Economic Perspective 2

GUINNESS V ARTHUR BELL: WHAT ARE THE ISSUES?

J H Love
Fraser of Allander Institute, University of Strathclyde

To the casual observer the bid by Guinness for Arthur Bell has all the hallmarks of high drama, as two ambitious empire-builders fight for control of one of the most prestigious names in the whisky industry. The timetable of events until the decision not to refer the bid to the Monopolies and Mergers Commission (MMC) gave the press a field day:

14 June Guinness makes a £300m bid for Bell ending weeks of speculation. Bell's Chairman, Raymond Miquel, immediately strikes an aggressively defensive posture.

20 June Bell complains to the City Takeover Panel over the use by Guinness of merchant bankers Morgan Grenfell, who had at one time acted for Bell.

25 June After missing each other narrowly on several occasions. Miquel and Guinness's Chief Executive Ernest Saunders finally meet. They have "frank discussions".

28 June The Guinness formal offer document is issued and claims that Bell has "lost its way".

12 July Bell's defence document is posted to shareholders. It attacks Guinness's own record and promises higher profits and dividends.

14 July Guinness complains to the Takeover Panel, claiming that the defence document distorts some aspects of the brewer's record of growth and profitability, and is misleading to shareholders.

23 July After a brief lull in the dispute Norman Tebbit announces that the bid will not be referred to the MMC. Battle is rejoined.

The public nature of this major takeover bid and the forceful personalities of the two main protagonists should not blind us to the fact that there are important issues at stake both for Arthur Bell and for the Scottish economy. The very fact that there will be no MMC investigation makes it all the more important that these issues should be aired in a dispassionate manner, away from all the controversy surrounding the bid itself. Before doing this it may be useful to consider why the bid was not referred to the MMC.

WHY NO REFERRAL?

After seeking advice from the Office of Fair Trading. the Secretary of State for Trade and Industry has fairly wide powers in deciding whether a particular bid should be referred to the full MMC. He has to decide that a "merger situation" is likely to exist and that either:

(a) there exists, or will exist. a monopoly in the market in question

or

(b) the value of assets to be acquired exceeds a certain value (presently £30m).

In practice option (a) is invariably waived, leaving the asset criterion as the basis for a referral. However, although these are necessary they are not sufficient conditions for the involvement of the MMC.

Once a proposed merger is referred the MMC must decide if it is likely to operate against the public interest. Under the 1973 Fair Trading Act the Commission may consider virtually any matter which it believes to be relevant to "the public interest". However, five specific issues are mentioned in the Act; four of these relate to elements of competition, but the fifth to the desirability of

> "maintaining and promoting the balanced distribution of industry and employment in the United Kingdom." (Section 84(1))

This is the area which Scotland has made its own. Within the past five years three major Scottish companies, Highland Distilleries. The Royal Bank and Anderson Strathclyde, have had bids for them by non-Scottish concerns turned down by the MMC either wholly or partly on regional grounds. No other region of the UK has played this card with such spectacular results.

When the MMC becomes involved the Secretary of State effectively loses control over its decision. He can, of course, choose to accept a minority view as was done in the Charter Consolidated bid for Anderson Strathclyde, but this leaves the Government open to potentially embarrassing public criticism. Much more subtle and less public political control can be exercised in deciding whether or not a bid shall be referred. Norman Tebbit clearly sees the job of the MMC as being a watchdog on competition, not as an adjunct of regional policy. This view is entirely consistent with the stance of the Thatcher administration which has shown little sympathy to the regional question.

Thus, while the Guinness bid for Bell fulfills the necessary conditions for referral, Tebbit has chosen not to do so because there are no expressly competitive issues at stake. There is no question of the concentration of ownership of distilleries because Guinness owns none; nor should there be any problems over the supply of whiskies other than Bell's through tied houses, because Guinness owns no pubs.

The very success with which the MMC has been used in Scotland in the past to fight unwelcome external takeovers may have been counter-productive in this case. From the Government's point of view the easiest way to prevent the Commission airing unwelcome issues is to bypass it.

THE ISSUES AT STAKE

Any proposed takeover of a regionally-based company has implications both for the company itself and for its region. Some of these internal and external issues are summarised in Table 1. Not all of these elements are present in every takeover, but many of them have been raised both by academic writers and in MMC reports. We now turn to examine those which appear to be relevant in the present context.

