The performance of major British banks, 1970–90

The banking sector has undergone radical change in structure and behaviour over the past two decades, as a result of technical progress, deregulation and heightened competition, accompanied by increased prudential supervision. This article[1] seeks to describe the effect of these changes on the performance of the four largest banks, using publicly available data only.[2]

Overview

From the war until the 1960s the British banking sector was remarkably stable. It operated within a highly structured financial system, with clear demarcations from other types of institution. This was reinforced both by its oligopolistic behaviour and by various forms of official control, such as lending constraints imposed for monetary policy purposes and exchange controls.[3] Both had the effect of restricting competition. Banking changed radically in the 1970s and 1980s as a result of deregulation and a changing market environment.

Growth in competition was initially stimulated by *Competition and credit control* arrangements (CCC) in 1971, as well as the earlier development of wholesale markets and the euromarkets. Despite periods of consolidation in the mid-1970s after the introduction of the supplementary special deposits scheme (the 'corset'), competition continued to intensify, notably after the abolition of exchange controls (1979) and the 'corset' (1980). In particular, on the domestic side, banks have been in intense competition with building societies for both mortgages and retail deposits, and with foreign banks for corporate lending. This is reflected in declining domestic margins and spreads, and a fall in the proportion of aggregate lending accounted for by the major banks.[4] Banking markets have become either more competitive or more contestable—where contestability refers to the maintenance of competitive conditions, despite the presence of only a small number of firms, owing to the threat of potential competition.[5]

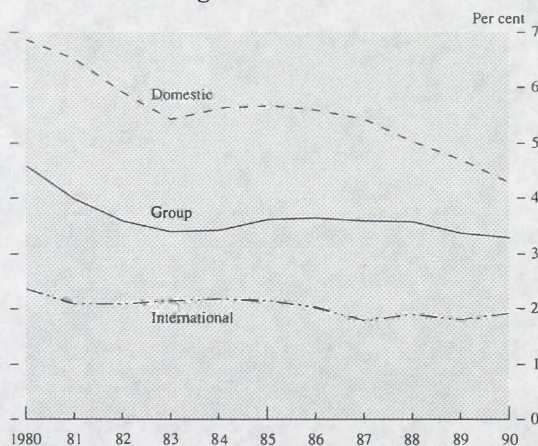
In recent years, the major banks' performance has been strongly influenced by non-performing LDC debt. This threat to their balance sheets was largely removed by substantial exceptional charges made in 1987 and 1989. However, though capital/risk asset ratios have been maintained above the levels specified in the Basle agreement,[6] the banks' balance sheets were weakened by domestic bad debts in 1990.[7] This poses difficulties for the future because, whereas through the 1980s accelerating lending to the UK domestic market offset declining margins, the growth in new lending is now much lower. Particularly in the context of the minimum capital adequacy requirements, this, and the need for provisions, means that cost controlling exercises have become increasingly important.

Income and expenditure

Margins, the endowment effect and spreads

Banks' margins in the 1970s were relatively wide and strongly influenced by the level of interest rates. For example, between 1972 and 1974, the Big Four's *net interest margin* (net interest income as a proportion of interest earning assets) nearly doubled. This increase occurred because, as interest rates rose in response to the increase in inflation, banks benefited from the *endowment effect* (net interest margin less net interest spread).

Chart 1
Net interest margins



(1) Prepared by Richard Colwell in the Bank's Economics Division.

(2) Data refer to the 'Big Four' banks, Barclays, Lloyds, Midland and National Westminster, except where otherwise stated.

(3) However, unlike other countries, notably the United States and Japan, segmentation was not enforced by legal restrictions on activities of financial institutions.

(4) For a detailed discussion of the effects of deregulation on banking structure and behaviour prepared at an earlier stage in the process see J S Fforde 'Competition, innovation and regulation in British banking', in the September 1983 *Bulletin*, pages 363–76.

(5) In the absence of irrecoverable (sunk) costs of new entry, there is a threat of 'hit and run' entry, which acts as a discipline on market participants. Table A provides a summary of the contestable features of key banking markets.

(6) The Basle agreement refers to the minimum target for international banks of 8% for the ratio of capital to risk-weighted assets. A secondary target stipulates that banks have to have 4% tier 1 capital against assets, where tier 1 excludes subordinated loan stock and general provisions. These requirements are set out fully in the BIS publication, *International convergence of capital measurement and capital standards*, July 1988.

(7) A detailed description of recent developments in banks' performance is provided in the *Bank of England Banking Act Report 1990/91*.

