Business and Politics 2019; 21(3): 327–350

Patrick Jahnke*†

Ownership concentration and institutional investors' governance through voice and exit

Abstract: Drawing on data collected in interviews with investors and corporates in the United States and Europe, this paper sheds light on the motives behind shareholder engagement. It explains why index funds engage in corporate governance, despite their apparent lack of financial incentive to do so. Applying Hirschman's concepts of exit and loyalty to the investment management industry, this paper suggests that for many institutional shareholders today, voice is more feasible than exit. For the largest index investors, the cost of engagement has fallen to a level where it is today negligible. The immense concentration amongst index funds, with the three largest fund managers controlling over 90 percent of assets, ensures sufficient return on their governance investments. Furthermore, interviews with activist investors suggest that they have learned to work with index investors and that index funds do not present barriers to successful campaigns. This paper therefore advocates against restricting index funds' voting rights. Doing so would muzzle those shareholders with the deepest pockets and the greatest potential for corporate oversight. Instead what is needed is regulation to ensure greater disclosure of engagement efforts by the largest fund companies enabling greater academic and public oversight of asset managers' engagement activities.

Keywords: corporate governance, index funds, mutual funds, engagement, blockholders

doi:10.1017/bap.2019.2

Introduction

Institutional ownership of stock markets has been rising consistently since the 1970s. The initial growth was driven by pension funds, leading Peter Drucker in 1993 to fear the onset of "pension fund socialism" in which workers, through

***Corresponding author: Patrick Jahnke,** School of Social and Political Science, The University of Edinburgh, 15a George Square, Edinburgh EH8 9LD, UK; Email: p.d.jahnke@sms.ed.ac.uk

† I am immensely grateful to Iain Hardie for comments on an earlier version of the manuscript. I would also like to thank participants at the oikos Young Scholars Finance Academy in Zurich, participants at the EISA Pan-European Conferences on International Relations in Barcelona, as well as the anonymous reviewers and the editors for their helpful comments.

© V.K. Aggarwal 2019 and published under exclusive license to Cambridge University Press

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

their pension fund holdings, would dominate corporate strategy.[1] In the 1980s and 1990s the rise of mutual funds took over the lead from pension funds resulting in the coining of the term "mutual fund capitalism." More recent definitions, such as "asset manager" capitalism, seek to be flexible so as to incorporate both mutual funds and Exchange Traded Funds (ETFs).[2] Whatever the term used to describe the contemporary capitalism, the growth of institutional investors has brought about a re-concentration of ownership and a curtailment of the collective action problem that hitherto complicated shareholders' exercise of control.[3]

Institutional ownership of companies has grown to the point that institutions today own approximately 80 percent of the market value of U.S. stocks.[4] Recent academic research explores this rising ownership concentration and debates the growing importance of "passive" or "index" investors.[5] This literature raises concerns that asset managers in general, and index funds in particular, may be becoming too powerful, while also exhibiting conflicts of interests.[6] Some, therefore, suggest that index funds have become so powerful, they will cast the deciding vote on any proxy battles between activist investors and corporate management.[7] Others see a conflicts of interest resulting from asset managers seeking to gain incremental assets from corporate pension funds, with the result that they will vote mainly with management, thereby inhibiting the corrective influence exerted by activist investors within the capitalist system.[8] One solution that has, therefore, been suggested is to disenfranchise index investors by preventing them from voting their proxy votes.[9]

Instead, this paper highlights that for the largest index investors, on whom much of the literature focusses, the cost of engagement (when expressed in basis points of profits earned from asset under management) has fallen to a

1 Drucker (1993).

2 For mutual fund capitalism, see Hawley and Williams (1997) and for asset manager capitalism, Braun (2016). ETFs are forms of passive investing. Passive investments are defined here in line with Braun (2016) as those that aim to track, rather than beat, the performance of a benchmark index. Unlike passive mutual funds, which can only be bought and sold once per day (typically a time lag of one or more days), ETFs trade like ordinary stocks and can be bought and sold continually on stock exchanges during market hours."

3 Gilson and Gordon (2013).

4 Pensions & Investments, 25 April 2017, "80% of equity market cap held by institutions."

5 Fichtner et al. (2017).

6 See Fichtner et al. (2017), Lipton (2017), and Shapiro Lund (2017) for a discussion of index investor power, and Bebchuk et al. (2017) and Gilson and Gordon (2013) for an investigation of conflicts of interest and agency costs.

7 Shapiro Lund (2017).

8 Bebchuk et al. (2017).

9 Shapiro Lund (2017).

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

level where it is today negligible. The literature fails to account fully for the significant economies of scale and therefore posits that index funds will not invest beyond a minimum standard of corporate governance as the benefits will accrue to all investors. However, the concentration amongst index funds, with the three largest fund managers controlling over 90 percent of assets, ensures sufficient return on any governance investment.[10]

Drawing on information collected in more than fifty interviews with institutional investors, corporate issuers, and their advisors, this paper contributes to this literature an examination of the nature of the investor-corporate dialogue. It finds that engagement on issues of corporate governance beyond proxy voting is, to date, primarily a domestic exercise, focused on the largest companies in each country. This is because domestic companies typically represent investors' largest holdings, both in terms of the percentage of the funds' assets and in percentage of the companies' outstanding shares.

This focus on high-profile companies has left some corporates with the belief that asset managers are motivated by marketing considerations as opposed to genuine concern for the issues at hand. Companies report no substantial increase in the number of engagements in recent years but remark instead that engagement is becoming increasingly public as illustrated by the publication of investors' letters to company boards. Satisfaction with the level of engagement appears to vary with company size. Larger, especially "mega-cap," companies report a high level of satisfaction with the level of engagement with investors while smaller companies voice concerns about a lack of access to investors' corporate governance teams. This corresponds with investors' strategy of focusing on their largest holdings.

Finally, interviews with activist investors suggest that index investors do not pose barriers to successful campaigns. Instead activists have learned how to engage them through online presentations, direct email communication, and conference calls. Indeed, the main concern corporations raised in relation to index funds was a fear that they may become instrumentalized by activist funds. This paper therefore advocates against restricting index funds' voting rights as index funds compete not only with one another for assets but also compete against active funds for assets.[11] The way for them to succeed in this competition is to invest in measures to ensure index constituents follow superior corporate governance practices.

Limiting the voting rights of index funds would muzzle those shareholders with the deepest pockets. Instead what is needed is regulation that ensures greater disclosure of engagement efforts by the largest fund companies. These

10 Fichtner et al. (2017).

11 See, also, Fisch et al. (2018).

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

companies have grown so large that they have become institutions of public interest. The condensed stewardship reports, published annually by asset managers, typically only provide abstract statistics on the number of companies engaged without providing the names of those companies, thereby frustrating academic and public attempts of oversight.

At a point in time when society is increasingly turning to the asset management industry for help in resolving issues the political process has failed to address, an understanding of the motives of institutional investors, their capacity limitations, and the process by which they prioritize corporate engagement is essential.[12] This paper concludes that for the largest institutional investors today, engagement is a more feasible choice than selling their stock. Unable to sell due to a mixture of passive mandates and liquidity constrained active funds, engagement is the only option to safeguard their customers' assets against corporate misconduct.

