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Should the Unilever Model of Capitalism Be Protected?

The Kraft Heinz bid for Unilever pits shareholder value maximisation against stakeholder value maximisation.

The aborted US$143 billion takeover of Unilever by Kraft Heinz has put a huge amount of pressure on Unilever to increase profit margins and accelerate returns to shareholders. Kraft Heinz, which is 50 percent owned by Warren Buffett's Berkshire Hathaway and 3G Capital, the Brazilian private equity firm, has **pleased investors** by creating value through an ambitious cost-cutting programme since its merger in 2015. It has targeted US$1.5 billion of annual cost savings and is said to be ahead of schedule in this regard.

This has thrown the spotlight on Unilever's much vaunted long-term focus on all stakeholders, the planet and society in general, which is where it believes long-term value can come from. The result is a very different governance model and corporate culture from Kraft Heinz.

Despite being much bigger than Kraft Heinz, with 168,000 employees and annual sales of 52.7 billion euros, Unilever's profit margins are half those of the American firm. Kraft Heinz has been profitable in previous quarters thanks to cost cutting but it has been less successful at boosting sales. In the latest quarter, the company saw a 3.7 percent decline in sales as consumers gravitate more towards fresher and less-processed food products. Kraft Heinz has arguably turned to Unilever where it could repeat its cost-cutting and asset sale approach.

The future of the Unilever model

Unilever has cleverly managed to fend off the unwelcome bid for now. But does Kraft Heinz's failure also say something about the zeitgeist? Are we moving into an era where a focus on creating sustainable value for all stakeholders and for our environment is considered a more desirable approach than a focus on short-term profit maximisation?

There seems to be little doubt that corporate raiders are no longer seen as swashbuckling heroes admired for liberating unrealised shareholder value. Rather they are starting to be seen as contributors to a growing anti-business sentiment and resentment of a "corporate elite" whose only interest is to enrich the already wealthy at the expense of everyone else. Or, as the Financial Times suggests in the article **"Kraft Heinz/Unilever: nowhere men"**, investors with a short-term profit maximisation focus have come to epitomise the "citizens of nowhere" style of capitalism that has helped trigger populist revolts across the globe. Reflecting the public mood, governments may no longer be willing to tolerate the loss of jobs and expertise to enrich shareholders in the short-term.

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The United Kingdom's government has responded to the Kraft Heinz bid by pledging to draft proposals on how to manage controversial takeover bids.

But this bid was but one skirmish in a long battle. It is far from clear whether it is the Unilever or the Kraft Heinz business model that will be successful in the long-term.

The takeover bid has focused attention on the fact that Unilever's margins are lower than those of its peers. Pressure has started to mount on the company to improve its capital efficiency and increase value for existing shareholders. For Unilever, this raises uncomfortable questions. To what extent can it improve short-term performance without compromising its view of long-term value creation? Since the creation of sustainable social and environmental value is a much vaguer and less easily quantifiable (though arguably more important) benefit than the delivery of short-term financial value, can Unilever, and must it, do better at making the non-financial value it is delivering more visible, more understandable and more appealing to shareholders? And even if it manages to do that, is there a bid price at which Unilever's shareholders will yield to a raider irrespective of the social consequences?

Should it be protected?

It is worthwhile asking whether there is a role that government must play. Both the Netherlands and the U.K. are focusing attention on improving corporate governance. Both are exploring ways of encouraging companies to balance short-term shareholder returns with increased social and environmental responsibility and long-term value creation. However, as the recent paper **''Beyond Governance: Towards a Market Economy that Works for Everyone"** by Radix, a London-based think tank, points out, there is little point in encouraging better governance standards "if companies that build such businesses are then subject to takeover by companies that have a different philosophy and may be based offshore. Decades of work might be undone in a matter of months." The paper recommends that corporate governance standards should be part of a public interest test for foreign takeovers.

The culture war between short-term profit maximisation and long-term societal value creation has only just started. It is not clear which way the bulk of investors will eventually go. The Kraft Heinz/Unilever skirmish should remind us that business and political leaders – as well as pension funds – with an interest in long-term value creation have more work to do if their perspective is to prevail.

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