Corporate Governance in Transition: Ten Empirical Findings on Shareholder Value and Industrial Relations in Germany

Martin Höpner

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Max-Planck-Institut für Gesellschaftsforschung
Paulstrasse 3
50676 Köln
Germany

Telephone 0221 / 2767 -0
Fax 0221 / 2767 -555
E-Mail info@mpi-fg-koeln.mpg.de
Home Page http: / / www.mpi-fg-koeln.mpg.de

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Abstract

Within the context of debates over national "varieties" of capitalism, this paper discusses the shareholder value orientation of the 40 largest listed German companies. Three dimensions of shareholder value are distinguished: the communicative dimension, the operative dimension and the dimension of managerial compensation. A shareholder value index compiling data on accounting, investor relations, variable top-management compensation and the implementation of profitability goals makes it possible to compare the shareholder orientations of the companies. The shareholder value phenomenon is explained first by the exposure to markets – the international product market, capital market pressures and the market for corporate control – and, secondly, by internal developments – changing management careers, increasing management compensation and reduced monitoring by banks and corporate networks – which cause external impulses to increase shareholder value to fall on fertile ground. Conflicts over shareholder orientation result in changing coalitions between shareholders, management, and employees. Shareholder value does not make companies opt out of central collective agreements or endanger the existence of employees' codetermination, but it does lead to more market-driven industrial relations.

Zusammenfassung

Mit Bezug auf die Debatte um Varianten des Kapitalismus wird in diesem Papier die Shareholder-Value-Orientierung der 40 größten börsennotierten deutschen Aktiengesellschaften diskutiert. Es werden drei Dimensionen kapitalmarktorientierter Unternehmensführung unterschieden: die kommunikative Dimension, die operative Dimension und die Dimension der Managervergütung. Anhand von Daten zur Bilanzierung, zu den Investor Relations, zur Anreizkompatibilität der Managervergütung und zur Implementation von Rentabilitätszielen wird ein Shareholder-Value-Index konstruiert, der einen Vergleich der Kapitalmarktorientierung der betrachteten Unternehmen erlaubt. Zur Erklärung des Shareholder-Value-Phänomen werden zwei Cluster an Erklärungen präsentiert. Erstens wird das Ausmaß an Kapitalmarktorientierung auf den Grad an internationaler Konkurrenz auf den Produktmärkten, auf die zunehmende Handlungsfähigkeit der Kapitalmarktteilnehmer und den Druck des Markts für Unternehmenskontrolle zurückgeführt. Zweitens führen interne Entwicklungen – veränderte Karrieremuster von Topmanagern, steigende Managergehälter und das abnehmende Monitoring durch Banken und Unternehmensnetzwerke – dazu, dass der externe Druck intern auf fruchtbaren Boden fällt. Hinter der Auseinandersetzung um die Shareholder-Value-Orientierung von Unternehmen verbergen sich wechselnde Koalitionen zwischen Aktionären, Managern und den Interessenvertretungen der Beschäftigten. Shareholder Value führt weder zum Ausstieg der Unternehmen aus Flächentarifverträgen, noch zu Versuchen, sich der Arbeitnehmermitbestimmung zu entledigen. Allerdings verstärkt Kapitalmarktorientierung den Trend zu zunehmend marktgetriebenen industriellen Beziehungen.

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1 Introduction[1]

This paper discusses the origins of the shareholder orientation of large German companies in the late 1990s. Why do managers implement shareholder value strategies although principal-agent theory emphasizes the different preferences of shareholders and managers? Whose side are employee representatives on? With ten empirical findings, I aim to answer these questions. Section 2 links the research question to the debate on varieties of capitalism. In Section 3, I claim that shareholder orientation is becoming more widespread. I develop a shareholder orientation index that makes the 40 largest listed companies comparable. In Section 4, three types of markets as environments of companies are discussed as predictors for the degree of shareholder orientation: product markets, capital markets and the market for corporate control. In Section 5, I discuss why pressures towards increasing shareholder orientation seem to fall on fertile ground among German managers. Section 6 deals with the role of trade unions and works councils. The different dimensions of shareholder value show different conflict lines and coalitions between shareholders, managers, and employees. While conflicts about shareholder orientation often result in conflicts over managerial control or as insider / outsider conflicts, the role of class conflict seems to be limited. Shareholder value does not jeopardize the existence of codetermination and central collective agreements, but the efficiency orientation of codetermination is on the rise. The conclusion examines the consequences for the view of institutional change found in varieties theory and discusses whether or not the current developments can be described as a convergence process.

2 Gateways of Institutional Change

This paper contributes to the debate on varieties of capitalism in which German capitalism has acquired the role of a paradigm case of a coordinated market economy with features that make it distinct from the Anglo-American model of

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1 This paper is based on a data set that was collected in the research project “The German system of industrial relations under the pressure of internationalization” headed by Wolfgang Streeck and Anke Hassel at the Max Planck Institute for the Study of Societies in Cologne. I wish to thank Jürgen Beyer, Michel Goyer, Anke Hassel, Gregory Jackson, Antje Kurdelbusch, Susanne Lütz, Britta Rehder, Fritz W. Scharpf, Wolfgang Streeck, Helmut Voelzkow and Rainer Zugehör for very helpful comments.

capitalism. Models of capitalism are seen as systems of economic and political institutions with strong interlocking complementarities that influence the behaviour of companies. Shareholder value must be interpreted as a change in one decisive element of the coordinated production system: the corporate governance arrangement, which organizes the interaction of the stakeholder groups. In upgrading the role of investors, shareholder value implies a convergence process towards Anglo-American standards in one institutional dimension of coordinated production regimes. Where does this institutional change come from? And does it affect other elements of the production system, in particular the industrial relations system? In this paper, company-based empirical investigations will be condensed into theses on these questions.

The varieties-of-capitalism approach exists in several variants (Jackson 2001c). To clarify the main arguments, I will refer to the work of David Soskice, who has developed the most influential approach on different variations of capitalism to date. The varieties approach describes production systems as configurations of institutional arrangements at the national level. One decisive assumption is that institutional arrangements in different domains of the production systems are in balanced positions to each other. David Soskice (1990, 1999a; Hall / Soskice 2001) distinguishes four interlocked spheres of production systems: the financial / corporate governance system, the industrial relations system, the education and training system, and the rules governing intercompany relationships. Similarly, Robert Boyer (2000) differentiates five spheres that organize production systems: the wage-labour nexus, the form of competition, the monetary regime, the state / society relations, and the insertion into the international regime.

According to the representatives of this approach, the coherence (Boyer) or interlocking complementarities[2] (Soskice) between the institutions are the main preconditions for economic success. Coordinated market economies are characterized by long-term, patient capital and company monitoring, centralized wage bargaining systems and cooperative industrial relations at the micro level, cooperation of firms in education / training and standardization, and the important role of business associations. By contrast, liberal market economies typically rely on short-term company financing, monitoring by capital market participants instead of insiders, decentralized wage bargaining, lack of codetermination and industry-based apprenticeship systems, strong anticollusion policies, and market-based standard setting.

The thesis of strong complementarities between those features is the crucial point of the varieties approach (Soskice 1996: 40f., 1999b: 109; Hall / Soskice 2001: 16–18; Streeck 1992b): The long-term time horizon of investment decisions in coordi-

2 See also Amable (2000).

nated market economies like Germany requires long-term company financing. This type of financing is only possible if institutions enable banks to carry out company monitoring for an indefinite period. This monitoring is supported by interlocking directorates and shares owned by banks and insurance companies. Success in diversified quality production requires the readiness of workers to invest in their skills portfolio. In return, employees receive a relatively high degree of job protection and the right to codetermine company decisions on social and personal issues. Coordinated wage bargaining hinders the headhunting of skilled workers. In this way, domains of production systems are interlocked, fit each other and are only successful in combination – in the sense that they stabilize each other and set incentives for a successful company strategy.

These assumptions have consequences for the view of institutional change. In contrast to Streeck (1997, 2001), Soskice views these production regimes as relatively stable. He is sceptical about the possibility of a coordinated market economy changing into a liberal market economy (Soskice / Hank 1996) or vice versa (Soskice 1996). In a review of Will Hutton's controversial book "The State We're In" (Hutton 1996), Soskice flatly refuses the idea of left-liberal intellectuals transforming the British economy into a stakeholder economy: The preconditions of a coordinated production system, such as long-term relations between industrial and financial companies, Soskice argues, cannot be produced by politics (Soskice 1996: 40). And, of course, supporters of the varieties approach are sceptical about the idea that one could remove one sphere of a coordinated production regime and replace it with Anglo-American style institutions. These institutions would lack stability, or the replacement would undermine the whole configuration that was responsible for the success of the economy.

It is uncontroversial that the German production regime was remarkably stable until the beginning of the 1990s. However, since the mid-1990s, the behaviour of some of the largest German companies has changed towards more Anglo-American style behaviour in shareholder orientation (Achleitner / Bassen 2000; Jackson 2001a; Jürgens / Rupp / Vitols 2000; Perlitz / Bufka / Specht 1997; Vitols 2000; Streeck 2001), a phenomenon which concerns the financing / corporate governance sphere of the production regime. Tendencies towards convergence in one sphere of a coordinated production regime constitute a test case for crucial assumptions of the varieties theory.

Does the varieties theory claim to include explanations for change? In earlier versions, Soskice's approach had features of a static theory that explains differences between countries, but not over time (Soskice 1990; Soskice / Hancké 1996). However, in the latest, and hitherto most elaborate, presentation of their approach, Peter Hall and David Soskice explicitly point out that their approach is a *dynamic* one that promises insights for developments diachronically (Hall / Soskice 2001: 47).

Although the varieties approach predicts stability rather than change, the authors do not deny the possibility of change. Because of the equilibrium in which economic governance institutions are located, the theory does not suggest changes because of internal impulses. Although one challenge for coordinated market economies could be the internationalization process, Hall / Soskice predict that the internationalization of company activities will only result in limited deregulation of coordinating institutions; their thesis is that internationalization (in this sense) will not lead to the destabilization of coordinated market economies (Hall / Soskice 2001: 51–52). However, the authors state that there is another side to the pressure of globalization: pressures associated with the internationalization of finance, both direct investments and portfolio investments. "This puts pressure on the institutions of coordinated market economy," Hall / Soskice argue. These impulses could lead to companies developing shareholder value strategies which could destabilize other spheres of continental European capitalism (Hall / Soskice 2001: 52–54).

There is no consensus among political economists on what the gateway of Anglo-American production-system elements might be in coordinated market economies. Hall / Soskice have committed themselves to financial internationalization. Sigurt Vitols (2000), for example, has interpreted shareholder value strategies[3] as responses to product market changes. Christel Lane (2000) is another expert who discusses the internationalization of production as the main challenge to the German type of capitalism. In contrast, the literature on Anglo-American funds (for example Nölting 2000) describes changes in financial patterns as driving forces behind the changes taking place in "Deutschland AG". Wolfgang Streeck (1997, 2001) has presented descriptions in which both internal developments (exhaustion of the German model, shock of unification) and the internationalization of production and financial patterns are seen as potential destabilizers.

The innovation of this paper is to break this discussion down at the company level. The research on varieties of capitalism can profit from the fact that the decisive variables differ among companies. As Hassel et al. (2001) have shown, the correlation of production-related and capital-market related indicators of internationalization is relatively weak, and both dimensions of internationalization can be clearly distinguished. The movement towards Anglo-American shareholder orientation standards affects some companies more than others (compare, for example, *Porsche* and *DaimlerChrysler*). And nearly all characteristic features of the German "model" of capitalism – bank influence, interlocking directorates, degree of codetermination, management autonomy, ownership concentration and

3 In his definition: the focus on core competencies, profitability goals, performance-oriented remuneration, international accounting standards, investment decisions according to discounted cash flow principles.

institutionalization, management compensation, ratios of equity capital, debt, management career features and so on – are not constant factors, but variables, making the comparison of companies a promising approach.

The 40 largest listed corporations in Germany from the sectors of industry, trade and commerce were chosen to form the sample upon which this study is based. These, in turn, are a subsample of the 100 largest German companies, a list of which is published by the Monopoly Commission every two years. The 40 firms in the sample are those that remain on the Monopoly Commission's 1998 list when banking and insurance firms are removed as well as firms not listed on stock exchange. The study covers the late 1990s: 1996–1999.

The main thesis of this paper is that the discussion on varieties of capitalism, especially the problem of driving forces and mechanisms behind institutional change, can profit from intercompany comparisons.

3 Comparing the Degree of Shareholder Orientation among Large German Companies

Finding 1: Since the mid-1990s, some of the largest German companies have changed their company policy towards increasing shareholder orientation.

Through the mid-1990s, the capital market played a limited role in the German "coordinated", "bank-oriented" or "insider" model – as distinct from the "shareholder" or "outsider" model of capitalism (Albert 1993; Jackson 2001c; de Jong 1997; Jürgens / Naumann / Rupp 2000; Lütz 2000; OECD 1998a; La Porta / Lopez-de-Silanes / Shleifer 1998; La Porta et al. 1998; Soskice 1999):

– Stock ownership is more concentrated than in other countries, while minority shareholders play a reduced role. A high proportion of large firms also remain unlisted private companies. In 1998, an average of only 26 percent of the shares of the 100 largest German companies was in dispersed ownership. 18 percent was family ownership, 14 percent was held by the state, 17 percent was foreign stockholding, and 14 percent of the shareholders were companies (including banks). As Figure 1 in the Appendix shows, ownership structures did not change rapidly in the last 20 years. One can observe a decline in family ownership, and unions do not play a role in company ownership any more. The positions of the other groups remain more or less stable.[4]

4 The figure shows a rise in the stock ownership of the state that can be easily misunderstood, because the *Deutsche Bundespost* changed from an authority to a company

– According to their weak position in stock ownership, the protection of minority shareholders is weak. German company law protects insiders more than outsiders. Codetermination gives employees and unions a strong position in company monitoring. Additionally, the German accounting rules of the Commercial Code, the *Handelsgesetzbuch* (HGB), result in a lack of transparency which can be described as insider-oriented, as distinguished from the outsider-oriented International Accounting Standards (IAS) or the General Accepted Accounting Principles (US-GAAP).

