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Varieties of Financialization? Evidence from German Industry in the 1990s

Following some general remarks on the impact of financialization on nonfinancial sectors of the economy, this article identifies common misconceptions about the German and American varieties of capitalism. It then outlines the post-1960 U.S. experience with financialization, including the reasons for the rise of financialization and its main consequences. The article will then look at Germany, a country with a very different entry point into the world of financialization, and ask when and to what degree the concept was adopted. Finally, a detailed case study of Siemens—one of Germany's largest industrial concerns—will explore how this icon of Germany Inc. adapted to the demands of financialization and coped with the external changes caused by globalization, deregulation, and digitalization.

Financialization not only denotes the increasing role of financial institutions in the economy after 1970 but is also a megatrend affecting nonfinancial sectors. Regarding industrial corporations, the term indicates a reorientation from the logic of production to the logic of finance. Corporations are increasingly perceived more as portfolios of diverse investments and less as integrated technical and social units. The interests of shareholders are deemed paramount—indeed, more important than those of other stakeholders.¹ This shift began in the United States in the 1960s and gained speed in the 1980s, in the tailwind of the neoliberal reforms of the Reagan administration. Financialization was part of a sea change that recast the Western world from around 1970 onwards, as the high growth rates of the postwar boom faded away

¹ Per H. Hansen, "From Finance Capitalism to Financialization: A Cultural and Narrative Perspective on 150 Years of Financial History," *Enterprise & Society* 15, no. 4 (2014): 605–42. See also Greta R. Krippner, *Capitalizing on Crisis: The Political Origins of the Rise of Finance* (Cambridge, Mass., 2011); Greta R. Krippner, "The Financialization of the American Economy," *Socio-Economic Review* 3, no. 2 (2005): 173–208; and Natascha A. J. van der Zwan, "Making Sense of Financialization," *Socio-Economic Review* 12, no. 1 (2014): 99–129.

and with it trust in Keynesian demand management as well as in welfare and managerial capitalism.

This article first addresses misconceptions in the variety-of-capitalism (VoC) literature. It moves on to outline the post-1960 American experience with financialization, the reasons for its emergence and pervasiveness, and its main economic effects. It will then look at Germany, a country that entered the world of financialization from a very different vantage point. When and to what degree was the concept adopted in Germany, and to what extent did it conflict with “coordinated capitalism”?² Did Germany prove resilient or did it undergo systemic changes? The final part of this article looks at Siemens, one of Germany’s largest industrial concerns.

Transatlantic Pitfalls: Comparing German and American Capitalism

The VoC literature argues that a very distinct line divides “liberal market” economies and “coordinated market” economies. The former—namely, Anglo-Saxon countries—lean toward corporations with limited liability, a divorce of ownership from control, a reliance on stock exchanges, and a mistrust of regulation. By contrast, coordinated economies, such as Germany, depend more on banks than on capital markets. They trust state enterprises and intervention, favor quality over mass production, and prefer apprenticeship systems to on-the-job training. They solve conflicts consensually through institutional mechanisms such as codetermination, cartels, and centralized collective bargaining.

This juxtaposition is not necessarily downright erroneous, yet it creates severe problems through its oversimplification and schematism. The characterization of these two economic models does not reflect historical complexity and often comes up against clichés; moreover, it offers a deterministic narrative. Once these economic systems are in place—that is, by the end of the nineteenth century—they lock everybody into long-lasting trajectories. The script of history has been written, with very little room left for historical contingencies, crossroads, and trend reversals.

Neither American nor German capitalism is immutable or on a predestined trajectory. Recent empirical research has contradicted the VoC models in a number of ways. For example, the concept of shareholder value is by no means a perennial feature of U.S. capitalism. It had prospered prior to 1914, when it was replaced by a managerial concept

² Peter A. Hall and David Soskice, eds., *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage* (Oxford, 2001); Wolfgang Streeck, “E Pluribus Unum? Varieties and Commonalities of Capitalism,” in *The Sociology of Economic Life*, ed. Mark Granovetter and Richard Swedberg (Boulder, Colo., 2011), 419–55; and “‘Varieties of Capitalism’ Roundtable,” *Business History Review* 84, no. 4 (2010): 637–74.

claiming that corporations were to serve a variety of stakeholders.³ Until around 1970, when the new mantra began to transform their behavior, U.S. directors were not very responsive to the interests of shareholders.⁴

The bonus culture found in Europe from the 1980s onwards was molded from Anglo-American models and did not have as long a tradition as the VoC proponents claim. In fact, the compensation paid to American executives was rather modest until the 1960s; the culture of large bonuses then had to be invented. In the first half of the twentieth century, corporate directors in Germany received higher bonuses, or *Tantiemen*, than did their counterparts in the United States or the United Kingdom, who at that time were rewarded mostly with fixed fees or their own shares.⁵

Recent research on initial public offerings (IPOs) on the Berlin Stock Exchange demonstrates that shareholders of German corporations were not generally disadvantaged between 1870 and 1933. On the contrary, their interests were relatively well protected by a series of legal reforms, which explains the vibrancy of the German IPO market—until the exchange was shut down for a year following the banking crisis of 1931. The Nazis' hostility toward publicly traded corporations had a much greater impact than the Depression of 1929 to 1933 and caused the market to virtually collapse in the 1930s.⁶

The distribution of features between the liberal-market and coordinated economies seems to be upside down when it comes to the relevance of the stock exchange. In 1913 the number of publicly traded companies per million inhabitants was three times as high in Germany as in the United States. The interwar years saw a considerable convergence, but even in 1938 Germany still led the United States by a thin margin. Then, after 1945, the positions of the two countries were reversed. In 1980 the United States had three times as many publicly traded corporations per one million inhabitants as Germany, and in 1990, four times as many.⁷ The traditional picture portraying the United States as a country with a strong shareholder-value orientation

³ Mary O'Sullivan, "What Opportunity Is Knocking? Regulating Corporate Governance in the United States," in *Governments and Markets: Toward a New Theory of Regulation*, ed. Edward J. Balleisen and David A. Moss (Cambridge, U.K., 2010), 335–62.

⁴ William Lazonick and Mary O'Sullivan, "Maximizing Shareholder Value: A New Ideology for Corporate Governance," *Economy and Society* 29, no. 1 (2000): 13–35.

⁵ Leslie Hannah, "The Origins, Characteristics, and Resilience of the 'Anglo-American' Corporate Model," *Essays in Economic and Business History* 33 (2015): 1–25.

⁶ Carsten Burhop, David Chambers, and Brian R. Cheffins, "Law, Politics, and the Rise and Fall of German Stock Market Development, 1870–1938" (ECGI Law Working Paper No. 283/2015, European Corporate Governance Institute, 2015), 1–44.

⁷ Raghuram G. Rajan and Luigi Zingales, "The Great Reversals: The Politics of Financial Development in the Twentieth Century," *Journal of Financial Economics* 69, no. 1 (2003): 5–50, esp. 17.

due to the common-law legacy of shareholder protection, and Germany as a country with a civil-law tradition of weak shareholder protection and a bank-based financial system, has to be revised—at least for the period prior to 1930. It took the Great Depression and, more so, intervention by the Nazi government to squelch the relatively strong equity culture that had developed in Germany since the early Empire. The moderate size of postwar Germany's stock exchange is not the result of a model set in stone but rather of specific historical developments during the 1930s. This article argues that financialization is another distinct epoch, beginning around 1970. The article does not look at the longer-term historical development of capitalism in the two countries, nor does it buy into the full set of premises of the VoC school. Terms such as “the American model” refer specifically to post-1970s financialization.

Financialization in the United States

During the 1970s, reliance on regulated and oligopolistic markets, as well as on strong (welfare) states and large conglomerates, was increasingly replaced by the neoliberal grand narrative that paved the way for deregulation, privatization, tax cuts, and waves of mergers and acquisitions.⁸ More and more, the economy came to be regarded as driven by financial processes. The “shareholder value conception,” according to which “the only legitimate purpose of firms is to maximize shareholder value,” gained prominence.⁹ In 1986, Alfred Rappaport published his best seller *Creating Shareholder Value*, which fit the neoliberal climate of the times to a tee. Managers, he argued, should first and foremost pursue the interests of shareholders by increasing the return on equity.¹⁰ The main criterion for success became the price of shares on the stock market.

⁸ Neil Fligstein, *The Transformation of Corporate Control* (Cambridge, Mass., 1990); Marina von Neumann Whitman, *New World, New Rules: The Changing Role of the American Corporation* (Boston, 1999); William Lazonick, “The Financialization of the U.S. Corporation: What Has Been Lost, and How It Can Be Regained,” *Seattle University Law Review* 36 (2013): 857–909.

⁹ Neil Fligstein, *The Architecture of Markets: An Economic Sociology of Twenty-First-Century Capitalist Societies* (Princeton, 2001), 148.

