Britain: the take-over battle for Marks & Spencer

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The recent take-over battle for Marks & Spencer, the doyen of British retailing, exposes much more than the dubious activities, social mores and relationships of the City speculators warring over control of the high street chain. It brings into sharp relief the economic and social decrepitude of British capitalism at the beginning of the twenty-first century.

For the last 20 years or so, hostile and rival take-over bids have been accompanied by public slanging matches between the rival parties. The bidders seek to convince the shareholders that the present directors are making a lousy job of delivering "shareholder value," while the incumbents try to defend their record, slag off the credentials of the bidders and rubbish their plans.

The battle for Marks & Spencer was somewhat different. Little was said on either side about their "vision" or "strategy" for delivering shareholder value until the end. Instead, for weeks, the press was full of the sordid goings-on of Britain's financial and corporate elite involved in the takeover.

Entrepreneur and Monaco-based tax exile Philip Green, whose private equity company runs the second-largest retailing chain in the UK, has long sought to take control of Marks & Spencer. Rebuffed five years ago, it had been the tea-room gossip in the Square Mile for weeks that he was trying to put together another bid.

Marks & Spencer, which has the single largest share of the clothing retail market at 25 percent—but was down from 30 percent five years ago—has struggled in recent years to make the profits that the City demands. A series of top executives, complete with their new revitalising packages to turn around the ailing giant, have come and gone as success eluded them. When the store turned in disappointing fourth-quarter results in April and shares fell, a bid seemed likely.

On May 27, after weeks of rumours, Green was forced by the Takeover Panel to admit his plans to bid for the company. He announced that he would buy M & S's shares at 290 pence a share when shares were trading at around 280 pence. The shares promptly rose to 380 pence in anticipation of a furious bidding war.

On May 31, M & S's board of directors thanked Chief Executive Roger Holmes and Chairman Luc Vandevelde for their services and paid them off with the now-customary and very generous golden handshake for failure.

After casting around for a new CEO, the board parachuted in Stuart Rose.

Rose promptly rejected Green's takeover bid. The price was just too low. They would not entertain anything less than 400 pence a share.

Rose is the kind of sleek operator that the City likes. He had served 17 years with M & S before leaving when he realised he was not going to get the top job. He made his reputation at his next jobs by getting the take-over bid price up and collecting a hefty payoff for his trouble.

His brief from M & S's top management was to fend off the long-expected but unwanted bid that could cost top management their well-paid jobs and turn round the store. According to the *Financial Times*, Rose has an agreement with M & S that could earn him almost £3 million in his first year. This is made up of a £850,000 basic salary, a bonus of up to 100 percent, and a £1.25 million golden handcuff and share options based on three-year performance targets that have yet to be disclosed. His hapless predecessor got a mere £600,000 a year.

Rose is on a 12-month rolling contract, so if Green had come up with an offer for M & S that shareholders could not refuse, he would have been in line for a very lucrative payoff for just a few weeks' work.

Rose had never made any secret of wanting to run the show. Just weeks before his appointment as CEO, he had himself been involved in discussions to take over the company, first with the billionaire property developers, the Reuben brothers, and then with Philip Green, a long-time friend. At one point, it was even thought that he would put together a management buyout.

On May 7, just an hour and a half after receiving one of a number of phone calls from Green to set up a meeting during which both Green and Rose state that M & S was not discussed, Rose invested £100,000 in M & S shares, which started to increase sharply in value just before Green announced his bid. He was not the only one. It was only one of a number of unusual share purchases that looked suspiciously like insider dealing.

On Sunday, May 12, Rose went to see Green in his London office. Green first insisted that his good friend Rose sign a confidentiality agreement not to talk about what was to be discussed to anyone. He then tried to persuade Rose to back his bid, offering him the prize of the top job if they were successful. Rose turned him down.

Soon Rose was under investigation by City Regulator, the Financial Services Authority (FSA) for buying 100,000 shares in the company in the run-up to a take-over bid. He is the first top-100 CEO to have the distinction of being hauled in front of the (feeble) City watchdog to explain his actions.

