The Changing Institutions of Governance in Corporate France: What Drives the Process?

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Abstract

Since the middle of the nineteen-eighties, the French system of corporate governance has undergone some major transformations. Originally, it was dominated by the State's important weight in the structures constraining managerial discretion in some of France's largest firms. But, the public administration has increasingly retired from its active role in corporate governance matters. This paper addresses the question of a theoretical explanation of the observed phenomenon of the dynamics of governance. The conceptual framework we propose is to a great extent based on the economic theory of institutional change. It strongly emphasizes the role of so-called 'organizational entrepreneurs', who lead the initiative aiming at a transformation of existing structures. In this context, a country's shared mental pattern is, however, supposed to be a force enhancing path dependence. Theoretical propositions are deduced and applied to the case of the French corporate governance system. The analysis of the latter's evolution yields some encouraging results, indicating that the proposed theory seems globally consistent with empirical facts.

Descriptors: Corporate Governance, Financial Policy, Institutional Change, Mental Patterns.

Introduction

A corporate governance system consists of a set of mechanisms which restrict managerial discretion, that is to say the CEO’s field of action (Charreaux 1997). In doing so, the instances of governance achieve an alignment of managerial behavior with the interests of different types of stakeholders, such as stockholders, financial intermediaries, employees, suppliers, clients, and the State. Mainstream explanations of corporate governance standing in the tradition of agency theory commonly focus on suppliers of financial capital (Shleifer and Vishny 1997: 737), whereas the more recent institutional literature interested in explaining cross-border differences in corporate governance equally considers other stakeholder categories (Aguilera and Jackson 2003). In fact, when examining the practice of governance in real context, one observes the existence of substantial differences in systems across national borders. There now exists a certain number of comparative studies traditionally opposing the Anglo-Saxon to the German and/or Japanese systems of corporate governance, supposedly representing polar types (Aoki 1994; Hall and Soskice 2001; Porter 1992). The constraints on managerial discretion in the Anglo-Saxon environment are traditionally described as being primarily driven by shareholder interests, whereas the Japanese and German systems are thought of as more stakeholder oriented (Guillén 2000, Schneper and Guillén 2002). Yoshimori (1995) makes an empirical investigation concerning a national philosophy’s answer to the following question : « In whose interest should the firm be managed ? » (Yoshimori 1995: 33). His study identifies three different concepts of the firm: monistic (Anglo-Saxon), dualistic (German) and pluralistic (Japanese), where monistic means focus on shareholder interests, dualistic includes employees’ interests and pluralistic refers to multiple stakeholders.

In a way consistent with this observation concerning the underlying “philosophy”, the control instruments at the disposal of different stakeholders that are to achieve the interest alignment are traditionally characterized by the important weight of the financial market in Anglo-Saxon countries and by more relational control instances in Japan and Germany (Berglöf 1997; Franks and Mayer 1990; Hall and Soskice 2001; Moerland 1995; Porter 1992; Schneper and Guillén 2002).

The comparative literature is rich of relatively static descriptions of national corporate governance systems. These studies are useful in order to highlight the existing differences between countries and to appreciate the historical roots of the different systems. However, they obscure the fact that, as a phenomenon of social interaction, corporate governance systems are dynamic and thus evolve over time. Signaling the need for a better understanding of its processual characteristics, Jensen (1993) describes the example of the American system, inside of which the weight of the capital market has experienced several changes over a long time horizon (Jensen 1993: 850-852). This study suggests some future research perspectives aiming, among other things, at an improved understanding of “how politics, the press, and public opinion affect the types of governance, financial, and organizational policies that firms adopt” (Jensen 1993: 872). In other words, what is needed is the development of a theoretical explanation of the active influence of different agents on governance mechanisms. Thus focusing on the active role of certain organizational leaders, be they politicians, journalists or managers, enables the researcher to address the determinants of the dynamic process constantly reshaping the incentive and control mechanisms to which a CEO is subject.

In fact, even though some researchers explicitly recognize the dynamic nature of corporate governance systems – Berglöf (1997: 105) observes a French system *in transition* – those accounts are often very descriptive, lacking a theoretical explanation. At best, what is proposed are different scenarios of the future development of the different national systems of corporate governance. Such a perspective is adopted by Aoki (1994), who studies the attributes of the Japanese and the "Western" settings. He presents four paths of evolution that can be imagined *ex ante*. These scenarios range from (A) "a convergence of financial attributes", (B) possibly "destabilizing effects" on polar and internally consistent systems by the interpenetration of particular attributes, and (C) the dominance of the attributes of a single system, to (D) the convergence "to a hybrid form of higher order". It should be noted, though, that more recently some progress has been achieved in gaining a better understanding of the dynamics underlying changes of various national systems (Aoki 2001; Dore et al. 1999; Lazonick and O'Sullivan 1997).

Our own paper tries to address the issue of the dynamics of corporate governance by applying the concepts of the broader theory of institutional change, such as proposed by D. North (1990; 1993), to the particular case of the mutations of the system of corporate governance in France. Studying the latter has two distinct advantages. First, researchers have, so far, paid less attention to the French system than to the supposedly polar cases of America and the United Kingdom on the one hand, and Germany and Japan on the other. Hall and Soskice (2001) explicitly recognize that they have some difficulty in accounting for a case like France by applying their conceptual framework. Hence, a description of the distinctive characteristics of France is likely to refine our empirical knowledge of international differences. Second, since the middle of the nineteen-eighties, the French corporate governance system has experienced several major transformations. We have thus chosen an especially well suited case to illustrate theoretical assumptions concerning institutional dynamics. The remainder of this paper is structured as follows. The first section gives a brief descriptive account of the basic features of the French system of corporate governance as well as of its most significant transformations. Section 2 summarizes North's theory of institutional change and attempts an application to the special issue of corporate governance. It deduces a certain number of theoretical propositions. The last section then confronts these propositions with the reality of the French case, in an attempt to ascertain the acceptability of the theoretical framework when it comes to explaining real-world phenomena.

The Quest for a Deeper Understanding of the Dynamics of the French Corporate Governance System

For the last twenty years, the French corporate governance system has undergone some major transformations. In order to fully appreciate their impact, it is however important to know the historical origins of French style corporate governance.

The Historical Roots of French Corporate Governance

Traditionally, the French attitude towards business distinguishes itself from a monistic representation of the firm, that is to say one that would be exclusively focused on shareholder interests. In fact, in 1995, Marc Viénot, a former CEO of one of France's most important banks, published a report on corporate governance which benefited from widespread attention in the French business community. It stipulates the "obligation" of the board of directors "to act in all circumstances in the *social interest* of the firm" (Viénot 1995: 6, our translation, italics added). The report then goes on to explicitly distinguish this perspective from an approach purely guided by the maximization of shareholder value (Viénot 1995: 9). According to Peyrelevade (1998: 31), a long-time CEO of formerly state-owned Crédit Lyonnais, the concept of the firm which underlies the Viénot report reflects the opinion of the majority of managers in France. Traditionally, in the French public opinion, "profit has a bad smell" (Lesourne 1998: 103). As a consequence, in spite of claiming the maximization of profits for shareholders, the dominant ideology favors "the prosperity and the continuity of the firm" (Peyrelevade 1998: 39).

The preceding paragraph indicates that the traditional French "philosophy" of the firm takes into account the interests of multiple stakeholders. In this context, what are the governance mechanisms *perceived* to be able to guarantee the respect of the dominant ideology's interests? In fact, the French tradition designates the State as the best suited actor in order to assure the alignment of all economic decisions with the previously described philosophy of value. According to Albert (1991: 266), France has cultivated "social colbertism" for a long time. The same author summarizes this doctrine, referring to Colbert, a very influential minister under France's absolutistic monarch Louis XIV, as follows: "the State [...] commands the economy in the name of a political ambition and of a strive for social progress" (Albert 1991: 266, our translation). From this perspective, the State's role is perceived as one of a referee between the demands of different stakeholders. It "acts in place of the economic and social actors" (Les Echos 11/17/1998, our translation). In doing so, the State is considered to be a "protector who assures redistribution according to the republican principle of *égalité*" (Les Echos 11/17/1998, our translation).

