What was the Whitbread Umbrella protecting? From brewing to coffee via pub retailing

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A topical theme in strategic management is that successful firms are those that are able to adapt to an environment of constant flux, conceptualised as 'dynamic capabilities'. However, rarely does this extend to a discussion of a firm's history in embedding culture and capabilities. I present a case study of UK former family firm, Whitbread, to explain how it survived beyond its traditional brewing operations to become one of Europe's largest leisure retailers. Central to the analysis is the 'Whitbread Umbrella' structure which provided a support mechanism as the firm repositioned towards the evolving UK eating-out market. By the time the Umbrella had outlived its initial role the firm was a self-supporting branded leisure retailer which acquired and nurtured Costa Coffee and Premier Inn. Whitbread's strategic transformation, prompted by significant change in the institutional environment, informs academic debate in several literatures and highlights the importance of history and context in supporting wider scholarly and practitioner knowledge.

INTRODUCTION

The history of the Whitbread group is synonymous with founder Samuel Whitbread and the UK's first purpose-built mass production brewery established at Chiswell Street in The City of London in 1750. It was from these premises that the Whitbread group and successive descendants of the family built a national brewer-retailer with operations that extended into various leisure industries such as hotels and restaurants. The era of direct family involvement ended in the early 1990s and the firm exited its heritage brewing and pub retailing operations in the early 2000s. Whitbread today is a leisure retailer spanning coffee shops (Costa Coffee), budget hotels (Premier Inn) and a small portfolio of restaurants (Beefeater and Brewer's Fayre), names developed or acquired since the 1980s.

Although the firm's place in UK business and economic history is associated with brewing and the descendants of the founding family, one of its key influential managers was an outsider, Sir Sydney Nevile. In conjunction with his protégé, Colonel W. H. Whitbread, Sir Sydney was credited with repositioning the traditional working class male drinking den - the public house (pub) - as a respectable outlet for wider social enterprise (Mutch, 2010). However, it was during the 1980s that a new breed of outsiders, many from marketing backgrounds in firms such as Unilever, made the step change in the direction of branded leisure retailing. An early pioneer of the pub-restaurant concept in Beefeater (first outlet opened in 1974) and budget hotels in Travel Inn (first opened in 1987), the acquisitions of Berni Inn steakhouses, and franchise agreements for US brands Pizza Hut and TGI Fridays, signalled a brighter future as a retailer even before the second anti-trust investigation into the UK brewing industry.[1]

[1] *The Supply of Beer: A Report on the Supply of Beer for Retail Sale in the United Kingdom (*MMC, Cm 651) was published in 1989 after a three year investigation. It is commonly referred to as the 'Beer Orders' given the enforced separation of a large portion of the major brewers' public house estates. An earlier investigation in 1969, *Beer: A Report on the Supply of Beer* (MMC, HC 216) while concluding that certain industry practices acted against the public interest, did not impose a restriction on the 'vertical tie' between brewing and pub retailing assets.

The 'Beer Orders' was a defining moment for a traditional industry which had relied on its political patronage to deter regulatory intervention (Bower and Cox, 2012). Some firms fared better than others in its aftermath as new strategies emerged. The original 'Big 6' brewers of the 1960s merger wave (Gourvish and Wilson, 1994) exist today largely as the subsidiaries of a set of international brewers (Geppert, Dörrenbächer, Gammelgaard, and Taplin, 2013). That the Whitbread name survives, however, when its competitive set are largely consigned to history, owes much to a family culture and the attributes embedded in the Sir Sydney and Colonel Whitbread era, and a rudimentary definition of a pub as a wider and socially acceptable outlet. The Whitbread Umbrella was the structural mechanism which supported the emerging strategy in the post-World War II dynamic and unpredictable institutional environment.

In contextualising the Umbrella structure and the underlying strategy of Whitbread I adjoin the debate about successful organisational forms that appear to contravene a Chandlerian ideal (Mayer and Whittington, 2003) and in particular the description of Whitbread as a 'worst-in-class' performer as a result of its structure (Higgins and Toms, 2011). Widening the structural argument brings this business history literature into the realms of contemporary finance literature where researchers are seeking to understand why dual-voting ownership models are gaining traction in the previously devolved and democratic US stock market (Chemmanur and Jiao, 2012; Lauterbach and Yafeh, 2011). In addressing structure and strategy I also link to the dynamic capabilities literature of strategic management in highlighting how the past informs the future, in particular in times of institutionally imposed change. Notwithstanding the exit of the family and the break with the centuries-old brewing and pubs heritage that the Whitbread name sits proudly above the coffee-to-budget hotel combine is a subject worthy of detailed inquiry.

THEORETICAL BACKGROUND

This chapter proceeds firstly in outlining the historical backdrop to the emerging market for corporate control before turning to the attributes of organisational structure in the performance of firms. I then proceed to a contemporary debate regarding the role of protective shareholding structures which were common in the UK in the post-World War II era as well as in many European markets but which had not featured in the democratised US corporate sector until recently. Finally I introduce the dynamic capabilities literature of strategic management to contextualise the ability of firms to respond and adapt to external shocks through lessons from the past in firm history and culture.

