



University of Navarra

BANKS AS SHAREHOLDERS:
DO THEY MATTER?

Jordi Canals*

RESEARCH PAPER N° 354
January, 1998

* Professor of Economic Analysis for Management, IESE

Research Division
IESE
University of Navarra
Av. Pearson, 21
08034 Barcelona - Spain

Copyright © 1998, IESE
Do not quote or reproduce without permission

BANKS AS SHAREHOLDERS: DO THEY MATTER?*

Abstract

Bank-industry relationships are a widespread organizational arrangement. In some countries, such relationships are the outcome of banks' financial support of non-financial firms to speed up the industrialisation process. Nowadays, they have become important as a result of the effort large banks are putting into their diversification process, as they move away from more traditional banking activities towards other businesses.

The purpose of this paper is twofold: first, to present a typology of banks and their strategies as shareholders in non-financial firms; and second, to discuss how and why bank-industry relationships affect firms' performance. We explore the specific chains of causality from bank ownership to non-financial firms. The factors that seem to have the strongest influence on firms' performance are the structure and functions of the board of directors and the banks' corporate strategy.

* Paper prepared for the Strategic Management Society Conference, Barcelona, October, 1997.

BANKS AS SHAREHOLDERS: DO THEY MATTER?

1. Introduction

The corporate restructuring of the early 1990s has spawned a great deal of interest in the subject of corporate governance. In the U.S., the revolt of shareholders on corporate boards and the threat of hostile takeovers are among the dominant mechanisms of corporate governance when it comes to turning companies around, replacing CEOs in underperforming companies and improving corporate efficiency.

In contrast, in Europe (except Britain) the mechanisms are different. The role of shareholders and capital markets is less pivotal than in the U.S. In continental Europe, a small number of large shareholders tend to have the upper hand in monitoring firms; they control the board of directors and appoint the CEO. Some of these shareholders are banks that have diversified their activities and entered non-bank activities.

Deutsche Bank, Commerzbank and Dresdner Bank in Germany (see Table 1), Société Générale in Belgium, Crédit Lyonnais and Indosuez in France, and Banco Bilbao Vizcaya and Banco Central Hispano in Spain are examples of banks that are involved in industrial firms as shareholders, above and beyond their function as lenders.

Table 1
Germany: Large banks' shareholdings (1994-1995)

	<i>(In % of total capital)</i>
Deutsche Bank	
Daimler-Benz (Automobiles, aeronautics, electrotechnical)	24.4
Philip Holzmann (Real estate)	25.9
Karstadt (Distribution)	10
Horten (Distribution)	25
Klöckner-Humboldt-Deutz (Machinery)	38
Linde (Mechanics)	10
Südzucker (Foods)	12.8
Hapag-Lloyd (Tourism)	10
Continental (Tires)	10.5
Metallgesellschaft (Metal)	10.6
Allianz (Insurance)	10
Münchener Rück (Insurance)	10
Dresdner Bank	
Bilfinger-Berger (Public works)	25
Brau & Brunnen (Restaurants)	25.6
Frankfurter Gesellschaft für Chemiewerte (Chemical group)	20
Heidelberg Zement (Cement)	24
Hapag-Lloyd (Tourism)	10
Metallgesellschaft (Metals)	12.6
Allianz (Insurance)	10
AMB (Insurance)	13.7
Münchener Rück (Insurance)	10.1
Commerzbank	
Karstadt (Distribution)	10
Linde (Mechanics)	10.3
Hochtief (Public works)	2.5
Thyssen (Steel)	5
DSD Dillinger (Steel)	30
MAN (Mechanics)	6.3
Heidelberg Druckmaschinen (Mechanics)	13.8
Kinotype-Hell (Mechanics)	6.7
Salamander (Footwear)	10.9

Source: Annual Reports

Investment by banks in non-financial companies over the past two centuries has been driven by several factors: the tradition of ownership concentration, sometimes in the hands of a few families, assisted by the lack of legal restrictions on such concentration of power; the late arrival of the first stages of the industrial revolution, which gave banks and the public sector a more important role in catching up with the industrial revolution in Britain; and finally, liberal laws that allowed banks to own non-bank companies irrespective of the growing concentration of risk they were assuming.

The differences between the U.S. system and the European system have led to the definition of two contrasting financial models (see Table 2). The first is the capital market-based model, the paradigm of which is the U.S. model. Its features include a low presence of banks in financing non-bank firms, the dominant role of capital markets in corporate finance, the disciplinary role of the stock market and hostile takeovers, and a low ownership concentration.

Model	Countries	Banks as financial intermediaries	Banks as lenders to companies	Banks as shareholders	Banks as strategic shareholders	Banks as managers
I. Bank-based model						
1. Specialised banks	United States Britain	Yes	No	No	No	No
2. Main bank	Germany Japan	Yes	Yes	No	No	No
3. Universal bank	Germany Spain France Italy	Yes	Yes	Yes	No	Yes
4. Conglomerate groups	Germany Japan Spain	Yes	Yes	Yes	Yes	Yes
II. Market-based model						
	United States Britain	Yes	No	No	No	No

Source: Canals (1997).

The second model is the bank-based system. In this model, banks play a decisive role in financing firms, and are shareholders of non-financial firms; corporate ownership is more concentrated; capital markets are narrower and have less liquidity; and hostile takeovers are not widely used. Germany, France and Spain, in Europe, and in Asia, Japan, are examples of countries dominated by the bank-based model.

Nevertheless, these two models cover different situations. Thus, among the bank-based models, it is crucial to distinguish between the countries in which governments have traditionally played a leading role in creating bank-industry groups, as in France or Japan, and the countries in which the role of government in this respect has been more modest, as in Germany or Spain. Another differentiating factor is the key role of the main bank in Germany (the “Hausbank”) and Japan.

The two different financial models give rise to different systems of corporate governance. The market-based model relies on solutions provided by the discipline of the stock market and the interests of the majority of shareholders. The bank-based model seems to rely more on the personal dealings between banks –which are shareholders– and CEOs. This is the reason why this system is also known as the relationship-based system.

This paper focuses on evaluating the bank-based model as a system of corporate governance, looking specifically at one of the dimensions involved: bank ownership and the effect it has on firms’ performance. Does bank ownership have any effect on corporate performance?

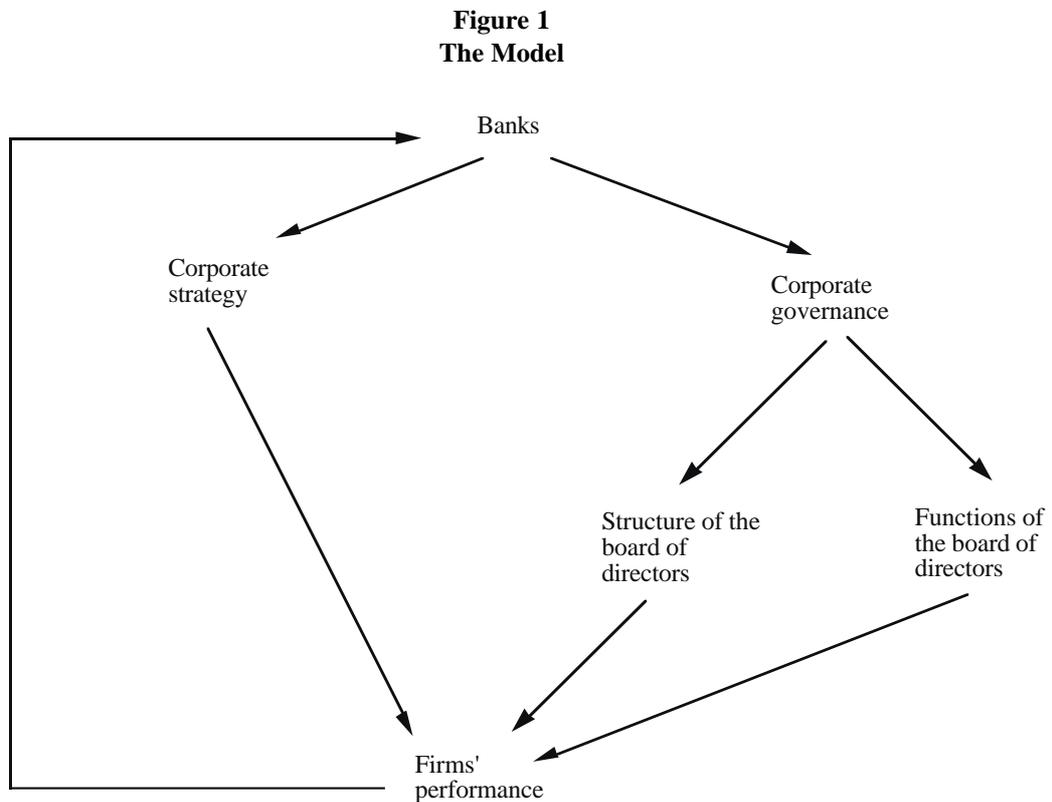
There are a few research papers that have addressed this question in the past, most notably Cable (1985), Hoshi, Kashyap and Scharfstein (1991), and Gorton and Schmid (1996), among others. Most of these papers look at the relationship between bank ownership and performance, but the focus is on whether that relationship actually exists, not on the specific mechanisms whereby banks could have an impact on firms’ economic performance.

