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# Bank Strategies in Euroland with Special Reference to the Benelux Area.

by

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DISCUSSION
PAPER

# BANK STRATEGIES IN EUROLAND
# WITH SPECIAL REFERENCE TO THE BENELUX AREA

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## ABSTRACT

In its first part, the present essay focuses on one main thesis. The transition to full EMU and the introduction of the euro will have a more lasting effect on European banking than the previous Single Market Project (Europe 1992). They deal directly with money, the basic material of banking, and they pave the way to more aggressive bank strategies. In conjunction with other factors, they not only induce “accommodating” reactions, mainly through cost-cutting, but also “autonomous restructurings” : less intermediation, more market activities and, most of all, external growth through M(ergers) and A(cquisitions). This significantly changes the structure and the policies of European banking.

Recently important and controversial M and A have occurred in the Benelux area. In the second part of the essay, these developments are analysed in the just described framework. After a global overview two case studies are presented : ABN-AMRO, n° 1 in the Netherlands; the GENERALE BANK, n° 1 in Belgium. The main conclusion is that the rationale behind the recent M and A is not mere size, but also accelerated rationalisation and penetration in foreign domestic markets, which was previously hampered by defensive and ultimately self-defeating strategies of strengthening the mere national domestic base. However, at the present stage, the importance of institutional resistance, even in small neighbouring countries, should not be under-estimated. Hence, cross-border restructurings in European banking will only increase gradually.


Key words : EMU, euro, bankstrategies, Benelux financial systems.

# BANK STRATEGIES IN EUROLAND WITH SPECIAL REFERENCE TO THE BENELUX ARIA[1]

## INTRODUCTION : CHANGING EMPHASIS IN EUROPEAN BANK STRATEGIES

In a survey of European banking and bankers carried out in 1993 by Arthur ANDERSEN, the EU Single Market Programme (the “Europe 1992” project”) was ranked first as a major driving force for the bank strategies in the years to come. Nevertheless, in a postal survey organised some years later (1995-1996) in the framework of the Single Market Review, the same factor ranked only fifth in the list (see figure 1). Technological change, domestic competition and domestic regulatory developments appeared to be the fundamental factors influencing bank strategies.

FIGURE 1 - THE RELATIVE IMPORTANCE OF SEVERAL FACTORS INFLUENCING BANK STRATEGIES

| Factor influencing strategy | Arthur Andersen (1993) [1] | Postal survey [2] |
|---|---|---|
| Technological change | 5 | 83 |
| Competition from domestic firms | * | 76 |
| Competition between banks and non-banks | 2 | 68 |
| Domestic regulatory developments | 4 | 65 |
| EU Single Market Programme | 1 | 65 |
| Competition from financial firms in other EU countries | 3 | 53 |
| Competition from financial firms in other non-EU countries | 3 | 47 |

* Not available
1 Ranking
2 Where 0 is “not important”, 25 is “of little importance”, 50 is “quite important”, 75 is “very important”, and 100 is

Source : European survey by Arthur Andersen carried out in 1993 and postal survey.
Source : Economic Research Europe (ERE) for the European Commission, 1997, table 4.38.

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1 A preliminary and incomplete version of the present essay was presented at the seminar on “The changeover to euro-fixed exchange rates, competition among EU countries and strategies of European banks”, jointly organised by the Associazone per lo Sviluppo degli Studi di Banca e Borsa and the Università Cattolica del S. Cuore, Secunda Facoltà di Economia at Angera on June 18-19, 1998. The present version has very much benefited from the discussion at this seminar and at the Annual Meeting of the European Association of University Teachers in Banking and Finance (Paris, September 1998). Valuable comments and corrections have been provided by Pierre Gilard, Dirk Heremans, Gaston Reinesch, Patrick Van Cayseele, Rudi Vander Vennet and Jerry Van Waterschoot. The author also gratefully acknowledges the help of the Belgian Bankers Association, the Netherlands Institute for Banking and Stockbrokering Industry, the Luxembourg Ministry of Finance and the Studies Department of the Artesia Bank Brussels, in collecting information and data.

One of the reasons mentioned by the authors is : "*The SMP has become implemented and more effective during 1992-96, .. its specific (perceived) impact on bankers' strategies has apparently reduced*" (p. 109). My explanation is that the SMP exerted its influence in conjunction with other driving forces. It worked mainly in an indirect and defensive way : "*The Single Market Programme exerted its main influence via national deregulation and modernization. The interaction and the combination of European integration and national deregulation increased the contestability of domestic financial markets. It induced the major domestic banks in various countries to strengthen their domestic base in order to avoid effective penetration by competitors, both domestic and foreign. The outcome was twofold : increased domestic competition and reduction of profitability for the major domestic banks, higher cost of entry into foreign customer markets, particularly in Northern and Western Europe*" (Abraham, 1997 a, p. 362-363).

In a more recent paper (June 1998), W.R. WHITE identifies changes in technology, deregulation, attitudes to shareholders value and demographic trends in the industrial countries as the "underlying forces for change" in European banking. In his opinion the euro may act as a catalyst for change but it is the underlying forces that will play a more important role in shaping the direction of that change" (p. 3). The implicit conclusion seems to be that the impact of the euro will be significant, but temporary.

The main thesis of the present paper is that the transition to full EMU (Stage Three) and the introduction of the euro also act in conjunction with other factors, which are now technological change, consolidation and globalisation. But its direct and specific influence is much more decisive and will have a more lasting impact than the SMP on the structure and the activity of financial markets and financial institutions. First, monetary integration with a single currency affects banking activity much more directly than the creation of a single market of goods and services, which also, but not primarily, includes financial services. In EMU, money by definition holds the stage and the banks are the prominent money changers and money dealers. They have to secure the conversion from national currencies into the euro, they will be the most important players on the financial markets of Euroland.

Secondly, the transition to full EMU makes more defensive strategies which only focus on strengthening and protecting the national domestic base increasingly self-defeating and obsolete. Euroland paves the way to and offers opportunities to a more aggressive approach to bank strategy.

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The first section of the present paper very briefly describes the various channels through which full EMU affects banking activity, and analyses its impact on several archetypes of bank strategies.

In the second section we focus on the changes of bank strategies in the three Benelux countries. After a general overview, two cases will be discussed : ABN-AMRO (Netherlands) and Generale Bank (Belgium).

## SECTION 1 :
## THE GENERAL IMPACT ON BANK ACTIVITY AND STRATEGY

### 1.1 FOUR CHANNELS OF IMPACT ON BANK ACTIVITY

The transition of full EMU and the introduction of the euro influence banking activity in many ways. They have been analysed in a vast literature and are discussed almost daily in meetings and seminars. They have stimulated the drafting and the implementation of "schémas de place" in several financial centres and of "Europrojects" in hundreds of financial institutions.

For the purpose of the present paper, which focuses on bank strategies, it will do to identify the main channels through which full EMU bears on bank activity and to list, in a not exhaustive way, the most significant effects channelled.

Channel 1 : The direct effects of introducing a single currency and a centralised monetary policy :

- crossing out, by one stroke, all forex transactions and/or interest arbitrage in national currencies within the euro-zone;
- blurring the distinction between domestic and cross-border payments within the euro-zone with its implications on clearing, transfer and settlement systems;
- shifting the attention of financial institutions from currency risk to market and credit risks;
- building a single yield curve for all financial institutions in the zone;
- introducing minimum reserve requirements in the countries of the euro-zone where they did not exist before. This reduces the attractiveness of previously off-shore financial centres within the euro-zone (Luxembourg) and increases the attractiveness of the financial centres outside the zone (London, Zürich) etc.

Channel 2 : The effects through changes in financial markets :

- reducing the number of markets e.g. merger of different types of exchanges, nationally and internationally;
- changing the absolute and/or relative size of the markets :
  * shrinking of the forex markets especially those which concentrated on national currencies of the euro-zone;
  * shrinking of those derivatives markets which previously concentrated on transactions in national currencies of the zone;
  * relative shrinking of government bond markets as a result of the implementation of the Maastricht criteria with respect to public finances;
- changing the activity of markets :
  * reduced segmentation of markets;
  * increased competition as a result of increased contestability of markets (easier entry and more participants);
  * new prospects for corporate debt : no longer crowding out of corporate by government debt, more liquidity;
  * new prospects of equity markets, less segmentation, more liquidity.

