if only factors of free exchange between two countries were involved. It is important to remember that the need for a license is the opposite of free economic exchange—a patent is by definition a monopoly on the product or process. It is also a fact that a company may be required to produce a product in a foreign country—most developing countries—in order to sell there, while imports into the country are regulated.

6. In addition to cheap labor, there are other benefits that accrue to the multinational firms when it shuts down domestic operations and relocates abroad. To illustrate some of these benefits, let me quote from an article in Business Week—July 11, 1970:

> Besides its labor pool, Taiwan offers foreign companies other bait: a five-year holiday from income tax and low taxes thereafter; unlimited remittance of earnings; 100 percent foreign ownership; and duty-free import of most material and machinery. The government offers other concessions such as low-interest loans for up to 70 percent of the value of a plant, and free transportation of goods to and from cargo ships.

A similar, rather typical report, appeared in the Journal of Commerce recently about Singapore:

> Formal exemption from Singapore income tax, to a new group of U.S. companies. Recipients of these pioneer certificates were Esso, General Electric, Union Carbide, Gulf Oil, Electronic Memories and Magnetic, Litton Industries and California Pellet Mills.

Low rents, favorable interest rates, tax loopholes, immunity from various regulations, and other concessions not available in the United

States are today's "comparative advantages." U.S. tax loopholes encourage U.S. firms to export production by deferring tax payments on income earned overseas.

Multinational corporations can use tax havens like this worldwide. A recent study, in a magazine called Management Science said:

In which liquid assets are sent to subsidiaries when needed, by manipulating transfer prices, managerial fees and royalties, dividends and intersubsidiary loans so as to minimize taxes paid to the world minus interest received.

Concessions to relocate are nothing new—in our industry—and in other industries as well. Free or low rent, local tax concessions and cheaper labor costs have been used to attract industry from industrial to rural regions of the United States. Such concessions, however, do not compare in scope or in scale to the many new "comparative advantages" available to the multinational firm.

"Concessions" in developed countries of the Common Market and Canada—tax arrangements, subsidies for exports, et cetera, also exist. A November–December Harvard Business Review explained that—

In 1960 Belgium sought investments in modern technological industries. Both national and local sources offered very attractive tax incentives and funding relationships to develop the proper industries and companies. Domestic capitalists and companies were preoccupied with their problems and did not respond, while multinational companies did.

Nor do they compare in economic analysis or impact because the U.S. economy started as one nation with a free flow of goods and services and labor moving freely among the several States. A U.S. minimum wage floor could be established and enforced, because there was no wall in one direction or a foreign government or a foreign culture.

7. Capital has an enviable and increasing mobility. Its mobility is worldwide in scope. Factory workers have very little mobility. Equipment process know-how, engineering and managerial skills, can all the be readily shifted to offshore low-wage areas. Workers, on the other hand, must usually remain in their communities.

Multinational firms are constantly adding to and improving their mobility, transferring operations, technology and resources in accordance with corporate profit objectives. Workers may improve their productivity and skills, but they cannot overcome their basic "disadvantage"—their high wages and benefits, compared with those prevailing in other parts of the world.

A recent survey of 167 IUE shops showed 55 had a minimum plant wage of less than $2 an hour. Two dollars an hour is just over $4,000 a year. The administration, in its welfare legislation, puts the poverty line at $3,920 for a family of four persons a year.

But even if we were to reduce wages to $1.60 an hour, the legal minimum, American workers cannot compete with wages of 10 to 30 cents an hour paid to Far Eastern and Mexican workers. Nor could American workers become competitive by increasing their man-hour productivity. In my industry, annual increases in man-hour productivity during the sixties approximated 4 percent. Wage and fringe benefit gains from 1960 to 1969 averaged 2.8 percent a year at General Electric and 2.6 percent a year at Westinghouse.

8. The American trade balance has declined from a high $5 billion annual surplus, and, omitting Government-financed exports, has shown

a deficit in recent years. The rate of rise of U.S. imports has outstripped the increase in U.S. exports since 1962 by ratio of about 1½ to 1. The increase in imports of consumer goods has been particularly large. Imports of consumer electronic products, for example, tripled between 1966 and 1969, almost reaching the billion dollar level. Roughly similar high import increases were reported in a number of other consumer industries.

The electric-electronics industry as a whole, depending on how it is measured, remains a trade surplus industry, but, while the ratio of exports to imports was 3.8 to 1 in 1960, it declined to 1.4 to 1 in 1969. If we were to eliminate Government-financed exports, the current ratio would show an even steeper drop.

Employment, of course, has been affected. In the electronics segment, we estimate a drop in employment since 1966 of over 60,000 jobs for workers. What is perhaps of equal importance is that the labor force will increase substantially during the next 5 years.

9. In today's world of multinational corporations in a world, that is, in which technology, products, production techniques, and jobs are readily exportable, and in which licensing agreements and joint ventures are common, traditional theories of international trade are no longer applicable.

One reason for this was explained in a recent article in the March 1970 Journal of Economic History on "Nonmarket Trade," where it is pointed out that much of the trade of the world is now intracorporate or "nonmarket trade." The author says:

> I have in mind, first of all, the modern multinational corporation with its trade between parent and subsidiary (and among subsidiaries) in different countries. The prices at which goods such as parts, components, and finished products change hands are governed chiefly by taxation and accounting advantages obtainable in the various countries where the corporation is located. Prices are set accordingly and bear no necessary relation to the market prices for these goods (if indeed market prices exist for them at all). There is no doubt that these transactions are generally regarded as trade, for they are universally included in the foreign trade and balance-of-payments statistics of the respective countries. Subsidiaries, moreover, are formally incorporated in the countries in which they are located.
>
> A second example is the trade between the state-trading corporations of Communist countries. A variety of factors govern the prices at which goods are traded here, including the political relations and national security objectives of members of the Communist bloc. Such prices bear no necessary relation to world market prices for these same goods.
>
> These two instances differ as much from each other as they differ respectively from conventional market trade. What these examples do share in common can be described negatively: the partners to these trade transactions are not trading at arm's length, and the prices are not formed in the market. Unless we are prepared to exclude such transactions from our concept of trade (thus excluding a rapidly growing portion of world commerce), we must accept in the present period the existence side by side of market and nonmarket trade in the international economy. (Those who deny that the above examples constitute trade must of necessity provide some alternative designation for goods which are formally bought and sold and shipped across international borders by corporations which are legally discrete entities.)

There is an urgent need to develop world trade on a rational basis, designed to benefit the world's people. The growth must be orderly, equitable, and must contribute to real growth in living standards. In our pursuit of this objective, we cannot permit living standards already achieved—as in this country—to be threatened or undermined.

Nor can we permit our growth industries and the employment they generate to be exported at a time of substantial increases in the labor force, and at a time when we are trying desperately to find jobs for the unemployed and underemployed poor.

Thank you, Mr. Chairman.

Representative WIDNALL. Thank you, Mr. Jennings.

The next witness will be Mr. Heribert Maier, director, Economic, Social and Political Department, International Confederation of Free Trade Unions.

Proceed, Mr. Maier.

STATEMENT OF HERIBERT MAIER, DIRECTOR, ECONOMIC, SOCIAL AND POLITICAL DEPARTMENT, INTERNATIONAL CONFEDERATION OF FREE TRADE UNIONS

Mr. MAIER. Thank you, Mr. Chairman.

Mr. Chairman, members of the committee, my name is Heribert Maier and I am the head of the Economic, Social and Political Department of the International Confederation of Free Trade Unions, grouping more than 50 million workers organized in free trade unions throughout the free world, with its headquarters in Brussels, Belgium.

Allow me to say, first of all, how much I appreciate your invitation to testify here today. I take this not so much as a personal honor but more as a recognition of the interest and involvement of the international free trade union movement in present-day problems of world trade and direct investments.

I do not intend to waste any of your valuable time talking about the size and scope of multinational companies. What I would like to bring to your attention, in the first place, are certain aspects of the relations between the governments and multinational companies—in particular those aspects which can have serious repercussions on the world of labor. I would also like to say something about relations between these companies and the trade unions, for these relations are likely to have a significant impact on industrial democracy and the promotion of democratic societies in general to which the free trade unions are firmly dedicated.

And finally, I would like to make some tentative suggestions about the kind of controls which could be in the interest both of governments and of labor to impose upon the hitherto almost untrammelled freedom of the multinational companies to operate in the fields of international trade and investment.

The increasing interdependence of national economies is the outstanding feature of recent economic trends. It is evident, however, that one byproduct of that interdependence is the possible emergency of economic and monetary instability at national levels. In the absence of any effective international control of the activities of worldwide economic power centers, national governments are bound to be seriously hampered in their efforts to cope with potential factors of instability.

The ability of multinational companies to take their profits where it best suits them, the so-called practice of profit smoothening, or transfer pricing, and to switch large sums of internal funds from country to country, such as uncontrolled long-term direct investments, for instance, or simply to delay or speed up the transmission of funds by "leads and lags," can have serious repercussions on a country's balance of payments and effectively limit a government's power to deal with an adverse balance.

International trade continues to expand at a rate on average twice that of overall economic growth, but an increasing proportion of the international exchange of goods is accounted for by multinational companies. International trading relations are changing in nature: foreign trade is becoming more and more a matter of transfers between the parent company and/or subsidiaries of vast multinational corporations. "Foreign trade," in fact, has become almost a misnomer; for the United States and the United Kingdom at least—the two countries where the growth of these companies has reached its apogee—this is neither foreign, nor from the point of view of mutual benefit between two given countries can it really be described as trade. Just to quote another example: The Netherlands being the mother country of the worldwide concern "Philips" has taken in 1967 the fifth position as world exporter of electrical goods. At the same time the Netherlands figured on place three as world importer of electrical goods.

There is no doubt that some of the financial and trading practices of multinational companies can raise serious problems for the successful implementation of government policies on domestic industrial development, taxation, investment, active manpower and other economic adjustment action. It is hardly necessary to add that these are all areas of government action in which the trade unions have a vital interest, since the welfare of their members and the workers and their families in general is inevitably at stake. Active manpower policies, for example, include the whole complex of measures which governments should take to offset market dislocation. Such measures are essential not only for the maintenance of high levels of employment but are also a basic prerequisite for a valid alternative to protectionist policies which everyone agrees help nobody in the long run. Another area of mutual concern to governments and trade unions is the problem of understanding the financial accounts of international companies. The free trade union movement is clearly interested with regard to labor costs and profits, while governments are interested not only in these matters but also in such questions as tax liability.

Apart from their own relations with the multinational companies which I will come to shortly, the trade unions are, therefore, bound to view with considerable concern the growing encroachment of these companies upon the sovereignty of the nation state. While in different countries the unions may attach varying emphasis to particular aspects of that concern—economic, cultural, psychological, political—they all share one common and firmly held belief. That is, that multinational companies are able to take unilateral decisions affecting the earnings and job security of workers in the countries where they operate—decisions; that is, in which neither the government nor the trade unions can take part and which may be motivated by considerations quite extraneous to the interest of the country concerned.

Lest there be any misunderstanding, I would like to insist at this point that the unions are by no means unaware of the positive aspects of the activities of multinational companies in respect of levels of employment and incomes. In particular, they welcome the potential benefit, flowing from the application of new technologies, the introduction of new growth factors, help in developing and expanding internal and export markets and in the speedier industrialization of developing countries.

In addition, these companies could form an important factor in favor of general liberalization policies to which the international labor movement is firmly committed, provided they are prepared to accept their full responsibilities toward the workers they employ and the societies in general in the framework of which they operate.

The trade unions have, nonetheless, one specific cause for anxiety arising out of the nature of relationships between multinational companies and governments. This is that, particularly in developing countries, the former may sometimes actively encourage the latter to favor antitrade union measures, permitting or even assisting companies to refuse to recognize trade unions, and to enter into bona fide collective bargaining. The international free trade union movement believes that the governments of capital-exporting countries have a strong moral obligation to insure that overseas investment does not promote unfair labor conditions. It is, of course, not only a moral obligation, but also in the very practical material interests of those governments, that such investment should not backfire on their own economies in the shape of market disruption.

In this connection a practice recently introduced by the Swedish Government may be of some interest. In that country export guarantees to cover losses due to political risks in connection with investments in certain developing countries carry certain so-called social conditions. These lay down that the investing company should offer satisfactory conditions of work and employment including recognition for trade union activities within the firm.

This brings me to the general question of relations between multinational companies and trade unions. Here experience has shown that certain specific characteristics of these companies can have a direct bearing on the performance of the unions. Organizations which have established themselves as recognized partners in the industrial relations systems of democratic countries only after long years of struggle are now finding their position in such systems jeopardized by the behavior of some of these companies.

By conceiving profitability on a worldwide rather than a national basis and by centralizing decisionmaking at their international headquarters they tend to exploit established industrial relation systems at national levels. The following are some of the grounds on which difficulties have arisen in dealing with multinational companies: preconceived antitrade union policies; foreign managers unaware of or ignoring established industrial relations procedures; difficulties in identifying the real center of decisionmaking; threats dangled during negotiations to shift production to other countries; difficulties in finding out the profit situation of the company because of the practice of "profit smoothening" or because of transfers of profits to low-tax countries.

The typical trade union reaction to these problems has been to organize bargaining power at whatever level is appropriate to the given situation and to seek to enter into coordinated bargaining at that level. The establishment of worldwide councils representing the workers of multinational companies in all the countries where they operate has been pioneered by certain international trade secretariats, which are international free trade union organizations associated with my organization grouping national professional unions. Efforts are being made to harmonize the expiry dates of contracts in a number of countries. Action has been undertaken in solidarity with workers in dispute in other countries, with special attention being given to the developing countries where the unions are weak and to the dictatorship countries where free trade unions are not able to operate.

We have obviously still a long way to go before we can expect any generalized extension of the few isolated examples of international collective agreements embracing both the United States and Canada. Nevertheless, negotiable areas for coordinated collective agreements in certain industries are being identified. Conditions of work—that is to say working hours, holidays, welfare arrangements, and housing facilities, for example—will no doubt be given higher priority than wages by the unions concerned in the immediate future. This does not mean, however, that the unions are not uneasy about the possibility of radically deficient wage structures becoming a factor of massive importance in a highly competitive world market. The exploitation of international labor cost differentials in order to boost profits is strongly opposed by the trade unions; this indeed is at the very core of their policy of fair labor standards in international trade. For developing countries with low-wage levels, the unions lay special emphasis on welfare expenditure jointly determined by the governments, trade unions, and multinational companies. They strongly support proposals such as that presented to the sixth session of the United Nations Committee for Development Planning—the so-called Tinbergen Committee—for the introduction of special tax contributions payable by such companies operating in developing countries.

The international free trade union movement has not been slow in reacting to the challenge posed by the growth of multinational companies and the far-reaching structural changes they are causing in the world economy. In 1968 the ICFTU submitted a resolution to the International Labor Conference in Geneva calling on the International Labor Organization to undertake a study of the problem with a view to encouraging the development of international industrial relations. Owing to the objection of the employers, this resolution, however, was not carried.

Last year the Ninth World Congress of the ICFTU adopted a comprehensive resolution on the subject. The text of this will be found in my prepared statement.

What we believe, Mr. Chairman, is required, so far as governmental action is concerned, is an international instrument outlining obligations of multinational companies toward governments and trade unions and which establishes "rules of the game" for international movements of long term capital. The instrument should include clauses making it compulsory for the companies to abide by ILO principles and, in particular, international conventions guaranteeing freedom of association and the right of workers to organize and engage in collective bargaining. It should furthermore call for compliance with all other ILO conventitons, whether or not they have been ratified by the governments of the countries in which the company may be operating. In this connection it is interesting to note a demand put forward by the International Metalworkers' Federation—a trade secretariat associated with the ICFTU and grouping 11 million workers in some 60 countries. This organization has proposed that any international regulations on multinational compaies should provide for the prohibition of investment in countries whose national laws—as in the case of the Republic of South Africa—impose racial discrimination in wages and employment.

The problems calling for international control in this connection are evidently multiple and overlapping. They involve economic and social questions, trade union freedom and basic human rights, as well as problems of international trade, investment and monetary affairs. It is, therefore, clear that no single intergovernmental agency could possibly be competent to deal with the elaboration and application of the kind of international instrument required to regulate the operations of multinational companies. The initiative might well be taken by the ILO but it would be natural and important for other agencies like GATT, the World Bank, the International Monetary Fund and the U.N. Trade and Development Conference as well as the OECD to join in a common effort to establish an international instrument. May I repeat here the proposal, just to mentiton one, of economist Charles Kindleberger, who testified here yesterday, I believe, that the United States call for a conference on the international corporation under the auspices of the United Nations.

What is basically required is an international code of behavior to govern multinational company operations. It should be applicable to both industrialized and developing countries. A useful model could be the international convention on the settlement of investment disputes which came into force in 1966. Under this convention there has been set up an international center as an autonomous institution. Similar arrangements could be envisaged for the application of an international convention on multinational companies, which could also be administered by an autonomous international center or agency. Provision should be made, too, for the consideration of complaints about infringements of the convention before a tripartite body representative of the governments, multinational companies and trade unions involved.

If you will allow me, Mr. Chairman, I would like to summarize the main conclusions to be drawn from the considerations I have placed before you. Very briefly, these are the following:

1. Democratic governments and free trade unions have a common interest in seeking to devise certain rules to govern the operations of multinational companies;

2. Action which could appropriately be taken by individual governments might include: (a) Measures for rendering the accounts of multinational companies more accessible and tax evasion more difficult; (b) steps to protect national development planning and to promote generous and effective active labor market policies; (c) governments should impose on multinational corporations the obligation to respect the principles of trade unions right and free collective bargaining in accordance with democratic procedures as outlined in interna-

tional labor conventions No. 87 concerning freedom of association and the right to organize, and No. 98 concerning the right to organize and collective bargaining; (d) the exercise of restraint by governments in not vying excessively with each other in offering investment inducements in the form of tax reliefs, public financing, antilabor policies or other concessions; (e) fair labor conditions to be incorporated in guarantees given to protect direct private investments—in particular the obligation to recognize trade union activities;

3. Nevertheless, there are wide areas of multinational company operations which are inevitably beyond the power of any one national government to control. There is, therefore, an urgent need for coordinated international action for regulating the activities of these companies;

4. Such international action could best be undertaken on the basis of a common initiative of some U.N. specialized agencies and intergovernmental bodies concerned;

5. The resulting international convention or instrument establishing a code of conduct for multinational companies could best be administered by an autonomous international agency or center modeled on the International Center for the Settlement of Investment Disputes.

The international free trade union movement is firmly convinced that the time has come to introduce the rule of law into the operations of multinational companies. This, we believe, should be the common gorund between democratic governments and free labor.

Thank you very much, Mr. Chairman.

Representative WIDNALL. Thank you, Mr. Maier.

(The prepared statement of Mr. Maier follows:)

PREPARED STATEMENT OF HERIBERT MAIER

THE INTERNATIONAL FREE TRADE UNION MOVEMENT AND INTERNATIONAL CORPORATIONS

I. INTRODUCTION

The increasing internationalisation of investment in manufacturing industry and the services sector is a striking phenomenon of economic development during the last two decades. It is true that, starting in the 19th cenutry, European and American capital played a predominent role in the development of the extractive industries—minerals and petroleum—and in basic agricultural production in the developing countries. The new wave of international investment, however, is very different in nature and in effect. The manufacturing and service sectors now affected are the fast-growth, advanced-technology industries.

The basic means of penetration used are the mastery of advanced technology and management techniques, marketing techniques, a world communication network and channels of trade. Production itself is becoming more and more technologically integrated on a world scale.

The Massey Ferguson Company for example, described its activities as follows in an advertisement in the Financial Times of 30 April 1970:

> We employ 45,000 people.
>
> We operate 42 plants in 14 countries.
>
> Our products are sold in 182 out of 218 countries of the world.
>
> We have achieved global financial flexibility and our manufacturing is highly rationalised and integrated.
>
> A French-made transmission, a British-made engine and a Mexican-made axle can be assembled with sheet metal in the United States, and the complete tractor put to work in the Caribbean."

Similar descriptions could be produced for a growing number of American and European companies. But their multinational character is not reflected in their ownership and management. There is no example of an industrial corporation or service, the control of which is shared by citizens of more than two countries. There are very few examples even of nationals of two countries exexercising control and formulating group policies: this is true of Unilever, Royal Dutch-Shell and Agfa-Gevaert, but very few companies that matter could be added.

The economic importance of this development has been sufficiently described elsewhere. Here we would like to insist only on the following points:

The increasing interdependence of national economies is the outstanding feature of recent economic trends. It is evident, however, that one by-product of that interdependence is a possible emergence of economic and monetary instability at national levels. In the absence of any effective international control of the activities of world-wide economic power centres, national government are bound to be seriously hampered in their efforts to cope with potential factors of instability.

The ability of multinational companies to take their profits where it best suits them and to switch large sums of internal funds from country to country, or simply to delay or speed up the transmission of funds by leads and lags, can have serious repercussions on a country's balance of payments and effectively limit a government's power to deal with an adverse balance.

International trade continues to expand at a rate on average twice that of overall economic growth, but an increasing proportion of the international exchange of goods is accounted for by multinational companies.

International trading relations are changing in nature: foreign trade is becoming more and more a matter of transfers between the parent company and/or overseas subsidiaries of vast multinational corporations. "Foreign trade", in fact, has become almost a misnomer; for the United States and the United Kingdom at least—the two countries where the growth of these companies has reached its apogee—this is neither foreign, nor from the point of view of mutual benefit between two given countries can it really be described as trade.

To take an example from Great Britain, according to a Board of Trade survey three-quarters of 1966 exports were accounted for by British companies or subsidiaries of foreign companies with international affiliation, while 22% of the total was made up of sales to subsidiaries abroad. A survey by the Department of Commerce in the United States similarly showed that, in 1965, 320 U.S. companies accounting for one-third of American exports made 52% of their sales abroad to their own subsidiaries. It was estimated that inter-company transactions of U.S. firms accounted for one fifth of the total volume of American exports in 1965; the present growth rate should have brought this proportion up to about one quarter in 1970.

According to a recent estimate of Professor John Dunning (Great Britain) direct investment now accounts for 75 per cent of the private capital outflows of the leading industrialised nations. The output of international companies outside their own countries is currently expanding at 10 per cent a year according to Professor Dunning. This is twice the growth rate of world gross national product, and is increasing 40 per cent faster than world exports.

II. WHAT IS THE GENERAL ATTITUDE OF THE INTERNATIONAL FREE TRADE UNION MOVEMENT TOWARDS THIS DEVELOPMENT?

Many aspects of multinational corporation activities present the trade unions with a new challenge which may well play a decisive role in the transformation of trade union strategies, activities and structures in the next ten years. This does not mean, however, that there is any serious trade union opposition to the development of multinational corporations as such. On the contrary, most trade union organisations are favourably disposed to the mobility of products, techniques and know-how to the extent necessary to secure the full utilisation of human and material resources. This position is so basic to the international free trade union movement that it is inscribed in the founding charter of the International Confederation of Free Trade Unions. The ninth ICFTU congress adopted last year a resolution on multinational corporations and conglomerates, the text of which follows:

"Industrial concentration, particularly in its form of multinational corporations and conglomerates, is a feature of our times causing far-reaching structural change in the world economy. It is a consequence of the development of worldwide markets and the use of new technologies and management techniques. The international organisation of production can play an important role in spreading new technical know-how and in giving an impetus to economic growth and social progress, provided that trade union action in all its aspects is brought to bear upon multinational corporations so as to safeguard the interests of the workers and the public as a whole.

Multinational corporations are global enterprises of massive economic and financial strength, which, by operating on a world-wide scale, escape any form of democratic control. Multinational corporations pose a new challenge to the international free trade union movement, by:

Jeopardising democratic national development planning, aimed at full utilisation of the social and economic potentialities of the countries concerned;

Arbitrarily transferring production facilities and research centres from one country to another without regard to balanced global and regional development;

Evading taxes by means of internal transfers at artificial prices between subsidiaries of the same group and restrictions imposed in certain countries on production and export opportunities which affect the balance of payments;

Inducing competition between the host countries by means of tax reliefs, public financing and other concessions.

Within the general trend of concentration a further challenge is posed by conglomerates based on stock market speculation, which constitute a threat to the jobs and working conditions of employees in plants taken over.

Multinational corporations place workers in different parts of the world and various industrial sectors under the same employer, and by concentrating vital economic and financial decisions at their international headquarters and establishing world-wide employment and industrial relations policies may:

Undermine established industrial relations systems;

Restrict the right of the workers to organise in defence of their interests, a right which has often been denied them as part of a systematic anti-trade union policy;

Limit their right to enter into coordinated collective bargaining at whatever level is appropriate;

Exploit international labour cost differentials in order to boost profits.

The Ninth World Congress of the ICFTU, meeting in Brussels from 2 to 8 July 1969—

Affirms that only the determination and international solidarity of the workers and the coordination of trade union efforts will enable the international free trade union movement to take up the challenge and protect the interests of the workers whom it represents;

Demands the recognition of the rights of the workers everywhere to organise and bargain collectively on all matters affecting wages, hours, working conditions, employment and income security, and to strike;

Urges the multinational corporations:

To negotiate wages, working conditions and fringe benefits with the trade unions, in keeping with the high level of corporate profits and the need for social progress in the national economy;

To abide by all ILO Conventions wherever they operate, and comply with existing social legislation, collective agreements and established working conditions and rights;

Urges the need to ensure that the priorities of national, economic and social planning are respected, in particular that company mergers be subjected to the approval of public authorities and that all measures are taken in good time to avoid social hardships caused by structural change and plant closure;

Insists that any new laws or regulations governing the international, regional or national operations of multinational corporations must include the principles set forth in this statement which provide full scope for the requirements of maximum social progress in a balanced economy;

Emphasises the need for adequate measures to establish democratic control at each level of decision so as to advance the democratisation of multinational corporations and in particular avoid undermining, or preventing the extension of, established practices and procedures for achieving effective industrial democracy in various countries;

Urges the International Labour Organisation to act swiftly on the request of the ICFTU and the International Trade Secretariats to examine the social and economic problems engendered by the growing power of the multinational corporations and the problems arising in international industrial relations;

Takes note of activities already developed on a national, regional and world-wide scale by the international trade union movement and in particular the ITS and welcomes the successes achieved in coordinating collective bargaining policies;

Requests the ICFTU Executive Board, in cooperation with its affiliates, its regional organisations and the ITS, to work towards these objectives by instituting and pursuing an exchange of experience and information on the practices of multinational corporations with a view to promoting effective international free trade union action to meet this new challenge."

Since the adoption of this resolution there has been a wide exchange of experience and information on multinational company practices within the international free trade union movement.

III. AREAS OF CONFLICT

The chief problems which trade unions have to face arise from activities of organisation, trade union recognition and collective bargaining. The situations experienced over the years and throughout the world by ICFTU-affiliated organisations are extremely varied. However, some broad conclusions can be drawn.

The main problem is the anti-trade union policy practised on a world scale by some very large multinational corporations, such as IBM, Kodak, First National City Bank, United Fruit or Firestone, and by runaway-type companies such as Singer, Fairchild, Motorola, Texas Instruments and shipping companies which register their fleets under flags of convenience. It must be pointed out, at once, that companies practising such a policy on a world scale are fortunately relatively few. It cannot be concluded that systematic anti-trade union policies are peculiar to multinational corporations: they are practised just as much by exclusively national undertakings, when they are able to do so. Some problems of trade union recognition and organisation, as well as difficulties put in the way of trade union representatives, sometimes arise also from the inexperience of foreign management personnel sent out to the new subsidiaries and from their ignorance of the way in which the national labour relations system operates.

A second set of problems arises from the absence of inter-governmental cooperation for regulating and controlling multinational corporation activities.

The anti-trade union policy of companies on the basis of their technological advance

One group of multinational corporations which systematically refuse to recognise trade unions comprises firms of American origin which developed this policy first of all in the United States. Their chief characteristics are that they use advanced production techniques, they sell new products and employ a very high proportion of technicans and white-collar workers and are operating in fast-growing sectors. The exclusive position from which these companies temporarily benefit gives them the comfortable illusion that their management structure can cope with any economic and social issue with which they may be faced. They consider themselves as separate entities with a life of their own, devotion to the company being the first condition required. This policy is very clear-cut in the case of IBM. In most countries, particularly in the United States, it is only with the greatest difficulty that the trade unions have been able to get a foothold in the company. On identical bases, this type of policy is also characteristic of certain companies operating in the services sector, and finance.

The challenge to the principle of free bargaining, the challenge to the existing systems of national industrial relations and to the efficacy of present trade union structures is evident. There can be no illusions about future difficulties with these companies. The fact is that the trade union movement is up against a strong opponent. By using the best experts in the human sciences and the latest organisation techniques, psychology and sociology applied to the management of broad groups of people, these companies have often managed to develop an undoubtedly efficient internal human relations machine ensuring a very high level of control over the workers they employ. In the same way they are very careful about the image they present outside. As they carry out their operations in high-growth sectors and their operations are very profitable, the conditions they offer their personnel appear to compare favourably with those of the average national firm of a similar nature.

Apart from the need to adapt trade union strategies, activities and structures, two factors which have had a favourable effect in successful attempts to penetrate some IBM subsidiaries are worth mentioning: the existence of a national industrial relations system in which a strong national trade union centre is faced by employers organised in strong federations; and the influence which the trade unions are able to exercise on legislation, economic policy, investment policy and government contracting. It is true that this combination of favourable factors, which explains the success of ICFTU-affiliated organisations in Sweden, for example, is not to be found in all countries. The problem of IBM, the First National City Bank, Kodak and the like remains as a major challenge to the international free trade union movement.

Runaway firms and their anti-trade union practices

A second group of companies systematically produces problems for trade unions in the countries where they become established. It includes companies such as Singer and Texas Instruments, Firestone and United Fruit, and shipping companies registering their ships under flags of convenience. Whether their activities are carried out on plantations, in the assembly of electronic components or of consumer durables such as radio and television sets, in clothing manufacture, or shipping, their common characteristic is that labour costs account for a large proportion of the production costs of their products or services. They can all, moreover, exploit their labour force with relative impunity, either because they have at their disposal an inexhaustible reserve of labour, or because they can simply transfer their activities to other low-wage regions. In much the same way the companies whose ships sail under flags of convenience have tried ever since the end of the war to recruit a growing proportion of Asian seamen. Japan, Formosa, Korea, Hong Kong, Mexico, some of the Caribbean Islands, Ireland, Spain and Portugal have become privileged places for the transfer of activities characterised by a high intensity of unskilled or semi-skilled labour. Very often the trade unions are weak in these countries and what is more they have to fight on two fronts: in the first place against the company which considers all means fair for preventing improvements in conditions of work including wages, for which the trade union is public enemy number one, and which does not hesitate to transfer production elsewhere when social conditions start to improve. In the second place, the companies often find allies among the local employers and in certain administrative and governmental circles. This is obvious in the case of dictatorship governments. Less obvious, but even more pernicious in the long-run, is the pressure on the unions in their activities and the exercise of their rights—restrictive pressures stemming from a misguided policy for attracting foreign investments.

Fair labour standards

The dynamic concept of fair labour standards was developed (especially in the sixties) by the free trade union movement in the context of the growth of international trade and the economic and social development process. In the case of transferred activities, the first to benefit from any reciprocal economic advantage should of course be the workers engaged in those activities. If the overall level of their wages and related benefits is similar to, or even below, the average level of activities in the host country, in spite of the level of productivity which is obviously higher, no real benefit will accrue for the host economy, and it can even be considered that a part of its human resources are diverted solely to the profit of the foreign firm. Nor do the consumers in the importing countries derive any benefit, because the prices charged are naturally the current prices on those markets. Higher company returns should, therefore, be redistributed by means of social charges and in the form of benefits for the community at large (vocational training schemes, clinics, workers' housing etc.), if disproportionate increases in wages were likely to disrupt local wage structures. In this regard, the ICFTU firmly supports the recommendation made by the United Nations Commission for Development Planning for a social development contribution from foreign private firms in the developing countries, to be levied in the form of a special tax. The content of what can be considered fair keeps changing with economic progress. Nevertheless, for the purpose of international action, there exists in any given situation a clear criterion of what is fair and what is not: fair labour standards are the standards which a strong free trade union, having taken into account all relevant factors, would agree to accept. Solidarity action on the part of free trade unions in industralised countries should contribute to strengthen trade unions in developing countries. Indeed, wherever trade unions are strong enough to secure by their own means respect for fair labour conditions, the question of international action to this end does not arise.

International trade union action

Action of this sort can assume many forms. In particular it covers all the activities of the ICFTU and of the ITS relating to the fight for trade union freedom and respect for the relevant ILO conventions and recommendations. Among the complaints lodged at the ILO by the ICFTU, some concerned cases of national legislation modified in such a way as to infringe trade union freedom, as guaranteed by ILO conventions directly at the instigation of multinational corporations (Firestone in Liberia, 1960, for example). It includes, of course, the day-to-day action of representatives of the ICFTU and of the ITS seconded to developing countries to carry out work of organising and helping trade unions in those countries. It also includes all the representations, pressure and other steps, initiated directly by the ITS and the ICFTU or through national centres, with the international management of the companies and/or governments concerned. Finally, there are countless instances of international trade union solidarity: action ranging from the refusal by dockers to unload a ship sailing under a flag of convenience until the International Transport Workers' Federation has concluded with the shipowners a satisfactory agreement for the crew, to boycotts, fund-raising and work stoppages.

A special remark should be made about the attitude of the international free trade union movement towards restrictive action intended to protect a national economic area from the import of products which may rightly be suspected of having been produced under unfair labour conditions. The policy of the ICFTU is first of all to exhaust all possibilities of positive action, such as the promotion of powerful trade union organisations and freely negotiated collective agreements; government action to promote a balanced and orderly adjustment of industries affected by such imports, including measures to ensure that the workers affected are adequately retrained or new jobs provided for them. Active manpower policies, for example, include the whole complex of measures which governments should take to offset market dislocation. Such measures are essential not only for the maintenance of high levels of employment but are also a basic prerequisite for a valid alternative to protectionist policies which everyone agrees help nobody in the long run. Positive action of this kind, if taken in good time, can obviate the need for protectionist policies.

As regards the export of capital for direct investment, apart from the need for inter-governmental control to which we will refer again later, the international free trade union movement believes that the governments of capital-exporting countries have a strong moral obligation to ensure that overseas investment does not promote unfair labour conditions. It is, of course, not only a moral obligation but also in the very practical material interests of those governments that such investment should not backfire on their own economics in the shape of market disruption. In this connection a practice recently introduced by the Swedish government may be of some interest. In that country export guarantees to cover losses due to political risks in connection with investments in certain developing countries carry certain so-called social conditions. These lay down that the investing company should offer satisfactory conditions of work and employment including recognition for trade union activities within the firm.

Collective bargaining with multinational corporations

The trade unions which are established as recognised partners in the industrial relations systems of the democratic countries only after long years of struggle for recognition now see their position as a partner in the system called in question by the nature and behaviour of multinational corporations. This unfavorable development stems from a number of special factors which characterise the multinational corporations as compared with national companies. Some of these factors we have already examined: a systematic anti-trade union policy; attempts at outbidding by governments in investment-attraction policies, resulting in pressure being exerted on the trade unions even to the extent of restricting their rights; management personnel of foreign nationality in the subsidiaries who are unaware of, or ignore, the national system of industrial relations; the ease with which multinational firms transfer production and jobs from one country to another and use this possibility as a threat in the course of beginning; the difficulty of knowing the real profitability of multinational corporation subsidiaries, since they use a number of special practices in their accounting procedures, in the fixing of transfer prices for goods and services between subsidiaries in different countries, and various practices designed to transfer profits to low-tax countries and to protect profits and assets against exchange rate variations and the policies of the host countries. However, the problem which is central to the challenge presented by the multinational corporations to the trade unions is that of narrowing the field of collective bargaining and the loss of substance in industrial relations in the national context. The centralisation at international headquarters of investment decisions and of decisions concerning employment and working conditions is a characteristic of multinational corporations. This is the central point of potential conflict between the trade union movement and these companies. There are two ways of meeting this threat. The first is to try and regain industrial cohesion at national level by calling for guarantees of the sort often negotiated with the help of the host government with regard to steady employment and income security and the extension of research facilities, development projects, etc. Action to this end is often taken when a multinational corporation takes control of a national firm. The other possible measure is to reconstitute trade union bargaining power and its ability to take action on the firm's world policy by negotiating with its international management. These two approaches are complementary. There is a contradiction between the economic and technological drive of multinational corporations and the global strategy they resort to worldwide on the one hand, and, on the other hand, the policy of fading into the anonymity of the national environment, which they tend to practise in their industrial relations, working conditions, wages, etc. This despite their higher level of profitability and despite the many advantages they receive from the host governments.

The chief tasks in strengthening trade union bargaining power against the multinational corporations fall to the national unions and their corresponding international trade secretariats. What has been accomplished so far covers many complementary fields: exchanges of information on working conditions and wages in the different subsidiaries; analysis of the consolidated balance sheets of the firm at world level; efforts to harmonise the dates of termination of collective agreements concluded with the same firm in different countries; the standardisation of minimum conditions to be secured in all countries; measures to prevent transfer of production from certain subsidiaries to others designed to compensate for loss of production in other subsidiaries due to industrial actions in the latter or a refusal to work overtime for instance.

At a further stage, not yet reached, all these activities could be geared to collective bargaining at international level. In this respect some progress has been made in recent years. Agreements have already been negotiated in North America, covering American and Canadian workers of the same undertaking. The best known of these is the one signed in 1967 with Chrysler; there are also some of earlier date, such as that with Continental Can, which since 1953 has had an agreement covering all its 60 plants in North America. Other companies similarly covered are in the aerospace industry and in air transport. Mention may also be made of certain results obtained at national level with regard to wage increases based on the overall profitability of a group at world level, despite the fact that the national subsidiary showed no profit.

IV. INTERNATIONAL TRADE UNION AIMS

The international free trade union movement—that is to say the ICFTU, its affiliated national centres and its associated international trade secretariats—has certain objectives in respect of multinational companies for the attainment of which it must largely rely on its own strength: international bargaining, the enforcement of fair labour standards, international trade union solidarity and assistance to the unions in the world's developing regions. These have all been examined in detail in the foregoing sections. There are others, however, which call for political action by governments or by regional authorities in view of the growing impact of the multinational corporations on the structure and overall operations of the economy.

In view of the increasing speed of change in technology, working methods, occupational skills, industrial structure, it is clear that the industrial policies of the national and regional public authorities (the European Communities for example) must be strengthened through trade union participation in order to exercise some control over these changes (a policy of modernising industrial sectors; a policy to adapt firms and management techniques; a regional policy; an active manpower policy; a scientific and educational policy, etc.).

It is clear, too, that policies must be strengthened to maintain an overall balance in monetary matters, business cycle, the balance of payments, the pattern of trade and capital flows, etc., and that inter-governmental cooperation to maintain these balances is becoming more and more necessary. The importance of trade union action in these fields is underlined by official trade union participation in the activities of economic bodies at national and international level. ICFTU relations with the UN and its specialised agencies, in particular the ILO, should be mentioned here. The ICFTU has also brought to the attention of the International Monetary Fund its views on the imbalancing factors created by the financial practices of multinational companies.

The initiative recently taken by Mr. Roosa, former U.S. Under-Secretary of State at the Treasury, in proposing the creation of a new international institution, "parallel to the GATT, or possibly within it," with the responsibility for evolving acceptable "rules of the game" for the movement of long-term capital should in this respect be carefully studied. There is, finally, the increased importance of development strategy and the orientation of economic growth to attain appropriate social and human ends. This applies both to the developing and advanced countries. We therefore, suggest that labour protection clauses be included in any new international regulations governing the flow of direct investment.

V. THE INSTITUTIONAL OUTLOOK

The growth of multinational corporations unquestionably calls for a profound re-evaluation of the existing instruments and institutions which govern international trade, investments and industrial relations.

Code of behaviour in international labour relations

In the course of its last 50 years of existence the International Labour Organization has developed a large number of industrial relations standards for application at national level. The new situations and numerous problems to which the growth of multinational corporations has given rise in recent years necessitates the elaboration of new standards. In June 1968 ICFTU submitted to the International Labour Conference a resolution which invited the ILO governing body:

"(a) to request the director-general to study the social aspects of the increasingly international character of economic and financial decisions based on the rapid development of multinational companies with a view to the promotion of, and to enhancing progress in, the establishment of international industrial relations;

"(b) to consider, when deciding on the agenda of Industrial Committees, the contribution these committees can make to the practical elaboration and effective implementation of policies and measures designed for the development of international industrial relations."

Owing to opposition from the employers' group it was not possible to adopt this resolution.

In September 1968 the ICFTU renewed this demand by submitting a resolution to the ILO Asian regional conference, and that conference authorised the governing body to examine the question. Such action by the ILO we think should lead to the establishment of an international instrument regulating relations between multinational corporations and governments. It should include clauses making it compulsory for multinational companies to abide by the fundamental ILO principles and standards on freedom of association and the right of workers to organise and engage in collective bargaining. It should also call for compliance with other ILO conventions, whether or not they had been ratified by the countries in which multinational corporations operate.

The problems calling for international control in this connection are evidently multiple and overlapping. They involve economic and social questions, industrial relations and basic human rights, as well as problems of international trade, investment and monetary affairs. It is therefore clear that no single agency could possibly be competent to deal with the elaboration and application of the kind of international instrument required to regulate the operations of multinational companies. The initiative might well be taken by the ILO, but it would only be natural for other specialised UN agencies—GATT, the World Bank, the International Monetary Fund and the Trade and Development Board—as well as the OECD to be associated with it.

What is basically required is an international code of behaviour to govern multinational company operations. It should be applicable to both industrialised and developing countries. A useful model could be the international convention on the settlement of investment disputes which came into force in 1966. Under this convention there has been set up an International Centre as an autonomous institution. Similar arrangements could be envisaged for the application of an international convention on multinational companies. It could also be administered by an autonomous international centre under the auspices of the specialised agencies mentioned above. Provision should be made, too, for the consideration of complaints about infringements of the convention before a tripartite body representative of the governments, multinational companies and trade unions involved.

The international free trade union movement is firmly convinced that the time has come to introduce the rule of law into the operations of multinational companies. This they believe is obvious common ground betwen the governments and organised labour.

Representative WIDNALL. The next witness will be Mr. Jacques Maisonrouge, President of the International Business Machines World Trade Corp.

STATEMENT OF JACQUES G. MAISONROUGE, PRESIDENT, IBM WORLD TRADE CORP.

Mr. MAISONROUGE. Thank you, Mr. Chairman. I am aware of and greatly appreciate the honor of being invited to testify here today.

It is, perhaps, symbolic of the times in which we live that I, a French national, working for a U.S. firm, should be speaking today to a group of American legislators about an international problem.

For the world continues to grow smaller and its people more interdependent.

Nowhere is this interdependence more evidence than in the growing internationalization of business.

One expression of this trend has been the emergency of large multinational companies which span many frontiers. To be sure, such companies are not new. They existed long before the war. But it is in the last decade that the multinational corporation, operating within an international concept of planning and strategy, has truly come of age. At the same time, there has been a growing need to rely on larger markets.

Twenty-five years ago, technologies were simpler, and by today's standards, development costs were relatively modest.

It was possible in those days to bring a product to consumers with the expectation of a profit within the relatively limited area of national boundaries.

That no longer is necessarily true. The burst of technological developments in the last two and one-half decade with their enormous costs, has frequently required the expansion of markets to justify those costs.

Relatively few people appreciate the underlying reasons for the rise of the multinational company. They simply view the final result—

large corporations that appear to spill over national boundaries from their own sheer momentum—and wonder if they are not some kind of threat to national economic security.

It is a measure of human ingenuity that people on both sides of the Atlantic can view the same phenomena and reach diametrically opposite conclusions.

On the one hand, some Europeans say, "You Americans are taking us over economically. You build plants and laboratories here, hiring away our most highly skilled workers and best minds. And, in the process, you make the most important sectors of our economy reliant on your know-how and your products. You even create a brain drain by hiring our engineers and scientists and taking them to the United States."

On the other hand, some Americans say, "You American companies are not supporting your country's economy. By building plants and laboratories abroad, you are exporting jobs that rightfully belong here. Furthermore, by manufacturing overseas, you are hurting U.S. direct exports and adversely affecting our balance of payments."

It has been my privilege to work for a multinational company both in Europe and the United States over the past 22 years and I believe that my experience has given me some understanding of both points of view.

To a European, the United States is an enormous country, untouched physically by World War II. It entered the postwar period with a tremendous advantage over a continent that had been largely destroyed. Its factories, its research laboratories, its workers, and its general population were intact, ready to turn their energies to peacetime production and consumption.

According to the European viewpoint, this initial advantage has been multiplying over the years until today the United States has far outstripped Europe on almost every front, from basic research to production methods.

Some Europeans believe this pervasive American presence can only be attributed to some formal U.S. plan to penetrate those sectors of national economies with advanced technologies and high rates of growth.