(a) Internal

One of the key areas highlighted by Guinness is that Bell has "lost its way" following over a decade of spectacular growth, and is heading for a period of decline. What is needed, argues Ernest Saunders, is the marketing expertise which Guinness can provide to revitalise the Bell's brand at home and to give it the push required in America and other important overseas markets. The precise method by which this is to be achieved is by no means clear, except that Guinness dismisses as insignificant Bell's purchase of Wellington Importers to handle its interests in the USA. In the absence of further information the Guinness claims on this issue must remain unproven, but they would do well to be more convincing. Hiram Walker were left looking rather

Table 1 Possible effects of acquisition

Internal effects

Favourable	Unfavourable
Access to new markets	Removal of products and product lines
Investment finance more readily available	Removal of important management functions and aspects of operation
Improved management techniques	Increased likelihood of "branch plant" contraction during recession
Possible transfer of production to the acquired firm	Profits for investment routed to parent comapany
More rapid growth	

External effects

Favourable	Unfavourable
Diffusion of new technology and techniques	Reduced use of local suppliers of goods and services
Acquisition of new skills for local labour force	Migration of and lower morale among management leading to restriction of entrepreneurial activity
Improved job opportunities within the region	Lower regional economic growth in long run as result of the above

foolish during their 1980 bid for Highland Distilleries over the same issue. The Canadian company claimed that The Famous Grouse blend would be more successful under their aegis because they had an international sales network which Highland lacked. The MMC, however, took the view that Highland's own plans for the blend were more soundly based, an important element in their decision to block the bid. Admittedly Guinness has no need to convince the MMC of its plans, but the Bell shareholders will no doubt be intrigued to know what the future would hold under Guinness.

The prospects for key management and the functions which they perform could be an important element in the bid. Raymond Miquel has painted a sorry picture of a dismembered "branch plant" Arthur Bell with limited autonomy, all the real power being exercised in London. It is hard to believe that Guinness really intends to spend £300m plus in order to effectively destroy the company, and they would be very foolish to do so given the expertise in whisky which Bell management has. It seems much more likely that the company would remain essentially intact, but with the need for financial reporting to London. Only if the company ceased to generate the necessary level of profits would more detailed control seem likely.

There is clearly the possibility of the loss of key management personnel should the bid succeed. The possible effects of this for Scotland are dealt with in the next section; here it is necessary to consider the internal effets of a change in management style. Potentially detrimental effects of a clash of style and of personalities were important considerations in the MMC's decisions to block both the bid by Hiram Walker for Highland and that by Charter Consolidated for Anderson Strathclyde. In the latter case the possible problems were thought to be so great as to extend beyond management into the area of worsened labour relations and even to the diminishing of effective competition because of lowered management morale. This argument was, however, expressly denied by the minority view which was accepted by Government.

The personality clash between Messrs Saunders and Miquel could scarcely be more obvious. While a **volte face** by previously feuding parties is by no means unknown in business, it is hard to imagine Mr Miquel playing second fiddle to anyone should the bid be successful. Were he to depart, it would be interesting to discover what effect this would have on the remaining management at Arthur Bell; it remains to be seen whether a clash of management styles exists at levels below the chairman's office.

The final internal question relates to the possible effects on products and employment. No-one has suggested that Guinness has any plans to tamper in any

Table 1 Possible effects of acquisition

Internal effects

Favourable	Unfavourable
Access to new markets	Removal of products and product lines
Investment finance more readily available	Removal of important management functions and aspects of operation
Improved management techniques	Increased likelihood of "branch plant" contraction during recession
Possible transfer of production to the acquired firm	Profits for investment routed to parent comapany
More rapid growth	

External effects

Favourable	Unfavourable
Diffusion of new technology and techniques	Reduced use of local suppliers of goods and services
Acquisition of new skills for local labour force	Migration of and lower morale among management leading to restriction of entrepreneurial activity
Improved job opportunities within the region	Lower regional economic growth in long run as result of the above

foolish during their 1980 bid for Highland Distilleries over the same issue. The Canadian company claimed that The Famous Grouse blend would be more successful under their aegis because they had an international sales network which Highland lacked. The MMC, however, took the view that Highland's own plans for the blend were more soundly based, an important element in their decision to block the bid. Admittedly Guinness has no need to convince the MMC of its plans, but the Bell shareholders will no doubt be intrigued to know what the future would hold under Guinness.

