Britain plc in liquidation

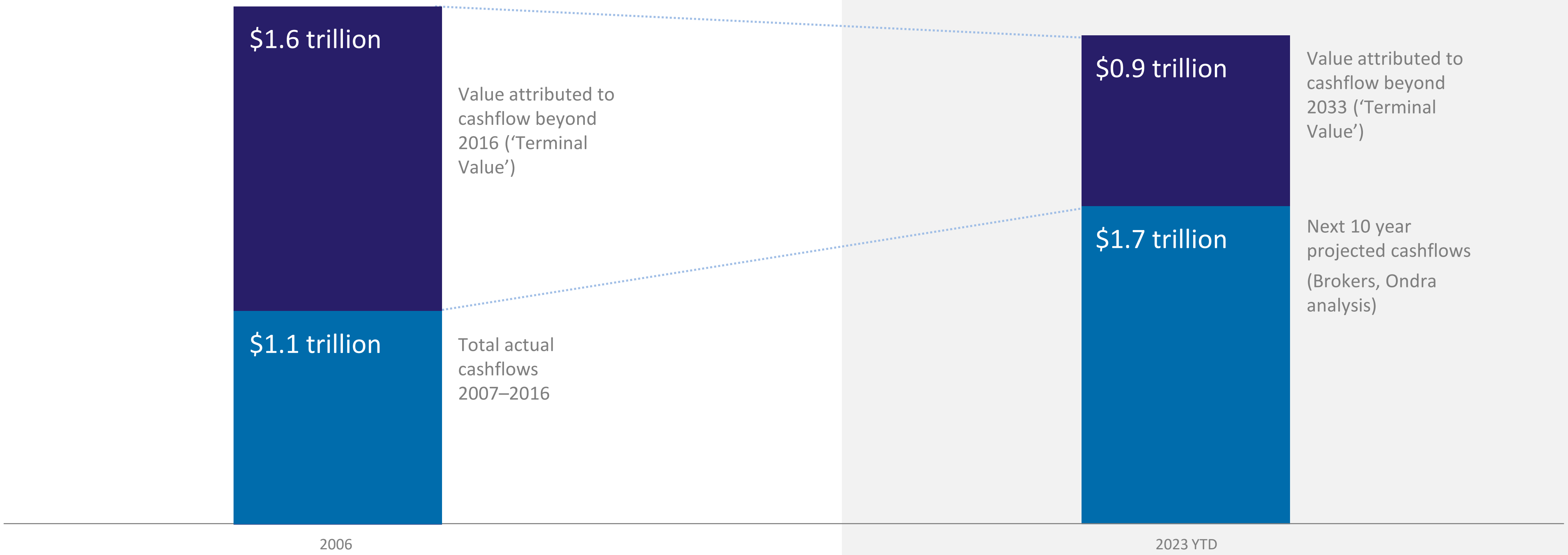
2006 - ?

October 2023

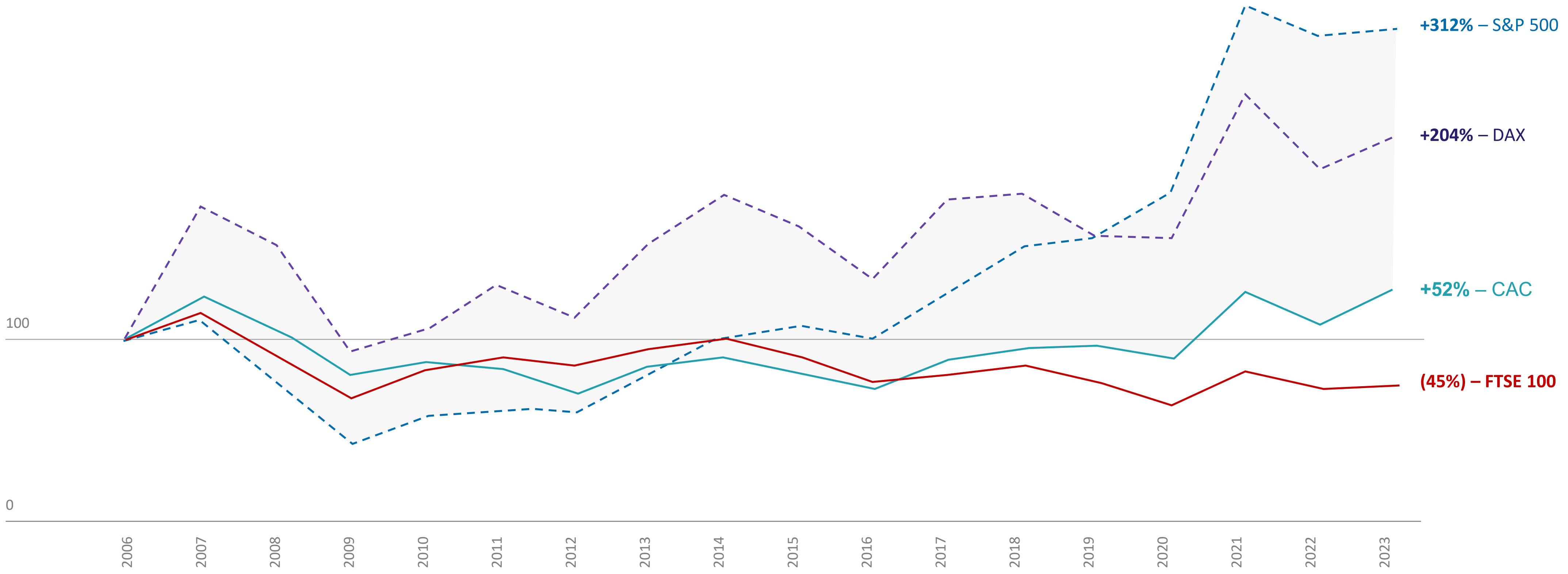
The value of the FTSE 100 attributable to the time horizon beyond 10 years (Terminal Value) has collapsed, which is reflected in the decline of the UK’s earnings multiple