The notion that 'structure follows strategy' is associated with Chandler and the Harvard Programme investigation of the organisational development of major US multinational enterprises after World War II (Burgelman, 1983; Chandler, 1962). The so-called 'M-form' divisional structure emerged in response to diversification strategies which required the devolution of decision making to the subsidiary level. Consequently the scale and scope of these firms led to the M-form structure replacing the predominantly 'U-form' holding company structure which had previously supported evolving strategies in both the US and UK (Shleifer and Vishny, 1991). Researchers have sought to extend the Harvard Programme to other contexts, both country and temporal to test the proposition that 'structure follows strategy' in different institutional settings (Mayer and Whittington, 2003, 2004) or to understand where modifications to an M-form might be beneficial, for example, in periods of turbulence where an 'entrepreneurial M-form' with a top-down approach driven by a strong central figure might be more appropriate (Eisenmann and Bower, 2000).

Central to a discussion about strategy and structure in the post-World War II era is the emergence of the market for corporate control. This performs the function of correcting management failure and 'hubris' (Roll, 1986) in instances where there is a misalignment of management and owner objectives, or 'principal-agent malfunction' (Jensen and Meckling, 1976). In the UK, notwithstanding legislation introduced in the 1948 Companies Acts, corrective mechanisms were hindered largely by inefficient and highly politicised institutional oversight (Bower and Cox, 2012; Roberts, 1992; Toms and Wright, 2002). Unlike in the US, where horizontal mergers were subject to strict anti-trust enforcement, underpinning diversification and subsequent 'M-form' structure (Shleifer and Vishny, 1991) UK firm diversification strategies proceeded as a function of capital market inefficiency, including dividend restrictions and aspects of the tax regime (Rowlinson, Toms and Wilson, 2007). Moreover, the idea that there was a 'one size fits all' or convergence towards a unique model of organisation and corporate governance was contradicted by evidence of '*path dependencies, punctuated equilibria and possible wrong turnings*' (Hannah, 2007, P 426), and a 'thirty year detour' from 1960-1980 when the conglomerate, or 'M form' was the popular structure (Shleifer and Vishny, 1991). Countries such as France and Japan, which pioneered shareholder democracy and the separation of ownership from control in the early 1900s, returned to protective (often family) holding structures after World War II. Where shareholder power resides with an elite group, they enjoy concentrated voting power over management decisions (Branston, Cowling and Sugden, 2006). As the recent past reminds us in the literature of 'financialisation' even in the now supposed devolved and democratic capital markets of the UK and US, not all shareholders are equal in overseeing important strategic decisions (Lazonick, 2010; Orhangazi, 2008).

One of the structural mechanisms firms have adopted historically to protect their often legacy family interests from capital market scrutiny, while retaining the benefits of a public listing, is a dual voting share arrangement. The origins of this in the UK are in the general avoidance mechanisms that allowed compliance with London Stock Exchange listing rules in the late 1800s and early part of the 1900s (Hannah, 2007). By issuing preference shares and/or debentures, it was common for a family to retain absolute voting control while owning only one-third of the securities. Today, these structures are typically associated with technology entrepreneurs and other dominant owners who seek to expand their firm without ceding control to outsiders (Lauterbach and Yafeh, 2011). The dominant or 'inside' shareholders retain a class of higher voting shares while public or 'outside' shareholders are concentrated in a class of lower or non-voting shares with commensurately higher dividend rights. Such dual class share structures have grown in popularity recently in the US to an estimated ten per cent of all listed firms, doubling since the 1980s. Their popularity is more significant elsewhere, in particular in Canada and in European capital markets (Chemmanur and Jiao, 2012). Theoretical modelling predicts that this structure is more likely in industries with high near-term uncertainty, where family ownership is significant and where there are large private benefits of control.

Notwithstanding frequent criticism from corporate governance specialists, the empirical evidence is not conclusive that dual class voting structures destroy shareholder value (King and Santor, 2008; Masulis, Wang and Xie, 2009). On the one hand, a large shareholder can exert stronger oversight of management and family-owned firms may make better investment decisions if afforded the luxury of a longer time horizon. On the other hand, the protection afforded from the market for corporate control can support insiders operating in their own self-interests at the expense of other stakeholders. Indeed, there is good reason to believe that the agent will not always act in the best interests of the principal (Jensen and Meckling, 1976, P308). In the case of family firms this may also mean extreme risk aversion that restricts investment decisions in the interest of protecting the family legacy (King and Santor, 2008).

In many respects the argument about 'structure' and 'strategy' relates not only to the situational (time-specific) perspective of performance but also a wider debate in strategic management related to the opposing perspectives of the 'top-down' versus 'bottom-up' paradigms in explaining firm performance. The 'Structure-Conduct-Performance' paradigm, with its origins in industrial economics (Bain, 1959; Caves and Porter, 1977; Porter, 1980) is considered weak in explaining why some firms appear to perform significantly better than their competitors notwithstanding general industry conditions (Rumelt, 1991). In contrast the organisational paradigm, with theoretical underpinning in the seminal work of Penrose (1959) and Nelson and Winter (1982) forwards the 'Resource-Based View' to explain firm-specific attributes in success and failure (Prahalad and Hamel, 1990; Wernerfelt, 1984). Nelson and Winter's (1982) biological analogy of firms as dynamic entities that evolve as a response to external signals provides the link from evolutionary economics to the concept of dynamic capabilities (Oliver and Holzinger, 2008), expressed as "*the act of aligning a company and its environment*" as a dynamic process (Porter, 1991, P 97).

