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Pioneering Modern Corporate Governance: a view from London in 1900

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Pioneering Modern Corporate Governance: a view from London in 1900.[1]

ABSTRACT.

Around 1900 Britain was exceptionally suited to pioneering large scale enterprises because of the precocious development of its equity markets and London's experimentation with a more eclectic range of corporate governance techniques than the world's smaller and less cosmopolitan financial centers. Information dissemination, incentives and reputation – developed by a serendipitous mix of legal compulsions and flexible voluntarism – set the scene for the growth of large, UK-based, national and international corporations in the twentieth century.

"The investment business is not with us as well developed or as well understood as it is in England."

Lyon, *Capitalization*, Boston, 1913, p. 207.

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I

The Chandlerian narrative, though rich in interesting detail on the development of organizational capabilities worldwide, went badly awry in its internationally comparative perspectives on the first half of the twentieth century in *Scale and Scope*.[2] It is now clear that some of its central drivers – British businessmen abnormally wedded to personal ownership and small management hierarchies, Americans quick to professionalize and divorce ownership from control, bank-guided Germans leading the move to large plants and firms, family enterprises unwilling to reinvest profits for growth, large manufacturing corporations as the main source of national differences in economic performance, and early twentieth century global oligopolies with pervasive barriers to entry by followers – are more than mildly problematic. These stereotypes – and those in the same tradition on France or Japan - have often failed to find support in representative, quantified samples, and, in some areas, the precisely opposite characterization has turned out to be more accurate.[3] Yet, from time to time, non-specialist economists and legal scholars still surface with attempts to explain why these things that did not happen in business history *must* have happened: the

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[2] Chandler*, Scale*. By contrast, his earlier internationally comparative perspectives on the M-form, diversification and integration - outlined in *Strategy and Structure* and developed with Channon, Pavan, Thanheiser and Pooley-Dyas in the 1960s (perspectives largely ignored in *Scale and Scope*) - have impressively withstood three tough tests: effectively explaining later business developments, widespread implementation in business schools and management consultancies, and critical scholarly analysis, see Whittington and Mayer, *European Corporation*.

[3] For a range of examples, see Berghoff, "End;" Broadberry, *Market Services*; Cassis, *Big Business*; Church, "Family Firm;" Colli, *History*; Dunlavy, "Corporate governance;" Fohlin, *Finance capitalism*; Fruin, *Japanese Enterprise System*; Hannah and Wada, *Miezaru*; Herrigel, *Industrial constructions*; James, *Family Capitalism*; Jones, *Evolution*; Jones and Zeitlin, eds., *Handbook;* Kinghorn and Nye, "Scale;" Miwa and Ramseyer, *Fable*; Owen, *From Empire*; Smith, *Emergence*; Wardley, "Emergence."

urge to explain what Chandler (and many others among us) wanted to believe is enduring.[4]

There has been some attempt to explain why key aspects of the Whig modernization myth that inspired these false perspectives proved so egregiously wrong, but the new perspectives leave many key questions unanswered.[5] Why – given the need for massive financial mobilization in their rapidly developing economies - were the Berlin or New York Stock Exchanges not as large, relative to their economies, as Paris or London? Why did France and Britain lead in divorcing ownership from control? Did that do the German or American economies any harm or was their higher level of personal ownership *actually an advantage*? (This perspective was instinctive to Adam Smith, and perhaps is again more digestible in our present age of private equity, than it was when the managerial modernization myth was at its height.[6]) On the other hand, did the quality of its corporate governance - or some other factor - explain why Britain's firms heading global oligopolies in the early twentieth century were initially larger and in the long run more sustainable than American and German ones?[7] This essay is intended as a contribution to what still remains for some a quaintly deviant activity: explaining British success. Central aspects of that success that still require explanation were the continued

[4] De Long ("Did J. P Morgan's Men") and Cheffins ("Mergers") attempt to show, among other things, why corporate IPOs and the divorce of ownership from control advanced further in the USA than in Britain before 1914, despite patient reminders from historians - every decade or so - that careful calibration of the facts suggest the opposite phenomenon is what requires explanation (see Davis, "Capital markets;" Sylla and Smith, "Information;" Hannah, "Divorce").
[5] Lamoreaux et al ("Against"); Clark and Trebilcock (*Understanding Decline*); and Hannah ("Whig fable") sketch explanations. One of the most striking reversals of perspectives is David Landes's recent *Dynasties*, a volume that does not sit easily with the Whig modernization theory he earlier imbibed at Harvard's postwar Research Center in Entrepreneurial History (compare his "French entrepreneurship.")
[6] Compare Jensen, "Eclipse."
[7] Hannah ("Marshall's trees," pp. 264-5) presents an alternative hypothesis to that explored here, suggesting that their international exposure and lack of tariff protection may be factors distinguishing British 1912 giants from their less successful American and German counterparts. The latter suggestion would be more plausible if it could be shown that British corporations reverted to lower growth and survival rates when the British aped American and German protectionism from 1932 onwards.

development of London as the largest stock exchange in the world in the early twentieth century and Britain's – perhaps not unrelated – hosting of an (above-par) number of large, quoted – and generally managerial and multinational - corporations that performed better over the century as a whole than the (somewhat below-par) performance of the economy in which they were headquartered.

II

Around 1900 Britain had similar real *per capita* GDP to the United States, but was little more than half the latter's economic size.[8] Some of its business activities were nonetheless more developed than its modest size would lead one to expect. Most spectacularly, it already derived most of its income from the service sector, more than half a century before that happened in the USA, and that despite *also* employing a higher percentage of its (smaller) labor force in manufacturing than Germany, France or the USA.[9] One key to British exceptionalism, driving its extreme specialization, was its unilateral commitment to free trade, which, in turn, had fueled the downsizing of agriculture and the precocious size and global reach of its financial sector. In 1902, toward the end of a massive company flotation and merger wave that still left the total of NYSE-listed securities at only $14 billion, listings on the London Stock Exchange were more than three times that level, with a value of $43 billion.[10] Issuing capital to public

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[8] Maddison (*World Economy*) suggests that in 1900 the UK had 2.6% of the world's population and 9.4% of the world's real GDP, against 4.9% and 15.8% for the USA. Maizels (*Industrial Growth,* p. 220) suggests that in 1899 it had 20.8% of the world's manufacturing production, compared with 40.6% for the USA.

[9] Lewis, *Growth*, p. 263; Bairoch et al., *La Population active*, pp. 53, 83, 96, 98.

[10] Pratt, *Work*, pp 81-2; *Stock Exchange Official Intelligence 1902*, p. 1098. These are par values; at market the US deficit would have been even wider, because of the greater prevalence of stock watering there. Even

investors was cheap for British companies. In 1870-1913, when the dominant issues on most stock exchanges were railways, British railway bonds yielded 3.7% and equities 4.3%, while, in the more capital-constrained USA, railroads paid 6.0% and 8.4% respectively.[11] London was a rich, mature savings market with a wall of money avidly searching for higher-yielding investments. Its apparently insatiable capacity to absorb imported food, raw materials and semi-manufactures created massive investor opportunities, in overseas development and trade, as well as at home.

Limited liability, joint stock enterprise - facilitating low-risk contracting between investors supplying funds and businesses requiring finance - had clearly made more progress in Britain than in continental Europe. Britain in 1900 had about 30,000 joint stock companies, probably as many as all the rest of Europe put together: Germany, for example, had only 5,400 *Aktiengesellschaften* in an economy with a larger population and roughly the same GDP as Britain's.[12] We cannot easily compare these figures for European corporations with American data, since comprehensive federal statistics for this period are lacking, but we know from the federal censuses that all US *manufacturing* corporations operated 40,743 establishments in 1899 and that there were 5,386 incorporated *mining* businesses in 1902.[13] It is likely that the total number of US

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if clearly international securities (in which London excelled and the NYSE was hardly a player) were excluded, London was larger.

[11] Edelstein, "Foreign Investment," p. 198.

[12] Wagon, *Finanzielle Entwicklung*, p. 7, for Germany. Somary, "Statistik" gives a total for around 1900 of 25,864 companies in continental Europe excluding Scandinavia, Iberia and the Balkans. A general problem in interpreting these statistics is that, in some countries, in sectors like railways, banks or utilities, companies could be formed outside the general company legislation to which the statistics are sometimes confined.

[13] United States Census Office, *Manufactures,* p.lxvi; Department of Commerce, *Mines and Quarries*, p. 78. The mining figure is the actual number of corporations but the total of manufacturing corporations will be less than the figure given, because one corporation may own more than one establishment. In 1954, the number of manufacturing corporations was 74% of the number of manufacturing establishments (Carter et al., ed., *Historical statistics*, 3, p. 559). Multi-unit enterprises probably increased their share overall by 1954, but the 1899 census was the last to include incorporated handworking establishments and other

incorporated enterprises for 1900, including the agricultural and service sectors, was somewhat in excess of 60,000.[14] If that guess is about right, then about half – and quite possibly more than half - of the world's corporations in 1900 were in the USA and nearly a quarter in the UK.[15] The prodigious spread of incorporation in Britain and America was no doubt partly because these countries were wealthy and innovative, but the flexibility of Anglo-Saxon common law compared with the Roman law commercial codes that dominated elsewhere may also explain it.[16] Whatever the reason, in the first decade of the twentieth century only a minority of German workers were employed by companies of any kind (AGs, GmbHs and Gewerkschaften), whereas a majority of workers in the USA, UK and Belgium were already employed by joint stock companies.[17] Germany remained pre-eminently a land of personal proprietorships and partnerships, where *Handwerk* and small-scale traditional firms still out-distanced its "modern" corporate enterprises.

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marginal producers, so around 75% may be a reasonable ratio to apply then too. That would put the number of manufacturing corporations at 30,557.

