A model of capital market pressure

Abstract

This study investigates the nature of capital market pressure as a tool for corporate control by performing nine interviews with senior management and board members from nine Swedish corporations listed on Nasdaq OMX Stockholm Large Cap and Mid Cap. The analysis presents significant support for previous research but also extends the existing theoretical framework. A model of capital market pressure is developed which contributes with a systematized way of analyzing capital market pressure. The model distinguishes between formal and informal pressure. Formal pressure is exercised by shareholders through voting and informal pressure is perceived implicitly through actions by the owners, financial reports, analysts, stock price and media. Additionally, the model highlights the interrelationships between these channels and the controllability of such pressure.

Keywords: Capital market pressure, short-termism, financialization, corporate governance, corporate control

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1 Introduction

1.1 Background

Senior management have to be able to balance the short- and long-term needs of their business (Ernst & Young, 2014). Yet, there are evidence suggesting capital markets focus excessively on the short-term and induce managerial myopia. Investors on the capital markets who seek short-term returns will exert pressure on corporate management to align their interests. The capital market pressure interferes with the managers' ability to balance the short- and long-term needs of the business.

The relationship between investors and managers have been prescribed as a principal-agent relationship (Shleifer & Vishny, 1997). Investors have been portrayed to have a couple of tools of corporate control at hand; appointment and dismissal of the CEO and setting remuneration schemes (Ernst & Young, 2014). The financialization of the economies have led to the rise of the shareholder value ideology and practice of shareholder value maximization in the corporate governance models (Palley, 2008). The concentration of ownership and power has increased in the hands of large institutional investors; institutional ownership accounts for over 80 % of UK equities (Roberts, et al., 2006). Institutional owners have at many times been accused for causing managerial myopia (Wahal & McConnell, 2000). They have been blamed for having a short-term perspective; valuing short-term gains instead of long-term value investing (Marston & Craven, 1998). Through their tools of corporate control, they have aligned senior management with their short-term interests. A large study performed by Graham, et al. (2005) disclosed almost 80 % of the CFOs of the largest listed firms in the U.S. would sacrifice economic value of the firm in order to meet consensus estimates. Short-termism is likely to continue in an ongoing financialization regime (Clarke, 2014). Lipton, et al. (2009) argues:

> *"Short-termism is a disease that infects American business and management and boardroom judgment. But it does not originate in the boardroom. It is bred in the trading rooms of the hedge funds and professional institutional investment managers who control more than 75% of the shares of most major corporations."*
>
> *(Lipton, et al., 2009)*

Nevertheless, corporate governance has been found to go beyond hard wired controls, through more implicit and active influence processes (Roberts, et al., 2006; Holland, 1998). Senior management is constantly contained by their investors desire; they are controlled by a 'disciplinary device'. In the spirit of financialization and short-termistic capital markets, my study further explores capital market pressure as a corporate governance mechanism and extends the existing theoretical framework by constructing a model of capital market pressure.

1.2 Purpose and research question

It is argued that capital market pressure might cause managerial myopia and short-termistic behavior underneath certain circumstances (Bolton, et al., 2006; Demirag, 1995; Ernst & Young, 2014; Graham, et al., 2005; Hayes & Abernathy, 1980; Lipton, et al., 2009; Marston & Craven, 1998; Miles, 1993; Porter, 1992; Stein, 1989; Wahal & McConnell, 2000). Plenty of research have quantitatively analyzed the effects of market pressure. However, such studies have merely enriched our understanding of how capital market pressure functions. They have claimed to contribute to the debate of short-termism and market pressure, yet our understanding remain ambiguous.

There exist a small amount of qualitative research (Barker, 1998; Holland, 1998; Roberts, et al., 2006) which have already significantly contributed to our understanding of capital market pressure. Yet the picture is far from clear. More research is needed to further develop our knowledge; hence this study aims to further investigate capital market pressure by interviewing senior management in Swedish listed corporations. My ambition is to understand what previous research has not been clear about; how do senior management experience pressure from capital markets. Ultimately, my research will develop the existing theoretical framework for understanding corporate governance, what seems to be of great importance in the spirit of financialization. This study is set out to answer; how do senior management experience capital market pressure?

1.3 Demarcation of research area

This study has emerged in the spirit of financialization. Yet, financialization is a very broad expression as it describes a fundamental change in the economy and society. Financialization includes the increasing role of financial markets in the economies which has countless possible impacts and can thus be explored in numerous ways. My research does not intend to explore the broad scope of financialization, but the potentially rising capital market pressure exerted by the incumbents.

The study will be limited to nine Swedish listed companies on Nasdaq OMX Stockholm and to senior management and board members that are or has recently been employed in these companies. The Swedish economy has experienced a high degree of financialization (Belfrage, et al., 2017). The economy has well developed financial and capital markets which gives this study great conditions for pursuing its purpose.

2 Previous research

Through my research I intend to explore capital market pressure. In order to develop my understanding of capital market pressure, I will first carry out a rigorous examination of previous research that will be useful in my study. This section will be devoted to exploring what previous research has found and what theories has been established. The material presented in this section will lay the foundation for my own research.

2.1 Financialization

Financialization refers to the increasing importance of financial markets in the economy (Palley, 2008; Belfrage & Kallifatides, 2018; Assa, 2012). Its three major impacts are (Palley, 2008); the increasing significance of the financial sector compared to the real sector; the transfer of income from the real to the financial sector and; the contribution to increased income inequality and wage stagnation.

In Sweden the financialization is evident (Kallifatides & Belfrage, 2018); the financial sector is enjoying a growing significance within the economy, the profit rates of the Swedish financial corporations have increased substantially relative to the non-financial sector and Sweden is suffering from rapidly rising rates of inequality. Profits of Swedish banks as percentage of Swedish GDP amounted to 0.5% in 2002 and 2.25% in 2014 (Kallifatides & Belfrage, 2018). In the period between 2005-2014, the Swedish financial corporations generated more profits than all non-financial corporations measured as share of national disposable income (Kallifatides & Belfrage, 2018).

One way the financialization has effected the economies is by the rise of the shareholder value ideology and practice of shareholder value maximization in the corporate governance models (Palley, 2008). These new practices alter corporate behavior and align it with the interests of the financial markets by putting focus on maximization of shareholder value as the primary objective.

The issue of corporate governance has been stamped as an agency problem within established economic theory and as a result, corporate managers are threatened by takeover or dismissal if the firm profits are not maximized (Palley, 2008). Senior management and organizational practices are shaped by ‘short-termist’ capital (Kallifatides & Belfrage, 2018). Managers are also offered stock options to align the interests of the managers and the investors. Both of these practices possibly incentivizes top management to maximize the short-term stock price due to obsessive emphasis on financial performance measures by the capital markets (Palley, 2008). The focus on financial performance measures infuses the whole organization, in turn shaping the duty of the corporate manager (Kallifatides & Belfrage, 2018).

2.2 Corporate Governance

In a corporation, there is often a separation of management and finance, or expressed in a different way as ownership and control (Shleifer & Vishny, 1997). Corporate governance is about ensuring managers act in the interest of the financiers. At the heart of corporate governance lies the agency problem (Shleifer & Vishny, 1997). The agency problem could be described as the issue of the financiers to make sure that managers are using their money to actually create value for them; what is actually in their interest.

One of the most basic ways of dealing with agency problems are contracts (Shleifer & Vishny, 1997). The investor hires a manager and they agree on a contract specifying the employment, including what the manager may or may not do with the money provided by the investor. However, neither is it feasible to specify every single detail and nor does the investor want to; one of the reasons to why the manager was chosen in the first place was his or her expertise in management (Shleifer & Vishny, 1997; Holland, 1998). There will be room for management discretion, giving the manager rights to take action based on his or her expertise under certain circumstances. However, the manager may consequently take action in pursuit for personal benefits which are potentially costly for the investor. One way of dealing with this issue is to create long term incentive contracts where the component of pay is large enough to outweigh the marginal value of personal benefits (Shleifer & Vishny, 1997). Examples of such common incentive contracts are stock options and share ownership.

