

FOREIGN DIRECT INVESTMENT CONTROLS

HEARINGS

BEFORE THE

SUBCOMMITTEE ON FOREIGN ECONOMIC POLICY

OF THE

COMMITTEE ON FOREIGN AFFAIRS

HOUSE OF REPRESENTATIVES

NINETY-FIRST CONGRESS

FIRST SESSION

ON

House Concurrent Resolutions 85 and 86

RESOLUTIONS CALLING UPON THE PRESIDENT TO
TERMINATE FOREIGN DIRECT INVESTMENT CONTROLS

MARCH 26 AND 27, APRIL 22, 23, 24, 29, AND 30,
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**STATEMENT OF DON A. ELLIS, TREASURER, TEKTRONIX, INC.,
BEAVERTON, OREG.**

Mr. ELLIS. Chairman Nix, Mr. Buchanan, I am Don Ellis, treasurer of Tektronix, Inc., a manufacturer of technical electronic measuring instruments in Beaverton, Oreg.

I am considerably dismayed to find that the 100 copies of our position that were mailed last week did not arrive and, therefore, I will make my presentation a little differently than I had intended.

I had intended to read the recommendation and merely condense the rest of the position. However, I think I had better now read the position of Tektronix. I will start with the recommendation, elaborate a little bit on that, and then read the position.

Tektronix has been doing its best to help the U.S. balance of payments. During the past 5 years it has brought more than \$125 million into the United States by increasing its investments outside the United States less than \$12 million. Exports from the United States and flow of payments into the United States by Tektronix have increased each year since 1963.

We strongly favor the Tunney resolutions calling for an end to the controls on foreign direct investments.

If elimination of controls is not outright we recommend changes that will not penalize companies who by making foreign investments, continue to expand their exports from the United States and their flow of payments into the United States.

We cannot see how an allowable increase in investments based on past years is a measure of what is advantageous for the future. We cannot see how limiting investments in the future to areas of investment in the past directs investment where it will be most productive.

Tektronix would have no foreign investment problem if there had been free trade in the past 10 years. It started to manufacture outside the United States only to keep competitive with foreign companies protected by trade barriers.

I might say the trade barriers may also include the "value added" tax that is being adopted in the common market and some other parts of Europe and is being talked about in this country because, if I understand it correctly, the value added tax applies to imports and is rebated for exports.

In addition to the free trade concept, in the past couple of years inflation has threatened our ability to compete. By this I mean the United States as well as Tektronix. If money supply feeds inflation, didn't OFDI contribute to inflation by requiring Tektronix to borrow \$2.1 million in London to add to the banks' supply of money in the United States rather than to be used to expand our U.S. business?

We did borrow \$2.1 million in London. We're paying $9\frac{1}{8}$ percent for that. We brought it into this country. It is deposited in the same bank in the United States at $6\frac{1}{4}$ percent. I feel this is not a very economic thing for us to do. In addition, since it is not adding to our business, it is adding to money supply and, we think, increasing the inflationary tendencies.

One other problem that OFDI has caused is to disrupt the smooth flow of funds into the United States within a year. Last year instead of bringing this in currently, we let it pile up outside until we found out what the requirements on us would be.

We feel this was not an advantage to the United States. Another tremendous disadvantage of the entire program is that it complicates the planning of companies with international operations. It takes a lot of time. Last year I probably spent 15 percent of my time merely trying to understand the program and to comply with it, and I have several of my associates also wasting time on this instead of on being productive in the business.

Every indication is that the import deposit required by the United Kingdom for us to export to the United Kingdom, it is a deposit that is just sitting there idle from our viewpoint, exceeds the entire Tektronix allowable investment outside the United States for the whole world, based on our past.

In other words the United Kingdom has added an import deposit for products brought into the United Kingdom requiring that one-half the value of that import be deposited for 6 months, and the amount that we will have on deposit in another month will be more than our entire allowable investment increase outside the United States.

I happen to be a member of the Portland Regional Export Expansion Council. That is a part of the Department of Commerce trying to promote expansion of U.S. exports. OFDI is also a part of the Department of Commerce and it does not seem to me to have the same objective as the regional export expansion council when applied to companies like Tektronix.

Tektronix is the world's largest manufacturer of cathode ray oscilloscopes. These complex electronic measuring instruments are more widely used than any other measuring instruments. They fit the category of products most suited to U.S. superiority for export. U.S. development and mass market make technological products most suited for territorial specialization.

