This PDF is a selection from a published volume from the National Bureau of Economic Research

Volume Title: A History of Corporate Governance around the World: Family Business Groups to Professional Managers

Volume Author/Editor: Randall K. Morck, editor

Volume Publisher: University of Chicago Press

Volume ISBN: 0-226-53680-7

Volume URL: http://www.nber.org/books/morc05-1

Conference Date: June 21-22, 2003

Publication Date: November 2005

Title: Spending Less Time with the Family: The Decline of Family Ownership in the United Kingdom

Author: Julian Franks, Colin Mayer, Stefano Rossi

URL: http://www.nber.org/chapters/c10277

10

Spending Less Time with the Family
The Decline of Family Ownership in the United Kingdom

Julian Franks, Colin Mayer, and Stefano Rossi

Entrebrawneurial Britain
I strut around my stately life
Hand in hand with lover and wife.
I even own a share or two
In a family firm my father grew.

Of course I have not the slightest view
On what this firm is supposed to do.
Nor have I any reason to care
Since *in absentia* I sit in a Chair,
Of a Board that yesterday I chose to hire
And tomorrow I've decided that I will fire.

Julian Franks is professor of finance at the London Business School. Colin Mayer is the Peter Moores Professor of Finance in the Saïd Business School, University of Oxford. Stefano Rossi is a Ph.D. candidate in finance at the London Business School.

We are grateful for helpful suggestions on this and a companion paper ("The Origination and Evolution of Ownership and Control") from participants at conferences at the American Finance Association meetings in Washington DC, January 2003, the National Bureau of Economic Research Program on the Evolution of Family Ownership conference in Boston, INSEAD and Lake Louise, the Political Economy of Financial Markets Conference at Princeton, September 2003, and the Research Institute of Economy, Trade, and Industry (RIETI) Conference on Comparative Corporate Governance: Changing Profiles of National Diversity in Tokyo, January 2003, and at seminars at the Bank of England, the Bank of Italy, Cambridge University, the London Business School, the London School of Economics, Studieförbundet Näringsliv och Samhälle (SNS), Stockholm, the Stern School, New York University, Université Libre de Bruxelles, University of Bologna, and University of California, Los Angeles. We have received helpful comments from Brian Cheffins, Barry Eichengreen, Charles Hadlock, Leslie Hannah, Cliff Holderness, Gregory Jackson, Kose John, Hideaki Miyajima, Randall Morck, Hyun Song Shin, Oren Sussman, Elu von Thadden, and Xavier Vives.

10.1 Introduction

The United Kingdom is a strange country. It does not have concentrated ownership; most countries do. It does not have pyramid structures; most countries do. Family ownership is of limited significance; in most countries it is extensive. There are few dual-class shares; in many countries they are extensive. It has an active market in corporate control; elsewhere, it is largely nonexistent.

By way of a measure of its peculiarity, Becht and Mayer (2001) report that in a majority of listed Austrian, German, and Italian firms there is a single voting block of shares that commands a majority of votes in these companies. Families account for 45 percent of blocks in Austria, 32 percent in Germany, and 30 percent in Italy. The average size of the blocks is 26 percent in Austria, 27 percent in Germany, and 20 percent in Italy. In the United Kingdom, on average the largest voting block will usually cast under 10 percent of votes, while less than 5 percent of blocks are attributable to families, and the average size of their blocks is only 5 percent. There is a stark contrast in the significance of families in corporate control between the United Kingdom and the rest of Europe.

Even by the standards of the United States, the United Kingdom is odd. Dual-class shares are by no means absent from the United States. Powerful families established some of the largest corporations in the United States, and pyramids were, at least at one stage, widespread. The United States may be odd, but Britain is even more peculiar.

Why is the United Kingdom so different? Was it always so deviant? The British business history literature would seem to suggest not. Family ownership has been a dominant theme in British business history. Alfred Chandler developed a thesis of comparative industrial performance around differences between managerial capitalism in North America and family organizations in Europe. He argued that the United Kingdom was held back at the turn of the century by a continuing reliance on family as against professional managerial capitalism. Successes were restricted to industries in which there were modest investment requirements, most notably branded packaged goods. Companies such as Beechams, Cadbury, Colman, Reckitt, and Rowntree were dominated by their owners and had little professional management. The consequences were most seriously felt in those industries that required large-scale investments—chemicals, electrical equipment, and metals; these declined markedly in relation to their German and U.S. competitors. David Landes (1965, pp. 536–64) described the stereotypical image of the British family firm as being an organization founded by fanatical fathers and succeeded by squabbling siblings who "worked at play and played at work."

According to this view, at the beginning of the twentieth century, as in most other countries, powerful families dominated the British corporate

sector. They may have been incompetent, but at least they were there, and presumably their extinction was a consequence of their incompetence. As a result, the origins of the British corporate system are quite conventional, and its current anomalous status is a consequence of the normal workings of market forces.

Plausible though this story is, we argue in this paper that it is probably not an accurate and certainly not a complete description of what transpired. At the very least, it does not capture the rich interaction that occurred between financial markets and companies in the United Kingdom.

There are many aspects of this that are misleading. The first is that while families were important at the beginning of the twentieth century, their significance did not in general derive from long-term large-scale ownership of British companies. By way of ownership, families were rapidly marginalized. The pattern of ownership, which we report above as characterizing corporate British today, emerged early in the twentieth century.

Instead, the significance of family influence claimed by Chandler comes from a different source. While families rapidly relinquished ownership, they retained control through their positions on the boards of directors. They often held the all-important position of chairman of the board, and even if they did not, then their board representation was frequently disproportionate to their ownership stakes. This is quite different from the pattern observed in Continental European countries of extensive family ownership with delegated managerial control. In Britain families exerted power without responsibility, whereas in most countries they had responsibility with at least limited power.

Still more interesting than the nature of ownership and control was the process by which it came about. Family ownership did not for the most part decline because families sold out. They did not typically abandon firms through company flotations or share sales. Instead, their holdings were diluted in the process of issuing shares to finance growth. In a sample of firms that we will describe below, we estimate that issues of shares associated with acquisitions, rights issues, and placings accounted for almost two-thirds of the decline in directors' shareholdings over the period 1900 to 1950. A majority of this issuance arose from one particular activity of firms, namely acquisitions. More than half of the dilution (36.2 percent) of the 61.6 percent is associated with issues of shares for acquisitions. Shares were not primarily issued to finance internal investments but rather to acquire other firms.

The changing pattern of ownership of British firms during the century was primarily a product of the immense amount of takeover activity that occurred during the twentieth century. Hannah (1976), for example, documents the three major merger waves that occurred around 1900, 1920, and 1930. Many of these mergers were consolidations of several companies, establishing the corporate groupings that dominated the rest of the century.

What is remarkable about this process of ownership dilution is that it occurred in largely unregulated equity markets with little protection to minority investors. In this paper we explore this acquisition process. We document how it went through various stages. In the first half of the twentieth century there was no market for corporate control. All mergers were the result of an agreement between the two or more boards of the merging companies. Often a holding company was created to buy all the shares of the combining firms, with the old boards of directors forming a new board. Mergers were the result of cooperation rather than competition between companies for a target in an auction market.

During the 1940s and 1950s there were important changes in the U.K. capital markets. First, following a number of scandals, minority investor protection was strengthened at the end of the 1940s. Disclosure was improved, and antidirector provisions were introduced. Second, there was a sharp increase in institutional ownership. By 1960, institutions were the largest shareholder in more than a third of the companies in our sample. Third, and most significantly, a market for corporate control emerged: "For the first time it became popular for the ownership of public companies to be determined simply by stock market transactions and for control to pass thereby to parties previously unconnected with the firm" (Roberts 1992, p. 183).

Charles Clore launched the first hostile takeover in 1953 for a large shoe chain called J. Sears Holdings. This bid introduced the concept of paying a significant premium for the shares of target firms. Whereas before 1950 there was little difference in cost between partial and full acquisitions, the emergence of hostile takeovers substantially increased the cost of acquiring full ownership. As a consequence, it became attractive to make partial rather than full bids for companies.

Companies responded by attempting to protect themselves and their minority shareholders against the takeover threat. We estimate that within a period of fifteen years about 7.5 percent of listed companies had issued dual-class shares with discriminatory voting rights. In others, they sought protection under the wing of a friendly parent. In particular, in the brewing industry, Whitbread provided protection through large stakes to several local brewers under what became known as "the Whitbread umbrella."