Stock options has increased in popularity and has gained a lot of attention (Yermack, 1995). There is an ongoing debate about whether stock options or performance linked pay actually decrease the costs related to agency problems. Yermack (1995) found that the most CEO compensation contracts that exist in practice are not in line with theoretical agency models of optimal contracting. Other studies have revealed that performance linked pay may lead to unintended effects such as earnings management (Abowd & Kaplan, 1999) or 'short-termistic' behavior (Bolton, et al., 2006).

The investors ability to make sure managers are pursuing what is in their interest largely depends on one corporate governance practice; the shareholders' ability to vote and appoint the board of directors (Shleifer & Vishny, 1997; Shleifer & Vishny, 1986; Ernst & Young, 2014). The board in turn has the power to appoint and dismiss the CEO and establish the remuneration scheme. Consequently, the CEO is very much in the hands of the board and can effectively influence the behavior of the CEO. By having tools for corporate control at hand, the investors can exert pressure to potentially force the management to deliver financial results in a short time horizon. Research has shown the existence of many mechanisms for corporate control. When the corporate control mechanism operating through the board of directors is too slow and costly, the market for corporate control can be utilized (Jensen, 1988). The market for corporate control ultimately refers to the threat of takeover, it is where alternative management teams compete for right to manage corporate resources. Additionally, financial reporting increases transparency and enables the investors to follow up, most commonly on a quarterly basis, on short-term financial measures and potentially pressuring management to perform every quarter. Market communications such as earnings guidance potentially exacerbates pressure additionally. Further, 'jawboning' might be used by larger shareholders which refers to informal negotiations with management to institute changes (Shleifer & Vishny, 1986).

The tools for corporate control which have been presented so far has been identified to be used quite carefully (Holland, 1998). Instead, there are more informal and implicit types of corporate control (Holland, 1998; Roberts, et al., 2006). In fact, "separation of ownership and control" seem to be a simplified image of reality. Corporate governance goes beyond hard wired controls, through more implicit and active influence processes; through social control. The influence on management is subtle and can be presented as *"[...] the disciplinary effects of such ways of knowing; the effects on executives of the knowledge of such scrutiny."* (Roberts, et al., 2006, p. 282). The meetings between the senior management and investors can be seen as a ritual which serves as a reminder of the interest of the shareholders in the company and thereby achieving permanent presence in the minds of the managers. Movements of stock price, press comments and analysts' recommendations also serve as constant reminders.

"[…] the discipline is realized in anticipation within the self, or at least rationalized in a defensive way that presents the self as already wanting what the investor wants." (Roberts, et al., 2006, p. 283)

Pre-conditioning is a tool for corporate control which arises through the implicit influence processes. It is used by financial institutions on their portfolio companies (Holland, 1998). Through private meetings and dialogues, the portfolio companies internalizes the interests of the financial institutions and consequently they align their policies and structures to the needs of the financial institution. Public pressure in the form of media leaks and symbolic stock sales are used to intensify the pressure on reluctant executives. However, when the financial institution has to intervene they may pursue formal ways of corporate control and kick out 'bad' management. Additionally, such actions deliver a very strong signal to other portfolio companies to not get into such circumstances.

The level and explicitness of pressure exerted has been found to be correlated with the well-being of the company (Holland, 1998; Gordon & Pound, 1993; Smith, 1996) and consequently also the macro economic state of the economy. First, stock price performance has been found to be inversely correlated with the probability of being targeted for shareholder activism (Gordon & Pound, 1993; Smith, 1996). Secondly, when the company is performing well, the implicit pressure is limited to informed questioning on matters like strategy (Holland, 1998). During times of struggle, more explicit methods tend to be used, such as dismissal of the CEO. The following quote originates from an interview with a top manager from one of Britain's largest investors:

"Our strength increases the weaker the company's position is. Until the company's strategy has been proved wrong all one is doing is exchanging opinions." (from Holberton, 1990, collected from Holland, 1998, p. 257)

Thirdly, firm size and level of institutional ownership have been found to be positively correlated with shareholder activism (Smith, 1996).

2.2.1 Interaction between management and investors

Senior management commit considerable amount of time and effort to the process of keeping the capital market informed (Barker, 1998). Credibility with the market is highly important and the market does not like surprises. Interpersonal meetings and interactions between financial institutions and their portfolio companies are of great importance for both parties; both draw considerable value from these meetings (Roberts, et al., 2006; Holland, 1998; Barker, 1998). Financial institutions even rank the meetings as the most important source of information regarding the company (Roberts, et al., 2006; Barker, 1998). They want to understand management personalities and qualities, and ultimately how the management might contribute to the financial performance in the company (Holland, 1998). "How well do managers know their business?" and "how have they performed according to earlier promises?" (Roberts, et al., 2006). For the portfolio companies, the meetings are an important opportunity for building understanding of strategy, future direction, receive feedback, build investor loyalty and manipulate expectations etc. Managers know investors have created a certain picture of the company and are taking investment decisions on this basis. The meetings are seen as an opportunity to influence the picture and thus manipulate the investment decisions. Holland (1998) interviews a representative from a financial institution:

> *"Meetings are about 'reading the personalities' in the company, interpreting the verbal nuances in the chairman's statements, and closely observing the behavior of executives." (Holland, 1998, p. 253)*

2.3 Capital market pressure and short-termism

Management has to balance the short- and long-term needs of a business in order to survive (Ernst & Young, 2014). There is evidence indicating capital markets excessively focus on the short-term and subsequently senior management act thereafter. This phenomenon is known as short-termism; the excessive focus on the short-term while potentially sacrificing economic value of the firm. Based on corporate governance theory, investors that seek short-term returns will exert pressure on corporate management to align their interest. Capital market pressure has been shown to alter companies' performance management systems, leading to a large focus on 'lagging' financial measures (Kraus & Lind, 2010). The capital market pressure ultimately interferes with the managers' ability to balance the short- and long-term needs of the business. The following section further explores previous research about capital market pressure and short-term behavior.

There has been a long ongoing debate regarding the existence of short-termism. U.S. managers have been criticized to be the reason to why American businesses experienced a deterioration of competitive strength (Hayes & Abernathy, 2007). Data showed the rate of productivity growth in America had declined during 1960s to the 1980s compared to Europe and Japan, and America was loosing its leadership position in various industries. The U.S. managers were blamed due to their failure of not pursuing long-term competitive investments and rather focus on short-term financial gain. Porter (1992) recognized the whole U.S. system of allocating capital as a failure leading to deterioration of competitive advantage. He observed the systems of Germany and Japan and partly recognized that investments in PP&E and intangible assets were higher than in the U.S. Furthermore, American CEOs believed their companies had shorter investment horizons than their international competitors and capital market pressure reduced long-term investments.

Kaplan (1984) addresses three types of short-run behavior where the most damaging is said to be, in similarity to what Porter (1992) later recognized, the reduction of expenditures on discretionary and intangible investments to improve the reported short-term profitability of the profit center. One may speculate why these kind of short-term behaviors have arisen; Kaplan explains how the pressure for short-term financial performance did not simply exist the same way in the 1920s and 1930s as in the 1970s and 1980s. Back then, performance measures could be based on averages of an entire business cycle. Ernst & Young (2014) concludes that financialization has contributed a lot to the rise of short-termist behavior; the growth of financial markets and international capital flows has led to reduced transaction costs, thus increasing the market volatility and potential short-term gain. More developed financial intermediation services have led to more investment opportunities and greater potential for short-term returns. This has also led to changes in the shareholding structure; a growing role of institutional investors with an increasing short-term investment horizon.

Financial institutions have many reasons to put short-term pressure on management because they operate under such pressure themselves, their portfolio performance is measured on a quarterly basis (Demirag, 1995). If shareholders do not understand the rational of long-term strategies, they will respond excessively to short-term performance measures. The better they understand the acitivites of the firms, the more carefully they are able to evaluate the performance of the company. However, investment analysts and institutional shareholders have been found to often lack the necessary skills to value long-term technology investments.

