THE DAVID HUME INSTITUTE

Papers prepared for the Inquiry into Corporate Takeovers in the United Kingdom

No 3

CORPORATE TAKEOVERS AND THE INTERESTS OF REGIONS AND LOCAL COMMUNITIES

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Hume Occasional Paper No.17

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INQUIRY INTO CORPORATE TAKEOVERS IN THE UNITED KINGDOM

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The David Hume Institute has been commissioned by The Joseph Rowntree Memorial Trust to conduct an Inquiry into the issues raised by Corporate Takeovers in the U.K. This paper is the third of a series presenting the results of research undertaken in the course of the Inquiry, and also submissions of opinion received from individuals and organisations which are thought to be of wide general interest. The Institute hopes in this way to keep the public informed of work in progress. The Final Report will appear in the late Spring of 1991.

The Institute has no collective views on any public policy question and is not committed to the views of any of its authors.

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ISBN 1 870482 17 4

Printed by Pace Print (Edinburgh) Ltd.

INTRODUCTION

Takeover bids are never far from the headlines. The latest predatory exploits of Lord Hanson, Sir Owen Green, Sir James Goldsmith, John Elliot and other colourful figures have provided much interesting copy in recent years. But for many the interest in takeovers goes beyond the key players and personalities involved. Takeovers and the operation of the market for corporate control can have significant consequences for the allocation of resources and the economic well-being of the nation which transcend the effects on the companies directly involved. There is therefore a legitimate justification for a public interest in what are essentially private transactions.

One area of increasing public interest concerns the number of well-known "regional" companies that were acquired during the "boom" years of the 1980s and the effects on the interests of their regions and local communities. The bids for Arthur Bell, Distillers, Matthew Brown, Rowntree, Pilkington and Scottish and Newcastle created much controversy and, with claim followed by counter-claim, frequently generated more heat than light.

In this paper we seek to consider the relation between corporate takeovers and the interests of regions and local communities, drawing on our research, and the work of others, in this field. Part one sets out the background and discusses the issues that we believe are relevant. In part two, we consider the problems to be overcome and the requirements for establishing the effects of external takeovers. Part three provides an overview of the relevant evidence and assesses the implications for regional performance and development. Finally, in the light of this evidence, the paper concludes with a critical assessment of competition policy in the UK and the authorities' treatment of the regional interest question.

1. BACKGROUND

Concern about the effects of external control on the performance of peripheral regional economies is not a recent phenomenon. In the 1950s and 1960s many commentators feared that a relatively successful regional policy was producing a branch-plant economy in the assisted areas of the UK. Branch plants, it was argued, would inevitably be more vulnerable to contraction and closure than their parent plants located in the south of England or beyond the shores of the UK. Yet during the 1970s and early 1980s, research demonstrated that these outcomes were by no means inevitable. The probability of future contraction and closure was found to be little different between parents and subsidiaries (Atkins, 1973; Clark, 1976), and overseas-owned manufacturing plants in Scotland were found to display a better overall employment record than indigenous openings and were less prone to job loss through closure but were subject to a higher rate of job contraction.

In view of these findings and the fact that the siting of new "greenfield" production facilities in peripheral regions provided much needed employment and income for depressed local economies, it might have been concluded that concern about the regional effects of external control was largely misplaced. However, such a conclusion would have ignored the significance of external control for the quality of regional growth and longer-run development.

Academic research on the determinants of regional growth had increasingly begun to move away from aggregate macroeconomic explanations of development towards analyses that focused on the microeconomic determinants. Evidence of increasing functional specialisation within firms and industry meant that regional development would depend not only on the type of industry located in the region but also on the functions performed. Even a fast growing industry such as electronics might not be so beneficial to long-run development if the activities located within the region amounted to little

more than assembly operations. Accordingly, when researchers examined the structure of externally controlled plants they were found to lack important control and operating functions such as investment planning, research and development, purchasing, sales and marketing (Hood and Young. 1976; McDermott, 1979).

In the late 1970s and early 1980s, the focus of interest in the subject of external control began to shift away from direct inward investments towards the effect of inward acquisition investments - external takeovers. This shift in interest constituted a response to the growing evidence of a relative growth in acquisition investment. For example, the ratio of the value of "greenfield" to acquisition investments undertaken by US multinationals in OECD countries fell from 3 in 1976 to 0.2 in 1979 (Hood & Young, 1982). Other researchers noted a similar trend at both national and regional levels (Mason, 1982; Smith, 1982). But perhaps of more importance was the emerging evidence that takeover activity within national economies was favouring companies controlled from core areas.

Figures 1 and 2, which are drawn from the recent work of Barbara Coppins, provide evidence for the UK and show the net change in regional control via takeover for the larger UK companies over the period 1968 to 1985 (Coppins, 1989). Figure 1 shows the cumulative net change in number of takeovers for each Standard region [1] over the period, while Figure 2 plots the annual net transfer of control to the South East from the rest of Britain. Clearly while these data show that there is no simple north-south divide in takeover activity, the balance of takeovers has, nevertheless, been consistently in favour of companies headquartered in the South East of England, with the corporate control of many leading "regional" companies shifting either abroad or to London and the South East [2]. Indeed, the imbalance may be greater than depicted since we note below that there is evidence that headquarters have been progressivly concentrating in the South East to take advantage of perceived localisation and agglomeration economies. A

Figure 1

Cumulative Transfers of Net Control

UK Regions: 1968 to 1985

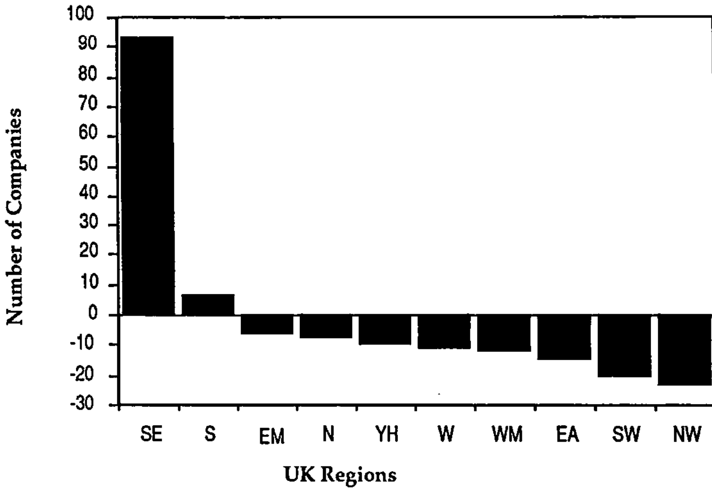
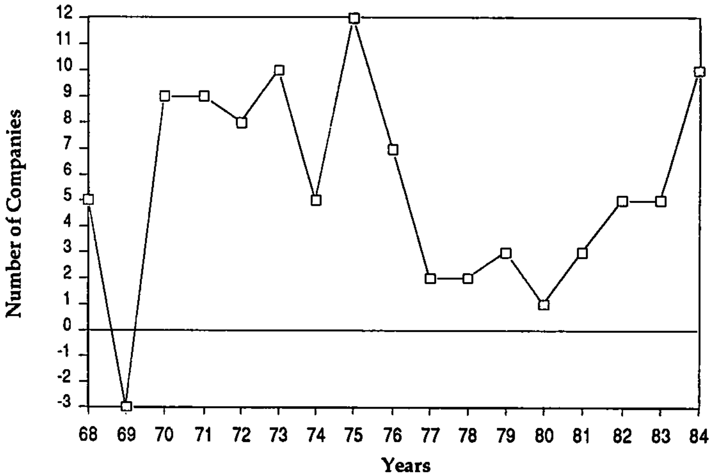


