

## European consumer finance

# Missed opportunity for UK banks?

**Britain is home to the largest consumer credit market in Europe. But banks from elsewhere in Europe are leading the development of cross-border consumer finance. Where does this leave the UK banks?**

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In contrast to progress in the wholesale markets, the integration of European retail banking markets has made slow progress.

However, consumer finance is proving something of an exception. The €850bn European market remains far from integrated, with significant obstacles to seamless cross-border provision. But despite the obstacles, internationalisation is taking place at a faster pace across Europe than in other retail banking segments.

Most of the major banks in the eurozone are investing heavily in the market. Leading banks and specialist consumer finance providers are building multi-national businesses in Europe without waiting for an optimal environment in terms of regulation and infrastructure.

## 1. Market leaders

The largest French banks BNP Paribas and Crédit Agricole have pioneered cross-border expansion in Europe. Through their specialist consumer finance subsidiaries Cetelem (BNP Paribas) and Sofinco and Finaref (Crédit Agricole), they have built extensive (and highly profitable) networks covering all the major markets in Continental Europe.

They are also well established in the new markets of Central and Eastern Europe (CEE). Among their CEE businesses, Crédit Agricole owns Lukas, which it describes as the leader in consumer finance in Poland while Cetelem claims to lead the market in the Czech Republic, Hungary and Slovakia.

Banco Santander, the largest Spanish banking group, has also built a major European network through Santander Consumer Finance. Santander has focused on auto finance, and its network includes CC-Bank, the largest German non-captive auto finance company.

Together with the American companies, GE Consumer Finance (GE Money), which also operates across much of Europe, and Citigroup with its extensive retail network, these five companies comprise a 'top tier' of consumer providers across Europe.

Société Générale is following its French peers. Already a major player in the German and Italian markets, SocGen announced the launch of consumer finance businesses in four markets (Bulgaria, Greece, Portugal and Slovakia) during July and August alone.

Other large European banks now are following the lead of Banco Santander and the large French banks.

For example, though better known internationally for its investment banking operations, Deutsche Bank has identified consumer finance as a growth market. It is establishing a centre of competence for consumer finance in Italy, where it is already a major player through Prestitempo, and recently announced the acquisition of leading consumer finance company norisbank in its domestic German market.

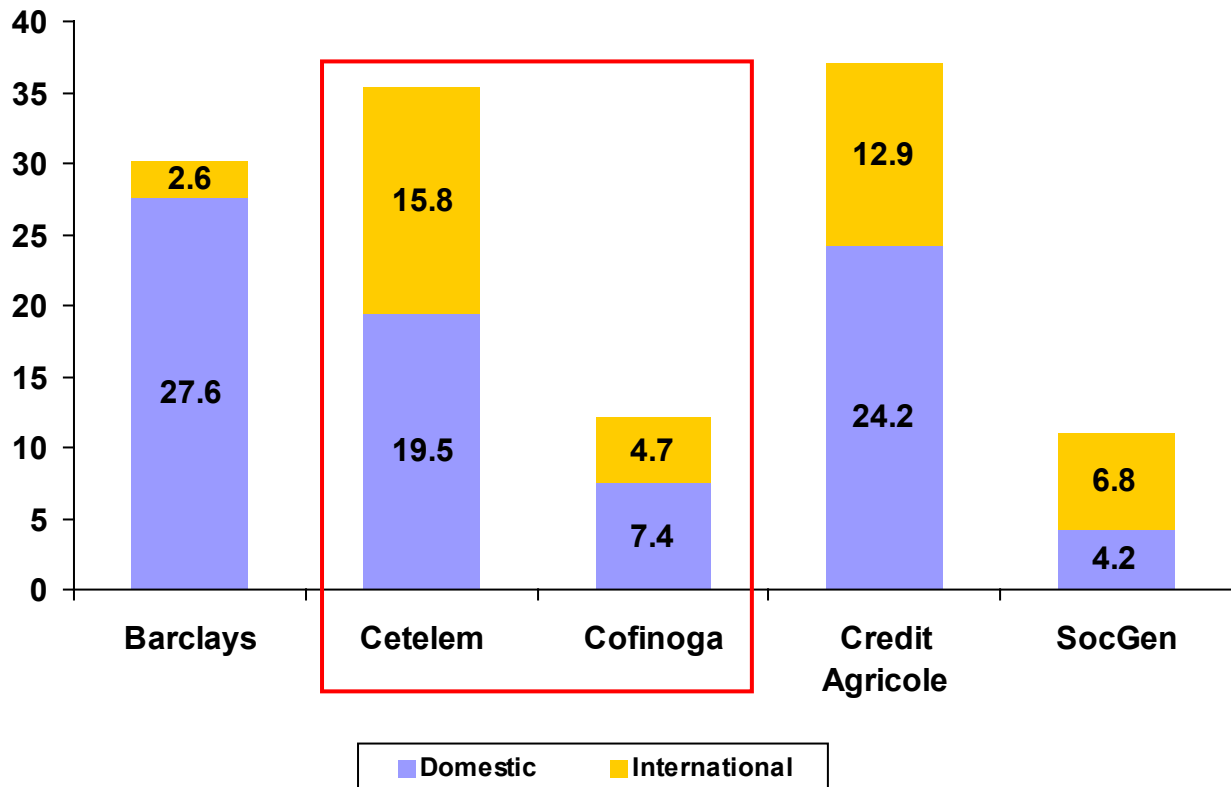
Alongside Deutsche Bank, BBVA, the second largest Spanish bank, Fortis, the large Belgo-Dutch banking group, and Nordea, the largest Nordic banking group, all announced ambitious plans during 2005 to grow their consumer finance operations.

