

Hancké, Bob; Cieply, Sylvie

Working Paper

Bridging the finance gap for small firms. The role of information flows across large firm-based production networks in supplying finance to small firms: the case of France

WZB Discussion Paper, No. FS I 96-311

Provided in Cooperation with:

WZB Berlin Social Science Center

Suggested Citation: Hancké, Bob; Cieply, Sylvie (1996) : Bridging the finance gap for small firms. The role of information flows across large firm-based production networks in supplying finance to small firms: the case of France, WZB Discussion Paper, No. FS I 96-311, Wissenschaftszentrum Berlin für Sozialforschung (WZB), Berlin

This Version is available at:

<https://hdl.handle.net/10419/44090>

Standard-Nutzungsbedingungen:

Die Dokumente auf EconStor dürfen zu eigenen wissenschaftlichen Zwecken und zum Privatgebrauch gespeichert und kopiert werden.

Sie dürfen die Dokumente nicht für öffentliche oder kommerzielle Zwecke vervielfältigen, öffentlich ausstellen, öffentlich zugänglich machen, vertreiben oder anderweitig nutzen.

Sofern die Verfasser die Dokumente unter Open-Content-Lizenzen (insbesondere CC-Lizenzen) zur Verfügung gestellt haben sollten, gelten abweichend von diesen Nutzungsbedingungen die in der dort genannten Lizenz gewährten Nutzungsrechte.

Terms of use:

Documents in EconStor may be saved and copied for your personal and scholarly purposes.

You are not to copy documents for public or commercial purposes, to exhibit the documents publicly, to make them publicly available on the internet, or to distribute or otherwise use the documents in public.

If the documents have been made available under an Open Content Licence (especially Creative Commons Licences), you may exercise further usage rights as specified in the indicated licence.

discussion paper



WISSENSCHAFTSZENTRUM BERLIN
FÜR SOZIALFORSCHUNG

SOCIAL SCIENCE RESEARCH
CENTER BERLIN

FS I 96 - 311

Bridging the Finance Gap for Small Firms

The role of information flows across large firm-based
production networks in supplying finance to small firms:
the case of France

Bob Hancké / Sylvie Ciepły

August 1996
ISSN Nr. 1011-9523

Research Area:
Labour Market and
Employment

Research Unit:
Economic Change and
Employment

Forschungsschwerpunkt:
Arbeitsmarkt und
Beschäftigung

Abteilung:
Wirtschaftswandel und
Beschäftigung

ZITIERWEISE / CITATION

Bob Hancké / Sylvie Cieply

Bridging the Finance Gap for Small Firms

The role of information flows across large firm-based production networks in supplying finance to small firms: the case of France

Discussion Paper FS I 96 - 311

Wissenschaftszentrum Berlin für Sozialforschung 1996

Forschungsschwerpunkt:

Arbeitsmarkt und
Beschäftigung

Research Area:

Labour Market and
Employment

Abteilung:

Wirtschaftswandel und
Beschäftigung

Research Unit:

Economic Change and
Employment

Wissenschaftszentrum Berlin für Sozialforschung
Reichpietschufer 50
D-10785 Berlin

Abstract

This paper discusses finance problems of small firms. Since small firms and banks belong to different economic worlds, as a result of which information asymmetries emerge, credit rationing leads to sub-optimal financing arrangements. The paper analyses institutional solutions to these information asymmetries between banks and small firms and argues that, as a result of the political-economic development of France since the Second World War, production networks around large firms have become the institutional solution for the finance problems of small firms. These intricate links allow for multi-layered information, which can be meaningfully understood by both, to flow smoothly between large and small firms. The paper concludes by raising the relevance of this particular solution for similar problems in other countries.

Zusammenfassung

In dem Papier steht das Finanzierungsproblem kleiner Unternehmen im Mittelpunkt. Angesichts der Tatsache, daß Kleinunternehmen und Banken unterschiedlichen ökonomischen „Welten“ angehören und es deshalb zu asymmetrischen Informationsniveaus kommt, folgen aus der Beschränkung von Krediten suboptimale Finanzierungsarrangements. Deshalb werden in dem Papier institutionelle Lösungen für diese Informationsasymmetrien zwischen den Banken und den kleinen Unternehmen analysiert. Bezogen auf Frankreich zeigt sich als Resultat der politisch-ökonomischen Entwicklung nach dem 2. Weltkrieg, daß Produktionsnetzwerke rund um Großunternehmen zu einer institutionellen Lösung der Finanzierungsprobleme der Kleinunternehmen geworden sind, da dadurch die bestehenden Informationsasymmetrien vermindert werden. Das Papier schließt mit der Überlegung, welche Bedeutung diese spezifische Lösung für ähnliche Probleme in anderen Ländern hat.

Table of Contents

1. Introduction	1
2. Worlds of production and financing conventions	3
2.1. The finance gap as information gap	3
2.2. Institutional solutions to market failure: the role of large firms	5
2.3. Managing the French institutional solution: the elite network	6
2.4. France in comparative perspective	8
3. The large manufacturing firm as an interface in finance	9
3.1. The integration of the SME in a commercial network	10
3.1.1. the network as a signalling structure	10
3.1.2. the commercial network of the SME as guarantee	11
3.2. Quality certification: the construction of public information	12
3.3. Quality audits by the large firm: vehicles for information	13
4. Delegation of finance to the large firm	14
4.1. Long and medium term inter-firm credit	15
4.2. Local development funds	16
4.3. Finance flows in the industrial district	16
5. Conclusion	18
References	21
Notes	24

1. Introduction

Since the early 1980s, scientific observers, business analysts, consultants and policy practitioners have drawn attention to the re-emergence of small firms as important economic actors. A vigorous debate, involving researchers in very different disciplines —economics, comparative political economy, industrial sociology, political science and policy sciences— ensued on the role of SMEs in economic development (Acs and Audretsch, 1990; Piore and Sabel, 1984; Loveman and Sengenberger, 1991; Harrison, 1994; Benko and Lipietz, 1992).

Surprisingly enough, up until very recently, this literature has given little attention to a fundamental (and logically prior) question —how SMEs obtained the finance necessary for their activities. Despite the obvious differences between large and small firms, it appeared as if, in economic theory in particular, they were treated as “small” versions of the large manufacturing firm, without further attention to whatever industrial specificities they may have.

However, finance in general and credit in particular is especially critical for SMEs, since they are too small to finance themselves through retained earnings and too unpredictable for equity financing, yet belong to a fundamentally different world from the banks —the volatility and instability of the entrepreneur versus the risk aversion and conservatism of the financial world— which makes access to credit difficult.

In recent years, the problem has received more systematic attention. Deeg (Deeg, 1992) and Vitols (Vitols, 1995) discuss the financing of SMEs in Germany, and go into detail about the institutional solutions provided by the German political economy: locally managed boards of local savings banks evaluate credit requests. In a related way, (Dei Ottati, 1994) discusses the intricate financing and production structures in (for his purposes idealtypical, but in reality Italian) industrial districts: through a mechanism of generalised exchange —interlinking credit is the technical term— small and large firms in an industrial district can use each others resources for investment.

This paper is a contribution to that debate. It argues that a specific institutional solution exists for the finance gap between SMEs and banks in France: the integration of the SMEs, as suppliers to large firms, into networks of administrative, industrial and financial elites.

