Focus on restructuring:

The drivers shaping the financial services sector

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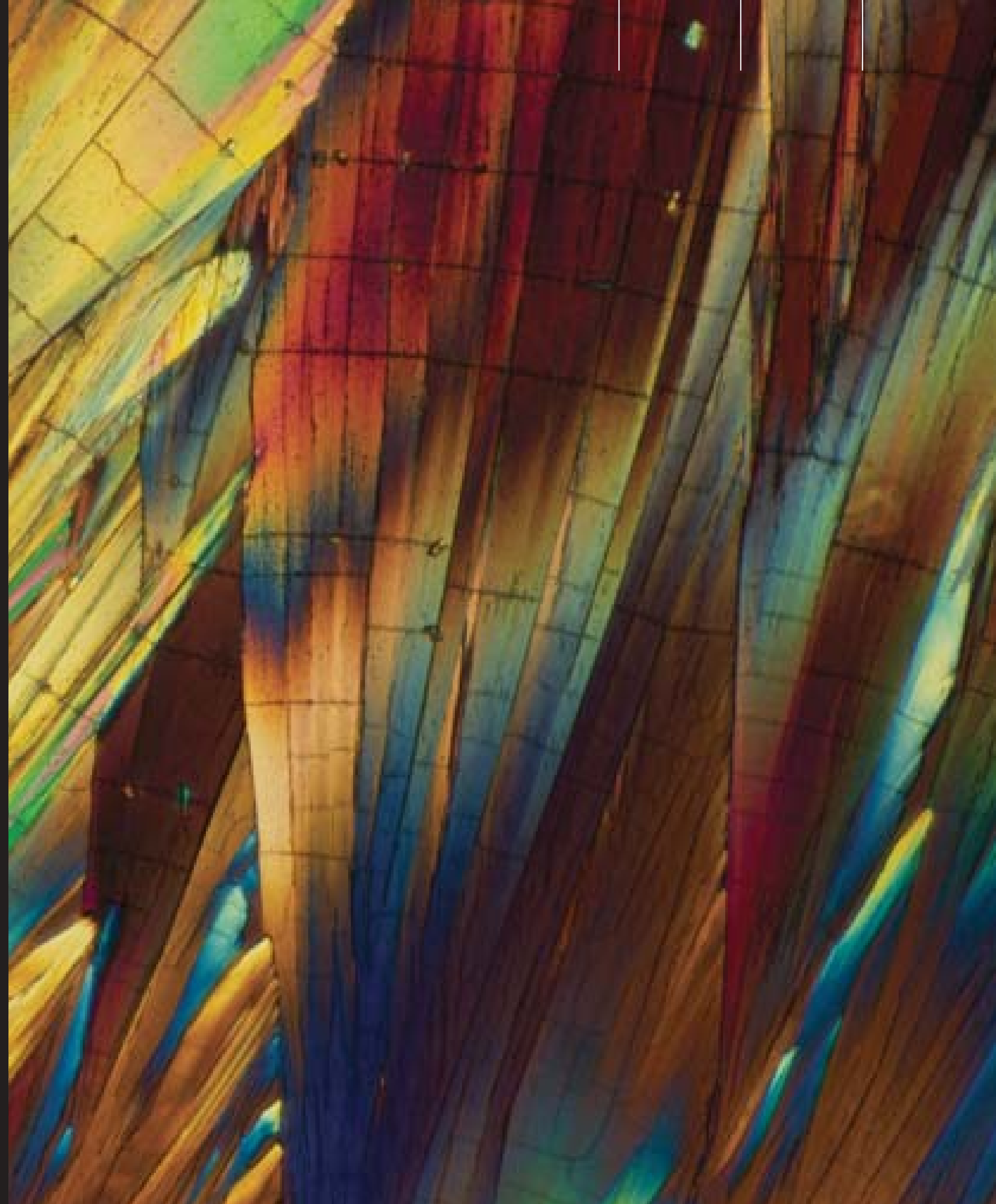

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A joint project with the Economist Intelligence Unit

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Welcome to the seventh in the series of our Financial Services briefing programme, entitled **Focus on restructuring: The drivers shaping the financial services sector**. This briefing, written in association with the Economist Intelligence Unit, examines the wider issues behind the increasing focus on restructuring within the global financial services sector.

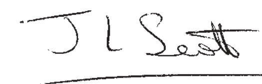
The research effort for this briefing comprised two key global initiatives:

- The Economist Intelligence Unit held over 25 one-on-one interviews with senior executives at financial institutions in the US, UK, Europe and Asia.
- The Economist Intelligence Unit and PricewaterhouseCoopers conducted a special online survey of senior executives in financial institutions on the subject of restructuring. 123 executives from North America, Europe and Asia participated in the survey, which was conducted during September and October 2003.

The interviews and survey findings were further supplemented by significant desk research.

I am confident that you will find this briefing insightful and thought-provoking. Soft copies of this briefing, along with previous briefings on Wealth Management, Economic Capital, Risk Management, The Trust Challenge, IFRS and Compliance are available, free of charge, from our web site www.pwc.com/financialservices

If you would like to discuss the findings of this briefing in more detail in relation to your company please speak with your usual contact at PricewaterhouseCoopers. We would also appreciate your feedback on this briefing as this helps us to ensure that we are addressing the issues that you are most focused on.



Jeremy Scott
Chairman, Global Financial Services Leadership Team

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As confidence in the financial services industry rises and talk of a new M&A wave increases, financial institutions are dusting off their strategies for growth and asking themselves some familiar questions.

What are they best at? What do their customers want? Does this square with their franchise and what the market thinks they stand for? Are they big enough to compete with their main rivals? If not, would they be better off withdrawing from certain markets? But would that increase the risk of being taken over by those same competitors?

This briefing, written by the Economist Intelligence Unit for PricewaterhouseCoopers, finds that a wave of dealmaking is expected in the financial services industry over the next five years. The rationale behind such deals will be traditional enough. Institutions will aim to satisfy the demands of customers by acquiring new products and capabilities and to stave off competitive threats by acquiring market share. They will seek to grow revenue by cross-selling and upselling to complementary client bases. And they will look to realise economies of scale and tighter management of capital and operational efficiencies. But the context for the next wave of restructuring is very different from the last great burst of dealmaking in the mid-to-late 1990s.

First, **regulators are exercising greater influence than ever**. The vigilance of the competition authorities aside, ratings agencies and regulators are forcing some companies to reassess their risk-adjusted returns, to rethink the manner in which they report and to improve their internal processes. In addition, many of the most critical regulations, from Basel II to IFRS, are moving targets. The results of a survey of 123 senior executives in the financial services industry conducted exclusively for this briefing reveal great uncertainty about the impact of regulatory changes on their businesses. Meanwhile, the ratings agencies have in some ways become de facto regulators; rating agency models and the potential for rating changes are becoming increasingly important in shaping the opinions of investment analysts and in determining corporate strategies.

Second, while the compliance burden is rising, **competition is intensifying.** As a result, companies are thinking hard about whether they can afford to remain in marginal businesses and in markets where they lack mass or pricing power. As Nigel Vooght, of PricewaterhouseCoopers in London, says: 'It is clear that across the financial services industry there are as many people who want to get out of particular businesses as there are trying to get in.'

