# Securing our today, for tomorrow

Future of financial markets

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# Financial Markets

Although there is a mention of the current conflict in eastern europe and its impact on the world economy, this publication majorly analyzes the future of the financial markets surrounding the pandemic which shut the world down and caused a significant shift and change in the entire financial scope of the world economies. Any forward-looking statements in this publication be it as it may must be used interpreted in the context in which it was used as the bank is absolved of responsibilities, which may rise from misconstrued assessment of such statements or information.

## Emergence of a new abnormal

Dear reader,

We started out this year intending to write a series of papers about the long-term prospects of the financial services industry. Obviously, the pandemic alongside the unrest in eastern europe changed our plans, as it has upended so many other things, from individual lives and businesses to geopolitics and entire industries. The pandemic has changed many aspects of financial services forever, accelerating trends already begun, creating new trajectories and slowing down or even stopping a number of changes previously underway in their tracks.

Therefore, we are asking ourselves in our recent series if we are adapting quickly enough, given the environment. Beyond this, we examined the impact of the pandemic on banks, insurers, and asset and wealth managers. Those pieces cover in more detail not only how the industry will look as we recover from the pandemic, but, more importantly, the specific steps that individual organizations can take to remain competitive and successful in this new world. On the same hand, we are currently dealing with the turbulence and incoherency caused in the markets as a result of the conflict in eastern europe and the sanctions which has followed and corresponding responses which has resulted to surging inflation and surge in unemployment rates all around the globe, mostly affecting the third world countries.

We have investigated new vulnerabilities and evolving risks. Do the leading financial institutions around the globe have top cyber-security and how can it improve? What could happen if the big tech firms that are dipping their toes in financial services dive in? What can we learn from the Chinese experience of leading online platforms moving into financial services? Where are the vulnerabilities from a decade of ultra-low rates around the world? We have sought to balance cutting-edge thinking with evidence and realism. For instance, the CEO of Visa Europe, Charlotte Hogg, described how their teams are using artificial intelligence to drive reductions in fraud and friction in payments. The payment system could be more resilient if firms had pre-agreed plans to 'step in' for each other if they had outages, she argued.

Throughout, I have kept a critical eye on whether the many new rules and bodies in the past decade work in practice and are efficient. What are the unintended consequences? Is open banking achieving its ambitions? Could the world's highly complex payments regulation improve? Has an uncoordinated regulatory landscape added cost or held back innovation?

The financing of major transitions, such as changes in demographics, climate change or addressing the shifts in global markets needs to be addresses too. The transition to a low-carbon economy is vital for the planet. It poses risks and opportunities for the financial sector and the economy. The bank is already a world leader in focusing on climate change. Roundtables highlighted that investors, lenders and insurers lack a clear view of how companies will fare as the environment changes, regulations evolve, new technologies emerge and customer behavior shifts. Without this information, financial markets cannot price climate-related risks and opportunities effectively. The task force on climate-related financial disclosures has made important progress in fashioning a standard. The bank should champion the mainstreaming of decision useful climate disclosures to help stakeholders assess if a company is transition-ready. Armed with this data, it should also undertake a climate change stress test of the global financial institutions.

The bank should be a world leader in the use of digital regulation. Machine learning and new data sets can strengthen the bank's armory to spot irregularities and get a better picture of the system's overall health and emerging risks. There is huge scope to use advanced analytics and new data sets for macroeconomic trends, financial surveillance and supervision. The explosion in data in finance demands new techniques. Supervisory teams now receive the equivalent of twice the entire works of shakespeare of reading each week. This is going to continue to increase.

The financial system is under almost constant cyber-attack. Firms, in collaboration with authorities, are preventing the overwhelming majority of incidents and investing to stay ahead. Individual institutions cannot prevent all attacks, yet in our connected world a paralyzing attack on one firm could potentially cause loss of confidence in others. To protect customers, financial institutions and public confidence, the bank and private sector should look to enhance data recovery in the event of a major incident, including a mechanism for firms to step in for each other. This should ideally be led by the private sector. Meanwhile, the bank will want to continue to help up the game of individual institutions alongside other authorities.

