

Drifting apart

**A study of the dis-integration
of the Euro-American economy**

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Abstract

The United States and Western European economies started dis-integrating with the 1971 unpegging of the dollar from gold and the 1973 oil crisis. This transformed the United States' leadership into hegemony resting on the dollar's naked power. While Japan moved closer to the United States because of this, Europeans reacted to this by integrating between themselves rather than with the United States.

Apart from a political and cultural dimension, the weakening of links is clearly shown by the slowly diminishing importance of reciprocal trade flows; by the stagnating importance of the operations of European and American multinationals in each others' home territories; by the chequered results of trans-Atlantic mergers; by the reduction of importance of Euro-American foreign direct investment after the end of the American boom in 2000.

Ample common ground of course still exists; Europeans and Americans, however, no longer recognise each other as brothers but rather as distant cousins.

Contents: 1. Introduction, p.3. 2. From co-operative leadership to American hegemony: Euro-American economic relations since World War II, p.4. 3. Europe and Japan: two different responses to American hegemony, p. 9. 4. The dis-integration of trade flows, p. 13. 5. The role of multinationals: an aggregate view, p.18. 6. Anecdotal evidence from the business world, p. 22. Conclusions, p.26. Notes, p.26. Bibliography p...

*I find the great thing in this world
is not so much where we stand
as in what direction we are moving.*

1. Introduction

Economic areas are usually much more than mere economic areas. Relationships between them are therefore usually not confined to economic aspects. They are part of a wider picture which includes, among others, cultural, strategic and political dimensions.

From this obvious truth, there follows that economic aspects of international relations can be studied *per se* only under the assumption that the other dimensions remain roughly constant. This has however not been the case for relations between Western Europe and the United States (*henceforth: Euro-American relations*) at least in the past two decades. In addition to that, Europe's borders keep changing over time.

Our specialist culture has hardly produced the necessary expertise to tackle this multifaceted problem and a 360 degree treatment appears to be lacking. We are therefore poorly equipped to respond to the need for analysis either of the economic consequences of structural changes in the geopolitical scene, like those induced by the dissolution of the Soviet Union, or of episodes of open political divergence, of varying intensity, as has been the case with the Kyoto treaty or the Iraqi issue.

We further find great difficulty in providing a conceptual framework to a seminal question many of us do not even like to put into words or to frame precisely: rather than integrate further within a dynamic globalisation framework, might the Western European and the United States economies in fact be dis-integrating, i.e. slowly dissolving ties that many thought would last forever?

This paper will try to grasp this nettle firmly by examining Euro-American relationships under three different angles:

- a) it will start by setting economic relationships in the broader field of political relationships between the two sides of the North Atlantic in a wide horizon stretching back to the end of World War II (par. 2 and 3);
- b) it will examine the relative importance of aggregate Euro-American trade flows from the Eighties to the present day (par. 4);
- c) it will look at direct investment in recent periods (par. 5);

d) it will finally provide a rough sketch, largely based upon anecdotal evidence, of M&As and developments by industrial sector (par. 6).

Tentative conclusions will be drawn in par. 7.

2. From co-operative leadership to American hegemony: Euro-American economic relations since World War II.

It can reasonably be argued that, up to the crisis of the Gold Exchange Standard in 1971 and the first oil crisis of 1973-75, economic relationships between the two sides of the North Atlantic were consistent with the hypothesis of the existence of a wider Euro-American geopolitical compact, whose essentials had been hammered out largely at the 1944 Bretton Woods Conference of 1944 (Skidelski 2001). This compact set out a fine balance of advantages and obligations for participants.

The United States obtained the acknowledgement by West Europeans (as well as by Japan) of a *de facto droit de seigneurage* (with a very limited autonomy for the United Kingdom). This gave them two direct and one indirect advantage. The first direct advantage consisted in putting American banks and financial institutions firmly at the centre of international monetary circuits, thus allowing them to sell financial services connected with and extract a levy on a large number of international transactions. The second, and more important, advantage was the absence of a foreign constraint in economic policy, i.e., given the world wide acceptance of the US dollar as a reserve currency, the possibility for the United States to run, at least for a limited period, whatever public and foreign deficit they thought fit while other countries were prevented from doing so.

The indirect advantage, a consequence of the lack of a foreign constraint, was the possibility for American firms to invest freely abroad and thus to buy out competitors with easily accessible dollars so that it could be said, with some exaggeration, that American multinational companies operating in Europe, and not Europe itself, represented the world's third largest economic power, after the US and the URSS,. This was "the American challenge", or, more properly *Le défi américain* (Servan Schreiber, 1967).

What did the Europeans get in return? First and foremost, US troops stationed in Europe. The American obligation to defend Western Europe, in case of war with the Soviet Union and its

allies, was tangibly substantiated by this presence, a solid guarantee of American involvement in Western European defence. Through the mechanism of NATO defence sharing, European countries left a considerable part of the joint defence burden to the American taxpayer; (this was at least partly offset by indirect benefits accruing to America in the form of jobs and profits from the world wide expansion of American multinational companies).

All this contained the further, implicit, guarantee of regular supplies and relatively stable prices of oil and other commodities for European countries.. It was thanks to these conditions that, while suffering from the effective limitation of their monetary sovereignty, Western European countries were able to shift considerable resources out of defence and run effective medium term economic policies to put their war-shattered economies back on course. This is one of the reasons that made European post-war recoveries and economic “miracles” at all possible (Deaglio 1985).

It must be stressed that Europeans were not passive recipients of American strategies. The “double key” system, devised for the use of nuclear weapons in a possible war in Europe, meant that European countries had at least the impression of being an essential part of the machinery. Perhaps, especially for the British with their “special relationship”, this was something more than an impression. On top of this, both Britain and France retained considerable influence in their respective post-colonial areas, in particular in Africa.

United States Presidents regularly consulted their European allies before taking important decisions; the posts of Secretary-General of NATO and of Director of the International Monetary Fund were traditionally filled by Europeans. Europeans, and the British in particular, thought, probably rightly, that they could effectively influence American strategy. During the Fifties and Sixties, many European statesmen would probably have agreed with Harold Macmillan’s often quoted wartime remark “We [*the British*] are Greeks in the American empire. We must run ... [*wartime Allied operations in Northern Africa*] as the Greek slaves ran the operations of the Emperor Claudius”¹.

