A Century of Banking Consolidation in Europe

Manfred Pohl,
Teresa Tortella and
Herman van der Wee

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The History and Archives of Mergers and Acquisitions

Edited by

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Preface

This book contains the papers and comments presented at the conference of the European Association for Banking History held in Madrid, Spain, on 13–14 June 1997. This colloquium took place at the headquarters of the Banco de España, the Spanish central bank, which hosted and organized the meeting jointly with the EABH. The title of the conference was 'A Century of Consolidation in Europe: The History and Archives of Mergers and Acquisitions'.

This was the first EABH conference bringing together both archivists and historians, and was attended by more than 90 people including some representatives of banks. The meeting was opened by the governor of the Banco de España, Dr Luis Angel Rojo, who made the inaugural speech, and also presented the second biennial Young Scholar Prize of the EABH, which was shared between Maria Angeles Pons, University of Valencia, and Monika Dickhaus, University of Bielefeld.

The subject of the colloquium proved to be an interesting one and there were very lively discussions following every session. In fact since the conference was held, mergers and acquisitions have been taking place among many of the European countries' banks and indeed, to a large degree, within the Spanish banking system.

Greatest thanks are due to all the participants, in particular the authors of the papers, the people who chaired and made comments and to the members of the Protocol Service and the Archives within the Banco de España, as well as the staff of the EABH for making this colloquium possible.

Manfred Pohl
Teresa Tortella
Herman van der Wee

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PART I
History and Archives of Consolidation in European Banking: General Trends and some Case Studies

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CHAPTER ONE

Introduction: A Century of Consolidation in European Banking – General Trends

Youssef Cassis

Consolidation rather than concentration has been chosen as the theme of the conference from which this book has issued. The two notions have much in common – both point to the idea of a larger share of the banking business in the hands of a smaller number of banks. There is no doubt that several common trends are likely to be identified whether a paper deals with concentration or consolidation in European banking. There are, however, differences, which this chapter will try to emphasize. In particular, consolidation puts greater emphasis on the microeconomic level, on specific banking institutions rather than on macroeconomic implications, though the latter should not be overlooked.

At first sight the outcome of a century of consolidation is strikingly similar across Europe. In all countries, banking systems have become dominated by a handful of giant, universal-type banks, most of which were already large and powerful institutions a hundred years ago. The major changes have been the *decrease* in the number of such banks and their *increased* internationalism and universalism. In some respects, the history of banking consolidation is therefore the history of a select group of large banks which have managed to maintain or to gain dominance over the industry, often – though not always – through mergers and acquisitions. In other respects, however, it overlaps with the history of the banking sector and its interaction with the economy as a whole.

The object of this chapter is to highlight some of the general trends underlying this consolidation process. Given the space available and the huge scale of the subject, such a presentation can only be general and tentative, and serve as a general introduction to the more specific topics which are discussed in subsequent chapters of this book. Despite the apparent common outcome of a century of consolidation in European banking, different routes have been followed and there still remain substantial differences. Moreover, consolidation is an ongoing process, which has gathered pace in the late 1990s.[1] The emphasis of the paper will be on the common features displayed by the European experience rather than on national peculiarities. However, in order to take account of the diversity of this European experience, a broad comparative perspective will be maintained throughout. To this end, six questions will be addressed, each related to commonly perceived trends in the consolidation movement in European banking.

1. How have Europe's largest banks reached their dominant position?

Let us first consider the end-result, at least for the time being, of a century of banking consolidation. Table 1.1 lists the 30 largest European banks in 1995, arranged by country of origin. Looking at the table from the perspective of consolidation, that is of a group of dominant core banks, three routes to the top can be identified.[2] A first group of banks reached a dominant position almost from the moment of their foundation in the very early days of joint stock banking. These were, to use the Chandlerian terminology, the first movers, the creators of a new form of banking organization. This was the case with the National Westminster Bank in Britain (The National Provincial Bank of England was founded in 1833 and the London and Westminster Bank in 1834); the Crédit Lyonnais, Société Générale and Paribas in France (founded

Table 1.1 The 30 largest European banks, 1995

Great Britain	France	Germany	Italy
HSBC Barclays Natwest Abbey National Lloyds	Crédit Lyonnais Crédit Agricole BNP Société Générale Paribas Suez	Deutsche Dresdner WestLB Commerz Bayer. Vereinsbank Bayer. Landesbank	Inst. Bancario S. Paolo di Torino Banca Nazionale del Lavoro Banco di Roma Banca Comerciale Italiana
Spain	**Holland**	**Belgium**	**Switzerland**
Hispano Central Bilbao–Vizcaya Santander	ABN AMRO Rabobank	Générale de Banque UBS SBS	Crédit Suisse

Sources: *Times 1,000, Banking Almanac.*

respectively in 1862, 1864 and 1872); the Deutsche Bank and the Dresdner Bank in Germany (1870 and 1872); the Banco di Roma and the Banca Commerciale Italiana in Italy (1880 and 1894); the Banco Bilbao–Vizcaya and the Banco Central Hispano in Spain (1857, 1900); the Crédit Suisse and the Swiss Bank Corporation in Switzerland (1856 and 1872); the ABN AMRO in Holland (its oldest constituent, the Nederlandsche Handel-Maatchappij, was founded in 1824); and of course the Générale de Banque in Belgium, founded as early as 1822. Half of the leading European banks in the early 1990s – 15 out of 30 – belonged to this first group, a very high proportion indeed. A few giants thus emerged at a very early stage in the history of modern banking development and have been able to retain their position since then.

