The Determinants of Globalization and the Canadian Brewing Industry

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Why is it that Canadian beer brands and brewers do not have a significant global presence? After all, one would be hard pressed to think of a nation more naturally advantaged when it comes to brewing. The vast northern territory has all of the natural ingredients -- barley, hops, and fresh water -- necessary to manufacture a world-class beer. Furthermore, there is a legacy of commercial brewing in Canada that stretches back over three and a half centuries. Canada's oldest and most successful brewers -- Molson, Labatt, Carling, Sleeman and Alexander Keith -- began their operations earlier than most of the global firms that have since taken them over. It is not that Canadian beers are inferior. Beginning in the late nineteenth century, Canadian ales, lagers and stouts won international awards for taste, quality and uniqueness. Many of these award-winning beers were once copiously consumed at home. A strong beer-drinking culture has existed in Canada since the Conquest. But Canadian brewers have had a difficult time penetrating foreign markets, leading one commentator to ask recently: "Why don't Mexicans drink Molson?"[1]

This paper will explore that question and the inter-related one, why is it that Canada's oldest and largest beer companies no longer exist as autonomous agents? By analysing the country-specific, industry-specific and firm-specific determinants of growth and survival, the paper offers a multi-layered institutional analysis of the historical determinants that have prevented Canada from creating global enterprises in what was one of the earliest, most successful and most diverse industries in the history of Canadian manufacturing.

Layers of Institutional Analysis

When theorists speak of "growth" they are referring to the increase in size [of a firm] as a process of development, "either organically or through merger and acquisitions."[2] The concept of "survival", on the other hand, refers to the maintenance of a firm's autonomy of action. In this respect, non-survivals, or "exits", include firms that have either been liquidated, dissolved, discontinued, or absorbed, as well as firms that have been acquired by, or merged with, other

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[1] Andrea Mandel-Campbell, *Why Don't Mexicans Drink Molson: Rescuing Canadian Business from the Suds of Global Obscurity* (Toronto, Douglas & McIntyre, 2007), pp. 141-7.

[2] Edith Penrose, *The Theory of the Growth of the Firm* (Oxford, Oxford University Press, 1959/1995), pp. 1-2.

firms, even if they were able to retain their corporate identity and continuity of existence for a significant period of time.[3] Growth and survival therefore have a dynamic element and as such can only be fully understood as historical phenomena.

In her classic study *The Theory of the Growth of the Firm*, Edith Penrose argued that growth and survival are consequences of a complicated interaction of a company's resources, capabilities and market opportunities. The pace and direction of growth is determined by a firm's technical and managerial capabilities as well as by developments in the marketplace. According to Penrose, growth is strongly associated with the number of competitive advantages of the firm. In the long run, the profitability, growth and survival of an enterprise depend on its ability to establish "relatively impregnable bases" (e.g. by raising barriers to entry or using restrictive practices) from which to adapt and extend their operations in an uncertain, changing and competitive world. [4]

While Penrose and other theorists concede that there is no "secret recipe" that explains survival and sustained growth of the firm, they do maintain that it is possible to monitor the evolution of firms by making systematic comparisons between the largest multinationals from different countries and assessing the type of relations they have developed among themselves.[5] The distinctive nature of studying the evolution of multinationals is that, beyond the multi-product and multi-plant dimensions, the firm also needs to possess other ownership advantages over competing indigenous firms when dealing with different economies and cultures.[6] What is unique to the alcoholic beverage sector, of

[3] Neil M. Kay, *Patterns of Corporate Evolution* (Oxford, Oxford University Press, 1997), pp. 78-81.

[4] Edith Penrose, *The Theory of the Growth of the Firm*, p. 137.

[5] Peter E. Hart and Robert D. Pearce, "Growth Patterns of the World's Largest Firms, 1962-1982" University of Reading: Discussion Papers in International Investment and Business Studies, No. 83 (9184).

[6] John Dunning, " Trade, Location of Economic Activity and the MNE: A Search for an Eclectic Approach", in B. Ohlin, P.O. Hesselborn, and P.M. Wijkman (eds.), *The International Allocation of Economic Activity* (London, MacMillan, 1977), pp. 395-418. These ownership advantages must be sufficient to compensate for the costs of setting up and operating a foreign value-adding operation in addition to those faced by indigenous producers or potential producers. Elsewhere, Dunning identifies three types of ownership-specific advantages: (1) those that stem from the exclusive privileged possession of or access to particular income generating assets (2) those that are normally enjoyed by a branch plant compared with a *de novo* firm, and (3) those that are a consequence of geographical diversification or multi-nationality *per se*. (See Dunning *International Production and the Multinational Enterprise* (London, Allen & Unwin, 1981), p. 27

which brewing is a part, is that it is a case of a non-science-based industry in which firms have both survived a long time and grown very large.

So why have some firms in the alcoholic beverage industry come to dominate global markets while others, like Molson, Sleeman and Labatt, have failed to survive as autonomous firms? In order to answer this question the paper analyzes the industry-specific, country-specific, and firm-specific determinants that have lead to growth and survival in the brewing industry.

The first section of this paper analyzes the industry-specific determinants of growth. These determinants are predominantly exogenous -- i.e. beyond the control of the firm -- and affect all firms within the industry equally. The three industry-specific determinants that had the greatest impact on the global brewing beverage industry since the 1960s are: the changing patterns of consumption, the level of industry competition, and the nature of the industry's structure.[7]

The second section of the paper examines the country-specific determinants of growth and survival. Such determinants are embedded in the institutional and natural environment and include government regulation, taxation, the national system of corporate governance, as well as the processes, structures, and cultures that have fostered or hindered the growth of the firm. Since the publication of Geert Hofstede's monumental study, there has been a growing body of literature on the role of culture in the growth, survival and internationalization of the firm.[8] Culture, corporate or otherwise, affects everything from consumer behaviour, to industry structure, to the nature of government-business relations, to appraisals of performance, to management objectives, and the humanization of work.[9] As will be seen below, this was the case in the Canadian brewing industry, and it helps examine why Canadian brewers have been relatively unsuccessful at penetrating foreign markets.

The third and final section of this paper analyzes the firm-specific determinants of growth and survival in the Canadian brewing industry since 1960. The focus is on Canada's biggest brewers, those firms that have dominated the domestic brewing industry and thus had the greatest chance of going global. Unlike country- and industry-specific determinants, these determinants of growth are endogenous to the firm; that is, they are factors that a firm can

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[7] *Global Brands* (Cambridge, Cambridge University Press, 2007), p. 21

[8] Geert Hofstede, *Culture's Consequences: International Differences in Work-Related Values*. (Beverly Hills, California, Sage Publications, 1980); Mark Granovetter, "Economic Action and Social Structure: The Problem of Embeddedness", *American Journal of Sociology* (1985), pp. 481-501.

[9] Geert Hofstede, "The Business of International Business is Culture," Peter J. Buckley and Pervez N Ghauri, *The Internationalization of the Firm: A Reader* (London, International Thomson Business Press, 1999), pp. 381-393.

control. Such determinants include strategic choices, corporate structures, brands and marketing knowledge, entrepreneurial talent, first-mover advantage, technology and economies of scale and scope. In her recent study of the evolution of multinationals in the alcoholic beverage industry, the business historian Teresa de Silva Lopes argues "it is the firm-specific determinants that most influence the firms' competitive positions."[10] As a result, more space will be dedicated to examining these determinants of the growth and survival of those firms operating in the global brewing industry.

It is important to note that these three levels of determinants do not operate in isolation. Rather they over overlap and complement one another, with each level providing important determinants for the growth and survival of firms.