Several studies have tested the market for short-termism (Miles, 1993; Wahal & McConnell, 2000). Miles approaches the potential short-termism in the UK market by assessing whether the discount rates implicit in the market valuations applied to cash flows which accure in the longer term are too high. His results did not strongly support the theory of short-termism, however clearly stating that one may not simply say that short-termism do not exist. McConnell (1985) looked at how corporate investment decisions influenced company stock price and found that for industrial firms, announcements of increases in planned capital expenditures are associated with significant excess stock returns and vice a versa. Thus, a manager seeking to maximize the value of the firm would whenever possible pursue a positive NPV investment. Stein (1989) later built on this reserach and gave evidence for a manager who want to increase the stock price can behave myopically even if the markets are fully efficient. His evidence is laid out through a signal-jamming model where managerial myopia could be viewed as the Nash equilibrium outcome of a noncooperative game between the managers and the stock market. Managers are trapped into behaving myopically:

> *"The stock market uses earnings to make a rational forecast of firm value - higher earnings today will be correlated with higher earnings in the future. Knowing this, managers will attempt to manipulate stockholders' signals, pumping up earnings to raise forecasted value. In equilibrium the market is not fooled by this jamming: it correctly conjectures that there will be a certain amount of earnings inflation, and take this into account in making its predictions [...] if the market conjectures no myopia, managers will have an incentive to fool it by boosting its current earnings." (Stein, 1989, p. 656)*

Wahal and McConnell (2000) investigated if insitutional investors exacerbate managerial myopia using expenditures for R&D and PP&E as a proxy for short- vs. long-term tradeoff. They found a positive relation between institutional investors and industry-adjusted expenditures for R&D and PP&E, indicating that institutional investors does not exacerbate managerial myopia and showing some evidence against the existence of short-termism.

There are also several studies which have investigated capital market short-termism through surveys with different capital market participants (Graham, et al., 2005; Martson & Craven, 1998; Demirag, 1995). If the markets are truly short-termistic or not is of less importance, if managers perceive the capital markets as short-termistic they will behave in such manner like a self-fulfilling prophecy (Demirag, 1995). 47,4% of surveyed group CFOs of UK companies frequently experience pressure for short-term profit maximization from capital markets which they also impose on subordinates which tends to reduce R&D expenditures and other activities required for successful innovation. 48,7% perceived a strong bias against high risk long-term research in favour of lower risk short-term product development. Graham, et al., (2005) surveyed 401 financial executives and found that the majority would give up economic value in exchange for smooth earnings and they would avoid investing in a positive NPV project if it would lead to missing the current quarter's consensus earnings. Martson & Craven (1998) gave evidence for that the market should not be seen as a homogenous group of actors exerting short-term pressure on organizations.

2.4 Shortcomings of previous research

I have now reviewed previous research about capital market pressure through existing theory and empirics. My review revealed several shortcomings that I would like to address. Little qualitative research has been done of capital market pressure. Quite a lot of research have quantitatively analyzed the effects of capital market pressure (including Wahal & McConnell, 2000; Miles, 1993; Graham, et al., 2005; Marston & Craven, 1998; Demirag, 1995). However, such studies have merely enriched our nuanced understanding of how capital market pressure functions. They have claimed to contribute to the debate of short-termism, yet our understanding of capital market pressure and short-termism remain ambiguous. Many of these studies have only led to the indication whether capital markets may induce managerial myopia or not. Little research has qualitatively investigated the mechanisms for corporate control. Holland (1998), Roberts, et al. (2006) and Barker (1998) have contributed a great amount through their research based on a qualitative approach. Results suggest capital market pressure go far beyond formal corporate governance practices. Additionally, the level of capital market pressure exerted correlates with other variables such as stock price performance and institutional ownership (Gordon & Pound, 1993; Smith, 1996). So far the research suggest that the subject of corporate control is complex and consequently the literature could strongly benefit from further qualitative studies by digging deeper into the mechanisms for corporate control.

Previous research has developed certain areas of the literature surrounding capital market pressure, such as implicit pressure (Roberts, et al., 2006) or traditional corporate governance (Shleifer & Vishny, 1997). Yet, as far as I am aware nobody has contributed with a complete framework for analyzing and understanding capital market pressure. Barker (1998) developed a grounded theory of the market for information which has enriched our understanding of stock market information flows. However, his research does not address the mechanisms of capital market pressure but contributes with a theoretical framework which creates a fundament for analyzing such pressure. Ernst & Young (2014) provide a model of corporate governance by analyzing a couple of mechanisms for corporate control; the board and the stock price. Clearly, this model is incomplete. Additionally, they acknowledge that corporate governance practices varies between countries, thus it may not be feasible to generalize such model. I will attempt to extend our understanding of capital market pressure and contribute with a more extensive model. My research will build on previous studies of capital market pressure and on experience from Swedish corporations and corporate governance. I will gather data from senior management in the Swedish capital markets. Ultimately, my research will extend the theoretical framework for understanding corporate governance, what seems to be of great importance in the spirit of financialization.

3 Method

This study has used a qualitative research method to approach the research question. Nine interviews have been conducted with senior management and board representing nine unique listed firms.

3.1 Study design

This study has used a qualitative research method with inductive reasoning. In an inductive approach one cannot guarantee the conclusion but make a best prediction in an abductive sense. The qualitative method used is an interview study with senior management in Swedish listed firms. The goal of the interview study is to get rich and nuanced data. Management at different companies are likely to experience pressure to varying degrees (Marston & Craven, 1998). A corporation listed on Nasdaq OMX Stockholm Large Cap is probably more likely to be exposed to media, larger liquidity of the stock, more attention from institutional investors, more analyst coverage etc., compared to a smaller company listed on Small Cap or First North. Given a lot of factors potentially affecting the management perception of capital market pressure, a broader understanding could be reached through an interview study than a case study. Through an interview study, we can better understand the nature of capital market pressure and how it works in different settings. More data will be available, potentially leading to more nuanced results which is in line with the purpose of this qualitative study.

3.2 Data collection

3.2.1 Risks

Vaivio (2008, p. 74) recognizes the risk of the researcher influencing the empirical study by prior theoretical focus ”[…] no researchers mind is an empty canvas […]”. Conversely, some theoretical orientation is needed to be able to structure the collection of data and to distinguish what might be interesting for my study. The observed data is, to some extent, inevitably influenced by the interviewer and the respondents; respondent bias. Additionally, the questions and discussions that originally formed the data involved the stock market in various ways. The stock market is cyclical and dependent of the state of the whole economy. At the moment, the Swedish economy is considered to be booming and this has probably had a large impact on the empirical data in this study, constraining the external validity (Ryan, et al., 2002). The amount of pressure the participants experience is likely connected to the economic state (Holland, 1998; Gordon & Pound, 1993; Smith, 1996). Additionally, several of the respondents reflected on how their answers would likely have been different if times would have been "bad".

"Do you believe your institutional investors would have been on you more during bad times? - Yes, that is not unlikely. It it always much easier when there are good times. Look at Ericsson and H&M, they have had really rough times, they are probably going through an extremely stressful situation." (ID 9, SVP of IR, Large Cap, Consumer Durables & Apparel)

Another risk with the data is the respondents' willingness to disclose information. My own perception is managers at the larger companies were more careful and gave more 'safe' and standardized answers during the interview. An attempt to mitigate this behavior was by being very clear about their anonymity during the interview

Lastly, I have recognized the common 'windsurfer problem' (Vaivio, 2008) by questioning statements such as "we are not affected by capital markets" and acknowledging that respondents who speak out more freely may be those who are promoting a certain practice or have interest in it while sceptics may remain in the background.

3.2.2 Technique and procedure

Data was collected through nine telephone interviews with ten people representing nine unique companies. To avoid respondent bias, the interviews were held with different roles of senior management; four CFOs, two former CFOs, two CEOs, one SVP of Investor Relations and one board member. CFOs were my main target because of their financial responsibility. An overall effort was made to interview firms within different industry groups, based on the findings of Marston and Craven (1998); that market pressure differs between participants.

Each interview was thoroughly prepared by performing research on the company through their website, online newspapers, financial platforms etc., research were also performed on the interviewee through LinkedIn. In this way, I knew what questions could be of higher relevance and consequently smaller alterations were made in the interview formula. For instance, if a company were found to have a large institutional owner I would modify the interview questions regarding ownership structure. By looking up each interviewee on LinkedIn, I could get a grasp of the persons' background. An attempt was made to use appropriate language depending on the profile. In general, scientific jargon was avoided; instead of saying "capital market pressure" I would phrase it as "influences from the stock market". However, a very sophisticated interviewee would normally follow such jargon.

