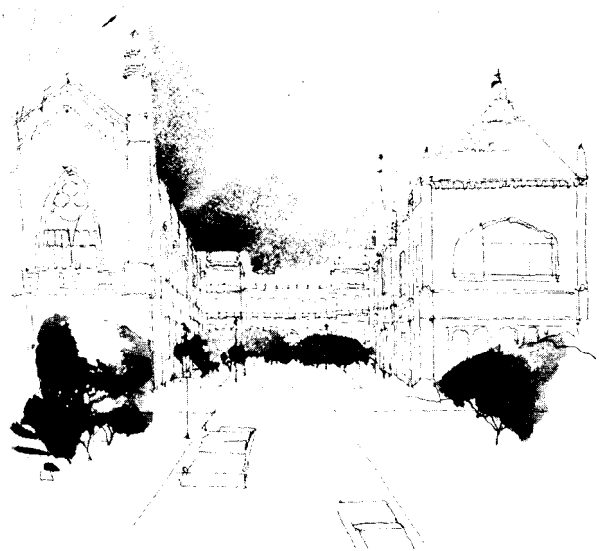


Selected Papers . No. **31**

# The American Presence in Europe

By **JACQUES DREZE**



**GRADUATE SCHOOL OF BUSINESS  
UNIVERSITY OF CHICAGO**

JACQUES DREZE *has divided his time in recent years between the United States and his native Belgium, where he is Professor of Economics and Statistics, and Research Director of the Center for Operations Research and Econometrics, at the Universite Catholique de Louvain. The Center, staffed by scientists from Western and Eastern Europe as well as the United States, ranks among the leading research units of the world in its fields. Professor Dreze did his undergraduate work at the University of Liege in Belgium and his doctoral work in the United States, primarily at Columbia. From 1952 to 1954 he was a Graduate Fellow of the Belgian American Educational Foundation, studying at Columbia and Harvard before visiting the Cowles Commission at the University of Chicago and the Survey Research Center at the University of Michigan. He was a Research Fellow at Carnegie-Mellon (1954), Research Associate at Purdue (1957), Northwestern (1962), and Wisconsin (1964), Visiting Professor at Carnegie-Mellon (1957-1958) and Northwestern (1962), and Visiting Ford Foundation Professor of Applied Mathematics at the University of Chicago's Graduate School of Business (1963-1964). From 1964 to 1968, he held a joint appointment between Chicago and Louvain, where he had been Charge de cours since 1958 and Professeur ordinaire since 1962. Professor Dreze has written and published widely in his mathematically based fields of interest, and also in education: he is co-author of **Conceptions de l'Universite**, published in Europe. In May 1968, at the Center for Continuing Education on the campus of the University of Chicago, Professor Dreze addressed a group of businessmen-members of the Council of the Graduate School of Business and the School's Associates Program-on the implications of the American business presence in Europe. This selected paper is based upon his talk.*

## The American Presence in Europe

THE TOPIC is the American presence in Europe. I think this presence is most conspicuous today in the windows of Continental bookstores, most of which have been displaying a book by M. Servan-Schreiber called *Le Defi Americain* ("The American Challenge"). There has been talk about the book in this country, also, as well as a number of book reviews, and an English translation is under way. The book apparently has sold more than half a million copies since it came out last November-and that's in the French-speaking part of Europe, which makes it one of the greatest publishing successes ever to be known there. The fact that the book has attracted such notice is perhaps more interesting than its content; there is indeed some evidence that it is being read by many people who have no direct professional interest in the matter, but who to some extent begin their response to this challenge by reading about it.

The book opens with the statement that if we look 15 years into the future the third largest industrial power in the world-after the United States and the Soviet Union-will not be Europe. It will be American industry in Europe. I don't know how qualified Servan-Schreiber is as a forecaster, but would point to the fact that the closing paragraph of his book refers to the situation in Vietnam and predicts (as of last November) that sometime during the 1968 presidential campaign someone in the United States would stand up and make a decisive move to get the war over with.

There are two types of presences in Europe that run through the pages of this book; I

think most of us in Europe, and many of you in the United States, are familiar with them. One is the presence of subsidiaries of American companies. These are either firms set up by American industry by direct investment—most-ly in some of the Common Market countries—or subsidiaries that have been acquired by purchases of stock and equity in existing companies in Europe. Servan-Schreiber observes that these firms seem to be the most dynamic element of industry in the Common Market countries. He says that they seem to be the only ones to really operate at the European level, and to take advantage of the new opportunities created by the abandonment of tariffs; and that they are really taking over. American industrialists, he says, are moving between Naples and Rotterdam with the swift maneuverability of Israeli tanks in the Sinai desert.

