Sibos 2009: Extending Critical Dialogue During Critical Times

Gareth Lodge, Andy Schmidt, Dushyant Shahrawat, Ralph Silva
TowerGroup
October 2009

TowerGroup Key Findings

- Sibos 2009, held in Hong Kong, attracted the largest Asian attendance in the history of the conference and exhibition, with 42% of the 5,782 attendees coming from Asia, compared to 45% from EMEA and 13% from the Americas.
- The critical dialogue at Sibos this year revolved around five major themes for financial services: innovation, globalization, responsibilities of the financial services industry, collaboration and coopetition, and the future of the financial services industry.
- One of the crucial insights gleaned from Sibos 2009 by attendees is that instead of standing back and letting regulators dictate the future of financial services, the financial services industry must proactively engage regulators to encourage them to pass more effective rules and regulations.
- This year's Sibos revealed that innovation in financial services is definitely not dead, as firms seek to innovate in new areas like risk management.
- While everyone looks to China as a major growth opportunity for the global financial services industry, it is time to consider the ambition of Chinese and Asian banks to compete against Western banks, not just in China but in Europe and America as well.
- Despite financial institutions being blamed for having brought the global financial system to its knees, the continued success of market infrastructures through all these stresses and strains gives us great hope that all is not lost.

Introduction

To many in the financial services industry, the third quarter of the year signifies one thing: Sibos. The event has become more than "just" the SWIFT user conference. The conference and exhibition is almost a one-stop shop for participants in the banking and securities industry, with product launches and demonstrations continuing to expand and attendance remaining high even in an economic recession. This year's event drew 5,782 attendees choosing from over 100 sessions, and it featured 176 exhibitors. Exhibit 1 shows key metrics about Sibos 2009, held September 14–18 in Hong Kong.

Exhibit 1

TowerGroup

Sibos 2009: Key Metrics

Geographical Diversity	▪ 5,782 attendees ▪ 45% EMEA, 42% Asia-Pacific, 13% the Americas
Attendee Profile	▪ 24% Directors, Vice Presidents, and Managing Directors; 29% Vice Presidents or Account Managers; 15% Department Heads; 8% Section Heads/Supervisors; 7% Board Members/CEOs; 7% Analysts/Consultants ▪ 173 journalists (117 from Asia)
Market Segments Represented	▪ 33% Payments, 21% Cash Management, 16% Securities, 16% Trade Services, 5% Other
Sessions	▪ 155 speakers participating in over 100 sessions ▪ Big Issues Debates ▪ Industry-specific discussions covering Banking, Payments, Trade, Corporates, and Securities ▪ Sessions on innovation and standards
Exhibitors	▪ 176 exhibiting firms

Despite its growth, Sibos still has the same objective it started with over 30 years ago. The annual conference revolves around key issues in the global financial services industry and strives to ensure that the participants hear and take part in critical dialogue that drives the industry forward. Whether the discussion is educative, an update, or controversial, delegates come away having been part of and added to the dialogue that takes place all around them at Sibos in conference sessions, on the exhibition floor, and in conversations in the corridors. That is why TowerGroup believes Sibos is such a critical event.

The goal of this report is to identify key topics of discussion at Sibos 2009 and, based on these themes and dialogues, provide perspectives on where the financial services industry will go from here. We have extracted the major elements that came through strongly from the 100 sessions held at Sibos and synthesized them under five broad themes. Under each theme, we describe how the notions that attendees brought to Sibos changed over the course of four intensive days of discussion, debate, and deliberation.

THE FIVE THEMES OF SIBOS

Based on the dialogue during the week of Sibos 2009 and discussions provoked by the over 100 sessions, five major themes emerged:

Innovation
Globalization
Financial services responsibilities
Collaboration and coopetition within financial services
The future direction of the financial services industry

These themes engendered the most critical dialogue during Sibos and will continue to be discussed in the 12 months until Sibos convenes again in Amsterdam in October 2010. The key discussion points are synthesized in Exhibit 2.