A semi-structured interview form was prepared, providing an agenda and structure but also elements of flexibility. The interview form was generated with regards to previous research, the research question and ethical aspects. See the interview form in the Appendix 8.1. The form consisted of a mix between leading and non leading and both specific and non specific questions. The first version was pilot-tested on fellow students and as a result several questions were revised. Also smaller alterations were performed continuously during the study. The alterations were executed when unexpected but valuable approaches were identified. Also, after having performed several interviews, my knowledge increased which lead to rewording and more effective interviews.

At the initial contact by e-mail and at the beginning of each interview, I presented myself, explained the independent nature of my study and their anonymity. During the interviews, the semi-structured interview form was effectively used. I lead the discussions, attempted to avoid irrelevant topics and used probing questions at interesting leads. At all times I avoided expressing my own opinions to prevent 'politization' (Vaivio, 2008). At the end of each interview, I summarized and clarified my perception of the interview to let the respondent correct any obvious misunderstandings. I also asked each respondent if there was anything that I had missed to ask about that could have been in my interest. In all cases, I had the possibility to follow up on the interviews if deemed necessary.

The interview study came to an end when I experienced a saturation in the answers, even after altering the interview form and considering that each interview was unique in regards to probing questions.

The interviews lasted between 30-70 minutes with a mean time of 44 minutes and all were held in Swedish, accordingly a careful translation has been performed by myself with the assistance of Google Translate. All interviews were audio recorded for analysis so I could focus on performing the interviews with proper technique.

3.3 Data analysis

The data analysis started following each interview as soon as it ended. I began the analysis by summarizing what had been said. Subsequently, I listened to the whole audio recording and created bullet points with topics of what was being said. Thereafter, I listened to the whole interview again, this time trying to go beyond what the respondent was actually saying, trying to catch up signals of jitters or defensiveness etc. For instance, I often found the respondents explicitly said “the stock price does not matter in the short run”, yet when they discussed other topics during the interview, the stock price could be mentioned and at that time it implicitly seemed to matter quite a lot.

Lastly, I listened to the recordings for the third time to catch citations which supported the topics. The whole process resulted in transcripts structured with bullet points around topics, in connection with sentiment analysis and quotes backing the topics. When the interview study was done, I started processing all of the transcripts. The transcripts were processed several times each to identify patterns and shared topics. The following section presents these finding.

4 Empirics

All respondents will remain completely anonymous throughout this paper based on their requests. The Global Industry Classification Standard (GICS) by Morgan Stanley Capital International has been used for classification of industries. The GICS structure consists of 24 industry groups. See interview list in Appendix 8.2.

4.1 Shareholders and the board

One of the major ways the shareholders could potentially pressure the companies is through large stock ownership. The largest shareholders of a company with the majority of the votes can control the board structure. Thus, the appointed board can be expected to represent the beliefs of that specific owner.

The board has regular meetings where top concerns are discussed; capital allocation, strategies, focus of business, investments decisions and other major decisions as appointment of the CEO. In that way, the shareholders have a great ability of controlling and exerting pressure on the management. Two of the respondents explicitly said how important it is to have an active board and a good relationship between the management and board. One of the respondents demonstrated the board as a catalyst; something positive for the company that filters bad decisions.

> *"We go to an offsite every year and devote two days for discussions with the board regarding the strategy of the company. The major shareholders are represented there and usually there are great discussions. I feel a large and strong support from our owners. It is important to have an active board." (ID 8, CFO, Large Cap, Telecommunication services)*

The relationship between the managers and the owners differ a lot between the respondents. One of the CEOs discuss how he has to manage the owners, make them like his ideas and plans for the company, because it happens he wants 'to do business' the board does not want to. Further he explains he manages them through phone calls and informal meetings, "*decisions are not always made in the board room*" (ID 4, CEO, Mid Cap, Real Estate). Another respondent states in contrast "*you cannot color your owners*" (ID 5, CFO, Mid Cap, Consumer Services).

Eight out of nine companies experience their owners to 'be in it' for the long term and have a positive attitude towards them. However, one respondent testifies that you can get in conflicts sometimes about what is best for the company and what is best for the owner "*they have to take both the ownership perspective and the company perspective*" (ID 5, CFO, Mid Cap, Consumer Services). The respondent suggest if the owner is very short-term and do not have any real commitment, you may receive opinions that are not respectable for the company.

4.2 Ownership structure

All of the respondents implied that the ownership structure significantly affects their ability to operate the business; the ownership structure lays the foundation for the company. Several different ownership structures were discussed during the interviews. Five out of nine interviewed companies were owned by families or entrepreneurs who originally started the business. In such structure, managing conflicting owners and pressure from the stock market was much less of a problem. In one of these companies, the nonexistence of pressure from the market pervades the whole business; they do not care about what analysts say and they do not care about the stock price, and the respondent further explains that it is because of their two owners who together hold more than 50 % of the company. A family structure allows the management to run the company with the least possible impact from the capital markets.

> *"We have two large and strong major owners. They always think long-term, they would never accept that we would decrease investments to deliver short-term results, that doesn't simply exist. It has been a strength for the company that we have had these two major owners that owns such large posts that we have always been able to work long-term. If we would have had a very scattered ownership and no real major owner of the company, the board would probably have been on us more regarding the stock price." (ID 3, Former CFO, Mid Cap, Consumer Services)*

An ownership structure with anchor investors is communicated to be a favorable structure by four of the respondents. An anchor investor can stabilize the decision-making in the board by its large ownership and long-term ownership horizon. And a very scattered ownership structure could be likely to inherent a large amount of conflicts of interest. However, one respondent mention scattered ownership as a suitable structure to some extent "*it keeps many eyes on the company and you are less dependent on what one owner thinks. There are more influences*" (ID 5, CFO, Mid Cap, Consumer Services). One of the respondents discuss about an extreme example of scattered ownership termed 'share of the people', and gives some examples like Telia, Ericsson and Fingerprint, which are largely owned by small investors which makes it difficult to effectively run the company.

> *"Without an anchor investor, the board and management becomes extremely lonely, they have no one to lean against. But if you have anchor investors that stays, then they contribute to stabilization of the decision-making." (ID 5, CFO, Mid Cap, Consumer Services)*

4.3 Financial reporting and performance measures

All of the respondents agree the financial reports are of great importance for the company and stock market participants. They contain a lot of information and are thus a valuable source. The reports are mentioned by three respondents as one of the major things about being a listed company. A lot of time and effort is put into construction of the reports. The management want to make sure they are relevant, consistent, standardized and easy to understand. They also want to make sure they are following all the rules regarding disclosure of information, one of the CFOs explicitly states "*it is very regulated and even punishable*" (ID 2, Former CFO, Mid Cap, Consumer Services).

> *"The financial reports are something I have put a lot of energy into […] I am meticulous about seeking feedback on the reports, I want the material to be relevant and consistent. To me the reports are very important, it should be analytically correct and easy to understand […] We try to standardize a lot, it makes it easy for the reader so they will know what to look for. It should be very predictable." (ID 5, CFO, Mid Cap, Consumer Services)*

The stock market participants tend to focus on different information under different circumstances. The majority of the respondents agree that there is a large focus on the financial key ratios such as earnings per share and various EBITDA multiples. However, leading indicators seem to be very important as well, particularly for growing companies. Two of the respondents experience a huge focus on keeping capital employed as low as possible. One of the companies experience that media is always against them, "*we have noticed that the media is always against us and always get stuck with the negative elements in the reports*" (ID 1, Board Member, Mid Cap, Consumer Services).

Quarterly reports can have a large impact on the business leading to potentially positive and negative effects. It is inevitable that the reports draw a lot of attention from the management. Three of the respondents describe how they fear delivering low profits that could potentially lead to a profit warning. One respondent mention how bad reports can make the board rethink, "*our CEO was resigned now for instance, so of course there are actions taken all the time if you don't perform on expectations, that is how it is*" (ID 6, CFO, Large Cap, Software & Services). However, three of the companies within retail agree there are large positive benefits from the quarterly reports, because the reports create energy, drive and creativity.

> *"We are driven by the quarterly reports, but I think that is positive. You should not reduce investments to create profit, then you are on the wrong path. But having a drive toward generating profit on a quarterly basis, having a goal to improve without sacrificing the long term plans, that creates energy." (ID 3, Former CFO, Mid Cap, Consumer Services)*

A large majority of the respondents' state that quarterly reports does not compete with the focus of the long term. However, three of the respondents mention clear disturbances. First, the reports take a lot of time and are not value creating activities. Secondly, two respondents mention that it is very important for the management to find the right balance between short- and long-term activities.

