2. Corporate strategy in the UK vehicle components industry: a comparison of Lucas Industries and GKN

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The stories of how Lucas Industries and GKN responded to the changing economic environment during the years of industrial decline in the UK is one of the classic cases of business strategy. Lucas Industries and GKN, manufacturers of automotive and aerospace industry components, were, in their heyday, two of the UK's largest listed industrial companies. Yet, while GKN managed successfully to negotiate the rapidly changing economic and industrial scene of the 1980s–1990s, Lucas Industries struggled to adapt and was eventually forced to merge with the North American Varity Corporation, in what many commentators regarded as effectively a takeover.

This classic comparative case study is an opportunity to apply key concepts from the positioning and resource-based views of business strategy in developing a case analysis.

Guidance on how to write a case analysis can be found in Chapter 1, 'Business cases: what are they, why do we use them and how should you go about doing a case analysis?'.

Introduction

In 1980, Lucas Industries and GKN were two of the biggest manufacturers of vehicle components in the UK. Although both companies had other businesses, vehicle components represented the largest part of their turnover – about 80 per cent in the case of Lucas, 50 per cent for GKN. Both companies, especially Lucas, were also substantially reliant on UK-based vehicle assemblers, principally British Leyland, Ford and General Motors (Vauxhall). During the 1970s this had become an increasingly precarious customer base, following the near-collapse of British Leyland in 1974 and the decision by the

How to cite this book chapter:

Owen, Geoffrey (2025) 'Corporate strategy in the UK vehicle components industry: a comparison of Lucas Industries and GKN', in: Sallai, Dorottya and Pepper, Alexander (ed) *Navigating the 21st Century Business World: Case Studies in Management*, London: LSE Press, pp. 17–38. https://doi.org/10.31389/lsepress.nbw.b

two American-owned assemblers to concentrate most of their new investment in continental Europe.

Thus, Lucas and GKN were faced at the start of the 1980s with two strategic issues. One was how to strengthen their position in the world vehicle components industry, which was then in the early stages of a shift from a nationally based structure (national component makers supplying national vehicle assemblers) to global sourcing. The world's leading car and truck manufacturers were beginning to restrict their component purchases to suppliers that were capable of meeting their needs throughout the world, and to delegate to them a larger responsibility for complete systems or subsystems, rather than discrete components.

To keep pace with these developments, Lucas and GKN needed to ensure that their products were competitive in cost, quality and technology, and to establish manufacturing facilities in the world's major vehicle-producing regions – continental Europe, North America and the Far East – whether through direct investment, acquisitions, joint ventures or licensing arrangements.

The second strategic issue was to decide whether, and, if so, to what extent, they should build up non-automotive businesses to offset their dependence on the motor industry. If they chose to diversify, should they focus on activities which had some sort of 'synergy' with vehicle components, or should they go for entirely different industries?

Resolving these issues became more pressing as a result of the severe UK recession of 1980–1981, when both GKN and Lucas made losses (Table 2.1) and their survival as independent companies looked in doubt. The two companies dealt with their problems in different ways, and the outcome at the end of the 1990s was that Lucas had disappeared as an independent company (although several of its businesses survived under different ownership), while GKN seemed well placed to maintain its position both in vehicle components and in the other sector – aerospace – into which it had diversified.

This section describes the strategic decisions taken by the two companies during the 1980s and 1990s, and considers the implications of their experience for theories of strategy. A chronology of the main events is set out in the Exhibits section.

Table 2.1: Pre-tax profits at Lucas Industries and GKN 1979–1995 (figures in £m)

Lucas			GKN		
	£m			£m	
1979–80	41		1979	126	
1980–81	(21)	loss	1980	(1.2)	loss
1981–82	20		1981	35	
1982–83	2		1982	41	
1983–84	33		1983	88	
1984–85	58		1984	120	
1985–86	95		1985	133	
1986–87	115		1986	132	
1987–88	146		1987	147	
1988–89	187		1988	178	
1989–90	191		1989	215	
1990–91	84		1990	172	
1991–92	23		1991	95	
1992–93	50		1992	122	
1993–94	(130)	loss	1993	98	
1994–95	30		1994	200	
1995–96	180	*	1995	322	

* In 1996 Lucas merged with Varity of the US to become LucasVarity
Source: Company annual reports

Lucas Industries

Origins and early growth

The original Lucas business was founded in Birmingham in 1872 by Joseph Lucas, an apprenticed silversmith, to make pressed metal goods, including ship, coach and carriage lamps; he later became a leading supplier of lamps and other components to the bicycle industry. The company went public in 1897, but the Lucas family continued to play a large role in the management. The founder's son, Harry, was chair from 1902 to 1918, and his grandson, Oliver, served as joint managing director and deputy chair in the inter-war years.[1]

With the growth of car production after the turn of the 20th century, Lucas turned its attention to vehicle components, and established a close

relationship with some of the emerging car manufacturers, notably William Morris in Oxford. In addition to lighting, the company made a wide range of other mechanical and electrical components. The range was extended at the start of the First World War to include magnetos (a type of electrical generator). Supplies of this device, an essential component both for motor vehicles and for aircraft, had hitherto come almost entirely from a German company, Robert Bosch, whose founder had invented the magneto in 1886; the British government urgently needed a domestic supplier for military purposes. Lucas took over Thomson-Bennett, a small Birmingham firm which made a copy of the original Bosch magneto and transferred production to its main factory at Great King Street in Birmingham. This transaction also gave Lucas a foothold in the aircraft industry, which became an important customer during the war.

