Chapter 1

THE SPECULATIVE MANAGEMENT OF CORPORATE RESTRUCTURING: INTRODUCTION AND OVERVIEW

Speculators may do no harm as bubbles on a steady stream of enterprise. But the position is serious when enterprise becomes the bubble on a whirlpool of speculation. When the capital development of a country becomes a by-product of the activities of a casino, the job is likely to be ill-done.

—John Maynard Keynes, writing on the problems with U.S. financial markets versus the less speculative British market[1]

As managers of a fund, we have an urgency. We are not short-term traders, but the urgency is still there. We have this burning in our stomach every day. It doesn't mean you buy and sell the businesses every day. But you constantly evaluate your investment, and the urgency is always there to hold management accountable for performance.

—Michael Price on the urgency of institutional investors[2]

You can't measure success by the interests of multiple stakeholders. You can measure success by how the shareholder fares.

—Albert J. Dunlap, CEO of Scott Paper and Sunbeam Corporation, on shareholder interests

I'm a great believer in predators.

—Albert J. Dunlap, CEO of Scott Paper and Sunbeam Corporation

That's another six hundred million. So we made a billion dollars on Sunbeam with no risk.

—Michael Price, institutional investment manager whose fund owns 20 percent of Sunbeam

[Dunlap] is persuading others that shareholder value is the be-all and end-all. But Dunlap didn't create value: He redistributed income from the employees and the community to the shareholders.

—Peter D. Capelli, Chair of Management Department at the Wharton School of the University of Pennsylvania[3]

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In the fall of 2001, the stock price of Enron, America's seventh largest corporation, collapsed amid reports of deepening accounting irregularities, fictitious profits, shredded audit documents, and the suspicious suicide of a key executive. Enron struggled to avoid bankruptcy but failed. Arthur Andersen, Enron's Big Five auditor, failed as well. Enron and its most important trading partners, Dynergy, Reliant, and CMS Energy, were found to have engaged in sham accounting, including the booking of "round-trip swaps" to inflate revenues and earnings by as much as $4 billion. Congressional hearings were held after the stocks of Global Crossing and WorldCom plummeted as accounting irregularities were discovered. The widening scandal underscored an uncomfortable change in U.S. capitalism: deft manipulation of stock prices and accounting figures have displaced the efficient management of industrial production as the central concern of U.S. corporate executives.

This book chronicles changes in U.S. finance that increased the power of the stock market over corporate life, diverting focus from production to *speculative management*, the control of corporate actions and results to raise the trading price of corporate shares. This book describes how the speculative logic of the stock market was transmitted through the mediation of financial accounting, the business media, and corporate governance to encourage the dramatic restructuring of America's largest corporations in the late twentieth century. Corporate change in recent times, from hostile takeovers in the 1980s, to downsizing of U.S. firms in the early 1990s, to the spectacular failures of Enron, WorldCom, and Global Crossing in the early 2000s, was closely bound to speculative trading in equity securities. Speculative management cuts across and deepens understanding of this broad spectrum of corporate change. The study's empirical focus is the episode of downsizing and corporate restructuring that peaked in U.S. corporations in the early 1990s. We begin with the consideration of a prominent example: Sunbeam Corporation.

CORPORATE RESTRUCTURING AT SUNBEAM CORPORATION

Like thousands of other workers in the 1980s and 1990s, employees of two Sunbeam Corporation factories, one in Bay Springs, Mississippi, and the other in McMinnville, Tennessee, learned in the winter of 1996 to 1997 that their plants were to be closed in a corporate restructuring.[4]

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The factory in Bay Springs (pop. 2,200) manufactured wire assemblies for electric blankets and, although small, employing only 125 workers, was efficient and profitable. The workers in this plant were the kind that American management had dreamt of during the preceding two decades: workers who were nonunionized, compliant, hardworking, and satisfied with modest wages (many worked for less than $10 per hour). One 30-year veteran of the factory described life within the plant in community terms: "It was a wonderful place to work. I had good supervisors and good coworkers. To me, that plant was like one big family. I guess I spent more time there than at home. The plant had been good to me" (Byrne 1999, p. 123).

The product made in the plant, "positive temperature coefficient" wire that allowed electric blankets to adjust automatically to the temperature of the user's body, was in high demand. Because of the advantages of the wire made in Bay Springs, Sunbeam dominated the electric blanket market in the United States. Workers in Bay Springs skillfully and efficiently produced a critical component for one of Sunbeam's core products and, in the winter of 1996, could have reasonably expected to continue doing so.

Workers at Sunbeam's factory in McMinnville (pop. 11,000) also had good cause to expect continuing employment. This plant employed 700 workers in the production of Oster hair clippers. The majority were sold in retail stores, but the most profitable line was sold to professional barbers and pet groomers. The plant was one of the best in the Sunbeam portfolio. It ran virtually nonstop and at a high profit. Production was quite high: the plant produced 3.3 million retail clippers in 1996 (15,000 a day), as well as 375,000 professional trimmers and 1.2 million replacement blades (Byrne 1999, p. 129).

The McMinnville plant boasted profit margins on its products that were higher than other Sunbeam products: 38 percent margins on the retail clippers, 50 percent margins on the professional clippers, and 65 percent margins on replacement blades. In all, the plant earned $40 million a year on sales of $110 million. The Sunbeam marketing executive who was responsible for selling the clippers this factory produced characterized it thusly:

> The McMinnville facility was just a jewel. Many of the people in the assembly area had been doing their work for twenty-five or more years. They could do their jobs with their eyes closed. . . . They had a

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> wonderfully committed workforce. The employees had tremendous values. . . . They had flexible production. If there was a surge in demand, they knew how to deliver. (Byrne 1999, p. 135)

Byrne indicates that workers and staff at both factories expressed shock at the news of their impending closure. Both of the plants seemed well run and productive if not completely aligned with the "lean and mean" corporate rhetoric of the times. But, like hundreds of other facilities, managers conspicuously committed to production efficiency and profit closed them.

