19th Annual Global CEO Survey/February 2016

Key findings in the banking and capital markets sector

Creating a platform for competitive regeneration

***176** Banking and Capital Markets CEOs in 62 countries were interviewed for PwC's 19th Annual Global CEO Survey*

Disruption and opportunity: Banking and Capital Markets CEOs believe that technology is the trend most likely to transform the expectations of customers, regulators and other key stakeholders over the next five years. 81% see the pace of technological change as a threat to growth, more than any other sector in the survey

Responding to uncertainty: 64% of Banking and Capital Markets CEOs plan significant changes in the way they define and manage risks

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About the 19th Annual Global CEO Survey

In this year's survey, global business leaders voice fresh concerns about economic and business growth. At the same time, they see a more divergent and multi-polar world where technology is transforming the expectations of customers and other stakeholders. In 'Redefining business success in a changing world', we explore how CEOs are addressing these challenges. We surveyed 1,409 CEOs in 83 countries and a range of industries in the last quarter of 2015, and conducted face-to-face interviews with 33 CEOs.

Today's business leaders have a tough job finding growth and delivering results year in, year out. But they know an even tougher task lies ahead: to prepare their organisations for a more complex future where customers and other stakeholders increasingly expect them to do more to tackle society's important problems.

To equip themselves for this challenge – and to build trust and ensure long-term success – CEOs are focusing on three core capabilities. Firstly, there's a stronger focus on customer needs as well as drawing on their organisational purpose – what their companies stand for – to define a more comprehensive view of how their business operates within society. Secondly, they're harnessing technology, innovation and talent to execute strategies that meet greater expectations. And finally, they're developing better ways to measure and communicate business success.

Introduction

Banking and Capital Markets (BCM) organisations are facing the immediate challenges of economic and political uncertainty and the longer term impact of new technology, more exacting regulation and shifting customer expectations.

Some long-established business models are struggling to sustain competitive relevance in the wake of these developments. In turn, new entrants are changing the competitive playing field and blurring industry boundaries. But today's market shake-up also opens up significant opportunities for reinvigorating growth and re-engaging with customers, employees and society as a whole.

In this report, we explore some of the key challenges and opportunities that are reshaping the BCM industry, focusing in particular on how to sustain returns in the face of uncertainty and change; how to navigate industry transformation and how to respond to changing customer, investor, employee, regulator, tax authority and other stakeholder expectations. We also look at how to define and measure success in this changing landscape.

71%

of BCM CEOs see more threats to growth today than there were three years ago, but 56% see more growth opportunities

"You're going to have a company that is ready for the next five years, where the only constant is rapid change. For that, you need people who can adjust to that change and comprehend the ecosystem."

Ajay Banga
President and Chief Executive Officer, MasterCard US

"We interviewed about 2,000 of our clients and we got a very sobering message from them. They said: 'Well, you should realise that we all need banking, but we don't need banks."

Ralph Hamers
CEO, ING Group, Netherlands

What comes through clearly from the survey findings is how quickly and effectively the market leaders are turning disruption into an opportunity. They're capitalising on the full value of technology and the creativity of their people to tap into new value chains and transform operational speed and cost. They're seeking out new sources of data and gathering the broad array of talent needed to enhance customer experiences and outcomes. Individually and through industry bodies, they're also playing a prominent role in supporting public policy priorities in areas ranging from promoting sustainability to advising clients, suppliers and other stakeholders on cyber risk management.

The winners will be those BCM organisations that move their businesses with purpose, speed and focus. They'll have excellent execution, the ability to attract top talent and the cultural systems that allow innovation to thrive.

Kevin Burrowes
Global Banking and Capital Markets Leader, PwC UK

Sustaining returns in the face of uncertainty and change

BCM organisations are striving to sustain returns in the face of economic uncertainty, regulatory upheaval and disruption to traditional business models.

The renewed optimism about the prospects for the global economy we saw in last year's survey has begun to fade. Only 31% of BCM CEOs believe that global growth will improve over the next 12 months, some way down from 43% last year. A quarter believe that growth will decline (15% last year), broadly in line with the less confident sentiment across all sectors in the survey.

"…increasing global political instability is an additional factor that we have to take into account – and above all the problems of financial and economic instability that can arise in our line of business."

Guillermo Tagle
Chairman, Credicorp Capital, Chile

Any faltering in global growth is likely to hold back both demand for banking services and further interest rate increases. It could also temper corporations' appetite for M&A. Only 31% of BCM CEOs are very confident about their own company's growth prospects over the coming year, down from 43% last year. However, 48% are very confident about their growth prospects over the next three years, suggesting that any dip will be temporary.

The faltering economic confidence is heightened by concerns over social and political instability. More than three-quarters of BCM CEOs see geopolitical uncertainty as a threat to growth and nearly 70% expressed fears over social instability (see Figure 1).

