

# Corporate & Investment Banking

## A Challenging Way Ahead

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(Version 3)



#### Disclaimer

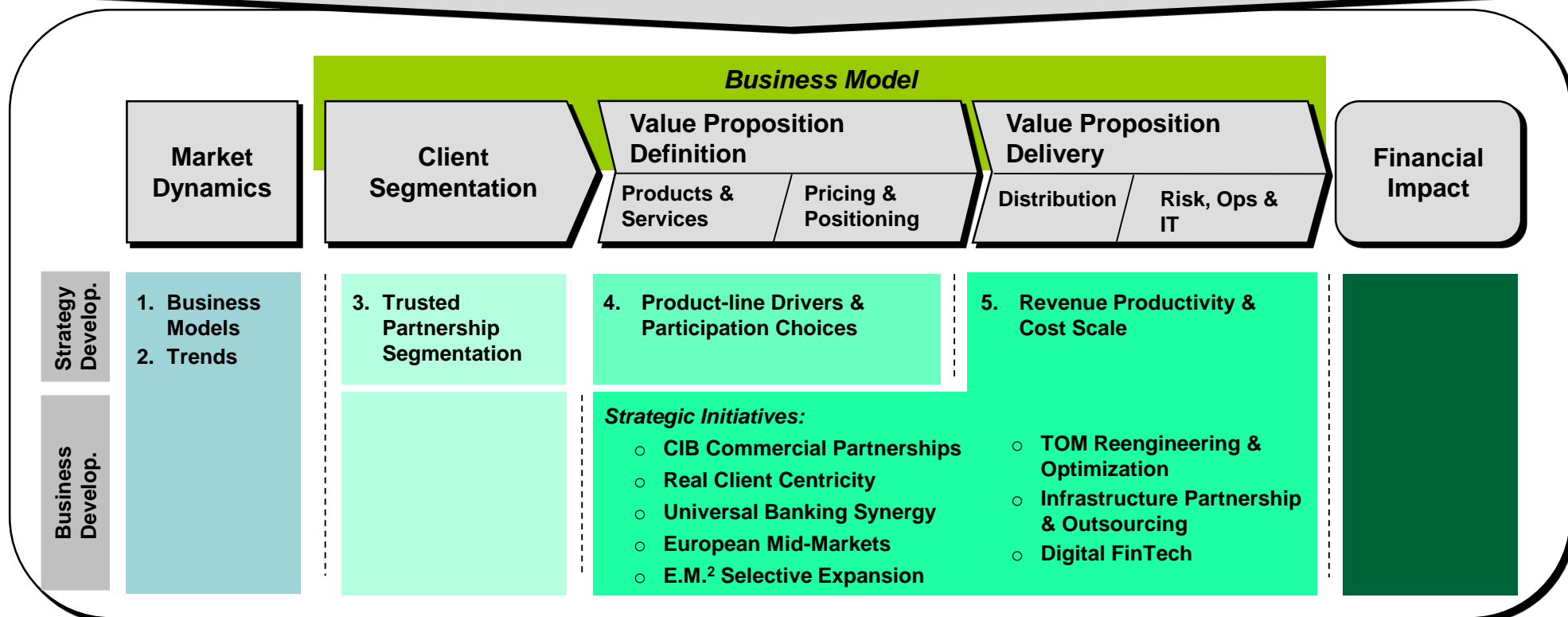
- **The objective of this paper is to provide a high-level, external reflexion on strategy & execution questions in the context of current industry trends in Corporate & Investment Banking.**
- **It is intended for an informal conversation without the benefit of internal information.**
- **This work has been done entirely independently by the authors based on publicly available information and reports of financial analysts. Any error/omission entirely the authors' responsibility.**

# A review of Corporate & Investment Banking industry’s 2 major challenges, through the Business Model framework, provides “food-for-thought” on 5 key Strategy & Execution topics

## CIB Banking Industry<sup>1</sup> – Major Challenges

1. CIB profitability, despite all the RWA and cost cutting so far, is still under question for a majority of players (RoEs < CoEs)

2. Banks have struggled to make bold participation choices to date, substantially impacting their Revenue & Cost structures

