International Capital Mobility and Domestic Institutions: Corporate Finance and Governance in Four European Cases

RICHARD DEEG* AND SOFIA PEREZ**

This article considers the impact of international capital mobility on the character of corporate finance and corporate governance in four European countries (Germany, France, Spain, and Italy). We take issue with the widespread view that the growth of international financial markets and the lifting of capital controls will in themselves produce convergence in national systems of corporate finance and governance. Although we find evidence of convergence in specific aspects of financial regulation (e.g., the abandonment of selective credit regulation and the dismantling of barriers to universal banking), these regulatory changes have not produced any clear convergence toward either the Anglo-Saxon model of corporate finance and governance predicted in much of the literature or the alternative German bank-based model. The reasons for this, we suggest, have much to do with the way in which the politics of financial reform are likely to differ from those postulated in market-driven models of regulatory change and the fact that countries are susceptible to international pressures in different ways.

This article considers the impact of financial integration on the character of corporate finance and corporate governance in four European countries (Germany, France, Spain, and Italy). Contrary to the widespread view that the growth of international financial markets and the lifting of capital controls will produce convergence in national systems of corporate finance and governance, we find that increased cross-border capital mobility since the mid-1980s has not led to such an outcome. Although we find evidence of convergence in specific aspects of financial regulation (e.g., the abandonment of selective credit regulation and the dismantling of barriers to universal banking), these regulatory changes have not produced any clear movement toward equity-centered systems of corporate finance or toward an "outsider" model of corporate governance. Corporate governance in all four countries continues to grant a dominant role to bank-mediated forms of finance and to corporate control by "insiders." Indeed, in those cases where old patterns of "insider" control have been disrupted by changes in financial regulation (as in the case of privatizations), new mechanisms to prevent an

*Temple University.
**Boston University.

Governance: An International Journal of Policy and Administration, Vol. 13, No. 2, April 2000 (pp. 119–153). © 2000 Blackwell Publishers, 350 Main St., Malden MA 02148, USA, and 108 Cowley Road, Oxford, OX4 1JF, UK. ISSN 0952-1895

overly active market in corporate control (such as an expansion of cross-shareholdings among firms) have emerged. On the other hand, there is also little evidence of convergence toward what is often considered the viable alternative, that is, the German model, in which banks offer long-term financing to industry while taking an active monitoring role in corporate governance. It thus appears that increased capital mobility is having at best a shallow effect on domestic institutions, and that it is not bringing about the kind of convergence toward the Anglo-Saxon model of corporate governance predicted in much of the literature, nor an effective move toward the alternative German model.

In the following section we set up the theoretical problem in light of some common assumptions about the impact of international financial integration on domestic financial systems. Thereafter we offer a series of case-by-case descriptions of the main changes that have taken place in each of the four countries, followed, in the next section, by an assessment of the cross-national patterns of change that can (and cannot) be observed. In the last section we set out to explain the failure of convergence in underlying institutional structures toward the kind of model we might expect from a market-driven process of change. The answer, we suggest, has much to do with the way in which the politics of financial reform are likely to differ from those postulated in market-driven models of regulatory change and the fact that countries are susceptible to international pressures in different ways. The kind of political dynamic envisioned in these models, we argue, is more likely to occur in countries that already have fairly competitive domestic financial systems prior to the onset of rapid market integration. In other countries the process of regulatory reform is likely to be led by public officials. Yet the reform incentives faced by such officials have foremost to do with the relationship between financial market institutions and their macroeconomic policy objectives, and therefore do not necessarily favor assertive reform of market structures. In these cases officials have reformed financial markets as much as necessary to achieve macroeconomic objectives while simultaneously attempting to preserve traditional institutions such as insider control. Indeed, the incentives that increased capital mobility create for firms are just as likely (if not more) to favor a search for new mechanisms of insider control as they are to promote a shift to an outsider model of corporate governance. Lastly, we suggest that the lack of an alternative pattern of convergence toward the German model of corporate finance and governance may be explained in terms of the absence of wider institutional conditions that support such a model in the German case and, more generally, to institutional path dependence.

THE QUESTION: INTERNATIONAL MARKETS AND DOMESTIC FINANCIAL SYSTEMS

One of the prevalent notions held today by political economists is that change in domestic institutions over the past two decades has been driven largely by the pressure of international market integration. The rise of global financial markets and the increase in cross-border capital flows, which have accelerated dramatically in the past two decades, are seen as being particularly important in this regard. Changes in the regulation of labor markets, welfare state regimes, and macroeconomic policies (including the levels of deficit finance, the status of central banks, and trends in taxation) are all seen to be responding in significant measure to these forces of international financial integration (see Garrett and Lange 1991; Scharpf 1991; Banuri and Schor 1992; Goodman and Pauly 1993; Moses 1994; Maxfield 1997).

Another area of regulatory change commonly attributed to the forces of international financial integration is that pertaining to national financial systems. The rise of international financial markets seems to have a particularly direct bearing on this aspect of domestic economies because it creates new forms of competition for domestic financial institutions. Both holders of liquid assets (savers, investors) and users of funds (in particular, firms looking to raise capital or loans) may look to international markets to receive better terms. Thus, it is believed, national authorities are forced to reform domestic financial systems in a manner that allows for greater allocative efficiency in order to avoid excessive capital outflows. In this market-driven convergence view, change in domestic financial institutions is a direct function of the overregulation and microeconomic inefficiency of existing structures, and efforts at financial reform can be expected to conform to the criterion of creating more efficient domestic capital markets (see, e.g., Frieden and Rogowski 1996; Thompson 1998).

One of the implications of this view is that historical differences in financial systems (as per Gerschenkron 1962; Zysman 1983) will be eroded by these competitive market pressures and that there will be convergence toward some form of "best practice" in financial systems (for an overview of these arguments see the discussion in Berger and Dore 1996). It is not entirely clear, however, exactly what kind of financial system would lie at the end of such a market-driven convergence process. On the one hand, in the area of banking regulation there seems to be pressure toward a generalization of the universal banking model, historically exemplified by Germany, in which banks are allowed not only to lend to, but also to hold stakes in, nonfinancial firms and, on the basis of inside information, can provide long-term finance and guidance to firms. A trend toward this model in national regulation can be seen not only in Europe but also in the United States (Deeg and Lütz forthcoming). On the other hand, the liberal or market-driven view generally predicts a shift toward equity markets as the providers of long-term investment finance because these markets involve lesser intermediation costs and are quicker to respond to underperformance in firms and hence are believed to be more efficient (OECD 1995b; Thompson 1998).

These two "financial system" models are also generally associated with opposite models of corporate governance. Universal banking is associated with an "insider" model of corporate governance in which banks are the primary providers of long-term external finance. Bank risk is managed by the presence of bankers on the boards of companies that have access to inside information and thus the ability to monitor business operations and conditions. Control over companies, in this model, is generally held by majority stakeholders. Ownership tends to be concentrated and stable, and there is not much of a market in corporate control. Equity markets, in contrast, are associated with an "outsider" model in which most long-term external finance is raised through issues of shares, and firms retain an arms-length relationship with banks, which provide mostly short-term finance. In this model, corporate governance pivots on the theoretical notion of protection of minority shareholders. Ownership is far less concentrated, independent directors and transparency in reporting standards are of the essence, and drops in share prices and hostile takeovers serve as the ultimate sanctions on performance. That is to say, there is an active market in corporate control.

Each of these corporate governance models is, in turn, attributed certain advantages and disadvantages. The universal banking-centered insider model is normally viewed as superior in promoting a long-term managerial focus (Porter 1992). It has also been argued that this model is a more efficient allocator of resources in industries with stable technologies (Allen 1993). The equity-market-centered outsider model, on the other hand, is typically viewed as superior at financing radical technical and product innovations, especially as embodied in new firms (Porter 1992; OECD 1995b, 29). On balance, however, the received wisdom is that international financial integration forces compliance with the standards of equity markets and tends to undermine the "insider" model of corporate governance. This is so because international investors generally demand greater information from firms and transparency and are concerned with maximizing shareholder value in the short term. Such demands are anathema to the insider model, which values long-term growth and other objectives over, or alongside, share price (OECD 1995b; Thompson 1998).

In this market-driven convergence view, changes in domestic financial systems thus respond directly to the dynamic of international market arbitrage. If this view were correct, then we would expect to find evidence for six kinds of trends: (1) a clear shift from borrowing to equity finance by firms, as firms utilize expanded opportunities to secure lower-cost capital directly from either domestic or foreign markets; (2) a significant broadening of the distribution of ownership of public companies, and (related to it) (3) a shift toward the "outsider" model of corporate governance; (4) the emergence of markets for corporate control, that is, as more firms move to the equity market and ownership broadens there should be a rise in open competition for the control of firms via takeovers; (5) as concerns the financing of small- and medium-sized firms (SMEs), a big uptick in Initial Public Offerings (IPOs) and venture capital as financial reform takes place; and (6) convergence in the cost of external finance, ceteris paribus, as firms can more readily shop different markets for funds.

Against this backdrop, we consider the recent experiences of the four largest European Union (EU) member states that entered the current period of rapid financial integration with bank-based systems and some version of the insider model of corporate governance: Germany, France, Spain, and Italy. These European experiences represent interesting cases from a theoretical perspective because the rate of increase in cross-national capital flows over the past two decades, which has been very large at the global level, has been particularly high in the EU. The principal factor behind this has been the extremely sharp rise in intra-EU capital flows that began in 1987 as a result of the lifting of remaining capital controls by several EU states, in accord with the Single European Act of 1986. The "growth of portfolio capital from and to Member States" grew "by almost 300% between 1990 and 1993," and the share of foreign direct investment in total gross fixed capital formation in the EU grew from 2.9% in 1985 to 6.5% in 1995 (European Commission 1997b, 6–7).