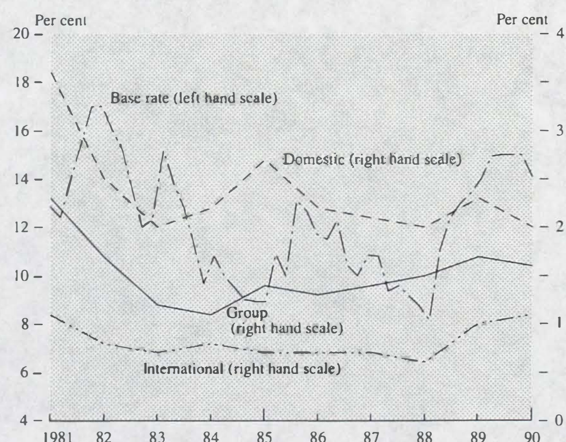
Table A
Contestable features of banking markets (a)

Markets	Contestable features	Non-contestable features
General features of financial products	Largely homogeneous products. Electronic information transmission. Multiproduct firms.	Reputation and expertise—intertemporal features. Residual need for face to face contact. Potential for strategic competition.
Retail deposit banking	ATM networks.	Branch network. Inertia of customers (tend to hold one account)
Credit cards	Facility of advertising/selling. Willingness of consumers to hold several accounts.	
Mortgages	Facility of advertising/selling. Ease of securitisation. Ease of entry and exit. Possibility of having mortgage book managed by another institution.	
Life insurance	Independent financial advisers.	Importance of reputation and long-term solvency. Need for branch network/sales force.
Small corporate banking		Customer information/credit relationships.
Mid-corporate banking	Some willingness to change banks (contestability midway between small corporate and wholesale banking).	Relationships.
Wholesale banking	Competition with securities issuance. Willingness of consumers to have many banks/bargaining power *vis-à-vis* banks. Globalised industry.	Relationships.
Securities issuance	Ease of entry of new firms (market integration). Globalised industry. Resources easily switched between sectors. Competition with wholesale banking.	Importance of reputation, expertise, innovation capacity.

(a) In the absence of restrictive entry regulation and excluding any capital needs.

In contrast, the 1980s have witnessed two periods of declining net interest margins, which were most apparent in domestic business. In 1980–83 the decline was due to the reduced endowment effect as interest rates fell—although spreads (the difference between the rate paid on interest-bearing assets and interest-bearing deposits) increased. However, the more recent downward pressure on margins in 1987–90 largely resulted from declining spreads. Falling spreads were related to heightened competition for loans, to the banks' increased targeting of low margin mortgage and large corporate lending,(1) and to the change in the deposit mix following competitive pressures on the liabilities side of the balance sheet (see page 514).

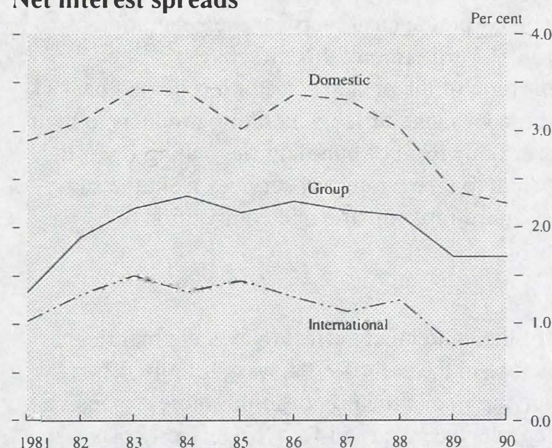
Chart 2
The endowment effect(a) and the banks' base rate



(a) Defined as margin less spread.

Competition for deposits has entailed, *inter alia*, the payment of interest on an increasing proportion of deposits, thus also reducing the benefit of the endowment effect when interest rates are high (see Chart 2).

Chart 3
Net interest spreads

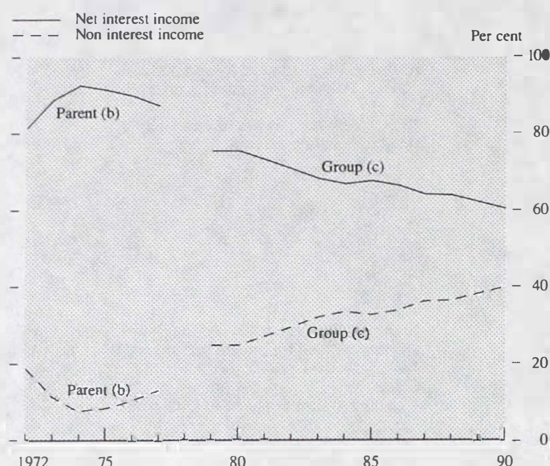


Income composition

Another major difference between the two decades relates to the banks' reliance upon interest income. In the 1970s this provided over 80% of total income, but had steadily declined to just over 60% by 1990. The counterpart has been the steady expansion of non-interest fee income. This reflects the banks' desires to diversify into new areas of business—prompted by increased competition in their traditional markets—as well as the need to economise on capital.

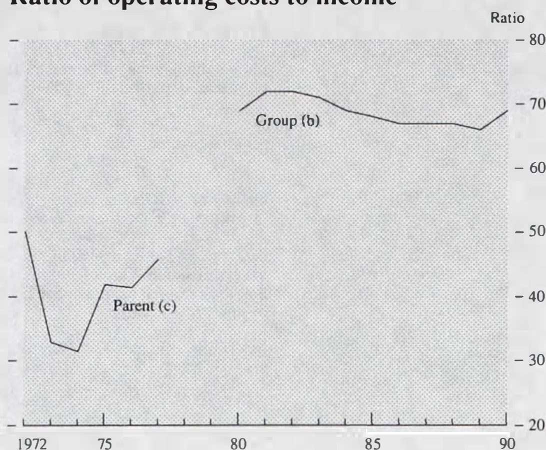
(1) However, in 1990 there were signs that banks were charging large company borrowers wider lending margins—see Chart 14.

