

There are several big issues at stake in the Northern Rock situation. If the Government gets it wrong we will all suffer the long term negative consequences of every issue mishandled. All of us, that is, except a few wealthy individuals behind the funds which have actively shorted the Rock down to these pitiful levels, or those behind the vulture funds who would like to buy it for nothing.

The first three issues are intertwined and concern the integrity of the British banking system, the role of the Bank of England/regulators and the lasting legacy of this Government for economic competence, prudence and stability. These together will determine the long term cost of capital in the UK economy and directly impact our national prosperity. Certainly the stance of the Bank of England has appeared to be *laissez-faire*; that banks who have any sort of problem should sink or swim on their own. This stance prompted comments from the French and German finance ministers of "extraordinaire" and "interesting". Neither were meant as a compliment. That is because it is widely known that the most important role of Banking is to take short term deposits/lending and turn it into long term capital/finance. Otherwise if you wanted a 20 year mortgage or business loan you would have to wait in vain for a 20 year depositor to show up. Without this the modern economy would not exist. The *quid pro quo* is that if a bank gets into trouble, not at all because of making bad loans but due to a failure of the inter-bank market which the Bank is supposed to supervise, then the Bank comes to its aid. It is crystal clear that if shareholders are to be wiped out in such an event, then other bank managements should exercise extreme caution and either stop lending or hugely raise the cost of capital. Probably some of both would result causing huge economic damage in the UK. It also follows that the Bank of England can be reduced to a skeleton staff if its only role is setting interest rates, while the Treasury would look after depositors. If this new *laissez-faire* Central Banking is the future, then the Treasury will have to do that again and again, as there will be other runs on other banks, each successively more panicky as fear tightens its grip.

Another major issue is the direct cost of wiping out Northern Rock, even if there were not the systemic damage outlined above. Locally in the North East up to five thousand people would lose their jobs, people who pay around £50m in tax and NIC, which will be lost to the Treasury. The ripple effect of these people spending less, plus suppliers losing contracts etc, could easily double this effect to £100m. Clearing up the mess with extra social security spending, family allowances and regional regeneration could double this again to £200m, not to mention the misery inflicted on thousands of families. The charitable foundation which distributed £175m over ten years would cease to exist, as would the £200m expected corporate tax payment from the Rock. Finally, analysts estimate the long term impact of the super-efficient lending of the Rock has been to squeeze mortgage lending margins across the whole UK market. As this market approaches £1 trillion, a reversal of this margin will cost all of us £5 billion.

A seldom talked about issue is the general public's perception of morality in business in general and financial markets in particular. In the long run this is extremely important. The perception that a coterie of funds have crushed an institution through a relentless campaign of shorting is damaging to us all. The associated panic and swirling rumours leave unpleasant memories and suspicions. Articles in a certain newspaper arguing for the "virtues" of vulture funds, followed by more articles repeating incessantly throughout this campaign that the Treasury wants shareholders to be wiped out, raise questions of press independence as these play only to the interest of the vulture funds. If these funds succeed and profits running to billions are taken abroad to their shareholders while the UK is left with a train wreck, what will this newspaper write then? Our Special Situations fund has become a large shareholder in the Rock after this crisis broke and we believe it is a decent institution which deserves to survive. I hope others do too. All of us can choose to use our money creatively to help build things up, or destructively to tear things down.

In conclusion, much will be lost if the Rock goes down. But we only have to lift our eyes to see that it can be saved. Richard Branson seems to see it and other solutions can be found, including the active promotion of normalisation in credit markets until the point is reached when the Rock can survive alone. There is no real cost to the public purse as the Rock pays an extra £100m penalty to the Treasury for every £10bn it borrows, above normal interest rates. We have a Prime Minister with a strong intellect, an inner moral compass and a concern for his lasting legacy in both the Economy and Nation. I hope he reads this letter. Even more, I hope his Government does the right thing.

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