In other words this is a kind of a product in which the United States has superiority at the present time and can export over the entire world. It has a big advantage over any other country.

Analysts estimate that Tektronix supplies between two-thirds and three-fourths of the free world market.

Therefore it is difficult if not impossible for Tektronix to closely forecast future sales, and, therefore, needs for investment in expansion. It tries to design the instruments that its customers will need, even those they don't know they will need. To maintain its share of the market, it must deploy its investments to be responsive to shifts in the market. It has, therefore, less control of its schedules than does a company with a small share of the market.

About one-third of net sales are international, almost entirely to developed countries. Flow of payments into the United States has grown consistently. I will brief a table relating to this after a few more words.

(The table referred to above follows:)

TEKTRONIX INTERNATIONAL BUSINESS AND EXPORTS

[The following table summarizes the growth of Tektronix, and the increasing importance of exports and internal sales. "Exported" includes payments received for royalties, technical service, and international office charges]

Year ended May—	Consolidated net sales	International net sales	Percent international	Exported from United States	Flow of payments into United States	Increase in investment outside United States
1960.....	44,762,255	9,685,133	21.6	9,095,662	-----	1,400,000
1961.....	50,282,197	12,209,493	24.3	12,567,509	-----	4,988,819
1962.....	60,139,148	14,260,093	23.7	14,736,676	-----	1,303,063
1963.....	70,450,810	18,255,864	25.9	12,530,139	-----	(1,319,784)
1964.....	75,502,572	22,335,008	29.6	18,684,728	17,241,335	3,400,728
1965.....	81,099,088	25,870,467	31.9	18,974,223	19,950,356	658,587
1966.....	101,759,192	30,061,655	29.5	21,660,935	22,144,887	1,921,429
1967.....	129,030,753	35,082,518	27.2	24,877,542	24,058,825	2,844,607
1968.....	133,656,005	43,487,800	32.6	27,578,941	27,718,119	3,843,314
Year ended Mar 8, 1969.....	144,061,347	48,286,056	33.5	29,741,562	31,597,776	2,489,227

¹ Estimated.

Mr. ELLIS. Although trade barriers for this type of products have been reduced somewhat over the past several years, they still exist to protect foreign competitors. To expand or maintain its share of foreign markets Tektronix has found it necessary to invest and assemble its products in countries protecting competitors. It firmly believes its exports would not have continued to expand without such investment and activity. Japan is the clearest illustration. I will talk about Japan considerably later on.

Tektronix has learned that marketing these complex instruments requiring skilled instruction and demonstration in use, application and maintenance, is far more effective than when performed by Tektronix employees who need not handle other product lines. In addition to covering the United States, Tektronix markets directly to customers through subsidiaries in six other countries. Expanding direct coverage to additional countries would increase international sales and exports.

And I will mention charts which show, I think, distinctly the advantage of Tektronix marketing directly.

We firmly believe that the only reason exports have continued to expand during these years is because we have invested outside the United States to overcome trade barriers by manufacturing.