EU financial systems have experienced a further competitive shock in the period since 1992 as a result of the Second Banking Directive. The latter made it possible for banks licensed in one member state to operate under their home country licenses throughout the EU (with some restrictions) as long as they meet certain standards of solvency and prudential regulation (for details see Story and Walter 1997, 254–271). Nevertheless, in the following analysis we seek to distinguish between changes in domestic regulation and financial systems that were under way before (or independently of) the requirements of compliance with EU legislation and thus presumably responded directly to market pressures, and those that seem to occur predominantly because of the need to comply with EU legislation.

Given the two competitive shocks in the EU (the dramatic rise in cross-border capital flows and the change in the European regulatory environment), we find much greater indeterminacy in the evolution of the four national systems of corporate governance considered here than we might expect from a market-driven process of change. While there has been a process of change in national regulatory regimes that seems to imply a form of negative convergence (convergence through the abandonment of certain old regulatory models such as state-directed credit-allocation), this change in regulatory institutions does not seem to have produced the kind of transformation in underlying patterns of corporate finance and governance expected by many observers. Indeed, the apparent convergence in regulatory patterns away from state intervention has been accompanied in several cases by clear efforts to reinforce an "insider" model of corporate governance. Before moving on to describe this pattern of change (and lack thereof) that we observe across the four cases, the next section first offers a brief overview of the character of postwar financial systems and recent regulatory and market changes in each country.

FINANCIAL REGULATION, CORPORATE FINANCE, AND CORPORATE GOVERNANCE IN FOUR COUNTRIES

In the four cases below we review the history of financial market reform and examine evidence for the following variables: changes in equity versus bank financing of firms; changes in the ownership pattern of large firms; changes in corporate governance patterns; changes in the market (or lack thereof) for corporate control; changes in the financing pattern of SMEs; and changes (convergence) in the cost of external capital.

Germany

In the literature on financial systems Germany is often thought of as representing the quintessential universal banking system. Since the late nineteenth century banks have acted as both lenders and investors in nonfinancial firms, often holding substantial equity stakes in individual firms. Bank representatives sit on numerous corporate boards and are regarded as playing an important role in corporate governance. The advantage of this close bank–firm relationship is said to lie in the provision of long-term, or "patient," finance for investment, which is made possible by the intensive exchange of information between bank and firm. Equity finance has traditionally played a secondary role to bank lending in this system, and ownership of large firms is typically concentrated in the hands of large, stable shareholders (mostly other nonfinancial firms, families, and banks). Thus, Germany has an insider system of corporate governance. The state, on the other hand, has played a comparatively peripheral role in this corporate ownership and governance system. In the postwar period, and especially in the past twenty years, there has been a substantial amount of state-subsidized credit to the private sector. Yet this state credit is mostly allocated by the banks according to market criteria and therefore does not resemble the system of state-directed credit allocation adopted in France and Spain during the postwar period (Deeg 1999).[1]

Pressures in favor of financial reform in Germany began to build in the mid-1980s, as the major German banks felt the need to keep up with financial market innovations in the U.S. and U.K. Large German nonfinancial firms were increasingly going abroad for capital and investment banking services and borrowing less and less from domestic banks. The German banks realized that traditional bank lending was in permanent decline and that the future lay in investment banking services, both for retail and corporate customers. However, despite this growing consciousness, the German regulatory system experienced few important alterations until the beginning of the 1990s when the completion of the Single European Market in Financial Services became imminent. Most of the change in German financial regulation since that time has involved securities rather than banking markets, since the model of banking regulation adopted in the EU's Second Banking Directive closely resembles, or at least largely accommodates, that of Germany. In addition, German banks are fairly competitive in Europe and the domestic German market has been competitive and relatively open to foreign competition for quite some time.

Stock exchange reform did not take off until 1992, when Frankfurt began to fear for its future in an integrated Europe. Large German banks wanted to compete with London and New York in investment banking markets and get more business of international institutional investors to come to Frankfurt. So the banks, together with the Finance Ministry and bank regulators, worked out measures to increase market transparency, remove restrictions on product innovation, and combat insider trading (Lütz 1998). Consequently, in the 1990s there was much more derivatives innovation, the creation of a new state securities regulator (modeled on the American SEC), and the beginning of commercial paper and money market funds. Other measures, such as tax changes, have also been adopted to encourage more investment by German households in equities and to encourage German firms to go public.

The concerted push to develop equity markets in Germany—referred to as the *Finanzplatz Deutschland* campaign—has stimulated the growth of securities markets. However, these reforms have not substantially altered most of the key features of the German model of corporate finance. Large German firms have enjoyed very high rates of self-finance and since the 1970s have been borrowing less from banks. They have also availed themselves of new ways to raise capital in securities markets, both in Germany and abroad. Yet the aggregate role of equity finance is the same today as it was at the beginning of the 1970s (see Table 1), and only a handful of the very largest firms are increasing their use of equity finance (Deutsche Bundesbank 1997, 28–32). SMEs still rely heavily on bank finance, with ample and cost-effective long-term financing. German authorities have gone out of their way to sustain the system of close bank–firm relations for SMEs and long-term bank finance in the face of financial market integration, by, among other things, promoting modernization in the savings bank sector and expanding SME lending by public banks. During the late 1980s and 1990s venture capital funds grew steadily, but they tended to be conservative, investing in established firms rather than startups. Since the introduction of a new exchange for small firms—the Neuer Markt—in 1997, the number of IPOs has jumped dramatically and many view this as the beginning of a new equity culture in Germany. But it is too early to conclude that this activity will bring about a real and active change in the German model of corporate finance. With just 115 listed firms as of mid-1999 (compared to some 5,000 on the U.S. Nasdaq), the IPO rush is still very modest in many respects. Moreover, the Neuer Markt focuses on technology stocks and its success may well be limited to such stocks: for

TABLE 1
Equity Shares as Percentage of Total Liabilities of Non-Financial Firms

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Germany	13.6	13.4	13.1	12.9	12.9	13.9	13.8	13.2	12.7	12.3	12.4	12.2	12.1	12.1
France	8.3	8.0	7.4	8.2	8.8	8.9	8.8	8.1	13.1	15.6	14.1	15.8	15.0	14.5
Spain	34.6	14.5	15.3	16.3	18.0	18.7	17.7	17.6	17.2	17.5	17.5	17.9	17.5	17.1
Italy	14.7	14.0	14.5	15.3	16.0	15.4	15.5	15.1	15.7	15.5	14.9	15.3	15.7	15.2

Source: OECD. Non-Financial Enterprises/Financial Statements

each success story of the Neuer Markt there are many more stocks of SMEs on the main Frankfurt exchange that are still barely traded (*Financial Times*, 11 June 1999).

As concerns patterns of corporate governance, despite the stock market reforms initiated in 1992, bankruptcy law reform, and the debate over whether to reform the German corporate governance system, there appears to be relatively little change. Ownership remains highly concentrated. Despite much debate, there are still no limits on bank equity investment in nonfinancial firms and banks still play an important (though usually overestimated) role in corporate governance. And even as banks have divested themselves of, or diluted, their equity holdings in nonfinancial firms, other nonfinancial firms have been acquiring and/or building up equity stakes in each other.[2] Nor is Germany becoming a nation of individual shareholders: on net, the percentage of German equities held by German households continues its gradual long-term decline (Deutsche Bundesbank 1997, 36–39).

Extensive cross-shareholdings and a concentrated ownership pattern mean that corporate governance in Germany does not appear to be changing all that much. Hostile takeovers within Germany are still uncommon and there is not much of a market for corporate control in the Anglo-Saxon sense (though there has been a great amount of M&A activity in Germany since 1990). As several large German firms have been internationalizing their capital base, they have begun to talk about "shareholder value," a notion imported from Anglo-Saxon markets. Presumably this means management will give greater weight to maximizing share price than in the past, but such talk is limited to a relatively small number of large firms and does not correlate with higher amounts of equity finance nor a move to outsider governance. The traditional stakeholder "mentality" and reality (especially since there is still co-determination and comparatively strong labor organization) still prevails.

France

The French postwar financial system was dominated, even more so than the German, by the role of bank credit in corporate finance. Yet it was subject to a rather different framework of financial regulation. In contrast to the "privately organized" character of the German system, bank credit in France was made subject to an extensive framework of administrative controls that allowed state officials to channel credit to particular users and uses in accordance with criteria of indicative planning (see Zysman 1983; Loriaux 1991). As the system evolved in the decade after the war it came to be characterized by two circuits of privileged financing (a Treasury circuit, in which a portion of the financial systems resources were allocated directly by public institutions, and a special rediscounting circuit, in which banks were granted privileged refinancing terms on credits to selected users). These circuits were progressively expanded to cover a widening range of economic activities from the late 1950s to the 1970s. Equity markets, which had played a significant role in French corporate finance before World War II, on the other hand, were eroded by the state's cheap credit policies over the same period.

Although corporate finance was based overwhelmingly on bank lending, commercial banks (which were partially nationalized after the war) played hardly any role in corporate governance. During the postwar period, when they were the main source of corporate finance, they were "never really represented on the governing bodies of any companies and their role was often confined to a passive distribution of credit" (OECD 1997, 125). The role of coordinating investment across firms and sectors was played instead by state officials who were in control of the system of selective credit regulation.

This framework of financial regulation began to evolve in the mid-1970s as the main mechanism of regulation shifted from selective credit rediscounting to selective credit rationing (Cohen, Galbraith, and Zysman 1982; Loriaux 1991) in order to address the new imperative of fighting inflation. French officials nevertheless remained committed to the principle of selective regulation through the end of the decade. After the failure of the Socialist government's experiment with redistributive Keynesianism in 1982–83, however, the government undertook a radical overhaul of the financial system which involved three major elements: the dismantling of the framework of selective credit regulation; changes in banking regulation intended to facilitate a move toward a universal banking model; and a major revamping of capital markets (including the creation of a secondary market in smaller firm equity) meant to serve as an alternative source of long-term financing for firms. In addition, the French public sector, one of the largest in the OECD, has undergone a major process of privatization, altering the terms of corporate governance in a significant portion of large firms. The banking sector itself, which was fully nationalized by the Socialist government in 1982, has subsequently been partially re-privatized by conservative governments.