FTSE 100 in 2006 and today, split into initial 10 years and thereafter

	2006	2023 YTD
MCAP	$2.7 trillion	$2.6 trillion
P/E (CY)	17x	11x

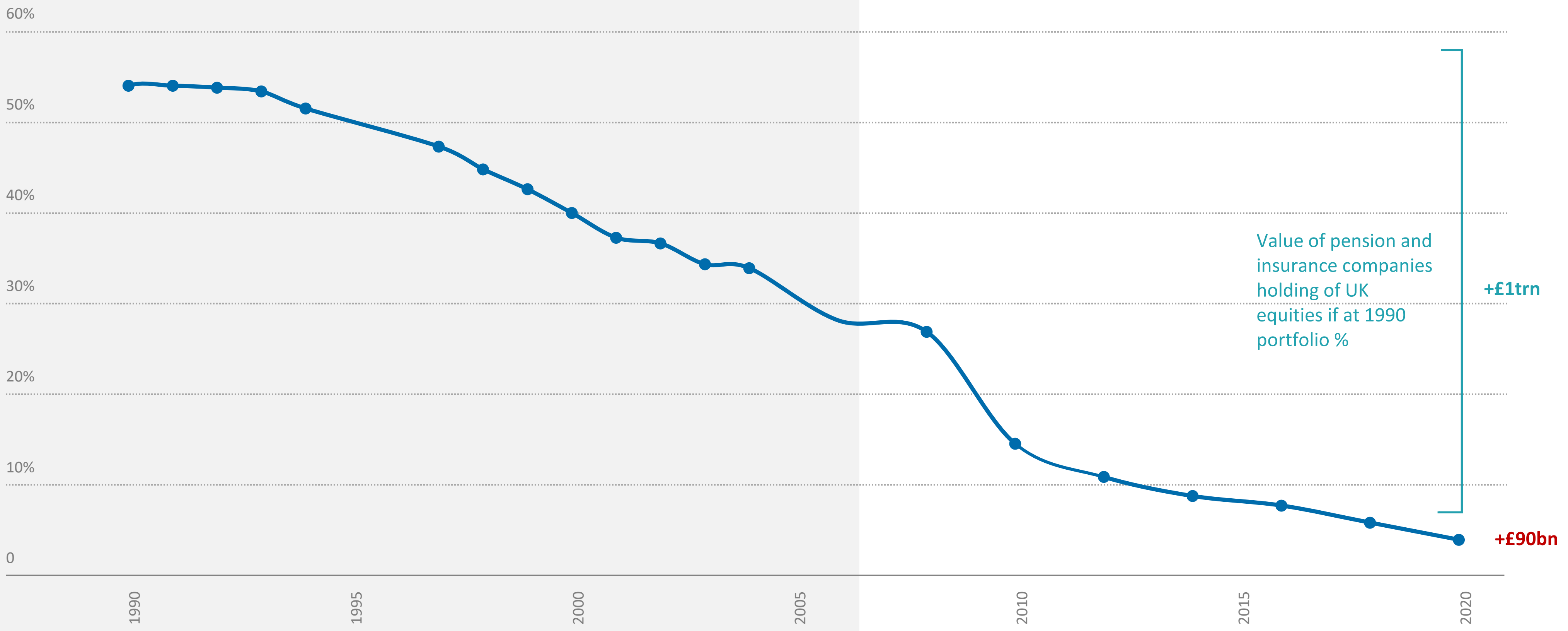


While the FTSE 100's Terminal Value has collapsed, that of our main peers has grown significantly over the same period



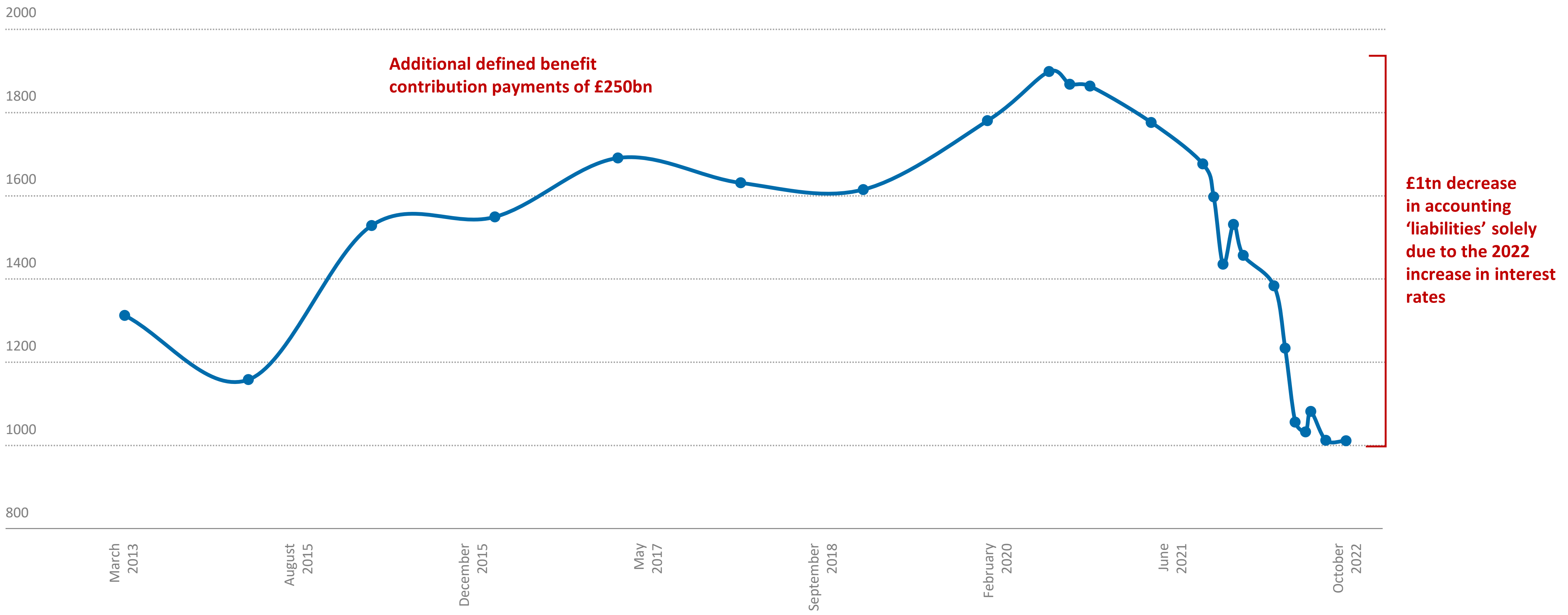
This all started with the liquidation by UK pension funds and insurance companies of their holdings of listed domestic equities, driven by pension accounting, regulation and consultants

Ownership of UK listed equities by domestic pension and insurance companies (%)



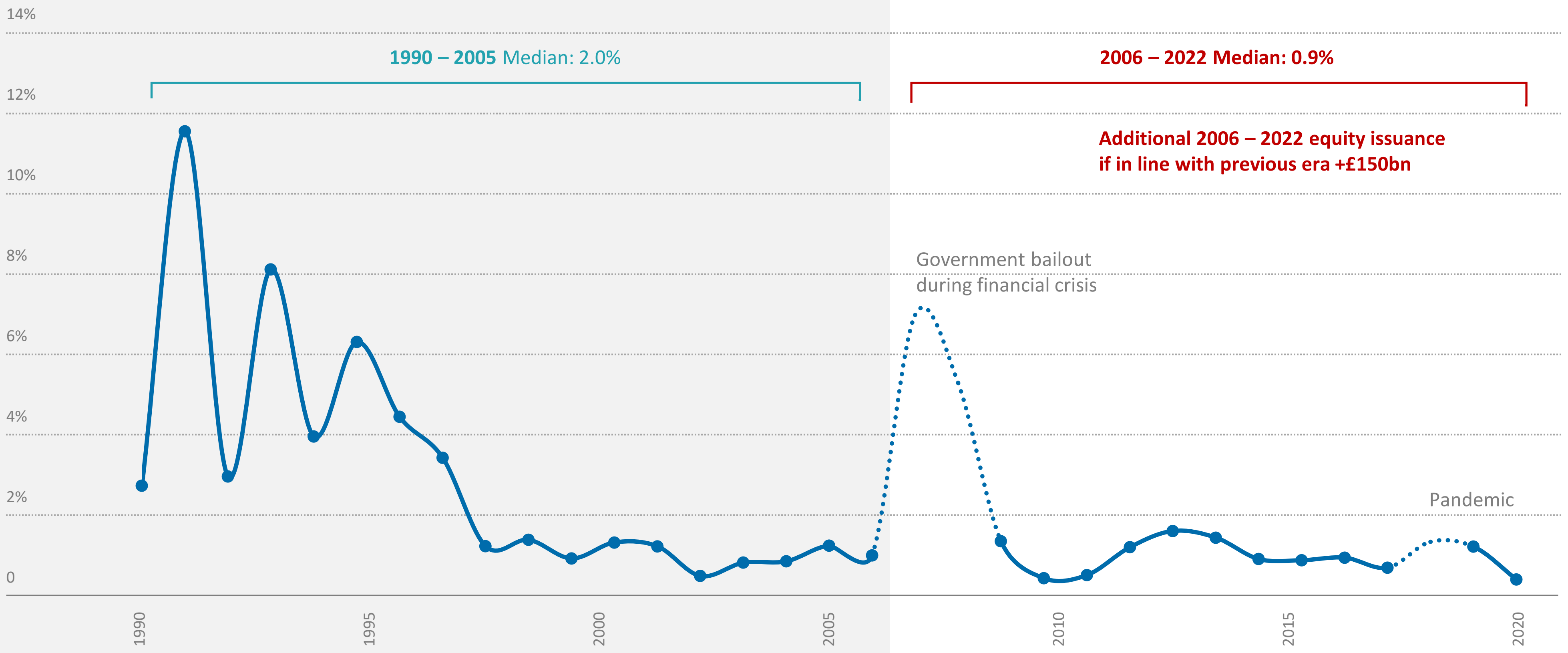
And was amplified by the £250bn of additional DB pension fund contributions driven by what was proven in 2022 to be an accounting fiction arising from a decade of low interest rates