Channel 3 : Industry-specific effects :

- high transitional costs associated with conversion towards the euro, changes in IT programmes and procedures, information and training programmes;
- increased pressure to overcome overbanking and to cut costs;
- increased pressure of desintermediation and competition from non-banks;
- generalisation of concentration movement.

Channel 4 : Firm-specific effects :

- significant burden of transitional costs (cf. supra);
- increased pressure to rationalise networks and cut costs (cf. supra);

- challenge to reach higher minimum size in many banking “métiers” : increased pressure towards economies of scale and scope;
- challenge to face the diversification-specialisation dilemma in the enlarged markets of the euro-zone.

## 1.2 IMPACT ON BANK STRATEGIES : CONCEPTUAL FRAMEWORK

Since the beginning of the nineties, my colleagues and myself have been trying to build and constantly adjust a conceptual framework for analysing bank strategies (cf. references at the end of the present paper). This framework has been derived from a supply-oriented approach to bank strategy, according to which the strengths and weaknesses of an individual institution - not the demand or regulatory conditions - should be the starting point for designing and implementing its basic strategy.

In this context we identify two types of restructuring policies.

The accommodating type aims at (adapting) the micro-level of the banking firm to often unforeseen developments in the macro-level of the economy and/or in the meso-level of financial markets (Abraham and Lierman, 1990, p. 416). The standard example of such a strategy is a cost-cutting and internal rationalisation of the firm in order to overcome a drop in profitability induced by stiffer competition, domestically or internationally.
In the autonomous restructuring type on the other hand, the strategy is based on the existing resources of the bank and is explicitly oriented “towards maximising the comparative advantages of the bank and minimising its comparative disadvantages in the financial markets”. It focuses on organic growth of the bank and/or external growth by mergers and acquisitions or cooperative arrangements.

The standard example of organic growth is “the stand alone” policy of many medium-sized banks which enjoy a reputation of solid and efficient management, excellent external relations with clients and authorities and a favourable internal social climate. In such a strategy, growth is regular, but slow. Relations banking is still important in the so-called local, regional or national customers’ markets, but transactions banking is practised in the globalised professional markets. Revenue from intermediation remains important, although declining in relative terms.

The standard example of external growth is provided by the emergence of mega-banks, through wordwide mergers and acquisitions. Such a strategy of “the biggest is the best”, or in pejorative terms “the fattest is the fittest”, is based on market power, globalised asset management and extensive worldwide corporate relations. Activities are concentrated on wholesale professional, not on retail markets. Fee business and capital gains are the main sources of income.

The empirical evidence on the economic gains of bank mergers remains mixed : “… While there are some real gains in bank mergers, they appear to take place in mergers between small banks. This raises the question what motivates the megamergers in the banking industry. Evidence on the real economic gains produced by such mergers is quite inconclusive” (Amihud and Miller, 1998, p. xi, mainly on the basis of the American experience).

## 1.3 IMPACT ON BANK STRATEGIES : THE EURO CASE

How can such a conceptual framework be applied to the transition to full EMU and to the introduction of the euro ?

Obviously, full EMU and euro are developments at the macro-level. But they were not unforeseen. They started with the Maastricht treaties in 1991-1992. They were dramatically interrupted by the currency crises in 1992-1993, but again put on the (right) political track afterwards. Historians will have to give credit to most banks in Continental Europe - not in the Anglo-Saxon world - that they have constantly supported the move to full EMU in spite of high transitional costs, in spite of vanishing forex income, in spite of the many difficulties and growing pains which will presumably occur in the launching period of the euro. Those banks should rightly claim - in the banking tradition of "high risk, high return" that the future gains (when ?) from the project should be reserved, at least partly, to those who took the risk of the operation and not to those who stood by the side of the road, ready to ridicule those "naïve

It would seem that in this context a good deal of the bank strategies, at present, are of the accommodating type, adjusting, both at the industry and at the firm level, to more intense competition in a world of increased accessibility and contestability. In this context the cost-cutting objective stands high on the agenda. But this is not new. Cost-cutting has been a "favourite" of banking strategies in Europe since the beginning of the nineties. Until recently, the performance was far from conclusive in several countries. The ERE (1997) reports that no overall improvement of cost-to-income ratios had been perceived (p. 87). The striking and paradoxical aspect of the cost-cutting drive in the nineties has been that, until very recently, the rationalisation measures did not lead to a significant reduction of the branch networks. In Italy, they have even been extended after the removal of restrictions on the geographic expansion of some credit institutions. On the contrary, central overheads have been cut almost everywhere (Abraham, 1997 a, p. 363).

The reasons for this relative "no-change" situation are well-known. First, the impact of cost-cutting devices on net profitability has been neutralised by "market share" strategies aiming at strengthening the domestic base of the bank. In this context each local bank manager claims that closing his branch will direct his customers to a competing bank and reduce the market share of his own institution. Secondly, branch networks are very labour-intensive. Closing branches at a (very) fast rate immediately creates the threat of a "bain de sang social". The prevailing philosophy in Euroland - which I share - is that the reduction of networks should be gradual and spread over time. It should be realised by favouring voluntary departures, not by firing people.

This approach is now being challenged in the Anglo-Saxon world. Striking here is the fact that cost-cutting is no longer considered as the accommodating device of an individual bank, but has become the dominant objective of mega-mergers. In Europe, the same trend can be seen in cases such as the merger of UBS and SBC in Switzerland (October 1997). Dropping 13,000 jobs has been advertised as the main objective and the main benefit to be expected from this mega-move.

In the context of the present discussion, it is to be feared that the transition to full EMU and the introduction of the euro will be used as a pretext, an excuse, an alibi, for doing "catastrophically" what should already have started as a regular accommodating device of a bank whose profitability is unsatisfactory. At the macro-level the Maastricht convergence criteria and "Europe" in general, have already been used as scapegoats for budgetary hardships, monetary restrictions and rising unemployment in Europe. Many (though not all) of the measures taken would have been necessary, also without monetary integration. It was, of course, easy to hide one's own shortcomings under the European veil. This should not be repeated in financial restructurings in the euro-zone.

Coming now to the topic of autonomous restructuring policies, two distinct but not unrelated moves seem to be highly relevant. In both of them the transition to Euroland is at work, but exerts its influence in conjunction with broader forces.

The first one is the sometimes frantic effort to check the impact of falling intermediation margins by other sources of income : fees and capital gains. This is a wordwide phenomenon which partly reflects the basic trend in Western financial systems to move from a B (banking) system to an M (market) system. However, as I argued elsewhere (Abraham, 1997 b, p. 62) the transition to an M system will "neither be general, nor automatic, nor irreversible". How does the transition to full EMU fit into this picture ?

It is highly improbable that the transition to full EMU will reverse this trend. In the process of convergence within Euroland, the higher margins in some, mostly Southern European countries, will probably adjust to the lower ones prevailing in N.W. Europe. Moreover, if the euro, as we expect it to do, acts as a catalyst for more aggressive policies beyond the traditional national domestic base, the increased competition will normally exert pressure on the margins. This explains the efforts to increase other sources of income by moves as bancassurance, asset management, involvement in primary and secondary equity markets.

However, one major qualification should be added to this too simple textbook analysis. I continue to share the J. Dermine's (1995) opinion that, in the customers' markets, banking with a "single currency" does not mean banking in a uniform market, which would indiscriminately cover the whole euro-zone. There will remain ample room for customer-linked, geographically, culturally and linguistically determined banking. But this kind of domestic bases will no longer be determined by national borders only. Between these regional markets some differentiation in interest rates and margins remains possible.

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A second important change in autonomous restructuring concerns the balance between organic internal and external growth, mostly through mergers and acquisitions. It is striking that in the last few years the balance has shifted significantly towards external growth.

In its two listings of the major European M and A since mid-1997, the European Banker (1998) distinguishes three main motives, the first two ones being predominant : consolidation (leading to cost-cutting, economies of scale and scope and other size effects), globalisation (wordwide) and diversification (e.g. bancassurance).

