

[It's not just UK banks the EC is after](#)

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Summary

The European Commission's requirements for continued state aid to RBS and Lloyds may look like unwarranted interference in the UK's domestic banking market. They are, however, consistent with the approach taken towards other dominant banking groups in other EU states. They are very likely to be of long-term benefit to UK consumers.

Analysis

The EC's intervention is not particularly remarkable. As the article points out, it is entirely in line with the general requirements for state aid to be reviewed to ensure it is not a distortion to the wider goal of promoting a single European market. Financial services in general, and banking in particular, cause greater challenges than most industries in this regard, as they are typically subject to close supervision at the national level. That in itself provides opportunities for market distortion across the EU.

The most interesting aspect of the restructuring of RBS and Lloyds is the need to dispose of substantial numbers of bank branches. Whilst the need for physical premises has declined over the last 20 years or so, a High Street presence is still a valuable marketing tool. It is even more valuable to a new entrant, and the disposals will not be allowed to be made to existing major banking groups. It will be interesting to see if organisations such as Tesco bid for some of the premises on offer. Tesco has already applied for a full UK banking licence, and it has a significant financial services business already, albeit currently limited to simple financial products. The acquisition of a branch network, together with supporting infrastructure, would give Tesco the opportunity to move swiftly into a wider range of consumer financial products. The ability to sell mortgages is an obvious one. What price Tesco as a bidder for Cheltenham & Gloucester, for instance?

The required disposals also impact on the wider debate about banks being "too big to fail", and certainly about the need to ring fence riskier elements of bank activity, eg proprietary securities trading, from strategically vital but low margin business such as money transmission. One of the key reasons that RBS had to be rescued was that it was estimated that 35% of all money transactions went across the RBS transmission network. Consequently a failure of RBS would have resulted in people with no direct exposure to the bank still suffering. I think we can expect to see a range of interested parties all using their influence to isolate the essential "plumbing" of the banking system (money transmission, retail deposit and short-term savings) from wholesale and investment banking. Requiring banks such as RBS and Lloyds, which are major players in banking "essentials" to offload non-essential parts of their operations clearly fits in with this wider governmental objective. Divesting non-core and non-complex operations such as insurance and fund management businesses is easy to achieve and can be done quickly. I suspect we will see further steps in the future as governments seek to bring about the divestment of riskier and more complex parts of the banking groups they control. We have already seen this with RBS, which soon after the UK government took majority control began to pull back from many markets and investment banking services. This restructuring may be easier to achieve via commercial means (ie disposals or simple closure of operations) rather than regulatory or legislative change, which is time-consuming and more rigid.

There is a need for EC involvement in much of the change taking place in European banking, and specifically the retail end of the spectrum. Banking has long been one of the industries most subject to the concept of "national champions". Governments and regulators have used (abused?) the local regulatory process to prevent cross-border acquisitions, of which I am not aware of a single hostile bid ever having succeeded in the face of local governmental or central bank opposition. The EC can at least ensure that such nationalistic behaviour does not indirectly provide such protected institutions with an unfair advantage with which to penetrate other markets. In the case of the likely sanctions on RBS and Lloyds, it is also perhaps going a little further and ensuring that competition is adequate in their domestic market. There is nothing wrong with that if it strengthens consumer choice, as is likely to be the case.

The EC has a long tradition of championing consumer interests. Deregulation of airfares in the EU, with the consequent rise of low cost airlines and increase in air travel; forced reduction of mobile phone roaming charges across EU borders; €1 billion fine of Intel for anti-competitive practices are all examples. Breaking up large, complex, apparently anti-competitive financial firms should be seen in the same way, even if there is a bit of quasi pan-European financial services regulatory creep in there as well.