Figure 2

Annual Transfer of Net Control

to South East from EOK: 1968 to 1985



takeover of a South East firm by a company headquartered elsewhere in the UK might be used to effect a transfer of the acquirer's headquarters or key functions to London and the South. Moreover, there are mechanisms other than takeover which can result in company headquarters functions moving South, including unilateral relocations by regional companies and management buyouts.

This increase in the extra-regional control of non-core area companies through corporate takeovers raises several questions about the implications of the process for the interests of peripheral regions and their local communities.

The fundamental concern is that the external takeover of regional companies may lead to decisions being taken in the interest of the the merged company as a whole but which could be to the detriment of the acquired company and the wider regional economy. Hypotheses about the potential impact of corporate takeovers on the interests of regions and local communities can therefore be considered in terms of internal and external company effects, and these are examined in greater detail in the next section.

NOTES

1. Northern Ireland is excluded because for every year except 1975/76 no Northern Irish firm was involved in takeover activity, and in 1975/76 there was one acquirer and one acquiree.

2. These data which are drawn from the Times 1000 lists of the largest UK takeovers occurring each year are clearly partial and may not reflect the spatial distribution of all takeover activity. However, subsequent and as yet unpublished research by Coppins suggests that the net shifts in control are broadly similar when a wider database is used.

2. TAKEOVERS AND THE REGIONAL INTEREST

2.1 Internal Company Effects

The traditional economics literature on mergers and acquisitions is not concerned with the spatial element in the takeover process. Moreover, the analytical framework provided by this work does not provide an appropriate approach to the analysis of regional acquisitions. The focus of this body of literature on market power, economies of scale, and product and process innovations, is inappropriate, or at least insufficient, to analyse the regional effects of takeovers. The external takeover of regional companies draws attention to the effects on the acquired companies and their regional economic environment, whereas the traditional economics literature on mergers is concerned with the acquired and acquiring companies taken together. The introduction of a regional policy dimension complicates the picture substantially and the range of possible relevant effects increases markedly.

Changes in the structure of production between acquired and acquiring companies are unimportant in the merger literature because they occur within the same unit of account eg. mergers and acquisitions within the UK. What is important in the merger literature is whether such rationalisations and reallocations of resources have net effects on the appropriate indicators of economic performance. No resources are lost to the unit of account and so the crucial question concerns whether mergers and acquisitions promote a more efficient use of resources. However, if a merger results in the more efficient use of resources in the combined company, for the acquired regional company this might be associated with a run-down in the scale of operations, a lower rate of growth, and a reduction in the sophistication of the company's operations. The latter effect may be associated with the removal of key control functions, key operational functions, with the consequent migration of qualified management and staff, and the removal and simplification of products and product lines.

Conversely, the acquired firm could enjoy an increase in the number, size and sophistication of its functions and/or gain access to markets, new products and processes, managerial expertise and finance as a result.

Table 1 summarises the favourable, unfavourable and often contradictory hypothesised outcomes for the acquired firm's scale, structure and conditions of production which researchers have suggested may be the result of external acquisition. The table makes clear that, unlike the merger literature, the professional interests of researchers concerned with the regional impact of corporate takeovers have been the nature and structure of the acquired firm's production rather than performance effects per se. We have seen that there are good reasons for this. Even if the performance of the acquired firm improves as a result of takeover, the improved performance may be associated with a reduction in the scale and sophistication of its operations which may in turn lead to important long-run effects on the development of the wider regional economy, a subject to which we now turn.

Table 1. Hypothesised Internal Company Effects of External Takeover *Source: Ashcroft, Love and Scouller (1987)*

Favourable	Unfavourable
Organisation and autonomy: New management techniques and practices.	Reduced control and operating functions.
Finance: Increased availability of finance for investment.	Income transfer to parent.
People: Improved quality of workforce.	Reduced labour skills. Worsened labour relations.
Plants: Access to new technology.	Greater probability of closure. Technological asset stripping. Reduced research and development.
Products and Markets: New products and increased product development.	Rationalisation of product lines.

2.2 Wider Regional Effects

The wider regional, or external, effects of corporate takeovers of regional companies embrace all the impacts on the region other than those directly affecting the acquired firm. These effects may occur in three ways. First, through changes in the organisation of the acquired firm and its demand for regional inputs; second, via direct competitive effects on other local economic activities, and third, through what may be termed intangible effects which are not the direct result of changes in market relations.

Acquisition may have an effect on the demand for regional inputs in two ways. An expansion or contraction in the scale of the acquired firm's production activities and functions performed will have a wider or multiplied impact on regional income and employment as the firm varies its demand for local inputs and as the change in the income paid to the firm's employees affects their local spending plans. In addition, the takeover may lead to changes in the composition of the firm's demands for inputs independently of the change in the scale of the company's activities.

Competitive effects occur when the performance of other regional companies in competition in either product or factor markets suffers or improves following the takeover. Other firms may suffer through the normal process of competition if the acquired company's performance improves enabling it to charge lower prices, offer an improved product specification and pay higher wages. In this situation local consumers will benefit and so such gains need to be set against the losses experienced by local firms. However, in the short run at least, local economic welfare is likely to fall if the benefits of increased competition are largely obtained by non-local consumers when the bulk of sales are outwith the region and displaced resources are not re-employed either in an expanded acquired company or elsewhere in the local economy. Ideally, in the medium term, local firms should respond to increased competition from

the acquired firm by raising their own efficiency and performance to the benefit of the regional economy. Alternatively, the acquired firm's link to the acquirer may be damaging to other regional companies through anti-competitive actions such as cross-subsidisation, tie-in sales and reciprocal buying. Such restrictions will be of little or no long-term benefit to the regional economy and are more than likely to be damaging.

Intangible effects are so called because they are not the direct result of changes in market relations between the acquired company and other regional firms. One typical befefit often cited relates to the transfer of superior technical and managerial skills from the acquirer, through the acquired company to other firms in the region. The transfer of information may occur through face-to-face contacts with the management and staff of the acquired company at local conferences, Chamber of Commerce meetings, educational institutions, trade associations, technical councils, local enterprise networks (LENs), and more recently, training and enterprise companies (TECs or LECs). A less direct transfer might be effected through the external labour market as staff eventually move from the acquired company to other local firms.

