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The German cooperative banking group as a strategic network: function and performance

von Rolf Greve

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Westfälische Wilhelms-Universität Münster
Institut für Genossenschaftswesen
Am Stadtgraben 9 ▪ D-48143 Münster
Tel. ++49 (0) 2 51/83-2 28 01 ▪ Fax ++49 (0) 2 51/83-2 28 04
info@ifg-muenster.de ▪ www.ifg-muenster.de

Table of contents

Table of figures

1 Introduction

"Institutions matter"[1] is one of the central statements of Institutional Economics. Institutions are the rules of the game in a society, they structure incentives in human exchange. Hybrid structures that lie between an arm's length transaction (market) and the pooling of resources under common command (hierarchy) are of particular interest in recent years. Due to changing general conditions the boundaries of firms are fading.[2] Networks are emerging by outsourcing and cooperation that combine elements of markets and hierarchies.

One of the oldest economic networks is the cooperative banking group in Germany. Already a few years after the foundation of the first credit cooperatives in the 19th century, they established regional central banks.[3] Companies with specialized financial services followed. The strength of the Cooperative Banking Group derives from combining the advantages of small local banks with those of a large group.[4]

Due to their success in Germany, credit cooperatives were created in several other countries around the world, some of them working together in networks, others staying autonomous.[5] Especially in developing countries credit cooperatives were established to organize financial markets for small and medium sized enterprises (microfinance). Studies have shown that access to credits for small and medium sized enterprises is one of the keys to alleviate poverty. Credit cooperatives are able to play the role of microfinance intermediaries in developing countries. The economic situation of Germany during the 19th century, when credit cooperatives were created to provide small and medium sized enterprises with credits, is comparable to that in several developing countries nowadays.[6] The problems of providing access to financial resources to farmers, merchants and craftsmen hundred years ago in Germany and today in development countries are similar. Therefore, the operation of the cooperative banking system in Germany is an interesting case study for several developing countries around the world.

In recent years the German cooperative banking group adapted its governance structure to changing general economic, legal, technical, and social conditions. By implementing a new, joint strategy, the German cooperative banking system is on its way to become a more "strategic" network. This paper will analyze the operation of the German cooperative banking group and its evolution towards a strategic network. It focuses on the governance

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1 North (1987), p. 419.
2 See Picot/Reichwald/Wigand (2001).
3 See Faust (1977), p. 226 f.
4 Cf. Bonus/Schmidt (1990), p. 192.
5 See Fischer (2000), MacPherson (1998).
6 See Akerlof (1970), pp. 489-499 who describes the function of local moneylenders in modern day rural India.

structures of cooperative banks and their networks. The German case can be compared to most of the national cooperative financial networks in Europe and to others throughout the world. The evolution of the German cooperative financial network is a case study of a highly developed community-oriented financial intermediary.

2 Institutions matter – The trend towards cooperation

The importance of cooperation is increasing continuously. Every day brings news about cooperation between individuals and companies. Cooperation has different faces and names: joint ventures, strategic alliances, virtual enterprises, networks, and franchising are only some of them. In 2001, the management consultancy ARTHUR D. LITTLE surveyed more than 1,200 companies in Europe, the US, and Asia from all major industries and markets to explore their perspectives with respect to cooperation. The study uses the term "partnering" instead of cooperation and defines it as "the linkage of value-added activities of at least two companies with corresponding strategic objectives and no major capital links"[7]. The survey shows that cooperation is of increasing importance to all companies and that the vast majority of executives recognize the business value of partnerships.[8]

Changes of the general economic setting are responsible for the increasing importance of hybrid – as this form of economic cooperation is often called – institutions in the economy.[9] The globalization makes economies international, formerly separated markets are growing together. At the same time, the delay for the development of new products and services is becoming shorter. Therefore many entrepreneurs are looking for potential partners in order to use economies of scale and scope, reduce risks and get access to know-how and other resources. Further, the progress in the information and communication technology revolutionizes the economy. Technologies like the world wide web or intranets and applications like email or video conferences make the division of labor easier than ever.

Finally, the trend towards cooperation can be explained by a changing importance of knowledge in recent years.[10] JENSEN/MECKLING distinguish between "general" and "specific" knowledge.[11] Knowledge is "specific" when it is costly to transfer among agents whereas "general" knowledge is inexpensive to transmit. In the 19th century, the key factors of success of industrial companies were the standardization of processes and the use of economies of scale. The necessary knowledge was "general"; it could be transferred easily. The establishment of big firms was the consequence. Today, production is more sophisticated and the essential knowledge is more "specific" than ever. Specific knowledge is based upon training and experience; it is unsuitable for translation into written form.[12] Specific knowledge is difficult to transfer, therefore experts have to work on one's own au-

7 Little (2001), p. 4.

8 95 percent of the companies surveyed were involved in partnerships and 69 percent plan to increase partnering activities in the long run. 17 percent of these companies generate more than a quarter of their turnover through cooperation. 55 percent of the respondents rate the importance of partnering as high or very high; when shifting to a long-term view, this number increases to 86 percent. See Little (2001), p. 7.

9 See Picot/Reichwald/Wigand (2001).

10 See Bonus (1998), p. 95 ff.

11 Jensen/Meckling (1992), p. 250 ff.

12 See Williamson (1975), p. 35 who calls this kind of knowledge "idiosyncratic".

thority; they need latitude in order to do their job in an appropriate way. But in some cases it is efficient to organize independent experts in hybrid institutions, e.g. if the reputation of the firm depends on the right use of the "specific" knowledge by the agents.[13] We will come back to this context later on.[14]

Economics takes up this development and increasingly deals with cooperation. Especially Institutional Economics[15] deals with this phenomenon. Cooperation can be classified as a hybrid structure[16] that is located between "markets"[17] or "classical contracts"[18] on the one hand and "firms" or "hierarchies" or "relational contracts" on the other hand. Cooperation in this sense is any form of relationship between these polar cases and is based neither on an arm's length or pure exchange contracts nor on the pooling of resources under common command. Cooperation unites elements of markets and hierarchies. It is based upon a nexus of treaties, which regulates and protects the economic activities in hybrid structures.[19] The starting point of these reflections was the path breaking article of COASE (1937) who asked why some economic activities are carried out over markets and others within firms. The underlying question is: where are the optimal boundaries of the firm? According to COASE, the use of institutions causes transaction costs.[20] NORTH (1987) has formulated a central finding: In a world with transaction costs the performance of economies depends on its institutions.[21] WILLIAMSON, one of the founders and supporters of the transaction cost approach illustrated the increasing importance of cooperation in economics. Whereas WILLIAMSON gave hardly any attention to hybrid forms in his book from 1975, "Markets and Hierarchies" he moved them into the center in "The Economic Institutions of Capitalism" in 1985.[22]

In the following, credit cooperatives and their financial network will be interpreted as hybrid structures in the sense of institutional economics. But before doing this, the origins and the current situation of the cooperative banking group has to be explained.

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13 For example franchise agreements
14 See section 4. infra.
15 See for an overview Richter/Furubotn (1999).
16 See Williamson (1985).
17 Cf. Williamson (1975).
18 See MacNeil (1978), p. 854 ff.
19 See Williamson (1990).
20 See Coase (1937) and (1960).
21 See North (1987), p. 419 and North (1990), p. 3.
22 See Williamson (1975) and (1985).

3 Cooperative banks in Germany and the cooperative banking group

3.1 The origins

Cooperative banks in Germany date back to the ideas of HERMANN SCHULZE-DELITZSCH and FRIEDRICH WILHELM RAIFFEISEN.[23] At the beginning of the 19th century, the pressure of competition resulting from the advance of industrialization and the liberalization of economic activity led to great economic hardship both in towns and rural areas. It was difficult for small craftsmen and merchants as well as for farmers to obtain raw materials and equipment because of a lack of capital. Furthermore, the banking market was not as developed as today. There were only a few urban banks that invested in the developing industry. This is why farmers, merchants and craftsmen depended heavily on local moneylenders who charged exorbitant interest rates. According to AKERLOF, this phenomenon can be explained as a problem of information costs.[24] Local moneylenders had to collect and evaluate a bulk of local and individual information of a nonstandard nature in order to evaluate credit worthiness.[25]

HERMANN SCHULZE-DELITZSCH and FRIEDRICH WILHELM RAIFFEISEN addressed this problem by creating cooperative associations.[26] These institutes were able to offer to their members reasonably priced short-term credit to finance working capital. They could do so because they drew on local insider information of their members, confined membership to people of solid local reputation and had them accept mutual and unlimited liability for their own cooperative.[27]

In order to use the local informational pools the credit cooperatives of the 19th century were limited geographically to small areas.[28] This, however, had a detrimental effect on their relationship to larger urban banks. In order to stabilize their liquidity[29], credit cooperatives had to deal with larger banks. However, the banks could not assess these institutions'

23 See Faust (1977), p. 536 ff. and Aschhoff/Henningsen (1996), p. 16 ff.

24 See Akerlof (1970), p. 498 f.

25 See Bonus (1986), p. 315 ff. and Bonus/Schmidt (1996), p. 186 ff.

26 In order to provide affordable operating equipment loans for craftsmen and merchants Hermann Schulze-Delitzsch founded the first "Vorschussverein" in 1850; these mutual loan associations were later called "Volksbanken". In an attempt to alleviate poverty among the rural population, Friedrich Wilhelm Raiffeisen founded the first "Darlehnskassenverein" in 1862; these loan societies were later called "Raiffeisenkassen".

27 Cf. Bonus (1986), p. 316 ff. and Bonus/Schmidt (1990), p. 186 ff.

28 See Faust (1977), p. 340.

29 At seedtime and before harvest the cooperative needed to raise funds to satisfy the high demand for credit, whereas after the harvest the surplus revenue had to be invested profitably. See Bonus/Schmidt (1996), p. 192 for details.

reliability and financial standing. In order to avoid being subject to opportunism[30] the institutional answer was a hybrid organizational form. The local credit cooperatives of a region formed a coalition and established a regional central bank of their own.[31] By supervising the regional central bank the credit cooperatives were able to keep the central banks from investing their money in a risky manner or refusing to pay out money when it was needed. In the middle of the 19th century the first central banks was created. For the purpose of liquidity management among cooperative central banks, the first top institution of the cooperative banking group, the "Preussische Central-Genossenschaftskasse", was born in Berlin in 1895 as the predecessor of DZ BANK.[32] Hence, a three-tier cooperative banking group was established that consists of local cooperative banks, regional central banks, and a nationwide top institution. The nationwide three-tier organization model lasted several decades until the 1980s when several regional central banks were taken over by the top institution.