What effect has this regulatory overhaul had on the pattern of corporate finance and corporate governance in France? Although one of the ambitions of the 1984–1986 reform was to move toward a German-style universal banking system in which banks provided long-term finance and also played a central monitoring and coordinating role, this aim does not seem to have materialized. Instead, the major changes that can be observed in French corporate finance are a relatively large increase in the ratio of equity financing of firms (see Table 1), coupled with a much greater reliance on their own funds, and a significant rise in foreign ownership stakes (in particular by British and American investment funds) in large French firms. Although these changes have hardly ended the predominant role of bank credit in French finance, they do represent the single largest shift in the structure of firm financing among the four countries being considered here.

The increase in the proportion of equity financing in France might seem to fit the notion that international financial integration will produce a shift away from the insider model of corporate finance that favors stakeholders toward the outsider model, which is geared toward the interest of the short-term or minority shareholder. Some very recent developments do in fact seem to support such a notion. In the period since 1995 a number of large French firms have shed some of their cross-equity holdings in order to raise capital because cross-shareholders did not have the liquidity to support their investment plans. Simultaneously, some recently privatized firms have begun to allow independent directors on their boards in order to attract minority shareholders (Goyer 1997; OECD 1997, 128–131). Meanwhile, neither banks nor institutional investors have taken a lead in governance matters (OECD 1997, 117).

However, other aspects of the evolution of corporate governance in France contradict the notion of a shift toward an "outsider" model. At 14.5 percent in 1995, the proportion of equity issues in French corporate finance, although reflecting a larger increase than in the other three country cases, remained quite low by OECD standards. Indeed, equity issues represented a slightly larger proportion of the liabilities of nonfinancial firms in Spain and Italy in that year (see Table 1). The amount of cross-shareholdings by large industrial firms, which prevent radical changes in the control of enterprises and shield CEOs from short-term market pressures on the other hand, remained strikingly high in France (OECD 1997, 111). Moreover, this pattern of corporate finance was re-created in the newly privatized firms through state-selected hard-core shareholder alliances that linked the newly privatized firms into two major financial groups: one connected through Paribas, the other through Indosuez (Morin 1996; Goyer 1997). And it also appears to have been reasserted by other large firms which, after experiencing a dilution in their ownership in the first years after the financial reforms, reestablished stable cross-shareholdings following the 1987 crash (Hancke and Soskice 1996). As late as 1994, 58 percent of the ownership of shares was held by other nonfinancial institutions, and these cross-participations did "not enable the recently privatised companies to adopt a truly private system of corporate governance" (OECD 1997, 126).

Lastly, as concerns small- and medium-sized enterprises (SMEs), we see even less of a move toward the so-called outsider model. To be sure, French authorities have done more than authorities in Spain or Italy to give SMEs access to equity markets. Nonetheless, the amount of financing raised by established SMEs through such markets is very small. While France (along with Britain) has led other European countries in the creation of a venture capital market, that market also remains small compared to the United States, and the proportion of venture capital destined to startups was only 13 percent in 1996 (compared to 35 percent in the U.S.; OECD 1998).

French banks have also not taken up the challenge of becoming long-term creditors to French SMEs because they do not have the capacity to gather sufficient information or monitor the operations of small firms. Instead, the major trend in French SME financing since the mid-1980s has been toward a new kind of structure in which large French firms have increasingly taken on the role of mediators in the financial system. This mediation takes a number of forms: the large firms "directly support the small firms financially by lending to them or by assuming large parts of investment cost." In addition, "SME investments are written off in part through increased prices. Frequently, large firms also lend money to SMEs when they take over parts of production that the larger firms intend to outsource. When the venture turns into a true spin-off, the large firms forgive the entire loan or a large part it" (Hancke 1996, 20). Thus the combination of financial reform and competitive pressures on firms seems to be leading to the emergence of a new kind of internal capital market among firms rather than an "outsider" model of corporate governance.

Spain

The financial system of Spain in the postwar period resembled that of France in a number of important aspects. Bank credit displaced all other forms of financing to industry during the Franco regime's autarkic industrialization drive in the 1940s, and in the early 1960s the regime introduced a framework of selective credit regulation modeled directly on that of France at the same time it liberalized trade and introduced indicative planning. This led to the establishment of two major circuits of privileged financing (one through official credit institutions, the second by way of selective rediscounting) that, as in France, were progressively expanded to new users and activities. The one major difference from France concerns the character of the domestic banking sector, which in Spain remained almost entirely in private hands. The sector was dominated by seven private commercial banks that held extensive equity stakes in Spanish industry and that until the mid-1970s were able to act, in practice, as a state-sanctioned cartel (Pérez 1997).

Significant changes to this regulatory structure were advanced by a group of reformers anchored in the research service of the central bank in the course of the democratic transition of 1976–1978. Prior to the transition, special rediscount lines had been abolished and replaced by compulsory ratios that obliged banks to direct set proportions of their lending to designated users. In 1977, having overcome the hurdle of the first democratic elections, the reformers passed a major package of financial liberalization measures that set in motion the dismantling of the compulsory ratio, along with other measures intended to free the monetary authority from interference by other branches of the state. However, this radical credit deregulation was not accompanied by any assertive measures to reform the highly oligopolistic structure of the Spanish financial market. It would take more than a decade after the 1977 package before the modernization of the Spanish stock market was initiated and before foreign banks were allowed to compete on more equal footing in the Spanish credit market.

In spite of the postponement of structural market reforms in the 1980s, the prospect of European financial integration did set off changes in the Spanish financial sector at the end of the decade. The most notable of these changes was a wave of mergers among the Big Seven commercial banks that reduced their number to three large (BBV, BCH, and Santander) banks and one smaller bank (Popular). These institutions are still, along with a couple of large savings banks and the newly formed state banking group, Argentaria, the dominant players in the Spanish financial system.

What impact have these changes had on Spanish corporate finance and governance patterns? Spanish firms, like French firms, underwent a major process of debt reduction and a shift toward greater reliance on their own funds over the course of the 1980s as credit rates soared. However, reflecting the lack of, and later limits on, capital market reform, this reduction in debt financing was not accompanied by any significant increase in equity finance. In spite of two valuation booms (one following Spain's entry into the EC in 1986, another in the late 1990s) the equity markets remain a highly circumvented source of financing. Although stock market capitalization rose to 42 percent of GDP in 1996, the market in the 1990s has been dominated, even more than in the past, by financial sector shares, which accounted for 34 percent of the Madrid Stock exchange in 1998. A further 23 percent is accounted for by electric utilities, 14 percent by telecommunication firms, and 6 percent by construction firms. Other industrial and service firms account for only 18 percent of the market's capitalization (Bolsa de Madrid 1998). The private bond market, on the other hand, at 7 percent of GDP, also remains one of the smallest in Europe (European Commission 1997b).

While companies significantly reduced their reliance on debt during the 1980s, they did not benefit from the kind of improvement in lending conditions or expansion in alternative sources of financing that one might expect from financial liberalization. This is reflected in the high cost that Spanish companies continued to bear on their external financing through the end of the 1980s, even as the public deficit and inflation were radically cut (see Table 2). The other persisting characteristic of corporate finance in Spain is the very high proportion of short-term as opposed to long-term lending to firms. The proportion of short-term debt to total debt in the early 1990s ranged from around 82 percent for large firms to 75 percent of debt for very small firms (Calvo and Lorenzo 1993).

As concerns corporate governance, among large Spanish firms the most notable feature is the high density of interlocking directorships across sectors with the commercial banks at the center (Aguilera-Vaques 1998). However, the Spanish commercial banks have generally treated their industrial stakes as a way of capturing credit market clientele or as a way of raising extraordinary profits. Although they have long been invested in particular sectors, they have also made a habit of divesting from industry in economic downturns and later moving again into equity

TABLE 2
Apparent Rate of Interest on Financial Debt (ratio of financial costs to external financing) Manufacturing Industry

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
Germany	—	—	—	—	—	5.8	5.3	6.2	6.9	7.4	8.6	7.9	7.1
France	14.1	12.8	9.5	9.4	8.5	7.9	7.0	7.3	8.0	8.1	8.6	8.0	6.8
Spain	13.5	12.9	13.4	12.3	11.3	12.0	11.4	12.1	12.0	11.6	11.4	11.0	10.1
Italy	14.8	14.6	17.8	16.6	14.6	12.6	12.0	12.6	13.3	12.8	14.6	13.6	10.8
UK	10.0	7.6	4.8	5.1	4.2	3.6	3.8	5.8	7.4	7.4	6.4	5.1	4.5
US	—	—	1.0	1.1	1.1	0.6	0.7	1.4	2.1	3.0	7.2	4.0	1.2

Source: European Commission, *European Economy, Supplement A*, no. 2, 1995, and no.4, 1996

in a pro-cyclical fashion. They thus never adopted the strategic role of providing "patient" capital and promoting industrial competitiveness attributed to German universal banks. In fact, according to one recent study, firms in which banks hold a 5 percent share of ownership or more tend to be both more indebted and less profitable than firms that do not have a bank among its controlling shareholders (Cuervo-Cazurra 1997). Also, the sectors in which the banks have maintained their stakes have been those least exposed to foreign competition or where a return was assured in some other way (in particular, utilities and firms with majority public ownership). By contrast, banks have often stayed away from the more competitive and innovative sectors of the Spanish economy where multinationals and foreign investors have been key investors. On the other hand, the banks have recently gained an important share in the telecommunications sectors, acting as the hard-core shareholders selected by the government in the process of privatization.