In an interesting analysis in Revue Banque (1998), Gaël de Pontbriand quotes four objective moving forces for European M and A : overbanking, size-effects, economies of scale and scope, pressure of shareholders for better short-term financial performance. But he adds subjective herding effects (effet de troupeau). More than sixty years ago, Keynes (1936) wrote that the financial world is driven by "animal spirits". In that world people prefer to fail conventionally, as members of the group, of the herd, rather than succeeding unconventionally , as lonely trouble-makers.

However, as stressed in the survey of the present herding literature by Devenow and Welch (1996) not all herding phenomena can be reduced to mere emotional, psychological reactions. "Rational" herding occurs when it creates payoff externalities, e.g. when following the herd makes for more depth and liquidity in financial markets; or, as suggested by some principal-agent models and by mere observation in daily asset management, when managerial performance evaluation is based not on absolute, but on relative performance (perform better than the industry benchmark .. belong to the top five …). Finally, "rational" herding also exists in conditions of informational externalities when "*agents gain useful information from observing previous agents' decision to the point where they optimally and rationally completely ignore their own private information*" (ibidem, p. 609). This may explain *the decisions of firms to merge with others and the form by which such mergers are accomplished (conglomeration, hostile takeovers, tender offers, etc.*" (ibidem p. 610). Whether this is "rational" or merely an expression of "animal spirits" is, in my opinion, often unclear.

This type of analysis inevitably raises the question whether the present "euroforia" and the concomitant wave of M and A in European banking is based on "rational herding" or, on the contrary, leads to inconsiderate restructurings and increased concentration, determined by megalomania and mere emotional actions and reactions rather than by objective factors. Recent M and A in- and outside the eurozone have not been homogeneous and uniform, which excludes a straightforward and standard answer to the euroforia question. The most significant cases differ from one another by their motivation, the business lines concerned and/or their geographical dimension (for these distinction, see Heremans and Van Cayseele, 1998). Most operations are motivated by the need to strengthen the bank's market position and/or by rationalisation and cost-cutting through economies of scale or scope. In this respect, the standard answer to the euroforia question is that the impact of the euro through the various channels mentioned above increases the minimum size required for many categories of financial transactions, especially on the capital markets. Organic growth is too slow to reach that higher minimum size in due time to face the new challenge of Euroland. External growth is necessary, first of all through horizontal (in the same business line) M and A. This argument makes sense in general. However it is to be tested case by case, especially when a bank tries to overcome the size-constraint by specialising is some **métiers** or by **niche playing** in market segments (e.g. private banking) where attractive **niches** have not (yet) become **dirty stables** with many competitors.

When rationalisation and cost reductioin are the main motives, the scope of direct cost-cutting is much more limited in "diversification" mergers, where complementary activities, business lines and institutions are merged, than in horizontal mergers, where the same line of activities are consolidated. In the latter case, the degree and the speed at which cost reduction becomes effective and significant depends essentially on the way in which IT platforms can be harmonised and unified and on the conditions under which personnel can be reduced on socially acceptable terms.

Finally, as to the geographical dimension, the euro obviously eliminates an important factor of market segmentation on a national basis. But the other factors, like geographical, cultural and linguistic "distance", differences in various national and regional regulations etc. remain. Their impact is undermined, but not destroyed by the transparency of a single currency. To overcome these obstacles and to penetrate foreign domestic markets, organic growth is often inadequate in Euroland. This paved the way for acquisitions of foreign networks and institutions, in a shift to more aggressive autonomous restructuring.

In my opinion, although M and A on a national basis still remain predominant for huge operations, this is one of the ways in which the transition to full EMU induces cross-border M and A and exerts a distinct influence on autonomous restructuring, alongside the pure size effect. In conclusion, the present wave of M and A in Euroland can be explained by some elements of "rational" herding, the relevance of which varies widely among several recent cases.

# SECTION 2 :
# EUROLAND IN THE BENELUX AREA

## 2.1 INTRODUCTION : THREE DIFFERENT FINANCIAL SYSTEMS : ONE AREA ?

When dealing with the transition to full EMS in the Benelux area, one has to deal with three financial systems which at first sight do not have much more in common than geographical proximity, small domestic markets and some remainders of the Belgian Luxembourg Union of 1922. Key data on the three countries are presented in Table 1.

The differences are numerous :

(i) Belgium and the Netherlands have traditional on-shore financial markets. Although moving slowly to an on-shore status, under full EMU regime, Luxembourg has an off-shore past, attracting the Belgian dentist wanting to escape the Belgian withholding tax and German banks wanting to circumvent the German minimum reserve requirements.

(ii) The three financial systems have been internationalised, be it, at least initially, in a different way (Abraham, Bervaes, Guinotte, 1994) : Belgium by an open-door policy towards foreign banks, the Netherlands mainly through internationalisation of the domestic banks, Luxembourg by attracting foreign banks through the opportunities of off-shore banking.

(iii) The systems of corporate governance of financial institutions are widely different. The Dutch system is of the Anglo-Saxon type with, at least in the top banks, widely dispersed shareholdership and extensive power of managers. Moreover - in contrast with the Anglo-Saxon example - the bank and its managers are protected from hostile take-over bids and analogous devices by extensive private arrangements ("besloten vennootschap", administratiekantoren, etc.).
In Belgium, the Latin holding culture is still alive, the bank and its management depending on a limited number of reference shareholders (Renneboog, 1997). This dependence is qualified but not suppressed by the restrictions imposed on the shareholders by authorities through the "protocol on the autonomy of the banking

Finally, most Luxembourg banks being subsidiaries or branches of important foreign banks, managers are very much dependent on the mother corporation or the head-office of their group.

(iv) The three countries are overbanked, but not in the same way and with the same pressure on profitability. The pressure on profitability seems to be highest in Belgium, because it is due to a very high ratio of branches (747 in 1996) per 1,000,000 inhabitants. However, the impact of the overbranching is mitigated by the small number of employees per branch (on average 3,5 !) (see table 1).
In Luxembourg overbanking is profitable because it refers to the number of banks, not of branches. They nearly all depend on banks abroad and have their own customers.
In the Netherlands, the process of consolidation of banks and branches (see table 1) began earlier than elsewhere. The effect was not primarily a drastic reduction of the number of credit institutions (172 against 134 in Belgium and … 214 in Luxembourg) but a concentration of more than 75 % of the assets in the five largest banks, of which 3 are top international players (see table 1).

(v) In spite of the differences in the number of banks, a few big banks - ABN-AMRO and Rabo in the Netherlands, the "Seven Sisters", now reduced to five in Belgium - are predominant on the domestic market (70 to 80 % of customers' markets). Both countries have had to face the issue of big banks in small countries. Their expansion abroad has been oriented differently, mostly in a radius of 400 km around Brussels and in a few international financial centers for Belgian banks; worldwide for ABN-AMRO.

Except for the three top Dutch banks, all “elephants” in their respective home markets are medium-sized at the European level and minor players at the world level.

When taking in account all the differences just mentioned, the question inevitably arises whether the problems of transition to full EMU have to be dealt with, separately for each system or globally for the whole Benelux area.

The view which I will develop is that under the pressure of banking with a single currency, a set of specific problems emerge for the area as a whole.

Dutch top banks are focusing on Belgium as their second or common domestic market or as the centre of their European operations; with much hesitation Belgian banks are giving up their “stand alone” policy; as already mentioned, Luxembourg is slowly moving to an on-shore status where geographical proximity and shareholders relations are driving forces for full integration in the Benelux area. However, as will be shown in the case study on the Belgian Generale Bank, this development meets with institutional resistance, which slows down the pace and the regularity of this move towards convergence.

