Funding the Future

Better Banking

Published: January 15, 2026, 12:13 am

Compass and the New Economics Foundation — two organisations with whom I work — have published a report entitled Better Banking.

The whole text is reproduced here, because I think it important.

“Whatever the character and programme of the next Government, a precondition for its success will be reform of the UKâ€šÃ„Ã¼s financial sector which has made itself rich at the expense of an increasingly fragile economy. In the aftermath of the devastating recession and in the face of new challenges like climate change, the UK is facing a great transition to a new kind of economy.

This Manifesto puts the Great Banking Question at the heart of the election campaign and calls for root and branch reform. The next Government has no more urgent matter than controlling the banks and re- building the system in which they operate.

No party yet has a credible plan to re-engineer the financial system so that it becomes the socially and economically useful servant of the productive economy rather than the greedy master.

We have a once-in a lifetime opportunity to shake-up the provision of finance in the UK, making banks serve the needs of their customers rather than provide short-term gains for shareholders and cream off the profits for themselves.

Yet, so far this election campaign the Banking Question has been sidelined. Economic coverage has been dominated by the question of public spending cuts. Cause and consequence have been disconnected. But all the parties must engage with it in some detail if we are to transfer wealth creation from the few to the UK economy as a whole. The difficulties — complexity, global reach, virtualism — must not deter us. Here is how it could be done.

The core function of banking must be re-stated. **nef**'s definition of the core function of a financial system is to facilitate the allocation and deployment of economic resources over time and places across to environmentally and socially useful purposes. And, it needs to do this in ways that maximise long-term financial and social returns under conditions of uncertainty.

A fundamental aim should be simpler banking, because complexity increases the banker's clip and private fees along whilst adding to social risks and costs

Both wholesale and retail business models must be changed because dysfunctional behaviour is embedded in both.

1. Separate retail banking from speculation

Retail banking services are a utility function that sits uncomfortably with the high-rolling, risky activities of an investment bank, yet most of our high-street banks have moved into casino banking in search of quick profits. Banks should separate off their risky activities and insulate their retail services from the volatility of international capital markets. Mervyn King, governor of the Bank of England, has called for a separation of banks' activities. Investment banks could then be allowed to go bust — instilling greater discipline and avoiding “moral hazard,â€šÃ„Ã¼ — while taxpayers would stand behind the retail division. In the US, Barack Obama has proposed a ban on proprietary trading by retail banks — buying and selling securities with the bank's own money — as well as a cap on the size of financial institutions.

2. Break up banks that are â€šÃ„Ã²too big to fail’

Allowing banks that are two big to fail has created â€šÃ„Ã»moral hazardâ€šÃ„Ã¼ — with bankers pursuing high risk activities confident that the public will have to bail them out if things go wrong, unacceptable costs to the taxpayer, but it has also resulted in a banking system that fails millions of people.

A properly functioning financial system should deliver credit and payment services to individuals and businesses at a competitive price. But in the UK, there are currently three million people without a bank account and small businesses are being starved of capital. Those individuals without bank accounts are among the poorest tier of society and yet they are vulnerable to predatory lenders where they pay interest rates of up to 2,000 per cent a year. They also pay more for basic services such as gas and electricity through pre-payment meters. Small businesses complain of lack of access to capital and high rates charged for funds. The Bank of England reported on April 1 that credit availability for small businesses had not increased in the first three months of this year, but rates charged had risen slightly.

Banks need to be broken up both to reduce costs and risks to the taxpayer, and also to improve the quality and range of services. Our financial system needs to encourage a proliferation of credit sources, many of them small and local that will reach out to the community and provide loans and services that mainstream banks will not touch. These could build on existing credit unions as well as new initiatives by local councils to promote banking services to the local community. For example, a social investment bank could be linked to a local network of community development finance institutions. Mutual structures also need to be encouraged. There are successful examples of mutualisation, trustee savings, and co-operatives that should be strengthened and expanded as a viable, trusted and secure alternative to private banks.

3. Create a national Post Bank based on the existing Post Office network

Create a national Post Bank based on the existing Post Office network to address financial exclusion and provide real, fairly-priced competition in local communities. The Post Bank would be a trusted and accessible new option, reaching areas currently abandoned by the high street banks and attract customers with few alternatives. It would need some government funding but, for example, could be allocated some of the proceeds of the Robin Hood tax on international transactions.

4. Set up a Green Investment Bank

A new Green Investment Bank is required to channel finance towards developing the environmental infrastructure we need, enabling existing industry to go green and to build the skills to make Britain a world leader in the field. National energy security would be enhanced as well as our ability to tackle climate change. It would need to lend in such a way that regional inequalities are taking into account. It could be partly funded by selling long-term “environment” bonds to pension funds and other investors.

