Financialization and Changes in the Financial Structure of European Manufacturing Companies

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The relationships between the financial sphere and the real economy have been an important theme in theoretical debates since the crisis in the 30s and have been among major concerns in implementing economic policies.

The expansion of financial markets and financial activities in the context of financial globalisation and the new problems resulting from it during the last twenty years have revived this debate. It concerns notably:

- the links between financial market boom and financial instability;
- the consequences of the financial market boom on the balance of power among stakeholders involved in the ownership, financing and management of companies and;
- the impact of financial activity boom on production, and notably on productive investment.

This paper sets out to analyze the results of an empirical study on the structural distortion of manufacturing companies' balance sheets in the Euro zone: Germany, Austria, Belgium, Spain, Finland, France, Italy, the Netherlands and Portugal. It offers an analysis of the most representative ratios of the impact of European economies' financialization on companies' activities. The study - based on the development of the European Commission BACH database – concerns the period from 1990 to 2006. Financial activities in the nineties have been deeply influenced by the expansion of the "internet" bubble connected with the rise of the "new" economy.

The concept of financialization has several meanings. In this study we distinguish financialization of economies from companies' financialization. Financialization of economies refers to changes within financial systems favoured by financial globalization. Its consequences are the boom of financial markets, increase in stock prices and substantial reinforcement in the role of institutional investors. The shareholder's "revolution" is an outcome of these changes. Companies' financialization expresses the effects of increasing hold of "shareholder's value creation" objective on corporate activities and companies' balance sheets.

This study highlights the strengthening – very marked until the early 2000s – of manufacturing companies' financial activities to which the diminution of the share of tangible and intangible assets is the corollary. This change combines with the slowing down of investment rates, general reduction of salary percentage in turnover and increase in corporate profitability.

Other studies pertaining to non financial French companies as well as non financial companies of OECD countries in the 1980s relay quick increase of securities within total assets (Bardos M., 1993; Serfati C., 1996). Our study shows that financialization of non financial companies in several European countries in the 1980s also affects manufacturing companies in the euro zone and carries on until the early 2000s.

The central assumption of this work is that the financialisation of European economies as well as the tightening of European macroeconomic policies in the 1990s – transition period to the single currency - contribute to the decrease in the rate of productive investment through two main channels: the slowdown in demand growth and the emergence of new entrepreneurial strategies. These strategies favour the shortening of time horizon for corporate management and a Neo-Malthusian investment policy.

This study has three parts. The first part focuses on ratios used and their evolution. The second part presents the analytical framework of the impact of financialisation on productive activity. The third part analyzes financialisation of European manufacturing companies.

EMPIRICAL STUDY

Sample and data

The data analysed concern three categories of companies: companies of all sizes, large companies (turnover of more than 50 million Euros) and small companies (turnover of less than 10 million Euros).
The study relates to the period from 1990 to 2006, for which complete data for most countries are available.

The ratios analysed are as follows:
- Fixed financial assets/Total assets;
- Tangible and intangible assets/Total assets;

Income statement ratios are also analysed through:
- Net acquisitions of tangible and intangible assets/Turnover;
- Net acquisitions of financial fixed assets/Turnover;
- Compensation of employees/Turnover and;
- Net profit/Turnover.

Fixed financial assets include both stocks acquisitions, which provide the company with a power of control over other companies, and securities that the company intends to keep in the long term. Fixed financial assets ate mostly the result of external growth operations. It is deemed that speculative logic can influence the acquisition behaviour of securities of placement whereas the acquisition of fixed financial assets meets strategic objectives of the search of synergies and/or diversification strategy. In fact, distribution between these two categories of assets is very difficult. First, there is a very significant increase of the fixed financial assets' liquidity. It is also observed that minority interest may include, on the purchasing date of securities, long- and short-term motivations according to the opportunities and expectations of market evolution. Moreover, the legal limit setting the distribution between long-term financial investments and securities of placement is very different from one European country to another. For instance, it is 10% in France and 20% in Germany. Finally, statistical data indicate that the share of fixed financial assets in the balance sheet of small companies is too large (e.g. 40% of assets in Sweden, 24% in Belgium and Finland) to be considered fully corresponding to true long-term investments. For these reasons, the financial concerns and the search for capital gains seem to significantly contribute to the increase in the share of fixed financial assets.

Results

As the data available are not fully harmonised, the comparison between structures of balance sheets from one European country to another may not be appropriate. That is why our comments mainly focus on the evolution of ratios (Our remarks refer only to the averages of the ratios of the euro-zone countries).

The calculation of ratios enables the following observations to be made (Annexes 1-10):

- The fixed financial assets /assets ratio increases quite clearly during the period analysed for almost all the countries of the euro zone. This evolution mainly results from the growth of acquisitions in subsidiaries, the other fixed financial assets being generally a small (less than 5%) and quite stagnant share for all the groups of companies and all countries.
  The increase of the ratio is high for large and companies of all sizes of all the European countries. The increase is clearly lower for small companies within most countries.
- In 2006, fixed financial assets ranged from 11% (Italy) to 51% (the Netherlands) of the total assets of companies of all sizes. For five of the nine countries (Belgium, Spain, the Netherlands, Germany, Finland), the fixed financial assets /assets ratio is higher, or even a lot higher than the tangible and intangible assets/assets ratio.
  Amongst the three leaders of the euro zone – Germany, France, Italy – the growth of fixed financial assets within total assets of manufacturing companies is particularly fast in Germany - 16 growth points for companies of all sizes – compared to 4 points for France and 3 points for Italy.

- The tangible and intangible assets/assets ratio generally tends to decrease for companies of all sizes and large companies.

- The net acquisitions of tangible and intangible assets/turnover ratio also tends to decrease in most European countries, as opposed to the net acquisitions of fixed financial assets /turnover ratio which tends to increase.

- Finally, there is a decrease in the share of labour costs in the turnover of companies of all groups of sizes (all sizes, large size, small size) and a very significant increase in the net profit/turnover ratio.

