Big Tobacco: Strategy, Structure and Competition Policy in the Post-War British Cigarette Market

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1 Introduction

The 1956 Restrictive Trade Practices Act (RTPA) outlawed business cartels in Britain. The Act required the registration and termination of collusive agreements between firms, creating a new presumption that such practices operated against the 'public interest' unless they could be proven to meet certain exempting 'gateways' in a court trial (*Restrictive Trade Practices Act* 1956). Board of Trade (BoT) President Peter Thorneycroft introduced the Bill to Parliament as a, 'powerful reinforcement to the system of free and flexible competitive enterprise' (HC Deb 1956a). Almost half of manufacturing was subject to collusion before the RTPA, and by 1966 at least 2,100 agreements had been terminated as a direct result of the Act (Hannah 1983; Symeonidis 2002).

However, the RTPA was controversial in its day and its impact—particularly the nature of its contribution to structural trends of rising concentration and firm market power in this period (Aaronovitch and Sawyer 1975; Geroski and Jacquemin 1988; Hannah and Kay 1977; Meeks 1977; Prais 1976)—remains a matter of debate. Mercer (1995) shows that business lobbying heavily shaped the contents and structure of the Act, arguing that, as a result, it was largely defective. Symeonidis suggests the RTPA boosted productivity growth in "treated" industries, arguing its structural impact was an innocuous by-product of increased competition (2000, 2002, 2008).

This paper examines the RTPA's impact on firm strategy and market structure, hoping to disentangle its beneficial and detrimental elements. This is done through a narrative case study of the domestic cigarette market. The British tobacco industry was the single most concentrated industry in the economy, had long been characterised by lack of competition, and featured unchecked collusion enforced through an industry cartel, the Tobacco Trade Association (TTA), which had existed since the 1930s. In 1956, market leaders Imperial Tobacco and Gallaher commanded 76.1% and 18.6% of the share of total domestic sales (by value) respectively, with a handful of other large, historic manufacturers left to fight over scraps.

Public awareness of tobacco companies' history and inner workings was limited in the 1950s (Corina 1975). However, as the issue of cartels and monopolies became increasingly prominent, being linked to concerns around inflation (Dow 1970; Heald and Wybrow 1986), the activities of the TTA and the large cigarette manufacturers were regularly brought up during parliamentary debates (HC Deb 1956b, 1956c, 1956d, 1956e, 1956f). Tobacco became the first industry to disband its cartel, only a month after the RTPA received the Royal Assent in August 1956, and quickly transitioned to a state of free competition. Shortly afterwards, in November 1956, the Monopolies Commission (MC) also began an investigation into the industry.

Less than a year after the end of collusion, *The Economist* (1957) spoke of how, '[f]or the first time since the thirties competition has now become really intense in the tobacco industry,' and suggested that 'there is strong chance that the industry [may see] interesting shifts in fortunes for many companies.' In reality, these hopes were short-lived. Here it is shown how dominant firms were able to circumvent the increased competition brought on by the RTPA by exploiting weaknesses in legislative design and by outright refusing to comply with regulatory enforcement. A detailed examination of primary sources—including previously unexamined archival materials and newly digitised, product-level data on cigarette prices and advertising expenditures—outlines the post-RTPA developments in this market.

It may seem the precepts of competition policy are abused here—is it really desirable that cigarette companies be "efficient" and "competitive"? The point is that the tobacco industry is instructive for revealing what could happen in other sectors, where competition's link to welfare is easier understood. This single industry—prominent in the period (Singleton, 2023), and the main source of indirect tax revenue (TNA: T233/1127)—yields generalisable insights that are relevant to the literature on competition, market structure, and government policy in post-war Britain (Crafts 2012; Harris 2013), and to whoever seeks to exploit the RTPA for empirical industrial organization research (as in Broadberry and Crafts 2001).

2 Increased competition and its structural impact

Existing work asserts that price competition increased following the RTPA without any serious attempts to measure post-collusion pricing behaviour in affected industries (Symeonidis 2000, 2002). By ending the collective enforcement of resale price maintenance and national price lists, there were fewer impediments to price competition—but this does not mean it occurred. Consider that collusion tends to accompany an oligopolistic market structure, and that when these markets are competitive firms tend to focus on advertising and/or technical innovation rather than prices (Schumpeter 1947; Sutton 1991, 2001); not to speak of the possibility of tacit collusion in prices.

There was no increase in price competition between cigarette manufacturers following the RTPA. This can be shown using data from *The Smoker's Handbook* (Figure 1)—a contemporary trade journal with product-level prices for all domestic manufacturers (Bristol: 38169/Pr/7/5)—where we find no instances of manufacturers undercutting each other in the disaggregated data. This seems to be broadly representative: an internal policy review by the BoT, in 1961, found that there had been 'little effect on prices resulting from cancellation of agreements' and that 'price leaders have frequently taken over function of price regulation' (TNA: BT258/1203).

So what of the intense competition we are told was occurring in the industry? This was realised through a competitive escalation in advertising efforts. Using monthly product-level data on cigarette advertising expenditures, collected from the *Statistical Review of Press Advertising* (1932-62),[1] we can closely observe the impact of the RTPA. Applying a changepoint detection algorithm (Aminikhanghahi and Cook 2017) to press expenditures (Figure 2) suggests a significant shift in firm strategy post-RTPA.

