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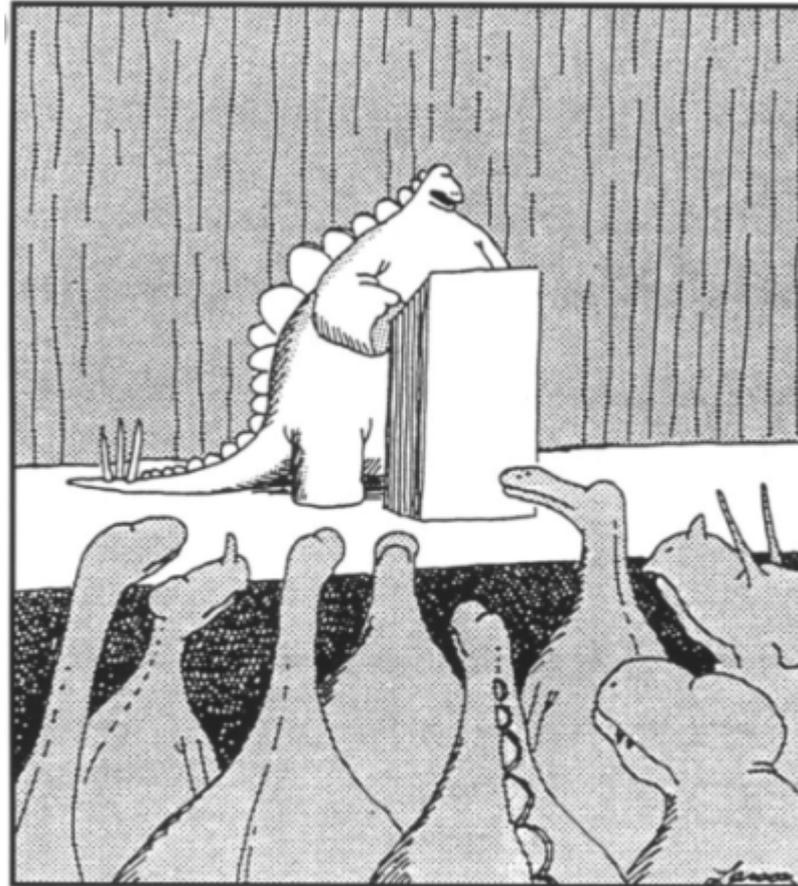
# Chairing a Bankosaurus

Has the meteor landed,  
or can banks evolve and survive.

Howard Davies,  
Chairman, Royal Bank of Scotland  
21 May 2018

# What should banks do to respond?

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"The picture's pretty bleak, gentlemen. ...  
The world's climates are changing, the mammals  
are taking over, and we all have a brain  
about the size of a walnut."

# Presentation structure

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1. How global banking has changed since the crisis
2. What has happened to capital, valuations and profitability?
3. What are now the main competitive threats to banks business models?
4. Can banks respond, or are they dinosaurs in a world hit by a fintech meteor?

# 1. How has global banking changed since the crisis?

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- the relative scale of Western and Eastern banks has changed a lot
- European and British banks have retrenched
- in spite of the effective ban on acquisitions, and of new entrants, concentration in Western markets has been stable or growing

# World's largest Banks by Total Assets (\$bn)

## December 2008

Dec-2008			
#	Institution	Country	Total Assets (\$bn)
1	Royal Bank of Scotland	UK	3,515
2	Barclays	UK	3,004
3	Deutsche Bank	Germany	2,896
4	BNP Paribas	France	2,729
5	HSBC	UK	2,527
6	JP Morgan	US	2,175
7	Credit Agricole	France	2,174
8	Citigroup	US	1,938
9	Mitsubishi UFJ	Japan	1,922
10	ING Group	Netherlands	1,858
<b>Total</b>			<b>24,739</b>

## December 2016

Dec-2016			
#	Institution	Country	Total Assets (\$bn)
1	Industrial & Commercial Bank of China	China	3,473
2	China Construction Bank	China	3,016
3	Agricultural Bank of China	China	2,816
4	Bank of China	China	2,604
5	Mitsubishi UFJ	Japan	2,589
6	JP Morgan	US	2,490
7	HSBC	UK	2,374
8	BNP Paribas	EU	2,190
9	Bank of America	US	2,187
10	Wells Fargo	US	1,930
<b>Total</b>			<b>25,669</b>

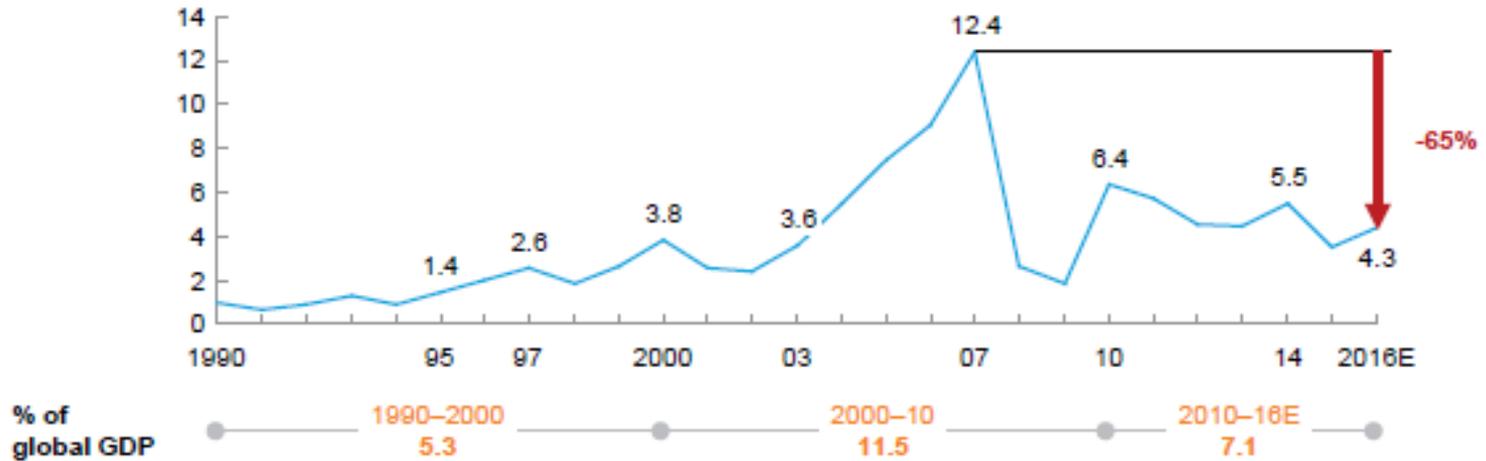
# UK and European banks have retrenched

No. G-SIBs	Region	Change 2007-15				
		Total assets	Capital	Home	Region	World
10	Euro area	-19%	1.80%	1%	1%	-2%
8	United States	10%	2.70%	5%	-3%	-2%
4	China	218%	1.60%	-3%	2%	1%
5	United Kingdom	-34%	2.90%	4%	-8%	4%
3	Japan	40%	1.00%	-8%	4%	4%
2	Switzerland	-45%	3.10%	7%	-7%	0%
1	Sweden	23%	0.40%	-7%	4%	3%
33	Total	5%	2.70%	9%	-4%	-5%

# Cross-border financial flows have declined

Global cross-border capital flows have declined 65 percent since the 2007 peak

Global cross-border capital flows<sup>1</sup>  
\$ trillion

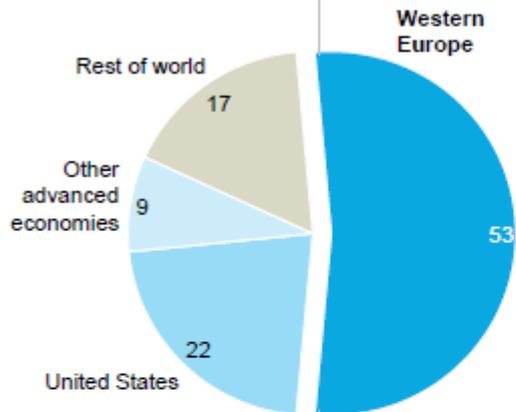


<sup>1</sup> Gross capital inflows, including foreign direct investment (FDI), debt securities, equity, and lending and other investment.