Since the finance gap has its roots, in our view, in information assymetries, this information gap needs to be bridged in order to resolve the liquidity

problems. The institutional solution provided in France builds on the central role of the large firm in the French industrial landscape. The large manufacturing firm acts as a go-between in the relationship between banks and SMEs. Because of its position vis-à-vis the small firm, it has a vast amount of operational *inside knowledge*, which, through the cohesive elite networks at the top of the French economy, is transferred to the banks —either as hard evaluations, or as signals about the estimated condition of the SME. This information then becomes part of the evaluation package that the bank uses in its assessment of the SME's financing question. In exchange for the “extra” information, obtained directly or indirectly through the LMF, the bank grants credit. If the bank remains uncertain about the financial risk associated with the SME, the large firm can, relying on the information it has at its disposal, become the prime financier for the small firm.

A few important limitations of the analysis in this paper should be addressed. First of all, it only deals with suppliers to large firms, not with other SMEs. Large firm intermediation in the relationship between the SME and the financial sphere is, as far as we can tell, specific to the supplier-buyer relationship.¹ Suppliers therefore are very different from other small firms: it is precisely the relative lack of support from larger firms that they can associate themselves with, which makes other types of firms especially vulnerable to the vicious cycle of underfinancing as a result of the finance gap. The machine tool sector and the textile industry are the prime examples of sectors consisting of many SMEs who produce directly for the market without being integrated into larger networks. Both went through severe crises in the 1980s, and succumbed to international competition or relocated in low-wage countries (Ziegler, 1994; Levy, 1994). Secondly, we also exclude groupings of SMEs who, by virtue of their combined size, have access to finance the way large firms do. Third and last, because of the institutional focus of the paper, it should be clear that what we say is only meant to apply to suppliers in France. It is only in France that the finance gap is bridged through the large firms, which belong to both the SME and the financial world. This being said, it should be clear that certain elements that we describe may be important in other countries as well, and we certainly hope that other researchers will be stimulated by our analysis to pursue similar ideas.

The paper consists of four parts. The first explores the theoretical relevance of studying small firm finance, and embeds the argument of the paper in the broader institutional literature. The second discusses the signalling effects in the relationship between the large firm, the small firm and the bank. The third discusses the delegation of finance to the large firm, and the final section concludes by recapitulating the main points of the paper.

2. Worlds of production and financing conventions

Small and medium-sized firms (SMEs below) do not belong to the same “world of production” as the large firms (Salais and Storper, 1993; Storper and Salais, 1992). The existence of SMEs is a result of their flexibility, i.e. their capacity of responding to non-anticipated fluctuations in demand, and of their specialisation in dedicated markets (Penrose, 1963; Berger and Piore, 1980). SMEs therefore are, in Salais and Storper’s terms (Salais and Storper, 1992), primarily located in the “Marshallian” world of production, where quality and versatility are the prime determinants of success, instead of the “industrial world” of standardised mass production, the vestige of the large firm.

2.1. The finance gap as information gap

Financing, however, is organised around the *problématique* of large, mass-producing firms. Banks use existing capital as collateral to loans —of which large firms, by definition, have more— evaluate investment projects in terms of the stability and certainty of their return —a direct function of the economies of scale associated with large firm strategies (see, for the continuing salience of economies of scale, Piore, 1993)— and are generally averse to the type of flexibility associated with economies of scope.

SMEs and banks thus belong to fundamentally different worlds: banks to the world of stability and risk aversion; small firms to that of volatility and entrepreneurship. And since they belong to different worlds, the usual (or better: “normal”) flow of information which structures financing conventions, is hard to sustain. The information from one world is almost “incommensurable” (borrowing the late Thomas Kuhn’s notion on competing scientific paradigms) with the evaluation criteria used in the other. The bank has no instruments to evaluate SMEs: the net value of firms is too low, and the industrial project too ephemeral and specialised for banks to understand. Because of this fundamental incommensurability, small firms are, in principle, caught in a vicious cycle of underfinancing and technological backwardness: unable to obtain credit, and too small and volatile for public offerings, SMEs almost naturally end up as traditional producers. The information asymmetries results in a finance gap (Binks, et al., 1992).

This universal problem of monitoring small and medium-sized firms takes on a particular salience in France where *Malthusianism* remains the dominant SME ideology, even in the late 20th century. Since SMEs are very frequently still family enterprises, owners prefer to keep all information on the operation of their firm from outsiders. The necessary information to assess the economic health of the firm is often kept even from the work force, despite legal

provisions for the dissemination of information to works councils.ⁱⁱ The practical alternative to bank financing is the stock market. For three reasons, however, French SMEs appear to be very unfavorable candidates for that. The first problem is the Malthusian nature of the small firms. One could, in the limit, envision the pater familias/company owner discussing the future of the company with a banker, even though the fear of the omniscient French state checking the books as well (through the ownership of banks) will certainly create some hurdles to the depth of trust in this relationship. But it is almost impossible to imagine a French family-owned SME to "go public," issue shares and be subject to relatively strict accounting and publication rules. French banks, moreover, are notoriously centralised and incapable of addressing their clients on their own terms, thus enlarging the finance gap (Quack and Hildebrandt, 1995). Second, as elsewhere, SMEs are usually simply too small and unstable to be able to issue stock credibly.ⁱⁱⁱ If banks are unable to assess risks, how would others be able to do so? Finally, the stock market has up until very recently basically been entirely marginal in financing French companies —true for the large firms, but even more so for the small firms.^{iv}

The usual bank response to this situation is *credit rationing* (Stiglitz and Weiss, 1981). Since every banker is supposed to be able to attribute a subjective default value to every request for funds, there is a threshold, below which credit becomes inaccessible for a firm. SME markets are more unstable than others; a condition which will translate into a relatively lower credit threshold — and therefore higher credit rationing (Cieply 1995b). In short: the information asymmetries lead to a sub-optimal financing situation.

This market failure problem can be resolved through *experts* (Knight, 1921; Rivaud-Danset, 1995). In order to evaluate the credit requests, the bank could appeal to an outside expert, who understands the markets of SMEs sufficiently to be able to assess the investment project of the SME. These experts are the only ones capable of objectifying the SME's (subjective) default probability. As a result, some SMEs, to whom credit was denied under the first response of the banks, will be able to obtain credit, while some projects which fell below the subjective threshold, but on false premises, will not be granted credit. The use of experts thus increases the allocative efficiency of the credit system.

In what follows, we will demonstrate that the French situation is analytically comparable to the expert solution described above. We make one central assumption, i.e. that the bank has limited in-house expert capacities, since these are concentrated in a limited number of departments (study and research department, for example) inside the bank; this forces them to look for outside experts. Furthermore, for the sake of simplicity we assume that one expert inside the bank follows one sector. Given the relatively high transaction costs associated with the evaluation of credit requests, this implies that small sum projects are excluded from this evaluation (see Psillaki and Mondello, 1995 for

an elaboration of this argument), which *de facto* excludes most SME requests for finance.

2.2. Institutional solutions to market failure: the role of large firms

The stalemate that ensues as a result of the informational asymmetries in the relationship between SMEs and banks cannot be resolved without recourse to other, largely non-economic resources. Since the distribution of those extra-economic resources —political and social institutions— is a result of history and therefore different for different institutional frameworks, solutions to the market failure problems identified above will tend to differ geographically (see Granovetter, 1985, for this argument in its most general way, and Deeg, 1992 and Vitols, 1995, and Dei Ottati, 1994, on the specifics for SME financing in Germany and Italy, respectively).