The inter-war years saw considerable growth in UK car and truck production, as well as an increase in the number of electrically operated components, including electric starters, electric horns and electric windscreen wipers. The vehicle assemblers bought most of their components from outside suppliers, and Lucas became the leading manufacturer in its field. This was achieved partly by buying out its competitors. In the mid-1920s Lucas acquired its two main rivals in electrical components, C.A. Vandervell (later CAV) and Rotax, and by the end of the decade it had a virtual monopoly in starting, lighting and ignition equipment.[2]

Lucas also protected its position in the UK through market-sharing agreements with its overseas counterparts. In the case of Bosch, a wide-ranging agreement was concluded in 1931, which barred Bosch from selling electrical equipment in Britain and British Overseas Territories, while Lucas stayed out of Germany. This arrangement provided for the creation of a jointly owned company, CAV-Bosch, to make diesel engine fuel injection equipment to Bosch's design. This was a time when manufacturers of commercial vehicles and farm tractors were beginning to switch from petrol to diesel engines, and CAV was to become one of the world leaders in this field. Lucas bought out Bosch's interest in the joint company in 1937 and acquired full control on the outbreak of the Second World War.

A similar agreement was made with Auto-Lite, one of the leading American suppliers of electrical components (later acquired by Ford). This involved the supply of technical know-how to Lucas as well as an agreement to stay out of each other's territory. Lucas had a close link with another American company, Bendix, which made brakes as well as electrical equipment. Lucas made Bendix starters under licence, and in 1932 it bought a majority stake in Bendix's UK brake factory. This side of Lucas' business was enlarged 10 years later with the acquisition of Girling, a leading British-owned brake manufacturer.

Much of Lucas' technology came from its foreign partners. Its forte was production engineering, not innovation. According to one account, Lucas 'copied the designs of others, principally American, German and sometimes French competition, most often under licence, but sometimes by skilful adaptation in a way that made the design amenable to large batch, flow-line production

methods.'[3] Lucas' senior executives, notably Oliver Lucas, were enthusiastic admirers of US management, and used an American consulting firm, Bedaux, to reorganise the Great King Street factory in the 1930s.

The Second World War, like the first, brought a big expansion of Lucas' business, especially in aircraft components. Some of the company's standard automotive products were adapted for military use, and Lucas made a variety of other war-related equipment, including gun turrets, aircraft wing sections, fuses and bombs. Rotax, now focused almost entirely on the aircraft industry, made magnetos for Rolls-Royce Merlin engines, the start of a long association with the leading British aero-engine builder.

Post-war prosperity

At the end of the Second World War, Lucas had some 40,000 employees and was one of the largest engineering groups in Britain. With the death of Oliver Lucas in 1948, the founding family was no longer directly involved in the management, but the family tradition lived on in a paternalistic approach to employees. Bertram Waring, chair from 1951 to 1969, was steeped in the Lucas culture. He had joined the company as an accountant in 1922 and later served as personal assistant to Oliver Lucas.

For the first 20 years after the war, Lucas enjoyed steady growth in sales and profits. There were no new entrants to disturb its monopoly, and, although most of the pre-war cartels had been dissolved, informal market-sharing arrangements tended to preserve national markets for national suppliers.

The heart of the business was the Lucas Electrical Company, accounting for some 75 per cent of the UK market for automotive electrical components. This subsidiary saw some important technical changes, including the replacement of the dynamo by the alternator, and, in the 1960s, the introduction of electronics into ignition systems and other products. Lucas, now committing more resources to research and development (a central laboratory was set up in 1957), was one of the first British companies to make a sizeable commitment to semiconductors and integrated circuits.

CAV, making diesel fuel injection equipment, continued to benefit from the shift from petrol to diesel by the commercial vehicle manufacturers, and the scale of production increased considerably after the war. One of the biggest investments was a new factory at Sudbury, Suffolk, to make fuel injectors. Described as 'unsurpassed in the world for making small, very high-precision components', this plant was producing some 450,000 injectors a month by the mid-1970s, and exporting 70 per cent of its output.[4] As before the war, acquisitions played a part in the growth of this business. Lucas bought Bryce Berger from Hawker Siddeley in 1960, and eight years later acquired Simms, its last remaining competitor in diesel fuel injection equipment. The takeover was partly prompted by the fear that Simms might have been sold to Bosch.

The other big automotive subsidiary, Girling, strengthened its position in the UK with the development of disc brakes, and began to win business

elsewhere in Europe. A factory was built at Koblenz, Germany, in 1961 to supply Ford and Daimler-Benz, despite strenuous opposition from Teves, the leading German brake manufacturer. A few years later a similar facility was built in France to supply Peugeot.

The aircraft components business, dependent on the unpredictable demands of the UK Ministry of Defence, was more volatile. The cancellation of the TSR-2 in 1965 and the bankruptcy of Rolls-Royce in 1971 forced Lucas to make sizeable write-offs and redundancies. Yet it continued to add to its interests in this field, and Lucas was seen by the Labour government of 1964–1969 as a suitable rationaliser of a fragmented sector; with the help of a £3m loan from the Industrial Reorganisation Corporation, it bought English Electric's aircraft component businesses. However, in the mid-1970s, Lucas Aerospace, as the division was now called, was making a negligible contribution to profits (Table 2.2).

Table 2.2: Lucas Industries in 1975: divisions' sales and surplus

	Sales (£m)	Trading surplus (£m)
Vehicle components	455	35
Aircraft equipment	71	0.9
Industrial products	43	2.5

Source: Lucas 1975 annual report

The 1970s slowdown

In 1972 Lucas was judged by the French business magazine, *L'Expansion*, to be the most dynamic company in Europe, as measured by growth in sales and profits. But the business outlook in the UK was darkening. The principal worry was the poor performance of the British motor industry. British Leyland, one of Lucas' biggest customers, was in the throes of what turned out to be a terminal decline – it was saved from bankruptcy by the government in 1974 – and car production in the UK was stagnating. Output reached a peak of 1.9m vehicles in 1972, only marginally higher than 10 years earlier; over the same period French production had doubled, from 1.4m to 2.9m, while German production had risen from 2.7m to 3.6m units. Car imports were rising rapidly, and international component suppliers, both European and Japanese, were setting up plants in the UK. It was clear that Lucas had to make itself less dependent on the domestic market.