In contrast, it is frequently alleged that the status of key figures in the local business community might decline following acquisition due to an expected reduction in their independence of action and thought. Leadership in the whole range of public and community affairs might be weakened, with damaging consequences for local development. Moreover, it is often argued that managers who become responsible to an ultimate authority outside the region may be less likely to consider the implications of their actions for the local economy than might otherwise have been the case. But a failure to consider the impact of company decisions on the local economy is not necessarily harmful. Where regional companies fail to act by postponing harsh decisions because of their impact on the local economy, then any short-run befefit might be at the expense

of harmful longer-run effects. The company might eventually close or contract substantially because of the earlier failure to adjust. Beneficial economic change might be prevented and the regional economy could suffer precisely because managers allowed such non-economic considerations to influence their actions.

The external effects of corporate takeovers will have greater significance for the future performance of the regional economy if they affect the availability and quality of the local economy's resources. Takeovers which lead to a changed requirement for certain functions to be performed within the acquired company and/or produce a change in the demand for local material inputs and services may precipitate significant supply-side responses within the regional economy. The most frequently hypothesised outcomes are changes in the net emigration of skilled personnel and changes in the skill level of existing staff.

Net emigration would be expected to increase with a reduction in the demand for management personnel and other labour following takeover and decrease when the demand for local inputs and functions is raised. However, the impact on migration is not automatic; it depends on conditions in the local labour market and a complex series of adjustments may be necessary before any effect on migration materialises (Ashcroft, 1988). Changes in skill levels may also occur. A reduction in functions could require staff remaining in place to work at a lower skill level, with the result that previously acquired skills atrophy and disappear. Conversely, an increase in the range and sophistication of functions performed might require an improvement in the skills provided by existing staff through the introduction of in-service training schemes and other methods of work improvement.

A change in the availability and quality of managerial and labour skills following takeover could affect the performance of the regional economy in several ways. The rate of new firm

formation could change since there is evidence of a positive correlation between the location of managerial skills, the degree of education of the labour force and the birth rate of companies (Gudgin, 1978). The rate of innovation, new product development, application of new technologies and investment, and adaptation to change, might also be affected. Indeed the competitive position of the regional economy might permanently change if the effects were sufficiently large.

In theory the wider regional effects of are, like the internal effects, quite complex and very difficult to forecast for particular takeovers. The preceding discussion has implied that the expected effects on the regional economy could just as easily be favourable as unfavourable. While this is probably a correct judgement for the effects on acquired company performance it is less so for those changes in the structure and conditions of production which it was argued could produce significant effects on the wider regional economy. Research on the process of industrial restructuring in the UK suggests that it may be producing a net transfer of headquarters and key corporate functions away from peripheral regions to the centre, particularly London and the South East (Goddard & Smith, 1978: Crum & Gudgin. 1976). In view of the evidence noted above on the sustained dominance of London and the South East as the principal source of acquirers, it is evident that corporate takeovers are the key mechanism effecting this transfer. This process must inevitably diminish and dilute the resource base of the regions which, it is hypothesised, will have longer-run dynamic effects on the performance of their economies, lowering competitiveness and the rate of growth.

Popular concern about the likely effects on regional economies of proposed takeovers of regional companies appears, therefore, not to be groundless. Nevertheless, it is clear from the preceding discussion that the expected outcomes for regional economies are by no means clear cut. To gain further insights we need to examine the available evidence. But before we do that we need to consider the methods and procedures that are

required to determine the significance and effects of corporate takeovers on the interests of regions and local communities.

3. ESTABLISHING THE IMPACT OF TAKEOVERS

3.1 Definitions

To establish the impact of external takeovers on regional economies we need to define carefully the terms on which the assessment is to be conducted. Here we follow the terminology and definitions adopted by Ashcroft, Love and Scouller (1987).

First, an external takeover can be deemed to have occurred when a regional company becomes the subsidiary of a company from outside the region. A subsidiary is taken to be a company in which a parent company holds more than 50%. of the nominal value of the equity of the firm in question. Usually a 50%. holding or more is necessary for the parent to control the composition of the board of directors, but it need not be so. The crucial definitional problem, though, concerns the criteria to be used in the differentiation of a regional company from those outside.

The definition of a regional company is clearly fundamental. Received popular opinion and the theoretical perspectives discussed above embrace the view that an external takeover of a regional company will produce a different outcome from that occurring in the absence of the acquisition. Even takeover by another regional firm would be expected to produce a different set of results. Any attempt to test these views must use a data-set where the regional companies are clearly distinguished from other firms, otherwise the subsequent evidence will have little meaning.

At first sight this might not appear to be a problem since location in the region would appear to be the obvious defining characteristic. Unfortunately not all companies are so conveniently located. A company might have one or more plants located in the region but have several others sited

outside. Another firm could have all its production activities sited in the region but its headquarters might be located elsewhere. Others may have a registered office in the region but have little or no production, managerial and administrative activities there. One further difficulty is that a company may appear to have the full range of functions and activities in the region yet it may be the subsidiary of a distant British or foreign firm with ultimate control exercised from another part of the UK or from abroad. It is clear that many other combinations of partial company location in the region could be envisaged. However, since the issues raised by external takeover concern the effects of the removal of local control of regional firms then in this context a company should only be classified as being from the region if ultimate control resides there. It follows that the only suitable operational indicator of the source of ultimate control is the location of a company's headquarters. Firms with activities sited in the region but with headquarters located elsewhere should not be counted as regional companies. Takeovers of these companies, or acquisitions solely of those parts of their activities located in the region, are not external takeovers. They cannot be treated as such because they represent only a change in the location of an existing degree of external control rather than a change in the level or extent of external control per se.

3.2 Methods

An understanding of the effects of takeover cannot be obtained by simply examining the structure and performance of the acquired company in the years after the acquisition. What is required is a forecast of what would have happened in the absence of takeover: the counterfactual position. Once this has been obtained, the effect of acquisition is deducible from a comparison of actual with "expected" performance.

The critical problem is the construction of the counterfactual. The simplest and least satisfactory solution is to take the average performance of the acquired company during a suitable

period before takeover - usually five years - and make the heroic assumption that performance would have continued unchanged if the takeover had not occurred. Clearly, this is unsatisfactory since the performance of the firm would be likely to change for reasons other than, or in addition to, takeover. What is required is a means of controlling for other influences. This may be achieved by direct modelling and statistical estimation of the impact of these influences, or by the selection of an appropriate comparator. The implicit hypothesis underlying the choice of any comparator is that it will exhibit a similar performance to that which would have been produced by the acquired firm if takeover had not in fact occurred.

Much of the evidence presented below is drawn from the study by Ashcroft, Love & Scouller (1987) - described there as ALS - who used both statistical analysis of published data and case study interviews to establish effects.

