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# THE BEER MONOPOLY

## How brewers bought and built for world domination

BRAUWELT
INTERNATIONAL

This book is a publication of
BRAUWELT International
Andernacher Strasse 33 a
90411 Nuremberg · Germany

www.brauweltinternational.com

BRAUWELT International is an imprint of Fachverlag Hans Carl

First published 2016

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Photographs
Hilda Lobinger and Liebenow Fotografie

Front cover design by Cornelie Müller
Design by Büro für Angelegenheiten · www.angelegenheiten.de

ISBN: 978-3-418-00916-2

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# DEDICATED TO RÜDIGER RUOSS

Networker extraordinaire · Founder and President
World Beer and Drinks Forum in Munich

# ACKNOWLEDGEMENTS

This book is the result of true teamwork. Individual chapters cannot be assigned to any one of us, since we both contributed to each one.

We owe a debt of gratitude to the French beer economist Germain Hansmaennel, whose Beer World Monopoly provided us with a model to think about globalisation in a wider context. Our many discussions with him over the course of writing this book helped us formulate our argument. His input into this book is far greater than can be expressed in words.

Over the years we have also benefitted greatly from talks with numerous executives and industry insiders. Our heartfelt thanks go to those we cannot name.

Among those we can, we want to single out for gratitude Theo Baal, Owen Barstow, Dr Tim Cooper and Nick Sterenberg, Wolfgang Drechsler, Dr Evan Evans, Björn Falkeström, Dr Karl-Ullrich Heyse, Lyn Kruger and Keith Lemcke, Charles A. Landsmann, Silvia Liebrich, His Royal Highness Prince Luitpold of Bavaria, Charlie Papazian, Wolfgang Riepl, Tullio Zangrando and Omri Zilberman.

Our thanks go to the many organisers of brewers' conferences around the world, who gave us the opportunity to present our ideas, above all Prof. Guido Aerts, John Brauer, Mario Delicio, Dr Lothar Ebbertz, Dr Josef Fontaine, Ian Jones and Mike Williams, Jaime Jurado, Dr Terry Kavanagh, Krishan Maudgal, Esko Pajunen, and the late Bill Siebel, who is sorely missed.

For all their generosity in sharing their wisdom, errors of fact or judgement are entirely our own.

Many people nonetheless contributed immensely to our ability to get this book out. We are boundlessly grateful to Michael Schmitt at Brauwelt International for hosting the roundtable discussion and for allowing us to reuse material from previously published work.

A special ‘thank you’ is owed to John Harvey, our dedicated first reader, to Simon Tuite for his contribution to the writing and editing of this publication, to Rebecca Jimenez and Jonathan Kovacs for their diligence in sorting out the footnotes and to Lyle Frink for coming up with the title. Many thanks also to Cornelie Müller, our designer, whose great skill and efficiency made it possible for us to meet our deadline. We owe each of them more beer than we can ever carry.

Last but not least, we have to thank our spouses Gabriele Faltermeier and Ernst Hebeker, without whose support this book would never have been finished, and Rüdiger Ruoss without whom this book would never have been begun.

# INTRODUCTION

While it is often said of a book that it has been a long time in coming, this is never more true than for this one; ours has in fact been in the pipeline for about a decade. At various times we have commented on the heady dealmaking that has been the dominant feature of the globalisation of the brewing industry, but have ultimately always refrained from publishing our thoughts. We feared that the window of opportunity for our book to make its appearance between two mega-deals would be brief. In fact, we had to wait until the endgame in the globalisation of the brewing industry, which was heralded in 2015 when the world's number one brewer, AB-InBev, made an offer for the world's number two, SABMiller.

With the disappearance of SABMiller the era of globalisation will be nearly over, simply because there are hardly any blank spots left in the world of beer where a heavyweight beer champion has not made its mark. All the major brewing companies appear to have settled into their seats, namely their dominant positions in their respective markets around the world.

Obviously, dealmaking in the brewing industry will continue as the spade of high-profile craft beer acquisitions in 2015 underlines. However, we forecast that on the global scene there will be a bit of a lull, which we hope will be long enough to prevent our observations from being overtaken by major events in the immediate future.