These transformations indicate a strengthening of the financial activities of European manufacturing firms, corollary of the weakening of their productive activities. It should be specified that the distortion of the structure of balance sheets does not reflect the increase in the market price of securities, as until very recently, according to the accounting principles of Western European countries, securities were not valorised at the market prices but at the cost prices.

FINANCIALIZATION OF ECONOMIES AND PRODUCTIVE INVESTMENT

Financialization of economies constitutes one of the major transformations in the last quarter of the 20th century (Plihon D., 2000; Chesnais F., 2004). The years 1990-2006 which is the scope of this study, are also characterised by low rates of investment and growth in many European countries.

The first section discusses various analytical tools for catching hold of the impact of financialization on corporate strategies and more generally on corporate behaviour, notably in the area of investment. Thereafter, we examine the notion of financialization of strategies which provides the theoretical framework of our study. The main vectors of financialization of corporate strategies are then presented and finally, the impact of this phenomenon on productive investment.

Theses overview

The concept of financialisation was developed within the framework of post-Keynesian and Marxist analyses in close connection with concerns about the future of capital accumulation in the context of financial globalisation. However, the phenomenon to which it refers – the relationship between financial and real activities – is also analysed by other schools of thought and particularly by the neoclassical school.

According to the portfolio choice theory, companies would be faced with the alternative of choosing either to invest their funds in financial markets or make productive investments from expected comparative rates of return and risk aversion (Epaulard A., Szpiro D., 1991; Serfati C., 1996). The high rate of return of financial securities during the last two decades of the 20th century would have thus favoured the crowding out of productive investment by financial investment.

The main criticism of this theory concerns the relationship established between financial and physical assets. Models of portfolio choice assume that within every period companies have to arbitrate between physical and financial assets based on anticipated return and risk. The assumed reversibility between physical and financial assets in each period would allow for a perfect substitutability between them. The hypothesis of reversibility of financial assets at any moment is considered unrealistic since management decisions for physical investments are strategic, having a pluriannual dimension and producing irreversibility phenomena (Serfati C., 1996). The theory of portfolio choices is also criticized in that the assumption of reversibility implies that company directors are able to achieve optimal resource allocation because they know the returns of these two types of investment. On the contrary, according to the Keynesian theory, the rate of anticipated return is characterized by radical uncertainty.

The second analytical tool for understanding the relation between financial and real activities refers to the notion of finance parasitism. The term « finance » includes capital owners in the wide sense of it, shareholders and providers of loanable funds. By levying a part of the profit made in the form of dividends, financial charges or repurchase of shares, finance would prevent capital from being invested in a productive way. By strengthening the power of finance, financialization of economies accentuates the predatory character of the latter.
The idea of finance parasitism has inspired many studies. It is also corroborated by empirical studies particularly on non financial American companies (Orhangazi Ö., 2008).

This notion reduces the consequences of financialisation of capitalist economies at the level of corporate income distribution while neglecting its impact on investment and production. It also tends to overvalue the place of cash-flow in investment decision. The conception of predatory finance also seems to obscure the reality of power relations between company shareholders and creditors. The rising weight of financial costs in operating profit should not be considered as a sign of increased influence of creditors and especially banking institutions on companies. It is rather the result of a deliberate policy of capital owners – including institutional investors – to maximize leverage. However, debt-financing – which has been considerably encouraged by financial innovations (LBO operations…) – is not privileged just because it contributes to profit maximization of equity capital. It is preferred also because it contributes more effectively – through compulsory regular levies on operating profit – to making company directors undertake tight management of costs. Finally, reducing financialization phenomenon to finance parasitism tends to underestimate its consequences for yet another reason: potential capital gains which form a part of the return on equity capital do not result in income distribution.

The concept of financialization of corporate strategies (or corporate management) constitutes a third tool for analysing the effects of financialization of economies on investment behaviour and more generally on companies' productive activity (Batsch L., 2002; Plihon D., 2003). From this point of view, the effects of financialization are felt mainly at the level of strategic corporate decisions and not at the level of income distribution. Financialization of strategies contributes to the increase of income distributed (dividends and financing costs) but its negative effects are not limited to that alone. From a global perspective, this phenomenon results in the pre-eminence of financial performance and in the will to make this pre-eminence accepted in the making of both strategic and operational decisions (Batsch, 2002). Financial performance meets the objective of short-term "shareholders value" maximization.

The concept of financialization of corporate strategies seems most appropriate for analyzing the consequences of financialization of economies at the level of capital accumulation. It makes it possible to anchor the negative consequences of the phenomenon in the sphere of production and production decisions. It also highlights the dominant role of production relations on both productive forces and revenue distribution relationships. It finally makes it possible to conceive the multiple facets and implications of the phenomenon. The decrease in corporate cash flow on which the notion of finance parasitism lays emphasis is therefore seen to be one of the consequences – but not the only one – of financialization of economies.

Yet, there is little or no clarification of the premise of this theory in the studies that refer to it. Consequently we will try to clarify the theoretical assumptions of the concept in the paragraphs that follow.

Theoretical assumptions of the concept of financialization of corporate strategies

The first theoretical assumption on financialization of corporate strategies is that of plurality of objectives of the capitalist enterprise. These objectives can be maximization of profit or shareholder value but also growth, expansion of market power, power over its partners… This hypothesis, inspired by post-Keynesian theory, is opposed to the neoclassical theory according to which the maximization of profit rate constitutes the sole objective of the firm (Stockhammer E., 2004).

The second theoretical assumption of financialization of corporate strategies concerns the impact of institutions. Post-Keynesian analysis considers that the specific objective or the relative weight of the different objectives pursued by companies depend on the institutional context. This context reflects the balance of power between social classes and different categories of stakeholders involved in the ownership, management and corporate finance. The economic and institutional context of « The Glorious Thirty » has enabled the corporate "techno-structure" - in Galbraith's terminology – to concentrate powers within the company in their hands. Therefore, the objectives of shareholders are at that time opposed to managers'. The former are interested in maximizing dividends and rising stock prices while the latter are rather aspiring to power and prestige that accompany increased market power and accelerated growth. In the period of managerial capitalism of the "Glorious Thirty", therefore growth rather than financial profit maximization predominates.