To be able to offer their customers a wide range of products and services, the cooperative banks established interlinked business operations with a number of associated corporations that specialized in different financial services such as home loans, insurances or investments. Cooperation in this field is advantageous because all the relevant information about a customer is available within the cooperative bank and can be shared with all associated companies. The customer has the advantage to get all financial services from the same institution.

3.2 The cooperative banking system today

The cooperative banking group comprises around 1,621 credit cooperatives (as of Dec. 31, 2001).[33] The locally active primary cooperatives work together with affiliated regional and central enterprises on the second and third tier (see figure 1).

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30 According to Williamson, opportunistic behavior can be defined as "self-interest seeking with guile". Williamson (1985), p. 47.

31 See Bonus/Schmidt (1990), p. 192 ff. and Bonus (1994b), p. 476.

32 See Faust (1977), p. 278.

33 Most of them are "Volksbanken und Raiffeisenbanken", but there are also "Sparda-Banken" (foundet by railwaymen), "Post-Spar- und Darlehnsbanken" (founded by postal employees), "Beamtenbanken" (civil servants' banks) and church credit cooperatives. See Aschhoff/Henningsen (1996), p. 54.

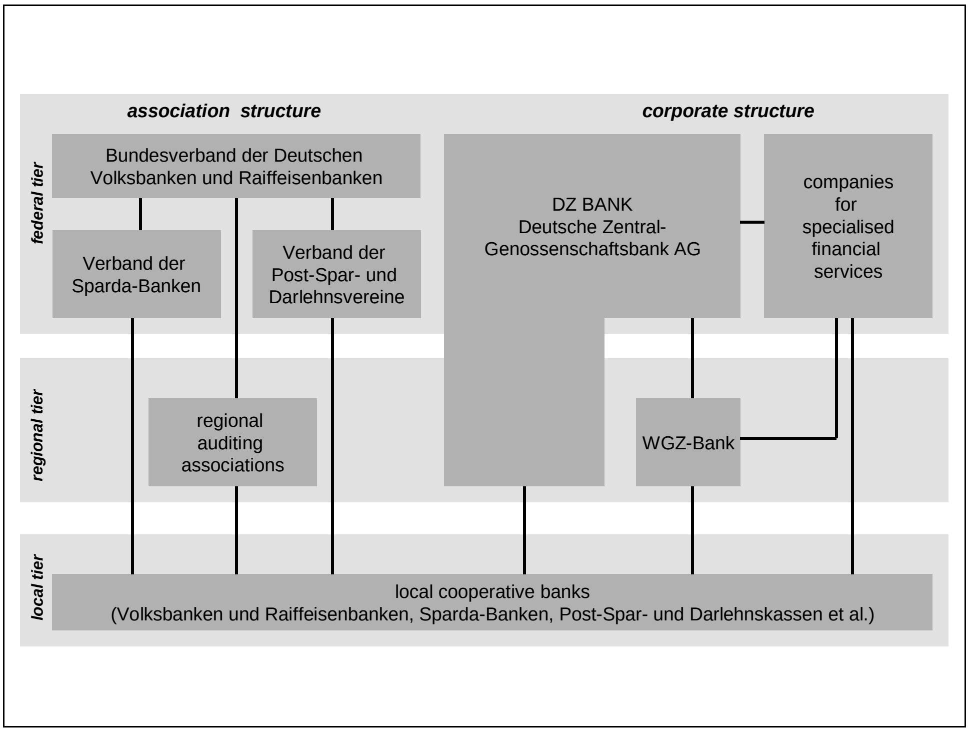

Figure 1: The cooperative system in Germany – association and corporate structure
Source: Following ASCHHOFF/HENNINGSEN (1996), p. 54 and POLSTER (2001), p. 295.

The second or regional tier consists of regional central banks. The top institution "Deutsche Zentral-Genossenschaftsbank" (in short: DZ BANK) and several companies for specialized financial services form the third tier. The group is divided into both, two-tier and three-tier regions. In the past there was an exhaustive net of regional "central banks" in Germany which formed the second tier. But through the years they were merged with the DZ BANK (formerly called "Deutsche Genossenschaftsbank", in short: DG BANK[34]). Hence, the formerly autonomous regional central banks became subsidiaries of the top institution. The last independent regional central bank is located in Rhineland and Westphalia , the "Westdeutsche Genossenschafts-Zentralbank" (in short: WGZ-Bank). The WGZ-Bank promotes the interests of the affiliated local cooperative banks by providing subsidiary financial services such as refinancing and investment options, joint loans, investment management, money and foreign exchange trading and securities transactions. The central bank, the DZ BANK, provides regional bank services to Volksbanken und Raiffeisenbanken in other parts of Germany. In addition, the DZ BANK is the central bank of the cooperative banking group and provides, for example, issuing and consortium services and international banking services.

[34] In 2001, the former regional central bank "Genossenschafts-Zentralbank Frankfurt/Stuttgart" (in short: GZ-Bank) and the former top institution „Deutsche Genossenschafts-Zentralbank" (in short: DG-BANK) have merged.

In contrast to most other banking groups[35], the line of command within the group of cooperative banks is from bottom to top. Regional and central enterprises are jointly owned subsidiary companies of the local cooperative banks and not vice versa. The local cooperative banks are registered cooperatives according to German cooperative law ("Genossenschaftsgesetz"). They are owned by 15 million members[36], who are owners and customers at the same time (cooperative principle of identity). The cooperative banking group has around 30 million customers in total, i.e. approximately every other customer is a member. At the general meeting of members of a cooperative bank, the supervisory board is elected. It appoints the management board and determines the banks strategy. The WGZ-Bank is a registered cooperative and is owned by the local cooperative banks in Rhineland/Westphalia. The capital shares of the former regional central banks in other regions has been transferred to regional holding companies, which are controlled by the local primary banks of the regions in each case. The top institution, the DZ BANK, has the legal status of a stock corporation. Its capital is mainly (82.5 percent) held directly or indirectly by local cooperative banks.[37] The rest of the shares are held by the WGZ-Bank (6.7 percent), other cooperatives (1.9 percent) and other shareholders (8.9 percent).[38]

In addition, the cooperative banking group comprises several companies for specialized financial services that are active throughout Germany. There are three mortgage banks ("DG HYP", "Münchener Hypothekenbank" and "WL-BANK"), the "Schwäbisch-Hall" home loan bank, the "R+V" insurance group, the "Union-Investment" asset management group and the "VR-LEASING", a provider of leasing contracts. Most of them are stock corporations whose capital is held for the most part by the DZ BANK. In addition, data processing is sourced out; after a process of concentration in recent years, three regional data processing centers within the cooperative banking group exist.

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35 The universal banks can be divided into three groups: the so-called private commercial banks, the public savings banks and the cooperative banks. The 314 private commercial banks are often branch bank systems with the legal status of a stock corporation. Deutsche Bank, Dresdner Bank, Commerzbank and HypoVereinsbank are the biggest banks which belong to this group. In contrast, the "Sparkasse" savings bank group and the cooperative banking group are federated networks. Although both savings banks and credit cooperatives are organized in federated networks, they show some main differences. *Size*: With an average balance sheet total of around 1.6 billion Euros the savings banks are far smaller than an average private commercial bank, but they are almost six times as big as a local cooperative bank with its average balance sheet total of around 298 million Euros. In recent years, several local cooperative banks have merged, therefore the average size of the cooperative institutes has grown and this development is still going on. *Ownership structure*: Owner of the savings banks and central giro institutions are the municipalities or the German federal states ("Bundesländer") whereas cooperative banks are owned by their members. The capital of the central banks and other specialized companies within the group is mainly held directly or indirectly by the local cooperative banks. *Legal status*: According to their ownership structure most of the savings banks and the central giro institutions have public-law status, whereas almost all local cooperative banks are registered cooperatives according to German cooperative law ("Genossenschaftsgesetz").

36 Cf. DZ BANK (2001), p. 15.

37 Most of the capital is held indirectly by regional holdings which are controlled by local cooperative banks of the region.

38 See DZ BANK (2002a), p. 6.

According to the German cooperative law registered cooperatives must be members of a regional[39] cooperative auditing associations.[40] These regional associations perform the compulsory audits of affiliated cooperatives. They also deal with consulting, support and training. The auditing associations are in turn controlled by representatives of the member banks. The regional cooperative auditing associations are members of the Federal Association of Cooperative Banks ("Bundesverband der Volksbanken und Raiffeisenbanken", in short: BVR). It is active on a nationwide scale. Its main task is to represent the technical and economic policy interests of the cooperatives as a group.

The supervision of banks in Germany is legally based on the "Kreditwesengesetz" (in short: KWG) and is enforced by a federal authority, the "Bundesantalt für Finanzdienstleistungsaufsicht" (in short: BAFin). Additional supervision authorities are the central bank ("Deutsche Bundesbank"), the federal ministry of finance, the federal government and for some specialized areas also authorities of the federal states. Supervision was established in Germany following a banking crisis in 1931. The main instrument of banking supervision are: issuing banking-licenses, auditing the equity capital and the ability to pay, supervising the lending business and the annual audit.

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39 For some of the cooperatives there are nationwide active, specialized auditing associations, for example for the "Sparda-Banken" and "Post-Spar- und Darlehnsvereine".

40 It is the task of the cooperative auditing associations to check whether the accounting and general management of affairs by the management board is adequate and orderly in a technical and legal sense. The supervisory board of the local cooperative bank, however, is supposed to ensure that the cooperative's strategy conforms to the members' business interests.