[14] What is required is a grossing up of the total of 35,943 mining and manufacturing corporations (estimated for around 1900 in the previous footnote) by an appropriate factor. Using the ratio of mining and manufacturing corporations formed in New Jersey, Ohio and Pennsylvania in 1890-1900 (16,967, see ibid pp. 541-547) to the total number of corporations so formed (29,360) as the factor produces an estimate of 62,196 for the whole USA. The first reliable federal statistics on corporations derive from the 1918 tax statistics, at which date there were 273,923 active corporations of which 77,935 were in manufacturing and mining (Ibid, p. 496). Using that ratio to gross up would produce a much higher 1900 estimate of 126,331 corporations in all sectors. The difference is substantially the consequence of the larger proportion of financial, retail and wholesale corporations at the latter date. Either financiers and retailers incorporated more prolifically in 1900-1918 than earlier, or New Jersey, Pennsylvania and Ohio had few financiers and retailers in 1900. The former seems more likely: hence the first estimate is preferred in the text, though the fact that there were 13,000 banks alone in 1900 suggests it may be an underestimate if most were incorporated.

[15] There were 1,340 companies in India, 4,254 in Japan and many in Canada, southern Africa, Australasia and elsewhere to add to the European figure of in footnote, though China had no limited liability law until 1904.

[16] Some modern literature (Klapper, Laeven and Rajan, "Business Environment") emphasizes the speed and cheapness of the company registration process as a determinant of international differences in new business formation. As far as I know, there is no similar historical comparison of costs or speed of company registration. It is possible, also, that national variations in bankruptcy laws made limitation of liability more attractive in some countries than others.

[17] Liefmann*, Unternehmungsformen*, p. 49; Stamp, *British Incomes*, p. 215.

The USA's precociously ample embrace of incorporation was also distinctive in that many of its corporations were effectively "private companies," with small numbers of shareholders, whereas Europe's incorporated enterprises were more likely to be quoted on a major stock exchange. Only 0.2% of our estimated total of America's corporations were in 1900 listed on the New York Stock Exchange (with perhaps a further 0.1% trading in the unlisted department), while the equivalent proportions for London were around 12% traded (with perhaps half those officially listed), for Brussels at least 12% officially listed and for Berlin at least 13% officially listed.[18] Of course, enterprises that had incorporated without dispersing share ownership were known in most countries (and in Germany had been given a separate legal designation since 1892 as GmbHs rather than AGs), but such personal and family enterprises appear to have been especially numerous among the incorporated businesses of the United States.[19]

However, other markets - regional stock exchanges, the New York curb, the New York Consolidated Exchange and over-the-counter markets - were probably of greater importance relative to the main metropolitan stock exchange in America, though over a hundred provincial exchanges also existed in Europe and dozens in Japan. Some of the apparently large transatlantic differences in the propensity of corporations to issue

[18]The London 12% figure is based on the assumption that only 10% of the companies listed in the *Stock Exchange Official Intelligence* were foreign-registered companies (as opposed to British companies operating at home or abroad). For officially listed companies operating in the domestic economy the proportion would be only 2%. The large difference between that and the 12% above is British-registered companies primarily operating abroad and provincially quoted companies not officially listed in, but tradable in, London, both types being in the denominator of 30,000, quoted and unquoted, British-registered joint-stock companies. No allowance is made in the German or Belgian figures for companies registered in those countries but operating overseas or for any metropolitan trading of provincially listed securities.

[19] The number of GmbHs was 4077 by 1900 (Wagon, *Finanzielle Entwicklung*, p.165). The 1907 British Companies a Act also formally recognized the private limited company, an equivalent of the GmbH, with less onerous reporting rules than for public companies. Such a separate form was not required in America because reporting rules were not stringent anyhow, so "private" companies disclosing little had evolved there (as in nineteenth century Britain) without special legislation.

publicly traded shares is a reflection of the underdevelopment of the New York Stock Exchange relative to rival American securities markets, but it is unlikely that allowance for that would invalidate the general picture of rather late-developing US stock markets, with fewer companies formally listed on major exchanges than in Europe, and an abnormally long tail of essentially private companies.[20]

European – and especially British - companies were also more internationally orientated than those of the United States. The pound sterling, British banks, insurers and accountants, and the English language and corporate and contract law were all widely used by businesses overseas, sometimes in locally modified form (there were separate incorporation procedures in British Empire countries such as Australia, Canada, Hong Kong and India, whose locally-registered companies are excluded from the British totals reported earlier), sometimes directly (British-registered "free-standing" companies operated in some continental countries, the USA, Malaya, Japan and Argentina, almost as freely as they did at home).[21] London had twice the population of New York partly because it was more of a world city. For example, more than half of all banks operating there in 1900 were foreign (or British-owned but primarily operating overseas) and half the world's stock of multinational investments originated from the

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[20] The evidence in Table 1 below suggests that exclusively provincial quotations would add only 22% to the London total market values of securities in brewing in 1900, but in other securities, like domestic rail and foreign companies, London was more dominant. 930 of the 5,400 German AGs (17%) were quoted on *all* German exchanges compared with 13% in Berlin alone, suggesting around a quarter (by number, possibly less by value) were exclusively provincially quoted (Wagon, *Finanzielle Entwicklung*, pp. 7, 175-21). I have not been able to locate any comparable estimate for the USA in 1900 but, for 1928-34, Berle and Pederson (*Liquid Claims*, p. 220) thought that stocks and bonds listed on *all* other US exchanges would be a little less than the total value of the securities of NYSE-listed companies. If that held for 1900 (though rail stocks, in which the NYSE specialized, were much more dominant then), that would make the NYSE clearly less dominant nationally than Berlin or London. "Over-the-counter" trading in most markets is an unknown quantity, but may also have been especially large in America.

[21] "English" rather than "British" law because Scotland preserved an independent, Roman-law-based, legal system. However, in corporate matters, Roman-based Scottish law closely mimicked English: a warning not to over-interpret the alleged restrictiveness of legal doctrine! On the same theme, demonstrated by Franco-American comparison, see Lamoreaux and Rosenthal, "Legal Regime."

UK.[22] Tariff-free Britain was a massive importer of raw materials and manufactures, as well as the world's largest exporter of manufactures, and free-trading Britons were, understandably, adventurous travelers.[23] The securities of more than four thousand companies traded in London – compared with only 200 on the New York Stock Exchange and around 800 in Berlin - but in Germany (and, even more, in America) they were overwhelmingly domestic, while in Britain many – possibly the majority - were companies (both British-registered and foreign-registered) operating primarily overseas.[24]

The problems of corporate governance raised by the public quotation of corporate securities and the associated divorce of ownership from control were, then, both exceptionally numerous and exceptionally international in London around 1900. They were also addressed by an unusually polyglot and experienced population of business leaders. Many British businessmen had been born abroad or had overseas experience. British citizens were in the early twentieth century directors of firms as diverse as Milwaukee & Chicago Breweries, Eastman Kodak, the Anglo-Californian Bank, International Nickel, British-American Tobacco, Canadian Pacific, Van den Bergh Margarine, Gebrűder Siemens, Apollinaris, Dynamit-Trust, Sankt Pauli Brauerei, Société Générale, Compagnie Internationale des Wagons Lits, Compagnie des Chemins de Fer du Nord, Compagnie Universelle du Canal Maritime de Suez, Baku Russian Petroleum, Burma Ruby Mines, Hongkong & Shanghai Bank, Standard Bank of South Africa, Great

[22] Lawson, "Lombard Street;" Whitaker, *Almanack*, pp. 291-296, 310-320. Dunning's estimate of international investment for 1914 suggests a 46% British share, but it is likely that there had been some catch-up – for example, by German and American multinationals - by then.

[23] See, for example, *Japan Weekly Mail*, 6 January 1900, pp. 20-21, for their dominance of the expatriate western community in Japan.

[24] 783 domestic companies were officially listed on the London Stock Exchange at the beginning of 1900. More than four thousand companies were listed in the *Stock Exchange Official Intelligence*. The difference is accounted for by companies mainly operating abroad (many officially listed) and provincially listed companies (which could also be traded by a London broker).

Indian Peninsula Railway, El Aguila , Central Uruguayan Railway, Waikiki's first hotel and the Kirin Brewery. By the same token, London – then, even more than now - was the favored second (and sometimes first) home for the affluent bourgeoisie of the rest of the world.[25] The British port authorities had long ago stopped inspecting passports (though traveling businessmen still found these documents useful for collecting *poste restante* mail and as introduction cards). Many wealthy Americans, like the banker J. P. Morgan or the industrialist George Eastman, liked to spend some of their spring or summer in London, while rich colonials like Cecil Rhodes or Max Aitken also found outlets for their wealth and talents there.

Despite the threatening froth of nationalism and imperial rivalry, Germans (and - less frequently - other Europeans) were also welcomed among the foreign-born in British boardrooms, including those of leading companies like the Bank of England, Vickers, the Union Bank of London, Brunner Mond, Nobel Dynamite, De Beers, GEC, Shell and Rand Mines. Corporate boardrooms - in Britain and worldwide – would, after the disaster of 1914 and its aftermath, not again benefit from such cosmopolitan diversity until the 1990s. While now the appointments of a Briton to head a Tokyo corporation or a German to lead a Detroit one retain some power to occasion surprise, their predecessors in the early twentieth century went largely unremarked in the cosmopolitan stride of that era. Britain's (and Europe's) largest industrial, J & P Coats, manufactured sewing cotton at its Scottish base and in dozens of subsidiary factories globally; its (German-born) managing director, O. E Philippi, was trusted by the Clark and Coats families and 25,000 other public shareholders (the company had been listed on London since 1890) to direct

[25] In 2006, London still had more of the world's billionaires as residents than any other city, though this is now probably more related to tax issues than it was in 1900 (when New York was the leading income tax haven, albeit unattractive to rich Europeans).

its global operations from its London sales center and was widely respected in British business circles. The US-headquartered Singer Manufacturing Company – making the machines that used Coats' sewing cotton – closely paralleled Coats' extensive global manufacturing and sales operations from its iconic new Manhattan skyscraper. In 1905, the (American) Clark and Proctor families asked their (British) vice-president, Douglas (later Sir Douglas) Alexander, to take over as Singer's president (the founders' heirs still dominated the 150 holders of Singer's unlisted stock, which traded only intermittently on the curb).