Given this fine mechanism, it was largely felt that Western Europe and America, often collectively described as “The Free World” would slowly integrate and result in one, large North Atlantic economic system. It is important, in this respect, to remember that the NATO treaty contained clear provisions for this integration and envisaged a linkage between the economic

and geopolitical angle of Euro-American relations. Article 2 stated that “The Parties ...will encourage economic collaboration between any or all of them”. During the Fifties, collaboration within the NATO area was actually pursued with vigour in many industries but results were unimpressive; it later became largely limited to the arms industry and even here did not prove particularly successful².

Although in production terms the two sides of the alliance fell far short of economic integration, the reserve currency use of the dollar, the defence guarantee and the peaceful international flow of basic commodities were planks that held the system firmly together. Thus, while the aim of creating an integrated Euro-American economic community slowly faded and was substituted by more ambitious projects of world economic co-operation, the carefully designed and carefully balanced system of mutual advantages worked well, although with increasing strains and stresses, for nearly a quarter century.

During this long period, the dollar, the defence apparatus and the international commodity markets could be considered as a common goods of “The Free World” since they made a consistent increase in international trade possible to the benefit of all parties (although the share of individual countries in such benefit has only rarely been analysed). The United States thus exercised a *leadership function* (Kindleberger, 1976) as managers of these common goods; a more sophisticated interpretation defines the American role as *cooperative leadership* (Hirsch and Doyle, 1977) or could be described as an *économie dominante* (Perroux, 1948)³.

If we go beyond economists’ interpretations and move to historians, it is tempting to depict the Western economic and political set-up as a global empire (*empire-monde*) in the terms of Wallerstein (1974) or a global economy (*économie-monde*) after Braudel (1977). While Wallerstein stressed the political element of international integration, Braudel looked mainly at the economic element - which he considered largely prevalent in everyday life - and described an *économie-monde* as an interdependent geographic space, not necessarily extending to the whole planet, with a dominant centre, intermediate zones and peripheral areas⁴.

If we adopt this model of international economic organisation, there is no doubt that, during most of the Fifties and Sixties, “The Free World” can be depicted as an *économie-monde* with the United States cast in a central role, which included all the vital monetary policy and financial functions, while other

NATO countries eagerly played the role of intermediate zones and retained at least a semblance of power-sharing. Japan also constituted an intermediate area, although with less power-sharing, while the periphery was made up of developing countries

The system started unwinding with the Vietnam war; Vietnam placed an extra burden on US finances, encouraged European powers to change part of their reserve dollars into gold under Gold Exchange Standard rules. This made the dollar less glamorous on international markets, and the downward pressures on its fixed exchange rates increasingly difficult to resist, and contributed to President Nixon's unilateral decision to unpeg the US currency from gold on August 16th 1971 and thereby to put an abrupt end to the fixed exchange rate system.

By denying foreign central banks the option of converting reserve dollars into gold, the United States left the rest of the world with no other choice than to accept the dollar as a reserve currency or to opt altogether out of the general financial circuit: no other currency was available in the necessary amount, no other financial market offered opportunities and financial products comparable, in quality and quantity, to the United States market.

From August 16th 1971 onwards, *seigneurage* has no longer been the result of an agreement but rested on the strength of the American currency's naked power. To paraphrase Macmillan, the European "slaves" had not been consulted or involved in this operation of the American emperor. The unilateral unpegging of the dollar thus fundamentally altered not only financial but general geopolitical conditions. The post-war compact fell further apart when, because of the 1973-75 oil shock, the United States no longer proved capable of offering the rest of "The Free World" the benefit of unquestionably stable commodity prices.

Co-operative leadership turned into hegemony, with the sole, if burdensome, obligation for the hegemonic power to keep its currency sufficiently attractive, which meant that access through the dollar to the American market had to be maintained and investment possibilities improved. The end of the Vietnam war (1975) eliminated a source of weakness, the resumption of US relations with China (1976) opened up new possibilities, a slow drive towards stabilisation started with the Carter presidency (1976-1980). Time was ripe for deregulation and liberalisation of financial markets with set the pace throughout the eighties and nineties: without deregulation and liberalisation it would have been impossible to attract foreign capital to the United

States and to keep the dollar at the centre of the world financial system.

Although sudden, this shift from co-operation to hegemony was certainly not complete, which suggests precisely the idea of a drift rather than a rift: new, if watered down, forms of co-operation and consultation with allies were instituted, in particular the G-5 (1975) later expanded to include Italy and Canada (G-7, 1976) and, partially, Russia (G-8, 1997). The International Monetary Fund and the World Bank (Boughton, 2001) reinvented themselves and adapted their goals and actions to a floating rate currency world; although with increasing misgivings, the United States maintained active participation in nearly all international organisations. In the new conditions, co-operation on single items remained possible, even necessary, but implied limited and clearly defined mutual advantage on single issues rather than the identification of a general common good. With the 1985 so-called Plaza Hotel agreement, the devaluation of the dollar was handled co-operatively and efficiently. And it must be stressed that Europeans continued to be provided military defence whose economic burden shifted even more towards the United States.

As stressed above, the price the United States had to pay for its hegemony was the opening up of the American financial markets to the rest of the world. This meant the reversal of *Le défi américain*, with European (and Japanese) companies making substantial purchases both of United States European affiliates and of all sorts of US-based companies. The beginning of this trend can be symbolically set in 1978 with the acquisition of the European division of Chrysler Corporation by the French auto maker Peugeot; its end can be, symbolically and tentatively, set in 2000 with the acquisition of Chrysler Corporation by the German auto firm Daimler (see par.6).

Although the number of United States banks, industrial companies and real estate bought up by Europeans in the more than twenty years in which the system worked is quite impressive, Europeans failed to impose their business style upon the US. On the contrary, they were rather subjugated by the American management style (paramount importance of the stock exchange, public companies with powerful managers and tame shareholders, large role of investment and pension funds); Japanese business style enjoyed a brief international season (see below) but failed to make a permanent mark. According to Nye (2002), the United States thus exercised *soft power*, based not only upon financial strength and technological prowess but also

upon the efficiency and cultural attraction of its political and economic institutions.