Industry-specific determinants

Globalization came late to the Canadian brewing industry, as it did to the brewing industry elsewhere.[11] Since the second industrial revolution in the late nineteenth century, many firms -- with competitive advantages derived from economies of scale and scope -- had established production facilities in foreign markets. Geographic expansion into distant markets provided a way for modern industrial enterprises to continue to exploit their comparative advantages. The automobile industry, for instance, began to globalize in the earliest days of mass production. By 1928, Ford and GM were assembling vehicles in twenty-four countries, including Japan, India, Malaysia, and Brazil. Ten years later both companies were operating large-scale integrated "transplant" facilities in Europe. After the Second World War, an increasing number of businesses -- a few of them Canadian[12] -- embraced a strategy of foreign direct investment as a means of global growth. Firms from around the world became successful challengers to what the eminent Harvard business historian Alfred Chandler termed "first movers" -- those Parsonian industrial organizations like Ford, GM, RCA, Du Pont, and Dow which had established branch plants in distant lands early in the twentieth century.[13] Having relentlessly expanded the output of their standard production line (i.e. increased their scale) and introduced new sorts of products (i.e. increased their scope), post-war industrial firms invested in new

[10] *Ibid*

[11] Benson-Armer et al. (1999).

[12] Between 1945 and 1970, Canadian corporations such as Inco, Brascan, Noranda, Cominco, Alcan, MacMillan Bloedel and Massey-Ferguson made substantial investments abroad. See Campbell, *Global Mission*; [12] MacKay, *Empire of Wood*, pp. 245-275; Neufeld, *A Global Corporation*, pp. 290-302.

[13] A. Chandler, *Scale and Scope*, pp. 117, 122, 171-5, 213-17, 446-52.

products and new geographic markets in order to grow.[14] The global enterprise thus evolved naturally out of the successful national corporation.

For those firms in the brewing industry, however, globalization did not occur until the end of the twentieth century. Consumer taste, entrenched regional brands, barriers to trade, and convoluted distribution systems made brewing a form of trench warfare: gains for those with global aspirations came only slowly. Until the end of the Second World War, the only international brewer was Ireland's Guinness which, in reaction to falling sales at home and increased protectionism following the First World War, introduced advertising in Great Britain and established a brewery in London.[15] After 1945, two other brewers that dominated their small home markets, Holland's Heineken and Denmark's Carlsberg, set out to turn their beers into global brands. In most countries, however, brewing remained a local business.

In Canada, the period between 1945 and 1965 witnessed the rise of the "national brewers" and a consolidation of the Canadian brewing industry. As other industries were going global, the brewing industry in Canada was finally shedding its regional skin and stretching out across the nation. Three brewers emerged to dominate the Canadian beer market. By acquiring existing breweries and building new production facilities from the ground up, Canadian Breweries Limited (which later became know as Carling-O'Keefe), Molson and Labatt came to dominate the national marketplace. By 1965, over ninety-five percent of the total volume of beer consumed by Canadians was being produced by these three firms. They thus became known as the "big three".

Fittingly, the first Canadian brewery to go national was E.P. Taylor's Canadian Breweries Limited. Having built a regional giant in Ontario[16], Taylor set his aim on the national market place.[17] "Having been successful in Ontario, we have now raised our sights and plan to repeat the process," Taylor proclaimed with a mixture of pride and prophecy, "so that we can become a truly national concern."[18] With that goal in mind, Taylor started buying up breweries across the nation. In 1951, he purchased the Frontenac Brewery in Montreal, and renamed it Carling Breweries (Quebec). The following year he took control of the National Breweries in Quebec, which had to bear the

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[14] *Ibid*, pp. 117, 122, 171-5, 213-17, 446-52.

[15] S.R. Dennison and Oliver MacDonagh, *Guinness 1886-1939: From Incorporation to the Second World War* (Cork, Ireland, Cork University Press, 1998), pp. 229-282.

[16] J.C.H. Jones, "Competition in the Canadian Brewing Industry", pp. 51-80.

[17] Taylor did this by acquiring ownership and control of existing Ontario breweries and rationalizing their operations. Largely as a result of his actions, the number of breweries declined sharply in Ontario from 36 in 1930 to just five in 1958. Albert Shea, *Vision in Action: The Story of Canadian Breweries Limited from 1930 to 1955,* pp. 68-128.

[18] Sneath, *Brewed in Canada*, p. 169.

unrelenting costs of over capacity; that is, of too many plants and too many brands. After the president of National Breweries, Norman Dawes, rejected his merger offer, Taylor purchased enough stock to give him effective control of the company. He subsequently reorganized and re-named the firm Dow Brewery Limited, after the company's flagship beer. Dow joined O'Keefe, Carling and Brading as brands that Canadian Breweries Limited would produce, market and distribute from coast-to-coast.

Given the regulatory regime (more below), having a national reach meant maintaining a physical presence in each of the provinces. As Taylor made note in a confidential company memo, it was "not practical" for breweries in central Canada to ship beer to the west and east and compete with local breweries. Taylor was profoundly aware of the provincial tariff barriers against imports from other provinces. Therefore, Taylor determined that "the proper course is to purchase two or three prosperous [regional] concerns."[19] South of the border and in the beer-producing nations of Europe, going national was far less capital-intensive, leaving them with more capital to diversify geographically. By 1960, Canadian Breweries Limited had a significant presence in every province except Prince Edward Island[20] and Carling, O'Keefe, Brading and Dow had become "distinctively national brands."[21] The problem was that while a few brewers in Canada were developing national brands, a few brewers elsewhere were taking their national brands global (see below).

For a time Canadian Breweries reaped the rewards of being the industry's "first mover" but soon the innovative corporation had competition on the national scene. In 1952, Labatt's board of directors authorized the company's first major investment outside of Ontario. At a cost of $6.5 million a state-of-the art brewery was built on a twenty-six acre site in the Montreal suburb of Ville LaSalle.[22] The historic brewery now had a solid presence in Central Canada, but as an internal report made note, the company was still not fully national. "It is desirable for John Labatt Limited to become a fully national company, marketing their products in all provinces. Under present government regulations it will therefore be necessary to establish plants in the three western provinces."[23]

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[19] E.P Taylor (26 October 1942), *ibid*.
[20] In 1958, Canadian Breweries Limited had a 14.9 percent share of the Nova Scotia beer market, a 5.7 percent share of the N.B. market, 51.8 percent share of the Quebec market, a 60.9 percent share of the Ontario market, a 41 percent share of the Manitoba market, a 34.2 percent share of the Saskatchewan market, a 7.9 percent share of the Alberta market, and a 36 percent share of the B.C. beer market. See J.C.H. Jones, "Competition in the Canadian Brewing Industry", Table 13, p. 79.
[21] J.C.H. Jones, "Competition in the Canadian Brewing Industry", p. 80.
[22] Tucker, "Labatt's", p. 308.
[23] *Ibid*, p. 328.

Shortly thereafter Labatt purchased three plants in Manitoba: Shea's Winnipeg Brewery, Pelissier's Brewery in Winnipeg, and the Kiewel Brewing Co. in St Boniface. Before the decade was out Labatt had purchased Lucky Lager in British Columbia. When, in 1962, the venerable brewery purchased Bavarian Brewing Company of Newfoundland, it could rightly claim to be brewing beer "from sea-to-shining-sea."[24]

Always a "fast follower" -- to use the terminology of Alfred Chandler -- Molson soon undertook its own national expansion. Like Labatt, it engaged in brown field and green field investments, acquiring existing breweries as well as building new ones. Having taken over the reins of the company in 1953, Hartland Molson's first move was to strike back at the Ontario brewers that had invaded his home province. In 1955, he authorized the construction of a 300,000-barrel brewery on Fleet Street. The $11-million plant sat on 3.8 hectares of reclaimed land on Toronto's lakeshore, right in Canadian Breweries' backyard. In 1958, Molson went west, purchasing the prairie powerhouse Sicks' Brewery. In 1962, Molson again quickly followed the actions of Labatt and Canadian breweries by purchasing an established brewery in Newfoundland. Thus, it too was a national concern.