The truth is that a large proportion of U.S. investments has been made in technology-based industries, not because of any single-minded U.S. strategy, but because these industries understand that the European market was growing fast and they went "where the action was." They did this independently of each other, but with similar dynamism and aggressiveness.

Moreover, during World War II scientific and technological advances were considerably slowed down in most European countries, with the exceptions, perhaps, of Germany and the United Kingdom. After the war, America could benefit substantially from its high technological level and its industries could fill the existing vacuum.

Thus, one of the ironies of the postwar period is that the European Common Market became a reality in part through the efforts of American companies.

Those companies, accustomed to doing business freely across 50 States, started out with the assumption that a Common Market made sense. They were used to large markets and appreciated their economic impact and importance. As soon as the Treaty of Rome was signed in 1957, therefore, they began to think and plan in terms of a unified European market with free movement of goods, people, and capital from one end to another.

During the decade of 1958–68, according to the Department of Commerce's June 1970 Survey of Current Business, the outflow of long-term private capital from the United States amounted to $24.1 billion, while income remittances on foreign investments totaled $42.2 billion, for a favorable balance to the United States of $18.1 billion. And growth has been vigorous. Whereas income remitted in 1958 was $2.4 billion, by 1968 it had more than doubled—to $6.2 billion.

Furthermore, between 1958 and 1968, according to the most recent survey of U.S. foreign direct investments, the November 1969 Survey of Current Business, U.S. corporate investments in Europe grew from $4.6 to $19 billion, an increase of $14 billion in just 10 years.

And these are book value figures which would have to be at least doubled, perhaps tripled, if they were translated into current values.

It is this sudden rise in U.S. investment that has brought governmental concern and caused fear and resentment among the European press. Some foreign commentators—and governments—particularly in Europe, fear this growth signals the takeover of their economies by U.S. business. And in some cases, this alarm has manifested itself in protective measures aimed against U.S. firms.

It is partly to avoid such counterproductive measures that multinational companies build plants and laboratories abroad, the better to become accepted in the markets they serve.

The basic fallacy behind the thinking of those Americans who view foreign plants as detrimental to the U.S. export position is that it presupposes the existence of a clear choice between manufacturing abroad and exporting from home. But in truth no such clear choice exists. The alternatives are not "manufacture abroad" or "export." They are "manufacture abroad" or "give up a major portion of your foreign markets." For if U.S. companies did not manufacture overseas, they would not sell anything approaching the amount of goods that they do sell in foreign markets, if only because transportation costs would compel them to price their products at a competitive disadvantage. This is particularly true of low-cost, high consumption articles like soap, toothpaste, or cereals.

Similarly, there is no such choice as "create jobs abroad" or "keep those jobs at home." If U.S. companies did not manufacture overseas, most of those jobs simply would not exist. Moreover, we begin to hear about the European challenge, that is, the investments made by European countries in the United States which in turn create jobs in this country. Recent examples are BASF from Germany, Pechiney from France, and British Petroleum from the United Kingdom.

For, in order to be successful in a foreign market, a multinational company must identify with local interests.

Certainly, experience has proven the wisdom of staffing subsidiaries with nationals of the countries in which they operate. These people are more responsive to the environment, service to the customer is better, and the business grows and prospers with all the benefits that growth brings to the host country as well as to the home country.

Now, let us consider the benefits conferred on the home country—in this case the United States.

From the economic point of view, there are two:

First, the direct financial return realized by investors. According to the Survey of Current Business of the Department of Commerce, in 1969 U.S. companies realized $7 billion on their investments abroad.

Second, markets created abroad produce demand for more products. In our own case last year, although we manufacture abroad, we still export from our plants in the United States, $267 million worth of products and parts to our companies overseas.

Then, there are the nonmonetary, but no less real, dividends remitted in the form of new knowledge.

For example, research and development work in computer hardware and software is being conducted by foreign scientists and engineers in our seven laboratories abroad. While their contributions are only a relatively small part of our total output, nonetheless, what they discover and invent becomes available to IBM in the United States and, eventually, to our American customers. And what is true of IBM is true of other U.S. based multinational companies.

Less directly, of course, multinational corporations benefit the home country through the overall results of their worldwide operations. For by contributing to employment abroad, by acting as an agent of technology transfer, by paying local taxes, by becoming substantial customers of local vendors and subcontractors, multinational firms help strengthen foreign economies. Certainly, if our generation has learned anything in the last 30 years, it is that a healthy vigorous world economy—as a prerequisite of world peace—is in the very best self-interests of the United States.

Benefits accrue to the host country as well.

There is, first, the company's normal economic contributions to the host country's economy:

As an important employer and a substantial customer of local subcontractors, it is a major generator of salaries;

It contributes both directly and indirectly to local tax revenues;

It is often a significant exporter of parts and finished goods, thus adding to GNP's and balances of payments; and

It provides products to meet a wide range of needs. In the process, it raises living standards and enriches the general quality of life, particularly in the developing countries.

Second, the multinational corporation plays a vital role as a "carrier" of technical know-how through such activities as licensing agreements; the training of foreign scientists, engineers, and production personnel; the establishment of subsidiaries; and international participation in scientific meetings, missions, and symposia.

By creating international career opportunities, it brings the people of many nations together on common projects and problems.

We who work for international firms quickly discover that intelligence and talent and creativity have been democratically dispersed throughout the world. We work with each other and we respect each other.

Yet, despite the demonstrably positive consequence of multinational companies operating in an environment of free trade, there are some in every country who would sever the arteries of commerce and undo what took men of good will on both sides of the Atlantic 20 years to create—the free flow of goods between Europe and the United States. And since the United States is the acknowledged leader of the free world, it is imperative that it continue to take the initiative in this area.

We should not forget that foreign trade represents a far greater part of European GNP's than it does for the United States. It reaches more than 70 percent in Belgium and the Netherlands, and a small variation in their foreign trade would have very serious consequences for their economies.

I fear the buildup—at least, for a period of time—of a form of Europeanism that would be the equivalent of a large-scale nationalism. Having finally realized that nationalism did not work, some technocrats, or as they are now called, Eurocrats, may try to build Europe against the United States. This is due to their fear of U.S. economic domination and manifests itself in some measures planned against U.S. firms. The recent Colonna report to the EEC, which suggests certain steps the Common Market countries might take in response to the "American challenge," is one manifestation of this trend. It does not go so far as this country's "Buy American" Acts. It suggests, though, that preference be given to European-based companies in government procurement.

A striking example of what may be lurking in the economic future are the recent restrictive agreements between the Belgian Government and two of Europe's leading electronics groups—Philips of the Netherlands and Siemens of West Germany—whereby fully 50 percent of the purchases of computers for state and other public use in Belgium is reserved to those two European firms.

Should agreements like these proliferate and spur retaliatory measures by other countries, the ultimate consequence could conceivably be a growing protectionism capable of substantially setting back the cause of world trade.

So there is a risk. Protectionist measures tend to escalate. And the protection of particular industries in the United States would lead to the protection of other industries in Europe. In all probability, these would be successful U.S. exporting industries.

Some people are concerned that, as modern management and production methods are introduced in Europe, European industry will have a tremendous advantage because of the low cost of manpower. This is not true for two reasons: first, labor costs are higher than they appear because of the many social benefits European companies offer their employees, frequently in response to legal requirements.

Second, labor costs are rising more rapidly in most European countries than they are here. U.S. Department of Commerce figures indicate that hourly manufacturing wages in the United States have risen in the last 12 months about 6 percent. In comparison, our European economists project a substantially higher increase in 1970. Germany, for example, is projected to increase about 18 percent and Italy at least 16 percent.

There is, finally, a political aspect of free trade and foreign investments which cannot be ignored. Investments by U.S. companies, like those originating in other industrialized nations, have a favorable influence on the standard of living of the host country. Such investments allow the private sector to complement all kinds of aid programs. Most people recognize that one of the great dangers for the future of peace is an increased income gap between developing nations and industrialized ones. Everything that is done to reduce this gap—and multinational companies do a great deal—will, in the long term, help us avoid the enmity of the underprivileged.

The best interests of both the United States and Europe, it is clear from all available evidence, lie in encouraging the continued growth of the worldwide economy and continued international cooperation in the reduction of trade barriers.

Thank you, Mr. Chairman.

Representative WIDNALL. Thank you, Mr. Maisonrouge. I have a question for you. Yesterday Guido Colonna, the former EEC official, gave unequivocal support to the development of a common currency for use in all EEC countries. What do you feel the impact on the dollar will be if this is carried out successfully?

Mr. MAISONROUGE. I don't think it will change the present situation much because current agreements on currency levels are already negotiated in the Group of Ten or through the Bank of International Settlement in Basel. Under Mr. Colonna's recommendation, the only difference is that a common European currency would be negotiated with the dollar—without major impact on the dollar, in my judgment. What it may achieve, though, is the elimination of currency fluctuations within Europe and this, in turn, may give Europe a slightly stronger position in such negotiations.

Representative WIDNALL. Your views on the multinational enterprise appear to contrast sharply with those of Mr. Jennings, especially with regard to labor's position. Will you please comment on Mr. Jennings' statement that many thousands of urgently needed jobs are being exported?

Mr. MAISONROUGE. In this regard, I must return to what I said earlier, Mr. Chairman. While I cannot speak for other companies, of course, in our company we certainly believe that if we were not now manufacturing abroad—and been doing so since 1920—we would have perhaps only 20 or 25 percent of the business activity that we do have overseas. The amount of IBM World Trade Corporation's sales last year has already been mentioned—$2.5 billion. But we must not forget that represented in this figure are a great number of jobs which must necessarily be carried out locally, such as servicing the computers. You cannot do that from the United States; you must have local manpower. The same applies to the selling of computers, administrative work, and so forth. So when you compare figures, you have to consider only the production figures and that makes a great difference.

Moreover, as I mentioned earlier, last year we exported more than $250 million worth of products and parts from the United States to our companies overseas and we believe that, even if we had no manufacturing operations whatsoever abroad, we would probably not have exported much more than than, because the market would have shrunk.

Nor should we forget the economic conditions that prevailed in Europe immediately after the war. Every country had rigid import restrictions because all had balance-of-payments problems. You had no choice—either you manufactured within the country or you did not exist.

Back in the 1955–58 period, for instance, some countries, like France, imposed an export-import ratio of 2 to 1 on all important companies. If we had no active manufacturing activity in France, we just would not exist in that market.

Representative WIDNALL. Mr. Jennings, your statement made a strong case for the argument that the multinational corporation causes exportation of jobs. Now, Mr. Maisonrouge in his statement says: "There is no such choice of 'create jobs abroad' or 'keep those jobs at home.' If U.S. companies did not manufacture overseas, most of those jobs simply would not exist."

Would you comment on Mr. Maisonrouge's statement?

Mr. JENNINGS. Well, I think that the unfortunate fact is what stares us in the face, and the fact is the movement of operations from the United States—from the states around the world, different countries around the world, that is a loss of jobs. That is an export of jobs.

The question of the impact of the multinational firms is a result of this is very, very clear. All we have to do is look at our own industry, what has happened to TV, what has happened with the radios, what is happening with the computers, and to say that the position of the multinational corporation has been one that has resulted in a growth of jobs is true. It has resulted in a growth of jobs and a diminution of jobs and what I think we should be giving our attention to is how do we guarantee jobs? How do we make sure that a gun does not get put at the heads of American workers by American corporations that are now multinational and can go anywhere around the world and that is the truth and this is a fact.

Representative WIDNALL. Coming back to Mr. Maisonrouge's statement, he contends the European advantage due to the low cost of manpower is diminishing, that much of this decrease of wage differentials can be attributed to the multinational corporation. Do you agree?

Mr. JENNINGS. Here, too, you know, you have to look beyond it. One of the things that we had hoped down through the years is by the establishment of effective trade unions around the world, they could do a good and effective job of raising their own wages, and we figured that this in the long run would have a beneficial impact around the world and also would help us. But what we have seen, for instance, in Japan, where we developed the relationship with a very good and effective and militant union, we have seen American companies moving into the Far East and threatening the wages that the Japanese workers have now won in Japan through this union and the result is that because of the American operations overseas, the Japanese corporations are telling the Japanese unions, you had better keep your demands down or else we are going to move to Taiwan or Hong Kong or somewhere else.

So, it is just a question of how long the game can be played and I do not think that American workers want to have that kind of a gun at their heads as they try to protect themselves.

Representative WIDNALL. There was recently an article in the Washington Post, on June 7 of this year, by Nat Goldfinger, director of research of the AFL–CIO. He called for the Government to regulate the operations of U.S. based multinational corporations. Could you please specify what kind of regulations the AFL–CIO is calling for?

Mr. JENNINGS. I would not want to be specific but the one thing that is absolutely obvious, nobody—nobody knows what is actually going on. Nobody knows the impact, nobody knows the investment, nobody knows the policies. No one controls them because these corporations have now become a world among themselves and I think that this is what Nat is talking about and when you try to get information, you just run up against a blank wall.

Representative WIDNALL. Well, your organization is not ready at this time to submit any recommendation to the Congress?

Mr. JENNINGS. No.

(The following information was subsequently supplied for the record by Mr. Jennings:)

1. Regulate and supervise export of capital to all countries.
2. Remove tax incentives now in law to spur foreign investment. This includes requiring taxation of profits wherever earned at the time that they are earned.
3. Require reporting of output, employment, hours, earning by establishment by SIC numbers to 7-digit level for foreign locations by U.S. firms, just as they are now required to report for U.S. establishments.
4. Refuse to grant new tax-loopholes, such DISC.
5. Require reporting of import and export data by product, not just dollar volume.
6. Require labeling of products by country of origin from any country—including U.S. brand items and all components.
7. Require uniform accounting procedures by multi-national firms as for defense contracts.
8. Tax the export of capital to create a disincentive to produce abroad.
9. Make U.S. government-subsidized patents the property of U.S. government with royalties paid to U.S. Treasury.

Representative WIDNALL. Do you have any facts or figures in connection with whether or not the final product in these overseas operations using what you say is very low-cost labor, has any ultimate benefit to the American consumer?

Mr. JENNINGS. We have just the opposite.

Representative WIDNALL. To the American producers? Could the American get the final product at a price better than it was before they went into overseas operation?

Mr. JENNINGS. We have just the opposite proof. We have been able to put together pieces of information where Westinghouse is now bringing stuff back from overseas, and components, and mostly these higher TV operations are put together overseas. There is no reduction in the price. There is an incredible amount of saving that goes to the company but there is no reduction in the price and the consumer gets no break at all.

Representative WIDNALL. Mr. Jennings, could you submit for the record, some of the evidence that you have along this line?

Mr. JENNINGS. Yes.

Representative WIDNALL. I think it would be very valuable to have.

(The following information was supplied for the record by Mr. Jennings:)

WHAT ABOUT CONSUMER PRICES?

Every consumer knows that U.S. prices have been rising rapidly. Every trade expert knows imports have been rising rapidly. Yet liberal trade advocates continue to say that consumer prices will go down because of imports or will go up if quotas are enacted. What are the facts? There is no clear-cut relationship.

By February 1969 over-all consumer prices had risen 32.5% from the 1957–59 level.

For some of the most rapidly rising imports, however, prices went up faster.

Shoes went up 45%. Ladies' shoes, 51.6%. No quotas exist.

Cotton blouses went up 24.9%. A quota exists under the Long Term Cotton Textile Agreement.

Street dresses of synthetic fibers went up 58.7%. No quotas exist.

Sugar went up 17.2%. This is controlled by quotas.

Coffee went down 2.6%. This is controlled by quotas.

Cola drinks went up 60.3%. No quotas.

Why, then, do some prices go up despite rising imports and others go down when imports rise. Why do some prices fail to show any relationships?

1. The U.S. economy is huge and imports represent only 4% of the total. By the time prices were strongly affected by imports, there would be mass injury to many industries, mass unemployment. There can be no clear-cut relationship.

2. Many retail stores import their products directly from countries like Taiwan, Japan, etc. The price to the importer is low. But the price to the consumer depends on prices that the companies can charge the U.S. consumer whose income is high. Demand affects prices in this market. Monopolistic pricing policies affect prices.

3. Global conglomerates produce different parts in different countries around the world at different labor costs and mingle the goods which they sell at the same price to the U.S. retail store. Kayser Roth, for example, produces gloves in several different countries, including the U.S. It sells them all at the same price here.

4. Many factors other than production costs affect prices.

5. U.S. firms with licenses in other countries import products in their brand names and set their prices for this market: The following products were made complete including boxing in Japan, Taiwan or Hong Kong. Here is part of a price list copied from one company's list.

Product	Price in Japan	Price landed in the United States	Suggested retail price
Portable radio	$11.66	$13.81	$39.95
Do	17.88	21.35	59.95
Do	19.20	22.10	59.95
Do	46.22	54.05	179.95
AM-FM tuner amplifier	(1)	39.10	119.95
Do	31.74	38.80	159.95
Stereo cassett tape recorder	(1)	52.63	149.95
Stereo reel tape recorder	70.65	90.00	219.95
Portable cassett	(1)	27.73	89.95
Stereo cassett tape recorder with speakers	(1)	66.00	189.95

[1] Unknown.

Business publications describe how this works. For example, the spokesman of an international U.S. based company, producing in Taiwan was quoted, as follows in *Electronics News* on March 2, 1970:

"Although assembly of complete color sets in Taiwan won't affect pricing stateside . . . it should improve the company's profit structure. Otherwise we wouldn't be making the move. We'd leave the sets where they are now." This suggests that profits, not consumer prices are the major reason for some imports.

Journal of Commerce on March 19, 1970 included this comment:

"Leaders of large multinational corporations and banks are fighting a holding action in their effort to prevent further restrictions of imports. They cite the advantage of foreign competition which can mean lower prices and a wider variety of goods for the consumer.

"(They don't say much about the benefit to their profits from being able to obtain cheaper components, parts and other supplies, which cut the costs of production in their plants spread around the world.)"

Representative WIDNALL. Mr. Dunning, in your prepared statement you describe a vast spectrum of attitudes and policies toward the multinational enterprise on the part of different host governments and even on the part of the same host government at different times. This being the case, do you see much hope for the creation of a GATT-type mechanism for multinational investment such as proposed to this committee by several witnesses?

Mr. DUNNING. Well, in general, Mr. Chairman, I am in sympathy with this kind of proposal. I think it has been pointed out in a number of submissions before you, that host countries, particularly host countries in Europe, have by their policies toward multinational enterprises tended to bid up the price which they have to pay for the benefits which these enterprises confer upon them.

For example, if Belgium wants to try and obtain further foreign investment in the areas of above-average unemployment, then it may well decide to give certain incentives to foreign firms to come in to produce in these areas. It might well be then that Holland or Germany or the United Kingdom finds that American companies are switching their programs from their particular economies. This they see as a possible threat to their own competitiveness and, in retaliation, they increase their incentives.

Now, all of this seems to me to be in the longrun interests only of multinational enterprises who will, naturally enough, tend to take advantage of these incentives. So, I would argue that, rather than try to formulate codes of good behavior for multinational enterprises in the way in which, for example, the Canadian authorities have tended to do, we should try and formulate some sort of code of good behavior for governments, and it is in this respect that the GATT-type mechanism rather appeals to me.

Representative WIDNALL. I think it might be interesting at this time to have the members of the Panel comment on statements made by other members of the Panel which may have been disturbing to them or where their own views conflict markedly with what has been stated, and I would like an exchange of views if you are willing to do that.

Mr. Maisonrouge?

Mr. MAISONROUGE. Mr. Chairman, there is one point I would like to take issue with and that is the contention that corporations hold a gun at the head of governments or trade unions and threaten that, if the government or trade union does not behave, the corporations will shift their production facilities elsewhere. First, it is an impractical posture because there is a limit to how much you can shift your production from one country to another.

Second, the so-called tax havens or low labor rate countries are generally pretty small and do not themselves represent large markets. Furthermore, I do not think a multinational corporation can be successful if it does not behave well in the host country.

I will give you an example. Back in 1962, two American-based companies closed their French production facilities, one a plant near Paris, the other a plant near Lyons, in order to rationalize their production—as they termed it—and transferred their facilities to another European country.

Well, they have never recovered from the effects of those decisions because the government has not forgotten their behavior. So, I think if you want to be successful over the long term, you have to be well accepted by your host country. Besides, your most important markets are always the industrialized countries of the world. It is not in Taiwan or in Singapore that large markets for computers exist, but in countries like Japan, Germany, and France.

In our own case, like most multinational companies, we certainly try never to do anything which might antagonize the French, German, British, or other governments, nor do we want to antagonize the labor unions or workers in those countries.

Representative WIDNALL. Essentially, that applies to your company and not to most other companies because you have a specialized product and not a variety of products like many of the companies have.

Mr. Jennings?

Mr. JENNINGS. You know, the host country by definition, is difficult to pin down because by the very nature of the growth of the multinational corporation, the countries that they will be in is a shifting panorama and the tragic part of this is that they go where the cost is the lowest and one host country might come up for a while but then these outfits will go somewhere else.

This is why it is important that somehow it be looked at and somehow there be an approach to their ability to play a role that is absolutely undetected up until this point. And to say that no gun is, you know—I use this figuratively. It happens every time we attempt to negotiate contracts here. People tell us we are going to shut down the operation, we are going somewhere else, because, you know, you are putting yourself out of the market. They are going to go down to Mexico, they are going to go to Japan, they are going to go to Latin America. So, this is something that we come up with every day and more and more of the labor movement on a worldwide basis is coming up against the same kind of thing. When the unions develop the ability to function effectively, this will be the threat that will be faced with.

Representative WIDNALL. Mr. Maisonrouge, Charles Kindleberger, and Guido Colonna agreed before this subcommittee yesterday that the growth in international investment points up the need for some kind of international machinery to resolve policy disputes. Do you also agree and if so, what kinds of machinery would you propose?

Mr. MAISONROUGE. I think it would be good for multinational corporations to have a counterpart which represented governments, although I must admit that I have no precise idea of what form such a counterpart might take. Perhaps such organizations as GATT or the International Monetary Fund could serve as models for an international counterpart to multinational companies, in which representation would be tripartite, for labor, government, and companies.

Representative WIDNALL. Would you like to comment on that, Mr. Dunning?

Mr. DUNNING. Yes; I would. I think we have got to distinguish between the type of international organization which might have, as its main target, the harmonization of fiscal policy, company law, mergers, legislation, and the like, as the affect the operation of multinational enterprises, and the type of organization which, in some way or another, might attempt to control or limit the way in which multinational companies are run. My own feeling—and I go along with both Charles Kindleberger and Harry Johnson on this—is just as within a nation state, it is up to the national government to create the appropriate environment so that its own economic agents can act with the maximum of freedom. Corporations exist primarily to advance the interests of their shareholders, but it it up to nation states to create the economic climate such that when national corporations act in this way, they benefit the community as a whole. And I would argue that this kind of approach should be extended to a world level, and that nations should seek ways and means whereby they might adopt appropriate economic policies so that multinational enterprises can get on and do the job which they are supposed to do, and at the same time operate to the benefit of the world economy. There is, of course, the very important question of the distribution of the benefits. As pointed out in my prepared paper, a lot of the problems which Mr. Jennings has rightly raised, deal with the sharing out of the fruits of the multinational enterprises.

Now, I would argue that so long as you got a free competitive environment, then multinational companies like national companies, cannot exploit labor or for that matter, any other sector of the community. They earn the profit which is necessary for them to operate efficiently in these countries and the host nations and the investing nations also benefit as a whole. So, a lot of these questions, I think, come down to the sharing of the benefits of the multinational enterprise and one has to be careful, I think, not to introduce policies which would kill the goose that lays the golden egg.

Could I just make one further point, Mr. Chairman? The issues which have been brought to our interest by Mr. Jennings this morning is reminiscent of the old debate of free trade versus protectionism. I cannot myself see any significant economic difference between wishing to control the operations of multinational enterprises and wishing to control international trade. I gave my rather simple example of oranges. Well, if multinational companies from the United States did not go aboard, to take Mr. Jennings' examples presumably American consumers would still wish to import transistor radios and cheap electrical products from Japan.

Now, what is the U.S. Government to do? Is it then going to say, well, let us stop Japanese firms from exploiting the U.S. market, by increasing import tariffs? You see, I do not really think there is any significant difference economically between this question of exporting jobs—about which I appreciate Mr. Jennings' concern—via the multinational enterprise, and the export of jobs which result when Americans buy products which are more cheaply made overseas by companies other than multinational concerns.

And, so, I do think—I have again said this in my prepared paper—that the multinational company does demand a great deal of economic flexibility on the part of host and investing countries. In the United Kingdom, this has not been too much of a problem. There have been examples of the rationalization schemes of American companies causing loss of jobs but my attitude to this would be you have got to take the rough with the smooth and it is up to the United Kingdom Government to introduce appropriate macroeconomic policies to see that any jobs which are lost are filled again pretty quickly. Here, Mr. Chairman, I put the onus fair and square on governments to maintain appropriate employment policies.

Representative WIDNALL. Thank you.

Mr. Maier, would you not like to comment on that?

Mr. MAIER. Thank you, Mr. Chairman. I just wanted to express my appreciation for the recognition by Mr. Maisonrouge that any international regulation of long-term private investment or, let us say, a code of behavior on multinational companies should be governed by a tripartite body. That means including labor unions.

Thank you.

Representative WIDNALL. Well, that is all that I have. I certainly want to thank you for appearing here today and I want to express the regrets of other members of this subcommittee who unfortunately, had last minute conflicts of a very major nature so they were unable to be here during the course of your testimony. Knowing them all, I know they are going to read it and enjoy it and will benefit greatly by it.

Thank you for appearing today.

The next meeting of the subcommittee will be held tomorrow morning, July 29, at 10 a.m., at which time Mr. N. R. Danielian, president of the International Economic Policy Association; Mr. Yves-Andre Istel, Kuhn, Loeb & Co.; Mr. Sidney E. Rolfe, professor of economics, Long Island University; and Mr. Robert Stobaugh, Jr., associate professor of business administration, Harvard Business School, will be the witnesses.

Thank you for being with us today. The meeting is adjourned.

(Whereupon, at 12:10 p.m., the hearing was recessed, to reconvene, at 10 a.m., Wednesday, July 29, 1970.)

A FOREIGN ECONOMIC POLICY FOR THE 1970'S

WEDNESDAY, JULY 29, 1970

Congress of the United States,
Subcommittee on Foreign Economic Policy
of the Joint Economic Committee,
Washington, D.C.

The Subcommittee on Foreign Economic Policy met, pursuant to recess, at 10:03 a.m., in room S-407, the Capitol Building, Hon. Henry S. Reuss (member of the subcommittee) presiding.

Present: Representatives Reuss and Widnall.

Also present: John R. Stark, executive director; John R. Karlik, economist; Myer Rashish, consultant; and George D. Krumbhaar, economist for the minority.

Representative Reuss. Gentlemen, be seated.

The Subcommittee on Foreign Economic Policy of the Joint Economic Committee will be in order for the third day of our hearings to examine the effects of direct investment across national boundaries and the growth of what are now recognized as multinational corporations.

Once again we have the privilege of an extraordinarily distinguished panel of witnesses. Appearing first is Dr. N. R. Danielian, president of the International Economic Policy Association. Then Mr. Yves-André Istel, a partner in Kuhn, Loeb, and then Prof. Sidney Rolfe, who is now teaching at Long Island University and has formerly served as consultant to the International Chamber of Commerce on the subject of multinational corporations. Finally, Robert Stobaugh, associate professor of business administration, Harvard University Graduate School of Business Administration.

You all have comprehensive prepared statements, gentlemen. Under the rule and without objection, they will be admitted in full into the record. And as you now proceed, I would hope you will summarize your prepared statements and put the high points in your oral statement.

Mr. Danielian?

STATEMENT OF N. R. DANIELIAN, PRESIDENT, INTERNATIONAL ECONOMIC POLICY ASSOCIATION

Mr. Danielian. Mr. Chairman, I have a prepared statement here which will be printed, with your permission, in the record. I would like to read a summary which will take me about 15 minutes.

Representative Reuss. By all means, and do not limit yourself to the summary if you want to go beyond it. But that is a good way of proceeding.

Mr. Danielian. Mr. Chairman, multinational corporations contribute perhaps 15 percent of the gross national product of developed and less-developed countries outside the United States and Communist countries. This would amount to $180 billion a year. If their contribution to U.S. gross national product were included at the same percentage, this figure would be doubled to $360 billion.

U.S. multinational corporations account for about 20 to 25 percent of total exports. It is likely that a similar percentage, if not more, of all international commerce is carried on by all multinational corporations. If so, that would account for $60 billion or more of world trade.

There is no other instrumentality with the same flexibility, inventiveness, initiative, and effectiveness as the multinational corporation in undertaking the extraction, refinement, fabrication, transportation, and marketing of resources in food, fibers, minerals, and chemicals, to meet the expanding needs of an ever-increasing population. No armies, no governments, no foreign aid, no international institutions can match this achievement.

The political environment in which these corporations are allowed to operate is not particularly suited to efficient allocation of their resources and technology.

They are confronted with a diversity of political motivations: some of emotional origin, such as nationalism; others ideological, such as communism; and some even humanitarian, as in the case of welfarism—which subject them to a multiplicity of restrictions and taxation of varying levels in different countries.

They have to do business in a variety of environments: the nation state, common markets, free trade areas, preference systems, state trading blocs, and democracies of varying degrees of popular representation, rebellions, revolutions, and too often, destructive conflagrations of war.

They have to cope with controls over imports and exports, tariffs, nontariff barriers, diversity of tax systems and tax rates, different welfare schemes, variety of employment policies, exchange controls, antitrust rules, and threats of nationalization and expropriation.

The multinational corporations, the most important instrument for economic development, are left starkly alone, buffeted by the violent currents of world politics, with no support in public opinion, no court of appeal, and often abandoned by their own governments.

It is often said, and it is true, that there is a conflict between national sovereignty and the multinational corporation. As states acquire greater power, and governments join their interests into larger blocs, one must expect that this contest will be resolved in favor of government sovereignty, whatever the economic consequences.

To remedy this situation and establish some standards of behavior, to give a degree of predictability to planning of business operations, a number of recommendations have been made. These are hopeful expectations of international cooperation through agreement: to guarantee investments, equalize tax burdens, establish uniform antitrust policies, allow flexible exchange rates, eliminate nontariff barriers, fix common labor standards and create a code of business practices.

Looking at the world as it is today, with 33 percent of the 3.6 billion people who inhabit the earth living under Communist systems, some

20 percent under non-Communist dictatorships, 7 percent just on the threshold of developing viable governmental organizations, 14 percent in India, and about 26 percent in various forms of democratic societies, it is hardly possible to be very optimistic about developing international standards that will cover a major portion of investments and trade.

Hence, I come to the conclusion that if any stability is to be accorded to the existence and operation of multinational corporations so that they can make their greatest contributions to production, the U.S. Government must take the initiative in international negotiations.

We find, however, that the U.S. Government does not have the bargaining strength in international economic negotiations it used to have in the early postwar years. The primary reasons for this diminution of bargaining power are the continued balance-of-payments deficits and accumulated net current liabilities; the deterioration of our export position; the internationalization of technology; and the development of trading blocs all over the world which violate the principles of unconditional most favored nation, national and reciprocal treatment. By and large, the U.S. market, a very powerful negotiating instrumentality, cannot be used effectively as long as we adhere to the principles of unconditional most favored nation, national and reciprocal treatment, while most other nations are honoring these principles only marginally.

To put the United States in a better bargaining position, to shore up its weaknesses, to enter international negotiations from a position of strength, we make the following specific suggestions:

To strengthen U.S. balance-of-payments position:

1. Establish an International Security Fund to share in the foreign exchange costs of our farflung military deployment for peacekeeping (excluding Indochina) purposes, especially in NATO, and thus curb the unfavorable effect of these expenditures on our balance-of-payments deficits. It is historically true, Mr. Chairman, that by and large our basic balance-of-payments deficits have been pretty close to the amount of our governmental expenditures abroad. And I believe that international banking and the diplomatic community could serve the world better if they applied themselves to this question of how to share the security costs of the world so that their balance-of-payments effects would be eliminated and the foreign exchange markets would be free from the overweight of these accumulated dollars and other currencies.

2. Place conditions upon the contributions of the United States to international financial institutions, with a view to eliminating the balance-of-payments impact of foreign aid thus channeled which still amounts to about $700 million a year.

3. Approve the Domestic International Sales Corp. (DISC), but expand its application to include service exports, and in particular, tourist and travel services. In addition, adopt incentives to encourage repatriation of foreign source income.

4. Codify by legislation the conditions of disposal of industrial property rights and know-how resulting from Government-financed research and development programs and establish a licensing procedure in foreign applications in exchange for economic value received. Sim-

ilarly, insist that the U.S. Government support the industrial property rights of its citizens in other countries. This policy, I believe, Mr. Chairman, would bring in a great deal of net earnings to the United States.

5. Amend section 5 of the Trading with the Enemy Act to exclude from its application capital movements between the United States and friendly countries. This would dispose of OFDI and carry——

Representative REUSS. What is OFDI?

Mr. DANIELIAN. Office of Foreign Direct Investment, and it will carry out one of the almost unanimous recommendations of this committee in its report on the President's report this spring.

6. Amend the antitrust laws to apply to foreign situations only where there is reasonable evidence of actual and substantial effect on the international commerce of the United States.

To strengthen negotiating techniques of the United States, we recommend as follows:

7. Recognize the reality that the world is divided into trading blocs, most of which will not conform to the principles of unconditional most favored nation, reciprocal and national treatment of other countries and their citizens. To secure control of U.S. market access as a bargaining lever, Congress may wish to amend section 251 of the Trade Expansion Act of 1962, as amended, from unconditional to conditional most favored nation; and amend section 211 to include not only the European Common Market, but also other nations, common markets, free trade areas, and the Commonwealth preference system, with such changes in the conditions as will reflect U.S. interests, and the desire to liberalize world economic activity on a reciprocal basis. Mr. Chairman, in making this recommendation I want to emphasize that the end purpose is to liberalize world commerce; but with this instrumentality, we are going to be able to talk reason into the policies of other nations better than merely talking at a multiplicity of conferences all over the world with no results that really are appreciable. I recall that our negotiations with Japan concerning the liberalization of their investment and trade policies started at the Cabinet level meeting between the Japanese and our Government in July 1965 and I must say that in 5 years, almost to the day, the results have been hardly noticeable.

With this kind of an instrumentality in the hands of the U.S. Government, I am sure we could get a more quick result.

8. Authorize the Executive to enter into bilateral negotiations with other nations, common markets, trading blocs, et cetera, on the full range of pending economic issues, not just trade, if they are to qualify for most-favored-nation treatment in the U.S. market. These issues should include tariffs, nontariff barriers, national treatment of investments, protection of industrial property rights, guarantee of investments, aid, agricultural policy, and contributions to the International Security Fund.

9. Establish in the Office of the President a Council on International Economic Policy. The United States appears to me to lack a cohesive machinery for defining our economic interests abroad and for negotiating about them from a position of strength. What has happened in the last 6 months is a good example of confusion in the Executive

departments and it seems to me that we need the focus of policy determination in the executive branch, in the Office of the President.

International economic policy has critical importance to domestic policy, as well as to international security. The former is the province of the Council of Economic Advisers, set up by Congress in 1946 to promote "employment, production, and purchasing power." The latter area has the National Security Council, established by statute in 1947 to advise the President on "domestic, foreign, and military policies relating to the national security." The third leg of the triangle, international economic policy, is distinguished by its absence.

We propose, therefore, that this committee consider the creation of a Council on International Economic Policy to advise the President. Whether this Council should be an intragovernmental body as an instrumentality of the administration; or whether it should consist of experts like the Council of Economic Advisers, giving full time and attention to the international aspects of economic policy; or whether the members should be nonpolitical specialists with long tenure, such as the Federal Reserve Board—requires detailed study.

However organized and staffed, the council should, in my view, do three things: First, identify and define our economic interests by areas in different parts of the world; second, make recommendations on minimum and maximum objectives in international negotiations affecting those interests; and third, prepare a realistic foreign exchange budget for the United States, which could analyze the critical and long neglected aspects of our total "costs' 'in foreign operations. Such a budget could, I am sure, be of great assistance to Congress—and to this committee in particular—as well as to the President and within the executive branch. Other departments of the Government would, of course, put their respective claims to foreign resources before this Council, and they would have the right, as always, to take their case to the President.

To these recommendations I would like to add also a further thought. At the present time the British are negotiating for entry into the Common Market. The Common Market agricultural policies have had a deleterious effect upon our exports; and with British and other EFTA country entrance into the Common Market, I think our export trade in agricultural products would be very detrimentally affected.

I suggest, therefore, that before these negotiations in Brussels are concluded, the President take the initiative to call an international conference among the principal producing and consuming countries for the puropose of defining, as far as possible, a viable and consistent agricultural policy on an international basis. Otherwise, I think the developments in Brussels are likely to lead to very serious and unhappy international diplomatic conflicts and controversies.

I have centered my recommendations principally on the things in which this Government can take the initiative because I feel that in the present context of the world structure, politically and economically, it is only through bargaining from a position of strength that we are going to be able to achieve some of these objectives.

I submit that in spite of the present confusion of opinion in the United States, these suggestions offer a practical means of creating an environment with greater stability and predictability than has been the case during the past decade. If we cannot put our own house in order, however, I see very little hope of achieving international agreements for the rationalization and standardization of economic behavior around the world. And I shudder at the prospect of traveling down the same road in the 1970's that we just came through in the 1960's.

Thank you.

Representative REUSS. Thank you for those crisp suggestions.

(The prepared statement of Mr. Danielian follows:)

PREPARED STATEMENT OF N. R. DANIELIAN

THE MULTINATIONAL CORPORATION AND ECONOMIC POLICY

It is indeed a privilege to appear before this Committee in the company of such a distinguished panel. In my recollection of the past 25 years, these hearings have been the most comprehensive concerning international economic issues.

They reveal substantial evidence that the multinational corporation has been an important vehicle for economic development, transfer of technology, increased productivity and higher standards of living. This view, of course, like all generalizations, is not unanimously held. Labor in this country has become very wary of American investments abroad for fear of losing jobs. There are those across the polar caps who never let a moment pass without repeating on the airwaves of the world that American investments are synonymous with "Imperialism," and insidious invasion of foreign countries, and a means of exploitation.

The experience of the last 25 years must, however, prove conclusively to any objective observer that there is no other instrumentality with the same flexibility, inventiveness, initiative and effectiveness as the multinational corporation in undertaking the extraction, refinement, fabrication, transportation and marketing of resource in food, fibers, minerals and chemicals, to meet the expanding needs of an ever-increasing population. No armies, no governments, no foreign air, no international institutions can match this achievement.

In this paper, I shall try to define the economic importance of multinational corporations, analyze some of the recommendations made to improve the international environment in which they operate, and suggest some concrete measures which are within the competence of the U.S. government to undertake.

THE ENVIRONMENT: ECONOMIC

It is true that many of these corporations are often identified with the nation of their origin. However, as savings increase with the rise in incomes throughout the world, a true internationalization of ownership may be the next step in the evolution of multinational companies. In 1968 European portfolio investments in U.S. corporations, many of them—probably most of them—of a multinational nature, amounted to over $16 billion. Our own portfolio investments in the securities of other national and multinational companies amounted to $18 billion. Many underdeveloped countries with large hard currency earnings through sale of mineral resources, such as those in the Middle East, invest their income in these companies. It is estimated that Switzerland alone channels $35 billion of other people's money into international investments!

In addition, direct investments by U.S.-based corporations abroad amounted to $65 billion in 1968, and European direct investments abroad probably were in the neighborhood of $50 billion.

In the early years of the Industrial Revolution the corporation was a most necessary instrument to assemble the savings of many people and apply them to specific production objectives. The multinational corporations are now serving the same purpose on a worldwide scale.

The gross national product of the world in 1968 can be estimated at about $2,640 billion. Figures for the Communist countries are necessarily very rough; but $640 billion is an acceptable approximation. The world outside of the Communist countries produced about $2,000 billion—that is two trillion dollars—worth of goods and services. A further division of this between developed and less developed countries gives a surprising result. Only 9.7 percent, or about $255 billion, was produced by less developed countries and $1,740 billion by developed countries. (The figures for LDC's are also incomplete, as they fail to account for production in the "subsistence" sector outside the market economy.)

The United States accounted for nearly half, or $866 billion, of this $1,740 billion total; the EEC, $380 billion, and all other developed countries, roughly $500 billion. Japan alone produced $142 billion of this last figure, and other European countries, outside EEC and Communist countries, $240 billion of the remainder.

The U.S.-controlled multinational corporations are said to have produced over $120 billion worth of goods and services abroad. This would be a little more than 10 percent of the gross national product of both developed and less developed countries, excluding the United States. If you add to this the contribution made by multinational corporations headquartered in other countries, the proportion of gross national product contributed by these institutions would probably be in the neighborhood of 15 percent or more. This is assumed from the premise that the value of foreign direct investments by multinational corporations based outside of the United States is estimated at a level at least one-half as much as the U.S. direct investments—appreciably more on a current value basis.

These figures do not take account of portfolio investments which, although they do not necessarily involve control of management, certainly contribute capital for economic development and make their contribution to the gross national product of other countries.

If one were to add to these figures the production contribution that these multinational corporations make to the gross national product of the United States, of which there is no separate estimate, it would come to a very large and compelling figure.

We have here, therefore, an instrumentality of much importance to the economic development of the world outside Communist countries. It must not be taken lightly or dealt with cavalierly by any country or jurisdictiton.

One must come to the same conclusion by looking at world trade figures. Of the $240 billion of world exports in 1968, $213 billion was accounted for by developed and less developed countries, and $27 billion by Communist countries. Developed countries exported $170 billion, of which the U.S. portion was approximately $35 billion, EEC's, $64 billion, Japan's, $13 billion, and the United Kingdom's, $15 billion.

In the case of the United States, it is estimated that approximately 20–25 percent of its exports are sales by multinational corporations to their affiliates abroad. There is no comparable figure for other countries' exports. Suffice it to say, however, that multinational corporations account for a large proportion of international commerce.

THE ENVIRONMENT: POLITICAL

The environment in which these corporations are allowed to operate to do their task of production and distribution is not particularly suited to efficient allocation of their resources and technology.

The reason is that political life is not as rationally organized and motivated as one would wish. There is no measure of cost effectiveness in the selection of objectives and expenditures of resources in politics. This is as true in the United States as it is elsewhere. Furthermore, there is a diversity of motivations, many of emotional origin, such as nationalism, leading to a variety of restrictions on trade and investments. Others are ideological; for instance, acquisition and control of power, as in Communism. Some are even humanitarian, as in the case of welfarism, and affect employment policies, social security, unemployment compensation, public housing, medicare, etc., with resulting tax burdens of varying degrees in different countries.

The diversity of motivations finds expression in a variety of institutions: the nation state, the common markets (i.e. EEC), free trade areas (i.e. EFTA), preference systems (British Commonwealth), the state-trading Communist bloc (COMECON), democracies of varying degrees of popular representation, unstable governments racked with revolutions, and countries caught in the destructive conflagrations of war.

These diversities find expression in a variety of policies: control of imports and exports, tariffs, nontariff barriers, varying rates and types of taxation, different welfare schemes, employment policies, exchange controls, different antitrust rules, nationalization and even expropriation.

It is a wonder that, instead of reviling the multinational corporations, some authority has not created an order of merit or a legion of honor to recognize the daring and the risks they undertake in pursuit of profit through production in this turbulent and disorderly world.

The only attempts to create institutions to deal with these international instabilities have been the United Nations, with indifferent success; GATT, to regularize trading rules, often circumvented; OECD, mainly a club for the "have" nations, advisory in its functions; IMF, which has brought some semblance of stability in monetary affairs, but has not been wholly successful because of the varying national economic policies and political necessities; and various international financial institutions that give credits and grants to less developed countries, such as the IADB and IDA.

The multinational corporations, the most important instrument for economic development, are left starkly alone, buffeted by the violent currents of world politics, with no support in public opinion, no court of appeal, and often abandoned by their own governments.

THE ENVIRONMENT: SOME FAMILIAR REMEDIES

To create an environment in which the multinational corporation can do its job of mobilizing savings for economic development without being impeded by these nationalistic crosscurrents and conflicts, many experts appearing before this Committee and others have recommended:

1. An international code to guarantee investments.
2. An international agreement on taxation to equalize tax burdens and eliminate double taxation.
3. An international agreement for uniform antitrust policies.
4. An international agreement on flexible exchange rates.
5. An international agreement on nontariff barriers.
6. An international code of labor standards.
7. An international code on business practices.

What are the chances of international cooperation on such a variety of issues in this turbulent world, where a third of the world's 3.6 billion people live under Communist systems, some 20 percent under non-Communist dictatorships, another 7 percent just on the threshold of developing viable governmental organizations, and 40 percent in democratic societies—of which percentage India alone makes up more than a third? I would think the chances of accomplishing a modicum of stability in the rules applicable to multinational corporations through international negotiations are rather dim.

Let us briefly look at the specific possibilities listed above.

The ideal conditions under which a multinational corporation could do its job best would be to free it from these vagaries of nationalistic and ideological conflicts, and establish some universal rules. This obviously is beyond our capacity at this time to sell to the rest of the world.