– Banks play an important role in the German corporate governance system. Because of their multifunctional role as creditors, shareholders, proxy voters, supervisors and investment banks, they find themselves in a powerful position. Given different preferences of shareholders and creditors, the strong role of banks also weakens the position of minority shareholders.

A recent study by McKinsey (2000) also shows that German corporate governance is further away from the shareholder-oriented ideal type of corporate governance than others. McKinsey asked 200 international institutional investors if they would pay more for the shares of a "well-governed company" than for those of a "poorly governed company" with comparable financial performance. A "well-governed company" was defined as having a majority of outside directors on the board with no management ties; holding formal evaluations of directors; being responsive to investor requests for information on governance issues; with directors holding significant stockholdings in the company; and a large proportion of directors' pay being in the form of stock options. The authors found that the actual premium investors say they would be willing to pay for a "well-governed company" differs from country to country. The companies with the largest "corporate governance discounts" were Italian companies, where investors would pay a 22 percent premium. It is interesting that both Japan and Germany share the second position (20.3 percent premium). Not surprisingly, the countries with the smallest "corporate governance discounts" were the US and the UK, beside Switzerland and Sweden.

Since the mid-1990s, the interests of minority shareholders seem to play a rising role in the company policy of several German corporations (Jürgens / Naumann / Rupp 2000; Streeck 2001; Vitols 2000). This reorientation in managerial behaviour, interpreted as steps towards shareholder value policy, concerns only some of the largest German companies (Achleitner / Bassen 2000; Bassen / Schulz 2000; Bühner / Sulzbach 2000; Coopers & Lybrand 1997; Glaum 1998; Graf / Lenke / Schießer

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and was divided into *Deutsche Post AG*, *Deutsche Telekom AG* and *Postbank AG*. Also, the *Bundesbahn* changed into a corporation (*Deutsche Bahn AG*). This privatization process implies a declining role of the state in the German economy.

1997; KPMG 2000; Pellens / Rockholtz / Stienemann 1997; Pellens / Thomaszewski / Weber 2000) – which implies that the divergence in corporate governance inside the German economy is rising. The following sections discuss several explanations of this phenomenon. The differences in the strength of shareholder orientation make the comparison of companies a promising approach. Shareholder value policy can be observed in three dimensions: investor relations / accounting, operational management, and managerial compensation. Four indicators help to estimate the degree of shareholder orientation of the 40 largest listed companies in the late 1990s:

– The first two indicators refer to the communicative side of shareholder orientation. The first one is the information quality of the annual report. Shareholder-oriented companies are supposed to publish annual reports of high quality. In the late 1990s, several companies made progress in transparency by using the International Accounting Standards or the General Accepted Accounting Principles instead of the insider-oriented accounting rules of the *Handelsgesetzbuch* (Hassel et al. 2001). Additionally, annual reports can be assessed by whether they provide segment reporting, a flow of funds analysis and information about the companies' strategy in the future. The first column in Table 1 is an analysis of the yearly German annual report competition published by Manager Magazin (standardized mean for the years 1996, 1997, 1998 and 1999) for the 40 largest listed non-financial companies (Enzweiler / Friese / Nitschke 1997, 1998; Luber / Nitschke 1999; Fockenbrock 2000).

– The other indicator that refers to the communicative dimension of shareholder orientation is investor relations: having an investors relations department, organizing road shows and analysts' meetings, publishing quarterly reports, organizing general shareholders' meetings of high quality and, most important, having one-to-one talks with institutional investors. The *Manager Magazin* also publishes an investor relations survey once a year. The second column in Table 2 shows the standardized average results for the years 1996, 1997, 1998 and 1999 (Enzweiler / Friese / Nitschke 1997, 1998; Luber / Nitschke 1999; Luber 2000).

One should note that high communication standards between managers and minority shareholders are more than symbolic company policy. Transparency and open communication reduce agency costs and minimize the room for managers to follow their own objectives. In particular, open communication on segmental performance makes cross-subsidization (Rappaport 1999: 93) visible and raises the pressure on segments to produce shareholder value. Therefore, the communication side of shareholder value has a value driving effect.

– Of course, the operational dimension of shareholder value is the most important one (Rappaport 1999). The shareholder value approach assesses the impact of business decisions on future cash flows, discounting these cash flows in order to decide whether investment decisions create or destroy shareholder value. Although there are many variations of value-based management systems, these strategies can be grouped into basic categories (Ryan / Trahan 2000: 2; Bühner 1996): the "initial" Discounted Cash Flow (DCF) approach by Rappaport; the Cash Flow Return on Investment (CFRoI) method, developed by the Boston Consulting Group; the Return on Invested Capital (RoIC) method by McKinsey; and the Economic Value Added (EVA™) approach, trademarked by Stern Steward & Co. As each of the concepts is linked to a consultant firm, the quality of each of the approaches is disputed (Price Waterhouse / ZEW 1998). The different variants of EVA™ seem to play the most important role for companies trying to implement operative shareholder-value management (Achleitner / Bassen 2000; KPMG 2000). It is difficult to assess the degree of operative shareholder orientation among companies because one cannot decide how important these concepts really are in the different companies. Additionally, the differentiation of value-based and "old-fashioned", non-value-based concepts is problematic. Therefore, a proxy variable is used to measure the degree of operative shareholder value management: the implementation of profitability goals for the segments or the company as a whole (Glaum 1998: 56–58; KPMG 2000: 30). Such profitability goals are "hurdle rates" that companies must fulfil in order to satisfy the shareholders' demands. In the case of segmental criteria, they produce pressure on segments that create a negative shareholder value. The third column in Table 1 shows whether or not the observed companies have implemented profitability goals by the spring of 2000 (1=yes, 0=no).

– The last indicator refers to the managerial compensation side of shareholder value. The salaries of top managers consist of two parts: one being fixed, the other being variable and dependent on profitability or stock price. Variable compensation is in the interest of shareholders because it generates incentives to increase profitability. Therefore, similar to transparency, it reduces agency costs. One instrument in variable payment is a bonus for exceeding predetermined quantitative or qualitative targets. In the late 1990s, incentives became a rising element in managerial compensation by introducing stock option plans (Glaum 1998: 58ff.; Graf / Lenke / Schießer 1997: 22; KPMG 2000: 31; Pellens / Thomaszewski / Weber 2000: 46). In his seminal book, Rappaport (1999: 133–158) described management compensation as the critical moment of shareholder-oriented company policy. In an interview, Rappaport (1998) called stock option plans the most important distinctive feature between shareholder-oriented and non-shareholder-oriented companies. Column 4 in Table 1 shows

an analyst's assessment of the incentive compatibility of the managerial compensation occurring at German companies in 1997 (Jahn / Prandl 1997).

The four indicators in Table 1 reflect different dimensions of shareholder value. The correlation matrix in Table 2 shows that the indicators are correlated, so one can assume a common factor behind them. This result allows the integration of the four indicators into one index. After the four indicators were standardized, the mean scorings for each company could be calculated. Table 3 shows the "shareholder value index" for the 40 largest German corporations in the late 1990s. Positive scorings point to an above-average shareholder orientation, zero indicates an average, and negative scorings point to shareholder orientation below average. According to this calculation, Bayer, Veba and Hoechst are exceptionally shareholder-oriented, while the shareholder orientation of Axel Springer Verlag, Holzmann and Strabag is very low – which is consistent with the ad hoc assumptions one would have.

Given the different preferences of shareholders and managers described by agency theory (Jensen / Meckling 1976; Jensen 1993; Shleifer / Vishny 1996), any reduction in agency costs should result in the rising inability of managers to reach their own goals. Here shareholder value is considered to be a strategy that opportunistic managers would not pursue if there were no control mechanisms protecting or promoting the interests of minority shareholders. Two groups of mechanisms can be distinguished: mechanisms in the environment of the managers, and mechanisms within the "social world" of the top managers themselves (Jackson 2001a).

4 External Market Forces

Finding 2: The shareholder orientation of companies is linked to the rise of institutional investors as shareholders of large German companies.

The most obvious hypothesis that can be tested with company-based data is the presumption that the degree of shareholder orientation is linked to the ownership structure of the companies. According to Jensen (1993: 850), the capital market is one of four factors to make managers act in the interest of the shareholders. The most noticeable change in the ownership structures of German companies in the 1990s is the rise of institutional investors (Deutsche Bundesbank 2001b; OECD 1998b) and the internationalization of stock ownership, especially the rise of Anglo-American institutional investors. At the same time, the importance of individual investors is in decline.

Different types of investors have different capacities to influence company policy. Hirschman (1970) has distinguished three possible reactions to bad performance on the part of firms or organizations: exit, voice, and loyalty. Table 4 shows a comparison of characteristics of individual and institutional investors. Loyalty is a characteristic of large family investors and, sometimes, individual investors, but not of institutional investors. The institutional investor's capacity to create "voice" is greater than in the case of individual investors, but should not be overestimated. In contrast to reports in business magazines such as *Manager Magazin* and *Capital* (Antrecht / Enzweiler 1995; Balzer / Nölting 1997), empirical studies show that institutional investors only rarely attempt to influence management (Engelhard / Eckert / Kößler 1998; Price Waterhouse / ZEW 1998: 5; Steiger 2000). Their corporate governance capacity lies in professionalizing information-gathering and investment strategy (exit). Therefore, stock prices are becoming more responsible to management decisions and more volatile. McKinsey (2000) found that institutional investors are willing to pay more for the stocks of a "well-governed" company than for a "bad-governed" company, assuming equal financial performance. The difference between the actual share price and the possible "well-governed" share price can be interpreted as a discount for companies without shareholder orientation. Thus, the governance mechanism of "exit" creates a necessity for managers to get rid of stock price discounts. Why do managers react adversely to stock price discounts? High share prices improve the possibilities of acquisitions if they are financed through stock swap. And the share prices influence the conditions of equity financing when new stock is issued. However, there is no indication that German companies increased their use of equity relative to debt or internal finance (see Figures 2 and 3).[5] On the whole, managerial reactions to "corporate governance discounts" can only be understood in combination with other mechanisms, such as share prices as instruments of reputation and the fear of hostile takeovers (see below).

As mentioned above, the role of Anglo-American investors rose dramatically in the 1990s. In 1999, 40 percent of the shareholders of *Mannesmann* were estimated to be British and American funds; 31 percent of *DaimlerChrysler*; and 27.5 percent of *Deutsche Telekom*.[6] Michel Goyer (2001a) has documented the investment strategies of Anglo-American institutional investors. He distinguishes between defined contribution (DC) schemes and defined benefit (DB) schemes. Pension funds such as Calpers are DB funds and invest in a large number of blue chip companies, directing their activism towards shaping the corporate governance institutions of a given country. For example, Calpers has published Corporate

5 Deutsche Bundesbank (1999: 139, 2001a: 29). Figure 3 shows that internal financing and change in liabilities substitute each other in a cyclical way, while injection of fresh funds remains stable.

6 Handelsblatt, November 8, 1999: 22.

Governance Principles for Germany (Calpers 1999). By contrast, mutual DC funds such as Fidelity invest more money in a smaller number of companies. They are less risk adverse and their investments have higher turnover rates. DC funds are more likely to be vocal regarding the strategy of corporations in which they have an equity stake. As a consequence, their ability for "strategic exit" is also higher. The strong relationship between the importance of institutional investors and shareholder orientation supports Michel Goyer's finding that there is a fit between preferences of Anglo-American institutional investors and the change of corporate governance in France and Germany.

Considering the nature of individual shareholders and institutional investors, one would assume a higher shareholder orientation in companies where institutional investors hold a high share of stocks. The importance of institutional investors ranges from 4.5 percent (VEW) to 75 percent (Veba). As Figure 4 shows, a positive relationship does indeed exist between shareholder orientation and ownership by institutional investors (Pearson's r=.63, n=30, p=.000).

Finding 3: Companies in sheltered sectors are less shareholder-oriented than those in internationally competing sectors.

According to Jensen (1993: 850), another governance mechanism that makes managers act in the interests of shareholders is the product market. Sigurt Vitols (1999: 5) has argued that the pressure from institutional investors is not strong enough to change the strategies of corporations; rather, he claims, the decisive pressures belong to product markets. Similarly, Michael Faust (1999: 70) discusses shareholder value as a concept that helps managers mobilize the response to product market competition. Allen / Gale (1999) discuss the limits of capital-market-driven governance mechanisms and come to the conclusion that competition in product markets, particularly international competition, is a powerful force for good corporate governance. In their view, the product market plays the role of the (restricted) market for corporate control: in the case of opportunistic managers, a firm with a stronger management team will capture the product market from the firm with the weaker management team (Allen / Gale 1999: 27). Other authors see the product market as a control mechanism that works to supplement the capital market or the market for corporate control (Baums 1996: 10; Monopolkommission 1998: 77; von Rosen 1997: 7).

Analyzing the balance sheets of all listed German industrial corporations, Albach et al. (1999: 514–517) come to the conclusion that internationalization led to a rapid increase in competition pressure in the 1990s.[7] Figure 5 shows the devel-

7 I wish to thank my colleague Jürgen Beyer for drawing my attention to this calculation.

opment of the market risk[8] between 1965 and 1996, estimated by Albach et al. on the basis of variance in sales. This figure indicates a strong rise in market risk, starting in 1992.