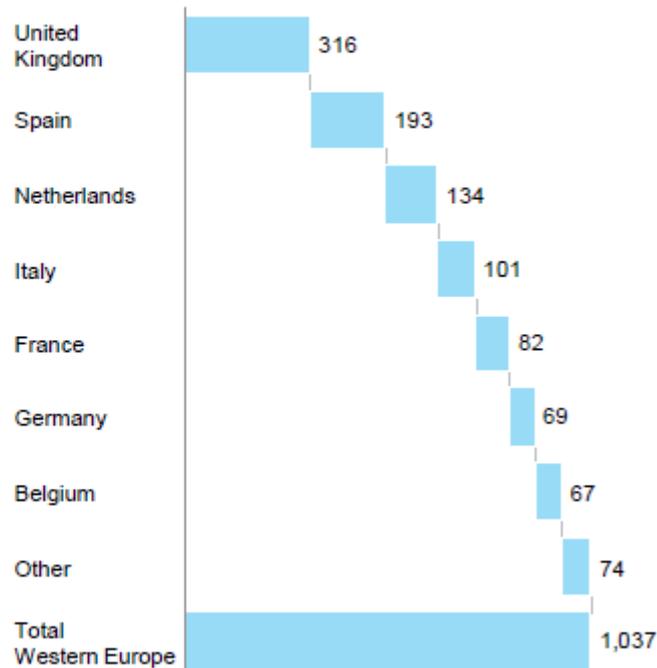
# They have divested assets on a large scale