Chart 4
Breakdown of total income[(a)]



(a) Given the break in series, attention is directed to changes rather than levels in 1975-80.
(b) Parent = UK bank.
(c) Group = Consolidated entity, including the UK bank.

Chart 5
Ratio of operating costs to income[(a)]



(a) Given the break in series, attention is directed to changes rather than levels in 1975-80.
(b) Group = Consolidated entity, including the UK bank.
(c) Parent = UK bank.

The increase in non-interest income has come from a variety of sources. For instance, the banks have sought to cross-sell related financial service products, such as insurance, while other fee-based financial activities such as estate agency, travel agency and investment banking have also been developed. Nevertheless, the most successful and stable sources of non-interest income have continued to be fees and commissions generated from more traditional banking services. This may seem to conflict with the fact that 'free if in credit' type banking facilities were introduced for personal customers in the mid-1980s. However, the banks rely heavily on corporate customers for the generation of account charges. Furthermore, this effective cross-subsidisation of the personal sector has helped banks to market a broader range of fee-generating products to their customer base. This form of bundling (ie making it worth customers' while to take a range of services from the same institution) is an example of strategic competition.[(1)]

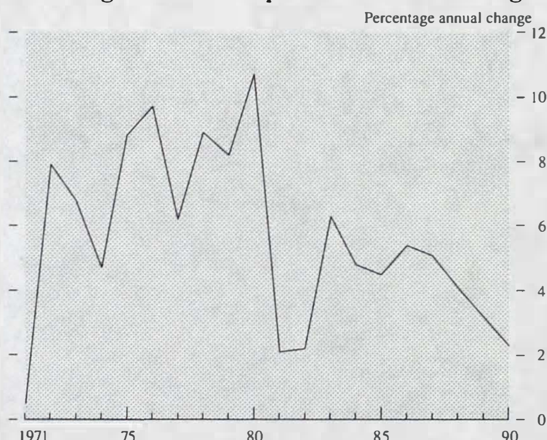
Costs

The benefit of the endowment effect to average margins, as interest rates rose in the early 1970s, was partially offset by the accompanying rise in the proportion of more expensive wholesale deposits (see page 514). Non-interest costs also rose substantially, partly as a consequence of inflation, but also because low levels of competition and the benefit of the endowment effect offered little incentive to cut costs. Although these factors have weakened through the 1980s, the Big Four's *cost/income ratio* declined only slightly and has remained at high levels. To a large extent, this reflects the size of retail branch networks, which were sustainable provided endowment profits were sizable, but became a burden when these were eroded. Other factors included the evolving nature of banks' 'business mix', in which there has been an increasing reliance on more labour (but less capital) intensive fee-generating activities (see Chart 4). The banks have recognised the need to cut costs in the face of reduced earnings, but costs in the 1980s were inflated by investment in new technology that has only recently begun to provide benefits. Also, the cyclical decline in the growth of operating income in 1989–90 has offset the improvements made in cost containment.

Staff and branch numbers

Trends in branches and employment have been strongly influenced by technical developments. For example, a major technological shift for banks is indicated by the structural (as well as cyclical) deceleration of growth in the volume of bulk *paper clearing* through the late 1980s (see Chart 6). Back offices and the payment mechanism have been automated for both personal customers (eg via Automated Teller Machines (ATMs))[(2)] and business customers (eg via the Clearing House Automated Payments

Chart 6
Annual growth of cheque and credit clearings



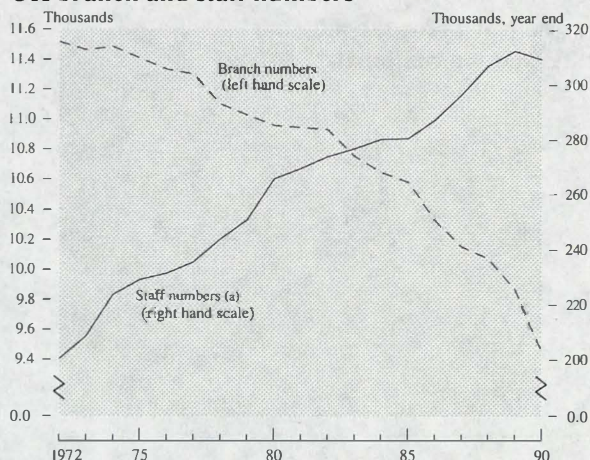
Note: Relates to all banks, not just the 'Big 4'.
Source: APACS.

(1) See, for example, J Tirole, *The theory of industrial organisation*, MIT press, 1988.
(2) The ratio of ATMs to branches for the Big Four is now about 1:1, with approximately 60% of all retail deposit withdrawals taking place through ATMs.

System (CHAPS)). Although the major banks were pioneers in the use of these automated payment mechanisms, they have been widely adopted by other institutions. For instance, in 1976 the Big Four owned all the ATMs in operation, whereas their share is now only 55%. This reflects the growth in competition for retail banking business. In addition, the authorities have latterly ensured open entry to large value payments systems.