It is important to emphasize that the control instruments of quite different corporate governance systems are theoretically consistent with a pluralist approach of the firm. Why, then, does the French tradition assign such a central role to the State in spite of privileging the mechanisms of direct negotiation between different stakeholder categories? One factor which is likely to contribute to an answer is the existence of very polarized interests in France. In fact, French trade unions are traditionally characterized by a "class-fight ideology" (Albert 1991: 268, our translation). Hence, there is a tendency towards adopting extreme opposite positions. This may partially explain the polarization of the interests of different stakeholder types. According to Peyrelevade (1998: 32), the notion of compromise often has a negative connotation. Knowing this, it is easily understood why the State plays the role of a referee. In fact, since direct compromise between certain stakeholder groups is problematic, the structuring of mutual relations necessitates the aid of a "superior" instance. The latter's position happens to be occupied by the State. Unlike the approach of certain other countries, the French State “is not [...] a simple instrument of social administration at the disposal of the citizens. It transcends the individuals and receives of the latter a sort of divine blessing, comparable to the one the monarchs received in the past” (Lesourne 1998: 92, our translation).

France’s traditional concept of the firm is thus based on a “profoundly anti-liberal instinct of a large part of the French opinion” (Les Echos 11/16/1998, our translation). This opinion refuses to consider a company as a tradable merchandise among others (Albert 1991: 280). Traditionally, free market mechanisms are regarded rather suspiciously, and there is a belief in the benefits resulting from the State’s role as an organizer of economic activity. According to this reasoning, the State must intervene in order to eliminate suspicions of private benefits primarily destined to financial investors. Denis Kessler’s statement (Les Echos 11/20 and 11/21/1998) seems to be quite significant: “Historically, the two great nationalized sectors were banks and insurance companies; *firms making money business simply had to be state owned*” (our translation, italics added).

In a manner consistent with the philosophy outlined above, the corporate governance system defining the limits of managerial discretion of a substantial fraction of the most important French corporations was characterized by the State’s strong influence during a significant lapse of time. In fact, in the past, this influence was exercised at least at four different levels. (1) Industrial politics sometimes led the State to interfere directly with certain important firms’ corporate strategies. (2) Its control over the financial circuit was a significant vehicle of influence. (3) The governance structures of the nationalized corporations, which included a certain number of “champions” of the domestic industry, depended directly on government decisions. (4) And, finally, a significant part of the managerial elite owed (and still owe) their education and first professional experience to the public administration.

At the end of the nineteen-forties, a certain number of reforms translated into legal rules the perception according to which the State had the privilege of efficiently organizing economic activity. This exerted a more or less direct influence on the managerial discretion in big corporations. In fact, in sectors considered to be strategic, the State conducted several nationalizations (e.g. energy), or very closely followed the management of firms which had remained in private hands. The latter case concerned for example the steel industry. In spite of the fact that it was not officially nationalized until the beginning of the nineteen eighties, the constraints which the State imposed on its strategy were very strong (Lesourne 1998: 96). These constraints' justification was primarily based on the financial resources directed to the development of the sector, which essentially took the form of public funds. The State granted, in fact, loans at a reduced rate of interest. Lesourne (1998: 96) quotes the statement made close to 1970 by a steel manager: "You want to know details concerning our accounts? Ask the public administration. They know them better than we do!" (our translation).

More generally speaking, the State controlled the essential dimensions of the whole financial circuit. Hence, capital export and import were limited because of exchange controls. The stock exchange played but a minor role in corporate finance. In this context, a famous quotation by de Gaulle is quite significant: "French politics are not decided at the stock exchange." (our translation). On the contrary, banks and the public treasury and its satellites contributed an essential fraction to financing the economy (Albert 1991: 269). In this context, the State's privileged position appears even more clearly knowing that the large deposit banks were also nationalized after world war II.

The specific governance structures of the nationalized firms depended directly on the government's policy. This concerned notably the composition of their boards of directors. It is, however, important to stress that the force of the State-controlled governance mechanisms varied with the type of firm under study. This force appeared to be most intense in the case of the nationalized firms. But even the private sector felt the (more indirect) influence of the

State. In fact, beyond its control of the financial circuit, the public sector was often a major client. In this way, "a close symbiosis takes place between the State and the private groups" (Lesourne 1998: 98).

Close ties between the State and certain corporations, be they nationalized or private, also existed, and still exist, at the level of higher education of the managerial *élite*. In fact, a great fraction of the biggest French firms' CEOs have received their education at the ENA (*Ecole Nationale de l'Administration*) and/or have started their professional career in the public administration. Bertin-Mourot and Bauer (1996: 22) observe that "it is in France [...] that the transfer of *élites* from the State's to the firms' top positions is greatest" (our translation). In this way, the large corporations partially delegate the "detection-selection-education" procedure to the State (Bertin-Mourot and Bauer 1996: 23). It is also quite interesting to note that the primary origin of the managerial *élite* seems to be rather constant over time (Bertin-Mourot and Bauer 1996: 23).

To summarize the preceding developments, we note that the State played traditionally an important role in the French corporate governance system. Albert (1991: 267) describes it as "a *colbertistic* State that has not ceased to dominate the economy: protectionistic and dirigistic on the one hand, but also an investor, [and] entrepreneur [...] on the other" (our translation). In what follows, we shall see that the limits imposed on managerial discretion by the public administration have progressively been alleviated. Even though they are presently weaker than they used to be, they remain frequently stronger than in other industrialized countries. For such a comparison, it is possible to refer to the example of the market for corporate control, which appears traditionally to be less developed in France than in the Anglo-Saxon sphere. In 1990, Franks and Mayer (1990: 228) still conclude that the public authorities have great discretion in the application of the takeover rules. Hence, in certain cases, the French government has allegedly retarded the takeover of firms by foreigners in order to find a domestic solution (Franks and Mayer 1990: 209). The recent example of the takeover battle opposing BNP to Société Générale and Paribas equally represents the attempt of interference by the public administration. But, at the same time, it perfectly illustrates the weakening of the means of public intervention. In fact, the Minister of Finance and the Governor of the Central Bank would clearly have preferred a privately negotiated solution to an open battle in the market place. In the course of these events, the State's representatives used their right to suspend a revised bid by Société Générale for Paribas to invite the different protagonists to the table of negotiation (Le Monde 06/27 and 06/28/1999). During the negotiations, the Governor of the Central Bank submitted his own proposals to the conflicting parties. Lacking the power to actually impose his project, the unsuccessful end of the negotiations implied, however, the obligation to wait for the closure of the official stock-exchange procedure in order to obtain a solution. A leading economic newspaper had the following comment. "This frustrating and unfruitful negotiation demonstrates that the public authority lacks the means of actively opposing the fact – in spite of the Finance Minister's publicly expressed wish to the contrary – that the mere 'luck of the market' determines one of the most important movements in banking France has ever known." (Les Echos 07/01/1999, our translation).