This paper aims to provide a framework for understanding these mechanisms and, in general, the causal relationships between bank ownership and corporate performance. We have studied the role of five leading banks in three countries with a bank-based model in order to generate some new hypotheses and develop a more comprehensive framework. The banks we have studied are: Banco Bilbao Vizcaya (Spain), Banco Central Hispano (Spain), La Caixa (Spain), Crédit Lyonnais (France) and Deutsche Bank (Germany). They are the banks with the largest industrial shareholdings in their respective countries.

There are two main reasons for reconsidering the research agenda regarding the effects of bank ownership on firm performance. The first is the renewal of interest in Corporate Strategy in the past few years (Campbell, Goold and Alexander, 1994; Collis and Montgomery, 1997) as a result of the integration of the resource-based theory of the firm and the Organizational Economics approach, in an effort to explain certain phenomena within large diversified corporations. One way to approach the study of large banks with industrial shareholdings is to consider them as diversified corporations with a number of different business units. When one looks at these banks from the point of view of corporate strategy, the picture one gets is very different from the traditional one. This perspective has implications both for the way banks manage their industrial shareholdings and for firms’ performance.

The second reason is the growing empirical evidence regarding the influence that the structure and functions of the board of directors can have on firms’ economic performance. In general, it seems that corporate governance does matter. By integrating some of the

hypotheses generated in this area in the past few years, we may shed new light on the effects of banks as shareholders. Figure 1 shows the relationships among the variables of the model that we shall be presenting in this paper.



The outline of this paper is as follows: In sections 2 and 3 we discuss the major features of the market-based and bank-based financial models in greater detail, with special reference to Germany.

In Section 4 we present a general typology of banks in their role as shareholders, and of their strategies.

In Section 5 we discuss how to approach and measure the link between ownership and firms' performance and present an alternative point of view on this subject.

In the following two sections we develop our main hypotheses. In Section 6 we discuss the role of corporate governance and formulate a number of hypotheses regarding the way banks that have a presence on a firm's board may influence that firm's strategy and, as a result, have an impact on its economic performance.

In Section 7 we consider banks that own non-bank firms as corporate groups with a corporate strategy. We discuss the concept of corporate strategy for such groups and the implications for financial performance. In Section 8 we discuss the effects of bank ownership on banks' performance. In Section 9 we give some of the conclusions.

2. The capital market-based model

The clearest examples of financial systems based on capital markets are those of the U.S. and the United Kingdom. They have very distinctive features. The first is that companies raise financial resources on the capital markets instead of relying on banks.

Second, there is a virtually complete separation between investors operating on capital markets, and firms. The investors play no part in managing firms. The only influence they have derives from the markets' assessment of the company's business decisions and performance (which may be more or less accurate, as the case may be).

Third, market-based systems offer a constant valuation of the various instruments by means of price mechanisms, providing invaluable help in improving the allocation of financial resources between alternative projects competing for the same financing.

Fourth, capital markets separate the risks of one financial asset from that of all other financial assets, so that the investor knows at any given time exactly where the risk is located and how much of it he is bearing, unlike in the bank intermediation systems, where the bank takes on the entire risk vis-à-vis its asset customers. Consequently, capital market-based systems, in principle, enable a more efficient diversification of resources; they also allow the risk borne by investors to be spread much more widely.

Alongside these advantages, the system based on capital markets has a number of disadvantages, which we describe below. The first is the difficulty of monitoring and supervising companies, owing to the fragmentation of ownership and, hence, of responsibility for this task.

When none of the shareholders are clearly involved in the company –due to the complete separation between capital markets and company– the “free rider” problem may arise: no single shareholder is large enough to be concerned about adequately supervising the quality of the company's management. In such situations, the shareholders are unlikely to detect potential problems.

It is true that financial intermediaries operating on capital markets try to provide ongoing information about what is happening inside companies. However, this information may be incomplete, insufficient or out of date, as the intermediaries do not always know what is really going on inside any given company, or else they may have information that is at odds with the information in the hands of the company's managers (Myers and Majluf, 1984).

In addition to this problem, capital markets are also affected by agency problems, that is to say, delegation problems between shareholders or bondholders –the principals– and the company's managers –the agents. Agency problems arise in situations where there is asymmetric information, i.e. where certain information is available to one of the parties but not to the other.

Agency problems can be partly solved by incentives that help prevent inappropriate behaviour in using this information, such as a management compensation scheme that takes into account annual financial performance over a period of three years, market share, and other such variables.

However, no matter how sophisticated the incentives are, all of these design variables obviously have advantages and disadvantages and none will ever be precisely

targeted enough to unfailingly induce a particular type of behaviour (Milgrom and Roberts, 1992).

Nevertheless, the evidence from the U.S. and the United Kingdom shows that financial markets enjoy important advantages in terms of raising capital, spreading information and allocating resources. We shall now weigh these advantages against those of the bank-based model.

3. The bank-based model

This model basically rests on the financial intermediation carried out by banks. This process is the main mechanism for allocating financial resources from savings into investment. The role played by financial markets in this model is less important.

The bank-based model is not uniform but allows for a great number of possibilities. The first is where banks play a major role in the industrial sector, as in Germany, France or Spain. The second consists of those countries in which the share of banks in total corporate financing is high, but consists mainly of short or long-term financing in the form of loans or credits, not of large holdings in companies' equity. The prototype of this variant would be Japan.

Bank intermediation may offer significant advantages, as it mitigates information problems between companies and investors. In fact, when the cost to the providers of financial resources of acquiring information on companies is high, the process of financing companies may be done more efficiently if the prospective investors delegate the task of obtaining this information to a specialized organization (Diamond, 1984). Therefore, financial intermediation can be justified on the grounds of the information collection and company monitoring functions performed by the banks.

The delegation of this function to banks offers significant advantages, owing to the scale economies involved: information collection and company monitoring are associated with substantial fixed costs, which can be absorbed by a greater volume of operations. Thus, banks may have a portfolio of loans whose respective returns do not correlate with each other at any one time. The main prerequisite for this to happen is the existence of true competition between the various financial institutions, so that the cost of the financing does not include monopoly income. Therefore, the presence of financial intermediaries provides significant incentives that allow many of the above-mentioned agency problems to be solved. This argument is useful, but it should not be taken to extremes: if it were universally valid, companies would operate with only one financial organization, which is not the case in real life (Hellwig, 1991).

Another advantage of bank-based financial systems is that there is a major shareholder –the bank itself– which, as owner of the company, is interested in its performance (Jensen, 1989; Berglöf, 1990). Bank shareholding is a way of aligning the investors' interests with the firm's performance. The large shareholder may influence the company's development –by appointing its senior managers, for example.

The relationship with the management team also enables the major shareholder to mitigate the asymmetric information problems mentioned earlier. In general, for the reasons we have stated above, banks are able to exercise control over companies at a lower cost.

Consequently, in a context of asymmetric information and incomplete contracts, banks may exercise control over a company more efficiently than financial markets, putting pressure on management or even firing managers (Shleifer and Vishny, 1986)

The bank-based model also has its problems and limitations. The first and most important is the excessive risk accumulated by the banks (Demsetz and Lehn, 1985). These holdings have been the cause of many banking crises, such as the U.S. crisis of the 1930s, or the Spanish crisis of the 1970s and 1980s. The recent cases of Cr dit Lyonnais and Banesto illustrate these problems.

A second limitation of the bank-based model is that control mechanisms are no longer based on the prices set by the market for certain financial assets but on the bank's ability to supervise the companies with which it has commercial and financial relations. Obviously, this requires a much greater effort on the part of the main shareholder or, in the case of a bank, the main shareholder and/or creditor.

Third, the absence of stricter disciplining mechanisms like those provided by capital markets may lead some companies to become complacent. This is particularly true in cases where the products offered by the company are not subject to market discipline. However, if there is a high degree of rivalry in the industry the company is operating in, this risk is lower.

Another problem is that large shareholders may try to put their own interests first, before those of the other stakeholders. This divergence of interests may lead to a wealth redistribution process and a potential abuse of minority shareholders (Grossman and Hart, 1988). In the case of Japanese banks, Weinstein and Yafeh (1994) show that Japanese firms that are controlled by banks pay higher financial expenses

The model based on bank intermediation has achieved good results in countries such as Japan or Germany, both in terms of high investment and in terms of social stability. This success has led some authors (Kester, 1992; Porter, 1992) to argue that capital market-based systems should gradually incorporate features of the bank-based system in order to maintain high investment rates and increase corporate competitiveness. Nevertheless, the evidence of the recent corporate crises in Germany and France suggests a need for caution before jumping to any such conclusion.

