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Corporate Governance: The Role of Other Constituencies

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Corporate Governance:

The Role of Other Constituencies

July 1997

Abstract

The paper discusses the role of various constituencies in the corporate governance of a corporation from the perspective of incomplete contracts. A strict shareholder value orientation in the sense of a rule that at any time firm decisions should be made strictly in the interest of the *present* shareholders would make it difficult for the firm to establish long-term relationships as the potential partners would have to fear that, at a later stage of the co-operation, the shareholders or a management acting only on their behalf could exploit them because of the inevitable incompleteness of long-term contracts.

One way of mitigating these problems is to put in place a corporate governance system which gives some active role to the other stakeholders or constituencies, or which makes their interests a well-defined element of the objective function of the firm. A commitment *not* to follow a policy of strict shareholder value maximization *ex post* can be efficient *ex ante*. Such a system would clearly differ from what is advocated by proponents of a "stakeholder approach", as it would limit the rights of the other constituencies to those which would have been agreed upon in a *constitutional contract* concluded between them and the founder of the firm at the time when long-term contracts are first established.

JEL Classification: D 21, 23, L 21

Key Words: corporate governance, theory of the firm, incomplete contracts

1. The Issues

I would like to start by admitting that initially I had the problem of finding out precisely what it is that I am supposed to talk about today. The topic "the role of *other* constituencies" was assigned to me by the organisers of this conference. Evidently, "other constituencies" must in some way be understood as those which are not the main constituencies or, to put it differently, constituencies other than those whose legitimate and factual role in the context of corporate governance is beyond any reasonable doubt. A common view of corporate governance is that it is about how to make managers act in the interest of shareholders. Thus, it first seemed to me that I was expected to talk about "other constituencies" as opposed to shareholders. However, in a preliminary version of the programme, the complete title reads: "The role of other constituencies: employees, stockholders". Thus my first guess was apparently wrong.

Still in search of a topic, I took a closer look at the programme for this conference. One of the main issues to be dealt with this morning is the role of the board - i.e. the board of directors or the conseille des administrateurs. So I thought I might take the term "others" to mean "other than the board". However, for me as a German this interpretation is also difficult to accept at face value because in the German co-determination system the influence of the employees on corporate governance is meant to be exercised through the supervisory board, whose members include representatives of the firm's workforce.

I finally concluded that if defining my assignment posed a problem, then this only served to underscore the wisdom of the organisers of this conference. I say this for two reasons. One is that they want us foreigners to be aware of the fact that France is a special case, also with respect to corporate governance issues (Pastré, 1997). Specifically, in France shareholders seem to be among the "other constituencies", whereas the central agent is probably the PDG and, with less importance, the conseil des administrateurs (CNPF, 1995). Secondly, they seem to want me to discuss the topic of corporate governance from a very general perspective and not to be misled by my professional background as a financial economist. However, while financial economists would typically subscribe to the narrow conception that corporate governance is

only about how to make the management act in the best interest of shareholders, I would like to emphasise right at the beginning that I do not share this belief, and I shall explain my reasons for this in the present paper.

Thus, I would like to discuss a broader notion of corporate governance which explains why corporate governance should also take into account the roles and the interests of constituencies other than shareholders and a board representing only them. I did not, of course, describe my initial puzzlement at the exact nature of my assignment in order to complain. On the contrary: I am very happy with the task as I have just now defined it because in my view one of the fundamental issues of corporate governance is precisely the question of why different constituencies play a role in the context of corporate governance and what "playing a role" means in this context. It can mean two things: that a given group of people do something (or play an *active* role), or that their interests are considered to be legitimate, i.e. that they "matter". These two things need not coincide. The interests of a person or a group may be central to a social system, and still the person (or persons) in question may not have any active role. And the most general question in this context is this: Whose decision problem is it to design a corporate governance system, and who or which entity assigns active roles and determines whose interests matter?

2. Some Basic Definitions

a) <u>The notion of corporate governance</u>: Referring specifically to profit-oriented, large firms in the legal form of corporations, I shall use the term "corporate governance" as follows: corporate governance is the totality of the institutional and organizational mechanisms, and the corresponding decision-making, intervention and control rights, which serve to resolve conflicts of interest between the various groups which hava a stakes in a firm and which, either in isolation or in their interaction, determine how important decisions are taken in a firm, and ultimately also determine which decisions are taken (Schmidt/Tyrell, 1997, p. 168, based on Williamson, 1985, p. 298-325). The most important relevant factors and mechanisms are the law, the structure of the financial sector of the country, market factors in input and output markets, and

the distribution of information, abilities and other resources or power bases. Underlying this definition is the notion of a (large) firm as a nexus of contracts (Jensen/Meckling, 1976). This notion is not precise, but it conveys two simple and important messages:

(1) There is, at least in principle, a contractual element in all relations between any group of resource providers and "the firm" (as the central contracting agent) or between all resource providers.