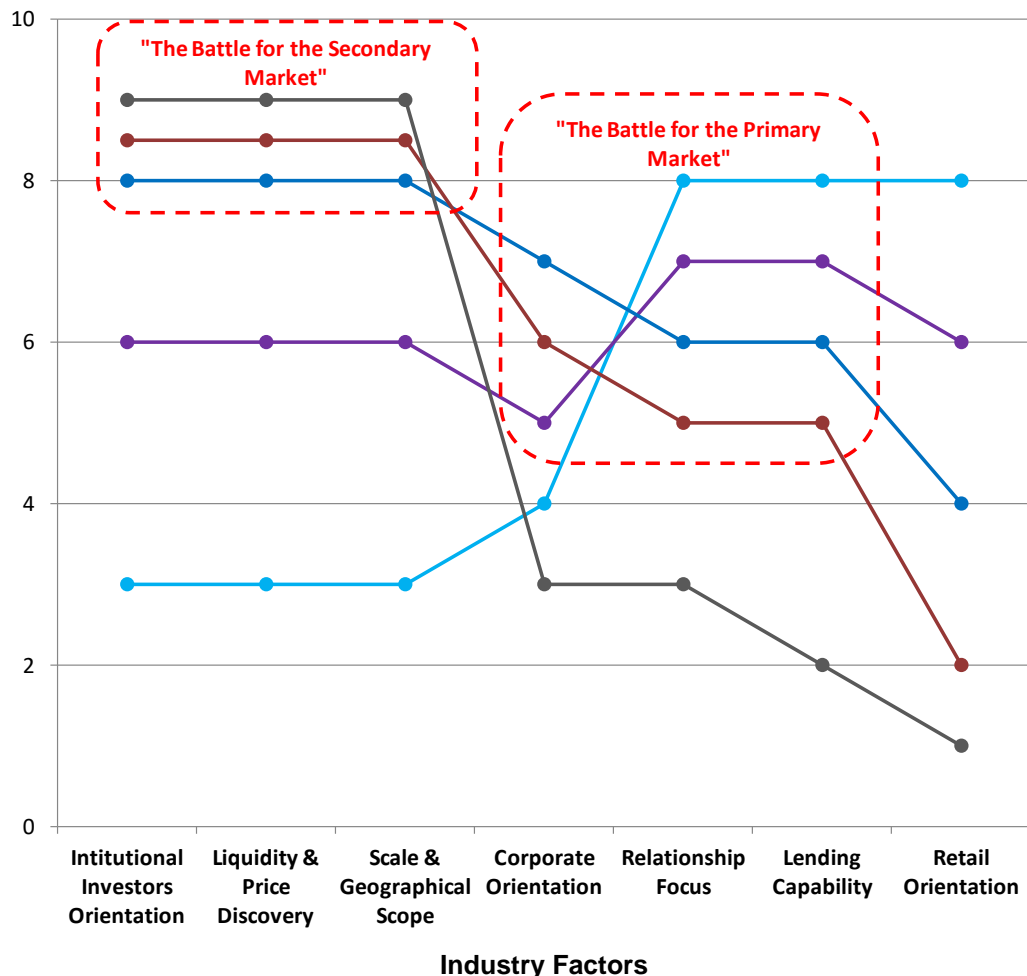


1. Corporate & Investment Banking; 2. Emerging Markets  
 Sources: McKinsey; BCG; Morgan Stanley; Oliver Wyman; own analysis

1 MARKET DYNAMICS – BUSINESS MODELS

**Banks have been evolving towards 5 distinctive business models, along 2 trade-offs: (a) global vs local, and (b) investor vs corporate vs retail orientation**

Strategy Canvas<sup>1</sup> – Corporate & Investment Banking



CIB Business Models

- Regional/Local Corp.Bank**
  - Strong retail in 1 region or 1 country, with a min. level of local CIB skills
  - Examples: LBG, DZ Bank, CaixaBank, Mediobanca, Credit Mutuel, Nordea,...
- Multiregional Universal**
  - Strong retail in at least 2 regions, with a strong level of CIB capability
  - Examples: Santander, Standard Chartered, RBC, ANZ,...
- Global CIB & Local Universal**
  - Global CIB coverage, with strong retail presence, at least, in home country
  - Examples: Deutsche Bank, Citi, BoA, JP Morgan, CS, UBS, Barclays, BNP...
- Global CIB Specialist**
  - Global CIB coverage, none or very low retail dedication
  - Examples: Goldman Sachs, Morgan Stanley, Nomura, Natixis, Daiwa...
- CIB Infrastructure Providers**
  - Players specialized in CIB infrastructure
  - Examples: BNY Mellon, State Street...