Third, **awareness of the challenges and pitfalls of undertaking mergers and acquisitions is high.** A raft of studies has

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shown that a surprisingly large number of deals fail to add value or even to cover the cost of capital and the usual obstacles to successful M&A – tax issues, local financing preferences and protectionism – have not dissipated. Asked to choose the most effective means of increasing shareholder value, twice as many survey respondents picked organic growth as did mergers and acquisitions. Successful dealmaking requires hard work and serious attention. 'The institutions that stand the best chance of succeeding in mergers or acquisitions are those that have a clear strategy, that communicate directly and clearly with the markets and that have experienced managers who are prepared to give deals the priority and attention they deserve,' says Nick Page, of PricewaterhouseCoopers.

Fourth, **the seeds of economic recovery remain fragile**, and the risk of a consumer-led retrenchment in several developed markets if interest rates start to rise sharply should not be ignored. Many insurers in particular are still facing a capital crunch from which they will recover only slowly. In both more mature markets in the west and faster-growing but unpredictable ones in developing countries, finding sources of profitable revenue growth is easier said than done.

Fifth, **risk appetite in all parts of the market will take time to recover** from the impact of the economic downturn and the effects of recent corporate governance scandals. Investors will need time to regain their enthusiasm for equity investing, with implications for the asset management industry. Regulators and institutional investors are demanding more transparency in reporting results and communication, making it difficult to structure complex deals or launch adventurous products. Reputational risk preoccupies executives and non-executives as never before (see our previous briefing, ***Compliance: A gap at the heart of risk management).***

Institutions still put restructuring at the heart of their strategies. Almost four out of five survey respondents expect their firms to be restructured significantly over the next five years. Bullishly, three in every five respondents said that their organisations did have a track record of success in M&A deals and other forms of restructuring. But in the face of the pressures outlined above, the next wave of restructuring is likely to be characterised by two new attributes: **innovation** and **focus**.

Innovation

The way companies approach restructuring is changing. Although the largest single group of respondents to our survey still thinks straightforward mergers and acquisitions are the way ahead, a majority are pondering alliances, joint ventures and various forms of outsourcing as possible alternatives. For example, retail banks have joined forces o boost efficiency and save costs in

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uncontroversial areas such as cheque clearing. Central banks are also acting as catalysts to cooperation; the Hong Kong Monetary Authority is encouraging banks within the territory, where possible, to consider sharing the burden of complying with Basel II.

Surprisingly, in an industry that depends so heavily on technology to deliver its products and to get close to its customers, a significant proportion of survey respondents said they were prepared to outsource not just call centres and the like, but the infrastructure and applications on which their information technology is based. Indeed, as managers focus their attention on their core competencies, more and more seem prepared to consider outsourcing functions higher up the value chain. Breaks are never entirely clean, however – in any jurisdiction, financial institutions are not permitted to delegate their regulatory responsibilities, only their operational ones. Outsourcing is also likely to be tempered by rising awareness of reputational risk.

Focus

Manulife Financial's recent acquisition of John Hancock and Bank of America's bid for FleetBoston have reinvigorated the debate over the importance of scale to being able to compete effectively, as has the merger between The St Paul Companies and Travelers Property Casualty. 'Deals like these offer companies the potential to reduce their costs and strengthen their margins,' says John Scheid, of PricewaterhouseCoopers in New York. But they do not herald a return to the blockbuster transactions that changed the industry landscape during the 1990s. In the current climate, visionary restructuring is finding it hard to gain support; a warmer reception is given to those that concentrate on filling in specific gaps in their portfolio and getting rid of awkward fits.

Rather than reshaping themselves in one risky bound, institutions will look to execute strategies incrementally, undertaking purchases and divestments, that fit neatly into a coherent strategy – witness the step-by-step expansion of RBS Group in recent months. Instead of seeking to dominate in every segment and territory in which they operate, many institutions will temper their ambitions, looking to expand regionally instead of globally or focusing on particular financial products and services.

Middle-tier institutions in mature markets will be the most likely victims of this trend, as larger institutions seek to consolidate their position in areas of strength and smaller players snap up niche businesses. Even the most innovative outsourcing and alliance strategies are unlikely to help solve the problems of weak market share, inefficient use of capital and inadequate differentiation. Over the next three to five years, therefore, many middle-tier players face an uncomfortable choice between being acquired or undertaking a radical repositioning as a multi-niche player.

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The value of focus will reinforce the rapid development of outsourcing. Deutsche Bank and AMP have already proved unwilling to invest further capital in fund administration and reversed their strategies, selling their in-house third-party administrators (TPAs) and leveraging the service skills of others. Standard Life, often regarded as a conservative institution, recently decided to outsource to Citigroup areas previously considered core. Many more such deals will follow.

Things are not getting any easier for financial institutions. Competition is forcing them to cut costs, while customers are demanding an ever-wider range of products and services. Regulators are increasing the pressure even further. Investors are demanding greater levels of transparency from institutions. 'A clearer understanding of risk-adjusted returns, allied to the need to demonstrate more careful stewardship of investors' capital, is encouraging companies to reassess their positions in certain markets,' says Richard Barfield of PricewaterhouseCoopers. In this environment, restructuring is likely to be realistic rather than radical, focused rather than freewheeling.

Do you measure up?

Whether you are a predator or potential prey, the next five years of restructuring will beg challenging questions of all financial institutions. To succeed, you need to do all of the following:

- **Define a clear strategy.** Only by defining such a strategy is it easy to identify genuine opportunities and to exit, through sale or outsourcing, marginal activities. Successful restructuring requires managers to know which areas of the business are truly core to achieving their goals. 92% of the survey respondents think that restructuring will be important, very important or integral to helping them complete their strategies.
- **Communicate superbly**, both inside and outside the company. If the stock market does not understand an institution's strategy, its shareholders will not endorse specific deals and it will lack the general credibility that brings restructuring opportunities, via investment bankers and other intermediaries, to its door. Research into *ValueReporting™* by PricewaterhouseCoopers has shown that only 10% of investors regard banks' and insurers' financial reports as very useful sources of information. Inside the organisation too, transparent governance and communication are critical to success.
- **Manage regulatory risk.** Regulatory activity will be a key factor over the coming years in determining everything from levels of capital to reporting processes. Survey respondents put regulatory restrictions and regulatory liberalisation above the state of the economy, shareholder demands and the cost of capital as key drivers of

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restructuring activity. 'Winners will understand the current and future regulatory environment and will embed a culture of compliance throughout their organisation,' says Arno Pouw of PricewaterhouseCoopers in Amsterdam. They will also have close relationships with the regulators, enhancing their ability to push through specific deals.

- **Differentiate yourself.** In markets where institutions require scale but where suitable acquisition opportunities are scarce, or where they lack scale and consolidation is likely, differentiation is key to winning the right target or getting the right price. More than a fifth of survey respondents pick out niche players as their most significant competitors.

- **Innovate.** Joint ventures, alliances and creative outsourcing with long-term partners bring risks of their own but can be more effective than mergers, acquisitions and disposals in reaching certain goals – they need to be part of an armoury of restructuring strategies. Survey respondents rate outsourcing as far more effective than M&A at cutting costs, for example; similarly, they reckon alliances are more likely to deliver improved customer service. 'Tired, old models are being consigned to the bin,' says Tom Fenton of PricewaterhouseCoopers in Sydney. 'Innovative approaches are gaining ground.'

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What a difference six months can make.

At the beginning of March, when most stock markets were flat on their backs and economic recovery still seemed a long way off, few financial services firms saw a reason to cheer. Now, suddenly, there is a renewed sense of confidence.

