THE ENTERPRISE OF THE FUTURE

...IN THE FINANCIAL MARKETS INDUSTRY

The five core traits of the Enterprise of the Future revealed in the IBM Global CEO Study hold important implications for the financial markets industry as it navigates one of the most financially devastating periods in history.[1]

HUNGRY FOR CHANGE

In September 2008, we witnessed the demise of the independent Wall Street business model, significant bailouts and double-digit stock market declines around the world.[2] Indeed, the recent credit turmoil has made two things exceedingly clear: massive herding into new product areas and geographies is taking its toll – and the industry faces an uphill battle to overcome these instincts. Not surprisingly, the percentage of financial markets CEOs who say their firms face substantial near-term change has shot up from 65 percent in our 2006 Global CEO study to 85 percent in 2008. And despite the need for rapid change, two-thirds of financial markets firms rate their agility as moderate to poor – and less than 5 percent feel confident about their risk management capabilities.[3]

Implications: Financial markets firms must shore up their capabilities from two angles: improving their ability to anticipate – and even drive – change while instilling the courage and ability to act quickly on those insights. This requires more than just data; having the right governance, culture and incentives will allow firms to manage change, not simply react to it.

> "Significant changes in the dynamics of the securities business are affecting us... there is always a fear of – and an opportunity for – disintermediation."
>
> *CEO, Large global custodian, Americas*

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> “We must become much more sophisticated – in order to meet each individual and customized client need.”
>
> *CEO, Universal Bank, Europe*

INNOVATIVE BEYOND CUSTOMER IMAGINATION

Three out of four financial markets CEOs say the emergence of better informed and more sophisticated clients will have a positive impact on their businesses. But their actions don’t seem to match their words. Across an array of industries, CEOs are ramping up investment by 22 percent over the next three years to serve their increasingly informed customers; financial markets CEOs, on the other hand, are raising investment by only half as much.

Implications: Moving slowly on this trend puts firms at risk of losing clients to innovators that are improving client collaboration and segmentation capabilities. Too often, financial markets firms guess at what their clients actually value: we found that 75 percent of executives were out of step with what their clients were willing to pay a premium for.[4] Firms must eliminate these disconnects. As they develop a deeper understanding of their clients and associated risks, they can begin to segment based on behavioral factors beyond just type and size. Above all, firms need to collaborate more directly and more extensively with their clients – not only to develop stronger relationships, but also to co-create meaningful innovation.

GLOBALLY INTEGRATED

When asked about business design changes being made in response to globalization, financial markets CEOs’ responses put them on par with other industries. However, we know from prior industry research that firms are struggling to globalize beyond brand and footprint: two-thirds of financial markets executives rank their firms’ ability to operate globally as moderate to poor.[5] With more than 60 percent of wealth increases coming from growth economies, CEOs understandably expressed concern about the ability of today’s rigid, headquarter-centric organizational models to capture the future global opportunity.

Implications: To compete effectively for emerging pools of financial and human capital, firms must pursue global integration not just a global presence. Operating models need to be designed around three key tenets: global asset leverage, dynamic capability assembly and open collaboration. Firms must be able to access and deploy their assets – people, process, technology, governance and culture – across product and geographic boundaries. They must simplify complexity and build modular capabilities that can be brought together rapidly to respond to shifting growth opportunities. To drive faster and bolder innovation, employees need the means to collaborate openly across organizational fiefdoms. And despite the industry's bias toward proprietary intellectual capital and a do-it-yourself approach, market realities are making external collaboration even more crucial.

DISRUPTIVE BY NATURE

Financial markets CEOs clearly understand the potential upside of business model innovation: 78 percent told us they are implementing significant business model changes over the next three years. But they may be innovating in the wrong places. Across all industries, financial outperformers are pursuing enterprise model and industry model innovation.[6] However, financial markets CEOs are focused elsewhere – on revenue model innovation. Historically, firms have not focused on innovation that helps them differentiate and grow, staying instead within their comfort zone tweaking their revenue models.

Implications: As the recent credit crisis shows, risk has not been valued properly within firms' business models. To rectify this, firms must manage their portfolio of businesses as a collection of risks, not just returns. Firms must also nuture a series of innovation programs that span multiple business model areas and include industry-changing plays. In this industry, perhaps more than most, technology will serve both as an enabler and an instigator of business model innovation.

TYPES OF BUSINESS MODEL INNOVATION CONSIDERED

Enterprise model
Specializing and reconfiguring the business to deliver greater value by rethinking what is done in-house and through collaboration.

Revenue model
Changing how revenue is generated through new value propositions and new pricing models.

Industry model
Redefining an existing industry, moving into a new industry, or creating an entirely new one..

GENUINE, NOT JUST GENEROUS

As clients, employees, investors and other stakeholders become more socially aware, CEOs everywhere are increasingly concerned about corporate social responsibility (CSR). More than two-thirds of CEOs across industries think customers' rising expectations related to CSR will have a positive impact on their businesses, but financial markets CEOs believe the opposite. Sixty-five percent say this trend is likely to have negative consequences if there's any impact at all. Theirs is by far the most pessimistic view across all the industries we studied. And in terms of relative investment in CSR over the past three years, healthcare payers are the only industry spending less than financial markets firms.

"CSR costs are considered expenses, not investments."

CEO, Large Investment Bank, Europe

Implications: Their negative reaction to client and regulator demands for increased transparency and ethical behavior may be causing financial markets firms to underestimate a major financial opportunity. We believe industry leaders will find ways to grow their bottom lines while being a socially responsible role model. They'll not only work to become more "green" and invest in social causes, but also eliminate incentives that encourage unethical behavior inside their own ranks.

BUILDING YOUR ENTERPRISE OF THE FUTURE

The current credit crisis has forced a critical inflection point upon the industry – an opportunity, if not a mandate, to reevaluate business and operating models. Leading firms will use this time of historic change, uncertainty and volatility to move ahead of the herd and reinvent themselves. We look forward to working with you, as you build your Enterprise of the Future.

For additional information about the IBM Global CEO Study, please visit ibm.com/enterpriseofthefuture or e-mail one of the following contacts:

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NOTES AND SOURCES:

1 "The Enterprise of the Future: The IBM Global CEO Study." IBM Institute for Business Value. May 2008. We spoke with 1,130 CEOs, general managers and senior public sector and business leaders from around the world, including 54 who head financial markets institutions.

2 MSCI Index Performance. As of September 24, 2008, the World Index had declined by nearly 22 percent year-to-date.

3 Dence-Duncan, Suzanne, Wendy Feller and Dan Latimore. "Get global. Get specialized. Or get out. Unexpected lessons in global financial markets." IBM Institute for Business Value. June 2007. As part of this research, we surveyed 955 business leaders – including 848 financial markets executives and, importantly, 107 corporate clients. In this study, "agility" was defined as the ability to respond quickly and effectively to external forces.

4 Ibid.

5 Ibid.

6 For companies with publicly available financial information, we compared revenue and profit track records with the averages for those in the same industry across our sample. Companies that performed above average on a particular financial benchmark were categorized as outperformers.

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