The main institution in the French context which provides the resources for the solution of these problems, is the large manufacturing firm (LMF henceforth). LMF —*grands groupes*, as they are called in France— play(ed) a central role in the country's postwar economic development. In 1988, roughly half of the industrial production in France took place in the 25 largest concerns and firms; the 30 largest firms accounted for over 50% of exports (Holcblat and Husson, 1990). Beside being the most important industrial agents in terms of contribution to GNP since the Second World War, they also indirectly control the fate of many suppliers, through supplier networks, sub-contracting arrangements and the purchase of machine tools.

As in many other countries, French large firms too have reorganised their activities fundamentally in the 1980s. Once typical vertically integrated large corporations, French LMF started to outsource many of their activities and restructured their ties with their suppliers. In response to increased competition and market volatility, large firms reorganised their operations and reduced their activities to what they considered their "strategic core." Many of the sub-contracting activities which used to be a "logical" part of the firm, were gradually transferred to outside suppliers, with whom the companies had simultaneously much closer and looser ties. Closer because the large firms involved the suppliers in strategic areas such as product development and technology acquisition; looser because whatever preferential relationship existed with some suppliers disappeared.

Gradually, as this process unfolded, the firms began to experiment with new arrangements. Instead of relying on a relatively large number of suppliers to deliver a multitude of small parts which are then assembled on the LF's premises, large firms sub-contracted these subassemblies and demanded from

their suppliers that they become systems suppliers, responsible for product development, delivery and quality (Sabel, 1993). As a result of this reorganisation of industrial activities, LMF and SMEs thus find themselves in a much tighter relationship than before; one in which the SME has virtually become a part of the large firm.

Yet characterising the relationship between the LMF and the SME as one of roughly equal partners in an industrial project, would not do justice to the finer details of the situation in France. Most fundamentally, the relation—in France as elsewhere (Harrison, 1994)—is fundamentally asymmetric: in France, the large firm controls the small firm without fear of reversal of the roles. SMEs hold no particular knowledge beyond the LMF's grasp, and even though the relationship may appear as "trust" from the outside (see Lorenz, 1988; Baudry, 1994, Baudry, 1995), at regular time intervals, the large firm reserves the right to redefine the relationship, up to the point of a total breakdown in the relationship—i.e. termination of the contract—if the SME does not meet the anticipated contractual obligations. Since there is no risk of the SME holding up the large firm,^V the large firm ultimately controls the relationship.

These power asymmetries are the basis for the relations between large firms and SMEs in contemporary France. They allow the LMF to force the SME to accept levels of intrusion that they would be hard-pushed to accept in many other situations. For example, even though all suppliers accept quality checks, in France such operations frequently amount to nothing less than full-fledged industrial and financial quasi-audits of the SME (more details later). These and similar informational links give the LMF deep knowledge of the industrial and financial situation of the SME.

2.3. Managing the French institutional solution: the elite network

The second institutional characteristic of French capitalism that is of interest for this analysis, is that both directly and indirectly, French firms are integrated in a broad network, organised by the state, which integrates administrative, financial and industrial elites.

The existence of this elite network has been documented for a long time, at least since Shonfield's characterisation of the French political economy as a conspiracy of big business and the state (Shonfield, 1965: 128; Birnbaum, 1994; Suleiman, 1979; Bourdieu, 1989; Bauer and Bertin-Mouro, 1987; Bauer and Bertin-Mouro, 1995). It has its basis in the educational system. After a highly competitive concours, the best young students are admitted to the *grandes écoles*, where they are prepared for a career in public administration.

After another round of tortuous exams, the top of these classes then moves into the *grands corps*, where they spend a few years at the highest level of the state apparatus. Through the typically French system of *pantouflage*, these people are parachuted at or near the helm of France's large companies or banks. The career track then typically takes one of two forms. The first is the circulation between the leadership of banks, industry and the state; the other is the gradual (but nonetheless fast) climb from the sub-top to the top of a company.

Several independent assessments (Bauer and Bertin-Mouro, 1995, Birnbaum, 1994) conclude that the circulation of elites from the state to finance or industry (and increasingly also back into the state -see Rouban 1994) has increased over the last 10 years compared to the previous period. In numbers: 32% of the CEOs of large companies were transferred from the *grands corps* in 1985, 38% in 1993. In 1985, 55% of the CEOs of large companies were students of three schools—*Polytechnique*, *ENA* and *HEC*. In 1993 this number had increased to 60%, an increase almost solely accounted for by the “*enarques*,” the graduates of the *ENA* (Bauer and Bertin-Mouro, 1995). Instead of losing importance as a result of economic and industrial modernisation, the elite network actually gained in importance throughout the 1980s (Suleiman, 1995).

This network provides a solution to the problems associated with information asymmetries, since for the bank—or more generally the financial sphere—the large firm bridges the incommensurability problems resulting from SMEs and banks belonging to fundamentally different worlds. The reason that the large firm can, is that it belongs to both.

With the SME, the large firm has direct industrial links and can bring its own expertise to bear on those links: it can evaluate the industrial project of the SME in ways that the banks generally cannot. The large firm not only has deep general knowledge of production technology and product markets in the industry where the SME operates, through informational channels specific to the large firm-SME relationship in France, it also has detailed specific knowledge about the actual state of the SME. In short, the fundamental informational asymmetries endemic to the bank-SME relationship simply do not exist in the large firm-SME relationship.

Within the large firm, the purchasing function, comprising both the purchasing department and the supplier selection and support services translate the rough technical-industrial data into more synthetic data, which can be used by the financial departments. Quality control, quality audits and management information systems are all designed with one idea in mind: to provide management with summary information about parts and products usually expressed in ways that are both useful and readable to those outside the immediate production sphere as well, most importantly to those who

negotiate contracts with suppliers (frequently lawyers and top management services). This is the point where information which was originally destined for workers and engineers only, has become extremely synthetic, standardised and data which can easily be mobilised and used by many different people with different goals—even the banks.

The flow of this information between the large firm and the bank, in turn, is organised through the broader political-economic elite network which organises the French economy and administration at the highest level. Since these people are socialised in the same educational channels, belong to the same *grands corps*, and have roughly the same experience after their school years, they share a common understanding of (a) how to detect and define issues, and (b) how to evaluate and respond to them. They are, in other words, because of their educational and professional experience, socialised into seeing, understanding and responding to problems in very similar ways. Put simply, they speak the same language (Bourdieu, 1989; Kadushin, 1995).

Moreover, since members of this network frequently move in and out of top-level positions in the industrial, financial and administrative world, the elite network manages their career on the basis of their reputation in the network. According to a recent study on the social composition of large firm CEOs in France, over 80% of current top management had a career in public service and/or formerly or currently state-owned banks and financial institutions (Bauer and Bertin-Mouro, 1987; Schmidt, 1996). Reputation monitoring within this network thus gives banks an additional mechanism to reduce financial risk.

Two things, as this short discussion suggests, therefore make up the specifics of the French case: the relationship between the PME and the LMF, which structures the information flows between them, and the network which exists between the large firms and the banks. These two elements explain how SMEs obtain access to finance. However, they also delineate what is particularly French in this set-up.

2.4. France in comparative perspective

Some of the elements discussed in this paper are vaguely reminiscent of Japan, where the relationship between the LMF and their suppliers are structured within the *keiretsu* groupings. In exchange for loyalty to the LMF, the supplier then has the guarantee of order by the large firm, and the large firm supports the SME in ways that are very similar to what happens in France, among others with financiers (i.e. the main bank and its affiliates) (Aoki, 1990; Asanuma, 1989). Yet two elements, critical for the operation of the French system, appear not to exist in the Japanese context.