¹⁰ O'Sullivan, “What Opportunity Is Knocking?,” 349–52; Alfred Rappaport, *Creating Shareholder Value: The New Standard for Business Performance* (New York, 1986). On the United States, see Lazonick and O'Sullivan, “Maximizing Shareholder Value.” On Germany, see Werner Abelshauser, *The Dynamics of German Industry: Germany's Path toward the New Economy and the American Challenge* (New York, 2005); Klaus Dörre, “Das Deutsche Produktionsmodell unter dem Druck des Shareholder Value,” *Kölner Zeitschrift für Soziologie und Sozialpsychologie* 53, no. 4 (2001): 675–704; Ralf Ahrens, Boris Gehlen, and Alfred Reckendrees, eds., *Die “Deutschland AG”: Historische Annäherungen an den Bundesdeutschen Kapitalismus* (Essen, Ger., 2013). For a comparison, see Mary

What were the underlying causes of this paradigm shift? The postwar boom came to an end around 1970 and was supplanted by slow growth, high inflation, and declining profits. At the same time, new competitors—especially Japan—challenged Western corporations. Secure, oligopolistic markets with high prices became a thing of the past. In this climate the performance and accountability of top management looked deficient, and new incentive structures seemed necessary to overcome negligence in the boardroom. In the United States, the emergence of the Rust Belt and such spectacular bankruptcies as that of the Penn Central railway company in 1970 due to grave mismanagement underscored the need for new approaches to corporate governance.¹¹

At the same time, shareholder activism that followed a change in the structure of stock ownership became a new force to be reckoned with. More money was channeled from savings accounts into funds (Figure 1). Individual retail investors had dominated markets in the 1950s and 1960s. By the 1980s, pension, mutual, union, and, from the late 1990s, hedge funds played an increasingly powerful role. Mutual and pension funds, as well as charitable foundations and university endowments, held \$112 billion in U.S. corporate equity in 1980. This figure had almost quadrupled by 1990 (\$393 billion) and increased by a factor of 22 by 1997, when it reached \$2.4 trillion. Taken together, all institutional investors—a category that includes banks, insurance and investment companies, and brokerage and security firms—accounted for \$504 billion in 1980, \$1.5 trillion in 1990, and \$6.4 trillion in 1997. This was the tectonic power shift that recast corporate governance in the United States.

Institutional investors behaved differently from individual equity holders. They sought higher returns and had the sophistication to pressure managers. They regularly attended shareholder meetings to exercise their clout.¹² In 1966/1967, the California Public Employees' Retirement System (PERS, from 1992 CalPERS) was allowed to invest up to 25 percent of its portfolio in stocks. In 1984 this limit was

O'Sullivan, *Contests for Corporate Control: Corporate Governance and Economic Performance in the United States and Germany* (Oxford, 2000).

¹¹ Joseph R. Daughen and Peter Binzen, *The Wreck of the Penn Central*, 2nd ed. (Boston, 1999); Stephen Salisbury, *No Way to Run a Railroad* (New York, 1982). See also Brian R. Cheffins, "Corporate Governance since the Managerial Capitalism Era," *Business History Review* 89, no. 4 (2015): 717–44.

¹² Brian R. Cheffins and Ian D. Armour, "The Past, Present, and Future of Shareholder Activism by Hedge Funds," *Journal of Corporation Law* 37, no. 1 (2011): 52–103; Stuart Gillan and Laura Starks, "The Evolution of Shareholder Activism in the United States," *Journal of Applied Corporate Finance* 19, no. 1 (2007): 55–73; Michael Useem, *Executive Defense: Shareholder Power and Corporate Reorganization* (Cambridge, Mass., 1993), 28–56. On hedge funds, see Marcel Kahan and Edward B. Rock, "Hedge Funds in Corporate Governance and Corporate Control," *University of Pennsylvania Law Review* 155, no. 5 (2007): 1021–93.

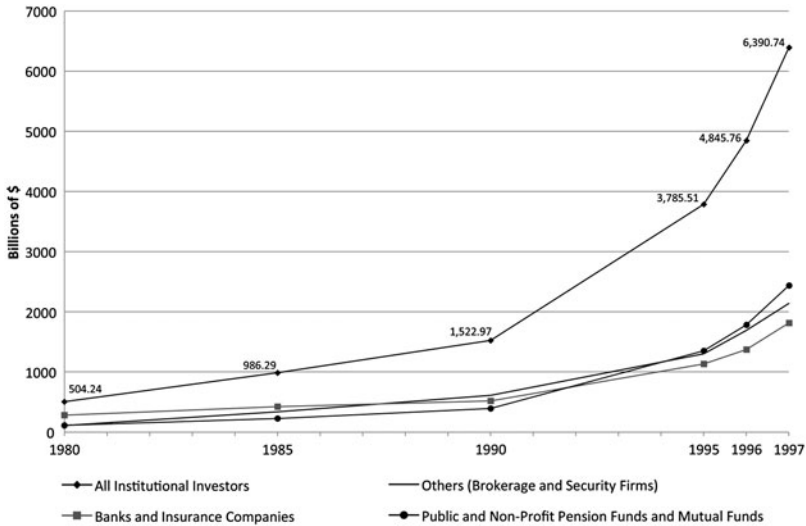


Figure 1. Institutional equity holdings in the United States, 1980–1997. (Source: Franklin R. Edwards and R. Glenn Hubbard, “The Growth of Institutional Stock Ownership: A Promise Unfulfilled,” *Journal of Applied Corporate Finance* 13, no. 3 [2000]: 94.)

dropped. By 1996, CalPERS represented more than one million people and managed a portfolio worth \$100 billion. In the 1980s, PERS pushed for the creation of the Council of Institutional Investors (CII), which became a vocal advocate for shareholder rights.¹³ In order to control management, the number of outside directors increased, effectively ending the coziness of self-control. To measure performance, analysts and corporations themselves employed short-term financial indicators, which were also used to determine managerial compensation, in order—so went the justification—to align the interests of shareholders and managers. There were also legal reasons. In 1993, Congress ruled that corporations could no longer deduct executive compensation over \$1 million a year as business expenses unless these payments were performance related.¹⁴ The result was a steep increase in compensation to executives in the 1980s and 1990s through bonuses, mostly in the form of stock options.¹⁵ These arrangements can create perverse

¹³ Gillan and Starks, “Evolution of Shareholder Activism,” 56–57.

¹⁴ Lynn A. Stout, “The Mythical Benefits of Shareholder Control,” *Regulation* 30, no. 1 (2007): 42–47.

¹⁵ See John Balkcom and Roger Brossy, “Executive Pay—Then, Now, and Ahead,” in *The History of Modern Corporate Governance*, ed. Brian R. Cheffins (Cheltenham, U.K., 1997), 410–23.

incentives and induce managers to suppress bad news, to prefer short-term over long-term results, to take on too much risk, and to engage in nontransparent or even fraudulent accounting practices. After all, their bonuses went up as long as the numbers met certain targets.¹⁶

The cumulative effect of these changes was a highly incentivized and financialized economy. Short-term financial results and stock-market quotations overshadowed long-term strategies. Corporations were seen as a bundle of assets that could be “deployed and redeployed depending on the short-run rates of return.”¹⁷ A booming and highly lucrative market for corporate control emerged. The offshoring or divestiture of underperforming divisions became the norm. The shareholder-value concept and the weakening of antitrust laws in 1981 by the Reagan administration set the stage for the corporate raiders of the 1980s.¹⁸ The “deal decade” saw a spate of mergers and takeovers, many of them hostile and highly leveraged. Aggressive investment firms such as Kohlberg Kravis Roberts & Co. (KKR) pursued large-scale leveraged buyouts, usually of inefficient conglomerates, thus profoundly restructuring the American economy and challenging traditional managerial capitalism with an investor-controlled alternative. These trends accelerated considerably in the 1990s, putting enormous stress on managers to secure high stock prices in order to prevent such takeovers and to keep their jobs.¹⁹

Financialization energized and destabilized the economy. While the list of Fortune 500 firms remained largely stable until around 1980, the 1980s and the late 1990s saw annual turnover rates rise to unprecedented levels.²⁰ The average tenure of chief executive officers (CEOs) declined while their income, increasingly through variable incentives, exploded.²¹ The ratio of the average earnings of the CEOs of two hundred large U.S. corporations to the pay of average U.S. workers was 42:1 in 1980, 107:1 in 1990, and 525:1 in 2000.²² At the same time, union membership among private-sector workers dropped from 16.8 (in 1983) to 9 percent

¹⁶ See Lucian A. Bebchuk and Jesse M. Fried, “Pay without Performance: Overview of the Issues,” *Journal of Corporation Law* 30, no. 4 (2005): 647–73.

¹⁷ Fligstein, *Architecture of Markets*, 150.

¹⁸ Cheffins and Armour, “Past, Present, and Future,” 75–79; Useem, *Executive Defense*, 22–27.