The reasons are not hard to find. A welcome bounce in equity prices since June 2003, after three consecutive years of decline, has come hand in hand with hopes that the world economy may recover more quickly than many had feared. Unsurprisingly, talk of mergers, acquisitions and alliances is on the rise.

The results of a survey of 123 senior financial services executives commissioned exclusively for this report suggest that a new wave of dealmaking may be in the offing. Almost four out of five respondents expect their firms to be restructured significantly over the next five years. Some 92% of respondents think that some form of restructuring will be important, very important or integral to helping them meet their goals.

Indeed, there is already evidence that firms are grasping the opportunity to make acquisitions that will reshape their businesses. Bank of America's $47bn offer for FleetBoston, if completed, will not only give the combined group a near 10% share of deposits across America; it will also put increasing pressure on Bank of America's American and Canadian rivals to seek similar deals to extend their networks and to grow their revenues.

The $11bn purchase of John Hancock, a life insurer based in Boston, by Manulife Financial, a Canadian rival, in September 2003 is another example, as is the planned $16bn merger between The St Paul Companies and Travelers Property Casualty. The deal between John Hancock and Manulife, if it goes ahead, will be the biggest takeover ever by a Canadian company and, at a stroke, will make Manulife the second largest insurer in Canada and one of the biggest in the United States.

All are big deals in terms of price, but none herald a return to the blockbuster transactions that changed the industry landscape during the 1990s. Much has changed since those heady days – the compliance burden is increasingly onerous, institutions are warier of reputational and other forms of risk and, while rising confidence over the state of the global economy may be sparking thoughts of restructuring, that confidence is still fragile. Indeed, more survey respondents identified continuing economic sluggishness over the next five years as an impetus to restructuring than an economic rebound.

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Salad days

Annual volumes of cross-border M&A in financial services.

	Value ($ m)	Deals
1998	115,739.67	701
1999	136,529.97	807
2000	206,952.77	874
2001	105,061.41	790
2002	77,241.52	673
2003*	65,748.06	486

* Up to Q3 2003

Source: Dealogic

For an alternative model, look at RBS Group, which is now the world's fifth largest bank by assets. In quick succession recently, it announced two deals which in themselves are unremarkable, but which taken together exemplify a strategy of growing through manageable acquisition. First, RBS paid £620m for First Active, an Irish mortgage bank. By combining First Active with Ulster Bank, which it already owns, RBS becomes the second largest mortgage bank in Ireland. Private banking is also a growing part of the company's business and, days later, for £227m, it snapped up Bank von Ernst, a Swiss private bank owned until then by Germany's Hypovereinsbank (HVB).

Favouring this model of focused expansion is the fact that the results of past mergers and acquisitions and the large ones in particular, have been patchy. Only 57% of the survey respondents agreed that their own institutions had a track record of success in M&A, dampening the appetite for further restructuring. As one jaundiced executive remarked, 'Things are tough enough at the moment as it is. Most of us want to be left to get on with the day job without having to worry about integrating new people, new systems and new products.' Indeed, the survey showed a preference for organic growth as a means of reaching almost every objective that institutions set themselves – from meeting growth targets and improving customer service to increasing shareholder value and managing risk.

The only exceptions are increasing market share and reducing costs, where M&A activity and outsourcing were recognised as more effective approaches respectively. 'The only way to expand market share is through mergers and acquisitions,' agrees Peter McNamara, chairman of Moneybox, an operator of ATMs in the UK and a former head of strategy at Lloyds Bank, 'but that doesn't mean you can skimp on investment or ignore the need for organic growth.'

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One thing is clear: few senior managers believe their firms can afford to stand still in the face of fiercer competition and pushier customers.

More than 70% of respondents said that increasing competition (such as price cuts and threats to market share) was the main reason for considering some form of restructuring. Another 45% cited the increasing demands of customers (for more flexible products and open-architecture offerings). Faced with a squeeze on profit margins and an increasingly fickle customer base, most institutions cannot rely on organic growth to meet their targets.

So the classic drivers of restructuring – competition and customers – will still be at the root of dealmaking. A majority of respondents in our survey said that boosting market share and meeting targets for revenue growth were the main goals of restructuring over the next five years. The need to expand the number of products or services they offer (cited by 72% of respondents), to expand their distribution channels (59%) and to expand geographic

What will be the main external drivers of your organisation's restructuring activity over the next five years? Please choose up to three answers.

Increasing competition (e.g. price cuts, threats to market share)	73%
Increasing customer demands (e.g. open-architecture products)	45%
Regulatory restrictions (e.g. compliance burden, capital requirements, competition issues)	29%
Regulatory liberalisation (e.g. convergence opportunities, new competitors)	26%
Sluggish state of economy (e.g. need to cut costs, cheap acquisition prices)	21%
Increasing shareholder demands (e.g. demand for transparent reporting and risk profile)	18%
Rebounding economy (e.g. better access to capital, more risk-taking)	17%
Development of outsourcing market (e.g. lower outsourcing costs, better technologies)	17%
Increased access to funding (e.g. lower risk premiums)	13%
Increasing IT costs (e.g. IT integration, security costs)	8%
Higher fixed costs (e.g. property costs)	7%
Higher cost of capital (e.g. regulatory capital requirements)	6%
Other	7%

Source: PricewaterhouseCoopers/Economist Intelligence Unit survey, September-October 2003

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coverage (57%) would be the principal drivers of this activity. On the cost front, respondents will look to reap the same operational efficiencies and economies of scale that have driven previous tides of consolidation.

But when it comes, the next wave of restructuring is likely to be very different from past waves. For one thing, it won't just be about M&A deals – more innovative forms of restructuring will come to the fore. For another, the next wave of restructuring will be about exiting old businesses as well as about getting into new ones.

To understand why, look first at the regulators. The tenor of the next five years will be set by them as much as by institutions themselves. Almost a third of the survey respondents pointed to restrictions imposed on them by regulators (such as tougher rules on compliance, capital needs and competition) as being a key external driver of restructuring.

Almost as many identified regulatory liberalisation as being critical. Some 64% and 53% of respondents respectively said regulatory capital and reporting requirements were the two issues most likely to have an impact on their firm's strategies for restructuring.

What that impact will be is still unclear – a fog of uncertainty hangs over the extent and nature of coming regulatory changes. Asked whether the increasing compliance burden and capital requirements for financial institutions will encourage them to exit existing businesses rather than enter new ones, the overall survey group was strikingly divided – 51% agreed and 49% disagreed. Respondents in Western Europe appeared to feel the weight of regulation more heavily than other regions: 62% of them agreed they would be likelier to exit businesses than seek out new ventures as a result of compliance requirements.

Please state whether you agree or disagree with the following statement: The increasing compliance burden and prudential/capital requirements for financial institutions will encourage them to exit existing areas of business rather than enter new ones.

Agree	51%
Disagree	49%

Source: PricewaterhouseCoopers/Economist Intelligence Unit survey, September-October 2003

Take the impact of Basel II, a new framework for matching banks' regulatory capital requirements more closely to the credit risk ratings of their borrowers that will benefit some banks and disadvantage others. More capital will be required for lending to poorly rated companies and for complex products such as securitised bank loans. This is likely to reinforce a trend that started in the mid-1990s for selling credit risk to non-bank investors:

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the world's biggest banks are reducing their overall exposure to credit risk with the use of loan sales, asset-backed securities and credit derivatives. Although lending by banks will continue to grow, a good chunk of the lending risk is being laid off elsewhere – with insurance companies and loan mutual funds.

