

What lies on the horizon?

New Players – New Rules – New Opportunities

The Outlook for Financial Services M&A in Asia | June 2010



the 1990s, the number of people who are employed in the service sector has increased in all countries. In the Netherlands, the number of people employed in the service sector has increased from 1.5 million in 1980 to 2.5 million in 1995.

There are several reasons for this increase. First, the service sector has become more important in the economy. Second, the service sector has become more attractive to workers. Third, the service sector has become more flexible.

The service sector has become more important in the economy. In 1980, the service sector accounted for 55% of the Dutch economy. In 1995, it accounted for 65%.

The service sector has become more attractive to workers. In 1980, the service sector accounted for 45% of the Dutch workforce. In 1995, it accounted for 55%.

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Executive Summary

Welcome to the fifth Asian FS M&A survey and report, entitled 'What lies on the horizon? New Players – New Rules – New Opportunities. The outlook for financial services M&A in Asia'.

This report is based on the findings and analysis of face-to-face interviews, web and telephone surveys of 122 senior M&A decision makers or influencers from across 13 territories in the region. The research was conducted on behalf of PricewaterhouseCoopers¹ by IDC Financial Insights Asia-Pacific during March and April 2010.

The report presents the overarching themes of the M&A scene within Asia's financial services sector and also reveals how these players are evolving in a post-crisis world and comments on their own growth trajectory and acquisition plans.

The report further touches on the drivers, and conversely the road blocks that would influence an acquisition. It concludes with the thoughts of the executives surveyed on the near-term M&A trends as their financial institutions continually evolve to respond to changing market dynamics and investment opportunities.

Among the key findings of the research:

Impact of the crisis in this region was not so much on revenues...

The Asian financial services industry (FSI) remained resilient amidst the adverse economic conditions of 2008–2009, with less than 16% of total respondents reporting year-on-year (YoY) declines in revenue. Contrary to expectations, despite the economic turmoil that characterised most of 2009, an impressive 54% managed to report higher revenues last year.

As we move further into 2010 and signs of post-crisis recovery become increasingly evident, confidence amongst the financial services industry in Asia-Pacific is growing in tandem with revenue. With the exception of operations in selected developed countries such as Australia, Japan and South Korea, seven in ten institutions interviewed for the study expect to grow their revenues in excess of 10% over the next 12 months.

Nonetheless, financial institutions across the region face some prevailing growth inhibitors that could constrain them from expanding revenues quicker this year. These include:

- a shortage of employees with the appropriate skill-sets;
- uncertain or restrictive government or regulatory policies, and
- limitations stemming from a lack of investments and efficiencies in technology platforms to support evolving business requirements.

...But on the competitive landscape

It is clear that the financial upheaval brought along changes that will prove to be much more significant and longer lasting than any ramification to earnings. We note the following observations:

- **The rise of Asia's super-regionals:** As forecasted in PricewaterhouseCoopers' report last year, 'Fortune Favouring the Brave', Asian FSI powerhouses have captured unprecedented growth opportunities to emerge as winners from the crisis. 'Super-regional strategies' refer to attempts by Asian-based institutions to acquire and manage regional units that are close in proximity to their headquarters or clustered within one part of the region. Early super-regional templates have already been crafted out by institutions in Australia: Australia and New Zealand Banking Group Limited (ANZ) and Commonwealth Bank of Australia (CBA), Singapore: DBS Bank, OCBC Bank and United Overseas Bank (UOB), Malaysia: Malayan Banking (Maybank) and CIMB Bank, Korea Development Bank (KDB), and Japan: Mitsui Sumitomo Insurance Group, Tokio Marine and Sumitomo Mitsui Banking Corporation. A few domestic champions from other countries are also laying out their respective Asian expansion plans.

'With a shake up in the financial services landscape from the resurgence of these commercial banks given distractions in the West, we expect these newly minted regional players to gain strength and compete against international institutions with significant Asia-Pacific focus, such as HSBC and Standard Chartered Bank' says Matthew Phillips, Partner at PricewaterhouseCoopers (China). Japanese institutions in particular, emboldened by a strengthening currency and lack of growth catalysts at home, are once again looking for regional opportunities. There are some signs that Korean institutions may seek to do likewise. To a great extent, super-regionals have filled the vacuum left behind by other western financial services players who have, as a consequence of the global financial crisis, retreated from the region as they regroup resources back to their home bases.

- **Introduction of new regulatory master plans:** In the near term, there will be changes to the rules of competition in the industry, with several jurisdictions introducing new financial sector master plans. For instance, Thailand and Malaysia are publishing new master plans in 2010, just as Taiwan, Vietnam and India are introducing salient changes to regulations governing competition in the banking and insurance sectors within their markets. In general, these

master plans aim to lift the efficiency and competitiveness of the industry, typically by encouraging consolidation and opening up certain sectors to a greater number of new or foreign players. Regulators will issue new licences, allowing new entrants to compete in previously closed areas of financial services. They will also allow new types of institutions to compete in the marketplace, as well as giving greater freedom to institutions to expand their distribution networks.

- **The new post-crisis regime of capital and liquidity management:** The crisis has ushered in a new regime of risk management and regulatory compliance. Respondents indicated an inclination towards holding on to higher capital buffers, as the crisis reiterated to financial institutions across the region the importance of having sufficient liquidity. Meanwhile, although the structure and extent of regulatory changes are still evolving and precise changes have yet to be ironed out, financial institutions are already basing acquisitive decisions on upcoming regulatory mandates and best practices. For instance, Basel III – with its proposed changes to the composition of capital and risk coverage at banks, and which comes into effect at the end of 2012 – already has respondents indicating a preference for targets with high capital and liquidity positions, and such criteria will guide M&A decisions moving forward.
- **Focus beyond mere numbers and look at intangibles:** Learning from the crisis, financial institutions are placing higher premiums on long term and sustainable business propositions that extend beyond traditional financial metrics. Beyond the dollars and cents, financial institutions are placing increased emphasis on non-financial factors such as the geographic coverage and quality of customer bases; the target institution's entrenchment and branding within the marketplace; and availability of highly skilled human capital. These factors will influence M&A valuations as institutions seek to grow, not just by sheer size, but in real value.

Interest in M&A is expanding...

As regional financial institutions manoeuvred their way through the weakest market conditions since the Asian financial crisis of 1997-98, they made a conscious effort to go 'back to basics', focusing on their core businesses throughout 2009. Our survey revealed that this included greater attention to higher margin client segments, improvements in products and service offerings, and increasing the reach and distribution channel effectiveness in existing markets. 'Focus on what is core' appears to be the mantra adopted successfully by the financial services industry to weather the crisis.

