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Financialization and its Societal Implications: Rethinking Corporate Governance and
Shareholders

**A typology of shareholders and constellations of actors in the external
coalition of the corporation. An exploration for the German case.¹**

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1. Introduction

Today's listed companies must explain and justify their strategies to capital market actors (Froud et al. 2006).² This is the core of a broad definition of (control) financialization, which we take as a basis in this paper (see Faust/Kädtler 2017). The debate that has now been going on for a good fifteen years in the relevant disciplines of economic and industrial sociology and political economy has generated a standard diagnosis for the transformation of the German model of political economy and corporate governance: that the German economy and society has entered a new development phase that can be identified as financial market capitalism (Windolf 2005a,b; Haipeter et al. 2016; Minssen 2012). Since the early 1990s, the dissolution of the proverbial "Deutschland AG" ("Germany Inc.") has been regarded as a core element of this transformation in the German model. Germany Inc. ("Deutschland AG") was characterized by the entanglements among the hundred largest German companies and by large banks and the insurance group Allianz holding shares in nonfinancial corporations,³ with the latter often serving as a stabilizing anchor investor.⁴ As Allianz and the banks retreated from their roles as shareholders at the crossholding center of the German economy, accompanied by a far-reaching (albeit incomplete) withdrawal from exercising corporate oversight, institutional investors rose to replace them as "new owners" (Windolf 2005a). As time went on, the structure of institutional investors simultaneously became more global.⁵ For various reasons, there is controversy (see Faust/Kädtler 2017 for an overview) over whether the newly emerging German political economy can be adequately conceived under the "financial market capitalism" diagnosis. For example, it is (more than) doubtful whether the corporate world in Germany actually consists primarily of listed companies with broadly distributed ownership by institutional investors (see Faust/Thamm 2015, 2016), as Windolf's (2005b) theory of financial market capitalism has assumed. Notwithstanding this and other controversies (Deeg 2005; Faust et al. 2011a; Faust 2011; Höpner 2003; Jackson 2005; Jackson/Sorge 2012; Jürgens et al. 2000; Vitols 2004), however, the undisputed fact remains that institutional investors in listed companies have gained in importance since the 1990s and are increasingly coming from abroad, and hence from institutionally and culturally "foreign" contexts. This development raises the question of whether institutional investors influence the listed companies in which they hold shares, as well as what kind of pressure they exert, which areas or issues are affected, and how uniform their influence is.

Regrettably, the research that deals with the change in the German corporate model has not pursued the empirical questions about the role and influence of institutional investors and analysts, but rather has used theoretical means to block off this direction of inquiry prematurely. The agency theory of the firm (Jensen/Meckling 1976), which developed in the US within the milieu of financial economics, defined the interests and fundamental strategic options of the actors said to hold decision-making power (management, shareholders). It became an established legitimation theory for modern "investor capitalism" (Useem 1996) and was hastily accepted as a description of institutional investors' and managers' actual conduct and their opportunities for action also within the critical camp. Windolf's (2005b) theory of financial market capitalism reads this way for long stretches.

This is how a conception of "financial market capitalism" became established in which theoretical deduction provided proof that institutional investors forced management to maximize profit in the short term, precluding innovation-based growth strategies associated with the long term. Thus established, the prioritizing of

1 This paper is a modified English version of an already published book chapter in German: Faust (2017). The empirical findings on which this article is based are taken from the research project "Financial Markets Orientation of Firms and Codetermination." We are grateful to the Hans Böckler Foundation for supporting this project. Casey Butterfield translated from German to English – for all remaining mistakes or lack of clarity the author should be called to account.

2 This is the deliberately broad definition in Froud et al. (2006). The authors start by criticizing the prevailing strategy discourse at business schools for its "common problem definition" involving "the firm in industry facing the product market" (p.8). They characterize it as having become anachronistic for its lack of consideration for the capital market, arguing that capital market pressure "has reshaped what American and British giant-firm management says and does" (p.4). Quite deliberately, Froud et al. refrain from equating this exposure to capital market pressure to "one invariant set of consequences in terms of firm performance or management behaviour" (p.7), subjecting it instead to a historically specific, contextualized, and situational analysis.

3 Shareholding by banks was not the central feature of a "bank-based" financial system (Vitols 2005), the term often used to characterize the German model of capitalism (Zysman 1983). Much more central was the house bank's relationship as a creditor and the role of the supervisory board, which was not based primarily on voting rights from individual shares, but stemmed from the bank exercising its voting rights as a depositary trustee.

4 See also Streeck/Höpner (2003).

5 The withdrawal of the German banks and Allianz from Deutschland AG was an aspect of the same process of globalization that brought international investors to Germany: from Germany to the world, from the world to Germany.

shareholder interests merely allows strategies to push down wages in favor of capital gains and to increase the precariousness of labor (Deutschmann 2005; Dörre et al. 2011). An empirical analysis of the interest definitions, strategies, and opportunities for action of capital market actors seemed as unnecessary as a more precise analysis of its “epistemic practices” (Mars 1998): the evaluation, framing, and categorization of the company being analyzed.⁶ Moreover, the standard theory of financial market capitalism implies that the “funds [use] the voice option when they coordinate their behavior and force management to follow their instructions” (Windolf 2008: 531). In this case the management – as provided in the agency theory of the firm – becomes a “fungible agent” of the new owners, while at the same time the new owners are conceived as a collective acting uniformly (Windolf 2005b: 5, 23). At the same time, it is assumed that the suggested and therefore implied mechanisms in agency theory for the transmission of the “operational logic of the financial markets on the real economy” (ibid.: 1) are available and effective: (a) hostile takeovers, (b) a market for corporate control, and (c) stock options as a compensation instrument of top-level management that is expected to produce a consonance of interests among shareholders and managers. In this theory of financial market capitalism, then, two different mechanisms of control and influence are brought to bear that cannot be readily reconciled. In contrast to these latter mechanisms, which make “the control exercised by financial markets” appear “abstract, anonymous and factual,” (ibid. : 5), the managers are immediately brought to heel when the voice option is exercised.

As we have already pointed out elsewhere (Faust/Kädtler 2017), we advocate always analyzing the relationships of individual stakeholders (here various types of shareholders) to the company within the overall structure of where the company is embedded. Such embeddedness results in contradictory expectations that are endowed with different enforcement powers depending on the constellation. Each individual stakeholder analyzes their chances of influence and articulates their expectations not only in the light of their own respective rights and other sources of power, but also by taking into account the claims or expectations articulated by other stakeholders and their chances of enforcement, which may also be legally regulated. From this it follows that the interest definitions and influence of shareholders (and their representatives or fiduciaries) *operative in practice* must be subjected to *actual* analysis as part of the analysis of these constellations; interest definitions and ways of interest pursuit cannot be derived from agency theory suppositions (as the current legitimation theory of an investor capitalism) (see Faust et al. 2011a).

We endeavor to make such an attempt in the present paper by analyzing one of the external stakeholder groups of the “multireferential enterprise” (Faust/Kädtler 2017), namely shareholders, and with them a section of the possible external coalition (Mintzberg 1983) of listed companies. We are fully aware that a complete analysis must also include other stakeholder groups’ interests, guiding principles, and chances of enforcement, but one must start somewhere. We do this through a typological analysis (see second section), distinguishing investment strategies according to the connection each one has to the real economy object of reference: the company (see Faust/Bahn Müller 2007). This permits initial insights into different interest definitions and ways of pursuing interests. To this typology of investment strategies we then assign different, empirically available funds and investor groups, illustrate them, and undertake to estimate their respective empirical relevance for Germany. This analysis step on the one hand demonstrates a considerable range of different connections to the real economy reference object that do not fit with the image of a uniform collective actor. On the other hand, interest definitions and strategies for pursuing interests cannot be analyzed in isolation, but rather only in typical constellations. Thus activist hedge funds (a subset of investment strategies with an explicit connection to the real economy reference object) are rather improbable and ineffective in the constellations frequently occurring in Germany, where listed companies have anchor investors and are therefore equipped with “patient capital” (Culpepper 2005).

In the third section, we abandon a fiction from the second section: that each investment strategy in the typology defines one limited actor. Investment strategies are best defined at the level of an individual fund and therefore also securely determined for external observers. In fact, however, some funds are typically part of larger investment companies with heterogeneous and sometimes mutually opposed investment prospects. This poses the question of whether the different interest definitions and strategies for pursuing interests are unified within the investment company, how this occurs in such cases, and what consequences this has for the various levels of the pursuit of those interests.

⁶ Similar to Benjamin Braun (2015) we advocate for the integration of micro-sociological studies of finance as epistemic practices and a more macro-oriented political economy approach that considers institutions and institutional change. These two necessarily meet at the meso-level of organizations. For earlier attempts see Faust and Bahn Müller (2007) and Faust (2011).

The conclusion summarizes the commonalities and heterogeneity of interests and interest behaviors of the various shareholder groups in the typology and the typical constellations in which they appear, the latter of which also represent the different degrees of strategic leeway available to management and other stakeholders.

2. Investment strategies with various connections to the reference object - a typology

The starting point of our analysis is our conviction that the fundamental assumptions of agency theory cannot adequately describe the interests of shareholders and the ways in which they pursue those interests. The unfeasibility of maximizing shareholder value is twofold: for one thing, maximization in the strict sense is unobtainable (see Faust et al. 2011a); for another, the interests of shareholders are not permanently fixed. “Demands of the shareholder value rhetoric are confusingly variable,” as Froud et al. (2006: 44) have stated, and Lynn Stout (2012) has pointed out that the premise set out in the shareholder value ideology (that the shareholder is interested in a short-term increase in the share price of the company those shares belong to) is just one definition of the interest of the shareholder, and a very narrow one at that. By way of contrast, Stout draws attention to the fact that shareholders as a group (“the universal investor”) are broadly invested and can therefore also be interested in the overall endurance of an economy that grows, maintains investment opportunities, and yields revenue: “[...] in directing managers to focus only on share price, shareholder value thinking *ignores the reality that different shareholders have different values*. It blithely assumes that the question of corporate purpose must be viewed solely from the perspective of a hypothetical entity that cares only about the stock price of a single company, today” (Stout 2012: 9). This perspective has been supported by Deeg and Hardie (2016) in suggesting that one should investigate the possible occurrence of “patient capital” more broadly, i.e. also among institutional investors, and not only as a characteristic of traditional owners (banks, families, other companies) in a “coordinated” (Hall/Soskice 2001) or “organized” (Höpner 2003; Streeck 2009) variant of capitalism as which Germany has been treated in political economy textbooks.

But how can one differentiate between different interest definitions and the various strategies for pursuing those interests? We take a first step with the typology of investment strategies that follows by documenting what, if any, connection each exhibits to the “real economy reference object.”⁷ Alternative typologies focus directly on the distinctions among investment companies or funds that are strongly influenced by the respective institutional rules, for example distinguishing between “mutual funds” and “alternative investment firms” (Braun 2016) also known as “hedge funds” (Goyer 2006). But these typologies avoid relevant differences in the connection to the real economy reference object that exist within each of the institutionally defined categories. We, on the other hand, take the second step of adding the institutionally defined degrees of freedom and constraints as an additional criterion. Financial sociology, at least if one wishes to follow Knorr-Cetina (2007), assumes that financial markets and financial market actors are generally unconnected to a “real economy reference object” in their epistemic practices. By contrast, we regard self-referential financial markets in these terms as only as *one* variant of an assortment of connections. This is presumably true for many financial markets, but certainly for the stock market. On the *stock market*, different actors have different representations of the market or the “objects” being evaluated and traded. This reflects the dual character of a stock: “It is on the one hand a monetary or other asset form that can emancipate itself from the movements of the economic units to which it originally referred (it was issued), and on the other hand a legal title that substantiates rights of property or control rights, which in turn establish the potential for a closer retrospective bond” (Faust/Bahn Müller 2007: 69). The variety of connections to the real economy reference object provides a first step for determining interests and possible ways of pursuing those interests. More or less gratifying learning opportunities may arise for the real economy reference object (and its representatives), depending on the extent to which investors’ connections to the issuing company include a social relationship, including communication and the potential for reciprocal influence. We therefore distinguish between these three investment strategies:

⁷ As we shall see, we must take into account two types of actor status: first, the individual fund, each of which independently determines its connection to the real economy reference object or receives that connection at the time it is founded, for example by being designated as an active fund with the benchmark DAX index, and second the fund company, which can combine different types of equity funds, fixed-income funds, and alternative investments/hedge funds under one roof and must define how to consolidate and/or integrate interests and what this says about the pursuit of those interests.

- Investment strategies without a connection to the real economy reference object
- Investment strategies with a connection to the real economy reference object
- Investments as a means of exerting strategic control or decisive influence

We examine the relevance of the different investor categories and illustrate them with support from our own case study material or from the literature. We then consider what this reveals about each group of actors' interest definitions and opportunities for action. *Institutionally defined rights and obligations* play a role here, as do *constraints on action*; these may bear upon the relationship to the company in which the relevant investment fund is invested, but they may also concern the relationship to the investors who have "entrusted" monies to the fund as a fiduciary for savings and/or growth purposes.⁸ The degree of *organizational⁹ and field-related embeddedness* is relevant for the definition of interests, and even more so for the opportunities for pursuing those interests: to what extent are interests uniformly defined and uniformly pursued; who is available to join coalitions? Finally, there are cognitive-cultural framings, varying in time and space, that serve as guides for defining interests and viable and appropriate ways of pursuing them.