4 Cooperative banks and the cooperative banking group as hybrid structures

4.1 Hybrid structures as safeguards within precarious relationships

As we will see later on, cooperative banks and the cooperative banking group have the function to safeguard against opportunistic behavior within "precarious relationships". BONUS defines precarious as "any relationship which involves involuntary transactions"[41]. Prominent sources of precariousness are (1) specificity and (2) plasticity.[42]

1. The term "specificity" stems from transactions economics.[43] Whoever invests in a chain of transactions becomes dependent on his partner in these transactions according to the degree of specificity. Specificity is the amount of capital tied exclusively to this chain of transactions. "Quasi-rents" are used to measure transaction-specific dependence. The quasi-rent is the difference between the value of an asset in its optimal use and its value in its second-best use.[44] If a component supplier produces custom-made component parts and the customer suddenly refuses to pay for them, then the supplier may only be able to sell them as scrap. The quasi-rent in this case is the difference between the price agreed upon with the customer and the proceeds from sale of scrap. The higher the quasi-rent, the higher is the dependence and the higher is the risk of expropriation by hold up[45]. Williamson postulates that the degree of hierarchy of the governance structure is positively related to specificity.[46]

2. Besides the issue of "hold up", there is another kind of opportunism, called "moral hazard"[47]. It is caused by "plasticity". The term "plastic" goes back to ALCHIAN and WOODWARD: "We call resources or investments plastic to indicate there is a wide range of legitimate decisions within which the user may choose, or that an observer can less reliably monitor the choice."[48] Production factors are "plastic" when they need great latitude to do their job which is based on experience, instinct, special feel or even sixth sense. The knowledge that is connected with "plastic" factors can

41 Bonus (1995), p. 3.
42 See Polster (2001a), p. 33 ff. Bonus quotes opportunism, information deficiency, regulation, and externality as sources of involuntary transaction. Bonus (1995), p. 4.
43 Cf. Williamson (1985), p. 52 ff.
44 See Klein/Crawford/Alchian (1978), p. 298. They definition is as follows: "The quasi-rent value of the asset is the excess of its value over its salvage value, that is, its value in its best use to another renter. The potentially appropriable specialized portion of the quasi-rent is that portion, if any, in excess of its value to the second highest-valuing user."
45 The term "hold up" is used by Klein/Alchian/Crawford (1978), p. 302.
46 See Williamson (1985), p. 79.
47 See Alchian/Woodward (1987), p. 116.
48 Alchian/Woodward (1987), p. 117.

be described as "idiosyncratic knowledge"[49] or "specific knowledge"[50]. Plasticity is a typical element of relationships between principals and agents. Examples of plastic factors are managers from shareholders' point of view, employees from employers' point of view and borrower from lenders' point of view.[51] The intensity of plasticity depends on two factors: (a) the greatness of latitude of the agent and (b) the degree of information asymmetry between principal and agent.[52] On the one hand, it would be good to supervise the agent in order to avoid that he uses his latitude in an opportunistic way. But on the other hand, plastic factors need a certain latitude to work effectively. Since plastic factors cannot be appropriately supervised, the organizational structure must be such that individuals have an incentive to apply them at their own discretion in the interest of the company (e.g. through a compensation policy).

4.2 Individual cooperative banks and financial cooperatives

Cooperative banks are a classic example of hybrid structures between market and hierarchy. Members of cooperatives concentrate their forces in order to achieve more than a single person or institution could do on its own (principle of cooperation). The economic advantages of cooperatives are as follows:

1. Cooperatives enable their members to use economies of scale and scope.[53]

2. Cooperatives improve the competitive strength of their members.[54]

3. The specific governance structure of cooperatives internalize dependence between transaction partners and thereby minimize transaction costs.[55]

The advantages (1) and (2) can also be realized by other organizational structures. Stock companies also reduce costs of production and strengthen their competitiveness by using the advantages of size. But only a cooperative minimizes transaction costs that emerge from the dependence between the debtor and the creditor because of its special governance structure.

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49 Williamson (1975), p. 35 defines idiosyncratic knowledge as "that intuitive knowledge, based upon training and experience, that is incapable of translation into written form". See also Bonus (1986), p. 328.

50 See Jensen/Meckling (1992), p. 251: "We define specific knowledge as knowledge that is costly to transfer among agents and general knowledge as knowledge that is inexpensive to transmit." Cf. section 2. supra.

51 See Alchian/Woodward (1988), p. 68.

52 See Dietl (1998), p. 10 f.

53 See Eschenburg (1971), p. 15 ff., Boettcher (1980), p. 31 ff., Bonus (1986), p. 313.

54 See Eschenburg (1971), p. 15 ff., Boettcher (1980), p. 31 ff., Bonus (1986), p. 314. This argument is taken from the concept of "countervailing power" of J.K. Galbraith (1952), S. 108 ff.

55 See Bonus (1986), p. 315 ff.

When compared to stock companies the specific features of cooperatives become obvious. The purpose of the cooperative enterprise is to promote their members households or companies (member value), but not to maximize profits or the shareholder value (promotion mandate). The clients of cooperatives are the owners at the same time (principle of identity). Members of cooperatives have an equal voting right regardless of their capital investment, as well as the opportunity to take part in the decision-making process (principle of democratic administration).

Following BONUS, the relationship between members and their cooperative is "precarious". In the past, the relationship between members and their credit cooperative was *precarious* because of high *transaction-specific investments*.[56] Apart from the local moneylender the local credit cooperative had a local monopoly position. The only alternative to obtain credits was the local usurer. In this way a high quasi-rent emerged that consisted of the difference between the credit conditions offered by the cooperative and those offered by the usurer. These quasi-rents could have been expropriated by a local bank by raising the loan rate or by claiming charges with the aim of making profit. Therefore, the quasi-rents had to be safeguarded institutionally. The borrowers safeguarded themselves by establishing a cooperative bank in which the members themselves are owners and exercise control. In the early cooperatives an elaborate system of controls was established. Within the governance structure of the credit cooperative *plastic factors* play an important role. Members are not able to control whether the members of the supervisory board and the management board do their job in an appropriate way. To make sure that the agents do not use their latitude in an opportunistic way all decision-making bodies were reserved to members who worked on an honorary base. Hence, all members were able to evaluate the quality of the decisions made bases upon their personal experience. The only professional, the "Rendant", who was to carry out the administrative activities of the bank, was supervised by the regional auditing association.

Nowadays, customers can choose between several banks; credit cooperatives have no longer local monopoly. In the modern competitive financial markets, there is little room for promotion of members in the conventional sense.[57] Because of the high market transparency, innovative financial products or services are rapidly imitated by competitors. The relationship between customers and a bank, however, is still *precarious*.[58] Nowadays the customer of a bank – especially small and middle sized enterprises – is confronted with a vast amount of financial products and services, promotion regulations, tax directions etc. without being an expert in this field. Since these customers cannot afford a staff of skilled experts, they rely on the advice of banks as external consultants. Financial advice, how-

56 Cf. Bonus (1986), p. 333 f and (1994b), p. 475, Bonus/Schmidt (1990), p. 190 f.
57 See Großkopf (1990).
58 See Bonus (1994b), p. 475 f and (1994a), p. 59 ff.

ever, is an important factor of production so that customers depend on their banks without being able to control it effectively (*plasticity*). During the business relations the customer undertakes transaction-specific investments, e.g. by making long-term contracts (*specificity*). An appropriate solution to avoid opportunism (like hold up and moral hazard) in such a situation is the above described hybrid structure of the cooperative.

To sum up: Cooperative banks are themselves hybrid structures because they unite characteristic features of markets and hierarchies[59]. On the one hand, members of credit cooperatives operate independently, e.g. as farmers, craftsmen or merchants, on the market. On the other hand, loans and other financial services – which are important factors of production – can be obtained at much better terms by minimizing transaction costs through a cooperation established by the members. In order to protect themselves against opportunistic abuse of dependency, members have to control the bank they depend on. Members are owners of the cooperative bank and have several rights to supervise it. Hence, an element of hierarchy becomes part of the governance structure. Members of cooperatives stay legally and economically independent (market) except for the business relationship to the credit cooperative (hierarchy).

4.3 The cooperative banking group

4.3.1 Different types of hybrid structures: "bottom-up" and "top down"

Not only the cooperatives themselves but also the cooperative banking group as a whole is a hybrid structure.[60] On the one hand, the strength of credit cooperatives lies in its smallness, which facilitates obtaining specific local knowledge about customers, fast decisions and flexible local operations. On the other hand, smallness can be an disadvantage, if a customer needs a credit of a size that exceeds capacity of the local credit cooperative, if a client wants to be supported in international business, or if the cooperative bank wants to offer a wide range of specialized financial products and services. In this case, local cooperative banks have to work together with larger banks or specialized financial companies. As a result, the credit cooperative would get dependent on these partners which are plastic factors. A *precarious relationship* arises. If the larger partner does not work properly, the smaller credit cooperative has to pay for the damage. Besides, they can misuse internal corporate information on customers to entice them away from the cooperative. In order to avoid these problems the cooperative banking group, a hybrid organizational structure, has been developed. The local credit cooperatives own the central bank and the specialized companies on which they depend. In this case, command within the cooperative group is

59 See Bonus/Schmidt (1990), p. 191 f.
60 See Bonus/Schmidt (1990), p. 192.

from the bottom to the top. The core of the cooperative banking group is not the central banks or the specialized companies but the locally acting credit cooperatives. Only the credit cooperatives have information about their customers and know what their customers' needs are. The cooperatives are the source of a trust relationship between the bank and the client. The larger centralized units are subsidiary suppliers and do business not on behalf of themselves but on behalf of the cooperative banks. Therefore the peripherally acting units determine the strategy of the banking group, not the larger "head" units.

A diametrically opposed example of a hybrid organizational structure is a franchising agreement.[61] The franchisor provides the franchisee with know-how and reputation. The success of a franchise system depends on the efficient use of the plastic know-how by the franchise dealer. In order to enable the local dealer to act like a entrepreneur and to use his ideosynchratic knowledge he needs latitude. On the other hand, the franchisor and other franchisees must insist on a minimum quality level to safeguard the brand-name capital[62] of the franchise system. Therefore, the franchise contract must include precise regulations and control devices. In this way, hierarchical (contract) and market (latitude) elements are combined in franchising. In this case, the authority to issue directives is *from top down*. In contrast to the cooperative banking group, in this case the central office, i.e. the franchisor, is the motor of the franchise system because he has developed the idea of the franchise system and gained a certain reputation. The knowledge that is required to support and further develop the franchise concept is under control of the franchisor. He has the competence to determine the franchise strategy.

To sum up: The cooperative banking group and a franchise have many things in common, but they also exhibit differences. Both are hybrid structures that utilize local, "plastic" knowledge. That, requires decentralized structures. Both need larger units to utilize economies of scale and bargaining power. Therefore central institutions are necessary. The difference between the cooperative financial group and franchising is their different business concept. The motor of the cooperative banking group are the locally acting credit cooperatives which are positioned peripherally. The core of a franchise system is the franchisor who is positioned centrally.

61 Cf. Bonus (1986), p. 332 f and (1999), Bonus et al. (1999), p. 12 ff.

62 See Klein, Crawford and Alchian, who note: "A franchisee is fundamentally a renter of the brand-name capital (and logo) owned by the franchisor." Klein/Crawford/Alchian (1978), p. 321.