The principal impression that emerges from the literature on SMEs (which are largely family owned in Spain, as in the other three cases) is the extreme difficulty that these firms have had in attaining investment finance at acceptable terms in Spain. Spanish SMEs depend heavily on bank finance in terms of external sources of finance, given the absence of a viable small firm equity market and the underdevelopment of the Spanish venture capital market (Calvo and Lorenzo 1993; OECD 1998, 138–142). Yet, under the extremely high credit rates imposed by banks in the 1980s, many firms that survived chose simply to avoid new debt and to restrict their investments to what they could finance from retained earnings. As a consequence Spain was, along with Britain, the only EU country where SMEs were better capitalized and less indebted than large enterprises in the early 1990s (European Commission 1997a). At the same time, we also see a move toward an internal financial market for SMEs in Spain that is analogous to developments in France. Thus, a significant share of short-term financing of Spanish SMEs in recent years has been coming from alternative sources to the financial system, that is, large companies that the SMEs supply (Calvo and Lorenzo 1993) and, in the case of family-owned firms, "intra-family informal investments" which represent "a significant and particularly flexible and less costly source of finance" (OECD 1998, 142).

Italy

The central hallmark of the Italian postwar financial system has been the heavy presence of the state. Public ownership is extensive and many banks have been highly politicized in terms of board appointments and credit decisions. Banks have tended to be viewed by public authorities as having a public interest rather than market function, and bank competition has been muted by restrictive regulation. A substantial portion of industrial lending has been subsidized and allocated according to political criteria, notably to stimulate investment in the South and depressed areas of the Center and North, and to finance the numerous state-owned companies (The Transformation 1997, 583). Unlike France and Spain, however, state credit allocation in Italy was not linked to the same sort of indicative planning. Moreover, the financial system was highly segmented and very decentralized, thus leaving Italy with comparatively small, localized banks.

For Italian nonfinancial firms, debt finance is comparatively high while equity finance is low (OECD 1995a, 70–71). As in the other three cases, a very high percentage of external debt is to banks,[3] and, as in Spain, a very high percentage of bank debt by firms is short-term (OECD 1995a, 72).[4] This is due largely to the fact that only special credit institutes have been allowed to do medium- and long-term lending, and their lending decisions were largely made by political and administrative bodies (The Transformation 1997, 595). SMEs often faced credit shortages, a high cost of borrowing, and heavy reliance on annually renewed overdraft facilities on current accounts (de Cecco 1994, 53).[5] As a result, few ordinary banks have the expertise to do long-term lending (Pradhan 1995). Although Italy has a very large bond market, this market has been overwhelmingly dominated by government debt and therefore has also failed to become a significant source of financing for firms (Pradhan 1995).

As with the other three cases, corporate governance practices in Italy also fit an insider rather than outsider model. In international comparison, share ownership in Italy is extremely concentrated. On average, the top five largest shareholders in a large firm hold 87 percent of its shares; more than half of listed firms are majority controlled by a single owner (OECD 1995a, 60–61). The stock market itself is, not surprisingly, very narrow—the five largest business groups accounted for 70 percent of the Milan Stock Exchange capitalization in the mid-1990s (Pradhan 1995). Cross-shareholdings are extensive and predominantly take the form of a pyramidal structure, enabling larger firms to control many smaller ones using relatively small direct equity stakes (though smaller companies are typically family owned).

Banks have not traditionally had equity stakes in nonfinancial firms and therefore do not perform a monitoring role in corporate governance. This is due to the relatively small size of banks compared to the large nonfinancial firms and tight restrictions on commercial banks holding equity and sitting on boards of nonfinancial firms (OECD 1995a, 73). Most firms have also tended to take loans from many different banks. Thus, while Italy is a bank-dominated financial system, relations between banks and firms are much more arms-length than in Germany (Cesarini 1994, 40). One notable exception is Mediobanca which, as a state-owned special credit institute, established a unique and powerful position as an investment bank with long-term lending and equity stakes in many firms. However, most big companies face little external control/monitoring, save for those firms operating within a group. There is also no real market for corporate control in Italy, since relatively few companies are listed and many of those shares are held long-term.

While some banking regulatory changes took place in the late 1980s, largely as a result of the First EC Banking Directive, major and more or less sustained regulatory and market change began only in 1990 with the so-called Amato Law. The Law, promoted in particular by the Bank of Italy and supported by most Italian banks, paved the way for public banks to be privatized, and was passed clearly in anticipation of financial market integration in Europe and the fear that large foreign banks would overrun much smaller Italian banks unless the latter consolidated extensively beforehand (Semler 1992; Desario 1994; Bank of Italy 1995, 174). Some important steps to reform the Italian securities markets have also been taken in the 1990s with the purported aims of lowering costs and increasing efficiency, combating insider trading, increasing the transparency of takeover deals, and protecting small shareholder interests. Other regulatory reforms have created the bases for an expanded role by institutional investors.

Another major element of regulatory reform was the comprehensive Banking Law passed in 1993. The Law was heavily shaped by EC directives, including the bank passport provisions, which significantly increased access of foreign financial institutions to Italy. This sweeping reform bill also manifested the desire among Italian financial officials to create a financial system resembling that of Germany and centering on close, long-term relations between universal banks and firms (Cesarini 1994). The new law permits ordinary banks to issue bonds and extend medium- and long-term credit, something previously reserved for special credit institutes. It also permitted qualified nonfinancial firms to issue commercial paper and long-term investment certificates in an effort to increase the availability of long-term funds to firms. The law also expanded the financial activities permissible for banks, including the ability to acquire stakes in nonfinancial firms. The Italian banking industry did not embrace many of these changes, especially those intended to stimulate securities markets (Onado 1996, 100). There was, however, little choice as most of this legislation was required by the EU. The Treasury and Bank of Italy, in contrast, welcomed the political opening created by the EU to modernize the Italian financial sector. These banking and securities market reforms were also partly a response to the fiscal problems of the Italian state and the anticipated need to cut public pensions, thus forcing Italians to rely more on private savings (and investments) for their retirement.

Recently these regulatory changes have begun to show some effect on corporate finance, as a number of Italian firms have begun to internationalize their capital sources and issue corporate bonds in Italy and in the Euromarkets (Latter 1998). The Italian mutual fund industry is growing and this is expected to stimulate more equity issues and bond issues (Marshall 1998). However, in spite of these recent signs of change, the stock and corporate bond markets have expanded only very slowly, partly because banks are not pushing their development. Neither can one speak of dramatic changes in firm financing patterns (Onado 1996; Esposito 1998). There has, as yet, been no significant increase in the aggregate role of equity finance for Italian firms (see Table 1). In 1998 the Italian stock exchange still only had about 200 listings with only 30 or so being fairly liquid. Even with several privatizations over the last few years and the efforts of the Treasury to create more small shareholders and increase transparency of ownership and control, concentration in ownership is still very high (Pradhan 1995). Voting trusts or informal coalitions are a traditional practice, and despite recent legislation it appears that this still occurs extensively in corporate governance.

In the last few years there has been a lot of merger activity among Italian banks and substantial concentration in the industry (Bank of Italy 1995, 142). Along with concentration there has been a substantial increase in bank competition. But with their new freedoms banks have been pumping up their loan volume and taking a more traditional portfolio approach to credit risk rather than real monitoring of firms (Cesarini 1994, 45–47). Neither have banks begun to assume significant equity stakes in firms and the monitoring role associated with such.[6] Thus it does not appear that banks and firms are moving systematically away from the more traditional situation in which the "bank–firm relationship in Italy is in most cases antagonistic, marked by contraposition, and is rarely one of true cooperation and trust" (Cesarini 1994, 48).

CROSS-NATIONAL OBSERVATIONS

Our observations of the four cases indicate that many of the predictions that would support the market-driven view of domestic institutional change in financial systems have not been materializing in Europe, in spite of the very large increase in cross-border capital flows that has taken place since 1987. It is not just that considerable divergence remains between the four European cases and, even more so, between the continental and Anglo-Saxon economies. More important, the changes we are able to observe (primarily in the area of financial regulation) do not seem to be producing any real convergence in the underlying institutional make-up of economies toward the equity-dominated/outsider model of corporate finance and governance. Indeed, in several cases, changes in financial regulation and in cross-border capital flows seem to have intensified efforts to ensure the control of insiders over firms and to limit the emergence of active markets in corporate control. On the other hand, we also do not see evidence of a successful move toward the alternative ideal-type of the German universal banking model.

We do see an increase in the size of equity markets in all four countries, but this increase has only a limited impact on corporate finance and corporate governance patterns. The increase is most significant in France, reflecting the efforts made by French authorities to expand the structure and financing available through equity markets. These efforts have also attracted foreign investors, so that by the late nineties, France had the highest level of foreign share ownership in the EU. However, despite the expansion and opening of French capital markets, the role that equity markets play in the external financing of nonfinancial firms remained quite limited in France in the mid-1990s. This is also true of Germany, where the proportion of shares in total liabilities of nonfinancial firms has actually been declining over the past decade and is now the lowest of the four countries. We also do not see a significant increase in the role of equity in Spanish corporate finance even though Spain underwent a similar credit deregulation process as France, nor, as of yet, in Italy. In both Spain and Italy firms continue to rely overwhelmingly on short-term debt rolled over by banks as a source of external finance.

This relative lack of change in corporate finance patterns is accentuated in the case of small firms. Small firms in France and Spain reduced their debt significantly in response to the high cost of bank financing in the 1980s and 1990s. But, in terms of their external financing sources, they continue to rely (along with Italian firms) very heavily on rolled-over short-term debt and, in second order, on internal capital markets (that is, on financing provided or mediated by larger firms or through informal personal or family connections) (Hancke and Soskice 1996; OECD 1998, 138–142). Only in Germany do small firms seem to have good access to long-term debt financing from banks, thanks to the pattern of close Hausbank relationships. This may explain why German SMEs are considerably more indebted than large German firms without any detrimental effect on their profitability (European Commission 1997a, 29). Though there has been a recent surge in some cases, we still see limits in the role played by venture capital markets. Again, France is ahead of the other countries in this area (with venture capital investments worth 0.06 percent of GDP in 1996, as compared to 0.03 in Germany, and 0.04 in Italy and Spain), but it is still far behind the U.S. venture capital market (0.13 percent of GDP), in particular as concerns the proportion of venture capital that is directed at start-ups (13 percent in France compared to 34 percent in the U.S.; see OECD 1998, 140–141). The number of IPOs in all four countries, while on the rise, also remains marginal.