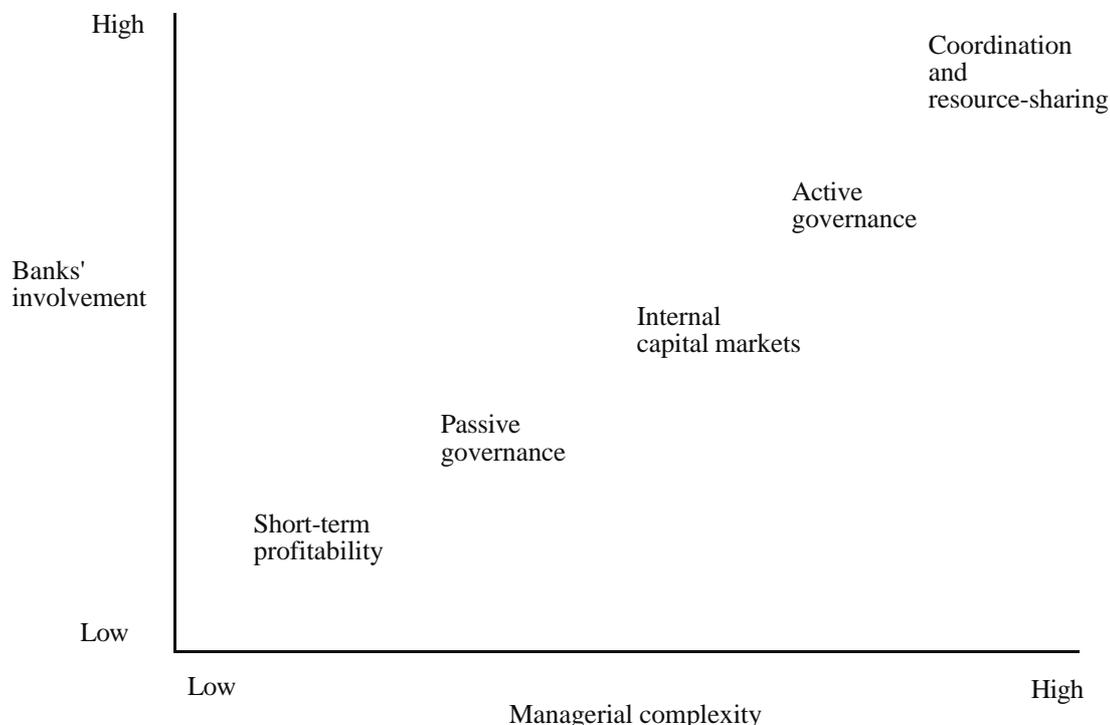
4. A typology of bank-firm relationships

As we have discussed in the previous section, the nature, goals and main features of the relationships between banks and non-financial firms vary across countries, industries and banks. In this section, we shall first define five different contexts for bank-firm relationships. After that, we shall present a typology of bank-firm relationships that takes into account the origin, objectives and evolution of banks' shareholdings.

4.1. Different contexts of bank-firm relationships

Figure 2 summarizes, from a theoretical viewpoint, the different degrees of bank involvement in the companies they have a stake in, combining the extent of a bank's commitment to a firm with the level of managerial complexity for the bank. From this perspective, we can define five different contexts for bank-firm relationships.

Figure 2
Different contexts of bank-firm relationships



The first context is defined by the objective of short-term profitability. In this case, banks are looking exclusively for financial performance, either in the form of the dividends the owned firm will pay its shareholders, or in the form of capital gains deriving from a revaluation of the firm's shares.

The second context is defined by the presence of the bank on the board of directors in a way that could be called passive governance. As a shareholder, the bank has a right to appoint representatives to the board of directors that supervises the firm's operations, budget and investments, without getting involved in its management.

The third context is the creation and management of an internal capital market between the bank and the firms it has a stake in. In this case, the bank plays the role of the capital markets, allocating resources to the different firms, but without getting involved in their management.

The fourth context, which we shall call active governance, is defined by the active presence of the bank on the firm's board. By active presence we mean that the board has a key responsibility for supervising the firm's management, helping to define its strategy, appointing its CEO and Executive Committee, and acting to enhance the firm's value.

The fifth context is defined by the coordination of certain activities between the bank and the firms. These activities go beyond establishing an internal capital market to encompass other activities, such as sharing the same brand name at group level, transferring management practices from one firm to another within the group, sharing information technologies, or establishing staff recruitment and promotion policies at group level.

Each context, as we can see from this brief description, involves different levels of commitment and different types of management, each with certain advantages and disadvantages. It is difficult to claim that any one of these contexts is superior to any other. Some banks are very successful running the firms they own as members of a corporate group, while others have been real failures. In the next section, we shall go further into the analysis of these relationships.

4.2. Models of bank-industry relationships

When one considers the focus and objectives of banks that own non-financial firms, it is possible to distinguish two types. The first is the profitability of the firm itself, as an indicator of the potential profit accruing to the bank as a result of its investment.

The second objective is the profitability of the business group as a whole. This includes not only the profitability of the firm itself, but also the benefits that accrue to the business group as a result of having the firm as one of its members.

Examples of such benefits include the sharing of financial resources and the establishment of an internal capital market, the transfer of resources and capabilities between the firm and other members of the group, and the coordination of other managerial activities within the group.

On the other hand, the time horizon in which the bank views its investment in the group could be the long term or the short term. Depending on this perspective, the investment may be managed in different ways.

The matrix shown in Table 3 combines these two variables –banks’ objectives and banks’ time horizons– to offer four different models of the bank-industry relationship.

		Banks' time horizon	
		Short-term	Long-term
Banks' focus	The firm	Independence	Supervision
	The group	Portfolio	Network

4.2.a. The independence model

The main feature of this model is the complete separation and independence of banks and firms. Banks look exclusively for financial profitability and approach their investments in non-financial firms from this perspective.

The time horizon of this perspective tends to be rather short. The reason is that banks are not looking for synergies or other types of advantage that may need some time to develop. If the financial performance happens to be good when an opportunity for selling the investment with a price revaluation arise, the bank will probably sell, irrespective of any other consideration.

The strategy of Banco Santander fits this model well. Its investments in non-financial firms –such as Airtel or British Telecom, in the telecommunications industry– and financial firms alike –such as its recent divestiture of First Union– clearly follow this pattern.

In this model, the bank acts as a shrewd and knowledgeable investor that uses its resources to buy and sell shares of companies that offer some potential for exceptional returns. The drawback of this strategy is that the bank may get loaded with volatile stocks.

The managerial outcome of this model is the complete independence of boards and executive committees. The impact of the bank on the company is clearly non-existent, except for a potential signalling effect: if the bank has a reputation as a good investor, its investment may drive other investors to buy stocks of the company.

On the other hand, the bank relies exclusively on public information to decide about its future course of action, just like any other external investor.

4.2.b. The portfolio model

The second model is the portfolio model. In this model, banks try to develop synergies by establishing an internal capital market. The bank acts as a portfolio manager, buying and selling stakes in companies, depending on their current and expected future performance and the diversification strategy of the portfolio. This model captures the bank's interest in the profitability of the group as a whole, although its focus is exclusively financial.

The main difference between this model and the independence model are the following. Firstly, in the portfolio model the bank wants to act, not just occasionally, but actively and consistently as portfolio manager, in part as a means of diversifying risk away from its traditional banking activities.

Sometimes, there is a second difference. When the bank has a large stake in a number of firms, it may create an internal capital market, allocating resources to the different firms centrally (in a sense treating them as business units) and managing their liquidity and financial investments. In the second case, one can argue that the horizon is the long term, not the short term. Nevertheless, the key factor in determining the choice of one time horizon or another is the profit potential the bank sees in each investment.

From a managerial perspective, in this model the bank relies not only on public information, but also on internal information from the different firms. Even if the bank does not interfere with the management of the companies, it may offer incentives to their managers

to act in certain ways. This can only be achieved when the bank has a large and controlling stake in the companies, otherwise it is not feasible.

Banco Central Hispano in Spain, Mitsubishi in Japan (and other Japanese banks, in general) and Crédit Lyonnais in France are good examples of the portfolio model. It is worth bearing in mind the problems some of these banks have had in recent years as a direct result of the poor performance of the companies they had a stake in. Those problems cast further doubts on the viability of bank intervention in non-financial firms in the role of portfolio manager, as part of an effort to diversify.

4.2.c. The supervision model

The third model is the supervision model. It combines a longer time horizon with an emphasis on the profitability of the firm itself, forgetting about the impact of the firm on the group as a whole.