4.3.2 Sources of precariousness

As mentioned above, the relationship between the local cooperative banks and the central banks and other centralized members of the cooperative banking group is *precarious*. Both, *specificity* and *plasticity* are sources of precariousness.[63]

Cooperative banks have invested in a *transaction-specific* way in their electronic data processing (EDP) infrastructure, for example. Most of the technical infrastructure (hard- and software) and the specific know-how of several employees of the bank would lose their value if the bank was forced to change to another EDP-center, e.g. the EDP-center of the savings banks. That is why the locally acting bank depends on its DP-center. Another example is the business relation between local cooperatives and central banks. In recent years, the WGZ-Bank and the DZ BANK not only offer standardized financial products and services but increasingly take over parts of the back office functions of cooperative banks with the aim of reducing costs.[64] An increasing specificity is the consequence of this process of outsourcing, because the re-integration of functions into the organization of the credit cooperatives is costly. Consequently the risk of a "hold up" is high.

Plasticity occurs in most of the business relations between cooperative banks and other members of the cooperative banking group. The central banks and specialized companies not only offer standardized products but to an increasing degree individual services. Over time, the employees of central banks and specialized companies gain experience and idiosyncratic knowledge emerges. In order to do their job in an appropriate way, the employees of the central banks need a wide latitude. In addition, the cooperative bank cannot supervise the employees of the central banks and specialized companies in a sufficient way. The local banks have neither the time nor the knowledge to judge whether the agent is reliable and uses his latitude in a responsible way. On top of that there is the great influence of central banks and specialized companies on strategic decisions within the group. The DZ BANK owns most of the shares of the specialized companies, such as "Bausparkasse Schwäbisch-Hall" or "Union Investment". Therefore, rather the DZ BANK determines the business policy of the latter much more than the local cooperative banks. The specialized companies themselves have a great influence on the design of the group's financial products and services. Therefore the risk of "moral hazard" is significant.

Appropriate institutional safeguards are indispensable to avoid opportunistic behavior of the centralized units within the cooperative banking group. We will deal with this topic later on.

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63 See Theurl/Kring (2002).
64 See e.g. Heinke (1998).

5 The relationship between strategy, structure and core competencies[65]

It was CHANDLER who stressed the strong interdependence between strategy and structure.[66] This duality is based on the "Market-based View of Strategy" of which PORTER[67] was the most prominent author. Within the last years, the increasing influence of the "Resource-based View of Strategy" underlined the importance of core competencies. The economist NELSON emphasized the relationship between them. He asked: "Why do firms differ, and how does it matter?"[68]. His answer is that there are three factors of differentiation for companies: "its strategy, its structure and its core capabilities."[69] These interdependencies must be considered; there must be a "fit" of strategy, structure and core competencies.

5.1 Strategy

5.1.1 Strategic management approaches

Although strategic management has been a separate section of business administration for almost 40 years, there is no common understanding what strategy is and how to manage strategies. A classic definition comes from CHANDLER who defines strategy as "the determination of the basic long-term goals and objectives of an enterprise, and the adoption of course of action and the allocation of resources necessary for carrying out these goals. Decisions to expand the volume of activities, to set up distant plants and offices, to move into new economic functions, or become diversified along many lines of business involve the defining of new goals."[70]

Different strategic management approaches can be distinguished according to their perspective. The "Market-based View" focuses on the industrial sector in which the company is located. PORTER as one of its main representatives is of the opinion that competitive advantages are depending on the specific features of the market, i.e. the external factors of a company.[71] His arguments are based on the "Structure-Conduct-Performance-Paradigm" postulated by the Harvard School.[72] The perspective is "outside in". The "Resource-based

65 Cf. Bonus et al. (1999), p. 14 ff.
66 Cf. Chandler (1962).
67 See Porter (1984) und (1985).
68 Nelson (1991), p. 61.
69 Nelson (1991), p. 67.
70 Chandler (1962), p. 13.
71 See Porter (1984) and (1985).
72 See e.g. Bain (1959).

View" however moves the internal factors of a company into the center.[73] It postulates that specific tangible and intangible resources of a company are crucial to reach competitive advantages. This approach chooses an "inside out" perspective. Although there is a strong separation in the strategic management literature, both theories complement one another: A positioning at an attractive market creates competitive advantage only if the company is provided with the suitable resources. On the other hand, resources and competencies only lead to a successful performance if they enable the company to achieve an attractive position in the market. The core competence approach integrates both aspects.[74] It will be explained later on.

According to PORTER, strategy is connected with the positioning of a company: "Strategy is the creation of a unique and valuable position, involving a different set of activities. If there were only one ideal position, there would be no need for strategy. Companies would face a simple imperative – win the race to discover and preempt it. The essence of strategic positioning is to choose activities that are different from rivals."[75] But which activity is right and how is it possible to be different from rivals?

5.1.2 "Concentration of forces" – The new strategy of the cooperative banking group

"Concentration of forces: One group – one strategy"[76] is the title of a study that was presented by the central association of the German cooperative banking system (BVR) in 1999. On this basis, the general assembly of the BVR decided to carry out seven subprojects. The highest aim was to create a uniform strategy for the whole group that is in line with the changing market conditions. An extensive final report "Concentration of forces: The joint strategy"[77] passed the general meeting of the BVR in 2001. Goals of the resolution are "a better exhaustion of market potentials, safeguarding and strengthening the efficiency and earning power by reducing costs and creating a standardized and efficient risk management"[78].

The latest strategic guidelines paint a picture of a strategic network with decentralized, economically and legally independent and locally acting cooperative banks.[79] The local cooperative banks are supposed to concentrate on their core competence which is the sale,

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73 See Selznick (1957), Penrose (1959), Wernerfeld (1984), Barney (1991), Grant (1991) and Peteraf (1993).
74 See Hellinger (1999), p. 26 ff.
75 Porter (1996), S. 68.
76 BVR (1999), title translated by the author.
77 BVR (2001a), title translated by the author.
78 BVR (2001a), S. 1, translated by the author.
79 Cf. BVR (2001a), p. 5.

whereas most of the products and services are produced by specialized companies that are part of the financial network. According to the BVR, an intensified specialization with the aim to reduce costs can be achieved by outsourcing tasks within the group.[80] Activities such as the development of financial products, administrative functions or processing of financial services have to be sourced out from local credit cooperatives to central institutions within the network.[81] An important component of the new strategy is to abolish competition between cooperative banks on local markets by mergers and to enlarge cooperative banks up to an efficient minimum size.[82] Following the thesis "structure follows strategy" the fitting structure was deduced from the new strategy.[83]

German universal banks have no strategy in the sense of PORTER.[84] To overstate it: All banks want to do the whole variety of banking business with all customers at all places.[85] There is no difference between private banks, savings banks and credit cooperatives. All universal banks follow the same strategy; which in the PORTER'S sense is no strategy at all. Strategy means to choose a course. One has to decide: "The essence of strategy is choosing what not to do."[86] The German cooperative banks do not want to exclude products, services, customers or markets. The lately passed "joint strategy" stresses this adjustment by defining the "cooperative bank of the future": "[The cooperative bank of the future] is a universal bank and offers all banking services to all customers in their regional market"[87]. The only evidence that could be interpreted as an attempt to differentiate is concerned with membership: "Membership as a central characteristic feature and the close relationship to customers […] characterize the business policy […] of every Volksbank and Raiffeisenbank"[88].

The early credit cooperatives had a clear strategy.[89] They were banks of the first small and medium sized enterprises. Cooperative banks were the only possibility of small sized farmers, merchants and craftsmen to get access to credits. This strategy was their key to success. Problems arose when they started to open up for everybody. The credit cooperatives wanted to be banks just as savings banks and private banks were. However, it is not possible to be different from competitors by acting this way. This is not a strategy that can

80 See BVR (2001a), p. 6.
81 See BVR (2001a), p. 6.
82 Cf. BVR (2001s), p. 7.
83 See BVR (2001s), p. 4 and (2001c), p. 4.
84 See Bonus et al. (1999), p. 15 ff. and Polster (2001b), p. 302 f.
85 See Steiner (1995), p. 19.
86 Porter (1996), p. 70.
87 BVR (2001b), p. 2, translated by the author.
88 BVR (2001a), p. 5, translated by the author. See also BVR (2001c), p. 6.
89 See section 3.1 supra and Polster (2001), p. 300 ff.

give orientation to an organization like the cooperative banking group, it is a "strategy of indiscriminateness".[90]

PORTER gives advice as to how companies can position themselves: "A company's history can […] be instructive. What was the vision of the founder? What were the products and customers that made the company? Looking backward, one can reexamine the original strategy to see if it is still valid. Can the historical positioning be implemented in a modern way, one consistent with today's technologies and practices?"[91] The identity of a company together with its origins could be a clue to find the appropriate strategy.[92] In this context, the core competencies of a company play an important role.

5.2 Core competencies

5.2.1 The core competence approach and its extension with the transaction cost approach

SELZNICK and PENROSE already argued at the end of the fifties that internal resources of a company are the condition to achieve competitive advantages. Their "distinctive competence" approach was a cornerstone of the resource-based view. Strategically important resources are defined as "all assets, capabilities, organizational processes, firm attributes, information, knowledge etc. controlled by a firm that enable the firm to conceive of and implement strategies that improve its efficiency and effectiveness."[93]

Other authors developed the approach further and combined it with aspects of the market-based view; the result was the core competence approach.[94] Their definition of core competencies illustrates the integration: "At least three tests can be applied to identify core competencies in a company. First, a core competence provides potential access to a wide variety of markets. […] Second, a core competence should make a significant contribution to perceived customer benefits of the end product. […] Finally, a core competence should be difficult for competitors to imitate."[95] Following PRAHALAD and HAMEL "the real resources of advantage are to be found in management's ability to consolidate corporatewide technologies and production skills into competencies that empower individual businesses to adapt quickly to changing opportunities."[96] Firms are supposed to identify, to cultivate and

90 Cf. Bonus et al. (1999), p. 15, Polster (2001), p. 303, von Stein (2000), p. 23.
91 Porter (1996), p. 76.
92 See also Bonus et al. (1999), p. 17, Polster (2001), p. 303.
93 Barney (1991), p. 101.
94 See Prahalad/Hamel (1990). Hellinger (1999), p. 26 ff., interpreted the core-competence approach as a combination of market-based and resource-based approaches of strategic management.
95 Prahalad/Hamel (1990), p. 84.
96 Prahalad/Hamel (1990), p. 81.

to develop new core competencies to be successful. A company needs “meta competencies”[97] to be able to manage core competencies. For this purpose, a strategic infrastructure has to be built up.