This book is called *The Beer Monopoly* in acknowledgement of Germain Hansmaennel's theory of the Beer World Monopoly which argues that there are certain analogies between the well-known Monopoly

board game and the globalisation of the brewing industry. Whoever buys certain streets (i.e. gains market dominance in certain markets), and whoever builds hotels (i.e. brands) has the best chance of erecting an empire which spans the globe.

Being an expert Monopoly player, he confidently predicted in 2006 that the globalisation of the brewing industry had reached the semi-finals and that we would next witness several mega-mergers. Two leading trans-continental groups — InBev (the precursor of AB-InBev) and SABMiller — would be fighting over the lead position. As he said: 'US brewer Anheuser-Busch, as well as the European brewers Heineken, Carlsberg and Scottish & Newcastle, are lagging behind by a large margin because they have stuck to their original markets. I am sure that SABMiller will be a finalist because the South Africans have grasped the rules of the game sooner than their competitors. … The other finalist will be the brewer who takes over Anheuser-Busch – InBev or Heineken. Without a large-scale takeover, no single brewer can obtain critical mass in the beer business worldwide which is in excess of 20 percent of the global market share. … On the other hand, there is also the possibility that the CEOs of SABMiller and InBev will agree to merge their companies. In this case there will be no final match but a friendly game of InBev/SABMiller against the rest of the world.'[1] His prognosis proved astute. In 2008 InBev bought the US brewer Anheuser-Busch and set its eyes on acquiring SABMiller.

By calling our book *The Beer Monopoly* we advance the argument that it was through dealmaking and by following

the roadmap outlined in Mr Hansmaennel's model that several groups became global players. As these costly acquisitions needed outside financing, the globalisation of the brewing industry fundamentally revolved around money. After each deal brewers had to deliver, meaning they had to produce consistent, dramatic upsurges in profitability.

Of course, there were rival models, such as the often-extolled tactic that brewers need to buy into politically stable markets with low per-capita beer consumption, a youthful population, growing GDP and few competitors, and they would reap the benefits of rising beer consumption.[2] But, in our opinion, this only applies to emerging markets and cannot explain why brewers in mature markets with flat or even declining beer consumption became takeover targets too.

While Mr Hansmaennel's strategy model lies at the heart of our analyses, it was only a means to an end: empire building. Our slogan, 'buy and build', captures the essence of globalisation. It proved a quicker and more profitable route to empires than the old strategy of 'build and brew' (also known as the Heineken Model), which characterised the previous era of internationalisation, and which in turn had superseded beer exports. The term 'build' appears in both, but its meaning has changed. When going 'international' brewers literally built a brewery and started selling locally produced beer. When going 'global' their goal was to build empires, with one takeover being the precondition for the next. It was SABMiller's late CEO Graham Mackay who pointed out that transactions

needed to create 'more value' than merely demonstrating 1+1=2. Our formula for dealmaking, 1+1=3, reflects this principle. Sizeable profit growth was the main trajectory as the whole 'buy and build' process followed a deeper rationale, whereby successful deals would help fund the next transaction. It was through taking on and paying down debt that brewers turned themselves into global groups and reliable debtors, thus making their investors very happy indeed.

The rapid globalisation of the brewing industry from the 1990s onwards benefitted from two external factors: politics and finance capital. It was the liberalisation of markets and a world awash with money that helped kick-start the takeover frenzy. What helped too was an industry-specific feature: precisely demarcated territories. Unlike other industries, for example soft drinks and spirits, which revolve around brands, the brewing industry tended to deal in national markets, each with their own players, dominant brands and beer styles, which were the manifestations of their respective beer cultures. This particular feature played into the hands of acquisitive brewers. If they bought the leading brewer in a country, they controlled that market.

Our analyses of the top four global brewers are preceded by a chapter which looks in some detail at dealmaking in the brewing industry since the early 1990s. As there are, and have been, many players in Beer Monopoly, we have included a useful reference list of them at the back of the book. In this chapter we will explain the principles of Mr Hansmaennel's empirical model in contrast with the

Monopoly board game. The differences are significant, most evidently when it comes to winning. The board game only has one winner, whereas the Beer Monopoly has several – meaning several empires. There were also different ways to play Beer Monopoly successfully. You could play it to become number two worldwide or to realise a lucrative sale. You could even play it so that you stalled a rival.