(2) Different parties to the network of contracts have differently defined rights to influence what decisions are taken. Although they may want to use these rights in their own interest or as they see fit, the outcome of their efforts to shape events will not only depend on what they want, but also on what others want to do and can do. There is thus no simple correspondence between the right to influence and the degree to which this leads to outcomes which reflect interests or wishes.

b) The notion of good - or workable - corporate governance: Whether corporate governance is good or workable depends on the "quality" of the decisions made in a firm. "Good" outcomes can be defined as those which

(1) further the interests of the present shareholders to the maximum extent possible, e.g. by leading to the highest share price ("shareholder value concept", narrowly defined), or

(2) further a somehow "weighted" average of the interests of different constituencies to the maximum extent possible, or

(3) ensure the survival, and perhaps also the growth, of a firm by enabling it to pay competitive prices for all the requisite inputs and to offer its products at competitive and cost-covering prices.

Evidently, these three definitions of "good" or "workable" outcomes are not necessarily antagonistic or mutually exclusive. However, they are also not necessarily one and the same thing merely expressed or looked at in three different ways.

3. Conventional Views of the Corporate Governance Problem

a) The narrow view. According to the narrow view, which Margaret Blair (1995, pp. 12f.) calls "the finance model", a large public corporation is the property of its shareholders, who are - by definition, it would seem - its owners. As there are many shareholders who lack the knowledge needed to run the firm and who could never reconcile their differing views and interests, a large firm is run by managers. In the ideal case, the firm is run by the managers in exactly the same way as the owners would run it if they knew how to do it. Of course, real managers have interests of their own and are also aware that it is difficult for the owners to monitor them. This gives rise to what I call the narrow view of the corporate governance problem: How can managers be made to act in such a way that, to the greatest extent possible, their actions are in the interest of the current shareholders of a corporation?

There are two well-known answers to this question. One is the Anglo-Saxon answer. It amounts to saying that there is a market for corporate control which does the trick: The permanent threat that some other management team could take over the company should motivate the incumbent managers to prevent a hostile take-over (Schmidt, 1989; von Thadden, 1990). They will best be able to defend their position if they make a take-over attempt as difficult, and notably as expensive, as possible. This can be done by seeing to it that the share price is as high as possible, which is exactly what the shareholders would want them to do.

The other answer, which would be more in the spirit of continental European economic systems, is that mechanisms like supervisory boards, duties of care and loyalty, reputation, financial incentives, peer pressure, etc., can be put in place and made to operate in such a way that in principle managers will act in the shareholders' interests (Roe, 1994).

As is well-known, in reality these two solutions to the problem - which come close to embodying what Franks and Mayer (1995) call the "outsider system" and the "insider system" - do not work perfectly, and the extent to which they work at all depends above all on the structure of a given country's financial sector.

It is interesting to note that those who advocate the narrow concept often do not bother much to ask why a large firm should be run exclusively in the interest of its shareholders in the first place. The - alleged - fact that the shareholders are "the owners" is often implicitly taken as sufficient justification, although this is of course circular reasoning (Blair, 1995, p. 202). However, general equilibrium theory does provide a sound rationale for the narrow concept: If all contracts with all providers of resources were perfect and complete, and if financial markets were also perfect and complete, profit (or shareholder value) maximising behaviour would lead to an efficient allocation of resources and an optimal position of all "stakeholders" (including shareholders) in a corporation (Hart, 1995), and it would be the best way of ensuring the survival of the firm. However, these very stringent conditions are not fulfilled in reality. If they were fulfilled, though, the problem of managers acting in a way which was not in the best interest of the shareholders could not arise in the first place, and thus there would be no need to bother about corporate governance because it would always be possible to write and enforce complete contracts between the shareholders and the managers (see Hart, 1995, and Schmidt/Terberger, 1996, p. 392).

