Multinational enterprises

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1 Introduction

The fourth in this valuable series of S.U.E.R.F. international conferences is a particularly significant one for us, being the first one to take place in the United Kingdom and the first one to take place under a U.K. chairman. So it gave me especial pleasure when your President invited me to give the opening address. Professor Stuart Wilson is an old friend of ours in the Bank of England, and I am happy to be here to support him in this very worthwhile venture.

The Bank of England have always been in sympathy with the objectives of S.U.E.R.F. and have supported your society from the outset, indirectly and through the membership of a number of our senior executives. We feel that conferences such as this, which bring together representatives of the academic world and those involved in the day-to-day operational and decision-making aspects of the topics discussed, are particularly valuable. The development of a continuing dialogue of this kind can only be of mutual benefit and lead to greater insight into the problems and their implications on the part of all involved. I am glad to say that it is something to which we in the Bank of England have given particular attention in recent years.

The conference which opens today deals with a topic which is peculiarly appropriate for such a meeting of minds. Multinational enterprises have been the subject of a great deal of comment in recent years but much of this has been vitiated by the adoption of partisan viewpoints or hampered by incomplete data. This is particularly true of the financial aspects of the operations of such companies. The attention which this conference is to focus on these aspects is valuable in itself, and also of particular interest to central bankers. While we are naturally interested in the overall rôle of multinational enterprises in our national economies, their influences on financial flows and markets are the aspects with which we are most intimately concerned.

However, multinational enterprises do not generally form an identifiable statistical category – they certainly do not in the United Kingdom – and all of us concerned with their operations find it difficult from time to time either to substantiate or to controvert some of the rather sweeping claims and allegations made about their operations. For this reason, therefore, I welcome the addition to informed and impartial analysis which I am sure will come out of this conference. I am confident it is going to produce worthwhile results and I am only sorry that other pressing commitments make it impossible for me to participate in the remainder of your deliberations.

2 Why the growing interest?

The co-ordination of operations on an international scale, under a centralised ownership and management, is no new thing. We in the United Kingdom have experience of this field reaching back to the Hudson's Bay Company, the East

India Company, and other chartered companies of the seventeenth and eighteenth centuries. In more modern times, banks, shipping lines, and latterly oil companies have been for generations a familiar element in the international business scene. Only the last, perhaps, can be deemed to fall within the narrower definition of multinational enterprises underlying the current debate – which I take to be operations embracing manufacture or extractive industry in a number of different countries. Why, then, the growing interest and concern which has been evinced about the operations of these enterprises in recent years? How do companies of this kind, and the environments in which they operate, differ from, say, before the Second World War?

I would single out four factors which together come close to making the difference one of kind rather than degree and go some way to explain the attention which these companies are currently receiving.

First and foremost, of course, is the element of sheer size. This is the product of rapid growth combined with mergers and a high rate of investment overseas. The output of multinational companies is currently expanding at around 10% per annum – twice as fast as world G.N.P. and if anything faster than the growth of world trade. This explains why multinational companies are steadily growing more powerful relative to the smaller economies, and accounts for the frequently-heard forecast that in a decade or two, world business will be dominated by perhaps as few as 300 companies. This is a situation which needs to be taken seriously by all national authorities, and particularly by the smaller economies. Few such territories are unaffected. In recent years multinationals concerned with extractive industries have broadened their operations to take in new territories where their particular commodity has been discovered. At the same time, rising standards of education and productivity have widened the range of countries in which manufacturing corporations are able to set up centres of production.

Second has been the long campaign to liberalise capital movements during the post-war period. A key objective in the field of international finance, until quite recently, has been the dismantling of wartime and pre-war controls which interfered with the freedom of movement and choice in both current and capital transactions. The success of this policy, pursued steadily through the 'fifties and 'sixties, facilitated an unprecedented growth of world trade with concomitant benefits to developed and developing countries alike. In recent years, de-stabilising capital flows have from time to time necessitated the reintroduction of controls, normally temporary, in some countries. But it is still broadly true that the move towards greater capital freedom has been a major change in the international financial environment, and one without which the multinational corporations would not have been able to build up their present sophistication in international money management.