The restructuring plan that affected these plants was one of the most extreme reorganizations of the late twentieth century, calling for the removal of fully half of the corporation's staff and workers. Sunbeam's chief executive officer (CEO) Albert Dunlap, whom the media nicknamed "Chainsaw Al" for his famously ruthless reorganizations of other firms, announced the restructuring from Sunbeam's Delray Beach, Florida, headquarters. The restructuring was planned like the "invasion of Normandy," Dunlap was quoted as saying in the *Wall Street Journal*, which reported the details of the plan:

> In an effort to improve the fortunes of the ailing consumer-products company, whose reins he took as chairman and chief executive officer in July [1996], Mr. Dunlap said he would eliminate fully 50 percent of the company's 12,000 employees; sell or consolidate 39 of its 53 facilities, including 18 of its 26 factories and 37 of its 61 warehouses; divest several lines of businesses; eliminate six regional headquarters in favor of a single office in Delray Beach, Fla.; and scrap 87 percent of Sunbeam's products. [Dunlap says the plan] would save the company $225 million a year starting in 1998. He said Sunbeam would exit the businesses of making furniture, clocks, scales and decorative bedding.[5]

The plants in Bay Springs and McMinnville were 2 of the 18 factories that were to be closed as part of Sunbeam's restructuring plan. The plan called for the transfer of the production line of the Bay Springs factory, which produced components for electric blankets, to the final assembly plant in Waynesboro, Mississippi, yielding a projected savings of $200,000 in annual transportation costs. The production of the McMinnville factory was to relocate to a Sunbeam blender and waffle-

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iron plant in Mexico City, a move projected to reduce costs by $28 million annually (Byrne 1999, p. 133).

The downsized employees of Sunbeam Corporation had plenty of company. The late twentieth century in the United States was a period of extensive, painful industrial reorganization. One-third of the 500 largest U.S. industrial firms in 1980 ceased to exist as stand-alone companies by 1990. Employment at the 500 largest industrials fell by 25 percent during this time, from 16 million to 12 million, and half of their total products were eliminated (Useem 1996, p. 2).

During the last two decades of the century, virtually every major corporation in the United States restructured its operations. Like Sunbeam, many of these corporations initiated layoffs, plant closures, and contract renegotiations. Consultants were hired to help "turnaround managers" eliminate layers of management and "reengineer" work processes. Corporate managers presented their reorganizing plans and results to the business community, which alternately celebrated and condemned these actions. Business discourse critical of restructuring often emphasized the destruction it occasioned. But proponents claimed creative consequences. The enhanced competitiveness, long-term profitability, and efficient growth of lean, mean, reorganized firms redeemed the destructive process. As a whole, business discourse wrapped corporate restructuring in a legitimating rhetoric of competitiveness and efficiency.[6]

A best-selling business book of the early 1990s, Michael Hammer and James Champy's (1993) how-to guide to corporate restructuring, *Reengineering the Corporation: A Manifesto for Business Revolution*, justified restructuring as a necessary response to intensively competitive global product markets:

> With trade barriers falling, no company's national turf is protected from overseas competition. When the Japanese—or Germans, French, Koreans, Taiwanese, and so forth—are free to compete in the same markets, just one superior performer can raise the competitive threshold for companies around the world. . . . If a company can't stand shoulder to shoulder with the world's best in a competitive category, it soon has no place to stand at all. (P. 21)

Global competition sharply affected the consumer appliances industry in which Sunbeam operated for several reasons:

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> [In] few industries is competition more Darwinian than in small appliances. The barriers to making toasters and irons are low. Technological innovation is quickly knocked off by a host of competitors here and in low-labor-cost nations like China. Pricing power is almost nonexistent in a retail environment dominated by giants like Wal-Mart. Even breakthrough items, such as breadmakers, quickly become low-margin commodities.[7]

Cutting costs to compete in such a world was the rationale that Sunbeam's Dunlap communicated to analysts and the business media. Dunlap argued that cost structure was Sunbeam's major problem. Two days after taking over as head of Sunbeam, Dunlap fired one of his rivals for the job and held a conference call for analysts to assess blame and outline strategy:

> After a two-day review of operations, Mr. Dunlap diagnosed Sunbeam as having excess capacity, high costs and irrational product lines. He said that while the company had strong brands and some solid products, it built new production capacity based on sales growth that never materialized. "We've got too many people, too many products, too many facilities and too many headquarters," Mr. Dunlap said during the conference call. He said management teams will start studying the operations more closely on Monday and begin announcing specific changes. . . . "We're going to look at everything," he said. Mr. Dunlap plans to centralize the company's sprawling divisions and offices, which now remain largely autonomous. "[Autonomy] is nonsense," he said. "The last thing we need is for people to be setting up empires."[8]

And so Sunbeam joined the ranks of major U.S. corporations that implemented drastic restructuring programs. Although painful to local communities and workers, restructuring held out the promise of gains for the surviving company, its managers, and its owners. In the legitimating rhetoric of restructuring's proponents, restructuring improves production efficiency, product quality, and profits in an era of tough global product market competition; restructuring is possibly the only way for U.S. industry to survive. In business discourse of the late twentieth century, restructuring might be ruthless, but it was definitely good production management.[9]

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Corporate restructuring meant different things at different points in the late twentieth century.[10] Business media emphasized plant closings and deindustrialization in the 1970s and early 1980s, takeovers in the late 1980s, and downsizing and reengineering in the 1990s. Deindustrialization crystallized as a coherent corporate strategy in the early 1980s (Bluestone and Harrison 1982).[11] Deindustrialization generally involved disposal or divestment of "noncore" lines of business. Production facilities U.S. corporations owned in the industrial Northeast and Midwest were closed and production shifted to new factories built in the southern United States, Mexico, South America, and Asia to exploit low-wage rates in those regions.

In the technical jargon of the academic finance literature, deindustrialization was a form of asset restructuring whereby a corporation strategically exited lines of business and entered others, changing the portfolio of businesses under corporate control (Donaldson 1994, Rock and Rock 1990). Although asset restructuring changed a firm's portfolio, capital restructuring altered the firm's capital structure, often by increasing the financial leverage—ratio of debt to equity—of the firm. Debt for equity swaps, stock repurchase plans, leveraged buyouts (LBOs), and leveraged recapitalizations redistributed cash to shareholders and forced the firm's management to deploy assets more efficiently. Capital restructuring was not oriented toward production improvements, but toward nonoperational matters, especially accounting profits.

During the 1980s, corporate restructuring became a euphemism for the external, transaction-based business reorganizations known as corporate takeovers. Using complicated forms of financing, competing groups of financiers and managers struggled with each other for the control and the spoils of U.S. corporations. The operational consequences of these reorganizations were often catastrophic: many of the companies taken over were subsequently broken up, their assets and subsidiaries sold off to pay the overwhelming debt burden the winning bidders incurred.

Many scholars of U.S. capitalism confirmed the crisis framing of restructuring found in business discourse, viewing it as an epoch-making response to the challenge of aggressive global competition. Scholars drew attention to many facets of restructuring. Some emphasized the transformation of industrial production systems to inject flexibility and

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rapid adaptability (Harvey 1989, Piore and Sabel 1984). Some focused on broad changes in the legitimating culture of management that encouraged the abstract control of firms in terms of financial measurements (Brewster Stearns and Allan 1996; Davis, Diekmann, and Tinsley 1994; Davis and Stout 1992; Fligstein 1985, 1990, 2001). Some emphasized concentration of corporate ownership by institutional investors that forced managers to restructure corporations to advance long-term shareholder interests (Useem 1996).