¹⁹ “Leveraged” means that the buyers relied on loans rather than on cash or on issuing new stocks. Allen Kaufman and Ernest J. Englander, “Kohlberg Kravis Roberts & Co. and the Restructuring of American Capitalism,” *Business History Review* 67, no. 1 (1993): 52–97; Bengt Holmstrom and Steven N. Kaplan, “Corporate Governance and Merger Activity in the United States: Making Sense of the 1980s and 1990s,” *Journal of Economic Perspectives* 15, no. 2 (2001): 121–44.

²⁰ Dane Stangler and Sam Arbesman, “What Does Fortune 500 Turnover Mean?” (unpublished paper, 2012), <http://ssrn.com/abstract=2078162>.

²¹ See Useem, *Executive Defense*, 101–24.

²² Calculated by the American Federation of Labor–Congress of Industrial Organizations (AFL-CIO) and quoted in William Lazonick, “Innovative Business Models and Varieties of

(in 2000).²³ In the 1950s it had been around 35 percent. Employment became increasingly flexible and insecure. Lifetime employment in a single firm with defined-benefit pensions and full medical insurance was phased out while interfirm mobility rose and employees were made to shoulder a larger share of elementary risks.

Critical voices condemn financialization as a self-destructive process in the long run as it exacerbates inequality and instability and thus erodes the social foundation of American capitalism. When executives favor massive stock buybacks over investments and job creation in order to boost stock prices from which they themselves are the first to benefit, growth potential may be wasted and the social consensus endangered.²⁴ Alfred Chandler, the doyen of U.S. business history, issued the following caution in 1991: “If you really believe—this is where I get upset—that the function of the firm is to give dividends to shareholders, we’re going to end up worse than Britain.”²⁵

The partial deindustrialization of the United States seemed to give credence to this view. Critics also maintain that financialization increases the likelihood of manipulative and fraudulent practices. Such outcomes were powerfully in evidence in the massive accounting scandals at Worldcom, Tyco, and Enron and in the financial crisis that erupted in 2007 and 2008.²⁶ Incentive-oriented compensation makes it a prerogative that CEOs meet earnings targets, one way or another. This picture might be one-sided, as the dynamism of the U.S. economy in the 1980s and 1990s, especially in the so-called new economy, cannot be explained without flexible labor and capital markets.

Germany: A Reluctant Latecomer

While the 1980s was a period of turmoil in the United States, Germany’s corporate world enjoyed relative continuity. The self-asserting forces of coordinated capitalism prevented radical change. Codetermination gave employees and unions a strong bargaining position. Through their associations, employers exerted considerable influence. When the conservative Christian Union took over government control from the

Capitalism: Financialization of the U.S. Corporation,” *Business History Review* 84, no. 4 (2010): 675–702.

²³ Bureau of Labor Statistics databases, accessed 6 Apr. 2015, <http://www.bls.gov/webapps/legacy/cpslutab1.htm>; Gerald Mayer, *Union Membership Trends in the United States* (Washington, D.C., 2004), 11.

²⁴ Lazonick, “Business Models,” 700–702; William Lazonick, “Profits without Prosperity,” *Harvard Business Review*, Sept. 2014, 2–11.

²⁵ Quoted in Hannah, “Origins, Characteristics, and Resilience,” 8.

²⁶ On the regulatory consequences, see O’Sullivan, “What Opportunity Is Knocking?,” 337–42.

Social Democrats in 1983 no abrupt change of economic policy occurred. Although Chancellor Helmut Kohl favored deregulation, privatization, and monetarism, he opted for cautious, piecemeal reforms and avoided the kind of sweeping change associated with Thatcherism and Reaganomics. In principle, he stuck to the “social market economy,” which was built on consensus and compromise. Thus, Germany—despite structural crises in many old industries—defended and strengthened its industrial base in traditional sectors while only very few new high-tech enterprises emerged.

The 1990s, however, was a decade of profound change. The Eastern Bloc collapsed, with globalization and deregulation going into full swing. In 1993, the European single market was completed. A phase of neoliberal euphoria began; after all, capitalism had obviously proved itself to be superior and without alternatives. In the 1990s, some characteristics of the old Germany Inc. vanished or were weakened.

The decade began in 1991 with the first hostile takeover of a large German corporation, namely, that of Hoesch by Krupp. Another takeover—that of Thyssen by Krupp, planned for 1997—failed due to political opposition, but the two ailing steel producers nonetheless merged in 1999. The decade ended with the hostile takeover in 2000 of Mannesmann by the British mobile telephone company Vodafone for €180 billion, the largest acquisition the world had ever seen at that time. The takeover had been preceded by the splitting up of Mannesmann’s industrial divisions, which had 102,000 employees and were later sold.²⁷ In 1995 the Post Office (Bundespost) with its roughly half-million employees was privatized. German Railway (Bundesbahn) became a joint-stock company in 1994 but remained in public ownership. The markets for energy, which had since the Nazi period been organized as regional monopolies, were liberalized in the second half of the 1990s. In 1998, two traditional automakers from Germany and the United States merged; Jürgen Schrempp, the CEO of Daimler-Benz AG, spoke of a “wedding made in heaven” and a “merger of equals.”²⁸ Actually, DaimlerChrysler was controlled from Stuttgart. Schrempp, a staunch advocate of the shareholder-value concept, wanted to create a “world corporation.” Thus, in 2000 DaimlerChrysler purchased 37.5 percent of Mitsubishi as well as 10 percent of Hyundai. The company sank billions into this failed vision. In 2005, Schrempp left the company, as did Mitsubishi, and in 2007 DaimlerChrysler was reintegrated back into the original companies.

The forces of change existed in globalization, in the crises of many old industries, and in the general tendency toward liberalization

²⁷ Mannesmann AG, *Annual Report* for 1999 (Düsseldorf, 2000).

²⁸ Peter Schneider, “Scenes from a Marriage,” *New York Times*, 12 Aug. 2001.

strengthened by the European Union. In addition, capital markets were increasingly deregulated and the shareholder-value concept widely accepted, at least by managers, bankers, and analysts. This reorientation was virtually forced upon them from the outside because of the growing danger of hostile takeovers by institutional investors from abroad. Indeed, such takeovers had increased noticeably due to the growth in the importance of investment banks operating internationally, as well as of private equity and of venture and hedge funds.

Offshoring, Outsourcing, and Divesting

After the fall of the wall, German corporations found low-cost locations at their doorstep, that is, in Eastern Europe. They seized this opportunity, especially as they wanted to establish a presence in what looked like future growth markets. Many firms, particularly small and medium-sized ones, opened factories outside Germany for the first time. Once they had taken this step, the notion of investing elsewhere—especially in Asia—appeared less daunting. However, most direct investment in this period went into the European Union. Outflows rose throughout the 1990s, accelerating considerably from 1996. Outsourcing and offshoring of lower-value-added activities became standard and highly controversial practices. Union functionaries demanded—without success—that companies that had relocated production to foreign locations be excluded from public contracts. Protests abounded, above all when German factory closures were announced.

Provided that simply giving up markets was not an option, there existed no realistic alternative to following the paths of international competitors, despite all the criticism and uneasiness. Thus, dividing the value chain across national borders on the basis of financial criteria became the norm. Firms underwent a process of almost constant restructuring. Never before had German corporations been so changeable. They now could be broken down into their components on short notice, recombined, and traded.

Siemens spent 8 billion DM for 434 equity investments between 1990/1991 and 1994/1995. Strategic alliances around the world were to strengthen existing divisions. Divestments, however, remained conspicuously rare until 1998. Between 1992 and 1997, Siemens reduced the number of its jobs in Germany from 253,200 to 197,000. Its foreign investments surpassed domestic ones in every single year.²⁹ The new plasticity of large companies to the point of complete divisibility is most readily discernible in the extreme case of Hoechst AG. A radical restructuring began in 1994. Numerous divisions were sold or spun off into joint

²⁹ Siemens AG, *Annual Reports, 1990/91–2000/01* (Munich, 1991–2001).

ventures. In 1995, Hoechst took over the U.S. pharmaceutical company Marion Merrell Dow, at a cost of 7.1 billion DM, and brought together all the pharmaceutical divisions of the company in the new group Hoechst Marion Roussel. Thereafter, the corporation concentrated on the pharmaceutical and agricultural business, and in 1997 sold the special chemistry branches and bought the French pharmaceutical manufacturer Roussel Uclaf. In 1999, Hoechst Marion Roussel and Rhône-Poulenc merged to form Aventis. All other operational branches of Hoechst AG were transformed into independent businesses or sold. Hoechst, a traditional company of Germany Inc., founded in 1863, had disintegrated within a few years into a perplexing number of distinct parts.³⁰

Playing Second Fiddle: Germany's Financial Sector

In the 1980s, large German banks began to abandon their role as credit providers and guardians (*Hausbanken*) for industrial firms by gradually selling their shares in these firms and withdrawing from their boards. The banks aspired to engage in the much more profitable investment banking, as practiced by Anglo-American banks.³¹ However, they did so with very limited success, mainly losing out to foreign rivals and financial markets. With the exception of Deutsche Bank, no German bank made it into the top tier of international investment banks. The reasons are manifold. In a long historical perspective, the weak tradition of international finance and the loss of expertise through the persecution of Jewish bankers have to be mentioned. In addition, the competition of publicly owned savings banks and *Landesbanken* as well as cooperative banks impaired the large players. When they decided around 1980 to turn to investment banking, they were coming late to the game. Deutsche Bank invested heavily by taking over Morgan Grenfell in 1990, merging that bank with Deutsche Bank's own investment banking sector, and relocating the new unit to London in 1995. The German bank also recruited entire teams of traders, including the group around the legendary Merrill Lynch banker Edson Mitchell in 1995. In 1999 Deutsche Bank acquired Bankers Trust in New York for the exorbitant price of almost \$10 billion.³² And still, for all the money it spent, Deutsche Bank never made it to the very top. In 2015, Deutsche Bank ranked twelfth of banks in Europe and fortieth

³⁰ Christoph Wehnelt, *Hoechst: Untergang des Deutschen Weltkonzerns*, 3rd ed. (Lindenberg, Ger., 2009).