However, the dawn of the economic recovery and the consequential strengthening of consumer and business confidence have allowed financial institutions to place higher emphasis on new sources of growth as opposed to just focusing on what is core. This is reflected in anticipated M&A activities, with 54% of respondents expecting to evaluate or undertake M&A transactions in 2010 as compared to 42% in

last year's survey. In tandem with this theme of growth, only 21% of respondents pointed to the likelihood of divesting business units in 2010, lower than the 25% recorded in the 2009 survey. They indicated that business units are, on the whole, performing up to par, and that the preference was to be buyers rather than sellers in 2010. This clear mismatch in supply and demand for financial services deals will put increased pressure on pricing.

Interest in M&A can be seen in light of a more intense battle for market share, especially as the crisis created further market share consolidation among top-tier players. 'Having high market share in one or two markets is not adequate for financial institutions having aspiration to be Asia's super-regionals. To truly compete regionally, the objective has to be having a critical mass in a number of markets, in particular the key markets in the region' states Nelson Lou, Partner at PricewaterhouseCoopers (China).

In many countries, Tier 1² financial institutions have become even larger, capturing a disproportionate share of business from their smaller peers. For the large players that we interviewed, M&A will solidify, once and for all, their dominance in the marketplace. Among the mid-sized Tier 2 players, growth through M&A would be the way to regain market share that was lost, even though they face growing challenges in funding required acquisitions. Tier 3 institutions will strive for success in local markets or in niche areas, even though many factors such as regulation, board directives and the search for economies of scale will continue to underscore that. Indeed, size is might in the region's financial services sector.

In 2010, several financial institutions will make maiden forays into new geographies across the region, with 56% of those who are looking to expand inorganically having ambitions to expand into new geographic regions. This includes domestic, in-country expansion for institutions in markets such as India and Indonesia that are geographically spread out and still have large or under-penetrated populations. It also refers to cross-border geographic expansions, which is an especially crucial motivating factor for foreign institutions that need to gain a foothold into new territories given the lack of avenues for organic growth on their home turf. Overall, we believe that countries that will see the highest number of new market entrants include China, India, Malaysia and Indonesia.

With the economic recovery well under way in the region, 36% of the financial institutions that are intending to make acquisitions have indicated that they are evaluating new avenues of growth such as the addition of new business and product lines. This might include expanding into new lines of business such as wealth management, investment banking and rural banking. Select multinational insurers are likewise moving across borders in Southeast Asia or North Asia, or expanding their scope of offerings within the life or general insurance market. This includes, for instance, insurers further exploring the online mode of product distribution, pursuing more aggressive bancassurance tie-ups, or expanding into product lines such as health or micro-insurance. These are leading to a reconfiguration of the product and services portfolio for players within the Asian financial services arena.

...But acquisitions cannot be done at any cost

Although respondents cited the need to attain critical size – with 91% of respondents agreeing that size is a core factor in providing their bank or insurer with a competitive edge – they understand that size cannot be attained at any cost.

While the adverse conditions of the past year may have presented opportunities to beef up assets at attractive valuations, as the crisis subsides, financial institutions are encountering fewer opportunities to acquire quality assets at competitive pricing. As 'value for money' deals get fewer and further between, institutions are not willing to compromise on due diligence. As such, respondents pointed to a few road blocks that could possibly derail M&A transactions. These include a lack of clarity in the true quality and robustness of targets' assets, mismatched pricing expectations between buyers and sellers given differing opinions on the extent and growth of the regional economies, and uncertain regulatory policies pertaining to sizeable M&A deals and equity ownership, amongst others.

Meanwhile, increasing market share concentration of top institutions will bring to the fore issues of collusion or unfair pricing power, and has not escaped the wary eyes of regulators. We expect anti-competition rules to be increasingly considered by regulators as more market share-concentrating M&As proceed across the region.

Post-merger focus areas

In general, history has proven that up to three in five M&As fail by not meeting projected synergy targets and post-merger objectives. Respondents were well aware of post-acquisition issues that warrant close attention. By far the most crucial threat to merger success cited by respondents is an under-emphasis on human capital issues. For instance, neglecting to communicate details and objectives of the merger clearly to the employees could create a high level of staff anxiety and disruptions in productivity. Meanwhile, a culture clash between the acquirer and acquired could result in repercussions such as talent exodus and, as a result, undermine shareholder and consumer confidence and mark down synergy projections.

Consequently, there is a need to integrate the people, processes and technology aspects of the two separate entities quickly such that there is minimal disruption to 'business as usual'. Time is of the essence, and this integration needs to be appropriately prioritised to unlock the most synergistic value. Matthew Phillips, Partner at PricewaterhouseCoopers (China), remarked that 'This is easier said than done. IT and people strategies on a standalone basis can often be very different from those required in an integration scenario. Those organisations who have given serious thought to these issues as part of their business strategy months, if not years, before a deal will be much better placed to make the integration happen quickly. This is a real competitive advantage.'

² Definition of financial services institutions by tier:

- Banks: asset sizes (Tier 1 > US\$100bn, Tier 2: US\$10–100bn, Tier 3 <US\$10bn);
- Insurers: net premiums written (Tier 1: >US\$2bn for life & annuity and >US\$1bn for property & casualty, Tier 2: US\$0.5-2bn for L&A and US\$0.5-1bn for P&C, Tier 3: <US\$0.5bn for both).

02

Introduction

A review of the FSI landscape over the past two years highlights how the global financial crisis has impacted financial services M&A activities across Asia-Pacific. A comparison of M&A transactions in 2009 finds that while selective deals were still being agreed, 2009 bore the brunt of the downturn.

The upheaval of the global economy came to the forefront of the business world when the effects of the sub-prime mortgage crisis in mid-2007 in the United States triggered the collapse of several large international hedge funds and the breakdown of inter-bank lending markets. These in turn resulted in the collapse of major financial institutions and exploded into a global credit crunch. By September 2008, the contagion effect was felt across Asia-Pacific, blanketing this region in a shroud of economic uncertainty (the worst since the Asian financial crisis of 1997-1998), and leaving the region with a real fear of 'what lies ahead'.