1 | Total corporate sector DB liabilities (£m, as per PPF)



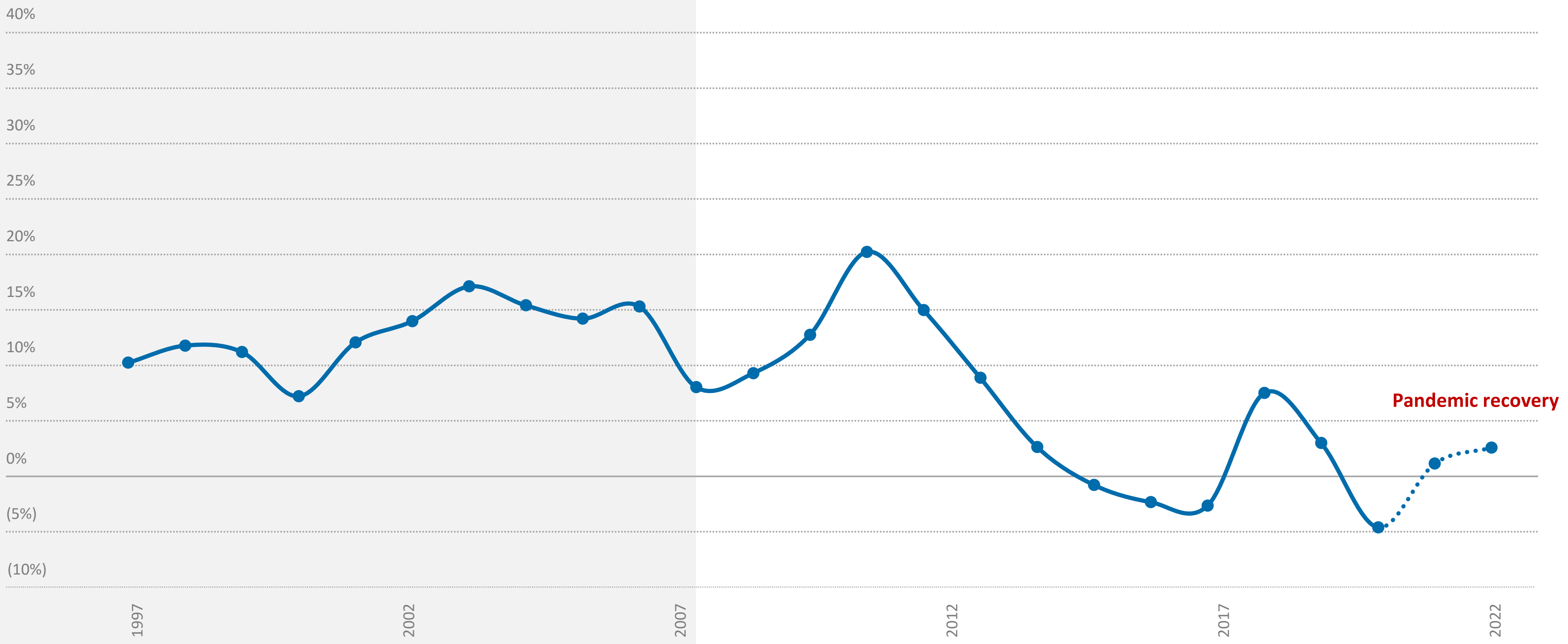
Not surprisingly, the disappearance of the domestic equity base and related liquidity has curtailed the supply of new primary capital for UK listed companies

2 | Primary capital raised as a percentage of FTSE 100 market capitalisation (%)



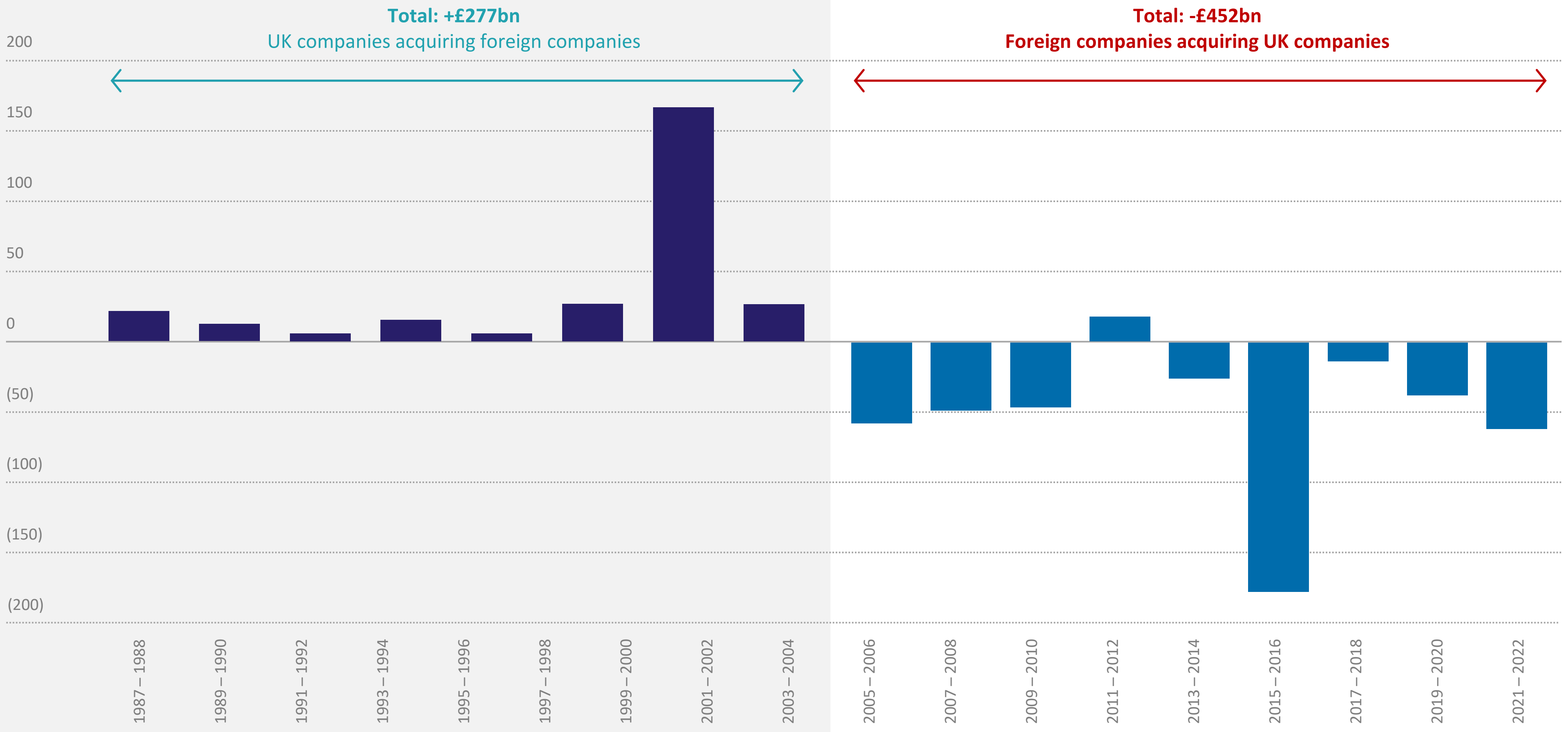
This burden, along with the absence of new primary capital, has heavily constrained UK companies' ability to invest, a key factor behind the declining earnings growth