The World Bank has been attempting since 1962 to develop an international convention for the protection of investments, without success. Much of the opposition has come from the less developed countries.

It has been difficult enough to negotiate bilateral treaties on taxation. A multinational approach to this problem would almost certainly doom it to failure.

We are probably unique in our concept of antitrust policies. For us to undertake to convert the rest of the world to our view would be impractical. This is not only a matter of business policy, but in some countries, as in Japan, it is almost a cultural fixation, and in others, as in Europe, trust have been a "lifestyle" of large business operations. In fact, whereas here we threaten jail sentences for conspiring to eliminate competition, among our citizens in Japan and England they are giving accolades and subsidies to merging competitors!

An international agreement on flexible exchange rates is feasible. In fact, in 1966, in our book on the U.S. Balance of Payments, we recommended a 2 percent spread from IMF parity rates. But this was intended to discourage speculation and raids on currencies. Fexible exchange rates or crawling pegs currently seem to be of dubious value for the United States. The *net* effect upon us is likely to be detrimental. Those countries that devalue their currencies in relation to ours will obtain an export advantage. Those few that might revalue their currencies will merely diminish the purchasing power of the dollar where our expenditures are fixed, as in the case of military deployments in the Far East and in Europe. The result will be increased budgetary and foreign exchange costs to us. For example, the recent German revaluation is costing us an extra $100 million a year to maintain our troops there.

An international negotiation of nontariff barriers is most desirable, although perhaps even more difficult than negotiations on tariff barriers. Here again our chances of obtaining an advantageous agreement will depend on our bargaining position, because the main issues are matters of fundamental economic interest, such as "Buy American" on our part, and the common agricultural policy on the part of EEC.

Common labor standards would be most difficult to obtain. As a starter, I assume U.S. labor would demand minimum wage commitments. Most of the less developed world needs labor-intensive industries to give employment instead of highly automated industrial plants giving limited high wage labor employment. Under-employment or unemployment in exploding urban areas of the less developed world is a major—and increasingly serious—consequence of the so-called "green revolution" which has deprived large numbers of peasants from work in agricultural production, so that they gravitate to the cities—which goes to show that it does not necessarily follow that what's good for the United States is good for Katmandu.

An international code of business practices is theoretically feasible, at least among the western developed countries because their interests are commensurate.

As Communist countries expand their operations on the international scene, with their different cost accounting, labor and welfare policies, it is doubtful that a purely western code of business practices can stand up, particularly if their claim to most-favored-nation treatment is granted.

Thus it appears, unfortunately, that our ability to accomplish the organization of the world into a rational legal framework with enforcement powers is very limited indeed.

If international standards are not now practical, a more modest objective would be to permit multinational corporations to do their task of economic development without impinging on the national sovereignty of host countries—to become good corporate citizens of each country where they operate. Even this is difficult because in many areas of the world there is almost irreconcilable confrontation between the basic philosophy of private ownership of productive property and dogmas about public control and operation—which get entangled with notions of national sovereignty.

If one declines national sovereignty, not in legal terms, but in its political context, it is the capacity of organized government within the boundaries of a state to control and mobilize its resources to achieve the then-current definition of its national interest. This is sometimes limited by the power and influence of other states with conflicting interests. Here, too, our ability or willingness to exercise such influence upon other states on behalf of purely economic interests is very limited.

STRENGTHENING THE NEGOTIATING CAPACITY OF THE UNITED STATES

What this Committee recommends must have some achievable reality, and it must lead to a definition of specific objectives and delegation of attendant authority to the Executive to accomplish them. And the starting point must be to bolster our own bargaining position—because without it, no persuasion and no international negotiations will result in any satisfactory agreement.

To this end, we should first straighten out our own thinking on some of the basic issues that define national power, as well as national interests. The word "power" may elicit fearful images of megatonic weapons and death-dealing instrumentalities, but this is not what I have in mind at all—although it must be admitted that even in that area of military capacities we have reached a point of diminishing return and standoff. I have a much more modest concept in mind, namely the ability to bargain peacefully across the negotiating table on a give-and-take basis by exchanging economic advantages. Even in this area our power has been diminishing in several respects.

What are the elements of national economic power in international negotiations? First, and historically foremost, there is the possession of purchasing power abroad which a government can dispense to other countries in exchange for reciprocal favors. We no longer possess this power of granting financial favors or credits or foreign aid because we have not had a net balance of payments credit, not since 1957. In fact, we have been huge borrowers abroad on national, as well as private, account.

It is true that we have investments abroad, but they are owned mostly by *private* individuals and corporations, whereas our *liabilities* are those of the government, and one cannot be offset by the other without requisitioning of foreign investments, as happened in England during and after World War II. The continued balance of payments deficits, created primarily by governmental activities in the military and foreign aid areas, has reduced our financial capacity abroad. The United States now has a debit with the outside world on current account, and has huge accumulated net liquid liabilities as well. Not realizing accurately the causes and appropriate remedies for rectifying this condition the U.S. government has limited the earning capacity of U.S.-based multinational companies by imposing controls on capital exports. The $7 billion or more annual revenue we get from foreign investments is absolutely necessary to sustain our military deployments, to import what we need, to travel where we wish. We should try to increase this source of revenue, instead of undermining its future.

Another source of power is our technology. Coupled with managerial talent, this is the envy of the world. It would be a mistake, however, to think of this as a monopoly. One of the byproducts of the technological revolution in communications and transportation is the easy transferability of technological know-how. As other countries acquire investable surpluses of capital, they will be able to buy the technology they need.

A third source of power that the U.S. government controls is the extensive internal market. Today perhaps this is the most important source of power, but unfortunately it has been eroded in most instances, given away with little or no *quid-pro-quo*, and today under the unconditional-most-favored-nation principle of GATT, this market power is almost an impotent instrumentality in major negotiations, except in a negative way—as when we threaten to withdraw some concession or to depart from MFN principles.

If we are to embark on any major international negotiations for the purpose of improving the economic performance of multinational corporations—in fact, in order to insure freedom for all Americans to spend their money wherever it will bring the greatest return, to travel freely, to consume at will—we must bring these components of our economic bargaining power under control. This means (1) we must bring our external accounts into balance by curtailment of government expenditures abroad; (2) we must increase our earning power abroad from sale of goods, services, and investment income; (3) we must put a price on our technology, whether it is government or privately owned, in order to secure income; and (4) we must restructure our basic trade policy in order to negotiate from strength.

No suggestion concerning freedom of operations of multinational corporations or any other phase of our international activities has a chance of success until these fundamental problems in our international accounts are resolved.

It is futile, I believe, to dream of engaging in a broad range of international negotiations concerning protection of investments. We may achieve something in this field through country-by-country negotiations if we have some reciprocal favors to grant in aid or trade. Our ability to do this, however, is limited because of our balance of payments deficits, our negative commercial trade balance, and the unconditional-most-favored-nation policy.

RECOMMENDED REMEDIES

1. The balance of payments

To bring the balance of payments under control, thereby enabling us to regain possession of our first element of bargaining power, namely purchasing power, I suggest specifically a joint resolution of Congress, which this Committee on its members can initiate, advocating the establishment of an International Security Fund to give practical effect to the principle, already agreed in NATO, that a country's military deployments in the common defense should not penalize it in terms of the balance of payments.

The more complex question of whether certain "budgetary" costs should be included, and the important matter of Japanese sharing of the Pacific defense burdens—perhaps by an "Asian Division" of the Fund—are best left aside for the present, in order not to complicate a simple and direct solution to the problem of offsetting the foreign exchange costs of our European deployment. Making it multilateral should help focus on the common interests involved and reduce the divisiveness of bilateral negotiations.

There are many technical variants, of course, but the simplest would be the establishment by the Fund of a "reserve" of currencies in surplus on the military account on which deficit countries could draw, either to repatriate their own currencies or to pay local currency costs. These would be subscribed annually by surplus countries to the extent that the last year's positive balance on the military account had not been fully offset by military or other incremental sales.

This International Security Fund is certainly as important as sharing foreign aid expenditures, which was the basis for the creation of the International Development Association. If nations are willing to make grants to the International Development Association for 50-year loans to help less developed countries, it is not believable that the U.S. diplomacy cannot sell the idea of an International Security Fund to our allies and Free World friends. This approach is better than selling unneeded arms, better than complete withdrawal, and certainly better all around than driving desperate countries into nuclear armament.

Specifically, there is an opportunity to activate such an International Security Fund as an amendment to or substitution for the Mansfield Resolution concerning troop withdrawals from Europe. In contrast to direct bilateral payments to the United States, this scheme would lift the onus from the U.S. forces of being "paid mercenaries" and from West Germany (and hopefully Japan) the implication of paying for "occupation troops." Such a solution would also remove the balance-of-payments costs as one of the major economic constraints, and allw our deployment decisions to be made on the merits of political and military factors.

In the second place, I recommend strongly that conditions also be attached to contributions made to international aid agencies so as to protect our balance of payments position. Foreign aid is still costing us approximately $700 million a year in balance of payments deficits. Most of this results from the contributions the United States makes to international institutions. With growing emphasis on internationalization of aid, the adverse balance of payments consequences of aid will be aggravated.

Unless we can shore up our balance of payments position and strengthen the dollar, it is going to be difficult to adhere to a liberal trade policy, or expect freedom of capital movements, or secure cooperation from our creditor countries in resolving some of the conflicts of policy and interests.

2. Increasing foreign source income

It is not enough merely to reduce the foreign exchange drain of military expenditures and aid. The United States is in dire need of a set of programs to increase the inflow of funds through expansion of exports, sale of services, and increase of investment income and its repatriation.

It is gratifying that the present Administration has taken cognizance of this problem and has instituted a number of desirable measures, which, although they do not go far enough, are headed in the right direction. The Domestic International Sales Corporation (DISC) idea is a good one. I only wish that it went further and gave definite tax relief instead of the circuitous tax deferral on export earnings. Service income, particularly to encourage travel to the United States, should receive similar consideration. I would definitely recommend that DISC be amended to include at least travel and tourist services, and preferably all foreign source income resulting from the sale of services.

Our ability to sell tourist or engineering services is an important component of our foreign exchange earnings. Whereas, in 1969 the total of exports was in the neighborhood of $36 billion on an f.o.b. basis, our service income was over $8 billion. World competition in the service field is just as fierce as in the commodity area.

Investment income, now in the neighborhood of $6 billion, requires special consideration. Unfortunately, our policies heretofore have been punitive. Instead, we should use the incentive approach and help our industries—these multinational corporations—to earn more on investments abroad and to repatriate their earnings.

To this end, I would suggest, first, that section 5 of the Trading with the Enemy Act be amended, exempting from its application capital movements to our allies. This should dispose of the Office of Foreign Direct Investments, as recommended almost unanimously by the Joint Economic Committee in its March 1970 report on the President's Economic Report.

I would further recommend limiting the application of antitrust laws to situations abroad that *actually* affect the foreign commerce of the united States to a *substantial* degree.

Finally, I would recommend the adoption of the principle of equality of taxation with our competitors abroad, not only in exports, but in foreign production and distribution as well. Our producers are faced with unequal tax burdens in competing in our domestic markets, as well as in foreign countries. Furthermore, our tax laws should encourage repatriation of foreign earnings. We have made extensive recommendations before the Ways and Means Committee to achieve these purposes.

3. Technology: Industrial property rights

The protection of our technology, one of our major assets in bargaining, is a much more complex problem. As a minimum, however, the U.S. government should clarify by legislation the conditions under which the results of government-financed research and development can be made available to other countries. These conditions now vary from department to department and product by product, with a wide range of latitude—at one extreme, public dedication, and at the other extreme, almost exclusive licensing. The results of the $16 billion per year research and development expenditure by the government should prove to be a valuable source of income if carefully husbanded.

In the private field we come inevitably to the protection of patents, copyrights and trademarks. Ever since the establishment of this Republic, the Congress has been resolute in protecting these rights as they apply to our own jurisdiction. In other countries, however, we have been perhaps somewhat less vocal than the importance of the subject merits. The rights of ownership of patents should be defended because these technical frontiers may prove to be more important to our long range welfare than some remote piece of real estate. This is a question of priority in the thinking of our own people and our dealings with other nations. I frankly cannot conceive, however, of a machinery whereby the Congress can impose its views upon our governmental representatives in this area, unless it is done as a part of trade legislation defining the contents of economic negotiations.

4. Trade policy

We come to our most vital negotiating element, an area which is definitely within the specific frame of reference of these hearings, namely trade policy. We must not lose sight of the major and preponderant goal of expanding world trade through reciprocal trade negotiations, which is perhaps the most important contribution to world development that our generation has made since the enunciation of Cordell Hull's farsighted principles, carried out by all our Presidents since 1934. One need not question the validity of the basic philosophy of GATT, however, to suggest that the instrumentalities to achieve its lofty aims may have to be changed to fit new political and economic conditions.

Let us state the objective: how to achieve the greatest possible international economic development and increased flow of commerce at the lowest possible cost, *sans* impediments. In this latter category, I would include not only barriers to intercountry commerce, but all impediments that interfere with the transfer and economical utilization of resources, such as capital controls, expropriation and violation of industrial property rights.

If this is the objective, the next question is what means does the U.S. government possess, or should it create, in order to bargain effectively with other countries to achieve these objectives?

There have been traditionally three basic principles in international trade policy; namely, unconditional-most-favored-nation treatment, reciprocity and national treatment. The United States has, by and large, adhered to all three of these principles. It is not true, however, that other countries have been equally faithful in observing them. The Commonwealth preference system, still tolerated under the grandfather clause of GATT, is a violation of the MFN principle. The EEC itself, and its expansion through new members, associate members, and special agreements is in violation of MFN principles, although in part sanctioned by the GATT.

The Communist world, as a trading partner, will simply not accept reciprocity because they say it is against their constitution. As for the MFN principle, which they wish to be accorded by others, they say they respect it, by *excluding* everybody! They conform to the national treatment principle, too, but there is such a difference in the status of individuals between their countries and ours that there is little solace for us in the promise of equal treatment.

Many countries are violating the national treatment principle, for instance, Japan; and there are ideas circulating in the European Economic Commission concerning favored treatment of locally owned companies. The variable levies on agricultural imports imposed by the EEC, without any compensation, certainly violate the principle of reciprocity. Under force of cricumstances, we, too, find ourselves in the position of increasing nontariff barriers, such as quotas, in order to rectify the results of unsatisfactoy negotiations of the past, but nonetheless in violation of the basic principles of the GATT.

A major proportion of $270 billion or more trade in the world in 1969 was carried on under conditions that violate these pirnciples of liberal trade.

In short, the principles of GATT, and for that matter of the OECD Conventions, are being violated right and left, and the so-called liberal trade policy, which has made a religion of the unconditional-MFN principle, is in shambles.

In large part because of these persistent departures from the reciprocity and national treatment principles and liberal trade policies on the part of other countries, our ability to compete in world markets, and to earn our way through the sale of exports, is sharply diminishing. The result is a persistent deterioration of U. S. commercial trade surplus to a net deficit. This factor, added to our military and foreign aid expenditures, creates a situation which is antithetical to the freedom of movement of goods and capital, which is the very marrow of a multinational enterprise.

How do we find our way back to a policy of expanding rather than restricting the opportunities for trade? We must regain control of access to the U. S. market so that in negotiations we can be more successful in obtaining respect for the principles of MFN, national and reciprocal treatment. We can do this by making access to our market conditional on adherence to these principles, in practice by other countries. But the application of these principles should not be confined merely to matters of commodity movements, but must encompass investments, repatriation of earnings, industrial property rights and other considerations of quantitative economic value. Economic progress is indivisible: trade, investments, property rights, travel, military expenditures and the balance of payments are interdependent.

This may be achieved by an amendment of sections 211 and 251 of the Trade Expansion Act of 1962, as amended, changing section 251 from unconditional to conditional MFN, enumerating the conditions of reciprocity and national treatment in both trade and investments; and expanding the negotiating authority of section 211, now applying only to the European Economic Community, to all nations, common markets, trade blocs and free trade associations.

Because there would be some effects on a number of existing treaties, this would not be a step to take lightly. Unless we are more successful than we have been so far in securing effective reciprocity through multilateral negotiations, this may be the only way to enable the United States to negotiate from a position of strength. It must be kept clearly in mind, however, that although the techniques of negotiation may change, as they are changing in fact, from multilateral to bilateral, the end purpose for which our negotiating strength should be used must remain freer movement of goods and capital on a *reciprocal* basis.

Everyone is fond of pointing out the obvious—that the 1970's are not the 1950's. Yet, in our international economic relationships, the United States still seems to act on the implicit premise that our size and power obligate us to different standards of behavior—and indeed to more self-sacrifice—than other states apply to themselves. There is, of course, some continuing validity to this notion. But, surely, the special situation which prevailed after World War II has now been corrected. In short, I think the United States should serve notice to the world that we feel we have met the special obligations imposed by our relative affluence, that we have problems of our own, and that while we will continue to carry out our basic responsibilities, as in the past, we must seek and expect reciprocal treatment in our economic relationships. Against the background of such a shifting emphasis—if you will, an "economic" version of the "Nixon Doctrine" on defense—it then becomes relevant to look at the specific institutional structure necessary to accomplish this result.

STRUCTURAL CHANGES

The United States appears to me to lack a cohesive machinery for defining our economic interests abroad and for negotiating about them from a position of strength.

1. A council on international economic policy

International economic policy, of course, has critical interrelationships with domestic economic policy on the one hand and international political-military policy on the other. The former area has the Council of Economic Advisers set up by Congress in 1946 to promote "employment, production and purchasing power." The latter area has the National Security Council established by statutes in 1947 to advise the President on "domestic, foreign and military policies relating to the national security."

The third leg of the triangle, international economic policy, is distinguished by its absence.

So we propose that this Committee consider the creation of a Council on International Economic Policy in the Office of the President.

Previous approaches to this problem area have included the Council on Foreign Economic Policy, which the late Clarence Randall chaired during the Eisenhower Administration, a State Department-sponsored "Undersecretaries' Committee," numerous interdepartmental committees and assorted *ad hoc* commissions, the President's Special Representative for Trade Negotiations, and the National Advisory Council on International Monetary and Financial Problems.

The last-named does serve an important coordinating function with respect to U.S. participation in international monetary and financial organizations. But this is still a long way from the overview of our total economic interests abroad and the identification of critical problem areas and long-term trends that I have in mind.

Whether this Council should be an intra-governmental body as an instrument of the administration, like the old Council on Foreign Economic Policy or the present National Advisory Council; whether it should be more of an "experts" group like the CEA; or whether its members should be non-political specialists with long tenure, such as members of the Federal Reserve Board, requires detailed study—as do questions of the Council's relationship to the Cabinet Departments, the NAC, the Special Representative, the NSC and CEA mechanisms. This might be worthy of staff study by this Committee—and indeed could be a profitable subject of inquiry by the Ash Committee which is currently examining government reorganization.

But the point is that the President needs a *full time* focus by talented experts on the critical issues of international economic policy, both for the short run and the long term, *at a level above departmental and interest group attachments.* The information and views of various departments of the government with foreign operations and interests would, of course, be considered by the Council in its recommendations to the President. The President would act on the Council's advice in the light of the views of his responsible Cabinet officers.

However organized and staffed, the Council should, in my view, do three things: First, identify and define our economic *interests* by areas in different parts of the world; second, make recommendations on minimum and maximum *objectives* in international negotiations affecting those interests; and third, prepare a realistic *foreign exchange* budget for the United States, which could analyze this critical and long neglected aspect of our total "costs" in foreign operations. Such a budget could, I am sure, be of great assistance to Congress—and to this Committee in particular—as well as to the President and within the Executive Branch.

2. Comprehensive negotiations

A second structural change in which Congress could take the lead would be the adoption of the principle of bilateral negotiations with nations, common markets, or trading blocs, with the objective of securing MFN, reciprocal and national treatment. This is merely a recognition of conditions as they exist today.

The negotiations should encompass not only matters of trade, but also investments and finance, the balance of payments, military expenditures for peaceful security deployment, foreign aid, protection of industrial property rights and other matters that may be relevant to that particular nation, region or bloc. MFN treatment in trade would be granted on conclusion of a satisfactory agreement which protects U.S. interests in these areas. The less developed countries might be given tariff concessions at least equal to those granted a most-favored nation in return for respect for the principles of reciprocity and national treatment of investments.

I have centered my recommendations on those things that this Congress and our government can do to improve the environment in which international economic relations can be conducted and multinational corporations, as important parts of the whole, can operate. I submit that, in spite of the present confusion of opinion in the United States, these suggestions offer a practical means of creating an environment in which multinational corporations can contribute their full potential to world economic development. However, if we cannot put our own house in order, I see very little hope of achieving international agreements for the rationalization and standardization of economic behavior around the world. And I shudder at the prospect of traveling down the same road in the 1970's that we just came through in the 1960's.

Representative REUSS. We will now hear from Mr. Istel.

STATEMENT OF YVES-ANDRÉ ISTEL, KUHN, LOEB & CO.

Mr. ISTEL. Thank you, Mr. Chairman. The multinational corporation, being discussed in these hearings, is deeply involved in the complex capital flows which are changing the way in which nations relate to each other economically. My basic argument today is a simple one: the importance of these capital flows is still severely underestimated relative to the attention paid to the movement of goods, and this lack of balance could be a major cause of foreign economic policy errors.

We all know that, by our accepted methods of measure, the United States has suffered balance-of-payments deficits of differing annual amounts over an extended period of time. Since 1960 this deficit has now exceeded $25 billion on the "liquidity" basis and $10 billion on the "official reserve transaction basis"; our monetary reserve assets only approximate $16 billion. Yet, over this same period our net international assets have increased by over $10 billion and represented in 1968 over $65 billion, the difference between assets of $146 billion and liabilities of $81 billion.

What is striking, I think, about these figures is two-fold, first, the paradox in trends—how does one increase assets (valued on a cost basis) by running losses?—and, second, the difference in magnitudes—the small size of our gold stock compared with those of our other gross or net assets.

It seems clear that our most commonly accepted measuring devices are no longer appropriate to our rapidly changing world and that the obsolescence in this area mirrors a lag in perspective on international economic intercourse.

If there is some truth in these observations, one is entitled to ask what has been happening and what it may imply in terms of policy.

One of the main reasons for the paradox cited above is that the undistributed cash flow of our multinational corporations operating outside the United States is not reflected in any balance-of-payments flows, only dividends when these are paid by the subsidiaries to the U.S. parent. The figures, of course, that I have mentioned on private foreign direct investment are probably very considerably understated, since they are book value figures. The "true" value is probably at least twice as great.

This applies as well, of course, to private investment by foreigners in U.S. assets but the mix is very different. While U.S.-owned direct investment exceeds $65 billion (at book), the reverse comparable figure is around $11 billion. Foreigners also own some $20 billion of U.S. equities (at cost) but the degree of under valuation is probably much less than for direct investment, particularly after the recent stock market decline.

One should also note, however, the geographical distribution of U.S. investments which indicates that we may have a net debtor position (on a cost basis, to be sure) in Western Europe, which is more than compensated for by our net creditor position elsewhere.

In addition, of course, we have seen a multitude of capital flows of varying nature that are either assimilated all into one category or arbitrarily divided into different categories, making them look fundamentally different when in fact, they may be quite similar. The purchase of marketable securities—U.S. equities for example—is lumped as a long-term capital flow with the funds expended for the building of a factory, which may well not be salable in any practical sense. On the other hand, the purchase of a 15-month Treasury note by a non-U.S. person is considered a long-term capital inflow, while the purchase of an 11-month Treasury bill increases the deficit, on the liquidity basis.

This confusion is not surprising because we are dealing with an international payments system designed largely—in terms of its reserve components and consequent adjustment procedures—in the early post-war years when trade between nations meant goods and services. It was natural then that when a nation's goods and services became overpriced in world markets, it should incur a deficit that would force it to follow an internal economic policy designed to demedy the situation. It was natural then, also, for the international reserve system to accommodate only "temporary" imbalances before forcing change. The system worked in good part because for all the world's major nations (except the United States) foreign trade was a sufficiently large component of their national product that it was economically critical and thus politically feasible for them to endure the disciplines of the system. The United States, of course, had a unique role.

When the United States did run into balance-of-payments difficulties it was able to finance through the private sector the outflows of the public sector. Restrictions on capital outflow—the interest equalization tax, and voluntary, then mandatory guidelines on foreign direct investment—did not prevent, for a while at least, the continuing accumulation of net private assets abroad. Then the emergence of the Eurodollar provided the first real non-U.S. unrestricted money market, perhaps now $40 billion in size, and the Eurobonds, or international capital market, provided the first sizeable unrestricted (at the source of issue anyway) capital market. This was on a rapidly rising scale of magnitude (from $1 billion in 1964–65 to over $3 billion in 1968 and 1969), but still quite small relative to the savings and financing of the internal markets of the major Western nations and Japan. In addition, however, large amounts of money have flowed into U.S. equities both directly and through "offshore" mutual funds.

The international capital market has evolved from an isolated market operating at the periphery of the national markets to a market which links and extends the national capital markets. This evolution is substantially, there arose great ingenuity as to techniques and a much attributable in part to necessity—as financing needs increased very wider net of distribution through larger and more informed syndicates—and in part to the limited possibilities of national markets. This evolution has been speeded up by the emergence of international investment trusts with sophisticated investment managers looking for interesting opportunities wherever they may exist. The flows of money into Japanese equities, both directly and through specialized investment trusts, and the success of large equity-linked issues for European companies such as Bayer, Badische, and Michelin attest to this new attitude.

This trend has some far-reaching implications. It is one more factor forcing many multinational companies to be profitable and growth-oriented, for those are the companies that will have preferred access to capital in a world where it is no longer an abundant commodity. American corporations were initially favored—not only because they generally had better growth prospects and rates of return but because the American stock market had so much greater breadth and selection. This aspect—the reward to the efficient, both industrial and financial—should perhaps be particularly emphasized at a time when Europe rushes toward bigness, sometimes with success, but often without. There are more and more governmental comments about the need for mergers within frontiers—to be then perhaps followed by agreements with foreign corporations—while the need for effective management is often sadly underestimated. I would guess that there will be an increasing shortage of good "Euro-managers," and that the effective multinational corporations will be favored by being able to offer more attractive financial and intellectual remuneration.

In recent months the combination of liquidity pressures in the U.S. market and the restrictions which have forced extensive borrowings by the subsidiaries of U.S. companies has probably resulted in a reversal of the favored U.S. position. It may well now be easier for the efficient non-U.S. multinational corporation to have access to capital and people than for its comparable U.S. counterpart.

No European exchange is close in size to the American, but the international capital market is gradually—still very gradually—evolving into a useful supplement and substitute. As European companies increase their capital, they will surely distribute shares more and more outside their own country. If the U.S. market has trouble from time to time absorbing the needs of its own largest corporations (virtually all multinational, by the way), the same holds all the more true in Europe. The international capital market can perhaps be viewed as the market which arose in part because multinational companies needed it, especially those based outside the United States.

Now, there is no doubt that the operations of multinational corporations of this international capital market have contributed to the volatility of increasingly large capital flows but it has also spawned very substantial balancing or equilibrating flows. The heavy long-term borrowings by the United States and the United Kingdom (both deficit countries), the lending then borrowing by Italy, and the immense recent lending by Germany (a major surplus country) are all sizeable examples of such balancing capital flows.

In the last few years it is probable that the sharp increase in U.S. private borrowing overseas, in these markets, may have halted, or nearly halted, the growth in the U.S. net investor position. In any case, the balance sheet has become heavier on both sides and the problem of weighing long-term assets against shorter term liabilities has arisen.

The Penn Central is a recent case where substantial long-term assets permitted incurring excessive short-term liabilities; sufficiently persistent losses, and perhaps poor management, then caused the short-term lenders to lose confidence. There is enough similarity between this and the present U.S. position to cause at least some mild anxiety in many quarters.

The problem is clearly compounded by the two-edged nature of many dollar transactions and flows. A Eurodollar deposit can be a convenience one minute and a potential dollar outflow the next, if the depositor for any of a series of reasons would prefer a deutsche mark or Swiss franc deposit. Since most central banks would like to avoid a further large accumulation of dollars, the Eurodollar and Eurobond markets have provided an attractive—and necessary—medium for keeping dollars in private hands.

The dollars can be made to stay in the dollar currency if the central banks—through swaps and other similar arrangements—are willing to do so, but if the flows become too large they are unlikely to do so. Viewed in this way the capital pools represented by the Eurodollar and Eurobond markets and the foreign holdings of U.S. securities are a sort of sword of Damocles suspended over the current dollar value by the thread of confidence.

Many Europeans have, as we all know, long resented the de facto dollar standard in world trade and finance, remarking that this has permitted the United States to have, or finance, deficits where others could not and that the linkages with their national markets have become so pronounced that their national economic sovereignty is imperiled, that in fact the U.S. rate of inflation becomes theirs. While this stance points to a genuine problem, the solution advanced in the past by European spokesmen for our balance-of-payments woes have eventually been adopted but with results perversely different than expected. When—just a few long years ago—our interest rate structure was lower than in Europe, it was suggested that higher U.S. rates would help attract funds and tend to reduce inflation here: the recent sharp rise in U.S. rates may be helping these objectives but their consequence—raising European rates even higher—has not been particularly appreciated. In this same period, U.S. industry was being denounced for buying up European companies with low-cost U.S. funds. When restrictions were placed on such capital outflows, U.S. companies borrowed the funds in Europe and in fact preempted, at least for a time, a large part of this market, which again delighted no one in Europe. Today, there is alarm at our short-term debts. If, however, we were to move more aggressively to turn our long-term assets into liquid assets (for example, by selling to Europeans a part of IBM World Trade, or other major U.S. company foreign subsidiaries), the impact on their capital markets would be severe and, again, not appreciated.

These comments are not meant to obviate well-founded criticisms, but are meant to suggest that the solutions the Europeans proposed also reflected, as did our own moves during this period, their own past experience in dealing with such matters rather than perhaps the full reality of our present world.

The next question is what we should do now that would properly reflect the new role of the multinational corporation and the at least partially related capital flows.

There is general unanimity that the first step is to restore more confidence in the dollar by reducing inflation at home; this is fortunately a major goal of our present domestic policy. There are also some serious discussions about greater exchange parity flexibility and about a tougher trade stance—two large subjects beyond the scope of these remarks.

Reducing inflation is devoutly to be wished on many domestic grounds and success in this respect would satisfy many of our European critics. We should not, however, let the general acceptability of this solution force us to accept the trade-oriented mentality it implies. Over a longer period of time, I am suggesting, a sound dollar will not just be the product of more competitively priced goods (though this is very important right now), but of a currency which must be free of capital as well as trade restrictions, so that it can play its inevitable role in world commerce for many years to come. The dollar role may well be a declining role, relatively (and this is constructive) but it will be a critical role nonetheless. We must, at the earliest opportunity, dismantle our own capital controls.

The policies which are adopted should reflect the complex interaction which now exists between trade and capital flows. The "perverse" relationship between trade and capital balances—when one increases the other tends to decrease—and vice versa—has been noted for some time. The practical implication is that in any given situation of balance-of-payments excessive surplus or deficit, a properly balanced policy mix should be applied. In the past—because of a trade-oriented history, the emergence of GATT, et cetera—the usual deficit reflex has been to restrict capital flows first and trade last. Similarly, when pressing for improvements in trade restrictions, such as reduction of nontariff barriers, it might be well to press equally for freer capital flows—starting at home. If we want to live comfortably with our neighbors, in the face of the de facto dollar standard and the predominant direct investment of the United States, we should obviously work much harder than we have been to encourage direct investment in the United States.

Like the United Kingdom at the turn of the century, the United States has been playing the useful and dangerous role of world banker. Both the United Kingdom and the United States incurred "deficits" in the usual balance-of-payments terms while accumulating very large and valuable foreign net assets.

The major Western nations, plus Japan, have a very large combined investment, both direct and through loans, in the less developed areas. It is probable that the industrialized world as a whole will thus have to run a very large balance-of-trade deficit to provide the less developed countries—LDC's—with the financial means of servicing their capital obligations, for the alternative is either a higher and more successful capital inflow into the LDC's than is now projected or an inability by the LDC's to service their debts and the foreign direct investment they have received.

The future policies implied by this last point will admittedly have to be taken on a multilateral basis, but we should be prepared to support and even lead this policy. I think it is important to note that the whole Western industrialized world will probably have to accept the notion of at least balance-of-trade deficits vis-a-vis the third world and perhaps over all balance-of-payments deficit vis-a-vis the third world for a long time.

Now, there are also some policies we can support unilaterally:

A pragmatic view of balance-of-payments problems to yield a better balanced and integrated policy between capital and trade movements;

A prompt—very early—removal of our capital restrictions combined with efforts to obtain similar concessions in other nations;

A more realistic view of our role in world commerce—not just in world trade—reflected in balance-of-payments statistics that should always include a balance sheet approach and a clear Government-private division as a supplement to the usual balance-of-payments "flow" figures.

Thank you.

Representative REUSS. Thank you very much, Mr. Istel.

Mr. Rolfe?

STATEMENT OF SIDNEY E. ROLFE, PROFESSOR OF ECONOMICS, LONG ISLAND UNIVERSITY

Mr. ROLFE. Thank you, Mr. Chairman, members of the subcommittee. I much appreciate the opportunity to be here, and thank you. In preparing this testimony I read the hearings of December 2–4, 1969, of this subcommittee. The wide-ranging views expressed there stand as tribute to both the subcommittee in encouraging the freest possible environment for expression, and to its staff. I would like to take advantage of this free atmosphere to make some modest proposals with respect to the balance-of-payments presentation, which I think this subcommittee may be uniquely able to consider and perhaps act upon.

Most students of the multinational corporate phenomenon work from a limited, usually the same, body of data. And all agree more data are needed. Nevertheless, widely divergent views flow from the data. It must follow that what is lacking is an accepted perspective view. Perhaps a universally accepted perspective is too much to ask, for when logical men differ from given—if meager—data, political or idiological differences are what are really being displayed. And those differences, as we know, are not easily dismissed.

The December hearings provided many of the inputs a perspective requires. I do not wish to reiterate, but only to emphasize a few which lead to the financial ramifications, the subject today. One point which emerges quite clearly to me is that the United States, and other countries as well, are at least 10 years out of date in their vision of the emerging international economy; all try to cut the surge of international activity, particularly direct investment, to fit the mold of their thinking and their accountkeeping. This procrustean effort gives rise to most of the friction; it is the mold, not the reality responding to new technologies, and new abilities to act on them, which must change.

Mr. Arthur Watson's point that, in computer language, this is a system is essential. Put on a historic axis, in the decades just before and after World War II, the world was still much more akin to the 19th century than it is today. Goods moved. Factors of production did not. With few exceptions, the economic area and the nation-state were coterminous. Foreign direct investment there was, of course, but mainly for oil and extraction; the U.S. total was some $7.5 billion in 1929 and only $7.2 billion in 1945. It was still in the main a world of exports and imports. Trade policy, the balance-of-payments system, the care with which GATT was nurtured when no similar arrangement for free capital flows existed, the IMF provisos, all reflect this perspective.

From the late 1950's, however, with convertibility and the Common Market, qualitative changes emerged. The factors of production—in the form of direct investment began to move extensively, especially in manufacturing and within the developed world, contra the past. They will continue to do so. The "internationalization of production" through the vehicle of the international corporation is now the major channel of international economic relations. I would refer to a 1968 OECD estimate made for the year 1966 which found the book value of direct investment abroad from all advanced countries to be some $90 billion; of this, the United States accounted for $55 billion, a portion not wholly out of line with its relative GNP. The output associated with this $90 billion investment, and some intracorporate portfolio "stakes" was probably about $250 billion per year; this figure was in 1966 nearly double the combined exports of all the advanced countries. Direct investment was larger, had grown faster, and promises to do so in the decade ahead, than exports. If the American challenge captured the journalistic and hence, popular imagination, these data suggest the challenge is really international. And in the decade ahead, the great outpouring of plant and equipment investment abroad is more apt to originate from Japan and Western Europe—especially if the Common Market can find its way to a common company law, or at least tax harmonization to unblock transnational mergers now in the works. A good part of that, parenthetically, will be in the United States; foreign direct investment in this country has risen to $11 billion in 1968, from $9 billion only 2 years earlier.

The international movement of the corporations is, as Professor Cooper noted in December, a recapitulation and a further geographic extension of the spread of the national corporations in the United States in the earlier decades of this century; and, he might have added, in Germany and elsewhere from regional to national corporate scope. The State of Michigan and the Confederation of the Rhine as effective economic units died in the shuffle.

Today, whole nations are threatened with obsolescence as industry expands, without reference to national borders. But as the international corporation promotes economic efficiency and integration, it raises new problems of sovereignty and national controls. This great thorn amongst the roses was faced by Professor Vernon, who instructed the committee on the art of multinationalizing the political response.

The vision for the 1970's, I think, must include these factors and more. I will not labor this perspective further. But it may be instructive to see how an international group of business leaders, meeting in Washington in May 1969 to consider the problems of direct investment, saw the problem. Their findings have been published and I attach their recommendations.

(The recommendations referred to follow:)

[Excerpt from "The Multinational Corporation in the World Economy," Rolfe and Damm (ed.), Praeger, N.Y., 1970]

RECOMMENDATIONS

On the basis of the background papers and discussion presented at the Conference on Direct Investment in the Atlantic Area (Chapters 1–6), the conference recognized that a new world economy is taking shape largely as the result of a trend toward the internationalization of production.

The volume of goods and services resulting from international investment has bypassed exports, and its present growth rate is considerably larger than that of international trade, thus making international investment the major channel of international economic relations. The international corporation is the main expression of this unprecedented phenomenon. Investment across national boundaries is largely a reflection of the development of technology, and affects every facet of the established order—financial, cultural, and political.

The economic consequences of foreign direct investment are held almost universally to be beneficial. The process expands the total of world investment and production. It is a strong factor for economic integration and brings about a better allocation of resources throughout the developed world.

But as international investment solves old problems, it raises new ones. Significant obstacles of a psychological, political, or economic nature exist, limiting or distorting the international investment procedure.

THE ROLE OF INTERNATIONAL CORPORATIONS

The conference discussed what the international corporations and the governments might do in order to reduce a number of these obstacles. Its recommendations on four basic areas are stated below.

First, the international corporations have to take full account of the policies, conditions, and aspirations of each country in which they are established. To do so is an essential of good management. The fears that exist in some countries about these corporations can best be allayed by better disclosure and publicity of corporate activity, including financial data, and by a greater effort in explaining the corporation's long-range goals, policies, and involvement in each nation's life.

Second, it is desirable that the governments of the Atlantic nations and Japan should take action to remove, in the most liberal and effective way, those obstacles which hamper transnational direct investment and develop rules of good behavior for both base and host countries to avoid the use of international corporations as instruments of national political policies by base countries and to avoid discrimination by host countries inconsistent with a reasonable exercise of national sovereignty.

The conference recommended to their respective governments full support of the principle of an international code under international sponsorship, including a reasonable statement of the obligation of investors and of host and base countries.

The focus of interest in the conference was on direct investment. However, the conference was aware that trade policy, customs barriers, the use of artificial incentives, monetary policy, financial integration, double taxation of corporate income, and other related factors were inseparable from the problem of direct investment in formulating government policy. These problems cannot be solved unilaterally, or even bilaterally, but only in a multinational framework.

Third, the conference concluded that the international capital market could no longer be regarded only as a substitute market and should be regarded as permanent. The recognition of that fact by governments, monetary authorities, and others would tend to keep the market free from unilateral interference taken without full consideration of the impact of any one nation's action on that market. Appropriate procedures should be developed, as a matter of urgency, to encourage multilateral discussion to assure maximum freedom of international capital flows.

Finally, the international capital market has grown without government surveillance. The conference recommended that the responsible banks and issuing houses exercise necessary care in order to ensure that it can continue to function in this way.

EUROPEAN INVESTMENT IN THE UNITED STATES

The conference dedicated particular attention to European direct investment in the United States. It felt that such transactions are highly beneficial both to the United States and to Europe in economic terms, and may, in the short run, contribute to the balance-of-payments adjustment process. The overriding motive for investment is the existence of a vast, dynamic, and sophisticated U.S. market. The conference also felt that direct investment in the U.S. by European companies would tend to balance the reactions against U.S. investment in Europe. Obstacles to investment in this market do exist, and to reduce them the following recommendations to the U.S. Government were made.

First, visa regulations should be eased to avoid the difficulties which currently arise in the employment and utilization of noncitizen management and technical personnel. Modification of the Selective Service System to exempt foreign personnel at work temporarily (up to five years) in the United States was urged.

Second, legal insecurity which stems from the action of U.S. antitrust enforcement authorities should be diminished. The conference concluded that great restraint should be used in extraterritorial application of the antitrust laws. The business review procedures of the antitrust enforcement authorities should be improved. Decisions should be rendered promptly and should be binding over a reasonable length of time. It is recommended that a clear statement of antitrust policy and the principles guiding its application be made available by the competent authorities.

Third, tax regulations should be amended to eliminate discriminatory taxation on those coparticipations in which U.S. companies own less than 80 per cent. The current law permits the filing of a consolidated return only when U.S. participation is 80 per cent or more. This inhibits a more equal distribution of the capital between the U.S. and foreign investors and thus tends to inhibit investment.

Fourth, the conference recognized and approved the stated intention of the present Administration to reduce and eventually remove the Interest Equalization Tax, as soon as conditions permit. In the meantime, consideration should be given to freeing from that tax issues and/or borrowings in the United States by non-U.S. corporations, if the proceeds are used in the United States for direct-investment purposes. Transactions of this kind should be clearly identifiable as such.

Fifth, after taking into consideration the usefulness of the presence of foreign banks in the United States to enhance the environment for direct investment from abroad, the conference recommended that U.S. banking laws be reviewed in order to encourage and facilitate the establishment and operation of foreign bank branches or subsidiaries. In this respect, it is also recommended that the One Bank Holding Act, if enacted, take cognizance of the special position of foreign banks having subsidiaries in the United States.

Two recommendations were directed to European governments: First, all efforts to bring about stronger economic, financial, and market integration in Europe should be actively encouraged. The European nations should take such steps as are necessary to eliminate the barriers to transnational mergers, to allow European companies to reach dimensions to become more effective competitors in the expanded world markets, and to make international direct investments. Second, certain tax reforms are desirable: Among others, foreign direct-investment income should not be penalized by the use of discriminatory tax legislation in the country of the parent.

Mr. ROLFE. However, if I may go back to the financial problems, a higher significant part of the system is financial. Mr. Watson admonished you in December that trade problems are in fact symptoms of monetary problems. And Professor Cooper, in vivid understatement, said that balance-of-payments considerations "intrude" on trade and investment policy. When in doubt, virtually all nations—the United States included—have rushed to investment controls. And in the United States and United Kingdom, this capital-control response came despite the fact that returns on foreign investment have been pillars on the surplus side of the balance of payments. Like the United Kingdom, we are willing to admit theoretically the long-term value to the national accounts of direct investment. But we would and did sacrifice this value to the short-term advantage of a 1-year cash surplus resulting from capital-outflow controls. The Eurodollar markets constitute a vast extenuating circumstance for U.S. controls. For through it, U.S. corporations—far more than British—have been able to be at once controlled at home and expanding abroad. And at least during the great bull market through 1968, the use of convertibles permitted financing at a lower cost than straight bond issues would have borne in the United States.

Given a resumption of improved share market expectations, this could well happen again, since the stocks of European holdings of U.S. shares seem still to be below saturation. The flows of capital may thus still take the form of convertibles to a greater extent than would be the case in the United States, where the demand for equity holdings is not growing as fast.

The Eurodollar markets are in fact the major financial manifestation of the systems approach to the new international economy. The unique characteristics of the Eurodollar market argue for its longevity. Those characteristics include its ability to move between the cracks of the numerous capital market controls that still assail Europe and the United States despite the numerous OECD, EEC, and private schemes and plans for reform:[1] It is indeed one of the few free markets in the world. They also include the market's efficiency, its breadth, convenience, relatively low charge structure. To be sure, all of these features could be improved, particularly effective secondary markets. But in an imperfect world where all things could be improved, these are cavils.

Second, the appearance of a very strong bloc currency—a real Euromoney—would reduce the dollar's dominance, as the mark and a few strong currencies—none large enough to replace the dollar—have already dented that dominance. But Euromoney is still a way off if indeed it ever sees light: the fate of "unit of account" bonds indicates some of the difficulties of dethroning the dollar.

Indeed, if Euromoney does not appear, and European companies do, they are apt to do much of their financing in the Eurodollar markets, dominating in dollars more often than not. The Eurodollar market's chief beneficiaries are already non-U.S. entities, corporate and parastatal and municipal. This trend is apt to grow.

The net result of all this is to create for the dollar a vehicle currency role of vast and unexpected proportion.[2]

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[1] S. E. Rolfe, "Capital Markets in Atlantic Economic Relationships," Atlantic Institute (Paris, 1967).

[2] "The Euro-Dollar Market: An Interpretation" by Alexander K. Swoboda, Essays in International Finance, No. 64, February 1968 International Finance Section, Princeton University, Princeton, N.J., USA.