Prechel (1997, 2000) and Prechel and Boies (1998) describe and explain late-twentieth-century restructuring of the legal form of U.S. corporations from organizations of divisions to subsidiaries. Subsidiaries, unlike divisions, have an identity and capital-raising capacity that is legally separate from the parent company. During the 1980s, many firms adopted a *multilayered subsidiary form*, essentially a holding-company structure that enabled greatly intensified embedding of U.S. corporations in financial markets. Parent companies were able to generate capital through security issues of their subsidiaries. The multilayered subsidiary form (MLSF) also facilitated corporate spin-offs, divestitures, and acquisitions. Transactional restructuring greatly facilitated the subsidiarization of U.S. industry.

During the early 1990s, the term *corporate restructuring* jumped off the business pages to enter the popular lexicon in the sense used in this book. In the early 1990s, corporate restructuring referred to *internal reorganization* of a corporation's existing lines of business, production processes, operations, and bureaucratic structure. In the media and popular usage, corporate restructuring ceased to be a synonym for corporate takeovers and became synonymous with employee downsizing and layoffs for the express purpose of boosting the productivity and profitability of the corporation. This form of restructuring included the fleetingly fashionable and broadly discussed form of reorganization known as *business process reengineering* (or *simply reengineering*). Internal reorganization altered a firm's interior organizational structure and processes within the continuing businesses of the firm. These intraorganizational changes aimed to increase corporate efficiency, to help firms become, in the words of an executive announcement, "leaner, tougher minded, more competitive." Table 1.1 and Figures 1.1, 1.2, and 1.3 present some of the social and economic consequences of corporate restructuring.

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TABLE 1.1
Occupational Losers and Winners during the Era of Restructuring: Total Employment in Selected Occupations, 1983–1997

	1983	1997	Change in Employment
Big Losers during the Age of Restructuring			
Typists	906	555	–39%
Computer operators	597	385	–36%
Computer equipment operators	605	392	–35%
Weighers, measurers, and checkers	79	53	–33%
Farm workers	1,149	796	–31%
Telephone operators	244	173	–29%
Communications equipment operators	256	185	–28%
Pressing machine operators	141	102	–28%
Extractive occupations	196	145	–26%
Textile sewing machine operators	806	607	–25%
Secretaries, stenographers, and typists	4,861	3,692	–24%
Textile, apparel, and furnishings machine operators	1,414	1,083	–23%
Secretaries	3,891	3,033	–22%
Telephone installers and repairers	247	197	–20%
Payroll and time keeping clerks	192	155	–19%
Stock and inventory clerks	532	454	–15%
Forestry and logging occupations	126	108	–14%
Bookkeepers, accounting, and auditing clerks	1,970	1,735	–12%
Financial records processing	2,457	2,196	–11%
Statistical clerks	96	89	–7%
Bank tellers	480	446	–7%
Big Winners during the Age of Restructuring			
Adjusters and investigators	675	1,701	152%
Insurance adjusters, examiners, and investigators	199	434	118%
Data entry keyers	311	664	114%
Securities and financial services sales	212	429	102%
Kitchen workers, food preparation	138	278	101%
Correctional institution officers	146	284	95%
Data processing equipment repairers	98	190	94%
Sales-related occupations	54	91	69%
Cashiers	2,009	3,007	50%

Source: U.S. Bureau of Labor Statistics, Employment and Earnings, monthly. Obtained from Statistical Abstracts Online. 2001.

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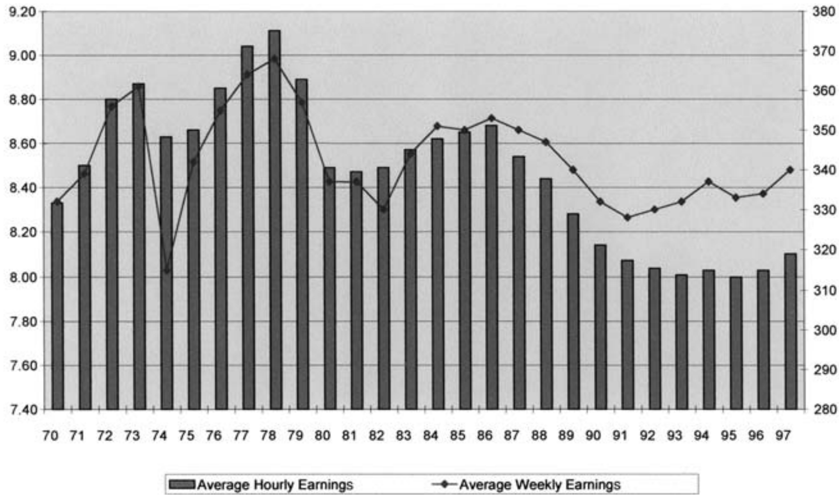
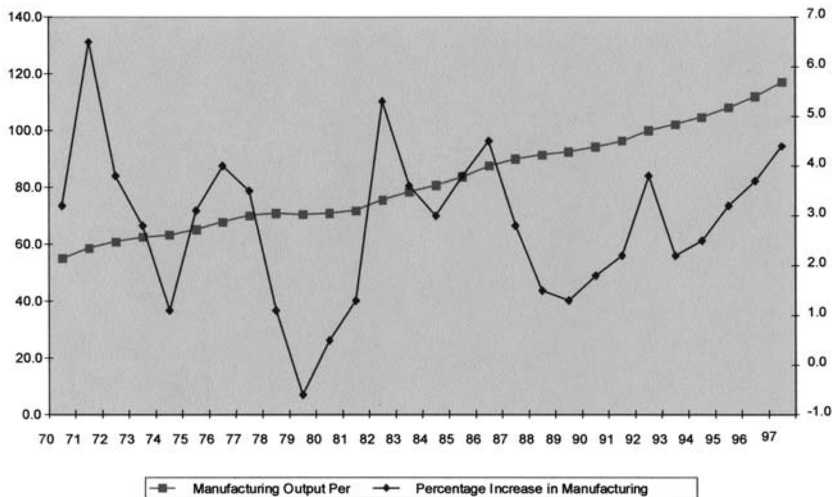
FIGURE 1.1
Real Hourly Wages and Weekly Earnings during Age of Restructuring, 1970–1997



Source: U.S. Bureau of Labor Statistics. 2001. Obtained from Statistical Abstracts Online.

FIGURE 1.2
Productivity Gains during Era of Restructuring: Output per Hour and Percentage Increase in Productivity, 1970–1997



Source: U.S. Bureau of Labor Statistics. 2001. Obtained from Statistical Abstracts Online.