³¹ Jürgen Beyer, *Pfadabhängigkeit: Über Institutionelle Kontinuität, Anfällige Stabilität und Fundamentalen Wandel* (Frankfurt, 2006), 94–116.

³² Bankers Trust had just been convicted of fraudulent accounting practices. Christopher Kobrak, *Banking on Global Markets: Deutsche Bank and the United States, 1870 to the Present* (Cambridge, U.K., 2007), 334–46.

worldwide. No other German bank figured at all in the top 100.³³ Banking has never been a leading sector in Germany, and its reputation has been (and is) far from great. Surveys among graduate students in business courses at German universities regularly show that banks are not considered attractive employers. Instead, the top preferences of students are car manufacturers, followed by Lufthansa, Google, Adidas, and Bosch. Germany still defines itself as a country of engineering and car manufacturing; the service industries count little.³⁴

The increasing turn toward the capital market and Anglo-American practices can also be discerned in the listings of German companies on the New York Stock Exchange. Daimler was first, in 1993, and fifteen other major companies had followed by 2002. Yet most of the anticipated advantages failed to materialize. Since the U.S. Securities and Exchange Commission made it easier in 2007 for foreign companies to delist, many German companies have retreated from New York.³⁵

German banks also lost out to new players in their home market. In the 1990s, American investment firms and funds increasingly pushed into Germany. German competitors were still marginal around 1990, although the first investment firm for private equity and venture capital had been founded in 1965. The portfolio of all German funds in Germany reached about €1 billion in 1988 and grew rather slowly until 1996, when the new-economy craze pushed it up—to €22 billion in 2001. Still, by American or British standards, these figures were meager. In 2003 the share of private-equity investments in the gross domestic product was less than half the E.U. average and only one-seventh of the figure for the United Kingdom, the European leader.³⁶ Germany's relative backwardness is underscored by the fact that it did not establish a specialized stock exchange for high-tech companies (Neue Markt) until 1997. In comparison, the NASDAQ was founded in 1971.³⁷

Investment firms also met with distrust and ideological prejudices. When KKR and Goldman Sachs bought Siemens-Nixdorf, a producer of automatic cash dispensers, in 1999 and organized a successful flotation on the stock market in 2004, the chairman of the Social Democratic Party, Franz Müntefering, excoriated American investment firms as

³³ Sebastien Jost and Anne Kunz, "Warum die Deutschen ihre Banken so sehr verachten," *Die Welt*, 6 May 2015.

³⁴ Ibid.

³⁵ Simon Hage, "Deutsche Konzerne. Flucht von der Wall Street," *manager magazin*, 6 Sept. 2007.

³⁶ Jürgen Schaaf, "Private Equity in Europa: Buy-outs stützen Wachstum, Gründungsfinanzierung abgestürzt," *Economics: Digitale Ökonomie und struktureller Wandel*, 26 Jan. 2005, 6.

³⁷ Holger Frommann and Attila Dahmann, *Zur Rolle von Private Equity und Venture Capital in der Wirtschaft* (Berlin, 2005), 13–16, 24.

“locusts.” Specifically, he said, “We must help those entrepreneurs who take their firms’ ability to survive in the future and the interests of their employees into consideration against the irresponsible swarm of locusts who measure success in a quarterly rhythm, suck out substance, and let companies collapse when they have devoured them.”³⁸ Many people in Germany shared this sentiment, although most buyouts of this type were successful and saved or created jobs.

Werner Seifert, the former CEO of Deutsche Börse (German Stock Exchange), used the same metaphor in his 2006 memoir, titled *Invasion of the Locusts*. Seifert described his unsuccessful attempt to take over the London Stock Exchange in 2000 and again in 2004 and his subsequent ouster in 2005, which was forced by several shareholders of Deutsche Börse under the leadership of the British hedge fund TCI. Several prominent members of the supervisory board later resigned. For the first time, well-organized minority shareholders had directly influenced the strategy and the selection of top management of a major company. Seifert’s reading of these events is made clear in the subtitle of his book: “How Hedge Funds Attack Germany Inc.” This sentiment was shared by many commentators in Germany.³⁹

Stalled Domestic Equity Culture and the Internationalization of Shareownership

The dot-com crash of 2000 and 2001—particularly the disaster of Telekom and Infineon shares, which had been massively promoted as shares for everyone—was a tremendous blow to Germany’s emerging equity culture. Ordinary savers who had just begun to overcome their traditional reluctance to invest in shares turned their backs on them again. While in 1992 only 6.4 percent of all Germans above the age of fourteen owned shares, this percentage had climbed to 9.7 (in 2000) before it shrank again, to 5.5 percent in 2008. If we include indirect ownership through funds, the participation rate for 2000 and 2008 was 18.5 and 14.4 percent, respectively.⁴⁰ Corresponding figures for the United States were 62 and 56 percent.⁴¹

³⁸ Franz Müntefering, “Freiheit und Verantwortung. Das neue Grundsatzprogramm der SPD” (speech delivered on 22 Nov. 2004) in *Programmheft I: Tradition und Fortschritt*, ed. Sozialdemokratische Partei Deutschlands (SPD) (Berlin, 2005), 18.

³⁹ Werner G. Seifert and Hans-Joachim Voth, *Invasion der Heuschrecken: Intrigen-Machtkämpfe-Marktmanipulation. Wie Hedge Fonds die Deutschland AG attackieren* (Berlin, 2007).

⁴⁰ Deutsches Aktieninstitut, *Aktionärszahlen des Deutschen Aktieninstituts 2014, Tabellen* (Frankfurt, 2015), 4.

⁴¹ Lydia Saad, “U.S. Stock Ownership Stays at Record Low,” *Gallup*, 8 May 2013, <http://www.gallup.com/poll/162353/stock-ownership-stays-record-low.aspx>.

A number of legislative reforms had previously strengthened the position of shareholders or were about to do so. In general, these laws also represented a late opening up on the part of Germany to the logic of financialization and international standards of investor protection. The Control and Transparency Act of 1998 (KonTraG) extended the liability of supervisory and management boards. It introduced mandatory early warning and risk management systems and abolished plural voting rights, which up to that point had favored large shareholders at the expense of ordinary investors. The new universal rule of “one share, one vote” strengthened the principle of shareholder democracy. Supervisory boards were required to meet four times a year instead of two and to hire external auditors. The KonTraG also authorized share buybacks and stock option plans.

In 2002, the Securities Acquisition and Takeover Act limited anti-takeover defenses and required transparency of information and the equal treatment of all shareholders.⁴² In the same year, a corporate governance code was implemented via the Law on Transparency and Publicity. This was the result of work by a government-appointed commission that—following the rules of coordinated capitalism—consisted of managers, union representatives, and social scientists. The commission’s code of conduct stepped up the requirements for transparency and strengthened supervisory boards. However, a radical break with the old boardroom culture was prevented by business interests. In 2004 the Investment Modernization Act permitted hedge funds to operate in Germany and granted them and other funds massive tax concessions. Several laws passed in 2005 made it easier for shareholders to take managers to court for incomplete or misleading information; in addition, the compensation of individual board members had to be disclosed.⁴³ And yet, most individual investors—after a short honeymoon—left the market in droves.

The most profound change occurred in 2000, when the capital gains tax was abolished for firms divesting themselves of shares they held in other firms. The rationale behind this move was that networks of cross-shareholdings within Germany Inc.—which had until then constrained the market for corporate control—would be dissolved. A marked increase in foreign and institutional shareholding was the consequence. As late as 1997 the proportion of foreign investors in DAX 30

⁴² John W. Cioffi and Martin Höpner, “The Political Paradox of Finance Capitalism: Interests, Preferences, and Center-Left Party Politics in Corporate Governance Reform,” *Politics & Society* 34, no. 4 (2006): 463–502, esp. 477–80.

