In the Pink

Our still mutual friend

Simon Carne rethinks Nationwide's vote not to float

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Summer 1997 was hot and sticky. It was also the windfall season. Those investors who put their money with Woolwich, Halifax or Norwich Union were rewarded with enough free shares to pay for several electric fans – and some were lucky enough to afford air-conditioning.

Savers with Nationwide building society took a different view. In 1997, they voted against candidates for the board who favoured a stock market flotation. And in 1998 they voted again, this time rejecting three motions that called for flotation.

Those members of Nationwide who voted to remain a building society may have been influenced by the words of the society's chairman, Charles Nunneley. "As a building society, we can afford to offer better interest rates *and services* year after year, [rather than] maximising profits for shareholders through higher mortgage rates and lower savings rates." (The emphasis on services is mine, not Nunneley's; I return to it below.)

I can think of few things more damaging to a building society and its investors than being dragged to the stock market against the wishes of senior management. A vote to float would probably have been followed by wide-ranging, and potentially disruptive, changes at the top. For that reason – and that reason alone – I viewed the result with some relief.

But with more time to reflect, the member vs shareholder debate deserves more careful airing. Nationwide is not, after all, the only remaining building society.

For a start, the initial shareholders on a flotation are the members themselves. Any reduction in savings rates – or increase in borrowing rates – is simply a reallocation of funds that allows members to see the different reward they receive as members and as shareholders.

Some former members do, of course, sell their shares to outsiders. Does that affect the argument?

Not really. The sellers exchange their future profits for a lump sum, while the buyers spend a sum of money in the expectation of future profit. That is, after all, one of the mainstays of the free market economy: the ability to swap your future rights, expectations, and all the associated uncertainties, for a fixed sum of money in the present, and the right to make the reverse transaction at any time of your choosing – although not necessarily at the same price.

Members of Nationwide have voted to deny themselves that right.

> On reflection, the members versus the shareholders deserves more careful airing

Some "no" voters may have thought that higher interest rates and lower mortgage rates represented the best deal. It is not possible to do the comparison precisely without knowing what the flotation arrangements, and in particular the windfall, would have been. But one can make a rough stab at the calculation, based on the not implausible assumption that the windfall would have averaged about £2,000 per member, as for Halifax and Woolwich flotations.

By investing this £2,000 in a basic savings account, an annual interest income of at least £80 could be earned. Is that better or worse than foregoing the windfall option in favour of higher interest rates?

An answer may be found by comparing Nationwide's interest rates at the time of the vote with those of Halifax. The typical Nationwide savings account offered about 0.25 percentage points a year more than Halifax's.

But, with that differential, you would need to have at least £32,000 invested with Nationwide to be better off with their extra 0.25 percentage points a year, rather than the windfall. And with £32,000 to invest, you would be able to take advantage of Halifax's premium savings account, which was paying at least 0.3 percentage points a year more than any Nationwide account at that time (and still pays out higher rates). The benefits of Nationwide's higher interest rates may not be as real as they first appear.

But perhaps building society members get better service, as pledged by Nationwide? That must, to some extent, be subjective. But any company executive who puts shareholders ahead of customers risks losing those customers to other groups. The effect on share prices, if customer numbers decline, will soon teach so unwise an executive a lesson.

A building society has no share price to remind executives of what matters to members, so the service incentive may not be quite so intense. As a quick test, try withdrawing money from Nationwide's highest interest paying account and then try the same at Halifax.

Nationwide require a form to be posted, which they action the next day (or the day after) making the funds available on the third or fourth day. Phone Halifax in the morning and the money can be cleared funds in your account – or any bank account of your choosing – that afternoon.

One has to wonder whether Nationwide nurtures its building society status for the benefit of its members, or to protect the management from the full effects of competition that a share price can lay so starkly open to public scrutiny.