Exhibit 2

TowerGroup

The Five Major Themes at Sibos 2009

Theme	Critical Questions Addressed
Innovation	▪ What will be the future of innovation in financial services? ▪ How can we innovate in risk management?
Globalization	▪ Where are the industry's growth opportunities? ▪ What opportunities do China and India represent? What challenges?
Financial Services Responsibilities	▪ What are the financial services industry's responsibilities to the public and to the global financial system? ▪ How can we work with regulators to ensure the passage of better laws?
Collaboration/ Coopetition	▪ How can banks compete with each other and yet collaborate on key issues? ▪ What are the opportunities for collaboration across the industry right now?
The Future of Financial Services	▪ What impact will new regulations have on the future of the industry? ▪ How will the industry manage risk going forward?

Source: TowerGroup

The insights gleaned from Sibos 2009 across these themes are clear, straightforward, and powerful. In order for financial services firms to prosper, they need to innovate in the way they deliver services, considering such options as collaboration and "coopetition" with other industry participants. The future direction of the banking industry will be determined by the swath of new regulations being prepared by global regulators and by the way the industry manages risk in the future. The financial services industry will continue to globalize, with Asia playing a major role in the competitive dynamics of the business.

Western financial institutions will encounter greater competition from Asian institutions, not just while competing in Asia but increasingly while protecting their territory in United States and Europe. At the same time, Asian institutions with global ambitions are actively seeking to develop a better understanding of the product management, client service, and delivery expertise they will need to acquire in order to compete effectively in the West.

All financial services firms will need to be aware of and act on their responsibility to their customers, the regulators, and each other in creating and preserving a healthy industry. Lack of action will surely result in a stronger regulatory backlash than the industry or the regulators desire. Fulfilling this responsibility will require dialogue to identify product and delivery risks and educate regulators on the mysteries of the financial services business.

Innovation

Innovation has always been an important theme for Sibos, and this year was no exception. But unlike previous years, the economic turmoil of the preceding 12 months put in question the priority of innovation for the financial services industry. In the current recessionary environment, funding for product innovation has become nearly impossible to secure. Most business units are short staffed and wary of new and possibly risky initiatives. Many heads of banking find expenditure on product innovation difficult to explain to shareholders looking for stability as the economy recovers. In the securities world, innovation has become a bad word, synonymous with financial engineering, derivatives, and exotic products, which grew dramatically over the last few years and were partly responsible for bringing down many large firms. Public opinion and political pressure seems to be more opposed to innovation in the securities industry today than ever before.

Sibos 2009 brought a fresh perspective on innovation and made people question old notions of what innovation is and what it isn't. Attendees' thinking about innovation was challenged in the plenary debate and main sessions as well as in many industry track sessions. Closing session speaker Guy Kawasaki, an authority on innovation, defined innovation not as something that brings about incremental change but rather as a dramatic rethinking of the way a product is sold, consumed, or distributed. In various track sessions, attendees concluded that innovation is as much about service delivery and consumption as about the creation of new products. Considerable discussion ensued concerning ways that innovation can support regulations and new customer expectations and about the importance of pursuing innovation as a risk mitigation tool and as a competitive imperative.

The new regulatory landscape that is a consequence of the world financial crisis is driving innovation in the financial services industry. Governments and regulators are aggressively pursuing greater transparency, vastly improved risk management solutions, and faster decision making. TowerGroup believes these requirements exceed the capability of most current solutions and will likely result in a market mandate for financial services firms to innovate regarding the ways they collect and use information. Another driver of innovation will be the economics of individual businesses altered by the degree of industry change and the impact of new regulations. For example, much of the investment management business is already experiencing severe downward pressure on fees. Faced with new requirements for greater transparency and disclosure, not to mention the new hedge fund registration rules, buy-side firms will be forced to look for innovative ways to reduce their cost base, which is bound to rise because of all these new requirements.

Nothing describes the mood toward innovation at Sibos 2009 better than Innotribe, the new SWIFT initiative that leverages the collective intelligence of SWIFT's broad community to find new ideas and projects and then establishes the infrastructure to help them grow. At Sibos 2009, Innotribe offered a rich program of presentations, face-to-face discussions, interactive workshops, and special challenges all aimed at one single goal: enabling collaborative innovation. Innotribe sessions were very well attended and moved the discussion on innovation forward in a meaningful way. Cloud computing was a frequent topic of discussion, with attendees expressing very different views about the future prospects of success for cloud computing as a way of accessing and delivering needed services. Exhibit 3 illustrates many of the key points from Guy Kawasakis' final plenary on innovation, which wrapped up the Innotribe track.