A second group, making up about just under a quarter of the whole, consists of what we could call the 'challengers', those banks which were able to rise to the top at a later stage of the development of joint stock banking. They were usually the result of mergers between two or several second-ranking firms among the large banking institutions. Such moves first took place in Britain: Barclays Bank was founded in 1896 through the simultaneous merger of 20 private banks whose partners were all linked by family ties;[3] while Lloyds and Midland (now part of the HSBC Group) are unique examples of provincial banks rising to the top through a systematic amalgamation policy.[4] In Switzerland, the Union Bank of Switzerland was created in 1912 by the merger of two middle-sized banks, the Bank in Winterthur and the Toggenburger Bank. In Germany, the Commerzbank, though founded in 1870 in Hamburg, did not reach a leading position before its mergers with the Mitteldeutsche Privat-Bank in 1920, and then with the Mitteldeutsche Creditbank in 1929. Similar steps were taken after the Second World War: in 1971 the Bayerische Vereinsbank (established 1869) merged with the Bayerische Staatsbank (established 1780) to become Germany's fourth largest bank; while, in Spain, Banco de Santander began its expansion in 1946 with the acquisition of several banking institutions and the opening of branch offices abroad.

The third group of banks reached the top through a completely different route: they emerged from the world of savings banks, mortgage banks and cooperative banks, which until recently had lived apart from the world of commercial banking. In Britain, Abbey National was a building society before becoming a bank and was converted from a mutual society to a public limited company in 1989.[5] Other building societies have recently followed a similar path, in the first place the Halifax, which in 1997 became one of the country's largest banks. In France the Crédit Agricole, at one time the world's largest bank, started with the 1894 law authorizing farmers to form small local mutual societies, the *Caisses Locales de Crédit Agricole Mutuel*.[6] In Germany the Westdeutsche Landesbank (WestLB), the Bayerische Hypotheken- und Wechsel-Bank (Hypo-Bank) and the Bayerische Landesbank started as mortgage banks or savings banks. The Banca Nazionale del Lavoro in Italy and the Rabobank in the Netherlands both have their roots in the cooperative movement. Altogether a surprising 27 per cent (8 out of 30) of the largest European banks in 1995 had such origins. Their expansion, however, has been fairly recent – with the exception of the Hypo-Bank, already the eleventh largest bank in Europe (and the third in Germany) by 1913.[7] Starting from a fairly narrow basis, banks such as Crédit Agricole, Banca Nazionale del Lavoro, Rabobank, WestLB (formed in 1969 by the merger of Rheinische Girozentrale und Provinzialbank and Landesbank für Westfalen Girozentrale) considerably enlarged the range of their clients and the scope of their activities in the decades following the Second World War.

2. Is there a meaningful relationship between banking consolidation and concentration?

The developments described above form merely the tip of the iceberg. Underneath, the banking population has remained very dense. Contrary to what one might think, consolidation has not been accompanied by a sharp decline in the number of banks. There were more than 23 500 banks in Germany in 1913, and still more than 22 000 in 1938, that is after the emergence of the so-called 'Big Three' (Deutsche, Dresdsner and Commerz) – though it must be admitted that over 19 000 of them were cooperative banks.[8] There were nearly a thousand banks and *établissements financiers* in France in 1960, *not* including the publicly owned savings banks which kept their balances with the Caisse des Dépôts et Consignations;[9] and as many as 319 banks in tiny Switzerland.[10] The number of commercial banks tended to decline more rapidly. Britain is of course the standard example, with a fall from 357 in 1880 to 75 in 1920, and only 16 for England and Wales in 1934.[11] The decline was more gradual in other countries, especially France, Germany and Italy, and did not really take place before the 1930s.

Interestingly the trend has been towards an increase in the number of banks in the last two decades as a result of financial innovation, globalization and deregulation. After falling to 3792 in 1960, the number of banks in Germany rose by 600 to 4390 in 1988. In Britain the number of banking institutions, including building societies, increased from 773 to 784 between 1983 and 1988, and in Switzerland from 593 to 630.[12] 'Specialized' banks and foreign banks have been mainly responsible for this resurgence, though many of the newcomers were subsidiaries of foreign or domestic financial institutions.

Similarly banking consolidation and banking concentration have not necessarily gone hand in hand. Comparing banking concentration among European countries is notoriously difficult for the early part of the twentieth century. Statistics are not available for all countries, and those available are based on heterogeneous banking populations. French figures, for example, are usually based on banks publishing their balance-sheets, British figures on deposit banks only and German figures on the entire banking system, including savings banks and cooperative banks. Nevertheless some general trends can be perceived.

Table 1.2 Percentage of top firms in total assets, 1988

Great Britain	32.6	Belgium	84.7
France	63.0	Denmark	50.9
Germany	31.2	Portugal	49.7
Italy	55.1	Ireland	71.0
Spain	34.7		
Holland	71.3		

Source: Gardiner, E.P.M. and Molyneux, P. (1990), *Changes in Western European Banking*, London: Unwin Hyman.