The deceleration in the growth of the volume of paper clearing has accompanied the on-going reduction in the number of *branches*. Developments in technology have helped to reduce the importance of the branch network as an entry barrier because financial institutions such as centralised mortgage lenders, using modern credit scoring techniques, have been able to sell financial products by newspaper advertisements or by telephone, without branches.(1)

Chart 7
UK branch and staff numbers



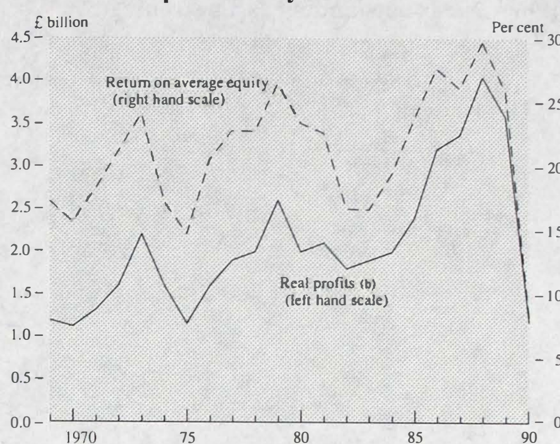
Source: British Bankers' Association.
(a) Average weekly total number of persons employed.

Staff costs represent the principal element of the banks' non-interest cost base, typically accounting for 55%–60% of total expenses. Following periods of rapid growth over most of the 1970s and 1980s, the growth in staff numbers has been falling since 1988, and an actual decline in numbers was recorded in 1990. Besides cutting staff numbers, banks have also sought to improve productivity. For instance, investment in technology is helping replace staff in back-office processing tasks, releasing them for front-office sales tasks (including the sale of insurance as well as banking services in recent years), and thereby increasing the return from branch networks.

Profits

Banks' profits are heavily influenced by interest rates and cyclical factors, as well as by the banks' own actions. For instance, the substantial increases in profit in the early 1970s were due to the effects of rapid credit expansion and the related benefit to endowment profits from high interest rates. However, although external factors may cause cyclical

Chart 8
Indicators of profitability[(a)]



(a) Pre-tax, pre-LDC profits.
(b) Pre-tax pre-LDC profits / GDP deflator (1985 prices).

movements in profit, the Wilson Report (1978) concluded that, even allowing for this, banks' profitability (as measured by the real rate of return on book value) substantially improved in the 1970s. This upward trend strengthened in the 1980s, and reflected the heightened profit consciousness of banks—and perhaps what proved *ex post* to be a willingness to move up their risk/return trade-off—in the light of greater competition.

In the late 1980s, however, bank profitability was strongly influenced by provisions made against LDC debt. During 1987 and 1989 the Big Four banks raised LDC provisions cover to 50%–70%, resulting in very poor profits. In 1989–90, the upward trend in profits excluding LDC provisions was also reversed (see Chart 9), as domestic bad debts began to accumulate, necessitating further provisioning.

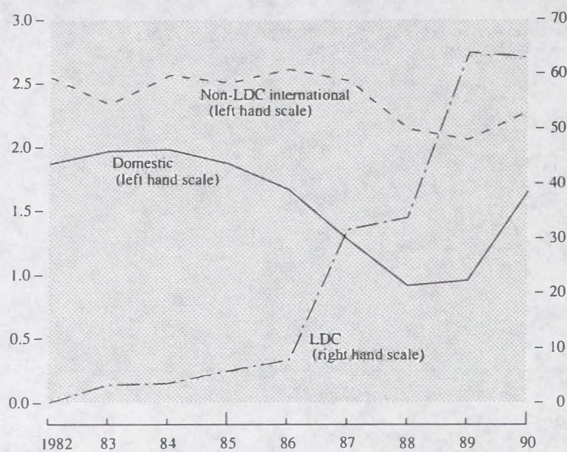
Bad debt provisions

In the 1970s the banks were not obliged to publish the extent of their losses, and did not adopt a policy of full bad debt disclosure until 1978, after a Price Commission Report. Consequently, there are no public data to illustrate the extent of the bad debts that had to be written down in relation to loans made to secondary banks and property companies following the 1973–75 downturn.

As a consequence of the world recession of the early 1980s, bad debts increased, and provisions rose in their wake. The upward trend in provisions outstanding as a proportion of lending continued at a reduced rate until 1984 on the domestic side, while the ratio of (non-LDC) international provisions to lending did not peak until 1986. In the mid-1980s the level of commercial provisions outstanding declined, mainly owing to the improved financial strength of the UK industrial sector, which meant recoveries were made from earlier provisions. Meanwhile, as noted above, LDC charges were substantial in 1987 and 1989, although the risk of large scale default first became apparent in 1982.(2)

(1) See the November 1990 *Bulletin*, pages 503–11 and the February 1991 *Bulletin*, pages 56–66, for a more detailed discussion.
(2) For a detailed analysis, see the article by M J Dicks, 'The LDC debt crisis', on pages 498–507.