A Brief Description of the Major Transformations

So far, we have primarily described the historical roots of the French system of corporate governance, which strongly influenced its shape roughly until the middle of the nineteen-eighties. Since then, the system has, however, undergone some significant transformations, as is illustrated by the BNP-Société Générale-Paribas case. In fact, following deregulation, which was initiated by the government in 1984, the evolution of French corporate governance has been characterized by the diminishing role of the State. In this context, the 1984 event lay the foundations of a rehabilitation of the capital market. The fact that this step was undertaken under a socialist government may appear as somewhat surprising. We will consider the importance of this observation further on, when returning to the case of France after the presentation of our conceptual framework. French deregulation implied as a consequence that certain companies gained direct access to the financial market to cover their need of capital funds. Hence the State's control over the financial circuit was alleviated. At first, an important fraction of the major corporations remained, however, under the direct control of the public administration. The government changed in 1986, bringing along a first wave of major privatizations. This further exasperated the State's retreat from direct corporate governance. The impact of the privatization program on the corporate sector in France appears to be significant. In fact, reviewing the literature on privatization worldwide and referring to the aggregate value as well as the number of firms, Alexandre and Charreaux (2004: 467) describe "the French program [as] one of the world's most ambitious privatization programs." The movement was temporarily interrupted due to another change in the political landscape, only to be continued in the form of a second wave of privatizations beginning in 1993. It should be noted, however, that the State's retreat was not complete. In fact, by installing the so-called *noyaux durs* (literally hard cores), the public administration maintained the capacity of at least indirectly influencing the development of the corporate governance structures of the newly privatized companies. *Noyau dur* is the term used to identify the group of major shareholders who are co-opted in the privatization process. Hence, in a first stage, direct control by the State was replaced by control through other companies which held significant capital stakes. The government thus exerted a certain influence by participating in building up these major shareholder groups. What is interesting is the fact that the circle of companies called upon to compose the *noyaux durs* in the context of the different privatizations was rather restrained. As a consequence of this, the system of corporate governance applying to some of the largest French corporations, formerly subject to the State's direct influence, was characterized by a dense network of cross shareholdings for several years. These cross shareholdings went generally hand in hand with personal ties in the form of an exchange of corporate directors. Around 1995, this network was starting to be undone (Les Echos 12/08/1998), progressively replacing the prevailing system of relational governance by more capital-market related mechanisms. As a result of this process, some of the major companies have, at present, a capital structure exposing them to the pressure of potential takeover.

This brief description of the French system of corporate governance since 1984 indicates some major changes in the institutionalized control mechanisms which typically apply to a large company's CEO. What drives this evolution? In the following section we propose the building blocks of a conceptual framework in an attempt to gain deeper insight into the dynamics of changing institutions of corporate governance.

The Evolution of Corporate Governance and the Economic Theory of Institutional Change

To construct the conceptual framework, we proceed in two stages. Hence, we shall first briefly report some major theoretical outcomes of North's theory of institutional change, before applying the latter to the specific case of corporate governance.

The Logic of Institutional Change according to Douglass North

North (1993) defines institutions as "the constraints that human beings impose on human interaction." There is a great variety of such constraints ranging from formal (rules of law) to implicit (ethical conduct). One implication of the existence of institutions is that, if the institutional constraints are properly enforced, their transgression is costly. In this way, the institutional matrix has a very strong influence on the economic opportunities of the agents it constrains. It is however important to stress that, even though institutions impose limits on human behavior, they are never capable of closely determining *every single* decision made by the agents who act in their realm (Mayer and Whittington 1999). For this reason, the human actor has discretion over a number of decisions.

This basic assumption about the relationship between the economic agent and his institutional environment having been presented, how can a change in the existing informal and/or formal constraints be explained? In fact, to render such an explanation plausible, a realistic model of human rationality is needed. Hence, North (1990: 17) makes some behavioral assumptions as to the fundamentally procedural nature of human reasoning (Simon 1982). This implies that the economic agent acts along the lines of trial and error (Simon 1983). This type of behavior can be explained by the fact that a human being never has complete knowledge of all parameters characterizing the environment he acts in, nor does he perfectly understand all factors that affect the outcome of his actions. What helps the economic agent to make decisions in the context of such uncertainty is a theory he holds on the functioning of the world in which he lives. In North's work on institutional change, such theories are referred to as "mental patterns" or "mental models". They are the starting block for concrete action within – or on the limits of – a given institutional framework. North (1993) expresses this in the following way. "The key to the choices that individuals make is their perceptions, which are a function of the way the mind interprets the information it receives." The mental pattern shapes these interpretations and hence influences an actor's perception of the opportunities implied by the institutional matrix. The latter is the "incarnation" of the dominant ideology, that is to say a mental pattern which is shared by several (influential) individuals. Hence, a given institutional framework can be looked upon as the translation of a shared mental pattern into real institutions. This is somewhat close to Aoki's (2001) conceptualization of institutions as "a self-sustaining system of shared beliefs." In order to understand how institutions evolve over time, it appears thus to be crucial to reach an understanding of the role of mental patterns. As Denzau and North (1994) put it, “institutions clearly are a reflection of the evolving mental models”.

In the theory of institutional change, ideologies and the institutions they shape are modified by the action of so called “organizational entrepreneurs”. According to North (1993), “the entrepreneurs of organizations induce institutional change as they perceive new or altered opportunities.” This statement can be translated into the terminology of mental patterns, because the latter help explain the perception of opportunities. In fact, an actor must weigh the costs and benefits he anticipates from action inside the existing institutional framework against the costs and benefits he hopes to derive from a change in the rules of the game. In this sense, an individual mental pattern is “entrepreneurial” to the degree that it diverges from traditional ideology, leading to the perception of better opportunities resulting from institutional innovations when compared to a strategy inside an unchanged environment. In spite of its appeal to a (boundedly) rational economic tradeoff, this perspective should not be confounded with accounts depicting man as over-rational and under-socialized. According to economic institutionalism, individuals do not choose their course of action as a function of some set of supposedly objective “real” parameters, but on the basis of their subjective representation of relevant parameters. According to Denzau and North (1994), “people act in part upon the basis of [...] ‘half-baked’ theories.” The formation of these theories or mental patterns is partly dependent on the specific socio-cultural context and the personal experience of organizational entrepreneurs. “History matters” to speak with Aoki (2001).

The foregoing discussion highlights the organizational entrepreneur as the driving force behind institutional change. In this context, two general traits characterize the typical entrepreneur. The first has already been presented, namely the holding of a mental pattern capable of transgressing the limits of dominant ideology. But, an innovative approach to institutional matters alone is insufficient to translate one’s philosophy into real action. For this to be possible, the potential entrepreneur also has to dispose of effective means of action. This explains why, in North's theory, it is not the individual that interacts directly with the institutional matrix. What brings about real change is, in fact, supposed to be the "continuous interaction between institutions and organizations" (North, 1993). Thus, the organization can be seen as an enabling device making real action possible. Hence, institutional entrepreneurs are typically the leaders of organizations. It should be noted, however, that the organizations which potentially serve entrepreneurs in an effort to influence institutions of corporate governance are not restricted to the corporate sector alone. The leaders of such diverse organizations as the national government, trade unions, professional associations and firms may use their organizational infrastructure and resources as a vehicle to initiate institutional change.

The foregoing developments can briefly be summarized as follows. Human individuals act in response to opportunities that are perceived as such through the lens of mental patterns. To the extent that an actor perceives better opportunities in an altered institutional environment than in the existing one, he has incentives to become an entrepreneur. He may initiate real change if he disposes of sufficient resources. The availability of the latter is typically conditioned on the support of an organizational infrastructure.

So far, we have mainly discussed the theoretical conditions that are the starting block for institutional change, without characterizing the nature of the process of change itself. We will address this question more closely in the context of the specific case of the evolution of corporate governance, and especially when explaining the role of the shared mental pattern as a force keeping institutional change on its historical trajectory. So, before we go on to the next section, we simply add that the nature of the evolutionary process is supposed to be "overwhelmingly incremental and path dependent" as stressed by North (1993) in the context of his general treatment of institutions. This is consistent with Bebchuk and Roe (1999) demonstrating the relevance of path dependence for an analysis concerning more specifically the institutions of corporate governance.

