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An Open Letter to the UK Government, the FCA, the London Stock Exchange and the UK Asset Management Industry

By Fraser Thorne, CEO, Edison Group

In the space of a fortnight, three of Britain's most recognised listed companies announced they were leaving the London Stock Exchange. First was SEGRO, Europe's largest REIT, a property giant with a £14 billion valuation, sold to US firm Prologis at a 42% premium to its traded price – compelling evidence, if any were needed, of just how deeply UK-listed companies are being undervalued. Then Bodycote, one of our most significant industrial engineers, went to a consortium of private equity buyers. And then EasyJet, one of Europe's largest airlines and one of Britain's best-known consumer brands, was snapped up by Apollo for £5.7 billion.

In one fortnight, three companies representing decades of British enterprise were transferred to private and overseas ownership. Together they represent 157 years as listed entities. This is the equivalent of felling 3 mighty oaks and arguing that 3 saplings will have the same environmental impact. We are experiencing the de-forestation of our stock market. We are allowing the culling of the very companies which create the oxygen for the markets to survive.

I want to be clear about what this means. When a company leaves the public markets, the jobs, at least for now, may well stay in the UK, but the profits follow the ownership. The returns that should be flowing to UK pension funds and UK retail investors – building wealth here in the UK – are instead flowing to private equity firms and overseas investors. When a company leaves the UK public markets, we are handing off the economic benefits of decades of British enterprise to investors that have no particular interest in the UK's long-term economic health.

This is not a new trend; it has been building for twenty years. The number of companies listed on the London Stock Exchange's main market has fallen from nearly 1,700 in 2006 to just 909 today. UK listings raised nearly £22 billion in 2006, but last year, that figure was £1.6 billion – a decline of over 90%.

Unfortunately, part of what drives this performance gap is structural. Firstly, the UK market is weighted towards what analysts call old economy sectors – energy, mining, banking and consumer staples – while the markets generating exceptional returns over the last two decades have been dominated by technology. Ironically, Britain does not lack innovative talent: ARM was designed here, DeepMind was founded here. But Britain’s tech companies end up scaling on NASDAQ or are acquired before they ever reach our public markets. Reversing that is going to take decades, but it will begin with having a public market worth listing on – which is precisely what is at stake.

Secondly, UK pension funds, which benefit from billions in annual taxpayer support through tax and National Insurance relief, have reduced their allocation to UK equities from 32% in 2006 to below 2% today. And that dynamic is self-reinforcing because, as domestic capital has retreated, demand for UK shares has fallen, valuations have stagnated relative to earnings, the case for listing in London has weakened, fewer quality companies have chosen to list here, and so returns have continued to lag – which justifies further reductions in UK allocation. Capital, entirely rationally, follows returns. Glencore's announcement last week that it is seeking a secondary listing in Australia – specifically to access the pension capital that Australian domestic incentives keep invested at home – is a pointed illustration of what happens when other countries make better choices than we have.

The retreat of long-term, active domestic capital has left London's market populated by passive index trackers, short-term macro traders and private equity predators who correctly identify that Britain's listed companies are cheap, and that someone will eventually buy them. Thirty-nine UK-listed companies have received takeover bids so far this year, worth over £43 billion – already ahead of last year's full-year total.

Fortunately, this structural issue is policy-led, and thus easier to address – in theory – than the make-up of the main market. And, to its credit, the UK Government and its regulators recognise the problem. The FCA's recent listing rule amendments are welcome, as is the LSE's LSE 24 announcement, which signals the exchange's genuine ambition to modernise its market infrastructure. And the government-backed campaign to encourage retail investing is a step in the right direction. These things matter, and I do not dismiss them.

But they are a plaster on what is fast becoming an arterial bleed.

The FCA's listing rule reforms do not introduce any competitive advantage – they merely remove a self-imposed disadvantage to bring us into line with international best practice. And, while the LSE may, in time, attract more international participation, no company is delisting from London because the market closes at 4:30pm. These are necessary measures, but they are certainly not sufficient ones.

So, what would sufficient look like? I believe four things, none of them radical, are necessary. I should also point out that every country with which we are competing already does all of these things.

First: incentivise domestic pension capital to invest in the UK. Australia's pension funds invest 45% of their equity allocation domestically, not because they are instructed to, but because the tax system makes it rational to do so. In 1997, Gordon Brown, during his tenure as Finance Minister, dismantled the equivalent UK system. Reversing that decision, or finding a modern equivalent, is arguably the single most powerful lever available to any government that is serious about this problem.

Second: abolish stamp duty on shares. The UK is virtually alone among major economies in taxing retail share purchases this way. It disadvantages retail investors relative to institutional players who use derivatives to avoid it. Removing it would be a clear signal that Britain is open for investment – and immediately encourage retail investment in line with the government's stated goal.

Third: stop the tax uncertainty. Last month, UK investors pulled £1.6 billion from equity funds, in part because of speculation about what the next Budget might bring. Confidence is fragile. Months of uncertainty, not to mention constant rumours about what may or may not happen when it comes to taxation, have eroded confidence to the point where investors are, at best, easily spooked and, at worst, prefer not to take any chances on UK equity. A clear, stable, predictable capital framework is a precondition for investment.

Fourth: quoted market investors need to think more like PE investors if they are to be competitive. Be more involved, PE has already crossed the line of shareholders staying at arm's length from their investments, compete with them to keep your holdings, do not sell them off cheaply, adopt their financial tactics, consider whether your holdings can run their balance sheets more efficiently.

These companies that are leaving – Bodycote, SEGRO, EasyJet – took decades to build. They cannot simply be replaced. A startup, however promising, does not become Europe's largest REIT or one of Europe's largest airlines in a budget cycle. And the overseas companies that might theoretically come to London to fill the gap are not coming either.

The London Stock Exchange has a proud history. Britain's public markets have funded industry, innovation and growth for generations. They remain worth fighting for. But the pace and scale of what is happening demands a response that is commensurate with the crisis – not one that brings us up to par with our competitors, but one that gives companies and investors a genuine reason to choose London.

The clock is running. So is the list of departures.

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