Like most British engineering firms, Lucas had traditionally derived the bulk of its business from the UK and the Empire. However, the growth of car production in Europe during the 1950s, together with the formation of the Common Market at the end of the decade, prompted moves to establish

a European presence. Waring set up a committee at the end of the 1950s to study the European market, and this led to a joint venture in France to make fuel injection equipment, followed by the Girling factories in Germany and France. However, the internationalisation of Lucas Electrical, the largest part of the group, was more problematic.

Lucas had a long-standing association with Ducellier, the leading French supplier of electrical components, which was partly controlled by Bendix. This arrangement was extended in 1962 when Lucas bought a 40 per cent stake in the French company. Bernard Scott, who became chair of Lucas in 1974, was keen to go further, and in 1977 the Lucas shareholding in Ducellier was increased to 49 per cent. Scott then opened negotiations with Bendix to acquire the remaining 51 per cent.

The idea was that a Lucas-Ducellier combination could be the nucleus for a powerful European electrical components group (which might include other firms, such as Marelli in Italy, at a later stage), and act as a counterweight to Bosch. Unexpectedly, this plan ran into opposition from the French government, which wanted a greater degree of national ownership in the vehicle components sector. Bendix was persuaded to sell its Ducellier shares to a French component manufacturer, Societe Francaise du Ferodo (SFF), which later became part of the Valeo group. The new shareholding structure was Lucas with 50 per cent and SFF with 48 per cent, with 2 per cent held by a French bank.

In the US, Lucas had some export business in the early 1970s, but no manufacturing operations. The first move towards a stronger US presence came in 1977, when it opened a plant in South Carolina to make fuel injection equipment for diesel engines. This was to serve the needs of a large British customer, Perkins Engines, which had started to manufacture diesel engines in the US. However, a bigger opportunity for fuel injection equipment soon materialised. This was a time of growing concern in the US about fuel economy, and some companies, notably General Motors (GM), believed that diesel-powered cars would take an increasing share of the market. In 1977 the American company began talking to Lucas about a device known as a microjector, a fuel injection device for diesel cars which Lucas had developed some years earlier. This led to a firm order, and the indications were that GM would need 1.36m microinjectors a year for five years from 1979. The South Carolina plant was expanded to meet this demand.

Thus, by the end of the 1970s an international strategy for vehicle components was beginning to take shape, but Lucas was still dependent on the UK both as a manufacturing base and as a market. The fragility of this situation was exposed by the recession of the early 1980s. Pre-tax profits, which had reached a peak of £77m in 1976–1977, fell to £41m in the following year, and 1980–1981 saw the first loss in the company's history.

The 1980s shock

The recession coincided with a change of management at the top. Godfrey Messervy took over as chair and chief executive from Bernard Scott in 1980. The new chair, like Scott, had spent his entire career with Lucas, and he stood for continuity rather than radical change. He delegated a good deal of authority to two joint managing directors, Tony Gill and Jeffrey Wilkinson, who were given responsibility for different parts of the business – Gill for Girling, CAV and Aerospace, Wilkinson for Lucas Electrical and its associated subsidiaries, Lucas World Service and the industrial division. This division of roles was to cause a good deal of friction.

The immediate response to the crisis was a drastic programme of cost reduction in the UK factories, coupled with renewed efforts to build up sales in Europe and the US. Looking further ahead, the plan was to develop a new source of profit in what was called the Industrial Products division – a collection of industrial businesses which had come into the group through acquisition and were seen as a 'third leg', diluting Lucas' dependence on the automotive and aircraft industries. The goal was to reduce the proportion of sales coming from automotive components to no more than 60 per cent, with aerospace and industrial products each providing 20 per cent of the total.

The biggest loss-maker in the early 1980s was Lucas Electrical, which was more dependent on the UK than either CAV or Girling; less than 10 per cent of its production was exported. Several factories within this division were closed between 1980 and 1983, but the UK operations continued to make heavy losses. This increased the urgency of doing a deal with the French over Ducellier; the hope was that an integrated Lucas-Ducellier company would not only cement Lucas' links with the French motor industry, but also permit rationalisation between the French and British plants. However, the French authorities continued to obstruct any deal that gave Lucas majority control. In 1983, an outline agreement was reached whereby Ducellier would be divided between Lucas and Valeo, the former taking electronics, lighting and ignition, while the latter took starters and alternators. Lucas planned to build on this with other acquisitions and alliances. However, the agreement was never finalised. In 1984, Lucas disposed of its stake in Ducellier, acquiring in return a small shareholding in Valeo which was later sold.

As the Ducellier negotiations stalled, Messervy and Wilkinson looked for other ways of strengthening Lucas Electrical. This led to the decision to acquire control of the electrical instrumentation business of Smiths Industries. Smiths, originally a clock and watch manufacturer which had diversified into vehicle instruments before the war, had decided to opt out of this business. It had seen the need for heavy investment to acquire the electronics expertise which it lacked, and the deal with Lucas was a convenient exit route. For Lucas, the case for the deal was much more questionable. Messervy justified it on the grounds that the combined group would offer a complete range of electronic control systems and cut out duplication in research and product

development.[5] However, the effect was to make Lucas Electrical even more dependent on the UK.

