Get global. Get specialized. Or get out.
Moderator: Suzanne Dence
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Suzanne Dence: Hi, this is Suzanne Dence, Industry Leader for Financial Markets for IBM’s Institute for Business Value.

Wendy Feller: And this is Wendy Feller, the Global Financial Services Sector Lead for the Institute for Business Value. Suzanne and I are very excited to share some insights with you from our latest study on the globalization of financial markets entitled Get global. Get specialized. Or get out. And what we’re going to do today is tag team a little bit, and ask each other questions, really interview each other about some of the findings of the study.

So just to begin, Suzanne, let me ask you a question on how you actually came about putting the study together, and some of the background of the study.

Suzanne Dence: Yes, sure. Well for starters, we always go out and do a bunch of interviews to understand what the burning issues are for executives to make sure that we get the topic right. And interestingly this time around when we do these interviews, executives wanted to understand a fundamental question, how can we make money from globalization? So we set out to answer four fundamental questions as part of the scope and approach for this study.

First question, where will capital pools emerge? So looking at sources of capital, and how they're shifting across the geographies.

Second question, what will clients pay a premium for? Interestingly, and somewhat disturbingly, executives do not know the answer to this question.

Third question, how will the bases for competition evolve? So of course the competitive instinct coming in here, we wanted to look at winners versus losers.

And last but certainly not least, this is a viewpoint through year 2025, and we wanted to make some practical recommendations about organizational designs on behalf of firms.

So we partnered with the economist intelligence unit as part of this research, and we'll get into a little bit more detail as to what exactly we partnered with them for. And the scope of this is fairly broad, we cast a wide net looking at financial markets industry participants across asset managers, broker dealers, processors, as well as key regulatory bodies that support the financial market system, and also leading academics as well.

So this is a truly global study, goes without saying it is the topic of globalization. But we achieved one-third Americas, one third EMEA, and one third Asia Pacific as well.

So with that by way of background, I’m going to ask you, Wendy, what did you learn?
Wendy Feller: Thanks, Suzanne, that's a great question. So to begin with, to your point, we set out to answer the question how will financial markets organizations make money or profit from globalization? And what we've found is that it is a good, bad and ugly story. So to begin with the good.

What we found after sifting through 35 national economies is that globalization presents a huge opportunity for financial markets, and 95 percent of executives believe globalization truly is an opportunity. Worldwide investable assets, defined as debt and equity assets, are expected to nearly double by 2015 to nearly 300 trillion, and quintuple by 2025 to close to 700 trillion. And just to put this in context, that is almost two times the worldwide GDP, so it's actually expanding at a pretty fast clip.

However, we found this as the opportunity won't be found in all the same places, 60 percent of future growth is expected to come from the prospect or emerging markets. And what we believe is that this will go beyond brick to countries like South Korea, Turkey, Poland, Mexico, Indonesia. So firms need to be looking in new places.

Secondly, the bad, while 95 percent of executives believe globalization is an opportunity, 93 percent say their firms are unprepared, and it really revolves around a few different dimensions. First they're not able to put the science behind art to quantify the opportunity. Secondly they don't understand what their clients will pay for, and third they feel constrained by today's rigid and headquarter centric organization.

So what's behind the ugly? It's really how are firms responding? What we found is that executives are saying they're only pretending it to be global, and they're competing with a me too strategy, they're hurting over to China for revenues, and India for costs. Thus we asked ourselves the questions, are executives making the right bets? And what can firms do going forward? And the answer, which we're going to describe in much more detail later, describes in the title becoming specialized and becoming globally integrated.

So next, Suzanne, I wanted to ask you the question, what are some of the unexpected lessons we found through the study?

Suzanne Dence: Sure, well for starters, just to recap what you mentioned, which is we were very surprised to the degree of the opportunity, just the sheer size of the opportunity, and the fact that it will be found in some unusual places. But the real surprise here is how organizations are not prepared to take advantage of the opportunity, where nine out of 10 firms believe that they're unprepared, and rank themselves as moderate to poor on multiple operating model capabilities. So size of the opportunity, but then also the lack of preparation on behalf of firms.

The second unexpected lesson is the real disconnects that we found with respect to what the firms think their clients will pay for. So we asked the clients, what will you pay your financial services provider a premium for? Then we asked the firms, what do you think your clients will pay for? And out of 12 categories, the firms only got it right three times, and these category ranged everything from superior client service to execution to performance. So clearly there's a disconnect there, and that issue is just going to be exacerbated where the number one reason firms cited behind going global is to broaden
The third unexpected lesson has to do with business models, the business models that most firms believe is best may actually not be the right bet. Where interestingly we found there's a bit of schizophrenia going on in the industry, where over 60 percent of executives voted for the universal banks in terms of the business model most likely to succeed in a more global economy.