In Canada, therefore, the brewing industry was characterized by a high degree of concentration. A relatively stable cartel of three firms, which was supported by the government and maintained by its policy of erecting high barriers to entry, dominated the national market. Between 1960 and 1990, the big three brewers manufactured between ninety-six and ninety-eight percent of the beer consumed by Canadians. While concentration was occurring the world over, the unique character of the Canadian case was that the system of government regulation mitigated against price-based competition, hampering the global competitiveness of Canadian firms in the long-run (more below).

By 1990 the biggest beer market was still the United States and the biggest American brewer was Anheuser-Busch, which made it the indisputable market leader in the world. That year the American brewing giant produced 104.6 million hectolitres of beer, which accounted for just over nine percent of total global beer market volume. Anheuser-Busch, along with the other leading U.S. brewing companies -- i.e. Miller and Coors -- based their operations predominantly in the United States and had an exclusive focus on beer.[25] Indeed, Anheuser-Busch derived eighty-five per cent of its sales from its home market. As in the past, their foreign expansion took place primarily through exports and

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[24] *Ibid*, p. 310.

[25] M. Stack and G. Myles, "The repeal of prohibition and the resurgence of the national breweries: productive efficiency or path creation?" *Management Decision*, Vol. 43 No. 3, (2005) pp. 420-32; Joan Holleran, "It's a small world for U.S. brewers," *Beverage Industry*, vol. 87, issue 5, (May 1996), p. 10.

licensing agreements covering production, distribution and commercialisation activities.

World Top Brewing Groups in 1990 (35.1%)

Rank	Brewery	Production Volume in millions of hl	Percentage of world beer production
1	Anheuser-Busch	104.6	9.1
2	Miller	62.2	5.4
3	Heineken	46.5	4.0
4	Kirin	34.6	3.0
5	Foster's	30.5	2.7
6	Danone	26.0	2.3
7	SAB	25.8	2.2
8	Brahma	25.5	2.2
9	Guinness	24.3	2.1
10	Coors	23.7	2.1

In those less-populated countries, like England, Scotland, Germany and Canada, where there was a strong tradition of brewing, but where brewers remained focused on the domestic market and therefore generally lacked international experience beyond exports, the size of the firms remained relatively small from a global perspective.[26] But the size of the home market did not necessarily determine the growth and survival of the firm. Exceptional enterprises like Heineken of Belgium, Guinness of Ireland, and SAB of South Africa, Forster's of Australia, and Kirin of Japan were able to become large and globally dominant despite the relatively small size of their domestic markets. These firms succeeded by developing corporate strategies, global brands and market knowledge that allowed them to penetrate foreign markets. Nevertheless, in comparison to other industries, in 1990, brewing remained relatively unconsolidated and local.[27]

But that changed during the 1990s, as the industry became very concentrated and truly global. Whereas in 1990, the top ten brewers represented 35.1% of the world's market share, by 2000 the top ten brewers controlled 36.9% of the world's beer market. The concentration accelerated thereafter. In 2005, the world's top ten brewing groups represented 54.9% of the world market share. And by 2010 the top ten brewers controlled just under three-quarters (74%) of the world's beer market. Since the 1990s, therefore, leading brewers in advanced

[26] Chris Lewis, "The Future of British Brewing: Strategies for Survival", *Strategic Change*, vol. 10 (2001), pp. 151-161

[27] The concentration was substantially less than in related industries. In the soft drinks sector, for instance, the top four players shared 80% of the world market.

economies have launched aggressive global campaigns, resulting in an unprecedented global consolidation. The global consolidation has become a key factor shaping global development as brewing companies achieve greater scale and their beer brands grow in more international markets. To survive and grow within this predatory global environment firms had to be quick on their feet and develop and redevelop the strategies and structures necessary to give them advantages vis-à-vis their competitors (more below).

Several factors propelled the industry towards globalization. On the demand side, traditional markets had gone flat. In the main markets of Northern Europe and North America, consumption remained static or declined gently after the mid 1970s, making it difficult for brewers to raise prices in established markets. In the United States, for instance, per capita consumption of beer increased by less then .04%, between 1975 and 1995, from 80.63 to 83.65 litres of beer per person, per annum.[28] During the same period, per capita consumption of beer in the Netherlands, the home of Heineken, increased from 78.96 to 85.80 litres. In the United Kingdom, the consumption of beer actually increased until 1980 and then declined just slightly over the next decade.[29] This might help explain why most British brewers continued to focus on the domestic market. In Belgium, on the other hand, per capita beer consumption declined substantially during the period, from 130.5 litres to 104.0 litres.[30] Similarly, per capita beer consumption declined in Denmark from 129.3 litres in 1975 to 124.4 litres in 1995. As a result Belgium's biggest brewer, Interbrew, and Denmark's Carlsberg geared up their global quest. Canada faced a similar decline in beer consumption. Having reached a post-war high of 86.8 litres in 1975, per capita consumption of beer fell to 80.7 liters in 1985 and then to just 77.1 litres in 1990. By 1995, the level of per capita consumption had fallen even further to 70.1 liters.[31] Unlike Interbrew and Carlsberg, however, Canada's biggest brewers chose to diversify out of beer, for reasons explained below, rather than to seek out new markets elsewhere. While other brewers were looking beyond the nation's boundary for growth, Canada's big three brewers remained defensive and inward looking.

This was unfortunate because while traditional markets were stagnant, emerging markets were rapidly expanding. Between 1975 and 1995, per capita consumption of beer in Mexico, for instance, increased by thirty-three percent.[32] Brazil also witnessed a rapid rise in beer consumption. But it was China, with its large population, demographics and rising real incomes that held the greatest

[28] Ed Gregory, Wendy Hurst and Thomas Gussman, *Alcoholic Beverage Taxation and Control Policies*, (Ottawa, Brewers' Association of Canada, 1997), p. 498.
[29] *Ibid*, p. 472.
[30] *Ibid*, p. 50.
[31] *Ibid*, p. 70.
[32] *Ibid*, p. 276.

promise for brewers. In 1995 the *Asian Business Review* predicted that, "China is set to become the world's largest beer market by the year 2000."[33] The magazine was wrong in only one regard: It wasn't until 2004 that China moved ahead of the U.S. to become the world's biggest beer market, with annual consumption of 300 million hectolitres that year. As barriers to international trade were lowered during the last two decades of the twentieth century, brewers from established markets rushed to gain a foothold in the emerging markets of the world. For country- and firm-specific reasons discussed below, Canada's largest brewers were unable to acquire a lasting share of the global market.

Country-specific determinants: "Rich by Nature: Poor by Policy"

In an article entitled "'Rich by Nature, Poor by Policy: The State and Economic Life in Canada", the business historian Michael Bliss argued government intervention had made Canadians poorer than nature had intended. Despite being one of the world's richest nations in terms of natural resource endowment, Canada had lagged behind other developed nations, specifically the United States, in terms of its economic performance because of its "addiction to the positive state."[34]

Few economic and business historians deny the role played by natural resources in the early development of Canada. The giant of the second generation of professional economists, Harold Adam Innis (1894-1952), formulated a "staple thesis" to explain Canadian growth and economic integration. The pattern and pace of early Canadian development, Innis and his many disciples maintained, was determined by the pursuit of primary products -- fish, fur, timber and wheat – and their export to foreign markets.[35] According to Innis, growth and development was best explained by the dynamics of the staple trades. Even those historians who have recently become skeptical of the universality of Innis's conclusions do not deny the basic fact that Canada has been "rich by nature". [36] The more perplexing question is whether public policy

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[33] Sarah Gregory, "Brewers Target Asia's Developing Markets," *Asian Business Review*, (February, 1995).