> *"You have to find that balance, I mean you have to be able to build the business from a long-term perspective while you continuously deliver every quarter." (ID 5, CFO, Mid Cap, Consumer Services)*

One respondent suggests that the importance of quarterly reports within a company heavily depends on the owners. It is important with owners that enables the management to focus on the long-term value creation.

4.4 Quarterly driven economy

Six respondents considered the stock market participants excessively focused on the short-term performance. The whole economy is quite driven on a quarterly basis; the respondents believe all participants are influenced to some extent.

> *"Is the stock market short-term? - Yes, quite much I would say. The market is more short term than I would wish. It would be wrong to say that it doesn't affect us, I often think, 'what will they say about this?'" (ID 4, CEO, Mid Cap, Real Estate)*

Since quarters are quite short cycles, it requires managers to balance the needs of short- and long-term investors. All of the respondents expressed they are able to do this. There is a large focus on optimizing every quarter, conversely what is expressed to be truly important is to drive the stock price in the long run. One of the respondents think long-term by building a buffer now when the economy is booming. Several of the respondents acknowledge they could drive the stock price today, but it would hit them like a boomerang the next quarters. However, one respondent admitted that sometimes you may not have a choice, like times during crisis "*then you have to make as smart short term decisions as possible*" (ID 4, CEO, Mid Cap, Real Estate).

> *"When the stock crashes and you get the knife to your throat, you make short term decisions because you do everything to survive. But if you are not in that situation, you run the company with the long term strategy in mind, then it is almost impossible to fail […] I would like to claim this; all short term decisions which are made under pressure are wrong. It is like sub optimizing the business in a weird way." (ID 4, CEO, Mid Cap, Real Estate)*

One of the respondents believe some industries are more vulnerable to short-term pressure, especially cyclical and local business, and it is explained like you could reduce the vulnerability by diversification of the business. Another respondent blame the short-term focus partly on high frequency trading, which constitutes a large amount of total trades in the financial markets "*these robots don't care about better times 3 years ahead, to these robots it is only now that matters*" (ID 2, Former CFO, Mid Cap, Consumer Services).

Stock options are discussed by two respondents. One of them believe the options do not influence their behavior. The other respondent think they have strong positive benefits for the company, at least when they are on a three-year plan and required some initial investment.

4.5 Analysts

The respondents agree about analysts having an important role, they enrich the flow of information in the market. Analysts are also highly respected by the majority of the interviewed managers and perceived as intelligent people, even though they find it frustrating when the analysts write bad things about the companies. The companies value their relationships to the analyst and put a lot of energy and work into building them. The analysts are furthermore perceived to have a lot of power through their consensus and recommendations, which creates fundaments for the perceptions of other stock market participants.

The number of analysts following a company varies. The senior management cannot decide themselves on how many analysts are to follow the company, but generally, the larger the company the more analysts tend to follow. Two of the respondents explain analysts decide themselves on which companies to follow. Thus, if they find the company an interesting case they will more likely follow. The amount of analysts has declined lately according to three of the respondents. One of them explained this is due to the industry going through a change.

> *"We try to have a close dialogue with the analysts and a good relationship, we try to be proactive. You are open, discuss things that works well and challenges […] but an analyst never likes surprises. The better you can explain results and why things went well and not as good and don't drag things under the carpet, it has a lot to do with credibility." (ID 8, CFO, Large Cap, Telecommunication Services)*

Six out of nine respondents phrased "analysts don't like surprises". And if you have to deliver a surprise, you need to be ready to explain it. If promises are made, you have to deliver on these, and even if you deliver ahead of plan, you need to be able to explain why. Analysts hate risks. It is very important to have clear communication and to build credibility.

Analysts ability to influence the management seem controversial. Two of the respondents mention a kind of indirect pressure from the analysts, they restrain the management from considering some actions. Another two respondents do not think the analysts affect them at all. The management have to follow their strategy and deliver according to it; the analysts might not approve but that does not control their thinking, "*some have us on buy, some on hold and some on sell, but that's what it is, it's natural*" (ID 8, CFO, Large Cap, Telecommunication Services).

"What consequences do you experience if you go against what the market thinks? - You don't. You have to consider the public opinion and the consensus." (ID 2, Former CFO, Mid Cap, Consumer Services)

There are also mixed beliefs about whether analysts are short-term focused or not. However, the group of respondents who think the analysts are short-term do not actually blame them for their short-termism. The management acknowledges that the analysts are strongly affected by their clients who push them to deliver every quarter, "*they breathe short-term for their clients*" (ID 9, SVP of IR, Large Cap, Consumer Durables & Apparel).

Management seem to have the ability to control the analysts to some extent. According to two of the respondents, they can push and manipulate the analysts to skip on delivering a recommendation one quarter. They basically do this by communicating with the analysts, make phone calls and book informal meetings. However, they also agree it is not possible to actually skew the recommendations. In the end, the companies do not have a lot of power over the analysts.

"You have to give them [analysts] time, when they are stressed, 'Bengt Bengtsson, it is better if we take a lunch and talk about this thoroughly before you release anything, than just talking on the phone, it is better if you don't release for this quarter'. And maybe they say 'yeah you are right, I won't send anything this quarter'." (ID 9, SVP of IR, Large Cap, Consumer Durables & Apparel)

Consensus is a kind of synopsis about what the analysts think about a company. The company in question can chose whether to stand behind the consensus or not. If there are a very few number of analysts contributing to the consensus, a company might consider that there is not enough substance behind the consensus and thus will not support it.

Two stereotypes of analysts are communicated by one of the respondents and another two respondents agree on those stereotype figures. One of the stereotypes is very often more junior and tend to be narrow-minded and are very stuck in their excel model; they do not understand how business actually works in reality. The second type is generally more senior, they grasp the industry and recognize subtle signals. The junior type is more difficult to deal with. Two respondents sense professional honor amongst the analysts; they get stuck with their beliefs for too long. One of the companies had the same analyst who put a sell recommendation on the company for seven years, and during these seven years the stock price doubled numerous times.

4.6 Stock price

None of the respondents described the short term stock price of importance. The stock price fluctuates daily, but that is communicated to be quite irrelevant. Yet, it seemed to disturb several of the respondents to some extent. Four of the respondents reflected a lot about how certain actions and events possibly influenced the stock price, such as investments, provisions, organic growth and acquisitions. One of them discussed even more about the stock price, how having a large "free float" or liquidity benefits the stock price. The liquidity of the stock can be distinguished from the real underlying business value creation. Another respondent mentioned that "*mentally, the stock price influences us a little, but we do not let it affect the business*" (ID 9, SVP of IR, Large Cap, Consumer Durables & Apparel).

> *"Is the stock price important? - Of course I look at the stock price, but it is the underlying performance that is more important to me than the daily stock price [...] my job is to deliver shareholder value so if I wouldn't care [about the stock price] I wouldn't be doing my job. But that is why I think about it in the long term, because it is in the long term we can build it." (ID 6, CFO, Large Cap, Software & Services)*

Respondents made a clear distinction between the short- and long-term stock price. Unlike in the short-term, the long-term stock price was very important, all respondents agreed on this. The reason to why the long-term stock price was important seemed to be because of the relation between long-term stock price and the underlying business performance and shareholder value creation. However, two of the respondents was experience their business thriving yet their share prices deteriorating. One of them explicitly conveyed frustration regarding this, "*we want to get paid for the work we do, so it is frustrating if we think we deliver long-term value but we don't see it in the stock price*" (ID 10, CFO, Mid Cap, Software & Services).

The share price was identified to have several possible ways of impacting the business. If the stock price become volatile, it may generate nervousness among the shareholders, which in turn could lead to increased attention to the management. Larger shareholders may contact the management seeking explanations. One respondent identified an implicit pressure that correlates with the market value of the company. The same respondent also argued that a high valuation affects the business by giving degrees of freedom in negotiations. When they acquire companies, a high valuation puts them in a good seat during the negotiations. It can also influence whether the transaction will be financed by cash or equity.

