AFTER THE TAKEOVER

Text of paper delivered to the Australian Society of Security Analysts at the Hotel Metropole, Sydney, on July 3, 1968, by Mr. Jonathan van der Borgh, Chairman of Slater, Walker Securities (Australia) Ltd.

I would like to tell you of some of the criteria we use in the Slater, Walker Securities group in reorganising our acquisitions and placing them on what we consider is the most desirable profit-earning and growth basis. I will also give you a description of how we went about our first acquisition in Australia, the Thomas Brown and Sons group.

First, I should point out that we make as thorough a pre-acquisition investigation as is possible in each particular circumstance and from this we get a fairly good idea of what we want to do. Immediately we take control, we reconstitute the board, make accounting arrangements and other formalities, and then begin a detailed investigation of every facet of the business.

This investigation—of turnover, capital employed and contribution to profits of each main division or product — isolates the problem areas, those not producing satisfactory returns or those making losses. Unless there is scope for significant short-term improvements, we cut our losses and eliminate the problem areas, either by sale as a going concern or by liquidation.

Then we concentrate on lowering the break-even point, studying all facets of expenditure with the emphasis on maximum and short-term improvements. Enormous scope for economies is usually found in buying and overheads. As you know, it is almost invariably easier to stop spending rather than increase your income.

Of course, it is not as easy as it sounds. Substantial reorganisation may be necessary to reach our objectives. Whole factories may need to be changed around to solve production and capacity problems —or various activities may need to be re-grouped. Products may need to be re-designed. The size of the job does not worry us—what we are aiming at is a new, improved situation.

Having established the new situation firmly, we start looking for more business, concentrating on marketing, sales and pricing policies to maximise turnover.

Our central management team is flexible and considerable use is made of outside consultants to underpin our trouble-shooting capacity. However, operational management following reorganisation is decentralised and made autonomous and fully responsible.

The central management team then has to be concerned with accounting—we have a rather simple but effective form of budgetary control—and overall policy, plans and problems.

"Quickest returns soonest" is the general theme. Naturally, it involves change, which is sometimes upsetting but more often is exciting and stimulating. The great satisfaction is watching profitability rise. And ultimately, I'm sure you will agree, that's what the whole business is all about.

Now, let me tell you about the Thomas Brown acquisition.

A member of Slater, Walker Securities Limited in England first spotted Thomas Brown & Sons Limited as an investment opportunity in May, 1966. The share prices at that time were $2.80 for the ordinaries and $1.70 for the preference shares. (The preference shares carried full voting rights.) This put a market capitalisation of $2.6 million on the Company and net tangible assets were $6.1 million.

About 65 per cent. of the shares were held in England, and 35 per cent. in Australia, and the shares were quoted in London and Brisbane.

Net profits after tax and minority interests for the previous three years had fallen as follows: $221,342; $199,852; $83,425. It was decided in London to send a man to Australia to investigate and he visited all the locations where Brown operated and compiled a report recommending that a take-over offer be made.

The report showed that the wholesaling side of Thomas Brown was barely profitable, but that the subsidiaries were profitable. The essence of the exercise was to sell off the wholesaling business to fund the whole of the purchase price, leaving four profitable subsidiaries standing in at no cost.

Slater, Walker began to buy shares on the market and by August, 1966, had purchased 30 per cent. of the ordinaries and 31 per cent. of the preferences. On 20th August they made an offer for the whole of both classes of shares worth $3.06 for each ordinary share and $2.50 for each preference share, which placed a market capitalisation of $3 million on the company. After negotiation with the Board of Thomas Brown, Slater, Walker increased the bid for the ordinaries to $3.51 which capitalised the company at $3.39 million, at which figure they received 100 per cent. acceptance.

What did we find and what did we do when we gained control of Thomas Brown?

We first of all had draft accounts prepared by the auditors. We also had divisional and subsidiary figures prepared.

These showed the following position:—

		Gross Capital Employed		Net Profit before tax and interest for previous period
Wholesaling activities (Darwin, Rockhampton, Townsville, Brisbane as main centres with smaller branches at Cairns, Mackay and Gold Coast)		$6.9 million	1.7%	$119,697
Brisbane Group Companies (Manahans, Holsums, Tunleys, Caledonian House and distillery)		$1.2 million	22%	$257,121
		$8.1 million	**4.7%**	**$376,818**
Gross (as above)		$8.1 million		$376,818
Less—Net overdraft	$600,000			
—Unsecured loan stock	$940,000			
—Short term loans	$460,000	$2.0 million	Less interest and tax	$293,393
Net Tangible Assets		**$6.1 million**	**Net profit**	**$ 83,425**

We had to make up our minds whether it was possible, or desirable, to try and revitalise the wholesale side of the company's activities so as to make it really profitable quickly. It was soon obvious that it would be very difficult and long-term to attempt this because there were too many wholesalers in Queensland and because manufacturers were selling more of their products direct to retailers rather than through the intermediary of a wholesale merchant.