**Where next?**

The bank has long played a highly influential role in charting the course of finance. The recommendations in this review will, we hope, create substantial benefits for our consumers and businesses and underpin a more resilient, effective and efficient wholesale and retail financial system. We hope they will also prove useful to the many central banks around the world wrestling with similar challenges.

All forecasts demand humility. To make my recommendations as all-weather as possible, we have taken a dual approach developing scenarios, including with help from industry experts, while also analyzing developments elsewhere in the world. We are delighted that many of our recommendations are already being taken forward by the bank, some before publishing this report. But there remains much to do in the years ahead. The job of protecting the financial system is never done.

In addition to those publications, we thought it would be helpful to examine some of the macro trends affecting the industry as a whole and their impacts on individual segments. We hope that you find these insights helpful and provocative.

Stay safe, and please feel free to reach out to us and our affiliates with your comments, inquiries and feedback.

Sincerely,

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## Where we are today - post pandemic economy

### The global economy, a severe shock to the system

To understand the future, we must have a sound grasp of the present. Financial services is a critical industry, in terms of not only employment and taxation but also - and perhaps most importantly - as a primary source of finance to support the so-called real economy. Prior to the pandemic and corresponding crisis, most of the industry was extremely well capitalized, but many firms struggled to earn acceptable returns due to a combination of higher regulatory costs, footprint reductions, a slowing global economy and low interest rates.

In contrast to the global financial crisis, the pandemic in 2019 triggered initial impacts in the real economy and will increasingly manifest itself in a second stage throughout the financial sector. The lockdowns and social-distancing measures imposed by governments around the globe to flatten the infection curves have caused significant damage to many industries, all of which are served by financial institutions. Compared with all previous crises - including the GFC, the oil-price shocks of the 1970s or even the great depression of the 1930s – the pandemic and its trickling effects will likely have the most substantial impact on the global economy, with a one-year reduction in worldwide GDP of more than 6 percent.

A few industry sectors - such as food retailing, telecommunications and capital markets - initially benefitted from the crisis, but many others have been negatively affected, including most manufacturing and services-related industries. The key factor in the severity of impact has been the level of decline in demand, from both corporate customers and individual consumers, directly because of imposed restrictions or indirectly because of temporary behavioral changes. Passenger transportation, hospitality, entertainment, tourism, and consumer goods and non-food retail are among the hardest-hit industries, with monthly revenues dropping by almost 50 - 90 percent in February in Asia, and with that impact spreading to Europe and the US in March and April of the year 2019.

Industries such as automotive and industrial manufacturing faced a similar contraction, and now appear to be headed for a prolonged 'U-shaped scenario,' characterized by a substantial, often double-digit reduction in revenues for 2020, which posed an unclear outlook for 2021.

At UB, we have developed a comprehensive set of econometric models and have analyzed pandemic's impact on each of the industry sectors, both globally and regionally.

| | |
|---|---|
| Positive | Digital Platforms |
| Neutral | Consumer Goods and Retail - - Telecommunications |
| Slightly Negative | Agriculture - - Healthcare - - Utilities - - Pharma and Life Sciences - - Technology and Software |
| Negative | Chemical - - Industrial Manufacturing - - Freight Transportation |
| Very Negative | Services - - Automotive - - Entertainment and Media - - Passenger Transportation, Travel and Hospitality |

**Comments**

- Increased consumption due to pandemic for instance, of masks and increased use of digital platforms and digitization efforts across industries.
- Stable B2C consumption as more consumers work from home and travel is limited.
- Overall reduction in economic activity and GDP drives less consumption. Workforce availability or productivity are at risk.
- Production stopped or output reduced throughout lockdown, uneven recovery.
- Point-of-sale closure and order cancellations through lockdown, period and strength of recovery unclear.

