Murder on the City Express - Who is Killing the London Stock Exchange's Equity Market?

Law Working Paper N° 714/2023
June 2023

Brian R. Cheffins
University of Cambridge and ECGI

Bobby V. Reddy
University of Cambridge

ECGI Working Paper Series in Law

Murder on the City Express - Who is Killing the London Stock Exchange's Equity Market?

Working Paper N° 714/2023
June 2023

Brian R. Cheffins
Bobby V. Reddy

Abstract

In Agatha Christie's Murder on the Orient Express, Poirot deduced that no single culprit was responsible for a murder on the eponymous train. In this article, which is intended to serve as an aide memoire to assess anticipated reforms, we similarly reason that there is no single suspect responsible for a recent decline in fortunes of the London Stock Exchange's equity market. We note that globally-relevant factors, such as the rise of private capital, may have impacted the health of the U.K.'s primary stock market. However, sufficiently material differences in various stock market metrics exist between the London Stock Exchange and stock markets elsewhere to suggest that U.K.-specific factors are also significant. We canvass several of those factors: Britain's listing requirements and corporate governance regime, a paucity of public company investment research, the withdrawal of U.K. pension and insurance firms as public company investors, a U.K. investment culture that prioritises dividends over growth, a lack of world-leading British corporations, and managerial shortcomings. We suggest that all of these factors likely have contributed to the U.K.'s equity market travails, a finding which implies that generating effective reforms will require coherent and expansive policymaking.

Keywords: London Stock Exchange, Corporate Governance, Listing Rules, Private Equity, Pension Funds, Analyst Coverage

JEL Classifications: G34, G38, K22, M13, M14, O32

Brian R. Cheffins*
S. J. Berwin Professor of Corporate Law
University of Cambridge, Faculty of Law
10 West Road
Cambridge, CB3 9DZ, United Kingdom
phone: +44 1223 330084
e-mail: brc21@cam.ac.uk

Bobby V. Reddy
Associate Professor
University of Cambridge
10 West Road
Cambridge CB3 9DZ, UK
e-mail: bvr20@cam.ac.uk

*Corresponding Author

Legal Studies Research
Paper Series

UNIVERSITY OF
CAMBRIDGE
Faculty of Law

PAPER NO. 16/2023

MAY 2023

Murder on the City Express - Who is Killing the London Stock Exchange's Equity Market?

Brian R. Cheffins & Bobby V. Reddy

Further information about the University of Cambridge Faculty of Law Legal Studies Research Paper Series can be found at http://www.law.cam.ac.uk/ssrn/

Murder on the City Express – Who Is Killing the London Stock Exchange's Equity Market?

Brian R. Cheffins* **and Bobby V. Reddy****

Abstract- *In Agatha Christie's Murder on the Orient Express, Poirot deduced that no single culprit was responsible for a murder on the eponymous train. In this article, which is intended to serve as an aide memoire to assess anticipated reforms, we similarly reason that there is no single suspect responsible for a recent decline in fortunes of the London Stock Exchange's equity market. We note that globally-relevant factors, such as the rise of private capital, may have impacted the health of the U.K.'s primary stock market. However, sufficiently material differences in various stock market metrics exist between the London Stock Exchange and stock markets elsewhere to suggest that U.K.-specific factors are also significant. We canvass several of those factors: Britain's listing requirements and corporate governance regime, a paucity of public company investment research, the withdrawal of U.K. pension and insurance firms as public company investors, a U.K. investment culture that prioritises dividends over growth, a lack of world-leading British corporations, and managerial shortcomings. We suggest that all of these factors likely have contributed to the U.K.'s equity market travails, a finding which implies that generating effective reforms will require coherent and expansive policymaking.*

Keywords- London Stock Exchange, Corporate Governance, Listing Rules, Private Equity, Pension Funds, Analyst Coverage

Introduction

In March 2023, the Chancellor of the Exchequer indicated that in the Autumn statement later in the year reforms would be introduced to make the London Stock Exchange (LSE) a more attractive place for companies to list their shares.[1] The scene was set earlier in the month when Arm, a leading U.K.-based software company, indicated that it would list in New York rather than on the LSE. Members of the

---

* Faculty of Law, University of Cambridge; SJ Berwin Professor of Corporate Law.

** Faculty of Law, University of Cambridge. Former partner, Latham & Watkins LLP. Fellow, Cambridge Endowment for Research in Finance. Visiting Professor, University of Notre Dame.

[1] Spring 2023 Budget Speech (15 March 2023) https://www.gov.uk/government/speeches/spring-budget-2023-speech. All URLs were last accessed on [30 April] 2023, unless otherwise stated.

Treasury Select Committee dubbed Arm's decision "a national humiliation"[2] and the LSE's CEO said the news demonstrated "the need for the UK to make rapid progress in its regulatory and market reform agenda."[3] Still, while Arm's snub "prompted a period of soul-searching in the City of London"[4] it was hardly a shock. As the Economist noted just prior to Arm's announcement, there had been "a long running exodus from Britain's capital markets. The 21st century has seen London's stock market shrivel compared with those in the rest of the world."[5]

It is open to question whether a robust stock market should be a policy priority.[6] Nevertheless, with the Chancellor having indicated that stock market-related reform is firmly on the agenda, it is timely to identify the potential culprits responsible for Britain's stock market malaise and assess the extent of their culpability. This article seeks to do so by offering a concise analysis of leading potential causes for the stock market decline the U.K. has experienced. The answers offered are by no means definitive. As with detective Hercule Poirot in Agatha Christie's *Murder on the Orient Express*[7] this article fails to assign blame conclusively for the decline of the U.K.'s equity markets to any single plausible suspect. Still, the article's analysis should aid with assessing whether the proposals the government generates in the Autumn Statement and related reforms will prompt a reversal of fortunes.

In the first section of this article, we canvass potential globally-relevant explanations for the decline of U.K. equity markets, focusing on a leading suspect, the rise of private capital. In so doing, we note that while the emergence of substantial private capital likely is impairing the health of the publicly traded company in Britain, the fact that on certain metrics U.K. equity markets have suffered in comparison to global counterparts indicates that there are U.K.-specific culprits. In the second

---

[2] P. Hosking, "Arm Move 'Humiliates Financial Watchdog and London'" (9 March 2023, *The Times*) https://www.thetimes.co.uk/article/arm-move-humiliates-financial-watchdog-and-london-630q8kbb5.

[3] K. Prescott and H. Cahill, "Arm's US listing Leads to Calls for Reform of London Stock Market" (4 March 2023, *The Times*) https://www.thetimes.co.uk/article/arms-us-listing-leads-to-calls-for-reform-of-london-stock-market-phkl9jlqj.

[4] H. Cahill, "How London Shot Itself in the Foot" (11 March 2023, *The Times*) https://www.thetimes.co.uk/article/how-the-london-stock-exchange-has-shot-itself-in-the-foot-bbfdvk59l.

[5] Gilt Complex (4 March 2023 *The Economist*), 17.

[6] B. Cheffins and B. Reddy, "Will Listing Rule Reform Deliver Strong Public Markets for the UK?" (2023) 86 MLR 176, 181.

[7] Agatha Christie, *Murder on the Orient Express* (London: Collins Crime Club, 1934).

section, we commence our analysis of domestic factors with a commentary on the U.K. listing regime and the governance framework applicable to companies traded on the LSE. We maintain that despite recent reforms this environment likely is contributing to the decline of U.K. equity markets. We then, in the third section, discuss leading U.K. market-oriented suspects, including a shortfall in public company investment research, deficiencies in the U.K.'s investor ecosystem, a lack of truly dominant, world-class British corporations, and possible managerial shortcomings. Each, we argue, is a plausible perpetrator in the downfall of U.K. equity markets. We finish with concluding remarks.

General explanations for the decline of the public company

While in the U.S., predictions of the publicly traded company's demise can be traced back at least to the late 1970s,[8] the most famous such prediction was made in 1989 and focused on private capital. Financial economist Michael Jensen proclaimed in the *Harvard Business Review* "The Eclipse of the Public Corporation" that what he called "LBO Associations" – now known as private equity firms – would replace the public company because the buyouts they led eliminated the managerial agency cost problems plaguing the publicly traded firm.[9] The publicly traded firm in fact prospered in the U.S. in the 1990s but new predictions of a dire public company future emerged with burgeoning private equity-driven public-to-private buyouts in the mid-2000s coinciding with a steady decline in the number of American publicly traded firms.[10] Similar private equity oriented forecasts were made in the U.K. in the mid-2000s,[11] even though the number of publicly traded firms bucked long-term trends and were actually increasing.[12] In the 2010s, predictions that the public company's days were numbered in the U.S. shifted to a different form of private capital – venture capital (VC) funding – that was sustaining

[8] B. Cheffins, *The Public Company Transformed* (Oxford: Oxford University Press, 2018), pp. 104-7.

[9] M. Jensen, "Eclipse of the Public Corporation", Harvard Business Review (Sept.-Oct. 1989) 61.

[10] B. Cheffins, *The Public Company Transformed* (Oxford: Oxford University Press, 2018), pp.227-29, 279-80 and 299.

[11] B. Cheffins, *Corporate Ownership and Control: British Business Transformed* (Oxford: Oxford University Press, 2008), p.398.

[12] B. Cheffins and B. Reddy, "Will Listing Rule Reform Deliver Strong Public Markets for the UK?" (2023) 86 MLR 176, 179 (Figure 1).

companies in the private realm well beyond the point when they traditionally would have gone public.[13] In the U.K. the private capital/fate of the public company spotlight has recently swung back to private equity, with "the big beasts of private equity" reputedly now "focusing on their favourite feeding ground, the FTSE 250."[14]

If Poirot were surveying the troupe of suspects involved with the potential death of the U.K. public company, the accusation with private capital would run as follows. For some growing companies, such as those with large levels of intangible assets or businesses predisposed toward risky long-term projects, debt may not be a feasible financing option.[15] Lenders cannot easily take security over intangible assets,[16] do not share in the envisaged large upside, and likely face substantial default risk. Furthermore, a pre-profit (or even low profit) company may struggle to service regular interest payments. Accordingly, equity investment of some form likely will be essential.[17]

Equity finance has always been available in the private markets, but a lack of liquidity has conventionally been a deterrent for many deep-pocketed investors.[18] Stock exchanges have traditionally provided an avenue for companies to continue growing after exhausting private finance

---

[13] B. Cheffins, *The Public Company Transformed* (2018), pp. 345, 353-54. On the nature of venture capital, see B. Zider, "How Venture Capital Works" (1998) Harvard Business Review (November-December); BVCA, "Venture Capital Explained" https://www.bvca.co.uk/Our-Industry/Venture-Capital.