Along with the lack of a more significant increase in the role that equity markets play in corporate finance, significant differences in the cost of external financing for enterprises have also continued in the 1990s, with Spanish and Italian firms bearing considerably higher costs than German and French firms (see Table 2). These differences cannot be explained by rates of inflation alone, since "interest rate differentials between EC Member States are more pronounced than the corresponding inflation differentials" and they seem to be even greater when it comes to SMEs. One recent background paper by the European Commission concludes that "considerable differences remain between the cost of credit [to SMEs] in various Member States," and that "SMEs have not yet reaped their share, in the form of cheaper bank finance, of the benefits expected from financial integration" (European Commission 1997b, 27).

Increased capital flows and changes in financial regulation thus appear to have had only a limited impact on patterns of corporate finance in Europe. But the prediction that the integration of capital markets will produce convergence toward the Anglo-Saxon model finds even less support as we move from corporate finance to other features of corporate governance. While there is much talk—and some action—about increasing standards of transparency in all four countries, there have been simultaneous moves to entrench the role of insiders. This is particularly evident in France. Despite an active domestic debate on the need to reform corporate governance, there have been no changes in French legislation to limit the power of the chief executive or to force companies to divulge key information on management practices (such as executive compensation) to investors. This inaction contrasts sharply with the sweeping changes imposed in the area of financial regulation by French governments in the 1980s and seems to reflect a determination by French government and business elites to prevent the emergence of an American-style market in corporate governance. Indeed tellingly, even the most vocal advocates of a shift to an Anglo-Saxon model of corporate governance within the French business community oppose calls by U.S. and U.K. investment funds to require firms to disclose key information on compensation and other management practices (see *Financial Times*, 23 July 1999). But, more importantly, the expansion of equity markets in France has actually been accompanied by very intense efforts to ensure the continuation of insider control over French firms. Not only have state officials made sure to create alliances of hard-core shareholders across privatized firms in order to prevent hostile takeovers. Large private companies have picked up where the state has left off by restoring stable cross-shareholdings that impede radical changes in the control of companies.

An analogous set of developments can be observed in the other cases. In Spain, the large banks have maintained their centrality in networks of interlocking directorships among large industrial, utilities, and telecommunications firms (Aguilera-Vaques 1998; Cuervo-Cazurra 1997). They have also been granted the role of hard-core shareholders in many privatized firms. In Italy, on the other hand, the pyramidal structure, whereby large companies are able to control many small companies, also persists. The privatization process has opened up ownership somewhat in the Italian case. But here too the state (with the help of the private investment bank, Mediobanca) has created a core of long-term shareholders who collectively control a substantial block of shares in recently privatized firms (see, e.g., *Financial Times*, 14 September and 15 June {Survey} 1998 on the privatizations of Telecom Italia and Banco Nationale de Lavoro, and 29 June 1999 on the restructuring of the shareholdership of Olivetti). Even the much publicized takeover battle of Telecom Italia by Olivetti in 1999 was settled only by the intervention of the Italian government, which threatened to use its golden share in the privatized telecommunications group to derail the alternative plan pursued by the firm's management for a merger with Deutsche Telecom (*Financial Times*, 6 May 1999). In Germany, too, we see relatively little change in corporate governance. While the banks have been somewhat reducing their role, most large firms are still controlled by the same core of large, long-term shareholders (Deeg 1999).

We also do not observe any significant dilution of ownership concentration patterns in any of the four countries. Some expansion of shareholdings is taking place as a result of investment by American and, more recently, European mutual funds, as well as a result of efforts by conservative governments in France, Spain, and Italy to create "nations of shareholders" by reserving portions of shares for small shareholders in the privatization process. However, this trend responds largely to political motivations (rather than international market pressures) and the same governments have simultaneously sought to give controlling shares in privatized firms to large, hard-core shareholders. The number of publicly listed companies in which the largest shareholder owned more than 50 percent of the stock thus remained at 50 percent in Germany, France, and Italy, and at 49 percent in Spain in the mid-1990s (Galve Gorriz and Salas Fumas 1993; OECD 1995b).[7]

The most notable feature of the evolution of corporate governance in the four European countries thus is the *reinforcement* of various "insider" models of corporate governance in the face of financial liberalization. The most visible example of this connection may in fact be the rush of mergers in the banking, telecommunications, and energy sectors that has followed the onset of EMU, almost all of which have reflected efforts by government and business elites to create national champions that are able to compete on a pan-European level or, at a minimum, are large enough to enter cross-border mergers as an equal partner rather than as a minnow to be swallowed by a larger fish (even when this has led to a resort to hostile takeovers, as in the case of the Telecom Italia–Olivetti merger and the recent battle to join the major French commercial banks). Although the argument might be made that these efforts represent simply a "last-stand" bid to prevent an inevitable loss of insider control over corporate governance, we see little evidence in support of such an interpretation in recent developments. The fact that foreign shareholdings have been increasing substantially even as structures of insider control have been reinforced seems itself to contradict the notion that the integration of financial markets will force firms to shift to an outsider model of corporate governance.

Along with the absence of a shift toward the Anglo-Saxon model of corporate governance, there is another outcome that requires explanation. As already noted, most of the convergence that we do observe is in the area of financial regulation. Along with the abandonment of state-directed credit allocation, there has been a move toward the "universal banking" model in banking legislation in the two countries—France and Italy—where commercial and investment banking had been kept separate in the postwar period.[8] All four countries now share the same basic model of banking legislation, and this model has been affirmed by the Second

Banking Directive which essentially eliminated barriers to universal banking throughout the EU. Taken together, these trends might indicate a generalized process of convergence in corporate finance and governance in the direction opposite to that stipulated in the liberal market view, that is, toward a generalization of the German model of bank-organized capitalism in which banks, or other institutional investors, provide long-term finance to firms on the basis of inside information and monitoring.

However, we do not see evidence of such an outcome, either. The German model was an important external referent in the financial reform efforts undertaken in France (Loriaux 1991) and Italy (Cesarini 1994; OECD 1995b). French reformers, in particular, appear to have envisioned that banks would play a strategic role in corporate finance and corporate governance as the state retreated from its traditional coordinating function in the French economy. However, neither French nor Italian banks have fulfilled this expectation. Although in both countries banks remain the most important source of financing for firms, their share of ownership in nonfinancial firms remains the lowest among banking sectors in Europe (OECD 1997). Indeed, in the one notable—and now infamous—case where a French bank sought to emulate the German universal banking model by purchasing large equity stakes in industry, Credit Lyonnaise, it fared very badly and was eventually forced to dispose of its industrial holdings. Moreover, in both France and Italy, banks have failed to take on the kind of central role in corporate governance associated with the German model even when they have been placed at the center of interlocking directorships of privatized firms. Neither have other institutional investors (insurance companies or mutual funds) taken on such a role (OECD 1997). In Spain, on the other hand, where the banking sector has historically had an important position of control in industry, banks have continued to treat their equity holdings in nonfinancial firms primarily as a means to capture clients and to attain extraordinary profits, eschewing the kind of long-term commitment associated with German banks (Pérez 1997). Lastly, in none of these three countries have banks taken up the role of providing long-term financing to small companies that lack access to equity markets as we see banks do in Germany.

In addition to the failure of convergence in corporate finance and governance toward the equity market–centered outsider model represented by the United States or, alternatively, a more successful emulation of the German model, we also note some important differences in the *processes* of regulatory reform in the four countries. One of these differences lies in the *extent* of change in the regulatory regimes of the four countries. The other concerns the *timing* of such change. Spain and France underwent major regulatory overhauls from the late 1970s to the mid-1980s. In both countries the old interventionist framework of credit regulation was abandoned and major changes in banking legislation were introduced. However, in France this abandonment of interventionism was accompanied by a major overhaul of financial market structures (the expansion of equity markets) whereas in Spain deregulation was placed ahead of market reform. In Germany and Italy, by contrast, change has been much slower to come. Only at the end of the 1980s and in the early 1990s do we see a significant amount of regulatory transformation in these countries; and, overall, a greater portion of the regulatory changes in Germany and Italy have responded to the need to comply with EC directives.

In summary, we observe a great deal of indeterminacy in the way that systems of corporate finance and corporate governance have been evolving in Europe, despite some apparently important elements of convergence in the regulation of the financial sector. We also observe some striking differences in the timing and patterns of regulatory reform in the four countries. These findings challenge the widespread belief that the integration of financial markets is the driving force behind contemporary regulatory developments, and that it will produce convergence in domestic market institutions.

EXPLAINING THE PATTERN: DOMESTIC FINANCIAL SYSTEMS AND THE POLITICS OF REFORM

What explains the differences we observe in the patterns of regulatory reform across the four countries and the failure of convergence in national systems of corporate governance toward the kinds of outcomes generally stipulated to follow from a market-driven process of change? The answer to these questions, we find, are to be found in the way in which the integration of financial markets affects, first, the politics of financial reform, and second, the behavior of firms, along with important elements of path dependence in the evolution of domestic institutions.

Political scientists who argue that the integration of financial markets is likely to result in converging domestic institutions have postulated two general kinds of domestic political processes whereby such convergence may take place. In one model, the principal agents of change are seen to be sectoral market actors (in particular, banks and other financial institutions) who want to maintain or bolster their ability to compete in international markets, or who are seeking to respond to the competitive pressures of foreign institutions and markets at home. Such actors actively lobby, or exert other forms of positive political pressure (voice) in favor of market-oriented regulatory reforms (Cohen 1989; Dollar and Frieden 1990; Moran 1991). In the second model, the pressures for financial liberalization and convergence are seen to be much broader and come in the form of uncoordinated market behavior (evasion and exit) by holders of liquid assets (not just financial institutions, but also savers and investors). In this latter model the agents of reform at the national level are political entrepreneurs (Frieden and Rogowski 1996) or public officials who seek to respond to these market pressures by creating more efficient domestic financial markets.