Divestitures, January 2007–December 2016<sup>1</sup>

Cumulative deal value  
100% = \$1.96 trillion

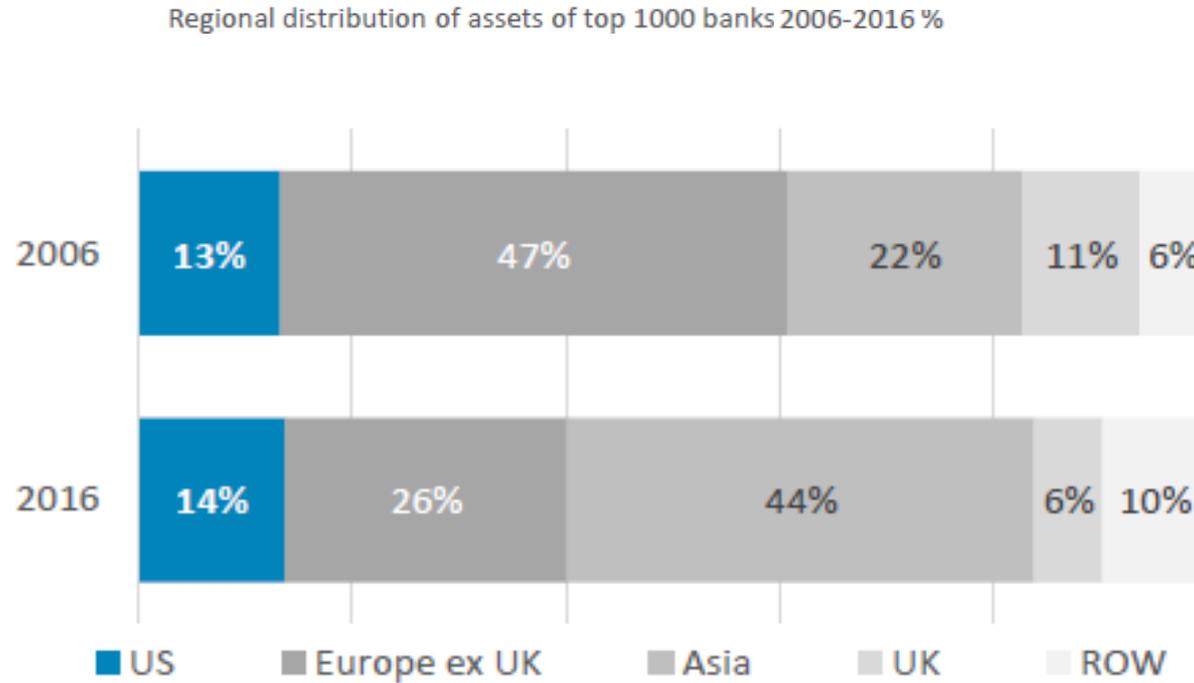


Cumulative deal value in Western Europe  
\$ billion

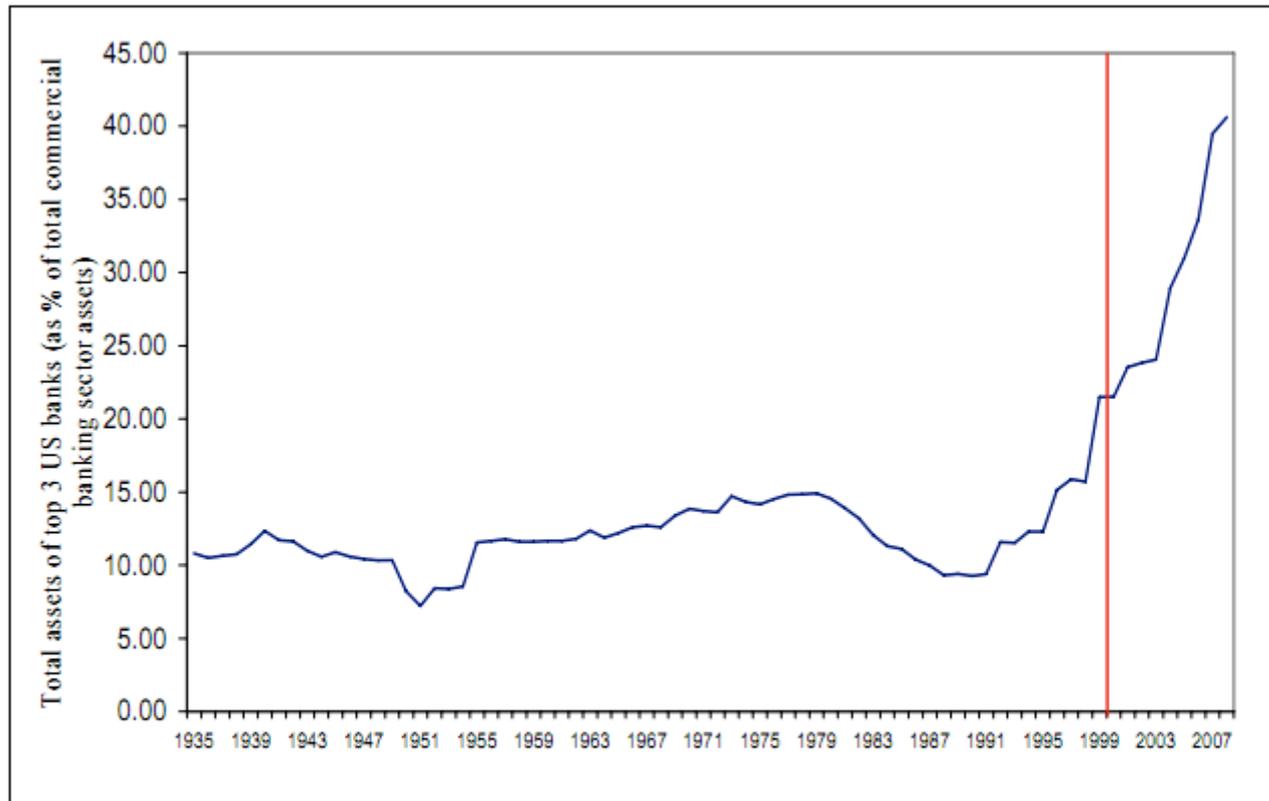


<sup>1</sup> Deal value of some divestitures not reported.  
NOTE: Numbers may not sum due to rounding.

# The changing geography of banking



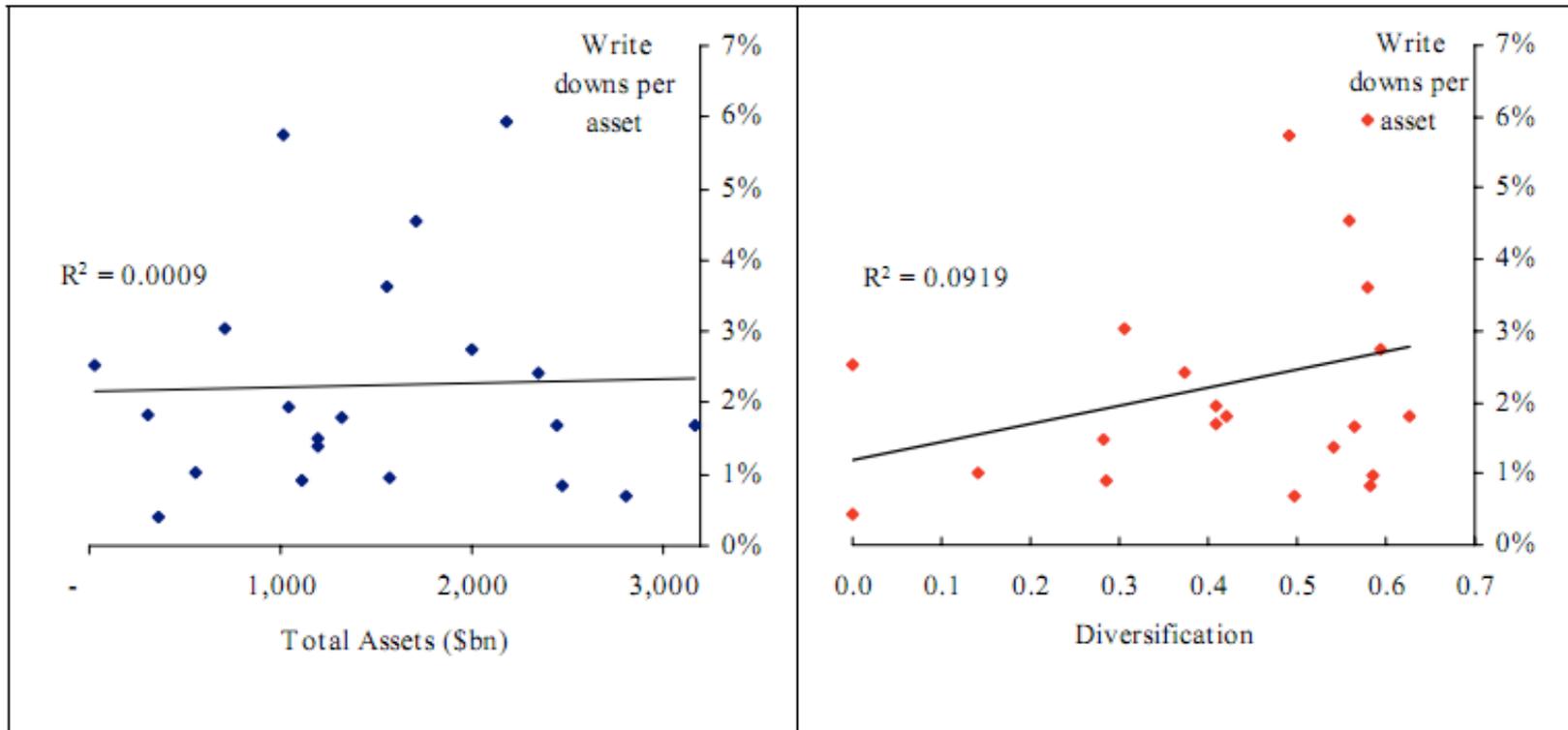
# Concentration in US banking has grown



- (a) Red line represents the Gramm-Leach-Bliley Act (1999) which revoked restrictions of Glass-Steagall
- (b) Top 3 banks by total assets as a % of total banking sector assets
- (c) Data includes only the insured depository subsidiaries of banks to ensure consistency over time - for example, non-deposit subsidiaries are not included.

Source: FDIC

# Even though big banks do not seem better or safer



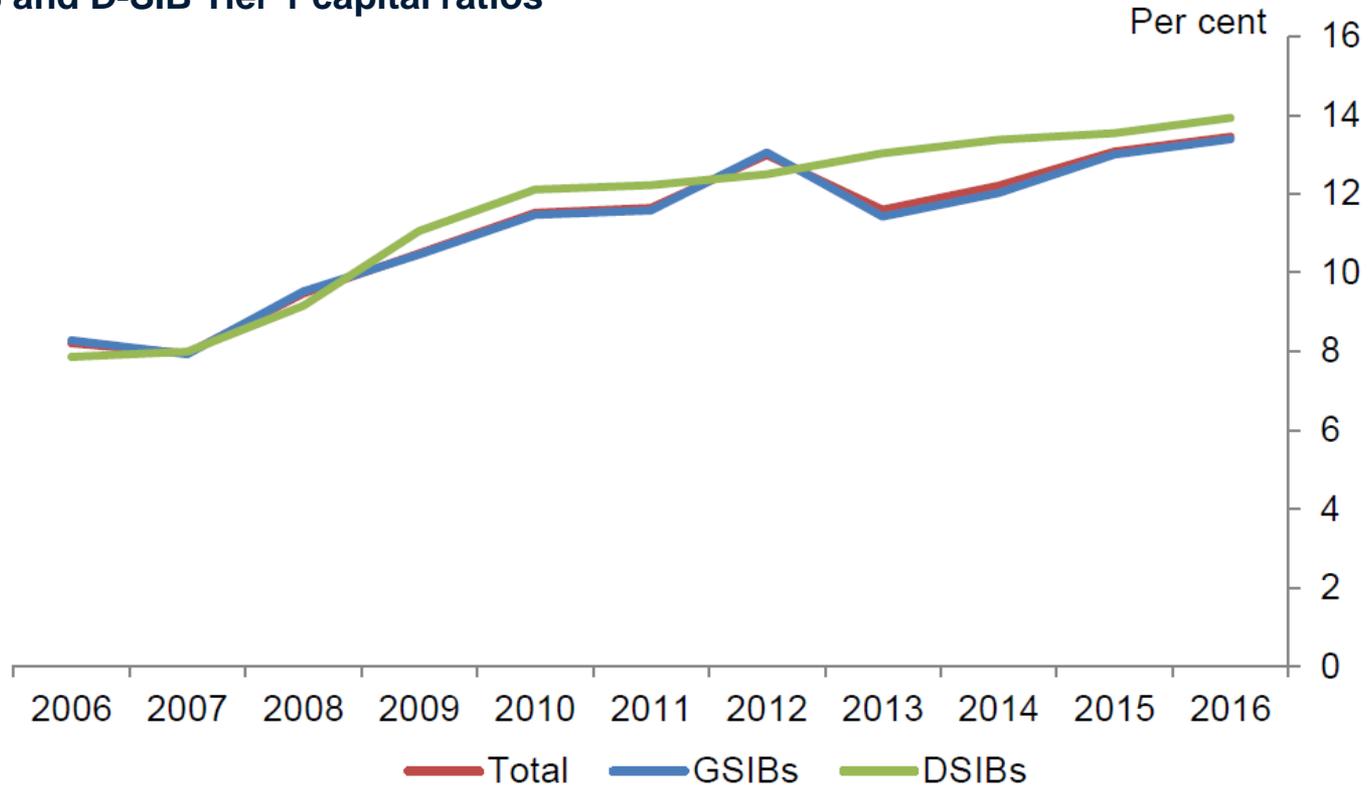
## 2. What has happened to capital, valuations and profitability