At a time when it took sixty days to travel round the world and international communication was by cable, not the more natural telephone, in such cases the social cement of a relatively homogeneous, international elite of merchants and businessmen, with a common European cultural heritage, no doubt aided global business development and interactions. Modern historians may retrospectively date "the strange death of liberal internationalism" to the turn of the century period, and symptoms were certainly visible, but tens of thousands of entrepreneurs, merchants, financiers, managers and clerks in leading port cities like New York, Yokohama, Shanghai, Bombay, St Petersburg, Hamburg, Rotterdam, Brindisi and London inhabited a cosmopolitan networked world where such forebodings seemed preposterous.[26] A key parameter in the emergence of the separation of ownership from control in securities markets - trust - is essentially unobservable. Yet, for pioneering industrial shareholders - whether more widely dispersed like Coats or in closely held firms like Singer - the demonstrated competence of top business professionals like these, bound together by shared loyalties,

[26] Compare Bayly, *Birth,* pp. 464-467, with Beerbűhl and Vőgele, eds, *Spinning the Commercial Web.*

norms and obligations derived from common commercial experiences, made their fiduciary role as boardroom trustees for the owners appear unproblematic.[27]

Foreign-born directors in London sometimes chose to adopt British nationality, though there was little overt pressure from the natives to do so of the kind travelers and businessmen in America sometimes complained of, though there were inducements for the wealthy and socially ambitious. With suitable charitable or political contributions, citizenship might be followed by a knighthood from the monarch (whose own surname was, after all, Saxe-Coburg-Gotha, until it was pointedly changed, in less happy times, to the un-Germanic Windsor). The mining financier, Alfred Beit, of Portuguese Jewish descent, was born a German Lutheran in Hamburg. After early experience with Dutch and French firms, he made his fortune in the Cape Colony and the Transvaal Republic, where his and Cecil Rhodes' insurrectionary conspiracy to overthrow the Boer government failed in 1895. His uncle, Ferdinand Beit, was one of the founding financier-chemists of the leading German dyestuffs manufacturer, BASF, but Alfred chose to establish what became the world's leading mining finance house, Wernher Beit, in London. As a naturalized British subject, he had a house in Park Lane to complement his Hertfordshire country mansion. Endowing British, German and South African universities, Sir Alfred Beit, company director and financier, remained on friendly terms with the Kaiser, dying in 1906, worth ₤8 million ($39 million). It is not easy to brand such a *Weltbűrger* by mere nationality.

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[27] Though the border between the corporate and the personal, particularly in closely-held firms like Singer, was then weakly drawn, see Bruland ("Babcock & Wilcox") for evidence that Singer directors used the company's manufacturing facilities to develop business for a company in which they personally (not Singer) held stock, behavior that would now be considered fraud on the outside stockholders.

The fundamental issues that had to be addressed in governing companies and mediating their relationship with the providers of capital were, of course, not wholly different in Germany, the USA, the Transvaal or Britain. If – as the evolutionary theory of the firm suggests – competition and diversity are two prime requirements for benign long-run outcomes of institutional experimentation, then the London of 1900 could credibly claim the world's richest commercial "gene pool" from which to start. It hosted a broad-based society of financial and organizational tinkerers, that (unlike the parallel universe of engineers and chemists transforming the material world) could hardly yet be matched by rival business centers; though on some dimensions Paris, Brussels and even Berlin came nearer to it than the – culturally diverse but more nationally blinkered – financial community of New York. Information, incentives and reputation were – as theory suggests they should be - at the heart of the solutions these men found and applied in London and worldwide. Cosmopolitan London was well aware that they were not addressed by identical methods everywhere and the wide range of economic actors – shareholders, stock exchanges, legal and accounting professionals, company boards, financiers and governments - that shaped the emerging global system of corporate finance centered on London did not suffer from a "not-invented-here" syndrome. There was extensive experimentation and foreign companies, banks and nationals could - and did - operate freely in London. One of Sir Alfred Beit's main competitors in South African mining finance, for example, was General Mining and Finance, the London vehicle of Dresdner Bank.

III

However, one institutional innovation central to resolving information asymmetries, and later widely adopted globally, was essentially British in origin and – in marked contrast to experience on the more regulated continent – essentially voluntarist. The remarkable late nineteenth century growth of external auditing of British companies was the work of professional accountants under the self-regulating auspices of the Institute of Chartered Accountants of England & Wales and of similar self-governing professional associations in Scotland and Ireland. When chartered in 1880 the English institute alone had 587 members and by 1901 this had grown to 2,831, though some worked overseas.[28] Whether working in America, China, France, South Africa, Australia or Britain, they had a rapidly growing workload. The number of companies listed in the *Stock Exchange Official Intelligence* - many British-registered and with securities listed on the London Stock Exchange, though also some foreign-registered listed companies and others provincially listed and dealt in only "over-the-counter" in London - grew from 1,585 in 1885 to 2,581 in 1895, 4,166 in 1901 and 5,337 in 1915.[29] In 1901, the president of the English institute reported that 75% of these companies were audited solely by his members, a further 4% partly by his members and 8% by members of the Irish and Scottish institutes, leaving only 13% (many of these French and American companies) audited by individuals, the corporations themselves or non-members. It is

[28] Fisher, "President's address," p. 1107. There were also thousands of uncertificated book-keepers (who also dominated the USA), as well as members of other regional or specialist professional accounting bodies, see Broadberry, *Market Services*, pp. 122-7. The absolute number of accountants in the USA did not overtake Britain until the 1920s and remained lower proportionately to population.
[29] Ibid., p. 1109; Jefferys, *Business Organisation*, p. 456. The 1901 count omits the small number of (mainly American) firms which named no auditor.

evident that this represents a relatively high degree of both professionalization and externalization of corporate auditing.

The ubiquity of the British company audit, though eventually reinforced by legislation, was largely achieved by the voluntary compliance of company boards, particularly in industry. The British Companies Acts had included model articles - requiring the presentation of an audited balance sheet and profit statement to the annual general meeting of shareholders - but these were purely advisory: it was a simple matter for a lawyer setting up a limited company to omit that clause, and many did. In the last third of the nineteenth century, some businesses – notably railways, regulated utilities like gas and electric companies, and banks – were, by legislation or tacit agreement (motivated by various, separate public interest considerations) required to publish accounts, in Britain (as often elsewhere). Yet the remaining London-listed British companies (and many foreign ones listed there) – who were not so compelled - nonetheless did so voluntarily before 1900.[30] This process had been considerably assisted by Sir Henry Burdett, secretary to the London Stock Exchange from 1881. His annual letters to companies, at home and overseas, including some quoted in the provinces, requesting copies of accounts, were a constant reminder of the desirability of providing timely information to shareholders. Even some large unquoted companies (apparently ones contemplating an IPO) were sufficiently impressed by his missives to send typewritten copies of their confidential accounts. The extensive archive of several

[30] Railway companies were legally required to publish accounts in 1868, life insurers in 1870, gas utilities in 1871 and electric utilities in 1882, while even private retail banks tacitly agreed to do so by the 1890s ("the Governor of the Bank of England's eyebrows" and threat of legislation being sufficient). In the USA the Interstate Commerce Commission, the Comptroller of Currency and various state regulatory bodies achieved much the same in these sectors. The main distinction in Britain was that *external* audit was typically required, whereas in the USA the companies' own staff often undertook the work. In both countries, the securities subject to compulsory disclosure were then the bulk of domestic securities quoted on their major stock exchange by value (though perhaps not, in London, by number).

hundred thousand British and foreign company accounts now held at London's Guildhall Library is a permanent monument to his labors.[31]

Companies had for several decades been required by the London Stock Exchange Listing Committee to publish accounts as a condition of new issues (a practice not emulated by the NYSE until 1895).[32] Sometimes, it is true, the Listing Committee winked. Unlike their modern descendants, they had no extraterritorial ambitions: foreign companies seeking a listing were allowed simply to comply with their own - sometimes lower - local standards (US and French companies generally kept to their own standards, but Australasian, Transvaal and Argentine companies, perhaps realizing the advantages for raising capital, often fell in with the London rules). Even for domestic companies, the committee did not require accounts publication of some breweries and shipping lines that only issued debentures and preference shares to the public. This was presumably on the ground that there was sufficient security on these companies' extensive real estate holdings (pubs) and (equally foreclosable) ships for profits in excess of fixed interest

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[31] Duguid, *Story*, p. 351. Burdett left the Exchange acrimoniously at the end of the nineteenth century to pursue a (not very distinguished) career as a company director, but his work was carried on by the professional team he had built up, who, after 1900, also had the option of a quiet word with the Registrar of Companies to initiate prosecutions of some non-compliant companies. Comments in this and subsequent paragraphs are based on the British and foreign accounts in the Guildhall Library collection. I examined the accounts for various dates between 1899 and 1912 of the largest 52 UK industrials (as listed in Payne, "Emergence"), some major American, French and African corporations, and an unsystematic sample of smaller company annual reports and accounts.