REVE and PICOT/HARDT combined the core competence approach with transactional cost economics in order to be able to determine the vertical and horizontal boundaries of a firm.[98] WILLIAMSON developed a heuristic model to solve the “make or buy”-problem in a vertical sense.[99] In order to optimize costs of transaction and production an efficient institutional arrangements between market and hierarchy has to be chosen. According to WILLIAMSON, the efficiency of governance structures depends on three dimensions: specificity, uncertainty and frequency. As mentioned above, in this paper we want to use the wider dimension “precariousness” because it includes both types of opportunism, hold up, as well as moral hazard.[100] The transaction cost approach, however, is not able to determine the horizontal boundary of a firm. For this purpose, a fourth dimension has to be taken into consideration, the “strategic importance” of a resource.[101] According to this argumentation the efficient institutional arrangement depends on two features: (1) precariousness and (2) strategic importance.

1. As mentioned above, “*precariousness*” emerges if someone within a cooperation becomes dependent on a partner so that the latter is able to use his position in an opportunistic way, while an institutional safeguard is not feasible.[102] Precarious relationships include involuntary transactions. Sources of precariousness could be “specificity” and “plasticity”.[103]

2. The feature “*strategic importance*” comes from strategic management.[104] Resources are strategically important if they enable the company to achieve competitive advantages in present and future. Competitive advantages like this result from advantages of costs or differentiation, from entering new markets or from changing conditions of an industry.[105] Strategically important resources are usually very specific, because firms want to make a distinction between themselves and their competitors.[106] Strategic important resources have to be protected against competitors. Re-

97 See Klein/Edge/Kass (1991), p. 4 f, who call them “metaskills”.
98 See Reve (1990) and Picot/Hardt (1998).
99 Cf. Williamson (1985), p. 85 ff.
100 See section 4.1 supra.
101 See Picot/Hardt (1998), p. 631 f, Reve (1990), p. 133 ff., Maselli (1997), p. 222 ff., Hellinger (1999), p. 117 ff. and Polster (2001b), p. 238 ff.
102 See Bonus (1994a), p. 84.
103 See section 4.1 supra.
104 See Picot (1991), p. 346, who uses the term “strategic importance” to determine the vertical boundary of a firm.
105 Cf. Picot/Maier (1992), p. 21.
106 This argument cannot be reversed. Specific resources are not always strategically important, e.g. a self-made software of a company is regularly very specific, because it has no other use when development

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sources with a high strategic importance should be integrated into the firm, because otherwise it is too expensive or even impossible to protect them against imitation.[107]

Moreover, PICOT/HARDT distinguish between three types of resources: core competencies, complementary competencies and peripheral competencies.[108]

- *Core Competencies* are the strategic heart and the motor of a firm. They are very specific and have a high strategic relevance. Therefore they have to be integrated into the boundaries of the firm. They have to be protected against imitation through competitors. For example, Honda has the core competence to build motors.

- *Complementary competencies* exhibit a medium specificity and strategic importance. In their absence, the utilization of core competencies is difficult. Complementary competencies are regularly core competencies of other companies that are specialized in this field. Therefore the firm has to cooperate with the owner of these competencies. Again an excellent example is Honda: Certainly the firm has a core competence in building motors, but it had to develop the antilocking system for their cars together with one of the specialized companies (Bosch and Nippon Denso). In this context, it is important to stabilize the hybrid organizational form by treaties or credible commitments.

- *Peripheral competencies* are complementing the products and services of a firm, but they are not strategically important. Also, they are not specific. Therefore these resources can be bought in markets without costly institutional safeguards. The delivery of cars is such a peripheral competency. This service is regularly offered by specialized forwarding agencies, that are not owned by the producer.

These standard strategies can be applied to cooperative banks. Prior to that, however, we have to identify their core competencies.

5.2.2 Core competencies of cooperative banks

What are cooperative banks good for? In which economic sectors are cooperative banks better than other banks? These questions have to be answered in order to identify their core competencies. In the literature and in strategic resolutions of cooperative banks the following special capabilities of credit cooperatives are quoted: (1) decentralized structure, local competence and customer closeness, (2) a good relationship with small and medium sized

moves on further in the meantime, but it normally has no strategic importance. See Picot (1991), p. 346 f.

107 See Picot/Hardt (1998), p. 631.

108 Cf. Picot/Hardt (1998), p. 629 ff. Also Hellinger (1999), p. 126 ff., Polster (2001), p. 239 ff.

enterprises, (3) the collaboration within the cooperative banking group and (4) membership and self-government.[109]

1. Compared to other banks credit cooperatives are small in size. This leads to advantages of smallness, e.g. local knowledge, human closeness and flexibility in decision making because of their autonomy.[110] These capabilities serve to increase the benefits of customers. But these features are not unique positions; they can not be protected against substitution or imitation. Particularly the German savings banks are structured in an comparable way and use advantages of smallness.

2. Traditionally there is a close relationship between credit cooperatives and small and medium sized enterprises.[111] Cooperative banks are founded by the emerging middle class: small farmers and craftsmen. This clientele is still one of the main groups of customers of credit cooperatives. Finally, cooperative banks themselves are small and medium sized enterprises. Their experience in consulting middle sized companies creates a noticeable additional customer benefit. Furthermore, the experience of cooperative banks provides access to several markets by cross-selling. However, other banks, i.e. the savings bank group, have a long tradition in consulting small and medium sized companies as well. Moreover, in several countries state-owned banks are specialized in lending money to small and medium sized enterprises. In Germany, the federal government intends to establish a new state-owned bank with the objective to grant loans to small and medium sized enterprises.[112] Therefore this strength of cooperative banks cannot be their core competence, at least not in Germany today.

3. Cooperative banks have a long experience in working together within the cooperative banking group.[113] The division of labor increases the cost-efficiency and the product quality of cooperative banks. As explained above, credit cooperatives combine advantages of smallness with advantages of size. In this way, the well experienced collaboration increases the benefit of the customers. Furthermore the cooperative network acts on several markets with different financial products and services. But almost every banking system has imitated comparable structures. Even

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109 See Hellinger (1999), p. 258 ff.
110 Cf. BVR (2001a), p. 13 f., Bonus (1994b), p. 59 ff. and Bonus/Greve (1996), p. 288 ff.
111 See e.g. Kubista (1992).
112 In order to create the new bank, it is planned to merge two existing state-owned banks, the “Kreditanstalt für Wiederaufbau” (in short: KfW) and the “Deutsche Ausgleichsbank” (in short: DtA). Cf. Stuhr (2002).
113 See Aschhoff/Henningsen (1996), p. 47 ff.

the savings bank group is structured exactly the same way.[114] That is why the ability of "networking" is not a core competence of the cooperative banking system.

4. Even today, membership is an important characteristic feature of cooperative banks. In the legal sense the membership and the promotion mandate are the "raison d'être" of a cooperative.[115] From an economic standpoint, the membership is indispensable to members because it is their institutional safeguard against opportunism. The membership enables customers to govern the bank which they depend on. In former days, members of cooperative associations depended on one single corporation to obtain credits. Nowadays the customer can choose between several banks. However, precarious relationships have emerged instead.[116] A bank customer who is not an expert in banking operations, for instance, depends on the bank's competence and reliability without being in a position to truly evaluate the quality of the job the bank does on his or her behalf. This is a classic example of a principle-agent-relationship. If the bank misuses its superior position in an opportunistic way, the customer will probably never find out but has to pay the bill. Membership protects customers against opportunism (moral hazard and hold up). In this sense the membership is able to increase the benefits of the customer in a noticeable way. Besides, empirical studies have shown that members are more valuable customers than others because they are loyal.[117] It has been observes that members do more business in several fields with "their" bank than non-members. This is an advantage for both the bank and the customer because both parties save transaction costs of bargaining and monitoring. Finally the membership is a unique position. The possibility to be customer and "owner" of a bank at the same time cannot be imitated by competitors that have different legal forms like stock companies or public institutions. The membership meets all requirements of a core competence. The membership is a unique position that can create competitive advantages. Nevertheless, the above mentioned strengths (1) to (3) of cooperative banks play an important role to complete the core competence.

5.2.3 Member-oriented relationship-management

As illustrated above, the membership can be the core competence of a cooperative bank. That is the theoretical result. In reality, cooperative banks in Germany adapted their strategy to other non-cooperative banks in recent years. It has become difficult to find differ-

114 Recently, the savings banks group has passed its new strategy guidelines. It is very similar to the strategy-paper of the cooperative banking group. It contains an intensified sale of products and services, reduction of costs and an increasing cooperation within the network of savings banks. See DSGV (2002).
115 See section 3.1 supra.
116 See section 4.1 supra.
117 Cf. Hammerschmidt/Hellinger (1998), Greve/Hammerschmidt (2000) and Hammerschmidt (2000).

ences between most of the cooperative banks and savings banks for example. Self-government of members is no longer playing an important role in German cooperative banks.[118] There are no noticeable advantages for most of the members of cooperatives in the banking sector except for an annual dividend.[119] Member-customers and non-member-customers are often treated equally when using the services of the bank.

In order to make membership a core competence, the cooperative bank has to build up a member-oriented relationship-management.[120] This concept is based on relationship-banking models.[121] Empirical studies state that successful banks are investing most of their resources to cultivate the relationship to their clients with the aim of binding them. SÜCHTING recommend relationship-banking particularly to locally-oriented banks with good knowledge about their customers, short lines of decision, flexibility and discretion.[122] As to credit cooperatives, the membership issue has to be moved onto the center stage of the corporate policy. Therefore, the promotion mandate has to be re-interpreted.[123] Presently, there is little room in the competitive banking markets for material promotion in the conventional sense.[124] Cooperative banks are not in a position to be cost-leaders in banking markets, because of their expensive decentralized structures that require a large staff. Moreover, every innovation in products or services will be imitated because of the high transparency of the market. However, the relationship between the bank and its small and mid-sized customers is precarious as explained above. In today's world, small companies[125] are confronted with financial agreements and promotion as well as investment regulations concerning asset values. These financial tasks are so complex that they can only be managed by specialists. Small companies are not able, however, to afford a staff of skilled experts. Therefore they have to rely on the advice of external specialists, banks in most cases, without being able to monitor them. "When relationships are precarious, then the partner's identity counts: what are the norms, values, and traditions to which the bank adheres, and which will guide the bank in its decision when none is around to watch? In this respect, the traditions of the cooperative associations become an invaluable asset."[126]

A bank with a solid capitalistic conception, like the big stock companies, will make different decisions in critical situations than a credit cooperative firmly based upon its tradition. The credit cooperative will not be primarily interested in profit rather than in its clients needs. The cooperative tradition must be cultivated to make the bank trustworthy. Particu-

118 See Bonus/Schmidt (1990), p. 197 ff., Bonus (1994a), p. 47 ff.
119 See Bonus (1994a), p. 122 ff.
120 Cf. Hellinger (1999), p. 296 ff. with further explanations. The strategy-paper of the BVR quotes a "Member-Relationship-Management". See BVR (2001c) p. 4.
121 See e.g. Süchting (1996), S. 263 f.
122 See Süchting (1996), p. 263 f.
123 See Bonus (1994a), who quotes several measures to put this aim into action.
124 Cf. Grosskopf (1990).
125 This argumentation can be applied to private clients, also.
126 Bonus/Greve (1996), p. 298.

larly cooperative banks are able to create trust. One can distinguish between trust in persons, trust in services and trust in systems.[127] Credit cooperatives have advantages in building up trust in persons and in the "cooperative system", whereas trust in services and products can equally be created by every bank.