2.1 Investment strategies without a connection to the real economy reference object

We group the following investment strategies in this category:

- Passive strategies, such as index funds, that track only a given market structure, without selecting reference objects.
- Behavioral finance strategies that make their selections by observing the selections of other market participants or on the basis of (putative) psychological "regularities" (the momentum strategy, for example).¹⁰
- Quantitative strategies (justified with analytical charts) that buy or sell stocks when the price development exhibits certain patterns that (supposedly) determined further price developments in the past.
- High-frequency traders, also called algo(rithmic) traders, who attempt to use super-fast computers to exploit extremely short-term arbitrage gains of various types (Beunza/Stark 2004).¹¹

What all these strategies have in common is that the price developments on the stock market itself become the reference used for the investment decision. Whether and how the economic results of the company "behind" the stock have evolved or will evolve does not play a role at the most indirectly, for example because market participants with other investment strategies ensure that a company is included in an index. In the aggregate, these investment strategies also generate price movements, but such movements are incomprehensible to the company affected or to other observers. Furthermore, since the strategies and their motives relating to the company are not communicated, or do not exhibit any connection to decisions made at the company level in the underlying market theory, a (mere) price movement cannot trigger a learning effect either. This process does not give the company in question a better grasp of the expectations it should live up to, nor an understanding of what it should do (differently). From the perspective of the issuer, it is simply noise. These strategies therefore

⁸ National differences play a major role here (Kahan/Rock 2007; Becht et al. 2014). The main focus of the debate is usually on issues of corporate governance (Faust 2013), meaning questions covering shareholders' rights and obligations in relation to the company and other stakeholders. Also important, however, are the rights and obligations of asset managers and/or institutional investors vis-à-vis the "actual" investors. These vary both internationally and in the same national context (aspects such as disclosure obligations, payout and thus liquidity obligations, or risk-spreading requirements) among fund and asset managers, for example the differences among mutual funds, public pension funds, and hedge funds (see Kahan/Rock 2007).

⁹ Funds are often part of a higher-level investment company that can include equity funds with various investment strategies, as well as funds from other investment classes such as corporate bonds, which may suggest other definitions of interest with respect to the company. The way in which such different interests are consolidated and how much weight they carry when the interests in relation to the real economy reference object are being defined (for example regarding the exercise of voting rights) is therefore an organizationally framed decision and cannot be "derived" from an abstract definition of interests based on what the connection to the reference object would suggest.

¹⁰ Beunza/Stark (2004: 376) call this group "extrinsic," whereas arbitrage traders are designated as "associational."

¹¹ The investor relations managers interviewed pointed out that these "shareholders" could not even be registered as such; they were "irrelevant to issuers" (IR U1).

exert no influence which these external actors do not have in mind either. Neither do they have any message.¹² This is highlighted by the complaint recently put forward by John Cryan, the head of Deutsche Bank, now that passive index funds comprise 36 percent of Deutsche Bank's shareholders: "he cannot say what his major shareholders want him to do; in many cases he simply has no one to contact" (Handelsblatt, 3 Aug 2016, p. 29).

Index funds have a certain intermediate position and merit an additional comment (see Braun 2015). Although the managers of index funds do not have a fundamentally reasoned selection process, by definition, and therefore do not need to concern themselves with the strategy and prospects for success of the respective companies, their selection nonetheless depends indirectly on the success of the companies in the index, since such companies have only achieved that inclusion based on their market valuation. Thus companies can also be dropped from an index because of a relative lack of success, or they can grow into inclusion based on a better valuation. This marker of success is always based on market valuation, however. If such funds are invested in a particular index, the performance of the fund is in turn dependent on the development of the included companies as a whole, inasmuch as this is reflected in their market prices. From this, we can derive that there is a theoretical interest in all companies in the index experiencing favorable development. This theoretical interest would correspond to that of the "universal investor" (Stout 2012). Whether and under what conditions this theoretical interest becomes effective requires further clarification (see below).

Empirical relevance in the overall spectrum of investment strategies

We cannot say for certain what percentage of investment strategies with no connection to the real economy reference object there is among shareholders as a whole or in the movements on the stock market, especially considering that investment strategies in various markets differ widely and that this distribution can change over time. For this reason, we can only contribute a few comments here on the relevance of the category as a whole and the individual groups within it.

In an alternative typology proposed by McKinsey¹³ management consulting to specify which investors companies should seek dialogue with, this first category largely corresponds to the "mechanical investor" (Palter et al. 2008). The authors of the McKinsey typology estimate that this category accounts for around 32 percent of the total investment volume in the US and is therefore very relevant, but that it cannot be addressed in a meaningful way through investor relations. We do not know of any estimates of this kind for Germany.

Palter et al. (2008) do not explicitly mention *high-frequency traders* (HFT), and these are probably not counted in the category of "mechanical investors." We cannot determine with any certainty whether they are shareholders who "hold" certain shares: the speed of their buying and selling makes them impossible to register. As a result, there is at best vague data on the share of *trading turnover* on the exchanges. In the United States, these traders have been responsible for 70 percent of the daily stock exchange turnover for some time now, while European stock exchanges are catching up (DIE ZEIT, 12 May 2010). Reimann (2014) estimates that 20 to 25 percent of sales on Deutsche Börse originate from HFT. Other investors fear negative developments for their own trading activities, so they make evasive movements. These have been leading the stock market to become increasingly fragmented by the introduction of alternative platforms and "dark rooms." Reimann (2014) suspects that given these evasive movements, the peak of the phenomenon may already have been exceeded.

Index funds became available for the first time in the mid-1970s; long of middling importance, these funds have experienced considerable growth over the past ten years. According to Braun (2016: 9), the availability of new technologies for the "mass production" of listed exchange-traded funds (ETFs) has contributed to their rise since the year 2000. Such funds have now garnered 4.5 trillion dollars in the US (Buchter 2016: 4).¹⁴ Morningstar fund research has reported that 200 billion dollars were withdrawn from actively managed funds in 2015, while

12 A representative from the investor relations department explained in an interview that he was always responding from his own company to price fluctuations (appearing by surprise) for which there was no adequate reaction possible, only conjecture, because the trading activities were not attributable and the motives were not communicated. "But it brings volatility for us. And sometimes even the board asks why we're rising or falling right now, and then we say that hedge-fund activities are probably behind this too."

13 "Communicating with the Right Investors" is the title of the article in the McKinsey Quarterly (Palter et al. 2008). It advises listed companies on the matter of capital market communication: who does it pay to explain company strategy to, from the perspective of the listed company?

14 The available figures vary, and we cannot clarify the differences. Braun (2016: 13) presents figures for the development of the assets invested in ETFs worldwide. This number rose from under \$5 trillion in 2005 to nearly \$3 trillion in 2015. During this period, the number of funds grew from around 500 to around 4,500. The difference in Buchter's figures in terms of fixed assets may be that they also include non-listed index funds. In any case, the growth is impressive.

in the same period 400 billion dollars were invested in index funds (*ibid.*). Inflows into index funds are increasing in Europe and Germany as well. The banks and insurance companies that are mainly responsible for selling funds to the general public in Germany tend to sell their own active funds, because those commissions are higher, but recently private investors (often via direct banks) have also been snapping up index funds and ETFs with greater frequency (Mohr 2016). In Germany, the share of ETFs in mutual funds had risen to 12 percent by 2016 and has more than doubled since 2010 (Buchter 2016: 8). The global market for index products is dominated by three fund companies: BlackRock, which rose to prominence by purchasing iShares from Barclays Bank when it was struggling in the financial crisis; Vanguard; and State Street Global Advisors (Braun 2016: 9).¹⁵ Increasingly, however, other fund companies are also entering this area of operations. In Germany, these are the banking subsidiaries Comstage (a subsidiary of Commerzbank) and db x-trackers (a subsidiary of Deutsche Bank).

Regarding issuers, passive index funds may accumulate among those companies that are listed in several large indices. For example, according to Bloomberg (*Handelsblatt*, 3 Aug 2016, p.29) Deutsche Bank shares are held to a whopping 36 percentage by index funds, while the Daimler shareholder register still shows 25 percent.

The rise of index funds and ETFs is also generating a change in the competitive situation on the fund market. More specifically, the competition in the fund sector is not just about the yield that a certain portfolio can generate (which itself is not certain at the moment of the investment decision), but rather a mixed “calculation” of fixed, relative costs of the service of “asset management” and the presumed or anticipated (but uncertain in any case) return. Today’s index funds tend to find their customers among *institutional* investors, because these are apparently more likely to notice that index funds are substantially more cost-effective, as opposed to retail banking customers who fall prey to the blandishments of their financial advisors. Annual fees on index funds are often only 0.1 percent (Mohr 2016) or an average of 0.36 percent (Buchter 2016: 8),¹⁶ whereas a “classic” actively managed equity fund has fees of 1.5 percent (Mohr 2016) or up to 2 percent (Buchter 2016: 8) a year. According to a study conducted by Morningstar Germany, the fees of 10,800 actively managed funds actually rose above the 2 percent threshold from 2007 to 2011 (Röder 2014). Furthermore, index funds do not have any front-end load, whereas actively managed funds may have a significant mark-up of up to 5 percent (*ibid.*).¹⁷ Classic funds would first have to make up for this cost difference through their portfolio management just to be equally worthwhile for investors. From 2010 to 2015, only 28 percent of the equity funds invested in Germany beat the market or their benchmark index at all (Buchter 2016: 8). A Morningstar survey reported that costs and performance correlated negatively in all fund categories (Haker 2016).¹⁸ For today’s investors, the decision-making process is complicated by the fact that other funds and fund companies are still to be found among the “successful.” Nor does choosing last year’s most successful fund put investors on the safe side. To the contrary, it can be precisely the inflow of assets resulting from a success that undermines the success conditions so far, because the increase in monies invested does not provide any additional investment opportunities matching the previous selection criteria.

The pressure on the fund sector overall has risen since the financial crisis. Institutional investors are now increasingly withdrawing funds from actively managed funds and managing their assets themselves with cheap index funds; Germany’s Federal Financial Supervisory Authority (BaFin) has called for more fee transparency in funds (thus putting pressure on those who offer them), since mutual funds had previously earned the most money. The increasingly important online banking sector is competing with classic fund sales through (retail) financial advisors at branch banks, and consumer protection organizations are touting index funds as investments

15 In a ranking of the world’s largest asset managers, the top three companies are also the largest index fund providers: BlackRock with \$4.7 trillion, Vanguard with \$3.2 trillion, and State Street with \$2.5 trillion in assets under management (Frühauf 2016). The assets under management, however, do not all migrate into equities, which is relevant to our question. What’s more, we know that, at least for BlackRock, actively managed funds are included under the company’s umbrella alongside the predominant index funds. Of \$4.1 trillion of assets under management in 2013, \$2.1 trillion was invested in equity funds; equity exposures were also found in mixed funds, which amounted to an additional \$.3 trillion dollars (data from 30 Sept 2013, Economist 7 Dec 2013). According to company data requested by the author, around 80 percent of the equity exposure in 2011 was passive, with the rest active on the basis of fundamental analysis.

16 Referring to recent Bloomberg data, Braun (2016: 9) reports fees of only .03 percent for ETFs. The drop in fees triggered by index funds and special ETFs has led to a kind of ETF price war (*ibid.*).

17 In addition to the costs for analysis, communication with management, and sales, the securities trading resulting from active selection is itself costly and impacts the fund performance. Only investment bank brokerages are pleased by transaction-intensive funds (not least through the aforementioned HFT) and less so by passive index funds, which generate little turnover.

18 According to this study, 15.3% of the funds in the lowest cost quintile of the “Global Equity Large Cap” fund category beat the comparison index, while not a single fund in the highest cost quintile succeeded (0%). The odds of beating the index were higher overall for funds in other fund categories (Europe Equity Large Cap, Emerging Markets Equity), but costs were the most reliable indicator of fund performance for all categories (*ibid.*).

(Neumann/Kayl 2016). This is why lowering costs and cutting staff has become so popular in the fund industry (Handelsblatt, 31 Jan 2013).

As an interim conclusion, we can state that investment strategies without a connection to the real economy reference object comprise a significant and indeed growing portion of shareholders as a whole. These shareholders “act” while saying nothing of their motives against the respective company, thus exercising no influence, not even casually. The increase in competition among fund providers that has come with this development does not increase the pressure on companies to maximize shareholder value in the short term, as Windolf (2005a) would lead us to expect. Instead, the conditions for active influence on companies in each respective investment universe are also becoming less favorable for the investment strategies connected to the real economy reference object. Influence has a cost, and it takes experienced staff to understand companies “intrinsically” and communicate with managers and supervisory boards. Such costs must now be increasingly justified in relation to less expensive providers.

2.2 Investment strategies with a connection to the real economy reference object

Three different investment strategies operate in connection to the real economy reference object:

- *Active*¹⁹ investment strategies based on a “fundamental analysis” of the “intrinsic value” of the real economy reference object. This category has also been described more specifically, with some semantic shifts, as “intrinsic” (Palter et al., 2008); “essentialist” (Beunza/Stark 2004) and “dedicated” (Bushee 1998)²⁰. We use the “essentialist” term for this group (Beunza/Stark 2004).²¹
- *Event-driven short-term investment strategies*, which are described in Palter et al. (2008) as event-oriented “traders” or in Bushee (1998) as “transient institutions.”²²
- *Activist hedge funds* (see Fichtner 2009, 2015; Becht et al. 2014; Kahan/Rock 2007) seek to bring about a desired event by means of activism in selected companies (“targets”).²³

The overlap in all three of these subgroups is that the development and/or positioning of the company in the real economy is relevant to the investment decision. There are differences in the depth of understanding sought and the resulting necessity and mode of influence. Some promise “transient” returns (often only a “benchmark”

19 There are two meanings for “active” investors. One refers only to the fact that the investment object is actively selected on the basis of an analysis. This applies to all three of the investment strategies dealt with here. The other meaning refers to the type of connection to the real economy reference object: is it contacted, is it influenced, is the right to vote exercised? The term “engaged” has also been used for the latter meaning; the Anglo-Saxon investors we interviewed used “engagement” as a label for their approach. At the same time, they distanced themselves from “activism,” which they reserved to refer to that particular type of hedge fund. “Activism” does not refer to the fact that a stock (and the issuer) were actively selected, but that a certain change in corporate policy is to be firmly induced.

20 The “dedicated” category is much more narrow in Bushee (1998), however, and goes back to a distinction by Porter, who originally wanted to categorize the “patient” anchor investors found in German and Japanese companies. Bushee defines the groups according to formal criteria based on previous investment behavior. The “dedicated institutions” include funds with relatively large stakes, low turnover rates, and almost no sensitivity to current changes in earnings (ibid.: 326). Since in the US it is unlikely for institutional investors to acquire large shares in a company, the proportion of “dedicated institutions” in the Bushee sample is very low, at 4 percent.

21 Bushee (1998) is aware of the “quasi-indexers,” but we do not wish to define these in their own category: they are a mixture of passive, index-mimicking strategies and active, more event-oriented investment strategies, and often only end up more expensive than real index funds. Braun (2016: 10) calls this strategy “closet indexing” and sees it as a fraudulent response from the “active” fund industry to the challenge posed by index funds.

