

5 December 2013

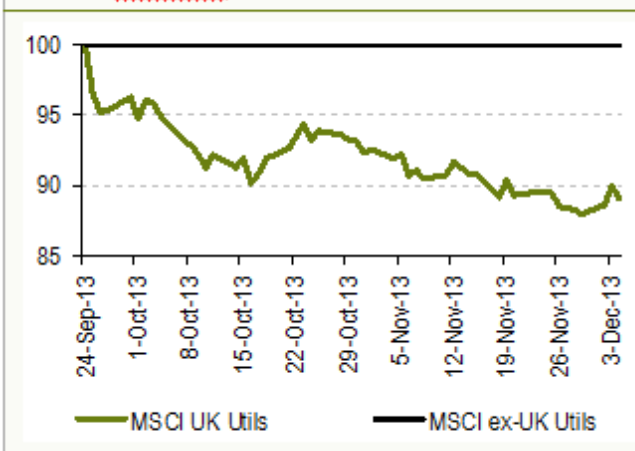
# Labour's Price Freeze Destroys £7bn to £11bn of UK Shareholder Value

## UK Utilities

In October we published a note entitled “Investors Selling UK & Buying Europe Due to Rising Political Risk”. This note looked at the impact on the valuation of UK utilities of the sharp rise in political risk faced by the sector following Mr Ed Miliband’s conference speech on 24 September that promised to impose an energy price freeze should the Labour Party win the next general election. At the end of a week when the government has attempted to politically neutralise Labour’s price freeze promise, we thought we would revisit this issue and re-assess the damage that the increased political risk has caused. We find that:

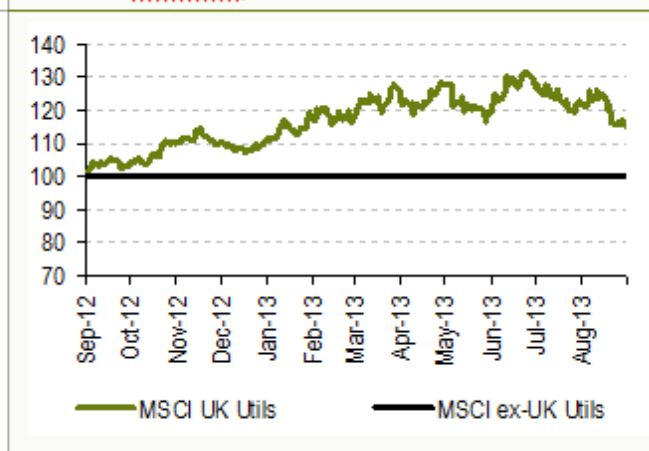
1. Since 24 September the UK utility sector has underperformed Europe by 11% (see chart 1). In the 12 months preceding 24 September the UK sector had outperformed Europe by 14% (chart 2).

**Figure 1: MSCI UK Utils vs. MSCI European ex-UK Utils since Mr Miliband's announcement**



Source: Bloomberg, Liberum

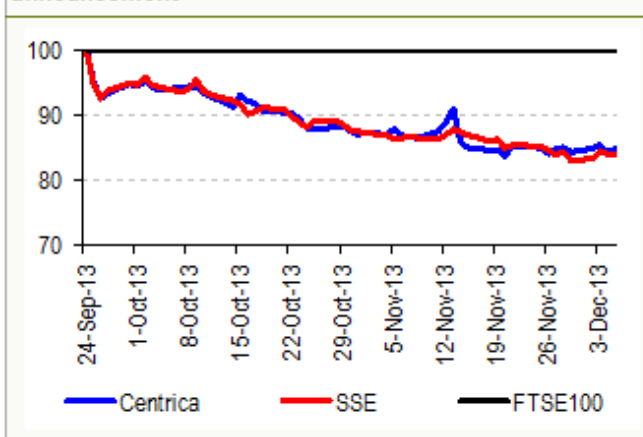
**Figure 2: MSCI UK Utils vs. MSCI European ex-UK Utils before Mr Miliband's announcement**