# TABLE 1 - KEY FIGURES BENELUX COUNTRIES (a)

| | Netherlands | Belgium | Luxembourg | Date-Source |
|---|---|---|---|---|
| ***Macro-economic figures*** | | | | |
| 1.Population (mio) | 15,57 | 10,17 | 0,416 | 1997-Eurostat-STATEC |
| 2.GDP (mia ECU) | 318,3 | 213,7 | 14,5 | 1997-Eurostat-STATEC |
| 3.GDP as % of GDP-Euro 11 | 5,70 % | 3,90 % | 0,30 % | 1997-EMI-STATEC |
| 4.GDP per inhabitant (ECU) | 20.392 | 20.998 | 34.222 | 1997-Eurostat |
| 5.Unemployment rate | 4,0 % | 8,8 % | 3,4 % | June 98-Eurostat-BCL |
| 6.Inflation rate | 1,4 % | 0,7 % | 0,4 % | Dec. 98 y/y - Eurostat |
| 7.General Government Deficit (% of GDP) | - 1,4 | - 2,1 | +1,0 | 1997-Eurostat-EMI |
| 8.General Government Gross Debt (% of GDP) | 72,1 | 122,2 | 7,1 | 1997-Eurostat-EMI |
| 9.Exchange rate (1 ECU = …) | 2,23 | 40,72 | 40,72 | Q2 98-<br>Datastream |
| 10.Short term interest rate - 3 months | 3,57 | 3,71 | - | Q2 98-<br>Datastream |
| 11.Long term interest rate - Benchmark 10 Y | 4,93 | 5,027 | 5 % | Q2 98-<br>Datastream |
| ***Banking*** | | | | |
| 12.Number of credit institutions | 172 | 134 | 214 | 1997-<br>ABB Vademecum-BCL |
| 13.Number of foreign banks | 62 | 73 | 207 | 1977-<br>ABB Vademecum |
| 14.Number of branches per 1 mio inhabitants | 284 | 747 | 214 (b) | 1996-NBB |
| 15.Number of bank employees per 1 mio inhabitants | 7.250 | 7.500 | 21.752 (c) | 1996-NBB |
| 16.% of government debt held by banks | 28 % | 61 % | 41 % | 1996-NBB |
| 17.Concentration ratio :<br>C3 in % of total balance | 67,5 | 35,3 | | 1996-NBB |
| 18.Concentration ratio :<br>C5 in % of total balance | 76,2 | 53,1 | | 1996-NBB |
| 19.Bank employment | | 76.939 | 21.752 | |
| 20.Total assets (mia ECU) | 635 | 684 | | 1996-NBB |
| 21.Total assets (% BBP) | 256 | 326 | | 1996-NBB |
| 22.Gross foreign assets/Total assets | 33,3 | 46,2 | 96,5 | 1996-NBB |
| 23.ROE | 14,6 % | 13,3 % | 15 % | 95/96-ABB-BCL |
| 24.ROA | 0,50 % | 0,31 % | 0,40 % | 95/96-ABB |
| 25.Risk assets ratio | 11,1 | 11,3 | 12,4 | 1996-ABB |
| 26.Number of banks in top 50 (Tier 1 capital) | 3 | 0 | 0 | 1997-The Banker |
| 100 | 3 | 2 | 0 | |
| 200 | 5 | 7 | 0 | |
| 300 | 5 | 7 | 0 | |
| 27.Number of banks in top 50 (Total assets) | 3 | 1 | 0 | 1997-The Banker |
| 100 | 3 | 4 | 0 | |
| 200 | 5 | 7 | 0 | |
| 300 | 5 | 7 | 4 | |
| ***Insurance*** | | | | |
| 28.Number of insurance companies | 491 | 255 | 81 | 1995-CDV |
| 29.Number of employees per company | 81 | 100 | 17 | 1995-CDV |
| 30.Premiums per employee (ECU) | 685.169 | 446.837 | 585.736 | 1995-BVV0 |
| 31.Premiums per inhabitant (B=100) | 157 | 100 | 356 | 1994-CEA |
| 32.Insurance level (Premium per inhabitant/<br>GDP per inhabitant (B=100) | 148 | 100 | 282 | 1994-CEA |
| ***Stock Exchange*** | | | | |
| 33.Number of quoted national companies | 185 | 143 | | 1996-NBB |
| 34.Market capitalisation (mia ECU) | 518,8 | 162,7 | 30,5 | May98-FESE |
| 35.Stock value of quoted national companies<br>(% of GDP) | 162 % | 76 % | 219 % | Own calculations |

Notes : (a) Information provided by the Research Department of Artesia Bank, Brussels and the Ministry of Finance, Luxembourg.
(b) Number of branches per 416.000 inhabitants.
(c) Number of bank employees per 416.000 inhabitants.

Abbreviations : ABB : Association Belge des Banques; NBB : National Bank of Belgium; CDV :Controle Dienst der Verzekeringen; BCL : Banque Centrale de Luxembourg; EMI : European Monetary Institute; CEA : Comité Européen des Assurances; FESE : Federation of European Stock Exchanges.

## 2.2 THE IMPACT OF EUROLAND : A GLOBAL OVERVIEW

The sensitivity to the banking aspects of full EMU, to banking with a single currency, developed much earlier in Belgium than in the Netherlands. Several factors were at work. The political commitment to a full EMU, including the single currency, has always been stronger. In the financial sector some Belgian banks - Kredietbank, Generale Bank - have played a leading role in promoting the ecu, the forerunner of the euro. Ecu transactions and ecu clearing have been developed as profitable "niche playing".

In this context, when full EMS came in for discussion, the consensus was reached rapidly that banking with a single currency was the future. The new opportunities provided by Euroland would compensate for the transitional costs and for the loss of forex income from intra-zone currency transactions. A cooperative effort of authorities and the private sector was launched to set up and to implement "un schéma de place" for the Brussels financial centre.

In the Netherlands, traditional pragmatism, a wordwide rather than a continental European outlook, and Anglo-Saxon influence led for a good deal of Euroscepticism in the financial community, at least with respect to the single currency aspect of full EMU. The "conversion" came later, but was effective.

Finally, in Luxembourg much attention went out towards establishing a credible Luxembourg central banking component in the European System of Central Banks (ESCB) and towards the implications of full EMU for fiscal harmonisation. It was (rightly) felt that when the veil of different national currencies would be lifted by the single currency, tax discrimination and privileges would be questioned even more, because "Le roi fiscal sera tout nu" !.

If Dutch banks were slow in recognising the impact of the introduction of a single currency, they were by far the first to initiate autonomous restructuring by consolidation, diversification and foreign acquisitions. They were among the first in Europe to succeed, in the early nineties, in merging the numbers one and two of their banks into the ABN-AMRO, in this way creating a global player at the world level. The strength of their institutional investors - insurance companies and pension funds - was transformed into bancassurance conglomerates like FORTIS and ING. The outcome is that, although the Dutch banks were slow to believe in the single currency, they are now the best prepared banks to meet the structural requirements of full EMU.

Their process of domestic consolidation has now practically been concluded, at least at the top. Four groups are now starring in the Dutch show :

- ABN-AMRO (primarily banking)
- The FORTIS GROUP which now comprises FORTIS NL, its insurance pivot and FORTIS B, its banking pivot
- ING, grouping NMB (banking), POSTBANK (banking), NATIONALE NEDERLANDEN (insurance)
- RABOBANK, which has absorbed ROBECO, a very important fund manager but did not succeed to merge with ACHMEA, one of the top Dutch insurers.

Meanwhile, important means have been accumulated for a worldwide expansion through mergers and acquisitions. In the first part of the nineties, Dutch banks (together with the Spanish banks) were already the record buyers in M and A operations abroad.

The transition to full EMU has refocused their attention to European markets (Van der Linden, 1998). Belgium has been targeted in the first place as a second or common domestic market (ING and ABN-AMRO), as a springboard to France and Southern Europe (ING) and even as the centre of their European activities (ABN-AMRO). In the second place FORTIS-AMEV has engaged in a partnership with AG-24 in Belgium in order to build a Dutch-Belgian Group of bancassurance. Thirdly, attempts, not very successful up to now, have been made to penetrate into Southern Europe in a significant and direct way (ABN-AMRO has failed to acquire CIC in the context of French privatisations, but is a significant player on the Italian scene).