Two battles under way, with Global CIBs (Local Universals vs Specialists) playing in both

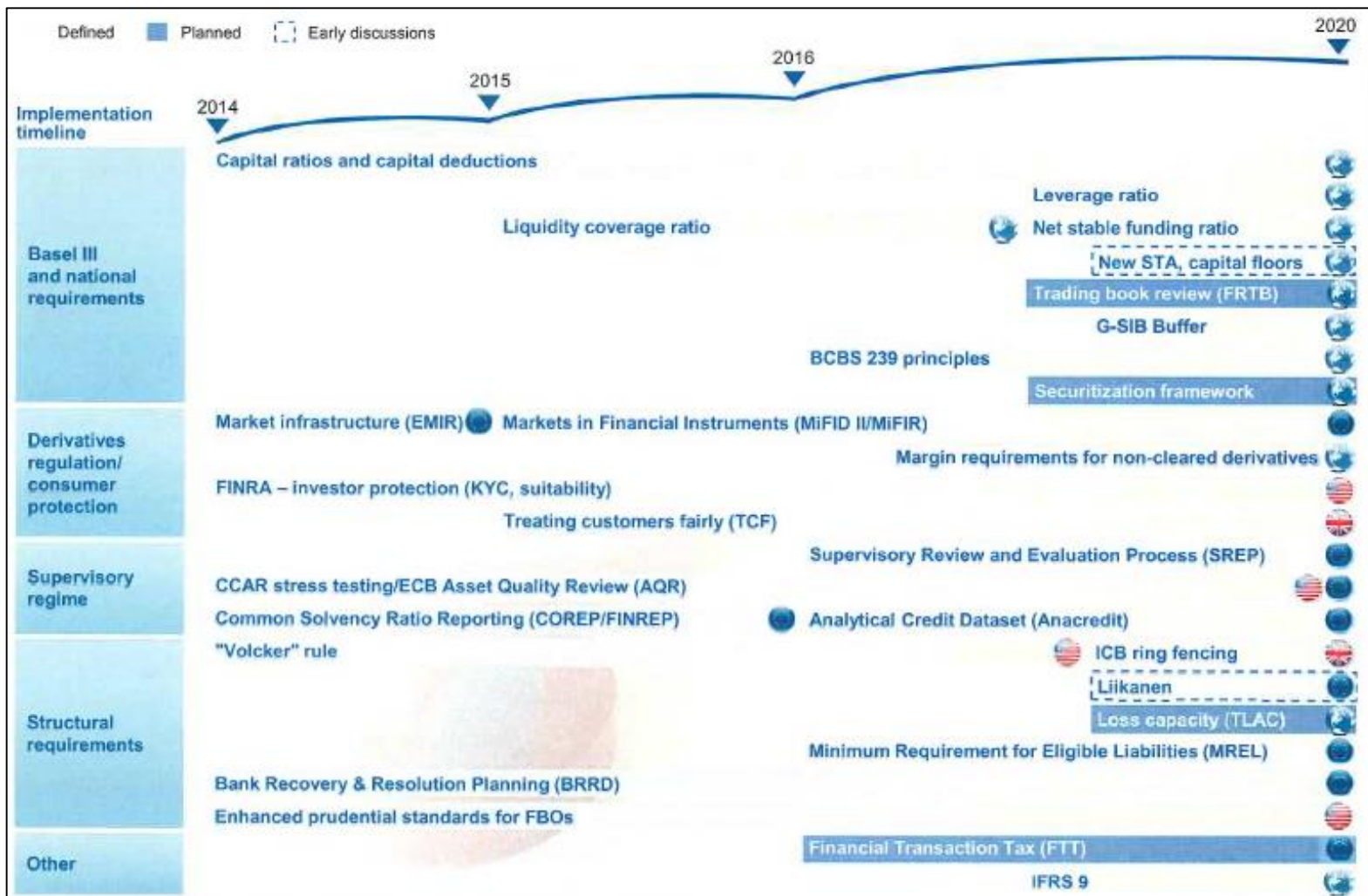
Note: ref. to Appendix for more detail on the "Battle for the Primary Market"

1. Strategy canvas is a Blue Ocean Strategy methodology that visualizes the value curves of each competitor or competitor groups based on key industry factors that determine the industry competitiveness 3

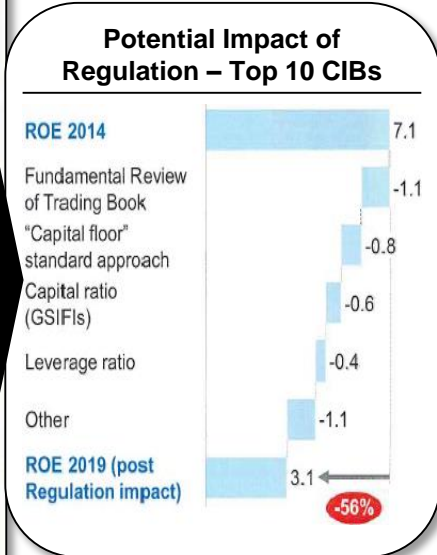
Sources: "Blue Ocean Strategy" (W. Chan Kim / R.Mauborgne, 2005); "The Future of Banking" (McKinsey, Apr.12); own analysis

2 MARKET DYNAMICS – TRENDS (1/2)

The banking industry is barely half-way through the avalanche of regulation expected till 2020, which is estimated will halve RoEs of Top-10 CIBs to barely c.3% (before management actions)