On the other hand, it would be relatively easy to sell off the assets and businesses of the wholesale side to other merchants because this would benefit them by strengthening their trade through increased turnover. We had already established this **before** the acquisition and had in mind potential purchasers were it to become necessary.

We therefore decided to put into immediate operation the prime philosophy of the Slater, Walker Group—that is, get rid of loss-makers and promote the profit-makers just as one would treat an investment portfolio.

So we sold off the wholesaling branches on favourable terms to Eyles Co-op. (Darwin), Burns Philp (Townsville), Denham Bros. (Rockhampton) and Foodstuffs-Q.C.T. (Brisbane). We liquidated the branches at Cairns, Mackay and Gold Coast and sold off the shirt-making business of Caledonian House.

We succeeded in selling all the assets of the wholesaling side by making the deals attractive to would-be purchasers. We gave credit terms to those who needed them and rented the premises of certain branches to the companies who took over the businesses but who could not buy the properties from us.

In one case we sold a warehouse forward eighteen months for over $1 million.

One of our prime concerns was the fate of the previous employees of Thomas Brown's wholesale division and branches who numbered about 700.

In the majority of cases the companies who bought the businesses took on most of the staff. In Rockhampton, however, we were faced with a possible redundancy of 65 people out of a complement of 90. So we got the former manager of the Rockhampton branch to spend a fortnight placing all the people in good positions. To those for whom we were unable to find jobs we gave generous compensation.

As far as we can find out, only eleven out of 700 were initially made completely redundant by our decision, and those people found satisfactory positions within a few weeks.

Now we come back to our draft Balance Sheet. After we took our decision to get out of wholesaling and shirt-making, we made conservative calculations of the probable losses and profits which would result from the disposal of the assets of these businesses. We provided for all such contingencies in the draft accounts, and the resultant position was a total of net tangible assets of $5 million.

What did we do with the four companies? Well, first we investigated them very carefully and then took the following action:—

A. Tunleys manufactured hessian sacks for primary industries (including fertilisers, sugar, peanuts and meat). Its management was good and its return on capital was high enough to leave well alone and to concentrate on those companies which needed help.

B. Beenleigh Rum Distillery was part of the wines and spirits division of Thomas Brown. As a result, it had merely been treated as a captive supply of rum, and manufacture had really been controlled on an indent system.
The price to merchants and breweries (other than the wines and spirits division of Thomas Brown) was higher than all other rum distillers in Australia, and thus uncompetitive. It had no marketing or

promotion activity to speak of. We therefore turned the distillery into a separate company which acquired the assets from Thomas Brown. We revised the price list to be in line with competitors and took on a marketing manager.

The two main products of the distillery were Beenleigh dark rum and a more mature and paler product called Amity. There was no colourless product to compete with Bacardi. It has taken 18 months to perfect such a product and to prepare a market campaign for our new colourless drink called Dryandra, and this new white hope came on to the market two days ago.

C. Holsum Products made essences for the food industry and also ground and packaged pepper and spices. It packed mixed fruit and bottled vinegar and concentrates.

The first thing we discovered was that although capital employed was divided equally between Brisbane and Sydney, the net return in Sydney was 4 per cent. against 16 per cent. in Brisbane. We closed the Sydney branch and concentrated on Brisbane.

A product analysis showed that some lines were quite unprofitable, although others made good margins. We abandoned all lines whose gross margin was below a certain level.

Finally we sold the rather unwieldy and sprawling old premises in Brisbane to our neighbours, and rented a more modern and suitable place nearby.

D. H. A. Manahan and Sons was a chain of 31 self-service grocery stores. Twenty of these were in country districts and 11 were in the city of Brisbane. Country stores made a profit, city stores made a loss, due to competition from the big chain stores. We decided to close the unprofitable city stores and concentrate on building up more effective coverage in the profitable country districts.

The company acted as its own wholesaler and warehouseman for about fifty per cent. of the various branches' purchases. This was unprofitable and time-consuming and management was probably spending more time on wholesaling than on retailing. We therefore closed the wholesaling activity and got a professional wholesaler to act as our supplier. This released a further \$¼ million of capital employed.

Finally we set out on a policy of standardising our country stores and administering them so that their marketing policies were similar and their layouts the same, wherever physically possible. We have closed two country stores whose gross margins were irredeemably low, and we have so far opened seven new stores, and four more are planned for this year.

We are now concentrating on increasing the number of times a year we turn over our stock at each store.

What did we do with all the cash in Thomas Brown? In December, 1966, we bought 44.6 per cent. of Wancol Holdings Limited. But that is another story.

At this stage, someone might ask "Well, how does the central management maintain secure control over widely varying activities at the same time as following a policy of growth through investment-based acquisition as distinct from industry-based mergers?"