Partial acquisitions, dual-class shares, and strategic block holdings gave rise, at least temporarily, to shareholding patterns that are currently commonplace on the Continent but were previously rare in the United Kingdom. This is a particularly interesting stage in the development of the British corporation because it could at this point have switched into Continental European mode with dual-class shares and pyramids. In Japan, similar takeovers threats in the post-WW2 period prompted the erection of elaborate defenses in the form of cross-shareholdings that have persisted until today. But this did not happen in Britain. Financial institutions had

become steadily more influential investors in equities by the 1950s and 1960s, and with the agreement of the stock exchanges they were able to deny these firms access to the capital markets. The result was the dismantling of the protective measures until they were virtually extinguished by the 1980s. The elimination of dual-class shares and pyramids in the United Kingdom was therefore due to the dominance of institutional investors. In other countries, corporations were more significant holders of corporate equity[1] and derived benefits from the retention of mechanisms such as pyramids and dual-class shares for sustaining control.

Instead, the more enduring response to the emergence of a market for corporate control was regulatory. The Takeover Panel was established in 1968. Its first rules included mandatory bid and equal price requirements ensuring that offers would be made at the same price to all shareholders once 30 percent of a target had been purchased. These two rules had the effect of preventing both discriminatory price offers and the buildup of large share blocks.

By the beginning of the 1970s the key features of current U.K. corporate ownership and control were in place: substantial institutional shareholdings, a hostile takeover market, and extensive minority investor protection. Together they had the effect of establishing active markets in corporate control.

In a companion paper, we have documented that dilution of family ownership has been a feature of the whole of the twentieth century, in large part due to share acquisitions. But not only was acquisition the main cause of the dilution, it was also its main effect. At the start of the century families could expect to retain control over extended periods as directors, if not owners, of their firms, and their approval was required before changes in control through takeover could take place. By the end of the century, family board representation was not sufficient to ensure continuity of control in the face of hostile takeovers. This had two consequences. First, the feature that Chandler had noted of the dominance of management by families was less evident by the end of the century. Second, dilution of ownership had control as well as cash-flow consequences for families. Management had therefore become more professional, and families were unable to preserve the continuity of control that they enjoyed in the first half of the century.

As Davies and Hopt (2004) note, despite similarities in the structure of their capital markets and the common law nature of their legal systems, the United Kingdom and United States today allocate decision rights regarding takeover offers in very different ways. In the United Kingdom they reside with the target shareholders, whereas in those state jurisdictions in the United States that are sympathetic to the use of poison pills as takeover de-

1. See, for example, Franks and Mayer (2001) for data on corporate holdings in Germany.

fenses, most notably in Delaware, they reside with the target management. The exposure of target management to hostile takeovers in the United Kingdom is not therefore simply a product of its common law or dispersed ownership system. Politics, in the guise of the growing influence of institutional investors in the second half of the twentieth century, may have been at least as important in establishing the United Kingdom's unusually active market in corporate control.

In section 10.2 we describe the data sets that we employ in this chapter. In section 10.3, we record the evolution of family ownership, board representation, and the rise of institutional share ownership. Section 10.4 describes the merger and acquisitions process in the first of the century. Section 10.6 looks at how a takeover market emerged in the second half of the twentieth century. Section 10.7 concludes the chapter and examines the implications of these developments for family control of British companies.

10.2 Data

We employ three data sets in this chapter. The first comprises individual firm data on the ownership and board representation of samples of firms incorporated around 1900 and 1960. There were twenty firms that were incorporated or reincorporated between 1897 and 1903 and were still in existence in 2001 and twenty firms that were incorporated between 1958 and 1962 and were still in existence in 2001; we have collected data on all of these. To avoid the obvious bias that might arise from the greater longevity of the 1900 than the 1960 sample, we collected a third sample of twenty firms incorporated around 1900 that are no longer in existence today. We compare the evolution of ownership and control of the 1960 sample with both the surviving and nonsurviving 1900 samples.

The data have been assembled from (a) archives of company accounts and share registers (including names and size of shareholdings) stored at Companies House in Cardiff, and at the Public Records in Kew, Richmond (Surrey);[2] (b) new issue prospectuses at the Guildhall Library in London; (c) annual issues of the *Stock Exchange Year Book,* which lists names of directors and the sources of any changes in issued capital; and (d) official lists of trading of securities from the British Library in London. Share registers provided evidence of annual ownership changes, and the annual returns to

2. Since the beginning of the twentieth century, firms in the United Kingdom have been required to file information at a central depository called Companies House, now situated in Cardiff, Wales. This is a remarkable and largely unique long-run source of data on firms. However, it suffers from one deficiency: Companies House retains complete records on all firms that are still in existence today but discards information on most, but not all, dead companies. We therefore supplemented data from Companies House with a second source of public information from the Public Records in Kew, Richmond (Surrey), which keeps some information on dead companies.

Companies House gave details of resignations of existing directors and appointments of new directors.

From these data, we collected names of directors, their shareholdings (including those of their families), the date and amounts of capital issued in acquisitions, new share issues via public and private placements, and other changes in share capital, such as capitalizations of reserves. We traced the founding family ownership from incorporation until the last family member left the board by recording shareholdings and place of residence of family members, taking account of name changes across generations when, for example, the daughter of a founder married. We also traced shareholdings through intermediary firms. For outside shareholdings, we limited ourselves to stakes greater than 1 percent of ordinary capital. We used newspaper archives to document evidence of tender offers and trading in provincial stock exchanges, especially in the early 1900s.

The second data set collected for this study includes information on antitakeover defenses (dual-class shares, voting right restrictions, and insider block holdings) for about 1,800 listed firms in two London Stock Exchange (LSE) industry classifications, breweries and industrials and commercials.

The third data set comes from Hannah's (1974a) list of takeovers over the period 1919 to 1939 and includes announcement dates of takeovers from the *Financial Times* newspaper, the medium of exchange, dividend changes and board turnover from the *Stock Exchange Year Book,* and share prices from the daily official list (at the Guildhall Library). Newspaper archives are used to document evidence on the hostility of takeover activity, particularly during the 1950s and early 1960s.

10.3 Ownership and Board Representation

10.3.1 Ownership

According to Rajan and Zingales (2003), the United Kingdom has had one of the largest stock markets in the world throughout the twentieth century. Table 10.1 reports the number of companies listed on the LSE and the market value of listed securities for the period 1853 to 1939. As the stock exchange did not collect aggregate statistics over this period, several other sources have had to be used. According to Killick and Thomas (1970) and Michie (1999), around 1850, provincial stock exchanges had more listed companies than the LSE—490 as against 200. Hart and Prais (1956) record a large expansion of listed companies on the LSE over the period 1885 to 1939, although their data refer only to industrial and commercial companies. From 1963, the LSE has kept a continuous series of aggregate equity market values, including preference and dual-class shares. One of the most striking features is the marked decline in the number of listed firms that has occurred over the past forty years (see table 10.1).

Table 10.1 The number of companies and market capitalization of companies listed on the London Stock Exchange (LSE)

Date	No. listed companies: LSE	No. listed companies: Provincial	Source				
			A. Pre-1950				
1847		490[b]	Killick and Thomas (1970)				
1853	200		Michie (1999)				
1885	70[a]		Hart and Prais (1956)				
1907	571[a]		Hart and Prais (1956)				
1913	1,700		Rajan and Zingales (2003)				
1939	1,712[a]		Hart and Prais (1956)				
	United Kingdom					International	
	No. of companies	No. of equity securities	Market value (£/M)	GDP current prices	Market development (GDP/MV)	No. of companies	Market value (£/M)
			B. 1963–2000				
1963	4,409	4,064	32,204				
1970	3,418	3,197	37,793	44,200	0.86	387	57,135
1980	2,747	2,283	86,720	201,000	0.43	394	183,846
1990	2,006	2,081	450,544	479,000	0.94	553	1,124,131
2000	1,904	2,272	1,796,811			501	3,525,701

Notes: This table reports London Stock Exchange statistics on a number of listed companies and market capitalization from various sources.

[a]Industrial companies only (Hart and Prais).

[b]Manchester, Newcastle, Liverpool, and Leeds.

