

CHAPTER 12

Conclusions

The merger situation

12.1. Under the terms of reference and the provisions of sections 69(1), 75(2) and 75(4) of the Fair Trading Act 1973, we are required to investigate and report whether arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a merger situation in which section 64(1)(b) will be satisfied. We are required by each of the references to exclude from consideration the condition under section 64(1)(a).

12.2. By virtue of section 64(8) a merger situation qualifying for investigation exists if two or more enterprises have ceased to be distinct enterprises in the circumstances described in section 64(1). On the basis of statements made to us by Standard Chartered and by HSBC it is clear that, unless prevented from doing so under the Act, each intends to proceed with a bid for the share capital of Royal Bank Group. Arrangements are therefore in contemplation which, if either is carried into effect, will result in the enterprises carried on under the control of Royal Bank Group ceasing to be distinct from enterprises carried on by or under the control of either Standard Chartered or HSBC.

12.3. The assets of Royal Bank Group at 30 September 1980 were £486.5 million. The condition in section 64(1)(b) (that the value of the assets taken over exceeds £15 million) is therefore satisfied in respect of each reference.

Issues of public interest

12.4. We consider first whether either merger may be expected to have adverse effects on the public interest; then whether either merger may be expected to produce benefits for the public interest and how far these balance or outweigh any adverse effects; and finally whether any safeguards are available to prevent such effects.

Anti-competitive effects

12.5. Neither of the bidders is engaged in retail banking in the United Kingdom. Each has a few branches engaged principally in foreign trade services and lending to companies, while Standard Chartered owns Chartered Trust, a finance house. There would consequently be no significant reduction in competition in United Kingdom banking if either of the bidders were to merge with Royal Bank Group. We considered whether there might nevertheless be a loss of potential competition, in that the successful bidder might, in the absence of a merger, have sought at a future date to enter directly into United Kingdom retail banking. We have had regard not only to what each of the bidders told us about the time and expense already incurred in establishing its

present limited presence, and about its intentions; but also to recent developments in other countries.

12.6. We conclude that the prospect is remote that either of the bidders will enter, by means other than acquisition, into retail banking in this country on any scale; and that the enhancement of competition by this means is too speculative to be taken into account. In respect of wholesale banking, including the provision of services to corporate customers, we observe widespread and active competition among numerous banks, both British and foreign-owned, and we conclude that the acquisition of Royal Bank Group by either bidder would not significantly restrict or inhibit this competition. We deal with other competition issues in paragraphs 12.31 to 12.36.

Effects on Scotland

12.7. We have been impressed by the arguments, summarised in Chapter 10, that the merger of Royal Bank Group with either HSBC or Standard Chartered may be seen as part of a process of economic centralisation which has been seriously damaging to Scotland and to some other regions in the United Kingdom. We do not underrate the contribution which inward investment has made to the Scottish economy through improved technology, products, management and business methods; and we consider in detail below what benefits the two mergers at present proposed might bring. But we accept that in certain cases the comparative economic difficulties of regions such as Scotland have been accentuated by the acquisition of locally managed and controlled businesses by companies from outside, whether elsewhere in the United Kingdom or overseas.

12.8. Such acquisitions have consequences for the scope and scale of local control and management and its responsiveness to local needs. The development of a 'branch economy' creates the danger that it will be the operation in Scotland that is first to be closed or reduced in hard times, while the main business elsewhere is maintained. Further, a local operation, even while it flourishes, will generally be responsible for fewer and less important functions than if it were a wholly independent concern. Overall direction of the enterprise is typically moved to the head office of the acquiring company, and with it major decisions in such areas as corporate and market strategy, financial policy, labour relations and the employment of senior personnel. The scope of the local managing director's job is correspondingly narrowed.