After all, as you probably saw in the Press last week, Slater, Walker (Australia) has now added the Thomas Brown companies I have been talking about to a range of activities which includes coal mining and plastic and rubber rainwear.

The key to control lies first in holding the purse-strings, then in demanding high performance from operational managements, and finally requiring regular evidence of performance. Just to give you an idea of the control, I shall outline the pro-forma agenda for the monthly subsidiary board meetings, which I, as chairman of each company, attend.

First, of course, the minutes of the previous meeting are read, discussed where necessary and approved.

Then comes Finance. We study the trading results for the period, for the year so far, then compare the figures against budget and the previous corresponding periods. We examine the cash position and future cash budget and consider any capital expenditure proposals.

Under the general heading of Sales, we consider: orders received for the period, the progressive figures for the year, and the outstanding orders position; orders lost and the reasons; inquiries received and the major prospects; sales and advertising programmes; and any major problems affecting sales.

Under Production, we have: volume for the period and progressive for the year, compared with budget and the previous corresponding periods; departmental capacity, comparison of future production commitments per the order book, with capacity available; stocks and work in progress; variations in production costs; changes in the employment situation and the reasons; improved methods; and major problems affecting production.

At this stage, we look at Technical matters such as: problems connected with current products; any new product developments; product cost reduction.

(Continued on Page 12)

SYDNEY MEMBERS *(Continued)*

M. J. NIEL
R. A. MacG. NOSS

M. J. O'NEILL
P. C. OSBORNE

D. R. PARR
R. H. PEET
P. S. M. PHILIPS
K. C. PHILLIPS
F. C. PIKE
G. E. PIRANI
C. A. POTTS
R. O. POWYS

O. RAHN
R. B. RAINES
A. J. REYNOLDS
J. REYNOLDS
A. S. RICKETSON
F. A. ROBERTSON
G. L. ROBINSON
J. K. ROE
G. W. F. ROSS
J. D. C. ROSS
DR. N. RUNCIE
B. RUTTER

G. SECK
B. A. D. SELLERS
W. J. SHELDON
K. F. SHIELS
R. H. SIMON
A. J. SMITH
L. A. SMITH
M. J. SOLOMON
K. W. STEEL
H. J. SUSSMAN
J. P. SWEENEY
R. E. SWIFT

A. R. TAYLOR
P. D. THOMAS
E. J. THOMPSON
R. M. THRELFALL
H. B. TODHUNTER
N. J. TRAYNOR
J. M. TROY
C. S. S. TURNBULL

A. H. URQUHART
A. G. UTHER

H. P. VAINS
J. H. VALDER
C. J. VAN HEYST
J. V. VALE
D. D. VAUGHAN
J. B. VERCOE
O. VIVANTI

G. P. WALKER
M. H. D. WARREN
K. WEDELL
I. S. WEISS
B. WHITTLE
B. W. WIESENER
F. W. WILLIAMSON
J. S. WILLS
E. W. WILLSON
P. C. WOLFE
J. D. WOLFENSOHN
P. R. W. WOOD

R. YEE

TAKEOVERS *(From page 9)*

Final regular business is Buying and we consider: any price increases; price reductions achieved; and future action on price reductions.

The meeting closes after discussion of Any Other Business.

You can therefore see there is not much room for things to get out of hand inside the month. And if anything does go wrong, we, that is, the central management, can move swiftly to correct the matter, if the operational management has not already taken it in hand autonomously.

The point to remember is that the central management is a team of trouble-shooters, vigilantes if you like. We are trained to identify problems, then eradicate them, with the ultimate aim, as I said earlier, of increasing profits.

BROKERAGE *(From page 10)*

are less. The two systems may be compared as follows:—

specified companies but have merely quoted representative share prices.

	U.K.	Australia
Basic Rate	$1\frac{1}{4}$%	2%
Consideration \$10,000-\$50,000	$1\frac{1}{4}$% on 10,000 $\frac{5}{8}$% on balance	2% on 10,000 $1\frac{1}{2}$% on balance
Consideration over \$50,000	$\frac{5}{8}$% on whole	2% on 10,000 $1\frac{1}{2}$% on 10-50,000 1% on balance

The minimum provisions are similar.

The effect of the Australian system is that the purchaser of a large block of shares pays 1.6% on the first \$50,000 of consideration and 1% on the balance compared with 0.625% on the total in the U.K.

I have therefore taken the liberty of adapting Mr. Holst's table to compare brokerage in Australia, the U.S.A. and the U.K. I have not

For the purposes of the table I have assumed that \$A1 = \$U.S.A.1 = "\$U.K."1 = 10/- sterling and have ignored stamp duties.

In the U.K. there is another concession in that if the same broker deals for the same client on the buying and selling side in the same shares in the same Stock Exchange Account (normally two weeks) one commission only is payable.