[14] Patrick Hosking, FTSE 250 at Risk as Private Equity Prepares to Take More British Companies Off the Table, Times, April 15, 2023, https://www.thetimes.co.uk/article/ftse-250-at-risk-as-private-equity-prepares-to-take-more-british-companies-off-the-table-wbz97n86x .

[15] M. Maher and T. Andersson, "Corporate Governance: Effects on Firm Performance and Economic Growth" (1999) OECD Publication 1, 36; V. Acharya and Z. Xu, "Financial Dependence and Innovation: The Case of Public Versus Private Firms" (2017) 124 Journal of Financial Economics 223, 238.

[16] C. Doidge et al, "Eclipse of the Public Corporation or Eclipse of the Public Markets?" (2018) 30 Journal of Applied Corporate Finance 8, 13.

[17] HM Treasury, *Financing Growth in Innovative Firms: Consultation* (August 2017), p.9.

[18] B. Black and J. Coffee, "Hail Britannia?: Institutional Investor Behavior under Limited Regulation" (1994) 92 Michigan Law Review 1997, 2071; J. Coffee, "Liquidity Versus Control: The Institutional Investor as Corporate Monitor" (1991) 91 Columbia Law Review 1277, 1318–1321; A. Röell, "The Decision to Go Public: An Overview" (1996) 40 European Economic Review 1071, 1074.

that might be available.[19] However, in recent years, vast levels of private, non-debt, funding has flooded global markets from the likes of VC and private equity funds which themselves collate capital from many of the same deep-pocketed institutional investors who also invest in listed companies. One could infer that such a rise in private capital diminishes the need for firms to rely on a stock exchange to generate growth finance.[20]

VC investment has indeed risen in the U.K. over the last ten years,[21] including for later-stage ventures.[22] With VC firms writing larger cheques at later stages in the life-cycles of private companies, the VC industry likely has played a role in the LSE's decline. Still, it must have accomplices. In the last five years, save for a post-pandemic surge in 2021 and early 2022, VC investment has largely plateaued in the U.K. as public listings of equity have continued to flounder (except for a modest IPO rebound in 2021).[23] In addition, the VC business model continues to envisage an exit, albeit later in a portfolio company's life-cycle, to crystallise VC investor returns.[24] To the extent fewer early-stage companies will go public due to plentiful private capital being available, this logically will lead to a dwindling of IPOs on the Alternate Investment Market (AIM), an exchange created by the LSE in 1995 to cater for smaller, less-developed companies. The pattern does not explain nearly as readily, however, why the LSE's "Main Market", comprised of larger, better-established listed companies has also

---

[19] W. Kim and M. Weisbach, "Motivations for Public Equity Offers: An International Perspective" (2008) 87 Journal of Financial Economics 281, 281; Department for Business, Energy & Industrial Strategy (DBEIS), *The Impact of Listing on Business Investment* (DBEIS, November 2022), p.9; Duncan Lamont, *What is the Point of the Equity Market?* (London: Schroeders, 2019), pp.2, 16-17.

[20] Elisabeth de Fontenay, 'The Deregulation of Private Capital and the Decline of the Public Company' (2017) 68 Hastings Law Journal 445, 459-461; S. Kumar, "Why are High-Growth Companies Staying Private for Longer?" (19 October 2021, *Torre Capital*) https://medium.com/torre-capital/why-are-high-growth-companies-staying-private-for-longer-126486a26e9b.

[21] KPMG, "Venture Pulse Q4 2019" (15 January 2020) 1, 68; KPMG, "Venture Pulse Q4 2022" (18 January 2023) 1, 62.

[22] KPMG, "Venture Pulse Q4 2022" (18 January 2023) 1, 52.

[23] KPMG, "Venture Pulse Q4 2022" (18 January 2023) 1, 62.

[24] Darryl Cooke, *Private Equity Law and Practice* (London: Sweet & Maxwell, 2021), 19.

suffered. Private companies that successfully grow to a size where VCs are seeking to exit should form part of the pipeline of companies for which a Main Market-listing on the LSE is a feasible option.[25]

Private equity plausibly is VC's partner-in-crime. For VC firms, an investee company exit option in addition to a public offering is a sale to a private equity firm. Private equity, which typically executes acquisitions rather than providing equity finance to companies in the manner of VC investment,[26] generally focuses on later-stage companies that may otherwise be prime listing candidates. However, similar to VC, with private equity U.K. acquisitions, there has been a plateau in the last five years.[27] Also, like VC funds, private equity funds have finite lifetimes, and, therefore, an exit from portfolio companies will inevitably be required.[28] Although multiple exit options exist, including acquisitions by other private equity firms (which will themselves be seeking an eventual exit) or sales to strategic acquirors, listing on a stock exchange such as the Main Market remains an option. Therefore, while the rise of private equity, as with the rise of VC, likely has contributed to a dearth of listings on the LSE there must be more going on.

In a previous article, we noted that a waning of IPOs only tells half the story with respect to the falling number of publicly traded companies on the LSE.[29] Plentiful exits from the excchange is just as important a factor in the decline of U.K. listed company numbers.[30] Private equity activity, as

---

[25] As has been noted in the US context, successful companies will ultimately stay "private for longer, not forever" (N. Bullock and R. Wigglesworth, "US Seeks Depth in the Listings Pool" (9 January 2018, *Financial Times*) https://www.ft.com/content/7457ee7e-f074-11e7-ac08-07c3086a2625.

[26] It should be noted that the difference between private equity and venture capital can sometimes be more opaque; variations exist in the use of the terms in different jurisdictions, and often with a degree of overlap (BVCA, "A Guide to Private Equity" (February 2010) 1, 6).

[27] KPMG, "UK Mid-Market PE Review" (February 2023) 1, 11; L. Hodgson, "UK and Ireland Private Equity in Five Charts" (7 September 2022, PitchBook) https://pitchbook.com/news/articles/uk-ireland-private-equity-trends.

[28] Darryl Cooke, *Private Equity Law and Practice* (London: Sweet & Maxwell, 2021), 19; B. Cheffins, *Corporate Ownership and Control: British Business Transformed* (Oxford: OUP, 2008), p.398-399.

[29] B. Cheffins and B. Reddy, "Will Listing Rule Reform Deliver Strong Public Markets for the UK?" (2023) 86 Modern Law Review 176, 208.

[30] B. Cheffins and B. Reddy, "Will Listing Rule Reform Deliver Strong Public Markets for the UK?" (2023) 86 Modern Law Review 176, 208.

anticipated by Jensen in 1989,[31] could be a crucial player in this context. However, between 2013 and 2022, only in three years did "public-to-private" acquisitions by special purpose vehicles commonly associated with private equity buyouts[32] reach double figures on the Main Market, and only in two years on AIM (Figures 1 and 2). Moreover, in only two and one of those years respectively did such private equity-style buyouts form a majority of all takeovers on the Main Market and AIM. Even though some have suggested that a weak pound since the Brexit vote in 2016 has led to the LSE becoming a delectable smorgasbord for a globally strong private equity industry,[33] there have not, as yet, been vast swathes of U.K. public companies de-listing as a result of private equity acquisitions.

[31] Fn. 9, and accompanying text.

[32] Data derived from Practical Law, "What's Market: Public M&A". All firm intentions to make an offer on the Main Market and AIM which did not either lapse, were withdrawn, or superseded by competing offers were included in the data. The Practical Law definition of "public to private" is "A bid for a listed company that is generally made by a newly incorporated unlisted company." The definition usually denotes the use of an acquisition vehicle by a private equity firm (although the numbers will overstate private equity takeovers where the relevant newly incorporated acquisition company has been established by other types of financial sponsors, including individuals and sovereign wealth funds, we have included these in the figures since such acquisitions are also customarily made with a view to eventual exit similar to the private equity business model).

[33] B. Marlow, "The weak pound has turned UK Plc into a sitting duck" (26 May 2022, *The Telegraph*) https://www.telegraph.co.uk/business/2022/05/26/weak-pound-has-turned-uk-plc-sitting-duck/; A. Massoudi et al, "SoftBank to Acquire UK's Arm Holdings for £24.3bn" (18 July 2016, *Financial Times*) https://www.ft.com/content/235b1af4-4c7f-11e6-8172-e39ecd3b86fc; "Big Bang to a Whimper" (2 October 2021, *The Economist*), p.9.

