

Conclusions

The merger situation

7.1. Under the terms of the reference and the relevant sections of the Fair Trading Act 1973 we are required to investigate and report whether arrangements are in progress or in contemplation which if carried into effect will result in the creation of a merger situation in which the condition set out in section 64(1)(b) of the Act will be satisfied.

7.2. On 18 March 1985 Scottish & Newcastle announced that it intended to make an offer for Matthew Brown, and on 3 April 1985 an offer was made by Morgan Grenfell & Co Limited on behalf of Scottish & Newcastle to acquire all the Matthew Brown ordinary shares which it did not already own. The offer lapsed on reference being made to the Commission, but it is clear that the acquisition of Matthew Brown is still in contemplation by Scottish & Newcastle.

7.3. The assets of Matthew Brown exceed £30 million (see Table 4.2) and the condition set out in section 64(1)(b) of the Act is therefore satisfied.

7.4. We conclude that arrangements are in contemplation by Scottish & Newcastle Breweries plc for the acquisition of Matthew Brown PLC which if carried into effect will result in the creation of a merger situation qualifying for investigation.

The public interest

Competition

7.5. In considering the likely effects of the merger on competition, it is necessary to distinguish between the on-trade, which is characterised by large numbers of brewery-owned tied outlets, and the off-trade (or take-home trade), in which although there are some brewery-owned off-licence outlets vertical integration is a much less important feature and major supermarket retail chains play an important part. In our view the merger would be likely to have no significant effect on competition in supply to the off-trade.

7.6. As regards the on-trade, it was represented to us that one of the principal consequences of the merger would be its adverse effects on competition in two distinct areas of the country—North and West Cumbria and the North-East. In the nine licensing divisions of North and West Cumbria Matthew Brown is at present by far the largest owner of tied houses, with about 40 per cent of the total. Scottish & Newcastle has few tied houses in the area, and the merger would therefore have little effect on competition as far as tied houses alone are concerned. However, it was argued that, since tied houses, free houses and clubs were all in competition with one another for the custom of the consumer, it was relevant to take account of the total number of on-trade outlets at present being supplied by the two companies. Against this it was argued that to take account of free outlets, both pubs and clubs, would overstate the effects

of the merger since free outlets can almost always, even when they have outstanding loans from brewers, readily switch to another supplier. We recognise that free outlets can indeed change their suppliers; but we accept that free houses and clubs compete for customers with tied houses, and we think that it is not irrelevant to consider the position in respect of all on-trade outlets supplied by the two companies as it would be immediately after the merger. Taking tied houses and free houses ¹ together, Matthew Brown's present share is just under a third and the combined total for the merged company would be about a half. If clubs ¹ are included Matthew Brown's present share is about 31 per cent and the combined total for the merged company would be just over half.

7.7. On the face of it, therefore, there would be a significant increase in the proportion of on-trade outlets being supplied by the merged group. However, we agree with Scottish & Newcastle that it is necessary to consider in detail what the effects of this situation on competition would actually be.

7.8. First, there is the ability, which we have already mentioned, of free outlets (both pubs and clubs) to change their supplier; they may choose not to do so, but the fact that they are able to means that to that extent they can protect themselves from being exploited by their supplier. Secondly, although there would be some increased concentration of outlets being supplied in North and West Cumbria, we do not accept that this is a meaningful concept as regards brewers competing for the custom of free trade outlets. Cumbria is not an isolated, self-contained area for purposes of competition; there is no physical or geographical factor to prevent all the national brewers and all those regional brewers that operate in the North-West from competing for free trade business there. Many in fact do so, and we do not consider that the merged company's increased share in Cumbria would affect the other brewers' ability to continue to do so. The number of separate brewers competing in the area would, of course, be reduced by one as a result of the merger; but although the loss of Matthew Brown as a separate competitor is a matter that we consider below in a wider context, we do not consider that reduction by one in the number of competitors in Cumbria has any special significance.