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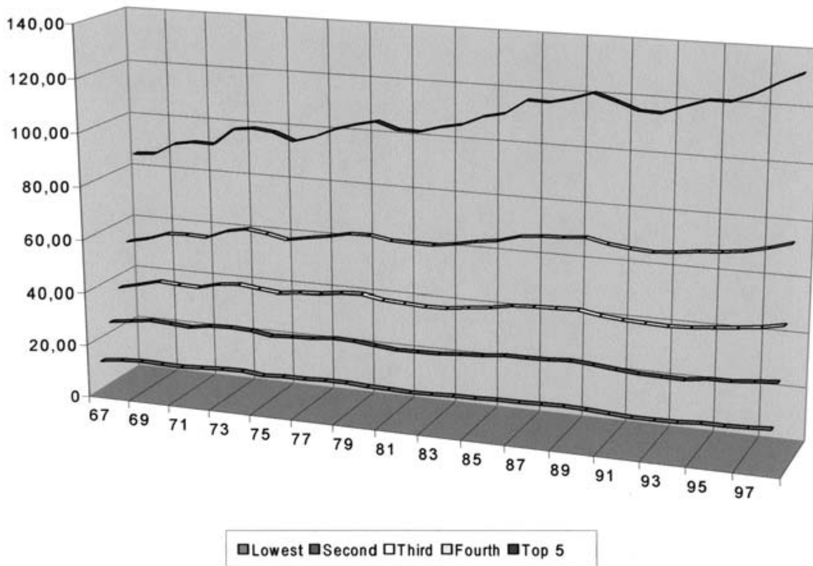
FIGURE 1.3
Income of U.S. Families during Late Twentieth Century:
Upper Limit of Each Quintile and Lower Limit of Top 5 Percent
(in constant 1998 dollars)



Source: U.S. Census. 2001. Obtained from Statistical Abstracts Online.

AMERICAN STEEL: RESTRUCTURING AS PRODUCTION MANAGEMENT

Wide acceptance of corporate restructuring as good production management rested, in part, on successful turnarounds of firms in struggling industries. U.S. industrial corporations faced severe problems in the last decades of the twentieth century. The combination of economic stagnation and high inflation in the macroeconomic environment of the 1970s and early 1980s was one challenge that constrained profits. New global competitors that sold product at much lower costs was another. These problems were especially acute in basic industries such as steel because added to cost pressures were imperatives to improve quality. Industrial purchasers of steel, especially automobile manufacturers, demanded higher quality steel and imposed demanding quality controls

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on suppliers. Restructuring the production process to achieve greater quality and efficiency became a prime management imperative.

Sociologist Harlan Prechel has studied corporate restructuring in the steel industry (Prechel 1990, 1994, 2000). One part of his research is an intensive case study of American Steel, a pseudonym for an integrated steel manufacturing and distribution firm that underwent an extensive reorganization between 1980 and 1992. An early phase of American Steel's restructuring focused on production improvements to achieve greater product quality and profitability, primarily through improvements in the corporation's cost accounting and information management systems. The reorganization began with the collection of highly detailed cost accounting data that allowed management to identify product costs and profitability at a high level of precision. The cost accounting system tracked more than 50,000 cost points. Restructuring decisions were tied to these data. Poorly performing products and the facilities that manufactured them were identified and closed down. Fully 30 percent of production capacity was eliminated through this process. This stage of American Steel's reorganization realigns the firm to its product and labor markets, and as such, is good production management.

The data were also used to analyze remaining production processes to identify areas where work process reorganization could yield additional cost savings. Consultants were employed to retune the corporate culture on decision accountability and cost management. The cost data allowed managers to track inventories better, for example, significantly reducing inventory carrying costs (no small matter when interest rates were high) and material shortages (Prechel 2000, p. 185–6).

The accounting system was further employed to provide cost and quality control information for each discrete managerial decision. The system could track the effect of small variations in production procedures on product quality and product cost. This allowed for the identification of optimal procedures and the centralization of production process controls in a manufacturing decision center. As stated in a corporate document, this highly sophisticated management information system allowed management to "increase accountability at each level and enlarge decision-making responsibility throughout the organization" (Prechel 2000, p. 192). The restructuring further coordinated the manufacturing process through the implementation of an "operations control center" that used computer technology to implement statistical quality control and statistical process control. Computer-aided manu-

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facturing and computer-integrated manufacturing were further used to optimize production processes, maximize efficiency, and ensure quality. This technological infrastructure enabled American Steel to cut its inventory by more than 90 percent, thereby reducing the amount of working capital required (Prechel 2000, p. 198).

This information infrastructure also enabled a restructuring of the organizational hierarchy at American Steel. The new information system altered the management function by assessing costs precisely, tracking managerial performance, maintaining consistent quality, and selecting optimal production processes. The system allowed for (and in some degree required) a thinning of the ranks of middle management. The information system centralized the design and conception of production, eliminating the need for autonomous, information-rich middle managers. Simultaneously, the information system allowed for the decentralization of responsibility for executing production. As a result, American Steel reduced the layers of lower and middle management by 50 percent during its restructuring (from eight layers to four), and cut 28 percent of its managers (Prechel 2000, p. 200).

The restructuring of American Steel led to a sharp turnaround in corporate profitability in the late 1980s.[12]

American Steel's reorganization conforms to images of restructuring as good production management such as those found in Hammer and Champy's (1993)book. The important role information technology played at American Steel to integrate work processes, provide highly detailed cost data, and closely monitor production processes conforms closely to Hammer and Champy's recommendations (p. 83–101). So too is American Steel's integration of computers into decision-making to select optimal processes that reduce production bottlenecks and quality problems. American Steel's decision to eliminate 30 percent of its products and production facilities in the restructuring not as crude cost cutting, but as part of a transformation of the managerial and production process for greater efficiency, quality, and profit.

SUNBEAM REVISITED: RESTRUCTURING AS SPECULATIVE MANAGEMENT

The production-efficiency rhetoric surrounding the restructuring of Sunbeam Corporation indicated that its restructuring would follow a formula similar to that of American Steel. Dunlap stated that "management

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teams," not unlike those at American Steel, would "study" the operations of Sunbeam to identify production and organizational improvements. Consultants observed Sunbeam's processes and developed an integrated restructuring plan. Sunbeam's managers expressed concern about low-cost global competitors and their focus on reducing costs to increase competitiveness, which mirrored the restructuring objectives of American Steel. The decision to close the Bay Springs and McMinnville factories, saving transportation and labor costs, appears consistent with similar decisions at American Steel.