Stimulated in large measure by U.S. regulations—the interest-equalization tax, and the voluntary-turned-mandatory capital controls for corporations, et cetera—fed by the supply of deficit dollars, sustained by the demand for the dollar as a relatively safe vehicle, the Eurodollar market is perhaps the greatest testament to the systems approach. The system requires a view broader than the export-surplus nation-limit which once sufficed as purview; more important, the system virtually guarantees that for each ponderous national control, the market will find an international loophole.

The Eurodollar market is a halfway-house, a short-run response, to the ultimate need for an international monetary mechanism for the developed world. The end of the road must be an international bank. This end may be a way off. Not only would the surrender of sovereignty in multinational agreements be required to set up and run such an OECD-nation bank, but developed-nation monetary and growth policies would need to be coordinated—more nearly unified—as a precondition. And this is surely a way off. In the interim, the Eurodollar market, assisted by ad hocery like the Basle agreement of 1961 will have to do.

American lawmakers should be, for the present, primarily concerned, I think, with maintaining confidence in the dollar, to permit it to play its vehicle role effectively. Confidence is compounded of many factors. Doubtless the most important is the rate of inflation. The current relative confidence in the dollar—I emphasize "relative"—reflects the world's belief that inflation is, if not quite in hand, certainly not out of hand in the United States. And certainly, this committee has had its full share of fiscal and money supply anti-inflationary advice, so that those labyrinths need be explored no further.

But confidence may also be helped, as it is in my opinion now hindered, by balance-of-payments statistics. These data, which are dreary stuff per se, are the data most used for present and future policy judgments. This is not only so for governments, but also for journalists, legislators, bankers, investors, and international corporate treasurers—half of dozen of whom can collectively make a run on virtually any currency. Yet, seen historically, balance-of-payments data are a relatively new phenomenon, having taken their present shape half a dozen years on either side of the Bretton Woods agreement. It has been amply demonstrated that economic conditions, notably but not only the vast importance of capital flows in the accounts, have changed substantially since. It is time the presentation of the data were reviewed and changed as well.

Disquietude about the balance-of-payments system abounds. Let me appeal to a few authorities.

William Butler, vice president and chief economist at the Chase Manhattan Bank, recently wrote:

> Balance of payments statistics are not only confusing—they can be highly misleading. For example, as much as half of last year's large deficit on the liquidity basis represented flow of American money into the Eurodollar market and back to the United States. The statistics report the outflow but do not count the return flow.[3]

[3] William F. Butler, "The Future of the Eurodollar Market—An American View." (Mimeo).

Parenthetically a criticism of the system offered by Professor Kindleberger, while less immediate, is also relevant.

And as the "deficit" country is not really in deficit in the two senses of that word, neither failing to add to its net worth, as in the case of a household in deficit, nor losing reserves in the case of a bank—assuming that the other countries understand the financial intermediation process and it is not carried to excess—so the "surplus" country which borrows for liquidity is not really in surplus.[4]

In both the United States and the United Kingdom, critics have noted a contradiction with respect to the asset position of those nations which Mr. Istel just alluded to. During 1962–68, when the pound was pilloried and devalued after serious runs, the external assets of the United Kingdom continued to grow. Partly to rectify this contradiction the Bank of England began to report[5] periodically the balance of payments not simply as an income statement, reflecting current flows, but also as something resembling a balance sheet, reflecting both liabilities and assets of the Nation. To be sure, assets held by virtue of direct foreign investment continued to be at book value. The Reddaway report estimated the market value of those assets to be 15 to 40 percent greater, averaging about 32 percent. But this refinement is yet to come. Her Majesty's Treasury also attempted, in a review of the 1969 balance of payments issued on March 9, 1970,[6] to take a more realistic view of capital flows as well. Noting the old—and still practiced—distinction between "long" and "short"' term flows (1 year or less) the report states "such a distinction based on the characteristics of assets has become increasingly unrealistic." The report attempts to improve the approach.

In the United States as well, some move is afoot to add a balance sheet approach to the system. The "Survey of Current Business" for October 1969 for example, present such an analysis.

In commonsense terms, no corporation could claim to know its position simply by an examination of current sales and expenses. And the Swiss banker who looks askance at the dollar (or pound) will admit the picture improves when real assets—preferably at market valuations—are included in the calculus. Indeed, this is the great strength of the U.S. position. Butler estimates U.S. foreign assets at net $50 billion. Of course, asset values (book) can be ferreted out of the balance of payments by diligent restructuring. But few economists and precious few journalists or bankers go through this painful exercise.

In conclusion, a few suggestions for a different presentation of the accounts are offered. It is not the scope of the Congress to go greatly into detail, nor do these suggestions. But were the decision to be taken to review and possibly change the presentation of the accounts, and thereby enhance confidence in the dollar, the United States is blessed with an abundance of able economists and analysts who would doubtless do the job. Nor would a new presentation obviate the need for other reforms. Wider bans or preferably a crawling peg are much needed in any event. Mr. Watson's December testimony that business can live with this system, that is, crawling pegs, indeed would prefer

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[4] C. P. Kindleberger, "International Policies for the Coordination of Growth," Ditchley Foundation, 1968 (mimeo).
[5] Cf. Bank of England Quarterly Report, December 1969.
[6] H. M. Treasury, mimeo, Mar. 9, 1970.

it, is relevant. The need for additional liquidity may also still persist, even with SDR's. And even if, as some argue, the effective demonetization of gold puts the world on a dollar standard, and force revaluations of strong currencies rather than dollar devaluation, the need for better presentation continues. Some suggested reforms would include:

(*a*) A statement of assets and liabilities—a balance sheet approach—should be added to the present income statement. Various aspects of this are discussed above. In summary, a realistic approach to long-term assets should be developed, to include estimated market as well as book valuation of direct investment. Offsetting liabilities should be more carefully analyzed. The long-short term question, and the failure to double entry certain short-term movements to which the Butler quote alludes, should be more aptly handled. The point of the exercise is, of course, to highlight rather than hide the underlying asset strength of the United States. Even if these assets have been acquired as a quid pro quo for gold, or with Europe's own money, as Gaullists use to charge, the assets are nevertheless real, income-producing, in the main intelligently selected, heavily net plus, and in short very valuable. This should be made clear. I should like to depart again from this text and say that I came back from Europe yesterday and when one testifies he ought to probably get back earlier and check with your colleagues. I think Judd Polk has prepared just the kind of summary balance sheets I am talking about, in his testimony earlier.

(*b*) The current "income statement" approach can be regrouped for greater clarity.

(1) Private transactions should be quite clearly separated from public transactions. The United States and United Kingdom deficits almost wholly arise in the public sector. These are then offset by surpluses in the private sector; and if they cannot be offset, a net deficit ensues. What is in fact at issue here is a policy trade-off. If it were clearly recognized that aid and particularly military expenditure policy is the source of the deficit we would still need to make a number of alternative policy judgments, but make them more intelligently.

The usual argument against this procedure is that the accounts are inextricably mixed. An expenditure deficit results in an export surplus as goods are shipped. No doubt this is the present sequence of events, but it does not rule out separate and clearer reporting. And if the decision is made to reduce public foreign expenditure, hence the deficit, it does not follow as night the day, that exports would fall in exact reflection. Some present recipients (including surplus nations) would use foreign exchange to purchase, others might not, et cetera. In any event, the source of the problem would be bared.

(2) Within the private sector there should be a very much clearer separation of capital and trade movements.

(3) Capital movements are particularly important. They are now many times their former size, absolutely and relatively. Gross capital inflows to the United States in the first half of 1968, for example, were 67 percent of exports; in 1964 they had been 31 percent. And even if 1968 is abnormal, by virtue of heavy purchases of American securities, the accretion has been steady.

At least two clearer distinctions are required. First, direct and portfolio movements (in and out) should be distinguished. Mr. Watson's estimate that return on private direct investment plus royalties, et cetera, will be some $11 billion per annum by 1975 emphasizes the unique and new structural position of this item in the accounts, requiring some new views.

Second, the long- and short-term flows, mainly in the portfolio area, require much more sophisticated treatment. Some elements of complaint have been cited above, and this is a subject worth a fuller hearing per se.

Representative REUSS. Thank you, Mr. Rolfe.

Before calling on Mr. Stobaugh, I should say that I have to make an appearance before the Rules Committee, so I am going to leave affairs in the capable hands of Mr. Rashish. I will be back.

Would you now proceed, Mr. Stobaugh.

STATEMENT OF ROBERT STOBAUGH, ASSOCIATE PROFESSOR OF BUSINESS ADMINISTRATION, HARVARD UNIVERSITY GRADUATE SCHOOL OF BUSINESS ADMINISTRATION

Mr. STOBAUGH. Thank you, Mr. Chairman.

Mr. Chairman and member of the committee, since the topic under discussion today concerns a broad spectrum of subjects. I thought it best to outline what I am going to cover. First, I will discuss balance of payments and some other economic effects of multinational enterprises. Following that I will turn to financial flows within a multinational enterprise system and their possible use to thwart governmental economic plans. Finally I will draw some conclusions about the future and suggest areas of possible improvement for U.S. economic policy. Much of this statement is drawn from my Harvard research into the activities of the approximately 200 relatively large U.S. firms that account for about 80 percent of U.S. foreign direct investment.[1]

I. BALANCE OF PAYMENTS

The trade, payments, and other financial consequences of U.S.-based multinational enterprises very often are considered in terms of their effects on the balance of payments of the United States and the balance of payments of the host country; that is, the country receiving the investment. A number of econometric models purporting to show these results have been prepared.[2] Unfortunately, at present, no econometric model exists that can tell us with reasonable certainty these effects. Not only that, no econometric model exists that can even tell us with reasonable certainty whether the net effect on either country's balance of payments is positive or negative.[3] This lack of predictive power

[1] This research is part of the Ford Foundation-Harvard Business School research project, "The Multinational Enterprise and the Nation State," coordinated by Prof. Raymond Vernon. My partners on the study of financial management of multinational enterprises are Prof. Sidney Robbins of Columbia University and Assistant Prof. Daniel Schydlowsky of Harvard University.

[2] Probably the best known and certainly the most sophisticated U.S. study is that by G. C. Hufbauer and F. M. Adler, "Overseas Manufacturing Investment and the Balance of Payments," Tax Policy Research Study No. 1, U.S. Treasury, Washington, 1968.

[3] This is an extremely brief discussion of the problems encountered in balance-of-payments studies. For a more detailed discussion, see Raymond Vernon, "U.S. Controls on Foreign Direct Investment—A Reevaluation" (New York: Financial Executives Research Foundation, 1969).

results from the fact that the predictions of any econometric model depend on several critical assumptions, and in the case of balance-of-payments models there is considerable controversy as to what the assumptions should be. This is especially true for those assumptions concerning trade, because the trade consequences of foreign direct investment are highly uncertain but are considerably larger than financial flows, such as the initial investment and the repatriation of funds.

One of the most critical assumptions concerning trade flows is whether the U.S. firm must make the foreign investment in order to serve the foreign market or whether the U.S. firm has the option of serving the foreign market from existing facilities, usually assumed to be in the United States. It if is assumed that the U.S. firm must make the investment in order to serve the market, then the econometric models usually show that the foreign direct investment helps the U.S. balance of payments; conversely, if it is assumed that the U.S. firm could have supplied the foreign market from its U.S. plant but chose instead to build a foreign plant, then the econometric models tend to show a negative effect on the U.S. balance of payments.

In my judgment, the appropriate assumption to be used is that most U.S. foreign direct investment takes place because an investment in the United States will not enable the firm to serve the market in question—in terms of manufacturing, the situation typically is that the firm must invest in a foreign country in order to serve the market in that country, although in some cases the foreign investment is made so that the firm can retain its U.S. market. I have a number of reasons for this belief.

First, I do not believe the popular notion that multinational enterprises are firms without a country, run by a group of top executives of various nationalities who systematically screen the world for investment opportunities and show no preference for any home country as a plant location—simply because the enterprise has no home country. Contrary to this popular notion, the overwhelming majority of U.S.-based multinational enterprises—and these are the majority of the world's multinational enterprises—are fundamentally U.S. corporations, managed by U.S. citizens. Granted, in many multinational enterprises most of the executives abroad are not U.S. citizens; but in virtually all U.S.-based firms the decision to build production facilities is made in the home office, and these home office decisions are made predominately by U.S. managers who must provide dollars for dividend payments. This need for dollars encourages U.S. managers to prefer to serve foreign markets from the United States because of currency risks. Political risks as well as increased uncertainty and greater communication problems in investing abroad are further incentives for prefering U.S. investments. As a result, the majority of U.S. firms require a higher projected return on investment for foreign investments than for those in the United States; furthermore, in those firms whose stated policy is not to require a premium on the return from a foreign investment, many of the individual managers still require a premium on foreign projects before they approve the project and pass it to a higher authority

My study of the chemical industry as well as a number of case studies in other industries reinforces my belief that most U.S. foreign investments are made to serve markets that cannot be served through investment in U.S. plants. In my study of a sample of representative chemicals, I did not find one case within a period of 60 years where a foreign direct investment was made until and unless there was some competition in the manufacture of the product; in other words, the original producer always built the first plant in his own home country and always supplied the world market from this plant until a competitor started production. A Harvard Business School case on how one of the giant U.S. electronics firms selects products for manufacture abroad further illustrates this preference for manufacture in the United States. Instead of screening the products and manufacturing abroad those on which the most money could be made, the firm selected only those products which it had to stop manufacturing in the United States because of losses or very low profits: its alternatives were to stop making the products or to make them abroad.

For these reasons I believe that most U.S. foreign direct investments are made because the firms must do so in order to hold and increase their markets; hence, since econometric studies show this type of foreign direct investment to be more beneficial to the U.S. balance of payments than investments made abroad that could have been made equally well in the United States, then by this standard, my judgment is that U.S. foreign direct investment tends to be favorable rather than unfavorable for the U.S. balance of payments. Lest I be misunderstood, I am not implying that companies are interested only in making sales and not profits because such is not the case; but sales are a prerequisite of profits.

In addition to this difficulty in determining causes of foreign investment, other weaknesses of econometric models exist. Some models do not give adequate weight to "anticipatory exports"; that is, those goods exported from the United States in anticipation of building the plant abroad, nor to "associated exports"; that is, those exports resulting from the sale of associated products because of the establishment of a foreign subsidiary.[4] In addition, my studies have uncovered another type of U.S. export which has not been incorporated explicitly into econometric models, but which sometimes results from the establishment of a plant abroad by a U.S. multinational enterprise. I call these "balancing exports." "Balancing exports" result after the first plant built in a foreign country is operating at capacity: consumption of the product grows smoothly, but additional plant capacity can be added only in large steps because each plant must be at least a certain minimum size to be economic. Therefore, there is a period during which the growth in the foreign market is served from the U.S. plant of the multinational enterprise. In some cases in the chemical industry, for example, such exports alone have exceeded the total plant investment—not just the equity investment. I am attaching a table based on realistic assumptions and illustrating a case in which a $1 million investment in a foreign plant results in $1.7 million of "balancing exports." If the initial plant had been built by a German firm, for example, then the German firm likely would have provided the "balancing exports." These "balancing exports" are different from the anticipatory exports for the second

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[4] For example, these criticisms have been made against the Hufbauer-Adler report prepared for the U.S. Treasury; see Vernon, op. cit., pp. 50–51.

plant that eventually will be built in the foreign country, because it is possible that the multinational firm owning the first plant will provide these exports even though it might not build the second plant.

(The table referred to above follows:)

MODEL SHOWING SIZE OF BALANCING EXPORTS RELATIVE TO SIZE OF PLANT INVESTMENT: ILLUSTRATIVE CASE FOR CHEMICAL INDUSTRY

[Plant investment=$1 million]

Year	Capacity of plant No. 1 in foreign country A (millions of dollars of annual output)	Consumption in foreign country A of products of the kind made in plant No. 1 (millions of dollars annually)	Balancing Exports= U.S. Exports to foreign country A of products of the kind made in plant No. 1 (millions of dollars annually)
1	1.00	1.00	0
2	1.00	1.10	.10
3	1.00	1.21	.21
4	1.00	1.33	.33
5	1.00	1.46	.46
6	1.00	1.61	.61
7	2.00	1.77	0
Total Balancing Exports			1.7

ASSUMPTIONS

1. The model starts in year 1 with consumption in the foreign country equal to capacity of 1 economic-sized plant with $1,000,000 output.
2. Consumption in the foreign country is growing 10 percent yearly.
3. The difference between capacity and consumption in the foreign country is provided by U.S. exports.
4. The second foreign plant, with a capacity of $1,000,000 annually, is brought onstream to operate at 77 percent of capacity during its 1st year of operation (80 percent is a figure often used in the industry).
5. An investment of $1,000,000 will produce $1,000,000 in annual output.

Mr. STOBAUGH. Finally, and this is an extremely important point, the econometric models do not show the dynamic effects of U.S. foreign direct investment in terms of maintaining and increasing the competitive strengths of U.S. firms. In my opinion, complexities such as this one and those mentioned previously mean that at the present time econometric models of U.S. foreign direct investment should not be used for national policymaking. If forced to answer the question, "Does U.S. foreign direct investment help or hurt the U.S. balance of payments?" my judgment is that it helps; further that it helps to a greater extent than indicated in most econometric studies, although it is impossible with our existing level of knowledge to make an accurate estimate of the extent.

Balance-of-payment analyses typically show that if a U.S. investment abroad helps the U.S. balance of payments, then it hurts the host country's balance of payments. This conclusion results from the assumption that any investment in the host country must be by a U.S. firm or by a national firm. Such an assumption is not realistic because another alternative often exists. Either a U.S. firm must make the investment or a firm from another advanced country, for example, Germany, will do so; furthermore, in many cases it is reasonable to assume that whichever firm makes the investment will secure the market of the host country. In analyzing these alternatives, if the U.S. firm makes the investment, the balance of payments of both the United States and the host country could be improved while the balance of payments of Germany could be worse off than if its firm had made the investment. Because of this analysis and because foreign investment often increases industrial efficiency of the host country and the host country's exports to third countries, it is incorrect to assume that if a U.S. foreign direct investment helps the U.S. balance of payments, then it automatically hurts the balance of payments of the host country.

II. OTHER ECONOMIC EFFECTS

Because we do not know the balance-of-payments effects of multinational enterprises and since, hopefully, the international monetary system will be made sufficiently robust to prevent recurring balance-of-payments problems among the advanced nations, other economic effects such as growth and efficiency are more important than the balance-of-payments considerations in any discussion of multinational enterprises. Therefore, it is not because these other matters are not important that I spend so little time on them today, but rather because they are being discussed during the other days of these hearings.

The multinational enterprise has proven to be an especially proficient vehicle for developing, transferring, and using complex technology. The real income of the world is larger because such enterprises exist; hence, there should be a presumption against unnecessarily inhibiting their growth. Of course, it is a problem to decide what action is unnecessary inhibition and what action is needed to keep a multinational enterprise's behavior consistent with the goals of the Nation. A nagging question is the extent to which actions by multinational enterprises interfere with the achievement of national policies.

III. THE POSSIBLE USE OF FINANCIAL TOOLS BY MULTINATIONAL ENTERPRISES TO THWART NATIONAL POLICIES

It is common practice among observers of multinational enterprises to talk about the use of intercompany transfer pricing to avoid taxes, the use of intercompany loans or extension of intercompany credit to avoid monetary restraints in the host country, and the engagement in currency speculation which weakens a nation's reserves. I would be the first to agree that such financial tools many times are used, and at times, they are used deliberately to circumvent a national policy. However, I believe that the actual use of such financial tools by multinational enterprises to thwart national economic policies is much less than imagined. The imagined use comes from the view of a multinational enterprise as one economic entity controlled by one "economic man" in headquarters rather than what the enterprise really is: an organization of numerous staff groups and subsidiaries, some of which are large and powerful in their own rights, and among which considerable negotiation takes place. In fact, gross simplifications about the behavior of multinational enterprises are misleading.

We have identified at least three distinct operating patterns among multinational enterprises.[5] Of these, the medium-sized multinational

[5] This is discussed in much greater detail in my "Financing Foreign Subsidiaries of U.S.-Controlled Multinational Enterprises," Journal of International Business Studies, I (Spring, 1970).

enterprises have a greater tendency than the other enterprises to attempt an overall systems optimization approach and more nearly approach the economists' concept of one "economic man" running the enterprise from headquarters; even so, these enterprises fall far short of such a mark. Because smaller firms lack international experience, they tend to have decentralized operations without close control from headquarters or coordination among subsidiaries.

The large multinational enterprises, which make up our third category, are more important economically than the other two groups and are the most feared by foreign countries. About one-third of all United States foreign direct investment is accounted for by a relatively few of these giants. There are at least three reasons why such large enterprises do not act as an organization run by one "economic man" from headquarters: First, the organizations are too large and complex to enable this to be done. Obviously a computer model would have to be used for such a purpose, but a model of a multinational enterprise system with dozens, and in some cases hundreds, of subsidiaries operating in as many as 100 countries, with numerous interconnecting flows of goods and money, would be so complex as to be well beyond the capabilities of today's most advanced high-speed computer systems. As a result of this complexity, the managers use a variety of rules of thumb to assist them in decisionmaking; for example, they set equity equal to fixed assets in forming a new subsidiary. I know of cases in which a firm could have saved millions of dollars in U.S. taxes, and still have been within the laws of the United States and the host country, had it used a greater portion of company funds in the form of debt instead of equity, rather than the decision rule which it used.

Even if a large multinational enterprise were capable of approaching some crude overall system optimum by using sophisticated financial tools, its managers would have little incentive to do so if such actions jeopardized the enterprise's position in a foreign country. To be sure, important savings can be made by financial manipulations, but such savings are small in relation to the earnings received from capitalizing on a firm's special strengths, such as technical know-how, managerial and marketing expertise, or a capacity to raise large sums of money. Reinforcing my belief in this reluctance to engage in financial actions, which though legal, might seriously upset local authorities, those multinational enterprises spending a larger than average amount of their revenue on research and development seem even more reluctant than other firms to use sophisticated financial tools, presumably because many of these firms have adopted a basic corporate strategy of focusing their resources on the introduction of new products.

IV. THE FUTURE

What does the future hold for the multinational enterprise? I agree with many other observers that the importance of multinational enterprises will grow. However, as much of this growth in importance will be a result of more firms' developing international operations—and this includes non-United States as well as U.S. companies—I do not think that a few giant firms are going to "take over the world." In many products and industries the giant firms lose their advantages as the product or industry matures. In the world petrochemical industry, for example, the multinational enterprises' share of the world's production facilities has declined as the products matured even though the world consumption of the products continued to increase in importance. In the electronics industry, the technology is being diffused worldwide at a rapid rate, and much is now in the hands of the Europeans and Japanese. And, of course, the major oil companies are losing their previously strong grip on the world oil industry; a good example of what can happen as an industry matures is the case of Peru and the Standard Oil of New Jersey) affiliate, International Petroleum Corp. While many observers explain Peru's nationalization in purely political terms, I believe the economic factors are just as important. The simple fact is that although the political problem existed for several decades, it was only recently that Jersey Standard's contribution to the Peruvian operations became relatively unimportant. Jersey's help ceased to be important because production and refining technology became mature and readily available for purchase, and Peru's internal consumption of petroleum-products was about equal to its oil production; thus the Jersey corporate network was no longer needed to take Peruvian oil.

Certainly there will continue to be tensions over the question of control as nations feel that, at a time when they have an extensive set of internal economic goals, they are prevented by multinational enterprises from being "masters in their own house"; but at the same time, the nations want the fruits brought by the multinational enterprise. Some who testified before you previously—and I refer specifically to Professor Vernon's testimony of last December—have suggested that international agreements affecting multinational enterprises would be desirable, especially to coordinate national policies on such matters as transfer pricing, taxation of the incomes of multinational enterprises, antitrust provisions, trading with the enemy, insurance of equitable treatment of multinational enterprises, and limitations on the jurisdiction of the U.S. Government within the boundaries of other countries. I heartily subscribe to this suggestion of international agreements and think that the managers of most multinational enterprises would too. In this way they would be assured of equitable treatment and would not have to worry about coping with widely varying tax laws, but could focus their energies on exploiting the major strengths of their firms. As it is now, the multinational enterprise often is caught between the conflicting desires of different nations—and at times even between two agencies of one department of one nation. I know of one case in which the U.S. subsidiary of a foreign company was under pressure from U.S. customs officials to increase the transfer price of goods purchased from the foreign parent and thereby increase import duty, and at the same time was under pressure from the U.S. Internal Revenue Service to lower the transfer price in order to increase reported profits of the U.S. subsidiary and thereby pay more U.S. income taxes. Pressures such as these reduce the economic efficiency of the multinational enterprise by taking top marginal talent away from the prime business interests of the firm.

Heightening this need for international agreement is the rapid increase in communications and transportation combined with the increasing capabilities of electronic computers which give the multinational enterprise headquarters a growing ability to operate the enterprise as an organizational whole rather than as a number of somewhat independent subsidiaries.

V. POSSIBLE IMPROVEMENTS IN U.S. FOREIGN ECONOMIC POLICY

In addition to international agreement on such matters as taxation and antitrust laws, other things could be done to help the multinational enterprise and the world economy. Most, if not all, managers in U.S. multinational enterprises are opposed to the mandatory capital restraint program. This program has had a relatively minor impact on U.S. foreign direct investment because most medium and large multinational enterprises have been able to raise money in Europe, although they have had to devote additional managerial time to fund raising in addition to paying higher interest rates; furthermore, in the process they lost some of the fund-raising advantage they previously had over their European competitors. In addition, the foreign investment plans of some smaller firms very probably were seriously affected. Since the mandatory program obviously has these harmful effects, since its overall results are difficult to assess and since it represents a unilateral rather than multilateral approach to the world's monetary problems, I would favor disbanding the program. This leads into my next subject: the great need for improvement of the world monetary system.

I will not dwell unduly on this because it has been the subject of other testimony. However, I do want to bring up one point that affects financial management of multinational enterprises: for adjusting disparities between currencies, changes in exchange rates should be used rather than the combination of changes in exhange rates, tariffs, quotas, other nontariff distortions, and capital controls that have been used in recent years. The multinational enterprise manager can focus more easily on one variable than on many; and furthermore, by hedging in forward markets for foreign currencies he can in effect buy insurance against changes in exchange rate; but no such insurance exists for changes in tariffs or quotas. Thus, the possibility of sudden changes in tariffs or the imposition of quotas makes the manager more reluctant to build a plant in one nation to serve a market in another. As as result, the potential for achieving scale economies which are so important in many modern industries is reduced. While solutions to the international monetary problem are a matter of first priority, they are quite beyond the scope of my testimony. Still, I want to make one additional observation. I believe that some international private bankers are reluctant to have more flexibility introduced into the international monetary system by the authorities' widening the range within which a currency's value must be maintained or by allowing currency values to make small moves in one direction for indefinite periods of time. These private bankers doubt the ease with which adequate forward markets could be maintained in foreign currencies. In my opinion, such bankers are underestimating the flexibility of the private financial institutions much as several years ago they grossly underestimated the ability of the Eurocapital markets to provide the huge amounts of funds they ultimately did.

The final point I make concerns adjustment assistance in the United States. The multinational enterprise has proven to be a marvelous vehicle for developing newer technology and products and upgrading the skills and pay of their U.S. work force while at the same time increasing U.S. employment. Furthermore, even whole industries—electronics, for example—have been able to adjust to very rapid increases in imports and still increase U.S. employment and wage rates as well as increase the industry's net trade balance. The multinational enterprises in such industries have played an important role in this adjustment process.

In cases in which adjustment cannot be made within an industry, an effective national adjustment system should be implemented to help move resources out of the industry into a higher technology industry. This would do far more to help the U.S. standard of living and the U.S. balance of payments than would applying quotas or increasing tariffs. These latter measures only freeze existing resources in, and encourage new resources to enter, industries in which the United States is not competitive worldwide; instead of such measures, we should be encouraging resources to enter those industries in which we have a competitive advantage worldwide.

Of course, it is possible that national policy dictates that a portion or all of an industry must be protected against foreign competition for reasons of national defense. In such case, I suggest that direct payments by the Government to the industry would be better than distorting the world trading system by imposing higher tariffs or quotas; albeit, I realize that such an approach might present political difficulties.

VI. SUMMARY

There is a great lack of knowledge about the trade, payment, and other financial consequences of multinational enterprises, primarily because there is no reliable model to answer the question: "What would conditions be if these enterprises did not exist?" It follows from this that any statements about the effect of foreign direct investment on the balance of payments must be based more on judgment than on econometric models. My judgment is that U.S. multinational enterprises make a positive contribution to the U.S. balance of payments. However, the skills of these enterprises in developing transferring, and using complex technology and in exploiting scale economies is more important than balance-of-payments considerations.

I believe that uses of financial tools by multinational enterprises to thwart governmental policies is not practiced to the extent often imagined; although to be sure there are some cases. The number and relative importance of multinational enterprises will continue to grow; however, because of the deterioration over time of the economic power of the largest firms in many product areas and industries, a few large firms will not take over the world.

What should U.S. foreign economic policy be? Encourage international agreements to relieve tension on such matters as transfer pricing, tax division, and antitrust practices; encourage the introduction of more flexibility into the international monetary system instead of relying on tariffs or quotas to change trade flows directly; and introduce a better adjustment system in the United States to allow continued increases in imports and the shifting of U.S. workers into more highly skilled jobs in the expanding industries.

In general, I favor encouraging the continued growth of the number and size of U.S. multinational enterprises—while, of course, insuring that competition does not suffer. At the same time we should continue studying such enterprises in order to increase our knowledge about the effects of their operations.

Thank you for inviting me to testify. I will be happy to answer any questions.

Representative REUSS. Thank you, Mr. Stobaugh.

Yesterday we heard from Mr. Paul Jennings, president of the Electrical, Radio & Machine Workers Union, concerning the thousands of jobs in the electronics industries that multinational corporations have transferred from the United States to Japan, Taiwan, and other countries. In your statement, Mr. Stobaugh, you say the electronics industry has been able to adjust to very rapid increases in imports while still increasing domestic employment, wage rates, and the industry's net trade balance. Could you provide for the record the data on employment, wage rates, and net trade balance of the electronics industry and perhaps a corresponding breakdown for the components of the industry which you consider relevant?

Mr. STOBAUGH. I do not have it with me, but I can get it this afternoon, if that would be helpful.

Representative REUSS. That would be most satisfactory. You can provide it for the record.

Mr. STOBAUGH. Yes.

(The following information was subsequently supplied for the record by Mr. Stobaugh:)

The attached four tables are from a report submitted on May 14, 1970, to the United States Tariff Commission by Mr. Alfred R. McCauley, Special Counsel to the Electronics Industries Association.

TABLE 1.—U.S. SALES OF ELECTRONIC ARTICLES, BY PRINCIPAL CLASSES, 1960–69

[In millions of dollars]

Year	Consumer products	Industrial products	Government products	Replacement components	Total
1960	2,018	1,980	6,124	555	10,677
1961	2,020	2,585	7,190	580	12,375
1962	2,435	3,025	8,080	620	14,160
1963	2,604	3,610	8,841	690	15,645
1964	2,940	4,268	8,775	620	16,603
1965	3,641	5,222	8,969	630	18,462
1966	4,528	5,842	10,330	640	21,340
1967	4,378	6,373	11,720	650	23,121
1968	4,619	6,693	12,504	675	24,491
1969	4,800	7,260	12,100	690	[1] 24,850

[1] Preliminary estimate provided by Marketing Services Department, Electronic Industries Association.

Source: Electronic Industries Yearbook 1969, prepared by Marketing Services Department, Electronic Industries Association.

TABLE 2.—U.S. IMPORT-EXPORT TRADE IN SELECTED ELECTRONIC PRODUCTS, 1966–69

[Dollars in thousands]

Commodity type	1966	1967	1968	1969
Consumer:				
Imports	$435,430	$454,144	$710,871	$994,509
Exports	64,562	64,494	85,229	106,621
Government, industrial, commercial:				
Imports	276,922	303,113	346,902	444,728
Exports	1,004,255	1,297,918	1,445,674	1,833,110
Components:				
Solid state devices:				
Imports	42,247	43,435	71,543	104,310
Exports	130,312	151,979	204,380	345,811
Tubes:				
Imports	53,430	52,621	56,162	43,582
Exports	75,524	80,798	78,628	91,995
Other components:				
Imports	108,488	137,395	176,966	244,313
Exports	251,105	289,791	337,230	423,898
Total:				
Imports	916,517	990,708	1,362,444	1,831,342
Exports	1,525,758	1,884,693	2,151,141	2,801,435
Net trade balance	609,241	894,272	788,697	970,093

Sources: Electronic Industries Yearbook, 1969 and Electronic Trends International, vol. 4, No. 2 (February, 1970), prepared by Marketing Services Department, Electronic Industries Association.

TABLE 3.—ESTIMATED ELECTRONICS EMPLOYMENT BY SELECTED YEARS, 1961–69

[Employees]

Category	1961	1946	1966	1967	1968	1969
End equipment:						
Government and space	283,000	250,000	327,000	340,000	350,000	NA
Industrial and commercial	126,000	165,000	169,000	172,000	175,000	NA
Consumer	89,000	100,000	144,000	138,000	145,000	NA
Total end equipment	498,000	515,000	640,000	650,000	670,000	
Components	280,000	305,000	440,000	434,000	440,000	NA
Total manufacturing	778,000	820,000	1,080,000	1,084,000	1,110,000	[1] 1,136,000

[1] Estimated from data obtained from U S. Department of Labor and industry sources.

Source: Electronic Industries Year Book 1969, prepared by Marketing Services Department, Electronic Industries Association.

TABLE 4.—EMPLOYMENT AND EARNINGS BY SELECTED ELECTRONIC INDUSTRY GROUPS, 1966–69

[Annual averages]

	1966	1967	1968	1969
Radio and TV receivers (sic 365):				
All employees (in thousands)	161.7	156.3	153.4	154.6
Women employees (in thousands)	91.8	90.1	88.6	87.3
Production workers (in thousands)	128.6	120.0	116.4	115.3
Production worker average weekly earnings (in dollars)	94.33	93.65	97.39	103.30
Production worker average hourly earnings (in dollars)	2.37	2.42	2.51	2.69
Production worker average weekly hours	39.8	38.7	38.8	38.4
Production worker average weekly overtime hours	2.8	1.7	1.6	1.5
Accessions per 100 employees	7.0	5.2	5.9	5.2
New hires per 100 employees	5.7	3.3	3.6	3.2
Separations per 100 employees	5.5	6.9	6.6	6.3
Quits per 100 employees	3.1	2.9	3.1	2.7
Layoffs per 100 employees	.7	2.5	1.6	1.8

TABLE 4.—EMPLOYMENT AND EARNINGS BY SELECTED ELECTRONIC INDUSTRY GROUPS, 1966-69—Continued

[Annual averages]

	1966	1967	1968	1969
Communication equipment (sic 366):				
All employees (in thousands)	467.7	510.9	522.9	525.1
Women employees (in thousands)	162.2	176.3	179.9	184.4
Production workers (in thousands)	235.2	252.5	257.8	257.1
Production worker average weekly earnings (in dollars)	121.35	126.18	131.38	142.83
Production worker average hourly earnings (in dollars)	2.91	3.07	3.22	3.45
Production worker average weekly hours	41.7	41.1	40.8	41.4
Production worker average weekly overtime hours	3.3	2.8	2.7	3.3
Accessions per 100 employees	3.5	3.0	2.5	2.8
New hires per 100 employees	2.8	2.3	1.8	2.2
Separations per 100 employees	2.7	2.7	2.8	2.8
Quits per 100 employees	1.6	1.5	1.5	1.5
Layoffs per 100 employees	.4	.4	.6	.6
Radio and TV communications equipment (sic 3662):				
All employees (in thousands)	339.6	380.9	392.3	384.0
Women employees (in thousands)	106.4	119.2	123.7	120.8
Production workers (in thousands)	148.2	165.2	171.3	163.3
Production worker average weekly earnings (in dollars)	120.67	125.66	131.84	140.22
Production worker average hourly earnings (in dollars)	2.88	3.05	3.20	3.42
Production worker average weekly hours	41.9	41.2	41.2	41.0
Accessions per 100 employees	4.0	3.3	2.5	2.6
New hires per 100 employees	3.1	2.5	1.8	1.8
Separations per 100 employees	2.9	3.0	3.0	3.0
Quits per 100 employees	1.7	1.6	1.5	1.5
Layoffs per 100 employees	.4	.6	.8	.7
Electronic components and accessories (sic 367):				
All employees (in thousands)	388.6	384.9	388.0	410.1
Women employees (in thousands)	233.6	222.9	219.1	230.3
Production workers (in thousands)	297.9	280.1	274.5	286.1
Production worker average weekly earnings (in dollars)	92.11	94.08	100.73	105.59
Production worker average hourly earnings (in dollars)	2.28	2.40	2.55	2.68
Production worker average weekly hours	40.4	39.2	39.5	39.4
Production workeraverage weekly overtime hours	3.0	2.0	2.2	2.2
Accessions per 100 employees	5.7	4.2	4.5	4.9
New hires per 100 employees	4.7	2.7	3.1	3.7
Separations per 100 employees	4.7	5.1	4.5	4.7
Quits per 100 employees	3.0	2.4	2.4	2.7
Layoffs per 100 employees	.6	1.6	1.0	.8
Electron Tubes (sic 3671-3):				
All employees (in thousands)	76.9	76.7	74.7	70.4
Women employees (in thousands)	39.4	39.2	36.5	33.5
Production workers (in thousands)	55.1	54.3	52.2	48.2
Production worker average weekly earnings (in dollars)	110.08	106.66	108.86	115.24
Production worker average hourly earnings (in dollars)	2.56	2.64	2.77	2.91
Production worker average weekly hours	43.0	40.4	39.3	39.6
Accessions per 100 employees	4.7	3.4	3.4	3.3
New hires per 100 employees	3.9	1.8	1.7	2.0
Separations per 100 employees	3.3	4.8	4.1	4.1
Quits per 100 employees	2.0	2.0	2.0	2.1
Layoffs per 100 employees	.2	1.8	.9	.9
Electronic components not elsewhere classified: (sic 3674-9):				
All employees (in thousands)	311.7	308.2	313.2	339.7
Women employees (in thousands)	194.2	183.7	182.6	196.8
Production workers (in thousands)	242.8	225.8	222.3	237.8
Production worker average weekly earnings (in dollars)	87.96	91.03	98.75	103.62
Production worker average hourly earnings (in dollars)	2.21	2.34	2.50	2.63
Production worker average weekly hours	39.8	38.9	39.5	39.4
Accessions per 100 employees	5.9	4.5	4.7	5.2
New hires per 100 employees	4.9	2.9	3.4	4.1
Separations per 100 employees	5.1	5.2	4.6	4.8
Quits per 100 employees	3.2	2.5	2.6	2.9
Layoffs per 100 employees	.6	1.6	.10	.8

Source: U.S. Department of Labor, Bureau of Labor Statistics. For years 1966–68 annual averages obtained from unpublished data from 1312 series (Employment and Earnings, United States) and 1969 annual averages from Employment and Earnings, vol. 16, No. 9 (March 1970).

Mr. STOBAUGH. Could I make a comment on that type of thinking?

Representatives REUSS. Yes.

Mr. STOBAUGH. The conceptual model that Mr. Jennings is using is that if a firm builds a plant in Taiwan, then automatically that is taking a job away from a U.S. worker. Some day the world electronics industry is going to be so large that there might be 100 million people all around the world employed in the electronics industry. Now, would anybody really say that all of those hundred million people should be U.S. workers? The answer is "No."

The way to look at it is: What work should U.S. workers be doing and what work can be best done abroad by foreign nationals? What has been happening in the electronics industry quite clearly is that the higher skilled jobs have been kept in the United States and the lower skilled jobs, particularly those that are labor intensive and use relatively smaller amounts of capital, have been transferred abroad. This incorporation of the foreign production facilities in the overall production systems of these electronic firms have made the firms stronger, and hence they can compete more readily with Japanese imports. As a result these foreign production facilities of U.S. firms have increased U.S. employment in the electronics industries rather than taken away from U.S. employment.

Representative REUSS. What proportion of the U.S. labor market is higher skill and what is lower skill? I ask that question because we Americans tend to have the idea that all Americans are very skilled or potentially very skilled workers. Yet, you visit European countries and, you find that the level of skills, at least among the natives, the non-Spaniards, Cretans, Greeks, Turks, Yugoslavs, and North Africans, is really very high. Their employment of lower skilled people is usually a temporary import arrangement which works out very well from the standpoint of Switzerland, Sweden, or Germany and is not much resented by the lower skilled individuals because while they are working and before they go back home, they do make good wages. We do not have quite that delightful solution to our manpower problems.

Would you throw that into your calculus and come back at me?

Mr. STOBAUGH. Yes. There are many different ways to measure skill levels, but one obvious way is education level; and I believe that our work force on the average is more highly educated than any other work force on earth. And another measure——

Representative REUSS. Really? Than Sweden? Than Switzerland?

Mr. STOBAUGH. That is my impression and I would count all the people that are doing the R. & D. which is a major contributor to U.S. exports and to the strength of the U.S. multinational enterprises.

Representative REUSS. Averages, of course, might be misleading. We might have the average of a lot of people with 8 years of graduate work and people who got through the seventh grade. Yet compared with a country where everybody went through high school, we might end up with more of a problem of how to deal with our own less-skilled workers than some of these European countries. Any light you can throw on that—we will leave a little space in the record there—will be helpful.

Mr. STOBAUGH. Fine. Thank you.

(The following information was subsequently supplied for the record by Mr. Stobaugh:)

I agree that averages do not tell the whole story about labor skills. I understand that the U.S. has a greater percentage of illiterates than some foreign countries, but yet, at the same time we have a greater percentage of highly skilled people—the U.S. work force contains a higher percentage of technical, professional, and managerial workers than that of any other major nation;[1] furthermore, a greater percentage of U.S. students are enrolled in higher education than in any other nation.[2]

I recommend educating and training our unskilled workers rather than adopting a trade policy that not only chains them to a low-paid job for the rest of their life, but encourages their children to enter the same unskilled, low-paid occupations as the parents. I grew up in the rural South and know personally many unskilled workers. In my opinion, most of these unskilled workers are unskilled not because they are dumb and untrainable but rather because they did not have adequate opportunity and encouragement to develop better skills. The development and use of these higher skills will do more toward raising the U.S. standard of living and helping the U.S. balance of payments than will the imposition of trade quotas which are designed to keep Americans employed in unskilled jobs.

Labor skills seem to be especially important in explaining U.S. export performance. The industries that account for the United States trade surplus use relatively more scientists and engineers in research and development, production, and sales than do other major U.S. industries[3] and U.S. exports contain a greater percentage of highly skilled labor than do exports of other countries, including those goods shipped to the U.S.[4] Thus, it is not surprising to find that the average wage embodied in U.S. exports is higher than that embodied in U.S. goods competing with U.S. imports.[5]

Representative REUSS. Now, to Mr. Danielian, Mr. Istel, and Mr. Stobaugh and maybe Mr. Rolfe, though he was not specific on this, you have all asked for the early abolition of controls on U.S. capital exports. Whenever this is brought up with this administration or for that matter with the last administration, we are always greeted with the answer that a rapid increase in capital outflows would occur after such abolition and, therefore, it is said we cannot do much right now about the controls.

How would you gentlemen answer that rebuttal on the part of the administration?

Mr. Danielian?

Mr. DANIELIAN. May I address myself to it? I would like to expand the objections. I think there are really three excuses given for maintaining the controls. One is a financial one, the question that you brought up, the possible massive outflows of capital.

We have many calculations and we find that for a variety of reasons the most that you can expect from the abolition is possibly a $600 million to a $900 million incremental outflow.

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[1] About 22% in the U.S. versus 17% in Sweden, for example; see *Year Book of Labour Statistics: 1969*, International Labour Office, Geneva.

[2] About 11% of U.S. students are in the highest education level (Level 3 in the U.N. *Statistical Year Book*) compared with about half this percentage in other major industrial nations. Additionally, Mr. Arthur K. Watson testified to this Subcommittee last December that nearly half of our young people obtain some form of post-high school education compared with 10 to 20 per cent in Europe and 1 to 5 per cent in the developing nations.

[3] William Gruber, Dileep Mehta, and Raymond Vernon, "The R&D Factor in International Trade and International Investment of U.S. Industries," *Journal of Political Economy*, LXXV (February 1967), pp. 20–37.

[4] Donald B. Keesing, "Labor Skills and International Trade: Evaluating Many Trade Flows with a Single Measuring Device," *Review of Economics and Statistics*, XLVII (August 1965), pp. 287–293.

[5] Helen Waehrer, "Wage Rates, Labor Skills, and United States Foreign Investment," in Kenen and Lawrence (eds.), *Open Economy* (New York: Columbia University Press, 1968); and Irving Kravis, "Wages and Foreign Trade," *Review of Economics and Statistics*, XXXIV (February 1956), pp. 14–30.

Representative REUSS. Annual increase in capital exports.