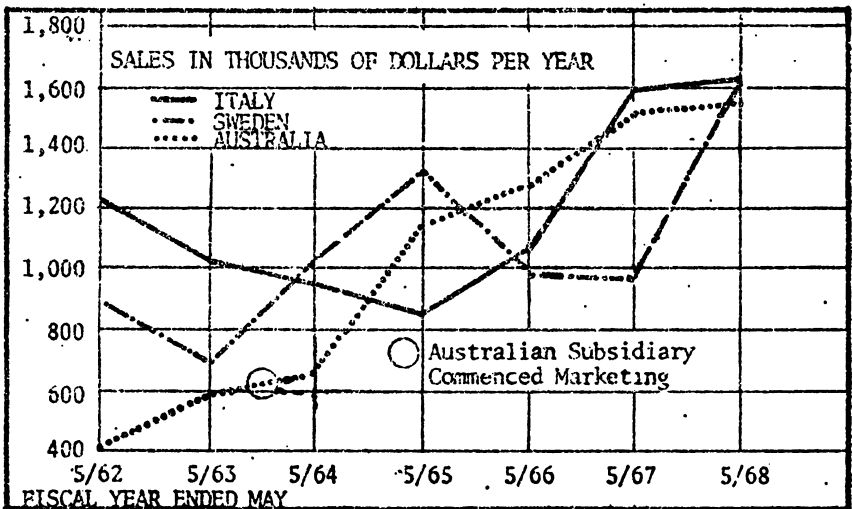
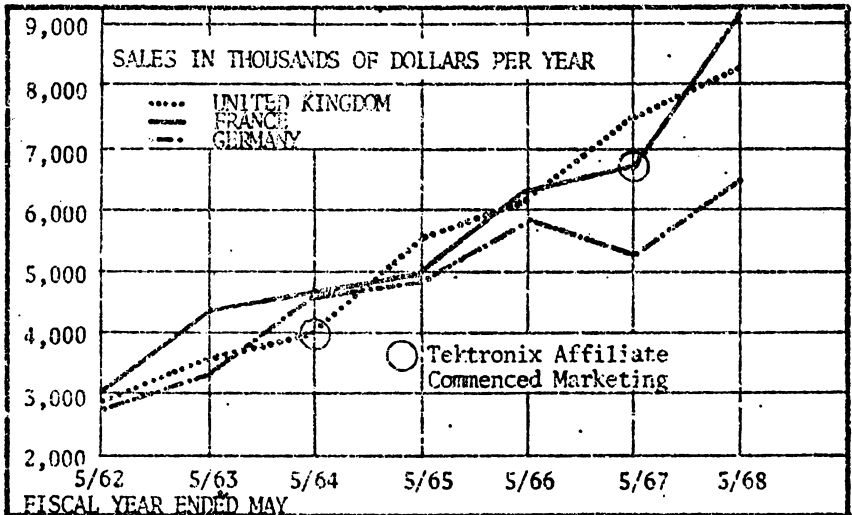
Even taking into account that 1969 investment is decreased and flow increased by \$2,100,000 enforced foreign borrowings flow ap-

proximates exports except in 1961. Therefore increasing exports has increased flow, with investment not at expense of balance of payments.

There is another chart here showing sales in three countries before and after Tektronix took over direct marketing in those and comparing them to markets of comparable size.

EFFECTIVENESS OF TEKTRONIX DIRECT MARKETING

Tektronix switched from marketing through independent distributors to direct marketing through subsidiaries in the United Kingdom, France, and Australia during the years indicated by circles on the charts below. Comparison with continued marketing by distributors in Germany, Italy, and Sweden clearly illustrates the advantage of direct marketing.



Mr. ELLIS. The first chart compares United Kingdom, France, and Germany where in 1962 and 1964 all had sales at about the same level. During 1964 we took over marketing directly in the United Kingdom and in 1967 in France. In 1968 sales in Germany were only a little over \$6 million and not appreciably greater than they were in 1966, while sales in the United Kingdom exceeded \$8 million and in France exceeded \$9 million, a substantial growth as a result of direct marketing.

We also show three other countries, Italy, Sweden, and Australia. They differ from the above charts in that they end up in 1968 with about the same amount for all three countries, something like \$6 million.

However, Australia was only \$400,000 less than one-half of Sweden and less than one-third of Italy in 1962.

We started marketing directly in Australia in 1963 or 1964, and have brought the level of sales in Australia up to the level of the other two countries.

Tektronix has always marketed directly in Canada. It started marketing directly in Switzerland about 1961 and subsequently in Australia, United Kingdom, France, and Japan, and it is confident that marketing directly in additional countries would result in increased sales. It would be regrettable from the viewpoint of both Tektronix and the United States if opportunities to do so were missed because of the program restricting direct foreign investment.

Opportunity could develop to either acquire the present foreign distributor or to replace it with a subsidiary or branch.

The importance of direct marketing cannot be overemphasized. Cathode ray oscilloscopes are extremely complex, the most widely used instruments in the technological field.

Tektronix field engineers in the United States are usually graduate electrical engineers or physicists with considerable experience when hired.

They then receive 1 year in-house training at Tektronix before they start their internship in the field. It is desirable that salesmen in foreign countries be similarly equipped.

Field engineers provide instruction and demonstration in the use, application and maintenance of cathode ray oscilloscopes. They help the customer choose the appropriate scope for his need.

They not only provide local individual instruction, but also conduct classes in several locations, as well as on the customer's premises. Well over half the field engineer's time is spent on the after sales service.