Despite apparent similarities between the restructuring of Sunbeam and American Steel, significant differences appear. Sunbeam's restructuring was justified with efficiency rhetoric, but few, if any, organizational changes Dunlap's management team made were refinements based on a close accounting of the costs of production processes. Dunlap's justifications also used other themes that had come to dominate business discourse in the late twentieth century. These themes focused on corporate shareholders: shareholder rights, shareholder value, and the price of corporate stock. A "shareholder value" orientation did not conspicuously feature in American Steel's reorganization[13] but predominated in Sunbeam's. The restructuring of Sunbeam Corporation focused on increasing the price of Sunbeam's stock.

Dunlap was named Sunbeam's CEO in the summer of 1996, just months after he published a ghostwritten book, *Mean Business: How I Save Bad Companies and Make Good Companies Great*, about his restructuring and downsizing philosophy. In this book, and in subsequent public statements about Sunbeam, Dunlap exalted the rights of shareholders and enthusiastically advocated the managerial pursuit of maximum shareholder value (stock prices). Dunlap told reporters on the day of his appointment to Sunbeam, "If I make a lot of money here [at Sunbeam]—which I certainly intend to do—then the shareholders will make a lot. . . . I'm in lockstep with the shareholders."[14] The following quotations from *Mean Business* illustrate both the broad legitimacy of shareholder rights in business rhetoric in the late twentieth century and the special salience of shareholder values in Dunlap's (1996) restructuring philosophy:

> In corporate circles, the world's most abused minority is the shareholder. Barely tolerated, not respected. . . . That's why a company's No. 1 responsibility is not to the customer but to the shareholder. It

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> doesn't mean that the customer is not of the utmost importance. But when you adopt the attitude of shareholder value first, then the way you spend the corporation's money becomes a function of how you spend money on behalf of the shareholder. (P. 193)

> It's the shareholder's company, not the CEO's. If the shareholders lose value, the CEO doesn't deserve to gain! Talk about mixed-up priorities. The risk of buying a share of stock is enormous. It's not like buying a U.S. Treasury certificate, which is guaranteed. When someone buys a share of stock, he or she may lose some or all of that money. That's why executives of a company must respect that investment and treat it as an awesome responsibility. (P. 194)

> Shareholders own the companies in which they invest. That means the employees—executives included—work for the shareholders. Let me put it in perspective. If you own a house, do you let the gardener tell you when you should sell your house? Does your auto mechanic say, "Oh, no, you can't sell your car!" Stock ownership is the only situation where someone who doesn't own the asset usually gets away with telling the owner what to do. (P. 195)

> The stock price drives me. You can fool the market for a short period of time, but you can't fool it forever. . . . Wall Street is always trying to understand if what has been announced constitutes normal earnings or good earnings. Can they be sustained? Will they grow? (P. 256)

> At Scott, I endeavored to be the most shareholder-friendly CEO in America. . . . How does a CEO become shareholder-friendly? For starters, he or she must be a shareholder. (P. 196)

Dunlap's compensation for becoming CEO of Sunbeam was heavily weighted toward equity-based compensation. Although he did receive a $1 million annual salary, the bulk of his compensation was in the form of huge grants of stock. Dunlap received *1 million shares* of restricted stock on his appointment. He also received stock options to purchase an additional *2.5 million shares*. He was also allowed to purchase $3 million in stock from the corporate treasury on the day before his appointment was announced so that he could profit immediately from any increase in value from his appointment.[15] All of

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Sunbeam's senior managers were granted substantial blocks of stock options and Dunlap forced many to make large open-market stock purchases. The result was that the vast majority of Sunbeam's management compensation came through stock price appreciation. Dunlap also transformed how the members of Sunbeam's board of directors were compensated, shifting from a mostly cash compensation plan to an all stock compensation plan. Each director was granted 1,500 shares per year. "I want directors who are as committed to shareholder value as I am," Dunlap said.[16] The predominance of equity compensation meant that "the executives and directors of Sunbeam are now shareholders in the company and will have an increased commitment to improving shareholder value."[17]

Like most corporate stock compensation plans, Sunbeam placed restrictions on when executives could exercise their stock options. In other words, a period of time had to elapse between the time when the stock options were granted and when an executive could actually obtain and sell the stock. This period often extended several years into the future and served as a means of discouraging short-term tactics to raise the stock price temporarily. At Sunbeam, however, each contract contained a clause that allowed executives to exercise their options immediately if a change of ownership occurred. If Sunbeam were to be acquired by or merged with another firm, Dunlap and the other Sunbeam executives could instantly cash out their stock options.[18]

This was precisely the mechanism that Dunlap employed to pocket about $100 million from the 1994 to 1995 restructuring of Scott Paper. Dunlap's restructuring activity at Scott Paper roughly tripled the stock price in 18 months, and when he sold the company to rival Kimberly-Clark, his restricted options for 750,000 shares of stock became immediately exercisable. In Dunlap's long career of turning around more than a dozen companies, the restructuring activity usually ended in the company being sold. Although business rhetoric in the late twentieth century often championed stock compensation plans because they created long-term incentives in management, the reality at Sunbeam (and many other companies) was that stock options encouraged aggressive, short-term management action to boost share prices. Dunlap and other stock-compensated managers at Sunbeam expected to restructure the firm massively, drive up its stock price, then sell the firm, cash in their stock options, and walk away wealthy.[19]

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At Sunbeam, as at Scott Paper and many other companies in the late twentieth century, corporate restructuring could affect the price of company stock. Restructuring was both a practice of production management and of speculative management (actions oriented toward financial markets and security values). One business media analyst, trying to make sense of Dunlap's conspicuous cutting, sees these actions as largely aimed at increasing stock prices:

> But why would Dunlap and his team choose to accentuate the supposed severity of the downsizing, in the face of a storm of criticism from the likes of then-Secretary of Labor Robert Reich and editorialists around the country? Maybe because Chainsaw Al wants to impress his most important constituent—Wall Street—as the meanest man in the valley, the cost-slasher nonpareil. The stock market pays a lot more for predators than for pussycats.[20]

In retrospect, the restructuring plan to close 18 of Sunbeam's factories, including the plants in Bay Springs and McMinnville, cut in half the workforce, and cut nearly 90 percent of the firm's product lines was poor production management.

Byrne reports that the plant at Bay Springs was closed primarily to save shipping costs. The Bay Springs product would no longer have to be shipped the 40 miles to the final assembly plant in Waynesboro. Additionally, one would expect that the cost of leasing and maintaining the building could be saved. Support staff, plant managers, maintenance crews, and other sundry employees could all be eliminated when the factory was consolidated with Waynesboro.