The development of financialization of economies since the 1980s has induced significant changes in the relationship between shareholders and managers as well as in the ownership of share capital (Stockhammer E., 2004; Plihon D., 2003). Full liberalisation of capital movements – *a sine qua non* condition of financial globalization – reinforces international competition. It also enhances capital mobility and its ability to arbitrate instantly between markets and securities. The power of shareholders to control or sanction managers is then increased considerably. This change is rooted in the rise of new financial players. Institutional investors, who substitute for traditional shareholders through the rapid development of institutional saving, are managers of funds committed to good business management as a result of increased competition (Plihon D., Ponsard J., 2002). The nature of the relationship between shareholders and managers is then deeply modified.

The reinforcement of shareholders' power enables them to impose on managers new management criteria and profitability standards consistent with their preferences. This situation is enhanced by modifying the remuneration structure of managers themselves. This is reflected by increased relative weight of stock options. The development of stock options tends to align executive compensation with changes in stock prices. This contributes to the approximation of interests and class position of management and capital owners.

The basic objective of business becomes the "creation of shareholder value" (Brissaud L., Ménétrier R., 2000; Batsch, 2002). This statement refers not only to maximizing profit rate of equity capital (financial profitability), which has always constituted the fundamental objective of capital owners. It also refers to fixing very high target rates of return. The objective of "shareholder value" favours the establishment of new criteria for company evaluation such as EVA (Economic Value Added). EVA measures what remains as free economic liquidity flow which can be potentially distributed to shareholders once they themselves but also other contributors (employees, suppliers, State and banks) have been paid. A positive EVA thus means creating value for the shareholders in addition to a "fair" remuneration of invested capital. The objective of creating shareholder value has a very strong influence on corporate strategies during the period of liberalized finance.

The third premise of financialization of business strategies concerns the links between corporate operational and strategic choices on the one hand and ownership and power relations, on the other. These choices are not the result of technological or industrial imperatives. The selection procedure is fundamentally driven by the goals of enlarged capital reproduction. It is also influenced by the desire to consolidate the existing balance of power between owners and management (Batsch L., 2002).

The shareholder revolution first favoured the establishment of refocusing strategies for companies (Batsch L., 2002; Dietsch, 2004). These strategies aim at simplifying company structures and concentrating activities in areas where companies have core competences. Refocusing corporate strategies succeed to conglomerate ones, which played a predominant role during the sixties and seventies in both Europe and the United States. The desire to better control management was instrumental to this transformation. Indeed, the opacity of conglomerate company structures makes control on management very difficult. It also allows the subsidization of less profitable activities by more profitable ones (cross subsidization) (Jensen). Refocusing strategies thus become one of the instruments used by capital owners to discipline managers and increase "shareholder value" creation.

The unprecedented Mergers-Acquisitions movement (M-A) which was experienced by Western economies in the last quarter of the 20th century is the other major vector of "shareholder revolution" (OCDE, 2001; Kechidi M., 2001). These operations initially had a disciplinary dimension. They aimed at making managers adhere to the objective of "shareholder value". In the United States, the first M-A operations (1980-1990) are thus hostile due to the opposition of management. The introduction of stock options encourages adherence to the objectives of shareholders. M-A operations become thus almost exclusively friendly from the nineties. The rapid growth of M-A is considerably enhanced by strengthening role of institutional investors. Several studies indicate a strong link between the focus of M-A operations and sectoral investment strategies of institutional investors, notably Anglo-Saxons. These operations being settled mostly by share exchange, their development leads to a significant increase in the percentage of fixed financial assets in total corporate assets.

External growth strategies and policies of refocusing on core activities are closely linked. M-A operations often lead to dividing the company into departments of which some are integrated into the activities of corporate acquirers while others disappear or are sold.

Financialization of corporate strategies and productive investment

The objective of "shareholder value" creation and the corporate strategies it inspires have negative consequences on real investment.

The very high rate of return required serving as reference for investment choice leads to the elimination of many investment projects. Statements of European business leaders corroborate the negative consequences of fixing high profitability target rates of return on real investment (Batsch L., 2002).

The objective of "shareholder value" also encourages balance sheets "downsizing" policies, which are considerably facilitated by refocusing strategies as well. "Downsizing" policy initially takes the form of abandoning non-strategic and capital-intensive activities. These policies promote relative weight reduction of tangible and intangible assets. In some branches, externalization policies are pushed to the extreme. Manufacturing companies are concentrated on two ends of the chain – both of them requiring non capital-intensive investment - model design on one side and assembly and marketing of products on the other. Manufacturing is hence transferred to subcontractors – often established abroad, in countries with low labour costs - who also assume the investment risks. These subcontractors sustain at the same time the weight of value creation objective of contract grantors in the form of pressure for price reduction of their products. This double constraint is not conducive for dynamic investment. Finally, shareholder value creation becomes more than a guide on operational and strategic choices for the management of listed companies. It influences the strategies and behaviour of subcontractors. It even permeates – as well as the ideological principles that underlie it – the attitude and strategies of all types of companies, public authorities and even society as a whole.

Equity capital economy constitutes the other face of balance sheets downsizing strategies. The aim of minimizing the contribution of capital equity leads to financial strategies that tend to increase indebtedness and favour share repurchasing and LBO operations.

The objective of creating “shareholder value” contributes to the sluggishness of productive investment by promoting salary reduction pressures as well. The systematic policy of compressing payroll charges – a condition *sine qua non* for the creation of “shareholder value” – has negative effects on consumer demand. It also encourages the process of relocation to countries with lower wages and this tendency has accelerated in recent years. Investment demand is thus reduced drastically. If increased Gross Formation of Fixed Assets in higher technology activities does not offset this investment drain, as is the case with many European countries, including France, globalisation of production then becomes a weakening factor of growth and global competitiveness (Fontagné L., Lorenzi J.-H., 2005).