Let us start, once again, with the situation in recent years. This can be considered as the – transitory – outcome of a century of banking consolidation. A convenient measure is the share of total assets held by a country's top five banking institutions. Figures for 1988 are given in Table 1.2. They reveal a high degree of banking concentration (more than 50 per cent of total assets held by the five largest banks) in all major European countries with the exception of Britain, Germany and Spain. (Spain is dealt with in detail by Gabriel Tortella in Chapter 2). Britain and Germany, for their part, experienced a contrasting development. A low level of concentration has been a permanent feature of German banking. In 1913, for example, the nine big Berlin banks did not control more than 12 per cent of the banks' total assets. Significantly this percentage remained fairly stable in the following half-century or so (11.6 per cent in 1938 as well as in 1960). This was a consequence of the strength of the public and mutual sectors of German banking, especially the savings banks which by the late 1980s still accounted for more than 20 per cent of the banks' total assets, having reached 45 per cent in 1938.

In Britain, by contrast, the 'Big Five' consolidated their position during the first half of the twentieth century, controlling some 80 per cent of the clearing banks' deposits – but the percentage falls to under 50 per cent if accepting houses, overseas banks, discount houses, finance houses, savings banks and building societies are taken into account.[13] However, clearing banks increasingly lost market share after the Second World War and especially in the last 30 years. This has been the result of the growth of other financial intermediaries, in the first place foreign banks. Overseas banks (mostly British-owned banks operating in the empire or in foreign countries) had always been an important constituent of the British banking system, though they did not account for more than about 8 per cent of banks' assets in 1951. The percentage had jumped to 65 per cent by 1979, thanks to the addition of the branches and subsidiaries of foreign banks in Britain, especially American banks which alone contributed 27 per cent.[14] In Germany, by contrast, less than 2 per cent of banks' assets were held by branches of foreign banks in 1988. The only other European country approaching Britain in terms of foreign banks' penetration was Belgium, where more than 35 per cent of banks' assets were in foreign hands in 1988, a percentage which stood at around 11 to 15 per cent in most other countries.[15]

Despite differences between European countries, the general trend in the relationship between consolidation and concentration has been the conjunction of two apparently contrary movements: on the one hand the increased dominance of a handful of large banks; and on the other hand a relative deconcentration at the level of the banking systems taken as a whole, especially in countries with strong foreign banking penetration. One of the explanations for this apparent contradiction is the high level of concentration existing within certain banking activities and within certain banking categories. In continental Europe, for example, international banking activities have been concentrated in the hands of the big banks, and this has helped them to establish a dominant position, whatever their share of domestic banking.[16] Germany and Switzerland are particularly revealing in that respect.

Concentration has also tended to increase within commercial banking (as opposed to savings banks, cooperative banks, mortgage banks and other types of specialized banks). Britain is of course the standard case. But even in Germany, where the commercial banks' share of total assets fell from 49 per cent in 1925 to only 15 per cent in 1938, the Berlin banks' share of *commercial* banks' assets rose from 25 to 70 per cent during the same period.[17] In France, the four largest banks (Crédit Lyonnais, Société Générale, Comptoir d'Escompte, Crédit Industriel et Commercial) controlled 59 per cent of the commercial and investment banks' deposits in 1913,[18] but only 30 per cent of the country's total deposits, if publicly owned financial institutions (primarily the savings banks and the Caisse des Dépôts et Consignations) are taken into account; by 1937, with the loss of confidence resulting from the depression, that share had fallen to only 17 per cent, while that of the savings banks and the Caisse des Dépôts had risen to a staggering 66 per cent.[19] The overall level of concentration, however, increased after the Second World War. With the nationalization of the deposit banks in 1946, the distinction between private and public sectors lost much of its relevance. However, the market share of the largest banking institutions increased significantly as a result of three factors: the growth of the large deposit banks and of the *banques d'affaires* (especially Paribas); the rise of the Crédit Agricole; and the relative decline of the savings banks.[20]

3. What has been the role of mergers in the consolidation process?

Mergers have played a significant, though by no means an exclusive, part in the consolidation process. In a first phase lasting until the First World War, large banks established a dominant position by pursuing three types of strategies: amalgamation with other banks; alliances through interest groups; and internal growth. To a certain extent these three strategies have been used simultaneously in all countries. However, in the three major European economies (Britain, France and Germany) the general trend has been for one model to prevail in each country.

The mergers and acquisitions model is best exemplified by Britain. By the early twentieth century, a dozen banks based in London with a network of provincial branches had emerged at the top of the English banking system. This was the result of an intense amalgamation movement, which started in the mid-nineteenth century, gathered pace in the 1890s following the Baring crisis, and kept its momentum until the First World War. The largest British bank in the 1880s, the National Provincial Bank, founded in 1833, acquired 27 banks in the previous four decades. It was, however, overtaken by Lloyds and Midland, the growth of which was entirely due to their amalgamation policy: Lloyds Bank acquired 33 banks between 1890 and 1914, the Midland 23. The two most prestigious London joint stock banks, the London and County Banking Company and the London and Westminster Bank, which had remained outside the amalgamation movement until the early twentieth century, had to merge in 1909 to keep their position at the top of the British banking hierarchy.[21]

The consolidating model based on the formation of common interest groups is most usually associated with Germany. The big German banks hardly opened any branch outside Berlin, nor did they launch into a large-scale amalgamation policy. Instead, they established a 'community of interests' (Interessengemeinschaft), based on cross-shareholding and pooled profits, with a number of provincial banks.[22] The Deutsche Bank had such links with 14 banks, including large provincial banks, such as the Bergisch Märkische Bank, the capital of which stood at 60 million marks. The constellations formed by such banking groups could reach gigantic sizes. The Deutsche Bank group's capital and reserves, for example, amounted to over 700 million marks in 1904.[23] German banks, however, followed the British model of mergers and acquisitions after the First World War. In the inflationary climate of the early 1920s, the great banks were encouraged to take over the provincial banks with which they were already linked through 'communities of interests'. The Deutsche Bank, for example, took over seven banks between 1920 and 1924, extending its network of branches from 15 in 1913 to 142 in 1924.[24] Other mergers, involving medium-sized and large banks, also took place during this period, for example between the Darmstädter Bank and the National Bank in 1922, to form the Danat Bank.