The interview methodology

This paper draws on information collected in interviews with twenty-one institutional investors and thirty-three stock market-listed companies ("corporate issuers"), as well as a number of corporate governance advisors to arrive at a multi-dimensional understanding of how engagement occurs in practice. The semi-structured interviews were mostly conducted in the spring and summer of 2018 and interviewees were selected from the United Stated, the United Kingdom, and Germany, with the aim of having approximately one third from each jurisdiction. These countries were selected due to the fact that they represent both common law and civil law countries, as well as different varieties of capitalism.[13]

12 For one such public policy example, see the call for asset managers to have "gun-free" portfolios in the aftermath of the shooting at the Marjory Stoneman Douglas High School in Parkland, Florida on 14 February 2018.

13 Legal origin and the level of investor protection are the most common country-level factors used as independent variables in cross-country governance research (Schiehll and Martins (2016); Schnyder et al. (2018)). See La Porta et al. (1998) for a discussion of the significance of law for finance, and Hall and Soskice (2001) for a discussion of the varieties of capitalism. Germany is a civil law country, while the United States and the United Kingdom are common law countries. The varieties of capitalism literature differentiate between liberal market economies (LMEs), such as the United Kingdom and the United States, and coordinated market economies (CMEs), such as Germany.

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

In sum the investors interviewed managed total assets of $14.3 trillion as of September 2018 with the smallest asset manager managing assets of $4 billion dollars and the largest asset manager managing assets of several trillion. The companies interviewed for this paper had a combined market capitalization of approximately $2.5 trillion, with individual market capitalizations ranging from $4 billion to $400 billion. Balancing assets under both management and market capitalizations was important as these are proxies for the financial means companies have at their disposal.

The selection of companies was a random sample from each of the countries, with the aim of ensuring a balance across sectors and market capitalizations. Once initial interviews were secured, interviewees were asked whether they would be prepared to provide further introductions. While this "snowballing" approach risks the selection of interviewees becoming non-random, a pre-set list of quadrants (size, type, and location of institutions) was used to steer recommendations. This, together with the fact that the governance community is a relatively small group of experts, ensured that the typical pitfalls of snowball sampling were addressed.

The rise of index investors

According to Hirschman, shareholders unhappy with a company's performance have three choices: they can simply sell their stock and move on (also referred to as the "Wall Street Walk"), retain their stock and voice their concerns, or choose to do nothing. Hirschman refers to these options as exit, voice, and loyalty, respectively.

Much has changed since Hirschman first published his thoughts on exit and voice in 1970. While the initial era of globalization from the 1950s onwards was focused on the trade of goods, by the 1990s the role of finance independent of trade became increasingly important. Davis remarks that while "twentieth-century American society was organized around large corporations, particularly manufacturers and their way of doing things. It is now increasingly organized around finance" (2009: xi).

Institutional ownership has been growing because individual investors increasingly delegate their asset management decisions to institutional investors. They do so for a number of reasons, including the diversification benefits funds offer, access to specific investment themes, as well as the perceived stock selection expertise on offer. Around the turn of the century, when institutional ownership surpassed 50 percent of all shares in issuance, Useem, Hawley and Williams, and Harmes drew attention to this phenomenon, referring to it as investor

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

capitalism, fiduciary capitalism, and mass investment, respectively.[14] Further significant factors contributing to the growth of institutional assets have been pension reforms and the falling costs of fund management products, caused in large part by the rise of passive investments, such as ETFs.[15]

The decrease in asset management fees has not been entirely voluntary. The growth of ETFs has played a large role. The fund management industry differentiates between two types of funds. "Active" funds, which typically charge higher fees, have fund managers who take active bets selecting only those stocks they believe will have the best risk versus reward characteristics. "Passive" funds, on the other hand, track established industry benchmarks such as the S&P 500 or the FTSE 100. In the case of passive funds, the aim of the fund manager is to limit the "tracking error" between her fund and the reference index. Tracking error indicates how closely a fund follows an index.

While not proving causality, Figure 1 shows how the rise in the assets of ETFs has been accompanied by a decrease in the fees charged by actively managed mutual funds. The following quote by Larry Fink, the CEO of the world's largest asset manager BlackRock, underlines this dynamic "When I am able to increase margins and increase market share through price cuts, I am going to do that. The key element is scale."[16]

Figure 1 further shows that U.S. equity ETFs have accumulated close to $2.5 trillion in assets over the past decade. This accumulation of assets has come at the cost of active managers. Not only have they had to lower management fees in response to the success of ETFs, ICI (2018) data shows that while ETFs enjoyed cumulative inflows of approximately $1 trillion since 2008, U.S. equity mutual funds suffered equivalent cumulative outflows of approximately $1 trillion over the same period. While initially regarding ETFs as the enemy, many mutual fund companies soon realized they could not afford not to have their own ETF offering. As a result, many of the large fund companies today offer both active mutual funds and ETFs.[17]

The popularity of ETFs and mutual funds has resulted in the ownership structure of companies being turned on its head. While in 1970 it was individual investors that controlled around 70 percent of all outstanding shares in the United

---

14 Useem (1996); Hawley and Williams (2000a); Harmes (2001).

15 While there were only sixteen ETFs in the United States in 1998, this number grew to 1,832 by 2018 (ICI (2018)).

16 *Bloomberg Markets*, 13 January 2017, "BlackRock Sees Record Flows Into Low-Cost ETFs as Passive Rules," available at: https://www.bloomberg.com/news/articles/2017-01-13/blackrock-fourth-quarter-profit-rose-on-etf-inflows-lower-costs (accessed on 20 February 2019).

17 *The Wall Street Journal*, 7 April 2015, "Fidelity's New Chief Confronts Market Shift," provides a history of how Fidelity has dealt with the challenge of ETFs.

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

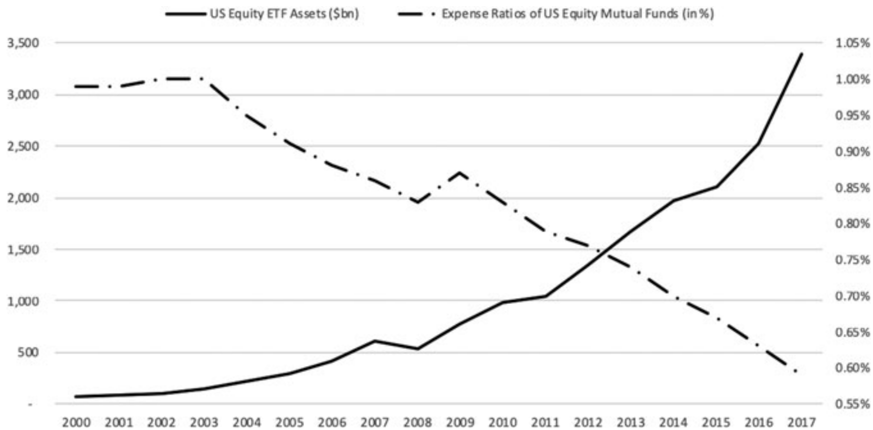

Figure 1: Rising ETF assets coincide with falling expense ratios of actively managed funds
Source: Investment Company Institute (ICI) 2018