In extending the theory of dynamic capabilities Teece, Pisano and Shuen (1997) considered how firms might exploit *existing internal* (author's emphasis) and external firm-specific competences to address changing environments. In this narrative, 'dynamic' refers to the capacity to renew competences to achieve fit with a changing business environment with 'capabilities' emphasising the key role of strategic management in adapting and internalising key skills and resources needed for the new environment (Teece, Pisano and Shuen, 1997, P 515). As part of the processes of adaptation and internalisation, routines are established (Eisenhardt and Martin, 2000; Pentland and Feldman, 2005). As part of the process of embedding routines firms, as part of 'trial-and-error' make mistakes; indeed, (small) failures provide the motivation to learn. Although mistakes are normally associated with internally-generated failure rather than those emanating from external shocks (Kim, 1998), dynamic capabilities are associated with change management and strategic renewal (Easterby-Smith, Lyles and Peteraf, 2009). Routines do not just preserve the past but pave the way for deliberate learning inside firms that shapes its future development (Winter 2000, 2003; Zollo and Winter, 2002).

I therefore seek to answer an issue arising in the 'structure follows strategy' debate in the recent business history literature where the Whitbread Umbrella was seen as a deterrent to positive performance (Higgins and Toms, 2011). In doing this I also aim to develop a deeper understanding of what constitutes dynamic capability in the context of long-term strategic change (Johnson, Yip and Hensmans, 2012). I present a historically-informed account of the transformation of Whitbread, from traditional brewer and pub retailer to leading European leisure retailer, supported by it 'entrepreneurial' M-form structure (Eisenmann and Bower, 2000).

WHITBREAD CASE STUDY

"*2001 was the year we became the company we are today. Our reinvention as the UK's leading hospitality business naturally coincided with the ending of this country's brewing and pub-owning tradition, started by Samuel Whitbread over 250 years earlier. Although our core businesses have changed, we remain true to Samuel's founding spirit by genuinely focusing on our customers, striving for the best and recognising that progress comes from innovative thinking*" (Whitbread plc).

Data and Methodology

I present findings from a multi-period, multi-source analysis of Whitbread drawing on data and information from two key periods in the firm's evolution. These periods are juxtaposed in a wider institutional context of change in the regulation of firms and industries and the prominence of the capital markets that has informed earlier studies for both this author and many others in related social sciences disciplines. I seek to inform a key debate regarding the importance of organisational structure in optimal strategy making and performance which spans both the business history literature and that of principal-agent analysis in the finance literature. I also, in presenting a second and later illustration link the current Whitbread to that of the past through an investigation of the dynamic capabilities and routines which were embedded to the extent that they provided a supporting platform for future survival and success in the face of adversity when the inevitable mistakes were made in the new, post 'Beer Orders' era. The unifying feature between the two eras is the group name, Whitbread and the social endeavour of serving UK consumers in their 'leisure' pursuits.

In addition to data and information collected in a related study of how some UK alcoholic beverages firms developed mechanisms to interacted successfully with the institutional constraints of competition policy, I also draw on private letters, file notes and board papers from the Whitbread archives housed in the London Metropolitan Archive, additional secondary information accessed in the Morland Brewery Company archive in the Oxfordshire Record Office collected during several visits in 2013. I have accessed other archive data and information of both a specific and official regulatory nature available online through the National Archives as well as contemporaneous information from media commentary, as indicated in the discussion below, and related studies in this industry.

The Whitbread Umbrella Era

The origins of the Whitbread group are in the brewery partnership formed by apprentice brewer Samuel Whitbread I and Godfrey and Thomas Shewell in 1742 (LMA/4453). Over the following two centuries, descendants of Samuel Whitbread, assisted by prominent outsiders such as Sir Sydney Nevile developed the firm as an integrated brewer-retailer. Prompted by the emergence of a market for corporate control in the post-World War II era (Roberts, 1992; Toms and Wright, 2002) Whitbread became the protector of a group of family-controlled regional brewers through a unique 'Umbrella' structure controlled by the Whitbread family (MMC, Cm 651, 1989). By the time of the 'merger wave' of 1968-72 (da Silva Lopes, 2002; Gourvish and Wilson, 1994) Whitbread had subsumed many of the original regional family brewery investments under its direct control. The structure remained in place until the provisions of the 1989 'Beer Orders' mandated divestment by November 1992 to comply with the pub ownership and control threshold, as described below, and a backdrop of a UK capital market increasingly antagonistic to complex family-inspired voting structures.