In the former case, the counterfactual was constructed using either the UK industry as the comparator - Minimum List Headings level on the Standard Industrial Classification of 1968 - or a comparator adjusted for a statistically significant trend in the performance of the firm in relation to its industrial comparator during the period before acquisition. An allowance for a time trend in the firm-industry relation was felt to be necessary because the industry of which the firm is part would be unlikely to be in equilibrium. It is reasonable to expect that between the pre- and post-acquisition periods some firms would improve their position relative to the industry average while the position of other firms would deteriorate. Allowing for a time trend in the firm-industry relation goes some way to accommodate this fact.

It is difficult to determine from statistical analysis of performance indicators alone whether a takeover has been beneficial or harmful to the acquired firm. There are a number of important issues which cannot be settled by the statistical analysis of published company results. These include the

motivation for the merger and the attitude to it of the acquired company, how finance flowed between the regional firm and its acquirer, the effects of takeover on labour relations and the structure of the firm, including the degree of local autonomy remaining, opportunities for management, whether any benefits were derived from new management techniques, the effects on important management functions such as marketing and R&D, and the effects on local supply linkages. Information on these effects can only be obtained by case studies involving interviews with, or postal questionnaires to, the firms involved.

The use of interviews or questionnaire surveys does of course have weaknesses. First, there are difficulties with the accuracy and precision of recall of respondents. Second, the method relies exclusively on the judgements of those interviewed and these are necessarily subjective. Finally, there is the difficulty of distinguishing between what happened after the merger from what happened because of it. This aspect of the counterfactual question is fundamental to the study of the impact of acquisitions, but it is not one that managers readily make. Interviewers must keep the distinction constantly in mind, particularly for those questions which are raised in the literature but cannot be tested statistically from published data, such as the effects of acquisition on labour relations or labour quality and most of the structural effects.

Whilst it is important to recognise these limitations of case studies based on interviews, they should not be overstressed. A purely statistical approach involves equally serious difficulties, both conceptual and theoretical, and in terms of obtaining acceptable data. Interviews can examine many of the factors which underlie the statistical trends that cannot themselves readily be analysed in statistical terms. In studying the effects of takeovers a combination of statistical and interview methods is in our view the most satisfactory approach.

4. OVERVIEW OF THE KEY EFFECTS OF CORPORATE TAKEOVERS

We now turn to a consideration of the evidence on the effects of takeover on acquired companies and the implications which this has for regional performance and development. In common with the earlier analysis, internal company effects and external effects on the wider regional economy are considered separately; however, there are clearly links between these two types of effect and some consideration is also given to possible interaction between them. Only a summary of the key effects is given here; for a detailed review and critique of the literature on external takeovers and regional development see Love (1989). Unless otherwise indicated, the evidence cited here is derived from the work of Ashcroft, Love and Scouller (1987) on the implications of the external takeover of Scottish companies.

4.1 Internal Company Effects

This section considers the effects of external takeover on acquired companies in two main areas, company structure (organisation and autonomy, including managerial opportunities and functions, finance etc.), and company performance (plants and employment, profits, sales).

Company Structure

When a previously independent company is externally acquired, by definition de jure control is lost to the indigenous economy. However, the extent of de facto control exercised may vary widely, from a loose 'hands off' approach to virtually complete integration with the parent company.

Nevertheless, the degree of autonomy exercised by local management is inevitably reduced to some extent [1], and the key issues are, first, by how much is autonomy reduced and, second, is the reduction of any consequence?

One of the problems here is defining what we mean by 'autonomy'. Clearly it is concerned with the extent to which local managers are able to run the company without reference to higher authority, and there are several measures of this. In a study of external acquisitions in the UK during 1973 and 1974, Leigh and North (1978) divided their studied firms into three categories according to the degree of local autonomy which remained after takeover:

1. Those retaining a high degree of managerial responsibility (control over product lines, production methods and some capital investment).
2. Those retaining a moderate degree of managerial control (largely as above, but brought into line with their parent organisation's conventions).
3. Those retaining a low degree of managerial control (essentially reduced to branch plant status with only routine management responsibilities).

Interestingly, in Leigh and North's research each category contained a roughly equal proportion of the companies studied, indicating that external acquisition is not necessarily always associated with a major loss of autonomy.

If we examine Leigh and North's categories more closely there appear to be three criteria which seem particularly useful in determining the extent of autonomy which remains after external takeover. First, the nature of the formal relationship between the subsidiary and its new parent; second, the nature of financial control exercised; and third, the extent to which top management functions are reduced in the acquired firm.

The first area of interest is the formal structure of the acquired company within its new parent and the extent to which new senior appointments are made after acquisition. In the ALS work, there was a distinct tendency for externally-acquired companies to remain either as distinct operating subsidiaries or become a major part of an existing or newly-formed division

of the acquirer. Complete integration with the parent company was extremely rare, although in some cases there was a tendency for a closer degree of operational integration to develop over time. The appointment of new board members took place in two-thirds of the companies studied in this research, indicating that at least some degree of control was being exercised by the parent company; however, in less than one-third of cases were new appointments made at the most senior level (managing director or chairman), indicating that wholesale changes of top management were the exception rather than the rule.

Another important aspect of autonomy lies in the nature of financial control exercised after takeover. In many respects this is of the essence in terms of the effects of takeover both on the firm and on the local community, since whoever controls the finances of a company has a very large say in its operations and development; very strict financial controls substantially reduce the acquired firm's operational discretion, no matter what the formal organisational relationship might be. Virtually all companies in the ALS study indicated that there was some degree of financial control exercised over them after takeover, with more than half indicating that this control was fairly or very strict. By far the most common type of control was by annual budget within the context of a medium term financial plan, often linked to clear expenditure and/or investment limits. There were exceptions, however, with one-third of the studied companies also being asked to provide monthly reports at various levels of detail. While the managers of some acquired companies found this reporting to be time-consuming and irksome, most admitted that the extra financial discipline which it imposed was a major benefit of acquisition in the long run. In addition, it was clear that the degree of financial control which was imposed was not done in an arbitrary fashion; although there were a few exceptions, generally there was a clear relationship between the financial position of the acquired company and the nature of control, with the poorest-

performing companies at the time of takeover being subject to to the tightest control. Crucially, the vast majority of acquired companies reported that it was easier and/or cheaper to obtain investment finance after takeover, either because there was access to the funds of a larger group or because banks were more prepared to lend money when the firms had the backing of a large group.

This study also attempted to determine the extent to which the number of senior management posts and associated promotional opportunities changed as a result of acquisition. In both cases there were examples of increases and decreases among acquired companies, but the net effect in both cases was substantially negative; that is, more acquired firms lost than gained senior managers as a result of acquisition, and more felt that promotion prospects had been reduced than felt they had been enhanced. It should be pointed out, however, that in both cases a substantial proportion of the acquired companies felt that no change had occurred because of takeover (68% in the case of senior posts and 44% in the case of promotion opportunities).

