UNDERSTANDING PRIMARY STAKEHOLDERS OF A FIRM IN RESPONSE TO MARKET INTEGRATION IN THE EUROPEAN UNION

Volkswagen, 1960-2005

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Muurame, February 22, 2009
Murat Akpinar

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LIST OF ABBREVIATIONS

ACEA	European Automobile Manufacturers Association
ASEAN	Association of South East Asian Nations
AWE	Automobilwerk Eisenach
AWZ	Volkseigener Betrieb Sachsenring Automobilwerke Zwickau
BASF	Badische Anilin und Soda Fabrik
BER 1400/2002	Block exemption regulation 1400/2002
BER 1475/95	Block exemption regulation 1475/95
BL	British Leyland
BLMC	British Leyland Motor Company
BMC	British Motor Corporation
BMW	Bayerische Motoren Werke AG
CECRA	European Council for Motor Trades and Repairs
CEO	Chief Executive Officer
DG	Directorate-General
ECSC	European Coal and Steel Community
EEA	European Economic Area
EEC	European Economic Community
EFTA	European Free Trade Area
EU	European Union
FDI	Foreign direct investment
GATT	General Agreement on Trade and Tariffs
GM	General Motors
MERCOSUR	Southern Common Market
MNE	Multinational enterprise
NAFTA	North American Free Trade Agreement
NELLI	National Electronic Library Interface
NSU	Neckarsulm
Porsche	Dr.Ing.h.c.F. Porsche AG
PP&E	Property, plant & equipment
PSA	Peugeot Société Anonyme Peugeot Citroën
R&D	Research and development
SAAB	Svenska Aeroplan Aktiebolaget
SEAT	Sociedad Española de Automóviles de Turismo S.A.
SME	Small and medium-sized enterprise

UK	United Kingdom
USA	United States of America
VW	Volkswagen Group
WTO	World Trade Organization

1 INTRODUCTION

This research is about a firm’s primary stakeholders, in other words actors who are dependent on the firm in order to achieve their own goals and on whom the firm is dependent for its existence (Rhenman 1964, 2/12; Clarkson 1995, 106)[1]. These actors include shareholders, employees, suppliers, customers, dealers, creditors, and the home government. The aim of the research is to enhance understanding of how primary stakeholders contribute to resolving the threats that may arise for some firms from market integration in the European Union (EU). In this research a threat refers to a forthcoming development that is likely to have an important negative impact on the ability of the firm to meet its goals (Ansoff 1980, 133)[2], and a primary stakeholder contribution refers to an act of the primary stakeholder which plays a major role in the resolution of the threat.

1.1 Environments and Challenges

Firms operate in challenging environments (Lawrence and Lorsch 1967). The environment is a broad concept, and thus it may be useful to classify the environments of the firm.

According to Dill (1958, 424), the task environment comprises the parts of the environment that are relevant to goal setting and goal attainment. It includes customers (and distributors), suppliers (of materials, labor, equipment and capital), competitors (for markets and resources), and regulatory organizations (e.g., government agencies).

The task environment could be subdivided into the market and the non-market (institutional) environment. The former refers to economic interactions intermediated by private agreements, and the latter to social, political, and legal interactions intermediated by the society, the government and its regulatory organizations, and the media (Baron 1995; Boddewyn 2003). Whereas customers, suppliers, and competitors belong to the market

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1 See section 2.3 for further discussion on primary stakeholders.

2 See section 1.1 to compare it with challenge and opportunity and section 1.2 for reasons behind the choice to focus on threats.

environment, regulatory organizations belong to the non-market environment (see Figure 1).

Industrial-organization theorists focus on the industry, which is a subset of the market environment. It comprises a group of firms producing products that are close substitutes for each other (Bain 1972, 34; Porter 1980, 5). According to this definition, the industry includes competitors and excludes other market actors such as suppliers and customers (see Figure 1).

The non-market environment can be subdivided into the political-legal and the social (Baron 1995; Boddewyn 2003). The former consists of organizations[3] that regulate market rules (North 1990). In view of the various regional-integration movements (e.g., the EU; the North American Free Trade Agreement – NAFTA, the Association of South East Asian Nations – ASEAN, and the Southern Common Market – MERCOSUR), it could be further divided into the national (comprising the government and its regulatory organizations) and the international (comprising supranational regulatory organizations). The social environment embraces the society and its norms (see Figure 1).

Task environment			
Market	Nonmarket (institutional)		
Suppliers Industry: competitors Customers	Political-legal		Social
	International	National	
	Supranational regulatory organizations	Government and its regulatory organizations	Society Norms

Figure 1. A classification of the firm's environments [4]

[3] In this research I prefer to use the term organization rather than institution because scholars of institutional theory define institutions in the broad sense in terms of socially habituated behavior (Hodgson 1994, 64).

[4] Compiled from the definitions given by Dill 1958; Bain 1972; Porter 1980; Baron 1995; Boddewyn 2003.

The international political-legal environment has been changing with increasing globalization and regional market integration. Levitt (1983) defines globalization as increasing interdependencies among world markets. Stiglitz (2002) defines it as the removal of barriers to free trade and the closer integration of national economies. In that respect, globalization implies worldwide accessibility to the same products and the same resources, thus increasing competition across borders (Zdravkovic 2007). Globalization implies also the declining autonomy of the nation state (Eden and Lenway 2001; Buckley and Ghauri 2004). The General Agreement on Tariffs and Trade (GATT), which was first signed in 1947, and its successor, the World Trade Organization (WTO), which was established on January 1, 1995, have been contributing to globalization through lowering barriers to cross-border trade.

In parallel to the above definitions on globalization, *regional market integration refers to the cross-border integration of national production, exchange and financial markets at a regional level with free flow of goods, services, labor and capital (i.e. negative integration: Scott 1996) along with the shift of policy-making power from governments of member countries to supranational regulatory organizations (i.e. positive integration: Scott 1996)*. The EU, NAFTA, ASEAN, and MERCOSUR have achieved market integration across borders at different levels. Consequently, supranational regulatory organizations have emerged as powerful actors, and the importance of the role of the nation state has been diminishing (Mercado et al. 2001; Eden and Lenway 2001; Buckley and Ghauri 2004).

These changes in the international political-legal environments have created challenges for firms and affected their operations (Tuulenmäki and Virtanen 1990; Seristö 1999). A challenge is a summons that may be threatening, provocative, stimulating or inciting (Merriam-Webster’s online dictionary 2007). In this research I adopt the definition used by Ansoff (1980, 133) and consider a challenge from the environment as a forthcoming development that is likely to have an important impact on the ability of the firm to meet its goals. A challenge and a threat are sometimes used synonymously (e.g., challenges and opportunities) (cf. Pitelis 2007, 53; German Association of the Automotive Industry 2007, 15). In my opinion, this use of the term is not necessarily correct: a challenge may be a threat for some firms and an opportunity for others at the same time.

I could perhaps explain this more clearly with the help of an example. The global oil crisis in 1973 triggered a change in consumer preferences in the USA from large cars towards smaller models that were more economical in terms of fuel usage. This change was a challenge for car manufacturers. It implied a threat to the Big Three American manufacturers, namely General

Motors (GM), Ford and Chrysler, which were catering large cars for the American market. At the same time, it implied an opportunity for manufacturers of small cars such as Japanese companies to penetrate the American market. As this example illustrates, I believe that challenge should not be used as a synonym for threat, and that both threats and opportunities may be challenging.

This is the case for globalization and regional market integration in that there are opportunities as well as threats (cf. Held et al. 1999; Stiglitz 2002). The opportunities of regional market integration may include decreased costs due to a reduced need to adapt to each market separately, increased cooperation with regional partners, ease of access to a larger market, and consequent economies of scale and increased profit margins (Cecchini 1988; Seristö 1999). The eased entry of competitive international players into home markets, on the other hand, may be a threat, arising from the fact that companies in the same industry compete for similar limited resources and markets (Pfeffer and Salancik 1978). Increased competition may result in reduced profit margins and the closure of the least efficient firms, and make smaller firms vulnerable to takeovers (cf. Seristö 1999; Mercado et al. 2001; Mirola 2006; Lévy 2007).

This research focuses on the EU and its car industry because the degree of market integration in the EU is the highest in the world (cf. Scott 1996; Mercado et al. 2001), and its highly competitive car industry has been subject to threats from market integration. The EU is a community of 27 member countries with a total population of about 487 million, and it is the largest single market for cars. Threats of regional market integration arise as a larger single market heightens regional competition (Zdravkovic 2007) and home governments hand over some of their autonomy to supranational regulatory organizations (Mercado et al. 2001; Eden and Lenway 2001; Buckley and Ghauri 2004) whose decisions may not be equally favored by different member countries and different groups of stakeholders. By car industry I mean the production and marketing of passenger cars[5]. Passenger cars in use in the EU-25 constitute 38 percent of the world total, which puts it in the top position, followed by the United States of America (USA) (24 percent) and Japan (10 percent) (cf. Licht et al. 2005, 81). Examples of threats on the European car industry include the threat of Japanese invasion following the

[5] The automotive industry covers the production and marketing of passenger cars, light commercial vehicles, trucks, and buses and coaches. Passenger cars are designed for passenger transportation and have a maximum of eight seats in addition to the driver's seat (Commission of the European Communities 2004, 160). Buses and coaches are also for passenger transportation but have more than eight seats in addition to the driver's seat, and weigh over five tons; light commercial vehicles are designed to transport goods, and weigh less than 3.5 tons; and trucks serve the same purpose but weigh over 3.5 tons (ibid.).

creation of the single market in the EU on January 1, 1993 (cf. Keller 1993, 24; German Association of the Automotive Industry 2007), the threat of possible loss of control over distribution as well as repair & maintenance networks following block exemption regulation 1400/2002 (BER 1400/2002), the threat of possible hostile takeovers by hedge funds[6] with the free flow of capital in the EU[7], and the threat of complying with the tight environmental requirements of the European Commission[8].

1.2 The Motivation for the Research

The aim of this research is to develop understanding regarding the contributions of primary stakeholders to resolving the threats that may arise for some firms from market integration in the EU.

As mentioned in the previous section[9], market integration in the EU has created challenges in the form of opportunities and threats. I deliberately chose to focus on threats because while the positive impacts of market integration in the EU have been explained well enough (cf. Viner 1950; Cecchini 1988; Seristö 1999), the negative impacts need further research attention (Eden and Lenway 2001). In my opinion, there is need to conduct such research especially from the perspective of stakeholders.

I chose to focus on threats also because modeling primary stakeholder behavior in the case of opportunities and threats simultaneously in the same piece of research may be difficult to achieve. A threat often implies a survival issue and requires a strategic response. When survival is the issue, primary stakeholders are likely to be the group that is most affected by the threat. It may be different in the case of an opportunity. The firm and its primary stakeholders may not perceive it at all, and even if they do, the firm may decide not to realize it for reasons of managerial preference or the unavailability of resources to be allocated (Penrose 1959). Furthermore, if the firm possesses the necessary resources, it may wish to realize the opportunity

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6 Unlike long-term investment funds, hedge funds are usually known as high-risk funds with short-term investments.

7 VW, for example, has been such a target due to its low price/earnings ratio (Juchemich 2004). Market analysts believed that the seven VW brands would be worth more independently than the current market value of the whole company (The Economist 2005a).

8 One aim was to reduce carbon dioxide emissions in the EU to an average of 120 grams per kilometer for each car manufacturer by 2012 (Commission of the European Communities 2006a). This is an ambitious target given the fact that Europe has an average carbon dioxide emission of 174 g/km (cf. Cleff, Heneric, and Spielkamp 2005, 173).

9 In this work, a section refers to a part of a chapter (e.g., section 1.1 refers to the first part of Chapter 1). A sub-section refers to a part of a section (e.g., sub-section 1.1.1 refers to the first part of section 1.1).

alone. Besides, an opportunity for the firm may not be an opportunity for its primary stakeholders: it may even be a threat for any particular one. Thus, the behavior of the firm and its primary stakeholders may be difficult to model in the case of an opportunity.

My choice of focus should not imply a negative image about market integration in the EU, though. As the Commission of the European Communities (2006a, 7) emphasizes, the strategic objective of the EU is to work towards creating long-term prosperity in Europe through sustainable growth. The numerous benefits, however, should not discourage us from researching the threats for some firms.

Strategically responding to a threat refers to actions taken to eliminate it or to avoid its negative impacts. A strategic response may range on a continuum from being reactive to being proactive depending on the perceptions and capabilities of the executive management, as well as the nature of the threat and the corresponding information available (Ansoff 1984; Sandberg 2005). There may also be more than one type of strategic response to a particular threat.

When a firm is under threat there may be significant negative implications for some of its stakeholders. Clarkson (1995) differentiates between primary and secondary stakeholders. In my opinion, primary stakeholders are covered in the narrow-sense definition of stakeholders given by Rhenman (1964, 2/12) and include shareholders, employees, customers, suppliers, dealers, creditors, and the home government. Secondary stakeholders are included in the wide-sense definition given by Freeman (1984, 46)[10], and include competitors, the media, special-interest groups, supranational organizations, and society as a whole. Primary stakeholders are in continuous relationships of interdependence with the firm in that they provide inputs and receive compensation in return (Ahlstedt and Jahnukainen 1971). In my understanding, this is the key difference between the two: secondary stakeholders are not in such a relationship. In this research I deliberately differentiated between primary stakeholders and secondary stakeholders, and focused only on the former because I assume that they are the ones that are directly affected by threats due to their interdependence with the firm.

A key motivation for this research came from my observations of the car industry. The more successful firms in this industry are from Japan and Germany, two countries in which stakeholder interests take precedence over shareholder interests (Pries 2005). In contrast, car manufacturers from the USA and the United Kingdom (UK), countries in which shareholder interests

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[10] Stakeholders are individuals or groups who can affect or who are affected by the achievement of a firm’s goals.

take precedence over the interests of other stakeholders, have performed poorly. The big British car manufacturers went bankrupt in the 1960s and 1970s. As of 2005, the credibility ratings of Ford and GM, the two major American car manufacturers, have been equivalent to junk bonds (cf. Pries 2006). I thought that this warranted further research.

The motivation for taking a stakeholder perspective arose from the need to understand firm-stakeholder relationships from the stakeholders' perspective (cf. Frooman 1999; Butterfield et al. 2004; Frooman and Murrell 2005). It is indeed the primary aim of this research to make a theoretical contribution in this direction. On the administrative level, this research may have implications for primary stakeholders, executive managers of firms that are under threat, and policy makers at the European Commission. The possible benefits for them may include the following.

First, it may help primary stakeholders to understand what they can do in order to resolve threats. Secondly, it may help executive managers in assessing the differing abilities of their primary stakeholders in resolving threats. Executive managers could perhaps take the lead and coordinate the abilities of their primary stakeholders in working towards resolution. Finally, policy makers at the European Commission are drivers of market integration in the EU. This research may help them to understand how various primary stakeholders are affected by their policies. I believe that such an understanding may be relevant today when the future of the EU is being questioned as citizens of France, Holland and Ireland have rejected by referendum the Treaty of Lisbon.

1.3 The Theoretical Relevance and Positioning of the Research

Stakeholder theory is deeply rooted in Continental Europe (especially in Germany and Holland)[11] and in the Nordic countries[12]. It has emerged as a response to the shareholder theory that prevails in the Anglo-Saxon countries (Freeman and Reed 1983; Smith 2003). Whereas shareholder theory emphasizes creating value for shareholders through profit maximization (Friedman 1970), stakeholder theory argues that executive managers in the firm need to pay attention to the interests of all stakeholders and not just to those of shareholders (Rhenman 1964; Freeman 1984). Whereas shareholder theory views shareholders as the sole bearers of risk in the firm, all stakeholders carry risk according to stakeholder theory (Kochan and

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[11] See Corporate Finance (2002a).

[12] See Näsi (1995a) for a review of literature from the Nordic countries.

Rubinstein 2000). Therefore, executive managers may need to consider and fulfill in a balanced manner stakeholders' needs in order for the firm to continue to exist (Brenner 1995).

One problem with stakeholder theory, in my opinion, is that it has evolved from the perspective of the firm according to which stakeholders are viewed as passive actors. This is interesting because it was more than 30 years ago when Dill (1975) first observed that some stakeholders sought active participation in managerial decision-making. Let me explain this further by looking into the three 'divergent' streams in stakeholder theory, the descriptive, the instrumental, and the normative (Donaldson and Preston 1995; Freeman 1999) (see Table 1).

Table 1. Streams of stakeholder theory (adapted from Donaldson and Preston 1995)

Name of stream	Descriptive	Instrumental	Normative
Focus of stream	Classification of stakeholders, actual behaviors of the firm and stakeholders	Impact of stakeholder management on corporate performance	Ethics, corporate social responsibility

The descriptive stream focuses on the behavior of the firm and its stakeholders. The topics addressed have predominantly evolved around the definition and classification of stakeholders (e.g., Freeman and Reed 1983; Clarkson 1995; Mitchell et al. 1997), and research from the stakeholders' perspective is relatively scarce (Frooman 1999; Frooman and Murrel 2005). Recently there is research which examines how stakeholders can influence firms in their decision-making (cf. King 2008; Zietsma and Winn 2008), but as scholars (e.g., Jones and Wicks 1999; Butterfield et al. 2004) confess, this stream is the least developed of the three. There is a need to learn more about firm-stakeholder and stakeholder-stakeholder relationships, especially from the stakeholders' point of view (Frooman 1999; Butterfield et al. 2004). In particular, the willingness of stakeholders to allocate resources to helping or harming the firm is an area deserving a better understanding (Freeman 1984, 26).

The instrumental stream argues that paying attention to stakeholder interests improves corporate performance (cf. Cochran and Wood 1984; Jones 1995; Berman et al. 1999; Hillman and Keim 2001)[13]. This argument is purely

[13] This argument is highly debated among scholars of this stream. See section 2.2 for more on this.

from the firm’s point of view in that stakeholders are viewed as a means to achieving goals.

The normative stream focuses on topics such as business ethics, moral behavior, and corporate social responsibility (cf. Beauchamp and Bowie 1983; Elias and Dees 1997; Carroll and Buchholtz 2003; Garriga and Melé 2004). The perspective is also that of the firm in that it prescribes how executive managers should treat the firm’s stakeholders.

This research views the firm as an organization through which a number of actors (i.e. primary stakeholders) serve their own purposes (through compensation) while contributing to the firm’s existence (through inputs) (Rhenman 1964; Ahlstedt and Jahnukainen 1971). The primary aim is to contribute to the descriptive stream of stakeholder theory by taking a stakeholder perspective and studying primary stakeholder contributions to resolving the threats arising from market integration in the EU.

This work also deserves a place in the field of international business. This is because this research deals with the highly competitive European car industry, which accommodates some of the world’s largest multinational enterprises (MNEs) which are a main research object in international business. As Peng (2004) suggests, the boundaries of international business research are reasonably open to beneficial scholarly exchanges. Zettinig and Vincze (2008) identify increasing economic interdependencies (e.g., the EU) and their impact on international business as a top priority in their list of critical issues requiring research attention in this field. Eden and Lenway (2001) and Buckley (2002) also recognize the challenges of globalization as one of the key topics to be included on the future research agenda. Therefore, this research deserves a place in international business also because it tackles primary stakeholders in response to regional market integration.

Management research on strategic responses to challenges from the environment has evolved around four perspectives: natural selection, contingency, strategic choice, and collective action (cf. Astley and Van de Ven 1983; Child et al. 2003). In all of these perspectives the focus is on the firm and its management. With emphasis on stakeholders in resolving threats from the environment this research may also provide new insights for this stream of literature.

In addition to the above, this research may be of further academic value in answering some of the earlier criticisms and recommendations. For example, focusing on threats originating from the non-market environment may be valuable in answering criticisms from North (1990) and Oliver (1997a) that this is an environment that has not received adequate attention from economists. Studying events longitudinally over long periods of time may be of value because this is relatively rare in management research (Jones and

Khanna 2006). Finally, differentiating between various types of stakeholders may further contribute to research on stakeholders as recommended by Harrison and Freeman (1999) and Winn (2001).

1.4 The Research Questions

This research starts from the assumption that market integration in the EU may impose challenges for firms and their primary stakeholders by liberating market forces across borders and thus fostering regional competition as well as through decisions of supranational regulatory organizations. For some firms these challenges may be threats to existing operations, and for others they may be opportunities waiting to be exploited (see Figure 2).

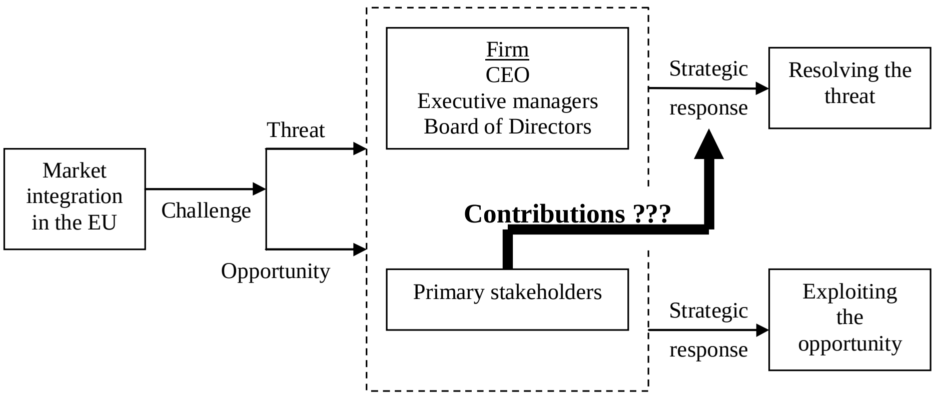

Figure 2. The problem setting

As discussed earlier in section 1.2, this research focuses on threats. I assume that threats to the firm[14] may threaten also some of the primary stakeholders in the system[15], and that the system needs to respond to the threats and resolve them. A strategic response that resolves a threat could be undertaken solely by the firm and need not involve any of its primary stakeholders. This kind of strategic response is not the focus of this research.

14 There are different levels of management at different locations, including executive, divisional, and operational managers, who are involved at different levels of decision-making (Bower and Gilbert 2007). Executive managers are the key decision makers, and the most influential executive is the chief executive officer (CEO). Critical decisions require the approval of the Board of Directors, which is a controlling committee selected by shareholders. These actors are highlighted in Figure 2 under the firm.

15 I view the firm and its primary stakeholders as elements of an open social system due to their interdependence. See section 2.5 for discussion on this system.

Rather, as highlighted by the thick arrow and bold question-marks in Figure 2, the aim is to find out how various types of primary stakeholders contribute to resolving the threats arising from market integration in the EU. This leads to the first research question.

Research Question 1: *In what ways do various types of primary stakeholders contribute to resolving the threats of market integration in the EU?*

Addressing research question 1 requires first a typology of primary stakeholder contributions. A typology is a classification of types, the implication being that among a large number of alternatives only a small number of combinations actually occur, and all others are rare or nonexistent (Stinchombe 1968, 47). It does not, however, offer any explanation or prediction as to which type of primary stakeholder can contribute in what way and under what circumstances. This would require an understanding of the determinants behind the choice of a particular type of contribution. Research question 2 addresses this issue.

Research Question 2: *What determines the type of contributions various primary stakeholders make in resolving the threats of market integration in the EU?*

This is an important question because it is only after answering research question 2 that I can go back and answer research question 1. The answering of these two research questions should contribute to increase understanding on primary stakeholders of a firm in response to market integration in the EU. Based on my literature review I conclude that there is not an available theoretical framework to answer the questions directly. Therefore, there is a research need for a theory of stakeholder contributions in resolving threats arising from market integration in the EU. This research aims to develop such theory and thus fulfill this research need.

1.5 The Structure of the Thesis

The research strategy was built on the purpose of theory development and the ‘adaptive theory approach’ (Layder 1998) which suggests the development of theory through the complementary use of deduction and induction (see Figure 3)[16].

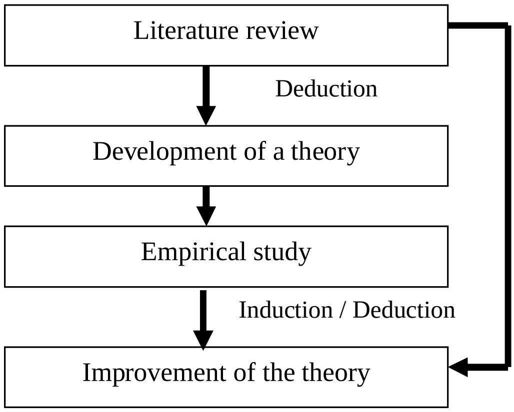

Figure 3. The theory-development process (adapted from Layder 1998)

Reviewing the literature is an important stage because knowledge is advanced by cumulatively adding new knowledge to what is already known (Chia 2002). This also prevents reinventing the wheel. I therefore spent considerable time identifying a research need and choosing the appropriate theoretical approaches to answer the research questions[17]. The primary reasoning used for theory development at the second stage was deduction logic. At this stage the theory comprised of a typology of primary stakeholder contributions[18], 15 propositions to determine the types of contributions[19], and a scheme for predicting likely primary stakeholder contributions[20]. **Chapter two** covers the literature review and the theory development.

A key aspect of the research strategy was the choice of research methodology. The methodology applied here was historical analysis, in other words a review of the past and analysis of past events in a systematic way (Gottschalk 1969; Gillette 1988). Historical analysis fits the needs of this research because market integration in Europe has been going on for at least 50 years, and strategic responses to threats are processes in time. The choices related to the research methodology and the procedures applied in data

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16 See section 3.1 for discussion on the selection of the research strategy.

17 The literature review also played a key role following the empirical study when I was attempting to improve the theory (see Figure 3).

18 See section 2.6.

19 See sub-section 2.7.3.

20 See section 2.8.

collection, data analysis and verification of findings are discussed in **Chapter three**.

Gummesson (2000, 79) argues that a preunderstanding of the research context helps to avoid possible shortcomings in the research. Therefore, in order to gain pre-understanding of the research context and also increase understanding on primary stakeholders (as needed for predicting their likely contributions to answer research question 1), I reviewed studies on the EU, its regulatory mechanism, and the EU car industry from a historical perspective: this review comprises **Chapter four**.

The third stage of the research was the empirical study, the aim of which was to improve the theory so as to provide a better reflection of the reality in the light of the empirical data. The empirical study, which is reported in **Chapter five,** consisted of the review of the history of the Volkswagen Group (VW) from 1960 to 2005 in the light of market-integration initiatives in the EU[21], and the analysis of four events[22].

In the first part of the empirical study I chose a focus car manufacturer, namely VW[23], and studied its history from 1960 until 2005[24] in search of primary stakeholder contributions. I chose a period starting from 1960 because the VW law, which is the subject of one of the studied events, was passed in 1960 during the privatization of the firm.

Following the review of the history of VW, I selected the following four threat events (out of a pool of 16 events) for in-depth analysis:

- The court case against the VW law (this event will be called the 'VW law event' in the rest of the thesis)
- The increasing competition from Japanese car manufacturers on VW following the creation of a single market in the EU (this event will be called the 'single market and VW event' in the rest of the thesis)
- The 13th EU directive on takeover bids (this event will be called the '13th EU directive event' in the rest of the thesis)
- The block exemption regulation 1400/2002 (this event will be called the 'BER 1400/2002 event' in the rest of the thesis).

I chose the events by means of theoretical sampling, which advocates that the choice is driven by the theory (Glaser and Strauss 1967, 45). The events were selected purposefully to cover elements of the theory in terms of variety

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21 See section 5.1.
22 See sections 5.2, 5.3, 5.4, 5.5, and 5.6.
23 See section 3.3 for reasons behind this choice.
24 This is because 2005 was the year for which the latest data was available when I started the review. The analysis of some of the events, however, continued until 2008.

in the nature of threat, types of contributions, and contributing primary stakeholders[25].

Having analyzed the four events, I improved the theory in **Chapter six** in two directions: longitudinally and cross-sectionally. The longitudinal improvement was crucial because the resolution of threats is a process[26]. In this kind of improvement I was able to develop temporal links between the types of primary stakeholder contributions. The cross-sectional theory improvement included fine-tuning of determinants of types of primary stakeholder contributions. This generated additional five propositions on top of the 15. Thanks to having studied in **Chapter four** primary stakeholders in the EU car industry, I could also predict with the aid of the improved theory the likely contributions of various types of primary stakeholders. This was a crucial step in answering research question 1 and also showing that the theory had predictive capacity (cf. Merton 1967).

The improved theory comprises the typology of primary stakeholder contributions and relationships between the types of contributions in time, the 20 propositions regarding the determinants of the types of contributions, and the scheme for predicting primary stakeholder contributions (see Table 2).

Table 2. Key elements of the improved theory

Element	Location in the thesis
Typology of primary stakeholder contributions and relationships between the types of contributions in time	Section 6.1
20 propositions to determine the types of contributions	Section 6.2
A scheme for predicting primary stakeholder contributions	Section 2.8[27]

In improving the theory I used induction and deduction simultaneously as I benefited from both the literature and the data that was collected from a variety of primary and secondary sources (see Appendix 1 for sources of information).

Chapter seven then discusses the theoretical contributions and the limitations of the research, as well as the implications for primary stakeholders, executive managers of firms, and policy makers at the European Commission. I also suggest a number of avenues for further research.

Finally, **Chapter eight** gives a summary of the research.

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25 See section 3.4 for discussion on the selection criteria.

26 A process is understood in this research as a sequence of acts that describes how things change over time (Van de Ven 1992; Pettigrew 1997).

27 This scheme preserved its validity in the light of the empirical study and therefore did not require any revision.

2 DEVELOPING A THEORY BASED ON LITERATURE REVIEW

The purpose of this research is to increase understanding about primary stakeholder contributions in the face of threats arising from market integration in the EU. In order to achieve that there is a need to seek or develop theoretical tools. The aim in this chapter, therefore, is to review the literature and to build a theory that will be useful in answering the research questions.

2.1 The Building Blocks of the Theory

In this section I introduce the building blocks of the theory[28]. The input-compensation interdependence between the firm and its primary stakeholders (Ahlstedt and Jahnukainen 1971) has encouraged me to conceptualize them as an open social system fulfilling Ackoff's (1981) three conditions for being a system[29]. This conceptualization, which is based on the descriptive stream of stakeholder theory and general systems theory, constitutes the foundation of the theory (See Figure 4). In answering the two research questions I needed to visit a variety of theoretical perspectives and apply relevant ones because there was not a readily available theoretical tool (See Figure 4).

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28 A theory refers to a logically interconnected set of propositions summarizing uniformities of relationships between two or more variables (Merton 1967, 41).

29 See section 2.5 for further discussion.

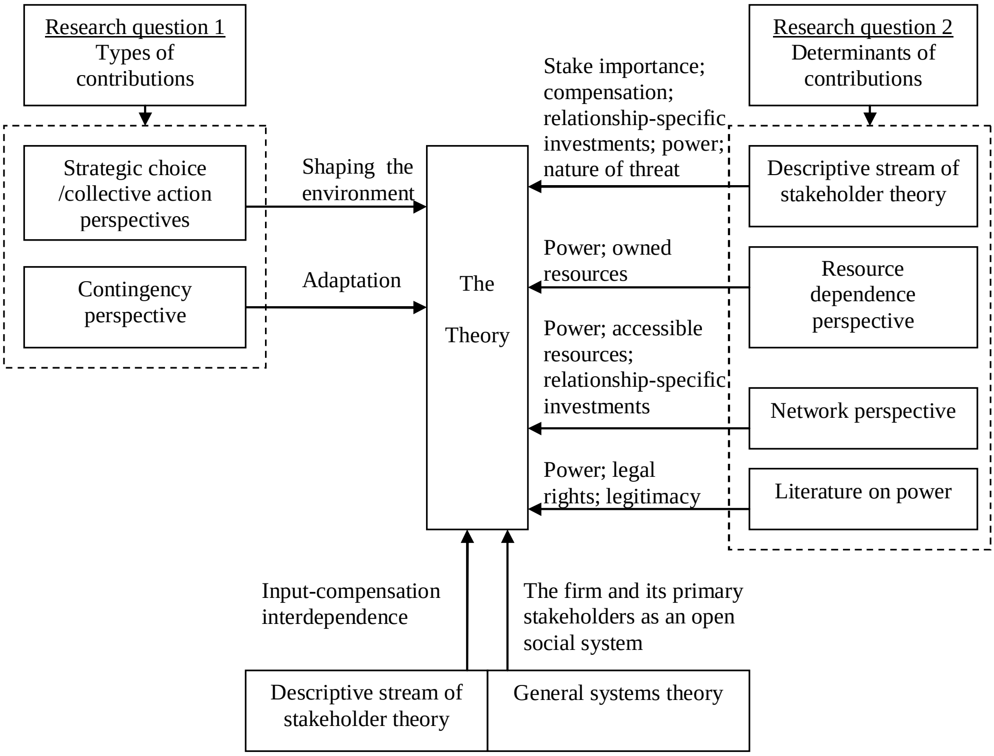

Figure 4. The building blocks of the theory

In response to research question 1, the concepts of adaptation from the contingency perspective (cf. Selznick 1957; Teece et al. 1997) and of shaping the environment from the strategic-choice (cf. Child 1997) and the collective action (cf. Commons 1950) perspectives contribute to the building of a typology of primary stakeholder contributions (See Figure 4)[30].

For research question 2, the descriptive stream of stakeholder theory presents concepts related to the importance of stake (including compensation and relationship-specific investments) and power (cf. Mitchell et al. 1997) as well as the nature of threat (cf. Savage et al. 1991; Rowley and Berman 2000; Lozano 2005) (See Figure 4). The resource dependence perspective suggests owned resources as a source of power (cf. Pfeffer and Salancik 1978). Likewise, the network perspective recommends accessible resources as a source of power (cf. Brass and Burkhardt 1993) and emphasizes the importance of relationship-specific investments (cf. Bensaou 1999). Finally

30 See section 2.6 for the typology.

the literature on power further suggests legal rights and legitimacy as sources of power (cf. Stinchombe 1968; Mintzberg 1983)[31].

Integrating theories may be problematic if the theories possess contradicting meta-theoretical assumptions (Burrell and Morgan 1979). Let me put up in front that I am not intending full integration of every detail in the theories but bringing together attributes that contribute to the development of a framework for answering the research questions. Especially in the answering of the second research question, I only borrow concepts from different theories and do not intend at all an integration of the theories[32]. In doing that I started naturally with the descriptive stream of stakeholder theory and then visited the resource dependence and network perspectives with the hope of finding other determinants not covered by the stakeholder theory. I visited these perspectives because they also analyze relationships and the phenomenon of interdependence which forms the basis of firm-primary stakeholder relationships. I consider that they are compatible with the stakeholder theory given by the fact that they have already been used in tandem with the stakeholder theory (cf. Rowley 1997; Frooman 1999). I moved finally to literature on power as it came out to be a key determinant in all perspectives[33].

I admit, however, that it is possible to speak of some degree of integration between the descriptive stream of stakeholder theory and general systems theory as well as between the stakeholder theory and each of the three perspectives used in answering the first research question. Let me discuss in the following paragraphs using the scheme of Burrell and Morgan (1979, 3) how such integration is possible from the lens of their assumptions of ontology, epistemology, human nature, and methodology.

In their ontological assumptions both the general systems theory and the descriptive stream of stakeholder theory adopt a realistic view of the nature of reality in trying to understand the relationships between a set of interacting elements. This is also the case for the strategic choice, collective action[34], and contingency perspectives which all study strategic responses to the environment. The realistic view is also the adopted view by the research strategy in this thesis[35] as it seeks first to develop a typology of primary

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31 See section 2.7 the model of determinants of the types of primary stakeholder contributions.

32 See section 2.7.

33 Besides organizational science, the concept of power is discussed in a variety of social sciences including politics and international relations (cf. Goldmann and Sjöstedt 1979; Berenskoetter and Williams 2007), sociology (cf. Emerson 1962; Lukes 1974; Cox et al. 1985), and social psychology (cf. Raven and Rubin 1976). In this research I limited my literature review on power in terms of their relevance to business studies, and it is covered in sub-sections 2.4.2 and 2.4.3.

34 This perspective has been used in tandem with stakeholder theory (cf. King 2008).

35 See section 3.1.

stakeholder contributions and then tries to identify the underlying factors behind the choice of contribution.

In their epistemological assumptions the above two theories and three perspectives all adopt a positivist view in terms of accepting the cumulative nature of knowledge and the ability to achieve understanding by observation. This is also the adopted view in this research[36] as the research started with the development of a theoretical framework based on review of literature.

The general systems theory and the stakeholder theory both adopt a view about the human nature which is neither completely voluntaristic nor completely deterministic. This lies in that both the elements of a system and primary stakeholders are free to pursue own goals, but they are at the same time interdependent with other actors for achieving their own goals. The strategic choice, collective action, and contingency perspectives differ in the degree of voluntarism they assume about the human nature. As Astley and Van de Ven (1983, 246) argue, however, some degree of integration of these perspectives is achievable with the condition that their distinctiveness is recognized. I tried to integrate premises from these three perspectives, but not from the natural selection perspective, because the natural selection perspective assumes a completely deterministic human nature. In my opinion, the three perspectives allow for some degree of integration and enable me to create the typology of primary stakeholder contributions[37].

Finally, the two theories and the three perspectives allow for both ideographic and nomothetic methodology depending on the research objectives and the nature of the phenomenon under study. As the objective of this research is theory development, the adopted methodology is ideographic[38].

To conclude, consulting multiple theoretical perspectives for answering the research questions was not problematic in my opinion. Instead, I am of the opinion that theoretical pluralism better captures reality in consideration of organizational complexity (Astley and Van de Ven 1983, 245), as it has been effectively achieved in some of earlier research (cf. Oliver 1997b; Sanchez 2003; Spulber 2003; Steel and König 2006). The theories and perspectives used in this research allow for some degree of integration thanks to their compatibility in terms of their assumptions about ontology, epistemology, human nature, and methodology. Let me explain in the following sections how I achieve that.

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[36] See section 3.1.

[37] See section 2.6 for further discussion.

[38] See section 3.2.

2.2 The Firm from a Stakeholder Perspective

The firm is the basic unit of production when a group of individuals (e.g., investors, employees, and managers) are drawn together by the motive of economic gain and are engaged in production activity transforming inputs (e.g., raw materials) into outputs (e.g., products and services) for customers (Coase 1937). This is a definition that is widely accepted by economists although there are different conceptualizations of the firm (see Table 3).

Table 3. Various theoretical views about the firm

Name of View	Focus	Related Theories	Pioneering Works
Transaction-cost	Market-exchange transactions	Transaction cost theory, internalization theory	Williamson 1975; Buckley and Casson 1976
Nexus of contracts	Contracts with employees, suppliers, customers and creditors	Agency theory	Jensen and Meckling 1976
Resource-based	Resources of the firm	Resource-based View	Penrose 1959; Wernerfelt 1984; Barney 1991
Knowledge-based	Organizational learning; knowledge of the firm	Evolutionary Theory; Knowledge-based View	Nelson and Winter 1982; Kogut and Zander 1993
Stakeholder	Stakeholders	Stakeholder Theory	Freeman 1984

The different ways of conceptualizing the firm enrich our understanding. In terms of building a theoretical framework, however, it may be crucial at the beginning to adopt a single view, which is the most appropriate in terms of answering the research questions. As the objective of this research is to increase understanding about the primary stakeholders of the firm, the stakeholder view seems to fit the best, and it is therefore the one that is adopted.

The stakeholder view defines the firm as an organization through which a number of actors (i.e. stakeholders) realize their personal goals while contributing to its existence (Rhenman 1964, 2/12). Thus, the firm is an organization engaged in mobilizing resources for productive uses in order to create wealth and other benefits for its stakeholders (Post et al. 2002, 17). This view gives rise to stakeholder theory, which focuses on managing relationships with stakeholders (Freeman 1984).

Stakeholder theory challenges the dominant shareholder theory in arguing that managers should pay attention to the interests of all stakeholders and not just those of shareholders (Freeman 1984; Brenner 1995; Smith 2003). Thus, stakeholder management involves designing and implementing communication processes with stakeholders, understanding and serving multiple stakeholders, proactively anticipating stakeholders’ needs and allocating resources accordingly, integrating stakeholders into strategy-formulation processes, and negotiating with them on critical issues and seeking voluntary agreements (Freeman 1984, 78–80).

There are three ‘divergent’ streams in stakeholder theory (Donaldson and Preston 1995; Freeman 1999), the descriptive stream, the instrumental stream, and the normative stream.

The descriptive stream examines the actual behaviors of the firm and its stakeholders (cf. Freeman and Reed 1983; Clarkson 1995; Mitchell et al. 1997). Some scholars (e.g., Jones and Wicks 1999; Butterfield et al. 2004) confess that this is the least developed of the three streams, and that there is a need to learn more about firm-stakeholder relationships especially from the stakeholders’ point of view (Frooman 1999; Butterfield et al. 2004; Frooman and Murrell 2005).

The instrumental stream examines the connection between stakeholder management and firm performance. There is still controversy over whether firms practicing stakeholder management will, other things being equal, be relatively more successful in terms of performance (cf. Cochran and Wood 1984; Jones 1995; Griffin and Mahon 1997; Berman et al. 1999; Rowley and Berman 2000; Hillman and Keim 2001; Heugens et al. 2002). Scholars who argue for a positive relationship base their claims on the notion that building long-term relationships with stakeholders based on cooperation (i.e. stakeholder engagement and partnership) may render value and competitive advantage in the long run (Jones 1995; Berman et al. 1999; Andriof and Waddock 2002) by creating and preserving organizational flexibility (Harrison and St. John 1996), and by increasing organizational learning and legitimacy (Heugens et al. 2002). In addition, stakeholder-engagement processes may help in terms of identifying threats and opportunities (Keijzers 2005), and also enhance the management of the firm’s social risk by connecting with stakeholders and building social capital (Andriof and Waddock 2002). For these reasons, favorable relationships with stakeholders are considered to be important relational assets of the firm (Post et al. 2002).

The normative stream focuses on topics such as business ethics, moral behavior, and corporate social responsibility (cf. Beauchamp and Bowie 1983; Elias and Dees 1997; Carroll and Buchholtz 2003; Garriga and Melé 2004). It is referred to as normative because it prescribes what managers should do in terms of both the goals they pursue and the means they utilize in achieving them (Jones and Wicks 1999).

The descriptive stream of stakeholder theory is the principal research stream from which I aim to benefit in developing a theory because it is about stakeholder behaviors, and issue management is a typical arena in which stakeholder thinking is applied (Näsi 1995b). It is also the research stream to which I intend to contribute.

2.3 Primary Stakeholders

There is controversy concerning the definition of stakeholders. A review conducted by Freeman and Reed (1983) distinguishes between narrow-sense and wide-sense definitions. In literature three are three highly referenced definitions. In chronological order they are the following:

1. *The Stanford Research Institute (1963): "Stakeholders are those groups without whose support the firm would cease to exist"* (Freeman 1984, 31).
2. *Rhenman (1964): "Stakeholders are individuals and groups who are depending on the firm in order to realize their personal goals and on whom the firm is depending for its existence"* (Rhenman 1964, 2/12).
3. *Freeman (1984): "Stakeholders are individuals or groups who can affect or are affected by the achievement of the firm's goals"* (Freeman 1984, 46).

Whereas the Stanford Research Institute (1963) and Rhenman's (1964) definitions are narrow-sense, the one put forward by Freeman (1984) is wide-sense. Perhaps Clarkson's (1995) classification of primary and secondary stakeholders fits best the distinction between the narrow-sense and wide-sense definitions. In my opinion, the former refer to primary stakeholders, while the latter include both primary and secondary stakeholders.

For the purposes of this study, Freeman's (1984) definition could be considered broad because those affected by the achievement of the firm's purposes may include a large variety of secondary stakeholders. There may be one-time effects. For example, if the firm decides to make a one-time donation, the individual or group receiving it may become a stakeholder in Freeman's terms, while according to Clarkson (1995) it would be a secondary stakeholder. This research does not concern such secondary stakeholders because they are not in a relationship of interdependence with the firm. There may also be individuals or groups (e.g., competitors) that are negatively affected by the achievement of the firm's goals, and would also be secondary stakeholders: they are not of interest here either because they are not in an input-compensation relationship with the firm. Moreover, there may be individuals or groups that may be able to affect the achievement of the firm's goals positively or negatively (e.g., regulatory organizations, interest groups) but lack an input-compensation relationship with the firm: these would also be secondary stakeholders.

The two narrow-sense definitions concerning primary stakeholders are similar. However, Rhenman (1964) establishes clearer attributes to stakeholder identification, namely the stakeholders' interests in the firm and the firm's dependence on the stakeholders. The first attribute is not specified in the definition by the Stanford Research Institute (1963). Thus, Rhenman's definition sets out a two-way dependence, and I borrow it for defining primary stakeholders.

This research deliberately focuses on primary stakeholders because they are in a long-term relationship of interdependence with the firm and thus should be the ones most affected when it faces a threat. They have divergent interests (Hill and Jones 1992), but they share a common risk - the risk of gaining benefit or experiencing loss as a result of the firm's operations (Post et al. 2002). Ahlstedt and Jahnukainen (1971) argue that these stakeholders contribute inputs to the firm and receive compensation in return (see Figure 5).

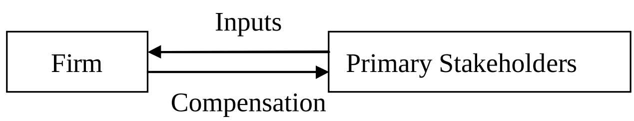

Figure 5. The interdependence between the firm and its primary stakeholders (adapted from Ahlstedt and Jahnukainen 1971)

Primary stakeholders may include actors inside the firm (e.g., shareholders, employees), actors along the value chain in the market environment (e.g., suppliers, dealers, customers and creditors), and actors in the non-market environment (e.g., the home government)[39]. In the following section I discuss the interdependence between the firm and its primary stakeholders in more detail.

[39] As the firm's managers are not included among the stakeholders in most of the literature, I also view them as part of the firm and not as primary stakeholders.

2.4 The Interdependence between the Firm and its Primary Stakeholders

Different forms of life are interrelated (Hawley 1950). As no business is an island (Håkansson and Snehota 1989), firms are embedded in webs of relationships with actors in their environments (Granovetter 1985). In other words, firms are interdependent. Interdependence exists when an actor does not fully control all of the conditions necessary for the achievement of an action (Pfeffer and Salancik 1978).

Zettinig (2003, 88) describes three types of interdependence based on the works of Hawley (1950), Thomas (1957), Thompson (1967), and Pfeffer and Salancik (1978): competitive interdependence, outcome interdependence, and behavior (pooled) interdependence.

Competitive interdependence refers to the situation in which two ‘like’ parties that are not directly connected are dependent on each other because they need the same resources, or they try to serve the same customers (Hawley 1950). Competitors in an industry, for example, are in a state of competitive interdependence. This is not, however, the type of interdependence observed between the firm and its primary stakeholders.

Outcome interdependence refers to the relationship between two ‘unlike’ parties in which the output of one is the input for the other (Hawley 1950; Pfeffer and Salancik 1978). This is the typical type of interdependence existing between the firm and for example its suppliers, its dealers, its customers, and its creditors.

Behavior (pooled) interdependence refers to relationships requiring two or more parties to ‘play together’ (Thomas 1957; Pfeffer and Salancik 1978), which Thompson (1967) names ‘pooled interdependence’. It is established when two or more parties use the same resource (e.g., a joint investment by two car manufacturers in an assembly plant), or when they enter into a common operation, each of them bringing in specialized resources and capabilities (e.g., a joint R&D project to which the parties contribute with their specialized knowledge). This type of interdependence exists between the firm and for example its employees and its shareholders.

Interdependence plays a key role in the systems, resource dependence, and network perspectives. In the following three sub-sections I review these perspectives in order to find theoretical tools to build on the interdependence between the firm and its primary stakeholders.

2.4.1 The Systems Perspective

A system is a set of interacting units or elements that form an integrated whole intended to perform some function (Skyttner 1996, 16). It is a ‘black box’, which transforms inputs into outputs (Von Bertalanffy 1974). It consists of elements, properties of elements, and relations between elements (Henderson 1970), and emerges from the interactions of its elements (Marion 1999). According to Ackoff (1981), a system must satisfy the following three conditions.

1. The behavior of each element affects the behavior of the whole;
2. The behaviors of the elements and their effects on the whole are interdependent;
3. The elements cannot form independent subgroups.

As Ackoff’s conditions clearly illustrate, the systems perspective is holistic[40] in that the behaviors of elements can be understood in the light of the relationships with other elements.

There are two types of systems, closed and open. Whereas closed systems are considered to be isolated from their environments, open systems exchange matter with their environments (Von Bertalanffy 1968). This exchange of matter is an essential factor underlying the system’s viability, its continuity, and its ability to change (Buckley 1967) in that the elements will tend towards disorder if they are left alone, i.e. entropy (Von Bertalanffy 1968). A system has cycles of events in which it transforms inputs into outputs (Katz and Kahn 1978). Such cycles create stable patterns of relationships and behavior among the elements and contribute to the avoidance of entropy. Regulation of the elements through a control mechanism of feedback is necessary in order to safeguard the continuity of the system. Open systems receive feedback from the environment, and this helps the elements to adjust internally on order to remain in step with it (Marion 1999). Since closed systems lack such feedback, threats from the environment may lead to their death (Von Bertalanffy 1968).

One can also differentiate between mechanical systems and social systems. Systems exhibit three states of behavior: organized simplicity, organized complexity, and chaos (Buckley 1967). A mechanical system exhibits organized simplicity: it is designed to perform a certain function almost automatically by means of energy transfer from one element to another. An example of this kind of system is a radiator with a thermostat: when the room

[40] Holism means that a system’s capacity for action exceeds the individual or summed capabilities of its elements (Marion 1999, 64).

temperature drops below a certain level, the thermostat senses it and turns on the radiator.

A social system is more complex[41] in that it has the ability to order interaction patterns within it (Marion 1999, 71). Its elements exhibit goal-seeking and behavioral choice. They carry information about their environment and about their past (Marion 1999). They learn from their experiences and adjust their behaviors accordingly. They also have the ability to anticipate their futures and to attempt to manipulate them (ibid.). These characteristics differentiate social from mechanical systems. The elements in a social system are human beings or groups of human beings. When there is a human factor there is inevitably also a struggle for power among the elements (Huff 1980; Mintzberg 1983). This brings a certain level of chaos to social systems, which may be useful in terms of adaptation, and most of them exhibit behaviors of organized complexity (Marion 1999). Social systems and their elements also interact with their environments. Therefore, most of them are also open systems. An example of an open social system is the firm (Ackoff 1974a; Katz and Kahn 1978; Scott 1987): it draws resources as inputs from the environment at one end and exports goods and services into the environment at the other (Miles et al. 1974, 246).