**NOT EXHAUSTIVE**

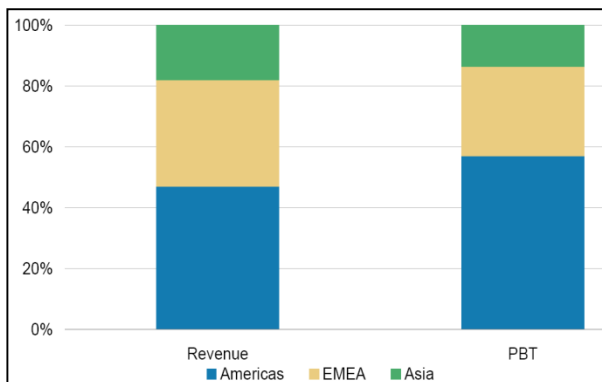


# Models will continue under heavy testing: (1) regionalization affecting portfolio participation, (2) market share redistribution from battles for primary/secondary markets and (3) RWA & cost cuts

## Business Model

### Client Segmentation – Portfolio Participation Decisions

CIB – Revenues & PBT (2012)

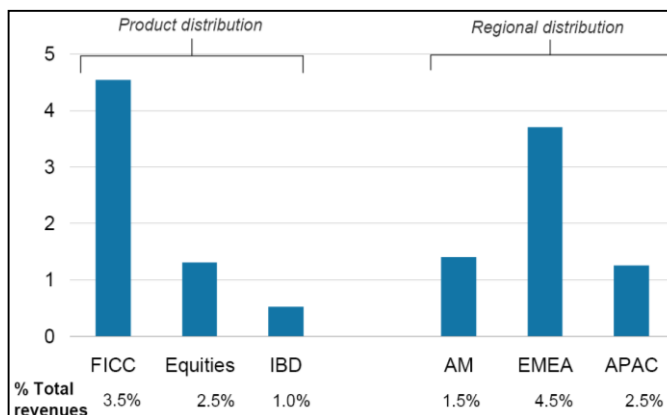


- **US as critical market to sustain a Global CIB model:** it concentrates 45-55% of Revenues & PBT which, along its growth momentum, drives scalability.
- **Strong regionalization:** most investors focus volumes on their home regions (70-75% for large, 80-95% for small investors).
- **Scale & operating leverage** are now key:
  - FICC: trend towards “flow monsters”
  - Equities / Investment Banking: trend to cut high cost base underneath weak economics

### Value Proposition Definition

Products & Services / Pricing & Positioning

CIB – Revenue Sacrificed from Exits (2012, \$bn)

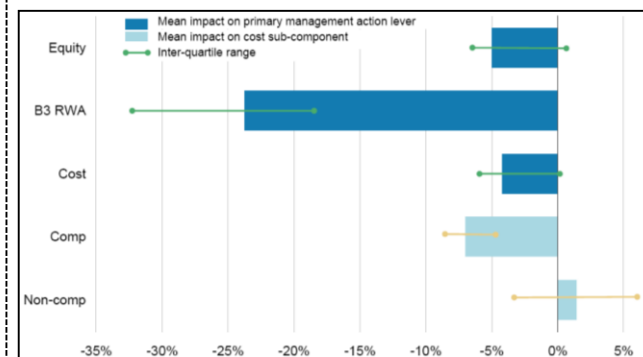


- **Rapid market share redistribution:** 1-3.5% depending on product line.
- **Battle of Primary Markets<sup>1</sup>:** attrition war, with Global CIB & Local Universal banks losing market share gradually to Regional/Local Corporate Banks in DCM, and CIB Specialists in M&A/ECM.
- **Battle of Secondary Markets:** affecting all Sales & Trading businesses, where investors concentrate spend with 3-4 dealers, who end up making 80% of their revenues from just 500-800 clients.

### Value Proposition Delivery

Distribution / Risk, Ops & IT

CIB – Equity, RWA & Cost Reductions (2011-12)



- **Evolving focus of cuts:** from RWAs (20-25% till 2012), to operational costs (2013 onwards).
- **Evolving operational cost reduction:** from easy-wins (i.e. compensation, discretionary expend), to in-depth re-engineering<sup>2</sup>:
  - Front-office & functional organizational alignment (5-10%)
  - Front-office / back-office alignment (5-10%)
  - Operational model optimization (10-15%)