Finally, internal growth has been the dominant feature in the consolidation of French banking. The leading banks established a national network of branches without taking over local banks. The Crédit Lyonnais took over a single bank before 1914, the Comptoir d'Escompte only eight. Banking groups admittedly also existed in France, though they were formed on a different basis. They tended to be business rather than strictly banking groups, transcending the frontiers of banking to include insurance companies, industrial companies, colonial companies, utilities and others. They were based on a majority or a minority stake held by a large bank in these companies, usually reinforced by overlapping directorships.[25] Strategic control was especially strong in the groups built around a *banque d'affaires*.[26]

'Big mergers', bringing together front-ranking banks, have been a characteristic of the second phase of banking consolidation and have shaped several countries' modern banking systems. The earliest took place in England in 1918, when five mergers, involving the ten largest banks in the country, resulted in the formation of five huge banks which immediately came to be known as the 'Big Five': Barclays, Lloyds, Midland, National Provincial, and Westminster (the last two merged in 1968 to form the National Westminster Bank). Germany followed a decade or so later: today's 'Big Three' (Deutsche, Dresdner and Commerz) originated from similarly far-reaching mergers: in 1929 between Deutsche Bank and Disconto-Gesellschaft, and in 1931 between Dresdner Bank and Danat Bank (the latter, however, following serious liquidity problems and imposed by the German government). Consolidation was pushed even further in the Netherlands: two mergers, involving the country's four largest banks, took place in 1964, leading to the formation of Algemene Bank Nederland (ABN) and Amsterdam–Rotterdam Bank; these two banks then merged in 1991 to form ABN AMRO. In Spain, mergers between major banks took place in the late 1980s and early 1990s, involving the two largest Basque banks, the two largest Catalan banks and two large Madrid banks. Interestingly, however, such big mergers have played no part in the consolidation process of countries such as France, Italy, Switzerland, or Belgium which all have higher levels of banking concentration. The Netherlands is different in this respect.

4. What have been the respective influences of market mechanisms and state intervention?

Factors affecting banking consolidation can conveniently be divided into two groups: market mechanisms and government intervention. For example, market mechanisms were fully at play in the amalgamation movement in British banking in the late nineteenth and early twentieth century, while government intervention was paramount in the mergers following the German banking crisis of 1931. The two factors, however, often interacted, especially from the 1930s onwards. This is not the place to discuss the specific circumstances in which consolidation has proceeded or receded. Some details about the way mergers were conducted, their costs and benefits, are given in subsequent chapters, while the role of the state is discussed by Ginette Kurgan in Chapter 6. This section will thus be limited to a few observations concerning these two general trends.

As far as market mechanisms are concerned, one should not forget the human and social dimensions. First, there is the role played by leading personalities – the entrepreneurs, who are all too often forgotten in banking history. The first name to spring to mind is of course Edward Holden (1842–1919), the man who transformed a medium-sized provincial bank into the largest bank in the world.[27] But there were other empire builders during this exceptional period of British banking history; for example, Howard Lloyd (1837–1920), the real creator of the modern Lloyds Bank, by means of a policy that, like Holden's, was dynamic, if not to say aggressive.[28] Other men were instrumental in bringing about a decisive merger; for example, Emile Francqui (1863–1935) was the architect of the timely takeover of the Banque d'Outremer by the Société Générale de Belgique in 1928.[29] Second, there is the role played by networks of relationships, whether based on family links, common religious beliefs or personal friendship. The foundation of Barclays Bank in 1896 brought together 20 private banks whose partners were all linked by a dense network of family connections and common membership of the Quaker sect.[30] Conversely, personal sensitivities seem to have prevented a merger between the Deutsche Bank and the Danat Bank, thus paving the way for the mega-merger with the Disconto-Gesellschaft in 1929.[31]

Mergers are meant to make sense economically.[32] The decisive motives behind the merger between the Deutsche Bank and the Disconto-Gesellschaft were 'considerations of cost reduction and anxieties about the availability of long-term capital, rather than visions of grandeur'.[33] Edward Holden did have a grand design – to make his bank 'one of the first in the kingdom'. But his analysis of the advantages derived from his most important amalgamation so far (with the City Bank in 1898) was far more practical and included the reserve fund (to become 'the largest of the Kingdom except the Bank of England'); the sum carried forward (increased by £20 000); additional profits; having secured 'most desirable Bank premises for Head Office' (which would otherwise have cost £200 000); as well as the improved prestige of the Bank in London.[34] However, another often forgotten aspect of the consolidation process is the occasional fashion, the recurrent moods of the market. The City of London, perhaps more than any other financial centre, could be seized by such fevers. This was undoubtedly the case in the 1890s, when the City's private bankers became resigned about their loss of independence and a race for size took place between the leading British banks.[35] Almost a century later stockbrokers, and especially jobbers, took a similar view concerning their fate as British and foreign banks engaged in a surge of buying in preparation for the 'Big Bang' of 1987.[36]