The firm is also a goal-seeking system, which is one that has goals and behavioral choice in their achievement (Ackoff 1974a). The elements of a system may also have their own goals (Von Bertalanffy 1968), and must transform inputs into outputs if the system and its elements are to realize these goals. Elements in a complex system are differentiated in that they perform specialized functions. They may form sub-systems, which are nested in the complex system through a hierarchical mechanism. In such complex systems the behaviors of the elements and sub-systems need to be integrated and coordinated (Katz and Kahn 1978).

A goal-seeking system is adaptive if it can modify itself or the environment when either of them has changed to the system's disadvantage so as to regain some of its lost efficiency (Ackoff 1974a, 35). It is also capable of learning how to adapt. A key notion in dynamic systems theory is that of stability (or equilibrium), and the response of a system to perturbation (Von Bertalanffy 1974; Henderson 1970; Katz and Kahn 1978). According to this theory, the elements of a system tend to have some kind of stability, and when the system is displaced to a small extent the elements will tend to adjust accordingly. This type of system behavior is called dynamic homeostasis (dynamic equilibrium), and the basic principle underlying it is the preservation of the character of the system (Katz and Kahn 1978, 26-27). If the displacement is large enough to

41 Complexity is a hybrid state that lies between simplicity and chaos (Marion 1999).

make it impossible to regain the old form of stability, then the elements may seek a new form. Perturbation from the environment increases the degree of chaos or disorder within the system. At such times, although conflict and competition may exist among the elements, cooperative behavior increases the chances of survival (Axelrod 1984; Kauffman 1993).

The concept of systemic equilibrium has been used in the context of business studies in the literature on entrepreneurship. Schumpeter (1951) conceptualized entrepreneurs as agents who creatively destroy an existing equilibrium in the economic system by bringing in new innovations. Kirzner (1973) put forward an opposing systems view on entrepreneurship, according to which opportunities exist in a state of disequilibrium as discrepancies, gaps and mismatches in the system, and the entrepreneur helps to bring the system towards equilibrium by perceiving and exploiting these opportunities.

The open systems perspective promotes understanding of the firm in interaction with its environment (Reason 1980, 35). In my view, it suits very well the conceptualization of the firm and its primary stakeholders. I discuss this choice more extensively in section 2.5.

2.4.2 The Resource Dependence Perspective

The resource dependence perspective views the firm as a coalition maintained by providing inducements to participants who support it (Pfeffer and Salancik 1978, 29). This is quite similar to the input-compensation relationship proposed by Ahlstedt and Jahnukainen (1971). The focus of this perspective is on influence and control, and on questions such as how actors can influence and thus manage their environments. It has been applied to the study of strategic alliances (e.g., Kleymann 2002) and of the mechanisms through which stakeholders influence the firm (e.g., Frooman 1999). It supports the stakeholder view in that the firm is dependent on the resources of its primary stakeholders for inputs, and vice versa, each primary stakeholder is dependent on the firm’s resources (and also indirectly on the resources of all other primary stakeholders) for realizing its goals.

Power is a key concept in the resource dependence perspective. It refers to the (potential or actual) ability of one party to impose its own will on others (Etzioni 1961; Reitz 1981). Dahl (1957), on the other hand, refers to it as a synonym of influence, and suggests that unused potential is not power: it is the ability or capacity to affect outcomes and to get things done (Stinchombe 1968; Mintzberg 1983). Emerson (1962) argues that the power of an actor is relationship-specific, and it is inversely proportional to its dependence on its relationship partner. The ability of an actor to influence other actors in its environment and thus to control its destiny determines its relative power (Pfeffer and Salancik 1978).

Power is a dynamic concept, and it can be gained and lost (Etzioni 1961). A party has power to the extent that it has or can gain access to coercive (e.g., the application or the threat of the application of physical sanctions), remunerative (e.g., rewards such as material benefits), or normative (e.g., symbolic rewards such as esteem, prestige, acceptance and a positive response) means (Etzioni 1961). Pfeffer and Salancik (1978) name three determinants of power in a relationship: resource importance, resource control, and resource alternatives.

Resource importance: Resource importance has two dimensions: the relative magnitude of the exchange and the criticality of the resource (ibid.). Magnitude refers to the ratio of the exchange amount of the resource to the exchange amount of the total input, while criticality refers to the ability of the firm to continue its operations without the resource. Possession of the critical resources the relationship partner needs is a source of power over that partner: the more critical the resources and the higher the magnitude of exchange, the higher is the degree of power.

Resource control: Resource control refers to the capacity of an actor to determine the allocation or use of a resource (ibid.). Sources of control derive from having possession of or access to the resource, or having the right to make regulations concerning its use. The higher the degree of control over resources, the higher is the degree of power.

Resource alternatives: Resource alternatives refer to other sources with the same resource or substitutes. Valuable resources that are also rare, imperfectly imitable, and non-substitutable are sources of sustained competitive advantage (Barney 1991). The fewer the alternative sources of important resources possessed by an actor, the higher is the degree of its power.

In sum, according to the resource dependence perspective an actor is powerful in a relationship when it controls important resources for which there is a lack of alternative suppliers.

This perspective is relevant to answering research question 2 since power is a key attribute in firm – stakeholder relationships (cf. Mitchell et al. 1997). Borrowing from this perspective, important and rare resources controlled by the primary stakeholder may be a determinant of its power[42].

[42] See section 2.7.

2.4.3 The Network Perspective

The network perspective may be relevant to better understanding primary stakeholders because the firm and its stakeholders have been viewed as a network (cf. Rowley 1997).

A network is an independent coalition of task- and skill-specialized economic actors operating without hierarchical control but embedded in dense lateral connections, mutuality, and reciprocity in a shared value system that defines the 'membership' roles and responsibilities (Achrol and Kotler 1999, 148). It is also described as a governance structure for organizing exchange through cooperative, non-equity relationships (D'Cruz and Rugman 1994). Easton (1992) describes networks in terms of relationships, structure, positions, and processes:

Network Relationships: Networks are clusters of long-lasting relationships that are continually changing as they are established, maintained, developed, and broken (Johanson and Mattsson 1988). Johanson and Mattsson (1987) identify four elements of relationships: mutual orientation, investments, bonds, and dependence. Mutual orientation is the readiness to cooperate in achieving common goals based on mutual knowledge and respect for each other's interests (ibid.). The driving force behind cooperation is the need to gain access to other resources (and opportunities) that an actor cannot manage alone (Powell and Smith-Doerr 1994; Håkansson and Snehota 1995). Investment is an important element of relationship development. Bensaou (1999), for example, provides a typology of relationships determined by the degree of relationship-specific investment by the parties involved. Bonds refer to the links between relationship parties. There may be multiple bonds, and information sharing is the common currency of network relationships achieved through these bonds (Tikkanen 1997). Strong relationships with network members through mutual orientation, relationship-specific investments, and the forging of strong bonds increase an actor's capacity to withstand external disruptive forces (Achrol and Kotler 1999).

The Network Structure: The network structure refers to the heterogeneous set of relationships among network actors. It gives a bird's-eye view of the network as a whole without any focus on a specific actor or relationship. It may be, however, difficult to determine the boundaries of networks (D'Cruz and Rugman 1994). A key aspect of the network structure is its density. This refers to the number of ties that link actors together. The denser the network, the more efficient are the communication channels and the faster is the diffusion of information (Rowley 1997).

Network Positions: A network position refers to the exchange relationships of an actor and describes its role, relative importance and identity in the network (Johanson and Mattsson 1992). A key feature of the network position is centrality. This refers to the number of direct ties an actor has to other actors, the ability to access other actors independently, and the degree of control over other actors (Brass and Burkhardt 1993). Centrality is a source of power (ibid.).

Network Processes: Networks are stable, but they are not static. The four types of network processes are entry, positioning, repositioning, and exit (Thorelli 1986). Networks evolve gradually over time as relationships are continually established, maintained, developed, and broken (Johanson and Mattsson 1988). Change can also occur in a revolutionary manner, such as when new resources are found, when different activities are executed using different combinations of resources, or when one actor loses control of a resource (Håkansson and Henders 1995).

In my opinion the firm and its primary stakeholders constitute more than a loosely-coupled network of actors because the bonds between them are stronger due to the input-compensation relationship. These strong bonds also allow identification of clear boundaries, which is difficult to achieve in the case of a network. In that respect the network perspective is perhaps not the most suitable in terms of examining the interdependence between the firm and its primary stakeholders. However, some of its premises may be relevant for this study. First, this perspective allows conceptualizing of power not only stemming from owned resources but also from resources which an actor can access in its network (Brass and Burkhardt 1993). Secondly, it highlights the significance of relationship-specific investments in building relationships (Bensaou 1999). Thirdly, the idea that mutual orientation and cooperation contribute to survival may be important to understand for the firm and its primary stakeholders. Finally, this perspective reminds that relationships between the firm and its primary stakeholders are subject to change over time. This reminder is important for the development of the theory longitudinally.

2.5 The Firm and its Primary Stakeholders as an Open Social System

The open-systems perspective views the firm as an open social system of which the internal primary stakeholders (i.e. those inside the firm such as shareholders and employees) are already considered a part. It is possible to extend this perspective to include external primary stakeholders. Thus, primary stakeholders and firm managers could be considered elements of this open system. Katz and Kahn (1978) argue that an open system should receive inputs from and give outputs to the environment, which would leave customers and suppliers outside. In my opinion, the only prerequisite for being an open system is that the elements interact with actors in the environment (or outside) of the system. Otherwise, how could one conceptualize an open social system consisting of a physician and a patient, for example (cf. Henderson 1970, 202)? In the case of the firm and its primary stakeholders, actors outside of the system are secondary stakeholders.

This is a new perspective on primary stakeholders. Earlier, Rowley (1997) described stakeholders as members of a network around the firm. The interests of the firm and its primary stakeholders are not always in harmony (Hill and Jones 1992). This applies especially when it comes to the distribution of revenues in which the executive managers of the firm pursue strategic negotiations with multiple stakeholders (cf. Lamberg et al. 2003). As in any social system, there is naturally a struggle for power between the firm and its various primary stakeholders. Therefore we could argue that an open social system comprising the firm and its primary stakeholders is complex. Nevertheless, the interests of these actors may converge because primary stakeholders share the risk of gaining benefits or experiencing losses as a result of the firm's operations (Post et al. 2002). This may apply precisely when survival is the issue, and is exactly the kind of situation in which Weick (1974) would expect this system to function in harmony. Mutual orientation and cooperation are acknowledged to enhance chances of survival (Axelrod 1984; Kauffman 1993; Achrol and Kotler 1999).

I should also note that some elements of the system could belong to other systems at the same time. For example, a supplier may supply different competitors simultaneously. The home government provides an infrastructure for all firms operating in the country. A creditor usually provides capital to all kinds of firms and their primary stakeholders, and a customer may also buy the products of competitors.

In my opinion, the set of primary stakeholders and the firm qualify as an open social system because it satisfies the following three conditions set out by Ackoff (1981).

Condition 1: The behavior of each element affects the behavior of the whole. Each and every primary stakeholder performs a particular task. Shareholders provide the business idea and capital. Suppliers provide parts. Employees transform these parts into products. Dealers bring products to customers, and customers buy them. The home government provides the infrastructure, and creditors provide further capital. If one of the primary stakeholders does not perform its task (e.g., the employees go on strike), then the system cannot function.

Condition 2: The behaviors of the elements and their effects on the whole are interdependent. When a primary stakeholder does not perform its task, this may affect all other primary stakeholders because they receive their compensation from the outputs and the corresponding generated revenues of the system. This interdependence of primary stakeholders is perhaps best reflected in the profit & loss statement of the firm (see Figure 6).

Customer input	→	Sales revenues	→	Dealer compensation
		Cost of materials	→	Supplier compensation
		Production costs	→	Compensation of production employees
		Selling & Administrative costs	→	Compensations of sales & administrative employees
		Operating profit		
		Interest expenses	→	Creditor compensation
		Before-tax profit		
		Corporate tax	→	Home government compensation
		After-tax profit		
		↓		
		Dividends	→	Shareholder compensation

Figure 6. The firm's profit & loss statement [43]

As Figure 6 shows, customers input revenues to the system from which the compensation of other primary stakeholders derives. It could thus be argued that the position of customers in the system may be slightly different than that of other primary stakeholders. This is indeed true for customers as end-users[44]: they are the sources of revenue from which all other primary stakeholders receive their compensation. Customers as end-users could be considered the weakest link in the system because they are the most vulnerable to leaving it in return for attractive offers from the firm's competitors.

Condition 3: The elements of a system cannot form independent subgroups. It is not possible for a number of primary stakeholders to form a subgroup and manufacture and sell the same products. Each and every primary stakeholder is needed for the system to function as a whole.

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[43] I should note that the government receives compensation from the compensation of all the other actors in the system. It takes corporate taxes from the firm, its suppliers, dealers and creditors. It receives income tax from employees and shareholders, and various taxes from customers (e.g., registration tax, value-added tax, and taxes on vehicle usage).

[44] Here it may be necessary to differentiate between customers as end-users (of products) and corporate customers purchasing resources (e.g., technology).

The fulfilling of the three conditions allows me to conceptualize the firm and its primary stakeholders as an open social system. It is on this basis that I address research question 1 in the following section.

2.6 A Typology of Primary Stakeholder Contributions

Research question 1 asked how various primary stakeholders contribute to resolving threats arising from market integration in the EU. This requires first the drawing up of a typology of primary stakeholder contributions. In order to establish such a typology I reviewed the literature on strategic responses to the environment and applied concepts from the contingency, strategic choice, and collective action perspectives from the point of view of primary stakeholders.

The literature on strategic responses to the environment mostly takes the firm's perspective. Child et al. (2003) categorize such research under three perspectives, namely the natural selection perspective, the contingency perspective, and the strategic choice perspective. Astley and Van de Ven (1983) provide a similar typology, but from four perspectives: the natural selection perspective, the system structural perspective, the strategic choice perspective, and the collective action perspective. The first three perspectives in the typology of Astley and Van de Ven (1983) match the perspectives provided by Child et al. (2003), with the exception that Astley and Van de Ven (1983) call the contingency perspective the system structural perspective. They also add a fourth, namely the collective action perspective. These four perspectives and their key premises are summarized in Table 4 and further elaborated below.

Table 4. Four perspectives on strategic responses to the environment (adapted from Astley and Van de Ven 1983; Child et al. 2003)

	Natural Selection	Contingency	Strategic Choice	Collective Action
Key premise	Selection of strong firms by the environment	Fit between the environment and the firm's strategy and structure	Shaping of the environment by the firm's managers	Collective shaping of the environment by networks of actors
Firm capabilities	Limited adaptive capability due to structural inertia	Capability to adapt to changing environments	Capability to shape the environment	Capability to shape the environment collectively through bargaining and conflict negotiation
Nature of the firm's response	Inactive (no response)	Reactive	Proactive	Interactive

The natural selection perspective assumes a deterministic environment that can select firms that will succeed (Hannan and Freeman 1977). Firms are assumed to be limited in their adaptive capabilities because there are internal and external pressures favoring structural inertia, i.e. the tendency of the firm to preserve its current structure (Hannan and Freeman 1984). Internal pressures may arise from heavy investments, internal politics, earlier commitments, and the firm's culture, while external pressures include barriers to entry and exit, high costs of information, the need to achieve legitimacy, and restrictions resulting from competitive behavior (ibid.).

The contingency perspective differs from the natural selection perspective in that it offers a dynamic view according to which the environment is still influential but firms can adapt to its changing needs. In other words, firms are able to respond to the environment, although in a reactive manner. This perspective is based on two assumptions. First, a good fit between the firm's strategy and the environment as well as between the organizational structure and the firm's strategy are important success criteria (Chandler 1962). Secondly, the firm is an adaptive mechanism that is shaped in reaction to the characteristics and commitments of its participants as well as to influences and constraints from the environment (Selznick 1957). According to this perspective successful firms are those that match their internal competences (i.e. strengths and weaknesses) with opportunities and threats in the environment (Learned et al. 1971; Hansén 1981). In that respect, there is no best way to organize, and not all ways are equally effective (Lawrence and Lorsch 1967). The best structure may be the one that fits the situation of the firm, and it may depend on environmental factors (e.g., uncertainty, degree of change), firm size, and firm strategy (Donaldson 2001). Whereas dynamic and uncertain environments favor more flexible organic structures, stable environments favor mechanistic bureaucratic structures (Burns and Stalker 1994).

Adaptation to the environment occurs at varying levels and may be driven by the environment or managers depending on the degree of flexibility in the firm (Vesalainen 1995). It involves the firm's abilities to integrate, build, and reconfigure its competences and resources in response to changing environments (see Figure 7).

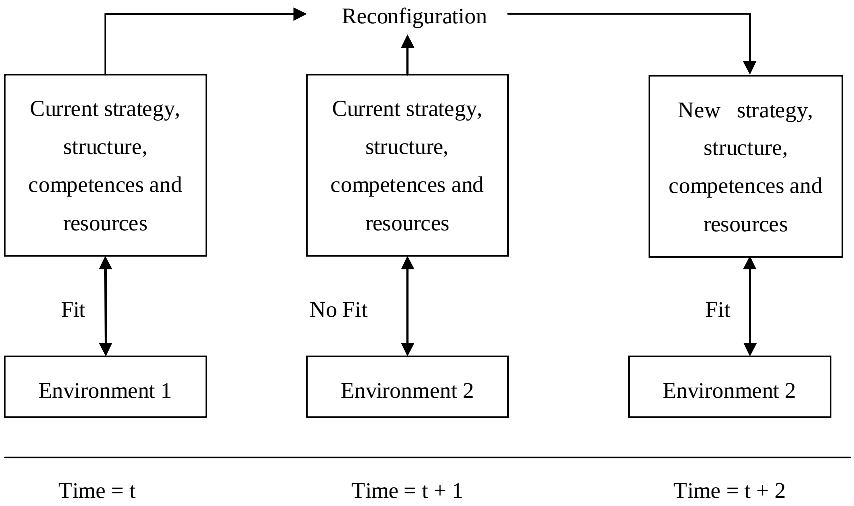

Figure 7. Adapting to changing environments (adapted from Teece et al. 1997)

According to Figure 7, at time t the firm's strategy, structure, competences, and resources fit the environment. As the environment changes at time (t+1), the firm's current set of attributes may no longer match the new needs. In this case it may need to reconfigure its attributes by time (t+2). This reconfiguration process may start at time (t+1) or even earlier, at time (t), depending on the management's capabilities to perceive changes in the environment and the flexibility of the firm to respond quickly.

The strategic choice perspective differs from the above two perspectives in that it denies the deterministic nature of the environment by arguing that it is the firm's executive managers who decide upon the courses of action (Child 1997). The effects of the environment are limited because managers can proactively select and modify the set of constraints by deciding in which markets the firm operates (Bourgeois III 1984). The strategic choices may also be related to the choice of strategies within each market and the choice of related structures[45]. According to this perspective, the roles of the environment are limited to constraining the set of available strategic choices and providing feedback on the selected courses of action through rewards and penalties (Child 1997).

The collective action perspective is similar to the strategic choice perspective in terms of the role it assigns to the environment, but it differs in that it adopts a more interactive view by arguing that managers of one

[45] See Ackoff (1974b) and Miles and Snow (1978) for typologies of strategic choices.

organization interact with each other and also with managers of other organizations through collective bargaining, negotiation, compromise, and political maneuvers as they jointly shape the environment (Commons 1950). Thus, the autonomy of managers is bounded by factors that are internal and external to the firm (Lu and Heard 1995). Within the firm, executive managers negotiate with each other in deciding on the strategic choice, and with the Board of Directors for approval. Outside, they seek to influence related parties in the realization of their strategic choices.

In sum, according to the reviewed four perspectives actors can respond to a threat in the environment in the following ways: they can proactively shape it either individually (*strategic choice perspective*) or in interaction with other actors (*collective action perspective*), they can reactively adapt themselves to avoid the negative impacts of the threat (*contingency perspective*), or they fail to respond by any means due to structural inertia *(natural selection perspective)*.

The conceptualization in this research accepts premises from the strategic choice perspective, the collective action perspective, and the contingency perspective, but rejects those from the natural selection perspective because that perspective conceives of an inflexible nature which does not enable responding to changes in the environment by any means.

The complementarity between the three perspectives arises from the fact that shaping the environment (either individually as stipulated in the strategic choice perspective or in interaction with other actors as stipulated in the collective action perspective) and adaptation (as stipulated in the contingency perspective) can all occur in time. This happens as actors may try proactively to shape the environment first, and in case of failure need to adapt to meet the requirements of the changing environment. In my opinion, being proactive does not imply the ability to shape threats given the rationally-bounded nature of human beings (cf. Simon 1945), and such cases require adaptation. This can be seen in the below model of the process of responding to threats from the environment (see Figure 8).

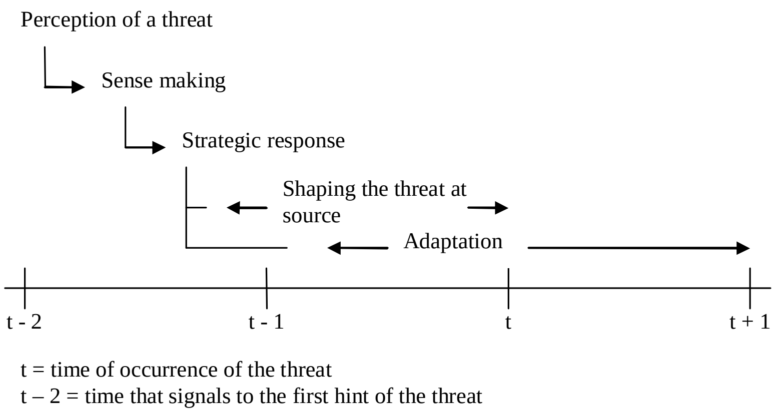

Figure 8. A model of the process of responding to threats

In this model, a threat from the environment does not occur in an instant. It rather emits weak signals of its occurrence in advance (Ansoff 1975). It is important for an actor to be able to perceive such signals because people can only respond to what they perceive (Miles et al. 1974). Environmental scanning and analysis methods can help to identify these signals (Elenkov 1997; Länsiluoto 2004). It is assumed in Figure 8 that the threat is perceived at time (t – 2).

Once a threat is perceived through signals before its occurrence, people try to make sense of it. Sense making involves turning circumstances into a situation that is comprehended explicitly in words and that serves as a springboard for action (Weick et al. 2005, 409). It refers to the process of ascribing meaning to reality (i.e. making it sensible) based on past experiences, beliefs, and assumptions (Weick 1995a). This could also be a prospective activity in which people imagine a meaningful future (Gioia and Mehra 1996). Hansén (1991) calls such an activity 'vision'. I believe that people can build their strategic responses on their sense making of a threat based on their past experiences, as well as on their visions of how a threat could occur, and how it may affect related actors. Sense making may also be a collective activity (Maitlis 2005; Pater and Van Lierop 2006). By interacting with other actors, people are able to gain a better understanding of threats (Calton and Payne 2003). Thus, they may collectively make sense of a threat through sense giving (i.e. influencing others' understanding of it) (Maitlis 2005). Communication between parties is an important aspect of collective sense making, and a genuine dialogue may lead to the co-creation of reality (Crane and Livesey 2003). Collaboration between different actors may be essential in addressing threats (Andriof and Waddock 2002; Pater and Van Lierop 2006).

Once a threat is perceived and made sense of, there is need to respond. This can be in two ways: shaping the threat at source (drawn from the strategic choice and collective action perspectives) or adaptation (drawn from the contingency perspective). According to the model, actors first try to shape the threat at source. They may or may not succeed given that they are rationally bounded in their abilities (cf. Simon 1945). In case of failure they need to adapt to avoid the negative impacts of the threat.

Let us now apply this model to the system of the firm and its primary stakeholders from the perspective of primary stakeholders. Earlier in section 2.5 I concluded that the firm and its primary stakeholders form an open social system. This is illustrated in Figure 9 by a dotted line around them.

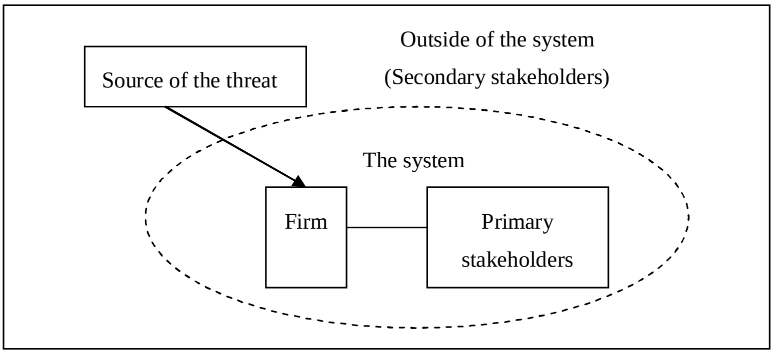

Figure 9. The system under threat from outside [46]

Outside actors may trigger threats to the firm, and these may also affect some of its primary stakeholders (see Figure 9). These outside actors are secondary stakeholders which may affect the firm's performance. In the context of this research such actors include for example EU regulatory organizations, competitors, hedge funds, etc. Threats from these actors may be a new legislation prepared by the European Commission, the entry of a strong competitor into the firm's markets, or the interest of hedge funds to acquire the firm.

I should note that the firm could resolve the threat by itself without the involvement of its primary stakeholders, but given the focus of this research such cases are not taken into account.

[46] In the figure the relationships within the system are simplified and represented by a single line between the firm and its primary stakeholders. In reality, multilateral relationships exist between various primary stakeholders (cf. Zietsma and Winn 2008).

Drawing from the strategic choice perspective, the collective action perspective, and the contingency perspective, I propose the following typology of primary stakeholder contributions to the resolving of threats of market integration in the EU.

1. Type-I: Shaping the threat at source. People are able to create their environments (Weick 1995a, 34). Shaping the environment refers to its active formation (Smircich and Stubbart 1985, 724). From the strategic choice and collective action perspectives, a primary stakeholder may be able to shape the threat at source and perhaps eliminate it before it materializes. This is represented in Figure 10 by the bold arrow from the primary stakeholders to the source of the threat.

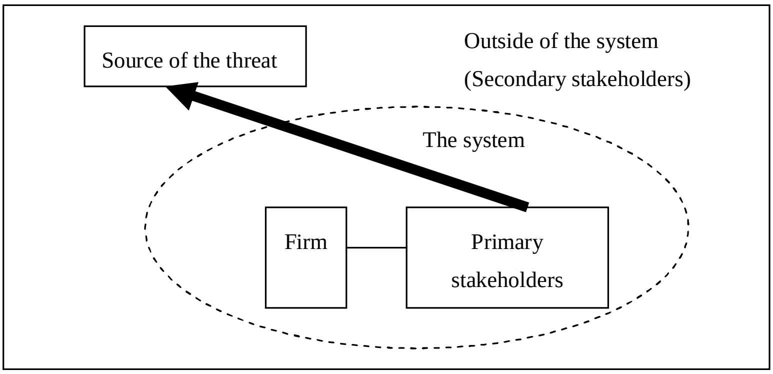

Figure 10. Shaping the threat at source

In the context of this research, this contribution could be in the form of lobbying EU regulatory organizations against a new regulation and preventing its adoption, for example. A primary stakeholder could affect EU regulatory organizations alone (strategic choice perspective) or through participating in a coalition with other primary stakeholders and/or the firm (collective action perspective).

2. Type-II: Adaptation within the system: shaping the firm or the conditions in the system. This type of contribution is derived from the contingency perspective: when the threat cannot be tackled at source, the system may need to adapt. It is initiated by a primary stakeholder, the aim being to protect the system from the negative impacts of the threat (see Figure 11).

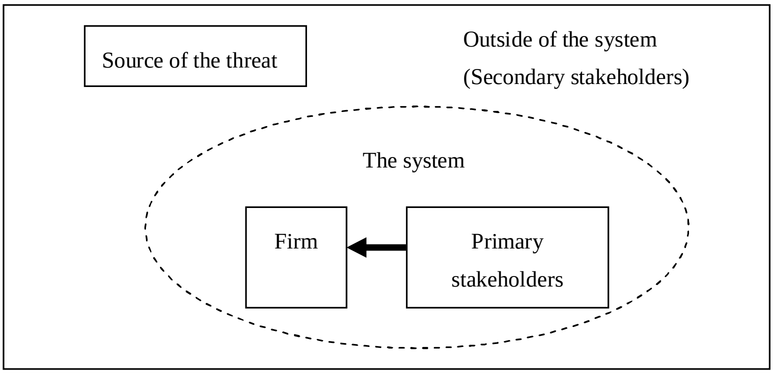

Figure 11 Adaptation within the system: shaping the firm or the conditions in the system

This is different from the first type of contribution in that the primary stakeholder does not tackle the threat at source but targets the firm itself or certain conditions in the system. This is represented in Figure 11 by the bold arrow from the primary stakeholder to the firm. An example of this type of contribution can be stakeholders' acquisition of the shares of the firm in order to protect the firm from the threat of acquisition by competitors or hedge funds.

3. Type-III: Adaptation within the system: compensation-related sacrifices or increased input. This type of contribution, which is also derived from the contingency perspective, occurs when the threat can neither be eliminated at source nor avoided through shaping the firm or the conditions in the system. This type of adaptation is usually initiated not by a primary stakeholder but by the executive management of the firm (as illustrated by the bold arrow in Figure 12).

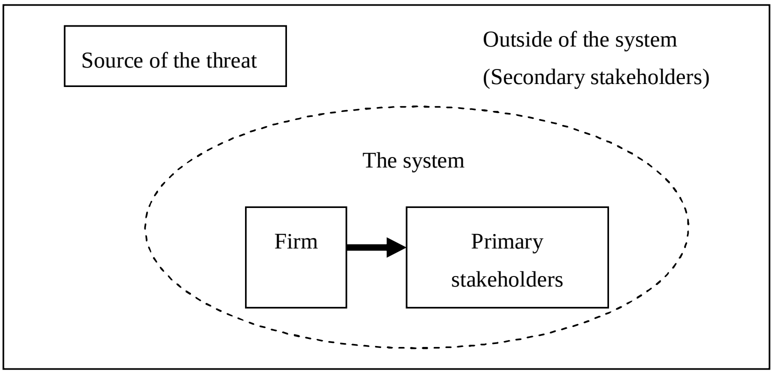

Figure 12. Adaptation within the system: compensation-related sacrifices or increased input

When the negative effects of the threat cannot be eliminated the firm's executive managers may demand contributions from primary stakeholders. Such contributions may be in the form of compensation-related sacrifice (e.g., employee layoffs, reductions in supplier prices or dealer commissions, a decrease in dividends) or increases in input (capital increase, requests for new investments from suppliers and dealers[47]). In this case the negative effects of the threat are shared among the primary stakeholders in order to relieve the burden on the firm. It is the least desired type of contribution, but it is sometimes necessary if the negative impact of the threat severely affects the firm's profits. Since this kind of contribution is not desired, some primary stakeholders may resist making it.

This typology of primary stakeholder contributions is helpful in answering research question 1. To answer this question there is further need to understand the determinants of the types of contributions. This is the subject of research question 2, and I address it in the next section.

2.7 Determinants of the Types of Primary Stakeholder Contributions

Research question 2 concerns the determinants of types of primary stakeholder contributions. In the following sub-sections I build a model based on the review of relevant literatures in the descriptive stream of stakeholder theory, resource dependence perspective, and network perspective as well as literature on power.

[47] As an example, car manufacturers have been globalizing their operations since the 1990s, and they have also requested their suppliers to follow them (Kinkel and Lay 2005; Kappelhoff 2005).

2.7.1 Searching for Determinants in the Literature

Freeman and Reed (1983) recognize that the nature of the stake in the firm and the nature of stakeholder power are two key attributes in relationships between stakeholders and the firm. According to them, the stake in the firm may be equity-based (e.g., shareholders), economics-based (e.g., employees, suppliers, customers, dealers, creditors), or influence-based (e.g., the home government). Equity-based stakes confer formal or voting power, economics-based stakes give economic power, and stakeholders with influence-based stakes have political power. Some stakeholders can have more than one type of stake and respective power.

Stakeholders make claims on the firm to which executive managers need to respond (Hill and Jones 1992). Rhenman (1964) points out that the goals and needs of stakeholders are a significant factor governing stakeholder claims: since they may be in conflict (Rhenman 1964; Calton and Payne 2003), executive managers may need to prioritize them (Mitchell et al. 1997). Stakeholder salience refers to the degree to which a claim has priority in the eyes of the firm's executive managers. Mitchell et al. (1997) identify three influential attributes of stakeholder salience, namely the legitimacy of the claim, the power of the stakeholder to influence the firm, and the urgency of the claim.

Legitimacy refers to appropriateness within some socially constructed system of norms, values, and beliefs (Suchman 1995). The legitimacy of a claim implies something 'at risk' (Mitchell et al. 1997), and is higher if it is backed up by various centers of power (Stinchombe 1968).

As mentioned in connection with the resource dependence perspective in sub-section 2.4.2, *power* refers to the (potential or actual) ability to impose one's own will on a relationship partner (Etzioni 1961; Reitz 1981) or to the overall ability to affect outcomes or to get things done (Mintzberg 1983).

Urgency refers to the importance of the claim to the stakeholder, and its time-sensitivity (Mitchell et al. 1997). A claim on the firm matters to a stakeholder owning relationship-specific assets and/or having high expectations from the firm (ibid.).

In sum, the stakeholder that is the most salient in the eyes of the firm's executive managers is the one with a legitimate claim at risk that is important and time-sensitive, and when the stakeholder has access to the means of power to influence the firm. Agle et al. (1999) provide empirical support for the link between these attributes and stakeholder salience.

Similarly, Kochan and Rubinstein (2000) propose three criteria for identifying critical stakeholders in the firm, namely providing critical resources, having something ‘at risk’, and having the power to affect the firm’s performance.

The *resources* provided include inputs (Ahlstedt and Jahnukainen 1971) such as capital, labor, and raw materials.

The *risks* at stake include equity (e.g., shareholders), revenues (e.g., suppliers, dealers, creditors, and the home government), employment (e.g., employees), and the continuity and quality of goods and services (e.g., customers).

In this research the *power* of primary stakeholders refers to their capacity to influence the source of the threat (i.e. to shape the threat at source) or the system (i.e. to shape the firm or the conditions in the system) in resolving threats. It could be related to the importance of the resources they provide, the degree of their control over the resources, and the existence of resource alternatives (Pfeffer and Salancik 1978). It may also be related to their access to resources (Brass and Burkhardt 1993), or to their legal rights and legitimacy in terms of imposing their choices on others (Stinchombe 1968; Mintzberg 1983).

The type of stakeholder engagement and the willingness of stakeholders to act may also depend on the particular issue facing them and the firm (Savage et al. 1991; Lozano 2005). Rowley and Berman (2000) argue that industry characteristics and the institutional context may also be important determinants of stakeholder willingness and type of engagement.

In sum, the determinants identified in the literature as having the potential to influence primary stakeholder contributions in the face of threats include *stakeholder power* (Mitchell et al. 1997; Kochan and Rubinstein 2000), the *urgency of the claim* (Mitchell et al. 1997), the *legitimacy of the claim* (ibid.), the *nature of the stake* (Freeman and Reed 1983), *stakeholder goals and needs* (Rhenman 1964), *stakeholder resources* (Kochan and Rubinstein 2000), *risks* (ibid.), the *industry structure* (Rowley and Berman 2000), the *network position* (Rowley 1997), the *nature of the issue* (Savage et al. 1991; Rowley and Berman 2000; Lozano 2005), and the *institutional context* (Rowley and Berman 2000). In the next sub-section I try to clarify the determinants.

2.7.2 Clarifying the Determinants

Some of the determinants overlap and some need adjustment because they were initially identified from the firm’s perspective. My aim in the following paragraphs is to rework these determinants and the relationships between them in order to provide a clearer model.

First of all, the term ‘claim’ sounds issue-specific to me. As I understand it, it refers not to a particular issue, but to the stake or interest of the stakeholder at risk. I therefore prefer to use the term ‘stake’ rather than ‘claim’.

Secondly, in my opinion, ‘goals and needs’ with reference to primary stakeholders are a very broad and also a very variable term, which makes it difficult to integrate into a theory and to derive testable propositions. A restricted but focused interpretation would be that they refer to the expectations that primary stakeholders have of the firm. In other words, it resembles how the firm fares in meeting their goals and needs. As Ahlstedt and Jahnukainen (1971) suggest, these expectations could be denoted by the word ‘compensation’. This is perhaps a simplification, but I believe that it captures the essence of the phenomenon while allowing for the emergence of testable propositions. I have therefore chosen to replace ‘goals and needs’ with ‘compensation’.

Thirdly, power can be viewed as a relationship-specific (Etzioni 1961; Emerson 1962; Reitz 1981) or a general attribute (Mintzberg 1983). In this research I adopt the relationship-specific conceptualization because such differentiation is implicit in the developed typology. In contributions to shape the threat at source it is the power relationship between the primary stakeholder and the source of the threat whereas in contributions to shape the firm or the conditions in the system it is the power relationship between the primary stakeholder and other actors in the system (i.e. the firm and other primary stakeholders), and in contributions of compensation-related sacrifices or increased input it is the power relationship between the firm and the primary stakeholder.

Pfeffer and Salancik (1978) define power as a function of resource importance, resource control, and resource alternatives. Kochan and Rubinstein (2000) also mention resources as an important source of power. In line with Brass and Burkhardt (1993), I argue that power stems not only from owned resources but also from accessible resources. A further potential source would be legal rights and the accompanying legitimacy[48] in terms of imposing choices on others (Stinchombe 1968; Mintzberg 1983).

In sum, I view power as a potential determinant of the ability of the primary stakeholder to contribute (and the type of contribution), and owned and accessible resources together with legal rights/legitimacy as its determinants (see Figure 13).

Fourthly I view the importance of the stake[49] as a potential determinant of the willingness of the primary stakeholder to make a contribution. As Mitchell

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48 Legitimacy of power refers to its being backed up by other centers of power (Stinchombe 1968).

49 Mitchell et al. (1997) call it urgency of the claim.

et al. (1997) argue it may arise from two sources that are at risk: (1) the compensation earned from the firm, and (2) the relationship-specific investments of the primary stakeholder in the firm[50] (see Figure 13).

Fifthly, the nature of the issue refers to the nature of the threat (e.g., being a threat only to one firm or a number of firms, concerning a certain part of the system or the whole system). In my opinion, the nature of the threat determines the degree to which a certain primary stakeholder may be affected by it. For example, if a threat is only specific to the distribution channel, dealers may be the most affected and also the most likely to contribute. Therefore, the nature of the threat may determine the willingness of the primary stakeholder to make a contribution. It may also determine the degree to which the threat can be shaped at source, and consequently which primary stakeholders are able to contribute. Since it is not a stakeholder attribute, I prefer not to consider the nature of the threat as a direct determinant of the type of primary stakeholder contribution: I rather see it as a moderating factor in determining the willingness and ability of the primary stakeholders to contribute (see Figure 13).

Sixthly, the institutional context seems to me a background factor that may affect for example the determination of power through legal rights. Therefore, I prefer not to include this as a direct determinant of the type of primary stakeholder contribution.

Finally, the industry structure refers to whether the industry is a monopoly or an oligopoly, or fragmented. In my opinion, it is also more of a background factor that may have an impact for example on the power of primary stakeholders such as suppliers and dealers. For this reason I prefer not to consider industry structure as a direct determinant of the type of primary stakeholder contribution.

Based on these deductions I propose in the following sub-section a model of determinants of the types of contributions.

2.7.3 Propositions on Determinants of the Types of Contributions

Following on from the above discussion, Figure 13 presents a set of potential determinants of the types of primary stakeholder contributions against the threats related to market integration in the EU. These are reflected in 15 propositions. The propositions are inserted into the figure (P1-P15) in order to better align the figure with the text following it.

[50] The importance of relationship-specific investments is also highlighted in the network literature (cf. Bensaou 1999).

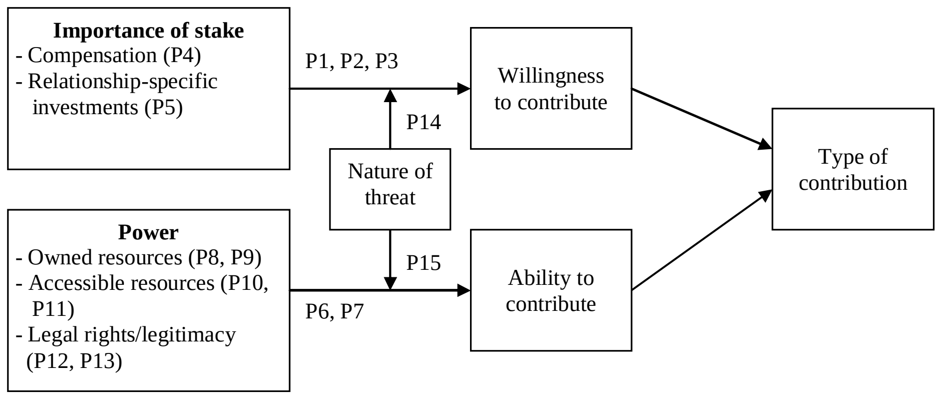

Figure 13. A model of determinants of the types of primary stakeholder contributions [51]

Propositions Related to Importance of Stake:

In this set the importance of the stake is argued to be a determinant of the willingness of a primary stakeholder to make a contribution. It refers to the degree of risk to which the primary stakeholder is exposed due to the threat to the firm (Mitchell et al. 1997).

The stake may be of high or low importance. High importance could mean either high relationship-specific investments in the endangered firm or valuable compensation from it (Mitchell et al. 1997). A contribution in a strategic response usually requests the allocation of resources from the primary stakeholder, which may have stakes in a number of firms. It may not contribute to them all, and thus needs to prioritize. In such a situation I believe that the importance of the stake is a major decision-making criterion. A primary stakeholder will be more willing to contribute if the importance of its stake in the firm is high, and vice versa. On the basis of these arguments from the descriptive stream of stakeholder theory I am able to make the following two propositions.

P1. Given that it has the power, a primary stakeholder is more likely to shape the threat at source, or shape the firm or the conditions in the system in case of a threat if the importance of its stake is high.

[51] Compiled from Etzioni 1961; Emerson 1962; Stinchombe 1968; Ahlstedt and Jahnukainen 1971; Pfeffer and Salancik 1978; Mintzberg 1983; Savage et al. 1991; Brass and Burkhardt 1993; Mitchell et al. 1997; Bensaou 1999; Kochan and Rubinstein 2000; Lozano 2005.

P2. Even though it has the power, a primary stakeholder is less likely to shape the threat at source or shape the firm or the conditions in the system in case of a threat if the importance of its stake is low.

According to the model, if the threat cannot be shaped at source or avoided by shaping the firm or the conditions in the system, then a negative impact may be unavoidable, and the firm's executive managers may demand compensation-related sacrifices or increased input from primary stakeholders. In that case, some of those with stakes of low importance may leave the system, and some of the more powerful may resist compensation-related sacrifice. However, drawing from the descriptive stream of stakeholder theory (cf. Mitchell et al. 1997) I argue that primary stakeholders with highly important stakes will be likely to make such sacrifices or to increase their input regardless of their power status. This is reflected in the following proposition.

P3. Primary stakeholders with highly important stakes are likely to make compensation-related sacrifices or increased input if the situation arises from an inevitable economic necessity.

Again drawing from the descriptive stream of stakeholder theory, the importance of the stake is determined by the primary stakeholder's compensation from the firm and its relationship-specific investments in it (Mitchell et al. 1997). This is reflected in the following two propositions.

P4. The amount of compensation earned from the firm increases the importance of the primary stakeholder's stake in the firm.

P5. The relationship-specific investments of the primary stakeholder increase the importance of its stake in the firm.

Propositions Related to Power:
The model argues that power is a determinant of the primary stakeholder's ability to contribute, referring to its possession of important resources (Pfeffer and Salancik 1978; Kochan and Rubinstein 2000), its access to important resources (Brass and Burkhardt 1993), or the possession of legal rights and legitimacy (Stinchombe 1968; Mintzberg 1983) that allow it to impose its will on the source of the threat or the system. These are extracted from the descriptive stream of stakeholder theory, resource dependence perspective, network perspective, and literature on power, and they are reflected in the following eight propositions.

P6. Given that a primary stakeholder has a highly important stake in the firm, it will shape the threat at source if it has the power to influence the source of the threat.

P7. Given that a primary stakeholder has a highly important stake in the firm, and that the threat cannot be eliminated at source, it will accomplish adaptation within the system by shaping the firm or the conditions in the system if it has the power to influence the system.

P8. The owned resources of the primary stakeholder increase its power to influence the source of the threat.

P9. The owned resources of the primary stakeholder increase its power to influence the system.

P10. The accessible resources of the primary stakeholder increase its power to influence the source of the threat.

P11. The accessible resources of the primary stakeholder increase its power to influence the system.

P12. The legal rights and legitimacy of the primary stakeholder increase its power to influence the source of the threat.

P13. The legal rights and legitimacy of the primary stakeholder increase its power to influence the system.

Propositions Related to Nature of Threat:
Based on the literature in the stakeholder theory, nature of threat plays a moderating role in the model in determining which primary stakeholders will be willing and able to contribute (Savage et al. 1991; Rowley and Berman 2000; Lozano 2005). For example, the threat could be general or specific (i.e. related to a specific area of the system). In the case of a specific threat contributions are to be expected only from related primary stakeholders, and other primary stakeholders may not be equally willing to contribute. In another example the source of the threat could play a role in the extent to which the threat could be shaped at source and by which of the primary stakeholders. I reflect these roles of the nature of threat in the following two propositions.

P14. The nature of the threat determines which of the primary stakeholders will be willing to make a contribution.

P15. The nature of the threat determines which of the primary stakeholders are able to make a contribution.

The set of 15 propositions constitute my initial answer to research question 2. In the next section I develop a scheme for predicting primary stakeholder contributions in order to answer research question 1.

2.8 A Scheme for Predicting Primary Stakeholder Contributions

Research question 1 asked how various primary stakeholders could contribute to resolving threats arising from market integration in the EU. To answer that, I developed a typology first[52]. Now, there is need to construct a scheme for predicting primary stakeholder contributions. The typology and the determinants of types of contributions help achieve that (see Table 5).

Table 5. A scheme for predicting primary stakeholder contributions [53]

		Power		
		Able to shape the threat at source	Able to shape the firm or the conditions in the system	Not able to shape the threat at source or to avoid it by shaping the firm or the conditions in the system
Importance of stake	High	Likely to shape the threat at source (P1, P6)	Likely to contribute by shaping the firm or the conditions in the system (P1, P7)	Likely to contribute by making compensation-related sacrifices or increase inputs (P3)
	Low	Not likely to shape the threat at source (P2)	Not likely to contribute by shaping the firm or the conditions in the system (P2)	May or may not contribute by making compensation-related sacrifices or increase inputs

According to this scheme, a primary stakeholder is likely to shape the threat at source or to shape the firm or the conditions in the system only if it has a highly important stake in the firm and if it has the necessary power to make such a contribution. In the case of shaping the threat at source, this power relates to the influence over the source of the threat, and in the case of shaping the firm or the conditions in the system it refers to the influence over the

52 See section 2.6.
53 The propositions which support the predictions are listed in parantheses in the table.

system. When a threat cannot be shaped at source and its negative impacts cannot be avoided, then the executive managers may ask for sacrifices from the firm's primary stakeholders. These sacrifices may take the form of a decrease in compensation or an increase in input, in which case primary stakeholders with stakes of high importance, regardless of their powers, would make such sacrifices. In this kind of contribution, willingness to contribute is not voluntary, thus it should be interpreted as involuntary acceptance of sacrifices based on the necessity of the situation. Primary stakeholders with stakes of low importance may or may not contribute depending on the nature and amount of the sacrifice[54].

In order to predict likely contributions of various primary stakeholders there is also need to assess their importance of stake and their power. In the model the importance of the stake is determined by compensation and relationship-specific investments. According to this assessment, a primary stakeholder has a highly important stake if it has high compensation from the firm, if it has high relationship-specific investments, or both (See Table 6).

Table 6. A scheme for assessing the importance of the stake [55]

		Relationship-specific investments	
		High	Low
Compensation	High	Stake is highly important (P4, P5)	Stake is highly important (P4)
	Low	Stake is highly important (P5)	Stake is not so important

According to the model, the power of the primary stakeholder is determined by its owned resources (See Proposition 8 and Proposition 9), accessible resources (See Proposition 10 and Proposition 11), and legal rights and legitimacy (See Proposition 12 and Proposition 13). Based on the assessment of these attributes it would be possible to judge whether a primary stakeholder could shape the threat at source or not, and whether it could shape the firm or the conditions in the system or not. Once we assess power and the importance of the stake for a primary stakeholder, we can predict with the scheme in Table 5 what its likely contribution will be[56]. To achieve that, I need to study primary stakeholders in a real context, in this research in the EU car industry[57].

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54 In case of severe hurt of the firm's profits the home government and shareholders automatically contribute via sacrifices from corporate taxes and dividends respectively.

55 The propositions which support the claims are listed in parantheses in the table.

56 See section 6.3.

57 See sections 4.3, 4.4, 4.5, and 4.6.

At this point I have managed to complete stage two of the research process. In the next chapter I discuss my choices regarding the research methodology and the empirical study.

3 RESEARCH METHODOLOGY

This chapter discusses the choices regarding the methodology, the research context, and the events. It also explains how the data was collected and analyzed, and how the findings were verified.

3.1 The Research Strategy and the Selection of the Methodology

The choice of strategy was guided mainly by the purpose of the research and the approach which I adopted for developing theory.

The purpose of this research is to increase understanding of the contributions of primary stakeholders to resolving threats arising from market integration in the EU. I aimed to achieve this by developing a theory. A theory is the end product of the process of theorizing, which includes activities such as abstracting, relating, generalizing, selecting, explaining, synthesizing, and idealizing (Weick 1995b). Its purpose is to increase understanding through a systemized structure capable of both explaining and predicting phenomena (Hunt 1983). It is a system of constructs[58] and variables[59] in which the constructs and the variables are related to each other by propositions, all bound together by the researcher's assumptions (Bacharach 1989, 498). The key constructs in this research are the willingness to contribute, the importance of the stake, the ability to contribute, and power. Related variables include compensation, relationship-specific investments, owned resources, accessible resources, and legal rights and legitimacy.

As illustrated in Figure 3 in section 1.5, I adopted the 'adaptive theory approach' and benefited from both deduction[60] and induction[61]. Ragin (1994, 57) calls this interplay between analytic frames that are derived from theory and images from data '*retroduction*', and such research is referred to as '*abductive*' (Coffey and Atkinson 1996, 155–156; Gummesson 2000, 64). The

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[58] Concepts that cannot be observed directly

[59] Observed units that can be measured empirically

[60] The roots of deduction lie in the philosophy of rationalism that reality exists independent from being observed by any human mind (cf. Hunt 1983).