In this context, banks appoint members of the firm's board of directors. They supervise and control the operations of the firm and appoint its senior managers. The board may take an active or passive stand. In the former case, it may adopt practices of good corporate governance that lead to a close monitoring of the firm. In the latter case, the firm may be dominated by the chairman or the CEO, and the members of the board may tend to vote with the chairman.

The supervision model tends to close the gap between shareholders and managers through the bridge established by the board of directors. Nevertheless, this flow of information may be put in serious jeopardy if the board takes a more passive stand and does not professionally control the management of the firm.

Deutsche Bank, Commerzbank and La Caixa are good examples of this model. In general, the presence of external directors appointed by the largest shareholders helps align interests between these shareholders and the firm's managers, and encourages greater professionalism in the management of the firm.

The effects of the bank on the firm flow through the channel of the board of directors. When the directors do a good job in terms of supervision, control and appointment of senior managers, banks contribute to the firm with good corporate governance practices.

Nevertheless, the only effect the firm has on the bank is its help in improving management systems and, eventually, its profitability. This has a positive dimension, insofar as it reduces managerial complexity. On the other hand, this approach may fall short of extracting the full benefit from banks' involvement in non-financial firms, preventing them from realising other forms of synergy.

4.2.d. The network model

This last point leads us to a discussion of the fourth model, which is the network or integration model. This model includes a long-term perspective, like that of the supervision model, but takes a different view regarding the relations of the firm with the rest of the group. In this model, banks approach their shareholdings as opportunities, not only in terms of the profitability of the firm itself, but also in terms of other advantages or benefits –tangible or intangible– that the firm may contribute to the bank and the business group as a whole.

These benefits are, on the one hand, its financial profitability; on the other, the advantages stemming from the presence of the firm in the group, owing to its size, financial resources, brand name, reputation, technology or managerial capabilities.

This perspective opens the door to the concept of corporate strategy. We can look at bank-firm groups as business groups in which banks play a key role as large and leading shareholders. The dimensions of corporate strategy vary widely, from a mere portfolio management approach to the sharing and transfer of resources.

In the network model, this latter dimension is the important one. Banks want to share certain resources across the group, from managerial talent to capital, including brand names and information technology.

The opportunities for sharing resources are considerable, but the obstacles managers will have to overcome in order to handle the disparity of relationships are similarly awesome. This is the greatest hurdle banks face in the network model. The hurdle gets bigger as the number of different industries in the group increases, since the managerial expertise available in some of these industries may be limited.

There are not many banks that follow this model, although one can recognize the efforts of Banco Bilbao Vizcaya to forge a network of companies that share resources and capabilities. Eventually, the bank's success will depend very much on the quality of its management –in terms of combining centralization and decentralization, autonomy and control, entrepreneurship and strict resource allocation procedures.

It is easy to see and conclude that the success of the network model will also depend on external factors, such as potential downturns in some industries, which may constrain the management's ability to react.

In Sections 6 and 7 we shall explore the consequences of these models along two basic dimensions: the bank's corporate strategy, and the firms' corporate governance. But before tackling these dimensions, in the next section we shall set the context by discussing the role of banks as large shareholders

5. Large shareholders and firms' performance

The effects of banks on firms' performance can be better understood by first discussing the effects of large shareholders on firms' performance. In a previous section, we mentioned some studies that support the idea that large shareholders are associated with better company performance. Nevertheless, there are also potential costs to large shareholders (Demsetz and Lehn, 1985) that may tilt the balance in the opposite direction.

As Berglöf (1997, pp. 111-112) points out, “our understanding of what explains these large variations in corporate governance systems and how they influence economic performance is still very limited. Indeed, it is typically difficult to compare the performance of individual corporate governance arrangements within systems. There is no uncontroversial way to measure performance, and even when there is some agreement on the appropriate measures and their interpretation, the more difficult problem remains to establish cause and effect.”

The evidence we have collected so far is not conclusive. Cable (1985), in his work on German banks, concludes that for the sample of German companies observed, companies that have a bank as shareholder are more profitable in their industry than those that do not. However, these findings do not indicate any direct causal relationship and must be treated with caution. He also states that the source of this superior performance lies mainly in the fact that the bank-company group offers an internal capital market that provides more stable sources of financing over time. Cable's study does not consider whether or not bank shareholdings have a positive effect on banks' economic performance.

Gorton and Schmid (1996) analyse the performance of German firms in 1974 and 1985. They conclude that German banks improved the performance of the companies in which they held equity in 1974. The explanation they offer is that banks had an incentive to oversee the firms because there was no liquid market in which to trade the stock. Nevertheless, they observe that banks did not exert the same influence in 1985.

Corbett (1987), in her research on bank-industry relationships in Japan, demonstrates the existence of implicit contracts between banks and industrial companies. These contracts guarantee continuity in the sources of finance for the company; in return, the company pays relatively higher interest rates compared with the market rates.

Industrial companies are willing to accept these conditions because banks offer them greater stability of the sources of finance. As a result, Japanese industrial companies pay higher interest expenses than if their financing were agreed at market prices, which in turn affects these companies' profitability and cost of capital.

A related conclusion is that banks' profitability shows greater variability. At times of high economic growth, when companies do not have financial problems, banks with large industrial shareholdings obtain a higher return on assets, in relative terms, than other banks in industrialized countries. On the other hand, during periods of slower economic growth, with a greater number of companies in difficulties, the banks' return on assets drops considerably.

Hoshi *et al.* (1990) compare companies inside and outside the "keiretsu", the Japanese conglomerates. Firms that belong to a "keiretsu" have less variability in cash flows, their profitability is lower than other firms in the same industry, and their investments seem to be immune to changes in cash flow.

The studies discussed above seem to follow an implicit model. They assume that bank ownership has an effect on economic performance, defined as return on equity or any other profitability ratio. Next, they define variables that may explain how ownership affects performance. They control for these variables and explain how the firm's performance changes as a result of changes in bank ownership.

Their approach is right from a methodological viewpoint, but it does not capture the details that explain the differences between systems of corporate governance. Simplifying, their implicit model can be summarised as follows:



The problem is that these studies do not explain whether the same level of bank ownership can have different effects on performance; nor do they pinpoint the variables through which banks have an impact on performance. In other words, the effect on

performance may be the same, but the mechanisms that affect performance may be different. Our objective here is to suggest a framework in which to analyze those mechanisms.

Kaplan (1994a,b) takes a different tack in evaluating performance. He tries to compare the effects of different corporate governance systems in three countries (Germany, Japan and the U.S.) between 1980 and 1988 by looking at changes in managerial turnover and managerial compensation. His implicit model (Kaplan 1994b) is

Firm's performance —————> Management turnover

or, his other model (Kaplan, 1994a):

Firm's performance —————> Executive compensation

In his studies, Kaplan uses three different measures of performance: sales growth, change in pre-tax income over total assets, and stock returns.

His conclusions are as follows: First, in the three countries included in the study the probability of management turnover is higher when firms experience losses. Statistically, the results in the three countries are the same. Second, sales growth explains why managers lose their jobs in Japan and the U.S., but not in Germany. Third, in Japan, stock performance is more important than sales growth in explaining managerial turnover. Finally, executive compensation in the three countries is also related to sales performance, return on equity and stock performance.

All in all, Kaplan's papers give a very different picture from previous studies. They show that different corporate governance systems tend to generate similar results. These systems also seem to react similarly to indicators of corporate performance, such as sales growth, return on investment or changes in stock prices.

Kaplan suggests that there is something intriguing about these results. It has to do with the fact that the German and Japanese systems do not have an active market for corporate control, unlike the U.S. system. In the U.S., capital markets may impose changes on companies when performance is poor.

In Japan and Germany, it is the board of directors (and the large shareholders on the board) that influences managerial turnover, perhaps by appointing outside directors. Management turnover increases substantially when new outside members join the board.

In other words, in Japan and Germany large shareholders and the board of directors seem to play the role performed by capital markets in the U.S.

Kaplan (1997) offers an explanation of his own results. He claims that, in industrial countries, corporate governance differences tend to have a milder effect on economic performance, because in these countries firms have to be competitive, respond to shareholders and try to attract capital in global markets. For these reasons, corporate governance is not a real issue so long as there is a strong market rivalry. On the other hand, governance may have a pivotal role in industries that are not growing, or that are mature or less competitive.

We do not agree with this latter explanation. If we accept that management has an impact on corporate performance (Schumpeter, 1947; Ghoshal, Hahn and Moran, 1997) and

that strategy and management systems may have a positive effect on the way firms evolve, Kaplan's explanation may not be comprehensive.