But the reality was that Sunbeam actually saved very little from closing this plant. Sunbeam did not own the 59,000-square-foot Bay Springs plant; the county government owned it and leased it to Sunbeam without rent. Sunbeam not only paid no rent on the building, but also paid no taxes; the county had long ago waived them to encourage Sunbeam to stay in the community. Furthermore, the Bay Springs facility employed many skilled workers running precision machinery—the wires had to be inundated with radiation during the manufacturing process, for example. Replacing these workers in Waynesboro would be difficult and would require expensive training. The annual expected cost savings from closing the plant: $200,000. The cost of relocating the

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plant: $8 million to $10 million. The move made little economic or production sense, which the mayor of Bay Springs noted:

> It doesn't take a genius to figure out it would take thirty to thirty-five years to get the payback to save $200,000 a year. If you can't make a profit in a free building with no taxes, how are you going to make a profit in an $8 million building in Waynesboro? (Byrne 1999, p. 121)

Closing the McMinnville plant made even less sense from the standpoint of production management. Even the consulting-firm partner whose team designed the restructuring plan admitted that the plant was very well run from a production standpoint:

> It was a good business. It ran by itself. It was doing well from that point of view. You could leave it alone, and it would be perfect. But you could get much more money out of it by moving . . . much more income for Sunbeam if you moved the easy part down to Mexico. (quoted in Byrne 1999, p. 132)

The restructuring plan projected cost savings of some $28 million of annual cost savings from the transfer of the McMinnville plant to Mexico. These savings came entirely from reductions in labor costs. In fact, relocating to Mexico City, to a plant that had been manufacturing blenders and waffle irons, would actually increase most other costs of producing clippers. Manufacturing these products required more skilled workers and precision manufacturing than did blenders and waffle irons. The McMinnville plant ran so efficiently that it could fill customer orders in one day (which meant that Sunbeam did not have to maintain an inventory of clippers). The plant operated to high quality standards and boasted a low warranty return rate. Furthermore, like at Bay Springs, Sunbeam had worked out extremely favorable terms on the lease of the McMinnville plant, paying just $29,000 a year for a nearly 170,000-square-foot plant (Byrne 1999, 131).

Finding and training workers in Mexico City to produce at this level proved difficult. Sunbeam brought 100 workers from Mexico City to McMinnville so that workers who were being eliminated in the restructuring could train their replacements. The last job some of the McMinnville workers completed was to crate their factory's machinery

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onto trucks for transport to Mexico. One Sunbeam executive described the Mexico City plant as a poorly run, outmoded facility that lacked the productivity and quality of the McMinnville plant:

> There was trash all over the place. Few of the workers could speak English. There was no communication. It was just chaos. It was absolutely crazy. It was brutal. You had no planners, no systems. They couldn't get trucks in because there wasn't a traffic department to control it. There was no pride among the employees. When you have people making $5 a week, they don't care. (quoted in Byrne 1999, p. 137)

The production efficiency of the Mexico City plant was well below that of McMinnville. The assembly line frequently was idled because of material shortages. The facility ran out of storage space and had to rent three additional warehouses. Quality was low, as was the volume of production because the plant produced only a quarter of its projected capacity during its first months. "The lost production destroyed profits, wrecked market share, alienated customers and consumed great amounts of organizational energy" (Byrne 1999, p. 138).

From the standpoint of production management, closing these plants in this manner made little sense. Some executives at Sunbeam carried on a stealth campaign to delay or block the closing of these plants because they needed their products and because they were profitable, efficient facilities. So why were they targeted for shutdown in the first place? In Byrne's account, Dunlap designed the restructuring plan to impress Wall Street analysts. The magnitude of the restructuring plan, the amount of annual savings and the size of the job cuts, Dunlap determined before his hired team of Coopers and Lybrand consultants ever opened a laptop. He wanted to tell analysts he was cutting half the workforce, so half were cut. He wanted to tell analysts that the restructuring would result in annual savings of $225 million, so costs of this magnitude were cut. He wanted to boast of having only 100 employees in the corporate headquarters, so 208 people were fired (Byrne 1999, p. 110–17). The restructuring decisions at Sunbeam were made to maximize their impact on stock analysts, not on production efficiency.

From a production management standpoint, the restructuring of Sunbeam was a disaster. The company has not been profitable since the restructuring began. Early, glowing accounting figures that reported record income under the Dunlap regime were later found to be fabricated

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and were restated to reflect deep losses. The losses continued in the following years. But for a period of time between 1996 and 1998, the restructuring plan at Sunbeam was very effective speculative management. The price of Sunbeam stock increased from roughly $12 when Dunlap was appointed CEO in summer 1996 to a high of $53 in the winter of 1998. By the fall of 2000, the shares were virtually worthless, trading at less than a dime a share.[21]

The reorganizations of Sunbeam and American Steel are examples of two very different orientations to corporate restructuring: production and speculation. The two cases match most closely in the shared emphasis on production efficiency in management's rhetoric. The two cases diverge most sharply in the substance and objectives of their restructuring activities.

This study conceptualizes the orientation of restructuring to financial markets and seeks to understand how restructuring actions were geared to influence financial actors and affect stock prices. Restructuring was a practice of speculative management—managerial action oriented toward financial markets. This study seeks to supplement interpretations of restructuring that focus on production efficiency and develop an appreciation for speculative management as a characteristic and important aspect of late-twentieth-century American capitalism.

SPECULATIVE MANAGEMENT IN CORPORATE RESTRUCTURING

> *Knowing how to simplify one's description of reality without neglecting anything essential is the most important part of the economist's art.*[22]
>
> —James S. Duesenberry

> *It is not enough to construct an abstract model and provide an explanation of how it operates; it is just as important to demonstrate the explanatory effectiveness of such a model as applied to historical realities.*[23]
>
> —Celso Furtado

This study constructs and focuses a model of speculative management to interpret a *particular, historically limited* social object: the late-twentieth-century wave of U.S. corporate restructuring.[24] This model was formed and refined using an ideal type methodology that the work of Max Weber (1949, 1978) inspired.[25] Research conducted under this

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logic develops one-sided, logically integrated heuristic concepts to understand empirical social objects.[26] Ideal type concepts are "ideal": they are mental constructs. These concepts do not represent averages or categories of empirical social phenomena. Instead, they are selectively constructed conceptual models that are simpler, more integrated, and more self-consistent than the empirical social objects that they help define. To Weber (1949), an ideal type is an analytical accentuation of certain elements of reality:

> An ideal type is formed by the one-sided *accentuation* of one or more points of view and by the synthesis of a great many diffuse, discrete, more or less present and occasionally absent *concrete individual* phenomena, which are arranged according to those one-sidedly emphasized viewpoints into a unified *analytical* construct. In its conceptual purity, this mental construct cannot be found empirically anywhere in reality. It is a utopia. (P. 90)

This study is intended to conceptualize a particular complex reality, the late-twentieth-century wave of corporate restructuring, from one standpoint, speculative management. The model and concepts formed in this study are deliberately one-sided. The speculative management model is designed to aid in the comprehension of financial market orientations and speculative interests in this particular reorganization wave. The model developed in this study is not an exhaustive interpretation. Other selective accounts of restructuring from other standpoints reveal features that speculative management does not. Speculative management is not the whole story of restructuring. It does, however, reveal important features of late-twentieth-century restructuring that are difficult to appreciate from production-centered standpoints.