3. Europe and Japan: two different responses to American hegemony

The establishment of United States hegemony drew two different responses from Japan and Europe. Japan sought to integrate strongly with America and therefore created the main pillar of the global system of the eighties and nineties. The *nichibei* (a Japanese term that can roughly be translated as Nipp-USA) was the dominant feature of world integration efforts during this period. US-Japanese trade was one of the fastest growing part of international trade in the long period between the first oil shock (1973) and the downfall of the Soviet Union (1992).

As expected by standard economic theory, the two countries specialised sharply as they mutually increased economic ties. The United States specialised out of a whole range of electric and electronic durable goods, from cameras to cars, leaving space to Japanese firms who either exported their wares directly from Japan or moved some of their productive capacity inside the United States. Japan was further the source of important computer components. In 1986, President Reagan tried to stop the “invasion” of Japanese microchips, supposedly dumped in the United States by Japanese companies, but he had to back down because of the misgivings of United States industries using precisely those basic products, a clear sign of integration and the United States - Japan treaty stabilising this trade was a much watered down version of the original American proposals. The Japanese, on their part stayed out of aerospace and defence as well as maintaining only a tiny presence in the drug industry, acknowledged American leadership in the financial field, and kept their trade surpluses firmly invested in the United States.

Thus both countries achieved what were to them important targets: the Japanese could enjoy rapid export-led growth which left their home market, including the politically sensitive agricultural sector and distribution system, substantially unchanged while the Americans could spend well beyond their internal resources on borrowed money which financed both the households’ spending spree, that took the economy out of the doldrums, and the investment cycle that begot the new economy. This solid association showed signs of strain only with the long Japanese recession of the nineties, the Asian crisis

of 1997-98 and the re-orienting of Japanese trade towards Asia after that crisis (see below).

The Japanese business style was closely studied by Americans (Womack, Jones and Roos 1987, to quote just one of several important studies) and “Asian values”, “just in time” production techniques and the emphasis on quality were obvious signs of the inroads made by Japanese business culture in America during the eighties. It is no chance that what is perhaps the first theoretical description of globalisation is the work of a Japanese scholar, Kenichi Ohmae working for an American consulting firm. His book on the *borderless economy* (Ohmae, 1991) appeared in English while American researchers in Harvard were refining the concept of “global industries” first presented some years earlier (Porter 1986); European business research on such matters was at the time either noticeably absent or cast in a secondary role.

While it brought Japan closer to the United States during the Seventies and Eighties, the emergence of United States hegemony drew a completely different response from Europe. European countries were faced by a stark choice: either integrate one by one, Japan-like, with the United States economy, adjusting their industrial structure to the demand, the financial pattern, the regulatory apparatus of the new global economy dominated by the United States, or try first to integrate between themselves at production and regulatory level and subsequently, if need be, negotiate jointly to achieve further integration.

The Europeans’ dilemma was heightened by the need to adopt a common currency in which to express financial transactions among themselves: under the fixed parity system, the dollar had been the obvious choice but in the new world of fluctuating currencies, lack of a common standard would create havoc with the European Economic Community’s (EEC) system of external tariffs and lead to trade distortions similar to those between Argentina and Brazil that nearly wrecked Mercosur in 2001. Thus the creation in 1979 of the European Currency Unit as a currency basket - a measure agreed upon by the French President Valéry Giscard d’Estaing and the German Federal Chancellor Helmut Schmidt against the judgement of many of their economic advisers - was much more than a mere technical decision: it was the starting point of the long march that led to the European Monetary System and later the European Monetary Union and the euro and gave substance to the attempt to reach a real European economic identity.

Those who derisively point at the European drive towards unity as merely based upon a currency might reflect that the European currency can itself be described as the product of the deeply felt European yearning for autonomy from the United States and the ultimate response to the unpegging of the United States dollar from gold. Although not anti-American, the evolution of the EEC, the Maastricht treaty of 1992, the adoption of the single market in 1993, the birth of the euro in 1999 and its effective circulation in 2002 can all be interpreted as a bid for diversity, for the creation of a European economic identity, based upon a different role of state and market and a different brand of capitalism and firm organisation.

It must also be stressed that, throughout this long period, major economic trends were pulling Europe and North America gently apart. The United States economic centre of gravity was steadily shifting westwards; the emergence of the *nichibei* - which can be interpreted as a big North Pacific industrial complex - reduced the importance of North Atlantic trade; intra-European trade was steadily growing at the expense, in relative terms, of Euro-American trade.

Italy can be taken as an example of this slow distancing: in 1951, the United States Italy's imports from the United States were larger than imports from the whole of what were to become EEC countries, in 1961 they accounted for less than 50 per cent of this total. The ratio had fallen to less than 20 per cent in 1971. In 1985, partly because of the high value of the dollar, it stood at slightly more than 12 per cent and has hovered around this figure ever since. A similar evolution took place in nearly every European country, including the United Kingdom, and it was precisely the structural weakening of trade links both with Commonwealth countries and with the United States that convinced Britain to join the EEC in 1975.

The weakening of Euro-American trade ties was hardly observable in the glittering world of the market globalisation of the nineties since trade volumes increased even as trade shares decreased. With it, however, went a deeper weakening of cultural ties and shared values. Bill Clinton was the first American president with no experience of World War II but he could still boast of having refined his education in England; George W. Bush lacked even this link with Europe, the true expression of a country where two thirds of the lawmakers have never been abroad. As Robert Kagan, one of the most articulate American critics of Europe, put it in a telling article in *The Washington Post*,

...it is not just the power gap that divides Americans and Europeans today...The European Union is a monument to Europe's rejection of the old power politics...Since World War II European society has been shaped not by the traditional exercise of power but by the unfolding of a geopolitical miracle: the German lion has lain down with the French lamb. The new Europe has succeeded not by balancing power but by transcending power...

This has put Europeans and Americans on a collision course...(and)...the irony is that this transatlantic disagreement is the fruit of successful transatlantic policies...Even today Europe's rejection of power politics ultimately depends on America's willingness to use force around the world against those who still do believe in power politics. Europe's Kantian order depends on the United States using power according to the old Hobbesian rules."