Chart 9
Bad debt provisions outstanding as a percentage of lending

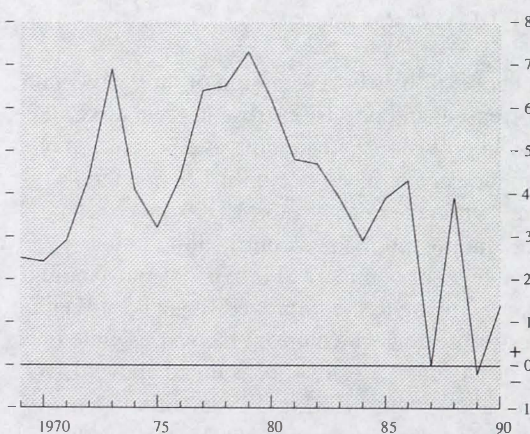


Non-LDC provisioning also started rising again in the second half of 1988 and this trend has continued into 1991. (This sharp increase in provisions may partially reflect earlier recognition of bad debts by the banks). As well as the economic slowdown, these provisions may indicate a pattern of lending to a broader range of borrowers over the 1980s, which was also initially reflected in higher apparent profitability. It is notable, however, that for the four major banks provisions outstanding as a percentage of domestic advances in 1990 were still below the levels of the early 1980s.

Distribution of profits

Historically, *dividend cover* (attributable profit/dividends) of three times has been typical for the major banks, and this has generally been maintained with comfort since 1972. However, in 1987 and 1989 the ratio fell well below this level owing to LDC provisioning. Then in 1990 it recovered but only to an average of just 1.4. Similarly, *retentions* were negative in 1987 and 1989 and only £309 million in 1990. This is in contrast to the preceding period of sustained high retentions—averaging £900 million from 1980 to 1986—which in turn made possible sufficient capital growth to support rapid balance sheet expansion.

Chart 10
Dividend cover



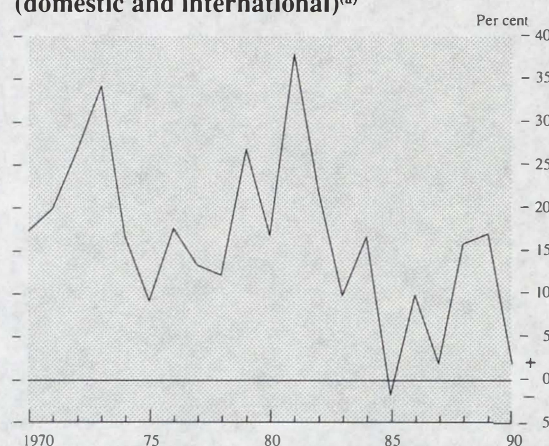
Balance sheet

In the main, this section refers more broadly to measures relating to the banking sector as a whole, owing to the difficulty in obtaining suitably disaggregated and publicly available data for the four major banks.

Assets

The removal of quantitative controls over *bank lending* in 1971 as part of the *Competition and credit control* arrangements (CCC)[1] enabled the banks to compete on a 'level playing field' with new entrants such as the secondary banks. Consequently, there was a significant amount of re-intermediation, with banks attracting back business that had been lost during the earlier period of direct controls.

Chart 11
Total asset growth for the 'big four' (domestic and international)[a]



(a) Foreign currency lending translated into sterling at prevailing exchange rates.

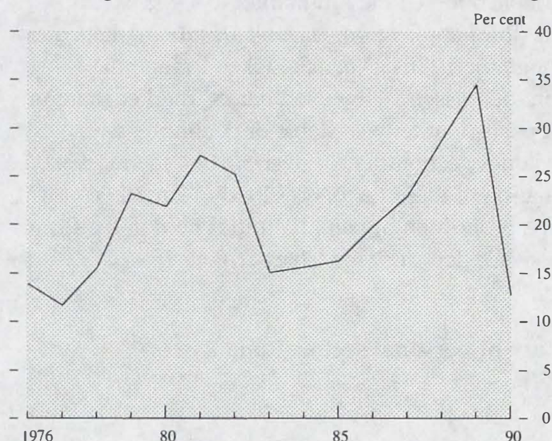
CCC was introduced at a time when government demand management policy was expansionary. This led to a significant growth in bank lending, which in turn further stimulated economic growth, as well as financing rising asset prices. When the authorities later decided to restrain this economic expansion, they chose to introduce a new quantitative control, the supplementary special deposits scheme (the 'corset') in December 1973. The 'corset' was designed to limit the growth of the banking system's sterling interest-bearing deposits; and thereby reduce its ability to lend. Its applications were over 1973–75, 1976–77 and 1978–80. This (as well as recession) succeeded in subduing the domestic asset growth of the banks over the late 1970s.