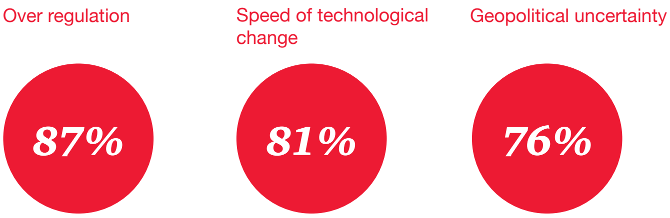
More than 60% of BCM CEOs intend to make significant changes to the way they define and manage risks in response to changing stakeholder expectations, making this as important as the use of technology in their business plans (see Figure 2). Across the industry, the scope of risk management is broadening to adapt to the fundamental changes in markets, business models and transactions. The key differentiator is being able to see risk coming, contain it early and adapt quickly. Better monitoring and control is part of the answer. What also marks out the most effective BCM organisations is the strength of the risk culture within the business and the connectivity between risk and frontline teams. Skills are required to handle not just credit market, operational and liquidity risks, but other kinds, like cyber, reputational and geopolitical risks. This in turn requires a connected view that can assess the risk impact on individual transactions all the way up to the broader corporate strategy.

Figure 1 **Concerns over economic, policy, social and business threats**

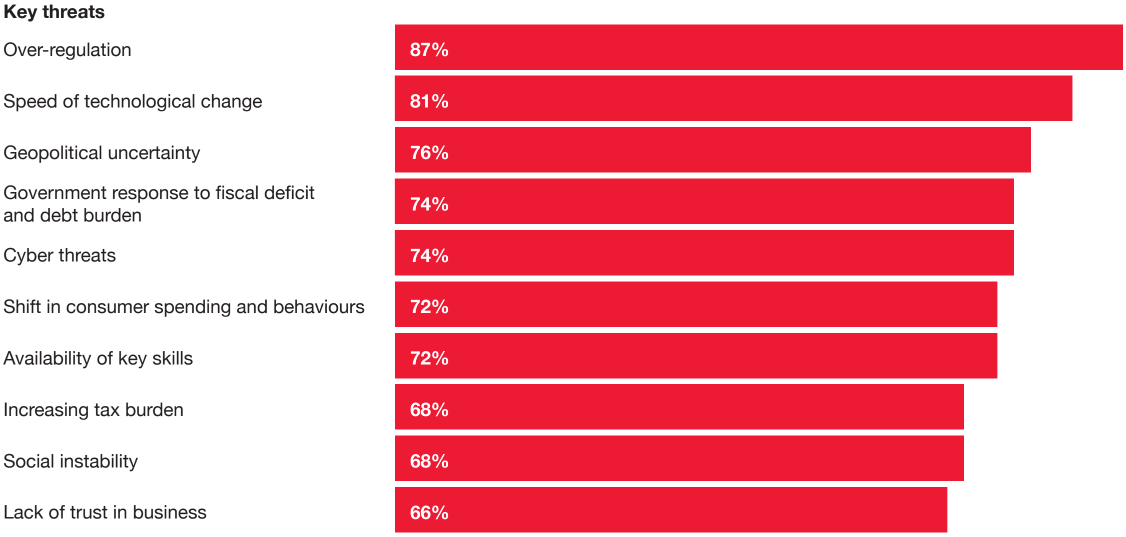
Q: How concerned are you about the following potential economic, policy, social and business threats to your organisation's growth prospects?

Respondents who stated 'extremely concerned' or 'somewhat concerned'

