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Institutions and preferences in settings of causal complexity: foreign institutional investors and corporate restructuring practices in France

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In this article, we illustrate how the interaction between institutional arrangements and the presence of different categories of firm stakeholders with specific preferences provides important insights to understand the conditions under which corporate restructuring practices are introduced. Institutions shape the range of actors' strategic options and mediate the translation of the preferences of firm stakeholders into corporate policies. Nonetheless, strategic choice remains possible since firm stakeholders constitute subgroups with different interests and incentives that influence how they operate in an institutional framework. In particular, we examine under what conditions UK/US-based institutional investors and equity-based compensation incentives are associated with the implementation of asset divestitures and employee layoffs in France. We uncover three key findings. First, the presence of hedge funds and equity-based pay influence the likelihood of French companies undertaking asset divestitures. Second, the impact of hedge funds on employee layoffs is contingent on the ownership structure of firms. Third, layoffs in France are driven by inferior performance – a result that contrasts with the American experience whereby employee layoffs are also used as a strategic mechanism to deal with institutional investors in good times. Our findings demonstrate the importance of the institutional constraints of (national level) employment protection and the moderating effects of ownership structure (firm level) on the strategic and employment policies of French companies.

Keywords: CEO compensation; comparative corporate governance; employee layoffs; employment protection; France; institutional investors; national institutional frameworks

Introduction

The impact of corporate governance, and more specifically of ownership, on employment relations has received considerable interest in recent years (Black, Gospel, & Pendleton, 2008; Zagelmeyer, Heckmann, & Kettner, 2012). In the USA, for instance, increased ownership by institutional investors over the last three decades has transformed the nature of employment relations. Creating shareholder value at the expense of other stakeholders, especially employees, is increasingly seen as the fundamental purpose of corporations (Jacoby, 2005). Drastic corporate restructuring activities, such as employee layoffs and asset divestitures, have been prevalent since institutional investors believe that these practices are one of the most effective means to maximize shareholder value (Davis, 2009). Moreover, American companies increasingly rely on employee layoffs, which were previously used as temporary labor force reductions caused by decreased product demand,

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in order to improve financial performance in the context of increased pressures from shareholder value-driven institutional investors (Budros, 2002; Farber & Hallock, 2009).

In this article, we study the undertaking of two important corporate restructuring activities: employee layoffs and asset divestiture. We examine how the ‘Anglo-American influence’ has shaped the introduction of corporate restructuring practices in France – an economy traditionally not receptive to the concept of shareholder value maximization (Culpepper, 2005; Djelic & Zarlowski, 2005). For this purpose, we identify two channels through which the Anglo-American influence can affect corporate restructuring: (1) via block share purchases by US/UK-based institutional investors and (2) via the adoption of CEO equity-based compensation (stock options and restricted shares). We develop and test hypotheses concerning their effects, utilizing a discrete-time event history analysis of corporate restructuring activities with a sample of 130 French nonfinancial public companies between 1998 and 2007. We also explore whether these effects hold in the current economic crisis.

Our argument highlights how the interaction between institutional arrangements and the preferences of different categories of firm stakeholders provides important insights to understand the conditions under which corporate restructuring practices are introduced (Goyer, 2011; see also Garrett & Lange, 1995). In contrast to previous studies (qualitative and quantitative alike) that seek to identify the direct effects of hypothesized independent variables as standing-alone explanations, we conceptualize institutions and preferences as being part of a phenomenon of complex causation whereby an outcome results from potentially different combinations of factors (Hall, 2003; Ragin, 1987). Institutional arrangements and firm-level corporate governance practices constitute key factors accounting for cross-national differences in trajectories of change (Hall & Soskice, 2001; Whitley, 1999). Institutions act as constraints that reduce the range of feasible options by structuring power relations inside companies (Campbell, 2004; Hall, 1986). The conversion of the preferences of actors, even powerful ones, into corporate policies is mediated by the institutional framework in which they are embedded (Garrett & Lange, 1995). Nonetheless, institutional arrangements are not specific enough to translate into predictions about the strategic behavior of actors. The presence of different interest groups in advanced capitalist economies – such as firm stakeholders – each with their own idiosyncratic set of preferences, and governed by different internally defined rules, affects how they operate within an institutional framework (Aguilera & Jackson, 2003). In particular, highly incentivized firm stakeholders are often better placed to mitigate the constraining effects of institutions by exercising their greater level of discretion in less institutionally constrained arenas (see, e.g., Peteraf & Reed, 2007; Whittington, 1988).

We investigate under what conditions the arrival of shareholder-oriented investors and the introduction of new governance instruments are likely to change two important corporate restructuring activities, employee layoffs and asset divestiture. We present three insightful empirical findings. First, the effect of UK/US-based shareholders on corporate restructuring varies contingently on the type of institutional investor and the ownership structure of targeted companies. We find that foreign institutional investors, when analyzed as one group, do not increase the likelihood of a firm initiating restructuring activities. Yet, when differentiating by type of foreign investors, we uncover the influence of hedge funds on corporate restructuring. The causal influence of hedge funds, however, exhibits significant variations between asset divestiture and employee layoffs. For instance, while we find a positive and significant association between hedge fund investments and asset divestiture for all the sampled firms, the association between hedge funds and employee layoffs is only present among firm with diffused

ownership. Our findings highlight the importance of the diversity of preferences across different categories of institutional investors interacting with the presence of significant institutional constraints of employment protection laws (national level) as well as of the moderating effects of the ownership structure (firm level).

Second, we uncover that French companies governed by CEOs with higher equity-based compensation are more likely to initiate asset divestitures, while the introduction of this UK/US-based financial incentive has a marginally negative association with employee layoffs. We consider this result as suggestive, if not strong, evidence that the rigid French employment protection laws act as a salient institutional constraint even on financially incentivized CEOs.

Third, our empirical results highlight that French companies undertaking employee layoffs experience superior operating performance as compared to those that do not. However, we do not find significant performance improvement in the case of asset divestiture. The difference in outcomes between these two corporate restructuring activities suggests the presence of heightened institutional constraints, and potential political tensions, associated with employee layoffs in France. Our empirical analyses also reveal that poor performance constitutes a key driver to employment reduction in France. This result demonstrates that the nature of employment reduction in France is distinct from 'offensive' layoffs more common in the USA in the last three decades.

The rest of the article is organized as follows. We first introduce our conceptual framework and describe the French empirical context. Second, we discuss the literature of the empirical research on the Anglo-American influence (foreign institutional investors and CEO stock options) on corporate restructuring activities from which we develop our hypotheses. Third, we describe our sample and present the methods used. Fourth, we present our empirical results, followed by a discussion and conclusion.

Theoretical framework and hypotheses

Analytical perspective

This study of the influence of Anglo-American institutional investors and new governance practices (CEO equity-based compensation) on the corporate restructuring activities (asset divestitures and employee layoffs) of French companies raises important theoretical issues regarding the generalizability of findings across national settings. Do causal relationships in one setting translate faithfully into another one? Our argument builds on an extensive, and theoretically insightful, literature in social sciences delineating how institutions constitute the outcome of political and social struggles in historically specific settings that, in turn, influence the direction and character of change (Elster, 1984; Hall, 1986). Historically contingent institutional arrangements, once in place, act as constraints that reduce the range of feasible options in an asymmetrical manner (Hall & Soskice, 2001; Whitley, 1999). The presence of institutional diversity across national business systems shapes the power of different firm stakeholders by offering disproportionate access to, and thus influence over, the decision-making process and its associated resources at hand (Campbell, 2004; Hall, 1986). An incorporation of institutional effects is particularly suited to the context of French employment relations given the provision of relatively strong legal employment protection as measured by the costs of hiring new employees, size of severance payments, terms of unfair dismissal and (lengthy) notice requirements for the initiation of dismissal procedures (Botero, Djankov, LaPorta, Lopes-de-Silanes, & Shleifer, 2004; OECD, 2004).

Yet, the salience of institutional arrangements, themselves the outcomes of political and social struggles, constitutes a too broad category that overstates their constraining character. Our argument specifically links the role of institutions with the nature of causation in social sciences. Key political, economic and social outcomes are rarely generated by the presence of one cause alone; they occur as the result of specific intersections of conditions (Hall, 2003; Ragin, 1987). Although institutions are crucial to understand important changes in economic life, they are part of a phenomenon of complex causation whereby an outcome results from potentially different combinations of factors. In this article, we identify two factors that highlight how the insights associated with the presence of institutional constraints are strengthened by an incorporation of the strategic choices of actors in an overall process of complexity.