The FSI revenues actually rose for the vast majority of players, as institutions stalled their plans for M&A to focus on their core. These developments thus marked a decline in M&A activities, which witnessed the number of financial services deals disclosed in Asia-Pacific slowing by 12.0%

from 567 transactions in 2008 to 499 in 2009 as the region felt the full force of the financial malaise.³ The largest decline in deal value was seen in Australia, which saw a drop of 62.4% from US\$27.7 billion to US\$10.4 billion.³ (Note, however, that 2008 was a bumper year for M&A in Australia with Westpac's US\$17.94 billion³ acquisition of St. George Bank accounting for the relatively large cumulative deal value.) Likewise, in Hong Kong, the value of transactions fell from US\$7.8 billion to US\$3.9 billion in what was a relatively dry year for the M&A rainmakers.³ India meanwhile witnessed an 82.9% decline in values from US\$4.2 billion to just US\$718 million.³

However, there remained a sprinkling of activities, with a core M&A theme in 2009 being the sale of Asian-based assets by US and European financial services firms. For instance, Citigroup and Bank of America sold more than US\$7 billion of

their Asian bank holdings, while American International Group (AIG), Dutch bank ING and the UK's Royal Bank of Scotland (RBS) each individually announced the divestiture of circa US\$3 billion worth of operations from this region.⁴

So while 2009 did not see a flurry of acquisition activities, and deal sizes in no way rivalled those of 2008, selective transactions were still being agreed. For instance, while Australia did not see any massive deals, its top four banks did make smaller strategic acquisitions. Amongst them, ANZ has been most impressive in its attempt to be a true regional player. In August 2009, ANZ acquired the Asian banking business of RBS (comprising its retail, wealth management, commercial and institutional banking businesses in six countries) for US\$550 million.⁵

2009 also saw a succession of acquisitions by National Australia Bank (NAB), aiming to increase both its wealth management and mortgage businesses. These included the US\$697 million⁶ purchase of Aviva's Australian wealth management business, as well as an 80% stake in the private wealth management division of Goldman Sachs JBWere. NAB also acquired the mortgage business of Challenger

Financial Services for US\$318 million⁶ in August, and 17.5% of mortgage originator Homeloans Ltd (with the potential to increase the ownership to 41%).⁷ This follows in the footsteps of rival peers like Commonwealth Bank and Westpac, which had also completed purchases of mortgage businesses in 2007–2009, in addition to making banking acquisitions.

In Singapore, OCBC Bank, the smallest of Singapore's local banks by asset size, also proved willing to jump at good acquisition opportunities. It surprised the industry by acquiring ING Asia Private Banking for US\$1.46 billion in October 2009,⁸ in the process ramping up its assets under management and building its prominence in the wealth management market across the region and into Europe and the Middle East.

Other key agreements inked in 2009 included those in Taiwan, where total financial services M&A activity actually rose. The total aggregated value of M&A deals in the former almost doubled from US\$15.3 billion in 2008 to US\$30.6 billion in 2009, while that in Taiwan rose 113% to US\$6.0 billion.⁶ The largest deal in Japan was that of Sumitomo

Table 1: Summary of 2009 financial services M&A transactions by deal value

| Target country | Number of total deals | Number of disclosed deals | Banking | Securities & capital markets | Mutual funds & asset management | Insurance | Others | Value (US\$m) |
|----------------|-----------------------|---------------------------|---------------|------------------------------|---------------------------------|---------------|--------------|---------------|
| Japan | 197 | 116 | 14,488 | 794 | 1,274 | 8,449 | 5,604 | 30,609 |
| Australia | 125 | 57 | 111 | 247 | 492 | 9,148 | 425 | 10,423 |
| Mainland China | 63 | 40 | 5,754 | 220 | 818 | 310 | 205 | 7,308 |
| Taiwan | 32 | 24 | 788 | 1,153 | 412 | 2,993 | 660 | 6,005 |
| Hong Kong | 46 | 36 | 2,657 | 182 | 587 | 237 | 204 | 3,868 |
| Kazakhstan | 16 | 2 | 2,390 | - | - | - | - | 2,390 |
| South Korea | 52 | 47 | 383 | 531 | 44 | 1,063 | 25 | 2,046 |
| Singapore | 18 | 12 | 1,703 | 10 | 148 | 68 | 27 | 1,956 |
| Malaysia | 20 | 10 | 1,610 | 6 | 9 | 180 | - | 1,805 |
| Thailand | 36 | 24 | 1,017 | 118 | 4 | 218 | 62 | 1,419 |
| Indonesia | 53 | 18 | 490 | 159 | 148 | 29 | 9 | 835 |
| India | 126 | 67 | 5 | 151 | 395 | 142 | 24 | 718 |
| New Zealand | 20 | 7 | - | 16 | 262 | - | - | 278 |
| Vietnam | 44 | 8 | 78 | 27 | - | 105 | - | 211 |
| Philippines | 18 | 7 | 112 | - | - | - | 12 | 123 |
| Pakistan | 16 | 3 | 46 | - | - | - | - | 46 |
| Others* | 33 | 21 | 46 | 2 | 8 | 9 | 216 | 279 |
| Total | 915 | 499 | 31,678 | 3,617 | 4,601 | 22,952 | 7,473 | 70,321 |

Note: *Others comprises: UAE, Macau, Armenia, Sri Lanka, Cambodia, Mongolia and Brunei.

Note that at the time of going to press, this table is based on deals announced rather than closed. For instance, the values for Australia include the pending acquisition of AXA Asia Pacific Holdings Ltd by NAB for US\$5.46 billion, announced on 17.12.09.

Source: Thomson Reuters, May 2010.

4 Source: 'Asia-Pac M&A activity up, US firms sell Asian assets', The Business Times, 06.01.10 (Business Times quoting mergermarket, www.mergermarket.com).

5 Source: 'ANZ buys RBS Asia businesses for \$A687m', Sydney Morning Herald, www.news.smh.com.au, 04.09.09.

6 Source: Thomson Reuters deal data.

7 Source: 'NAB to acquire Challenger's mortgage management business', Australian Stock Exchange Announcement, www.asx.com.au, 18.08.09.

8 Source: 'ING to sell Asian Private Banking business to OCBC', ING press release, www.ing.com, 15.10.09.

Table 2: Actual and forecasted growth in GDP, 2008–2011

| Region | 2008A YoY GDP Growth | 2009A YoY GDP Growth | 2010F YoY GDP Growth | 2011F YoY GDP Growth |
|-----------------|----------------------|----------------------|----------------------|----------------------|
| Central Asia | 6.1% | 2.7% | 4.7% | 5.9% |
| East Asia | 7.3% | 5.9% | 8.3% | 7.7% |
| South Asia | 6.4% | 6.5% | 7.4% | 8.0% |
| Southeast Asia | 4.3% | 1.2% | 5.1% | 5.3% |
| The Pacific | 5.4% | 2.3% | 3.7% | 5.0% |
| Asia (ex-Japan) | 6.6% | 5.2% | 7.5% | 7.3% |

Source: Asian Development Outlook 2010, April 2010.

Mitsui Banking Corporation's acquisition of securities brokerage firm Nikko Cordial Securities for US\$5.8 billion, followed by the US\$4.4 billion purchase of non-life insurer Nipponkoa Insurance by Sompo Japan Insurance, both announced in the first quarter of 2009.⁹ In Taiwan, core deals included that of Primus Nan-Shan Holdings' US\$2.15 billion acquisition of Nan-Shan Life and KGI Securities' US\$0.9 billion acquisition of Taishin Securities.⁹

In 2010, Asian economies are seeing clear signs of recovery, as trade flows, ever important for the region's emerging economies, regain strength. Domestic demand has also picked up considerably on the back of government stimulus plans, improved employment levels, better income prospects and an overall revival of market sentiment.