Overseas, Lucas' fortunes in the early 1980s were mixed. Girling scored a notable success when it secured a contract from Ford in the US; a brake factory was set up in Cincinnati in 1982 to supply the American company. However, this was offset by a setback on the diesel injection side. By the end of 1981 it was clear that GM's projections for diesel-powered cars in the US had been too optimistic; there were also technical problems in converting the engine of one of its models, the Oldsmobile, from petrol to diesel. Orders from Lucas were sharply reduced, to the point where the South Carolina plant was no longer viable.

Meanwhile, in the UK the cost-cutting continued – employment in the UK fell by a third, from 70,000 to 47,000, between 1979 and 1983 – but, with the UK economy improving, Lucas gradually regained some financial flexibility. In 1985 it launched a £89m rights issue, the purpose of which was to finance acquisitions in the aerospace and industrial divisions. Lucas also took advantage of the surplus in its pension fund to take a pensions' 'holiday', suspending contributions to their pension scheme for two years. Pre-tax profits rose to £95m in 1985–1986, surpassing the previous peak in 1977.

Yet the underlying problems had not been solved. Lucas still had too many businesses, especially within Lucas Electrical, that were not internationally competitive. The aerospace division was too dependent on the UK, and on Rolls-Royce in particular; and diversification through what was now called Lucas Industrial Systems had been half-hearted and lacking in direction.

By this time, the leading figure in the company was Tony Gill, who became sole managing director in 1984 (Wilkinson had resigned after the collapse of the Ducellier negotiations). He succeeded Messervy as chair three years later. Gill was an engineer who had come into the group through the Bryce Berger acquisition in 1960, and, prior to his appointment as joint managing director, had been in charge of CAV.

1986–1996: the search for a defensible position

A more forceful personality than his predecessor, Gill saw that productivity in the UK was still too low, particularly in relation to the Japanese factories, which were now seen as the benchmark. An early decision was to introduce what were called 'Competitiveness Achievement Plans', measuring each plant against its best competitors and setting a clear timetable within which improvements were to be implemented. The programme was led by John Parnaby, an engineering academic who was hired in 1983 to be group director of manufacturing technology. Parnaby was well informed about Japanese manufacturing methods and sought to spread them around the group.

Gill also took a more radical line in streamlining the product portfolio. The termination of the Ducellier negotiations had removed any remaining chance that Lucas could be a major force in the European electrical equipment

market. Apart from electronics-based systems, Gill regarded most of the old Lucas Electrical as low-technology, commodity-type business which Lucas should get out of. In the second half of the 1980s several of these operations, including lighting, starters and batteries, were closed down, put into joint ventures or sold. Among the divestments were most of the instruments companies that had been bought from Smiths Industries in 1983.

The strongest of the automotive businesses were Girling and CAV, but even here there were some problems. Although Girling had a strong worldwide position in disc brakes, it had missed out on the trend towards fully electronic anti-lock brakes. It had developed its own electro-mechanical anti-lock braking system (ABS), which for a while looked the most likely contender for mass-produced cars, but the take-up of fully electronic systems came quicker than Girling had expected. By the end of the decade its main international competitors – Bosch, Teves and Bendix – were well ahead in ABS.

Meanwhile, Gill was determined to build up the non-automotive divisions, and this was the stated purpose of the £163m rights issue launched in 1988. In aerospace the aim was to reduce the group's dependence on Rolls-Royce by building a larger business in the US, principally through acquisition; some $300m was spent on buying American companies between 1985 and 1990. Ambitious targets were also set for the industrial division, now known as Lucas Applied Technology. The main focus was on measurement and control systems, but there was some uncertainty as to whether the role of this division was to be a completely separate profit centre or a provider of technology and other support to the automotive and aerospace businesses. There was also concern towards the end of the decade about whether the division's acquisition programme, mainly involving small and medium-sized companies, was absorbing money and management time that could be better used in Lucas' core activities.

Thus, at the start of the 1990s the strategic problems which had faced Lucas 10 years earlier had been only partially resolved. Automotive now accounted for only 59 per cent of total sales against 72 per cent in 1981, and the proportion of sales made in the UK had come down from 46 per cent to 32 per cent (Table 2.3). But there were still weaknesses on the automotive side, and, while the aerospace division was now more strongly placed, the return on the acquisitions that had been made in Applied Technology had been poor.

Hence Lucas was not well placed to withstand what turned out to be an exceptionally severe recession in the early 1990s; operating profits in vehicle components fell by more than half between 1990 and 1991. In September 1992, the share price fell to its lowest level for seven years, valuing the group at some £550m, less than half its pre-recession peak. To make matters worse, there was uncertainty over the succession to Gill; a new group managing director, Tony Edwards, who had been running the aerospace division, was appointed in February 1992, but he lost the confidence of the board and left the company eight months later.

Table 2.3: Lucas sales in 1981 and 1991 (per cent of total sales)

By destination		
	1981	**1991**
UK	46	32
Rest of Europe	29	38
North America	6	21
Rest of world	19	9

By sector		
	1981	**1991**
Automotive	72	59
Aerospace	19	30
Applied Technology	9	11

Source: Lucas 1992 Annual Report

Some of the non-executive directors believed that the right way forward for Lucas was to make a transforming acquisition which would radically alter the balance of the group, making it less dependent on automotive and aerospace. Several possible candidates were identified, including a large American manufacturer of process control equipment, a field in which Lucas already had some experience. Such a deal might also have solved the succession problem, since the chief executive of the target company seemed well qualified to take over as chief executive from Gill. However, the proposal was turned down by the board early in 1993.

The succession issue was eventually resolved by the appointment as chief executive of George Simpson, a well-regarded manager who was widely credited with reviving the Rover car company over the previous decade. He took up his post in April 1994 and Sir Brian Pearse, formerly head of Midland Bank, was brought in as non-executive chair.