The United States and Europe disagreed openly on a wide number of subjects. In trade matters, Americans strongly supported GMOs and hormone feeding for cattle, two areas in which home industries were particularly strong, and were piqued by the European Union unconditional closing of their frontiers; they were further highly critical of "promotional" expense that some European companies were allowed to use in trying to secure contracts in emerging countries and that they branded as corruption. Europeans, on their part, favoured the maintenance of import quotas for bananas grown in their former colonies, and much resented American export subsidy schemes like the Foreign Sales Corporation, import duties on steel and tax rebates for farmers which they branded as unfair.

Differences of views had their origin in increasing differences of interest. Although not quantitatively very relevant, these disputes were characterised by viciousness and bitterness, another sign of the drift. This did not stop the United States and the European Union being in broad agreement on a number of trade subjects in international conferences like Cancun 2003, where their common stand against demands by a number of important emerging countries was one of the elements that prevented the reaching of an agreement.

On a broader range of subjects, Europeans and Americans found, often with profound dismay, that their disagreements sometimes ran deeper than immediate economic interests and ranged from the environment to the death penalty, from privacy regulations to industrial transfer prices. The *Transatlantic Trends 2003* survey, a project sponsored by three foundations with interests spanning the Atlantic⁵, had this to say about divergence at grass root level:

When asked whether Europeans and Americans have different social and cultural values, majorities on both sides of the Atlantic overwhelmingly

agreed (83 per cent of US and 79 per cent of European respondents). Each side perceives a value gap, although it is not clear what this perception is rooted in⁶.

This is the background against which must be set not only the recent political divides between Europe and America but also the wild fluctuations of the dollar/euro exchange rate, the half failure of the Doha trade conference in 2001 and the nearly complete failure of the Cancun conference in 2003. A common ground still exists, American arms do still indirectly protect Europeans in a turbulent world and when they look out of Europe, Europeans still find that no other part of the world is closer to them; but when Europeans and Americans look firmly into each others' eyes they now no longer recognise themselves as brothers but rather as distant cousins.

4. The dis-integration of trade flows

The weakening of Euro American trade ties during the seventies and eighties appears to be consistent with the above discussed unwinding of the close Euro-American relationship prevailing since the end of World War II.

This could be interpreted as the natural result of an enlarging global economy in which both sides make new friends without renouncing old bonds, both formal and informal. There is however more to it. Gordon (2003) has clearly documented the United States' shift to economic regionalism during the nineties. The NAFTA treaty, which was signed in December 1992 and took effect from January 1st 1994, is an eloquent example of this shift and the most conspicuous case of the flourishing of Regional Trade Areas (RTAs); it is interesting to notice that the World Trade Organisation, the watchdog, among other things, of global *versus* regional trade started its operations in 1995, i.e. one year later.

Figures 1 and 2 effectively document this perhaps undramatic shift but apparently fundamental shift from global to regional through an analysis of United States' foreign trade shares in 1980-2002. As shown in Figure 1, in 1980, Western Europe (31 per cent of United States exports) still enjoyed the distinction of being the United States' foremost foreign customer clearly topping what were to become NAFTA countries, i.e Canada and Mexico considered jointly (25.4 per cent). By 2002, the NAFTA countries' share had increased by roughly half, reaching 37.9 per cent. while the Europeans' share had dropped by about a quarter and stood at 22.5 per cent. Western Europe was

struggling with Asia (20.7 per cent of total United States exports) for second place.

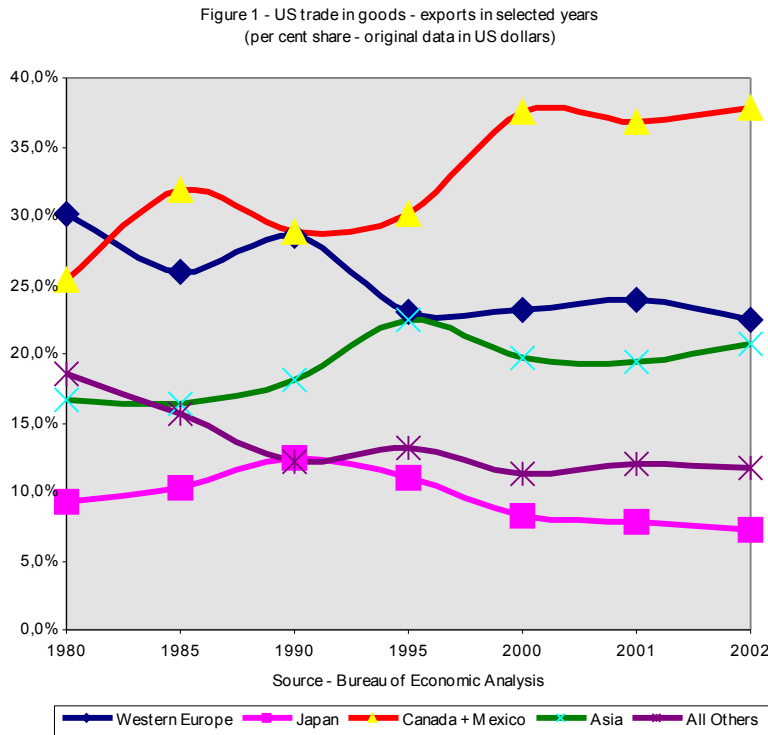
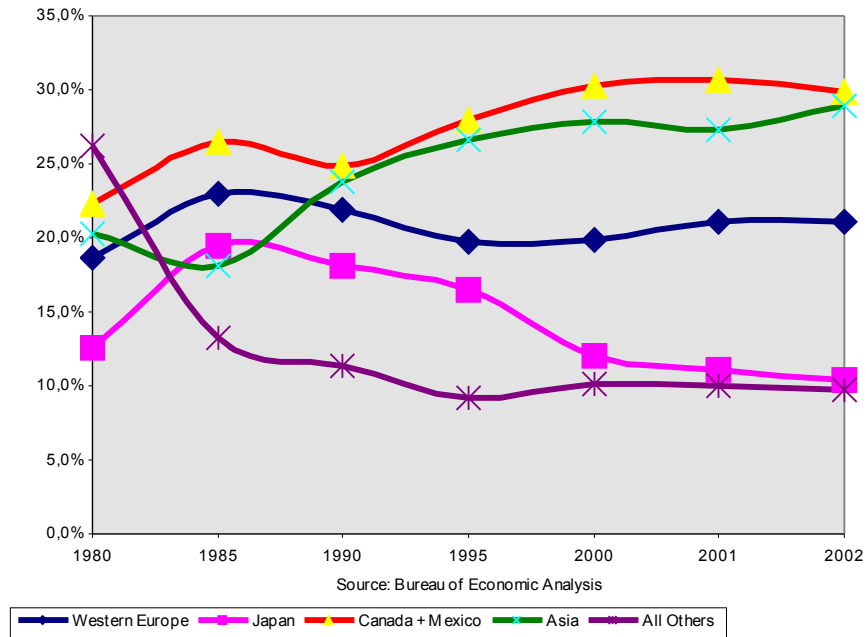