Mr. DANIELIAN. Yes. Assuming all other things being equal, including comparative interest rates between this country and Europe, the business conditions, and labor-wage settlements, which, of course, have been going up in Europe, where there is a shortage of labor, the subtle controls that are available in Europe, the guided economies—assuming all these factors to be equal, we do not feel that there is going to be any really major change in our international accounts, particularly when you consider the fact that the Eurodollar market, the ebb and flow of capital, short-term capital, is in billions and billions of dollars and it affects the appearance of our balance-of-payments accounts to a much larger extent than the direct investment factor, and in addition, of course, we are now getting into massive international foreign aid programs which have their own balance-of-payments effect upon the United States. And then there are the continued expenditures on military account.

So, when you really put it in perspective, direct investment is a very small factor in our international balance-of-payments picture and everybody seems to be agreed that in the long run controls are bad for the United States. If it is bad for the United States in the long run, you can keep them only on the assumption that the balance-of-payments deficit is a short-term factor.

Well, it has been amply proved that it is not a short-term factor. It is almost chronic and, therefore, the acquisition of income-bearing assets abroad should be a prime concern of the United States.

The other two excuses given are that the European governments are opposed and there will be a reaction. Well, I do not find that at all. I understand that most of the European countries have branch offices of their industrial development departments in the United States to drum up direct investments in their countries. And this——

Representative REUSS. This seems to me a very unsubstantial objection, if true.

Mr. DANIELIAN. It is given as an argument.

Representative REUSS. Any European country that wants to forbid or condition American investment can do so.

Mr. DANIELIAN. This is an argument advanced by our own officials as a reason for keeping the controls—unfavorable reaction from Europe. And I do not think that is substantial. I have talked to a great many people in Europe; and with the possible exception of West Germany, which has plenty of capital, I do not find any objection to direct investments in Europe and they are all drumming up new business in the United States.

A third factor, of course, is the attitude of labor. Whether we like it or not it is a political fact in the United States that labor is of the opinion that it hurts their business. I think they are confusing international competition and costs and international trade with the investment problems and that has affected Government policy and doctrine here.

I am sure that whether the administration is Republican or Democratic, they do listen to the attitude of labor, and I think here there must be a dialog created, perhaps under the auspices of some neutral agency, between labor and industry and this committee. I think it is sort of an ideological fixation, and I think it is unfortunate because it is hurting the long-range interests of the United States.

Representative REUSS. Thank you.

Mr. Istel, you took a somewhat more relaxed view of the consequences of a balance-of-payments deficit than Mr. Danielian. So, I imagine——

Mr. ISTEL. Yes.

Representative REUSS (continuing). Your answer to my question will be even more so than Mr. Danielian's, but let us hear it.

Mr. ISTEL. I think obviously, it is extremely difficult to predict what would happen. What I was trying to say, and I think it is practical as well as theoretical, is that with the kind of role that the dollar has been playing, the confidence factors that have also been mentioned by Professor Rolfe, become so important that a restoration or an improvement in the confidence factor overall would probably play a beneficial role in bringing in capital imports into this country and financing on a longer term basis the American debts abroad.

I would be very surprised if there would be a negative impact in the way we measure the balance of payments from the removal of those at a good time.

What I mean by a good time, I think, is any time very soon when actually we can show some progress in combating inflation here and our balance of trade is showing some improvement. I do not think that the outflow for direct investment would increase appreciably and I think that the inflow of long-term capital that would come into this country over a period of time would probably more than compensate for it. So, I do not think there would be any net negative impact of significance.

Representative REUSS. Mr. Rolfe, while you did not specifically——

Mr. ROLFE. I will pass on this one.

Representative REUSS. You want to pass on this. All right.

Mr. Stobaugh?

Mr. STOBAUGH. First, I do not have an estimate of the effect that it would have on our capital flows but my approach to the problem would be as follows. First, it is not clear that we are measuring the balance of payments correctly. It is not really clear that we have a balance-of-payments problem except that we in this country were largely responsible for bringing it to the attention of the world by our controls and by the way we measure it.

For example, if we measure our claims differently and included the liquid assets of the multinational enterprises abroad, we would have enormous liquid assets to cover any liquid claims on us. My estimate of the liquidity of the U.S. multinational enterprises abroad is that their liquid assets plus the other liquid assets of the United States far exceed the liquid claims that foreigners have on us.

The second point is that if there is a balance-of-payments problem, I do not think it should be met by capital controls. I think we ought to turn to enlarging world reserves or varying the exchange rates rather than going to controls of either capital or trade flows.

Representative REUSS. Of course, our partners have not shown much enthusiasm for varying exchange rates.

Mr. STOBAUGH. That is right. And I do not know the details of our negotiations with our partners so I do not know what the outcome of those negotiations will be, nor do I know what levers we have to use on them. Still, that would certainly be my approach to the problem.

Representative REUSS. Mr. Karlik, did you have a question?

Mr. KARLIK. Yes. I think I do have a question I would like to ask.

In the course of these hearings since Monday, an interesting diversity of opinion regarding the U.S. balance of payments, I think, is appearing. Mr. Danielian seems to be somewhat more concerned about it than some of the other witnesses. He is in favor of, for example, the DISC, and more active use of section 252 of the Trade Expansion Act against other countries who apply illegal trade barriers against us.

Mr. DANIELIAN. While I have not mentioned section 252 in these proceedings, I mentioned the revision of 251. Section 252 has been invoked only once in the case of agriculture to which it applies. (During the so-called "chicken war.")

Mr. KARLIK. On the other hand, for example, Mr. Istel said that the United States or industrialized nations generally, are going to have to have a substantial trade deficit if the developing countries are going to be able to service their debts, and the implication there is that he would not be disturbed by small U.S. trade surpluses or even occasional deficits.

In addition, there is an emerging emphasis on the balance sheet approach to the balance of payments. Periodic balance sheets would presumably be linked by income statements. Judd Polk brought up this idea on Monday.

There are two things I would like you people to comment on. First, the figures that Judd Polk presented indicated that there has been virtually no increase in U.S. net external asset position since 1966.

Now does this fact imply the United States has a balance-of-payments problem? Second, could an emphasis on the net external asset position of the United States lead to, well, some kind of mercantilism? In other words, if we start emphasizing the net external asset position, is direct investment from abroad in the United States a bad thing?

Mr. DANIELIAN. May I comment on that because——

Mr. KARLIK. I would like everybody to comment on it.

Mr. DANIELIAN (continuing). I do take strong exception to that new calculus that Mr. Polk has put in the record. I think it is one of the most dangerous pieces of arithmetical accommodation to a very serious problem that we face.

What he is doing is really equating privately owned assets abroad against official Government liabilities abroad and the only way you can equate those two is if you make the connecting link; namely, that the Government has the right to requisition these private assets abroad at some time when it is called upon to pay on these dollars that are held abroad. This, of course, is what Britain had to do during and after World War II. And I really think that this does not solve the problem at all. It may give a new picture of the asset and liability structure of both the Government and the private citizens of the United States, but unless you are willing to make that connection, it does not hold.

Now, second, I would agree with the proposition that as an investor on a worldwide basis, ultimately the future of this country will be as a trade deficit country. This is the only way you can get paid in real goods, the return on your investments. Now, England was perfectly happy to live under those conditions for decades.

The difficulty with that, however, is that there are noncommercial outlays. Unless you find some way of exporting resources to take care of your noncommercial obligations abroad which may be in the area of probably, say $8 billion a year, unless you are able to push out real goods to compensate or to take care of these noncommercial obligations abroad, then what you are forced to do is borrow abroad to pay for them.

Now, the ultimate effect of that is, and this comes to the point recently made, that we should encourage foreign investment in the United States, by all means. I think the future of the world is in the internationalization of both ownership and enterprise; but if you do not eliminate the noncommercial obligations of the United States abroad, you have to have net earnings to pay for them. However, if you equalize your own asset position abroad by direct investment from abroad in the United States, let us say foreigners have $60 or $70 billion of investments in the United States, you have to pay out interest and dividends. If the interest and dividends on those offset the interest and dividends you receive from abroad, you have killed your net position and you will not be able to finance your noncommercial undertakings abroad. So, it seems to me, you cannot solve this problem purely by equalizing assets and liabilities between countries as long as you have noncommercial outlays on behalf of the Government. You have got to have net earning power abroad.

Mr. KARLIK. Mr. Istel?

Mr. ISTEL. I think to answer the very well put question that was presented to us, my attitude is twofold. One, a question of timespan. I think probably everybody here, maybe not, would agree that reducing the very high rate of U.S. inflation is an extremely high priority, probably first priority, and that a corollary benefit will be improvement in our balance of trade to the degree that we are successful in accomplishing this.

I think this is probably important in the world in which we now live from many points of view, including the confidence factor. What I was saying is that what we want now, an improvement in our trade balance, may not necessarily be what we will want to have for a longer period of time. In the meantime, whether we like it or not, the dollar is playing the role of world currency and, threfore, you have a complicated, very complicated series of capital flows that are moving back and forth and that are affecting this particular aspect. I do not believe it is fair to say that I am not concerned about the balance-of-payments aspect. I am very concerned about it. I think all of us here are. I think what we are all trying to do is to get a more balanced approach into how to analyze and deal with the problem and also start looking beyond the immediate reaction which has always been that the minute that you run a balance-of-trade deficit you must follow an internal economic policy to offset that balance-of-trade deficit and that that kind of reaction, that kind of policy, is no longer appropriate for the kind of world economy that we have.

Mr. KARLIK. Mr. Rolfe?

Mr. ROLFE. I think that before you can make many generalizations about this set of figures that Judd Polk prepared about the stability of the net asset position from 1966, a lot more analysis would be needed.

Mr. ISTEL. I think that is my point.

Mr. ROLFE. I am particularly concerned with the changes in the short-term asset position here; I think in this short-term asset position, there is a lot of double counting, a lot of half counting, a lot of wrong counting, and I can see a period—that is point 1 and I think counting ought to be improved. But nevertheless, even if the counting were dead right, this kind of approach will lead to periods of leads and lags, will lead to periods of shifting. It will not be a steady accretion and it will not matter if it is not.

I think the period from 1966 to 1970 has been unique in the United States in the impact of inflation, the sucking in of imports, the whole pattern that we have undergone. I do not think that it is a characteristic period and in the long run I still think—this is contrary to Mr. Danielian and agreeing with Mr. Polk—that this is the kind of approach because this is the kind of world we live in. What we are is not a trade nation exporting only and counting at the end of the year, end of the month. We are an investing nation doing an entirely different kind of international operation.

Now, it is conceivable that you are going to get leads and lags, going to get variables going at different rates, and whatnot, but I do not think that invalidates the whole approach by any means.

Mr. KARLIK. Mr. Stobaugh, do you have a comment?

Mr. STOBAUGH. I think one of the problems of this type of presentation is that people might really believe the figures too much. There are a couple of dangers in it. One is that we have book value instead of real value on the U.S. balance sheet. Well, everybody says they know it but yet they still say, "Aha, between 1967 and 1969 our net worth went down $0.8 billion."

Now, what does that mean? It really does not mean anything in terms of trying to measure a difference of $0.8 billion, because this balance sheet systematically understates the value of our direct investment.

First, the book value of direct investment is the largest category and we know that this value is more likely to be understated than the value of a bond or other portfolio investment. So, we know that this type of approach systematically understates the strength of the U.S. position.

Second, in valuing U.S. securities, most people look at earnings per share a lot more than they do a balance sheet. It is not clear to me why we should be using only a balance sheet valuation method for our overall international business.

I want to pick up one point and that is this point on the effect of inflation on trade. A lot of people think that the major effect of inflation on trade is in the price effect, but during times of high inflation much of the U.S. domestic industry is running at or near capacity. Now U.S. industry tends to give priority to U.S. customers and as a result, the foreign customers have to wait in line and sometimes do not get the goods at all, thus, during inflationary times this is one of the major harmful effects on our exports, and conversely, on our imports. If you look at the chemical industry, for example, during some of these inflationary times we actually have had rationing of chemicals in this country and the turning down of export orders in a number of chemicals just because it takes a couple of years to build a plant.

Representative REUSS. Mr. Danielian?

Mr. DANIELIAN. I think we would be making a serious mistake if we blame the balance-of-payments deficit or the deterioration of trade primarily on inflation. There is no question that since 1965 it has been a factor but it is a historical fact that before that—I think it was in 1964 when we had a $6.8 billion balance-of-trade surplus and yet our balance-of-payments deficit was still $2.8 billion (including special transactions) in that year. And in the years prior to that we had probably the period of the most stable prices, and yet every year our balance-of-payments deficits were high.

So, I think it would be a mistake to hope that even if we brought our inflation under control, we can just wish the balance-of-payments deficit problem away. We have to really keep our eyes on the basic causes, which are the distribution of resources and the purposes for which they are used. I claim that the basic deficit situation will continue as long as we have noncompensatory Government expenditures abroad of massive proportions which cannot be compensated by either investment income or a trade surplus. But the trade surplus will have to be, oh, possibly $8 billion or so in order to make up for noncompensatory Government expenditures, and I cannot foresee even under conditions of complete stability of prices that kind of trade surplus.

Representative REUSS. Mr. Widnall?

Representative WIDNALL. Thank you, Mr. Chairman.

Mr. Danielian, before this subcommittee on Monday, Charles Kindleberger advocated the formation of a GATT for international investment. Also, several other witnesses have stated that the best solution to the problems of the multinational corporation would be through multilateral agreements.

Would you please be more specific in your assertion that a bilateral approach would be more advantageous?

Mr. DANIELIAN. Well, if I may read a part of my main statement on that, perhaps it would answer the question, Mr. Chairman.

What are the chances of international cooperation on a variety of subjects that are offered for international agreements?

The ideal conditions under which a multinational corporation could do its job best would be to free it from these vagaries of nationalistic and ideological conflicts, and establish some universal rules. This obviously is beyond our capacity at this time to sell to the rest of the world.

The World Bank has been attempting since 1962 to develop an international convention for the protection of investments, without success. Much of the opposition has come from the less-developed countries.

It has been difficult enough to negotiate bilateral treaties on taxation. A multinational approach to this problem would almost certainly doom it to failure.

We are probably unique in our concept of antitrust policies. For us to undertake to convert the rest of the world to our view would be impractical. This is not only a matter of business policy, but in some countries, as in Japan, it is almost a cultural fixation, and in others, as in Europe, trusts have been a life style of large business operations. In fact, whereas here we threaten jail sentences for conspiring to eliminate competition among our citizens, in Japan and England they are giving accolades and subsidies to merging competitors.

An international agreement on flexible exchange rates is feasible, and I am glad to have this opportunity to comment on that. In that, in 1966, in our book on the U.S. balance of payments, we recommended a 2-percent spread from IMF parity rates. But this was intended to discourage speculation and raids on currencies. Flexible exchange rates or crawling pegs currently seem to be of dubious value for the United States. Now, I am always looking at these things from the point of view of the United States.

The net effect upon us is likely to be detrimental. Those countries that devalue their currencies in relation to ours will obtain an export advantage. Those few that might revalue their currencies will merely diminish the purchasing power of the dollar where our expenditures are fixed, as in the case of military deployments in the Far East and in Europe. The result will be increased budgetary and foreign exchange costs to us. For example, the recent German revaluation is costing us an extra $100 million a year to maintain our troops there.

An international negotiation of nontariff barries is most desirable, although perhaps even more difficult than negotiations on tariff barriers. Here again, our chances of obtaining an advantageous agreement will depend on our bargaining position, because the main issues are matters of fundamental economic interest, such as "Buy American" on our part, and the common agricultural policy on the part of EEC.

Common labor standards would be most difficult to obtain. As a starter, I assume U.S. labor would demand minimum wage commitments. Most of the less-developed world needs labor-intensive industries to give employment instead of highly automated industrial plants giving limited high-wage labor employment. Underemployment or unemployment in exploding urban areas of the less-developed world is a major—and increasingly serious—consequence of the so-called green revolution which has deprived large numbers of peasants from work in agricultural production, so that they gravitate to the cities—which goes to show that it does not necessarily follow that what is good for the United States is good for Katmandu.

An international code of business practices is theoretically feasible, at least among the Western developed countries because their interests are commensurate. However, I wonder how far we would go on this with Japan.

And as Communist countries expand their operations on the international scene, with their different cost accounting, labor and welfare policies, it is doubtful that a purely Western code of business practices can stand up, particularly if their claim to most-favored-nation treatment is granted.

Thus, it appears, unfortunately, that our ability to accomplish the organization of the world into a rational legal framework with enforcement powers is very limited indeed.

For this reason, I come to a restructuring of our negotiating posture vis-a-vis the rest of the world so we can achieve some of these objectives from a position, stronger position of economic influence.

Representative WIDNALL. Professor Rolfe, did you want to comment?

Mr. ROLFE. Yes. May I just comment on that? I think in defense, if I may, of the Kindleberger position there is a great danger in overaggregating what you are going to multinationally survey. The brutal fact is, whatever the moralities to the contrary, that the economic integration, the vast huge flows of investment back and forth that we see, are primarily phenomena of the developed world and when you talk about the developed world you are talking about literally a handful of countries which have in the past in some cases evidence willingness to engage in cooperative activity. I do not think that the probability of future cooperation is totally nil, especially if you limit your purview to where the action is, so to speak.

I quite agree that the less-developed countries are another matter. You have held another set of hearings here and I think that the thinking in this area is advanced if one departs from the conventional morality and divides the world into two separate areas, one developed and one underdeveloped. I agree that you are not going to get very far on trying to make the whole world a rational market legal system. It is extraordinarily difficult. And I would also say that there are informal organizational structures as well as formal organizational structures to accomplish this in the developed part.

For example, if one looks at some of the changes in the attitude toward antitrust, if I may return to that, which have come pursuant to discussions within the OECD on that subject, it is really quite a remarkable change. It is true that there is a penchant for trusts in Europe. It is also true that there is a hell of a fight within the EEC now about this position, about the adoption of certain antitrust regulations, and my guess for whatever it is worth, would be that if a positive program of rationality were put forward, the chances of its adoption in Europe might very well be enhanced. I am not sanguine as to the chance elsewhere because the possibility of getting Peru and Brazil, for example, to cooperate, are small.

I think this is something we have almost got to try. The initiatives in the past have come from the United States. Even a failed initiative is better than no initiative and the United States is uniquely in the position, I think, to try that initiative.

Representative WIDNALL. Does either of the other members of the panel wish to comment on that?

Mr. STOBAUGH. My belief would be about like Mr. Rolfe's in that we have got to take the initiative. I am not sure that we will get an agreement within a relatively short period of time, but I think eventually we will.

In the meantime, it has been my observation that the nations themselves are getting a lot more expert in dealing with multinational enterprises, and that now the enterprises are facing a complexity of rules about what they can and cannot do, varying by each country as the countries gain more expertise in dealing with them.

For example, there is this possibility of granting credit to a subsidiary through intercompany loans. Well, some of the countries are now saying, you have to pay your bills to other intercompany subsidiaries within a certain date. They are putting credit restraints on multinational enterprise subsidiaries—the kind of restraint that does not apply to a national company. You have these things that are going on as the nations are learning to deal with multinational enterprises, but I think from the point of view of the United States and the multinational enterprise it would be better to have one set of rules rather than may sets of rules.

Representative WIDNALL. Mr. Istel, you made a persuasive case for changing our balance-of-payments accounting to include a balance sheet approach which would, I understand, prescribe our international assets and liabilities.

In your statement you calculate that our net worth on an international basis amounts to over $65 billion. On the other hand, you state there is enough similarity between the Penn Central situation and ours, long-term assets against short-term liabilities, and I quote, "to cause at least some mild anxiety in money matters."

Is not this latter fact really the most important one?

Mr. ISTEL. To the degree that the U.S. dollar is used as an international money, and that you have $35–$40 billion of Eurodollars which are short, convenient short-term money market instruments held in dollars for the structural and practical convenience that they offer, you have the problem that I have alluded to of the short-term liabilities. What I was trying and I think I did go on to say was that, therefore, the confidence factor and the overall approach that we took is particularly important at this time because we do not want these dollars to suddenly flow into other currencies which could have some very serious effects on international commerce.

On the other hand, I think the facts of life are that as I also suggested, if we were to try to take some of our long-term assets and render them liquid, if IBM World Trade, or Ford or General Motors in Germany, were to decide to sell a substantial portion of their non-American companies into the European capital markets, it would certainly be a salable and attractive security. All of a sudden—I am just following the example—if they repatriated those funds in all the ways in which we look at this—you would have diminished a long-term asset, would have cut down the book value of our assets by whatever amount you sold, but you would have increased your short-term assets.

So that I think once again, it is a question of time and confidence. If confidence were totally lost in the dollar in the short run it is only the short-term liabilities that count. Over a longer period of time and under more normal circumstances, the amount of long-term substantial revenue-producing assets is probably more important. One also must remember the liabilities are much easier to count. If you owe something to somebody or the BIS does a study of the Eurodollar market, they can count reasonably accurately what the liabilities are. To estimate the value of assets is much more complex, but I for one, would rather see the United States have taken that initial dollar and instead of having lent it to somebody, have had somebody like IBM invest it in Europe.

I think the accrual of assets and the eventual income return over a a period of time is likely to be much greater. It does not prevent the point that you raised and that I raised with you, that on a short-term basis you must maintain sufficient confidence that people do not call your short-term loans.

Representative WIDNALL. Well, do you really believe that a change in our balance-of-payments accounting would be able to ease the anxiety cased by our investor position?

Mr. ISTEL. No, and I was not really suggesting a change in the balance-of-payments accounting. I was suggesting a supplement to it. In other words, that I think you should look at it as an integrated whole. We have very good, or at least reasonably good, flow figures. I did not know about Mr. Polk's statement but we have had very cursory up to now balance-sheet accounting. The report of the Council of Economic Advisers does present some 1968 figures in that respect but I just think that they have got to be developed more completely, looked at on both a private and governmental basis separation (which Mr. Rolfe also mentioned) looked at as balance sheets and as flows, and then form some kind of integrated idea as to both what our short-term policy should be in these regards and our longer term policy should be in these regards. And the same way that if somebody were analyzing a company, I do not think they would want to look at either one, just the profit-and-loss statement or balance sheet, but they try to look at the two together to decide what the best financial policy should be and that is what I was suggesting.

Representative WIDNALL. In describing a proposal for the reform of the international monetary system such as the widening of bands or crawling pegs, Mr. Stobaugh makes a point that international private bankers are reluctant to make the system more flexible for they doubt the ease with which adequate forward markets could be maintained in foreign countries. Mr. Stobaugh comments, however, that such basics underestimate the flexibility of private financial institutions. Mr. Istel, would you comment on his statement and conclusions?

Mr. ISTEL. Well, far be it from me in any case to raise my voice against the ingenuity of private bankers but I do really think Mr. Stobaugh is generally right, that the forward market that would develop would be much more effective and much larger than people now think.

I do think, however, that we should not ignore the fact that to the degree that this is so, to the extent that Professor Stobaugh is right, the interlinking of the capital markets will become even more integrated and even deeper and I do not know to what extent all the world's major nations are ready to live with the consequences of that event.

If you have performing forward exchange markets, very large and effective forward exchange markets of course, then it no longer really matters what currency you are borrowing in now because you can obviously protect yourself vis-a-vis wherever your main currency is. The result would be an even deeper penetration of the so-called international market of Eurobond or Eurodollar markets into the national markets and, as I say, I do not know how ready everybody is for that.

Representative REUSS. Mr. Stobaugh?

Mr. STOBAUGH. Could I go back to one prior question—I did not realize we were leaving that subject—and that is the possibility of

General Motors', Ford's or IBM's selling stock in their French, German, or United Kingdom subsidiaries.

I think from a balance-of-payments point of view, you can raise a question and say, well, look, we could sell these, but I think that is one of the problems of being so preoccupied with balance of payments, because if you did something like that, you would do massive harm to the efficiency of the world, and to the world industrial system, because one of the things that gives Ford the industrial power it has is it ability to manufacture in the United Kingdom and ship the parts to Germany for assembly, and vice versa.

Now, as soon as you start getting a lot of stockholders in Germany in a German subsidiary and a lot of stockholders in Britain in a British subsidiary, then you are going to make these flows of parts much more difficult for the parent company to effect or for the subsidiaries to effect between themselves, because of this very great problem of transfer pricing.

Mr. DANIELIAN. May I also interject the thought that this is an admission of what I warned about, that what this new accounting system implies is a balancing of private assets abroad against public liabilities. Again I say that we cannot let the Government keep on building up deficits abroad, which is the source of the dollars floating around the world, and then expect the private companies to say, all right, take my IBM investments in France and some other place and pay for them. I am always concerned with who ends up with the marbles, and as long as we continue building up these deficits, we are going to lose the marbles.

Mr. ISTEL. If I may just add, I was not at all advocating the sale of these shares. I was trying to use it as an illustration of the fact that that potential exists, that the conversion from a long-term asset to a short-term asset was at least theoretically potentially possible, that in fact, not only would the American companies not want to do it but I am sure the Europeans would be very reluctant to own just a minority, overall minority stake in these companies and have these massive demands made on their capital markets which they would like to reserve for their own national priorities.

I was pointing it out to indicate that the problem, perhaps, of the short-term debts was not in the long run as long as we maintain confidence, as serious as it seemed because nobody would even want us to take those measures which would solve the short-term, long-term problem.

Mr. ROLFE. I am in advocacy of this kind of balance sheet and I would like to say one must not overstate its value. Just in commonsense terms if you talk to a European banker and he tells you how terrible things are, you can turn that conversation around 180 degrees in 2 minutes by getting him on to the assets, and it is largely a kind of psychological trick, but nevertheless, it is a psychological trick, if you like, based on a real situation which our present data hides. You can ferret the things out but you have not to work like the devil and in most balance-of-payments accounts of other countries you cannot ferret it out. And I am saying you know it is time we put it forward.

But in a general way I would like to agree very heartily with Mr. Danielian, that the basic problem here is the deficits in the public expenditures, in the public sector. I think most analysts have in the past used a kind of semantic of acquiscence which said, yes, the public sector will spend what it will and then the private sector must hustle along and overcome those deficits. But what is happening in this committee and in the thinking of economists and in the thinking in general in this country is that maybe the public sector really ought to live within some bounds of resources or ought to make policy decisions which are not quite as free as they have been in the past with respect to creating deficits abroad.

I think it is a tremendous burden on the private sector to say you overcome whatever we choose to spend, and we will count your assets as sort of ransom. I think this is absolutely true and this is a very essential and key point—I tried to make it—that somehow public expenditure sectors have got to be under constant surveillance.

Representative WIDNALL. This is not truly apropos of what we are talking about but the thought just occurred to me, I still do not fully understand the dollar-Eurodollar transactions in the markets. But as I believe it happens, actually the assets are there for the same institution, the American institution, and their foreign subsidiary or foreign bank that is attached to them, and they can if they want, borrow Eurodollars at 11 or 12 percent because things are not available in their own bank here, but actually, it is just a bookkeeping transaction on the part of the bank in America. Now, am I wrong?

Mr. ROLFE. No. I think they are borrowing assets that belong to somebody else. I do not think it—perhaps Mr. Istel ought to comment on that but it is not simply a bookeeping transaction in the sense it is their own money on both sides of the balance sheet. I think they are going into the markets and saying to Arab sheiks and central banks and what not, you lend it to us and we will pay you x percent, and they sometimes bring it back to the United States. These are very real assets, money created by American deficits—it depends on who you listen to—and if you listen to Milton Friedman, he says it is all a bookkeeping trick, but whatever it is, those are real assets owned by somebody other than American persons or corporations, trusts or individuals. That is a real borrowing transaction.

You may want to comment.

Representative WIDNALL. They are deposits in a U.S. bank abroad, are they not?

Mr. ROLFE. Some. Sometimes they are in foreign central banks.

Representative WIDNALL. Cannot that interest rate be very easily manipulated?

Mr. ISTEL. It is a very large and reasonably competitive market. The latest figures are somewhere around $35 billion, $40 billion for Eurocurrencies. The $35 billion may be roughly for the Eurodollar market, and that represents all the non-U.S. persons who would rather hold their short-term instruments in dollars which includes a tremendous variety of holders, of course, ranging from governments, governmental agencies through corporations and through private holders. And the supply and demand for that market works quite well. It is a very competitive market. It has been largely influenced, I would add, in the last year or so by the repatriation of some of these dollars back to the United States, meaning the foreign branches of

American banks bidding for these dollars, obtaining the deposits and relending them back to the United States to get around the problems of the stringency of domestic U.S. policy, and of regulation Q, so, since the American economy is so powerful and the American banks so credit worthy they have been able to exert an overall very important effect on the interest rates particularly in the last year or so, though in the last 3 months as we know, that total has not really changed appreciably.

Representative WIDNALL. To what extent are the moneys involved influenced by the deposits or swinging around of deposits of corporate treasurers of a major nation searching for the highest interest rates, winging from one place to another? Is much of that done between the dollar market and Eurodollar market?

Mr. ISTEL. Well, all the major large international corporations that are direct investors abroad are subject to the Office of Foreign Direct Investment which has regulations that govern their liquid balances at yearend from year to year and which is designed specifically to inhibit an American corporation from moving liquid balances from the United States abroad in order to seek higher interest rates. Is that not right, Mr. Stobaugh?

Mr. STOBAUGH. Yes.

Mr. ISTEL. Maybe you would like to comment.

Mr. STOBAUGH. No. I think that is right.

Representative WIDNALL. During the course of the year they can do a lot of things.

Mr. ISTEL. During the course of the year they can and do. I might just add that in examining these balance sheet figures, certainly the growth in assets is understated so that the no-net increase in our net investor position over the last few years may not be correct. But it is certainly true, I think, that over the last 2 or 3 years the very large borrowings by American corporations abroad have probably offset to a very large extent even if not completely, the accrual of values on the asset side.

The problem is that lately as the rates have risen very sharply, and as there has been less confidence in the dollar, the borrowings have become more and more short term in the Eurodollar market rather than founded through long-term bonds, and this represents a potential outflow (the way we measure the balance of payments) that we did not have a few years ago.

Not only have our private borrowings increased very substantially but their average maturity has probably been declining quite rapidly in recent years.

Representative WIDNALL. I just have one further question. I would like to address it again to you, Mr. Istel. Any corporate treasurer of an international business must take great care in protecting the corporation's cash balances against the parity changes in the currencies in which he deals. At the time of the 1969 German and French currency reevaluation, several financial commentators concluded that much of the hot money which fed the speculative fires was in fact the work of corporate treasurers doing their job. Do you believe that there should be some sort of controls put on this kind of activity?

Mr. ISTEL. No, I do not. I do not think so. I think that the currency flows that come from this kind of movement are to a large extent inevitable. They are people protecting their assets in terms of whatever thir main currency is.

I would add that the nonfinancial flow measures that are used to protect against such threats of devaluation are probably even greater than the financial flows. An example would be that when the corporate treasurer with a subsidiary in France thought the franc was going to be devalued, he probably built up very substantially his inventories in France and borrowed short-term francs against the inventories, which does not show up as capital flows—the so-called leads and lags—and I think this is a part of international commerce with which we will have to learn to live.

Representative WIDNALL. Well, then, do you believe that reform of the exchnge rate structure could reduce the need for corporate treasurers to engage in this kind of hedging?

Mr. ISTEL. If I understand the question correctly, if we move to wider parity bands—2 percent on each side of the parity rate instead of three-quarters, as now—I would guess that the amount of hedging that would go on might be greater, not less, unless it were already reflected in the relevant interest rates.

Representative WIDNALL. Do the others on the panel react the same way?

Mr. ROLFE. I presonally do not. It seems to me that the problem for the corporate treasurer is to anticipate two things. First of all, a growing tension in the currency situation, and then a walloping devaluation or revaluation because nobody does it until after all the tension has built up and everybody is screaming and the treasurer has been fired and whatnot, and consequently, they are under enormous tension to beat this shift in the peg.

Now, supposing you had preannounced crawling pegs, for example, of x percent per month. I do not think it really pays them to speculate in the same way because the concomitant of these crawling pegs by most of the literature's admission is a shift in the interest rate to accommodate that. Consequently, the net value of the money is offset hopefully equally by shift in the interest rates and it, therefore, becomes a zero gain to shift money around. Speculation (or defense—the same thing) does not make that much sense.

You know what is going to happen, you know what is going to happen with respect to the interest rates. You are not banking on a 10-percent devaluation of the franc or a 10-percent, even if it floats up to 10 percent, increase in the mark. You have a much—sort of steadier road ahead.

I would think that in terms of the corporate treasurer's net return considering interest as well as capital accounts, he would tend not to have to anticipate so much.

Mr. ISTEL. I would agree to that on the crawling peg. I am not so sure I would on the wider bonds—4 or 5 percent.

Mr. ROLFE. It depends on what happens in the course of the movement.

Mr. STOBAUGH. I think we need to open up another factor that the corporate treasurer sees. Again, he is not the economic man getting the last cent out of his business. One of the things he wants to do is protect himself against devaluation loss because, under our accounting conventions, a devaluation loss typically shows on the company balance sheet at the end of the year and somebaody on the board of directors says, why did you lose a million dollars in the sterling devaluation?

Now, if that same corporate treasurer spends a million or a million and a half dollars in hedging or in higher interest rates, it never appears on his balance sheets at the end of the year. That action is fine with the board of directors. They do not know anything about it. Expenses are just a little higher but you know out of all the millions they deal with they do not know about that other million or so.

So, as long as we use accounting procedures similar to those we do now, I think we are going to see corporate treasurers worried about devaluation losses. They probably worry about them more than they should worry about them.

The other thing I wanted to mention concerns hedging activity; there are various things that corporate treasurers can do to protect themselves against devaluation and a lot of them do relatively little, contrary to what a lot of observers of multinational enterprises think. But some of them do—they build up inventories, for example. But this use of hedging in foreign exchange markets is quite all right with most governments; and the big hedges that are done by the big companies—and really we are talking about a few big companies that are most feared by the nations—are sanctioned by the government. If a big company goes into a forward market very frequently the government is the one that indirectly under the current system supports this foreign currency sale. In other words, if a big oil company has $50 or $100 million worth of sterling that it wants to transfer back as dividends to the United States, 3 months hence, and it goes into the sterling forward exchange market, you can bet the United Kingdom Government knows all about it and in effect, gives its blessing for the company to do so.

Now, that type transaction in which a company participates in the forward market is an entirely different type of transaction than taking all of your cash and moving it to francs, marks, or dollars every week or every month. So, I think we need to distinguish between the firm that is operating in a normal market and the other that generates very large financial flows for purely speculative reasons.

Representative WIDNALL. Thank you very much.

Mr. Chairman, that is all.

Representative REUSS. Thank you, each of you, for your most helpful contribution.

The subcommittee will now stand in adjournment until 10 o'clock tomorrow morning in this room.

(Whereupon, at 12:25 p.m., the hearing was recessed, to reconvene, at 10 a.m., Thursday, July 30, 1970.)

A FOREIGN ECONOMIC POLICY FOR THE 1970'S

THURSDAY, JULY 30, 1970

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON FOREIGN ECONOMIC POLICY
OF THE JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The Subcommittee on Foreign Economic Policy met, pursuant to recess, at 10:05 a.m., in room S-407, the Capitol Building, Hon. Hale Boggs (chairman of the subcommittee) presiding.

Present: Representatives Boggs, Reuss, and Moorhead; and Senators Symington, Javits, and Percy.

Also present: John R. Stark, executive director; John R. Karlik, economist; Myer Rashish, consultant; and George D. Krumbhaar, economist for the minority.

Chairman BOGGS. The subcommittee will come to order.

Today is the last in the current set of hearings scheduled by the Subcommittee on Foreign Economic Policy to study the effects of direct investment and the problems raised by the rapid growth of multinational corporations over the past decade. Although this is our last session, it may well prove to be the most exciting, both because of the exceptionally strong panel of witnesses who have agreed to testify and because we are concentrating on the legal and political conflicts arising from the activities of multinational companies.

These disputes generally arise over such issues as antitrust policy, trading with the enemy, tax avoidance through the manipulation of transfer prices, the location of manufacturing plants, and borrowing by foreign firms in national capital markets. I am sure that today's panel will have a number of useful suggestions on how to deal with these issues.

We have a very distinguished panel today composed of, first, Professor Hymer, who is professor of economics at Yale University.

We are very very happy to welcome you here, doctor.

Second is one well known to all of us, Mr. Seymour J. Rubin, who formerly served as general counsel of the Agency for International Development, and for some years as our representative at the DAC.

Mr. Melville H. Watkins, professor of economics at the University of Toronto—we are very happy to have a representative from Canada here this morning because we have a few questions about Canada—and head of the Task Force on the Structure of Canadian Industry. The report issued by this task force is popularly referred to as the Watkins Report in honor of our distinguished visitor.

And finally, and certainly not least, is Jean-Jacques Servan-Schreiber, who is the publisher of one of the great magazines in France, and also the author of "The American Challenge," and recently elected deputy in the French National Assembly.

He advised us that he would be a bit late, and that we should proceed, which we shall do.

Our first witness this morning is Mr. Hymer.

STATEMENT OF STEPHEN HYMER, PROFESSOR, ECONOMIC GROWTH CENTER, YALE UNIVERSITY

Mr. HYMER. I think I would prefer to make just a few remarks orally and to put my prepared statement into the record.

Chairman BOGGS. Yes. And it would be very helpful if all of you could do that. And your prepared statement will be made a part of the record.

And let me say that any statement that any member of the panel would like to submit after the panel, that is, within a period of 30 days, will be made a part of the record.

Mr. HYMER. Thank you.

I took as my theme a quotation from John Powers, president of the Pfizer Corp. that "Practice is ahead of theory and policy," with regard to the multinational corporations. What I take him to mean is that the actual business practice of multinational corporations are creating a new world economy. And that he feels policymakers and theoreticians are lagging behind, sometimes serving as obstacles rather than as aids in the construction of this new world economy.

Foreign investment is now growing, and has been growing for the last 10 or 20 years, at the rate of 10 percent a year. If it continues this way for the next 30 years it will profoundly change the structure of the world economy. Such a change would require a correspondingly radical change in the political and economic structure of the world, even including the withering away of the State, as George Ball has been arguing.

The question arising is, "Will the multinational corporations be able to mobilize the political power necessary to bring about this kind of reconstruction of the world economy?"

I think the best way to start answering that question is to look at the practice of the multinational corporations and to see what is in store for us.

On the one hand the multinational corporations spread capital, technology, and management ability throughout the world. In this sense they are integrators, and perhaps a very powerful force for spreading the industial revolution to backward countries, and also for bringing American technology and practice to other developed countries.

But the movement of the multinational corporation is a double movement. They spread, but they also centralize control. With every outward decentralizing movement of the corporation there occurs a centralizing movement by the formation of instruments of coordination and control at higher level to plan the strategy of the organization.

This creates a stratification within the corporation of levels of decisionmaking. The corporation is in fact a pyramid. In the case of the multinational corporation, its base spreads over the whole world. As this happens its control tower at the center rises to become stronger and more powerful.

Centralization of command within a corporation has a correspondence in centralization of control in the world economy. We can think of the corporation as consisting, for simplicity, of three levels of organization; a bottom level—the operating level—where the actual manufacturing occurs; a second coordinating level, and a high-strategic level. Each of these levels has different location characteristics. The operations level is spread widely throughout the continental United States in the case of American firms, and throughout the world in the case of multinational firms.

Coordinating levels, however, are confined to key cities. And strategy levels are typically concentrated in one major spot, such as New York, for the very important reason that this is where the top people can communicate with each other most readily.

If we apply the scheme to the world economy, where some people feel we will soon have a regime of 300 or 400 multinational corporations controlling 60 or 70 percent of the world industrial output. We can also expect a centralization of higher level activities in a number of key cities, capital cities, surrounded by regional subcapitals and lesser towns and villages. If one had to guess, I think the best bet is that the capital cities would be Tokyo, New York, London, Paris, and Frankfort; these, along with Moscow and probably Peking, would form the strategy capitals of the world; that is, places where one can raise a hundred million dollars for a major project.

A number of regional subcapitals—Montreal, Buenos Aires, and Singapore for the Pacific, and so forth—would serve as coordinating headquarters, for various divisions; other parts of the world would deal with the lower level operating problems of the economy.

Such a structure would, of course, have important implications for the whole range of human activity. Income would tend to be highest at the capital cities and then radiate outward on a declining curve to all the other cities and towns. Consumption patterns and tastes would be set in the major cities, and other cities would copy. Top decisions, those requiring the highest knowledge, would take place in central cities. Lesser cities would deal with lesser problems.

Since the multinational corporations tend to be large firms in whatever country they operate, the whole character of the country would tend to take on the attributes of the level of decisionmaking with which it is associated. This means that most of the world outside the major capitals, and perhaps some of the subcapitals, would really be branch plants cities engaged in middle management activity.

What we would get is an international division of labor that is vertical, where certain places do higher level activities and other places do lower level activities.

How far along are we?

The very rapid growth in Europe following the formation of the Common Market in particular, and the general recovery from the Second World War in general, created, I think, an important challenge to the large American corporation, which found itself losing its share of the world market, but was able to respond by investing in Europe and gaining a share of the European market.

This in turn created a challenge for European corporations, who responded by merging and amalgamating and, I think, beginning to engage in foreign investment.

Over the next few years one probably can expect an expansion of European foreign investment, first in Europe, but also in Latin America, Asia, and Africa, and even in the United States.

If European firms become more multinational, and if American firms continue investing abroad, we will create a number of large North Atlantic corporations no longer tied specifically to any particular nation. Many American corporations now have 20 to 30 percent of their sales and often 40 to 50 or 60 percent of their employees are citizens of countries outside the United States.

One can easily imagine this continuing without a recurrence of serious disagreements between European countries such as the ones which characterized most of the century and resulted in two wars.

However, a number of problems remain, the first being that Japan is not by any means fully integrated in this system. It has not allowed inward investment. And I am not sure that the Japanese economic system could develop towards multinationalism in the way the North Atlantic system would because of its special interface of business and government.

Chairman Boggs. Can you sum up now, Professor?

Mr. Hymer. Well, I will just talk briefly about the position of the United States.

I think that what this involves for the United States is first of all perhaps a lessening of its autonomy and greater dependence on the world economy.

More than that, I think it involves an increased cleavage between the large firms which are multinational and other firms which are not. Such a cleavage comes up, for example, in the case of balance of payments, where those firms which can meet the challenge of foreign competition through foreign investment want freedom to invest abroad, and those firms which can only do it through export want restrictions on investment.

Similarly a cleavage arises between firms and labor. Labor cannot escape the country to meet challenges as capital can. Also over taxation: large multinational firms have flexibility for escaping taxation, that national firms do not have. These cleavages can be expected to grow as investment grows.

My final point is that because multinational corporations are associated with a system of stratification and hierarchy, they require a great deal of political power to support them.

Since the United States is at the center, the burden of maintaining in equality and protecting the investment of the corporations would fall to the United States and these costs are likely to increase greatly through time.

(The prepared statement of Mr. Hymer follows:)

PREPARED STATEMENT OF STEPHEN HYMER[1]

The Multinational Corporation and Uneven Development

SUMMARY

1. The multinational corporation, because of its great power to plan economic activity, represents an important step forward over previous methods of organiz-

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ing international exchange. It demonstrates the social nature of production on a global scale and as it eliminates the anarchy of international markets and brings about a more extensive and productive international division of labor, it releases great sources of latent energy.

2. But the multinational corporation is still a private institution with a partial outlook and represents only an imperfect solution to the problem of international cooperation. It creates hierarchy rather than equality, and it spreads its benefits unequally. As it crosses international boundaries, it pulls and tears at the social and political fabric and erodes the cohesiveness of national states.

3. Whether one likes this or not, it is probably a tendency that cannot be stopped. Through its propensity to nestle everywhere, settle everywhere, and establish connections everywhere the multinational corporation destroys the possibility of national seclusion and self-sufficiency and creates a universal interdependence.

4. This applies to the United States as well as to other countries. Continued growth of U.S. direct foreign investment at its present rate of 10% per year implies an increase cleavage between international and national interests, i.e., more dependence upon the world economy, greater difficulty in controlling large corporations, and greater involvement in maintaining law and order to protect international private property.

5. However, in proportion to its success, the multinational corporation leads other groups, particularly labour and government to mobilize their power; it creates counterforces in the form of conflicts within major centers, between major centers and between the major centers and the hinterland.

6. The present crisis may well be more profound than most of us imagine, and the West may find it impossible to restructure the international economy on a workable basis. One could easily argue that the age of the Multinational Corporation is at its end rather than at its beginning. The present hearings may be the epitaph of the American attempt to sustain the old international economy, and not the herald of a new era of international cooperation.

The Coming Crisis of the Multinational Corporation

Since the beginning of the Industrial Revolution, there has been a tendency for the representative firm to increase in size from the *workshop* to the *factory* to the *national corporation* to the *multidivisional corporation* and now to the *multinational corporation.*

Until recently, most multinational corporations have been from the United States. Now European corporations, as a by-product of increased size, and as a reaction to the American invasion of Europe, are also shifting attention from national to global production and beginning to "see the world as their oyster." If present trends continue, multinationalization is likely to increase greatly in the next decade as giants from both sides of the Atlantic (though still mainly from the U.S.) strive to penetrate each other's markets and to establish bases in underdeveloped countries, where there are few indigenous concentrations of capital sufficiently large to operate on a world scale. This rivalry may be intense at first but will probably abate through time and turn into collusion as firms approach some kind of oligopolistic equilibrium. A new structure of international industrial organization and a new international division of labor will have been born.