Only in Germany, among our four cases, do we see a process closely resembling the first of these two models. The reform of the stock exchanges and securities regulation was actively promoted by a coalition of large banks which sought to recapture lost business with large German multinationals and to make Frankfurt competitive with London and New York (Coleman 1996; Lütz 1998). In the three other countries, by contrast, the regulatory reform process has been overwhelmingly state-led, thus apparently resembling the second model. However, among these countries there are also significant differences that seem to challenge standard market-driven accounts. The timing with which reform is undertaken, for example, differs significantly, and these differences do not seem to respond to the intensity of capital flows, that is, international market pressures. The process of liberalization is undertaken first in Spain, in the midst of the political regime transition of 1976–1978, followed by France in the mid-1980s, and only in the early to mid-1990s do we begin to see a move to dismantle the mechanisms of state control over the financial system through the privatization of state-owned banks in Italy. Yet Spain was no more vulnerable to international capital flows or foreign creditors in the mid-1970s than France, or, for that matter, Italy. Moreover, as we have noted, in neither Italy nor Spain were financial markets reformed in such a manner as to make them more competitive or efficient until the arrival of the single European market in financial services in 1992 became imminent.

Another kind of contrast is important as well. While Spain and France underwent major regulatory overhauls prior to, and independently of, the EU process of financial integration, much of the change in financial regulation that has taken place in Germany and in Italy only really materialized once the EU-level process of European financial integration had been set in motion. One possible explanation for the contrast between the first three countries is that the Spanish and French regimes of selective credit regulation entailed greater allocative inefficiencies than the German system, which involved few state administrative controls and had been subject to free capital movements for a considerable time. This pattern of divergence would hence seem consistent with the notion that change in financial institutions is a function of the inefficiencies created by overregulation.

However, this apparent fit with the market-driven explanation dissipates once we look more closely at the cross-national pattern of reform and expand it to Italy. While both France and Spain abandoned interventionism prior to the launching of the process of EU financial integration, credit deregulation was only accompanied by serious reform of financial market structures in the case of France. The Spanish financial system remained highly oligopolistic until 1992, belying the primacy of efficiency-oriented international market pressures. On the other hand, the Italian financial system, although not subject to the same kind of selective credit regulation found in France and Spain, was hardly market-conforming in the 1980s. Indeed, a great deal of the credit extended by state-owned banks in Italy was subsidized and subject to direct political discretion (Nardozzi 1983). Yet, by contrast to France and Spain, Italy did not experience any substantial changes in its framework of financial regulation until the early 1990s.

If changes in financial systems are being driven by efficiency-oriented international market pressures, why was credit deregulation in Spain not accompanied by serious reform of financial market structures for more than a decade? And why did the Italian financial system not experience any substantial changes prior to the 1990s? Moreover, what explains the fact that sectoral actors (private financial institutions) played a driving role in the German process of financial reform but not in any of the other three countries?

An important part of the answer, we find, is that countries are susceptible to international pressures in different ways. The kind of domestic response to the growth of international financial markets characterized in the first of the two market-driven models (a process of reform instigated and pushed forth by financial market actors) is most likely to occur in countries whose domestic financial institutions either are significant players on international markets (the U.S., the U.K.) or are accustomed to operating in a relatively competitive domestic financial system and therefore are not as fearful of giving up existing regulatory and market structures. Within our four-country sample, only Germany fits this characterization.

Where financial institutions, in contrast, are accustomed to a protective regulatory structure and limited market-based competition, they are likely to be at best reluctant partners in a process of financial liberalization and, even more likely, to exert political pressures against radical reform of financial market structures. In such cases financial reform is more likely to be advanced by public officials. This in fact is what happened in Spain, France, and Italy. However, the experiences of these three countries suggest that the politics of such state-led financial reform also differ in important ways from the second model of market-driven reform, in which the principal criterion of reformers is that of creating efficient domestic market structures. Only in France, among the three cases, is there an assertive effort in the 1980s to approximate such an outcome. In Spain, credit deregulation is allowed to proceed in the context of an oligopolistic market structure, and only at the end of the decade, in anticipation of the Single European Market in Financial Services, is the reform process taken a step further with the reform of the stock market. In Italy, meanwhile, there is little change until the privatizations of state-owned banks in the 1990s and the adoption of EU directives into Italian law.

This divergence in the three reform processes conflicts with the notion that the growth of international financial markets in itself will induce governments to reform their domestic financial systems in a manner that leads to the creation of competitive and efficient domestic financial market structures. It reflects the fact that, in many cases, the principal way in which international financial integration impinges on governments involves not the microeconomic efficiency of domestic financial markets but rather the nature of macroeconomic policy (Pérez 1998). The financial reform efforts of Spain and France in the 1970s and 1980s were driven, in first order, by the desire of state officials to dismantle a regulatory framework that made it difficult to impose monetary austerity from a political standpoint. The framework of "selective credit regulation" adopted in the two countries in the postwar period had the effect of requiring public authorities to decide who would, and who would not, get credit at preferential rates when monetary policy was tightened. It thus forced elected authorities to decide who would bear the burden of monetary austerity, a position that carried considerable political costs.

By reducing the leeway for expansive monetary policies, international financial integration created powerful incentives for political authorities to dismantle such a regulatory framework. However, these incentives did not extend with equal force to other aspects of financial reform required to create competitive and efficient financial markets where in fact none existed. Indeed, given that major financial institutions in both countries were accustomed to the benefits of a protected and artificially apportioned domestic financial market, and given that the tightening of monetary policy that financial reform was intended to facilitate was likely to put pressures on the profitability of banks, we would expect there to be considerable pressures against an assertive approach to financial market reform. The problems of the French banking system, which were in fact exposed to a far more radical alteration of domestic financial market structures than Spanish banks, bespeak this tension in the reform process. The fact that French governments in the 1980s did pursue, nonetheless, a fairly aggressive pace of market reform renders this case more the exception than the rule. Such an outcome was, in any case, highly dependent on the fact that the French banking sector had been under the tutelage of the state since the 1940s and that its interests were therefore more easily subordinated to those of French nonfinancial firms by an overlapping network of state elites that was heavily invested in the competitiveness of French industry.

The primacy of macroeconomic constraints, rather than microeconomic efficiency, also helps us understand the Italian experience. One reason why Italy did not experience the same kind of state-led drive for financial reform in the 1980s that we see in France and Spain is that the postwar framework of financial regulation instituted in Italy, while entailing many obstacles to allocative efficiency, did not subsume the instruments of monetary policy (Pérez 1998). Although a great deal of credit was allocated in line with political criteria by state-owned financial institutions, this form of financial interventionism did not interfere with the Bank of Italy's ability to control overall monetary magnitudes. Thus, politicians in Italy did not face the same incentive to dismantle the existing framework of financial regulation that French and Spanish governments encountered. The first real impetus to alter the existing financial framework came instead by way of the pressures to address the fiscal crisis of the state and prepare for the EC-mandated opening of the relatively protected Italian financial industry. Only then did the state take the lead in reforming a reluctant Italian banking sector.

We find, therefore, that the principal impetus for financial system reform in all but the German case comes not from the search for allocative efficiency by market actors, but rather from the way in which increased international capital mobility impinges on macroeconomic policy institutions, and more specifically, on the political costs that those institutions have for governments. It is this element of the politics of regulatory change that accounts for much of the variation among our cases, and for the fact that the course of regulatory reform departs significantly (at least until the onset of the Single European Market in Financial Services) from the objective of creating more efficient domestic financial markets in at least two of our cases (Italy and Spain).

If the absence of incentives to create more efficient capital markets explains much of the variation we see in the patterns of financial reform, the question remains as to why financial liberalization has not induced a shift toward an outsider model of corporate governance within firms even where (or when) reforms have led to the emergence of more efficient capital markets. Part of the answer, to be sure, may simply be that most European firms are not so dependent on equity finance as to compel them to implement any changes in response to shareholder demands. The more important piece, however, may be that there is no compelling relationship between a firm's ability to raise equity finance and the nature of its management structure. Although there is a common presumption that investors have an interest in some form of direct control over companies, the principal factor driving investors into new markets (whether foreign or domestic) is the search for higher returns. Yet it is quite possible for governance structures that favor control by insiders to bolster the ability of firms to offer attractive returns.[9] Indeed, from an investor viewpoint, insider systems of control offer certain advantages and an ideal corporate governance system would probably include features from both insider and outsider systems (e.g., see Kester 1996).

There is evidence that rates of return on equity and other measures of economic performance are not as closely related to corporate governance structures as the proponents of the "market-driven convergence" thesis seem to assume. One recent study on the thirty largest listed German companies included in the DAX index, for example, shows that measures of shareholder value (such as listing on the New York stock exchange, the use of U.S. accounting standards, and stock options for managers) are not positively associated with profitability, nor for that matter with market share, even if they are associated with higher growth in share value (Vitols 1999).[10] Moreover, the very fact that foreign funds have been eager to invest heavily in countries such as France and Germany despite the dominance of an insider model of governance seems itself to suggest that such governance practices do not represent a major obstacle to the ability of firms to raise equity finance in an integrated financial market.

There remains, however, one other puzzle that arises from the experiences of our four countries: namely, the failure of convergence toward the alternate (German) model of bank-organized capitalism. We noted that there is a clear cross-national trend in banking legislation toward permitting single financial entities to engage in virtually all lines of financial business (whether as a single, universal bank or a holding company); a trend that has been enshrined in the Second European Banking Directive and that extends beyond the European context to the U.S. and, recently, to Japan. To the extent that most countries have removed—or are engaged in the process of so doing—barriers to universal banking, there is convergence. However, this change in banking legislation seems to have a surprisingly limited impact on patterns of corporate finance and corporate governance.