A good way of making the cooperative bank trustworthy is to strengthen the membership. In order to achieve a "renaissance" of membership in German cooperative banks, membership must become a privilege as it used to be. Credit cooperatives have to make their members feel not only as customers but as partners of the bank. The democratic administration is one of the key factors in this respect. Most of the credit cooperatives in Germany have representatives' assemblies because of the large number of members. In these cases local meetings are necessary to facilitate communication between members and their representatives or bank managers, respectively. Other possibilities to integrate members are advisory boards or expert groups. Also, modern information and communication technologies, e.g. extranets, enable cooperative banks to intensify the exchange of information concerning the corporate policy. In precarious relationships members will trust their credit cooperative if they feel they have their bank under control.

To sum up: The membership can be a core competence of cooperative banks. It meets all basic requirements of a core competence: The membership cannot be imitated by the competitors. The trusting relationship between the cooperative bank and the member can create transactions in several business segments (cross-selling). Last but not least, members can save transaction costs of bargaining and monitoring. These savings are a additional benefits for the members. A member-relationship-management is an adequate strategy to ensure that membership gets the status of a core competence.

5.3 Structure

5.3.1 Strategic networks

Back to the triad "strategy, structure and core competencies". As pointed out above, a competitive *core competence* of cooperative banks in Germany can be their specialized knowledge and their experience in dealing with their members. A suitable *strategy* is a member-relationship-management.

Now we have to analyze whether the existing *structure* of the German financial cooperatives fits with this strategy. As mentioned above, cooperative banks in Germany are part of a complex network together with regional and central banks, specialized enterprises, and

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[127] See Luhmann (1989), p. 40 ff.

associations.[128] A network is a hybrid structure that is located between the arm's-length transaction of markets and the hierarchy in firms.[129] "Corporate networks are a long-term arrangement among distinct but related for-profit organisations. As such, they are an organisational form between markets and hierarchies. Compared to markets, a network has more structure, produces more interaction among the network organisations, provides "thicker" information channels, demands more loyalty, exhibits more trust, prefers voice to exit, and puts less emphasis on prices. If compared to hierarchies, a network is somewhat underorganised, due to the loose coupling of the network organisations and due to the open boundaries of the network itself."[130]

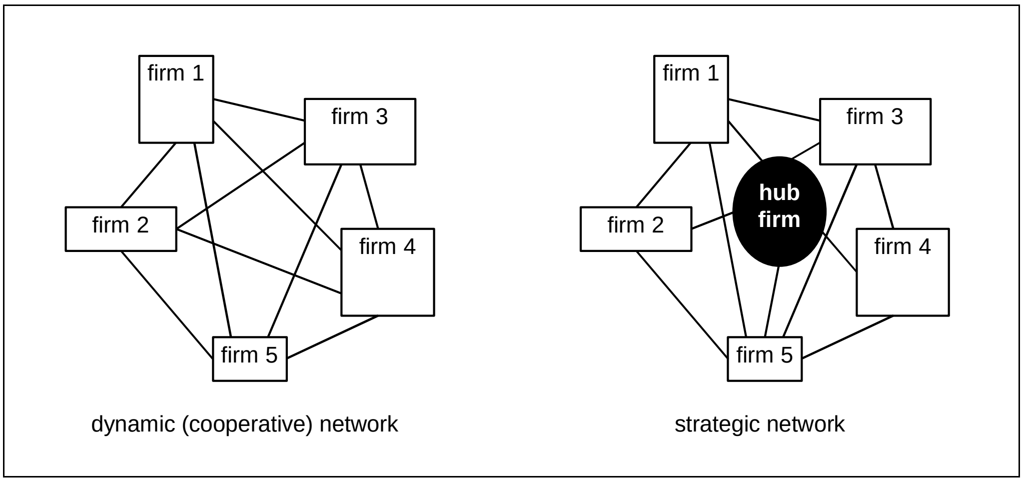

Figure 2: Dynamic (cooperative) networks and strategic networks
Source: Following SYDOW/WINAND (1998), p. 14 and 19,
GREVE/POLSTER (2000), p. 202 and GREVE (2002).

Networks can be subdivided into internal networks, dynamic networks and strategic networks (cf. figure 2).[131]

- *Internal networks* are enterprises that are organized in a modular manner. They are the result of modularization of former hierarchically organized enterprises or of acquisitions. Modularization is defined as the restructuring of organizations into smaller units that have own decentralized competencies and are responsible for their profits, e.g. profit center or fractal organizations. The coordination of the modules is not hierarchical but resembles the market mechanisms. Internal networks are *intra*organizational, whereas dynamic and strategic networks are a *inter*-organizational form of cooperation.

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128 Cf. Hellinger (1999), p. 33 ff. and Greve/Polster (2000), S. 206 ff.
129 Cf. Williamson (1991), p. 281.
130 Sydow/Windeler (1993), p. 193.
131 Cf. Miles/Snow (1986), p. 64, Snow et al. (1992), Fleisch (2001), p. 74, Picot et al. (2001), p. 14, 273.

- Following MILES and SNOW *dynamic networks* can be described by four characteristic features: Vertical disaggregation, market mechanisms, a broker and a full-disclosure information system.[132] Dynamic networks are a result of vertical disaggregation. Business functions such as research and development, production, marketing and distribution are performed by independent organizations within the network. The process of vertical disaggregation is described in the management literature as "outsourcing"[133]. Resources that are not core competencies of the firm are taken out of the organization and are offered by partners in the network. The functions within the business group are carried out mainly through market mechanisms. Since each function is performed by different organizations, a broker takes the order and subcontracts for services required. The broker bundles up the partial services and gets in touch with the clients. Full-disclosure information systems are used as substitutes for lengthy trust-building processes based on experience in a dynamic network so that contributions of each participant can be mutually and instantaneously verified. An example of a well-known dynamic network is the virtual organization, i.e. a project oriented ad-hoc formation of teams or value chains.[134]

- A *strategic network* is a long-term institutional arrangement among distinct but related for-profit organizations that is based upon an extensive interfirm division of labor and intensive interfirm cooperation, and – as opposed to other types of interfirm networks – is led by a center or hub firm.[135] This organizational form that combines in an intelligent manner elements of market and hierarchy, either results from intensified cooperation among interdepent firms (quasi-internalization) or from outsourcing of functions and activities (quasi-externalization).[136] In contrast to other forms of inter-organizational networks, strategic networks have hierarchical elements, above all a strategic center: "Essential to this concept of strategic network is that of "hub firm", which is the firm that, in fact, sets up the network, and takes a pro-active attitude in the care of it".[137] In the literature, strategic networks are often compared with other forms of strategic cooperation such as Japanese Keiretsu, Supply Chain Management or franchise agreements.[138]

Dynamic networks can also be described as "cooperative networks"[139] because command within the group is *from the bottom to the top*. Strategic networks are diametrically opposed to cooperative networks. In strategic networks command is *from top down*. The co-

132 See Miles/Snow (1986), p. 64.
133 Outsourcing comes from „**out**side re**sourc**e us**ing**". See e.g. Koppelmann (1996), p. 2.
134 See e.g. Bultje/Wijkt (1998) and Göransson/Schuh (1997).
135 See Jarillo (1988), p. 32 and Sydow (1992), p. 78.
136 See Sydow (1992).
137 Jarillo (1988), S. 32.
138 See e.g. Fleisch (2001), p. 78.
139 Cf. Polster (2001), p. 263 f., Greve (2002) and Fischer (2002).

operative banking group in its initial structure can be classified as a cooperative network. However, the command within the group gets increasingly centralized in recent years.[140] The cooperative banking group is on the way to get a strategic network. It depends on the organization of the hub firm, whether local acting cooperative banks hold onto the command within the network.[141]

5.3.2 The division of labor within the cooperative banking network

Following the above mentioned definitions of networks, the cooperative banking group can be identified as an interorganizational network because legally and mostly economically cooperative banks collaborate within the network. The central banks, the specialized corporations and the associations are only a means to an end. These central units have been created by credit cooperatives in order to exploit the advantages of size without foregoing the advantages of smallness.

Outsourcing plays an important role within networks. Therefore, we have to determine which partner within the network has to take on which function. In other words, the "boundaries of the firm" of the cooperative banks and their partners within the network has to be determined. Moreover, institutional safeguards are indispensable to protect the specific quasi-rents emerging from dependence within the network. As explained above, PICOT and HARDT developed a possibility to determine the horizontal and vertical boundaries of a firm by combining the core competence approach and transactional cost economics. Depending on the degree of two criteria, "specificity" and "strategic importance", they differentiate between core competencies, complementary competencies and peripheral competencies of a corporation and give organizational advice. In contrast to PICOT and HARDT, we will use the criterion "precariousness" instead of "specificity" because "precariousness" combines both consequences of opportunistic behavior, "specificity" and "plasticity" (cf. figures 3 and 4).

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140 See section 5.1.2 supra.
141 See section 6 infra.

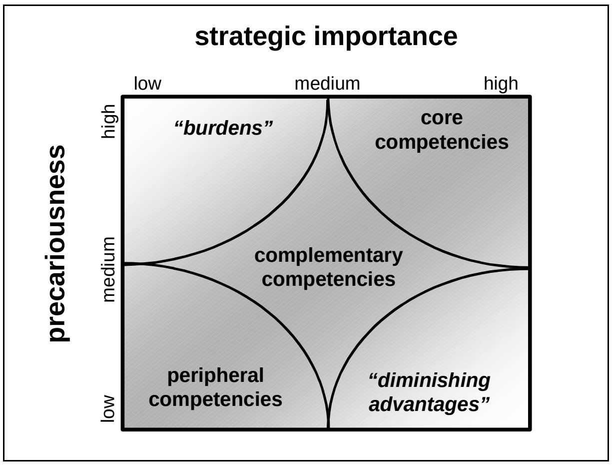

Figure 3: Competencies within the precariousness-strategic importance-portfolio
Source: Following PICOT/HARDT (1998), p. 632 and POLSTER (2001b), p. 10.