Institutional Change and Corporate Governance

If we choose to accept the definition of a corporate governance system as *the set of mechanisms which restrict managerial discretion* (Charreaux 1997), the explanation of institutional change summarized in the preceding subsection can easily be transferred to the field of the dynamics of governance. In fact, *restrictions on managerial discretion* are a special case of “the constraints that human beings impose on human interaction”, which corresponds to North’s definition of institutions. As a consequence, the system of corporate governance consists of a subset of the entire set of rules composing the institutional matrix of a given country. Figure 1 represents this relationship between institutions and corporate governance, where corporate governance is one specific institutional domain among others, the different domains typically being complementary (Aguilera and Jackson 2003; Hall and Soskice 2001). Note that an individual firm’s CEO is generally not subject to all mechanisms potentially available inside the governance system of a particular country. The management of a company that is not listed on the stock exchange, for example, does not support the pressure of potential takeover in the open market as a disciplinary device. Hence a national system of governance allows for the coexistence of several subsystems. As a matter of fact, different activities may be governed through varying control mechanisms, even within the same national context. To achieve focus, the following analysis of French corporate governance is highly stylized, exclusively featuring stereotypical large-scale companies, as those included in the stock-market-index. Special cases like small family business and partnerships are thus explicitly excluded from our study.

[Insert figure 1 about here]

By constraining managerial discretion in certain ways, the corporate governance system achieves an alignment of the CEO's actions with the interests of certain stakeholder categories (Shleifer and Vishny 1997). This has important theoretical implications if we want to make the very broad concept of the mental pattern operational for the explanation of the dynamics of governance. In fact, as a special form of the "rules of the game", the available governance mechanisms can be represented as being the institutional "incarnation" of the shared mental pattern in a given country. We owe a great deal of our present understanding of the workings of corporate governance to research standing in the tradition of financial economics and positive agency theory (Shleifer and Vishny 1997; Daily et al. 2003). Following this tradition, the concept of value is of central importance (Jensen 2001) in achieving parsimonious modeling of the impact of the conflict of interests between stakeholders on the adoption of specific governance structures. Even though in these models value is often confounded with *shareholder value*, this need not necessarily be so (Castanias and Helfat 1991; 1992; Garvey and Swan 1994). In fact, confounding value with shareholder value is based on the very restrictive assumption that the shareholders are the only residual claimants of the firm. But, such an assumption is itself likely to be influenced by a particular mental pattern, namely the one which Yoshimori (1995) identifies as the "monistic concept of the firm". Since the latter does not apply equally to different countries, an explanation of corporate governance based exclusively on such an approach has weak explanatory power, especially when it comes to dynamics. Hence, it is reasonable to define value more broadly as the overall organizational rent (Charreaux and Desbrières 2001). The conflict of interests between stakeholders may then be framed in very general terms as a struggle for the creation of rents and their appropriation. Under these conditions, the commonly shared "theory (or ideology) of value" has a major impact on the accepted rules that apply to the creation and redistribution of rents in a specific institutional environment. This is consistent with Aguilera and Jackson's (2003) proposition that the precise nature of conflicting interests depends on the institutional context. The following definition of the mental pattern for modeling the dynamics of governance may thus be proposed: a mental pattern is "*a representation of the role of different stakeholders in the value creation process as well as of the appropriate remuneration of their services*" (Wirtz 2001). This is, of course, a highly stylized representation of a mental pattern, and it is very likely that the effort to observe *real* mental models would yield much more complex constructs. Hence, our approach aims at achieving parsimony in explaining the evolution of corporate governance systems. It is not meant to contribute to a descriptive inventory of cognitive maps.

The proposed definition can be viewed as what may be called the ideological core assumption of the mental pattern. It contains a means-ends representation as well as a normative component. Supposedly "good" corporate governance is hence weighed by the different actors against such an ideological benchmark. In order to be able to do so, besides the core assumption, the mental pattern has to contain a representation of the economic effects of different incentive and control mechanisms. We propose to refer to this as *the technical component* of a mental pattern concerning governance issues. An example of this technical aspect is the belief in the efficacy of an active market of corporate control to achieve shareholder interests (Jensen 1993; Schneper and Guillén 2002).

What is important for the dynamics of corporate governance systems as represented in the present conceptual framework is the fact that an individual's mental pattern, though partially influenced by cultural learning (Denzau and North 1994), may diverge in a more or less important manner from the traditional concept of the firm. Such differences potentially concern fundamental core issues or simply some technical aspects of governance. In this context, an entrepreneurial mental pattern leads to the perception that an institutional innovation has a positive effect on the opportunities of rent creation and on the possibility of its appropriation by the entrepreneur. In order to be attractive to the latter, the anticipated benefits from changing the existing governance structures must outweigh the anticipated costs such a change implies. At this point, it is useful to specify, however, that our use of the term innovation does not necessarily imply the invention, *ex nihilo,* of a totally unknown governance mechanism. In fact, the transfer of a mechanism already existing in a foreign institutional matrix to one's own national environment can also be considered as an institutional innovation. The preceding developments highlight a mechanism supposed to be an important driver of the institutional dynamics of corporate governance, which may be framed in terms of proposition 1.

Proposition 1: The organizational entrepreneur perceives the opportunity of changing particular features of the country-specific configuration of corporate governance mechanisms as a function of his individual mental pattern. The relative weight of different stakeholder categories in his representation of the value creation process favors the entrepreneur's sponsorship of the development of governance mechanisms associated with those stakeholders supposed to make a critical contribution.

The first proposition concerns primarily the individual organizational entrepreneur. The latter can be, but is not necessarily, the CEO of a large company. His initiatives have a more or less immediate impact on the national system of corporate governance, depending on the organizational infrastructure and resources supporting his action. Hence the manager of a single corporation, by pursuing his personal strategy, has probably an impact on the system as a whole, which is much lighter than what can be expected from the prominent leader of a regulatory body. However, through a feedback loop working along the lines of trial, error, and the imitation of supposedly successful strategies, local action may exert a decisive influence on the overall system in the long run (Roberts and Greenwood 1997: 361-362). In this context, the velocity and the form which characterize a change in the system of corporate governance is *a priori* subject to the distance between the entrepreneur's innovative approach and the shared mental pattern. Hence, the following proposition concerns the interface between the local level of the individual firm and the overarching level of the system of corporate governance.

Proposition 2: The shared mental pattern contributes to maintain changes of the features of country-specific configurations of governance mechanisms on a historical path. The effects of an individual entrepreneur's initiative implying too large a departure from traditional routines of governance are likely to be moderated by influent stakeholders' invocation of the dominant ideology.

To be sure, in addition to the shared mental pattern, there are other forces enhancing path dependence, such as various institutional complementarities and the rent seeking behavior of entrenched interests (Bebchuk and Roe 1999). Our emphasis lies however on institutional dynamics, where mental patterns play a central role. Hence, representing the shared mental pattern as a moderating force must not obscure the fact that the dominant ideology is itself subject to change. Path dependence does not signify absolute inertia. Thus, in principle, changes in the shared mental pattern are possible. Theoretically, they tend however to be of a gradual rather than of a disruptive nature. In fact, it seems reasonable to suppose that different stakeholder categories engage in adaptive learning as a result of observed past success. According to Vromen (1995: 119) "*[b]eliefs* can be said to be improved in the sense that the agents come to recognize *ex post* what ways of behaving do and what ways of behaving do not yield satisfactory results" (italics in original). The underlying logic is a long-term tendency towards relative – that is to say constrained – efficiency (Roberts and Greenwood 1997), which does not exclude, however, transitory periods of relative inefficiency (Hill and Jones 1992). In fact, it can be imagined that changing a shared mental pattern implies costs of adaptation. Their relative weight depends on the number of stakeholders that have to engage in this type of learning and on the effort it imposes on them. Thus, for learning to take place, the concerned stakeholders must perceive the effort to be outweighed by the benefits. For gradual it may generally be, when a change in the ideology of reference actually does take place, this is likely to cause a transition in the system of corporate governance. In fact, the latter is the shared mental pattern's institutional "incarnation". Hence proposition 3.