In two of our cases, France and Italy, state officials consciously set out to emulate the German model in the course of recent regulatory overhauls. They created the regulatory conditions under which banks could assume significant equity stakes in nonfinancial firms so as to allow them to emulate the German model, in which banks are able to provide long-term (or patient) investment financing by establishing a close relationship with firms and taking on a key monitoring role in corporate governance. Such a model would allow the state to dismantle the framework of state-directed credit allocation, but at the same time still enable domestic industry to be dominated by a core of stable national shareholders amenable to state influence. Similarly, Italian authorities have sought to exploit the political opening created by EC directives to reform the Italian banking system along the lines of the German model. They have encouraged newly privatized banks to take on the role of core, long-term shareholders in other privatized firms, and they have hoped that, with the removal of heavy restrictions on bank ownership of nonfinancial firms, banks would begin more exclusive and long-term relationships with Italian firms, especially SMEs which are less likely to gain access to equity markets (Cesarini 1994).

However, neither the French nor the Italian efforts to create German-style universal banking seem to have been successful. Indeed, in the French case, the effort to transform large banks into financiers and monitors of French industry has been a notable, and very costly, failure. In the Italian case it may simply be too early to tell, since the requisite reforms have been so recent. But even here early developments do not indicate there will be any rapid or certain movement. Large Italian banks have mostly been engaged in the process of consolidation and only a few seem interested in taking major stakes in large privatized firms. Moreover, as noted earlier, in neither country do we see a secular increase in long-term lending to firms—the hallmark of universal banking in Germany. Nor do we see such a pattern in Spain, where universal banks with extensive industrial holdings have existed since the early part of this century.

Why has the convergence in banking regulation not led to more convergence in corporate finance and corporate governance patterns? We can explain this outcome, at least in part, in terms of institutional path dependence. For the German system to work as it does, a wide range of institutional and regulatory factors must be in place—from bank regulation to tax codes to bankruptcy laws—that encourage and sustain this kind of bank–firm relationship. Moreover, German banks ended up holding substantial equity in nonfinancial firms frequently not so much by choice but by force of historical circumstance, for example, the Depression and early postwar reconstruction eras (Deeg 1999). The confluence of these conditions led German banks to develop internal organizational structures that could support their wide-ranging monitoring role in the economy. The fact that the regime of banking regulation in and of itself is not sufficient to produce such an outcome is illustrated by the comparison with Spain, where the large universal banks invested predominantly in oligopolistic or protected sectors that offered high profits opportunities and did not play the strategic role in helping companies to adjust to new market conditions generally attributed to German banks (Pérez 1997). It is also illustrated by the failure of the German banks themselves to make firm commitments in the economic transformation of the former East Germany, where many of the broader institutional conditions existing in the West were missing (Griffin 1994).

While the framework conditions have been set for French and Italian banks to move toward German-style universal banking, there are other market strategies open to them that are likely to be profitable and do not involve such close relations to firms. Given their lack of experience with universal banking, it seems probable that they will continue to follow more traditional relations and practices. Indeed, even in Germany large banks have been reducing their risk shareholdings in individual large firms as German firms have become financially more autonomous (Deeg 1999).

The failure to emulate the German model is likely to be particularly acute precisely where it is most needed, that is, in the financing of SMEs, which account for an extremely large share of economic activity and employment in the French, Spanish, and Italian economies. These firms generally do not avail themselves of the new equity and international finance opportunities because they are too small to use them efficiently or cost effectively, or because they prefer not to give up control. Foreign financial institutions are also generally not going after their business because the high cost of gathering information does not make it profitable for them (European Commission 1997a). Thus, systems of financing for SMEs are somewhat sheltered from international pressures and traditional patterns of finance largely continue. It is also important to note that, in the German case, the provision of long-term bank finance to SMEs is a job borne primarily by smaller public savings and cooperative banks. Indeed, the German small firm financing model is largely a political creation involving semi-public institutions that reflects a historic, and ongoing, effort on the part of the state to have a competitive banking market at that level (Deeg 1999). Change in this area thus really depends on whether a distinct political commitment is made to alter the financial environment for SMEs and whether this has been backed up with systematic efforts to realize these objectives.

Simply clearing the path to bank competition and universal banking thus does not inevitably produce specific changes in firm financing behavior, inter-firm relations (in terms of equity ownership and corporate governance), or bank strategies and capacities. Creating the regulatory conditions for German-style universal banking, with all its presumed advantages, therefore, is not likely to lead to such a financial system any more than the rise in international capital flows is likely to produce, by itself, efficient and adequate domestic equity markets.

CONCLUSION

What general lessons can we extract from the recent evolution of domestic financial and corporate governance systems of the four European countries examined here? The first important lesson we are able to draw is that, although the growth of international financial markets does seem to yield a certain degree of convergence in financial regulation, this element of regulatory convergence does not invariably induce (independently of European directives, in our cases) the creation of more competitive and efficient market structures. We have explained this by arguing that the politics of financial reform differ from the models that are commonly stipulated by exponents of the market-driven convergence view. Where there is already a fairly competitive domestic financial market environment, the kind of process envisioned by those authors appears most likely. However, in cases where this condition does not hold, financial market actors are unlikely to be the main agents of change. In these cases state elites, sometimes driven by external political pressure (such as EC/EU directives), are more likely to push reform. But the pressures faced by state elites are foremost those on the character of macroeconomic policy. In several cases financial markets were reformed only to the extent that they related directly to those pressures, and were not necessarily driven by the objective of greater microeconomic efficiency.

If increased cross-border capital flows thus do not appear to transform domestic financial systems in a manner that would concord with the market-driven convergence view, there is even less evidence that they have the kind of impact on patterns of corporate governance suggested by proponents of that view. Our review of corporate governance patterns in the four European cases offers little support for the view that the liberalization and integration of financial markets leads invariably to the adoption of an outsider model of corporate governance. Part of the reason for this may be that European firms simply are not dependent enough on equity finance to compel a move toward an outsider model of corporate governance. However, just as important, we estimate, is the fact that the ability of firms to attract capital depends foremost on their ability to provide the necessary levels of profitability and returns to investors rather than on corporate governance practices and ownership patterns. European firms appear, in any case, to have been able to attract a great deal of foreign capital even as they have (with the collaboration of national financial institutions and governments) moved to entrench an insider model of corporate governance through the intensification of cross-shareholdings and the creation of national champion firms, in order to prevent an overly active market in corporate control.

The effect of financial integration on patterns of corporate finance and governance thus appears to be both more shallow and far less determinate than advocates of the market-driven convergence thesis would have it. In addition, we find that there is a great deal of path dependence in the evolution of national systems of corporate governance. For various reasons well-discussed in the institutionalist literature, institutions are sticky, and this has proven to be the case in financial systems as well, despite the overwhelming transformative capacity attributed by many observers to international capital mobility.[11] We do not see a strong shift to equity finance and the outsider model of corporate governance (even in France, where the increase has been the largest), nor do we see efforts to emulate the German model succeeding. Systemic convergence in underlying patterns of corporate finance and corporate governance remains elusive. Moreover, to the extent that we can observe a general pattern of change, it is in the increased reliance of small firms on new kinds of internal capital markets among firms, rather than a generalization of the outside model of corporate governance.

Lastly, it should be noted that considerable change in EU financial systems is likely to follow with the implementation of monetary union, which will increase the liquidity of European securities markets and make pricing of financial products more comparable. Indeed, EMU is likely to constitute a greater competitive shock to national financial systems than the lifting of capital controls and of barriers in banking and financial services. However, it is important to differentiate such future effects theoretically from those of international financial market arbitrage, as monetary union is a phenomenon that has been driven and determined largely by political decisions and motivations. Moreover, while EMU may lead to a further integration of securities markets and expand financing sources for large European firms, it is less clear that it will produce convergence toward either of the alternative "best practice" models of corporate finance and governance (the equity-market based/outsider model or the German model of bank-mediated and monitored provision of patient capital). If there is one notable common trend across our four cases, it is the efforts of governments and business elites to maintain the control of insiders (stable core shareholders) in corporate governance. Yet, as we have seen, these efforts do not necessarily produce the kinds of positive effects in corporate governance traditionally associated with the German case. It remains to be seen, therefore, what kinds of effects a further integration of

European capital markets may have on patterns of corporate governance and finance. The preceding analysis suggests that those effects may well be less uniform and profound than the market-driven convergence thesis would lead us to expect.

Notes

1. The German section draws heavily on this source.
2. At the end of 1995, 42.1 percent of all shares in circulation in Germany were held by nonfinancial firms; this compares to nearly 60 percent in France and 15 percent in the U.S. (Deutsche Bundesbank 1997, 29).
3. In 1995, 81 percent of lending to firms in Italy was done by banks; compared with 77 percent in Germany, 73 percent in France, 56 percent in U.K., and 22 percent in the U.S. (Thomas 1998).
4. In 1992, 84.7 percent of bank loans were short-term (less than 18 months [Cesarini 1994, 32–36]). However, it was also common practice among banks to repeatedly renew short-term credits without loans being earmarked for specific uses in firms, thus to some extent overcoming the lack of long-term financing (OECD 1995a, 77).
5. With closer ties to cooperative banks, SMEs in industrial districts often fared better. SMEs tied to large business groups also borrow from partners in the group (OECD 1995a). There is also very little venture capital (Mondello 1994, 202–203).
6. Though many smaller Italian banks apparently want to emulate the German hausbank model and are starting up corporate financial services for SMEs (Jewkes 1997).
7. Pedersen and Thomsen (1997), in a study of ownership patterns in twelve European countries, also find striking differences across national markets.
8. Legislation separating commercial and industrial banking was also introduced in Spain in the 1960s, but it was qualified in ways that allowed the large commercial banks to maintain their equity holdings and to expand these holdings by creating industrial bank subsidiaries. The separation of commercial and industrial banking was abolished in the 1970s, but it had never truly taken effect (see Pérez 1997, 80–83).
9. In the case of Germany, for example, it has often been argued that firms closely associated with banks have had greater profitability than firms without such an affiliation (though other recent studies question this conclusion). For discussion of this debate see Deeg 1999.
10. The study also finds that capital market pressures are not the factor driving some companies in Germany to adopt shareholder value, but that such change is primarily reflective of product market strategies chosen by some managers, and that one of the common arguments offered for adopting a "shareholder" value approach is precisely that measures from capital markets are inadequate and that one needs to create internal constraints through "shareholder value" principles (Vitols 1999, 8).
11. For further discussion of path dependence in financial systems see, for example, Deeg 1999; OECD 1995b, 29–31.