The sample of 40 listed German companies can be divided into companies that are exposed to international competition and companies in the sheltered sector. In the "new" company-based discussion on welfare policy, the sheltered / exposed distinction plays the decisive role in explaining company behaviour (Clayton / Pontusson 1998; Manow 2000; Mares 1996, 2000; Pierson 2000: 794; Swenson 1991a, 1991b, 1997; Swenson / Pontusson 2000). Being exposed to international competition means producing goods that compete with the goods of foreign suppliers (Crouch 1990: 69). In contrast, companies in the sheltered sector are not exposed to this kind of competition, because their goods or services are stationary. Typical sheltered sectors are, for example, personal services. In the sample, three sectors can be classified as non-exposed: construction, trading, and journalism / publishing. What these sectors have in common is that international competitors would have to open German subsidiaries to make sales in the German market. All other companies represented in the sample produce internationally traded goods and are therefore exposed to the increased international competition described by Albach et al. (1999).[9]

Looking again at the shareholder value ranking in Table 3, one can see that the scoring divides the sample into exposed and non-exposed sectors. All the companies belonging to the sheltered sector – *Axel Springer Verlag* (journalism / publishing); *AVA*, *Spar*, *Karstadt*, *Metro* (trading); *Bilfinger+Berger*, *Holzmann*, *Strabag* (construction) – find themselves in the last twelve places of the ranking. If the exposed / sheltered distinction is taken as a dummy variable, the correlation with the shareholder value scoring appears to be strong (Pearson's r=.71, n=40, p=.000). Additionally, companies belonging to the most highly internationalized sector of chemicals / pharmaceuticals (Hassel / Höpner / Kurdelbusch / Rehder / Zugehör 2001) turn out to be located on the upper positions of the shareholder value ranking.[10]

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8 Albach et al. have calculated market risks for every firm in every year they observed. Figure 5 shows the average scorings. The basis of the calculations is data on variance of sales. A description of this index can be found in Bruse (1984: 976–980).

9 I wish to thank Fritz W. Scharpf for advising me on the distinction between exposed and non-exposed companies in the sample. The concept refers to whether or not a firm stands in direct competition with foreign firms. Of course, even sheltered-sector companies are affected by internationalization. In Berlin, for example, the majority of construction employees are foreign workers, especially from Eastern European countries; but this point refers to another dimension of internationalization.

10 Grant / Paterson / Whitston (1988: 115–122) show that the chemical industry traditionally stood outside "Deutschland AG", depending more than others on self-

Multiple regression shows that both the institutionalization of ownership structure and the competition with foreign goods have significant effects on shareholder orientation (see Overview 1). According to this model, these two variables explain 62.5 percent of the variance in the shareholder value ranking. The variables are significant at the 0.01 (institutionalization) level and at the 0.001 (exposed / sheltered sector) level.

Finding 4: The shareholder value orientation of companies is linked to the exposure for the market of corporate control.

The capital market and the market for corporate control are strongly linked, and are not necessarily treated as being distinctive mechanisms influencing the degree of shareholder orientation. The risk of hostile takeovers is one of the reasons why managers have incentives to combat stock price discounts and choose policies targeting high share prices. Jensen (1993), for example, subsumes the market-for-corporate-control mechanism under the capital-market mechanism. In this article, I view shareholder value orientation motivated by efforts to minimize the likelihood of hostile takeovers as a distinctive mechanism:

– Although capital markets and the market for corporate control are both markets in which shares are commodities, the traded goods are different. The market for corporate control is the market where the discretionary power of disposition over companies is traded.

– Paul Windolf (1994: 84) points out that the market for corporate control is a market with its own distinct business cycle. Consequently, he distinguishes four markets in capitalist economies: commodity markets, labour markets, capital markets and markets for corporate control.

– Not every company that is exposed to the capital market is exposed to the market for corporate control. Companies with a high percentage of state, family or company ownership are sheltered from takeovers, although they may

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financing, having no strong *Hausbank* relationships and less interlocking directorates, and being more internationally oriented than other industrial companies. The fact that the chemical / pharmaceutical industry turns out to be more shareholder-oriented than other industries may have led to the hypothesis that shareholder orientation itself is a phenomenon that emerges outside the “Deutschland AG”. However, this hypothesis can be refuted by investigating the relationship between shareholder value and the degree of interlocking in the ownership network in 1996, measured by the percentage of shares held by large companies (Pearson’s r=-.10, n=40, p=.529). Shareholder orientation does not emerge outside, but both inside *and* outside the company network that is called “Deutschland AG”.

have share price discounts and capital market participants gaining influence through voice strategies.

– Historically, the emergence of a market for corporate control (including the possibility of hostile takeovers) is a recent phenomenon, while the share market appeared in the nineteenth century.

The governance function of the market for corporate control was first described by Henry Manne (1965: 113):

> The lower the stock price, relative to what it could be with more efficient management, the more attractive the take-over becomes to those who believe they can manage the company more effectively.

Postulating a strong relationship between managerial performance and share price, Manne described takeovers as a mechanism for disciplining management. Even the threat of a takeover may be sufficient to generate greater shareholder orientation. However, the experience of hostile takeovers in the US sparked a controversial debate on the welfare and distribution effects of hostile takeovers (Chelma 1998; Davis / Diekmann / Tinsley 1994; Davis / Robbins 2001; Davis / Stout 1992; Franks / Mayer 1995; Kraakman 1988). Several lessons of this debate are: hostile takeovers set incentives for target firms to act in a share-price oriented manner; hostile takeovers also set incentives for the bidding company to act opportunistically; the distribution effects of hostile takeovers seem to be more indisputable than welfare effects; hostile takeovers require a liquid capital market; and managers have invented several defensive strategies that weaken the market for corporate control (Höpner / Jackson 2001: 4–7; Shleifer / Vishny 1996: 29–31). Henk de Jong (1997) has used the presence or absence of a market for corporate control as a distinguishing feature of corporate governance systems and has shown that corporations in systems enabling hostile takeovers pay more value added to their shareholders, pay less value added as wages and are less growth-oriented.

It seems obvious to interpret shareholder value strategies as defenses against the probability of hostile takeovers, because both phenomena appeared in the middle of the 1990s. Germany traditionally enjoyed a relatively low level of friendly mergers. Ownership structures, the influence of banks, the role of the state, accounting and disclosure issues, codetermination and company law all worked as barriers against hostile takeovers. A comparison of the three biggest takeover attempts targeting German companies in the 1990s shows the erosion of barriers against hostile takeovers (Höpner / Jackson 2001):

– The most far-reaching effect is that large banks have changed from the *Hausbank* paradigm to the investment bank paradigm. *Deutsche Bank, Dresdner Bank*

and *Commerzbank* are loosening their strong links with industrial firms. In 1996, 29 members of the Deutsche Bank's board of managers occupied supervisory seats in large German corporations. Only two years later, in 1998, the number of seats declined to 17 (see below). Strong relationships with domestic industrial corporations would endanger a bank's reputation in investment banking. Consequently, banks gave up their role as guardians against hostile takeovers. *Krupp*'s takeover attempt for *Thyssen* in 1997 was the first case where the *Deutsche Bank* supported a takeover attempt.

– The stock corporation law was developed in a direction that makes hostile takeovers more likely. Above all, the *Gesetz zur Kontrolle und Transparenz im Unternehmensbereich (KonTraG)* (1998) forbid voting rights restrictions; these restrictions were one of the most important of *Continental's* defensive actions against the takeover attempt of the Italian tire company *Pirelli*. Additionally, the *Kapitalaufnahmeerleichterungsgesetz* (KapAEG) (1998) made the economic worth of corporations more transparent. Also, cultural attitudes toward share ownership have changed. Since the listing of *Deutsche Telekom* in 1996, interest in the stock market has grown in Germany, which helps bidders who promise a higher shareholder value after an exchange of shares.

– Codetermination does not act as a strong barrier to hostile takeovers any longer. Codetermination has moved in a productivity-oriented direction, which means that "in the foreseeable future, [it] will simply be one of the many elements of corporate governance" (Mitbestimmungskommission 1998: 7; translation by the author), instead of an instrument of class conflict. Comparing the cases of *Thyssen* (1997) and *Mannesmann* (1999 / 2000), one can see that unions have changed their political attitude towards hostile takeovers: from fundamental opposition against "predator capitalism" *(Raubtierkapitalismus)* in 1997 to the approval of hostile takeovers as an acceptable instrument of economic behaviour in 2001.

The probability of being the target of a hostile bid differs from company to company. Unfortunately, it is difficult to estimate this probability. First, the threat of a takeover depends on the ownership structure. The willingness to sell shares to a hostile bidder may rise with the importance of institutional investors, while private investors are told to have a more "emotional relationship" with their shares. In addition, financially oriented blockholders may be more willing to sell than strategically oriented ones; one can assume that family owners and the state would never sell to a hostile bidder. It was shown above that the shareholder orientation tends to be higher where ownership structure is highly institutionalized, which supports the hypothesis of takeover threats as mechanisms constraining managers to act in a shareholder-oriented manner. Second, the probability of a hostile takeover differs with the number of competitors. Corporations whose

products are internationally traded have more competitors than others. That is why the strong correlation between shareholder value and the exposure to international product market competition may also support the takeover thesis. Third, the threat of a takeover appears to be high when the share price is low. Share price discount can be caused by the degree of diversification. Because of their reputation for being less transparent, clumsy and economically inefficient, highly diversified corporations tend to be undervalued (Amelung 1999; Denis / Denis / Sarin 1997; Morck / Shleifer / Vishny 1990; Rajan / Servaes / Zingales 1998). The moderate correlation between shareholder orientation and the number of sectors of the economy in which the companies are involved (Pearson's r=.43, n=40, p=.006) may be interpreted in the sense that conglomerates are more likely to be targets of hostile takeovers. In the US, the takeover wave during the 1980s led to the de-conglomeration of US corporations (Davis / Robbins 2001).

Empirical evidence supports the presumption that the threat of takeovers tends to increase shareholder orientation. However, one should note that the perception of being a potential takeover target differs from company to company. In the case of *VEBA*, the crucial impulse to implement a more shareholder-oriented strategy in the early 1990s was a study by S. G. Warburg that showed a large conglomerate discount and described the company as a candidate for a hostile takeover. Similarly, the shareholder-oriented strategies of *Bayer* and *Hoechst*[11] (in the mid-1990s) and *Siemens* (in the late 1990s) can be interpreted as reactions to takeover threats and rumours. In other cases such as *Mannesmann*, the takeover hypothesis fails to explain strategies targeting high share prices. According to the investor relations department of *Mannesmann*, the perception of being a takeover target did not appear before the end of 1998, when a more shareholder-oriented strategy was already in progress.

5 Shareholder Value as a Managerial Initiative

In the last section, three external impulses for the shareholder orientation of companies were identified: capital market exposure, international product market competition and the market for corporate control. According to these arguments, shareholder value appears to be a strategy that external forces push and that managers would not implement voluntarily. The structure of the discourse on shareholder value shows that this may only be one part of the story; shareholder value also seems to be some kind of a "managerial ideology" that increases the

11 See Eckert (2000).

reputation of managers (Faust 1999: 70; Vitols 2000). This section discusses whether there are empirical indications for shareholder value as a strategy that managers themselves may choose, without external forces in the environment of the corporation.

Finding 5: Shareholder-oriented companies enjoy a high reputation among German managers.

A first indication of the high reputation of shareholder-oriented strategies among managers comes from image surveys. In the spring of 2000, the weekly economic magazine *Wirtschaftswoche* asked 1,400 German managers to give their opinion on the innovation image – in the sense of new, pioneering, productivity-enforcing – of large German companies.[12] Figure 6 shows the result; the lower the number, the better the company image is. *DaimlerChrysler* appears to have the best and *Holzmann* the worst image. The shareholder orientation is shown on the vertical axis, yielding a strong correlation between shareholder orientation and the company image among managers (Pearson's r=–.66, n=33, p=.000). This finding supports the view that shareholder value seems to possess features of a managerial ideology by being a strategy that enjoys a high reputation.

Finding 6: The social world of German top managers has changed and is still changing towards a more competitive and financially oriented world of experience.

The business systems literature has emphasized the importance of management education and careers and their influence on managerial identity and value orientation (Lane 1989; Lane 1992: 71). Therefore, management ideology (in a neutral sense) acts as a variable that connects management education and careers with management style. International comparisons and country studies have shown several nationally specific features in the "social world" of top managers (Byrkjeflot 1996; Egan 1997; Hartmann 1997; Lane 1989, 1992; Sorge / Warner 1986; Sorge 1999; Steward et al. 1994; Walgenbach / Kieser 1995):

– The most discussed feature of German business careers seems to be the role of professional training. While US or UK executives advance into management by specializing in business administration, German top executives conceive of themselves foremost as experts in a technical field (*Fachmann*). As a consequence, the German executive appears to be more directly involved in production. Regarding the 1970s, a survey among top managers came to the conclusion that only a half of them were university graduates; 60 percent of them

12 Wirtschaftswoche, June 1, 2000: 96.

were engineers or natural scientists, 30 percent were economists and 10 percent were lawyers (Poensgen 1982: 17).

– In contrast, financial economics do not play an important role in the management education and the career of German managers.

– A management-distinct job profile is more elaborated in Britain and the United States than in Germany which does not have the Anglo-American tradition of elite business schools.

– The role of the external labor market for managers is limited in Germany because a significant number of top managers are recruited internally. Anglo-American top managers usually look for management positions on the general labour market. In effect, the competition between German top managers of different corporations is limited.

– Top executive turnover is a frequent phenomenon in Britain and the United States, while German top executives spend a longer time in office.

One should note the complementarities between the education and career features and other spheres of the German production regime. According to Byrkjeflot (1996: 12), the German top manager is embedded in a much stronger technical culture, which leads to a strong emphasis on production design. Thus, German factories show a strong tendency for technical functions to be incorporated into the management hierarchy, which limits the relative importance of financial economics (Egan 1997: 6). Also, the importance of technical expertise and training effects management culture. The productivist ethos of the business organization acts as an integrating mechanism, forcing the consideration of technical employees and placing emphasis on vertical integration, training, quality standards and build-up of long-term market share (Egan 1997; see also Streeck 1992b and Soskice 1999). Additionally, the long years in office can be interpreted as a requirement for the long-term relations that German top managers enjoy with their suppliers, customers, other corporations, banks and works councils. Similarly, the limited role of the external labour market may favour the tendency to work for long-term profits instead of short-term success. In sum, one would assume shareholder value policies more in the context of Anglo-American career and education features than in the German environment.

I collected information on the careers of all 90 top managers who were chief executives in the 40 largest listed industrial corporations in Germany in the 1990s.[13]

13 These top managers, in the order in which their firms are listed in Table 1, are: Frank Niethammer, Udo G. Stark, Klaus Daudel, Kurt Lindemann, Jürgen Strube, Hermann J. Strenger, Manfred Schneider, Hans-Otto Wöbcke, Rolf Kunisch, Christian Roth,

Figures 7 and 8 show the development of the career and education features of top managers in the 1990s.

– Figure 7 shows a trend towards professionalization. The share of chief executives without higher educational training declined from just under 14 percent to zero percent in 1998 and 1999.