FTSE 100 – 10 year rolling earnings CAGR (%, USD)



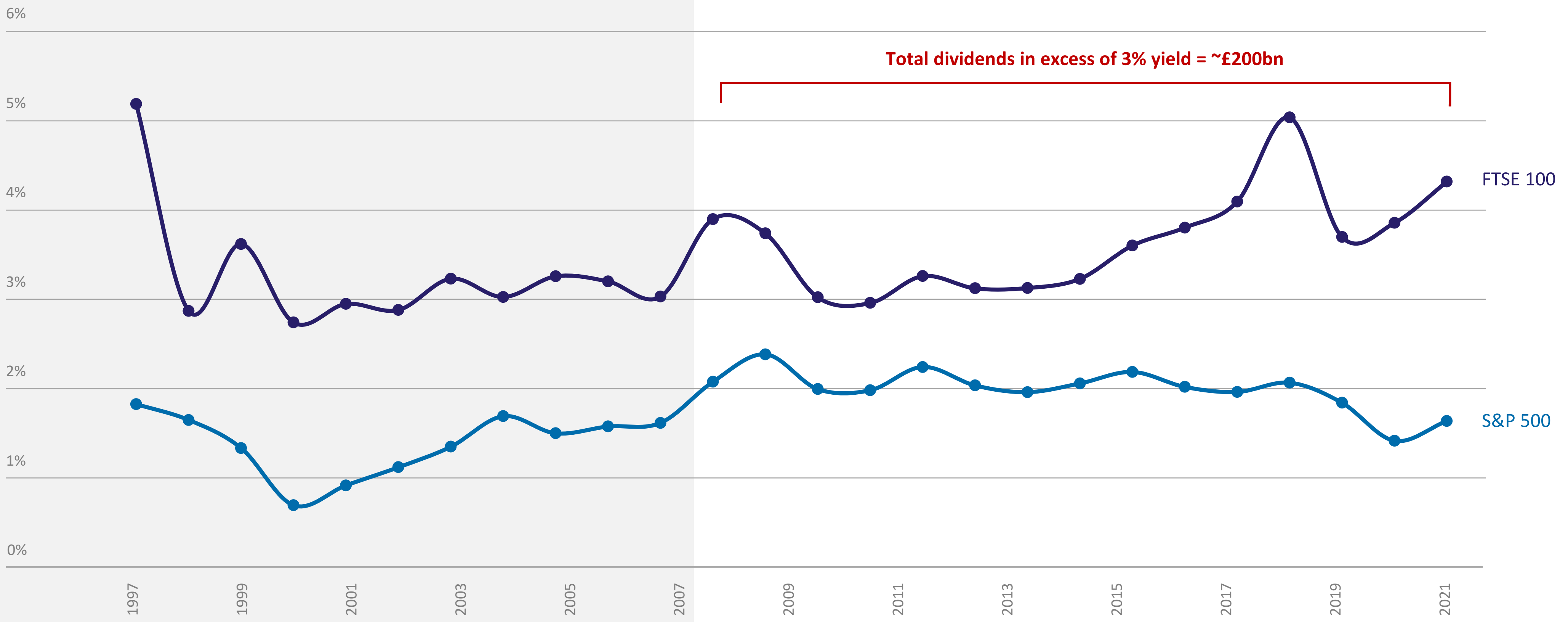
This is further reflected in the complete reversal of the M&A trend – from significant overseas acquisition led growth to wholesale liquidation

Total net value of outward / (inward) M&A of UK Companies (£bn)



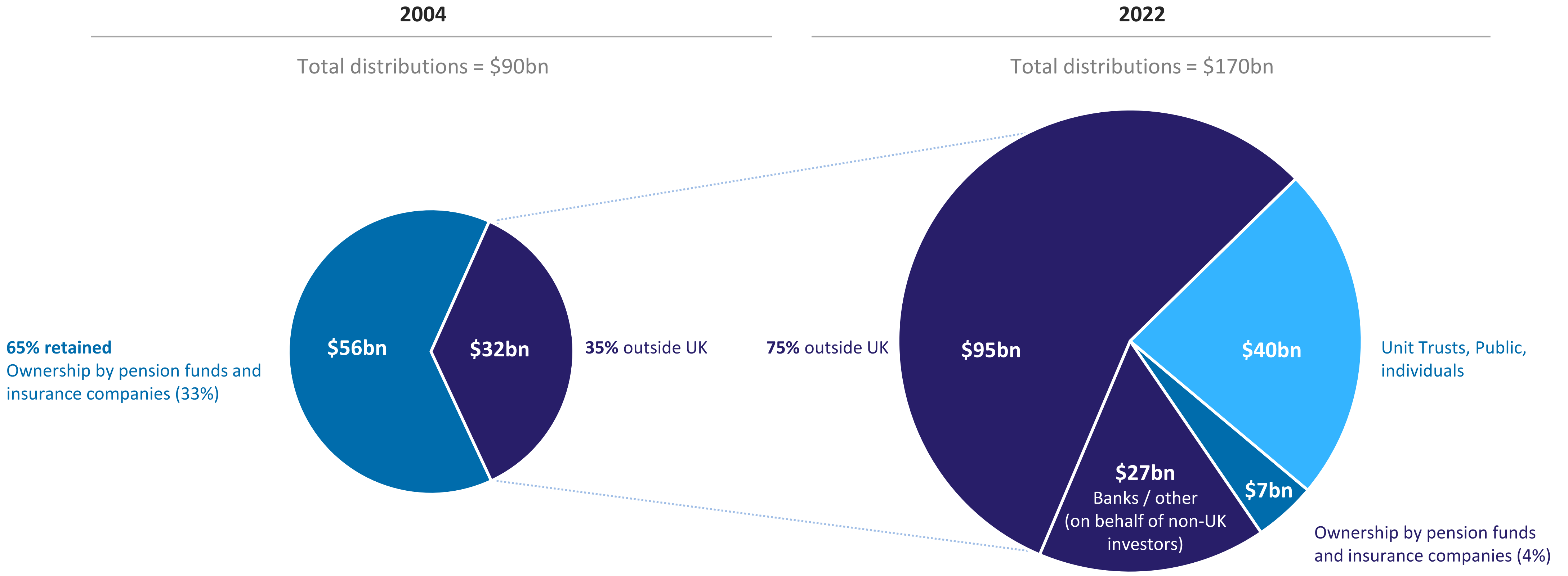
Declining earnings growth, in turn, has been a primary driver of higher dividend expectations to compensate for the lack of capital appreciation