Exhibit 3

TowerGroup

Innotribe in Action at Sibos 2009

Source: Swift

As part of Innotribe, SWIFT organized a contest to identify the most promising new idea presented at Sibos 2009. Of the many good ideas presented, the judges selected an idea called eMe, a start-up proposing the introduction of a "digital safety deposit box." The concept involves storing personal information in a secure method under the safety of a bank brand. The benefit would be having a central trusted location that provides flexibility for customers dealing with vendors and for firms managing employee needs. This interesting solution is an excellent example of the truly innovative ideas discussed at Sibos 2009.

Crisis is said to be the ultimate motivator of change and innovation. Despite being in the midst of an economic crisis, Sibos delegates wisely seemed reluctant to innovate for the sake of innovation. However, they widely agreed that pragmatism should dictate what we innovate and why. For example, much of the discussion in the Banking and Securities tracks centered on greater innovation in the risk management process itself, so that the industry can better manage overall risk in global financial services.

Globalization

Globalization has always been a major theme at Sibos because of the international nature of SWIFT's business and the diverse group of attendees it attracts to the annual event. Which other major industry conference can you think of that is held in different continents each year and has traveled to over seven countries in the last 10 years?

The increasingly global nature of the financial industry was much discussed at Sibos this year and was a topic covered in several sessions. Through much debate, attendees reached the realization that globalization is not just about the opportunities for financial services firms to grow in foreign markets (especially emerging and frontier markets). Many other facets of this issue need to be closely discussed and debated as well.

First is the confirmation that the engine of growth for the financial services industry in the next five to eight years is likely to be Asia, especially China and India. This is especially true in certain business lines like consumer banking and payments. Dominic Barton, Worldwide Managing Director of McKinsey, warned Sibos 2009 attendees, "If you do not have a footprint in Asia, you will become an irrelevant institution within 10 years." The realization was also expressed at Sibos that Asia not only offers enormous opportunity but also can be a leader and a great influence in the global financial industry. The financial stability of Asian institutions compared to their Western counterparts in the last few years has given them confidence and strengthened the notion of Asia providing industry leadership rather than being a silent follower.

The euphoria about Asia being the growth engine for global financial services in the next many years was tempered by some new realities discovered by Sibos 2009 attendees. One is that further growth in major Asian markets will require critical changes to local regulations and financial practices and greater maturity of local markets. A comment about Indian regulation from James Shapiro, Head of Market Development at the Bombay Stock Exchange, says it best, "It's time for India to be more relaxed over the participation of foreign international investors to allow it to benefit from greater capital flows and, more importantly, new investment practices." Another realization was that for emerging markets to lead economic and financial growth in the world, they must not only focus on export-led growth but also stimulate domestic demand. The opinion of Huiman Yu, Vice President of ICBC, was also spot on: "If we cannot boost consumer demand, the sustainability of growth will be checked."

Another theme that emerged is that globalization does not just mean Western financial firms entering emerging markets; it also means emerging market institutions competing in Western markets like United States and Europe. Leaders from the biggest transaction banks discussed this issue during their panel, mentioning the growing ambition of banks like ICBC to compete with Western banks on their home turf, whether it is New York or London. There was general agreement that emerging market institutions would need to invest significantly in new products and to acquire customer and market knowledge to compete effectively in Europe and North America. This is especially true in areas like consumer banking, in which understanding the needs of Western customers may require considerable investment of time and attention, or the securities business where Asian firms will need to develop securities expertise and knowledge to operate effectively in the West.

An important aspect of financial services globalization is the need for global institutions and local regulators to cooperate across regions on crafting rules and harmonizing regulations. Inadequate coordination across regulatory agencies and their practices is one widely acknowledged cause of the recent financial crisis. The actions of major central banks and financial institutions in 2007 and 2008 to control the financial crisis lacked coordination, which significantly delayed the recovery process and exacerbated the severity of the crisis. SWIFT and its community can play a major role in coordinating and facilitating global action to ensure a more stable future for the financial services industry.