### *Two Gaps*

This presumes one type of presence which may be evidence of the so-called *managerial gap*: if these firms are so successful, they must have superior management. The other form of presence is not industry itself, but its products. And Servan-Schreiber notes that there are a number of products, especially the most advanced and modern, for which not even American subsidiaries have been able to set up production lines, and which must be imported from the United States. This bears the connotation of the so-called *technological gap*. I would like to comment about these two topics in succession.

As you may imagine, the writer of this book, being a Frenchman, cannot be perfectly happy with this growing presence of American subsidiaries on the Continent. His reasons for being unhappy are roughly three.

One is that with the most progressive and dynamic part of European industry under American control, producing under American patents, and operated as part of American companies, there is a substantial flow of royalties from Europe to the United States, and certain kinds of profits accruing essentially to American firms. These are the profits typically obtained through innovation. There is clearly innovation in taking advantage of the presence of freer trade in Europe and in setting up more modern types of industrial activities. And the combination of patent royalties and profits accruing to innovation means a certain drain of resources from Europe to the United States.

Second, says the author, it looks today as if Europe is becoming an economic colony of the United States.

Third, he asserts that the presence of American subsidiaries quite naturally introduces foreign practices into the European business scene. A standard joke has it that if you ask an American businessman, who has been working for one of these firms in Brussels for the past three years, what to do if you get involved in a traffic accident, he will tell you, "Call up the American embassy." And if you ask his wife how to arrange a formal dinner party she will say, "Of course, you call up the American Women's Club of Brussels."

Now that's no great problem in itself, but the attitude it illustrates will carry over into business, so that if you want to fire your sales manager you call up an American lawyer and ask him how to go about it. This may to some extent reflect ignorance of the habits and traditions of the country; yet in some cases this is clearly to the good. It is so because one of the advantages that many of us see in the opera-

tion of American firms in Europe is that such operation is a very effective way of breaking the traditions, and of breaking a number of arrangements that exist for no particularly good reason,

### *Labor Relations*

At the same time, there are cases where people do indeed suffer from this pattern; one area to which reference has been made most frequently is precisely the labor relations field. An engineer who has been working at the same firm somewhere in Europe for the past 2.5 years would never think of leaving that firm and looking for a better job elsewhere. Neither does he expect to be fired, even if the blow would be tempered by the fact that he has three years' separation pay coming. That just isn't done by Europeans; when it is occasionally done by American firms it gets publicity, and it makes some Europeans unhappy.

How should we view these matters, while trying to be objective about the balance? I feel that the presence of a number of subsidiaries of important American companies has resulted basically in a number of good things, like more jobs in those countries which have been particularly successful in attracting such firms, lower prices through more competition, and access to a wider-and in some cases, a better quality-line of products.

### *Management and Patents*

I think this been accomplished essentially because of American management and American patents in these firms. I find it only natural that there is a price paid for these things; and unless some evidence appears that the royalty level was not normal or competitive in any sense, I would find it quite natural that royalties be paid.

If profits indeed result at the high level associated with innovations, I would say that we should be smart enough (we Europeans, I mean) to realize that the large share of these profits are being realized by American firms, and to buy stock in those firms. We have the opportunity to invest in them, and if we are concerned because they are reaping profits on the Continent we can get our share that way.

There are, however, two aspects of this American presence about which we don't seem to know a great deal, and about which I think we ought to know more, and perhaps ought to try to generate somewhat more orderly conditions which also could help relieve some of the tension that is attested to by Servan-Schreiber's book. One has to do with the capital flow, the other with the scientific flow.

As has been pointed out, most of the business ventures by American firms in Europe are financed through borrowings on the Euro-dollar market, and we know pretty well from looking at the statistical record what use is made of the funds available for long-term financing on that market.

One thing we don't know very much about is where these funds come from. It's very hard to trace, statistically, the supply of long-term financing on these markets to nationals of various countries, or to managers of various institutional funds of retained earnings of business firms, or the savings of individuals, and so on. Thus, we don't really know whether this investment has been accomplished with a net increase of financial capital made available to Europe, or whether-on the contrary-it has been entirely financed out of European financial markets, with the possibility that there has been constriction of the funds available to European countries.

