CAN LOCAL BANKS COMPETE IN A GLOBAL MARKET?

By Dr. Edwin L. Weinstein

When it comes to trade banking, large corporates in Asia are thinking hard about their banking relationships. Despite historically deep relationships, they are more likely to deal with a new bank than corporates in other regions of the world. Globalization is increasingly a fact of life, and this fact should cause Asian banks to re-think their strategy for competing in their home markets. Complacency will not be a strategy for survival. Let's look at some of the facts.

The facts discussed here come from the Asia-Pacific Report of Brendan Wood International's 1999-2000 Global Trade Study. This report, completed late in 1999, is based on interviews with 500 of the largest exporters and importers in Asia. Most of these companies had annual revenues in excess of US$250 million in the country where they were interviewed and many had revenues in excess of US$1 billion locally and US$5 billion globally. The companies interviewed for this study represent the bulk of foreign trade for the region, so what they are doing is critical for banks in the region.

Most Asian banks draw their strength from their domestic market, but trade is an international business. Exporters/importers with annual revenues in excess of $1 billion are well under 1% of companies but represent more than half of global trade ***(see Exhibit 1)***. If we drop down to $100 million in annual revenue, we include nearly 90% of global trade. These companies cannot stay competitive if they remain local in their thinking. Their banks cannot stay competitive if their thinking is local too.

Let's take a look at the challenges facing Asian banks in a global market, and then, we will look at some of the possible ways that Asian banks can compete. While specific strategies for each bank must depend on their positioning in the large corporate market, we can point to some general directions.

WHAT ARE THE CHALLENGES FOR LOCAL BANKS?

Asian corporates typically have 3-4 main banking relationships depending on their market. The banks they deal with often have different capabilities, especially in terms of their geographic reach. If we look at the reach they get from their relationships, we find ***(see Exhibit 2)*** that one-quarter of relationships are with regional banks *(i.e., banks with a multi-country presence in Asia but not in Europe or the Americas)* and the remainder are split between local and global banks. This suggests a need for both local presence and foreign market reach. In fact, only one out of six companies can get all of their trade banking needs met solely by local banks

Exhibit 1
Trade Volume and Company Revenue

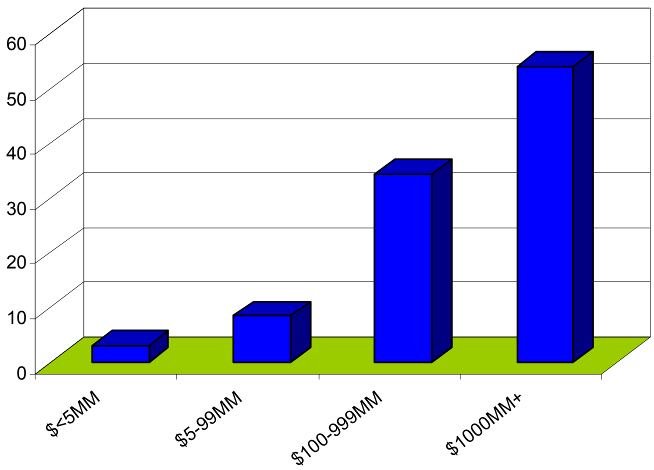
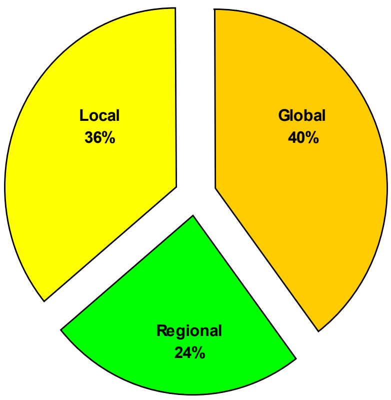


Exhibit 2
Mix of Banking Relationships



WHAT ARE THE CHALLENGES FOR LOCAL BANKS CONTINUED?