The prospects for key management and the functions which they perform could be an important element in the bid. Raymond Miquel has painted a sorry picture of a dismembered "branch plant" Arthur Bell with limited autonomy, all the real power being exercised in London. It is hard to believe that Guinness really intends to spend £300m plus in order to effectively destroy the company, and they would be very foolish to do so given the expertise in whisky which Bell management has. It seems much more likely that the company would remain essentially intact, but with the need for financial reporting to London. Only if the company ceased to generate the necessary level of profits would more detailed control seem likely.

There is clearly the possibility of the loss of key management personnel should the bid succeed. The possible effects of this for Scotland are dealt with in the next section; here it is necessary to consider the internal effets of a change in management style. Potentially detrimental effects of a clash of style and of personalities were important considerations in the MMC's decisions to block both the bid by Hiram Walker for Highland and that by Charter Consolidated for Anderson Strathclyde. In the latter case the possible problems were thought to be so great as to extend beyond management into the area of worsened labour relations and even to the diminishing of effective competition because of lowered management morale. This argument was, however, expressly denied by the minority view which was accepted by Government.

The personality clash between Messrs Saunders and Miquel could scarcely be more obvious. While a **volte face** by previously feuding parties is by no means unknown in business, it is hard to imagine Mr Miquel playing second fiddle to anyone should the bid be successful. Were he to depart, it would be interesting to discover what effect this would have on the remaining management at Arthur Bell; it remains to be seen whether a clash of management styles exists at levels below the chairman's office.

The final internal question relates to the possible effects on products and employment. No-one has suggested that Guinness has any plans to tamper in any way with the product itself, or to do anything to harm the carefully-cultivated up-market image which the product as a whole enjoys. Nor is there any indication that Guinness intends to make additions to or reductions in the Scottish firm's range of whiskies. As well as the well-known "Bell's" blend the company markets several variations on the same theme as well as three single malts. There is nothing wrong with the products, argues Guinness, just with the way they are sold.

One of the most hotly-disputed issues has been employment. Guinness made a no redundancies pledge in its original offer document, which was soundly condemned by Bell on the grounds that similar promises to other Guinness plants have subsequently been broken. Raymond Miquel has played heavily on the redundancies theme, but it is difficult to see why or in what areas they would arise. Guinness has no whisky interests at present, so there is no question of rationalisation within a parallel network as has happened with previous whisky takeovers. Scotch whisky can legally only be distilled in Scotland, so there is no question of production being transferred out of the country. However, most production workers are employed in blending and bottling which can be located anywhere. Once again it is difficult to see exactly why redundancies should be thought likely in this area, given that Bell's blending and bottling operations are generally considered to be highly efficient. The relative lack so far of comments by union representatives and other labour spokesmen is perhaps relevant here, as is research presently being carried out by the author which suggests that whisky firms externally acquired during the 1970's have fared well in comparison with the industry as a whole.

(b) External

The external issues in a proposed inward acquisition are rather more difficult to judge **ex ante**, but are no less important for that. Relatively little discussion of the possible impact on the Scottish economy has as yet taken place, other than scaremongering at the most general level.

One of the most obvious areas of concern is the possible effects of the takeover on material and service inputs to Bell from other Scottish companies, and the effect on employment within these companies. Where there are no major horizontal or vertical elements of integration there is usually little reason to expect much change in the use of local material inputs, especially where there is unlikely to be much change in the product range of the acquired company. However, the situation with regard to the use of local services may be very different. There is a body of academic evidence which indicates that externally-acquired companies do tend to make less use of local professional services such as banking, solicitors, accountants, etc, either because such activities are carried out internally within the acquirer or because those (non-Scottish) professional companies employed by the acquirer automatically receive the business of the new subsidiary. This possibility was expressly mentioned by the MMC as an area of concern during the proposed takeover of Anderson Strathclyde.

Whether this situation would arise with Arthur Bell would depend to a large extent on the degree of autonomy retained if the takeover went ahead. The impact of this removal of services is very difficult to judge in quantitative terms, and there is no suggestion that the acquisition of a single company is of great concern on this issue. Nevertheless, as the level of external control in Scotland increases it may become a more pervasive and intractable problem for a country which has long prided itself on its professional skills.