– The share of top managers who went through the German apprenticeship system is in decline (from 30 percent in 1990 to 15 percent in 1999).

– Most remarkably, the role of the external labour market is clearly rising. In 1990, 17 percent of the observed top managers were recruited from outside the company; in 1999, the percentage rose to more than 35 percent. Conversely, the role of *Hauskarrieren* is in decline.

– Figure 7 also shows that the percentage of top executives who can be classified as financial experts[14] is rising. 39 percent of the 90 chief executives have studied economics, 24 percent have trained as lawyers, and 32 percent have studied natural science or technical subjects.[15] Comparing these data with information on the 1970s (Poensgen 1982) suggests that changes occurred between the 1970s and the 1990s, because the role of natural science and technical subjects was higher in the 1970s.

– Figure 8 shows the average duration of the time spent in office. One can see that the average time in office is in dramatic decline, from more than 13 years

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Herbert Bodner, Eberhard v. Kuenheim, Bernd Pischetsrieder, Joachim Milberg, Hans-Ulrich Plaul, Horst W. Urban, Hubertus von Grünberg, Stephan Kessel, Edzard Reuter, Jürgen E. Schrempp, Gert Becker, Uwe-Ernst Bufe, Heyo Schmiedeknecht, Klaus G. Lederer, Heinz Ruhnau, Jürgen Weber, Ron Sommer, Kajo Neukirchen, Werner Kirchgässer, Anton Schneider, Helmut Sihler, Hans-Dietrich Winkhaus, Wolfgang Hilger, Jürgen Dormann, Hans-Dieter Anders, Hermann Becker, Lothar Mayer, Heinrich Binder, Walter Deuss, Gerhard Cromme, Hans Meinhardt, Gerhard Full, Klaus Götte, Rudolf Rupprecht, Werner Dieter, Joachim Funk, Klaus Esser, Heinz Schimmelbusch, Jens Odewald, Wolfgang Urban, Klaus Wiegandt, Hans-Joachim Körber, Ernst Pieper, Michael Frenzel, Hans U. Brauner, Friedhelm Gieske, Dietmar Kuhnt, Dietmar Hopp, Hasso Plattner, Giuseppe Vita, Karlheinz Kaske, Heinrich von Pierer, Helmut Dotterweich, Arwed Fischer, Peter Tamm, Günter Wille, Günter Prinz, Jürgen Richter, August A. Fischer, Peter Jungen, Otmar Franz, Jörg Kuchenwald, Karl Schneider, Klaus O. Fleck, Theo Spettmann, Heinz Kriwet, Dieter H. Vogel, Ekkehard Schulz, Klaus Piltz, Ulrich Hartmann, Klaus Knizia, Fritz Ziegler, Gert Maichel, Werner Lamby, Alfred Pfeiffer, Georg Obermaier, Wilhelm Simson, Carl H. Hahn, Ferdinand Piëch.

14 Top managers who once worked for the financial division of any company were classified as financial experts.

15 These data were weighted for the duration of the time in office.

in 1965 to less than 7 years in 1996. Please note that only completed times in office were quoted, so the line should have no "natural" tendency of decline.

Summing up, one can see a trend towards professionalization, a greater importance of economic and financial issues, recruitment from the external labour market for managers, and shorter times in office. These data suggest that the changing "social world" of top managers helps explain why shareholder value strategies enjoy the high reputation among managers. The changing context in which managers are acting changes their perception of goals that might be pursued. The emergence of a highly competitive labour market for managers requires the application of measurable performance criteria such as CFROI, EVA™ and – of course and objectively comparable – share price development. At the same time, the willingness of supervisory boards to fire top managers is on the increase. In the 1990s, several chief executives were forced to retire from office because of bad performance and the resulting crises of confidence in the supervisory board, for example Horst W. Urban (*Continental*), Anton Schneider (*Deutz*), Heinz Schimmelbusch and Heinrich Binder (*Metallgesellschaft*), Bernhard Walter (*Dresdner Bank*), Dieter Vogel (*ThyssenKrupp*). As a result, the incentive to follow strategies targeting high share prices is also rising. Beyond that, the increased importance of financial economics in education and careers favors the willingness to utilize financial indicators. Of course, the causality in these cases might be recursive; a given shareholder value orientation should also raise the demand for financially oriented managers. What is emphasized here is a distinct, non-recursive influence of "management culture" variables on management behaviour. The professionalization and the marketization of management create a climate that favours some management ideologies more than others. The suggestion is to take cultural variables into account in order to enrich the discussion on changing "varieties" of capitalism.

Finding 7: Shareholder value policies legitimate rising management remuneration.

Another reason why managers themselves may be interested in shareholder-oriented company policy is that it legitimates rising compensation. One dimension of shareholder value refers to the rise of the variable part of compensation, particularly in the form of stock options. Experience shows that managers receive stock options in addition to their fixed salaries. The case of *BASF*, where top managers have to invest one part of their fixed salaries in order to receive stock options, is an exception to the rule.[16] Shareholder value has, generally, an increasing effect on salaries. It is interesting that, beside stock options, the fixed parts of managerial compensation are rising rapidly in the late 1990s.

16 Handelsblatt, October 8–9, 1999.

Table 5 shows the average and percentage increase in salaries for board members of the 40 largest listed corporations in 1996 and 1999. These enormous rates of increase exist even excluding the boom in managerial stock options. Contrary to the creation of incentives by rising variable parts of payment, the rise in fixed salaries is not in the interest of minority shareholders; stock option programmes with hurdle rates that are too low are often combated by shareholder activists.[17] In 1996, the average salary for an average board member was DM 1.2 million. The lowest was DM 280,000 (*Rheinmetall*), the highest was DM 2.6 million (*Metro*). The average increase between 1996 and 1999 (when board members received an average of DM 1.94 million) was 66 percent, ranging from minus 21 percent (*Spar*) – nomen est omen[18] – to 466 percent (*Daimler-Benz* / *DaimlerChrysler*). Some of the data must be explained as isolated cases. Of course, the explosion of remuneration at *Daimler* – where an average board member earns DM 7.93 million plus stock options with low hurdle rates! – happened because of the *Daimler* / *Chrysler* merger. Shareholder activists such as Ekkehard Wenger claimed that the fusion was motivated by the opportunity to raise management remuneration to the American level. Another case with an exorbitant rise, *Agiv* (mechanical engineering), is a company that is close to disintegration. This management is playing an endgame because it does not have to fear punishment for its action. This is a clear indication that managers actually work for their own goals if they have the room to manoeuvre. Correlations between salary growth and corporate governance indicators show how the German corporate governance system is changing.

– The concept of managerial control (Berle / Means 1932) refers to the absence of large shareholders and is measured by a variable combining (a) the part of shares in dispersed ownership and (b) the number of years in the 1990s in which the chairman of the supervisory board was an ex-manager of the same company. One finds a highly significant correlation (Pearson's r=.50, n=38, p=.001) between the extent of managerial control and managerial compensation in 1996. This finding, again, supports the principal-agent hypothesis that managers follow their own goals if they have the ability to do so.

– Referring to the development after 1996, one finds that the increase in salaries is significantly higher if the supervisory board chairman is a banker (Pearson's r=.35, n=36, p=.038). This is interesting because in 1996 the direction of the influence was the other way round: in the broad tendency, bankers as chairmen had a drop in remuneration (Pearson's r=-.28, n=40, p=0.84). This indicates a change in how bankers are monitoring (see Finding 8 below).

17 Handelsblatt, March 3–4, 2000: K3; Handelsblatt, November 7, 2000; Handelsblatt, November 27, 2000: 18; Handelsblatt, May 30, 2001: 1.

18 "Spar" comes from "sparen," to save or economize.

– Looking at the 1999 data, managerial compensation turns out to be significantly correlated with the shareholder value orientation of the companies (Pearson's r=.39, n=36, p=.018).

These findings have two important implications for the debate over shareholder value. First, the impact of shareholder orientation on top management compensation – in the form of stock options and, surprisingly, even on fixed remuneration – shows that managers themselves may have an interest in the reorientation of company policy. Second, the shareholder value phenomenon appears in a context where the extent of managerial control from inside seems to be declining.

Finding 8: While shareholder value increases control by capital market participants, the extent of internal control is decreasing.

Contrary to outsider systems like the US and the UK, the supervision of German company policy has traditionally been provided by insiders, especially by banks (Beyer 1998; Cable 1985; Edwards / Fischer 1994; Jackson 2002; Monopolkommission 1976; O'Sullivan 2000; Schröder 1996; Sherman / Kaen 1997; Streeck / Yamamura 2001; Vitols 1996, 2002). The reorientation of banks from the *Hausbank* to the investment bank paradigm contradicts their willingness to play a major role in the monitoring of industrial companies (Beyer 2001; Höpner / Jackson 2001; Streeck 2001), because a close relationship to industrial companies would weaken their reputation among international customers of financial services. Figure 9 points to a clear decline in the role of banks in company monitoring. Especially the *Deutsche Bank* is withdrawing monitoring; as mentioned above, the *Deutsche Bank* has nearly halved its supervisory board chairs in German companies. Beside the personal involvement of banks, the overall density of interlocking directorates in Germany is declining (O'Sullivan 2000: 280–287; Windolf 2000). This development can be expected to accelerate in 2002 when the "*Eichel-Plan*" (named for the German Minister of Finance, Hans Eichel) abolishes the tax on the profits of sales of share blocks (Höpner 2000).

Figure 10 shows the density of interlocking directorates, defined as actual personal involvement as a percentage of mathematically possible involvement, for the 100 largest corporations and the years 1980–1998. Who compensates for this lack of inside monitoring? The answer is – – managerial control. Figure 9 indicates that a rapidly growing number of supervisory boards is led by ex-managers from inside. Corporate governance is exhibiting more market control and less insider control[19]. The explosion of managerial compensation arouses the suspicion

19 Michel Goyer (2001b: 18) found that in 1998, only 3 percent of supervisory board members elected by shareholders could be classified as independent directors.

that this development is not contrary to the preferences of managers. It is doubtful whether managerial control is actually in decline, taken as a whole.

6 Shareholder Value, Unions and Codetermination

What role do employee representatives play in shareholder-oriented companies? Coffee (1990: 1496) has suggested that we view the company as a set of coalitions between managers, shareholders and employees, in which any two players can form a coalition against the third. Three types of conflicts can thus be distinguished: conflicts over managerial control, where shareholders and employees go up against managers; insider-outsider conflicts where managers and employees oppose shareholders; and the class conflict, in which employees on the one side are in conflict with shareholders and managers on the other side (Figure 11). When the conflict lines behind the shareholder-value strategies are revealed, we can find different constellations that affect shareholder value.

Finding 9: Shareholder value manifests itself as a conflict about managerial control or as an insider/outsider conflict, while incidences of class conflict are limited.

The role of the trade unions and works councils is most indisputable with respect to the communicative dimension, especially the discussion on accounting. Of course, the conflict over transparency is a principal-agent conflict between managers and shareholders. While far-reaching transparency decreases agency costs, a lower degree of transparency increases the room for manoeuvre of managers and secures their jobs. In this conflict, German trade unions have decided to side with shareholders.

Unions recognize that international accounting standards, whether IAS or US-GAAP, seem to be, at first sight, investor oriented. In effect, they are viewed as being employee oriented, too. Trade unionists argue that they have called for company transparency all along, because they need accurate information to achieve the goal of codetermination: to monitor economic power. Unions have supported the legislation on company finance (*Kapitalaufnahmeerleichterungsgesetz)* that has allowed the use of international accounting methods and have even called for an EU directive that obliges German companies to use IAS. One important reason for this demand is that works councils have a great interest in being able to compare the performance of subsidiaries in different countries, which becomes difficult if different accounting standards are used. German unionists argue that transparency is a tool for codetermination (Bolt 2000; Köstler 2000a,

2000b; Küller 1997a, 1997b; Putzhammer / Köstler 2000; Scheibe-Lange / Prangenberg 1997).

Contrary to the traditional accounting rules of the German Commercial Code, international standards place constraints on accumulating hidden reserves in times of good performance. One could, however, argue that it might be in the interest of employees to hide cash flows in good times and have reserves in bad times. Trade union experts do not agree with this view. Hidden reserves, they believe, have a levelling effect on the balance sheets of companies. With regard to the distribution of dividends and earnings, the effect of German accounting rules is not anticyclical but procyclical. In bad times, companies using German accounting rules publish earnings that come from hidden reserves, while in fact there is no operating profit at all. Published earnings lead to distribution demands that may eat up substance of the firm, which is dangerous especially for employees. In contrast, in the context of high earnings, published profits are minimized even though the company would be able to distribute them to employees and shareholders.

Far from being just theoretical, this issue played an important role in the biggest German company crisis of the 1990s. In the case of *Metallgesellschaft*, management published earnings and paid dividends although the operative situation in the years 1990–1992 turned out to be disastrous (Knipp 1998: 83). In the case of *Holzmann*, dividends were being paid out to shareholders just before the government intervened to save the company from bankruptcy in 1999. The veiling of operative losses is also dangerous because it may delay necessary action against the causes of bad performance. The unions' position of rejecting traditional German accounting standards as being superior to international accounting standards is shaped by the works councils. The works councils of the 40 companies investigated here were asked for their opinion on international accounting standards (IAS or GAAP) (see Table 6). 24 of them replied to the question. 16 of the 24 companies had changed their accounting in favour of international standards. None of the works councils answered that they were opposed to international accounting. Three works councils said that they were indifferent, while the other 13 works councils supported the change in accounting. Both employee representatives, be they unions or works councils, and shareholders prefer high transparency rules in accounting standards.

Another dimension of shareholder orientation where the preferences of employee representatives and shareholder activists are similar is top management compensation (Engberding 2000). Unions share the view of capital market participants that top managers' salaries should be variable according to the level of company success. Just like shareholder activists, unions criticize the trend towards escalating salaries. Because top management remuneration is decided by the personnel

committees of supervisory boards, employee supervisory board members have the possibility of co-determining stock option plans. In practice, most employee representatives accept stock option plans and demand that they be extended to employees as additional salaries or as a right to acquire shares at reduces prices. In our survey, 20 of the 40 works councils interviewed answered the question of whether or not they accepted stock option plans. Only five of them said that they opposed stock option plans, while 15 actually supported them. From an employees point of view, it might be desirable to tie top management compensation to social goals, above all to employment; but there is no empirical example of such a compensation plan in practice.