Globalisation began in earnest when brewers did trans-continental deals. The first such deal was Belgium's brewer Interbrew buying the Canadian brewer Labatt in 1995. This transaction marks the game-changer, although export-driven strategies persist to this day.

In the end, though, dealmaking proved a faster path to profit growth than any hike in beer sales could have accomplished. In 1990, US brewer Anheuser-Busch was the world's major brewer, although focused on its home turf, with an output of 108 million hl beer and a profit of $2.1 billion. In 2015, AB-InBev's volume was almost four times larger (410 million hl beer), yet its profit eight times bigger ($16.8 billion), which goes to show that raw size (Anheuser-Busch in the 1990s) is not the same as global clout … or longevity, for that matter.

For investors the growth in the financial numbers alone has been enough to give brewers the thumbs up. By following the beer drinkers and buying into profitable markets, both mature and emerging, brewers managed to grow their bottom lines and succeeded in driving up their share prices. This is reflected in their market capitalisations – the total dollar market value of all of a company's outstanding shares. In 1990 Anheuser-Busch's

market capitalisation was $14.4 billion,[3] a modest figure compared with AB-InBev's $200 billion (September 2016). Increasing the share price was clearly of great interest to shareholders. But it was even more important to the brewers themselves. They became predators rather than prey and could afford to clinch deals that were often deemed excessively expensive.

When discussing the top four global brewers we will also examine how dealmaking affected their respective cultures and mindsets. AB-InBev's climb to the top was achieved through 'building positions in the most important beer profit pools in the world', as well as taking a 'disciplined approach to cost management and efficiency' thus 'giving it a strong track record of industry-leading margins and cash flow generation'.[4] Once it stopped being exclusively 'volume-driven' (growing beer sales, that is) and became 'finance-led' (a regime of accumulation dominated by financial valuations), in the words of analysts, AB-InBev revolutionised the industry's *raison d'être*. The most visible effect of this sea-change is the brewers' ranking. In the past companies and markets were ranked according to beer volumes produced. No longer. Because AB-InBev set new standards, the league table for investors nowadays measures companies' profits and countries' profit pools.

In the past century, brewers took great pride in the volumes of beer they produced, as if they rendered a public service by quenching customers' thirst. They strove to be profitable too, but this would have been a secondary consideration to their main objective: raising their beer sales and outperforming their rivals. As soon as they all

became stock market-listed companies and had to dance to the tune of investors, business objectives were turned upside down. It became dollars over hectolitres, especially since it was cash and debt that fuelled their chequebook strategies.

Despite its imminent disappearance, SABMiller is given its own chapter because the South Africans' strategy culminated in the most profitable exit in the history of the brewing industry. To secure a high price in the final sale, SABMiller proved a skilful dealmaker. Whereas most of its rivals strove to protect some sort of cultural hegemony (the Brazilians at AB-InBev, the Dutch at Heineken, the Danish at Carlsberg), SABMiller's top management mastered the fine art of keeping large shareholders with diverse cultures and targets in line. Not only did the flexibility that they displayed in this help stabilise the fragile ownership structure, it allowed them to shape and control their own destiny to the very end. Unlike SABMiller, the next-ranking Heineken and Carlsberg are well-protected from being taken over. Heineken has repeatedly stated its desire to remain independent. Among the world's leading brewers it sticks out not least because it is one of the few still in the hands of the founding family – an achievement that is an act of courage and ingenuity. Similarly, Carlsberg has a clear shareholder structure (it is owned by the Carlsberg Foundation) to defend itself from unwanted attention.

Although Heineken was the first brewer to seriously engage in beer exports, it came to globalisation late, probably due to its excessive prudence and risk aversion, characteristics often found in family companies with chequered histories.