[32] The NYSE undermined its own authority by allowing stocks of non-compliant companies to trade in its "unlisted" department (established in 1885 and not abolished until 1910). There was a supplementary list in London, too, with lighter requirements, but some of the largest American industrial companies were in the New York unlisted department, while the London official list had massively greater listed company numbers and almost all large firms were in it. I do not know of any surviving copy of the supplementary list, but companies in the *Stock Exchange Official Intelligence* whose names were not published in the *Stock Exchange Daily Official List* were presumably either in the supplementary list or traded "over-the-counter" by London brokers.

reasonably to be a private matter, disclosed only to the (unquoted) ordinary shareholders.[33]

Yet when the British state did finally – some time after their continental equivalents, though long before the USA - require more from all companies, this affected only a relatively small rump of recalcitrant London-listed companies. Legislation in 1900 required companies to appoint auditors, who could not be employees or directors, to prepare accounts, and present them to shareholders attending the AGM. Wider publication was not legally required until 1907, when balance sheets had to be filed annually with the Registrar of Companies.[34] Profit statements were not required until the 1929 Companies Act, though, since the balance sheet disclosed reinvested profits and distributed profits could be deduced from the dividends, this was an insubstantial omission. In fact, all but a few (and those mainly breweries) of Britain's largest domestic industrial companies by 1900 published a balance sheet and profit and loss account and some laggards had fallen into line by 1907. By contrast in the United States, 43 of the largest 100 industrial companies did not even publish a balance sheet in 1900, while in continental Europe industrial companies - typically required by their national commercial codes to present accounts to shareholders at an earlier date than in the common law countries – often did not use trained, external, accounting professionals to comply.[35]

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[33] *Economist,* 12 April 1902, pp. 565-566, for criticism of Ind Coope directors for not publishing accounts. Other large breweries still refusing to publish accounts were Courage, Barclay Perkins, Bass and Worthington, though Worthington did disclose profits in an annual circular, see *Investor's Review*, 8 December 1900, p. 721.

[34] For *public* companies only, and this part of the law only applied to newly registered public companies, so many pre-existing *public* companies (or newly registered *private* companies) still published balance sheets voluntarily or because of Stock Exchange listing requirements, not because of state compulsion.

[35] Bunting, *Rise*, pp. 16-19, 155-156; Fear and Kobrak, "Diverging Paths." Given the greater size of the US economy, Bunting's American top 100 companies turn out to be the roughly equivalent size range to

The *quality* of the reported accounting information is less clear. It is logically possible that British businessmen who published accounts at the behest of the Stock Exchange (or later the government) did so feeling they could now more perfectly bamboozle shareholders by publishing false information than by publishing none at all, even though that was clearly not the intention of the Stock Exchange Listing Committee or the professional accounting bodies. Historians of British accounting certainly dwell on the shortcomings of what was published and there is no reason to dissent from Arnold's decidedly lukewarm judgment, based on checking the published shareholder accounts against the internal management accounts of 30 British companies, that corporate disclosures of the time, though "not as poor as they might have been", were *sometimes* "uninformative and misleading."[36] Part of the problem was that external auditors, though formally appointed by the shareholders in the annual general meeting, in practice were chosen by the directors. They were no doubt – within the capacious limits of their professional standards - somewhat biddable.[37] Depreciation accounting rules were not well developed and there remained a wide range of allowable treatments; holding companies were not required to consolidate the accounts of subsidiaries; directors could create secret reserves by understating profits in good years, raiding them - without disclosing this - in bad. Some companies notoriously observed only the letter of the law (it was a requirement to publish a balance sheet every year, but the law did not until 1928 specify that it had to be a new one every year!).

Payne's top 52, on which I base my comments on Britain. By the time the US compelled publication in 1933, the level of voluntary/NYSE-induced compliance, of course, had grown and was similar to that achieved in Britain in the early 1900s.

[36] Arnold, "Publishing." See also Hannah, "Takeover Bids;" Lee, "Company Financial Statements;" Edwards, *Company Legislation*, pp. 3-5, 12-13; Kennedy, *Industrial Structure*, pp. 125-6. Of course, apart from weaknesses in contemporary accounting standards, some auditors were plain incompetent, as cases such as Dumbell's Bank and the London & Globe scandals of 1900 showed.

[37] Ingall and Withers, *Stock Exchange*, pp. 124-131.

Plainly, this was not a world of rigorously prescribed *rules* (such as modern regulators impose in onerous detail), but it was a world of shared *values* or *standards* (that is, broadly understood norms of good practice which directors and accountants – and sometimes, *in extremis,* judges – could be expected to enforce). We perhaps underestimate the power of Victorian cultural norms of professional, reasonable and fair behavior in enabling securities markets to work effectively, even with what by modern standards appear as poorly articulated disclosure laws and investor protections.[38] The great majority of companies in fact published more and better information than was legally required and, in the absence of evidence to the contrary, this was treated by contemporary investors as broadly accurate. Shareholders would rationally peruse company accounts with some skepticism, but that externally audited accounts conveyed some information – and that directors generally and willingly used them to signal their more-or-less-honest views on the sustainability of declared dividends – were taken for granted. The informational content was weak, if judged against a hypothetical ideal, but it was not nugatory. Significantly, scholars making *comparative* rather than absolute judgments, have usually ranked British disclosure standards highly in the period around 1900: Sylla and Smith, for example, conclude that Britons then had "the best information possessed by any investors anywhere."[39] The editor of the *Wall Street Journal* agreed, warning British investors in 1900 of the exceptionally poor disclosure even by recently

[38] Compare Coffee, "Do Norms."

[39] Sylla and Smith, "Information," p. 190; see also Hawkins, *Corporate Financial Disclosure,* for evidence this view was shared by contemporary Americans, worried by the failure of their own legislators and others to match it. Kobrak and Fear ("Diverging Paths," pp. 16, 21) also suggest limited German external audit capacity/quality in this period. It should be noted, however, that we do not, as far as I know, have overseas studies of the quality of Arnold's UK study, so it is difficult to make such comparisons authoritatively.

floated American industrials that did publish accounts: "their annual reports are nothing but mockeries - with a very few honourable exceptions."[40]

Most of the thousands of company accounts published annually in Britain were also in a reasonably standard form: remarkably whether for a railway worth hundreds of millions or for a one-million-pound restaurant chain. They consisted of a balance sheet with some breakdown of assets and liabilities and a profit and loss account showing broad aggregates and their allocation (but not, typically, what were still considered commercially sensitive matters like sales revenue). Published accounts only rarely exceeded four pages and the reports generally did not contain extensive or detailed remarks on the company's business, but that was sometimes the subject of the chairman's AGM speech, usually reported in the press and often also circulated to shareholders. Few British companies provided the impressive mass of operational and financial detail that was given from 1902 in the published accounts of US Steel (prepared by the British accountants, Price Waterhouse), though that steel giant was then also a somewhat exceptional US firm, assiduously courting the role of the "good trust."[41] Against the case of America's largest industrial firm stood its second largest, Standard Oil, quoted only on the curb until 1920 and publishing no information on its assets or profits save its capital stock and annual dividend. It was what was known at the time as a "blind pool" - accounts were a private matter for the Rockefellers and other directors, not available to mere stockholders – and, as we have seen, many American industrials followed this

[40] Letter from Thomas F. Woodlock, dated 20 December 1900, published in *Economist*, 5 January 1901, p.15.

[41] Among those in London with comparably extensive detail in reports published around the turn of the century were some South African mining firms, while railways and utilities disclosed information on sales and other issues (sometimes through other disclosures than the annual report) on a regular basis. French reports and accounts in the Guildhall collection are more extensive than the *average* British one.

approach. There was something to be said for the standard British norm, most obviously for investors interested in making comparisons between possible industrial investments.

This is palpable in the financial journalism of the time. The ethics of financial journalists in the early twentieth century - worldwide - are not a topic for the squeamish, but occasionally periodicals and newspapers rose above the venal norm. The range and quality of discussions of corporate accounts data – on matters like the degree of interest cover for preference dividends or long-run industry trends in rates of return – in British journals aimed at investors - the *Economist, Statist* and *Investor's Review* - were, in my judgment, higher than in New York's *Commercial and Financial Chronicle*.[42] This favorable view of London information sources is not universal: Nicholas, for example, believes that in New York "independent investor services like Moody's and Standard and Poor's provided an antidote to asymmetric information," an advantage he thinks London lacked.[43] However, that optimistic interpretation requires an unsupported faith in these publishers' ability to do more than collate the, often inadequate, accounting information disclosed by American industrials.[44] Probably more significant

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[42] This judgment is based on a complete reading of three years' issues of the four journals for 1900-1902. In January 1900, for example, the *Commercial and Financial Chronicle* contained serious comparisons of the accounts only of US banks and railways, while the *Economist* had comparative, accounts-based, articles on UK stores and trading companies, leading domestic industrials, London dock companies, Australian railways and "Westralian" mining; while the *Statist* excelled, with articles on the accounts of Rand gold mines, "Westralians," Indian mines, Australian hardwood companies, colonial life insurance and UK railways, life insurance, fire insurance, banks and coal mines. The *Investor's Review* published some similar articles (for an example in brewing see Table 1 below), but added a distinctive approach in regular articles analyzing shareholders' registers, with a view to diagnosing potential moral hazard from insider dealing by directors or large shareholders.
[43] Nicholas, "Enterprise," p. 236.
[44] The published Moody and Poor volumes for the early twentieth century USA sometimes point to the absence of accounts for industrial companies, occasionally guessing at what such accounts might have contained. It is not obvious that such guesses were superior to information derived from externally audited accounts in comparable British concerns. A perusal of John Moody's autobiography (*The Long Road*) betrays no convincing secret weapon, beyond a principled unwillingness to accept a bribe from American Tobacco for falsifying information and insider gossip at the Waldorf Astoria. There were honest men and hotels in London, too. The Poor and Moody volumes have one clear advantage over their London counterparts, Burdett and Skinner, in that they report far more accounting details for companies that *did*

for well-informed specialists were the confidential trade reports on corporate creditworthiness of Dun & Bradstreet, but these were, of course, paralleled by Seyd's subscription credit rating service in London.[45]

Accounts were the most visible means of information transmission in the financial markets, but that does not necessarily mean that they were the most important. Mining engineers and geologists, for example, were a source of external information on the mining market, a sector chronically prone to misinformation. Lawyers also played a part. One of the leading City law firms, Slaughter & May, had learned the hard way from judicial criticism in the early 1890s of the dangers to their reputation of dubious stock exchange dealing. The partners were, thereafter, scrupulous in their insistence on fair disclosure to shareholders on the boards on which they sat.[46] Another City law firm and other professionals provided more direct advice and diversification services for investors by launching successful investment trusts.[47]

For other information channels so much of what happened can only be guessed at. When an IPO was oversubscribed, vendors and promoters often gave preference to the suppliers or customers of the floated firm, not only cementing their loyalty but incidentally increasing the trade knowledge of the average shareholder. As it was also common for the promoters and/or vendors of enterprises to remain on the board after a public issue, often retaining a major shareholding, it is likely that they also monitored the share price with some knowledge and interest. Such insiders and trade

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publish accounts, but this simply reflects the fewer corporate quoted securities American directories had to cover, and specialist publications (Duncan on breweries, Rylands on coal, iron and steel, Garcke on electricals etc) proliferated for similar coverage in Britain.