The first factor, inspired by actor-centered approaches, illustrates the asymmetric influence of different categories of firm stakeholders in the governance of companies (Aguilera & Jackson, 2003; Gourevitch & Shinn, 2005). Firm stakeholders are characterized by the presence of groups with different interests, and governed by distinct internally defined rules that, in turn, shape their preferences. For instance, the preferences of UK/US-based shareholder value-oriented investors can be divided along their investment strategies, size of equity stake, time horizon, prominence of commitment versus liquidity concerns and the degree of their embedded position in national corporate networks (Brav, Jiang, Partnoy, & Thomas, 2008; Goyer, 2006). The presence of groups with different interests and preferences suggests that how they learn to operate in a single, and constraining, institutional framework can therefore lead to different adjustment paths.

The second factor emphasizes how processes of institutional creation are often characterized by piecemeal diffusion whereby new institutions are introduced in a limited number of areas of the economy, while other spheres are left untouched (Locke & Thelen, 1995). In the first four postwar decades, for instance, French policy-makers simultaneously sought to stimulate economic growth while minimizing its economic dislocations (Berger, 1981; Hall, 1986). As a result, organized labor was provided with by strong employment protection for core workers that, in turn, makes it difficult for employers to pursue strategies of external flexibility (OECD, 2004). At the same time, however, French policy-makers also sought to exercise strategic influence over large companies that, in turn, led to the non-introduction of several firm-level institutional arrangements currently found in coordinated market economies – such as Germany (Goyer, 2011, pp. 1–50). French policy-makers avoided giving extensive legal rights to firm-level works councils that would have acted as constraints on managerial autonomy (Zysman, 1977). In other words, the position of legally based strength of organized labor against external restructuring has not been matched by legal provisions at the firm level that would have enabled French employees to serve as partners in the strategic direction of the firm – as in the German case, for instance (Maurice, Sellier, & Silvestre, 1986).

The above discussion of the importance of causal complexity in the analysis of firm governance leads to three key implications for this study. The first one is that the ability of different firm stakeholders to secure their favorite outcomes does not take place in an institutional vacuum (Campbell, 2004; Hall, 1986). Firms are embedded in different institutional settings across national business systems that, in turn, shape power relations at the firm level (Hall & Thelen, 2009; Whitley, 1999). The second implication suggests that actors can exercise more influence over strategic choices in less institutionally/regulatory constrained arenas (Peteraf & Reed, 2007; Whittington, 1988). These areas are often associated with greater range of possible courses of actions, thereby highlighting how the piecemeal introduction of institutions itself reflects how the sources of power of actors are

implemented in different institutions (Locke & Thelen, 1995). As a result, the translation of foreign practices could work more smoothly in less institutionally constrained domains. The third implication suggests that the presence of less institutionally/regulatory constrained arenas in national economies will be exploited in an asymmetric manner by different categories of firm stakeholders who are themselves characterized by different interests and governed by different internally defined rules (Aguilera & Jackson, 2003).

Anglo-American institutional investors and corporate restructuring: preferences and institutional context

The French economy has long been characterized by the importance of state policies on the governance of companies. State officials implemented policies designed to modernize the economy from above in order to enable French firms to become 'national champions' from the late 1940s onward: regulation of the financial sector designed to influence the allocation of flows in the economy, instauration of controls over inward/outward flows of capital, presence of state ownership in the banking and nonfinancial sectors and the periodic use of currency devaluations to stimulate the economy (Eichengreen, 2007, pp. 113–118; Hall, 1986). In contrast, the last two decades have witnessed the withdrawal of the state from many areas of economic activities, most notably, although not exclusively, through privatizations of the bulk of the largest state-owned companies, the removal of capital controls, the completion of the EU internal market, the deregulation of the financial sector and adhesion to a common European monetary system that is depriving policy-makers of the currency devaluation option (Djelic & Zarlowski, 2005; Hancké, 2002).

The withdrawal of the state from many areas of economic activities and the introduction of market friendly policies have also been followed by the emergence of shareholder value-driven institutional investors from the USA and the UK. The importance of UK/US-based institutional investors in France is first captured by the significant increase of their stake in large domestic companies, from 17.4% to 36.1% from 1990 to 2000, a progression superior as compared to other major Continental European economies (Goyer, 2006, p. 406). The increased ownership by foreign institutional investors in France also comes in the wake of their heightened monitoring and shareholder activism in the home market whereby employee layoffs have been used as a strategic option by which companies are dealing with shareholder value-driven investors, no longer solely as a mechanism for managing their workforce (Budros, 2002; Farber & Hallock, 2009).

Yet, broad statements about increased foreign ownership in France are not specific enough to translate into predictions about their influence over the strategy of portfolio firms. The presence of significant differences in the preferences of institutional investors matters for their differentiated influence on corporate restructuring activities of companies. Different categories of institutional investors – hedge funds, mutual funds and pension funds – constitute investment organizations that are themselves governed by different institutionally defined rules. In particular, they exhibit variation on important characteristics of their internal organization: set of incentives (remuneration) of fund managers, investment horizons and the extent to which the investment strategy is driven by performance concerns versus risk diversification/reduction of management fees (Brav et al., 2008; Goyer, 2006). Managers of hedge funds are mainly driven by performance goals, not by diversification concerns through a long-term index strategy and/or reduction in portfolio management fees. They possess heightened incentives to reap the maximum possible absolute returns, not just achieving targeted mandated minimum returns. Moreover, the compensation of hedge funds' managers derives from the amount of assets

under management (1 to 2%) and, to a substantial extent, from incentive fees (usually 20% of profits). These incentive fees are paid only in the event of the returns on the portfolio exceeding preestablished returns. As such, hedge funds possess strong incentives to monitor and engage with portfolio companies by acquiring firm-specific information about the business strategy of corporations (Kahan & Rock, 2007). Mutual/pension funds, in contrast, are more likely to focus on different aspects of corporate governance practices rather than acquiring detailed and specific knowledge of the business strategy of individual portfolio companies. In comparative terms, shareholder activism by hedge funds is far more aggressive and aimed at the strategy of companies as compared to mutual/pension funds (Brav et al., 2008).

Reflecting on the presence of heterogeneity among institutional investors characterized by different sets of preferences, we split block share purchases into two subgroups: hedge funds versus pension funds/mutual funds. We expect that hedge funds constitute the category of institutional investors, best incentivized to apply pressures on management for the implementation of specific corporate restructuring activities (Kahan & Rock, 2007). The differentiation between categories of institutional investors is particularly important in that corporate restructuring activities are relatively difficult tasks to implement, characteristically different from other goals, such as forcing management to distribute more dividends.

At the same time, however, an exclusive focus on the preferences of different groups of foreign institutional investors is unlikely to be sufficient to provide a full account of the corporate restructuring activities of French companies since the translation of preference inputs into corporate policies is mediated by the embedded institutional context (Campbell, 2004). An important component of our complex causation perspective suggests that local institutional arrangements reduce the range of strategic options for foreign institutional investors, even for highly incentivized and motivated actors. We focus our empirical analysis on the employment protection laws in France, the regulative pillar of institutional arrangements of corporate restructuring (cf. Scott, 2008). Compared to other advanced capitalist economies, French employment legislation is characterized by strict and rigid regulations against employee dismissals that impede and/or significantly delay downsizing strategies via layoffs (Supiot, 2002). Institutional arrangements of employment relations in France provide strong legal employee protection by international standards as measured by the costs of hiring new employees, size of severance payments, definition of unfair dismissal and (lengthy) notice requirements for the initiation of dismissal procedures (Botero et al., 2004; OECD, 2004). Moreover, French employees possess extensive legally entitled information rights over important areas of corporate decisions that seriously limit the ability of French firms to adjust to short-term fluctuations via substantial reductions in the number of permanent employees (Gumbrell-McCormick & Hyman, 2006). In particular, provisions of the French labor code stipulate that companies must draw a 'social plan' that sets out the reinsertion and training measures to be implemented before proceeding to employee layoffs, thereby constraining restructuring strategies based on the rapid use of employee dismissals.

The undertaking of asset divestitures as a part of an overall refocusing strategy on a limited number of core units, in contrast, might encounter less institutional resistance than employee layoffs. A refocusing strategy can be achieved by selling non-core divisions to other companies rather than proceeding to straightforward downsizing in the number of employees, thereby generating cash flows that serve to address liquidity problems as well as constituting a strategic alternative in the context of rigid employment laws (Atanassov & Kim, 2009). Therefore, as our complex causation perspective suggests, UK/US-based

hedge funds could compensate for the limits on their discretion in one realm of choice by using their greater level of discretion in other arenas characterized by reduced institutional constraints (see, e.g., Peteraf & Reed, 2007; Whittington, 1988). The institutional constraints associated with the regulation of dismissals in France are likely to shape the characteristics of the contextual influence of hedge funds even if the latter is considered a far more aggressive category of institutional investors with heightened incentives. The above discussion suggests the following hypothesis.