So profound a change in economic structure will require correspondingly radical changes in the legal, political and ideological framework. At present "Practice is ahead of theory and policy," as John Powers, President of the Charles Pfizer Corporation has put it. Multinational Corporations, through their everyday business practice are creating a new world environment, but policy makers (and theoreticians) are lagging behind.

In other words, the situation is a dynamic one, moving dialectically. Right now, we seem to be in the midst of a major revolution in international relationships as modern science establishes the technological basis for a major advance in the conquest of the material world and the beginnings of truly cosmopolitan production. Multinational corporations are in the vanguard of this revolution, because of their great financial and administrative strength and their close contact with the new technology. Governments (outside the military) are far behind, because of their narrower horizons and perspectives, as are labor organizations and most non-business institutions and associations. Therefore, in the first round, multinational corporations are likely to have a certain degree of success in organizing markets, decision-making, and the spread of information in their own interest. However, their very success will create important tensions and conflicts which will lead to reactions by other groups.

Thus, whether foreign investment can continue to grow at 10% per year, as it has for the past twenty years, with the drastic implications such an expansion has for world order, is an open question. Economic factors, in the sense of an expanding world market, are favorable. Political factors are a different matter. Since economic power cannot long be out of phase with political power, multinational corporations must mobilize political power, or they will not be able to create the new world economic order we hear so much about.

Uneven development

Suppose giant multinational corporations (say 300 from the U.S. and 200 from Europe and Japan) succeed in establishing themselves as the dominant form of international enterprise and come to control a significant share of industry (especially modern industry) in each country. The world economy will resemble more and more the United States economy, where each of the large corporations tends to spread over the entire continent and to penetrate almost every nook and cranny. What would be the effect of a world industrial organization of this type on international specialization, exchange and income distribution? To what extent would it perpetuate the present system of uneven development, i.e., the tendency of the system to produce poverty as wealth, underdevelopment, as well as development?

The growth of firms involves a double movement; differentiation and organization, decentralization and centralization. On the one hand, the multinational corporation because of its power to command capital and technology and its ability to rationalize their use on a global scale, will probably spread production more evenly over the world's surface than now is the case. At the same time, it will tend to centralize strategic decisions in regional coordinating centers and in corporate headquarters. Horizontal expansion of corporations through the world will be accompanied by a vertical differentiation of levels of command (symbolized by the corporate skyscraper) and a stratification of employees from operatives to executives, with wide differences in authority, status, remuneration, horizons, mobility, mental demands and development.

The spatial or geographic implication of the corporate structure lies in the close correspondence between the centralization of control within the corporation and centralization of control within the international economy. A system of North Atlantic Multinational Corporations would tend to produce a heirarchial division of labor between geographical regions corresponding to the vertical division of labor within the firm. It would tend to centralize high-level decision-making occupations in a few key cities in the advanced countries, surrounded by a number of regional sub-capitals, and confine the rest of the world to lower levels of activity and income, i.e., to the status of towns and villages in a new Imperial System. Income, status, authority, and consumption patterns would radiate out from these centers along a declining curve, and the existing pattern of inequality and dependency would be perpetuated. The pattern would be complex, just as the structure of the corporation is complex, but the basic relationship between different countries would be one of superior and subordinate, head office and branch plant.

One would expect to find the highest offices of the multinational corporations concentrated in the world's major cities—New York, London, Paris, Hamburg, Tokyo. These along with Moscow and perhaps Peking, will be the major centers of high-level strategic planning. Lesser cities throughout the world will deal with the day-to-day operations of specific local problems. These in turn will be arranged in a heirarchial fashion: the larger and more important ones will contain regional corporate headquarters, while the smaller ones will be confined to lower level activities. Since business is usually the core of the city, geographical specialization will come to reflect the hierarchy of corporate decision-making, and the occupational distribution of labor in a city or region will depend upon its function in the international economic system. The "best" and most highly paid administrators, doctors, lawyers, scientists, educators, government officials, actors, servants and hairdressers, will tend to concentrate in or near the major centers.

The new economy will be characterized by a division of labor based on nationality. Even within the United States ethnic homogeneity increases as one goes up the corporate heirarchy; the lower levels contain a wide variety of nationalities, the higher levels become successively more pure. A similar phenomenon will probably develop on a world scale as firms try to balance the need for adaptation to local customs and circumstances with a centralized strategic point of view.

Day-to-day management in each country will be left to the nationals of that country who, being intimately familiar with local conditions and practices, are able to deal with local problems and local government. These nationals remain rooted in one spot, while above them is a layer of people who move around from country to country, as bees among flowers, transmitting information from one subsidiary to another and from the lower levels to the general office at the apex of the corporate structure. In the nature of things, these people (reticulators) for the most part will be citizens of the country of the parent corporation (and will be drawn from a small culturally homogeneous group within the advanced world), since they will need to have the confidence of their superiors and be able to move easily in the higher management circles. Latin American, Asians and Africans will at best be able to aspire to a management position in the intermediate coordinating centers at the continental level. Very few will be able to get much higher than this, for the closer one gets to the top, the more important is "a common cultural heritage."

The multinational corporate system thus does not seem to offer the world national independence or equality. Instead it would keep many countries as branch plant countries, not only with reference to their economic functions but throughout the whole gamut of social, political and cultural roles. The subsidiaries of multinational corporations tend to be among the largest companies in the country of their operations; and their top executives play an influential role in the political, social and cultural life of the host country.

Yet these people, whatever their title, occupy at best a medium position in the corporate structure and are restricted in authority and horizons to a lower level of decision making. The governments with whom they deal tend to take on the same middle management outlook, since this is the only range of information and ideas to which they are exposed. In this sense, one can hardly expect such a country to bring forth the creative imagination needed to apply science and technology to the problems of degrading poverty.

CORPORATIONS AND NATIONS

"For a worldwide enterprise, national boundaries are drawn in fading ink.," wrote *Business Week* (February 17, 1968), as a headline with reference to George Ball's now famous argument that corporations are modern institutions and nation states are old fashioned institutions rooted in archaic concepts. What does this mean in particular for the United States, the most powerful nation state of all?

In the first place, one should note that the conflict is not really between corporations and nation states, but between groups of people within corporations and nation states struggling over who decides what and who gets what, i.e., between big multinational corporations over the share of the world market, between big business which is internationally mobile and small business and labor which are not; between the middle class of different countries over managerial positions, between high wage labor in one country and low wage labor in another; and between excluded groups and elites within each country over the direction development is to take.

The importance of these conflicts depends upon the scale of foreign investment. The rapid growth of U.S. foreign investment over the last twenty years has already revealed certain cleavages between the interests of international investors and the rest of the domestic economy over taxation, balance of payments, extraterritoriality, and foreign aid. For example, multinational corporations have pressed for relief from taxation on foreign income and from regulation by antitrust and other laws. They would like the United States to adjust its balance of payments by deflating the economy or controlling imports rather than controlling foreign investment. At the same time, they would like freedom to produce where costs are lowest, unhampered by tariffs and trade. On these issues they conflict with other domestic taxpayers who wish equal taxation for foreign income; firms who cannot meet the challenge of foreign competition through investment but must rely on exports or on the domestic market; and certain classes of labor threatened by foreign competition.

These types of problems will grow as foreign investment continues to grow. Three major types of complications are likely to emerge.

First, the United States will become increasingly interdependent with the world economy. The multinational corporation is a medium by which laws, politics, foreign policy and culture of one country intrude into one another. Already United States antitrust laws and balance of payments controls quickly feed into other countries via multinational corporations and then quickly react back on the United States government. More of this can be expected in the future, as the multinational corporation acts as a viaduct for transmitting pressure from one country to another, thus reducing the sovereignty of all nations and requiring the building of supranational institutions to coordinate policy and reduce conflicts. To many, this is its most positive feature.

Second, the ability to control large corporations will be reduced. Multinational corporations because of their world wide horizons and scope of operations have a certain flexibility for reducing the control of any one country over them. This applies to monetary policy, fiscal policy and a host of others, and is perhaps best illustrated by tax questions. In an environment of free capital movements and free trade, a government's ability to tax multinational corporations is limited by the ability of those corporations to manipulate transfer prices and to move their productive facilities from country to country. Countries become like cities competing for branch plants.

Third, because the multinational corporation is associated with world stratification and inequality in property, power and income, it creates a goal in those lower down the hierarchy to try to change it. This tendency is dampened to the extent that the system provides continuous improvement and opportunity for everybody. The multinational corporation, because of its dynamic qualities, has a certain stabilizing effect in this regard. But the available evidence indicates that it can provide some degree of participation for at most one third of the world's population. The remaining two thirds, who get only one third of income, gain little. And, along with the many dissatisfied of the upper third, present a continuous challenge. The United States, because of its special position, pays the largest part of the cost of maintaining the system in face of these challenges. These costs have been rising rapidly and may easily come to exceed any benefits the nation as a whole is alleged to gain from them (as opposed to the substantial gains accruing to the limited sector directly involved in foreign investment). At any rate, this is what happened to the British Empire.

Chairman BOGGS. Thank you very much.

Now, Mr. Watkins, if we may hear from you, sir.

STATEMENT OF MELVILLE H. WATKINS, PROFESSOR OF ECONOMICS, UNIVERSITY OF TORONTO, AND HEAD OF THE TASK FORCE ON THE STRUCTURE OF CANADIAN INDUSTRY

Mr. WATKINS. Your invitation, Mr. Chairman, suggested to us that we should try to assist you in the discussion of legal, social, and political questions caused by the growth of multinational corporations and I have two initial difficulties with that mandate. It is certainly very broad. And I do in fact want to talk very generally about the political situation, with particular reference to American ownership in Canada.

Chairman BOGGS. That is what we would like to hear about.

Mr. WATKINS. But I see two difficulties with that terminology. The major one is the question of what do we mean by a multinational corporation. And we are in danger of assuming away the most important question of all, which is, are so-called multinational corporations in fact multinational?

In my view the short answer is that they are not, that if they were, there would not be the tensions and conflicts between home countries and host countries which I would guess had some part in motivating these hearings. Multinational corporations have an address and a nationality, rhetoric and intentions notwithstanding, and what we should be talking about here are American corporations operating abroad.

The absence of genuine multinationality is most evident in the tendency for American corporations to bring American law with them, that is, the problem of extraterritoriality, and that causes my second difficulty, because I do not think myself that the legal problem is a fundamental problem. I think rather it is a symptom of the asymmetry of power that inheres in foreign direct investment, and that attempts to solve it in a vacuum are mostly irrelevant and futile. Extraterritoriality, or legal imperialism, is the tip of the iceberg or political control, and to eliminate it alone does not touch the base of the iceberg.

Now, it is well known, I think, Mr. Chairman, the extent of foreign ownership in Canada, and especially American ownership. About two-toriality, or legal imperialism, is the tip of the iceberg of political controlled by foreigners and about three-fifths of our secondary manufacturing industry; of this foreign control about four-fifths is American.

Our larger enterprises are typically in the hands of foreigners, as are the most dynamic sectors of our economy. The statistics I have been citing almost certainly underestimate the present extent of foreign ownership, because they are at least 5 years out of date. In the past 3 years there has been a merger movement in this country which has spilled across into Canada. And also there appears to be a built-in tendency for the giant corporation, whether owned at home or abroad, to extend its control.

Now, this is in no sense a new phenomenon for Canada. Indeed, we could argue that American corporations as they became national corporations in the late 19th century also became international or multinational, and they moved quickly to Canada because of its proximity. And the resulting process of Americanization of the Canadian economy has continued unabated through war and peace, boom and depression.

It might be thought to be self-evident that Canada benefited from this intrusion of capital, technology, managerial skills and so on, but this is not necessarily so. On the one hand, there is the problem of servicing foreign equity in perpetuity. It has been estimated that between 1960 and 1967, Canadian subsidiaries and affiliates sent $1 billion more to their parent companies in the form of profits, and $2 billion more if royalties, license fees, and management fees are included, than they received from them in the form of capital imports. Foreign direct investment results not in the export of capital but rather in a drain of surplus to the United States.

There is also the distinct possibility, if we look at the process of economic development, that the presence of foreign inputs simply replaces domestic inputs that might otherwise have taken their place. Foreign direct investment may make growth too easy, may build in dependence to an unnecessary degree. It is possible that the benefits for Canadians of foreign direct investment are more illusory than real, while the costs are all too real.

There will also appear to be a very specific moral here for us with respect to the resource industries, because the United States, as the advanced metropolis of the world, has come to rely heavily on imports of raw materials, and to a very considerable extent tries to minimize uncertainties of supply through American corporate ownership of foreign resources.

But these American advantages may be bought at heavy cost to the raw material exporting countries such as Canada. A very large economic rent, as the economists would put it, results from resource ownership, and this is alienated into foreign hands instead of being captured at home to aid in domestic development.

The further processing of raw materials and the jobs that result are more likely to take place in the United States when American corporations call the tune.

And also the resource industries—and I think here particularly of the Canadian case—are those industries in which we are most efficient, and they would be the industries in which it would make most sense for us to insist on Canadian ownership in order that we could do the kind of learning by doing in these industries that lies at the heart of economic development.

But looking at it this way, I think the most serious error that Canada as a resource-rich country has made is to permit widespread foreign ownership of its resources. And I think this point is particularly relevant at the present time when the United States is turning increasingly, looking increasingly, to the north, toward Canada, as a resource base.

Foreign ownership of the major industries of a country has, I think, major consequences for that country. In Canada we talk about the existence of a branch plant economy. We talk about how we tend to have the same number of firms that operate in most industries in the United States operating in Canada. We tend to have, say, the same number of firms producing refrigerators in the Canadian market as the United States with a much small market, and they tend to be inefficient, and they tend toward high cost and high prices to Canadians.

We can talk about the problem of research and development or R. & D. pending, which I think has already been dealt with at these hearings. And we know that there is a very strong tendency for research and development to be concentrated at the site of the parent company in the United States. And this threatens to cast countries like Canada perpetually into the role of being imitators rather than innovators.

But these effects do not stop there either. When your economy comes to be substantially controlled outside of the country, it becomes very complicated, indeed, to even have an effective national economic policy. What I have in mind here are the important problems of controlling inflation, of creating jobs, in general of affecting the rate of economic growth in Canada. And I think I can say that in the Canadian case the capacity o four government to do much in this area has been very seriously constrained indeed by the extent of investment and trade with the United States.

I think further that the existence of a branch plant economy leads to a branch plant quality in many other aspects of the lives of Canadians in our labor movement, in our universities, in our media. We tend to have our major corporations controlled outside the country. And this sets up a kind of pattern where we would not be surprised to learn, for example, that the labor movement comes substantially to be controlled by so-called international unions which are simply American unions operating in Canada.

We are not surprised to find that our educational system and our media become increasingly Americanized in order to train us for life within this kind of branch plant economy.

It might well be asked what kind of reaction there has been by Canadians, or from Canadians, while this has been happening. And the answer is that there has been surprisingly little until recently. But I think what has been happening very recently might be more indicative of what is happening in the future.

I think the reason this issue has not surfaced in Canada in spite of the long history of foreign ownership is essentially because the business class in Canada has a disproportionate amount of power, and that business class has been pretty thoroughly emasculated, and essentially Canadian businessmen work as managers of branch plants, and are not fundamentally interested in the question of independence.

I think the reason the issue has surfaced now could be related to a broad range of things that are happening in the world, to an increasing feeling, to some extent at least, to a feeling within Canada that the extent of Americanization has gone too far, and this particularly at a time when many people are questioning some of the activities of the United States, notably in Vietnam.

Now, what this has meant, in my view—and we can see very clearly how it happened—is a rising wave of nationalism in Canada. And there is no fact more important to the future of Canadian-American relations than this unexpected development of Canadian nationalism.

And in this context Canadian business leaders and Canadian politicians are being increasingly forced by the Canadian people to do something. And in fact things are being done at this very moment.

You have already made reference, Mr. Chairman, to a task force which I headed and which reported in 1968. We made a number of specific recommendations for changes in Canadian policy. These changes were mostly of a very modest nature.

That report was rejected at that time by the Government, in spite of the modest character of the recommendations.

But in the context of the increasing nationalism in the past 2 years the Government's hand has been forced, and new policies toward foreign ownership are expected to emerge shortly as legislation. And it would appear that these policies will be modeled in some considerable part on the report of that task force.

How much all of this will matter remains to be seen. The Canadian Government appears to act on this issue only when its hand is forced. And it is likely to do as little as it can politically to get away with.

I doubt very much that the new policies in Canada will do all that much. We are likely to end up with a somewhat more efficient and a slightly less dependent Canadian economy. But I see little threat to the American corporations from that kind of policy.

Even should Canadian reaction turn out to be stronger than I am predicting, its main thrust will still be to create a less dependent but still a capitalist economy, and that would, it would seem to me, offer no real threat to the American corporate interests.

There are, however, a number of Canadians, albeit not a majority, amongst whom I count myself, who will not be satisfied with thesse modest changes, and who have worked and will continue to work for a more radical restructuring. We will advocate that the more sensible alternate to private ownership of the Canadian economy is public ownership, a Canadian economy owned and controlled by Canadians for Canadians.

I do not wish to suggest that this point of view is going to prevail toworrow. But it is already on the agenda of Canadian politics, and is likely to become more relevant as time passes, as we find an increasing number of Canadians, like Americans, being turned off by the present system.

No demand, it seems to me, is more pervasive today than the demand for genuine democracy, for a control of our own lives. And no institution is more undemocratic and more vulnerable to the charge of authoritarianism than the giant corporation.

On the northern periphery of the American empire, a rising nationalism has to a degree unprecedented in Canadian history a strong anticapitalist and socialist component. This new anti-imperialist sentiment is, of course, to be found in the United States as well as in Canada, but the possibilities for its being translated into political action may be greater in Canada than in the United States because Canada does have a viable socialist tradition.

In the near future, Canadian policy toward foreign ownership is likely to continue to be articulated to meet nationalist demands, but the socialist content of these demands cannot be indefinitely contained. Public ownership has been used in the past to a considerably greater extent in Canada than in the United States; this difference could well become more striking in the future.

I may seem to have wandered far afield from what may have been the intent in inviting me here, but my point in saying these things is to emphasize that the heart of the problem of the multinational corporation is a political problem. And what the political problem seems to me to be about is, where are decisions made, and how are they made, and that the positive alternative to the multinational corporation would in fact be a democratic socialist economy.

My remarks have been motivated by the conviction that it is no longer enough to see the issue of foreign direct investment merely as how to minimize the tensions and conflicts created by American business abroad. It is time to seek out alternative futures and perceive the possibilities which they may hold. The American people as much as the Canadian people stand to gain from that exercise.

Chairman Boggs. Thank you very much.

(The prepared statement of Mr. Watkins follows:)

PREPARED STATEMENT OF MELVILLE H. WATKINS

I appear before you today as a professional economist who is a student of foreign direct investment in general and of foreign ownership in Canada in particular and who, in that capacity, headed a Government of Canada Task Force on foreign ownership in 1967–68. I also appear before you as a citizen of Canada, deeply concerned about the possibilities of survival of my country and with a bias toward viewing the United States from a foreign, specifically Canadian, perspective. Finally, I appear before you as a democratic socialist and political activist who is presently a Vice-President of the New Democratic Party and a founder of a new left caucus within that party, and who is inclined to have some serious doubts about the virtues of private foreign investment.

The invitation of your Chairman invited me to assist this Committee in considering "the legal, social and political implications posed by the growth of the multinational corporation and the spread of direct foreign investment". The broadness of the mandate offers a scope for which I am grateful, but I find two difficulties with that wording.

The major difficulty is that the very terminology "multinational corporation" assumes away the most important question of all, which is: are so-called multinational corporations in fact multinational? The short answer, in my view, is that they are not. Indeed, if they were, there would not be the tensions and conflicts between home countries and host countries which I would guess had some part in motivating these hearings. Multinational corporations have an address and a nationality, rhetoric and intentions notwithstanding, and what we should be talking about here are American corporations operating abroad.

The absence of genuine multinationality is most evident in the tendency for American corporations to bring American law with them, that is, the problem of extraterritoriality, and that causes my second difficulty. The quotation previously cited gives pride of place to the legal implications of foreign direct investment. My own feeling would be that that problem is simply a symptom of the asymmetry of power that inheres in foreign direct investment, and that attempts to solve it in a vacuum are mostly irrelevant and futile. Extraterritoriality, or legal imperialism, is the tip of the iceberg of political control, of that manipulation and exploitation which is imperialism proper. To imagine that eliminating extraterritoriality would remove this political cost is similar to believing that cutting off iceberg tips would make shipping less hazardous.

The massive extent of foreign, most American, investment in Canada is well-known. About two-thirds of our resource and primary manufacturing industries are controlled by foreigners and about three-fifths of our secondary manufacturing industry, of this foreign control about four-fifths is American. In the words of a 1965 Twentieth Century Fund study: "a very large and strategic part of Canada's industrial assets are owned and controlled by non-residents, much of them being directly controlled *via* the foreign parent-domestic subsidiary relationship. In addition such concentration tends to be in the larger enterprises and in industries whose growth prospects appear to be among the most dynamic in the whole economy. Indeed, the concentration is extremely heavy in various key export sectors as well as important sectors of domestic manufacturing industry both of which tend to be prime movers of the Canadian economy. To a very large extent therefore it appears that Canada's economic growth is increasingly dominated by nonresidents and will be strongly conditioned by decisions made by companies located in the United States and subject to U.S. laws, customs and activities." Since these words were written, U.S. ownership has risen, in part because the U.S. merger movement of the past decade has spilled across the undefended border, and in part because it is in the nature of the modern corporation to extend its control through its capacity to appropriate the surplus of the economies in which it operates.

Foreign direct investment is not a new phenomenon for Canada. Foreign capital settled Canada as truly as immigrants did. As American corporations went national after the Civil War, so also they went international and particularly to Canada, given its proximity. The process of Americanization of the Canadian economy has continued unabated through war and peace, boom and depression.

It might be thought to be self-evident that Canada benefitted from this intrusion of capital, technology, managerial skills and so on, but this is not necessarily so. On the one hand, there is the problem of servicing foreign equity in perpetuity. It has been estimated that between 1960 and 1967, Canadian subsidiaries and affiliates sent $1 billion more to their parent companies in the form of profits, and $2 billion more if royalties, license fees and management fees are included, than they received from them in the form of capital imports. Foreign direct investment results not in the export of capital but rather in a drain of surplus to the United States.

On the other hand, there is the distinct possibility that the absence of foreign inputs would have facilitated the growth of domestic inputs. Foreign direct investment results not in the export of capital but rather in a drain of surplus to the United States.

On the other hand, there is the distinct possibility that the absence of foreign inputs would have facilitated the growth of domestic inputs. Foreign direct investment makes growth too easy and builds in dependence to an unnecessary degree. On the assumption that the Canadian people are as innately clever and capable as the America people, the benefits for Canadians of foreign direct investment are more illusory than real while the costs are all too real.

I think there is an important moral here for all of us, Americans and foreigners, and it is that foreign direct investment is much less necessary to economic development outside the United States than is frequently thought to be the case.

Further, there would seem to be a very specific moral with respect to the resource industries. The United States, as the advanced metropolis, has come increasingly to rely on imports of raw materials, and attempts insofar as possible, to minimize uncertainties of supply and maximize the surplus appropriated by Americans through American corporate ownership of foreign resources. These American advantages are bought. however, at heavy cost to the raw materials exporters. The surplus that inheres in resource ownership is alienated into foreign hands instead of being captured by the exporting country to aid in its development. The further processing of raw materials and the jobs generated thereby are more likely to take place in the United States where American corporations call the tune. And the resource industries are exactly those industries in which the exporting country has a comparative advantage in trade and where it could most sensibly engage in that "learning by doing" which is at the heart of an on-going process of economic development.

From this perspective, the most serious error that Canada as a resource-rich country has made is to permit widespread foreign ownership of its resources. This is particularly the case now when Canadian resources are being viewed even more covetously than in the past by the United States.

Now foreign ownership of Canadian resources and industries has had profound and pervasive effects. To lose control of the economy is to lose control of the essence of our modern technological society. Widespread foreign ownership has reduced the Canadian economy to that of a branch plant.

The number of large American firms operating in any industry in Canada is typically the same as in the United States. The result is the fragmenting of markets, inefficiency, high costs and high prices to Canadian consumers. The fact that American corporations go everywhere and are typically profitable everywhere does not mean that they are efficient everywhere: indeed, the Canadian experience suggests that the opposite is more likely to be the case. As a minimum. the open door to American corporations should have a screen that keeps enough out to prevent this costly proliferation.

There is, then, in the language of the economist, a problem of static inefficiency. But there is also an equally serious problem of dynamic inefficiency. I understand that your hearings have already dealt with technology, and presumably therefore with spending on R & D. I would imagine that the point has already been made that R & D is typically highly concentrated in the United States and that subsidiaries in the host countries are perpetually cast in the role of imitators rather than innovators. It is bad enough to be inefficient today but it is surely intolerable to see that as the only future.

Nor do the spread effects of the branch plant economy stop there. National economic policy tends to degenerate into managing a branch plant economy within the rules of a game determined elsewhere. The capacity independently to control inflation, or create jobs, or in general to effect the rate of economic growth is constrained almost to the point of non-existence in Canada. To those of us trained to believe in the "new economics", it is frustrating to see its irrelevance, while the Canadian people are certainly entitled to ask in what sense American corporations in Canada or their government in Washington can assume the essential tasks that seem to have slipped out of the hands of our own governments.

Nor is it surprising that a branch plant economy leads to a branch plant quality in most areas of the lives of Canadians—in our labour movement. our universities. our media. Canada is unique in having much of its unionized labour force in international unions, which are, in fact, simply American unions operating in Canada. The result has been seriously to impede the emergence of a Canadian labour movement able to mobilize Canadian workers for such Canadian objectives as greater economic and political independence. It can hardly be doubted that this has worked to the benefit of American corporations in Canada.

Similarly. the Americanization of the economy has been followed. predictably, by the Americanization of the Canadian educational system and the Canadian media. the better to train Canadians for lives as consumers and workers in an American-style society. The view sometimes encountered that economic dependency does not preclude creativity and independence in other spheres is not borne out by the Canadian experience.

It might well be asked what reaction there has been from Canadians while all of this has been happening. The answer is surprisingly little. until recently, but that it is the most recent past. I think. that is most indicative of things to come. Canada has been unique not only in the extent of foreign ownership of its economy but also in the laissez-faire character of its policy, with the latter contributing substantially to the former. It is only in the past decade that the extent of foreign control has become an explicit issue in Canadian politics. Its failure to surface earlier can be put down as largely due to the fact that Canada, like the United States, is a capitalist economy in which the business class has a disproportionate amount of power and that the Canadian business class has been so thoroughly emasculated that it has been more than willing to settle for the role of managing branch plants for foreign masters. That it has surfaced now I would attribute to an increasing concern that Canada as a nation-state will disappear in the face of the present wave of Americanization, to an increasing distaste for what the United States has been doing recently, notably in Viet Nam, which has given a new logic to the pursuit of independence, and to a rising level of discontent with life within a dependent capitalist economy, not only because of the nature of dependency but also because of the nature of capitalism. In effect, a growing number of Canadians are, like a growing number of Americans, being turned off by the present system.

Within this country, I know that such behaviour is thought by some to be un-American, and within my country, I can report from personal experience that it is thought by some to be anti-American. It is, of course, neither but rather is anti-imperialist.

Anti-imperialism in Canada understandably takes the form of a growing Canadian nationalism, and there is no fact more important to the future of Canadian-American relations than this latter development. Canadian business leaders and Canadian politicians are increasingly being forced by the Canadian people to do something.

Things are in fact being done at this very moment. In February of 1968, the Government of Canada tabled the Report of a Task Force which I headed which made a number of recommendations for dealing with foreign ownership: more disclosure by and surveillance of foreign-controlled companies; strict measures to block the intrusion of American law into Canada through the medium of the parent-subsidiary relationship with respect to east-west trade, anti-trust legislation and balance of payments controls on direct investment firms; the setting up of a Canada Development Corporation so that future initiatives would be more likely to end up in Canadian hands; increased share issue by foreign-owned subsidiaries so as to permit greater Canadian participation.

The fate of that Report is instructive. The Government, under heavy pressure from the business community, rejected the modest recommendations of a Task Force which it had itself appointed. But the rising tide of nationalism in the past two years, particularly on the left of the spectrum of Canadian politics, has forced the Government's hand and new policies toward foreign ownership are expected to emerge as legislation shortly. It is likely that these new policies will be modeled in considerable part on the Task Force Report, on its spirit if not its letter.

How much all of this will matter remains to be seen. A government which acts only when its hand is forced, and this is clearly the case in Canada, is likely to do as little as it can politically get away with. I will not myself be surprised if we do not go beyond tinkering with the system. The result will probably be a somewhat more efficient and sightly less dependent Canadian economy. There would seem to be little for American corporations to fear.

Even should Canadian policy turn out to be stronger than I predict, its main thrust will be to create a less dependent but still capitalist economy and that would, it seems to me, offer no real threat to the American corporate interests.

But there are a number of Canadians—certainly a growing minority—among whom I would count myself—who will not be satisfied by such modest changes and who will work for more radical restructuring. We will question the logic of interfering with the status quo for on grander purpose than to take the economy out of the hand of foreign capitalists and put in the hands of local capitalists. We will advocate that the only sensible alternative to foreign private ownership of the Canadian economy is Canadian public ownership, a Canadian economy owned and controlled by Canadians for Canadians.

I do not mean to suggest that this point of view will prevail tomorrow, but it is already on the agenda of Canadian politics and is likely to become more relevant as time passes. For Canadians, like Americans, and particularly the youth, are coming increasingly to doubt, if not reject, the very nature of the modern corporation and the system of corporate capitalism which it has woven. No demand is more pervasive today than the demand for genuine democracy, for control over our own lives, and no institution is more undemocratic and more vulnerable to the charge of authoritarianism than the giant corporation.

On the northern periphery of the American empire, a rising nationalism has to a degree unprecedented in Canadian history a strong anti-capitalist and socialist component. This new anti-imperialist sentiment is, of course, to be found in the United States as well as in Canada, but the possibilities for its being translated into political action may be greater in Canada than in the United States because Canada does have a viable socialist tradition. In the near future, Canadian policy toward foreign ownership is likely to continue to be articulated to meet nationalist demands, but the socialist content of these demands cannot be indefinitely contained. Public ownership has been used in the past to a considerably greater extent in Canada than in the United States; this difference could well become more striking in the future.

I may seem to have wandered far afield from what may have been the intent in inviting me here, but if I am right at all, then it will matter to the operation of American corporations abroad, at least in Canada. Today giant corporations plan for single industries across many countries and do so in a most undemocratic manner. The positive alternative to this system is democratic socialism, the planning for many industries within one country, in the most democratic manner conceivable. My remarks have been motivated by the conviction that it is no longer enough to see the issue of foreign direct investment merely as how to minimize the tensions and conflicts created by American business abroad. It is time to seek out alternative futures and perceive the possibilities which they may hold. The American people as much as the Canadian people stand to gain from that exercise.

Chairman Boggs. Now, Mr. Rubin, it will be like old times here for you.

We are very happy indeed to have you.

STATEMENT OF SEYMOUR J. RUBIN, FORMER GENERAL COUNSEL, AGENCY FOR INTERNATIONAL DEVELOPMENT, AND U.S. REPRESENTATIVE ON THE DEVELOPMENT ASSISTANCE COMMITTEE, OECD

Mr. Rubin. Thank you very much, Mr. Chairman.

As Professor Watkins has said—and I tend to concur—the legal problems may be merely the tip of the iceberg. So I will try to be, as accustomed as lawyers are to that role, relatively brief.

Chairman Boggs. Yes; I notice that you have a prepared statement that is not brief. We will make it a part of the record. And you may sum it up.

Mr. Rubin. Thank you very much.

The first point that I would like to make is that in my view the problem that we have before us is not merely the question of possible conflicts, particularly in the legal field, arising from interlocking corporate ownership. It does seem to me that we do have a problem of definition of what we mean by the generalized term multinational enterprise. There I have in mind the fact that the problem, to the extent that problems exist, can be created as much by other relationships as they can by the fact that an American corporation owns a Canadian or a French or a Brazilian subsidiary. Licensing arrangements, for example, may very well give effective control to the home country over the activities in what is generally called the host country. So that I think that we have a problem really of doing business rather than necessarily a problem of multinational enterprises or of the usual characteristic of those multinational enterprises—interlocking corporate ownership.

Secondly, it does seem to me that the basic problems—and again I say to the extent that we do have problems—arise out of the possibility of a clash of sovereignties, at least insofar as the legal field which I hope to address myself solely to is concerned.

In that arena you do have two problems which have been alluded to, Mr. Chairman, by yourself and by others, in the course of these hearings, which are generally considered to be characteristic, if not the most important, of the legal problems which are likely to arise.

My own view is that on neither of these problems is the area of conflict tremendously important. To a certain extent conflicts do exist.

One of these areas is that of antitrust. In the field of antitrust there are, of course, ample opportunities for a clash of sovereign wills. There have been cases—the ICI-DuPont case in the United States is one of the ones that is most frequently cited—in which there has been a direct clash of orders from courts of competent jurisdiction, each to an entity within its own jurisdiction.

But in that particular case, as I think has been the case in a great many other situations, the difficulties have been worked out in practice, and worked out by a course of compromise, for example, by an American court taking cognizance of the fact that it should not order an American corporation to do that which a British court has forbidden it to do.

There are, other ways in which the field of antitrust is gradually being reconciled. In the first place, despite a number of statements by American corporations that they have difficulties with the supposedly more stringent application of antitrust laws in the United States than exists abroad, you do have a continuing practice of consultation here in the United States between the Department of State, which may be considered in this capacity to be sort of a lawyer for the foreign "client," and the Department of Justice as the guardian of our antitrust policy. That practice of consultation tends to mitigate the force of the conflict.

There is a gradual emergence under the Treaty of Rome. Also, of an antitrust policy in Europe—the same tendency is noticeable in other developed countries—which again tends to mitigate these difficulties. I have in mind also what was referred to, I think, in the course of these hearings earlier—a committee in the OECD which has had the function of providing an organization of consultation.

Thus, it does seem to me that while there is a possibility, certainly, of conflict in the arena of antitrust, the possibility is not all that important.

The other classic example of conflict of sovereignties is in what one may generally call restraint policy or denial policy, the situation in which the United States will say, not only to an American corporation, but to that American corporation's foreign subsidiary you may not ship goods to China or to Communist Cuba, whereas the foreign country may feel that a more relaxed trade policy with Communist China or with Cuba is in its own foreign policy interest.

Clearly there have been cases of this sort in which in my own practice as a lawyer I have encountered what I consider to be a rather stringent and perhaps unfortunate interpretation of the Trading With the Enemy Act here in the United States.

But again there is a tendency toward relaxation. The morning's news today contains an item over the radio about the United States having licensed the sale of trucks which contain General Motors engines from Italy to Communist China. There is, in any case, an attempt on the part of the United States, and I would suppose other nations as well, to try to work out their policies abroad as well as at home with or without regard to multinational enterprises, with or without regard to American or other ownership of an entity operating in another country.

In my own experience in the Department of State during the war years in connection with the Mutual Defense Assistance Control Act, the Battle act, which I had the honor of being Deputy Administrator of for a while, it has seemed to me perfectly clear that the United States will try to enforce its own foreign economic denial policy, whether or not there is American ownership of a foreign subsidiary.

We have been pretty successful in doing this. There are all sorts of ways in which this can be done. But the attempt has been generally fairly successful.

Again, the problem, to the extent that there is a problem, has been mitigated by reason of fairly understanding administration of rules, and also because a good many of the developed countries have more or less the same attitude with respect to a good many of these problems.

Now, Mr. Chairman, it seems to me that, as Professor Watkins said, the legal problems are merely the tip of the iceberg. And as was said by Mr. Hymer, practice may have been outrunning theory in this particular case.

As I observe the situation as it develops, it seems to me that there are more multinational enterprises being established these days, rather than fewer. One can pick up the pages of a publication like Business International, and every issue will contain an indication that an American corporation is concentrating its sales in Latin America through its Mexican subsidiary, that a group of German, Japanese, and other entities are establishing a consortium to exploit bauxite reserves in Australia, et cetera.

I could have listed in my statement a number of other examples. I do not wish to bore the committee here with excessive detail in this respect.

But I can assure you that I could supply off my desk additional examples.

I recognize of course the fact that in certain areas this tendency is causing problems. Some of these areas are not precisely (toward multinational enterprises) the areas where the legal conflicts have ordinarily been thought to arise. One of these areas, for example, is precisely the reason in my view why labor in the United States is so concerned about multinational enterprises, and why the attitude of labor has in general changed from a rather liberal attitude to one which I would myself consider to be rather restrictive.

There the fear is not that the last country will shut down a plant abroad, as the Remington people did in their French plant near Lyons, the fear is rather that the American company, when there is a crisis of sales, will choose to manufacture abroad rather than at home. And as wage differentials may be substantial, and as mechanization may increase abroad, this may well be a possibility.

It does seem to me that there is a strong possibility for multinational enterprises to be able to leap across tariff and quota boundaries.

What should be done about all of this? I have made a series of proposals toward the latter part of my paper. Briefly to summarize them:

(1) I would like to support the suggestion made during the first day of hearings by Professor Kindelberger (who put me in a category somewhat more extreme than the one that I think I take)—I would like to support the suggestion that we should attempt to create a forum for the discussion of these problems. There I would suggest that at least two different forums should be set up. One, to deal with the problems of relationships between these large multinational enterprises in the less developed countries, where you have precisely those questions that Professor Watkins was alluding to, the questions of resource control.

It seems to me that the problem of American corporation controlling the oil resources of Peru or the copper of Chile, and so forth, is quite different from the problem of whether an American corporation has another computer plant in France. The two are perhaps both important problems, but they are quite different. I would suggest use of the organization of American states as a first forum for the discussion of the problem insofar as it relates to developing countries, those to the south of the United States.

I had restricted this suggestion, Mr. Chairman, in my paper to the less developed countries. After listening to Professor Watkins perhaps we might have an American hemisphere discussion, which would include Canada, because his discussion of the Canadian situation seems to me to be conceivably one which might find a strong echo in Brazil or in Chile or one of our neighbors to the south.

(2) The other proposal that I put forward, Mr. Chairman, is that we utilize the forum of the OECD and the BIAC for a discussion between the developed countries where the problems are quite different from those of developing countries. I think a continuing and regularized discussion of some of these problems, in the OECD/BIAC, would be extremely useful.

Thank you.

Chairman BOGGS. Thank you very much.

(The prepared statement of Mr. Rubin follows:)

PREPARED STATEMENT OF SEYMOUR J. RUBIN[1]

The legal implications of the growth of multinational companies are an aspect of the possible clash of national sovereignty in respect of multi-state enterprises. Inevitably, the lawyer tends to regard the problems arising from the existence of concurrent and possibly conflicting sovereignties in somewhat different terms than would the economist or political scientists. For one thing, the lawyer is in many instances the technician whose job is to implement a policy which had already been determined by the needs and the desires of his client. He may therefore find himself occupied not so much with what *should* be done as with *how* it can best be done. For another, there are those who look with some suspicion on the ability of lawyers, trained as they are, or are supposed to be trained, to deal with broad policy questions. The eminent 18th century French writer on diplomacy, de Callières, stated that ". . . the training of a lawyer breeds habits and dispositions of mind which are not favorable to the practice of diplomacy."

[1] Former General Counsel, Agency for International Development and U.S. Representative on the Development Assistance Committee, OECD: Partner, Surrey, Karasik, Greene & Hill.

And others, like George Kennan, have suggested that words rather than substance tend to fascinate lawyers, with deleterious results for sensible policy.

I, and perhaps some eminent members of this Committee, may have a different view. At least, lawyers like myself, who have dealt with the practical problems of multilateralism in corporate activity both within the Government and while in private practice, may claim that our experience has been empirical, while our jobs have compelled more than a little consideration of what is likely to happen and what should be done about it. Mr. Justice Holmes' aphorism, that a page of history is worth a volume of logic, may here have a certain relevance.

With this *apologia*, I turn to some of the legal implications—on aspects of the sovereignty issue—attendant upon the growth of multilateral or international enterprise.

1. Definition of the Multinational Enterprise

It is important at the outset to try to state just what it is that we are talking about. Obvious though this proposition may seem, it is not always certain that writers on the subject a dissecting the same creature. I tend to use the term multinational "*enterprise*" rather than the more usual term "international corporation" or "multinational company". This is not, in my opinion, merely a matter of terminology. In discussion, the context generally will indicate that the speaker is thinking of a corporate enterprise which has its ownership in one country, or perhaps, in some cases, in a number of countries, and its operations scattered, directly or via subsidiaries, through various national markets.

Even so defined, the multinational enterprise can take a number of different forms; an American company with operating subsidiaries abroad; a base company organized under a law of convenience—Lichtenstein, Nassau, Panama—with subsidiaries in other countries; and so forth. But companies may go abroad through means other than corporate ownership; by means of licensing agreements, for example, where there is little or no element of stock ownership, but where the control by the licensor is more or less equivalent to that which would be exercised by a parent corporation. And some of the consequences of multinational business operations—for example, effective allocation of markets—may be achieved via simple agreement.

Possible conflicts of national sovereignty and of national policies may be little affected by the *manner* of multinationalism. If an American licensor is directed by the United States government to operate under one set of rules—as for example in regard to commerce with Communist China or Cuba—and a French or Canadian licensee finds that its own government has a different set of rules for that trade, the difficulties are the same as they would be in the case of direct ownership. It is therefore important, in defining the issues, to clarify and to understand the *substance* of the control factors and of the possible policy conflicts, rather than focussing on the mechanics which, for one business reason or another, may dictate the *form* of multinationalism.

I should further like to mention, by way of definition, one interesting item, falling perhaps somewhere between fact and speculation. Generally, we talk of the multinational enterprise, and its posing a threat to the national sovereignty of the foreign state in which it may exercise power of decision. But it is quite possible to have an institution whose ownership and whose interests are so diversified among a number of nations as to be responsive not to its "home" state—the usual problem—but to no compulsions other than its own economic interests. I believe this situation today to be quite unusual; but it may not be so tomorrow.

2. Nature of the "Sovereignty" Issue

National concern with multinationalism in business, industry, banking, etc., may be a matter of simple pride, or of concern with preservation of what have been traditional values. I would not underrate these factors: there may be as much resentment in France today against the introduction of snack bars and quick service luncheonettes as against American dominance of the computer industry. But in general, what we are talking about here is the ability of a foreign corporate entity to take decisions which importantly affect the economic or political life of the nation in which those decisions are carried out.

It is of course not unknown that a business comes into conflict with its own government. What is good for General Motors is not always considered to be good for the United States. And one can think, at this present moment, of price and wage decisions where business—and labor—may take a different view of the desirable from that held by the government.

But the isue is dramatized, and the reaction sharply intensified, if decisions which have a substantial policy impact are taken abroad. Disquiet is the greater if the decision may not be solely a matter of business economics; and the growing association between government and private enterprise, in a host of ways, and even in the most avowedly private-enterprise-minded state, may bring into question whether a particular decision is one of business, or of government policy. This possibility of clash, of conflict of objectives, together with the fluorishing state of multinational corporate life, has engendered the disquiet which has been publicized and discussed. Indeed, the distinguished authors of several rather well-known works in that area are among the witnesses at this Panel.

Of the issues centered on conflict of sovereignties, the ones generally discussed by lawyers are two: (*a*) what is rather roughly contained within the rubric of "antitrust"; and (*b*) the somewhat ill defined topic of "denial policies". The first involves the attempt by one state to extend to acts abroad its rules governing what we may call for convenience fair and desirable marketing practices; the second concerns a state's attempt to compel foreign entities to comply with its criteria of desirability in respect of eliminating all or some trade with certain third countries.

A. ANTITRUST

Here the potential for conflict seems high. and there are indeed some examples of conflicting rules sought to be imposed in the different countries in which a multinational enterprise operates. The Restatement of the Foreign Relations Law of the United States, in Section 18, concludes that a state has jurisdiction to prescribe a rule or law which gives legal consequence to conduct outside its own territory if the conduct causes an effect *within* its territory, under certain conditions. Those conditions are that the conduct and the activity must be parts of the activity to which the rule applies, that the effects must be substantial and foreseeable, and that the "rule" is not inconsistent with the principles of justice generally recognized by states that have reasonable developed legal systems". The Resetatement rule seems to go rather far; the case on which it relies (the Alcoa case in the 2d Circuit, in 1945), had some rather special features of affiliation, and the opinion seems to have required both an intent to affect the American market and achievement of that intent.