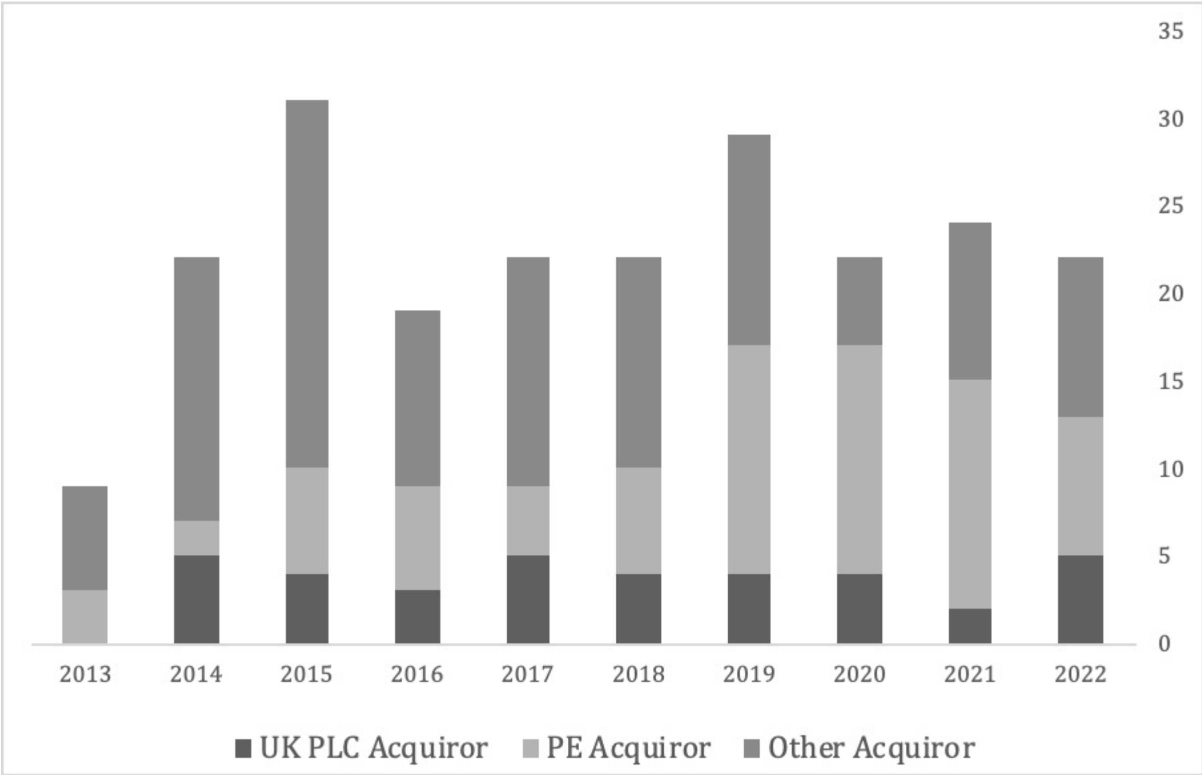

Figure 1: Main Market Announced Firm Intentions to Make Offers (not including offers lapsed, withdrawn or superseded by competing bids) 2013-2022

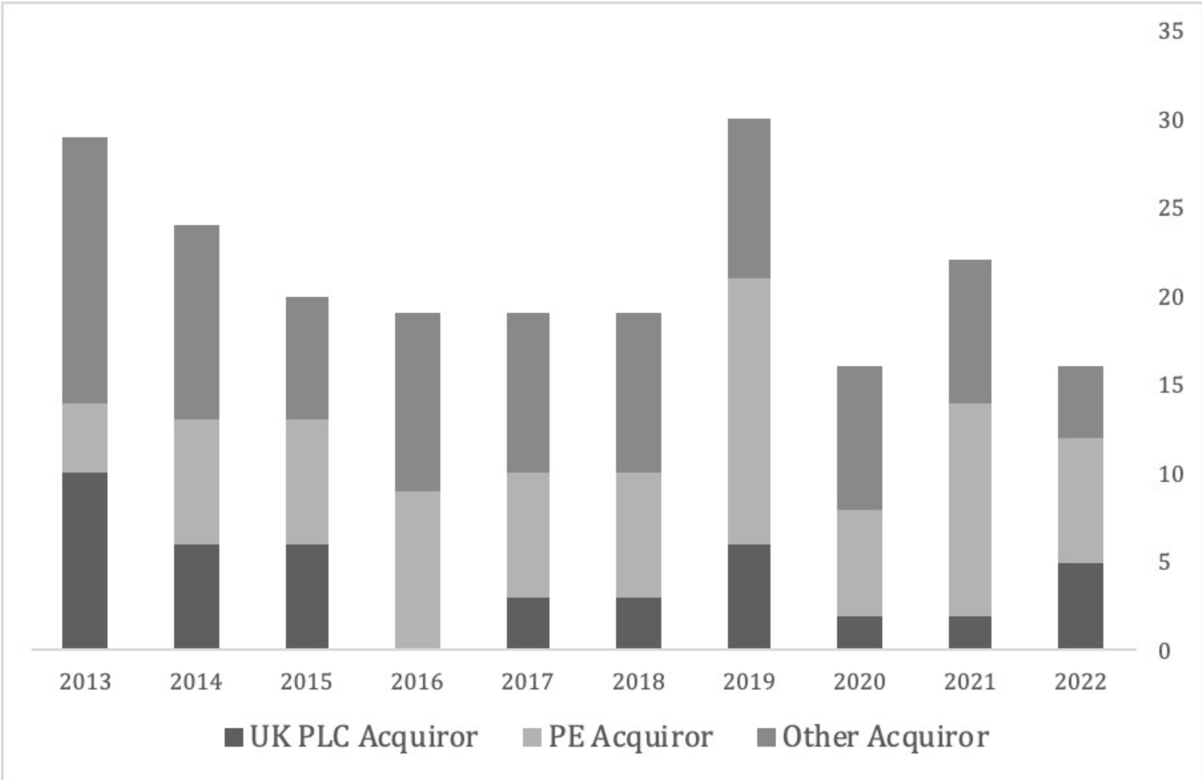

Figure 2: AIM Announced Firm Intentions to Make Offers (not including offers lapsed, withdrawn or superseded by competing bids) 2013-2022

In sum, with the diminished status of the public company on the LSE, the rise in the availability of private capital is culpable but cannot be the sole culprit. We will consider additional U.K.-specific suspects shortly. Before doing so, we pause to consider the extent to which the decline of U.K. equity markets is simply part of a global economic trend. To the extent that this is the case, presumably with cross-border factors in addition to the rise of private capital playing a role, the odds would be against Britain being able to pull policy levers that revive its stock market because the factors involved would be global rather than local.

While speculation about the public company's demise extends back to the late 1970s in the U.S.,[34] U.K. data provides a more forceful case than the U.S. that time has passed the stock market by.[35] In the U.S., since 2018, the ratio of the aggregate market capitalisation of publicly traded stocks to Gross Domestic Product (GDP) has typically been greater than previous record highs set in 1999 and 2000,[36] which indicates that the stock market is unprecedently large in relation to the American economy. Similarly, profits generated by publicly traded firms as a proportion of GDP has also been on an upward trend since the 1990s despite the declining number of publicly traded firms.[37] In contrast, in the U.K., the 1999 aggregate market capitalisation/GDP ratio of 1.75:1 has never been surpassed.[38]

The U.K. stock market has retreated relative to foreign peers generally, not just in relation to its American counterpart. Admittedly, the decline in the number of publicly traded EU companies was

---

[34] Fn. 8, and accompanying text.

[35] B. Cheffins and B. Reddy, "Will Listing Rule Reform Deliver Strong Public Markets for the UK?" (2023) 86 MLR 176, 178.

[36] GuruFocus, "USA Ratio of Total Market Cap over GDP" https://www.gurufocus.com/economic_indicators/4602/usa-ratio-of-total-market-cap-over-gdp

[37] M. Roe and C. Wang, "Are Public Firms Disappearing? Corporate Law and Market Power Analyses" (2023) unpublished working paper, 13 https://ssrn.com/abstract=4372070.

[38] B. Cheffins and B. Reddy, "Will Listing Rule Reform Deliver Strong Public Markets for the UK?" (2023) 86 MLR 176, 180 (Figure 2); CEIC, United Kingdom Market Capitalization: % of GDP, https://www.ceicdata.com/en/indicator/united-kingdom/market-capitalization--nominal-gdp .

similar to Britain's between 2009 and 2019 (-15% vs. -23%).[39] On the other hand, while the number of companies traded on the LSE was nearly two-fifths lower in 2020 (1,944) than in 1980 (3,141),[40] according to World Bank data the number of listed companies worldwide was nearly 250 per cent higher,[41] and global aggregate market capitalisation/GDP ratio hit a record high in 2020 of 1.33:1.[42] Moreover, between 2006 and 2021, the LSE's share of global equity values fell from 8.5% to 3.6%.[43] Collectively, then, while there is some contrary evidence, the U.K. stock market's decline has a substantial Britain-specific orientation. Accordingly, domestically-oriented explanations for Britain's stock exchange travails merit investigation. We turn in this direction next, with the first suspect being the U.K.'s regulatory and governance environment for listed companies.

Listing Rules and Over-Governance

A Poirot style investigation of U.K.-specific stock market culprits needs to take into account two related, possibly UK-specific, factors: overly-severe listing requirements, and unduly restrictive governance arrangements. Both could act as *ex ante* deterrents to listing, and serve as *ex post* incentives to de-list.

The severity of the listing requirements applicable to companies seeking to list on the Main Market has attracted the attention of the U.K. regulators and government officials focusing on the state of the stock market. In 2020, Jonathan Hill, at the behest of HM Treasury, commenced a review into the U.K.'s "primary" markets listing regime,[44] resulting in recommendations in early 2021 (the Hill

---

[39] W. Wright and E. Hamre, "The Problem With European Stock Markets" (March 2021), Fig. 8, https://newfinancial.org/wp-content/uploads/2021/03/2021.03-The-problem-with-European-stock-markets-New-Financial.pdf

[40] See sources cited by B. Cheffins and B. Reddy, "Will Listing Rule Reform Deliver Strong Public Markets for the UK?" (2023) 86 MLR 176, 179 (Figure 1).

[41] The World Bank, "Listed Domestic Companies, Total" https://data.worldbank.org/indicator/CM.MKT.LDOM.NO (17,273 in 1980, 43,248 in 2020).

[42] The World Bank, "Market Capitalization of Listed Domestic Companies (% of GDP)" https://data.worldbank.org/indicator/CM.MKT.LCAP.GD.ZS.

[43] "How to Revive London's Flagging Stock Market", *Financial Times*, 8 January 2022, 10.

[44] HM Treasury, *Call for Evidence – UK Listing Review* (19 November 2020).