12.9. We have been given many examples of cases which illustrate this tendency—ranging from insurance to motor manufacture to electronics; in many cases, subsequent events disproved the hopes that the scale and independence of local operations would be maintained. We accept that such a process of centralisation can have serious effects. It may reduce the responsiveness of the local business to local needs. A distant management, however intelligent and unprejudiced, may not give the same weight to local concerns as would a manager who is part of the local community and has full responsibility on the spot; an element of judgment enters into almost all business decisions, which are not generally made on the basis of cold reason

alone. Career opportunities in Scotland are reduced. Functions such as marketing or product development may be removed from the menu of opportunities in Scotland. Bright young Scots have less opportunity to develop their talents; alternatively, they realise their potential by emigrating to England or overseas. The harm done by the loss of such people, or by failing to develop their skills, is not limited to the direct effect on them and their businesses. The vigour of a local economy is seriously affected by the general level of professional and business skills available there. Companies depend on each other to create and maintain a pool of managerial skills on which everyone can draw. Good managers learn from their peers in other local businesses through social contact, business clubs and commercial dealings with suppliers and customers. The effect of losing good people from Scotland, or failing to develop their talents adequately, is fundamental.

12.10. We believe that an important factor in Scotland's economic difficulties has been the progressive loss of morale which the taking over of large companies has caused; and we accept that this is damaging to Scotland. Entrepreneurial spirit and business leadership depend critically on self-confidence, and on balance we believe that such self-confidence has been weakened.

12.11. These general arguments will not have the same impact on every merger affecting a Scottish company. Their effect will depend on the nature of the company and its importance for the economy of Scotland. We now turn to their application to the case of Royal Bank Group. We do so mindful that among the matters which we are required to take into account is the desirability of 'maintaining and promoting the balanced distribution of industry and employment in the United Kingdom'.¹

12.12. We accept that there may be a tendency in manufacturing and some service industries for branch operations located in Scotland to be reduced or closed down in preference to operations in England or overseas. But retail banking is by its nature tied to where its depositors and borrowers are found and will continue so to be unless there are radical changes in money transmission and similar technology. These are already in prospect, but if such developments did lead to reduced employment in branches this would happen in any case and would not be the result of a merger. We do not therefore expect either merger to lead to a loss of employment in Scotland. Indeed there might be some net gain in numbers employed, in the case of Standard Chartered if the headquarters of its new Domestic Division (mentioned in paragraph 7.16) were in Scotland, and in the case of HSBC through Royal Bank Group's position as HSBC's 'flagship' in Europe.

12.13. That apart, we conclude that either merger may be expected to accentuate the problems which we have identified above. Scotland is the only part of Great Britain to have retained independent clearing banks. The three Scottish clearing banks are the largest components of the financial sector of the Scottish economy, which includes other companies of importance which have their headquarters in Scotland. Not only has the financial sector retained

¹Section 84(1)(d), Fair Trading Act 1973.

a strong Scottish character, it has also been one of the more successful sectors in the Scottish economy, providing increasing employment over a number of years when employment in manufacturing has been falling and when unemployment has been high relative to most other regions of Great Britain. At present approximately 80 per cent of clearing bank deposits in Scotland are held by the two clearing banks with their headquarters and direction there; but if Royal Bank Group were acquired by one of the bidders, substantially less than one-half of clearing bank deposits would be held by the remaining Scottish bank with headquarters and direction in Scotland.

12.14. RBS is therefore an important company in an exceptionally important and prosperous Scottish industry; and it is a company not only registered in Scotland, but managed and controlled there. Royal Bank Group, which owns it, is perhaps the largest remaining company of which management and control are located in Scotland. We recognise that a large part of the business and profits of the group relates to England. But the degree of control and management exercised by Scots from Edinburgh, the size of the company and the importance of it and its industry for Scotland lead us to conclude that removal of management and control of the group from Scotland would be a serious detriment.

12.15. As noted in paragraph 12.12, either merger might have neutral or beneficial effects on numbers employed in Scotland. We have considered also the effects on the range and level of senior directing and executive posts. In the case of merger with Standard Chartered we expect that there would be a reduction in the range of such posts in Edinburgh and perhaps also in Glasgow, where RBS has part of its international division, because work now done in these places would be done in future by the proposed International and Wholesale Division in London; although this would be in some degree offset by additional posts in the proposed Domestic Division if it were located in Scotland. In the event of a merger with HSBC, we could not expect at this stage to know enough of the organisation and policy which would be adopted to form a view of the effects on senior directing and executive posts.