22 Kahan/Rock (2007) distinguish hedge funds from “traditional institutions” that include mutual funds and public pension funds. In their characterization of “traditional institutions,” they do not make the distinction we have between “transient” and “dedicated” institutions (Bushee 1998). According to this distinction, traditional institutions are generally more “incidental and ex-post” (Kahan/Rock 2007: 1022) in their actions. This is why we believe that distinctions of particular relevance to the relations between institutional investors and companies are being lost.

23 As a group that is defined as solely negative and specifically as unregulated, hedge funds are so heterogeneous as to be impossible to assign to one category in their entirety (Kahan/Rock 2007; Spindler/Schmidt 2008; Fichtner 2009). For this reason, only the activist hedge funds with a special connection to the real economy reference object are separately listed here. Some of the other hedge funds do not even have any exposure in the stock market, but rather in other investment classes. Hedge funds with equities exposure include both mechanical-quantitative funds and funds with a connection to the reference object; there are also those, however, that sell short and/or use various derivatives because of classic hedging motives. Unless hedge funds enter into strategic bets, announce them to the company and the general public, and exercise influence so that those bets can reach fruition (see Fichtner 2015; Becht et al. 2014), hedge funds are largely irrelevant as far as influence goes. Spindler/Schmidt (2008) consider only 4 percent of all hedge funds as activist, Kahan and Rock (2007) only 5 per cent.

advantage) from short-term buying and selling, and as a result their contacts with the company have, at best, the goal of securing the informational advantage hoped for. With these event-oriented strategies, influence is neither useful nor intended.²⁴ Investors with a long-term orientation, on the other hand, strive to discover an economic “essence” (Beunza/Stark 2004) that can unfold in their favor over the course of time.²⁵ Investors of this type analyze the real economy reference object longer and more thoroughly before adding it to their portfolio, which itself often contains larger individual stakes. This makes it more difficult to diversify risk, and the larger share packages can complicate a quick exit. Investors of this type communicate intensively with the management of the issuer, which is important even for the initial decision. The fund managers have an opinion on the company that is based on the original investment idea, which they also represent to the management. This is acted out more behind the scenes, however, rather than on the open stage of a shareholders’ meeting or at investor conferences.²⁶ If the company’s development has run contrary to assumptions and desires, and/or the original investment idea has been exhausted (for example, if a quality identified as undervalued has made up the difference), investors of this type tend to choose the exit option rather than initiate a campaign to change the corporate strategy.²⁷

Case studies: Investors with a long-term orientation and their dialogue with companies

There is a large fund company in the United States (KAGUS2)²⁸ that uses this type of investment strategy and owns a relatively large share of various listed companies in Germany. In our interview, their representatives explained that the analyst who is responsible for the industry in question and analyzes many similar companies from the sector will meet the respective company’s management in person in the run-up to a decision: “There will always be a dialogue before they’ve even invested in the company” (Interview KAGUS2).²⁹

In addition to the strategic issues and the attempt to gain an assessment of the “quality of management,”³⁰ the investment process also includes the so-called ESG issues (environmental, social, governance). The main consideration is to avoid risks to their own commitment.

“It has to do with the way that the research analysts will make their stock recommendations, so when they consider the financial performance and the management, the corporate governance structure, they will also consider whether there are environmental or social issues that could be risks for the company, or [whether] they could be opportunities: if this company has the right kind of business, it could benefit from those trends. So it’s just the way that the research group works; it’s thinking about everything rather than just thinking about the numbers” (Interview KAGUS2).

24 As an example of such strategies, Palter et al. (2008: 59) mention betting on whether a drug from a pharmaceutical manufacturer will pass or fail an authorization procedure. Barring unauthorized access to insider knowledge, such a strategy is highly speculative. But it is neutral with regard to the question of whether influence is possible. Event-oriented strategies, however, fundamentally ignore the idea of inducing events (especially externally) in the brief period in which these strategies operate, even if one assumes that the cause-and-effect relationship that induces events is adequately understood. This is precisely where these strategies deviate from activist hedge funds: they nurture the fiction that knowing how to achieve better results for shareholders is possible, and that these results can be brought about. Because the fiction entangles other shareholders to a relevant extent, the short-term price effect will regularly occur upon the mere announcement of hedge fund activism (Becht et al., 2014).

25 Beunza/Stark (2004) aptly correlate the category of “essentialists” to “value investors” who seek to identify undervalued companies in the market. Whether, to what extent, how often, and how reliably they can actually do this is not a matter of debate here. In general, it is becoming increasingly doubtful that active management can stably and reliably generate higher returns than those from passive exposures at all, especially if the costs of active management are taken into account. But even the unjustified belief in such an ability, or the presence of this belief among the gullible, has consequences for the questions that interest us: which shareholders influence the real economy reference object, how they do it, and what their targets and time horizons are.

26 The difference between the individual fund and the fund company is important in this context. Individual fund managers may be restricted to direct talks with IR and management, whereas representatives of the fund company can also speak publicly at general meetings and/or make use of the press.

27 Influence is still exerted, but in a more subtle way: if the fund management disagrees with the current management’s policy and communicates this, the management is aware that there is an exit option behind this divergent opinion, even if no threat is made. Since investors of this type often hold larger share packages, the potential price movements are also greater. Palter et al. (2008: 59) show that the “intrinsic” investors hold their shares for a relatively long time, often “several years”; if they buy or sell, it will be in larger packages, which can be the case at both entrance and exit.

28 „KAG“ is short for „Kapitalanlagegesellschaft“ and is the German term for investment company. “US”, “D” or “UK” indicates the country origin of the investment company quoted here from our interviews.

29 The interview took place in 2012 as a group interview in London. It involved members of the Europe team for the entire investment process, including the exercise of voting rights and the marketing division responsible for Germany.

30 On the difficult effort to determine the “quality of management,” see Faust/Bahn Müller (2007).

Considering ESG issues is not the same as offering an especially affluent segment of the public a special opportunity to invest according to certain moral standards, as occurs elsewhere through special sustainability funds (socially responsible investing, or SRI). Instead, it is a question of making a long-term equity investment economically successful by including in the “real economy” analysis a “calculation” that there may be social movements or political campaigns in contemporary societies that can do serious damage to the commercial success and accordingly the market value of companies whose business policies are declared to be “unsustainable” because they violate environmental or social standards. This does not depend on the moral impulse of the analysts or fund managers, nor their clients who expect such selection criteria from their fund managers. Rather, all that matters is that the decision-makers take into account moral motives and the social movements and/or political regulations that grow out of them; these can constrain a company’s opportunities for action or open up new opportunities for action that facilitate economic success (see also Walker 2015).³¹ “Reputation risks” can generate damage early on, for example when consumers react to environmental scandals or child labor in subcontractors by cutting back on purchases.³²

ESG issues are becoming more significant precisely because the actively managed funds tend to make more long-term commitments. Over these longer time frames, environmentally or socially questionable practices can turn into visible problems, “disasters waiting to happen”:

“There’s lots of examples. [...], the analysts would often go out to see the operations³³ and they’ll see for themselves if a company is running a shoddy operation. And there have been cases where they thought that it was a disaster waiting to happen and then the disaster did happen. It would [happen] in the next year or two. And these things might not happen straightaway, so if you’re a short-term investor you don’t care. You think: we need three days. Then you don’t pay attention to these things. But if you’re investing for three or five years then you have to think about everything that could happen” (Interview KAGUS2).

As the investment process continues, other members of the investment team will make direct contact with the company and its management, namely the fund managers in charge who have included the asset in their portfolio or would like to. Trust will be built with the company’s management. In the “dialogue” with management, which begins before the investment decision, expectations are increasingly communicated more or less implicitly. If during the course of the engagement it becomes clear that the company is developing in a different direction than anticipated or expected, the commitment will be “reevaluated.” Those in charge at KAGUS2 explained that it remains an open question at this point whether to try to influence management or to utilize the exit option (“walk away”). Influence is not their “first choice”:

“It happens, [...] it’s not our first choice. We’re not an activist fund manager, so we don’t buy shares in a company so we can try and change them.³⁴ But there are occasions where management will perhaps begin to do something, maybe related to merger and acquisition or in a structural activity, and it may be something that you think is not in the best interest of our clients. And that would be a situation where you think: okay, either we exit the investment or we try and perhaps influence management’s state of mind or do something differently. And now and again it will come to an evaluation, because if you think there is a lot of value in the company and it’s not being realized and it’s a bad time to sell shares – because, you know, you’d lose value – then you may try and influence management. So there have been cases, and it’s rare: it’s not something that happens every day. [...] But sometimes it’s more of a friendly call, where the company may be interested in the views of the investor. [...] they value the input from our research analysts, who obviously have been in the industry a long time. So it could be more of a dialogue rather than us just trying to put pressure on management” (Interview KAGUS2).

31 The fact that wider audiences in Western societies are increasingly evaluating commercial enterprises according to moral standards can also lead fund managers to make public announcements about their abiding consideration for ESG issues in the investment process. In this way, fund companies act in accordance with “rationalized expectations” (Meyer/Rowan 1977). In an interview with KAGD1, it became clear that the German fund company was facing higher expectation pressure to match others on this issue: “We are, of course, partially being pressured on this by the public, as the largest German asset manager, as an affiliate of [large German bank]. Of course this has a certain media appeal for critical groups, so we were on TV probably three times last year with land grabbing and cluster bombs. That’s why we’ve given it more gas than others who are not in this media bonfire” (KAGD1). Paradoxically, the non-moral, instrumental reasoning for considering ESG issues leads to what may be a more precise pursuit of these aspects because there is a conviction that doing so will influence the main measure of success, the fund performance.

32 We encountered this approach at various fund companies, both German and Anglo-Saxon. “ESG is now part of our investment process; we don’t have any special department” (KAGD1). Other fund companies from our sample also had explicitly “sustainable” funds in their fund universe, or others with a commitment to “socially responsible investing” (SRI). There are different selection and assessment approaches for this purpose (see Walker 2015). This segment is on the rise in terms of investment volumes, but it is still in a markedly minority position (Nessel 2012).

33 See also Faust et al. (2011a) on the value of site visits in analysts’ and fund managers’ assessments of a company.

34 This sets them apart from activist hedge funds (see below).

This type of relationship between company management and fund management is also confirmed by the other side, here by an IR manager who specifically addresses institutional investors with this type of long-term orientation:

“It’s actually a fruitful exchange, because you can have a great dialogue, especially with institutional investors, great feedback on what to do, how to position your strategy. You can utilize them as a sparring partner, you can use them as a mirror to discuss what you have done yourself in your corporate strategy, with people who know the entire industry all over the world [...] and fundamentally can just be of help to us in reflecting on our business model and looking at it again a little bit: is this standard for the industry, have we maybe overlooked something in the strategy, is a competitor maybe moving in a different direction. It’s a very pleasant exchange” (IRU2).

In this IR representative’s perception, the Norwegian sovereign wealth fund is another fund with a long-term orientation and is introduced as a countermodel to activist hedge funds.³⁵

“because they are quite interesting, because on the one hand they are not active either, in terms of being aggressively so, but they also want to look after their interests, to have an opinion and also be ready to express it on corporate stuff [...], always fairly, [...] [and they] also give the company a chance to react to it and don’t drive the company into something or other just to obtain a financial advantage, as an activist hedge fund would, but rather they really believe in the good cause” (IRU2).

The IR representative (IRU2) stated that even during periods of greater criticism, such as when the management wants to maintain its investments in innovation at the expense of possibly improving margins in the short-term, this type of investor understands: not only are these investors able to reconcile these decisions analytically, but they can also make them consistent with their own time horizons (for details see Kädler et al. 2017).

IR representatives have also confirmed that sustainability issues have become established in the investor dialogue, beyond the specialists.

“But a much more important trend is that mainstream investors are also asking about this, precisely because of the relevance in our industry of such strategic questions, like the environment. [Mainstream investors] are not wondering whether the resource consumption now is 3 percent higher or lower in a year; they’re asking as a matter of principle – and this is in conversations with management, as well – ‘have you ensured that your business model is future-proof? Can you ensure that you comply with future regulations, can you ensure that you meet future customer requirements and that you can go along with social change?’ What would happen if big cars were no longer in demand, were avoided just because customers no longer wanted them, didn’t want to be seen in them? And these are questions that have occupied an extremely large space” (IRU2).

The influence of “essentialists” is more dialogue-related and encompasses a longer time horizon, and therefore a broader range of topics as well. This dialogue is usually not public and is not accompanied by campaigns aimed at mobilizing followers and establishing pressure scenarios.

Activist hedge funds

But these actions are at the heart of the strategy of *activist hedge funds*, from which all the fund management companies we interviewed explicitly distanced themselves. Activist hedge funds take their engagement and announce it to the market, looking for allies in the process, and combine this engagement with specific demands brought forward through the campaign that target a skyrocketing increase in price and/or a special dividend. Whether they garner success or persistent failure, they continue on their search for new objects. According to Kahan/Rock (2007: 1022), the conduct of activist hedge funds is “directed at significant changes in individual companies (rather than small systemic changes), it entails higher costs, and it is strategic and ex-ante (rather than incidental and ex-post).”³⁶ Activist hedge funds have a connection to the real economy reference object and the field in which they are moving, insofar as that they have to determine promising opportunities and the conditions for success at them. A deeper understanding of the company’s capabilities and its strategy is not required. On the other hand, successful campaigns that lead to short-term success for the hedge fund through measures like special dividends can also undermine the medium- to long-term prospects for the company’s success. With this in mind, the main charge leveled against hedge fund activism is that investors of this type seek short-term returns

35 Regarding sovereign wealth funds as candidates for “patient capital” see Deeg/Hardie (2016).

36 Campaigns require time, especially when coalitions need to be forged. Fulfilling demands is usually dependent on formal requirements (shareholder meeting date) and/or on the conduct of other actors (takeovers). For this reason, the engagements can differ from those of short-term, event-oriented investors, since the desired event has yet to be induced and cannot simply be taken. Of the approximately 1,800 cases in the regions of the triad studied by Becht et al. (2014), the average hold duration is around one and a half years, with several years in individual cases (see also Fichtner 2015: 347).

that can come at the expense of the long-term profitability of the company as a whole and therefore also go against shareholders and/or other stakeholders with different strategies (Kahan/Rock 2007).³⁷ According to the relevant studies, activist strategies concentrate on a limited set of events to be achieved (Becht et al. 2014; Fichtner 2009, 2015):³⁸

- Refilling a position on the management board
- Payouts in the form of either a share buyback or a special dividend
- Restructuring, i.e., the spinoff of a non-core business unit or the prevention of a diversifying acquisition
- Takeover of the target company through a strategic or private-equity investor

Because the motives for them are discussed, the investment decisions of both “essentialists” and activist hedge funds result in price movements that are associated with potential learning effects for the company. Both of these groups can exert an influence, because for these investors, changes in the real economy are significant for their own success. However, as we have already shown, there is substantial variation in whether these changes are apprehended, what kind they are, and the relative intensity of their occurrence. For activist hedge funds with a limited arsenal of goals, pronounced influence in the form of a campaign is typical because their returns also depend on the fact that they are fighting against reluctance, so that the differences in valuation are more pronounced in the case of success. Similar to activist hedge funds, the proponents of event-oriented short-term strategies are focused on a limited spectrum of events in the real economy. Since they are only betting on the occurrence or nonoccurrence of such events, however, they remain in passing; influence is not part of their strategy.