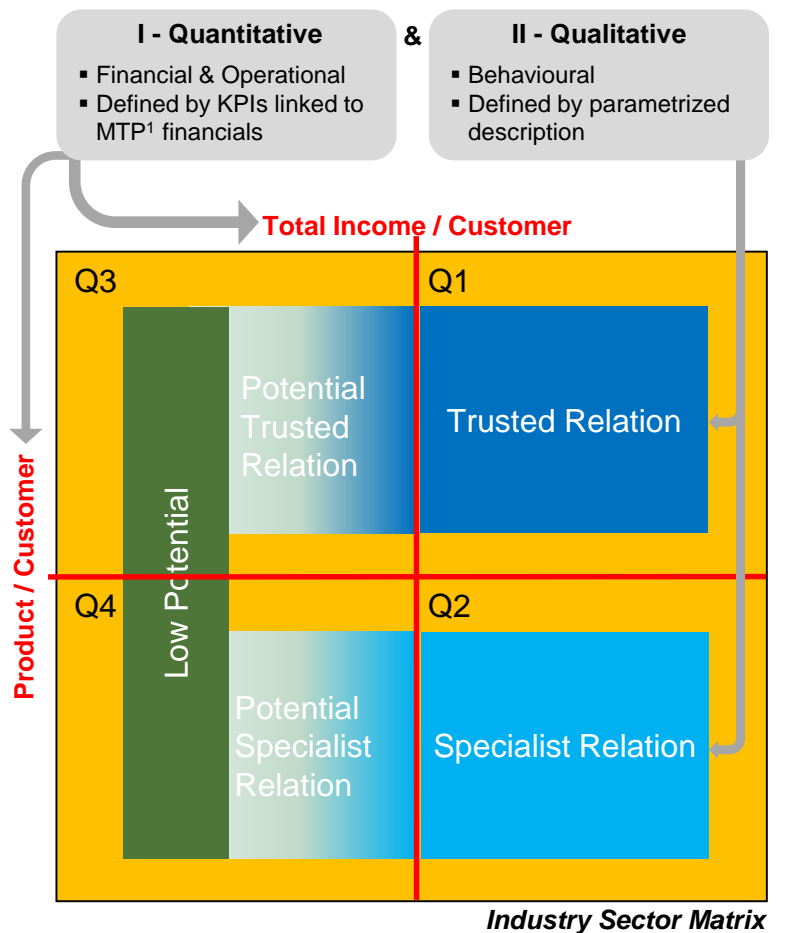
1. Ref. to Appendix; 2. Estimates of cost reduction potential in parenthesis

Sources: “Wholesale & Investment Banking Outlook: Global Banking Fractures – The Implications” (Morgan Stanley / Oliver Wyman, Apr.13); own analysis

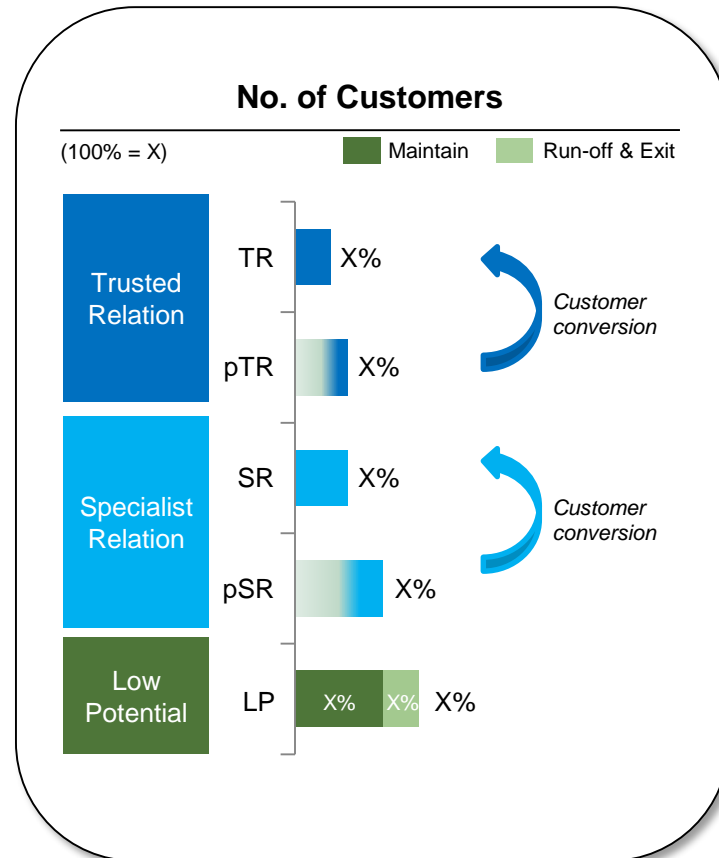
3 CLIENT SEGMENTATION – TRUSTED PARTNERSHIP SEGMENTATION

CIBs need to focus on their core customer franchise adopting a quantitative & qualitative segmentation approach and managing their portfolios towards customer conversion