The rise of short-termism, which accompanies shareholder «revolution», is not favourable to the process of accumulation either. Indeed, the difficulties of anticipating due dividends in the distant future and the instability of the environment the past 25 years – financial globalisation, volatility of interest rates… - make shareholders more interested in short-term valorisation of share prices than in long-term dividend maximization. The shortening of temporal horizon of investors and management is also supported by the significant reactivity of stock prices to information (volatility of market prices). This volatility reinforces the prospects of achieving short-term profits and encourages speculation. Reinforcement of institutional investors in company shareholding has considerably contributed to the rise of short-termism. According to the literature on institutional saving managers, the stock markets dominated by institutional investors tend to undervalue firms with good long-term profit prospects but short-term low profitability. These types of behaviour are not conducive to taking the risk on investment.

Concerning the implications of the rise of external growth operations on productive investment, it is a controversial issue. These operations have undeniably contributed to strengthening the influence of shareholders on management. They have thus contributed to the sluggishness of productive investment. However, views differ on the possible crowding out effect that M-A could have on internal growth operations. Following several analyses, policies of downsizing, carving up and abandonment of activities in which many M-A operations have resulted, is an inevitable consequence of overcapacity that increasing international competition has greatly favoured (Holmstrom B., Kaplan S.N., 2001). Weak internal growth operations would then be explained by an excess of supply and not by the development of financialization. This point of view seems questionable. As stated previously, financialization of corporate strategies contributes to a drop in demand. Furthermore, it is very difficult to distinguish the consequences on internal growth operations of financialization of economies from those related to overproduction crisis. First, financial globalisation improves transparency and visibility of operators who can easily find undervalued listed companies with high growth perspectives and therefore a source of potential capital gains. Improving transparency and visibility stimulates the development of external growth operations. Furthermore, the significant increase in share prices over a long period promotes the development of equity control at the expense of internal growth operations as it allows the buyer to minimize the risk of loss, given the anticipated rise in “Price Earning Ratio” (PER). Expectations for rising prices also enhance the attractiveness of M-A operations, since these operations are now largely settled by exchange of shares. The same effect produces the rise of short-termism that accompanies financialization of economies because of the rapid adjustment of production capacity made possible by M-A operations.

FINANCIALIZATION OF EUROPEAN MANUFACTURING COMPANIES

Financialization of corporate strategies, which accompanies the phenomenon of financialization of economies, is one of the fundamental reasons for changes in the financial structure of European manufacturing companies. These changes are reflected by the relative decrease in the weight of tangible and intangible assets in favour of fixed financial assets. However, financialization of strategies and distortion of European industrial balance sheets structure in favour of financial assets also reflect the negative impact on investment demand of austerity policies implemented in Europe in the 1990s, a period of transition to the single currency.

First, we will discuss the negative effects on productive investment of the 1990-2000 European macro-economic policies. Thereafter, the major quantitative and qualitative factors of financialization of corporate strategies in European industrial companies will be clarified.

European macro-economic context, drop in demand and slowdown of capital accumulation.

Since the mid 1980s, the European macro-economic context is characterised by two major changes: the expansion of financial globalization and the relaunching of European economic integration with the Single European Act (1986) and the European Economic and Monetary Unification (EMU) project.

There is a close link between the relaunching of the European integration process and financial globalisation (Sifakis C., 2007). The Single European Act constitutes the first step towards the European monetary unification. It also paves the way for integrating the European community into the process of financial globalization and the shareholder “revolution”. Indeed, the Single Act (1986) calls for a reform package which includes a complete lifting of all barriers concerning the circulation of goods (single market) and services - especially financial services - and provides freedom of establishment of financial institutions (European financial area). Full liberalisation of capital movement, including movement of capital for non-residents, was also agreed on in the Act - without any condition of reciprocity, while only the liberalisation of European capital movements was necessary for the implementation of the European financial area, a complement to the single market.

The liberalisation of capital movements concerns capital transactions, the short-term operations, securities operations (acquisition by residents of non-quoted foreign shares and admission of foreign bonds and shares in the domestic stock exchange markets) as well as monetary operations (current accounts in local currency and in foreign currencies). Deregulation of European financial systems, as well as privatisation of banks, is also carried out within the framework of the European financial area. Liberalization of capital flows was to be completed by 1992. This reform which occurs at about the same time as the “big bang” of the City of London and the liberalisation of the Japanese financial system, constitutes one of the key dates of the financial globalization movement.

The EMU project leads to a tightening of macro-economic policies in Europe (Fitoussi, J.-P., 1994; Créel J., Sterdyniak H., 1995). Economic policies based on strict control of inflation were already in operation in most European countries since the late seventies. However, the nominal convergence process to which candidates for the single currency were committed, following the Maastricht Treaty (1992), has further buttressed the restrictive nature of the European macroeconomic policies. The Treaty of Amsterdam (1997) institutionalises the maintenance of these policies for the period after the introduction of the euro.

Disinflation promotes the reduction of nominal interest rates, which is consistent with the maintenance of real interest rates, especially long-term rates at high levels. This stimulates the growth of financial markets: high real interest rates improve the yield of debt securities whereas expectations of diminishing nominal interest rates favour stock price increase and therefore expectations in making speculative profits. Governments contribute to this growth through privatisations, “securitization” of public debt (France, Italy, Greece…) and establishment of a favourable regulatory fiscal framework. The development of financial markets is reflected by the considerable increase in the value of securities within GDP of European countries. This also leads to the increasing importance of securities in the income as well as in the balance sheets of non-financial corporations.

The restrictive nature of the European economic policies contributes to slowing down growth in demand, while financialization of economies reinforces the mobility of capital and its bargaining power *vis-à-vis* labour factor. The impact of these developments is the significant drop of wage share in the wealth created. Indeed, declining wage share in turnover is noticeable for all groups of manufacturing firms between 1990 and 2006 (annexes 3, 6 and 9).

Atonic demand in Europe constitutes the primary factor behind the slowdown in productive investment. It also leads to underutilizing production factors and achieving overcapacity that favours expansion of external growth operations.