Top three threats



Key threats

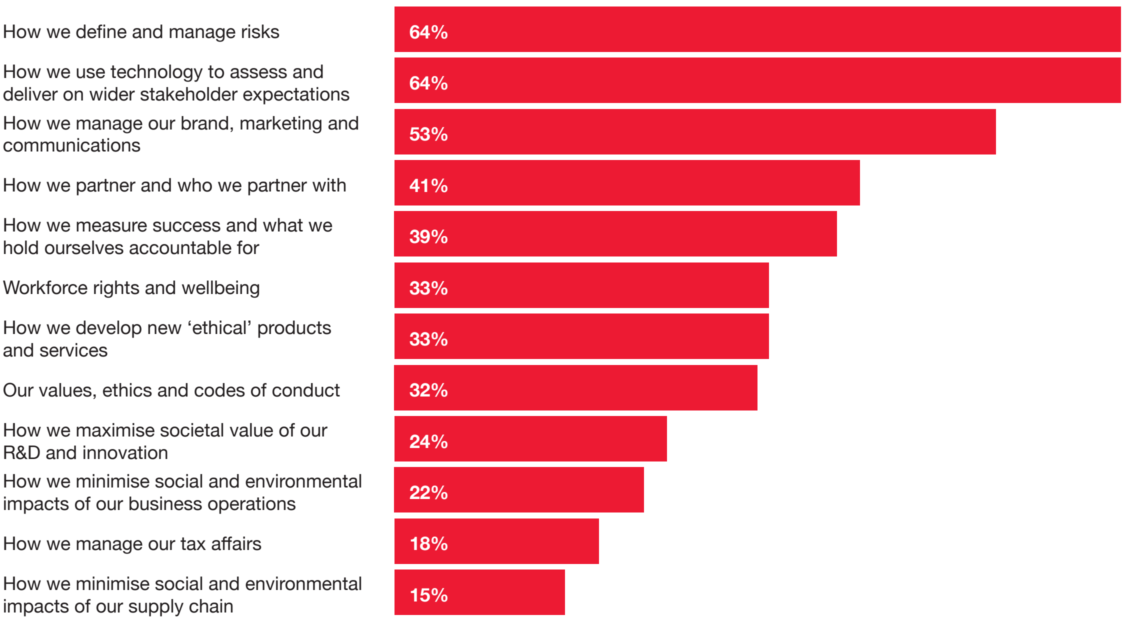


Source: 176 BCM CEOs participating in the 19th Annual Global CEO Survey

Figure 2 **Meeting changing expectations**

Q: To what extent are you making changes in the following areas in response to changing stakeholder expectations?

Respondents who stated 'significant change'



Source: 176 BCM CEOs participating in the 19th Annual Global CEO Survey

Regulation reshapes the playing field

Regulation continues to be costly and complex – 87% of BCM CEOs see over-regulation as a threat to growth. The combination of higher capital charges, liquidity demands and compliance costs is forcing many BCM organisations to abandon what had once been profitable mainstays of their business.

However, while regulation continues to be one of the most disruptive forces within the BCM market, we're at last beginning to see some certainty ahead. Phase one was the legislation resulting from the investigation into what went wrong during the crisis. Phase two was the resulting regulation, and now we're finally into the third phase, the actual implementation. While some BCM organisations have yet to address the strategic capital and liquidity levels in their businesses, the operational impacts of this new regulatory era are becoming clearer and the key priority is working out how to meet regulatory and compliance demands more quickly, at lower cost and with less management distraction.

The pace of regulatory change has required a lot of reactive responses and inefficient fixes and patches. The result could be likened to a ship that's been battered by an endless series of storms. Now's the time to get this leaky vessel into dry dock for a major refit. Work is therefore required to sift through the huge number of regulatory projects and de-clutter them. A combination of technology, outsourcing and centralised centres of excellence will be at the heart of the leaner and more streamlined approach to compliance that emerges.

"Whenever the pendulum swings, it usually swings too far, but regardless of the regulatory situation, it is what it is. So how do we digest that? We actually believe that it's a competitive advantage for us, because of our technology platform. We build those regulations into our systems and processes, not leaving them for someone to figure out on a manual spreadsheet. Our technology will help people comply with what needs to be done, and because we can do it better, faster and more efficiently, that's an advantage."

Bill Emerson
Chief Executive Officer,
Quicken Loans

Focusing resources

Higher regulatory capital charges are changing the economics of BCM and spurring further retrenchment and restructuring.

The scaling back of market operations within investment banking, particularly within Europe, has been especially marked. The global players are shrinking to a core of the biggest and best capitalised investment banks, with headquarters in economies large enough to support their balance sheets – primarily the US at present, but also strong Asian countries. The space left by the exit of some of the bigger players is being filled by an array of hedge funds and shadow banking funds and entities, which have brought greater innovation but also greater fragmentation to a fast-changing market – for more perspectives on the road ahead see 'Capital markets 2020: Will it change for good?'.

And restructuring across the market will continue – more than 10% of BCM CEOs plan to sell a majority interest in a business or exit a significant market over the next 12 months. Divestment opens up considerable opportunities for acquisition, greater specialisation and sharper strategic focus. As some traditional revenue streams come under threat, it's important to identify which parts of the business will still be viable in three to five years' time. Carrying this out in a systematic way, allocating revenue and costs sensibly and viewing all of this from a customer-centric position is no easy task. Success will allow management to refocus resources and exit from any operations that are likely to hold back returns. The cost of capital and new cost benchmarks are clearly important considerations. But it's also important to take account of the brand implications, talent, location and technological capabilities.

"…during a certain period of time we tried to do a lot of things that were not in our core business and not in our main objective. We tried to diversify too much, and we probably tried to enter into areas of risks that we couldn't control, and cycles that we didn't control either. So we are returning to basics."

Dr. Nuno Amado
Banco Comercial Português, S.A. Portugal

Cost-competitive

More than two-thirds of BCM CEOs plan further cost reduction initiatives over the next 12 months. Are they going far enough? Dr. Nuno Amado, CEO of Banco Comercial Português reports that his bank has achieved a 30% cut in costs. Is 30% the kind of benchmark other banks should be targeting? With pressure on cost coming from new digital players, it may have to be. If so, how can it be achieved? Despite several years of sustained cost reduction, there's still a lot of fat to be cut back within the industry. Many BCM groups employ thousands of people to take care of on-boarding, for example. Could such operations be handled at much lower cost and greater speed by a dedicated provider? In a further example, a huge proportion of the BCM employees working within high cost commercial centres such as London, Hong Kong or New York don't need to be there, especially now that technology allows for much greater virtual collaboration. The way forward is a much clearer identification of unit costs, how these compare to the new benchmarks and what options are available to cut them down to size.