Singapore, for instance, announced a 32% growth of its trade-dominated economy in the first quarter of 2010 on a seasonally adjusted annual basis.¹⁰ Most recently, a Monetary Authority of Singapore (MAS) poll revealed that economists are expecting the Singapore economy to expand by a stellar 9%¹¹ this year, boosted by an unexpectedly strong boom in manufacturing and exports. Strong economic data in recent months indicate that India's recovery is likewise well underway, with impressive performance in the first quarter of 2010 and the government confident that the economy will grow by 8–8.5% in fiscal year 2010/11 (April–March).¹² This positive news came hot on the heels of an improving job situation in South Korea following strong performances in manufacturing and trade, and mainland China reporting an 11.9% YoY growth in its first-quarter GDP,¹³ even as long-struggling Japan begins showing signs of life with brisk trade and retail sales.

Consequently, the Asian Development Bank's (ADB's) annual flagship economic publication, Asian Development Outlook 2010, is projecting a robust growth of 7.5% in 2010 for Asia (excluding Japan), well up from 5.2% in 2009,¹⁴ supported by a modest recovery in global trade and the ongoing effects of fiscal and monetary stimulus.

So, while our last year's M&A report ('A new playing field – Report and survey results: The outlook for FS M&A in Asia', June 2009) had several interviewees referring to the M&A market as one in a 'state of paralysis', this is now no longer the case.

With Asia's recovery having taken a firm hold, and a return to stronger and sustainable growth now in sight, the mood has decidedly changed for the better – the storm clouds are giving way to clearer skies.

The economic shakeout in 2008–2009 actually presented a powerful opportunity for financially stable institutions to scout for accretive opportunities, utilising the economic downturn to strategically position themselves for the upturn.

9 Source: Thomson Reuters deal data.

10 Source: 'Singapore's GDP soars 32 percent in first quarter', BusinessWeek, www.businessweek.com, 14.04.10.

11 Source: 'Growth forecast up to 9%', The Straits Times, 10.06.10

12 Source: 'Indian economy to grow by 8.5 pc in 2010-11' The Economic Times, www.economicstimes.indiatimes.com, 16.05.10.

13 Source: 'China's quarterly GDP expands more-than-expected 11.9%', The Wall Street Journal, www.marketwatch.com, 15.04.10.

14 Source: 'Highlights – ADO 2010', Asian Development Bank, www.adb.org, 13.04.10.

03

Action items for financial institutions

This section explores how financial institutions that have emerged relatively unscathed from the economic turmoil and have pragmatically scouted for investment opportunities can focus on post-deal integration to strengthen their value proposition and financial standing within the industry.

As the storm clouds make way for clearer skies, M&A is coming back into favour. In addition to the perennial need to comprehensively evaluate their target and to price in and capture all potential synergies, financial institutions would do well to incorporate these other essential elements as they undertake their acquisitive forays:

- **Act swiftly to capture remaining opportunities at favourable pricing, but heed any red flags.** We mentioned earlier that attractive acquisition targets are increasingly scarce, though 81% of the executives surveyed expect M&A activities to ramp up in 2010 and indicated that size was core to success. Consequently they are assessing possible acquisition targets, and with demand exceeding supply, opportunities to purchase at a competitive pricing are becoming limited. We expect parties looking for acquisitive growth to act quickly over the next few months to ink deals.
- **Place utmost emphasis on the ubiquitous cultural resistance issue.** Respondents to our survey, in both mature and emerging markets, were unanimous in voting 'cultural resistance/mismatch' as a core challenge for acquirers – this could stem from either cross-border cultural diversity for organisations expanding geographically, or differing corporate cultures between institutions. A collision of divergent cultures serves only to disengage staff, disrupt operations and shake customer confidence.

However, due diligence continues to reveal adverse information, and in closing the deal, these risks are often not appropriately priced. In the process, businesses need to be extremely aware of the impact uncertain global capital market conditions could have on cost of capital (if debt is required to furnish the acquisition), and the impact the deal would have on capital levels of the merged entity.

Cultural issues need upfront attention, even before the deal papers are signed, and players that are most successful in tailoring change management programmes are those that weigh and assess the potential impact of the human capital

and cultural aspects right from the start during the negotiation phases. They also actively incorporate positive elements of each company's culture during the structural organisational design and integration stage.

- **Enhance the probability of success by designing a thorough M&A strategy upfront.** Institutions that pause momentarily to develop an M&A strategy are generally better equipped to execute a deal with maximum speed and effectiveness thereafter. 'Worryingly, due diligence in Asia is increasingly being seen as a necessary evil rather than a tool to critically analyse the deal's ability to deliver against a pre-determined set of criteria. Deal and integration risks that arise in due diligence are often played down or ineffectively addressed through mitigating steps only for the same issues to resurge later. Institutions can combat this tendency by clearly setting out the strategic rationale and requirements before diligence begins. This includes clear expectations as to how and when integration will be carried out and the team that will be responsible. If a deal fails to meet these expectations, then buyers should walk away,' commented Matthew Phillips, Partner at PricewaterhouseCoopers (China).

Meanwhile, a 'clean team' might be formed, working under strict confidentiality to create a road map for consolidated strategic, structural, operational, technology, marketing and branding efforts to be launched immediately after the deal is sealed. Creation of such teams would better enable the capturing of full synergies because they understand their objectives as well as the potential deal-breakers, and are able to structure plans allowing the integrated entity to take on the marketplace soon after. They would also be better equipped to deal with local nuances and regulations in the target territory and manage early expectations of board members, especially of those based in foreign headquarters, who may not appreciate the local market conditions.

- **Remember to treat the merge as a holistic process all the way to the end.** Many organisations make the mistake of treating their pre- and post-deal processes as discrete activities, perhaps tapping on the expertise of totally different teams before and after the acquisition. This often comes about in the politics of selecting who will take on the management and integration roles after the deal. In some cases, this results in a lack of clarity, and in effect the acquirer hands over the control to incumbent management who have little appreciation of or buy-in to the original strategic intent. It creates a lack of continuity, consistency and accountability, and a disconnect between the valuation projected during due diligence and the numbers finally achieved post-merger.

Instead, deals are most successful when the acquisitions are treated as a continuous lifecycle, with the same core team involved in the pre-merger strategy planning, progressing with the deal execution, and – after the deal announcement and accompanying fanfare dies down – continuing with the post-merger integration to ensure that projected benefits are realised within a reasonable time frame. Ideally, there should be overlaps in the teams responsible for pre-acquisition valuation and post-acquisition synergy capture, as they would have the clearest

comprehension of how to achieve the integration projections. Integration specialists might also be brought in during the due diligence phase to reduce the risk of surprises in terms of integration costs or timetables.