b) The broader view: It is not self-evident that firms should - or can - always be run solely in the interest of their (present) shareholders. Instead of a one-sided shareholder orientation, one could advocate a pluralistic concept of "stakeholder orientation". Or one could argue that a large firm is more than just an association of its shareholders and that we should distinguish between the loyalty which the managers owe the corporation as a legal entity composed of all shareholders on the one side and, on the other, the loyalty which they owe the firm as an economic and social entity composed of all stakeholders including shareholders as well as important lenders, core employees, long-term clients and suppliers, the local community and even the respective nation or country. This is the common view of the advocates of a "stakeholder orientation", and it can also be found in relevant legal doctrines (Schmidt/Spindler, 1997, and Blair, 1995, p. 235). Evidently, in this context other constituencies would have a role to play at least in the sense of their interests being relevant from a normative point of view and also of them having at least a certain active role to play.

Seen in the context of the stakeholder approach, the corporate governance problem has two different aspects. One aspect is that the role or task of deciding "fairly" how much weight should be assigned to the different stakeholders' interests would fall to the managers and enhance the power which they in any case have. Moreover, they can hardly be expected to make this decision in a disinterested and equitable manner as they themselves are one of the interested parties - or "other" constituencies or stakeholder groups - and how they function as arbitrators between different groups may affect their own role as managers considerably. From the shareholders' perspective, they are likely to give too much weight to the interests of other stakeholders. The second aspect is that even though managers are considered as being accountable to several groups of stakeholders, there is still a need to limit their discretionary powers, which they could use to further their own interests. In fact, the vagueness of their obligations towards several groups of stakeholders is likely to expand the scope of their discretionary powers and thus to make the central problem of corporate governance, namely the agency problem of binding managers as agents to the interests of their principals, all the more difficult (Schmidt/Spindler 1997).

4. A Contractual View of the Corporate Governance Problem

For an economist, the narrow concept of corporate governance as a mechanism to ensure that a firm is managed solely in the interest of its shareholders is more appealing than the notion of corporate governance as a process of balancing the interests of different groups of stakeholders and managing a company in their common interest. The narrow concept is consistent and well-defined and its implications are straightforward. In contrast, the "stakeholder approach" makes every economist uneasy as too many questions are left open: What should be the yardstick for weighing or aggregating different interests? Why should the management, which after all also constitutes a group of "stakeholders", be trusted to strike a "fair" balance between the interests of the different groups? And what is the welfare-economic rationale for the entire approach?

But whatever misgivings a theoretically inclined economist may have regarding anything but a strictly shareholder-oriented corporate governance system, there is no denying that the stringent conditions under which the exclusive adherence to a policy of maximising profit or shareholder value is applicable, and also attractive from a normative standpoint, are not fulfilled in reality. In a world of imperfect and incomplete contracts and capital markets (or non-negligible transaction costs), the *a priori* arguments that can be advanced to explain why major decisions in large firms should only be taken in the interest of the shareholders (according to the objective function of maximising the market value of the equity) are rather weak, and share prices are at best an incomplete indicator of what the common interest of all shareholders is and the extent to which management serves this interest (Hart, 1993). In the following, I wish to suggest a general concept of what could be a guideline for the design of a corporate governance system. It takes at least some of these problems into account and implies a double role for "other constituencies" in corporate governance: the role of being people whose interests should count as well as an active role in the workings of a corporate governance system.

In a world in which information and incentive problems are not easily solved, many contracts are incomplete. Among other things, this gives rise to the hazards of opportunism, and this in turn makes it difficult for all parties to enter into long-term relationships which would be attractive for both sides if only there were not the danger of their being exploited (or "held-up" in the sense of Klein, Crawford and Alchian, 1978) once they have made relationship-specific investments. Other potential stakeholders, such as lenders, employees and suppliers, could rightly be concerned that a given firm - or its owners or its management acting solely in the owners' interest - will use any chance to profit from acting opportunistically if the future provides an opportunity for such behaviour (Shleifer/Summers, 1988). They would therefore try to avoid getting into a situation in the first place in which they would suffer from such behaviour. If the firm wishes to dispel these concerns in order to induce potential partners (stakeholders) to enter into long-term relationships, it must find ways to bind itself and to indicate that it will abstain from abusing any dependence, i.e. power, which might result from the relationship. Putting potential partners at ease will be difficult or impossible if it is

foreseeable that future decisions will only be made in accordance with the interests of those who will *then* be shareholders or, in other words, if it is clear that profit or shareholder-value maximisation will be the only concern at any given time.