The most important is the asymmetrical distribution of exit options: the possibility of the large firm in France to leave the relationship. If a LMF does something similar in Japan, the suppliers' association would bring its power to bear on the LMF, its strategic partners, company union and even the banks, who would immediately use their power to redress the relationship. In short, the relationship is far more symmetrical in Japan than it can ever be in France. Additionally, despite appearances to the contrary, the elite network does not play the same role in Japan. There is some kind of *pantouflage* (van Rixtel, 1995), but it is differently organised. It involves high-level civil servants who are parachuted into top-management of holdings and banks, and whose sole job it is to smoothen the relationships between the firm and the relevant ministries. Yet they do not necessarily belong to the same elite, and there is, because of the retirement situation, no way back into the state apparatus.

What follows elaborates the institutional argument on France in detail. Section 2 deals with the large firm as an interface in the credit relationship of the SME. We first address the signalling effects in the triangle large firm-SME-bank. Then we discuss the way substantive information that the large firm has on the SME, is used by the bank. Section 3 deals with the situation where the bank does not grant credit, but the LMF itself finances the SME.

3. The large manufacturing firm as an interface in finance

The relation between banks and firms is usually analysed as a bilateral relationship. The firm provides information to the bank, which the bank analyses and, as the case may be, decides to grant or to refuse credit. By and large, two parties are involved in the relationship: the financial agent and the industrial enterprise.

Yet the relationships between firms, in this case between SMEs and their industrial and commercial environment, contains relevant information for banks in many different ways. Firstly, the existence of a commercial contract with a signature from a LMF buyer assures the bank that the SME is a sufficiently serious industrial partner for the large firm and therefore a lower risk to run for the bank. Secondly, quality certification according to ISO 9000 norms (in its local or firm variants) have the same effect: being awarded the ISO certificate (or AFAQ certificate, as it is called in France), is the equivalent, in the world of SME finance, of a stamp of "proper risk." Thirdly, tailorised quality audits of LMF who are customers of the SME, signal to the bank that the supplier has been checked, controlled and approved by the LMF, thus indirectly increasing its rating for the bank.

These three types of relationships have the same mechanism at their basis: they reduce the bank's risk by virtue of the information of the industrial relationship between large and small firms. The information is, in other words, public information.

3.1. The integration of the SME in a commercial network

Increasingly, as many observers noted over the past decade, the relationships between large and small firms have changed in character, from relatively atomised, purely contractual relationships to strongly integrated "organic" production networks, organised around relational contracts, or wider technological or commercial networks around large firms (Sabel, 1989; Harrison, 1994).

Being part of such a network with established large firms at their core, has two types of effects on the access of SMEs to capital. First, *ex ante* the existence of a commercial or sub-contracting arrangement or of an industrial partnership between a LMF and a non-established firm, provides a signal for the banks about the quality of the SME and therefore of the risk associated with lending. Secondly, *ex post* the existence of a contract provides a final repayment guarantee for the bank.

3.1.1. the network as a signalling structure

When an established large firm chooses an industrial or commercial partner among non-established firms, it indicates to the bank the quality of the SME. Since the small firm is usually a supplier to, rather than a client of the large firm (Duchéneault, 1995: 195), the commercial contract between the small and the large firm formalises the existence of the SME's market and demonstrates the relevance of its core activities to outsiders. The supplier relationship reduces the uncertainties of the SME in its market: it stabilises demand for its products. Since supplier contracts are, as a rule, concluded for the life cycle of a product, the client firm can not easily change suppliers. And since the supplier relationship was conceived because the large firm either lacked inside knowledge of technology or products, it is equally hard to make the product itself. The large firm thus guarantees the small firm the production volume needed to write off investments.

Negotiations on price-setting and the conventions on price revisions also allow the SME to be(come) innovative and flexible. As a rule, LMF do not reappropriate the full profits resulting from productivity improvements and economies of scale. The reason is that such practices would not really be in

their interest, since they reduce the capacities of the SMEs to be innovative, they may jeopardise the quality of the products, and they may even make the SME less flexible to respond to market fluctuations. The more equitable redistribution of profits thus also protects the LMF, who does not run the costs associated with bankruptcy of a supplier —finding another one, production stops, and loss of customers.

Once this position of the SME in its industrial and commercial world is taken into account, the non-established firm suddenly appears less fragile to the financial world, since its markets are less uncertain and more diversified. In 1990, more French SMEs were suppliers than in 1980, but in each one of them, sub-contracting accounted for a smaller proportion of turnover than ten years before: 52% of the SMEs makes less than one-third of their turnover as sub-contractors in 1990, against 38% in 1980.

3.1.2. the commercial network of the SME as guarantee

The second way the insertion of the SME in wider networks matters to the financial world is as simple guarantee for credit repayment, i.e. as collateral. This is related to the practice of commercial discounts, protected by the Commercial Code in France. The discount, which is found among medium-sized enterprises in particular, is a credit which is extended by the bank on the basis of the debts that the clients of the small firms has a result of a commercial contract. The banker thus makes credit available for the holder of a contract against the transfer of (part of) the rights to the fruits of the contract. Such a discount presents only a minor risk to the bank because of the provisions of solidarity of contracting parties against creditors in commercial law: the law treats all creditors on an even footing.

The mechanism at the basis of this information-credit loop, is that the bank, instead of analysing the creditworthiness of the SME directly, analyses the creditworthiness of the debtor, i.e. the LMF. The only action the bank undertakes with regard to the SME, is ascertaining that it does not provide false information, such as false letters of intent, false bills, or bills which have already been submitted to another credit institution.

This practice of mobilising outstanding debts through the use of letters of commitment (*lettre de change*) from the large firm thus gives the SME the opportunity to use its commercial relationships in order to obtain credit. Essentially, the bank moves the risk from a non-standard company (the SME) to a firm which is recognised as a very reasonable risk by the banking community (the LMF).

3.2. Quality certification: the construction of public information

Since a few years, and as part of a wider modernising drive, LMF in France have begun to emphasise “quality,” i.e. making things right the first time. Whereas up until then, competitiveness was primarily the product of a combination between progress in product technology and low relative costs, in the mid-1980s large exporting firms actively initiated programs to increase quality. The idea behind this was that many problems of production costs were, in fact, accumulated quality problems (Lucas and Joco, 1992).

Since between 50% and 85% of the value of a good is produced by outside suppliers, quality of final products is to a large extent the outcome of quality in supplied parts. The LMF's increased quality preoccupations therefore quickly led to attempts to impose stricter quality requirements upon suppliers. LMF thus installed a variety of mechanisms to monitor quality, first after receipt of parts and later, when this proved difficult because of JIT delivery systems (where parts are delivered when needed in production and therefore cannot be checked between delivery and utilisation), primarily through pro-active monitoring systems. These quality monitoring systems between large firms and SMEs are at the basis of the information flows between large, small and medium-sized enterprises and banks.

Without doubt the most wide-spread of such monitoring systems are the quality certification systems. In line with developments in other countries and in part as a way of benefiting of the favourable relative cost-competitiveness of French industry, LMF are demanding from their suppliers that they be certified according to ISO 9000 norms. These quality norms assess how a product is made, and the resources devoted to and the organisation in place for monitoring (a) that pre-set quality standards are attained and permanently monitored; and (b) that corrective action is taken when errors are found. The ISO 9000 procedure, which exists in different national, sectoral or company variants, essentially serves to demonstrate that a company can reflexively correct its operations. ISO 9000 norms are, unlike DIN norms or most other categories of ISO norms, procedural norms: they evaluate the process used to make a product, in theory without consideration of the product itself.