⁴³ David Furch, *Marktwirtschaften unter dem Druck globalisierter Finanzmärkte: Finanzsysteme und Corporate-Governance-Strukturen in Deutschland und Italien* (Wiesbaden, 2012), 153–69.

companies was as low as about 10 percent but already rising. Between 2001 and 2008, following the new tax law, the figure jumped from 35.5 percent to 52.6 percent. These investments originated mainly in the United States, the United Kingdom, and the rest of Europe. The average proportion of shares in DAX 30 companies held by foreigners reached 56 percent in 2014, while institutional investors, most of them foreign funds, held a staggering 65 percent. There were six DAX 30 companies with more than 70 percent of their shares in foreign hands.⁴⁴

New Kids on the Block: The Changing Management Elite

Despite many misgivings and delays, the principles of financialization began seeping into Germany. Harbingers of this change were young top managers who had gathered firsthand experience in the United States or the United Kingdom. One of them was Ron Sommer, the former CEO of Sony USA, who in 1995 took over as CEO of Deutsche Telekom, the telecommunications division of the privatized post office. Between 1996 and 2000, Sommer successfully floated Telekom shares with unprecedented advertising campaigns directed mainly at savers who had no experience in the stock market. After the dot-com crash of 2000 and 2001, it became clear that Deutsche Telekom shareholders had paid absurdly exaggerated prices and faced losses of up to 80 percent. By the time Sommer stepped down in 2002, he had contributed significantly to the transformation of a sclerotic state-owned enterprise into a private, market-oriented corporation—as well as to the annihilation of the savings of millions of small investors.⁴⁵

Another star was Thomas Middelhoff, the CEO of the de facto family-owned media giant Bertelsmann (founded in 1835) from 1998 to 2002.⁴⁶ Middelhoff, who was fascinated by the new economy and

⁴⁴ See Bundeszentrale für politische Bildung, "Aktionärsstruktur von DAX-Unternehmen," <http://www.bpb.de/wissen/oZUWM5>; ARD, "Studie von Ernst & Young. Dax: Ausländer kaufen weiter zu," <http://boerse.ard.de/anlagestrategie/geldanlage/dax-auslaender-kaufen-weiter-zu100.html>; "Aktionärsstruktur des Dax. Wer steckt alles im Deutschen Aktienindex?," Private Banking Magazin, 8 June 2015, <https://www.private-banking-magazin.de/aktionaersstruktur-des-dax-wer-steckt-alles-im-deutschen-aktienindex-1433770687>; Andreas Prosvac, Frederik Frank, and Kay Bommer, "Investoren der Deutschland AG 2.0. Die Aktionärsstruktur des deutschen Leitindex DAX," presentation 2015, [https://www.dirk.org/dirk_webseite/static/uploads/Ipreo%20%20DIRK%20-%20DAX-Studie%20Juni%202015%20\(final\).pdf](https://www.dirk.org/dirk_webseite/static/uploads/Ipreo%20%20DIRK%20-%20DAX-Studie%20Juni%202015%20(final).pdf); Daniel Eckert and Holger Zschäpitz, "Ausländer übernehmen die Deutschland AG," *Die Welt*, 20 May 2015. All retrieved 22 Dec. 2015.

⁴⁵ Peter Glotz, *Ron Sommer: Der Weg der Telekom*, 2nd ed. (Hamburg, 2001); "Heute beherrsche ich alles, was ich brauche," *Die Welt*, 28 July 2014, <http://www.welt.de/wirtschaft/article130615513/Heute-beherrsche-ich-alles-was-ich-brauche.html>.

⁴⁶ Hartmut Berghoff, "Blending Personal and Managerial Capitalism: Bertelsmann's Rise from a Medium-Sized Publisher to a Global Media Corporation, 1950–2002," *Business History* 45, no. 6 (2013): 855–74.

the American corporate world, pushed ahead with daring investments in Internet firms. Colleagues and media referred to him as a “wildcatter” and a “deal junkie who likes to stir the pot.”⁴⁷ His Internet strategy did indeed turn parts of the conservative media conglomerate upside down, engaging it in an endless string of investments in Internet firms and their subsequent sales. The biggest and most lucrative of such deals was the sale of Bertelsmann’s shares in AOL Europe for \$6.8 billion in 2000, just in time to avoid the bursting of the dot-com bubble and to cash in on the shares’ grossly inflated value.

In 1998, Bertelsmann purchased Random House and thus became the world’s largest publisher. The book division transferred its headquarters to New York in 2011 and was renamed Random House. This step, the appointment of American Peter Olson as CEO of Random House, and the adoption of International Accounting Standards (IAS) were in line with the company’s new self-description as a “European-American media company with German roots.”⁴⁸ As for Middelhoff, he “was highly visible in New York, where he kept an apartment and sought the media spotlight, pontificating on panels and swanning around at galas.”⁴⁹ He presented himself as part of a cosmopolitan management elite. His financial results were mixed, though. Some truly lucrative deals were accompanied by glaring blunders. In 2002, Middelhoff resigned amid tension between himself—the visionary, in part reckless, modernizer—and the conservative business culture of the family firm.⁵⁰

Another example of this new type of executive was Klaus Esser. The lawyer with an MBA from MIT, who had worked in a New York law firm, joined the Mannesmann board in 1994 and became CEO in 1998. Although he initially fought vehemently against Vodafone’s hostile takeover (1999), he finally supported it. It was alleged that financial motives lay behind his sudden change of heart and that his severance package was excessive. Esser’s disloyalty to Mannesmann and the

⁴⁷ Jonathan Bing, “Bertelsmann CEO a Man of Mystery,” *Variety*, 29 July 2002, <http://variety.com/2002/scene/news/bertelsmann-ceo-a-man-of-mystery-1117870501>.

⁴⁸ “Editorial,” *Bertelsmann Management News* no. 64 (1998), 4.

⁴⁹ Bing, “Bertelsmann CEO.”

⁵⁰ Hartmut Berghoff, “From Small Publisher to Global Media and Service Company: Outline of the History of Bertelsmann, 1835 to 2010,” in *175 Years of Bertelsmann: The Legacy for Our Future*, ed. Corporate History Bertelsmann AG (Munich, 2010), 8–83, esp. 54–70. As CEO of Arcandor—the operator of Karstadt, once Germany’s largest department store chain—Middelhoff led this time-honored German retail concern into a spectacular bankruptcy between 2005 and 2009 and was subsequently charged with fraud, embezzlement, and tax evasion. After he was found guilty, he waited in prison for appeals of his conviction; from prison, he filed for personal bankruptcy in March 2015. See Jack Ewing, “Thomas Middelhoff, Ex-Chief of Bertelsmann, Must Remain in Jail during Appeal,” *New York Times*, 20 Nov. 2014; and “Ex-Arcandor-Manager: Thomas Middelhoff stellt Insolvenzantrag,” *Spiegel Online*, 31 Mar. 2015.

breakup of a company with a 110-year history and 138,000 employees were, according to the *Economist*, for many Germans “an affront to the traditional way of doing business in their country, where consensus is valued and executives are paid modest amounts compared with those in America and Britain. Indeed, in a country where hostile takeovers are a rarity, and hostile takeovers by foreigners virtually unknown, almost everything about Vodafone’s tilt at Mannesmann was deeply unpopular.”⁵¹ Esser’s severance package of around €31 million was at the center of several trials, and he was accused of *Untreue* (breach of trust), which could be neither verified nor refuted. In the end, the case was dismissed, with Esser having to pay an “administrative fine” (*Verfahrenseinstellung gegen Geldbuße*) of €1.5 million.

Severance packages reached unprecedented highs in the 1990s. For example, Middelhoff received around €20 million, Sommer around €12 million. At that time, these amounts were considered scandalous. But when compared with the United States—where Stanley O’Neal, CEO of Merrill Lynch, and Richard Grasso, CEO of the New York Stock Exchange, walked away with \$160 million and \$140 million, respectively—even the most controversial cases in Germany looked pretty small.⁵² General Electric’s legendary CEO Jack Welch received an estimated \$417 million when he retired in 2001. Pointing to the United States was a standard practice for German executives demanding higher payouts.⁵³

Middelhoff, Sommer, and Esser were not typical of the German managerial elite. On the contrary, they were exceptional figures, but their behavior is indicative of the direction of general change. The tenure of CEOs in the fifty largest German corporations shrank only slightly, from 9.9 to 8.4 years, between 1990 and 2000.⁵⁴ Despite the prevalence of a still relatively conservative top management, shorter time horizons, weaker loyalty to organizations, and a stronger interest in maximizing personal income were on the rise.