A host of other well-known figures also had some explaining to do. Michael Spencer, a close friend of Rose and one of the City's richest men, bought 2 million shares worth £5.5 million after lunching with Rose in May. The children's trust fund of Scotland's richest man, Tom Hunter, bought 375,000 shares, and the property developers, the Reuben brothers, bought 860,000 call options.

They had nothing to fear. Famous for its dilatory investigations that have been known to last for years and come up with nothing of substance, the FSA pulled out all the stops and exonerated Rose and Spencer in an unprecedented 13 days.

Then things descended into a farce that dominated the front pages of the newspapers for weeks.

*There was a huge fracas over whether Rose had leaked his confidential meeting with Green to someone at the Chelsea Flower Show.

* That led to a very public bust-up between Green and Rose outside M & S's head office.

* Someone got hold of Rose's mobile phone records, and details of whom he had called and wined and dined were leaked to the press.

* According to Rose, his wife's bank statements were intercepted.

* Rose's friends accused Goldman Sachs, Green's advisors, of orchestrating a smear campaign against him.

*Both sides accused each other of corporate espionage, with the city pages of the press full of stories about what corporate sleuths and gumshoes get up to on their clients' behalf.

* Green sent prostitutes' cards to Rose in response to requests to all of Green's advisors requesting, under the Data Protection Act, details of any information they held about him.

* Writs for reputational damage started flying.

* Green lost his cool when being interviewed on Channel 4 News.

On June 16, Green upped his offer to offer to 370 pence a share, valuing the store at £8.5 billion, and demanded that M & S talk to him. The M & S board rejected that, too. Then, on July 7, he made his final offer at 400 pence a share, equal to £9.2 billion. This was getting close to what the City wanted and the level that the M & S board had said it would consider.

But again the board rejected it. On July 12, Rose announced his plan for delivering shareholder value, and two days later, M & S's shareholders at the AGM refused to take up Green's offer. Despite having the support of 35 percent of the shareholders, Green withdrew his bid and flounced off to Monaco.

The corporations, management gurus and the media portray business success as a function of the personal qualities and expertise of top management who have a toolkit of techniques that can endlessly improve efficiency, turn round ailing firms and deliver the ever-rising profits that shareholders demand. It never occurs to these people that their difficulties may be the result of wider objective processes beyond their control.

Though Marks & Spencer started out more than 100 years ago, its development as a huge retail chain was bound up with the post-war economic expansion that enabled broad layers of workers to buy clothes, household and other consumer goods on a scale that was never possible before. With its products designed to appeal to the broad mass of the population, it became Britain's largest and most popular clothing chain.

It widened its product range from clothing to ready prepared meals, alcohol, household goods and furniture. It turned to consumer credit, and finance became its most profitable line. When faced with the limits of the domestic market, its strategy was twofold. It sought to expand overseas where its winning formula was less easy to implement, and to reduce its costs by cutting staff and sourcing its goods in low-wage economies.

By the late 1990s, its phenomenal growth came to a halt and profits slumped. Every year, it began new initiatives aimed at different segments of the market that failed to catch on. This was not just a failure of design or pricing. Rather, Britain's ever-increasing social polarisation had a logic of its own, and people' shopping habits reflected it with the ever-greater market segmentation. It was no longer so easy to cater to all social layers.

In this regard, just consider what it was that Rose offered to do to placate the shareholders.

He would close some stores, lay off 650 workers, and cut costs and product lines. Most of the cost reductions would come from better "supply chain management"—a euphemism for forcing the burden of adjustment onto the already impoverished workers in the sweatshops of Morocco, Sri Lanka, Bangladesh, etc. In all, he aimed to take £250 million worth of costs out in 2005-2006 and £320 million in 2006-2007.

But the main plank of his strategy was to "hand back" £2.3 billion in cash to the shareholders, equivalent to a pound a share. The institutional shareholders—the insurance companies, pension funds and unit trusts—could get even more. To do this, he had the high street stores revalued at £3.6 billion, an increase of £1.4 billion on their book value, so that they could be used as collateral for a loan.

