FINER

EMPOWERING TRANSFORMATION

May 2017

EUROGROUP CONSULTING

European Banks: Competing in an Uncertain Geopolitical Environment - Caution is required!

By
Pierre
REBOUL

The European Union currently faces many political and economic pressures, including slow growth (1.3% forecasted for 2017) and persistently high unemployment in many countries, as well as the rise of populist right-wing political parties. For the first time in our history, in an increasingly multipolar world, many are becoming openly anti-European or Eurosceptic. USA President Trump's arrival on the world stage has been met with widespread anxiety in Europe. Many fear that his "America First" rhetoric, skepticism toward multilateral institutions and enthusiasm for Brexit signals a disengagement from the rules-based order that most Europeans consider the bedrock of their prosperity and security.

The new dynamics at work in the US Administration have caused a great deal of uncertainty within the European finance and banking market. The first step was the nomination of Carl Icahn, responsible for slashing regulations on business, as special adviser and many other former senior Wall Street executives, notably a number of ex-bankers from Goldman Sachs such as chief strategist Steve Bannon and Treasury Secretary Steven Mnuchin. The second step was the signature of an executive order aimed at repealing the Dodd-Frank legislation, which was a key component of the broad global regulatory overhaul resulting from the 2008 financial crisis. Eurozone policy makers are concerned about the proposed USA retreat from the Basel bank capital rules, which would be very dangerous as loosening capital rules when central banks are running loose monetary policies would replicate the conditions that led to the global financial crisis. It would also create an un-level playing field between the USA and European financial institutions, fueling demands for protection. The outcome of these actions would be further damaging fragmentation of the global financial system, and potential market erosion for the EU banks. However, despite business leaders in the USA being optimistic over Trump's sweeping pledges for pro-growth policies, some banks and corporates are delaying their next big decisions to see how his proposals take shape, and whether his administration can actually turn them into laws.

However were cracks beginning to appear in the global model of bank regulation even before Trump signed the aforementioned executive order, with the Brexit and EU dislocation developments only exacerbated by Trump? Upon the news that the UK will be leaving the European Union, movements have taken place in many other European nations to examine whether EU membership is in their best interest. Since the Brexit vote, it appears that the relationship between the USA and UK has been strengthened and many have questioned whether we are witnessing the beginning of the end of the EU, especially after Trump announced he will strike a favorable USA-UK trade deal after Brexit. Outside the EU, the USA is currently the UK's biggest export market, with 20% of UK goods and services sent there, equivalent to 6% of UK GDP.

The EU faces several challenges in 2017, in particular the elections being held in France and Germany, where populist right-wing parties are threatening to cause Brexit or Trump-style upsets to the existing order. Europe's key 2017 elections will take place with France in April and May, and Germany in September. In addition, the UK has now called a snap election for June, but the outcome is likely to keep the existing pro-Brexit Conservatives party in power. These two elections could prove to be severely destabilizing for other parts of the EU, including Italy and Greece that are already facing an accelerating pace of capital outflows and are suffering from severe strains in their banking system, as well as the Eastern Europe EU members that may become disillusioned by the whole EU project. And if these countries do elect far-right candidates, it could plunge the EU into uncertainty and financial volatility, especially considering France and Germany are the 2 main pillars of the EU (providing 37% of the EU's GDP).

With so many contradictory forces at the moment, it is hard to foresee the future. More than ever collaboration and togetherness are urged, rather than for example an EU vs joint USA & UK relationship that would not be beneficial for all parties involved. A world with a hard Brexit or where each bank reverts to their own country for core business would be very troubling. For example,
in the UK's case the financial services sector is precious and annually earns approximately GBP 190-205bn in revenues, employs 1.1million people and has total assets of GBP 20 trillion as of 2015, within which GBP 40-50bn of the revenue amount is business related to the EU. Vice-versa it must not be forgotten that the EU finance and banking sector is still very prominent within the global economy, and comprises a huge wealth of assets. At the end of 2015 the total assets of the overall Euro area financial services sector stood at about EUR 68.5 trillion, of which EUR 27.7 trillion was attributed to the banking sector. Furthermore the relative size of the overall Euro area financial sector has increased between 2008 and 2015, from 5.3 to about 6.1 times GDP.
France and Germany have bank assets that amount to 350-400% of their GDP, whereas in the USA it is equal to just over 100% of GDP. EU businesses will have an interest in retaining access to the UK as an international financial centre, not only for the services provided directly but also as a conduit for global investment into the EU. Within all this, one matter is guaranteed, it certainly promises to be an interesting 2017!