This research attempts to unify several decisive aspects of a wave of corporate restructuring and the late-twentieth-century U.S. capitalist context in which it occurred with an underlying logic or imagery (Weller 2000) of speculative management. This study aims to develop a complex conceptualization of corporate restructuring that unites tendencies in several elements of late-twentieth-century firms and their capitalist context. These tendencies and elements include: corporate governance and control, secondary financial markets, equity securities valued as capitalized earnings, financial accountancy, and the business media.

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Complex, multidimensional ideal types, including the speculative management model of restructuring developed here, are still one-sided in the sense that they are constructed to reveal features of social reality from a particular point of inquiry. The elements unified into complex types do not deplete the essential features of a particular social object because other features would come into view from other points of view. Some features of late-twentieth-century corporate restructuring, such as product-market and production-efficiency orientations, are better brought into view with other, more production-centered models. Speculative management is not intended as a comprehensive replacement or substitution for other models, but it is intended to augment understanding of restructuring by providing an optic that allows the role of financial and speculative interests to be viewed clearly.

A provisional description of speculative management in corporate restructuring is expressed here:

> Late-twentieth-century restructuring of American corporations was to a significant extent undertaken by managers to realize pecuniary gains. Restructuring was calculated to influence the market valuation of corporate stock in mass, secondary stock markets. Restructuring was, therefore, a practice of speculative management. Corporations were connected to these markets by social intermediaries that enabled, structured and constrained the manipulation of market value in restructuring.

In addition, this study constructs, refines, and employs several concepts to interpret aspects of corporate restructuring and late-twentieth-century financial markets. The most important of these are:

Speculative management (contrasts with *production management*): Corporate actions oriented toward secondary stock markets with the intention of influencing the trading price of corporate equity shares (stock). Many corporations express speculative management in terms of maximizing shareholder value. The concept also contrasts with investor capitalism, as an image of the primary orientation of late-twentieth-century U.S. capitalism.

Internal reorganization (contrasts with *transactional reorganization*): intraorganizational restructuring as a business event.

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May include downsizing, reengineering, or streamlining. Synonymous with *corporate restructuring* in the early 1990s. When initiated to generate reorganizer's profit, a type of pecuniary reorganization based on accounting accruals rather than an external transaction.[27]

Transactional reorganization (contrasts with *internal reorganization*): extraorganizational restructuring from a business reorganization deal. May include takeovers, acquisitions, divestitures, mergers, and more complicated transactions such as equity carve-outs. Synonymous with *corporate restructuring* in the 1980s. When initiated to generate promoter's or reorganizer's profit, a type of pecuniary reorganization.

Pecuniary reorganization: A disruptive event that triggers a reevaluation of corporate securities and thereby generates reorganizer's profit. There are two types: transactional reorganization (mergers and spin-offs) and internal reorganization (corporate restructuring).

Reorganizer's profit (compares to *promoter's profit*): Increase in the trading price of a firm's securities due to a pecuniary reorganization. Represents an increase in the market value, or shareholder value, of the firm (fictitious capitalization). Comparison term is promoter's profit (Hilferding 1910, Veblen 1904), which represents the increase in value of a privately held firm on listing on a public securities market. Whereas a promoter's profit emerges from initial public offerings (IPOs) on primary markets, a reorganizer's profit arises from pecuniary reorganization and is captured on secondary markets. Reorganizer's profit accrues almost entirely to owners of record before the reorganization is announced.[28]

Conceptions of aggressively good management: Prevailing views among financial market participants, corporate executives, and the business media of the managerial practices that are most likely to maximize shareholder value (trading price of corporate stock). Management consultants specialize in the marketing of innovative conceptions of aggressively good management.

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> **Social intermediaries** (compares with *financial intermediary*): Social institutions that connect corporations to secondary stock markets. This study focuses on three structures: corporate governance structures, financial accounting, and the business media (including print, broadcast, and electronic media). Comparison is to financial intermediaries that link firms to primary financial markets.

Not only the overall model, but also the focused concepts developed in this study are ideal types rather than empirical categories.[29] Transactional reorganization (for example, mergers and divestitures) and internal reorganization (for example, reengineering and downsizing) are two selective, one-sided logics for restructuring. Speculative management (practices aimed directly at manipulating stock values on financial markets) and production management (practices aimed directly at operations and performance on product markets) are both selective, one-sided renderings of executive orientation. Concrete instances of corporate restructuring exhibit a blend of orientations and practices and different forms of restructuring were taking place at different firms at the same time.

An assumption of this study is that restructuring activity in the late twentieth century was sufficiently oriented to financial markets to warrant a speculative management interpretation. Evidence is presented to demonstrate that a speculative management interpretation of restructuring is plausible and that such an interpretation effectively explains the inflection points of the rise, reign, and decline of the late-twentieth-century restructuring wave. Some sectors (aerospace, computer chips, steel) appear to have been less oriented to financial markets and reorganized to a production logic rather than a speculative logic. The management-information-system–based internal reorganization of American Steel is close to the type of restructuring as production management.[30] Byrne's (1999) account of Sunbeam's restructuring conforms closely to the type of restructuring as speculative management.

THE SCOPE OF EMPIRICAL INVESTIGATION

This study began in 1994 with an empirical investigation into corporate restructuring that examined how managers communicated these activities to shareholders and the financial community in news releases and

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shareholder reports. The information herein is based on a deeper and more systematic investigation that inspected a sample 100 of the largest industrial U.S. firms and an array of 67 other very large firms in financial services, diversified services, transportation, utilities, and retail. The aim was to track the wave of restructuring as it passed through corporate America from 1984 to 1997.

Empirical materials were gathered and analyzed that allowed for the refinement of the speculative management model of corporate restructuring. Materials were sought to address several related research questions: Why did the stock market reward firms that announced large losses due to restructuring activities with an increase in market value of the firm's shares? How were firms communicating restructuring activities to shareholders and the financial public? What information was available to the investing public to enable them to view restructuring activities? What connecting structures make it possible for corporations and financial markets to assess and influence each other mutually?