Figures 3 and 4 aggregate this product-level series to the manufacturer level, showing raw monthly press advertising expenditure and shares of total industry expenditure respectively. Commercial television, funded through advertising, also emerges in Britain in the mid-1950s (Paulu 1961). The large cigarette manufacturers were typical early adopters: those in oligopolistic industries manufacturing low-cost consumer goods with a high purchase frequency (*Financial Times* 1956a). I also collect data on TV advertising expenditure from the *Review*; these are aggregated to the manufacturer level in Figures 5 and 6, again showing the raw series and industry shares.

The plots show large manufacturers consistently outspending smaller rivals on advertising. Additionally, not every pound spent was equally effective; the fact that larger firms were able to direct their advertising towards more effective (but costlier) mediums (TV) and had access to nascent commercial market research firms (Fitzgerald 1995; Tinkler 2001; O'Neill 2015), would have given them an additional

[1]For a discussion of this source, see Clayton (2010).

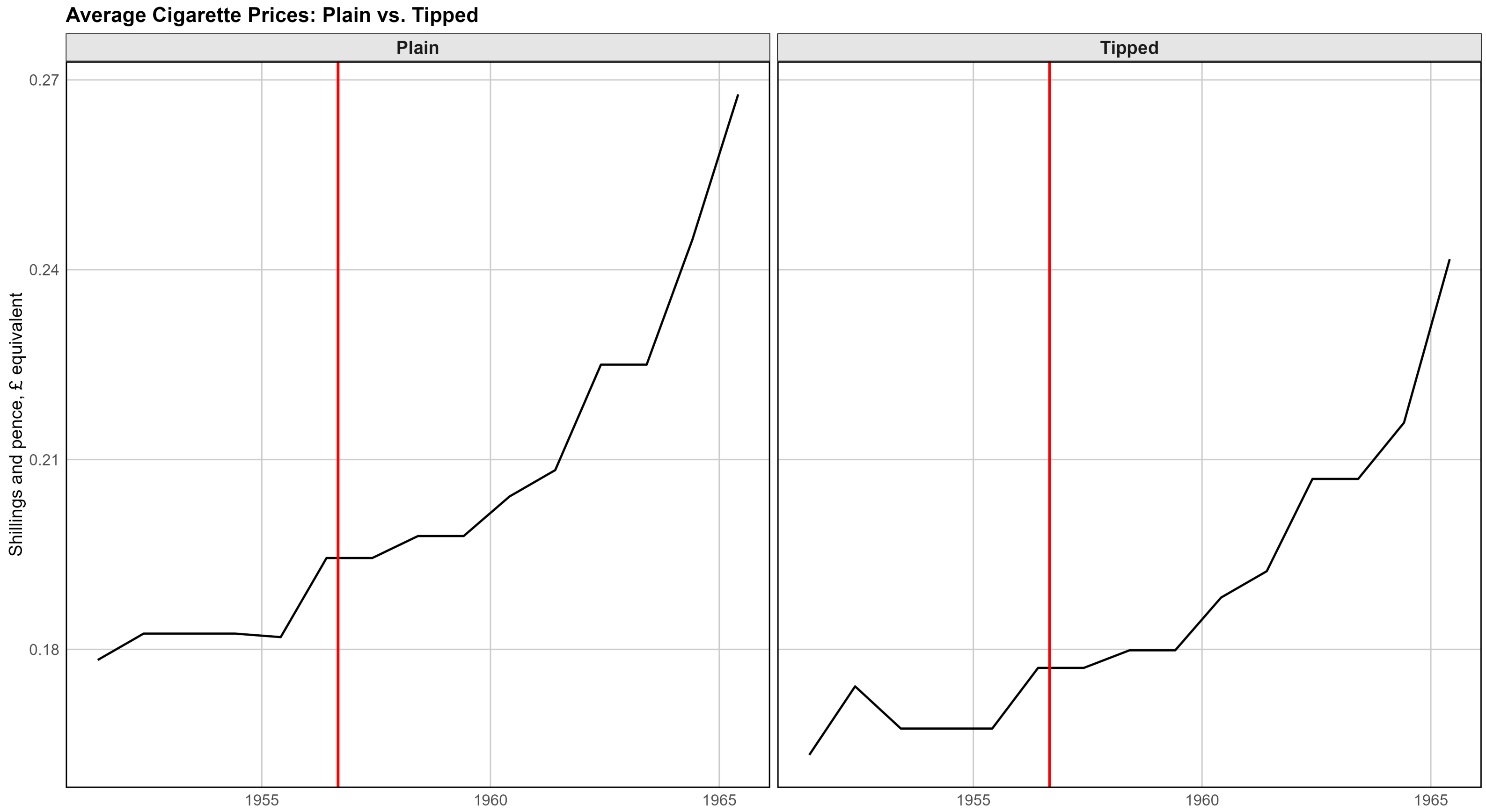
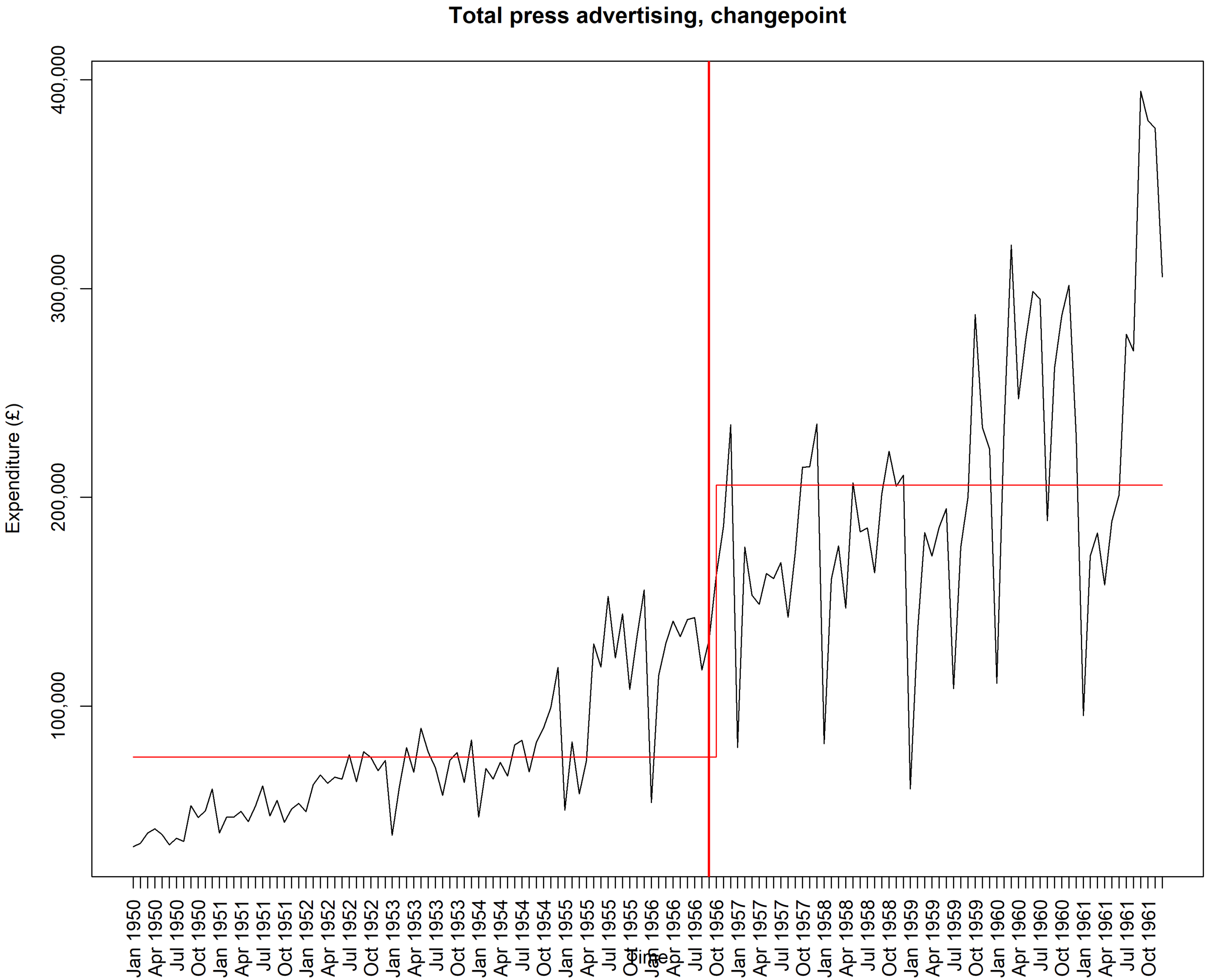


