

Nothing will ever be the same

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The banking sector has in fact been taken over by governments, according to Sławomir Lachowski, supervisory board member of Meritum Bank, former president of BRE Bank SA, former deputy president of PKO BP, as well as founder of mBank and MultiBank. He was addressing the Polish Financial Forum in Warsaw in October.

The crisis has not led to a catastrophe only because of mass government aid. Such aid had had no precedence in history. It entailed first of all bailout funds to banks in trouble. It also consisted of asset quality assurances, direct credits to secure liquidity and credit guarantees. And last but not least – it was also the public sector that allowed flexible interpretation of some terms of accountancy and asset counting (margin appraisal). Consequently, the banks – especially in Western Europe and in the United States - were not obliged to report their real losses. They would have had to do so if rules binding for the past decade or so had been adhered to. Admittedly, it was the public sector and Western governments that saved the world from what I dare to refer to as a catastrophe.

Although the crisis was born in the United States, banks in Europe were affected just as much and perhaps even more. This was not bound to happen at all but banks in Europe have been heavily affected by the crisis as a consequence of their greed, lack of imagination and incompetence. As a result, some had to fear for their survival.

The crisis has altered a lot in the financial field, and in particular in the banking sector. It is said that the architecture of the banking system will change in the future, i.e. after the crisis. In terms of ownership, as well as system of operations, the situation in many companies has changed already. For one, the strict separation of investment and commercial banking in force in the United States since 1936 no longer applies. It does not because investment banks no longer exist. All the biggest investment banks in the world no longer operate as independent or investment banks. Lehman Brothers, the world's fifth largest investment bank, went bankrupt. Bear Stearns, the fourth largest, was taken over

by J.P. Morgan. Merrill Lynch, the world's second largest investment bank, was taken over by Bank of America. 21% of the stakes in Morgan Stanley, another major US bank, was acquired by Mitsubishi Corporation of Japan. Goldman Sachs is now the only bank that has stayed independent in terms of ownership. It has, however, transformed into a commercial bank. It gave up its status of an investment bank of its own accord to be able to do what investment bankers mocked at – to collect client deposits. To-day, literally nothing has remained of the traditionally-perceived investment banking system nursed in the United States for many long years.

It turned out that government aid programmes addressed to the banking sector in Europe were larger than in the United States. In Europe aid to bail out banks reached more than EUR1 trillion, while official aid to failed banks in the United States aid amounted to USD 900 billion. Interestingly, during a similar bail-out operation during the 1930s depression, aid given to 6,000 US banks amounted to USD1.3 billion. This compares to USD200 billion in today's value terms. That amount is four times less than the US government aid provided in 2008-2009.

Europe followed the same path. It emerged that most governments were outdistancing each other in declaring the amount of means considered indispensable to bail out the banking sector. In Belgium, its three biggest banks practically went bankrupt. 99% of the stake in Fortis (the bank is now present also in Poland) was taken over by the state and then sold to the French BNP Paribas. A proportion of Fortis shares in the Netherlands was acquired by the state for EUR16.5 billion. Dexia and KBC received additional capital as well as inter-bank credit guarantees to prevent an instant paralysis of the Belgian financial system. In the UK, government aid amounted to GBP500 billion. Lloyds/TSB and Royal Bank of Scotland, the two largest banks in the country, are now national banks after the government acquired 65% and 70% of their stake respectively to keep them afloat. Earlier, these banks had taken over their major competitors: Lloyds/TSB acquired Halifax/Bank of Scotland, the biggest mortgage bank in the British Isles, while Royal Bank of Scotland took over National Westminster Bank, its main competitor. Consequently, we are dealing in the UK with an oligopoly run by the state. A similar thing happened in Germany. The government there declared aid of EUR300 billion to prop up guarantees and credits and EUR80 billion of additional capital. Commerzbank AG which is the second, but now in fact the largest German bank, received EUR18 billion of government aid to save it from bankruptcy after its merger with Dresdener Bank, its competitor.

Poland, its banking sector, the economy and bank clients were far away as well as

close to these difficult crisis situations. Far away in the sense that while Polish banks have experienced some difficulties, Polish clients have in real fact reaped some benefits. For due to the fact that Polish banks had difficulties in securing means to finance their operations, ordinary customers could earn much better interest on their deposits. Banks were pressed to raise money through deposits at home rather than by financing the foreign financial market in Poland.

Now, what about the future? For the banking system in the world and in Poland nothing will ever be the same. The changes to come will be shaped first of all by the new role played by the state perceived as the key owner. This is already the case with regard to leading banks in Britain as well as in Germany, where additional capital was given also to other banks apart from Commerzbank. The same holds true about the Netherlands where ING received EUR10 billion euros in aid. What will be that role of the state as the owner, its role as the guarantee of liquidity? After all, the financial market is still functioning to this day thanks to the central bank's guarantees of loans and inter-bank credits. It is the state that guarantees the assets of many technically failed banks. These banks have not become bankrupts only because low quality assets, for instance in Holland or Germany, were moved out from banks to special purpose institutions and guaranteed by the state. I am sure that the state will play an absolutely decisive role in what will be happening.

The need for new regulations is another issue on the agenda. Regulations are required to shape a new image of the banking sector and first of all to define the size of capital needed for functioning as well as for measuring the financial and credit risk within banks.

Surely, the thing that will change the image of the banking sector is consolidation. This has already been accomplished in the United States following the acquisition of its main investment banks by commercial banks. A swift wave of consolidations has swept over the US banking sector in 2008-2009. In a spectacular development, JP Morgan took over Washington Mutual Inc. creating, in effect, the third largest para-bank institution in the United States. The acquisition of Merrill Lynch by Bank of America was another example. In Europe, the same had already happened in Britain with BNP taking over Fortis Bank, and partly also in Germany following the acquisition of Dresdener Bank by Commerzbank.

And last but not least, the future and the changes in the banking sector will also be shaped by new initiatives. There is ample room for such initiatives in the vacuum that has emerged as a result of bankruptcies and debacles. Banks which

received huge aid from the state are first of all bound to deal with their own problems. New regulations will alter their mode of functioning. Technology and civilisation will change clients and their expectations. It follows that new initiatives are feasible. We are going to witness new banks emerging not only due to consolidation but also as completely new ventures.

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The crisis began in the United States but it was Europe that felt the pain the most. American banks, which received public aid, paid it all off with the exception of Bank of America and Citigroup. In Europe, it may take banks decades to pay back the aid received. The future therefore puts before Europeans a major challenge in terms of regulatory as well as business matters. The situation of the American banking sector and the American economy, primarily in terms of its competitiveness and aggressive market attitude, is nowadays better than that of Europe.