Core competencies are strategically important and require resources that are specific or plastic to a high degree.[142] They have to be integrated into the boundaries of the firm ("*make*"). If strategic relevance and precariousness are only at a medium level, hybrid organization forms are advisable ("*cooperation*"). These functions are called *complementary competencies*. Depending on the degree of fulfillment of the criteria the institutional answer could vary from joint ventures to long-term contracts. *Peripheral competencies* are standardized; they are not of strategic importance and the risk of hold up and moral hazard is low. Therefore, they can be bought on markets ("*buy*").

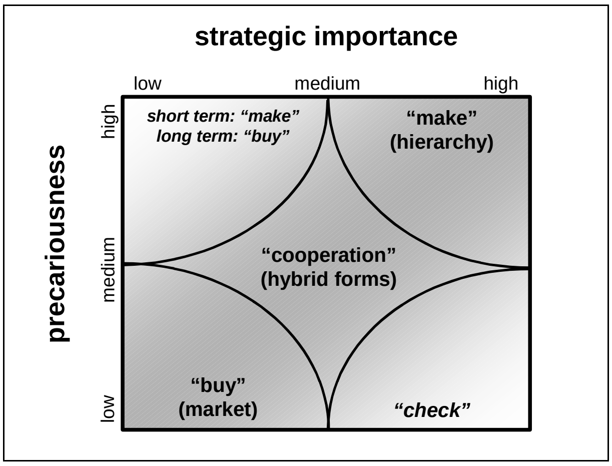

Figure 4: Institutional forms within the precariousness-strategic importance-portfolio
Source: Following PICOT/HARDT (1998), p. 633 and POLSTER (2001b), p. 11.

This organizational advice, however, is not static. A change in general settings, e.g. information and communication technology, know-how, law or competition, is able to alter the

142 See Picot/Hardt (1998), p. 631 f.

strategic importance or the precariousness of functions and resources.[143] Hence, "burdens" and "diminishing advantages" emerge. "*Burdens*" are characterized by their low strategic importance and high precariousness. They should be carried out within the corporation in the short run, but in the long run they have to be turned into peripheral competencies, e.g. by standardizing the underlying functions, so that they can be carried out on markets. "*Diminishing advantages*" are highly important strategically but the risk of opportunism caused by specificity and plasticity is low. If the risk of imitation of this competence is high the corporation should decrease its strategic relevance in order to turn it into a peripheral or complementary competence.

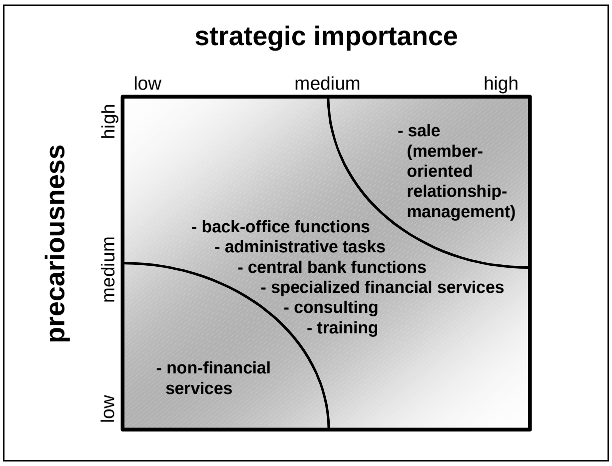

Figure 5: Division of labor within the cooperative banking network
Source: Similar HELLINGER (1999), p. 339 and POLSTER (2001b), p. 11.

According to this concept, we can explain the current situation of the division of labor within the cooperative banking group (cf. figure 5).[144] Sale is the main task of the locally acting cooperative banks. Membership is their core competence and an adequate strategy is the member-oriented relationship-management. Complementary competences with medium strategic relevance and precariousness should be carried out by central banks, associations, and specialized institutes within the network. Back-office functions, administrative tasks and other functions (e.g. refinancing and investment options, joint loans, securities transactions, money and foreign exchange trading, payment transactions) have to be offered by central banks, such as the WGZ-Bank or the DZ BANK. Mortgage loans, asset management, insurances etc. are complementary competencies that should be delegated to specialized corporations within the network. Besides, the consulting of the cooperative banks as well as the training are functions that are precarious and strategically important to a certain degree. The regional cooperative associations are assigned to offer these functions. Only non-financial services, e.g. facility management, cleaning and guarding ser-

143 See Picot/Hardt (1998), p. 631.
144 See Hellinger (1999), p. 229 ff. with further explanations.

vices, the vehicle fleet, materials management, can be bought on markets without a further institutional safeguard because their strategic importance and precariousness is low. These services can be classified as peripheral competencies.

6 The cooperative banking group as a strategic network – implications

The cooperative banking group is one of the oldest networks in the German economy. Its origins date back to the middle of the 19th century. Along with change in general settings, the institutional structures have been developed further. The next step could be to create a strategic network of cooperative banks. In the following, some implications of this institutional change will be pointed out.

(1) The broker

The broker plays an important role within a network. It is a central characteristic of networks that every partner does what he can do best; he concentrates on his core competencies. The broker has the function to represent the network to the customers. Therefore, he has to guarantee for the performance of the network. In the case of the cooperative banking group, the locally acting credit cooperatives take over the role of the broker of the network. [145] From the customers' point of view the cooperative banks are the closest link of the financial value-adding process. Since their core competence is relational-banking they are predestined for the role of the broker.

Cooperative banks carry out their brokering activities in a complex financial network. They have to play the part of an "information navigator" who shows the way through the "jungle" of financial services.[146] In this context, credit cooperatives have the function to bundle up the differentiated products and services of the cooperative financial network. For this activity it is especially important to consider the specific circumstances of every customers' life. Credit cooperatives have the advantage to possess a lot of information about their customers. The cooperative bank ideally supports their customers during their whole life, literally spoken "from the cradle to the grave". This can only be the case if the customer trusts in the cooperative system that protects him against opportunism in precarious relationships. In this respect, a cooperative bank can be called a "network-navigator".[147]

(2) Size

The optimal size of a (cooperative) bank is difficult to determine.[148] According to the findings explained above, the cooperative bank should not be too big, otherwise the member-

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145 See Bonus et al. (1999), p. 40 ff.
146 Cf. Hellinger (1999), p. 334 f. and Bonus et al. (1999), p. 42 with further references.
147 See Bonus et al. (1999), p. 42.
148 See e.g. Tebroke (1989).

oriented relationship-management cannot be realized.[149] This strategy gives a human touch to the bank-customer relationship and is in line with geographically restricted business districts. A very favorable factor is that the credit cooperative does not need to be very big because most of the products and services it offers are provided to them by their network partners. In order to bundle up information and create an individual set of financial products the cooperative banks do not need to be large units. Therefore, mergers are oftentimes not favorable. With regard to the extended core competence approach that was explained above, a merger is useful if the core competence of one cooperative bank should become a core competence of another bank. However, if a bank wants to employ complementary competencies of another bank, a cooperation between cooperative banks with neighboring business districts or a more sophisticated cooperation with the central units of the network would be the right institutional reaction.

If mergers are motivated by the removal of competition among cooperative banks on local markets, however, they can be reasonable because they strengthen the forces of the cooperative banks involved.[150] Yet, if a merger strategy is followed, the dependency between the cooperative bank and its customers must be safeguarded by effective institutional structures. Therefore appropriate self-government structures are required.

In reality, however, it seems that these findings are not known at all. In recent years, mergers are not only motivated by the reasons that are mentioned above. According to an estimation of the BVR, in 2010 only 800 cooperative banks with an average balance-sheet total of about 1 billion Euros will remain in Germany. The number of branches will be reduced from 16,000 to 10,000 in order to drive down costs. The process of concentration is already in full swing. From 1999 to 2001, mergers have reduced the number of local cooperative banks in Germany from 2,035 to 1,621, which is a decrease of 20.3 percent.[151] During the same period, the number of branches has decreased at a lower rate from 15,793 to 14,584 (7.7 percent).[152] However, the aim of a minimum-size of 1 billion Euros balance sheet total for cooperative banks has not been reached yet. At the end of 2001, only 94 cooperative banks (5.8 percent) in Germany had exceeded this limit.[153] 1.013 cooperative banks (62.5 percent) even had a balance sheet total significantly lower than 250 million Euros at the end of 2001.[154]

149 See Bonus et al. (1999), p. 42 f. and p. 51.

150 Cf. the motto of the BVR strategy-paper „one (local) market – one bank" in BVR (1999) and BVR (2001c). See also Bonus et al. (1999), p. 51.

151 See Deutsche Bundesbank (2002), p. 104.

152 See Deutsche Bundesbank (2002), p. 104.

153 Without the cooperative banks, that are not represented by the BVR (Sparda-Banken, PSD-Banken and specialized cooperative banks) the number decreases to 72. See BVR (2002), p. 104.

154 Without the cooperative banks, that are not represented by the BVR (Sparda-Banken, PSD-Banken and specialized cooperative banks) the number diminishes to 1.011. See BVR (2002), p. 104.

(3) Products

In recent years, credit cooperatives have developed a portion of their products by themselves in order to be able to offer a wide range of products and to differentiate themselves from competitors. If the cooperative banking group wants to continuously develop towards a strategic network, standardization of products is indispensable.[155] Due to the growing complexity and the decreasing transparency of financial markets, it is difficult for customers to oversee and evaluate the variety of products. In order to build up trust it is crucial to create a standardized range of high-quality products that the customer will identify as the trade mark of the cooperative banking network. Positive experiences combined with the effect of recognition lead to a high consumer trust. The trust in services is the first step towards trust in the system "cooperative bank". Hence, a standardized range of products supports the common appearance of the cooperative financial network in markets. Besides, the standardization leads to cost savings because redundant work can be avoided. For these reasons, the cooperative financial group has established a centralized unit that bundles up the development of the products of the whole network.[156]

(4) Outsourcing

In order to develop a strategic network, the cooperative banking system has to optimize their division of labor. POLSTER pointed out that there still is potential for outsourcing activities within the cooperative banking group.[157] He differentiate between three value-adding activities of financial services, i.e. sale, risk management and production. According to their degree of strategic importance and precariousness he characterizes sale as the core competence, risk management as the complementary competence and production as the peripheral competence of cooperative banks and deduces the accompanying institutional solutions ("make", "cooperation" or "buy"). In reality however, risk management is not only carried out by partners within the group but also by cooperative banks themselves. Besides, production is not carried out on markets but also by cooperative banks themselves, central banks and other corporations within the group. These theoretical findings are considered in the BVR strategy-paper[158] and in a recent initiative of the WGZ-Bank. [159] Yet, it relegates to legal provisions that prevent banks from sourcing out more functions.[160]

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155 See Bonus et al. (1999), p. 44 f.