Review)[45] intended to attract Main Market IPOs of early-stage, growth companies.[46] Having cited some dismal U.K. stock market statistics,[47] the Hill Review implicitly criticised the UK's listing regime for having put the LSE at a competitive disadvantage relative to other global exchanges by not attracting listings of the "companies of the future",[48] and explicitly suggested that the Main Market's listing requirements were "overly-complex" and consisted of "burdensome requirements".[49] The Hill Review further conjectured that a lack of flexibility in the listing regime was a "key factor" in "driving business to our competitors".[50]

The Hill Review spurred UK policymakers into action, and many of its recommendations were broadly implemented by the Main Market's regulator, the Financial Conduct Authority (FCA), over the course of 2021.[51] This initial phase of listing reform focused on perceived impediments that deter companies from listing in the first place. The regime was relaxed to allow firms to list on the Main Market's premium tier, the LSE's most prestigious segment,[52] with capital structures that give dominant individuals in companies going public the right to veto takeovers and preserve their board positions for a finite period of time post-IPO through the retention of shares with disproportionately high voting rights.[53] The relaxation was driven by a concern that other exchanges were more attractive to founders of high-growth, innovative companies especially susceptible to undervaluation and, accordingly, opportunistic takeovers at a time when their business prospects were not easily observable to public

---

[45] HM Treasury, *UK Listing Review* (3 March 2021) (Hill Review).

[46] Hill Review, p.19.

[47] Hill Review, p.1.

[48] Hill Review, p.1.

[49] Hill Review, p.2.

[50] Hill Review, p.2.

[51] FCA Policy Statement PS21/22, *Primary Market Effectiveness Review: Feedback and final changes to the Listing Rules* (December 2021).

[52] In relation to the differences between the premium and standard segments of the Main Market, and the reasons why the premium tier is the preferred option for most issuers, see B. Reddy, *Founders Without Limits: Dual-Class Stock and the Premium Tier of the London Stock Exchange* (Cambridge: Cambridge University Press, 2021), pp.47-52.

[53] See now the listing rules (LRs) applicable to Main Market-listed companies as promulgated by the FCA (the Listing Rules), LRs 9.2.22AR-9.2.22FR.

shareholders. The Main Market's free-float requirement – the level of shares required to be held in public hands – was also relaxed,[54] with a view to encouraging the flotation of companies not ready to distribute large levels of equity to public shareholders. Rules were also modified to promote the listing of special purpose acquisition companies (SPACs) on the Main Market.[55] SPACs are cash-shells professional sponsors list intending to acquire a private company. SPACs therefore represent a route companies, particularly those with innovative, complicated businesses, can use instead of listing directly to join the stock market.[56]

As of the time of writing, further reforms are on the cards targeting the secondary market – the raising of equity capital by firms that have already listed. A government-initiated Secondary Capital Raising Review[57] has made several proposals. These include reducing the period during which offers of shares to existing shareholders must remain open, and raising the threshold where a prospectus must be generated in support of further share issuances by publicly traded companies, together with removing the requirement for a sponsor to be appointed for such transactions.[58] Additionally, proposals have been made to give the FCA greater discretionary powers as to when prospectuses are required in lieu of the current statutory system,[59] and to relax the liability standard for "forward-looking statements" in

---

[54] See now LRs 5.2.2(2)G, 6.14.2(2)R and 14.2.2(3)R.

[55] See now LRs 5.6.8G, and 5.6.18AG-5.6.18FG.

[56] U. Rodrigues and M. Stegmoller, "Why SPACs: An Apologia" (2022) unpublished working paper 1, 27, 43 https://ssrn.com/abstract=4072834; B. Reddy, "Warning the UK on Special Purpose Acquisition Companies (SPACs): Great for Wall Street but a Nightmare on Main Street" (2022) 22 Journal of Corporate Law Studies 1, 6.

[57] HM Treasury, *UK Secondary Capital Raising Review* (July 2022) (Secondary Capital Raising Review).

[58] Secondary Capital Raising Review, pp.88, 93 and 110. The Secondary Capital Raising Review also made several proposals to encourage further retail investor participation in the public markets. These included urging the FCA to permit offerings larger than €8 million to be made to retail investors without the requirement for a prospectus (Secondary Capital Raising Review, p.63), relaxing the financial promotion rules which require an FCA-authorised person to approve marketing material submitted to retail investors (Secondary Capital Raising Review, p.78), reducing the period of time that an offer to issue shares in which retail investors can participate must remain open (Secondary Capital Raising Review, p.79), and exploring the use of technology to ease participation by retail investors in share offerings (Secondary Capital Raising Review, p.190).

[59] See the draft statutory instrument, Financial Services and Markets Act 2000 (Public Offers and Admissions to Trading) Regulations 2023 (Draft FSMA Regulations), regulation 8; Financial Services and Markets Act 2000 (FSMA 2000), s.71K (as proposed to be amended by the Financial Services and Markets Bill 2022-23).

company prospectuses from a negligence to a reckless standard.[60] A less onerous forward-looking statements regime potentially could facilitate IPOs in addition to secondary issuances since firms can explain their reasonable future prospects to public shareholders with less fear of litigation. Collectively, implementation of the proposed reforms should simplify the operational processes for existing listed companies seeking further equity finance from the public markets, with the implication being that restrictions associated with the current regime will no longer discourage firms from listing and remaining listed on the LSE.

As far as over-governance is concerned, its complicity in the LSE's listed company travails emerges from a supposed surfeit of legislation and regulatory rules that apply exclusively to Main Market-listed companies. For example, Main Market-listed companies must make disclosures regarding capital structure and distributions[61], publish directors' remuneration reports[62] subject to shareholder votes,[63] make lengthy periodic financial reports,[64] and implement mandatory audit overview arrangements.[65] Additionally, "premium tier" listed companies must produce detailed corporate governance statements relating to the U.K. Corporate Governance Code,[66] and are subject to shareholder approval requirements in relation to transactions involving related parties[67] and substantial assets.[68] Concerns have been raised that companies confronted with this barrage of requirements are

[60] See Draft FSMA Regulations, regulation 27 and Schedule 2 Part 2.

[61] Listing Rules, rules (LRs) 9.8.4–9.8.6

[62] Companies Act 2006 (CA 2006), s. 420.

[63] CA 2006, ss. 439 and 439A.

[64] See the rules promulgated by the FCA under the Disclosure Guidance and Transparency Rules sourcebook (DTRs), DTR 4.

[65] DTR 7.

[66] LRs 9.8.6(5) and 9.8.6(6). In relation to the propensity for the UK Corporate Governance Code to create greater costs than benefits for companies, see: B. Cheffins and B. Reddy, "Thirty Years and Done – Time to Abolish the UK Corporate Governance Code" (2023) Journal of Corporate Law Studies https://doi.org/10.1080/14735970.2022.2140496.

[67] Listing Rules, Chapter 11.

[68] Listing Rules, Chapter 10.

discouraged from listing.[69] Companies already listed are for their part ostensibly constantly contemplating escape from the stifling hand of public company governance.[70]

U.K. policymakers are aware that regulation could be a culprit with the decline of the publicly traded company. According to the 2021 Hill Review, "regulatory requirements on business…is one of the frequently cited reasons as to why there has been a trend of companies shifting from the public markets to private ones or never accessing the public markets at all."[71] Moreover, in 2022, the FCA consulted on a possible unification of the premium and standard tiers of the Main Market with deregulatory ramifications.[72] It was suggested in the context of such unification that issuers should be permitted, at the time of IPO, to disapply the requirement that planned substantial transactions be approved by shareholders.[73] For a growth company with an acquisitive strategy, such a relaxation could give it more flexibility, nimbleness and confidentiality when pursuing acquisitions.[74] Arm's decision to list in the U.S. rather than on the LSE fostered speculation that the FCA would under the proposed

---

[69] B. Wright, "Don't Blame Private Equity for the Red Tape Choking the Stock Market" (9 July 2021, *The Telegraph*) Business, 4; Department for Business, Innovation & Skills, *Investigation into the Motivations Behind the Listing Decisions of UK Companies* (BIS Research Paper No 126, August 2013), pp.44 and 46.

[70] A. Ralph, "Delisting has been a 'breath of fresh air' for Aveva" (24 March 2023, *The Times*) https://www.thetimes.co.uk/article/delisting-has-been-breath-of-fresh-air-for-aveva-g8zqsphlb; G. Searjeant, "Boardrooms Should Soak Up the Culture of Private Equity" (1 February 2007, *The Times*) https://www.thetimes.co.uk/article/boardrooms-should-soak-up-the-culture-of-private-equity-pcfdfc6hmc3.

[71] Hill Review, p.5.

[72] FCA Discussion Paper DP22/2, *Primary Markets Effectiveness Review: Feedback to the discussion of the purpose of the listing regime and further discussion* (May 2022).

[73] FCA Discussion Paper DP22/2, *Primary Markets Effectiveness Review: Feedback to the discussion of the purpose of the listing regime and further discussion* (May 2022), p.32. In relation to relaxing listing requirements, the FCA also proposed that the unified segment would not incorporate the premium tier's current three year revenue earning track record eligibility requirements, with the intention being to open the segment to early-stage high-growth companies which have yet to make significant profits (FCA Discussion Paper DP22/2, *Primary Markets Effectiveness Review: Feedback to the discussion of the purpose of the listing regime and further discussion* (May 2022), pp.23 and 25).

[74] Bobby Reddy, *Founders Without Limits: Dual-Class Stock and the Premium Tier of the London Stock Exchange* (Cambridge: Cambridge University Press, 2021), p.63.

unified segment permit firms to disapply the related-party transaction regime,[75] apparently a deal-killer for Arm when considering the LSE.[76] Whether or not the FCA follows through, it seems as if the regulators have accepted that over-governance could be hampering the LSE's listed company prospects.

Could relaxing listing requirements and alleviating the governance burden on listed companies reverse the fortunes of the public company in Britain? The fact that the initial phase of Main Market-focused listing reforms have not appreciably improved the LSE's situation raises doubts.[77] It is possible that those reforms were not sufficiently ambitious, as various commentators have suggested.[78] Alternatively, there may be deeper-seated issues at play which listing reforms cannot, in and of themselves, resolve. To the extent this is correct, the second phase of secondary markets reforms and any additional changes trailed in the 2023 Autumn statement are unlikely to move the needle materially.