- **Organise integration workflow according to the level of synergistic value.** Many interviewees spoke of the need to ensure swift integration of the acquirer and acquired institutions. Organisations need to commence integration beginning with high value activities and postpone lesser value ones. For instance, if an acquiring bank or insurer had touted the cross-selling opportunities to the enlarged customer base as a key driver of the consolidation, it then needs to enable the rapid transfer of customer information, and develop integrated customer account plans and break down silos within the two organisations.

Companies that organise their integration activities on a functional basis (for example, on a process or procedures basis, such as consolidating databases, rationalising technology applications and product offerings) need to consider the fact that not all such consolidation activities generate equal benefits and should thus not have equal priority. All eyes are on the ability of the enlarged entity to deliver on the value promised, and with time being of the essence, the various functions and business processes need to be consolidated with their value-creation contribution in mind.

- **Align the business and information technology functionalities to execute an effective post-merger integration.** Many ingredients need to come together to support the creation of strategies and road maps for integration, and no less important is the need to integrate information technology. In fact, 64% of respondents pointed out 'technology integration issues' as a post-integration challenge.

IT outcomes are often quantifiable, measured by established 'hard' key performance indices, with industry estimates that financial institutions expect ongoing IT savings to the tune of 20–30% of the pre-merger IT expenditure. However, for these targets to be met, expertise would be required to achieve effective application integration, application build-and-enhancement, application decommissioning, data migration, data archival and IT governance.

'To translate business goals into IT organisational priorities, the IT integration office needs to guide the enlarged entities toward the new technology model, and oversee the balance between operations delivery, information technology integration and cost savings. This calls for a clear view of the capital investment requirements, prioritisation of all discretionary technology initiatives and investments, consolidation of shared services functions and elimination of excess capacity, and possibly the implementation of interim applications, interfaces and gateways before transitioning to the final architecture,' says Ben de Haldevang, Director at PricewaterhouseCoopers (Singapore).



The 'new' post-crisis landscape: New players, rules and opportunities

We underscore the many changes – both positive and otherwise – that institutions across the region have seen as a consequence of the recent financial upheaval. There are external factors at play, such as the introduction of new financial sector master plans and rules governing competition by the regulators. There are also significant shifts in financial institutions' priorities, such as greater regard, or the articulation of aggressive regional expansion plans. All these point to how the crisis has transformed the industry.

Despite all references to an industry reverting to the pre-crisis days and recovering from the global contagion, it is becoming clear that the financial services industry is itself much changed and is operating in a much-transformed marketplace. In many ways, the industry will not return to pre-crisis conditions. There are notable changes as to who competes in the market.

IDC Financial Insights predicts that the number of financial institutions worldwide will decline in the aftermath of the crisis (for example, IDC Financial Insights estimates that the number of banks worldwide fell by 5% in 2009, projecting further that global numbers will continue to shrink by another 4% by the end of 2010). However, it believes that the Asia- Pacific region is set to have more, and not fewer, financial institutions. The region's financial services market remains largely under-served, and the industry expects to see more new players coming into the marketplace to take advantage of the upside.

New market entry strategies will be seen, for example, from the likes of consumer finance companies applying for banking licences, or of banks extending themselves into new lines of business, such as wealth management or insurance. New non-bank players will also gain in prominence as domestic conglomerates make their first forays into financial services via the acquisition of small banks, with a view to expanding these organically in the long term. For instance, this is a strong trend in South Korea.

There will also be financial institutions – both Asian-based domestic and international brand names – making their inaugural forays into new geographies. The markets that will see the highest number of new market entrants, as indicated by respondents to our survey, include mainland China, India, Malaysia and Indonesia.

A review of the list of players to watch in 2010 also points to certain institutions no longer in the market compared to pre-crisis years, as some US and European-headquartered groups scaled down their operations in Asia to concentrate on core home markets. The crisis has seen large global institutions divesting shareholdings after lock-up periods (this trend is especially apparent in mainland China), or even exiting certain segments in Asia altogether. Most notable among these are RBS' sale of its Asian banking business,¹⁵ Citigroup's sale of Nikko Cordial (to Sumitomo Mitsui Financial Group),¹⁶ and ING Group's divestment of its Asian private banking assets (acquired by Singapore's OCBC Bank).¹⁷ Herein, an executive from an acquiring company acknowledged that one positive outcome of the crisis was that it brought significant targets on to the market that would not otherwise be up for sale.

As international players exited, Asia-Pacific-based institutions stepped up to fill in the vacuum. They have become more ambitious and are aggressively undertaking acquisitions to support 'super-regional strategies'.

This was a term coined by ANZ Bank to describe its aspirations beyond Australia and New Zealand, but is now commonly used in reference to attempts by Asian institutions to acquire and manage regional units that are close in proximity to their headquarters or clustered within one part of the region and which exploit regional trade flows or other cross-market synergies.

Interestingly, the emergence of these regional powerhouses transpired in a short period of time, underscoring how home-grown institutions are furiously building significant region-wide platforms to seize opportunities in the broader Asia-Pacific market. As the dust of the crisis settles, we see these institutions gaining strength to compete against massive players such as HSBC and Standard Chartered Bank, which are global institutions with significant Asian focus. Table 3 (on page 12) presents a list of these super-regionals and their most recent M&A and consolidation activities.

¹⁵ Source: 'ANZ buys RBS Asia businesses for \$A687m', Sydney Morning Herald, www.news.smh.com.au, 04.09.09.

¹⁶ Source: 'Citi to Sell Nikko Cordial Securities to Sumitomo Mitsui Banking Corporation and to Forge Alliance with Sumitomo Mitsui Financial Group', Citigroup Inc. press release, www.citigroup.com, 01.05.09.

¹⁷ Source: 'ING to sell Asian Private Banking business to OCBC', ING press release, www.ing.com, 15.10.09.