Whitbread entered the public arena as a result of an 'offer for sale' on The Stock Exchange on 5 July 1948. Although this was the first time ordinary share capital had been offered for sale to the public the fact that approximately 30 per cent of the "A" Ordinary Stock Units (one vote for every £1 stock) and 60 per cent of the "B" Ordinary Stock Units (one vote for every 1s stock) at inception remained in the beneficial ownership of the Directors was crucial to the future direction of the firm:

"*my earnest wish that the connection between my family and the Company may be maintained unbroken and that the very strong sense of tradition engendered by this long connection through generations may also continue hand in hand with the reputation for progressive management of the business, to which our record during the past two centuries entitles us, I think, to lay just claim*" (W.H. Whitbread, Chairman, LMA/4454/A/02/001).

The Whitbread Investment Company (WIC) was an investment trust comprising minority shareholdings in a large array of regional and family brewers which was incorporated on 8 March 1956, under the Companies Act of 1948 (Whitbread Investment Company Limited, Memorandum and Articles of Association, LMA/4453/A/02/001). Although WIC was a listed company quoted on the UK stock exchange it was *de facto* controlled by the Whitbread group, having been established and majority owned by the firm and members of the Whitbread family, with the chairman of Whitbread fulfilling the role of a main board director of WIC. Consequently, the aggregated public-private interests which also incorporated the underlying trading relationships with the regional brewers whose equity WIC owned were collectively known as the 'Whitbread Umbrella'. In reflecting on its merits as a protective structure the Chief Executive Officer at the time of the 1989 Beer Orders, Peter Jarvis, described WIC as a "*powerful force for stability in the beer market*" ('Whitbread puts end to two-tier voting structure: Brewing giant decides to purchase remainder of investment company', *The Independent*, 7 October 1993).

As explained in the Beer Orders inquiry (MMC, 1989, Cm 651: Pages 183-184), the backdrop to the establishing of WIC was the emergence of the market for corporate control following the 1948 Companies Acts legislation. Fearing that their independence was at risk from hostile approaches, a group of family-controlled regional brewers with attractive city-centre pub property portfolios sought the guardianship of Whitbread, which obliged with equity investment in return for formalised trading agreements. In some cases a more substantial relationship ensued with a Whitbread director joining the board of the regional brewer. As the 1950s progressed, Whitbread expanded the number of such relationships before ring-fencing them inside the dedicated WIC structure.

The controlling relationship between WIC, Whitbread and the Whitbread family was cemented in WIC's strategy of accepting Whitbread 'A' (ordinary) shares in lieu of payment for Whitbread's acquisition of the controlling rights of some of WIC's investments and the purchase of high voting 'B' shares from Whitbread family members when they became available. By the time of the 'merger wave' of 1968-72 (da Silva Lopes, 2002; Gourvish and Wilson, 1994) Whitbread, via the agency of WIC, had brought under full ownership and control the majority of the original 20 regional brewery investments (MMC, Cm 651: Page 183, para 6.89). Consequently, Whitbread became one of the largest national brewer-retailers through the sequential absorption of the smaller firms in the Umbrella while being itself protected from the gaze of the capital markets, the complexity of the arrangement, seen as an effective deterrent to hostile approaches at a time when many entrepreneurs (Charles Clore, Maxwell Joseph, and Canadian brewer E.P Taylor) had spotted attractive investment opportunities in traditional brewery assets. The continuation of the structure through the aggressive merger wave of the 1980s was also important; competitors Allied-Lyons and Scottish & Newcastle were both on the receiving end of hostile approaches from Australian finance and brewing conglomerate, Elders IXL.

How the Umbrella worked in practice: The Whitbread Umbrella was a firm-conceived solution to institutional change in the post-World War II period and the emergence of managerial capitalism (Rowlinson, Toms and Wilson, 2007). Much has been made of the role played by Colonel Whitbread as the industry's protector. The Colonel, who had been managing director of the group since 1927, succeeded Samuel Howard Whitbread as group chairman in 1944, and remained in that role until 1971 (Colonel W. H. Whitbread, Obituary, *The Times*, 30 November, 1994). Yet behind the gloss of respectability, the motives of Whitbread as a driven and purposeful consolidator in its own right are clear in both wider consumer circles if not the contemporaneous notes and letters of the Colonel's mentor, Sir Sydney Nevile. That the Umbrella might not have acted in the best interests of the operation of the wider brewing industry was summed up in a Campaign for Real Ale poster which described the arrangement as:

"*A fine idea in principle, but as the murdered diplomat Gregory Markov discovered, an Umbrella can be a pretty nasty weapon in the wrong hands*", (CAMRA poster, June/July 1988).

That Whitbread might have had an ulterior motive in the formation and operation of the Umbrella that worked against the interests of the smaller brewers was the position of CAMRA in its aggressive lobbying effort in the run up to final deliberations in the 1989 anti-trust inquiry. Support for such a proposition can be forwarded in interpretation of some of the letters and file notes from Sir Sydney Nevile's personal collection in the Whitbread archive (LMA, 4453/A/09/069). Having been considered one of the most influential figures in the twentieth century UK brewing industry, from his position as chairman of the Brewers' Society and association with the 'improved public house movement' (Mutch, 2010), on his retirement as Managing Director of Whitbread on 31 December 1948, Sir Sydney remained a Director of the Company under a renewable 'Services Agreement' with a brief to further the interests of the firm (LMA, 4453/A/01/005, Pages 165-166). In this specially created post-retirement role he was a 'roving ambassador' for Whitbread and *de facto* in-house investment banker. So for example, at the time of the creation of WIC in 1956 he was sent a 'Highly Confidential' letter inquiring:

"*Would your Company be interested to purchase a Scottish brewery in Edinburgh, G. Mackay & Co Ltd? Like many people nowadays certain shareholders are getting alarmed at the situation that might arise in event of the death of certain shareholders. For this reason it has been decided to consider disposing of the whole business*" (Letter of 5 November 1956 from Mr Douglas Winter of John M Winter & Sons, St Jame's Street, London).