Figure 1: See text.
Note: In Figures 1-6, vertical line denotes end of TTA.



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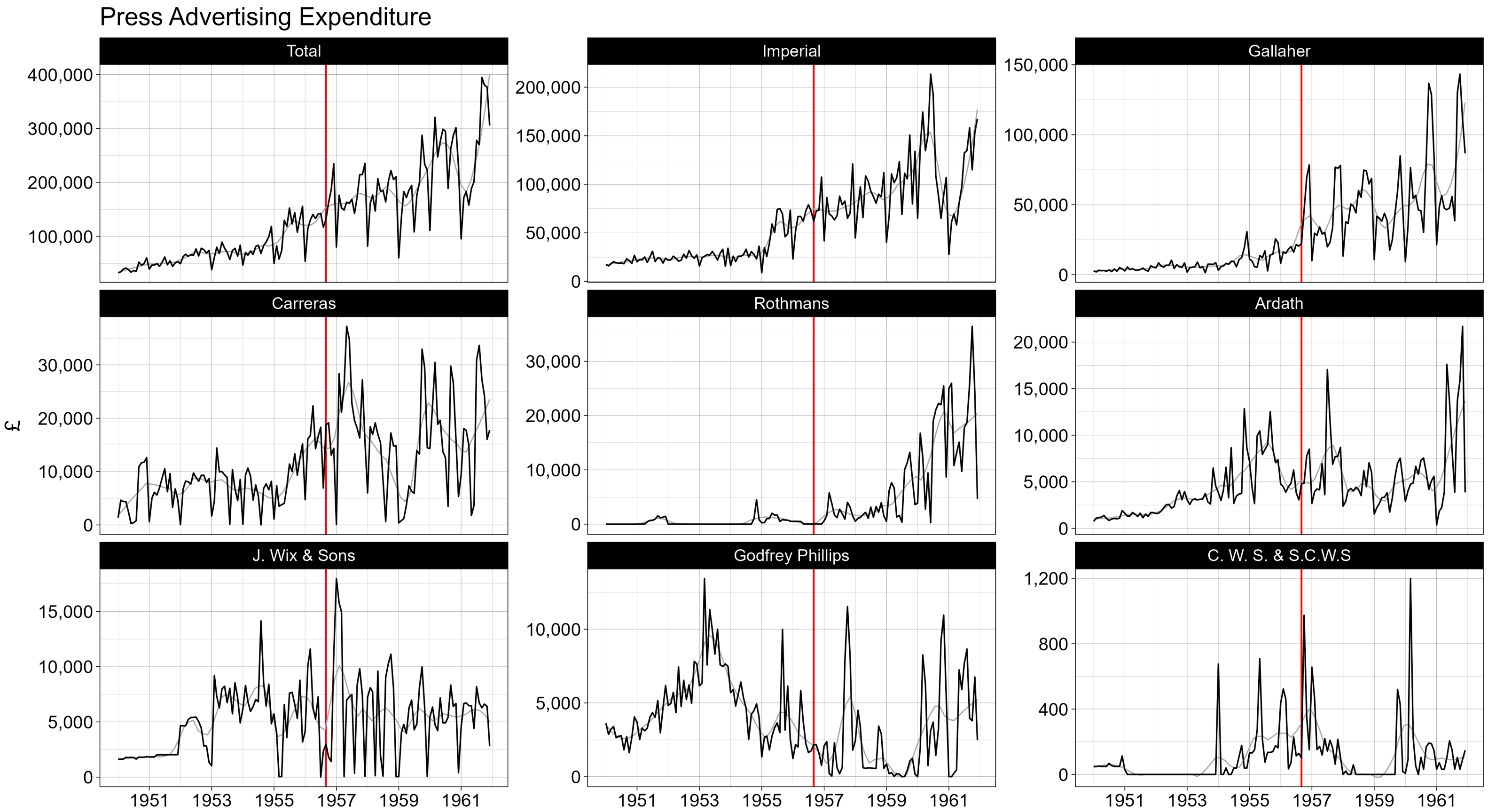
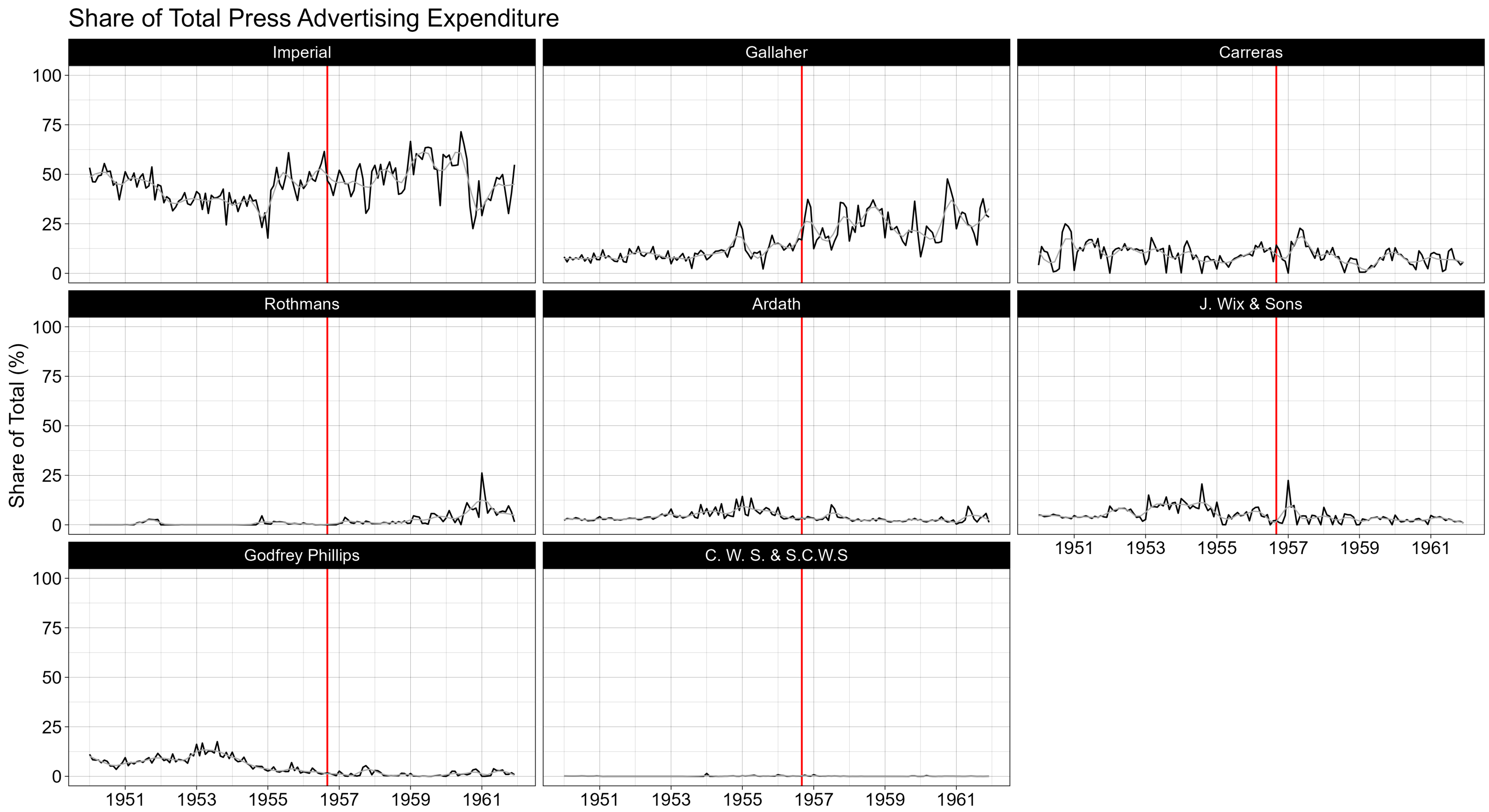


Figure 3: See text.
Note: Manufacturer-specific y-axes. In Figures 3-6, loess smoothing span = 0.1.