156 See BVR (2001a), pp. 36-39 and (2001d) and BVR (2002), p. 26.

157 See Polster (2001), p. 19 f.

158 See BVR (2001c), p. 15 ff. One example of outsourcing is the "Bank für Wertpapierservice und -systeme" (in short: bws-Bank AG). The cooperative central banks founded it in the year 1998. The bws-Bank is a typical example for a production-bank. It offers all trust banking services around securities brokerage. It handles all responsibilities relating to securities transaction, portfolio management, deposit and settlement.

159 The regional central bank WGZ-Bank plans to strengthen the cooperation with their member banks. It offers their member banks to take over some administrative tasks (back office) in order to enable local

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(5) Hierarchy and hub firm

Now, we have to answer the question how much leadership is needed within the cooperative financial network. As mentioned above, strategic networks need a center or hub firm. The function of the hub firm can be explained on the basis of franchise agreements, for example.[161] Franchise systems are characterized by two features: (1) Franchise systems have a uniform brand name, and (2) the franchisor has extensive rights to monitor the franchisees and to impose instructions to them.

1. A crucial asset of a franchise system is the uniform brand name and its reputation, e.g. the golden “M” of McDonald’s. Customers often do not recognize that franchise units are economically independent corporations because of their uniform look. The uniform brand name is a valuable asset because it supports the reputation of the whole group. Positive experiences with one of the units of the network will be transferred to the other units and vice versa. The brand name stands for a certain quality of the whole network. If a single franchisee reduces the quality with the aim to save money, this free rider-behavior could have a negative (external) effect on the reputation of the whole franchise system.[162] Such persons are called “free riders” because they do not have to bear the negative consequences of their actions which affect the group as a whole. Therefore, the “brand name capital” has to be protected against devaluation by “black sheep”. In this respect, the relationship between the franchisor and the franchisees is precarious in both directions.

2. The resulting dependency can be integrated by complex contracts or a democratic constitution[163]. In the case of franchising, the detailed franchise contract prevents the franchise system from opportunism. It is the franchisor task to guarantee a good reputation. He has the right to monitor and to sanction “black sheep” with the aim of safeguarding the brand name capital.

Within the cooperative banking group mechanisms are similar. The cooperative banks in Germany have a common brand name, too. They use a uniform trade mark, most of them call themselves “Volksbank” or “Raiffeisenbank”, and they carry out joint advertising on television or in magazines. In the case of franchise systems, the franchisor ensures a certain quality of products or services in order to protect the brand-name capital of the whole sys-

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banks to concentrate their forces on their core competence, the relationship-management towards members and customers. See WGZ-Bank (2002).

160 See BVR (2001c), p. 15.

161 Cf. Miles/Snow (1984), p. 26, Sydow (1992), p. 29 ff. and Sydow (1998), p. 124 ff.

162 If a single franchisee spends less money on the common brand name (e.g. reducing expenses for common advertising) or even changes its name or brand figure to differentiate from other cooperative banks, the brand name capital will be decreased, too.

163 Miles/Snow (1995), p. 7 ff., give an example of a network with a democratic constitution that is protecting dependencies against opportunism.

tem. Cooperative banks have chosen another way to prevent their network from opportunism. Their strategy is to create a democratic constitution that is based on interlocking capital arrangements.

In this respect, the cooperative financial network is not a classic strategic network because the cooperative banks take up the position of the hub firm. Whereas in the case of a franchising system command is top down, in the case of the cooperative banking network it is bottom-up.[164] The "leader" of the cooperative banking network is not a sovereign like the franchisor but a democratic government. The government is legitimized because the cooperatives bind themselves to decisions made within the network. The basic constitution is based on institutional structures: The capital of the central banks and the specialized companies is mainly held (directly or indirectly) by the cooperative banks.

In recent years, the continued development of the cooperative banking group was hampered by the autonomy of cooperative banks. Decisions that were made in the general assembly of the BVR were not put into action by all cooperative banks in most cases. However, in order to exploit the advantages of a strategic network, decisions require a certain binding force. A solution could be a democratically legitimized "parliament of local cooperative banks".[165] For example, the cooperative Rabobank-Group in the Netherlands is structured this way.[166] Every cooperative bank is able to influence the strategy of the network through democratic means. However, when a decision is made it has to be put into action even if some cooperatives have a differing opinion with the aim of strengthening the network as a whole. The direction of command would be "bottom-up" as before, but the decisions would be more binding. The "parliament of cooperative banks" could be the hub firm of the strategic network. In other words: The role of the strategic leader and planer can be played by a federation with democratically decided democratic rules of consultation and voting once it has been given the role to do just that. The federation can compile the strategic initiatives coming from the primary cooperative banks.[167]

(6) Risk management

External effects within the cooperative banking group also emerge, if a single cooperative bank is involved in risky transactions, e.g. loans or dealings in equity. If the high-risk transaction comes to a good end, the cooperative bank reaps the benefit on its own. If the transaction leads to bankruptcy, the deposit guaranty fund of the cooperative banking group will bear the losses. If the affected credit cooperative cannot be revitalized, it is merged

[164] See section 2 supra.
[165] Cf. Bonus et al. (1999), p. 46, Thiemann (2000), p. 163.
[166] See Zakostelsky/Hagspiel (1999), Disselbeck (1999) and Polster (2001), p. 338 ff. for further information.
[167] See Fischer (2002).

with a neighboring cooperative that is in a sound financial position. These safeguarding mechanism are established in order to avoid a loss of reputation due to a bankruptcy. The problem is that the "black sheep" is not confronted with the negative consequences of its action. The cooperative banking group in Germany has realized this problem and is on the way to reform their deposit protection scheme. The draft of the new deposit protection scheme intends to group the cooperative banks into four categories (A-D) depending on the degree of risk of their business. According to the classification and some special rules, cooperative banks have to pay a certain contribution to the deposit guaranty fund.

The contribution that is to pay into the deposit guaranty fund by the credit cooperatives is depending on the classification and some special rules. This reform improves the incentives of banks to avoid high-risk transactions.

(7) Competition

The network-theory underlines the importance of competition within networks.[168] Competition is based on redundancy, i.e. similar functions are offered by a number of corporations. Redundancy ensures safeguards (in contrast to dependency), flexibility (in contrast to stability), competition (in contrast to cooperation) and learning and innovation (in contrast to backward steps).[169] Competition is a process of discovery.[170] If cooperative banks have the opportunity to choose between a number of suppliers of complementary competencies, the incentives to lower costs and to increase quality are higher than without competition within the network.[171]

In reality, the German cooperative banking group does not allow for competition. On the contrary, it insists upon "Verbundtreue", i.e. loyalty in relationships between cooperative banks and central institutions within the network with the aim of bundling up their business and realizing economies of scale and scope.[172] There is only one sector, the mortgage loan sector, that allows for competition within the network. Mortgage loans are offered by three suppliers, but their merger is already in discussion. The problem is that cooperative banks will become dependent on the monopolistic suppliers without having a redundancy of activities and suppliers. It is difficult to weigh the positive effects of independency in the case of redundancy and against cost savings in the case of "Verbundtreue".

Some cooperative banks are dissatisfied, because they are expected to buy from the suppliers of the network only, but the suppliers not only sell their products via the cooperative

168 See e.g. Sydow (1992), p. 83 ff.
169 See Bonus et al. (1999), p. 36.
170 See von Hayek (1969), p. 249 ff.
171 See Bonus et al. (1999), p. 52.
172 Cf. BVR (2001a), p. 28 and Pleister (2000), p. 56.

banks but also directly to customers by using their own agents. This is a offence against the principle if subsidiarity. Moreover, some suppliers charge higher prices to cooperative banks than to direct customers or pay lower commissions to cooperative banks than to other salesmen. If the loyalty is to exist at all, it has to take effect in both directions, from the cooperative towards the central institutions *and* from the central institutions towards the cooperative banks.[173]

If most of the cooperative banks agree upon the absence of competition within the network, the importance of institutional safeguards increases. Most of the cooperative banks in Germany have realized this connection. In order to increase their influence, the credit cooperatives demand to hold more shares of the central institutions and to send more representatives into the supervisory boards of the central institutions. This aspect is discussed in the new strategy-paper of the BVR.[174] The first step in this direction is the appointment of an ombudsman[175] at the DZ BANK who has the function to settle litigation issues between cooperative banks and the DZ BANK.[176]

173 Direct selling of central institutions with specialized products is not against the principle of subsidiarity if the local credit cooperative agrees with it because the bank has not enough staff to ensure a sufficient sale of specialized products in its business area for example.

174 See BVR (2001a), p. 52 and (2001e).

175 The ombudsman is called “verbundpolitisch Beauftragter”. See DZ BANK (2002b), p. 8 and 9. For an economic interpretation see Theurl/Kring (2002), p. 59.

176 An ombudsman is a institutional safeguard that refers to a “neo-classical contract”. Although the cooperative banking network is based on a “relational contract” that is usually used for long-term cooperation, an ombudsman could strengthen the governance structures of networks in addition. See MacNeil (1978), p. 865-886.

7 Summary

According to institutional economics, credit cooperatives and the cooperative banking group can be interpreted as hybrid organizational forms (cooperation). The relationship between customers and the cooperative bank on the one hand, and between the cooperative banks and the central units within the group on the other hand can be called precarious because dependencies can be uses in an opportunistic way. Hybrid organizational forms have been established to solve hold up and moral hazard issues that are caused by opportunistic behavior. The institutional devices of the cooperative banking group have to be adapted on the changing general settings. Nowadays, as in the past, the core competence of cooperative banks in Germany is the membership that ensures dependability in precarious relationships. The suitable strategy is a member-oriented relationship-management. A structure in line with this strategy can be a strategic network. In order to continuously create a strategic network the cooperative banking group has to modify its institutions. Some of the required measures correspond to the latest strategy-paper by the central association of the German cooperative banking system. The institutional change is already in full swing.

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