Innovation and transformation

Technology is transforming customer expectations, lowering barriers to market entry and opening up growing competition from FinTech entrants. BCM CEOs believe that technology is the trend that's most likely to transform the expectations of customers, regulators and other key stakeholders over the next five years (93% ranking it in the top three) – more than the technology sector itself (92%).

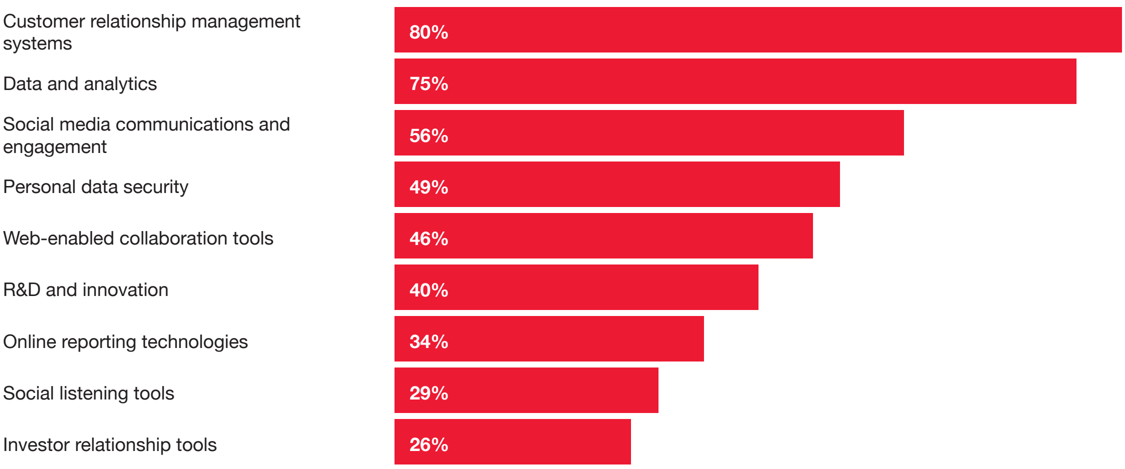
New technology can help businesses to foster a more informed and engaged relationship with customers – Figure 3 highlights the areas of technology BCM CEOs see as generating the greatest return in terms of engagement with wider stakeholders. The ability to analyse more data, more quickly and with more predictive capabilities than ever can also ensure a faster, more targeted and more forward-looking response to customer demands and capital market developments.

"We're all still learning how to use this untethered computing power to distribute products, services, and information differently, but technology is going to lead to sea changes in how companies are organised and run across all industries, and ours is no different."

Brian Moynihan
Chief Executive Officer of Bank of America Corporation US

Figure 3 Technological priorities

Q: Please select the connecting technologies you think generate the greatest return in terms of engagement with wider stakeholders.



Source: 176 BCM CEOs participating in the 19th Annual Global CEO Survey

But technology has also created new benchmarks for cost, customer understanding and speed of response, which are putting severe strains on the often slow and unwieldy systems within many established businesses. The disruptive impact is highlighted by the fact that 81% of BCM leaders see the speed of technological change as a threat to growth. More than 70% of BCM CEOs also see shifts in consumer spending and behaviour as a concern. As many established organisations struggle to meet these demands, FinTech is moving in to fill the gaps, using advanced digital profiling to target customers and low-cost digital distribution to undercut traditional competitors.

"The ones where you can't predict where they're going are the FinTechs. And the FinTechs are the new eager, young, hungry, agile, fast-moving companies that go after a single part of the value chain, and then basically try to create inroads into how a bank works and try to excel at that one part of the business and through which they can make money."

