



**WHY CANADIAN BANK
MERGERS ARE NOT IN THE
NATIONAL INTEREST**

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CHECK AGAINST DELIVERY

Thank you very much ladies and gentlemen for that warm welcome. I must say it's a pleasure to be here.

Now, as the title of my remarks suggests, what I'd like to address is the subject of financial sector policy and, in particular, the proposed bank mergers. I'd like to offer some facts and look at a few of the issues that I think are most important and relevant to what is the single most important decision Canadians and their government will make concerning our financial system; the most important decision in the past half century.

This truly is a critical and very complex question of public policy. It's not something that should be debated on the basis of personalities or name calling or silly innuendos like Scotiabank has somehow reversed its policy views, which, by the way, we have not! That sort of thing is just papering over the real issues -- the very important issues that matter -- and must be considered carefully -- with a very broad range of input and research.

Financial sector policy must be defined based on facts because it's about what's in the best interests of all Canadian consumers and businesses right across the country. It's about establishing the right future policy direction for our financial system, which is crucial to the functioning of our economy (Just look at the mess in Japan!). It's about competition and choice. It must be looked at in terms of facts, with policies established in the broad national interest.

In fact, I strongly suspect that many people here this afternoon understand well that we all have a significant stake in this issue. As entrepreneurs, professionals and business people, you know that competition and choice are the only true safeguards to ensure good and reliable access to credit, quality services, and tough price competition.

Now, before we look at certain facts -- I'd like to make two observations. First, as many of you know, tomorrow is an important day in terms of government's review of financial sector policy. Tomorrow morning Harold MacKay will table a major study and recommendations for the federal government to consider.

Mr. MacKay has led the work of a Task Force appointed by government, by Finance Minister Paul Martin in 1996, to review the future direction of Canada's financial sector. It's a process that the industry asked for, that Scotiabank has supported from the outset, and that we've participated in several times.

Harold and his colleagues have looked at the complete range of issues concerning the financial sector including banks, insurance, credit unions -- and consumers and small business as well! The Task Force recommendations will kick off further careful study and consideration through Parliamentary Committees and extensive consultation with Canadians, which is another process that we fully support.

Now, obviously, I don't have a copy of the report, but I suspect that many of the Task Force's general views will be in line with Scotiabank's thinking, such as the need for increased flexibility for financial institutions to increase the scope for holding companies, joint ventures and various forms of partnerships, and the need for a more progressive regulatory system.

On some other issues, I'm sure we won't agree with the Task Force at all. There will be different studies and different points of view, which obviously is healthy and an important part of finding the right policy framework for Canada.

I also suspect that the Task Force will suggest the need for careful study by government, by Parliament and ultimately, by the Finance Minister, of bank ownership policies including the pros and cons of mega-mergers. This sort of careful study is also something we support and, in fact, is something we recommended to the Task Force last year. Government must consider mega-mergers as one issue in the broadest possible way by taking into account issues concerning the entire financial sector and the interests of all Canadians.

We fully support the government's process and, most importantly we fully support government moving the policy agenda onto the broadest footing possible by considering the full range of issues and not just the narrow issue of bank mergers. The mega-merger issue has -- unfortunately -- really pre-empted the consideration of all other important aspects of our sector. The aim must be to define and implement a new legislative framework for our financial sector before we go anywhere on specific proposals.

The second observation I would make, by way of background, is that historically, and today, Canada's financial sector, and in particular, our banking system is an important part of the economy and fabric of our country. Our banking system is highly efficient, very safe and stable, and extremely competitive. It's a national system with five strong players and it's very technologically advanced.

These, by the way, are not just my conclusions. They are from the World Economic Forum, the Canadian Bankers Association, and a broad range of experts and other institutions from around the globe.

We have a winning system with all major banks competing for share and turning in record domestic profits, with returns on equity in our domestic operations ranging from 20% and up. In other words, this isn't an industry under attack. To the contrary, it's an industry that has adjusted very well over the years to new competition, to new technologies and to other challenges. It's an industry that's thriving and serving its customers well and rewarding its shareholders, notwithstanding recent market corrections!

In my view, the primary aim of government in considering the MacKay report and the future direction of Canada's financial sector must be to maintain and build upon these great strengths of our current system.

This is why greater competition must be the foundation of changes to Canada's financial sector. The more competition the better. In particular, Canada needs a high degree of competition in core banking markets -- every day banking services that touch virtually every Canadian household -- personal deposits, transaction accounts, loans and mortgages -- as well as in small business lending.