In contrast with the Dutch experience, the Belgian record of autonomous restructuring through domestic consolidation and external growth has been chiefly disappointing, until recently.
Up to early 1997 autonomous restructuring was limited to :

- the absorption of small institutions, often savings banks, by larger ones. Typical examples of such transactions are the absorption of the savings banks EURAL and UNISPAR by PARIBAS BANK BELGIUM and the absorption of the BANK VAN ROESELARE and the savings bank SPAARKREDIET by KREDIETBANK (number 3 on the banking list). More important was the acquisition of the CREDIT LYONNAIS NEDERLAND by the GENERALE BANK;
- the setting-up of partnerships and joint ventures, partly in the context of privatisation of public credit institutions;
- BANQUE DE LA POSTE, through a 50-50 % stake of the POST OFFICE and the GENERALE BANK;
- DEXIA, associating CREDIT COMMUNAL DE BELGIQUE et CREDIT LOCAL DE FRANCE through a stake of 50 % in each other's operating units;
- most of all, FORTIS AG acquiring CGER and SNCI in the context of privatisation and setting up a Dutch-Belgian conglomerate of bancassurance with FORTIS-AMEV.

Apart from those cases, only an impressive list of failures can be mentioned :

- the failure to merge AMRO and GENERALE BANK in 1990;
- the failure to integrate BBL into ING in 1992;
- the failure to set up "the" big Belgian Bank through the merger of GENERALE BANK (n°

These failures are due to conflicting interests between shareholders, to conflicts between the "stand alone" approach of the management and the plans of major shareholders to disengage themselves, and finally to personal rivalries among some of the main actors. Observers have identified these failures as the decline and even the end of "Belgian capitalism" based on holding culture, political pressures and vested interests.

Since early 1997, however, four big cases have radically changed the Belgian scene. We list them in their chronological order, which happens to be their order of increasing importance :

- Spring 1997 : acquisition of a majority stake in the highly profitable PARIBAS BANK BELGIUM by the ARCO-BACOB BANK (n° 7) GROUP, the financial institution of the Christian Social Movement in Belgium. This transaction illustrates the retreat of French banking groups (PARIBAS, to be followed by SUEZ-LYONNAISE DES EAUX in the GENERALE BANK case) from the Belgian scene;
- November 1997 : acquisition of BBL (n° 2) by ING; up to now, this transaction seems to head for success. ING respects the specificity of BBL in Belgium and integrates BBL-people as full partners in its organisation. The latter are happy to be members of a worldwide international credit institution.
- February 1998 : merger between KB (n° 3), CERA (n° 6), ALMANIJ (holding) and ABB (insurance).
  This is a highly impressive project since it realises an integration at four levels :

* at the bank level, as a rationalisation project of two branch networks without a significant loss of customers and in a favourable social climate;
* at the level of bancassurance, because it promotes a formula of integrated financial services;
* at the level of holdings, by integrating ALMANIJ and ABB, not only as controlling entities but hopefully also as providers of risk capital and equity;
* at the international level, where the new conglomerate may become a significant player via partnership with RABO BANK;

– Spring 1998 : the struggle between the FORTIS Group and ABN-AMRO to control the GENERALE BANK (n° 1). Ultimately, the battle was won by Fortis in June-July. This illustrates the many contradictions of Belgian capitalism, but it also initiates a new era on the Dutch scene, because the implicit "non-aggression" pact among the leading Dutch financial groups has been violated.

Following the worldwide pattern in merger activity in the wake of the mid-summer financial crisis, operations in the Benelux area subsided somewhat in the second semester of 1998.

Notable exceptions were :
– the take-over of the ANHYP Bank by the insurance group AXA through its subsidiary ROYALE BELGE and the planned merger of ANHYP with IPPA Bank within the AXA Group;
– the acquisition of very active CREDIT LYONNAIS BELGIUM by DEUTSCHE BANK. This ends the apparent neglect of the Benelux area by leading German banks. The previous CL Belgium will operate under the name Deutsche Bank. Its aggressive marketing is already being felt by competitors.

For evident reasons, Luxembourg banks do not play a significant role in these developments. But they undergo the outcome and the consequences of the operations in their respective groups. Each merger or acquisition at the level of the mother company or the head office has its repercussions on the subsidiaries and branches in Luxembourg. In this way, the Luxembourg scene is a "derivative" of those in the neighbouring countries.

The transition to full EMU, the prospect of banking with a single currency is obviously not the only determinant of the many kinds of restructuring which we are trying to analyse. But it acts as a catalyst of underlying forces of consolidation and diversification, which were already at work in the Netherlands at the beginning of the present decade but which exploded only recently in Belgium. In this way bank strategies in the Benelux area tend to converge.

## 2.3 **CASE STUDY I : THE ABN-AMRO CASE** (THE NETHERLANDS)

### 2.31 INTRODUCING THE TWO CASE STUDIES

In the following paragraphs we focus on the two N° 1's in the Benelux area : ABN-AMRO in the Netherlands, the Generale Bank in Belgium. They have - at least partly - a common origin and a common "Founding Father", King William I, who ruled the United Kingdom of the Netherlands from 1815 until 1830. His kingdom amalgamated Dutch and Belgian provinces (Van der Wee and Verbreyt, 1997). As "<u>the last enlightened despot and the first champion of the modern industrial society in the Low Countries</u>" (ibidem, p. 14), he forced, in the 1820's, the foundation of :

– De Nederlandse Handelsmaatschappij (The Netherlands Trading Society), which was at the origin of the later ABN;
– De Generale Maatschappij (the later Belgian Société Générale), which was at the origin of the Generale Bank;

– De Nederlandsche Bank, which was to become the Dutch central bank.

The two case studies have the same structure : historical background - present profile and strategy - recent moves. The key statistical and accounting data are presented in separate tables.

## 2.32 ABN-AMRO'S HISTORICAL BACKGROUND

As emphasised by De Leeuw (1996), ABN-AMRO is a "continuous process of mergers and acquisitions", which are spread over more than 300 years. After World War II, the main events were :

– in 1964, the merger of the Nederlandsche Handelsmaatschappij (1824) with the Twentsche Bank (1861) to constitute the Algemene Bank Nederland (ABN);
– also in 1964, the merger of the Amsterdamsche bank (1871) and the Rotterdamsche Bank (1863) to constitute the AMRO-Bank;
– in 1991, the merger between the ABN-Bank and the AMRO-Bank to constitute the ABN-AMRO Bank.

The ABN-component had developed an extensive international activity and an international network. The AMRO-component had a more domestic focus. On the occasion just mentioned, the private banking institutions of ABN (Mees and Hope) and AMRO (Pierson) were merged in MeesPierson, but sold to the Fortis-Group in 1996.

This short survey illustrates the strong focus on external growth in the Dutch banking tradition.

In my opinion, this can be explained, at least partly, by the corporate governance system in the Netherlands. The shareholdership of the bank is often dispersed and has a limited impact on the managers. In M and A operations, managers have much decision power and act quite independently, in a rather pragmatic way to adjust the structure of their banking firms to new domestic and international conditions.

## 2.33 ABN-AMRO's PRESENT PROFILE AND STRATEGY

As emphasised in the KALFF Interview (Euromoney, 1997), the merger of 1991 - which occurred after the unsuccessful attempt to merge AMRO and Generale Bank in a Benelux cross-border operation - was a "marriage of necessity". The driving forces were to increase local market share and to build on the combined commercial and financial strengths in order to grow internationally. The dominant idea was that the growth potential of Dutch banks was rather limited on the mature domestic market and that it had to be found outside the Netherlands (Nawas, 1996). So, the combined number of branches in the Netherlands has been gradually reduced form about 1.400 at the beginning of the decade to 967 by the end of 1997 (see table 2A).

TABLE 2 - DATA ON ABN-AMRO

2A KEY FIGURES 1997

| | | UNITS | Bn NLG | Bn ECU | % |
|---|---|---|---|---|---|
| 1. | EMPLOYMENT | | | | |
| | worldwide | 76.749 | | | |
| | of which : Netherlands | 34.071 | | | |
| 2. | BRANCHES AND OFFICES | | | | |
| | wordwide | 1.888 | | | |
| | of which : Netherlands | 967 | | | |
| 3. | NUMBER OF COUNTRIES WHERE PRESENT | 71 | | | |
| 4. | EQUITY | | | | |
| | group | | 53,0 | 23,8 | |
| | bank | | 25,8 | 11,6 | |
| 5. | TOTAL ASSETS | | 836,4 | 375,4 | |
| 6. | CUSTOMER DEPOSITS | | 396,7 | 178,1 | |
| 7. | OPERATING PROFIT (before tax) | | 5,79 | 2,60 | |
| 8. | NET PROFIT (after tax) | | | | |
| | total | | 3,85 | 1,73 | |
| | to shareholders | | 3,67 | 1,65 | |
| 9. | RATIOS | | | | |
| | ROE | | | | 15,7 |
| | cost/income | | | | 69,1 |
| | risk asset | | | | |
| | total | | | | 11,36 |
| | tier I | | | | 6,96 |
| | non performaning loans/total private sector loans | | | | 1,59 |
| | amounts written off/private sector loans | | | | 0,28 |
| 10. | CREDIT RATINGS FITCH-IBCA | | | | |
| | short term | | | | A1+ |
| | long term | | | | AA+ |

Source : ABN-AMRO Report 1997.