Proposition 3: National corporate governance systems change as a function of the evolution of shared mental patterns.

To a great extent, research on governance has been stimulated in the field of corporate finance. Shleifer and Vishny (1997) propose a survey of this literature. They state that "[c]orporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return to their investment" (Shleifer and Vishny 1997: 737). According to this perspective, financial investors are a potentially important stakeholder category, trying to assure themselves a part of the organizational rent. Their perception of the way in which this objective can best be achieved depends on their particular mental pattern. Investors' expectations of appropriate returns are thus likely to depend on the "philosophy" according to which value is supposed to be created and redistributed in a given firm. Hence, it seems reasonable to assume that investors condition investment decisions on the consistency of their own mental pattern with the one reflected by the CEO of the firm to which they choose to channel their funds. As a result, the ready availability of liquid financial resources gives management discretion in pursuing its strategy (Wirtz 2001), hence proposition 4.

Proposition 4: Investors' perception of managers as being capable of creating value in a way consistent with their own mental patterns facilitates firms' access to external resources. Those resources potentially enhance managerial discretion.

The managers of financial investment organizations may also be considered as a particular category of organizational entrepreneurs. This is the case when they actively promote specific governance mechanisms which are unfamiliar to the actors belonging to a given national corporate governance system. Recall, however, that to actually become an entrepreneur, leaders of organizations have to dispose of sufficient means of action. Institutional investors having access to large amounts of liquid resources possess such an enabling device, if they are free to invest their funds where they see the best opportunities, and if these funds are perceived to be critical to corporations. As firms in a given country increasingly have recourse to financial capital controlled by investors with an entrepreneurial approach towards corporate governance, new governance mechanisms will eventually become institutionalized. The result should be a gradual transformation of the country-specific configuration of corporate governance mechanisms. This leads us to proposition 5.

Proposition 5: When a country's firms increasingly resort to a certain type of finance, this is one potential cause of a modification of the range of particular governance mechanisms making up the national system of corporate governance.

The theoretical propositions summarize a conceptual framework which aims at a better understanding of the dynamics of corporate governance systems on the basis of the interaction between organizations, their leaders and the institutional context. It is the innovative mental pattern of an entrepreneur which is supposed to stimulate the process of change. In order to actually play the role of an entrepreneur, the leader of an organization must have discretion. Large amounts of liquid financial resources and control over important organizational infrastructures are possible means of enhancing such discretion.

The following section is destined to confront the conceptual framework with a stylized account of the mutations of the French system of corporate governance. In doing so, we seek to ascertain whether the theoretical propositions derived from the economic theory of institutional change are consistent with the characteristics of an actual historical process. Unfortunately, the Anglo-Saxon literature is so far rather poor of descriptions of French corporate governance, with the notable exception of Schmidt (1996), which obliges us to base our analysis mainly on French sources. The latter range from accounts by academic observers (Albouy and Schatt 2004; Hirigoyen 1994; Lesourne 1998) and by well-informed managers of large corporations having occupied major positions in the French business landscape (Albert 1991; Fauroux 1998; Peyrelevade 1998; Riboud 1999; Viénot 1995) to articles and special inquiries published in the economic and general press (Les Echos; Le Monde).

The Theoretical Framework Applied to the French Case

Figure 2 recalls some of the most significant milestones in the process transforming the French corporate governance system.

[Insert figure 2 about here]

The following analysis systematically examines these changes in the light of the conceptual framework presented in the preceding section. Our reading of the evolution of corporate governance in France since the end of the second world war suggests that it is possible to roughly subdivide the total period into three distinct sequences. In fact, a first sub-section illustrates how the dominant ideology contributes to effectively counteract the initiative of an individual organizational entrepreneur. In spite of such transitory resistance, however, institutional entrepreneurs located at the very heart of traditional French-style capitalism – that is to say the State – succeed in triggering deep reaching transformations, as will be shown in the second sub-section. Among other things, these transformations bring about a liberalization of capital transfers. In the following years, this makes it possible for foreign investors to increase their influence on major French corporations, which is the central theme of the third sub-section. In this context, the activism of certain institutional investors, especially from the Anglo-Saxon sphere, appears to contribute to the promotion and the increasing acceptance of new standards of corporate governance.

The Traditional Mental Pattern Resists Disruptive Change (1945-1983)

We have already indicated that the traditional French concept of the firm was rather hostile towards governance mechanisms that enhance private benefits which can easily be appropriated by shareholders. According to this point of view, the interests of different stakeholder categories were thought to be properly represented by the State's predominant role in corporate governance. On the technical side, this representation was coupled with a preference for relational control mechanisms working through a network of personal ties over anonymous mechanisms of the market. Such an economic "philosophy" was not necessarily shared by every single individual, however, which means that entrepreneurial initiative could not be excluded. This assessment is well illustrated by the conditions surrounding the first important control fight in the French capital market since the end of world war II.

In fact, in December 1968, Antoine Riboud, then CEO of B.S.N. (Boussois-Souchon-Neuvesel), an important glass manufacturer which later took on the name of Danone, one of its better known brand names, launched a hostile raid on his major French competitor, Saint-Gobain. The latter company had been founded in 1665 by Colbert, and its trajectory has been an integral part of France's industrial history. In his own words, Riboud described the strategic motives of his initiative as follows.

"We [A. Riboud and A. de Vogüé, CEO of Saint-Gobain] had two opposite strategic visions. Our own strategy was to rapidly gain strength in our [main] activities, to concentrate our investments and to specialize our factories in order to ameliorate productivity. [...] On the other side, at Saint-Gobain, management was based on a *'colbertistic' conception* of enhancing the value of assets in the long run. 'Immediate profits and short-term return on investment must in certain circumstances be limited to assure long-term security and growth', Arnaud de Vogüé had said. These to strategies had led to results which were translated into the share prices. The 200,000 Saint-Gobain shareholders had seen the value of their shares decline between 1958 and 1968, whereas the BSN share had tripled." (Riboud 1999: 82-83, our translation, italics added).

Perceiving an important potential to create rents by the merger of the two groups and in the face of his counterpart's refusal, A. Riboud decided to launch a hostile tender offer. The latter was, at that time, a very unusual strategy in the French context. It thus appears that in Riboud's perception only a radical departure from traditional corporate governance routines, which his active sponsorship of hostile takeover clearly implied, would help to realize the anticipated wealth gains. This observation is consistent with proposition 1, according to which the organizational entrepreneur perceives the opportunities of a change of particular features of country-specific corporate governance as a function of his individual mental pattern. Riboud's emphasis on the development of shareholder wealth lends further credibility to proposition 1. The latter contains, in fact, the idea that the relative weight of different stakeholder categories in the entrepreneur's representation of the value creation process is a favorable condition for the development of control mechanisms associated with those stakeholders supposed to make a critical contribution. The CEO of B.S.N. appears to have lent relatively more attention to shareholders as a stakeholder category than did his counterpart at Saint-Gobain. The latter actually promoted a more traditional *colbertistic* approach. In a manner consistent with his emphasis on shareholder value, Riboud had recourse to a governance mechanism of the capital market, that is to say a hostile tender offer. Such a strategy is consistent with proposition 1 to the degree that the entrepreneur subscribes to the assumption that the market for corporate control is a disciplinary mechanism achieving an alignment of the behavior of a firm's management with shareholder interests (Jensen 1986).