*Impact on Science*

There also has been much concern about the possibility that the extent to which European industry relies upon foreign patents may have discouraging effects on the level of scientific activity performed in European firms. Some feel this loss may be offset-or even transformed into a gain-by the employment of scientists in the American subsidiaries. There is still, however, the feeling that the net balance is probably negative; one clear sign is that the "brain drain" has continued into recent years.

These are, then, two areas in which you Americans and we Europeans could perhaps clean our barn on both sides of the Atlantic; if we were to do so, there would probably be less quibbling and more acceptance of the American investment in Europe.

I would hope that the United States could dispose of its balance-of-payments problem, and that in the presence of such a development we might move more clearly into a merging of the long-term financial markets across the Atlantic. I think this is really the best answer to the first type of criticism that has been voiced on the Continent. If all Europeans clearly had access to financial investments in this country as well as in Europe-if there were no restrictions to the flow of investment capital as between the United States and Europe-I think the situation would tend to be normalized in this respect: There would probably be a net inflow of investment funds into Europe to take advantage of the investment opportunities there; and at the same time there would be some reshuffling of the portfolios held by Europeans, in order to avail themselves of profits-if present-irrespective of the nationalities of the companies which operate on the European scene.

### ***For Europe To Solve***

At the same time, I think it is for Europe to solve the "brain drain" problem by initially creating conditions under which the best European scientists will find it equally attractive to work in Europe as in other countries. I think if that problem were under control, then clearly a substantial flow of scientific activity would be stimulated in Europe. Thus, if the level of scientific research performed by American subsidiaries on the Continent were as high as that performed in the United States, much of the resulting industrial research would be carried out on the Continent as well, and I am sure the concern over the American presence would be reduced.

From a discussion of the first aspect of the American presence, the so-called managerial gap, let us move on to the second, which has to do with advanced technology. A few areas are singled out by Servan-Schreiber as being critical at this time: nuclear energy and its applications, in particular in the production of electricity; space exploration; supersonic air transportation of the post-aluminum type (not the Concord, but the Boeing type); and computers. It is indeed a fact that Europe is currently buying satellites or satellite facilities from the United States, buying most of its computers here, depending in large part upon the United States for the development of nuclear energy, and failing thus far to tackle supersonic air transportation at the U.S. level of technology.

The author points out that one reason for the gap may well be that these advanced technological ventures are essentially defense-based, that much of the motivation comes from the defense area, and that, to a large extent, the investment in the development of the new products and the new technology is provided

by government contracts aiming at defense. Before I tell you what he suggests Europeans might do, I think it proper to ask why Europeans should be concerned about being in second place in this area. Why should we try to be on a par with the United States in these fields?

### *The Eastern Challenge*

The technological leadership of the United States in these areas is stimulated to a large extent by another challenge—to be ahead of the Eastern world. I'm fairly sure there would be much less rush to get to the moon if someone else wasn't trying to get there first, and if there weren't the feeling that the one who leads in that race also leads in the technology of defense. You Americans appear to me to be trying to meet a Soviet challenge in this domain. If the Common Market is to try to do this, other countries may feel that they must meet the Common Market challenge in this area, and in the resulting chain of responses there could be substantial world overinvestment in the research and development activities connected with this type of technology.

I think Europeans would do best to sit tight and say, "We are perfectly glad to buy your satellites one year after they have been developed, and spare ourselves the tremendous expenditure required to be first in this particular kind of race." What should worry me as a European is that the time would come when the United States would no longer be willing to bear alone the cost of all this very expensive development, which is going to benefit the whole Western world in any case. I should be more concerned about what we would do in that case, and how long we can really ride on your coattails, than about the kind of effort we should make to be first, or even keep in the race.

I feel somewhat differently about computers. While some of the more dramatic developments may be by-products of military-based or space-exploration types of research, there are a number of other valid and interesting applications; and the notion that the industry which does not master the computer may be working at a substantial disadvantage in the future is well-founded. We in Europe do need the best computers that are available today for the research, and for the modernization of management. And if we have to buy these computers in the United States today, I say let's buy them; but let us, at the same time, make some special effort at the software level that may in the near future reduce our reliance on the latest type of hardware.

In going other routes, in trying to ban the American computer from the European scene or in trying to prevent acquisitions or mergers that would deprive the Continental firms of their autonomy, we may be lagging much more; we should not deny ourselves the best computers available for scientific and industrial uses today.