2B RANKINGS OF THE BANKER : ABN-AMRO AND ITS COMPETITORS IN THE NETHERLANDS AT THE END OF 1997

| | N° world ranking | Strength | Size | Sound-ness | Profits | Performance | | | BIS |
|---|---|---|---|---|---|---|---|---|---|
| | Tier I capital | Tier I capital m $ | Total assets m $ | Capital/ Assets % | Pre-tax m $ | Profits on average capital % | ROA % | Cost/ Income % | Ratio % |
| 1. ABN-AMRO | 8 | 15.864 | 414.654 | 3,83 | 2.868 | 19,3 | 0,69 | 69,1 | 10,65 |
| 2. RABOBANK Nederland | 18 | 12.680 | 209.692 | 6,05 | 1.416 | 11,7 | 0,68 | 79,9 | 11,10 |
| 3. ING Bank Group | 35 | 8.730 | 190.269 | 4,59 | 1.278 | 15,5 | 0,67 | 74,0 | 10,77 |
| 4. BANK NEDERLANDSE GEMEENTEN | 187 | 1.751 | 58.971 | 2,97 | 168 | 9,9 | 0,29 | 19,4 | 28,00 |
| 5. FORTIS BANK Nederland | 189 | 1.738 | 38.680 | 4,49 | 267 | 17,4 | 0,69 | 75,3 | 10,80 |
| 6. SNS BANK Nederland | 350 | 815 | 17.094 | 4,77 | 97 | 13,3 | 0,57 | 73,7 | 14,30 |

Source : The Banker, July 1998.

Another important move was towards developing investment banking besides and in combination with commercial corporate banking. This started in 1992 by the acquisition of Hoaring Govett, a small investment bank subsidiary of the Bank of America in London, and was followed by the acquisition of other entities in Milan, Madrid, France and Scandinavia, but also by intensive internal growth (Kalff Interview, 1997).
Now, ABN-AMRO is a top international group, which ranks 8th on the World Ranking List of The Banker 1998 (see table 2B) and 4th on its Regional Ranking for Western Europe. Its soundness and performance indicators 1997 were quite remarkable for an expansionary institution (capital/assets ratio of 3,83, BIS risk/asset ratio : 10,65, profits/average capital : 19,3, ROE : 12,83, see table 2A and 2B). In 1998, ABN-AMRO has significantly felt the impact of the crisis in many emerging markets. Hence, its Moody’s rating has been recently reduced.

Its present profile can be summarised in two features :

- universal banking : doing everything in commercial and investment banking, market activities, private banking, wholesale and retail. However, ABN-AMRO wants to remain a bank and not to merge banking and insurance;
- worldwide banking : ABN-AMRO is present in 71 countries and in the main international financial centres. However, in commercial banking its two main markets are the Netherlands and the US, especially the Midwest. In investment banking ABN-AMRO is an “Amlo affair” : Amsterdam-London. Up to now, ABN-AMRO has no distinctive Euroland profile.

ABN-AMRO aims to belong to the top-5 universal banks worldwide by combining strong organic growth with selective acquisitions. In a number of countries it wants to develop all banking activities on the basis of a strong market position, which supposes that it should belong to the top 3 to 5 in that country. It concentrates trading and investment banking in four regional centres (Amsterdam/London, Chicago/New-York, Singapore and Hong Kong) but it also has more than 60 local trading rooms.

Finally - and this links up with the main theme of the present paper - ABN-AMRO wanted to play a leading role in the euro-zone. This ambition is justified. In the more unified markets of the euro-zone the size effect will be at work and will favour ABN-AMRO. As the 4th largest Western European Bank it will be able to play a significant role in the euro-payments system and to accept operations and risks on a European scale. It will also enjoy the so-called short list-effect, being chosen among a limited number of competing banks for the syndication of mega-loans and for large deals on the primary equity and bond market.

RECENT MOVES IN EUROLAND

Nevertheless, although the group is present in all the countries of the zone, that leading role is still wishful thinking. Its penetration into Germany is disappointing, and two recent important moves, one in France and one in Belgium (Generale Bank), have proved to be unsuccessful. Why ?

The attempt to take over the “Crédit Industriel et Commercial” in France in the context of the CIC’s privatisation raised the traditional suspicion of the French authorities concerning handing out a major French institution to a foreigner, even though this foreigner is a Euro-partner.

The failure to take over the Belgian Generale Bank is a much more complicated issue, which will be discussed into more detail in the next paragraphs.

At the moment, we limit ourselves to stating that this failure is much more surprising than the French one because ABN-AMRO’s offer :

– was made in a country with a tradition of open-door policy;
– was not a mere attempt to absorb a Belgian bank and its network. The proposal was to localise the management of all European commercial activities of the group - including those in the Netherlands themselves - at the Generale Bank in Brussels, which would become a new European division in ABN-AMRO’s organisation;
– was favoured by the management and the majority of the staff members at the Generale Bank, when it appeared that the traditional “stand alone” policy could no longer be maintained. Under these circumstances, management and staff members preferred to be integrated into a worldwide organisation with no overlapping network in Belgium;
– did not clash with the offer of an exclusively domestic Belgian competitor but with that of a Belgian-Dutch Group : Fortis. This broke up the consensus model on which Dutch banking was established;
– was financially attractive : it provided not only for exchange of shares, but also for additional cash.

## 2.34 CONCLUDING THE ABN-AMRO STUDY

The ABN-AMRO case shows that a bank can develop into a worldwide organisation, even if it has to start from a small and slowly growing domestic base. But this requires
(i) supplementing organic growth by continuous external acquisitions
(ii) strong management.

ABN-AMRO’s worldwide expansion did not, until very recently, focus primarily on the euro-zone. Its top management probably shared the Dutch initial scepticism about the introduction of the euro. When Euroland became a prospective reality rather than a vague dream, the Group tried to integrate the euro-approach into its worldwide strategy. Logical steps in view of that aim were to penetrate much more into the two key countries of the euro-zone : Germany and France, and to enlarge the domestic base to include Belgium.

But the Group handled at least the Belgian case in a rather undiplomatic way, with some improvisation and a bit of arrogance, which aroused the suspicion by traditional Belgian circles of that “Anglo-Saxon cowboy style”. This sapped the credibility of an attractive approach which tended to :
(i) recognise the Benelux countries as a specific area inside the euro-zone;
(ii) to enlarge the domestic base of the ABN-AMRO Group

(iii) to set up a specific European division located on an Amsterdam/Brussels basis for managing commercial operations in the euro-zone as a whole.

Together with the impact of their involvement in emerging markets, the institutional resistance to this approach has recently mitigated the interest of the ABN-AMRO managers in enlarging their domestic base southwards in Europe.