States, today it is institutional investors who own 80 percent of the outstanding shares of U.S. companies by market capitalization. Also, much of what remains as individual ownership today is in fact ownership by founders and senior management. This change in ownership structure has had profound consequences for the corporate governance of firms. In the period of "managerialism" that preceded the 1980s, company executives faced a disjointed shareholder base as individual shareholders were faced with a collective action problem in their ability to co-ordinate their views on company policy.[18] "The scattering of stock among thousands of small owners had undercut the capacity of shareholders to oversee their enterprises."[19] However, the onset of asset manager capitalism provided a solution to this collective action problem.[20] This is because "by centralizing investment decision making within disintermediated capital markets, institutional investors seem to have increased the ability of investors to exercise direct forms of power over corporate and sovereign borrowers."[21] In asset manager capitalism it is not the many ultimate investors but their intermediaries that typically engage with companies and exercise the voting power.[22]

While providing a remedy for the collective action problem, asset manager capitalism also poses a new challenge. Ever-greater shareholdings by a relatively

18 Davis (2009).

19 Useem (1996).

20 Hawley and Williams (1997).

21 Harmes (1998), 106.

22 Gilson and Gordon (2013), therefore, identify an "agency cost of agency capitalism." See, also, Bebchuk et al. (2017), Hart and Zingales (2017), and Strine (2019).

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

small number of very large institutional investors means it is increasingly difficult for these institutions to sell their positions in a company without substantial negative price effects. The tracking error constraints that come with passive management further limit the ability to sell. While asset manager capitalism has given investors greater influence over company strategy, if this influence does not suffice to achieve the desired effect in corporate policies, then investors may find themselves in a situation where they have little say and no ability to sell. In Hirschman's terms, asset manager capitalism has increased the potential of voice but decreased the ability to exit.

Choosing between voice and exit

The use of voice is motivated by the (in)ability to exit and the prospect for successful use of voice.[23] As ownership concentration increases, the ability to exit stocks becomes less feasible and voice should become a preferred option. In their 1998 paper "Law and Finance," La Porta, Lopez-de-Silanes, Shleifer, and Vishney (hereafter referred to as LLSV) study the relationship between shareholder concentration and shareholder rights. For their analysis they identified the ten largest companies by market capitalization for each country, excluding companies that were part-owned by governments, as well as financial companies. At the time they found that for U.S. listed companies the median ownership of the ten largest non-financial domestic firms by the three largest shareholders was 12 percent. Table 1 shows that repeating this calculation twenty years later returns a median holding of 19 percent for the United States. This gives an indication of the extent to which ownership concentration in the United States has increased over the past two decades.[24]

But not only have the levels of ownership concentration harmonized across countries, so too have the names on the share register. When one looks at the shareholder registry of a typical company, whether in Germany, the United Kingdom, or the United States, there are six names that come up repeatedly. These are BlackRock, Vanguard, State Street, Fidelity, BNY Mellon Investment Management, and Capital Group. Together these asset managers control approximately $20 trillion of assets, equal to approximately 25 percent of the $79.2 trillion

23 Hirschman (1970).

24 The decrease in concentration in Germany is a special case and the result of the dismantling of "Deutschland AG," which was a structure under which many German companies, banks, insurance companies, and industrial companies, held stakes in one another. This factor outweighed the increase in ownership concentration caused by the growth of asset managers, which has also occurred in the shares of German companies.

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

Table 1: 1998 vs 2018: Ownership of ten largest nonfinancial domestic firms by three largest shareholders

	Germany	UK	U.S.
Mean: LLSV 1998	48%	19%	20%
Mean: own data 2018	21%	16%	20%
Median: LLSV 1998	50%	15%	12%
Median: own data 2018	19%	16%	19%

Source: LLSV (1998), Bloomberg, author's own calculations, as of August 2018

global asset management industry.[25] The assets of these fund management companies are contained in a large number of individual funds. Together they make up "fund families."

Fichtner et al. separate out the passive equity assets and show that BlackRock, Vanguard, and State Street manage over 90 percent of all Assets under Management (AuM) in passive equity funds and that these three institutions (the "Big Three") together constitute the largest owner in 438 of the 500 most important American corporations.[26] Substantial economies of scale are responsible for this concentration of assets in the investment management industry. A fund manager has the same investment universe to look through whether his portfolio has €10 million euro or €1 billion in assets under management so long as the benchmark investment universe remains the same (though fund size will impact what stocks can be invested in from a liquidity perspective). An established fund management team can therefore manage, for example, a doubling of assets without the need for a meaningful increase in resources. Similarly, other staff such as legal and governance support will also not need to be increased so long as the total number of stocks held does not increase in response to the new assets. Index investing further increases the importance of economies of scale, as fees typically explain the majority of any performance differential. Scale has been employed by the larger asset managers to decrease fees with the aim of taking market share from the smaller asset managers, who typically have a higher cost base.[27]

While the increase in ownership concentration is supportive of the use of voice, it has negative consequences for the ability to exit. The ability to sell shares and exit a stockholding is primarily determined by three factors: a fund's

25 Boston Consulting Group (2018).

26 Fichtner et al. (2017).

27 *Bloomberg Markets*, 13 January 2017, "BlackRock Sees Record Flows Into Low-Cost ETFs as Passive Rules," available at: https://www.bloomberg.com/news/articles/2017-01-13/blackrock-fourth-quarter-profit-rose-on-etf-inflows-lower-costs (accessed on 20 February 2019).

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

investment guidelines (whether it is an active or passive fund), the fund managers' willingness to take on tracking error risk, and transaction costs. Since it is passive managers' task to track a reference benchmark as closely as possibly, they will usually opt to buy all stocks contained in such indices.[28] A passive fund manager will not be able to sell a stock for as long as it is contained within her benchmark. Bank of America Merrill Lynch estimates the market share of passive managers at 45 percent.[29]

However, it is not only index funds that are unable to sell. Active managers typically have a universe from which they may pick stocks and a benchmark against which their performance is tracked. If a fund manager decides to sell her holding in a stock that is contained within her benchmark this will increase "tracking error" (similarly, buying a stock that is not included in the benchmark may do the same).[30] Even when funds do not have an official benchmark they track, the fund manager will often have an internal benchmark according to which her performance is measured. In some cases, fund managers may have a formal quantitative "tracking error constraint" that specifies how much tracking risk they may take; in the other cases it will be down to their own discretion and thus their personal risk appetite. Risk appetite will be a function of the pay structure of the fund management company as well as the career risk a fund manager perceives will result from a bad result (closely tracking an index may ensure that one is not one of the worst performers and thus at risk of being let go). In practice, some fund managers have therefore chosen to invest in a manner that has been referred to as "closet indexing" or "benchmark hugging."[31]

Benchmark hugging must not be voluntary though. There are also fund managers who would like to be more active but are liquidity-constrained due to the size of their funds. While the exit of any one individual retail investor is an insignificant affair, the exit of a large institutional shareholder may have a much more substantial impact. Any institutional investor looking to sell out of a stock holding on the

28 Legally they are not required to do so and may, for example, choose to exclude the smallest stocks in an index, though the decision to do so will increase the tracking error. Also, "synthetic" ETFs will enter into "index swap agreements" with banks in order to track the performance of indices rather than buying a basket of individual stocks.