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- capital ratios have risen sharply under regulatory pressure
- but investors have not been very impressed
- perhaps because returns on capital have, on average, remained much lower than before the crisis

# The capital strength of large banks has grown

**G-SIB and D-SIB Tier 1 capital ratios**



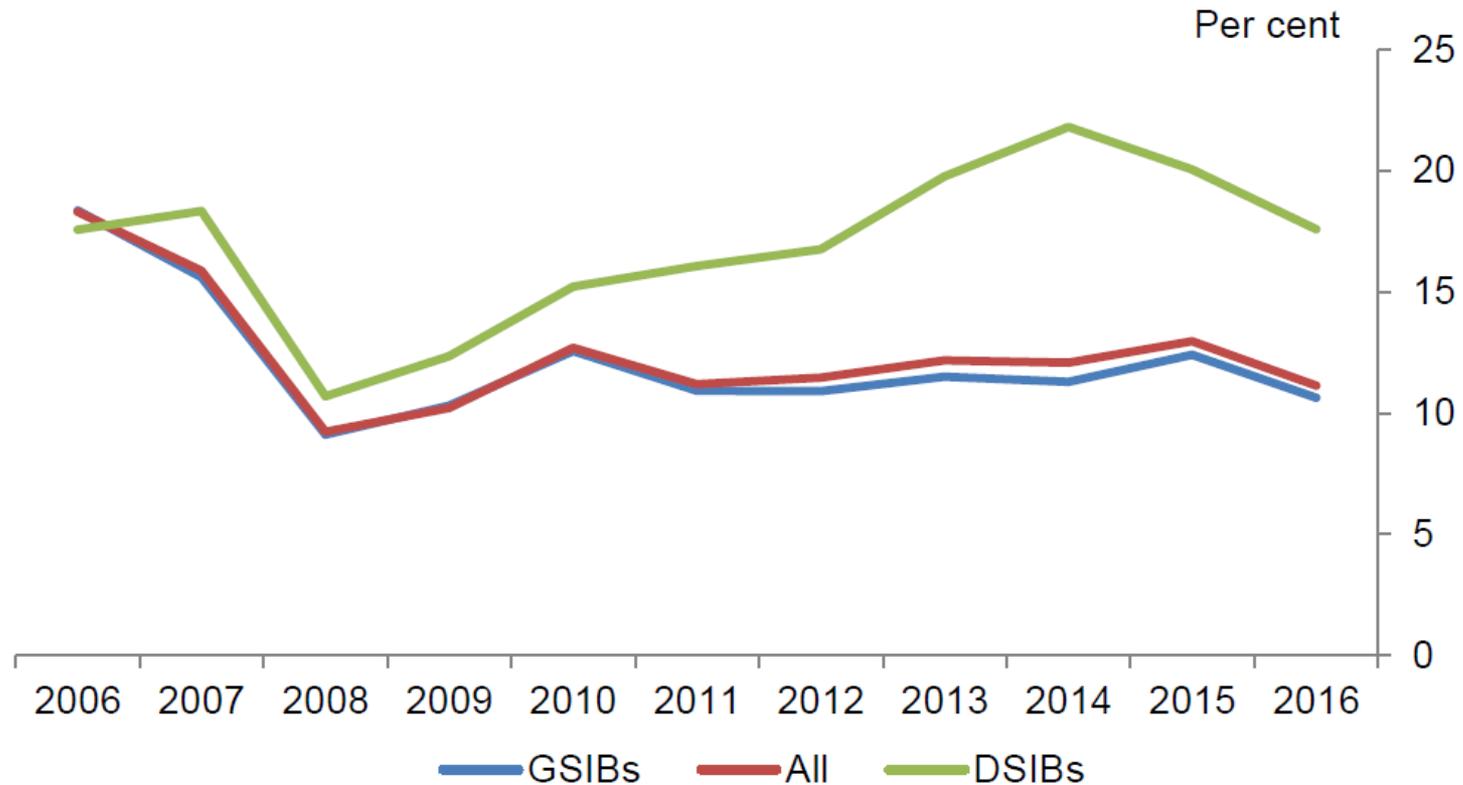
# But price to book valuations have fallen

**G-SIB and D-SIB price-to-book ratio**



# So on a market valuation basis banks do not seem so strong

Capital ratio using market value of equity



# Bank returns have been under pressure

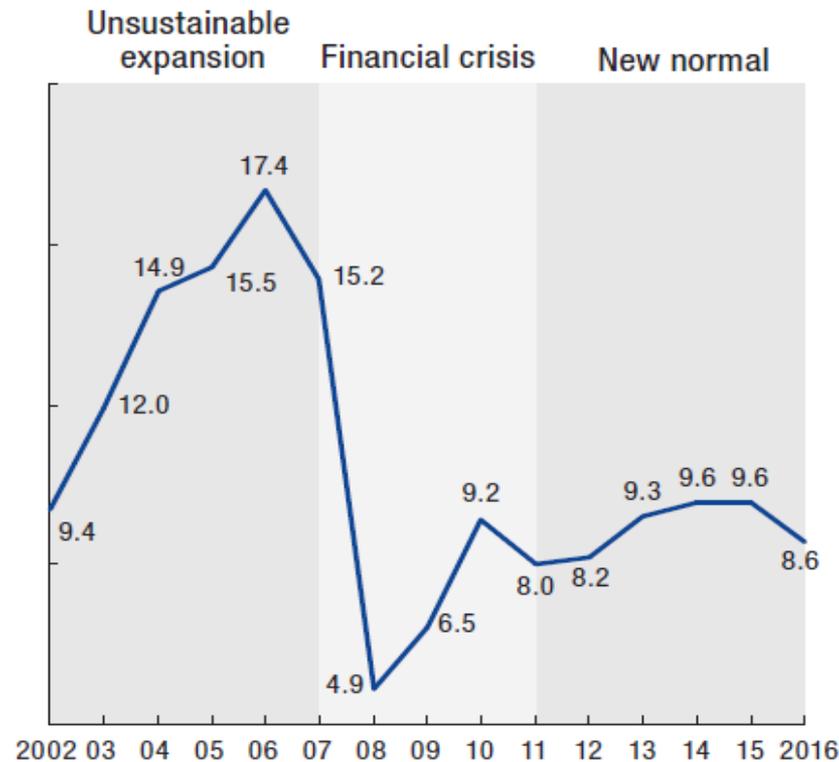
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- higher capital requirements have increased the cost of capital
- regulatory fines and compensation have been huge: \$321 billion or more (Boston Consulting Group calculation)
- very low interest rates have depressed Net Interest Margins