Some banks, such as those with sizeable consumer businesses, should benefit from the new rules on capital adequacy to be introduced under Basel II. In theory, such banks could set aside less capital for certain risks, giving them more headroom to make acquisitions. Indeed, since US regulators have said that only 12 of the country's largest banks, which between them carry out 99% of the country's foreign banking, will fall within the Basel II net, some European banks may actually gain a competitive edge over US institutions. In practice, however, the need to deploy extra funds to cover operational risk and the uncertain reaction of the ratings agencies to any reduction in capital, may nullify this potential source of advantage.

As for reporting requirements, the use of International Financial Reporting Standards (IFRS) by listed companies in the EU from the start of 2005 will also have a significant impact. The aim of IFRS is to help improve the transparency of financial disclosures, reduce anomalies and boost the development of Europe's financial markets (for more on IFRS, see ***Illuminating value: The business implications of IFRS***, published in March 2003). The precise nature of IFRS in financial services is still in flux, but the likely requirement for firms to use fair-value accounting is expected by many to deter institutions from shouldering as much risk on their balance sheets, for fear that the resultant volatility would show up in their results. For life insurers in particular, IFRS could make guaranteed products and with-profits policies far less attractive.

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German banking: In need of repair

Regulators are not just tightening rules. Almost as many respondents to our survey chose regulatory liberalisation as a driver of restructuring. And there are plenty of opportunities to exploit. Take Germany, whose banking market is ripe for reshaping.

In most need of rebuilding are the public-sector banks, which make up the first of the industry's three main groupings and include the regional banks (Landesbanken) as well as the savings banks (Sparkassen). But because the country's economy has been wobbly of late, neither the privately-owned commercial banks (such as Commerzbank and Deutsche Bank), which form the second grouping, nor the credit co-operatives (Volksbanken and Raiffeisenbanken), which make up the third, have entirely escaped an overhaul.

Together, the publicly owned Landesbanken and Sparkassen control around 36% of total banking assets in Germany. Add in the building and loan associations and a gaggle of public banks with special functions and the amount in public hands in one way or another rises to a whopping 45%.

Until recently, the Landesbanken enjoyed the support of laws under which the regional authorities not only protected the banks but guaranteed their liabilities. Unsurprisingly, this meant that the Landesbanken enjoyed high credit ratings and could thus borrow cheaply.

Until, that is, the European Union decided that this legislative buttress must go. Under the new rules, liabilities created before July 2001 will be covered until maturity; those created between July 2001 and July 2005 will be covered but only if they mature before the end of December 2015. Without state guarantees, the banks' credit ratings will tumble and their borrowing costs will soar. And without a subsidised cost of capital, the Landesbanken will have to compete more directly with the private commercial banks – a prospect that is sending ripples throughout Germany's banking system.

Alexander Stuhlmann, chairman of the board of the North German Landesbank HSH Nordbank, says that his bank is employing a range of strategies to navigate the obstacles ahead. Some are internal. For example, instead of focusing primarily on the credit business (which accounts for around 80% of Landesbanken earnings) the bank wants to generate fee income as well. With good reason. 'If a bank focuses exclusively on its credit operations, it will have a return on equity of no more than 10% to 13%.

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But if it manages to generate a significant portion of its earnings from services that carry no risk and tie up no capital, then the return on equity rises,' says Mr Stuhlmann.

HSH Nordbank, which sees itself in the vanguard of reorganisation, is investing in new products and people. It plans to syndicate some of its debt and to place other credit business with investors. The important thing, says Mr Stuhlmann, is to develop a better mix of business. Or banks can opt for external changes, like mergers: HSH Nordbank itself was formed by the June 2003 merger of Hamburgische Landesbank and Landesbank Schleswig-Holstein.

More such mergers are likely to follow. The removal of state guarantees, the reduction in credit ratings, together with fall-out from the planned introduction of Basel II, as well as the need to cut costs, are all likely to spur a faster pace of change within Germany's banking industry. Dr Max Häring, chairman of the board of Landesbank Saar, reckons there could well be mergers between individual savings banks. But he doubts whether there will be deals between savings banks and private banks – in other words between one industry grouping and another.

This may not be enough to satisfy the privately-owned commercial banks. They point out that the public-sector banks will continue to have a competitive advantage because they will still enjoy higher credit ratings than some of their privately-owned rivals and because they won't have to stump up regular dividends. Critics argue that the ideal solution would be for commercially competitive public-sector banks' operations to be privatised. Even in a period of regulatory flux, that may prove too big a pill for the country's legislators to swallow.

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Where will the next wave of restructuring activity be most focused?

Basel II should help precipitate banking consolidation in many markets, as should the impact of expected rises in interest rates on consumer spending. But three other sectors also come to mind – insurance, asset management and alternative investments.

Insurance first. In Europe, a combination of falling stock markets and a period of economic malaise have left many insurers weakened and introverted. In the past, life companies, as well as those insuring general risks, have been a reliable source of capital for the financial markets. No longer. Unprofitable underwriting and falling share prices have taken their toll, as has a period of the lowest interest rates in decades. All this has led to a capital crunch among insurers of all types.

Although stock markets have helped them of late, many insurers' and reinsurers' credit ratings have deteriorated for much of the year, so adding to their cost of capital. Since many reinsurers have been in a similar plight, insurers have been unable to find great shelter there either.

Matters will be made worse by the planned introduction of stiffer standards of reporting and disclosure under IFRS in many parts of the world. This will make insurers' accounts more transparent and so make it harder for them to hide businesses which soak up a lot of capital but which deliver inadequate returns. 'It will become more apparent which bits of an organisation's business are capital-efficient and which are not,' says Charles Garnsworthy of PricewaterhouseCoopers in London. As a result, companies will come under pressure to improve their returns or reduce their exposure to these businesses, perhaps through joint ventures or by selling them altogether.

In consequence, the deals that are being done are about tidying up and strengthening portfolios as much as about aggressive expansion. For example, Zurich Financial recently sold its life business and parts of its non-life operation in France to Generali of Italy and in the Netherlands to SNS Reaal Groep. Banks that do not see a long-term future in insurance are likely to grasp the opportunity to withdraw and an increasing number are hiving off their insurance interests into joint ventures. Earlier this year ABN AMRO did so in a deal with Delta Lloyd. ING entered a similar arrangement with Australia's ANZ Bank. Others may follow.

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Banking on insurance

Bancassurance, a way of selling insurance products through banks' branches, can be tricky. In theory, it has an appealing symmetry to it: banks can make better use of their branches and staff by selling a range of complementary products to the same customers. Everybody gains: the bank collects a handy commission and the insurer has access to customers it might otherwise find it hard to reach. In practice, it doesn't quite work like that.

Deals between banks and insurers seem to work best in countries where the bank manager is still regarded as a part of the community. Bancassurance has also caught on more in countries where the market for private pensions is still undeveloped. Bancassurance is booming in Spain and Italy and seems to work well in parts of France and the Benelux countries. The UK, Europe's biggest market for insurance, has proved a tougher market to crack, as has Germany, (although Allianz, the country's largest insurer, still hopes that its purchase of Dresdner Bank in 2001 will one day pay off). In Switzerland, Credit Suisse has had to pour billions of francs into its insurance offshoot, Winterthur.