The second important external effect to be considered is possible changes in the skills of both workforce and management. At the workforce level changes in work practices could lead to the acquisition of new skills which could gradually be diffused into companies which have contact with the acquired company; on the other hand, the same process could lead to the decay and death of existing skills which may never be replaced in the regional economy. While this sort of effect is likely to be limited at Arthur Bell, of possibily greater significance could be the long-run effects of internal changes among Bell's management. If skilled managers were to leave the company as a result of takeover, the effect on Scotland would depend very much on where they moved. If they find jobs in other Scottish companies which require their skills the net effect to the regional economy may be neutral or even beneficial. But if they choose to move out of Scotland because job prospects are better elsewhere then this constitutes a loss to the Scottish economy. Much the same effect could occur if Guinness were to entice able Scots down to the London headquarters with a view to wider career opportunities, especially if career prospects at Perth seemed more limited as a result of takeover.

In the long-run the migration of skilled management may have a detrimental effect on entrepreneurial activity within the regional economy, possibly leading to a lower rate of economic growth than would otherwise be the case. To some extent it could equally be argued that a major management shake-up might just provide the spur for potential entrepreneurs to branch out on their own. although this begs the question of whether any such entrepreneurial activity would take place within Scotland.

In case some of these issues should seem rather esoteric in the context of one potential takeover, it should be pointed out that they were precisely the matters held by the MMC to be of importance in its report on the bids for The Royal Bank by Standard Chartered and Hong Kong and Shanghai Banking Corporation:

> "We believe that an important factor in Scotland's economic difficulties has been the progressive loss of morale which the taking over of large companies has caused; and we accept that this is damaging to Scotland. Entrepreneurial spirit and business leadership depend critically on self-confidence, and on balance we believe that such self-confidence has been weakened." (para 12.10)

And later the report concludes that the effects of the proposed mergers on

> "..... career prospects, initiative and business enterprise in Scotland would be damaging to the public interest of the United Kingdom as a whole". (para 12.38)

The sentiments expressed in the Royal Bank report mark the zenith of Scottish influence on inward acquisitions through the MMC, but the issues raised remain important for a country which believes itself to be more than just another region of the UK.

THE DECISION

The previous sections outlined the reasons why the Guinness bid for Arthur Bell was not referred to the MMC, and discussed some of the important issues. Two questions remain to be answered.

1) Does the failure to refer the bid sound the death knell of "the regional question" as an issue in mergers policy?

2) Are any of the issues raised above likely to be of importance in influencing the decision of Bell's shareholders?

The decision to allow market forces to prevail in this instance does not **per se** remove regional issues from the sphere of competition policy. What it does is to confirm the relegation of these issues to much lesser status than has been the case in recent years. The key point here is that an existing trend is merely being **confirmed**; the pattern was set by the rejection of the majority MMC report in the Anderson Strathclyde takeover and by some fairly unambiguous recent comments on the subject by Alex Fletcher. Regional issues will not form the major grounds for MMC referral during the remainder of this administration, but this does not preclude their re-emergence under a Government of a different political hue.

Large financial institutions own the majority of Bell's shares, and it is these institutions which the protagonists must convince of their claims. The primary motivation of these shareholders is to obtain the maximum return on their investment; for them such internal issues as possible effects of takeover on the Scottish company's plants and employment are of little significance in their own right. Their only importance lies in their direct or indirect influence on the value of the institutions' investment. If these **internal** issues are of peripheral concern one can all too readily imagine the importance placed by these major investors on topics relevant to the regional economy as a whole, such as the possible effects of acquisition on linkages with other Scottish companies, impact on entrepreneurial activity etc.

For all its flaws, one thing which is overwhelmingly in the MMC's favour is that in its reports the Commission must have as its overriding consideration "the **public** interest". The major institutions have no such public criteria to consider in deciding the future of Arthur Bell.

References

HMSO (1980) "Hiram Walker-Gooderham & Worts Limited and the Highland Distilleries Company Limited: a report on the proposed merger" (HC 743)

HMSO (1982) "The Hong Kong and Shanghai Banking Corporation, Standard Chartered Bank, The Royal Bank of Scotland Group Limited: a report on the proposed mergers" (Cmnd 8472)

HMSO (1982) "Charter Consolidated and Anderson Strathclyde Limited: a report on the proposed merger" (Cmnd 8771)

Hood N, A Reeves and S Young (1981) Foreign direct investment in Scotland: the European dimension", Scottish Journal of Political Economy, Vol 28(2), pp165-184.

Leigh R and D J North (1978) "Regional aspects of acquisition activity in British manufacturing industry", Regional Studies, Vol 12(2), pp227-245.