12.16. We foresee a detriment to the public interest in Scotland in the case of either merger arising from the removal of ultimate control from Edinburgh. Major decisions on marketing, investment, company strategy, risk-taking and expansion would naturally and rightly be the concern of the centre, whether it was in London or Hong Kong. No doubt a great deal of responsibility would be delegated to the local management in Edinburgh; we do not envisage large scale intervention day-to-day by the centre. But it would be unreasonable to expect either parent to give full autonomy to a part of the business which, however substantial and well-run, was at the policy level dependent on and linked with the overall operation of the group. The vast majority of individual business decisions would continue to be made on the spot in Scotland. But we would not expect the general policy stance of a London or Hong Kong based owner in relation to the expansion of Scottish business and the support of Scottish initiative to be as sensitive to local interests as a native management based in Edinburgh. Nor would we expect management to be as quick to respond.

12.17. In addition, the deterioration in the quality and importance of decisions made in Scotland by the most senior Royal Bank Group managers would mean reduced career opportunities in Scotland and some increase in the rate of emigration of able Scots. The links of the Edinburgh financial community would no longer be with a major Scottish bank with complete power of decision, and personal contacts would not be with a chief executive of a genuinely independent clearing bank. These effects would be more rapid and more marked in the short-run in the event of a merger with Standard Chartered. But in the long-run we do not believe that HSBC would refrain from exercising control over its new acquisition, particularly if it were to serve as the group's 'flagship' in Europe. We have been given many examples where, although there is no reason to doubt the good faith of those who gave promises of independence, business logic subsequently made some centralisation of control necessary and desirable.

12.18. The damage would not be confined to the Royal Bank Group or to the financial sector centred in Edinburgh. Loss of Scottish control of RBS would be seen as a significant step in the long process of centralisation and of weakening local control over local economic affairs. It would reinforce the impression of a 'branch economy' and diminish confidence and morale in Scottish business. It would also, by reducing the number of key independent positions in Edinburgh, weaken the public life and leadership of the city and the country.

12.19. We also think there is value in preserving such independent local centres of business initiative and opinion as survive in the United Kingdom. Scotland and Scottish banking have an honourable record of innovation, and we believe that the independence which fosters such innovation is best preserved by leaving full control of the bank in Edinburgh.

The HSBC bid: issues arising from transfer of control overseas

12.20. Standard Chartered and Royal Bank Group have deployed arguments against the bid made by HSBC; and the Bank of England has also argued strenuously that the acquisition of Royal Bank Group by HSBC would be against the public interest, because ultimate control of the group would be transferred overseas. We are conscious that some of the considerations which arise from such a transfer go much wider than the issues which we are normally required to consider in merger cases, and on which we would be guided by the previous work of the Commission. We have paid particular regard to the views of the Bank of England, bearing in mind its special authority and responsibility in this area. But we are of course required to reach our own conclusions on the evidence before us, taking into account all matters which appear to us in the particular circumstances to be relevant.¹

12.21. Some of the arguments have not seemed to us wholly persuasive. A good deal was made, for example, of the likely loss of effectiveness of the Bank's supervision both in relation to monetary control and for the protection

¹Section 84(1), Fair Trading Act 1973.

of depositors. It seemed to us, however, that the supervision of the group's domestic banking would derive from the fact that the group—or more exactly its component banking companies—would continue to be recognised banks in the United Kingdom, notwithstanding the change of ownership. All the figures needed for monitoring whatever measures and ratios may from time to time be regarded as significant for monetary control would continue to be provided and it did not seem to us likely that a parent company abroad would resist making any adjustments required by United Kingdom authorities.