Within a few months of his arrival, Simpson concluded that Lucas needed to go further and faster in focusing on its core activities, and in disposing of underperforming businesses. Several divestments and closures took place, the effect of which was to incur exceptional costs of over £200m in the 1993–1994 financial year. Most of these costs related to acquisitions that had been made over the previous five years. In 1995, the Applied Technology division was disbanded, with its residual operations transferred to other parts of the group. In that year the automotive content of group sales had gone back up to 75 per cent, and its share of profits was even higher.

By this time the recession was easing, but Simpson still had doubts as to whether Lucas could make it on its own. In his view, the world vehicle components industry would soon be consolidated in the hands of a small number

of 'super-integrators', serving vehicle manufacturers worldwide. These companies would either be broad integrators capable of providing a range of systems, such as Delphi in the US, Bosch in Europe and Nippondenso in Japan, or more specialised firms offering individual subsystems, such as Valeo in France. One option for Lucas was to join forces with one of the bigger groups. Another was to merge with, or acquire, a components company of comparable size.

While these options were being debated, the company was faced with an unexpected problem – that of the succession to George Simpson. Within a few months of his arrival at Lucas, Simpson had been approached by GEC (General Electric Company) as a possible successor to Lord Weinstock as managing director of that company; by the start of 1995 he had decided to accept the offer. The choice of successor then became a matter of urgency, and it was resolved in an unconventional way. This was a merger with Varity, a US-based engineering group whose businesses included Kelsey-Hayes, a leading US brake manufacturer.

Lucas had considered making an offer for Kelsey-Hayes when it had been put on the market some years earlier – it would have been a good fit with Girling – but had felt unable to match the price paid by Varity. Now a full-scale merger with Varity offered the prospect not only of strengthening Girling's position in the US, but also of solving the Lucas succession problem. The Varity chief executive, Victor Rice, was an obvious candidate to take over from Simpson and run the enlarged group.

The merger went through in May 1996. Rice became chief executive of the merged group, and most of the other key positions were filled by Varity executives. This led City commentators to complain that the deal had been a reverse takeover, not a merger, and that Varity had achieved this without paying a premium. The City was further upset in 1998, when Rice tried to shift the domicile of LucasVarity from the UK to the US; shareholders rejected this plan by a narrow majority.

In the following year, Victor Rice, apparently believing that the company was still not big enough, negotiated a merger between LucasVarity and another American components manufacturer, TRW. TRW subsequently sold the diesel injection business to Delphi, keeping brakes and electronic systems; the Lucas aerospace business was sold to Goodrich. Thus, although several of Lucas' businesses survived under different ownership, the original parent ceased to exist.

GKN

Origins and early development

In 1900, John Guest, whose family owned one of the largest iron and steel producers in South Wales, merged his business with a Birmingham manufacturer of nuts and bolts, controlled by Arthur Keen. Two years later the combined

group joined forces with another Midlands company, Nettlefolds, which made screws and fasteners. The three-way merger which created Guest, Keen & Nettlefolds was an early example of vertical integration between steelmaking and steel-using industries, and the new group was one of Britain's largest industrial companies, employing some 12,500 workers.

GKN continued to expand by merger and takeover before and after the First World War. Two of the biggest acquisitions were F.W. Cotterill, a rival manufacturer of nuts and bolts which also owned Garringtons, a drop-forging business, and, in 1920, John Lysaght, which made sheet steel. The latter included Sankey, which made wheels, chassis frames and body pressings for the motor industry. This industry became an important customer for other GKN companies in the inter-war period, but at this stage GKN was predominantly a supplier of semi-finished materials – forgings, castings and pressings – rather than the proprietary components in which Lucas specialised.

The strategy of vertical integration and growth by acquisition continued after 1945. The acquisitions included a number of vehicle component companies, starting with BRD, a manufacturer of propeller shafts in 1956. At the time of this purchase British Motor Corporation (BMC) was developing the Mini, a revolutionary small car which incorporated a front-wheel-drive design, and it was looking for a new type of drive shaft which would transmit torque from the engine to the wheels. BRD competed for the order, but the preferred supplier was Hardy Spicer, a subsidiary of the Birfield group, whose patented technology in constant velocity joints (CVJs) fitted BMC's requirements. Birfield became the sole supplier of CVJs for the Mini and for BMC's subsequent front-wheel-drive cars.

In 1966, GKN acquired Birfield, and this proved to be a hugely significant move. In addition to its special position in CVJs, Birfield had a 39.5 per cent stake in Uni-Cardan, a German company which had similar technology and supplied components to Volkswagen and other continental assemblers. GKN had traditionally been geared to Commonwealth markets, and the Uni-Cardan stake provided a European dimension which other British vehicle component makers (including Lucas) lacked.

GKN bought other British vehicle components businesses during the 1960s, including Vandervell Products, a manufacturer of engine bearings, and it was also diversifying in other directions. It entered the plastics industry, for example, both as a processor of plastic materials and as a manufacturer of plastics machinery. However, the heart of GKN remained steelmaking, and its raison d'etre was vertical integration; in the mid-1960s it was using 2.5m tons of steel a year, 12.5 per cent of UK steel production. That strategic core, which had dominated GKN since its creation, was removed in 1967 when the Labour Government nationalised the steel industry, and GKN had to look in new directions.

For the first few years after nationalisation the redirection of GKN proceeded in a halting and uncertain manner. Several acquisitions were made, mostly of engineering companies loosely linked to GKN's existing activities.