The operative dimension of shareholder orientation turns out to be more complex. 18 out of 40 works councils gave their opinion on the implementation of profitability goals for segments of the company or for the company as a whole. 9 of them opposed profitability goals, 2 supported them, and 7 professed to be indifferent. In the case of profitability goals for company segments, the negative response was somewhat higher. It is interesting that the statements on profitability goals are highly correlated with the overall shareholder orientation: Pearson's r equals –.61 (n=18, p=.008), and r=–.61 (n=17, p=.004) in the case of profitability goals for segments. This result suggests that works councils oppose profitability goals if they appear in a shareholder-oriented context. One can assume that shareholder-oriented companies tend to be faster at selling companies that fail operative targets;[20] in consequence, works councils find such targets more dangerous when profitability goals are communicated with shareholders and management pay is related to profitability. Similar to this finding, works councils oppose strategies that focus on core competencies if the context is a highly shareholder-oriented company strategy. In this view, the operative dimension of shareholder value seems to create a coalition of shareholders and managers against employees (class conflict) or a conflict in which managers and employees oppose unreasonable profitability demands or demands for radical restructuring by shareholders (insider / outsider conflict).

However, case studies show that even the operative side of shareholder value sometimes can be a conflict over managerial control. One example of this is the conflict over the separation of subunits at *Mannesmann* (before the hostile takeover), where both employee representatives and shareholders pressed the management into restructuring. Shareholders have a strong preference for separated subunits that limit the possibility of cross subsidization. This is the reason why conglomerates are often faced with a discount in share price (Denis / Denis / Sarin 1997; Morck / Shleifer / Vishny 1990; Rajan / Servaes / Zingales 1998). Interest-

20 Not surprisingly, shareholder value and M&A (mergers and acquisitions) activity correlate positively (Pearson's r=.36, n=40, p=.021); data for 1996 / 1997.

ingly, in some cases unions and works councils will shape that preference. In 1999, *Mannesmann* was an extremely heterogeneous company, active in the telecommunications sector, in machine tools and automotive accessories, tubes and luxury watches. Telecommunications had become the focal segment within *Mannesmann* and attracted a growing proportion of funds for investment. An interviewed trade unionist at *Mannesmann* described the situation as follows:

> The development of telecommunications slowly became dangerous for the other divisions. At the same time, as billions were being spent on the acquisition of *Orange*, in the classic businesses we had to fight tooth and nail for every hammer.

The return on investment for the traditional businesses was lower, but the risk was much lower, too. Organized labour supported the separation of these firms in order to allow these businesses to continue developing without being disturbed. At the same time, trade unionists working in telecommunications had a preference for separation to get rid of the conglomerate discount that made acquisitions expensive and, of course, increased the danger of a hostile takeover.[21]

A similar constellation appeared in the case of *Thyssen Krupp*, which was planning a (since revised) new company structure. The company saw its future in industrial services. The classical steel subunit had developed from a core business to a marginal activity. *Thyssen Krupp* planned to spin off *Thyssen Krupp Steel*. Initially, a stock listing of 30 percent of *Thyssen Krupp Steel* was planned. The works council chairman Dieter Kroll (2000: 27; translation by the author) supported the planned stock listing demanded by shareholders:

> For two years now, we have observed that steel is no longer seen as a core competency. We don't attract high investments. … The scenario is: either be sold or become stunted. Under these conditions, the stock listing might be a prospect. … Without stock listing, we would have no chance of becoming a core business.

These cases show that spin-offs and return to corporate specialization can be undertaken with the consensus of organized labour. Here capital market orientation and "co-management" style codetermination are hardly irreconcilable opposites. The mixture of core and marginal business is problematic for employees, too. Employee representatives in the core businesses see the advantages of strategies to focus on core competencies, because these strategies strengthen the core companies and decrease stock price discounts. In the view of employees engaged in marginal activities, a change in the main shareholder may increase the chance to become a core business. In most cases, management and employees oppose shareholders' demands for radical restructuring. A good example of such an in-

21 For a detailed case study on *Mannesmann*, see Höpner / Jackson (2001).

sider / outsider conflict is the demand of some major shareholders to break up the *Bayer* conglomerate into legally separate corporations.[22]

All in all, in contrast to what one could conclude from the public debate, shareholder orientation is more likely to cause an insider / outsider conflict or a conflict over managerial control than a class conflict. My thesis is not that class conflict does not play an important role any more, but that it does not play itself out with regard to shareholder-oriented strategies. One essence of class conflict lies in pay policy. There is no example of a company acting radically differently with regard to pay policy once it has become more shareholder-oriented. None of the companies investigated have opted out of central collective agreements (*Flächentarifverträge*). Shareholder-oriented companies even seem to avoid any sort of confrontation over pay policy. The reason for this is not the shareholder orientation but background variables: the size and degree of internationalization of these companies.

There are three reasons why large, international companies profit more from central collective agreements than small ones (Hassel / Rehder 2000; Manow 2000; Thelen 2000). First, they enjoy greater productivity and would be confronted with higher wage demands if they opted out of central collective agreements. If unions base their wage claims on overall productivity development, highly productive corporations tend to have decreasing unit labour costs, while less productive companies are faced with increasing unit labour costs. Second, union organization tends to be greater in large companies than in smaller ones, which increases the likelihood of strikes. Third, shareholder-oriented companies belong to the exposed sector and are therefore especially vulnerable in labour disputes. Shareholder-oriented companies are not indifferent to pay policy but have clear preferences, which is why they do not provoke class confrontation, but are indeed afraid of it. Another reason why big firms do not opt out of central collective agreements is the existence of plant-level pacts, where managers and employees relinquish salaries above the centrally agreed scale in exchange for job security (Rehder 2000, 2001; Hassel / Rehder 2000). There is no statistical correlation between the degree of shareholder value and the existence of plant-level pacts. Antje Kurdelbusch (2001) has shown that shareholder-oriented companies tend to create variable salaries not only for managers, but also for employees. She found a very strong correlation between her index on variable payments and shareholder value (Pearson's r=.76, n=24, p=.000). These variable payments are not the

22 Handelsblatt, July 21–22, 2000: 24. Other examples of this constellation are *Veba, Siemens, MAN, Degussa-Hüls, Deutsche Telekom*. Most cases are a mixture: management tends to focus on core competencies, more (*Veba*) or less (*Siemens*) supported by works councils (Zugehör 2001), but shareholders' demands turn out to be more radical and are opposed by insiders.

result of confrontation, but are created in consensus with employee representatives at the micro level.

Another field that some authors interpret as distributive policy is codetermination. There is absolutely no indication that shareholder value companies attempt to put an end to codetermination. Shareholder value seems to strengthen some trends that were already observable in the 1980s. Five trends in codetermination[23] can be distinguished (Deppe 1998; Gerum 1997, 1998; Jackson 2001b; Kotthoff 1998; Mitbestimmungskommission 1998; Müller-Jentsch / Seitz 1998: 367; Reppel 2001; Streeck 1984, 1996, 2001: 21, 26; Thelen / Turner 1997):

1. *System conformity*. Codetermination is no longer seen as an instrument for transforming the economic system into a mixture of capitalist and socialist elements (*Wirtschaftsdemokratie*). It is fully accepted that codetermination operates in firms whose natural goal is to generate cash flows and earnings.

2. *Efficiency orientation*. Democratic participation at the workplace is still one legitimizing force behind codetermination. However, increasingly codetermination has also to prove that it is not only the more democratic or social, but also the more efficient model for organizing the micro-relationship between employers and employees.

3. *Co-management and professionalism*. In practice, codetermination goes far beyond its legal foundations, interfering in and legitimizing company policy not only in social and personnel issues, but in economic issues also. The boundary between management functions and codetermination becomes increasingly harder to discern.

4. *Consensus orientation*. While confrontation between works councils and employers is becoming rare, codetermination seems to have committed itself to being a cooperative process. Both sides see themselves as partners, not as opponents in class confrontation.

5. *Negotiation of rules*. Similar to the guideline on European Works Councils (EWC), evidence is growing that the role of labor law is decreasing, while the importance of negotiated codetermination rules is increasing. For example, several corporations have set up "working teams of works councils" (*Arbeitsgemeinschaften der Betriebsräte*) that rely on negotiated rules instead of works councils at the holding level (*Konzernbetriebsräte*) that are based on labor law.

23 Distinguished from pay policy.

Finding 10: The increasing micro-orientation of codetermination gives rise to a micro/ macro conflict between works councils and unions.

Summing up, codetermination practices are becoming more micro-founded and micro-oriented. This complicates the relationship between works councils and unions who see themselves as the macro forces of the labour movement. Micro and macro goals of employees can contradict each other, so the micro / macro conflict of employees goals is a further conflict line that is influenced by the trends described. The unions' axiom that codetermination should go beyond micro goals becomes increasingly undermined by practice. One example of this is the discrepancy between micro and macro reactions to *Krupp's* hostile takeover attempt in 1997. While *IG Metall* was fighting hostile takeovers as an illegitimate instrument of economic behaviour, *Krupp* employees were supporting the takeover attempt. When 30,000 members of *IG Metall* were demonstrating against hostile takeovers and the role of the *Deutsche Bank* in March 1997, not even the works council members of *Krupp* participated. The different micro interests of employees could not be dominated by common macro interests. Employees defined their interests as company member interests, not as class interests. Because micro interests are more heterogeneous than class interests (Streeck 1992a), the heterogeneity of interests inside unions increases.

Another example of this is tax and regulation policy. While unions and employees as a whole may have an interest in high company taxes, works councils often criticize high tax rates as endangering international competitiveness. The development of the tax rate of *Hoechst* (now *Aventis*) shows how company taxes are declining (see Figure 12). One reason for this is that internationally oriented companies have a host of possible ways to avoid paying taxes. One important trade union expert on accounting, Ingrid Scheibe-Lange, criticizes employee supervisory board members because they do not inform union experts – not even anonymously – on companies' tax avoidance strategies. In other instances of company regulation, similar conflicts arise. For example, several works councils criticize the high environmental standards that unions support.

7 Conclusion

This paper has discussed the shareholder value orientation of large German companies in the light of a company-comparing data set. It has shown that the shareholder value phenomenon is connected to the increasing role of international markets. First, international product market competition rapidly increased in the 1990s. Companies who were exposed to international product markets were im-

plementing shareholder value strategies to increase efficiency, while companies in sheltered sectors were not. Second, shareowners became more demanding and began to compete with each other. That is why shareholder value is strongly related to the importance of institutional investors in ownership structures. Third, in the late 1990s, barriers against hostile takeovers that were characteristic features of the German model ceased to work any more. The probability of hostile takeovers differs from company to company. There is a broad tendency for companies that are exposed to the market for corporate control to be more shareholder-oriented than others. In Section 2, it was shown that experts disagree as to whether the exposure to international competition or the internationalization of finance patterns leads to the adoption of Anglo-American standards; the empirical findings show that both spheres seem to be gateways for shareholder value.

However, the exposure to international product markets, capital markets and markets of corporate control is only one part of the story. A realistic description of the shareholder value phenomenon has to take into account that shareholder orientation enjoys a high reputation among German managers. External impulses to increase shareholder orientation fall on fertile ground. Shareholder orientation increases managerial compensation, both variable surpluses and fixed salaries. And changes in the social world of top managers – growing professionalism, growing competition on the labour market for top managers and the growing role of financial expertise – are fitting with strategies that have comparable financial code numbers as targets.

Overall company monitoring does not seem to be increasing, because growing monitoring by capital markets is being replaced by shrinking internal monitoring of company networks and banks. Different control groups shape different preferences. Bank and company network monitoring allowed companies to distribute risks by diversifying company activity among different sectors. Capital market participants, especially institutional investors, are averse to company diversification because contemporary investment technology allows them to develop their own diversification strategies (Zugehör 2001), which constrains managers' preferences. In the field of management compensation, constraints seem to vanish and the managers' room to manoeuvre seems to grow.

While different external gateways for the adaptation of Anglo-American standards in company policy are frequently and controversially discussed in the literature, the thesis of the major role played by internal factors is more innovative. It is difficult to say whether the shareholder value phenomenon would also have appeared if internationalization had not transpired. At least, in addition to internationalization, internal developments have led to company strategies that are alien elements in the German model. This point is interesting with regard to the varieties theory that describes the spheres of the political economy as forming an

equilibrium that could perhaps be destabilized by external impulses, especially the internationalization of finance. One should not misunderstand the term of interlocking complementarities as total harmony between spheres and stakeholder groups; discrepancies inside the production systems are strong enough to lead to destabilization – especially if they are combined with external impulses.

Unions and works councils were shown to have played a different role than one would have expected. Shareholder value does not lead to a tightening-up in class confrontation. In the fields of pay policy and the employees' right to codetermination, internationally oriented employers – similar to employees – are getting more conflict-averse rather than conflict-oriented. The operative dimension of shareholder value creates changing coalitions between managers, shareholders and employees. The communicative dimension and the managerial compensation dimension seem to contain a conflict over managerial control in which both employees and shareholders are in opposition to managers.

Codetermination and central collective agreements are not jeopardized by shareholder value, and at this point shareholder value and codetermination are getting along better than one might have expected. Given the neat fitting complementarities between constrained capital markets and codetermination in the past, as emphasized by varieties theory, one might have predicted more tension between shareholder value and codetermination. A characteristic feature of David Soskice's varieties theory is his scepticism about the possibility of a mixture between continental European and Anglo-American economic institutions. Of course, shareholder orientation in some of the largest German companies is a new phenomenon, and actors are tending to improvise rather than adopt a fixed behavioural strategy. Nevertheless, first impressions of the interplay of shareholder orientation and codetermination raise doubts about whether one can know *ex ante* if these economic features will fit and lead to successful company strategy. The convincing thesis of interlocking complementarities between a weak role of shareholders in company policy and monitoring, on the one hand, and cooperative industrial relations, on the other hand, has been developed *ex post*, and the fit was neither predicted nor intended (Höpner 2001; Jackson 2002). It is conceivable that future research will emphasize the combination of shareholder orientation and codetermination as a precondition for economic success in post-millennium Germany, because only codetermination might allow employees to have faith in a process that would otherwise undermine quality production and incremental innovation. Another future scenario could be that divergences inside national economies continue to grow and accommodate different kinds of fits in sectors (Schmitter 1990; Hollingsworth / Schmitter / Streeck 1994) or regions (Voelzkow 1999).