12.22. On the prudential side the Bank argued that with a parent company in Hong Kong it would no longer have the continuous familiarity with the strategic thinking of the group that it expected in its relationships with other clearing banks. Moreover, the current Hong Kong legislation on banking supervision was said to leave gaps in the knowledge that the Bank here could acquire about some of the activities of subsidiaries of the HSBC group in other parts of the world. Because of these factors the Bank of England might have difficulty in maintaining a full assessment of all aspects of the group's strength in the way that it believed necessary in relation to a United Kingdom clearing bank. It was urged by HSBC on the other hand that with modern communications the Bank could enjoy the fullest dialogue at all times with its top people and that new legislation in Hong Kong would repair any gap in the existing supervisory powers of the Hong Kong Government and enable any necessary information to be passed to the Bank of England in accord with the Basle Concordat. While we should hesitate to treat lightly the Bank's concern in these matters, we have found it hard to convince ourselves on balance that these difficulties over supervision would in themselves engender unacceptable risks to depositors with Royal Bank Group banks if they were acquired by HSBC.

12.23. However, it became clear in any case that the Bank would oppose on other grounds the transfer abroad of ultimate control over a United Kingdom clearing bank even where it was satisfied that no significant problem arose over supervision. To this broader issue we now turn.

12.24. The Bank questioned whether, given the key part played by the London and Scottish clearing banks in the United Kingdom economy, it could ever be right to allow control of any of them to pass into hands not fully committed to the United Kingdom public interest. Where as a result of acquisition control passes to a parent company overseas, possibilities of conflict of interest are inevitably opened up; these possibilities arise from the fact that the parent company is bound to respond to the policy requirements of its own home government and, more generally, to give primacy to its responsibility to the needs and interests of the people of its area. In some circumstances these requirements may well be inconsistent with enabling a subsidiary abroad to be fully responsive to the authorities in the country where it operates, or to the interests and needs of the people there.

12.25. We have considered whether this argument should be illustrated by suggesting examples of the type of divergences of interest, perhaps involving external relations or economic and monetary issues, that might arise. There is,

however, always a risk that an example, even if hypothetical in intention, might be misread as some form of prediction of actual events. We are particularly anxious in this context not to be taken to be making any assessment, let alone any prediction, reflecting on the economy of Hong Kong. But we think it can hardly be gainsaid that the transfer of control over a British clearing bank to a parent company in almost any part of the world might give rise over a period to possible divergences of interest. Moreover, it has to be remembered that where banking is concerned, damage can be done to confidence not only by actual events but by public unease in face of contingencies which do not in the end occur.

12.26. This general line of argument seems to us at least to raise a presumption that the transfer overseas of control over a significant part of the United Kingdom clearing bank system would have undesirable consequences. The detriment to the public interest, according to this line of argument, is not the chance, which may be remote and will surely be unquantifiable, that a specific conflict of interest of this kind envisaged above may arise from the transfer of control. The argument is that the transfer of control overseas, as a specific consequence of an acquisition, is itself detrimental to the public interest because it avoidably opens up, in an industry central to the economy, possibilities which are not merely fanciful of divergence of interest which would not otherwise arise. The presumption is in principle rebuttable and particular cases must be judged on their merits. For example, a United Kingdom bank might be so clearly in need of fresh blood and impetus that a bid from outside would on balance be preferable to the *status quo*. In the present case it might be argued that the Royal Bank Group's share of United Kingdom clearing banking should be treated as *de minimis* or that an acquisition by HSBC should not be regarded as involving a transfer of control overseas.

12.27. We wish to emphasise that the proposition under discussion here is in no sense hostile to the competition provided by overseas banks in this country. As was shown in Chapter 3, the number of overseas banks directly represented in London has grown over the last decade to about 350 and many have developed substantial business, particularly in wholesale and investment banking. It is undeniable that the United Kingdom authorities have operated a conspicuously liberal regime in relation to this influx and that the competition so provided has been beneficial. Nor is it to be inferred that all aspects of retail banking and money transmission should, according to the argument under discussion, be insulated from overseas influences. It is necessary to look at the merits of particular cases and put them in the context of the structure of banking in the country concerned.