Ralph Hamers
CEO, ING Group, Netherlands

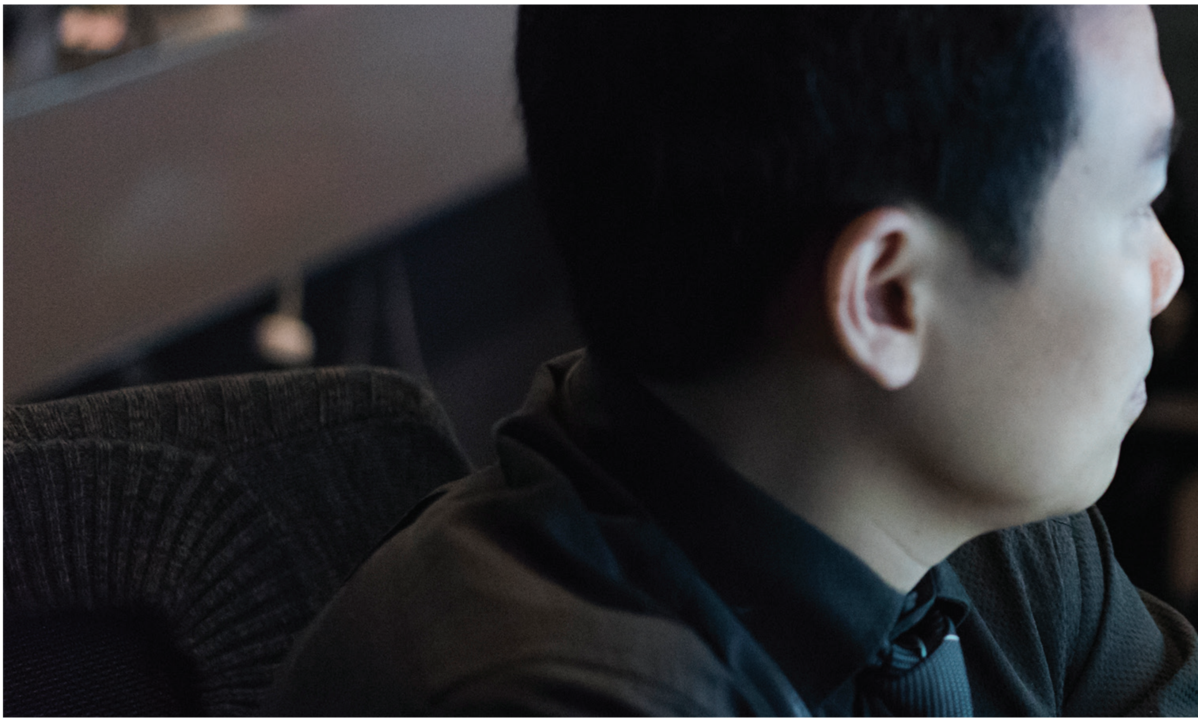
Building on their platform in payments and peer-to-peer lending, FinTech businesses are now moving into the mainstream and targeting further areas of the value chain ranging from investment advice to money market funds. They're also creating new commercial networks that use payments data and connections as the basis for advanced customer profiling, marketing and loyalty incentives. But FinTech businesses also present opportunities for partnership and growth. Established players can offer the funding, infrastructure and compliance advice that many FinTech businesses will be looking for. Strategic alliances can also help to refresh the brand and allow established businesses to reach out into less-tapped markets, be this rural communities in emerging economies or younger digital natives in developed markets.

"As an innovator, we engage the market and our clients are the disruptors in the FinTech area. At the same time, a lot of banks push back and say, "That's disruption we don't want to be part of." As we view it, we're also going to be a partner for these types of clients in the FinTech area. We have to figure out how to be part of their backbone."

Greg Becker
President and Chief Executive Officer, Silicon Valley Bank

"Even with all the new technology, people skills are actually more important now. Whether it's providing day-to-day services in our bank branches or managing our data analytics; it's all about people. So the risk is, can we hire, retain, and develop the top talent and, frankly, will they be happy working here?"

Brian Moynihan
Chief Executive Officer, Bank of America Corporation US



How far could disintermediation go? Could we even see the emergence of institutions who focus solely on monetising information and relationships, without taking any risks onto their balance sheet? "If you look where technology business models are going, you basically see that it's all about access and not about assets." says Ralph Hamers, CEO, ING Group NV. "The largest media company in the world is Facebook. They don't produce any content. The largest hotel company in the world is Airbnb, and they have no hotel rooms. And the largest taxi company in the world is Uber, and they have no taxis whatsoever. So the question really is why couldn't the largest bank in the world be one that doesn't have a balance sheet?"

The need to keep pace demands a flatter and more flexible organisation, which can interpret digital intelligence as it comes in and rapidly mobilise around market openings. Ralph Hamers, CEO of ING Group believes that to ensure agility, the business needs "…to move faster in the market, like the FinTechs are moving, which basically means you should work in a more agile/scrum way than working according to established hierarchical patterns".

The impact of technology requires more people with both banking and digital skills. Few as yet possess these hybrid capabilities. Competition to attract them isn't just coming from traditional peers, but also FinTech start-ups and technology groups looking to develop their presence within the BCM and wider financial services market. Little wonder then that 72% of BCM CEOs see the limited availability of key skills as a threat to growth.

Cost constraints and the limited availability of key skills may hamper your ability to attract, develop and retain the talent you need. So it's important to explore all available options. This includes investment in automation and robotics to take care of routine transactions, trading and research, which would not only reduce costs, but also allow key personnel to devote more time to developing customised solutions and focusing on more complex and higher value accounts. This flexible and fast-response approach also includes more virtual collaboration, use of contingent labour and sharing of resources with competitors.

Many BCM organisations have been bringing in people from or partnering with FinTech enterprises. But their ideas and initiatives can easily be smothered by established hierarchies, decision making processes and ways of working. It's therefore important to think about how to overcome the barriers that hold back new thinking and ways of working. Is the answer to establish incubators, green field sites,

experiment in one brand area only or attempt full integration? BCM organisations are exploring different models with as yet no clear view at present as to what works best for their individual culture and ways of working.

Combatting cyber threats

With technology comes a new and escalating raft of cyber and broader financial crime risks – nearly three-quarters of BCM CEOs see cyber threats as a barrier to growth. BCM organisations have always been in the frontline of the fight against cybercrime, though they are only as strong as the weakest link in an ever more extended business chain.

