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Five headaches for investment banks in the next 12 months

__Paul Ford__ of Anchura Partners outlines the big worries for investment banks in 2017, and says that Brexit is not one of them

The evolving financial services landscape continues to challenge the sector in all sorts of ways. Here are the biggest issues that investment banks face in 2017, based on preoccupations voiced to us by senior executives in our client base and beyond.

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LOOKING AHEAD

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01 Revenue is not coming back – and business models need to change

The market in which investment banks operate has changed fundamentally – and with it so has the business model. In a post-crisis environment where the revenue pool has declined, and where senior managers can no longer count on top-line growth to swamp their cost base, leaders will need to start running their organisations like businesses in other sectors. That starts with not assuming revenues will come back. My view is that banks have to think about revenues and costs at the same time, what business lines they are in, and the interaction of all those lines. Investment banks were not set up like that however: they were built when it didn't really matter what it cost.

With senior management spending more time looking internally these days, alive to the need to have comprehensive risk and compliance controls, the danger is that they will take their eye off the ball and not give sufficient focus to how the market is shifting. If you become too internally focused, you may miss that there are people out there who will eat your lunch.

"I would highly recommend Anchura's services to anyone looking for professional, hard-working team players who have the enthusiasm and drive to make change happen"

COO, Tier 1 Investment Bank

02 Risk-averse leaders are clinging on for their pay days

The generational change at the top of investment banks has yet to happen because the banks' leaders are hanging on for deferred compensation accrued in the good years. These are people who've had their hands on the tiller for the past 10 years and – almost to a person– they have golden handcuffs. As a result, the prevailing culture in many banks is one of risk aversion and survival. That creates a lot of indecision.

Over time, the current cadre of leaders will leave for fresh challenges, aware that regulators' drive for greater personal accountability could threaten wealth that has taken years to build up. However, if that happens in the short term, it could pose a real problem: these people all have a very similar mindset and might bail out at the same time, leaving their organisations in the hands of a next generation not yet sufficiently experienced.

03 Regulators are taking a more draconian stance

After a peak in the volume of regulation coming from the authorities in the wake of the 2008 crisis, we are almost back to business as usual, in the sense that there is always some regulatory change on the way. Nonetheless there are a number of significant pieces of regulation that will impact the banking industry coming over the next few years – including the accounting standard for financial instruments IFRS9, MiFID II and the Fundamental Review of the Trading Book (FRTB).

Perhaps more significant than these however, is the way that regulations are being applied. Regulators are much less tolerant these days. The attitude used to be: "We've told you what the rules are and we expect you to do it properly." Now it's: "Demonstrate to me you're in compliance; we are going to be pretty draconian when you come up short."

"Anchura provides a unique combination of flexible resourcing solutions and industry knowledge, which is simply not offered by more traditional consulting firms"

COO Derivatives Management, Tier 1 Investment Bank

This has far reaching implications on cost and efficiency but also requires a new culture to be successfully embedded across all functions.

04 Intense and potentially fatal competition is coming from disruptors

The investment banking industry has yet to wake up to the threat from fintech and other disruptors. It's true that investment banking is a big whale, scarcely bothered for now by a few piranhas trying to take a chunk out of it. But there will come a point when some of these challengers become really problematic. Retail banks are already facing huge problems from Apple, peer to peer lenders and others stealing their profitable lines of business. Investment banks will surely face their turn as parts of their business get picked off by start-ups.

The growth in challengers will be fuelled by the current generation of banking leaders seeking a fresh challenge at the industry's cutting edge as their tenure at the helm of big institutions comes to an end. Their boredom with the risk-averse day job, coupled with the need to push through cost savings, is also likely to usher in a new wave of sector consolidation. This could be led from the US, where banks have emerged stronger from the crisis than their European counterparts.

05 Staff cuts are hurting the ability to adapt

The most enthusiastic cost cuts have all been in investment banks' front offices. Senior managers in these divisions have axed anyone surplus to the generation of revenue and the result is banks stripped of their ability to adapt.

Now banks faced with new regulatory demands do not have the staffing to deal with change. That's why they are coming to companies such as Anchura to help with compliance regimes as well as to execute the build-out of new revenue generating businesses. Whether it takes two years or five years, banks tend to see regulatory changes leading to structural and operational changes as temporary, and they don't want to rehire people. But the shortage of appropriately skilled staff and accompanying danger of dropping plates, can be overcome with flexible, skilled resources. Bandwidth can be regained.

And here's something that you may suppose is a preoccupation, but I don't think is:

While the mechanics of triggering Brexit continue to occupy the minds of the country's politicians, I believe that for the City at least it will be business as usual. The end to existing passporting rules that allow UK institutions to operate across Europe will pose a challenge for sure – and until we know the precise nature of Brexit the scale of the challenge is uncertain.

"The quality of the work and the professionalism of the team provided by Anchura has surpassed my expectations. Their contribution has been instrumental in the development of the necessary structure and governance required for a programme of this size. I would highly recommend their services to anyone looking for professional, hard-working team players who have the enthusiasm and drive to make change happen"

Risk Programme Director, Tier 1 Investment Bank

But banks are very good at finding a way around these sorts of problems – they conduct business in many countries outside the EU and passporting as a common tool is nearly 10 years old. Banks have a toolkit that they use now that can deal with Brexit. They may need Bandwidth but they know how to deal with this.

Meanwhile the critical mass of people and services in London mean the City will be sure to retain its crown as Europe's financial centre. There are estimated to be 360,000 people working in financial services in London and the population of Frankfurt is only 700,000. Where would all those rehoused City people live? It's not going to happen.

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