Primary materials that illuminated management presentations of restructuring plans to shareholders of the firm and to the financial public were especially important to this research. These materials included corporate annual reports and Securities and Exchange Commission (SEC) filings, financial and business media archives, corporate news releases, trade publications, and numerous other sources. Because restructuring initiatives frequently generated significant costs for firms, financial statements of firms and regulatory filings revealed how these costs were recognized.

Rules and procedures of financial accounting constrain management presentations of financial information, so pronouncements of accounting standards-setting boards and business discourse about them were examined in accounting trade publications, professional training materials, and the financial media. The public documents of accounting rule-making bodies, particularly meeting minutes of the Emerging Issues Task Force (EITF) of the Financial Accounting Standards Board (FASB) and public response forums, available via the Internet, were especially useful. The investigation of financial patterns of restructuring and financial accounting relies heavily on my professional training and experience as an auditor.

Additional materials revealed how financial publics processed the restructuring activities of firms.[31] Financial media archives were greatly used for this purpose. Publications and statements by investor

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organizations and major financiers were also used. Electronic information media, such as Lexis-Nexis and Dow Jones Interactive facilitated the search for specific information. Additionally, the Internet sites of large corporations became a useful source of information because they are often geared toward investor relations. Many sites contain the annual report to shareholders, news release archives, SEC filing archives, and so on, which made obsolete, for some purposes at least, the maintenance of a physical archive of annual reports.

Other critical information formerly available only in archives became instantaneously available via the Internet in the 1990s. The SEC and FASB each maintain information-rich Web sites that facilitated this research. Internet investing Web sites, such as BigCharts.com, allowed for the generation of graphs of stock performance, summaries of analyst earnings projections, and other financial information.

The ideal type method employed in this study calls for the empirical refinement of concepts and models through interpretive contact with a wide range of materials. The construction and refinement of ideal type concepts, in Weber's work especially, requires the confrontation of comparative and historical materials: Kahlberg (1994) describes Weber's concepts as "historically saturated." The ideal types in this study have been formed and refined in conjunction with a selective inquiry into the structure and dynamics of U.S. markets for corporate securities and the relationship of these markets to the industrial factories and plants that underlie the securities traded on them. Sociologists have not thorougly researched this area of American life (the secondary security markets). American corporate finance was compared with the financial systems of continental Europe to form an image of its unique features. American finance was also studied historically (genetically) to conceptualize how it came to be so structured.

Comparative study pointed to the dominating secondary stock market as a characteristic feature of U.S. finance. Financial markets in Europe, until quite recently, have lacked a strong, active secondary stock market and are much closer to the image of markets portrayed in the socioeconomic literature. Historical and comparative study helped to establish limits to the concepts employed in this study and aided in their refinement.

Methodical study provided only a part of the source material drawn on for this study. The speculative management model of corporate restructuring was formed and tested against a much wider set of

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empirical materials than are cited herein. I majored in business administration as an undergraduate, worked for a time as an auditor for a Big Six accounting firm, and later as a research director for a business consulting firm. While a graduate student in sociology, I continued to read widely on business matters, completed coursework in economics, and taught in an organizational behavior department. I have been a daily reader of financial and business news for more than a decade and have maintained a clipping file on restructuring and financial speculation. As much as possible, I immersed myself in relevant materials that were examined from many angles, giving me the opportunity to come across inconvenient facts that forced me to refine my thought.

Consistent with the concept-forming purpose of this study, the empirical materials presented in this report were selected to illustrate vividly and communicate the interpretation of speculative management in restructuring, not to prove the argument.

OVERVIEW

The study investigates and interprets financially oriented corporate restructuring in the late twentieth century, developing and supporting the position that downsizing restructuring (internal reorganization) of the kind characteristic of the 1980s and 1990s receded from the corporate landscape by the end of the 1990s. This was especially true of leading firms and of industrial (as opposed to financial or medical) firms. During the 1990s bull market, the financial news buzzed with stories of corporate reorganization, but these stories described mergers, acquisitions, and other transactional restructuring more often than "downsizing" packaged as a corporate event. The exceptions, including Coca-Cola's announcement of the elimination of 20 percent of its workforce in early 2000, were greeted more with indifference or aversion than cheers. Rather than boosting stock market valuation, Coke's year 2000 downsizing caused a drop in its stock price.[32]

Chapters 2 through 8 present the interpretation of corporate restructuring as speculative management. Chapter 2 provides some historical financial context for the emergence of internal reorganization as a management practice in the 1980s. Chapter 3 presents findings from an extensive investigation of more than 2,000 annual reports to shareholders and SEC filings for 167 very large U.S. firms. Corporate

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restructuring (internal reorganization) emerged as a management practice intimately tied to corporate takeovers in the very early 1980s and spread slowly among the firms in the study throughout the rest of the decade. Corporate restructuring sharply increased in both frequency and magnitude during the early 1990s as corporations became unable to pursue external reorganization and focused their speculative management activity internally instead. Corporate restructuring activity fell sharply in 1994 when accounting regulators constrained the use of internal reorganization as a mechanism to manipulate corporate financial statements. Corporate restructuring declined further in the late 1990s as financial markets ceased to view internal reorganization as a good management practice.

In each of the three phases of the "wave" of restructuring (the rise, reign, and decline), institutions that connect firms to secondary equity markets (stock markets), conceptualized herein as *social intermediaries*, were found to be important for channeling speculative management interests into and out of corporate restructuring. The three social intermediaries discussed here: corporate governance structures, financial accounting and the business media (including print, broadcast, and electronic media) contributed to the emergence of internal reorganization as a discrete management strategy, helped support restructuring as a good management practice during its reign and contributed to the decline in restructuring. Chapter 4 conceptualizes financial accounting and the business media as social intermediaries. Chapter 5 considers issues of corporate control and theories of markets from a standpoint sensitive to social intermediaries and speculative management. Chapters 6 through 8 analyze the rise, reign, and decline of restructuring using detailed illustrative material selected from annual reports, shareholder communications, and business media articles. The speculative management view of corporate change is summarized and concluded in Chapter 9 with a brief comparison of the speculative management perspective to others currently employed in the study of corporate restructuring.

Late-twentieth-century corporate managers and business reorganizers represented restructuring to business constituencies as production management, an effort to increase the efficiency of industrial corporations. This study develops a view of corporate restructuring as speculative management engaged in to increase the trading price of corporate securities. Although other studies have brought into view how restructuring was used to increase corporate profits from increased industrial

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efficiency, this study highlights how restructuring was used to capture profits from increased stock values.

This book explains the historically limited episode of corporate change that swept through U.S. corporations in the late twentieth century and moves toward a broad interpretation of the structure and dynamic of the U.S. market for financial securities that enables financiers to capture gains through pecuniary reorganizations of their business.

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