Data protection is central to reputation. It's therefore vital that cyber risk is recognised as a strategic risk that demands board-level insight and leadership, rather than simply seeing it as a matter for IT or compliance. Key questions BCM boards should be asking as they look to strengthen protection include:

Who are our adversaries, what are their targets and what would be the impact of an attack?

We can't lock down everything, so what are the most important assets ('crown jewels') to protect?

Are we integrating threat intelligence and assessments into proactive cyber-defence programmes?

"As technology transforms our company, the risk of intrusion and cybersecurity worries us the most. Now, we've spent serious amounts of money on this, but the reality is you're never done. As much as we used to think about protecting our physical assets, it's the same today with our non-physical assets. They're in the hands of different people, and it's sometimes harder to figure out."

Brian Moynihan
Chief Executive Officer, Bank of America Corporation US

Do we assess vulnerabilities against known tactics and tools used by perpetrators who might target them?

Beyond confines of your own systems, it's important to identify and tackle the weaknesses within client and partner businesses like retailers or service providers and other partners. This requires a more collaborative approach in which you not only work more closely with clients and suppliers to share expertise, threat intelligence and protective systems, but also governments and technology companies within a multi-agency approach.

Responding to changing stakeholder demands

Stakeholders are demanding more from banks, not just in the value they deliver to them individually, but also in their contribution to society as a whole.

For many BCM CEOs in our survey, these developments are not just spurring a review of business strategy, but a more fundamental rethink of their vision, objectives and how they measure success. Thirty per cent of industry leaders say that their organisation has changed its purpose in the past three years to take account of its broader impact on society and a further 12% are considering this. As Ralph Hamers, CEO of ING Group explains, "...bringing the purpose alive in a company…means that you have to be able to explain that the purpose is real, it's one to be followed…it's the starting point of everything you do".

"These core values of trust, integrity, transparency, objectivity, fairness, these are completely non-negotiable."

Chitra Ramkrishna
Managing Director and CEO, National Stock Exchange of India Limited (NSE) India

But as our survey highlights, it can be difficult to balance the potentially conflicting demands of different stakeholders without raising costs and eroding profitability (see Figure 4). Technology and innovation will be critical in delivering the outcomes stakeholders want at a cost customers and investors are willing to bear. As you look at how to target resources, it's also important to gain a deeper understanding of customer, regulator and wider stakeholder expectations and how to align these with the priorities of your business.

Further priorities include identifying areas of common interest with governments and the community. The focus of this unifying purpose is likely to centre on five key areas:

Financial stability and conduct

Economic development

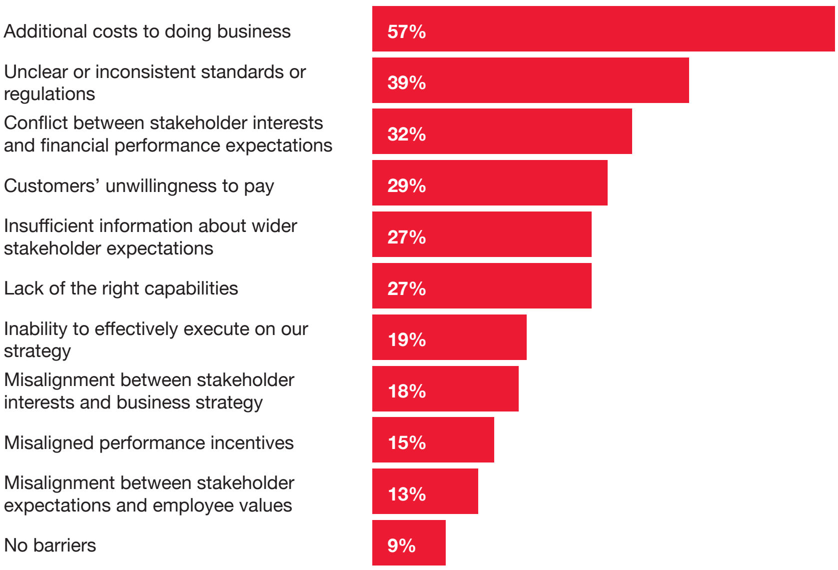
Social progress

Elimination of tax evasion, corruption and terrorism

Sustainability

Figure 4 **Barriers to meeting expectations**

Q: Which of the following barriers, if any, is your organisation encountering when responding to wider stakeholder expectations?



Source: 176 BCM CEOs participating in the 19th Annual Global CEO Survey

The focus on social as well as financial value is likely to be one of the keys to attracting talent – 53% of BCM CEOs say top talent prefer to work for organisations with social values which are aligned to their own, making this more important than competitive compensation (45%). Looking five years ahead, 63% believe this will be the case (compensation 34%). This increase reflects the perspectives of the new generations coming into the workforce. Since 2008, we've been carrying out periodic surveys into what people born between 1980 and 1995 want from the world of work. The findings consistently show that millennials want their work to have a purpose, they want to feel they contribute something to the world and they want to be proud of their employer. The ability to build and communicate meaning and social value will therefore be an increasingly crucial employer brand differentiator.