Cross Border Mass Payments: Take it or leave it!

By
Michel
RUCHTI

It seems banks are losing their touch with the payments market. Newcomers are challenging their monopoly on the activity, which still represents 40% of their revenues. Global payments volume will continue to increase, but the unit price is constantly decreasing – at the same time as banks suffer from their high structural costs and have to put up with their slow and complex process.

The payment market is growing and its volume will continue to rise, fed by the boom in international business. Related revenues have been growing at a rate that exceeds all expectations. From $1.7 trillion in 2014, it is expected to reach $2.3 trillion by 2019. While this growth remains strong, structural changes are challenging historical actors. DSP2 impacts the regulatory framework in Europe. The existing cross-border infrastructures remain slow, expensive and difficult to push forward. New non-bank actors are forcing entry into the market: GAFAs that rely on a large customer base, and digital start-ups with a substantial technological lead or simply a rule-changing approach to service delivery. If the banking sector wants to remain at the heart of the payment process, an effective strategy has to be put into place.

While the sector has mostly focused its attention on shifts within the domestic payments ecosystem, **opportunities associated with cross border payments have generally been overlooked**. This specific market is growing and its volume will continue to rise by 8% a year over the next 5 years, fed by the boom of international business and travel. It already generated $300 billion in revenue in 2015. It is expected to climb from 5% of total payment revenue in 2013-2014 to 14% by 2014-2019. The B-to-B market is based on high-value payments and mostly remains the exclusive preserve of a few happy global banks, competing to capture the business of regional players.

In this context, **cross border mass payments will be the next battle for banks**. To this day, processes and back-end systems remain slow, not very transparent, difficult to track as well as expensive. Customers' expectations are growing, and newcomers on the scene are ready to meet their demands. This means the payments will have to be cheaper and faster. As a result, banks will have no choice but to rethink their strategy to remain in this growing market.

However, banks cannot be too fast and cheap when building their own infrastructures on all country-currency links.

They will have to specialise **through a concentration on specific "country-currency payment corridors" consistent with their client base**. Banks should not waste energy nor money to develop systems with a limited utility and no power of differentiation. For example, BNP developed a high-profile US$ corridor to the US through Bank of the West and BIAT built a niche corridor between France and Tunisia. Now they are marketing the use of these highly efficient corridors to partner banks to increase volumes and revenues.

For non strategic corridors, in order to offer a high level of service at a minimum cost, two different and potentially compatible strategies can be contemplated:

- **A fruitful alliance, with one of the promising payment fintech companies**: rely on their outstanding understanding of new technologies (e.g.: blockchain), supply customer base and brand, in order to leverage new payment channels, bypassing outdated infrastructures, to offer top-notch services at a minimal price.

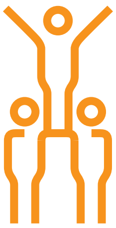
- **Outsourcing of payment pipes**, in order to offer efficient and cost-effective services without large investments. Whether within an alliance with other banks or new actors, it can be smoothly implemented, perhaps even within existing environments. This option can be considered for all cross-border payments or limited to low-priority corridors.

One thing is certain: no actor can afford to sit tight until further notice, because the technology gap is widening and newcomers are rapidly conquering customers and market shares. The two market drivers are price and speed. Banks are currently at a crossroads: either they address the challenge resolutely to offer the expected service, or they will be pushed out of the market. Failing to adapt will ensure that the payment market is left to the innovative non-banking actors.

Managerial Innovation: A new deal

By
Cécile
JEHANNO

When stress increases, motivation decreases. Over the last 10 years, the percentage of employees that complain about high levels of stress has risen from 40% to 61%. Studies show that 40% of managers are perceived by their teams as not innovative enough, and 50% of them do not support the development of their teams enough.
According to Harvard and MIT, happy employees are two times less sick, six times less absent, nine times more loyal, 31% more productive and 55% more creative.
"The Freedom Form Company", "Managerial Bankruptcy", and "Lost in Management" are the latest titles in the Management sections of bookstores. Are these perhaps the weak signals of the emergence of another form of management?



Managerial innovation consists in finding new answers to questions that have been raised for years, such as:
- How to develop more agility and freedom?
- How to increase enjoyment and wellbeing at work?
- How to establish trust-based relationships?
- How to develop creativity and innovation?
- How to improve commitment and loyalty?
- How to strengthen sense of responsibility and independence?