**Financial services : no crisis so far; a mixed outlook for the future**

For the financial services industry, the negative impact from the pandemic will not be uniform for all segments; rather, some sectors will fare worse than others. Through midyear, even as the pandemic hammered a host of industries, it had a relatively modest and mixed impact on the financial services industry. Insurers have benefitted from consumers staying close to home and the subsequent reduced claims frequency in personal lines. Higher trading revenues due to market volatility have boosted capital markets businesses, while central bank activities and government support of businesses and individuals have so far limited damage to bank balance sheets and prevented the types of contagion we saw during the global financial crisis in 2008.

Although volatility remains high, the markets overall have stabilized and recovered quite a bit from the lows experienced in the first weeks after the crisis expanded beyond China. We would argue that the financial services sector will be hardest hit by so-called second-order or trickling effects. That is, the deteriorating credit quality of customers, along with the continued low interest rate environment, as the pandemic and its aftereffects will be felt throughout the real economy over the next several years.

Longer term, the economic impacts of the crisis are likely to affect the sector for years to come. We have come to the end of a positive credit environment that lasted more than a decade, and we will see increasing numbers of both personal and business defaults. This is already being reflected in firstand second-quarter bank loan loss reserves. In addition, any hope of a medium-term normalization of interest rates has been dashed as central banks have been forced to further reduce them.

## Macro trends that matter and their impact in a post-pandemic world

### Global macro trends

To understand the future, we must have a sound grasp of the present. Financial services is a critical industry, in terms of not only employment and taxation but also - and perhaps most importantly - as a primary source of finance to support the so-called real economy. Prior to the pandemic and corresponding crisis, most of the industry was extremely well capitalized, but many firms struggled to earn acceptable returns due to a combination of higher regulatory costs, footprint reductions, a slowing global economy and low interest rates.

**Low interest rates will continue wreaking havoc on margins and business models** - the response to the pandemic will likely significantly prolong ultra-low or even negative interest rates, fueling further margin compression in the short term for the banking sector and asset-price distortions in the long term. As part of their response to the crisis, we are seeing strong fiscal and monetary intervention by governments and central banks, ultimately driving greater indebtedness and incentives to keep interest rates low. This is in addition to the fact that central banks have maintained a low interest rate environment since the GFC, augmented by substantial quantitative easing, which has driven down net interest margins for banks and investment returns for insurers and asset managers.

However, lower rates have also pushed investors away from cash, increasing assets under management at asset and wealth management firms. We see low interest rates persisting for the near future, requiring that institutions increase investment in measures to reduce costs, digitize and improve productivity to maintain margins and profitability. In addition to these low rates, depressed asset values and returns have had a negative impact on life insurance prospects and are forcing insurers to look at their business model and the cost of servicing customers via digital channels.

U.S Economy : ▼ - 15 percent | Large EU Economy : ▼ - 25 percent | Japan Economy : ▼ - 25 percent

- Extremely strong fiscal and monetary interventions.
- Low interest rate levels will endure; rising prices of sought-after asset classes.

**The recession and asset impairments caused by the pandemic will reduce risk-bearing capacity for regulated industries to support the real economy as it enters the recovery stage over the next year** - the asset impairments resulting from the pandemic will ultimately further constrain lending and the risk-bearing capacity of regulated banks and insurers to support the real economy during the recovery phase. This will be particularly problematic in europe, where companies obtained almost 90 percent of their new funding in 2018 from bank loans. In any case, most businesses will need to develop a broader choice of funding options and increase the share delivered by capital markets and the so-called shadow banking or alternative financing industry such as PE funds and sovereigns over today's levels. For insurers, a combination of low interest rates, asset impairments, and the potential for increased pandemic payouts for business interruption are all serious concerns regarding the ability to fulfil obligations and underwrite new business. As such, additional risk-reduction efforts, footprint reductions and an increase in run-off books and, in some cases, insolvency will be the result of these challenges. Therefore, insurers will need an increased focus on rebuilding capital, rationalizing product portfolios and maximizing per-client profitability

**Alternative providers of capital are set to become an even more important part of the global financial system** - as has been properly documented, post GFC regulation increased the cost differential and availability of regulated versus unregulated capital, thus significantly boosting the role of nonbank providers of capital. In fact, the role of alternative financing has been on a dramatic rise since 2010. For the reasons previously noted, we see this trend accelerating as the rebuilding of the economy post-pandemic will require fresh sources of capital. This will be especially true in the small and medium-sized enterprise sector, which provides the bulk of employment in most countries. For established financial institutions, the rise of alternative capital brings into question their very role as a capital provider versus an intermediary, how the platform economy and various funding models will evolve in the future, and where they should play in this ecosystem.