The nature and timing of the global economic recovery is another aspect of globalization that was debated. Delegates argued, on the one hand, that the world economy is still in the interim stages of globalization, globalized just enough so that all regions have been affected by the financial collapse. (This view disputes the decoupling hypothesis that the fate of emerging markets is unrelated to that of developed markets.) On the other hand, the economy is not globalized enough, such that emerging markets are recovering much faster than developed markets with the MSCI EAFE index up 74% through October 8, 2009, while the MSCI World Index was up by 44%.

Financial Services Responsibilities

A hotly debated issue at Sibos this year was: What does the financial sector owe to the wider economy? What are its responsibilities? Joseph Yam, CEO of the Hong Kong Monetary Authority, said, "Financial systems should not have a life of their own." This was a stern reminder that the financial industry exists not just for itself but also to make the rest of the economy operate efficiently. The responsibilities of the financial industry were being discussed at Sibos because of major failures in regulations, laws, practices, business models, and risk measures undertaken by the financial industry in the last few years.

Although all sectors of the global economy have suffered, the financial services industry has been at the center of controversy about the financial crisis, with serious questions being raised about the industry's responsibility to the global economy, excessive executive compensation, financial bailouts, and the lack of transparency and disclosure. Even though most failures and bailouts of financial firms have happened in the United States and Europe, a cloud hangs over the entire global financial industry. Even Asian institutions are realizing how inextricably linked their prospects are with those of other regions.

With the global financial industry under siege for the last two years, under pressure from regulators and shareholders, and being questioned by governments and the public, attendees came to Sibos this year with humility and some acceptance of responsibility for the collapse of the global financial system. While attendees from some regions had a greater notion of responsibility for the global financial failure than those from other regions, almost everyone left with the profound realization that we are all part of one industry and must work together to restore investor faith and confidence in our business.

Several areas were discussed in which the financial industry acknowledges that further improvements could be made. There was acceptance that product innovation and complexity had grown out of control in the last 10 years. There seemed to be agreement that the industry needs to migrate back toward simplicity and investor education with regard to new products being introduced. Greater transparency and disclosure was another area identified as being important. Atsushi Saito, President and CEO, Tokyo Stock Exchange, said, "The lack of transparency was the cause of the current crisis." Kah-Chye Tan, Global Head of Trade Finance, Standard Chartered, asserted: "We owe it to our customers to rebuild trust."

The next area of collective responsibility that was identified involves working with regulators to better explain how the industry works as well as its perspective so the regulators will consider the wider implications of their actions when they promulgate new rules and regulations. Cathy Bessant, President, Corporate Banking, Bank of America, said, "How we do what we do is a mystery to those trying to regulate or nationalize us. We need to educate them." The last area of financial responsibility was better and more effective risk management practices to be undertaken by the industry. One example is curbing the amount of leverage that securities firms can take on.

Amid the doom and gloom of the last few years caused by excesses in the global financial system, some financial services industry participants recognize that several industry infrastructures worked very well and averted much greater disaster. Mike Bodson, Senior Managing Director of DTCC, talked about securities infrastructure, noting that the "clearing and settlement systems succeeded in providing stability, safety, resilience, and risk reduction during the crisis." Similar comments were made about the payments infrastructure, which held up remarkably well despite all the stresses and strains it experienced during the meltdown. These examples give us faith in the resilience of the financial industry. Participants in the industry need to rededicate themselves to fixing the things that did go wrong, however calamitous the outcome may have been.

Collaboration and Coopetition in Financial Services

SWIFT CEO Lázaro Campos opened the closing plenary at Sibos with the word "collaboration." It's a concept that all Sibos participants understand well and can relate to, since SWIFT itself exemplifies successful industry collaboration. The less familiar concept of "coopetition" was also a topic of frequent discussion at Sibos 2009 (the neologism combining the words competition and cooperation, goes back almost 100 years). Coopetition, a topic that came to the fore at Sibos 2009, in many ways captures the essence of Sibos. Where else could you see so many competing firms gather at a single location and hold open and frank conversation about major challenges facing the financial services industry today?

A clear example was the Big Issue Debate 3 on the Transaction Banking business — a panel discussion among four heads of transaction banking from Citi, Bank of America, HSBC, and Deutsche Bank. Fierce competitors, they discussed opportunities to collaborate on noncompetitive elements (like infrastructure) which could not just benefit the banks by lowering costs but also offer better service to clients and reduce operational risk for the entire industry.