Third, the expansion of international business has been accompanied by the development of world-wide banking networks, on a more sophisticated level than hitherto, to ensure that financial services are available to meet the needs of the biggest international companies. Similarly, the growth

of the euro-currency markets has provided a new range of facilities for mobilising short or long-term funds, or investing them, in a form consistent with the international outlook of the multinational companies, and largely free of national restrictions. These facilities, allied to vastly improved communications networks and the development of electronic data processing, have put at the disposal of the sophisticated company treasurer new and more efficient machinery for cash transmission and the deployment of liquid assets.

Fourth, there is nowadays a growing sensitivity in most countries to social and political issues generated by the activities of multinational enterprises. This can be seen in the vigorous representations made from time to time by groups interested in environmental and ecological questions, and in the reaction of national and international trade unions to questions of labour relations and employment policy. The communist-inspired World Federation of Trade Unions is holding this week in Santiago a conference to examine ways of undermining the multinational enterprises. The International Confederation of Free Trade Unions, to which our own Trades Union Congress is affiliated, has declined to take part, but that can be attributed more to the sponsorship of the Santiago conference than to any lack of sensitivity to the underlying issues. In some countries, governments have intervened to limit the degree of foreign control of key sectors of industry or otherwise to preserve the national interest. This problem is potentially more embarrassing in the smaller territories, where it is sometimes seen as having neo-colonial overtones. Strictly speaking, the problem arises as a result of private foreign direct investment rather than from the activities of multinational companies as such; the two issues tend to become confused because of the predominance of such companies in investment in sensitive areas.

These and other factors have led many people to question whether the interests of multinational enterprises do not diverge from those of host governments, and – more importantly – whether their power is such as to represent a significant reduction in the sovereignty of the host government in the situation where such divergence occurs. Before I go on to examine and comment on some of the specific areas of concern where this divergence of interest may emerge in the financial field, I would like to make two points that arise out of the general considerations I have just outlined.

In the first place, 'bigness' is part of a modern trend towards bigger units and greater interdependence; this is evident in both the political and economic fields. This trend is a fact of life which is not going to be reversed – though it may well slow down. It behoves us therefore to attempt squarely to evaluate the benefits and disadvantages of such expansion, to see how the benefits can be maximised and the disadvantages controlled and reduced to a minimum. In the context of multinational enterprises, such evaluation includes political, economic, social and ecological elements; and trade unionists, consumers and others have a contribution to make as well as economists and public servants.

The second general point to which I would draw your

attention is the fact that the biggest companies have a reputation and a 'good name' which they need to maintain. They cannot afford to engage in confrontations with government or become involved in lengthy wrangles with government departments to the detriment of their good name as responsible organisations. Nor indeed can they flout public opinion indefinitely with impunity. This is not to say of course that saintliness will characterise their every action. It does mean, however, that they will usually be at least as scrupulous as their domestic counterparts, if not more so, in keeping their operations within the law and the bounds of defensible commercial practice.

3 Areas of concern

I turn now to the examination of some specifically financial aspects of the operation of multinational enterprises which have given rise to criticism and comment. Many will no doubt be dealt with elsewhere in more detail as the conference proceeds. My purpose now is mainly to open up these areas for discussion, and in so doing to comment on some of the misconceptions which I find on occasion confuse the debate.

Some of the these areas I must admit are not a central banker's immediate concern (except indirectly as far as they affect the balance of payments). For that reason, I will refrain from substantive comment. But I feel that at least a passing reference is called for to three topics. The first is the question of marketing arrangements, under which access to particular export markets is sometimes reserved to particular members of a multinational group, thus depriving an individual subsidiary of possible exports – to the detriment of its host country's balance of payments performance. The second is the general question of capital investment policy; whether by switching productive capacity internationally, the giant multinationals can wield undue influence through their ability to slow down or speed up investment. Both these are primarily the concern of the Department of Trade and Industry, but they raise interesting questions of the interaction of legitimate commercial judgment and the natural concern of governments for the national interest.