Table 3: Top Asian Super-Regionals and recent regional activities

| Bank | Home market | Asia-Pacific regional presence |
|--|------------------|--|
| Australia and New Zealand Banking Group Limited (ANZ) | Australia | <p>ANZ has built an impressive Asia-Pacific platform with stakes in, among others, ANZ Panin in Indonesia (85%), AmBank in Malaysia (19%), ANZ Royal Bank in Cambodia (55%), and Tianjin City Commercial Bank (20%) and Shanghai Rural Commercial Bank in mainland China (19.9%). Furthermore, ANZ owns ANZ New Zealand and the National Bank of New Zealand on a combined basis, which makes ANZ the largest bank in New Zealand and the South Pacific.</p> <p>In August 2009, ANZ acquired parts of the Asian banking business of Royal Bank of Scotland (RBS). The acquisition included RBS' retail, wealth, and commercial businesses in Taiwan, Singapore, Indonesia and Hong Kong, and the institutional businesses in Taiwan, the Philippines and Vietnam. In September 2009, the bank opened the Chongqing Liangping ANZ Rural Bank, making ANZ the first Australian bank, and one of the first international banks, to enter mainland China's rural market.</p> |
| OCBC Bank | Singapore | <p>In 2009, OCBC acquired ING Asia Private Banking, in the process ramping up its assets under management and building its prominence in the wealth management space, not only in the region but also in Europe and the Middle East. The ING Asia Private Banking acquisition will build on its already considerable platform that includes a subsidiary in mainland China, Malaysia and Indonesia (Bank OCBC NISP). It also has stakes in Ningbo Bank in mainland China (14%) and VP Bank in Vietnam (15%). OCBC also has an Islamic banking subsidiary, OCBC Al Amin.</p> |
| DBS Bank | Singapore | <p>DBS's major overseas operations are in Hong Kong (primarily through the former Dao Heng Bank, acquired in 2001) and Taiwan (through Bowa Bank, acquired in 2008). DBS also has subsidiaries in mainland China (where it was the first Singaporean bank to locally incorporate), India (where it has a small corporate and personal banking network) and Indonesia. It also owns the Singapore-based Islamic Bank of Asia.</p> <p>In Malaysia, DBS has a licensed offshore bank in Malaysia called the DBS Labuan Branch. DBS recently sold a 37% stake in Cholamandalam DBS Finance in India, articulating that it will focus on its banking licence in the country.</p> |
| Malayan Banking (Maybank) | Malaysia | <p>Expanding from its significant business in Singapore where it has qualifying full bank (QFB) status, Maybank acquired stakes in Bank Internasional Indonesia (97%), MCB Bank in Pakistan (20%) and An Binh Commercial Joint Stock Bank in Vietnam (15%). Maybank has a small network of branches in Cambodia, Brunei and its subsidiary in the Philippines. In mainland China, it has one branch and one representative office. Maybank Islamic Banking, a subsidiary, is a major player in the bank's home market.</p> |
| CIMB Group | Malaysia | <p>CIMB Group owns CIMB Niaga in Indonesia and CIMB Thai (the former BankThai). It also has a growing business in Singapore. In 2009, CIMB acquired a 20% stake in Bank of Yingkou in mainland China. We expect forays by CIMB into the Philippines, Vietnam and Cambodia in the medium term.</p> |
| Commonwealth Bank of Australia (CBA) | Australia | <p>CBA has banking investments in Qilu Commercial Bank (20%), Jinan City Commercial Bank (11%) and Bank of Hangzhou (20%) in mainland China, Commonwealth Bank Indonesia (100%), and ASB Bank in New Zealand (100%). In March 2010, CBA announced an acquisition of a 15% stake in Vietnam International Bank (VIB). It also has life insurance operations in New Zealand (Sovereign), Indonesia (Commonwealth Life) and a joint venture in mainland China (BoCommLife).</p> |
| United Overseas Bank (UOB) | Singapore | <p>UOB has subsidiaries in mainland China, Malaysia, Thailand and Indonesia (through the recently merged UOB Indonesia and Bank UOB Buana). It has a 15% stake in Vietnam's Southern Commercial Bank. It also has a 15% stake in Evergrowing Bank in Shandong, mainland China.</p> |
| Mitsui Sumitomo Insurance Group (MSIG) | Japan | <p>MSIG accounted for one of the largest M&A deals in Japan in 2009 when it paid US\$3.9bn for Aioi Insurance in January that year.</p> <p>MSIG has since made a US\$65 million investment in Shanghai-based China Pacific Insurance (the third largest Chinese life insurer and second biggest casualty insurer) in December 2009 to become the third largest foreign non-life insurer in mainland China. This was followed by an equity stake of 7% in Sinatay Life Insurance of mainland China for US\$26 million in April 2010. MSIG had also earlier ventured into other parts of the world – for instance, it acquired a licence from the Qatar Financial Centre in December 2008.</p> |
| Tokio Marine Holdings | Japan | <p>Japan's second largest non-life insurer made a US\$4.7 billion acquisition of US non-life insurer Philadelphia Consolidated Holding in 2008, and continues to step up on its overseas expansion plans. Focus is not only on the developed nations (such as the US) but is also on Asia (and specifically the Indian) and Latin American emerging markets that are expected to expand exponentially in the future. The group specifically mentioned that large-scale M&As abroad was crucial to its growth and by 2011, overseas insurance business is expected to account for 27% of its total business. It also has plans to expand into Islamic insurance operations.</p> |
| Sumitomo Mitsui Banking Corporation (SMBC) | Japan | <p>While financial holding company Sumitomo Financial Group is consolidating its various subsidiaries and recent acquisitions (particularly its recent acquisition of Nikko Cordial from Citigroup), its banking unit, SMBC, continues to expand its cash and trade services through partnerships across the region. The primary intention is to serve Japanese corporates in their regionalisation strategies, but the bank is starting to articulate its plans for an international retail strategy. SMBC has created a cash and trade partnership with major banks in mainland China, Indonesia, Vietnam and Hong Kong. SMBC has already received approval from the China Banking Regulatory Commission for the establishment of a branch in the city of Shenyang, Liaoning Province, in mainland China.</p> |

Source: IDC Financial insights, May 2010.

New rules of competition

In the near term, the industry will also see an evolution in the competition rules, with several jurisdictions introducing new financial sector master plans. For instance, Thailand and Malaysia are introducing new master plans in 2010, just as Taiwan, Vietnam and India are launching key changes to regulations governing competition in the banking and insurance sectors within their markets.

In general, these master plans aim to improve the efficiency and competitiveness of the industry, typically by encouraging consolidation and opening up of certain encouraged sectors to a greater number of new or foreign players. Significant stipulations included in the master plans are as follows:

- The Thai Financial Sector Master Plan Phase II, to be implemented between 2010 and 2014, is expected to encourage more types of competitors, expand the scope of business for some players, and ease the burden of regulatory compliance. The master plan implicitly states its preference for locally incorporated commercial banks. After the success of the first master plan in bringing to market new players such as GE Retail Bank, TISCO Bank and LH Bank, this next instalment encourages further M&As, using tax measures and improved efficiencies in the M&A regulatory approval process.
- The new master plan for Malaysia prepares for, among others, the entry of up to nine new players to compete in traditional and Islamic-based commercial banking. At the same time, Bank Negara Malaysia (the Malaysian central bank) will push for the next phase of banking consolidation in Malaysia¹⁸ to strengthen financial positions and equip banks with sufficient capital under the upcoming Basel III framework that comes into play globally at the end of 2012.
- The banking industry road maps throughout most of the region will allow commercial banks to enter new business areas such as wealth management, trust, custody, venture capital and private equity management, and micro-finance. In the process, some financial institutions will be encouraged to consolidate subsidiaries and associate units, in order to improve supervision and risk management as well as to attain operational synergies.