The defense of the incumbent Saint-Gobain management was to a large extent based on a campaign mobilizing many stereotypical perceptions that were shaped by the traditional ideology. Thus, Hirigoyen (1994: 377) holds “cultural inertia” responsible for “the impossible success” of the takeover attempt. He shows that different stakeholder categories, such as the employees at different hierarchical levels, members of the board of directors and even the shareholders, were very attached to continuity. In fact, Saint-Gobain’s capital was characterized by weak mobility, hence corresponding to a system of “dedicated capital” (Porter 1992). As Hirigoyen (1994: 378) puts it, “one inherits Saint-Gobain shares, one does not buy them”. Hence, in a manner consistent with what we have earlier identified as the traditional shared mental pattern of France, the shareholders’ mentality refused to look at Saint-Gobain as a tradable merchandise.

When defending his position, A. de Vogüé, the incumbent CEO, explicitly linked his approach to the public opinion. In fact, he called B.S.N.’s takeover attempt a maneuver “stimulating *instinctive* opposition in the public” (quoted in Hirigoyen 1994: 379, our translation, italics added). It is in order to point out that the important aspect of the incumbent’s statements is not an assessment of his adhesion to every detail of what may be considered as the shared mental pattern. What matters is that, by integrating aspects of the dominant ideology into his rhetoric, he was able to rally the different stakeholders to his cause. The support given to de Vogüé’s defense as a response to perceptions shaped by the shared mental pattern appears hence as a significant cause of the outcome of the takeover battle. Roger Fauroux, who became Saint-Gobain’s president in 1980, gives his version of the takeover fight. “[...] in order to defeat the financial offers of its adversary, Saint-Gobain had established secret relationships with friendly firms which were to acquire a significant stake of its shares for a high price. Today, these things may seem surprising, but *when honor was at stake, ethical conduct forbade that one counts his money*.” (Fauroux 1998: 42-43, our translation, italics added). The “friendly” companies’ support appears thus to have been motivated by shared moral standards. Further contributing to our evaluation of B.S.N.’s strategy as having been opposed to dominant ideology, Fauroux (1998: 43) describes the public opinion's image of the aggressor as "really poorly educated". Riboud (1999: 91) also states that in traditional business circles he had a rather bad image. So everything indicates that in the institutional context of his time, B.S.N.'s CEO transgressed a major taboo.

The foregoing analysis seems widely consistent with proposition 2. According to the latter, the shared mental pattern contributes to keep changes of particular features of country-specific configurations of governance mechanisms on a historical path. In fact, B.S.N.'s tender offer was defeated, largely because of resistance which was mainly justified by elements of the shared mental pattern. The latter thus contributed to keeping the French system of corporate governance on its historical path. As a matter of fact, France did not develop a relatively active market for corporate control until the nineteen-nineties. The recent takeover-fight (1999) opposing three major banks (BNP, Paribas, Société Générale) indicates the great distance French capitalism has traveled since B.S.N.'s defeat. The following section delves deeper into the events that subsequently influenced the gradual change of French-style corporate governance.

The State as a Platform for Institutional Entrepreneurs (1984-1994)

According to Lesourne (1998: 132), the traditional representation of French business relations was at its highest in the nineteen-sixties. In fact, at that time, economic growth increased people's confidence with respect to the predominant ideology, which seems consistent with the idea of a positive feedback loop linking supposedly efficient outcomes to a perpetration of the dominant ideology. Since, the French mental pattern has however undergone certain transformations. In this context, some well informed observers speak of "a forceful penetration of American values into France" (Albert 1991: 274, our translation). This evolution was made possible by the State itself. The latter appeared to be the central instance of governance according to the shared mental pattern. Interestingly, it is precisely the initiative of the public administration which triggered a vast transformation of the French financial market. In fact, in the middle of the nineteen-eighties, the government "heals France's inhibitions and rehabilitates the fundamental values of the market economy" (Albert 1991: 269, our translation). The increasing role of the capital market in the supply of corporate finance progressively induced a change in the attitude towards certain governance mechanisms. Hence, we observe the spreading of ideas, which were traditionally more readily associated with the Anglo-Saxon referential. The increasingly internationalized capital market thus appears to have been one important vector pushing a change in dominant ideology. As a matter of fact, a significant proportion of the largest French firms is presently in the hands of foreign investors. The most active among them, as it is the case of certain American pension funds, promoted – and still do - a mental pattern which emphasizes shareholder demands and governance mechanisms supposed to maximize shareholder value. Accordingly, the pressure coming from the capital market has come to be perceived by French managers as a challenge to the established system of corporate governance. The following quotation from the Viénot report is a typical example of the influence the perception of the demands from the market has exerted on French thinking about corporate governance: "the Committee notes that the participation of independent directors complies with a *demand from the market*" (Viénot 1995: 15, our translation, italics added). According to Peyrelevade (1998: 43), who is even more radical in his conclusions, the need to have recourse to finance of foreign origin forces compliance with the "ideas of the *Financial Times*".

To summarize the preceding developments, one can say that the State, which was at the very center of the traditional shared mental pattern, was also at the origin of an important move to liberalize the French financial market. In this way, the public administration contributed to legitimize a concept of the firm, which diverged from traditional ideology. Following this initial move, the financial market has become an important vector for the diffusion of a "philosophy" of corporate governance, which gradually started moving away from the traditional French representation of efficacious control and incentive mechanisms. The public debate concerning the rules of “good governance”, which has put increasing emphasis on shareholder interests (Peyrelevade 1998), was far from being neutral with respect to the actual institutions of governance. We thus have an illustration of the plausibility of proposition 3, according to which national corporate governance systems change as a function of the evolution of shared mental patterns. As a matter of fact, during the last fifteen years, the dominant ideology in France has made increasing space for the market.

It was in 1984 that the State created the basis for its progressive retreat from the control of large corporations. What is interesting is the fact that this major reorientation took place under a socialist government. *A priori*, this may strike as rather surprising, but it eventually facilitated the legitimization of the increased importance of the market by other political currents. In the middle of the nineteen-eighties, the role of the entrepreneur with an innovative approach to the conditions of corporate governance was thus played by leading members of the French national government. Financial deregulation which was initiated in this way has been a significant cause of the long-term development of the market’s role in corporate control. The COB (recently re-baptized AMF) which is the French equivalent to America’s Securities Exchange Commission received strong authority (Albert 1991: 271) in order to ascertain the proper functioning of the capital market mechanisms. Conceived to assure the security of operations and to guarantee investor interests, the new rules contributed to extract the stock exchange from its marginal position. Hence, for certain firms, the State facilitated the direct access to market finance. A change in the corporate governance system has thus brought about a modification of the entire set of possibilities open to corporate finance.

But at a first stage, in spite of the impulse given to a liberalization of the financial market, not all firms were free to procure themselves finance at the stock exchange. In fact, the nationalized sector, being composed of some of the biggest companies, continued to play a very significant role. In this context, a second major change took place in 1986. The Chirac government launched the first important wave of privatizations. The following account helps appreciate the far reaching implications of this event.

“[...] eight large groups, the majority of which are of enormous importance (e.g. Saint-Gobain, Paribas, CGE, Havas, Société Générale, and Suez), have been transferred from the national to the private sector. The initial motivations of this new French policy can make one think of a target such as approaching the Anglo-Saxon model, in that increasing the dimension of the stock exchange by creating several million new stockholders had priority.” (Prodi 1991 ‘Entre les deux modèles’. *Il Molino*, quoted in Albert 1991: 265, our translation).

The privatization procedure, however, took on a very particular form, which should shape the face of French capitalism for several years to come. In fact, the French State did not want the newly privatized firms to become easy takeover targets. Because of this, the so called *noyaux durs* (hard cores) were installed. These were groups of permanent shareholders, controlling significant capital stakes. In this way, even though it retired from direct control of privatized firms, the public administration still maintained some influence on the future evolution of their control structure. One important peculiarity of the *noyaux durs* system was that a relatively restrained circle of companies was called upon to compose the groups of permanent shareholders (Les Echos 12/08/1998 ‘Le Planisphère’). Consequently, a very dense network of cross shareholdings was created. “Hence, most of the big French companies, be they private or privatized between 1986 and 1987 or between 1993 and 1994, were often shareholders of their own principal shareholders” (Les Echos 12/08/1998, our translation). It is also interesting to note that the exchange of capital stakes generally went hand in hand with an exchange of corporate directors. Consequently, the corporate governance system was characterized by a relational network which was relatively well shielded off against outsiders.