[61] The roots of induction lie in the philosophy of empiricism which argues that science begins with observations in the real world (cf. Hunt 1983).

goal in such research is to achieve a two-way fit between explanation and observation (Ragin 1994, 98). That is what I tried to achieve in my research.

In adaptive theory approach a priori theory is shaped by incoming evidence as the data are filtered through (and adapted to) the theoretical materials that are at hand (Layder 1998, 38). This approach assumes that the social world is complex and focuses on the multiple interconnections there; using both deductive and inductive reasoning for developing theory it embraces objectivism and subjectivism in terms of its assumptions about ontology, epistemology, human nature, and methodology (Layder 1998, 133). From an ontological perspective, this research adopts a more objective view by accepting that reality exists independent of its being perceived (cf. Burrell and Morgan 1979). This is evident in that the research aims to build a typology of primary stakeholder contributions and determine underlying factors leading to types of contributions. This view of objectivity is also reflected in the epistemological assumptions in that knowledge is accepted to be cumulative (ibid.). That is why the research starts from literature review and builds on prior knowledge. When it comes to assumptions about the human nature, this research takes a more subjective view in that it accepts a relatively voluntaristic nature of human being[62]. The relativity arises in the sense that the free will is assumed to be rationally limited (cf. Simon 1945). Finally, the research takes again a more subjective perspective in its methodology by exploring the historical background of the research subject (cf. Burrell and Morgan 1979). This is because the objective of the research is theory development, and the phenomenon under study needs a longitudinal methodology. Thus, this research embraces both objectivism and subjectivism in its assumptions.

In deductive reasoning, a priori reason and logic are the means to construct a theory. I partially agree with this way of constructing theory. That is why I tried first to develop a theory by means of deduction. In doing that I built a typology of primary stakeholder contributions[63], identified their determinants[64], and produced a scheme to predict likely contributions of different types of primary stakeholders[65]. I started with a typology because building a typology at the start of the research clarifies thinking, suggests lines of explanation and gives direction to theoretical imagination (Layder 1998, 74). Forming typologies is a key approach in developing middle-range

[62] The research denies completely deterministic nature of human being and excludes for example the natural selection perspective, and the degree of voluntarism varies in the adopted perspectives in answering the first research question.

[63] See section 2.6.

[64] See section 2.7.

[65] See section 2.8.

theories (Pinder and Moore 1979), and this suits well to this research since the developed theory can be classified as a middle-range theory[66].

Despite my partial agreement with the way to construct a theory by deduction, I have serious doubts that a theory based on pure deduction can provide a true account of reality in the first instance because, as with every human being, the creativity of the researcher's thinking is subject to bounded rationality (Simon 1945). Thus, I am of the opinion that connection with empirical data contributes to theory development (Glaser and Strauss 1967). Therefore, I tried to improve the theory by conducting an empirical study. The empirical study consisted of the review of the history of the Volkswagen Group from 1960 to 2005 in the light of market integration initiatives in the EU[67], and analysis of four selected events[68].

The methodology applied in the empirical study was historical analysis, which involves *the review of the past and the analysis of past events in a systematic way* (Gottschalk 1969; Gillette 1988). My choice of this methodology was based on the fact that it is difficult to identify a single threat whereas it is possible to observe a variety of contributions from a variety of primary stakeholders. Therefore, I needed to choose a methodology that would allow me to identify a number of threat events related to market integration in the EU. There were basically three directions in which I could search for such events: time, industry, and region. For reasons of focus, relevance, and personal interest, I preferred to keep the industry (i.e. the car industry) and the region (i.e. the EU) stable and go in the direction of time to find the events in history. Since such events do not take place every day, it was necessary to study within a long time frame. Moreover, market integration in the EU is a historical process originating in the 1950s, and strategic responses to threats are processes in time. In that respect, historical analysis suited the purpose of this research best. I elaborate further on this methodology in the next section.

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[66] A middle-range theory comprises abstractions that may be incorporated into propositions that permit empirical testing (Merton 1967, 39).

[67] See section 5.1. I chose 2005 as the closing date of the review because this is the year for which data was available when I started the empirical study. The establishment of the European Economic Community (EEC) in 1957 motivated me to start the historical review from 1960. In some of the selected events (e.g., the VW law event, the single market and VW event, and the BER 1400/2002 event), contributions from primary stakeholders were observed after 2005. Therefore, 2005 was not necessarily considered a cut-off year in the analysis and I included later contributions.

[68] See sections 5.2, 5.3, 5.4, 5.5 and 5.6.

3.2 Historical Analysis

Indeed, I had difficulty giving a name to the methodology which I used in this research. The reasons for this were that the studying of events is similar to case-study methodology[69], the term 'longitudinal retrospective' is used in business research to refer to studying the past, and the terms 'history[70]', 'historical review[71]', and 'historical analysis[72]' are used interchangeably to refer to the same methodology.

In my opinion, the term historical analysis best describes the nature of the methodology applied in this research, for the following reasons.

First, case study may not be appropriate because the study of case events comprises only the second part of the empirical study, and case study refers to the study of contemporary events (Yin 2003, 5). This research includes events the starting points of which date back at least 20 years[73].

Secondly, in my opinion, 'longitudinal retrospective' refers to a continuous time frame starting from today and going back in time. Since the time frame of the 13th EU directive event does not cover today, I preferred to use the term 'historical' rather than 'longitudinal retrospective'.

Finally, the choice among history, historical review, and historical analysis was not easy. Since it is not the purpose of this research to reconstruct the history of the EU car industry (cf. the definition in Topolski 1976, 51 of 'history') or even to review it[74], I chose to adopt 'historical analysis' to describe the methodology I used.

Nevertheless, I also made use of the literature on the history, historical review, longitudinal retrospective, and case-study methods due to their similarities. Whereas the two first-mentioned were useful mainly during the first part of the empirical study, the literature on the case study was helpful during the second part.

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69 Yin (2003, 5) compares the study of past events (which he calls 'history') to case-study methodology. He finds similarities in that they are both qualitative research methods that are appropriate for studying causal relationships and mechanisms (i.e. answering why and how things happen) in situations in which researchers have little control over the events.

70 Topolski (1976, 51) defines history as a research procedure for the reconstruction of past events. It is the systematic study of the past through a process of critically examining and analyzing past records (Gottschalk 1969; Gillette 1988). In other words, it is the process of collecting, verifying, interpreting, and presenting evidence from the past (Golder 2000, 157). Its main goals are the search for the truth about the past and the search for regularities and causal links among past events (Garraghan 1973).

71 Ghauri et al. (1995, 87) define historical review as the study of the past with the aim to understand the present or plan for the future. The link in time is based on the argumentation that business is path-dependent (cf. Greiner 1972; Teece et al. 1997).

72 See Gummesson (2000, 97-111). See also Reitzel and Lindemann (1982).

73 See Figure 14 in sub-section 3.4.1.

74 I begin with a review, but the core of the empirical study is the analysis of the selected four events.

Historical analysis is a methodology that is useful in longitudinal research involving the study of change (Gummesson 2000, 97). Longitudinal research is recommended for studying processes, describing patterns of change over time, and establishing causal relationships (cf. Miller and Friesen 1982; Pettigrew 1990; Van de Ven 1995; Pettigrew et al. 2001; Menard 2002; Schuh 2004; Paavilainen and Raukko 2006). In that respect, the methodology of historical analysis is similar to the methods used in natural sciences such as astronomy and geology (Jones and Khanna 2006). The similarity arises in that it is a method that accepts and explores complexity by tracing connections between interdependent variables over time. It is exactly this additional level, i.e. the temporal dimension that makes historical analysis well suited to theory development in the context of longitudinal phenomena (Welch 2000). Further motives for using historical analysis as a methodology may include the following.

First, it may not always be possible to understand the current state without an insight into history. This is because the past is our pre-understanding (Gummesson 2000), and some issues cannot be addressed except in the real long run (Jones and Khanna 2006).

Secondly, history provides patterns (Gummesson 2000). It gives a sense of perspective and puts a problem in its context. Thus, it helps us to see where we fit in and also enables us to move beyond issues of path dependence (Jones and Khanna 2006).

Thirdly, history provides a fixed point for triangulation between the past and the present (Gummesson 2000). Therefore, it provides opportunities for comparisons in time. Historical variation may be a valuable complement to contemporary cross-sectional variation (Jones and Khanna 2006).

Finally, history helps us to avoid reinventing the wheel by finding over time examples of phenomena that we might mistakenly consider ‘new’ (Gummesson 2000; Jones and Khanna 2006).

Some philosophers and researchers have not considered historical analysis a scientific method. Aristotle, for example, referred to poetry as more scientific than history[75]. Bonoma (1985) classified the study of archives as non-science, including in the same category the study of stories, myths and legends, and personal opinions[76]. It has been acknowledged in international business research that history matters, but its potential has not been fully exploited (Jones and Khanna 2006).

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75 Quoted in Golder (2000, 156).

76 Ironically, however, Bonoma (1985, 203) cites written archives as a source of data to be consulted in doing case studies.

Despite criticisms, historical analysis is a scientific method for the following reasons, as cited by Gottschalk (1969) and Golder (2000). First, historians collect and evaluate data rigorously. Events are established based mainly on written documents from a variety of sources. Due to the fact that historians have not observed the past events they are studying, they are highly skeptical towards both the sources of evidence and the evidence they collect. In addition, historians do not simply record the past. They analyze causes of past events and provide a narrative. Finally, historians generate knowledge that is subject to falsification.

3.3 The Selection of the Research Context

This research focuses on the EU and the car industry, i.e the industry of passenger cars, within it. I chose the EU as the focus region because the single market represents the highest degree of regional market integration in the world (Scott 1996; Mercado et al. 2001). Cars are mostly consumed in the region of the Triad in which they are produced (Ohmae 1985), possibly for reasons connected with different consumer tastes (North American consumers prefer larger cars whereas Europeans prefer smaller ones, for example), different regulations across the Triad regions, and geographical distance (ibid.). Therefore, the car industry is regional rather than global (Rugman and Hodgetts 2001; Rugman 2003; Rugman and Collinson 2004). Given this regional nature of the industry, it is reasonable to focus on a certain region of the Triad – in this case the EU.

I chose to focus on a single industry because focusing on a single industry may reduce industry-specific variation and also yield a depth that may be difficult to obtain in a multiple-industry context (cf. Hansén 1981; Miles and Cameron 1982; Kleymann 2002). A single-industry focus is also suitable when the perspective is historical (cf. Lamberg and Laurila 2005). The reasons for choosing the car industry are the following.

First, it is an important industry for the EU because car manufacturing constitutes three percent of the gross domestic product, between six and seven percent of total manufacturing employment, and seven percent of total manufacturing output (Commission of the European Communities 2004; Commission of the European Communities 2006a). According to a report published by the European Automobile Manufacturers Association (ACEA), given its close links with other manufacturing industries such as chemicals, plastics, steel, metal-working, and electrical and electronic parts, total direct and indirect employment provided by the industry reaches about 12 million people in the EU-25, which is 43 percent of total manufacturing employment[77] (ACEA 2007). The industry also has strong links with several service sectors, namely research & development (R&D), information technology, financial services, transport, and trade. Its importance to the EU is further strengthened by the fact that automotive exports represent five percent of all EU exports and provide a trade surplus of €35 billion (Commission of the European Communities 2006a).

Secondly, it is '*the industry of industries*', in other words, it is representative of most manufacturing industries (Drucker 1946). Based on this fact, I would assume that findings of this research could be transferable to other manufacturing industries.

Thirdly, it is a highly competitive industry with a regional nature including some of the largest MNEs in the world (Rugman and Collinson 2004).

Finally, it is highly subject to EU regulations due to safety- and environment-related concerns (cf. Wagner 2008).

I chose the car industry rather than the automotive industry which includes also the manufacturing and marketing of light commercial vehicles, trucks, and busses and coaches. This is because passenger cars account for ca. 70 percent of total motor-vehicle production (International Organization of Motor Vehicle Manufacturers 2007), and car transportation constitutes 78 percent of all passenger transport in the EU (German Association of the Automotive Industry 2007, 85). Such a restriction provides focus. If I were to take the automotive industry as a whole, then I would have to consider competition in four different strategic business areas, namely passenger cars, light commercial vehicles, trucks, and buses and coaches. This would be difficult because there are different competitors in each of these areas, and the nature of the competition is also different.

I chose VW as the focus firm for the first part of the empirical study because this German car manufacturer has lived through the market-integration process and has managed to become the market leader in car sales in the EU. Earning 70 percent of its total revenues from the EU, it was probably one of the manufacturers most affected by market integration in Europe. A second reason for the choice was that German car manufacturers are among the most successful, apart from the Japanese and the French, and Germany is a country in which long-term stakeholder orientation is preferred to short-term shareholder orientation (Pries 2005). Therefore, I expected to find contributions from various primary stakeholders behind the success of VW in the EU. Furthermore, the choice of a German firm was motivated by

[77] See Chapter 4 for a review of the car industry in the EU.

my proficiency in the German language, which enabled me to review company documents as well as to follow company news in the local media[78]. Finally, it is important to keep the research practicable within the limits of the researcher's resources (Harrison 2002, 173). Choosing a focus firm for a thorough historical review was deliberate because the period concerned is long.

3.4 The Selection of the Events

Following a review of the history of the car industry in the EU and a review of the history of VW, I identified 16 events and out of those chose four for detailed analysis[79]. As Siggelkow (2007) and Eisenhardt and Graebner (2007) argue, case events can serve as illustration and provide a bridge between rich qualitative evidence and mainstream deductive research. This happened in this research and the analysis of the events contributed to the improvement of the theory[80].

In choosing the events I followed the *principles of theoretical sampling,* which advocate that the choice of events be driven by the theory (Glaser and Strauss 1967, 45). Theoretical sampling focuses efforts on theoretically useful cases, such as those that fill conceptual categories (Eisenhardt 1989, 533). The researcher deliberately seeks to maximize the selected differences or similarities between cases (Partington 2002, 150). Maximizing selected differences increases the likelihood of finding new theoretical properties (Partington 2002). In choosing the events I aimed to maximize differences in terms of the nature of the threat, types of observed contributions, and contributing primary stakeholders[81]. The unit of analysis in the events was the system of the firm and its primary stakeholders.

Whereas Eisenhardt (1989) recommends the study of at least four events in order to generate theory with adequate complexity, Dyer and Wilkins (1991) argue that it is not the number of events but the quality of the story in each one that contributes to better theory generation. This is also true in that there are many classics in business research based on the analysis of a single case[82]. I took these recommendations into account and selected four 'quality' events for improving the theory.

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78 There is extensive secondary material about VW and the car industry.

79 See sub-section 3.4.1 for the selected events and 3.4.2 for the unselected events.

80 See Chapter 6.

81 See Table 7 in sub-section 3.4.1.

82 See Dyer and Wilkins (1991, 614) for a review.

3.4.1 The Four Events

The selected events are the VW law event, the single market and VW event, the 13th EU directive event, and the block exemption regulation 1400/2002 event.

The VW law event[83] involves the European Commission's efforts to abolish the VW law and the strategic responses of VW and its primary stakeholders in return. I chose this event because the abolishment of the VW law would create the takeover threat by hedge funds. This is an interesting event because it presents a contribution to shape the firm or the conditions in the system.

The single market and VW event[84] involves strategic responses of VW and its primary stakeholders against increasing competition from Japanese manufacturers following the creation of the single market in the EU. I chose this event because VW was the most threatened from this development due to its high cost structure and its market leader position in the EU.

The 13th EU directive event[85] involves efforts of the European Commission to create an active takeover market in the EU and the strategic responses of German stakeholders which felt threatened from this development. This is an interesting event in that it shows a contribution to shape the threat at source.

Finally, *the BER 1400/2002 event*[86] involves the European Commission's efforts to liberalize distribution and repair & maintenance networks in the European car industry and strategic responses of car manufacturers and their dealers. The four events cover all three types of contributions and a variety of contributing primary stakeholders (See Table 7).

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[83] See section 5.2 for details of this event.

[84] See section 5.3 for details of this event.

[85] See section 5.4 for details of this event.

[86] See section 5.5 for details of this event.

Table 7. The events and their differences

Name of event	Nature of threat	Types of observed contributions	Contributing primary stakeholders
The VW law event	Concerns VW only	Adaptation within the system: shaping the firm or the conditions in the system	Business-to-business customer and strategic partner
The single market and VW event	Concerns VW as well as other manufacturers in the mass-market segments (e.g., Fiat, Renault, Ford, GM)	Adaptation within the system: compensation-related sacrifices or increased input	Employees, suppliers
The 13th EU directive event	Could concern any firm in the EU. Perceived in Germany as a major threat	Shaping the threat at source	Home government, employees
The BER 1400/2002 event	Concerns distribution and repair & maintenance services in the car industry	Adaptation within the system: compensation-related sacrifices or increased input	Dealers

The studied time frames in the events lie mostly between the late 1980s and 2008 (see Figure 14). The only exception is that I also studied the year 1960 in the VW law event because the VW law was adopted by the Parliament of the Federal Republic of Germany on July 21 of that year. The VW law event included the year 1960 but focused mainly on the time frame from 2000, the year when intentions of the European Commission to abolish the VW law became evident, until 2008.

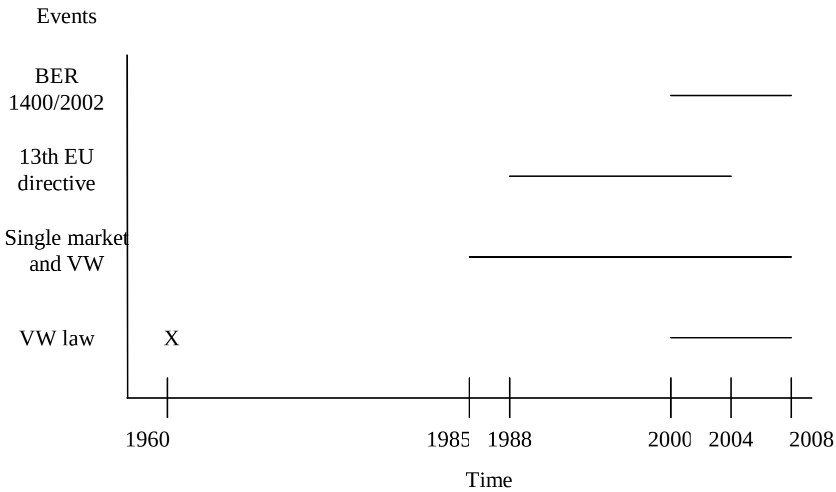

Figure 14. The studied time frames in the events

The time frame of the single market and VW event started from 1985 because the first sign of the creation of a single market in the EU appeared in a White Paper published by the European Commission on June 14 of that year. The increasing commitment of Japanese manufacturers to the EU market following the single market program put pressure on VW to adjust its prices and its cost structure accordingly. This pressure and the need for adjustment became most evident as the 1993 crisis in the European car industry took hold. The time frame extends to 2008 since VW has been continuing to take measures to improve its competitiveness against the Japanese.

The time frame of the 13th EU directive event started from 1988 in that the European Commission issued the first draft 13th EU Directive on December 21 of that year. The directive, which had its origins in the Anglo-American type of corporate governance, was a threat to firms in continental Europe, and above all in Germany. The threat was perceived more clearly in Germany at the turn of the century when the British telecom firm Vodafone acquired the German telecom firm Mannesman in a hostile takeover. The time frame ended in 2004 when a new directive was adopted on April 21 of that year.

The time frame of the BER 1400/2002 event started in the year 2000 when Mario Monti, the EU Commissioner for Competition Policy, gave the first signals of radical changes in distribution and repair & maintenance networks in the car industry in a speech on May 11 of that year in Brussels (Monti 2000). This was perceived as a threat to the existing operations of car manufacturers and their dealers (ACEA and CECRA[87] 2000). The European Commission adopted a new block exemption regulation in 2002 in order to foster competition in the distribution and repair & maintenance networks to the benefit of consumers. The time frame extends to 2008.

3.4.2 The Unselected Events

I also considered, but rejected, twelve other events. In chronological order, they were the following:

The establishment of a customs union in the EEC in 1968. I rejected this event because it constituted an opportunity for VW rather than a threat in that it was beneficial to VW's export strategy in Europe in the 1960s. In addition, it was not yet possible to talk about real market integration in the EU in the 1960s.

The entry of Denmark, Ireland, and the UK to the EEC in 1973. I rejected this event of market enlargement because the focus in this research is more on market integration[88].

The global oil crisis in 1973. Although this event was a threat to all firms, I did not choose it because it was not related to market integration in the EU.

The southern enlargement of the EEC with the entry of Greece in 1981 and Portugal and Spain in 1986. VW took this development as an opportunity to enter the Spanish market by acquiring Sociedad Española de Automóviles de Turismo S.A. (SEAT) in 1986 and moving production of small-size Polo cars from Germany to Spain. This was a threat to VW employees in the Wolfsburg plant in Germany. I rejected this event because the threat was resolved by the VW management (i.e. without contributions from its primary stakeholders) in that they promised to increase Golf production in the Wolfsburg plant to compensate for the loss of Polo production. Besides, this event was related to market enlargement rather than market integration.

The replacement of national quotas against Japanese exports by an EU-wide quota in 1991 which was completely abolished later in 1999. This event is indeed covered under the single market and VW event. I did not specifically focus on it because Japanese manufacturers changed their European strategies from exporting to foreign direct investment (FDI) in the 1990s.

The adoption of EU-wide vehicle type approval in 1992[89]. I rejected this event because the harmonization of technical standards and the adoption of a

[87] The European Council for Motor Trades and Repairs.

[88] In this research I differentiated between market integration (see definition in section 1.1) and market enlargement (joining of new country markets to the single market) and focused on threats arising from market integration only.

single type of vehicle approval system in the EU was more of an opportunity for car manufacturers in terms of reducing their costs.

The entry of Austria, Finland, and Sweden to the EU in 1995. I rejected this because it was related more to enlargement than to integration.

The establishment of a customs union between the EU and Turkey in 1996. I rejected this event also because it was related more to enlargement than to integration.

Legislation on vehicle scrapping and the use of hazardous materials in 2000[90]. I rejected this event because the nature of the threat was similar to that in the BER 1400/2002 event.

The adoption of a single currency in twelve member countries in 2002. I rejected this event because it was more of an opportunity to reduce the risks and costs resulting from currency exchange.

The eastern enlargement of the EU in 2004. I rejected this event because it was also related more to enlargement than to integration.

The European Commission's goals to reduce carbon dioxide emissions to average 120g/km for each car manufacturer by 2012. I rejected this industry-specific event because it was very recent. Thus, there was not enough data to track the strategic responses to resolving the threat.

Having selected the four events in consideration of appropriateness for improving the theory, I continue in the following sections by describing how the data was collected and analyzed, and what I did to ensure verification of the findings.

3.5 Data Collection

In the empirical study I collected mostly qualitative data because qualitative data fits theory development better than quantitative data as it captures better the complexity of the reality (Eisenhardt 1989; Yin 2003; Gummesson 2006). Following recommendations by Gottschalk (1969) and Golder (2000) to be skeptical about historical data, I collected data from a variety of sources including press releases of car manufacturers, press releases of EU regulatory organizations, press releases of industry associations, annual reports of car manufacturers, media news[91], minutes of Board of Directors meetings at VW

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89 Cf. Council of the European Communities (1992a).

90 Cf. European Parliament and the Council of the European Union (2000).

91 Media news in English language was covered mainly by using the electronic databases of the National Electronic Library Interface (NELLI) portal in Finland, and media news in German language was covered mainly by using the electronic databases of the library of the Fachhochschule Braunschweig / Wolfenbüttel University of Applied Sciences in Wolfsburg and the archives of VW.

until 1977, related EU and German legislation, and interviews (see Table 8. See also Appendix 1 for the full list of information sources).

Table 8. Major sources of data in the empirical study

Part of the empirical study	Major sources of data
Review of the history of VW 1960–2005	1) Annual reports of VW for every year from 1960 until 2005 2) Publications on VW 3) Archival documents of VW for the years between 1960 and 1977
The VW law event	1) Press releases of Dr.Ing.h.c.F. Porsche AG (Porsche) about the event 2) Press releases of VW about the event 3) Official documents of the Court of Justice of the European Communities 4) Published opinion of the advocate 5) Archival documents at VW related to the VW law from 1960 6) Media news 7) Interview with the head of the Berlin office of the German association of the car industry on July 13, 2007
The single market and VW event	1) Publications on VW about the event 2) Press releases of VW about the event 3) Annual reports of VW
The 13th EU directive event	1) Official documents of the European Commission, the European Parliament and the Council of Ministers from 1988 until 2004 2) Published speeches of EU commissioners about the event 3) Media news
The BER 1400/2002 event	1) Block exemption regulation 1475/95 (BER 1475/95) and BER 1400/2002 2) Press releases of CECRA and ACEA about the event 3) Published speeches of EU commissioners about the event 4) Media news 5) Interview with the head of the Finnish association of motor trade and repairs on September 19, 2007

Data was collected primarily from written sources because they are considered more reliable in terms of studying the past (Garraghan 1973; Golden 1992). Documentary records constitute a rich source of insights. Indeed, they are often more comprehensive than the kind of material that a researcher who is new to a context could obtain from either interviews or questionnaires (Forster 1994, 148). In choosing written documents I heeded warnings that written documents from the past need to be from competent and trustworthy sources, and that they should not be taken at face value but triangulated with other sources of data (Gottschalk 1969; Forster 1994; Golder 2000; Howell and Prevenier 2001).

I also conducted two interviews in order to gain further insights (see Appendix 3). I conducted the first one on July 13, 2007 in Berlin with the head of the Berlin office of the German Association of the Car Industry, Dr. Gerd Hoff. This interview provided me with insights into the German car industry, about the lobbying efforts of German car manufacturers in the EU, and about their relationships with different types of primary stakeholders. During the interview I also had chance to ask about the VW law event. Recording and transcribing interviews enables the maximum use of relevant data (Partington 2002, 144). Following this recommendation, I recorded the interview on audio-tape and later transcribed it. It was conducted in the German language. In order to make sure that I transcribed the interview correctly, I had it checked and corrected by a German native speaker. I carried out the second interview with the head of the Finnish Association of Motor Trade and Repairs, Mr. Pentti Rantala, who was also a member of the Board of CECRA, on September 19, 2007 in Helsinki. The aim was to gain further insight into the BER 1400/2002 event. Since I already had good knowledge of the event from written sources, this was a semi-structured interview. I also recorded it on audio-tape and later transcribed it for analysis.

There were two major reasons behind my limitation for using interviews in this research. The first one was that I was turned down by the management of VW because they believed that for example the VW law event involved a sensitive issue due to the continuing court process. With the publishing of my thesis and the ending of the court process, I can perhaps hope to have opportunity for interviews with VW management in the future. The second one was related to the criticism that interviews may not be reliable sources of data for eliciting historical accounts because interviewees may not recall such accounts easily, or their recall may be faulty (Golden 1992). Indeed, I acknowledged this issue during my interviews when I noticed that the interviewees had difficulties to recall some specific details on past events. Instead, I found timely-published speeches and publications of involved actors very useful for my study and made extensive use of them. As Welch (2000) suggests, such documents often provide immediate and precise records.

The review of the history of VW was based mainly on its annual reports since 1960. I was provided with electronic copies of the reports during my first visit to the VW archives in Wolfsburg, Germany between May 22 and May 24, 2006. I developed my insights further at this point through reviewing publications about VW and the car industry, and perusing archival documents of VW up to 1977, to which I was allowed access during my second visit in Wolfsburg between July 9 and July 12, 2007[92].

In the VW law event it was a contribution from Porsche that resolved the threat. A key document for understanding this contribution was a mandatory offer by Porsche to the shareholders of VW (published on April 26, 2007), which provided detailed background information on the actions of Porsche and the underlying motives. I also consulted other written material such as press releases of Porsche and VW, published documents of the Court of Justice of the European Communities, published opinion of the advocate, archival documents at VW related to the VW law from 1960, and media news about the event. These were supplemented with data from the interview with Dr. Hoff.

For the single market and VW event I benefited from written sources provided by people who were primarily involved in the design of the contributions. These included two publications by Peter Hartz, the human resources director on the management board of VW in 1993, who devised the concepts of the four-day-week, the VW week, and the breathing company (cf. Hartz 1994; Hartz 1996), and a publication edited by Jürgen Peters, the head of VW's main trade union IG Metall (Hanover region) in 1993 (cf. Peters 1994). These were supplemented with data from VW's press releases and annual reports.

With regard to the 13th EU directive event I benefited mainly from written sources such as official documents of the European Commission, the European Parliament and the Council of Ministers about this event from 1988 until 2004, published speeches of EU commissioners about the event, and media coverage from 1988 until 2004. I accessed the official documents of EU regulatory organizations from PreLex[93] and the Europe Documentation Centre Collection located at the library of the Faculty of Law at the University of Helsinki. I extracted speeches of European commissioners from their personal Internet pages at the European Commission[94].

For the BER 1400/2002 event I benefited from written sources such as the earlier regulation (i.e. BER 1475/95) and the new regulation (i.e. BER 1400/2002), the press releases of CECRA and ACEA, published speeches of EU commissioners, and media coverage since 2000. These were supplemented with data from the interview with Mr. Rantala.

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92 Due to an EU regulation, the archives of VW for the last 30 years are not open to the public, which is why I was allowed access only to documents until 1977.

93 The Internet pages of the European Commission on the monitoring of the decision-making process between institutions, <http://ec.europa.eu/prelex/apcnet.cfm?CL=en>, retrieved on 1.11.2007.

94 See <http://ec.europa.eu/archives/commission_1999_2004/index_en.htm> for the Prodi Commission, and <http://ec.europa.eu/commission_barroso/index_en.htm> for the Barroso Commission, retrieved on 1.11.2007.

3.6 Data Analysis

The data analysis which I explain in this section mainly covers analysis of the four events.

I decided to analyze the data manually rather than use a specialized computer program for qualitative analysis such as NVIVO, NUD.IST, CAQDAS, ATLAS, or QUALRUS. My reasons for making this decision were that the data was at a manageable level, and the guidance by the theory developed in Chapter two eased its organization. The four events yielded a total of 326 documents for analysis (see Appendix 4 for the analysis carried out in a sample document), and all documents are available upon request.

Regardless of whether I used a computer program or not, in the end I was the one to make the necessary judgments in the analysis. As Silverman (2000, 168) argues, "*Theory building is generally done in the mind or with the aid of paper*." Computer programs are useful when the data set is large. In order to make better judgments, I preferred the diligent manual route so that I could stay close to the data, which enhances accuracy in the analysis (Vincze 2004, 117). Perhaps this was also advantageous for my learning in this first experience of qualitative data analysis.

Theory should guide not only what you look for and where you find it in the field, but also what you look for in your data (Strauss and Corbin 1990, 30). Following this suggestion, the data analysis in this research was driven by the theory. The key mechanism applied was '*coding*'[95], which involved the following three stages:

1. Data reduction: Data reduction is the task of selecting, focusing, and simplifying the data (Miles and Huberman 1994). At this stage I used elements of the theory in identifying categories[96], properties[97], and dimensions[98], on the basis of which I extracted and analyzed the data (see Table 1 in Appendix 4).

A problem with using categories from the theory is that there may be the risk of not seeing categories that emerge from the data. Glaser (2001, 77) critically describes this behavior as the *forcing of theoretical codes on the data*. As Silverman (2000, 147) argues: "*Every way of seeing is also a way of not seeing*". Uncategorized activities may sometimes also be equally important. Taking these warnings into account, I paid attention to whether other categories that were not covered in the theory emerged.

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95 Coding of data refers to breaking it down, conceptualizing it, and putting it back together in new ways (Strauss and Corbin 1990, 57).

96 A category refers to a code for a concept.

97 The properties of a category refer to its causal conditions and consequences.

98 The dimensions of a category refer to the range of values that can be attributed to it.

2. Putting back the coded data: Putting back the coded data refers to making connections among categories. In doing so, the researcher needs to identify properties and dimensions for each category and build links between them (Strauss and Corbin 1990, 96–97). Data displays such as tables, matrices, and diagrams are helpful tools in the search for patterns (Miles and Huberman 1994). Another helpful tool is the theoretical memo[99], for as Miles and Huberman (1994, 101) emphasize: "*Writing is thinking. It is the analysis itself*". Data displays and theoretical memos also assist the movement of the researcher away from the data to abstract thinking, and then back to the data (Strauss and Corbin 1990, 199). In this research I benefited from theoretical memos in terms of putting back the coded data (see Appendix 4).

Patterns emerge both within and across case events (Eisenhardt 1989; Yin 2003). In this research, cross-event analysis seemed problematic at first sight in that the four case events were not replicates of each other in terms of the types of primary stakeholder contributions they exhibited. I overcame this challenge following the suggestions of Halinen and Törnroos (2005, 1294) in that I used the same theoretical base and pursued the same objectives for each event.

3. Drawing conclusions: In drawing conclusions from the data through the use of data displays and theoretical memos, I compared them with the theory and tried to achieve double-fitting between the elements of the theory and observations (Ragin 1994, 98).

3.7 Verification of Findings

Verification is the final step after the data analysis before dissemination of the research findings. It is a crucial step that should not be omitted, because as Silverman (2000, 175) argues: "*Unless you can show your audience that the procedures you used to ensure that your methods were reliable and your conclusions valid, there is little point in aiming to conclude a research dissertation*". Different researchers use different terms for the verification criteria they use[100]. I used four criteria that carry the same content but have different names in different studies (see Table 9).

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[99] Theoretical memos are theorizing write-ups of ideas about categories and their relationships.

[100] See Creswell (1998, 200) for a review.

Table 9. Verification criteria in the literature

Criteria	LeCompte and Goetz (1982)	Lincoln and Guba (1985)	Yin (2003); Rowley (2002)	Meaning
1	Internal validity	Credibility	Internal validity	Sense making of findings
2	External validity	Transferability	External validity	Ability to generalize
3	Reliability	Dependability	Reliability	Ability to replicate
4	Objectivity	Confirmability	Construct validity	Ability to get acceptance

Internal validity (credibility): Internal validity refers to the concept that findings make sense and answer the research questions (LeCompte and Goetz 1982; Lincoln and Guba 1985; Rowley 2002; Yin 2003). Linking data well with the categories of the theory, building explanations, considering rival explanations, seeking negative evidence, and checking for internal coherence of concepts all help to improve internal validity (Miles and Huberman 1994; Yin 2003). I took these recommendations into account during the data-analysis process and tried to establish coherent links among the elements of the theory with the aid of the data.

External validity (transferability): External validity is the degree to which the findings can be generalized or transferred to other contexts (LeCompte and Goetz 1982; Lincoln and Guba 1985; Rowley 2002; Yin 2003). The lack of generalizability has been a major criticism against qualitative research, and especially against case studies (Lukka and Kasanen 1995; Gummesson 2000; Siggelkow 2007), and as a result, qualitative research has long been assumed to play its greatest role in the exploratory phases of researching a topic area (Alasuutari 1995; Conger 1998).

In quantitative research, a large enough random sample that is representative of the population enables generalization through statistical analysis. This is not possible in qualitative research, when generalization is analytic or theory-connected (Manning 1982; Yin 2003). In such research sample selection is driven by theory (Glaser and Strauss 1967), and it aims to generalize cases to theoretical propositions rather than to populations (Bryman 1988). As Alasuutari (1995, 156–157) argues, perhaps extrapolation rather than generalization captures better what is intended in case studies. This is because the researcher is trying to relate observations from a case not to a population but to abstract constructs beyond it.

In this research, the four events are representative in that they cover all three types of contributions from a variety of primary stakeholders. In order to increase the external validity of the findings I searched for ‘deviant’ primary stakeholder contributions in the history of VW that could not be categorized in the typology. In addition, I described the characteristics of the events fully in order to allow adequate comparison with each other and other events in the future. Finally, I suggested contexts in which the theory could be further tested[101].

Despite criticisms on generalizing from case studies, I am of the opinion that the elements of the developed theory would apply to a large extent in other contexts such as different regions or different manufacturing industries. This is because both the typology and the propositions (except for maybe Proposition 17[102]) are independent of the context. In my opinion, also Proposition 17 could be transferable to all contexts where regulatory mechanisms function properly. Of course the predictions which are derived from the theory could change in the context of different industries[103] based on the changing attributes of importance of stake and power, but this does not damage the external validity of the theory because the predictions themselves are not elements of the developed theory[104].

Reliability (dependability): Reliability refers to the extent to which findings can be replicated or reproduced by another inquirer (LeCompte and Goetz 1982; Lincoln and Guba 1985; Rowley 2002; Yin 2003). In order to increase reliability in this research I approached the historical data with skepticism and used documents from competent and trustworthy sources (Garraghan 1973; Howell and Prevenier 2001). I consulted data from a variety of sources (Eisenhardt 1989; Forster 1994; Yin 2003). Following suggestions by Golden (1992) and Welch (2000) I used archival data as main sources in historical analysis and benefited from interviews, which may bear biases in this methodology, only as a supplementary source. Finally, a well organized collection of evidence strengthens the repeatability of the research and increases the transparency of the findings (Yin 2003). In order to achieve that I created a database and used reference numbers to link the evidence[105].

Objectivity (confirmability/construct validity): Objectivity refers to whether other researchers can also achieve the same findings from the same data (LeCompte and Goetz 1982; Lincoln and Guba 1985; Rowley 2002; Yin 2003). Gummesson (2006, 175) argues that excluding subjectivity from science completely is unrealistic as it necessitates excluding the personalities of scientists, their personal motives and social behavior. Achieving objectivity in historical analysis may be difficult especially if the analysis is based purely

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[101] See section 7.3.

[102] The context-dependence arises since this proposition specifically addresses EU regulatory organizations. See sub-section 6.2.2.

[103] I would still expect them to hold true for other manufacturing industries since the automotive industry is representative (cf. Drucker 1946).

[104] See Table 2 in section 1.5.

[105] The database consists of four files (one for each event) and a total of 326 documents. The documents are organized in chronological order and numbered.

on written documents (Dovring 1960): written sources need interpretation by a researcher who has not observed the events. In these instances, the researcher relies on his or her own experiences, which may be subject to bias.

I agree with Gummesson (2006) and Dovring (1960). However, I also think that the degree of subjectivity can be minimized. Indeed, compared with interviews for example, the quality of archival data is less dependent on the circumstances under which it was collected (Welch 2000). Popper (1979) suggests the method of falsification for achieving objectivity. This method is based on the premise of seeking to refute the assumed relationships in the theory until they can no longer be refuted. I searched for primary stakeholder contributions in the history of VW that did not fit the typology: I was able to classify all the identified contributions under one of the three types. I also subjected the theory to criticism by experts in purposefully well-selected forums, and improved it accordingly. Finally, following the recommendations of Ragin (1994) and Silverman (2000), I also aimed for 100-percent compliance between data and theory. These attempts aimed to decrease the degree of subjectivity to a minimum.

This discussion on the verification of the findings ends this chapter. The next chapter introduces the research context, namely the EU and its car industry.

4 RESEARCH CONTEXT

Gummesson (2000, 79) recommends arriving at a pre-understanding of the research context in order to avoid shortcomings in the empirical study. In line with this recommendation, this chapter is devoted to providing an understanding of the EU and its car industry. In order to achieve that I start with the history of market integration in the EU and of the roles of the key supranational regulatory organizations in preparing, adopting, and implementing legislation. Following that I compare and contrast shareholder-oriented and stakeholder-oriented corporate governance: an understanding of these different corporate governance systems is important because it is the subject of the 13th EU directive event, and it helps to assess how primary stakeholders such as shareholders and employees can shape the firm. Finally, I study the EU car industry from a historical perspective since 1960 and assess primary stakeholders of car manufacturers. In this research, understaning about primary stakeholders is important to be able predict their contributions and thus to answer research question 1.

4.1 The EU

The EU is one of the key regions in the global economy (Ohmae 1985; Grimwade 1996). It is the most ambitious example of regional market integration anywhere in the world (Scott 1996; Mercado et al. 2001). It is a supranational structure with its own regulatory and judiciary organizations such as the European Commission, the Council of Ministers (i.e. the Council of the European Union), the European Parliament, and the Court of Justice of the European Communities. There are two contrasting views as to what the EU stands for (Pinder 1996): the supranational view and the intergovernmental view.

According to the supranational view, the EU is the ‘United States of Europe’, as pronounced by Winston Churchill in a speech at Zurich University in 1946 (Churchill 1946, reprinted 1997). It carries supranational powers concerning trade, currency, taxation, security, and the environment (Pinder 1996). Supranational law that precedes national law is ensured by a supranational judiciary.

According to the intergovernmental view, the EU represents cooperation among governments in which power is concentrated in the governments, and the role of the union is similar to that of international organizations such as the United Nations, the International Monetary Fund, or the World Bank (ibid.).

The EU is neither a federation like the USA nor an organization simply promoting cooperation between governments (Europa 2006a). It is a unique supranational structure in which member countries give up some of their sovereignty (but still remain sovereign countries) with the goals of achieving political and economic coordination (Fligstein and Mara-Drita 1996) and gaining the strength and world influence that none of the countries would have on their own (Europa 2006a). It is a network involving the pooling of sovereignty (Keohane and Hoffmann 1994). As it lacks police power, however, it is not much of a government, and this is intentional in its organizational design (Fligstein and Mara-Drita 1996). It is founded on cooperation in the areas of the European Community, common foreign and security policy, and justice and home affairs (Salmon 1996; Mercado et al. 2001; Bomberg and Stubb 2003). The first area aims at achieving a single market with common policies, the second at establishing common foreign and security policies, and the third at cooperating across borders in matters of justice and home affairs (e.g., asylum, immigration). The subject of this research falls into the first area which I describe from a historical perspective in the following sub-section.

4.1.1 The History of Market Integration in the EU

As defined in section 1.1, regional market integration refers to the cross-border integration of national production, exchange, and financial markets with free flows of goods, services, labor, and capital at a regional level (i.e. negative integration: Scott 1996) along with the shifting of policy-making power from governments of member countries to supranational regulatory organizations (i.e. positive integration: Scott 1996). The dream to achieve a single market in Europe could be achieved step by step (Schuman 1994). An initial step was the signing of the Benelux Customs Union agreement in 1944 between Belgium, the Netherlands, and Luxembourg. This was followed in 1951 by the establishment of a community on the industry level (i.e. the coal and steel industries) between six countries, namely the European Coal and Steel Community (ECSC). Jean Monet, the drafter of the ECSC and the so-called ‘father of Europe’, called it ‘the first expression of the Europe that was being born’ (Urwin 1996, 5). The ECSC included West Germany, France, Italy, Belgium, the Netherlands and Luxembourg, and placed the decision-making about the coal and steel industries in these countries in the hands of an independent, supranational body called the ‘High Authority’ (Europa 2006b). The Treaty came into force in 1952, and Luxembourg became the temporary headquarters.

The ECSC was a narrow arrangement limited to the coal and steel industries (Parsons 2006). A greater step towards integration occurred in 1957 when the same six countries signed the Treaty of Rome, creating the EEC. The Treaty came into force in 1958, and Brussels became the EEC headquarters. This was a move towards stage one of economic integration, namely the free trade area (cf. Balassa 1961).

The economic success of the EEC led other Western European countries, which had previously rejected involvement, to revise their opinions and to seek membership (Urwin 1996). A separate movement took place in Europe in 1960 when Austria, Denmark, Norway, Portugal, Sweden, Switzerland, and the UK formed the European Free Trade Area (EFTA) by signing the Stockholm Convention. In 1961 Ireland, the UK and Denmark, and in 1962 Norway, formally applied to join the EEC. Negotiations with all applicant countries were suspended in 1963 when France doubted the political intentions of the UK (Europa 2006b). A key characteristic of the integration process in the 1960s was the non-cooperative behaviors of member countries, and especially of France. The French president Charles de Gaulle threatened the EEC in 1963, 1964, and 1965 with ultimatums: do it his way or France would destroy the entire project (Vanke 2006). For example, as set out in the Treaty of Rome, the EEC was expected to move in 1966 to qualified majority voting in the Council of Ministers. Since Charles de Gaulle would not take the risk of France being outvoted in decisions, he provoked a crisis in 1965 that was resolved by the Luxembourg Compromise of 1966, allowing countries to exercise a veto in decisions when their national interests might be adversely affected (Urwin 1996). Charles de Gaulle’s view of the EEC was intergovernmental as he described it as a ‘concert of European states’ (De Gaulle 1994). Thus, in the 1960s sovereignty remained with the member countries, and it passed to the supranational level only when and to the extent that member countries were willing to cede it (Martin 2006, 140). It was only on July 1, 1968 (eleven years after the signing of the Treaty of Rome) that the Customs Union could come into force. This was a move from stage one to stage two of regional economic integration (cf. Balassa 1961).

Griffiths (2006) calls the 1970s a ‘dismal decade’ for European integration. Intergovernmental behaviors continued, and the EEC experienced severe turbulence as it tried to digest UK membership in 1973 and faced two global economic oil crises, one in 1973 and the other in 1979. The UK’s membership was perceived suspiciously, especially by France. Charles de Gaulle feared that UK membership would be a ‘Trojan horse’ for bringing American influence into Western Europe (Lynch 1996, 61). Finally, after two vetoes (in 1963 and 1967), the UK, together with Denmark and Ireland, became members of the EEC as of January 1, 1973. The UK had an intergovernmental view of Europe (Thatcher 1994). It did not want to weaken its ties with the USA and the Commonwealth, but it did not want to be out of the EEC either. As a result, it pursued a pragmatic line by focusing on short-term problem solving, maximizing national interests, favoring the EEC’s enlargement but not its integration, and reducing the costs of membership. Despite signing Free Trade Area agreements with EFTA in 1973, EEC member countries increased protective measures (e.g., non-tariff barriers) even against each other in response to the two oil crises in the 1970s, which triggered high inflation, high unemployment, and stagnation of growth.

At the 25th anniversary of the Treaty of Rome in 1982, Pieter Dankert, the president of the European Parliament, compared the EEC to a ‘feeble cardiac patient whose condition was so poor that he could not even be disturbed by a birthday party’ (Griffiths 2006, 187). Enlargement continued as Greece became the tenth member as of January 1, 1981; Spain and Portugal joined as of January 1, 1986; and Germany was reunified in 1989. Nevertheless, the EEC was still far from being a Common Market (stage three of economic integration: cf. Balassa 1961) as the member countries continued to erect non-tariff barriers against each other (Commission of the European Communities 1985; Ludlow 2006). In the car industry, subsidies were given by home governments to save their national champions from bankruptcy (e.g., the UK government to British Leyland (BL), the Italian government to Fiat, and the French government to Renault).

At the beginning of the 1980s not only did American firms increase their lead over Western European competitors, Japanese firms also emerged as serious challengers (Ludlow 2006). Market fragmentation in Europe was believed to be a major reason why European industries were less competitive in world markets (Cecchini 1988). Trapped in their small, semi-protected national markets, European firms lacked both the incentives to invest in new technologies and the economies of scale that American and Japanese firms had due to their larger home markets (Ludlow 2006). In these circumstances the European Commission, led by Jacques Delors, took the initiative and issued a White Paper on June 14, 1985 on completing the internal market. The aim was to create a single market in which resources (i.e. goods, services, labor, and capital) would flow freely.

Indeed, this ‘relaunching of Europe’ arose partly from demands of business leaders from Europe’s largest firms (Greenwood 1997, 1). Worried about *losing out in competition to American and Japanese firms, they saw the single market as a strategy for survival (ibid.).*

The second half of the 1980s was an active period of market integration (Ludlow 2006). The Single European Act, signed on February 28, 1986, extended the scope of the qualified majority-voting procedure, and it became the norm for most decisions related to the single market (Dinan 1999). This marked a shift from the intergovernmental nature of the EEC towards the supranational type. It implied a transfer of power from the governments of member countries to the supranational organizations, which in turn contributed to 'positive integration', i.e. the harmonization of national policies (Scott 1996). The European Parliament was given a greater role in the legislative process, and the European Commission became the driving engine for the implementation of the single market. In order to achieve this goal, the European Commission suggested measures to remove all non-tariff barriers between member countries, which existed in the form of physical barriers (e.g., border stoppages, customs controls), technical barriers (e.g., divergent product standards), and fiscal barriers (e.g., protectionist government policies).

The Single European Market was officially established on January 1, 1993 with the free flow of goods, services, labor, and capital, and the EU was officially established when the Maastricht Treaty[106] came into force on November 1, 1993. The establishment of the EU was a move towards the Common Market (cf. Balassa 1961). The single market program contributed to 'negative integration', i.e. the liberalization of market forces within the region (Scott 1996). Enlargement and integration went hand in hand in the 1990s and the 2000s. The European Economic Area (EEA) was created between the EU and the EFTA countries on January 1, 1994. Austria, Sweden, and Finland joined the EU on January 1, 1995. The Customs Union between the EU and Turkey came into force on January 1, 1996. The entry of Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, and Slovenia on May 1, 2004 was the biggest enlargement in the Union's history, and Bulgaria and Romania became members on January 1, 2007.

Efforts towards monetary union also gathered pace with the Treaty on the EU, which stipulated four convergence criteria among the member countries: price stability (maximum allowed inflation 1.5 percent higher than the average of the three best-performing member countries), budgetary discipline (maximum allowed budget deficit three percent of the gross domestic product, and a public debt ratio not exceeding 60 percent of the gross domestic product), currency stability, and interest-rate convergence (maximum allowed interest rate two percent higher than the average of the three best-performing

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106 The treaty was signed on February 7, 1992.

member countries) (Dinan 1999). The European Central Bank was established on June 1, 1998 in Frankfurt, and national central banks became branches of this independent bank. On January 1, 1999 exchange rates were fixed irrevocably among twelve member countries of the EU-15 (excluding the UK, Sweden, and Denmark), and finally a single currency, the Euro, entered into circulation in these twelve countries on January 1, 2002. These developments marked the transition of the EU into an Economic Union (cf. Balassa 1961).

Despite these considerable achievements towards market integration, the economic performance of the EU has been mixed (Sapir et al. 2004). While macroeconomic stability improved during the 1990s, the single market program did not deliver satisfactory growth performance and fell short of some expectations (ibid.). For example, the economic goal of the EU, which is to become the most competitive and dynamic knowledge-based economy with sustainable economic growth and greater social cohesion by 2010, is yet to be achieved. The move towards deeper integration on the one hand and the digestion of the recent enlargements on the other are challenges facing it.

Following this historical review I will consider in the following sections how the regulatory mechanism works in the EU, and how various actors are able to lobby the regulatory organizations.

4.1.2 The Regulatory Mechanism in the EU

It is particularly important to understand the regulatory mechanism and the working of the supranational organizations involved in order to investigate the first type of contribution, namely shaping threats at source.

By regulatory mechanism I mean both the preparation and the adoption of legislation and its proper implementation. Treaties and laws adopted by the EU regulatory organizations constitute sources of legislation which can be of. four types: regulations, directives, decisions, and recommendations and opinions (Nugent 1994; Goodman 1996). A regulation is of general application, binding in its entirety and directly applicable in all member countries. A directive is different in that it is not binding in its entirety but only in the result to be achieved: the choice of method of application is left to the national authorities. A decision is specific in that it addresses a specific set of actors, and is binding in its entirety. Recommendations and opinions are not binding and do not formally constitute part of EU law.