There has also been an increasing role of the government, which has provided both equity and non-equity support for the corporate sector. This shift has several implications: financial institutions need to adjust their business models to a less pronounced role in providing capital and find new ways to participate in the value chain of intermediation and marketing. To enable alternative financing to flourish, policymakers need to make much needed regulatory, tax and legal changes. Incentives are also needed, at least outside the US. This will be crucial to the availability of funding to SMEs.

- Banks' primary role in providing financing has been further challenged in the last decade.
- In the last decade, private debt has seen tremendous growth with 11 percent CAGR.
- Additional measures will need to be taken to improve returns on RWA.
- Funds and other financial intermediaries increasingly providing liquidity in the markets fuel this trend.

**The pandemic will not delay but may accelerate the implementation of current and planned regulatory measures in many countries and regions** - regulation has been, and will be, a significant trend in the industry. Relief measures put in place by regulators as part of the pandemic reaction have been modest and temporary in nature, and they will eventually be scaled back. Regulatory initiatives that had been planned or temporarily postponed will be implemented in short order. In fact, the US could even see a wave of new regulation, depending on the outcome of this year's presidential election. Regardless of the situation in the US, regulation will continue to be a major consideration in such areas as sanctions, anti–money laundering and know-your-customer, IFRS 17 implementation, and LIBOR replacement or reference rate reform, among others. The implementation of Basel IV and tighter capital regulation will continue, challenging traditional lending business models and institutions across the board.

In terms of environmental, social and governance criteria, the massive investments put into the real economy to address the pandemic and support the most severely hit industries and regions - via either direct spending, equity investments or the provision of financing capacity - will increasingly be driven by an ESG mindset. The asset management sector is rapidly adopting this mindset. Already, 90 percent of the top 50 asset managers worldwide subscribe to the Principles for Responsible Investment - PRI. At the same time, reporting requirements in jurisdictions like the EU will increasingly require detailed disclosures regarding sustainability and other related measures. Finally, as providers of capital, banks and insurers will increasingly serve as a mechanism to transmit - through risk-pricing and funding costs - both the benefits and the costs of sustainability to clients.

- Profitability of loan portfolios will be significantly impacted under Basel IV.
- Existing cost and margin-improvement programmes are unlikely to fully mitigate impact.
- Additional measures will need to be taken to improve returns on RWA.

**Continued de-globalization will further align the size of financial institutions to the GDP of their home countries while continued offshoring will increase operational risk across the industry** - in the wake of the GFC, regulation was focused on shrinking the world's preeminent financial institutions, as governments decided that they could no longer backstop a financial system where capital and risk were deployed globally but bailouts were entirely local. As a result, we have seen a striking rise in the size and scope of Chinese institutions, while the relative shrinkage of many European institutions has been dramatic. Collectively, with few exceptions, this amounts to a new financial world order, one that is more aligned with national economic power.

At the same time, cost pressures spurred financial institutions to further separate their front office operations located in the US, Europe, Japan and Southeast Asia from their often outsourced banking operations typically in India, Central and Eastern Europe, and other low-cost regions or countries. Thus, nearly all international and many national institutions have substantial operations in India, and prior to the pandemic, nearly every one of them had plans to increase their use of Indian resources for both cost and quality reasons.

These operations are now so critical that most institutions realized during the pandemic that if India fails, they fail. The good news is that despite some initial hiccups - and thanks to the often heroic efforts of their teams - Indian employees and outsourced providers of major financial institutions have performed remarkably well during the crisis, despite experiencing one of the most extensive lockdowns in the world. Nonetheless, de-globalization could lead to a renewed focus on nearshoring and the diversification of offshore locations. At a minimum, we will likely see institutions with scale operations increasingly focused on diversifying within India, particularly if they are adding new capacity. Asset and wealth management that is not viewed as affecting systemic risk has followed a different path, with greater globalization in some cases, and, in others, more localization or regionalization.