The acquired firms were allowed to continue as independent businesses, and there was no attempt to weld them into an integrated group. Moreover, the company's senior managers, most of whom had spent their working lives in the company, continued to regard themselves as steelmakers. One of the old GKN mills, at Brymbo in Wales, was bought back from the nationalised British Steel Corporation in 1973, and a new rod mill was built at Cardiff.

By the mid-1970s GKN had become an engineering conglomerate, with over 100,000 employees spread around a large number of mostly unrelated businesses, all competing for resources and management time. A sharp fall in profits in the second half of the decade prompted a reappraisal of policy, in which 'new men', less emotionally committed to GKN's heritage, played an important part. An influential figure was Trevor Holdsworth, an accountant who had joined the group in 1963, having previously worked for Bowater, the papermaker. Holdsworth climbed up the GKN ladder on the finance side, before becoming deputy chair of the group in 1974; he was appointed managing director in 1977 and chair in 1980.

Holdsworth's view of GKN in the mid-1970s, as set out in a subsequent speech, was that the company represented 'the quintessence of the British problem: a manufacturer of mature engineering products, largely a sub-contractor, predominantly in Britain with a large commitment to the troubled and reducing British motor industry. Its international involvement was based upon following the flag round the Commonwealth. Although we had adopted all the then fashionable techniques of corporate planning and every year produced large volumes of divisional and group plans, we were drifting uncertainly into the future without a clear strategy.'[6]

Out of this rethinking came a four-point plan: not to be a steel company (though GKN might still make steel on a small scale to support downstream operations); to build up the automotive components business; to dilute the dependence on the automotive market, and on manufacturing in general, by investing in wholesale distribution; and to invest internationally.

The choice of vehicle components as the main avenue for growth was logical. Many of the world's vehicle manufacturers, responding to the growing demand for small, fuel-efficient cars after the first oil crisis, were switching to front-wheel-drive and GKN was well placed to supply a key component, the CVJ. At the end of the 1970s, Ford in the US decided to buy CVJs from an outside supplier rather than make them in-house. As it was not prepared to rely on CVJs imported from Europe, Ford encouraged GKN to build a plant in the US. Thanks to this contract, together with the expansion of Uni-Cardan in continental Europe, GKN by the end of the 1970s was on the way to becoming an international vehicle component supplier. Additional shares in Uni-Cardan were acquired during this period, giving GKN majority control.

GKN was looking for growth in other sectors of the vehicle component business during this period. In 1979, it bought Sheepbridge Engineering, and its piston business was put together with Vandervell to form GKN Engine Parts Division. GKN also tried to buy Sachs, a German company whose principal

subsidiary, Fichtel and Sachs, was the leading German clutch manufacturer, but this was blocked by the German competition authorities.

The move into wholesale distribution was to be achieved largely by acquisition, and several companies were bought in the 1970s. In addition, GKN formed what proved to a profitable joint venture with Brambles, an Australian company which had built up a pallet-pooling operation in Australia. The partnership was called CHEP (the Commonwealth Handling Equipment Pool), and it was extended in 1981 to include Cleanaway, a waste management business.

Thus, by the end of the 1970s, GKN's situation was better than that of Lucas to the extent that its vehicle component business had become less dependent on the UK. However, it was still widely diversified, as a result of the unfocused acquisition policies of the preceding two decades. It had several 'heritage' businesses, such as nuts and bolts, which were either losing money or had little growth potential; the cartel arrangements which had protected these businesses in the past had broken down, and import competition was increasing. Moreover, apart from the joint venture with Brambles, most of the distribution businesses that had been acquired proved to be disappointing or worse. The group as a whole was not in good shape to withstand the recession of the early 1980s.

The Thatcher shock

As in the case of Lucas, the loss that GKN reported in the 1980–1981 financial year was a traumatic event and prompted a strenuous effort to cut costs; GKN's UK labour force dropped from 70,000 to less than 25,000 during the 1980s. However, the strategic redirection which took place in the first half of the decade was more comprehensive than at Lucas, and involved a sharper break with the past.

With Holdsworth and a few like-minded colleagues now firmly in charge – most of the 'old guard' had retired – drastic action was taken to clean up the portfolio. Many of the peripheral businesses, including the two original ones, nuts and bolts and fasteners, were sold and GKN rethought its approach to distribution. Holdsworth and his colleagues realised that what they had bought were mostly collections of small businesses, more suitable for ownership by an owner-entrepreneur than a big industrial group. A series of disposals left the Brambles joint venture as the main asset in what was now called the industrial services division, although the car aftermarket business was retained.

The 1980–1981 recession also underlined the urgency of getting out of steel. The first step came in 1981, when GKN's Cardiff-based wire and rod interests were pooled with those of the state-owned British Steel Corporation to form a separate company, Allied Steel and Wire; this company was later floated on the stock exchange. A similar deal, covering GKN's engineering steels, was agreed with British Steel in 1986; again, a new company was formed, United Engineering Steels (UES), with GKN retaining a minority interest.

Profits from vehicle components, especially Uni-Cardan, kept the group afloat in the early 1980s, and the prospects for the CVJ business looked good. However, Holdsworth believed that CVJs on their own were not enough to ensure GKN's survival in the vehicle components industry. To establish a broader base, GKN attempted in 1983 to enlarge its stake in engine components by making a takeover bid for AE (formerly Associated Engineering), the leading UK manufacturer of bearings, pistons and cylinder liners; the bid was blocked by the Monopolies Commission on competition grounds. Two years later, Holdsworth briefly pursued the idea of a merger with Lucas, but this did not find favour with the Lucas managers; they could see no benefit of linking their vehicle components business with what they saw as GKN's distinctly low-technology operations.