Table 10.2 records family shareholdings of a sample of twenty companies incorporated around 1900 and twenty incorporated around 1960 that were still in existence in 2001 (the "survivors") and a sample of twenty companies incorporated around 1900 that died during the century ("nonsurvivors"). It documents the number of companies where the founding family's shareholding passes a particular threshold of 25 percent, 50 percent, and 75 percent of equity. Franks, Mayer, and Rossi (2004) report that insider ownership declined rapidly and at similar rates in the first and second halves of the century. Rates of ownership dispersion were similar in samples of companies incorporated in 1900 and 1960. Table 10.2 confirms that family ownership was rapidly diluted throughout the century. By 1940, forty years after incorporation, the number of firms in which families owned more than 25 percent of shares had declined from thirteen to four among the survivors. Family ownership was initially even less pronounced among the nonsurvivors (nine out of twenty companies passed the 25 percent threshold), but pro rata to the number of survivors it then declined less rapidly to four out of twelve survivors in 1940.

Table 10.2 Family shareholdings and ownership thresholds

	Survivors				Nonsurvivors				
	25%	50%	75%	*N*	25%	50%	75%	*N*	No. of observations
1900 sample									
1900	13	9	8	20	9	8	6	20	40
1910	10	7	7	20	9	8	5	20	40
1920	11	8	7	20	8	6	4	17	37
1930	7	4	3	20	8	4	3	16	36
1940	4	3	3	20	4	4	3	12	32
1950	3	3	2	20	4	3	3	10	30
1960	2	1	1	20	3	2	1	4	24
1970	0	0	0	20	2	1	1	3	23
1980	0	0	0	20	1	1	1	2	22
1990	0	0	0	20	0	0	0	1	21
2000	0	0	0	20	0	0	0	0	20
	25%	50%	75%	No. of observations					
1960 sample									
1960	16	15	7	20					
1970	8	5	3	20					
1980	7	2	1	20					
1990	1	1	0	20					
2000	0	0	0	20					

Source: Own calculations.

Note: This table reports the number of companies in our sample where the founding family owns more than 25 percent, 50 percent, and 75 percent of issued ordinary share capital, respectively.

Table 10.2 shows that this dilution of family ownership was even more noticeable in the 1960 than in the 1900 sample. For example, forty years after incorporation, there was no company in the 1960 sample in which family ownership passed the 25 percent threshold. Family ownership therefore diminished rapidly throughout the century but much more so in the second half of the century.

Table 10.3 documents how financial institutions emerged to take the place of families as dominant owners of corporate Britain around the middle of the twentieth century. It reports the number of cases where a financial institution was the largest shareholder of our sample of firms. Forty years after incorporation, there were four cases in the 1900 survivor sample where a financial institution was the largest shareholder, compared with thirteen in 1990 for the 1960 sample. The average size of institutional stakes was also larger in the second half of the century. The average stake of the four financial institutions that were the largest shareholders in the 1900 sample was 5.9 percent in 1940, compared with an average stake of 16.2 percent in the thirteen companies in the 1960 sample in 2000. Thus, in

Table 10.3 Is the largest shareholder an institution?

	Survivors			Nonsurvivors		
	Institution	Block size	No. of observations	Institution	Block size	No. of observations
1900 sample						
1900	0		20	0		20
1910	1	5.00	20	0		20
1920	0		20	0		17
1930	0		20	1	6.90	16
1940	4	5.89	20	1	0.90	12
1950	7	3.73	20	3	8.95	10
1960	8	4.18	20	0		4
1970	9	5.35	20	0		3
1980	8	6.46	20	0		2
1990	16	10.77	20	1	11.70	1
2000	17	12.85	20	0		0
	Institution	Block size	No. of observations			
1960 sample						
1960	0		20			
1970	4	4.88	20			
1980	5	16.27	20			
1990	10	15.39	20			
2000	13	16.20	20			

Source: Own calculations.

Note: This table reports the number of companies where the largest shareholder is an institution, along with the average size of these largest block holdings.

the first half of the century institutional shareholdings were largely absent, and where they were present they were quite small. In contrast, in the second half of the century, there were a larger number of stakes held by institutions, and they were much more significant in size.

In summary, family ownership declined rapidly in the first half of the twentieth century, and institutions emerged to take the place of families from the middle of the century.

10.3.2 Board Representation

Table 10.4 shows that family representation on boards persisted for much longer than their ownership. It documents the profile of board representation for the two samples of firms at ten-year intervals. Over forty years from 1900 to 1940, the percentage of board seats held by outside (nonfamily) shareholders in the sample of survivor firms (panel A) increased from 46 percent in 1900 to 64 percent in 1940. The proportion of firms in which families occupied the position of chief executive officer (CEO) of the board

Table 10.4 Board composition

	Board size		Family CEO	Board members outside founding family (%)		No. of observations
	Mean	Median		Mean	Median	
			A. 1900 sample, survivors			
1900	5.40	5.00	16	45.46	41.45	20
1910	5.80	5.00	17	44.48	52.75	20
1920	5.95	5.00	13	59.75	66.60	20
1930	6.45	6.00	10	64.37	72.35	20
1940	6.65	6.00	10	64.16	71.55	20
1950	6.90	6.50	9	71.10	87.50	20
1960	7.20	7.00	4	76.15	100.00	20
1970	9.15	8.00	2	81.88	100.00	20
1980	7.95	7.00	2	86.71	100.00	20
1990	8.25	8.00	2	90.68	100.00	20
2000	7.90	7.00	2	92.51	100.00	20
Mean	7.05		7.91	70.66		
			B. 1900 sample, nonsurvivors			
1900	4.93	4.00	11	68.23	100.00	20
1910	5.33	5.00	10	76.44	100.00	20
1920	5.92	5.50	9	70.34	72.90	17
1930	5.82	5.00	8	72.82	77.70	16
1940	4.86	6.00	5	92.84	100.00	12
1950	3.50	3.50	3	95.83	100.00	10
1960	9.67	8.00	3	100.00	100.00	4
1970	5.50	5.50	2	100.00	100.00	3
1980	7.00	7.00	2	100.00	100.00	2
1990	4.00	4.00	0	100.00	100.00	1
2000			0	100.00	100.00	0
Mean	5.06		7.74	79.42		
			C. 1960 sample			
1960	2.80	3.00	16	43.15	41.65	20
1970	5.55	5.00	12	66.48	77.50	20
1980	6.47	6.00	8	74.94	86.65	20
1990	7.35	7.00	4	82.55	100.00	20
2000	7.00	6.00	3	83.62	100.00	20
Mean	5.83		10.90	70.15		

Source: Author calculations.

Note: This table reports board size and the percentage of board members that do not come from the founding family.

declined from 80 percent (i.e., sixteen out of twenty) to 50 percent (i.e., ten out of twenty). As table 10.2 recorded, the proportion of survivor firms in which families held more than 25 percent of shares declined much more rapidly by 45 percent from 65 percent (i.e., thirteen out of twenty) in 1900 to 20 percent (i.e., four out of twenty) in 1940. Family representation on the boards did not therefore decline as rapidly as their ownership.

Table 10.5 provides a summary measure of this. It reports separation of family ownership and control as measured by the difference between family representation on the boards of firms and family ownership of shares. A positive number means that family board representation is disproportionate to family ownership. Table 10.5 shows that at the beginning of the century, family ownership was in excess of family board representation, but by 1940 it had become disproportionately high.

Panel B of table 10.4 reports lower family board representation among

Table 10.5 **Separation of ownership and control**

	Survivors	No. of Survivors	Nonsurvivors	No. of Nonsurvivors	Full sample	No. of observations
1900 sample						
1900	–1.16	20	5.69	20	1.86	40
1910	6.78	20	2.00	20	4.67	40
1920	–7.87	20	9.88	17	–1.00	37
1930	8.97	20	14.25	16	10.91	36
1940	15.60	20	6.17	12	13.16	32
1950	13.15	20	4.02	10	11.04	30
1960	14.99	20	0.00	4	12.45	24
1970	15.04	20	0.00	3	12.60	23
1980	12.03	20	0.00	2	11.13	22
1990	9.15	20	0.00	1	8.71	21
2000	6.69	20		0	6.69	20
Mean	8.50		6.94		8.13	

	Mean	No. of observations
1960 sample		
1960	–1.52	20
1970	3.13	20
1980	6.70	20
1990	10.50	20
2000	11.94	20
Mean	6.15	

Source: Author calculations.

Notes: This table reports mean and median separation of ownership and control. Separation is defined as the difference between the proportion of founding family members on the board and family shareholdings. A negative value indicates that there is a greater proportion of family ownership than board representation.

the 1900 nonsurvivors than the survivors. Family board representation was only 32 percent in 1900, in comparison to 55 percent among the survivors, and it declined to 7 percent in 1940. There was therefore less family ownership and less family board representation among the nonsurvivors than the survivors in 1900, and families failed to retain board positions among nonsurvivors to the degree that they did in survivors. Table 10.5 confirms that family board representation did not increase to the same extent relative to ownership among nonsurvivors as among survivors. So families retained neither ownership nor board positions among nonsurvivors. Whether the decline of families on the boards as well as in the ownership of nonsurvivors was a cause or a consequence of their demise is not a question to which we attempt to provide an answer here. All we do is to note that the difference in family ownership and board representation among surviving and nonsurviving firms may be an interesting approach to evaluating the contribution of families to corporate performance.