**The client-driven shift to a platform and ecosystem-based financial services industry will create a new wave of disruption and disintermediation** – the pandemic has altered customer behavior and accelerated the move to digital. The shift to a more platform- and ecosystem-based industry, including more digitized client interactions, will create a new set of challenges and opportunities for the industry. For insurers already grappling with the balance between direct and broker-based distribution models, and for large banks struggling with incursions from new payment platforms and SME lenders competing more and more with crowdfunding institutions, platforms are set to continue their growth in volume, value and importance to the financial services industry.

For example, now that the world has spent several months minimizing the use of physical money, the move to cashless economies has clearly accelerated and will continue post-pandemic. This has spurred the use of electronic payment platforms, including those linked to digital currencies. These cryptocurrencies, perhaps the biggest disruptors in the long term, have only begun to gain acceptance at an institutional level, but there are signs that we are about to witness a dramatic acceleration in adoption. According to the bank for International Settlements, more than 40 central banks are researching forms of digital currency that they can issue. China is piloting a digital RMB in four areas.

Finally, in an environment with big tech companies pushing into arenas formerly exclusively owned by banks such as payments and credit, increasing client satisfaction and trust with a wider and evolving set of products and services is an important anchoring factor

**Cryptocurrencies move to the mainstream**

Daily transaction volume

| Visa | Mastercard | Bitcoin | American Express | Square | Ron | Zander |
|---|---|---|---|---|---|---|
| **30.3B USD** | **16.5B USD** | **10.3B USD** | **3.2B USD** | **1.3B USD** | **1.2B USD** | **0.8B USD** |

## A new way to think about the future of your business

### A world of challenges and opportunities

The post-pandemic world brings many challenges and uncertainties, but these can also yield business opportunities for financial institutions. Changes in the geopolitical setting, the structure of the global financial system and a difficult credit environment provide banks, insurers and asset managers with opportunities to support clients in navigating these challenges, adjusting portfolios and developing new investment opportunities. Crises tend to reveal weaknesses in business strategy and execution as well as show the merit of wise strategic choices on where to play and how to win. These include capital allocation and maximizing risk-bearing capacity in provisioning credit to individual clients and client segments, as well as potential mergers and divestiture options.

Strategic options also include new opportunities for partnerships, better leveraging of technology, more productive use of the industry's workforce, and various forms of intellectual, cognitive and network capital.

### Translating thoughts into action

One of the primary challenges of any organization is how to best allocate its precious resources to enact the types of changes required to not only manage through the crises of today, but be successful tomorrow. As you think about the future, it may be helpful to have a structured way to think about your organization, operating platform and overall business. At Universal Banks – UB, as part of our Future of Industries project, we determined the four key categories and areas of focus to consider as you prepare for tomorrow.

**Areas of focus for recovery of financial services**

## Repair

- Portfolio management - prepare for restructuring and workouts.
- Fee-based revenue - develop new products, consider acquisitions.
- Trust - use the crisis to help regain the trust of society and regulators.
- New business capacity - rebuild capital, rationalize portfolios to rebuild capacity.

## Rethink

- Management - adopt a more agile and less structured organization and approach.
- Ways of working - rationalize real estate footprint, formalize remote working, and integrate productivity tools.
- Talent and innovation - increase crowdsourcing and use of gig economy, upskill talent.
- Customer and strategy - accelerate move to digital channels, align business strategy to new reality.

## Reconfigure

- Cost structure - drive 25 percent to 30 percent additional reduction.
- Change budget and focus - re-evaluate and rationalize to improve ROI.
- Emerging technology - drive adoption of cloud and use of AI and SaaS solutions.
- M and A - as needed to re-establish scale, enter growth markets, exit markets or poor-performing businesses.
- Partnerships - increase partnerships with non-traditional providers, technology companies and fintechs.

