Economic Perspective 2

THE TSB AFTER INCORPORATION

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On 21 July 1986 the issue of ownership of the Trustee Savings Banks was finally settled with the vesting of the assets of the Trustee Savings Bank Central Board, the Trustee Savings Bank (Holdings) Ltd and the four regional Trustee Savings Banks in the TSB Group plc and the new regional TSB public limited companies, including TSB Scotland plc. The transfer had not been achieved without public controversy and acrimony but has now been settled beyond recall. The Trustees Savings Bank Central Board subsequently through an Offer for Sale sold shares in the TSB Group plc to the general public. After providing for free shares to qualifying employees, making allowance for loyalty bonus shares and after setting aside some £86m for the expenses of the issue, the offer for sale will raise an estimated £1,274m for the TSB Group plc when the shares are fully paid in September 1987. The offer for sale was heavily advertised and highly successful in that it was over-subscribed eight times and applications had either to be scaled down substantially or rejected. After the initial allotment the TSB Group plc had 3.1m shareholders; 1.3m customers and employees and 1.8m others, mainly individual shareolders as international demand was largely unmet. The shares rose to a substantial premium suggesting that the issue had been underpriced and with an unnecessary underwriting expense.

The new structure

The new structure of the organisation reflects to some degree the issues raised during the debate on the ownership and control of the Trustee Savings Banks concerning the independence of the regional banks after incorporation. Pressure arose mainly in Scotland for the maintenance of the separate identity and independent management of TSB Scotland. Such an assurance was given in a letter from the Chairman of the TSB Central Board to the Chancellor of the Exchequer. This independence has also been extended to the other regional TSBs with an assurance that the head office of each of the bank subsidiaries would remain in the territory in which it was incorporated. To protect independence representation on the Group Board is guaranteed for the Chairman and chief executive of the regional subsidiaries. In fact there are four TSB Scotland directors on the main Group board.

The regional boards are free to appoint their own directors and determine the senior positions on the board subject to Group approval. There is also a residential qualification requiring three quarters of the directors to be normally resident in the territory where the bank is incorporated. Directors are also enjoined to take the interests of bank customers and employees into account when taking decisions. Furthermore, limitations have been placed on the total dividends paid by the banking subsidiaries to the parent group, leaving the remainder to be utilised by the board of the subsidiary. A special majority of the subsidiary's board is necessary for any changes in the agreement to be made.

It is possible to argue that under the new structure the regional TSBs will enjoy at least as much freedom after incorporation as they enjoyed previously, although always ultimately controlled by the Group which holds all the shares in the operating companies.

TSB Foundations

Another attempt to maintain a link with the traditional Trustee Savings Bank's concern and involvement with the local community is through the setting up of TSB Foundations in each of the territories serviced by the regional banks. The boards of these Foundations will be appointed by the Group - one quarter - with the remainder appointed by the bank in the territory in which the Foundation is located. These TSB Foundations will support general charitable activities mainly within its own area. Financial support for these Foundations is to be provided from the profits of the TSB group, amounting to one third of one percent of the aggregate profits for the previous three years. The distribution to the Foundations, approximately £1,360,000 in the first year, is determined by a formula which gives 72.12% to the Foundation in England and Wales, 19.46% to Scotland, 5.35% to N Ireland and 3.07% to the Channel Islands. TSB Foundation in Scotland should receive some £264,000 in the first year. The Foundation also has the right to nominate two non-voting members to the appropriate TSB board.

As a result of the pressures exerted during the discussions leading up to incorporation, various measures have been introduced to maintain and develop the regional independence of the new TSB banks, without removing the ability of the Group board to determine overall performance and permitting the banking subsidiaries to reap the benefits of belonging to a national banking organisation.

Scottish pressure in the run-up to incorporation resulted in the TSB Group plc being registered in Scotland. This was merely a sop to the Scottish Lobby and has no practical significance as far as the control of the Group is concerned or the level of activity in Scotland.

Using the capital raised

Perhaps the dominant reason for seeking incorporation was to provide the bank with the ability to raise capital from the public should it be necessary. The successful Offer for Sale has demonstrated this ability with a vengeance, with the bank receiving some £650m with a similar amount to follow next September. The interesting question now is what is the Bank going to do with this vast fund of liquidity. The Prospectus provided little hard information on the likely use of the funds, beyond an estimated £300m which is expected to be spent over the next three years on the existing retail distribution network and on technology development. In addition, the geographical coverage of the bank will be extended. It is likely that this latter expenditure will be incurred in the South East of England where the bank has only limited representation. There will be expenditure in branch refurbishment and relocation in Scotland, but major branch expansion is unlikely in a market already well covered in a country regarded as being over-banked. Other areas where expansion and new products are mentioned is the life insurance and pension businesses. The TSB already has subsidiaries operating in these areas but more rapid expansion can be achieved by takeover. One possibility is that Scottish institutions may feature in the takeover options open to the TSB.

One of the areas where a recognised bank is expected to have expertise is in the foreign trade and finance sector. To enhance its new status the TSB may extend its present limited involvement in foreign business through takeover. Expansion into Europe at some future date is also an option mentioned in the prospectus. The scope for takeover activity is obviously enormous given the actual and prospective resources at its command and no doubt the City merger brokers are working hard at putting together attractive packages to entice the TSB.

Expansion of traditional business

It is the intention of the TSB to maintain its principal role in the personal finance sector where it has a large customer base. As with other banks the TSB is facing severe competition in the retail deposit market and has lost market share in competition with other deposit taking institutions - particularly the building societies. Growth in deposits in TSB Scotland has been relatively slow at 6% per annum in the 1980s compared to 12% for the TSB as a whole. In the personal sector deposit market TSB Scotland has also experienced slower growth than other Scottish banks. There have, however, been substantial changes over the years with a more than tenfold increase in advances to customers since 1980, from an admittedly low base. There is a move to attract more non-personal business, especially professional practice accounts and small to medium-sized company accounts. The TSB concentrates its corporate business in head offices, regional offices and specially selected branches where scarce specialist staff can be used to greatest effect. In addition, TSB Scotland has established a new team to compete in the venture capital market. It has recently purchased the estate agency Slater Hogg & Howison to support its personal lending in the mortgage market and has targeted the agricultural sector as a growth area. TSB Scotland also retains an ability to develop its own products and has achieved this successfully with the Business Plus Account - a high interest chequing account. It is currently developing a card based account as a major step towards automated banking. It has shown an ability to sustain a good profit record with a growth rate of 18% compound between 1980 and 1985, superior to that achieved by the Scottish and London Clearking banks and the TSB Group as a whole.

The funds raised by the share issue ensure that the TSB will grow. The direction in which the growth will take place is not clear, but the intention is to build on existing strengths whilst expanding in related areas. The role of TSB Scotland in this process is unclear. It retains the potential for a significant degree of independent development under the new structure. Its ability to secure a significant share in the funds available for investment apart from branch refurbishment and upgrading is more open to question, given the generally depressed state of the Scottish economy and the already competitive market in Scotland, and the fact that the activities targeted for expansion are not headquartered in Scotland. Scotland may attract some of the central services business which may arise from the rationalisation of existing activities. The recently announced decision to transfer routine processing activities from Glasgow to Manchester shows that this will not necessarily be a one-way process. In this case there is a reciprocal flow of development work to Glasgow from other parts of the Group which will provide an offset in employment terms, and may indeed offer greater long-term prospects.

The significance of the Scottish operations in the total Group operations is likely to diminish as the expanding TSB group undertakes new ventures, probably outside Scotland. However, TSB Scotland supported by expanding central services should be able to sustain its competitive position in the domestic market.