[45] Seyd's confidential archives do not appear to have survived, unlike Dun & Bradstreet's (in the Baker Library, Harvard Business School), but their limited print versions circulated to subscribers are available as copyright deposits in the British Library.

[46] Dennett, *Slaughter*, pp. 98-105, 120-125.

[47] McKendrick and Newlands, *"F & C,"* pp. 13-19.

investors may have been inclined to sell when they considered the share price too high and to buy when they considered it too low. The range of information they used in making such decisions would, of course, have been wider, deeper and more timely than that incorporated in the published annual accounts. This would have had the desirable effect of aligning share prices with underlying values, increasing confidence in the share price as a conveyor of information. The concern that more ill-motivated insider dealing (in corners and ramps) might have the opposite effect appears to have been less an issue in London than in New York, perhaps because some technical differences between the markets made such behavior less prevalent in London.[48]

There is also some evidence that banking firms like Rothschilds played a role in share price formation for large internationally traded stocks like Anaconda, Consolidated Goldfields and Rio Tinto (in which they were significant investors), monitoring London Metal Exchange prices and share quotations in New York, Paris and London.[49] For many smaller stocks, the survival of vigorous provincial exchanges in this period also argues for local networks remaining a significant source of business information. The London market provided a pool of liquidity for the larger provincial issues, but parallel trading on the provincial exchange facilitated information inputs from local investors with more expert or insider knowledge. Hence the Liverpool Stock Exchange specialized in shipping and insurance, Manchester in textiles, Birmingham in bicycles, Glasgow in iron and tea, Sheffield in steel and so on. More distant exchanges also played a tributary role, signaling their special expertise and contributing to London

[48] Michie, *London and New York*, pp. 266-7. Sylla and Smith ("Information," p.195-97) interpret the contemporary opposition of some in the Wall Street oligarchy to higher accounting standards, as motivated by a desire to preserve their profits from insider information.
[49] Ferguson, *World's banker*, pp. 876-81.

price formation: Toronto for Canadian industrials, Johannesburg and Sydney for mining, New York for American rails, Alexandria for Egyptians, Buenos Ayres for Argentines, Paris and Brussels (as well as St Petersburg) for Russian securities. As one American commentator remarked, contemporary investors used stock exchanges because they offered "free of charge, the opinions of the most competent financiers in Europe and America."[50]

IV

Shareholders were, of course, not just interested in passively noting information from directors – or from market prices - about their company, but also in ensuring that the board pursued investor interests. The question of director incentives was, of course, what had led Adam Smith and others to be so skeptical of the future of joint stock enterprise and is central to modern discussions of the principal-agent problem.[51] One of the simplest ways of harmonizing the interests of shareholders and directors was to ensure that the directors were very substantial shareholders, though this was less common in Britain than in America, Germany or France.[52] Although many companies specified a minimum qualifying shareholding for directors, this was often only a tiny proportion of the capital, particularly in the case of large banking or railway enterprises. More importantly, company promoters encouraged vendors of businesses to retain a substantial shareholding and remain as directors, to give the public company the benefit of their experience, though sometimes the newly enriched families wished to employ

[50] Conant, "Function," p. 437.
[51] Smith, *Wealth*, p. 700.
[52] Hannah, "Divorce."

professional managers and pursue cultural, political or social interests elsewhere. Where – as was also frequently the case – vendors did want to retain a key role, the London Stock Exchange listing requirement meant that they could not retain more than 33% of any listed security (larger holdings were commonly retained by owning families in Berlin, Paris or New York). Directors in Britain typically received fees for the job, which were publicly disclosed, whereas in America in this period they often did not (it was assumed they were remunerated as stockholders).[53]

On the other hand, broader share ownership in the UK did mean that the threat of removal by the shareholders was more real. Plutocratic control and board entrenchment via voting trusts or director protections in New Jersey and Delaware law in the USA inhibited shareholder actions there, but legal suits against negligent directors and shareholder votes on substantive governance issues actually happened in the UK, particularly in the tail of smaller quoted commercial and industrial businesses that characterized the more extensive British market, where only a few hundred shareholders could carry a meeting.[54] Some central London venues, like the Cannon Street Hotel, could accommodate around a thousand shareholders and sometimes did, while in Germany or America more than several dozen attendees were exceptional. No major British railway company chairman could claim, with the president of the USA's Great Northern, that he had chaired shareholder meetings with *no one* present.[55] Well-performing boards could, of course, usually command a controlling majority of

[53] Executive salaries were not, however, disclosed, so the aggregate rewards of a British full-time managing director could be concealed.
[54] The *Economist* from time to time contained denunciations of the poor shareholder safeguards in the USA, for example 10 May 1902, p. 733. Directors in Germany, as in the UK, were pressured to leave for bad performance, see Fohlin, *Finance Capitalism*, pp. 215-218.
[55] Testimony of James Hill, Pujo Committee, *Evidence*, p. 1953.

shareholder votes (and some chairmen came to the AGM armed with proxies sufficient to defeat dissidents), but, when performance slipped, it was not uncommon for shareholders' committees to be elected by the meeting to enquire further into past mistakes or to monitor the directors' currently promised remedies; in some cases such committees replaced some or all of the incumbent directors. Shareholder vigilance helped attenuate agency problems, though, of course, directors could still act in their own interests rather than the company's, provided they did not do so too transparently and egregiously.

Several structural options to align the board's interests more closely with those of shareholders were also being explored. The continental commercial code model of board remuneration by *Tantiemen* or *tantièmes* – supercharged board rights to substantially larger shares of incremental profits after a pre-determined trigger point, like payment of a 5% ordinary dividend – were similar in effect to some modern management options (also matching modern potential problems of perverse incentives for directors to engage in excessive risk-taking or accounting misbehavior). Nothing similar was enshrined in British statute law, but the same incentive effects could be achieved by parallel common law innovations. Founders' shares – sometimes also called deferred shares – were sometimes issued to vendors, promoters or directors, with dividends on these kicking in only when all prior charges had been paid and a basic ordinary dividend had been declared, giving the board strong incentives to grow profits. As with *Tantiemen* (which were eventually abandoned on the continent), such incentives, if successful, caused some shareholder resentment and could cease to be effective. Some very valuable founders' shares in gold and diamond mining enterprises were bought out in the early

1900s. In Harrods department store, the professional directors, who had taken over from the founding family when the company was floated, were so successful that their £1 founders' shares were worth £200 each, so they floated them as a separate company in 1895 to cash in part of their interest, thus somewhat diluting the intended incentive![56]

The most extreme form of incentivising the directors was, of course, to leave all the upside in their hands. One way round the London listing requirement that the vendors retain no more than one-third of any security was to list only fixed interest bonds and/or non-voting preference shares (to each of which the one-third rule was separately applied), with the directors or owning family retaining all the ordinary shares (which typically carried voting control and rights to all residual profits). The public preference shareholders and bondholders were then concerned only with their fixed dividends and interest payments: effectively the boards of such companies had sold investors cash flow rights but not control rights. Business historians tend to emphasize the effect of this in entrenching allegedly inefficient family management, but this pessimistic assessment ignores the incentive effect, which has received more attention in the finance literature.[57] Before such a company flotation, if a family mismanaged the business and profits fell to a third of the previous level, they merely reduced their own income; after such an arrangement, similar mismanagement would typically cost them their whole income (i.e. the ordinary dividend): hardly an incentive to coast along. There was a similar encouragement to good performance on the upside: any improvement in performance above the norm envisaged when the capital structure was fixed went to the owning directors, not to the fixed interest security holders. Perhaps not surprisingly, the

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[56] *Statist*, 23 March 1895, p. 377.
[57] Zingales, "Insider ownership."

companies that adopted such a structure around the turn of the century – companies that included Imperial Tobacco (cigarettes), GKN (metal fastenings), Lever Brothers (soap) and Worthington (ale)– did have continuing - but declining - family involvement in management. They were also among the top-performing and long-lasting public companies of their day.[58]

V

The third aid to overcoming agency problems, along with information and incentives, was reputation. There were, of course, in all markets a mixture of rogues and saints and quite a lot of people who came somewhere in between. It was important that the rogues were locked up, when something damaging could clearly be pinned on them, and also, more positively, for investors to learn to recognize honest directors who could be trusted. There was a danger in stressing the negative and relying too much on detailed legal prescription, if that simply discouraged financial innovation. Many thought the German bourse law of 1896 came into that category, for example in its restrictions on futures trading: Deutsche Bank responded by moving many of its international securities activities to London. Dr Georg von Siemens, Deutsche's president, publicly attributed the

[58] Gomes ("Going Public") has modeled a multi-period dynamic game, in the presence of moral hazard and asymmetric information, that will result in effort by family directors to develop a reputation, so that they can more profitably divest their holdings in the long-run. This is not a bad description of what happened in many such British (and overseas) companies. It is one possible resolution of the paradox that some capital markets developed well, in the nineteenth century and the first half of the twentieth, without very much in the way of formal protections for minority shareholders, protections that are considered by modern financial economists to be a key reason why securities market are larger today in some countries than others.