Empirical relevance of investment strategies with a connection to the real economy reference object

Here, too, quantitative assessments are difficult, and we limit ourselves to a few indications when estimating the relevance of the category and its subgroups. Palter et al. (2008) estimate that 35 percent of all investors belong to the type of the short-term, event-oriented trader, while “intrinsic” investors (“essentialists”), upon whom communications from management should concentrate, comprise about 20 percent. We are not aware of any comparable estimates for Germany.

After BlackRock, which is predominantly invested through index funds, the financial investors identified by Faust/Thamm (2015) that belong to the ten most frequently represented fund companies with commitments of over 3 percent among the 160 DAX companies are generally fund companies with a declared preference for active management. The Capital Group (fourth place), which has twenty often larger stakes, fits firmly into the pattern described.

The Capital Group portfolio for 2010 identified by Faust et al. (2011b: 8) contains 17 stakes above the reporting threshold. The spectrum ranges from 3 to 10 percent, with three stakes at the 10 percent threshold and ten more over the 5 percent threshold. This strong concentration of holdings already speaks for a fundamentally reasoned selection of securities, but also for a more long-term commitment, since with such high equity values a rapid exit is not possible without damages, especially since these are often not particularly liquid values from small or mid cap issuers.

37 “Hedge funds harm universal owners” (Stout 2012: 92), or at least the activist ones, because they are the exact opposite of the “universal investor.” They are not diversified. The manager of such a hedge fund “comes as close as any living entity can to the Platonic ideal of the undiversified shareholder who cares only about the price of a single company equity” (ibid.).

38 Fichtner identifies a more limited set of targets for activist hedge funds in Germany. Both the “refilling supervisory board positions” and the “takeover” objectives are missing. Both objectives are also more unlikely to be achieved in the face of the structural and institutional restrictions in Germany, such that the announcement of such an objective could end up mobilizing little support. Special cases such as the Deutsche Börse cannot be ruled out, however.

Table 1: The 10 largest financial investors and their stakes in the 160 DAX companies at the end of 2014

Financial investor:	Number of stakes
BlackRock	47
Allianz Global Investors	22
Staat Norwegen	21
Capital Group	20
Deutsche Asset & Wealth Management	17
Fidelity	16
Franklin Templeton Investments	15
Sun Life Financial	12
BNP Paribas	7
Threadneedle	6

Source: SOFI survey 2014, Faust/Thamm 2015: 71–72.

Figures from the Capital Group put the average hold time for the shares at around two years. These figures tend to be supported by the minimum retention periods (ibid.) that have been reconstructed from Germany's company register (unternehmensregister.de), which tracks reporting history going back to 2007 pursuant to section 21 of the German Securities Trading Act (WpHG).³⁹

Table 2: Significant stakes in listed companies in Germany (above the 3 percent threshold) held by Capital Group in 2010

	DAX 30		MDAX and TecDAX	
Capital Group	Adidas AG	5.01	Continental AG	5.14
	Bayer AG	10.02	Fraport AG	5.08
	Beiersdorf AG	5.02	FuchsPetrolub AG Vz	3.00
	Commerzbank AG	5.04	Heidelberger Druckm. AG	3.14
	Deutsche Börse AG	3.03	MTU AG	7.71
	K+S AG	5.20	Symrise AG	5.27
	Linde AG	9.93	WINCOR NIXDORF AG	5.01
	Merck KGaA	9.79	Pfeiffer Vacuum Technology	5.87
	SAP AG	3.19		

Source: Faust et al. 2011b: 8

Overrated hedge fund activism?

The significance of hedge fund activism in Germany is not easy to estimate. The total assets managed by hedge funds are not a good indicator, since even the equity exposures of hedge funds are by no means all activist in nature. Offsetting this, however, is that hedge funds can leverage their targeted exposures with debt.

³⁹ It is not possible to calculate exact hold durations from this because the values before 2007 cannot be considered. In addition, stocks newly incorporated into the respective portfolio, with their inevitably short hold duration, push the average result downwards.

Nevertheless, the following comparison gives an idea of the magnitudes: BlackRock, whose exposure is mainly in index funds, with a lesser portion in actively managed funds, was managing more assets worldwide (\$4.7 trillion) at the end of 2014 than the entire hedge fund sector (\$3 trillion) (Braun 2016: 7).⁴⁰

We can approximate the scale of hedge fund activism by the number of interventions, which is more in line with the character of the non-diversified investor (Stout 2012: 92). We can ascertain cases of intervention because they leave media traces. Quantitative studies, which are primarily interested in the short-term financial effects of activism for shareholders (e.g., Becht et al. 2010, 2014), tend to overestimate the number of cases because they have to rely on simple indicators for practical, research-related reasons. We can see this in Fichtner's study, with its support from qualitative case studies (2015: 343). Of the 170 listed companies he included for the period from 1999 to 2010, Fichtner was able to identify only eleven cases for Germany in which one of these companies became the target of activist hedge funds. This is far less than the 41 cases for Germany identified in Becht et al. (2010).

The most empirically comprehensive study is from Becht et al. (2014). They identified a total of 1,796 activist interventions in North America, Europe, and the Asian region (mainly Japan) in the period from 2000 to 2010. Their investigation makes it possible to distinguish between activist interventions that achieve the desired and publicly disclosed result (such as takeovers or payouts) and those that fail during the holding period. Overall, only about half of all interventions achieved at least one of their desired outcomes; only these are associated with financial success for hedge funds as well.

The level of hedge fund activism varies considerably between regions and countries. Of the approximately 1,800 cases in the study, 1,166 occurred in the United States, 186 in Japan, and 168 in the UK, with these three countries covering 85 percent of all interventions. Germany accounted for only 55 cases in the total period, which is 3.06 percent.⁴¹ At any rate, hedge fund activism is not as relevant to the overall picture in Germany as the few spectacular cases (such as Deutsche Börse) would suggest. Braun (2016) rightly criticizes the fact that "alternative investment companies," in which hedge funds are included, have attracted the lion's share of the attention of economic sociologists and political economists, whereas the "ordinary" investment funds that manage a plurality of assets have not seen further scrutiny, perhaps because they do not seem as scandalous as the hedge funds or private equity funds that former SPD party chair Franz Müntefering famously referred to as "locusts" in 2005.

The extent of hedge fund activism depends on the rules of corporate governance, which concern the rights of shareholders at the annual shareholders' meeting or the rights of the shareholders' meeting as far as they affect the supervisory board or the management board. It also depends on the actual distribution of power due to the shareholder structure and on cognitive-cultural factors that go beyond the legal rules determining what constitutes appropriate pursuit of interest (see also Becht et al. 2014: 25-26). All three factors are likely a part of the explanation for the low level of hedge fund activism in Germany, without being able to say for certain how much weight each of them has. We can estimate the significance of the structural factors better. Companies with an anchor investor acting as "patient capital" (Culpepper 2005) are largely excluded as a target for activist hedge funds (Fichtner 2009, 2015; Faust/Thamm 2015). An institutional threshold is important here. "According to the German Stock Corporation Act, the control threshold of 25 percent is of decisive importance in order to be able to exert a significant influence on decisions at the shareholders' meeting" (Achleitner et al. 2011: 20). This is why we can also speak of a blocking minority.⁴² This blocking minority can be positioned not only against hedge fund activism, but also represents an important protection against hostile takeover attempts (Höpner 2003; Höpner/Jackson 2001; Jenkinson/Ljungqvist 2001; Fichtner 2009); this structural hurdle for hedge fund activism continues to be very high in Germany. As of 2014, 58.1 per cent of all 160 DAX companies still had a de jure investor with more than 25 percent of the voting rights according to share ownership.⁴³

40 For these reasons, hedge fund activism also tends to be directed against smaller and medium-sized listed companies, where larger shares can be acquired more easily with less effort (see also Fichtner 2015).

41 Information is not available for how many of the 55 interventions in Germany were successful, so we also do not know whether the success conditions in Germany are better or worse than the average for all cases (about 50 percent).

42 "Under German stock corporation law [AktG], several important decisions at the shareholders' meeting require a qualified voting majority of 75 percent, e.g., the extraordinary dismissal of a member of the supervisory board (§ 103 AktG), amendments to the articles of association (§ 179 AktG), capital increases (§§ 182, 193 AktG), and the dissolution of the company (§ 262 AktG). Because of this provision in the stock corporation law, a shareholder with at least 25 percent of the voting rights can block such decisions. This is why the control threshold of 25 percent of the voting rights is referred to as a blocking minority. This gives a shareholder a large de facto influence over the aforementioned decisions at the shareholders' meeting" (Achleitner et al. 2011: 20; see also Jenkinson/Ljungqvist 2001).

43 The proportion of listed companies with an anchor investor was significantly higher in the 1990s, at over 85 percent (depending on the study and sample, with certain variations). Clearly, a financialization of the corporate landscape has taken place in Germany since

The experts we surveyed were familiar with the fact that anchoring investors often slow down hedge fund activism before the majority can even play a role at shareholders' meetings.

“Obviously there are private equity and hedge funds in particular that don't dare to address such firms because they say, ‘no, I can't exert influence when I go there and make a lot of noise and say, ‘you have to finally do something different,’” and then they [the funds] get received by the management board and they [the board] say ‘yes, yes, it's very nice you came,’ you get a friendly ear there, but they know you can't really change anything. Sometimes it really is good if firms have a blockholder, because then they have a highly interested shareholder who takes care that things are going well” (Interview with (multiple) member of supervisory boards, capital side).

An *actual* blocking minority can also be achieved in the case of dwindling or low attendance at shareholder meetings (Fichtner 2009; Spindler 2006; Faust/Thamm 2015),⁴⁴ or if share values have already dropped. Two developments have been brought to bear in explaining declining attendance at shareholder meetings (Spindler 2006): (1) The decreasing attractiveness of voting rights for the depositary banks, which on the one hand has to do with the withdrawal of the major German banks from the obligations of “Deutschland AG”⁴⁵ and on the other hand with the fact that depositary management⁴⁶ has become costly and generates income for the banks from its fees. (2) The internationalization of the shareholder structure means that foreign fund companies in particular, having assessed the costs of exercising their opportunities for influence (including the alienation caused by the unfamiliar institutional circumstances), do not exercise their voting rights. Many foreign investors also fear that registering their voting rights for the shareholder meeting will deprive them of the ability to use these shares for trading during this time. The pronounced restraint in the exercise of voting rights points to the current attitude of “rational apathy” (cf. also Kahan/Rock 2007; Black 1998), according to which, after weighing the costs of an “informed” exercise of voting rights or other influence against the possible “income” from influence, in the face of the free-rider problem (other funds also benefit, even if they themselves remain passive), it is rational to abstain from voting or to exercise influence in some other way. If registering the stock in order to exercise their voting rights threatens to constrain their alternative method of exerting influence (i.e., choosing the exit option) when they are dissatisfied with the development of the real economy reference object, evidently many funds are reaching their own conclusion to refrain from casting an uninformed, *pro forma* vote.

Low attendance at shareholders' meetings has implications for how the blocking minority is determined. Taking into account the actual attendance at shareholders' meetings held in 2014, the proportion of companies with *de facto* anchor investors was 71.3 percent, compared to the *de jure* 58.1 percent (see also Fichtner 2009 for an earlier study). Accounting for a *de facto* blocking minority on the one hand confirms that hedge fund

then. The proportion declined in the years that followed and leveled off again in 2014 at 58.1 percent, slightly higher than the previous low (Faust/Thamm 2016: 25; see also Fichtner 2015). Compared to internationally, however, Germany still has a high degree of concentration of share ownership. At any rate, it is a long way away from the structural norm of “financial market capitalism,” in which companies have a large float with high institutional ownership.

44 According to Spindler (2006), attendance at shareholders' meetings of DAX30 companies fell by 15 percentage points between 1998 and 2005, to an average of 45.87 percent. Companies with strong anchor investors, such as BMW for example, see markedly above-average attendance at their shareholders' meetings because of the guaranteed presence of the voting rights of the anchor investors; companies with a large float and institutional ownership see markedly below-average attendance. Attendance at shareholder meetings of Allianz AG, for example, decreased from 70 percent to 35 percent between 1998 and 2005. Adidas had only 25 percent attendance in 2005. Attendance at shareholders' meetings has recovered somewhat since then, and in 2015 was around 55 percent for the DAX30 (Deutsche Schutzvereinigung für Wertpapierbesitz (DSW); <http://www.sdk.org/assets/Statistiken/HIV-Praesenzen/paesenzen-dax15.pdf>, 26 July 2016). The fact remains, however, that companies with a large float have considerably worse attendance rates than companies with anchor investors (Faust/Thamm 2015: 59). A member of the supervisory board from the company U4 reported that the remaining family share of 6 percent in the largely free-float company represented a *de facto* voting share of 16 percent.

45 The possibilities of proxy voting are generally overestimated. This was already true for the exercise of depositary voting rights by the German banks during the period of organized capitalism, or is at least the conclusion reached by Elsas and Krahn (2004: 227) in their retrospective assessment of the German house bank system: “Finally, contrary to the common presumption in the literature, the available evidence does not suggest that banks use proxy-voting rights in a systematic way to influence management decisions.” The reasons they invoke are still valid today: “This might be due to the fact that the exercise of proxy-voting rights is complex because of inherent free-rider and coordination problems” (ibid.).