Sir Sydney's subsequent note to Whitbread's Managing Director, Charles Tidbury of 23 January 1957, revealed perhaps the true nature of Whitbread's intent:

"*I think we need from Winter the list of houses by Mackays with their addresses and trades. We should then have the houses inspected from the outside and some of them visited as ordinary customers inside avoiding as far as possible any idea of Whitbread's interest*"

The objective of the Umbrella was to support the strategy of Whitbread while retaining the family's investment for future generations. As the 1950s progressed financially motivated consolidation of the UK brewing industry became increasingly apparent and Whitbread sought a wider role than mere 'protector' of a string of family brewers. Charles Clore's failed hostile bid for Watney Mann in 1959, and the aggressive expansionary objectives of Canadian brewing magnate, E.P. Taylor, prompted the 'defensive' consolidations that led to the emergence of the 'Big 6' (Gourvish and Wilson, 1994, Pages 460-461). That Whitbread might insert itself in a statesman-like manner into a topical debate about the role of finance and its short-term impact on the industry's operation and structure is clear from the note of a meeting between Sir Sydney and Dudley Robinson, MD of

Burrough's Wellcome Ltd, and board member of the Independent Commercial Finance Corporation:

"*Whitbread's policy (is) to associate ourselves with other companies and keep them alive rather than completely absorbing them......I suggested that the interest of his company was merely to speculate in shares and then sell them to the highest bidder, which was not Whitbread's line*" (File note of 27 March 1961).

Yet, as time moved on, many of the initial investments of the 1950s-1960s were fully absorbed into the Whitbread group, prompting the criticisms of the campaign group CAMRA, as discussed above. As part of the 1989 Beer Orders the major brewers were forced into the '*draconian*' measure of dismantling large parts of their vertical tie (*The Supply of Beer: A Report on the Review of the Beer Orders by the Former DGFT*, OFT 317, 2000). Under the provisions of the 'Tied Estate Order' of the 1989 legislation Whitbread was defined as a 'brewery group' and was therefore forced to choose between selling its own pubs and reducing WIC investments to the 15 per cent threshold ownership level. An ensuing internecine conflict between two of the larger regional Umbrella holdings in many ways cemented the latter over the former. Greene King's 1992 hostile approach for Morland pitted one WIC investment against another. Morland was the longest duration relationship in the Umbrella and indeed, Colonel Whitbread had been a director of the Abingdon, Oxfordshire-based brewer in the 1950s (Morland archive, History Centre, Oxfordshire County Council, 22 November 1957). Greene King's hostile approach for Morland coincided with the November 1992 deadline for compliance with the Beer Orders and in so doing provided a potential exit route for WIC's investment in Morland. In its initial defence document of 4 June 1992, Morland referred to WIC as a 'forced seller' of its 43.4 per cent stake. Greene King had struck a direct deal with WIC to acquire 28.5 per cent of it to provide a platform for the hostile bid (*Final offer by Robert Fleming on behalf of Greene King*, 10 July 1992, History Centre, Oxfordshire County Council). Although ultimately unsuccessful, the Greene King bid undoubtedly informed the decisions to disband the Umbrella, and in addition the dual voting share structure during 1993 and 1994.

The Leisure Retailing Era

While much attention has focused on the UK beer producers and the associated international spirits market, spanning the literatures of business history, industrial economics and strategic management (Bower and Cox, 2010; Da Silva Lopes, 2002; Geppert, Dörrenbächer, Gammelgaard and Taplin, 2013; Nalebuff, 2003; Slade, 2011) much less has been written about the remainder - the public houses and wider leisure assets of the former brewers. Here, Whitbread is a notable survivor of a period of considerable institutionally-imposed upheaval and is an example of a firm which fundamentally reshaped its business under the guise of regulatory intervention, if not emanating from the financial markets (Johnson, Yip and Hensmans, 2012). It left the traditional brewing operation behind in carving out a leadership position as a focused UK leisure retailer.