The clear implication of the research outlined above is that external takeover does result in a reduction in autonomy at the local level; de facto as well as de jure control tends to drift towards the acquiring company. Whether this is of any consequence for the acquired company depends on the possible effects of reduced autonomy. Several detrimental consequences are possible. First, local management can no longer operate solely on the basis of the interests of the local business as they see it, because the interests of the parent company have to be considered. Needless to say these interests may not coincide. Second, the need for detailed reporting and strictures on investment limits may slow down the ability of local management to make quick commercial decisions. This may help prevent them from making mistakes, but it may also prevent them from capitalising on opportunities which require fast decisions to be made. Finally, as a result of the reduced

status of local management and reduced promotion opportunities it may become more difficult to to attract and hold managers of high quality.

However, there can be benefits as well as costs to a loss of autonomy for the acquired firm. Improvements in both the availability and control of finance were outlined earlier, and there is also the issue of replacing management where an independent firm is poorly managed and is performing badly. In Britain shareholders, even institutional shareholders, rarely act to replace the directors of poorly-performing companies, preferring instead to sell their shareholding in companies whose performance disappoints [2]. This puts a lot of importance on the takeover mechanism as a method of replacing less able managers with more able substitutes, and in some cases a loss of autonomy may be a necessary condition for improving company performance and ensuring long-run survival. The proper working of this process may have been of some importance in the Scottish study discussed above, in which well over half the companies studied were considered to have had a pre-acquisition performance which ranged from mediocre to very poor. There may, however, be a wider price to pay for this potential benefit of the takeover process, and this price is discussed later in the section on the external effects of acquisition on the regional economy.

Company Performance

a) Plants and employment

Where inward investment into a region results in the establishment of a new plant or office an immediate direct positive effect on local employment can generally be expected, although there is no guarantee of this in the long term. However, where an enterprise moves into external control via acquisition even this immediate benefit to employment cannot be assumed, and in the long run the situation is very uncertain.

Much of the early British work on the regional implications of

takeovers indicated that the direct employment effects of takeover were not encouraging, especially in the medium to long term. The work of Healey (1982), for example, suggested that in general acquired manufacturing plants showed a significantly greater incidence of closure than non-acquired plants five to six years after takeover. However, this work did not distinguish between external takeovers and those originating from within the regional economy, and was concerned exclusively with a declining industrial sector (textiles) in which acquisition might be expected to contribute to necessary corporate restructuring, possibly including a relatively high degree of plant closure. Rather more worrying was the analysis of Smith (1979, 1982) on the employment effects of external takeovers in the Northern region between 1963 and 1973. Smith concluded that plants which were externally acquired between these years showed a markedly higher incidence of job losses through closures during the period than did indigenously-owned plants or plants which had been controlled from outside the region since before 1945. Smith further speculated that the reasons for the relatively high closure rate may be explained at least in part by 'technological asset stripping', where the acquired company finds its plants closed down because its production capacity is peripheral to the needs of the acquirer, while its technical expertise is removed to some external location.

Most of the work on the employment implications of external takeover, including that of Healey and of Smith, suffer from a failure to address the issue of the counterfactual raised in section 3; that is, what would have happened in the absence of acquisition. The ALS study explicitly tested this point by comparing employment performance after acquisition relative to an appropriate industry comparator with pre-acquisition performance relative to the same comparator for five years before and after takeover. Overall, no significant effect of acquisition was found, although there was a tendency for public companies to fare significantly worse than private companies following takeover. Given that peripheral regional economies

tend to have relatively few public companies and that these tend to be among the largest employers, this may be a finding of some significance. Overall, evidence to date appears to indicate that external acquisition is unlikely to be beneficial to the employment of the acquired companies in the short to medium term, although there is equally little systematic evidence of detriment.

b) Profitability and sales

In the industrial organisation literature on mergers there is a long tradition of using profitability indicators as measures of the 'success' or otherwise of mergers [3]. Despite the fact that changes in profitability and sales are obvious (but incomplete) measures of a company's post-acquisition performance, virtually no attempt has been made to analyse systematically the impact of external takeover on these variables. One exception to this is the ALS study, which used the industry comparator approach described above with regard to employment to determine the effect of external acquisition on Scottish manufacturing companies. In addition to an analysis of the acquired companies' performance on sales, two measures of profitability were used; return on capital employed (ROCE) and return on sales (ROS).

Comparing the performance of the companies five years before takeover with five years after, it was found that both ROCE and ROS showed a statistically significant deterioration, while sales performance showed a significant improvement. However, due allowance has to be made for the fact that the performance of any acquired firm could have been improving or deteriorating relative to its industry in the pre-acquisition period, which would affect the result of the statistical analysis. When this allowance was made there was no discernible effect on ROCE in the post-acquisition performance, although the negative effect on ROS persisted. The positive effect on sales also disappeared when this allowance was made, except when comparing the first two years after acquisition with the five

year period before, where the significant sales improvement was still found.

Some tentative conclusions could be drawn from this analysis. Despite the fall in profitability, these results are consistent with the view that acquisition increases efficiency and competitiveness. It was noted earlier that improved access to investment finance was one major benefit of takeover for many companies, and an increase in capital-intensity and improved efficiency could be consistent with reduced ROCE [4] and improved sales. The systematic increase in sales would also be consistent with improved market opportunities as a result of acquisition, and the accompanying decrease in ROS could indicate a move towards a more high sales volume, low margin strategy following acquisition.

4.2 Effects on the Regional Economy

This section considers the evidence on the effects of corporate takeovers on the wider regional economy of which the acquired company is part. By their nature these external effects are more difficult to establish and quantify than those which relate directly to the acquired companies. For example, changes in the level of inputs purchased from local suppliers or an alteration in the requirement for top management functions resulting from an individual takeover may have relatively little effect on the wider economy; but if effects such as these show a systematic pattern through time their cumulative effect may be substantial, although it may not be obvious that their ultimate source is the process of acquisition. Some attempt must therefore be made to arrive at a conclusion on these external effects.

It might be thought that the best way to proceed would be to examine the behaviour of key economic aggregates of the regional economy which it is thought could be affected by external takeover (for example, GDP growth, the rate of new firm formation, the closure rates of suppliers and competitors etc.), and attempt to relate changes in these aggregates to the

incidence of corporate takeovers. In practice this is extraordinarily difficult to achieve. There is first the problem of establishing a suitable counterfactual at the aggregate level which would require a model of the behaviour of the chosen variables, and even if this problem could be overcome some of the external effects might not be sufficiently great to show up in an aggregate analysis, or might appear with a considerable time lag.

Because of difficulties such as these the ALS research, and other work in the area, has concentrated on seeking to establish whether the conditions necessary to produce wider regional effects are actually present in the acquired companies themselves following takeover. While this makes quantification of these external effects difficult, it does allow some idea of the direction of these effects and in some cases their scale. The effects considered below are grouped into three areas: changes in linkages with other regional companies; changes in headquarters and operating functions; and other effects, including competitive effects on other firms and the morale and prestige of the local business community.

