A new financial order

29 June 2009

This story on the Web

Get the full report

Download **A new financial order**, a newly published report from the IBM Institute for Business Value (353KB)

Learn more
Read about how a smarter planet manages its money

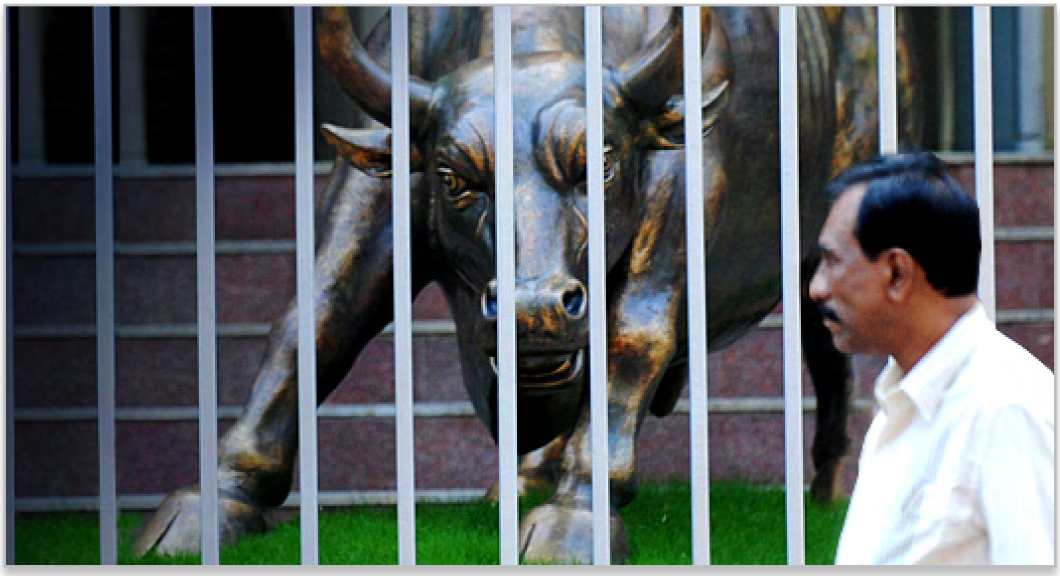
We're here to help
Easy ways to get the answers you need.
Call us at **1-800-IBM-7080**
Priority code: **US7AN05T**

Get in the conversation
Join the Smarter Finanacial Services group on LinkedIn®

Stay on top of innovation
More Ideas from IBM

Syndication
RSS **Subscribe via RSS**

Help with subscribing



If you're like the average investor, you've lost money in the stock market since last September

In fact, **40%** of wealth has been lost since May 2008.[1]

There has been a lot of information about what went wrong with the markets. Individual investors are nervous, sitting on the sidelines, and many industry executives are unsure of what their business will look like even in the near future.

Over the past few months, IBM talked to more than 2,700 financial services industry participants to:

- Better understand the short-term and long-term impacts of the market upheaval
- Find out what investors are looking for now
- Understand how financial institutions will make money in this new environment

Here's what we found.

April 27, 2009 Suzanne Duncan, IBM, discusses research report on the future direction of the financial industry on CNBC Squawk Box.

Watch the video

The big returns are gone

Ninety percent of industry executives believe that the returns of the past—with their corollary risks—are gone. From 2001-2007, profit margins for financial services firms averaged 26 percent;[2] by 2012, it is estimated that these will shrink to 12 percent.

At the same time, returns on investment for the average investor will hover between 3 and 6 percent, with most of the appetite for risk stripped away.[3]

Headed for divorce?

We have all heard about the increasingly antagonistic relationship between Wall Street and Main Street. This is reflected in the growing gap between financial services firms and their clients. By gap, we mean a lack of trust and knowledge of each other's expectations... not unlike two parties in a divorce case.