State intervention can have a direct effect on banking consolidation. It can reinforce consolidation by promoting mergers – as in the case of the 1966 merger between the Banque Nationale de Crédit and the Comptoir National d'Escompte de Paris to form the largest French bank, the Banque Nationale de Paris; or it can restrain it by discouraging mergers – for example the recommendation of the Treasury Committee on Bank Amalgamations (appointed in 1918), which led to the understanding given to the government by the banks that all proposed amalgamations were to be submitted to the Treasury and Board of Trade and concluded only with their consent. However, the effects of state intervention can also be indirect and exacerbate underlying market conditions. The decision to create the Swiss National Bank in 1905 and to grant it a monopoly for issuing banknotes made the activities of existing issuing banks redundant. There followed an intense concentration movement in Switzerland, with 76 banks being taken over and another 37 liquidated between 1911 and 1920.[37] Wars and international treaties could also influence events. The high level of banking concentration in Austria in the interwar years was an indirect effect of the partition of the Habsburg monarchy – 'a process of contraction rather than of concentration'.[38] Conversely, deconcentration could follow regulations requiring the separation between deposit and investment banking, as in Belgium in 1934 or Italy in 1936, though the effects could be offset by the formation of holding companies.

5. Has there been a discernible chronological pattern?

Can chronological trends be perceived in the process of banking consolidation? One would be tempted to reply in the negative. One reason is that consolidation has been a more or less continuous process in the last hundred years and even longer, starting with the appearance of the modern joint stock banks and still going on today. Ernest Sykes's classical study of the amalgamation movement in English banking takes 1826 as a starting point, the year a law first authorized the formation of joint stock banks: mergers and takeovers quickly ensued. The large French deposit banks, established in the 1860s, immediately started to consolidate their position at the expense of local private bankers by building a national network of branches: ten years after its foundation in 1864, the Société Générale had already established 80 provincial branches, while the Crédit Lyonnnais, founded in 1863, had 70 branches by the mid-1880s.[39]

It is true that in Britain the consolidation process reached a climax in the 1890s and 1900s and came to a halt in the early 1920s, following the creation of the 'Big Five' and the affiliation of Irish and Scottish banks. This, however, does not apply to continental Europe, where it intensified in the 1920s and 1930s. The German big banks embarked on mass acquisitions in the early 1920s. In France the larger provincial banks strengthened their position at the expense of the local banks. In Belgium the expansion of the Société Générale reached its climax in 1930, with the bank controlling 55 per cent of the resources of the principal Belgian banks and groups.[40] The Depression of the 1930s, if anything, accelerated the process. In Austria the 1934 merger between the Creditanstalt (following its collapse and rescue in 1931) and the Wiener Bankverein resulted in the domination of a single bank over the entire Austrian banking system. Private banks were particularly affected by the Depression. In Germany the number of private banks fell from an estimated 2000 in 1929 to an estimated 1350 in 1937, as a result of the one-sided government aid for the 'great' banks at the height of the 1931 crisis, the increasing competition from the savings banks as well as the 'Aryanization' policy of the Nazi regime.[41] In France nearly 600 banks disappeared between 1930 and 1934.[42] The 1950s are usually seen as a relatively quiet period as far as banking consolidation is concerned. However, the reconstruction of the three German 'great' banks (Deutsche, Dresdner and Commerzbank), dismantled by the Allies at the end of the Second World War, was a major step in the consolidation process of German banking. And since the 1960s in all European countries the combined effects of innovations, deregulation, globalization and competition have reactivated the trend towards consolidation.

Chronological patterns are of course more easily identifiable at the national level. National cases cannot be discussed individually in this general survey. One question, however, must be briefly addressed: has there been any link between consolidation, and more specifically merger activity, and the economic situation? In most countries it is often assumed that mergers are more likely to take place during an economic depression.[43] With the exception of England, however, such a proposition has not been systematically tested. Our impressionistic and cursory survey of the European scene rather suggests a continuous process; and, as far as England is concerned, Capie and Rodrik-Bali reach the conclusion that 'neither periods of prosperity nor depression, contraction nor expansion in the economy influenced the rate at which firms merged'.[44] Further research is obviously needed on the subject. In the meantime one has to be content with very wide time spans, in other words meaningless chronological trends, such as the period from the early twentieth century to the 1930s, or from the mid-1960s to the present.

6. Has there been an international dimension to the consolidation process?

The lack of a European chronological trend may well be due to the fact that banking consolidation has so far remained confined within national frontiers. Consolidation in international banking has mainly concerned overseas banks, especially the British overseas banks, whose development by far exceeded that of any other European country: from 27 in 1928, and still 18 in 1955, their number shrank to nine in 1970, and multinational banking became integrated into the British commercial banks.[45] Mergers between European banks have been rare, though their occurrence has increased in recent years, especially in the form of the acquisition of small specialized banks by large universal banks. The most common, though by no means the only cases, have been the takeovers of City merchant banks by large continental European banks.

Such moves, however, are only small steps in the consolidation process of European banking.