The rapid growth of liberalized finance has contributed to the sluggish growth in Europe through an additional channel. The rate of return on shares especially the rate of expected stock market profits has been very high during most of the period under survey. During the same period, the long-time real interest rates that determine the cost of capital are at a high level in Europe, while increased competition caused by globalization and the single market makes valorisation of productive capital more difficult.

Financialization of strategies and structural distortion of balance sheets in European manufacturing companies

Financialisation of strategies of European manufacturing companies is mainly reflected by the increase of fixed financial assets’ share in total assets.

The analysis of the previous section has enabled us to identify the expansion of external growth operations, the development of outsourcing policies as well as the reinforcement of the role of institutional investors as major vectors of financialization of business strategies.

To assess the full extent of financialization of strategies in European industrial companies, we will rely on the following indicators: size and characteristics of M-A operations, extent in refocusing on core activities policies and importance of institutional investors in the GDP of European countries. The evolution of the regulatory context will also be analyzed. Emphasis is laid on the major economies of the euro zone, and more particularly on German and French economies.

The financial liberalization of European economies after the implementation of the Single European Act (1986) stimulates a process of external growth that creates considerable financing needs for big European companies. It also allows massive influx of Anglo-Saxon institutional investors into the European financial markets. Since 1991, about 10,000 external growth transactions are recorded annually in Western Europe i.e. 3 per day (de Perthuis Ch., 2000).

The rise of external growth operations is stimulated by a significant development of Foreign Direct Investment (FDI), which takes almost exclusively the form of M-A transnational operations. According to an OECD study, Europe has been in favour of 45% of the incoming M-A carried out around the world in the nineties and 60% of outgoing M-A, against 36% and 27% respectively for the United States (OECD, 2001). Three European countries – United Kingdom (21%), France (12%) and Germany (9%) – make up 42% of outward FDI for the period 1990-2000. The increase in the “critical” size of companies following the establishment of the single market has also contributed significantly to reinforce this phenomenon (Roche F., 1999, p.2). External growth expansion affects not only big companies but also small businesses. During the 1990s, 500 small and medium-sized companies were acquired in 500 international M-A worth $10.6 billion mostly from Europe or North America (OECD, 2001).

Rising stock prices facilitates this trend and explains the increase of shareholding as method of payment. In 1999 nearly half of the very large transnational M-A (exceeding €1 billion) is funded by shares. Increase in share settlements from the mid 1990s has contributed to the relative weight increase of fixed financial assets in corporate balance sheets.

Among the most active sectors much as in number as in amount of cross-border operations features the manufacturing industry, taking into account target companies as well as those that initiate operations. An OECD study notes that transnational M-A is the new face of industrial globalization in the 1990s. M-A between manufacturing companies represent from 40 to 60% of external growth operations carried out in Europe in this period (OECD, p.20). In Germany F-A activities have become permanent practice of industrial companies. The number of F-A has doubled between 1989 and 1990 and this along with the rise of the financial power of the Anglo-Saxons pension funds (Gehrke I., 2002, p. 151).

External growth operations fall within the framework of refocusing the activities of European manufacturing companies in their core business. According to the same study, over 80% of the amounts invested by European acquirers during the 1990-1999 period, were destined to get hold of companies within the same business sector. If we take into account target-companies, the share of intra-sectorial operations is 74%. A study conducted for the Economy and Finance Ministry in France states that one of the criteria used by investment funds for deciding to maintain shareholding is the pursuit by managers of refocusing on core businesses strategies. The development of external growth operations is an important channel for extending the shareholder value model in Europe. This point of view is corroborated by a study carried by the Commission-general for planning (Dietsch M., p.55).

The rise of external growth operations depends on and strengthens at the same time, the rise of institutional investors. One can appreciate this strong rise by examining the share of financial assets of institutional investors in the GDP of European countries (table 1) as well as the proportion of institutional investors in the financial wealth of households (table 2).

Table 1: Financial assets of Institutional investors/GDP (1990 – 2001

Austria		Belgium		Dane.		Finland		France		Germany.		Italy		Luxem.		Nether.		Portugal		Spain.		Sueden		G - B	
90	01	90	01	90	01	90	01	90	01	90	01	90	01	90	01	90	01	90	01	90	01	90	01	90	01
23	76	41	109	54	103	31	82	51	132	33	81	12	94	790	4337	119	191	8	52		62	80	154	104	191

Source : OECD, *Institution al Investors Statistics*, Volume 2003

Table 2: Financial assets of Institutional investors /Financial wealth of households

	1995	2000
Germany	35	42
Spain	24	33
France	40	48
Italy	15	33
Netherlands	59	62
Europe of 5	33	43
Grate Britain	59	61

Source : Plihon D., *Le nouveau capitalisme*, La Découverte, coll. Repères, p. 32

Increased role of institutional investors is also reflected by their growing weight in the market capitalization of listed companies. The detention rate for firms listed by institutional saving institutions is now well above 50% in France. The share of foreign investors has itself increased sharply and reached an average of 40% in 2002, in large groups of CAC 40 (Plihon D., 2003 p. 149). The same trend can be observed in Germany. According to data from the first investment fund in this country, 60% of the shares of big German companies is held by institutional investors (Gehrke I., 2002, p.49).

There is a cause-and-effect relationship between growing power of investment funds and increasing orientation of business management to “shareholder value”. Companies whose growing capital share is controlled by institutional investors are forced to adapt their management to the “shareholder value” model. A study of German and French companies (p.148) shows that the principles of Anglo-Saxon business administration model are progressing in both France and Germany. In the year 2000, a survey of firms was carried out in some Western European countries on the question of whether companies should give priority to shareholder interest or comparable importance to the interest of all stakeholders. According to this survey, 36% of French and 33% of German companies that participated in it are of the opinion that shareholder interest should be given priority. This same opinion was expressed by 22% and 17% respectively in 1990.