29 CNBC, 19 March 2019, "Passive investing automatically tracking indexes now controls nearly half the US stock market," available at: https://www.cnbc.com/2019/03/19/passive-investing-now-controls-nearly-half-the-us-stock-market.html (accessed on 28 April 2019).

30 Tracking error, also known as active risk, indicates how closely a fund manager tracks the performance of his benchmark. The greater the tracking error, the greater the chance that the fund outperforms or underperforms the index.

31 ESMA (2016).

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

open market will have a negative impact on that company's share price as the size of the institutional investors' stake is likely to be greater than the available liquidity in the stock. Any such "market impact" resulting from a negative impact on the share price contributes to the cost of exit. For a typical mutual fund where the fund manager's performance is evaluated versus that of her peers, at the end of the year a few basis points often make the difference between coming, say, third or fifteenth in a league table. A 2015 study by McKinsey & Company estimated that 10 percent of U.S. assets qualify as "benchmark-hugging."[32] Adding the market share of index funds (45 percent) to this gives an indication of those managers currently unable or unwilling to sell. In today's financial markets "voice" has become more relevant than "exit."

Why passive investors engage

Increased press coverage of corporate governance matters gives the impression of a widespread increase in the number of engagement activities by investors.[33] However, the reality is more mixed. The Big Three asset management firms have bulked up their corporate governance teams significantly in recent years, yet the wider industry changes are subtler than the press attention suggests.[34] Interviews revealed that while the nature and focus of engagement has changed, the actual volume of engagement has remained relatively unchanged in recent years; signified by the fact that investor relations (IR) headcounts at corporate issuers have remained largely constant.

Rather than the number of engagements increasing, it is the type of engagement that has changed. IR managers commented on the increased use of "CEO letters" written by fund management CEOs and addressed to corporate managers. These are either directly released to the press or find their way there indirectly. The IR manager of one U.S. listed corporation explained that when he returned to work

32 For Europe, ESMA (2016) conducted a study on a sample of 2600 funds for the period 2012–14. Their results presented in 2016 indicate that between 5 and 15 percent of equity funds "could potentially be closet indexers."

33 A search for newspaper articles containing the term "shareholder engagement" returned between 16 and 123 articles per year for the period 2006 to 2013. For the years 2017 and 2018, there are 505 and 605 results respectively.

34 *The Financial Times*, 28 January 2017, "BlackRock, Vanguard and State Street bulk up governance staff," reports on the corporate governance staff increases that have occurred at the Big Three. Besides increased engagement, the increased headcount may also be a reflection of asset managers bringing corporate governance functions previously outsourced to proxy advisors in-house.

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

in IR in 2016, after a period of four years working in an operational role, he found "a much bigger marketing element to governance."

Investors have sought to reduce the free-rider problem inherent in governance activity through the establishment of investor networks that amplify the collective voice while reducing the individual investor's costs of engagement. Institutional investors therefore regularly meet both in general forums, such as the United Nations Principles for Responsible Investment (PRI), as well as at designated networks, such as the International Corporate Governance Network (ICGN) or the Ceres Investor Network on Climate Risk and Sustainability (CERES).[35] There they are able to find common ground on which to engage with corporates.

While critics may question the motivation behind investors' engagement, the majority of IR managers described the quality of engagement as good. As the head of IR of a German DAX company put it, there has been a learning curve as both corporates and investors have had to figure out how to handle topics of corporate governance. Overall, IR managers felt that institutional investors are still figuring out how to incorporate corporate governance into their investment processes.[36]

Index funds have no apparent financial incentive to engage with corporates. They are paid only to track an index and any engagement they conduct has costs attached to it. Furthermore, any improvement in corporate governance that results from engagement benefits all other shareholders, enabling them to free-ride. This line of argument, however, ignores the fund management industry's structure. In reality, the Big Three asset managers have such large asset bases and such dominant market positions when it comes to the share of equity inflows captured that the cost of engagement is minimal when compared to the profits they generate.[37] As a result, the benefit from engagement only needs to be marginal to justify the money spent on engagement.[38] Yet as this section will show, the benefits are anything but marginal.

Firstly, the Big Three are not entirely passive investors. On top of their passive assets, BlackRock, Vanguard, and State Street manage $478 billion, $431 billion,

35 CERES comprises more than 150 institutional investors, collectively managing more than $24 trillion in assets.

36 IR managers explained that they typically engage with their top thirty to forty shareholders, who, in sum, represent the vast majority of their outstanding share capital. Amongst these top holders are the relatively well-resourced big index houses and the growing ownership concentration means that these top shareholders represent a growing percentage of the issued share capital.

37 BlackRock company filings show that net income for the twelve months ending 30 September 2018 was $5.69 billion. Fichtner et al. (2017) report a 71 percent ETF market share for the Big Three.

38 Deeg and Hardie (2016) show that at its root the decision to engage is a cost–benefit calculation based largely on investor characteristics.

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

and $102 billion respectively in active assets.[39] That $1 trillion in active assets would require a voting function irrespective of whether passive funds vote or not. In practice, the large asset managers have one corporate governance team that votes all shares of all funds irrespective of whether the mandates are passive or active.[40] Just as with fund management in general, the economies of scale in proxy voting are almost limitless.

Secondly, better corporate governance will lead to higher share prices which will lead to greater inflows.[41] Along these lines, Professor John Kay, author of the United Kingdom's 2012 Kay Review, suggests "it is in the interest of passive managers to engage. If they helped increase the value of their investee companies, this would raise their assets under management and thus their fee income."[42]

While the impact of governance improvements may be reflected in only very minor valuation accretions, failure of governance systems may result in much more significant losses, such as those that occurred in the share prices of Facebook following the data scandal, BP following the Deepwater Horizon oil spill, or Volkswagen AG following the diesel scandal. Their market share means that the Big Three benefit most from equity inflows that result from a country having a strong equity culture. Any such equity culture requires trust in markets and corporate scandals undermine this trust. It is thus in the interest of the big passive managers to ensure no corporate scandals occur in the large benchmark indices. The fact that passive investors, cannot sell out of holdings means that corporate governance is their only control function. Consequently, this may actually make them more incentivized than active managers to ensure good corporate governance.[43] An example of this is the impact of the March 2018 "data scandal" at Facebook and the resultant sell-off in U.S. equities it caused that resulted in $245 billion of market value being wiped off the S&P 500 index on 19 March 2018.

39 Fichtner et al. show that the Big Three asset managers use "coordinated voting strategies and hence follow a centralized corporate governance strategy" (2017: 298). With coordinated voting they are referring to non-differentiated, centralized voting by the corporate governance team. In such cases the corporate governance team votes every share held by the fund family in the same way, irrespective of the individual fund's characteristics. Voting all shares in the same way, ensures giving maximum weight to the institution's voice. However, this uniform voting of shares held by diverse funds with potentially opposing interests has been highlighted as a conflict of interest and a potential break of fiduciary duty by Lipton (2017).

40 Fichtner et al. (2017).

41 Appel et al. (2016a).

42 *The Financial Times*, 26 April 2015, "*Compulsory stewardship by passive managers moves closer*." See, also, Fisch et al. (2018).