Mergers, especially big mergers, are not the only path towards consolidation. In some countries, the largest banks have been able to expand through internal growth. This, however, would be impossible on the European stage. So far authorities have generally opposed the absorption of large commercial banks by foreign concerns, even in a society as liberal as Britain. In the acquisition of the Midland Bank by the HSBC Group in 1992, the suitor was regarded as an acceptable marriage partner both because of the British influence within its management since its foundation in 1865 and because of the recent shift of its domicile from Hong Kong to the United Kingdom. The only merger between two leading European banks took place when the French Suez group acquired control of the Société Générale de Belgique in 1988. One of the reasons for such sensitivity on the part of the state is the central role played by large banks within the economy, particularly during the twentieth century. The likelihood of mergers between large European banks thus depends on the degree of economic integration, in particular monetary union. The advent of the Euro could thus herald a new era in the history of banking consolidation in Europe. It is to be hoped that meaningful lessons will still be learnt from the study of past national experiences.

Notes

1. No attempt has been made to update the analysis up to 1998, as any update would be immediately superseded by current events.
2. Information on the history of individual banks can be found in the volume edited by the European Association for Banking History (1994), *Handbook on the History of European Banks*, Aldershot: Edward Elgar, as well as in numerous monographs which cannot be listed here. For bibliographical references, see Cassis, Y. and Cottrell, P.L. (1994), 'Financial History', in *Financial History Review*, **1** (1), and Goodall, F., Gourvish, T. and Tolliday, S. (eds) (1997), *International Bibliography of Business History*, London: Routledge.
3. See Matthews, P.W. and Tuke, A.W. (1926), *History of Barclays Bank*, London.
4. See Sayers, R.S. (1957), *Lloyds Bank in the History of English Banking*, Oxford; Holmes, A.R. and Green, E. (1986), *Midland: 150 Years of Banking Business*, London.
5. See Reid, M. (n.d.), *Abbey National. Conversion to PLC*, London.
6. See Gueslin, A. (1984), *Histoire des crédits agricoles*, Paris.
7. See Cottrell, P.L. (1998), 'Concentration and internationalization: Aspects of banking in northern and central Europe, 1880–1913', in Kinsey, Sara and Newton, Lucy (eds), *International Banking in an Age of Transition: Globalisation, Automation, Banks and their Archives*, Aldershot/

Brookfield VT: Ashgate Publishing Ltd for EABH, paper presented at the Symposium in honour of Dr Wilfried Guth, Frankfurt am Main, 2 November 1995.

8. Hardach, G. (1995), 'Banking in Germany, 1918–1939', in Feinstein, C.H. (ed.) (1995), *Banking, Currency and Finance in Europe between the Wars*, Oxford: Clarendon Press.
9. Wilson, J.S.G. (1962), 'France', in Sayers, R.S. (ed.) (1962), *Banking in Western Europe*, Oxford: Clarendon Press.
10. Ritzmann, F. (1973), *Die Schweizer Banken. Geschichte – Theorie – Statistik*, Bern.
11. Banking specialities performed by discount houses, merchant banks, overseas banks, savings banks and building societies are usually not included in British banking statistics for the early twentieth century; their inclusion would raise the figure to several hundreds.
12. See Sayers (ed.) (1990), *Banking in Western Europe*; Gardener, E.P.M. and Molyneux, P. (1990), *Changes in Western European Banking*, London: Unwin Hyman.
13. See figures in Collins, M. (1989), *Money and Banking in the UK. A History*, London: Croom Helm.
14. Ibid., chs 11 and 12.
15. Gardener and Molyneux, *Changes in Western European Banking.*
16. In Britain, by contrast, such operations were left for a long time to merchant banks and overseas banks.
17. Hardach, 'Banking in Germany'. Interestingly, the number of savings banks, though still high, fell from 866 in 1960 to 585 in 1988, while their total assets increased by more than five times.
18. Bouvier, J. (1973), *Un siècle de banque française*, Paris, p. 123. The figure is based on banks which published their balance sheet.
19. See figures in Gueslin, A. (1992), 'Banks and the state in France from the 1880s to the 1930s: the impossible advance of the banks', in Cassis, Y. (ed.) (1992), *Finance and Financiers in European History 1880–1960*, Cambridge: Cambridge University Press.
20. The market, however, was not closed to new entrants in the shape of specialized banking institutions and finance companies, which were able to control as much as 20 per cent of banks' assets by 1988.
21. See Cassis, Y. (1994), *City Bankers, 1890–1914*, Cambridge: Cambridge University Press; Capie, F. and Rodrik-Bali, G. (1982), 'Concentration in British Banking, 1870–1920', *Business History*, 29 (3); Sykes, J. (1926), *The Amalgamation Movement in English Banking*, London: P.S. King & Son.
22. See Pohl, M. (1982), *Konzentration im deutschen Bankwesen (1848–1980)*, Frankfurt am Main.
23. Riesser, J. (1906), *Zur Entwicklungsgeschichte der deutschen Grossbanken mit besonderer Rücksicht auf die Konzentrationbestrebungen*, Jena, p. 228.
24. Feldman, G.D. (1992), 'Banks and Banking in Germany after the First World War: strategies of defence', in Cassis (ed.), *Finance and Financiers in European History*; and 'The Deutsche Bank from World War to World economic Crisis' in Gall, L. et al. (1995), *The Deutsche Bank, 1870–1995*, London: Weidenfeld & Nicolson.
25. See Bouvier, *Un siècle de banque française*, pp. 102–9; Bonin, H. (1995), *Les groupes financiers français*, Paris.