In the second half of the century, family representation on boards declined more rapidly. Forty years after incorporation, a family member was chairman/CEO in three companies in the 1960 sample, in comparison to ten in the 1900 survivors. Likewise, the proportion of seats on the boards occupied by families declined to 16 percent forty years after incorporation in the 1960 sample, in comparison to 36 percent in the 1900 sample. Thus, family representation on boards as well as ownership declined more rapidly in the second than in the first half of the century.

Table 10.4 shows that, relative to their ownership stakes, family representation on boards moved in a very similar way in the 1960 sample compared to the 1900 survivors, starting from slightly more ownership than board representation in 1960 and ending with markedly more board representation than ownership forty years after incorporation in 2000. Thus, families did not match the very rapid decline in their ownership in the second half of the century with their share of seats on boards of firms.

In summary, dilution of family ownership occurred rapidly throughout the twentieth century. As the next section describes, this was primarily due to growth through acquisition. However, in the first half of the century families were able to retain control in surviving firms through representation on the boards of firms. In the second half, board control as well as ownership was rapidly extinguished. A new form of ownership, institutions, emerged in the middle of the century to replace families, and, as we document in section 10.5, a new form of corporate control, the hostile takeover, appeared to replace that exerted by families.

10.4 Mergers and Acquisitions in the First Half of the Century

Franks, Mayer, and Rossi (2004) argue that the main cause of dispersion of ownership during the twentieth century was equity issuance. In particu-

lar, their sample of firms grew rapidly through acquisition and in the process issued equity to outside shareholders, thereby diluting insiders' shareholdings. Franks, Mayer, and Rossi report that insider holdings were diluted over the period 1900 to 1950 at an average rate of 12.6 percent per annum. Of this, none was attributable to initial public offerings (IPOs), 4.6 percent to rights issues, 20.8 percent to placings, and 36.2 percent to mergers and acquisitions.[3]

During the first half of the century, mergers and acquisitions were usually made by the bidder approaching the directors and agreeing to purchase their shares: "An approach through the directors, followed by controlled stock transfers on the recommendations of the directors (rather than contested takeover raids) remained the norm in these years" (Hannah 1974b, p. 68). A price was negotiated, and management wrote to the shareholders stating that "the offer has been unanimously accepted by the Directors of your company for the whole of their individual shares, and they have no hesitation in recommending its acceptance to the shareholders" (*Financial Times,* 19 January 1920). The same terms were offered to outside shareholders as the directors.

As Hannah (1974b) has noted, "The loyalty of shareholders to directors was strong, and the directors of other companies had a natural aversion to challenging it. Even if a direct bid were to be made, the directors of the victim firm remained in a strong position relative to their own shareholders. In practice the shareholders would recognize the superiority of the directors' information and tend to take their advice on the true value of the company in relation to the bid price" (pp. 70–71); "Directors felt a responsibility to recommend offers to their shareholders when the bid price was pitched reasonably" (pp. 68–69). It is therefore unsurprising that there was a complete absence of hostile takeover bids in the first half of the century.

The continuing presence of families on boards, in particular in the position of chairman, even in the absence of ownership, may have been important in upholding reputations. So too were titled directors. Florence (1953) reports that there were 654 English peers as active members of city firms in 1932. Titled directors were particularly common in the largest companies, although "at a rough estimate almost half the titled directors inherited their title or acquired it by prowess in the fighting services or sport and not in business" (Florence, p. 245). Florence notes that "one well-known insurance company in 1937 had among sixteen directors, three knights, one baron, one marquis, one earl and two dukes" (p. 245). Likewise, May (1939) reports that of 654 British peers, 189 of them were directors of companies

3. In the first half of the century shares were often traded without a prospectus. Shares would simply be issued and sold directly by the company to subscribers or be sold through advertisements in the press. The IPO event was much more formal after 1948, when prospectuses were compulsory and their content strictly regulated prior to trading on recognized stock exchanges such as the LSE.

and held 562 directorates between them: "Sometimes a man with a 'good name,' knowing nothing about the business and even without residence in the country, is set up as chairman with the principal duty of reading the annual speech, which has been written out for him, to the shareholders" (May, p. 145). As Lord Justice Scrutton said in the Court of Appeal in the judgment on Combined Pulp and Paper Mills Ltd. 1932, "The company promoter wants a man whose name will appeal to the public and who does not know too much about the business. The name will attract capital—the company promoter will do the rest" (pp. 35–36 of the transcript).

In tables 10.6 and 10.7 we examine the workings of the acquisitions market in the first half of the century. We undertook a series of tests on bid premia, changes in boards, and dividend responses of targets similar to those that are now routinely performed on recent acquisitions in the United Kingdom and United States. We report data on forty-one mergers and acquisitions (M&As) in the United Kingdom over the period 1919 to 1939. This is the entire population of M&As that met three criteria: the market value of target assets exceeded £1 million, the targets were listed on the LSE, and they were classified by the LSE as being in one of three industries—breweries and distilleries; industrial and commercial; or iron, coal, and steel.

Table 10.6 shows the proportion of target directors who were retained on the board after the merger, the number of cases in which the chairman was removed, and the change in dividends around the announcement of the mergers. On average, two-thirds of the target directors remained on the target's board after the acquisition. In fourteen of forty-one cases (approximately one-third of the total), the chairman was removed. In comparison, in a study of thirty-five successful hostile takeovers in 1985 and 1986, Franks and Mayer (1996) report that 90 percent of directors were replaced within two years of the bid's being consummated. The equivalent figure for

Table 10.6 **Takeovers in the United Kingdom, 1919–39: Target board turnover and dividend changes**

Time period	Proportion of target board resigning after takeover (%)	Chairman resigned	Dividend constant	No. of observations
1919–23	5.36	0	10	11
1924–28	33.76	3	11	12
1929–33	16.68	2	7	7
1934–39	57.80	9	8	10
Total	30.28	14		40

Sources: Hannah (1974b) and author calculations.

Notes: This table reports the proportion of target directors that resign after a takeover, the number of target companies where the chairman resigns and the proportion of target companies keeping the dividend constant two years prior to the takeover for a sample of 40 takeovers over the period 1919–39.

Table 10.7 Bid premia in the United Kingdom

Time period	No.	Months –4 to +1 (%) EW	Month 0 (%) EW	Total market value (£/millions)
		A. 1919–39		
1919–23	11	–10.02	–3.34	31.5
1924–28	12	+14.69	+0.55	43.3
1929–33	7	–2.45	–1.13	19.0
1934–39	10	+14.84	+0.22	26.6
Mean		+4.93	–0.90	

	Target	Months –4 to +1 (%) EW	Month 0 (%) EW
		B. Hostile takeovers, 1953–58	
1953	J. Sears	122.22	90.48
1958	Savoy Hotel	87.00	19.53
1958	British Aluminum	39.53	17.47
Mean		82.92	42.49

	No.	Months –4 to +1 (%) EW	Months –4 to +1 (%) VW	Month 0 (%) EW	Month 0 (%) VW	Total market value (£/billions)
			C. 1955–85			
1955–59	151	28	25	16	11	0.5
1960–64	190	24	26	18	14	1.4
1965–69	262	27	24	19	12	3.7
1970–74	196	35	41	25	23	2.8
1975–79	383	38	34	30	22	3.8
1980–84	281	27	27	25	30	10.0
Mean		30	30	22	19	

Notes: This table reports the bid premia for the United Kingdom in the twentieth century. Panel A considers 40 U.K. takeovers over the period 1919–39 and computes premia as the raw (unadjusted) stock returns for targets over the periods (–4 to +1) months and month 0, where month 0 is the announcement month. Panel B refers to the first three hostile takeover bids of the 1950s, as reported in Roberts (1992), and computes premia as in panel A. Panel C refers to 1,463 U.K. takeovers in the period 1955–85 and computes premia as the market-adjusted stock returns for targets over the periods (–4 to +1) months and month 0, where month 0 is the announcement month. The source for panel C is Franks and Harris (1989).

thirty-five accepted bids was 50 percent. Board turnover was appreciably lower in the first half of the century in comparison with both accepted and hostile bids in the second.[4]

4. This might indicate greater private benefits accruing to target directors in the early part of the century.

Table 10.6 also shows very little change in dividends in the year of the bid compared to the previous year in the 1919 to 1939 sample. In comparison, Franks and Mayer (1996) report that dividends were increased in a substantial proportion of both hostile and accepted takeovers in 1985 and 1986. They were increased in 76 percent of targets of successful hostile takeovers in the year before the bid and in 73 percent of targets two years before the bid.