> *"There is some kind of implicit pressure that slowly but surely increases with the value of the company, and it shows in some way but very implicitly, not explicitly." (ID 10, CFO, Mid Cap, Software & Services)*

4.7 Strategies

Six out of nine respondents communicated that they wouldn't had changed their strategy if they were non-listed. Conversely, two of the respondents explained they do not even consider potential investments they know larger institutional investors would be against, "*you don't swear in the church*" (ID 2, Former CFO, Mid Cap, Consumer Services). If a large institutional investor is unhappy, they could sell of immediately and that would certainly impact the stock price.

> *"The long term strategy is affected in a way that, if you and I run a non-listed company we can choose to take on larger risks; enter a market that is not very appropriate but indeed very profitable. If we are listed, you take the public opinion in consideration or what you call consensus from the analysts. If you are a listed company, it gives you less space to try new things." (ID 1, Board Member, Mid Cap, Consumer Services)*

Two of the respondents described their intense focus on keeping capital employed low. In one of the companies, it infuses the whole organization, even performance linked pay was based on capital employed. When the company was to perform an acquisition the deal could be called off due to too much assets and PP&E on the targets balance sheet. Good deals with suppliers regarding merchandise could also be called off if they did not provide enough days of credit to be able to turn over the merchandise before the next quarter, even if the supplier offered them an extra discount. Yet, the respondent believed the positive benefits outweigh these smaller issues "*having a trimmed balance sheet and focusing on not binding capital is basic business economics*" (ID 7, CEO, Mid Cap, Consumer Services).

4.8 Communication with the market

The communication with the capital market participants can be complex, and all respondents agree that the communication is very important. The main communication channels are the financial reports, meeting with analysts and shareholders and the capital market days. Even though the communication is expressed to be very important and something that the companies take very seriously; two of the respondents inform that the communication is often very limited. 'Quite periods' can also be very problematic because it limits managers' communication with the market. It is of mutual interest to make sure the latest information is in the market. A good relationship to the stock market facilitates communication.

> *"Everybody understands that a plan is a plan and everything can't always go as planned, so it is very important to be able to communicate with the [capital] market. But if something happens and you don't know about it, that is dangerous. It is very important to have the trust of the market." (ID 6, CFO, Large Cap, Software & Services)*

The company has to be able to clearly articulate their business model which can be difficult and a continuous process. Sometimes misunderstandings occur and investors or other market participants focus on the wrong things. One respondent mention how they continuously have to remind the analysts about how specific events impacts their business in order for the analyst to be able to make the correct valuation. Another respondent explains how the analysts sometimes do not understand their accounting principles.

> *"If some analysts don't like it, then you have to discuss with them why they don't, and then maybe you have to explain stuff in a different way. Our business is very complex, a lot of markets etc. It is important to make the analysts understand how our company creates value." (ID 8, CFO, Large Cap, Telecommunication Services)*

5 Analysis

In this section I will interpret the data gathered through the empirical study. In qualitative research, the role of interpretation is crucial (Vaivio, 2008). I will try to make theoretical sense of what was found important and credible in the empirical study together with previous research in Section 2. My goal is to understand how capital market pressure can influence the management. I have contacted two of the respondents again for clarification and reassurance.

Capital market pressure is a tool for corporate control and I will distinguish between formal and informal capital market pressure. It is important to note channels or sources of capital market pressure may have characteristics as both formal and informal to some extent. The final denotation was determined based on their major characteristic.

5.1 Formal capital market pressure

Formal capital market pressure is explicit and well-defined actions exercised by shareholders to align the interest of senior management with their own, such as exercising voting rights.

5.1.1 Ownership structure

The most fundamental aspect of capital market pressure originates from the shareholders of the company. A large shareholder has substantial voting rights and can in that way largely influence and pressure the managers. The ownership structure makes the foundation on which capital market pressure builds in the following ways. First, it was found in the empirical study that the ownership could ultimately determine whether the company is exposed to capital market pressure or not, by remaining non-listed or the original owner keeping a major stake in the company. Secondly, the ownership structure is not a binary variable (either ‘good’ or ‘bad’ ownership), it is a continuous variable which significantly determines the total possible impact capital market pressure may have on a company. In previous research the capital market pressure has been found to be positively correlated with the level of institutional ownership

(Smith, 1996) and negatively correlated with insider ownership (Gordon & Pound, 1993). Additionally, the empirical study found that an 'unstable' ownership structure; ownership consisting of large minority shareholders, is likely to be more vulnerable to capital market pressure.

> *"[…] it has been a strength for the company that we have had these two major owners […] If we would have had a very scattered ownership and no real major owner of the company, the board would probably have been on us more regarding the stock price." (ID 3, Former CFO, Mid Cap, Consumer Services)*

Conversely, previous research suggests that in ownership structures with large minority shareholders, they need to make alliances and matters are more complicated. Therefore, the power of managers tend to be larger (Shleifer & Vishny, 1997). These findings might seem contradictory, yet they are not. In a scattered ownership management may perceive greater amounts of pressure. Smaller increases in share price volatility quickly leads to interrogation by shareholders. Still, the power of managers can be larger and their ability to manage owners can be greater; what managers say might have a larger impact. In that way they could receive more pressure but also better fend against it.

Thirdly, significant ownership grants access to the board which is a formal and effective way of exerting pressure (Shleifer & Vishny, 1997; Shleifer & Vishny, 1986). A large shareholder with at least 51% ownership have a general interest in profit maximization and enough control over the assets of the firm to have their interests respected. The pressure exerted through voting control is very visible and it is also expected by the senior management; if a company performs poorly the board is often expected to take actions. The investors are able, through voting rights, to engage in capital allocation decisions, appointment and dismissal of CEO, set remuneration schemes, strategy formulation, focus of business, investment decisions and certain decisions of high importance.

5.2 Informal capital market pressure

Informal capital market pressure is implicit and less-defined actions exercised by various capital market participants which ultimately influences the behavior of senior managers. Management perceive informal pressure as subtle and implicit. It may be thought of as actions that indirectly influence senior management behavior. The empirical study shows that informal capital market pressure is identified to exist through several channels; ownership structure, stock price, financial reports, analysts and the media. The ability of management to cope with the pressure from capital markets varies depending on through which channel such pressure is derived.

5.2.1 Ownership structure

The shareholders are also a source of informal pressure. The informal pressure is subtle and it is not exerted explicitly or occasionally; but it actively influences the behavior of senior management. This type of informal pressure is reinforced through jawboning (Shleifer & Vishny, 1986) or investor meetings where investors can discipline the managers (Roberts, et al., 2006). Additionally, the investors have the ability to "pre-condition" the senior management (Holland, 1998) and in that way the interests of senior managers are always aligned with the interests of the investors. The majority of the respondents in the empirical study explicitly claimed their interests did not conflict with their owners; hence at first glance one might disregard from capital market pressure. Such claims are somewhat in line with previous research which has found outside blockholder-directors to be on average strategically aligned with management (Gordon & Pound, 1993). Yet, I suggest these claims hold large respondent bias because the managers have likely been pre-conditioned by their investors.

"[…] the discipline is realized in anticipation within the self, or at least rationalized in a defensive way that presents the self as already wanting what the investor wants." (Roberts, et al., 2006, p. 289)

Nevertheless, one former CFO and board member clearly stated they would not even consider potential investments which they knew larger institutional investors would be against "*you don't swear in the church*" (ID 2, Former CFO, Mid Cap, Consumer Services).

Roberts, et al. (2006) present how the investor meetings are a way for investors to remind managers that they are being watched over. From the perspective of senior management, they present the meetings as an opportunity to change the picture investors have about the company. In similarity, the empirical study present how a manager manipulates his investors through phone calls and informal meetings to make them like his ideas; "*decisions are not always made in the board room*" (ID 4, CEO, Mid Cap, Real Estate). Conclusively, it seems that managers have the ability to handle pressure from their investors.

5.2.2 Financial reports

Financial reports are a channel of informal capital market pressure because they indirectly influence management behavior. The actual reporting process itself inevitably directly influence management behavior, however in this analysis I focus on the influence on management behavior outside the reporting process itself. The reporting can be seen as a disciplinary process which capital markets can leverage to align their interest. First, the empirical study found management to spend a lot of time and effort into making sure the reports are appreciated by the capital markets. Thus, the reporting procedure requires managers to process investors preferences and subsequently to some extent internalize them. Secondly, the reporting process remind the senior management that they are being watched. Roberts, et al. (2006) present the investor meetings as a ritual of reminder, I suggest the reports should be seen as such ritual as well.