As an aside, I want to emphasize that the mega-merger debate is not about mutual funds, or wealth management, or monolines, or pension fund assets. It's about core banking. It's about access and choice for Canadian consumers and small businesses. It's about chequing and savings deposits and ABMs, the core franchises that are completely dominated by the big banks.

Certainly, I appreciate the desire of some to try to focus the issue on broadly defined markets. But that's not the way to assess the impact of bank mergers.

On that note, let's turn to the proposed bank mega-mergers specifically and let's consider some facts.

Scotiabank is in favour of competition. We're in favour of enabling banks and other players to grow and bolster international competitiveness. However, we're against mergers that substantially lessen competition and significantly reduce choice for Canadian consumers and businesses.

Fact: mega-mergers would represent a truly massive and irreversible restructuring of our financial system.

Fact: mega-mergers would mean that we'd lose one-third of our banking system. Going from 5 national banks to 3 will obviously not increase competition.

Fact: mega-mergers would mean that almost 70% of core banking in Canada would be in the hands of two institutions. This level of concentration would not be tolerated anywhere else in the world!

Last week we released some analytical work that we commissioned from Deloitte and Touche. This research documented, for the first time, domestic banking asset concentration levels for major developed countries around the world.

This work shows that in Canada the two-bank concentration level in a post-mega-merger environment would be 66 per cent, representing the most highly concentrated market in the world. Much, much higher than the U.S. or the U.K., and even higher than the Netherlands and Switzerland which are often referred to incorrectly as the most concentrated markets anywhere!

Fact: mega-mergers are an extremely high-risk option for Canada -- and would not be in the best interests of our country.

Fact: bigger is not better! Scotiabank's strong international network -- we're in 53 countries around the world -- and we're a top-ten bank in global and U.S. syndication markets. Canadian banks don't have to merge with each other to achieve international success. If size were the key determinant of success Canadian bankers would have given up long ago to the likes of Citicorp, Chase, or Barclays, and so on.

Fact: Canadian banks -- with or without mergers -- are small to mid-sized by international standards. You'd have to add up basically the entire Canadian financial system to get to the size of the market capitalization of Citi/Travelers or NationsBank/Bank of America. The merged Canadian banks, as well as Scotiabank, would be "sitting ducks" if takeovers were permitted in Canada (although I recognize that's a significant "if" in terms of government policy). Obviously, in today's world, size is no defense.

Fact: foreign banks control only about 8% of total banking sector assets in Canada. This is one of the lowest totals in the world, the U.S., for example, is at about 14%. And 16 of the 20 biggest banks in the world are already here in Canada and many other institutions have come and gone.

Fact: monolines such as Amex, Household Finance, GECC, GMAC, Templeton have been here for many, many years, since before I joined The Bank of Nova Scotia. And notwithstanding, over the past 35 years Canadian banks have flourished. Our market share is about the same in terms of the total system and, as I said, profits and returns are at all-time records.

Fact: foreign competition is an important part of the financial sector by adding an important element of choice, which is good for consumers and businesses, and it is a challenge for Scotiabank and our domestic competitors, as I've said many, many times over the years. But foreign competitors are not threatening Canadian bank viability. And keep in mind that these foreign institutions do not compete, and will not compete, mergers or no mergers, in a meaningful way in core banking, or in SME lending, or in small towns and rural Canada.

Fact: in-market mergers mean serious cuts in employment and branches. Now, obviously, I don't know my competitors' plans and maybe mergers can be managed with few job losses. But, based on our experience in integrating Montreal Trust and National Trust, based on the computer modelling that we've done on branch overlaps, and based on our examination of other in-market mergers in the U.S. and around the world, we think there could be significant cuts if the mega-mergers are allowed.

Conservatively we've estimated 20,000+ job losses and 1,000+ branch closures across the country and that's at the low end. You may have seen in yesterday's Toronto Star that Doug Peters, former Secretary of State for Finance and Arthur Donner, both senior economists -- presented a paper to a conference at Laurentian University that concludes job cuts could run as high as 40,000. These sorts of cuts, by the way, seem to line up with the announced \$1 billion restructuring charges for each merger -- \$2 billion in total -- is a lot of jobs and branches given 60% of banking is people expense.

Toronto, incidentally, could be particularly hard hit. We would see two head offices disappear and we estimate -- based on our experience and research -- permanent job losses of 10,000, and branch closures would likely total more than 300.

Fact: the idea of economies of scale is very questionable. While short-term cost cutting is doable (20,000 jobs, 1,000 branches), there is little evidence to support efficiency gains over the longer term. A recent Bank of Canada report and a number of Federal Reserve reports have concluded that there is no empirical evidence to support arguments that banks have to be mega-institutions to achieve most economies of scale.