There can be, and have been, conflicting mandates resulting from the concurrent jurisdiction of different states. The 1951 Imperial Chemicals-DuPont case was based on a licensing agreement construed by the American court to involve an illegal division of markets. In this respect, it is similar to the complaint filed only last April by the Department of Justice in the Mitsubishi-Westinghouse situation, where there have for long been reciprocal agreements regarding the interchange of technological data.

Both cases—without any attempt to prejudge the Mitsubishi-Westinghouse matter—would seem to rest on the classic rationale of market allocation. In the ICI-DuPont case, an equally classic example of conflict was obtained: the American court ordered compulsory licensing, while the British court ordered ICI to fulfill its contract. A saving clause in the American decree, exempting action taken to conform to foreign law to which the company was subject, avoided a final joining of forces.

Much more could be said on the antitrust issue, but not within the limits of a paper such as this. Essentially, I feel that the fears of conflict in this area are exaggerated, at least in the context of a discussion of multinational enterprises. There is no necessary relation, in fact, between, on the one side, the interlocking and multinational ownership which is the hallmark of the international corporation and, on the other, the antitrust issue. Thus, both the ICI-DuPont and the Mitsubishi-Westinghouse cases arise from licensing arrangements—not cross-ownership. The problem is one of doing business—not of multinational corporations.

Secondly, the increasing attention being given to antitrust in countries other than the United States, and the gradual reconciliation of antitrust doctrine, at least among the so-called developed nations, suggests both that the issue will not long remain (as it has tended to be considered) an American problem. Differences will be eliminated or reduced as laws are harmonized. Beyond this, the various attempts, via informal consultation (as between the United States and Canada) and via the good offices of institutions like the OECD Restrictive Business Practices Committee, plus the continuing liaison in the United States between the Departments of State and Justice, should go a long way to avoid conflict in this area of law.

This harmonization of what is generally thought to be antitrust may not, however, solve another and perhaps more important matter. The multi-state enterprise may well have a substantial impact on trade. Where manufacturing enterprises in various countries are under the same corporate roof, market allocation may be based on a management decision, rather than agreement; the economic effect may be the same in the two cases. What will be the consequences of multinationalism on trade policy—questions of tariffs and quota, of American Selling Price and so forth—is hard to say. American firms, as M. Servan Schreiber eloquently has pointed out, have accommodated to the common tariff of the EEC as happily as our mosquitos have adjusted to and now thrive on DDT; and European and Japanese firms which find the American barrier at the border inconvenient may leapfrog it via an American subsidiary or affiliate in much the same way as the American have entered Europe. As among the developed countries, multinational business and industry may compel in the near future a considerable amount of hard thinking on trade policy.

B. DENIAL POLICIES AND NATIONAL SECURITY

When the multinational firm is the instrument of imposition of foreign policy of one country or another, one may expect harsh and direct clashes. The United States Trading with the Enemy Act is frequently cited as a source of this kind of trouble. For example, the French subsidiary of an American company may be prohibited from doing business with Cuba because of American objections to such trade, though French policy may be quite to the contrary. The possibility of psychological trauma when the host country realizes that aspects of what it considers to be *its* foreign policy are being determined by a foreign government is evident. It is equally evident that if the United States prohibits trade between its companies and Cuba it will not be indifferent to such trade between American subsidiaries abroad and Cuba.

This problem, however, like that of antitrust, is far broader than the issue posed by multinational corporations. With or without direct ownership (or licensing) of foreign entities, American policy has always been to try to compel adherence to its Trading with the Enemy Act controls abroad as well as at home. This was the case during World War II, through the medium of the threat of blacklisting. It was the policy of the United States in the post-war years, through the medium of export and financial controls. The Mutual Defense Assistance Control Act of 1949 (the Battle Act) required the termination of American aid to Marshall Plan countries which violated American precepts as to strategic trade with the so-called Sino-Soviet Bloc. And the attempt was then made, not without success, to secure recognition of and adherence to these American policies even in non-Marshall Plan countries—that is, where termination of aid was not even an apparent threat.

Understanding and rational administration of these policies, plus consultative devices designed to achieve agreement on what was and what was not strategic, did much to alleviate the potential conflicts. Nevertheless, these experiences with a direct foreign intervention in matters of trade have served to reinforce the long-existing conviction on the part of most governments that foreign ownership, at least in some areas, was potentially dangerous. Controls may be put into effect in the absence of ownership; the ownership relation makes such controls easier, and broadens the scope of foreign decision-making.

The United States has been no stranger to the nationalistic sentiment. Certain activities in the United States—mainly relating to such things as coastwise shipping and communications—are generally restricted to American nationals. During World War II, the United States worried about German and Japanese control of industrial and business companies in the United States. And even in the post-war sales of vested assets the fear of German re-entry into the industrial life of America resulted in purchase of these businesses being limited to Americans. It seems a long time ago, now.

There has also more recently been some worry about the possibility that foreigners (or unsavory Americans) utilizing Swiss bank secrecy laws, were acquiring substantial interests in American defense-related industry. And foreign—

or, indeed, American—"hot money" intervention in American business generally, via foreign banking accounts, has been troublesome.

Nonetheless, in relation to these issues, foreign ownership has been more a potential than a real threat. Wartime ownership by foreign enemy entities has been handled more than adequately by supervisory or vesting procedures. The existence of the physical facility within the jurisdiction of the "host" country has provided a basis for requiring compliance with one's own security standards: German-owned companies in the United States produced for the American war effort, as German subsidiaries of American companies built trucks for the Wehrmacht.

It may, of course, be the peculiar point of view of one who was at least partially responsible, during World War II, for the foreign policy aspects of the Trading with the Enemy Act, and who briefly attempted to administer the Mutual Defense Assistance Control Act, but the type of restraint or denial policy about which we are here talking does not seem very significant, either in producing results or in stimulating intergovernmental dispute. The controls, such as they are, have only a tangential effect. Denials of strategic materials have in fact been said to have had an effect opposite to that intended, and to have induced speedy establishment of foreign production facilities. On the sovereignty issue, the clashes with friendly foreign countries, while still annoying to those who have to deal with antiquated licensing procedures, touch mainly on sensibilities, not substance.

3. The Countervailing Trend

What has above been said emphasizes certain conflicts of national interest and national policy which arise from the multinational enterprise, and its removal of decision-making from national, host country, control. Other more important problems have been noted by such writers as Messrs. Servan Schreiber, Watkins, Dunning, Vernon and Kindelberger. Nonetheless, despite all the worries, there has in practice been a trend toward facilitating rather than impeding the entry of the international corporation.

Some rather dramatic instances of conflict do exist. The decision taken by Remington to close down its plant at Lyon would have been resented if taken by a French company; taken by an American corporation, it could be regarded as a detestable example of what can happen if economic decisions are made abroad. Given a choice, an American corporation might prefer to close down its French rather than its American plant. The same applies to other foreign enterprises. In view of the size and the tendency to expand of American industry, the "challenge" is likely to be thought of as American. But there was French opposition to a Fiat-Citroen deal. The Agfa-Gavaert merger was a source of concern in Belgium. When, in 1968, the Dresdner Bank had decided to merge its holdings in Germany's largest petroleum refining enterprise into Compagnie Francaise de Pétroles, it checked the decision with its government, which opted to exercise the veto thus offered and to give aid to the German oil companies in consolidaing and strengthening their operations. The takeover of the principal Norwegian aluminum producing facility by Aluminum Ltd. of Canada caused comment.

Nonetheless, the movement continues. If one follows the company reports through the pages of such a publication as *Business International*, one may note recently a merger of operations between the French and German chemical giants, Rhone Poulenc and Bayer; the acquisition by Cutler-Hammer, an American electrical equipment manufacturer, of the assets of its former Australian licensee; the formation of a jointly owned tractor corporation by Ford of the United States and Hokkai Jidosha Kogyo of Japan; the formation of a consortium between American, Japanese, Dutch and German interests, with some Australian participation, to develop a bauxite-alumina complex in Western Australia; and so forth. Neither the political nor legal obstacles, such as they are, seem to affect adversely this tendency toward internationalism, so evident at least as among the developed nations of the world.

Nor has foreign ownership seemed to produce, in the fact, many of those conflicts of economic policy which have been much anticipated. Clearly, foreign ownership of a substantial segment of national industry is worrisome. The Chrysler takeover of Simca in 1963, despite its aspect as a rescue operation, stirred angry headlines. But during the "events" of May and June, 1968, when red flags flew over many a French plant and when there was rioting at the

Renault plant at Flins, the Simca factory a few miles away continued to turn out autos; and Simca now exports more autos in Europe than Renault, Peugeot and Citroen combined. The real benefits in export earnings seem to have overcome the prideful objection to the foreign ownership.

Moreover, fears have been allayed by experience, which has shown corporations acting as good citizens, or at least as being responsive chiefly to objective non-chauvinistic profit considerations. Activity will be centered where it is profitable—not patriotic. Increasingly, American corporations concentrate on manufacturing abroad, if profitable, hence the recent Bendix move to emphasize production in and exports from Mexico. And so forth.

In point of fact, what is now coming to the fore is the possibility that multinationalism may be detrimental, not to the nation in which the subsidiary operates, but to the "home" state. France may worry that an American corporation will prefer unemployment abroad to unemployment at home, and thus shut down a foreign subsidiary in a time of falling demand. But American labor will and does worry that in such times the choice will be to favor the foreign subsidiary at the cost of the home industry. Especially is this so where labor costs abroad are substantially less than those at home, and where increased mechanization abroad has cut down or eliminated the former advantage of higher productivity at home. In these circumstances, will the automobile industry prefer to produce in Europe or the United States? The question is certainly a real one. And it is large responsible for the shift in favor of many a labor union in the United States from a liberal to a restrictive trade policy.

In any case, foreign fear of the multinational enterprise seems not to be reflected in governmental action. Thus, the effort of the European Economic Community to develop a single company law for the Community seems to reflect approval rather than disapproval of multinationalism. The Community has for some years been working on a proposal for a common Community Company Law. Writing in the September/October 1969 issue of the *Columbia Journal of World Business*, Dr. Raffaello Fornasier, legal adviser to the Secretariat of the Councils of the EEC states both that "the main problem of company law within the EEC is today largely psychological" and that ". . . conflicts which arise from differences in the law" can best be dealt with via a "single company law throughout the Common Market countries. Uniform law would make it possible for companies to combine to achieve optimum size, move freely to the best production location, rationalize their research and distribution networks through common efforts, and have access to available sources of finance in the country of their choice".

What has been proposed, in the Common Market, are basically two methods of achieving these results. One is the process, already entered upon through the Conventions of February 27 and 29, 1968, of harmonization. The other, launched in 1959, and toward which progress seems under way, is that of the Market company law, designed to provide for three categories of cases: mergers across national frontiers; establishment of common subsidiaries of companies of different nationality; and establishment of holding companies on the European level. That such a company law will soon be achieved seems unlikely; differences, as for example, in connection with the role of labor in management, are too varying to be easily reconciled. Moreover, even the proponents recognize the possibility of use of a Market company law to escape restrictive domestic legislation.

Since, according to the *Journal of Commerce*, (June 11, 1970), "it appears generally agreed that subsidiaries of American firms in Community countries will be free also to form a European company", the proposal will, if adopted, have little effect on the continuing American invasion of Europe. But it will probably have a beneficial psychological effect; it may facilitate in some degree the formation of European companies, in fact as well as name.

Whatever may be the real effect of a single company law for the Common Market, the effort to achieve that law certainly looks toward more—not less—internationalism.

4. The Problem Areas

It is, in fact, clear that a number of quite different problems do exist. There is one reaction to a multinational corporation if it is, for example, Brazilian and another to the corporation that is American. There is the worry in some developed countries—Britain has expressed it, as has France—over possible American domination of the production of sophisticated equipment, where there might be no fear of such domination in other industrial areas. There is likely to be one reaction in a developed, and another in a developing, country.

It is along the lines of this last distinction that it seems to me that it would be useful to organize further inquiry and work, that is, the rôle of the international enterprise vis à vis the developing countries on the one hand, and among the developed nations, on the other.

(*a*) Whatever a nation like France may feel about American pre-eminence in the field of computer technology, the less developed nations feel in much greater measure about foreign control of their natural resources. Especially is this so in those countries dependent on a limited number of such resources for the major part of their foreign exchange. Ownership by foreigners of such essential industries, often in the extractive field, where resources can rapidly be depleted, has often been a matter as painful as sometimes it has been profitable. The point of view of the developing nations has been expressed in countless United Nations General Assembly resolutions, expressing their inviolable right to their natural resources. The response has generally been in the form of insistence on the rule of law, and on prompt, adequate and effective compensation in the case of expropriation. The counter response has been, at least among our Latin American neighbors, reiteration of the principles of the Calvo doctrine—that a subsidiary is subject to the law of the state in which it operates, and that the government of its parent cannot intervene in its behalf.

It can be observed empirically that direct ownership of extractive industries, and of public service companies—bus lines, for example, where fare increases affect many people, where inflation and rising costs compel such increases or bad service or both (a situation not unfamiliar to Washingtonians)—is productive of dispute. Most international investors are fully aware of these facts. The proposals of Professor Hirschman, for a positive program of disinvestment in Latin America, and of Professor Vernon, for recognition of the Calvo clause, go beyond what I would think feasible or desirable. But they respond to a real issue.

(*b*) As among the developed nations, the problems are perhaps more complicated and at the same time easier. Some of those problems—in the areas of antitrust and denial policy, for example—I have attempted to put in perspective. Some others—the effect of multinational enterprises on trade and trade policy—are to my thinking both more important and less manageable. There is clearly a substantial clutch of questions here, which deserve rational and sustained thought.

5. A Proposal

I propose that the United States take the lead in organizing a continuing forum, in which Government and private interests could come together for the regular consideration of these matters. The participants, official and private, would meet often enough to become acquainted with each other, with the various points of view, and with the specific of the problems. Where and when necessary, they could propose agreements for ratification by governments. More often, they might merely present analyses, perhaps together with recommendations for cooperative action. In a sense, this would be like one aspect of the old negotiations for an International Trade Organization, out of which the GATT was so usefully salvaged. A sort of GATT, dealing with the questions which are now before this Committee, could bring not only light, but also hopefully some measuse of harmony, into the increasing phenomenon of multilateralism in the business and industrial life of nations.

I, of course, recognize that there are many forums which at present exist and which do deal with these issues. I have no desire to multiply either national or international bureaucracies. But the many discussions which now take place—and I alone, though representing neither government nor industry, have sat in on at least four in the last 18 months—tend to elicit statements, rather than attempts to identify and resolve the definable issues. Continuity is lacking. Participants are prestigious, the present speaker excepted—but without any mandate from anyone. The discussion is always interesting, often learned. But conclusions are, in the interest of something like flow-of-consciousness thinking, avoided more than sought. The measure of agreement which often emerges tends to no ascertainable result.

I would hope that the establishment of such a forum might be within the framework of existing organizations. Since I consider the problems of the developing nations, on the one side, and the developed nations among themselves, on the other, to be quite different, I would suggest that initial discussions be held with the cooperation of different international organizations. Here, in view of the parochial interests of the United States, I would propose utilization of the machinery of the Organization of American States, as a first step in the dialogue with the developing nations. The nations of the Americas are at various stages of development. Mexico, for example, is in many ways an advanced industrial nation; others are less far along. An inter-American forum would produce a variety of viewpoints, and could precede similar African and Asian forums.

On the other side—the developed nations—I would think that the OECD, and its very useful adjunct, the BIAC, would be the appropriate place in which to begin talks.

I take the liberty—and the risk—of mentioning a few among the many topics which might be on the agenda of the organization I suggest:

1. Multinational enterprises and the developing countries; "national resources" and foreign investment; the effect of the Calvo clause, and the rule of prompt, adequate and effective compensation.

2. Multinational enterprises and their effect on international trade; the question of whether the ability of a multinational enterprise to allocate production and sales among its different national units may diminish the intended effects of tariffs (and other trade restrictions); the impact of that possibility on the economic policies of "home" and "host" nations, and on the trade policies of those nations; the consequences of multinationalism on world trade patterns.

3. National policies in the field of antitrust and their relation to and impact on multinational enterprises; the effect of varying national policies, and the effectiveness of such policies.

4. Multinational enterprises and national political objectives; ability to affect foreign political or economic policy; the citizenship obligations of multinational enterprises.

For a starter, this list is already too long. It may only illustrate areas in which argument rather than agreement would result. But I have the unprovable feeling that discussion of such matters, in a forum which might be, in the field of multinational enterprise and international investment, something like the GATT in the field of trade, would give both governments and private industry better understanding. And out of such understanding, there might come better policies.

Thank you.

Chairman BOGGS. And now it is my great privilege and honor to welcome to the Joint Economic Committee our fellow parliamentarian, a distinguished deputy in the French Chamber of Deputies, the Honorable Jean-Jacques Servan-Schreiber.

I might say to you, Mr. Deputy, that you are on a very distinguished panel. You were not here when I introduced them, but we have with us this morning Prof. Stephen Hymer, who has previously testified. He is professor of economics at Yale University.

And then Mr. Watkins from our neighboring country of Canada, who is the author of a very famous report known as the Watkins report.

And your neighbor on your right, Mr. Seymour Rubin, who has been very active in the question of European unity.

Let me also say in welcoming you here, sir, that I have many reasons for being glad that you are here. First, I come from Louisiana, which has a great French heritage, as you know.

And secondly, I know of the great work that you have done in promoting the concept of the unified Europe.

Way back in the 80th Congress, I sponsored, with Senator Fulbright, what was known as the Boggs-Fulbright resolution, which said, it is the sense of Congress to encourage the establishment of a United States of Europe. At that time we had been engaged in what was called piecemeal aid to a number of countries in Western Europe. Shortly thereafter the late great revered General Marshall made a speech at Harvard which led to the establishment of the Marshall plan. It was some years thereafter, but not too many years, that I had the pleasure of getting to know well and, shall I say favorably, the revered John Monnet, a man, I think, of great vision. And I think his contribution to the Treaty of Rome is one of the great contributions to the history of mankind.

Earlier this week we had with us Mr. Guido Colonna and a man with whom you are well acquainted.

For the benefit of those who have come in late, I should like to say that I know that you come from Lorraine, a section of France that is dear to the heart of me and my fellow Louisianians, where many of them came from, or their ancestors did.

So welcome. And we will let you proceed now.

STATEMENT OF HON. JEAN-JACQUES SERVAN-SCHREIBER, DEPUTY, FRENCH NATIONAL ASSEMBLY, AND PUBLISHER, L'EXPRESS

Mr. SERVAN-SCHREIBER. Mr. Chairman, as you know, I am not as accustomed as you are to the responsibility of being a parliamentarian. That is the reason for my being delayed this morning. I am very happy.

Chairman BOGGS. We understand. We are honored that you should come. And I know what an imposition it was on you. I know how late it was last evening when you arrived.

Mr. SERVAN-SCHREIBER. The first time I got acquainted with the United States was thanks to you and Senator Fulbright. I got from you directly a 3 month completely free possibility of studying America.

I appear before you as a fellow parliamentarian, recently elected by the legendary region of Lorraine, the land of the Cross of Lorraine—for me a joyous cross to bear. I also appear as one dedicated—as you are and as many American parliamentarians are—to the ideal of an integrated and unified Europe.

In 1967, while I was still a journalist and publisher, I wrote a book: "The American Challenge." The Communists criticized it as a hymn to American capitalism. Others saw it as an anti-American call to arms. In truth, I tried to express both admiration for your economic dynamism and anxiety lest its vitality and our passivity engulf the European way of life. Today, I would like to comment on how we are all affected by this challenge, which has become multinational, and by various other challenges that we are facing in common.

That is why your hearing today to me seems so appropriate.

First, we have common concerns. Economics and politics, you know better than I do, cannot be any more considered one without the other. I personally lived 13 years ago a tragic drama in my own country. I wrote a book at that time called "Lieutenant in Algeria," recounting what happened when my country got in the grip of human degradation, economic bankruptcy, and the ominous stirrings of military power because of a war in the far distant continent.

With all the pronounced respect I have for this body in Washington, with friendly concern, we cannot, of course, as you know, be indifferent to your predicament in Vietnam. And I think we cannot separate the subect today and the conflicts of it.

This great Republic with all of its economic power, and all it represents for the multinational corporation and industrial progress, could be overwhelmed, I think, by the kind of crisis that my own country experienced for many years in Indochina and Algeria. And, of course, this would spell disaster for your own economies as well as our own and for your own security as well as our own.

We have no lessons to give to anybody. This is the great lesson we learned in the last 25 years.

But the rebirth of France as a country started with the complete ending of the Algerian war and the Indochina war. We learned that it is a futile and vain attempt to try and impose political systems on other continents by the force of strength.

But this is all I think I can correctly say about Vietnam today.

The end of the war in Vietnam, it seems to us in Europe, I would say to almost all of us, a preface to what we can do together economically in the world, America and Europe. Because now we should be able as soon as possible to mobilize all our energies toward the need to preserve and even more to reform the industrial society in which we live here and in Europe.

The growing rebellion against certain features of the new industrial state is deeply rooted and potentially violent. Those who dismiss this dismiss it as an ill-humored attempt of youth are being naive, I think. For the radicalism of youth in our country and in yours stems from a deeply felt conviction that a system which allows the excesses of economic competition, especially on a multinational basis, to ride herd over social life, is basically immoral. And those who run the great multinational corporations today, most of them Americans, notice their children's concern. They get it at the breakfast table every morning.

Yet we are not 18 years old, and we know that a modern market economy is the most powerful and the only tool for material progress. This we must preserve and respect. But we must put it at the service of society. And this is the problem, the essential problem for multinational corporations.

This quest for human dignity in this very rapidly becoming complex economy of the multinational corporation is in our mind the essential role of politics, reform of that industrial state, of that multinational industry state, without revolution is possible.

I am sure it is your belief. It is ours. If it is possible, then it is our duty to bring it about in this generation.

How can we have modest suggestions toward that aim?

We think that like church and state, economic and political power should be as much as humanly possible separated, if each of them is to fulfill its mission.

This was in a way, if I may recall a very historical event, the essence of Luther's reform philosophy between church and state, and today it is between economy and state. It holds a vital message for us today.

Private industry must be allowed—and Europe now understands that much better than just a few years ago—to perform to the full of its function as an effective term progress. Politics has another and more crucial role: to concentrate itself to the service of man, the worker, and not to the efficiency of production, the corporation. This is the responsibility of the entrepreneurs.

We believe now—and I am sure you know the progress that that very simple idea has made in the last 5 years in Europe and in my country and Germany and other places—we believe that the ferociousness of competition among business enterprises is good. It is a locomotive for innovation for development of invention. And we, as you have done sometimes, must give full play to it.

This is the task of the entrepreneur, the private entrepreneur.

But the main goal of politics is to prevent as much as we can this ferociousness from hurting man itself.

The British economist, John Maynard Keynes, wrote in the thirties:

> That the essence of capitalism is the preponderance of the role of money in society, and the love of money by the individual.

This is John Maynard Keynes, the great reformer of our time.

It is this that we must extirpate from our social system with human generosity and solidarity and profound reform. And we do not have much time. This reform is the urgent mission that I think we have to gather in the seventies.

Now, on multinationalization of business, the rapidly intensified conduct of business across national borders has, first of all, augmented the benefits, the efficiency, and the creativity of the free market economy system. It has also developed its miseries. The development of corporate activity on a global scale by the multinational corporation—I would not cite any name, you know all the names of those corporations. Eight out of 10 are Americans. Some are Europeans, and some in my country.

First of all, they have brought more efficient productivity and cost authorizations for products. So we consider it as a force, and a good force. But because they have created, and they are creating now—and thanks to you you are capturing the interest and imagination of the people who think all over the world.

And what are the consequences of that rapid development, the new development? They are creating a worldwide empire that they are carving for themselves, those multinational corporations. And in this worldwide empire there is no political law. It is becoming a new jungle. They are widely spread all over the world, and they are accountable to no single political authority.

Since international law and authority is so feeble, or almost nonexistent, they are free to dictate and decide their own authority.

Profitmaking activities, which draw undue advantage from tax haven insurance, holding company privileges, the weaknesses, the tragic weaknesses and contradictions of international tax enforcement—I know you are more aware than I am of that—and other loopholes rob society, rob the public power, of much of the material abundance created by the market economy, and the dynamisms of international business. That portion of available wealth that is created by them which should go into collective investments for the benefit of all, like health, education, housing, transportation, at this time, because there is no law, because we are in a kind of jungle, is too often diverted into the hands it is not needed.

The American challenge has awakened us a few years ago to the problems of the multinational corporation.

I would just like to give you two or three figures, and that is all. We must consider together the fact that the real value of American investment in the European Common Market today stands close to

$40 billion. American subsidies in my own constituency of Europe control 95 percent of total production of integrated circuits, the basis of the electronic industry, and, we consider, the basis of all future industry in the next 10 years.

American subsidiaries control 80 percent of all electronic calculators and computers in Europe, and 30 percent, just as an example, of the automobile business.

It is not the fault of the American business. They are forging ahead, and they are welcome. It is largely the fault of the slowness of the process of integration on my continent. And I know that my own country for the last 10 years has been a principal offender in that stagnation in front of multinational corporation dynamism.

Not only our industrial market is dominated, but the capital market. And this is new. This happened in the last 2 years. It is dominated by American-controlled institutions. Indeed, the banking centers of London, Frankfurt, Zurich, Paris, seem, and are, at the mercy of the mighty, and occasionally not-so-mighty, Eurodollar.

In 1959, for example, American borrowing in Europe stood at around $500 million. Last year it reached almost $3 billion in less than 10 years.

During the same period the proportion of U.S. generated funds coming directly to Europe to get into investment shrunk from 25 to 16 percent. In other words, the multinational American corporations, forging ahead as they should do, are investing our own funds in their own development. This is a very challenging and complex issue that we have to meet.

I am not a nationalist. I detest nationalism. American investments are welcome in France. I wrote it, if I can say, some 3 years ago, and I confirm it today, as a politician. And as you know, it is more difficult. They stimulate the efficiency and energy of our own economies.

But we cannot help being disturbed by the form of the invasion in certain sectors. Our industries in the science-based sectors, the centers of the future, are still too unsophisticated to stand up really in a competitive sense against the multinational American giants in face-to-face competition. This has been demonstrated.

So there is a very strong penetration by multinational corporations, meaning American corporations most of the time. In foreign countries it is good. It is natural. It should be encouraged.

But it cannot go without a commensurate sense of social responsibility. The larger a multinational corporation is, the greater its sensitivity should be to its responsibility socially.

They must respond to our need for industrial decentralization, they must understand it. And they are understanding it. You can help them more than we can, and we shall help you. They must realize that we too have differences of a type which exist, for instance, between West Virginia and Massachusetts.

I for one intend to do more for Lorraine on the sensitive banks of the Rhine. I propose to campaign for greater American multinational investments, multinational corporation investments in the reasons which have the scientific and technical skills that any multinational corporation may require.

So you see I am not against multinational corporations. In fact, quite the contrary. They mean progress. And I have been personally involved for the last 3 years in my own enterprises in a direct partnership with a fine American company, McGraw-Hill. And this has helped, with no drawbacks as long as people who make the decisions are not far away but are the people on the spot.

Mr. Chairman, together, we and you in America have a tremendous task, make coherent our multinational corporate strength so that we can forge ahead of the East. Russia is learning the limits of its system, of its military power. The Russian empire is discovering the inevitable link between economic progress and human freedom. This is possibly the tender sward which would open the East to our tools for economic progress.

For Europe this affords opportunities at the East, which are at once economically attractive and helpful, maybe helpful in a major way, in strengthening the fragile fabric of peace.

The dynamic character of production, multinational production in Western Europe, Japan, and the United States, is now publicly the object of envy in the eastern countries. If the eastern countries wish to participate in the feast of industrial development, they can no longer afford, and they know it, the luxury of splendid isolation and suppression of creative freedom.

This process, I believe—and I am very happy to be able to say it here today—this process of going to the East and opening it to economic progress and thus to freedom, must be helped. We can help it.

If the gap in industrial development is to be narrowed, East-West intercourse must extend beyond the mere exchange of commodities. The domain of technology and management, multinational management, must be given primary attention by American corporations and European corporations that have now a responsibility in the East in our own self-interest.

In other words, to conclude, I suggest for your discussion, Mr. Chairman, that the coming task we have together, starting now that Europe has discovered that it can have power—thanks largely, as you recall, to American generosity, incredible historical generosity, after the war, thanks to American protection, Europe is now becoming a power. And this can of course help Europe. But it can also help you. The challenges that we have together to face in the seventies—first Europe, if you will allow me to speak of my own country—must be much more integrated economically and politically, and it is going to be.

The Germans, the French, will do it with the others. Nationalism—I believe it, I have seen it, I have felt it in a modest way I have proved it—is a dead issue in Europe.

Then Europe can play a special role, because our old continent no longer aspires to any dream of world empire, or to any dream of military power.

We have learned from bitter experience that if we are able to create this new form of power, this could help you.

The second task, is on this side of the Atlantic. You can help us, multinational corporations can help us, and American policy can help us, as it has done, in creating a more federalized Europe, largely, more self-sufficient, socially more just, and democratic. You can do that for us.

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The third task and challenge will be for us, then, together to give priority to East-West reconciliation, not in a passive sense of coexistence, but active exchange, economic, industrial, technical know-how, management, everything we can to create economic progress inside the eastern Russian empire is in our own best interest.

I think this is the challenge that we will have to meet together. It is easier for the European multinational corporations to do it in the Communist countries than it is for you. So we can help you.

The last but the largest, the greatest, the most stimulating and also disquieting challenge is the passion of youth. In your country, in my country, in all the countries of Europe it is the same. It is admirable in its motivation, dangerous if it does not meet any response. The quest of youth for dignity, sincerity and truth in the industrial establishment, and especially in the multinational industrial establishment that does not respond to any political law any more, this passion of youth is one of the two greatest sources of human energy.

The other source is modern science-based industry.

These two forces, the mobile passion of youth, and the strength of modern industry, remain as they are today on a collision course. Our future is thus. If we are able to forge an alliance between them by reform, urgent, radical reform, then we will have met the challenge of our generation.

Chairman BOGGS. Thank you very much for, in my judgment, one of the finest statements that I have ever heard before the Joint Economic Committee.

(The prepared statement of Mr. Servan-Schreiber follows:)

PREPARED STATEMENT OF HON. JEAN-JACQUES SERVAN-SCHREIBER

THE MULTINATIONAL CHALLENGE OF THE 1970'S: REFORM WITHOUT REVOLUTION

I appear before you as a fellow parliamentarian, recently elected by the legendary region of Lorraine, the land of the Cross of Lorraine—for me a joyous cross to bear. I also appear as one dedicated to the ideal of an integrated and unified Europe.

In 1967, while I was still a journalist and publisher, I wrote a book: "The American Challenge." The Communists criticized it as a hymn to American capitalism. Others saw it as an anti-American call to arms. In truth, I tried to express both admiration for your economic dynamism and anxiety lest its vitality and our passivity engulf the European way of life. Today I would like to comment on how we are all affected by this challenge, which has become multinational, and by various other challenges that we are facing in common.

1. COMMON CONCERN

Economics and politics have become so intertwined that one cannot be considered without the other. Thirteen years ago I wrote a book that received less attention here: "Lieutenant in Algeria". It recounted a tragic drama in whose grip my country experienced a foretaste of human degradation, economic bankruptcy, and the ominous stirrings of military power.

With due respect, but also with friendly concern, we cannot be indifferent to your predicament in Vietnam. If this great Republic were to be overwhelmed by the kind of national crisis that overcame France in May of 1958, the consequences for Europe and for the world would be incalculable. They would spell disaster for our own economies, and for our security.

The end of the war in Indochina and then, at tremendous national cost, the end of the war in Algeria, reopened our road to salvation. We have learned the futility of attempt, by a country like mine or yours, to impose our own ideals on other continents.

For those of us who love America, who remember how generously you participated in our rescue and reconstruction, it is painful to see this country tear at the fabric of its social life. No matter how sternly we criticize your actions and illusions in Indochina, we instinctively know that the United States has, within the moral fiber of its people and its youth, the means to cure this cancer.

Vietnam is an aberration. What must mobilize our energy and ingenuity is the need to preserve and reform the industrial society in which we live. Only if we dare to make this reform sufficiently profound and rapid will we save our peoples from all-consuming anarchy. The growing rebellion against certain features of the new industrial state is deeply rooted and potentially violent. Those who dismiss it as an ill-humored tantrum of youth are being naive. From the radicalism of the young stems a deeply-felt conviction that a system which allows the excesses of economic competition to ride herd over social life is basically immoral. Herein lie the roots of rebellion, roots which cannot be eradicated by the elders in a fit of blind rage. Those who run the great multinational corporations know the sincerity of their children's concern. They get it at the breakfast table every morning.

Yet it is clear that the modern market economy, with its freedom of private initiative and the bracing energy of competition, is a powerful tool for material progress. This tool must be at the service of society. Man cannot, after centuries of poverty and servitude, be allowed to sink back to the status of a mere object, a cog in an aimless machine of production.

This quest for human dignity in our contemporary economy is not a Utopia. It is the essential role of politics. Reform without revolution is possible; and it is the duty of our generation, in Europe and in America, to bring it about.

2. ECONOMIES AND POLITICS

Like church and state, economic and political power must be separated as much as possible if each is to fulfill its mission. This was the essence of Luther's reform philosophy. It holds a vital message for us today. The best judges in matters of investment and profitability are generally the entrepreneurs, not the state. Public ownership of means of production has been irrevocably discredited by the experience of the Communist East. Private industry must be allowed to perform to the full its function as a factor of material progress. Politics has another and more crucial role: to consecrate itself to the service of man—the worker—rather than to the efficiency of production—the corporation.

The ferociousness of competition among business enterprises is a locomotive of innovation, development and enrichment. It must be given full play. But the main goal of politics is to prevent this ferociousness from hurting man himself. If those who lord over industry are also to be those who by their influence dictate the direction of political life, then we will inescapably fall into the most bitter and dangerous social upheavals. The separation of economic and political power is, therefore, a primary task for the future.

The great British economist, John Maynard Keynes, wrote in the 1930's that "the essence of capitalism is the preponderance of the role of money in society, and the love of money by the individual." It is this that we must extirpate from our social system with human generosity and solidarity. This reformist objective is a worthy and urgent mission for the 1970's.

3. THE MULTINATIONALIZATION OF BUSINESS

The intensified conduct of business across national borders has augmented the benefits and the miseries of the capitalist system. The development of corporate activity on a global scale by firms such as IBM, Ford, Siemens, Fiat, Phillips and Lafoarge make for more efficient productivity and a wholesome cross-fertilization of intelligence, talent and of creativity. Consequently, it is a force for social well-being. But, because of the world-wide empires which they are carving out for themselves, the multinational corporations are also able to create a new jungle. Widely spread out in their component parts and commanded from geograpically remote bases, they account to no single national authority. And since international laws is feeble, or non-existent, they are free of international authority as well. Fraudulent or undisciplined organizations, often operating with funds invested by unsuspecting people of modest means, enjoy far-ranging immunity from any meaningful form of regulation or supervision, unless you consider Panama or Liechtenstein acceptable legal systems.

Profit-making activities which draw undue advantage from tax havens, holding company privileges, the weaknesses and contradictions of international tax enforcement and other loopholes without any redeeming economic function, rob society of much of the material abundance created by the market economy and the dynamism of legitimate multinational business. That portion of the available wealth which should go into collective investment for the benefit of all (health, education, housing, transportation, etc.) is too often diversted into hands where it is not needed and where it does not belong.

Some of us see models in the institutions which you have developed during the momentous days of the "New Deal": the Security and Exchange Commission, for example. But we are also afraid of the awesome size and vigor of your business institutions, and we must take steps in our own defense.

4. THE SCOPE OF THE AMERICAN CHALLENGE

Consider the fact that the real value of American investments in the European Common Market currently stands at close to 40 billion dollars. American subsidiaries control 95 percent of the total production of integrated circuits, 80 percent of electronic calculators and 30 percent of automobiles. Because the process of integration on the Continent is so slow, and so heavily obstructed by nationalistic considerations (my own country being a principal offender), it is difficult to develop a coordinated policy vis-a-vis the multinational corporation. The European countries vie with each other for a larger share of these investments, occasionally offering generous subsidies and tax concessions. When General Motors was denied the privilege to build a plant in Alsace, it was immediately welcomed across the border, to use German workers and supply the French market under the preferred tariff structure of the European Economic Community.

Our capital markets are also dominated by American-controlled institutions. Indeed, the banking centers of London, Frankfurt and Zurich seem to be at the mercy of the mighty, and occasionally not so mighty, Eurodollar. And it is an extraordinary paradox that the savings of Europeans are used to finance the acquisition of local industries by U.S. companies. In 1959, for example, American borrowings in Europe stood around 500 million dollars; in 1967 it reached 2.6 billion dollars. During the same period the proportion of U.S.-generated funds to finance investments in Europe fell from 25 percent to 16 percent.

I mean to be neither nationalistic nor Chauvenistic in pointing out the drama of this situation of the patterns which it announces for the future. American investments are welcomed in Europe. They stimulate the efficiency and energy of our own economies. But we cannot help being disturbed by the form of the invasion in certain sectors. Our industries are still too unsophisticated to stand up against the multinational American giants in face-to-face competition. This is demonstrated by the fact that European companies which venture into the U.S. market with operating subsidiaries are hardly able to hold their heads above water.

Penetration into a foreign country, which is a natural by-product of the multinational phenomenon, cannot go without a commensurate sense of social responsibility. The multinational corporations must show greater sensitivity than they have to conditions prevailing in the host country. What is good for General Motors may be good for America, but not necessarily for Belgium or Holland. They must respond to our need for industrial decentralization; they must realize that we too have differences of a type which exists between West Virginia and Massachusetts. And I, for one, intend to do more for Lorraine on the sensitive banks of the Rhine. Unashamedly, I propose to campaign for a greater share of American and European investments in a region which boast all of the resources and the scientific and technical skills that any multinational corporation may require. So, as you see, I am not against multinational corporations. On the contrary, I regard them as new tools of progress. In fact, a very fine one, McGraw-Hill, has been for more than three years a partner in my enterprises in France.

5. TRADE VERSUS IDEOLOGY

Happily, the world is no longer as polarized as it used to be. Strong centrifugal forces are at work both in the East and in the West. Russia, no less than America, is learning the limitations of military might and developing dangerous internal cracks. The empire over which it presides is discovering the inevitable link between economic progress and human freedom. This is the tender sword which will open the East.

In the last few years the Eastern countries have given evidence of their desire to become integrated into the world economy. They deserve to be met halfway. Today, the national leaders of Communist countries scarcely disguse their admiration, even envy, of Western production and marketing efficiency. For Europe, this affords opportunities which are at once economically attractive and helpful in strengthening the fragile fabric of peace.

Communist planners are groping for new techniques to improve the competitive position of their economies and the standard of living of their people. The dynamic character of production in Western Europe, Japan and the United States has become the main object of their envy. Under these new conditions, international co-operation becomes imperative. If the Eastern countries wish to participate in the feast of industrial development, they can no longer afford the luxury of splendid isolation and the suppression of creative freedom. This process must be helped along, for it can help to reopen the East.

The economic experience of the last two decades has proven the indivisibility of technical progress. Men living apart on their own side of the ideological fence cannot generate as ample and varied a range of goods and ideas as can be produced by the entire world pursuing innovation and freely exchanging its benefits. If the gap in industrial development is to be narrowed, East-West intercourse must extend beyond the mere exchange of commodities. The domain of technology and management must be given primary attention, along with broadly based business co-operation across the borders of geography and politics.

As Europeans, we view the East in light of the economic and cultural indivisibility of the Continent, rather than its ideological cleavage. While the longing for civil and intellectual liberties in the Communist societies still remains unfulfilled, a manifestation of national identity and a rejection of the dogmas of the past is clearly in evidence. Indeed, the Gaullist notion of "Europe des Patries" has touched a more responsive nerve in the Eastern than in the Western part of the Continent.

6. COMMON TASKS FOR 1970'S

It is becoming increasingly clear that in the 1970's Europe will have a much more important economic and moral role to play than in the two previous decades; a very special role, since our old Continent, at least that part of it which lies to the West, no longer aspires to the dream of world empire. It has learned from bitter experience that military conquest brings no rewards. Within this experience lies a lesson which can help you.

A major task at the other end of the Atlantic is the construction of a federalized Europe, one which is larger, more self-sufficient, socially more just and democratically more compatible. In this you can help *us*.

Priority must be given to East-West reconciliation, the road toward which objective passes through active co-existence, economic and industrial co-operation and broader exchange of products, ideas and men. This is an enterprise which we shall tackle *together*.

By far the greatest challenge is the passion of youth, admirable in its motivation, dangerous in its frustration. The quest of the young for dignity, sincerity and truth in our generation is one of the two great sources of human energy. The other source is industry. Both are highly progressive and liberating forces. If we allow them to remain as they are today, on a collision course, the future will be dark. If we forge their alliance by reform, then we will have met the challenge of our generation.

Chairman BOGGS. May I say to you that Mr. Stark, who is the executive director of this committee and myself, will be in France to study some of the very issues you raised on August 20, 21, 22, and 23. And may we visit you, sir, in your constituency? We would like to.

Mr. SERVAN-SCHREIBER. August 23?

Chairman BOGGS. August 21, 22, and 23.

Mr. SERVAN-SCHREIBER. I will take the 3 days. Will you come?

Chairman BOGGS. Thank you.

Mr. SERVAN-SCHREIBER. I am very honored. This is very important news.

Chairman BOGGS. Each member will examine for 10 minutes. And as a chairman I will ask the first questions.

Now, Mr. Deputy, there is one glaring omission in your statement. You talk about the events in Indochina which are indeed sapping the energy of this country. You mention your own experiences in Algeria. But somehow or other there is no reference anywhere to the Middle East and the explosive situation prevailing there as I address you. So let me ask you several questions.

No. 1, do you agree or disagree with President Pompidou's decision not to aid Israel in supplying replacement parts for French aircraft in Israel?

Mr. SERVAN-SCHREIBER. Do you have other questions on the Middle East?

Chairman BOGGS. Not quite as difficult as that one.

Mr. SERVAN-SCHREIBER. That is why I would like to start with the last one.

Chairman BOGGS. It is always best to have the worst one first. Would you please reply to that?

Mr. SERVAN-SCHREIBER. Of course. I am at your disposal.

I am so much in the multinational mind myself. First, I would like, if I may, to make a personal remark. I came here, I work regularly, and two of my close friends are here now. One of them is a Frenchman, a man that was in my own promotion 25 years ago, in my school, who has become an active French inventor, banker, in Wall Street. And we are working together. His name is Paul Lepere.

Chairman BOGGS. We welcome you, Mr. Lepere.

Mr. SERVAN-SCHREIBER. The other man is an American, Mr. Samuel Pisar, who is an American lawyer who has decided that the best way to center his activity over the world is Paris, who is the exact opposite of Paul Lepere.

Chairman BOGGS. A very wise decision for him.

Mr. SERVAN-SCHREIBER. So Paul Lepere and myself are not a corporation, we are a multinational team.

So being multinational in our essential conviction, I do not think there is any limit to the frankness that I must have in answering your question.

Chairman BOGGS. I would expect you to be frank, sir.

Mr. SERVAN-SCHREIBER. The fact that I am troubled by the policy of my government in Israel is not essential, but the fact that the large majority of the French people are more than troubled is an essential fact. What we cannot understand—and least of all accept—is that a country that needs for its own defense, vital defense—vital not only for itself, but to all of us—the sacred defense of Israel—all of us at least who participated in the war against Nazi Germany, and you and I, are old enough to do that.

Chairman BOGGS. Yes, sir. I was in uniform just as you were.

Mr. SERVAN-SCHREIBER. We all consider the sovereignty of the state as a sacred cause. There is no limit to what should be done to defend it. I know this is understood in America. I know it is understood by my own people, and by the people in Europe, and more than any by the Germans.

The French official policy is not defendable. It is even less defendable since at the same time we are still refusing to deliver to Israel the warplanes that they have paid for, they have contracted for. This is a breach of honor. This is a breach of contract. At the same time that we do that we are offering weapons to the Greeks and the dictatorship, having in jail patriots, democrats, and people who have fought against the Nazis in a dramatic way, my own government is at the same time offering arms to the Greeks, and refusing to Israel what it needs for its vital defense is not defensible, and it has not been jurable, because I believe in my country, I believe that the feeling of the public opinion in any country as in yours, finally, is the greatest strength, and will change French official policy.

Chairman Boggs. Thank you very much. You have answered the question frankly.

My next question is—the answer is obvious now—but, No. 1, you disagree totally with Pompidou?

And No. 2, obviously you must disagree totally with De Gaulle as well?

Mr. Servan-Schreiber. I have been on the record, not on the Congressional Record yet, but I have been on the record publicly as disagreeing with De Gaulle entirely, totally on that issue, and many others.

But Pompidou—you must understand that the President of my country has a problem. I give you a frank answer. Allow me to say that he has a problem.