## 2.4 **CASE STUDY II : THE GENERALE BANK CASE** (BELGIUM)

### 2.41 THE GENERALE BANK'S HISTORICAL BACKGROUND

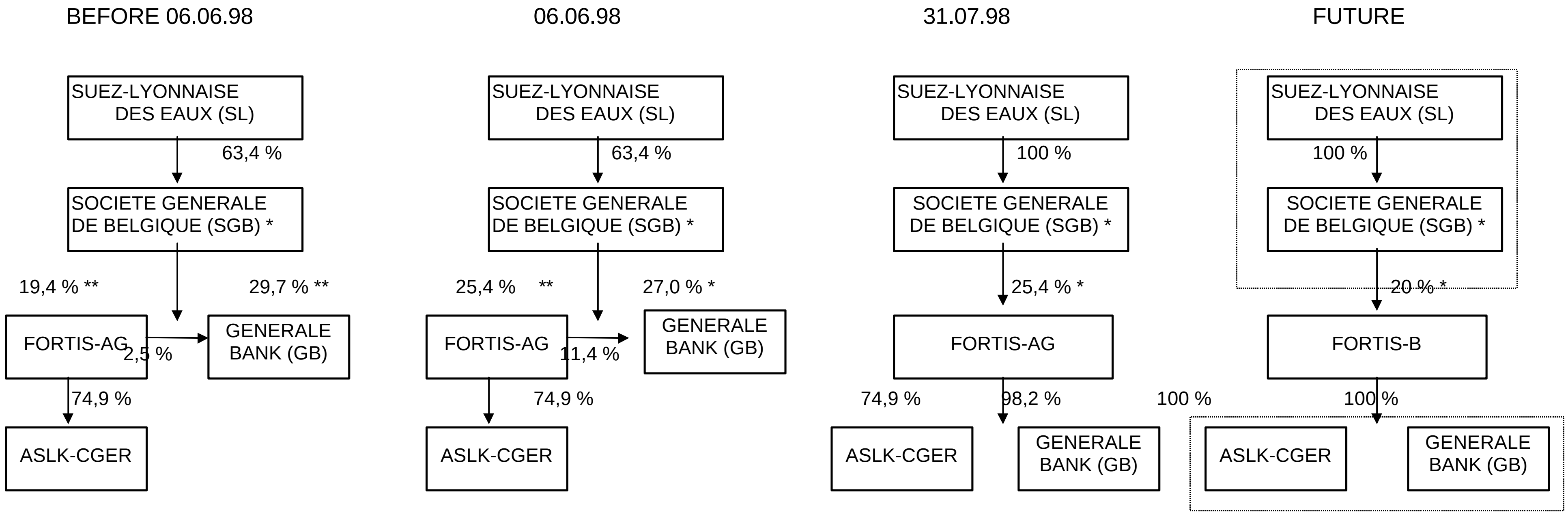
Twice in a decade, the destiny of Belgium's N° 1 bank was at stake. The first time was in 1988, when the de Benedetti "raid" on the Société Générale de Belgique (SGB) - the mother holding company of the bank - resulted in a transfer of control to the French Suez Group. A second crucial period was the first semester of 1998, when the Suez Group - after its merger with Lyonnaise des Eaux - decided to concentrate its interests on the public utilities sector and no longer considered its stake of 29,7 % in the Generale Bank (through SGB) as a strategic investment (see figure 2). As a consequence of the planned disinvestment by Suez, the Generale Bank became the battle field of two prospective buyers, the Dutch-Belgian Fortis Group and ABN-AMRO. The former had links with Suez and SGB, the latter had good connections with the Generale Bank's management.

This makes it likely that the history of the Generale Bank (GB) is not dominated, as ABN-AMRO is, by successive mergers and acquisitions under the pressure of markets and competitors. Very often, the driving factor was <u>the relation between the bank and its major "reference" shareholders</u>. This is typical of the Belgian holding culture, in which, after the Latin tradition, shareholdership is much more concentrated than in the Anglo-Saxon countries and the Netherlands.

For more than a century, from 1822 until 1934, the Société Générale, first Dutch, afterwards Belgian, did not experience that tension between shareholders and managers. It was a "<u>banque mixte</u>", which not only practised commercial banking but controlled the major part of Belgium's industry. The Great Depression of the 1930's put an end to this dubious "mix", and led to a split, imposed by the authorities, between commercial banking and controlling holding company activities.

The institutional implication of that split was the separation between a holding company - the <u>Société Générale de Belgique</u> - and the banking firm which, in 1965, went by the name of <u>Société Générale de Banque</u>, after a significant intra-group merger. In 1985, this was shortened to <u>Générale de Banque</u>, <u>Generale Bank</u>.

FIGURE 2- CHANGES IN THE HOLDING STRUCTURE OF GENERALE BANK 1998




Note : * SGB stands for Société Générale de Belgique and daughter companies
** including direct stakes of SL in Fortis and Generale Bank

Source : - Offre publique d'échange par Fortis AG
- Press Releases and Comments

At the beginning, the holding company was very powerful : "The bank emerged from the split in 1934 as the poor cousin of the group, with very slender resources and only a very limited degree of autonomy (Van der Wee and Verbreyt, 1997, Section 9.3, The Great Paradox).

But the situation changed over time. The holding company stagnated and, from the 1960's on, it had to bear the burden of the crisis in Belgium's traditional industries. The bank, on the contrary, prospered, it expanded nationally and internationally and became less dependent on the holding company. Its growth was mostly internal and organic, except for the important 1965 merger between the Generale Bank, the Banque d'Anvers and the Société Belge de Banque. All three had links with the Société Générale. In this way and to a certain degree, this merger can be considered as an intra-group operation.

The autonomy of the bank vis-à-vis its reference shareholders - in the first place vis-à-vis the SGB - was bolstered by the authorities. The Banking Commission promoted protocols on the "autonomy of the banking function" (1960, 1974, 1992).

This growing autonomy favoured a stand-alone policy which was only temporarily interrupted under the threat of the de Benedetti raid on the Société Générale (1988). In a defensive mood, merger negotiations were started with AMRO Bank. As soon as the threat decreased, the project was abandoned. What might have been the first important cross-border bankmerger in the European Union has never come true.

# TABLE 3 - DATA ON GENERALE BANK

## 3A KEY FIGURES 1997

| | | UNITS | Bn BEF | Bn ECU | % |
|---|---|---|---|---|---|
| 1. | EMPLOYMENT | | | | |
| | consolidated group | 27.200 | | | |
| | non consolidated | 14.932 | | | |
| 2. | BRANCHES AND OFFICES | | | | |
| | wordwide | 1.328 | | | |
| | Belgium | 1.064 | | | |
| 3. | NUMBER OF COUNTRIES WHERE PRESENT | 46 | | | |
| 4. | EQUITY | | | | |
| | consolidated | | 137 | 3,35 | |
| | non consolidated | | 103 | 2,53 | |
| 5. | TOTAL ASSETS | | | | |
| | consolidated | | 5.912 | 144,99 | |
| | non consolidated | | 4.077 | 99,96 | |
| 6. | CUSTOMER DEPOSITS AND CERTIFICATES | | | | |
| | consolidated | | 3.496 | 85,71 | |
| | non consolidated | | 2.119 | 51,96 | |
| 7. | OPERATING PROFIT BEFORE TAXES | | 29,9 | 0,73 | |
| 8. | NET PROFIT | | | | |
| | consolidated | | 17,1 | 0,42 | |
| | non consolidated | | 10,6 | 0,26 | |
| 9. | RATIOS (consolidated) | | | | |
| | ROA | | | | 0,30 |
| | ROE | | | | 12,83 |
| | cost/income | | | | 60,3 |
| | non performing loans/private sector loans | | | | 2,44 |
| | amounts written off/private sector loans | | | | |
| | risk asset total | | | | 0,28 |
| | tier I | | | | |
| | pay-out ratio | | | | 11,36 |
| | | | | | 6,01 |
| | | | | | 53,4 |
| 10. | CREDIT RATINGS FITCH-IBCA | | | | |
| | short term | | | | F1+ |
| | long term | | | | AA |
| | financial stability | | | | B |

Source : - Generale Bank, Annual Report 1997
- Prospectus offre publique d’échange par Fortis AG sur Générale de Banque.