Hypothesis 1: The acquisition of blockholding stakes by hedge funds in French firms is likely to lead to the implementation of asset divestiture.

The effectiveness of UK/US-based hedge funds as shareholder value-driven institutional investors may also be contingent on the ownership structure of targeted companies given the typical size of their blockholding acquisitions – more than 5% but invariably less than 20% of the firm's outstanding shares. The ability of firms to resist the activism of foreign institutional investors is shaped by the stake of controlling shareholders (Ahmadjian & Robbins, 2005). Noncontrolling investors are not as well placed as insiders in regard to the strategic direction of companies. The circulation of information in France is often internal especially in the presence of a controlling owner (see, e.g., Clark & Wójcik, 2007). The incorporation of the ownership structure of companies in investigating the monitoring role of hedge funds is particularly appropriate given the broad range of ownership structures in France whereby only one-third of listed firms are widely held (Sraer & Thesmar, 2007).

Moreover, the contingent character of the influence of hedge funds in France is likely to reflect another aspect of the ownership structure of domestic companies, namely the legal rights of minority shareholders. Foreign investors can play a more effective monitoring role in ownership-diffused companies since French corporate law is better suited at protecting the rights of minority shareholders from the value destroying actions of managers in ownership diffused settings than at dealing with the strategies of controlling owners seeking to capture private benefits of control in the context of ownership concentration (Conac, Enriques, & Gelter, 2007). Fiduciary duties of care and loyalty are strongly enshrined in French corporate law and are not hierarchically subordinate to the actions of corporate executives. Directors are required to oppose attempts by corporate executives at self-dealing in the spirit of the overall equal treatment for all categories of shareholders (Schmidt, 1999). In contrast, the main shortcoming of French corporate law is that the enforcement of legal mechanisms against controlling shareholders' self-dealing strategies designed to capture private benefits of control is limited in scope, i.e. they are usually limited to cases of bankruptcy (Conac et al., 2007). French courts have been less active in penalizing large owners in conflict-of-interest situations that are not threatening the existence of the company. The above discussion leads us to suggest the following hypothesis.

Hypothesis 2: The ownership concentration of French firms is likely to weaken the positive effects of hedge fund investment on French firms' undertaking employee layoffs.

CEO pay and corporate restructuring

The undertaking of corporate restructuring activities is often associated with difficult decisions and costly efforts. Sanctioning major layoffs could be one of the most important

decisions CEOs would have to make due to its associated negative political and social implications (Roe, 2000). Managers involved in employee layoffs tend to be subject to media criticism and loss of community standing, a nonnegligible issue in the close knit of French corporate networks. CEOs may be reluctant to implement employee layoffs because of their desire for peaceful relations with the workforce (i.e. the 'quiet life') and/or secure private benefits of control at the expense of minority shareholders (Bertrand & Mullainathan, 2003). Moreover, the undertaking of corporate restructuring activities might be also be unsuited to the interests of CEOs themselves given the existing literature on executive pay which suggests that firm size is the most powerful predictor of compensation (Frydman & Jenter, 2010).

The issue of executive compensation constitutes an excellent case that highlights the importance of preferences of actor and the role of institutional frameworks in their translation into corporate outputs. A large body of empirical studies suggests that equity-based compensation provides incentives to help align CEOs' interests and the equity return objectives of minority investors (Frydman & Jenter, 2010; Jensen & Murphy, 1990). Equity-based compensation is different from cash pay, such as salaries and bonuses, in that the latter rewards CEOs for past efforts (accounting-based) but does not explicitly motivate future equity value-enhancing behavior. Previous studies on American companies have provided consistent evidence suggesting that CEO equity-based pay grants an effective internal incentive mechanism to induce CEOs to restructure (Dial & Murphy, 1995). French CEOs, whose incentives could be closely aligned with those of foreign shareholders via equity-based compensation, are more likely to be incentivized to initiate corporate restructuring activities. However, as discussed for Hypothesis 1, highly incentivized CEOs are still facing important institutional constraints in the areas of employment protection in France. Therefore, we expect that equity-based compensation is likely to incentivise CEOs to initiate asset sales, not for the undertaking of employee layoffs.

Hypothesis 3: CEO equity-based compensation incentives are likely to lead the implementation of asset divestiture.

Corporate restructuring and firm performance

Previous studies explored whether and how foreign blockholders influence corporate restructuring activities of domestic companies in economies previously unexposed to demands for the maximization of shareholder value (Ahmadjian & Robbins, 2005; Culpepper, 2005). These rich empirical studies have often conceptualized employee layoffs and asset divestiture as two alternative strategies of shareholder value creation that would result in the enhancement of firm performance. However, we suggest that these two dimensions of corporate restructuring may have different post-effects consequences on the performance of French companies. They might not constitute functionally equivalent mechanisms of shareholder value enhancement since the sources of power of actors, and their identities, are embedded in different institutions.

The strength of organized labor in France has been contingent upon the presence of national employment protection laws that stand in the way of adjustment strategies based on job cuts (Howell, 1992; OECD, 2004). In contrast to Germany and other coordinated market economies, the legal rights of firm-level works councils in France are seriously underdeveloped, thereby reflecting the previous importance of state activism in the management of the economy whereby policy-makers sought to exercise in an unimpeded manner strategic influence over the behavior of top corporate executives (Hall, 1986;

Zysman, 1977). In particular, the weak position of works councils in France has reduced the ability of employees to influence managerial decisions over the development of skills (Maurice et al., 1986). French employees are likely to be particularly concerned about the consequences of reorganization schemes on job security.

The implementation of asset divestitures schemes, on the other hand, might prove politically easier for French corporate executives. Asset divestitures are characterized by a Janus-face character, i.e. they could be implemented as part of a refocusing strategy on a limited number of core activities or, alternatively, could serve as a mechanism to generate cash flows to distribute to protect current employees. The financial consequences of asset divestitures schemes as a strategy of shareholder value enhancement vary across countries according to the relative legal protection of labor vis-à-vis shareholders (Atanassov & Kim, 2009): in flexible labor markets characterized by weaker legal protection for employees, the implementation of asset restructuring schemes is consistently associated with superior financial performance; in rigid labor markets characterized by stronger legal protection for employees, by contrast, the relationship between asset divestiture and financial performance is ambiguous and inconsistent. The reason is that, under the latter institutional scenario, major asset sales are often implemented in order to adjust to economic fluctuations or generate cash flows to address liquidity problems. Strategies of employment reduction are difficult to implement, even if employment reduction might be more economically efficient, in settings characterized by strong legal protection for employees (Botero et al., 2004). If, in the context of strong employment protection, asset divestitures programs serve to protect employee welfare by minimizing employee layoffs, one would not expect strong performance improvement after the implementation of asset divestiture as compared to employee layoffs schemes. The above discussion suggests the following hypothesis.

Hypothesis 4: The effect of employee layoffs on operating performance improvement is likely to be stronger than the effect of asset divestiture on operating performance improvement in the French context.

Methods

Data and sample

Our sample consists of companies in the Paris Stock Exchange SBF 120 between 1998 and 2007. Historical information on the member of the SBF 120 index was used in order to avoid self-selection issues. Consequently, our sample includes firms founded later than 1998 and companies that cease to exist sometime before 2007. Some studies on corporate restructuring focus solely on poorly performing firms because they seek to analyze acute stakeholder conflicts when the size of the firm shrinks (Atanassov & Kim, 2009). We do not restrict our sample to poorly performing firms because the effect of performance on the propensity of a firm's undertaking corporate restructuring is also our concern. We also dropped 22 financial firms from our sample as their financial statements are not readily comparable with those of industrial firms. Finally, 21 companies were additionally excluded due to several reasons, such as being foreign subsidiaries (12), being listed for less than two years (5) and missing data (4). Our final sample includes 130 French companies.