So what can a firm do? Simply promising that it (or its owners or managers) will not act opportunistically would be "cheap talk": it would not create a binding commitment to adhere to what has been promised (Schelling, 1960). Nevertheless, before asking how a credible commitment could be created, it is worthwhile asking what would be promised or what would be the substance of a contract under the ideal condition that words would be credible. The answer is, generally speaking, that potential partners would be promised a contingent claim which they would value at least as highly as the best alternative open to them *before* they enter into the relationship. For various reasons, this claim would have to be contingent on what will happen in the future, and the persons who have at some point made a promise or concluded what amounts to an implicit contract may no longer be in command in the future, and this is why it would be so difficult to make a simple enforceable promise or to conclude explicit contracts with the other stakeholders.

One conceivable way of overcoming, or at least mitigating, the problem of creating a credible commitment is by instituting a system of corporate governance which gives those stakeholders who are not shareholders certain rights to protect their interests (Hart, 1993). Thus, the corporate governance system can also be interpreted as a contract - not a contract stipulating what payments and other benefits the stakeholders are entitled to obtain in the future under various circumstances, but a *constitutional* contract defining the rights to influence how unforeseen and perhaps unforeseeable future situations shall be dealt with (Laux, 1996). The notion of reserving "certain rights" for the other resource contributors or stakeholders is, of course, also vague. So what should these rights be? How extensive should they be? They include rights to be informed or to discuss or to veto certain decisions or to be involved in the selection and monitoring of the people who prepare and implement or ratify these decisions (Ganske, 1996). Based on the idea that these rights would be agreed upon in a (constitutional) contract which

determines the governance structure of the firm in such a way that co-operation is facilitated, it is evident that rights granted to the other stakeholders should be sufficient to protect them from the hazards of opportunism on the part of a firm or its owners or managers acting only in their interest. At the same time, these rights would be *only* those agreed upon in an ideal - costlessly written and costlessly enforceable - constitutional contract between all parties concerned or all groups of stakeholders in the firm. This latter requirement implies that the outcome of such a contract is not the same thing as what proponents of a simple "stakeholder orientation" would suggest. In most cases, those who bear the residual risk would bid the most for their interests to be given particular weight in the decisions of the firm. Traditionally it may have been self-evident that those who provide equity capital are the residual risk-bearers most interested in acquiring residual control rights. However, it has recently been recognised that in times of greater economic change, major lenders and employees with pension claims and/or career expectations have increasingly also become residual risk-bearers. That the ideal contract would be one concluded simultaneously between all parties is essential because what rights are granted to one party has implications - or external effects - for other contracting parties.

Such a constitutional contract would include the management as a party with a special status as its role is to make the concrete decisions involved in running the firm. Therefore, the contracts would have to grant to the management a certain degree of freedom to act unilaterally as the future unfolds, among other things in order to be able to act in good faith towards those stakeholders who are not shareholders. But as it is foreseeable that the management will always be exposed to the temptation to use this freedom of discretion to act in its own interest, the constitutional contract would also have to include a general rule which would limit management discretion and provide directions for the exercise of that discretion. Disregarding measurement problems for the moment, the general rule would be to maximise the (hypothetical) total value of the claims of all stakeholder groups on the firm's resources as seen at the (hypothetical) moment at which the contract was concluded. Thus, the contract would establish profit or shareholder value maximisation *under the restriction that the other constituencies must be given "fair" treatment* as the objective of the firm which the management would be expected to

pursue, as well as institutional devices which would further management's adherence to this objective as well as ensure the effectiveness of the constraint placed on management by the legitimate concerns of the other constituencies (Schmidt/Spindler, 1997).

5. Explaining and Assessing Corporate Governance Systems

It goes without saying that the idea of a "constitutional contract" or corporate governance contract determining the distribution of rights among the different groups of stakeholders, including the shareholders and the management as particularly important parties to the contract or as evidently important constituencies, should not be regarded as a practical device. It is not a blueprint for drawing up the charter and the bylaws of a corporation. In reality, such a contract would be too difficult to design in the first place, and it would also be impossible to write and enforce it. But even as a mere construct it may be useful in several ways. First of all, it provides a general answer to the fundamental questions of whether "other constituencies" have relevant rights in the context of corporate governance, and what these rights are. The answers are: Yes, they have certain rights, and the rights would be those on which all parties would agree in a contract concluded under ideal conditions.