One response was to expand international bank lending to LDCs and others.[2] Moreover, the 'corset' was not effective in reducing credit expansion as a whole, particularly during its last application, because large scale disintermediation took place, whereby banks continued to enable companies to

(1) See 'Reflections on the conduct of monetary policy: text of the first Mais lecture' in the March 1978 *Bulletin*.
(2) Some commentators have referred to this process as 'recycling', but others suggest the banks played a much more active role in the process than this term implies.

borrow through fee-earning off-balance-sheet activities.[1] Some authors[2] also suggest that banks began to avoid the constraint by engaging in switching; for instance, by reducing interest rates on savings deposits and cutting charges on non-interest-bearing deposits, they could switch funds out of the controlled category. This may help to explain the recovery in the banks' domestic asset growth in 1979. In addition, the abolition of exchange controls that year enabled funds to be obtained offshore, rendering the 'corset' ineffective. Largely as a result, the 'corset' was abolished in June 1980.[3] Subsequently the banks have not been subject to any quantitative constraints, enabling greater competition to take place and facilitating the growth in lending in the 1980s.

Chart 12
Annual growth rates of domestic bank lending[(a)]



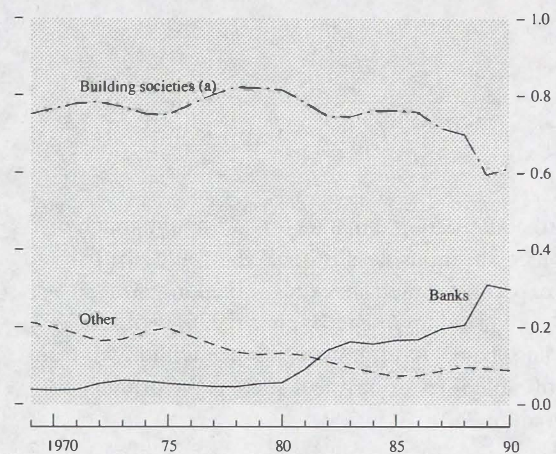
(a) Relates to all UK banks, not just 'Big 4'.

During the 1980s the banks saw their *domestic advances* grow rapidly at an average rate of around 19%. The fastest growth rates were experienced in 1981–82 and 1986–89. The first period largely reflected the large scale distress borrowing by companies during the recession of 1981–82. However, the subsequent growth was fuelled by lending to the personal sector as well as to the company sector.

Competition in *consumer lending* increased considerably over the 1980s, notably after the abolition of hire purchase controls in 1981. For example, non-bank financial intermediaries increasingly offered credit through newspaper advertisements, while the Building Societies Act 1986 enabled societies to provide limited unsecured lending facilities. The volume of credit card transactions increased by about 75% between 1985 and 1990; however, although partly reflecting the growing number of institutions, much of the associated lending has remained on the banks' balance sheets.

The *mortgage market* has also become increasingly competitive following the abolition of the 'corset'. With virtually no mortgage loans on their books, banks were able to increase mortgage lending considerably without suffering portfolio imbalance. In addition, the break-down of the building societies' interest rate cartel led to mortgage rates moving more in line with money-market rates, and consequently funding could increasingly come from the wholesale market, buttressing banks' competitiveness. In the light of increased competition in their traditional markets, such as for corporate loans, as well as, latterly, the

Chart 13
Share of mortgage market



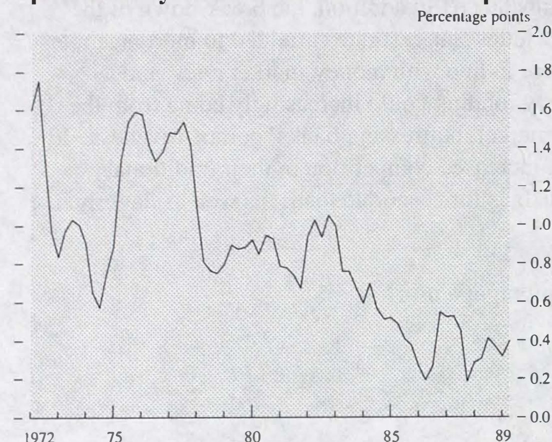
Source: CSO.
Note: Relates to all banks, not just the 'Big 4'.
(a) Abbey National figures included with building societies up to and including 1988, and with banks from 1989 onwards.

relatively favourable 50% risk weight for capital adequacy purposes on mortgage loans, the banks have sought to consolidate their position in this market over the last decade. Mortgages now represent a key area of banks' portfolio; and they have increased their market share to about 30% from under 10% in 1980.

In the meantime, the relative importance of *lending to industrial and commercial companies* declined in the 1980s, despite rapid growth in the 1987–89 takeover and investment boom. However, a growing part of banks' corporate business has come to be supportive of borrowing elsewhere, rather than direct lending by banks to companies, in response to the tendency for large corporate customers to raise finance direct from bond markets, or through commercial paper, rather than by way of bank loans. This disintermediation and the consequent increase in off-balance-sheet activity[4] was facilitated by the fact that, following the banks' LDC experience, many potential corporate customers' had better credit ratings than some banks, and could consequently borrow funds as or more cheaply on the open market in their own names. Furthermore, increased competition from, in particular, foreign banks and the price sensitivity and willingness of customers to deal with many banks has resulted in narrow margins on wholesale corporate lending (see Chart 14 for

(1) Note that part of the funding occurred through the 'bill mountain'.
(2) See, for example, D Pierce and P Tysome (1985), *Monetary economics. Theories, evidence and policy*, Butterworths, page 276.
(3) For a detailed analysis of the 'corset', see 'The supplementary special deposits scheme' in the March 1982 *Bulletin*, pages 74–85.
(4) Off-balance-sheet activities involve contingent commitments not captured under conventional accounting procedures (although they are taken into account by supervisors for capital adequacy calculations). Four types of such activity can be distinguished: unused credit facilities (eg NIFs), guarantees (eg acceptances), forward contracts and underwriting.