The privatizations of 1986 have clearly decreased the State’s direct control. However, the initiative was temporarily interrupted as a result of the election of a new government. Hence, an analysis of the evolution of financial relations concerning the biggest French firms shows that, in 1991, the nationalized companies were still quite numerous and of considerable weight (Les Echos 12/07/1998). Later, a new change of governments took place in 1993 leading to a second wave of privatizations. The latter still operated by installing groups of permanent shareholders and thus reinforced the previously described network of mutual relations.

It is interesting to note that these major institutional changes were launched as initiatives by the State. The organizational entrepreneurs, who were at the origin of this process, must hence be located at the level of the public administration. With respect to this issue, it is useful to recall the assumption that an entrepreneur has to comply with two conditions. First, he should have a perception of opportunities that partially diverges from traditional ideas. Second, he should dispose of some sort of enabling device to realize his strategy. In this context, it seems probable that liberalization gained legitimacy by the fact that the representatives of the State, central player in the shared mental pattern, were themselves the initiators. This may explain why, in this case and quite to the opposite of Riboud's earlier isolated initiative, the traditional ideology was not a serious obstacle to institutional change. In fact, proposition 2 considers the distance between the shared mental pattern and the cognitive structure of the organizational entrepreneurs. In the French case, it seems plausible to suppose that the distance perceived by the public opinion was quite small this time, due to the fact that the State itself controlled the transition. This is in line with an observation made by Albert (1991: 267) concerning the traditional perception of the State's role: "a *colbertistic* State which has not ceased to dominate the economy: protectionistic and dirigistic on the one hand, but investor, *creator,* [...] on the other" (our translation, italics added). Due to the fact that it was emanating from the central figure of dominant ideology, the initiative appeared to be legitimate. At this point, we should also signal that the first *noyaux durs,* which were in part composed of still nationalized firms, featured a clear preference for a French solution. In this way, the State indicated its wish to transform the system, without stimulating too violent a departure from national routines.

The growing importance of capital market mechanisms for the governance of French firms at the end of the nineteen-eighties is also illustrated by Franks and Mayer's (1990: 198) observation, according to which only recently "a number of hostile bids have been launched in France and [...] these are set to increase in the future". In fact, simultaneously with the State's first major draw-back from direct corporate control, the disciplining force of a potential hostile-takeover risk was kept small for certain companies, as a consequence of the above mentioned network of cross shareholdings. Hence, the evolution of the governance system since 1984 really was double. It was characterized by two distinct forms of control substituting for the traditional State-dominated governance mechanisms. In fact, direct control by the State was progressively replaced, either by a system of cross shareholdings, or, in the rare cases of widely held firms, by the pressure stemming from a potential hostile tender offer.

The Increasing Capital Stakes of International Investors and Their Consequences (1995 and later)

In the context of globalization, French firms have increasingly been exposed to international competition. But, on a global scale, the big French companies have not always played in the major league. A strategy oriented towards internationalization, as explicitly promoted by certain managers, such as those of French steel producer Usinor (Wirtz 2001), recently renamed Arcelor, for a relevant example, led to important demands for external capital funding. In this context, one possible solution for firms was to call on the liberalized financial market to supply the necessary financial resources. Recall that certain companies had gained direct access to the capital market due to the various initiatives of deregulation and privatization conducted during the nineteen-eighties. As a consequence of the growing international integration of capital markets, transaction costs were constantly reduced. This facilitated the implementation of those investors' strategy wishing to (geographically) diversify their financial investment portfolios. Hence, a major proportion of the biggest French firms came to be characterized by a capital structure where foreign investors gained increasing weight. In fact, a study conducted by the *Conseil National du Crédit et du Titre* on corporate finance in France considered that, "during recent years, finance from non-residents has been amplified because of their wish to diversify their placements" (CNCT 1999: 181, our translation). In only ten years, the proportion of the French stock exchange's capitalization held by foreign investors increased from originally 10% to 36% (statistics from *Banque de France*, quoted in Les Echos 12/09/1998). Hence, CEOs wishing to issue new equity increasingly came under the influence of actual and potential foreign stockholders. In this context, especially the Anglo-Saxon pension funds, very attached to shareholder value, were quite active in defending their own stockholder-centered "philosophy" of corporate governance. Aguilera and Cuervo-Cazurra (2004) have recently put significant emphasis on Anglo-Saxon institutional investors' activism as one important driver of the diffusion of codes of "best practice" in corporate governance on a global scale. The following account highlights institutional investors' potential role as organizational entrepreneurs relating to issues of corporate governance: "Activism represented a shift [...] to institutions challenging managers and directors on a variety of issues, such as urging firms to make structural changes in their boards of directors and redesign firm voting procedures. Leading institutional investors, such as CalPERS in the USA, believe that 'good governance is good business', and hence will by default create shareholder value. The fact that in 1996 CalPERS established a corporate governance office to pressure domestic and international firms to adopt shareholder-friendly proposals and other measures designed to improve stock performance is an example of growing shareholder activism." (Aguilera and Cuervo-Cazurra 2004: 428).

Anglo-Saxon institutional investors of this sort typically disliked the opaque network of cross shareholdings and interlocking directorships pervasive in the French economy up to the mid nineteen-nineties. Consequently, the growing importance of foreign investors in big French companies' capital structures coincided with successively disentangling the capital links established in the middle of the nineteen-eighties and at the beginning of the nineteen-nineties. Les Echos (12/08/1998), comparing data for 1991 and 1998, observed a "historical decline of cross shareholdings". This phenomenon appears to have been accelerated since 1995. Consequently, some of the largest French firms acquired more diffuse ownership than in the past, exposing them to disciplinary mechanisms historically absent from French-style corporate governance, such as hostile tender offers. Capital structure statistics concerning the biggest French firms and published by Les Echos (12/08/1998) show that ten of the corporations composing the CAC 40 stock market index had attained a proportion of permanent shareholders inferior to 15%. To be sure, when compared to Anglo-American ownership patterns, the capital structure of French corporations remained relatively concentrated on average (La Porta et al. 1999). However, the present paper's emphasis lies on the dynamics of a given national corporate governance system, and France experienced real change in the form of a significant decrease in the density of cross shareholdings (Les Echos 12/07-12/10/1998), in spite of persisting international differences. So, what continued relative concentration of ownership really teaches us about patterns of corporate control in France is not that they were static, but that their past evolution was highly path-dependent. In certain cases, the real influence exerted by active Anglo-Saxon investors on the governance mechanisms of (even family controlled) listed firms became especially strong. This can be demonstrated by the analysis of the successful proxy contest over Groupe André, initiated in early 2000 by the Franco-American investor Guy Wyser-Pratte and supported by another Anglo-Saxon investment fund, NR Atticus (Albouy and Schatt 2004). After having acquired a significant foothold through the stock market in Groupe André's capital structure, initially

25% family-controlled, the professional Anglo-Saxon investors defeated incumbent management and successfully imposed significant changes in the composition of the supervisory board. This precedent casts, as a matter of fact, serious doubt on the continuing relevance of a representation of French capitalism as being efficiently shielded off against the interests of shareholders acting in the stock market. The fact that the André proxy contest was quite unique in the French setting when it occurred made it an entrepreneurial initiative in the above-defined sense. Quite interestingly, the protagonist of this move to actively curb managerial discretion, Guy Wyser-Pratte, explicitly stated his desire to push French practice of corporate governance toward "American principles" (Albouy and Schatt 2004: 60).