26. See for example Bussière, E. (1992), *Paribas. Europe and the World 1872–1992*, Antwerp. Similar business groups existed around the Belgian universal banks, alongside more narrowly defined banking groups: in 1930 for example the Société Générale group included the Banque d'Anvers, the Banque Italo-Belge and a number of subsidiaries of the Société Générale. See Kurgan-van Hentenryk, G. (1992), 'Finance and Financiers in Belgium, 1880–1940', in Cassis (ed.), *Finance and Financiers in European History*.
27. See Edwin Green's chapter in this volume (Chapter 4) as well as his entry, 'Holden, Sir Edward Hopkinson (1848–1919), Clearing banker', in Jeremy, D. (ed.) (1984–86), *Dictionary of Business Biography*, 5 vols, London: Butterworths, vol. 3.
28. See Sayers, *Lloyds Bank*.
29. See Kurgan-van Hentenryk, G. (1996), 'Francqui Emile', in Kurgan-van Hentenryk, G., Jaumain, S. and Montens, V. (eds) (1986), *Dictionnaire des patrons en Belgique*, Bruxelles.
30. See Matthews and Tuke, *History of Barclays Bank*; Cassis, *City Bankers*.
31. Feldman, 'The Deutsche Bank from World War to World Economic Crisis', pp. 231–2.
32. For a discussion of the contrasting conclusions reached by the literature on this issue see Gabriel Tortella's chapter in this book (Chapter 2).
33. Feldman, 'The Deutsche Bank from World War to World Economic Crisis', p. 233.
34. Midland Bank Archives, Edward Holden's Letter Book. Letter to J.K. Brown, 7 October 1898.
35. See Cassis, *City Bankers*, pp. 21–2, 46–9; Sykes, *Amalgamation Movement*, pp. 48–9.
36. See Reid, M. (1988), *All-Change in the City. The Revolution in Britain's Financial Sector*, Basingstoke and London: Macmillan; and David Kynaston's chapter in this book (Chapter 9).
37. See Ritzmann, *Schweizer Banken*. Among issuing banks, however, cantonal banks, which were public institutions, were able to remain independent.
38. Weber, F. (1995), 'From Imperial to Regional Banking: The Austrian Banking System, 1918–1938', in Feinstein (ed.), *Banking, Currency and Finance*, p. 337.
39. Bouvier, J. (1973), *Un siècle de banque française*, Paris, p. 201.
40. Kurgan, 'Finance and Financiers in Belgium', pp. 320 and 326.
41. See Wixforth, H. and Ziegler, D. (1994) 'The niche in the universal banking system: the role and significance of private bankers within German industry, 1900–1933', *Financial History Review*, 1 (2).
42. See Plessis, A. (1991), 'Les banques, le crédit et l'économie', in Lévy-Leboyer, M. and Casanova, J.-C. (eds) (1991), *Entre l'Etat et le marché. L'économie française des années 1880s à nos jours*, Paris, p. 356.
43. Bouvier, *Un siècle de banque française*; Pohl, *Konzentration im deutschen Bankwesen*; Higonnet, R.P. (1957), 'Bank Deposits in the UK 1870–1814, *Quarterly Journal of Economics*, 71 (3), quoted by Capie and Rodrik-Bali, 'Concentration in British Banking'.
44. Capie and Rodrik-Bali, 'Concentration in British Banking', p. 290.
45. See Jones, G. (1993), *British Multinational Banking 1830–1990*, Oxford: Clarendon Press.

CHAPTER TWO

Bank Mergers and Consolidation in Spanish History[1]

Gabriel Tortella

Why do bank mergers take place? The straightforward answer for an economist should be: because there are economies of scale and scope (*à la* Chandler) in banking as in other branches of economic activity. This would mean that when two banks merge, or when one bank absorbs another, the resulting larger unit is more profitable than the previous two units in isolation. A key concept often mentioned here is *synergy*, a word which is not included in all dictionaries (*synergism* seems to be preferred), but which refers to the combination or common action of two organisms having effects which are not achievable by each organism separately. This is a rather biological concept, and why synergism should appear in living beings is something I cannot speculate upon here. In economics, however, this synergism can only be derived from economies of scale and/or scope.[2] Economies of scale or scope imply the existence of fixed costs, that is, costs which do not increase in proportion to output. Economies of scale or fixed costs thus seem to be the most acceptable explanation for mergers and combinations, in banking and in other fields of enterprise. However, many students (and at least some bankers I have talked to) doubt the existence of economies of scale in banking as a general rule. In fact the case for economies of scale as a powerful factor in bank mergers is widely disputed, and while there is no agreement on this point, the majority of scholars seem to be sceptical, although there is a respectable minority who affirm their existence. Here I am going to give a sample of academic opinion, mostly dealing with bank mergers in the United States, which is the most thoroughly researched country, although there is a growing body of studies on European countries, including Spain. Then I will deal with my main topic, bank mergers in Spanish history.

The international evidence

Boyd and Graham,[3] for example, note that most studies fail to find economies of scale in the US banking industry for firms with deposits above $100 million, and according to Houston and Ryngaert (1994, p. 1156) 'recent studies of actual mergers between banking institutions with assets in excess of $100 million find little evidence of a decrease in operating expenses arising from the mergers'. Caves (1987, pp. 164–5) is even more specific: 'little evidence connects the empirical achievement of [synergistic] gains to merger transactions'. In the same collective book as Caves, Ravenscraft makes an assertion which also implies the rejection of the *synergy* explanation: 'Although the stock market reacts positively to merger announcements, bidding up the stock prices of target companies, [...] mergers and acquisitions do not improve the postmerger performance of combining firms.' Another author who doubts the synergy theory is Brooks (1987, pp. 238–9), who thinks 'it has been largely discredited by the collapse and progressive dismantling of the conglomerates formed' during the 1960s, the period when the theory was most in vogue. Chandler (1990, chs 4 and 5) shows that mergers and integration took place in industries with economies of scale, where firm size was profitable (oil, rubber, steel), whereas in labour-intensive industries (paper, glass, textiles, furniture, leather, and so on) amalgamation and mergers were less pervasive and less durable. Most people believe that, being a service industry, banking is labour intensive. These last four authors, however, are dealing with mergers in general, not only bank mergers.