Some foreign distributors have done and are doing a good job of marketing Tektronix cathode ray oscilloscopes. In other countries the market does not seem big enough for an independent distributor to take the risk of training people to market Tektronix oscilloscopes as intensively as our own people will do. Most of them must also work with other lines of instruments and technical equipment. Our investment possibilities are described later.

MANUFACTURING TO AVOID TRADE BARRIERS

Japan provides the best illustration (below) of why Tektronix has found it necessary to assemble instruments outside the United States. Such instruments are assembled largely from components exported from the United States.

There are several reasons Tektronix has such a large share of the oscilloscope market.

The company is large enough to invest more in engineering and development than the total sales of any but one competitor. This engineering effort is based on an attitude of dedication to filling the customer's needs. The company also markets directly some 90 percent of its sales.

Assembly of the instruments has always involved the attitude of quality and reliability. But just as important a reason is that Tektronix manufactures a large portion of the components, particularly the specialized ones that are used in its instruments. Most important is the cathode ray tube. Recent trends have resulted in nearly as many production employees making components as assembling instruments. The nonproduction people working in the component-manufacturing areas are highly skilled. Each year they comprise a larger portion of our work force.

The major advantage of manufacturing our own components is control of their design. When engineers can design both components and circuits, they can tailor the characteristics to optimize performance.

Because of the efficiency of our well-trained employees and the magnitude of output warranting special tooling, costs of instruments manufactured in the United States are low. Therefore, the hope of even lower costs was not the reason for our manufacturing outside the United States. In spite of much lower pay rates, all the evidence is that costs there are not lower.

JAPAN

In Japan in the late 1950's, it is believed, more than three-quarters of the precision oscilloscopes in use had been imported from Tektronix in the United States. During calendar 1960, Tektronix exported \$¾ million to Japan of an estimated \$1 million Japanese market. Japan then instituted stronger trade barriers, including currency restrictions and import licenses. Japanese competition developed rapidly.

The early instruments made by the developing Japanese competitors were copies of Tektronix instruments, because customers insisted on them, but were not of as high quality. As these companies gained experience and skill, the oscilloscopes they made improved. At present many Japanese-manufactured oscilloscopes are not close copies of Tektronix instruments.

Tektronix exports to Japan stabilized between \$¾ million and \$1 million from 1960 through 1964. During that time we believe the Japanese market grew from \$1 million to \$5 million, dropping Tektronix share of the market from 75 to 20 percent. All the evidence is that this growth was being supplied by Japanese companies, a tremendous growth from very little to as much as \$4 million.

Figures have been announced by Japanese Government agencies clearly indicating continued rapid growth of the Japanese market for oscilloscopes. It is obvious Japan has become the second largest market for oscilloscopes in the free world. The indications are that the market grew from about \$5 million in 1964 to a little over \$7 million in 1965 to an estimated \$14 million in 1968.

To maintain or increase its share of the Japanese market, as well as to slow down the growth of the Japanese competitors and lessen their threat to other Tektronix markets, Tektronix formed a joint venture with Sony Corp. to assemble Tektronix instruments in Japan. Assembly was started in May of 1965. Sale of Sony/Tektronix-made instruments during the balance of 1965 was not very great. Thereafter, production grew effectively, to result in sales of Sony/Tektronix-assembled instruments approaching \$1 million in 1967 and \$2 million in 1968.

Until late 1967, the independent distributor in Japan performed marketing services both for instruments assembled by Sony/Tektronix and for those exported from the United States. In late 1967, after several months of preparation, Sony/Tektronix took over direct distribution of Tektronix instruments in Japan. It carries an inventory of Tektronix instruments, including demonstrator models. It now provides marketing service. It is expected to greatly increase the sales of Tektronix instruments in Japan, with the hope of regaining a larger share of the market.

By manufacturing in Japan, followed by increasing the investment and marketing directly to the users, Tektronix has increased its sales in Japan from the \$1 million level in 1964 to at least \$3.5 million in 1968, and expects further rapid increase. Exports increased during the same 4 years from \$1 million to \$2.5 million.

Since the Japanese market increased to approximately \$14 million in 1968, it can be seen that protected Japanese competitors grew strongly from less than \$1 million sales in 1961 to at least \$10 million in 1968. It has taken direct investment and struggling effort by Tektronix to increase its sales to Japanese customers from around \$1 million in 1965 (only 15 percent of the market) to \$3.5 million in 1968 (25 percent of the market). Had this not been done, it is highly unlikely exports could have been increased from 1964's \$1 million to 1968's \$2.5 million. It is highly probable exports would have declined, a loss of \$4 million exports in 4 years.