Our observation period begins in 1999 and ends in 2008. The selection of 1999 as the beginning of the observation period reflects the absence of UK- and US-based hedge/mutual funds in France prior to the late 1990s (Goyer, 2011, pp. 51–83). The closing date

of 2008 was selected in order to focus on the challenge generated by the pressures of shareholder value in France on the governance of domestic companies. An analysis of the corporate restructuring activities of French companies prior to the advent of financial crisis is insightful regarding the path dependent character of institutional constraints. The institutional arrangements of employment relations in France, and in other non-liberal market economies, have often been presented as a source of rigidities that prevent companies to adapt quickly to market changes (Siebert, 1997). When examined over the longer term, however, the path dependent character of institutional constraints might result in the sustainability of commitments and other mechanisms of competitive advantage. These forces might be washed out by short-term pressures (Clark & Wójcik, 2007, pp. 103–129; Hall & Thelen, 2009, pp. 22–26). We also conducted some additional analyses for the current economic crisis in order to explore the contextual dimensions of the causal influence of our hypothesized independent variables.

Data on CEO compensation and tenure, ownership structure and board composition were hand-collected from the annual reports of companies and supplemented by the Dafsaliens and Factiva databases. We collected data on foreign investment entries from the French Financial Supervisory Authority (AMF). Compliance with Section L233-7 of the French Commercial Code requires any institutional investor or person has to report shareholding to the AMF and whether the acquired equity stake exceeds or falls below certain threshold values. The AMF and the issuing firm then publicize this information that contains the underlying ownership stake, the date of the transaction, the identity of shareholders, their location of incorporation, and the fraction of shares held after the purchase. Other data, such as stock price and accounting information including the number of employee, and Standard Industrial Classification codes were obtained from Datastream, and asset divestiture data from Thomson One Banker.

Measures

This section describes all our variables and how they are measured. All independent and control variables were lagged by one year relative to dependent variables.

Dependent variables

We define *asset divestiture* as the sale of a subsidiary by the parent firm to another firm with a value of at least US\$10 million. We assigned the value of one if such transaction occurred at least once in a firm during a given year and zero otherwise. We chose a US\$10 million minimum to ensure that only significant divestitures are included in our sample – it is slightly larger than in some other studies on corporate restructuring of European firms (Chikh & Filbien, 2011). We identified 171 divestitures between 1999 and 2008, and the time series variation in the number of asset divestiture is large. The annual number of asset divestitures ranges from as low as 14 cases in 1999 to as high as 22 in 2005.¹

Employee layoffs is a dichotomous variable equal to one when the number of employees of a firm decreased by 5% or more between year t and year $t - 1$. Five percent represents substantial layoffs, which can be separated from a random fluctuation or gradual adjustment in employment level (Ahmadjian & Robbins, 2005). As a robustness check, we perform several tests using both, a discrete variable with the 10% threshold and a continuous variable (i.e. percent change in employment). The results remain qualitatively consistent (results available upon request).

Independent variables

Given the heterogeneity among institutional investors (hedge/mutual/pension funds), we focus on hedge funds' activities and code *hedge fund investment* as one if there is a block share purchase by a hedge fund at the fiscal year-end and zero otherwise. Building on previous studies, we define blockholding investments by UK/US-based hedge funds as the acquisition of an equity stake of at least 5% in a publicly listed company (Brav et al., 2008). We excluded equity stakes which remain in the portfolio firms for less than one month because those shareholdings can be related to other activities, such as short selling.

As for compensation incentives, we draw on previous studies (Brookman, Chang, & Rennie, 2007) by seeking to understand the effect of CEO equity-based compensation with the use of fair value of the compensation. We consider not only newly granted stock options during the current year but also those granted in previous years to better capture CEO incentives (hereinafter *CEO equity-based incentives*). As emphasized by Yermack (1995), one cannot determine whether an executive has an appropriate level of incentives by only examining newly granted equity-based compensation. CEO equity-based incentives are defined as the change in the amount of CEO wealth (thousands) from a 1% change in stock price of the firm (Core & Guay, 1999). It is the sum of delta of each option times the number of the stock options in the CEO option portfolio. The delta of stock options is measured using the Black and Scholes option pricing model adjusted for dividends (Merton, 1973).

In order to ensure that our results are robust to the alternative measure of incentive compensation, we used two other incentive measures considering only newly granted stock options in a given year. The first one, similar to the measure above (equity-based incentives), captures the euro changes (in thousands) in CEO wealth for a 1% change in stock price (Core & Guay, 1999); and the second one is the euro change in CEO wealth for a euro change in firm value (Jensen & Murphy, 1990; Yermack, 1995). The results are virtually the same as those presented in this article, and the significance level is even higher in some tests (results are available upon request).

Ownership concentration is measured as the portion of stakes held by the largest shareholder (excluding UK/US institutional investors) of a firm's outstanding shares.

Control variables

Building on previous studies, we include a set of control variables that are likely to affect the undertaking of corporate restructuring activities: *CEO tenure*, the number of years served in his/her quality of CEO in the firm; percentage of *independent director* defined as those not sitting on the management committee; *firm size* measured as the log of total assets; and *leverage ratio* coded as short- and long-term debts over total assets. These indicators of corporate governance were important in the introduction of the interests of shareholders in the strategic direction of companies in the American context, invariably at the expense of employee (Jacoby, 2005). We also consider block share purchases by other than hedge funds, such as UK/US-based pension funds and mutual funds, and define *other foreign investors* as one if such funds hold 5% or more in the firm at the fiscal year-end. We control for *cross-listings* in US stock exchange markets because listing in a prestigious institutional environment is often regarded as conduit for institutional contagion (Sanders & Tuschke, 2007). Three measures of firm performance are included as managers are under heightened pressure from shareholders to initiate portfolio restructuring if expected cash flows are reduced: *ROA* (return on assets) defined as profits before taxes and extraordinary items divided by total assets; *sales growth* measured as the percentage

growth in sales between year $t - 1$ and year t ; and *stock performance* defined as the one-year holding-period return for the company's common shares over the calendar year before the restructuring event. Strategically unfocused firms might be under stronger pressure to undertake either asset divestitures and/or employee layoffs given that diversification strategies have been increasingly seen as inefficient (Berger & Ofek, 1995). We use two proxies for the *level of diversification*: the number of segments reported by management and a revenue-based Herfindahl index. Finally, we control for possible industry differences and year differences by including *industry* and *year* fixed effects.

Analysis

We used discrete-time event history methodology (Allison, 1984), using logit models of dichotomous outcomes to estimate the hazard of a firm initiating corporate restructuring in a given year for a pooled sample of each firm observed during each of the 10 years studied. Pooling data allow us to take advantage of the greater degree of freedom and to capture dynamic information of time series and the variation due to cross-sections. All variables were updated annually, resulting in annual spells with time-varying covariates except some time-invariant variables, such as cross-listing and industry dummy. Because corporate restructuring activities were repeated events and different odds of a firm initiating restructuring practices may be attributable to a lack of independence of observation and/or unobserved firm-specific factors, coefficient estimates could be incorrect. That is, observations on the same company in different years create serial correlation in the error term, deflate standard errors, and, therefore, inflate t -statistics. Thus, we estimate panel robust standard errors using the cluster option in Stata.

As a robustness check, we used a random-effects logit model which yielded virtually identical results to those presented in this study. However, we were unable to use fixed-effects regression models because a large percentage of firms in the sample never initiated any of corporate governance activities during the study period, and these firms would be dropped in a fixed-effect procedure.

Results

Table 1 presents descriptive statistics and a correlation matrix for the variables used all periods. Figure 1 shows rates of employee layoffs over time and Figure 2 shows rates of asset divestiture. As for foreign blockholdings, there were 152 incidences out of 1061 where foreign institutional investors owned 5% or more equity stakes in French companies. Among the 130 firms in our sample, there are 72 companies that were at least targeted one time by UK/US-based institutional investors between 1998 and 2007. The sample is heterogeneous enough to allow the comparison of non-targeted companies to targeted companies by foreign investors. Mean (median) equity-based incentives indicate the amount of CEOs wealth from a 1% change in their firm stock price is, on average, €63,487 (€2035), that is \$87,207 (\$2795).² Other US studies using the same measure for equity-based incentives report mean (median) of CEO equity-based incentives of their sample firms of \$558,000 (\$117,000) (Core & Guay, 1999) and \$1,036,600 (\$265,500) (Shin, 2008).

Tables 2 and 3 report the results of the tests for our hypotheses regarding asset divestiture and employee layoffs, respectively. Model 1 of each table includes only control variables, while in models 2 through 4, we introduce the predicted effects to test our hypotheses. Model 5 presents the full model with all independent and control variables.