[34] Michael Bliss, "Rich by Nature, Poor by Policy: The State and Economic Life in Canada", p. 88.

[35] H.A. Innis, *The Fur Trade in Canada: An Introduction to Canadian Economic History* (Toronto: University of Toronto Press, 1956); W.T. Easterbrook and H.G. J. Aitken, *Canadian Economic History* (Toronto Macmillan, 1956).

[36] See for instance Béatrice Craig, *Backwoods Consumers & Homespun Capitalists: The Rise of a Market Culture in Eastern Canada* (Toronto: University of Toronto Press, 2009), Douglas McCalla, *Planting the Province: The Economic History of Upper Canada* (Toronto, University of Toronto Press, 1993); Robin Neill, *A History of*

has made the nation poorer than nature had intended, by compromising Canada's global competitiveness, particularly in the case of brewing and beer.

When it comes to brewing, Canada has long had a comparative advantage. The nation is ideally suited to produce beer. All the necessary natural ingredients – barley, hops and fresh water -- are located within the national boundary. Canada has an abundance of fresh water. Indeed, the expansive northern nation is near the top of water-rich countries, trailing only Brazil, Russia and China.[37] It also has plenty of grain. The most popular grain used in beer production is barley. As the brewing historian Richard W. Unger attests, the best barley grows in the northern hemisphere between latitudes of 45° and 55°.[38] Most of Canada is situated in this portion of the globe. The final ingredient that is necessary to produce beer is hops. Since the sixteenth century, hops have been used as a flavouring and stabilizing agent in brewing. Hops contained resins that help prevent contamination of the beer by bacteria and thus help beer to last longer and travel better. Like barley, the hop plant grows best under specific climatic and soil conditions; a minimum of 120 frost-free days is needed along with direct sunlight for at least fifteen hours a day. Thus hop cultivation is limited to those regions that are situated between 35° and 55° latitude. In Ricardian terms, therefore, Canada enjoys a comparative advantage in brewing.

It is not surprising therefore that beer was one of the first commodities to be manufactured in Canada. The history of Canadian commercial brewing stretches back three and a half centuries.[39] Admittedly, a number of other nations could claim a longer legacy. Commercial brewing in Holland, Belgium, Denmark and Germany dated from the Middle Ages. Nevertheless, Canada's breweries

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Canadian Economic Thought (New York, Routledge, 1991); Frank D. Lewis and M.C. Urquart, "Growth and the Standard of Living in a Pioneer Economy: Upper Canada, 1826-1851, *William and Mary Quarterly*, 56 (Jan. 1999), pp. 151-81; Marvin McInnis, "Marketable Surpluses in Ontario Farming, 1860" *Social Science History*, vol. 8, (9184) pp. 395-424. This group of "post-Innisians" do not reject the staple thesis but have moved beyond its emphasis on external forces, and rather stress the endogenous factors in economic growth and development.

37 Estimates vary depending on how one defines "fresh water" – whether it means "available," "usable," or merely "existing." One study claims that Canada has 20% of the world's fresh water – ranking it at the top – but only 9% of "renewable" fresh water. (See Manuel Ramon Llamas and Emilio Custodio (eds.), *Intensive Use of Groundwater: Challenges and Opportunities* (Netherlands, Swets and Zeitlinger, 2003) p. 302

38 Richard W. Unger, *Beer in the Middle Ages and the Renaissance* (University of Pennsylvania Press, 2004), pp. 53-106.

39 M.J. Bellamy, "'Rich by Nature, Poor by Policy'? The premature birth and quick death of commercial brewing in Canada, 1667-1675", *Brewery History* no. 137 (Fall, 2010), pp. 48-70.

were among the first established in North America. When John Molson took over the operation of a thirty-six by sixty-foot log-built brewery in Montreal in 1786, he laid the foundation for a firm that would go on to be the longest-lived family business in Canadian history and the oldest continuous brewery in North America. In the decades that followed Alexander Keith (in 1820), John Carling (in 1843), John Sleeman (in 1847), and John Labatt (in 1848) founded the firms that would later dominate the Canadian market. Thus Canada not only had the natural resources but also the historical legacy that should have enabled, at least in theory, the nation's brewers to compete in the global market place.

One therefore returns to the original question: Why haven't Canadian brewers come to dominate world markets, as much as global players have come to dominate the Canada beer market? Part of the answer lies in the nature of government business relations, and the country-specific character of regulation and taxation. Perhaps no industry has been as heavily taxed and regulated as the brewing industry. The uniqueness of the Canadian case is that brewers faced a dual system of regulation and taxation. Under the terms of the nation-forming British North American Act of 1867, the provinces had the constitutional power to regulate the retail sale and distribution of intoxicating drink, while the federal government had the power to regulate the production of beer and other alcoholic beverages. At the dawn of the twentieth century, provincial governments took these powers to the extreme when they attempted to legislate the brewing industry out of business. Prohibition had a destructive effect on the Canadian brewing industry. Nationally, the number of breweries in operation was cut in half, from 112 in 1915 to just 66 in 1935.[40] The relatively strong and dynamic growth of the Canadian brewing industry up to the 1920s was retarded by the country-specific determinant of government regulation.[41] While growth was also restrained during the period of prohibition south of the border, it was not held back in the beer-producing nations of Europe. Thus they continued to grow, while brewers in North America were battling just to survive.

Bottom feeders like Edward Plunkett Taylor – later dubbed Excess Profits Taylor by his critics – used the opportunity created by prohibition to capture assets at rock-bottom prices and to construct large breweries that could capitalize on modern production techniques and advertising. By 1935, Taylor's company, Canadian Breweries, was twenty times the size of most turn-of-the-century breweries and represented a new post-prohibition Canadian reality. Taylor's aspiration was to create a brewery with national scope. But Canadian Breweries again ran into the bugbear of provincial legislation. In the period following prohibition, provincial governments instituted tariffs and imposed import quotas that limited out-of-the-province beer or stopped it altogether. As a result, beer

[40] M.J. Bellamy, "The Canadian Brewing Industry's Response to Prohibition, 1874-1920", *Brewery History*, no. 132 (Fall, 2009), pp. 6-7.
[41] Lopez, *Global Brands*,

sold in the province had to be produced in the province. While good for provincial treasuries, the move ultimately prevented firms within the Canadian brewing industry from benefiting from economies of scale. The "shipping brewers" south of the border could sell their products across the nation, which led to larger breweries concentrated in relatively few cities. It also gave U.S. brewers, like Pabst, Anheuser-Busch and Coors, a substantial head start in creating and marketing a few "national brands" – brands they would eventually take global. According to the business historian Teresa da Silva Lopez, brand development is critical to the growth and survival of the multinational enterprise in the alcoholic beverage industry.[42] The world's most successful alcoholic beverage brands have been long established, some being created as far back as the eighteenth and nineteenth century.[43] While brewers elsewhere began to look beyond the national boundary for growth, Canadian brewers were concentrating their efforts on dominating and protecting their share of the domestic market (more below).