Many delegates came to Sibos this year wondering what factors had changed from last year and how well the industry weathered the recent turmoil. The bullish answer, at least from the Banking sessions, was that large parts of the business had worked remarkably well, largely because of industry participants having worked closely together through the crisis. Throughout the conference, however, there was a clear call to the industry not to rest on its laurels. New legislation was highlighted as a major area for which greater collaboration is required. Financial institutions from every region and across banking, payments, and securities discussed a shared responsibility to ensure that regulators don't create new legislation in a vacuum and to limit any unintended consequences of new legislation. There was a warning to all attendees that though although financial services providers have survived the crisis and are witnessing signs of growth again, they must work with each other and with global regulators.

Collaboration takes many forms. Standards is one area in which it has clear benefits. During one of the Standards Forum sessions, Tomas Kindler, Managing Director of Link Up Markets, said: "Standardization enables a level playing field — players can then compete at the value-add layer." Under SWIFT's leadership, the global financial services industry has made great strides in standardizing major financial processes across banking, payments, and securities processing in the last 20 years. Standardization has lowered costs for individual and corporate customers, greatly enhanced client service levels, and lowered financial and operational risk.

However, a sense of collaboration and coopetition doesn't extend equally across all participants in the global financial services industry, nor across all geographies. Institutions in the securities industry, particularly the large investment banks, have historically been loath to collaborate, thinking of each other as arch competitors. Indeed, examples of true collaboration are far fewer in the securities industry than in payments and banking. This is partly because of the highly competitive nature of the securities business and partly because in trading, one investor's gain is always another's loss. If an investor gets out of a bad stock in time, then by definition someone else is left "holding the bag." Nonetheless, even in the securities business, there are glimmers of hope for common ground because of the intense criticism and scrutiny of the global securities industry during the financial crisis. The post-trade processing space is one area in which securities firms worldwide are keen to work together, although we will need to wait to find out if such efforts bear fruit.

Looking forward, it will be interesting to see how much of the collegial ethos evinced at Sibos will continue. The most likely place will be in payments, where vehicles for discussion already exist and collaborative bodies such as SWIFT provide a platform for deeper discussion. With the engagement process known as "2015" that SWIFT is undertaking to determine where it should focus its attentions, perhaps banks will review where they will focus their own activities and seek opportunities to explore collaboration and coopetition. Payments has more elements than other parts of financial services that can be considered "plumbing" or support infrastructure and where cooperation is likely to be more beneficial than competition.

Future Direction of the Financial Services Industry

As Martin Wolf, chief economics commentator of the *Financial Times,* noted in the first Big Issue debate, "Despite rebounding stock markets and unprecedented levels of government intervention, the world's financial and economic infrastructures remain under a cloud of uncertainty." Although this observation is true, the uncertainty varies by the type of business, because the impact of the downturn has been uneven across different types of financial services firms and across different regions. The question becomes: "What will be the future of the financial services industry in light of the newfound realizations around risk and all the impending regulations?"

For the payments business, the outlook remains positive. Funds still need to move between payers and payees, and the payments infrastructure remained resilient even during the height of the economic downturn. However, the overall decrease in payments volumes reported by SWIFT and many Sibos delegates is unsustainable over the long term and endangers existing business models, as noted by Citi's Global Head of Trade and Supply Chain Finance, John Ahearn. Even greater uncertainty remains in the consumer lending and securities businesses, where credit standards have been tightened in response to credit losses and derivatives have become taboo because of their perceived lack of transparency. Collectively, these interventions, resilient qualities, and market shifts have somewhat restored confidence in the market, but what of institutional trust? Sibos delegates and clients wanted answers to two key questions: When will the markets return to "normal"? What will be the future of the financial services industry?

The challenge in trying to "get back to normal" is the financial industry's need for appropriate risk taking, especially in the lending and securities businesses. Risk taking is what drives much of a financial service firm's profits. With profits come rewards in the form of incentive bonuses, which in turn drive firms to push the boundaries. However, the amount of risk taking and the overall lack of transparency have come into question because of the financial crisis. Hong Kong Monetary Authority CEO Joseph Yam raised the issue of the pursuit of profits (and bonuses) leading to lower financial efficiency and increasing risk to the financial system. Ronnie Chan, CEO of Hang Lung Properties, was blunt in his assessment that there is "no other industry with more conflicts of interest than investment banking." The logical inference is that the previous normal state of the financial services industry may no longer exist. Instead, there will be a "new" normal state in which risk taking is more sober and deliberate — at least for a while.