The role of Public authorities in the emergence and consolidation of shareholders capitalism is considerable. The radical financial liberalization of the 1980s opened the way for shareholder power control. Public authorities have also contributed to the establishment of new principles of corporate governance based on the U.S. model, in favour of sustaining shareholder value creation objective. These principles include the improvement of the quality of information for shareholders, protection of minority shareholders (among whom are institutional investors), modifying working rules of the Board of Directors with the aim of reinforcing control on management and removing anti-takeover measures. The new principles of corporate governance also provide authorization for share repurchase operations as well as forms of executive remuneration such as to encourage them to pursue the goals of "shareholder value".

In France government gives law force to two Vienot reports (1995 and 1999) written at the request of employers' organisations which establish the principles of "good" corporate governance inspired by the Anglo-Saxon model (Plihon D., 2003). In Germany there is a similar shift in the attitude of public authorities with regard to the principles of "good" corporate governance (Gehrke I, 2002 ; Jürgens U., Naumann K., Rupp J. (2000).

Institutionalizing the Anglo-Saxon way of good governance leads to weakening or even partially challenging the fundamental characteristics of French and German models of group control. These models are characterized by the notion of hard core (France), cross-shareholding (France, Germany) as well as central importance of banks and insurance companies – often holding shares with multiple voting rights – which ensure the coherence of the models (Plihon D., 2003; Morin F., 2000 ; Jürgens U., Naumann K., Rupp J., 2000).

Financial liberalisation and prospects of very high financial return turn banks and other financial intermediaries of patient shareholders into active promoters of value creation strategies. This trend leads to relaxation of the cross-shareholding system and partial dismantling of hard cores. Public authorities have encouraged this development. Thus, a tax reform decided by the Schröder government provides for the abolition of taxes on capital gains on assignment of shares as from the year 2000. This arrangement not only favours M-A developments but also encourages the questioning of cross-shareholding by inciting banks to dispose of their shares in equity capital of manufacturing companies (Jürgens U., Naumann K., Rupp J., 2000).

CONCLUSION

This study has shown that the financial structure of European manufacturing companies has been marked by a number of similar developments in almost all countries in the euro area. These developments include increase in the share of financial assets during the period 1990-2002 notably equity investment in subsidiaries. Corollary to it is the diminution of the relative weight of tangible and intangible assets. There is also a significant increase in net acquisition of financial assets in turnover while that of tangible and intangible assets is declining. These changes particularly characterize groups of big manufacturing companies. Finally, there is a rapid increase in net income and a decline in salary shares in turnover.

The distortion of the structure of balance sheets in favour of fixed financial assets reflects the financialization of European business strategies and sluggish demand in the euro area.

The financialization of European corporate strategies is reflected primarily by the considerable increase both in number and in volume of external growth operations in Europe during the 1990s. It is also reflected in the increasing weight of the institutional investors in all the euro zone countries as well as by the general policies of outsourcing and balance sheets' "downsizing".

The expansion of external growth operations has greatly contributed to the distortion of the structure of balance sheets in favour of financial assets. This impact has been the direct result of increasing settlement of these transactions by exchange of securities. It has also been indirect since M-A operations constitute a major vector for achieving shareholder value maximization, a factor of stagnating productive investment.