superiority of London as a financial center to the unwise German legislation, though it was 1909 before the over-restrictive German law was significantly modified.[59]

On the other hand, many thought that America's inter-state competition to reduce corporate supervision to the absolute minimum led to laws that were too lax. The license to lie or conceal vital information from outside investors in prospectuses and merger offer documents in America, was, for example, extreme. British governments generally left these matters to stock exchange and accounting self-regulation, but good practice was enshrined in law where MPs with financial, business and legal expertise agreed it could be effective. For example, the British law on prospectuses was tightened up in 1900 and the next year the fraudulent financier, Whittaker Wright, was extradited to the UK from America and convicted for behavior which he would have got away with there.[60]

The creation of a culture where prudence was valued and risk-taking was rewarded also relied on more positive reputational reinforcement mechanisms. One of the signals that investors looked for was the track record of directors of companies that were being offered to the public. Promoters and financial intermediaries who wanted to be in the business for the long run would strive to appoint directors with a good reputation. As we have seen this sometimes meant encouraging vendors to stay on, but other reputations could also be leveraged in directorships. The most obvious concrete manifestation of such a mechanism is the publication of directories to facilitate the reading of this quality signal. London's first *Directory of Directors* had been published by Henry Kent in

[59] *Economist*, 13 October 1900, p. 1437.
[60] Moody, *Truth*, pp. 365-9. See also Hannah, "What did Morgan's Men," for evidence of deliberate concealment of information from New York investors by J. P Morgan in the 1901 US Steel issue that was already criminal in London.

1736.[61] At the time it was perhaps most useful for identifying counter-parties for notes and bills, but company directors' reputations were already valued by shareholders. John Freame, of Barclay & Freame, for example, was then pioneering the business of corporate reconstruction by bankers. He had financed the London Lead Company's smelting innovations early in the century, with both loans and equity, but when corrupt dealings by the company's directors were suspected, he helped expose them and in the 1730s re-financed and ran the company.[62] Directories showing the board portfolios of directors proliferated in the home and overseas railway booms of the 1840s and 1850s and the *Directory of Directors* assumed its modern, annually revised, form in 1881, when the leading London financial publishers, Skinner, took it in hand. Other financial centers began publishing directories of directors later: the Berlin and New York volumes both date from 1898.

Of course, quality signals from directors' reputations could be ambiguous or downright misleading. The "signal" that attracted the most negative comments was the appointment of aristocrats or elected members of parliament to boards (a problem criticized in republican France as well as in Britain). The principle was a sound one: such people had a reputation won elsewhere, which they were essentially posting as a bond for good behavior as a company director. By 1896 over a quarter of the British peerage were company directors, while a sample of over 600 companies in 1895-1904 suggests that the typical company had at least one member of recognizable, if less exalted, elite groups on the board.[63] However, there was a plain moral hazard in this commercial market for

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[61] Kent, *Directory.*
[62] Ackrill and Hannah, *Barclays*, pp. 13-14.
[63] Thompson, *English Landed Society*, p. 307; Braggion, "Credit Market Constraints," Table 1.2. Braggion includes knights, baronets, M.P.s and J.P.s, as well as the nobility, in his elite. There is, of course, an

reputation and, even if the director himself intended no harm, his signal could be misappropriated. Hence the incompetent dummy director - or “guinea pig” (director’s fees were usually expressed in guineas not pounds) - became a Victorian figure of fun in the operettas of Gilbert and Sullivan.[64] Some of the most roguish company promoters were, in fact, members of the House of Commons who found their gift of the gab more lucrative in financial misrepresentation than in politics. Several – like Jabez Balfour M.P. and Horatio Bottomley M.P. - ended up in the criminal or bankruptcy courts and jail. The corrupt promoter, Sir Ernest Hooley, claimed in court to have paid aristocrats between £500 and £25,000 each to front his IPOs, though this may have been as inventive as his watery prospectus capitalizations of companies like Schweppes and Dunlop.[65] Another fraudulent promoter, Whitaker Wright, used Lord Dufferin, the retired Governor General of Canada, and other gullible peers without business experience, as dummy directors of his London & Globe Corporation. Its collapse at the end of 1900 caused investors to lose an astounding £7 millions through market-rigging of mining shares, aided by brokers and jobbers who went unpunished by a toothless stock exchange committee.[66]

Yet, it is too easy to conclude from such appalling cases that signaling by director reputation *generally* did not work. Successful prosecutions of wrongdoing can be cited as evidence of effective disapproval and discouragement of such behavior, rather than of its prevalence: the jailing of an Enron executive is not usually held to demonstrate that all Harvard Business School graduates are crooked. In fact, the higher ratios of

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apparently contrary argument in the Wiener thesis: that Britain’s aristocrats was profoundly averse to modern business. Dedicated “declinists,” of course, have no problem in reconciling the two: it is a *very bad thing* when aristocrats join industrial boards and betrays a deep national cultural flaw when they do not!

[64] Gilbert, *Utopia,* p. 434.

[65] Harrison, “Joint-stock Company Flotation,” pp. 174-6.

[66] Ingall and Withers, *Stock Exchange*, pp. 108-109; *Investor’s Monthly Manual*, 31 January 1901, p. 2.

market prices to nominal (par) share values in London (and Berlin and Paris) suggest significantly less capital watering by promoters there than in New York. The fraudulent MPs were exposed, expelled from parliament and imprisoned and the British press could be withering in its censure of those whose reputations were corruptly or incompetently for hire.[67] Wright found the aristocratic establishment arraigned against him when he tried to secrete his ill-gotten gains after bankruptcy: the shame was so great that he took arsenic to avoid serving seven years. American equivalents might remain on the Social Register, or, as the *New York Evening Post* bitterly described the contrasting outcome that they believed Wright would have faced over the water, "walk the free air, lavish in their philanthropies, lauded in the pulpits as exemplars for our youth."[68]

Many elite directors, with some native shrewdness, business experience and a lot more to lose, successfully posted their reputational bond as a guarantee of company quality with more positive outcomes. Lord Salisbury, who, in 1900, as prime minister, governed Britain and much of the world under the Pax Britannica, had served his apprenticeship in senior administration as the (very effective) chairman of the Great Eastern Railway, nursing it from bankruptcy to prosperity in 1868-1872.[69] At the same time, the Duke of Marlborough and other peers served on the initial board of Land Securities as it raised the launch capital for its successful life as a leading real estate

[67] See, for example, the criticism of Sir Seymour Blane in *Economist*, 23 November 1901, p. 1730.

[68] Quoted in Moody, *Truth*, p. 368. On the other hand, CharlesYerkes, the Chicago fraudster, was hounded out by local opinion and made a new career in London; while a local British rogue, Sir Ernest Hooley, managed repeatedly to mislead investors, despite several exposures and bankruptcies. The protections in the UK were stronger than in the USA, but still weak. However, it is perhaps worth noting that the ones who got away lightly, Hooley and Yerkes, left behind worthwhile (if temporarily over--priced) industrial undertakings and an electrified London underground, while Wright left behind a tissue of lies, hot air, and low-value mining claims.

[69] Barker, "Lord Salisbury."

company.[70] Sometimes economic ministers out of office and retired senior civil servants embarked on careers as company directors.[71]

While rogue promoters might seek "guinea pigs" in these markets, others more benignly sought to match acknowledged expertise with legitimate investor demands for reassurance. When the American entrepreneur, George Eastman, floated his global holding company for Kodak on the London Stock Exchange in 1898, he appointed Lord Kelvin (a noted Glasgow professor of physics, who also ran his own marine instruments business) and members of the British political elite to the board. Investors who trusted the signal had no reason to feel this was a misjudgment. The combination of Kodak's product reputation and these quality certifiers was sufficient to make Eastman's London IPO a success and Kodak proved an excellent London-listed investment in the long run (while in New York it was only traded on the curb, even after Eastman, for tax reasons, moved the corporate headquarters from London to Rochester). Whether such directors made any large contribution to management doubtless varied, and, in Kodak's case, that was plainly not the prime intention. It appears likely from the many such cases which did not turn out badly that the signal of director reputation may have been more positive than its generally harsh treatment in the literature suggests. Moreover, it might also have delivered more than boards merely disinclined to perpetrate fraud on their shareholders: Braggion found a correlation between elite representation on British boards and corporate growth in the 1895-1904 period.[72]

[70] Rutterford, "Company Prospectus."
[71] Cassis, *City bankers*, pp. 64-66.
[72] Braggion, "Credit Market Constraints." He interprets this as an indicator of elite access to informal credit networks, rather than director quality signalling.