Arguably the failure to take over AE (and to merge with Lucas) was a fortunate outcome for GKN. The engine components sector was more competitive and more crowded than CVJs, and although the combination of GKN and AE would have yielded some scale economies, neither company was strong in continental Europe or the US. As it was, GKN was able to concentrate single-mindedly on CVJs, where it had a clear technical advantage. (GKN's engine components division was subsequently sold to another British components manufacturer, T & N.)

By the time of Holdsworth's retirement in 1988, GKN had been extensively reshaped and had made an impressive recovery since the slump in profits at the start of the decade. Although there was some tidying-up to be done – GKN still had a substantial stake in automotive parts distribution – the two main pillars of the group were now vehicle components (mainly CVJs) and industrial services (mainly the joint ventures with Brambles) (Table 2.4).

Table 2.4: GKN pre-tax profits by sector in 1987 (£m)

	£m
Automotive and defence	92
Industrial services	35
Automotive parts distribution	11
Related companies	38
Net interest	(29)
Total	147

1988–2002: specialisation plus opportunism

Holdsworth's successor as chair and chief executive was David Lees, who had previously been finance director. While the change at the top brought no immediate change in strategy, Lees believed that GKN had an opportunity

to develop a profitable 'third leg', which would be complementary to its two existing businesses.

GKN had a long history as a supplier to the Ministry of Defence, most recently as the manufacturer (through Sankey) of a fighting vehicle, the FV432. In 1985 GKN won a contract to build a new armoured personnel carrier, the Warrior. Lees believed that defence contracting could be expanded to the point where it made roughly the same profit contribution as vehicle components and industrial services.[7] He thought that GKN, with its expertise in light armoured vehicles, could capitalise on the trend within NATO towards mobile equipment suitable for a 'rapid reaction' strategy. This led him to consider the helicopter industry as a suitable area for diversification.

In 1988, GKN acquired a 29.9 per cent equity stake in Westland, the British helicopter manufacturer. (The shares were acquired from Fiat and Hanson, both of which had bought the shares during the Westland crisis of 1986.) Westland had a technical partnership with Sikorsky, the American helicopter maker; its parent, United Technologies, held an 8 per cent stake in Westland.

Lees made it clear at the time of this purchase that his ultimate aim was to acquire majority control, and that the helicopter company formed part of his plan to make GKN a major defence contractor; he wanted a position in army weapons systems akin to that of British Aerospace in air systems and Vickers Shipbuilding and Engineering in ships and submarines.[8] In 1994, United Technologies decided to sell its stake, and GKN used this opportunity to make an offer for the whole of the company.

At the time of the takeover, Westland was one of three competing European helicopter manufacturers in a market which was not big enough to sustain more than two; the others were Eurocopter (a partnership between Aerospatiale of France and MBB of Germany, and now part of EADS [European Aeronautic Defence and Space Company]) and Agusta of Italy. A logical step, since GKN and Agusta were already collaborating on a major European project, the EH101 military helicopter, was for these two companies to join forces. An agreement was reached to create a new company, AgustaWestland, which would be owned on 50-50 basis.

One of the attractions of Westland to GKN was that, in addition to helicopters, it had a separate business making aerospace structures and components for airframes and aero-engines. Following a trend which was already under way in the motor industry, the big aircraft manufacturers were beginning to delegate more responsibility to their suppliers, and Lees saw this as an opportunity for GKN to establish itself as a 'tier one' aerospace component supplier. An important step in this direction came in 2000, when GKN announced the acquisition of the fabrication operations of Boeing's Military Aircraft and Missile Systems Group.

Thus, by 2001 GKN's 'third leg' was substantially larger than it had been 10 years earlier, and different in composition. The armoured vehicles business was sold in 1998 to Alvis, another UK company which specialised in tanks and armoured personnel carriers; in return GKN obtained a 29.9 per cent stake

in Alvis. In 2001 GKN's aerospace division – consisting of aerospace services (structures, components and design services for aircraft and aero-engine manufacturers) and the joint venture with Agusta – reported an operating profit of £119m on sales of £1.5bn; this compared with profits of £187m in the automotive division, on sales of £2.8bn.

GKN continued to expand in CVJs, helped by the increasing popularity of four-wheel-drive vehicles which also relied on this component. Although this business was no longer protected by patents, GKN had a first-mover advantage which made it difficult for other component makers to catch up, and most of the vehicle assemblers, although they had the technical capacity to make CVJs in-house, were content to buy from GKN because of its advantages in scale, cost and technology. By the end of the 1990s GKN's share of the world CVJ market was just under 40 per cent.

There was still some debate within GKN as to whether the group should diversify into other parts of the vehicle components industry. One possibility was to merge with T & N, which had acquired AE in 1988 and had become a major world player in engine components. However, T & N had heavy financial liabilities arising from its previous involvement with asbestos, and this was a deterrent to any potential acquirer. Thus, GKN decided to concentrate on CVJs and on closely related products.

Its only major diversification within vehicle components, but outside CVJs, was in powder metallurgy, a process for making lightweight components more economically than could be achieved through conventional forging and machining methods. This was a fragmented sector, and GKN believed that through acquisitions and organic growth it could become the dominant player. GKN made two large acquisitions in the US, and by 2001 sales by the Powder Metallurgy division had reached some £600m – still small compared to the Automotive Driveline division (£1.8bn), but growing fast.

As for industrial services, growth continued in the 1980s, and at the end of the decade the important decision was taken to establish CHEP into the US. When it did so, there was no national pallet pool in existence, and a substantial investment was necessary to build a nationwide presence. By the end of 1992, CHEP USA had a pool of over 2m pallets operating from four regional centres and supported by a national network of over 130 depots.

David Lees remained chair and chief executive of GKN until 1997; in that year he became non-executive chair and was succeeded as chief executive by C.K. Chow. Under Lees' leadership GKN had concentrated on three areas – vehicle components, industrial services and aerospace (Table 2.5).