Figure 2 analyses the import side of the United States' foreign trade during the same period. This time series clearly shows the drop of the share of "other countries", which includes oil exporting countries, as a result of the collapse of oil prices during the first half of the eighties. The Western European share, however, did not benefit from this: its but remained roughly constant, hovering around 20 per cent, while Canada plus Mexico increased theirs by nearly one third, reaching 29.8 per cent. The share of Asian countries overall - excluding Japan - jumped by nearly half (from 20.3 to 28.9 per cent).

Figure 2 - US trade in goods - imports in selected years
per cent shares - original data in US dollars



It is even more significant to look at the destination of additional exports and the origin of additional imports. Of the total increase of United States exports in the boom years of 1990-2000, a mere 20.3 per cent, measured in current dollars, went to Western Europe, against 42.6 per cent to the NAFTA area and 29.3 per cent to Asia, including Japan; of the total increase in imports, the European share was almost identical (20.2 per cent) while NAFTA supplied 32.3 per cent of additional imports and Asia, including Japan, 41.5 per cent.

Together with this change in quantitative importance, a subtle change in qualitative terms is also detectable: in essential consumer goods, Europe and the United States have largely grown apart, instead of forming a unified market. After initial success, European car makers failed to establish a firm foothold in the United States market, something the Japanese managed very well. From 1992, the technical specifications of the European Single Market constituted a further hindrance to most American consumer products while creating a large unified market in most of Western Europe. Unlike Japan, Europe did not specialise with a view of supplying the United States economy. Rather, it specialised with a view of serving its own new internal market.

Table 1 provides further evidence of this shift. The first part shows the *intra-regional export share*, i.e. the ratio of exports among members of a RTA over total trade (with members and non-members) of the RTA itself. It can be seen that while the European Union has achieved a stabilisation of this share, with values around 60-65 per cent, NAFTA is far from being stabilised: the share of exports between members on their total exports, which was stagnant or dropping during the seventies, increased by one quarter during the eighties and took a further jump (between one quarter and one third) during the nineties. The slight decrease in 2001 has to be attributed to the worsening business climate.

A decade long periodisation fails to appropriately describe the importance of this shift to regionalism. In 1990-2001, 45.6 per cent of additional United States exports, measured in current dollars, went to their NAFTA partners but this average can be sharply divided into two subperiods: in 1990-1995 the share of NAFTA partners was 31.9 per cent, while in 1996-2001, i.e. in a period entirely covered by the new NAFTA agreements, the corresponding figure was 65.7 per cent. The attraction power of NAFTA was even greater on the two partners of the United States: 92 per cent of extra Mexican exports for 1990-2001 went over its Northern frontier, while approximately *all* new Canadian exports went to their Southern neighbour.

The obvious conclusion is the increasing trade insularity of North America, a result not of a blind trend but of the political will of the United States and their North American partners to seek further economic integration. New free trade agreements are being negotiated by the United States at an increasing pace: one was signed in 2002 with Chile, talks are going on for another with Central American countries. And a wider ranging agreement with South American countries is bandied about by the United States administration. Of course, given the respective size of the economies, this means that other signatories opt for integration in the United States economy which might be moving towards a new form of isolationism.

The shift of the United States towards regionalism can be considered to be the economic counterpart of the “new unilateralism” in foreign policy, a term invented by columnist Charles Krauthammer (in a Washington Post column on June 8th 2001). It might be summed up by a sentence in a private letter by the United States trade representative Robert Zoellick quoted by Gordon (2003, p. 105): “It took the completion of NAFTA and the first APEC Summit to persuade the European Union to

close the Uruguay Round”. Although presented as a strategy of trade liberalisation on multiple fronts the United States foreign trade policy appears to have lost interest in co-operation and rather believe in twisting partners’ arms and putting before them a *fait accompli*. Another *fait accompli*, the unpegging of the dollar from gold, can therefore be seen as the first of a long series of unilateral actions.

Table 1 - Direction of trade indicators in the European Union and NAFTA countries

	1970	1980	1985	1990	1995	2000	2001
<i>a) intra-regional export shares</i>							
European Union	59.5	60.8	59.2	65.9	62.4	62.1	61.2
NAFTA	36.0	33.6	43.9	41.4	46.2	55.7	54.8
<i>b) intra-regional export concentration ratios</i>							
European Union	1.5	1.6	1.6	1.5	1.6	1.7	1.6
NAFTA	1.9	2.2	2.7	2.6	2.8	2.9	2.9

Source: WTO, *World Trade Report 2003*, Tables IB.11 and 12.

The second part of Table 1 offers what is perhaps a better measure of intra-regional trade bias, i.e. *concentration ratios*. These are calculated as the ratio of a region’s intra-regional trade share to that same region’s share of world trade. This measure adjusts for the size of the RTAs and their degree of openness to the rest of the world. The idea is to see whether a given country trades more with a fellow trade block member than it does with any one country in the world (WTO, 2003, p. 56). The concentration ratio is 1 if geographical patterns of bilateral trade are proportional to the distribution of total trade. Values above 1 detect a concentration of the country’s trade within the regional group. It will be seen that, there is a fairly constant trend for the European Union and a sharp increase over time for NAFTA.