After the Second World War, the nation's brewers -- through their lobbying agency the Brewers' Association of Canada -- successfully pressured the federal and provincial governments to protect them from foreign competition. The battle with the prohibitionists during the late nineteenth and early twentieth century had taught the brewers the value of lobbying.[44] And after the war, they again put this practice to use. The federal government responded to the brewers' pressure tactics by increasing the tariff on imported beer to a minimum of 12.5% per gallon.[45] The brewers had come to embrace the Canadian tradition. As Michael Bliss has argued, few Canadian businessmen have liked dangling on the strings held by Adam's Smith's invisible hand of free-market forces. "They looked to government to cut those strings, to liberate them from the harsh discipline of competition by taking them under its protective wing."[46] This was especially true of Canada's biggest brewers during the post-war period.

In addition to having to pay the federal tariff, foreign brewers seeking to sell their product in Canada would have to hurdle three non-tariff barriers used by provincial authorities to discourage the domestic consumption of non-Canadian beer (i.e. listing practices, distribution requirements and

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[42] *Ibid*, p. 36.

[43] Paul Duguid, "Developing the Brand: The Case of Alcohol, 1800-1880" *Enterprise and Society*, vol. 4, no. 3 (2003), pp. 405-441.

[44] M.J. Bellamy, "The Canadian Brewing Industry's Response to Prohibition, 1874-1920", *Brewery History*, no. 132 (Fall, 2009), pp. 2-17.

[45] The 12.5% tariff was the rate at which beer from British preferential or most-favoured-nation countries (e.g. the United States) were taxed. See Brewers' Association of Canada, *Brewing in Canada*, p. 97.

[46] Michael Bliss, "Rich by Nature, Poor by Policy: The State and Economic Life in Canada", p. 86.

discriminatory mark-up policies). Each province had its own unique distribution system, with its own distinct policies and practices. These added to the foreign brewers' cost of doing business in Canada and thus further protected domestic brewers from competition. Liquor control boards routinely imposed conditions on the supply of imported beer. For example, sales quotas and performance standards had to be continuously met. Distribution systems restricted the sale of imported beer to provincially-run liquor board outlets, where foreign brewers were forced to pay extra fees and meet additional requirements. For example, in Ontario, imported beer was only allowed to be sold in 6-packs instead of full cases. In other provinces restrictions were placed on the type and size of bottles sold. In addition, mark-ups and handling charges were higher on foreign beer sold in Canada.[47] Thus many foreign brewers, including U.S. brewers with plants close to the Canadian border, found it next to impossible to compete on a price basis. As a result for most of the post-war period, domestic brewers regularly manufactured over ninety-eight percent of the beer consumed in Canada.[48]

But the same regulatory regime that so successfully protected Canada's brewers from foreign competition led to plants of suboptimal size. According to a Conference Board of Canada report, the minimum plant size necessary to achieve ideal manufacturing efficiencies produced an annual output of at least 2.2 hectolitres.[49] Other reports put that figure higher.[50] But by the mid 1980s only five of Canada's twenty-eight brewers were operating at the 2.2 million hectolitres in capacity (all of them were in Ontario), and about half of Canada's production came from suboptimal plants. The same study concluded that beer production per plant in Canada was just over one-quarter the level, on average, of U.S. plants.[51] Canadian breweries were thus operating at a disadvantage relative to the optimal U.S. plants. As a result, when the news reached the boardrooms of Canada's brewing establishment that the federal government of Brian Mulroney was negotiating a free trade accord with the United States, the brewers' lobby quickly mobilized in an attempt to hold back the *laissez faire* tide.

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[47] In Ontario, for example, the handling charge for domestic brewers was 30 cents a case, while foreign brewers were required to pay $1.25. See James Sherbaniuk, "Regina vs. Canadian Breweries Ltd: An Analysis of a Merger Case" (Ph.D. Dissertation, University Washington, 1964), p. 97.

[48] Brewers' Association of Canada, *Brewing in Canada*, p. 97; Ed Gregory, Wendy Hurst and Thomas Gussman, *Alcoholic Beverage Taxation and Control Policies*, (Ottawa, Brewers' Association of Canada, 1997), p. 75.

[49] Conference Board of Canada, "The Canadian Brewing Industry: An Assessment of the Impacts of Liberalized Interprovincial Trade in Canada" (June 1990), p. 7

[50] Kathryn Collins, "The Canadian Brewing Industry" (Midland Walwyn Research, February 1991), p. 11.

[51] *Ibid*.

Free trade, the brewers maintained, would be the death knell of domestic brewing.[52] Even Canada's biggest brewers were far too weak to compete in an open marketplace. The structure of the Canadian beer industry was such that it worked against economies of scale. Due to the system of provincial barriers to trade within Canada, the industry's productive system was hopelessly fragmented in numerous uncompetitive plants across the country. Provincial rules forced the operation of breweries of suboptimal size. In a position paper presented to James Kelleher, the Minister of International Trade, the brewers lobby argued:

> Bilateral free trade with the United Stattes in beer must be considered in the context of the historical and continuing highly-regulated and trade-restricted domestic market environment, resulting from high interprovincial trade barriers and restrictions on inter-provincial shipment of beer. This environment has led to the development in Canada of numerous small-scale breweries which, while they have attained international recognition for their quality products, are not cost effective or cost competitive with their larger scale international competitors.[53]

A number of academic studies later gave some objective weight to the brewer's position, although most weren't willing to advocate continued protection.[54] The brewers therefore asked that the protective practices be grandfathered under the new accord, and threatened that if they weren't, they would come out publicly against the entire FTA. The threat worked, and as a result, brewing was one of only three industries to be exempt from the FTA. The protectionist regulatory regime remained in effect until 1995 when trade barriers finally came down. Canadian brewers could no longer hide behind the traffic wall, in an artificial environment free of price-based competition. Now, for the first time, they were forced to compete in an increasingly open, integrated, global marketplace. To survive they would have to have significant international activity and firm-specific advantages in relation to foreign firms. As will be seen below, this did not happen.

Firm-specific determinants

[52] Bruce Doern and Brian Tomlin, *The Free Trade Story: Faith and Fear*, pp. 78-79.
[53] Brewers' Association of Canada, "Perspectives on Canada-United States Free Trade (Ottawa, May 1985), p. 1
[54] See for example, I.J. Irvine, W.A. Sims, A. Anastasopoulos , "Interprovincial versus international free trade: the brewing industry" *The Canadian Journal of Economics / Revue canadienne d'economique*, Vol. 23, No. 2 (May, 1990), pp. 332-347.

Success in the brewing industry is determined in large part by a firm's ability to development global brands.[55] The world's largest beer companies manufacture the world's most popular beers. For example, Anheuser-Busch InBev, the world's biggest brewer, owns and manufactures Bud Light, Skol, Budweiser and Brahma -- the world's second, third, fourth and seventh best selling beers, respectively. The world's third largest brewer, Heineken, owns the world's sixth most popular brand, and the world's best selling international beer, with a non-domestic volume in 2008 of over 25 million hectolitres.[56] Not a single Canadian brand is listed among the world's top twenty-five most popular beers. Part of this is explained by the industry- and country- specific determinants analyzed above. The regulatory regime in Canada fragmented the Canadian industry for most of its history. As a result, the development of national brands, that might later be taken global, was delayed. But these exogenous determinants are only part of the explanation. Firm-specific factors played an equally critical role.