You cannot imagine, or you can imagine with difficulty, the incredible charisma that General De Gaulle has had over my country for 30 years—this is very exceptional in history—and still has, not on public opinion—this is diminishing—but on the Gaullist party, and all the leaders of the Gaullist party. They love him. I respect their love for him. I respect him. He was their leader. In very tragic moments I served him. And their way—not all of them, but many of the French Ministries and leaders of the Gaullist party—their way of continuing to respect De Gaulle is to think that what he has made as decisions as to foreign policy are a credo that cannot become changed.

Chairman Boggs. One of our panelists is Dr. Watkins. De Gaulle frightened us in Louisiana when he went to Canada and suggested that Quebec leave, because we were afraid that 17 States might be so tempted in this country.

Mr. Servan-Schreiber. I am invited to Canada the first of September to repair the damage.

Chairman Boggs. Mr. Deputy, what in your opinion would be the effect of the obliteration of the people of Israel? I will put it this way, if Russia becomes dominant in the Middle East, what future do you see either for Israel or for the free world?

Mr. Servan-Schreiber. This is two questions. The domination of Russia in the Mediterranean, and the obliteration of Israel?

Chairman Boggs. Right. Two questions.

Mr. Servan-Schreiber. It is not the same thing.

Chairman Boggs. Please deal with both those subjects, if you would.

Mr. Servan-Schreiber. I will just make you a remark. I am glad to make it. We are very far from international corporations. It means that the American Congress is very free in its discussion. I welcome it.

Russia's presence in the Mediterranean does not trouble me at all. We have fought for 8 years a tragic war in Algeria which tore apart the fabric of French democracy, as we know, just because we wanted Algeria to remain part of the Western World, and we wanted the French settlers in Algeria to remain in Algeria. And the great argument at that time was, the propaganda of the people that were fighting the war, was that if France left Algeria, the Russian fleet and the Russian bases would come to Algeria. They are there. But what difference does it make? Russia's presence in the Mediterranean I do not believe is an acute problem. The American presence in the Mediterranean is very powerful also.

So all these military games, I think, are just games. Because Russia, at least not until now, is wise enough not to come to direct collision course with American power. I do not think it will do it. I think the situation today, in 1970, compared to 1962 in the Cuban crisis, is much better. The Russians have learned their lesson, and nobody would like to have a direct conflict between America and Russian presence in the Mediterranean or anywhere else.

So I put it in a very schematic way. I am sorry to waste your time. I am not interested in military problems, except for the general security of the world. We are happy that America has the nuclear deterrent. But all these little games of military bases and strength all over the world are just games, and a waste of time and a waste of energy.

The obligation of Israel is inconceivable. I believe that America, and rightly so, would be very shy of getting into any nuclear conflict crisis before a conflict with Russia. Two places in the world could immeditaely create the nuclear crisis, Berlin and Israel. And I think it should be that way. And we are grateful to the Americans that they can subscribe to that sacred contract.

Chairman BOGGS. Thank you very much for that reply.

Now, turning to multinational corporations——

Mr. SERVAN-SCHREIBER. This is multinational interests anyway.

Chairman BOGGS. Your visit is fortuitous for a number of reasons. Today we have a growing protectionism in this country. And right at the very moment the Legislative Committee is working on the trade bill, which is very severely criticized. One reason for that, Mr. Deputy, is the feeling, whether justified or not, that the six have looked inward and not outward.

Mr. SERVAN-SCHREIBER. Yes, the Economic Market.

Chairman BOGGS. No. 2, would the accession of the United Kingdom and Norway, Denmark and Ireland to the Treaty of Rome, rather than accomplish the idea which you and I so devoutly believe in: namely, a unified Europe, which hopefully ends the conflicts that have torn Western Europe apart for generations and centuries—your own country has fought three bloody wars.

Mr. SERVAN-SCHREIBER. A century of civil war in Europe. This is ended.

Chairman BOGGS. Please reassure me. Tell me what happens when England comes in? Do you get in a trade war with the United States and Japan?

Mr. SERVAN-SCHREIBER. As you know, Japan is more protectionist than the Common Market.

Chairman BOGGS. I understand that perfectly.

Mr. SERVAN-SCHREIBER. So please ask a Japanese to come sometime. Because they must answer on that problem.

Chairman BOGGS. They have been here. They had a hard time.

Mr. SERVAN-SCHREIBER. Not like me.

First of all, the Common Market will certainly enlarge. This is now inevitable. It is in the cards. England will come in. And not only England, but all the countries that will come with England—the northern countries are very interesting to us—Denmark, Norway, and Sweden, I think are an essential part of Europe.

And I also think that the mission of Europe is to enlarge that a bit further. And Europe should go from Spain to Sweden, and from England to Greece. And it will come in the next few years.

Now, will that be the beginning of a commercially industrial war against the United States? Any progressive industrialists, any progressive statesman or politician, should welcome competition, which is war in a way. I am very happy if an automobile factory like Arnot or Volkswagen or Fiat tried to invade your country, I am very happy, because you are invading ours. And this is good. This is just economic war.

Chairman BOGGS. It is a free enterprise system.

Mr. SERVAN-SCHREIBER. It is the progressive system. It is like that that you progress. It is competitive economy.

Now, protectionism, whether it is here or in Europe, is a regressive measure.

I want to be very frank and make two remarks: One on the American attitude; the second on the European attitude.

On the European attitude, I think we are allowed—not by you, we are not waiting for your permission—but we are allowed by our own self-interest to be a little bit careful on the very advanced technological industries like computers, electronics, the industries that are creating all the system of the future. We should be able to be part of it. And the Americans should not deliver it freely, it should not be a new Marshall plan on technology.

So we have to develop it by our own means. This takes a little bit of time. And we should be careful on these sectors. On all other sectors there is no reason for protectionism in Europe.

Now, protectionism——

Chairman BOGGS. How about agriculture, Mr. Deputy?

Mr. SERVAN-SCHREIBER. Protectionism in America—we feel that the debate here is taking a turn that might have very grave consequences. Because we must have not a doctrine—we are not doctrinaires, we are not and you are not—and we should not have a religion, but we should have a kind of orientation toward progress.

If America becomes protectionist, what is the message of America? The message of America, it seems to me, after it is finished with those vain attempts to make people accept by military pressure or military wars any system, message of America, an immense possibility for America would be economic growth all over the world, including Russia, and including China. So protectionism here is exactly in contradistinction with your message.

Chairman BOGGS. Let me say to you that I was shocked and distressed and dismayed when President Nixon recommended a quota by law on textiles. I think we will resolve that problem as we go down the road.

Now, isn't it a fact that if the Europe that you envisage, namely, one that is open, and the Japan which today is a modern miracle, and the productive capacity of the United States, if we utilize every textile mill, every steel mill, every productive facility in all of these developed areas of the world, we still could not supply the demand that exists in the world in the developing nations, isn't that right?

Mr. SERVAN-SCHREIBER. That is so true.

Chairman BOGGS. Finally, when you come together, will you have a common currency?

Mr. SERVAN-SCHREIBER. Europe?

Chairman BOGGS. Yes.

Mr. SERVAN-SCHREIBER. We will start with the common reserves—gold, dollar reserves. This will be, I believe, a starter. We must organize our common reserve system so that we will not fight but negotiate with the American dollar, which we are not doing today.

Chairman BOGGS. Right.

Mr. SERVAN-SCHREIBER. And then from the common reserves the next objective would be common currency. But as you know, obviously this means a kind of federal power. You cannot have a common currency without some kind of federal power. This is why just logic will lead us to federal power.

Chairman BOGGS. Address yourself to that, please.

Mr. SERVAN-SCHREIBER. I would like to tell you that one of the reasons that we admire America for its history and its development, even if we criticize its policy in more sober terms, as you are doing yourself.

Every time we are attacked as being too much critics of American policy, I take speeches by the Senators or the Congressmen here and say, they are much worse than we are.

But even if we attack American policy on such and such a sector, we have a great admiration for what you have built here.

But one of the things we must have in mind is that Europe should not be a copy of America. In other words, there will not be, I believe, a United States of Europe. There will be something else. There will be federal power, obviously, because you cannot have common currency, you cannot have foreign policy, you cannot have defense, without federal power, at least in a limited way.

But I believe it will be more of a committee, a federal committee at the head of Europe, elective committee, responsible to parliament, but not a president of Europe. We shall not do it because we think it is not very good, it is a little bit outmoded. And second, we do not want to copy the American model.

Chairman BOGGS. You have been very generous. And the committee has been very generous with me.

Our distinguished senior Senator from New York, Senator Javits, who has made a monumental contribution to trade policy as well as to policy between Europe and America.

Mr. SERVAN-SCHREIBER. Senator Javits is known in France as well as America.

Senator JAVITS. Thank you very much.

I thank the deputy, Mr. Servan-Schreiber, for his kind observation. And I am very grateful to the panel for appearing to help us with this great problem.

I also was deeply interested in hearing what you had to say about the Middle East, and about the Soviet Union.

As an anecdotal memo, you may be interested to know that Mr. Pisar accompanied Mrs. Javits and myself to the Soviet Union 7 or 8 years ago, where we looked for the first time into the opportunities, possibilities, and barriers to international trade with the Soviet Union. So it is very felicitous that you have him with you.

I would like also to know some of the things that I think are important to us; first, what is the attitude toward the value or worth of the multinational corporation (as you have described as mainly American in Europe); and second, what is to be done about it, aside from the primordial competition which ensues?

Could you tell us whether or not in your view the coming of the multinational corporation to Europe has been beneficial to the people of Western Europe?

Mr. SERVAN-SCHREIBER. The answer is definitely yet. By definition I think multinational corporations are strong, dynamic, and they are creative. They invent new processes all the time.

I will be more specific. One example: In one of the most beautiful parts of France, in the southeast, there is one of the major laboratories, research laboratories of IBM, in the Provence part of France, And this laboratory, having French scientists working for it, is making new inventions for IBM all the time. And so this is excellent, because it puts French scientists in a very good and creative mood, because it creates incentive for other French industries to do the same, and because it forces us to become competitive.

Now, the thing we are worried about is our own passivism in recent years and the fact that the American multinational corporations have been able to play all around the Common Market with a completely free strategy, because the Common Market is a purely commercial agreement. My fight, and our fight, many people in France, is that it should not remain a purely commercial agreement, it cannot do that. it is a jungle, and it is a jungle where the American corporations are dominating just by the force of nature. And so we should have a political power, not to prevent the American international corporations for coming, because they are beneficial, undoubtedly, but just to have law, some kind of public law, like in this Republic.

So it is our problem. We have nothing to ask you on that. It is our problem, our responsibility, and we should do it.

Senator JAVITS. Isn't it true, however, that if you should utilize the power of politics to restrain or restrict the multinational corporation, that it will cease to be your problem, and will become our problem too, as it is just as possible to exclude products, ideas, and stimulation to your own economy by repression through law and politics as it is by repression through economics?

Mr. SERVAN-SCHREIBER. No. I did not say repression, I did not say restraint. I do not mean it. I said that I think this separation between politics and economics like the separation of church and state, should be one of principle.

But what I mean is this. A multinational corporation today in Europe responds to no interlocutor for new political power. It is just its own master. It does not exist in your own country. What we want in Europe is something resembling the American partition of responsibility, there is political power, there is economic power, and there is constant negotiation between those powers and the union powers. In

Europe today there is the multinational corporation economic power, and there is no political power that can talk to it, not prevent or restrict or make it impossible, but just talk to it. What are we suggesting to do, where are you going, in what region of Europe, how can we help you, and what are you going to do for us? Talking to these people. They just do what they want, because there is no interlocutor.

We shall not restrict. This is not our philosophy, it is just the opposite.

Senator JAVITS. As a matter of fact, the corporations in Europe are subject to all the local laws, are they not? For example, IBM as per your description, is subject to the law of France; correct?

Mr. SERVAN-SCHREIBER. Yes, sir.

Senator JAVITS. So that if France had an antitrust law like that of the United States which, incidentally, is a considerable restraint on the multinational corporation—as we apply the law of extraterritoriality, that is, as we apply the antitrust law to the IBM even in its operations in France, don't you think that is the beginning of an important political restraint on a multinational corporation?

Mr. SERVAN-SCHREIBER. The only thing I would like to see ending is the fact that since we have no political power at all in Europe except national powers, each one of these national powers is intervening in a very negative way, because they are trying to subsidize the American corporations to go to such-and-such a place for problems of national identity and not for problems of economic progress.

That is why I am fighting in Lorraine, for instance, because this is the heart of Europe—one of the hearts of Europe—I do not want to make too much of it, but it is a very sensitive part of Europe. And the political response is to discuss, not to prevent, but to discuss with the multinational corporations, where it is better for us to go, let us discuss about it. Today nobody discusses about it. It is just subsidizing and saying that they should go to such-and-such a national state, which is not in the better interest of the people of Europe.

Senator JAVITS. I am very interested in your broad ideas. And I quote one from your prepared statement. I would like to get to one of the other witnesses on this one. You say:

> This quest for human dignity in our contemporary economy is not a Utopia. It is the essential role of politics. Reform without revolution is possible; and it is the duty of our generation, in Europe and in America, to bring it about.

Do you believe that we can enlist the multinational corporation into a true organization of economic progress not only for ourselves but for the countries in which it operates, so that it becomes a greater incentive, not only to competition in the stimulation of the activities and initiatives, let us say, of French industry, but also to human freedom? And if so, how? In short, shall we adopt Mr. Rubin's concept of a GATT, or General Agreement on Tariffs and Trade, as kind of a world body to deal with the problems of the best public usefulness of multinational corporations? Shall we insist on a nationalization of multinational corporations in the countries in which they operate, that is, where a very important part of the ownership be vested in the indigenous population? What do you think we ought to do in order to take an admittedly great instrument like the multinational corporation, which has shown an ability greater than any international instrument that we have yet developed for economic advance and breakthrough, and use it for the benefit of all the people?

Let us have you, Mr. Servan-Schreiber, and then we will get to Mr. Rubin.

Mr. SERVAN-SCHREIBER. Your question is very subtle. We have two problems here.

First, and more urgent, and perhaps the most simple problem, is whether by creating industry, know-how, technology, helping to do it in the eastern empire of Russia, we can bring about progressively more freedom. I think it is obvious—I think it is obvious—I think they are discovering—because we have the Russian text and the Czechoslovakian text and the Hungarian text, they write it themselves, they say without competition, without responsibility, without initiaive, modern economy cannot be competitive, and this need to be so. They are changing. This is the subject of your friend Pizar's book. They are changing. And this is very encouraging. So without reforming—because it is your judgment, and a reform of our own industrial state is not a task that she can do in a few weeks. But the fact that we should decide whether or not American and European industry in the eastern empire of Russia is good for all of us in an urgent question to answer. And when we see that someone like Henry Ford, to be called by Mr. Kosygin to build factories in Russia, and as far as I can recall, and if my information is correct, that the American Government vetoed such a decision, we do not understand what is the American policy.

The more enterprises, the largest number of enterprises that Henry Ford, and others, and IBM and General Motors and Westinghouse, could create in Russia, the best our interests will be served.

So American policy should be clarified.

European policy is clarified on that issue. The Germans are invading Russia. Siemens is invading Russia. Mercedes-Benz is invading Russia. German Chemical Industries is going to Russia. French industry is going to Russia. And Fiat is going to Russia and Eastern Europe. For once we have a policy. We think it is good. And I think this is a question for Americans to answer in a clear way.

But the second question is more difficult; reform of our industrial system. Because this is our own pacific civil war, or maybe not so pacific.

This I do not think you want me to be too long on. We have prepared in France, and we are discussing with the German Social Democrats, with the Austrians, with the Swedish, we are meeting in October exactly on that point in Europe, where we have the luck of not being a great power militarywise, of not having your responsibilities in crises and problems. We have a great privilege—we are paying for a hundred years of civil war and now we are a peaceful power in Europe. So we can get together to discuss what is the real form of the industrial.

I have my proposal. I will not take your time. If I may, I will send you what I have published.

Chairman BOGGS. We would like your proposal as part of the record of this hearing.

Senator JAVITS. I ask unanimous consent for that privilege.

Chairman BOGGS. Without objection it is so ordered.

Mr. SERVAN-SCHREIBER. Mr. Chairman, I will send it, if I may, in the next 3 days a summary in 20 pages of what are the reforms that we have proposed in France, that we have won votes on, and that we are discussing now with the Germans.[1]

Just one little item, because it is significant—I am sorry, it is personal, but significant.

The book we wrote about my party which is called "The Radical Manifesto," radical in France does not mean radical in America, it means moderate reform.

Chairman BOGGS. The same as the Democrats in the United States.

Mr. SERVAN-SCHREIBER. That book is today No. 2 on the best seller list in Germany. This is very encouraging. The Germans are quite open to the free exchange of ideas and discussion, and they have proposed 10 days ago to me in Bonn that in October all the reformist people in Europe should meet to have a common program, common propositions. I think at that time it will be then more important for you to have those suggestions and examine them and criticize them and perhaps discuss them.

Chairman BOGGS. Exactly.

Senator JAVITS. My time has expired.

Chairman BOGGS. You have 5 additional minutes.

Senator JAVITS. In that case, I would like to ask Mr. Rubin to comment on that.

Mr. RUBIN. Thank you very much.

I would like to say that I agree entirely with what Mr. Servan-Schreiber has just said, particularly with respect to the futility of a restraint policy so far as the United States in concerned in its relations with Eastern Europe. My own experience with the Battle Act indicated that one is likely to induce the creation of factories rather than inhibit the development. I would agree entirely with him on his general observations there.

There is one other observation that I would like to make. That is in connection with his own thesis about the American multinational corporation and his prognosis of what is happening. It does seem to me that there may well be changes in Europe in connection with the multinational corporations there, as industry matures. This has been the case, I think, in connection with the oil industry, say, in the less developed countries: at first they were highly dependent upon American Home Office. As technology advanced, as they found that they could hire the technology from many sources. They then ceased to be so dependent upon an individual company with production and marketing competences, and they became more and more independent. Yesterday there was a suggestion that the IPC case in Peru might have depended more upon that economic factor, than on political factors.

Third, I would like to say that I think I detect in the remarks that Mr. Servan-Schreiber has made some support for my thesis that there ought to be a forum, perhaps the OECD and perhaps another forum, for the discussion of these various problems.

Senator JAVITS. Thank you.

Chairman BOGGS. Mr. Reuss?

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[1] The information referred to by Mr. Servan-Schreiber for inclusion in the record was not available at the time of printing the hearings.

Representative REUSS. Thank you, Mr. Chairman.

Mr. Servan-Schreiber, you mentioned to the chairman before your trip to America some years ago. I recall, on that trip, your being in my city of Milwaukee and coming to my home. And we discussed, among other things, the Congress which I then proposed running for, and the National Assembly. It is good to see you here again.

Mr. SERVAN-SCHREIBER. It is good to see you here.

Representative REUSS. I listened with intent interest to your exposition, and I took a few notes on it. I would like to read them back to you to see whether I have got you straight. What you said, in essence, was that increasingly young people today seem to be turned off by industrial society, and particularly by the multinational corporation, and that you think some reform is necessary, and included in those reforms would be at least the following goals for this country:

1. Take a lesson from the French in Indochina and Algeria and extricate ourselves from Southeast Asia as speedily as possible.

2. Intensify the cooperation between America and a federalized Europe.

3. Intensify economic cooperation between the countries bordering on the Atlantic and the eastern European countries—Poland, Rumania, the Soviet Union, and so on.

4. Develop institutions for subjecting multinational corporations to social control.

Is that a fair statement of your thesis, which I find an inspiring one?

Mr. SERVAN-SCHREIBER. I was told last night when I was in Washington that as soon as Mr. Reuss starts speaking I should be afraid, because he is such a sophisticated economist. So I am afraid. But I will try to answer you.

I think you are clarifying very well what I tried to say. But this covers what I would say should be the foreign policy of the industrial state, ours. It does not cover the world reform as I meant it.

When you say stop military adventures, I could not take any more.

Three, more debtable but very important, open the East to freedom through economic corporations and exchange.

And four, as you said, more social, or let us say, political control of multinational activity all over the world.

Those four points I would agree entirely would be the foreign policy of the industrial state.

To me the term "reform" is what is the internal reform of the industrial state. What do you do for the American industry and the European industry to become something that is more human, for, in its objects, and results, and benefits, and second, in its open performing system? Those are the reforms, internal reforms which I propose to send to the chairman, because I do not want to waste much of your time.

Just to give you one example of what we mean by reform, we think that people who are becoming chief executives of big corporations, the masters of the decision, will not in the future, and should not be, chosen without any consensus from the people they are going to govern. We believe in some kind of democracy inside the industrial state. We do not think it is possible to maintain for very long the fact that 450,000 workers in a corporation suddenly can be told that a new boss is going to direct their lives and their activity, and they have nothing to say about it.

It is conceivable in a democracy in political terms. We think it is inconceivable in industrial terms. We will have to find a solution.

Another example, when a man is a creative man, and becomes a big industrialist, and creates activity, science, invention, and development, we do not think there is a problem if he becomes a rich man. He deserves it. This is incentive, and this is good.

This is where we completely break with the religion of State-owned industry and collectivist society and Communist society, and what is called a Socialist society. So we believe in incentive. And if that man pays his taxes he has a complete right to enjoy what he brought to the world by his creativity. But why should he—this is more true in Europe than in the States—why should he by the law of inheritance give to his children the same right, even if they are incompetent? This should be reformed also. And we have proposed that this should be profoundly reformed, in other words, introduce democracy and participation inside the industrial state.

Just two examples. This is the internal problem. And you clarified very well on the foreign issues the foreign problem.

Representative REUSS. Let me now turn briefly to the radical Socialists, lower case. I take it gentlemen, that your reaction must be like mine, that as capitalists go, Servan-Schreiber is an edifying one. However, he does come down strong on the side of separating political and economic life. And in a sentence there he says:

> If those who reign over industry are also to be those who by their influence dictate the direction of political life, then we will inescapably fall into the most bitter and dangerous social upheavals.

Both of you gentlemen, Mr. Hymer and Mr. Watkins, feel that public ownership in at least a large sector of industry is the way to overcome some of the defects of our system as you now see it. Is that a fair statement of your view? And if it is, how do you meet Servan-Schreiber's point—don't mix economics and politics?

Mr. HYMER. I do not think that you can separate economics from politics. The last 25 years of prosperity may have been deceiving on this score. Perhaps the last 5 years, which I at least interpret as 5 years of serious trouble and difficulty, are more indicative of what the next 30 holds.

It is hard to give all the arguments that one would wish to use to bear out this case. For now I would just like to note that the test of these ideas will be practice.

We might use two historical models to understand how an international world based on the multinational corporation could come about. First, the unification of the U.S. economy. I do not want to talk about the difficulties necessary to bring about this unity, the Civil War, for example. I just want to say that conditions prevailing in the United States were quite different than conditions now prevailing in the world as a whole, which is organized into nations with long traditions. Therefore I do not see that the ideas on which America was built can serve as a model for world organization.

Second, and perhaps more important, we should note that this is not the first attempt to build an international economy. It was just about a hundred years ago in 1870, that England attempted to construct its world system. And I daresay that the representatives in Parliament at the time were more optimistic about capitalism triumphing than their counterpart here today.

We now know that following this "new imperialism," we did not get a century of free trade, Pax Britannica and material improvement as expected. Rather we got war, depression, breakdown of the international system, and war again.

I do not want to be too pessimistic, but I do not think that it is correct to underestimate the seriousness of the problem. The corporation is a private institution, and a partial institution: to think that the whole 4 billion people of the world can be organized along lines envisaged by a few—what did Mr. Servan-Schreiber call them? Masters of decisionmaking—is, I think, not realistic, aside from the fact that I do not think it is right.

Representative REUSS. Thank you very much.

I would like to give Mr. Watkins and Mr. Servan-Schreiber a chance to comment on this. So I will yield now and wait for the second go-around.

Chairman BOGGS. Senator Percy?

Senator PERCY. Mr. Chairman, on a personal note, I presume that Deputy Servan-Schreiber has noted, as I have, since he is now a new deputy in the French National Assembly, that you finally get down to the newer Members of the Congress toward the end of the morning.

What he might not have noticed is that in the room for the first time that I know of in my 3½ years in the Senate are two Senate wives, Mrs. Javits and Mrs. Percy. My own daughter is also here. My wife, Loraine, is not used to coming down frequently, but she came to see the deputy from the legendary region of Loraine.

I think you have been a great attraction. I trust you have gained a great deal of popularity among the women in your own district.

Mr. SERVAN-SCHREIBER. Mostly older women.

Senator PERCY. Mr. Chairman, I would like to refute that, but I will not.

We had another Frenchman come to the United States in 1832. And I believe——

Chairman BOGGS. He wrote a book too.

Senator PERCY. Right. And I think almost anyone who fails to really understand American institutions and the source of our strength should go back to de Tocqueville and reread him. Because I think he still today has the best insight that anyone has as to why this country has become a great country and how any country can become a great country. I really look on this second coming of a French prophet—and I think the impact of our guest this morning is going to be just as great.

For those who are in the business community as I was, and who feel that this country cannot compete, and ask for quotas and protections and tariffs and restrictions and try to turn the clock back 30 years in trade relationships, I strongly recommend that they read "The American Challenge" to restore faith in their own country. And I hope the executive secretaries of the trade associations in this room will reread it.

Mr. SERVAN-SCHREIBER. I would like to say at this time that though we never met, Senator Percy, you are advertising any book on a friendly basis.

Senator PERCY. And I am not asking for a fee at all.

Mr. SERVAN-SCHREIBER. I am overwhelmed.

Senator PERCY. But it is a great book with great insight into our country. And we are all for you.

I would like to ask, because you have indicated that U.S. companies are using the savings of Europeans to finance the acquisition of local industries, whether you feel that the direct investment controls imposed in 1968, which then put great pressure and encouraged rapid growth of U.S. corporate borrowings in Europe, might not have really ended up in a way that we did not intend at the time they were put on. I opposed their being put on. I encourage their being taken off.

Wouldn't their being taken off relieve this kind of pressure?

Mr. SERVAN-SCHREIBER. They are being taken off?

Senator PERCY. No, they have not been taken off yet. President Nixon said that he would take them off at the earliest possible time. But wouldn't taking those controls off ease the pressure on the use of European capital for the acquisition of companies abroad by American companies?

Mr. SERVAN-SCHREIBER. Direct investment control, instead of preventing or putting the brakes on American investing, has caused our own money market to borrow.

Senator PERCY. And driven interest costs up?

Mr. SERVAN-SCHREIBER. Of course.

Senator PERCY. There is one other area of pressure that could be relieved. Just within the last month the Economic Committee of the North Atlantic Assembly unanimously approved a resolution suggesting that burden sharing be accepted by the European NATO countries for NATO expenditures by the United States for the common defense. We have a billion and a half dollar balance of payments deficit because of NATO costs. Wouldn't it help relieve this pressure if European countries budgets picked up a more proportionate share of defense costs in their own defense commensurate with their present levels of prosperity?

Mr. SERVAN-SCHREIBER. Senator Percy, I know you have been leading a movement toward that aim. I cannot envisage as a European any reservation to follow your philosophy. I think we should support what you have asked for. I think we should say publicly, say it publicly in Europe, from Paris, from Bonn, from Rome, this will help you here, and not only you, but America's economy and America's understanding of the world problems. It is not normal, you are so right, that we are free to criticize, attack, not only American policy in Vietnam, but also the dollar domination and all the other problems of economic or money-type problems, and in the meantime under the table we ask the Americans to take all the bill for our own defense. It is not healthy. And your views on that are already known in Europe, but not enough. Explain it to Europe. It is very important. Go to Germany, go to Italy, go to France, and tell them, let us be very clear, what do you want? What is your own interest? I think your proposition is a health one not only for the balance of payments, but for the health of our relationship.

Senator PERCY. I am very happy to be able to report to you that I did go to Germany. I talked to Chancellor Brandt——

Mr. SERVAN-SCHREIBER. The Germans are responding well.

Senator PERCY. I talked with the leaders of the major parties in Germany. And I have no disagreement with them whatsoever.

Mr. SERVAN-SCHREIBER. Germany is responding very well. And they are the most determined. So the Germans are taking the lead, answering your question. And this should be known here.

Senator PERCY. I would like to clarify once again your attitude on East-West trade, because I think it can be exceedingly helpful to us. I have always said that European countries look on us as suckers when they see restrictions by the U.S. Government on our doing business with Eastern European countries when goods are freely available in France, Germany, Great Britain, and other countries. They are amazed that we have such blinders on. In our ideological battle, what we forget is that what we lack is gold, and what we need is trade. We need to improve the balance of payments, and we are restricting artificially our doing business abroad and opening these markets to European countries.

Chairman BOGGS. Would the gentleman yield to me?

Senator PERCY. I would be happy to.

Chairman BOGGS. I would like to say for the benefit of our distinguished visitors, all of our visitors, that a year ago Senator Percy was president of one of the great camera companies in this country. His great competition came from Japan. And he came before this subcommittee, and also before my Subcommittee of the Ways and Means Committee, which is a legislative committee, and he testified against any import restrictions on Japanese cameras.

Mr. SERVAN-SCHREIBER. And he still got reelected?

Chairman BOGGS. No; he had not run then.

But I am sure he will be reelected. I hate to say that as a Democrat.

Mr. SERVAN-SCHREIBER. This is very important.

What was excatly the question, Senator Percy?

Senator PERCY. The specific questicn is, don't you really feel that it is contrary to the interest of the free world and to the U.S. self-interest for us to have all these artificial restrictions on American business doing business in nonstrategic goods with Eastern Europe? Isn't the best way to penetrate the Iron Curtain to normalize wherever we can our relationships between all countries?

Mr. SERVAN-SCHREIBER. Absolutely.

I will give you one little concrete example of what can happen. Four years ago France, as you know, had a normal relationship with Communist China. I believe Communist China is one of the wise countries in the world. It talks very loud, but it does not act in an adventurous way. I do not know of any action taken by Communist China that resembles the responsible actions that either Stalin or Khrushchev have made. So I have respect for the wisdom and carefulness of China's Communist policy.

So the French Government has a normal relationship with Communist China. And I hope your Government will have as soon as possible.

The Government of General De Gaulle made a commercial deal with Communist China on a very fine French plane, the Caravel, as you know. But because in the Caravel there is a little part of American technology, America vetoed the deal, and the French were not allowed to deliver the Caravel, which is a very peaceful plane, to Communist China, because the small part of American technology in it gave America the right to veto it.

So this is how we can be embarrassed by the unclarified issues of our own self-interest.

So I entirely agree with you.

We shall discover, I think in the 1970's, because it is so obvious and so forceful, that the way we can change the relationship with the Eastern World and change the internal structure of the Eastern World is by making no limit on trade, exchange, the creation of industries, economic progress. Everything we can do is good for them, and for us.

Senator PERCY. I thank you very much. I have been extremely pleased with the progressive attitude of the Nixon administration with respect to China. I think it has taken several very significant steps to indicate that more doors can be opened to take China out of the outlaw condition which is dangerous for all of us.

But there has to be some response from Peking to the three initiatives that have now been taken before we can take the fourth, I think.

It is also interesting that Communist China has not put a single soldier in Vietnam.

Mr. SERVAN-SCHREIBER. I am quite sure if Communist China had wanted to make an assault on Quemoy and Matsu any time in the past 10 years America could not have prevented it. But they have done nothing that is adventurous. This is important. They are less adventurous than the Russians.

Senator PERCY. Mr. Chairman, I would like to put my last question to the other three panelists.

Let me precede it by a statement that we have high regard for each one of you, and we are privileged to have each one of you here. And I trust that you will have to understand that we simply can reach you so much easier than we can our fellow legislator from France.

Chairman BOGGS. May I concur in that statement?

Senator PERCY. We just hope you will excuse our concentrating so heavily on him, because we feel that we will be inviting you back many times. I tend to think that the increasing responsibilities that will be taken by our fellow legislator in France wil keep him rather occupied and not able to go back and forth as frequently as you can.

He has already expressed himself on Japan. I had a long talk with Mr. Aichi recently in which I said that I did not see how Japan could continue out of one side of its mouth to talk like a developing nation and keep restrictions on investment and products being brought in on the one side, and on the other side talking about how they are one of the most powerful economic nations on earth. They cannot have it both ways. How dangerous do each of you feel it is if Japan does not remove some of these restrictions that they now have so that those who want protection and barriers built around countries will not have this example to point to? It is utterly unfair. And I say that as a long-time friend of Japan, and an admirer of its economic power.

Mr. RUBIN. If I may respond first, Mr. Chairman—and I will be very brief—I am here in Washington, so I am very available. I live a block from you, so I am even more available.

Senator PERCY. Drop over any time. And I hope I may feel privileged to do likewise.

Mr. RUBIN. I find certainly on the basis of my own experience in the OECD that this ambivalent policy on the part of Japan is one which is most unfair and unfortunate from the point of view of Japan as well as from the point of view of other countries, developed and less developed.

Senator PERCY. Thank you very much.

Mr. WATKINS. I find it difficult now to understand what happens in Canada and advise there without trying to understand what happens in Japan. But I would have thought that we would have to point out that Japan is an extremely dynamic and very rapidly growing economy. And there are some people in my country who are impressed by the skillfull way in which the Japanese can use protectionist measures and can strengthen their own corporations in the process and increase the rates of their economic growth. And I would share Professor Hymer's views stated earlier, that the rebuilding of the international economy is a far more complicated task than simply saying, "everybody must be for free trade." And I would be most reluctant to tell the Japanese that they do not know how best to run their own affairs in this manner.

Senator PERCY. But what they are doing is not just running their own affairs. What they are going to bring on is retaliation—and that affects all trade throughout the world—if they do not do something to correct their internal policy. It is not just an internal policy. We simply cannot say that what they are doing affects Japan only. It affects every one of us. They cannot have unlimited access to this market in steel, and let me stand up for my constituents such as a company like Inland Steel, and at the same time not take back American automobiles and refrigerators with Japanese steel in them. That affects our policy toward Japan and I cannot defend Japan's policy.

Mr. WATKINS. I would say in that case, sir, that is a problem for the United States. What I am trying to get at really is to suggest that we have to do a lot of rethinking about the virtues of free trade and the virtues of the international economy.

When you talk about the various kinds of dependency, on the whole the rest of the world is very much more dependent on the United States than the United States is dependent on the rest of that world. And again I would be most hesitant to say to Japan that we can be absolutely positive that they must free their trade in order to be a responsible member of the world community.

Chairman BOGGS. We will go now to Mr. Moorhead.

Senator PERCY. Thank you very much, indeed.

Representative MOORHEAD. Thank you, Mr. Chairman.

And thank you particularly for assembling this inspiring and edifying panel of witnesses. It has been the most interesting testimony I have heard since being in Congress.

With your permission, Mr. Chairman, and your example, I would like to ask a question not related to multinational corporations, but with respect to Israel.

Chairman BOGGS. The rules of relevancy do not apply.

Representative MOORHEAD. Mr. Servan-Schreiber, in reply to the questions of the chairman, you stated what I think is the most important aspect, that the majority of French people do support Israel. But then you alluded to the experiences of World War II. And I wonder if that same feeling applies to the younger generation, those who do not have any memory of World War II? Does the younger generation share your strong commitment to the preservation of Israel?

Mr. SERVAN-SCHREIBER. I understand the question.

The answer, I am afraid, is no. But I would like for a few minutes to comment, because it is a very grave answer.

Representative MOORHEAD. It is. And it was what I feared. But I hoped it was not going to be your answer.

Mr. SERVAN-SCHREIBER. I have to be frank with you. I am quite sure that if you were taking a real poll of opinion today in my country, or all Germany, on the support of Israel, unqualified support, anybody over 35 would be 90 percent, people of 20, I would not care to say what would be the number, it would not be very small, not at all in the same proportion. But why? This is our problem.

These young people—and you know them as well as I do in my own country—they are always on the side of what they feel are the weaker people. It is true for the Negroes, it is true for the poor people, it is true for the North African workers in my country, and it is true for all over the world. It is true for the underdeveloped world. Now, in the Middle East situation the feeling is that Israel is very strong militarily. The fact that Israel has won every war in such a superb way makes them feel that Israel is the dominating power in terms of strength. So they tend normally to be on the side of the weaker people, to be sympathetic to the Palestinian guerrillas, and even to the Arab countries, because they are weak. This is not bad. But this shows how your question is important and delicate.

Second, everybody knows that the only real protection, of Israel, not against Egypt, but against Russian missiles or Russian pilots, or Russian attack, is America. Since America in the minds of the young radical people is linked to some kind of imperialism, because of Vietnam, the image of America, altered by Vietnam, has consequences on Israel, and on the backing of the young people toward Israel. If America was not fighting a war in Vietnam, my answer to your question, sir, would be—and I would be so happy—would be yes, they are exactly the same. But today because of the altered image of America they would not go all alone.

Representative MOORHEAD. I thank you again for your very frank answer.

Mr. Watkins, I would like to ask you a question about your prepared statement. You state that the foreign direct investment is much less necessary to economic development than is usually thought to be the case. Are you referring to a developed country like Canada, or do you include in that statement the underdeveloped countries of the world?

Mr. WATKINS. I know more about the developed countries, but I would in fact believe that this statement is generally true, that the argument in its simplest form is that these countries have to learn to do things themselves, that the entry of giant and powerful corporations which may well create short-run benefits may have the very longrun and serious effect of inhibiting the kind of initiative that these countries themselves must take.

Representative MOORHEAD. Do you include foreign aid in this?

Mr. WATKINS. That would depend, I would think, on what the character of that aid was, what the nature of it was, what strings were attached, whether that aid is or is not used as a means by which America or any other country giving that aid tries to get special access for its corporations or special access in terms of its trade. I would regard the use of aid if that is involved, as quite inappropriate, and simply another kind of dependence that is being imposed on the country.

Representative MOORHEAD. Did you want to comment, Professor Hymer?

Mr. HYMER. I just want to say that I agree. I think there is no question that the underdeveloped world needs to borrow technology, and in some cases capital, and also to exchange goods with the rest of the world. But for underdeveloped countries to allow major decisions—and I think that foreign investment is basically a movement of decisionmaking—to be made far from their country would not promote development. I think it is important to realize when we look at underdeveloped countries that, roughly speaking, the top one-third of the population get but two-thirds of the income, and the bottom two-thirds of the population share but one-third. The prognostications of the Pearson Commission, the United Nations, or anyone else about the development in the future do not promise by the end of the century much improvement in the lot of the bottom two-thirds of the population.

You can go now to the most rapidly growing places in the world, to Hong Kong, to the Philippines, and see poverty produced at the same rate as development. This uneven character of development is one of the reasons for the great dependency on multinational corporations.

The multinational corporations supply a small, high-income sector with automobiles, lipstick, and other things—even cameras—with brand-name products made by foreign corporations. The national middle classes are outward looking in their taste patterns and therefore dependent. If the underdeveloped countries were to concentrate on what their real problems, and I think all of us would agree it is the problem of poverty, that is the problem of providing shoes and basic food for the whole population. Their dependence on foreign corporations would be much less. The strength of the multinational corporation lies in advanced products, not in the necessities of life.

Representative MOORHEAD. Mr. Servan-Schreiber, I read with great interest the way you phrased the contest between the economic and the political forces. And as a politician yourself you said that the main goal of politics is to prevent this ferociousness of competition from hurting man himself. And certainly we here in Washington have seen, tasted, and smelled the situation of air pollution in recent days, and we have seen it all along the eastern seaboard of the United States. The only consolation we can take is that it seems to be more ferocious in Tokyo. I think that this would be one of the things that we would have to watch about the multinational corporations, so that they would not go to those national states where they could continue their dirty, dirty ways. And since the air blows freely across borders, some institution would have to control this problem.

But because my time is running short, I think I see the basic conflict that comes out of this panel, that you, sir, would say, let us separate economics and politics——

Mr. SERVAN-SCHREIBER. In a relative sense.

Representative MOORHEAD. Yes—and permit and even welcome multinational corporations going across artificial borders, and you think that this is the way of the future, whereas Mr. Watkins, at least insofar as Canada is concerned, would advocate domestic socialism, nationalism of the industries, and presumably the prevention, or at least limitation of international corporations crossing over the border. The concern I have about Mr. Watkins' proposal applied generally would be that it would seem to re-create the force of the nation state, which is the very thing that I think you are advocating a change in. Would that be correct, sir?

Mr. Watkins should be allowed time to rebut this statement, after you make any comment you wish to make.

Mr. SERVAN-SCHREIBER. You spoke about air pollution as an example of some lack of responsibility until now from the industrialists. It is true. And we are encouraged by the fact that American industry is taking cognizance of that kind of problem, and that the American Congress is forcing them to take cognizance of it.

Japan, I think, is a fantastic example in front of us, and very illuminating. When I was speaking—and it was too schematic to be true—of a progressive separation between the political responsibility and the industrial responsibility, I was thinking largely about Japan. In Japan industry and Government are in the same hands, largely speaking. The same people are in Government, and at the head of industries. Then you have a crisis. Of course, it is expanding. But you cannot swim on any beach on the coasts of Japan, because it is so filthy. And you cannot breathe in Tokyo. Because only the expansion of industry is considered both by the industrialists, which is normal, and by the legislative body, or the Government people, because they are the same people.

So Japan is the example of what we should not do in terms of human progress, and not only gross national product.

Now, I was not advocating, of course, that the state and the public power should be indifferent to the industry. On the contrary. But whose responsibility is each state? I do not think that the state is the best entrepreneur. And I do not think, which is more important, that the state money, which is the taxpayer's money, should go into a deficit industry. It should not go. It should go, to make it very quick, I think to do two things: First, the basic equipment of the company, in hospitals, and education, in health and communication, in housing.

This is the public responsibity. And it takes a lot of money.

So if you do not put the state money into industry, you put it into infrastructure and collective equipment.

And second, if we want industry to forge ahead so as to be able to dismiss people and put people out of work, which happens, of course, in change, then the state responsibility and money should be devoted to taking care of these people so that this revenue has never diminished, and they can progress in their qualifications and their profession.

Chairman BOGGS. We are going to have to move on now.

Just one question that I would like to direct to the very able witness, Mr. Watkins, from Canada.

I have a Washington Post story written by Gerald Waring, with an Ottawa dateline. The essence of it is that every corporation in Canada would have to have at least 51 percent Canadian ownership. Are you aware of this?

Mr. WATKINS. Yes, sir. That is a recommendation made by a House of Commons Committee on External Affairs in Canada, and a report that has not yet been made public, but that is now widely known.

Chairman BOGGS. Do you agree or disagree with this?

Mr. WATKINS. I want to see more Canadian ownership in Canada. But I do not think the 51-percent way is the way to do it, because we all know in fact if the remaining 49 percent is held in a concentrated way that control will continue to exist with the foreign country.

Chairman BOGGS. Let me ask you a question that is relevant to us as Americans, and relevant to you as a Canadian.

What has happened to the separatist movement in Quebec?

Mr. WATKINS. The separatist movement is still very much alive in Quebec. A party advocating separatism took approximately one-quarter of the votes in the recent Quebec Provinces election. If you allow for the fact that most non-French Canadians were not willing to support the separatist position, then about one-third of the French appear to have voted for a separatist position.

I think what we are seeing in Canada is what we might hope will happen in the other parts of the world, that is, the spreading of democracy downward to lower levels.

I am not suggesting that I am in favor of the separation of Quebec from the rest of Canada, but I do think rather English Canadians and French Canadians have to learn to live together and form a common alliance and work out new federal arrangements. And I think on the whole that this kind of new decentralization will reduce the appeal of the separatist.

I would like to see the United States decentralized also.

I would like to see other nation states, to go to another point——

Chairman BOGGS. What you are saying is something that I think many people would agree to; namely, that we cannot run every program in the United States from Washington.

Mr. SERVAN-SCHREIBER. I would like to say that what has just been said is perhaps an essential problem for all of us, and a very intelligent program, that democracy should go downward. This is an answer to many problems.

Mr. WATKINS. That is why we are opposed to the multinational corporation, because democracy does not go downward.

Chairman BOGGS. Mr. Hymer, would you mind commenting upon Japanese protectionism?

Mr. HYMER. I think Senator Percy was probably right, that Japan, if it wants to continue its outward expansion, will have to make more concessions and allow the entry of corporations into Japan. Steps in this direction are already taking place. You can read of agreements being signed every day.

Chairman BOGGS. We have a very interesting observation made by one of our witnesses this week, in which he said that the very prosperity of Japan was creating such internal inflationary pressures—the workers want more pay and more television sets and more of everything—that the impact upon its export market might be such that, the internal demand could become so great that that in itself would have a great impact.

Mr. HYMER. Could I make another point.

I think one should also focus on the considerable outward expansion of Japan, around the whole rim of the Pacific, Siberia, Alaska, the west coast of Canada, and the west coast of the United States, Latin America, and the South Pacific.

Chairman BOGGS. Thank you very much. We really must conclude now.

This has indeed been a most outstanding panel. And on behalf of the committee I should like to thank all of you.

This will conclude our series on multinational corporations and related problems.

This concludes our series of hearings.

Thank you very much, gentlemen.

(Whereupon, at 12:40 p.m., the subcommittee adjourned, to reconvene subject to the call of the Chair.)

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