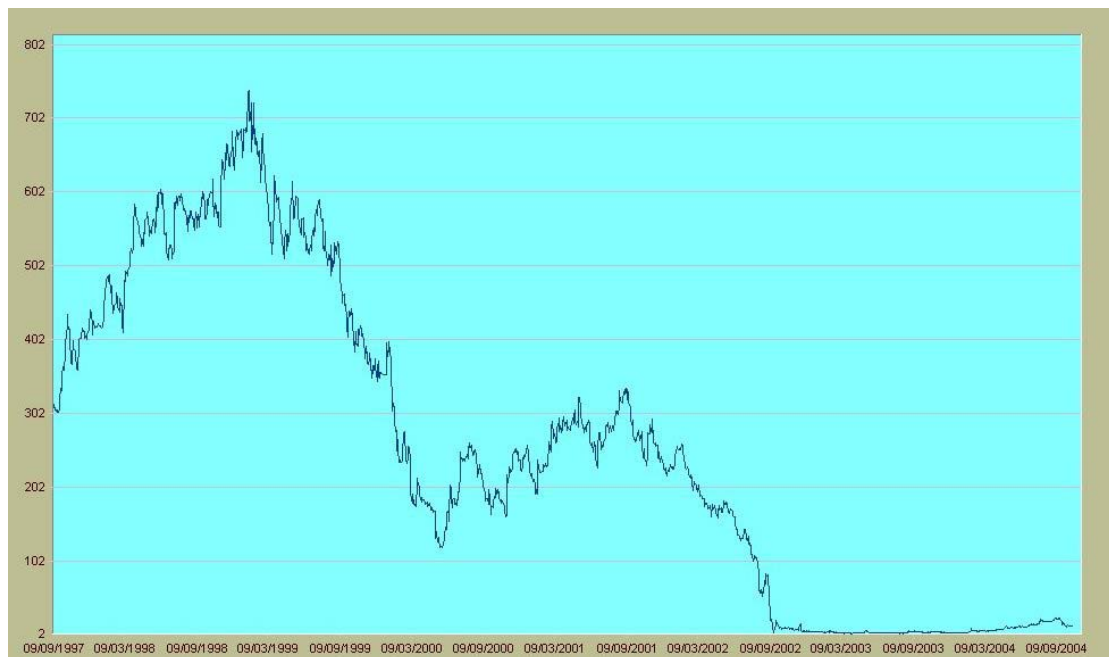


British Energy and the Lessons for Private Shareholders

Malcolm Stacey, a former BBC Radio Four presenter, lost £90,000 when British Energy came to a crisis in 2002. He was one of many private shareholders who effectively had most of their investment wiped out, including employees of the company who had bought shares. As the shares were originally sold as a "privatisation" issue, many unsophisticated private shareholders were also holding the stock.

Note that after the initial IPO of British Energy, the share price climbed from £3 to over £7, but has recently traded as low as 4p. The following chart shows the share price history.



British Energy Share Price 1997-2004

The difficulties of the company seemed to stem primarily from a fall in energy prices when the company was highly geared, both operationally and financially and vulnerable to charges in the market price of electricity. The restructuring proposed in 2004 means that ordinary shareholders will be left with only 2.5% of the company (although they get warrants to subscribe for another 5%). Creditors will own the rest, following a debt for equity swap.

Malcolm, with the co-operation and help of Polygon, a big UK hedge fund, and Brandes Investment Partners, formed an "Action Group" and they called an Extraordinary General Meeting to overturn the proposed restructuring. They argued that with the price of oil and gas now rocketing, British Energy would make huge profits in the future; and other restructuring plans were surely possible that would be fairer to ordinary shareholders. British Energy threatened legal action, and also threatened to put the company into administration (they said they would have no alternative as the company could not meet its obligations if the restructuring did not go through). They also delisted the shares immediately before the EGM which seemed an aggressive and unnecessary move by the company.

However at the EGM, there was a three to one vote in favour of the restructuring, and the threat of legal action, or the impracticality of pursuing their campaign, appeared to have encouraged Polygon and Brandes to drop their opposition and vote against their own resolutions.

The Lessons for Private Shareholders

There are a number of lessons that shareholders can learn from this debacle:

1. Keep an eye on your investments and ensure you follow the company carefully. In other words, do not simply "buy and forget". The problems that ultimately lead to the downfall of the business as a sound investment did not suddenly appear. They were a developing story over many months if not years.
2. Do not continue to hold an investment on the basis that it might recover. The use of "stop-loss" devices, or selling if the trend appears unfavourable, are trading techniques that can avoid the worst disasters (and in this case could have actually protected a substantial profit).
3. Be very wary of investing in highly geared companies who have lots of debt. The bankers will end up owning the business if it gets into difficulties.

In summary, this company was never one for "widows and orphans" to invest in. And any investor who did acquire shares in the company certainly needed to follow its progress and the associated business background with care. Note that with internet access, it's now possible to get free share price charts at any time, and news clippings on any company via email on a daily basis. There is no longer any reason why private shareholders should be misinformed.

Roger W. Lawson 23/10/2004