In other words, he was loading the company with even more debt to buy off the institutional shareholders, making future profits and survival even harder to deliver. In addition, he would raise £762 million from the sale of its financial services arm—its most profitable subsidiary—to the high street bank, HSBC.

This was not so much a plan to turn round the company as to loot it.

It reveals the depth of the economic crisis facing British capitalism and the parasitism of the entire financial system—a far cry from all the rhetoric about the capital markets providing finance for investment and expansion. But this in turn means that an ever-smaller workforce has to work even harder to pay back the banks and deliver dividends to the shareholders.

This was not the first time that M & S had mortgaged the future on behalf of the shareholders. Green made the point that a cash handout would only make the situation worse. "They gave back £2 billion to the shareholders in 2000 and the business went backwards. It would add £135 million a year in interest costs and could bring earnings down," he said.

Such was the cynicism among the analysts in the press that many doubted that Rose could even achieve his cost-cutting targets. Why then was there opposition to Green's bid? After all, there was little to choose between the two. M & S would be loaded with debt, either way.

Unlike most take-over battles, this was not an attempt by one public corporation to take over another. Instead, it was a private equity deal. The move to private equity, while still small, is increasing.

Green and his family were to put a staggering £1.6 billion of their own money in and raise the rest in loans to take over M & S, which he would keep as a private company. But Green does not come from an old moneyed family. That such a person can raise so much money is yet another indication of the extent to which a small layer has enriched itself in this last period. As he repeatedly said, the £12 billion that he had raised to buy and refinance M & S was a lot of money, and he was the only person in Europe to have persuaded the banks to promise so much.

A private equity deal would have loaded the chain store with debt, slashed costs, and stripped the assets. But the corollary of this is that the surplus value created by the working class accrues to a few private individuals and banks, rather than a wider body of shareholders and shareholder institutions, in turn increasing the wealth of an ever-smaller financial elite. With blue chip companies such as Marks & Spencer representing an important source of investment for the big financial institutions, they did not look kindly on a deal that would have taken its profits out of their orbit. Hence, their reluctance to back Green's bid.

This was why the battle for M & S was Britain's most venomous since Lord Hanson, the corporate raider and Margaret Thatcher's favourite businessman, tried and failed to take over Britain's then premier company, the chemical giant ICI, in 1991. In that battle too, Hanson was up against huge vested interests. But that did not stop ICI breaking itself up in almost exactly the same way that Hanson had planned.

Green's bid for M & S is the harbinger of a new form of corporate raid: the virtual bid. While in a traditional take-over deal, the bidder makes a formal offer, with or without the support of the target company's management; in this case, Green simply said he was "thinking" of making an offer, providing certain conditions were met.

Though this avoids the costs and City rules that accompany a formal offer, it makes it more difficult to access the company's financial books. Hence, the bully-boy tactics and dirty tricks designed to discredit M & S's management.

Though this one was unsuccessful, its wider significance lies in the fact that it provides a new weapon for the financial markets to dictate terms to the corporations and squeeze the working class.

Irrespective of which side won, M & S's workforce will be the losers. Six hundred and fifty jobs are to go. Since other "efficiency savings" are required, more will follow. The sale of M & S's financial services to HSBC means the transfer of 1,650 staff to HSBC, which has been at the forefront of outsourcing financial services jobs to India. The finance director refused to give any assurances about their future job security.

Additionally, amid the brouhaha of the battle for the corporate control of M & S, very little attention was given to the impact this would have on M & S's pension fund. To the extent that the media did focus on the issue, its concern was the degree to which the pension fund would act as a "poison pill" and affect the outcome of the take-over battle.

Though the corporation is to raise loans to "give back" £2.3 billion to the shareholders, the pension fund is in deficit by £585 million, although earlier in the year M & S raised a loan of £400 million to plug some of the gap.

According to the trustees, the company's annual pension contributions could climb to between £350 million and £490 million on even the most modest assumptions. But an increasingly debt-laden company would find it difficult to find the cash, thereby affecting the fund's ability to pay both the existing and future pensioners.

There is every chance that the take-over battle will be repeated in the coming period as M & S fails to deliver and the financial elite seeks to defend its interests by whatever means necessary.