Table 1. Pearson correlation coefficients and descriptive statistics.^a

| Variable | Mean | SD | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | 12 | 13 | 14 | 15 |
|-----------------------------|--------|---------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|-------|
| 1. Asset divestiture | 0.147 | 0.355 | 1.000 | | | | | | | | | | | | | | |
| 2. Employee layoffs | 0.146 | 0.353 | 0.101 | 1.000 | | | | | | | | | | | | | |
| 3. Other foreign investors | 0.143 | 0.351 | 0.023 | 0.049 | 1.000 | | | | | | | | | | | | |
| 4. Hedge fund investment | 0.027 | 0.163 | -0.002 | 0.051 | 0.410 | 1.000 | | | | | | | | | | | |
| 5. CEO equity incentives | 63.487 | 142.684 | 0.208 | -0.071 | -0.030 | -0.057 | 1.000 | | | | | | | | | | |
| 6. American deposit receipt | 0.264 | 0.441 | 0.242 | 0.104 | 0.057 | -0.027 | 0.211 | 1.000 | | | | | | | | | |
| 7. Ownership concentration | 32.355 | 21.977 | -0.246 | -0.096 | -0.177 | -0.020 | -0.154 | -0.265 | 1.000 | | | | | | | | |
| 8. CEO tenure | 8.515 | 8.409 | -0.072 | -0.110 | -0.073 | -0.041 | 0.041 | -0.131 | 0.017 | 1.000 | | | | | | | |
| 9. Diversification | 0.513 | 0.237 | -0.203 | -0.113 | -0.001 | 0.070 | 0.055 | -0.076 | 0.072 | 0.089 | 1.000 | | | | | | |
| 10. ROA | 0.142 | 0.105 | -0.153 | -0.221 | -0.124 | -0.049 | 0.026 | -0.145 | 0.227 | 0.077 | 0.077 | 1.000 | | | | | |
| 11. Sales growth | 16.248 | 31.617 | -0.114 | -0.150 | -0.034 | -0.058 | -0.088 | -0.080 | 0.031 | 0.053 | 0.117 | 0.236 | 1.000 | | | | |
| 12. Stock performance | 15.444 | 48.930 | -0.068 | -0.176 | 0.029 | -0.015 | 0.014 | -0.053 | 0.075 | 0.048 | 0.036 | 0.282 | 0.175 | 1.000 | | | |
| 13. Leverage ratio | 0.256 | 0.158 | 0.051 | 0.095 | 0.012 | -0.009 | 0.006 | 0.018 | -0.086 | -0.026 | 0.021 | -0.184 | -0.041 | -0.060 | 1.000 | | |
| 14. Independent directors | 0.220 | 0.158 | -0.106 | -0.024 | 0.003 | 0.012 | -0.137 | -0.193 | 0.127 | 0.222 | 0.088 | 0.126 | 0.158 | 0.023 | -0.020 | 1.000 | |
| 15. Log (total assets) | 7.798 | 1.907 | 0.406 | 0.077 | -0.024 | -0.098 | 0.380 | 0.381 | -0.229 | -0.198 | -0.153 | -0.256 | -0.271 | -0.110 | 0.174 | -0.361 | 1.000 |

Note: Pearson correlations greater than 0.067 are significant at 0.05 (2-tailed test).

^a n = 720.

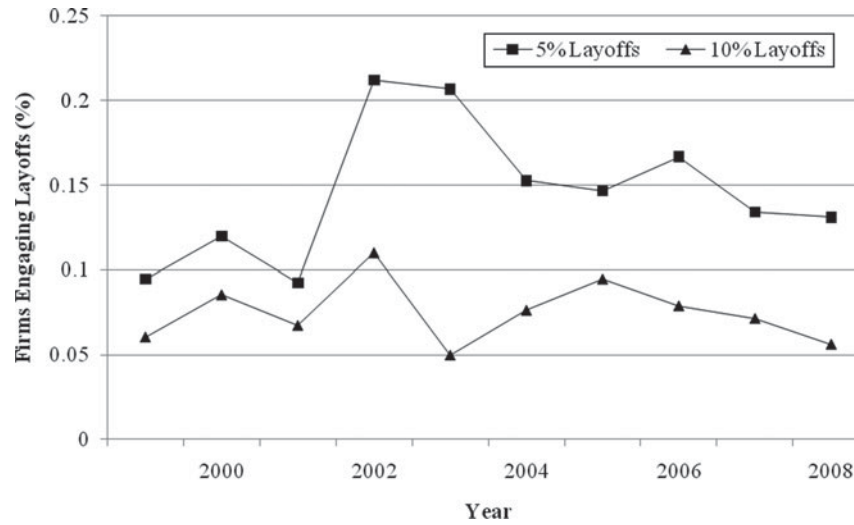


Figure 1. Percentage of French firms engaging in employee layoffs, 1999–2008.

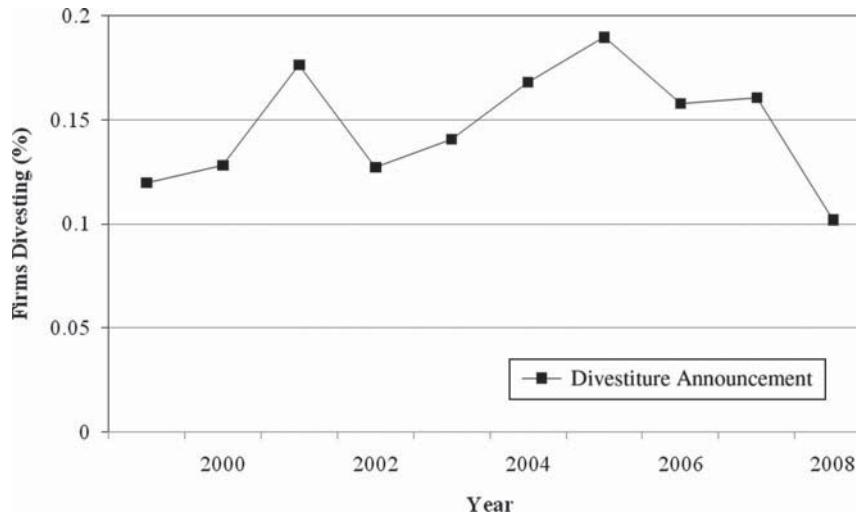


Figure 2. Percentage of French firms engaging in asset divestiture, 1999–2008.

To compare results from asset divestiture and from employee layoffs, we included the predicted effects in Table 3 in the similar fashion to Table 2.

Hypothesis 1 suggested that hedge fund investments have positive effects only on asset divestiture due to the rigid legal employment protection in France. Evidence in model 2 and model 3 (Table 2) provides support for this hypothesis (consistent with H1, $p < 0.037$). As can be seen in model 1, other foreign investors do not have significant effects on asset divestiture. These results suggest the importance of heightened activism by hedge funds as compared to other foreign institutional investors.

As for employee layoffs, we hypothesized that the effect of hedge fund investment may be conditional on the ownership structure of their portfolio firms (Hypothesis 2). The

Table 2. Results of logistic regression analysis for asset divestiture, 1999–2008.

| | <i>Dependent variable: asset divestiture</i> | | | | |
|----------------------------------|--|---------------------|---------------------|---------------------|---------------------|
| | <i>Model 1</i> | <i>Model 2</i> | <i>Model 3</i> | <i>Model 4</i> | <i>Model 5</i> |
| | <i>Baseline</i> | <i>H1</i> | <i>H1</i> | <i>H3</i> | <i>Full model</i> |
| Hedge fund investment (H1) | | 1.613* (0.774) | 1.423† (0.827) | | 1.428† (0.797) |
| CEO equity-based incentives (H3) | | | | 0.001* (0.001) | 0.001* (0.001) |
| Ownership concentration | -0.024** (0.008) | | -0.024** (0.008) | -0.023** (0.007) | -0.023** (0.007) |
| Other foreign investors | -0.022 (0.294) | 0.229 (0.283) | 0.027 (0.293) | -0.032 (0.286) | 0.021 (0.285) |
| American deposit receipt | -0.000 (0.326) | 0.191 (0.338) | -0.002 (0.328) | -0.068 (0.314) | -0.076 (0.314) |
| CEO tenure | 0.014 (0.019) | 0.021 (0.020) | 0.016 (0.019) | 0.006 (0.021) | 0.008 (0.021) |
| Diversification | -2.310** (0.789) | -2.431** (0.780) | -2.370** (0.760) | -2.296** (0.811) | -2.368** (0.782) |
| ROA | -3.662 (2.264) | -2.834 (2.341) | -3.484 (2.308) | -4.183† (2.290) | -4.012† (2.331) |
| Sales growth | -0.006 (0.008) | -0.006 (0.008) | -0.005 (0.008) | -0.005 (0.008) | -0.005 (0.008) |
| Stock performance | -0.006 (0.004) | -0.007† (0.004) | -0.006 (0.004) | -0.006 (0.004) | -0.007† (0.004) |
| Leverage ratio | -0.246 (1.001) | -0.021 (1.099) | -0.147 (1.011) | -0.130 (1.038) | -0.033 (1.044) |
| Independent directors | -2.022† (1.047) | -1.399 (1.064) | -2.030† (1.064) | -1.990† (1.093) | -1.990† (1.109) |
| Log (total assets) | 0.800** (0.117) | 0.899** (0.125) | 0.829** (0.115) | 0.740** (0.122) | 0.768** (0.120) |
| Constant | -5.122** (1.643) | -7.364** (1.555) | -5.574** (1.557) | -4.680** (1.675) | -5.140** (1.592) |
| Log-likelihood | -290.3 | -297.7 | -288.6 | -287.4 | -285.6 |
| No. of firm-year observations | 904 | 904 | 904 | 863 | 863 |
| No. of firms | 122 | 122 | 122 | 114 | 114 |