12.28. As will be seen from paragraph 12.40 below, we do not believe in this case that the presumption against transferring control overseas can be rebutted by any overriding need to bring fresh blood and stimulus to Royal Bank Group. In paragraphs 12.31 to 12.36 below we deal with the question whether there are benefits from either merger to set against any adverse effects. We do not think that the 5 per cent of retail banking controlled by Royal Bank Group can be regarded as *de minimis*, particularly in view of RBS's large share of the

market in Scotland. We have also considered whether an acquisition by HSBC of Royal Bank Group should be seen as an exception to the general argument that transfer of control to an overseas bank might give rise over a period to possible divergences of interest. Certainly there is no question of our regarding HSBC as a 'foreign' bank; but that does not in itself avoid the presumption set out in paragraph 12.26. In the case of Hong Kong there is the further consideration that the United Kingdom Crown remains the sovereign power and it may be contended that because of this no conflicts of interest of the kind envisaged in the argument can arise. We think it is well understood, however, that the Government there must have primary regard to the welfare of its population and the interests of its territory, and it therefore seems to us right in common parlance to regard control of Royal Bank Group by HSBC as involving a transfer of control overseas.

12.29. The fact that HSBC proceeded with its bid, notwithstanding the Bank's clear indication that the bid would be unwelcome, may be seen as an example of the kind of divergence of interest that might arise and as an indication that HSBC, if in control of a United Kingdom clearing bank, would not always be prepared to accept the Bank's customary authority in United Kingdom banking matters. A consequence of HSBC's proceeding further with its bid is that the Bank's authority in this area would be seen by others to be weakened.

The overseas exposure of Standard Chartered

12.30. Standard Chartered, as is shown by Table 5.1, is dependent for a good deal of its profits on assets in Africa, particularly South Africa. There are plainly political risks associated with these countries, in some cases substantial risks, from which Royal Bank Group is at present free. Since Standard Chartered and Royal Bank Group are both British banks, their merger, though extending those risks to a clearing bank, would not increase the United Kingdom's exposure in Africa, and would not in our view create a material detriment to the public interest in this respect. As for potential conflicts of interest, such as are discussed in paragraph 12.26, the issue does not arise in the case of Standard Chartered, which is registered and controlled in the United Kingdom.

Possible benefits from either merger

12.31. All three principal parties claimed that there would be benefits for the public interest in the merger of Royal Bank Group with a larger bank having an extensive network of branches outside the United Kingdom. The claimed benefit would arise in part from linking each of the two operating banks in the group with an established network of branches in other countries, of a scope which Royal Bank Group on its own would not be able to build up within the foreseeable future. It is argued that a bank can offer better foreign trade services through branches or affiliates than it can through correspondents; and that Royal Bank Group would be able to offer more effective competition in supplying foreign trade services following a merger. It was also suggested that affiliates might create new opportunities for inward investment.

12.32. Our survey of major United Kingdom companies with an interest in exporting indicates that many commercial customers do indeed perceive some advantage in dealing through banks overseas which are linked by ownership, either with the United Kingdom bank with which the company deals, or with a multi-national bank with which the company deals in the United Kingdom. On the other hand, we note that German and Japanese banks do not have any significant overseas branch networks; and that a very great part of British export trade is to European countries where United Kingdom banks have few or no branches or subsidiaries. On balance, we conclude that the proposed links with overseas networks would enable Royal Bank Group to make some improvement in the foreign trade services it offers, especially in the fast-developing region of South East Asia. The possible effect on inward investment appears too uncertain for us to give any weight to it.

12.33. Another benefit to the public interest claimed for each merger is that associated with the larger size of the group formed. This might work in two ways. First, the greater financial strength of the group would enable the two operating banks to raise their customer limits, and so make larger loans; this would mean that fewer of their customers would need to seek loans from a group of banks and reduce the chances of their largest customers feeling obliged to transfer to another bank as principal banker. Secondly, the larger financial resources behind the two operating banks might enable either or both of them to expand at a faster rate than at present; this could be particularly useful in the expansion of W & G's branch network. We conclude that there may be some small advantage for the public interest in this respect from the formation of a larger group.

12.34. More generally, it was claimed that the merger of Royal Bank Group with Standard Chartered would create a 'fifth force' in the United Kingdom, and this would itself constitute a public benefit. Similarly it has been suggested that a merger with HSBC would add to effective competition in retail banking. The United Kingdom has a concentrated banking sector, dominated by four very large banks, and this is particularly striking by comparison with such successful economies as Germany and the USA. Any merger which claims to reduce this concentration deserves particularly careful attention. If we believed that either of the possible new groupings would bring about some radical new departure in retail banking, that consideration would weigh very heavily with us. But none of those concerned contended that they would aim at fundamental changes in the approach which the Royal Bank Group would bring to competition in banking under new ownership.