43 Appel et al. (2016a).

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

Such significant stock moves can affect the size of the AuM of asset managers in two ways. First, there is the stock specific drop in AuM and second there may be a wider stock market sell-off if the affected stock is of significant enough size. A rough calculation illustrates the potential financial impact: In Q1 of 2018, Blackrock, Vanguard, and State Street held approximately 146.2 million, 173.6 million, and 87 million shares, respectively.[44] On Friday, 16 March, Facebook closed at a price of $185.09. Following the news of the data scandal, the stock closed $12.53 lower at $172.56 on Monday, 19 March, and continued to fall by approximately an additional $20 over the following days. Taking just the initial first-day move equates to a decrease in AuM of $1.83 billion, $2.18 billion, and $1.09 billion for the Big Three, respectively. Assuming an average management fee of 0.1 percent of assets (across passive and active) the loss in revenue would equate to $1.83 million, $2.18 million, and $1.09 million, respectively. However, this loss is not a one-off loss, but lowers the AuM of asset managers in perpetuity. There are several ways to approximate this. One could, for example, treat the $2 million as a negative perpetuity that is discounted with an interest rate to arrive by a present value estimate. Alternatively, one could approximate the loss in income by the negative income this will have to the valuation of the asset manager itself. Asset managers are typically valued at between 1-2 percent of their AuM. In the case of the Facebook example, the $1.83 billion reduction in AuM for BlackRock would, by that logic, equate to a loss of between $18.3 million to $36.6 million.

But the above calculation covers only the stock-specific loss in AuM; there is also the wider market sell-off it triggered. Prior to the Facebook announcement the S&P 500 had a market capitalization of approximately $24 trillion. On 19 March 2018, the S&P 500 subsequently lost 1.17 percent in value. Assuming an average valuation of 1 percent of AuM for the Big Three, and a mean holding of 17.6 percent of S&P companies (Fichtner et al. (2017)), implies that these three asset managers lost as much as $718 million in market value as a result of the S&P 500 move on 19 March 2018.[45] The fewer scandals occur, the safer equities appear and the more assets the passive managers can attract. And while the Big Three might have to pay for it, they also receive a large portion of the inflows.

Bebchuk and Hirst argue that index funds have strong incentives to under-invest in stewardship due to the agency relationship between asset managers and their beneficiaries, the ultimate owners of the assets.[46] Due to the low fees

44 Approximate shareholdings as of Q1/2018, Source: Bloomberg.

45 The $718 million estimate is calculated as follows: $24 trillion (market capitalization of the S&P 500) x 1.17% (market move of S&P 500) x 17.6% (market share of Big Three) x 1% (typical valuation of asset managers). This estimate includes the stock-specific loss resulting from Facebook.

46 Bebchuk and Hirst (2018).

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

they charge, the authors argue, index fund managers will only capture a very small proportion of any increase in company value that their governance efforts generate. The authors provide the following numerical example: An asset manager holding a stock position worth $1 billion increases the value of said company by 0.10 percent as a result of better corporate governance. Since the asset manager only charges a fee of 0.50 percent, they will only capture $5,000 worth of value ($1 billion x 0.10 percent x 0.50 percent). However, this example only considers a very small stock move such as it may result from better governance. It does not account for the annual compounding of this benefit and it does not consider the possibility that a significant stock sell-off might be avoided as a result of better governance.

In addition to these valuation effects, there may also be a marketing consideration to engagement as there may be a "halo effect" emanating from engagement activities. For example, a fund management company challenging excessive executive remuneration is likely to improve their public image. The head of IR of a German DAX corporation said that he believed institutional investors have discovered a positive correlation between their assets under management and the frequency with which they appear in the press with corporate governance issues.[47] A fund manager at a German mutual fund company, who acknowledged that they track the frequency with which they appear in the press for this purpose, confirmed this point. This may also explain why corporates reported engagement mainly from domestic investors and only rarely from international shareholders. Confrontations between investors and their domestic corporations are most likely to gain the attention of the investors' local customer base.[48]

The largest asset managers are likely to benefit the most from the overall halo effect, but even for the smaller managers, corporate engagement, when conducted in the open, is a cheap means of publicity. Along similar lines the IR manager of a U.S. listed corporate noted how "shareholder letters are an interesting dynamic. They are full of platitudes that probably everyone can agree to, but the recommendations are not necessarily actionable. These letters come particularly from passive CEOs and we receive three to five letters regularly. The fact that they are also released to the press tells you a lot about their purpose."[49] However, even critics accept that what may have started as a marketing exercise has matured into serious

47 Brière et al. (2017) explain that institutional investors will engage in "delegated philanthropy." They expect investors to consider issues such as climate change, if they believe such activities represent their clients' values and preferences and enhance the asset managers reputation.

48 This finding is in line with Dimson et al. (2018), who note that investors are more likely to lead coordinated engagement when the firms are domestic and that the success rates are also elevated when the lead investor is domestic.

49 Telephone interview with the head of investor relations and the company secretary of a S&P 500 member, 22 February 2018.

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

governance engagement because retail investors "have taken the bait and are showing interest" in engagement as the head of investor relations for a German DAX company put it. In their study of index fund incentives, Bebchuk and Hirst assume that "stewardship does not affect the flow of funds."[50] Yet this assumption neglects both the existence of the halo effect as well as the fact that the Big Three receive the majority of inflows and thus stand to suffer the greatest losses should a major scandal harm the reputation of stocks as a safe means of investment.

Finally, client demand is an important driver of passive investors' engagement activities. When institutional asset owners outsource their asset management mandates, they typically not only outsource the portfolio management function but also with it proxy voting and engagement functions. Clients will expect proxy voting at the very least and fund managers have reported explicitly charging for this function. Regulators may also have an expectation of what the fiduciary duty towards clients entails. In a world in which ownership concentration has reduced the ability to sell the shares of underperforming companies, institutional investors increasingly have no choice other than to become active stewards of the companies they invest in if they are to fulfill their fiduciary duties towards their clients. Regulatory requirements differ from country to country, and in the case of Germany, for example, proxy voting is not required legally. In the United States employing the services of a proxy advisory firm may suffice for the fulfillment of fiduciary duties.[51] In the United Kingdom the Stewardship Code explicitly states that "For investors, stewardship is more than just voting."[52] Engagement by passive fund managers may therefore also be seen as a safeguard from future regulation.[53] In addition to the previously mentioned marketing-halo, index investors may therefore also engage with companies in order to seek protection from regulation by means of a regulatory-halo.

Ownership concentration and activist campaigns

In recent years, the criticism of passive investors has shifted from accusations of being "absentee landlords" with no "skin in the game" towards unease about

50 Bebchuk and Hirst (2018), 17.

51 However, the situation in the United States is in flux, following the decision in September of 2018 by the SEC (2018) to withdraw the staff issued letters to Egan-Jones Proxy Services (27 May 2004) and Institutional Shareholder Services, Inc. (15 September 2004).

52 Financial Reporting Council (2012).

53 Unlike large banks, the large mutual fund companies are not presently considered Systemically Important Financial Institution (SIFI) as their growing size is not considered to present a financial risk.