Material and Service Linkages

When a firm is acquired by a company from outside its local area the possibility always exists that the purchasing of both material inputs and services will be rationalised, with local suppliers being replaced by those of the acquirer or by in-house provision. This in turn could have repercussions throughout the regional economy if this business cannot be replaced. Of course, the effect could go the other way, with local suppliers gaining more of the acquired company's business following takeover; however, the evidence indicates that this is fairly rare.

In the ALS study the majority of acquired firms in the sample (68%) found that there was no effect of acquisition on material inputs purchased from local suppliers. But the group which did find such an effect was seven times more likely to decrease

than to increase purchases from local suppliers. For services the findings were even more clear-cut; 72% of the sample firms had decreased their use of services from within the regional economy, and none had increased their use of these services. As a rule it was professional services which were most notably affected, with over half the acquired companies ceasing to use Scottish auditors, and 40% ceasing to use a Scottish bank as their principal bankers. Other service inputs such as stockbrokers, advertising agencies and solicitors (despite the differences of Scots and English law) were adversely affected to a lesser extent. In addition, the ALS study concluded that while reduced service linkages were a general phenomenon associated with external takeover, reductions in purchases of materials from local suppliers tended to be strongly associated with those firms whose immediate pre-acquisition commercial performance was poor.

This general pattern is consistent with other research in the UK such as Leigh and North (1978), who found evidence in inter-regional takeovers of a limited reduction in material inputs from local suppliers, but a very marked tendency for local service linkages to be reduced or severed. Very similar linkage effects were found by Love (1990) in an analysis of external takeovers in the Scotch whisky industry which was supplemented by data from the regional suppliers of acquired companies. This study further concluded that even where an acquired company's sales rise as a result of takeover, certain sectors of the regional economy may suffer a measurable reduction in output and employment because of a systematic tendency to switch to external suppliers.

The findings on linkages, especially service linkages, are of some concern. Several of the peripheral regions of the UK, notably Scotland and Wales, have been actively seeking to promote their expertise and acumen in the financial services industry, which during the 1980s was one of the fastest-growing sectors of the British economy. Yet there is evidence that the process of corporate acquisition may systematically erode the

indigenous use of these very skills, making their continued growth and development more uncertain than would otherwise be the case.

Headquarters and Operating Functions

Changes in top management functions and promotion prospects were considered earlier as internal effects of takeover on the acquired companies themselves. However, these changes may have long-term consequences for the regional economy. For example, Firn (1975) has highlighted the difference between 'innovative, entrepreneurial-type decision making' and 'routine, management-type supervision'; if the former is adversely affected by external takeover or by any other means the regional economy may suffer, because " much of the drive, enthusiasm and invention which lies at the heart of economic growth is removed, reduced, or at best, suppressed." (Firn, 1975 p 410). The process by which this might occur revolves around a lack of key management functions resulting in reduced opportunities for the professional and managerial labour force of the region, which may, as outlined in section 2, lead to emigration of entrepreneurial talent and hence a lower rate of new firm formation and regional growth.

In addition to top management functions there may also be some operating functions exercised by the individual enterprise which are not only fundamental to its existence as an autonomous unit, but which by their presence help either to improve the productive capacity of the regional economy or form an important element in its economic independence. Research and development (R&D) and marketing appear to fall into this category, the former because it helps maintain the competitive edge of the regional economy, and the latter because it provides firms with the direct exposure to the market which is essential for economic sovereignty.

The ALS study found evidence of detrimental effects on these key operational functions following takeover. For both R&D

and marketing, externally-acquired firms were more than twice as likely to to have these functions reduced than increased following takeover, although a substantial minority (48% for R&D and 44% for marketing) showed no change after takeover. For other management functions, such as personnel and purchasing, the results were even more marked, with half the sample companies undergoing reductions and none achieving increases following acquisition. Once again, there is evidence from this research that the pattern of function loss is not random, with poorly-performing acquired companies showing a markedly greater tendency to lose operating functions. There was also some tendency for function loss to be particularly associated with horizontal takeovers, which is unsurprising because it is generally assumed that there is more scope for function rationalisation where both companies operate in the same product market.

Other Effects

External takeover may also affect the regional economy in more subtle ways. If an acquired company improves its competitive position following takeover this may appear to be a clear benefit to the regional economy. However, this depends on whether this improvement is at the expense of other firms from the same region operating in the same market; conceivably the improved competitiveness of one acquired company could have such a devastating effect on its local competitors that the net effect in the regional economy could be detrimental, at least in the short run. The reverse argument applies in the case of worsened competitiveness for an individual company following takeover. There is no clear evidence from the studies of external takeover of the extent or nature of these effects, and no conclusions can therefore currently be drawn.

There are also more intangible effects which could, in the long run, have important consequences for the regional economy. These could include the effect of takeovers on the transfer of technical and managerial skills, and any effects on the morale,

image and prestige of local business people and their contribution to the economy as a whole. In the ALS study 44% of the acquired companies studied benefited from improved management techniques introduced by their acquirer, with financial control and management most frequently mentioned. This represents a benefit for the acquired companies themselves, and implies that the potential exists for these improved techniques to be passed on to other regional companies in the long run, perhaps through the management of acquired companies subsequently moving to other employment within the regional economy. However, there is little clear evidence that such transfers have actually taken place, nor is it clear how such transfers and their effect could be quantified.

Even more uncertain is the effect of takeover on community leadership and the morale of the business community. Several companies in the ALS study indicated a loss of local identity following takeover, with the concomitant possibility of less consideration being given to the local community when post-acquisition management decisions were being made. However, it proved impossible to come to any conclusion on the prevalence or scale of this effect, except to suggest that it seems unlikely to be beneficial to the long-run development of the regional economy [5].

4.3 Conclusions

The research reviewed above indicates that externally-acquired companies do suffer real reductions in autonomy, although the extent to which this takes place is clearly linked to the performance of the acquired companies before takeover and cannot therefore be regarded as necessarily detrimental even where it takes place to a marked degree. Offsetting this is the finding of improved management techniques, financial control and access to investment finance which frequently follows takeover. In terms of performance, although there is a systematic tendency for profit reductions to follow takeover,

this may not be a symptom of decreased efficiency, and there is evidence that improved sales and access to new markets does tend to follow external acquisition. There is mixed evidence on the direct employment implications of external takeover, with the ALS study finding no systematic effect while earlier studies have suggested an increased likelihood of employment loss through plant closure following takeover. However, unlike ALS, these studies make little attempt to establish an explicit counterfactual position.