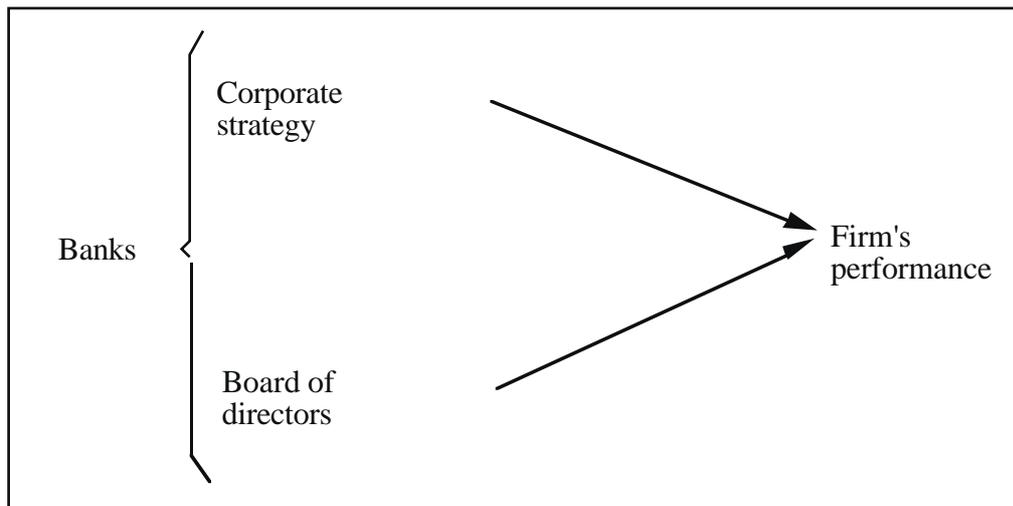
In the rest of this paper we shall outline a different way of thinking about the effects of bank shareholding, and of corporate governance in general, on firms' performance. If we accept that strategy affects performance,

Strategy \longrightarrow Firm's performance

the key point is whether the systems of corporate governance have an impact on strategy design and implementation.

The model we propose assumes that the system of corporate governance may lead banks to design a corporate strategy, set up governing bodies with specific functions (for instance, the role of the board of directors and the role of the executive committee) and establish decision-making rules that may have an impact on strategy design. Also, the corporate governance system has an impact on the way strategy is designed and implemented through various management committees, and control and incentive systems.

This view can be summarised as follows:



In the next two sections, we shall outline some hypotheses that try to make these ideas more explicit and discuss their implications.

6. The links between banks and firms' performance: The role of corporate governance

6.1. The structure of the board of directors

Banks may have an impact on firms' performance through the structure and composition of the board of directors. Board structure is affected by the existence of large shareholders, outside directors, banks that are shareholders, and other blockholders.

The board of directors is a corporate governance mechanism that helps the management of the firm to achieve its objectives. Its responsibility is to ensure that the CEO performs his/her duties and brings his/her interests into line with those of the shareholders. Some recent studies show that boards and their structure do have some influence on corporate performance.

Large shareholders

Shleifer and Vishny (1986), Franks and Mayer (1994) and Kaplan and Minton (1994) show, in different contexts, that large shareholders have an effect on firms' performance.

The link between ownership and firm value may work through the influence of shareholders on corporate decisions. Bethel and Liebeskind (1993) show that blockholders' ownership affects the lobbying of senior managers in the case of corporate restructuring and, consequently, has an impact on the firm's value. They suggest that blockholder ownership is associated with corporate restructuring. In other words, senior managers restructure when they are under pressure from large shareholders.

Large shareholders seem to affect firms' diversification. Hill and Snell (1988) have studied the role of insider ownership and shareholder concentration. They suggest that both are constraints on the firm's diversification efforts. Managers tend to diversify more when their interests do not coincide with those of shareholders.

Denis, Denis and Sarin (1997) confirm that the level of diversification is negatively correlated to managerial equity ownership and ownership by outside blockholders.

Wright *et al.* (1996) explore the influence of ownership structure on corporate risk-taking. Contrary to some previous work, such as that of Amihud and Lev (1981), they find that the relationship between insider equity ownership and corporate risk-taking may not be monotonically positive.

All in all, these studies seem to show that ownership structure, the mix of inside and outside directors on the board, and CEO duality are channels through which banks may exert an influence on firms' performance.

Some recent cases highlight the importance of this factor. First, the leading role played by Deutsche Bank and its representatives on the board of directors of Metallgesellschaft A.G., when the latter company entered a crisis in 1994-1995. As a shareholder, Deutsche Bank led the way to a restructuring of the firm, a rescheduling of the debt, and a top management reshuffle. The intriguing thing in this case is the bank's failure to detect and avoid the crisis in the first place.

The second case concerns the appointment of a new CEO who brings a new outlook into the firm. This was the case of Banco Bilbao Vizcaya, La Caixa and Argentaria, all of them large shareholders of Telefónica. The Spanish government, which was Telefónica's largest shareholder in 1996, wanted to replace the firm's Chairman. It could not do so until it obtained the agreement of the three banks on a candidate and on the plans of the new Chairman.

Inside and outside directors

Boards are composed of outside and inside directors. This is a classical distinction in corporate governance. Outside directors are individuals who are not affiliated with the firm on whose board they serve. Inside directors are managers associated with the firm. They can provide more information on the industry and the company itself, but are unlikely to challenge the CEO. In contrast, outside directors tend to be more aligned with stockholders. As a result, the presence of outside directors has an effect on the board's actions on issues of strategic control, strategic change and restructuring.

A higher ratio of inside directors on a board tends to weaken board control (Beatty and Zajac, 1990), while the presence of outside directors seems to be positively related to board control and performance (Shleifer and Vishny, 1986).

Stulz (1988) shows that a firm's market value first increases, then decreases with rising insider ownership. In other words, the value increases with the level of insider ownership, until it starts to fall when insiders become entrenched (Morck, Shleifer and Vishny, 1988).

CEO duality

The existence of CEO duality is also a factor that affects performance. Duality exists when a firm's CEO is also the Chairman of the board. An independent Chairman seems to have more flexibility in monitoring the firm and ensuring the board functions properly. A Chairman who is also CEO will reinforce his/her power and control over the firm (Finkelstein and D'Aveni, 1994).

6.2. *The functions of the board of directors*

Banks can have an impact on firms' performance through the functions of the board of directors, which the banks themselves, as shareholders, help design. This is another dimension of corporate governance. The functions of the board may evolve from non-interference in the management of the company to complete control. The specific functions of the board may include discussing and designing the firm's strategy in collaboration with the CEO and other senior managers, appointing all key management posts, approving certain investment and financial decisions, controlling the resource allocation process, monitoring performance, and determining executive compensation.

As Pound (1995) points out, the problem in corporate governance is not power imbalances, but failures in the corporate decision-making process. In other words, the problem has to do with the functions of the board of directors.

Traditionally, the main functions of the board of directors have been to appoint the CEO and senior managers, monitor their performance, and replace them when performance is unsatisfactory. This is a model that seems to have its focus in monitoring the CEO.

In this approach, directors are not involved in setting goals and fixing the firm's priorities, nor do they interfere with the CEO unless serious problems arise.

Recent corporate crises in Europe, Japan and the U.S. have reopened the discussion of the functions of the board of directors. Some ideas about corporate strategy emphasize the

importance of the board of directors in helping senior managers design healthy strategies, make effective decisions and detect potential crises in advance.

This set of functions for the board of directors is especially useful in cases where a bank is a large shareholder. These functions mean that directors should get involved in discussing the firm's strategy with the CEO and other senior managers, and in jointly fixing goals, objectives and policies. The board should also approve the basic outlines of strategic, policy and budgeting procedures: who approves what and when, who is responsible for the firm's various activities, and how and when the CEO will report to the board.

In other words, board members have to focus their attention not on reviewing the past, but on jointly reflecting with senior managers on the company's future. The role of senior managers is to propose and discuss with the board the firm's strategy and, once it has been approved, implement it.

The experience gathered in certain cases of corporate restructuring lead Donaldson (1995) to the conclusion that boards need some management tools to carry out their functions. He suggests a simple tool known as "strategic audit".

This may include some of the following elements: a definition of the data and criteria to be used in the review process; a procedure for ensuring the consistency of the information used, with the help of the firm's public auditors; and the selection of a strategy committee within the board, whose function will be to conduct periodic reviews and submit its conclusions to the board.

Strategic audit involves creating a new control system. In general, control systems are formal procedures used by the board to monitor senior managers' organizational behaviour and the firm's performance.

Simons (1994) defines four types of management control systems that banks could find useful in defining the agenda and functions of the board of directors. First, belief systems. These are systems used by the board and top managers to communicate the purpose and mission of the firm.

Second, boundary systems. These are a set of rules that establish limits to be respected by all members of the firm, and include codes, directives and formal budgeting and planning systems.

Third, diagnostic control systems. These provide regular feedback about organizational performance and deviations from established objectives.

Fourth, interactive control systems, which the board uses to get involved in the decision-making process. They force interaction among all the members of the organization.