Managerial innovation is defined by its differences with what is considered classical management, i.e. structural-functional hierarchical management (one structure, one function, one manager) in control/command mode (orders and control systems). Anything that breaks with the classical model, through disruption or evolution, is considered to be managerial innovation.

Current managerial innovation places collaborative work at the core of people's concerns and enterprise performance issues. Control systems are increasingly costly and complex and generate new forms of bureaucracy. Societal demand is changing. Employees want to participate more and no longer accept a position of passive obedience. The call for innovation and the quest for wellbeing are leading work relations to be viewed differently.

Today, HR Departments and teams in charge of innovation are focusing on the subject and wish to coach business lines and managers to help them become better agents of change, better communicators, with a more collaborative approach in the way they manage, and undertake peer-to-peer exchanges.

- To do this, it is necessary to work **both on disruptive innovations** in order to think outside the box, and to address **everyday** managerial innovation needs and **continuous improvement** of management methods.
- To durably transform the managerial innovation culture, it is essential to be able to experiment and test multiple approaches, draw lessons, apply them to other situations when relevant, and renounce when necessary. This capacity to "sow seeds" in the organization is a success factor.
- To legitimize managerial innovations over the long term, it is good to acquire tools to measure the changes wanted. Measuring also allows you to adjust the systems you implement if required.

We coach our customers in these experimentations: some are designed to "disrupt" the managerial paradigm, others, more continuous, to support and transform practices:
- Managerial Innovation Hackathons
- Lab' / Innovation room
- Deployment of innovative practices: peer-to-peer feedback
- Digital workshops to enable dialog 2.0 and give managers tools
- Exchange of best practices with managerial co-development and learning networks, etc.

Authors

Pierre REBOUL
Partner | Member of Executive Committee - Eurogroup Consulting
pierre.reboul@eurogroupconsulting.fr

Before joining Eurogroup Consulting as member of the Executive Committee, Pierre was a Senior Partner at a strategy consulting firm where he headed the « Corporate & Investment Banking – Asset and Wealth Management » practice globally. Pierre is a graduate from Massachussetts Institute of Technology. As a specialist in investment banking and technology, he has overseen a large number projects aimed at optimising finance and risk oversight, improving operational performance and sales efficiency, and transforming information systems.

Cécile JEHANNO
Partner | Eurogroup consulting
cecile.jehanno@eurogroupconsulting.fr

For more than 18 years, Cecile has been advising financial institutions on driving and improving their major transformation projects. She has developed an expertise mainly in the retail banking on change management and managerial innovation issues. She is part of the Eurogroup Consulting Managerial Innovation Think Thank, with ESSEC Business School.

About

TRICUMEN
Bespoke Analysis of the Financial Markets

Tricumen provides bespoke analysis of the financial markets. An offer for actionable intelligence on performance, organisational structures, business models and working practices.

The firm leverages its core staff by drawing on a global network of research partners.
Their permanent staff are almost exclusively drawn from the industry and have unrivalled knowledge of financial products and the working of the markets.

Tricumen's research centres near Cambridge in the UK and in Croatia and administrative office is in London.

Further Reading

An experimental think tank on new ways of managing
ESSEC Business School, in partnership with Eurogroup Consulting, launches the new Managerial Innovation and Operational Excellence Chair. The objective of this new research chair define and implement new forms of management which will serve to shape the business of the future. It will organize events throughout the year such as conferences, learning expeditions and international meetings. The chair will also develop teaching and academic resources and carry out research-action projects with a team of associate researchers, particularly regarding issues of technology, neuroscience and managerial capacity.
For any additional information, please visit www.essec.edu

www.eurogroupconsulting.fr
www.linkedin.com/company/eurogroup-consulting-france
www.twitter.com/EurogroupFR
www.youtube.com/user/EUROGROUPCONSULTING
www.nextcontinent.net

Our Network

35 offices covering 29 countries

AACHEN
ABU DHABI
AMSTERDAM
BANGKOK
BARCELONA
BRUSSELS
BUCHAREST
BUENOS AIRES
CASABLANCA
DETROIT
FRANKFURT
HAMBOURG
HO CHI MINH
JAKARTA
KUALA LUMPUR
LISBON
LONDON
LOS ANGELES
LUXEMBOURG
MADRID
MANILA
MEXICO CITY
MILAN
MONTREAL
NEW DELHI
PARIS
ROMA
SAN FRANCISCO
SAO PAULO
SHANGHAI
SINGAPORE
STUTTGART
TUNIS
VIENNA
YANGON

nextcontinent