5. OPPORTUNITIES AND RISKS

The management challenges of Europe 1992 are complex and profound, but in essence they are no different from the North American problems of globalization, increased competition and accelerating technology. Europe's euphoria may subside as the opening of long-protected markets leads to casualties. Canadians are closely monitoring the European situation but have not yet taken a leading role. The market is very pragmatic; so should the players be.

Canadian financial institutions should not neglect their role in Europe despite the pre-eminent role of the domestic market in expansion plans, and despite the opportunities currently available in the U.S. market. The EC market will likely achieve an increasingly prominent position, whereas the U.S. market remains fragmented. The EC offers a choice locale for the most up-to-date techniques, and new products are constantly entering markets there. Competition may be fierce and returns sometimes uncertain, but major institutions must maintain a significant presence there. The Chase Manhattan Bank, after selling its branch network in the Netherlands and Belgium to Crédit Lyonnais in 1987, is coming back to these countries to develop M & A. North American institutions can also gain experience in the EC with products they are not allowed to trade at home, preparing them for changes in legislation.

The Toronto Dominion Bank has taken a leading position in selling insurance products in anticipation of reformed financial regulations. Elaborated to cope with crises, these regulations have lost their significance. American brokers, accustomed to relentlessly fighting the commercial banks' encroachment on their exclusive investment banking territory, are now taking a much softer stand. The Canadian Imperial Bank of Commerce (CIBC), the Toronto Dominion Bank, and the Royal Bank are already seeking licences to deal in U.S. securities now that restrictions on commercial banks operating in the U.S. are being eased.

Economic conditions can change very rapidly. Financial institutions are familiar with the cycles that regularly affect their business. Variations in interest rates between countries are having an impact on currency rates, pushing companies to diversify internationally. For example, the earnings of the American automobile industry in Europe are a major contribution to consolidated revenues even though its production there is considerably smaller than in the U.S. Because of their European affiliates, General Motors and Ford had relatively limited drops in 1989 profits; Chrysler, with no presence in Europe, experienced a free fall in profits in 1989.

In summary, the European market unification will have far reaching effects, although these are difficult to predict. Canadian companies that start working now will be able to choose solid partners for joint ventures; attractive candidates will become increasingly elusive as more deals are sealed. Many recent joint ventures, new holding companies or partly owned subsidiaries have been set up not with cash but with an exchange of shares or transfer of assets. This strategy permits recapitalisation and also increases equity funds.

Many commentaries on Europe 1992 have focused on concerns over reciprocity. However, the grandfathering clause that will apply to Canadian financial institutions in Europe makes this concern irrelevant. The real question is the future position of North American financial institutions in Europe.

Canadian financial institutions have lost ground in the EC, despite their mastering of new financial techniques and technologies. However, a lack of distribution networks can be compensated for by Canadian expertise in direct marketing, with supports such as credit cards and mailing campaigns, which should be sufficient to increase market share.