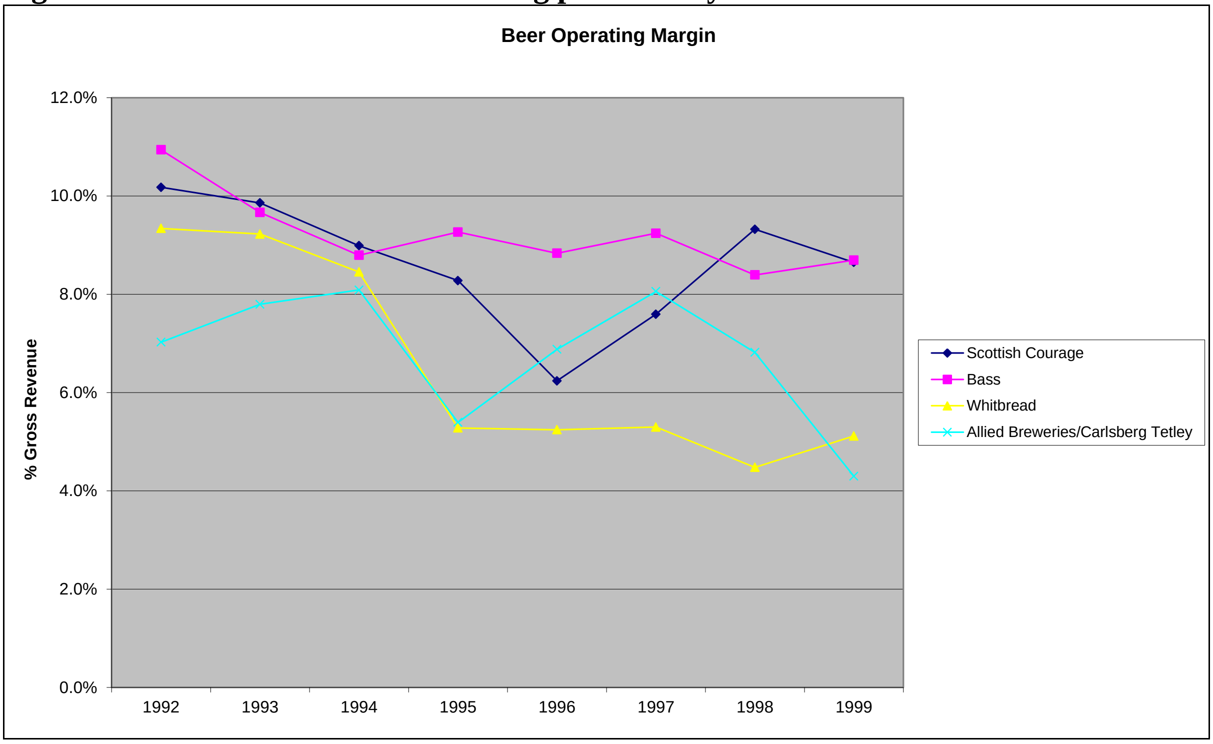
Whitbread has been cast as a 'worst-in-class' firm in historical studies (Higgins and Toms, 2011). This analysis considered the structure, strategy and performance characteristics of pairs of competitors in the period 1950-1984 as a function of their returns on capital. Referring to the earlier work of Mutch (2006), Whitbread's relative underperformance was seen as emanating from its unique type of 'M-form' structure – in many aspects one might argue it was more akin to an 'entrepreneurial M-form (Eisenmann and Bower, 2000) - the Whitbread Umbrella. This was seen as a deterrent to much needed rationalisation of inefficient brewing capacity in both Whitbread and the associated regional sector. The firm was also criticised as much for lacking strategic ambition as the experience to operate as an effective 'M form' organisation (Higgins and Toms, 2011, Page 107). Yet the Umbrella, in providing the context, as well as the support for the evolution of the leisure retailing approach initiated by Sir Sydney Nevile, may be the very reason why the Whitbread name survives. Not only is a reliance on return on capital measures for an industry endowed in property assets problematic[2], but to define Whitbread as a national brewer in the context of the other 'Big 6' brewers in many respects is to miss the point. As the 1980s progressed it became clear that brewing, in common with spirits was internationalising. None of the 'Big 6' UK brewers was able ultimately to establish a strategic position in the international beer market, notwithstanding the valiant attempts of Scottish & Newcastle in the 2000-2007 period (Geppert et al, 2013). Recasting Whitbread as a leisure retailer, embedding the culture and competence of the long-term property investment game under the protection of a supportive Umbrella allows strategic inference to be drawn that transcends the cut-off point of 1984 in the earlier study.

During the 1980s, as the eating-out market developed in the UK, in particular in the South-East of England, Whitbread's position as the pre-eminent competitor in this market became increasingly apparent; retailing increased from around one third of Whitbread's profits to one half by the start of the 1990s as a result of the combination of aggressive organic investment as well as acquisitions such as Berni Inn steakhouses. However, in an environment when vertical integration was the dominant industrial architecture Whitbread's expansionary spending in upgrading its managed estate of pubs and pub-restaurants was the source of much City criticism (Whitbread beer mission may knock down family skittles, *The Guardian*, 26 September 1992). Consequently, by the time of the Beer Orders, the decision to sacrifice brewing for a stronger position in retailing was already an open secret. The decision to formalise a visible separation of the brewing and retailing operations was taken in altering the terms of the transfer pricing arrangement between the brewing and retailing operations. That this reflected the market conditions of the 1990s revealed even more starkly the weak competitive position in brewing, as shown in Figure 1 below.