12.35. Implicit in the 'fifth force' argument is the view that Royal Bank Group as at present constituted is not big enough to match the 'big four' or significantly to affect the development of banking in the United Kingdom as a whole, despite its predominance in Scotland. We are not convinced that this is so. On a world scale Royal Bank Group is already large; and W & G seems capable of making a distinctive contribution despite its small share of the English market. We are not persuaded that competition will necessarily be enhanced by the creation of an additional banking group of the same kind as the 'big four'. Nor do we believe that the promised benefits add up to a

transformation of Royal Bank Group into a much more serious competitor to the 'big four'.

12.36. We do not therefore believe that, on the basis of the advantages claimed by the parties, there would be any substantial contribution to competition in United Kingdom banking from either merger.

12.37. We have also considered the claims (paragraphs 7.4 and 8.6) that a merger between Standard Chartered and Royal Bank Group would benefit the public interest because it would strengthen Standard Chartered. While the improvement of a British company's competitiveness, prosperity and stability is clearly in the public interest, we think that Standard Chartered, which is already a prosperous company, does not have any great need for further strengthening and that therefore the benefit of a merger between it and Royal Bank Group would be minor in this respect. We do not give any weight to the improvement of a company's tax position or a reduction in its exposure to the risk of takeover.

Conclusions

12.38. In respect of the proposed merger between Royal Bank Group and Standard Chartered, we find (in paragraphs 12.15 to 12.19) that its effects on career prospects, initiative and business enterprise in Scotland would be damaging to the public interest of the United Kingdom as a whole. These adverse effects outweigh any benefits that we can foresee. We therefore find that the proposed merger may be expected to operate against the public interest.

12.39. In respect of the proposed merger between Royal Bank Group and HSBC, we find not only the adverse effects on Scotland mentioned in paragraph 12.38, but also that transfer of ultimate control of a significant part of the clearing bank system outside the United Kingdom would have the adverse effect of opening up possibilities of divergence of interest which would not otherwise arise (see paragraphs 12.26 to 12.29). We conclude that, taken together, these effects adverse to the public interest outweigh any benefits that can be foreseen. We therefore find that this proposed merger also may be expected to operate against the public interest.

12.40. We wish to make it clear that it is not our intention to imply that leading Scottish financial institutions in general, or clearing banks in particular, should in no circumstances be taken over by companies based outside Scotland. If we had thought that Royal Bank Group needed better management or additional capital which could be obtained only by a merger, or that it had poor long-term prospects as an independent concern, we might well have been persuaded that in the circumstances of the case a merger would not be expected to operate against the public interest.

Possible safeguards

12.41. We have considered, as is our duty under section 72(2) of the Fair Trading Act 1973, whether any action could be taken for the purpose of

remedying or preventing the adverse effects which in our opinion each merger situation may be expected to have. In relation to effects in Scotland we have assessed them on the assumption that Standard Chartered would establish the headquarters of a domestic division in Scotland, most probably in Edinburgh; and, even so, we find the adverse effects referred to in paragraph 12.38. We have considered the safeguards suggested to us, as described in Chapter 10, and conclude that they would not be effective. The adverse effect would arise from the fact that with the change from scattered shareholdings to a single or dominant shareholder, ultimate control would shift from the present management to that of the new parent company. Whatever formal definitions of management responsibility were laid down, the last word would rest with the parent.

12.42. In relation to those considerations which apply only to HSBC, again we can devise no effective safeguard. It is the passage of ultimate control outside the United Kingdom that we regard as an effect which may be expected to operate against the public interest; and for the same reasons as given in paragraph 12.41, there is no remedy for this.

Recommendation

12.43. Since we find that either merger may be expected to operate against the public interest, and since we cannot propose any alternative action to prevent the adverse effects which either may be expected to have, we recommend that neither merger should be permitted.