- While there remain some exceptions (for instance, an executive from a bank in Hong Kong mentioned that an inhibitor to organic growth stems from 'regulatory positions that preclude our organic growth in select countries by restricting the numbers and locations of foreign bank-owned branch network'), regulators across the region will, by and large, allow for greater freedom in opening branches and distribution channels for both banks and insurers.

However, new licences will be subject to stringent business rules, risk management guidelines and capitalisation thresholds, raising questions as to whether some organisations are prepared to meet the constraints that may be imposed.

Greater emphasis on real assets

The global financial crisis has reinforced the need for businesses to be built on long-term sustainable propositions. One executive in South Korea observed that 'the pre-crisis environment encouraged leverage to be greatly used to drive revenue growth'. Eventually, of course, this proved to be the industry's undoing. Learning from past mistakes, the financial institution of today is going 'back to the basics', focusing on strong balance sheets of loans and deposits, rather than being overly dependent on financial leverage or gearing.

¹⁸ 'Malaysia liberalises financial sector' Malaysian Investment Development Authority announcement, www.mida.gov.my, 08, 29.04.09.

This pursuit of real growth is evident in institutions' attempts to acquire new customers and expand product portfolios – and in several cases, venture into new geographies in the pursuit of both. For banks, great premium is placed on the size of the customer base, especially in deposits. They believe that extensive customer bases give an edge over competitors by providing an ever-precious source of low-cost funding. Echoing this, a banker mentioned that

'the name of the game is to strengthen net interest margins by reducing the cost of funding and credit'

An executive from a top-tier bank in Indonesia points out that larger domestic banks in the market have successfully positioned themselves to capture customer deposits that have shifted from shakier, smaller banks towards bigger institutions that are deemed more financially sound and thus, have engendered customer trust. The growth of his bank's customer bases provides opportunities for further deepening relationships through product cross- and up-sell. Consequently, this keener focus on the customer has influenced his particular bank in its initiatives to integrate and optimise distribution channel capabilities that support its retail business.

Meanwhile, it can also be seen that the post-crisis institution is placing importance on understanding customer behaviour (whether it pertains to product preferences, customer habits or demographic segmentation), and crafting products and services to better suit these requirements. The assumption is that a customer of today is much more discerning and demanding compared to a customer of the pre-crisis days. This need for greater regard for customers as an institution's asset is seen in the insurance business as well, with a key regional player stating that 'as a result of the crisis, our management team has been observing peers within and out of the industry on how they adapt to customers' requirements and expectations. Consequently, we are now better at understanding and reacting to the varied customer demands.' Furthermore, together with this expansion of customer bases comes the enlargement of the breadth of product portfolios to enhance cross-sell opportunities and capture a larger share of the customers' wallets, smooth out income streams and drive up recurring revenues.

The new era of risk management and compliance

Despite the Asian FSI emerging relatively intact following the financial upheaval, the crisis was a realistic demonstration of how failures of risk management can wreak havoc on an entire industry and have far-reaching and drastic impact on all players. As such, our survey highlights a greater focus on risk management and compliance amongst the respondents.

The industry expects regulatory compliance to become more onerous as regulators come up with an expanded list of requirements to fill in gaps exposed during the crisis, and to adopt best practices observed during the course of recovery. In banking, for instance, the Basel Committee on Banking Supervision has issued a comprehensive reform package to address the lessons of the crisis, including proposals on strengthening global capital and liquidity regulations and the resolution of systemically significant cross-border banks. The committee is proposing changes to both the composition of capital and the risk coverage of the capital framework, as well as the introduction of a leverage ratio and measures to promote the build up of capital buffers. The stated intention is to promote a more resilient banking sector, to improve the banking sector's ability to absorb shocks, to improve risk management, and to strengthen bank transparency and disclosure.

'As with the previous tightening of capital requirements in Basel II, the proposed changes will increase the pressure for consolidation in many Asian markets, although we are unlikely to see this resulting in a flurry of deals in the short term'

commented Matthew Phillips, Partner at PricewaterhouseCoopers (China).

Basel III represents significant compliance and monitoring costs for all banks concerned and a few executives in the survey mentioned that this impending Accord, while serving a positive purpose, would also imply ‘an increased (possibly too onerous) capital requirement, lower lending limit, and perhaps restrict the offering of certain type of financial products.’ Similarly, Chris Lewis, Partner at PricewaterhouseCoopers (Australia), noted that

‘Over the last 18 months we have been seeing financial institutions using pricing, liquidity and security demands to ration the growth of credit while they increase their liquidity and revise their capital structures...’

These changes are leading to less gearing of the sector and thus reducing the availability of credit. At the same time those same changes in the dynamics of credit markets have substantially reduced the capacity of non-bank financial institutions to fill the credit gap.’

At present, the precise extent of this regulatory change remains highly uncertain, though even now, several institutions are already making M&A decisions with Basel III at the back of their minds. For instance, a respondent in Hong Kong mentioned that ‘any future acquisition that we consider would have to take the impact of Basel III into account (on both our, and the target's capital and liquidity positions).

...‘for instance, Basel III would have requirements on the liquidity of banks, and if the core retail deposit of a target company is too low compared to regulatory requirements, we might consider abandoning plans to acquire it’

This raises an interesting question as to whether those institutions that are particularly reliant on wholesale funding might be encouraged to use M&A to increase their deposit base in their existing markets. Clearly, with the recovery comes greater focus on liquidity and capital preservation. Certainly, financial institutions are now more conscious of the risk of illiquidity and having too much money tied up in any one area. As such, liquidity and capital considerations feature heavily as financial institutions assess M&A and regionalisation opportunities moving forward. One super-regional player interviewed remarked, ‘the greater focus on liquidity means that the threshold that an interested party needs to cross before it decides to acquire has been raised. The company not only has to do more capital-raising to cover the purchase itself, but also has to take into account adequate provisions for risk management. The bank of today likes to hold more capital – hence acquisitions, which are in essence capital-depleting, have to be thoroughly assessed to determine that synergistic benefits way outweigh the costs and risks.’



Opportunities for growth: Moving beyond focus on the core

As markets gain greater clarity over expectations of the future, this section focuses on their growth trajectory, their ‘back to basics’ approach, and on how, despite greater circumspection, most of them are more open to acquisitions now than in the recent past.