But it is in relation to bid premia that the differences are most pronounced. Panel A of table 10.7 records that in the sample of forty targets target shareholders received bid premia of –0.9 percent during the month of the bid (i.e., "month 0"), calculated on an equal weighted basis. These bid premia are raw equity returns with no adjustment for market movements or risk. Bid premia for months –4 to +1 on the same basis were 4.9 percent. Bid premia were therefore little different from zero. In contrast, Franks and Mayer (1996) report bid premia of between 20 and 30 percent for hostile and agreed bids during 1985 and 1986 in the United Kingdom.

The picture that emerges is one of cooperative consolidations between merging firms in the first half of the century. The support of management was required for approval by shareholders. Bid premia were low, the medium of exchange usually involved share exchanges, management was frequently kept on the target board, and dividend changes were modest. Since acquisitions frequently involved share exchanges, acquiring firms avoided the devaluation of their currency that dual-class shares would have entailed. The absence of dual-class shares in the first half of the century may therefore have been intimately linked to the importance of takeovers and their form of financing.

This picture of cooperation and little competition was dramatically altered in the 1950s, as we will describe in section 10.6.

10.5 Three Case Studies

This section describes three cases that illustrate the way in which three prominent British firms expanded during the eighteenth, nineteenth, and twentieth centuries; the contribution of acquisitions to their growth; the changing nature of family ownership and board representation; and the contribution of incorporation and mergers to that process.

10.5.1 Case Study of GKN

Dowlais Iron Company was set up in 1759 in the village of Dowlais near Merthyr Tydfil in South Wales. John Guest was appointed as manager of Dowlais in 1767, and his grandson became the company's sole owner in 1851. The Dowlais Iron Company was at this stage the largest ironworks in the world, operating eighteen blast furnaces and employing more than 7,300 people. The business was the first licensee of the Bessemer process,

constructing the world's most powerful rolling mill in 1857, and producing its first Bessemer steel in 1865.

The Keen family established the Patent Nut and Bolt Company in 1856 in Smethwick, England. In July 1900, Guest, Keen, and Company Limited was incorporated in Birmingham with the purpose of taking over the Dowlais Iron Company and the Patent Nut and Bolt Co., Ltd. The shareholders of the two companies received 250,000 ordinary shares. At the same time, 400,000 ordinary shares were issued via public subscription, and the company was floated with 546 ordinary shareholders and more than 2,000 preference shareholders. Both classes of shares were traded on the London and Birmingham Stock Exchanges. There was no evidence of the company's being dispersed before 1900: the company history suggests that both Dowlais Iron Co. and the Patent Nut and Bolt were 100 percent owned by directors and their families. Evidence for this comes from a comparison of directors' holdings with the shareholdings of the two companies before the merger. Since directors' holdings after the flotation were 33.6 percent of the ordinary shares, and the newly issued shares were 400,000, compared with a pre-issue total of 250,000 we can compute a lower bound of directors' ownership pre-issue of 87.3 percent.

In 1902 the company acquired Nettlefold and Company, one of the world's leading manufacturers of screws and fasteners, which set up in Smethwick in 1854, by issuing 315,000 new ordinary shares. The new company name then became Guest, Keen, and Nettlefolds Limited, and Mr. Edward Nettlefold joined the board. By 1910, the directors held 26.4 percent of issued ordinary shares. In 1920, shares in Guest, Keen, and Nettlefolds Ltd. (GKN) were quoted at Birmingham, Bristol, Cardiff, Edinburgh, Glasgow, Liverpool, Manchester, and Sheffield, while the prices of the transactions were marked (i.e., reported) on the official list of the LSE.

A crucial decade in the evolution of ownership and control of GKN was then about to begin. First, the company acquired John Lysaght Limited of Bristol (also quoted in Bristol and London) in one of the largest tender offers of the decade.[5] In November 1923 GKN then undertook two other major tender offers, acquiring D. Davis and Sons and Consolidated Cambrian of Cardiff.

As a consequence of these acquisitions there was a huge increase in the number of shareholders: GKN had about 1,000 shareholders before 1920, and more than 20,000 in 1924. At this stage, GKN was one of the largest manufacturing businesses in the world, involved in every stage of manufacturing from coal and ore extraction to iron and steel making and finally

5. Details of the deal are as follows: in January 1920, GKN issued 1,989,919 new ordinary shares and 2,652,331 preference shares. Ordinary shareholders of John Lysaght Ltd. were offered four new second preference and three new ordinary shares in GKN for every three ordinary shares held.

to finished products including the nuts, bolts, screws, and fasteners, for which it was renowned during this period.

On June 14, 1946, GKN formally listed on the LSE. By then the directors owned a negligible stake, and the largest shareholder of the period was the Royal Bank of Scotland, with 2.37 percent of issued ordinary shares. In the second half of the century, Prudential Assurance, Norwich Union Life Insurance, Schroder Investment Management, and Scottish Widows Investment Management, among others, alternated as the largest shareholders, with stakes varying from 3 percent to 5.25 percent of issued equity capital.

The picture that emerges from GKN is of a firm whose shares were initially traded on local provincial exchanges, that expanded rapidly through acquisitions and broadened its shareholder base both numerically and geographically in the process, and that by the beginning of the second half of the twentieth century was widely held primarily by institutional shareholders.

10.5.2 Case Study of Schweppes

In 1783, forty-three-year-old German-born Jean Jacob Schweppe invented an efficient system for the manufacture of mineral water. In 1790, he entered a partnership to expand the business and established a factory in London. Around 1800 he changed his and the business's name to Schweppes, while continuing to expand on a national scale. By 1831, J. Schweppes and Co. became the Supplier of Soda Water to the Royal Household. In 1834, John Kemp-Welch and William Evill bought J. Schweppes and Co. and extended the product range to include flavored soda drinks such as lemonade. The following year the firm was awarded the royal warrant by Queen Victoria, and in 1851 it won the contract to supply "Temperance" beverages at the Great Exhibition in the United Kingdom. By 1870, the firm's product range included tonic water and ginger ale. The former rapidly became popular with the British in India, as it contained quinine, which was used as a preventive measure against malaria. In 1877 the firm opened its first factory in Sydney, Australia, and seven years later a factory in Brooklyn, New York.

The sudden death of John Kemp-Welch in 1885 precipitated the formation of Schweppes as a limited company in the following year. Although no direct evidence exists on the ownership structure at this stage, it would appear that the company was 100 percent owned by the directors until its public flotation in London on March 6, 1897. After flotation the directors and their families held collectively 27.2 percent of the 300,000 ordinary shares. The new company, Schweppes plc, was incorporated to acquire the business of J. Schweppe and Co. established in 1783, and a total of £1,250,000 new capital (of which £300,000 was perpetual debenture stock issued to the directors and £950,000 was a public subscription, in the form

of 300,000 ordinary shares, 300,000 preference shares, and 350,000 deferred shares).

The public flotation was extremely successful and oversubscribed. At the end of 1897, there were more than 1,650 ordinary shareholders and 750 preference shareholders. There was evidence of the company's shares being traded in Manchester.

In 1919 the Kemp-Welch family relinquished the chairmanship (although two members remained on the board until the early 1940s), and under the new chairman, Sir Ivor Phillips, the company started a new period of expansion. Overseas development was conducted through a newly formed fully owned subsidiary, Schweppes (Colonial and Foreign) Ltd. The strategy was to manufacture locally in the overseas countries, in order to reduce the group's reliance on exports. At the end of Sir Phillips's chairmanship in 1940, the company had more than 2,700 ordinary shareholders, and it was formally listed on the LSE on December 19, 1942.

During the 1950s there were several major acquisitions paid in shares: L. Rose and Co. acquired in 1957 with 1,544,400 new ordinary shares, and Chivers and Sons, W. P. Hartley, and W. Moorhouse all acquired in 1959 with together 4,000,000 new ordinary shares. In 1969, Schweppes plc merged with the Cadbury Group to form Cadbury-Schweppes.

