

Strategic Analysis of Japanese Megabanks - Macro Scenario Analysis of Financial Services

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April 2020

We perform a series of 5 strategic analyses of Japanese Megabanks. This paper is the second analysis in the series, where we carry out a macro scenario analysis of financial services relevant to Japanese Megabanks. We look to study the implications such a scenario analysis has for corporate strategy, outline the time and scope of the analysis performed and highlight the limitations via a case study with reference to RUS¹ Megabank.

Introduction

We perform a macro scenario analysis of the Financial Services industry and UK Corporate Lending sector as per appendix A. The PESTEL acronym is used to identify the key industry drivers as per table 2.1.

Table 2.1 PESTEL Key Industry Drivers

- Political
- Economic
- Social
- Technological
- Ecological
- Legal

A PESTEL scenario analysis can be used with a **prediction** emphasis to forecast megatrends, inflection-points and weak signals or with a **learning** emphasis to generate scenarios of plausible future macro environments in order to manage uncertainty, external opportunities and threats. (Ramirez et al 2017).

¹ See appendix for full case study details

Scenario Analysis

Firstly we use PESTEL analysis to identify industry opportunities and threats.

Reviewing the key environmental drivers, from figure 2.1, for the financial services industry and UK corporate finance sector leads to the following discussion points.

Figure 2.1 PESTEL Macro Industry Analysis for Financial Services

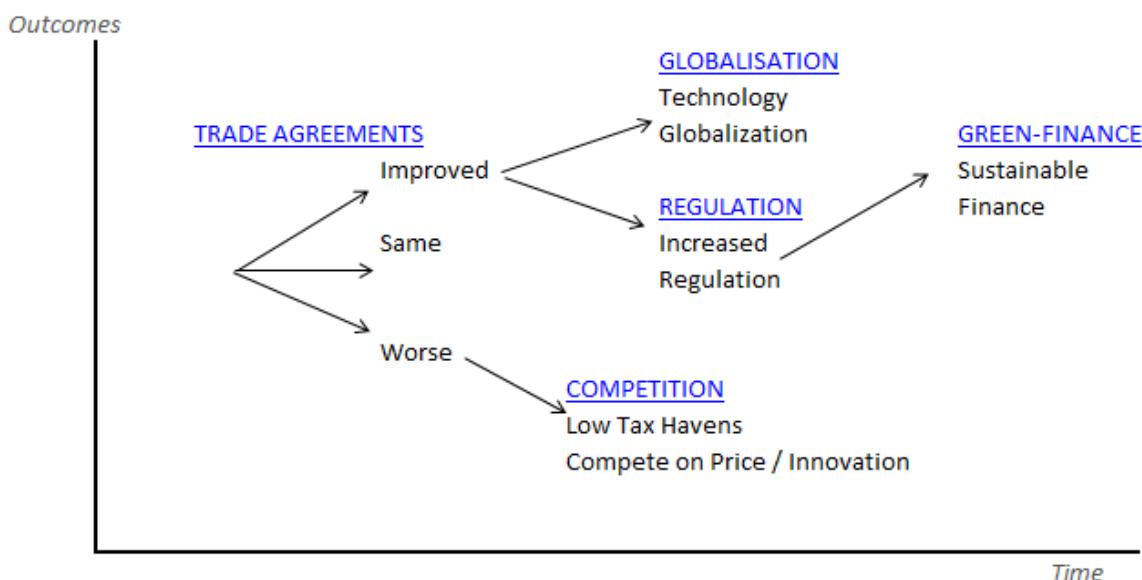


- Political
 - Widespread **regulatory disruption** from FRTB, Basel III et al
 - **Hard-Brexit** risk of adding trade barriers and additional cost to businesses
 - New trade deals and increased **globalisation** opportunities to access to new markets
 - Interest rate / **Libor reform**, see [\(Burgess, 2019a\)](#) and [\(JP Morgan 2019\)](#)
- Economic
 - Weak economies & **quantitative easing** programmes
 - Negative interest rates i.e. pay to deposit funds!
 - First-to-market opportunities to capture market share from Libor reforms to markets and products, similar to that experienced by Tesla [\(Forbes, 2020\)](#)
- Social
 - Exodus of IT workforce due to **UK Tax Reform** (IR35)
 - **Workforce disruption** and economic fallout from coronavirus (COVID-19)