It is impossible to be more specific here, as the substance of such a (hypothetical) contract would depend on the specific circumstances under which it were concluded. For instance, the extent to which employees would bargain to obtain rights of co-determination would depend on the general features of the labour market, on the educational system, on the general orientation of the management and on the rights which other constituencies such as lenders had (Aoki, 1994). The rights which banks would want to obtain (and "pay for" by accepting certain compensating obligations as part of the implicit contract) would depend on the bankruptcy law of the country, on the structure of the shareholding and the financing patterns of the non-financial firms involved and on many other factors including the orientation of management and the co-determination rights of the employees (Hackethal/Tyrell, 1997). Similar considerations apply to the management.

Even though general unconditional statements about which constituency or stakeholder group should have which rights would appear unjustified, other general statements of a more abstract nature can be made. They refer to what I call configurations of rights for different stakeholders, or "regimes". As the examples mentioned above indicate, there are two sets of factors which determine the attractiveness of certain rights for certain stakeholder groups. One set of factors comprises the rights of other stakeholders, and the other set consists of external factors like the laws of the country, the structure of its financial sector, the technologies of the firms or the nature of competition in the markets in which they operate, etc. Some regimes would not be attractive for all parties concerned. This would be the case if the rights of one group undermined the functionality of the rights of some other group or if they were incompatible with the external factors. Other regimes, in which the different rights of different stakeholders would complement each other and be consistent with the external factors, would constitute "workable" corporate governance systems.

Recent research into the nature of the interdependent systems formed by national modes of corporate governance and national financial sectors has begun to analyse the concept of "regimes" (or, more precisely, the consistency or "systemic" properties of such configurations) (Franks/Mayer, 1995; Hackethal/Tyrell, 1997). For instance, the recent literature on the Japanese, American and German systems of corporate governance and, almost as a mirror image, of the respective financial sectors, has shown that, at least until a few years ago, the regimes of these countries were "workable" and were probably conducive to the economic well-being of the countries (Knobling, 1996). By contrast, to date no one has been able - at least as far as I know - to discern any workable or consistent system in the interplay of corporate governance and financial system in France.

The single most important author in this field, whose pioneering effort to study the internal logic or consistency of different corporate governance systems has very much influenced the idea which I have just presented, is Jonathan Charkham, the chairman of this session. His insightful work makes it absolutely clear that understanding the "workability" of such regimes

is important (Charkham, 1994). It always has a double function: for one thing, it helps to explain certain features of these systems, including their stability and their effects on the real side of the respective economy; for another, it helps to assess them and to guide the small group of persons who, in their capacities as law-makers or major actors, are in a position to influence these regimes. For many other economic agents, it is of practical importance to be able to understand how the different elements of the corporate governance and financial systems interact and either support each other or work against each other. Knowing why and how a machine functions has always been a way of enhancing one's ability to benefit from it, as anyone will know who has ever tried to ride a motorcycle across the United States (Pirsig, 1974).

6. Concluding Remarks about the German System of Corporate Governance

For me as a German scholar it is an intriguing question whether specific features of the combination of German corporate governance and the German financial sector with institutionalised co-determination rights for employees, the very strong position of the big banks, the underdeveloped state of the stock markets, and the specific structure of corporate law (H. Schmidt *et al.*, 1997), make for a consistent or "workable" regime. I tend to agree with Mr Charkham (1994) that they do. However, I am not too sure whether this system is also stable enough to withstand the present strains to which it is exposed or whether it is good enough to meet the current challenges. I wish to conclude this paper with four observations regarding the systemic features of corporate governance *cum* financial sector in Germany.

First of all, I want to emphasise how important it is to understand the system well. Let me illustrate this by giving a brief account of how a newly-appointed chief executive of a very important German corporation has evidently had to learn this lesson the hard way. After the law which enables firms to limit payments to employees on sick leave was passed in parliament in the autumn of 1996, the new chairman of Daimler-Benz, Jürgen Schrempp, was one of the first to seize this opportunity and push for a decision by Daimler's management board to cut benefits to which the employees felt they were entitled as a long-standing, well-established right. In the