Chart 14
Spreads on syndicated credits to UK companies



Note: Weighted moving average.

patterns in the international market[(1)]). Although much of the off-balance-sheet business is booked through the parent banks, the expertise of their investment banking arms, developed in the lead up to Big Bang in 1986, is often utilised. Major banks have, however, since withdrawn from some unprofitable lines of business such as the primary eurobond market.[(2)]

The underlying level of *foreign currency lending* rose substantially in the 1970s, as the banks intermediated funds to developing nations. Voluntary lending virtually ceased in 1982, when Mexico announced it could no longer service its international debts. However, the growth in foreign currency lending continued over the first half of the 1980s, nearly doubling in importance as a constituent of banks' balance sheets over 1980–86. Geographic diversification was justified on the grounds that it would yield counter-cyclical benefits and support the business of major customers. After peaking in 1986, however, foreign currency lending by the Big Four as a percentage of their assets has declined. As well as reflecting the relative strength of the domestic market up to 1989 and, until recently, low spreads (see Chart 14), this also signals the change in banks' attitudes away from the pursuit of asset growth *per se*, on account of the need to maintain profitability and adequate capital ratios.[(3)]

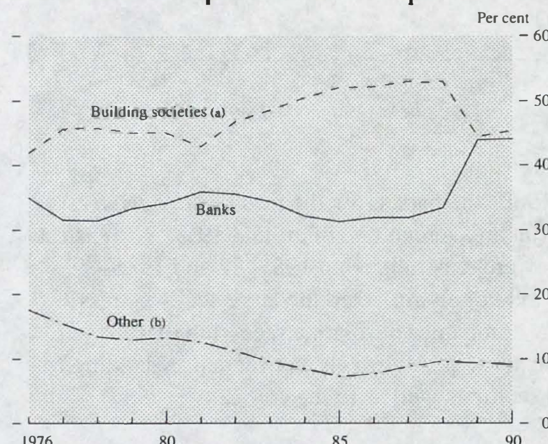
Moreover, the view that major corporate customers need a bank's presence in all the countries they operate in is no longer widely held. Instead, the emphasis is on achieving adequate profitability in all areas of business, both geographically and by product. This theme is reflected in the major banks' approaches to the completion of the EC single market by the end of 1992. From a defensive perspective, they have focused on strengthening their domestic operations by improving the quality of service and increasing cross-sales to existing customers. In other EC countries, although differing in their views on which markets to enter, the banks have tended not to focus on the retail and medium-sized corporate sectors, preferring to concentrate on large corporate and investment banking and non-banking financial services. Acquisitions have been mainly of second tier specialist subsidiaries or regional banks, while minority shareholdings have not generally been favoured.

Liabilities

(i) Deposit structure

In the early 1970s, the banks developed new techniques of 'liability management'. In essence, banks came to fund loans rather than lend deposits. This change was associated with the development of new markets and financial instruments such as the interbank market and certificates of deposit. Although the 'corset' slowed balance sheet expansion, it encouraged the bill market to some extent, notably in its third application. The *wholesale* markets grew further through the 1980s as banks looked to fund the expansion in their assets. However, banks' market share in the *retail* deposits market was stable or declining, with building societies accounting for over 50% of the market. The combination of these factors resulted in a marked decline in the proportion of bank liabilities held in the form of personal sector deposits (see Chart 16).

Chart 15
Market share of personal sector liquid assets



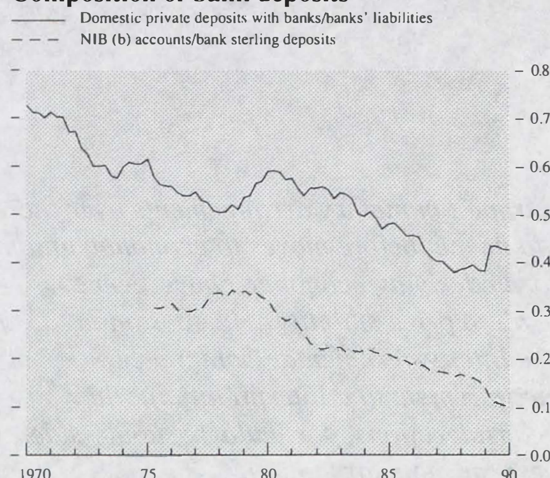
Note: Relates to all banks, not just the 'Big 4.'
Source: CSO.

(a) Abbey National figures included with building societies up to and including 1988, and with banks from 1989 onwards.
(b) Comprises: certificates, bonds and SAYE, ordinary and investment accounts, tax instruments and local authority temporary debt.