The preparation and adoption of legislation mainly involve the European Commission, the Council of Ministers, and the European Parliament while the responsibility for implementation rests mainly with the European Commission, and disputes arising during the implementation phase are handled at the Court of Justice of the European Communities, the Court of First Instance, and at national courts (see Figure 15).

LEGISLATION PREPARATION & ADOPTION	LEGISLATION IMPLEMENTATION
Legislation Proposal European Commission	Implementation European Commission
↕	↕
Co-decision Procedure European Parliament Council of Ministers	Resolving of Disputes Court of Justice of the European Communities Court of First Instance National courts

Figure 15. The EU regulatory mechanism

The Preparation and Adoption of Legislation: The European Commission is entitled by the Treaties to initiate legislation that represents the general interest of the EU and its citizens (Bomberg et al. 2003). This happens in the following way. At first, a related Directorate-General (DG)[107] in the European Commission initiates new legislation and prepares a draft via internal consultation with all related DGs and Services in the Commission and external consultation with national authorities, experts, interest groups, and other stakeholders. The draft is revised within the Commission until it is approved by the College of Commissioners[108]. As the College of Commissioners is expected to be independent of national interests in the pursuit of its duties, the European Commission has more of a supranational nature, and it has been the driving force behind market integration in the EU since 1985 (Edwards and Spence 1997). The cabinets[109] of commissioners play a key role in

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[107] DGs are like mini Ministries, but they are not executive organizations (Spence 1997). They are not directly linked to commissioners because there is no direct correspondence between the competences of DGs and the portfolios of policy areas allocated to commissioners. The European Commission is organized in 26 DGs and nine Services, which are required to work closely together in the preparation of legislation and decisions.

[108] The European Commission is made up of 27 commissioners (each from a member country). This group of commissioners is also called the ‘College of Commissioners’ (Commission of the European Communities 2007a).

[109] Each commissioner has his or her own circle of six advisers, called a ‘cabinet’ (cf. Donelley and Ritchie 1997). Cabinets play a major role in the day-to-day running of the Commission. They gather

intermediating between the DGs and the College of Commissioners during this process. At the initial stages of legislation preparation the cabinets are a primary focus for lobbying among industrial and national interest groups (Donelley and Ritchie 1997). The draft legislation must be agreed upon by the cabinets and the chiefs of cabinet, and finally by the College of Commissioners. It may be extensively revised during this process. At the final stage the College of Commissioners may accept the legislation, reject it, or send it back to the relevant DG for revision. Once the draft legislation is approved, it becomes a 'European Commission proposal' and is sent to the European Parliament.

For a European Commission proposal to come into force it must be approved by the European Parliament[110] and the Council of Ministers[111] through a co-decision procedure. This procedure applies to legislation related to areas such as internal market measures, the free movement of workers, consumer protection, public health, and environmental programs (Greenwood 1997). Under the procedure the European Parliament and the Council of Ministers jointly examine the proposal in a maximum of three readings, with the European Commission playing the role of mediator until the legislation is adopted (Commission of the European Communities 2007a). The European Parliament and the Council of Ministers have equal power to affect the fate of the legislation[112]. The procedure operates as follows (Goodman 1996, 84).

Once the 'European Commission proposal' reaches the European Parliament an assigned parliamentary committee reviews it and prepares a draft opinion. The European Parliament adopts this opinion after a first reading and presents it to the Council of Ministers. The Council of Ministers reviews the opinion and tells the European Parliament its common position on the proposal. The European Parliament then reviews the common position of the Council of Ministers in a second reading and may either approve the legislation proposal, reject it, or suggest amendments to it by absolute majority.

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information and keep their commissioners informed of developments within and outside of their allocated policy areas.

110 The European Parliament is made up of 785 senators, and the seats are shared out in proportion to the population of each member country (European Parliament 2007). The senators sit in Parliament according to their political affinity, not according to their nationality. This makes it a supranational organization.

111 The Council of Ministers, also called the Council of the EU, is made up of ministers of the member countries (Council of the European Union 2007). Since it represents the interests of the governments of member countries, it is an intergovernmental organization.

112 This came into force after the Single European Act in 1986. Earlier the Council of Ministers had been the more powerful organization in adopting legislation, and the European Parliament was regarded as an advisory organization (Nugent 1994; Watson and Shackleton 2003).

In the case of approval, the Council of Ministers adopts the proposal by qualified majority[113], and the legislation comes into force.

In the case of rejection, a Conciliation Committee formed by an equal number of members from the European Parliament and the Council of Ministers reviews the proposal. If the Conciliation Committee cannot come to an agreement in favor of the proposal, rejection by the European Parliament is confirmed and the proposal fails. If the Conciliation Committee reaches an agreement in favor then the European Parliament goes for a third reading. Following that, the proposal is voted on at the European Parliament, and the result of the voting determines the final decision of whether it is adopted or rejected.

In the case of amendment the European Commission reviews the suggestion, and accepts or rejects the amendment. Its decision goes to the Council of Ministers, which then adopts or rejects the legislation proposal. In the case of rejection a Conciliation Committee is formed comprising equal numbers of members from the European Parliament and the Council of Ministers. If the Conciliation Committee cannot come to an agreement in favor of the proposal, rejection by the Council of Ministers is confirmed and the proposal fails. If the Conciliation Committee reaches an agreement in favor, then the European Parliament goes for a third reading. Following that, the proposal is voted on at the European Parliament, and the result of the voting determines the final decision of whether it is adopted or rejected.

The Implementation of Legislation: The responsibility for the proper implementation of adopted legislation rests with the European Commission. As the guardian of the Treaties, it may sue a party (a government or a firm, for example) for breaches of the law. Cases of breaches and disputes are reviewed and resolved by the Court of Justice of the European Communities[114], in its lower tribune the Court of First Instance, or in national courts depending on the nature of the case. The key role of the Court of Justice of the European Communities is to ensure that all member countries, organizations and individuals comply with EU treaties and laws. It is the final arbiter in all kinds of disputes, and it has the power to fine a party that breaches the treaties and laws.

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[113] Most of the decisions in the Council of Ministers rest on qualified majority voting. Each member country is assigned a certain number of votes depending on its population. For a decision to be adopted it needs a minimum of 255 votes out of 345 (Council of the European Union 2007).

[114] The Court of Justice of the European Communities consists of 27 judges (one per member country), plus eight Advocates General who make a thorough examination of assigned cases and draft opinions for the judges (Court of Justice of the European Communities 2007a).

4.1.3 Lobbying EU Regulatory Organizations

Lobbying refers to efforts to influence the thinking of legislators or other public officials for or against a specific cause, or to get them to take a desired course of action (Columbia Encyclopedia 2007; TheFreeDictionary 2007). It is an attempt to influence policy-makers to adopt a course of action that is advantageous or not detrimental to a particular group or interest (Watson and Shackleton 2003, 90). It is carried out by individuals or pressure groups who present the concerns of special interest to the legislators and administrators.

Lobbying the regulatory organizations of the EU has increased considerably following the Single European Act of 1986 because enlargement and integration have increased both the range of authority of these organizations and the number of actors competing for the same resources (Molle 2001; Watson and Shackleton 2003). Organizations involved in lobbying EU regulatory organizations include firms, national and international trade associations, national and international industry associations, chambers of commerce, interest groups, law firms, political consultants, management consultants, and public-relations consultants (Jokinen 2000, 52).

There are two major channels through which to lobby EU regulatory organizations, namely the European route, i.e. direct influence or influence through European intermediaries, and the national route, i.e. the use of national intermediaries (Greenwood 1997). Car manufacturers use both routes in lobbying the European Commission and the European Parliament but the national route for lobbying the Council of Ministers since this organization is extremely difficult to access for lobbyists other than the home government (see Figure 16).

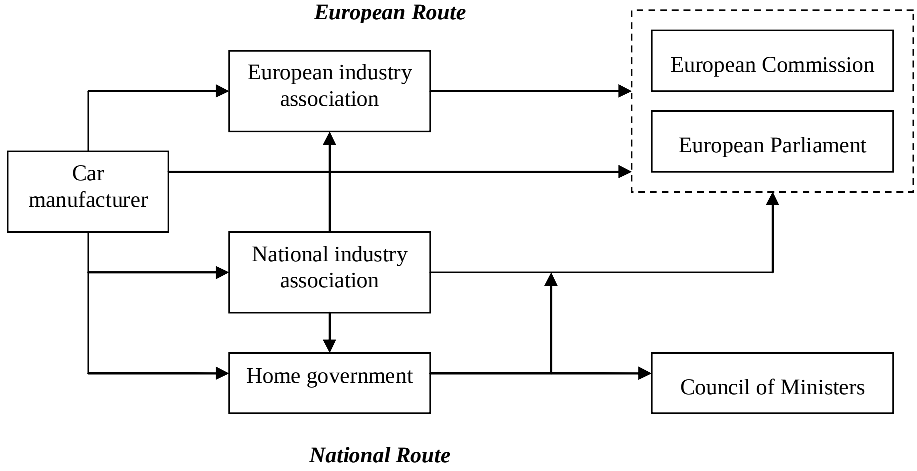

Figure 16. Lobbying routes to EU regulatory organizations (adapted from Greenwood 1997)

A key target for lobbying is the European Commission: it is the initiator of EU legislation, and it is at the early stages of initiatives that most influence can be exerted (Greenwood 1997). Officers in the European Commission are easily accessible given the aim to maintain as open and wide a dialogue as possible with all interested parties (Watson and Shackleton 2003). These officers benefit from this interaction because it provides them with detailed technical expertise and knowledge of industry-specific problems (Mazey and Richardson 1997). As a European Commission initiative, for example, the CARS 21 high-level group was set up on January 13, 2005 on the initiative of the EU Commissioner Günther Verheugen to provide recommendations about short- and long-term public policies and a regulatory framework for the sustainable development of a competitive European car industry. The group included members of the European Commission, representatives of member countries, members of the European Parliament, representatives of the car industry, as well as representatives of trade unions, nongovernmental organizations, and consumers (Commission of the European Communities 2006a). The establishment of this high-level group is evidence of the European Commission's intention to pursue an integrated approach combining the efforts of all stakeholders to achieve societal aims (Commission of the European Communities 2006a, 15). In accordance with this integrated approach, the CARS 21 high-level group recommends that all stakeholders should be involved at an early stage in the drafting of proposals (Commission of the European Communities 2006a, 19–20).

As Figure 16 shows, car manufacturers lobby the European Commission directly, via ACEA, the European car industry association which is located in Brussels and represents the interests of its members at the European level, via their national industry associations which also have their own offices in Brussels, and via their home governments.

The European Parliament and the Council of Ministers are also important targets for lobbying in that they are involved in the co-decision procedure. Lobbying these organizations is much more difficult, however, because once a proposal has left the European Commission the chances of exerting influence are reduced to reactive ‘fire fighting’ rather than seeking to shape the agenda before or during its emergence (Hull 1993). With increasing legislative power, members of the European Parliament in particular are increasingly subject to lobbying. The European Parliament has an open approach towards lobbyists in that it grants annual passes to outsiders who apply (Watson and Shackleton 2003). Car manufacturers lobby Members of the European Parliament directly, via ACEA, via their national industry associations, and via their home governments. The Council of Ministers is extremely difficult to access for lobbyists other than the home government, and therefore the national route is the only possible channel for lobbying this organization.

Representatives of various primary stakeholders such as trade unions, national and European supplier associations, national and European dealer associations, and consumer groups are sometimes able to lobby the EU regulatory organizations regarding some of the issues that concern them. As Figure 16 shows, however, the home government is the most influential primary stakeholder in terms of lobbying EU regulatory organizations.

Having reviewed the regulatory mechanism in the EU, I open next a section on two types of corporate governance, namely shareholder-oriented and stakeholder-oriented. This is because it may be relevant to understand them for better assessing the 13th EU directive event and also understanding how internal stakeholders like shareholders and employees can shape the firm. Understanding stakeholder-oriented corporate governance is of further relevance because the VW law event and the single market and VW event concern primary stakeholders of VW in Germany, a country with this type of corporate governance.

4.2 Shareholder-oriented vs. Stakeholder-oriented Corporate Governance

Corporate governance refers to the structure of relationships and the corresponding responsibilities within the firm among shareholders, Boards of

Directors, and managers (Davies 2006, 3). It is the mechanism through which firms are directed and controlled.

Financial markets are highly developed in shareholder-oriented Anglo-American corporate governance, and the ownership structures of firms are highly fragmented (Visentini 2006; Fliaster and Marr 2006). A substantial majority of the Board of Directors consists of independent directors who are representatives of principal shareholders. The Board of Directors elects, appraises, and plans the succession of executive management (e.g., the CEO); reviews and approves performance results, long-range plans, policies, and capital allocations; and provides advice and counsel to top management when needed (Monks and Minow 2004, 200). Individual stakeholders have little direct influence over management, and unsatisfied stakeholders end their contracts or sell their shares in the firm (Clarke and Bostock 1997).

Stakeholder-oriented German corporate governance is different in that it relies on the continuous monitoring of managers by primary stakeholders who have a long-term relationship with the firm (Clarke and Bostock 1997; Lane 2006). Employees, for example, are integrated into the governance mechanism by law. German firms with more than five hundred employees and all firms in the iron, steel, and mining industries (regardless of their size) must have two boards, the Management Board[115] and the Supervisory Board[116]. The Management Board runs the day-to-day operations of the firm. The Supervisory Board appoints, supervises, consults, and approves the decisions of the Management Board, and removes it if necessary (Schmid and Kretschmer 2004; Schmid et al. 2007). It has a significant influence on the firm because it decides the salaries of top management and elects the Chairman of the Management Board (ibid.).

According to the German codetermination law of 1976, half of the seats on the Supervisory Boards of all firms with more than two thousand employees and all firms in the iron, steel and mining industries (regardless of their size) must be filled by representatives of employees or the trade union (Thimm 1976; Aglietta and Reberioux 2005). The chairman of the Supervisory Board, whose vote counts double in the case of a tie, is elected by shareholders, however. The proportion of employee representatives falls to one-third in firms with less than two thousand but more than five hundred employees (Clarke and Bostock 1997; Aglietta and Reberioux 2005).

This two-tier system in Germany produces a compromise in management between shareholders and employees, and balances the pursuit of short-term profit with social-justice considerations and long-term strategic planning

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115 In German it is called the ‘Vorstand’.
116 In German it is called the ‘Aufsichtsrat’.

(Clarke and Bostock 1997; Aglietta and Reberioux 2005; Lane 2006). There are different opinions about codetermination. It is cited as a major reason for Germany's post-war economic success due to its aligning of the commitments of employees, managers, and shareholders (Clarke and Bostock 1997; Volkswagen 2007), but it is also criticized for being rigid in that it makes it difficult for firms to take decisions quickly enough (Hahn 2005).

Banks have also been powerful players in the German corporate governance system because the financial system has historically been founded on bank credit, and the stock market has not been fully developed (Lane 2006). Until 1998 banks were not only lenders but also major shareholders in firms because they had the right to vote for shares of private and corporate investors that had deposited their shares in banks (Clarke and Bostock 1997). This gave them a high degree of power at general shareholders' meetings. The power of the banks declined under the Corporate Sector Supervision and Transparency Act of 1998 and the Corporate Governance Code of 2002, which limited their exercising of voting rights (Monks and Minow 2004, 332; Knudsen 2005, 510).

After this review of the two corporate governance systems, I will turn next to the EU car industry and discuss it from a historical perspective.

4.3 Developments in the EU Car Industry, 1960–2005

The EU car industry is mature with a history of over 115 years. Indeed, the first car in the world to carry the architecture of the modern motor car was built in Europe by the French manufacturers René Panhard and Émile Levassor in 1891 (Citroënët 2007). Since they did not standardize their cars, however, the Benz Velo, manufactured by Karl Benz in Germany in 1894, entered the automotive history books as the first large-scale production car in the world (Mercedes-Benz USA 2007).

After World War II the USA was the leader in car manufacturing, followed by the UK, Germany, France, and Italy. GM and Ford were the largest manufacturers worldwide, and they already had manufacturing facilities in Europe. By 1960 there were 47 car manufacturers with manufacturing facilities within the current borders of the EU-27 (see Table 1 in Appendix 2). Of these, 17 were British, nine were German, eight were Italian, six were French, two were American, two were Swedish, two were Czechoslovakian, and one was Spanish (see Table 2 in Appendix 2). The following paragraphs review key developments in the EU car industry from 1960 until 2005 by decade (see Table 3 in Appendix 2 for a summary).

The baby-boom decade of the 1960s could be characterized as the decade of economic recovery for Continental Europe, and of growth for car manufacturers. However, it was not so glorious for all manufacturers, especially the British ones. Bowden and Turner (1998) argue that the turning down of the UK application to join the EEC in 1963 had a high cost for the UK car industry. The EEC provided growth opportunities in Europe for German, French, and Italian car manufacturers, of which British manufacturers were deprived. Growth is necessary in the car industry in order to achieve economies of scale because of the high need for investment. Since the British manufacturers could not achieve growth through internationalization, they responded by merging among themselves. Jaguar merged with the British Motor Company (BMC) in 1966 (Car Directory 2006a), the Leyland Motor Company acquired Rover in 1967 (Car Directory 2006b), and BMC and the Leyland Motor Company merged in 1968 to form the British Leyland Motor Company (BLMC) (Car Directory 2006a). There was consolidation at the national level in Italy, Germany and France as well, although not of such magnitude as in the UK. In Italy, Fiat acquired control of Autobianchi in 1967 and of Ferrari and Lancia in 1969 (Car Directory 2006c; Fiat 2006). In Germany, VW acquired Auto Union from Daimler Benz in 1965 and Neckarsulm (NSU) Motorenwerke in 1969 (Volkswagen 2003), and Bayerische Motoren Werke AG (BMW) acquired Glas in 1966 (BMW 2006; Car Directory 2006d). The French manufacturer Citroën acquired Panhard in 1965 and Maserati in 1968 (Car Directory 2006e). An important event in the 1960s was the entry of Chrysler, the third largest American manufacturer, into the European market in 1966 via its acquisition of Simca in France and the Rootes Group in the UK (Car Directory 2006f). As a result of such acquisitions the number of car manufacturers dropped from 47 in 1960 to 39 in 1970 (see Table 2 in Appendix 2).

European economies suffered the negative impacts of two oil crises in the 1970s, one in 1973 following the Arab-Israeli war and the other in 1979 following the change of regime in Iran. Being highly dependent on general economic conditions, the car industry also felt the effects of these economic crises. The UK industry, the second largest in the world in the 1950s, collapsed as BLMC, the largest British manufacturer, went bankrupt and was nationalized in 1975 (Bowden and Turner 1998). Even the entry of the UK into the EEC in 1973 was not of much help because all European economies were in trouble. In France, Citroën went bankrupt and was acquired, according to a directive of the French government, by Peugeot in 1975 (Car Directory 2006e; PSA Peugeot Citroën 2006). The Italian company Fiat acquired Abarth in 1971 (Car Directory 2006c; Fiat 2006), and Lamborghini went bankrupt in 1978 (Car Directory 2006g). Chrysler, the third largest American manufacturer, was in crisis and abandoned its European operations in 1978 (Car Directory 2006f). Subsidies were provided by home governments to save their national champions from bankruptcy (e.g., the UK government to BL, the Italian government to Fiat, and the French government to Renault), and by the end of the decade the number of car manufacturers fell further to 31. The oil crises increased demand for economical models. Car manufacturers responded to the changing consumer demands by developing fuel-economy technologies such as diesel engines and the fifth gear. This development benefited Japanese manufacturers in particular, which increased their total market share by 1980 to 10 percent in Western Europe[117] (Volkswagen 2003, 110).

The car industry responded immediately to initiatives towards market integration and enlargement in the EEC during the 1980s. Starting from the beginning of the decade, Spain grew to be a major manufacturing location for low-cost mini and medium-sized cars due to its skilled low-cost labor force. Cross-border acquisitions accelerated after 1985. In 1986 VW acquired 51 percent of SEAT in Spain (Volkswagen 1987) and GM acquired Lotus in the UK (Car Directory 2006h; General Motors 2006). Ford acquired AC Cars and 75 percent of Aston Martin in 1987 and Jaguar in 1989 (Brinkley 2003; Car Directory 2006i; Ford 2006). Finally, GM acquired 50 percent of Svenska Aeroplan Aktiebolaget (SAAB) also in 1990 (Car Directory 2006j; General Motors 2006). The decade also saw newcomers entering the market. Two French manufacturers, Aixam Mega and Microcar, were established in 1983 and 1984 respectively to produce micro cars for an emerging market segment (Aixam 2006; Microcar 2006), and Chrysler, having recovered from its crisis, reentered the European market by acquiring the Lamborghini brand in 1987 (Car Directory 2006f). As a result of these entries, the number of car manufacturers remained at 31 between 1980 and 1990.

Two trends in the industry in the 1980s were increasing automation and the spreading of the Japanese lean-manufacturing system to replace the mass-production system of Ford. The degree of automation increased with the usage of computerized numeric control systems and robots. The success of the Japanese car manufacturers was attributed to their lean-manufacturing system (Womack et al. 1991), which gave more responsibility to employees and aimed at zero defects via proactive quality control, and zero inventories with just-in-time production that required synchronization with suppliers.

The EU car industry entered the 1990s in the midst of one of the severest economic crises in its history. Car sales in Western Europe dropped from

[117] Japanese manufacturers supplied European markets in the 1970s via exports from Japan. Japanese car exports to European markets were restricted by national quotas, which were as low as three percent of the car market in France, one percent in Spain, two percent in Italy, 14 percent in Portugal, and 15 percent in West Germany (Drei 1995).

13,498,072 units in 1992 to 11,252,494 units in 1993 (ACEA 2006). In the meantime, under the single market program a number of measures towards market integration have been implemented in the EU. Some of these have affected the car industry directly (i.e. industry-specific measures) (see Table 4 in Appendix 2), whereas others have been more general and have had indirect effects (i.e. horizontal measures).

A key industry-specific development was the replacement of national quotas for Japanese exports with an EU-wide quota. As part of the General Agreement on Tariffs and Trade, the European Commission and the Japanese Ministry of Trade and Industry signed the “elements of consensus” on Japanese motor vehicle exports in July 1991. This replaced the national quotas with an EU-wide quota for a transition period until December 31, 1999, and stipulated its abolishment after that.

Another key industry-specific development was the completion of the harmonization efforts concerning technical standards for vehicles. As a result, technical approval was standardized under the “European whole vehicle type approval program” (Council of the European Communities 1992a)[118]. This program came into force after January 1, 1998 and allowed the approval of a new car in the EU following its approval in one of the member countries. This was a major step in that car manufacturers were no longer forced to obtain separate approvals in member countries. Furthermore, the weights and dimensions of cars were also standardized (Council of the European Communities 1992b), and community-wide measures were set to limit the levels of pollutants from vehicles (Council of the European Communities 1991; European Parliament and the Council of the European Union 1994).

Responding to environmental concerns, the End-of-Life Vehicle Directive, which was adopted on September 18, 2000, aimed to increase levels of vehicle recovery (i.e. the reuse of materials from scrap vehicles) and to achieve a reduction in the use of hazardous substances in their manufacture (European Parliament and the Council of the European Union 2000).

The harmonization of taxes has been the most difficult objective to achieve. Despite the reduction in the differences between value-added tax rates, differences in sales taxes continue to exist (Commission of the European Communities 2006b).

A further industry-specific development was the introduction of a new block exemption regulation in 2002, the aim of which was to change the

[118] Efforts towards harmonization of technical standards were initiated in 1970 (cf. Council of the European Communities 1970).

structure of distribution and repair & maintenance networks in the EU (Commission of the European Communities 2002a)[119].

Horizontal measures affecting the car industry included the removal of borders among member countries as of January 1, 1993 (facilitating the free movement of goods and labor), and the restricting of national governments from bringing in measures that could disturb competition. The European Commission also intended to foster the free movement of capital by preparing a takeover directive aimed at easing hostile takeover attempts[120].

Increasing market integration led to the following major changes in the EU car industry after 1990.

First of all, Japanese car manufacturers could not take the risk of being left out of the EU (Egan and McKiernan 1993) and responded by increasing FDI in the region. Major Japanese FDI in the EU include the assembly plants of Nissan in the UK (1986), Mitsubishi Motors in Holland (1991), Toyota in the UK (1992), France (2001) and the Czech Republic (2005), Honda in the UK (1992), and Suzuki in Hungary (1993) (Japanese Automobile Manufacturers Association 2007).

Secondly, the Korean manufacturers Hyundai and Daewoo entered the attractive EU market with exports. Korean brands increased their market shares from 0.1 percent in 1990 to 3.8 percent in 2005 (ACEA 2006)[121]. As a result, competition in the EU intensified.

Thirdly, consolidation among car manufacturers in the EU intensified, the numbers decreasing from 31 in 1990 to 21 in 2005. VW acquired Skoda in 1991, and Bentley, Bugatti, and Lamborghini in 1998 (Volkswagen 2003). BMW acquired Rover in 1994, and Rolls Royce in 1998 (BMW 2006; Car Directory 2006d). Daimler Benz merged with Chrysler in 1998 to form DaimlerChrysler (Car Directory 2006f; DaimlerChrysler 2006). In 1999 Ford acquired Volvo (Brinkley 2003; Car Directory 2006i; Ford 2006), Renault acquired Dacia (Car Directory 2006k; Renault 2006), and in 2000 GM acquired the remaining 50 percent of SAAB (Car Directory 2006j; General Motors 2006).

Fourthly, car manufacturers also increased cooperation among themselves. Renault and Nissan formed an alliance in 1999 (Car Directory 2006k; Renault 2006), followed in 2000 by the alliances between GM and Fiat (Car Directory 2006c; General Motors 2006). The latter did not work out, however, and was dissolved in 2005 (ibid.).

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[119] See section 5.5 for an analysis of this event.

[120] See section 5.4 for an analysis of this event.

[121] Hyundai established a manufacturing facility in the Czech Republic in 2006 (Czech Republic 2006).

Fifthly, increasing competition caused car manufacturers to move towards international manufacturing and sourcing (Pries 2005). In the EU, the new member countries the Czech Republic, Poland, Slovakia and Hungary were attractive production locations due to their qualified low-cost labor forces. The internationalization of production also affected the business model in the supply chains, creating a three-tiered structure, and first-tier suppliers followed the manufacturers to new international production sites (Kinkel and Lay 2005). Thus, market integration in the EU increased competition among car manufacturers, and this spilled over to the suppliers. As a result, there was drastic consolidation among automotive suppliers in the 1990s, which has been continuing in the 2000s (Kappelhoff 2005)[122].

Finally, BER 1400/2002 has also increased competition among dealers leading to consolidation in the distribution networks (Weimer 2006; Akpinar 2007)[123].

These observations about suppliers and dealers support the relevance of this study in that it seems that market integration in the EU affected the weaker actors in the car industry more severely. These weaker actors also include some of the manufacturers' primary stakeholders, such as suppliers and dealers.

4.4 The State of the EU Car Industry as of 2005

In sum, consolidation in the EU car industry reduced the number of manufacturers from 47 in 1960 to 21 in 2005 (see Table 2 in Appendix 2). The most severely hit were the British (a net loss of 13 manufacturers) and the Italians (a net loss of seven). Fiat, the only Italian survivor, is looking back longingly to its glory days of 1973 when it was the market leader in Western Europe (see Table 5 in Appendix 2). Likewise, Sweden, Spain and the Czech Republic have all lost their national champions (see Table 2 in Appendix 2).

Increasing competition hit car manufacturers with relatively smaller market shares (e.g., Saab, SEAT, Skoda, and Volvo) and niche manufacturers (e.g., Alfa Romeo, Ferrari, Jaguar, and Lamborghini). Otherwise, the market-share concentration in the industry remained relatively stable between 1973 and 2005 despite some major shifts: the total market share of the top five increased only from 58.0 percent in 1973 to 63.9 percent in 2005 (see Table 5 in Appendix 2). Of those with high shares, the losers were Rover and Fiat:

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[122] See sub-section 4.6.1 for further discussion on changes in supply networks of the EU car industry.

[123] See sub-section 4.6.1 and section 5.5 for further discussion on changes in distribution networks of the EU car industry.

Rover, the UK manufacturer, saw a decrease from nine percent in 1973 to 2.7 percent in 1994 when it was acquired by BMW, and likewise, Fiat, the market leader in Western Europe in 1973 with 14.9 percent of the market, saw its share go down to 6.6 percent in 2005. The winners, in turn, were VW, Japanese manufacturers, Korean manufacturers, BMW, Daimler Benz, and PSA, while Ford, GM and Renault maintained their relative percentages (see Table 5 in Appendix 2).

In terms of consumption in 2005, Germany (22.9 percent of new car registrations in the EU-15 plus Norway and Switzerland), the UK (16.8 percent), Italy (15.4 percent), France (14.3 percent), and Spain (10.6 percent) were the largest markets in the EU (see Table 6 in Appendix 2). Cars are manufactured in 17 countries in the EU-27 (see Table 7 in Appendix 2), but not surprisingly, the above five countries were also the countries in which the manufacturing is concentrated accounting for 82 percent of total manufacturing in 2004: Germany (31 percent), France (20 percent), Spain (16 percent), the UK (10 percent), and Italy (five percent) (see Table 8 in Appendix 2).

As of 2005 The EU car industry had an oligopoly structure carrying some of the world's largest MNEs. 21 manufacturers were producing cars in the EU. Of these, the four UK firms (Bristol Cars, Caterham Cars, Morgan Motor and TVR), the two French manufacturers of micro cars (Aixam-Mega and Microcar), and the Czech manufacturer of sports cars (MTX), all specialized manufacturers or niche players, together shared less than one percent of the EU market. The remaining 14 were larger players manufacturing cars in between two and eight different segments (see Table 9 in Appendix 2). VW was the market leader with an 18.9 percent market share, followed by PSA (13.7 percent), Ford (10.9 percent), GM (10.6 percent), Renault (9.8 percent), Fiat (6.6 percent), DaimlerChrysler (6.2 percent), BMW (5.3 percent), and Toyota (5.3 percent) (see Table 6 in Appendix 2). European manufacturers (e.g., VW, PSA, Renault, and Fiat) have lost considerable market shares in their home country markets between 1960 and 2005 due to increasing competition (cf. Molle 2001, 263)[124].

Adapting the classification scheme used by the European New Car Assessment Programme I looked into the product positioning of some of the car manufacturers in the EU. The analysis shows which ones are strong in the various size classes, and who the key competitors are (see Table 9 in Appendix 2).

Car manufacturers in the EU have also diversified into other strategic business areas. According to their 2004 annual reports, the percentage of

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124 They were still the market leaders in their home markets in 2005 (see Table 6 in Appendix 2).

revenue earned from the car business unit of the total revenues was 62 on average but varied from 45 (Fiat) to 91 (Porsche) (see Table 10 in Appendix 2). Financial services are a key related strategic business area in which all of the manufacturers operate. Other business areas include light commercial vehicles, trucks, component supply, motorcycles, and buses and coaches (see Table 10 in Appendix 2).

Car manufacturers are powerful actors in their market environments, due in part to the fact that they control key resources along the value chain (product-development technologies and marketing know-how, for example) and have easier access to financial resources (some even have their own banks). The differential in power is also evident in their relative size in comparison to suppliers and dealers.

In the following two sections I focus on primary stakeholders and elaborate on their relationships with car manufacturers in the light of industry characteristics.

4.5 Primary Stakeholders in Review

The primary stakeholders included in this research include shareholders, employees, customers, suppliers, dealers, creditors, and the home government. Table 10 summarizes the inputs made by these primary stakeholders and the compensation received in return.

Table 10. The inputs and compensation of primary stakeholders (adapted from Ahlstedt and Jahnukainen 1971)

Primary stakeholder	Input	Compensation
Shareholders	Capital, business idea	Dividends, appreciation of firm value
Employees	Labor, knowledge	Salaries, wages, benefits
Customers	Money	Products, resources, technology
Suppliers	Raw materials, intermediate goods, services, equipment	Revenues
Dealers	Sales services, repair & maintenance services	Revenues
Creditors	Loans	Interest
Home government	Infrastructure, reduction of uncertainty, investment incentives	Taxes, increase in societal welfare

Shareholders are owners of the firm. It may be worth distinguishing between principal shareholders and minority shareholders in publicly traded firms. Principal shareholders are the real owners of the business as they have either started it themselves or have acquired it with the intention of continuing it. They hold considerable percentages of shares with voting power, and their stakes are long-term in that they are usually committed to the business. Minority shareholders are in general short-term investors who invest capital in order to earn financial returns. Their investments in the firm are usually part of a larger portfolio. Principal shareholders input capital and the initial business idea, while minority shareholders only input capital. Both types of shareholders receive compensation in terms of dividends and appreciation of the market value of the firm. Dividends are calculated from the firm's annual profits and are distributed once a year. Appreciation of the firm's market value is realized only when shareholders decide to sell their shares. Shareholders meet once a year at the general shareholders' meeting. They approve the annual operating results and appoint a new Board of Directors, or extend the term of the existing Board.

Employees work for the firm and include both manufacturing and administrative personnel. They input labor and knowledge and receive as compensation wages or salaries. Having a job and a regular monthly salary provides status and security in a person's life. Some firms offer their employees fringe benefits such as housing allowances, pension schemes, or stock-option plans. Employees usually belong to a trade union. The unions represent employees in collective wage and salary discussions. In the case of a lack of reconciliation between the management representatives and the union representatives, employees have the right to go on strike. Germany, the home country of the focus firm VW, has work councils[125] inside firms dealing with the daily problems of employees and protecting employee rights at the work place. German employees are further empowered through representation on the Supervisory Board.

Customers are buyers of a firm's products. For a car manufacturer they may be end-users (individuals or firms buying company cars) or corporate customers (i.e. business-to-business customers such as other car manufacturers purchasing technology, resources, or intermediate products). End-users are revenue generators for car manufacturers during the lifetime of the vehicle as it is estimated that after-sales services account for 40 percent of the total costs of owning a car (Ealey and Troyano-Bermudez 1996). Customers input money (i.e. revenue for the firm) and receive products and resources. In that respect they are different from all other primary stakeholders in that their inputs are sources of compensation for the firm and all the other primary stakeholders.

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[125] 'Betriebsrat' in German. The works council has two faces in Germany: by law, it is the counter-party of the employer, and as representative of the employees, it is closely integrated into the daily management processes in terms of safeguarding the jobs and the working conditions of employees as well as managing employer-employee relationships (Andresen 2005).

Suppliers provide raw materials, intermediate goods, machines, equipment, and services, and in return they receive sales contracts and subsequent sales revenue. According to this broad definition, a car manufacturer's suppliers may be various and numerous, and could include an advertising agency preparing an advertising campaign or a reinsurance firm providing reinsurance services. The focus of this research is more on suppliers of components, modules, and systems since they constitute the bulk of supplier organizations.

The distribution and after-sales-service networks of a car manufacturer include a variety of primary stakeholders such as general importers, distributors, dealers, and sub-dealers. For the sake of simplicity I will focus on dealers (including sub-dealers) since they constitute the majority of this group of actors in terms of numbers. They provide customers with sales and repair & maintenance services, and also intermediate financing and insurance services, on behalf of car manufacturers, creditors, and insurance firms.

Creditors input loans to the firm and receive interest as compensation. They are key primary stakeholders for car manufacturers because financing is highly necessary in the investment-intensive car industry. As a result, most manufacturers operate in the financial-services strategic business area, and some (e.g., VW) have their own banks. Car manufacturers obtain outside financing mainly through banks or by issuing bonds in financial markets.

Finally, home governments have traditionally been influential primary stakeholders due to their ability to rely on legitimate control over the means of coercion (Streeck and Schmitter 1985; Hamilton 1994) and thus to exercise authority over other organizations (Lindblom 1977). Whereas Porter (1980) argues that home governments may affect the industry structure through their effects on market forces, Rugman and Verbeke (2000) suggest that government regulations may have an immediate impact on the firm and should thus be treated as a separate force. The powers of home governments in the EU are diminishing due to the empowering of supranational organizations (Mercado et al. 2001; Buckley and Ghauri 2004). Home governments are hidden shareholders due to taxation on corporate profit. They also receive compensation from all other primary stakeholders in the system. Since they seek the welfare of their societies, they benefit further when their societies benefit from the existence of the firm. Home government inputs may be in the form of providing infrastructure, the reduction of uncertainty through regulations, and the provision of investment incentives. Infrastructure is especially important to the car industry because it needs good quality roads for transport purposes (cf. Cleff, Heneric, and Spielkamp 2005).

4.6 Analysis of Car Manufacturer-Primary Stakeholder Relationships in the Light of Industry Characteristics

The key characteristics of the car industry that may significantly affect the nature of relationships between car manufacturers and their primary stakeholders are the nature of the product, labor intensity, and investment intensity. I describe each characteristic in more detail below.

4.6.1 The Nature of the Product

I focus in the following paragraphs on three attributes of the car and their impacts on relationships between car manufacturers and primary stakeholders.

Attribute 1: The car is a durable product requiring the second biggest cash outlay in the family budget after the purchasing of a house (Sloan 1990; Rhys 2004). As such, creditors are influential primary stakeholders in terms of providing financing to customers and thus promoting car sales. This attribute also makes demand very much dependent on the general economic level in a country market (Sloan 1990; Rhys 2004). Downturns in the economic environment affect customer behavior in that they can delay their decisions on car renewal. As Iacocca and Novak (1984, 286) phrase it, "fuel is the blood of the car industry, and interest rates are the oxygen". Low fuel prices and interest rates contribute to higher car sales. Perhaps a third element affecting sales is tax. In that respect home governments are also influential primary stakeholders in that they can shape conditions in the system through adjusting taxes and interest rates[126].

Attribute 2: The car is a complex product made up of more than 10,000 components (Womack et al. 1991). There is no other product on earth that incorporates so many materials, processes, and technologies in its creation (Keller 1993, 2). As a result, car production necessitates the coordination of up to 1,000–1,500 suppliers per model (Womack et al. 1991). A consequence of having so many components and thus so many suppliers is that the industry is traditionally buyer-dominated, and suppliers are highly dependent on manufacturers (Mercer et al. 2004; Akpinar and Zettinig 2008a).

The European component market is the largest in the world, with 1,500 major and 10,000 minor suppliers grouped around their home-country car manufacturers (Womack et al. 1991). The supply industry has a tiered structure (cf. Heneric et al. 2005). First-tier suppliers supply the manufacturers

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126 In the EU, the abilities of home governments to adjust interest rates are limited as this is under the responsibility of the European Central Bank.

directly. They are also called system integrators if the product they supply is a module or a system[127]. Second-tier suppliers produce value-adding parts in the minor sub-assembly phase, and supply first-tier suppliers. Finally, third-tier suppliers supply second-tier suppliers with engineered materials and special services such as rolls of sheet steel, bars and heat treating, and surface treatments.

The structure of supplier networks in the EU car industry has been changing since the beginning of the 1990s in that first-tier suppliers have been taking over value-chain activities in both design and manufacturing that used to be carried out by the manufacturers (Lamming 1993; Lilliecreutz 1998; Ebel et al. 2004; Heneric et al. 2005). Two key reasons for this type of vertical backward disintegration from the car manufacturers' point of view are that in this way they can relieve themselves of some of the investment load (Rhys 2004), and suppliers are able to perform the same operations with lower labor costs (Williams et al. 1994).

Globally operating manufacturers demand globally operating first-tier suppliers that can finance their assembly plants all over the world (Heneric et al. 2005, 30). Thus, the trend is towards global sourcing, systems sourcing, and single sourcing (Pfaffmann and Stephan 2001), thereby creating fewer suppliers with enhanced competences (Lilliecreutz 1998; Akpinar and Zettinig 2008b).

There is also a trend towards forging partnerships between car manufacturers and their first-tier suppliers. Especially since the crisis in 1993, European and American manufacturers have been moving from the traditional model of adversarial relationships with suppliers towards the Japanese model of long-term partnership sourcing (Shook 1988; Frey and Schlosser 1993; Hyun 1994; Helper and Sako 1995; Leverick and Cooper 1998). Consequently, car manufacturers are requesting their first-tier suppliers to make site-specific and relationship-specific investments (Backhaus and Bueschken 1999; Rugman and Collinson 2004). This challenge, together with that of increased product responsibility and demand for innovations, resulted in increasing internationalization and consolidation of the supply industry via mergers and acquisitions in the 1990s (Cleff, Licht, Spielkamp, and Urban 2005; Kappelhoff 2005). Car manufacturers are expected to outsource more of their previously in-house activities and related R&D to suppliers, and this may result in further consolidation in their supply chains (German Association of the Automotive Industry 2001).

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[127] A module is a physical subassembly, such as a seat or a dashboard, whereas a system is a functional aggregate of components, such as the brake system (Collins et al. 1997).

Despite the trend towards partnership, there is also increasing cost and price pressure from car manufacturers on suppliers (Roth 2006). This cost pressure further threatens the existence of suppliers on all tiers because most of them are small and medium-sized enterprises (SMEs) that are challenged by increases in raw-material prices (e.g., the prices of steel, aluminum, oil, plastics, and ores have risen considerably over the last four years) and volatility in demand (German Association of the Automotive Industry 2007).

Attribute 3: The car requires maintenance at regular intervals for reasons of public safety (Sloan 1990). It is not like any other product that customers buy 'off the shelf' everyday (ibid., 281). It is a 'unique' complex high-tech product that at regular intervals requires repair & maintenance by trained specialists for reasons of public safety[128] (ACEA and CECRA 2000).

For this reason, distribution and repair & maintenance activities in the EU car industry were highly protected until 2002 by block exemption regulations (cf. Commission of the European Communities 1995), and manufacturers have tried to retain control over their distribution and after-sales networks[129]. Under this protective regime, dealers were allowed to market cars only within territories allocated by the manufacturers, and parallel trade across country borders was not allowed. Dealers were also obliged to use only original spare parts in carrying out repair & maintenance activities. They also had to have separate showrooms for each car brand they sold. These conditions gave manufacturers extensive control over the quality of both the after-sales services offered and the spare parts used (Weimer 2006; Akpinar 2007).

As a result, the EU car industry has traditionally had a fragmented distribution system[130] (Vickerman 1992), meaning that most dealers are SMEs that are highly dependent on the manufacturers. A further consequence of the protective regime was that the building of a dealer network was a major barrier to entry (especially for Japanese and Korean manufacturers) in country markets with national manufacturers such as Germany, France, and Italy (cf. Toyota Motor Corporation 1988).

[128] As a minimum requirement, EU countries stipulate the official testing of cars at certain intervals. Certification to operate in traffic depends on the fulfillment of technical criteria concerning public safety and the environment.

[129] Each car manufacturer had its own dealer network, although Finland was an exception. As I was informed by Mr. Rantala, following the economic crisis in the first half of the 1990s many Finnish dealers went bankrupt. Consequently, the car manufacturers allowed them to pursue multiple branding in the same showroom.

[130] The distribution system comprises general importers for each country market (in some countries the car manufacturer undertakes this role itself), distributors acting as regional wholesalers in a country market, and dealers and sub-dealers acting as retailers. As of the year 2000, there were a total of 512 distributors and 120,000 dealers in the EU (Andersen 2001).

The BER 1400/2002 was meant to change this kind of relationship between car manufacturers and their dealers[131].

4.6.2 Labor Intensity

A further significant characteristic of the car industry is that it is labor-intensive: in 2002, including the supply industry, it employed 2.13 million people in the EU-25, accounting for between six and seven percent of total manufacturing employment (Commission of the European Communities 2004; Commission of the European Communities 2006a). Given its close links with other industries, it is an engine for growth and employment (Heneric et al. 2005, 11). Car manufacturers are among the largest firms in the world in terms of employment: there were four in the top ten of the Fortune Global 500 list in 2005 (CNNMoney 2006). DaimlerChrysler had the largest workforce with 384,723 employees (see Table 11 of Appendix 2). These statistics clearly show the importance of car manufacturers to employees and home governments[132].

As a consequence, there is continuous power play between car manufacturers and governments regarding production-location decisions (Stopford and Strange 1992; Studer-Noguez 2001). The influence of home governments is particularly obvious in that, on average, a significant proportion of the total production (ca. 52 percent) is carried out in their home countries (see Table 11 of Appendix 2). On the other hand, manufacturers are also moving from a pure export orientation toward regional production, for two reasons. The first reason is that lean production, the Japanese manufacturing management technique that has overtaken the mass-production management technique of Ford, favors FDI because it achieves highest efficiency, quality, and flexibility when all activities from design to assembly occur as close to the customers as possible (Womack et al. 1991, 200). The second reason is that export orientation carries the risk of fluctuations in exchange rates between the US Dollar, the Euro, and the Japanese Yen because costs and revenues are realized in different currencies. Knowing that price is a key determinant of demand (Rhys 2004), exporting manufacturers can easily become uncompetitive in world markets if the exchange rates change to their disadvantage.

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131 See section 5.5.

132 In developing countries it is commonly understood that one of the first steps to economic growth is the establishment of a car industry (Keller 1993).

Labor is a significant cost item in the car industry (cf. Cleff, Licht, Spielkamp, and Urban 2005). This represents a competitive threat for manufacturers competing in mini and medium-sized segments and manufacturing in Western Europe where labor costs are high and productivity levels are not high enough to compensate[133]. As the labor content does not increase proportionally with car size, mini and medium-sized models are relatively more vulnerable to high labor costs. In the EU, the average labor cost per hour in 2002 was €27.25 in Germany, €13.63 in Spain, €5.39 in the Czech Republic, €5.27 in Poland, €4.91 in Hungary, and €3.59 in Slovakia (Eurostat 2005, 169). The trend in the EU is for manufacturers to shift the manufacturing of their mini and medium-sized cars to countries in which labor costs are low: Spain became a popular host country in the 1980s. Based on the 2004 production figures, I compiled a map of EU car manufacturing by manufacturer and country (see Table 8 in Appendix 2). Spain accounted for 16 percent of total EU car production: VW (having acquired SEAT, the national manufacturer), Peugeot Société Anonyme Peugeot Citroën (PSA), Ford, Renault, and GM manufacture a significant number of their mini and medium-sized cars in Spain (cf. International Organization of Motor Vehicle Manufacturers 2007). The current popular host countries in the EU are Central and Eastern European countries such as Poland, the Czech Republic, Slovakia, Slovenia, Hungary and Romania, and the candidate country Turkey. The labor-productivity levels in some of these countries (e.g., Slovakia and Hungary) have already reached the EU-15 average (cf. Cleff, Licht, Spielkamp, and Urban 2005). Fiat is sourcing its mini cars from Poland and also manufacturing in Turkey; Toyota and PSA are jointly producing their mini cars in the Czech Republic; VW has production facilities in the Czech Republic, Slovakia, Poland, and Hungary; other manufacturers in the region include GM in Poland; Renault in Slovenia, Turkey and Romania (having acquired Dacia); Suzuki in Hungary; and Toyota, Ford and Honda in Turkey (cf. International Organization of Motor Vehicle Manufacturers 2007). Between 1995 and 2002 some of these countries achieved impressive annual growth in output (e.g., 28 percent in Slovakia, 25 percent in Hungary, and 20 percent in the Czech Republic) (Heneric et al. 2005, 16). Further manufacturing investments under construction in the region include a 300,000-a-year PSA plant in Slovakia (PSA Peugeot Citroën 2005a), and a 300,000-a-year Hyundai plant in the Czech Republic (Czech Republic 2006). These

[133] The EU-15 has a significant labor-productivity gap compared to the USA and Japan due to low working hours per employee. In the year 2001 the annual working hours per employee averaged 1,583 in the EU-15 compared to 2,032 hours in the USA and 2,023 in Japan (Cleff, Licht, Spielkamp, and Urban 2005, 112). Hence, labor productivity corresponded only to ca. 75 percent of that in the USA and Japan (Cleff, Licht, Spielkamp, and Urban 2005, 114).

additional capacities are likely to stimulate competition in the EU between different production locations (Heneric et al. 2005) because foreign car manufacturers are investing in Eastern Europe mainly in order to supply the EU-15 market, and particularly Germany (Licht et al. 2005)[134].

4.6.3 Investment Intensity

Cars could be regarded as high-tech products as the total proportion of electrical and electronic parts has increased to 50 percent (Ebel et al. 2004; Pries 2005; Roth 2006). Investment and innovation are the engines of economic development (cf. Schumpeter 1951). In the car industry, whereas productivity and labor costs are the drivers of competitiveness in the short-run, the ability to innovate and the capacity to invest in R&D are crucial determinants of long-term competitiveness (Cleff, Licht, Spielkamp, and Urban 2005; Pries 2006). The future of the European industry lies in innovation rather than price competition (Roth 2006). Some of the technologies to be utilized in cars in the future include brake-by-wire, steer-by-wire, navigation, and active sensor systems[135] (cf. Wallentowitz et al. 2004; Meissner and Jürgens 2006). This drive for new technologies is also highlighted by manufacturers in their annual reports. Toyota, for example, claims with its motto: “Today, Tomorrow, Toyota” that it is positioned for the future, and maintains that the only possible way it can control its own destiny is through far-sighted innovation in all of its operational areas (Toyota 2005). Similarly, BMW uses the logo “The Ultimate Driving Machine” to emphasize its competitiveness in technology and design (BMW 2005; Kiley 2004).

According to my calculations from the annual reports of car manufacturers, the average R&D costs in the car industry in 2004 accounted, on average, for 4.3 percent of revenues (see Table 12 in Appendix 2). The reasons for R&D investments include the development of future technologies, the introduction of new models, the reduction of overall unit costs, achieving flexibility in production, and improving the quality of working life (Rhys et al. 1993). The car industry is a major driver of new technologies: almost 20 percent of all manufacturing R&D in the EU is undertaken by car manufacturers

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134 In 2002, exports to the EU-15 constituted 80 percent of all car exports from Eastern Europe (Licht et al. 2005, 58).

135 The brake-by-wire system aims to replace the brake pedal with an electrical mechanism and thus to shorten response times. Similarly, the steer-by-wire system aims to replace the steering wheel, which jeopardizes the driver’s safety in case of an accident. Navigation systems are already in use and make point-to-point travel easier when the route is unknown to the driver. Active sensor systems aim to increase travel safety and comfort by decreasing the need for continuous judgment and interference on the part of the driver.

(Commission of the European Communities 2004). The European industry is spending about €19 billion per year on research under the platform provided by the European Council for Automotive Research and Development, which a number of manufacturers established in 1994 (ACEA 2007).

The industry is investment-intensive not only in terms of R&D, but also in terms of property, plant & equipment (PP&E). According to my calculations from the annual reports of car manufacturers, the average investments in PP&E in 2004 accounted, on average, for four percent of revenues (see Table 13 in Appendix 2), mainly related to greenfield investments, the introduction of new models, the upgrading of technology, and the expansion of capacity.