Under the circumstances, Heineken has navigated globalisation well. While managing to maintain the family's control and culture, it rejigged its outlook, extracted itself from constricting partnerships and clinched a few formative deals. As a reward it will move up to number two slot in the global brewers' ranking once SABMiller is no more.

Like Heineken, the global number four brewer, Carlsberg, was a late participant in Beer Monopoly. The Danish only joined the club of the big brewers when they entered into a joint venture with Norway's Orkla in 2000. Drawn into the thriving eastern European beer markets, Carlsberg developed a mission to become the fastest-growing brewer worldwide. Yet the decline of the Russian and the Chinese markets has hit Carlsberg hard, both in terms of bottom-line and self-esteem. Controlled by its Foundation and shy to grow through partnerships, Carlsberg may have maintained its Danish corporate culture, yet business-wise it presently finds itself in an impasse.

If we focus on the top four brewers that's because our methodological approach to dealmaking has revealed that among the top four brewers only AB-InBev and SABMiller managed to play Beer Monopoly to its fullest potential. Given the restrictions imposed by their major shareholders Heineken was forced to embark on a catch-up course while Carlsberg had to combine incompatible globalisation strategies. All the brewers further down the ladder, like Japan's Asahi and Kirin, North America's Molson Coors and Turkey's Efes, have been bit-players, in our view, unwilling or unable to follow the rules of the Beer Monopoly.

In going through this book readers cannot fail to notice that certain seminal transactions crop up in several chapters. This is deliberate. Individual motivations varied to such an extent that we felt it necessary to look at them from a number of different perspectives.

To make this book more accessible, we have refrained from using a lot of financial jargon. However, there are a few business metrics that general readers will need to familiarise themselves with, such as profits, profit pool, market share and volumes.

Focusing on cash elements is a response to businesses being finance-led these days. 'Cash flow and profits are brewers' new bedfellows', is something that even Scottish punk brewers BrewDog are keen to stress.[5] Brewers' yardsticks are total EBITDA and profit margins. We use profits either synonymously with EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortisation), or EBIT (Earnings Before Interest and Taxes), which are the internationally accepted standardised means for comparing companies' earnings. Another important and closely related measure is the size of the beer profit pool. Usually given in EBIT, it is an estimate of the total profits earned by all brewers in one market. Not included in the profit pool are the distributors' and the on-trade's profits. For the reason that brewers' market shares based on profits are hard to guess, we use market shares by volume – the percentage share a player holds of total beer volumes sold — instead. Nevertheless, since beer is profit coupled with volume – in 2000, incidentally, it was still 'beer is volume with profit' according to an annual report

by Miller Brewing Company — we will give hectolitres (1 hectolitre – hl – is 100 litres) where necessary.

Although we have conscientiously followed the money, this book is not primarily aimed at investors. Our journalistic approach to evaluating brewers' aptitude at playing Beer Monopoly forced us to look backwards because only by assessing their earlier manoeuvres and taking into account formative events in companies' histories will corporate behaviour begin to make sense. Investors, on the other hand, are only interested in the future, more precisely in financial models that will help them predict brewers' prospective growth, profits and share price developments.

Since this is not a book about beer, perhaps we should come clean at this point and state that this is not a book about craft brewing either. The explanation for this omission is straightforward. Craft brewers have not played a role in the Beer Monopoly yet. The stress is on 'yet'. That's why we devote the final part of our book to craft brewers, consumers and politics since they are the three major disrupters in the game and a serious threat to the big brewers.

We readily admit that the Monopoly game can only go so far in explaining the reckless dealmaking in the brewing industry. The board game is finished as soon as there is a clear winner who has driven all his rivals into bankruptcy, while the Beer Monopoly is far more complex since it takes market realities into account. As such it does not allow for closure or a single winner. Our market economies are based on competition, which necessitates at least two players. Undoubtedly, dealmaking will continue, even if

only to help the big brewers pay down debts from past acquisitions. It's equally beyond doubt that dealmaking can continue when Mr Hansmaennel's roadmap has run its course and there is nothing meaningful left to buy in beer. It is in recognition of this difference that our book does not have a Conclusion. Rather, we have included our round-table discussion, which covers a range of issues, not least our musings on what the next round of empire building might look like.

