Speech by the Governor of the Bank of England

Given at the biennial dinner of the Institute of Bankers in Scotland on 22nd January 1973

Although this is not the first time I have been privileged to propose the toast of the Institute of Bankers in Scotland – the oldest institute of its kind in the world, I believe – it is ten years since I last did so. In fact I have never before attended this dinner while Governor of the Bank of England. I hope this will not be taken to show a lack of interest in Scottish banking or in the fortunes of Scotland generally. Such indeed would be a regrettable attitude for anyone holding my position. The facts are quite otherwise. Although my visits to Scotland are less frequent than I should like, I was here and in Glasgow briefly last August when I had most useful and instructive talks with Scottish bankers and industrialists. Similar visits by directors of the Bank are also made from time to time, while our office in Glasgow maintains continuous contact with Scottish industrialists. Maybe some day, if the Scottish banks did not find it too outrageous, we might even think of doing a little banking in Scotland, in conjunction with our new plans for improving our arrangements for supplying you with Bank of England notes. I doubt whether we should offer the Scottish banks much of a challenge, so let no one lose any sleep over that thought.

There are plenty of real challenges which face us all in the years ahead. The biggest, of course, is to get our economy running efficiently and prosperously. We have passed through a miserable decade which has sapped our self-confidence alarmingly. It is small comfort to know that many other countries are now in a similar plight. Our inflation is among the worst. Many despair of curing it, but we must not give up trying. I am sure that the Government's action in the field of prices and incomes has widespread support from the people, now thoroughly frightened by what will happen if it fails. I do not propose to enlarge on that theme tonight or to discuss whether control of the money supply is the complete and only answer to inflation as some maintain. I have already acknowledged that the money supply is an important factor and we shall continue our efforts to slow down the rate of its growth so far as is consistent with the Government's objectives for the expansion of the economy. For the time being this means we have to accept interest rates which are historically very high (at least in nominal terms). These rates will come down as inflation subsides but not otherwise. So we all have good reason to support the Government in their efforts to cure our economy of this debilitating disease.

Then, we are at last members of the European Community – surely the only name by which it should in future be known. As you all know, I have always whole-heartedly supported this objective and I am delighted that it has now been achieved. Our industry and commerce will shortly be able to taste the first fruits of a greatly enlarged home market, meaning one where within a measurable time no tariff barriers will exist. Whether or not this proves enjoyable will of course depend upon success in competition. The challenge will be exciting but success will need to be worked for.

In the field of banking, on which I want to touch tonight, great changes have of course already taken place. The clearing banks in Scotland, as in England, now disclose the full state of their balance sheets and profit and loss accounts. It seems to me that in recent years the major banks in this country have brought efficiency and profit into a closer partnership with service to the community. Clearing bank amalgamations south of the border have gone as far as would be permitted for as far ahead as one can see. In Scotland the same process has taken place with official blessing, and I hope that the rationalisation which it permits will be carried forward with all possible speed. The new arrangements which we introduced fifteen months ago under the heading of "Competition and credit control" have removed constraints and opened up opportunities which seem to have been eagerly grasped.

Looking ahead, we in the Bank have been giving thought to the changes and problems in the banking world which we may expect to come as the nine nations of the Community progress along the road to economic and monetary union. In particular it seemed to us that the British banking industry might see advantage in some changes in structure in order the more effectively to compete in the wider market for banking services now opening up. We were concerned, therefore, to examine our attitude to banking participations in various respects, and in particular to links between our banks and those of other countries in the Community to ensure that obstacles to change were not unnecessarily retained. As you know, the Bank of England have, as a result, modified their attitude quite significantly.

There are some who think that the mere removal of obstacles is not enough and that those in authority should devise blue prints for the future development of banking. I am chary of this approach, believing that those actively engaged in the business are the better able to judge the changes which it is desirable and necessary to make. It is indeed difficult to tell what changes will flow from our new rules on mergers and participations, but that there will be changes there can be little doubt. Perhaps the most likely development will be the arrival of the all-purpose bank in the United Kingdom. This will not be unwelcome provided it does not lead to the submerging of the special talents and expertise of the merchant banker. Less likely and less welcome, in my opinion, would be a change in the relationship between the main deposit banks and industry in imitation of some continental models. Many have yearned for such a change ever since the Macmillan Report of 1931 and probably for longer, and certainly one can sympathise with the desire to see pressure through the medium of the banking system being brought to bear on industry to improve its efficiency. This is a vitally important objective which has got to be achieved somehow, and, as you know, I have so far had only moderate success in persuading the institutional investor to take on this task. I shall persevere but I would not think it right to seek to persuade the banks to become large-scale equity investors in industry so that they may do the job. I prefer banks to run their business primarily with the accent on liquidity and with the safety of their depositors in mind, as our banks always have done. The capital market is the place for equity investment, as has been underlined by the recent changes which have been made in the application of corporation tax. We are fortunate in having one of the few great capital markets of the world. Our continental friends have to make up for the fact that they are less well served in this respect.