With respect to over-governance, it remains to be seen whether the FCA proceeds with its plans to lessen the weight of continuing requirements on listed companies on a unified segment.[79] However, there is no indication the extensive disclosure obligations of listed companies will be reduced materially. Indeed, the FCA has suggested that companies listed on the proposed unified segment will need to apply the UK Corporate Governance Code, which means companies that formerly had a

---

[75] B. Martin, "London Considers Shake-Up of Key Listings Rules" (30 March 2023, *The Times*) https://www.thetimes.co.uk/article/london-considers-shake-up-of-key-listings-rules-nmlw5wmrz.

[76] J. Nimmo, "FCA Offers to Bend the Rules to Land Arm Float" (5 Febraury 2023, *The Sunday Times*) https://www.thetimes.co.uk/article/fca-offers-to-bend-the-rules-to-land-arm-float-7xmxl2nrz; A. Gross et al, "FCA Regulator Blamed for Arm's Decision to Shun London Listing" (3 March 2023, *Financial Times*) https://www.ft.com/content/40a0f9c1-3be1-4973-a473-3893a1675d28.

[77] With respect to the number of listed companies, 2022 was a poor year for the Main Market,. A small net increase of two issuers in 2021 was completely reversed in 2022, when there were 63 exits and only 42 new admissions (excluding reverse takeovers and global depositary receipt listings). 2022 was the joint fifth lowest year for new admissions on the Main Market since 1999. (Data derived from London Stock Exchange Reports https://www.londonstockexchange.com/reports?tab=issuers).

[78] B. Cheffins and B. Reddy, "Will Listing Rule Reform Deliver Strong Public Markets for the UK?" (2023) 86 Modern Law Review 176, 204; J. Payne and C. Pereira, "The Future of the UK IPO" (2022) 1, 29 https://ssrn.com/abstract=4029933; D. Thomas and P. Stafford, "UK Tech Sector Seeks More Listing Reforms to Keep IPOs Rolling" (7 February 2022, *Financial Times*) https://www.ft.com/content/363d8d3d-456c-4d73-b6ad-a9c778bdb2b5.

[79] See text accompanying fnn. 72-75.

"standard" listing will face new governance disclosure requirements as compared to now.[80] The lack of a regulatory appetite to confront listed company disclosure could well be a promising clue for a certain world-renowned, moustachioed detective to pursue with respect to the decline of U.K. equity markets. Nevertheless, overly zealous regulatory and governance stipulations are not fully culpable. AIM, for example, has suffered a similar decline to the Main Market in recent years,[81] even though it imposes far fewer disclosure requirements and has a considerably less prescriptive approach to governance than the LSE.[82] Additionally, the United States, where Arm and various other U.K.-based businesses have opted to list,[83] is hardly known for its lenient governance regime,[84] and U.S.-listed firms are subject to considerably greater litigation risk than their U.K-listed counterparts.[85]

The fact that the regulatory environment for listed companies cannot be the LSE's only source of public company strife means that market-oriented factors that disproportionately impact the U.K.'s listed company ecology probably are pertinent. We canvass leading suspects next.

Market-Oriented Factors

In this section, we discuss some of the UK-specific market-oriented considerations that could be incriminated in the decline of the U.K.'s equity markets. We begin with analyst coverage, consider

[80] FCA Discussion Paper DP22/2, *Primary Markets Effectiveness Review: Feedback to the discussion of the purpose of the listing regime and further discussion* (May 2022), pp.31 and 32.

[81] B. Cheffins and B. Reddy, "Will Listing Rule Reform Deliver Strong Public Markets for the UK?" (2023) 86 Modern Law Review 176, 179 (Figure 1).

[82] B. Cheffins and B. Reddy, "Thirty Years and Done – Time to Abolish the UK Corporate Governance Code" (2023) Journal of Corporate Law Studies 1, 15 https://doi.org/10.1080/14735970.2022.2140496.

[83] See text accompanying fn. 2; B. Dummett et al, "New York Beats London to Land Arm IPO, One of Year's Largest" (4 March 2023, *Wall Street Journal*) A1.

[84] O. Shah, "New York is No Fairytale Solution for those Tired of Life in the FTSE" (26 February 2023, *The Times*) https://www.thetimes.co.uk/article/new-york-is-no-fairytale-solution-for-those-tired-of-life-in-the-ftse-00qcdrhlp.

[85] B. Reddy, *Founders Without Limits: Dual-Class Stock and the Premium Tier of the London Stock Exchange* (Cambridge: Cambridge University Press, 2021), pp.348-351.

investor culture and composition, take the size of companies traded into account, and conclude by considering managerial capabilities.

Insufficient Analyst Coverage

It is reasonably intuitively obvious why the rise of private capital and onerous regulatory arrangements applicable to publicly traded companies could have an adverse impact on the health of the stock market. With the decline of the LSE's equity markets, the relevance of a market-oriented factor - poverty of issuer analyst coverage[86] - is less obvious. Still, research analyst coverage is a plausible suspect.

A 2023 HM Treasury review into analyst coverage noted that "low levels of investment research can make it harder to value companies and…for companies to attract investors" and suggested that good analyst coverage ensures that companies "obtain the valuations they deserve".[87] More formally, analyst coverage can potentially influence a stock market's "informational efficiency" – the extent to which information relevant to an issuer is impounded in the share price – and "fundamental efficiency" – the extent to which share price reflects the actual value of an issuer.[88] Greater analyst coverage can increase market liquidity and perhaps bolster share prices,[89] and further decrease volatility in the face of rumour and speculation.[90] The corollary of poor analyst coverage with the LSE is that companies will fail to enjoy well-grounded and perhaps more generous valuations available elsewhere, which will deter LSE IPOs and, for those compaies that do list on the LSE, provide an incentive to change their listings to another exchange. Similarly, undervalued existing LSE issuers could find

[86] HM Treasury Policy Paper, *Terms of Reference – Investment Research Review* (3 April 2023).

[87] HM Treasury Policy Paper, *Call for Evidence – UK Investment Research Review* (3 April 2023).

[88] J. Armour and B. Cheffins, "Stock Market Prices and the Market for Corporate Control" (2016) 3 University of Illinois Law Review 761, 766-768.

[89] P. Irvine, "The Incremental Impact of Analyst Initiation of Coverage" (2003) 9 Journal of Corporate Finance, 431, 437, 448.

[90] M. Brennan et al, "Investment Analysis and the Adjustment of Stock Prices to Common Information" (1993) 6 The Review of Financial Studies 799; J-M. Sahut et al, "Stock Volatility, Institutional Ownership and Analyst Coverage" (2011) https://ssrn.com/abstract=1735324.

themselves subject to opportunistic takeovers by acquirors prepared to investigate closely the business fundamentals of potential targets to identify bargains.

Why the dearth of investment research on the LSE? A 2014 FCA missive that asset managers should only accept investment research services from brokers executing their trades if the research was "substantive" has been cited.[91] The U.K.'s 2018 implementation of the EU's revised Markets in Financial Instruments Directive (MiFID II),[92] which required asset managers to split the costs of trading activities from investment research, has also been blamed. MiFID II in particular has been blamed for asset managers cutting research analysis budgets.[93]

With the U.K.'s departure from the EU, the U.K. disapplied MiFID II's investment research "unbundling" rules in 2022 for issuers with market capitalisations of less than £200 million.[94] Complete abolition could now be on the agenda. However, perhaps regulation affecting investment research, including MiFID II, has been falsely accused. The public company decline in the U.K. was evident before the FCA's 2014 reforms,[95] and certainly well before MiFID II's implementation in 2018.[96] Additionally, while AIM has experienced a similar decline to the Main Market recently,[97] MiFID II's

---

[91] FCA Policy Statement PS14/7, *Changes to the Use of Dealing Commission Rules: Feedback to CP13/17 and Final Rules* (May 2014).

[92] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (recast) (OJ L 173, 12.6.2014, pp. 349-496).

[93] H. Agnew et al, "Arm's Flotation on Nasdaq 'A Huge Potential Blow' to London" (11 February 2022, *Financial Times*) https://www.ft.com/content/f99b7980-8f2c-4633-9c9b-1f6f0475daa3; A. Timms, "After Years of Talk, MiFID II is Live. Here's How it's Already Changing the Research Business" (28 March 2018, *Institutional Investor*) https://www.institutionalinvestor.com/article/b17jgmg3dls3mz/after-years-of-talk,-mifid-ii-is-live-here's-how-it's-already-changing-the-research-business.

[94] FCA Policy Statement PS21/20, *Changes to UK MIFID's Conduct and Organisation Requirements* (November 2021).

[95] fn. 91.

[96] fn. 92.

[97] B. Cheffins and B. Reddy, "Will Listing Rule Reform Deliver Strong Public Markets for the UK?" (2023) 86 Modern Law Review 176, 179 (Figure 1).

impact on the extent of research analysis has been greater on the Main Market than on AIM[98] where nominated advisors appear to have filled the research gap.[99] Furthermore, deficiencies in analyst coverage are thought to be especially acute for innovative, high-growth, especially tech, companies.[100] There does not seem to be an obvious reason why MiFID II should have disproportionately impacted the amount of tech company coverage. On the contrary, tech is known for high levels of intangible assets not valued in accounts, and is therefore an industry which could especially benefit from professional research.[101]

In sum, although reversing MiFID II may help with fostering analyst coverage and bolstering the public company in the U.K., it is unlikely to be the complete solution.[102] At least two further factors complicate matters. First, there may well be a "chicken-and-egg" scenario revoking MiFID II will not solve. To the extent that the LSE lacks a substantial cohort of growth-focused companies and an IPO pipeline featuring such firms, even absent MiFID II, it will not be cost effective for investment banks to build up analysis expertise in this space.[103] Likewise, without analyst coverage, it is unlikely the substantial cohort of growth-focused companies will emerge in the first place. Second, companies prioritising long-term growth rather than current profitability may not appeal to LSE investors, meaning that the investment community will not be inclined to pay for, or factor-in, applicable investment

---

98 Anqi Fu et al, 'Research Unbundling and Market Liquidity: Evidence from MiFID II' (2022) 1, 2 https://ssrn.com/abstract=3991912; J. Cox, "MiFID and UK Small-Caps: How Bad is it?" (4 March 2019, *Global Capital*) https://www.globalcapital.com/article/28mts1wjsrfaw4lipraps/regulation/mifid-and-uk-small-caps-how-bad-is-it.