# Banks have stabilised at a lower RoE

**ROE, 2002-2016**

Percent

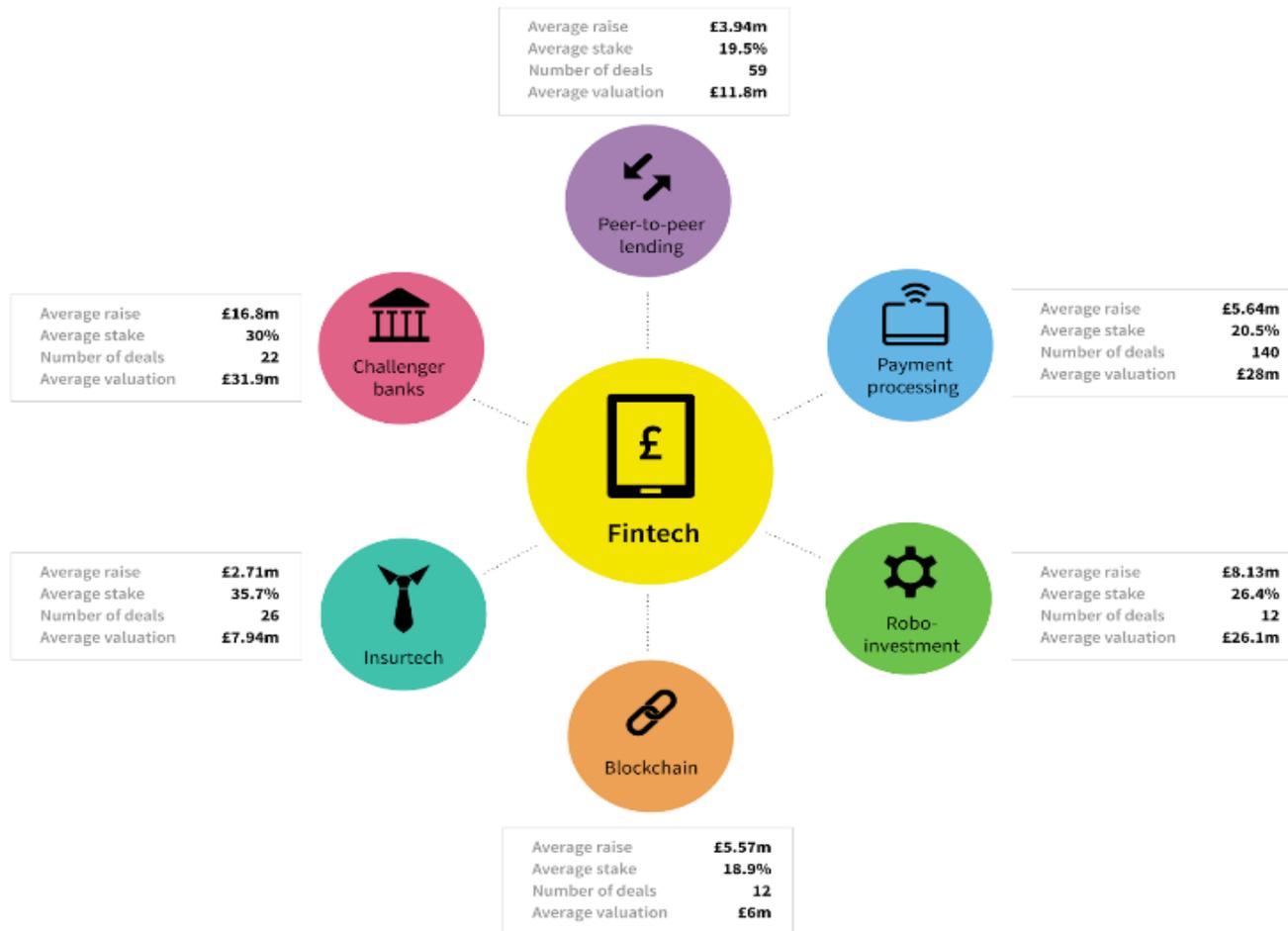


### 3. What are the main competitor threats to banks' business models?

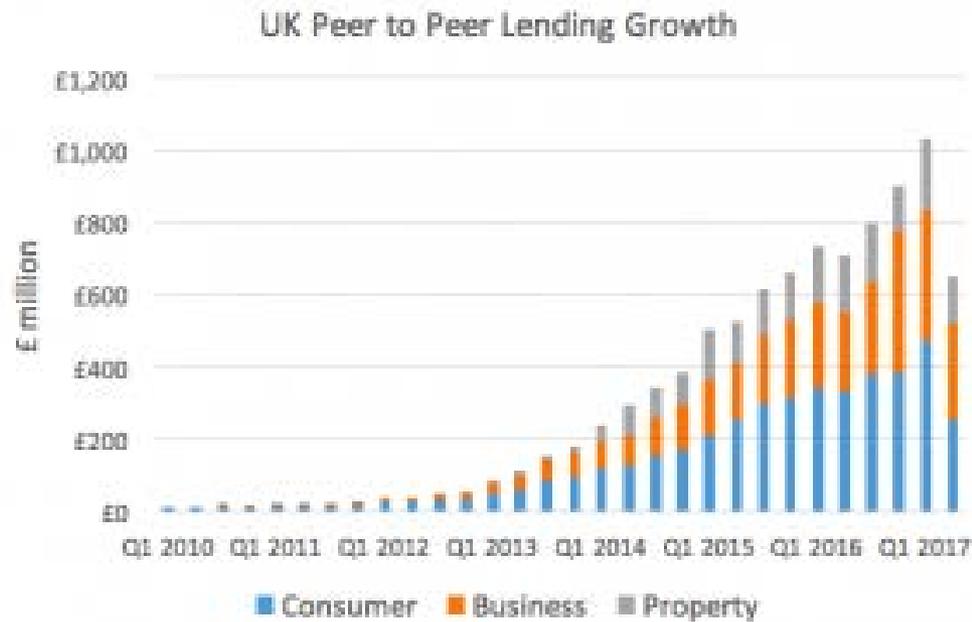
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- peer to peer lenders
- new entrants into payment systems
- fintech, especially digital platforms

