Knowledge

The Decline of an Iconic British Brand

By Morten Bennedsen, The André and Rosalie Hoffmann Chaired Professor of Family Enterprise at INSEAD

There were no sweet goodbyes when Britain lost Cadbury to U.S. food giant Kraft. How did the once family-owned firm run on strict Quaker values fall victim to globalisation?

In late August 2009, Roger Carr, chairman of British chocolatier, Cadbury, received a message from Irene Rosenfeld, chairman of Kraft, America's largest food company: "I'm in the U.K. next week and I wouldn't mind coming over for a cup of coffee." It was an understated opening to a takeover battle that would soon make headlines around the world.

Cadbury's board was quick to reject Kraft's £10.2 billion offer, but when Rosenfeld took the bid public a showdown was inevitable. On one side the 186-year-old independent British chocolate maker, famous for its Quaker history and close ties to the community, and on the other side Kraft, a company that had grown quickly under the wing of U.S. tobacco giant Philip

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Morris.

The British press was hostile to the proposed takeover. Unions campaigned against it and government ministers – including the Prime Minister – were drawn into the debate. Ironically it was Britain's anti-competition legislation preventing Cadbury from purchasing Rowntree's some years earlier (a move which would have created a large company structure more difficult to acquire) which helped open the way for the Kraft takeover.

Hedge funds holding the strings

Once the bid was made public Cadbury's share price soared from £5 to £8.

With 50 percent of the stock already owned by Americans (compared to 28 percent British) many investors were tempted to sell. Hedge funds moved in fast, raising their stake from 5 percent to 31 percent and indicating to Carr they would be happy to trade their stock for a gain of 20p per share.

Convinced the transaction was a fait accompli, Carr set out to get as good a price as possible striking a deal of £8.50. "I'm paid by the shareholders and I delivered huge value to the shareholders … that is my responsibility," he said.

His private thoughts were less straight-forward. "Something has happened to the system that appears to tip the playing field to short termism," Carr later told the Said Business School in Oxford, referring to the role hedge funds played in the deal. "Whilst capitalism is efficient, it may be unreasonable that a few individuals with weeks of share ownership can determine the life-time destiny of many."

Outgrowing family ownership

The reality of the move was not sudden. Cadbury's ownership profile had been evolving since the end of WWI when fears that Europe's leading chocolatier, Nestlé, was looking to buyout struggling British brand Fry, prompted Cadbury to merge with the smaller entity to become the British Cocoa and Chocolate Company. The move doubled the number of family members holding shares in the firm.

Over the next decade the chocolate business faced growing global competition as U.S. firms moved into the European market introducing new countline chocolates – chocolates sold by number not weight. Meanwhile

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Nestlé, which had been buying up smaller Swiss chocolate factories, began to promote their block chocolate heavily in Britain. Cadbury was ready, launching a 15-year-investment programme at the company's Birmingham and Somerdale plants, increasing the scale of operations to enable the manufacturing of one million Dairy Milk bars and 2 million chocolate assortments every day. The price of Dairy Milk chocolate was reduced by 70 percent during this period and 10,000 people were employed.

By the 1940s WW2 rationing forced a slow-down as the newly modernised factories were converted to support the war effort. Once rationing was over the advent of television in the 1950s had a dramatic effect on the chocolate market, as companies found a century of customer loyalty could be overturned by one good television campaign.

The IPO

In these difficult conditions, Paul Cadbury, chairman from 1959 to1965 and great-grandson of the company's founder John Cadbury, faced another challenge - the company's increasing share base. In the early 1960s the number of family members who held shares had increased to several hundred – of which only 10 were actively involved in the business. With non-managing family members keen to have access to their capital, pressure to take the firm public was growing and the Cadbury board floated the company in 1962. For the first time in its history, Cadbury was no longer under direct family control.

Three years after the IPO, Paul Cadbury stepped down to be replaced by his cousin, 36-year-old Adrian. Adrian realised that some aspects of the Quaker business developed over the previous century were now outdated. The collaborative style of management meant decision-making could be slow and he wanted to establish clear lines of accountability and responsibility. Most important of all, he wanted to alter strategy. The business was vulnerable, with an almost total dependence on cocoa. Adrian was also keen to improve the firm's geographical spread and expand the foods division.

In 1969 it merged with soft drink company, Schweppes. For the traditional Quaker firm born out of the Temperance goals of forbearance, this was not an easy move. Schweppes soft drinks were used with alcohol and the company distributed the alcoholic brand Dubonnet. But, lured by the opportunity to extend geographical reach in a fast-moving world, these historic values were overlooked and the merger went ahead.

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The fork in the road

Cadbury, now with an annual turnover of £250 million, was one third the size of Nestlé. But there was an important difference between the two that gave the Swiss firm an even greater advantage. Nestlé had a two-tier share system with registered shares limited to Swiss citizens, protecting it from hostile advances and making a takeover virtually impossible.

Cadbury lacked this insurance and was strangled by Britain’s competition legislation which prevented it from seeking protection in size by acquiring its weakened British rival, Rowntree’s. Nestlé, under no such limitation, put up its own bid and acquiring Rowntree’s for £2.5 billion in 1988, giving the Swiss firm its much longed-for foothold in the British market.

“This was a big fork in the road,” noted Dominic Cadbury (Cadbury CEO from 1983 to 1993 and chairman from 1993 to 2000). “It was *the* great opportunity to create a British world leader in chocolate but we didn’t have a prayer in pulling it off with government thinking at the time.”

When he retired in 2000, Dominic was the last of the Cadbury family to have worked at the company. At this point the family and family trust shares had declined to less than 1 percent.

Company split leaves Cadbury vulnerable

In 2007, American billionaire Nelson Peltz bought three percent of Cadbury Schweppes shares through his hedge fund, Trian Fund Management. Peltz had a plan to bring an easy return to shareholders by separating the confectionary and soft drink divisions. Combined, the company was worth around £12 billion; if separated, the Schweppes was valued at £7-9 billion and Cadbury at £9 billion.

Cut off on its own, Cadbury confectionary would be an attractive takeover target. Nevertheless under shareholder pressure to adopt Peltz’s plan, in 2007 the Cadbury Schweppes board agreed to split the company. The timing was unfortunate. In the spring of 2008, as the credit crunch hit, the cost of demerging rose sharply to £1 billion, one tenth of the value of Cadbury Schweppes.

One year later in 2009, Cadbury did indeed receive the unwanted attention of Kraft foods. For the two former family chairmen Sir Adrian and Sir Dominic the news of the sale to the American conglomerate was “a tragedy”.

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“One hundred and eighty years of history gone,” observed Dominic. “And, I would argue 180 years of being a beacon of good practice ... all gone and it was so easy.”

This post is based on a two-part case study conducted by INSEAD and Deborah Cadbury into the history of the firm until its takeover by Kraft.

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