Fact: Scotiabank and TD, which are the two smallest of the big 5 today, have been the most efficient banks in Canada for many, many years. If efficiency gains are possible why haven't the larger banks in Canada proven to be more efficient than TD and ourselves who are two-thirds their size domestically?

As Michael Porter, the Harvard guru, said earlier this year on the subject of banking: "You asked about scale. I must say I am a skeptic on scale. There is increasing evidence you don't need as much scale compared with 10 to 20 years ago to be efficient. We've learned about outsourcing." So, even on technology, efficiency gains are not an issue.

Fact: long-term consumer benefits will not come from mega-mergers. Access and choice will be reduced. Lower income, older Canadians and small business, as well as people in smaller, rural communities would be hardest hit. I'm expecting announcements of service charge reductions or freezes, or other such short term tactics to win public support even though I think people are too smart for that!

Research for Scotiabank by First Manhattan Consulting Group examines the issue of consumer benefits, looking at the experience in California, where there have been several major mergers over the past few years and where concentration levels are quite high.

Despite California being raised as a point of comparison by some, it's a bit odd to compare a U.S. state to Canada's national system because this is about Canada. But California is the one area where at least some data exists.

The bottom line is that consumer prices in California have gone up not down as banking sector concentration levels have risen through mergers. Deposit rates for consumers are lower in California than elsewhere in the U.S. Coincidentally, this conclusion was recognized by the Royal Bank in a 1996 policy paper to government and termed "excess spread" looking at markets in the U.S. with high levels of banking sector concentration!

Fact: mega-mergers will hurt small business. I'm sure many people here today have seen the results of a poll conducted by the Canadian Federation of Independent Business -- 68% of its members oppose bank mega-mergers. The main concern is the loss of competition and less choice. And, not surprisingly, the concerns are greater the smaller the firm, which are typically businesses and people with fewer banking and financing options already.

I know that Royal and BMO have announced a plan to combine their small business lending operations and create a new division. And I applaud them on this initiative. But this is still not new competition and, obviously, mega-mergers, despite this sort of positioning, mean less choice and less access to capital for Canada's small businesses.

Ladies and gentlemen these are the facts, and facts are what this debate must be about! This is about Canada and Canada's banking system. It's about core banking not mutual funds or wealth management or monolines, or pension funds. It's about competition and choice.

There is no case to support mega-mergers. To the contrary, mega-mergers are highly anti-competitive and represent a high risk irreversible policy option.

They would eliminate one-third of our country's banking system and increase concentration to levels not seen anywhere else in the world.

I want to emphasize that I'm not arguing for the status quo. Clearly, the Canadian financial sector and our banking system must change just as it has changed and adapted in the past. In fact, public policy has always been an important part of how our system has evolved, and the strength of our current system. But there are better policy options than mega-mergers. Government must take its time because doing it right is more important than doing it fast.

Clearly, turning down the proposed mergers is not interventionist as some suggest. It is government's responsibility to put in place the best policy framework for Canada and the financial system that's in the best long-term national interest -- in the interests of all Canadians.

I commend government on the basis of taking the time to thoroughly assess what is the single most important decision in Canada's modern financial history. By pre-empting much of the debate over the past nine months, unfortunately the mergers have sideswiped all other aspects of financial sector policy. This is not healthy -- it's not right -- and it's certainly not in the best interests of Canada.

Facts must guide government's decisions -- facts, not personalities -- facts, not rhetoric and public relations campaigns -- facts, not goodies and giveaways.

I commend, as well, Finance Minister Paul Martin and Minister Jim Peterson for staying focussed on the broader agenda, for undertaking full and comprehensive studies of all aspects of financial sector policy, and for ensuring that the interests of all Canadians will be taken into account.

I await with interest the MacKay report tomorrow, which will be one important input to government, along with reports from the Competition Bureau, the Finance Department and the Office of the Superintendent of Financial Institutions, along with input -- I hope -- and I encourage -- from a very broad range of Canadians.

Ladies and gentlemen, on one final note, especially to the Scotiabank customers here this afternoon, let me assure you that Scotiabank is and will continue to enjoy great success with or without mergers. Our strategy is clear, to stay focussed on you and to continue to build our commitment, and the service we provide, to communities here in Toronto and right across Canada, and to deliver consistent relationship-oriented service. And let me assure you, we appreciate your business.

Ladies and gentlemen -- thank you very much.