Sixty percent of investors "stongly" agreed that providers "offer products and services that are in their own best interest, not mine." Worse, many of the executives agreed with them! Forty percent of respondents in Europe, the Middle East, Africa and Asia think their companies put their own interests first and the figure rises to 49 percent in the United States.

Further, 79 percent of the executives proved to be disconnected from their clients in understanding what they value. For example, providers think offering clients "best in class" financial products such as managed mutual funds is the most important thing they can do, followed by a one-stop-shopping type of organization.

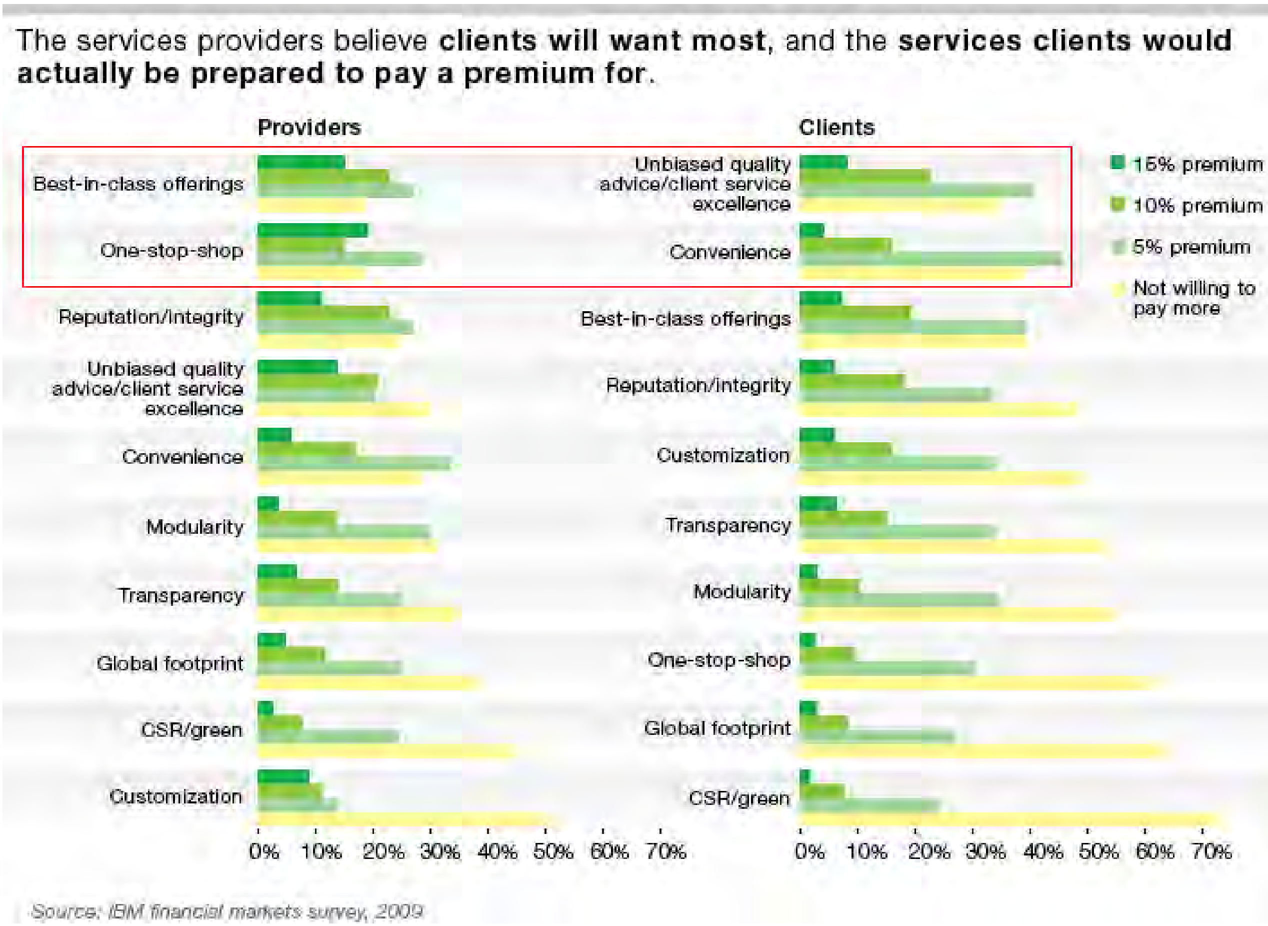
Not true, say clients.