7.9. Thirdly, from the point of view of the consumer and the effect on the consumer of increased concentration, it is not meaningful to consider an area the size of North and West Cumbria or even one the size of a licensing district within it. The relevant area for consumers is typically the individual town or even village. There are towns or villages where the preponderance of outlets is supplied either by Matthew Brown or by Scottish & Newcastle and there are a few villages where the only outlet is supplied by one or other of them; but on the information available to us we believe that there is no town or village big enough to support a number of pubs where, as a result of the merger, there would not still be an adequate number (having regard to the size of the population) of outlets supplied by brewers other than the merged company. Even where there would be a majority of outlets supplied by the merged company a substantial proportion of such outlets would be free houses or clubs, which could, as has been pointed out, change their supplier.

¹Excluding those currently supplied by more than one supplier.

7.10. In the North-East Matthew Brown has fairly recently begun to acquire free trade accounts, and expects to continue to do so. It was argued that it was against the public interest that this new competition to Scottish & Newcastle in the area should be eliminated. We agree that in principle the elimination of Matthew Brown as a separate competitor would be undesirable, but the company's presence in the North-East has not yet become a significant factor in competition there and we doubt whether in the foreseeable future it would become so. We do not therefore consider the likely effects of the merger on competition in the North-East amount to a material public interest detriment.

7.11. The remaining areas where Matthew Brown is active in the on-trade are Yorkshire and Lancashire. In both these areas Matthew Brown is to some extent in competition with Scottish & Newcastle, though in Yorkshire this is mainly because of Matthew Brown's recent acquisition of Theakston. However, in both Yorkshire and, to a lesser extent, in Lancashire the merged company would have only a minor share of the on-trade, and we consider that competition in those areas would not be significantly affected.

7.12. It is relevant to consider the effects of the elimination of Matthew Brown as an independent competitor not only in particular areas but also on competition in the brewing industry as a whole. The wider implications for competition need to be considered against the background of the fact that significant features of the brewing industry are the degree of concentration and the extent of vertical integration. Over 75 per cent of the sales of beer are in the hands of the 'Big Six', each with national coverage and (with the exception of Scottish & Newcastle) with large estates of several thousand tied houses amounting together to about a quarter of the total number of on-licensed premises. It was argued that the five largest national tied estate brewers enjoyed substantial advantages arising from the size of their tied estates, from their ability to take advantage of the current trend away from ale and in favour of lager and in particular to incur the heavy expenditure necessary for the advertising and promotion of national brands of lager, and from their ability to survive and prosper in the increasingly important take-home trade which is now largely in the hands of major retail chains and where the brewers' margins are consequently under pressure. Scottish & Newcastle claimed that the advantages were so great that regional brewers, including Matthew Brown, would in the long run be unable to compete effectively and would cease to be independent.

7.13. Even if it were accepted as likely that Matthew Brown would cease to be an independent competitor, this by itself would have no bearing on the effect on the public interest of the present merger since if the merger takes place Matthew Brown will indeed, and with certainty, cease to be an independent competitor. However, Scottish & Newcastle claimed that it was itself at a disadvantage *vis-à-vis* the five major brewers with national coverage and large tied estates and that, particularly in the North-West, its ability to compete would decline if it did not acquire Matthew Brown. The merger was thus represented as being positively in the public interest because of the enhancement of competition through Scottish & Newcastle's increased ability to compete with the five national tied estate brewers, with no detriment to competition through the disappearance of Matthew Brown as a separate competitor since that would occur in any case.

7.14. We have referred in paragraph 2.27 to the conclusion reached by the Price Commission in 1977 that the combination of high concentration and vertical integration in the industry had made entry into it more difficult and had resulted in price leadership by managed houses, the effect of which had been to lead prices up. We accept that these are the likely consequences of high concentration and vertical integration, and that the maintenance, and if possible enhancement, of competition to the major national tied estate brewers and the prevention of further concentration are therefore matters of concern to the public interest. The acquisition of Matthew Brown might do something to enhance Scottish & Newcastle's ability to compete with the national tied estate brewers, but we do not think the effect could be very great because Scottish & Newcastle would still be much smaller than any of them in terms of national tied estate.