EUROPE

The picture in Japan is much more obvious, although no more real, than in Europe. For exactly the same reasons, Tektronix started manufacturing on the Isle of Guernsey, in the European free trade area, in 1959 and in The Netherlands, within the Common Market, in 1961. Instruments assembled are only those for which there is potential competition in the areas, and for which there is trade-barrier protection. It is our firm belief that this manufacturing has allowed Tektronix to maintain or increase its share of the market. Without it, we firmly believe we would not only have lost a share of market, but we may very well have failed to grow appreciably.

For 4 out of the last 6 years, the growth of sales of Tektronix has been primarily international. Only in fiscal 1966 and 1967 was U.S. growth predominant.

It may seem that manufacturing overseas replaces exports. We do not believe this is true. Not only has export of limited instruments continued to grow; most of the components assembled into instruments in the other countries are exported to them for Tektronix in the United States.

TELEQUIPMENT

In January 1967 Tektronix, Inc., through its Swiss subsidiary, Tektronix International A.G., completed arrangements to acquire Telequipment, Ltd., of London, the quality manufacturer of cathode ray oscilloscopes of a performance and price range below that of Tektronix, who concentrated in the precision market. This was done because it was realized that failure to compete in this market would allow competitors to expand into the precision market. Teleequipment products were of such quality that the company was capacity limited. Until the direct investment program intervened, it was evident that Tektronix could make facilities available for Teleequipment to expand its output at as rapid a rate as would be healthy. It is expected to expand at least 50 percent per year for several years. Its sales for 1967 were approximately \$3 million.

Teleequipment was purchased on an installment basis, the price to relate to sales. The last payment was made in March 1969.

Teleequipment obviously will need to expand its investment in inventories, customer receivables and facilities for several years. Tektronix also has a marketing company, Tektronix United Kingdom, Ltd., in London. The earnings of these two companies are expected to be sufficient to finance the expansion of both. We would like to merge them. The allowable increase in investment in that B schedule areas seems to be great enough for this purpose.

FUTURE NEEDS—MANUFACTURING INVESTMENT REQUIREMENT

In addition to the expansion of facilities needed by Tektronix mentioned above customer demands for Tektronix instruments manufactured in the Netherlands make a 30,000-square-foot addition to buildings there desirable. The Netherlands will subsidize this 25 percent and furnish 35 percent mortgage financing if Tektronix provides the other 40 percent. Such a building with furnishings is estimated at a cost of \$875,000.

This still means \$350,000 investment in the Netherlands in order to have that added capital.

The Netherlands has also been assisting Tektronix expansion there by agreeing to a special low-income tax rate during the early years. Last year the rate was less than 20 percent. This agreement has been renewed for 5 more years.

This means that when dividends are received in the United States they will be larger, and the Internal Revenue Service will collect more income tax.

Construction of a 30,000-square-foot warehouse estimated to cost \$450,000 on the Isle of Guernsey will allow space in the other buildings to improve manufacturing operations.

MARKETING FACILITIES

It has become more and more difficult to find suitable facilities available for rent for our marketing subsidiary operations. During 1968 an 11,000-square-foot building costing \$260,000 in Sydney, Australia, was completed. We see no adequate solution but to build a building in

Montreal, Canada, also. We understand this is not hampered by the restriction program.

In February 1969 our French marketing subsidiary moved into a 24,000-square-foot building it had just constructed for \$950,000 in an excellent location.

Our London marketing company outgrew the only rented space available to it. It just bought and is remodeling a 20,000-square-foot building for a total cost estimated at \$500,000.

All of these would have been easily financed from earnings. Had we not had the program, we would not have to send any money from the United States to do this.

MARKETING IN ADDITIONAL COUNTRIES

As has been mentioned it would be regrettable to miss opportunities to establish or acquire marketing subsidiaries or branches in other countries should such opportunity develop and all foreseeable such countries are in schedule C areas. Except for the restriction program funds from foreseeable earnings will be sufficient for such investment.

We have had discussions over the last year with distributors in six schedule C countries. Three of these are willing to negotiate turning the business over for Tektronix to market directly.