A third topic of this kind is the multinational groups' practice of allegedly maximising profits in lower tax areas, at the expense of profits in higher tax areas. This can be done by the adjustment of prices between members of the same group, assuming that the pattern of intra-group trade (in both goods and services) lends itself to such a practice. In some cases, however, we know that multinational groups prefer to fix prices to a large extent on an arm's-length basis *i.e.* as if between unconnected buyers and sellers. In the United Kingdom, supervision of these matters is primarily the concern of other regulatory bodies than the Bank. I therefore confine myself to commenting that they illustrate again how a principle generally accepted in domestic matters – that 'no one is obliged to so arrange his affairs as to allow the Revenue to insert the largest possible shovel into his store' – can give rise to contention when applied at the global level.

I turn now to matters of a more directly central banking interest.

I should like to start by taking up the question of the much-publicised ability of multinational groups to shift their liquid assets around in times of exchange crisis in such a way as to protect their interests – and in the process to accentuate the pressure on exchange markets. The recent dollar crises have led to renewed comment on the rôle of multinational enterprises in these recurring surges of short-term capital. A study just published by the United States Tariff Commission puts a figure of $268 billion on the liquid assets (at the end of 1971) of bodies participating in the international money markets, of which some 70% were held by United States multinational corporations and banks. No doubt today's figures would be considerably higher. Of course not all these funds are freely available for transfer – the assets of one body may be the liabilities of another; and working capital has to be retained or made good from somewhere. But $268 billion was more than twice as large as total world reserves at that time ($122 billion) and the sudden redeployment of even 1% of this total would be sufficient to cause a noticeable disturbance in the exchange markets.

The exact rôle of multinational corporations in the sterling crisis of June last year and the more recent international crisis of February/March this year has still to be evaluated. However, there is no doubt that transfers of liquid balances by multinational companies did account for an important part of the transfers which eventually led to the floating of the pound, the devaluation of the dollar, the floating of the yen, and the situation of widespread floating in which we now find ourselves. Perhaps the fact that a devaluation of the dollar against all currencies appeared imminent, and most of the biggest multinationals are United States controlled, had something to do with the size of these flows during the recent crises.

It would be wrong to assume that the international cash management policies of all multinational corporations are dominated by the search for short-term gain through currency speculation. But in situations of exchange market uncertainty, where the options appear to be all one way, normal prudence would suggest defensive policies designed to protect assets against loss. These considerations apply not to multinational corporations alone but to all companies whose trading is not wholly domestic. What distinguishes the multinational companies is their greater opportunity to switch funds from one currency to another and perhaps the greater sophistication they are able to employ in doing so.

The same features of greater opportunity and sophistication also characterise the ability of multinational companies to make use of another technique for shifting the currency composition of assets and liabilities – the practice of 'leading and lagging'. Payments or receipts for international transactions may be hurried forward or delayed in the hopes of profiting, or avoiding a loss, from a change in exchange rates. If there is substantial international trading within the group, a multinational company will have more opportunity to engage in leading and lagging than will purely national concerns dealing with foreign trading partners at arm's length.

A third way in which, it is sometimes suggested, multi-

national groups may adapt their practices in response to exchange market developments is in their policy over profit remittances. For example, they may hasten to declare and remit abnormally large dividends from subsidiaries in countries threatened with devaluation. Whatever may be the practice of individual companies, this suggestion is not in fact borne out by aggregated statistics, as analysed in Professor Lee Remmers' useful work *The Strategy of Multinational Enterprise*,[1] or by a more recent study by Mr Manser of Baring's *The Financial Role of Multinational Enterprises*.[2] In any case – as far as the United Kingdom is concerned – remittance is only allowed subject to certain limitations and after proper provision for tax has been made.