The need to innovate on the one hand and to invest in PP&E on the other creates barriers to entry into the industry (cf. Porter 1980) and necessitates economies of scale. Rhys (2004) estimates that the minimum efficient number for full-scale (i.e. manufacturing cars in all segments) car manufacture is about three million units a year. One way of reducing the optimum size would be to outsource the production of components such as engines, castings, and pressings (ibid.). Indeed, there is an increasing amount of supplier involvement in production and design, as mentioned earlier. Another strategy is to ally with another car manufacturer or to acquire it. Cooperation among manufacturers and acquisitions go hand in hand in the car industry. Finally, the need for financing high investments makes creditors again a crucial primary stakeholder for car manufacturers.

4.6.4 Summary

The key characteristics of the car industry and their implications for primary stakeholders can be summarized as follows:

First of all, car manufacturers and their primary stakeholders are vulnerable to economic crises because the car is an expensive high-involvement product that customers can delay purchasing during times of crisis (Sloan 1990; 2004). At such times, the home government may play an important role in shaping the conditions in the system. Creditors are also influential primary stakeholders since the industry is investment-intensive, and purchasing of a car requires a significant investment by customers.

Secondly, the car industry is buyer-dominated (Mercer et al. 2004; Akpinar and Zettinig 2008a; Akpinar and Zettinig 2008b). Car manufacturers need to manage a large number of suppliers in a tiered structure since the car is composed of a large number of components (Womack et al. 1991). Changes in the EU car industry since the 1990s have increased the pressure on suppliers, led to consolidation in supply chains, and increased cooperation between car manufacturers and their first-tier suppliers (cf. Frey and Schlosser 1993; Hyun 1994; Helper and Sako 1995; Cleff, Licht, Spielkamp, and Urban 2005; Kappelhoff 2005).

Thirdly, because of the various protective regimes, the EU car industry has traditionally had fragmented distribution channels (Vickerman 1992). As a result, manufacturers have managed to maintain control over their distribution networks, but their relationships with dealers may be subject to change under BER 1400/2002 (Weimar 2006; Akpinar 2007).

Fourthly, the car industry is crucial for employees and home governments because it creates job opportunities for a large number of people and is regarded as a key factor in economic growth (Keller 1993). As a result, there is power play between home governments and car manufacturers with regard to the choice of production location (Stopford and Strange 1992; Studer-Noguez 2001).

Finally, the car industry is highly competitive and demands continuous investments in R&D and PP&E. This increases the importance of creditors in terms of financing and suppliers in terms of taking over some of the investment burden.

This chapter provides a pre-understanding of the research context, the EU and its car industry, from a historical perspective. I will now move on to the next chapter and the empirical study, which is the third stage of this research process.

5 EMPIRICAL STUDY

This chapter comprises the empirical study which is made up of two parts. The first part reviews the history of VW from 1960 until 2005, and the second part analyzes four threat events in the light of the theory.

5.1 The History of VW

VW is the leading German car manufacturer in the EU. As of 2005, it manufactured and sold the Volkswagen, Audi, SEAT, Skoda, Bentley, Bugatti, and Lamborghini brands. In addition, it provided financial services (e.g., direct banking, financing, leasing, insurance and fleet management) for its customers and also operated in the strategic business areas of light commercial vehicles, heavy trucks, buses and coaches, automotive supply, car rental, energy, real estate, IT, and venture capital. Cars constituted its core strategic business area, representing 83 percent of its revenues (see Table 10 in Appendix 2). My focus in the following review of VW’s history is on the key developments that may enhance understanding of the firm’s relationships with its primary stakeholders.

VW was established as a state-owned firm on May 28, 1937 following the development of an affordable ‘people’s car’, i.e. the Beetle, by Ferdinand Porsche (Volkswagen 2003, 4). When Germany lost the Second World War, VW, which was considered an asset of the Nazi government, came under the trusteeship of the British Military Government in June 1945. In September 1949 the British Military Government handed it over to the State of Lower Saxony with the provision that they take control of it on behalf of, and under the supervision of the West German government (Volkswagen 2003, 24). Under the leadership of CEO Heinrich Nordhoff, in the 1950s VW became a symbol of the German economic miracle, achieving sales of ca. 888,507 vehicles in 1960, and 58 percent of the cars was sold out of West Germany (see Table 1 in Appendix 5). Those days VW’s strategy rested on the mass production of a single product, the Beetle, and its internationalization via exports (Haipeter 2000; Widuckel 2004).

Employees at VW were provided with above-average wages and benefits by West German standards, and this was criticized by employer associations as well as by the West German government because it threatened antiinflationary efforts (Volkswagen 2003, 30). One reason for high wages was the shortage of labor in the country on account of the Second World War and the location of VW plant in Wolfsburg, a city near the border with East Germany, which was far from being attractive. A second reason was VW's success and Heinrich Nordhoff's generosity in sharing it with the employees. In a speech in 1948 he explicitly expressed this in the following words: *"…When we succeed and earn some money, then our employees should be the first to benefit …"* (Nordhoff 1948; cited in Speidel 2005, 60). Thirdly, there was a strong trade union, namely IG Metall, and a strong works council at VW. In the case of VW, the trade union has historically been strong. This was due to the fact that the company was established in 1937 with the aid of funds from the Deutsche Arbeitsfront, a Nazi organization that nationalized and used the properties of all German trade unions in 1933 (Selenz 2005, 31–32). VW has always had a special place in IG Metall in that it has had its own agreements separate from the metal industry, and IG Metall has always sent its top manager to the negotiations. In accordance with the Allied Works Council Law of 1946, the VW works council had the right to participate in matters concerning the hiring, firing and transfer of employees, as well as in determining their wages and salaries (Volkswagen 2003, 18). In addition, the law governing industrial relations, passed in 1952, empowered employees by providing them with one-third representation on the Supervisory Board (Andresen 2005).

5.1.1 Privatization in 1960 and the VW Law

VW's economic miracle of the 1950s and accompanying rapid growth necessitated funding, and privatization was a means to achieve that. It would also end the debate as to who was the real owner of the firm, the government of the Land of Lower Saxony, or the West German government (Die Welt 1957). On November 12, 1959 the government of the Land of Lower Saxony and the West German government agreed to privatize 60 percent of the shares of VW while owning the rest, i.e. 20 percent each. They also agreed to create a 'Volkswagenwerk Foundation' for the revenues from privatization. The foundation would lend the money from privatization to the West German government for 20 years and charge interest. The interest revenues would be used to support science.

The two parties were concerned about keeping control of VW following its privatization in 1960. In order to achieve that, they passed the VW law through the parliament on May 9, 1960 which included the following key points (Government of the Federal Republic of Germany 1960a).

1. No single shareholder could exercise more than 20 percent of voting rights at the Annual General Shareholders' Meeting (regardless of the percentage of shares held).
2. The West German government and the government of the Land of Lower Saxony would each have the right to appoint two members of the Supervisory Board of VW even if they sold their shares[136].
3. The adoption of resolutions at the General Shareholders' Meeting would require agreement by holders of more than 80 percent of the share capital[137].
4. Decisions regarding the future of production locations (e.g., closure, the transfer of production facilities) would need the approval of two thirds of the Supervisory Board.
5. The government of the Land of Lower Saxony would support the candidate of the West German government as president of the Supervisory Board.

They also imposed legal restrictions regarding the purchase of shares at privatization in order to make sure that the shares would be distributed among a large shareholder base of people in the low-income class and would not be acquired by a few influential investors. The law regarding VW privatization was passed on July 21, 1960, and the restrictions included the following (Government of the Federal Republic of Germany 1960b):

1. 60 percent of the shares would be privatized and would be sold only to individual persons.
2. A single individual could purchase shares to the maximum value of 500 German Marks (1,000 German Marks for VW employees).
3. Those primarily eligible to purchase VW shares should have a maximum annual income of 8,000 German Marks (a total of 16,000 German Marks if married to an income-generating spouse). Those with a higher annual income could purchase the privatized shares only if it proved impossible to sell them all.
4. A discount of 20 percent would apply to the purchase price if the shares were kept for five years without being sold.

The VW law and the restrictions imposed by the two principal shareholders clearly illustrate their intention to protect their interests against the threat of a future hostile acquisition of a majority of VW shares. I would classify this act as a proactive contribution to resolve an envisioned threat by means of adapting within the system: shaping the firm or the conditions in the system.

136 The West German government never exercised this right, and it sold its shares in 1988 (Volkswagen 1989; Selenz 2005).

137 According to German company law of September 6, 1965, this condition is fulfilled with 75 percent of the share capital (Court of Justice of the European Communities 2007b).

This act also illustrates that such contributions may be made in parallel with or even before shaping the threat at source when a future threat is imagined and made sense of. This inference led me to improve the model which was presented in Figure 8 concerning the process of responding threats[138].

5.1.2 Crisis, 1971–1975

The 1960s were glory years of growth for VW, as thanks to increasing international sales vehicle sales increased by 148 percent from 1960 to 1970 (see Table 1 in Appendix 5)[139]. VW achieved this mainly through the exporting[140] of a single product, the Beetle, but this could not last forever. The export-oriented, single-product firm entered a crisis at the beginning of the 1970s following the collapse of the Bretton Woods system of fixed exchange rates in 1971, when the value of the German Mark appreciated against all major currencies[141]. This threatened VW's competitiveness in major world markets[142], and in return VW had to respond. The situation became even worse when the Arab-Israeli war in 1973 triggered the first global oil crisis, which hit the car industry hard. The management responded to the crisis with a number of measures. These included measures to reduce costs, which necessitated contributions of compensation-related sacrifices from some of its primary stakeholders, mainly employees and suppliers. Below I analyze how these contributions occurred by type of primary stakeholder.

Employees. VW decreased the workforce in its German plants by 25 percent from 124,792 in 1970 to 93,026 in 1975 (see Table 2 in Appendix 5) through 'voluntary' termination, early retirement, and a freeze on the hiring of new staff. In addition, management took a tough line in the collective salary negotiations with IG Metall which demanded a 15-percent increase in wages for 1974 (Volkswagen 1974a). IG Metall was not willing to make sacrifices at the beginning as voiced by VW's CEO Rudolf Leiding:

"…It looks as if IG Metall took no account of the general economic situation and the economic situation of VW…We had to tell them in the

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138 See section 6.1 for the improvement.

139 As of 1970, exports made up 71.5 percent of total foreign sales (Volkswagen 1971).

140 Some montage plants were established in countries with market potential and import restrictions, such as Brazil, Mexico, South Africa and Australia.

141 For example, 56 percent increase against the US Dollar from 1969 to 1976 (Informationsdienst des Instituts der Deutschen Wirtschaft 1977).

142 In an interview, Toni Schmücker, the chairman of the VW Management Board from 1975 until 1982, cited VW's dependence on a single model, the Beetle, as the major reason for the crisis (Auto Motor und Sport 1977a).

negotiations that VW pays higher salaries than the competition[143]*, that 1974 is a special year, and that employers and unions should be partners. However, the limitless demands of the union, which could destroy the firm if met, have proved that partnership is not possible. The negotiations should be carried out with utmost toughness, even if it means a strike…"* (Volkswagen 1974a; Volkswagen 1974c).

VW was on the verge of bankruptcy in the second half of 1974 (Auto Motor und Sport 1977b). The employee representatives finally realized the need to contribute, and in the end the employees contributed through a decrease in the workforce during 1975. As Mr. Leiding said at the Board Meeting on September 3, 1974: *"In the meeting with the works council I got the feeling that they have finally an understanding of the urgency of the situation"* (Volkswagen 1974d).

Suppliers. A second target for cost reduction during the crisis was suppliers. The relationship between VW and its suppliers could be described as a fight between one strong player and hundreds of weak ones (Junge Wirtschaft 1976). Despite drastic increases in raw-material prices[144] between 1971 and 1974, VW strongly resisted its suppliers' efforts to impose price increases. In a discussion forum arranged by the Manager Magazine, Carl Otto Bauer, the owner of Wuppertaler Schraubenfabrik Carl Bauer GmbH & Co., a supplier of VW, expressed VW's attitude towards suppliers as follows:

"…This is <u>power play</u>. A VW supplier developed a part and provided VW with a model and drawings. VW used these drawings to ask for bids from suppliers all over Europe. The supplier that had developed the part was then pressured into decreasing the price to the level of the lowest bidder…VW is imposing the risks of general business conditions on its suppliers. For example, parts prices were reduced for 1975 and 1976. In the same period VW has increased car prices…" (Manager Magazine 1977).

Shareholders. VW did not pay any dividends to its shareholders in 1975 and 1976 because it made losses of 807 million and 157 million German Marks in 1974 and 1975 respectively (Volkswagen 1975; Volkswagen 1976). This was a temporary sacrifice on the part of shareholders as the firm made a profit of 1,004 million German Marks in 1976 and paid a dividend of 90 million German Marks in 1977 (Volkswagen 1977).

Home governments. Since corporate taxes, compensation to the home government from the firm, are dependent on the firm's profits, the German

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[143] According to a report, the personnel costs of VW in Germany were 34 percent higher than those of Opel (Volkswagen 1974b).

[144] For example, between 1971 and 1974 the kilogram prices (in German Marks) of copper, lead, and aluminum increased from 390 to 630, 90 to 175, and 170 to 235, respectively (Volkswagen 1974e).

government had to make a temporary sacrifice when VW made losses in 1974 and 1975.

Dealers. Dealer compensation from car sales is mostly variable in terms of mark-up (i.e. dealer margin on the price) and bonuses. Therefore, with lower sales volumes the compensation of dealers also decreased during the crisis.

Creditors. It appears in the case of VW that creditors did not sacrifice, but indeed benefited from the crisis: VW was not able to generate adequate cash to fund its operations and investments, and as a result needed more external financing (see Table 3 in Appendix 5). VW's additional need for external financing during the crisis turned into correspondingly increasing interest expenses, i.e. increasing compensation for its creditors[145].

Customers. VW reflected some of the increases in its costs in its prices with a total of 25-percent price increase during 1974 and 1975 (Der Spiegel 1976). Despite that its total sales revenues decreased from 11,827 million German Marks in 1973 to 11,227 million in 1975 (Volkswagen 1974g; Volkswagen 1976). This shows that at least 25-percent of VW customers decided not to buy VW cars. Therefore, it cannot be argued that customers need to make sacrifices.

From the above observations I would conclude the following. First of all, in times of economic crisis primary stakeholders make sacrifices in terms of decreasing compensation, except for creditors and customers. Creditors indeed benefit from the crisis since firms need additional financing. Customers cannot be forced to sacrifice. Competition protects them from any obligation to make large sacrifices. In the end, they are powerful (and perhaps more powerful during times of crisis) in that they decide to buy or not to buy.

Secondly, sacrifices are necessary in times of economic crisis because the total revenues of the firm (and thus the system) decrease. For the firm and the system to survive, the losses need to be shared among the firm and its primary stakeholders.

Thirdly, some of the sacrifices occur naturally since compensations are variably dependent on the total revenues of the system. This is the case for example with shareholders (dividends are dependent on the level of the firm's profits) and the home government (corporate taxes are also dependent on the level of the firm's profits).

Finally, other sacrifices which do not occur naturally need management intervention. This is the case for example with employees, and it requires tough negotiations. In times of good economic conditions employee

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[145] The additional external credit in 1974 was provided mainly by a consortium of German banks including Bayerische Vereinsbank, Norddeutsche Landesbank, Bayerische Landesbank, Bank für Gemeinwirtschaft, and Bayerische Hypotheken- und Wechselbank (Volkswagen 1974f).

representatives bargain to get the best benefits for employees, and in times of economic crisis they bargain to avoid sacrifices from their earned compensation.

5.1.3 The Codetermination Law of 1976

Codetermination has had a long tradition at VW since 1945 when the Allied Works Council Law of 1946 gave the works council in VW a voice in the decision-making process (Widuckel 2004). Following the passing of the law governing industrial relations in 1952, a Supervisory Board was established at VW on August 28, 1953, on which employee representatives occupied one third of the seats (Volkswagen 2003; Andresen 2005). In 1972, when the law governing industrial relations was revised, a general works council was formed with expanded rights of involvement in decision-making (Volkswagen 2003). This general works council represented the interests of employees at the firm level, whereas works councils at plants represented interests at the plant level, and the latter reported hierarchically to the general works council (Widuckel 2004).

A codetermination law was passed in Germany in 1976. According to this law, employees and unions in firms with more than 2,000 employees would occupy half of the seats in the Supervisory Board (Thimm 1976). The size of the Supervisory Board would vary from 12 to 20 (according to the size of the firm), and there would be at least two union representatives. The chairman of the Supervisory Board would be a representative of the shareholders and have two votes in case of a tie in the voting. All members of the Board of Management would be elected by the Supervisory Board with a two-thirds' majority.

Following the passing of this law, a new Supervisory Board was elected at VW on July 5, 1977 comprising ten members representing shareholders and ten members representing employees (seven from the works councils and three from IG Metall) (Volkswagen 1978)[146]. The new law altered the balance of power between employees and management at VW to favor employees due to the existing VW law. There were two main reasons for this.

First, as per the VW law, the government of the Land of Lower Saxony had the right to appoint two shareholder representatives, and these representatives were naturally interested in the preservation of jobs in the Land of Lower

[146] Earlier the VW Supervisory Board had 21 members, of which 14 were shareholder representatives and seven were employee representatives (five from works councils and two from IG Metall) (Volkswagen 1977).

Saxony, where VW accounted for 15 percent of employment, 26 percent of industrial output, and 21 percent of industrial investments (Janssen 1994, 81). Therefore, even though the chairman of the Supervisory Board had two votes in case of a tie in the voting, the two social democrat shareholder representatives appointed by the government of the Land of Lower Saxony would shift the balance of power to favor employees.

Secondly, the VW law stipulated that decisions concerning the transfer of production across plants, the build-up or acquisition of new plants, and the shut-down of existing plants required approval from two thirds of the Supervisory Board. Obtaining approval for such decisions became more difficult following the codetermination law. With equal representation on the Supervisory Board employees and their representatives gained the status of 'social partners' in the decision-making, and VW top management needed to convince the general works council first, and then the employee representatives on the Supervisory Board, before key decisions concerning employees could be implemented (Speidel 2005).

VW internationalized its codetermination structure in 1990 by setting up its European general works council comprising a total of 17 employee representatives from Germany, Spain, and Belgium (Speidel 2005, 211). With the further Europeanization of production in the 1990s, new representatives joined this council from the Czech Republic, Italy, Poland, Portugal, Slovakia, and the UK. The European general works council met at least once a year to discuss issues related to employees and production locations, and to seek cooperation on the European level. Further internationalization of codetermination followed when a World general works council was established in 1996, with representatives from production locations in Brazil, Mexico, South Africa, and Argentina joining those from the European general works council (Speidel 2005, 214). The aim of this council was to seek cooperation and solutions to issues on a worldwide level.

Employee representatives at VW appraise the vital role of codetermination in the firm's success with the saying: "*Without codetermination no innovation*" (Volkswagen 2007, 5). According to Carl H. Hahn, the CEO of VW from 1982 until 1993, however, the corporate governance system in Germany, and especially the codetermination law, hindered the competitiveness not only of VW but of all German industries (Hahn 2005, 294). There were three main reasons for this.

First, it isolated Germany from the rest of the world and disadvantaged it in terms of attracting FDI[147].

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[147] German business leaders have cited this as a key reason why foreign firms do not buy German firms and keep their headquarters outside Germany (The Economist 2005b).

Secondly, it reduced efficiency by increasing bureaucracy. As Hahn (2005, 295) cites: *"No machine can be moved, no employee be fired or transferred to a new location, no overtime be made, and no managers be promoted without a written approval from the works councils – a first class veto right..."*

Finally, the philosophy of IG Metall[148] was based on confrontation, aiming as a top priority to protect jobs and the rights of workers. Such an attitude made it almost impossible to take radical decisions in order to improve competitiveness.

5.1.4 The Europeanization of VW, 1980–2005

VW lacked a clear European strategy at the beginning of the 1980s (Hahn 2005, 140). Its brands were poorly represented in Southern Europe: the total market share of the Volkswagen and Audi brands in Spain was about 0.5 percent in 1980, for example (Hahn 2005, 146). With increasing pressure towards market integration and the accompanying threat of Japanese penetration into European markets, VW had to build up its strategies for Europe.

As a first step the VW management decided to establish a presence in all major West European markets with its own general importer organizations. The company therefore established its own general importer in Spain in 1981, and acquired its general importers in Italy and the UK in 1984 and 1993, respectively (Hahn 2005, 142). An opportunity for southern expansion arose when Fiat withdrew its technical support from SEAT, the Spanish national car manufacturer, and SEAT, suffering heavy debts, was offered to VW for acquisition. This acquisition would provide VW with a large dealer network and a higher market share in Spain, as well as with new low-cost production capacity that would partially offset its high manufacturing cost in Germany. The acquisition of an unknown firm with heavy debts was risky, and the VW management therefore decided, as a first step, to sign an agreement with SEAT covering technical cooperation and the assembly of Volkswagen cars in Spain. This strategic move attached SEAT to VW and enabled VW to get to know the Spanish firm better before acquiring 51 percent of its shares on June 18, 1986 (Volkswagen 1987).

SEAT's acquisition was a milestone in VW's southern expansion in Europe. VW pursued a multi-brand strategy and kept SEAT as a separate brand beside Volkswagen and Audi. It positioned SEAT in Europe as a

148 All but three percent of VW employees belong to IG Metall (The Economist 2004; Business Week 2005).

trustable, quality sportive brand to suit the Mediterranean taste to compete against Fiat's sportive cars. VW's success in SEAT was later acknowledged by Fiat's major shareholder Umberto Agnelli: "*VW manufactured the best Fiat*" (Hahn 2005, 149). As a result of SEAT's rapid reach to 2.3 percent market share in Western Europe, VW overtook Fiat to become the market leader in 1990 (ACEA 2006).

The decision to acquire SEAT was negatively perceived by employee representatives in Wolfsburg at first. They were not so happy to transfer the manufacturing of Volkswagen Polo, a small car for the low-price market segment, from Wolfsburg to Spain. In order to obtain their support at the general works council, the management compromised by offering to increase Golf production in Wolfsburg to compensate for the loss of Polo production (Hahn 2005, 145). As a result, employees in Wolfsburg were not required to make sacrifices.

The reunification of Germany in 1989 and the opening of new markets in Central and Eastern Europe following the collapse of the Soviet Union opened up opportunities for VW to expand eastwards in Europe and to further Europeanize its production base (Keller 1993). Following tough negotiations with the Czechoslovakian government, on December 10, 1990 VW was granted the right to acquire 100 percent of Skoda, the Czechoslovakian car manufacturer (Volkswagen 1991). When the acquisition was realized on April 16, 1991, VW kept Skoda as a separate brand with a Czech tradition and accessed significant market share and dealerships in Central and Eastern Europe.

VW took advantage of its geographic closeness to Eastern European markets and further expanded its production base in the region in the 1990s. It invested in Mosel, Chemnitz, and Eisenach in former East Germany (Volkswagen 2003). Other investments included the acquisition of an assembly plant in Bratislava/Czechoslovakia in 1991, the establishment of an assembly plant for light commercial vehicles in Poznan/Poland in 1993, and the establishment of an engine plant in Györ/Hungary in 1994 (ibid.).

The multibrand strategy of VW was built upon clear positioning of brands vs. competitors as articulated by Ferdinand Piëch, the CEO of VW after January 1, 1993 (Lewandowski and Zellner 1997):

"The Volkswagen brand resembles purity and value and it shall compete against Daimler Benz.

The Audi brand resembles the niche sportive and it shall compete against BMW.

The Skoda brand resembles endurance and it shall compete against Volvo.

The SEAT brand resembles the southern sportive and it shall compete against Alfa Romeo and Lancia."

VW increased its spectrum of brands by acquiring the luxury brands Bentley, Lamborghini, and Bugatti in 1998. The move into the upper market segment continued with the introduction of the luxury model Phaeton in 2001 and the sports utility vehicle Touareg in 2002. As a result, the single-product firm of the 1950s and 1960s became a multi-brand firm covering all market segments with a variety of products ranging from the 3-liter Volkswagen Lupo TDI to the 18-cylinder Bugatti EB 218 (Stiens 2001)[149].

As a result of the global economic recovery in the second half of the 1980s and its aggressive expansion policy in Europe VW achieved total sales of 3,030,179 vehicles by 1990 (see Table 4 in Appendix 5), but the start of the 1990s witnessed a new general economic crisis in Europe, which began to hurt the car industry and VW, as the market leader in Western Europe, in 1993[150]. VW responded to this crisis in a number of ways and managed to survive due to sacrifices from its primary stakeholders, primarily employees and suppliers[151].

The economic recovery in West European markets in the second half of the 1990s, the improvement in the firm's position in the North American market following the introduction of the New Beetle, and increasing sales in China, Central and Eastern Europe and Russia, enabled VW to recover from the crisis, and total sales reached 5,161,143 vehicles in 2000 (see Table 5 in Appendix 5) and remained at that level in the first half of the 2000s (see Table 6 in Appendix 5).

This ends the review of VW's history. In the following four sections I analyze the four threat events and primary stakeholder contributions in resolving them.

5.2 The VW Law Event

The abolishment of the VW law was debated in Germany in the 1990s when German company law was changed, but the attempts towards its abolishment were successfully blocked by Gerhard Schröder, who was at that time the Minister President of the Land of Lower Saxony and served on the Supervisory Board of VW (Handelsblatt 1994a; Handelsblatt 1994b). Mr.

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149 VW could achieve economies of scope thanks to its modular manufacturing which enabled the sharing of components across product lines (Automotive News Europe 2001; Automotive News Europe 2003a).

150 New car registrations in Western Europe dropped by 17 percent from 13,498,072 units in 1992 to 11,252,494 units in 1993 (ACEA 2006). VW's sales in Western Europe dropped by 22 percent from 2,367,021 units in 1992 to 1,834,575 units in 1993 (ACEA 2006).

151 The contributions which were similar to those in response to the 1973 crisis are discussed in section 5.3.

Schröder expressed his worries: "*VW contributes 25 percent of the industrial production in the Land of Lower Saxony. Therefore, if VW has a running nose, then the Land of Lower Saxony is sick. Changing the VW law is illogical because the law protects VW from hostile takeover attempts and safeguards workplaces*" (Handelsblatt 1997). As I was informed by Dr. Hoff, the director of the Berlin Office of the German Association of the Automotive Industry during our interview on July 13, 2007, the abolishment of the VW law could have triggered a hostile takeover of the firm due to its chronically low share price as hedge funds considered that the sum of the market values of the seven brands of VW would exceed the market value of the firm as a whole[152]. Dr. Hoff: "*How far can we open our capital market to hedge funds from China or Russia, for example, which are under state influence? It isn't an issue if Gazprom, the Russian energy firm, acquires a German football club, but when key industries are under threat, that needs to be discussed.*"

Given the move towards a single market in the EU, the European Commission considered this law a barrier to the free flow of capital. In its view, the use of golden shares and multiple voting rights in some EU member countries hindered fair competition (Handelsblatt 2001a; Handelsblatt 2001b; Commission of the European Communities 2002b). This view was also echoed by a group of high-level company-law experts, based on the principle of "one share, one vote" (Handelsblatt 2002a). Consequently, the European Commission first warned and then initiated court action against firms that made use of golden shares and multiple voting rights[153]. At the turn of the century, there were also increasing worries that the European Commission would take action against the VW law (Handelsblatt 2000a).

5.2.1 The Initial Attempts to Resolve the Threat

In response, VW managers started developing plans to defend the firm against possible hostile takeovers. In 2000 the company bought back 13 percent of its ordinary shares[154] from the market through VW Beteiligungs GmbH, its 100-percent-owned subsidiary, in order to strengthen its shareholder structure (Volkswagen 2001, 91). A further plan was to find a friendly strategic partner

152 Whereas the total market value of VW was €16.5 billion, it was believed that the Audi brand alone was worth €10 billion (The Economist 2005a).

153 These included the Dutch government's shares in the telecommunications firm KPN and the shipping firm TNT Post Group, French government shares in the oil firm TotalFinaElf, and the Italian government's shares in the telecommunications firm Telecom Italia, the oil firm Eni, and the defense firm Finmeccanica (EU Business 2007).

154 VW had two types of shares: ordinary shares carrying voting rights and preference shares with no voting rights.

or partners to acquire a total of about 20 percent of the ordinary shares (Handelsblatt 2001c). This would allow control of more than half of the ordinary shares since the Land of Lower Saxony already controlled 18.2 percent and the VW management controlled 13 percent (see Table 7 in Appendix 5).

Worries at VW increased further when a British investment group made a written complaint to the European Commission against the VW law in 2001, and Frits Bolkestein, the commissioner responsible for the internal market, promised to investigate the complaint and the law in detail (Handelsblatt 2001d). Thanks to Romano Prodi, the Italian President of the European Commission, the complaint process was delayed in 2002 out of respect for the parliamentary elections in Germany, but in early 2003 Mr. Bolkestein brought the issue back onto the agenda of the European Commission (Handelsblatt 2003a).

The German government was against abolishment of the VW law, and Gerhard Schröder, the German Chancellor, expressed this clearly when Mr. Bolkestein visited Berlin on February 14, 2003 (Handelsblatt 2003b). Mr. Schröder was determined in his position as he said at a meeting of the general works council at Wolfsburg: "*Under my leadership there will not be any changes to the VW law in Germany, and we will fight everyone who wants to bring such changes via Europe*" (Handelsblatt 2002b). In the European Commission the complaint process against the VW law was delayed due to opposition from commissioners Günther Verheugen, Michaele Schreyer, Pascal Lamy, Loyola de Palacio, and Franz Fischler (Handelsblatt 2003c; Handelsblatt 2003d; EU Business 2007), but finally Mr. Bolkestein succeeded in persuading the commissioners and started the process on March 19, 2003 (Handelsblatt 2003e).

In this process The European Commission aimed at first to have a structural dialogue with the German government and to avoid filing a court action (ibid.). The German government, however, refused to make any changes to the VW law. Christian Wulff, the Minister President of Lower Saxony, wrote letters to all of the commissioners, arguing that the VW law was in accordance with EU regulations (Handelsblatt 2004a). The tension between Mr. Bolkestein and the German government increased as both sides held strongly to their positions and resisted compromise (Handelsblatt 2004b). Finally, the European Commission gave the German government an ultimatum: if it did not take any action regarding the VW law by mid-July of 2004, the Commission would initiate court action at the Court of Justice of the European Communities (Handelsblatt 2004c; Handelsblatt 2004d).

In 2004 the VW management entered into serious negotiations with the Mubadala Development Company, the state investment company of Abu

Dhabi in the United Arab Emirates, to sell 6.5 percent of its shares (Handelsblatt 2004e). The sale would improve the stability of VW's shareholder structure and also send a clear message to the European Commission that some investors may not have been of the opinion that the VW law was a barrier to the free flow of capital[155]. Unfortunately, the negotiations came to a halt when the market price of VW shares dropped and the Mubadala Development Company asked for 9.8 percent of the shares for the same price (Handelsblatt 2004f; Volkswagen 2004a).

In the meantime, as the German government continued not to compromise on the VW law, the European Commission decided on October 13, 2004 to take the case to court (Handelsblatt 2004g). Following the European Commission's decision, Christian Wulff gave the first signs of compromise in suggesting that the German government could at least give up its right to appoint two members of the Supervisory Board at VW (Handelsblatt 2004h). These last-minute efforts were in vain, and the European Commission brought court action against Germany at the Court of Justice of the European Communities on March 4, 2005 (Court of Justice of the European Communities 2007b). As I was informed by Dr. Hoff during our interview, stakeholders, including the government of the Land of Lower Saxony, the German government and the trade unions, fought hard during the court process to preserve the VW law, but they had to accept in the end that it could no longer be defended. Mr. Ruiz-Jarabo, the advocate general, gave his opinion on February 13, 2007 that the VW law was against the free flow of capital in the EU and suggested levying a fine against Germany (ibid.). Thus, attempts by primary stakeholders failed to shape the threat at source.

5.2.2 The Contribution by Porsche

Porsche had historical connections with VW. Ferdinand Porsche, the founder, designed and manufactured the first Beetle (Volkswagen 2003; Porsche 2007a). Anton Piëch, Ferdinand Porsche's son-in-law, managed VW from 1941 until the end of the Second World War (Stiens 2001). When VW resumed production after the war it signed an agreement with Porsche, on September 16, 1948, which included the following terms (Stiens 2001, 58):

1. Porsche would receive a license fee of five German Marks for each VW Beetle manufactured.

[155] According to Bernd Pischetsrieder, CEO of VW: "Abu Dhabi would constitute a reliable and long-term oriented investor" (Automotive News Europe 2004a).

2. Porsche would receive the right to construct a sports car based on VW parts.
3. Porsche would receive the right to use the VW dealer network to sell its sports cars.
4. Porsche would receive the right to use the VW service organization for the repair and maintenance of Porsche cars.
5. Porsche would carry out R&D for VW.
6. Porsche would receive the right to be the exclusive general distributor of VW cars in Austria.

As Ferry Porsche, the son of Ferdinand Porsche, said, "*VW management knew very well that we could easily develop a second Beetle to compete against them... And they wouldn't want that…At the end VW was our spiritual property [due to the Beetle's design by Ferdinand Porsche]…*" (Stiens 2001, 58).

VW and Porsche jointly developed the VW-Porsche 914, VW-Porsche 924, and VW-Porsche 944 sports cars, and also operated a joint sales company from 1969 until 1974 (Porsche 2007a, 24). Ferdinand Piëch, grandson of Ferdinand Porsche and a Porsche shareholder, joined VW's sister firm Audi NSU Auto Union on August 1, 1972 (Stiens 2001). After serving successfully there for about 20 years he became the CEO of VW on January 1, 1993, a position he held until April 16, 2004 when he was appointed Chairman of the Supervisory Board. Cooperation between VW and Porsche continued during Mr. Piëch's era. In the 1990s Porsche developed the high-performance RS2 station wagon for Audi (Automotive News Europe 2005a). The two firms jointly developed the sports utility vehicles Porsche Cayenne and Volkswagen Touareg (Porsche 2007a). These cars are being manufactured on the same platform at VW's plant in Bratislava, Slovakia, together with the Audi Q7. As a result, Porsche's purchased services and materials from VW, which were mostly body shells and engines for the Cayenne, accounted for 24 percent of its total purchases in 2006 (Porsche 2007a, 24). VW and Porsche are currently working on joint projects such as developing a hybrid engine and a joint electronics platform, and manufacturing painted body shells for Porsche's forthcoming four-door coupe, the Porsche Panamera (Automotive News 2006). As of December 31, 2004 Porsche also owned less than five percent of VW's shares (Handelsblatt 2005a).

When the European Commission launched the court action against the VW law in 2005, Porsche was worried that a potential hostile takeover of VW could endanger its crucial holding in the firm, and therefore decided on September 25, 2005 to increase its shares from less than five percent to 20 percent (Porsche 2005a; Volkswagen 2005a). Wendeling Wiedeking, the CEO of Porsche, stated: "*Our planned investment is the strategic answer to risk. We* *wish in this way to ensure the independence of VW in our own interest. Making this investment, we seek to secure our business relations with VW and make a significant contribution to our own future plans on a lasting, long-term basis*" (Porsche 2005a; Private Placement Letter 2005)[156]. Porsche made it clear in its press release on September 25, 2005 that the investment would not reach the barrier of 30 percent at which point under German law it would have to make an offer to acquire all shares of VW (Porsche 2005a). According to Arndt Ellinghorst from Dresdner Kleinwort Wasserstein, Porsche may have wanted to acquire more shares in order to obtain power to influence decision-making at VW (Automotive News Europe 2005b). In my opinion, a key motive for Porsche to gain control of VW could also be a response to the threat of complying with the European Commission's intentions to reduce average carbon dioxide emission levels by car manufacturer (cf. Commission of the European Communities 2006a)[157]. Nevertheless, Porsche's move was warmly welcomed at VW since the firm was already in search of a trustable strategic partner to strengthen its shareholder structure against the threat of a hostile takeover (Volkswagen 2005a). It was also warmly welcomed by VW's key stakeholders such as the government of the Land of Lower Saxony and the German government (Handelsblatt 2005b).

Porsche, which had been acquiring VW shares since September 25, 2005, became its largest shareholder[158]: as of March 31, 2007 it owned 22.64 percent of the total number of VW shares and 30.93 percent of the voting rights (Porsche 2007a, 13). This was more than enough to safeguard VW from possible hostile takeovers. Why, then, did Porsche continue to buy shares to increase its voting rights to above 30 percent, especially when it had declared on September 25, 2005 that further purchases were not intended?

Formulating its strategy on the assumption that the VW law would be abolished, Porsche wanted to acquire at least 25 percent of the voting rights in order to secure a blocking minority at the General Shareholders' Meeting, as stipulated by German law (Handelsblatt 2006a). With such a blocking minority Porsche could block all key decisions necessitating a 75-percent majority at the General Shareholders' Meeting, and become the single most powerful shareholder. As it acquired more shares its attitude towards the court action against the VW law also changed in that it wanted the court process to speed up, and the VW law to be abolished as soon as possible: as the largest

[156] Despite these motives, there were also worries in the market that the image of Porsche could suffer from closer connection to VW (Business Week Online 2005).

[157] Porsche manufactures cars with very high carbon dioxide emission levels. Acquisition of VW would automatically decrease the company average.

[158] Porsche acquired different amounts of VW shares on 28.9.2005, 13.11.2006, 14.11.2006, and 26.3.2007 (Porsche 2005b; Porsche 2007a, 14).

shareholder it did not want its voting rights to be limited (Handelsblatt 2006b; Handelsblatt 2006c; Handelsblatt 2006d). With this action Porsche showed that it did not fear creating conflicting interests with other stakeholders, such as the government of the Land of Lower Saxony, which were fighting to keep the VW law (Handelsblatt 2006e). As Jürgen Pieper, an automotive-industry analyst at Bankhaus Metzler, stated: "*The possibility of a complete takeover by Porsche is no longer excluded. Porsche is ready to use any means to fight for power at VW*" (Handelsblatt 2006f). Mr. Wiedeking, the CEO of Porsche, compared their strategy at VW to a chess game: "*Other players who did not expect our planned moves are now nervous*" (Handelsblatt 2006g).

In order to fulfill the requirement of German company law regarding controlling shareholders with more than 30 percent of the voting rights, Porsche gave a mandatory offer on April 26, 2007 to purchase the remaining shares of VW (ibid.). The offer was an obligatory act and did not signal a complete takeover of VW shares, reflected in the fact that the prices offered for the ordinary and preference shares were lower than the market prices (Handelsblatt 2007a). As a result, only 0.2 percent of VW shares were sold to Porsche through this mandatory offer (Handelsblatt 2007b)[159].

The Court of Justice of the European Communities announced its decision on October 23, 2007 that the VW law restricted the free movement of capital (Court of Justice of the European Communities 2007c). The threat of a hostile takeover by hedge funds was over, however, thanks to the contribution initiated by Porsche.

5.2.3 Analysis of the Event

This event exemplified a contribution of adaptation within the system: shaping the firm or the conditions in the system achieved by a primary stakeholder who was both a business-to-business customer and strategic partner. During the course of the event there were also attempts by firm management and various primary stakeholders to resolve the threat such as VW management's buy back of VW shares in 2000, the effort to sell VW shares to the Mubadala Development Company in 2004, and lobbying efforts of various German primary stakeholders against the European Commission (see Figure 17).

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[159] Despite that Porsche increased its share of voting rights to 35.14 percent on September 16, 2008 and declared intentions to further increase it above 50 percent (Porsche 2008).

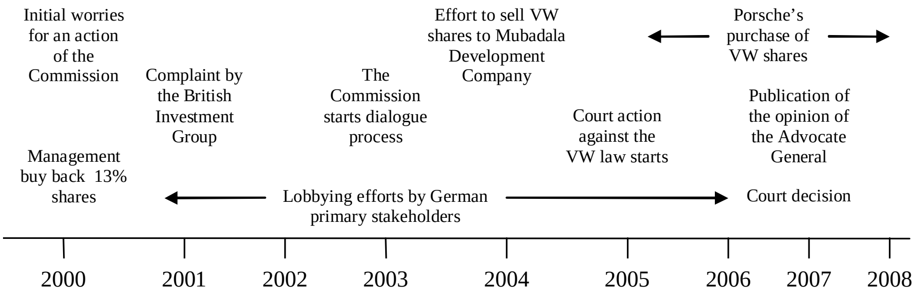

Figure 17. Key episodes in the VW law event

Insights from this event support the theory in the following ways. First of all, the typology is supported because the contribution by Porsche which resolved the threat can be classified as a type in the typology.

Secondly, legal rights and legitimacy increase power against EU regulatory organizations. In this event the coalition of primary stakeholders could not succeed in shaping the threat at source because the VW law, which was an exception even in German company law, had no legal basis. This supports Proposition 12.

Thirdly, legitimacy is also important in terms of giving the primary stakeholders power to shape the firm or the conditions in the system. Such an act may be hindered by a coalition of the firm and other primary stakeholders if it is not approved. In this case, Porsche's acquisition of VW shares was welcomed by the VW management, the government of the Land of Lower Saxony, the German government, and the trade union. This supports Proposition 13.

Fourthly, a primary stakeholder's power to shape the firm or the conditions in the system depends on its owned and accessible resources. Porsche could afford to finance the purchase of VW shares from internal funds due to its high profitability and liquidity (Porsche 2005a; Porsche 2007b). Because of its strong financial position a consortium of financial organizations granted it a loan up to €35 billion on March 26, 2007 for purchasing the remaining VW shares through the mandatory offer (Porsche 2007a, 41). These support Proposition 9 and Proposition 11.

Fifthly, a primary stakeholder's willingness to contribute to heading off a threat depends on the importance of its stake in the firm. Porsche contributed because it had a highly important stake in VW that could have been jeopardized in the event of a hostile takeover. For Porsche, the importance of its stake was a function of its compensation from VW (24 percent of its total material purchases) and relationship-specific investments (the sharing of R&D

costs and new technology). This supports Proposition 1, Proposition 4, Proposition 5 and Proposition 7[160].

Sixthly, there is also support for Proposition 2 because there was not any contribution observed from a primary stakeholder with stake of low importance.

Finally, I discuss Porsche's multiple stakes at VW. Porsche was a corporate customer purchasing body shells for its Cayenne model and a partner in developing technologies such as a hybrid engine and an electronics platform. In my opinion, having multiple-stakeholder bonds does not run contrary to the theory. They imply higher compensation and perhaps higher relationship-specific investments, and thus higher importance of the stake and a greater willingness to contribute.

Insights from the event offer three points to consider for improving the theory. The first point is that efforts to shape the threat at source and to adapt within the system may occur in parallel (see Figure 17). Indeed, efforts to adapt within the system may even start earlier. Whereas the German primary stakeholders started lobbying efforts in 2001, the VW management bought back 13 percent of the shares in 2000, and it has been looking for a reliable partner to acquire shares since then. This insight necessitates the improvement of the model on the process of responding to threats, presented in Figure 8. There is need to develop this temporal model in a way that reflects the temporal connections between the three types of contributions.

The second point regards Porsche's changing attitude in this event. Porsche was initially motivated to safeguard its stake in VW. Later, it continued purchasing more shares than was necessary to avoid hostile takeovers. Porsche management also supported the abolishment of the VW law after Porsche became VW's major shareholder (Handelsblatt 2006b; Handelsblatt 2006c; Handelsblatt 2006d). Perhaps they viewed this threat to VW as an opportunity for Porsche from the very beginning: Mr. Wiedeking declared that Porsche's moves were planned (Handelsblatt 2006g). The fact that Porsche started to purchase VW shares (first purchase on September 28, 2005) after the court process had started on March 4, 2005 also suggests that Porsche was making its plans on the assumption that the VW law would be abolished one day. Porsche did not reveal any opportunistic intentions at the beginning, and was perceived by the VW management and other primary stakeholders as a 'white knight' coming to save VW from the threat of hostile takeovers. Whereas the firm and its primary stakeholders are conceptualized as a system, Porsche's

[160] With the condition that Proposition 7 is revised not to include the phrase 'and that the threat cannot be eliminated at source'. This is because this event showed that efforts for adaptation within the system can start before efforts to eliminate the threat at source.

attitude reminds that elements of the system pursue individual interests which may change in time.

The third point concerns the observation that the firm and its primary stakeholders do also collaborate in efforts to shape the threat at source. This was the case in this event when the German government, the government of the Land of Lower Saxony, and the trade union lobbied the European Commission. I need to incorporate this kind of coalition-building for this type of contribution into the theory.

5.3 The Single Market and VW Event

The creation of a single market in the EU with the free flow of goods, services, labor, and capital created new opportunities (Cecchini 1988), and Japanese car manufacturers, which had been emerging as serious competitors since 1980, did not want to miss them. They wanted to be inside the EU, so they initiated manufacturing FDI there in the 1990s (Egan and McKiernan 1993).

The increasing presence of Japanese manufacturers in Europe was a threat to European manufacturers competing in the same market segments. VW, the European market leader, was a primary target (Speidel 2005; Volkswagen 2005b). It had long succeeded in demanding premium prices for its cars due to its quality image based on German engineering. With the increasing presence of Japanese cars, which offered equivalently high quality at lower prices, competitive pressure on VW heightened at the beginning of the 1990s. VW responded to this threat in a number of ways (see Figure 18).

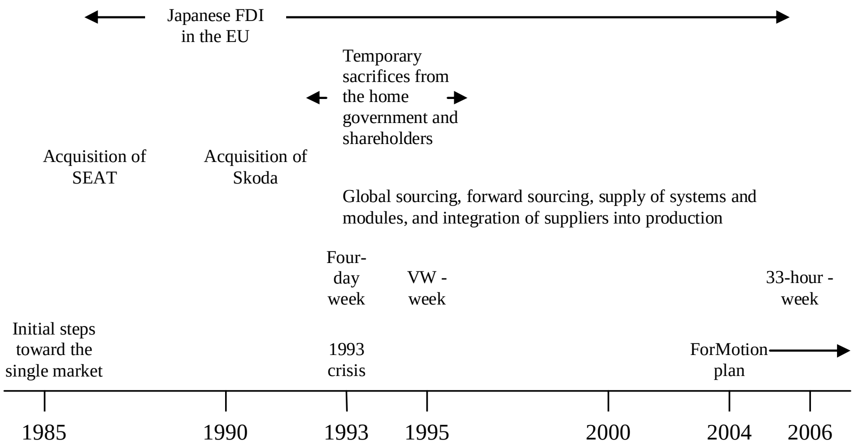

Figure 18. Key episodes in the single market and VW event

As presented in sub-section 5.1.4, it took advantage of the opportunities by successfully Europeanizing its production base via acquisition of SEAT in 1986 and Skoda in 1991. At the same time the management initiated cost-reduction plans after 1988 (Haipeter 2000). The need to reduce costs became urgent when the most severe crisis in the European car industry hit VW in 1993 when VW's sales in Western Europe dropped from 2,367,021 cars in 1992 to 1,834,575 in 1993 (Volkswagen 1993; Volkswagen 1994). As a result, VW was faced with massive overcapacity in Europe, and the management took a number of measures in consultation with the general works council so that it would survive its biggest crisis since 1975. These measures included contributions from its primary stakeholders (mainly from its employees in the German plants, its suppliers, its shareholders, and the German government) in the form of lower compensation and increased input.

5.3.1 The Contributions of Employees at German Plants

A key issue affecting the price competitiveness of VW was the high labor costs in its German plants, in which 64 percent of the total workforce was employed in 1990[161] (Volkswagen 1991). VW had reduced its workforce in Germany from 125,882 employees in 1991 to 108,467 in 1993 in order to adjust to the fall in sales (Volkswagen 1992; Volkswagen 1994). These reductions were realized mostly through early retirement for employees over 55 years of age and the non-renewal of limited-term contracts (Volkswagen

[161] This figure was down to 52 percent in 2005 (Volkswagen 2006a).

1993; Volkswagen 1994). When the crisis hit in 1993, the need to cut down the workforce in Germany rose by an additional 30,000, and this had to be realized by the end of 1995[162] (Hartz 1994).

Cutting down the work force is perhaps more difficult in Germany than in any other country in the EU due to the codetermination law. It is necessary to convince the general works council and also to obtain the approval of employee representatives on the Supervisory Board. In 1993 the VW management made it clear to the employee representatives at the beginning of the negotiations that it was a management priority to preserve all 30,000 workplaces in Germany, but that there was a need to cut costs (ibid.). The employee representatives on the general works council and at IG Metall also made it clear that they would not accept mass layoffs in Germany (Schwitzer 1994). Klaus Volkert, the president of the general works council, told the management before the negotiations that the threat should be resolved creatively rather than through the normal solution of mass layoffs (Hartz 1994, 21). The employee representatives were also aware of the urgency of the crisis and the accompanying need to contribute. Following a 13-hour marathon negotiation session throughout the night of November 24, 1993 the two parties agreed on the four-day-week solution (see Figure 18), which was drafted by Peter Hartz, the director of human resources. The solution required employees to give up at least 20 percent of their annual earnings in return for a reduction in their weekly working hours from 36 to 28.8 (four-day week), and overtime would apply from the 36th hour onwards (Hartz 1994). In return for this sacrifice, the management compromise was to preserve 20,000 jobs in Germany until the end of 1995.

Subsequent sacrifices from VW employees came during the wage and salary negotiations in 1995, 2004, and 2006. The reduction in wages and salaries in 1993 decreased VW's labor costs, but it did not improve productivity because of the shorter working week. It did not suit the cyclical nature of demand, either. These negative sides of the four-day week became apparent as the general economic crisis in Europe eased and production at VW plants had to be increased to meet increasing demand. As a result, Mr. Hartz introduced the concept of the 'breathing company' in 1995 (Hartz 1996). The new concept replaced the four-day week with the 'Volkswagen week' (VW week: see Figure 18), which required flexible working hours from employees: the weekly hours would be determined according to customer demand. This so-called flexibility meant that the number of hours worked in a week could vary from 28.8 to 38.8, and bonuses for Saturday working and overtime were

[162] There would be 20,000 reductions in 1994 and additional 10,000 in 1995 (Schwitzer 1994). See Table 8 in Appendix 5 for details of the planned reductions at VW's German plants.

reduced from 50 and 40 percent respectively to 30 percent each (Hartz 1996, 137). This was a sacrifice in terms of both increased input and decreased compensation.