While both local and foreign reach are necessary, the need for global reach is clear when we look at the use of global banks by large exporters and importers ***(see Exhibit 3)***. On average, two-thirds of these companies use a global bank. **In most of Asia, more than 70% of these large companies use a global bank for part of their trade services.** With the exception of Bank of Tokyo-Mitsubishi (BTM) in Japan *(and depending on your view HSBC in East Asia)*, the global bank used is not a domestically-owned bank with global reach. Widespread usage makes it clear that global banks have capabilities that exceed those of local or regional banks in many cases.

The need for global reach may also be impacting sales, and at the moment, Asia is more open to new banking relationships than any other major region in the world ***(see Exhibit 4)***. More than half of the companies in Asia that were solicited by a new bank selling trade services indicate that they are likely to do business with this new bank. While these new relationships will likely start out by giving new business to another bank, particularly in a growth market like Asia, it still involves a potential loss of position for existing banks. Many of these banks will not immediately know they are losing the business, since it will be incremental business that initially goes to their competitors. This will happen most in Singapore, which is particularly open to switching. The same changes will take place in Korea, Hong Kong and Taiwan (East Asia) too.

Regardless of which part of Asia we are talking about, global banks will disproportionately benefit from new business ***(see Exhibit 5)***. **More than half of new business will go to global banks, one-third will go to regional banks, and only one-sixth will go to local banks.** This is not a matter of marketing activity, since the exhibit shows that each type of bank is roughly responsible for one-third of sales calls in the market. Rather this is just the result of large local corporates and multinationals seeking out the capabilities they need, and quite often, these are not available at their local bank.

Exhibit 3
% Companies Using a Global Bank

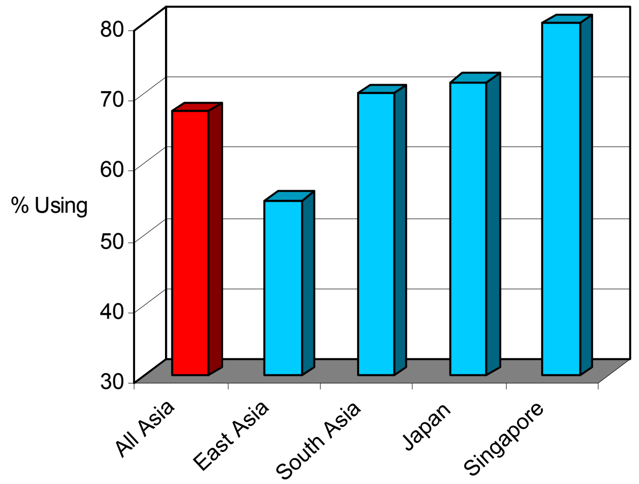
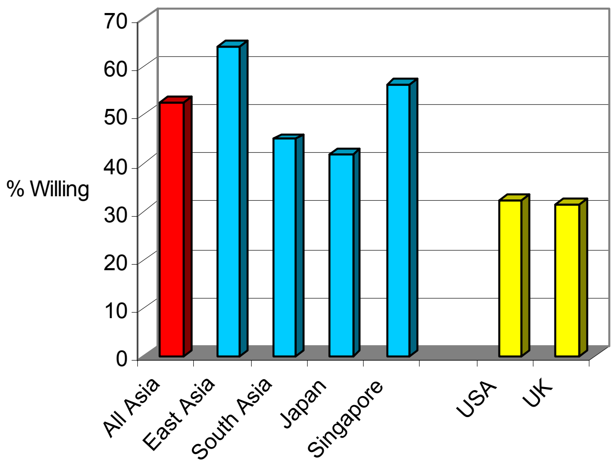


Exhibit 4.
Willingness to Switch/Add Banks



WHY ARE GLOBAL BANKS GAINING GROUND?

Global banks are gaining ground because of their capabilities. Banking service is judged on three major criteria: Access, Price and Day-to-day service. Access is the mix of branch and electronic access to trade services. Price reflects the tradeoff between the amount of credit a bank extends to a client and the price of its processing services. Day-to-day service reflect the accuracy, timeliness and problem-solving that characterize smooth service. When we combine the several dimensions that underpin each of these three major criteria, we find that clients rate their global banks higher in two areas *(see Exhibit 6)*. **Global banks clearly excel at Access to service, largely because of their electronic capabilities. Day-to-day service is also better for global banks, and in our view, this can also be attributed to their systems capabilities.** When it comes to price, global and local banks are about even. Despite all of the areas where global banks lead though, clients are still equally satisfied with their local banks overall. Some might see this as meaning that price is the driver for their satisfaction, but our analysis shows that price is less important than relationship and the ability to get problems solved quickly.