99 Anqi Fu et al, 'Research Unbundling and Market Liquidity: Evidence from MiFID II' (2022) 1, 2 https://ssrn.com/abstract=3991912. AIM issuers are required to have a corporate advisor known as a "nominated advisor" or "NOMAD" (LSE, *AIM Rules for Companies* (1 January 2021), Rule 1.

100 E. Anderson, "British Tech Companies Should List in the US, Nasdaq Boss Says" (17 November 2014, *The Telegraph*) https://www.telegraph.co.uk/finance/markets/11234274/British-tech-companies-should-list-in-the-US-NASDAQ-boss-says.html; Briefing, "Britain's Sluggish Stockmarket" (2 October 2021, *The Economist*) 18; HM Treasury Policy Paper, *Terms of Reference – Investment Research Review* (3 April 2023).

101 M. Barth et al, "Analyst Coverage and Intangible Assets" (2001) 39 Journal of Accounting Research 1, 2.

102 D. Thomas, "Ditching Mifid Research Rules Will Help London Market But is No Panacea" (23 March 2023) https://www.ft.com/content/a3c424f0-aea7-42e1-bd9c-2032ace7b44c.

103 Briefing, "Britain's Sluggish Stockmarket" (2 October 2021, *The Economist*) 18.

research on such firms. Such potential investor deficiencies merit independent investigation when assigning blame for the decline of the public company, and we take up this point next.

Investor Deficiencies

Those running a privately held company might be eager to exit (at least partially) via the stock market and/or raise equity capital but such aspirations are dependent upon the "buy side" - investors prepared to purchase shares made available to the public.[104] "Buy side" shortcomings have been identified as a market-oriented explanation for the U.K.'s stock market travails. For instance, in 2023 the *Times* declared "Until the City 'Gets' Tech, British Companies Will Keep Crossing the Pond."[105] The *Economist* elaborated, saying "Tech bosses…have been left with an uncomfortable suspicion that the City's equity investors simply aren't interested in the kind of innovative firms they are trying to build."[106] The LSE loses in turn because companies that otherwise might contemplate an LSE IPO either remain private or seek a U.S. listing, and because existing LSE-listed firms have incentives to forsake Britain in favour of a U.S. listing.

Two related charges have been laid against the U.K. buy side: (1) domestic investors have little interest in buying shares traded on the LSE; and (2) to the extent there is demand for shares, the investors are counterproductively cautious. On point (1), despite £4.6 trillion of assets British pension and insurance funds hold,[107] reputedly "There are no domestic equity investors here", which could mean that with respect to factors involved with U.K. equity markets decline "everything else is a symptom".[108]

---

[104] On the "buy side" with equity markets, see B. Cheffins, *Corporate Ownership and Control: British Business Transformed* (2008), pp.8-9 and 85.

[105] K. Prescott, "Until the City 'Gets' Tech, British Companies Will Keep Crossing the Pond" (29 March 2023, *The Times*) https://www.thetimes.co.uk/article/until-the-city-gets-tech-british-companies-will-keep-crossing-the-pond-0x6d8v30z.

[106] "Punishment Beating" (29 January 2022, *The Economist*) 23.

[107] "Tiddlers, Not Titans" (25 June 2022, *The Economist*) 16.

[108] N. Asgari et al, "There are no Domestic Equity Investors: Why Companies are Fleeing London's Stock Market" (4 March 2023, *Financial Times*) https://www.ft.com/content/eb872818-22be-4be3-9abe-4d8c0f8a074f.

According to a *Financial Times* analysis of the "City's malaise", "dwindling investment of U.K. pension schemes" has been a "particular bone of contention".[109]

As for point (2), with respect to those who might be prepared to own shares, they reputedly prioritise companies with steady profits and reliable dividends at the expense of firms with uncertain but substantial upside potential. Accordingly, firms with a growth agenda, such as those in tech, "worry City investors are too focused on short term profits to take their businesses seriously",[110] or, according to a London-based VC quoted in the *Economist*, the LSE "attracts an old fashioned institutional base that doesn't fully comprehend the new economy."[111] In addition, according to Sir Nigel Rudd, nicknamed "the Man Who Sold Britain" due to overseeing as board chair the sale of various well-known U.K. companies,[112] "The UK market doesn't like UK companies acquiring things. They [fund managers here] are very risk-averse...and executives are very fearful of the reaction of shareholders."[113] If there is truth to this characterisation, it is no wonder that UK investors have little appetite for investment research focusing on growth-focused companies.[114]

American equity markets stand, at least by reputation, in sharp contrast. While with a dearth of domestic-based LSE investors "(l)iquidity is more puddle than pool"[115] according to media reports the U.S. features a "deep investor pool"[116] comprising "more people, more money and more

---

[109] H. Thomas, "Pension Fund Wariness Only Adds to City's Malaise", (4 October 2022, *Financial Times*) 12.

[110] "Don't Gloat About the Float" (23 July 2022, *The Economist*) 21.

[111] "Order Floww" (19 March 2022, *The Economist*) 24. See also "Start Up, Fade Away" (25 June 2022, *The Economist*) 23 ("Tech firms perceive mainstream British asset managers as being somewhere between indifferent and hostile, prizing earnings today over the promise of growth tomorrow"). See also N. Asgari et al, "There are no Domestic Equity Investors: Why Companies are Fleeing London's Stock Market" (4 March 2023, *Financial Times*) https://www.ft.com/content/eb872818-22be-4be3-9abe-4d8c0f8a074f ("Domestic UK investors have not evolved with the times").

[112] R. Marsden, "How the Man Who Sold Britain Made His Money" (3 September 2021, *The Daily Mail*) 16.

[113] O. Shah, "How do You Solve a Problem Like the FTSE?" (26 September 2021, *The Sunday Times*) Business & Money, 2.

[114] See the section: *Insufficient Analyst Coverage*.

[115] O. Shah, "New York is No Fairytale Solution for those Tired of Life in the FTSE" (26 February 2023, *The Times*) https://www.thetimes.co.uk/article/new-york-is-no-fairytale-solution-for-those-tired-of-life-in-the-ftse-00qcdrhlp.

[116] B. Masters, "The EU Has a New Weapon in the Stock Market Battle" (8 December 2021, *Financial Times*) https://www.ft.com/content/5bd53ec1-41a2-4aef-bb94-561c27208f81.

specialisation"[117] that yields "depth of liquidity".[118] Access to a greater number of investors is a draw for British businesses looking Stateside,[119] but a belief investors give companies higher valuations likely is a greater driver.[120]

With a global industry such as Arm's (semiconductors), firms logically should be valued the same regardless of where they are listed.[121] Still, the received wisdom is that the U.S. is "an environment that embraces higher growth" in a way U.K. equity markets do not.[122] A NYSE company executive elaborated in a 2023 interview: "The U.S. investor base has an understanding and appreciation of the future earnings, and so they assign a better present value to future earnings for a pre-revenue or pre-profitable company."[123] For instance, while asset managers in the U.K. want to know for a pre-profit company "when it will be profitable", in the U.S., investors "want the companies they invest in

---

[117] S. Foy, "LSE Battles to Plug Tech Drain as New York Woos Start-ups" (2 February 2021, *The Telegraph*) Business, 4 (quoting the CEO of a UK-based software firm).

[118] C. Jones, "Give Us Your Undervalued Firms, New York Tells the City" (11 March 2023, *The Times*) https://www.thetimes.co.uk/article/give-us-your-undervalued-firms-new-york-tells-the-city-5zxlr5bkj (quoting a New York Stock Exchange executive).

[119] "FTSE 100 Companies Make More Money in US than UK" (22 March 2023, *The Telegraph*) Business, 18.

[120] B. Dummett et al, "New York Pushes London Aside in Battle of Financial Centers" (3 March 2023, *The Wall Street Journal*) https://www.wsj.com/articles/chip-designer-arm-intends-to-list-in-new-york-12210e53. See also P. Hosking, "London's Calling Falls on Deaf Ears for Firms Looking to List" (4 March 2023, *The Times*) https://www.thetimes.co.uk/article/london-s-calling-falls-on-deaf-ears-for-firms-looking-to-list-3v2s3p3qt (quoting the head of research at a London broker firm as saying with regard to the "magnetic pull" of the US "it's all to do with valuation".)

[121] J. Thornhill, "Britain Must Boost its Technological-Financial Complex" (10 February 2022, *Financial Times*) https://www.ft.com/content/a45764ba-3fe9-4bf9-a21d-ea290faf3f3c.

[122] N. Asgari et al, "There are no Domestic Equity Investors: Why Companies are Fleeing London's Stock Market" (4 March 2023, *Financial Times*) https://www.ft.com/content/eb872818-22be-4be3-9abe-4d8c0f8a074f. See also D. Thomas, "More Risk, Fewer Rules: the Plan to Revive the City of London" (15 February 2023, *Financial Times*) https://www.ft.com/content/477318a9-5b05-4305-9e0d-f605431692db (New York investors "get growth").

[123] C. Jones, "Give Us Your Undervalued Firms, New York Tells the City" (11 March 2023, *The Times*) https://www.thetimes.co.uk/article/give-us-your-undervalued-firms-new-york-tells-the-city-5zxlr5bkj.

to grow market share - market share really excites U.S. fund managers".[124] Correspondingly, for companies traded on the LSE, "(a)nyone shifting a listing [to the U.S.] hopes for a pleasant one-off bump higher in the share price".[125] Waiting for deep-pocketed, growth-focused U.S. investors to seek out and buy shares traded on the LSE will be futile because many have policies barring the purchase of securities on foreign exchanges and others typically prefer to avoid the currency risk and other challenges associated with investing abroad.[126]

How did the buy side end up in such a problematic state? With weak domestic investor demand, the chronology is straightforward. The proportion of shares in publicly traded U.K. firms held by domestically-based pension funds and insurance companies increased from 16% in 1963 to 52% by 1993 and then fell precipitously to under 10% by 2014 and below 5% by 2020.[127] Foreign owners

---

[124] G. Wearden, "Can London Stock Market Shake Off Dinosaur Image to Boldly Go?" (4 January 2022, *The Guardian*) https://www.theguardian.com/business/2022/jan/04/can-london-stock-market-shake-off-dinosaur-image-to-boldly-go (quoting an executive from a U.K. based asset manager). See also E. Warner, "America's Frontier Spirit Leaves City in the Dust in the Race for Flotations" (13 March 2023, *The Times*) https://www.thetimes.co.uk/article/americas-frontier-spirit-leaves-city-in-the-dust-in-the-race-for-flotations-w69x3f258 (American investors "have proved much more willing to embrace the unusual, novel, unconventional or simply hyper-aspirational").