If we know where the risks lie in terms of transparency, risk taking, and conflicts of interest, what is the right course of action? Is heightened regulation truly the right approach? The sentiments expressed universally by Sibos 2009 attendees were aptly summed up by Andrew

Long, Global Head of Transaction Banking and group General Manager at HSBC in the statement: "Regulation will be increased, driven by politics and emotion." The question is simply when more regulation will be forthcoming, not if. This belief initially left many attendees resigned to higher compliance requirements and costs (which may or may not be passed to clients) as well as an atmosphere in which regulations would be made in a vacuum without industry input. This sentiment was best put by Franco Passacantando, Managing Director, Central Banking, Markets and Payments Systems Area, Banca d'Italia, who said, "We risk adjusting for the problems of the past while failing to anticipate the problems of the future."

Protectionism seems to be an element of new regulation, as governments seek to safeguard their domestic markets — a stance that Lawrence Webb, Global Head of Trade and Supply Chain, HSBC, described as "bad for the world." Such underlying aspects of new regulation will greatly hinder the market harmonization and standardized global regulation desired by financial industry. The goals of harmonization and standardization are already beset by conflicting approaches and degrees of enforcement as well as lack of clarity about the dates that major industry initiatives like SEPA and Target2 Securities will take effect.

After critical dialogue at Sibos 2009 about imminent regulations, attendees from different businesses and different regions realized that they need not feel helpless about new regulations being promulgated without their input that would determine the future of the financial services industry. Instead, the financial industry has an opportunity to engage directly with regulators to demystify the inner workings of their firms and to help balance the conflict between what's good for individual companies and what is in the long-term interest of the entire financial system. Together, the financial industry and its regulators can and should collaborate to create a consistent regulatory framework that provides the transparency that markets, regulators, and clients require.

Summary

Sibos 2009 (www.sibos2009.com) succeeded in its mission to bring the global financial services institutions together to conduct critical dialogue on major issues facing the industry today. The event recorded its highest Asian attendance ever, evidence of the changing prospects of future growth for the financial services industry. By attending almost two-thirds of the more than 100 sessions and through countless conversations with attendees, TowerGroup analysts identified five major themes that emerged at Sibos 2009: innovation, globalization, financial services responsibilities, collaboration and coopetition, and the future of financial services. Each of these themes was the subject of critical dialogue at Sibos, and attendees left the conference with a much richer understanding of these issues than they had when they arrived.

Although innovation seems taboo in many parts of the financial services industry right now (most definitely in securities), it is certainly not dead, and firms are considering how to innovate in areas like risk management, product distribution, and delivery.

Regarding globalization, Sibos 2009 reaffirmed the tremendous growth potential of Asia, but attendees gained the understanding that markets like China and India need to make major reforms before their true growth potential can be realized. Asian banks seeking to enter Western markets were cautioned that competing with current players in the West will require significant customer knowledge and new product creation suited to Western markets.

On the theme of collaboration and coopetition, the world's largest transaction banks acknowledged that although they are arch competitors in some areas, they are ready to collaborate on areas like shared infrastructure.

The theme of financial services responsibilities was at the center of critical dialogue about what the financial services industry's responsibilities to other industries, to governments, and to the general public. Recognition was clear that the industry must take greater responsibility for its actions and governments, investors, and the public will hold financial services players more accountable for their actions in the future than they have in the past.

The future of financial services occupied heightened attention at Sibos 2009, the key issues being how the industry's future would be influenced by new regulation, the altered view of risk management, and continued uncertainty.

Sibos 2009 is over but critical dialogue on its main themes continues around the world within banks, securities firms, trade services divisions, and at corporates, as well as across the Sibos community at www.swiftcommunity.net. We urge you to actively participate in this dialogue and do your part in moving the financial services industry forward while SWIFT prepares for Sibos 2010, to be held October 25–29 in Amsterdam.

TowerGroup

SWIFT commissioned TowerGroup to prepare an independent and objective perspective on the themes, trends, and concerns discussed in conference sessions and dialogues among attendees at Sibos 2009. The content of this report is the product of TowerGroup and is not tied to any vendor product or solution.