3 | Dividend yield of FTSE 100 & S&P 500 (%)



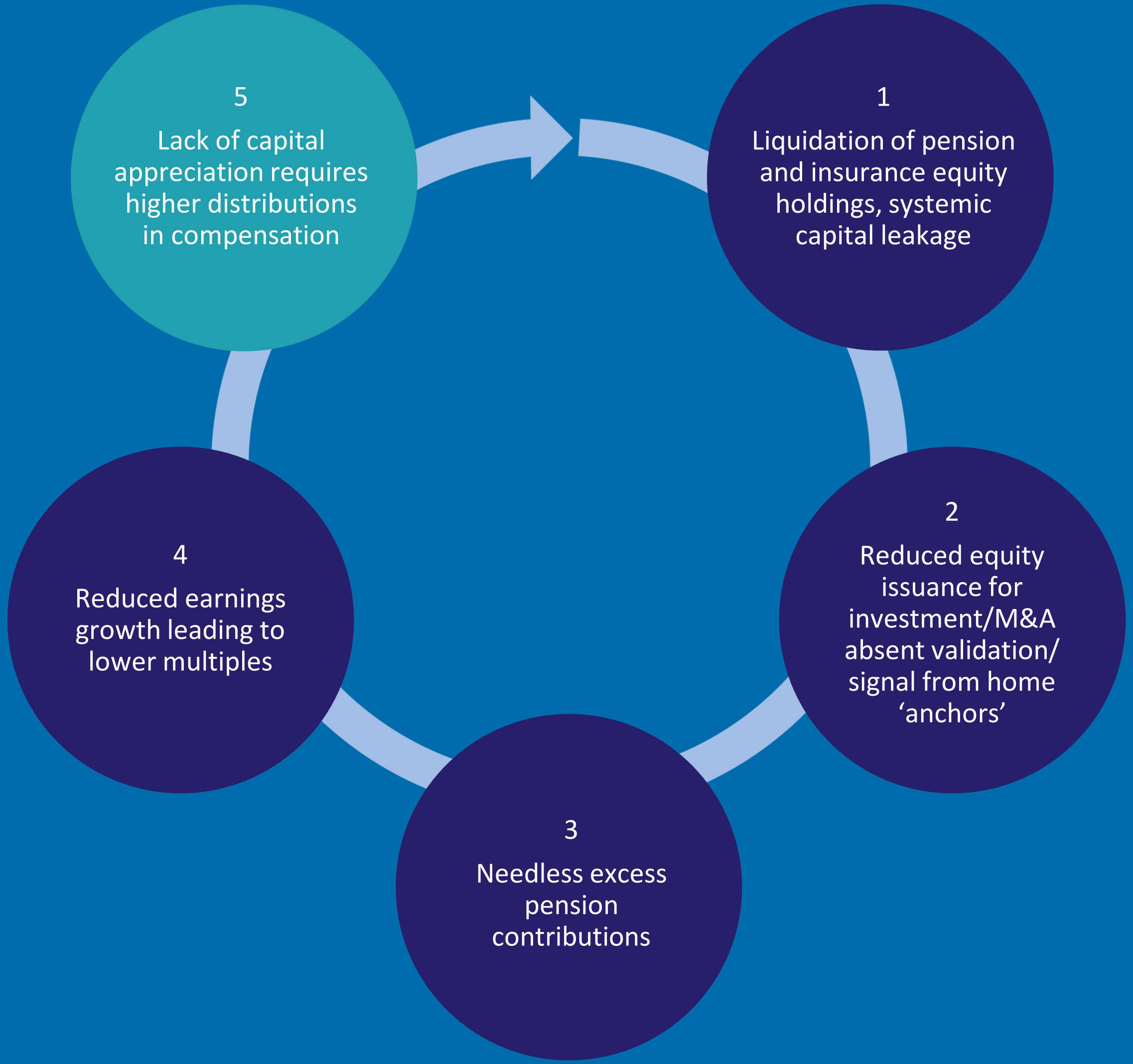
Overseas ownership of listed UK equities now entails significant capital leakage – every year

4 | FTSE 100 dividends and buybacks in 2004 and 2022



Additional recycling within the UK system if pension funds and insurance companies had maintained equity % = £200bn

The UK corporate sector is now at the tail-end of a self-reinforcing liquidation process