## 2. Market attractions

Why the focus on consumer finance?

First, income from consumer loans and credit cards is already a significant contributor to overall retail banking income. Together, consumer loans (excluding mortgages) and credit cards accounted for approximately 25% of

Consumer finance: domestic vs international lending – 2005 (€bn)



Notes:

1. Figures cover loans outstanding. Figures focus on specialist consumer lending subsidiary / division but may not be fully consistent on the extent to which consumer lending through the retail network is included.
2. Figures may not be fully consistent because some are year average and some are year end.
3. International includes lending outside Europe.
4. Barclays – figures for Barclaycard. Domestic figures cover UK credit cards - average extended credit balances (£8.6bn) and UK loans - average consumer lending balances (£10.3bn). International figures cover average extended credit balances (£1.8bn). Converted into euros at average 2005 £/€ rate of 0.684 (Source: ECB).
5. Cetelem increased its stake in Cofinoga to 50% in early 2006.
6. Société Générale – figures for Société Générale Consumer Finance, excluding loans distributed by its French retail networks.

Sources: Banks and consumer finance companies

banking revenues from personal customers across the EU in 2004 according to a recent analysis by the European Commission.

Further, leading banks are attracted by the prospects for the sector:

- Growth prospects remain strong across much of Europe. In the eurozone, the annual growth rate in consumer credit reached 7.9% in 2005 according to the ECB. In the developing markets of Central and Eastern Europe, growth rates are much higher.
- At a European level, the consumer finance market remains fragmented, creating

opportunities to grow both organically and through acquisition.

- Interest margins are comparatively high in consumer finance compared with loans in other sectors.
- There is strong pressure to remove the remaining barriers to cross-border activity, with the implementation of SEPA (the Single Euro Payments Area) likely to stimulate cross-border activity
- Retail lending will be one of the major gainers under the new Basel II capital adequacy accord.

### 3. UK banks

The speed with which leading eurozone banks are building multi-national networks raises questions about the strategy of the major UK banks.

The large UK banks rank among the largest European consumer finance providers because their domestic market is the largest in Europe.

However, perhaps the size of their home market has left UK banks paying too little attention to expansion opportunities on the Continent. With the exception of HSBC (following its acquisition of Household in the US), UK banks' consumer finance activities are dominated by their domestic businesses. Their presence in mainland Europe remains modest. It is negligible in the fast growing CEE markets (where arguably the most active UK investor in consumer finance has been home credit specialist Provident Financial).

HBOS and Lloyds TSB have no significant presence on the Continent.

Barclays in contrast has not ignored European expansion. It has issued its Barclaycard in Germany for more than a decade and now issues its credit card in several European markets. Last year, it launched a Nordic joint venture with leading Swedish bank Swedbank. But compared with the leading French banks, Barclays' consumer finance business continues to be dominated by its domestic lending (see chart).

While international balances accounted for less than 10% of Barclaycard's lending in 2005, they accounted for approximately a third of Crédit

Agricole's consumer credit lending and over 40% of Cetelem's lending. Further, the French banks' international lending is growing much more quickly than their domestic lending.

One reason for the success of BNP Paribas, Crédit Agricole and Banco Santander in consumer finance is their expertise in working through intermediaries (retailers, car dealer networks and other distributors wanting to offer credit to their customers) as well as branches and direct channels. Like GE Consumer Finance, developing this essentially business-to-business market has been central to their foreign expansion.

Of the UK banks, RBS has made the largest investment in this segment of the market. It operates across several European countries through its Dutch-based 'Comfort Card' business. But Comfort Card remains small compared with a Cetelem or Sofinco.

UK banks are facing a much more challenging domestic consumer credit market:

- After years of heady expansion, growth is inevitably slowing.
- There are concerns about asset quality.
- Regulatory pressure is increasing on important revenue streams such as credit card default charges and commission from payment protection insurance (PPI).

As the domestic market becomes tougher, where do the UK banks look to for business growth in consumer finance? As they ponder the expansion achieved by European competitors, may they regret not making greater use of their expertise in consumer credit to build comparable networks?

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