Even a look at some less controversial managers underscores that Germany’s corporate world was experiencing a truly transformative phase. In 1997, Heinz-Joachim Neubürger, a graduate of INSEAD and a former investment banker with J. P. Morgan (from 1981 to 1989), became the new

⁵¹ “Corporate Germany on Trial,” *Economist*, 23 Jan. 2004.

⁵² Dan Ackman, “Grasso Overpaid by Any Measure,” *Forbes*, 28 Aug. 2003; Liz Moyer, “Super-Size That Severance,” *Forbes*, 31 Oct. 2007. Robert Nardelli walked away from Home Depot in 2007 with a severance package worth \$210 million. See also “Richard Grasso,” *Wikipedia*, accessed 8 Apr. 2015, http://en.wikipedia.org/wiki/Richard_Grasso. Grasso’s package was contested in court, but all charges were dismissed in 2008.

⁵³ Christina Anselmann and Hagen Krämer, “Wie wird man Millionär? Erklärungsansätze steigender Topmanagergehälter,” *WISO direkt*, Nov. 2012, 4.

⁵⁴ This figure had been 12.3 years in 1980. Wolfgang Streeck, *Re-Forming Capitalism: Institutional Change in the German Political Economy* (Oxford, 2009), 82.

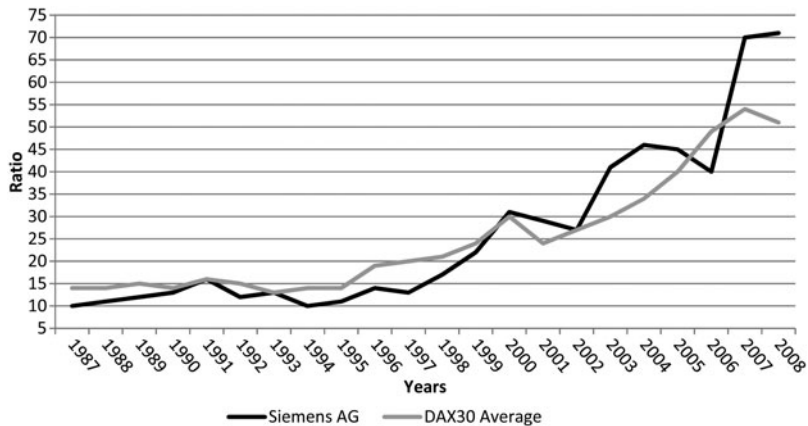


Figure 2. Executive board's compensation per head as ratio of total labor costs per head. Siemens AG and the average of all DAX 30 corporations, 1987–2008. (Source: Joachim Schwalbach, "Vergütungsstudie 2011: Vorstandsvergütung, Pay-for-Performance und Fair Pay: Dax30-Unternehmen, 1987–2010" [unpublished report, Humboldt Universität, Berlin, 2011]).

chief financial officer of Siemens. Neubürger's predecessor had worked his way up through the ranks, never having worked outside Siemens. The company's industry sector was shaken up in the late 1990s by Edward G. Krubasik, who joined Siemens from McKinsey in 1997. His appointment to the executive board was made against the vote of most workers' representatives on the supervisory board—an unprecedented event.

In terms of compensation, German corporations did not fully adopt American practices. In 1990, the average compensation of executive board members of the DAX 30 companies was fourteen times higher than the average per capita personnel cost in their firms (Figure 2). This ratio had risen to 24:1 by 1999 and then took off, reaching 54:1 in 2007.⁵⁵ Increasingly, compensation included stock options and performance-related elements. This significant increase caused much public debate but, from an American perspective, was relatively moderate.

Siemens paid its executive board slightly less than the average of DAX companies up to 1999. A real break in the trend came only in 2003/2004 when Klaus Kleinfeld, who had worked previously for Siemens in the United States, was appointed to the executive board and then made CEO. The next, even starker jump occurred in 2007

⁵⁵ Joachim Schwalbach, "Vergütungsstudie 2011: Vorstandsvergütung, Pay-for-Performance und Fair Pay": *Dax30-Unternehmen, 1987–2010* (unpublished report, Humboldt Universität, Berlin, 2011), 181.

when Peter Löscher was appointed CEO. Löscher was the first top executive in the 160-year history of Siemens to come from outside the company. He had previously been CEO of GE Healthcare and then president of Global Human Health of Merck & Co. For direct transfers from top U.S. positions, the average compensation of German managers looked inadequate. Thus, there was an enormous increase on top of the already steep rise in average executive pay.

Financialization and the Reinvention of Siemens AG in the 1990s

Financialization deeply affected the way corporations were run. German companies underwent dramatic changes but still did not lose all their traditional characteristics, and they certainly were not clones of Anglo-Saxon corporations. Unfortunately, few detailed business histories cover the 1990s. Siemens is an exception: the company commissioned a history to be written about the period from 1966 until 2011 and has granted unrestricted access to its internal documents.⁵⁶ On this basis, it is possible to observe from a microperspective how the principles of financialization affected a major industrial firm. There is no way of determining how representative Siemens is. However, it is fair to say that, by and large, this rather conservative enterprise, whose origins reach back to 1847, followed rather than led general trends.

During the 1990s, many industrial firms in Germany announced earnings targets for the first time in their history. Because those targets exceeded previous profits in most cases, many people took exception. The adequacy of margins is indeed an intricate question, and one that attracted more and more attention in the 1990s. In the case of Siemens, the search for higher earnings became a leitmotif of that era. The company was challenged by a chronic earnings problem that was aggravated by the recession of 1991 to 1993, the appreciation of the DM within the European Monetary System, and the end of the German unification boom. These short-term factors disappeared but the long-term structural reasons for Siemens's poor performance lingered.

Since the 1980s, globalization, deregulation, and digitization had been changing the basic parameters of the electro-engineering industry. Markets that once had been secure became highly competitive, and margins eroded. Hardware expertise—one of Siemens's great strengths—lost

⁵⁶ See Siemens AG, "Historians to Study Siemens' Development over Three Decades," Press Release, 17 Dec. 2012, www.siemens.com/press/pi/AXX20121214,e; and Hartmut Berghoff and Cornelia Rauh, *Die Große Transformation: Die Geschichte der Siemens Ag im Zeitalter der Globalisierung, 1966–2011* (unpublished manuscript, Munich, 2015). Due to obligations of confidentiality on the part of Siemens AG, not all sources within the following sections can be fully disclosed.

importance to software competence. Internal debates reached fever pitch in 1992, when the core business produced a 560 million DM loss. Of seventeen divisions, eight were in deficit. Yet the balance sheet still looked good and the company reported a profit of 1.8 billion DM after taxes, which corresponded to a return of 2 percent. This had been the norm throughout the 1980s.⁵⁷ At the beginning of the 1990s, Siemens was living off of its substance and reported profits that had not been earned in its core operations. Its enormous reserves and portfolio investments stabilized its position as a solid, first-class debtor. This was not an acute but rather a long-drawn-out structural crisis that posed no immediate danger but was unsustainable in the long run.

The reaction at Siemens—despite heated internal debates—was cool-headed and cautious. The transition from Karlheinz Kaske, an engineer born in 1928, to Heinrich von Pierer, a lawyer born in 1941, at the helm of the company in 1992 had long been planned and was not an emergency measure. The new CEO had been with Siemens since 1969. His career was absolutely typical of the Germany Inc. of his generation. Top managers were engineers or lawyers, hardly ever people with a background in finance, economics, or management. They had worked their way up in a company over a long period of time. Long stays in foreign countries did not typically occur. Their strengths lay in their extremely dense networks and their intimate knowledge of their firms.⁵⁸

“Keeping the Shop Together”: Cautious Crisis Management, 1990–1998

Heinrich von Pierer’s background did not make him blind to the necessity of far-reaching changes, but he proceeded gradually in order not to disrupt the firm’s corporate culture. Loss-making units had traditionally been tolerated and subsidized by profitable ones. In 1990/1991, 158 subdivisions operated profitably, while 122 sustained losses—some of them heavy ones, like semiconductors and IT. This practice was maintained but reduced step by step and supplemented by cost-cutting and productivity programs inspired by the experience of competitors who had implemented them much earlier.⁵⁹

⁵⁷ For an analysis of the 1980s and early 1990s, see Hartmut Berghoff and Cornelia Rauh, *Siemens 1966–1997: Die Herausforderungen der Globalisierungen* (Munich, forthcoming 2016).

⁵⁸ Hartmut Berghoff and Ingo Köhler, “Redesigning a Class of Its Own: Social and Human Capital Formation in the German Banking Elite, 1870–1990,” *Financial History Review* 14, no. 1 (2007): 63–87.

⁵⁹ George Eckes, *The Six Sigma Revolution: How General Electric and Others Turned Process into Profits* (New York, 2001).