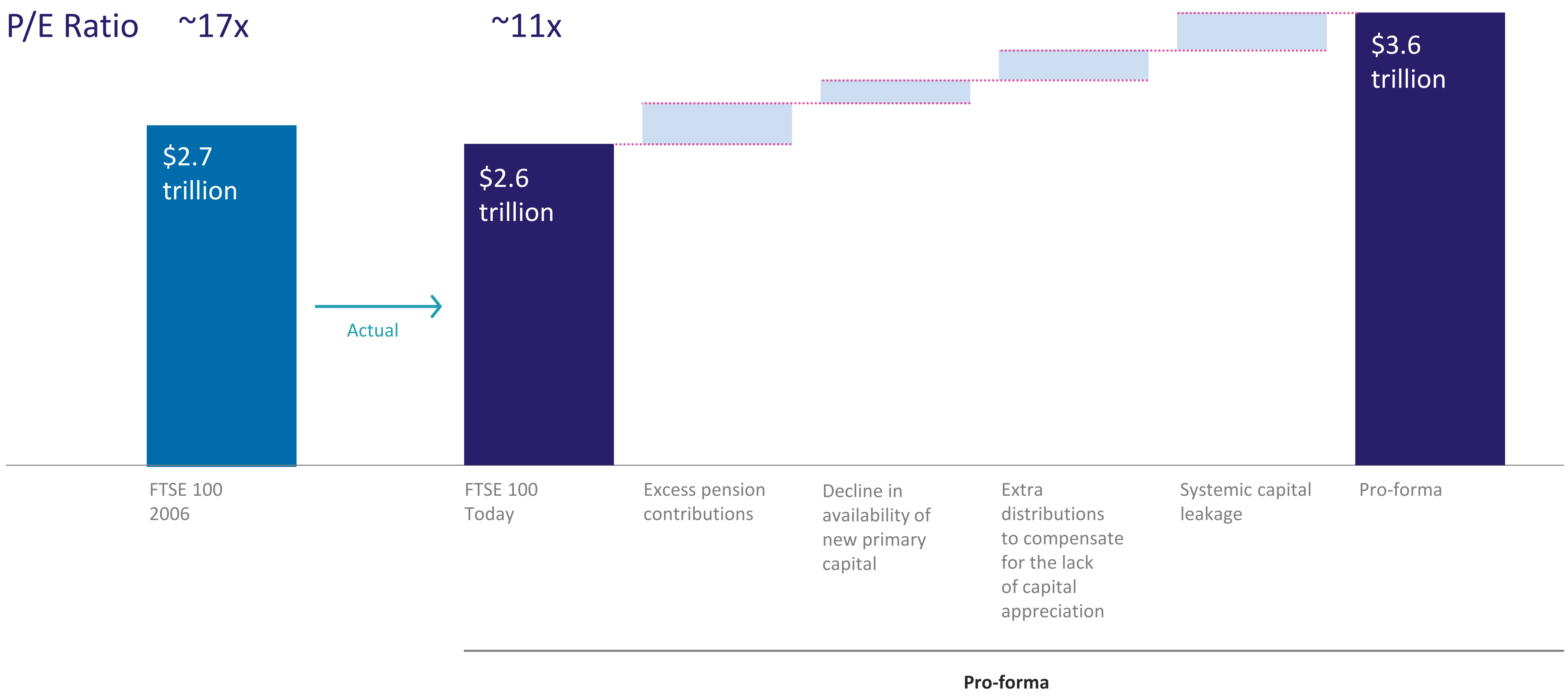


These four factors aggregate to £850bn, which more than account for the absence of FTSE 100 value creation during the last two decades

		Estimated impact	Explanation
1	**Excess pension contributions**	~£250bn	Amount of excess pension contributions by sponsors to UK defined benefit pension funds
2	**Decline in availability of new primary capital**	~£150bn	UK new primary capital issuance to continue in line with long-term historic average
3	**Extra distributions to compensate for lack of capital appreciation**	~£200bn	Assuming long-term FTSE 100 dividend yield remained at 3%, consistent with earnings growth prevailing in early 2000s
4	**Systemic capital leakage**	~£200bn	Assuming UK pension funds and insurance companies maintained their one-third interest in UK listed equities in line with early 2000s

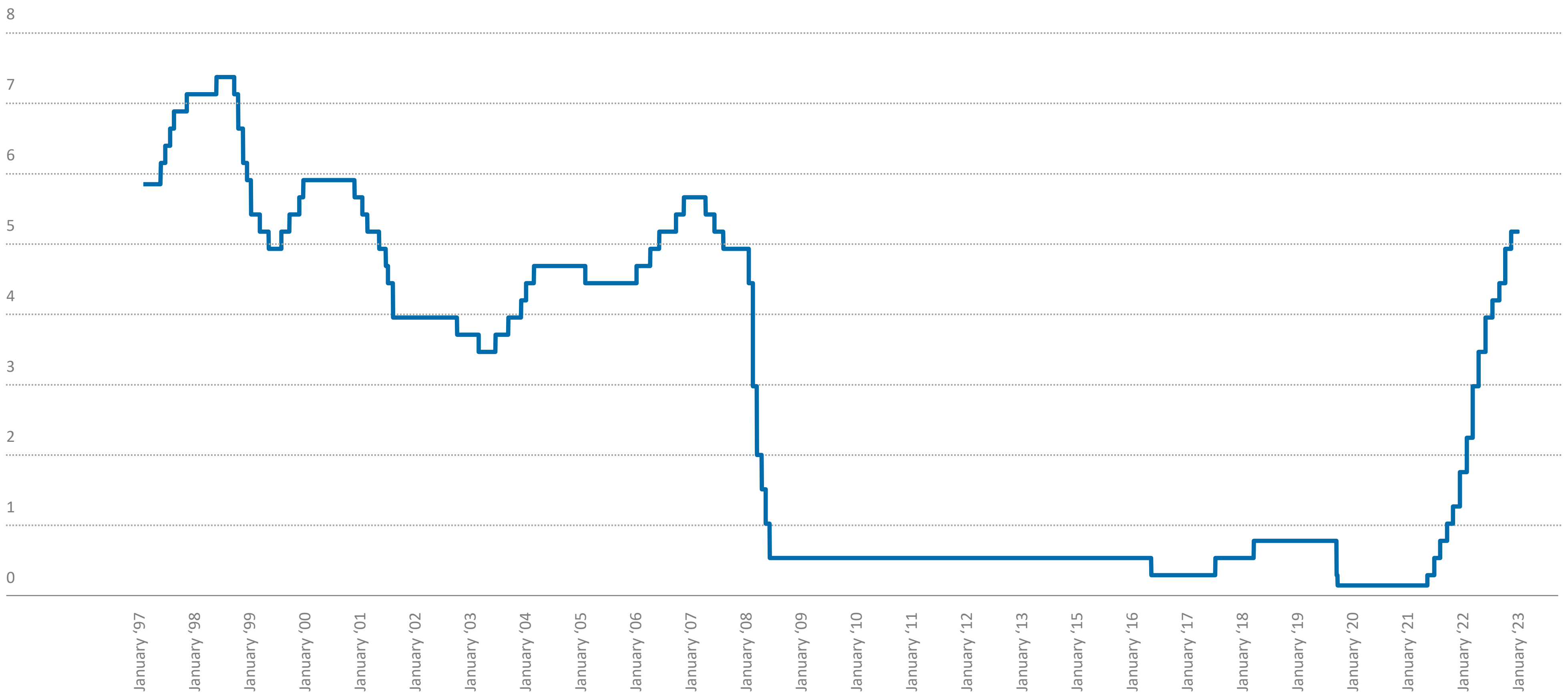
But for these capital burdens and leakages the FTSE 100 value creation would have been respectable

Estimated as pro-forma Terminal Value of FTSE 100 incorporating $1.1trn effect of the four factors (US$trn)