Elsewhere, looser alliances appear a better bet than mergers and acquisitions. Since 2001 Barclays has had a relationship with Legal & General (L&G), an independent insurer, which sells its products through Barclays' branches. L&G has similar arrangements with Alliance & Leicester and Northern Rock; it recently also struck a deal in Britain with National Australia Bank which owns Clydesdale, Yorkshire and Northern Bank, all of which have big mortgage businesses.

Such deals may become more popular in future as banks everywhere reassess whether they can afford to have capital tied up in their own insurance offshoots. Until now, banks have counted the value of their insurers against so-called Tier 1 capital. But they have also been allowed to deduct that figure from their overall level of capital. Not so under Basel II, which will require half the value of insurance subsidiaries to be deducted from Tier 1 and half from Tier 2. This will prove less favourable for most banks and could result in more insurance subsidiaries being put on the block.

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Europe's life insurers may be looking inward, but many of those in North America are eyeing each other up as potential partners. Three recent deals – Manulife Financial's $11bn bid for John Hancock of Boston, the purchase of Mony Group by France's AXA Financial and the planned $16bn merger of The St Paul Companies and Travelers Property Casualty – have confirmed what many had suspected: North America's life-insurance market is ripe for consolidation. Around ten big deals have either been announced or are reckoned to be in the pipeline.

At the last count, according to Standard & Poor's, there were 50 large life-insurance groups in the US. Five of them are giants, led by AIG; many of the rest could seek partners in the coming months and years. The process has been made easier by the fact that many have demutualised and become listed companies. At one point the bulk of America's life insurers were owned by their policyholders; now only about 30% are. Being listed on the stock market has proved a double-edged sword: it has enabled the companies to pay for acquisitions with their shares but it has also made the companies themselves more accessible to predators.

As well as insurers, the asset and fund management sectors are also in the limelight as a focus of restructuring. The three-year bear market in shares wiped the smiles off their faces as the value of their clients' assets tumbled. A few unsuccessful fund managers have been forced to sell the right to manage some of their funds; successful ones have been cherry-picking the assets they want.

Although the partial recovery in stock markets since March has relieved some of the pressure on fund managers, it has done little to persuade investors that they should again put the vast majority of their savings into equities, the most profitable part of the managers' business. Expect more mergers and alliances and greater outsourcing by asset gatherers in the coming months and years as they seek out economies of scale and greater efficiencies.

A fresh wave of consolidation is expected not just among investment managers (the manufacturers of the product), but among service providers too. Since firms still find it difficult to vault tax and regulatory barriers, this could lead to increasingly flexible arrangements between investment managers and those who distribute their products.

According to ***Changes on the Horizon***, a new survey on Global Investment Management from PricewaterhouseCoopers, fund managers are likely to concentrate on expanding revenue from higher-margin products with successful track records. Managers are unlikely to chance their arm, or their bottom line, on exotic new products that may, or may not, become popular with investors, particularly if financial markets remain volatile and risky.

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Although risk aversion is likely to be a theme of the next five years, among institutions and retail investors alike, there is a countervailing current of risk-taking to consider. As banks retreat from certain areas of riskier lending, there will be more use of private equity to fill the gap. Barclays' recent acquisition of Gerrard Management Services and RBS Group's purchase of Bank von Ernst are recent examples of a quickening interest in private-client businesses.

Alternative investment vehicles are becoming available to a wider public, albeit with safeguards to protect the unsophisticated and are providing a source of liquidity and speculative risk-taking to the market. The rise of hedge funds (see box, Small is beautiful) will continue and should help offset another strong trend: the greater use of investment products that track indexes. Too much indexing can hinder the process of price formation, another reason why the growth of hedge funds may not be discouraged by enlightened regulators.

Small is beautiful

When Sandy Weill, 70, bowed out in October as chief executive of the world's biggest financial services group, he did so in style. Citigroup, the company he created, reported a 20% rise in net income for the third quarter to a record $4.7bn. In Mr Weill's eyes, big may still be best, yet an increasing number of people who work on Wall Street and in financial markets elsewhere reckon that small is gaining ground. Fed up with working for large organisations, more and more executives are setting up on their own.

Indeed, everywhere that there is a deal to be done, money to be managed, a specialist trade to be executed or advice to be given, boutiques are springing up. At the last count, according to Euromoney, there were 5,000 hedge funds worldwide. That is more than 50 times the number 20 years ago and probably double the number only a few years back.

Although the fund management industry in general has been going through a difficult patch, independent managers with specialist mandates are showing giddy growth.

One reason, of course, is that over the past three years, as markets have fallen, thousands of experienced people have been let go by the big investment banks and financial services groups. At their peak the bulge-bracket investment banks in the US had an average of 1,800 people working in their advisory departments. Now that number has been cut by more than half.

As happened in California at the height of the technology boom, this has spawned not just a new wave of start-ups but a new way of working. These days, hedge fund managers are as likely to stroll to work at the bottom of the garden as they are to set up shop next to their former employer.

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Small is beautiful continued

Technology has made it as easy to work from home as it is to trade from the top of a tower in the City of London. The surge in the market for credit and other forms of specialised derivatives has also given rise to the need for specialist advice – advice that the large investment banks, which themselves trade in these securities, are not always best placed to give.

The biggest investment banks retort that they are still attracting an increasing proportion of the deals on offer. But competition is pushing down fees and forcing banks to share mandates for debt and equity underwriting among a wider and wider circle. True, the trend may be reversed when the flow of deals picks up, but by then an increasing number of boutiques will have made their mark. It is interesting to note, in this regard, the small but significant threat niche players represent in the minds of the survey respondents.

Which category of institutions represents the most significant competitive threat to your organisation over the next five years? Please choose one answer only.

Category	%
Established broad-based financial institutions already competing in your market	50%
Niche players	21%
Established broad-based financial institutions moving from one market to another	17%
New competitors moving from retailing into financial services	8%
Start-up institutions	3%
Other	1%

Source: PricewaterhouseCoopers/Economist Intelligence Unit survey, September-October 2003

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What role will globalisation play in the next wave of restructuring in the financial services industry?

Emerging markets cannot be ignored, both as outsourcing locations (of which more below) and as a source of growth. Over time, China and India are likely to be two of the world's largest markets for banking and other financial services and they already offer opportunities. India now accounts for more than 15% of Standard Chartered's overall profit, for instance, yet it has only 2% of the country's total banking market. As in China, there remains a lot of market to play for.

That said, many banks owe the recent improvement in their profits to the resilience of their domestic operations, not to gains from overseas. Indeed, some European banks have taken steps to withdraw from marginal businesses in Latin America and elsewhere, as a way of reducing their risk. Tax and regulatory obstacles to expansion overseas are also likely to temper instincts to rush into new markets and, unsurprisingly, most survey respondents picked their own regions as places where they expect to make acquisitions over the next five years.

Overall, Western Europe came top of the list of regions in which respondents expect to expand. The next couple of years could see a wave of consolidation among the continent's 5,000 or so co-operative banks – with total customers, according to the *Financial Times*, of 100m people.

In terms of the geographic distribution of your organisation's dealmaking and restructuring activity over the next five years, please identify in which of the following areas you expect to *expand your activities through acquisition*. Please choose as many answers as apply.