The thing they most value is unbiased, quality advice and excellent client service—not products—followed by convenience, as in "make my life easy." This could mean something as simple as talking to a live person when you call. And investors say they are willing to pay a five percent premium for this convenience.

"We have lost sight of the client in our own striving for outsized returns. We must get back to basics and focus to a far greater extent on our clients."

– *Global Head of Prime Brokerage, large U.S. bank*

“Herein lies the opportunity,” says Suzanne Duncan, financial services marketing executive. “The institution that knows its clients well can create the sorts of products and services that provide this added convenience and tap into that five percent premium that clients say they would be willing to pay.”



Think about **your favorite hotel...**

“They are constantly gathering information about your preferences and using that data to improve your guest experience, whether it’s the newspaper you read, which pillow you prefer, or the car rental company you use,” says Duncan. Financial services companies have the advantage of already possessing a lot of valuable data about their clients: the flow of money in their lives and events such as a new job, marriage or retirement that can signal the need to change their financial strategy. If institutions can present the right counsel or product at the right moment—that’s the start of strengthening the relationship.

Looking to other industries

For many firms, delivering better client service might mean “unbundling” their supermarket business model. Our research shows that specialized firms, independent advisors and boutique firms have a better sense of what their clients want and can deliver it. Yet,

Customer service excellence for leaner times

Customer Service in a Shrinking Economy
—*BusinessWeek*

Business Week's 2009 top customer service companies list reveals that even in times of layoffs and cost cutting, the winners aren't reducing service. They remain relentlessly focused on knowing what their customers want, refining their services and products, cross-training their employees in multiple service roles and creating different "tiered" experiences.

when asked which business model they favor, executives most frequently chose a universal banking model. Simplifying the "all in one" model will allow firms to eliminate redundancies, reduce costs and focus more specifically on improving service.

While institutions recognize they have to change, many say this is something they are not very adept at: Only 12 percent think they are effective at capitalizing on new technologies and 18 percent feel they can manage the risk of new products.

They might have to look to other industries for examples of how to transform their business models. For example:

Bharti Airtel, India's largest private-sector telcom operator, is able to keep up with a stunning pace of growth—about 1.5 million new customers per month—by focusing all of its efforts on customer service, and outsourcing its IT, billing and 60 platforms to IBM.

Endo Pharmaceuticals, sometimes referred to as a "virtual company," relies on third parties for all of its manufacturing and distribution. Endo, with its supply chain provider, UPS Supply Chain solutions, designed the two distribution centers UPS now runs for the company. This approach enables Endo to expand and contract in line with (volatile) demand volumes.

So what does all of this mean for the individual investor? We believe:

- Returns will be smaller, but more sustainable.
- Consumers will need to take more responsibility for their investments, researching institutions and instruments.
- Banks and institutions might become smaller, choosing not to operate in certain markets.
- You might have fewer institutions to choose from, but service will be more personalized.

1 Based on MSCI World Index year-over-year returns as of May 14, 2009.

2 Profit margins are average annual net operating margins.

3 Returns are based on 55 interviews with portfolio managers and academics.

SEND US YOUR FEEDBACK:

We're interested in hearing what you think about this article. Do you have a question, comment, suggestion or story idea to pass along? Please e-mail **Ideas from IBM**.

IBM Corporation
New Orchard Road, Armonk, New York 10504, USA