Account management is the personal relationship side of this business and here we can also compare banks on three major criteria: Advisory skills, Regular contact and Depth of relationship. **Advisory skills**, which reflect industry knowledge and ability to help manage risks, **are clearly where global banks excel** *(see Exhibit 7)*. Global banks also show greater relationship depth, reflecting their knowledge of how to get things done in the world of trade. Global and local banks are about even in the regularity of their contact and in their clients' overall satisfaction.

While not highlighted here, the bigger puzzle is why regional banks are gaining ground, since they are typically rated lower on most service dimensions. It is our sense from other parts of our study that people go to regional banks expecting the systems advantages of a global bank with the local knowledge and presence of a local bank. What they get is somewhat disappointing. Asian regional banks typically lack the scale to build systems with the robustness of global banking systems, but rather try to extend their domestic market systems to a few foreign markets and find that the systems don't quite work as planned. The dot.com adage of "Go big or go home" seems to be at work here.

Exhibit 5.
Impact of Sales Effort

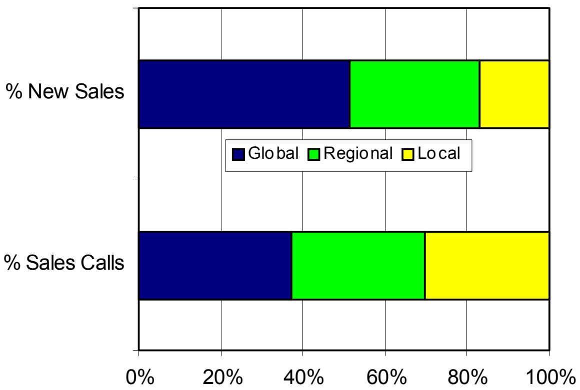
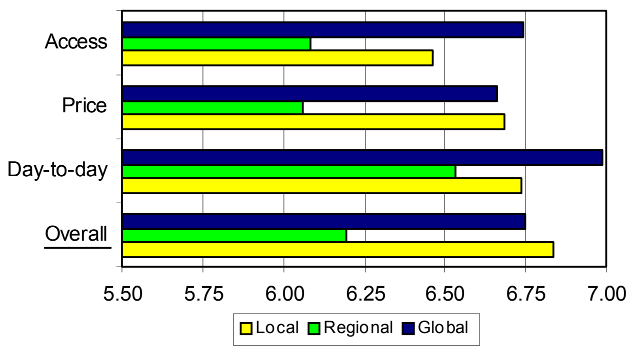


Exhibit 6.
Satisfaction with Bank Service



WHAT CAN LOCAL BANKS DO TO COMPETE?

Giving advice for how to compete in an article like this is about as dangerous as diagnosing a patient that a doctor has never seen. In reality, we must look at the condition of each bank and prescribe cures that fit the exact ailments. Nonetheless, this is a 'common cold', so perhaps we can talk to some common cures.

Most of the cures come from the details that we have glossed over. Let us make it simple by stating a few things that you can do and we will then describe them in detail. The top five strategies as we see them, in no particular order, are:

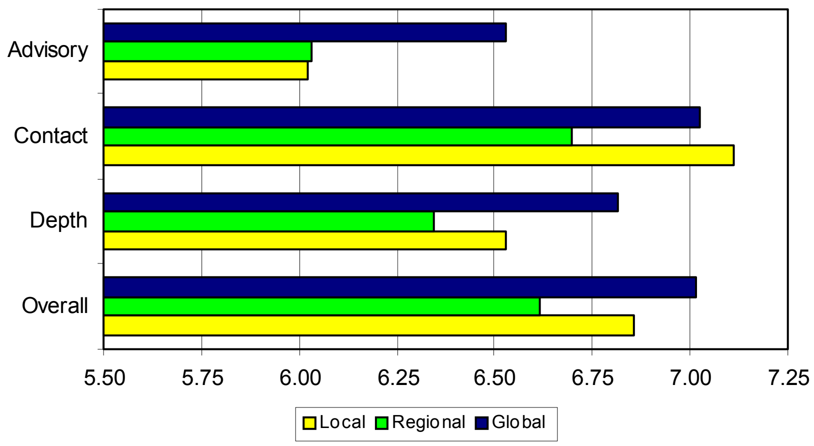
1. **Technology 'leapfrogging';**
2. **Centralize processing operations;**
3. **Increase financing capabilities;**
4. **Capitalize on long-term relationships; and**
5. **Hire/train industry specialists.**

Technology is an area where global banks lead and it is difficult to catch-up with them when you are relying on a single local economy as a source of your business. One solution is not catching-up, but rather leapfrogging. This means that you will organize your business differently and try to **adopt new models for handling trade flows**. Skipping right into **internet-based services** is one route, whether developed or preferably bought and adapted. The market is looking for internet-based invoicing and payments, as well as issuing wires with embedded foreign exchange. Embracing new initiatives like **TradeCard**™ and **Bolero**™ can also give you a competitive advantage. With less invested in maintaining legacy systems, you can afford to move in new directions while global banks fight to adapt their existing systems.

Centralizing processing operations is another way to improve your competitive positioning. **Centralized operations are typically more cost-efficient, but even more to the point here, they improve clients' perceptions of the bank and its people.** In many cases, this translates into better client retention.. Centralized operations allow you to create a cadre of service representatives to deal with client problems on the operations side. This means that problems get resolved more quickly and your clients get answers to their questions more rapidly. If properly organized, centralized groups like this build knowledge rapidly and are an asset to your operations. With the proper tracking you will also spot operational problems more quickly and fix them before they impact client service.

Suggesting that you increase trade financing will immediately be met with skepticism, but we are not talking about taking additional risks. **There are three main approaches you can take to increase financing without increasing risk**. First, if you do have an appetite for risk and available credit, you can contain your risk by buying the kind of expertise available to global banks. Companies like LTP Trade in London provide risk management services that will allow you to value your trade portfolio, better assess deal risk and manage your risk in a tightly controlled manner. If you don't have any risk appetite, then you can look to your correspondent banking network to either buy or syndicate your trade paper. Finally, if you have an investment banking arm, securitizing receivables due from "blue-chip buyers" is a strategy that may prove useful in your market, just as it has in other markets.

Exhibit 7.
Satisfaction with Trade Account Management



Capitalizing on long-term relationships is a matter for your advertising arm. One of the consistent advantages that local banks enjoy is their relatively low account manager turnover. Advertising that builds on this advantage can be powerful, since changing account managers is something that most clients prefer to avoid. You can position your account manager as the person who sticks with the company through its 'ups and downs' and knows their needs best.

The final point ties in to account management as well. Global banks have two kinds of account manager that are less common in local banks. The first is the industry specialist and the second is people who have banking experience in the markets where their clients send their exports. Both of these give the global banks a real credibility advantage on the advisory side. With a few dominant industries in most countries, building industry expertise in trade is a solid strategy, particularly if you can bring in experts with foreign market experience. Industry expertise helps retain and cross-sell your clients, and in many cases we find that industry expertise helps you identify better risks because of specialized knowledge. In short, **industry expertise both increases sales and reduces losses.** While your expertise may be more localized, this will allow you to compete more effectively with your global counterparts, and your investment in your own people is unlikely to be wasted.

SUMMARY

Large corporates and multinationals look for systems, money and quality people when they decide where to place their business. In Japan, all three are equally important. In Greater China and Korea, money concerns dominate the picture. Other Asian markets fall between these two extremes. Regardless of the drivers in your market, our solutions address all three of these issues and are based on solid research. While our five solutions may not be the perfect medicine for your ailment, we suspect that they will improve the health of most local banks that take some of our cures.