Region	%
Western Europe	45%
South Asia (China, ASEAN, India)	40%
North America	39%
Latin America	26%
Eastern Europe	25%
North Asia (Japan, Korea)	13%
Australia/NZ	12%
Middle East	9%

Source: PricewaterhouseCoopers/Economist Intelligence Unit survey, September-October 2003

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Many have already huddled together under three main umbrellas: Rabobank in the Netherlands, Oko Group in Finland and Germany's BVR. Further consolidation is likely and there are successful models to follow, two of them, curiously, from rule-bound France. By floating its central body on the stock market last year, Crédit Agricole gave itself the clout and currency with which to acquire Crédit Lyonnais. In doing so, it vaulted into a different league. Caisse d'Epargne recently agreed to merge its commercial arm with that of Caisse des Dépôts et Consignations – a deal that could benefit both banks. Expect more savings banks and co-operatives to follow suit.

In markets such as the UK, Spain and Scandinavia, where consolidation is already further advanced, cross-border activity is the obvious avenue of growth. Entering markets through acquisitions may lose ground to more innovative strategies, however. Peter McNamara at Moneybox reckons that in small countries with concentrated populations, a limited network of branches, complemented by a developed ATM infrastructure, may be enough to conquer new markets. He estimates that in the UK a foreign bank would require just 400 branches to reach 90% of the population. Indeed, ING Group has made headway with its savings products of late with little or no branch network.

Across the Atlantic, the US banking market looks even more fragmented than Europe's. A few years ago, there were 13,000 independent banks in the US; now there are closer to 8,000. Many believe that number could soon fall again as outsiders, particularly consumer banks from Europe, look for acquisitions.

US banks, hobbled by lawsuits and ethical censure following the collapse of Enron and other accounting scandals, are also likely to look first to their home market for growth. Many local institutions are opening new branches as a way of attracting cheap deposits during a period of low interest rates. But here too expansion will be tempered by caution. According to Ajay Banga, president of North American retail banking at Citicorp, it usually makes more sense to buy branches from competitors than to open new ones. Not surprisingly, Citicorp reserves its openings of new branches for only a handful of choice locations.

In Latin America, Brazil is likely to be the only market big enough and stable enough to attract international interest in the foreseeable future. Some, like ABN AMRO (through Banco Real), already have sizeable businesses there. Others, like HSBC, are taking opportunities as they see them. Argentina will remain a low priority while it continues to wrestle with the International Monetary Fund over its obligations to international creditors.

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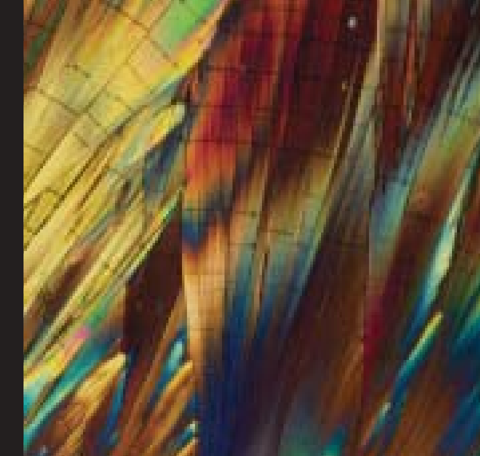

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Interest in Asia is high around the world.

A third of North American respondents and 40% of Western European respondents have set their sights on the region as an important target for acquisition activity. Yet there are good reasons to doubt that Western banks will follow through on all their ambitions.

After all, they haven't yet, despite serious encouragement. A great need to recapitalise local banks after the region's financial crisis of 1997-98 led governments, notably in South Korea, Thailand and Indonesia, to throw open their banking systems to foreigners. On the whole, big foreign banks declined to come in. This coyness strikes some as strange. In the light of an Asian boom in consumer finance, surely big regional or multinational banks are just the ones to profit from cross-border moves to bring in the branding, marketing and systems expertise needed to handle a sizeable consumer-finance operation? Yet the coyness is likely to continue.

Only three Asian economies – Japan, China and South Korea – are sufficiently big to feature in most global banks' strategic calculations. But all present significant challenges.

In Japan, the failures of the financial institutions in 1997 have encouraged the financial authorities to tighten supervision, although there is plenty of scope for further work in areas such as rules for deferred tax assets. Foreign-owned financial institutions have taken advantage of bankruptcies of life insurance companies, banks and securities houses to strengthen their presence in the market. The attractiveness of the Japanese market to foreign capital will rest largely on whether, as the population ages, the savings ratio will increase as people prepare for retirement or decrease because of extremely low interest rates.

In China, the state banks, though technically insolvent, still hog the show. Even when foreign capital is invited in, the regulatory climate remains unpredictable: look at Newbridge Capital's attempt to acquire a controlling stake in Shenzhen Development Bank, rebuffed despite a slew of central-government assurances.

The transformation of South Korea's banking system is extraordinary. Yet even there, politics can stymie things. A local uproar denied HSBC the chance to buy Seoulbank, on the grounds that HSBC was being sold national treasures on the cheap.

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For global banks, the lengthy negotiations with government involved in buying distressed local banks, the unsolved challenge of turning huge potential into actual profit and the need for considerable investment make the process very much less attractive than supposed. For this reason, many acquisitions in most Asian markets will continue to be sweetened by a large dollop of opportunism.

It is important, however, not to paint too bleak a picture of Asia's financial prospects. Unlike Western Europe and North America, where the proportions of survey respondents expecting to buy and sell are broadly comparable, significantly fewer institutions expect to divest operations in Asia than to make acquisitions. This will, for many years, remain the world's most vibrant region, with opportunities for foreign banks as well as local ones. For instance, consumer-finance operations benefit enormously from economies of scale and only the biggest banks can truly reap them. That is why the processing centres that HSBC has in Guangzhou, Hyderabad and Bangalore, or Standard Chartered in Kuala Lumpur and Chennai, are likely to bring striking gains for these two banks and those that mimic them.

China's insurance market: Ajar

It may be a tough market, but China's potential will keep encouraging outsiders to take risks. Foreign insurers are falling over themselves to get into the country, for instance, and it is not hard to see why. According to the China Insurance Regulatory Commission (CIRC), total insurance premiums written in the country during the first six months of this year were 212.6 bn yuan ($25.7bn). That was 32% more than in the same period last year.

Life-insurance premiums, at 165.3 bn yuan, were up by even more. Low interest rates, a volatile stock market and lower state benefits have encouraged many Chinese, who traditionally save a lot, to look for other ways of providing for their families and old age. For the moment, participating life products, which secure the capital paid down and offer higher returns than those available from bank deposits, seem to fit the bill. David Campbell of PricewaterhouseCoopers in Shanghai estimates that at least 60% of new life policies written in China are participating. According to the Financial Times, 17% of individual life policies were sold by banks in 2002, up from virtually nothing the year before.

A snag is that the market is opening up to foreigners much more slowly than it is growing. Under the terms of China's entry into the World Trade Organisation (WTO) in

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China's insurance market: Ajar

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2001, foreign insurance companies will be able to acquire licences to operate nationally in 2005. Until then, the CIRC is granting licences for branches one at a time.

Even when they are allowed into the country, overseas life insurers are obliged to set up joint ventures with domestic partners whose main business does not have to be, and rarely is, insurance. Chinese partners can often bring handy contacts with government officials but, because of cultural differences, often fail to see eye to eye with their foreign partners.

An exception to most rules in China is AIG, America's insurance giant. AIG started doing business in China before the Second World War and has been operating profitably there for several years. It recently took the ambitious step of buying a 9.9% stake in PICC, the first of three big Chinese insurers due to list their shares internationally over the next few months.