[125] P. Hosking, "London's Calling Falls on Deaf Ears for Firms Looking to List" (4 March 2023, *The Times*) https://www.thetimes.co.uk/article/london-s-calling-falls-on-deaf-ears-for-firms-looking-to-list-3v2s3p3qt. See also H. Agnew et al, "Arm's Flotation on Nasdaq 'A Huge Potential Blow' to London" (11 February 2022, *Financial Times*) https://www.ft.com/content/f99b7980-8f2c-4633-9c9b-1f6f0475daa3 (quoting a veteran UK fund manager as saying "If you want the highest price…surely you'll list in the country with the highest appetite for risk"). For an example see T. Wilson and H. Agnew, "Can Shell Close the Valuation Gap With US Rivals" (3 March 2023, *Financial Times*) https://www.ft.com/content/1d3b8a08-f5e0-4dd1-9b39-b07b39f11d40 (Exxon and Chevron were valued at six times cash flow trading in the U.S. as compared with three times for LSE listed Shell).

[126] B. Dummett et al, "New York Pushes London Aside in Battle of Financial Centers" (3 March 2023, *The Wall Street Journal*) https://www.wsj.com/articles/chip-designer-arm-intends-to-list-in-new-york-12210e53.

[127] Office for National Statistics (ONS), *Ownership of UK Quoted Shares 2020* https://www.ons.gov.uk/economy/investmentspensionsandtrusts/bulletins/ownershipofukquotedshares/2020.

primarily filled the gap, with the proportion of shares held by such investors increasing from 4% in 1981 to 36% by 2001 and to 56% by 2020.[128]

As for why key domestic institutional investors retreated from their previously dominant role, due to tougher pensions regulation, changes to the accounting treatment of pensions in company accounts and maturing workforces, pension funds became obliged to pay much more attention to imminent payout obligations than they had to in the past. Accordingly, bonds matched-up with their priorities better than shares, and pension funds, also mindful of the 1997 abolition of a *de facto* exemption from paying income tax on dividends, switched steadily out of shares. Investment in UK equities was hit particularly hard as pension fund trustees simultaneously sought to increase global exposure.[129] Regulatory changes designed to fortify insurer financial buffers prompted insurance companies to join pension funds in exiting from UK equities.[130]

With respect to the reputed investor bias in favour of caution, the orientation has been described as "deeply cultural"[131] featuring a "risk-averse and complacent" City.[132] At least as far back as the 1980s, numerous industrialists, economists and politicians were lamenting that publicly traded companies were counterproductively forsaking long-term success to keep onside investors interested only in short-term earnings data and the next dividend pay-out.[133] The fact that a 2007 London School

[128] ONS *Ownership of UK Quoted Shares 2020* https://www.ons.gov.uk/economy/investmentspensionsandtrusts/bulletins/ownershipofukquotedshares/2020.

[129] B. Cheffins, *Corporate Ownership and Control: British Business Transformed* (2008), pp.388-90. See also W. Wright, *What Are Stock Exchanges For and Why Should We Care?* (New Financial/Pension Insurance Corporation, 2019), p.38. The dynamics remain similar today. See, for example, H. Agnew et al., "Corporate Rush to Offload Pensions Adds to Pressure on UK Equities" (10 March 2023, *Financial Times*) https://www.ft.com/content/eee78bf3-9cae-4211-875c-cde85ca19e5d.

[130] B. Cheffins, *Corporate Ownership and Control: British Business Transformed* (2008), pp.387-88.

[131] O. Shah, "Why a British Elon Musk Remains Light Years Away" (17 April 2022, *The Times*) Business and Money, 9.

[132] D. Thomas, "More Risk, Fewer Rules: the Plan to Revive the City of London" (15 February 2023, *Financial Times*) https://www.ft.com/content/477318a9-5b05-4305-9e0d-f605431692db.

[133] C. Wolman, "Keynes Followers Rally Behind Industrialists" (3 March 1987, *Financial Times*) 8; D. Clutterbuck and D. Bowen, *The Decline and Rise of British Industry* (London: Mercury Books, 1988), pp.311-14; "At Odds, Again" (2 March 1991, *The Economist*) 94.

of Economics study of AIM remarked "the success of AIM has prompted imitation, envy and criticism from around the world"[134] suggests British investor predilections have hardly always been "anti-growth". Nevertheless, as the 2000s got underway, concerns were being expressed that because risk-averse fund managers preferred to take stakes in big companies, medium-sized UK firms were being deprived of the benefits that they expected from going public.[135]

Investor-related reform is currently on the agenda. The Chancellor of the Exchequer's March 2023 budget speech indicated that "measures to unlock productive investment from defined contribution schemes and other sources" would be detailed in the 2023 Autumn statement.[136] Revamping accounting rules governing companies sponsoring pension plans that require such firms to hold pension fund deficits on their balance sheets is a change advocates of reform have identified.[137] As for insurance companies, the reform most often mooted is relaxing Solvency II,[138] an EU measure that reduced for insurers the appeal of shares as investments by increasing the amount of capital insurers had to hold against riskier assets.[139] It is possible that implementation of such reforms would foster domestic-based demand for U.K. equities to some degree but, even so, the risk aversion which ostensibly affects City investors in a way that prompts U.K. companies to look Stateside seemingly would go unaddressed.

---

[134] S. Arcot et al, *From Local to Global: The Rise of AIM as a Stock Market for Growing Companies* (London: LSE, 2007), p.9.

[135] D. Smith, "Middle Market Demands a Better Deal from Investors" (17 June 2001, *The Sunday Times*) Business, 12.

[136] I. Smith et al, "Executives Dismayed That Reforms to Boost London Stock Market Yet to Come" (16 March 2023, *Financial Times*) https://www.ft.com/content/89c72d58-b095-4ea7-b2ef-34898613b398.

[137] E. Dunkley, "Fund Managers Call for Pensions Rule Change to Revive UK Stock Market" (10 March 2023, *Financial Times*) https://www.ft.com/content/db531562-73bf-49f8-bc2a-fd2af2911d91.

[138] Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (OJ L 335 17.12.2009, pp.1-155).

[139] W. Wright, *What Are Stock Exchanges For and Why Should We Care?* (New Financial/Pension Insurance Corporation, 2019), pp.38 and 41; D. Thomas, "More Risk, Fewer Rules: the Plan to Revive the City of London" (15 February 2023, *Financial Times*) https://www.ft.com/content/477318a9-5b05-4305-9e0d-f605431692db; "Capital Ideas" (24 September 2022, *The Economist*) 27.

No "Winner-Take-All" Companies

While investor deficiencies could be credible culprits with the decline of U.K. equity markets, other distinctive market-oriented aspects of the U.K.'s corporate economy also deserve investigation. As discussed above, while both the U.K. and U.S. have seen a decline in the number of listed companies, unlike the U.K., the U.S. has seen a rise in its aggregate market capitalisation/GDP ratio.[140] It might seem paradoxical that the number of publicly traded firms can move down while aggregate market capitalisation/GDP ratio can move up. The U.S. paradox can be resolved readily: companies that are publicly traded today are worth considerably more on average than their stock market forerunners.[141] Furthermore, a trend potentially explains why the number of publicly traded firms can fall while the size of firms traded on the stock market increases – namely an economy that increasingly operates on a "winner-take-all" basis.[142] This logic resonates in the American context. Not so much in Britain, though.

Explanations for the emergence of a winner-take-all corporate economy tend to focus on "network" effects where firms with a dominant position benefit because customers find that switching to a competitor is a self-defeating strategy (for example, internet search engines) and on first mover advantages already dominant firms have when refining new technologies and getting products to market. In this environment, small enterprising companies will often be worth more as part of large companies than they are as independent entities. Operators of small private companies thus will do

---

[140] See text accompanying fnn. 36-38.

[141] B. Cheffins, "Rumours of the Death of the American Public Company are Greatly Exaggerated" (2019) 40(1) Company Lawyer 4, 10.

[142] On this line of reasoning see X. Gao et al, "Where Have All the IPOs Gone?" (2013) 48 Journal of Financial & Quantitative Analysis 1663; B. Tingle et al, "The IPO Market in Canada: What a Comparison with the United States Tells Us about a Global Problem" (2013) 54 Canadian Business Law Journal 321, 355-56; M. Roe and C. Wang, "Are Public Firms Disappearing? Corporate Law and Market Power Analyses" (2023) unpublished working paper 1, 18-20 https://ssrn.com/abstract=4372070.

better by selling out by way of a "trade sale" to a dominant incumbent than by trying to operate as an independent firm relying on internal growth. Since dominant incumbents are likely to be publicly traded themselves, when they use acquisitions to scale-up in this way the stock market should grow even though the number of public companies will be declining due to smaller companies eschewing IPOs. Additionally, the winner-take-all approach is consequential for the impact of listed company exits on the health of a stock exchange.[143] If publicly traded firms are simply being taken over by other publicly traded firms on the same exchange, the market capitalisation of the exchange will not substantially suffer, since the relevant assets remain on the market.[144]

The winner-take-all process apparently works differently in the U.K. Reputedly, with the life cycle of companies, "(a)t the early stages, Britain excels"[145] but "Britain has fallen down…in turning fledgling companies into listed worldbeaters".[146] "To nurture a British Amazon, Alphabet or Microsoft is a dream of policymakers,"[147] but larger firms on the UK stock market have been described as "mature, old economy companies where the task is simply that of managing decline".[148] As of 2022, the average age of the five biggest firms with headquarters in Britain was 135 and none was worth over $250 billion,[149] substantially below the $314 billion threshold for the 20 largest firms in America's S&P 500

[143] See text accompanying fn. 30.