46 Funds must hold their investment monies in safekeeping as fund assets at a depositary bank. Depositary banks are paid for this service; there is cost competition for it, so loyalty to parent companies (e.g., among the bank-dependent fund managers) no longer plays a role. KAGD1, the asset management of one of the largest German banks, which formerly formed the core of Deutschland AG, does not use its parent company as a depositary bank at all anymore. Instead, it uses a US company that evidently offers more favorable conditions (Interview KAGD1). The exercise of voting rights is another cost for the depositary banks and must be reimbursed by the fund companies. We know from our interviews with managers of fund companies (KAGD1) and voting-rights intermediaries (PAD1) that depositary banks require additional fees for this service. In the increasingly cost-driven competition between funds and fund companies (see above), this too suggests “rational apathy” in the exercise of voting rights.

activism in Germany is facing significant barriers, since now well over 70 percent of DAX companies (DAX30, MDAX, SDAX, TecDAX) exhibit ownership constellations that tend toward the unfavorable. On the other hand, when we also consider attendance at shareholders' meetings, we see that activist hedge fund that invest in companies whose free-float shares are held by institutional investors are able to acquire larger voting packages relatively quickly; such funds usually concentrate their resources on a small number of target companies, often pile on to these as a pack, and can leverage their own funds by loans (Kahan/Rock 2007; Fichtner 2015). In the five cases investigated by Fichtner (2015), the activist hedge funds achieved a maximum vote of 20 percent (CEWE-Color) or 25 percent (IWKA/KUKA). The most prominent case of a successful intervention by hedge funds in Germany, the Deutsche Börse Group, was made possible by the fact that once its anchor investors (the German banks) had pulled out, Deutsche Börse's free float was held by institutional investors, and the high percentage of foreign investors engendered very low attendance at shareholders' meetings. The case was also characterized by other funds joining the initiators from the activist hedge fund camp. In the end, the group, which voted against the London Stock Exchange's takeover of Deutsche Börse and instead demanded a payout, garnered 35 percent of the votes (Kahan/Rock 2007: 1034-36). The case of Deutsche Börse stimulated a discussion about the avoidance of "random majorities" (Spindler 2006).

More recently, the large DAX companies where foreign institutions hold much of the free-float shares have seen improved attendance at shareholders' meetings once again. One reason for this is that fears that the shares would not be tradable during the registration process have been overcome; another is that apparently more and more fund companies are using the services of professional voting advisors or brokers, who help to reduce the costs for these activities (Handelsblatt 1/2/3 July 2016, p. 14). However, the utilization of intermediaries conceals a broad range of different uses: a fund may hire them for analysis and voting recommendations with these external service providers supplying only information, or the entire process may be passively delegated to them, according to their guidelines and recommendations (interviews with PAD1, PAD2, PAUS1).⁴⁷ Whereas some of those in IR we interviewed (IRU1) feared a strong standardization and homogenization of the voting rights according to the specifications of the US service providers (who can no longer be influenced by the fund company's own arguments), German voting rights intermediaries who work according to the BVI guidelines can assert their legal right to contribute to a vote that is better suited to the German situation. The German representative of the US proxy advisor (PAUS1), on the other hand, emphasized that the US service provider took the German conditions into account in his voting rights recommendations and often also used other guidelines supplied by clients upon request. The representative also noted that many clients exercised their voting rights independently and merely took note of the intermediary's recommendations.

2.3 Investment strategy as strategic control or decisive influence

Finally, we define a third type of investment strategy, which we call "strategic control." Although this equity investment is connected to the real economy reference object (as in the second type), it differs from *both* of the previous ones. This type does not place a priority on the targeted return from an investment that is to be generated from equity exposure (in different ways for each, depending on the underlying theory). Regardless of whether the investment strategy in the other two types is connected to the real economy reference object, the goal in those cases is the yield from the *financial* investment. The third type has strategic control as its primary goal, with its reference as the strategic value of the company for the shareholder. To be clear, the financial yield is not unimportant. But it is linked to a strategic alliance with a company whose shares are held in such great numbers that it is possible to exercise either control or at least influence that is sufficiently decisive to fend off other control claims. Shares of such proportions cannot even be sold on the stock market without triggering downward price movements, which constrains opportunistic behavior. Strategic stakes can also be reevaluated by their respective owners, of course, and are not for eternity. Nevertheless, equity investments of this type differ fundamentally from those of prototypical shareholders, who reduce the risk of equity investment precisely because they distribute the assets intended for this form of investment into smaller shares with as much liquidity as possible, across various companies, which allows them to choose the exit option at any time. This manifests in the Anglo-Saxon model of a company with free-float shares. Historically, strategic control has been linked more to other forms of incorporation than to publicly traded stock corporations. In Germany and other

47 PA stands for Proxy Advisor; BVI is the abbreviation for the German Investment Companies Association.

continental European countries, a different use of the listed company had previously prevailed, one in which ownership was much more concentrated (Höpner 2003; Beyer 1998, 1999).

But even anchor investors in stock corporations can only exercise a form of control in the restrictions of the legal form of the stock corporation. The stock corporation is pluralistic in constitution and is not conceived to be a mere tool of its owners. Its management board and supervisory board are bound by the “best interests of the company,” which not only must take the interests of the shareholders into account, but also consider those of other stakeholders.⁴⁸ Above all, the “best interests of the company” are geared toward the sustained continuation and prosperity of the company, which is seen as a legal entity and a functional economic unit (not just a “legal fiction” of a set of contingent contracting relationships, as agency theory suggests). This also binds individual groups of owners to the large mass of other shareholders, although the former are entitled to special rights (such as seats on the supervisory board) by virtue of their share packages. For our context, it is sufficient to establish that the approximate legal provisions of the stock corporation determine how (bodies and responsibilities) and by which thresholds (voting rights, majorities) decisions are made. As already mentioned above, the 25 percent blocking minority defines an important threshold for influence and control. It is in any case decisive for fending off others’ control claims, even if the anchor investor otherwise has little influence on company policy (in mind). At sparsely attended shareholder meetings, blocking minorities can even become effective at a de facto threshold below 25 percent; as stated above, they make hedge fund activism largely ineffective and can fend off attempts at hostile takeovers and thus prevent the emergence of a market for corporate control. The extent to which anchor investors actually influence company policy, however, depends not only on the size of the share package but also on the entrepreneurial ambitions of the respective generation or management group of the anchor investor, and can only be analyzed on an ad hoc basis. Thus it often happens in publicly traded family companies that the families or founders not only have a blocking minority, but that family members also occupy positions on the supervisory board and/or management board (Achleitner et al. 2011; see also Faust/Thamm 2015, 2016). However, the members of the owner family can also choose to define their function more as guardians of the company’s independent development (which is the responsibility of the board of executive directors (“Vorstand”)), without developing their own entrepreneurial ambitions.⁴⁹

Regardless of the actual influence in each individual case,⁵⁰ two determinations are of paramount importance if we are to analyze the constellations of external influence here: On the one hand, anchor investors establish an influence that is at least decisive for fending off control claims by others that (may) disadvantage the company as a whole. It must be assumed in this case, however, that the anchor investor has sufficient stability in its own decision-making process. This cannot be taken for granted; from an empirical point of view, a large percentage of anchor investors in Germany are families and founders (and their families). The stability of the family as a social context and thus also as an anchor for companies has been an open question for a long time (the Buddenbrooks effect), especially in times of eroding family ties. Current reports on the sometimes paralyzing family disputes at companies like Aldi and Oetker have drawn attention to this phenomenon. So far there has been no research into whether the often tacitly implied stability of branched family ownership is undermined when attractive alternative investments are available on the capital market or when the family company is classified as a “cluster risk.”⁵¹

On the other hand, anchor investors are developing an interest in maintaining and growing the functional and social coherence of the company and rather than the short-term and opportunistic exploitation of returns.

48 The German Corporate Governance Code (DCGK) also commits the management board to act in the “best interests of the company” while considering the “needs” of various stakeholders in a “sustainable” approach; no reference to “shareholder primacy” is made (see Stout 2012 for a discussion of the US jurisdiction). The reference to the interests of the company (which is based on the concept of the company as a legal personality) and to the plurality of legal claims to be considered is already anchored in the German Stock Corporation Act (Schmidt/Tyrell 2004: 51; Rieckers/Spindler 2004; Faust 2013), but it is set out more clearly in the DCGK: “The Management Board assumes full responsibility for managing the company in the best interests of the company, meaning that it considers the needs of the shareholders, the employees and other stakeholders, with the objective of sustainable value creation” (DCGK, Convenience Translation, 7 Feb 2017; <http://www.dcgk.de/en/code.html>).

49 See the example of the municipal shareholders in RWE AG, who present themselves as custodians of public services and a barrier against hostile takeover attempts (see Faust/Thamm 2015: 59).

50 In the range of cases included in our study, when family members occupied positions on the supervisory board there was a distinctly entrepreneurial understanding of how duties were to be fulfilled, despite a clear separation of responsibilities (as required by law) between the management board and the supervisory board.

51 Our corporate case studies have given us insight into the ways in which entrepreneurial families, sometimes with many branches, can be “organized” to counteract centrifugal forces and facilitate the long-term cohesion of the family as an economic unit. This is a research topic in itself and merits further study.

Ways this is currently being expressed include greater patience for innovation projects (see Kädtler et al. 2017). Such anchor investors consequently qualify as potential alliance partners for other stakeholders who also have longer-term commitments to the respective company, specifically the core workforce and their representatives, but also strategic partners among suppliers and customers.

We have indications from all companies in the case spectrum with an anchor investor of a (possible) emergence of a special constellation in the triangle of anchor investors, management, and employee representatives. It is by no means self-evident that entrepreneurial families are involved with representing others' best interests, particularly those of union members. A historical perspective certainly does not portray family owners as having a natural affinity for co-determination, especially the quasi-equal representation of employee interests in the running of a company. Indeed, the German associations of family entrepreneurs and prominent entrepreneurial families were precisely the ones to complain about the Codetermination Act (Mitbestimmungsgesetz) of 1976. Those with pronounced opposition to codetermination today are specifically found among family-owned companies without publicly traded stock. Historically, therefore, attempts by entrepreneurial families to bond core employees have more widely manifested in the form of entrepreneurial paternalism, which was also always directed against trade union influence. Thus it was the political and legal implementation of codetermination which first established the official arenas for the negotiation of interests and endowed workers' representatives with rights; years of conflict, negotiations and settlements in these arenas facilitated learning processes on both sides as a result. Within this framework, constellations of cooperative conflict processing have become established in listed companies that have families as anchor investors. The family representatives in this three-party constellation (usually in the role of supervisory board members) supplement the cooperative conflict relationship between management and employee representatives (Müller-Jentsch).⁵² In conflicts between management and works councils, whose key representatives are often also members of the supervisory board, employee representatives have the opportunity to engage the owner family in an informal manner.⁵³ "If there are true hard feelings, or something strategic is going on," the key employee representative meets with the representatives of the owner family directly, according to representatives of one of our case study companies (U2).⁵⁴ Unlike in publicly held companies, these owners have a face and a voice and are approachable. In many cases, the family representatives and key employee representatives have been members of the supervisory board the longest – often much longer than most managers – so there is also a chance to forge personal trust. Under these conditions, the owner family representatives develop a lasting interest in these relations: to hear from the employee representatives (who acquire very special "insider knowledge" through their formal and informal information channels) about any grievances or undesirable developments in the company that the family would not have heard from management, or at least would not have heard so soon.

"And the sustainability issue is already playing an important role. But I am not alone in this, and that's also a point that's especially well and good to discuss with the works council or with the trade unions; they can play a great and active part in it, and I believe we have good conditions in this respect. [Company U4] traditionally always had good people in the works council [...]. You know, the worst thing that can happen to you in the industry is when you have a bad works council. I mean, the works council is a given, and employees are the most important capital that we have, so we have to treat them well. And the works council helps us do that. The times have completely changed, so this is what it's like in the German industry; it may be different elsewhere, but we aren't experiencing ideological conflicts anymore" (Supervisory board member on the capital side, U4).

52 We found such constellations (in variation) in our case companies with an anchor investor. How prevalent they are otherwise is unknown.

53 The formal arenas of corporate codetermination found on the supervisory board, its committees, or its steering committee here represent only the official framework for models of trusting relationships to emerge that go beyond the formal roles: you have your counterpart's phone number, and your call is put through.

54 "Look, we're always talking about anchor investors – at [U4], the family is the biggest investor and the family has one thing in common with the works council for sure: we want to preserve the company. The works council first of all [wants] to preserve jobs and [our] jobs and the share price and who knows what. But there's no contradiction in that" (ARU4). We take this statement as proof of an orientation that keeps more options in play. Whether and how this orientation will be effective in the branched conflict situation at the company is another matter. In specific company decisions, there continue to be conflicts between the various objectives, for example when choosing a location. In such cases, the conflicts are often defused through agreements, in order to handle unavoidable downsizing without layoffs. This interviewee asserted that he was involved in a conflict between management and the works council over a plant shutdown by the works council, and that he had advocated to the management for a reexamination of alternative concepts drafted by the works council, which led to a revision of the original decision.

This three-party constellation of cooperative conflict management (management-employee representatives-anchor investors) appears as an idiosyncratic melange of rights-based codetermination, paternalistic attitudes, and company loyalty.

Empirical distribution of the constellation in Germany

The usual candidates for anchor investment are other nonfinancial companies and related companies from the same sector, and/or company founders or entrepreneurial families, with the latter group also appearing in the guise of foundations. Since the withdrawal of the major German banks and the Allianz insurance company from the proverbial “Deutschland AG”,⁵⁵ banks and insurance companies have only materialized as anchor investors when they hold shares from affiliated companies from the same or neighboring sector(s) which is a rare incident nowadays (Faust/Thamm 2015). In some cases, the federal state, the “Länder” or regional municipalities will be the anchor investor, even if these shares do not necessarily exceed the 25 percent threshold and represent only de facto anchor investors. This applies not only to the well-known example of Lower Saxony’s stake in Volkswagen AG, but also to the municipal shareholders in RWE AG, a large utilities company, and the Thuringian holding company in Jenoptik AG. Companies from abroad are also anchor investors; for example, a Spanish construction company is the main shareholder of Hochtief AG. Likewise Qatar Holding’s stakes in Volkswagen AG (17 percent), Hochtief AG (10 percent) and Solarworld AG (just under 50 percent) are probably strategic in nature, even if not all of them exceed the threshold for a blocking minority.⁵⁶

The data on how anchor investors as a whole (as measured by the 25 percent threshold) break down into different categories of investors is somewhat contradictory, since there is no uniform use of categories and the sample sizes of the respective studies differ (see Achleitner et al. 2011; Fichtner 2009; Faust/Thamm 2015). Taken together, however, these analyses show that we are dealing with two different types of listed companies with anchor investors. Family companies, which often combine voting rights with active control or participation in the management of the company, represent a significant portion of these companies with “patient capital,” but not all of them. Also included are other “strategic investors” (equivalent to other industrial companies) and “nonfamily insider ownership” (Achleitner et al. 2011: 54).