## 3B RANKINGS OF THE BANKER 1998 : GENERALE BANK AND ITS COMPETITORS IN BELGIUM AT THE END OF 1997

| | N° world ranking | Strength | Size | Sound-ness | Profits | Performance | | | BIS |
|---|---|---|---|---|---|---|---|---|---|
| | Tier I capital | Tier I capital m $ | Total assets m $ | Capital/ Assets % | Pre-tax m $ | Profits on average capital % | ROA % | Cost/ Income % | Ratio % |
| 1. GENERALE BANK | 93 | 4.176 | 160.136 | 2,61 | 862 | 21,6 | 0,54 | 60,3 | 11,36 |
| 2. KREDIETBANK | 104 | 3.588 | 112.898 | 3,18 | 589 | 18,0 | 0,52 | 56,7 | 10,80 |
| 3. BBL | 126 | 2.877 | 111.970 | 2,57 | 528 | 19,8 | 0,47 | 69,1 | 11,26 |
| 4. ASLK-CGER (a) | 142 | 2.464 | 82.334 | 2,99 | 480 | 20,4 | 0,58 | 55,1 | 11,03 |
| 5. CERA (b) | 156 | 2.120 | 45.170 | 4,69 | 208 | 10,6 | 0,46 | 75,2 | 11,69 |
| 6. BACOB BANK | 184 | 1.770 | 71.347 | 2,48 | 192 | 13,7 | 0,27 | 62,0 | 12,19 |

(a) to be merged with Generale Bank in 1999 to become FORTIS BANK
(b) merged in 1998 with KREDIETBANK

## 3C DERIVED AGGREGATES (unconsolidated) AND RATIOS

| | N° world ranking | Strength | Size | Soundness | Profits |
|---|---|---|---|---|---|
| | Tier I capital | Tier I capital m $ | Total assets m $ | Capital/Assets % | Pre-tax m $ |
| 3C 1 | | | | | |
| 1. GENERALE BANK + ASLK-CGER | 51 | 6.640 | 242.470 | 2,74 | 1.342 |
| 2. KREDIETBANK + CERA (KBC) | 61 | 5.708 | 158.068 | 3,61 | 797 |
| 3C 2 | | | | | |
| GENERALE BANK | | | | | |
| as % of AMRO | | 26,3 | 38,6 | | 30,1 |
| GENERALE BANK + ASLK-CGER | | | | | |
| as % of AMRO | | 41,9 | 58,5 | | 46,8 |
| as % of KBC | | 116,3 | 153,4 | | 168,4 |

Source : The Banker, July 1998.

Meanwhile, the approaching prospect of the euro-zone increased the fear that, standing alone, even a national N° 1 of the size of the Generale Bank, would become a minor and less significant player on a European banking scene with a single currency.

This constituted the background to resume negotiations. The wish of Suez-Lyonnaise to liquidate its stake in the Generale Bank acted as a catalyst. Negotiations were re-initiated between SL, SGB and Fortis without immediate involvement of the managers and much hesitation on their part afterwards. The project was strongly supported by the Belgian political and financial establishment. Oddly enough, it was promoted as a big Belgian Bank "bis", while it is, in fact, part of the Benelux strategy of a Dutch-Belgian entity : Fortis. Finally, the management gave in on May 12$^{th}$ and endorsed the proposal of an exchange of shares : 7 Fortis AG against 3 Generale Bank. ANB-AMRO joined the competition too late, but with a more attractive proposal, including cash (cf. supra). This counterbid met with much criticism and resistance in traditional Belgian circles. But the Generale Bank management reversed its position and supported the ABN-AMRO bid. The Banking Commission accepted both bids for a procedure of public offering. Fortis finally won the battle even before the opening of the official public offering : on June 5$^{th}$ Fortis made a new bid, which topped the ABN-AMRO offer by about 6 %. At the same time, the Board of Generale Bank, led by the reference shareholders, officially considered the ABN-AMRO bid as hostile and issued a poison pill by increasing the bank's capital by 10 %, reserving the increase for SGB and its allies. One day later, ABN-AMRO withdrew from the race, utterly disgusted. The end of the story was standard :

- a public exchange of shares of SGB against SL shares (1/1) in June, which raised the stake in SGB up to the targeted 100 %
- a public exchange of shares + cash + guarantees on the basis of 7 Fortis against 3 GB in July, which, in two stages, raised the stake of Fortis in GB to 98,2 % (see figure 2).

The outcome of the battle has important implications for the structure and the working of financial markets in the Benelux-area :

- it forced the Fortis Group to re-examine and strengthen its internal structure. The various entities of the Group are redeployed around a banking pivot located in Belgium (Fortis-B) and an insurance pivot centered in the Netherlands (Fortis-N). The process of integrating the main components in one single entity, the "FORTIS BANK" will be spread over a period of five years;
- in the banking group, the planned merger between Generale Bank and ASLK-CGER, complemented by MeesPierson and VSB, creates an entity which will rank in the 50's in the World Ranking list of the Banker and be a significant player in the euro-zone. The present overlapping of the branch networks of the Generale Bank and ALSK-CGER - the last 25,1 % of its capital having been acquired at the end of 1998 - requires an intensive cost-cutting operation by closing at least 500 branches and crossing out at least 2.000 jobs. Cost-cutting is all the more required since it has to compensate for the high price that Fortis had to pay to acquire the control of the Generale Bank;
- the Generale Bank case raises many serious questions about the adequacy of the institutional structure and corresponding procedures in Belgium. In the private sector the future of SGB as 100 % daughter of SL and as intermediate holding of Suez-Lyonnaise Group in Belgium is uncertain. On the financial markets, some interventions have not been "marktconform" and quite a number of loopholes and uncertainties have been detected in the legislation and the procedures. The lack of transparency and the loopholes in the "rules of the game" have been sharply criticised not only by ABN-AMRO but also in the Dutch press and in the Dutch public opinion (the "Belgian coup");
- in the Netherlands, the rift between Fortis and ABN-AMRO has, at least temporarily, broken the implicit consensus among Dutch banks;
- in the whole Benelux area the banking atmosphere has become more aggressive as a consequence of the Generale Bank case.

### 2.43 CONCLUDING ON THE GENERALE BANK CASE-STUDY

The Generale Bank study leads to some paradoxical conclusions about the impact of the euro-project on banking strategy in the Benelux area. It confirms that the prospect of the euro-zone has induced a more aggressive approach in bank strategies. This mainly applies to the Dutch banks. But at the same time, it highlights the institutional resistance to cross-border M and A, primarily in Belgium. This resistance is a source of disappointment for worldwide-oriented banks like ABN-AMRO, which are now tempted to return to a lower profile in their European strategy.

The Generale Bank case also illustrates the problems which arise when strategic decisions are not based on a consensus between shareholders and management. This mainly applies to countries with a culture of reference shareholders. It is less relevant in cases where shareholdership is dispersed and managers have great decision power.

Finally, the Generale Bank case shows the limits even of a well designed and well managed stand-alone policy when a wave of M and A dramatically raises the size of your competitors and threatens to cross you of the list of significant players, even in a geographically limited area like the radius of 400 km around Brussels.

## GENERAL CONCLUSION

In conjunction with other forces like technological and globalisation, the transition to full EMU and to banking with a single currency induces a shift from defensive bank strategies to more aggressive ones.

This shift is reflected predominantly in the present wave of mergers and acquisitions either at the domestic or the cross-border level. External growth is considered as a condition for ultimate survival in many bank strategies. This changes the structure and the working of many financial markets and confirms our main thesis that the transition to full EMU will have more lasting effects than the SMP-project of the early Nineties.

The rationale behind the M and A is not only mere size, but also accelerated cost-cutting and penetration into foreign domestic customers' markets, which was previously hampered by defensive and ultimately self-defeating strategies of strengthening the national domestic base.

In the Benelux area, the penetration of Dutch banks into the Belgian domestic market is a striking example of this kind of strategy.

In my opinion, this does not lead, in customers' markets, to a uniform market in the euro-zone but to (supra)regional financial markets which are no longer determined by national borders and a national currency, but by geographic, cultural and linguistic proximity.

However, in the present process of consolidation, the factors of institutional resistance, even in small neighbouring countries, should not be underestimated.

As exemplified by the first 1999 bankmergers (BCH and Banco Santander in Spain, Société Générale and Paribas in France), it is therefore probable that in many countries of the euro-zone, important M and A will primarily remain domestic, at least in the next few years. At any rate, cross-border restructurings will increase only gradually, the Benelux area and Scandinavia being either exceptions, or testcases for the future. This should not be regretted in all aspects. It may, at least, prevent M and A based on pure megalomania and emotional herding effects. Ultimately, such operations lead to abuse of power and to operational inefficiency. This is not what we should expect from EMU and from that fantastic endeavour of countries which, half a century ago, had just finished fighting each other in a bitter way and are now going to share the same currency, not by domination, but by consensus and free decision.

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