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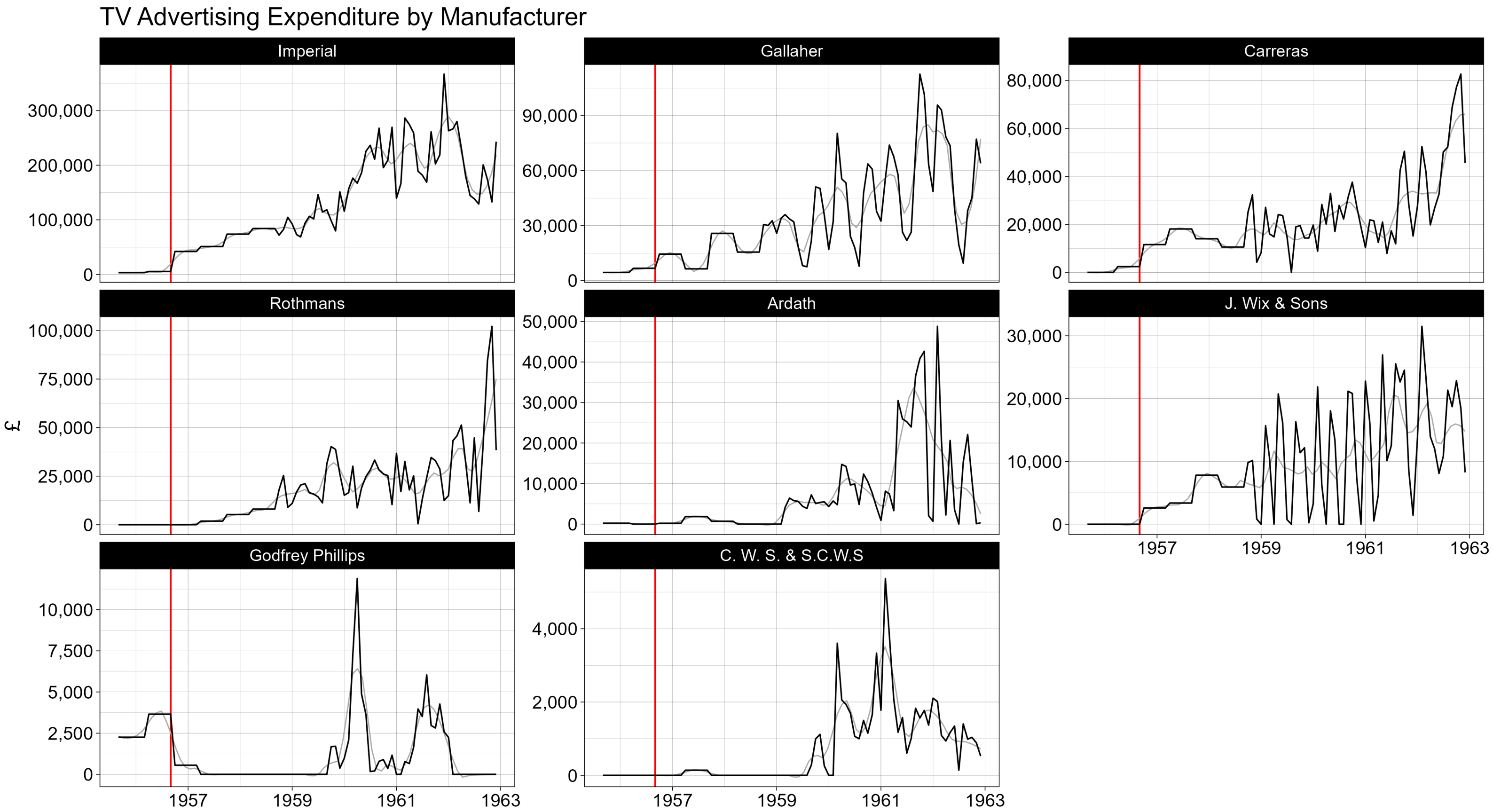

Figure 5: See text.
Note: Manufacturer-specific y-axes.

