Europe 1992—Fraternity Or Fortress?

The following 1989 William K. McInally Memorial Lecture was presented at the University of Michigan by Gerrit Jeelof, a champion of the movement toward European economic unity. He discusses the upcoming European integration and its implications for world trade.

Gerrit Jeelof

As very often happens in this world, a new idea, a new approach, is tried somewhere, and in the process, all kinds of side effects begin taking place elsewhere in the world. That is certainly the case with Europe 1992.

We in Europe started the movement toward 1992 and suddenly in the United States, there is talk about Fortress Europe. Moreover, we detect a certain emotional attitude towards foreign ownership. Now, obviously, these developments are related. That is why, instead of dedicating (this) lecture only to Europe 1992, I think it is worthwhile to bring some of these other elements into the picture as well because they have a strong bearing on global trade and other global issues.

With regard to the origins of Europe 1992, most of you know that in 1957 we signed the Treaty of Rome, with six members. Briefly, the main reasons were related to agriculture and steel. There was a desire to cut through agricultural arrangements and to do something about the steel and coal situation which demanded that there be some kind of supra-national policy.

Europe, of course, is enormously complex. We have 12 countries that are members of the European Common Market, we have 10 cultures, we speak nine languages, and we have no fewer that 12 different currencies. You know they story about the currencies. Suppose you go to Europe with $500 in your pocket. As you go to each country you would change the money into the currency of the country, and when you leave, you change to the next country. Finally, after not having spent a penny, you will have only $150 left. In another example, if you wanted to be a certified chartered accountant in each European country, you would have to study 50 years.

We have a dozen separate markets averaging some 25 million people each. We are separated by borders, border controls, border taxes, border subsidies, nationalistic policies, and protected industries. By the end of the 1970s, we had a pretty bad economic situation in Europe, with very high unemployment, and the Common Market was not making much progress. We were said to be suffering from "Eurosclerosis." It was a very negative attitude. Then, at the beginning of the 1980s, private enterprise took the lead and said, "We need a new initiative, we need a new way to work."

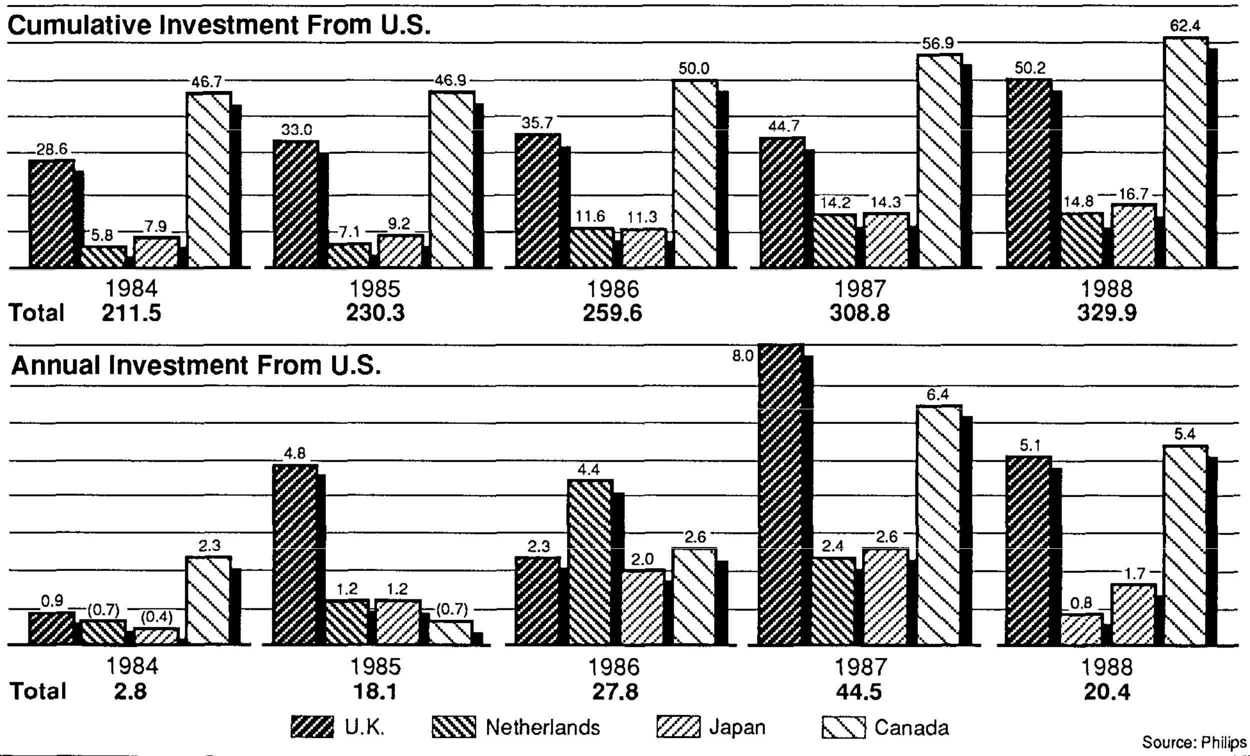
It was Dr. Dekker who said, "Look, what should we do to get Europe going, to form a really homogeneous, barrier-free market out of Europe?" And that is how it started. At that time this plan was called Europe 1990. Brussels thought it might take two more years, and that is why it became Europe 1992. The Commission in Brussels, and many of the national governments, took this as a stimulus—and they managed to excite the interest of the people in most European countries.

