NextWave

Integration of GSIB organisations

Devising a strategy for operations integration capabilities

April - 2023

GSIB merger and integration approach

Banks have endured a turbulent ride over the past 15 years. Markets have evolved, margins have been squeezed and regulation has dictated the terms of engagement (think mandatory clearing and mandatory reporting). Certain functions of the traditional global markets infrastructure, namely Fixed Income Securities, have remained largely unchanged. The US Securities Market is undertaking a necessary realignment of its Settlement Model (T+1). This is the context around Global Change programmes required to keep the lights on.

What is the most interesting aspect of GSIB's? Well, the fact that internal infrastructure has remained largely in place, over the past 15 years. Roles, have changed, primary locations have become slimmer, as further afield, centres of processing excellence have swelled across cities in Asia, Eastern Europe, and smaller Cities/States within the more familiar Western Countries. By and large, this has been a consistent strategy across the majority of Sell Side firms and has enabled Banks to build footprints across these locations, build feeders from local University Campus and deliver cost effective operating models to enable Banks to offset the squeeze on margins. A largely successful strategy, with no plans to do anything different yet (ChatGPT might well change that, but let's not predict or hypothesize yet).

Roll the clock forward to March 2023, and we are witnessing and awaiting the ink to dry on the Credit Suisse/UBS Tie-up. Nobody has any insight into the Strategy around how these Big Beasts will move ahead! What will be integrated, people, business units, positions, infrastructure, what will remain and be wound down over a period of time, and what will be touted for immediate sale. The recent news around Credit Suisse AT1 Bonds, will no doubt make for an interesting representation in the Q1'2023 Financials, but the most intriguing conundrum, no doubt comes with the question that UBS will be pondering over, which is how do we make these Credit Suisse pieces fit neatly, or neatly over time, into a broader and deeper UBS Jigsaw, which has been performing well since they decided to scale back their Investment Banking/Markets business over the past 10 years.

How much time does UBS have before the weight of the Credit Suisse Anchor pull the ship further down, and either the lower levels burst and float away into the sea, or they remain trapped with no escape.

No doubt, each Business needs to have clarity, but there are often such complex inter-connectedness within GSIB's, that each business needs to be forensically analysed through multiple lenses, to assess what they want to achieve, with the $1billion question being, 'How are we going to do it".

GSIB Merger and Integration Approach

If we head back to the previous Offshoring strategy, yes, this works in a BAU (Business as usual) construct, but do these functionally aligned verticals possess the deep business knowledge, and the Front to Back prowess to integrate and possibly migrate tens of thousands of positions, hundreds of thousands of open trades, and 2 of the biggest challenges, what to do with matured and failing trades and approx. 60% of trading book volume which exists to support Inter-company (intermediated) activity?

The true litmus test for success resides with the true substantiation of Bank Balance Sheet accounts i.e. the general ledger accounts, representing, in simplest form, the presentation of 'Realised/Settled Cash'. It is true that accounting entries are posted, reversed and reclassed and reclassified and it is true that the vast majority of accounting entries are systematically generated through Accounting Engines, containing deep and complex rules, some of which are so complex, that the IT developers who implemented the accounting code within the Operations infrastructure have moved on or left the organisations some years ago.

The Back Office Control/Finance teams who perform the month-end sign-off process, consider successful sign-off and substantiation as merely managing by exception, without the appreciation of evaluating the concept of a true cash reconciliation, or implementing scenarios which review the 'close-down' position of a Legal Entity set of accounts, and the appreciation of a race to the bottom. Forensic evaluation is no longer deemed to be a core control either on a day to day or month-end close basis.

If all positions and trades were off-loaded, would the Bank Nostro (Bank Accounts) be fully explainable, or would there remain the accumulated Life to Date P&L, generated over the years, which by design has already been hedged out to the Bank's Ledger ccy, so even applying any residual would need to be approached with a 'wow' factor, of who/which business line is going to get the residual cash, or inadvertently, have to stump up the cash to clear down the shortfall?

Years of Industry reconciliation platforms have existed, but none have fundamentally questioned this, probably because no bank would ever want to predict the need to have it, but it does raise questions about how truly under control are all those Back office organisations, all mandated to understand, reconcile, substantiate and sign off each account balance and reflect and attest to the accuracy of the Bank's Books and Records.

GSIB Merger and Integration Approach

Banking mergers and integration have been with us forever. Now, with the increased number of incumbents in the market and some may say the market is "overbanked" banks continue to seek to drive cost reduction and efficiency programs. So what factors to consider when undertaking an integration?

Firstly, and probably most importantly, is the question of strategy. Why are two banks choosing to integrate? We often hear of the word "synergy" but how is it measured and quantified? Synergies refer to the expected cost savings, growth opportunities, and other financial benefits of the combination of two entities. The synergy of a merger or an acquisition is the value of the e combined entity minus the fair value of the two firms as separate entities,

There are a number of considerations that need to take place from the pre-merger, execution, and post-merger phases.
The word "strategy" is banded around quite loosely. CEOs and Boards need to consider the overall focus of the combined entity. Important questions such as is the bank going to be famous for wealth management? Or will the bank be in emerging markets? The strategy and focus are some of the key initial points for consideration. Typically senior management work with ExCO members, shareholders, and the regulator to essentially define what the bank wants to be famous for. As many incumbents now dominate the market place having this clearly articulated is critical.

As we get into the implementation of the integration, the next key area of consideration is the operating model. Essentially, a clearly defined operating model must detail legal entity structures, and organizational structure and translate the strategy into implementation. This will include consolidation of financial reporting. In addition, cross-divisional requirements and obligations need to be carefully consolidated.