In an attempt to reduce costs and increase shareholder value, executives at Canada's big three breweries made the short-sighted strategic decision to enter into licensing agreements with foreign firms to manufacture and promote their beer within the national boundary.[57] Licensing agreements had the advantage of circumventing international trade barriers. Foreign beers that were brewed in Canada under license were not subject to either the federal tariff or the discriminatory mark-ups that other imported beers faced at the provincial government outlets. But the advantages did not end there. Licensing agreements substantially reduced transportation costs and allowed brewers to more quickly get their product to market. For these reasons brewers began approaching other brewers around the globe, particularly in the largest beer-drinking markets, to get them to brew their beer.[58]

In 1965, Labatt became the first Canadian brewery to sign a licensing agreement with a foreign competitor. The license with Guinness Overseas gave Labatt the exclusive right to brew and market their famous Guinness Stout brand in Canada. The landmark agreement was a sign of things to come. After a decade of unsuccessfully attempting to persuade Canadians to purchase domestic imitations of American light beers (e.g. Labatt's Cool Springs and Special Lite lager), Labatt opted instead to produce the "real stuff". In the spring of 1980

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[55] Lopes, *Global Brands* (Cambridge, Cambridge University Press, 2007)

[56] Impact, *The Global Drinks Market* (New York, M. Shanken Communications Inc, 2010), p. 439

[57] Jeffery Karrenbrock, "The internationalization of the beer-brewing industry," *Report of the Federal Reserve Bank of St Louis*, (St Louis, MO, November/December, 1990), pp. 6-8.

[58] *Ibid*, p. 6.

Labatt announced that it had licensed the right to brew Budweiser -- the "King of Beers" -- and distribute it to thirsty Canadians. Labatt had initially approached Anheuser-Busch with a proposal to brew Michelob north of the border. The undisputed brewing leader in the United States rejected that idea, however, suggesting instead that Labatt brew its Budweiser. Anheuser-Busch was harbouring as-yet-unannounced international ambitions. While the American beer giant controlled thirty-two percent of the U.S. market, by 1980 growth had become stagnant. Executives at Anheuser-Busch decided that in order to grow in the future, it would have to tap into external markets.[59] With that goal in mind, executives at Anheuser-Busch decided that Budweiser, and not Michelob, had the best chance of becoming a global brand.

At Labatt there was a sense that the international brewing industry was moving in a new direction; that in the future there would be a homogenization of tastes and a globalization of brands.[60] "We saw the globalization of brands," stated Don McDougall, the company's president in 1979, "and thought being ahead of everyone else might be a good idea."[61] Having joined Labatt shortly after receiving an MBA from the University of Western Ontario in 1961, McDougall quickly moved up the ranks at Labatt. Between 1973 and 1979 he held the titles of President and Senior Vice President and was a driving force behind the licensing agreement with Anheuser-Busch. The deal that he signed gave Labatt a ninety-nine-year license to brew Budweiser in Canada.

In the summer of 1980, Labatt rolled out the product in Alberta and Saskatchewan, a region where there had been a long tradition of brewing and drinking American-style lagers.[62] It wasn't until the following year that the Canadian brewer made Bud available to beer drinkers in Ontario, Quebec and British Columbia. By 1982 Budweiser accounted for about seven percent of the total Canadian beer sales.[63] The Americanization of Canadian brewing was underway.

The other big Canadian brewers took immediate notice. For Canadian Breweries Limited, which had been renamed Carling O'Keefe after the sale of the company to the British tobacco giant Rothmans in 1969, licensing the right to brew and market American beer in Canada held out the possibility of reversing its fortunes. Once the industry leader, Carling O'Keefe had suffered during the 1970s from not having a "national brand". Executives hoped that licensing the right to manufacture a well-known American beer would give them a brand that they could promote nationally. The decision was made that Miller High Life would be Carling-O'Keefe's Bud.

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[59] Maureen *Ogle, Ambitious Brew: The Story of American Beer*, p. 321.
[60] Brent, *Lager Heads*, pp. 63-64.
[61] *Ibid*, p. 63.
[62] Wiliam A. Hagelund, *House of Suds: A History of Beer Brewing in Western Canada*
[63] Brent, *Lager Heads*, p. 69.

Miller was launched in the summer of 1983. In an effort to make its new beer stand out, Carling decided that it would sell Miller in a tall-necked bottle of the same proportions as the U.S. Miller bottle. It marked the beginning of the end of the "stubby" bottle -- perhaps the single most distinctive feature of Canada beer in the post-war period. Miller quickly gained a 7-8% market share.

In November 1985, Molson Breweries of Canada Ltd. joined its major Canadian competitors in offering a domestic version of an American beer. Molson was rarely a "first mover". The corporate culture was such that conscious and conservative conduct was promoted and celebrated. As Molson's president Jacques Allard stated in 1985: "We watched to see how successful the other brands would be. Then with an eye on the future we moved." [64] After two years of talks with Coors of Golden, Colorado, Molson signed an agreement to brew Coors and Coors Light under license in Canada. Viewed through the prism of domestic market share, Molson's slow and deliberate action paid off. By the early twenty-first century, Coors Light was Canada's largest-selling light beer and the second best-selling brand in Canada overall (although the gain in market share came at the expense of Molson's historic brands). Viewed through the prism of global competitiveness, however, the move undermined the development and promotion of the firm's own brands, and ultimately compromised the growth and survival of the firm. As Teresa da Silva Lopes points out, own global brands is essential to growth and survival of multinationals in the alcoholic beverage industry.[65]

The success of brands like Coors Light led executives at the big three to conclude the licensing and then brewing and promoting of American brands was the way to go. But this was short-sighted in the extreme. To be sure, owning the right to brew the most popular American brand could add to the firm's bottom line. After all, brewing in Canada was a zero-sum game. Little revenue was generated from the big three's beer sales outside of the national boundary. Brewing and licensing these American brands made financial sense given the institutional environment. But the signs were already pointing in the 1980s to the globalization of the beer industry. What product would Canada have to offer the world if its beer was American?

Beyond developing global brands, successful alcoholic beverage firms are diversified in terms of geography and the products that they produce. Diversification has always held a special place in the minds of executives faced with stagnant or declining markets for their original product, as was the case in the alcoholic beverage sector after 1975. As Alfred Chandler has noted, during the 1970s, the drive for growth through diversification into related and unrelated

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[64] Fran Halter, "Molson Launches Coors Beer", *The Gazette* (7 November 1985), p. D-1.

[65] Lopes, *Global Brands*, pp. 129-179.

products "had almost become a mania."[66] This became the age of the protean multinational corporation, an enterprise dedicated to internationalization and the pursuit of synergies -- a seemingly magical mixture of business activities that were stronger and more profitable together than they were apart. Diversification could be rewarding, but it took substantial resources and continual commitment. The timing and type of diversification was also crucial in determining its success or failure. For those firms in the alcoholic beverage industry, diversification generally produced positive results when it related to the firm's core competencies; that is, when there were physical and/or knowledge linkages to the firm's assets that could be easily exploited. For example, when Louis Vuitton Moët Hennessy diversified into perfumes in the 1990s, it allowed the firm to exploit not only its marketing knowledge in terms of the general management of brands and distribution, but also its knowledge about specific markets, such as the Far East.[67] On the other hand, diversification often went wrong when a firm expanded into industries that were unrelated to its core business, and thus when physical and knowledge linkages were absent.

During the 1970s and 1980s, Labatt had joined many other companies, both and at home and abroad, which were diversifying in an effort to sustain their growth. More so than elsewhere, Canadian corporate managers believed that having "all your eggs in one basket" was a dangerous strategy. This mentality emerged out of a conservative corporate culture that stretched back to at least the late nineteenth century. There had long been unwillingness on the part of Canadian businessmen to believe in the global appeal of their products, beyond natural resources. This collective corporate culture led brewers to be derivative, first in copying and selling American brands at home, and then by diversifying into unrelated businesses within Canada or the United States, rather than concentrating their efforts on taking their principal business overseas. Consequently, Labatt diversified into media and entertainment, food businesses, dairy products, fruit juices, chemicals and retailing.[68] These diversifications did not bring the anticipated profits. The large dairy operations and packaged foods, for example, brought in revenues that showed only a thin margin of profit. Milk and the products made from it could not be marked up in price with the same ease as beer. As a consequence, whereas Labatt's brewing division returned a profit of $218 million in 1993, the dairy division, which had a book value of $140 million that year, showed no profit at all.[69] Like a number of Canadian companies, Labatt had diversified beyond what was optimal.