5. Launch a competition enquiry into the banks, that looks also at the role played by ratings agencies and accountancy firms

There is a desperate need for a competition inquiry into the tight cartel of banks that raise funds for the government and companies in the international capital markets. The financial crisis has led to many banks withdrawing from these markets so that the small group that dominates can set its own fees for what is essentially a commodity service. The fact that this is so lucrative was borne out by the large profits made by leading banks in this area - Goldman Sachs, for example, had one of its most profitable years ever last year - just a year on from the financial crisis that wrought havoc in the world economy. Ironically, many governments are selling bonds to finance the bank bail-outs required by that financial crisis! Investors are increasingly concerned about the charges imposed by banks on companies for raising funds and for mergers and acquisitions. An enquiry would also provide the opportunity to look in more detail at the shadowy role in the banking crisis of the ratings agencies and accountancy firms.

6. Introduce controls on bonuses

One development more than any other that has prompted public anger in the wake of the credit crisis, is the continued payment of bonuses to bankers who brought the system to its knees. While regulators have sought to restrict bonuses, calling on banks to pay them in shares and introduce claw back elements for failed bets, no- one has called for an outright ban. We believe that a bank that makes an overall loss or has been forced to bolster its capital over the year, should be banned from paying bonuses in that year's pay round. This would concentrate bankers' minds over the allocation of their capital - to protect the business rather than pay out in remuneration. It would therefore make the system safer. In light of the risky and divisive nature of the bonus culture we call for a 95 per cent tax on any bonuses that would take a yearâ€šÃ„Ã¼s remuneration for an individual employee beyond £1 million.

7. Introduce a financial transaction (or â€šÃ„Ã²Robin Hood’) tax

The IMF has proposed both a new levy on banks as well as a tax on profits and remuneration. But an automatic transactions tax has huge potential too. Just a small levy of 0.05 per cent on the billions of financial transactions taking place worldwide would raise billions of pounds. Some of this could be used to promote alternative sources of finance in the UK, for example in helping to capitalize the new Post Bank, as well as fund a green investment bank. A small tax would also throw some "grit" in the system and could be used to slow financial speculation that was one of the causes of the credit crunch.

8. Demand better regulation

An effective system of regulation needs to question institutions more and not accept the prevailing orthodoxy. The regulator needs to "lean against the wind." Just because banks told the regulator that financial innovation such as collateralised debt obligations spread risk and therefore made the system safer in the run-up to the crash, there was no reason to believe them. In fact, this meant that when the crisis occurred, risk had spread to every major institution in the world, causing a domino effect. Banks need to be forced to hold more capital, particularly in a boom when risks are greater. Better regulation needs to be counter-cyclical, preparing for bad times when things are going well, and scale-related, being much tougher on institutions whose behaviour can cause more damage.

We need to bring onto the balance sheet, rigorously check and officially license all “exoticâ€šÃ„Ã¼ financial instruments. Anyone trying to circumvent the rules by going offshore or onto the internet should face the simple and effective sanction of “negative enforcementâ€šÃ„Ã¼ — their contracts would be made unenforceable in law. Ultimately our aim is an orderly downsizing of the financial sector in relation to the rest of the economy. A UK Community Reinvestment Act should be brought in, which insists that banks lend money where they are prepared to take deposits, and - when they fail to do so — funnel investment from them via new community development financial institutions.

9. Bailouts are not free: bring-in a taxpayer â€šÃ„Ã²quid pro quo’

We are currently sleepwalking towards another crisis. The government bailed out the banks with staggering sums: £1.3 trillion at its peak . It has demanded only a few feeble reforms in return. These changes provide only a sticking plaster to the structure of the industry rather than a philosophical rethink. In future help for banks in trouble must be linked to commensurate controls. Adair Turner, head of the Financial Services Authority, has said;"British citizens will be burdened for many years with either higher taxes or cuts in public services - because of an economic crisis whose origins lay in the financial system, a crisis cooked up in trading rooms where not just a few, but many people earned annual bonuses equal to a lifetime's earnings of some of those now suffering the consequences."

10. Introduce a Universal Banking Obligation

There must be a Universal Banking Obligation which covers both location and a banking code covering the principles of fair charges.

Banks are deeply unpopular with the public and — not only since the current credit crisis. In recent years high street banks have made huge profits from their retail customers - billions of pounds in overdraft and credit card charges. At the same time, banks have retreated from their expensive, but popular, high-street branches, closing almost a fifth in the past 10 years. Britain now has just over 200 branches per million people compared with 500 in Germany and 1,000 in Spain.

Conclusion

Britain's banks have retreated from their core function of supporting socially and economically useful activity, in pursuit of consolidation, international expansion and short-term profit. This has made our financial system unresponsive to the needs of many ordinary people and unable to provide the boost to industry required to pull the UK out of recession.

Banks have abandoned much of the â€šÃ„Ã»relationship bankingâ€šÃ„Ã¼ which allocated loans to small start-ups and local businesses, preferring instead a crude credit-scoring approach. They have also boosted their profit margins by concentrating on large loans to big companies rather than helping small businesses.

We believe it is vital to institute far-reaching reform of our banks rather than tinkering around the edges. This is the only way to try and head off another financial disaster. A key feature of our approach is to draw on lessons from corners of the financial system that are outside the mainstream such as community and social finance. Many of these institutions have weathered the crisis well and reach areas that our traditional banks have abandoned.”