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

their influence.[54] At the heart of this debate lies a concern that passive investors may have different objectives to active investors and that these differing objectives could hamper the proxy campaigns of other shareholders, especially activists.[55] What is indisputable is that the sheer size of their combined assets means that in an increasing number of proxy battles they will cast the deciding vote. Their objectives and proxy voting policies, therefore, warrant extra attention.

Passive managers' objectives may differ from those of other shareholders, in particular with regards to three dimensions: time horizon, "universal ownership," and "common ownership." Activist investors may seek certain corporate actions, such as special dividends or disposals of certain business units, to drive up the share price. Some of these measures, however, may only have a short-term impact on share prices. As passive managers cannot sell stocks when they please, they cannot take advantage of corporate actions that increase share prices only in the short-term. In such instances, passive investors may therefore choose to vote against such proposals if they feel the short-term effect may come at the cost of better long-term performance.[56] Unable to sell on bad news, passive investors may be considered as providers of "patient capital."[57]

The concept of universal ownership refers to the fact that the big asset managers hold stakes in virtually every company and thus a slice of the entire economy.[58] Universal owners will therefore care about externalities, such as pollutions, as the costs saved by one portfolio company shirking environmental regulation may be outweighed by additional costs faced by another portfolio company that will need to clean up the pollution. An example of this would be two plants operating on the same river. The company operating the upstream plant saves on filtration devices and pumps its untreated sewage into the river. The

54 *Investments & Pensions Europe*, 2 June 2011, "Absentee landlord' shareholders no longer acceptable – Hermes EOS."

55 Activist investors are typically hedge funds; private, limited partnerships that are most often domiciled offshore for tax and regulatory purposes. They will focus their limited resources on a concentrated portfolio of companies. With the help of leverage, they will purchase significant stakes in companies and call for significant strategy changes, typically involving calls for management changes.

56 In their own words, BlackRock (2017) explains the situation as follows "The performance track records of activist investors are mixed; many have experienced big wins, but many have generated large losses. Generally, activists have a shorter-term view than index investment managers."

57 Deeg and Hardie (2016).

58 United Nations Principles for Responsible Investment, "Macro risks: Universal ownership," available at: https://www.unpri.org/sdgs/the-sdgs-are-an-unavoidable-consideration-for-universal-owners/306.article (accessed on 20 February 2019).

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

downstream plant operated by another firm will need to invest in additional filtration units before being able to use the water.[59]

"Horizontal shareholding," often referred to as "common ownership," may be considered the dark side of universal ownership. The debate here is concerned with the anti-competitive effects that may result from asset managers owning stakes in multiple companies within the same industry. The literature does not assume that there is explicit collusion or that asset managers directly request that companies do not compete. Instead, corporate executives aware of the portfolio holdings of their owners internalize their owners' objective function. Any one company going for market share would do more harm to the industry's combined profits than that one company would generate in additional profits. Common ownership will therefore lead to increased prices as companies do not compete for market share but instead increase price, thereby maximizing returns to their owners' portfolios.[60]

Furthermore, the "blockholder" literature suggest that the Big Three may be harming activist campaigns by further splitting the voice of shareholders.[61] If this were the case, then the rise of index funds should have decreased the presence of activists. However, between 2010 and 2015 activists' assets increased by 269 percent.[62] In fact, following an already busy 2017, activists had their busiest year yet in 2018.[63] Not only has the number of activist campaigns increased, so too has the size of the companies targeted. Campaigns have targeted such "mega cap"

59 The concept of universal ownership was coined by Hawley (2000b) to refer to large asset owners such as pension funds. It has since been applied more broadly also to asset managers, even though these are technically not owners but investors (see UNEP Finance Initiative, 2011). Fichtner and Heemskerk (2018) refer to them as "The New Permanent Universal Owners." See, also, Hawley and Williams (1997).

60 The issue of common ownership has received regulatory attention both in the United States and Europe. See the following papers for a thorough discussion of the anti-competitive effects of common ownership: Azar et al. (2018), Elhauge (2016; 2018), Posner et al. (2018), Schmalz (2018), Scott Morton, and Hovenkamp (2018). Elhauge (2018) posits that "horizontal shareholding" should be used to refer to holdings within the same industry, while "common ownership" should be limited to references concerning overlapping vertical ownership. The issue of common ownership that is not limited to passive funds may also occur with active funds. One example often highlighted is that of Berkshire Hathaway's holdings in the U.S. airline industry.

61 Shareholders with stakes in companies exceeding 5 percent of the issued share capital are commonly referred to as blockholders. This is a very simplistic definition and as Edmans and Holderness (2016) suggest, it may also be worth considering stakes below the 5 percent threshold and to expand the definition to take account of the dollar value of a shareholding.

62 *Investments & Pensions Europe*, 24 February 2015, "Activist hedge fund assets increase 269% over last 5 years — AIMA paper."

63 *The Wall Street Journal* reported "A record of more than 280 companies around the world with market values of more than $500 million were publicly subjected to activist demands in 2018"

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

companies as Nestlé, Unilever, Procter & Gamble, and DowDuPont. This suggests that activists have learned to adapt to the peculiarities of the new finance capitalism.[64] If they are able to mobilize the large fund management companies on their behalf, the necessity for proxy battles with corporate management teams may decrease, thereby significantly reducing the activists' costs and reducing any free-rider problem. There is thus no need to curtail the voting rights of index investors in order to ensure activists continue to play their role within capital markets.

A strategy followed by activists in their communication with other investors is to publish online presentations explaining the business case for their campaigns, often on dedicated internet domains registered for this purpose.[65] The purpose of these presentations is to explain the activist's thinking and to give other shareholders the means to engage the target companies more easily. One European activist investor explained that they seek contact with the large mutual fund companies in order to convince them of their arguments and to encourage them to engage with the corporate in question. Another European activist explained that they will regularly look at the shareholder structure, and even look up the proxy advisors employed by the largest shareholders, before deciding on whether and how to engage with a corporate. In the August of 2018, I sat in on such a call between an American activist and a German mutual fund company. The activist explained that the purpose of the call was a mutual exchange of views and to see whether the mutual fund company could be persuaded to engage the corporate. The activist explained that they had scheduled calls with fifteen institutional investors representing approximately 10 percent of the company. The activist acknowledged that companies expected activists to be "loud" and that as a result the voice of traditional institutional investors carried greater weight due to the fact that they raised their voice less frequently.[66]

Indeed, an issue that was brought up repeatedly in the interviews with corporates was the fear that activists could instrumentalize passive investors. The same fear has been raised with regards to the proxy advisor industry. However, an example involving the activist investor Nelson Peltz indicates that activists have a mixed record in mobilizing passive investors: In 2017, Nelson Peltz took on the management of Procter & Gamble and tried to gain a seat on the board. According

https://www.wsj.com/articles/activist-investors-gain-clout-as-stocks-tumble-11545825600 (accessed on 20 February 2019).

64 This finding is in line with Appel et al. (2016b).

65 For an example of Elliott Associates' campaign at the U.S. utility Sempra Energy, see the following website: http://web.archive.org/web/20180616191049/https://sustainablesempra.com/ (accessed 28 April 2019). For a list of activists' presentations, see: https://www.10xebitda.com/hedge-fund-presentations/ (accessed on 20 February 2019).