- Technological
 - Business opportunities in **digital finance**
 - New technology benefits using machine learning, AI, cloud technology etc.
 - Innovation is costly however ([Burgess, 2019b](#))
- Ecological
 - Major opportunities financing large-scale government '**green projects**' to combat climate change and meet carbon-neutral infrastructure targets
 - Social media, activist and reputational risk pressures
- Legal
 - Libor reform and existing contract disputes. Over \$350 trillion of existing loan contracts are linked to Libor ([JP Morgan, 2019](#))

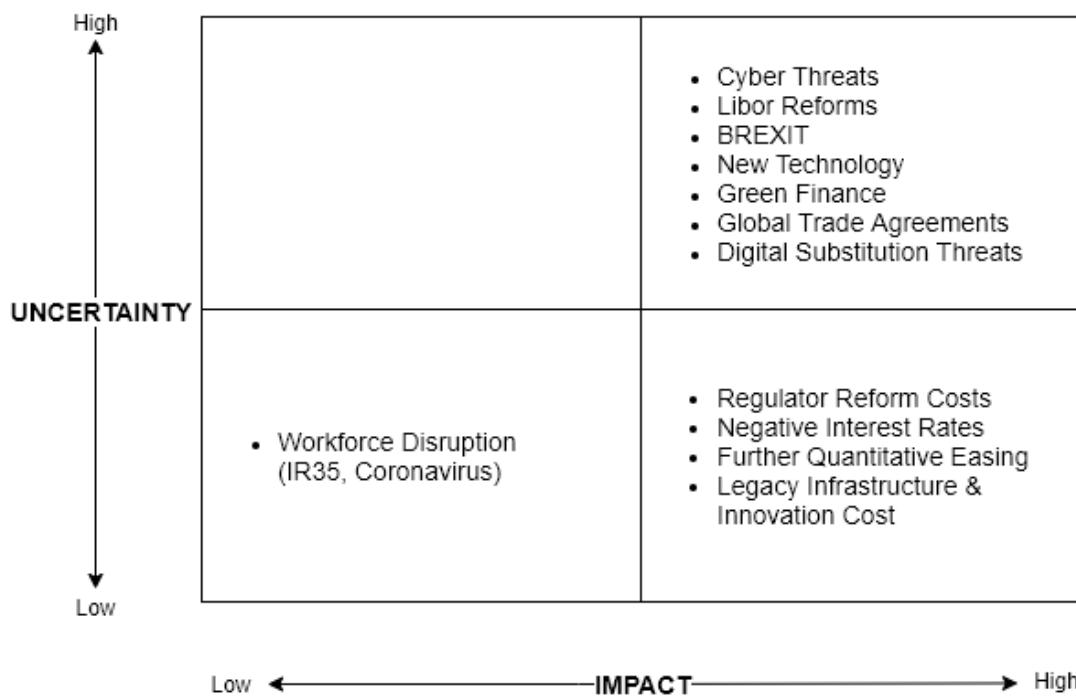
Firstly using the above 'PESTEL' analysis we forecast the current megatrends to **predict** plausible future scenarios as shown in figure 2.2.