In the relationship between the LMF and the supplier, ISO 9000 norms also serve another, related but still somewhat different function. It comes close to assuring the LMF that the SME can adjust its production in a similar way. Being good at making a particular part now, can be the result of deep, perhaps extremely specific knowledge about that part, or of being able to flexibly adjust production and quality to different demands. In the first of these two possibilities, parts suppliers cannot guarantee that they can adjust to volatile market conditions and/or rapid technological or material innovations, since their capabilities are tied to stable markets, in technologically mature industries. In

the second case, the LMF knows that the SME masters the instruments to adjust itself to new market conditions or technological shocks. ISO 9000-type procedural norms provide (the closest thing to) guarantees to the large firm that the SME can survive extreme demands on its capacities. This explains why many large firms, in France and elsewhere, have pressured their suppliers to be ISO 9000-certified (Baudry, 1994).

The practical organisation of quality certification is left to a private, quasi-cooperative agency, The *Association Française pour l'Assurance de la Qualité* or AFAQ, sponsored by the industry federations and the large firms, and whose goal it is to test, audit and improve the quality system in the companies. The AFAQ sends a team consisting of a certified quality auditors and a sectoral expert. For both of these, professional knowledge is the basis for their appraisal: quality norms are very different in a poultry farm than in ceramics or car parts, and hence the double angle of quality and sectoral knowledge. For their certification, the firms pay the AFAQ a fee. Through a transfer of authority from the state agency responsible for norming, the *Association Française de Normalisation*, the AFNOR, to the AFAQ, (they signed an agreement in March 1993, mutually recognising each other's certificates) the quality certificates bear an official *imprimatur*.

The primary and secondary functions of quality certification for the LMF —the assurance of quality and the relative certainty of reflexive adjustment to changing market conditions— thus are signalling elements in the triangle between the SME, the LMF and the bank. They demonstrate to the bank that the SME is positioned favorably in a volatile world, and that its so-called “industrial project” can be regarded as viable. Put more bluntly: an AFAQ-certified company is, in every possible regard, a safer risk for a financier than a company that is not certified.

3.3. Quality audits by the large firm: vehicles for information

A second important instrument, which serves a similar purpose in this triangle, is the quality audit. Whereas many large firms rely solely on quality certification à la ISO 9000 in their selection of subcontracting partners, a sizeable group retains its own in-house system of private and customised quality audits.^{vi} These are exercises whereby the LMF sends out a team of their own experts to examine the supplier's operations in great detail. The team examines all the processes that play a role in the production of the part or the service that the supplier delivers, and that bear on quality, delivery, price or other relevant aspects. By focusing on aspects of the production process instead of the spot-checking associated with product quality, the larger firm assures a proper understanding of the supplier's capability to follow the technological path that the large firm takes or may take with its products.

However, and much more importantly, the quality audit is not limited to what is immediately relevant for the part or service under the supplier's responsibility. During the audit, the team also examines most other components of the firm's operations: training and recruitment, balance sheet, finance, links with other SMEs and larger firms, product development capabilities and market strategies, technology, etc. In short, the so-called quality audit, as should be apparent from this short list, is in reality a true audit of the entire company. This information, read through the eyes of the experienced auditors typically found in these auditing teams (all have many years of factory as well as headquarters and financial experience, which also explains why there are only few of them), will allow them to assess the potential of the supplier for long-term process and product innovation with relative confidence. Some go even further: *Renault*, for example, sends out a team of supplier consultants to help the supplier improve its performance.^{vii}

These three mechanisms —discounting contracts against bills, quality certification and customised quality audits— which all rely on public information, are found combined in practice, and therefore reinforce each other's impact. All three work according to the same mechanism: the existence of a relationship between LMF and SME itself, without further, often more intimate knowledge of the substance of this link, is a signal to the bank that it should treat the financing requests of the SME seriously.

Two assumptions were critically important in this treatment of the use that the SME can make of its commercial, technological and productive network relations in order to obtain finance. The first was the absence of opportunism (i.e. deliberately false signals) from the part of the SME, the other was that the bank trusted the information provided by the SME as valid. Both assumptions are reasonable if the existence of interfirm commercial or productive ties is public knowledge, accessible to all actors, and if there are supplementary mechanisms —such as common socialisation, trust generated through iterated interactions, and reputation monitoring— which reinforce the bank's conviction that the LMF expert will not willfully distort information.

4. Delegation of finance to the large firm

If, instead of relying on the LMF as an expert, the bank chooses to ration credit, a different, complementary form of finance could develop in response, which is called "*double intermediation*" in the literature (Dei Ottati, 1994): the established large firm, which itself obtained credit in a regular manner in the financial world (first intermediation), directly or indirectly becomes a financial intermediary

itself. Direct intermediation means that the large firm grants payment delays to a client, grants long or medium term loans or that the LMF takes a participation in the SME. Indirect mediation refers to the provision of services, licenses, technology transfer etc. Secondly, the LMF supports local SMEs financially and technically as part of a broader strategy of local economic development (sometimes compensating the local impact of a large restructuring). Credit provision in industrial districts follows a third large pattern: here, the LMF acts as a bridge to the financial world for all the SMEs in the district.

4.1. Long and medium term inter-firm credit

The first type of credit is the one where the LMF directly or indirectly subsidises activities by the SME. The LMF provides the SME with services and/or technology that are relatively hard to obtain for the SME because of its proprietary nature, relatively expensive or simply inexistent but impossible for the SME to create —however, they may be necessary for the SMEs competitive survival. LMF, for example, frequently organise and fund training programmes for the SME's workers or engineers, helps install quality monitoring tools, makes machinery available to the supplier, subsidises the acquisition of new technology or licenses, helps the SME explore new products or markets, and generally put their expertise at the supplier's disposal. What are, given the total turnover of the company, relatively small investments for the LMF, may be of existential importance to the SME.

Why and how do LMF proceed to such a transfer of means and resources, and engage in this type of support “in kind”? “Why” is a relatively easy question to answer. The process of industrial reorganisation in the 1980s has forced LMF and SMEs to forge such close ties. Even though SMEs are by far the more dependent party in the relationship, neither of the two is fully autarkic, and both of them therefore have to invest in the relationship: the supplier by providing high quality goods at low costs, the LMF by defining the relationship as long-term.^{viii}

By doing this, the LMF also safeguards its own future: by reducing the risk of bankruptcy of the supplier, the LMF assures continuity in its own operations. These types of *interlinking credits* (Dei Ottati, 1994) thus allow the LMF to stabilise the market of the SME and thus to safeguard the industrial partnership.

“How,” then, is related to the information flows discussed before: the quality audits and quality consulting services. Through these recurrent in-depth investigations, the LMF has a detailed view of the supplier's product market,

technology, training and financial situation, which is used to assess the future of the partnership link. The LMF knows, as discussed before, both the strong and weak points of the supplier, and can adjust its support accordingly.

4.2. Local development funds

The second type of credit is part of the policy of large firms to simultaneously make their local environment more dynamic and to stabilise it. For many reasons, the LMF considers itself responsible for the vitality of its local economy. First of all, the LMF needs a dynamic network of SMEs as suppliers and subcontractors, especially in situations of just-in-time delivery. Secondly, the existence of such an active industrial environment will allow the large firm to keep its own social peace, by being able to transfer employees to new or existing supplier firms and thus further the employment of workers in the group.