# P2P and Payments have attracted most investment

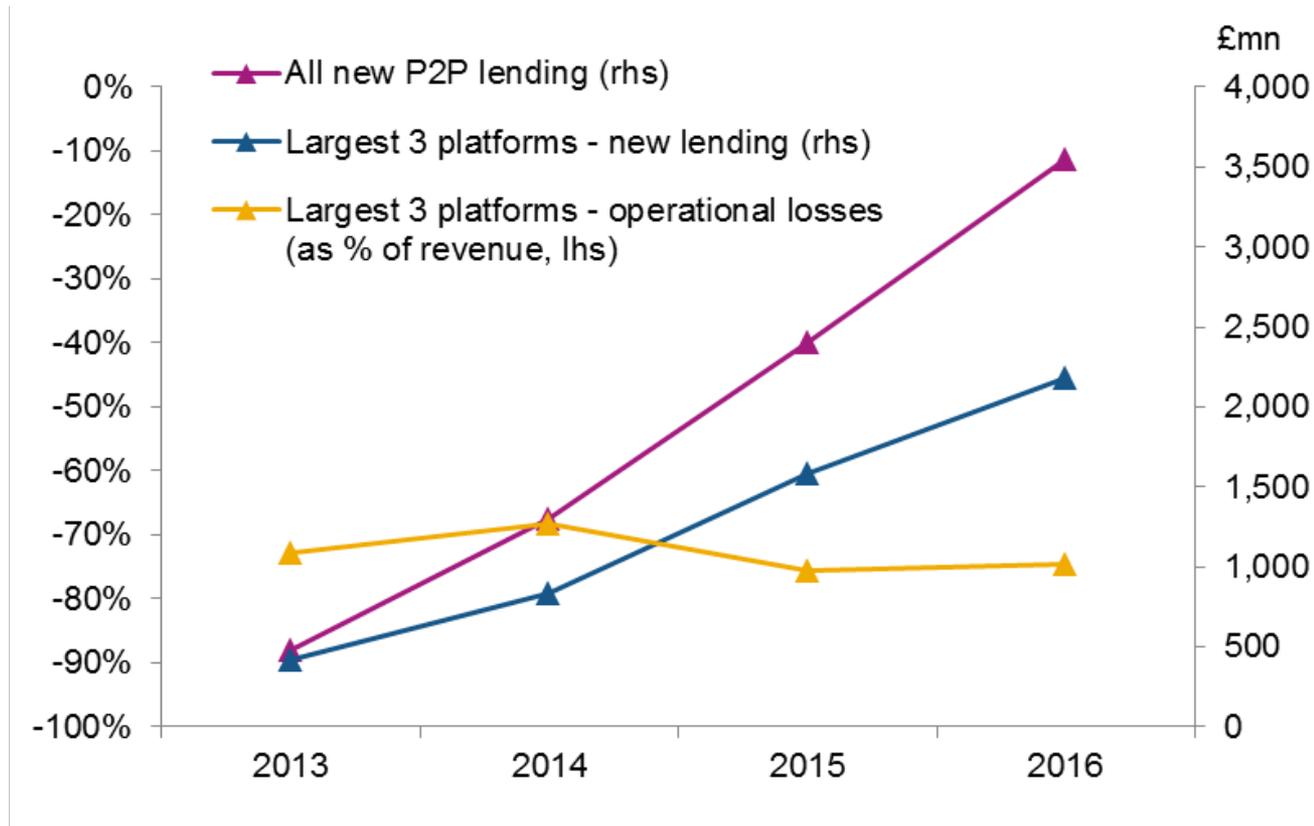


# P2P Growth has been explosive.....



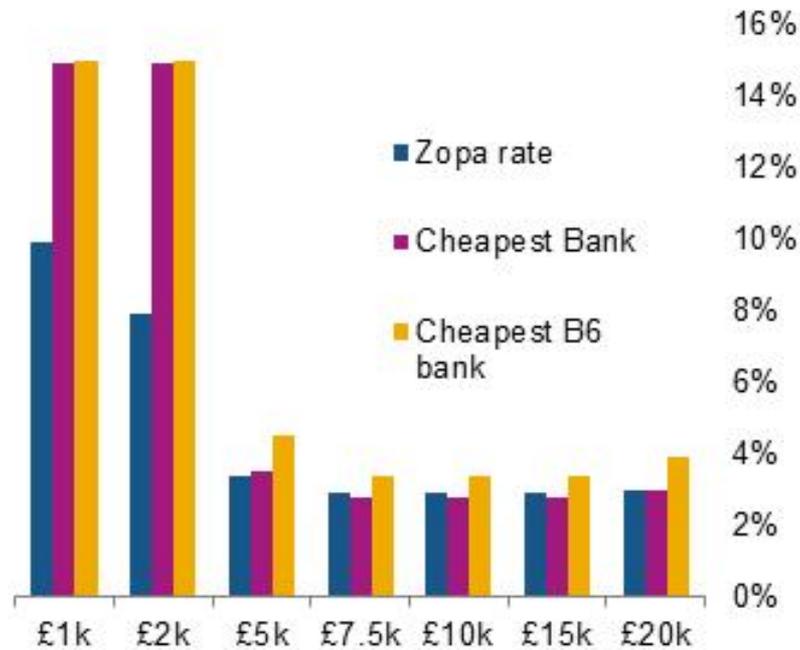
# P2P lenders still struggle to break even

Lending growth and operational losses of selected UK P2P platforms



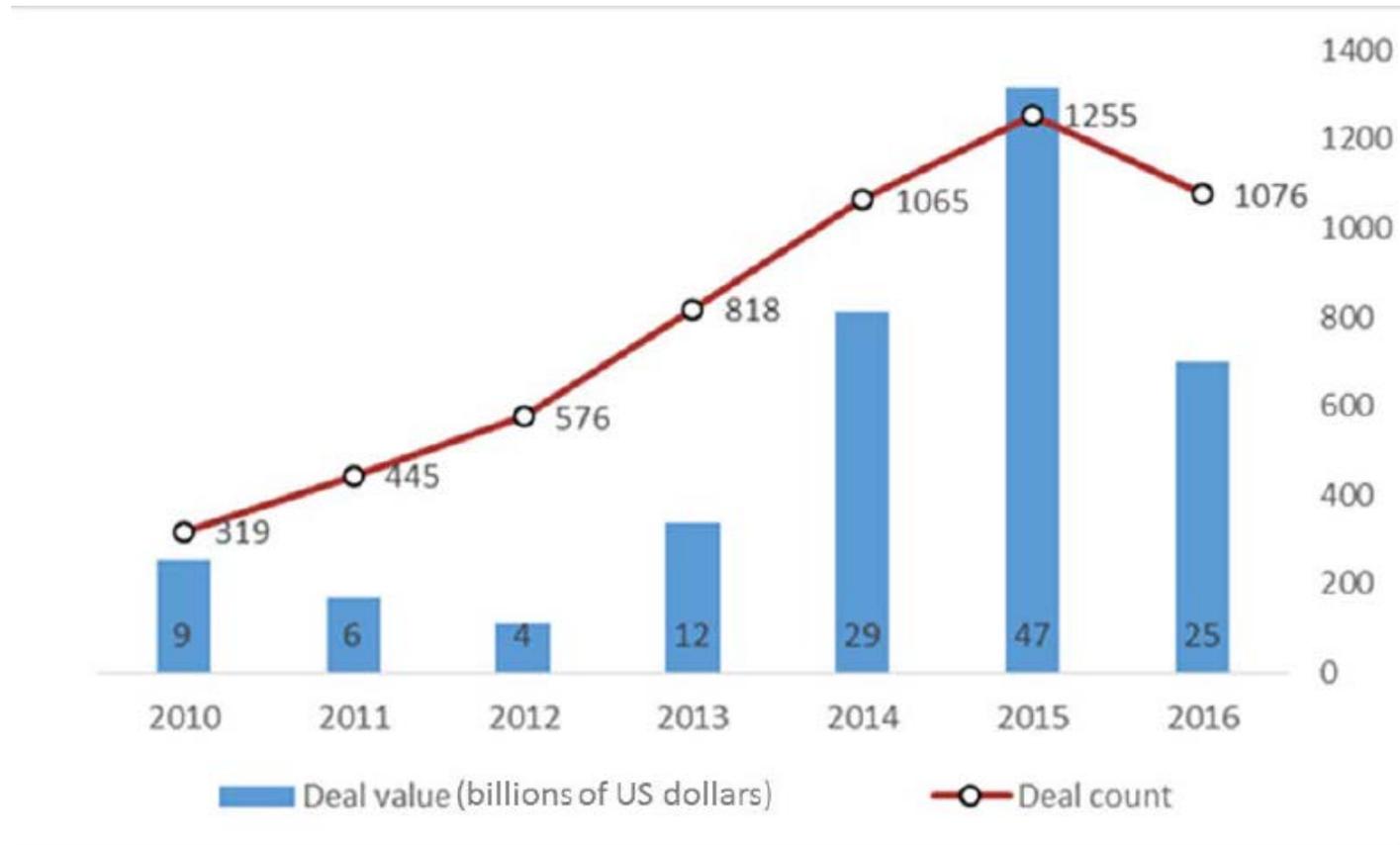
# And they are not much cheaper for borrowers