References

Aguilera-Vaques, R. 1998. Directorship Interlocks in Comparative Perspective: The Case of Spain. *European Sociological Review* 14(4):319–342.

Allen, F. 1993. Stock Markets and Resource Allocation. In *Capital Markets and Financial Intermediation*, ed. C. Mayer and X. Vives. Cambridge, England: Cambridge University Press.

Bank of Italy. 1995. *Annual Report*. Rome.

Banuri, T., and J. B. Schor, eds. 1992. *Financial Openness and National Autonomy: Opportunities and Constraints*. Oxford: Clarendon Press.

Berger, S., and R. Dore, eds. 1996. *National Diversity and Global Capitalism*. Ithaca, NY: Cornell University Press.

Bolsa de Madrid. 1998. (www.bolsamadrid.es)

Calvo, J. L., and M. J. Lorenzo. 1993. La estructura financiera de las PMEs manufactureras espanolas. *Economia Industria*, n. 293:37–44.

Cesarini, F. 1994. The Relationship Between Banks and Firms in Italy: A Banker's View. *Review of Economic Conditions in Italy* 48:29–50.

Cohen, B. J. 1989. European Financial Integration and National Banking Interests. In *The Political Economy of European Integration: States, Markets, and Institutions*, ed. P. Guerrieri and P. C. Padoan. London: Wheatsheaf.

Cohen, S. S., J. Galbraith, and J. Zysman. 1982. Rehabbing the Labyrinth: The Financial System and Industrial Policy in France. In *France in the Troubled World Economy*, ed. S. S. Cohen and P. A. Gourevitch. London: Butterworth.

Coleman, W. D. 1996. *Financial Services, Globalization and Domestic Policy Change: A Comparison of North America and the European Union*. London: Macmillan.

Cuervo-Cazurra, A. 1997. Large Shareholders and Private Benefits: The Relationship Between Bank Shareholdings and the Capital Structure and Performance of Firms in Spain. Paper presented at the Harvard Center for European Studies, Cambridge, Mass. October.

de Cecco, M. 1994. The Italian Banking System at a Historic Turning-point. *Review of Economic Conditions in Italy* 48: 51–67.

Deeg, R. 1999. *Finance Capitalism Unveiled: Banks and the German Political Economy*. Ann Arbor: University of Michigan Press.

Deeg, R., and S. Lütz. Forthcoming. Internationalization and Financial Federalism —The United States and Germany at the Crossroads? *Comparative Political Studies*.

Desario, V. 1994. The 1993 Banking Law: The New Configuration of Supervisory Controls. *Review of Economic Conditions in Italy* 48:175–190.

Deutsche Bundesbank. 1997. Shares as Financing and Investment Instruments. *Monthly Report of the Deutsche Bundesbank*, January, 27–40.

Dollar, D., and J. A. Frieden. 1990. The Political Economy of Financial Deregulation in the United States and Japan. In *Structural Change in the American Financial System*, ed. G. Luciani. Rome: Fondazione Olivetti.

Esposito, P. 1998. Securitization. *International Financial Law Review* (Supplement, "Italy: A Legal Guide"), April, 43–47.

European Commission. 1997a. Financial Situation of European Enterprises. *European Economy, Supplement A* n. 7 (July).

European Commission. 1997b. Advancing Financial Integration. *European Economy, Supplement A* n. 12 (December).

Frieden, J. A., and R. Rogowski. 1996. The Impact of the International Economy on National Policies: An Analytic Overview. In *Internationalization and Domestic Politics*, ed. R. O. Keohane and H. Milner. New York: Cambridge University Press.

Galve Gorriz, C., and V. Salas Fumas. 1993. Analisis de la Estructura Accionarial de la Gran Empresa. *Revista Espanola de Economia Aplicada* II(4):75–102.

Garrett, G., and P. Lange. 1991. Political Responses to Interdependence: What's Left for the Left? *International Organization* (Fall):539–564.

Gerschenkron, A. 1962. *Economic Backwardness in Historical Perspective*. Cambridge, MA: Harvard University Press.

Goodman, J. B., and L. W. Pauly. 1993. The Obsolescence of Capital Controls? Economic Management in an Age of Global Markets. *World Politics* 46:50–82.
Goyer, M. 1997. The Reality Check That Bounced Back: Privatization and Corporate Governance in France." Paper presented at the Annual Meeting of the American Political Science Association, Washington, D.C.
Griffin, J. R. 1994. Investment and Ownership in a Volatile Economy: Big Banks and the Case of the East German Economic Transition. *Politics and Society* 22:389–420.
Hancke, B. 1996. Industrial Reorganization in France: Changing Relationships Between Large and Small Firms. Discussion Paper # FS I 96–301, Wissenschaftszentrum Berlin für Sozialforschung (Berlin, Germany).
Hancke, B., and D. Soskice. 1996. Coordination and Restructuring in Large French Firms: The Evolution of French Industry in the 1980s. Discussion Paper #FS I 96-303, Wissenschaftszentrum Berlin für Sozialforschung (Berlin, Germany).
Jewkes, S. 1997. Italy's Merchant Banks Take Stock. *Europe* (July / August):20–21.
Kester, K. 1996. American and Japanese Corporate Governance: Convergence to Best Practice? In *National Diversity and Global Capitalism*, ed. S. Berger and R. Dore. Ithaca, NY: Cornell University Press.
Latter, E. 1998. On the Road to a Credit Market. *Euroweek*, 12 June.
Loriaux, M. 1991. *France After Hegemony: International Change and Financial Reform*. Ithaca, NY: Cornell University Press.
Lütz, S. 1998. The Revival of the Nation-State? Stock Exchange Regulation in an Era of Globalized Financial Markets. *Journal of European Public Policy* 5:153–169.
Marshall, J. 1998. La Dolce Vita. *Global Investor*, May.
Maxfield, S. 1997. *Gatekeepers of Growth: The International Political Economy of Central Banking in Developing Countries*. Princeton, NJ: Princeton University Press.
Mondello, A. 1994. The Relationship Between Banks and Firms: An Industrialist's View. *Review of Economic Conditions in Italy* 48:191–205.
Moran, M. 1991. *The Politics of the Financial Services Revolution: The USA, UK and Japan*. New York: St. Martin's Press.
Morin, F. 1996. Privatisation et dévolution des pouvoirs: le modèle français du gouvernement d'entreprise. *Revue Economique* 47:1253–1268.
Moses, J. W. 1994. Abdication from National Policy Autonomy: What's Left to Leave? *Politics and Society* 22(June):125–148.
Nardozzi, G. 1983. *Tre sistemi creditizi*. Bologna: Il Mulino.
OECD. 1992. *Bank Profitability: Statistical Supplement, 1981–1990*. Washington, DC: OECD.
OECD. 1995a. *OECD Economic Survey: Italy, 1994–95*. Washington, DC: OECD.
OECD. 1995b. Financial Markets and Corporate Governance. *Financial Market Trends* 62(December).
OECD. 1997. *Economic Surveys: France*. Washington, DC: OECD.
OECD. 1998. *Economic Surveys: Spain*. Washington, DC: OECD.
Onado, M. 1996. The Italian Financial System and the Challenges of the Investment Services Directive. *Review of Economic Conditions in Italy* 50:89–103.
Pedersen, T., and S. Thomsen. 1997. European Patterns of Corporate Ownership: A Twelve-Country Study. *Journal of International Business Studies* 28:759–778.
Pérez, S. A. 1997. *Banking on Privilege: The Politics of Spanish Financial Reform*. Ithaca, NY: Cornell University Press.
Pérez, S. A. 1998. Systemic Explanations, Divergent Outcomes: The Politics of Financial Liberalization in France and Spain. *International Studies Quarterly* 42(4):755–784.
Porter, M. 1992. Capital Disadvantage: America's Failing Capital Investment System. *Harvard Business Review* (September / October):65–82.
Pradhan, M. 1995. Privatization and the Development of Financial Markets in Italy. *Finance and Development* 32(4):9–20.
Scharpf, F. W. 1991. *Crisis and Choice in European Social Democracy*. Ithaca, NY: Cornell University Press.
Semler, P. 1992. Italy: Save Our Sweeteners Say Bankers. *Euromoney* (September):263.
Story, J., and I. Walter. 1997. *Political Economy of Financial Integration in Europe: The Battle of the Systems*. Cambridge, MA: MIT Press.
Thomas, G. 1998. EMU a Panacea for Corporate Issuance. *Corporate Finance*, May.
Thompson, J. K. 1998. Shareholder Value and the Market in Corporate Control in OECD Countries. *Financial Market Trends*, February.
The Transformation of the Financial Markets. 1997. *Review of Economic Conditions in Italy* 51:577–599.
Vitols, S. 1999. The Reconstruction of German Corporate Governance: Capital Market Pressures or Managerial Initiatives? Paper presented at the Conference on the Political Economy of Corporate Governance in Japan and Europe, Robert Schumann Centre (European University Institute). June.
Zysman, J. 1983. *Governments, Markets, and Growth: Financial Systems and the Politics of Industrial Change*. Ithaca, NY: Cornell University Press.