Segmentation Model



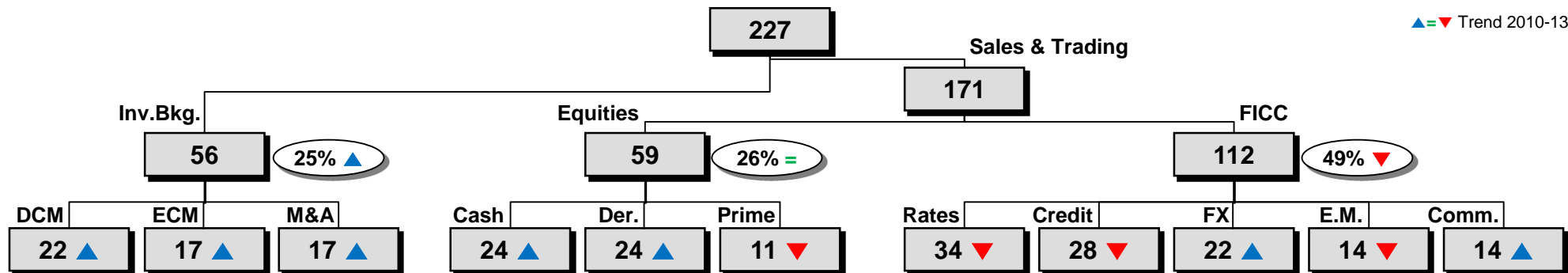
Portfolio Characterisation



4 VALUE PROPOSITION – PRODUCT LINE DRIVERS & PARTICIPATION CHOICES

All product lines are under radical transformation, obliging CIBs to take high-stakes participation choices along geography, corporate/investor client franchise and product mix

CIB – Global Revenue Pools (£bn, rounded, 2013)



▲=▼ Trend 2010-13

Product Line Drivers

- Bank disintermediation drives up DCM from Corporates in Europe and Asia
- Corporates gradually make use of excess cash for acquisitions

- Prime subsidization of Cash and Research finished
- Moderate shift to electronic trading

- FICC subsidization of Corporate Banking finished
- Reduced capability for rates & credit liquidity provision
- Huge shift to electronic trading (FX: 70%; Rates: 50%)

- War for OTC infrastructure for across all Sales & Trading:
  - Value moves from execution to post-trade (CCP/client clearing, collateral mgmt./transformation, margin lending)
  - Affects \$60-75bn of S&T revenues, expecting to decline \$5-10bn driven by 5-20% volume reduction
  - Shortfall of \$1.4tr. in collateral expected by 2018

Participation Choices

**Geography Coverage:**

- US for foreign CIB:** deepen or exit
- Europe:** optimization of fragmented markets
- Asia & MEA:** local vs hub vs exit

**Client Franchise – Corporates:**

- CEO-led agenda:** industry content excellence, capital markets distribution
- CFO-led agenda:** financing & hedging, transaction services

**Client Franchise – Investors:**

- Equities-only vs FICC-only vs both**
- Traditional broker vs Clearing broker vs Integrated broker**

**Product Mix:**

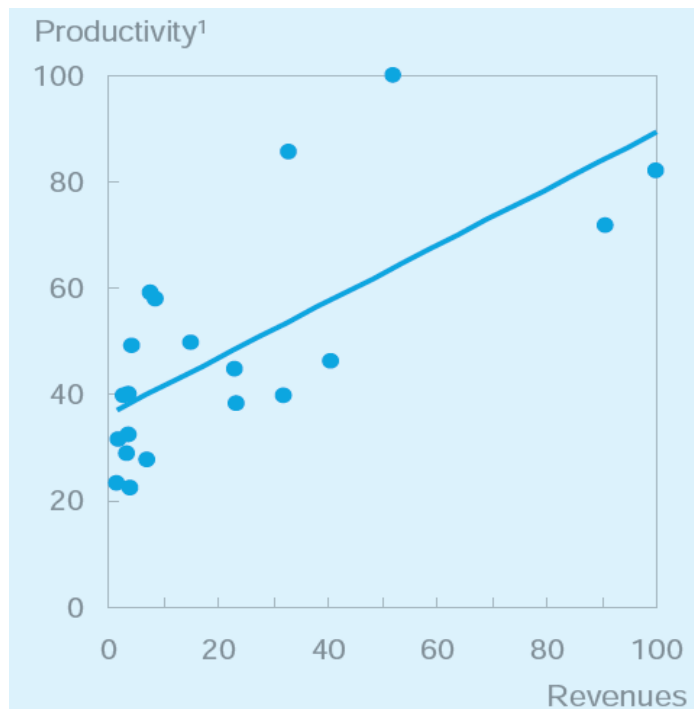
- Advisory & Research:** many exits
- Illiquid Trading & Risk Mgmt.:** many exits
- Flow Trading:** consolidation
- Treasury & Risk Mgmt.:** kept selectively
- Emerging Markets:** locals win