66 This finding is in line with the shareholder salience literature; see, for example, Gifford (2010).

to CNBC Peltz lost the vote by 0.2 percent this is despite winning the support of the three big proxy solicitors, Egan-Jones, Glass Lewis and ISS. State Street and BlackRock sided with Peltz, while Vanguard backed Procter & Gamble. This is noteworthy for two reasons: the proxy advisors were not on the winning side, and the three big passive houses did not vote in concert with one another. This implies that, at least in such large high-profile cases, index investors are carefully considering their voting decisions.[67]

Conclusion

"It's amazing how all those tiny nest eggs can add up when you put them together and let a handful of people decide how to invest them."[68]

The growth of the asset management industry, and its ownership concentration in particular, poses both a major opportunity and significant challenge. More influential shareholders provide better oversight of corporate conduct. If investors do so only by constraining the ability for corporate executives to enrich themselves (principal-agent thinking), the increased influence of shareholders may be a net-positive for society. If, however, the increased influence comes at the cost of other stakeholder groups such as employees and consumers, recent trends in ownership concentration may raise social concerns. The debates surrounding the desirability of share buybacks, investigations into common ownership, as well as the debates in the United Kingdom and the United States about adopting worker representation on company boards are indicative of this.

"Corporate power and responsibility are matters of public concern" and as such these new institutions, with the means to challenge corporate conduct, are also of public concern.[69] It is therefore imperative that we question the policies and processes by which these investors engage with corporate issuers. However, we also have to acknowledge that the control of corporate power is the first-order concern, while the means by which asset managers seek to exercise control over their investee companies is the second-order concern. Limiting the influence of institutional investors, risks forgoing the opportunity to employ them for the benefit of private governance alongside regulatory governance.

67 With regards to the risk of instrumentalization of the Big Three passive managers by activists, it is also unclear how the interests of their approximately $1 trillion of active asset influences their overall voting decision. In theory, consideration for their smaller active assets could also be driving the proxy voting decisions.

68 Harmes (2001).

69 Brammer et al. (2012).

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

Global asset managers increasingly match the global footprint of the companies in which they invest. This means they have the potential to act as global standard setters working alongside governmental oversight. Serafeim therefore argues for index funds, benchmark-constrained active funds, and large pension funds to act as the "stewards of the commons."[70] With their long time horizons and common ownership they are able to provide the "commitment mechanism" necessary to ensure that companies work together to internalize externalities created within each industry.

Rather than the big asset managers exercising too much influence, there appears to be too little engagement beyond the domestic, high-profile, "mega-cap" companies. Indeed, the extent of shareholder influence on corporate policies to date is unclear.[71] The level of critical engagement appears to be in its infancy, with Fichtner et al. reporting that the Big Three vote with management in more than 90 percent of all proxy votes.[72] The *Financial Times* further reports that BlackRock, as the world's largest asset manager, said it had never filed a shareholder resolution.[73] The Big Three will need to become active stewards in order to avoid the "power vacuum" that would leave "corporate chieftains unaccountable."[74]

Hirschman posits that the "decision on whether to exit will often be taken in the light of the prospects for the effective use of voice."[75] In this regard, the increased ownership concentration has reduced the cost of voice, as any engagement costs can now be spread across a greater asset base. Moody's Investor Service estimates passive investing will overtake active in just four to seven years in the United States.[76] The future of engagement will depend, in part, on how the market share of passive managers develops in relation to active managers and

70 Serafeim (2018).

71 Knafo and Dutta (2016) suggest that while shareholders are often blamed for encouraging short-sighted corporate decision making, this reasoning likely overstates the influence investors have had in decades past.

72 Fichtner et al. (2017). See also Bebchuk and Hirst (2018) for a criticism of index funds' tendency to be deferential to corporate managers.

73 *The Financial Times*, 24 November 2018, "BlackRock takes on proxy advisers in dispute over investor rights." In fact, almost all the asset managers I interviewed stated that they did not file shareholder proposals as this required specialist legal knowledge and because asset owners were likely better placed to take on such issues.

74 John Bogle founder of Vanguard, warning on index funds' concentration of ownership in an interview with the *Wall Street Journal* (*The Wall Street Journal*, 29 November 2018, "Bogle Sounds a Warning on Index Funds," John C. Bogle, available at: https://www.wsj.com/articles/bogle-sounds-a-warning-on-index-funds-1543504551).

75 Hirschman (1970), 37.

76 Moody (2017).

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

how the market share of the Big Three develops within the passive market. If passive assets continue to grow faster than active assets and the Big Three continue to take the lion's share of new inflows, then perhaps little will change as the voting "degradation" that comes with growing passive investing is counterbalanced by the fact that the majority of new passive assets are won by the comparatively well-resourced large houses. They may control the outcome of shareholder interventions as Shapiro Lund suggests, but it is likely they will do so from an informed position, at least as regards the largest proxy battles.[77]

References

Appel, Ian R., Todd A. Gormley, and Donald B. Keim. 2016a. "Passive Investors, Not Passive Owners." *Journal of Financial Economics* 121 (1): 111–41.

Appel, Ian R., Todd A. Gormley, and Donald B. Keim. 2016b. "Standing on the Shoulders of Giants: The Effect of Passive Investors on Activism." *The Review of Financial Studies. Advance online publication available at:* https://doi.org/10.1093/rfs/hhy106 (accessed on 19 February 2019)

Azar, José, Martin C. Schmalz, and Isabel Tecu. 2018. "Anticompetitive Effects of Common Ownership." *Journal of Finance* 73 (4): 1513–65.

Boston Consulting Group. 2018. "*Global Asset Management 2018—A Digital Metamorphosis.*" Available at: http://image-src.bcg.com/Images/BCG-The-Digital-Metamorphosis-July-2018-R_tcm30-197509.pdf (accessed on 19 February 2019).

Bebchuk, Lucian A., Alma Cohen, and Scott Hirst. 2017. "The Agency Problems of Institutional Investors." *Journal of Economic Perspectives* 31 (3): 89–102.

Bebchuk, Lucian A., and Scott Hirst. 2018. "Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy." *ECGI - Law Working Paper*, No. 433/2018. Available at: https://ecgi.global/sites/default/files/working_papers/documents/finalbebchukhirst.pdf (accessed on 19 February 2019).

BlackRock. 2017. "Index Investing and Common Ownership Theories." Available at: https://www.BlackRock.com/corporate/literature/whitepaper/viewpoint-index-investing-and-common-ownership-theories-eng-march.pdf (accessed on 19 February 2019).

Brammer, Stephen, Gregory Jackson and Dirk Matten. 2012. "Corporate Social Responsibility and institutional theory: new perspectives on private governance." *Socio-Economic Review* 10 (1): 3–28.

Braun, Benjamin. 2016. "From performativity to political economy: index investing, ETFs and asset manager capitalism." *New Political Economy* 21 (3): 257–73.

Brière, Marie, Sébastien Pouget and Loredana Ureche-Rangau. 2017. "*BlackRock vs Norway Fund at Shareholder Meetings: Institutional Investors' Votes on Corporate Externalities*." Presentation at the Chaire FDIR. Available at: http://fdir.idei.fr/wp-content/uploads/2014/01/Pouget-Presentation-14-Decembre-FDIR.pdf (accessed on 19 February 2019).