- Business lines and products - align front-office resources, service models and capital to the most profitable products.
- Compensation and incentives - align to new strategies and objectives.
- Digitization and productivity - accelerate digital labor and transformation initiatives.

Report

- ESG - EU, other mandates.
- State aid - SME assistance, capital, other support.
- Accounting standards - CECL, IFRS 17.
- Regulatory - supervision and communication.
- Shareholders - enhanced disclosure.
- Society - purpose and value.
- Taxes - increasing transparency of tax contribution and strategy.

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### Repair the damage

The damage from the pandemic to the real economy and, by extension, the financial system is manifesting itself in various ways. This damage will require deliberative activities to repair financial institution balance sheets and reputations.

The following repair activities should be top priorities for financial institutions across the board:

- **Prepare for restructurings, workouts and wind-downs** – post-pandemic, organizations will need to decide the best route to restructure businesses and portfolios. Most institutions have seen their restructuring talent and expertise retire or move on to other areas. The last decade has seen little need for this capability, but firms should priorities the rebuilding of this muscle memory.
- **Increase the proportion of fee-based revenue** - one of the fastest ways to repair the balance sheet is to become more capital-efficient by increasing the mix of fee-based versus capital-intensive revenues. This effort should involve both organic and inorganic growth.

- **Accelerate 'trust-building' activities** - consider how the pandemic can be used to advance the institution's efforts to build trust with the community, regulators and shareholders. These include an increase in charitable efforts; actions to assist borrowers, investors, and policyholders; and 'telling the story' in a consistent, effective manner.

- **Create new business capacity** - history shows that times of crisis are also moments of great opportunity to drive new business and improve market share if you have the financial, human resource and management capacity to capitalize on them. Create these types of capacity as an explicit business goal in all of your activities. For example, insurers can look to close the protection gap by combining traditional and innovative products.

## Rethink the organization

Many of the questions about organizational structures and talent that existed before pandemic the efficacy of remote working and the productivity of agile teams have been answered. These and related tools and approaches are now being deployed, and are succeeding, on a massive global scale.

Rethinking the organization requires a focus on the following priorities:

- **Adopt a modern management approach** – a committed management team can drive the necessary employee engagement that can align people around a common objective. The key to success is managing in a flexible manner with cross-functional teams instead of rigid hierarchies, as well as promoting a modern corporate culture, adapted to each individual institution in which prudent risk-taking is rewarded, yet failure is allowed.

- **Embrace new ways of working and digital upskilling** - set out a strategy, and set of goals to support remote working, including tools and techniques to not only facilitate such work but allow for the measurement and management of productivity. This component closely relates to the nature and extent of the organization's real estate footprint, which is likely to be very different than in the past. Finally, committing to upskill employees is critical to an organization's success in a digital world.

- **Crowdsource talent and innovation** - crises tend to drive increases in innovation in successful institutions. Financial institutions have traditionally lagged the technology and many other industries in terms of leveraging the gig economy for both human resources and innovation. Intense cost pressures and the emergence of new talent platforms such as MBO Marketplace, uTest and others have created the opportunity for more flexible, less-expensive talent acquisition compared with the traditional employee or contractor model. Medallia's Crowdicity is one of many collaboration platforms that perform the same crowdsourcing function for ideas.

- **Redesign the customer journey and strategy** - as both retail and institutional clients increasingly migrate to digital channels, the opportunity exists to take bold moves to significantly reduce or even eliminate non-digital channels such as branches, physical outlets and travelling salespeople. With the advent of 5G and improved telepresence, the ability to create meaningful virtual experiences will increasingly impact customer-facing strategies.

## Reconfigure the business and operating platform

Along with the repair and rethink activities, many financial services institutions will need to reconfigure the business and operating platform, in some cases making profound changes in order to succeed in the future. To be sure, the post-GFC changes were also profound, as the industry grappled with increased regulatory costs by selling businesses, reducing workforces, increasing offshoring and taking many other important actions. The pandemic is only accelerating trends well underway in each sector and underscores how much work remains to be done.