However, the observed continued existence of codetermination and central collective agreements is superficial. The dismantling of institutions is only one extreme kind of institutional change. As Kathleen Thelen (2001: 29–30) points out, "[a]nother way that institutions change is through processes of institutional conversion, as institutions designed with one set of goals in mind are turned to other ends. These processes can be set in motion by a shift in the environment that confronts actors with new problems that they address by adapting existing institutions to new ends." One indication that shareholder orientation inspires such a kind of institutional change is the enormous rise in the variable pay of blue-collar workers and the strong correlation to shareholder orientation (r=.76, n=24, p=.000) that Antje Kurdelbusch (2001) has found.[24]

Central collective agreements were initially arranged to save wages from competition between firms. The idea of "solidaristic wage policy" was to leave the market outside wage policy. Nowadays the introduction of contingent compensation makes individual wage depend more and more on market mechanisms (Kurdelbusch 2001: 25) – not alongside, but rather inside, the institutional framework of codetermination and central collective agreements. As mentioned above, shareholder value strengthens the general trend towards the efficiency orientation of codetermination. In this sense, the prediction of varieties theory that changes in one sphere of an economic regime have to lead to changes in other spheres is supported by empirical evidence.

This process can be described as a change in the embeddedness of markets. Sociological theory uses this term in two different directions. The first one is the insight of Granovetter (1985) and others that every market transaction – be it on the job market (Fernandez / Weinberg 1997), the diamond market (Bernstein 1992) or even the financial market (Abolafia 1996) – is embedded in (coexists with, is shaped by and depends on) other, non-market based, social relations (Carruthers / Babb 2000). In this sense, embeddedness is a general pattern that every market relation in every time and every place possesses. The second way "embeddedness" is used is to describe the role of markets at different times and in different places. Value-accumulating rational economic behaviour can offend the spirit of a society (and, therefore, be suppressed) in one period, but be accepted a decade later (Weber 1988: 17–83). Karl Polanyi has described the way in which the economy is instituted by society as a changeable variable (Polanyi 1992). For example, when product markets were emerging, they were physically fenced in to save societies from market practices (Polanyi 1997: 95).

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24 According to Kurdelbusch, the rise of profit-related pay is another area where the efficiency orientation of codetermination at the micro level is on the increase, creating micro / macro conflicts between works councils and trade unions.

Despite the fact that undismantled institutions of industrial relations have been observed to exist, one cannot fail to notice that economic issues in coordinated market economies are becoming increasingly market-driven. In the financing / corporate governance sphere, market transactions are becoming possible that were out of the question in the 1970s and 1980s. One example is the emergence of Anglo-American style investor relations. Before shareholder value, it was considered to be in poor taste for a company to advertise its own shares (Günther / Otterbein 1996: 291). The development of a market for corporate control, including hostile takeovers, is another example of the market capturing more terrain from society (Höpner / Jackson 2001). In the field of industrial relations, market orientation does not destroy codetermination or central collective agreements, but pervades the existing institutions. Codetermination used to be seen as an institution that limits the influence of markets on work relations; now, codetermination is increasingly required to be a competitive institution itself (Mitbestimmungskommission 1998). The demarcation between market and society is in motion, and it is an increasingly difficult exercise to decide who embeds whom (see Polanyi 1997: 88–89).

Experts engage in much heated debate as to whether or not the changes in coordinated market economies can be interpreted as a process of convergence towards the Anglo-American production regime. This question would be easier to answer if the point of reference were not a whole political economy, but one economic sphere or industrial sector. As to the sphere of corporate governance in the largest companies, tendencies of convergence towards Anglo-American standards cannot be denied. In the industrial relations sphere, as discussed, the finding is more complex. We observe functional change in the context of stable institutions. Several authors avoid the term “convergence” and describe recent developments as “hybridization” (exogenous influences combined with path-dependent processes) of the political economy (Casper / Kettler 2000; Lane 2000; Jackson 2002; Vitols 2000). It is difficult to draw a clear dividing line between these concepts.

My thesis is that the refutation of the convergence concept is based on extremely solid criteria for convergence. One should note that in the 1950s, 1960s and 1970s, even more limited developments in much more divergent regimes were described as convergence processes. In his “Dix-huit leçons sur la société industrielle”, Raymond Aron (1964) argued that both western democracies and the Soviet Union were variants of industrial societies with convergent developments. John Kenneth Galbraith wrote that in eastern as well as in western companies, the power to make decisions was in the hands of organized experts who were not the owners of the firms. In both systems, the new economic elite was a “technostructure” that made the systems converge (Galbraith 1967: 76–88). The idea was not that one of the systems would collapse, but that they were characterized by far-reaching parallelisms. For the Dutch Nobel laureate Jan Tinbergen, conver-

gence meant a decrease in, not the disappearance of, the differences between the systems. He observed tendencies towards decentralization in the socialist economies, and a growing role of economic planning (in the context of Keynesianism) in the capitalist states (Tinbergen 1961, 1986). These concepts gained much influence among political economists of different leanings. Critics were either Liberals (Dahrendorf 1961: 23–26, 1992: 152–161) or Marxists (Meissner 1969; Rose 1970), who insisted on the fundamental differences between socialism and capitalism.

With such criteria of "convergence" in mind, it does not seem off-base to describe the current developments in coordinated market economies as a convergence process. Whether or not one likes the self-imposed semantic problem of convergence versus hybridization, a realistic description of recent trends nevertheless indicates that coordinated market economies are undergoing an unambiguous process of expanding market mechanisms.

Appendix

Table 1 Four Indicators of the Shareholder Orientation of Large German Companies in the Late 1990s

Company	Information quality of annual report	Investor relations	Implementation of profitability goals	Incentive compatibility of management compensation
Agiv AG	–0.63	–0.67	1	60
AVA AG	–0.40	–0.82	0	40
Axel Springer Verlag AG	–0.99	–2.24	0	–
BASF AG	0.50	0.96	1	80
Bayer AG	1.29	0.80	1	100
Beiersdorf AG	–0.39	–0.05	0	70
Bilfinger+Berger AG	–0.83	–1.37	0	30
BMW AG	–0.53	0.10	0	50
Buderus AG	0.68	0.37	0	50
Continental AG	0.52	0.63	0	60
Daimler–Benz AG	0.67	1.23	1	60
Degussa AG	0.24	–0.25	1	70
Deutsche Babcock AG	–0.69	–0.98	0	30
Deutsche Lufthansa AG	–0.07	1.04	0	70
Deutsche Telekom AG	0.61	0.82	0	50
Deutz AG	–1.40	–0.61	0	–
Henkel KgaA	1.02	0.68	1	70
Hoechst AG	1.24	0.39	1	80
Holzmann AG	–2.10	–1.59	0	–
Karstadt AG	–0.69	–1.44	0	30
Krupp AG	–0.22	0.64	1	30
Linde AG	–0.16	–0.46	1	60
MAN AG	0.47	0.16	1	40
Mannesmann AG	0.61	1.17	1	70
Metallgesellschaft AG	0.16	0.38	1	70
Metro AG	–0.25	0.18	0	20
Preussag AG	0.14	0.39	1	50
Rheinmetall AG	–1.18	–0.29	1	40
RWE AG	0.34	0.78	1	70
SAP AG	0.85	1.21	1	80
Schering AG	1.34	0.66	0	80
Siemens AG	0.11	0.44	1	80
Spar AG	–1.02	–0.45	0	10
Strabag AG	–2.79	–2.27	0	20
Südzucker AG	–0.62	–0.91	0	10
Thyssen AG	0.54	–0.09	1	30
VEBA AG	1.43	1.09	1	80
VEW AG	–0.02	–0.51	0	50
Viag AG	0.57	0.27	1	50
Volkswagen AG	0.48	–0.38	0	50

Note: Information quality of annual report, Investor relations: Data standardized by Z-transformation. Means for 1996, 1997, 1998 and 1999. Incentive compatibility of management compensation: scale from 0 (less incentive compatible) to 100 (very incentive compatible). Data for 1997. Implementation of profitability goals: 1=yes, 0=no. Data for autumn 1999.

Sources: Enzweiler / Friese / Nitschke (1997), Jahn / Prandl (1998), Enzweiler / Friese / Nitschke (1998), Luber / Nitschke (1999), Luber (2000), Fockenbrock (2000), annual reports, websites, calculations by the author.

Table 2 Correlation Matrix: Indicators for Shareholder Orientation

	Annual report	Investor relations	Compensation	Profitability goals
Annual report	1.00***	0.81***	0.69***	0.47***
Investor relations	0.81***	1.00***	0.67***	0.51***
Compensation	0.69***	0.67***	1.00***	0.48***
Profitability goals	0.47***	0.51***	0.48***	1.00***

Note: Pearson's r.
*** = significant at the 0.01 level.

Table 3 Index of Shareholder Orientation in the Late 1990s

Company	Score	Company	Score
Bayer AG	1.61	Deutsche Telekom AG	0.16
VEBA AG	1.48	Krupp AG	0.16
SAP AG	1.33	Buderus AG	0.04
Hoechst AG	1.20	Agiv AG	0.00
BASF AG	1.14	Beiersdorf AG	–0.17
Mannesmann AG	1.11	Volkswagen AG	–0.26
Henkel KgaA	1.09	Rheinmetall AG	–0.31
Daimler-Benz AG	1.02	BMW AG	–0.43
RWE AG	0.90	VEW AG	–0.46
Siemens AG	0.86	Metro AG	–0.70
Schering AG	0.74	AVA AG	–0.81
Metallgesellschaft AG	0.72	Deutsche Babcock AG	–1.08
Degussa AG	0.55	Deutz AG	–1.18
Viag AG	0.55	Karstadt AG	–1.23
Preussag AG	0.45	Bilfinger+Berger AG	–1.25
MAN AG	0.36	Spar AG	–1.28
Deutsche Lufthansa AG	0.28	Südzucker AG	–1.30
Linde AG	0.22	Axel Springer Verlag AG	–1.70
Continental AG	0.21	Holzmann AG	–1.90
Thyssen AG	0.17	Strabag AG	–2.29

Note: Data combined by summing up z-transformed scales.

Sources: See Table 1.

Table 4 Characteristics of Individual and Institutional Investors

	Individual investors	**Institutional investors**
Invested capital	low	high
Performance orientation	low	high
Capacity to collect and interpret information	not professional	professional
Loyalty	possible	low
Duration of investment	long	short

Source: Kirchhoff (2000: 42).

Table 5 Development of Board Member Compensation in Large German Companies between 1996 and 1999

Company	**Compensation for whole board** (millions of DM)		**Size of board**		**Average board member compensation** (millions of DM)		**Growth in compensation per member** (%)
	in 1996	in 1999	in 1996	in 1999	in 1996	in 1999	1996–1999
Agiv AG	2.36	13.20	3	5	0.79	2.64	+235.7
AVA AG	1.65	7.83	3	3	0.55	2.61	+374.4
Axel Springer Verlag AG	5.96	12.36	4	6	1.49	2.06	+38.3
BASF AG	19.20	18.03	11	9	1.75	2.00	+14.8
Bayer AG	15.01	16.11	8	8	1.88	2.01	+7.3
Beiersdorf AG	5.79	7.25	6	6	0.97	1.21	+25.3
Bilfinger+Berger AG	7.68	4.90	7	4	1.10	1.23	+11.8
BMW AG	13.80	14.11	7	8	1.97	1.76	–10.5
Buderus AG	2.66	3.51	4	4	0.67	0.88	+32.0
Continental AG	8.37	10.16	5	6	1.67	1.69	+1.2
Daimler-Benz AG	14.00	103.10	10	13	1.40	7.93	+466.5
Degussa AG	8.70	18.03	6	11	1.45	1.64	+13.1
Deutsche Babcock AG	3.21	–	3	–	1.07	–	–
Deutsche Lufthansa AG	4.30	4.10	6	4	0.72	1.03	+42.9
Deutsche Telekom AG	10.35	14.87	8	8	1.29	1.86	+43.6
Deutz AG	2.01	3.17	3	4	0.67	0.79	+18.5
Henkel KgaA	13.03	16.77	9	8	1.45	2.10	+44.8
Hoechst AG	13.76	–	9	8	1.53	–	–

Holzmann AG	3.49	5.56	6	5	0.58	1.11	+91.1
Karstadt AG	8.69	12.76	7	7	1.24	1.82	+46.8
Krupp AG	7.80	17.64	5	9	1.56	1.96[a]	+25.6[a]
Linde AG	8.39	–	7	–	1.20	–	–
MAN AG	8.27	9.43	8	8	1.03	1.18	+14.1
Mannesmann AG	11.18	19.64	7	6	1.60	3.27	+105.0
Metallgesellschaft AG	8.10	–	5	–	1.62	–	–
Metro AG	15.61	11.85	6	5	2.60	2.37	–8.9
Preussag AG	9.24	10.10	8	6	1.16	1.68	+45.7
Rheinmetall AG	1.68	2.45	6	5	0.28	0.49	+75.2
RWE AG	7.73	7.33	11	5	0.70	1.47	+108.5
SAP AG	7.51	10.84	8	5	0.94	2.17	+130.9
Schering AG	7.58	12.85	5	5	1.52	2.57	+69.6
Siemens AG	20.50	42.53	13	11	1.58	3.87	+145.2
Spar AG	2.72	2.15	3	3	0.91	0.72	–21.1
Strabag AG	3.83	2.85	6	3	0.64	0.95	+48.9
Südzucker AG	3.75	4.31	5	5	0.75	0.86	+15.0
Thyssen AG	11.50	17.64	7	9	1.64	1.96[a]	+19.3[a]
VEBA AG	16.90	18.82	9	9	1.88	2.09	+11.3
VEW AG	3.25	4.92	3	4	1.08	1.23	+13.7
Viag AG	5.49	7.00	4	5	1.37	1.40	+2.1
Volkswagen AG	13.22	16.82	7	5	1.89	3.36	+78.2

a Thyssen-Krupp.