Beginning in 1981, GE underwent a radical overhaul that left no stone unturned. Managers were traded out in a grand fashion. Revenues and returns rose as staff size dropped considerably. Relative returns were double to triple those of Siemens. Likewise, ABB completed a total restructuring, temporarily presented fantastic numbers, and managed to quintuple its share price between 1988 and 1996.⁶⁰ GE and ABB were able to offer their products at lower prices, which exerted downward price pressure on the entire industry. Deregulation of the markets and cost reductions of competitors worked hand in hand against Siemens.

GE's Jack Welch epitomized the shareholder-value approach to management. He closed factories, reduced payrolls, shifted jobs to low-cost countries, and cut or sold underperforming units. He broadened the stock options program to include nearly one-third of GE's workforce. The financialization of GE went so far that Welch added a huge financial services unit to the industrial giant. Today, GE's website celebrates Welch for having increased the company's market value from \$14 billion to \$410 billion during his tenure as CEO (1981–2001).⁶¹

For Siemens, GE was a constant point of reference but also the archetype of what Siemens did not want to be. GE's profitability was admired but never reached. Welch's brutal cost-cutting was closely observed at Siemens, but more often repudiated than emulated. When von Pierer started as CEO, he was told that he had "to keep the shop together."⁶² For him and many traditionalists at Siemens, social responsibility and coherence were key values because people were seen as the foundation of the corporation. Apart from this attitude, for which the *Financial Times* dubbed von Pierer a "social romantic," the legal framework in Germany prohibited von Pierer from engaging in the unfettered despotism of Welch's management style.⁶³ For von Pierer the support of the works council was paramount. He wanted to work with his staff, not against it. In general, he maintained close relations with workers' representatives. In fact, according to codetermination laws, they held 50 percent of the seats on the supervisory board and could obstruct almost anything. This setup reduced friction and conflicts.

⁶⁰ However, appearances were deceiving, and soon, hitherto hidden problems surfaced. Tatiana Zalan and Vladimir Pucik, "Rebuilding ABB (A)" (Case IMD-3-1797, International Institute for Management Development, 2007), 1–19.

⁶¹ "Past Leaders: John F. Welch Jr.," *GE.com*, accessed 11 Apr. 2015, <http://www.ge.com/about-us/leadership/profiles/john-f-welch-jr>.

⁶² Heinrich von Pierer, interview by Hartmut Berghoff and Cornelia Rauh, 5 Mar. 2013. For his attitude towards Welch, see Heinrich von Pierer, *Gipfel-Stürme: Die Autobiographie* (Berlin, 2011), 208–13.

⁶³ "A Pragmatic Capitalist and Social Romantic," *Financial Times*, 27 Nov. 2000.

Nevertheless, the extent of change in the first half of the 1990s was enormous. In 1993, von Pierer introduced the productivity program “time-optimized processes” (*top*), which had been codesigned by McKinsey. Workers’ representatives were also involved and supported the program, at least initially. Among other changes, *top* doubled the number of invention announcements to more than six thousand per year between 1992/1993 and 1996/1997. The share of turnover of products that were more than ten years old dropped from 22 to 7 percent.⁶⁴ More than before, locations were evaluated according to cost perspectives, which often led to closures of German factories. Von Pierer wanted Siemens to become a transnational company whose value chain was to be distributed worldwide to the most appropriate locations in each case. Although Siemens was still far removed from this ideal, it now had found its direction for future development.

As financialization requires metrics for performance, Siemens enhanced the transparency of accounting. Traditionally, Siemens had not openly evaluated the performance of its divisions. In 1994, the earnings of the eight sectors (*Arbeitsgebiete*), each consisting of one to five divisions, were published for the first time in order to “educate management.” From 1995/1996 onwards, the earnings of the fourteen divisions were published to push back the granting of hidden cross-subsidies. Transparency and management “by numbers” were the new guidelines.

Top was a success and a failure at the same time. For several years, productivity increased by around 10 percent per year. In this way, the company saved about 36 billion DM between 1991/1992 and 1996/1997. Unfortunately, these impressive gains were simply not large enough to keep pace with price erosion, the high cost of redundancy payouts, and negative currency effects. It was a vicious circle: the productivity programs of the entire industry accelerated the drop in prices, which, in turn, again raised the necessity of further rationalization. Siemens fell behind its competitors and suffered from notorious problem divisions—above all, semiconductors and IT. Although the executive board adopted neither a stringent nor overly harsh restructuring strategy, debates about necessary reforms abounded.⁶⁵ Still, the shareholder-value concept was perceived with a mixture of distance and suspicion. Surveys revealed that not even a third of Siemens staff considered shareholder value very important.⁶⁶

⁶⁴ Siemens AG, *Annual Report for 1996/97* (Munich, 1997), 6, and Siemens AG, *Annual Report for 1995/96* (Munich, 1996), 33–34.

⁶⁵ Whereas IBM and Philips in the period from 1986 to 1993 had each eliminated over one hundred thousand jobs, and GE eighty-eight thousand, the figure at Siemens was about forty thousand.

⁶⁶ Christian Stadler, *Unternehmenskultur Bei Royal Dutch/Shell, Siemens und DaimlerChrysler* (Stuttgart, 2004), 195.

“Germany’s Biggest Corporate Transformation in Years”: The Ten-Point Program of 1998

When another slump, caused in part by the Asian financial crisis, hit Siemens in 1996 and 1997, generating a negative cash flow of 3.9 billion DM, the need for immediate action became obvious. In contrast to the crisis of 1991/1992, increased pressure now came from outside. Analysts from investment banks and consulting firms had become decisive actors in the financial market. Whereas it had been difficult for them to schedule a meeting with the CEO of a large German company in the 1980s, these analysts were now attended to with great care. Analysts and consultants had internalized the shareholder-value concept and increasingly found attentive ears. They set standards for comparison and doled out merciless criticism. Thus, Siemens found itself ever more on the defensive.

External analyses of Siemens in the first half of the 1990s were downright devastating. McKinsey and Goldman Sachs pointed out that unit costs were 25 to 50 percent higher than those of its competitors.⁶⁷ Stock price performance was below average. Analysts spoke of a “Siemens disease.” The firm was characterized as “[a]n ailing corporate monster: no competitive culture, too slow, extremely low profitability and, as a result, generating no shareholder value.”⁶⁸ Analysts, critical media, and management pushed for reforms, while banks, shareholders, and institutional investors played no significant role.

Rumors circulated in 1997 and 1998 that von Pierer would soon be sacked—if true, he would have been the first Siemens CEO in 150 years to be fired. In order to reduce the pressure on both Siemens and von Pierer, the company presented its “10-Point Program” to the public, which the *Economist* called “Germany’s Biggest Corporate Transformation in Years.”⁶⁹ The message was that Siemens would henceforth play by the rules of the financial markets, completely restructure its corporate portfolio, and catch up with its competitors. In the face of this escalating crisis, traditionalists within Siemens lost ground and the board finally succeeded in overcoming blockades to reform. Von Pierer announced the following measures, among others, in July and November.⁷⁰

For the first time in its long history, Siemens got rid of an entire division. The loss-making semiconductor division was to be spun off. Later,

⁶⁷ McKinsey & Co, Inc., et al., *Wachstum durch Verzicht. Schneller Wandel Zur Weltklasse: Vorbild Elektroindustrie* (Stuttgart, 1994), 63–65; “Eine Revolution von oben,” *Spiegel*, 7 Nov. 1994.

⁶⁸ ANB AMRO, *Siemens: Scanning for Returns* (London, 2003), 2, 28.

⁶⁹ Graham Bowley, “Siemens Restructures,” *Financial Times*, 11 May 1998.

⁷⁰ Various press statements and speeches by von Pierer in 1998, ER 1076, ER 1005 AXX 079836, and 1198002, Siemens Akten Archive, Munich.

Siemens divested IT and all the telecommunications divisions, the historical heart of the corporation. *Top* was replaced by *top*⁺, which became compulsory for all divisions. Tolerance of unmet goals was revoked. Siemens established Economic Value Added (EVA) as a binding measure of performance. Now one could determine at a glance whether a particular unit added or diminished value. EVA had been developed in 1991 by the U.S. consulting firm Stern, Stewart & Co. This approach, which spread rapidly in the 1990s, was intended to reduce capital lockup and increase returns. Through identification of “dead capital” in the company, long-term cross-subsidies should be prevented. If a unit was identified as a weak point and restructuring failed, the unit would be sold or closed.⁷¹ To prepare for the listing on the NYSE, Siemens switched its accounting methods to U.S. Generally Accepted Accounting Principles (GAAP) in 1999/2000. Simultaneously, massive stock buybacks were announced to raise the share price.