In the field of government, law and regulation, the challenges will be different. The aim will be to develop closer and closer economic and monetary ties. The watchword will not be competition but co-operation and the Community spirit. Nine countries with many different languages must work towards this greater unity, ensuring that differences in their economic, fiscal and monetary policies, their trade, industrial and professional practices, and perhaps also in their law, do not impede the creation or distort the operation of that unity. Much devoted and laborious work over many years will be required. Many problems will be hard to solve. In the banking field, we are already beginning to grapple with one of great importance, the harmonisation of banking legislation. Here, as in other matters, it will, I believe, be most important not to confuse ends and means. In every country the authorities have a duty to see that the banking system conducts its business in a prudent manner and that the public are protected from the activities of unsound or unscrupulous concerns. In some countries this duty falls mainly on the central bank; in others it falls on a government agency. Furthermore, the manner in which this duty is discharged varies quite considerably from country to country. The supremacy of London as an international banking centre, in which the Scottish banks, of course, play their part, is founded on a freedom from vexatious banking legislation equalled in few countries in the world. Our banking system has thrived under a general rule of law and surveillance by the central bank; and generally speaking by its conduct has justified the freedom and flexibility it has been given. It would be a tragedy if this position were radically altered simply to satisfy bureaucratic tidiness. Some changes, no doubt, will be unavoidable. Some, in fact, may be desirable either to ensure fairness within the Community or to enable the authorities to exercise their proper influence over an ever widening circle of financial institutions. Early developments are not to be expected but we must be on our guard. The Bank of England are participating fully in the relevant discussions in Brussels. They will keep the re-formed British Bankers' Association in touch with developments and you may be sure that in their advice to Government they will be concerned to protect the free development of our banking system.

Now I would like to say a word about "Competition and credit control". There is a very small minority who regard this 'new deal' as an unmitigated disaster in all its aspects. Rather more than these are dubious whether the new arrangements will be operated so as to provide adequate credit control. I have some sympathy with these latter critics but none with the small minority. Certainly our record on credit control, at least in the first half of last year, was somewhat disappointing. Although we need longer experience before attempting a measured assessment, I tried to analyse the causes of disappointment in my Mansion House speech on the 19th October last year. I suggested that we had perhaps left action too late. This cannot, I think, be said of our more recent moves. To Scottish bankers, indeed, the recent call for Special Deposits may have seemed somewhat harsh. I hope you will, however, appreciate that it is the essence of the new arrangements that a call for Special Deposits should be uniform, and that distinctions can be drawn only at the risk of slipping back towards surveillance of individual banks' positions, which would be inhibiting both for them and for us. Meanwhile, I see little to complain of in the more competitive banking world which we have succeeded in fostering. The situation is in some ways less tidy than it was, but that is to be expected when competition is freer. I am sure that the banking system is healthier and doing its job better than it did under the old conditions.

All these changes, past and prospective, add up to a considerable challenge to the banking community. Computers, decimalisation, bank mergers, the new arrangements for competition and credit control to which I have just referred – there has been plenty to keep bankers on their toes in the last few years. I believe that so far they have done pretty well. They have shown themselves well able to respond to a changing world with new techniques and methods of working, in all of which – as might be expected – the Scottish banks have played their full part.

I have no doubt that they will continue to do so. Your predecessors, gentlemen, blazed a trail when they founded this Institute as the first of its kind nearly 100 years ago. Its original purpose of fostering the training of bankers and the developments of banking skills is one which is more relevant and necessary today perhaps than ever before. And I know that you have recognised this in the fundamental rethinking of your educational programme which you have recently completed and which has led to the new pattern of studies and examinations currently being introduced.