Table 2 offers further insight in the changing nature of Euro-American relations by breaking down by area the overall United States trade deficit. The United States being the greatest economic power on earth and in control of the world’s major currency, a country’s large surplus towards the United States induces this country to hold large amounts of dollars that are, sometimes willy nilly, lent back in the American financial market. By computing the United States trade deficit by area and comparing it with Us exports (Table 2), it can easily be

concluded that Euro-American trade is less unbalanced than Japanese-American trade. United States exports to Japan are almost consistently less than half United States imports from Japan (and therefore the ratios shown in Table 2 are below -100 per cent).

Table 2 - Area trade deficit as per cent of United States exports to single areas

Areas	Area trade deficit (-) or surplus (+) as % of Us area exports						
	1980	1985	1990	1995	2000	2001	2002
Western Europe	31,2%	-38,3%	1,0%	-11,5%	-36,2%	-40,6%	-60,3%
Japan	-50,3%	-196,4%	-88,3%	-94,1%	-130,8%	-126,4%	-144,5%
Canada + Mexico	2,0%	-29,8%	-10,9%	-20,8%	-27,7%	-32,7%	-34,5%
Asia	-35,2%	-73,0%	-68,7%	-54,5%	-123,9%	-123,8%	-139,2%
All Others	-57,9%	-32,5%	-19,8%	9,9%	-41,0%	-31,2%	-41,9%
Total	-11,4%	-56,6%	-28,7%	-30,3%	-58,6%	-59,4%	-70,8%

The United States still ran a trade surplus with Europe during most of the Eighties but then the situation deteriorated; in 2002, their deficit was equivalent to slightly over 60 per cent of their exports a level reached by Japan in the early Eighties. The integration of the Japanese economy with the United States economy is documented by the fact that, by 2002, for every dollar spent in the purchase of US goods, Japan received 2.4 dollars in payment for goods shipped to the United States. In relative terms, Japan's surplus was enormous and it would have been much more difficult for the Japanese than for Europeans to shift such amounts of money out of dollar investment, even if they wanted to, without provoking exchange rate tensions. This urge was much lower for Western Europe and it became even lower when the European financial market stretched its wings with the start of the euro.

The result was a scarcely discriminating Japanese spending spree in North America, in particular during the Eighties, with the acquisition of status symbol real estate, like the Citicorp and Exxon skyscrapers in Manhattam, heavy industrial investment, in particular by car manufacturers and a considerable wave investment in government bonds and other financial instruments. The Europeans were more cautious and more choosy, but even so could not resist the charm of what looked like a superior financial and business culture.

5. The role of multinationals: an aggregate view

The slowly emerging geopolitical drift and the more dramatically surfacing trade gap do not provide conclusive evidence of a Euro American estrangement. Both could still be bridged by multinational companies. American multinational companies could repatriate profits from their European sales and European multinationals could invest in the United States, thus offsetting the deficit;. In a globalising world, a Euro-American, possibly Mid-Atlantic business culture and business community could take shape and the old dream of a united economy could still come true.

Has this been the case so far? Have European and American companies been active in each others' markets through their own subsidiaries or joint ventures, so that the slow distancing of the two worlds detectable through international trade is in fact offset by closer financial and company relationships?

It is extremely difficult to give a rigorous answer to such a problem; in spite of attempts by UNCTAD, it is hard to measure correctly the impact of multinational companies in host economies. A very thorough study of the impact of MOFA (Majority-Owned Nonbank Foreign Affiliates of Unites States companies) conducted by the *Survey of Current Business* (Mataloni and Yorgason 2002) with its 1999 Benchmark Survey does nonetheless throw some light on this matter.

This study found that the operations of US multinational companies expanded at roughly the same pace as the world economy and that while Europe remained the major location for production abroad, the most rapid growth in the 1989-88 period was in Asia and Latin America. Increases in Europe were concentrated in the United Kingdom, reflecting mainly increased production by MOFAs in service industries and in Ireland (reflecting an increase in pharmaceutical manufacturing). Table 3 gives a picture of that.

A rough calculation, based on the weight of the European Union countries (derived from World Bank data in US \$ 1997) shows the share of MOFAs overall for the European Union to be 3.20 per cent in 1989, 3.05 per cent in 1994, 3.38 per cent in 1999. Even considering the natural inaccuracy of national accounts and the added difficulties of comparing data derived from company accounts with national aggregates, this confirms a picture of stability. If Ireland and the United Kingdom, the two major recipients of direct investment by United States

companies, are taken are taken out of the total, figures of course drop sharply but the impression of stability is confirmed.

Table 3 - Gross Product of Majority-Owned Nonbank Foreign Affiliates of United States companies as a percentage of GDP of selected host countries

	1989	1994	1999
<i>EEC countries</i>			
Ireland	12.4	12.1	16.8
United Kingdom	6.2	6.1	7.0
Belgium	5.6	5.1	5.1
Netherlands	5.8	4.4	4.5
Germany	3.0	2.7	2.9
Sweden	1.2	1.3	2.6
France	2.3	2.4	2.6
Portugal	1.9	2.5	2.2
Italy	1.9	1.8	2.0
Spain	1.9	1.7	1.8
Denmark	1.2	1.9	1.7
Austria	1.6	1.7	1.6
Finland	0.9	1.2	1.5
Greece	1.0	1.4	1.8
Total EU*	3.20	3.05	3.38
Total EU, excl. UK and Ireland *	2.61	2.45	2.64

Source - Survey of Current Business - March 2002 Table 8, page 34
own calculations

This leads to two different conclusions:

- a) barring exceptions like Ireland, of little overall significance, and the United Kingdom (easily explained by historical ties) the share of MOFAs in European Union GDP, although not negligible, is not of primary importance;
- b) this presence has remained roughly constant during the Nineties.

Although more extensive observation would be needed to reach a firm conclusion, it seems highly unlikely that, in the Euro-American case, constant business ties can offset diminishing trade ties.

More confirmation of this comes from the analysis of MOFA's trade with the United States, presented in Table 4. Not only foreign trade by Europe-based MOFAs appears to be a tiny portion of the total Euro-American trade, whose order of magnitude exceeds \$ 400-500 bn range, it also appears to be relatively balanced, with imports from the United States exceeding exports to the United States by about 10 per cent. Its effect on the United States trade deficit, running in the \$300-

400bn range, not only is very small but runs in the opposite direction of what could be expected if United States multinational companies were to offset the United States trade deficit with overseas revenues.

