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Press Release

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Government Planning to Ignore Shareholders' Rights?

Shareholders in Northern Rock now fear that the Government is rushing towards a decision that will prejudice all the stakeholders in the company, and wipe out the interest of shareholders.

The LiberalDemocrats are urging the Government to "temporarily" nationalise the company and several newspapers have declared the company worthless and the only way out of the current dilemma is to take the company into public ownership. But the UK Shareholders Association (UKSA) deplores this encouragement to the Government to obtain control of this company and extract its assets from the grip of shareholders. In our view this is a direct attack on the property rights of the 100,000 and more private shareholders with a stake in this business. In addition, it is not a solution that will solve the problems that are being faced.

The Government's Problem

In essence the Government's problem is that it has lent the company about £25 billion pounds to enable it to continue trading. This is partly as a result of the "run" of retail depositors taking their money out but also due to the general credit crisis in financial markets. The Bank of England is acting as the "lender of last resort" as laid down in the Banking Acts, but as representatives of SRM Global and RAB Capital (two major shareholders) said at the recent Extraordinary General Meeting, the original crisis was mishandled by the Bank of England (BofE) so it is perverse to suggest shareholders should be wiped out as it was not their fault. Unfortunately Mervyn King introduced the concept of "moral hazard" and refused to lend to the company when other central banks did make such loans.

But the Government wants its money back as soon as possible, even though it is profiteering by charging a penal rate of interest, to the benefit of the taxpayer. The company is trying its hardest to arrange alternative funding, or find some other solution via its "strategic review" process. But it now seems that no such simple solution may be forthcoming. And it is now clear that the Government has drawn up contingency plans for nationalisation and even have a new Executive Chairman (Ron Sandler) lined up to run the new business.

What Nationalisation Involves

Nationalisation would involve the compulsory purchase of all the shares in the company. They may offer some financial compensation as a result, indeed they need to do so because of European law, but what that might be nobody knows. For example on Railtrack they originally offered nothing to shareholders and only begrudgingly paid something after a long and expensive law suit by shareholders.

But Northern Rock is a very different sort of company to Railtrack. It has an excess of assets over liabilities, and is still profitable so far as we know. Indeed in the projections given to prospective bidders as part of the "strategic review", it forecast hundreds of millions in profits within a few years time – in other words it was expecting to return to its former level of profitability in very short order.

Short Term Nationalisation?

Many observers have suggested that any nationalisation could be "short term" although they often don't make it clear whether they mean months or years. But even Prime Minister Gordon Brown has recently said "*Because stability is the issue we will look at every option and that includes taking the company into public ownership and then moving it later back into the private sector*".

One can easily see how this might work. Extract the company from the hands of shareholders and pay them little in compensation, then include equity ownership as a "sweetener" to any institutions willing to fund the business and replace the BofE loans. In effect this would be a neat way of transferring the future interest of shareholders in the profits of the company to a third party, while those parties are currently reluctant to pay a fair price for the business. This is morally repugnant in our view and not something that shareholders or the public should accept.

Why the Company is Not Worthless

Northern Rock is like a lot of public companies. It has substantial debts (including in this case to the Bank of England), and is reliant on the continuing support of its creditors in the sense that any instant withdrawal of those loans would mean it would need to cease trading. But that does not mean the company is worthless. No independent valuation of this business would reach that conclusion unless it was clear that nobody would be willing to buy the company at any price (given normal markets for such assets). There are lots of ways to value businesses – on future profits, on discounted cash flows, on net assets – but even based on the latter basis this company is clearly worth a very substantial amount to anyone who can realise the assets in due course.

Other Options?

Note that justifying nationalisation by suggesting there is no alternative is simply the latest "spin" without substance. There are several other alternatives that could be explored including conversion of the current debt to some other form of security or partial interest by the Government in the company – which might even be placed in the open market fairly quickly. The only obvious reason why the Government would consider nationalisation in full is because it bypasses any need to get the consent of existing shareholders.

The Damage Caused by Nationalisation

Nationalisation has always been a recipe historically for either destroying once profitable businesses and/or the erosion of jobs. It has never managed to revive a business or restore its profitability and Government subsidies tend to increase in size and be endless. Indeed the longer a business stays in public ownership the more moribund it tends to become.

In the case of Northern Rock, the only way the Government can get it's money back rapidly is to sell assets cheaply and generally "down-size" the company. This will shrink the business and shrink any employment in it.

The impact on the North-East of England might be severe, particularly as the Northern Rock Foundation, one of the major charitable bodies in the area, relies heavily on the company at present. And their interest and income would presumably also be lost via nationalisation.

No, the nationalisation of Northern Rock is not in the interests of any of the stakeholders except possibly the Government's. But why would it be in their interests? They probably would not get their money back any quicker, and would be assuming total responsibility for all the potential liabilities of the company. This simply makes no sense.

In addition if the company was nationalised, most of the liabilities of the company, totalling about £100 billion, would be added to the public sector debt - reference an article in the Financial Times on 17/1/2008. To quote from that article, this would "blow the sustainable investment rule out of the water" and would raise the public sector net debt ratio from 36.7% of GDP to 43.8%.

So in summary the only beneficiaries of nationalisation would be those financial institutions that might be involved in any "re-float" of the company, who would be raking in future profits that are rightfully the property of current shareholders.

UKSA Calls on Everyone to Oppose Nationalisation

The UK Shareholders Association calls on all stakeholders - the shareholders, the employees, the trade unions who represent them, the politicians we elect, the directors of the company, the customers and suppliers of Northern Rock, the media commentators and all sensible people in this country to oppose nationalisation before it is too late to stop it.

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Note that the UK Shareholders Association has formed a "Shareholders Action Group" to promote the interests of private shareholders in this company and this page of our web site is dedicated to our campaign: www.uksa.org.uk/NorthernRock.htm . There are currently over 5,000 shareholders who have joined this campaign many of whom have contributed to a fighting fund to promote their rights.

About the UK Shareholders Association (UKSA)

UKSA is the leading independent organisation which represents the interests of private shareholders in the United Kingdom. We campaign to protect the rights of shareholders in public companies, and to promote improved standards of corporate governance. Our educational activities, regular regional meetings, company “analyst” meetings and the resources of our web site, help to inform the public on investment management. UKSA is a “not for profit” organisation which is financially supported primarily by its individual members.

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