Note: This table reports the effects of covariates on the probability of a firm undertaking asset divestiture. All data are winsorized at the 1% and 99% levels. The robust standard error was estimated using the cluster option in STATA. All covariates are lagged by one year. Industry and year dummies were included in all models.
† $p < 0.1$, * $p < 0.05$, ** $p < 0.01$.

reason is that the negotiation power of hedge funds is reduced in the presence of a controlling shareholder. As shown in model 2 of Table 3, hedge funds do not have significant effects on employee layoffs without considering the degree of firm ownership concentration, which may suggest that the strong employment protection in France imposes stringent institutional constraints on employee dismissals. Model 3 of Table 3, however, highlights that the interaction term is negative and significant (consistent with H2, $p < 0.039$), and the main effect of hedge fund investment is significantly positive in the presence of the interaction term ($p < 0.043$). The interaction between them is graphically shown in Figure 3, holding other variables at their means. This result demonstrates that the effect of hedge funds on the propensity of French firms initiating

Table 3. Results of logistic regression analysis for employee layoffs, 1999–2008.

| | <i>Dependent variable: employee layoffs</i> | | | | |
|---|---|---------------------|---------------------|---------------------|---------------------|
| | <i>Model 1</i> | <i>Model 2</i> | <i>Model 3</i> | <i>Model 4</i> | <i>Model 5</i> |
| | <i>Baseline</i> | | <i>H2</i> | | <i>Full model</i> |
| Hedge fund investment (H1) | | 0.714 (0.588) | 1.627* (0.804) | | 1.648† (0.848) |
| Hedge fund investment x ownership concentration (H2) | | | −0.036* (0.018) | | −0.040* (0.018) |
| CEO equity-based incentives | | | | −0.002† (0.001) | −0.002† (0.001) |
| Ownership concentration | −0.006 (0.005) | −0.006 (0.005) | −0.004 (0.005) | −0.005 (0.005) | −0.003 (0.005) |
| Other foreign investors | −0.092 (0.284) | −0.055 (0.277) | −0.036 (0.278) | −0.079 (0.280) | −0.019 (0.272) |
| American deposit receipt | 0.183 (0.294) | 0.177 (0.294) | 0.166 (0.296) | 0.190 (0.298) | 0.169 (0.302) |
| CEO tenure | −0.035* (0.015) | −0.034* (0.015) | −0.035* (0.015) | −0.037** (0.014) | −0.037** (0.014) |
| Diversification | −1.244† (0.657) | −1.272* (0.648) | −1.262† (0.648) | −1.022 (0.650) | −1.039 (0.642) |
| ROA | −6.743** (1.655) | −6.681** (1.673) | −6.666** (1.680) | −6.311** (1.784) | −6.211** (1.815) |
| Sales growth | −0.016* (0.008) | −0.016* (0.008) | −0.016* (0.008) | −0.017* (0.008) | −0.017* (0.008) |
| Stock performance | −0.012** (0.003) | −0.012** (0.003) | −0.012** (0.004) | −0.013** (0.004) | −0.013** (0.004) |
| Leverage ratio | 2.326* (0.912) | 2.347* (0.918) | 2.501** (0.926) | 2.790** (0.926) | 3.025** (0.939) |
| Independent directors | −0.640 (0.791) | −0.662 (0.793) | −0.717 (0.797) | −0.497 (0.852) | −0.537 (0.859) |
| Log (total assets) | −0.113 (0.072) | −0.099 (0.074) | −0.094 (0.076) | −0.061 (0.074) | −0.042 (0.079) |
| Constant | 0.078 (1.359) | −0.168 (1.282) | −0.189 (1.311) | −0.705 (1.399) | −1.013 (1.379) |
| Log-likelihood | −332.8 | −332.0 | −330.7 | −319.4 | −317.2 |
| No. of firm-year observations | 902 | 902 | 902 | 861 | 861 |
| No. of firms | 122 | 122 | 122 | 114 | 114 |

Note: This table reports the effects of covariates on the probability of a firm undertaking employee layoffs. All data are winsorized at the 1% and 99% levels. The robust standard error was estimated using the cluster option in STATA. All covariates are lagged by one year. Industry and year dummies were included in all models.

† $p < 0.1$, * $p < 0.05$, ** $p < 0.01$.

employee layoffs is stronger in firms with more diffused ownership structure. Combining the results of Hypotheses 1 and 2, we suggest that hedge fund investment is positively associated with asset divestiture for all sampled firms, whereas the effect of hedge funds on layoffs varies contingent on ownership concentration. Our findings highlight the importance of institutional constraints of employment protection laws (national level) as well as of moderating effects of ownership structure (firm level) on the employment decisions of French companies. In unreported analyses, we examined the effect of other

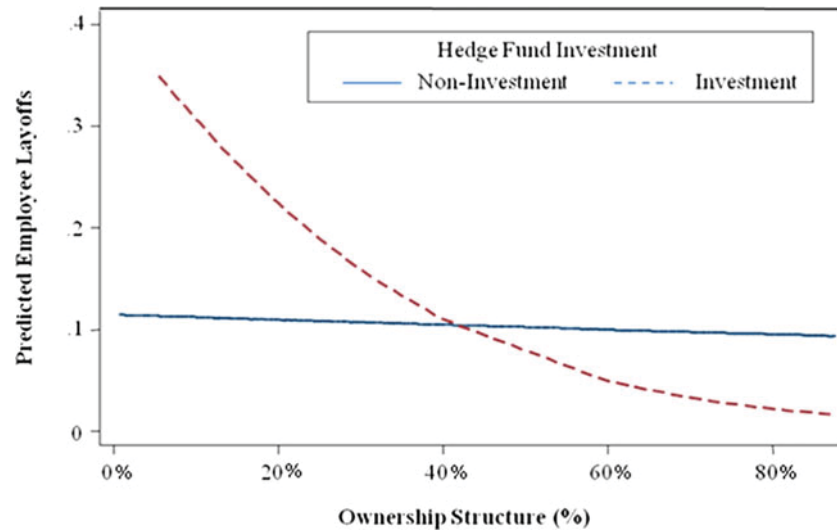


Figure 3. Interaction between hedge fund investment and ownership concentration, employee layoffs.

foreign investors on layoffs and did not find any significant association between them *even* when considering the ownership structure of targeted firms.

In model 4 of Table 2, we examine the effect of equity-based incentives on asset divestiture (Hypothesis 3). The empirical results suggest that CEO equity-based incentives are positively related to the incidence of asset divestiture (consistent with H3, $p < 0.046$). For the purpose of comparative analysis, model 4 of Table 3 examines whether equity-based incentives influences the likelihood of a firm undertaking employee layoffs. Surprisingly, the result indicates that equity-based incentives have marginally significant but negative association with layoffs ($p < 0.075$). This result appears to be counterintuitive because it stands in contrast to the idea that stock-based compensation incentivizes CEOs to proceed to employee layoffs in order to maximize shareholder value. We consider this result as suggestive, if not strong, evidence that the French employment protection law constrain even financially incentivized top executives.

The comparison of the control variables' effects on employee layoffs and asset divestiture illustrates interesting features of corporate restructuring activities. As for capital structure, the effect of leverage ratio is positive and significant on the incidence of layoffs, but not on the case of asset divestiture. It indicates that the increased threat of bankruptcy makes it easier to extract concessions from employees. With respect to firm performance, our findings show that poorly performing firms, measured by ROA and sales growth, are more likely to engage in employment reductions, while there is no significant association between performance and asset divestiture. Many existing studies focusing on the USA highlight the changed nature of workforce reduction – from defensive to offensive (Budros, 1999). That is to say that even a firm that already enjoys strong profits engages in workforce downsizing. Our results, however, tell a different story, namely that poor performance may be still necessary for substantial employment reduction to occur in France.