There has been a tendency to point the finger at multinational companies because they have the most obvious scope for redeployment of liquid assets and the organisation of 'leads and lags'. One of the questions which this colloquium might consider is whether the difference between multinational and domestic companies in those respects is fundamental, or simply one of degree. It would certainly be unwise for the U.K. authorities to ignore the extent to which purely domestic companies can seek the protection of those devices. In any event the problem of short-term international capital flows seems to me to raise wider questions still. They reflect a failure in international adjustment which has reached a point where the business and financial communities are no longer confident that they can afford to deny themselves the protection against loss that is available – and act accordingly. Whatever we may seek to do by direct action to moderate such flows, we should not ignore the imperative need to tackle problems of international maladjustment at the root, through timely corrective policies domestically and, where necessary, externally.

There are many interesting questions about direct action to control capital flows that could be studied. Some are philosophical, what we ought to be trying to do. How far does the national interest diverge from that of the individual company or group? How should the balance in official policy be struck, between controlling capital flows and responding to them with adjustments in other instruments of policy? But matters of principle cannot be the only guide: the practical issues are likely to be dominant. We in the United Kingdom have long had certain types of control over capital movements, while leaving many transactions relatively free. This has not prevented very large short-term capital flows. And the same applies to the experience of most other countries. Some types of external transaction are impossible to control closely without a degree of supervision that is almost unacceptable. This suggests that controls are probably not a complete answer to the problem of mobile capital flows. Nevertheless, it can be argued that a degree of control is of some assistance. The world is still groping its way towards a solution of this difficult problem. I shall therefore pass these questions to you without further comment on my part.

I turn now to a more domestic topic – the interaction of credit control and monetary policy with the operations of multinational enterprises.

As I have said before, companies of this kind are not

1 Michael Z. Brooke and H. Lee Remmers *The Strategy of Multinational Enterprise: Organisation and Finance* Longman, 1970.

2 W. A. P. Manser *The Financial Role of Multinational Enterprises* Cassell/Associated Business Programmes Ltd., 1973.

normally treated as a specific category in U.K. statistics or policy decisions; in the eyes of the exchange control, for example, companies are either resident, resident but non-resident-controlled, or non-resident. There are some limitations – not onerous – on borrowing in the United Kingdom by the middle group. In general, however, multinational companies have never been discriminated against in U.K. credit control policy and administration; except for some exchange control purposes, they are treated 'on all fours' with other British companies.

Have they – that is to say the subsidiaries in the United Kingdom of foreign multinational parent companies – succeeded however in evading the impact of restrictive policies in the past?

Various studies have demonstrated that such subsidiaries, once they are established on a firm footing, rely mainly on internally-generated cash flow and local borrowing sources, such as the banks, for the bulk of their finance; capital from elsewhere in the group is conventionally the smallest element. It will be appreciated that cash flow and local borrowing are sources of funds which are usually available to all companies equally. On the other hand, access to funds from elsewhere in the group when local borrowing becomes more difficult or expensive can put a multinational affiliate in an advantageous position.

As regards bank finance, I have no reason to believe that multinational subsidiaries have been treated in a discriminatory way at times of credit stringency. However, the standing and 'name' of the group as a whole, and the explicit or implicit guarantee of the parent company, might be said to give them a slight advantage, as compared with a domestic company of similar size and function.

Against this must be set the fact that it is difficult for such firms to raise long-term capital by public issue in the United Kingdom – as it is, for various reasons, in most domestic capital markets. On the other hand, access to the euro-bond market has been increasingly in recent years a useful source of funds for international (including U.K.-based) groups; despite the growing number of borrowers taking advantage of this market not many purely national firms are big enough.

For some years now such groups have been taking a substantial proportion of euro-bond issues (nearly 40%, for example, over the period 1964–68). These are largish sums, but still fairly modest in comparison with the total domestic credit made available in, say, North America plus the United Kingdom and Western Europe.

To sum up therefore it may be argued that multinational subsidiaries have a slight edge over similar domestic companies at times when credit is being rationed. But I have no reason to think that such companies' borrowing has operated to the detriment of U.K. monetary policy or credit control in the past (which when exercised selectively was after all usually aimed at consumption and speculation rather than industrial activity generally).

