

## PRESS RELEASE

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### **BANK COMPETITION IS COMING, NO MATTER THE ELECTION RESULT**

*Heading into next month's election, the basic assumption is that no single party is likely to obtain an absolute majority. Therefore, manifestos will logically get 'diluted' by a coalition agreement, says Filippo Alloatti, Senior Credit Analyst, Hermes Credit.*

The matters affecting the banks directly – such as liquidity, capital and leverage ratios – are already being dealt with. The requirements from the BoE and PRA are already going well beyond global standards.

No matter what the election result may be, most of these reforms are practically irreversible. In fact, banks as diverse as HSBC, Barclays and RBS have begun to pave their paths towards the future, but regulation and conduct issues still loom.

#### **A focus on competition**

A lot of political focus appears to be on increasing competition in the banking sector. For example, Labour wants to see at least two large challenger banks. This might have already happened, or may be about to happen, with M&A between the second tier banks gaining pace. Other parties are proposing help to new and existing challenger banks. When talking about competition, it is also important not to forget the ongoing CMA investigation on retail banking competition, specifically in current account and SME lending.

The major parties are also seeking to establish a British Investment Bank, in the case of Labour, or the Conservative and LibDem-led expansion of the Business Bank. This will eventually provide competition to the incumbents, but volume from this new lender will be slow to pick up.

Since 2013, 11 new banks have been authorised by the PRA. Metro Bank was the first one to start afresh under the new two-step process. Five banks have listed on the stock exchange in the past year, with more to follow. The likes of RBS' G&W unit, Metro Bank and potentially Santander UK could be listed in the near term. Despite this, the 'Big 4' banks still command about 85% market share in current accounts, mortgage and SME lending.

#### **Importance of financial services**

Since 2011, the economy has done much better than literally anyone had forecast. Each side of the political spectrum is aware of the importance of financial services, given its weight in economy. Confidence is therefore crucial.

The banking sector is performing well and the loss ratio, arguably a lagging economic indicator, is still trending down on a year-on-year basis. Competitive pressures on asset margins, as well as subdued loan growth – both in mortgages and corporate lending – are themes to watch. The low volume in mortgage origination can be partially explained by the June 2014 introduction of the Mortgage Market Reform, which was a de facto tightening of underwriting criteria.

Issues to keep an eye on remain the same: rising taxes after the elections and the beginning of interest rate hikes.

#### **Final thoughts**

The noise surrounding Standard Chartered and HSBC – both penalised by a tax levy based on global liabilities – moving headquarters to Hong Kong or other Asian destinations is a 'sideshow' at the moment. Standard Chartered has already highlighted two main challenges in re-domiciliation; the likelihood of capital gains tax liability and re-applying for a number of banking licences. Both activities would take time.

Before any relocation, both Standard Chartered and HSBC need put their houses in order, especially StanChart. Reports of HSBC spinning-off its UK retail bank are very preliminary, and we simply do not know the technicalities. Will it dispose of the legal entity HSBC Bank Plc, de-consolidate it, or simply transfer the UK retail business out from this entity? As mentioned, it is too soon to obtain any clarity.

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#### **Notes to Editors:**

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