Consumer of Zopa (leading P2P consumer platform) and bank consumer lending rates by size of loan ( 5 year maturity)

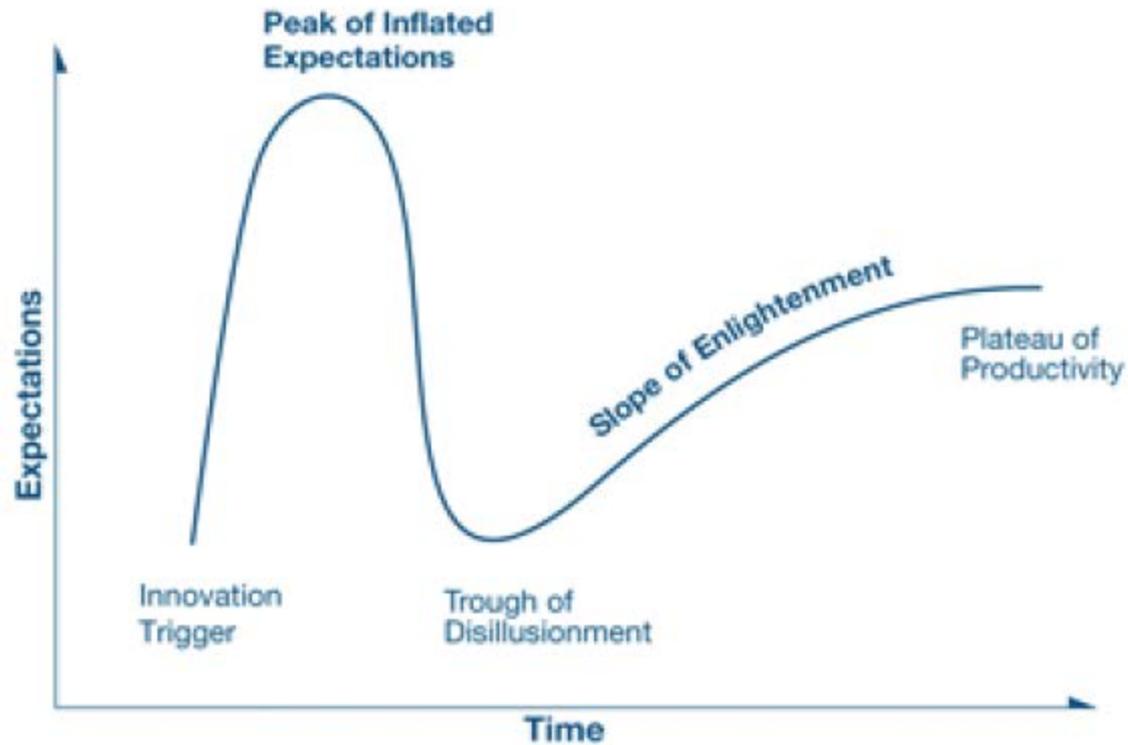


# Fintech investment boom may be tailing off

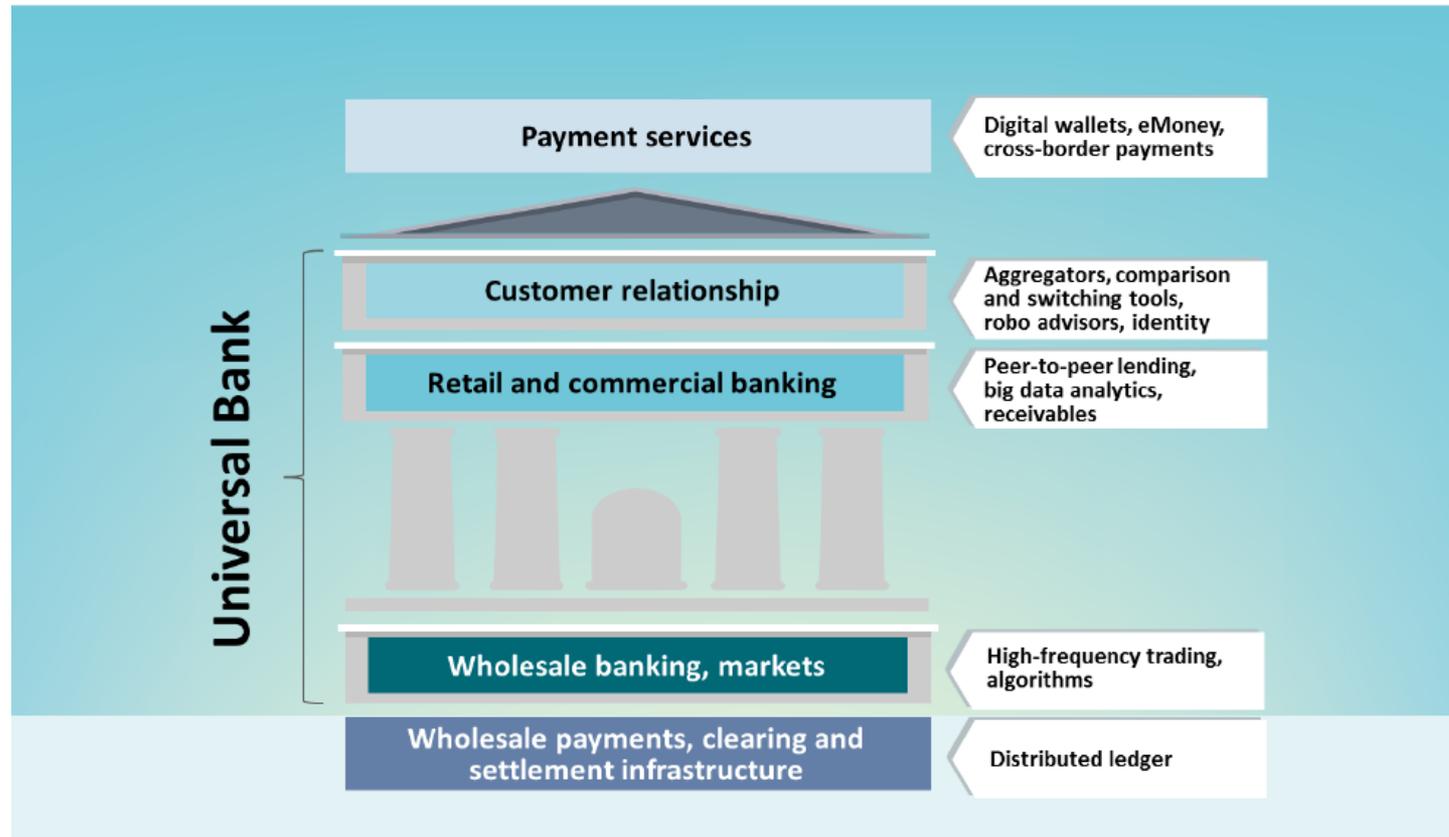
Total global investment in fintech companies 2010 - 2016