My remarks up to this point have focused – as indeed this conference as a whole is to do – on what are after all rather limited areas of a multinational group's overall activity.

One should always remember that they are in business to mine or process or manufacture something and then to sell it. They expand their operations to improve their production and marketing capacity, not to take advantage of some (perhaps short-lived) variation in tax rates or exchange arrangements. For the most part, the complexities of life which confront the multinational companies as a result of financial variations between the countries in which they operate are accepted much more as a necessary evil than as providing scope for bigger and better manipulations. No one criticises a national group of companies, which operate purely in one country, if they so arrange matters between the members of the group as to maximise profits or protect themselves against currency losses. Such self-protection is equally natural to a group that operates across frontiers. Trouble comes when such actions are seen to be at variance with national objectives; and it is then that difficult questions arise for policy.

4 Concluding remarks

The debate on whether the operations of multinational enterprises confer a net benefit overall takes a different form in relation to host countries on the one hand, and to home-based countries on the other. It is a debate that will no doubt continue for a very long time without reaching a definite conclusion. We in the United Kingdom have had long experience of both rôles. Our general view is that on both counts companies of this kind tend to be sufficiently above average in their technological know-how and managerial drive to generate economic advantages for both home and host country. Professor Dunning's recent study for The Economist Advisory Group, for example, showed that between 1957 and 1970 affiliates of United States companies accounted for one third of the increase in U.K. exports. Their net contribution to the U.K. balance of payments, on both current and capital accounts, was of the order of £600–700 million in 1970. However, there are other matters which need to be weighed in the balance; some of them we have already considered and some lie outside the terms of reference of this conference. The commercial interests of a multinational enterprise may not coincide with the national interest of a country where it operates; and further work remains to be done on how best such conflicts of interest can be reconciled, so as to preserve national objectives without necessarily killing the goose that lays the golden eggs.

I doubt myself whether international controls or legislation provide the answer, although there may be a case for a freer interchange of information between fiscal authorities and other supervising agencies in different countries. After all, subsidiaries of foreign parent companies have to comply with domestic government policy and legislation just as domestic companies do. They are therefore subject to the same curbs in fields such as company legislation, monopoly and merger policy, exchange control, and general employment and investment policy.

The enlargement of the European Community will lead over time to a measure of harmonisation in these important fields, and (more importantly) in fiscal and monetary matters also.

As this development takes place, the difficulties which at present face multinational companies operating under a variety of systems will diminish with a consequent gain in efficiency – and a reduction in the temptation to take advantage of such variations. There are already signs that U.K. industry is increasingly eager to expand its international operations through mergers across European frontiers. In the banking field, we expect to see more cross-frontier mergers in Europe to provide better and more co-ordinated facilities in step with developing industrial and commercial needs. For our part, we announced in November that a more liberal régime would apply, from the date of our joining the Community, to mergers and participations involving the 'marriage' of European banks with British banks (including merchant and overseas banks). At the same time, the 'open door policy' in relation to the establishment in London of branches and subsidiaries of reputable non-E.E.C. banks will be maintained.

The improvements in the international monetary system which are now being vigorously pursued have among their objectives the improvement of the adjustment process and the minimising of de-stabilising capital flows. The Committee of Twenty deputies have now set up a special study group to concentrate on the latter aspect of the problem. The events of recent months have lent extra urgency to this debate, and among the techniques being closely examined are the various possibilities in the field of capital controls. In this context the rôle of multinational corporations will be closely scrutinised.

Now I would like to raise our sights somewhat beyond our present difficulties, to a time when reform of the international monetary system is a reality. When the objective of finding a proper balance between stability and flexibility of adjustment is attained, the incentive, and the need, for multinational companies to engage in the operations that have been criticised in recent years may be significantly reduced. This will enable them to concentrate more exclusively on their real business, of contributing to higher standards of living not only in the host countries but also, through increases in world trade, in the developing countries. This in turn should lead to an improvement in the quality of life for all the peoples of the world.