10.5.3 Case Study of Cadbury

In 1794, Richard Cadbury, a prominent Quaker, moved from the West Country in Britain to Birmingham. Thirty years later his son John opened a shop at 93 Bull Street, then a fashionable part of Birmingham, to sell tea, coffee, hops, mustard, and a new sideline—cocoa and drinking chocolate, which John prepared himself using a mortar and a pestle.

In 1847 John Cadbury took his brother Benjamin into partnership in 1847, changing the name of the business to Cadbury Brothers of Birmingham, and renting a new factory in Bridge Street in the center of Birmingham. Thanks to a reduction in tax on imported cocoa beans, the business expanded and received the first of a series of royal warrants of appointment by Queen Victoria.

The Cadbury Brothers moved their manufacturing operations to Bournville, United Kingdom, and established the Bournville factory and village, which became an important addition to the U.K. industrial landscape. By the time that Cadbury Brothers was incorporated as a limited company (on June 16, 1899), and the Bournville factory had 2,600 employees. At that stage, Richard and George Cadbury, the sons of the late John Cadbury, owned 100 percent of the ordinary shares.

A crucial year in the company history was 1919, when Cadbury Brothers merged with J. S. Fry and Sons of Bristol, whose product range (e.g., Turkish delight) complemented Cadbury's chocolates. After the merger, the new company was registered as British Cocoa and Chocolate on May 19, 1919,

with a capital of £2,500,000. The two families shared both board seats and company ownership, with the Frys holding four seats on the board as well as the chairmanship and 45.44 percent of ordinary shares, and the Cadburys holding the rest (six seats on the board, and 54.56 percent of ordinary shares). Another former director of Fry also sat on the board.

As the company's operations expanded and factories opened around the world, the Fry family board representation declined, while Cadbury's increased. Shortly before the merger with Schweppes plc in 1969, the Cadbury family held the chairmanship and seven of the thirteen seats of the board of directors, while only one Fry remained on the board. The Cadbury family held slightly more than 50 percent of the ordinary shares, while the Fry family held just over 10 percent. The rest was dispersed among more than 200 ordinary shareholders. There was evidence of trade on both London and Birmingham Stock Exchanges of ordinary and preference shares before the merger with Schweppes in 1969.

These three case studies illustrate the speed with which ownership was dispersed and how much of the dilution of the original family's ownership was due to acquisitions for share exchanges. They also show how one of the founding families came to dominate the merged entity even where the merger was apparently between equals. This dominance persisted as the ownership of the founding family dwindled.

10.6 Takeovers in the Second Half of the Century

In the spring of 1953, Charles Clore, a self-made millionaire from business and property ventures, launched a bid for J. Sears and Co., the parent company of a shoe shop chain, Freeman, Hardy, and Willis. Instead of following the conventional approach of negotiating with target management, Clore mailed offer documents directly to Sears's shareholders over the heads of management. Roberts (1992) writes, "The Sears directors, who were taken entirely unawares, retaliated by announcing the tripling of the dividend. Shareholders were astonished by this sudden largesse, which was perceived as a desperate and irresponsible act on the part of the management. Faith in the incumbent board being thoroughly undermined, there was a rush to sell to Clore, who quickly acquired control of the company. 'We never thought anything like this would happen to us', were the Parthian words of the outgoing Sears' chairman" (p. 186).

The unconventional nature of the approach was reflected in exceptional financial features of the bid. In contrast to the observation made above that dividends did not in general change around acquisitions, the Sears directors responded to the bid by tripling the value of their dividend. While the average value of bid premia had historically been around zero, the bid premium for Sears was 90 percent in the month of the bid and 122 percent in the five months from month –4 to +1.

As table 10.7 shows, there were then several bids that recorded bid premia that were very large by previous standards. In the case of the bid by Land Securities Investment Trust in autumn 1953 for the Savoy Hotel Co., owners of the Savoy, Claridge's, and Simpson's in the Strand, the bid premium was 19 percent in the month of the bid and 87 percent in the five months around the bid. In the bid for British Aluminum by Reynolds Metals of Virginia in 1958, the month-zero bid premium was 17 percent and the five-month bid premium was 17 percent.

It is not entirely clear why the takeover market emerged at this juncture in Britain. Alfred Chandler associates the emergence of a market for corporate control in the United States with the rise in institutional shareholding (Chandler 1990). But, as table 10.3 shows, in the United Kingdom the market for corporate control predated the accumulation of most institutional shareholdings. A more plausible explanation is that the tighter financial disclosures required of company accounts by the 1948 Companies Act provided the basis on which corporate predators could for the first time make reasonably accurate estimates of asset values and earnings, and thus launch bids without the cooperation of the target (Hannah 1974b). In Charles Clore's takeover of Sears, Roberts (1992) reports that "Clore launched his attack on being informed by a partner in the estates agent Healey & Baker that Sears' balance sheet under-estimated the real estate value of the firm's 900 high street stores by £10 million" (p. 186).

The response of the corporate sector was to seek protection against the rapidly emerging takeover market. It initially received a sympathetic ear from the government and the Bank of England, which were concerned about the impact of hostile acquisitions on the corporate sector and the government's policy of dividend restraint (Roberts 1992). All levels of government were involved—including, in the case of the bid for the Savoy, the prime minister, Winston Churchill, who was worried about the possible impact of the bid on his favorite dining club at the Savoy. But while it found this form of buccaneering capitalism distasteful and ungentlemanly, the government felt impotent to do much about it, and in any event, by the time of the next merger wave at the end of the 1950s, it had come around to the view that "Mr. Clore appears to have improved the retail shoe trade of the country."

Unable to gain protection from the government, the corporate sector began to erect its own defenses. Table 10.8 reports incidence of antitakeover measures in three years: 1950, 1965, and 1975. In the case of 1965 and 1975 the table also shows changes (adoptions of antitakeover defenses in existing companies, emergence of new companies with antitakeover defenses, and abandonment by existing companies) from 1950 and 1965, respectively. Antitakeover measures are said to exist if any of the following are present: dual-class shares, voting restrictions, or share blocks by insiders in excess of 50 percent. Statistics are reported for three LSE sector classifications: commercial and industrial, breweries and distilleries, and iron, coal, and steel, which totals more than 2,000 companies.

Table 10.8 **Incidence of antitakeover measures**

	No. of companies	% of listed companies				
A. 1950						
Commercial and industrial	56	3.60				
Breweries and distilleries	13	6.30				
Iron, coal, and steel	4	1.82				
Total	73	3.68				
	Static analysis		Dynamic analysis (since 1950)			
	No. of companies	% of listed companies	Adoptions	New companies	Delisting	
B. 1965						
Commercial and industrial	236	11.80	98	86	4	
Breweries and distilleries	10	10.20	2	4	9	
Iron, coal, and steel	3	2.21	0	2	3	
Total	249	11.15	100	92	16	
	Static analysis		Dynamic analysis (since 1965)			
	No. of companies	% of listed companies	Adoptions	New companies	Dropped	Delisting
C. 1975						
Commercial and industrial	145	7.25	18	7	32	84
Breweries and distilleries	6	6.06	1	0	1	4
Iron, coal, and steel	1	2.08	0	0	1	1
Total	152	7.08	19	7	34	89

Source: Own calculations.

Note: This table reports the incidence of antitakeover measures (dual-class voting, voting restrictions and insider ownership greater than 50 percent) in the United Kingdom in 1950 in panel A, 1965 in panel B, and 1975 in panel C.

Table 10.8 reports that the number of companies with antitakeover measures increased from 73 in 1950 to 249 in 1965. This represents an increase in incidence of antitakeover measures from 3.7 percent of the sample to 11.1 percent between 1950 and 1965. There were 100 new adoptions by companies that were already in existence in 1950, and ninety-two new companies were formed with antitakeover defenses.[6] The incidence of takeover defenses therefore increased substantially during the 1950s and 1960s.[7]

A further form of takeover defense that emerged was to seek protection

6. There is a residual of sixteen companies that were delisted.

7. The companies with antitakeover measures were nonacquisitive companies and did not therefore expect to use their own shares to purchase other companies.

under the wing of a friendly company. The brewing industry was particularly fragmented, with a large number of small local brewers. Whitbread took share stakes in several of these as a way of providing protection against hostile bidders.

For a brief period during the 1950s and 1960s, the landscape of corporate Britain began to resemble that of Continental Europe. There was an unregulated takeover market with the potential for acquiring control through purchases of partial share stakes and discriminatory offers. Companies responded by introducing dual-class shares and voting right restrictions, and pyramid structures emerged as companies sought protection under the wing of others.