Worldwide, perhaps the most ubiquitous board quality certifier was the banker. J. P Morgan, puzzled that his Congressional tormenters on the Pujo Committee should single it out as a sign of wickedness, correctly remarked in 1912 that the new American practice of appointing bankers to boards was about as old as the European company. Bankers came in many shapes and sizes in an advanced financial market like London and there is something of a consensus that they were divorced from British business and played a smaller role on corporate boards than elsewhere. The evidence suggests a less black-and-white conclusion. Given that the most culture-free definition of a banker is someone who can borrow more cheaply than he can lend, it is hardly surprising that their reputation was considered one of the most unimpeachable and that they were particularly valued as board members, in Britain as elsewhere.[73]

Cassis's careful analysis of directorships held by 460 London bankers identifies industrial companies as an area with relatively low banker representation: he suggests only 24% of large British industrial companies had a London banker on their board in 1905.[74] Yet this "low" figure is slightly higher than the average figure for all joint-stock companies (including banks themselves) in Germany (a country conventionally held to have extensive banker representation). In the same year, 1905, only 23% of German AGs had a banker on the board (only half of these from the *Grossbanken,* which are commonly supposed to have had a critical monitoring role).[75]

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[73] Bankers who could not borrow more cheaply than they could lend – like those who had lost reputation – did not remain bankers for very long. Those who consider that General Electric – which can also borrow more cheaply than it can lend – is an electrical manufacturer, not a bank, have not read this company's recent annual reports.
[74] Cassis, *City bankers*, p. 177.
[75] Fohlin, "Balancing Act," p. 18; though Fohlin, *Finance Capitalism*, p. 134 reports a higher figure (56%) for an 1898 sample of *Berlin-quoted* firms, and both these samples include a lot of small German companies: *smaller* British industrials were probably less likely to have a London banker on the board. On

Moreover, Cassis shows that, among his London bankers in 1890-1914, service on non-industrial boards was much more common: only 7% of bankers were on the boards of industrial companies, 7% on utility boards and 8% on mining boards, but this rose to 49% who held insurance directorships, 31% on investment trust boards, 24-42% with railway directorships (the largest quoted companies of the day) and 12% in shipping.[76] London bankers sat on boards as diverse as French, Austrian, Argentine and British railways, the big London insurers and investment trusts, Cunard, Anglo-American Telegraph, Shell Transport & Trading, Mexican Eagle Oil, Consolidated Goldfields, De Beers, Guinness, Vickers, Fine Cotton Spinners & Doublers, and United Alkali. Only 22% of the London bankers sat on no boards, while 20% sat on five or more. If provincial bankers, stockbrokers and the more respectable company promoters who cultivated long-run business (like John Ellerman, JuliusWernher or Henry Osborne O'Hagan) were added, the percentage of companies with "finance" representatives on their boards would be even higher. These activities cannot be directly compared with the German banker representation figures (definitions in both numerators and denominators differ and they are incompatibly disaggregated), but the propensity of public company boards to include financiers did not differ as markedly between the two countries as is sometimes suggested.

Of course, the *role* of the bankers on boards differed between companies and countries. British boards already varied widely in their structure and function: some were entirely or mainly non-executive (in the manner of the German *Aufsichtsrat* or supervisory board), some had a chairman and managing director with a "chief executive"

the other hand, the Fohlin data include German provincial bankers, while Cassis's British figures included only London bankers.

[76] Cassis, *City bankers*, pp. 151, 153, 168.

role near to that of an American company president, while yet other boards constituted an effective working committee of the company's senior executives. Many British bankers perhaps served on railway boards because they were seen as reliable, informed and trustworthy public trustees of very large businesses, with a responsibility to a range of stakeholders as well as shareholders. Certainly their presence there cannot easily be interpreted as designed to support securities issuance: blue chip British railways (and banks themselves) typically had sufficient market reputation to issue their own new securities, without significant financial intermediation: all they required was a stockbroker to negotiate the formalities of the additional Stock Exchange listing.[77] Other bankers *were* on boards for the direct financial knowledge and issuing services they had provided or might in future provide: a Baring long remained on the board of Guinness because the bank had sponsored its IPO; a Rothschild representative was on the board of De Beers and Rio Tinto because they were financial advisers and major shareholders. There was nothing to parallel the routine German banker membership of supervisory boards by virtue of *Depotstimmrecht* (representation of shareholder proxy votes), though there were parallels to German banker representation as substantial owners (as with Mannesmann or Rio Tinto) or as new issue quality certifiers. The latter practice was more common in Germany, but German bankers averaged 17 directorships (and one had as many as 35), while Cassis's data suggests less pluralism in Britain. Pluralist German directors were certainly criticized at the time for devoting insufficient time to the job.[78]

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[77] Whereas serially bankrupt American railroads understandably required the intermediation of bankers like J. P Morgan, who typically refused reconstruction deals unless he could be confident of control through a voting trust, see Tufano, "Business failure."

[78] Economist, 10 August 1901, pp. 1217-8; see also Fohlin, *Finance Capitalism*, p. 35; Cassis, *City bankers*, p. 151. Collins, "English bank development" is consistent with a picture of long-term bank lending and oversight, and aid to distressed firms, of the kind that is more frequently associated in the literature with the German system.

Britain had a more competitive and varied supply of financial services than other countries at this time and few British firms would have felt constrained to admit a banker to their board solely to guarantee access to capital, while bankers would have avoided getting saddled with such a relationship of need. Banker relationships motivated by access to more constrained financial channels may have been more common in both Germany and America, though there, too, industrialists balanced directors from several banks and broke free of banker control where they could.

VI

Financial economists who discuss these matters appear to suffer from extreme schizophrenia.[79] Many picture the agency problem between directors and shareholders in Hobbesian state-of-nature terms: insider directors routinely and ruthlessly loot hapless investors, with no moral, cultural, legal or professional restraint on their naked self-interest, as they avidly feather their own nests. Other financial economists portray what, on the face of it, is a very different world: one in which investors, plagued by severe information asymmetries, willingly hand over successive, large tranches of cash to nice, quasi-monopolist, quality-certifiers like J. P. Morgan or Deutsche Bank, who, apparently, can be implicitly trusted, without a hint of agency problems. The real world of British corporate finance around 1900 contained recognizable elements of both these models, but I doubt whether many shrewd and informed market participants of the time would have swallowed either view whole. Rather the financial markets resemble a

[79] A point nicely made in Allen, "Do financial institutions." I am grateful to Yoshiro Miwa for drawing the point to my attention.

Schelling repeated game world, in which investors cautiously and skeptically learnt whom to trust, always keeping a sharp eye open for being taken for a ride and, when necessary, administering very real tits for tat. Meanwhile solid, but always potentially alienable, reputation was cultivated by many directors and many intermediaries, who had more to gain (in the longer run of repeated interactions) from delivering value to investors than from making a fast buck by cheating on one deal. This was not so much the unattractive "opportunism with guile" view of humanity posited by transactions cost theorists as the "trusting, fair behavior, with skepticism" more plausibly supported by current developments in behavioral and experimental economics.

The complexity (and potential for wrong turnings as well as effective positive feedback) in such an iterative, evolutionary process can be glimpsed in a 1900 snapshot of the brewing industry, shown in Table 1. There had been a boom in the flotation of brewery companies in Britain, following Baring's successful IPO in 1886 of the Dublin brewer of Guinness stout, then probably the world's largest producer of alcohol. Among the many other brewery issues was the more recent (1898) merger of three large London breweries into the second largest UK brewer, Watney, Combe, Reid. There is general agreement among the industry's historians that this boom resulted in over-enthusiasm for public issues: Barings had probably under-priced the Guinness offer and it went to a considerable premium. There was consequently no shortage of capital in the industry; indeed arguably there was too much.[80] Investors could get a yield of only 2.6% on consols and 2.9% on prime railway debentures, but brewery debentures paid

[80] Gourvish and Wilson, *British Brewing Industry*, p. 263; Vaizey, *Brewing Industry;* Watson, "New Issues Market," "Banks" and "Funding enterprise." The *Investor's Review*, on which Table 1 is based , tracked down 122 more quoted British brewing companies than Watson found in the *Stock Exchange Official Intelligence*, presumably mostly small provincial issues.

Table 1. The Investment Performance of Quoted Brewery Companies in early 1900.

	Number of Companies	Nominal Value of Capital £M	Market Value of Capital £M	Average Size £M	Appreciation/ Depreciation %
Guinness	1	5.2	14.3	14.3	+175
Watney, Combe, Reid	1	12.7	13.4	13.4	+5
Other London-listed UK	164	81.6	74.8	0.46	-9
Provincially-listed UK	272	15.2	23.4	0.09	+54
London-listed Overseas	na	14.4	7.0	na	-51
Total	na	129	132	na	+2

Source: *Investor's Review*, 19 May 1900, pp. 686-87; author's calculations for Guinness and Watney.

3.9% and, at that rate, the brewers still considered themselves better off than borrowing the money from banks at 4-5%. The plentiful public subscriptions to fixed interest - and equity - issues not only financed expansion of brewing plant, but vertical integration forward to the ownership of pubs. Although Guinness did not follow this strategy (relying on its brand reputation and advertising to market its product), most British breweries did, as stricter licensing laws restricted the number of outlets, increasing an already strong tendency to tying pubs. With restricted new entry into beer retailing, the strategy of forward integration was initially profitable, but increased beer taxes and the retail restrictions successfully restrained demand: the industry was about to experience a sustained decline in sales, which would produce capital losses for some investors.[81] One of the most prolific promoters of brewery issues, Henry Osborne O'Hagan, recounts how

[81] As was already feared by informed commentators, see *Investor's Review*, 6 January 1900, pp. 3-4.

he found the price asked by brewery vendors increasing; so he sought overseas alternatives, in the USA and elsewhere, in a bid to supply investor demand with better value securities (hence the bottom row of the table).[82]

The output of the brewing industry in Germany and the United States was only slightly larger than that in the UK, but finance and organization varied considerably among the three.[83] Most large American breweries were in family ownership (the NYSE listed no breweries at all) and none were as large as the largest British breweries. In Germany, too, breweries were small and family-owned, though dozens were quoted on the Berlin and regional stock exchanges.[84] It is, in fact, far from obvious that there were great advantages in substantially divorcing ownership from control in this industry and stronger family ownership seems to have served Americans and Germans perfectly well. By contrast, the scale of British stock exchange investors' incursions into brewing was spectacular, indeed, perhaps excessive. The value of the brewery securities in Table 1 *alone* exceeded that of *all the domestic industrial equities* (including breweries) quoted on the Berlin exchange at that time![85] Moreover, as the low average sizes in the fourth column suggest, even in Britain small family breweries, distributing barrels locally by horse and dray, remained viable. Indeed, by the yardstick of appreciation in securities values over par (the last column in the table), the smaller provincial issues seem to have

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[82] O'Hagan, *Leaves.*

[83] In 1899, beer production in Germany was 68 million hectoliters, in the United States 65 million hectoliters and in the UK 61 million hectoliters (Picard, *Bilan*, p. 431).

[84] The 66 quoted German brewery AGs had a nominal capital totaling £11 million (less than Watney Combe Reid alone) and averaging £0.16 million in 1900 (much smaller than the typical British listed brewery in Table 1), see Wagon, *Finanzielle Entwicklung*, p. 195.