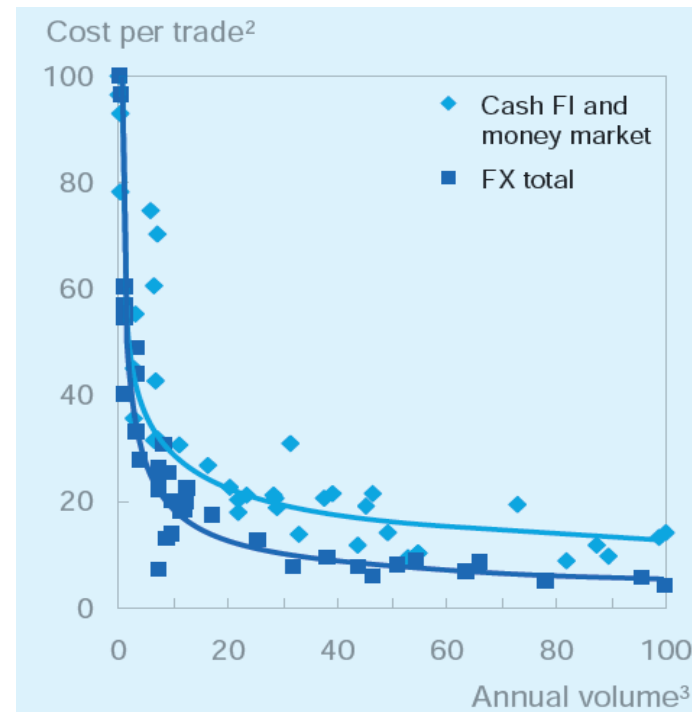
5 VALUE PROPOSITION – REVENUE PRODUCTIVITY & COST SCALE (1/2)

This transformation requires the selection of strategic initiatives to deliver higher revenue productivity & bigger cost scale,...

Revenue Productivity



Cost Scale



▪ Need of strategic initiatives to expand market share & share of wallet

▪ Need of strategic initiatives to optimize platform and secure more volume

1. Revenues per FTE; 2. Middle-office, back-office, IT and third-party costs; 3. Number of front-office trades per year  
Sources: "The triple transformation: achieving a sustainable business model" (McK, Oct.12); own analysis

5 VALUE PROPOSITION – REVENUE PRODUCTIVITY & COST SCALE (2/2)

... for which 8 potential areas of opportunity arise

Revenue Productivity

Strategic Initiatives	Description
1 <b>CIB Commercial Partnerships</b>	<ul style="list-style-type: none"> <li>Expand market share by providing:                             <ul style="list-style-type: none"> <li>a) overall CIB product to local/national players</li> <li>b) complementary product to CIB specialized players</li> </ul> </li> </ul>
2 <b>Real Client Centricity</b>	<ul style="list-style-type: none"> <li>Develop robust analytical tools &amp; big data focused on: cost-to-serve, behaviour modelling, real-time MIS to client and relationship profitability</li> <li>Measure holistic client satisfaction across the organization</li> <li>Upscale talent towards true client service with uncompromised values &amp; compliance</li> </ul>
3 <b>Universal Banking Synergy</b>	<ul style="list-style-type: none"> <li>Real delivery of often elusive synergies:                             <ul style="list-style-type: none"> <li>a) Lending: holistic cross-selling</li> <li>b) Transaction Bkg.: holistic e-portal</li> <li>c) Servicing/Clearing: single collateral mgt.</li> <li>d) Treasury: A&amp;L mgmt. / FI reciprocity</li> <li>e) Wealth: product design &amp; distribution</li> </ul> </li> </ul>
4 <b>European Mid-Markets</b>	<ul style="list-style-type: none"> <li>Extension of CIB coverage to MidCorps<sup>1</sup> for some product lines to develop capital markets/direct lending access to investors</li> </ul>
5 <b>E.M. Selective Expansion</b>	<ul style="list-style-type: none"> <li>Increase of share of wallet within selected Emerging Market geographies with enough potential</li> </ul>