[2] In the first anti-trust inquiry of the UK brewing industry in 1969 (MMC, HC 216), confidential information was given to the Commission by the major brewer-retailers about their financial performance (Appendix 12: Page 172). The Brewers' Society made representations regarding the apportionment of profit and returns to one activity relative to another given the vertically-integrated operating structure. The Commission accepted this position (Page 173, para 7). The Commission considered that the use of total capital employed as a measure of performance was problematic due to the historic cost versus re-valued cost of premises (not all of the 11 brewers re-valued their property portfolios and the methods and timeframe used differed), the inclusion of goodwill in the calculation of capital employed by some, but not all brewers, and of particular importance for Whitbread, the treatment of trade investments, where the investment was of sufficient trading importance to the brewer that it should be included in capital employed calculations.

In the second anti-trust inquiry in 1989 there was a more extensive financial and economic analysis of the vertical tie by a less malleable MMC. The issue of valuation of the brewers' estates was clarified for the purposes of establishing returns under 'economic rent' criteria (Cm 651, Page 409). Whitbread submitted evidence to indicate a wide variation in 'open market' rental yields and consequent returns on capital employed for pubs dependent on location, quality of outlet and whether the outlet was in a major city; the yield range quoted was 6 per cent in prime London locations to up to 20 per cent for poorly trading pubs in secondary cities (Page 409, para 8). Quantifying the 'trading benefit' from the minority shareholdings in the Umbrella was therefore complex, although in evidence WIC claimed that over the previous ten years it had outperformed the *Financial Times All-Share* index and the brewers' index (Page 184, para 6.92).

Figure 1: Post Beer Orders UK brewing profitability



Source: Company accounts

The formal break with the family in both management – the appointment of Sir Michael Angus from Unilever as chairman to replace Sam Whitbread - and the disbanding of the Umbrella and dual ownership structure in 1993 and 1994 corresponded to the internal decision on transfer pricing of the brewing operations. It was at this stage that expectations surrounding a major strategic move in retailing gained traction, with the new chairman having commented in the prior year that the voting structure would be sacrificed:

"*If in the future, we wished to do something on a scale that involved financing that could involve equity*" (*The Guardian*, 26 September, 1992)

The Allied Retail 'fiasco': The opportunity for such a transformative acquisition came in the aftermath of the restructuring of the international spirits industry, prompted by the 1997 merger of Grand Metropolitan and Guinness to form global leader Diageo (Bower and Cox, 2013). This landmark merger forced a strategic reappraisal at the remaining two international spirits firms, the UK's Allied Domecq and Canada's Seagram (these two firms had considered merging in the late 1980s and rumours circulated again during the mid-1990s of a similar transaction even before the Diageo deal). Having recently exited brewing through a two-stage agreement with Carlsberg[3], the impetus for change at Allied Domecq was prompted by the arrival in 1996 of respected industrialist Sir Christopher Hogg as group chairman. On 25 May 1999 Whitbread announced that it had reached agreement to acquire Allied Domecq's UK retail portfolio for the equivalent of £2.4bn, by way of an equity offer of Whitbread shares to Allied Domecq shareholders ('Whitbread's £2.4bn is accepted by Allied', *The Guardian*, 26 May 1999).

The announcement was well received by the stock market. However, within a matter of a month the euphoria began to unwind as first private operator Punch Taverns, acting in partnership with Bass, entered the bidding for the Allied operations, closely followed by the

[3] *Allied-Lyons PLC and Carlsberg A/S: A Report on the Proposed Joint Venture* (MMC, Cm 2029, 1992); *Bass PLC, Carlsberg A/S and Carlsberg-Tetley PLC: A Report on the Merger Situation* (MMC, Cm 3662, 1997)

intervention of the regulatory authorities. The Secretary of State for Trade and Industry's July 1999 decision to refer the Whitbread (but not the Punch Taverns/Bass counterbid) acquisition to the Competition Commission for a full investigation was based on the advice of the Director General for Fair Trading (DGFT) that it:

"*...raises competition concerns in respect of the market for brewing and on-licence retailing in the UK*" (DTI Press Release, P/99/611)

This announcement was a surprise not just to the management of Whitbread, which had concluded from private 'soundings' with the DGFT that the merger would proceed unopposed, but to the wider industry. Two days after the announcement of the referral, Whitbread abandoned the merger. As evident from Figure 2 below, the sharp downwards movement in the firm's share price during 1999, and one that continued into the early 2000s, marred much of the tenure of the merger's instigator, David Thomas's time as chief executive officer of Whitbread. Commentary pointed to a DGFT irate at David Thomas making public his interpretation of confidential discussions:

"*Whitbread's purchase of Allied Domecq's retail arm was considered a done deal until the chief executive said too much and Punch Taverns stepped in*" (The Lawyer, 13 September 1999).

The high-profile failure to secure the Allied Retail operation, in what would continue to haunt the management of the firm and restrict significantly its enthusiasm for future mergers and acquisitions, might have ordinarily led to a strategic impasse. Yet in May 2000 the group carried through in the pledge to exit brewing, and as part of a wider strategic review, proceeded to refocus its operations around restaurants, hotels and leisure. The criticism of David Thomas continued however, notwithstanding the public support from group chairman, respected industrialist Sir John Banham:

"*There are only two types of chief executive: those whose reputations outrun their achievements; and those whose achievements are only recognised with hindsight. David Thomas falls into the latter camp*" ('Doubting Thomas' in *Director*, September 2001).