# BEER GOES GLOBAL, OR THE NEW RULES OF ATTRACTION

“We will be the world’s beer company”, August Busch III, the President of Anheuser-Busch, predicted in 1996. Twelve years later, Anheuser-Busch was no more. The King of Beer got taken over by a Brazilian-Belgian go-getter called InBev, which had only been formed four years previously. Was Mr Busch’s ill-judged prophecy a case of ‘pride goes before a fall’? Or had he not seen the writing on the wall, which spelt ‘do lunch or be lunch’? August III was an extremely competent corporate chieftain, which his son and successor August IV was not. Both Buschs proved blinkered. While they kept gazing at the US from their executive suites in St Louis, the world of beer was changing beyond recognition. Those who took part in globalisation and its flurry of mergers and acquisitions survived. Those who only reluctantly did so – like Anheuser-Busch – ended up as prey.

Globalisation – in words and deeds – has been with us for so long that few can remember when it all started in the brewing industry. Was it in the late-1970s, when several western brewers entered China through joint ventures that eventually proved doomed? Or was it in the 1980s when two swashbuckling Australian brewers dreamt up the madcap plan to conquer the world by acquiring breweries in Canada, the US and the UK? Or did it only begin in earnest in 1991 when a few determined Finns and Swedes crossed the Baltic Sea to Estonia to take over a state-owned brewery, Saku, that had been advertised as up for privatisation? Could they perhaps have been beaten to the title of first mover by an Australian of the name of Tony Oates who arrived in the Polish port of Gdansk in

1990 to buy some run-down breweries, and whose new beer label, EB, would become the most popular brand in Poland within a few years? Or would that title have to go to Belgium's Interbrew, which in 1995 purchased the Canadian brewer Labatt?

Before memories fade, it is time to lean back in the chair, stare into the embers, and tell the story. And what a story it is. The plot is thick with brash Yankees, boisterous Aussies, soft-spoken Scandinavians, laddish Icelanders, hardboiled Brazilians, pussyfooting Mexicans, no-fuss South Africans, fun-seeking Belgians, dithering Dutch, plus a few clueless Germans and Brits in supporting roles who quickly shunted themselves to the sidelines. All of them had a go at mergers and acquisitions because they came to realise this was the best way to create more value for their companies. As in all good stories, there have been winners and losers, there were chancers and also-rans. And there was what the military calls collateral damage – secondary casualties, but casualties nonetheless.

Of course, all industries that went global in the past two decades have had their fair share of blunders and rookie mistakes, usually made by people who were over-confident but under-informed, not least about cultural differences, thus miscalculating the time horizon needed and the risks involved. But few other industries had such infamous yet colourful characters who hammed it up centre stage with the limelight fully on them. Admittedly, none were a match for August Busch III, the Machiavellian operator who coldbloodedly ousted his father Gussie in a 1975 boardroom putsch and stabbed his own son

in the back during the InBev takeover.[1] But in terms of serviceable yet likeable villains, the asset-stripper and convicted fraudster Alan Bond – who became the world's fifth-ranking brewer in 1987 – would be a close second.

If this were a novel, any good editor would send the manuscript back to the author with the comment: 'Overdone, overworked, too many protagonists for the reader to keep track of. Needs major revisions.' But this is not a piece of fiction. It is how the brewing industry came to look the way it does today. In 1990, the top four brewing companies controlled only 25 percent of global beer production. This may seem a lot, until you take into account the fact that three of the four brewers – Anheuser-Busch, Miller and Kirin – sold their beers mostly in their respective domestic markets. But after several gobsmacking transactions between 2000 and 2014, the top four's share had risen to nearly 50 percent.

## Doing it the slow way

Even before globalisation became a buzzword, brewers had embarked on a course of internationalising their sales through direct exports. Brewers' early internationalisation stories share several commonalities: location (often near a port) and destination (their countries' historic colonies). Take Bass Ale. By 1870, Bass was the largest brewery in the world, with an annual output of over one million hl beer. Its pale ale, known for its distinctive red triangle on the label, was exported throughout the British Empire. By the 1880s Dutch Amstel, brewed in Amsterdam, was exported to Great Britain and the Dutch East Indies. Early on, these brands competed with the German beer

brands Beck's from Bremen and Löwenbräu from Munich. As Germany came to colonies late, her beers drew their international clout and reputation from German brewers' advanced technologies and allowed them to catch up on the lead the other countries had.