Data is probably one of the most important areas of integration planning due to heightened regulatory environments. SMCR, conduct and culture, MiFID, ESG, liquidity, and funding and liquidity requirements all require prudent capturing and monitoring of data. Data models need to be carefully architected and converted for business activity. Automation and manual processing opportunities as well as data cleansing. In the case of large financial institutions with legacy systems, consolidating, cleansing, and effecting reporting of data can be taxing activity. It is, for this reason, an increased number of banks are partnering with fintech or building their own technology capabilities. Legacy reconciliation platforms will need to be reviewed as part of consolidation exercises.

Pre-Merger Approach

Ensuring your Organization is ***'Factory Ready'***

1

	Actions	Outcomes
Evaluation of Existing Strategy	• Review existing Portfolio and Associated Strategic Programmes • Review existing RTB vs CTB Programmes	• Defined Roadmap of Programme deliverables • Classification of Mandatory vs Discretionary • Business Cases, Funding Source, Duration, ROI
Evaluation of Business Performance	• Regional vs Global Products and Services • Revenue vs Cost Assessment • Evaluate 3rd Party vendor Costs (ie: Data, Custody, Clearing)	• Defined Business ScoreCard • Evaluation of Performance, Risk and Control • Incident Evaluation (Operational Risk)
Operating Model Design	• Documented Operating Models, by Asset Class • Regional Footprint • Inter-Company Booking Models	• Evaluated Client Jurisdictional activity • Optimized Bi-lateral vs Netted Opportunities (Clearing Cost and Reduced Settlement Fails)
Digitation / Data Strategy	• Defined and Documented Data Structures • Regional Variances and Data Stores • Assessed Manual Processes/High Touch Points	• Data Cleanup (Tactical approach) • Data repository / Warehouse identified
Regulatory Assessment / Remediation	• Documented Regulatory Effectiveness, utilizing Horizon Scanning • Existing Regulatory Reporting Regime • Up-coming Regulatory Reporting Regime (ie: CRD6)	• Identified Business Reporting deficiencies • Business and IT Architecture documented • Regulatory Reporting Risk Mitigated
Liquidity / Capital / Funding	• Defined Liquidity Swing reporting (x-entity) • Establish Collateral Pools • Optimize Inventory • Evaluate Failing Transactions	• Treasury Funding Model Documented • Firm Financing and Capital Ring-fencing • LCR Calculations and Swings

Integration Approach

Ensuring your Organization is *'Execution Ready'*

2

	Actions	Outcomes
Execution of Integration Strategy	• Programme Definition • Divisional and Cross Divisional Co-ordination • Central Programme Governance	• Execution Roadmaps • Execution Run Books • Communication (Internal and External)
Business Migrations	• Identified Business Units • Identified Asset Classes • Identified Hedges • Identified Collateral	• Risk and Exposure migrated to New Entities
Business Wind-Downs	• Business Tooling to run multiple simulations to protect and orchestrate migration activity	• Legacy Business Risk managed and Operationally managed to Wind-down
Data Mapping / Hierarchy	• Define Integration Data Mapping required • Data Creation and Testing	• Data Structure implemented for Conversion of Business activity
Tactical Migration Architecture, Tooling, Reconciliation Platforms	• Integration Reporting created • Positional and Transactional completeness • Front to Back Integrity (all Asset Classes) • Internal vs External Reconciliation / Remediation	• Successful Dress Rehearsals for Conversion of activity • UAT testing for Tactical Tooling • Reconciliation Platforms exist post Migration
Risk & Control Readiness (Exceptions: Finance, Operations, Client Receivables	• Balance Sheet Substantiation • P&L Signed off and Reconciled • Fails, Reconciliations substantiated	• All activity successfully converted and reflected within Books and Records • Full Front to Back Sign off of all positions ahead of Day 1 business

Post Integration Stabilization

Ensuring your Organization is *'Operational, Robust and Controlled'*

3

	Actions	Outcomes
Run the Bank Strategy	• Incorporation of broader and deeper business units • Pre and Post Integration Performance Metrics • Key Risk Indicators	• Adapted Reporting Suite to meet new Control Framework and Standards • Dynamic Performance and Risk Management reporting • Pre and Post Integration evaluation
Residual Business Wind-Down	• Adaptation of Non-Core residual business units to fit new Risk and Control Framework • Determine Ring Fencing Capabilities • Evaluate Resourcing Augmentation for Non-Core	• Non-Core Operating Model • Determine Legal Entity Warehouse of legacy positions • Evaluate Infrastructure and architecture capabilities required
Internal Infrastructure / Architecture Capabilities	• Evaluate Residual Business and Technology requirements • Evaluate redundant components (ie: Trade Netting/Settlement Netting)	• Legacy Business Risk managed and Operationally managed to Wind-down • Legacy Reconciliation Platforms evaluated
External Market Infrastructure Capabilities	• Nostro, Depot, CCP, Exchange memberships, Swift Gateways, Agent Bank Network, Market Utilities (FX, OTC, SBL, Securities)	• Cost elimination analysis • Account Closures (external and Internal) • Retained Capabilities with Outlined Duration
Tactical Non-Core Architecture vs External Platform Sourcing Capabilities	• Evaluation of Reduced Infrastructure Tenancy • Evaluation of Non Core Unit Duration • Assess viability of 'Off the Shelf' Platform to meet Business requirements	• Fully Justified Business and IT Architecture Design • Global Operating Model and Business activity • Run the Bank Spend
Organizational Design, Reporting Hierarchy, Cross Divisional Integration	• Organizational Design • Consolidation of Functional Reporting • Integration with Cross Divisional Requirements and Obligations	• Booking Procedures and Policies around Trade Execution Capabilities • Liquidity and Collateral Requirements