months before this decision was taken, Mr. Schrempp had established himself as one of the strongest advocates of a strict shareholder value orientation and earned considerable praise for this in the conservative press. It does not appear too far-fetched to call the decision by the board of Daimler-Benz an act of opportunism in the technical sense of the term coined by Williamson (1975 and 1985). It appears that Mr. Schrempp did not really understand the German system because after a few days the board had to rescind its decision, and this was probably not so much a consequence of the strikes that took place as it was an outgrowth of the belated recognition that the planned restructuring of the Daimler-Benz group could never be undertaken without the co-operation of the employees and their union. Mr. Schrempp went so far as to declare in public that he would never use the term "shareholder value" again, as *Der Spiegel* (No. 47/1996, p.122) reported gloatingly a few days later. This incident was a quite striking practical demonstration of something that, at a more abstract level, was already well-known, namely the extent to which the entire German socio-economic system is based on rules which put great emphasis on a "reaso nable" consensus. This general feature is also reflected in the corporate governance system and in the way labour representatives and banks tend to behave in their roles as active participants in the governance of non-financial corporations.

The second observation refers to the problems entailed in changing the system. If it is indeed true that giving important groups of "other constituencies" an *active* role in German corporate governance has been a wise step and has helped German industry to develop its particular competitive strengths, as Mr. Charkham (1994, esp. p. 43-49) argues convincingly in his book, then this casts doubt on the wisdom of certain recent developments which aim at changing elements of this coherent and functional system or "regime". As reasonable as they may appear at first glance, some individual reform measures may be detrimental to the consistency - or the workability - of the system (Schmidt/Tyrell, 1997, p. 178). I am not too sure what implications recent and current efforts to strengthen the role of the stock market, and especially to make hostile take-overs easier and to introduce stock-option plans tying management more closely to the immediate interests of shareholders will have for the workability of a system of corporate governance and general corporate policy which is so strongly based on discussion, consensus

and implicit contracts. Some of these measures might lead to an unworkable blend of an "insider system" and an "outsider system", to use the classification of Franks/Mayer (1995). The possible outcome might ultimately not be any consistent system at all.

The most striking empirical evidence to support the contention that it would be difficult to combine the features of the traditional German ”insider control” system in which the banks play a central role of the banks with capital market-based control mechanisms like take-overs, was provided on the final day of this conference: The top news story on that day was that Krupp-Hoesch was attempting a hostile take-over of Thyssen, an attempt which was abandoned only a few days later because it was not likely to succeed. The reasons for this failure can easily be traced to the importance and the nature of the other elements of the German system of corporate governance and financing.

The third concluding observation deals with the dynamics of change and looks briefly at the possible future of corporate governance in Germany. More important in this context than internal German changes are international developments such as the globalisation of financial markets and the process of European harmonisation and integration. These trends give rise to regulatory and competitive pressures. It would require more space than I have here to discuss at sufficient length why I believe that the likely outcome of the ongoing process of regulatory harmonisation and interpenetration of the vastly different systems of corporate governance and finance in the various European countries may not be anything like a smooth transition to a compromise or a middle-of-the-road position somewhere between the German and the English systems which would incorporate the strengths of both systems (but see Schmidt/Tyrell, 1997). If one wishes to assess likely future developments, one must understand that these systems are indeed systems, i.e. their different elements are designed, and function, in such a way that they tend to reinforce each other's effectiveness. Therefore, selective changes to individual elements of the systems can hardly be expected to change the general way in which the systems operate. This creates a certain rigidity, and rigidity may cause a system to "break", i.e. break down. For this reason, we should bear in mind that a process of transition could involve considerable

destabilisation. The German system, with its heavy emphasis on implicit contracts, is particularly vulnerable to this danger. This, in turn, is the reason why an abrupt end to what, in my view, still constitutes its strength and "workability" might be ahead. It remains to be seen whether the above-mentioned attempt by Krupp-Hoesch to take over Thyssen in a hostile manner in mid-March, and the damage which this seems to have done to the reputation of the two largest German banks, marks the beginning of a bumpy transition process.

Finally, we should remember precisely what it is that made the German post-war system work so well in more prosperous times - namely the emphasis on discussion and consensus, a certain degree of immobility and a certain lack of transparency, the sharing of active roles in corporate governance among several actors with some conflicting and some common interests, and, as a consequence of all this, a high degree of stability and/or inflexibility within the German regime of corporate governance *cum* financial system, and possibly also a corresponding instability and/or inflexibility on the part of the large German corporations which have had to operate under this regime. We must recognise that this simply may not be the most appropriate system for the new era of global and dynamic competition and change. However, these very same features of our system make it difficult even to conceive of alternatives that might be better, to envision where change could lead us, and to imagine how - and by whom - change might be initiated.

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