FINANCING

Earnings outside the United States have been growing satisfactorily. They have covered the increased investment outside the country for the past few years. They are expected to exceed needs for investment in the future, so that flow of funds into the United States would have exceeded exports even without the direct investment restriction program.

Earnings of foreign subsidiaries in each of our fiscal years ending May 1966 and May 1967 were approximately \$3 million. Earnings for the year ended May 1968 exceeded \$4.5 million, and for the year to end May 1969 are estimated to approximate \$6.5 million.

Consolidated earnings of Tektronix for each of the last 2 fiscal years have exceeded \$13 million, and are expected to grow. Some \$10 million are now invested in short-term securities in the United States in anticipation of financing the expanding investments. Consequently, the company does not need to borrow to finance its expansion for the foreseeable future.

The investment restriction program seems to require repatriating investments and earnings to such an extent that the amount left outside the country would not be sufficient to finance desirable investments. The proposal to borrow outside the country to finance these investments would be costly, because the interest rate would far exceed the rate that can be earned in this country on reinvesting these excess funds.

For a company that needs to borrow to finance its expansion, borrowing overseas instead of in the United States is not particularly onerous. But, for a company to be forced to borrow when it otherwise would not need to do so seems uneconomical, unwise and uncomfortable.

TEKTRONIX ALLOWABLE INVESTMENT INCREASE

During the base period years ended May 1966 and 1967, investment growth was primarily in schedule B countries. The potential for investment to enhance exports is mostly in schedule C countries. Basing allowed growth on the past ignores the shifts that provide opportunities in the future. Tektronix base period allowable is \$1,538,000 in schedule B countries, but only \$335,000 in schedule C where investment is needed.

Apparently the Office of Foreign Direct Investment felt Tektronix was unduly penalized by the program. In September 1968 Tektronix requested relief in the form of a \$2,100,000 increased allowable based upon increased export receivables but to substitute reducing of receivables for payment of dividends.

We happen to have a foreign personal holding company problem and we preferred not to have to pay dividends, so we questioned could we reduce our receivables instead of paying dividends.

OFDI surprised us by granting \$4,200,000 relief. One-half of this was substitution for payment of dividends bringing into this country \$2,100,000 proceeds of foreign borrowing and investing it outside the company. This would add to the inflationary potential.

We did this but are not happy with the cost. We borrowed \$2,100,000 Eurodollars from a London branch of a U.S. bank now paying interest at the rate of $9\frac{1}{8}$ percent per annum.

The proceeds were invested in a certificate of deposit with the New York branch of the same bank at $6\frac{1}{4}$ percent.

The other relief was increased allowable of \$2,100,000 in actual increase in export accounts receivable from subsidiaries.

Unfortunately, we did not expect relief in this form. We had already greatly reduced such receivables to minimize the dividend that would otherwise have to be paid. We received notice of this relief on December 26, 1968, far too late to do anything about it by December 31, 1968.

You cannot increase your receivables from subsidiaries in 5 days. Late in 1968 the United Kingdom instituted an import deposit program to inhibit imports. Importers, and we have subsidiaries in the United Kingdom which must deposit for 6 months without interest one-half the value of products imported.

Our United Kingdom subsidiary investment in this deposit is approaching \$2 million. It is not allowed to borrow this in the United Kingdom. Therefore, more than our allowable investment increase for a whole year in the whole world is now tied up idle in London.

Would the program prefer we discontinue exporting to the United Kingdom?

We're convinced Tektronix' contribution to U.S. balance of payments would have been even greater had we not had to expend so much valuable time and effort trying to understand the program, requesting relief and inefficiently arranging things to meet the requirements, then being frustrated by late relief we could not use.

I would like to reiterate then, that we strongly favor the Tunney resolutions and if they cannot be eliminated would like to see the regulations changed so that they do not penalize growth companies that

are increasing their exports and are increasing their flow into the United States.

Mr. NIX. Thank you very much, Mr. Ellis, for a most informative report.

Mr. Buchanan?

Mr. BUCHANAN. Thank you, Mr. Ellis, for this very helpful testimony; as you know the administration's position is to move toward relaxation and elimination of these controls and has taken the first step in that direction and described it as a first step, so that it is my hope that OFDI will take a hard look at your testimony and that of Mr. Simmons and other witnesses to again gain some specific ideas as to what future steps might be, providing these controls are phased out rather than eliminated in the near future.

Mr. ELLIS. Thank you.

Mr. NIX. Thank you very much.