Regardless of the necessary examination of motives for engagement in individual cases, we can determine the prevalence of anchor investors by identifying the number of companies in which the relevant thresholds of 25, 50, or 75 percent of voting shares are being exceeded. We conducted this test with data from 2014 for the 160 companies of the DAX (DAX30, MDAX, SDAX and TecxDAX) (Faust/Thamm 2015). We are not covering all listed companies by any means. But all known studies based on larger samples of listed companies seek out higher levels of concentration in share ownership, for example in the CDAX (see, e.g., Achleitner et al. 2011 or Jenkinson/Ljungqvist 2001; for an overview see Faust/Thamm 2015), so our data can be regarded as a more cautious estimate of the prevalence of this constellation. According to these figures, 58.1 percent of listed companies have an anchor investor defined by a blocking minority of 25 percent, 33.1 percent have a majority shareholder (more than 50 percent of votes) and 8.1 percent have a super majority (75 percent of voting rights). As has already been shown, the concentration of share ownership in Germany by this measurement has significantly decreased since the 1990s, but it is still very high compared to internationally. Furthermore, the study by Achleitner et al. (2011) shows that a large part of the financialization of the corporate landscape, as measured by the growth in listed companies since the 1990s, was the result of founders and families who wanted their company to be listed – not to withdraw themselves as private business owners, but to continue the company with additional equity without giving up control, i.e., with at least a blocking minority. In fact, family companies again disproportionately withdrew from public trading in the years directly following the stock market crash at the turn of the millennium; these companies (presumably including those with broken or more than dubious promises) could not build a viable business model. Nevertheless, the overall movement resulted in a sustained, substantial increase in the number of family enterprises among the CDAX companies even after the end of the stock market boom in the 1990s (see Achleitner et al. 2011: 38; Faust/Thamm 2015: 74–81). The development,

55 Even during the Deutschland AG era, which was empirically linked to the capital crossholdings within the circle of the hundred largest companies according to the data of the Monopoly Commission, many stakes held by banks and insurance companies were below the threshold for a blocking minority, meaning that they were not anchor investors according to this definition (Höpner 2003; Faust/Thamm 2015).

56 The stakes held by sovereign wealth funds from the Arabian Peninsula are often dubious cases, where it is not always possible to say for certain whether the stake is purely financial or strategic, or merely the hobby of a bored sheikh investing for sport (Formula 1).

which from one perspective can be seen as the financialization of the corporate landscape in Germany because the share of listed companies increased sharply during a defined period (1990 to 2000), from another perspective seems to indicate the proliferation of family companies on the capital market: “financialization” and “familialization” as parallel aspects of an evolution.

3. Heterogeneity and integration at the level of the fund company

In this third section, we relinquish a fiction from the second section: that each individually standardized investment strategy defines one capable actor in particular. Investment strategies are best defined at the level of an individual fund and therefore also securely determined for external observers. We previously introduced the index fund example as an investment strategy that does fine without a connection to the real economy reference object because only the index is selected, rather than any individual company. But index funds may be part of a complex investment company’s larger fund universe, one which includes equity funds with passive as well as active investment strategies, as well as fixed-income funds with bonds from the same companies that are also represented as issuers of shares. The simultaneous effectiveness of the equity perspective (stocks), which seeks uncertain returns from share price development and dividend yields, and the debt perspective (bonds), which seeks contractually fixed interest payments and as certain a repayment of the borrowed capital as possible, suggests a broad spectrum of potential definitions of interests. What’s more, fund companies’ interactions with the issuing company are often not only as fiduciary representatives for the interests of their investors, but as current or potential clients of the issuer at the same time: the issuer will use the fund company to invest the issuers’ own assets or pension provisions. In addition, conflicts of interest may enter into play with the parent company of an asset management company, the former of which, as a bank, will have its own business relations with the listed company in question. This poses the question of whether the different interest definitions and the strategies of pursuing those interests are unified within the investment company, as may be the case, and what consequences this has for the various levels of the pursuit of interests.

3.1 Do conflicts of interest resulting from organizational embeddedness modify influence?

We begin with possible conflicts of interest that may arise from the fund company acting as a fiduciary representative for shareholder interests in interactions with an issuer and in other business relationships, when the parent company of the fund company is seeking or already maintains such a relationship with that very issuer. Typically, this affects fund companies that belong to a bank which, in turn, provides support with bond placements and/or M&A activities, supplies loans, or sits on the supervisory board of the same company that the fund company is meant to be monitoring (Kahan/Rock 2007: 1054-56).⁵⁷ The German legal situation is clear: the respective fund or investment company has a responsibility to execute its fiduciary duty to observe the interests of the actual investors in the fund. The fund does this at its own discretion, unless otherwise instructed; it is supposed to avoid conflicts of interest and, should they occur, to disclose them and mitigate their effects.⁵⁸ Fiduciary representation at the institutional level comes with only a basic definition of interests, which are to be observed at the fund’s own discretion, but it is framed and specified by established standards of corporate governance (in Germany, for example, these are enshrined in the Corporate Governance Code). How these rules are applied and made effective, however, is decided in concrete situations where the organizational embeddedness

⁵⁷ The large German banks’ withdrawal from Deutschland AG was also motivated by a desire to avoid potential conflicts of interest between their role as investment bankers (M&A, capital market transactions) and their role as supervisors and owners (Höpner 2003). But their withdrawal as owners and supervisors did not remove the potential conflicts of interest between their fiduciary role as asset managers and the business interests of the bank’s parent company in cases of engagement with one and the same company (Kahan/Rock 2007: 1054–56).

⁵⁸ As the passage in §26 of the KAGB states, the “investment company [Kapitalanlagegesellschaft, or KAG] is obliged to act [...] in the best interest of the investment funds it manages or the investors of these investment funds, and of the integrity of the market.” It also calls upon KAGs to “take all appropriate measures to avoid conflicts of interest and, where these cannot be avoided, to identify, settle, observe, and where appropriate, disclose these conflicts of interest in order to (a) avoid these having a detrimental effect on the interests of investment funds and investors, and (b) ensure that the assets managed by it [the KAG] are treated fairly [...]” (Source: KAGB, <http://www.gesetze-im-internet.de/kagb>).

of the actors who should exercise this fiduciary role is also important. The corporate governance literature discusses this as “conflicts of interest.”

In practice, one cannot rule out that the fiduciary representation of interests in dealings with the issuer is specifically “colored” by informally transmitted information from the parent company or other departments, or through simple tacit agreement, especially since violations are not easy to detect or litigate. Conversely, however, it can be extremely bad for a fund company’s business if suspicions exist that the fund has been violating its fiduciary obligations by giving precedence to the interests of its parent company. Blatant consideration for the parent company must be avoided in all cases. Which institutional investor would give money to an investment company believed to put the interests of its parent bank over those of its (institutional) customers? In our interviews, at least, representatives of fund companies with a parent bank emphasized their independence and provided examples of conspicuous critical interventions at German companies where the parent bank was also present in some other role. For example, a fund representative talked of using his own votes to deny approval to the chair of the supervisory board, who also chaired the supervisory board of the fund company’s own parent company, a large German bank (KAGD1).

Conflicts of interest may also arise in nonbank fund companies if such companies also offer their services as fund providers (for company pension funds, for example) to the companies in which they are also shareholders in a fiduciary role. There arises the question of whether a fund manager will still vigorously represent critical challenges to bonuses for management if that fund manager intends to win a contract to administer pension funds from that selfsame management. According to our findings, the two tasks (sales on the one hand and “commitment” to observing shareholders’ rights on the other) are generally perceived separately from one another in the organizational perspective, but this does not exclude sales expectations from “coloring” the monitoring tasks. In some cases, moreover, the same person is responsible for executing both jobs. The KAGUS1 representative for Germany, carrying out both missions, sees no problem with this: in his opinion, the fund company understands its commitment to matters of corporate governance as dialogical rather than confrontational. KAGUS1 conveys its positions in direct talks (behind the scenes) and not at shareholders’ meetings or with the press as other fund companies do.

The effects of such potential conflicts of interest on the formulation of interests and the commitment of fund or asset managers cannot be determined externally – and insiders are reluctant to talk about them.⁵⁹ But we cannot deny the argument by Kahan/Rock (2007: 1055) that investment funds tend to be cautious because of potential conflicts arising from parent company business with the issuer or the fund’s own business with the issuer, and that fund company expectations are usually expressed in a less public manner and with less vehemence. They do not want to acquire a reputation as a “governance troublemaker” (ibid.). This reason also suggests a taciturn, “dialogical” attitude to the company that will not escalate conflictual issues.⁶⁰

3.2 Cacophony of voices or role definition as “universal investor”?

Investment companies will often assemble the entire universe of conceivable investment strategies for equities under one umbrella, with all their various connections to the real economy reference object. In many large investment companies, moreover, there are fixed-income funds of various types, including those that can contain bonds issued by those companies that are also represented in various equity funds.⁶¹ In this way, a large investment company is likely to hold both shares from various active and passive funds and corporate bonds from active and passive investment of a large company like Siemens or Daimler. If we were to classify the

59 Conflicts of interest are discussed quite openly among (sell-side) bank analysts. Evidence can be found in the ethnographic study by Mars (1998) and in Faust/Bahn Müller (2007) and Faust et al. (2011a).

60 But the fund management’s potential consideration of the interests of the parent bank certainly does not result in any “global corporate control” by an integrated financial industry (Vitali et al. 2011), as was hastily concluded from the misleading network study from the ETH Zurich (e.g., Dörre 2012: 78), which erroneously counts the shares of banks’ own fund companies as shares of the parent banks. The fact that fund managers may consider the business relationships of the parent bank does not mean that the higher-level bank strategically integrates the various relationships that it and its subsidiaries maintain with listed companies (for more detail see Faust 2014; Faust/Thamm 2015).

61 Take BlackRock, for example, the world’s largest investment company, with \$4.1 trillion in assets under management, \$2.1 trillion in stocks, and \$1.2 trillion in bonds. Its remaining funds are invested in mixed funds (\$.3 trillion), money-market funds (\$.3 trillion), and hedge funds/private equity (\$.1 trillion) (data from 30 Sept 2013, Economist 7 Dec 2013). In both large categories, the majority of the funds are passive and comprise indices (64 percent in total) (ibid.). According to company data (author’s inquiry), around 80 percent of the equity exposure in 2012 was passive, with the remainder active on the basis of fundamental analysis.

institutional investors who made claims against the listed company as a collective actor, we would have to assume that, at least at the level of the fund company, an integration or perhaps consolidation of the different perspectives at the company in question was occurring. Is this the case? And, if so, how does this happen?

Variation in the degree of integration of different investment perspectives

Our empirical examples provide insights into the opportunities and limitations of integration and consolidation of this kind, but we cannot provide evidence on the empirical prevalence of different form or degrees of integration. Indeed, the degree of organizational integration is very different. In various cases, the different investment classes and even the different fund types within the equity investment are administered in separate organizational units whose representatives do not even communicate with one another, let alone consolidate the different perspectives at a particular real economy enterprise.

For example, a large German insurance company combines German and European asset management, as well as US asset management, under one umbrella. Although the US company is traditionally bond-heavy, both companies now offer both bond and equity investment. The two companies are more likely to compete within the group than to even exchange, let alone coordinate, their respective perspectives on jointly held shares (KAGD2). The second-largest institutional investor in the world, KAGUS2, holds larger share packages in a great number of listed companies in Germany. KAGUS2 is divided into various autonomously operating divisions or subsidiaries by region and by customer group (“retail” and “institutional”) each of which may hold shares of these German listed companies: “We’re disaggregated from the other parts of [KAGUS2]. So there are three separate investment groups. And there is no visibility between the ownership of the stocks that are invested by each of these groups” (KAGUSD2). The governance team of the unit responsible for Europe and European institutional clients integrates engagement with issuers on environmental, social, and governance issues (ESG), but only for the shares their own unit holds in their portfolios. This means that one German listed company may hear questions and expectations from representatives from several investment vehicles of KAGUS2. In the case of two German investment companies (D1, D3), the activities in passive or “quantitative” funds have been outsourced to their own legally separate company. The representative from KAGD3 could not even say whether the available voting rights (for €15 billion in investment volume, in this case) were being exercised. He is not in charge of these, at any rate; he organizes the exercise of voting rights for the active funds in Germany. He generally assumes that in these investment schemes,

“there’s no voting, or its importance is far, far downstream: the quantitative funds are a mechanical affair, so there’s no fundamental content behind them, which means that there is no evaluation taking place, or no evaluation of the contents. And sometimes the strategies are also very short-term or momentum strategies in the market, meaning that in the end they’re holding them only briefly and they don’t make the necessary record date at all, or even the particular time during which they can vote. So I don’t know that a lot of voting behavior is taking place, at least. It’s also that if you go to a shareholders’ meeting now and you look at the shareholder register telling you whose representatives are there, you usually don’t find any passive funds” (KAGD3).⁶²

These shares, which are held separately by passive or quantitative funds, are “voiceless”: they exhibit no connection to the real economy reference object. Furthermore, the fund company does not exercise its available voting rights in such cases either, so that these funds contribute to low attendance at shareholders’ meetings and thus also to the possibility of coincidental majorities.⁶³

How different equity and bond perspectives are integrated

In other cases, different equity and bond perspectives are present simultaneously in a fund company. The prime example is KAGUS1, which is represented on all relevant indices in Germany and thus, alongside with some actively managed funds, has become the most important institutional investor in Germany. As in all other cases, the index funds here lack a voice with the management of the company in which they hold shares (there is nothing to tell them), whereas the fund managers who use active selection have their own perspectives at the

⁶² KAGD3 recognizes that KAGUS1 is an exception, however.