Source: Bloomberg, Liberum

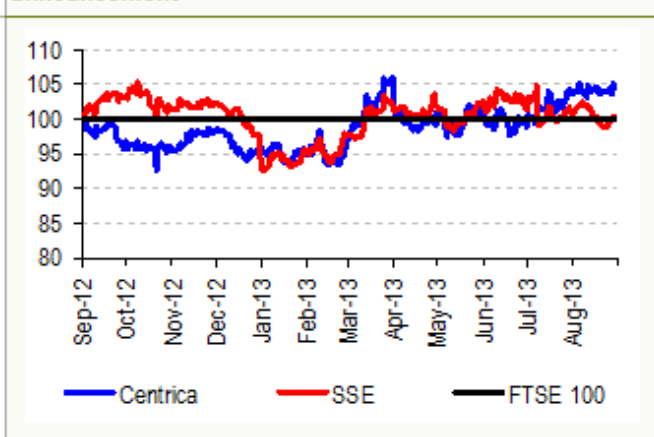
2. Since 24 September Centrica and SSE have underperformed the FTSE100 by 15% & 16% respectively (chart 3). In the 12 months preceding 24 September Centrica had outperformed the FTSE100 by 5% and SSE had traded in line (chart 4).

**Figure 3: Centrica, SSE vs. FTSE100 since Mr Miliband's announcement**



Source: Bloomberg, Liberum

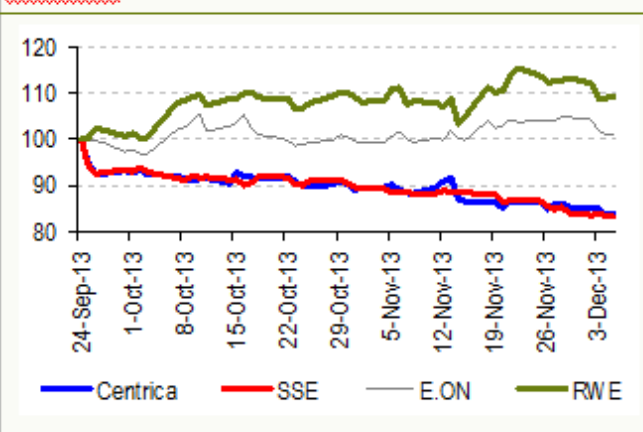
**Figure 4: Centrica, SSE vs. FTSE100 before Mr Miliband's announcement**



Source: Bloomberg, Liberum

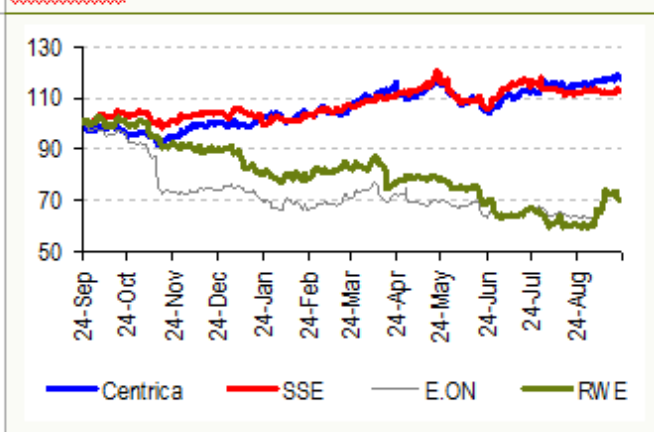
3. Since 24 September Centrica and SSE have underperformed E.ON by 17% and RWE by 25%. In the 12 months preceding 24 September Centrica and SSE had outperformed E.ON by 42% and RWE by 47% (chart 6).

**Figure 5: Centrica, SSE vs. E.ON RWE, since Mr Miliband's announcement**



Source: Bloomberg, Liberum

**Figure 6: Centrica, SSE vs. E.ON RWE, before Mr Miliband's announcement**



Source: Bloomberg, Liberum

4. A total of c.£6.7bn has been wiped off the value of the MSCI UK Utility index since 24 September.
5. If the MSCI UK index had merely maintained parity with the European sector index since 24 September then the market capitalisation of the UK utility sector would be c.£11bn higher today than it is.
6. If the UK utility sector had maintained parity with the FTSE100 since 24 September then the market cap of the sector would be c.£7bn higher today than it is.

### Conclusion

The heightened political risk faced by the UK utility sector following the announcement of the Labour Party's price freeze has materially impacted on the valuation of the sector and reversed the five year utility sector trade of Long UK / Short Europe. Total shareholder value lost so far amounts to between £7bn to £11bn. In our view, if the UK government is successful in politically neutralising Labour's price freeze policy then some of this loss, but probably not all, could be regained. Some of the loss is likely to be permanent in our view because it is now apparent that UK politicians (like those in Europe) are unwilling to stand by the logic of their own energy policy and enforce the higher costs onto consumers that naturally follow from their de-carbonisation strategy.

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