C J M HARDIE (*Chairman*)
R L MARSHALL
J S SADLER
R STEPHEN
N E D Burton (*Secretary*)

22 December 1981

The following members of the group dissented from the conclusions for the reasons set out in their notes of dissent.

SIR ALAN NEALE
R G SMETHURST

Note of dissent

by Sir Alan Neale, KCB, MBE

I sympathise with but cannot join in my colleagues' conclusion that these mergers may be expected to have adverse effects on Scotland sufficient to constitute a detriment to the public interest in the United Kingdom. My difficulty is that the United Kingdom is an economic union of long standing within which economic resources including people are free to move and do move to take advantage of available opportunities. This is consistent with

taking positive action of many kinds to decentralise industrial and commercial activity and devolve governmental and other responsibilities to Scotland as to other parts of the kingdom. But I cannot myself believe that the negative act of banning proposed mergers in the supposed interest of retaining particular responsibilities or levels of decision-making in Scotland can make enough difference to the otherwise free play of trends and forces to be justified.

In the particular case before us there is little or no evidence that employment would be lost to Scotland on balance as a result of either merger and it seems to me clear that the chief executive of the Royal Bank of Scotland Limited and his senior colleagues would continue to play distinguished parts in the intellectual and financial life of Edinburgh and the bank itself would continue to serve the community responsibly, notwithstanding a change of ownership and ultimate control. Accordingly I cannot in conscience recommend that either merger be prevented on this ground. As I support the other ground (as set out in paragraphs 12.26 to 12.29) for finding against the HSBC bid, this means that I would not oppose the bid from Standard Chartered.

(signed) ALAN NEALE

22 December 1981

Note of dissent

by Mr R G SMETHURST

My colleagues have identified two detriments to the public interest, which they have called the effects on Scotland (paragraphs 12.7–12.19) and the issues arising from the transfer of control overseas (paragraphs 12.20–12.29). They conclude that although either of the merger proposals may result in benefits (paragraphs 12.31–12.35), the balance of public interest lies in stopping them both. I do not disagree with the identification of the detriments and benefits, but with the relative weight ascribed to them. Because I give less weight to the detriments and more to the benefits, I conclude that neither merger would operate against the public interest.

In the case of the Scottish arguments, my colleagues have concluded that the removal of ultimate control from Edinburgh would lead to a deterioration in the quality and importance of decisions made in Scotland, to reduced career opportunities for Scots in Scotland, and to loss of easy access to the most senior management of the group for the rest of the Edinburgh financial community. This would, they feel, be a significant step in the long process of centralisation, reinforcing the impression of a 'branch economy', diminishing confidence and morale in Scottish business, and weakening public life and leadership in Edinburgh and Scotland.

If the Royal Bank of Scotland alone, and not the whole Royal Bank of Scotland *Group*, were the object of the bids, I should agree with the majority of my colleagues that these arguments are decisive. But I am unable to attach such weight as they do to these arguments because of the presence in the group of Williams & Glyn's Bank Ltd.

In 1979 and 1980 W & G supplied more than half the group's pre-tax profits, and employed over 40 per cent of the group assets. Its asset and deposit growth over the last five years was below that of the Royal Bank of Scotland, but its pre-tax profit growth—admittedly from an unusually low base—was considerably above that of RBS. Its share of sterling deposits in England is declining slowly, standing currently at about 2.6 per cent.

In Scotland RBS has a 41 per cent share of sterling deposits. Over the next decade it is hard to see any great expansion of RBS activities in Scotland: its already extensive branch network is likely to be deployed largely to defend its very large market share there. The scope for profitable expansion of W & G activities in England, however, seems to me to be very considerable. I therefore believe that even if the mergers are forbidden, the focus of management in the Royal Bank of Scotland *Group* will nevertheless still shift to London, both because of the opportunities for W & G, and because I assume that the group will continue to seek an enhanced international dimension. An international strategy must reinforce the important presence in London of both RBS and W & G because of the location there of the international capital markets. The group Board already meets alternately in London: I have doubts about for how long it will be realistic to apply the Scottish arguments to the group as a whole even if the mergers are forbidden.