The overall conclusions of this work suggest that, for the acquired companies themselves, acquisition is relatively frequently beneficial and relatively rarely completely harmful. This was certainly the finding in the ALS research for the companies subject to detailed case-study analysis; 56% of these acquisitions were judged to have been beneficial to the acquired companies with only 20% clearly detrimental. The remaining 24% were broadly neutral in their effect. The general lessons of this research are that, as a rule, external takeover tends to be harmful where the acquirer is motivated by its own tactical interests rather than those of the acquired firm. By contrast, external takeover tends to have beneficial consequences for the acquired companies where there is something apparent which the acquirer can do for its new subsidiary (e.g. supply funds, technical help, marketing expertise etc.) and if the acquiring company is large, financially-secure, well-managed, and has some experience of managing subsidiaries.

When we turn to the external effects of takeover on the wider regional economy the findings are much less encouraging. There is very clear evidence of a systematic tendency for external takeover to result in reduced linkages with local suppliers; this effect is particularly pervasive in the professional services, which may have severe long-run consequences for the regional economies which are affected in this way. There is also clear evidence of a reduction in both top management and key operational functions. In conjunction with the lessened use of local professional services by acquired companies, this

effect could have detrimental consequences for the regional economy as a result of reduced opportunities for highly-skilled personnel, which could in turn lead to increased emigration and a lack of dynamism and entrepreneurship.

NOTES

1. Where the externally-acquired company is the subsidiary of an indigenously-owned company the range of possibilities on autonomy increases. While reduced autonomy may be considered the most likely outcome, it is conceivable that the new parent could allow local management to exercise more control over the company's operations by adopting a more 'hands off' approach than was previously the case. Under certain circumstances, therefore, external takeover could result in increased autonomy.

2. This is the exercise of 'exit' rather than 'voice'. See Charkham (1989) for a useful discussion of the drawbacks of this approach to managerial discipline.

3. See Hughes (1989) for an excellent summary of this literature, and of other approaches to merger evaluation.

4. The denominator of ROCE is overall capital employed, and so an increase in assets will result in a fall in ROCE, other things remaining equal.

5. This effect was expressly considered by the Monopolies and Mergers Commission as a possible detriment to the national interest in its investigation of the proposed takeover of the Royal Bank of Scotland by the Hongkong and Shanghai Banking Corporation and Standard Chartered Bank (HMSO, 1982a).

5. POLICY IMPLICATIONS

5.1 Legislation and Current Practice

The rationale for merger policy in the UK rests on the belief that some mergers may have detrimental consequences for "the public interest", and so should be prevented or modified. This notion of the public interest is made explicit in section 84 (1) of the 1973 Fair Trading Act, and refers in the main to the desirability of maintaining and encouraging competition. Crucially, however, another element of the public interest is:

> "maintaining and promoting the balanced distribution of industry and employment in the United Kingdom."

The **regional** interest is therefore recognised as forming part of the **public** interest. However, the public interest is not applied consistently at all parts of a merger investigation, as can be seen by a brief discussion of the criteria for referral of a proposed merger to the Monopolies and Mergers Commission (MMC) compared with the criteria adopted by the MMC during its investigation.

a) Referral

In deciding whether or not to recommend a qualifying merger [1] for investigation by the MMC, the Director General of Fair Trading (DGFT) is not obliged to take account of the public interest criteria outlined above, nor are the reasons for his recommendation made public. The statutory public interest criteria apply only to actual investigations carried out by the MMC.

In a booklet designed to help intending merger parties understand the way in which the procedure works [2] the OFT indicates that regional considerations may be considered by the DGFT if thought relevant in a particular case. But it is made clear that it is employment which is the aspect of regional outcomes which will be considered in particular cases.

Moreover, the regional issue is clearly held to be secondary to those of competition and efficiency.

b) The MMC Investigation

Once a bid has been referred the MMC must consider all aspects of the public interest as defined by the Act, and the weight to be given to the evidence. Moreover, the bidder is not required to show that the proposed takeover is in the public interest. Instead the burden of proof is on the MMC which must demonstrate that there is an expectation - not just a possibility - that the bid is against the public interest for the bid not to be allowed to proceed. So, in examining each referral, the MMC is required first to identify any expected detriments to that interest and then, if any are found, to consider whether there is an expectation of benefits which would be likely to compensate for the detriments.

An indication of the practice of the MMC with respect to the regional issue was provided at a conference in 1989 [3] by Mr Ian Lang, Minister for Industry and Education at the Scottish Office who suggested that:

> "while it would be rare that a bid would be blocked on these (regional interest) grounds alone, regional arguments are not ruled out".

At the same conference the DGFT also took the view that the regional dimension could not have great weight in the MMC's proceedings, essentially for two reasons: first, because the Anderson Strathclyde (HMS0,1982b) case proved how difficult it was for the MMC to come to a clear-cut decision, largely because of disagreement about the likelihood of the company and regional effects; second, because the burden of proof specified in the legislation is favourable to takeovers and mergers so that:

> "the desirability of maintaining a balanced distribution of industry and employment is more

> likely to be significant for the MMC when considering whether a takeover that has adverse effects on competition should nevertheless be permitted - evidence may show that the target company may fail and redundancies arise without the takeover - than as an adequate basis for making an adverse finding when competition problems are absent."

There appears, therefore, to be an asymmetry in the treatment of expected regional effects: regional grounds are generally not sufficient to prohibit a merger but can be sufficient to allow a merger to proceed; the regional effects of takeovers are held to produce no expectation of detriment.

5.2 A Critique of Current Practice

It is our view that questions about the adequacy of the legislation to deal with regional considerations, while important, are secondary to the issue of the appropriateness of the authorities' treatment of the matter within the existing legislation.

Three issues are relevant: the nature of the evidence concerning regional detriments; the relation of regional effects to the "public interest"; and the role of mergers policy. We contend that it is the authorities' views and perceptions of these matters that accounts for current practice.

a) Evidence on the Regional Effects of Takeovers

At the conference noted above, the DGFT cited the Anderson Strathclyde case as indicating the difficulty of establishing detrimental regional effects in merger cases. But it is worth noting that the majority of Commission members in that enquiry did consider that the regional effects produced an expectation of detriment. Moreover, in both the Royal Bank and Highland Distilleries cases (HMSO, 1982a; HMSO, 1980) Commission members appear to have been in broad agreement

about the nature and significance of expected detrimental regional effects.

Even if in the late 1970s and early 1980s evidence on the regional effects of takeovers was "weak and speculative", our knowledge today is much greater than it was then as the above discussion of the evidence shows. Moreover, we have shown above that the ALS study concluded that while acquired Scottish companies on balance benefited from acquisition, the effects on the wider Scottish economy appeared to have been negative. Indeed, the severance of local linkages and loss of key operational and management functions in the acquired firms was held to be sufficiently widespread and pervasive to warrant the conclusion of a clear **probability** of functions being lost rather than gained, to the detriment of the Scottish economy.