Why did the private sector welcome the 1992 initiative? European industry is very much in favor of this development because it is going to save us a lot of money. We have calculated that our overall costs will be reduced by about 10 percent. We have calculated the cost of non-Europe is somewhere in the area of $75 billion a year, resulting from inefficient national procurement policies, lack of competitiveness, and the like, across all Europe.

Companies already established in Europe are going to benefit significantly. Ford has announced an investment program of $17 billion for the next five years. IBM, DEC, Westinghouse, and General Motors have been there for many, many years. They were required to compete in the same way as European companies such as Philips. Also, quite a few American companies have decided now that this is becoming a less complex environment, they will set up shop and play a role in this very prosperous and steadily growing market. You may know that Philips and AT&T entered into a joint venture four or five years ago. AT&T also wants to get into Europe because the only way to do business in a major way is to be there, to play a role. So, that is what we believe is going to happen: companies will find a much more pleasant and efficient environment than before.

In the period 1975-1980, the two major foreign direct investors in the world were the U.S. and Europe. In the next five-year period, America's investments declined,

***Figure 1.* OUTWARD FOREIGN DIRECT INVESTMENT TRENDS ($ billions)**



and European investments grew. The big period of U.S. direct investment was the 1950s and the 1960s, especially in Europe, in the context of The Marshall Plan program. Enormous progress was made by the U.S. in Europe in those years. At the same time, Japan was playing only a minor role in foreign direct investment in Europe and the rest of the world, largely in underdeveloped countries. The picture that emerges is a well-developed two-way street between Europe and the U.S., a well-developed investment balance. With Japan, the balance is not there—it is a lopsided situation.

In 1988, total U.S. investment abroad was something on the order of $330 billion, while foreign investment in the U.S. was about $304 billion. Thus, although the U.S. still holds more investment outside the U.S. than foreigners have in the U.S., the gap is closing. That has to do with the weak dollar, among other things, which invites more people to invest in the U.S.

Where did these U.S. investments go? Canada, of course, is a very big resource for this country, as are the U.K., Latin America, and Holland. Investing in Japan, on the other hand, is apparently difficult, but let's not rub it in!