Figure 2.2 McKinsey Topology of Uncertainty using Alternative Futures Approach



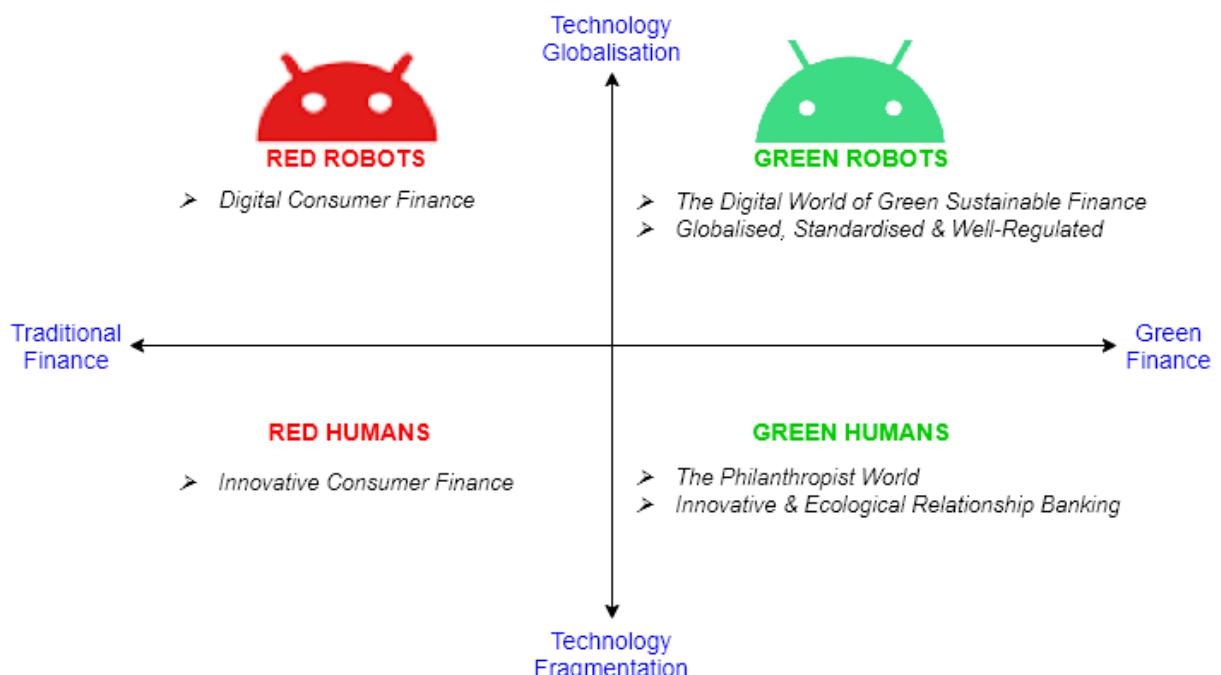
Secondly we apply the key drivers from figure 2.1 to a scenario matrix with a **learning** emphasis to help reframe RUS strategy to be robust enough to manage high uncertainty and high impact events.

Figure 2.3 Scenario Matrix of Uncertainty – Key Industry Drivers for Financial Services and UK Corporate Finance.



Considering two plausible **independent** drivers with high **impact** and **uncertainty** from figure 2.3, we select new technology and green finance to conceive the four worlds of financial services in figure 2.4.

Figure 2.4 The Four Worlds of Financial Services



Time Span & Scope

The time span for the analysis was five years, chosen to capture market disruptions and events from the current industry cycle. We didn't want to predict and extrapolate too far into the future to restrict the analysis to plausible outcomes. The scope of the analysis was to the financial services industry and the UK Corporate Lending sector.

Limits of the Analysis

The PESTEL factors can be unstable and quickly change, making aspects of the analysis redundant. The scenario matrix in figure 2.3 performs well on the extremes with high and low factors, but manages moderate key drivers less effectively, blurring in the analysis. The scenario analysis supports pipeline industries better than it supports platform or global industries that are highly interconnected. It can be difficult to assess global businesses the Japanese deposit market and UK lending markets effectively at the same time.

Implications for Organisation's Strategy

Considering the alternative futures demonstrated in figure 2.2 RUS appears **risk averse** and **well prepared for external challenges** such as 'Hard-Brexit', FRTB, Basel III and Libor Reform ([JP Morgan, 2019](#)). However RUS is ill-prepared to exploit advances in technology and green finance opportunities due to **legacy core system constraints**.