Cost Scale

Strategic Initiatives	Description
6 <b>TOM Reengineering &amp; Optimization</b>	<ul style="list-style-type: none"> <li>Estimated 65% of cost base is firm-specific, but can be optimized along 3 axis:                             <ul style="list-style-type: none"> <li>a) Asset-class specific costs (20%): Front-office IT, price engines,...</li> <li>b) Cross-asset common costs (20%): e-channel, collateral management,...</li> <li>c) Cross-divisional costs (25%): CRM, payments, treasury IT,...</li> </ul> </li> <li>Develop an internal capability for best-practice process reengineering across COO areas</li> </ul>
7 <b>Infrastructure Partnerships &amp; Outsourcing</b>	<ul style="list-style-type: none"> <li>Estimated 35% of cost base is industry-related: KYC, IT databases, reconciliations, settlement,...</li> <li>Study and execute externalization of some processes:                             <ul style="list-style-type: none"> <li>a) Partnerships with other CIB market players</li> <li>b) 3<sup>rd</sup> party utility providers (IT vendors, BPOs, clearing houses,...)</li> </ul> </li> </ul>
8 <b>Digital FinTech</b>	<ul style="list-style-type: none"> <li>Corporate Bkg.: digital credit &amp; SC<sup>2</sup> analytics for high speed &amp; efficiency</li> <li>Sales &amp; Trading: blockchain has the potential to revolutionize back-offices</li> </ul>

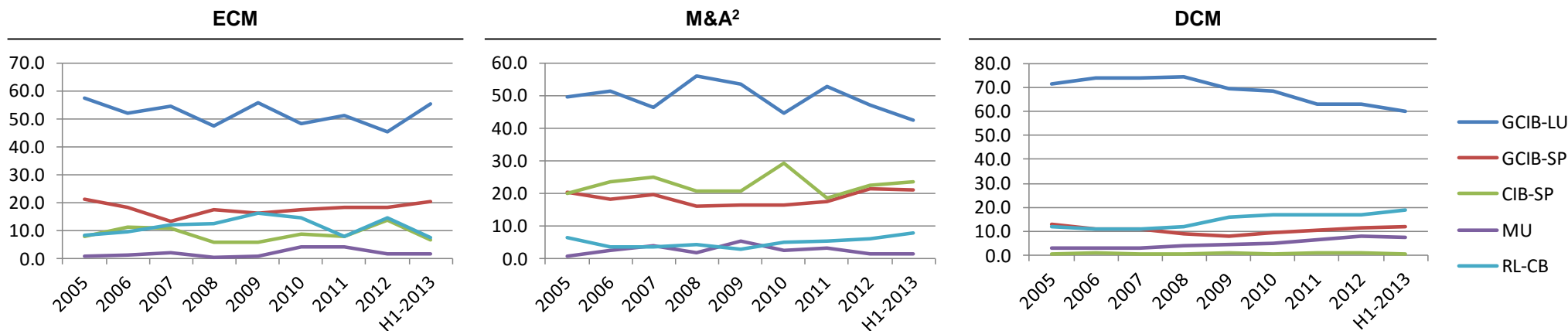
1. MidCorps defined as corporates with turnovers between £25m and £500m; 2. Supply Chain

Sources: "Trends in Corporate & Investment Banking" (McKinsey, Dec. 15) ; "The Quest for Revenue Growth" (BCG, May 14); "The triple transformation: achieving a sustainable business model" (McK, Oct. 12)

## 1. THE BATTLE FOR THE PRIMARY MARKET

## Global CIB & Local Universal banks' leadership has been gradually eroded by CIB Specialists in M&A/ECM and by Regional/Local Corporate banks in DCM

European Investment Banking Revenue Market Share by CIB Business Model Group (2005-1H13, %)<sup>1</sup>



- **Global CIB & Local Universal banks command market shares, however with a downward trend** for all of them (M&A: from peak 57% to 42% (12); ECM: from 58% to 46%; DCM: from 74% to 63%).
- **Global CIB Specialists have broadly kept their market shares stable** across the whole period for the 3 areas (average c.18% in ECM and M&A, 10% in DCM... range within +/-2%).
- **CIB Specialists and Regional/Local Corporate Banks have been gradually eroding GCIB-LU leadership:**
  - For M&A and ECM, the latter's downward trend looks zig-zag, reverse-mirroring the market share of CIB Specialists (M&A: from 20% (05) to 23% (12); ECM: from 8% (05) to 14% (12))
  - For DCM, it looks smooth, reverse-mirroring the market shares of RL-CBs (from 12% (05) to 19% (12)).
- **Multiregional Universals are practically out of the game**, with avg. market shares below 5% across

Note: GCIB-LU (Global CIB & Local Universal) / GCIB-SP (Global CIB & Specialist) / CIB-SP<sup>1</sup> (non-Global CIB & Specialist) / MU (Multiregional Universal) / RL-CB (Regional/Local Corporate Bank)  
 1. Ref. pg.5, for this analysis, GCIB-SP has been split in CIB-SP to include many midsize specialist banks very common in ECM and M&A rankings, but that are much smaller and regional than GCIB-SP; 2. M&A market shares are published with overlap of bookrunners, so they have been normalized to sum up 100%  
 Sources: Thomson Reuters database; own analysis