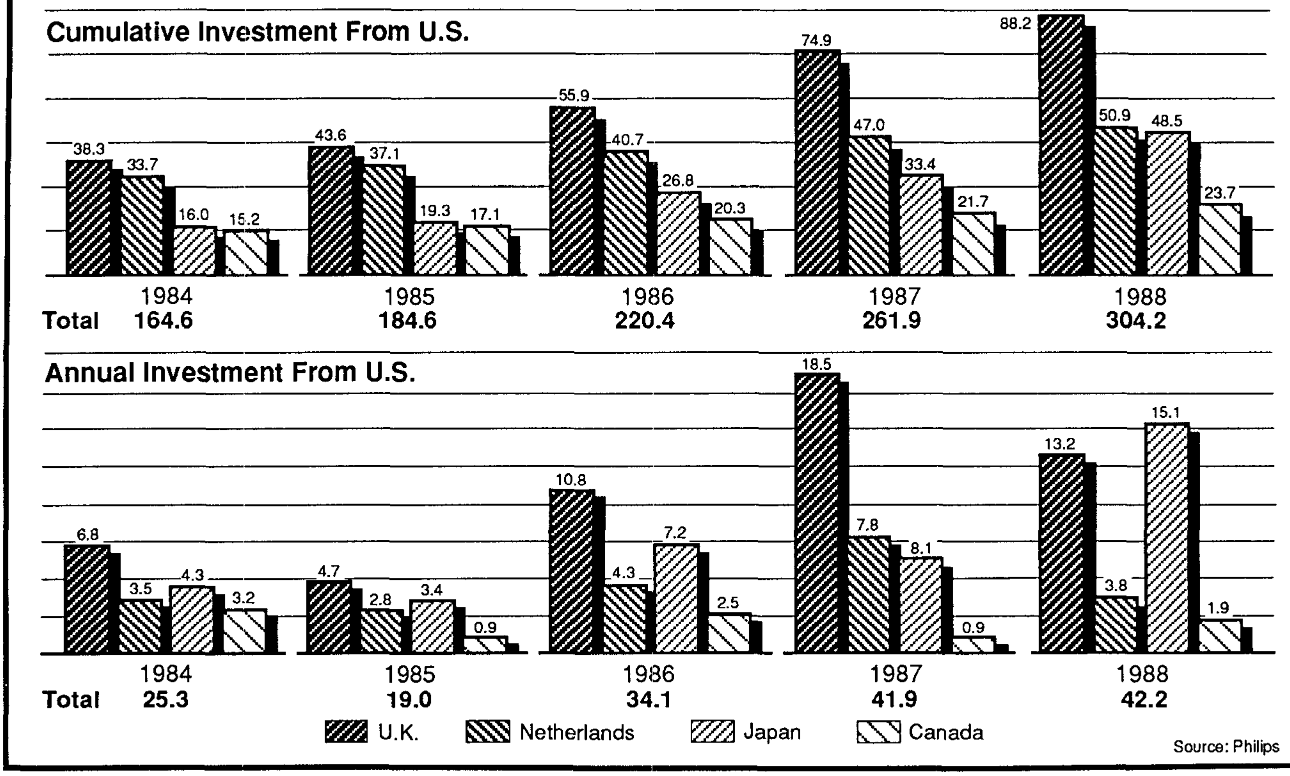
Who is investing in the United States? As on 1988, the total cumulative investment—$304 billion—the biggest is the U.K., with something like $88 billion, and number 2—surprise, surprise—is Holland, a pretty small country, yet for many reasons a country where some very big multinationals are established. Notice, however, that in 1988 the sharpest growth of foreign investment in the U.S. comes from Japan. In fact, Japan's direct investments in the U.S. more than doubled in 1988.

What about the balance of trade? Japan has an enormous surplus, while the U.S. has an enormous deficit. Europe has a minor surplus, but that mainly consists of a big deficit with Japan, and a surplus with the rest of the world.

Now, to come back a moment to Europe, what do we have to do to achieve all the things I have said from the beginning? It sounds easy. Should we go for a European Central Bank? That is an interesting issue. European currency? Quality? What do we do about reciprocity? What should we do about our social policy in Europe? You can imagine that in Holland, for instance, where social benefits are very good, that people are afraid that any change in the system may diminish benefits as they are today. A basic problem is what shall we do about fiscal policies? Added value tax? As it is being used all over Europe? How much of your national sovereignty are you willing to give up to accept a homogenous and united Europe? A Central Bank is the best example. If you accept a united Europe you have to give up some of your own independence.