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[66] A. Chandler, *Scale and Scope*, p. 622.
[67] Lopes, *Global Brands*, p. 115.
[68] *John Labatt Annual Report*, (1987), pp. 9-11
[69] Albert Tucker, "Labatt's: A History – From Immigrant Family to Canadian Corporation" (unpublished manuscript), p. 431.

It was a similar story at Molson. Under the leadership of Mickey Cohen, a cultured corporate lawyer who had become Molson's president and CEO in 1988, Molson diversified into chemicals and the home improvement sector, spending hundreds of millions to purchase Beaver Lumber, a 45.1% interest in the Quebec-based Réno-Dépôt Inc. chain, and a 25% stake in Home Depot. The diversifications were as disastrous for Molson as they had been for Labatt.[70] If Molson had diversified into spirits, wines or even soft drinks there would have been at least the potential to exploit physical and knowledge linkages as well as to foster economies of scale and scope. But the firm chose instead to diversify into unrelated industries, where it had little expertise. For this, Molson paid a heavy price; not only in terms of its short-term financial results, but also in stripping it of the cash it might have used to promote its core business overseas.[71]

More important to the success of firms in the global alcoholic beverage industry than product diversification is geographic diversification. Indeed, some of today's most successful multinationals in the alcoholic beverage industry only briefly diversified out of alcohol. For example, even at the height of the diversification mania in the 1970s, Heineken still derived close to ninety per cent of its total sales from the sale of its alcoholic beverages.[72] It appeared that the business theorists of the post-diversification craze were right: the wisest strategy for big business was to "stick to the knitting." The mentality of the global age was to do what you do best, and do it the world over. As a result, firms in the alcoholic beverage sector intensified their efforts to expand into new markets. As the economist Charles Kindleberger succinctly put it, "in going abroad, they grow abroad."[73] Some firms had a "first-mover" advantage, which greatly benefited them in the long run. For example, Heineken and Guinness had long derived a substantial percentage of their sales from outside their home continent.[74] Initially they did this through exports, then by entering into licensing agreements with foreign firms and then by way of foreign direct investments. As a result, by 1990, forty percent of Guinness's total sales and twenty-five percent of Heineken's came from outside of Europe.

This was not the case in Canada however. Canadian brewers had never established a significant presence outside of the continent. Indeed, as late 1990, fully ninety-nine percent of Canada's beer exports went to the United States,

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70 Tucker, "Labatt's", p. 431.

71 Molson's financial results were mediocre at best in the early 1990s. Sales rose from \$2.55 billion in fiscal 1990 to \$3.09 billion in fiscal 1993, but earnings vacillated from \$117.9 million in fiscal 1990 to a net loss of \$38.67 million the following year, before rebounding somewhat to \$164.69 million in fiscal 1993.

72 Lopes, *Global Brands*, pp. 242-243.

73 Kindleberger, *American Business Abroad*, p. 6.

74 Lopes, *Global Brands*, pp. 242-243.

representing only ten percent of total beer production.[75] There had been some earlier, but generally unsuccessful, attempts at geographical diversification through mergers and acquisitions. For example, in 1987, Labatt launched Labatt Lager (Blue Light under a foreign guise) in England by way of a licensing agreement with the regional brewery Greenall Whitley. Not content to let others manage the brand, Labatt soon began pouring resources into the United Kingdom, a market that quickly proved to be far different from the cozy Canadian oligopoly to which it was accustomed. Its initial £6.5 million advertising campaign for Labatt Lager was a series of television commercials starring a red-coated character named Malcolm the Mountie. The campaign, which ran during most of the brewers push in Britain, boasted the tag line: "Malcolm the Mountie always gets his can." The campaign served to anger Canada's national police force more than win over beer drinkers in Britain. In 1991, Labatt Lager ranked a lowly number nine among lager brands in Britain.

When George Taylor took over as CEO of Labatt in 1992, he was determined to control more of the North American market. In 1994 he made his intentions clear when Labatt paid $720 million for a twenty-two percent stake in Mexican brewer FEMSA Cerveza SA. This was not a plan to slowly break into a foreign market, as was the case in the United Kingdom. FEMSA controlled 48% of the Mexican market, which was twice the size of Canada's. FEMSA's largest brewery at the time produced six million hectolitres of beer annually (or about 220 million cases of beer), triple the amount produced in Labatt's largest Canadian brewery.

Mexico also represented an opportunity for brewers in North America. Lucrative as it was, stagnant population growth and an aging population made the Canadian business a zero-sum game of expensive market share swaps and no growth. Once Labatt had mastered domestic quality control and marketing, the main challenge for senior management was to invest the resulting stream of earnings. In an absence of serious, competitive price wars, the structured and regulated domestic brewing business was a powerful engine that made substantial amounts of capital available for acquisitions. The strategic logic of the purchase in Mexico made sense given its size, proximity and demographics. Furthermore, like Canada it was a government-protected duopoly, with FEMSA and Groupo Modelo, the brewer of Corona, controlling the market.

Perhaps if the timing had been right, Labatt would have made money in Mexico. But, unfortunately for Labatt, the timing could not have been worse. Just a few months after the Canadian brewer paid out almost three-quarters of a billion dollars for FEMSA a currency crisis stuck the Latin nation. In December the peso began a free fall as two political assassinations, a guerrilla insurgency in

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[75] Ed Gregory, Wendy Hurst and Thomas Gussman, *Alcoholic Beverage Taxation and Control Policies*, (Ottawa, Brewers' Association of Canada, 1997), p. 75.

southern Mexico and a change of government led foreign investors to pull billions out of the country. And while U.S. officials and powerful media outlets like the *New York Times* told people that the currency crisis "does not reflect fundamental flaws in Mexico's newly liberalized economy"[76], the peso continued to fall. By 10 March 1995, the Mexican peso was worth only half of what it was when the financial crisis began in mid-December.

The usually conservative Canadian brewer had not hedged its Mexican purchase against a possible devaluation of the peso and as a result the firm lost heavily. On the day that the peso hit a new record low, Labatt president George Taylor conceded that "there is no question whatsoever that the devaluation is a significant setback for the company."[77] Just nine months after buying its stake, Labatt was forced to write down the carrying value of its FEMSA holding by $272 million and expected a further $110 million reduction in the investment's carrying value.[78] The market was tremendously bearish about the prospect of turning a profit in Mexico in the near future. "You can't be positive about it," stated Jacques Kavaflan, an analyst with Lévesque Beaubien Geoffrion Inc. in Montreal. "There's not going to be an earnings contribution from Mexico until the end of the century…"[79]

The Mexico fiasco brought an abrupt end to Labatt's global aspirations. Still, at home beer sales were still strong. Labatt Blue and Budweiser were selling particularly well in Canada and, as a result, Labatt's share of the domestic beer market increased from 44.2% in 1993 to 45% in 1994.[80] The company continued to turn a healthy profit, making it an attractive target for those multinational enterprises in the industry looking to further diversify geographically.