The changes that Deutsche Bank and Banco Bilbao Vizcaya have recently made to some of the boards they sit on as shareholders are, above all, a reaction to the problems that some banks have experienced as a result of unanticipated corporate crises affecting the non-bank firms they own. However, these banks also share the belief that a board of directors with well defined functions can have a huge impact on the way the firm is managed and how it performs.

7. The links between banks and firms' performance: The role of corporate strategy

Banks as large shareholders may have an effect on the performance of a firm they own by developing a corporate strategy that supports and fosters the firm's own strategy. This is one dimension of what Campbell, Goold and Alexander (1994) call "parenting". This hypothesis is consistent with the organizational innovations that some large corporations are adopting in order to manage, develop and grow different business units. Bartlett and Ghoshal (1993) use them as a reference to call for a managerial theory of the firm.

To be successful, corporate strategy calls for the transfer of tangible and intangible resources and capabilities from the parent company to the other firms in the group. These resources must have an economic value. In other words, they must be scarce and difficult to imitate, and there must be no ready substitute for them (Barney, 1991). If these conditions are not met, the resources would cease to have any special economic value for the group.

Banks may offer advantages to the firms they own through the critical resources they share with the firms. The evidence of the banks we have studied shows that the development of internal capital markets and managerial competence are the two most valuable capabilities that banks can transfer to the firms they own (Table 4).

Table 4	
Banks' resources	
<u>Tangible resources</u>	<u>Intangible resources</u>
<ul style="list-style-type: none"> - Internal capital market - Information technology 	<ul style="list-style-type: none"> - Managerial capabilities - Corporate strategy <ul style="list-style-type: none"> - Mission - Vision - Organizational design - Entry into new business - Restructuring - Learning transfer - Management development - Brand name

Internal capital markets

An internal capital market gives headquarters control rights to allocate resources and shift funds from one business unit to another (Williamson, 1975; Stein, 1997). At the same time, it enables firms within a bank group to obtain quick access to financial resources at a lower cost. This resource is very important in explaining the growth of bank groups.

An internal capital market in a bank group may work in several ways. The first is when the bank manages the firms as if they were a portfolio of businesses that has to achieve a certain mix of risk and return. The parent company will buy or sell firms as necessary in order to balance the portfolio and achieve its financial goals. The second way is when the bank sets financial targets for each of the firms or business units, allocates capital to each one and intervenes through the firm's managers when targets are not met.

For a bank, what advantages does an internal capital market have over external capital markets? There are two main advantages. First, the bank can monitor and control each firm more closely than the capital markets could, simply because managers have information that capital markets do not. The second advantage is that the internal capital market allows the bank to act more quickly when it detects an opportunity to buy or enter a new business.

Banco Santander provides evidence of this behaviour. For the past three years it has used its financial resources to become a key shareholder in a number of non-financial companies and acquire banks in the U.S. and Latin America whenever the opportunity has presented itself. At the end of 1996, 37% of its assets and 42% of its return on assets came from its investments in those companies.

To summarise, an internal capital market could be a key asset for a bank group, although one must not forget that if the group is not well managed, the internal capital market may become a millstone around its neck. The reason is that having financial resources immediately available can lead to risky investments.

Managerial competence

A firm's intangible resources include, among other things, corporate reputation, brand name and managerial competence. In a corporate group, managerial competence includes the ability to manage, coordinate and control each of the business units from the group's head offices. This is a critical resource in large, diversified business groups (Goold and Campbell, 1987; Bartlett and Ghoshal, 1993), and particularly in large banks (Canals, 1997).

Certain business groups have developed and used managerial competence successfully. This is the case of General Electric and ABB or, in the banking industry, Banco Bilbao Vizcaya and ABN Amro Bank. However, successful corporate groups are thinner on the ground than the failures and this is particularly true in the banking industry, where attempts to discover and exploit synergies have gone beyond what is reasonable.

The foremost managerial capability in a corporate group is the ability to develop and implement a corporate strategy, that is to say, to manage the group along certain dimensions:

- The first dimension is the identification, development, deployment and renewal (Hamel and Prahalad, 1994) of the critical resources or capabilities that clearly add value to each of the group's firms. This is a fundamental task in a business group.

The group justifies its existence by the value it creates, and this value is influenced by the contribution made by the corporate centre through certain resources. Managing these resources –in the aspects listed above– is critical. If the resources disappear or cease to have value for the different business units, the logic of the group becomes shaky.

Banks such as Commerzbank, Barclays, ABN Amro and Banco Santander have taken steps to transfer resources from the corporate center to firms within the group, or from one business unit to another. In the banks we have analyzed, we can see certain basic resources being transferred: managers, capital, brand names, marketing practices and information systems.

- The second dimension is to articulate an organizational design, with planning and control systems that help maximise the corporate group's contribution to each firm. In other words, the parent company has to design an organizational structure that makes the resource transfer process efficient, minimises internal conflicts, aligns incentives and reduces the possibility of wasting resources.

This is the approach being taken by La Caixa, the second largest savings bank in Europe. In the past five years it has invested heavily in telecommunications, energy, transportation, utilities and leisure. It has a strong influence in appointing these firms' CEOs. From an operational viewpoint, it transfers proven management systems that help the firms to tighten up their operations.

- The third dimension refers to decisions to take the group into new businesses. Such decisions can be broken down into at least two parts. The first is to analyse the potential of a new business, both the generic attractiveness of the industry as such and the specific attractiveness of the company that is to be acquired or developed. The second part of the decision is to analyse how the resources that have driven the corporate group's success in the past can be deployed in the new business.

Banco Central Hispano has a long tradition of industrial shareholdings. These investments have targeted companies with high growth potential in industries such as oil, construction and energy. BCH has developed a strategy of diversification away from traditional banking activities. It manages its portfolio of companies according to the prospects of each firm and the industry it operates in.

The ability to restructure a firm is the second managerial capability that the group can transfer to firms. Banco Santander is a specialist in discovering firms whose market value is below their real value and then turning them around with a restructuring plan.

Banco Santander and its acquisition of Banesto in 1994 is a clear case of this transfer of resources. Banesto was almost bankrupt in 1993, when the Bank of Spain decided to intervene and later sell it to another bank.

In April 1994, Banco Santander bought Banesto and put together a new management team, which started to rationalize the bank. The turnaround process was a success, and in less than three years Banesto was back on its feet.

Restructuring processes have a number of common features: cost-cutting, changing the management team, flattening the organization structure, changing employee compensation schemes, refocussing the business on certain products and eliminating other less interesting products, and selling assets or businesses that are not vital to the company's core business. The parent company can share with the firms it owns its unique capabilities in corporate restructuring.

8. The effects of bank ownership on banks

Banks invest in non-financial firms in the search for diversification opportunities. Nevertheless, bank-industry relationships may have a negative impact on banks for the following reasons: risk concentration, corporate diversification and managerial complexity.

Risk concentration and corporate diversification

Historically, the first problem that banks with industrial shareholdings have experienced is an excess of risk concentration. A rule of thumb in banking is to avoid risk concentration in lending. Large industrial shareholdings demand a long-term commitment of capital. Banks' performance is intrinsically linked to the fate of the firms they own.

In general, the recent experiences of certain universal banks with industrial shareholdings, in France (Crédit Lyonnais), Germany (Deutsche Bank) and Spain (Banesto), suggest that the idea of banks diversifying into non-financial firms may be fine in theory, but very risky in practice, because it hurts banks' performance and puts their financial health in jeopardy.

The evidence would appear to reinforce the notion that corporate diversification into unrelated businesses (which is what happens when banks acquire shareholdings in non-financial firms) is riskier than diversification into related businesses. In the case of banks, the risk concentration factor plays a differential role in explaining their diversification performance.

Managerial complexity

Managerial complexity is another factor that may hamper the performance of banks that invest in industrial companies. This complexity emerges as a combination of agency, information, coordination and influence costs.

Agency costs in a universal bank consist of the costs of designing the explicit contracts between the bank and the firms (in this case, the bank is a blockholder), the cost of supervising these contracts, and the cost of ensuring fulfilment of the contracts. Normally, the contracts have to do with defining the budgeting and policy systems, and the performance evaluation and compensation systems which the corporate headquarters decides to apply to each business unit.

A second problem facing universal banks, one that is related to the fact that the agents involved have asymmetric information, is the moral hazard. This hazard arises when the interests of those within the firm who possess information (senior managers unaffiliated with the bank) are in conflict with the interests of those responsible for making a decision on the basis of that information (the bank's representatives on the board of directors). This situation opens the door to opportunistic behaviour, whereby senior managers may manipulate the information so that the board's decision benefits them.

A third organizational problem is the cost the bank incurs in coordinating the various business units. In general, coordination problems come about as a result of the specialization of the work performed by different people or different units within an organization.