# Some may not succeed



# But the threat to business models is comprehensive



# Scouting for ideas and partnerships

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# Hold onto customers

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“The battle between start-ups and incumbents revolves around one key question:

Do start-ups get distribution before incumbents get innovation?”

*Silicon Valley V.C.*

# Banks must become more agile

## 5 Characteristics of agile distribution



### Customer first

Offering customers "what they need," not "what the bank has," hyper-personalized products and services.



### Revenue ready

Transforming fixed costs into variable costs and investing savings in revenue generation opportunities.



### Fast twitch

Flexing distribution, making channel decisions quickly and often.



### Test, learn, tweak

Replacing complex distribution processes, continually adjusting offerings as the market dictates.



### Right channeling

Combining digital and physical channels to grow market share without traditional branches.

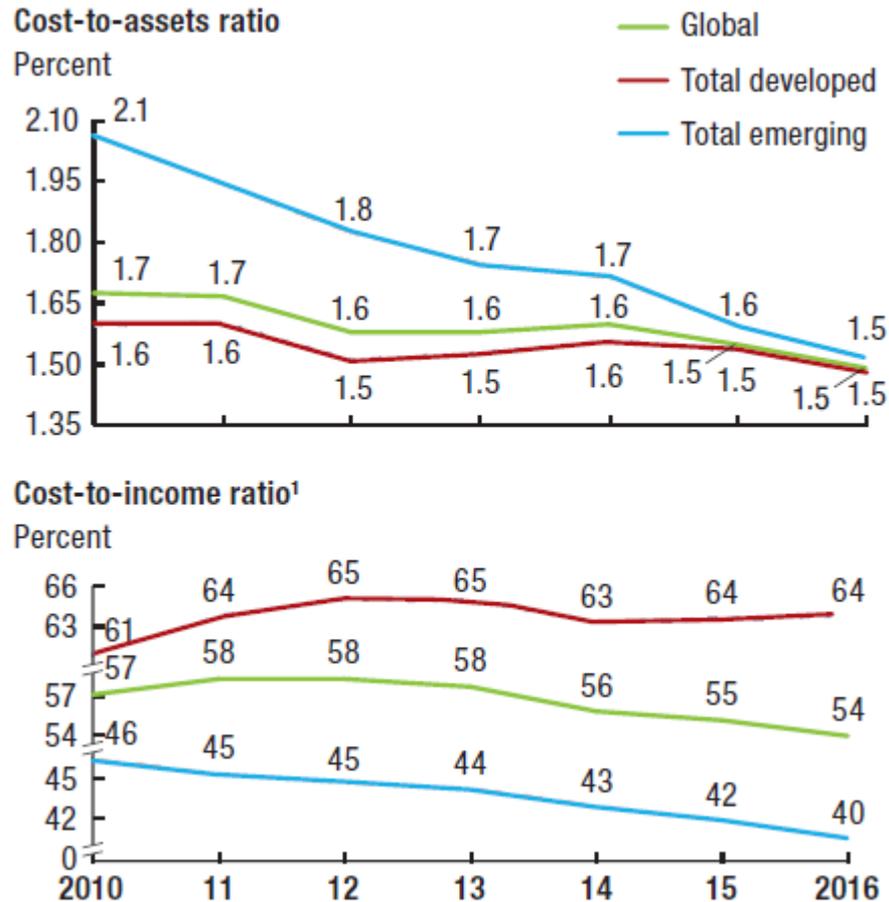
# Risk Management must assist prudent growth

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“What if we don’t change at all ...  
and something magical just happens?”

# Efficiency must be a major focus



<sup>1</sup> NOTE: Cost-to-income ratio of developed market banks increased in the last two years; however, this is due to margin erosion that could not be offset by the advance in cost efficiency

# Banks must be determined to lead



## It's the spark that says 'What if?'

It's the vision to challenge the status quo, to find new and improved ways to serve people.  
It's imagining what would be.

## It's the drive to keep going.

The tenacity to never give up, to be committed people who take ownership and follow up.  
It's the ability to keep going, and going, and going...



## It's the time to think clearly.

The thoughtfulness to do things the right way, to live our values and show our integrity.  
It's taking it personally.

## It's delivering great experiences.

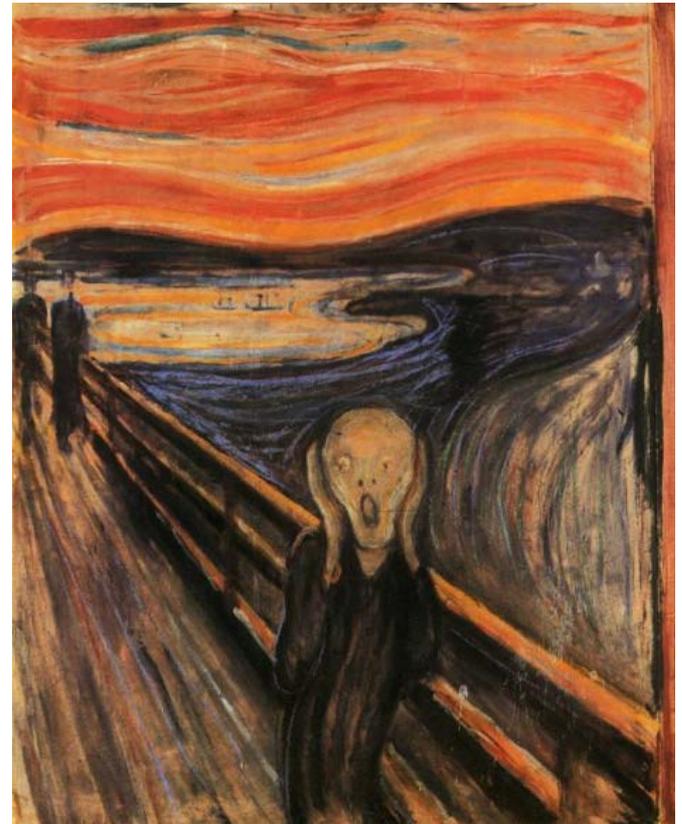
The passion to deliver value and delight, for customers, for colleagues and for communities.  
It's believing in a better experience.



# So the answer is to be....

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- **S**couting for opportunities
- **C**ustomer – centric
- **A**gile
- **R**isk aware
- **E**fficient
- **D**etermined



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Thank you