Financial reports are released most commonly on a quarterly basis in Sweden, so they also significantly contribute to the 'quarterly driven economy' described in the data. The empirical study very clearly demonstrates the level of importance senior management draws to the financial reports; as well as the amount of energy and focus. The process of creating financial reports is not a value creating process for the underlying business itself; and can thus be seen as a conflicting interest. The opportunity cost is the time and energy management could have spent on creating value in their business.

"It takes a lot of time, A LOT of time. But it can be fun, however just because it is fun doesn't mean it is value creating" (ID 10, CFO, Mid Cap, Software & Services)

Financial reports are commonly associated with financial measures such as EPS, EBITDA etc. The empirical study found that in most cases the stock market is indeed focused on financial measures (previous research has claimed an excessive focus, including; Kraus & Lind, 2010; Kallifatides & Belfrage, 2018; Clarke, 2014; Demirag, 1995) and it also showed management are very aware of what is liked and disliked by the market. The knowledge of knowing what the market wants is very likely a considerable source of subtle pressure. Two of the respondents described an intense focus on keeping their balance sheets slim because they knew that is what the capital market rewards in terms of stock price and valuation. The pressure to keeping capital employed low resulted in several effects. First, it shaped the performance management systems. This is in line with what Kraus & Lind (2010) found; capital market pressure ultimately alters internal work processes. Secondly, it reformed their acquisition strategies. Even acquisitions that would be considered as good deals would sometimes be called off because the target company having too much capital employed. Thirdly, the operations were affected in a way that if current assets could not be turned over before the next financial report, these current assets would not be purchased even if a heavy discount was offered.

Yet, the reports are also a way for companies to cope with market pressure. Holland (1998) describes how investor meetings are a way for senior management to manipulate the investors picture of the company. The empirical study suggests financial reports achieve a similar purpose. Ultimately the senior management decide on how they want to present the company and what to include in the report, assuming regulations are followed. In that sense it is possible to manipulate the picture of the company. Earnings management could be thought of as an extreme example of how company manages pressure.

5.2.3 Analysts

Marston and Craven (1998) found that senior management does not perceive all capital market participants as equally short-termistic. In similarity, the empirical study suggest there are two stereotypes of analysts and these were very likely to ask different kind of questions (Barker (1998) also distinquished between two types of analysts, yet distinguished in a different way); consequently exert different amount of pressure. The more junior stereotype was communicated to be more difficult to deal with and not as respected. Analysts level of competence varies individually and ultimately it affects the valuation of the company and the recommendation analysts make. Additionally, the empirical study found that analysts ask questions to develop their models and to make as precise valuations as possible. Barker (1998) found analysts consider direct contact with the senior management as the most valuable source of information, largely due their ability to ask questions in such situation. From the perspective of senior management, the questions analysts demand answers to are a way of interpreting what analysts value.

Analysts are a channel of informal pressure. The pressure is derived from formal analyst meetings when they can ask questions but also through voluntary informal contact and meetings. The pressure is legitimized by analysts ability to deliver recommendations or valuation guidelines to the market. The analysts ability to exert pressure heavily depends on how important management perceive the analysts. Indeed, the empirical study found the majority of managers value their analysts highly.

Further, the data provided strong support for senior managers ability to influence analysts and in that way cope with such pressure. Primarily, analysts try to be rational when valuating the company based on the information they have at hand, but clearly fails at this. The empirical study show how senior management occasionally have to remind analysts about certain events which ultimately have an effect on their valuation. Secondly, the business strategy can be difficult to decode for analysts and it is crucial how the company communicates it because it may have a large impact on the valuation by the analyst. The importance of how managers articulate their business strategy was also found by Roberts, et al. (2006) and Holland (1998). Demirag (1995) found analysts often lack the necessary skills to value long-term technology investments.

Thirdly, the empirical study suggests analysts can be manipulated to some extent regarding whether to release their recommendation or not.

5.2.4 Stock price

The empirical study suggests short-term stock price fluctuations are not of considerable importance for senior management. Still, the managers thought a lot about the stock price, in most cases on a daily basis which supports previous research (Barker, 1998). Managers thought about how it changed and why it changed. It is safe to say; the stock price is very frequently in the minds of the senior management, even though they express it to be of less importance. Several of the respondents expressed concern regarding the risk of having to deliver a profit warning and the stock price impact of such warning. Holland (1998) found financial institutions used small but symbolic stock sales to increase the pressure on their portfolio companies. In that sense, the stock price seems to be a considerable channel of informal pressure. Additionally, one of the respondents described how the stock price directly had an impact on the negotiations with potential target companies during acquisitions; the stock price and the valuation could ultimately determine whether the acquisition would be financed by cash or equity.

It was found that; if the stock price became volatile, senior management could experience increased attention from the board. Thus, when volatility increases, informal pressure increases from the investors through questioning or potentially formal pressure through intervention. Smith (1996) discovered stock price performance to be inversely correlated with the probability of being targeted for shareholder activism. Holland (1998) found the amount and intensity of capital market pressure is correlated with the well-being of the company. During better times, influence was limited to questioning on matters like strategy from institutional investors; ‘weak’ pressure. During times of struggle, more explicit methods were used, leading to ‘stronger’ pressure. My finding both support and nuances existing literature; not only does there seem to be an inverse relationship between performance and shareholder activism, but also a relationship between volatility and informal pressure.

The capital market pressure perceived through the stock price was heavily dependent on the ownership structure. The empirical study clearly present how a large, stable and long-term shareholder could allow the senior management to neglect short-term stock price fluctuations. However, if management were faced with such pressure the ability of management to deal with it were low. Management were identified to be able to increase the short-term stock price through various ways, but such actions would hit back in the following quarters.

5.2.5 Media

In previous research by Holland (1998), media has been found to operate as a device for exerting pressure on senior management. Public pressure in form of media leaks were used by financial institutions to intensify the pressure on senior management in their portfolio companies, which strongly suggest that media is a channel of informal capital market pressure. Similarly, some evidence was found in the empirical study. Two of the respondents expressed concern regarding media and the public opinion. They gave indications of how they were influenced by it; through considering what media would say regarding specific decisions the management would take. Holland (1998) also found financial institutions increased awareness regarding certain issues through the media. In that way, a shareholder can gather support amongst other less informed shareholders. Media is thus not only itself a channel of informal pressure but also a very effective device for increasing pressure from other channels.

> *”The media can be useful in getting a point of view across to other shareholders, maybe small shareholders and institutions who may not be aware of what is happening, and getting a groundswell of opinion to put more pressure on management.” (from Hosking, 1994, p. 8, Collected from Holland, 1998, p. 258)*

In similarity to the financial reports, media is also a medium for communication, yet a less formal kind. The empirical study found the ability to communicate with the market very important; if something unexpected happens you have to be able to explain it. Depending on how well management are able to communicate around such things, they can consequently manage pressure from media to varying degrees.