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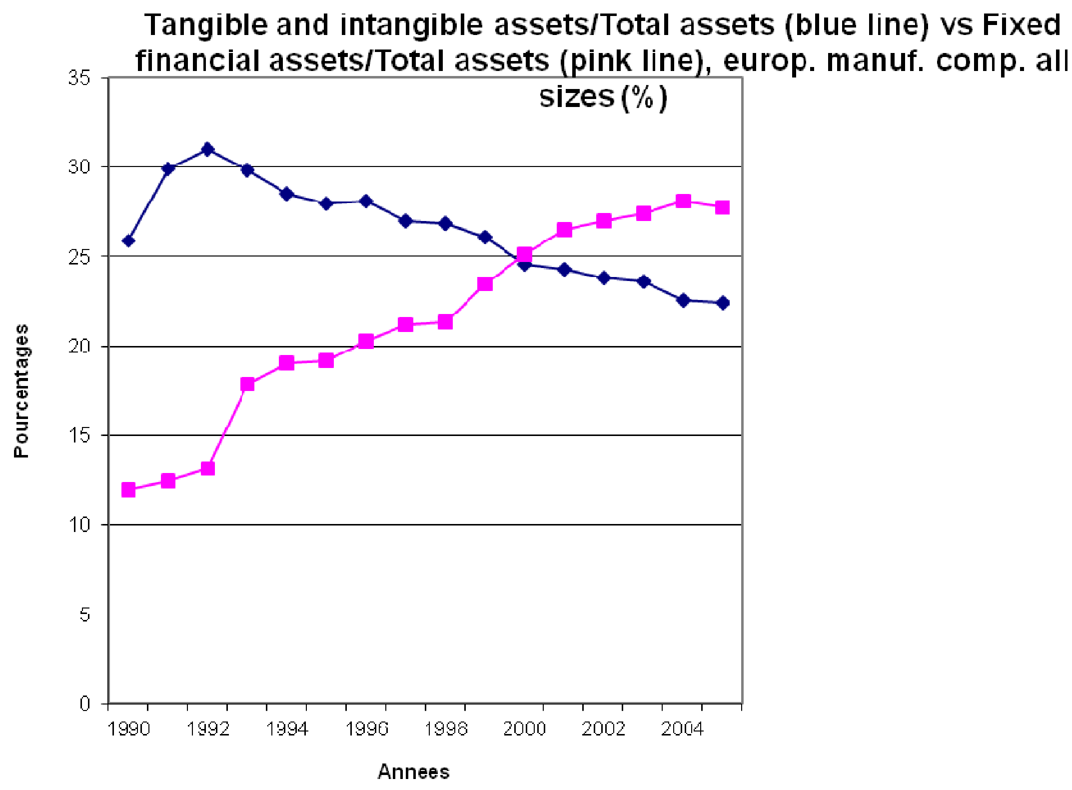
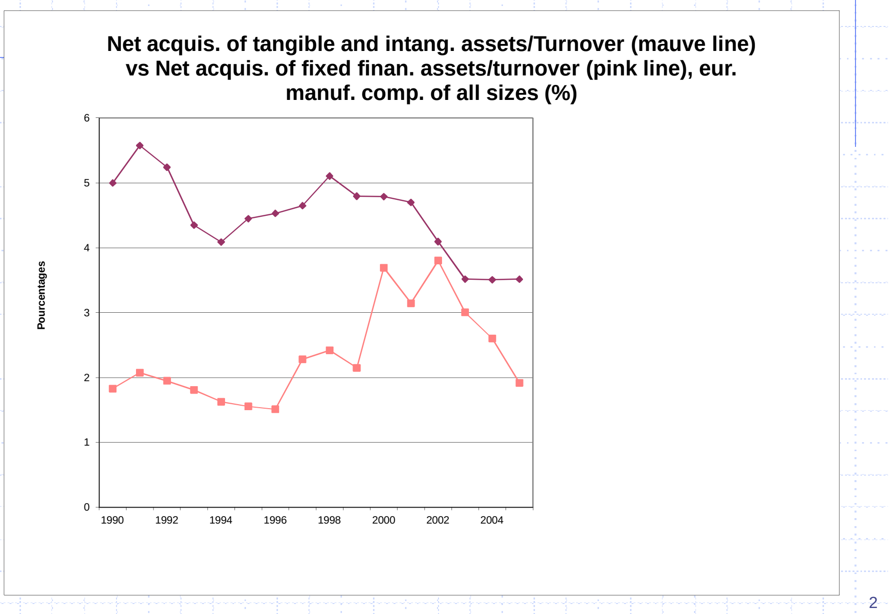
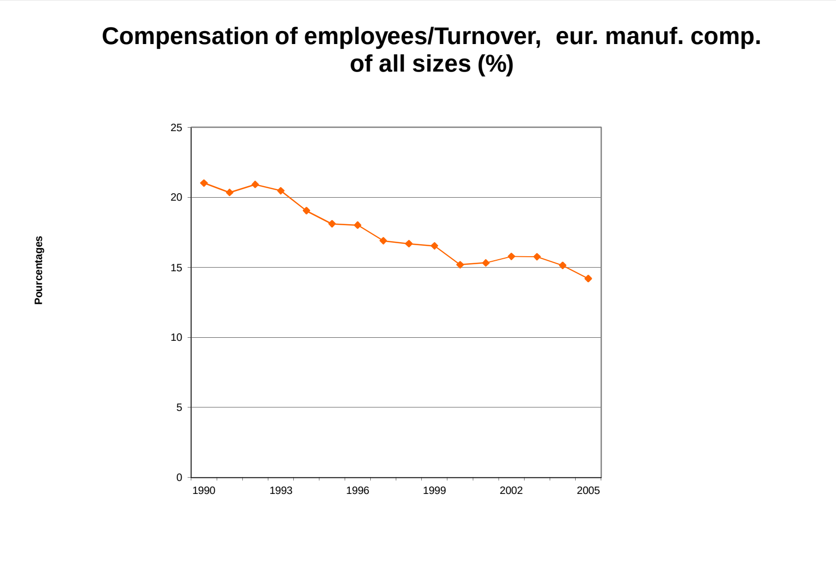
Annexe 1