Sources: Annual reports.

Table 6 Selected Results of the MPIfG Works Councils Survey

Question	Average score	Correlation to shareholder value[a]
If the company changed accounting practice to international standards (IAS or US-GAAP): Did the works council agree with that? (1=no; 2=indifferent; 3=yes)	2.81	r=.38
If the company is increasingly focussing on core competencies: Does the works council agree with that? (1=no; 2=partially; 3=yes)	2.05	r=–.51**
If the company has implementetd a profitability goal for the company as a whole: Did the works council support the implementation? (1=no; 2=partially; 3=yes)	1.61	r=–.61***
If the company has implemented profitability goals for the company units (segments): Did the works council support the implementation? (1=no; 2=partially; 3=yes)	1.71	r=–.66***
If top management compensation was increasingly coupled to financial success: Did the works council disagree with that? (0=no; 1=yes)	0.25	r=.07
If the company has made substantial foreign investments in recent years: Did employees on the supervisory board vote for these investments? (1=no, in most cases not; 2=yes, in most cases; 3=yes, always)	2.61	r=.23
What is the works council's opinion upon dividends in recent years? (1=dividends were too low; 2=dividends were adequate; 3=dividends were too high)	2.20	r=–.14

a Pearson's r between survey responses and the shareholder value index (see Table 3).

* = significant at the 0.1 level
** = significant at the 0.05 level
*** = significant at the 0.01 level

In the MPIfG works councils survey, questionnaires were sent to the works councils of the 111 largest German corporations. 77 responded (69 percent). For this table, all of the councils from companies that are not listed or are in the financial sector were excluded. The table is thus based on 24 of the 40 largest listed non-financial corporations.

Overview 1 Multiple Regression

Dependent variable: Shareholder Orientation Index

Independent variables: Exposure to International Product Markets (EXPOSED)
Part of Institutional Investors in Ownership Structure (INSTIT)

Model Summary

Model	R	R square	Adjusted R square	Standard error of the estimate
1	.807	.651	.625	.6179

ANOVA[b]

Model	Sum of squares	Degrees of freedom	Mean square	F	Significance
Regression	19.247	2	9.623	25.204	.000
Residual	10.309	27	.382		
Total	29.556	29			

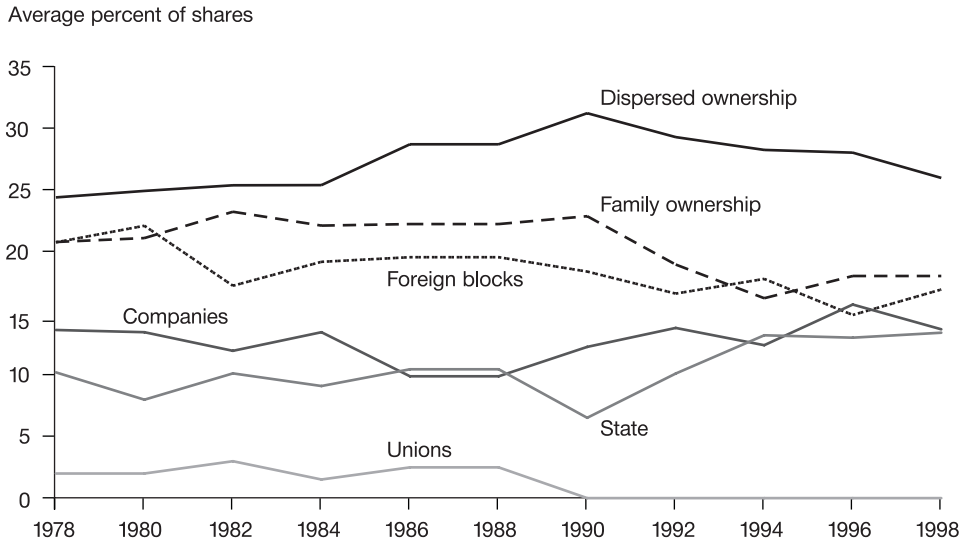
Coefficients

Model	Unstandardized coefficients		Standardized coefficients		
	B	Standard error	Beta	t	Significance
(Constant)	–1.862	.306		–6.093	.000
INSTIT	1.85E-02	.006	.397	3.194	.004
EXPOSED	1.489	.331	.559	4.494	.000

Software: SPSS

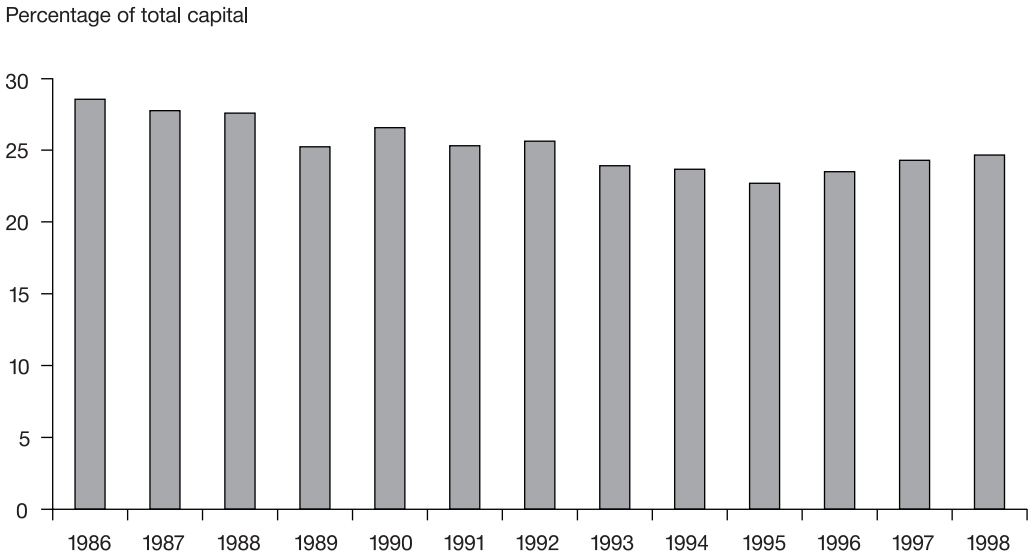
Note: The results remain the same under statistical control of company size (net value added), which turns out to be an insignificant predictor.

Figure 1 Ownership Structures of the 100 Largest German Corporations, 1978–1998



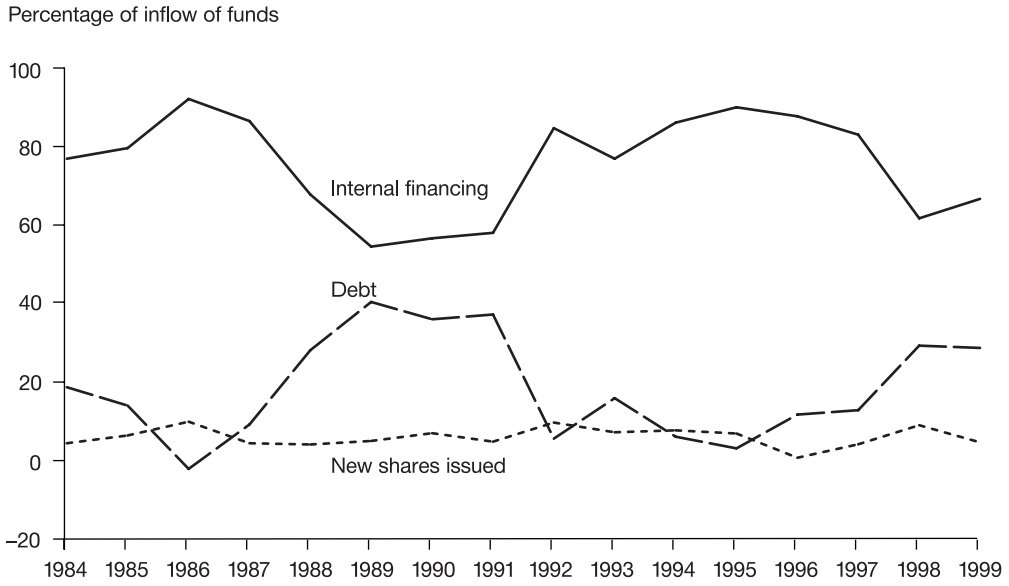
Sources: Several publications of the Monopolkommission.

Figure 2 Average Ratios of Equity Capital, 40 Corporations, 1986–1998



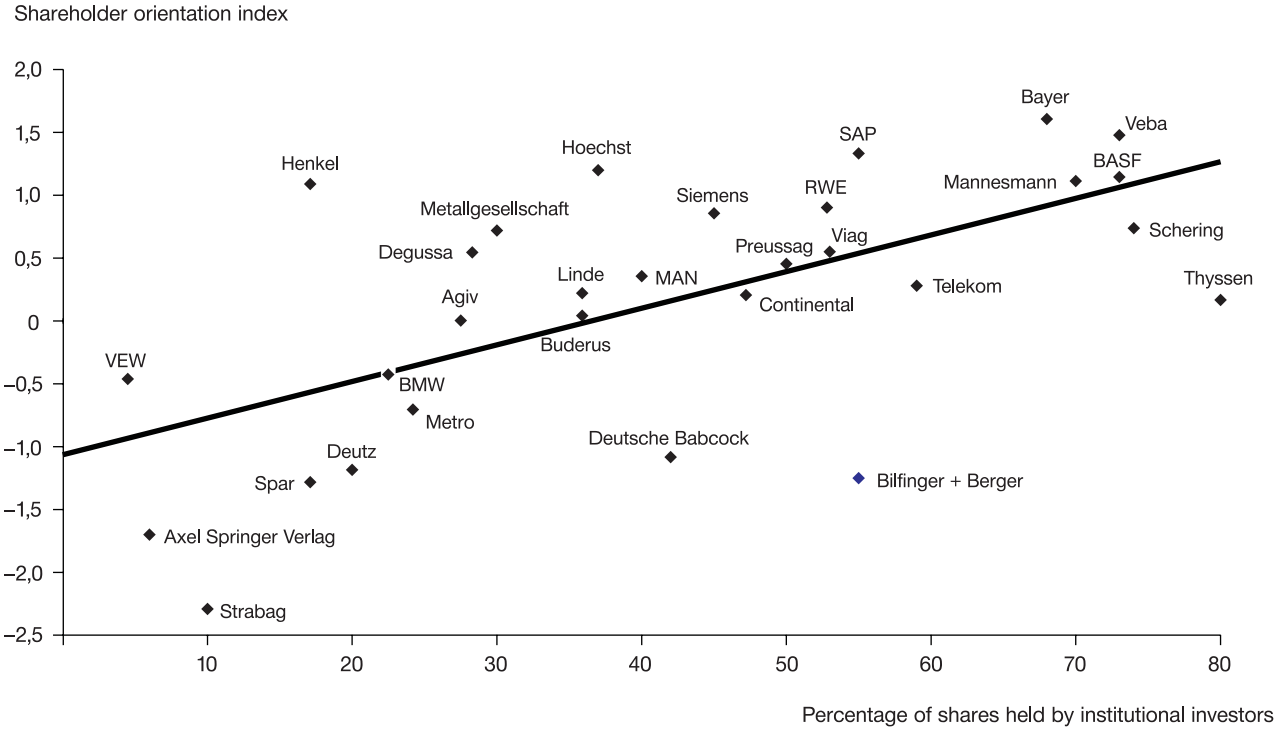
Source: Hoppenstedt Bilanzdatenbank.

Figure 3 Sources of New Finance of All German Corporations, 1984–1999



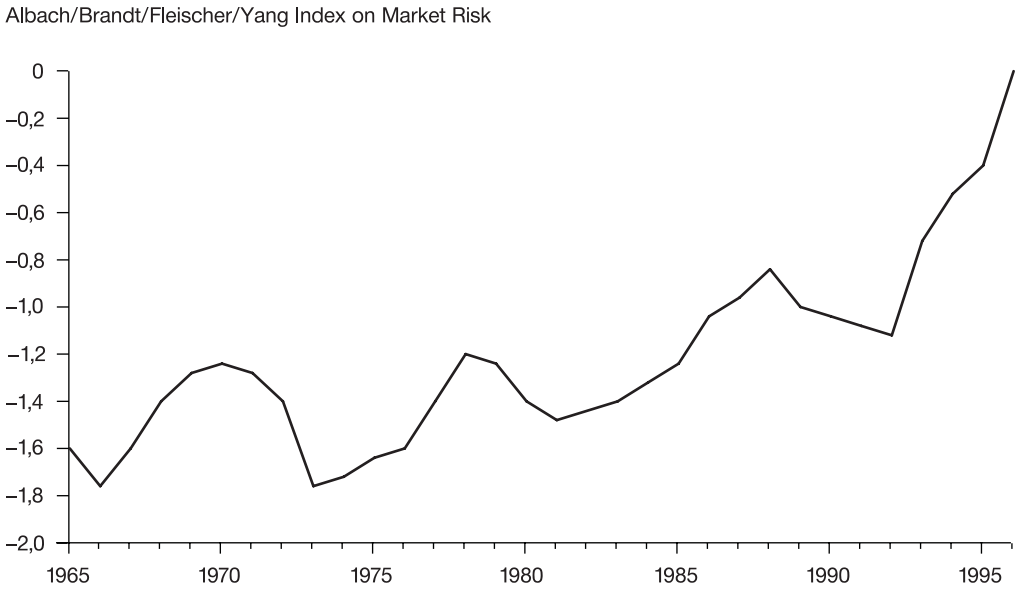
Sources: Deutsche Bundesbank (1999: 139, 2001: 29); calculations by the author.