⁶³ It is not so easy to determine the cases in which voting rights result from passive or quantitative investment strategies at all. Very short-term holding periods (as in high-frequency trading) do not allow for any stock registration. Even in the case of index funds, voting rights only come about if the fund is based on physical replication, meaning that the fund also acquires the shares that are in the index.

companies in which they are invested. They have different valuation criteria that can entail a specific influence, as well as buying and selling decisions.

“When it comes to financial decisions, sometimes the portfolio manager will take one view while another portfolio manager may want to vote a different way. In a merger or acquisition situation, for example, they may take a portfolio-centered view where maybe our team would take more of a company-centered view” (KAGUS1).

The active fund managers at KAGUS1 perceive their role in a way similar to those in the KAGUS2 fund (see above).⁶⁴ They develop an opinion on the company that is fed on comparisons with competitors but colored by a portfolio perspective.

“And then we can say, yes, we dealt with a comparable company in America or in Asia, this is what’s happening there, and they’re dealing with similar issues and maybe here they take a different approach. And this is then a good, important discussion that’s being had, but not in the sense that we’re influencing the company as concerns the company’s focus on business areas, on strategy” (KAGUS1).

This individual point of view is addressed in communications with the management. Whether the fund managers are always aware of their own blind spot, the portfolio perspective, is unclear. They are certainly conscious of their own limitations:

“We don’t deliver performance by trying to just bungle into companies, but by evaluating the companies and then making investment decisions on whether we want to keep them or sell them” (KAGUS1).

As a result, these fund managers distance themselves from activist hedge funds and strategically operating anchor investors to the same degree:

“We don’t measure ourselves against whether we can understand the strategy of the company or lead it better than the management. And since we’re invested all over the world, it would be quite presumptuous if we assumed that. So we don’t meddle in the strategic issues. However, it can be that a portfolio manager will decide independently that ‘this doesn’t suit me, I don’t like this, other companies are stronger, I’m selling this one.’ But then this isn’t a decision by [company name], it’s a decision by the person in charge of a client portfolio” (KAGUS1).

Even if the shares from the index fund are “voiceless” in this way, they still have voting rights at the shareholders’ meeting. KAGUS1, the largest index fund provider in the world, also exercises these voting rights in a different way than in the aforementioned cases. This process is organized by a higher-level team, which at the time of our survey of the entire company consisted of around twenty people, four of whom in London are responsible for Europe, the Middle East, and Africa (EMEA). The fund managers of the active equity funds have a voice in this process and can also contribute their own points of view, though this is rare. This central team for corporate governance and responsible investment gets local support from the national subsidiaries, which are also in dialogue with the companies in which the fund company is invested, meaning that they also personally represent the company’s sales interests (see above). Thus not only is the engagement team in charge of executing the voting rights at the shareholders’ meeting, but also for dialoguing with the management. Issues in corporate governance are a concern here, including the environmental and social issues that can end up on the agenda (similar to KAGUS2, see above). The fund company interprets its fiduciary duty to represent the interests of its actual investors broadly and includes in it the otherwise “voiceless” index votes.

“So anyone who buys a DAX ETF with us is making a conscious investment decision: ‘I want to buy German large-cap stocks.’ And of course every investor – whether they do it through an ETF or another product – is additionally still trying to outperform [the market] by overweighting; both investor groups have an interest in the company being managed properly and the value increasing sustainably. And this goes for both passive and active [investments], so that’s why we always exercise our voting rights in their entirety” (KAGUS1).

Fund management relies on the conviction that “good” corporate governance will also lead to better economic results for investors in the long term:⁶⁵ “We exert an influence on good governance. And we are of the opinion

⁶⁴ The basic orientation is similar at the German fund companies as well: “But we do not interfere in companies; we don’t want to be insiders, we will not take a seat on the supervisory board or anything. And it’s very clear for us in the end: the company decides, that is, the management board decides; in large matters [it decides] in coordination with the supervisory board. But we have our ideas, of course” (KAGD1).

⁶⁵ There is debate (see Kahan/Rock 2007) over whether this conviction that good governance leads to good results is supported by studies (as a representative of KAGD1 believed) or by agency theory alone. But this basic conviction is shared by many and is thus part of the general expectation horizon. Whoever doubts it only makes themselves vulnerable, and puts the beneficial effects of their own actions into question besides.

that if the management is good and the management works within a good process, then the result for the company will be right too” (KAGUS1). Because the index funds give the fund company automatic and sustained representation in the most important listed companies of a country, in the view of KAGUS1 representatives, a long-term perspective is a natural outgrowth of this.⁶⁶ As a leading index fund provider, the fund company is distinctly and unavoidably diversified, which makes for an even more markedly macroeconomic perspective rather than a solely microeconomic, company perspective.⁶⁷

In addition to its exposure in various equities, the fund company also combines a considerable number of fixed-income funds under the same umbrella, so that the bondholder and equity investor can be one and the same company. The fund company thus has both bond and share perspectives in one entity. The two perspectives differ significantly at the level of the investment decision,⁶⁸ as various respondents confirmed:

“There certainly can be a bond-centric view or equity-centric view [...] for example it’s good for a bond if the company is economizing – that’s good for the bondholder – but it’s bad for the shareholder, because it could go well or better for shares if investment were being made in technology for the future and debt were being taken on. [...] these are partially opposed interests”(KAGUS1).

A manager of this investment company, who used to work at a major rating agency, was familiar with distinguishing between “shareholder-friendly decisions” and “fixed-income-investor-friendly decisions” from her time there. “By nature fixed-income people are focusing on downside or protecting from downside, and equity can have ups and downs” (KAGUS1). Differences manifest in decisions about dividend payouts in particular, where the various “funders of the capital structure” push and pull in different directions (ibid.). Possible conflicts (the kind that can be triggered by activist hedge funds demanding special payouts,⁶⁹ for example) can be manifest in value transfers from bond investors to shareholders, which can even be quantified.⁷⁰ The fact that the payout issue is a core controversy between the bond and equity perspectives was also confirmed by company representatives who are involved with both groups of actors.

“This is, of course, a cash outflow, so it’s generally always seen as [...] negative on the bond side: there’s less money there to pay interest or redeem bonds. And of course the equity investors want to see a nice return on their capital, in addition to the share price, which hopefully continues to improve” (IRU3).

“Yes, of course it’s different if that’s how you look at your basic requirements, because the fixed-income investor wants the repayment of the capital and actually would like to see a bit of almost this old HGB-type thinking [Handelsgesetzbuch, the German Commercial Code] about protecting creditors: as little risk as possible, high capital ratios, lots of cash to ensure interest payments and debt repayment. So this is a bit of a contradiction to what the equity investor wants: lots of leverage and the least cash possible, with all of what’s there being paid out instead, and earnings growth” (IR U2).

The IR representative from company U1 explained that his company was aiming for a sustained dividend distribution of around 40 percent, but that in the big crisis after 2008 they had also had to cancel a dividend once. While only some of the equity investors had seen this as a good thing, the rating agencies and fixed-income investors gave it a markedly positive reception: “they found it very, very logical, and the management gained a lot of credit for it.” Share buybacks as an alternative payout form are increasingly being rejected by the rating agencies “because the interests of the equity investors are too strongly foregrounded” (IR U1).

66 “Like most indexed investors, we are by nature long-term,” reads a company brochure on engagement practice. If one thinks in the long term, ESG issues can have an effect as well: “ESG practices are a focus because they have considerable potential to affect performance over time.”

67 Lynn Stout (2012: 89) asks the question, “Why do so many diversified investors seem blind to their own interests as universal owners? One response could be that if the diversification is automatic and unavoidable, as it is with index funds, it is easier to take the broader perspective of the “universal investor.” Thus the diversified investor does not have to succumb to the shareholder value ideology, which binds a company’s objective exclusively to the perspective of a hypothetical entity that is only concerned with the stock price of a single company on the present day (ibid.: 9).

68 For example, rating textbooks teach that companies that can distribute risks across various client relationships, business areas, and regions are better rated (Hiß/Nagel 2012: 117), whereas the shareholder perspective shaped by agency theory advocates a focus on core businesses because investors are entitled to diversify through their own equity portfolio and are not interested in entrepreneurially motivated safeguards (hedged) (Faust/Bahn Müller 2007: 62). Furthermore, rating agencies are more interested in adequate equity cover for loans, which in bad times serves as a loss buffer (Hiß/Nagel 2012: 115). Agency theory tells us that a higher debt ratio is also advantageous for principals, then, because of its disciplinary effect on the agent, the management; specifically, borrowing costs accrue continuously as cash-based financing costs and must be taken into account ahead of time for reasons of liquidity. Equity costs, by contrast, can only be considered as imputed values and are too easily ignored by shareholders, who expect opportunistic agents.

69 In general, activist hedge funds are often in conflict with bond valuations (Stout 2012: 92).

70 A study on the activism of hedge funds in the United States (Klein/Zur 2009) calculated that the implementation of higher payout ratios or an increase in the risk profile of the target company by activist hedge funds led to an “average abnormal loss” of 6.4 percent in the following year (Becht et al. 2014: 6).

Seriously considering the differences between the bond and the stock perspectives also opens up a new view on the overall constellations from the company's perspective. Whether a company has an anchor investor (or not) and therefore has few (or many) concerns about price weakness in its own shares, whether it relies on financing through the stock market (and is therefore interested in a high stock market value), whether it can finance growth and innovation mainly from retained earnings, or whether it needs cheap debt financing from the capital market: from the perspective of the real economy company, all of these different conditions shift the importance of the bond (or equity) perspective and thus that of the rating agencies and bank analysts. Whose expectations should be given top priority, whose can be pushed back? The following example illustrates the case of a company with an anchor investor for whom the fixed-income perspective tends to take precedence. In this company, investor relations is responsible for creditor relations as well, and also manages the rating agencies and the bond investors.

"Fixed income is almost more important for us [...] we finance all our industrials from our own cash flow; we don't need any debt financing here. Quite the contrary: we have over 12 billion in net financial assets, we hold a cash position and we don't take on any liabilities. At the same time, however, we're taking on 15 to 20 billion in financial liabilities every year for our financial services business. We don't need any equity for the car business, nor for the financial services business. We can accumulate this from our own earnings; we just have to get ourselves borrowed capital for it. So we take great care with the rating agencies [...], [we] have very good ratings. [...] On the other side, we're talking to the investors themselves because our philosophy on refinancing is that we don't want to depend on the banks. In other words, we're trying for placement directly on the capital market, using the banks only as an intermediary, but we borrow almost no money from banks" (IRU2).

The fund management of KAGUS1 is aware of the potential conflicts between the bond and equity perspectives, which can also be reflected in different valuations and, where applicable, in the influence of the respective fund managers. However, just as we have seen as in the perception of different equity perspectives, the higher-level fund management claims that "both interests converge" in the long-term perspective. The fund manager on the bond side has a personal voice he can use to express his expectations, but no voting rights, unlike the shareholders. Nevertheless, both voices can be jointly articulated on ESG issues and as part of the exercise of voting rights.

"So the bond voice is just as important as the shareholder voice and is of course represented by us in the same terms as the corporate governance issues that are now coming together. This is not a contradiction. [...] And it's why we can't play one side against the other: these are sometimes opposing interests, but in the long run both interests obviously converge. And then we talk about the issues where both are converging, [...] that there's good governance happening, that a company is being managed with transparency, that high ethical standards dominate, that there is zero tolerance for corruption. Bondholders *and* shareholders profit from this" (KAGUS1).

Thus the perspectives of passive index funds, active investment funds, and fixed-income funds, all of which can potentially diverge at the fund level, are being integrated by this US fund company at the higher level of engagement, which concerns ESG issues and the exercise of voting rights linked to the agenda at the shareholders' meeting. Corporate governance issues such as capital increases, remuneration schemes, payouts, and the composition of the supervisory board are at the forefront, while environmental and social standards are less frequently discussed (see section 2.2 above).⁷¹

On this basis, the fund operates in a dialogical, constructive, nonconfrontational, "nuanced and sensitive" (company brochure) and long-term-oriented manner, without public appearances or use of the media, in line with the respective regional and national rules of "good corporate governance" – and therefore not as an ambassador for a universal, exemplary model.

"We can only take on issues with long-term significance or that concern the framework of the company, but not the decision of the company itself. [...] We don't go onto the supervisory boards, we are fundamentally supportive, we look at governance issues [to ensure that] the dividend policy is right, the governance is right, there's no abstruse compensation being paid, the incentives for the management are right, the standards correspond to either international standards or good standards in Germany" (KAGUS1).

Fund management in Germany considers itself a sort of "successor" to Deutschland AG. This is a slightly exaggerated characterization of its own role since, as insiders, the characters in the old Deutschland AG had a

⁷¹ The KAG reported on its engagement and voting practices. In the year 2014/2015, among all engagements it addressed "corporate governance" issues 1550 times while "environmental" (78) and "social" (98) were less frequent. In 2014/2015 KAGUS1 exercised its voting rights at a noticeable 15,386 shareholder meetings worldwide. However, only in about 10% of all companies in which it exercised voting rights the investment company also showed engagement of any kind.

far more influential say in the long-term fates of the companies. It also overlooks the fact that many listed companies still feature a stabilizing anchor investor who is responsible for monitoring management and exerting strategic influence. The anchor investors are therefore much more of a functional equivalent to Deutschland AG. But for many index-listed companies with free-float shares that often see low attendance at shareholders' meetings because of the "rational apathy" of the others, KAGUS1 is often the largest individual investor that is also permanently connected by the index relationship. At any rate, there's a feeling that one is called upon to fill the gap that has been created, to define this as a sociopolitical duty.⁷²

"If you are the, quote, 'successors' of Deutschland AG, which is in fact what we are, you have a ticket, you have a responsibility. And if no one votes at the shareholders' meetings and no one talks to the management [...] who's going to do it if we don't? Or who has a right to do it?"

"...we're also fulfilling a sociopolitical duty here. With our very positioning, we don't belong to a bank, and we haven't been involved in the banking crisis in any way, quite the contrary. One of our main businesses is tidying up toxic assets: we're the manager of the bad banks, so we tidy up what the banks have left behind and from there of course we're also available as a dialogue partner for politicians, central banks, other institutions, and these kinds of governance duties that we perceive as being part of this overall package somewhere" (KAGUS1).