An emerging trend and one we predict will get stronger is the BCM sector's role in sustainability, especially following the recent Paris Accord. We believe that the sector's ongoing exposure to economies and companies that are not environmentally focused will receive increasing attention, not only from within BCM institutions, but also from stakeholders and external commentators. BCM organisations' decisions over whether or not to finance carbon producers on the one side and their investment in new technologies on the other will increasingly be in the spotlight.

"...our younger employees are driven to be successful, but they're also here to do things that make society better. It's critical for us to recognise that demand and then to shape the company around it."

Brian Moynihan
Chief Executive Officer, Bank of America Corporation US

Defining and measuring success

Eighty five per cent of BCM CEOs believe that business success in the 21st century will be defined by more than financial profit – one of the highest percentages of any sector taking part in the survey. Nearly two-thirds (65%) say that their purpose is centred on creating value for wider stakeholders, compared to 33% who say that their primary purpose is creating value for shareholders. More than half (53%) say that creating value for wider stakeholders helps them to be profitable.

Innovation is the area that BCM CEOs see as most important to measure (see Figure 5), but is lower down the priorities for communication (see Figure 6). Promoting innovation capacity and achievement should be more of a priority, given its importance in attracting customers and sustaining investment.

Figure 5 Measuring success

Q: In which of the following areas do you think business should be doing more to measure impact and value for wider stakeholders?

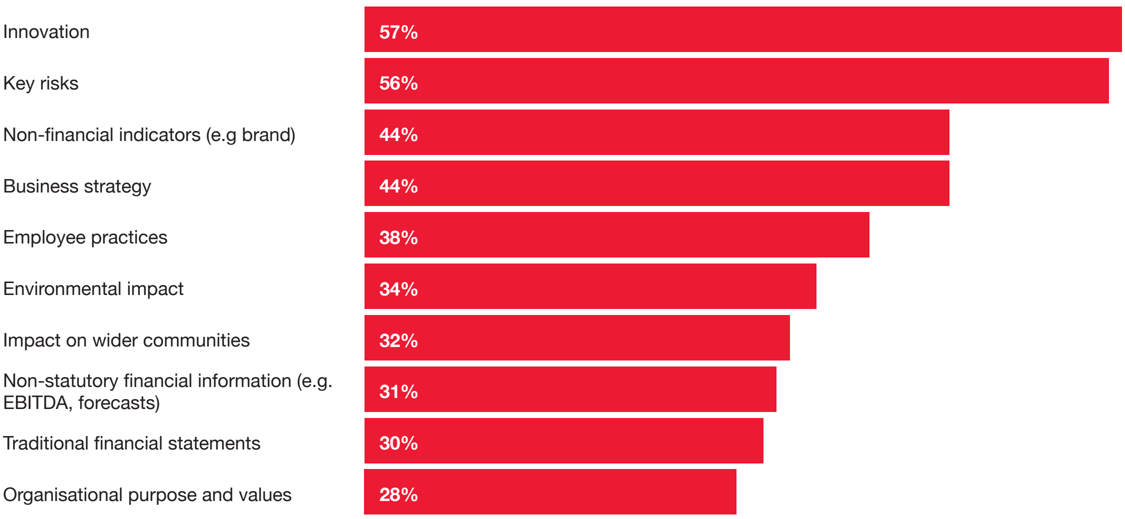


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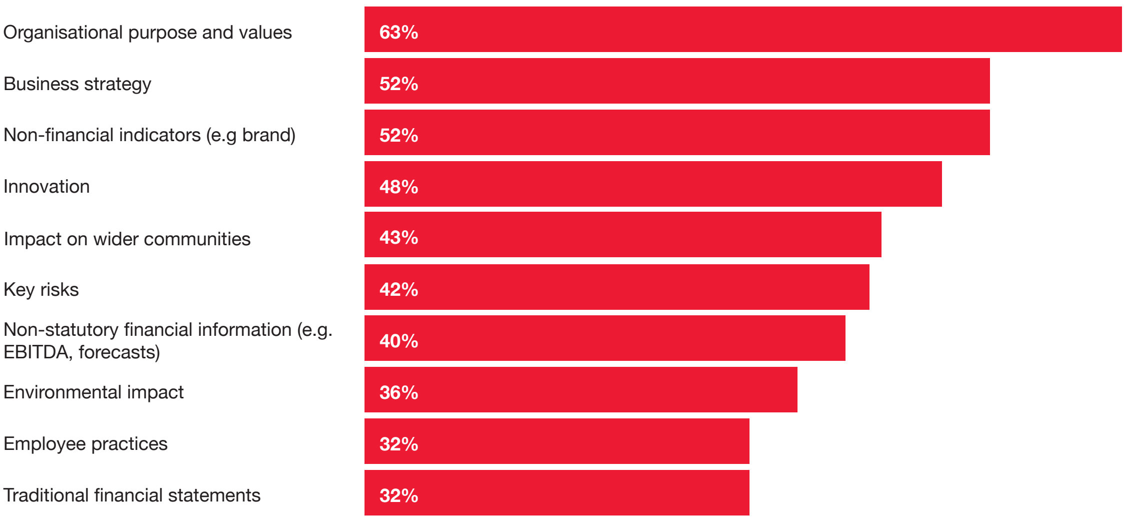
Figure 6 **Priorities for communication**

Q: In which of the following areas do you think business should be doing more to communicate impact and value for wider stakeholders?