Now at the same time, we asked a slightly different question, and asked what are the top drivers of shareholder value creation? And they pick specialist capabilities, things like agility, and client service, they picked the specialist organizations above and beyond the universal banks in four out of six categories. We then took this a final step further and we quantified, we did a battle between the universal bank versus the specialist organizations, and we found that on two dimensions, one revenue growth, and two average operating margin over the past decade, it's the specialist organizations that have far outperformed the universal banks. And that's not to say that past performance is necessarily indicative of future expected returns, but that does beg the question whether organizations really have the business model right.

And just to be clear, universal banks we're defining as organizations that have a very large retail footprint, as well as a large institutional footprint, so you can think of firms such as (JP&C), Citigroup, but also other organizations such as the Deutsche Bank, for example.

And last but not least, the importance of culture we've found has been somewhat underestimated throughout all of this, culture was cited both as the number one barrier to profiting from globalization, but also as the number one enabler to profiting from globalization. So we found that organizations will minds, and Wendy will get into the findings in a little bit more detail here. But win minds both externally and also internally in order to take advantage of the importance of culture.

So going to ask Wendy a couple of questions here. Why is globalization occurring? And then I mentioned this, and I started to hint at the recommendations, what are the recommendations that we found in the study?

Wendy Feller: Thank you, Suzanne, great question. So, you know, I've been asked this a couple of times, which is why is globalization occurring, and why is it occurring so quickly? And it really boils down to one major factor with a couple different components sitting beneath it, and that is sophistication of the markets. What we've found is that if we break that down, there are two primary factors, the first being socioeconomic factors that have to do with the regulatory system, political stability and legal structure. So real aspects like financial liberalization, how open is the banking sector, what's the quality of the regulatory system, et cetera.

The second factor really has to do with what we're calling connectivity, and we can define this as things like transportation and communications infrastructure that will drive speed and transparency across markets.

So not only is that driving the speed of globalization, but what we've seen is that in the past, financial markets organizations have had the profits to go it alone. And they've been
able to profit in the big domestic markets, but as these profit pools really become more competitive, they're going to need to look elsewhere for higher margins, they're no longer going to be able to just innovate to avoid the commoditization trap in the big dominant markets.

So we have actually seen - again I talked about a 60 percent growth expected to come from prospect or emerging markets, part of what's driving this is a shift from deposits to security assets as countries do become more sophisticated. And what we see is by 2025, the security to deposit ratio in prospect markets will be much closer to the typical veteran market profile. So if you take China as an example, the compound annual growth rate for securities will be 17 percent, versus 11 percent for things like the - assets like deposits, so you're almost seeing this leapfrog effect in securities investing.

And what we've seen is that countries are learning from the other bigger dominant markets on the need to educate investors, and how, and really this starts with transparency.

So you asked also about what are the recommendations for organizations going forward? And we break it down into four primary recommendations. First organizations need to align their portfolio with the emerging revenue pools, that means know which markets to enter with which products at which time, and as we said up front, it needs to be more science, less hurting.

The second piece is about really becoming much more extroverted. And we think extroverts will be those that will really capture the dominant share of value going forward.

But first of all they need to become much more - two aspects to this, much more closer to the clients. As Suzanne outlined, there are significant disconnects between what clients want and what their providers think they want.

Secondly they need to reconsider their role in the industry, and this has to do with really understanding how to specialize around what your clients want. Third factor is they need to re-calibrate their operating model; they need to learn how to leverage global assets, things like talent or partnerships, or new sources of innovation. But also be able to dynamically assemble and disassemble capabilities, and be much more open in their collaboration models, which will help them to drive innovation. Many executives have pointed out the need to ask themselves whether today's peers will be their friends versus foes.

And lastly, as Suzanne mentioned, firms really need to win minds. Culture was cited again as the number one barrier and enabler to profit from globalization and a big aspect of this is really developing a global management team.

So again, Suzanne, I'd like to ask you one final question, which is when you looked at this study in developing it, how did you see that it actually differed from other studies coming out on globalization?

Suzanne Dence: Well we are very careful with our topics, and we did a scan in terms of what research is out there, both academic and also from other organizations. And we found that this study is fairly unique in that it approaches globalization on two levels, one from a macro level, and two from a micro level. And what do I mean by that? From a
macro level, we did work with the economists and built a forecasting model to make significant projections out through year 2025, we also looked at globalization of things like talent pools of market infrastructure.

So we tackled it at that very high level with respect to the macro orientation of the study. But then at the same time, we combined that when we realized that firms just are not prepared to profit from globalization, we realize we had to tackle it at the micro level as well, so we got pretty detailed in terms of making practical recommendations in how firms must redesign their organizations in order to actually profit from globalization, becoming truly global instead of pretending to be global.

Well thank you everyone for listening in today, we hope you enjoyed this Podcast. You can access the study at www.ibm.com/industries/financialmarkets/getglobal, and feel free to contact with Wendy Feller or Suzanne Dence, myself, for additional information. Thank you very much again for your participation.