In addition to this, foreign trade by Europe-based MOFAs is clearly dwarfed by similar trade by MOFAs based in Canada and Mexico, which confirms the insular inclination of the United States economy; no historical comparison is possible on the basis of this study, but it is reasonable to suppose that the share of MOFAs based in NAFTA countries received a boost after the NAFTA treaty was signed.

Table 4 - Foreign trade with the United States by MOFAs in 1999

a) in millions of dollars

	Exports to US			Imports from US		
	parent company	others	Total	parent company	others	Total
Europe	27.863	4.025	31.888	43.945	4.085	48.030
Canada + Mexico	90.880	12.311	103.191	78.437	22.919	101.356
Mexico	25.916	1.641	27.557	23.248	6.171	29.419
Asia & Pacific	31.341	4.519	35.860	37.816	3.826	41.642
Other	8.122	2.222	10.344	12.566	22.910	35.476
Total	158.206	23.077	181.283	169.530	33.384	202.914

b) in per cent of total

	Exports to US			Imports from US		
	parent company	others	Total	parent company	others	Total
Europe	15.4%	2.2%	17.6%	21.7%	2.0%	23.7%
Canada +Mexico	50.1%	6.8%	56.9%	38.7%	11.3%	50.0%
Asia & Pacific	17.3%	2.5%	19.8%	18.6%	1.9%	20.5%
Other	4.5%	1.2%	5.7%	6.2%	11.3%	17.5%
Total	87.3%	12.7%	100.0%	83.5%	16.5%	100.0%

Source - Survey of Current Business - March 2002

As can be derived from another study by the same official publication of the US Bureau of Economic Analysis (Borga 2003), United States direct investment position abroad grew between 1999 and 2002 by roughly \$ 300 millions on a historical-cost basis. Of these, about half went to Europe but once again this was concentrated in a few countries (the United Kingdom, Ireland and the Netherlands accounted for \$ 80 million, while the three major Euroland economies - Germany, France and Italy - accounted for a mere \$ 20 million). The general picture of a gentle drifting apart seems confirmed by these general trends.

The same study found that, in 2002, the historical-cost position of foreign direct investment in the United States decreased for

the first time since at least 1946. This decrease reflected financial restructuring and write-downs in the wake of the boom in foreign investors' acquisitions of United States companies between 1998 and 2000, reduced requirements by existing United States affiliates for financing from their foreign parents and a sharp slowdown in new investment by foreign parents; furthermore, foreign parents on average chose not to reinvest their share of earnings in their affiliates (Borga 2003, page 22). The largest decreases in this position came from Germany (-\$27 billions) as a result of negative valuation adjustments in the information sector; in contrast, the positions of France increased (+\$22.3 billions) largely as a result of acquisitions in information and in professional, technical and scientific services. Overall, the European position showed an increase of 0.9 billion dollars. Although there was no flight, this is hardly an expansionary situation.

Mention must be made, at this point of contrary opinion, tending to stress the value of proximity between the United States and European economies rather than the distancing that has occurred in recent years. This tends to come from official or quasi-official sources, ranging from informed studies to ambassadorial speeches. They tend to highlight the static picture of the sheer value of Euro-American ties rather than the trend. In an study whose title is strikingly similar to the present one - with the obvious difference of the lack of the final question mark - Rodman (1999) stresses the importance of Euro-American relationships for the stability of the whole world. One of the important features of Rodman (1999) is the year in which it was written: that even when the sun seemed to be shining with no clouds on the new economy boom, the possibility of a drift was considered so serious as to need refutation.

Moving forward a few years, when the new economy boom had evaporated and clouds were prominent on the international horizon. one of the most informed and vibrant voices is that of Haass (2002). The Director of Policy Planning at the US State Department stresses the quantitative importance of ties between Europe and America (a transatlantic trade and investment relationship which can be valued at around \$ 2000 bn) and reflects on the reinterpretation of these ties in a turbulent and changing world. The gist of his argument is that the weakening of these ties would be a sheer loss not only for Europe and America but for the equilibrium of the whole world. This conclusion is hard to dispute; in a historical perspective it is important to note that the "weakening of the ties" is treated as a possibility.

A partial rebuttal to Haass (2002) is to be found in Stephens (2002). A columnist for the London *Financial Times*, shifts the weight of the analysis from business data to broad strategy. Europe, he argues “which made peace with its own history through the institutional architecture of the European Union, wants live in a global system based on multilateralism”, In this respects he frankly refers to “consternation in Europe at Mr. Bush’s ‘axis of evil’ speech”. The primacy of politics and the issue of multilateralism vs unilateralism is clearly highlighted. In a wide ranging and well documented essay, Quinlan (2002) concludes that the Transatlantic Economy enjoys a primacy in world affairs. Again, the emphasis is on the sheer might of Euro-American ties and to past trends relatively little attention is given to present day trends. Quinlan, a Fellow of the Center for Transatlantic Relations of John Hopkins University, makes a detailed analysis of Euro-American foreign direct investment, and, precisely focusing on the present situation rather than trends⁷. The fact is, that, to quote the Oliver Wendell Holmes quotation that is used as an epigraph for this paper, *the great thing in this world is not so much where we stand as in what direction we are moving.*

6. Anecdotal evidence from the business world

A further line of observation is at multinational company level. By exploring transatlantic merger and acquisition (M&A) deals as well as company strategy it is possible to acquire a non rigorous but still very valuable “ground level” impression of what links are actually being formed. This exploration is however difficult because M&A deals are sometimes arduous to catalogue exactly, the value may vary between the time the deal is announced and the time it is actually struck; there is no easily available official record of these transaction.

It is therefore with a number of *caveats* that table 5 sums up major M&A deals (whose individual declared value exceeds \$ 10bn and therefore can be thought to have special strategic importance not only at company or sector but also at national level. The number of such deals is 14 (although it cannot be excluded that some may have been left out). Their value is \$ bn 40.5 in 1998, 83.7 in 1999, 126.3 in 2000, 36,8 in 2001. No transaction exceeding \$ 10bn is recorded after this year.