A more fitting legacy for Mr Thomas, who was chosen to run Whitbread in 1997 for his significant achievements during the 1990s in developing the managed pubs and leisure subsidiaries, is the profile and positioning of Travel Inn (now known as Premier Inn following the £536m acquisition of Premier Lodge in 2004), the 1995 acquisition of David Lloyd sports clubs for £200m (later sold for £925m) and, most significantly, the 1995 acquisition of Costa Coffee for £20m (*The Telegraph*, 23 October 2010). Established in London in 1971 by Italian brothers, Sergio and Bruno Costa as a coffee roasting operation, when purchased Costa was a £55m turnover chain of 41 coffee shops thinly spread across the UK (*The Herald Scotland*, 19 September 1995). Within Whitbread, Costa is now a £570m turnover business of which £81m is derived from overseas, generating profits of some £90m. It has more than 2,500 outlets, with an increasingly diverse international footprint of 692 stores in Europe, Middle East and India and 257 stores in China and South East Asia (Whitbread, 2013). The capital markets would later acknowledge the potential in Costa and Travel Inn as shown in Figure 2 below and considered on Mr Thomas's departure from Whitbread in 2004:

"*With hindsight (the failed Allied deal) was a blessing in disguise, forcing him and the board into some ruthless choices: about their declining beerage inheritance*…" (Lombard, Financial Times, 6 May 2004).

Figure 2: Whitbread share price relative to FTSE 100 index since the Allied Retail bid

Source: Google Finance (UK)

On replacing Mr Thomas, Alan Parker, described the need to elevate Whitbread's returns and as part of this objective, it was clear from the return on capital of 30 per cent and the backdrop of a growing but fragmented market why Costa Coffee was s suitable replacement for brewing and pub retailing as the future focus for Whitbread. Alluding to the deep-seated culture and competence of Whitbread that underpins this he noted:

"*I'm absolutely convinced that nobody could have run and developed Costa better than us*" (*The Telegraph*, 23 October 2010).

CONCLUSIONS

My case study set out to identify and explain the reasons why Whitbread has survived and ultimately prospered beyond its history in the vertically-integrated UK brewing industry to become one of Europe's largest leisure retailers with interests in coffee shops (Costa Coffee), budget hotels (Premier Inn) as well as family restaurants (Beefeater and Brewers Fayre). The main contribution of my article is in demonstrating the importance of history and context in understanding survival and corporate transformation.

A significant factor in the transformation of this patriarchal and traditional brewer was the ability to remain independent in the immediate post-World War II era, when financial entrepreneurs spotted opportunities in the extensive city-centre property portfolios of the brewers. During the 1980s merger wave, which predated the second anti-trust inquiry into the industry's vertically-integrated architecture, the firm's ownership structure was enough to deter even the hint of an aggressive approach at a time when other Big 6 brewers, Allied-Lyons and Scottish & Newcastle, were under attack from the next generation of entrepreneurs.

The formation and duration of the 'Whitbread Umbrella', which incorporated a dual voting structure and tight arrangement with a group of smaller regional and family brewers under the investment trust banner of the Whitbread Investment Company, was crucial in allowing a longer term strategy to emerge and flourish without the intervention of the capital markets. Continuing the theme of the influential Sir Sydney Nevile and his 'improved public house movement' (Mutch, 2010), the modus operandi of his protégé, Colonel Whitbread, has been the subject of strategic as well as organisational criticism (Higgins and Toms, 2011). However in considering the re-positioning of the firm in the 1980s as the pre-eminent leisure retailer - the only name from the Big 6 era to remain – and the platform it created for continued innovation in the rapidly changing consumer markets, a reappraisal of its performance is appropriate. In this sense the reasons for, and potential benefits of, a supportive share and ownership structure in a rapidly changing institutional environment add historical context to current trends in the US capital markets which have puzzled scholars (Lauterbach and Yafeh, 2011). This long-term strategic transformation stands in stark contrast to the contemporary and frequently finance-driven business models of the 'financialisation' era after the 1980s merger wave (Lazonick, 2010; Orhangazi, 2008; Shleifer and Vishny, 1991).

By the time the Umbrella had outlived its usefulness the firm was a self-supporting branded leisure retailer which acquired and nurtured Costa Coffee and Premier Inn. The culture and capabilities of 'social service' and which underpin the transition from brewer-pub retailer into the wider leisure industry are encapsulated in the commentary of successive generations of Whitbread managers; most notably Mr Parker's view that only a firm such as Whitbread could have delivered the evident success of Costa Coffee. That the firm was able to chart a path after the highly public embarrassment of the failed Allied Retail merger owes much to its embedded culture. It is an illustration of what Teece, Pisano and Shuen (1997), in coining 'dynamic capabilities', consider how firms might exploit existing internal as well as external competences to address changing environments. Consequently, Whitbread's strategic transformation, prompted by significant change in its institutional environment, informs several topical academic debates in finance and strategic management.

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