Specialised financial institutes, frequently tied to the large firm through ownership or partnership links, grant medium and long-term credits to the local SMEs. Such "*reconversion societies*" (sociétés de reconversion), which are created by the LMF in France have exactly this goal: they organise credit flows among their local suppliers and other local SMEs. On occasions, these loans are transformed into subsidies if the SME hires workers from the large firm associated with the loan, and the LMF will even help the SME administratively or consult it on strategy and business plan.^{ix}

4.3. Finance flows in the industrial district

In the industrial district, finally, the financial links between LMF and suppliers take a related but different form. The reason why this form of economic organisation commanded such attention in the 1980s and 1990s, was that they were able to compete successfully with large firms, despite their presumed diseconomies of scale and their reliance on traditional craft methods (Marshall, 1919; Becattini, 1990; Sabel, 1989).

After a few years of research into the operation of industrial districts, especially those in Germany, but afterwards in other countries as well, a major corrective to the initial images was introduced. In many cases, it turned out, the districts were tied into the world economy as much through the intermediary of large firms as through their own activities, and in most cases, it was simply impossible to think of the regional economies that thus emerged without also thinking of the large firm that organised them. (Streeck, 1992; Harrison, 1994; Mueller and Loveridge, 1995). In short, the conclusion of these two waves of

research was that large firms remained critical actors, even in the industrial districts.

This observation is crucial for a proper understanding of why the industrial district is the fourth form of SME finance through the large firm (Dei Ottati, 1994). In an industrial district, the argument goes, the division of labour between firms is such that it reinforces what Durkheim called “an organic social solidarity:” the activities of one firm are indispensable to the survival of all and vice versa, analogous to the mutual dependence of families in subsistence economies. Because of this, co-operation is necessary, and this reinforces pre-existing trust relationships. Trust is therefore a resource whose value grows with use (Dei Ottati, 1994). Relying on trust in economic transactions clears the way for more diffuse relationships, which makes possible economic transactions—at relatively low cost—which would otherwise be very hard to carry out.

In such a system, trust becomes the medium that clears the way for information, which, in turn, becomes the basis for the extension of credit in the district. As Dei Ottati (Dei Ottati, 1994:540-41) points out, only the established firm extends credit. This firm has inside knowledge about production technology and capabilities of the SMEs in the district, and has the links with world markets, and is therefore able to assess investment projects of the (usually sub-contracting) SMEs. It directly finances investment projects, including start-ups of the SMEs—often by discounting the loan in part from the orders of the large firm with the sub-contractors.

The large firms also act as gate-keepers for bank finance. The double inside knowledge is equally useful for banks: they can, as described above, rely on the expert knowledge of the large firm to assess investment projects for them, and trust them because of a combination of local experience of co-operation (which reinforces trust) and a socialisation of the communicating officers in the bank and the large firm through the same educational, administrative and general career networks. Bank finance in the industrial district is, in other words, a special case of the general principle of delegated selection of investment described above (section 2).

No detailed descriptions of the operations of industrial districts are available which allow us to conclude that these credit mechanisms also play the crucial role in France which they play in the Italian industrial districts. The most obvious explanation for this are the crucial differences in their nature. Whereas Italian industrial districts are, certainly since the initial statements by Brusco (Brusco, 1986) and Piore & Sabel (Piore and Sabel, 1984), associated with industrial dynamism, the parallel cases in France are rather the opposite. The few cases that persisted throughout the postwar period, were the result of residual

“backwardness,” rather than forward-looking dynamism (Ganne, 1992). And in these cases, financing innovation was not a central issue.

On the other hand, “new” districts, which emerged in the high-tech regions — Rhône-Alpes, or the Bassin of Paris— were much closer to a form of industrial organisation that the banks recognised, and were, anyway, centered around large firms. The area around Grenoble, in the French south-east, for example specialises in machine-tools, is highly concentrated, invests heavily in research and development, and has several large firms who stabilise the region: Thomson-CSF, Merlin-Gerin, Hewlett-Packard,... (Courlet and Pecqueur, 1992: 101). For the banks, this setting represents a totally different type of risk evaluation than a “pure” small-firm industrial district would.

However, in the regional economies in the west of the country, even though they borrow only a little from the industrial district model, some of these large-firm centered models are operative. In the Rennes-Laval area, for example, the Citroën plants, which located there in search of a relatively docile, cheap labor force in the 1960s, act as a single interface between its suppliers and the rest of the world, and therefore also the financial world.^x The relationship is not unlike that of the old “notable” in the village, who also was its only link with the central state before modernisation set in after the Second World War (Ganne, 1992).

Industrial districts —or better: regional economies— in France are, even more perhaps than in Italy, therefore dependent upon and a product of the large firms. Local development banks do not exist, so credit cannot flow into the district in this way; surviving “old” industrial districts are signs of backwardness instead of local dynamism, so financing innovation is not a necessity there; and the existing regional economies are firmly anchored in and, hence, also dominated by large firms. It is fair to say that, without the large firms, regional economies simply would not exist in France.

5. Conclusion

Small and medium-sized companies face particular problems when trying to obtain external finance in the classical ways. Their general situation is too far removed from the world that financing sources know well in order for them to neatly fall into the evaluation categories that the banks use. As a result, since the bank cannot use its resources to evaluate the investment plans of the SME, financing by the traditional sources is low for SMEs.

The solution for this *cul-de-sac* is provided by the large firms. They are part of the industrial world of the SME, and thus have the knowledge and expertise to be able to evaluate the request for funds, but also of the bank, and can therefore relay that information to the bank. The mechanism through which this transfer of information is assured, is the dense elite network at the helm of the French economy, which comprises both large firm CEOs and bankers. The members of this network not only are educated in the same schools and received a similar professional socialisation, which allows them to understand each other, they also monitor each other's career in the network closely. Both mechanisms breed trust, upon which the financial relationship is based, which closes the circle. In many ways, as we documented in the paper, the large firm indirectly guarantees the bank that its investment is safe and sound, and when the bank cannot be convinced, the large firm might directly take over some of the financing.

The large firm is therefore the institutional solution to permanently underfinanced SMEs in France. Other countries (may) have other solutions, but we suspect that the large firms play a relatively important role in many other countries as well. The reason is that everywhere in Europe (and the US) large firms have reorganised their activities in order to concentrate on what they consider their core tasks. This, as we discussed for France, changed the basic parameters of the relationship between large and small firms. To some extent, as we suggested at several places in the text, the large firm's action as a go-between for bank and SMEs is also in its own interest. Helping the SME obtain finance also secures the relationship. Precisely these characteristics are also found elsewhere: on the new industrial map, all large firms benefit if their suppliers are dynamic and stable and help in finance is a reasonable *quid pro quo*.

In other words, if industrial restructuring is truly as profound as many observers now agree, the mechanisms that we analysed in this paper for France, may well be or become very important in other countries as well, even though they will graft themselves in different ways upon the prevailing institutional framework which organises the relationships between firms. Some existing financing arrangements, for example, are more favorable to SMEs than others, and legal frameworks make the construction of trust-based relational investment strategies, encompassing large and small firms, more likely in some countries than in others. But the tools are there, and economic actors can decide whether or not to use them.^{xi}

In conclusion, this takes us to a very old, recently revitalised debate in the social sciences. According to a very important current in political economy, dating back as far as Smith and Marx, national economic systems asymptotically converge on a similar, most efficient system as a result of selection through the market (Kerr, et al., 1964). The argument in this paper

suggests something else: even if the problems that companies and (by extension) nations face, increasingly are “objectively” the same, since their definitions and the repertoire of possible solutions are institutionally generated, there will be just as many differences as before in response to these similar market pressures. Convergence remains therefore, even in this most conducive of worlds, a very unlikely outcome.