The ALS study could not be certain that this evidence amounted to an expectation of detriment within the terms of the Fair Trading Act but it was felt that the probability of loss was sufficient to justify the OFT in recommending referral of a proposed merger to the MMC [4]. The MMC would then investigate more closely to ascertain whether in the particular case there was sufficient expectation of loss of functions to constitute a detriment. Even then, of course, a finding of detrimental effects need not necessarily imply that a particular proposed merger should be prohibited. What it means is that in such circumstances those proposing the merger must then demonstrate an expectation of benefits, sufficient in the view of the MMC to compensate for the external detriments.

So while one might wish to debate whether a "probability" amounts to an "expectation" of detriment to the wider regional economy, we feel that the DGFT's view that these effects:

> "are really not specific to any particular merger. They concern the effects of takeovers in general by firms from outside Scotland and the long-term damage to the Scottish economy of erosion of skills and losses

in the requirement for professional and financial services. In any case there are many reasons for such erosion and such losses besides takeovers" [5]

is misleading and beside the point. It is "misleading", because the evidence suggests that the effects, or their source, are sufficiently large to be associated with particular mergers - it is not a matter of a significant general effect reflecting an accumulation of imperceptible and therefore immeasurable effects at the acquired company level. And it is "beside the point" because to argue correctly that there are many reasons for such losses should not mean that one ignores a principal and identifiable cause. Presumably the DGFT would not argue that the effects of a merger on competition in an industry should be ignored simply because other forces were operating to increase concentration and reduce competition in the sector. We see no reason why he should adopt that position towards the regional effects of mergers.

b) Regional Effects and the "Public Interest"

In our view, the Fair Trading Act clearly implies that if there are reasons to expect that a merger will be detrimental to the interests of one of the less prosperous regions, there is a case for referral to the MMC. But the phrasing of the legislation has allowed an inconsistency to arise between the referral criteria employed by the OFT and the criteria to be adopted by the MMC. Put briefly, this inconsistency means that in making a referral the question of the public interest, as defined by the 1973 legislation, may be ignored but once a referral has taken place the public interest must be considered. We have also considered this particular issue in some earlier work and argued for a change in the legislation (Ashcroft & Love 1988). Logic suggests that the grounds for referral conform to the criteria laid down by the Act for use in the inquiry once the bid has been referred. A change in the wording of the legislation, as suggested by the Scottish Council Development and Industry [6], to bring "grounds of public interest" into the referral criteria would make this obligatory and explicit.

However, the legislation does not articulate the weight to be given to competition and consumer/price effects on the one hand and regional effects on the other. It is evident from the various official statements on the matter that if regional effects are considered at all they are given a much lower weight by both the OFT and, on recent practice, the MMC. The essential reason for this stems from a belief in the primacy of market forces. In Sir Gordon Borrie's words:

> "....current Government policy is based on the belief that the interests of all parts of the UK will be best served, in the long run, by the freest possible operation of market forces." [7]

Armed with this belief it is easy to view any direct and harmful effects on regions as simply interregional equity issues that are the unfortunate outcome of the national wealth maximising effects of market forces in general and the operation of the market for corporate control in particular. It can then be argued that equity issues should clearly be given minimal weight in mergers policy which is after all an economic policy. And such issues are best handled by interregional income transfers through the tax and benefits system, or other non-economic policies.

The difficulties with this view are twofold. First, it assumes that the national economic benefits from the takeover process are considerable when they appear from the body of academic evidence [8] to be at best quite small. Second, it ignores the findings of much academic research as well as casual empiricism which suggests that the large and widening regional imbalances in the UK, a product of largely unfettered market forces, are damaging to national economic performance [9]. Indeed, the tenuous nature of Sir Gordon's and the Government's stated belief in the primacy of market forces is highlighted when one remembers that Government competition policy, and Sir Gordon's own official role, is a response to the failure of market forces to guarantee competition. So for

mergers that restrict competition he is not prepared to accept that company shareholder's know best, yet he is prepared to adopt that position when it comes to the wider regional effects of mergers which, in worsening regional imbalance, serve to damage national economic efficiency.

It is, however, not unreasonable to argue that the likelihood of detriment from the regional effects of takeovers may be weaker than that from the restriction of competition, since the latter is buttressed by a well-developed economic theory and has much empirical support. We would not necessarily disagree with this view, but then it is no part of our argument that regional considerations should be dominant, only that they should be given greater weight in the referral process and the MMC investigation.

c) The Role of Mergers Policy

Even if the authorities accepted some of the above arguments about the regional effects of mergers, it does not follow that they would accept our recommendations for greater weight to be given to them in the application of mergers policy. Again a fragment from Sir Gordon's speech at the Hostile Bids Conference is illustrative:

> "It is not thought that mergers policy should be used as some sort of selective and highly speculative form of regional assistance."

And in one of his answers to questions Sir Gordon reinforced this point by noting that matters of regional policy were not the appropriate business of the competition authorities. But it is difficult to see why mergers policy should be limited to competition issues when it can be clearly demonstrated that mergers have a wider impact than competitive effects. It is surely a mistake effectively to argue that other Government policies and institutions must treat the symptoms simply because the organisation of the functional responsibilities of Government departments and agencies prevents policy focusing on the cause.

To summarise, there are inadequacies in the mergers policy legislation in the treatment of the regional effects of takeovers, but it is the application of the legislation in this connection that gives us most cause for concern. Insufficient weight is given to recent evidence on the regional effects of mergers and its implications for the public interest. The focus of mergers policy is the "public interest" as defined by the Fair Trading Act. In our view, that Act's expression of the desirability of maintaining a balanced distribution of industry and employment in the UK, is not simply - or even - a sop to regional special pleading and interregional equity considerations but constitutes a recognition by Parliament that mergers may have harmful effects on both regional and national economic welfare other than through restrictions on competition.

Notes:

1. A qualifying merger is one which satisfies at least one of the following criteria:

   i) the merged enterprise will consume or supply at least 25% of the relevant market;

   ii) the gross value of worldwide assets taken over exceeds a certain value (currently £30 million).

2. "Mergers: a guide to the procedures under the Fair Trading Act 1973", HMSO, London, 1985.

3. "Hostile Bids and Investor Loyalty", organised by Scottish Financial Enterprise and held in Edinburgh during May 1989.

4. And note that the evidence of ALS suggests that the OFT's focus on the direct employment effects of a regional takeover may be misplaced. In the acquired Scottish companies studied employment tended on average neither to increase nor decrease. Other external consequences of takeover were considered to be more important in determining the public interest consequences of regional acquisitions.

5. "Hostile Bids and Investor Loyalty" op cit 1989.

6. Paper presented to the conference "Whose Business are Business Mergers?" organised by the Law Society of Scotland and held in Edinburgh during March 1990.

7. "Hostile Bids and Investor Loyalty" op cit 1989.

8. For a brief and accessible survey of the methodology and results of this literature see J H Love & J Scouller (1990).

9. The effect of regional imbalance on Britain's economic performance is clearly discussed in David Smith (1989) North & South, Penguin.

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