Short tenured CEOs are more likely to engage in layoffs across all models of Table 3, whereas we do not find such association for asset divestiture. This evidence suggests that CEOs' long relationship with workers deters the undertaking of employee dismissals (Bertrand & Mullainathan, 2003). In addition, all models in Table 2 indicate that the

degree of diversification was significantly and positively associated with the incidence of asset divestiture, uncovering that French firms are more likely to sell their assets to get their business segments consolidated and thus focus on core competencies. Firm size has a significantly positive effect on asset divestiture, but not on employment reduction. This result shows that large firms consisting of many business parts are more likely to sell assets during financial distress due to more flexibility in deciding which assets to sell. Finally, the coefficient on ADRs is not significantly different from zero, indicating weak spillover effect from cross-listing on the US stock markets.

We now turn to Hypothesis 4 where we argue that French firms undertaking employee layoffs exhibit improvement of operating performance relative to those without layoffs; and that French firms engaging in asset divestiture do not show performance improvement as compared to those without asset divestiture. In Table 4, we show the post-effect of each corporate restructuring practice on operating performance (ROA) in the post-restructuring period (year + 1 and year + 2). We used event study methodology with a new dependent variable, namely change in operating performance. Following Barber and Lyon (1996), we measured change in the operating performance of firms by comparing operating

Table 4. Univariate analysis for no downsizing versus downsizing firms: post-downsizing period.

| Variable | No downsizing firms | Downsizing firms | Difference | p-value |
|--|---------------------|--------------------|---------------------------------|------------------|
| Panel A: operating performance (ROA) after employee layoffs | | | | |
| Year 0 | 0.152 (0.132) | 0.087 (0.091) | 0.065*** (0.041)*** | 0.000 (0.000) |
| Year + 1 | 0.148 (0.128) | 0.086 (0.089) | 0.062*** (0.039)*** | 0.000 (0.000) |
| Year + 2 | 0.136 (0.121) | 0.098 (0.095) | 0.039*** (0.026)*** | 0.000 (0.000) |
| Panel B: change in ROA over year after employee layoffs | | | | |
| From year 0 to + 1 | -0.005 (-0.001) | -0.002 (-0.003) | -0.003 (0.002) | 0.645 (0.880) |
| From year 0 to + 2 | -0.013 (-0.005) | 0.015 (0.01) | -0.027*** (-0.015)*** | 0.000 (0.000) |
| Cumulative | -0.016 (-0.008) | 0.012 (0.003) | -0.028** (-0.011)** | 0.001 (0.004) |
| Panel C: operating performance (ROA) after asset divestiture | | | | |
| Year 0 | 0.149 (0.133) | 0.105 (0.107) | 0.045*** (0.027)*** | 0.000 (0.000) |
| Year + 1 | 0.145 (0.129) | 0.102 (0.105) | 0.043*** (0.024)*** | 0.000 (0.000) |
| Year + 2 | 0.136 (0.122) | 0.099 (0.103) | 0.037*** (0.020)*** | 0.000 (0.000) |
| Panel D: change in ROA over year after asset divestiture | | | | |
| From year 0 to + 1 | -0.004 (-0.002) | -0.003 (0.003) | -0.002 (-0.005) [†] | 0.770 (0.067) |
| From year 0 to + 2 | -0.009 (-0.004) | -0.004 (0.000) | -0.005 (-0.004) [†] | 0.413 (0.064) |
| Cumulative | -0.013 (-0.007) | -0.007 (-0.005) | -0.005 (-0.003) | 0.497 (0.127) |

Note: This table reports the difference in changes in corporate performance (ROA) between non-downsizing and downsizing firms. Value in bracket is median.

[†] $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$.

performance in the restructuring year (year 0), and those in year +1 and year +2, respectively. In Table 4, ‘no downsizing firms’ are firms not undertaking employee layoffs (see rows with Panels A and B) and asset divestiture (Panels C and D) in year 0, respectively, while ‘downsizing firms’ are their respective counterparts. The *t*-statistic tests are used for mean differences between subgroups, and the Z-statistic tests from a Wilcoxon rank-sum test are used for median differences (median values in brackets).

Panels A and C report that firms engaging in either employee layoffs or asset divestiture underperform their counterparts respectively in the year 0, +1, and +2, and the difference is statistically significant at the 0.1% significant level ($p < 0.001$). Panels B and D suggest that the change in ROA varies according to the type of restructuring activities: when firms cut jobs, they experience a significant improvement in ROA in year +2 relative to their counterparts. The improvements in performance are statistically significant, and the mean (median) cumulative increase in firms cutting jobs over two years is 0.012 (0.003), which represents an increase of 12.2% (3.16%) in ROA in year 2. We, however, do not find the performance improvement when firms engage in asset divestiture. When comparing the median ROA, operating performance of firms selling their assets is slightly better than their counterparts in each of post-restructuring periods. The mean (median) cumulative increase of restructured firms is not significantly different from their counterparts. The overall results thus provide insightful evidence to support Hypothesis 4.

Finally, we conducted additional tests to uncover the potential effect of the banking and sovereign debt crisis of 2008–2011 on corporate restructuring activities (see Tables 5 and 6). The French economy has been particularly hit as a result of massive losses in the financial sector and overall low economic growth (Goyer & Valdivielso del Real, 2014, pp. 804–806). We seek to explore whether the financial crisis affected the uncovered relations between corporate governance and corporate restructuring. Our analyses yield three insightful results. First, the hedge fund acquisition of blockholding stakes in French companies ceased to influence both indicators (asset divestitures and employee layoffs) of corporate restructuring (see Tables 5 and 6). This is largely explained by their substantial shrinkage with the advent of the banking/financial crisis, accompanied with their substantial losses (Ben-David, Franzoni, & Mousswi, 2012). For the specific case of France, we encountered only seven instances of UK/US-based hedge funds acquiring an investment stake of 5% or more in listed companies in this period.

A second insightful empirical result, on the other hand, shows that the effect of CEO equity-based compensation on restructuring activities remains intact during the crisis period: CEO incentive pay increases the likelihood of French companies undertaking asset divestitures, but has no significant effect on employee layoffs, which corresponds to our findings for the precrisis period (see Tables 5 and 6). It corroborates that irrespective of the macroeconomic context, French employment protection law constrains financially incentivized top executives in the undertaking of employee layoffs. In contrast, CEO equity-based pay does provide sufficient incentives on French executives to implement asset divestiture policies.

The third empirical result reveals that poor performance is still necessary for French companies to undertake employee layoffs even in the postcrisis period, which suggests the continuing salience of the institutional constraint of strong employment protection in France (see Table 6). It also highlights the importance of institutional differences among national business systems as illustrated by the American experience where employee layoffs are also used in good times as a strategic option to deal with institutional investors (Jacoby, 2005).

Table 5. Results of logistic regression analysis for asset divestiture, 2009–2012.

| Variables | Dependent variable: asset divestiture | | | |
|-------------------------------|---------------------------------------|----------------------|----------------------|-----------------------|
| | Model 1 Baseline | Model 2 | Model 3 | Model 4 Full model |
| Hedge fund investment | | 1.636 (1.049) | | 1.220 (0.878) |
| CEO equity-based incentives | | | 0.023* (0.011) | 0.020* (0.010) |
| Ownership concentration | -0.003 (0.010) | -0.002 (0.010) | -0.001 (0.011) | -0.001 (0.010) |
| Other foreign investors | -0.521 (0.892) | -0.478 (0.895) | -0.452 (0.882) | -0.426 (0.887) |
| American deposit receipt | 0.836† (0.453) | 0.807† (0.448) | 0.767† (0.454) | 0.744 (0.453) |
| CEO tenure | 0.041 (0.028) | 0.043 (0.027) | 0.036 (0.028) | 0.039 (0.027) |
| Diversification | -0.216 (0.754) | -0.180 (0.763) | -0.481 (0.811) | -0.437 (0.811) |
| ROA | -4.860† (2.776) | -5.376† (2.845) | -5.774* (2.904) | -6.036* (2.950) |
| Sales growth | 0.012 (0.009) | 0.012 (0.009) | 0.012 (0.008) | 0.012 (0.008) |
| Stock performance | -0.001 (0.007) | -0.002 (0.006) | -0.003 (0.006) | -0.003 (0.006) |
| Leverage ratio | 1.284 (1.573) | 1.313 (1.562) | 1.756 (1.413) | 1.697 (1.425) |
| Log(total assets) | 0.549** (0.162) | 0.593** (0.154) | 0.478** (0.170) | 0.519** (0.161) |
| Constant | -11.854** (3.457) | -12.644** (3.309) | -10.616** (3.527) | -11.331** (3.389) |
| Log-likelihood | -87.82 | -87.14 | -86.18 | -85.81 |
| No. of firm-year observations | 407 | 407 | 407 | 407 |
| No. of firms | 107 | 107 | 107 | 107 |

Note: This table reports the effects of covariates on the probability of a firm undertaking asset divestiture. All data are winsorized at the 1% and 99% levels. The robust standard error was estimated using the cluster option in STATA. All covariates are lagged by one year. Industry and year dummies were included in all models.