In order to increase price competitiveness, the management introduced a cost-cutting program in 2004 called ‘ForMotion’ (see Figure 18), the target being to cut labor costs by 30 percent until 2011 (Volkswagen 2004b; Volkswagen 2005b; Ward’s Auto World 2005). The program put customers at the top and required solidarity from all other stakeholders along the value chain in terms of achieving more value for the customers (Volkswagen 2004c). Peter Hartz said: “*This is a necessary move to respond to increasing global competition. In achieving targets, our utmost priority is to safeguard workplaces in Germany*” (Volkswagen 2004b). One key area for cost cutting was labor costs in German plants. Despite major cost improvements in the 1990s, high labor cost in German plants was still a key competitive issue for VW as of 2004 because the contractual salaries and wages were on average 11 percent higher than in other car manufacturers in Germany (Volkswagen 2004d; Ward’s Auto World 2005). What was even worse, the figures were up to 80 percent higher than in VW’s own production sites outside of Germany (Volkswagen 2004d), and labor costs accounted for 17.4 percent of its revenues compared with a European average of 15 percent (Automotive News 2005a; Automotive News Europe 2006a). Besides, in terms of productivity no VW plant ranked in the top 10 in Europe (Automotive News Europe 2006b). Especially its component plants in Germany were far from economical (Automotive News Europe 2006a).

Germany is not only the most expensive place on earth to manufacture cars but also the most resistant to address issues of high cost and low productivity (Ward’s Auto World 2005). At the start of the negotiations in September 2004 the standpoint of the IG Metall representatives was very different from that of the management in that they asked for wage and salary increases of four percent (European Industrial Relations 2004). IG Metall was not willing to make any sacrifices on behalf of the employees. As far as management was concerned, this selfish behavior showed that IG Metall did not grasp the essence of the situation and was endangering jobs in Germany by burdening VW with additional costs (Volkswagen 2004e). Following tough negotiations the two parties agreed on freezing wages and salaries for a period of 28 months in return for guaranteed jobs in Germany until 2011 (Volkswagen 2004f). This was a compromise from both sides.

In 2006 the management took a further step and increased working hours from 28.8 to 33 per week for production employees (see Figure 18) and 34 for administrative employees, without any increase in wages and salaries (Volkswagen 2006b). When negotiations started the management target was the introduction of the 35-hour week without more pay (Volkswagen 2006c). As Dr. Horst Neumann, the member of the Board of Management responsible for human resources, said: "*Negotiations were very tough, but they were characterized by the joint resolve to improve the competitiveness of VW. Competitiveness is the prerequisite for jobs, and we have achieved this with a return to normal working hours*" (Volkswagen 2006b). According to Klaus Dierkes, the chief negotiator on behalf of the management and head of human resources, this was necessary to safeguard employment at VW's traditional plants in Germany in the face of the steadily growing competition (Volkswagen 2006b; Volkswagen 2006d). This increase in working hours was a contribution from employees in the form of increased input.

Analysis of employee contributions:
Employees have had a highly important stake in VW in that they have received compensation that could not be matched by any other firm in the metal industries. This supports Proposition 4. Employee representatives have been a powerful force and resisted the sacrifices as much as possible. Despite their power and resistance, however, they had to contribute in the end because the threat, which could not be eliminated, had serious profit implications and targeted employees directly. It was the jobs in the German plants that were under threat, where the high labor costs decreased VW's competitiveness in the increasingly competitive market. Had the employees not contributed, VW's profitability would have suffered, thereby endangering its survival in the long run. This supports Proposition 3. Employee contributions also support the typology in that they can be classified as a type in the typology.

5.3.2 The Contributions of Suppliers

When Ferdinand Piëch became the CEO of VW in 1993 one of his first accomplishments was to recruit Jose Ignacio López de Arriortúa, the purchasing director of GM whose nickname among suppliers was 'the merciless cost killer' (Speidel 2005, 115). Mr. López introduced at VW the concepts of global sourcing, forward sourcing, the sourcing of modules and systems, and the integrating of suppliers into production (see Figure 18).

The idea behind global sourcing was to decrease VW's purchasing costs through the creation of competition among well-known suppliers from all around the world (Haipeter 2000; Speidel 2005). Under this strategy VW purchasing personnel were required continuously to identify new acceptable suppliers from all over the world, compare their prices, and ask those with lower prices to give offers. Suppliers located in countries with low labor costs clearly had a price advantage over German suppliers (The Economist 1993). These lower offers were then taken to the existing suppliers in Germany, who were asked to beat them. This was a ‘last call’ option for the existing suppliers to maintain their businesses, and was aimed at introducing competition between them and potential alternative suppliers (Gehrke 1996). In most cases the existing suppliers had no choice but to sacrifice from their compensation in order to keep their businesses since they had highly important stakes in VW due to their relationship-specific investments.

The purpose of forward sourcing was to incorporate the selected suppliers into the product-development processes at an early stage (Haipeter 2000; Speidel 2005). In this way it would be possible to benefit from their innovative capabilities, and also to transfer to them some of the burden of high R&D expenses. This change demanded a sacrifice from suppliers in that they had to make new investments in R&D, but on the other hand it also increased their power as they began to control new resources that were important for VW.

The increasing competition in the car industry forced VW to rationalize its supply chains by creating a tiered structure (Haipeter 2000; Speidel 2005)[163]. In this structure VW reduced the number of its direct suppliers by supplying modules and systems rather than parts. The so-called system integrators or first-tier suppliers were asked to manufacture and bring systems and modules directly to the production line. This reduced the logistics costs for VW and integrated its first-tier suppliers into the manufacturing process.

This kind of integration into manufacturing required sacrifices from first-tier suppliers. VW asked them to move their operations closer to its production plants, i.e. in-sourcing (Automotive News 1998a), and 140 suppliers have moved to Wolfsburg since 1995 (Automotive News Europe 2004b). It also asked its German first-tier suppliers to internationalize their production facilities and to start operations near VW plants abroad (Haipeter 2000, 375). These demands necessitated sacrifices from first-tier suppliers in the form of increased input, i.e. new investments.

When Francisco Javier Garcia Sanz became director of purchasing at VW in 1996, he indicated that VW would start long-term-partnerships with its first-tier suppliers (Automotive News Europe 1999; Automotive Industries 2005a), the reasoning being that innovations could be expected from motivated suppliers only through relationships based on mutual trust (Automotive News Europe 2000a). However, this was not going to be a partnership of equals, as Mr. Sanz said in an interview with Automotive News: “*We are only going to work with a world-class supplier base that thinks and acts like we do. VW is*

[163] A tiered structure in their supply chains was observed among suppliers of all car manufacturers in the 1990s (cf. Lamming 1993; Lilliecreutz 1998).

not going to be an easy customer. When VW talks of partnership, it does not mean a harmony club. Suppliers should expect criticism and accept that they will have to improve" (Automotive News 1998b). Suppliers were also skeptical of VW's plans for cooperation (Automotive News 2005b).

Despite this implied change in relationships, VW continued to pressure its suppliers to save on costs and reduce prices. As part of its ForMotion plan, it demanded collaboration from suppliers in joint cost-saving projects (Automotive News 2004; Automotive Industries 2005b; Automotive News Europe 2005c). It held talks with 38 of its main suppliers with a view to streamlining operations and cutting costs (EU Business 2005). As a result of pressure from VW its suppliers lowered their prices by an average four percent in 2006: VW demanded an additional eight-percent cut for 2007 (Automotive News Europe 2006c).

Analysis of supplier contributions:
With increasing competition, suppliers have been forced to make sacrifices in order to contribute to VW's competitiveness. VW's supply chain has gone through a major consolidation process, and suppliers have lacked the power to defend themselves against it. This power differential is evident in that whereas VW is a large multinational, most suppliers in Germany are family businesses. In addition, suppliers have highly important stakes in VW since VW accounts for a large proportion of the sales for many of these suppliers, and suppliers have high relationship-specific investments. The suppliers have agreed to the sacrifices because they have had no other choice given their highly important stakes in VW. These observations support Proposition 3, Proposition 4, and Proposition 5. Supplier contributions are also supporting the typology in that they can be classified as a type in the typology.

5.3.3 Other Contributions

There were also contributions from the home government and shareholders in the form of compensation-related sacrifice during the 1993 crisis (see Figure 18). The home government lost in terms of corporate taxes as VW's profitability was hit due to lower sales. Likewise, VW had to decrease its dividend payments from 11 German Marks per ordinary share in 1991 (Volkswagen 1992) to two in 1992 and 1993 (Volkswagen 1993; Volkswagen 1994). Dividends gradually improved to three German Marks per ordinary share in 1994 (Volkswagen 1995), six in 1995 (Volkswagen 1996), nine in 1996 (Volkswagen 1997), and 12 in 1997 (Volkswagen 1998).

The fact that these contributions were temporary leads me to conclude that they were consequences of the 1993 crisis rather than of the single market. Such temporary contributions were also observed during the 1973 crisis. Despite that, this finding leads me to differentiate between temporary and permanent compensation-related sacrifices if the firm gets into a crisis due to realization of the threat. When the crisis decreases the firm's sales, the total compensation pie for the firm and its primary stakeholders diminishes. In such a situation primary stakeholders who receive compensation from the firm's sales may need to make temporary sacrifices: this includes all primary stakeholders except customers and creditors.

5.4 The 13th EU Directive Event

The European Commission prepared a proposal for the 13th EU directive on takeover bids for the first time on December 21, 1988 (Commission of the European Communities 2007b). The proposal which had its origins in the Anglo-American type of shareholder-oriented corporate governance laid down transparency requirements for takeover bids. The key objective was to achieve the free flow of capital in the EU by eliminating obstacles against hostile takeovers (Andersen 2004; Bernitz 2004). Further objectives included drawing up fair common rules for takeover bids in the EU, offering increased legal assurance to firms when operating in several member countries, and providing proper protection to minority shareholders in the case of a change of control (Commission of the European Communities 1990; Business Europe 2001a; Bolkestein 2002).

The proposal was submitted to the Council of Ministers on January 19, 1989, and to the European Parliament on March 8, 1989 (Commission of the European Communities 2007b). Following reception of the opinions of the European Economic and Social Committee and the Committee of the European Parliament, the European Parliament decided on its first reading on January 17, 1990 to approve the proposal but with certain suggested amendments. As part of the co-decision procedure the Council of Ministers declared on the same day that that it agreed with the decision of the European Parliament.

The European Commission amended its proposal on September 10, 1990 and transmitted it back to the Council of Ministers and the European Parliament (Commission of the European Communities 1990). On February 28, 1991 the European Economic and Social Committee expressed discontent with the amended proposal, arguing that there was a need for the national regulatory authorities to be provided with powers allowing them some measure of flexibility during the implementation of the directive (European Economic and Social Committee 1991). This need for flexibility was based on the fact that the directive was new to countries in Continental Europe where stakeholder-oriented corporate governance prevailed (cf. Corporate Finance 2002a). Indeed, member countries were not in favor of the new directive. Germany and the Netherlands were in principle against encouraging takeovers, and other countries were opposed to the overly detailed text of the proposal. Even the UK feared that the new directive would create problems in its active takeover market through the introduction of legal challenges and tactical delays (Knudsen 2005). As the general economic climate in Europe changed as a result of the crisis at the beginning of the 1990s, the proposal encountered strong opposition from member countries (Commission of the European Communities 2002b), and as a result the European Commission decided to withdraw its proposal (Commission of the European Communities 2002b; Knudsen 2005).

The European Commission drew up a new proposal on February 7, 1996 in which it took into consideration the concerns of the member countries and set out a general framework for takeovers without attempting full harmonization (Commission of the European Communities 1996; Commission of the European Communities 2007c). Under the new proposal member countries were given the freedom to meet the requirements of the directive in the manner most consistent with their existing structures. The proposal entered the co-decision process, but it was delayed due to Spain's opposition in the Council of Ministers regarding an issue with the UK concerning Gibraltar (Handelsblatt 2000b). When the issue was resolved in 1999 the governments of the 15 member countries were finally in agreement and ready to adopt the new proposal (Handelsblatt 1999).

5.4.1 The Contributions by German Primary Stakeholders

It was a big hit in Germany when Mannesmann, Germany's telecommunications national champion, was taken over in a hostile manner by Britain's telecommunications giant Vodafone. This was the largest of the four hostile takeovers in the previous 50 years of German business history (Telegraph 2007a). It heightened public awareness in Germany of the threat posed to national champions by acquisitive foreign firms (Corporate Finance 2002b). As Franz-Jörg Semler, an industry expert, commented: "*Vodafone Mannesmann has left its traces. It was widely seen as the dismantling of a prestigious firm and the loss of a large number of jobs. It has led to public* *support for German firms to be allowed to use protective measures against hostile takeover bids*" (Handelsblatt 2001b).

Mannesmann's hostile acquisition by Vodafone changed attitudes in Germany towards the 13th takeover directive proposal of the European Commission which allowed the management of the target firm to use defensive measures (e.g., poison pills) against the takeover attempt only upon the approval of its shareholders (cf. Commission of the European Communities 1996). Industry associations[164] and trade unions in Germany started to lobby intensively the German government and the members of the European Parliament against the adoption of the proposed directive (Handelsblatt 2001b; Telegraph 2007b). VW and Badische Anilin und Soda Fabrik (BASF), the German chemical firm, feared the threat of hostile takeovers the most (Handelsblatt 2001b). Ferdinand Piëch, CEO of VW, and Jürgen Strube, President of BASF, met with Gerhard Schröder to explain their worries (Handelsblatt 2001e; Handelsblatt 2001f). The argumentation of the opposing stakeholders was based on the following three points.

First, poison pills, which were prohibited under the new proposal, were widely used in the USA, and this would produce unfair competition against US firms (Handelsblatt 2001g; The Economist 2001a; The Economist 2001b; Commission of the European Communities 2002b).

Secondly, the use of golden shares was already prohibited in Germany while the governments of Spain, Italy, and the UK allowed them[165]. Prohibiting poison pills without prohibiting golden shares in the EU would create unfair competition against German firms (Handelsblatt 2001a; Handelsblatt 2001b; Commission of the European Communities 2002b).

Finally, the new proposal did not adequately protect employees working for companies involved in a takeover bid (Commission of the European Communities 2002b; Knudsen 2005).

The lobbying efforts in Germany were fruitful in that the German Christian Democrat Members of the European Parliament suggested changes to the directive proposal allowing managements to use poison pills against hostile takeover bids without having to consult shareholders (Business Europe 2001b). They succeeded in getting a decision from the European Parliament on December 13, 2000 with a request for amendments from the European Commission regarding this issue (Commission of the European Communities 2007c). Behind this success were the intensive lobbying efforts of the German industry associations, trade unions and influential individuals like Ferdinand

[164] Industry associations represent firms and therefore are not considered as primary stakeholders in this context.

[165] There were about 25 large European firms that were protected by golden shares (The Economist 2002).

Piëch and Jürgen Strube (Handelsblatt 2000c). The amendment request was a blow to the European Commission. It was not acceptable to the Council of Ministers either as it had already unanimously agreed in July 2000 that poison pills should be prohibited (Handelsblatt 2000d; Business Europe 2001b). The European Parliament thus took a position against the common position of the European Commission and the Council of Ministers regarding the new proposal (Handelsblatt 2000e). As a result, a Conciliation Committee was formed comprising an equal number of members from the European Parliament and the Council of Ministers in order to resolve the differences (Commission of the European Communities 2007c).

Before the hostile takeover of Mannesmann the German government led by Gerhard Schröder was also in agreement with the other member countries in the Council of Ministers concerning the adoption of the European Commission's new proposal (Handelsblatt 2001h). It had even delayed the adoption of a German takeover directive to wait for the EU takeover directive's adoption (Handelsblatt 2000e). As opposition heightened in Germany following Mannesmann's acquisition, Gerhard Schröder could not resist the increasing pressure and changed his position as well (Handelsblatt 2001e; Handelsblatt 2001h). Consequently, the German government took a major step on March 12, 2001 and prepared a draft proposal for a national directive on takeover bids without waiting for the forthcoming EU takeover directive (Handelsblatt 2001i). The new German directive, which would come into force as of January 1, 2002, was more in line with the proposals of the European Parliament and gave management the right to take defensive measures against hostile takeover bids (Handelsblatt 2001j). This act of the German government was a clear sign of its changing position to Brussels, and it was warmly welcome by the European Parliament as an example of a compromise takeover directive for the EU (Handelsblatt 2001k).

On no other occasion were the German government, the opposition parties, German industry, and the trade unions so united as against the EU takeover directive (Handelsblatt 2001f). The conciliation process witnessed immense power play and tactical maneuvering between the European Commission, the Council of Ministers and the European Parliament (Handelsblatt 2001l). Despite the lobbying efforts of the German coalition, the European Commission and the Council of Ministers succeeded in dividing opinion among the EU Parliament representatives in the Conciliation Committee, and the Conciliation Committee decided on June 5, 2001 to approve the proposal of the European Commission (Handelsblatt 2001a).

According to the co-decision procedure, there was only one final step left before the takeover directive was adopted: the suggested directive of the Conciliation Committee had to be approved at both the Council of Ministers and the European Parliament. Following this defeat the industry associations and trade unions in Germany engaged in intensive lobbying in Brussels and Berlin (Handelsblatt 2001m). The German government also took a key role in lobbying members of the European Parliament. As one senior EU official said: "*The Germans are extremely influential in the European Parliament, beyond their numbers, and they have got a long memory, so nobody wants to get on the wrong side of them*" (Telegraph 2007a). In the end, the proposal of the Conciliation Committee was rejected at the European Parliament on July 4, 2001, with a historical tie of 273 votes for and 273 votes against, with 22 abstentions and 58 who did not bother to vote (Business Europe 2001c). Unlike on most occasions, Members of the European Parliament voted this time according to national interests rather than party affiliation (see Table 9 in Appendix 5). This brought howls of protest from supporters of the proposal and a noticeable sigh of relief from Germany (Global Finance 2001).

Mr. Bolkestein blamed Gerhard Schröder and German industry for the failure of the proposal (Handelsblatt 2001n). Following this rejection the European Commission engaged a group of high-level experts in company law to produce a report for drafting a new directive on takeover bids. The report was published on January 10, 2002, and proposed maintaining the neutrality of target-firm management during takeover bids. The group also suggested abolishing golden shares and multiple voting rights in Europe, based on the principle of "one share, one vote" (Handelsblatt 2002a). The majority of member countries, especially those in which golden shares and multiple voting rights existed, were against these suggestions (Commission of the European Communities 2002b; Handelsblatt 2002c), the only country to welcome them being the UK (Handelsblatt 2002d).

After extensive negotiations between the European Commission, the Council of Ministers and the European Parliament, an EU takeover directive was finally adopted on April 21, 2004 (European Parliament and the Council of the European Union 2004). However, it remained optional to member countries whether or not to insist on the neutrality of target-company managements. The use of multiple voting rights during hostile takeover attempts also remained optional. In the light of these measures it could be argued that the European Commission initiative promoting a harmonized active takeover market in the EU was blocked (i.e. shaped at source) by resistance from German industry supported by contributions from primary stakeholders such as the home government and employee representatives.

5.4.2 Analysis of the Event

This event was an example of a contribution to shape the threat at source by a consortium including industry associations and primary stakeholders led by the German government and employee representatives (see Figure 19).

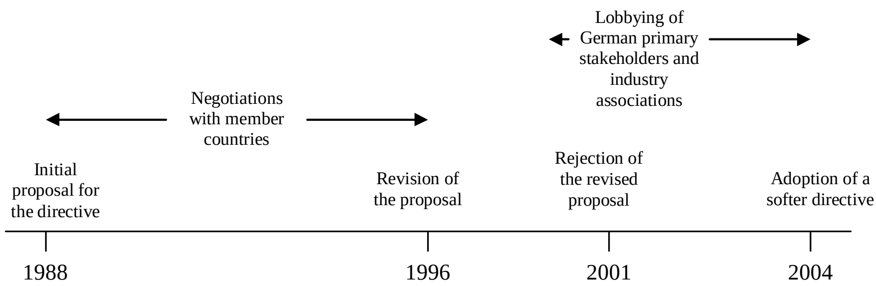

Figure 19. Key episodes in the 13th EU directive event

This event supports the theory in the following ways. First, there is support for the typology because the contribution which resolved the threat could be classified as a type in the typology.

Secondly, the nature of the threat played a moderating role in determining the willingness of the primary stakeholders to contribute. The primary stakeholders, who were the most exposed to the negative effects of takeovers, were employees since their jobs were in danger. Thus, it was the employee representatives, i.e. the trade unions, which first lobbied strongly against the proposal. This supports Proposition 14. The nature of the threat also determined which primary stakeholders were able to contribute. In lobbying the EU regulatory organizations during the adoption of the new legislation, the home government was the most influential actor. This supports Proposition 15.

Thirdly, power is an important determinant of the ability to contribute in terms of shaping a threat arising from forthcoming new EU legislation at source. The home government has the power to shape such threats at source because the adoption of new legislation is based on a co-decision procedure involving the Council of Ministers and the European Parliament, two organizations on which the home government and its bureaucrats have the most influence through their national representatives[166]. This supports Proposition 10. In my opinion, had the German government not been persuaded to change its position in this case, it would not have been possible

[166] See sub-section 4.1.3.

to block the original proposal of the European Commission. Having said this, I should also mention that the powers of the home governments of EU member countries are not the same: the German, UK, and French governments are perhaps more powerful than others because these countries account for a large proportion of the EU economy and also have more votes in both the Council of Ministers and the European Parliament due to their high populations. Had the original EU takeover directive proposal been perceived as a threat only by a single, small member country rather than by Germany, it would probably not have been possible to prevent its adoption, either. This supports Proposition 6 and Proposition 8.

Fourthly, the powers of German stakeholders to affect Members of the European Parliament stemmed mainly from their legally based claims concerning the new proposal. These included the right to fair competition within the EU (through the abolishment of golden shares and multiple voting rights, which existed in some EU countries) and against the USA (through preserving the management right to use poison pills, which existed in the USA). This supports Proposition 12.

Fifthly, the German government made a contribution because the threat concerned national champions of Germany such as VW and BASF. The importance of the government's stake in these firms was high because of the welfare they provided to the German society in terms of employment, taxes, etc. Had the threat been only for a small number of SMEs, the German government may not have been equally willing. This supports Proposition 1 and Proposition 4.

Finally, there is also support for Proposition 2 because there was not any contribution observed from a primary stakeholder with stake of low importance.

This event also opened up new areas for improving the theory. First, it showed that the willingness to contribute is subject to change in time. For example, the German government was in favor of the EU takeover directive proposal at first. It changed its position following the lobbying efforts in Germany. I will take into account the dynamic nature of this concept when improving the theory.

Secondly, shaping a threat at source may need the combined efforts of a number of actors in the case of lobbying EU regulatory organizations. Firms and their primary stakeholders may build up a coalition in order to achieve that. This happened in this event when the German industry associations and trade unions, and the CEOs of VW and BASF lobbied the German government and achieved contributions from it in the form of lobbying the European Parliament. I need to incorporate this into the theory.

Finally, this event showed that power may also reside in influential personalities in firms or among their primary stakeholders. In this case the meeting between Ferdinand Piëch, Jürgen Strube and Gerhard Schröder played a key role in changing the position of the German government (Handelsblatt 2001e). I discuss this further in improving the theory.

5.5 The Block Exemption Regulation 1400/2002 Event

Distribution and repair & maintenance have long been highly protected by regulation in the European car industry (cf. Commission of the European Communities 1995), which has led to a fragmented network structure (Vickerman 1992). In his speech at the Forum Europe Conference on May 11, 2000 Mario Monti, the commissioner for competition policy, gave the first signals of the European Commission's intentions to lift the existing protection in 2002 when the current regulation, i.e. BER 1475/95, was due to expire. According to Mr. Monti, the following three assumptions that had previously justified the existence of BER 1475/95 were open to question (Monti 2000).

First, the assumption that there was effective competition in the car industry was questionable given the fact that the top six manufacturers in Europe had a combined share of about 75 percent of the European car market. In addition, competition between dealers was restricted by the banning of active marketing outside of allocated territories. Manufacturers' contractual rights to end dealerships at only two years notice made it wise for dealers not to pursue sales policies which their manufacturers disliked.

Secondly, the assumption that there was a natural link between car sales and repair & maintenance, and that dealers had to provide repair & maintenance services, could not be justified on any technical grounds. Indeed, such bundling of value-chain activities was a serious restriction on competition.

Finally, the assumption that car repair required brand specialists could also be questioned in terms of whether the repairers really needed to belong to the manufacturer's network, or whether independent repairers could do the work if they had full access to all technical information.

The European Commission's intentions to change BER 1475/95 intensified when the British Consumers' Association sent 20,000 protest notes signed by British consumers complaining about the high prices in the UK and the difficulties they encountered when they wanted to purchase cars from dealers in Continental Europe (Monti 2000). Dealers in Continental Europe were prevented by their manufacturers in various ways from selling cars to foreign consumers, and this was a clear indication that the single market was not functioning[167]. In addition, there was also a need to incorporate e-commerce into the regulation since it had become an alternative distribution channel following the technological advances in the use of the Internet.

The European Commission argued that BER 1475/95 favored manufacturers and did not give dealers adequate freedom in car distribution. Indeed, it was of the opinion that car manufacturers were abusing the power that the exemption rules gave them (Automotive News Europe 2000c). Mr. Monti described the existing situation as the manufacturer sitting in the back seat of the car and giving instructions to his chauffeur, the dealer, on how to drive down the distribution highway to the consumer who buys the car (Monti 2000, 9). This was far from the intended situation in which the consumer had to be sitting in the driver's seat (Monti 2000, 2). There was therefore a need for a new regulation with the following objectives (Monti 2000): to encourage the functioning of the single market in favor of consumers through the development of parallel trade across borders, to strengthen the dealers' independence from manufacturers, to put independent repairers in a better position to compete in the after-sales market, and to provide spare-part manufacturers with direct access to dealers.

5.5.1 The Attempts to Shape the Threat at Source

The European Commission's proposals faced strong opposition, mainly from car manufacturers but also from dealers who would lose territorial exclusivity (Monti 2002, 3). There were worries that supermarkets would drive small dealers out of business, dilute car-brand integrity and reduce the level of service for consumers (BBC News Online 2007). On October 25, 2000 ACEA and CECRA published a joint press release in which they expressed their worries about the intended changes. They argued that in a free-for-all system market forces would create a concentration on the more profitable sales and routine repairs in highly populated areas, and would also tend to increase production and distribution costs (due to inherent heavy demand fluctuations). As a result, prices would increase, consumer choice would be reduced, and delivery periods would be longer (ACEA and CECRA 2000). Both manufacturers and repairers perceived the intended changes as threat to their operations. Manufacturers feared losing control over their distribution and repair & maintenance networks, and dealers feared losing their jobs due to

[167] For example, VW forbid sales from its Italian dealers to German and Austrian consumers between 1993 and 1996. As a result, it was fined €90 million (Automotive News Europe 2000b).

increasing competition in their territories. CECRA suggested the prolongation of BER 1475/95 by adapting it to suit the requirements of e-commerce (CECRA 2001, 10). In defending the regulation CECRA issued position papers and sent them to all commissioners, chiefs of cabinets, general directors, Members of the European Parliament, the Committee on Economic and Monetary Affairs, and the Legal Affairs Committee, participated in the hearings of the European Commission and the European Parliament, held meetings with Mr. Monti, and organized two lunch meetings with Members of the European Parliament (CECRA 2001; CECRA 2002a)

In addition, CECRA's national member organizations and dealers also wrote letters to the commissioners and Members of the European Parliament in their countries, and to their national governments in defense of BER 1475/95 (CECRA 2002a). There was also opposition from national governments and their politicians. Werner Müller, Germany's Economy Minister, wrote a letter to Mr. Monti, criticizing his intended modification (BBC News Online 2007). Gerhard Schröder said: "*The destruction of the block exemption regulation would bring huge competitive disadvantages to the German car industry. Changes threaten Germany's already weak labor market*" (Ward's Auto World 2002).

Despite the strong opposition, the European Commission presented a draft proposal for a new block exemption regulation at the beginning of 2002. According to Jürgen Creutzig, the president of CECRA, the European Commission's goal to achieve a 20 percent decrease in car prices with the new regulation was unrealistic (CECRA 2002b). He was also disappointed that the draft proposal did not contain clauses suggesting a minimum period for the termination of contracts or protecting the high relationship-specific investments that dealers had to finance (CECRA 2002c). Mr. Creutzig warned that if the proposal was passed unchanged, then tens of thousands of the 108,000 authorized dealers in the EU, which were mainly SMEs, would very soon disappear from the market (ibid.). CECRA sent letters again to all commissioners and Members of the European Parliament asking them not to accept the draft proposal (CECRA 2002d; CECRA 2002e).

CECRA's attempts bore some fruit in that the European Parliament asked the European Commission to include the following amendments in the new regulation (CECRA 2002f):

1. The abolishment of the location clause permitting dealers to set up outlets anywhere in the EEA should be postponed until October 1, 2005, and should come into force only after a review of the situation by the European Commission.
2. Car manufacturers should be obliged to give reasons when they wanted to terminate dealers' contracts.

3. Car manufacturers should pay compensation if they terminated contracts and if the dealers' investments had not been amortized at the time the notified termination came into force.

5.5.2 The New Regulation: An Opportunity for Car Manufacturers?

Unlike the 13th EU directive on takeover bids, BER 1400/2002 did not necessitate a co-decision process because it was the renewal of an existing regulation, and this was under the responsibility of the European Commission as the regulatory organization responsible for implementing EU legislation.

The European Commission adopted regulation 1400/2002 in July 2002 (Commission of the European Communities 2002a). It came into force on October 1, with the exception of the abolishment of the location clause due to come into force on October 1, 2005 (Commission of the European Communities 2002a). The new regulation implied four key changes from the old regulation (Akpinar 2007, 177):

First, under the old regulation dealers were allowed to carry out active sales operations only in allocated territories (exclusive and selective distribution). Now manufacturers have to choose between the following two distribution systems in each country market:

- Exclusive distribution – dealers are allocated a given territory, but they are free to sell to independent resellers (supermarkets and Internet sellers), which can trade anywhere in the EEA.
- Selective distribution – dealers can carry out active sales[168] anywhere in the EEA except for markets in which the manufacturer is operating under the exclusive distribution system. In this case, dealers are not allowed to sell to independent resellers, however.

Secondly, the new regulation eases multi-branding opportunities for dealers. Whereas previously they had to open a second showroom to sell cars of a different brand, they are now able to sell other brands in the same showroom (in clearly distinct places, however).

Thirdly, the new regulation separates repair & maintenance from distribution.

Finally, under the new regulation repairers are no longer required to use original parts. They may supply equivalent "non-original" parts obtained from independent suppliers.

CECRA was disappointed that the European Commission did not take into account the European Parliament's suggestion to review the situation on the

168 The setting up of outlets was after October 1, 2005, however.

location clause before abolishing it on October 1, 2005 (CECRA 2002g). CECRA was also disappointed in that the new regulation provided no protection for the huge relationship-specific investments that dealers and repairers had to make in their businesses, separated distribution from after-sales services, defined leasing companies as end users and opened a new sales channel besides the authorized network, and allowed direct sales from manufacturers to end users (CECRA 2002a; CECRA 2002g). On the other hand, there were also points that CECRA positively welcomed. These included the achievement of a branch-specific block exemption regulation instead of belonging to the umbrella regulation 2790/1999, and the necessity for car manufacturers to give two years' notice and also give good reasons in writing when terminating dealer contracts.

Changes in the new regulation did not necessitate cancellation of existing contracts between manufacturers and dealers in that the old contracts could be adapted with amendments to include the new clauses (CECRA 2002a). This is not what happened, however. As I was informed by Mr. Rantala during our interview, many manufacturers took advantage of the changing situation in that they cancelled all their dealer contracts and offered completely new ones with unfavorable conditions only to the dealers that they wanted to work with (see also Automotive News Europe 2002a).

Mr. Rantala: "*Under the new contracts the manufacturers took a tighter grip of the dealers. The standards they set were financially more severe than before. In addition, they also decreased dealer bonuses. Earlier the bonuses were fixed, but under the new contracts they were divided into fixed and variable parts. The variable part required meeting all kinds of qualitative criteria, which were difficult to achieve. In the end, many dealers could not achieve 100 percent of the variable bonuses, and even those that achieved to meet the criteria earned less in bonuses, in total, than earlier.*"

Car manufacturers wanted fewer, larger, and more financially stable dealers (Automotive News Europe 2002a). This was also mentioned by Dr. Hoff during our interview. According to dealers, BER 1400/2002 became an excuse for car manufacturers to get rid of dealers they had planned to fire anyway (Automotive News Europe 2002b). As Axel Koblitz, secretary general of the German dealer association, put it: "*Of course the manufacturers will take this opportunity to cut their networks…As the stronger partner they are in a good position to negotiate a better deal for themselves with their networks*" (ibid.). The downsizing of dealer networks in Europe started to accelerate in 2001, and continued at a high speed until 2004. According to a report prepared for the European Commission evaluating the impacts of BER 1400/2002, the total number of dealer outlets in Western Europe decreased from 104,643 in 2000 to 74,160 in 2004 (London Economics 2006, 42). Dealers that were terminated were mostly small workshop-style operations in rural areas, which did not have the money to invest in new equipment (Automotive News Europe 2002c). According to Jürgen Creutzig, "*Manufacturers set standards so high that many dealers and repairers cannot meet them. They are also squeezing dealer margins and making it more difficult to sell other brands despite the new rules*" (Automotive News Europe 2003b). VW decreased its fixed margin from 15 to 11 percent, and scrapped most bonuses, thus decreasing the top achievable margin from 20 to 18 percent (Automotive News Europe 2005d). CECRA recommended that dealers sign the new contracts even if they believe that they do not comply with EU laws. As Mr. Creutzig remarked, "*Dealers and repairers can face ruin if they refuse new contracts. They have no choice. If they do not sign, they will not have new cars, tools, equipment and training. Then the business is out. It is bankrupt*" (ibid.).

5.5.3 Analysis of the Event

This event exemplified contributions of compensation-related sacrifices or increased input from dealers realized through the opportunistic act of powerful car manufacturers during the changing of an EU regulation. Initially, the initiative of the European Commission to change the existing BER 1475/95 has been perceived by car manufacturers and dealers to threaten the existing system. Efforts to shaping the threat at source have failed, and with the coming into force of BER 1400/2002 manufacturers have exploited the opportunity to rationalize their distribution networks by terminating all dealer contracts and offering new ones with unfavorable conditions only to selected dealers (see Figure 20). This has resulted in contributions from dealers in the form of compensation-related sacrifices (i.e. decreased margins) and increased input (i.e. new investments to meet higher manufacturer standards).

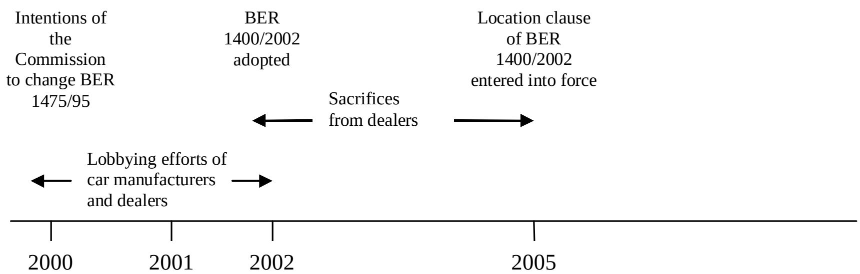

Figure 20. Key episodes in the block exemption regulation 1400/2002 event

This event supports the typology in that the contribution of dealers could be classified as a type in the typology. The event also provides support for the theory regarding the nature of the threat which determined the primary stakeholders that would be willing to contribute. As the threat concerned distribution and repair & maintenance networks in the car industry, the willingness to contribute came naturally from dealers. As the threat originated from an initiative of the European Commission, CECRA took a leading role in the lobbying efforts, and national dealer associations lobbied their home governments to influence the European Commission. This supports Proposition 14.

The nature of the threat also determined the ability of the primary stakeholders to contribute. This event showed that it is more difficult to influence the European Commission during the implementation of EU legislation as the coalition of dealer associations, car-manufacturer associations, and home governments could not shape the threat at the European Commission. This supports Proposition 15.

Dealers had highly important stakes in car manufacturers as they were the only sources of compensation and they had to invest for brand-specific criteria in their showrooms. This provided evidence for the connections of the importance of stake to compensation and relationship-specific investments supporting Proposition 4 and Proposition 5.

This event also gave insights for improving the theory. It showed that the actors involved in the threat may behave differently during the different phases. At first the car manufacturers and dealers collaborated in trying to shape the threat at the European Commission. When they realized that this was no longer possible, the powerful car manufacturers gave up on the collaboration as they took the opportunity to reap benefits for themselves at the expense of the dealers. I will elaborate more on this finding in improving the theory longitudinally. This finding also led me to reconsider Proposition 3. This event does not challenge Proposition 3 but perhaps necessitates a new proposition to incorporate the case of opportunistic behavior since it is exemplified that compensation-related sacrifices can also occur out of such behavior.

Finally, power of car manufacturers over dealers stems from two sources: owned resources (e.g., technical information and equipment for servicing cars) and legal rights (e.g., rights to terminate dealer contracts).

5.6 Cross-event Analysis

In this section I synthesize evidence from the events to support or challenge the theory and suggest insights to improve it.

In this cross-event analysis I reach a conclusion to accept an element of the theory if there is support from at least one of the events, and there is not any challenging evidence from another event (see Table 11). I need to emphasize that it is not possible to find evidence for all of the propositions in a single event. This is because 11 of the propositions (except for Proposition 4, Proposition 5, Proposition 14, and Proposition 15) are specific to the type of contribution, and there is only one type of contribution analyzed in each of the events.

Table 11. The theory in the light of the empirical study

Element of theory	The VW law event	The single market and VW event	The 13th EU directive event	The BER 1400/2002 event	Conclusion
Typology	Support	Support	Support	Support	Acceptance
The process of responding to threats	Challenge				Revision
Proposition 1	Support		Support		Acceptance
Proposition 2	Support		Support		Acceptance
Proposition 3		Support			Acceptance
Proposition 4	Support	Support	Support	Support	Acceptance
Proposition 5	Support	Support		Support	Acceptance
Proposition 6			Support		Acceptance
Proposition 7	Conditional support				Minor revision
Proposition 8			Support		Acceptance
Proposition 9	Support				Acceptance
Proposition 10			Support		Acceptance
Proposition 11	Support				Acceptance
Proposition 12	Support		Support		Acceptance
Proposition 13	Support				Acceptance
Proposition 14			Support	Support	Acceptance
Proposition 15			Support	Support	Acceptance

As Table 11 shows, the empirical study supports the typology and the 15 propositions[169] but challenges the process of responding to threats which was presented in Figure 8. There may be criticisms against fully accepting 14 of the 15 propositions based on the empirical study. These may include that the propositions are general or that they leave room for interpretation. I can only partially agree with this criticism in that the only propositions which are general are the ones related to the nature of threat (i.e. Proposition 14 and Proposition 15). All other propositions, in my opinion, are specific in terms of the linkages between the variables. I agree that there is room for interpretation or rather the judgment of the researcher in analyzing the events with respect to the propositions. This is due to the nature of the variables and the applied methodology. I paid on the other hand utmost attention to minimize such interpretation, and I would disagree that the acceptance of the propositions is due to the nature of the propositions. In my opinion, the key reason why a majority of the propositions found support from the events is that the propositions are based on strong theoretical foundations, and the fact that the propositions cannot be falsified adds to the strength of the developed theory (cf. Popper 1979).

The empirical study suggests at least four areas to improve the theory. The major area for improvement is the process of responding to threats which requires better thinking of temporal links between the three types of contributions, i.e. longitudinal theory development. This need came out as the VW law event challenged the model presented in Figure 8. Related to this there is also need to integrate into the theory coalition-building among the firm and its primary stakeholders during efforts to shape the threat at source, i.e. at EU regulatory organizations. This insight came out from the VW law event, the 13th EU directive event, and the BER 1400/2002 event.

A second important area to consider in improving the theory is the acknowledgement that despite the fact that they are elements of a system the firm and its primary stakeholders pursue individual interests. As a result, some of the powerful actors in the system may behave opportunistically as observed in the VW law event and the BER 1400/2002 event. As it happened in the BER 1400/2002 event, such opportunistic behavior may lead to sacrifices from primary stakeholders. This needs to be incorporated into the theory with a new proposition. Related to this area, I should also bear in mind that the willingness to contribute and power are dynamic concepts.

Thirdly, the comparison of the VW law event and the 13th EU directive event showed that legal rights and legitimacy are the most important

[169] Except for Proposition 7 which requires minor revision.

determinants to shape the threat at the source of EU regulatory organizations. I need to incorporate this into the theory with a new proposition.

Fourthly, the single market and VW event and the BER 1400/2002 event provided insight that owned resources, accessible resources and legal rights are all important sources of power for firms to realize compensation-related sacrifices. By legal rights I mean here regulations governing relationships between the firm and its primary stakeholders. These need to be integrated into the theory with three new propositions.

Finally, I should discuss in the theory whether power resides in organizations or individuals such as Ferdinand Piëch and Jürgen Strube (see the 13th EU directive event) and also differentiate between temporary and permanent compensation-related sacrifices (see the single market and VW event).

This concludes the empirical study which clearly indicated the need for improving the theory. I respond to this challenge in the next chapter.

6 IMPROVING THE THEORY WITH THE AID OF THE EMPIRICAL STUDY

The empirical study in the previous chapter indicated that there was room for improvement of the theory. As reported in this chapter, I accomplished that in two ways. First, I improved the theory longitudinally to reflect temporal connections between the three types of contributions during the process of responding to threats. Secondly, I extended the theory regarding the key determinants of the importance of stake and power with five propositions. Finally, I benefited from the scheme[170] developed for predicting likely contributions of primary stakeholders and the pre-understanding of primary stakeholders in the car industry[171] and produced predictions concerning their likely contributions. These predictions show the ways in which various primary stakeholders can contribute to resolving the threats of market integration in the EU and thus answer research question 1.

6.1 The Process of Responding to Threats

Research question 1 asked for the ways various types of primary stakeholders can contribute to resolving the threats arising from market integration in the EU. To help answer that question I had derived a typology[172]. This typology maintained its validity in the light of the empirical study. In other words, I did not encounter a contribution which I would not be able to classify into the typology which consists of the following three types of primary stakeholder contributions.

1. *Type-I: Shaping the threat at source.* A primary stakeholder can shape the threat at source and perhaps eliminate it before it materializes. Examples of this kind of contribution are the lobbying of EU regulatory organizations and the blocking of new legislation that threatens the firm and its primary stakeholders (e.g., the 13th EU directive event).

170 See section 2.8.
171 See sections 4.5 and 4.6.
172 See section 2.6.

2. *Type-II: Adaptation within the system: shaping the firm or the conditions in the system.* In the event of a threat, the system may also need to adapt. In this type of contribution the primary stakeholder shapes the firm or certain conditions in the system. As a result, the threat and its negative impacts on the system can be avoided to a large extent (e.g., Porsche's contribution in the VW law event).
3. *Type-III: Adaptation within the system: compensation-related sacrifices or increased input.* This type of contribution occurs if the threat hurts the firm's profits (e.g., the single market and VW event) or if the executive managers of the powerful firm benefit opportunistically (e.g., the BER 1400/2002 event). In both cases the executive managers demand contributions from primary stakeholders. These may be in the form of compensation-related sacrifices (e.g., employee layoffs or reductions in suppliers' prices or dealer commissions) or increased input (e.g., an increase in capital or additional investments).

In the process of responding to threats the theory assumed that following perception of a threat and sense making about its likely outcomes a first strategic response would be to try to shape the threat at source before initiating adaptation[173]. The VW law event showed that this need not be the case. The event showed that in reality contributions to adapt within the system by shaping the firm or conditions in the system can be initiated much earlier when a potential threat is envisioned, and efforts for both types of contributions can run in parallel (see Figure 21).

[173] See Figure 8 in section 2.6.

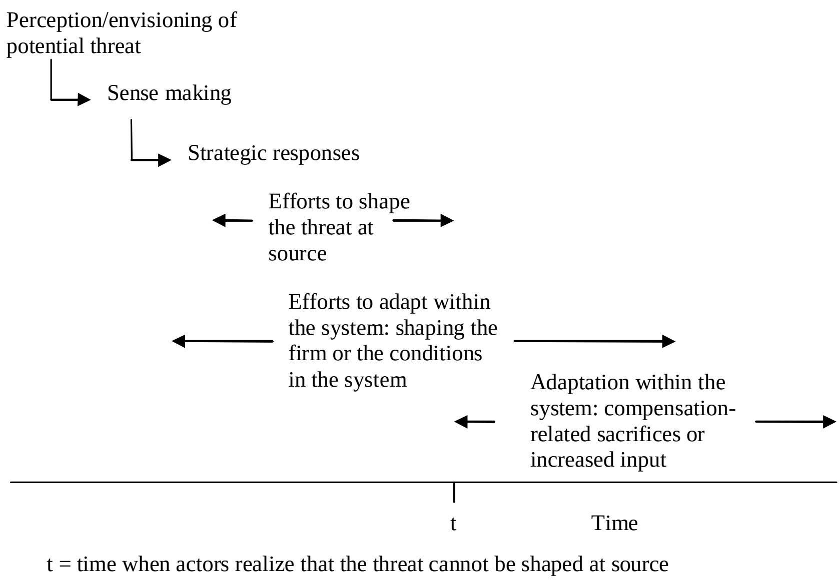

Figure 21. The revised model on the process of responding to threats

According to the revised model a strategic response in the form of a contribution of ‘adaptation within the system: shaping the firm or conditions in the system’ could occur not only after perception of a threat (e.g., VW management efforts to find strategic partners in the VW law event) but also after envisioning of a possible threat in the future (e.g., the passing of the VW law). Efforts for this type of contribution could run parallel to efforts to shape the threat at source, or they could start when it becomes clear that efforts to shape the threat at source are failing (e.g., Porsche’s purchase of VW shares in the VW law event).

Efforts to shape the threat at source may occur in terms of lobbying EU regulatory organizations and trying to influence the outcome in their favor. In so doing firms (including industry associations) and their primary stakeholders can collaborate and build up a coalition. In the 13th EU directive event it was initially the industry associations and trade unions that lobbied against the threat, and later they managed to get the German government into their coalition as well (see Figure 22).

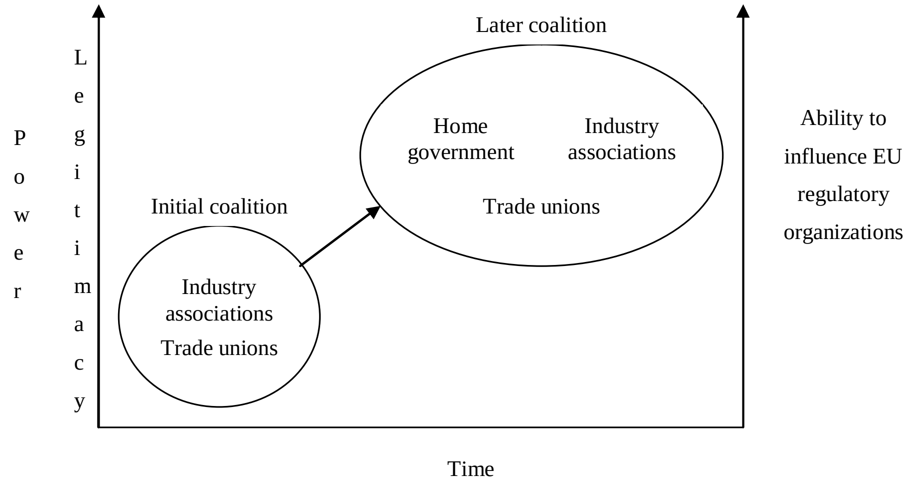

Figure 22. Coalition-building in the 13th EU directive event

Coalition building increases the power and legitimacy of the lobbying actors and the ability to shape the threat at source (see Figure 22). In coalition building it is therefore important to ensure the willingness of powerful primary stakeholders to contribute. In this event, the German government played the key role in lobbying members of the European Parliament, thereby shaping the threat at source. This kind of act was also observed in the BER 1400/2002 event when national dealer associations wrote letters to their home governments in the expectation of gaining support for lobbying against the new regulation.

A critical point in time is when it becomes clear that the threat cannot be shaped at source (i.e. time t in Figure 21). When it is evident that the threat is likely to occur, then we may see opportunistic behaviors from the more powerful actors in the system. In the VW law event Porsche started to acquire VW shares after the court case against the VW law started, and it increased its shares to above 30 percent, the threshold level for gaining control. As it did so, Porsche changed its ambitions from protecting its stake in VW to gaining control of it in time and even lobbied for the speeding up of the court process. A more severe situation occurred in the BER 1400/2002 event when BER 1400/2002 was adopted. Many car manufacturers used the opportunity to rationalize their dealer networks by terminating their unsatisfactory dealers and reducing the margins for all of the others. These observations together with premises from general systems theory lead me to develop a model of systemic behavior in time (see Figure 23).

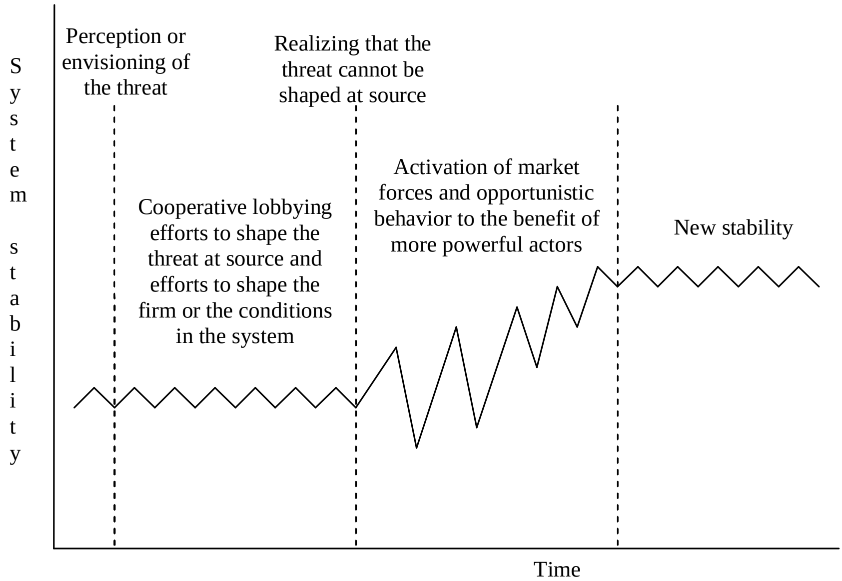

Figure 23. A model of systemic behavior in time

General systems theory stipulates that elements of a system tend to be in some kind of stability or equilibrium (Von Bertalanffy 1974; Henderson 1970; Katz and Kahn 1978). When the system experiences perturbation from the outside, the elements try at first to resist the perturbation. Cooperation among them strengthens this resistance. In line with these thoughts I argue that when a threat is perceived or envisioned, the firm and its primary stakeholders collaborate to defend the status quo. This may be in the form of cooperative lobbying efforts to shape the threat at source as was the case in the VW law event, the 13th EU directive event, and the BER 1400/2002 event. It may also be in the form of attempts to shape the firm or the conditions in the system with the purpose of adapting within the system so that the negative effects of the threat can be avoided (e.g., the VW law event). During this period I consider the system of the firm and its primary stakeholders to be in a stable state (see Figure 23).