Usually, each unit has partial or incomplete information about the rest of the organization. Consequently, it is vital to find a system that enables information to be shared and thus achieve efficient actions. One of the specific goals of coordination in a universal bank is to discover and strengthen the supposed synergies between the different business units in order to share costs or increase revenues.

Again, although the coordination problem is a classic problem of any organization (Williamson, 1975), in the case of universal banks it has certain unique features that make it different from the coordination problem in a specialised bank.

Finally, diversified banks face an additional problem that is typical of all complex organizations, namely the influence costs. Influence costs are part of the more general problem of rent-seeking activities, that is, the activities that are not productive and that seek to modify income distribution between different groups of individuals. Support of protectionist interests in certain industries is a clear example of rent-seeking activity.

Influence costs emerge in an organization when there are decisions that establish ways of distributing costs and profits within the organization as a whole. Decisions of this kind obviously exist in any universal bank (in fact, in any diversified company) and they are often the subject of argument among managers. In universal banks, influence costs arise in any activity or decision that seeks to transfer costs from one business unit to another, or to share revenues and costs among different units.

There are a number of general criteria for minimizing these costs: decentralize the resource allocation and decision-making process as much as possible; try to limit the negative consequences of income redistributions (e.g. by establishing similar remuneration structures in all of the corporate group's units); and establish or agree the policies affecting resource distribution *a priori*, with a commitment not to revise the decision.

None of these criteria in itself will guarantee that the problems will be eliminated. Nor can a combination of criteria guarantee this, although it can be said that when the right combination is obtained, the chances of minimizing conflict and its consequences are greater than ever.

All in all, risk diversification, corporate diversification and managerial complexity may have negative effects on banks. The dangers pointed out in this section give cause for deep concern about the increasing complexity of managing bank-industry relationships. Some investments considered by banks as outstanding business opportunities have all too often become troublesome, as the firms that banks invested in proved more difficult to manage than originally expected. The arguments reviewed merely serve to highlight the daunting task facing bank managers, as the recent cases of Banesto and Crédit Lyonnais demonstrate.

9. Some conclusions

Corporate governance has been the subject of intense debate in the 1990s, partly as a result of the corporate restructuring process taking place in the U.S. and Europe. The financial models and arrangements in these countries have different features and provide a different foundation for corporate governance.

A key factor in explaining corporate governance is the role of large shareholders and, more specifically, the role of banks in non-financial firms, both as shareholders and as lenders. In some European countries that have a bank-based model, banks have a vast presence in the corporate sector and on corporate boards. In the capital market-based model found in the U.S., banks play a more secondary role in corporate governance.

The presence of banks as shareholders in some non-bank firms may have an impact on their economic performance. In this paper, we have provided a framework that links bank ownership with corporate performance.

This framework relies on certain hypotheses. First, that banks may have an effect on corporate performance by designing and implementing a sound corporate strategy that allows the non-bank companies they own to share in the banks' resources and capabilities.

Second, banks may have an effect on corporate performance through the structure and composition of the board of directors. The presence of outside directors and other blockholders may improve the firm's performance.

Third, banks may have an effect on the firm's performance by designing a set of functions for the board of directors. These functions include not only reviewing past financial performance, but also collaborating with the CEO and senior management to define current and future strategies, and to set up the appropriate control and management systems and procedures.

Fourth, in recent years banks have invested in non-bank firms as a way of diversifying their revenues away from the increasingly competitive banking industry. Nevertheless, managing a business group around a universal bank may be a daunting task for managers. Managerial complexity is the result of agency, information, control and coordination problems.

All in all, past experience regarding the role of banks in corporate governance is inconclusive. As Kaplan (1997) points out, modern corporate governance systems in Germany, Japan and the U.S. have different features, but in terms of performance the differences are not so clear.

When one looks at the question of the effects that banks have on firms' performance, the evidence is even less clear. Nevertheless, if banks can have an impact, it will be through the wise use of corporate strategy and careful attention to the functioning of the board of directors. □

References

- Amihud, Y. and Lev, B. (1981): “Risk reduction as a managerial motive for conglomerate mergers”, *Bell Journal of Economics*, 12, 605-617.
- Aoki, M. (1988): *Information, incentives and bargaining in the Japanese economy*, Cambridge University Press, Cambridge.
- Barney, J. (1991): “Firm resources and sustained competitive advantage”, *Journal of Management*, 17, 99-120.

- Bartlett, C.A. and Ghoshal, S. (1993): “Beyond the M-form: Toward a managerial theory of the firm”, *Strategic Management Journal*, 14, Special Issue, Winter, 23-46.
- Beatty, R.P. and Zajac, E. (1990): “Top management incentives, monitoring and risk-bearing: A study of executive compensation, ownership and board structure in initial public offerings”, *Academy of Management Best Paper Proceedings*, 7-11.
- Berglöf, E. (1990): “Capital structure as a mechanism of control”, in M. Aoki, B. Gustafsson and O. Williamson (eds.), *The firm as a nexus of treaties*, Sage, London.
- Berglöf, E. (1997): “Reforming corporate governance: Redirecting the European agenda”, *Economic Policy*, April, 24, 91-124.
- Bethel, J.E. and Liebeskind, J. (1993): “The effects of ownership structure on corporate restructuring”, *Strategic Management Journal*, 14, 15-31.
- Boyd, B.K. (1994): “Board control and CEO compensation”, *Strategic Management Journal*, 15 (5), 335-344.
- Cable, J. R. (1985): “Capital market information and industrial performance: The role of West German banks”, *Economic Journal*, 95, 118-132.
- Campbell, A., Goold, M. and Alexander, M. (1994): *Corporate-level Strategy*, John Wiley, London.
- Canals, J. (1997): *Universal Banks: Theoretical Perspectives and International Comparisons*, Oxford University Press, Oxford.
- Collis, D. (1991): “Corporate strategy: A research agenda”, mimeo, Harvard Business School, Boston.
- Collis, D. and Montgomery, C.A. (1997): *Corporate strategy: Resources and the scope of the firm*, Irwin.
- Corbett, J. (1987): “International perspectives on financing: Evidence from Japan”, *Oxford Review of Economic Policy*, 3 (4), 30-55.
- Demsetz, H. (1983): “The structure of ownership and the theory of the firm”, *Journal of Law and Economics*, 26, 375-390.
- Demsetz, H. and Lehn, K. (1985): “The structure of corporate ownership: Causes and consequences”, *Journal of Political Economy*, 93, 1.157-1.177.
- Denis, D.J., Denis, D.K. and Sarin, A. (1997): “Agency problems, equity ownership and corporate diversification” *Journal of Finance*, 52 (1), 135-160.
- Diamond, D.W. (1984): “Financial intermediation and delegated monitoring”, *Review of Economic Studies*, 51, 393-414.
- Donaldson, G. (1995): “A new tool for boards: The strategic audit”, *Harvard Business Review*, July-August, 99-108.
- Edwards, J. and Fischer, K. (1994): *Banks, finance and investment in Germany*, Cambridge University Press, Cambridge.

- Fama, E.F. (1980): “Agency problems and the theory of the firm”, *Journal of Political Economy*, 88, 288-307.
- Finkelstein, S. and D’Aveni, R.A. (1994): “CEO duality as a double-edged sword: How boards of directors balance entrenchment avoidance and unity of command”, *Academy of Management Journal*, 37 (5), 1.079-1.108.
- Franks, J. and Mayer, C. (1990): “Corporate ownership and corporate control: A study of France, Germany and the U.K.”, *Economic Policy*.
- Franks, J. and Mayer, C. (1994): “The ownership and control of German corporations”, Manuscript, London Business School.
- Franks, J. and Mayer, C. (1996): “Hostile takeovers and the correction of managerial failure”, *Journal of Financial Economics*, 162-181.
- Franks, J. and Mayer, C. (1997): “Corporate ownership and control in the U.K., Germany and France”, *Journal of Applied Corporate Finance*, 9 (4), 30-45.
- Ghoshal, S., Hahn, M. and Moran, P. (1997): “Management competence, firm growth and economic progress”, Working Paper, Insead.
- Gibbs, P.A. (1993): “Determinants of corporate restructuring: The relative importance of corporate governance, takeover threat and free cash flow”, *Strategic Management Journal*, 14, Special Issue, Summer, 51-68.
- Goold, M. and Campbell, A. (1987): *Strategies and styles*, Basil Blackwell, Oxford.
- Gorton, G. and Schmid, F.A. (1996): “Universal banking and the performance of German firms”, Working Paper, Wharton School.
- Grossman, S. and Hart, O. (1988): “One share-one vote and the market for corporate control”, *Journal of Financial Economics*, 20, 175-202.
- Hamel, G. and Prahalad, C.K. (1994): *Competing for the future*, Harvard Business School Press, Boston.
- Harm, C. (1992b): “The relationship between German banks and large German firms”, Working Paper, The World Bank.
- Hart, S. and Bambury, C. (1994): “How strategy-making processes can make a difference”, *Strategic Management Journal*, 15 (4), 251-269.
- Hellwig, M.F. (1991): “Banking, financial intermediation and corporate finance”, in A. Giovannini and C. Mayer (eds.), *European financial integration*, Cambridge University Press, Cambridge.
- Hill, C. and Snell, S. (1988): “External control, corporate strategy and firm performance in research-intensive industries”, *Strategic Management Journal*, 9, 577-590.
- Hitt, M.A., Hoskinsson, R.E. and Ireland, R.D. (1990): “Mergers and acquisitions and managerial commitment to innovation in M-form firms”, *Strategic Management Journal*, 11 (Special issue), 29-47.

