Small Is Beautiful Around The World

by Steve Brown

Small is beautiful. This is the title of a collection of essays by the British economist EF Schumacher that was written in the midst of the energy crisis of the 1970's. The idea behind the essays was that through smaller, more personalized institutions, people were empowered and the result was better for the planet as well (we don't have to tell community bankers this idea is right on!). Since that time, however, globalization and business consolidation have created a proliferation of large enterprises in practically every industry. Yet, the minimalist ideals of Schumacher's message still matter to many people. Farmers' markets are in vogue, neighborhood cafes abound and small breweries are on the rise throughout the US. In cafes, huge portions are also no longer the norm, as frequently small platters are offered in an attempt to help conscious patrons win the battle of the bulge.

Consolidation has dominated the world of finance and perhaps even more so than in other industries. The financial behemoths JP Morgan Chase, Citicorp, Wells Fargo and Bank of America dominate the American landscape. But in the US, there are also more than 5,700 other banks under $2B. While the percentage of assets this group controls is dwarfed by the biggest banks, they still are a market force in almost every locale in the US.

Things are different though in other parts of the world. In Canada and Europe enormous financial entities occupy center stage even more than they do in the US. Canada's "Big 6" banks control a startling 90% of the total banking assets in that country. In addition to controlling almost all of the banking assets, these big banks swept up independent investment dealers and trust companies during the 1980's and 90's. With these vast managed assets and capabilities they have built wealth management divisions with global tentacles.

Banking in Europe has followed a similar trend. The five biggest banks in France control 86% of the monetary system there, and in England, the big four banks control 75% of the market.

When financial institutions are this big and control this much of a market, they gain many advantages. They can control product offerings and raise banking fees with impunity. While big banks have consolidated a great deal of control, they haven't completely eliminated their smaller counterparts. Personalized service and prudence have kept smaller institutions alive even in the consolidated markets in Europe.

In France, for example, three small family banks (BAMI, Pouyanne, and Martin Maurel) maintain very strong capital levels and almost entirely avoided the excesses and problems of the credit crisis. Their small business customers love them because they make decisions quickly and based on their familiarity with their dedicated customers. There is almost no employee turnover and with that solid knowledge and dedicated customer base, these banks have thrived.

Many small and medium-sized businesses in Canada likewise prefer local financial establishments. According to a recent Canadian Federation of Independent Business report, credit unions and smaller banks were seen as better serving the needs of smaller businesses. The survey went to 13,000 small businesses with questions regarding bank fees, willingness to lend, accessibility of staff and the simplicity of bank statements.

So, when your bank struggles with a larger competitor, keep in mind some of the advantages you have with a smaller sized organization. Remember also that it's probably easier to be a community bank in the US than in most other countries. Finally, it is good to know that small bank traits like good service and qualified staff are valued everywhere in the world.

BANK NEWS

M&A

The Lincoln National Bank of Hodgenville ($179mm, KY) will acquire Kentucky Home Bank ($109mm, KY) for an undisclosed sum.

Bank Suit

A judge has ruled Target must defend itself against a group of banks that have claimed the retailer played a key role in allowing harm to occur when hackers stole customer data for millions of people.

TBTF Charge

The Fed said it will propose a capital surcharge for the largest US banks on Dec 9 that is largely expected to be around 1.0% to 2.5% depending on risk and complexity. The charge is intended to help protect the financial system and was originally expected to be released back in 2013.

Less Regulation

In an effort to reduce the regulatory burden on community banks, the Comptroller of the Currency has proposed exempting banks with < $10B in assets from the Volcker rule, allow banks to change business strategies without having to change charters and raise the asset threshold to $750mm (from $500mm) for banks to participate in an 18 month exam cycle.

Data Risk

Experian reports about 80% of data breaches are the result of employee negligence or human error.

Passwords

McAfee reports the average person has about 18 passwords, which is one reason there is so much interest in biometrics solutions.

Rate Hikes

JPMorgan indicates consensus expectations for the timing first Fed rate hike have moved over the past few weeks and Sep 17 is now the expected date. Global economic weakness and fear of disinflation pushed the date from Jun to Sep, however Fed members still continue to talk about mid 2015 as the most likely date for the first hike so we will have to wait and see.