Portfoliobereinigungen meant cleaning up the portfolio. Siemens stated that in order to “continually increase the value of the company . . . , we concentrate on businesses in which we can be market leaders.”⁷² Suddenly, the future of at least a third of the company, as measured by sales, was unclear. And with this, a fundamentally new perspective of the company took hold that was, at its core, oriented to the capital market. Siemens was no longer viewed as an organically grown whole but rather as a portfolio of an investor who buys and sells in the short term. Welch’s motto—“fix, close, or sell”—was taken up literally. Although it was in no way executed with the same rigor that GE displayed, an almost permanent restructuring began. Siemens also sought to strengthen the portfolio through numerous acquisitions, the largest being the industrial division of the Swiss Elektrowatt and the fossil power plant business of Westinghouse. Between 1991 and 2001, Siemens bought more than one thousand companies and spent €17 billion on mergers and acquisitions.⁷³

Traditionally, the culture of Siemens had been heavily influenced by German civil service. Lifelong employment and slow, steady promotion was the norm. The company often referred to itself as the “Siemens family.” This concept, which had cherished continuity, was now abandoned. The “family” became a volatile portfolio on the short springs of incalculable market forces. In 1998, the firing of two board members caused a sensation throughout the firm because executive directors

⁷¹ Holmstrom and Kaplan, “Corporate Governance,” 399–400.

⁷² Siemens AG, *Annual Report 1997/98* (Munich, 1998), 7.

⁷³ Kai Lucks, “Das Ende des Schreckens – Erfolgreiche M&A-Integration,” *Dialog intern*, June 2001, 15.

had previously been untouchable. The next level down—the boards of Siemens divisions—also saw numerous involuntary staff changes.

The pressure on middle and upper management grew. One result was the spread of dubious payments and corrupt practices. Although there is exact data only for the 2000s, it is clear that such activities increased considerably in the 1990s and were most pronounced where the new maxims threatened the existence of divisions. It was symptomatic that the telecommunications sector, which had lost its competitive edge, accounted for the majority of irregularities at Siemens.⁷⁴ Numerous interviews with lawyers and implicated Siemens managers confirmed that hectic reorganizations, ever shorter time frames, and the loss of traditional certainties created a sense of imminence that encouraged unethical behavior. Many middle managers involved in corrupt practices honestly believed that they were acting in the best interest of Siemens and would safeguard endangered divisions.

The end of job security was accompanied by new incentive models for board members. They received only 40 percent of their compensation from a fixed salary, with 60 percent tied to performance objectives. The variable portion diminished with one's place in the hierarchy. The Stock Corporation Act made it possible for managers to have stock options from 1998, and they did so from 1999 onwards. All in all, Siemens proceeded cautiously, although the new catchphrase was "high-performance culture." The change in rhetoric was remarkable. In 2001, management received the following messages: "The concept of 'core business' has largely vanished from our language"; "there are no inalienable units"; and there was "no longer any protection behind which one can hide." Further, "traditional thinking has given way to an orientation to the world class. . . . Above all, Siemens has internalized the high measure of the capital market."⁷⁵ At the same time, the annual report announced that various units with about sixty thousand people were to go. Such a sober announcement by the CEO—to divest "50 subdivisions of a total of more than 200 as a first step"—would have been simply unimaginable ten years earlier.⁷⁶

This ten-point program marked the end of the "old" Siemens AG, although the shift did not take place overnight. Debates about necessary reforms and their inadequate realization were to last well into the

⁷⁴ It is also indicative of broader changes in the corporate world that several other German corporations, including Daimler-Benz and Deutsche Telekom, as well as prominent European firms such as BAE, Alstom, Alcatel-Lucent, and Total, had massive corruption scandals in the 2000s that reached back into the 1990s.

⁷⁵ Michael Mirow and Michael Sieglin, "Konglomerat oder nicht Konglomerat," *Dialog intern*, June 2001, 7–9.

⁷⁶ Siemens AG, *Annual Report 1997/98*, 7 and 60.

twenty-first century. Despite drastic changes, the culture of consensus survived in part, and the program was never fully implemented. A 1998 comment in the *Financial Times* that Siemens had abandoned the German model “in favor of an Anglo-Saxon approach” covered only part of the company’s “breathtaking” transformation.⁷⁷

Conclusion

The tenets of financialization are universal.⁷⁸ However, the concept is modified in various national contexts due to divergent legal, political, and cultural frameworks. Regulations differ, as do the roles of unions, the structure of capital markets, and the attitudes of politicians and the public. Germany moved with hesitation and reluctance toward the American model from the late 1990s onwards without wholeheartedly embracing it. Although the adoption of some principles of financialization from American business schools and boardrooms appeared to many Germans as a kind of economic imperialism, one has to beware of linear narratives. Decisions were made in Germany, and many preconditions of financialization had already been in place.

Germany’s delay by at least ten years and its lasting objections to and deviations from financialization can be explained by the fact that various stakeholders other than shareholders and managers had more influence there than did their counterparts in the United States. Financialization changed German capitalism but not enough to dissolve Germany Inc. Despite dramatic changes in some of its parts, the most important pillars of Germany Inc. remained intact. Unions, employer associations, and works councils survived and continued to strive for consensus rather than for confrontational solutions, even if they were weakened through offshoring and a rising number of firm-level deviations from industry-wide agreements. The already low number of working days lost through strikes declined in the 1990s and was only one-fourth of corresponding numbers in the United States.⁷⁹ The equity culture remained weak as most Germans continued to distrust shares and despise the financial sector. Shareholder activism continued to be insignificant, just as private equity and venture capital stayed relatively small. However, the protective mechanisms that had shielded German companies from

⁷⁷ Bowley, “Siemens Restructures.”

⁷⁸ Jürgen Beyer, “Varietät Verspielt? Zur Nivellierung der Nationalen Differenzen des Kapitalismus durch Globale Finanzmärkte,” in *Wirtschaftssoziologie*, ed. Jens Beckert and Christoph Deutschmann (Wiesbaden, 2009), 305–25.

⁷⁹ In Germany, eleven workdays on average were lost per one thousand employees per year between 1991 and 1999; between 2000 and 2007, this number fell to five. In the United States, the corresponding numbers were forty and thirty-two. Hagen Lesch, “Erfassung und Entwicklung von Streiks in OECD-Ländern,” *IW-Trends* (Mar. 2009), 8.

market forces and risks—be they cross-holdings, networks, cartels, or *Hausbanken* (principal banks)—began to disappear. Insecurity and volatility increasingly featured in the landscape.⁸⁰

In general, financialization has a bad reputation, not least because of its social costs. At the same time, it might be too early for a final verdict; it seems likely that financialization reinvigorated many businesses and saved jobs that would have otherwise been untenable.⁸¹ German industry definitely emerged energized from its first decade of financialization. The “sick man of Europe” of the 1990s developed into an industrial powerhouse whose competitive position has continuously improved since 1995, as it lowered relative labor costs and raised productivity, especially in manufacturing.⁸² This advantage strengthened Germany’s export capacity, but also led to an increase in income inequality prior to 2007.⁸³ The slow and cautious adoption of financialization, coupled with the preservation of many traditional features of Germany Inc., might have been the secret of the country’s success.

Germany in general and Siemens in particular, were latecomers in adopting components of the new concept. It is hard to conceive what kind of alternative would have been available. The world was changing around them, with globalization breaking down national barriers in a period of rapid technological change. Isolation was not an option, especially not for a world-market-oriented economy and a multinational corporation. Siemens entered the 1990s with a massive earnings crisis and needed reforms to survive in the long run. The cautious approach of the early 1990s—increasing productivity and “keeping the shop together”—delivered impressive results but was insufficient to offset the impact of deregulation and globalization on an industry that had long benefited from secure markets. Thus, in 1998, Siemens finally flipped the switch and resorted to new radical measures like selling and spinning off major parts of the company. The fact that this happened without acrimonious conflicts again underlines the ongoing functioning of the coordinating mechanisms of Germany Inc.⁸⁴ Its culture of consensus seeking remained intact. As a consequence of these drastic reforms, Siemens was a more transnational, more efficient, and more profitable organization in 2000, although returns remained below those of major

⁸⁰ Jürgen Beyer, “Die Strukturen der Deutschland AG: Ein Rückblick auf ein Modell der Unternehmenskontrolle,” in Ahrens, Gehlen, and Reckendrees, *Deutschland AG*, 31–56.

⁸¹ For a balanced view, see Holmstrom and Kaplan, “Corporate Governance.”

⁸² Ludwig Siegele, “Germany on the Mend,” *Economist*, 17 Nov. 2004.

⁸³ Christian Dustmann, Bernd Fitzenberger, Uta Schönberg, and Alexandra Spitz-Oner, “From ‘Sick Man of Europe’ to ‘Economic Superstar’: Germany’s Resurging Economy,” *Journal of Economic Perspectives* 28, no. 1 (2014): 167–88.

⁸⁴ Stephen J. Silvia, *Holding the Shop Together: German Industrial Relations in the Postwar Era* (Ithaca, N.Y., 2013), 220–26.

competitors. It became clear that the need for restructuring would persist and that navigation of the company would mainly follow financial parameters. Siemens indeed had transformed itself from a stable “family” to a fluid “portfolio” requiring continuous changes.

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