I think you can see from my remarks thus far that I find many of the ideas of Servan-Schreiber's book stimulating and worth considering, but not in every instance convincing or conclusive. The same goes for the kind of recommendations Servan-Schreiber proposes in order to meet the so-called challenge.

### *Involving Britain*

One set of recommendations is aimed at bridging the so-called technological gap; that could best be done, he feels, by getting British industry to collaborate with Continental industry. This may mean getting the United Kingdom into the Common Market. (There is

another Frenchman with an interesting view on this problem.) It may also require modifying the Common Market structure in the direction of more federal authority and fewer veto rights; it may require a federal budget for the Common Market, probably including the U.K., which could be used to support European projects in such fields as space exploration or supersonic air transportation. Even if these projects are not based upon defense, there seems to be an implication that the need to meet the American challenge could provide the same kind of incentive for technological progress as the desire to be first in defense.

As for the managerial challenge, the recommendations are that there be a change in attitudes on the part of management, and that there be intensive educational programs. (Let me note in passing that for improvement in both the technological and managerial area Europe needs to have larger industrial units, larger firms; I do not recall a single word in the book about the monopoly power associated with this; the problem does not seem to be recognized.)

Here, then, is a book which has been read by half a million people in the French-speaking part of Europe over the past six months. Does this mean that indeed the Europeans accept the American presence as a challenge and are about to meet it? The answer is probably, "No." I think it is even less likely that Europe will react to the challenge since the book has been so widely read. Let me explain why. One reason why so many people took an interest in this issue was that it was raised at a time when the U.K. was making its second bid for entry into the Common Market. Many people on the Continent were impressed with Servan-Schreiber's argument that the U.K.'s admission was

the only chance for Europe to bridge the technological gap.

### *Not Convincing*

Now that to me is very unconvincing reasoning. The insistence on federal Common Market intervention to stimulate technological projects in Europe is certainly interesting in its own way. But granting Servan-Schreiber's assumption that this is necessary for certain types of technological ventures-is it sufficient? Is European industry ready to receive federal money and put it to really good use in this particular field? One of my colleagues at the Graduate School of Business, George Stigler, likes to quote Alfred Marshall, who wrote that, "Any government can have the works of Shakespeare printed, but no government can have them written." It is clear that any federal institution in Europe could convince industry to undertake certain contracts, but whether they would be successful in terms of developing modern technology is another matter. I am afraid that this half a million readers of the book I have been talking about have accepted what sounds like an answer, and accepted it gladly, as an excuse for the fact Europe is not in the economic and technological lead today. If this reasoning is accepted, there will be less effort made to look at the sufficient-as well as necessary-conditions, to look at the practical ways, at the lower level, at the realization level whereby the managerial gap in particular can be bridged and industrial efficiency of European firms can be raised to the American level.

I think I have been talking like a European, specifically like a Belgian. Belgium has attracted more of these American subsidiaries than most of the other countries-either per square mile, or per capita, or per dollar of national income, or per traffic hazard, or on any other basis.

Perhaps I should address myself more to this audience of Americans, who may be interested in what there is in this for the U.S. Your presence in Europe is as much a challenge for American industry as for European industry. And I am not sure that you can respond to it any more effectively than Europe is responding.

### Learning

I see this challenge to you along two lines. The first has to do with the U.S. lead in management skills and technological knowledge. You will have to export these things, both to more and more countries as they develop, and in ever greater degree as the technology of management and the technology of science and industry develop. Exporting managerial skills and technological knowledge is quite different from exporting refrigerators or things of that nature. A number of American firms have found this out, to their cost. There are certain types of activities in which the failure rate of European subsidiaries has been extremely high, including management consulting, for example. Exporting managerial talent is not the same thing as exporting products; you are sending skills to parts of the world which have different cultures, different languages, different legal and institutional arrangements. This is the first part of the challenge to Americans-to discover effective ways of moving these talents and experiences overseas and reducing the costs of their "translations" to the foreign settings.

The second part of the challenge I envision for you has to do with what you might learn abroad that you could use at home. There are things to be learned, for instance, about product design. Your subsidiaries in Europe operate

under different structures of factor prices, and this may lead to different product designs which may very well be the source of useful ideas for the home market. I would assert, for example, that our automobiles are better designed than yours. European firms have been unable to make a major dent in the American market: when they tried, Detroit responded with compacts, and killed the European effort. I suppose this would happen again, if another small European were to try to creep into this big market. But I would hope that your industrial firms could learn to pick the best of what may exist in a different country and make effective use of it at home.