General systems theory further stipulates that when some kind of perturbation destabilizes the system by a small amount, the elements will tend to move back towards stability (Katz and Kahn 1978, 26–27). This type of system behavior is called dynamic homeostasis (or dynamic equilibrium). If the displacement is so that the old form of stability can no longer be achieved, then the elements seek a new form. Applying this to the model, I argue that when it becomes clear that the threat cannot be shaped at source, there is possibility that market forces are activated and cooperation among system elements may give way to opportunistic behaviors. It seems that the activation of market forces benefits the more powerful actors in the system. In the VW law event it was Porsche that took the opportunity to gain control of VW. In the BER 1400/2002 event it was the car manufacturers that used the opportunity to rationalize their dealer networks.

The latter case resulted in contributions from dealers in the form of compensation-related sacrifices and increased input. In my opinion, this type of contribution occurs only after it is realized that the threat can not be shaped at source. This is because it is the least desired from the primary stakeholders' point of view as it demands sacrifices. This would occur in two situations: necessity resulting from decrease in the firm's profits (e.g., the single market and VW event) or opportunistic behavior of powerful actors in the system (e.g., the BER 1400/2002 event).

Compensation-related sacrifices could be temporary or permanent. Temporary sacrifices occur when the firm's profits decrease during the course of the threat. For example, lower profit for the firm implies lower corporate taxes for the home government and lower dividends for shareholders. These are temporary sacrifices because if the firm profits return to normal levels following the threat, the need for sacrificing is also over.

Permanent sacrifices are mostly subject to compromise between the firm and its primary stakeholders. The primary stakeholders need to be convinced to make such sacrifices. This may be achieved following tough negotiations (e.g., employee contributions in the single market and VW event) or enforced by power (e.g., dealer contributions in the BER 1400/2002 event). Key target primary stakeholders for permanent sacrifices are suppliers and employees in the automotive industry because raw-materials and labor are key cost items. A crisis eases the firm management's task by adding legitimacy and also a sense of urgency to the request for this type of contribution.

This section has improved understanding as to how the three types of primary stakeholder contributions may occur in time. In the next section I further improve the theory regarding the determinants of the types of contributions.

6.2 Determinants of the Types of Primary Stakeholder Contributions

In reply to research question 2 I had presented a set of determinants under 15 propositions following literature review[174]. In this set, the importance of stake and power were key determinants, and the nature of the threat played a moderating role. The empirical study suggested the acceptance of the

[174] See Figure 13 in sub-section 2.7.3.

propositions as well as adding five new propositions[175]. In the following sub-sections I discuss these in the light of the empirical study.

6.2.1 The Importance of Stake

As worded in Proposition 1 and Proposition 2 and drawn from the descriptive stream of stakeholder theory (cf. Mitchell et al. 1997), a primary stakeholder needs to be willing to contribute, and this is determined by the importance of its stake in the firm.

P1. Given that it has the power, a primary stakeholder is more likely to shape the threat at source, or shape the firm or the conditions in the system in case of a threat if the importance of its stake is high.

P2. Even though it has the power, a primary stakeholder is less likely to shape the threat at source, or shape the firm or the conditions in the system in case of a threat if the importance of its stake is low.

In contributions to shape the threat at source or to shape the firm or the conditions in the system, willingness refers to the desire to initiate efforts to contribute. These two propositions were supported by the VW law event and the 13th EU directive event in that the contributing powerful primary stakeholders had highly important stakes, and no powerful primary stakeholder with stake of low importance contributed.

In contributions of compensation-related sacrifices or increased input, willingness refers to the involuntary acceptance to sacrifice. Such acceptance is involuntary because sacrificing from compensation is not a desired act. This kind of situation arises either from an economic necessity (i.e. a situation which hurts the firm’s profits) or from opportunistic behavior of powerful actors as seen in the BER 1400/2002. The former supports Proposition 3, which was drawn from the descriptive stream of stakeholder theory (cf. Mitchell et al. 1997), and the latter is formulated in a new proposition, i.e. Proposition 16.

P3. Primary stakeholders with highly important stakes are likely to make compensation-related sacrifices or increased input if the situation arises from an inevitable economic necessity.

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[175] Only Proposition 7 needed minor revision. See section 5.6.

P16. Primary stakeholders with highly important stakes and low power are likely to make compensation-related sacrifices or increased input if the situation arises from opportunism.

As worded in Proposition 4 and Proposition 5 based on the work of Mitchell et al. (1997), the importance of the stake is a function of the compensation from the firm and relationship-specific investments.

P4. The amount of compensation earned from the firm increases the importance of the primary stakeholder's stake in the firm.

P5. The relationship-specific investments of the primary stakeholder increase the importance of its stake in the firm.

All four events provided support for Proposition 4, and there was evidence in the VW law event, the single market and VW event, and the BER 1400/2002 event for Proposition 5. The empirical study did not reveal any other determinant for the importance of stake. Therefore, I maintain this part of the theory.

6.2.2 Power

According to the theory the primary stakeholder's willningness is not sufficient to realize contributions to shape the threat at source or to adapt within the system by shaping the firm or the conditions in the system. The primary stakeholder needs to be able to do such contributions, and this relies on its power. Power is considered in this research as a relationship-specific concept (Emerson 1962). Thus, in contributions to shape the threat at source it refers to the power of the primary stakeholder to influence EU regulatory organizations, and in contributions to adapt within the system by shaping the firm or the conditions in the system it refers to the power of the primary stakeholder in relation to the other actors in the system. These thoughts lead to Proposition 6 and Proposition 7.

P6. Given that a primary stakeholder has a highly important stake in the firm, it will shape the threat at source if it has the power to influence the source of the threat.

This proposition was supported by evidence from the 13th EU directive event. As the event showed, the home government is the most powerful primary stakeholder to realize this type of contribution, and it requires efforts by other primary stakeholders to build a coalition including the home government.

P7. Given that a primary stakeholder has a highly important stake in the firm, it will accomplish adaptation within the system by shaping the firm or the conditions in the system if it has the power to influence the system.

This proposition was supported in the VW law event by the act of Porsche. Porsche had a highly important stake in VW in that VW supplied 24 percent of its material purchases (i.e. high compensation), and it was also an important partner in technology development (i.e. high relationship-specific investments).

I had identified three sources of power drawing from the descriptive stream of stakeholder theory (cf. Kochan and Rubinstein 2000), the resource dependence perspective (cf. Pfeffer and Salancik 1978), the network perspective (cf. Brass and Burkhardt 1993), and literature on power (cf. Stinchombe 1968; Mintzberg 1983): owned resources, accessible resources, and legal rights and legitimacy. These were reflected in Propositions 8–13.

P8. The owned resources of the primary stakeholder increase its power to influence the source of the threat.

P9. The owned resources of the primary stakeholder increase its power to influence the system.

P10. The accessible resources of the primary stakeholder increase its power to influence the source of the threat.

P11. The accessible resources of the primary stakeholder increase its power to influence the system.

P12. The legal rights and legitimacy of the primary stakeholder increase its power to influence the source of the threat.

P13. The legal rights and legitimacy of the primary stakeholder increase its power to influence the system.

Proposition 8 and Proposition 10 were supported by the 13th EU directive event. Resources are needed for lobbying EU regulatory organizations. Coalition building among the firm and its primary stakeholders provides a means of increasing power by generating resources for lobbying. Having more resources, however, does not necessarily guarantee the ability of the coalition to succeed in shaping the threat at source. In my opinion, the coalition in the VW law event consisting of the VW management and stakeholders such as the Land of Lower Saxony, the German government, and trade unions did not fail due to lack of resources to lobby for the VW law: it failed because it lacked the legal basis of a legitimate claim in defending it.

Proposition 9 and Proposition 11 were supported by the VW law event as Porsche's power to acquire VW shares stemmed from the financial resources it owned, and which it could access due to its outstanding financial performance.

Proposition 13 was supported by the VW law event. The legitimacy of the primary stakeholder in the eyes of the firm's management and the other primary stakeholders is important in contributions via shaping the firm or the conditions in the system. If the contribution is not perceived as legitimate, the firm's management or a coalition of actors in the system may attempt to prevent a particular primary stakeholder from realizing this kind of contribution. In the VW law event primary stakeholders, in particular the government of the Land of Lower Saxony, the trade union and the German government, opposed a takeover by hedge funds because they feared its consequences: the hedge fund might break down VW into its brands and sell them separately, or close plants in Germany and move production abroad. The same primary stakeholders welcomed Porsche's acquisition of VW shares because in their eyes Porsche was a strategic partner and would not attempt such acts that would endanger the interests of other primary stakeholders. We could say that Porsche had legitimacy in the eyes of the VW management and other primary stakeholders in the system.

Proposition 12 was supported by both the VW law event and the 13th EU directive event. The events showed that the key source of power over EU regulatory organizations lies in finding legitimate claims. In the 13th EU directive event, the coalition against the 13th EU takeover directive was able to convince members of the European Parliament because they argued that the new regulation would bring unfair competition both within the EU and against the USA. These were against what the European Commission wanted to achieve, which was fair competition. In the VW law event, however, the coalition failed since there was not any legitimate basis to defend the VW law. These observations lead me to put forward a new proposition, i.e. Proposition 17.

P17. Legal rights and legitimacy are the most influential determinants of the power to influence EU regulatory organizations and to shape threats at source.

In contributions of adaptation within the system via shaping the firm or the conditions in the system, all three determinants of power seemed to be equally important, and they are already worded in Proposition 9, Proposition 11, and Proposition 13.

In contributions of adaptation within the system via compensation-related sacrifices or increased input, again all three determinants of power seemed to be important. In this type of contribution power refers to the relationship between the firm and its primary stakeholders. The power of car manufacturers to extract permanent sacrifices from unwilling dealers in the BER 1400/2002 event stemmed from their control of key resources (e.g., technical information and equipment) and their legal rights (e.g., to terminate dealer contracts with advance notice). In the single market and VW event, VW was able achieve discounts on raw-material prices from its suppliers by forcing them into a bidding competition with global suppliers. Thus, VW's power stemmed from the availability of global resource alternatives (i.e. accessible resources). These observations lead me to make Proposition 18, Proposition 19, and Proposition 20.

P18. The owned resources of the firm increase its power to realize contributions from its primary stakeholders in the form of compensation-related sacrifices or increased input.

P19. The accessible resources of the firm increase its power to realize contributions from its primary stakeholders in the form of compensation-related sacrifices or increased input.

P20. The legal rights and legitimacy of the firm increase its power to realize contributions from its primary stakeholders in the form of compensation-related sacrifices or increased input.

An interesting aspect of the 13th EU directive event was that some individuals played key roles in the success of the lobbying efforts: it was Ferdinand Piëch and Jürgen Strube who influenced Gerhard Schröder. This raises the question as to whether power is rooted in individuals or in organizations. It would be wrong to accept the former and to deny the latter. The powers of Mr. Piëch and Mr. Strube came from the fact that they were leading the largest firms in Germany in their industries. It would also be wrong not to recognize the roles of influential individuals and their connections. Mr. Schröder had been the Minister President of the Land of Lower Saxony, and served on the Supervisory Board of VW when Mr. Piëch was the CEO. Therefore, they knew each other quite well. I thus conclude that power rests with organizations, but influential individuals may use it more efficiently in their lobbying efforts through their personal connections. This conclusion does not necessitate formulation in a new proposition.

6.2.3 The Nature of Threat

As shown in Proposition 14 and Proposition 15 I drew from the descriptive stream of stakeholder theory (cf. Savage et al. 1991; Rowley and Berman 2000; Lozano 2005) and argued that the nature of the threat played a moderating role in determining which primary stakeholders would be willing to and which ones would be able to contribute.

P14. The nature of the threat determines which of the primary stakeholders will be willing to make a contribution.

P15. The nature of the threat determines which of the primary stakeholders are able to make a contribution.

Both propositions found support from evidence in the 13th EU directive event and the BER 1400/2002 event. In the former event it was employees who were the most exposed to the negative effects of takeovers. Thus, it was the employee representatives, i.e. the trade unions, which first lobbied strongly against the proposal. Likewise, the scope of the latter event concerned mainly dealers.

Perhaps the nature of the threat also played a role in the outcome. It seems that the chances of influencing EU regulatory organizations are higher during the process of legislation making (e.g., the 13th EU directive event) than in the revising of existing legislation (e.g., the BER 1400/2002 event) or in attempts to defend violation of EU law (e.g., the VW law event). In the case of completely new legislation, the European Commission is itself open to inputs from all stakeholders. Besides, the co-decision procedure necessitates the approval of the Council of Ministers and the European Parliament. The implication is that there is more time for lobbying efforts and that there are a number of stages at which a contribution to shape the threat at source can be made. In the analysis I used scope of the threat and the source of the threat as properties for the nature of the threat. Unfortunately, data from the four events was not sufficient to improve the theory further along this direction.

I present in Figure 24 the revised model of determinants of the types of contributions with 20 propositions.

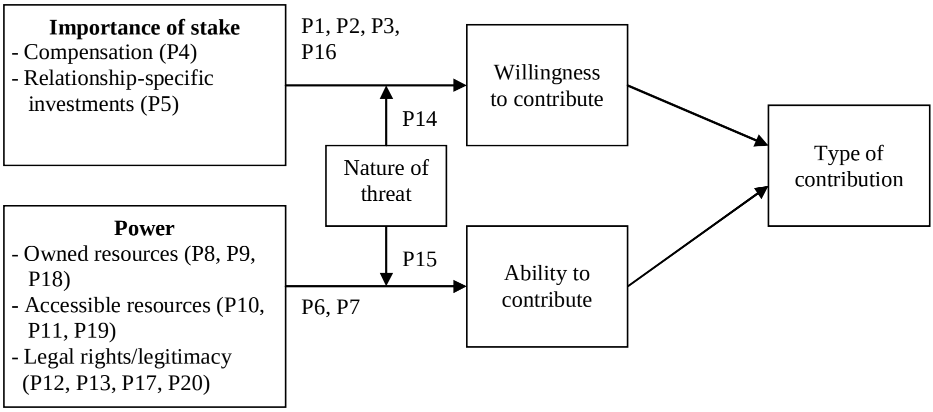

Figure 24. The revised model of determinants of the types of primary stakeholder contributions

This set of 20 propositions provides the answer to research question 2. I make in the next section predictions regarding the likely contributions of various types of primary stakeholders. Those predictions aim not only to show the predictive capacity of the theory but also to answer research question 1.

6.3 The Likely Contributions of Various Primary Stakeholders

In the theory I had developed a scheme for predicting primary stakeholder contributions[176]. This scheme preserved its validity in the light of the empirical study. In this section I will use that scheme and predict likely contributions of various kinds of primary stakeholders including principal shareholders, employees, customers as end-users, business-to-business customers, suppliers, dealers, creditors, and the home government. The scheme demanded the assessment of the importance of the stake and power. I accomplish that in the following sub-sections based on the understanding about these primary stakeholders from the review of literature on the EU car industry[177].

[176] See section 2.8.
[177] See sections 4.3, 4.4, 4.5, and 4.6.

6.3.1 Assessment of the Importance of Stake

The importance of stake hints at the willingness to contribute: the higher the stake, the more willing is the primary stakeholder to make a contribution. As stipulated in the theory, it is of high importance when the primary stakeholder has high relationship-specific investments and/or high compensation from the firm.

Principal shareholders[178] have highly important stakes in the firm in that they have considerable relationship-specific investments (e.g., paid-in-capital and long-term commitment), and the compensation is highly significant because it is the return on their investment. They would therefore be willing to contribute to the resolution of threats.

Employees also have highly important stakes in the firm: their investments are highly relationship-specific in that they give their efforts and time to the firm, and their compensation is their primary means of living. Therefore, I assess that they would also be willing to contribute to the resolution of threats.

The stakes of end-users in a car manufacturer are low in importance because of increasing resource alternatives thanks to competition. Besides, in purchasing and owning a car the end-user does not make much of a relationship-specific investment: it is relatively easy to sell an old car and to buy a new one. Therefore, I argue that customers as end-users would not be willing to contribute.

Business-to-business customers of a car manufacturer may have highly important stakes in a car manufacturer if the technology or resource they are purchasing is of high importance to them and if there are no alternative suppliers. Therefore, they may have stakes of high or low importance, and those with high importance would be willing to contribute.

Suppliers are highly dependent on car manufacturers because there is no other outlet for their products (i.e. significant compensation), and they need to make relationship-specific investments in conducting business. As a result, their stakes in car manufacturers are highly important to them, and they would be willing to contribute.

Dealers earn their compensation through car sales and repair & maintenance. In addition, they make relationship-specific investments in order to conduct business with car manufacturers. As a result, they also have highly important stakes in car manufacturers and thus would be willing to make a contribution.

[178] I limited the selection to principal shareholders because there can be a variety of minority shareholders, making it difficult to generalize.

Creditors are banks that are among the world’s largest corporate organizations. Their core business is in financial operations, and they have a variety of customers from all industries. Their main concern when giving loans is to protect themselves against the risk of bad debts (i.e. customers not being able to pay back their loans). They often achieve this by taking guarantees from their customers in amounts that more than cover the loans. They therefore do not need to make relationship-specific investments in any of their customers. Given the wide portfolio of customers and the need to safeguard against risks, I would conclude that the stakes of banks in car manufacturers are low in importance, and thus they would not be willing to contribute.

Finally, a car manufacturer is highly important to its home government because it is a significant source of taxes and a provider of employment (i.e. increased societal welfare). The home government need not make any relationship-specific investment, but the compensation is high. It therefore has a highly important stake in the car manufacturer and would be willing to make a contribution.

Based on the above assessments I place the above discussed primary stakeholders in the scheme of the importance of stake (See Table 12).

Table 12. The importance of stake for varous primary stakeholders

		Relationship-specific investments	
		High	Low
Compensation	High	Stake is highly important Principal shareholders Employees Suppliers Dealers	Stake is highly important Business-to-business customers with high compensation Home government
	Low	Stake is highly important	Stake is not so important Customers as end-users Business-to-business customers with low compensation Creditors

6.3.2 Assessment of Power

According to the theory power indicates the ability to contribute and thus the type of contribution. A primary stakeholder with power to influence the source of the threat is able to shape the threat at source, and one with power to influence the system is able to shape the firm or the conditions in the system. Power of a certain type exists if the primary stakeholder owns or has access to key resources, or when it has legal rights and legitimacy. In the assessment of power I consider only those primary stakeholders that have highly important stake in the firm because others are not willing to contribute.

Based on the review of lobbying in the EU regulatory organizations and the events, I would argue that only the home government has the power to shape a threat at EU regulatory organizations on its own. All other primary stakeholders need to build a coalition and also include the home government in order to achieve this type of contribution. The power of the home government has a legitimate base in that the governments are represented directly at the Council of Ministers. Besides, members of the European Parliament usually have a background in national politics and thus have connections with their home governments.

Principal shareholders have the legal right to shape the firm through representation on the Board of Directors and through their decisions at general shareholders' meetings. In Germany, however, power arising from this legal right is somewhat limited, especially in firms with more than 2,000 employees, in which the Supervisory Board comprises equal numbers of shareholder and employee representatives. Still, the balance of power is with the shareholders because the chairman of the Supervisory Board, who is one of their representatives, has two votes in case of a tie. Therefore, I argue that principal shareholders have the power to shape the firm or the conditions in the system.

Employees are legally empowered in German firms to participate in the firm's decision-making process. However, even in firms with more than 2,000 employees they need to gain the approval of the shareholder representatives on the Supervisory Board in order to take action. Therefore, I argue that employees lack the power to shape the firm or the conditions in the system on their own.

Business-to-business customers with highly important stake include mostly other car manufacturers. I argue that car manufacturers, which are among the largest MNEs in the world, are powerful actors with the resources to shape the firm or the conditions in the system.

I also believe that in the buyer-dominated automotive industry suppliers lack the resources to shape car manufacturers or the conditions in the system. This also holds true for dealers which are mostly SMEs.

Some home governments in the EU shaped the conditions in the system in the car industry until the 1990s by setting quotas for Japanese imports and providing state aid. Under the single market program they are not allowed to interfere in business in any way that disturbs fair competition. Despite these limitations, home governments can shape the conditions in the system through adjusting taxes as well as making legislation in the country. Thus, I argue that home governments have the power to shape the firm or the conditions in the system.

6.3.3 The Predictions

Having assessed different types of primary stakeholders in terms of the importance of their stakes and their powers, I can predict what would be their likely contributions with the aid of the scheme developed in Table 5[179].

Prediction 1. In the case of a threat from market integration in the EU, principal shareholders are not likely to shape it at source on their own by lobbying EU regulatory organizations.

This prediction is based on the assessment that despite their highly important stakes principal shareholders (except if they are simultaneously home governments) lack the power to influence EU regulatory organizations on their own.

Prediction 2. In the case of a threat from market integration in the EU, principal shareholders are likely to realize adaptation within the system by shaping the firm.

This prediction is based on the assessment that principal shareholders have the power to influence the firm via the Board of Directors.

Prediction 3. Principal shareholders may need to make compensation-related sacrifices if the profits of the firm are hurt by the threat.

This proposition is based on the fact that shareholders earn their compensation annually in the form of dividends from the profits of the firm. When the firm’s profits are hurt, shareholders make compensation-related sacrifices. These sacrifices are usually temporary.

Prediction 4. In the case of a threat from market integration in the EU, employees are not likely to shape it at source on their own by lobbying EU regulatory organizations.

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179 See section 2.8.

This prediction is based on the assessment that despite their highly important stakes employees lack the power to influence EU regulatory organizations on their own.

Prediction 5. In the case of a threat from market integration in the EU, employees are not likely to realize adaptation within the system by shaping the firm or conditions in the system.

This prediction is based on the assessment that despite their highly important stakes employees lack the power to shape the firm or the conditions in the system.

Prediction 6. Employees may need to make compensation-related sacrifices if the profits of the firm are hurt by the threat.

Employees in the labor-intensive car industry represent a key target for cost savings when sales drop. Managers of car manufacturers lay off workers in order to decrease fixed costs. This is not so easy in Germany, however, because such decisions need to be approved by the Supervisory Board, half of which comprises employee and trade-union representatives. There would definitely be a power struggle: employees would fight to preserve their status, but they would also have to compromise by making compensation-related sacrifices if the threat necessitates it. These sacrifices are usually permanent.

Prediction 7. In the case of a threat from market integration in the EU, customers as end-users are not likely to shape it at source on their own by lobbying EU regulatory organizations.

Prediction 8. In the case of a threat from market integration in the EU, customers as end-users are not likely to realize adaptation within the system by shaping the firm or some conditions in the system.

Prediction 9. Customers as end-users do not need to make sacrifices if the profits of the firm are hurt by the threat.

Predictions 7, 8, and 9 are based on the assessment that customers as end-users have stakes of low importance in the firm. Indeed, customers as end-users benefit from increased competition resulting from market integration in the EU.

Prediction 10. In the case of a threat from market integration in the EU, business-to-business customers are not likely shape it at source on their own by lobbying EU regulatory organizations.

This prediction is based on the assessment that business-to-business customers lack the power to influence EU regulatory organizations on their own.

Prediction 11. In the case of a threat from market integration in the EU, business-to-business customers with highly important stakes are likely to realize adaptation within the system by shaping the firm or the conditions in the system.

This prediction is based on the assessment that business-to-business customers with highly important stakes are mostly other car manufactures which have resources to shape the firm or the conditions in the system.

Prediction 12. Business-to-business customers with highly important stakes may need to sacrifice as increased input if the firm's profits are hurt by the threat.

In my opinion, when threats severely hurt the profits of the firm a business-to-business customer with a highly important stake would accept a reasonable price-increase demand given the importance of the resource and the lack of alternative suppliers.

Prediction 13. In the case of a threat from market integration in the EU, suppliers are not likely to shape it at source on their own by lobbying EU regulatory organizations.

This prediction is based on the assessment that despite their highly important stakes suppliers lack the power to influence EU regulatory organizations on their own.

Prediction 14. In the case of a threat from market integration in the EU, suppliers are not likely to realize adaptation within the system by shaping the firm or conditions in the system.

This prediction is based on the assessment that despite their highly important stakes suppliers lack the power to shape the firm or the conditions in the system.

Prediction 15. Suppliers may need to make sacrifices in the form of decreased compensation or increased input when the firm’s profits are hurt by the threat or when the firm’s executive managers realize an opportunity.

This prediction is based on the assessment that suppliers constitute a target for cost savings in the face of threats that significantly damage the profits of car manufacturers. Besides, as the review of previous studies shows, car manufacturers can also play suppliers against each other in order to obtain price discounts.

Prediction 16. In the case of a threat from market integration in the EU, dealers are not likely to shape it at source on their own by lobbying EU regulatory organizations.

This prediction is based on the assessment that despite their highly important stakes dealers lack the power to influence EU regulatory organizations on their own.

Prediction 17. In the case of a threat from market integration in the EU, dealers are not likely to realize adaptation within the system by shaping the firm or some conditions in the system.

This prediction is based on the assessment that despite their highly important stakes dealers lack the power to shape the firm or the conditions in the system.

Prediction 18. Dealers may need to make compensation-related sacrifices when the firm faces a threat that hurts its profits or when the firm’s executive managers realize an opportunity.

This prediction is based on the fact that dealer compensation is related to car sales, and it includes performance bonuses from car manufacturers. When profits of the firm are hurt or when an opportunity comes up, executive managers of car manufacturers may demand a compensation-related sacrifice in the form of bonus reduction. This may be a permanent sacrifice.

Prediction 19. In the case of a threat from market integration in the EU, creditors are not likely to shape it at source on their own by lobbying EU regulatory organizations.

Prediction 20. In the case of a threat from market integration in the EU, creditors are not likely to realize adaptation within the system by shaping the firm or some conditions in the system.

Prediction 21. Creditors do not need to make sacrifices when the firm faces a threat that hurts its profits.

Predictions 19, 20, and 21 are based on the assessment that creditors have stakes of low importance in the firm. Actually, when the threat is to their profits, car manufacturers have an additional need for financing. Therefore, creditors benefit in such situations because they sell additional loans.

Prediction 22. In the case of a threat from market integration in the EU, the home government is likely to shape it on its own by lobbying EU regulatory organizations if the firm under threat is of high importance to it.

This prediction is based on the assessment that home governments have the power to influence EU regulatory organizations.

Prediction 23. In the case of a threat from market integration in the EU, the home government is likely to realize adaptation within the system by shaping the conditions in the system if the firm under threat is of high importance to it.

This prediction is based on the assessment that home governments have the power to shape the conditions in the system.

Prediction 24. The home government may need to make a compensation-related sacrifice when the firm faces a threat that hurts its profits.

This prediction is based on the fact that home-government compensation rests on corporate taxes on profit. Such sacrifice is temporary.

Table 13 summarizes the likely contributions of the different types of primary stakeholders in the car industry by citing their related prediction numbers.

Table 13. The likely contributions of various primary stakeholders in the car industry

Primary stakeholder	Shaping the threat at source	Shaping the firm or the conditions in the system	Compensation-related sacrifices or increased input
Principal shareholders		Prediction 2	Prediction 3
Employees			Prediction 6
Customer as end-users			
Business-to-business customers with highly important stake		Prediction 11	Prediction 12
Suppliers			Prediction 15
Dealers			Prediction 18
Creditors			
Home governments	Prediction 22	Prediction 23	Prediction 24

According to this, the home government is the most influential primary stakeholder in terms of shaping the threat at source or shaping the conditions in the system. No other primary stakeholder would be likely to shape the threat at source on its own, and principal shareholders and business-to-business customers with highly important stakes are the only other primary stakeholders which would be likely to shape the firm or conditions in the system. All primary stakeholders except for customers as end-users and creditors would make compensation-related sacrifices or increased input if needed. This provides the answer to research question 1 and ends the improving of the theory. The conclusions from the research are presented in the next chapter.

7 CONCLUSIONS

This chapter discusses the theoretical contributions, limitations and policy implications, and suggests further research avenues.

7.1 Theoretical Contributions and Limitations

This research contributes primarily to the descriptive stream of stakeholder theory in demonstrating that a firm's primary stakeholders can and do contribute to resolving the threats of market integration in the EU, and by increasing the theoretical understanding of how they can do so. More specifically, the key contribution of this research is a theory which helps us to explain observed primary stakeholder contributions as well as predict future ones. This research differs from earlier research in the following ways:

First of all, it integrates strategic choice, collective action, and contingency perspectives into the literature on stakeholders. This is a contribution in that so far only collective action has been used in tandem with stakeholder theory (cf. King 2008). In my opinion, this is also a contribution to the strategic-management literature because much of the earlier research on strategic responses to the environment takes the firm's perspective and does not look into what stakeholders can do in the responses.

Secondly, it contributes further to the strategic management literature by achieving some degree of integration among the strategic choice, collective action, and contingency perspectives while recognizing their distinctive attributes. This is a contribution given the scarcity of efforts to achieve a more complete theoretical foundation for managerial decision-making (Sanchez 2003).

Thirdly, it tackles a crucial topic of international business, namely market integration in the EU, and thus contributes to that literature (cf. Eden and Lenway 2001; Buckley 2002; Buckley and Ghauri 2004).

Fourthly, it takes a longitudinal approach and studies strategic responses as a process over a long period beginning in 1960. This kind of historical approach is rare in business studies (cf. Jones and Khanna 2006), and such process-oriented research is highly needed to advance the descriptive stream of stakeholder theory (cf. Derry and Waikar 2008; Zietsma and Winn 2008).

Fifthly, it adopts a systems perspective. This is new in that most of the earlier research on stakeholders takes the perspective of the firm, and they view the firm and its stakeholders as a network (cf. Rowley 1997) or firm managers as agents of stakeholders (cf. Hill and Jones 1992).

Sixthly, it contributes further to the descriptive stream of stakeholder theory in differentiating between various types of primary stakeholders (cf. Harrison and Freeman 1999; Winn 2001). It is a contribution to show that different types of primary stakeholders contribute differently.

As a result of this research we understand better that when the European Commission takes market-integration initiatives promoting competition for the benefit of consumers, the more powerful actors in the system can also benefit at the expense of some of the less powerful primary stakeholders.

We also understand better that different determinants are important in different types of contributions in terms of resolving the threats of market integration in the EU. It is the legal rights and accompanying legitimacy that give primary stakeholders the power in lobbying EU regulatory organizations. When it comes to adaptation within the system, however, power stems equally from owned and accessible resources as well as legal rights and legitimacy. This finding is a contribution of this research to the current literature on stakeholders, which treats stakeholder attributes as constant in all circumstances (cf. Mitchell et al. 1997).

The results of this research also support the earlier finding that stakeholders have conflicting interests (cf. Freeman 1984; Hill and Jones 1992; Mitchell et al. 1997). This is shown in the empirical study in that the firm and its primary stakeholders prioritize their own interests, possibly even at the expense of the interests of other actors in the system. Despite that, it is also clear from this research that the interests of the firm and its primary stakeholders may change over time and even merge as in the case of fighting against a common threat, e.g., lobbying EU regulatory organizations.

Finally, the finding that primary stakeholders can and do play roles in resolving the threats of market integration is an important contribution to the discussion in the instrumental stream of stakeholder theory on the performance implications of stakeholder orientation. The evidence in this research supports the argumentation in terms of showing that primary stakeholders can contribute to firm survival. This is also a contribution to the descriptive stream because most of the literature which emphasizes the active behaviors of stakeholders is limited to those behaviors that target to influence the firm (cf. Frooman 1999; King 2008).

The findings of this research, however, are limited in at least four ways. First, they cover primary stakeholder contributions in the EU car industry. I had to impose such a limitation in order to be able to conduct a historical empirical study, and to gain in-depth understanding of the research context. This limitation raises the question about the extent to which the elements of the theory could be generalized to other contexts such as different regions or different industries. As I discussed in section 3.7, the only element of the theory which may be context-dependent is Proposition 17[180]. The typology and all other propositions are independent of context, and this makes transferability possible. The predictions could be different based on the attributes of importance of stake and power, but this is not against the theory or its transferability.

Secondly, although this research differentiates between various types of primary stakeholders, it overlooks the possibility of finding different behaviors within each group[181]. To avoid that I could have focused on a single group in the empirical study, but I did not do so because it would have limited me more in terms of finding an adequate number of contributions to cover the elements of the theory. To give an example, I would not have been able to find a case event for shaping the threat at source if I had focused only on dealers. In that case I would also have missed the whole picture from the eyes of different primary stakeholders.

Thirdly, this research is limited to threats connected with market integration. I deliberately excluded opportunities because modeling primary stakeholder behavior with regard to opportunities and threats simultaneously in the same piece of research would have been difficult.

Finally, secondary stakeholders are excluded, based on the assumption that they would not be willing to contribute because they do not earn compensation from the firm, and they do not have relationship-specific investments in it.

7.2 Managerial and Policy Implications

The implications of this research concern primary stakeholders, executive managers of firms, and policy makers at the European Commission.

Implications for primary stakeholders:

The theory facilitates the deduction of strategic policies for the primary stakeholders included in the research. In developing the strategies I left customers as end-users and creditors off from the list of primary stakeholders

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[180] In my opinion, also Proposition 17 could be transferable to all contexts where regulatory mechanisms function properly.

[181] Except for differentiating within shareholders (i.e. principal shareholders and minority shareholders) and customers (i.e. customers as end-users and business-to-business customers)

(see Table 14) because the importance of their stakes in the firm are low, and as discussed they are indeed likely to benefit from the threats.

From the perspective of primary stakeholders, the least desired type of contribution is related to lower compensation or increased input, which occurs after the realization of the threat event. Therefore, when there is a threat from EU regulatory organizations, primary stakeholders should focus on counteracting it before it occurs. There are two ways of doing this: lobbying EU regulatory organizations and preventing the threat-creating regulation from being adopted, or shaping the firm or the conditions in the system. Primary stakeholders differ in their powers on both counts (see Table 14).

Table 14. The powers of primary stakeholders with highly important stakes

Primary stakeholder	Power to lobby EU regulatory organizations	Power to shape the firm or the conditions in the system
Principal shareholders	Low	High
Employees	Low	Low
Business-to-business customers	Low	High
Suppliers	Low	Low
Dealers	Low	Low
Home government	High	High

Employees, suppliers, and dealers constitute the bulk of the primary stakeholders included in Table 14 in terms of numbers, but unfortunately they all lack both types of power. They are also the most vulnerable to sacrifices if the threat occurs. Since the more powerful actors can take advantage if the threat cannot be avoided, these three types of primary stakeholders need to concentrate their efforts on shaping the threat at source, in other words lobbying EU regulatory organizations. As they lack the power to do this on their own, the only viable strategy is to build a coalition and attract their home governments, the only actor with the power to influence these organizations, into the coalition. It is essential to know which regulatory organizations are involved in the threat-creating legislation and which channels to use in the lobbying: these could save resources. If it is legislation requiring the co-decision procedure for adoption, the European Parliament may be a key lobbying target, and the home government would be the most influential primary stakeholder for doing that. It is crucial to the success of lobbying efforts to build one's argumentation on a legal and legitimate basis. It is also very important for these primary stakeholders to get involved in lobbying efforts at an early stage when a draft proposal is being prepared at the European Commission: the chances of shaping the threat at its source are higher then. In doing these associations of these primary stakeholders (e.g., trade unions, supplier associations, dealer associations) have key responsibilities.

A primary stakeholder with the power to shape the firm or the conditions in the system (except for the home government) may not be as willing to lobby EU regulatory organizations because it may even turn the threat into an opportunity if it cannot be shaped at source. I exclude the home government under the assumption that it would not be pursuing opportunities in the market environment. This is not a wrong assumption since the European Commission has strictly forbidden the governments of member countries from taking actions that could disturb competition in the market place. If a powerful primary stakeholder aims to shape the firm or the conditions in the system, it needs to take into account the possible reactions of the management of the firm and other primary stakeholders: its move needs to be 'approved' in the system; otherwise, other stakeholders may collaborate to block it.

If the threat event occurs, it could also be the firm as the powerful actor in the system that takes advantage of it at the expense of some less powerful primary stakeholder. In that situation the powerless primary stakeholder can do little apart from using its legal rights and complaining to the EU regulatory organizations about the unfortunate impact of the new legislation. Primary stakeholders in the system that are highly dependent on the firm (e.g., dealers and suppliers) do not have many strategic options for defending themselves on such occasions. Employees in Germany in particular are more fortunate in that they are empowered by the codetermination law to defend themselves.

There may be times, such as when there is a general economic crisis, when sacrifices are inevitable. Solidarity between actors in the system is important for its survival during such times. I suggest that all primary stakeholders and the firm's management should collaborate in finding solutions for living through the bad times with the least possible damage to all concerned, and this starts with the recognition by all actors in the system that there is need to make sacrifices. In my opinion, the pursuit of individual interests and opportunistic behavior at such times will hurt not only the less powerful actors in the short-run but also the more powerful ones in the long-run. Taking and implementing a systems perspective should benefit all actors in the long run. The solutions that the VW management and employees found during the 1993 crisis (i.e. the four-day week and later the VW week) are examples of such solidarity, and should be analyzed and used as models.

Finally, despite the limitations on its powers by the European regulatory organizations, the home government is still the most powerful primary stakeholder in terms of both lobbying EU regulatory organizations and shaping the conditions in the system. I heard complaints from both of my interviewees that neither the German government nor the Finnish government had contributed much to their respective car industries. In my opinion, the home government would contribute the most by playing a leading role in promoting systems thinking among firms and their primary stakeholders via incentives towards long-term cooperation.

Implications for executive managers:
This research showed that a firm's primary stakeholders may be valuable resources in terms of contributing to the resolution of threats. I therefore make the same recommendation to executive managers, that they adopt a systems perspective. This has already been done in part by Japanese car manufacturers in that they treat their suppliers as long-term partners. European and American manufacturers are also following the Japanese approach to suppliers in the belief that it contributes to firm performance by bringing in more supplier-initiated innovations, and they have been involving their first-tier suppliers more in design and manufacturing processes. Likewise, firms are also adopting schemes to increase employee involvement to improve firm capabilities (e.g., employee stock option plans, Japanese total quality management, and Japanese life-long employment).

In my opinion, such long-term stakeholder orientation, not only with suppliers and employees, but also with all other primary stakeholders, contributes to the system as a whole. This does not mean, however, that firm managers should keep low-performing stakeholders in the system: they rather need to collaborate towards improving the performance of the total system and not just that of the firm. Increasing stakeholder performance would increase the performance of the system and also that of the firm.

A related second implication concerns the building of a coalition for lobbying EU regulatory organizations. A key role for firm managers could be to lead and coordinate such coalition-building activities. This research shows that both the willingness and the power to contribute are dynamic concepts that may change over time. Executive managers can demonstrate their leadership skills by persuading powerful primary stakeholders, especially home governments, to lobby EU regulatory organizations. Ferdinand Piëch and Jürgen Strube have shown this kind of leadership.

A third important lesson for executive managers is that they need to effectively manage primary stakeholder compensation in times of growth and also in times of crisis. The review of VW's history and the single market and VW event showed that extra compensation given during times of growth (e.g., higher salaries and wages for employees) could turn out to be a source of competitive disadvantage in the future. This is because such compensation is path dependent (i.e. the level of current compensation is dependent on earlier increases or decreases), and it could be difficult to take back extra compensation awarded earlier. In order to avoid such situations it may be wise to reward primary stakeholders in good times with one-time bonuses rather than an increase in compensation.

Managing employee compensation is perhaps the most difficult in labor-intensive industries that are sensitive to general economic conditions, such as the car industry. This is because labor costs are fixed whereas revenues are variable. A possible solution to this would be to introduce variable salaries and wages so that labor costs are to a certain extent independent of the level of sales. This is difficult to achieve because people working for fixed salaries and wages usually seek security and certainty. Naturally, they would not be willing to accept fluctuations in their monthly earnings. VW tried to resolve this by introducing flexible working hours and breaking the salary system into fixed and variable elements, a compromise solution[182]. This enabled VW to partially adjust its costs.

Car manufacturers are powerful actors in the system. Their executive managers are definitely aware of this power differential against some of their primary stakeholders, especially suppliers and dealers. It is essential for executives adopting a systems perspective not to abuse this power differential. In my opinion, in the long run this is to the benefit of all actors in the system, including the firms in question.

Implications for policy makers at the European Commission:

As the EU regulatory organization driving market integration in the EU, and also responsible for the implementation of EU legislation, it would be beneficial for the European Commission to understand the systems perspective of the firm and its primary stakeholders.

In its aims to foster competition for the benefit of consumers (or customers as cited in this research) it should remember that they are elements of a system. Anyone wishing to change the dynamics of the system for the benefit of a certain element of it should be aware of the possibility that this will activate market forces that may work against some of the less powerful actors. This may be the case when the change is not intended to increase the total revenues of the system, which is exactly what happened in the BER 1400/2002 event.

Yes, the European Commission is adopting a multi-stakeholder perspective and encouraging all stakeholders to provide inputs during the process of preparing new legislation. In cases in which there are conflicting claims from different stakeholders, the European Commission needs to prioritize these

[182] Mr. Hartz called workers “co-entrepreneurs” and aimed to make 30 percent of wages and salaries performance-based (The Economist 2004).

claims. So far, it has used its priorities in favor of customers. This has in some cases been to the benefit of the more powerful actors in the market environment at the expense of the less powerful. Thus, when we consider the whole system, there have been benefits to some elements but at the same time costs to others. What is the total impact? This needs to be carefully assessed in order to avoid total systemic losses in the effort to create benefits for some elements. This can only be achieved by adopting a systems perspective.

In my opinion, employees are protected by regulations against opportunistic acts in the system. This is perhaps not the case for dealers and suppliers. I was informed by Mr. Rantala during our interview that it was not because of the BER 1400/2002 but because of lack of necessary measures in the Civil Law that car manufacturers could take advantage of the change in regulation. I would recommend that the European Commission reviews the relevant regulatory framework to ensure more protection against opportunistic acts for dealers and suppliers which are highly dependent on car manufacturers.

7.3 Future Research Avenues

This research enhanced understanding of primary stakeholder contributions in responding to the threats of market integration in the EU. The realization that both the willingness to contribute and power are dynamic concepts leads to the categorization of primary stakeholders along these dimensions, and to the emergence of new research questions (see Figure 25).

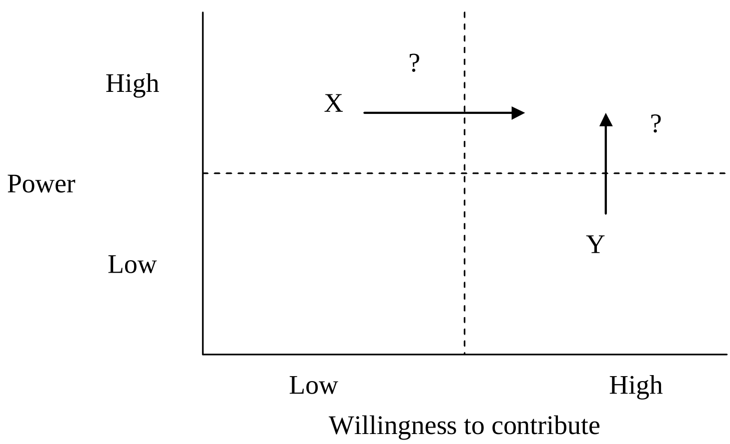

Figure 25. New research questions

It is postulated in the theory that a primary stakeholder can shape a threat at source or shape the firm or the conditions in the system if it is willing to contribute and if it has the necessary power to do so. These two attributes may not be present simultaneously. In such cases, new research questions would be:

1. How could a powerful primary stakeholder (e.g., primary stakeholder X in Figure 25) be made willing to make a contribution?
2. How could a primary stakeholder that is willing to contribute (e.g., primary stakeholder Y in Figure 25) acquire the power to do so?

Question 1 may be relevant to firm managers and primary stakeholders wishing to attract powerful primary stakeholders in lobbying against EU regulatory organizations, and question 2 may be relevant to all primary stakeholders that are willing to contribute. In order to increase understanding it may be useful to review further literature on power and motivation and carry out research via longitudinal case studies.

A second research avenue would be to test the theory by testing its propositions and predictions. This could be achieved through conducting a survey for the different types of primary stakeholders. Positive results from these tests would strengthen the theory, and negative results would suggest ideas for further improvement. The tests would also reveal whether there are differences in types of contribution within a certain group of primary stakeholders.

Thirdly, it would be useful to conduct similar research on the opportunities associated with market integration in the EU: it would be interesting to see whether the behaviors of the firm and its primary stakeholders would change in this case.

This research was limited to primary stakeholders. A similar study could focus on secondary stakeholders, which would be interesting in terms of achieving a better understanding of the differences in behaviors between the two groups.

Finally, it would also be possible to carry out this type of research in different industries and regions. The results would be useful for comparative purposes.

8 SUMMARY

Market integration in the EU has been creating challenges for firms and their primary stakeholders. These challenges are opportunities for some and threats for others. This research focused on threats and aimed to increase understanding of how primary stakeholders of the firm contribute to their resolution by answering the following two research questions:

1. In what ways do various types of primary stakeholders contribute to resolving the threats of market integration in the EU?
2. What determines the type of contributions various primary stakeholders make in resolving the threats of market integration in the EU?

Since there was not any ready theoretical tool to answer the research questions, the development of a theory was the main objective of this research. The research strategy comprised initially the deduction of the theory based on literature review, and then its improvement through an empirical study.

The literature review and the deduction of the theory were accomplished in **Chapter two**. The theory was built upon premises from the descriptive stream of stakeholder theory, general systems theory, the strategic-choice perspective, the contingency perspective, the collective action perspective, the resource dependence perspective, the network perspective, and literature on power. Key elements of the theory included a typology of primary stakeholder contributions[183], a total of 15 propositions on the determinants of types of contribution[184], and a scheme for predicting primary stakeholder contributions[185].

The methodology applied in the empirical study was historical analysis, which was suitable because market integration in the EU has been a 50-year process, and responding to threats is also a process that takes time. The methodological choices were further discussed in **Chapter three**.

The EU, its car industry and primary stakeholders in the EU car industry were reviewed in **Chapter four**, the aim being to gain a pre-understanding of the research context before starting the empirical study. This understanding was also needed later in assessing the attributes of power and the importance

183 See section 2.6.
184 See sub-section 2.7.3.
185 See section 2.8.

of the stake for different primary stakeholders in predicting their likely contributions.

The empirical study was reported in **Chapter five.** It comprised the review of the history of VW from 1960 to 2005 in the light of market integration initiatives in the EU, and the analysis of four events, namely the VW law event, the single market and VW event, the 13th EU directive event, and the BER 1400/2002 event.

The analysis of the events enabled improvement of the theory in **Chapter six**. In the improved theory the typology of primary stakeholder contributions preserved its validity. According to this typology a primary stakeholder can contribute to resolving of a threat either by shaping the threat at source, or by shaping the firm or the conditions in the system so that the system is not anymore vulnerable to the threat, or if necessary by making compensation-related sacrifices or increased input. I improved this part of the theory by elaborating on the temporal relationships among these three types of contributions[186]. In the improved theory the 15 propositions on the determinants of types of contribution were preserved with a minor revision of Proposition 7, and the empirical study led to the induction of five further propositions[187]. This set of 20 propositions provided the answer to research question 2 (see Figure 26). Finally, the scheme for predicting primary stakeholder contributions also preserved its validity in the light of the empirical study. Based on the assessment of the attributes of power and importance of stake, I was able to predict likely contributions of different types of primary stakeholders to resolving of threats arising from market integration in the EU[188]. This was the answer to research question 1 (see Figure 26).

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186 See section 6.1.
187 See propositions 16-20 in section 6.2.
188 See section 6.3.

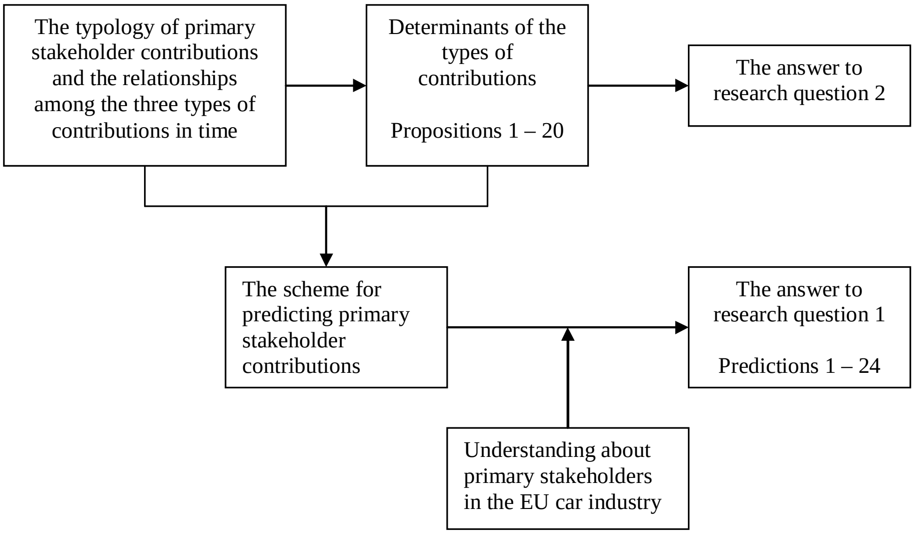

Figure 26. From the theory to the answers of the research questions

This research contributes primarily to the descriptive stream of stakeholder theory in demonstrating that the primary stakeholders of the firm can and do contribute to the resolution of the threats arising from market integration in the EU, and by enhancing understanding of how they can do so through a theoretical lens which was developed in the research for this purpose. The research is of further academic value in that it integrates strategic-management approaches to responding to the environment into the stakeholder literature, tackles an important area of international business, takes a longitudinal view and studies events over a long period of time beginning in 1960, adopts a systems perspective, and differentiates between various types of primary stakeholders. Despite some limitations, the findings have implications for primary stakeholders, for executive managers of firms in the EU, and for policy makers at the European Commission. They also open up possible avenues for further research. All these issues were discussed in **Chapter seven**.

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APPENDIX 1: SOURCES OF INFORMATION

The sources of information are grouped according to types of documents, and the groups are presented in alphabetical order (e.g., annual reports of car manufacturers, EU legislation and related documents, German legislation and related documents, interviews, media news, minutes of board meetings at VW, press releases from car manufacturers, press releases from EU regulatory organizations and their personnel, press releases from industry associations, and various others).

Annual Reports of Car Manufacturers:

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Fiat (2005) *Annual Report 2004*. Fiat.
Ford (2005) *Annual Report 2004*. Ford Motor Company.
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Note: I studied every annual report of VW since 1960 when I was reviewing the firm's history, but I list here only those from which I used references.