7.15. We do not accept that Matthew Brown will in any case, even if it is not acquired by Scottish & Newcastle, disappear as an independent competitor. It seems to us that it can be no more than a matter of speculation that Matthew Brown will not continue as an independent regional brewer. In our view the prospects for the company's continued survival and prosperity are good and we see no reason why the company should cease to be an independent competitor in the foreseeable future. In the absence of the merger there is at least the possibility (and, we believe, the probability) of its remaining independent: if the merger takes place there is the certainty that it will not.

7.16. We consider that in the interests of healthy competition, and also in the general interests of the areas in which they operate, it is desirable that there should continue to be viable and vigorous regional brewers. But this does not mean that no mergers involving regional brewers should be allowed to take place. There may well be a strong case on public interest grounds against acquisition of a regional brewer by any of the five largest national tied estate brewers, but we are not convinced that in the interests of averting further concentration there is a strong enough case to prevent the acquisition of Matthew Brown by Scottish & Newcastle.

7.17. As far as competition is concerned our view is, therefore, that there are not sufficient grounds for concluding that the merger would be against the public interest on account of its effects on competition either in particular geographical areas or in the brewing industry as a whole.

Prices

7.18. It was represented to us that beer prices in the present Matthew Brown tied houses would be likely to rise if the merger took place. It was asserted that the national brewers on average charge more for comparable products than do regional brewers and also that Scottish & Newcastle's regional prices tend to be higher than those of Matthew Brown. Therefore, it was argued, Matthew Brown's prices would rise since Matthew Brown's beers would not be allowed by Scottish & Newcastle to retail at less than its own beers where the outlets were in competition or where both beers were being sold in the same outlet.

7.19. Retail beer prices in any area differ according to the quality of the outlet in which the beer is sold, and also according to the type of bar in any particular outlet; and price differences are therefore not meaningful unless the

outlets concerned are comparable. Price surveys were submitted to us by both Matthew Brown and Scottish & Newcastle; but, because of the necessity to make subjective judgments about the comparability of outlets, we consider that it would be unsafe for us to reach any general conclusion about the relative levels of their prices. There would be some scope for increasing prices following the merger since price is unlikely to be the only factor which determines a consumer's choice of beer or of pub—the perceived quality of the beer and the general atmosphere of the pub are also important factors. Nevertheless competition would in our view be generally likely to impose a limit on the extent to which prices could be increased, and we do not think that the merger would have any markedly adverse effect on prices.

Consumer choice and service to the public

7.20. Scottish & Newcastle argued that, although the two companies each had a wide range of beers, they did not duplicate one another but tended to be different in character and in their appeal to consumers and were therefore complementary ranges. Consumer choice would, according to Scottish & Newcastle, be enhanced because Matthew Brown beers would, as a result of the merger, have a wider distribution and because both free trade outlets and the tenants or managers of tied outlets would have a wider range of beers from which to choose and, where space permitted, would be able to have a wider range on sale to the consumer.

7.21. Matthew Brown, on the other hand, argued that the two ranges of beers were largely similar and that it was inevitable that after the merger there would be some rationalisation resulting in the elimination of some brands. Consumer choice would thus be reduced. Moreover Matthew Brown claimed that in practice space would frequently not permit the stocking or display of a wider range of draught beers and that in the smaller pubs there would be insufficient demand for a choice of cask-conditioned ales to be practicable since these keep for only a short time once they have been opened.

7.22. It appears to us that these arguments are not mutually exclusive. There may well be some rationalisation of the two ranges, but it seems unlikely that this would be drastic since Scottish & Newcastle is anxious to take advantage of the local image enjoyed by Matthew Brown's beers in the North-West and Cumbria. Thus, although consumer choice could be reduced by the disappearance of some brands, there could still be a wider range of beers available to the outlets of both companies than the outlets of either company had had previously. In our view, however, it is unlikely that consumer choice would be either adversely or beneficially affected by the merger to any significant extent.

7.23. It was represented to us by opponents of the merger that in some areas there would be a loss of amenity to the public because some of the smaller pubs owned by Matthew Brown would be closed if the merger took place. In support of this contention it was asserted that Scottish & Newcastle had a policy of closing pubs taking less than five barrels a week. We were assured that in fact Scottish & Newcastle has no such policy. It is, however, its policy to review the viability of its smaller tied pubs, and in some cases to dispose of them to individuals willing to run them as small, probably part-time, businesses; in that event Scottish & Newcastle would seek to continue to supply them. We do not see closures of pubs as being a material consequence of the merger.