Another interesting subject is antitrust legislation which varies from country to country. Three years ago, General Electric was not allowed to buy Plessy because of a business monopolies policy. One year later, Alcatel

***Figure 2.* INWARD FOREIGN DIRECT INVESTMENT TRENDS ($ billions)**



was allowed to buy ITT. Why? Because of the differences in policy between England and Brussels. Now an effort is being made to come to one type of legislation, one type of regulation, for these kinds of situations.

Obviously, the European Market today, taken country by country, represents enormous complexity, and, at the same time, tremendous capabilities. Also obviously, Europe has many obstacles to overcome. In the search for solutions, there is agreement in principle, but as I mentioned there are some problems that are really tricky. Of course, it can not be expected that on the first of January 1993, all that must be done will be done.

The important (aspect) is that the spirit of the whole thing—integration—will be sorted out. But the spirit is there, of course. We will be seeing a lot of political compromise, but I believe that Europe at the beginning of the 1990s will be a different place for business. There is no doubt about it.

One thing I have not mentioned is the issue of nationalism. There has always been a lot of nationalism in the policies of the European countries. Each country has its "national champions." We call them that because outside their country, they cannot compete all that well. This system of national champions, along with nationalistic protection, will have to be dismantled.

As a result of the changes now taking place in the European community, we are hearing all kinds of talk around the world. . .talk about fair trade. . .talk about protectionism. . .talk about. . .a European Fortress. And, now I detect another kind of talk—an emotional discus-

Table 1.
FOREIGN DIRECT INVESTMENT

	FDI Outflows, %	
	1975—1980	1981—1985
Japan	5	12
U.S.	42	19
Europe	45	56
ROW	8	13
	100	100
	FDI Inflows, %	
	1975—1980	**1981—1985**
Japan	0.5	0.7
U.S.	25	40
Europe	43	31
ROW	31	28
	100	100

Q&A Session Reveals Audience Concerns

Following the lecture, Jeelof lobbied questions from the audience regarding such issues as the state of European economies and industries. Here is a sample of his responses:

The Japanese, in general, are worried about Europeans bashing Japan, politically and economically. I have two questions regarding this subject–1) Does your opinion reflect the general tendency of the leaders of European economies, and 2) If so, is there any possibility that that kind of emotion may lead to a special EC policy targeted toward Japan?

The way I put some of these things may sound a bit critical, but I was only giving you the facts. Direct investments from foreign countries in Japan are very small, while direct investments of Japan in the rest of the world are growing very, very fast. That's an imbalance that Japan will not get away with. It is the responsibility of a global worldwide company, wanting to operate in a major market, to bring resources to that market. If a country only exports products in and takes away jobs, that is something it will not get away with long-term. You begin to make industrial enemies. We see it happening now. All of a sudden we see Japanese industries opening up factories in Europe, factories in the United States. Because that policy of making everything in one place and exporting it from there, when you want to be a major player, it just does not work that way. The world is not made that way . And, if you want to be a successful factor in a major market, you have to be a responsible corporate citizen.

Can you give a timetable for the development of a common European currency?

I think that is going to take quite a bit on time. There is a possibility that it may result in the devaluation of some European currencies, but for business, a stable currency is a great asset. It is a fantastic advantage.

Why do you think the expression "Fortress Europe" is widely used in the American press and in American business terminology?

We feel that the expression "Fortress Europe" describes something which is impenetrable, and that is not what the European market is all about. We are creating an environment in which everybody who wants to play a role can come in, and that is different from a fortress. That is why we are concerned about this expression "Fortress Europe" being heard in business circles and the news media. In terms of a bargaining position of the outside world, it will now be much easier to deal with a united Europe rather than deal with 12 independent countries, playing one against the other. Now, you have only one entity to deal with, and that, of course, is one of the purposes of the exercise.

We hear a lot about how the big companies will be advantaged by European integration in 1992. What about small European companies? How will they benefit from unification?

We believe that competition is very healthy. If some companies exist and continue to exist because of an artificial environment, we have always said that is wrong. I would say, in general, business in Europe will benefit, be it big or small, because Europe will be growing. The gross national product of Europe will be growing, and that is always good for business.

Aren't Spain and Portugal benefiting from the 1992 European unification process because of their labor rates?