† $p < 0.1$, * $p < 0.05$, ** $p < 0.01$.

Discussion and conclusion

Analyses in social sciences are often framed as a paradigm war between different theoretical perspectives. Scholars seek to demonstrate the explanatory power of their 'selected' independent variable by measuring its direct effects on outcomes. The results are often disappointing as these studies focusing on single explanations invariably fail to capture the presence of strategic interaction in processes of causal complexity. In qualitative studies, researchers seek to demonstrate the explanatory power of their independent variable by holding other factors constant. By holding institutions/preferences constant, scholars aim to highlight how changing preferences/institutions produces different values on the dependent variable. The challenge is that the causal influence of a hypothesized independent variable is contingent upon the specific context of causal complexity causal in which it is embedded (Gourevitch, 1999; Mahoney, 2008).

In quantitative studies, the use of regression techniques is often designed to identify the average effect of the 'selected' independent variable across a large number of

Table 6. Results of logistic regression analysis for employee layoffs, 2009–2012.

| Variables | Dependent variable: employee layoffs | | | |
|-------------------------------|--------------------------------------|--------------------|--------------------|-----------------------|
| | Model 1 Baseline | Model 2 | Model 3 | Model 4 Full model |
| Hedge fund investment | | −0.052 (0.850) | | 0.027 (0.884) |
| CEO equity-based incentives | | | −0.008 (0.015) | −0.009 (0.015) |
| Ownership concentration | 0.003 (0.008) | 0.003 (0.008) | 0.002 (0.008) | 0.002 (0.008) |
| Other foreign investors | −0.608 (0.469) | −0.610 (0.474) | −0.631 (0.471) | −0.630 (0.475) |
| American deposit receipt | 0.387 (0.419) | 0.388 (0.419) | 0.408 (0.416) | 0.408 (0.415) |
| CEO tenure | −0.022 (0.020) | −0.022 (0.020) | −0.021 (0.020) | −0.021 (0.020) |
| Diversification | −0.462 (0.599) | −0.466 (0.601) | −0.447 (0.604) | −0.445 (0.609) |
| ROA | −4.092* (1.975) | −4.085* (1.957) | −3.936* (1.988) | −3.939* (1.974) |
| Sales growth | −0.018 (0.013) | −0.018 (0.013) | −0.018 (0.013) | −0.018 (0.013) |
| Stock performance | −0.016* (0.008) | −0.016* (0.008) | −0.016* (0.008) | −0.016* (0.008) |
| Leverage ratio | 3.815** (1.137) | 3.817** (1.145) | 3.783** (1.137) | 3.782** (1.145) |
| Log(total assets) | −0.054 (0.145) | −0.055 (0.147) | −0.038 (0.156) | −0.038 (0.160) |
| Constant | −2.790 (3.050) | −2.774 (3.072) | −3.002 (3.211) | −3.011 (3.256) |
| Log-likelihood | −153.1 | −153.1 | −152.9 | −152.9 |
| No. of firm-year observations | 407 | 407 | 407 | 407 |
| No. of firms | 107 | 107 | 107 | 107 |

Note: This table reports the effects of covariates on the probability of a firm undertaking employee layoffs. All data are winsorized at the 1% and 99% levels. The robust standard error was estimated using the cluster option in STATA. All covariates are lagged by one year. Industry and year dummies were included in all models.

† $p < 0.1$, * $p < 0.05$, ** $p < 0.01$.

observations. The aim is to uncover the independent variable with the highest predictive power as compared to other (competing) hypothesized variables. The results of these large N studies have also been disappointing – particularly in the area of employment relations. For instance, the impressive number of empirical studies of employee downsizing in the USA is characterized by the overall lack of consistent results that, in turn, reflects the limited focus of the bulk of these empirical investigations on the direct effects of hypothesized independent variables (for critical overviews, see Datta, Guthrie, Basuil, & Pandey, 2010; Dencker, 2012). In other words, the vast majority of these empirical analyses have failed to incorporate the moderating effects of contextual factors in understanding their influence on the dependent variable. This shortcoming is not only methodological, but also reflects important assumptions about the nature of causation in social sciences (Hall, 2003). The insights of moderating variables do not simply consist in producing consistent (and statistically significant) results, but also incorporate the notion of causal complexity.

The main theoretical contribution of our study is to demonstrate that the influence of UK/US-based institutional investors and CEO equity-based compensation on the corporate restructuring activities of French firms is contingent on how institutions and actor preferences interact to generate an outcome that would be substantially different without their joint presence. The first component of our complex causation perspective highlights the constraining role of institutions on the strategic behavior of actors and how the translation of stakeholder preferences, even for powerful and motivated actors, into corporate outputs is contingent on the embedded institutional context. The second component of our complex causation perspective illustrates how the presence of groups with different interests, and governed by different internally defined rules, affect their strategic decisions under stable institutional arrangements.

Our empirical study presents a more nuanced account of the influence of UK/US-based institutional investors and imported strategic practices (CEO equity-based compensation) at two levels. First, our empirical findings suggest that the presence of variations in the interests and preferences of Anglo-American institutional investors brings key insights to the investigation of corporate restructuring in France. While the investment allocation of foreign investors when analyzed as an aggregate group was not significantly associated with restructuring activities, we uncover that hedge fund investment is significant and positively associated. Even after controlling for firm performance, financial condition and diversification status, corporate restructuring activities in France are more likely to occur in the presence of UK/US-based hedge funds as blockholders. Different categories of institutional investors encompass key variations regarding their incentive structures, time horizons and investment goals. In other words, strategic choices of actors do not derive mechanistically from an institutional framework. The opportunities provided by market liberalizing moves in the French economy have not been 'seized' equally by foreign funds. Preferences do matter.

Nonetheless, the effects associated with hedge fund investments on corporate restructuring vary across the type of restructuring practices as well as the ownership structure of targeted firms. The investments of hedge funds have a positive impact on asset divestiture, whereas their effects on employee layoffs are positive and significant only in the case of companies with diffused ownership. We suggest this asymmetric influence of foreign actors on corporate restructuring in France highlights the importance of institutional constraints associated with rigid labor laws on employee dismissals. The presence of an institutional setting characterized by strong employment protection reduces the ability of highly incentivized hedge funds to force firms to undertake employee layoffs. The capacities of actors for strategic choice are important but not without limits since the translation of their preferences into corporate actions is mediated by the presence of institutional constraints in the area of employment relations. Institutions do matter.

The constraining character of institutions is also observed with regard to the nature of French layoffs as compared to the USA. The literature on employee dismissals has extensively documented the changed nature of workforce downsizing – from defensive to offensive – in the USA since the 1980s (Budros, 1999). Employee layoffs are increasingly used as a tool for earnings management (managing investor pressure and boosting stock price). Our empirical results, however, indicate that poor firm performance in France is significantly associated with the incidence of employee layoffs. Not only stock performance but also operating performance has a strong negative effect on the propensity of employee dismissals. Moreover, the demand side, as measured by sales growth, is also a significant predictor for layoff decisions. Institutions do matter.

Second, our empirical evidence suggests that CEO equity-based compensation may work in France as an incentive mechanism as prescribed in the USA, but in a

circumscribed institutional context. CEO stock option incentives are effective in incentivizing French CEOs to initiate asset divestitures, but not enough for them to induce layoffs due to presence of institutional constraints French employment law. In other words, CEO equity-based compensation has been used to implement corporate restructuring in less institutional areas. Institutions and preferences do matter.

To conclude, we think that our theoretical framework and empirical findings help us move beyond often sterile methodological debates between qualitative and quantitative approaches. The interaction between institutional arrangements and actors' preferences highlights a unique conceptualization of causation in social sciences, namely complexity of processes.

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Notes

1. We also used an alternative measure for asset divestiture equal to one when total assets of a firm are reduced by 5% or more, while there is no 5% or more decrease in the number of employees in the same year. The results remain qualitatively unchanged.
2. The 2007 annual average dollar–euro exchange rate was applied, i.e. 1 dollar = 0.728 euro.

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