As the mega breweries raced to tap into China and other emerging markets, they simultaneously sought to acquire existing breweries in established markets, rationalizing their operations. The goal was to upgrade and enhance the marketing of local and regional brands while concomitantly introducing their "global brands" in some markets. The approach was pioneered by Belgium's Interbrew SA, which had been making beer in Europe since 1366.[81] In 1995, the debt-free family-controlled company was Europe's fourth-largest brewer, with sales of more than $2 billion. In the early 1990s, Interbrew began gobbling up breweries in emerging markets such as Romania and southern China. At the same time it began to eye the $30-billion North American beer market. But

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[76] "Mexico: Don't Panic Over the Peso", *New York Times* (29 December 1994),
[77] Mariana Strauss, "Labatt Caught in Peso Plunge", *Globe and Mail* (10 March 1995), p. B1.
[78] *Ibid*.
[79] *Ibid*, p. B2
[80] *Ibid*, p. B2
[81] Schumacher, H. (2002) 'The Global Beer Industry 2001 Review: Toto, We Are Not in Kansas Anymore', *Modern Beverage Age,* vol. 36, no. 5, pp. 7-9.

Interbrew's big brands, beers such as Stella Artois and Jupiler, were virtually unknown to North American beer drinkers. And after exhaustive study, Interbrew's executives decided that it was impossible to penetrate that highly competitive, mature market through exports alone. Thus in April 1995 Interbrew offered to acquired Labatt for $2.7 billion or $28.50 per share. Once the deal had been approved by the shareholders, Interbrew quickly set Labatt on a course to get "back to basics." As Interbrew's Belgium-based spokesman Gerard Fauchey noted: "It's very simple. We're brewers, not managers of hockey or baseball teams or television stations."[82]

The acquisition of Labatt by Interbrew left Molson as the biggest Canadian-owned brewer. Having acquired Carling O'Keefe a few years earlier, in 1995 Molson had a 46.5% share of the $10 billion Canadian beer market. Nevertheless, in international terms Molson was small. "It may look like a giant in Canada," wrote one beer industry analyst, "but when it crosses the border it looks more like Tom Thumb."[83] To make matters worse, Molson's own brands were losing their grip on the Canadian consumer. Admittedly, Molson wasn't the only Canadian brewer to suffer declining sales at home. Sleeman, Canada's third largest brewer, had seen its share of the market decline over the last decade. This was a result of two factors: the microbrewery revolution, which had been underway since the mid-1980s and, the rise in imported beer, particularly from the Netherlands, the United States and Mexico.[84]

In a belated effort to gain a presence outside of North America, in March 2002 Molson took the audacious step of paying $1.1 billion to acquire Cervejarias Kaiser SA, Brazil's second largest brewer. Molson had already missed its chance of become a autonomous global player. While its conservative corporate culture had served it well domestically, it had held it back internationally. A "fast follower" at home, Molson was simply a follower on the global stage. Still the purchase of Kaiser was risky move into what was at the time the world's fifth largest beer market. The deal gave Molson 17.8% of the South American country's beer sales, when combined with Bavaria, which Molson had purchased from Ambev two years earlier.

But the deal was marred from the start. The key to success in Brazil, as in other emerging markets, was to have a strong distribution system. This led a number of the leading multinationals in the global alcoholic beverage industry to form joint ventures with local partners to produce, bottle and distribute locally. Molson's Canadian counterpart in the alcoholic beverage industry, Seagram, understood the value of forming alliances to distribute its distiller spirits worldwide. In 1972, it formed one of the world first joint ventures in Asia with

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[82] *Maclean's*, 19 June 1995

[83] Peter Reid, *Modern Brewery Age*, (13 September 2004)

[84] Carlo Rupnik, "Canada's Beer Trade" A Swing to Imported Brands", Statistics Canada, *Analytical Paper* (February 2006), p. 14.

the Japanese brewer Kirin. Seagram brought its manufacturing technique while Kirin contributed its sales network and market knowledge to sell Seagram's brands Robert Brown, Dunbar, Emblem, Burnett's Gin and Nikolai vodka in Japan.[85] But unlike Seagram, Molson arrogantly chose to go it alone. To make matters worse, the company did not integrate vertically through wholly owned distribution units. Rather the firm relied on sixteen coca-cola bottlers to distribute its beer to the country's more than one million points of sale. Molson lacked market knowledge: a situation not helped by the fact that the man appointed to oversee Molson's Brazilian operations brewery was a financier who had never lived outside of Quebec and who didn't speak Portuguese. In 2004, Kaiser's market share was down to 11 per cent. Just two years after the purchase Molson sold its ill-fated billion dollar Brazilian brewery for a mere $108 million. Just a few months after the sale of Kaiser, Molson merged with Colorado's Adolph Coors Company.

Conclusion

So why is it that Canadian beer brands and brewers do not have a global presence, and why is it that Canada's oldest and largest beer companies no longer exist as autonomous agents? The answer to that question lies in the interwoven layers of industry-specific, country-specific and firm-specific determinants of growth and survival.

In the period before the gale winds of globalization gained full force, it was possible for the big three Canadian beer companies to grow and survive without constantly rebuilding their firm-specific advantages. This was due to the fact that industry-specific and country-specific determinants were not adverse for those firms within the brewing industry, like Molson, Labatt and Carling-O'Keefe, which lacked significant international activity. This was a period when brewing was a relatively unconsolidated and fundamentally local industry. Added to which, consumption patterns of beer were primarily specific to the regional culture in which the beer was being sold. The period was also one in which the regulatory regime in Canada protected the big three brewers from foreign competition, allowing them to survive despite not having firm-specific advantages relative to their international counterparts. The regulatory regime in Canada was such that it fragmented the industry along regional lines, leading to cost inefficiencies and suboptimal production levels that hampered the development of large, internationally competitive firms. Safe behind the tariff wall, Canadian brewers had little incentive to internationalize through foreign direct investment. Rather they spent millions of dollars a year on national advertising campaigns in an effort to gain a larger share of the domestic market.

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[85] Lopes, Global Brands, p. 99.

The doppelganger of federal and provincial legislation protected existing firms and enabled them to survive without developing managerial capabilities, marketing skills and global brands. When the protective trade barriers were dismantled in the mid-1990s Canadian breweries were forced to compete on an even playing field.

When one reflects on the firm-specific strategies of the big three brewers in Canada since 1960, one is reminded of Adam Smith's scorn for the feudal lords who traded their leadership for a pair of silver buckles. The principal decisions made by executives at the big three were myopic, in that they were aimed at maximizing short-term profits rather than promoting longer-term growth and survival. Instead of manufacturing, marketing and developing their own brands, they decided to manufacture the brands of their foreign competitors and to promote them within the national boundary. While lucrative in the short-term, the move served to cannibalize the sales of their existing brands. More damaging to their future survival, was the fact that the strategy served to strip Canadian beer of its "Canadian-ness." By choosing first to brew American styled-beers, and promote and package them in an American way, and then by licensing the right to brew popular American brands, Canadian brewers Americanized the Canadian brewing industry. At the same time that they were derivative in terms of their marketing, they were derivative in terms of their diversification strategy. As a consequence, when the brewing industry became truly global after 1990, Canadian brewers no longer had unique, distinctively Canadian brands to offer the world.

One might argue that the brewers were just responding to a consumer demand; that Canadians wanted American-style beers, and thus the big three brewers sensibly supplied them. To a certain degree the assertion has an element of truth. In the 1980s a thirst for differently styled beers existed, in part because the institutional environment stifled innovation at Canada's big breweries. This lack of ingenuity on the part of the big three led to the microbrewery revolution. But one must remember that between 1960 and 1990 the big three brewers controlled between ninety-six and ninety-eight percent of the market. What did they have to gain by such a move? The answer is: a slightly larger share of the domestic market. And that is the point. The Canadian brewing industry was emblematic of the Canadian corporate condition: an inability on the part of all but the most dynamic of Canadian corporations to look beyond the national boundary for opportunities for growth.