OnLine Case 13.1
GEC – General Electric Corporation

The growth years of GEC are really the story of Arnold (Lord) Weinstock who was once described by fellow industrialist Lord Hanson as ‘the best manager Britain has produced’. Born in 1924, Weinstock died in 2002. Until his retirement in 1996 he was ‘the dominant figure in the British electrics and electronics industries’. Weinstock was recognised for his strong focus on cost control and his sustained ability to deliver on profitability and shareholder value. He was criticised by some for his caution and for avoiding risks by staying away from the fastest growing sectors of electronics. ‘He was good at generating cash but less good at spending it’. One might expect bankers and financiers to criticise businessmen who don’t borrow money but instead build up reserves – there is no profit for them in that! But the empire he built so carefully would crumble in the years after his retirement.

Weinstock first worked for the Admiralty and then as an estate agent before he joined his father-in-law’s business in 1954. Michael Sobell owned Radio and Allied, which manufactured radios and televisions. Weinstock soon took over the business and improved its profitability – before selling it to GEC in 1961, when he became a director of the new owner. By 1963 he was Managing Director of GEC. He established a small top team to run the company and set out to reduce bureaucracy. He also switched the focus from heavy industry to consumer products. In 1967, and with connivance from the Labour government of the time, GEC absorbed AEI. One year later GEC was a ‘white knight’ bidder for English Electric, which was being stalked by Plessey. English Electric had earlier acquired telecommunications business, Marconi. Between 1970 and 1977, and with rationalisation, profits increased fivefold.

In 1985 GEC bid for Plessey, but this time the Monopolies Commission stood in the way. Plessey was acquired though in 1988, when GEC put in a joint bid with Siemens of Germany. Around this time GEC also collaborated with Alsthom of France (in power engineering) and GE (the American General Electric) in domestic appliances. By 1990 GEC had also bought important parts of defence business, Ferranti. Some time later Weinstock considered bidding for British Aerospace (BAe) but didn’t. Instead he acquired Vickers Shipbuilding in 1995.

When he retired (1996) GEC was a diversified conglomerate in an era when focus was becoming strategically more acceptable. He favoured ‘eggs in several baskets’. Power engineering, telecommunications and domestic appliances accounted for 40% of the company, and they were all joint ventures. Defence electronics, semiconductors, shipbuilding, elevators and wire cables were other important activities. GEC was the UK’s second largest defence supplier (after BAe) with ‘a number of excellent businesses with stable cash flows’. Profts amounted to £1 billion a year from a turnover of £11 billion. There were 80,000 employees,

Weinstock controlled the empire from his London Head Office, rarely visiting the factories themselves. He relied on detailed financial reports and regular phone calls to his managers. He had a telephone switchboard on his desk to facilitate instant access. He set out to build and hold cash reserves – they amounted to £1.4 billion in 1996 - to help the company through business downturns and cyclical variations. The diversified portfolio meant his businesses were not all in recession at the same time. Outside work he was passionate about the opera and horseracing. A bloodstock owner, his horse won the Derby in 1979. He had ‘little enthusiasm for conventional business school strategy and even less for exploring synergies .. .. he allowed the businesses to operate with autonomy’.

Weinstock recruited a Scottish accountant to succeed him. George (Lord) Simpson has built his career in the car industry. He had spent several years at British Leyland/Rover before its acquisition by British Aerospace, which he joined and became Deputy CEO. In this role he engineered the sale of Rover to BMW. He then left to join Lucas, which, in turn, he sold to Varity of America.

Once installed at GEC Simpson recruited John Mayo as his Financial Director. Mayo had worked for S.G. Warburg (investment bankers) and Zeneca (pharmaceuticals) and was described as 'brilliant but utterly ruthless'. His view was that if any business produced below 7% cash flow returns on investment, after inflation and tax, it must cut costs. But if earnings exceeded 12% a business should grow as fast as possible, using the cash it was generating.

Simpson and Mayo concluded the existing management had 'got it all wrong'. They simply did not have a risk-taking approach to growth. They quickly abandoned the joint ventures, divesting most but buying out Siemens' share in telecommunications, and sold the defence businesses to BAe to build up an acquisitions war chest of £5 billion. The new focus was to be on high growth telecommunications and they looked for acquisitions in America, although, because of the dot.com bubble (which had yet to burst), prices were inflated. The two major buys were Beltec (a network and access specialist) for $2.1 billion and Fore Systems (Internet switching and networking) for $4.5 billion. In no time the company had debts of some £3 billion. But, as Simpson pointed out, 'cash in the bank earns a very low return'. One critic suggested that GEC was 'buying from the Americans businesses no other Americans wanted'.

In 1999 GEC opted to change its name to Marconi to reflect its new focus. The share price - £3.50 before the change of strategy – was on the rise, reflecting favourable investor reactions. By late 2000 the price had more than tripled to £11.50. But in 2001 telecom shares everywhere began to fall when investors concluded they had grown too rapidly.

Marconi declared poor results in May 2001 but Simpson and Mayo were promising renewed growth. The reality was the company was running out of cash. When a serious profits warning was issued in July, the share price had fallen back to £3.75. Chairman Sir Roger Hurn tried to persuade institutional investors to adjust the Directors' share option scheme to allow them to buy at lower prices and he continued to promise 'gold around the corner'. Was this credible when 4000 job cuts were announced? In the end over 10000 jobs would be lost in the UK in 2001. Shareholders were 'outraged at the duplicity' and the share price was soon down to £1. Mayo was forced to resign. To many he was the real culprit for bringing the company to its knees. Initially Arnold Weinstock (a leading shareholder and non-executive director) continued to back George Simpson, but by September both Simpson and Hurn were gone. In 2002 another 4000 jobs would be lost.

When Mike Parton took over as CEO – an internal promotion – debts had risen to £4.4 billion and the shares stood at 50 pence. There was an exceptional profit charge of £3.5 billion because of the fall in value of the US acquisitions. Future and planned capital expenditures were slashed. There would be further disposals and Marconi would focus on network communications.

There was then a major financial restructuring (in 2003) when thousands of shareholders lost out. By the summer of 2005 it was clear that Marconi was up for sale. Huawei (based in Shanghai) was exploring the prospect, but in the end the new owner would be the Swedish company Ericsson – which paid £1.2 billion for the bulk of the business. Ericsson was interested in the part of Marconi that made equipment for fixed-line telecommunications, to complement its own mobile telephony interests. The remaining activities – the provision ot telecommunications installation and maintenance services to customers such as BT - were renamed Telent. Mike Parton would run this business 'for the time being'.

Question: What do you think might have happened if Weinstock's strategy and style of management had been retained? Was he correct to avoid risky industries or is this inevitably a flawed strategy in the long run?