Competition for retail deposits resulted in the introduction of explicit[(4)] interest-bearing current accounts in the mid-1980s, reducing the endowment effect and cross-subsidisation, as noted above. Despite this increase in their cost, retail deposits are generally a cheaper and less volatile source of finance than wholesale deposits. However, despite launching a wide range of new products targeting specific market segments, the banks have yet to increase their share of the personal savings market significantly.[(5)]

(1) Recent developments in the international syndicated loan market are discussed in the February 1990 *Bulletin*, pages 71–7.
(2) See 'Excess capacity in securities markets' in the November 1989 *Bulletin*, page 527.
(3) For example, the speech by Mr Brian Pitman, 'Banking—an industry in turmoil' at the CIB London Centre, on 22 January, 1991.
(4) Before this, current accounts paid notional interest that was offset against fees for other account services. Now these are often paid for directly.
(5) The increase depicted in Chart 15 is due to the inclusion of Abbey National as a bank from 1989.

Chart 16
Composition of bank deposits[(a)]



(a) Relates to all banks, not just the 'Big 4.'
(b) NIB = Non-interest-bearing.

(ii) Capital account

In the late 1970s and early 1980s the Big Four's *equity/assets ratio* dropped sharply as rapid balance sheet growth took place. The ratio was then strengthened as new capital was injected by way of retained profits and funds from rights issues. The major British banks maintained strong capital positions through the remainder of the decade, and in contrast to some of their international competitors comfortably met the *Basle capital standards* interim target of 7.25% capital to risk-weighted assets by the end of 1990. They have in fact operated at ratios in excess of 8% since the proposals were announced in December 1987. Despite the recent deterioration in profitability and decline in the equity/assets ratio, tight risk assets control and adequate tier 2 capital (such as subordinated debt) has enabled the banks to maintain relatively high capital ratios.

Relative share price performance

After a period of strength in the early 1970s, the *share performance* of all quoted banks relative to the FT 500 index deteriorated steadily from 1974 to 1982. And in spite of periods of recovery from time to time through the 1980s, the bank index is currently close to the bottom of the long-term trend, as downward re-ratings are made in the light of lower profit growth than other industries and the sharp decline in the quality of domestic lending. Partly as a counterpart, the *dividend yield* (dividend/share price) on bank shares has consistently been higher than average yields through the 1980s, rising to a peak of about 1.8 percentage points above the market average in 1984. Finally, the banking sector's *PE ratio* (share price/earnings per share) relative to the UK market as a whole has not been above 70% since the mid-1980s, suggesting that investors have perceived the sector's growth potential to be lower than the average for UK industries.[(1)]

Chart 17
Equity/assets

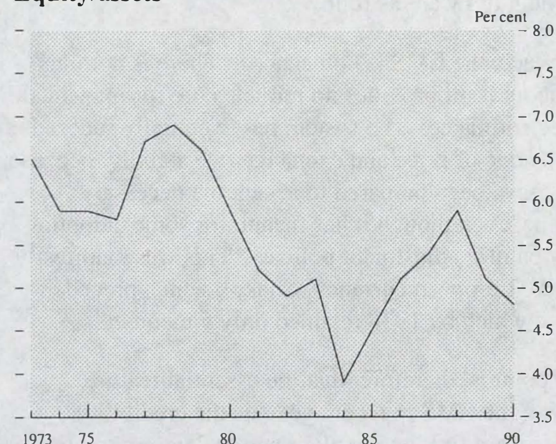
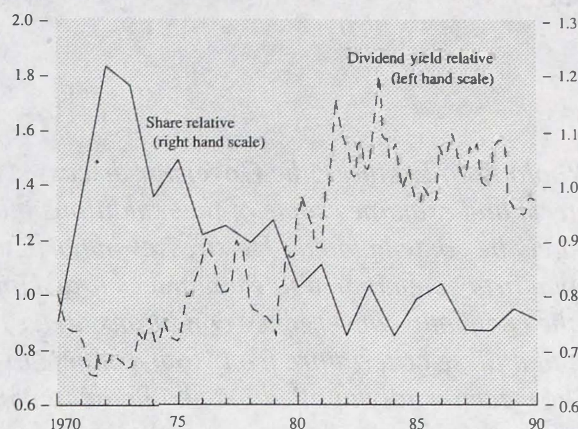


Chart 18
Banks' relative share prices and dividend yields[(a)]



Source: Datastream.
(a) Relates to all banks, not just the 'Big 4'.

Conclusion

This article has described how the removal of regulatory and institutional barriers, together with advances in technology, has changed the structure of the British banking sector from an oligopolistic to a more competitive framework. The major banks' share of core markets has fallen while margins and latterly spreads have declined. In response, the banks accelerated their balance sheet growth and diversified their activities. However, this increased risk, as has been apparent in the magnitude of LDC non-performing loans and in the extent of the recent sharp rise in domestic bad debts. The introduction of the Basle capital standards has now focused greater attention on the need to maintain capital appropriate to the level of risk undertaken and, for this, to generate adequate returns on equity. The major responses to these developments on the part of the banks include:

- a much greater emphasis on cost control;
- a greater questioning of whether business justifies the capital it requires; and
- diversification into less capital intensive fee-earning areas such as insurance.

(1) However, some analysts suggest that because of the distortion of exceptional items and the nature of bank investment valuation, the actual value of accounting profits and hence of PE ratios may be questioned.