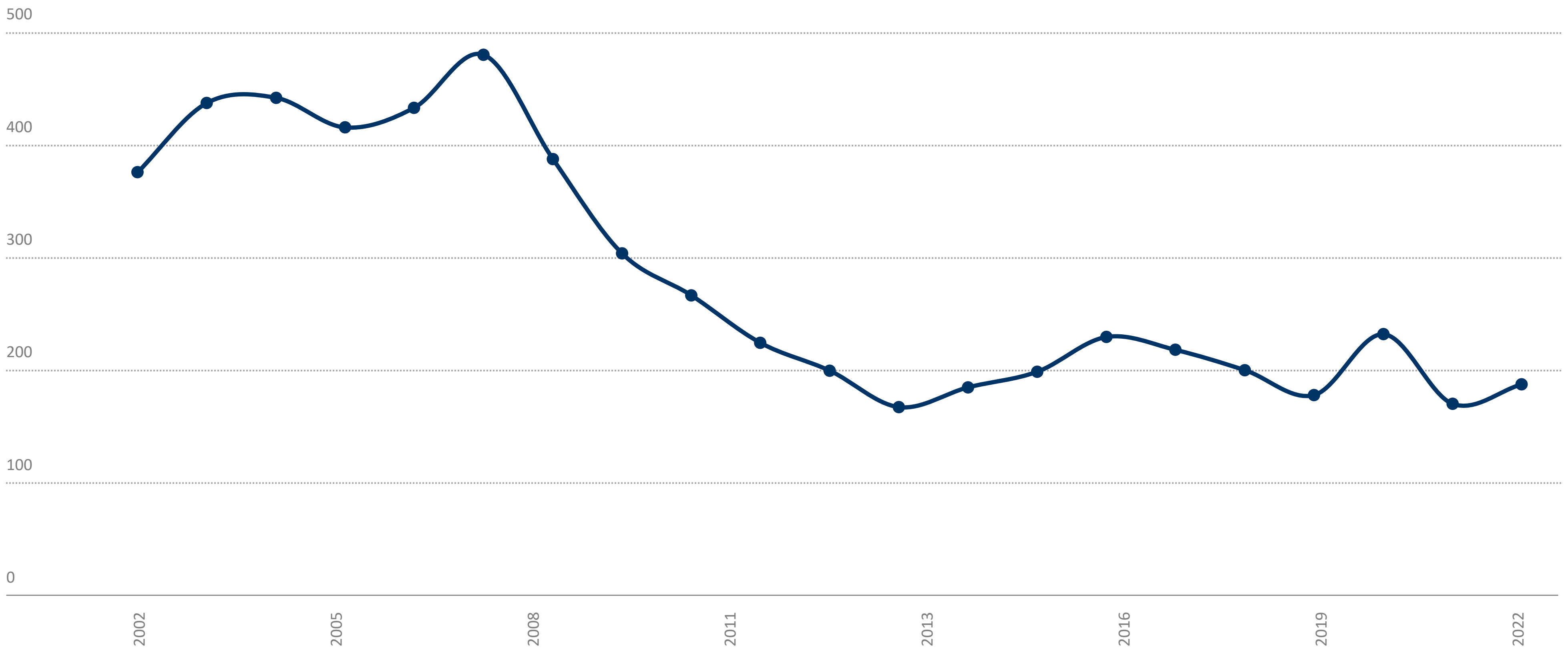
Supporting material

The decade-long period of near-zero interest rates beginning in 2009 severely raised defined benefit pension liabilities for UK corporates leading to substantial deficit contributions



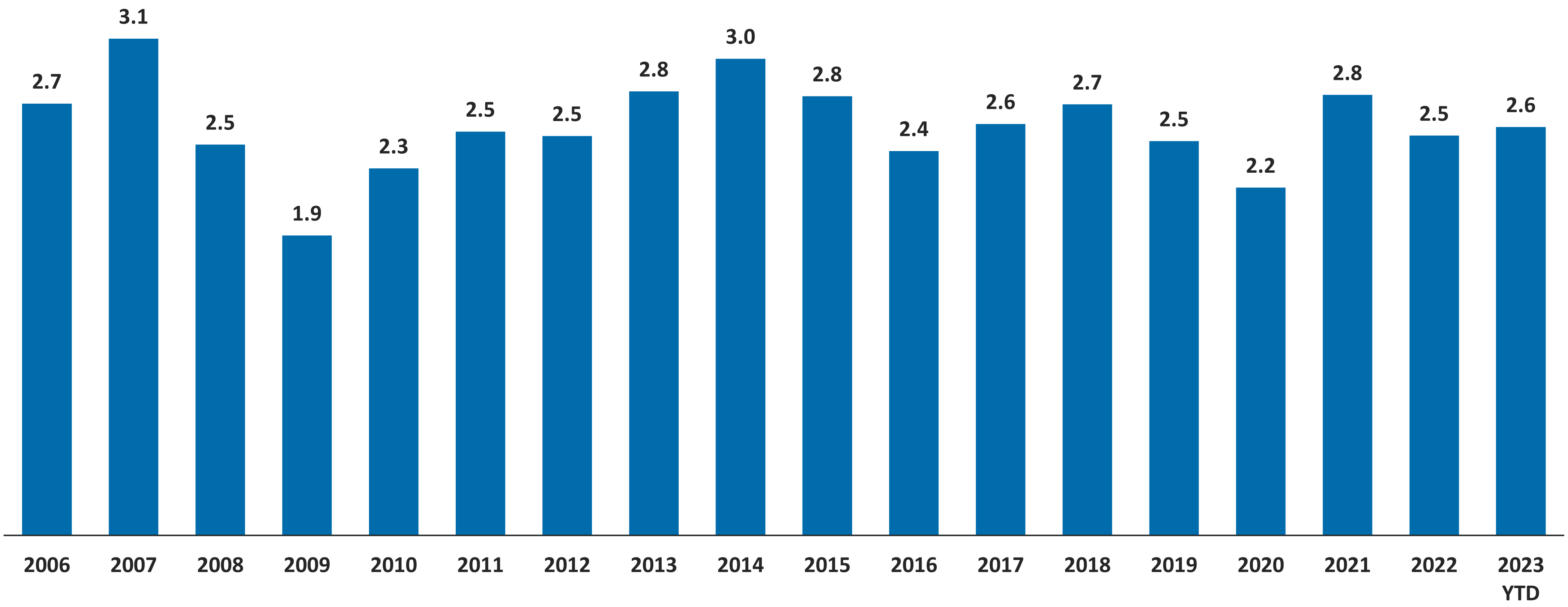
FTSE 100 has experienced a steady decline in trading volume, severely decreasing domestic liquidity, a key condition for raising new capital

FTSE 100 trading volumes (bn shares)



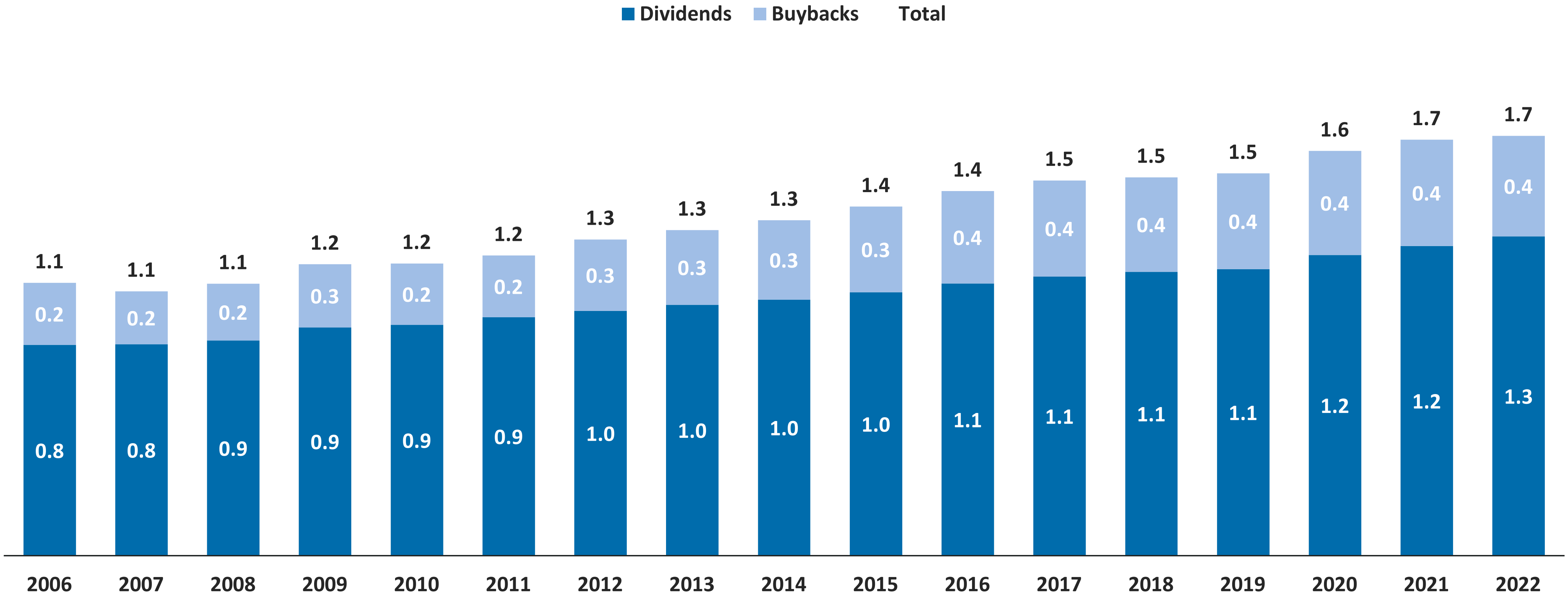
The performance of the FTSE 100 has been flat since 2006