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Similarly, more BCM CEOs say their organisations measure the impact of key risks than communicate this information. Within today's uncertain risk environment, measurement and communication of risk assessments are going to be crucial in sustaining confidence among investor, regulators and other key stakeholders.

In seeking to balance different stakeholder demands, it's important to ensure that performance objectives, evaluation and incentives take account of the different impacts of strategy and operations. "It's not just about the financial impact of what you do. It is about the broader real impact of what you do and today I think we are all coming out with different metrics to measure if this is working like a catalyst." says Chitra Ramkrishna, Managing Director and CEO of the National Stock Exchange of India Limited (NSE).

And employees need to be at the centre of this dashboard. "We've seen success in terms of the value of the stock, but you don't measure everything with that. You also measure with employee engagement. There's no shortcut to the steps you've got to take to bring your employees with you on this fascinating journey that the company is on." says Ajay Banga, of MasterCard.

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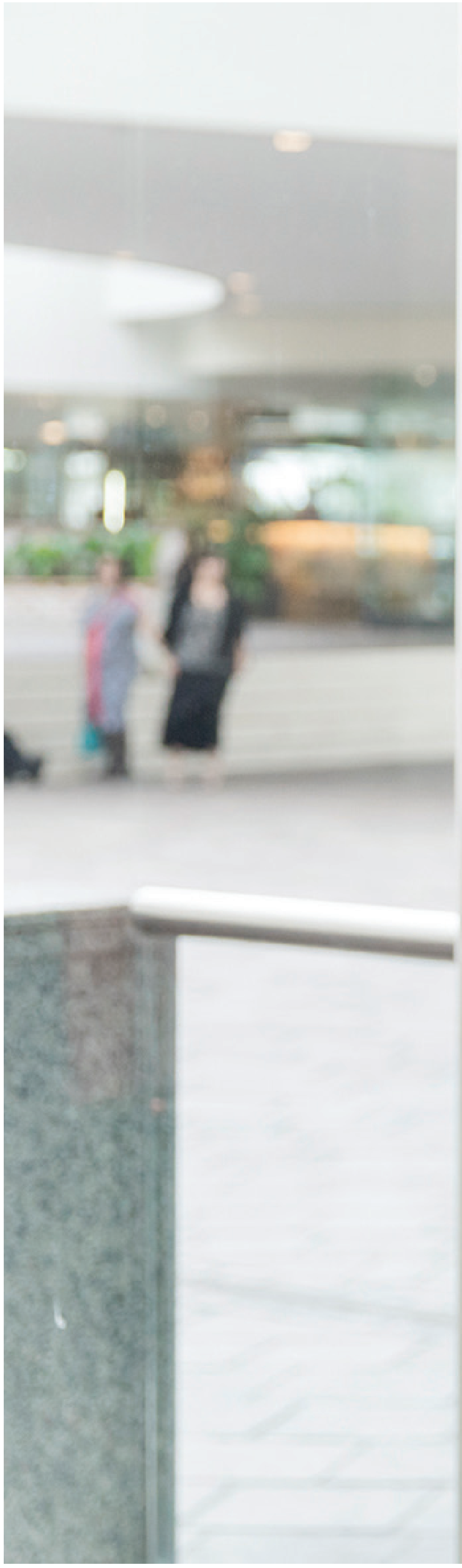
Defining and measuring success

"We've seen success in terms of the value of the stock, but you don't measure everything with that. You also measure with employee engagement. There's no shortcut to the steps you've got to take to bring your employees with you on this fascinating journey that the company is on."

Ajay Banga
MasterCard US

This report is a summary of the key findings in the banking and capital market sector, based on a survey of 176 banking and capital markets CEOs in 62 countries and in-depth interviews with Dr. Nuno Amado, CEO, Banco Comercial Português; Ajay Banga, President and Chief Executive Officer, MasterCard; Greg Becker, President and Chief Executive Officer, Silicon Valley Bank; David Bojanini, President, Grupo SURA; Bill Emerson, Chief Executive Officer, Quicken Loans; Herman Gref, CEO and Chairman of the Executive Board, Sberbank; Don Lam, Chief Executive Officer and Founding Partner, VinaCapital; Brian Moynihan, Chief Executive Officer, Bank of America Corporation; Ralph Hamers, CEO, ING Group' NV; Chitra Ramkrishna, Managing Director and CEO, National Stock Exchange of India Limited (NSE); Eduardo Stock da Cunha, CEO, Grupo Novo Banco and Guillermo Tagle, Chairman, Credicorp Capital.



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