- Hoshi, T., Kashyap, A. and Scharfstein, D. (1990): “The role of banks in reducing the costs of financial distress in Japan”, *Journal of Financial Economics*, 27, 67–88.
- Hoshi, T., Kashyap, A. and Scharfstein, D. (1991): “Corporate structure, liquidity and investment: Evidence from Japanese industrial groups”, *Quarterly Journal of Economics*, 106, 33-60.
- Iaquinto, A.L. and J.W. Fredrickson (1997): “Top management team agreement about the strategic decision process: A test of some of its determinants and consequences”, *Strategic Management Journal*, 18, 63-75.
- Jensen, M.C. (1989): “The eclipse of the public corporation”, *Harvard Business Review*, September-October, 61-75.
- Johnson, R.A., Hoskinsson, R.E. and Hitt, M.A. (1993): “Board of director involvement in restructuring: The effects of board versus managerial controls and characteristics”, *Strategic Management Journal*, 14, 33-50.
- Kaplan, S.N. (1994a): “Top executives, turnover and firm performance in Germany”, *Journal of Law, Economics & Organization*, 10 (1), 142-159.
- Kaplan, S.N. (1994b): “Top executive rewards and firm performance: A comparison of Japan and the U.S.”, *Journal of Political Economy*, 102, 510-546.
- Kaplan, S.N. (1997): “Corporate governance and corporate performance: A comparison of Germany, Japan and the U.S.”, *Journal of Applied Corporate Finance*, 9 (4), 86-93.
- Kaplan, S.N. and Minton, B. (1994): “Appointments of outsiders to Japanese boards: Determinants and implications for managers”, *Journal of Financial Economics*, 36, 225-257.
- Kester, W.C. (1991): *Japanese takeovers: The global contest for corporate control*. Boston: Harvard Business School Press.
- Kester, W.C. (1992): “Banks in the board room: The American versus Japanese and German experiences”, *Managing the Financial Services Firm in a Global Environment*, Harvard Business School, Research Colloquium.
- Kosnik, R.D. (1990): “Effects of board demography and directors’ incentives on corporate greenmail decisions”, *Academy of Management Journal*, 33 (1), 129-150.
- Martin, K. and McConnell, J.J. (1991): “Corporate performance, corporate takeovers and management turnover”, *Journal of Finance*, 46, 671-687.
- Milgrom, P. and Roberts, J. (1992): *Economics, organization and management*, Prentice Hall, New York.
- Morck, R.A., Shleifer, A. and Vishny, R. (1989): “Alternative mechanisms of corporate control”, *American Economic Review*, 79, 842-852.
- Morck, R.A., Shleifer, A. and Vishny, R. (1990): “Do managerial objectives drive bad acquisitions”, *Journal of Finance*, 25, 31-48.

- Myers, S. and Majluf, N. (1984): “Corporate financing and investment decisions when firms have information that investors do not have”, *Journal of Financial Economics*, 13, 187-221.
- Pfeffer, J. (1983): “Organizational demography”, included in L.L. Cummings and B.M. Staw (eds.), *Research in organizational behaviour*, Vol. 5, pp. 229-357, JAI Press, Greenwich, CT.
- Porter, M.E. (1992): *Capital choices*, Council of Competitiveness, Washington, D.C.
- Pound, J. (1995): “The promise of the governed corporation”, *Harvard Business Review*, March-April, 89-102.
- Prahalad, C.K. and Bettis, R.A. (1986): “The dominant logic: A new linkage between diversity and performance”, *Strategic Management Journal*, 7, 485-501.
- Prowse, S. (1992): “The structure of corporate ownership in Japan”, *Journal of Finance*, 47, 1121-40.
- Schumpeter, J.A. (1947): “The creative response in economic history”, *The Journal of Economic History*, 7 (2), 149-159.
- Shleifer, A. and Vishny, R. (1986): “Large shareholders and corporate control”, *Journal of Political Economy*, 94, 488-461.
- Shleifer, A. and Vishny, R.W. (1996): “A survey of corporate governance”, NBER, Working paper 5554.
- Simons, R. (1994): “How new top managers use control systems as levers of strategic renewal”, *Strategic Management Journal*, 15 (3), 169-189.
- Smith, M. and White, M.C. (1987): “Strategy, CEO specialization, and succession”, *Administrative Science Quarterly*, 32, 263-28.
- Stein, J. (1997): “Internal capital markets and the competition for corporate resources”, *Journal of Finance*, 52 (1), 111-133.
- Stulz, R.M. (1988): “On takeover resistance, managerial discretion, and shareholder wealth”, *Journal of Financial Economics*, 20, 25-54.
- Weinstein, D.E. and Yafeh, Y. (1994): “On the costs of a bank-centered financial system: Evidence from the changing bank relations in Japan”, Manuscript, Harvard University.
- Williamson, O.E. (1975): *Markets and hierarchies*, The Free Press, New York.
- Wright, P., Ferris, S.P., Sarin, A. and Awasthi, V. (1996): “Impact of corporate insider, blockholder, and institutional equity ownership on firm risk taking”, *Academy of Management Journal*, 39 (2), 441-463.
- Zajac, E.J. and Westphal, J.D. (1996): “Who shall succeed? How CEO/Board preferences and power affect the choice of new CEOs”, *Academy of Management Journal*, 39 (1), 64-90.

IESE**DOCUMENTOS DE INVESTIGACION - RESEARCH PAPERS**

No.	TITULO	AUTOR
D/336	Partner selection and trust building in Western European-Russian joint ventures: A western perspective. February 1996	Ariño A. Rykounina, I. Skorobogatykh, I. Vilá, J.
D/337	Una visión económica de la pobreza y marginación en Cataluña. Febrero 1997	Argandoña, A.
D/338	What is an efficient capital market for a medium-sized company? April 1997	Santomá, J. Sebastián, A. Suárez, J.L.
D/339	La motivación en los trabajadores cedidos a través de una empresa de trabajo temporal: Fase PREETTOS y ETTOS Mayo 1997	Suárez, E. Pin, J.R. Huertas, F. Sánchez, E.
D/340	A new way to define the operations in the hotel industry. Mayo 1997	Muñoz-Seca, B. Riverola, J. Sprague, L.
D/341	Liberalización económica y empleo. Mayo 1997	Gual, J.
D/342	El liderazgo, clave del éxito de la mejora continua. Mayo 1997	Rodríguez, J.M.
D/343	Estudio de la evolución del PIB en España. May 1997	Ariño, M.A.
D/344	Gestión del riesgo de tipo de cambio en la empresa. Julio 1997	Faus, J. Rahnema, A.
D/345	La motivación en el trabajador a través de una empresa de trabajo temporal: Fase POSTETTOS. Julio 1997	Pin, J.R. Suárez, E.

IESE**DOCUMENTOS DE INVESTIGACION - RESEARCH PAPERS**

No.	TITULO	AUTOR
D/346	Consejos de administración en empresas familiares: Características de composición y funcionamiento. Niveles de utilidad. Julio 1997	Gallo, M.A. Cappuyns, K.
D/346 BIS	Boards of directors in family businesses: Characteristics regarding membership and functioning. Levels of usefulness July 1997	Gallo, M.A. Cappuyns, K.
D/347	The contribution of the neo institutional school to organizational theory: Paving the way to the political hypothesis. September 1997	Alvarez, J.L.
D/348	To do or not to do? Non-cooperative behavior by commission and omission in inter-firm ventures. October 1997	Ariño, A.
D/349	Survey of theories employed in business ethics. October 1997	Torres, M.
D/350	Volatilidades, betas y alfas de empresas españolas. Períodos 1990-1996 y 1986-1989. Octubre 1997	Fernández, P.
D/351	The employment debate: Employment performance and institutional change. October 1997	Gual, J.
D/352	Crecimiento y empleo en España ante la moneda única: ¿Cuál puede ser el papel de las reformas estructurales? Octubre 1997	Gual, J.
D/353	Incorporación de graduados universitarios a la empresa familiar. El aprendizaje. Octubre 1997	Gallo, M.A. Cappuyns, K.
D/353 BIS	Bringing university graduates into the family business. Learning. October 1997	Gallo, M.A. Cappuyng, K.