But these takeover defenses met with stiff opposition from an influential quarter—the institutional investors and the LSE. They were concerned about the interference with the takeover process, the ability of management to entrench itself behind takeover defenses, and the withdrawal of their voting rights. Under pressure from the institutions, the stock exchange made it known that it disapproved of the use of dual-class shares and would not permit their use in new equity issues.

The intervention of the institutions and the stock exchange proved decisive, and during the 1970s and 1980s companies steadily withdrew dual-class shares. Panel C of table 10.8 reports that by 1975 the proportion of listed companies with dual-class shares in the three sectors had declined from 11.1 percent to 7.1 percent. The number of companies in the commercial and industrial sector that dropped dual-class shares between 1965 and 1975 was well in excess of those that adopted them. By the late 1980s there were only a handful of companies with dual-class shares left among listed companies in the United Kingdom.

Meanwhile, under prompting from the Bank of England, in 1959 the city established a working party to produce a code of conduct for takeovers. This initially yielded a series of ineffectual recommendations, but, in the face of several prominent takeover scandals[8] and under the looming threat of legislation, in 1967 it produced the City Code on Take-Overs and Mergers and created the Panel on Take-Overs and Mergers to enforce it.[9] This in due course established the principle of equal treatment of all shareholders, the requirement of acquiring firms to disclose their shareholdings and reveal their intentions, and the obligation to make offers for all shares at highest prices once 30 percent of the target firm's shares had been acquired. In other words, it re-created by self-regulation the equal price treatment that had prevailed by convention without regulation in the first half of the century before hostile takeovers.

8. One example of this was the Jasper Affair in 1959, involving takeover malpractice and the misuse of building society funds.

9. The power of the panel to sanction firms that do not comply with the code has proved to be highly effective.

What is striking about these developments is the fact that the political process was not at the end of the day guided by the interests of the corporate sector, which sought to limit hostile bids and to erect takeover defenses, but by those of the financial institutions. It was the institutions that prevented firms from implementing dual-class shares and the institutions that drew up the rules by which takeovers were subsequently conducted. It was therefore the financial sector that prevented the United Kingdom from drifting into a Continental-style corporate structure with dual-class shares, pyramids, and limitations on takeovers, and that set the ground rules by which an active market in corporate control could develop. Through the takeover code and panel, the financial sector also prevented the corporate sector from erecting the takeover defenses, in particular poison pills, that became commonplace in the United States. The distinct nature of the U.K. corporate sector is therefore in part a consequence of the dominance of equity institutions that placed shareholder returns above the private interests of either corporate shareholders or management.

10.7 Conclusions

This paper has documented the rapid erosion of family ownership of U.K. corporations during the twentieth century. The dispersed ownership that characterizes the U.K. corporate system today emerged early in the twentieth century. The United Kingdom did not start off life in the twentieth century like Germany or Italy today. In terms of ownership concentration and the involvement of families, it looked more like the United Kingdom today than Germany or Italy.

The observations on the dominance of families in the running of firms are a reflection of their board representation rather than their ownership. Board participation by families became disproportionate to their ownership stakes. There were good reasons for being concerned about this development. The divergence between ownership and control undermined the efficient running of corporations, as documented by Chandler.

But what was remarkable about this was the process by which it came about. The decline in family ownership was not for the most part a consequence of families' selling out but a result of equity issues. These equity issues were not primarily used to finance internal growth (there was rather little use of equity for this purpose in the first half of the twentieth century) but to acquire other companies. Equity-financed acquisitions accounted for a high proportion of the dilution of family holdings.

What is equally striking is the fact that these substantial equity issues took place against the background of informal, largely unregulated stock markets. Nevertheless, shareholders trusted directors to uphold principles of equal price treatment for all. There was little evidence of the partial

share offers and price discrimination that characterizes the takeover market in many countries today.

Why directors abided by this and were not tempted to accept cheaper partial offers at the expense of minority investors is not entirely clear. But one clue comes from the significance of acquisitions and equity issuance to the growth of corporations. Large British companies were particularly reliant on the stock market to fund growth. This may reflect the absence of a local banking system of a type that exists in many other countries and through which companies in those countries are able to establish close relations and borrow on an ongoing basis. To be able to access the stock market, companies in the United Kingdom had to sustain the trust of their shareholders, which in part revolved around ensuring that they were equally treated in new share issues. Discriminatory offers might reduce the costs of particular acquisitions, but these were more than offset by the higher cost of using equity in subsequent acquisitions. Regulation was not therefore required since it was in the self-interest of directors to ensure the fair treatment of their shareholders.

The nondiscriminatory treatment of shareholders in takeovers also goes some way toward explaining the absence of pyramids in the United Kingdom. Acquirers were not able to purchase the partial share stakes in companies that would have allowed them to create pyramids. Target firms were absorbed into the merged company and essentially disappeared as separate listed entities.

However, this collaborative arrangement broke down in the middle of the century in the face of a hostile takeover market. Target directors were no longer in a position to enforce equal price rules since acquirers could go behind their backs and appeal directly to controlling shareholders. Directors initially tried to protect themselves and their minority investors by erecting takeover defenses. For a brief period, the United Kingdom took on the appearance of Continental Europe, with dual-class shares, pyramids, and discriminatory price acquisitions. But the takeover defenses incurred the wrath of the institutions, which mounted a successful attack on them through the stock exchange and succeeded in devising the rules by which takeovers were to be conducted.

Once again the development of the U.K. corporate sector was determined by the interests of shareholders to a degree that probably did not occur in most other countries. At an optimistic level, the reason for the oddity of the United Kingdom noted at the start is the well-developed and efficient nature of its stock market and the dominance of financial institutions that eschewed the private benefits of Continental Europe. Equally plausibly, it is a consequence of its centralized banking system and the unusual reliance of its corporate sector on the stock market during the twentieth century.

References

Becht, Marco, and Colin P. Mayer. 2001. Introduction. In *The control of corporate Europe,* ed. Fabrizio Barca and Marco Becht, 1–45. Oxford: Oxford University Press.

Chandler, Alfred D. 1990. *Scale and scope: The dynamics of industrial capitalism.* Cambridge, MA: Harvard University Press.

Davies, Paul, and Klaus J. Hopt. 2004. Control transactions. In *The anatomy of corporate law,* ed. Reinier Kraakman, Gerard Hertig, Paul Davies, Henry Hansmann, and Klaus J. Hopt, 157–91. Oxford: Oxford University Press.

Florence, P. Sargant. 1953. *The logic of British and American industry.* London: Routledge & Kegan Paul.

Franks, Julian R., and Robert S. Harris. 1989. Shareholder wealth effect of corporate takeovers: The U.K. experience 1955–1985. *Journal of Financial Economics* 23:225–49.

Franks, Julian R., and Colin P. Mayer. 1996. Hostile takeovers and the correction of managerial failure. *Journal of Financial Economics* 40:163–81.

———. 2001. Ownership and control of German corporations. *Review of Financial Studies* 14:943–77.

Franks, Julian R., Colin P. Mayer, and Stefano Rossi. 2004. Ownership: Evolution and regulation. London Business School and Saïd Business School, University of Oxford. Mimeograph.

Hannah, Leslie. 1974a. Mergers in British manufacturing industry 1880–1918. *Oxford Economic Papers* 26:1–20.

———. 1974b. Takeover bids in Britain before 1950: An exercise in business "prehistory." *Business History* 16:65–77.

———. 1976. *The rise of the corporate economy.* London: Methuen.

Hart, P. E., and S. J. Prais. 1956. The analysis of business concentration: A statistical approach. *Journal of the Royal Statistical Society* 119:150–91.

Killick, John R., and William A. Thomas. 1970. The provincial stock exchanges, 1830–1870. *Economic History Review* 23:96–111.

Landes, David. 1965. Technological change and development in Western Europe 1750–1914. In *Cambridge economic history of Europe, Vol. VI: The Industrial Revolution and after,* ed. H. J. Habakkuk and M. Postan, 536–64. Cambridge: Cambridge University Press.

May, Wilfred. 1939. Financial regulation abroad: The contrasts with American technique. *Journal of Political Economy* 47:457–96.

Michie, Ranald C. 1999. *The London stock exchange: A history.* Oxford: Oxford University Press.

Rajan, Raghuram G., and Luigi Zingales. 2003. The great reversals: The politics of financial development in the 20th century. *Journal of Financial Economics* 69: 5–50.

Roberts, Richard. 1992. Regulatory responses to the rise of the market for corporate control in Britain in the 1950s. *Business History* 34:183–200.