The alternative worlds presented in figure 2.3 indicate that RUS' strategy is **best suited for traditional finance** 'Red Human' worlds and not sufficiently prepared for highly automated, innovative 'Green Robot' worlds.

In order to defend core businesses, trade new products and increase market share I recommend enriching performance metrics to include ROCE² and production credits³. This would improve visibility of the value chain, see ([Burgess 2020c](#)) analysis 3, figure 3.1 and highlight the business units creating value to invest in and those diluting value to be pruned. The lack of such metrics is effectively a tax on business as shown in analysis 3, figure 3.3.

To mitigate the reliance on legacy infrastructure and products, fintech and internal alliances should be explored to increase economies of scale, innovate efficiently and reduce cost overheads ([Kavadias et al 2016](#)). Caution should be exercised here and alliances should only

² Return on Capital Employed

³ Similar to sales credits to measure value generated by non-profit centre business units such as HR, research teams etc.

be formed when value can be added, perhaps with our American internal partners where cultural and other CAGE⁴ distances are low ([Ghemawat et al 2019](#)).

Appendix

Case Study

Organization: Rainbow & Unicorn Securities, London (RUS)

Industry: Financial Services

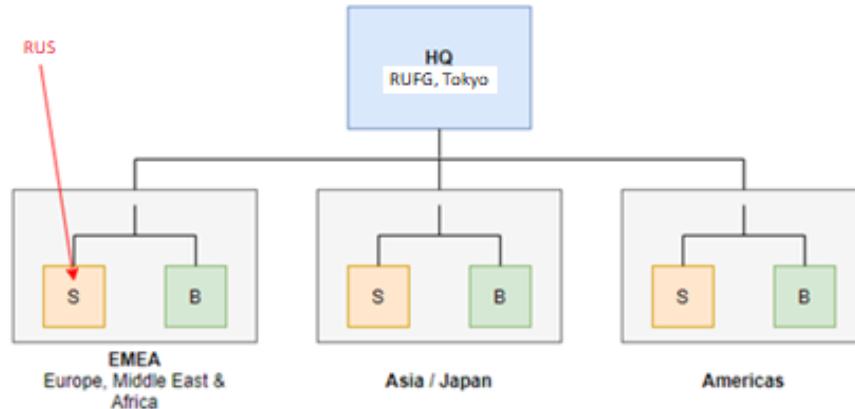
Sector: UK Corporate Lending & Project Finance

RUS provide financial services, trading expertise and risk management solutions within the interest rate, fixed income and credit markets. It specialises amongst other things in corporate lending and project finance within the UK and also Europe, Middle-East and Africa (EMEA).

RUS is fully owned by Rainbow & Unicorn Financial Group Tokyo (RUFG), which has a sizable balance sheet, predominantly due to large Japanese deposits. Japanese investors are extremely risk-averse with many business relationships based on trust, reputation and long-term track record formed over decades!

RUFG is one of three 'Japanese Megabanks' that dominate the financial services industry in Japan with combined deposits exceeding USD 10 trillion ([Piece-of-Japan, n.d.](#)). RUFG itself has assets of USD 20 billion and employs 50,000 staff with 500 offices worldwide.

Figure A1: RUFG Organization Chart



⁴ An acronym to describe cultural, administrative/political, geographical and economic differences, which often destroy value.

RUFG has 3 regional hubs to provide concentrated coverage in Europe & EMEA, Asia & Japan and the Americas. RUFG subsidiaries are siloed with Corporate Banking (B) ring-fenced and Investment & Securities (S) businesses separated to satisfy legal and regulatory requirements.

Corporate Banking subsidiaries (B) have large balance sheets, good access to capital but poor legacy systems & infrastructure. Investment & Securities (S) businesses however have good technology and systems, but small balance sheets and little access to capital.

This case study is fictional, yet inspired by adapted from real-world industry practice and first-hand experience.

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