There are a myriad of reconfigure activities, but for purposes of brevity, we will highlight the critical areas:

- **Double down on cost reduction, digitization and reshaping the change portfolio** – we are sticking with our pre-crisis view that legacy financial institutions will need to reduce costs by 25 percent – 50 percent over the next three to five years to remain competitive. If anything, that timeline has shrunk. The next wave of cost reduction will mostly come from productivity improvement, digitization and reshaping organization priorities as opposed to traditional measures such as reducing discretionary expenditures and making across-the-board headcount reductions.

- **Increase cloud adoption and the use of emerging technologies** - the acceleration of new partnerships that have been announced between financial institutions and technology companies highlights the extensive efforts to access and deploy cloud and other emerging technologies in order to gain a competitive advantage in the marketplace. The emergence of digital-only players with unique value propositions powered by technology have also shown incumbents the future. Institutions must implement cloud-based solutions, AI, algorithms and coming changes such as 5G and digital currency or risk being left behind.

- **Use M and A to bolster strategic position** - For certain institutions, M and A might be a key solution to further spread costs and increase top-line growth by accessing new markets, optimizing the portfolio and creating value, and thus increasing overall efficiency. Despite geopolitical tensions and uncertainty, financial institutions, fintech and technology players around the world continue to evaluate opportunities in both developed countries and emerging markets such as China and southeast Asia. At the same time, a number of partnerships are being formed between banks and fintech players around the world. However, it is unclear whether cultural and political challenges can be overcome in order to see mergers of, say, and large european banks. In insurance, we also expect to see a number of consolidation efforts, divestitures, asset sales and joint venture possibilities, as we did in the aftermath of the GFC. The pressure on the balance sheets and solvency of insurance companies will not decrease in a low-interest environment; in fact, this pressure creates a further need for consolidation, accelerated by failing institutions.

  The same applies to asset and wealth management, where the crisis is only accelerating the shakeout in the industry, particularly as it relates to actively managed funds. We also expect to see a number of wealth management spinoffs and consolidations occurring when valuations fully adjust to the changes in market. To realize this, financial institutions need a sustainable strategy to grow through M and A, along with capabilities to identify the 'right' targets that are in line with acquirers' strategic ambitions. Once a target has been identified, financial institutions need a clear perspective on a deal's commercial viability, the financial impact of executing the deal and whether the deal will deliver the expected value over time.

- **Collaborate with non-bank lenders and embrace change in market structures** - we discussed earlier that the role of banks might change, due to a lack of capacity to refinance rescue measures post-pandemic. We argued that part of the volume will be picked up by nonbank lenders, including ecosystem, effectively reducing the future revenue pool for banks. In this environment, particularly for capital-scarce institutions, finding ways to participate in the value of alternate credit intermediation may be a necessity in the future. In these arrangements, it is critical that both partners benefit from the jointly created revenue pool. In addition, the partnership needs to be set up in a structural, systematic fashion. Assessing these opportunities on a deal-by-deal basis will not work.

- **Optimize business or product mix and align incentives** - in a world with an even more pronounced focus on profitability and a changing role for banks and their balance sheets, financial institutions need to align strategy with client and product offerings. In addition, implementing stringent service and incentive models aligned to economic client profitability and prudent risk management is key.

## Report the results

As various stakeholders demand more transparency and accountability from financial institutions, the focus will increasingly turn to complete and accurate reporting in a range of areas, including financial performance, ESG, regulatory compliance and the like. In addition, it will be critical not to miss perhaps the most important attribute of any successful financial institution in the future: being able to articulate its unique culture, story and value to society. The pandemic has led to unprecedented challenges for the financial services industry, creating massive new disruptions and dramatically accelerating others that were already underway. Depending on one's perspective, the future of the industry could be either perilous or promising. **We choose to focus on the latter**.

Significant upheavals create new opportunities for innovation. The challenge for leadership teams is to look forward, understand the scope of changes underway and be bold in responding to them. We look forward to helping you and your institution successfully secure your tomorrow, today.

## Accessibility

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