[85] Berlin's industrial equities were worth only £107 million in early 1900 and even with bond and preference share values added (as they are in the British brewery data) would have only modestly exceeded the value of breweries alone in Britain. The table only includes quoted British brewery securities; there were also substantial unquoted ordinary shares in firms whose other securities were quoted (Gourvish and Wilson, *British Brewing Industry*, pp. 262-263, 266, 384), as well as thousands of unquoted breweries.

performed significantly better (+54%) than the general run of larger London-quoted breweries (-9%), suggesting that, after family ownership was diluted by stock exchange flotation, *local* information networks and monitoring had real advantages. As the editor of the *Economist* put it, in relation to IPOs generally: “A really good thing from Glasgow, or Yorkshire, or Lancashire, or the Midlands, seldom comes to London to be floated on the public. The insiders naturally keep it to themselves and their friends.”[86] It is evident that efficient production for local markets was possible at a wide range of sizes, though scientific processes were increasingly applied to brewing beer, bottling was being mechanized and there were significant scale economies in capital-intensive, urban plants. Yet Guinness and the Burton ale brewers in the UK (and some US and German equivalents) were still exceptional in being able to charge premium prices in broader markets than their home city, distributing beer by rail and ship on a national scale and for export.

Guinness (on whose board a Baring, involved since handling its IPO in 1886, still served) generally retained investor confidence and justifiably so. The firm had consistently ploughed back substantial profits into the business, in addition to paying generous dividends.[87] It also, arguably, had the largest, most effective and most professional management hierarchy of any world brewing company, which proved capable of further developing large-scale production, brand value and global distribution. One indicator of its exceptional management quality familiar to most of us now – but still then a trade secret - is that, every time we use a t-statistic, we are indebted to William Gossett, one among many Oxbridge scientists recruited to the Dublin management team

[86] Hirst, *Stock Exchange*, p. 216.
[87] *Investor’s Review*, 11 August 1900, pp. 171-172.

from 1893 by Claude Guinness. This early graduate recruitment program enabled the company to catch up with Paris, Copenhagen and Munich in the application of biochemistry and statistics to industrial processes and management.[88] Gossett spent his whole career with the firm and, after the Irish Free State was established, became managing director of Guinness's new British mainland subsidiary. He invented the t-statistic to determine the sample size required for reliable testing of Guinness quality and later applied it to measuring the effectiveness of advertising.[89]

There were in 1900 rather more London market doubts about Watney Combe Reid. Its chairman, the former family owner of the Combe third of the merger, Cosmo Bonsor M.P., was also a director of the Bank of England and of the South Eastern Railway. Essentially he and the other families had unloaded their interests at the top of the long bull market in brewery shares: owners were in a better position than outside shareholders to judge when profits had peaked.[90] Like many breweries it was to meet

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[88] The t-statistic was known to an earlier generation of statisticians as "Student's t," that being the pseudonym Gossett used in launching it on the world in *Biometrika 1908,* see Dennison and MacDonagh, *Guinness*, pp. 89-90.

[89] Ibid, pp. 16-38; *Investor's Review*, 27 October 1900, pp. 518-520. The prevailing interpretations of Guinness perfectly reflect the rose-colored Whig bias of much American writing and the reverse "declinist" bias of the British. One financial columnist (Kay, "The scholars behind the stout") recounts how his editor at the *Financial Times* queried his (correct) account of the invention of the t-statistic as inherently implausible. By contrast, Chandler's unflattering assessment (*Scale*, p. 267) of Guinness's marketing scale and skill, relative to Pabst, Schlitz, Anheuser Busch, Schultheiss and other brewers in the United States and Germany, strikingly lacks support. Guinness at the turn of the century had two-thirds of the Irish market, extensive distribution on the British mainland and sold nearly 5% of its output in the USA and other overseas markets, while the named German and American firms were smaller by obvious indicators such as barrelage or capital. Chandler may have been misled by the US habit – which amused contemporary Europeans as much as the proverbial postwar Texans - of claiming to have the biggest and best in everything, though that was only sometimes true. For example, it was routinely claimed in the 1890s that Busch's St Louis brewery was the "largest brewing establishment in the world" and similar claims were made for Pabst's Milwaukee brewery (Muirhead, *United States*, p. 276; Plavchan, *History*, p. 65). Guinness's Dublin output was a lot larger and even British-owned US brewery mergers, such as St Louis Breweries and Milwaukee & Chicago Breweries, had higher outputs. (Ibid, p. 230; Dennison and MacDonagh, *Guinness*, pp. 37-39; Duncan, *Manual*, pp. 279, 282. Note that the old English gallon - still in 1900 used in the USA - was one-sixth smaller than the standard Imperial gallon used in the UK from 1824).

[90] *Economist*, 3 November 1900, pp. 1533-1534; Gourvish and Wilson, *British Brewing Industry*, p. 297, 311.

difficulties from 1900, but Bonsor was frank with the shareholders, dismissed the managing director and reduced the capital to a more realistic level. Watney weathered the storm and remained a large producer. Allsopp's, a large Burton brewer, had even more grossly overpaid for assets and overoptimistically invested in a large, new lager brewery under the management of the recklessly spendthrift Percy Allsopp. In 1900 the two-thirds of the shareholders who had subscribed to the public issue of ordinary shares turfed him out and installed a new chairman.[91] There is, then, clear evidence that mistakes had been made – mistakes of overinvestment and of poor director selection - but they were being corrected. And the investors who had trusted in Bass and Worthington - Allsopp's two major Burton rivals - were to do well in the long term, though the family owners (like most German and American brewers) kept the ordinaries to themselves at this time.

British brewery companies operating overseas (the fifth line in the table) - though they often had reputable and experienced British brewers on their boards – had performed particularly poorly. Those in South Africa and Germany generally did better than those in the USA and Australia (where the local rogues enjoyed ripping off innocent foreign capitalists). In the USA, for example, some of the best family brewers had refused to sell to British (and American) financiers, while others had sold out, then started up rival breweries. More generally, the supervision and monitoring of distant enterprises in competitive industries was perhaps one magnification too far of the London versus provincial information problem.[92] Truly multinational enterprises in the drinks industry did not prosper until the changed conditions after World War Two.

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[91] Ibid, p. 311; *Investor's Monthly Manual*, 31 August 1900, p. 446; *Economist*, 24 August 1901, p. 1281; Watson, "Banks, " p. 77.

[92] Baron, *Brewed,* pp. 268-72. The total for foreign breweries includes only companies registered and/or quoted in Britain. It excludes the securities of British capitalists resident overseas, like those who for

Complex lessons were, then, slowly being learned by investors and by managers, in Britain and in the world of which it was in 1900 the financial center. It is tempting to conclude that, because, at the dawn of the twenty-first century, two London-headquartered multinational firms were still the largest in the world alcoholic drinks industry, that city's early and precociously varied experimentation with corporate governance in this sector was an evident success. After all, one of these modern corporate giants, Diageo, is a merger of the leading firm in Table 1 – Guinness – with Distillers (the leading Scotch whisky producer), while the other - SAB Miller - is a merger of South African Breweries (an 1895 foundation appearing in the fifth line Table 1, which, after a spell headquartered in Johannesburg, returned to its London origins) with the Miller beer division of Philip Morris (in 1900 a small London cigarette producer, which later migrated to America and, among other things, acquired Miller). In fact, of course, these long-run outcomes had more complex, constantly mutating and varied causes, among which the sterling services of the US and German governments in support of British corporations' global alcoholic dominance should not be forgotten. (Prohibition in 1917-1933 ensured that British firms could develop without challenge, while government regulation - the *Reinheitsgebot* - kept German brewers inefficiently small in subsequent decades). Moreover, after many years of efficient, family-controlled, professional management, Guinness fell into the hands of a professional manager that the courts branded a corporate crook for share price manipulation in the 1980s. Its survival, despite

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decades ran the Yokohama-based Japan Brewing Company (registered as a British Hong Kong company, with $HK shares, but traded "over the counter" in Tokyo) before selling out in 1907 to Mitsubishi (who renamed it after its famous brand, Kirin). Such hands-on local expatriate management appears to have been more successful than arms-length transoceanic investment in this industry.

that disreputable episode, clearly owes more to its deeply-rooted managerial and marketing capabilities than to the immutability of good corporate governance practices.[93]

The case of the global drinks industry supports the view that the British – like other nations - had only equivocal success in pioneering solutions to the complex and constantly changing problems of corporate governance. It remains a mistake to seek in British governance innovations around 1900 – impressive as they are by contemporary standards - the roots of long-run decline or success, in the reductionist mode so ridiculously pursued in Whig modernization theory. Business reality is more complex and messy than that. If it were not so, you would have concluded your reading of this article by clearly understanding the magic formula by which corporations, everywhere and forever, can be efficiently governed by wise, reputed, incentivized, transparent and trustworthy directors. Like the many thousands listed in London's *Directory of Directors* in 1900, you do not inhabit such a world, though – then, as now – these included people diligently and creatively working toward it. They did so while trying to earn a more-or-less honest penny or two, within a balanced system of corporate law, professional practice and ethical norms that left room for experiment and enterprise, but, unsurprisingly, was to prove capable of further improvement. That involved a movement to more intensive, rules-based and legally-mandated regulation. From the 1930s that trend was led by the United States, though London has generally followed Washington and New York along this path. Yet, today - in the City's distinctive self-regulation of take-over bids, in its voluntary ("comply or explain") corporate governance code and in its caution on emulating the onerous, box-ticking, manufactured "ethics" of Sarbanes-Oxley - faint traces still remain of London's 1900 view: that enterprise, flexibility and

[93] Guinness, *Requiem*.

shareholder protection are more effectively bolstered by values, standards, voluntary compliance and rare (but decisive and equitable) judicial interventions, than by complex and detailed legal prescription.

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