7.24. Our attention was drawn to the substantial extent of Matthew Brown's involvement in local and regional community affairs, particularly by way of sponsorships including that of sport. We accept that Matthew Brown makes a valuable contribution in this respect, but we think that this is a normal commitment for a brewer and we are satisfied that Scottish & Newcastle's contribution is no less valuable. We do not therefore think that the benefits of Matthew Brown's involvement would be put at risk if the company were to come under the control of Scottish & Newcastle.

Employment

7.25. It was generally assumed by opponents of the merger that there would be substantial loss of employment as a result of closure of some, or even all, of Matthew Brown's breweries. It is possible that some of the breweries might be closed following the merger; but Scottish & Newcastle assured us that it would not close Blackburn or Masham. This was expressed as follows: 'We have stated categorically, publicly, and in writing that without any question whatsoever the Blackburn and Masham breweries are sacrosanct for continued brewing purposes'.

7.26. No such assurance was given in respect of the Carlisle and Workington breweries. Indeed Scottish & Newcastle told us that 'the continued operating of all four breweries of Matthew Brown could prove uneconomic in the longer term, and a programme of rationalisation could result in brewing being discontinued at Workington or Carlisle or both'. There are about 60 employees at Carlisle and about 110 at Workington, of whom only about a half are employed on brewing. The total number of jobs at risk from the possible closure of the breweries would not therefore be great, but the effect would be particularly marked because the losses would occur in areas of very high unemployment.

7.27. Scottish & Newcastle argued that if these losses were to occur they could not be attributed solely to the merger since it was likely that in due course the Carlisle and Workington breweries would be closed by Matthew Brown even if the company remained independent. Matthew Brown, on the other hand, although not giving any categorical assurance that the breweries would never be closed, emphasised that it was its policy to keep them open. We accept that Matthew Brown has no present intention of closing these two breweries, but we believe that in the long run the closure of one or both of them might come to appear to Matthew Brown to be inescapable in the interests of greater efficiency and cost saving. We believe that, whether the merger takes place or not, the future of these breweries cannot be regarded as totally secure.

7.28. Scottish & Newcastle's record in connection with the closure of the Holyrood Brewery in Edinburgh appears to have been good and to have been recognised as such by the Transport and General Workers Union. If this merger takes place there may well be greater difficulty in implementing similar procedures because of the absence of Scottish & Newcastle locations in the areas concerned; but we were given in some detail an account of the company's policy and practice in relation to manpower reductions and we believe that the company goes to considerable lengths to implement a policy designed to alleviate as far as possible the consequences of closures.

7.29. Scottish & Newcastle told us that rationalisation of certain functions other than production could be expected to lead to some loss of employment (see paragraph 5.79). Although the company was not in a position to make any firm estimate, it suggested that the job losses involved might be not much in excess of 100. Scottish & Newcastle claimed that to some extent these losses might be offset by increased employment as a result of increased business following the merger; but we regard this as no more than a possibility and as too speculative to be given much weight. However, the company told us that it expected that it 'would be able to achieve most of these reductions in manpower without recourse to compulsory redundancy'.

7.30. The preservation of goodwill amongst the local population is a matter of considerable importance to a brewer and we have no doubt that if the merger takes place Scottish & Newcastle will in its own interests do its utmost to minimise job losses and to alleviate their consequences.

Conclusion

7.31. We discern no material advantages to the public interest arising from the proposed merger; but the question before us is whether the merger may be expected to operate against the public interest, and in our view there are not sufficient grounds for such an expectation.

7.32. We conclude that the merger situation which will be created if arrangements in contemplation by Scottish & Newcastle Breweries plc for the acquisition of Matthew Brown PLC are carried into effect may be expected not to operate against the public interest.

D G RICHARDS (*Chairman*)

S McDOWALL

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N E D BURTON (*Secretary*)

18 October 1985