Annexe 2

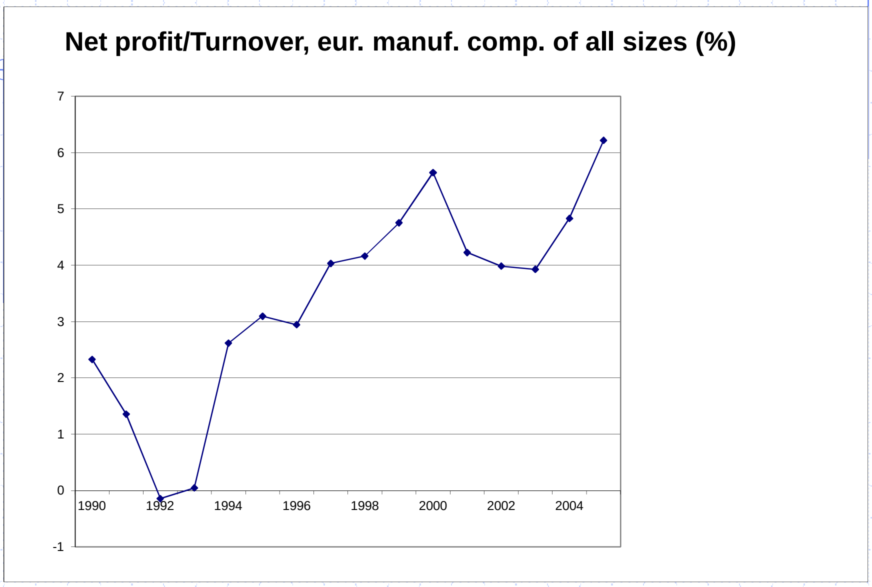


Annexe 3



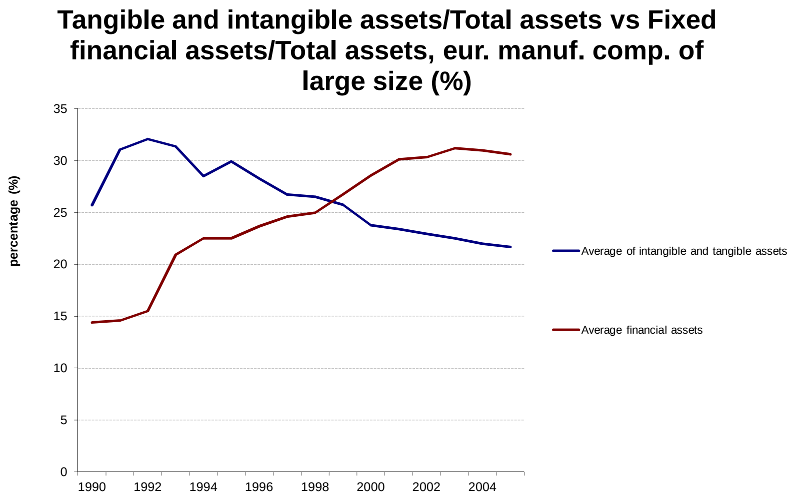
3

Annexe 4



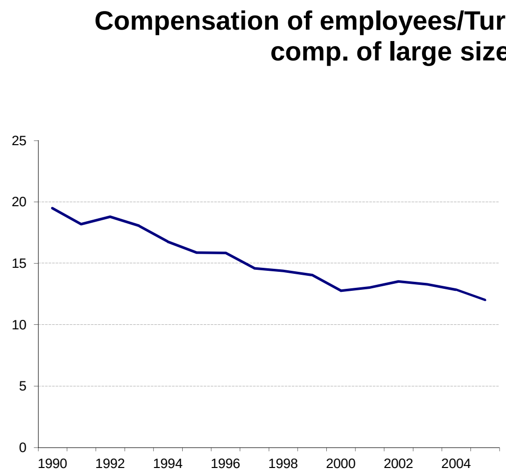
4

Annexe 5



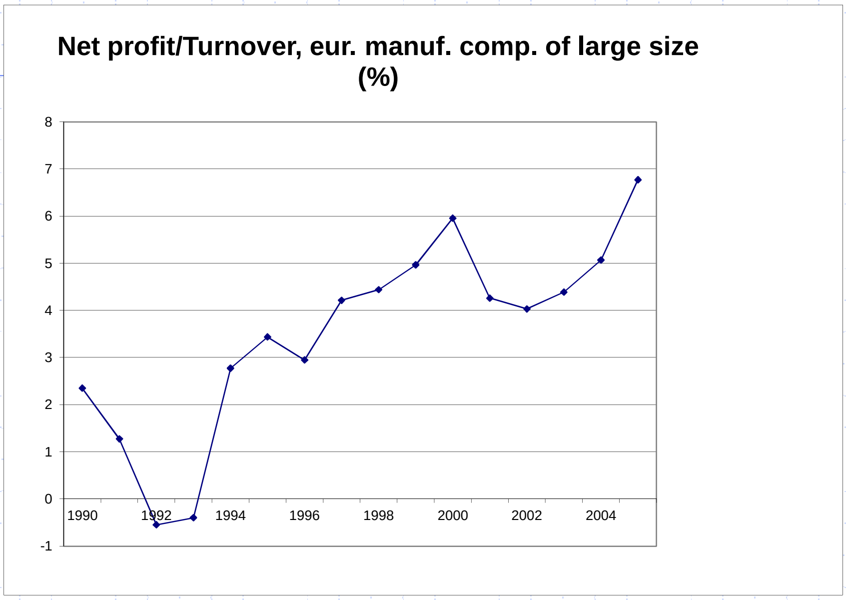
5

Annexe 6



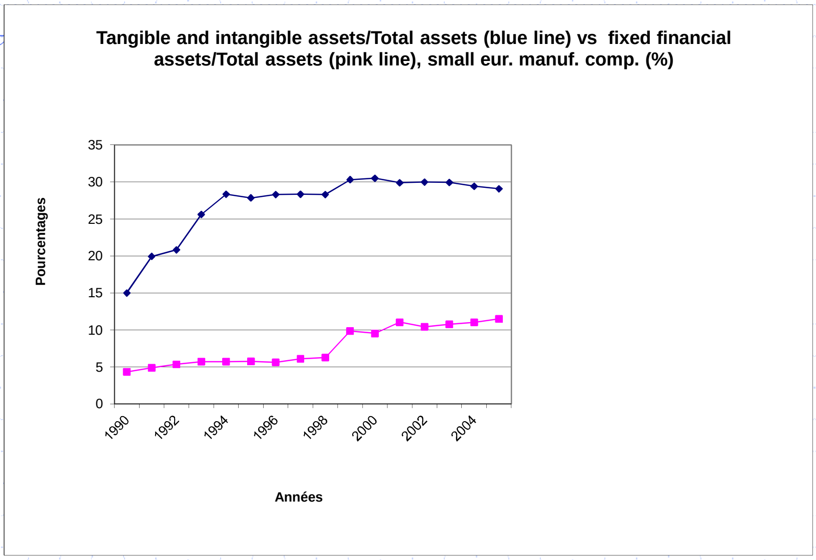
6

Annexe 7



7

Annexe 8



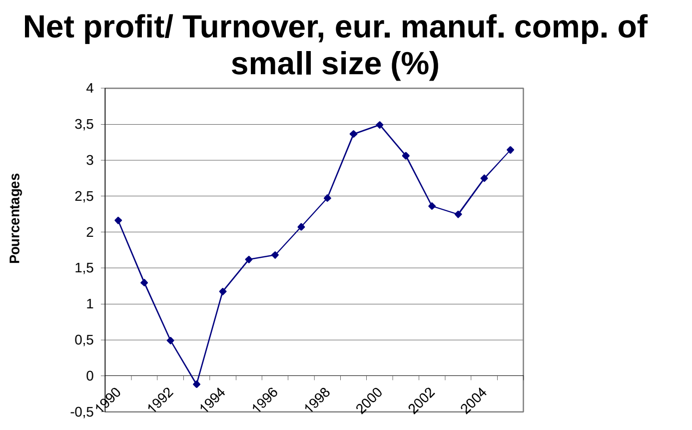
8

Annexe 9

Compensation of Employees/Turnover, eur. manuf. comp. of small size (%)
Pourcentages
29
28,5
28
27,5
27
26,5
26
25,5
25
24,5
24
1990
1992
1994
1996
1998
2000
2002
2004

9

Annexe 10


Net profit/ Turnover, eur. manuf. comp. of small size (%)
Pourcentages
4
3,5
3
2,5
2
1,5
1
0,5
0
-0,5
1990
1992
1994
1996
1998
2000
2002
2004

10