

## **Should banks be nationalised?"**

**By Roger Lawson, of the UK Shareholders Association**

Should UK banks be nationalised? Bank nationalisation seems to be advocated by those who think it will solve the crisis in the UK's financial system by enabling the Government to influence lending policies, and recapitalise the banking system without the hindrance of shareholders. Emotionally, it relies on the feeling that banks have to be punished for past misdeeds by a cathartic solution which wipes the slate clean (and in the process of course wipes out the ordinary shareholders).

But this is not the only or even the best solution to the problems in the economy and the banking system. And such calls for nationalisation fatally undermine the whole investment and financial structure of the UK banking system.

Banks are not being inhibited from lending solely because they are short of cash. If they don't wish to lend to house buyers on low incomes to buy overpriced property in a falling housing market, this is simply prudence. Likewise, if they don't wish to lend to businesses that are facing liquidity problems when a recession is clearly upon us, who can blame them? If the Government wishes to lend taxpayers money to such businesses, for sound social or economic reasons, then they can do this in various ways. Indeed they already own two banks as a result of past nationalisations which could be used as channels for that purpose.

Alternatively they could channel funds to suitable recipients via the existing banks by the use of suitable loan structures – but they do not need to do this via equity injection which damages existing bank shareholders enormously. Other options which the Government are already pursuing are the provision of suitable loan guarantees, or insuring the risk of defaults on existing assets, so as to encourage more lending by commercial banks.

But UK banks have also been put under pressure by the withdrawal of funds from overseas depositors and lenders – to quote John Grout of the Association of Corporate Treasurers, “We see a lot of foreign banks going home with their ball” and that is partly a consequence of Government interest rate policy and partly a consequence of the threat of nationalisation. Nobody wants to lend money to or invest in a business that is at risk of being nationalised. We have a situation where the Governor of the Bank of England, and the Chairman of the Treasury Select Committee have publicly talked about nationalising whole swathes of the banking sector. It is also clear from the Government's actions on Northern Rock, and the wording of the new Banking Bill, that no compensation will be paid to ordinary shareholders in these companies if the Government does step in.

Share prices in the UK banks have been shot to piece, but not because the market fears any toxic debt or derivative overhang, but because they fear the dead hand of state interference.

If money needs to be provided to individual institutions it should be done at market rates, in exchange for proper security, not by the state acquiring an equity interest. As it is the Government is now perceived to be attempting to take over some or all of these businesses, in a wave of socialist motivated, stealth nationalisations. The resulting fall out from this has been a total lack of confidence to the point of blind panic, a collapse in share prices, resulting in hundreds of billions of pounds being lost by millions of citizens from their savings and

pension funds, and debasing the value of the underlying share collateral for any Government loans. By their own actions the Government is destroying the banking industry and bankrupting the taxpayer.

The funding that the Government is providing in the form of preference shares is usurious, unlike other countries who have gone for market rates. That gives us a clear message of intent to make a profit at the expense of shareholders, and betrays the contempt in which the Government and its leaders hold the savings and pensions of private shareholders.

Although shareholders in UK banks have stepped up to the plate and subscribed for rights issues in recent months, it would seem that the Government wants on deterring such investors by punitive actions. In effect, they have made UK banks “uninvestable” propositions for anyone who examines these issues. This does not just affect investment in equity, but also in bonds and other debt. Here is what Richard Thomson of Henderson Global Investors had to say in the Financial Times on this subject: “The bank capital debt market is frozen due to concerns over Government involvement. The lack of consistency in the treatment of bondholders in previous Government actions has led to the ability of market participants to become comfortable with the risks involved”.

Another problem with nationalisation is that the end result is that instead of the Government having specific limits on their liability, they end up responsible for the total liabilities of the bank, with additional complications concerning European Community rules on state support for businesses.

What are the other consequences of nationalisation (other than destroying shareholders wealth)? The result we have seen from all past nationalisations, which many people are now too young to remember, is not the creation of profitable, well managed businesses but of organisations that are run in the interest of social objectives. Often this seems to be more about preserving jobs and social lifestyles rather than facing new challenges or becoming more efficient – the result is unprofitable and declining businesses that can’t stand up to international or private competition. No, nationalisation would be a mistake, whether it’s short term or long term.

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