Although the amounts are considerable in themselves, they are a relatively modest part of international M&As (valued at around \$ 700bn in 1999). This is because most international M&As

tend to take place between neighbouring countries of are of a comparatively small amount. The total amount of these operations which took place over five years is moderately higher than the \$ 350bn mammoth merger between Time Warner and America on Line (January 2000). It may further be noted that 13 out of 14 such deals consist of acquisitions of American companies by European companies and that 7 out of 14 have taken place between Anglo-Saxon, i.e. British and American, firms for a total value of \$217.7 bn., equivalent to slightly more than 55 per cent of the total.

Table 5 - Major Euro-American M & A deals completed in 1998-2003

Acquiring company	Home Economy	Target company	Host economy	Year	M&A Value (\$ bn)
Vodafone Group	EU/UK	AirTouch Communications	US	1999	60.3
British Petroleum	EU/ UK	Amoco	US	1998	55.0
Deutsche Telekom	EU/D	Voicestream	US	2000	50,7
Daimler-Benz	EU/ D	Chrysler Corp.	US	1998	40.5
Vivendi	EU/F	Seagram	CAN	2000	34.0
Prudential	EU/UK	American General	US	2001	26.5
BP Amoco	EU/UK	ARCO	US	2000	27.2
Unilever	EU/UK	Bestfoods	US	2000	25.1
UBS	SW	PaineWebber Group	US	2000	16.5
Cap Gemini	EU/F	Ernst & Young Consulting	US	2000	11.8
Scottish Power	EU/UK	PacificCorp	US	1999	12.6
Aegon	EU/NL	TransAmerica Corp.	US	1999	10.8
Nestle	SW	Ralston Purina	US	2001	10.3
NTL	US	CWC	EU/UK	2000	11.0

Sources: United Nations and Centro Einaudi data bank.

CAN = Canada; D = Germany; EU= European Union; F = France; NL = Netherlands; SW = Switzerland; UK = United Kingdom; US = United States

The impression that even in M&As Euro-American move along traditional lines showing a fairly strong Anglo-Saxon link is therefore strengthened. A look at sectors further confirms this: the most important transatlantic M&As can be found in oil (BP's major acquisitions of Amoco and ARCO show that); further transatlantic aggregation has taken place the drug industry (a notable example is the merger between the US firm Pfizer and the Swedish firm Pharmacia); cosmetics, music, advertising show some sectorially important transatlantic developments. The major restructuring of really important sectors, however, appear to take place within national borders or at most within neighbouring states.

Apart from these developments, transatlantic M&A activity during the Nineties and the early year of the new century

aggregate depended resulted mainly in European acquisitions of United States firms driven by two main motives:

- a) to buy back from United States companies their European subsidiaries: this motivation was, in fact, quite strong during the late eighties when the United States went through, among other things, a banking crisis and a severe bout of stagflation but persisted somewhat in the Nineties;
- b) to ensure a foothold in the United States market on the assumption, which proved to be right, that this would combine technological excellence and high economic dynamism. European buyers came with a (probably justified) inferiority complex, to be instructed rather than rule.

Acquisition as part of a global expansionary strategy comes a poor third and many times it yielded poor results. Vivendi is a good case: in June 2000, this French utilities group which branched out into the new economy (in particular cell phones) , media and entertainment under the leadership of CEO Jean Marie Messier, announced a merger the Canadian firm Seagram, the owner of the well known Universal studios, for about \$34 billion, one of the greatest transatlantic mergers in history. The French company was aiming to make the United States its main market and to use the cell phone network as a container in which to pour the contents of the Hollywood studios, a project with more than superficial similarities to those behind the merger of United States giants AOL and Time Warner. Not unlike other new economy projects, Vivendi fell ran into hard times; barely over a year later, Mr. Messier had to resign and the company started selling subsidiaries in an attempt to stave off mounting debts. In November 2003, it sold 80 per cents of its American entertainment activities to General Electric.

The acquisition of Chrysler Corporation by the German concern Daimler-Benz AG is another example of how difficult it is for a European company to cross the Atlantic and remain in good health.

The history of major Euro-American mergers of the eighties and nineties, as well as that of Euro-American direct investment projects is fraught with failures. The cases of Vivendi, Daimlerchrysler and Walt Disney serve as an example.

7. Conclusions

None of the evidence of dis-integration in the Euro-American economy presented in this paper could, *per se*, be considered conclusive. The different viewpoints, however, converge on an inescapable conclusion.

The findings from the analysis of foreign trade clearly indicate a weakening of ties; this is not counterbalanced by findings concerning trade flows and evidence, both aggregate and anecdotal, concerning multinational companies. All this is coherent with the general interpretation outlined in paragraphs 2 and 3. The weakening of ties does not appear to be a once for all occurrence but rather a continuing process.

Further research should concentrate both on getting a better understanding of this drifting process through both qualitative and quantitative analysis and on speculating about how, if at all, it could be slowed or reversed.

The rhetoric of denial should be abandoned: rather than attempting to minimise differences between Europe and America, attention should rest on what divides rather than on what unites us. It is only by focusing upon these rather unpleasant facts of life that the estrangement process might perhaps be stopped.

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¹ These remarks, addressed to Richard Crossman, are reported in Sampson (1968), pp. 65-66

² NATO still organises a yearly Economic Colloquium.

³ François Perroux («Esquisse d'une théorie de l'économie dominante», in *Économie appliquée*, n° 2-3, 1948).

⁴ Braudel, F (1977), tr. it. *La dinamica del capitalismo*, il Mulino, Bologna 1981, pp. 89-94.

⁵ *Transatlantic Trends 2003*, sponsored by The German Marshall Fund of the United States, Compagnia di San Paolo and Fundação Luso-Americana

⁶ *Transatlantic Trends 2003*, page 4.

⁷ One of Quinlan's main arguments is that trade statistics are a poor indicator of the interdependence between the European and the United States economy. He looks at foreign affiliate sales, adds them to imports and exports respectively (i.e. he adds global affiliate sales of US companies in Europe to total US exports and total affiliate sales of European companies in the US and adds them to US imports) thus trebling the total. Perhaps a better interpretation is to consider that US affiliates in Europe and European affiliates in the US are primarily part and parcel of the US and the European economy respectively and to compute among exports only the sales to their mother country.

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