6 Conclusions

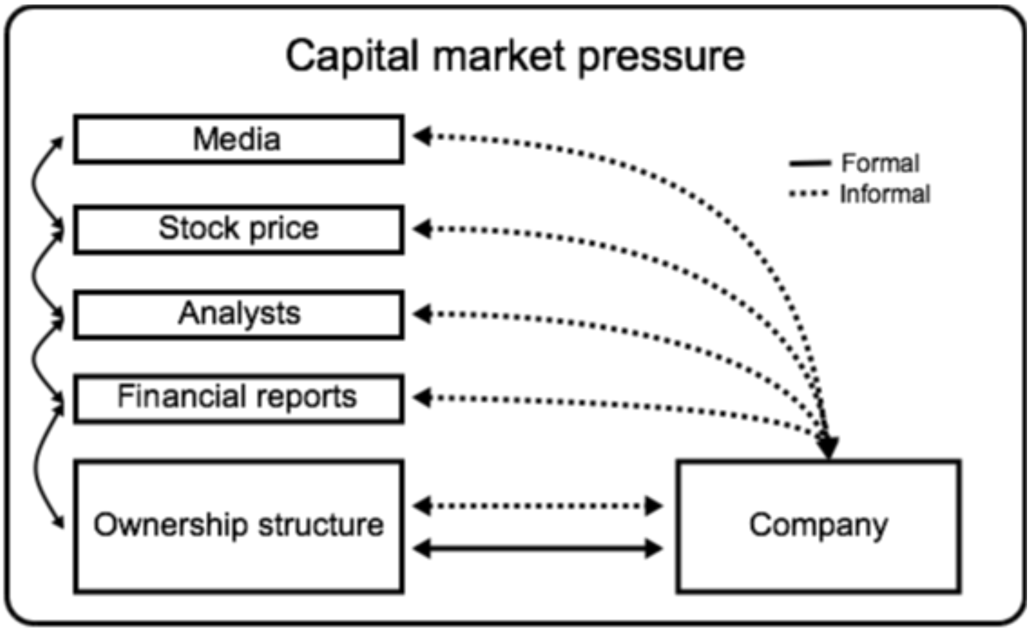
6.1 Summary

Capital market pressure is a tool for corporate control which investors use to make sure managers are pursuing what is in their interest. Capital market pressure have increased in the spirit of financialization and have been claimed to cause short-termism and managerial myopia. In this study, nine interviews have been held with senior management from Mid Cap and Large cap Nasdaq OMX Stockholm listed companies in Sweden to identify how managers may perceive capital market pressure.

The analysis revealed senior management may experience capital market pressure in two distinguished ways; formal and informal. The formal pressure is exerted through the ownership structure. Such pressure is expressed through voting and board representation, which ultimately take shape of actions such as appointment and dismissal of the CEO and setting the remuneration schemes. The informal pressure is implicit and indirectly influence the behavior of senior managers. Informal pressure can be expressed through various channels; the owners, financial reports, analysts, stock price and media. Depending on which channel the pressure is perceived through, managers have the ability to deal with it through different techniques and to different degrees. Additionally, the various channels of pressure interrelate with each other; ownership structure can ultimately determine if the company is exposed to other channels of pressure from capital markets or not.

6.2 Contributions and discussion

The empirical study and analysis have given strong support for previous research, but more importantly extended the existing theoretical framework by addressing what previous research has left ambiguous. The model below summarizes the analysis and the contributions of this study.



This model shed light on the nature of capital market pressure. To begin with, previous research has presented various ways of how managers may perceive capital market pressure which have resulted in a loose emballage of tools for corporate control. Through my analysis, I have distinguished between two types of capital market pressure and addressed them as formal and informal. I acknowledge the distinction between formal and informal can be difficult at times, yet does such distinction enable us to start thinking about capital market pressure in a more systematized manner. The analysis identified several channels; the ownership structure was identified as a formal and informal channel of pressure and the financial reports, analysts, stock price and media were identified as informal channels. These have been analyzed and explained in depth in Section 5. However, I do not claim the channels addressed in my study are exhaustive, indeed I advocate further research to explore additional potential variables.

Previous research has presented several relationships between the various variables. First, stock price performance has been found to be inversely correlated with the probability of being targeted for shareholder activism (Gordon & Pound, 1993; Smith, 1996).

Secondly, when the company is performing well, the pressure is limited to informed questioning on matters like strategy (Holland, 1998). During times of struggle, more explicit methods tend to be used, such as dismissal of the CEO. Thirdly, firm size and level of institutional ownership have been found to be positively correlated with shareholder activism (Smith, 1996). My study support these findings to a large extent, although more importantly my study contributes with more nuances. Not only is there an inverse relationship between performance and shareholder activism; my analysis suggest a positive correlation between share price volatility and informal pressure.

Further, my study strongly contributes to the literature by addressing the controllability of capital market pressure through various channels where it may be perceived. When managers are faced with pressure from capital markets, they were found to be able to deal with such pressure to differing extents; the controllability of capital market pressure. The level of controllability depends greatly on the channel through which the pressure is perceived. Several techniques to manage pressure were identified; managers manipulate their investors through informal meetings and consequently make them like their ideas; senior management ultimately have the control over their financial reports and are therefore able to decide what to present and redirect focus; managers manipulate analysts and in that way impact their valuations or prevent them from releasing a recommendation; senior management can boost short-term stock price yet it is likely to give consequences following quarters; managers can communicate with the public through media. The controllability of capital market pressure is heavily dependent on the ownership structure; the ideal ownership structure in terms of capital market pressure is a structure which enables management to balance short- and long-term needs of their business and thus ignoring capital market pressure. In the empirical study, these structures tended to exist of family ownership or the original entrepreneur.

As far as I am aware, previous research has not addressed the controllability in terms of capital market pressure very much, presumably because no framework has established the structure for such analysis. Roberts, et al. (2006) presented how managers see investor meetings as an opportunity to influence their picture of the company; my study show support for such behavior as well. Yet, in general previous research has presented managers as somewhat powerless and in the hands of capital market pressure. Conversely, my research suggest managers have the ability to cope with the pressure depending on the ownership structure and which channel the pressure is perceived through. These findings contribute with new perspectives to the debate of capital market pressure and short-termism and has implications for further research.

6.3 Limitations and future research

The aim of this qualitative study was to understand and describe capital market pressure; no attempt has been made to quantify the data. My research has to some extent systematized our knowledge of capital market pressure by distinguishing between formal and informal pressure and addressing various channels of pressure. There were several identified channels of informal capital market pressure, however the relative importance or impact of these channels remain uncertain because of the research method. Further research of the relationships between the channels would develop our understanding of the dynamics of capital market pressure.

The Corporate Governance literature has traditionally paid a lot of value to the hard wired controls such as appointment and dismissal of the CEO. However, this may be disproportionately to what is actually used in practice. Holland (1998) found institutional investors seem to perform little explicit corporate governance and rely more on implicit pressures. Based on the model developed in this study, further quantitative research could attempt to measure the importance of formal and informal corporate governance. Furthermore, such research may also attempt to measure the effectiveness of various types of pressure and analyze in what settings certain kind of channels tend to be used.

The empirical research is built on nine telephone interviews which limits the reliability of the data. Furthermore, in qualitative research the participants are likely to influence the data, thus respondent bias also limits the reliability.

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8 Appendix

8.1 Interview form

Opening question

- Tell me a little about your background

Ownership

- How is your company affected by being listed?
- How does the ownership structure look in the company and how are you affected by it?
- Are you able and allowed to pursue the strategy you like?
- Does it ever happen that the owners question the decisions you make?
- Do you think the owners tend to be short-term or long-term?

Capital markets

- How often do you have contact with the analysts and what do you think about that part of your job?
- Can it be difficult to communicate your strategy to the analysts?
    - Do they always understand you?
- In what ways can a good relationship to the analysts be positive?
- Do you experience any stereotypes of analysts?
- Does it ever occur that you bring forward a number of possible decisions and test them with the analysts to see what they think?
- Do you get to "see" the consensus before it is released to the market?
- What do you experience of most importance for the analysts?
- Does it require a lot of work to create the financial reports?
- Do you experience a large focus on the quarterly reports?
    - Do you see any effects of this quarterly focus?
- Do you know what your stock price is at right now?
- Is the stock price important to you and does it influence you?

Goals and strategies

- Do you have any explicit short-term and long-term goals?

- Who decides on these goals?

- How do you work to pursue your goals?
- Have there at anytime been hard to reach those goals and how did you act then?
- Do the long-term goals and the short-term goals require different actions?
- Does the long-term part of the business compete with the requirement to deliver good results on a quarterly basis?
- Do you consider the market short-term or long-term?
  - How does that influence you?

Ending question

- Considering what we have discussed, are there anything that you think I have forgot to ask about?

8.2 Interview list

Identity	Title	List	GICS (industry group)	
1	Board member	Mid Cap	2530	Consumer Services
2	Former CFO	Mid Cap	2530	Consumer Services
3	Former CFO	Mid Cap	2530	Consumer Services
4	CEO	Mid Cap	6010	Real Estate
5	CFO	Mid Cap	2530	Consumer Services
6	CFO	Large Cap	4510	Software & Services
7	CEO	Mid Cap	2530	Consumer Services
8	CFO	Large Cap	5010	Telecommunication Services
9	SVP of IR	Large Cap	2520	Consumer Durables & Apparel
10	CFO	Mid Cap	4510	Software & Services