I therefore place less weight upon the Scottish arguments than do my colleagues because I doubt whether by forbidding the mergers the detriments which they see will in fact be arrested.

On the arguments about overseas control of clearing banks, my colleagues have concluded that it is unlikely that the Bank of England would be unable adequately to supervise the Royal Bank of Scotland Group (RBSG) even if it were controlled by the Hongkong and Shanghai Banking Corporation. I agree with their assessment. But I am unable to agree when they go on to conclude that 'the transfer of control overseas, as a specific consequence of an acquisition, is itself detrimental to the public interest because it avoidably opens up, in an industry central to the economy, possibilities which are not merely fanciful of divergence of interest which would not otherwise arise' (paragraph 12.26).

I accept that there may well be possible mergers in the financial sector which would open up possibilities of divergence of interest. But also I agree with my colleagues' view that all aspects of retail banking and money transmission should not be insulated from overseas influence by this argument about possible divergences of interest, and that it is necessary to look at the merits of particular cases and put them in the context of the structure of banking in the country concerned.

If, therefore, the argument about divergence of interest cannot be a general argument, it must have particular application if it is to be sustained. I agree that no such issue occurs in the case of the proposed merger with Standard Chartered Bank Ltd, since it is registered in the United Kingdom. But I also conclude that no such issue occurs in the case of HSBC, since Hong Kong is a Crown Colony, and HSBC is not therefore a foreign bank. It is perfectly true that either bidder may be subject to pressures on its group operations because of its worldwide activities. But these are not different in kind from the pressures to which most of the London Clearing Banks are subject because of their international networks. Certainly, neither Standard Chartered, because it is registered in the United Kingdom, nor HSBC, because it is registered in a Crown Colony, could be faced with a conflict of interest of the kind which might be posed by, for example, some US legislation. But even if the bidder were an American bank, the need to look at the particular circumstances of the case would, in my view, be decisive; and the fact that a bank accounted for only 5 per cent of United Kingdom retail banking would therefore be very important. So I am inclined to believe that, because of the size of the RBSG share of the United Kingdom market, there would be little chance of conflict of interest arguments being decisive in any case; but in the case of the two bids actually under consideration, I cannot agree with my colleagues' arguments.

I therefore find no decisive detriment on either the Scottish arguments or the arguments about overseas ownership of clearing banks. On the benefits side I give rather more weight than my colleagues to the creation of a 'fifth force' in banking. I share their scepticism of the benefits of linking RBSG with extensive overseas networks, concluding, with them, that there would be some small gain to the public interest.

But I place more emphasis on the effect on United Kingdom retail banking. Neither bidder made much of this in his arguments to us, perhaps because of a desire to fit in with the arguments on the desirability of an overseas network advanced by RBSG and perhaps because of a wish not to emphasise an argument which might seem to increase Scottish fears. In any merger reference the Commission is faced with choosing between alternative pictures of the future: my belief is that both bidders would give a significant boost to Williams & Glyn's. To this extent the fact that both bidders, although not 'foreign', have a background in retail banking outside the narrow group of London and Scottish clearing banks is an added attraction, offering the possibility of a distinctive contribution.

If such a distinctive pattern developed it might indeed entail increased anxiety for the Bank of England in its supervision and control of the financial sector. But increased competition rarely makes life easier for regulatory bodies. True competition entails the trying out of new ideas, new products, new techniques of production: that is why it is desirable, but why it may also test familiar relationships and patterns of control. When it is considering a sector which has a highly concentrated structure, the Monopolies Commission, as a body concerned with the promotion of competition, should, I believe, have exceptionally strong arguments before interfering with any potential entrant capable of providing genuine competition for those who are well established.

Because of the weight I attach to this consideration, because I cannot give as much weight as my colleagues to the Scottish arguments, and because I find no detriment in the possible transfer of control to a bank based in Hong Kong, I find that both bids should be allowed to proceed. I do not see why contested bids should not occur in this sector, where the need to comply with prudential ratios should protect depositors; and managers should not be protected from, nor shareholders deprived of the benefits of, the ordinary forces of competition in a capitalist economy.

(signed) R G SMETHURST

22 December 1981