AIG's expertise could prove useful for PICC, which has 70% of China's market for property insurance and may need help to keep the lid on expenses at its 4,300 branches. By helping to train PICC's 26,000 sales staff and 65,000 agents, AIG hopes in return to open the door to higher sales of its own products and services.

But foreign insurers without a toehold in China should not lose hope. The market is likely to continue growing at a fast clip. And there is more than enough room for new entrants. Although by far the dominant foreign insurer in China, AIG had a mere 1.9% of the life market in 2001 and a trifling 0.3% of the market for property insurance.

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It is clear from the survey that not all companies will plump for a big takeover as their chosen restructuring vehicle, even if they have the capital.

Many may opt for alliances or joint ventures as a way of boosting their sales. To cut costs, others may simply outsource more of their operations, particularly those in the back office or in information technology. Asked which strategies would be the primary focus of their organisation's restructuring activities over the next five years, more respondents plumped for innovative approaches such as JVs, alliances and outsourcing than did for M&A and divestitures.

Which of the following strategies will be the primary focus of your organisation's restructuring activities over the next five years? Please choose one answer only.

Strategy	%
M&A	42%
Alliances	21%
Outsourcing	17%
Joint ventures	16%
Divestitures	4%

Source: PricewaterhouseCoopers/Economist Intelligence Unit survey, September-October 2003

Outsourcing is no longer regarded simply as a way of cutting costs. Many see it as a logical result of the need by financial services firms to stick to what they do best. Why waste capital and management time trying to stay on top of a back-office function that is incidental to the business and that contributes little or nothing to the bottom line?

'Lift-outs', as they are known, are popular among asset gatherers and fund managers, for whom processing paperwork and holding documents can be a chore. Typically, the service provider takes on not just the book of business but the staff, part of the existing IT systems and often the building in which employees sit.

Mark Speller, a corporate finance partner at PricewaterhouseCoopers, confidently predicts that over the next few years outsourcing will continue to 'move from more basic administration services into higher added-value areas and (eventually to) complete end-

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to-end service provision'. 'This development will completely transform business models,' says Mr Speller. 'Financial institutions will allocate capital, develop products and enhance sales channels, whilst transaction processing will be carried out by other types of organisation.'

In our survey, for example, fully 75% of respondents cited IT infrastructure and applications as an area in which they would expect to expand their outsourcing. JP Morgan and Chase Manhattan did exactly that when they merged in 2002 and claim to have cut more than 15% from the combined group's IT budget. As part of a $5bn deal over seven years, IBM assumed responsibility for JP Morgan Chase's IT infrastructure, data centres and all its networks. Similarly, ABN AMRO awarded EDS a $1.3bn contract at the end of 2002 to provide technology services and applications development for its wholesale business.

Financial institutions will outsource to both domestic and offshore service providers, but Asia will be a particular centre of activity. The region's plentiful supply of high quality and low-cost labour will spark contracts and acquisitions by major financial services and outsourcing services groups seeking lower processing costs. Capita's recent acquisition of 60% of Mastek, an Indian outsourcing firm, is a case in point, as is the recent decision by HSBC to transfer a further 4,000 jobs from Britain to the bank's existing processing centres in India, China and Malaysia. Outsourcing specialists in India in particular have raised their game: they now do everything from writing programs to installing enterprise software and monitoring computer systems from afar, as well as performing voice and text messaging services plus higher value-added services.

There are risks in the outsourcing trend, however. The danger is that, by hiving off the parts of their operations that keep the organisation's heart beating, companies will lose one of their main sources of competitive advantage. The logical implication is that, at some point in the future, bargaining power will switch away from the financial institutions and towards the service providers as they build up critical mass in their businesses. There are also questions about the ability of financial institutions to ensure that the offshoots they have hived off comply with the necessary regulations. A break is never clean. In some jurisdictions, particularly in Eastern Europe, certain activities cannot be outsourced at all because regulators fear the implications of loss of control on retail investors or policyholders. In others, management are allowed to make their own decisions about operational arrangements but retain full regulatory responsibility, and therefore the risk, if things go wrong.

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In terms of business functions, please identify in which of the following areas you expect to *expand your outsourcing activities.* Please choose as many answers as apply.

IT infrastructure and applications	75%
Human resources & training	42%
Customer contact centres	39%
Finance & accounting functions	36%
Procurement	20%
Supply-chain management	17%
Other	8%

Source: PricewaterhouseCoopers/Economist Intelligence Unit survey, September-October 2003

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The pressures on financial institutions to restructure are immense – tougher competition, squeezed margins and more demanding customers make inertia impossible.

But the environment over the next five years will be less conducive to risk-taking than it once was. The only certain thing about the regulatory landscape is that it is in flux; governance scandals and shareholder demands for greater transparency will reinforce an aversion to risk; continuing uncertainty about the economic climate means that growth aspirations will be tempered by a need to cut costs; and regions that offer the greatest growth potential also entail the greatest gambles.

There will be restructuring and lots of it, but much of it will be designed to sharpen focus, improve efficiency and take incremental steps forward. There will be blockbuster deals, of course, but the approach of building by smaller steps, as popularised by the likes of RBS Group, is likely to become more common. Risky mega-mergers of equals will be avoided. As institutions attune their capital management to the risks they face and strive to be better stewards of their shareholders' capital, firms will reassess their positions in certain markets.

In this environment, communication will be central to success. 'Articulating the strategy behind restructuring will become ever more critical,' says Nick Page of PricewaterhouseCoopers. Winning the stock market's support will be crucial not just in courting shareholders' approval for a particular deal; it will also be vital for a company to be credible in the eyes of the market, so that opportunities come its way in the first place. As reporting requirements and greater activism on the part of investors enhance the value of transparency, communication skills are likely to become as important as dealmaking ability in the months and years ahead.

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The Economist Intelligence Unit and PricewaterhouseCoopers conducted a special online survey of senior executives in financial institutions on the subject of restructuring. Executives from 123 institutions in North America, Europe and Asia participated in the survey, which was conducted during September and October 2003. Our thanks are due to all those who responded, for sharing their insights with us.

Please note that totals do not always add up to 100 because of rounding, or because respondents could choose more than one answer.

Section 1: About you

1. In which region are you personally located?

Africa	3%
Asia	23%
Australia/NZ	7%
Eastern Europe	6%
Latin America	8%
North America	23%
Western Europe	30%

2. In which region is your organisation headquartered?

Africa	5%
Asia	18%
Australia/NZ	7%
Eastern Europe	2%
Latin America	7%
Middle East	1%
North America	32%
Western Europe	30%

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3. What is your area of responsibility?