References

- Acs, Z. J. and D. B. Audretsch, 1990. *Small firms and Entrepreneurship: a comparison between west and east countries*, Wissenschaftszentrum Berlin für Sozialforschung, Discussion Paper FS IV 90-13
- Aoki, M., 1990. Toward an Economic Model of the Japanese Firm, *Journal of Economic Literature*, vol. 28, no. 1
- Asanuma, B., 1989. Manufacturer-Supplier Relationships in Japan and the Concept of Relation-Specific Skill, *Journal of the Japanese and International Economies*, vol. 3, no. 1
- Baudry, B., 1994. De la confiance dans la relation d'emploi ou de sous-traitance, *Sociologie du Travail*, vol. 36, no. 1
- Bauer, M., 1988. The Politics of State-Directed Privatisation: The Case of France. 1986-88, *West European Politics*, vol. 11, no. 4
- Bauer, M. and B. Bertin-Mouro, 1987. *Les 200*, Paris, Le Seuil
- Bauer, M. and B. Bertin-Mouro, 1995. *L'Acces au Sommet, des Grandes Entreprises Francaises. 1985-1994*, Paris, C.N.R.S. Observatoire des Dirigeants and Boyden
- Becattini, G., 1990. The Marshallian industrial district as a socio-economic notion, (in) *Industrial districts and economic regeneration*. F. Pyke and W. Sengenberger (ed.), Geneva: ILO
- Benko, G. and A. Lipietz (ed.), 1992. *Les régions qui gagnent. Districts et réseaux. Les nouveaux paradigmes de la géographie économique*, Paris, Presses Universitaires de France
- Berger, S. and M. J. Piore, 1980. *Dualism and Discontinuity in Industrial Societies*, Cambridge MA, Cambridge University Press
- Binks, M., C. Ennew and G. Reed, 1992. Information asymmetries and the provision of finance to small firms, *International Small Business Journal*, vol. 11, no. 1
- Birnbaum, P., 1994. *Les sommets de l'état. Essai sur l'élite du pouvoir en France*, Paris, Le Seuil
- Bourdieu, P., 1989. *La Noblesse d'État. Grandes écoles et esprit de corps*, Paris, Éditions de Minuit
- Boyer, R. and J.-P. Durand, 1993. *L'après-fordisme*, Paris, Syros
- Brusco, S., 1986. Small firms and industrial districts. The experience of Italy, (in) *New firms and regional development in Europe*, D. Keeble and E. Wever (ed.), London, Croom Helm
- Casper, S., 1995. *How Public Law Influences Decentralized Supplier Network Organization in Germany: The cases of BMW and Audi*, Wissenschaftszentrum Berlin für Sozialforschung, Discussion Paper FS I 95-314
- Courlet, C. and B. Pecqueur, 1992. Les systèmes industriels localisés en France. Un nouveau modèle de développement, (in) *Les régions qui gagnent. Districts et réseaux: les nouveaux paradigmes de la géographie économique*, G. Benko and A. Lipietz (ed.), Paris, Preses Universitaires Françaises

- de Saint Louvent, P., 1991. *Analyse de la perception de la banque par les petites et moyennes entreprises en Grande Bretagne, Allemagne et France*, Bossard Consultant,
- Deeg, R., 1992. *Banks and the State in Germany. The critical role of subnational institutions in economic governance*, Political Science, MIT
- Dei Ottati, G., 1994. Trust, interlinking transactions and credit in the industrial district, *Cambridge Journal of Economics*, vol. 18, no. 6
- Duchéneault, B., 1995. *Enquête sur les PME françaises. Identités, Contextes, Chiffres*, Paris, Maxima
- Ganne, B., 1992. Place et évolution des systèmes industriels locaux en France. Economie politique d'une transformation, (in) *Les régions qui gagnent. Districts et réseaux: les nouveaux paradigmes de la géographie économique*, G. Benko and A. Lipietz (ed.), Paris, Presses Universitaires France
- Granovetter, M., 1985. Economic Action and Social Structure: The Problem of Embeddedness, *American Journal of Sociology*, vol. 91, no. 3
- Harrison, B., 1994. *Lean and Mean. The Changing Landscape of Corporate Power in the Age of Flexibility*, New York, Basic Books
- Holcblat, N. and M. Husson, 1990. *L'industrie française*, Paris, La Découverte
- Kadushin, C., 1995. Friendship Among the French Financial Elite, *American Sociological Review*, vol. 60, no. 2
- Kerr, C., J. Dunlop, F. Harbison and C. Myers, 1964. *Industrialism and Industrial Man*, New York, Oxford University Press
- Knight, F. H., 1921. *Risk, Uncertainty and Profit*, Houghton Mifflin,
- Levy, J., 1994. *Toqueville's Revenge. Dilemmas of institutional reform in post-dirigiste France*, Department of Political Science, MIT
- Locke, R. M., 1995. *Remaking the Italian Economy*, Ithaca NY, Cornell University Press
- Locke, R. M. and K. Thelen, 1995. Apples and Oranges Revisited: Contextualized Comparison and the Study of Comparative Labor Politics, *Politics and Society*, vol. 23, no. 3
- Lorenz, E. H., 1988. Neither Friends nor Strangers. Informal Networks of Subcontracting in French Industry, (in) *Trust. Making and Breaking Cooperative Relations*, D. Gambetta (ed.), Oxford, Basil Blackwell
- Loveman, G. and W. Sengenberger, 1991. The Re-emergence of Small-Scale Production: An International Comparison, *Small Business Economics*, vol. no. 3
- Lucas, F. and P. Jocou, 1992. *Au cœur du changement. Une autre démarche de management: la qualité totale*, Paris, Dunod
- MacLean, M., 1995. Privatisation in France 1993-94: New Departures or a case of plus ça change?, *West European Politics*, vol. 18, no. 2
- Marshall, A., 1919. *Industry and Trade*, London, MacMillan
- Midler, C., 1993. *L'auto qui n'existait pas*, Paris, Interéditions
- Mueller, F. and R. Loveridge, 1995. The 'Second Industrial Divide'? The Role of the Large Firm in the Baden-Württemberg Model, *Industrial and Corporate Change*, vol. 4, no. 3