Table 2.5: GKN sales by business in 1997 (£m)

	£m
Automotive	2049
Industrial services	430
Aerospace and special vehicles	904

The final withdrawal from steelmaking had taken place in 1995, when GKN's stake in United Engineering Steels was sold to British Steel. In the same year, the sale of the US automotive aftermarket distribution business was announced. Lees described these transactions as the last in a series of divestments of strategically peripheral businesses, leaving GKN fully focused on its core activities. The cash raised by the divestments, he said, would not be used for diversification. 'The business strategy is to go deeper, not wider, and therefore the plan is to use the cash for bolt-on acquisitions rather than to expand into new businesses.'[9]

Over the next few years an important change took place in GKN's portfolio. The relationship between GKN and Brambles, though profitable to both partners, was complicated by the fact that the joint venture had become an increasingly important part of Brambles' business. CHEP was a big international company in its own right, and the 50-50 ownership, requiring both parents to agree on major decisions, was no longer an appropriate arrangement. As Lees commented later, 'Running a fast-moving growth business like CHEP in a joint venture was really putting pressure on the system and impacting on its efficiency.'[10] In 2001, the two companies agreed on a scheme whereby CHEP and Cleanaway would be demerged from GKN into Brambles, and GKN shareholders would acquire 43 per cent of the enlarged Brambles Group.

The outcome was to narrow GKN's portfolio to two legs – automotive and aerospace – both of which were seen as capable of profitable growth.

Preparing the case

In preparing the case analysis you might like to consider three specific questions in particular:

- Compare and contrast the ways in which Lucas Industries and GKN handled their vehicle component businesses, and how they handled their diversification outside vehicle components.
- What insights does the positioning approach to business strategy provide in the case of Lucas Industries and GKN?
- Is the resource-based theory of strategy relevant to this story?

Postscript

While GKN survived as independent company through the 1980s, 1990s and early part of the 21st century, it was eventually acquired in a hostile and highly controversial takeover by 2018 Melrose Industries, a relative upstart in the engineering industry which had been founded by corporate financiers David Roper, Christopher Miller and Simon Peckham in 2003. Melrose's business strategy was to buy and turn around underperforming businesses. In March 2023, Melrose announced its decision to demerge parts of the former GKN business into Dowlais Group plc, a pure-play automotive component supplier.

Following a series of disposals and the demerger of its automotive business, Melrose is now focused on the former GKN aerospace operation. Roper stood down as executive vice-chair of the industrial conglomerate in May 2020, leaving with shares worth £30m.[11] In March 2024, Miller and Peckham both stepped down from the board after more than two decades of dealmaking. They were the biggest beneficiaries of a £180m bonus pot declared prior to their departure.[12]

Further reading

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Exhibits

GKN chronology

1900–1902	Three-way merger creates Guest, Keen & Nettlefolds
1919	Acquires F.W. Cotterill
1920	Acquires John Lysaght
1948	Acquires Brymbo Steel Works
	Acquires 50 per cent stake in BRD (automotive components)
1955	Acquires Lincoln Electric (welding machinery)
	Acquires full control of BRD
1962	Acquires Acton Bolt (nuts and bolts)
1966	Acquires Birfield (vehicle components)
1967	Steel nationalisation
	Acquires Vandervell Products (vehicle components)
1969	Acquires R.H. Windsor (plastics machinery)
1973	Buys back Brymbo from British Steel Corporation

1974	Forms joint venture with Brambles in industrial services
1979	Acquires Sheepbridge Engineering (vehicle components)
1980	Trevor Holdsworth appointed chair
1983	Bids for Associated Engineering, rejected by Monopolies Commission
1987	David Lees appointed group managing director, succeeds Holdsworth as chair in the following year
1988	Acquires stake in Westland
1994	Acquires full control of Westland
1995	Sells minority stake in UES Holdings to British Steel
1996	Sells US automotive parts business
1997	Lees becomes non-executive chair, succeeded as Chief Executive by C.K. Chow
2001	Puts Westland into joint venture with Agusta
2001	Demerges industrial services business into Brambles

Lucas chronology

1872	Joseph Lucas founds the business in Birmingham
1897	Becomes a public company
1914	Acquires Thomson-Bennett, manufacturer of magnetos
1926	Acquires C.A. Vandervell (later known as CAV)
	Acquires Rotax
1929	Acquires Rist
1943	Acquires Girling (brakes)
1959	Forms joint venture with Ducellier in France to make fuel injection equipment
1960	Opens Girling factory in Germany
1962	Acquires 40 per cent stake in Ducellier
1977	Builds factory in the US for fuel injection equipment
1980	Godfrey Messervy appointed chair
1983	Buys control of Smiths Industries' instrumentation business
1984	Sells holding in Ducellier
1986	Sells starters and alternators to Magneti Marelli, lighting to Fausto Carello
1987	Tony Gill appointed chair and chief executive
1994	George Simpson succeeds Gill as chief executive, Brian Pearse appointed non-executive chair
1996	Merges with Varity to form LucasVarity
1999	LucasVarity acquired by TRW
	TRW sells CAV to Delphi
2001	TRW sells Lucas Aerospace to Goodrich
2002	Northrop Grumman announces plan to take over TRW, together with the sale of TRW's vehicle components business to the Blackstone group

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[5] *Financial Times*, 8 January, 1983.

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[7] *Financial Times*, 10 March, 1988.

[8] *Financial Times*, 4 October, 1988.

[9] *Financial Times*, 7 December, 1995.

[10] *Sunday Times*, 22 April, 2001.

[11] *The Times*, May 2019.

[12] *Financial Times*, 3 June, 2024.