Rhoades is perhaps the most adamant critic of bank conglomerations and one of the most sceptical about the alleged efficiency gains from such operations. In *Power, Empire Building and Mergers*, the title of which already makes clear what his thesis is (1983, pp. 151–2) he makes trenchant statements such as the following:

> Surely the evidence is clear about one thing – conglomerate and agglomerate mergers in this country [the US] since 1960 have in general provided no gains in economic efficiency [...] Some observers have contended that the requirements of modern technology [...] necessitate the replacement of many smaller companies with corporate giants. [However, this contention] does not accord with the facts. Indeed the evidence suggests just the opposite. Smaller and medium-size firms provide the best environment for research and development.

According to his study based upon the analysis of 898 bank mergers carried out in the United States between 1981 and 1986, and measuring efficiency by means of various expense ratios, and whose results, 'based on OLS [ordinary least squares] and logit analyses are robust [..., the findings] indicate that during 1981–1986, horizontal bank mergers did not yield efficiency gains.'

A parallel opinion is held by Rose (1989), who, after a study of the main characteristics of bank mergers in the United States, finds that:

> Acquiring banks and bank holding companies tend *not* to average greater profitability than banks and banking companies that do not merge, nor is there any solid evidence of subsequent increases in profitability or greater future risk as an outcome of the merger process. Acquiring banks do not seem to grow faster, on average, than banks choosing not to merge.

In the same manner Madura and Wiant (1994) write about US bank mergers:

> We find a strong negative share-price reaction following the acquisition, which tends to continue over a 36-month period. The results suggest that banks generally do not realize the potential benefits from acquisitions, or that any advantages are offset [...]
>
> Several studies have analysed the market reaction to banks' acquisitions of other banks [...] The results vary with the sample studied.
>
> The results [of our tests] were negative [that is, they showed negative abnormal returns] regardless of the model used [...], the measurements of abnormal returns [...], and the measurement of cumulative abnormal returns [...] used to measure valuation effects. Our results are somewhat similar to those of Agrawal et al. (1992).

Although this seems to be the predominant view, it has been challenged by some authors. Alhadeff, the author of a classic book on *Monopoly and Competition in Banking* (which in fact is a defence of branch banking and a plea for its generalization in the United States), in a chapter on comparative cost patterns between small banks, large banks and branch banks, states as a matter of fact that 'unit costs vary inversely with size of bank' (1954, p. 77), basing this statement upon expense/loan ratios of a sample of California banks. This seems to be contradicted by the results of Rhoades's more recent (1986) study for the entire United States.

The opinions and findings of Hawawini and Swary (1990) also contrast sharply with those of Rhoades and most of the others cited above. Their method consists of measuring market reactions to the announcements of mergers in the week after the announcement has been made. They generally find a strong positive reaction (average increase 11.5 per cent) in the quotation of shares of target banks, and a small negative reaction (average fall of 1.5 per cent) in the market value of shares of bidders; from this they deduce that 'bank mergers create *net aggregate wealth* to shareholders. The dollar gains realized by the shareholders of target banks exceed the dollar losses incurred by the shareholders of bidding banks' (p. 211).

Hawawini and Swary also find that the 'magnitude of the target bank abnormal returns is positively correlated to the size of the bidding bank relative to that of the target bank [and] the absolute size of the bidding bank' (p. 211), which they interpret as 'consistent with the synergy hypothesis of mergers' (p. 169).

However, I find some problems with this reasoning: first, a week is a short time – other estimates for longer periods of time yield very different results, as we have seen; and, second, distinguishing between abnormal (that is, determined by the announcement) and normal fluctuations in share prices may pose serious estimation problems.

All in all, Hawawini and Swary have a clear preference for branch banking and the abolition of state limitations on banking (Glass-Steagall Act, etc.), and tend to view mergers as beneficial and as clear proof that the market prefers large, diversified banks. However, they make clear that 'except at relatively low output levels, there do not appear to be economies of scale [or] global economies of scope [, that is] there is no evidence to suggest that larger banking organizations have a cost advantage over small banks' (p. 3). In which case, if there are no economies of scale, where do these 'aggregations to net wealth' come from? We shall return to this question in due course.

Probably the most impressive defence of increasing returns to scale in banking that I have come across is made by McAllister and McManus (1993), who find fault with the statistical methods of their predecessors' research.

> Most previous empirical research of scale efficiency in banking has found increasing returns to scale only among relatively small banks, and *decreasing* returns to scale among larger banks. The present study shows that these results were biased by problems in the statistical techniques used [that is, translog cost functions] and by the fact that the models ignored an important input required for the intermediation process, financial capital [as a prevention against risk]. When econometric problems are solved and the relationship among size, diversification and risk is properly accounted for, there is strong evidence for increasing returns to scale for banks of about $500 million in total assets and approximately constant returns for larger banks. (p. 389)

However, this is not as novel as it sounds. Perhaps the main novelty in their research is their focus upon 'financial capital' as a source of economies of scale.