- Penrose, E., 1963. *Facteurs, conditions et mécanismes de la croissance de l'entreprise*, Neuilly-sur-Seine, Editions Hommes & Techniques
- Piore, M. J., 1993. The revival of prosperity in industrial economies. Technological trajectories, organizational structure, competitiveness, (in) *Technology and the Wealth of Nations. The Dynamics of Constructed Advantage*, D. Foray and C. Freeman (ed.), London, New York, Pinter Publishers
- Piore, M. J. and C. F. Sabel, 1984. *The Second Industrial Divide. Possibilities for Prosperity*, New York, Basic Books
- Pillaki, M. and G. Mondello, 1995. *Financement des PME : coûts de transaction et coordination*, Table ronde : finance et Industrie, Lyon, 24-25 March
- Quack, S. and S. Hildebrandt, 1995. *Hausbank or Fournisseur? Bank Services for Small and Medium Sized Enterprises in Germany and France*, Wissenschaftszentrum Berlin für Sozialforschung, Discussion Paper FS I 95-102
- Rivaud-Danset, D., 1995. Le rationnement du crédit et l'incertitude, *Revue d'économie politique*, vol. 105, no. 2
- Rochard, M. B., 1987. *La sous-traitance: entreprises et emplois. Le secteur de l'électronique professionnelle*, CEE-CEREQ-SESSI,
- Sabel, C. F., 1989. Flexible specialisation and the re-emergence of regional economies, (in) *Reversing industrial decline? Industrial structure and industrial policy in Britain and her competitors*, P. Hirst and J. Zeitlin (ed.), Oxford, Berg
- Sabel, C. F., 1993. Learning by Monitoring, (in) *The Handbook of Economic Sociology*, N. Smelser and R. Swedberg (ed.), Princeton NJ, Princeton University Press
- Sabel, C. F., 1995. Bootstrapping Reform: Rebuilding Firms, the Welfare State, and Unions, *Politics and Society*, vol. 23, no. 1
- Salais, R. and M. Storper, 1992. The four 'worlds' of contemporary industry, *Cambridge Journal of Economics*, vol. 16 no. 2
- Salais, R. and M. Storper, 1993. *Les mondes de production. Enquête sur l'identité économique de la France*, Paris, Éditions de l'École des Hautes Études en Science Sociales
- Schmidt, V. A., 1996. *From State to Market? The transformation of business in France*, Cambridge, Cambridge University Press
- Shonfield, A., 1965. *Modern Capitalism. The Changing Balance of Public and Private Power*, Oxford, Oxford University Press
- Stiglitz, J. E. and A. Weiss, 1981. Credit rationing in markets with imperfect information, *The American Economic Review*, vol. 71, no. 3
- Storper, M. and R. Salais, 1992. The division of labour and industrial diversity: flexibility and mass production in the French automobile industry, *International Review of Applied Economics*, vol. 6, no. 1
- Streeck, W., 1992. *Social Institutions and Economic Performance*, London, Sage
- Suleiman, E., 1979. *Les Elites en France*, Paris, Le Seuil
- Suleiman, E., 1995. *Les ressorts cachés de la réussite française*, Paris, Le Seuil

- van Rixtel, A. A. R. J. M., 1995. *Amakudari in the Japanese banking industry: an empirical investigation*, CEPR/WZB Conference, Berlin, 1-2 December,
- Vitols, S., 1995. *German Banks and the Modernization of the Small Firm Sector: Long-Term Finance in Comparative Perspective*, Wissenschaftszentrum Berlin für Sozialforschung, Discussion Paper FS I 95-309
- Ziegler, N. J., 1994. *Retooling the Industrial Plant. Political Strategies for Technological Advance in France and Germany*, manuscript,

NOTES

-
- i . Despite these limitations, suppliers are an important category of firms in the French industrial landscape. The national statistical office, the *INSEE*, distinguishes between manufacturers of intermediate goods (U04, a proxy for suppliers), equipment goods (U05, a proxy for machine-tools) and consumer goods (U06). In 1990, the distribution of firms with a size between 50 and 500 employees over these categories was: producers of intermediate goods (U04) 3217 firms (33% of total), equipment goods (U05) 2708 firms (28%), and consumer goods (U06) 3805 firms (39%). Also, compared to other European countries, a larger proportion of SMEs in France are suppliers: in 1991, 43% of the small firms realised over one-third of their turn-over as sub-contractors —the corresponding figures for the UK and Germany are below 20% (de Saint Louvent, 1991).
- ii . This appears increasingly true of large firms as well. Labor unions are too weak and lack the competence to evaluate business plans; small shareholders have no access to the books; and class action suits do not, as a rule, exist in France, even consumers have few means at their disposal to counter employers' actions. According to some observers, this explains the rise in CEO-linked legal cases in recent years. Only few of them are actually convicted —but in the absence of other practical means, legal action makes a detailed look inside the company possible (see *Le Monde* 10 Feb 1996 for details).
- iii . Since very shortly, some attempts are going on to create a separate Bourse for SME stocks in Paris. From all accounts, there are major difficulties with this new stock market model, for precisely the reasons outlined above (see the *Economist* 25 Feb 1995; *Libération* 15 Feb 1996 for more on the SME stock markets).
- iv . Things appear to be changing now because the government is selling off the large state-owned firms through public offerings, which by its very nature increases the role of the stock market. However, as several assessments have concluded, instead of truly “privatising” the firms, what appears to be happening, both in the 1986 denationalisations and in those of the 1990s, is that a stable nucleus of shareholders emerged, consisting of a few other major large firms, which acted as a protective shield against hostile take-overs and overly demanding small shareholders. Not surprisingly, the political-economic elite which governs France's administrative apparatus and its large firms (see below) plays a critical role in this reconfiguration of ownership in French industry (see Bauer, 1988; MacLean, 1995).

-
- v . Why this is so, is beyond the scope of this paper; however, it is fair to say that it is probably related to two elements in the organisation of French industry. The first is that in some sectors, despite the extremely oligopolistic structure, companies are involved in fierce, head-to-head competition. Thus, as a result of the 15% dependency rule of the supplier, the SME becomes too independent and there is no guarantee for any of the large firms that the competition will not benefit from the contract that one firm has with the supplier. This is the case, for example, in cars (Renault and Peugeot) and consumer electronics (Thomson, Moulinex). The second reason is that the French system remains one in which the organisation of decision-making in product development is still, despite other steps that have been made to make the system more efficient, extremely hierarchical (Taddéi and Coriat, 1993; Boyer and Durand, 1993; and Midler, 1993). Conceptual work and strategic decision-making power remains at head quarters, while suppliers execute. A report describing the situation in the mid-1980s used the term inter-company Taylorism to speak of the relationship between large firms and their suppliers (Rochard, 1987). Things have changed since then, but the basic structure is still the same.
- vi . The composition of this group suggests the guiding hand of the French state, who uses its economic clout to organise the SMEs into competitive firms. Almost all the companies who have kept separate individual quality audits, even among AFAQ-certified suppliers, are state-owned: e.g. Renault, EDF-GDF, Rhône-Poulenc, ELF, etc. The information was provided by the AFAQ itself during interviews in October 1994. See Note AFAQ/DG/J/251. maj 1994.10.19.
- vii . Interview at Renault purchasing department, 25 Oct 1994.
- viii . Note that the relationship is therefore not one in which the supplier can hold up the LF. The SME has not enough strategic knowledge and the LF can reassign the contract —a costly option, but not prohibitive.
- ix . See, for example, the aid package put together by the French national electricity company: *Développement économique local*, EDF/DII, 1995.
- x . Information obtained during interviews with Citroën management and labour unionists in the area in April 1993. More details are found in *Auto-Hebdo*, the Citroën house magazine. These structures are not unlike what Locke (Locke, 1995) describes in Italian regional economies, and Vitols (Vitols, 1995) for the relations between small savings banks and SMEs in Germany.
- xi . See Steve Casper (Casper, 1995) for the metaphor of the toolkit in analysing the relationships between companies in Germany. Put simply, the argument is that institutional frameworks do not offer a single solution to existing problems, as institutionalists tend to suggest (see Locke and Thelen, 1995), but a wide variety of possible strategies, among which firms can choose. Once chosen, the process may be relatively path-dependent and irreversible, but up until that moment, many choices are open. It could be, of course, that, in addition to the first, a second, third, fourth, etc. branching point appears, itself conditioned by the previous ones, but with a relatively large number of options. Looked at over a longer period of time, it may then appear as if the world could be reconstructed from the bottom up. The central question is how the different strategies are related —are they part of the same, relatively limited family of options, or is everything possible, as Sabel (Sabel, 1995) seems to suggest?