Fund management defines "good" governance as good according to the valid standards in Germany, for example as stipulated in the German Corporate Governance Code. The corresponding guidelines are adapted to the respective country, so that in Germany they fit the requirements of the two-tiered system of corporate supervision and codetermination at corporate level.

"We are trying to ensure the best governance for a German company, which can be quite different from that of a Greek company or an American company, and [to ensure] that we are very aware of these differences: there's codetermination here, there are supervisory boards with equal representation here, etc." (KAGUS1).

The US fund company does not see itself as an ambassador for an American model. The German representative of KAGUS1, himself a German, sees it more as the reverse: a growing appreciation of the German model among adherents to Anglo-Saxon capitalism.

"I've been noticing, maybe for the last two or three years now, that the understanding of and the appreciation for the German model has increased among Anglo-Saxons, which clearly has to do with the fact that we came through the crisis well and that our governance in Germany was obviously one reason. So I've never seen or experienced someone going in there and saying, 'we don't understand this, and now you have to do it exactly the way we know from America, and codetermination, what's that?' I've never experienced that. So the question is not what is good governance from America that we import to Germany, but what is good governance in Germany" (KAGUS1).

Although the fund acts only behind the scenes with respect to individual companies, more recently it has made its mark with contributions to public discussions in which it positions itself as a kind of "universal investor" (Stout 2012) with a superordinate, more macroeconomic perspective. In a letter to all the companies in which the company holds shares, the asset manager wrote that he was "concerned about the short-term thinking on the capital markets" and asked the CEOs to "invest in the future more" instead of increasing dividend payouts or buybacks of shares (source: Manager Magazin 14 April 2014) (see also Kädtler et al. 2017).⁷³

The relative persistence or intensity of the engagement process at the companies cannot be verified empirically. One reason it does not become too confrontational is to avoid doing intentional damage to other business interests with the issuers. However, there is also a certain pressure in the expectations of their own clients, the investors, who are themselves often institutional investors and must demonstrate fiduciary responsibility. This means that the fund company must also demonstrate its engagement effectively and report on it. All the same, the engagement ought not be too costly for the customers and/or the fund company itself, since there are always free-riding competitors taking the easy way out. Fund management is therefore also aware that it is important to try to keep the engagement "within limits for our company as well. This is not our main task, so we have to do it within a certain framework" (KAGUS1).

72 KAGUS1 did not become the world's largest fund provider until after the global financial crisis, when it took over the assets of struggling banks. Its own positioning attempts to profit from the banks' loss in reputation.

73 Exhortations to management not to "save [company U3] into collapse" and to go back to investing more in growth were also made by another fund company (KAGD3), which likewise emphasizes its long-term orientation.

4. Conclusion: Heterogeneity in various constellations

We have developed a typology of investment strategies in which we differentiate according to the type of connection to the real economy reference object. These different connections suggest different definitions of interests and different strategies for pursuing those interests. This affects the communication with and the influence on the reference object. The illustrative examples and evidence of each type's relative pervasiveness in Germany offer an impression of their respective relevance. From this we have worked out two key results: The investment strategies identified are extremely heterogeneous indeed, and they vary considerably with regard to the questions of whether investors wish to influence the respective company at all and of what kind of influence results. This variation is particularly marked between investment strategies with a connection to the real economy reference object and those without. In the case of the latter, no motives for the investment decision are communicated. The resulting price movements are effective as such, but mute. But there is also a fundamental difference between investment strategies *with* a connection the real economy reference object and ownership of enough shares to control the company. The former have no link to the company and retain an exit option for themselves. There are considerable differences within the group of investment strategies *with* a connection to the real economy reference object, specifically between activist hedge funds and essentialist investors. Whereas activist hedge funds are the prototypical representatives of the short-term interests of shareholders who may pursue those interests at the expense of other shareholders and/or stakeholders, essentialist investors can take a long-term perspective that makes it seem prudent to introduce issues of ESG or sustainability, since they hope to reap their own benefit from the expected improvements. In the middle of this group are investors who are keeping an opportunistic eye out for their chance without going too deeply into any one company, much less blatantly creating opportunities for influence in the way that activist hedge funds do. But opportunism also implies that these actors are vulnerable to being mobilized into the campaigns of activist hedge funds.

The heterogeneity captured in this typology contradicts the basal assumption of the theory of “financial market capitalism” (Windolf 2005b): that company management faces a collective actor with uniform behavior in the form of the institutional investor, one with not only a unified will, but also the capability to “compel” management to maximize shareholder value in the short term (Windolf 2005b: 5, 23).

Regarding the German case (and presumably quite some other continental European cases) to a considerable degree the ownership structure of listed corporations is still characterized by anchor investors (more than 25 percent of votes), a constellation that discourages hedge fund activism and is a remedy against unfriendly takeover bids deemed to discipline corporate managers. 58 percent of listed corporations in Germany (Faust/Thamm 2015, 2016) are in this way protected by „patient capital“ (Culpepper 2005; Deeg/Hardie 2016). Moreover, also among the other investors the basic connections to the real economy reference object are too heterogeneous to speak of a unified interest definition in terms of corporate strategy, not to speak of a unified pursuance of interest to justify the parlance of *one* “collective actor” that stands vis-a-vis corporate management. Then there is the verifiably false habit of immediately classing “Anglo-Saxon” investors, who are actually more involved in listed companies in Germany than they were in the 1990s (see Faust/Thamm 2015, 2016), as the type of shareholders who are oriented towards a short-term increase in the market value of a company. These actors are perceived to be culturally “alien,” but they are not necessarily emissaries of an American or Anglo-Saxon model of corporate governance.⁷⁴ Instead, they are (or act as) situated actors who consider their embeddedness into local contexts when defining their interests and pursuing those interests. This embeddedness varies and has institutional (e.g., corporate governance rules defining rights and obligations of various stakeholders), structural (property structures), or cognitive-cultural (local/regional ideas of a “good,” “responsible,” “sustainable” company) aspects.

The evidence on the prevalence of activist hedge funds already points to the second major insight, namely that the interest definitions and especially the action strategies of the individual types of actors should not to be understood as independent of one another. Thus it is *constellations of actors* that count. Additionally, which voices become important depends on institutional factors, specifically the institutionally defined thresholds for influence, and on structural factors, in particular the shareholder structure. Institutional rules define what can be structurally effective here (see Faust/Kädtler 2017). The decisive structuring is whether a company has a (stable) anchor investor. Having an anchor investor frustrates or obviates both the classic strategies of disciplining the management by threatening a hostile takeover and the “exploitation strategies” of activist hedge funds.

⁷⁴ The corporate governance of the United States and Great Britain is much more heterogeneous than often assumed (Jackson 2010; Black/Coffee 1994; Becht et al. 2014), and is itself in transformation (Ajibo 2014; Ho 2010).

Essentialist investors with long-term investment horizons can in turn benefit from stabilizing anchor investors who, for purposes of their own interests, actively take on the task of monitoring management, while company management (IR) is interested to maintain a more dialogical exchange with these essentialist investors.⁷⁵ Furthermore, how important a real economy company considers the (sometimes contradictory) valuations and expectations of its shareholders to be (which ultimately can be reflected in the share price, and which the management may also take into account) also depends on whether the company relies on the stock market to finance growth or business development.⁷⁶

Activist hedge funds particularly favor those companies with free-float shares and often low attendance at shareholders' meetings; depending on the assortment of other shareholders at such meetings, they can find allies to use in "wolf pack" campaigns (Kahan/Rock 2007). On the whole, and despite the advance of financialization during the 1990s and early 2000s, the institutional and structural conditions in Germany continue to be relatively unfavorable to disciplinary strategies on the basis of hostile takeover threats and to activist hedge funds, which is why campaigns by the latter are comparatively rare in this country. Constellations of an unfavorable assortment of shareholders are still conceivable, however, which can put considerable pressure on company management that is facing challenges.⁷⁷ In such situations in any case, something different must be done, if only to gain time and forge new hope through a new "narrative" (Froud et al. 2006). The more frequent top management changes over the past two decades indicate that something like this is happening now and again. Whether such incidents come at the expense of the company's long-term development and/or impacts less powerful stakeholders can only be answered with a case-by-case analysis.

In a next step, we also examined whether and how the different investment strategies of shares (which in fund companies can be represented together with the bond or fixed-income perspective) can be translated into a higher-level definition of interests, and what this means for the influences exerted on companies. Our findings on this are mixed. In many cases, the different perspectives are pursued separately, from an organizational standpoint, and the potential resulting influences are not consolidated, making their influence on the respective companies heterogeneous. For example, communicating with and/or exerting influence on the management does not seem to be opportune in many cases involving passive or quantitative investment strategies, and no voting rights are exercised in such situations either. This also applies to some of the investment strategies with a connection to the real economy reference object: such strategies will favor "rational apathy" in the cost-driven competition for investment monies, trusting that others will take over this monitoring function. Thus each of these individually operated funds contributes to the emergence of those constellations of low attendance at shareholder meetings among companies without an anchor investor, the same low attendance that benefits activist hedge funds.

The different perspectives that may be present at large fund companies concerning the companies they hold can remain effective individually as portfolio perspectives, but they may nevertheless be combined at a higher level in the communication with and influence on those companies. The latter concerns the higher-level issues of corporate governance and meanwhile (after having experienced the global financial crisis and increasing pressures from a general public and organized social movements demanding more attention to environmental protection and social standards. The influence of this type of fund company remains heterogeneous and somewhat inconsistent because (divergent) individual perspectives continue to be effective. The fund company presented as a prominent case here, however, a highly diversified and long-term investor, approaches the role model of the "universal investor" in its overriding influence. According to Lynn Stout (2012: 86ff), and in contrast to the shareholder value ideology, the "universal investor" should be interested in the endurance of an entire economy, one that grows, supplies investment opportunities, and yields revenue. Our empirical approach does not indicate how much weight voices of this type have when taken together with other voices and the voiceless.

75 Excessive compensation packages for top executives, with incentives that are often decoupled from (ongoing) evidence of success, are less pronounced in companies with anchor investors, for example.

76 Although this is rarely the case on average (see van Treeck et al. 2007), it can sometimes be quite significant indeed (see Faust et al. 2011a). Alternatives to equity financing through the stock exchange are internal financing through retained earnings or debt financing from banks or the capital market. How well the alternative financing conditions are arranged also determines the power position of the company vis-à-vis the different shareholder groups.

77 The IR representative of a company with free-float shares pointed to experiences in Germany with hedge fund activism through Deutsche Börse and IWKA/KUKA, where "certain investor groups that simply see economic capital in shareholder activism" could then also become capable of winning a majority. IRU1 thought that the company must also be "in a very sorry state," however, and that there must be "great dissatisfaction with the management." Whether such a thing could even be possible at an industrial icon the size of U1 remained unanswered.

Nevertheless, the fact that these voices exist among financial investors, and that they are quite prominent and do have a weight, gives company management (and in particular those stakeholders who enter into a stronger bond with the “going concern”) the opportunity to refer to a broader range of definitions of *the* “shareholder interest.”⁷⁸ However, the stubbornness and effectiveness of an engagement by this type of fund company can also be hampered by considerations for other business interests, as well as by cost-driven competition, which does not suggest “rational apathy” so much as moderate and selective engagement.

Constellations of external influences on the listed company of course comprise more than just the shareholders’ connections (heterogeneous, as we have seen) to the real economy reference object. Other areas in which the “multireferential company” is embedded are also helping to determine how and in how far shareholder influence becomes effective. This is already happening in the efforts by shareholder representatives to define the interests of the shareholder while executing the fiduciary role in light of other legitimate and effective interests. If we include bond investors and rating agencies alongside the shareholders in our constellation analyses, those perspectives desiring to rely on dependable, long-term development and to prevent the hasty distribution of returns become more significant; their position can also be consistent with the definitions of shareholder interests used at the higher levels of fund companies’ influence on companies. The effects of the bond and equity perspectives on the company’s also depend on how much the company relies on having a supply of equity and/or debt. The political and cultural developments that affect the company as a whole will determine whether environmental and social standards will play an additional part, alongside the classic corporate governance issues, when shareholders evaluate and influence companies. When politicians, trade unions, the general public and nongovernmental organizations criticize or even pillory a company for its environmental policies, corruption, or violations of human rights or social standards, this increases the likelihood that fund companies will also take up such considerations when evaluating and selecting companies, as well as when influencing them, if only because this type of noncompliance can also lead to economically harmful reputation risks that affect the equity investment. The institutional safeguarding of codetermination in workplace decisions, as exists in Germany, mainly shifts the balance of power in the internal coalition, as does the relative power of the positions held by works councils and trade unions, respectively, that may widely differ within the same institutional context. Power distribution within the company also contributes to how external influences are perceived and evaluated and which of them become relevant to the strategy formation of the multireferential company (see Faust/Kädtler 2017). In short, a complete analysis includes the various constellations of external influence and mediates these with the internal coalition. We hope with this article to have taken the first steps along this path.

Regarding the newly accentuated interest in the relevance of “patient capital” (Deeg/Hardie 2016 and the respective SER Special Issue) for the analysis of both capitalist diversity and processes of financialization our contribution reassures the relevance of traditional carriers of “patient capital” (notably family owners even among listed companies) in Germany. Moreover, we concur with Deeg and Hardie that it is worthwhile to consider other potential carriers of “patient capital” beyond the traditional candidates, i.e. also among financial investors, and give some indications why particular types of investors are more likely to be patient. Finally, we suggest that the analysis of constellations of actors in the external coalition (Mintzberg 1983) adds additional insights under which conditions which kinds of interest definitions (including “patient” ones) will emerge and become relevant. Institutional rules, defining the rights and obligations of actors, including the purpose of the corporation, that in most cases are determined on the national level, continue to be relevant in defining the arena in which patient and impatient capital meet and the likelihood of which predominates.

⁷⁸ This has an internal side as well: what the shareholder interest(s) is/are is of course a matter of perception and interpretation, in which the boundary spanners to the capital markets (IR, CFO) have the structural and cognitive-cultural advantage. They can use their estimates of threats and opportunities for micro-political games in strategizing (for more detail Faust/Kädtler 2017).

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