Comment Barry Eichengreen

In this paper Franks, Mayer, and Rossi significantly advance our understanding of the history of corporate ownership in the United Kingdom. To be sure, the first phenomenon they trace, the decline of family ownership, is well known. The modest capital requirements, limited scale, and family-based ownership structure of early nineteenth-century manufacturing enterprise are staples of the history of the British industrial revolution. In the 1820s the typical Manchester cotton mill employed 100 to 200 operatives and required capital investment of perhaps £9,000. Neither shared ownership nor separation between ownership and control were essential for establishing or operating such an enterprise. But by the middle of the nineteenth century, with changes in technology and the extent of the market, the representative cotton mill had grown larger, often by several orders of magnitude. Increasingly, specialized management and complex modes of raising capital became the order of the day. Responding to this reality, first joint-stock companies and then limited liability were sanctioned by Parliament in 1844 and 1856.[1] Companies sold shares to individual investors as a way of raising funds for now more extensive investment. They established boards of directors to help run these more complex organizations. With the second industrial revolution centered on the steel, chemical, and engineering industries at the end of the nineteenth century, the importance of scale, scope, and therefore fixed investment and outside finance grew more important still. Share issuance and professional management became the rule rather than the exception. In this way the forward march of technology and markets progressively diluted family ownership and control.

In addition, there is a prominent strand of historical writing on Britain's loss of its early nineteenth-century economic preeminence (the "clogs to clogs in three generations" interpretation) that blames the grandsons of the founding generation of industrialists for effectively running into the ground the firms that their forbears had so diligently worked to create. Educated in the humanities rather than management, the third generation poured its energies—and financial resources—into politics and landed estates rather than the further development of the family firm. The minority of early nineteenth-century firms that survived were sold off to other owners with more narrowly economic objectives.[2]

Barry Eichengreen is George C. Pardee and Helen N. Pardee Professor of Economics and Political Science at the University of California, Berkeley, and a research associate of the National Bureau of Economic Research.

1. These had been available previously through private acts of Parliament, but more restrictively.

2. An influential interpretation along these lines is Landes (1969, p. 336 and following). To quote, "Thus the Britain of the late nineteenth century basked complacently in the sunset of economic hegemony. In many firms, the grandfather who started the business and built it by

While not speaking directly to this interpretation of Britain's so-called relative economic decline, Franks, Mayer, and Rossi shed considerable new light on the dynamics of ownership and control. They show that loss of family control was often the price of public share issues floated to raise finance not for internal investment but to finance expansion through mergers with competing firms. Although there are hints of this finding in, inter alia, Hannah (1976), it has not been documented as thoroughly before. Another of the authors' findings, which appears to be entirely new, is that families, even while having their ownership position diluted, were able to retain control to a surprising extent by occupying a disproportionate number of seats on the board of what was no longer the family firm (often even chairing the board). Moreover, most directors of the company that was the target of the acquisition, and even the chairman, retained a position on the new board. Adherents of the "clogs to clogs in three generations" thesis will nod their heads at this finding, although this is not a connection that the present authors pursue.

Franks, Mayer, and Rossi then document the gradual erosion of disproportionate family control in the second half of the twentieth century, reflecting the growing influence of hostile takeovers and institutional investors. Indeed, what they document is not merely an erosion but a transformation. Whereas families possessed board representation disproportionate to their ownership at the beginning of the twentieth century, by the end of the century substantial family-controlled voting blocks were even less common than in other advanced economies. In the United Kingdom today, dual-class shares through which block holders—often, in other countries, family members—share ownership but not control are virtually unknown.

What explains this transformation? Franks, Mayer, and Rossi argue that disproportionate family representation on the boards of the merged public companies was made possible by the weakness of minority investors' rights. This is consistent with the older historical literature critical of late nineteenth- and early twentieth-century stock flotations and mergers, through which minority investors were often ripped off.[3] But, partly in response to earlier scandals, protection for minority investors was strengthened after World War II. Important reforms included strengthened disclosure requirements through the adoption of the 1948 Companies Act. The

unremitting application and by thrift bordering on miserliness had long died; the father who took over a solid enterprise and, starting with larger ambitions, raised it to undreamed-of-heights, has passed on the reins; now it was the turn of the third generation, the children of affluence, tired of the tedium of trade and flushed with the bucolic aspiration of the country gentlemen. (One might more accurately speak of 'shirtsleeves to hunting jacket—or dress coat, or ermine robes—in three generations'.) Many of them retired and forced the conversion of their firms into joint-stock companies. Others stayed on and went through the motions of entrepreneurship between the long weekends."

3. See, for example, Macrosty (1907).

ability of minority investors to vote with their feet and the ability of firms to launch takeovers on the basis of publicly available information (and thus without the cooperation of the potential target) led to the development of a market in corporate control that threatened the entrenched position of board members. The latter attempted to defend themselves by building large block holdings, developing strategic alliances, and issuing dual-class shares on a significant scale for the first time in British history. But that defense proved temporary: institutional investors, who worked hand in glove with the stock exchange, were able to impose sanctions against firms that engaged in such practices, denying them access to outside finance, if, for example, they sought to use dual-class issues in new equity flotations. The city was able to strengthen sanctions against directors who did not advance the interests of all shareholders, including minority investors, with its Code on Take-Overs and Mergers in 1967. Regulation, notably as a result of the establishment of the Takeover Panel in 1968, cemented this new equilibrium.[4]

It is worth observing that this account is not obviously consistent with the currently fashionable literature emphasizing Britain's common-law tradition as an explanation for the precocious development of its financial markets.[5] Protection for minority investors went from relatively weak in the second half of the nineteenth century to relatively strong in the second half of the twentieth despite no obvious change in legal inheritance. Rather, legal and institutional reforms protecting minority investors responded to past scandals; thus, they may have had an element of path dependence. They also responded to politics and policy in the manner argued by Rajan and Zingales (2003). The openness of the British economy to trade and finance prevented entrenched interests from closing down its financial markets in response to the crisis of the 1930s and thereby diminishing the markets' influence, in the manner of other countries. As a result, the market power and political sway of the institutional-investor community—and the big financial institutions in particular—sufficed to force through reforms strengthening minority investor rights and creating a true market in corporate control.

At this point the reader, his appetite having been whetted, wants to learn more. He wants to know about the nature of the changes in British financial markets and the economy, presumably produced by the crisis of the 1930s and World War II, that enhanced the power of the big financial institutions, allowing them to effectively discipline directors and protect minority investors where they had not been able to do so before. He wants to know why big financial institutions, which were certainly not unrepre-

4. Although the authors only imply, as opposed to arguing, that this too was a consequence of the growing influence of institutional investors.

5. See, for example, LaPorta et al. (1998).

sented in countries like Germany, Japan, and France, did not have a similar tendency to suppress big block holdings, family control, and director autonomy. If it is the precocious development of British financial markets that accounts for the influence of institutional investors, one wonders whether a legal tradition conducive to financial deepening may have been responsible for these developments after all. Or was the emergence of large institutional investors itself a response to the weakness of minority shareholder rights and the shortcomings of investor protection? If inadequate information disclosure and the absence of sanctions against self-interested directors are the explanations for why there did not exist a thriving market in corporate control until the second half of the twentieth century, as the authors argue, then how is one to understand Sylla and Smith's (1995) emphasis on the Directors Liability Act of 1890 (which made company directors liable for statements in prospectuses soliciting buyers for company shares) and the Companies Act of 1900, which strengthened the principle of compulsory corporate disclosure, as the explanation for why British financial markets developed so rapidly around the turn of the century, to the point where they quickly overtook those of the United States? At a minimum, this suggests that the 1948 Companies Act and the 1967 Code on Take-Overs and Mergers were not radical departures from the status quo ante; rather, they had a prehistory whose economic archeology deserves to be uncovered.

References

Hannah, Leslie. 1976. *The rise of the corporate economy.* Baltimore: Johns Hopkins University Press.

Landes, David. 1969. *The unbound Prometheus.* Cambridge: Cambridge University Press.

LaPorta, Rafael, Florencio López-de-Silanes, Andre Shleifer, and Robert Vishny. 1998. Law and finance. *Journal of Political Economy* 106:1113–55.

Macrosty, H. W. 1907. *The trust movement in British industry.* London: Longmans Green.

Rajan, Raghuram, and Luigi Zingales. 2003. The great reversals: The politics of financial development in the 20th century. *Journal of Financial Economics* 69: 5–50.

Sylla, Richard, and George David Smith. 1995. Information and capital market regulation in Anglo-American finance. In *Anglo-American financial systems,* ed. Michael Bordo and Richard Sylla, 179–208. New York: Irwin.