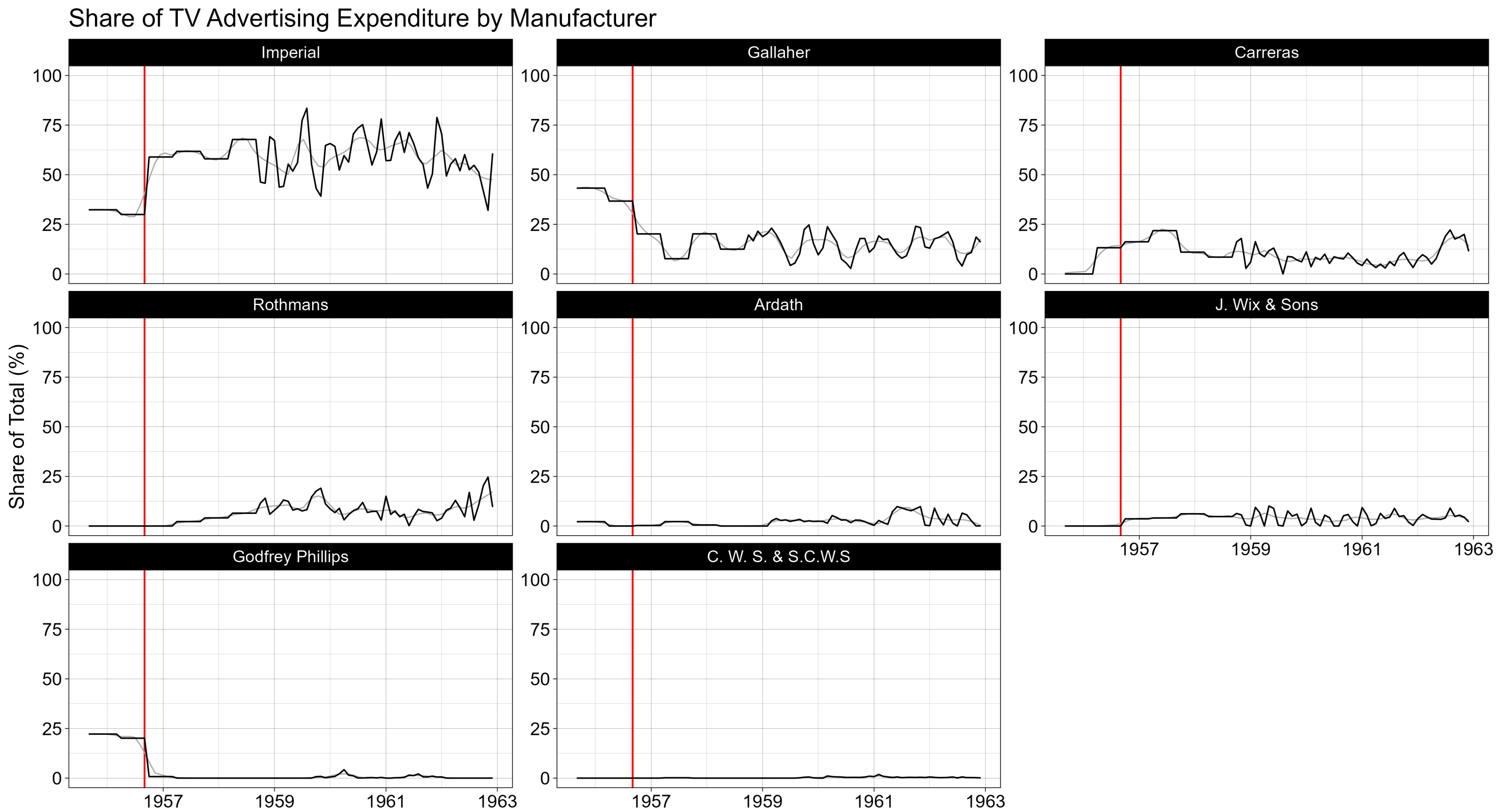

Figure 6: See text.

advantage. These facts, combined with a strong theoretical argument for the idea that an intensification in advertising competition increases the equilibrium level of concentration (Sutton 1991, 2001), suggest that this was one channel through which the RTPA exerted a structural influence in the cigarette market.

Indeed, there is direct evidence of this. Manufacturer Godfrey Phillips told the MC that by the early part of 1960 they were faced with having to exit the domestic market, citing an inability to keep pace with the need for increasing advertising expenditure (MC 1961). Imperial acquired control of Godfrey Phillips in 1960; a takeover which was later referenced in Parliament as an example of how a firm could be 'squeezed out' by the aggressive advertising efforts of its larger competitors (HC Deb 1964). Likewise, Carreras and Rothmans joined forces in 1959 to create the Carreras-Rothmans Marketing Division Ltd. (MC 1961). Rationalisation was also pursued amongst the subsidiary branches of Imperial; in 1957 its flagging Stephen Mitchell branch was subsumed into one of its flagships branches, Wills, whereafter it was decided that Mitchell's brands were to be 'pushed in all areas with the support of press advertising' (Bristol: 38169/A/2/14/M.154).

3 Competition-offsetting mergers and acquisitions

Increased competitive pressure leading to acquisitions of struggling firms was not the only source of structural change resulting from the RTPA. That idea that compensatory, anti-competitive mergers occurred following the RTPA was advanced by MPs and economists at the time (HC Deb 1959, 1960; *The Economist* 1959, 1960; TNA: BT 258/1203), and is often suggested in the secondary literature (Crafts 2012; Hannah 1983; Owen 1999; Prais 1976).

The RTPA did not introduce any means for merger control, and larger firms could strategically use M&A either to neutralise the threat from smaller competitors who began to pose a threat ('killer acquisitions': Cunningham *et al.* 2021), or to shield themselves from regulation within the legal form of an 'interconnected bodies corporate'. A striking example of the former can be found in the cigarette market. The story centres on the reintroduction of coupon trading to the market; a promotional scheme where gift coupons would be included with packs of cigarettes, which could be saved up and exchanged for consumer goods.