Total market capitalisation of FTSE 100 stocks ($trn, average over the year)



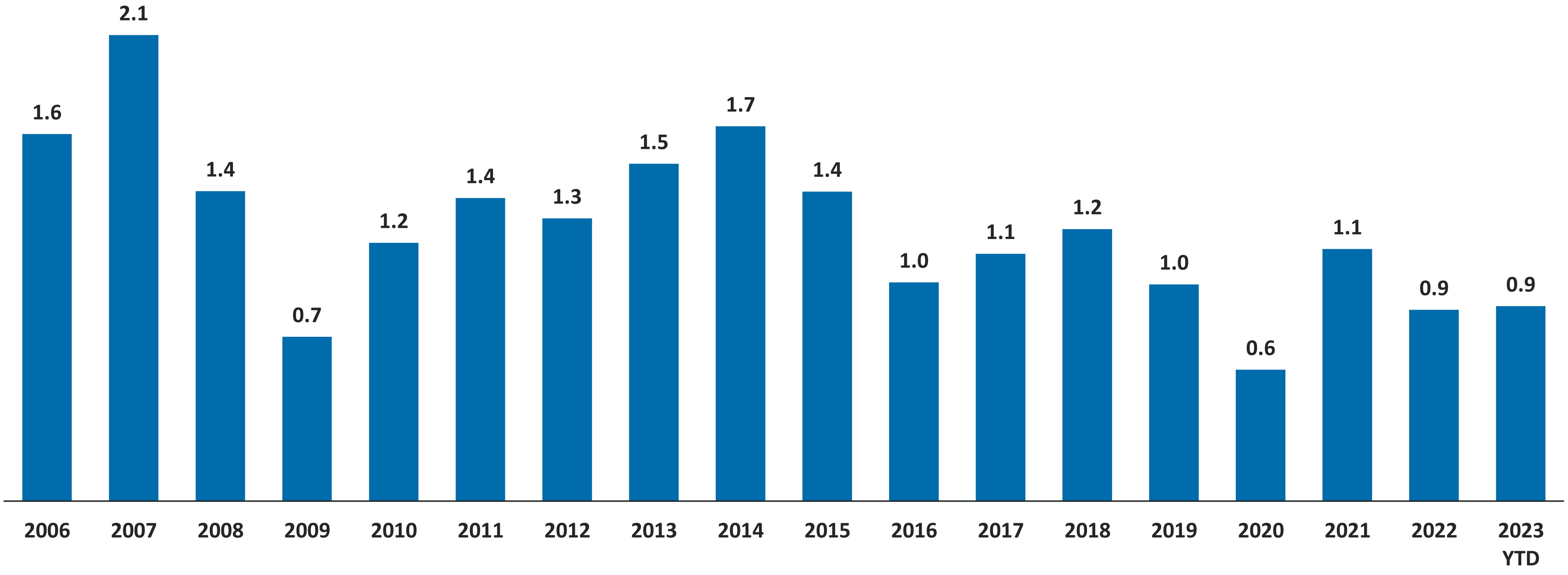
Next 10 year total distributions to shareholders (dividends and buybacks) continue to climb

Assuming 3% p.a. dividend growth and $40bn p.a. of buybacks in (fixed) ($trn)



Leading to a collapse of the Terminal Value

FTSE 100 market capitalisation minus next 10 year distributions (dividends + buybacks)



Sources and footnotes

Page(s)	Source(s) and footnotes
2 - 16	Main sources: Bloomberg; ONS, PPF
2-3	Source: Bloomberg; Notes: **(1)** Index composition as of 13/09/2023. **(2)** Index figures (market capitalisation, buybacks, dividends, earnings…) calculated as summation across current constituents based upon average over the period. **(3)** P/E ratio calculated as summation of constituent earnings / summation of market capitalisations. **(4)** 10-year figures are summation of ten-years forward dividends and buybacks respectively. **(5)** Figures post-2012 include projections 2023 onwards based on 3% YoY dividend growth and flat $40bn p.a. buybacks for FTSE 100 (in line with last 5 year average). **(6)** UK, US, France, and Germany, refer to FTSE 100, S&P 500, CAC, and DAX indices respectively.
4	Source: Office for National Statistics (Ownership of UK quoted shares); Notes **(1)** Based on the percentage of total market value of UK quoted shares where the beneficial owners were insurance companies or pension funds.
5	Source: PPF 7800 Index (PPF Purple Book). See Tony Blair Institute “Investing in the Future: Boosting Savings and Prosperity for the UK” for £300bn of excess pension contributions (of which £250bn assumed in relation to FTSE 100 companies)
6	Source: Bloomberg (Primary issuance incl. IPO’s); Notes: **(1)** Percentage calculated as: (summation of new primary equity issuance raised by UK companies above $100m) / (average market capitalisation of the FTSE 100) for each respective year; **(2)** Medians of 2.0% and 0.9% respectively calculated as the median from 1990-2005 inclusive and 2006-2022 inclusive respectively. If new issuance had been maintained in line with 2% median for 1990 – 2005, this would correspond to £380bn of additional new issuance. **(3)** Average new issuance between 1997 – 2005 was 1.2% vs. 0.7% between 2007 – 2022 (excl. government bank bailouts). If new primary issuance had been maintained at 1.2% level between 2006 – 2022 this would correspond to £167bn of new primary issuance. £150bn applied as a conservative measure.
7	Source: Bloomberg; Notes: **(1)** 10 year rolling growth is calculated as the percentage growth CAGR from the current year and 10 years prior for the FTSE 100 index
8	Source: Office for National Statistics (Mergers and acquisitions involving UK companies); Notes: **(1)** Outward M&A defined as transactions with a UK acquirer and foreign target; Inward M&A defined as transactions with a foreign acquirer and UK target, net values were then calculated using acquisition values.
9	Source: Bloomberg. Calculated as CY dividends divided by average market capitalisation over the year. 3% is the approximate yield that prevailed in the early 2000s when earnings growth of the UK corporate sector was significantly higher than today and is therefore a rough proxy of what the dividend yield would be today if earnings growth had been maintained (average dividend yield from 1998 – 2005 of 3.1%). Excess dividend paid between 2006 and 2022 above 3.1% of £199bn
10	Source: ONS (Ownership of UK quotes shares), Bloomberg (total distributions of dividend and buybacks). Ownership by “rest of world” (RoW) of from 2004 to 2022 of UK equities has increased from 36% to 56%. If RoW ownership had been maintained at 2004 levels $287bn had been maintained within the UK system while if UK Pension funds and insurance companies had maintained ownership levels at 2004 levels (33%), then $416bn of dividends and buybacks would have been maintained within the UK system. £200bn applied to adjust for the theoretical double counting of excess dividends above 3% equivalent to c.$35m (c.f. slide 9).
13, 15 - 19	Source: Bloomberg

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