Senior management (CEO, CFO, COO, Chairman)	31%
Finance	11%
Strategy/planning	11%
Risk management	7%
M&A	5%
Marketing and communications	5%
Compliance	3%
Operations	3%
Internal audit	2%
Treasury	1%
Other	21%

4. What industry sector of financial services do you personally focus on? Please check as many areas as apply.

Retail banking	25%
Investment banking	21%
Life insurance	20%
Non-life insurance	16%
Investment management	34%
Capital markets	23%
Private equity	16%
Corporate banking	25%
Private banking	16%
Outsourcing services provision	9%
Other	11%

5. What was your organisation's total global income, in US dollars, in 2002?

Less than $500m	41%
$500m-$1bn	13%
$1bn-$3bn	10%
$3bn-$8bn	11%
Over $8bn	25%

6. How many mergers and acquisitions has your company conducted over the last three years?

0	27%
1-2	21%
2-5	22%
5-10	16%
10-25	3%
25 and above	11%

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Section 2: Drivers of restructuring

7. Do you agree or disagree with the following statements?

	Agree	Disagree
Our organisation will undergo significant restructuring over the next five years	78%	22%
Our organisation is already structured in the way we want	34%	66%
Our organisation has a track record of success in M&A and restructuring	57%	43%

8. How central is M&A and other restructuring activity to the completion of your organisation's business strategies?

Absolutely integral	22%
Very important	40%
Important	30%
Unimportant	5%
Completely irrelevant	3%

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9. What will be the main external drivers of your organisation's restructuring activity over the next five years? Please choose up to three answers.

Driver	%
Increasing competition (e.g. price cuts, threats to market share)	73%
Increasing customer demands (e.g. open-architecture products)	45%
Regulatory restrictions (e.g. compliance burden, capital requirements, competition issues)	29%
Regulatory liberalisation (e.g. convergence opportunities, new competitors)	26%
Sluggish state of economy (e.g. need to cut costs, cheap acquisition prices)	21%
Increasing shareholder demands (e.g. demand for transparent reporting and risk profile)	18%
Rebounding economy (e.g. better access to capital, more risk-taking)	17%
Development of outsourcing market (e.g. lower outsourcing costs, better technologies)	17%
Increased access to funding (e.g. lower risk premiums)	13%
Increasing IT costs (e.g. IT integration, security costs)	8%
Higher fixed costs (e.g. property costs)	7%
Higher cost of capital (e.g. regulatory capital requirements)	6%
Other	7%

10. What will be the main goals of your organisation's restructuring activity over the next five years? Please choose up to three answers.

Goal	%
Meeting revenue growth targets	55%
Increasing market share	50%
Increasing shareholder value	46%
Reducing costs	41%
Improving customer service	27%
Focusing on core businesses	25%
Improving capital efficiency	16%
Managing the organisation's risk profile	14%
Meeting evolving regulatory requirements	11%
Accessing new talent	9%
Other	2%

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11. What growth-related objectives are likeliest to drive M&A and other restructuring activity at your organisation? Please choose up to three answers.

Answer	%
Need to expand product/service offerings	72%
Need to expand distribution channels	59%
Need to expand geographic/regional coverage	57%
Need to acquire certain technologies	20%
Need to reposition organisation to exploit regulatory changes	19%
Need for personnel to acquire certain skills	16%
Need to access sources of funding	13%
Other	3%

12. What cost-related objectives are likeliest to drive M&A and other restructuring activity at your organisation? Please choose up to three answers.

Answer	%
Maximising operational efficiencies (e.g. centralised back office)	62%
Achieving economies of scale	61%
Minimising cost of capital	35%
Exiting underperforming and non-core businesses	34%
Reducing headcount	24%
Exiting underperforming and non-core markets	18%
Reducing IT costs	16%
Other	3%

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13. Please state whether you agree or disagree with the following statement: The increasing compliance burden and prudential/capital requirements for financial institutions will encourage them to exit existing areas of business rather than enter new ones.

Agree	51%
Disagree	49%

14. What are the regulatory and compliance issues that are most likely, in your view, to have an impact on your organisation's M&A and restructuring strategies? Please choose up to three answers.

Regulatory capital requirements	64%
Reporting requirements	53%
Directors' compliance requirements	34%
Data protection rules	34%
Money-laundering regulations	31%
Exchange listing rules	12%
Other	6%

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Section 3: The mechanics of restructuring

15. Which of the following strategies will be the primary focus of your organisation's restructuring activities over the next five years? Please choose one answer only.

M&A	42%
Alliances	21%
Outsourcing	17%
Joint ventures	16%
Divestitures	4%

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16. Which of your organisation's goals are best achieved through which of the following strategies? Please choose one strategy only for each goal.

	Organic growth	M&A	Divestitures	Joint ventures	Alliances	Outsourcing
Meeting growth targets	45%	29%	0%	5%	18%	3%
Reducing costs	15%	11%	12%	4%	4%	54%
Increasing market share	23%	47%	0%	6%	22%	2%
Focusing on core businesses	51%	4%	21%	4%	9%	11%
Increasing shareholder value	52%	25%	7%	5%	8%	3%
Meeting evolving regulatory requirements	46%	15%	9%	8%	11%	11%
Accessing new talent	41%	29%	1%	9%	12%	8%
Improving capital efficiency	32%	29%	16%	5%	3%	15%
Managing risk profile	54%	11%	12%	7%	6%	10%
Improving customer service	59%	7%	2%	5%	15%	12%

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17. In terms of the geographic distribution of your organisation's dealmaking and restructuring activity over the next five years, please identify in which of the following areas you expect to *expand your activities through acquisition*. Please choose as many answers as apply.

Region	%
Western Europe	45%
South Asia (China, ASEAN, India)	40%
North America	39%
Latin America	26%
Eastern Europe	25%
North Asia (Japan, Korea)	13%
Australia/NZ	12%
Middle East	9%

18. In terms of the geographic distribution of your organisation's dealmaking and restructuring activity over the next five years, please identify in which of the following areas you expect to *expand your outsourcing* activities. Please choose as many answers as apply.

Region	%
South Asia (China, ASEAN, India)	47%
North America	27%
Western Europe	27%
Latin America	17%
North Asia (Japan, Korea)	16%
Australia/NZ	15%
Eastern Europe	12%
Middle East	11%

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19. In terms of business functions, please identify in which of the following areas you expect to *expand your outsourcing activities.* Please choose as many answers as apply.

IT infrastructure and applications	75%
Human resources & training	42%
Customer contact centres	39%
Finance & accounting functions	36%
Procurement	20%
Supply-chain management	17%
Other	8%

20. In terms of the geographic distribution of your organisation's dealmaking and restructuring activity over the next five years, please identify in which of the following areas you expect to *reduce* your activities through sale and divestitures. Please choose as many answers as apply.

North America	28%
Western Europe	26%
Australia/NZ	23%
South Asia (China, ASEAN, India)	18%
Latin America	15%
Middle East	14%
North Asia (Japan, Korea)	11%
Eastern Europe	3%

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21. Which category of institutions represents the most significant competitive threat to your organisation over the next five years? Please choose one answer only.

Established broad-based financial institutions already competing in your market	50%
Niche players	21%
Established broad-based financial institutions moving from one market to another	17%
New competitors moving from retailing into financial services	8%
Start-up institutions	3%
Other	1%

22. What are the principal barriers to undertaking M&A deals in your own organisation? Please choose up to three answers.

Lack of attractive targets	49%
Cost of M&A deals	34%
Lack of capital	29%
Potential exposure to reputational risk	23%
Poor shareholder value	21%
Resource constraints within management team	19%
Competition restrictions	14%
Uncertain regulatory requirements	13%
Lack of information on target organisation	13%
Poor track record of M&A success	12%
Compliance issues	9%
Lack of market understanding of M&A deals	9%
Organisation unable to accommodate further change	9%
Other	2%

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23. Do you agree or disagree with the following statements?

	Agree	Disagree
Our organisation's total income will be smaller in five years than it is now	3%	97%
Our organisation will be active in fewer geographic territories in five years' time than it is now	14%	86%

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