Cigarette gift coupons were first introduced in the 1920s and by 1929 all leading cigarette manufacturers except Imperial had coupon brands (MC, 1961). The TTA's 1934 registration agreement contained a clause binding signatories not to manufacture or sell coupon-bearing goods, nor to trade with anyone who did. Imperial's market share jumped from 55% in 1933 to more than 79% in 1934 following the removal of gift coupons. Two decades later, on the cusp of a new competitive regime being ushered in through the RTPA, their market share had been maintained at this level. The MC would later comment that this period between the end of coupon trading and the enactment of the RPA was one where Imperial lacked 'any effective stimulus to efficiency' (Ibid.).

The RTPA, by bringing an end to the TTA, meant issuing gift coupons was feasible again. In October 1956, only a month after the disbandment of the TTA, J. Wix & Sons became the first manufacturer to announce a gift coupon scheme (*Financial Times* 1956b). The coupons (Figure 7) came with their Kensitas cigarettes, five per pack of twenty; gifts ranged from nylon stockings, obtainable for 125 coupons, to a gold wristwatch, for 7,600 coupons (Bristol: 38169/Ad/GC/12-13). The scheme was a success for Wix, largely thanks to being the first to move in the field (MC 1961), and their simultaneous refocussing of advertising materials around the "free" gifts (Figure 8).

The firm became profitable in 1957, paying dividends for the first time since 1954, and steadily increased profits and market share thereafter (Figure 9). By 1961, five years after the RTPA, profits totalled £2.2m, the Kensitas brands represented 5–6% of the overall cigarette market, and Kensitas

Figure 7: Kensitas gift certificates. Author's personal collection.

Figure 8: Press cutting from *Picture Post*, 14 January 1957. Author's personal collection.

Tipped was the second-best-selling brand in the filter-tipped sub-market (*Financial Times* 1961a; Alford 1973). By this point, the larger manufacturers could no longer ignore the rapid ascension of the firm.

On the 14 December 1961, a deal was signed where Gallaher agreed to acquire the whole of J. Wix's share capital from their American parent company in exchange for around 13% of Gallaher shares (*Financial Times* 1961b). In one fell swoop Gallaher had nullified the competitive threat from the firm which had most successfully exploited the new freedoms of the RTPA, and now controlled the only majorly successful coupon-bearing brand. Gallaher chairman Cecil Mason commented that it is 'much less risky acquiring a successful seller than attempting to launch a new rival' (*Financial Times* 1961c). How many other post-RTPA mergers were of a similar character?

4 Enforcement failures

In November 1956, the MC began their investigation into abuses of competition in the supply of cigarettes, tobacco, and tobacco machinery. Their report was published in July 1961 and shockingly revealed that Imperial was secretly maintaining a large shareholding in Gallaher (MC 1961), their apparent main rival, a fact which even Ministers were unaware of (TNA: BT258/1949.) Imperial acquired 51% of Gallaher's ordinary shares in 1932, later reducing this to 42.5% in 1946 after discussions that holding companies may be forced to publish accounts for subsidiaries (Cohen Report 1945). Imperial clearly intended to conceal the shareholding.

The MC recommended Imperial divest from Gallaher, finding it could operate against the public interest and prevent competition. However, in December the BoT President (then Frederick Erroll), after lengthy discussions with Imperial, announced this would not be implemented. This marked the first time the Government rejected a major MC recommendation.

Prime Minister Macmillan asked for clarification on the decision, wondering whether it was discussed at any Cabinet Committee meetings beforehand (TNA: PREM11/4027/M202/61). It had been: at a meeting of the Economic Policy Committee on 6 December 1961, where Erroll admitted, 'there is no existing power to require Imperial to dispose of their shares' (TNA: IR40/14187). Before Erroll had publicly announced his decision, Imperial's chairman, Roger Clarke, had repeatedly stated they would not willingly accede to the MC's divestment recommendation (*The Economist* 1961; *Daily Mail* 1961), implying a voluntary agreement could not be reached. Erroll was initially attacked for his 'unconditional surrender' (HC Deb 1962a), but at this point there was little public recognition of how little leverage the government had in the situation.

After further questioning in Parliament, Erroll was forced to admit he lacked the necessary statutory powers. Attempting to save face, he suggested that 'a company of [Imperial's] standing might well have accepted the Government's wishes ... had I wished to ask it to' (HC Deb 1962b). Even if this is true—that he simply didn't want to force divestment—the fundamental point is that resistance from *any* industrial sector would have similarly meant the government could not implement the MC's recommendations. A general need for new 'power[s] to require divestment of assets' was recognised by BoT Ministers in a policy review, where they cited the Imperial-Gallaher case (TNA: BT64/5223). It is reasonable to suggest this encouraged firms to pursue competitive restraints with more vigour, and without fear of political reprisal, than they otherwise would have. Gallaher's acquisition of Wix, finalised a few weeks after Erroll's announcement, and which Imperial had prior knowledge of (Bristol: 38169/HAF/6/46/Sa.118/61), might be taken as a fitting example.