Figure 4 Institutional Investors and Shareholder Orientation, 30 Corporations, Late 1990s



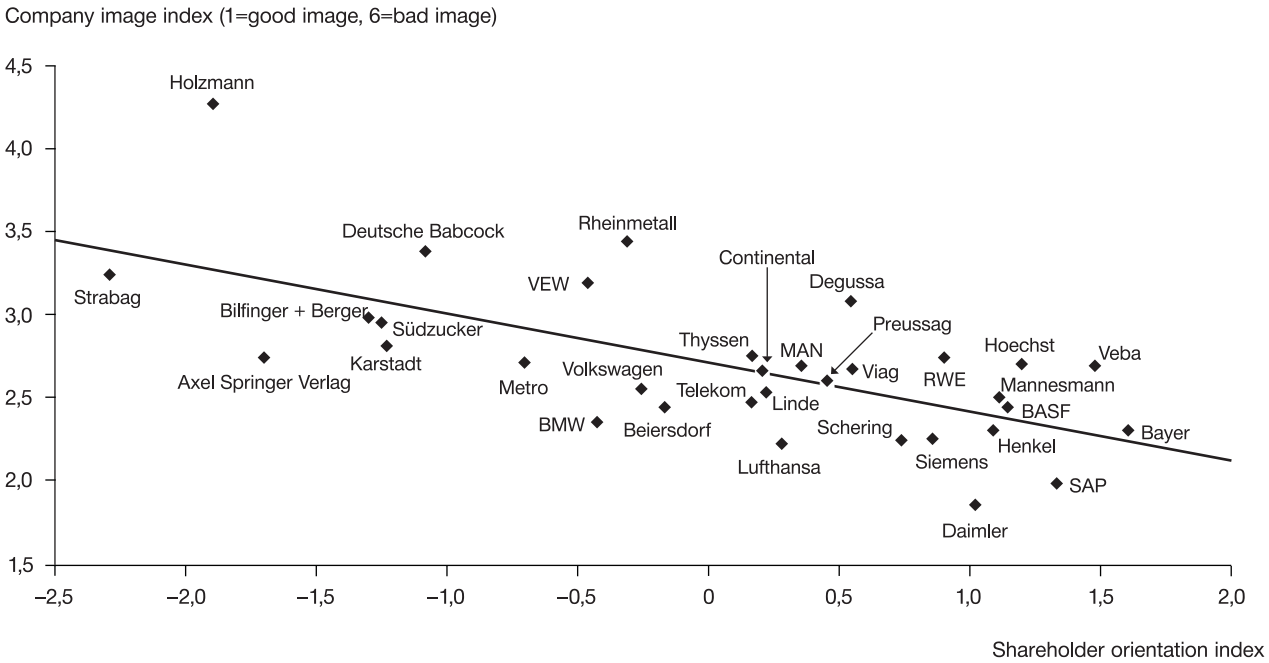
Sources: Annual reports, websites, newspapers, investor relations departments.

Figure 5 Development of Market Risk, Listed German Corporations, 1965–1996



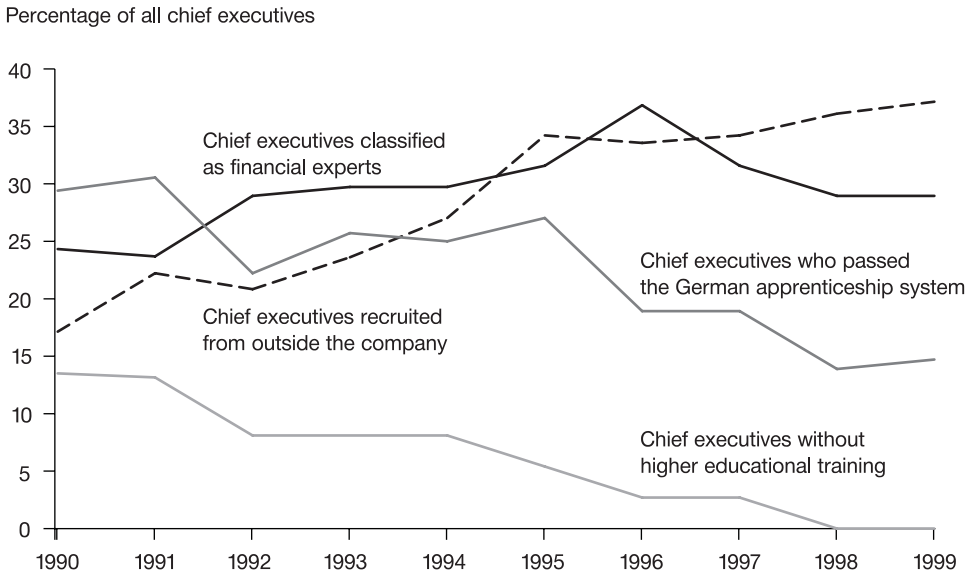
Source: Albach et al. (1999: 515).

Figure 6 Shareholder Orientation and Company Image in the Late 1990s, 33 Corporations



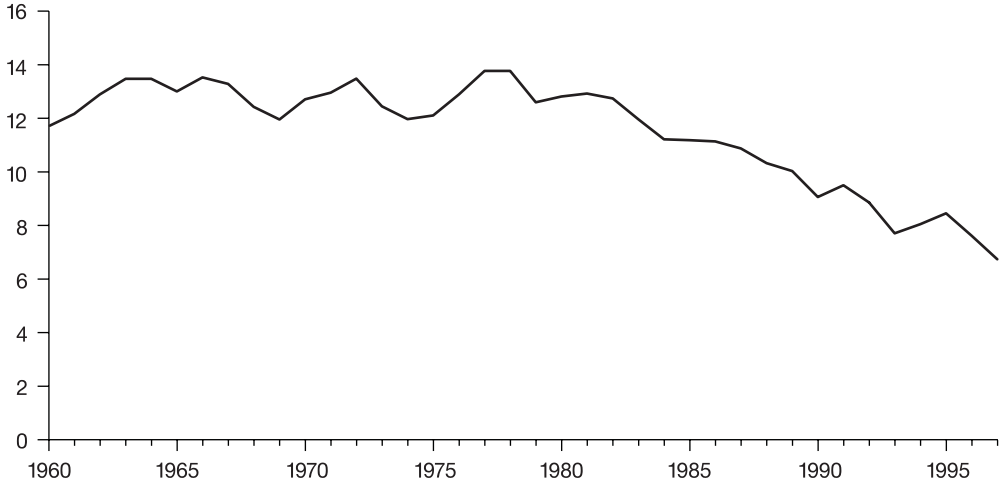
Sources: Shareholder orientation: see Table 3; company image: Wirtschaftswoche 23/2000, 102–105.

Figure 7 Careers of Chief Executives, Selected Indicators, 40 Corporations, 1990–1999



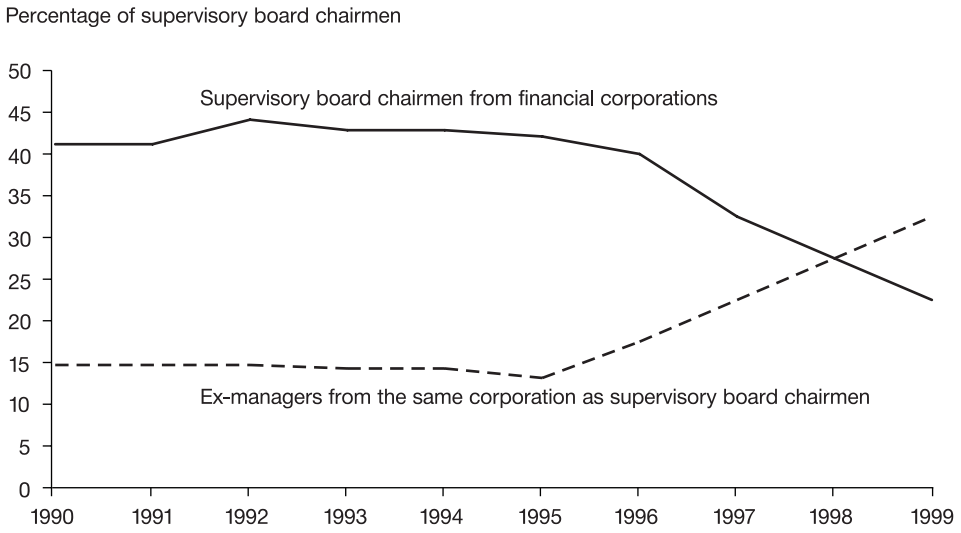
Note: The sample of chief executives changes from year to year.
Sources: Annual reports, Munzinger Archiv, websites, newspapers.

Figure 8 Average Years in Office of Chief Executives, 40 Corporations, 1960–1997



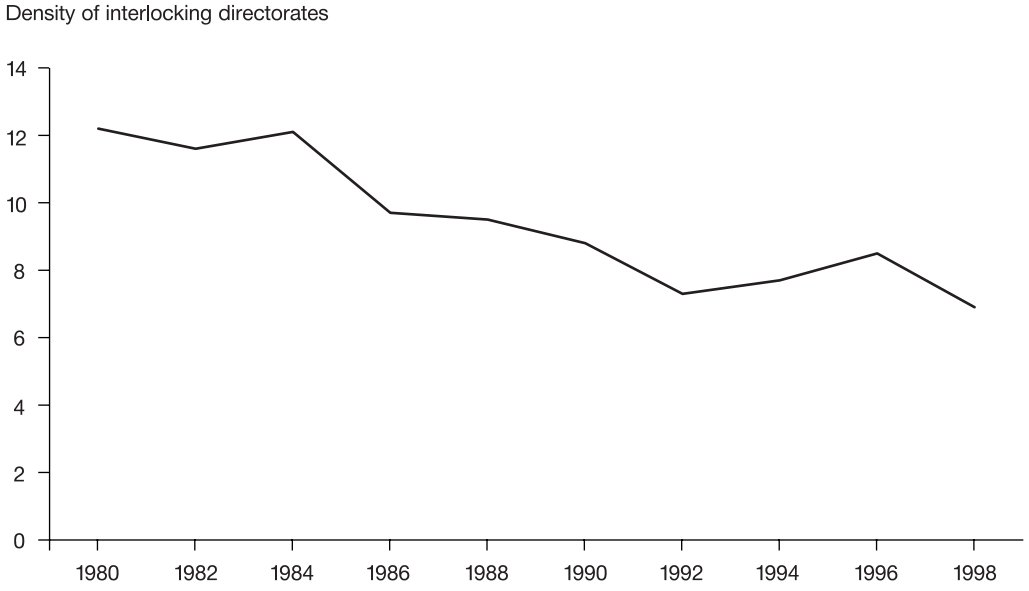
Note: The sample of chief executives changes from year to year.
Sources: Annual reports, Munzinger Archiv, websites, newspapers.

Figure 9 Backgrounds of Supervisory Board Chairmen: Representatives of Financial Companies and Former Employees, 40 Corporations, 1990–1999



Sources: Annual reports, Munzinger Archiv, websites, newspapers.

Figure 10 Density of Interlocking Directorates, 100 Largest German Corporations, 1980–1998



Note: The index is defined as actual interlocking directorates as a percentage of all mathematically possible interlocking directorates.
Sources: Several publications of the Monopolkommission.

Figure 11 Three Types of Coalitions and Conflicts between Shareholders, Employees, and Management

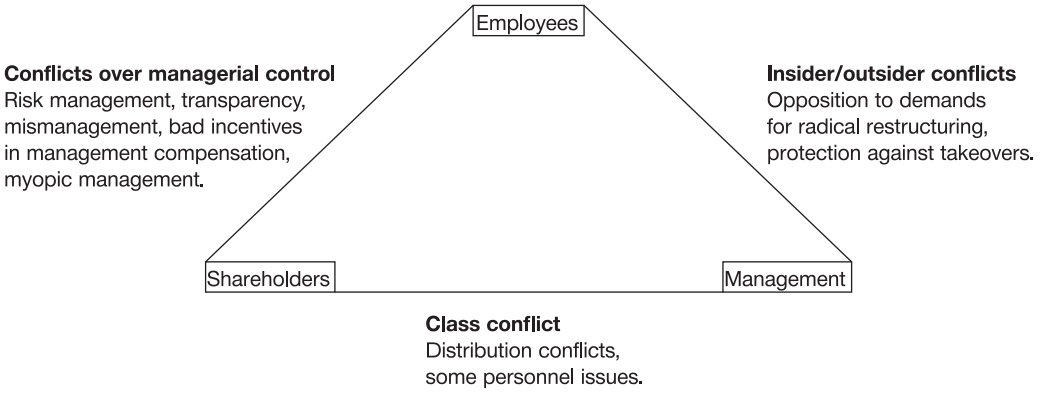
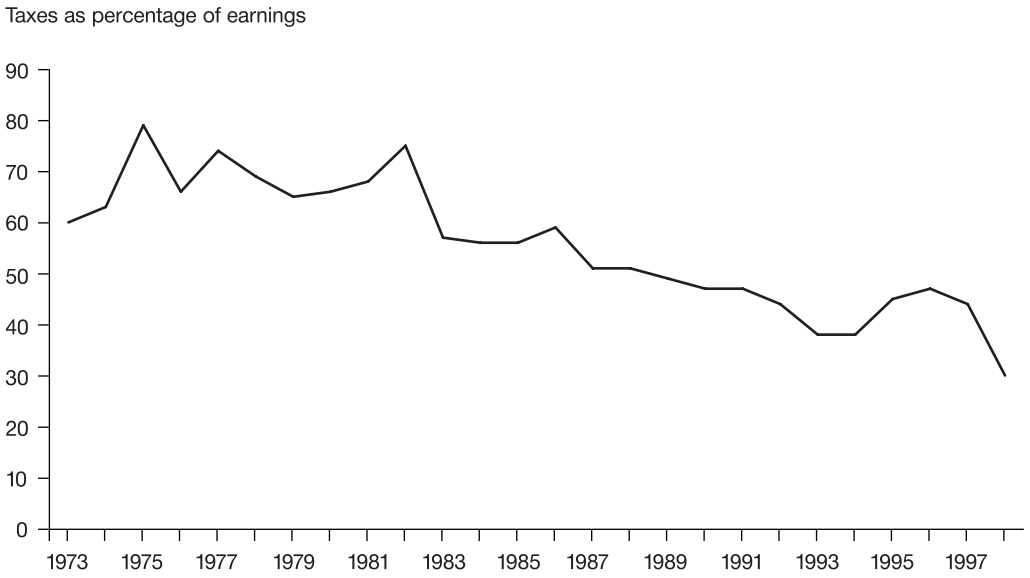


Figure 12 Tax Ratio of Hoechst (Worldwide), 1973–1998



Source: Eckert (2000: 132).

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