[144] B. Eckbo and M. Lithell, "Follow the Assets: Is the US Listing Gap 'Real'?" (2020) un-published working paper,1, 1-2 https://gess.unimannheim.de/fileadmin/user_upload/2020_Eckbo_Lithell_Follow_the_Assets__2020_.pdf.

[145] "Start Up, Fade Away" (25 June 2022, *The Economist*) 23.

[146] "Oversold, Over Here" (15 May 2021, *The Economist*), 67. See also A. Gross and T. Bradshaw, "UK Gaming Veterans Call for Investment in British Companies" (28 February 28 2022, *Financial Times*) https://www.ft.com/content/605e06bf-68a6-4646-b777-faf49b35a338 (quoting a video game executive as saying "We find it hard to go beyond a certain growth stage without being acquired"); "Tiddlers, Not Titans" (25 June 2022, *The Economist*) 16 ("Britain is not a good place to turn promising startups into titans").

[147] P. Hosking & K. Prescott, "London Stock Exchange Still Stuck With its Jurassic Park Image" (27 August 2022, *The Times*) https://www.thetimes.co.uk/article/london-stock-exchange-still-stuck-with-its-jurassic-park-image-kl9hdkb7j.

[148] E. Warner, "America's Frontier Spirit Leaves City in the Dust in the Race for Flotations" (13 March 2023, *The Times*) https://www.thetimes.co.uk/article/americas-frontier-spirit-leaves-city-in-the-dust-in-the-race-for-flotations-w69x3f258.

[149] "Start Up, Fade Away" (25 June 2022, *The Economist*) 23.

index of shares.[150] Leading firms of such modest size will not provide the UK equity markets with the vibrancy that compensates for fewer listed companies.

In relation to the acquisition of existing publicly traded companies, Figures 1 and 2 above show that only a small minority of U.K.-listed company takeovers are by other U.K.-listed firms. In contrast, between 1990 and 2020, U.S.-listed corporations were three times more likely to be acquired by other domestic listed firms than was the case in other advanced economies.[151] Hence, while a winner-take-all economy potentially plays itself to something of a draw with the U.S. stock market – fewer but larger publicly traded firms – in Britain the other shoe does not fall, in the form of its large firms growing at a rate sufficient to sustain the vibrancy of the stock market. But who is to blame? We have already discussed that investors on the LSE may for various reasons not be supportive of the growth-oriented firms that could potentially become winner-take-all companies,[152] but Britain's public company executives might also be culpable. We pivot to a brief assessment of the U.K.'s managerial capabilities next.

Managerial Capabilities

Unlike some of the other factors discussed in this article, managerial shortcomings are not often identified as a prime suspect for the U.K.'s equity market woes, but this factor deserves further examination in two respects. First, those running fledgling businesses in Britain arguably lack the drive and ambition to scale-up their ventures by way of a public offering of shares, thereby compromising the IPO-pipeline. Second, those managing companies that are already publicly traded may not be well-

---

[150] Statista, Market capitalisation of Largest Companies in S&P 500 Index as of April 22, 2022 https://www.statista.com/statistics/1181188/sandp500-largest-companies-market-cap/.

[151] B. Eckbo and M. Lithell, "Merger-Driven Listing Dynamics" (2022) un-published working paper 1, 47 https://ssrn.com/abstract=3547581; M. Roe and C. Wang, "Are Public Firms Disappearing? Corporate Law and Market Power Analyses" (2023) unpublished working paper 1, 23 https://ssrn.com/abstract=4372070.

[152] See text accompanying fnn. 110-113 above.

suited to push their companies to global dominance, meaning that the LSE lacks the huge firms that have sustained the vibrancy of American stock markets despite a decline in the number of publicly traded companies.

Claims that amateurish management are compromising the prospects of British business success have featured since at least the early 20th century.[153] Still, while "(t)here is a large literature blaming long-term decline on sloth, complacency and amateurism,"[154] 21st century Britain does not lack entrepreneurial verve. The *Telegraph*, in a 2012 article on tech companies, said "(t)he UK is a nation of innovators."[155] More recently, the *Daily Mail*, when launching an ultimately futile campaign to ensure that Arm listed on the LSE, said "It is not that we're short of tech entrepreneurs and fantastic, innovative businesses in the UK."[156] Similarly, according to the *Times* "the private (unlisted) tech sector is vibrant, with lots of capital and talent."[157]

While Britain may have innovative commercial spark, the drive to push businesses to the next level may be lacking. The *Telegraph* has explained a dearth of companies going public partly on the basis of "a particular cultural mindset" that "encourages founders to sell to rivals, often foreign, before hitting the big time. Too often the ambition is no more than to build fast, and before anyone can find you out…".[158]

As for companies that are already publicly traded, history helps to explain why Britain lacks its own Apple, Amazon or Tesla. In the 1980s there were "big opportunities for those entrepreneurs with

---

153 B. Cheffins, "Are Good Managers Required for a Separation of Ownership and Control?" (2004) 13 Industrial and Corporate Change 591, 596.

154 "Oversold, Over Here" (15 May 2021, *The Economist*), 67.

155 X. Rolet, "Tech Minnows Can Pull Us Out of the Quagmire" (30 September 2012, *Sunday Telegraph*) B4. See also P. Campbell, "Why the UK Has Failed to Produce a Tech Giant" 3 January 2013, *The Daily Mail*) ("The vast wealth of technology expertise in the UK means that there will always be small companies and start-ups emerging.").

156 R. Marsden, "Bring Arm Back to the London Stock Market" (18 February 2022, *The Daily Mail*) 16.

157 P. Hosking & K. Prescott, "London Stock Exchange Still Stuck With its Jurassic Park Image" (27 August 2022, *The Times*) https://www.thetimes.co.uk/article/london-stock-exchange-still-stuck-with-its-jurassic-park-image-kl9hdkb7j.

158 J. Warner, "Boardroom Wokery is Driving Companies out of Public Markets" (22 August 2021, *The Telegraph*) Business, 16.

the ruthlessness and courage to tackle the legacy left by decades of poor management and trade union domination."[159] By the early 2000s, however, "many of the British business icons" had been "besmirched"[160] and "swashbuckling UK plc (had) lost its swagger," with adventurous growth by acquisition or otherwise being largely forsaken.[161] Due perhaps to British business's "tendency to walk on the mild side" seemingly little has changed in the years since,[162] which may help to explain why the market capitalisation of Apple exceeds the entire FTSE 100.[163]

Conclusion

When investigating the murder of an incognito American gangster on the Orient Express, Agatha Christie's star detective Poirot eventually discerns without definitive proof that pretty much all of the plausible suspects acted together. Similarly, it is impossible to pin responsibility for the LSE's declining equity markets on one overriding, decisive factor. There are several possible explanations, ranging from the global rise of private capital, to regulatory and governance hurdles, and U.K.-specific market-oriented factors. Furthermore, amongst market-oriented factors, there are various plausible culprits, including insufficient investment research, investment biases of U.K.-based pension and insurance funds, and a domestic investor and management culture that fails to fortify the sort of bold entrepreneurial verve that drives growth in fledgling companies and ultimately dominant industry leaders.

---

159 "Animal Spirits" (4 August 4 1995, *Financial Times*)17. For background on the forces involved, see R. Lambert, "The Shocks That Forced 'Fat, Lazy' British Business to Get Fit" (19 September 2016, *Financial Times*) 13.

160 "A Bruising Boom" (21 October 2000, *The Economist*) 42.

161 D. Roberts and I. Dey, "Sale of the Century: How Swashbuckling UK plc Lost its Swagger" (26 November 2006, *The Telegraph*) City, 6.

162 O. Shah, "Why a British Elon Musk Remains Light Years Away" (17 April 2022, *The Times*) Business and Money, 9.

163 M. Sweeney, "Apple's $2tn-plus Value Overtakes the Entire FTSE 100" (1 September 2020, *The Guardian*) https://www.theguardian.com/technology/2020/sep/01/apple-value-ftse-100-iphone-coronavirus.

U.K. regulators and policymakers appear to have recognised that there are several protagonists contributing to the LSE's decline, given numerous consultations and reform proposals spanning a wide array of themes. There is a danger, however, that the potentially relevant themes will be addressed in a futile and perhaps even counterproductive piecemeal fashion. The reforms seem much more likely to succeed if they are developed as part of a coherent overarching strategy. For example, a regulatory approach that focuses on attracting IPOs without engaging with contemporary attitudes of U.K. investors is unlikely to foster enduring stock market growth in the U.K. Similarly, attracting pension funds and insurers back to the domestic equity investment exchange will have a limited beneficial impact on the stock market without additionally ensuring these investors are prepared to back the sort of corporate growth that has bolstered U.S. exchanges even as the number of publicly traded companies has declined. On the contrary, reforms without joined-up thinking could make the LSE's situation worse, such as by battering investor confidence by attracting companies to list that deliver poor returns because they were weak stock market candidates.

This article is intended to serve as an *aide memoire* to assess forthcoming U.K. equity market reforms as they are made. We accordingly leave full analysis of solutions proposed and ultimately adopted, for now, to further research. However, the paper does indicate that when it comes to reviving U.K. equity markets, regulators and policymakers, unlike Poirot, will need to engage proactively with the various murder suspects to solve the mystery of Britain's stock market decline.

about ECGI

The European Corporate Governance Institute has been established to improve *corporate governance through fostering independent scientific research and related activities.*

The ECGI will produce and disseminate high quality research while remaining close to the concerns and interests of corporate, financial and public policy makers. It will draw on the expertise of scholars from numerous countries and bring together a critical mass of expertise and interest to bear on this important subject.

The views expressed in this working paper are those of the authors, not those of the ECGI or its members.

Electronic Access to the Working Paper Series

The full set of ECGI working papers can be accessed through the Institute's Web-site (https://ecgi.global/content/working-papers) or SSRN:

Finance Paper Series	http://www.ssrn.com/link/ECGI-Fin.html
Law Paper Series	http://www.ssrn.com/link/ECGI-Law.html