Also, there are industries which have dwindled or disappeared here but which have been kept alive in Europe because of different institutional situations. As you may know, we have some good and fast passenger trains, running between the European cities, called "Trans-Europe Express Trains." Maybe someday you can copy one of these and run it between Washington and New York, for example.

There are other things to be learned in Europe. Take the field of industrial relations; maybe it is a good thing that an engineer who has worked for a firm for 25 years doesn't get fired. There may be a compromise possible between the toughness required for efficiency and the softness that makes life pleasant. If a firm knows that one does not fire an engineer after 25 years, irrespective of what happens, it has to adapt to this situation somehow and it has to be run somewhat differently.

This is just another example of things that you may learn in the process of operating businesses abroad. But as I said, I'm not particularly optimistic that you will meet that particular challenge, any more than I am optimistic about Europe meeting your challenge.

### Division of Labor

I could be more optimistic on another ground—that of having America and Europe jointly meet what I would call the Atlantic challenge. That is the challenge of organizing this huge economic area, encompassing North America and Western Europe and perhaps other parts of the world, and organizing it in a way that will respond to modern technology, so that a new division of labor can emerge of which we can all make effective use. This would imply that the nationality of business corporations would progressively disappear and that they would operate at this broad international level, as in such fields as finance and science where there are no borders today. I think this may have substantial benefits to all of us that go beyond the immediate benefits of a better division of labor. You may, for instance, find in this Atlantic economy an answer to the problem of monopoly power which has been a source of concern over the years here. We in Europe may find there are ready-made answers to the problems of markets and returns to scale which have prevented us from being effective in certain lines of activity.

Thus, even if we don't meet the American challenge, and you don't meet the European challenge, we might try, together to meet the Atlantic challenge. I think if this gets done, however, you will have to accept the fact that your public relations and the American image in Europe and elsewhere will not improve substantially. I would like by way of conclusion to tell you why I think so, and also why it shouldn't worry you. A professor at The University of Chicago, a close friend of mine, who had just spent most of the year in Louvain, remarked after the June 1967 Israeli-Arab

War: "We have to hand it to you. You have a great man in Europe, General DeGaulle. See how clever he is; he provides Israel with military equipment, then he goes on television and says a few words on the Arab side, and he comes out with the love of everybody. Whereas we tried to be honest with everyone, and end up with a sunken ship and both sides unhappy about what we did." So I said, "If he's such a great man, why don't you hire him for your next President?" He said, "I would certainly wish to do so if I didn't feel he's immortal." Here was an American who had been living abroad for a year and adjusting remarkably, but was still very sensitive to the public opinion and sentiment about his country, and I can understand why. But you will never really straighten that problem out, because the best of the United States is not visible abroad and is not part of your presence in Europe today. We are very pleased to import your managerial and technological skills, but that's not the best of the United States.

To someone like me who has had the privilege of spending five or six years in this country, the best of this country, I would say, is the fact that children are very nice to younger children, and communities as a whole are nice to children, and ask you to drive slowly to protect their lives-and people do this. The best of the United States is that there really is some deep-rooted democracy in this country, both at the local level where people care about the community in which they live, and at the national level where even the most difficult problems end up being resolved within the democratic process. The best of the United States is that people have such a positive attitude towards life in general; that so many people have a basic attitude of being grateful for the fact that they live in this country, instead of being

bitter about what has happened to them in their lifetimes. And that they are ready to move, and to move toward better things. One sign of this, of course, is the great regard in which education is held-not only education of the type we try to provide at Chicago, but also education of the type that millions of Americans are getting in community centers, or buying through the mail, and so on).

And it's all those things which are perhaps more visible in the small towns than in the big cities, and that are more visible in the life of the people as citizens than in the organization of the business firms-it is these that make this a great country, in the eyes of someone who has been able to observe it closely. These are not the things that you can export at this time; they are not the things that belong to your presence in a place like Europe. Hence, I think that no matter what happens, the public image of the United States abroad will always fall short of what it should be. And when you react yourself to public opinion abroad vis-a-vis the United States, you should remember that this is not an informed opinion about what the United States is, but what it looks like through the specialized products that get into this export business. For that reason, I hope that no matter how much American presence there ever will be in Europe, there also will be a discovery by Europeans of the best of the United States-and this can only happen through European presence in the United States.