Spain and Portugal are cheap labor markets, but when their standard of living comes up to the level of other countries, their labor rates will rise. Don't you have the same thing in the United States? We must begin to look at Europe as one country.

sion about foreign ownership. That discussion has got to stop in the U.S. We, as a global company, believe that is a dangerous development. I have shown to you that the investments of European countries in the U.S., of course, are major, but the moment you begin to discriminate against foreign-owned companies, you have created a dangerous development, because it leads to immediate retaliation, and I think that is the last thing we want. Nowadays, we have all decided that businesses are to be global, that the world is to be one big marketplace, and that we want a high degree of free trade. Then, if a company establishes itself in another country, and has a role to play, we should expect not to see discrimination. This brings me to a rather interesting and topical subject—High Definition Television (HDTV).

HDTV is the next step in the development of television, after black-and-white and color. The moment you talk about new developments, you must also discuss a world standard. The same was true for the VCR and the compact disc. Unfortunately, the U.S. did not play an important role in these developments because the consumer electronics industry in the U.S. had virtually disappeared. So, when there was a meeting in Dubrovnik, Yugoslavia about three years ago to define the new standards, the Americans thought the Japanese system was the best way to go. Fortunately for the Americans, the Europeans knew it was not the best system and not the right way to go. Then, all of a sudden, HDTV became an interesting topic. At the same time—and this is a point which we have been making for many years—consumer electronics became a very important product. If you want to be a major player in electronics, you cannot abandon consumer electronics.

Not only did the U.S. abandon the consumer electronics industry, but the very company which invented color television, RCA, gave up, as did many other companies. It has to do with short-term bottom line management. I am not trying to suggest that short-term bottom line management is always wrong, but you have to have staying power in consumer electronics so that when something new comes on the horizon, like HDTV, you are there and able to play a role.

While the U.S. was abandoning the consumer electronics industry, companies like Philips were establishing themselves here and investing for the future. As a result, today in the U.S. we have research centers, we have integrated manufacturing, and we employ more people together than the top 10 Japanese electronics companies combined. So we are playing a responsible role in the U.S. economy. And now, in spite of the fact that Philips has enormous experience in TV and HDTV, we are now hearing, "Well, the U.S. may develop something in the area, but foreign-owned companies are not allowed to participate." We believe that is wrong.

If we were a fly-by-night operation, then we would understand, but we are a responsible corporate citizen making a major contribution to the economy of this country, and we do not think this kind of discrimination should exist. Moreover—and here I come to my point of reciprocity—in Europe, IBM, AT&T, DEC are participating in programs which are subsidized by European countries, by European taxpayers. If we Europeans continue to be excluded from American programs, then, of course, you will get retaliation. For these reasons I say we should not talk about Fortresses, we should talk about fraternity, we should talk about reciprocity.

Now then you ask: 'How shall a global, international company behave?' It may interest you to know that Philips has existed nearly 100 years, we are established in 60 countries, and we have learned one thing in 100 years—if you want to play a role in a major market you have to bring something to the table.

My next point is that it is absolutely impossible to have a philosophy that says: 'I'm going to make everything in my home market, and from there, I'll export to the rest of the world.' You can do that for a certain length of time, you can do that for certain products, but if you want to be a major player, there is only one way to go—to establish yourself in the major market, and have manufacturing activities, have research activities, have resources over there, because that is the only way you can become a respected corporate citizen and that is the only way you can really do business in a profitable way; you must be part of the environment. When you see the profits being made by companies like Ford and General Motors in the European operations, you know that they have established themselves in the European operations, and have done that in a very profitable way.

In closing, I would like to say that the major industrial regions of the world—the U.S., Europe, and Japan—should have a level playing field. There should be similar opportunities for companies of one country in the other areas and vice versa. Moreover, if we are not careful in this respect, then we may indeed end up with a Fortress Europe, Fortress United States, and a Fortress Japan. And I have a plea: Let us not make this a self-fulfilling prophecy.

Gerrit Jeelof is vice chairman, N.V. Philips of The Netherlands and chairman, North American Philips Corporation. For his contributions to industry and commerce, Jeelof was made a Commander of the British Empire. He has also been honored by Italy and The Netherlands with their highest civilian honors.