So when did internationalisation kick off in earnest? It began with Heineken in 1931 when, together with Fraser & Neave (F&N) of Singapore, a sparkling water company, they set up Malayan Breweries, later to be called Asia Pacific Breweries. Eighty-one years down the road, in 2012, Heineken bought back F&N's stake for $4.6 billion, or at a phenomenally expensive 17 times profits. Back in the 1930s, going it alone was not an issue for Heineken. Sharing the spoils with a local associate proved a profitable undertaking. In the 1930s the Dutch acquired the interests in existing breweries in Egypt, Morocco, the former Dutch East Indies, French Indochina, the Belgian Congo and Palestine. In effect, these deals mark the beginning of Heineken's worldwide expansion.

It was in the 1950s and 1960s that Heineken changed its strategy to 'build and brew' and a series of breweries sprung up in Africa. Changing tack was born out of necessity. Once African countries had gained their independence, they often introduced protectionist taxes, which made imported beers too expensive for the locals. Heineken's only way of response was to enter these markets directly by establishing local breweries. Otherwise they would have lost these markets altogether. Nevertheless, this whole evolutionary process – from exports to build and brew – proved to be a time-consuming strategy, often

taking decades to implement. But it came to be known as the Heineken model, and other brewers too adopted this *modus operandi* when seeking to tap into distant markets. Except for Heineken, though, most brewers in the 20th century would have considered beer exports merely pocket money, not their main focus. All the while punters back home were downing their beer in huge quantities, they had better things to do – counting their profits.

We are so used now to hearing Europe's brewers moan about diminishing returns because of supermarket price wars and declining consumption, it is easy to forget that there were times, not so long ago, when brewing was a licence to print money. As recently as the 1970s, a German brewer's business plan was such that all the profits they made from selling mineral water were enough to cover brewing costs. The way they saw it, revenues in brewing equalled profits. Earnings rose even higher when brewers discovered that consumers were willing to pay more for a beer purely on the basis of branding. That is when they began advertising their products as premium beers and turned them into national brands with the help of television advertising. Hence the derogatory term 'TV beers' for large national beer brands. Anheuser-Busch clearly excelled at this because, by branding Budweiser as a premium beer and lifting its price, they increased their market share from 6 percent in 1950 to over 45 percent in 1990 without having to buy a single domestic rival.

Leading Brewing Groups – 1987 (millions of hectolitres)

| 1 | Anheuser-Busch | US | 90.1 |
|---|---|---|---|
| 2 | Miller Brewing | US | 47.2 |
| 3 | Heineken | Netherlands | 43.0 |
| 4 | Kirin Group | Japan | 30.4 |
| 5 | Bond Brewing | Australia | 29.9 |
| 6 | Stroh | US | 25.8 |
| 7 | Elders (Forster's) | Australia | 21.1 |
| 8 | BSN (Kronenburg) | France | 18.9 |
| 9 | Coors | US | 19.2 |
| 10 | Brahma | Brazil | 18.0 |

*Source: Impact Databank*

In 1987 the world's major brewers sold an impressive amount of beer but, except for Heineken and Foster's, this would have only quenched local thirsts. That is because they still had it very easy. In those days, brewers were considered the pillars of their societies. In the English-speaking countries there was even a word for them: 'beerage', a pun on peerage, or 'brewing royalty'. Whether they were called Santo Domingo (Colombia), Fernandez (Mexico), Busch, Coors, Molson, Guinness or Heineken, all believed themselves to be special, a cut above the rest.

However, Britain has always had an ambivalent attitude towards its beerage; a commentator for the *Spectator* magazine wrote in 2008 that this 'cosseted bunch of arrogant monopolists' used their enormous wealth to 'grease the political system, bankrolling the Conservatives who duly obliged by preserving the industry's traditional privileges – including ownership of vast pub estates that