EU Legislation and Related Documents:

Commission of the European Communities (1990) Amended Proposal for a thirteenth Council Directive on Company Law Concerning Takeover and Other General Bids. *Official Journal of the European Communities*, OJ C 240, 7–30.

Commission of the European Communities (1995) Commission Regulation (EC) No 1475/95 of 28 June 1995 on the Application of Article 85 (3) of the Treaty to Certain Categories of Motor Vehicle Distribution and Servicing Agreements. *Official Journal of the European Communities*, OJ L 145, 25–34.

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Commission of the European Communities (2002b) *Proposal for a Directive of the European Parliament and of the Council on Takeover Bids*. COM (2002) 534 Final, 2.10.2002, Brussels.

Commission of the European Communities (2007b) Monitoring of the decision-making process between institutions: Proposal for a thirteenth European Parliament and Council directive on company law concerning takeover and other general bids, COM (1988) 823, 0186 COD. <http://ec.europa.eu/prelex/detail_dossier_real.cfm?CL=en&DosId=105995#131258>, retrieved on 10.9.2007.

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Council of the European Communities (1992b) Council Directive 92/21/EEC of 31 March 1992 on the Masses and Dimensions of Motor Vehicles of Category M1. *Official Journal of the European Communities*, OJ L 129, 1–10.

European Economic and Social Committee (1991) Opinion on the Amended Proposal for a Thirteenth Council Directive on Company Law Concerning Takeover and Other General Bids. *Official Journal of the European Communities*, OJ C 102, 49–52.

European Parliament and the Council of the European Union (1994) Directive 94/12/EC of the European Parliament and the Council of 23 March 1994 Relating to Measures to be Taken against Air Pollution by Emissions from Motor Vehicles and Amending Directive 70/220/EEC. *Official Journal of the European Communities*, OJ L 100, 42–52.

European Parliament and the Council of the European Union (2000) Directive 2000/53/EC of the European Parliament and of the Council of 18 September 2000 on End-of-Life Vehicles. *Official Journal of the European Communities*, OJ L 269, 34–43.

European Parliament and the Council of the European Union (2004) Directive 2004/25/EC of the European Parliament and of the Council of 21 April

2004 on Takeover Bids. *Official Journal of the European Union*, OJ L 142, 12–23.

German Legislation and Related Documents:

Government of the Federal Republic of Germany (1960a) Gesetz über die Regelung der Rechtsverhältnisse bei der Volkswagenwerk Gesellschaft mit bescränkter Haftung [Law on the Arrangement of Rights at Volkswagenwerk with Limited Liability]. *Bundesgesetzblatt*, Section 1, No. 23, 13.5.1960, 301.

Government of the Federal Republic of Germany (1960b) Das Gesetz über die Überführung der Anteilsrechten der Volkswagenwerk Gesellschaft mit beschränkter Haftung in private Hand [Law on the Privatization of Volkswagenwerk with Limited Liability]. *Bundesgesetzblatt*, Section 1, 27.7.1960, 585–587.

Interviews:

Hoff, Gerd, Managing Director of the Berlin Office of the German Association of the Automotive Industry, Berlin, July 13, 2007, 11.00–12.00.

Rantala, Pentti, Managing Director of the Central Organization for Motor Trade and Repairs in Finland and Member of the Board of Directors of CECRA, Helsinki, September 19, 2007, 13.00–14.00.

Media News:

Auto Motor und Sport (1977a) Die Schatten sind deutlich kürzer geworden: Interview mit VW Chef Schmücker über seine Pläne für die Achtziger Jahre [The Shadows Have Become Clearly Shorter: Interview with VW Chief Schmücker about his Plans for the 80s], 12.4.1977, No. 8, 3–4.

Auto Motor und Sport (1977b) Volksvermögen: VW in Zahlen [Property of the Public: VW in Numbers], 12.4.1977, No. 8, 7–7.

Automotive Industries (2005a) VW sees suppliers as partners, September 2005, Vol. 185, No. 9.

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Automotive News (1998a) VW entices suppliers with Wolfsburg park, 20.7.1998, Vol. 72, No. 5776.

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Automotive News Europe (2001) VW drops platforms, changes to modules, 29.1.2001, Vol. 6, No. 3.

Automotive News Europe (2002a) VW close to sealing new dealer contracts, 7.10.2002, Vol. 7, No. 19.

Automotive News Europe (2002b) Dealers say carmakers hide behind rules, 23.9.2002, Vol. 7, No. 18.

Automotive News Europe (2002c) VW plans gradual reduction of dealers, 14.1.2002, Vol. 7, No. 1.

Automotive News Europe (2003a) Piëch’s modular plan reaches fruition, 28.7.2003, Vol. 8, No. 15.

Automotive News Europe (2003b) Dealers, carmakers clash on contracts, 25.8.2003, Vol. 8, No. 16.

Automotive News Europe (2004a) Lease deal a win for VW, 3.5.2004, Vol. 9, No. 9.

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Automotive News Europe (2005a) Porsche stock purchase would weld it to VW, 3.10.2005, Vol. 10, No. 20.

Automotive News Europe (2005b) Porsche’s influence on VW could be deep, 17.10.2005, Vol. 10, No. 21.

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Automotive News Europe (2005d) German dealers wary of new VW margins, 19.9.2005, Vol. 10, No. 19.

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Automotive News Europe (2006a) VW board faces critical choices, 17.4.2006, Vol. 11, No. 8.

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Automotive News Europe (2006c) VW demands more from suppliers, 16.10.2006, Vol. 11, No. 21.

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APPENDIX 2: STATISTICS ON THE EU CAR INDUSTRY

Table 1. Car manufacturers in the EU in selected years (compiled from European Commission 2004, 164; International Organization of Motor Vehicle Manufacturers 2007; press releases; media news)

1960	1970	1980	1990	2005
47 manufacturers	39 manufacturers New entrants: 5 Disappearing: 13	31 manufacturers New entrants: 1 Disappearing: 9	31 manufacturers New entrants: 7 Disappearing: 7	21 manufacturers New entrants: 4 Disappearing: 14
Abarth	Abarth	AC Cars	Aixam-Mega	Aixam-Mega
AC Cars	AC Cars	Alfa Romeo	AWE	BMW
Alfa Romeo	Alfa Romeo	Aston Martin	AWZ	Bristol Cars
Alpine	Alpine	AWE	BMW	Caterham Cars
Alvis	Aston Martin	AWZ	Bristol Cars	DaimlerChrysler
Aston Martin	AWE	BMW	Bugatti	Fiat
Autobianchi	AWZ	Bristol Cars	Caterham Cars	Ford
AWE	BLMC	Caterham Cars	Chrysler	GM
AWZ	BMW	Dacia	Dacia	Honda
BMC	Bond Cars	Daimler Benz	Daimler Benz	Microcar
BMW	Bristol Cars	De Tomaso	De Tomaso	Mitsubishi
Bond Cars	Chrysler	Fiat	Fiat	Motors
Borgward	Citroën	Ford	Ford	Morgan Motor
Bristol Cars	Dacia	Ginetta Cars	GM	MTX
Citroën	Daimler Benz	GM	Marcos	Nissan
Daimler Benz	De Tomaso	Lotus	McLaren	Porsche
De Tomaso	Fairthorpe Cars	Morgan Motor	Microcar	PSA
Fairthorpe Cars	Fiat	MTX	Morgan Motor	Renault
Ferrari	Ford	Nissan	MTX	Suzuki
Fiat	Ginetta Cars	Porsche	Nissan	Toyota
Ford	GM	PSA	Porsche	TVR
Ginetta Cars	Jensen Motors	Reliant	PSA	VW
Glas	Lamborghini	Renault	Reliant	
GM	Lotus	Rolls Royce	Renault	
Jaguar	Marcos	SAAB	Rolls Royce	
Jensen Motors	Morgan Motor	SEAT	Rover Group	
Lancia	MTX	Skoda	Skoda	
Lotus	Peugeot	Tatra	Tatra	
Maserati	Porsche	TVR	TVR	
Morgan Motor	Reliant	VW	VW	
NSU	Renault	Volvo	Volvo	
Panhard	Rolls Royce			
Peugeot	SAAB			
Porsche	SEAT			
Reliant	Skoda			
Renault	Tatra			
Rolls Royce	TVR			
Rootes Group	VW			Table 1 (continued)

Rover SAAB SEAT Simca Skoda Tatra TVR VW Volvo	Volvo			

Note: AWE stands for Automobilwerk Eisenach, and AWZ stands for Vertriebseigener Betrieb Sachsenring Automobilwerke Zwickau. TVR and MTX are not abbreviations.

Table 2. Number of car manufacturers in the EU by country of origin in selected years (compiled from the list of car manufacturers in Table 1)

Country of Origin	1960	1970	1980	1990	2005
UK	17	14	10	9	4
Germany	9	6	6	6	4
Italy	8	5	3	3	1
France	6	4	2	4	4
USA	2	3	2	3	2
Sweden	2	2	2	1	0
Czech Republic	2	3	3	3	1
Spain	1	1	1	0	0
Romania	0	1	1	1	0
Japan	0	0	1	1	5
TOTAL	47	39	31	31	21

Note: Germany also includes manufacturers in East Germany.

Table 3. Key events affecting the EU and key events in the EU Car Industry from 1960 to 2005 (compiled from Europa 2006b; press releases; media news)

Key events affecting the EU	Key events in the EU car industry
<u>1960s</u> 1960 – EFTA established among Austria, Denmark, Norway, Portugal, Sweden, Switzerland, and the UK 1963 – The UK's application to the EEC rejected 1966 – Luxembourg Compromise (EEC members get the right to veto decisions) 1967 – The UK's application once more rejected 1968 – The Customs Union in the EEC	<u>1960s</u> 1961 – Borgward went bankrupt in West Germany 1963 – Lamborghini founded in Italy 1965 – VW acquired Auto Union from Daimler Benz 1965 – Rover acquired Alvis in the UK 1965 – Citroën acquired Panhard in France 1966 – Chrysler entered Europe by acquiring Simca in France and the Rootes Group in the UK 1966 – Jaguar merged into BMC in the UK 1966 – BMW acquired Glas in West Germany 1966 – Dacia founded in Romania 1967 – Fiat acquired Autobianchi in Italy 1967 – Leyland Motor Company acquired Rover in the UK 1968 – BMC merged with the Leyland Motor Company in the UK to form BLMC 1968 – Citroën acquired Maserati in Italy 1969 – Fiat acquired Ferrari in Italy 1969 – Fiat acquired Lancia in Italy 1969 – MTX founded in Czechoslovakia 1969 – VW acquired NSU Motorenwerke AG in West Germany
<u>1970s</u> 1973 – UK, Denmark, and Ireland join the EEC 1973 – The First Oil Crisis Table 3 (continued)	<u>1970s</u> 1971 – Fiat acquired Abarth in Italy 1971 – Reliant acquired Bond Cars in the UK 1971 – Jensen Motors went bankrupt in the UK 1971 – Marcos went bankrupt in the UK 1973 – Caterham Cars, manufacturer of light-weight sports cars, founded in the UK

1979 – The Second Oil Crisis	1975 – Peugeot acquired Citroën in France and formed PSA 1975 – BLMC was nationalized following bankruptcy in the name of BL 1975 – De Tomaso acquired the Maserati brand from PSA 1976 – Fairthorpe Cars went bankrupt in the UK 1978 – Lamborghini went bankrupt in Italy 1978 – Renault acquired Alpine in France 1978 – Chrysler pulled out of Europe 1978 – PSA acquired Simca and Rootes Group brands from Chrysler
<u>1980s</u> 1981 – Greece joined the EEC 1985 – The White Paper of the European Commission on completing the internal market 1986 – The Single European Act (extended the scope of qualified majority voting, shift of power to supranational organizations) 1986 – Spain and Portugal joined the EEC 1989 – The reunification of Germany	<u>1980s</u> 1980 – Nissan starts first production in Europe in Spain 1981 – Marcos reborn in the UK 1982 – BL went bankrupt 1983 – Aixam-Mega, French micro-car manufacturer, founded 1984 – Microcar, French micro-car manufacturer, founded 1986 – VW acquired 51percent of SEAT in Spain 1986 – Fiat acquired Alfa Romeo in Italy 1986 – GM acquired Lotus in the UK 1987 – Ford acquired AC cars in the UK 1987 – Bugatti reborn in Italy 1987 – Ford acquired 75 percent of Aston Martin in the UK 1987 – Chrysler acquired the Lamborghini brand 1989 – GM acquired 50 percent of SAAB in Sweden 1989 – Ford acquired the Jaguar brand in the UK which was dissolved in 1984 from the Rover Group 1989 – Ginetta Cars went bankrupt in the UK
<u>1990s</u> Table 3 (continued)	<u>1990s</u> 1990 – VW acquired the remaining 49

  1991 – The collapse of the Soviet Union 1991 – The break-up of Yugoslavia 1991 – The Gulf War 1993 – The establishment of the EU and the single market 1993 – Economic Crisis in the EU and its car industry 1993 – The break-up of Czechoslovakia 1994 – The establishment of the EEA between the EU and EFTA countries 1995 – Austria, Finland, and Sweden joined the EU 1996 – The customs union between the EU and Turkey	percent of SEAT 1990 – McLaren founded in the UK 1991 – VW acquired Skoda in Czechoslovakia 1991 – Mitsubishi Motors started production in Europe together with Volvo in Holland 1991 – AWE and VEB, two East German car manufacturers, went bankrupt 1992 – Toyota's first manufacturing plant in Europe in the UK 1992 – Honda's first manufacturing plant in Europe in the UK 1993 – Suzuki started its first production in Europe in Hungary 1993 – Chrysler entered Europe once again with manufacturing plants in Austria and the UK 1993 – Ford acquired the remaining 25 percent of Aston Martin 1993 – Bugatti acquired the Lotus brand from GM 1993 – Fiat acquired the Maserati brand from De Tomaso in Italy 1994 – BMW acquired the Rover Group in the UK 1994 – Megatech acquired the Lamborghini brand from Chrysler 1996 – Proton acquired theLotus brand from Bugatti 1998 – Daimler Benz merged with Chrysler to form DaimlerChrysler 1998 – VW acquired Bugatti in Italy 1998 – VW acquired the Lamborghini brand from Megatech 1998 – VW acquired the Bentley brand 1999 – Renault allied with Nissan 1998 – BMW acquired the Rolls Royce brand in the UK 1999 – Ford acquired Volvo in Sweden 1999 – Renault acquired Dacia in Romania 1999 – Tatra went bankrupt in the Czech Republic
<u>2000–2005</u> Table 3 (continued)	<u>2000–2005</u> 2000 – GM allied with Fiat 2000 – DaimlerChrysler allied with Mitsubishi Motors

	2000 – GM acquired the remaining 50 percent of SAAB 2000 – Ford acquired the Land Rover brand from BMW 2000 – BMW dissolved the Rover brands, retaining only MINI, Triumph, and Riley 2000 – Daimler Chrysler acquired 40 percent of McLaren 2000 – Marcos went bankrupt in the UK
2002 – Single Currency (Euro) entered circulation in twelve member countries (not in the UK, Sweden, and Denmark)	2002 – Reliant went bankrupt in the UK
2004 – The Eastern Enlargement: ten new member countries joined the EU	2004 – De Tomaso went bankrupt in Italy
	2005 – The GM-Fiat alliance ended 2005 – The DaimlerChrysler-Mitsubishi Motors alliance ended 2005 – Porsche acquired 18.53 percent of VW

Table 4. Selected EU legislation affecting the EU car industry

Legislation No.	Legislation Date	Legislation Content
91/542/EEC	1.10.1991	Limits on gas emissions
92/21/EEC	31.3.1992	Masses and dimensions of motor vehicles
92/53/EEC	18.6.1992	Approval of motor vehicles
94/12/EC	23.3.1994	Limits on gas emissions
EC 1475/95	28.6.1995	Car distribution, repair & maintenance
2000/53/EC	18.9.2000	Vehicle scrapping, use of hazardous materials
EC 1400/2002	31.7.2002	Car distribution, repair & maintenance

Table 5. The market shares (percentage) of car manufacturers in Western Europe in selected years (compiled from Rhys 2004, 883; and ACEA 2006).

Manufacturer	1973	1985	1990	1995	2000	2005
Fiat	14.9%	12.2%	13.8%	11.1%	10.0%	6.6%
VW	11.3%	12.9%	15.7%	16.8%	18.7%	18.9%
PSA	10.9%	11.6%	12.7%	12.0%	13.1%	13.7%
Ford	10.6%	11.6%	11.5%	13.7%	10.8%	10.9%
Renault	10.3%	10.7%	9.7%	10.3%	10.6%	9.8%
GM	10.1%	11.4%	12.0%	13.1%	10.8%	10.6%
Rover	9.0%	3.9%	2.7%	-	-	-
Japanese	7.6%	11.0%	11.8%	10.7%	11.4%	13.5%
Daimler	2.0%	3.3%	3.2%	4.0%	6.2%	6.2%
BMW	1.4%	2.5%	2.9%	6.4%	3.4%	5.3%
Korean	0.0%	0.0%	0.1%	1.5%	3.4%	3.8%
Others	11.9%	8.9%	3.9%	0.4%	1.6%	0.7%
TOTAL	100.0%	100.0%	100.0%	100.0%	100.0%	100.0

Note: PSA in 1973 includes Peugeot (5.6 percent) and Citroën (5.3 percent).

Table 6. 2005 car sales in the EU-15 plus Norway and Switzerland by country and car manufacturer (adapted from French Association of Car Manufacturers 2006)

(in 000 units)	VW	PSA	Japanese	Ford	GM	Renault	Fiat	DaimlerChrysler	BMW	Korean	Others	Total	Percentage of total
Germany	1 030	189	388	292	375	169	61	400	291	103	21	3 319	22.9%
UK	336	244	434	458	363	175	43	107	157	78	45	2 440	16.8%
Italy	251	225	268	198	208	143	627	133	92	82	10	2 237	15.4%
France	228	633	179	124	118	534	65	76	53	49	9	2 068	14.3%
Spain	333	313	132	167	162	191	51	56	47	70	7	1 529	10.6%
Belgium	90	101	52	44	57	52	15	24	27	15	3	480	3.3%
Holland	79	62	79	58	57	40	19	17	17	34	3	465	3.2%
Austria	95	29	48	24	31	19	17	15	14	16	0	308	2.1%
Sweden	48	29	43	71	35	13	1	10	10	13	1	274	1.9%
Greece	46	25	67	23	29	10	13	14	8	34	1	270	1.9%
Switzerland	53	25	59	22	25	16	13	20	17	13	2	265	1.8%
Portugal	35	37	27	18	28	29	7	11	9	5	0	206	1.4%
Ireland	28	13	53	25	16	11	3	5	7	9	2	172	1.2%
Finland	26	15	45	22	10	7	6	7	3	6	1	148	1.0%
Denmark	29	27	39	13	12	4	6	2	2	14	0	148	1.0%
Norway	25	10	36	13	10	3	0	4	4	5	0	110	0.8%
Luxembourg	11	7	5	4	3	6	2	3	4	3	1	49	0.3%
TOTAL	2 743	1 984	1 954	1 576	1 539	1 422	949	904	762	549	106	14 488	100.0%
Percentage of total	18.9 %	13.7 %	13.5 %	10.9 %	10.6 %	9.8 %	6.6 %	6.2 %	5.3 %	3.8 %	0.7 %	100.0 %	

Table 7. Major assembly plants in the EU as of 2005 (adapted from Automotive News Europe 2005e)

Manufacturer	Plant Location
BMW (7 plants)	Germany (4) – Dingolfing, Leipzig, Munich, Regensburg UK (2) – Goodwood, Oxford Austria (1) – Graz
DaimlerChrysler (10 plants)	Germany (6) – Bremen, Düsseldorf, Ludwigsfelde, Osnabrück, Rastatt, Sindelfingen Austria (1) – Graz France (1) – Hambach Spain (1) – Vitoria UK (1) – Woking
Fiat (8 plants)	Italy (7) – Cassino, Maranello, Melfi, Mirafiori, Modena, Pomigliano d'Arco, Termini Imerese Poland (1) – Tychy
Fiat – PSA joint venture (2 plants)	France (2) – Hordain, Lieu Daint-Armand
Ford (13 plants)	UK (7) – Castle Bromwich, Coventry, Gaydon, Halewood, Newport Pagnell, Solihull, Southampton Belgium (2) – Genk, Ghent Germany (2) – Cologne, Saarlouis Spain (1) – Valencia Sweden (1) – Gothenburg
GM (14 plants)	Germany (3) – Bochum, Eisenach, Rüsselsheim UK (3) – Ellesmere Port, Luton, Norwich Poland (2) – Gliwice, Warsaw Belgium (1) – Antwerp France (1) – Cerizay Italy (1) - Grugliasco Portugal (1) – Azambuja Spain (1) – Zaragoza Sweden (1) – Trollhättan
Honda (1 plant)	UK (1) – Swindon
Mitsubishi Motors (2 plants)	Holland (1) – Born Portugal (1) – Tramagal

Table 7 (continued)

Nissan (2 plants)	Spain (1) – Barcelona UK (1) – Sunderland
Porsche (3 plants)	Germany (2) – Leipzig, Stuttgart-Zuffenhausen Finland (1) – Uusikaupunki
PSA (10 plants)	France (6) – Aulnay-sous-Bois, Cerizay, Mulhouse, Poissy, Rennes-la-Jannais, Sochaux Spain (2) – Madrid-Villaverde, Vigo Portugal (1) – Mangualde UK (1) – Ryton
Renault (10 plants)	France (6) – Batilly, Dieppe, Douai, Flins, Maubeuge, Sandouville Spain (2) – Valencia, Valladolid Romania (1) – Pitesti Slovenia (1) – Novo Mesto
Suzuki (2 plants)	Hungary (1) – Esztergom Spain (1) – Linares
Toyota (2 plants)	France (1) – Valenciennes UK (1) – Burnaston
Toyota – PSA Joint-venture (1 plant)	Czech Republic (1) – Kolin
VW (19 plants)	Germany (7) – Dresden, Emden, Hanover, Ingolstadt, Mosel, Neckarsulm, Wolfsburg Czech Republic (3) – Kvasiny, Mlada Boleslav, Vrchlabi Spain (2) – Martorell, Pamplona Belgium (1) – Brussels Hungary (1) – Gyor Italy (1) – Sant'Agata Bolognese Poland (1) – Poznan Portugal (1) – Setubal Slovakia (1) – Bratislava UK (1) – Crewe

Table 8. 2004 manufacturing figures by manufacturer and country (compiled from International Organization of Motor Vehicle Manufacturers 2007)

(in 000 units)	Germany	France	Spain	UK	Belgium	Italy	Others	Total
VW	1 776		649	8	185	2	796	3 416
PSA		1 808	517	180		4		2 509
Ford	742		449	257	440	9	251	2 148
Renault		1 084	489				117	1 690
GM	556	15	402	147	231	13	257	1 621
Daimler Chrysler	1 005	96	39				119	1 259
Fiat		21				797	293	1 111
BMW	760			190			113	1 063
Toyota		209		242				451
Nissan			35	320				355
Honda				191				191
Suzuki			16				72	88
Mitsubishi Motors						8	80	88
Porsche	74						10	84
TOTAL	4 913	3 233	2 596	1 535	856	833	2 108	16 074
Percent of total	31%	20%	16%	10%	5%	5%	13%	

Note: Others include Austria, the Czech Republic, Finland, Holland, Hungary, Poland, Portugal, Slovakia, Slovenia, and Sweden.

Table 9. Numbers of car models by manufacturer and car segment (compiled from BMW 2006; DaimlerChrysler 2006; Fiat 2006; Ford 2006; General Motors 2006; Honda 2006; Mitsubishi Motors 2006; Nissan 2006; Porsche 2006; PSA Peugeot Citroën 2006; Renault 2006; Suzuki 2006; Toyota 2006; Volkswagen 2006e)

	Microcar	A-segment	B-segment	C-segment	D-segment	E-segment	F-segment	Sports	Multi-purpose	Total
VW			132	413	360	65	39	39	217	1 265
PSA		8	61	46	44	8		26	45	238
Ford		7	74	191	200	11	10	13	77	583
Renault			76	46	122			17	82	343
GM		27	39	61	159	26		25	94	431
Daimler Chrysler	8		22	17	18	22	6	72	61	226
Fiat		7	51	26	27	4	2	13	18	148
BMW		7		27	41	37	19	58	32	221
Toyota		14	22	45	55	4	1	12	52	205
Nissan			32	19	7			7	22	87
Honda			3	14	15			2	11	45
Suzuki		3	6	6					12	27
Mitsubishi Motors			14		9			3	44	70
Porsche								12	4	16
TOTAL	8	73	532	911	1 057	177	77	299	771	3 905

Note: The product segments are classified according to a classification scheme based on car length adapted from the European New Car Assessment Programme (cf. European New Car Assessment Programme 2006): the microcar segment (less than 330 cm), the A segment (330–360 cm), the B segment (370–400 cm), the C segment (410–440 cm), the D segment (450–470 cm), the E segment (480–500 cm), and the F segment (over 500 cm). The sports segment includes all coupe, cabriolet, and roadster models, and the multi-purpose segment includes all sports utility vehicles, crossovers, and multi-purpose vehicles.

Table 10. The percentage revenues of car manufacturers by strategic business areas in 2004 (compiled from BMW 2005; DaimlerChrysler 2005; Fiat 2005; Ford 2005; General Motors 2004; Honda 2005; Mitsubishi Motors 2005; Nissan 2005; Porsche 2004; PSA Peugeot Citroën 2005b; Renault 2005; Suzuki 2005; Toyota 2005; Volkswagen 2005c)

	Cars	Light commercial vehicles	Financial services	Trucks	Component supply	Motorcycles	Busses and coaches	Others
VW	83%	6%	10%	1%			0%	0%
PSA	64%	9%	3%		19%			5%
Ford	48%	36%	13%	2%			0%	1%
Renault	82%	12%	6%	0%				0%
GM	46%	36%	16%	1%				1%
Daimler Chrysler	58%	13%	9%	16%			2%	2%
Fiat	45%	10%	0%	6%	10%		2%	27%
BMW	82%		16%			2%		0%
Toyota	66%	8%	4%	5%	12%		1%	4%
Nissan	71%	22%	5%	2%			0%	0%
Honda	80%	1%	3%			12%		4%
Suzuki	65%	13%	0%			19%		3%
Mitsubishi Motors	76%	21%	2%	1%				
Porsche	91%		9%					0%

Note: Financial services include financing, insurance, direct banking, professional fleet management, and short-term car rental, and component supply includes only sales to third parties. Fiat's high figure in other revenues comes mostly from the sales of agricultural and construction equipment, which accounted for 20 percent of its total sales.

Table 11. Employment figures in 2004 (compiled from BMW 2005; DaimlerChrysler 2005; Fiat 2005; Ford 2005; General Motors 2004; Honda 2005; Mitsubishi Motors 2005; Nissan 2005; Porsche 2004; PSA Peugeot Citroën 2005b; Renault 2005; Suzuki 2005; Toyota 2005; Volkswagen 2005c; International Organization of Motor Vehicle Manufacturers 2007)

Manufacturer	Total Workforce	Percentage of production in home country
BMW	105 972	61%
DaimlerChrysler	384 723	68%
Fiat	160 549	48%
Ford	324 864	46%
GM	324 000	45%
Honda	137 827	38%
Mitsubishi Motors	36 970	45%
Nissan	183 607	46%
Porsche	11 668	89%
PSA	198 600	57%
Renault	130 573	53%
Suzuki	na	na
Toyota	260 000	54%
VW	342 502	37%
Average	200 142	52%

Note: ‘na’ stands for not available.

Table 12. Total R&D costs in 2004 (compiled from BMW 2005; DaimlerChrysler 2005; Fiat 2005; Ford 2005; General Motors 2004; Honda 2005; Mitsubishi Motors 2005; Nissan 2005; Porsche 2004; PSA Peugeot Citroën 2005b; Renault 2005; Suzuki 2005; Toyota 2005; Volkswagen 2005c)

Manufacturer	R&D Cost (million Euro)	R&D Cost (Percentage of revenues)
BMW	2 818	6.4%
DaimlerChrysler	5 658	4.0%
Fiat	1 810	3.9%
Ford	5 949	4.3%
GM	5 226	3.4%
Honda	3 479	5.7%
Mitsubishi Motors	512	3.2%
Nissan	5 196	8.1%
Porsche	na	na
PSA	2 118	3.7%
Renault	1 383	3.4%
Suzuki	645	3.7%
Toyota	5 074	3.7%
VW	3 797	4.3%
Average	3 359	4.3%

Note: ‘na’ stands for not available. US and Japanese figures were converted at 1€ = 1.2439$, and 1€ = 134.44 Yen, which are the year average figures for 2004 (cf. European Central Bank 2006).

Table 13. Total investments in PP&E in 2004 (compiled from BMW 2005; DaimlerChrysler 2005; Fiat 2005; Ford 2005; General Motors 2004; Honda 2005; Mitsubishi Motors 2005; Nissan 2005; PSA Peugeot Citroën 2005b; Renault 2005; Suzuki 2005; Toyota 2005; Volkswagen 2005c)

Manufacturer	Investment in PP&E (million Euro)	Investment in PP&E (Percentage of revenues)
BMW	3 079	7.0%
DaimlerChrysler	6 386	4.5%
Fiat	2 112	4.6%
Ford	1 468	1.1%
GM	2 027	1.3%
Honda	2 296	3.8%
Mitsubishi Motors	988	6.2%
Nissan	7 667	12.0%
Porsche	177	2.8%
PSA	1 382	2.4%
Renault	1 540	3.8%
Suzuki	689	4.0%
Toyota	6 508	4.7%
VW	5 445	6.2%
Average	2 983	4.0%

Note: US and Japanese figures were converted at 1€ = 1.2439$, and 1€ = 134.44 Yen, which are the year average figures for 2004 (cf. European Central Bank 2006).

APPENDIX 3: INTERVIEW QUESTIONS

- Interview with Dr. Gerd Hoff, Managing Director of the Berlin Office of the German Association of the Automotive Industry, Berlin, July 13, 2007, 11.00–12.00:

1. What are the key success factors for the successful continuation of the German automotive industry?
2. In the light of increasing consolidation and cooperation, how do you see the future of the automotive industry from the point of view of German car manufacturers?
3. How do you assess Porsche's acquisition of Volkswagen shares?
4. How do German car manufacturers see their relationships with suppliers?
5. Considering the high labor costs in Germany and the emergence of competitive production locations such as in Eastern Europe, how do you see the future of Germany as a production location?
6. How do German car manufacturers see their relationships with dealers and how are these relationships changing with BER 1400/2002?
7. What has been the attitude of the German government towards the automotive industry?
8. Can you tell me about the lobbying efforts of German car manufacturers in EU regulatory organizations? What mechanisms are they using and which actors are involved in general?
9. When Mannesmann was overtaken by Vodafone in a hostile manner, there were also rumors that Ford had intentions to take over Volkswagen. At the same time the 13th EU takeover directive discussions were going on, and in the end it was the efforts of Gerhard Schröder that led to the refusal of the takeover directive in July 2001. Can you recall and describe the atmosphere in Germany against the 13th EU takeover directive?
10. What has been and what is today the role of the banks for German car manufacturers, and what kind of relationships do they have with them?

- Interview with Pentti Rantala, Managing Director of the Central Organization for Motor Trade and Repairs in Finland and Member of the Board of Directors of CECRA, Helsinki, September 19, 2007, 13.00–14.00:

1. Why was it necessary to change BER 1475/95?
2. How did CECRA or ACEA try to influence the European Commission during the period when it was drafting the new regulation?
3. What are the main problems of dealers in their relationships with car manufacturers?
4. How do dealers and car manufacturers see each other in this relationship? Is this a relationship of dependence or is it a relationship of equal partners?
5. How did BER 1400/2002 change the relationship between dealers and car manufacturers?
6. According to the new regulation, car manufacturers could choose between selective and exclusive types of distribution. Most car manufacturers chose the selective type. What was the key reason for their choice?
7. According to the new regulation, dealers can sell multiple brands in the same showroom. In practice we see that this option is exercised by some dealers and not others. For example, Volkswagen dealers sell only Volkswagen. What is happening in practice? Is Volkswagen telling its dealers not to sell Toyotas or Fords?
8. According to the new regulation, dealers are no longer required to carry out repair and maintenance services. Do they generally continue to provide these services, and why do they prefer to do so?
9. According to the new regulation, dealers are no longer required to use original spare parts. How does this work in practice? Are dealers offering all kinds of spare parts and letting customers choose, or are car manufacturers using some incentives to encourage the use of original spare parts?
10. Of all the stakeholders that were influenced by this regulation, which ones in the end benefited from it, and how?
11. When there is an economic crisis that affects the sales of cars negatively, in what ways do dealers respond?

APPENDIX 4: ANALYSIS OF A SAMPLE DOCUMENT

This appendix exemplifies the analysis of one of the 326 documents in the empirical study. Table 1 provides the codes used in the analysis, and the italic and bold quotations in brackets in the text of the document are my notes and memos extracted from the underlined parts of the document.

Table 1. Codes used in analyzing data in the document

Name of category and its code	Properties of the category and their codes	Dimensions of the category / property
1. Nature of threat	1a. Scope of threat 1b. Source of threat	General, specific to the industry, specific to a branch of the industry, firm-specific Regulatory organization, competition, hedge fund
2. Importance of stake	2a. Relationship-specific investments 2b. Compensation	High, low High, low
3. Power of primary stakeholder to affect the source of the threat	3a. Owned resources 3b. Accessible resources 3c. Legal rights	High, low High, low High, low
4. Power of primary stakeholder to affect the firm or the conditions in the system	4a. Owned resources 4b. Accessible resources 4c. Legal rights	High, low High, low High, low
5. Ability to contribute	5a. Ability to shape the threat at source 5b. Ability to shape the firm or the conditions in the system	Yes, no Yes, no
6. Willingness to contribute		Yes, no
7. Type of contribution		Type-I, Type-II, Type-III

38th document from file 4, CECRA (2002a)
Title: CECRA Congress, 18.9.2002 in Frankfurt a.M., Statement by Jürgen Creutzig, President of CECRA, CECRA: Brussels
[The document is from a reliable source.]

Ladies and Gentlemen,
It is my pleasure to address the 2002 CECRA Congress on the subject of the new Block Exemption Regulation for the Motor Retail and Repair Industry. This new Block Exemption Regulation, abbreviated to BER, will change the professional life of all the European businesses that are active in the field of selling, maintaining and repairing motor vehicles, not only within the current European Union, but also in the countries which will soon join as new member states.

1. Principles:
- It is in the best interest of consumers that dealers be economically independent.
- Dealers are not mere pawns of their manufacturers ***[4: low]***. They form part of a manufacturer's network yet also remain independent with their own objectives and opinions ***[Prioritizing own interests. Individualistic thinking rather than systems thinking]***. Certainly dealers and manufacturers have many opinions in common but they can also diverge on certain issues.
- Therefore CECRA has worked towards two objectives:
  - To strengthen the economic independence of the authorized dealers and repair shops
  - To obtain unhindered access to the necessary technical information in order to strengthen the position of all dealers and repair shops who require it, whether authorized or independent.

2. What CECRA did:
- From the outset CECRA has been extensively involved ***[7: Type-I, efforts to shape the threat at its source; 6: yes]*** with the new legislation replacing the existing BER 1475/95. In particular a task force chaired by Mr. David Evans identified and examined various problems and formulated CECRA's policy in conjunction with combined meetings with the Car Division (Chairman Mr. Jean-Paul Bailly), Truck Division (Chairman Mr. Massimo Campilli), Independent Repairers Division (Chairman Mr. François Ralite) and Legal Working Group (Mr. Chairman Mr. Arnold Koopmans). Draft papers were formulated and agreed by the Executive Bureau.

- CECRA's position was ublished in our September/October 2001 brochure. This contained all our requests and can now be compared with the results, which we have achieved.
- CECRA, in addition has sent position papers to all Commissioners, Chefs the Cabinets, General Directors and to individuals who are responsible for competition in the different Directorates. These were also forwarded to members of the European Parliament, in particular to members of the Committee on Economic and Monetary Affairs and the Legal Affairs Committee. Furthermore, other associations on a European level have been encouraged to support our position ***[Aiming to build a coalition and increase legitimacy]***.
- CECRA has had numerous meetings with those members listed above. The Executive Bureau has also met with Mr. Monti, other Commissioners and their staff on several occasions.
- CECRA has made several press releases available to keep the public informed of our position.
- CECRA has also taken part in hearings, which the Commission, the European Parliament and more specifically the Committee on Economic and Monetary Affairs have organized.
- CECRA organized two lunch meetings with members of the European Parliament.
- CECRA has repeatedly requested all member associations to support our lobby work.
- Some members associations (SIMI, GANVAM, FACONAUTO, FEDERAICPA, Bundesgremium des Fahrzeughandels, ZDK, CNPA, European IVECO Dealer Council, European Volkswagen/Audi Dealer Council) have organized a congress on the new BER and have invited me to inform about CECRA's position and the latest situation. At some of those meetings members of DG Competition have taken part so that members could inform them directly about their concerns and opinions.

3. What members have done:

- Member associations have written to the Commissioners and/or Members of the European Parliament in their country and in some cases have had meetings with them.
- They have also written to their respective National Governments ***[Stakeholders building a coalition against the European Commission. Attracting other stakeholders to the coalition increases power and its legitimacy and thus the ability to shape the threat at its source]*** and met with the relevant representatives.
- Entrepreneurs have written to the Commissioners and their staff and to

Members of the European Parliament

- Below are details of the requests in we did not succeed (4), the outcomes we refused (5), those outcomes, which are negative for one sector of members, and positive for another (6) and finally those with which we are in full agreement (7).

4. Unfortunately CECRA did not succeed in the following requests

- The link between sales and after sales services was not maintained. At the beginning Mr Monti seemed to be in favor of total independence of both parts of the business. CECRA on the other hand argued repeatedly how vital that link was in the interest of the consumer. As a result of this Mr. Monti's staff seem to have changed their position. There is talk of "re-organization" meaning subcontracting.
- However they have combined this new way of business with many conditions (for example, to supply the repair shop's name and address prior to completing the sales contract and to inform the customer about the distance to the repair shop) with the effect that subcontracting will be the exception.
- I will not repeat the reasons CECRA has argued for keeping the link. But it is certain that good service could very well result in the customer purchasing a new car. The customer expects good support from one business-seller.
- We also did not succeed in prohibiting the direct sale of vehicles from manufacturers to the end-user. The Commission argued that this intervention would be too restrictive to Competition. They did not agree with the decision of the US Anti Trust Office and the Dealers' Protection laws of some States of the USA, which provides for the prohibition of direct sales by vehicle manufacturers. To avoid negative implications for the dealers it is now up to the European Dealers Association to negotiate a fair and reasonable solution with their manufacturers. CECRA will support them in this.
- We were unable to receive the <u>protection we sought for our immense investments in our businesses</u> ***[2a: high]***. The Commission was of the opinion that they could only agree to the two years termination clause and all further regulations are a case of national civil law. This situation was extremely disappointing as CECRA had already successfully lobbied the European Parliament for this protection clause and <u>the Commission had previously promised to follow the Parliament's proposals</u> ***[Positions of actors may change in time]***. In some cases they followed the proposals but despite knowing the importance of the protection for investments <u>they did not follow the parliament on this issue</u>

[Conflicting opinions of different EU regulatory organizations. It is important to know which regulatory organization plays the leading role in making legislation. In this event, the European Parliament had only advisory position because this was not a completely new legislation and thus did not necessitate the co-decision procedure]. This point will also be a matter for agreement between Manufacturers and their Dealer Associations. In relation to this, CECRA has made an acceptable proposition in our September/October 2001 brochure. I recommend that you read this brochure once more.

5. Outcomes refused by CECRA

- Manufacturers in the EU can use different distribution systems, i.e. in one country a manufacturer can operate the selective distribution system, however in another the exclusive system and finally in a third country, direct sales to end-users may be used. It is the opinion of CECRA that this manner of operating discriminates against dealers and this should be proved in the courts.
- The Commission can declare by a regulation, that where parallel networks of similar vertical restraints cover more than 50 percent of a relevant market, the BER shall not apply to vertical agreements containing specific restraints relation to the market. The Commission itself knows that in the EU 100 percent of the market have the same vertical restraints in the vehicle dealer's contracts. So, in effect, <u>the Commission indicates to us, please pay attention you know that at any time I can end the Block Exemption. This is like having the Sword of Damocles hanging over our heads</u> ***[1a: branch of the industry; 1b: regulatory organization (the European Commission)]***.

6. Outcomes with ambivalent effects

The new BER contains clauses, which are on one hand positive for a sector of our membership and on the other hand negative for another.

- Quantitative selection for authorized repair shops is no longer possible. Thus manufacturers must accept whoever fulfils the qualitative standards, which they set for authorized repair shops. The repair shop has a legal claim to be authorized. This can be advantageous for independent repair shops or former authorized dealers whose contract has been terminated by their manufacturer and who want to continue as an authorized repair shop of that manufacturer. It may be disadvantageous for the manufacturer and their network if the termination was made due to restructuring of the network.
- The most controversial item is the prohibition of the location clause for

dealers who distribute passenger cars and light commercial vehicles. The outcome of this is that this ban comes into force on 01 October 2005, which is two years later than the expiration of the BER. This rule will be dangerous for those members who do not have the financial means to open outlets in other regions within the EU. CECRA estimates that the group just mentioned makes up 80 percent of our members. On the other hand this rule is quite advantageous for the other 20 percent of our members ***[There may be actors with differing power based on differing financial resources (4a) within a specific type of primary stakeholders. In addition, the same event can be a threat for some of these primary stakeholders (i.e. the less powerful ones) and an opportunity for others (i.e. the more powerful ones) at the same time]***. However, they will also have to examine the financial viability of such an investment.

- There is no restriction in relation to the location of the establishment of authorized repair shops within the selective distribution system. Naturally this is beneficial to them but imposes a large amount of economic responsibility on them as to whether the location is economically viable or not. It is also less positive for existing networks as it will result in increased competition.

7. Points which members of CECRA positively welcome

- We have achieved a branch specific BER ***[7: Partial Type-I contribution]***. You may recall that at the outset Mr. Monti intended to let BER 1475/95 expire so that the umbrella BER2790/1999 would be applicable to our branch. As you are aware this BER 2790/1999 lacks any dealer protection and places power solely in the hands of the manufacturer.
- There is no specific distribution channel for Internet dealers, supermarkets etc. Mr. Monti had originally contemplated opening such a parallel distribution channel besides the existing network.
- Trucks were not excluded from the BER. At the outset it was proposed to exclude trucks partly out of this BER and to leave them to the umbrella BER, also the definition of a light commercial vehicle was reduced from 6 tons to 3.5 tons.
- It may happen that we will have different agreements with the manufacturers: one for sales and after sales service as at present, one only for sales of spare parts, one only for after sales service. This is beneficial for the dealer to decide in different ways which contracts he wants to keep and which not.
- The authorized dealer/the authorized repair shop is permitted to sell their contract to another authorized dealer/repairer respectively of the same make. Finally with this rule the contract has taken on new worth, which it

never had in the past. The dealer decides whom he wishes to sell it to, not the manufacturer. The manufacturer has no right of veto.

- The BER is applicable to contracts with sub-contracting enterprises.
- The BER is applicable to agents.
- In relation to multi-branding the new rules permits the dealer to sell several different makes in different sales areas of the same show room. Furthermore, CECRA has also requested that specific sales personnel may be provided but only if the dealer and not the manufacturer want it this way and that the manufacturer will pay for the additional costs of these personnel. This is precisely what is in the final text of the new BER. This rule should result in savings for our members.
- Authorized repair shops are entitled to purchase spare parts from spare parts manufacturers as well as from independent third parties. They are free to sell them to all independent repair shops.
- The 2-year termination period for ordinary termination has been re-introduced. You may recall that at the outset Mr Monti was of the opinion that this clause was a matter of National Civil Law rather than European Competition Law.
- Manufacturers are obliged to provide written notice of termination and to give the reasons for this termination. These reasons must be both objective and transparent. Further reasons cannot be reinforced in a follow on discussion.
- The access to all necessary information is extended in line with CECRA's concerns. I cannot mention all details because of the restricted space here.
- The arbitration clause has also been extended in line with CECRA’s requests. As a result even members of the boards of dealers associations can go to the arbitrator on their members’ behalf if they are pressed by their manufacturers. In the past this would not have been possible.

8. Transitional period

During the period, which extends from 01 October 2002 to 30 September 2003, existing agreements, which satisfy the conditions of BER 1475/95, are exempted. As a result there will be contradictions between the existing and new BER. For example: A Volkswagen dealer whose contract has been cancelled wants to become an authorized Volkswagen repair shop in Brussels. However Volkswagen already has a dealer’s agreement with a Volkswagen dealer with repair shop in this region. The contract states that Volkswagen can install another repair shop only with the consent of that dealer. Thus if the dealer does not give his consent, Volkswagen is in a difficult position. If it refuses the repair shop it violates the new BER, but also if it authorizes the repair shop it violates the existing contract with the dealer. CECRA is of the opinion that the interpretation of the European Parliament, which would give precedence to the existing contract, would be an acceptable solution. However the Commission did not incorporate this into the new BER so it is up to the Court to decide this question.

This was our first assessment of the new BER. CECRA will support, in particular, the European Dealers Associations in transforming the new rules into their contracts. Please note that CECRA underlines that the new BER can be implemented into the existing dealers' contracts without cancellation. It only requires that both sides agree on the new clauses. If a manufacturer has cancelled or intends to cancel existing contract, members should be cautious, as CECRA feels it is not necessary and <u>the manufacturer may use the cancellation of the contract for other reasons, such as reducing the dealer margin</u> ***[4c: high manufacturer power based on contractual rights]***.

9. Final remarks

The speaker is now going to deal with the new developments.

APPENDIX 5: STATISTICS ON VW AND THE EVENTS

Table 1. Key figures of VW in comparison 1960–1970 (compiled from Volkswagen 1961 and Volkswagen 1971)

	1960	1970	Change
Vehicle sales (units)			
Germany	374 478	725 055	+94%
Abroad	514 029	1 481 866	+188%
Total	888 507	2 206 921	+148%
Employment (persons)			
Germany	64 139	124 792	+95%
Abroad	11 389	35 421	+211%
Affiliates	-	30 093	-
Total	75 528	190 306	+152%

Table 2. Key figures of VW in comparison 1970–1975–1980 (compiled from Volkswagen 1971, Volkswagen 1976, and Volkswagen 1981)

	1970	1975	Change	1980	Change vs. 1975
Vehicle sales (units)					
Germany	725 055	625 555	-14%	787 591	+26%
Abroad	1 481 866	1 412 302	-5%	1 707 156	+21%
Total	2 206 921	2 037 857	-8%	2 494 747	+22%
Employment					
Germany	124 792	93 026	-25%	118 766	+28%
Abroad	35 421	59 157	+67%	99 060	+67%
Affiliates	30 093	24 641	-18%	40 104	+63%
Total	190 306	176 824	-7%	257 930	+46%

Table 3. Financing at VW during 1972–1975 (adapted from Volkswagen 1974g and Volkswagen 1976)

(in million German Marks)	1972	1973	1974	1975
Owners' equity	3 786	3 912	3 258	3 068
External financing	4 944	6 389	10 278	9 851
Interest expenses	53	76	91	197

Table 4. Key figures of VW in comparison 1980–1984–1990 (compiled from Volkswagen 1981, Volkswagen 1985, and Volkswagen 1991)

	1980	1984	Change vs. 1980	1990	Change vs. 1984
Vehicle sales (units)					
Germany	787 591	708 446	-10%	945 384	+33%
Abroad	1 707 156	1 436 688	-16%	2 084 795	+45%
Total	2 494 747	2 145 134	-14%	3 030 179	+41%
Employment					
Germany	118 766	115 874	-2%	128 680	+11%
Abroad	99 060	77 703	-22%	95 934	+23%
Affiliates	40 104	44 776	+12%	44 130	-1%
Total	257 930	238 353	-8%	268 744	+13%

Table 5. Key figures of VW in comparison 1990–1993–2000 (compiled from Volkswagen 1991, Volkswagen 1994, and Volkswagen 2001)

	1990	1993	Change vs. 1990	2000	Change vs. 1993
Vehicle sales (units)					
Germany	945 384	935 989	-1%	1 018 923	+9%
Abroad	2 084 795	2 026 170	-3%	4 142 265	+104%
Total	3 030 179	2 962 159	-2%	5 161 143	+74%
Employment					
Germany	128 680	108 467	-16%	104 675	-3%
Abroad	95 934	102 434	+7%	160 274	+56%
Affiliates	44 130	40 742	-8%	59 453	+46%
Total	268 744	251 643	-6%	324 402	+29%

Table 6. Key figures of VW in comparison 2000–2005 (compiled from Volkswagen 2001 and Volkswagen 2006a)

	2000	2005	Change
Vehicle sales (units)			
Germany	1 018 923	1 019 000	0%
Abroad	4 142 265	4 174 000	+1%
Total	5 161 143	5 193 000	+1%
Employment (persons)			
Germany	104 675	101 028	-3%
Abroad	160 274	166 213	+4%
Affiliates	59 453	77 661	+31%
Total	324 402	344 902	+6%

Table 7. Shareholder structure of VW as of 31.12.2004 (adapted from Volkswagen 2005c)

Name of shareholder	Ordinary Shares	Preference shares	Total shares
Land of Lower Saxony	18.20%	0.00%	13.70%
VW Beteiligungs GmbH	13.00%	0.00%	9.80%
Brandes Investment Partners	10.70%	0.00%	8.05%
Others	58.10%	100.00%	68.45%
TOTAL	100.00%	100.00%	100.00%

Note: VW had two types of shares: ordinary shares with voting rights (75.27 percent of all shares) and preference shares with no voting rights (24.73 percent of all shares).

Table 8. Planned employee reductions at VW German plants 1993–1995 (adapted from Hartz 1994, 19)

Plant	1993 Actual Employment	1995 Target Employment	Targeted reduction
Wolfsburg	36 400	21 300	15 100
Kassel	14 200	10 700	3 500
Hannover	14 000	11 900	2 100
Emden	9 400	5 000	4 400
Salzgitter	7 800	5 200	2 600
Braunschweig	5 700	4 500	1 200
Others	15 700	13 300	2 400
TOTAL	103 200	71 900	31 300

Table 9. Votes on the EU takeover directive by country (adapted from Knudsen 2005)

Country	Number of Yes votes	Number of No votes	Percentage of Yes votes
Austria	4	14	22%
Belgium	5	16	24%
Denmark	13	0	100%
Finland	11	2	85%
France	45	26	63%
Germany	1	95	1%
Greece	2	21	9%
Ireland	10	2	83%
Italy	32	36	47%
Luxembourg	5	1	83%
Netherlands	9	22	29%
Portugal	19	1	95%
Spain	26	31	46%
Sweden	19	0	100%
UK	72	6	92%
TOTAL	273	273	50%

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