

## Pub Companies and Tenants

*"Those who don't know history are destined to repeat it" – Edmund Burke*

This response to the consultation is made by "

### REASON FOR SUBMISSION

The above-mentioned book traces the long line, beginning in the 1960s, of official investigations into the brewing and pub industries, with particular emphasis on the 1989 Report by the Monopolies and Mergers Commission (MMC), *The Supply of Beer*, the resulting Beer Orders and their impact. As part of the research for the book, interviews were conducted with over 60 individuals intimately involved in the 1989 Report, including members of the MMC, senior civil servants, the then junior Minister who led the Commons debate on the Report, leading industry executives, and representatives of pub tenants and consumers. In addition, extensive use was made of Hansard reports, and copious amounts of information were obtained under the Freedom of Information Act.

We are making this submission armed both with the combined experience of over 120 years either working in or being closely associated with the industry, and with a highly detailed knowledge of intervention in this industry and its effects. We have learnt that well intended regulation, such as flowed from the 1989 Report, can easily produce highly unwelcome consequences, even the very opposite of what the legislators had intended. We note that it is stated in the Consultation document that the Government is aware of the dangers of unintended consequences and of the importance of proportionality in market intervention; but the tone of the press release announcing the consultation leads us to suspect that, a quarter of a century on, neither the scale of the damage visited on what had been one of the UK's leading industries, nor the risk of repeating the error, are fully appreciated.

### THE BEER ORDERS

By the end of its lengthy investigation the MMC in 1989 had identified a long list of consumer detriments, and it proposed fundamental remedies. These were widely regarded as draconian, and, even after modification by the government, constituted, in the form of the Beer Orders, perhaps the biggest industrial intervention in post-nationalisation Britain.

There were two principal obligations in the Beer Orders: first, that brewers which owned over 2000 pubs – there were six – should completely free from the product tie half of the excess number above 2000; and second, that those same large brewers should allow their tenants to stock one cask-conditioned ale supplied by another brewer.

The authorities' objective was to bring about increased competition amongst the major brewers, which would benefit customers in the on-trade through downward pressure on the retail price of beer and enhanced brand choice. Alongside these expected results, the security and income of tenants would be improved, chiefly through modifications to the Landlord and Tenant Act. What had been glaringly – and, as things turned out, disastrously – lacking from the MMC Report was any detailed consideration of the way these undoubtedly desirable aims would be achieved in practice.

### EFFECT ON CONSUMERS

The most conspicuous consequence of the Beer Orders was that the price of a pint of beer in the on-trade, far from falling, went up – by 50% in real terms (excluding duty) in the 20 years following the Beer Orders, including a leap of around 15% in the first two years alone. Academic and other writers have attributed the increase in varying degrees directly to the Beer Orders. Wholesale prices did indeed decline, as the MMC had surmised, but this simply resulted in a transfer of margin from brewers to the new pub companies. The massive increase in retail prices, the direct opposite of what was intended, represents a colossal policy failure. It also contributed, during the same 20-year period, to an astonishing 53% decline in on-trade beer consumption, which itself contributed to the closure of over 10,000 pubs.

The MMC seems to have expected the major brewers, effectively forced to dispose of thousands of pubs, to concentrate instead on brewing. This was based on a flawed understanding of where the brewers made their returns, and again the opposite transpired, with most of the major brewers exiting brewing to focus on pub retailing. By 2008 the brewing interests of all of the former six major UK brewers, which before the MMC inquiry had had a beer market share of 75%, were concentrated in the hands of just four foreign brewers, with a market share of 84%. Furthermore, in foreign hands the major brewers had abandoned all but two of their leading ale brands. None of this could have been amongst the government's intentions in enacting the Beer Orders.

The MMC also intended that its proposals would benefit regional and local brewers, with which it made clear that it aligned consumers' interests. It expected, for example, that these companies would buy up large numbers of the thousands of pubs that would be coming on to the market; but these pubs were inevitably often of inferior quality, and local companies in any case proved reluctant to buy outlets outside of their heartlands. What positively harmed many smaller companies, however, was the intensification of competition in the wholesale market, with the result that 20 years after the MMC started its inquiry only four of the eleven leading regional brewers and 26 of the 40 local brewers were still in existence.

Thus were yet more brands lost to the consumer. [Within the last decade the reduction in duty paid by the very smallest brewers has improved brand choice, but this has, of course, nothing to do with the Beer Orders.]

The MMC predicted the creation of small pub co-operatives, pooling their buying power in the newly competitive market, but totally failed to foresee the creation and growth of mammoth pub companies, a business model hitherto largely unknown. It was these that bought most of the pubs that came on the market and which captured the benefit of lower wholesale prices, without passing them on to consumers. It is, of course, the supreme irony of this saga that the government now feels the need to regulate the very entity which it largely created.

## EFFECT ON TENANTS

It had been hoped that many sitting tenants would buy the pubs offered for sale by the big brewers, but this didn't happen on any scale, largely because mortgage finance was tight, even where a tenant had the ambition to buy his/her pub. The guest beer provision may have brought some advantage, but because it was available only to the tenants of large brewers, such advantage was often gained at the expense of other tenants, who had no such entitlement and thus suffered a competitive disadvantage. But the tenants of large brewers suffered in another way, namely, because of the extended period of anxiety they were forced to endure whilst the brewers grappled with implementing the Beer Orders. In order to comply, in a relatively short period, with the requirement to draw up new agreements conferring new rights on tenants, brewers issued many tenants with notices to quit. One way or another, some 30% of tenants left the trade within two years. Again, all of this was the opposite of what was intended.

## CONCLUSIONS

Although [redacted], and therefore detached from the current state of the industry and the immediate subject of the consultation, we are able to draw on our knowledge - [redacted] in this industry and its consequences over a period of several decades. We offer our submission as independent and impartial observers. We do not pass comment on the possible detailed effects of the proposals if enacted, but we suggest that several important lessons emerge from the recent history of regulation in brewing and pubs, and specifically from the 1989 Beer Orders.

First, it is of the utmost importance that regulators and interventionists model the range of possible results of their proposals, for without such modelling new regulations represent nothing more than a leap in the dark. [The Trade and Industry Select Committee recommended in 1995 that the MMC should in future produce a detailed assessment of the results expected from its proposals. This recommendation was never adopted.]

Second, regulators should always have in mind that commercial organisations, run by highly incentivised executives and responsible to shareholders, will, if confronted with a threat to their financial interests, not simply bow to that threat, but will adopt all possible measures, including *in extremis* a complete change of industrial strategy, to counter it or remove themselves from it.

Third, attempts to differentiate between operators of different sizes within the same industry from the impact of intervention are likely to produce unfair - and even perverse - results, with no benefit to consumers.

The paramount conclusion is that the unexpected must be expected, and that, at the very least, things will not go entirely to plan. This argues for proceeding with caution, always looking for alternative approaches, and wherever possible advancing in a step-by-step manner. This was not the course followed in the case of the Beer Orders. A lower risk, more targeted approach - consisting, for example, of reform of the (then highly restrictive) licensing system and action on local pub monopolies - seems to have been given scant thought, and the radical solution was implemented in undue haste. It is our hope that the lessons of history will not be neglected in this instance.