Davis, Gerald F. 2009. "*Managed by the markets: how finance reshaped America*." New York: Oxford University Press.

77 Shapiro Lund (2017).

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

Deeg, Richard, and Iain Hardie. 2016. "What is patient capital and who supplies it?" *Socio-Economic Review* 14 (4): 627–45.
Dimson, Elroy, Oğuzhan Karakaş, and Xi Li. 2018. "Coordinated Engagements." SSRN. Available at: https://ssrn.com/abstract=3209072 (accessed on 19 February 2019).
Drucker, Peter. 1993. "*Post-capitalist society*." New York: Harper Business.
Edmans, Alex, and Clifford Holderness. 2016. "Blockholders: A Survey of Theory and Evidence." *IDEAS Working Paper Series* from RePEc.
Elhauge, Einer R. 2016. "Horizontal Shareholding." *Harvard Law Review* 129 1267–1317.
Elhauge, Einer R. 2018. "How Horizontal Shareholding Harms Our Economy – And Why Antitrust Law Can Fix It." SSRN. Available at: https://ssrn.com/abstract=3293822 (accessed on 19 February 2019).
European Securities and Markets Authority (ESMA). 2016. "*Statement—Supervisory work on potential closet index tracking*." Available at: https://www.efama.org/Publications/Statistics/Other%20Reports/EFAMAReportClosetIndexFunds.pdf (accessed on 19 February 2019).
Fichtner, Jan, and Eelke Heemskerk. 2018. "The New Permanent Universal Owners: Index Funds, (Im)patient Capital, and the Claim of Long-termism." SSRN. Available at: https://ssrn.com/abstract=3321597 (accessed on 19 February 2019).
Fichtner, Jan, Eelke Heemskerk, and Javier Garcia-Bernardo. 2017. "Hidden power of the Big Three? Passive index funds, re-concentration of corporate ownership, and new financial risk." *Business and Politics* 19 (2): 298–326.
Financial Reporting Council. 2012. "*The UK Stewardship Code*." Available at: https://www.frc.org.uk/getattachment/d67933f9-ca38-4233-b603-3d24b2f62c5f/UK-Stewardship-Code-(September-2012).pdf (accessed 19 February 2019).
Fisch, Jill, Assaf Hamdani, and Steven Davidoff Solomon. 2018. "Passive Investors." *ECGI Working Paper Series in Law*, Working Paper No. 414/2018.
Gifford, James. 2010. "Effective Shareholder Engagement: The Factors that Contribute to Shareholder Salience." *Journal of Business Ethics* 92 (Suppl. 1): 79.
Hall, Peter, and David Soskice. 2001. "*Varieties of Capitalism: The Institutional Foundations of Comparative Advantage*." Oxford: Oxford University Press.
Harmes, Adam. 1998. "Institutional Investors and the Reproduction of Neoliberalism." *Review of International Political Economy* 5 (1): 92–121.
Harmes, Adam. 2001. "*Unseen Power: How Mutual Funds Threaten the Political and Economic Wealth of Nations*." Toronto: Stoddart.
Hart, Oliver D., and Luigi Zingales. 2017. "Companies Should Maximize Shareholder Welfare Not Market Value." *ECGI—Finance Working Paper*, No. 521/2017.
Hawley, James, and Andrew T. Williams. 1997. "The Emergence of Fiduciary Capitalism." *Corporate Governance: An International Review* 5 (4): 206–13.
Hawley, James, and Andrew T. Williams. 2000a. "*The Rise of Fiduciary Capitalism—How Institutional Investors Can Make Corporate America More Democratic*." Philadelphia: University of Pennsylvania Press.
Hawley, James, and Andrew Williams. 2000b. "The Emergence of Universal Owners." *Challenge* 43 (4): 43–61.
Hirschman, Albert O. 1970. "*Exit, voice and loyalty: responses to decline in firms, organizations, and states*." Cambridge, MA: Harvard University Press.
Investment Company Institute (ICI). 2018. "2018 Investment Company Fact Book." Available at: https://www.ici.org/pdf/2018_factbook.pdf (accessed on 19 February 2019).

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press

Knafo, Samuel, and Sahil J. Dutta. 2016. "Patient capital in the age of financialized managerialism." *Socio-Economic Review* 14 (4): 771–88.

La Porta, Rafaela, Florencio Lopez de Silanes, Andrei Shleifer, and Robert W. Vishny. 1998. "Law and Finance." *Journal of Political Economy* 106 (6): 1113–55.

Lipton, Ann. 2017. "Family Loyalty: Mutual Fund Voting and Fiduciary Obligation." *The Tennessee Journal of Business Law* 19 (175).

Moody's. 2017. "*Moody's: Passive investing to overtake active in just four to seven years in US; global traction to pick up*." Available at https://www.moodys.com/research/Moodys-Passive-investing-to-overtake-active-in-just-four-to–PR_361541 (accessed on 19 February 2019).

Posner, Eric, Fiona Scott Morton, and Glen Weyl. 2018. "A Proposal to Limit the Anti-Competitive Power of Institutional Investors," *Antitrust Law Journal* 81 (3).

Schiehll, Eduardo, and Henrique C. Martins. 2016. "Cross-National Governance Research: A Systematic Review and Assessment." *Corporate Governance: An International Review* 24 (3): 181–99.

Schmalz, Martin C., 2018. "Common Ownership Concentration and Corporate Conduct." *CEPR Discussion Paper* No. DP12598.

Schnyder, Gerhard, Mathias Siems, and Ruth Aguilera. 2018. "Twenty years of 'Law and Finance': time to take law seriously." *Socio-Economic Review* published online 2 November 2018.

Scott Morton, Fiona and Herbert Hovenkamp. 2018. "Horizontal Shareholding and Antitrust Policy." *Yale Law Journal* 127 (7): 2026–47.

SEC (U.S. Securities and Exchange Commission). 2018. "*Statement Regarding Staff Proxy Advisory Letters*." Available at: https://www.sec.gov/news/public-statement/statement-regarding-staff-proxy-advisory-letters (accessed on 19 February 2019).

Serafeim, George, 2018. "Investors as Stewards of the Commons?" *Journal of Applied Corporate Finance* 30: 8–17.

Shapiro Lund, Dorothy. 2017. "The Case Against Passive Shareholder Voting." *Coase-Sandor Working Paper Series in Law and Economics* 829. Available at: https://chicagounbound.uchicago.edu/law_and_economics/846/ (accessed on 19 February 2019).

Strine, Leo E. 2019. "Fiduciary Blind Spot: The Failure of Institutional Investors to Prevent the Illegitimate Use of Working Americans' Savings for Corporate Political Spending." University of Pennsylvania, Institute for Law & Economics, Research Paper No. 19-03.

UNEP Finance Imitative. 2011. "Universal Ownership - Why environmental externalities matter to institutional investors." Available at: https://www.unepfi.org/fileadmin/documents/universal_ownership_full.pdf (accessed on 19 February 2019).

Useem, Michael. 1996. "*Investor capitalism: how money managers are changing the face of corporate America*." New York: Basic Books.

https://doi.org/10.1017/bap.2019.2 Published online by Cambridge University Press