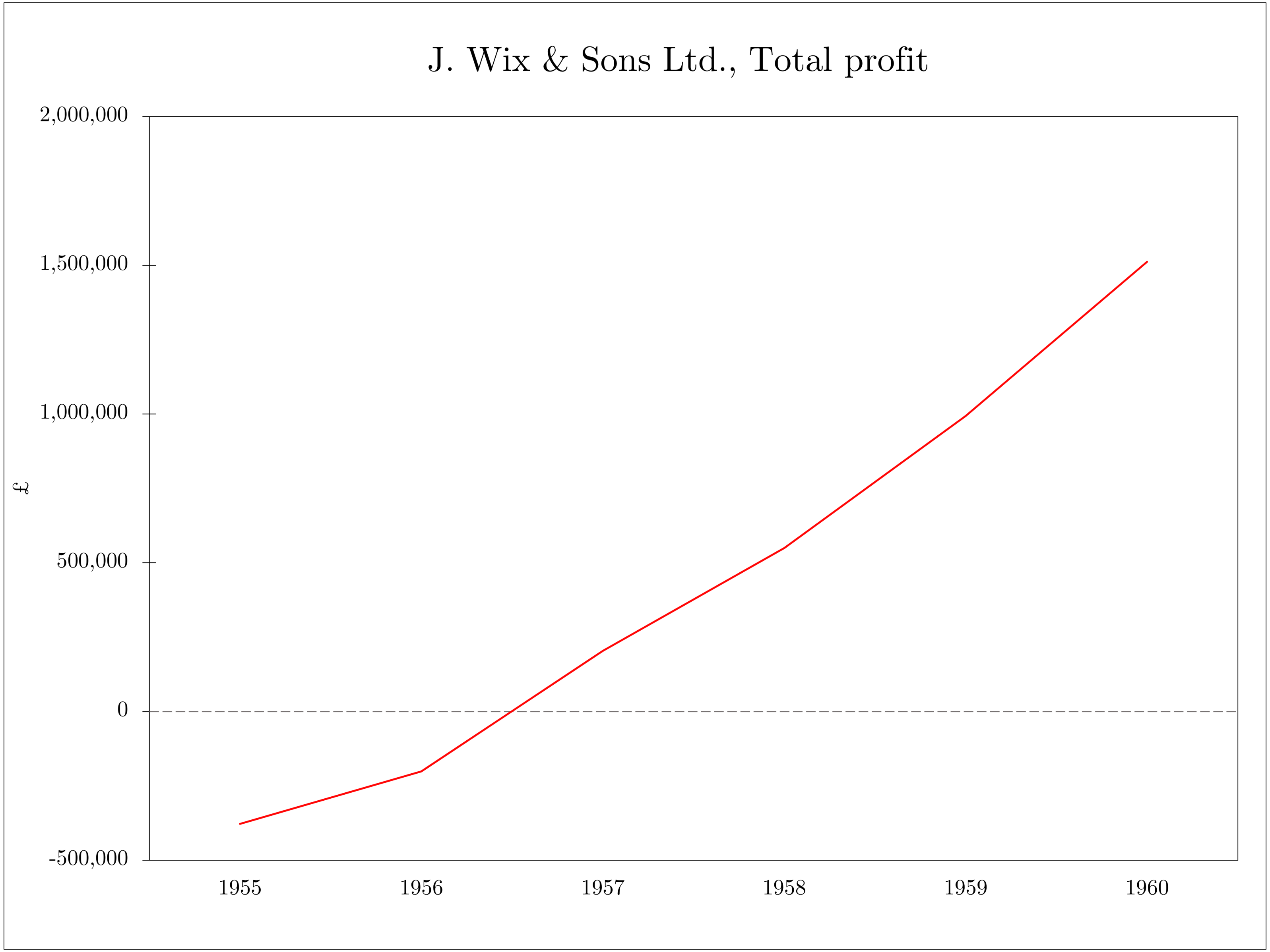

Figure 9: Data from Meeks, Wheeler, and Whittington (1998).

5 Conclusion

The RTPA represented a necessary step in the evolution of British competition policy. However, a lack of consideration as to how firms would seek to circumvent competition ultimately undermined its positive impact. Its defects—namely, what was left out of its provisions—induced structural changes that, in the view of P.W.S. Andrews, were 'an unfortunate consequence from the general economic point of view' (TNA: BT 258/1203). Yes, part of its structural impact was as a result of increased competition, which it could be said 'cannot be avoided' in many cases (Symeonidis 2000) and so should not automatically arouse suspicion. But we cannot assume that everywhere *price* competition was the main driver, instead of a more ambiguous, controversial form of competition (vis-à-vis its social value), like an advertising arms race.

The RTPA, then, was a Potemkin policy, with an 'appearance of action' (HC Deb 1956h) but representative of broader failures in post-war competition policy. According to Crafts (2012; Crafts and Toniolo 2008), lack of competition was a key factor in Britain's weak productivity growth and relative economic decline during the post-war "golden age". While recognising the RTPA's imperfections, Crafts seemed to view it as the best of a bad bunch, singling it out as the 'only' Act from this period which 'had teeth' (2017). *British* teeth?

This is the first narrative study concerning the RTPA's impact on firm strategy and market structure. Existing empirical work reports the effects of the RTPA in terms of parsimonious statistical associations between relevant firm or industry variables. Under this approach, the tobacco industry has been misclassified as an industry which was 'never ... directly affected by competition policy' in this period (O'Brien *et al.* 1979). If we looked at the tobacco industry five years, say, either side of the RTPA, through the lens of quantitative data that can be collated and coherently analysed for most British industries, then it would certainly *appear* that nothing changed. But this idea is clearly dispelled here. It is a reminder that our methodological framework inevitably shapes the nature of the insights.

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