It should be noted that foreign investors who acquired capital stakes in French companies did not necessarily do so in the context of new equity issues, thus injecting fresh financial resources into firms. It is likely, however, that such new issues, whether actually undertaken or simply anticipated in the future, directly or indirectly contributed to an amplified exposure of domestic firms to the influence of foreign investors, who had become major players in the global capital market.

Their increasing weight may be explained, at least partially, by the conditions surrounding the supply of and the demand for foreign capital funds in the French economy. On the supply side, we have already hinted at big institutional investors' wish to geographically diversify. They were and are, above all, interested in firms (French or other) that offer *from their point of view* the best perspectives with respect to return on equity. The latter is conditioned by a company's approach to the creation and the redistribution of rents. The investors' appreciation of a firm's capacity to create value and to distribute it in a supposedly "appropriate" way, thus enhancing return on equity, depends on their mental pattern. Hence, it appears to be plausible that at least those French corporations which came to be characterized by very large capital stakes held by Anglo-Saxon institutional investors gave an image of themselves as being managed according to shareholder-oriented standards of governance. This is consistent with proposition 4.

When examining the demand for foreign capital funds emanating from French companies, one may observe that it was to a great extent stimulated by certain structural features of national savings. In fact, "[French] households have a strong preference for the liquidity and the security of their investments" (CNCT 1999: 182, our translation). Thus, even though the study of the CNCT (1999: 183) clearly indicated national savings in excess of domestic needs, households invested only an insignificant part of their savings in corporate shares. In addition, those of the French financial institutions traditionally specialized in the management of a significant proportion of national savings also invested very little of the funds under their control in corporate equity. The CNCT (1999: 184) concluded from figures from the *Comité Européen des Assurances* (European Insurance Committee) that, "in a group of seven European countries [Germany included], France is the one where insurance companies invest the weakest part of their funds in corporate shares [approximately 15%]". Consequently, it seems plausible to suppose that French firms issuing equity in the financial market, probably more so than their counterparts in other national economies, underwent increasing pressure to comply with demands from foreign investors. This was at least partially a consequence of the weak propensity of domestic investors to put their money into corporate shares and of the simultaneous supply of excess funds from non-residents. Hence, the CNCT (1999: 194) stated that "the portfolio investments of non-residents in the French market progress strongly and have attained 414 billion French Francs in 1997 [, against 257 billion Francs of portfolio investments made by residents in foreign countries]" (our translation).

As far as corporate governance is concerned, the massive arrival of foreign capital stimulated an intensifying debate over the efficiency of the French corporate governance system. Hence, the recommendations of the Viénot report were mainly justified by the perception which managers in France acquired concerning the demands from investors acting in the financial market. Marc Viénot expressed this in the following way: “[...] the strongest pressure in favor of transparency and of better shareholder information has come from Anglo-Saxon pension funds, the latter being very determined on this issue. The weight of their capital stakes also gives much weight to their recommendations.” (quoted in Les Echos 12/09/1998, our translation). The increasing recourse to capital stemming from foreign investors and the consequent adjustment of the routines of governance thus confer a certain credibility on proposition 5. According to the latter, a modification of the range of particular governance mechanisms composing the national system of corporate governance may be brought about when a country’s firms increasingly resort to a certain type of corporate finance. As a matter of fact, in the French case, financial policies adopted by several significant corporations potentially exposed domestic firms to entrepreneurial action emanating from institutional investors and aiming at a transformation of particular features of the specifically French configuration of corporate governance mechanisms.

Conclusions

In this paper, we have tried to make intelligible the rationale underlying the major transformations of the French system of corporate governance since the middle of the nineteen eighties. Two main objectives have guided our investigation. First, we would like to fill a gap in the comparative literature on corporate governance systems, which has much neglected the French case. The latter is also very interesting in that it is characterized by several major changes which have taken place over the last two decades. This enables us to respond to our second objective, namely to illustrate the plausibility of a conceptual framework of the evolution of national systems of corporate governance. In fact, research on this issue is still in its infancy. Although many questions are still left unanswered, the stylized facts concerning the transformation of corporate France over the last decades seems roughly consistent with theoretical propositions derived from the economic theory of institutional change. Different initiatives to introduce new governance mechanisms into the French setting emanated from so called organizational entrepreneurs. These entrepreneurs disposed of mental patterns that diverged more or less from traditional ideology. The latter represented however a serious obstacle to disruptive changes in traditional routines of corporate governance in certain circumstances. So the evolution of a national corporate governance system, such as the French one, though real it may be, was shown to be highly path dependent.

Our analysis also indicates that the State was, for a long time, the primary platform for institutional entrepreneurs in France. Private initiative played a relatively less important role. In fact, an institutional innovation was attempted by the CEO of B.S.N., in 1968, but ran into fierce opposition and was consequently abandoned. One of the interesting aspects of the transformation of French capitalism is that the State was at the origin of its own progressive retreat. Hence, the traditionally strong institutional support for the entrepreneurial initiative by members of the State executive having diminished, the field was left open to potentially new types of entrepreneurs. Recently, institutional investors have proved very active on this front, promoting a “philosophy” of corporate governance which aims at enhancing shareholder interests.

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Figure 1

Different levels of analysis – the relation between a country's institutional framework and its system of corporate governance

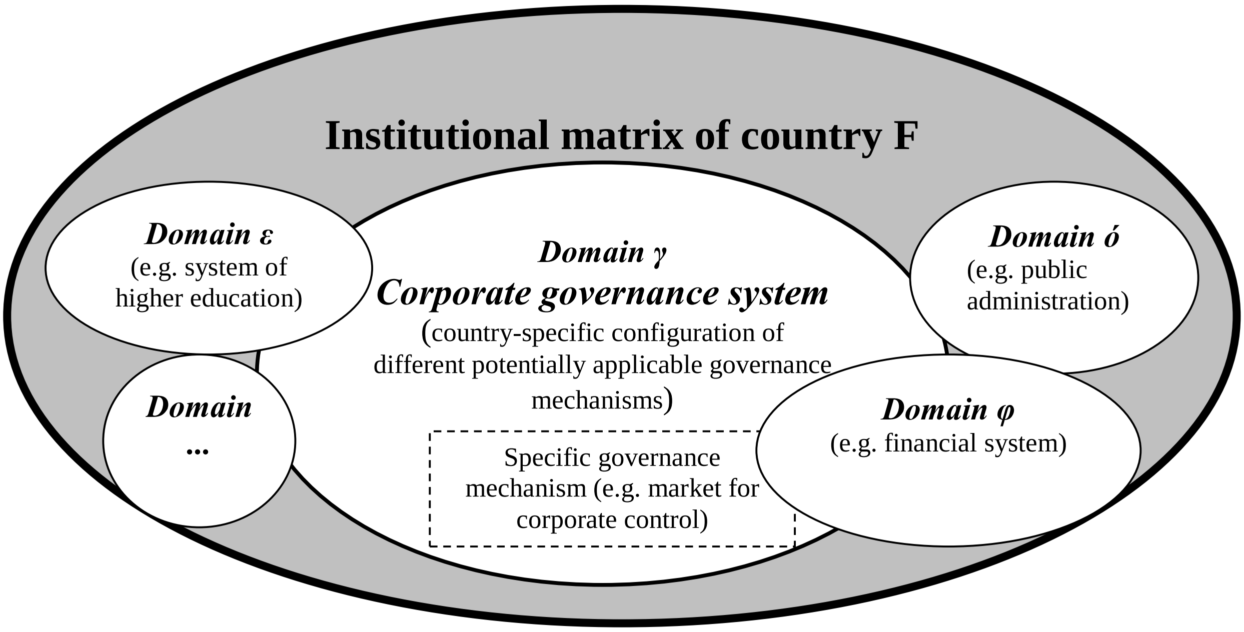

Figure 2

Significant milestones in French corporate governance