Our earlier comment that the global financial crisis did not have deep repercussions on Asia's financial services sector is highlighted by the finding that only 16% of respondents report declines in revenues in 2009. In turn, 54% even report higher revenues YoY. Furthermore, looking back to what was supposed to be a turbulent year in 2009, a good number of respondents revealed impressive performance, with a few of them even chalking up record-setting revenue and profits. In these instances, references to a comeback or a revival are obviously not applicable.

The region's institutions attribute their strong performance to the focus on core operations, deliberate mining of existing high-yielding client segments, improvements in products and services offerings, and increased reach into existing markets.

While a timely expansion to tap into new sources of growth (such as the addition of new business lines, or entry into new markets) was also a contributing factor, it was evident that the ‘focus on the core’ was the thesis used to weather the financial crisis successfully.

As such, those institutions surveyed that saw a fall in revenues in 2009, attribute the declines to their inability to see growth in their core business (especially for investment banking and advisory services. These saw a dearth of market activity, resulting in the fall in fee income), and problems in their existing assets, either through higher delinquencies in their loan portfolios or through churn in their customer bases.

Sources of growth

The emergence of clear signs of revival in the global financial services industry gives the Asian region's institutions yet more confidence. Virtually all financial institutions expect medium to high growth in 2010, with around seven in ten institutions projecting that their business would expand by more than 10% over the next 12 months. Encouragingly, only 6 of 122 respondents expected low growth of between 0–5%, while none from our sample anticipated revenue declines.

So, as these organisations prepare to take advantage of the more positive economic climate, we queried the executives on whether the 'focus on the core' thesis still holds, or if they will divert attention towards new sources of growth. Indications point towards the former, but with the onset of recovery, institutions are also expanding their scope of coverage and exploring the latter.

In banking, for instance, IDC Financial Insights projects that five markets – Indonesia, Thailand, Malaysia, Taiwan and South Korea – will see the highest jumps in lending in 2010. The more aggressive lending plans of banks in these markets will show how the credit freeze that characterised the global financial crisis has to all intents and purposes thawed out in this part of the world. We note that whilst lending was buoyed during the depths of the crisis by government stimulus measures (IDC Financial Insights estimates the total price tag to be US\$3.1 trillion in Asia, most of which was accessed through traditional banking channels), these programmes will be wound down in 2010. Looking ahead, the industry will therefore have to look beyond stimulus programmes and take on lending activities in the broader market.

The deposits and lending business will both see further upward momentum in 2010. Risk-averse customers will continue to be wary of structured, complex investments and will thus maintain funds in low-risk, interest-bearing accounts. Banks are therefore expected to further scale up their deposit-type offerings accordingly. Over the course of the crisis, the industry saw customers moving towards larger or state-backed banks, on the assumption that these were more stable. As such, we noted significant deposit market share shifts to the benefit of Tier 1 or government-linked banks in Australia, India, the Philippines and Malaysia. In these same markets, there will be a discernable battle for these Tier 1 players to retain these deposit customers.

Likewise, similar growth stories resonate within other financial services business areas such as private banking, wealth management and transaction banking, and other niche plays such as Islamic banking and micro-finance. The reenergised economic environment presents much upside, encouraging financial institutions to aggressively take first-mover advantage in the still-nascent areas of financial services.

Over in the insurance sector, performance likewise remains commendable, with pockets of growth even in Asia-Pacific's more mature economies. Fundamentals in these economies remained healthy through the crisis, supported by factors like high GDP per capita, rapidly ageing populations, and increasing need to provide for retirement.

Elsewhere growth for emerging insurance markets proved even more resilient, given still-nascent insurance penetration rates, economic development supported by domestic consumption, public sector investments, and improved household incomes and living standards.

Other sources of growth include evolving consumer demographics and greater awareness of the need for insurance coverage, deregulation and liberalisation that create new markets and opportunities for foreign insurers, and affordable and more efficient modes of distribution channel management that increase the number of touch points and make it easier to purchase policies.

Impediments to growth

Nonetheless, the industry is mindful of several impediments to post-crisis growth, of which the most frequently cited in our survey were the lack of personnel with appropriate skills, government regulation, and inability of IT technology platforms to support burgeoning operations.

The lack of skilled staff was the principal inhibitor of growth for most of the organisations interviewed. The problem does not necessarily come from how drastically employee numbers were cut during the crisis, there were only a few passing references to how the crisis forced institutions to cut staff, but on how new players in the market and incumbent players that are becoming more aggressive are fighting for crucial, but scarce, skills. One government-owned bank in India talked of massive hiring just to catch up with the growth opportunities in the market. The bank's executive director remarked, 'hiring talent with the right skills is one of the key challenges we are facing. It does not help that we also have a number of senior employees due for retirement in coming years.' This difficulty in catching up is also seen even in a

mature market like Japan, where one executive stated that his firm has been 'busy employing people, but we have a lot more work to do on the recruitment front'. As such, the industry realises that the pursuit of organic growth will become increasingly difficult and expensive as this would entail competition for scarce resources, the foremost being skilled employees.

There will also be more costs associated with incremental customer acquisition (particularly marketing and promotion, and cuts in margins for commodity-like financial products). They also cited a more restrictive regulatory environment as a factor that is arresting their growth momentum post-crisis. One executive from a global player making significant forays in the region commented that

'regulators are putting more constraints in how we are going to grow our business and what risks we can take'

This is echoed by other executives, particularly in markets like mainland China and India, where new government regulations and policies have implications on what core and adjacent businesses financial players can compete in, and on what level of business growth institutions should keep to. Furthermore, the lack of clarity of what government policies are short term versus long term makes it difficult for organisations to plan their growth road maps.

The other issue that respondents believe is hampering expansion stems from the fact that amidst tightened technology budgets over the past two years, their organisations are now unable to respond to growth opportunities effectively. A shortage of effective distribution channels and lack of investment in improving processes can in the same way hinder their ability to scale up businesses quickly or respond swiftly to changing business dynamics. Institutions obviously want to take advantage of opportunities in the marketplace quickly, and all these factors are motivating them to explore acquisitive growth as an alternative moving forward.

Shift towards inorganic expansion

More than half of our respondents (54%) said they were most likely going to carry out an acquisition, or would be considering one within the next 12 months. This is higher than the 42% who gave the same response in the 2009 survey. Also in alignment with this theme of growth, only 21% of respondents pointed to the likelihood of divesting business units in 2010, lower than the 25% recorded in the 2009 survey. Financial institutions believe that their business units are, on the whole, performing up to par, and that the preference was to be buyers rather than sellers in 2010.

However, the current level of interest in M&A has still not reached the high levels seen prior to the crisis. Around 65% of our respondents recall how their institutions were assessing M&A opportunities 12 months prior to the escalation of the crisis in 2009. Nonetheless, the percentage favouring acquisitions in 2010 may actually be higher than it appears, given that some parties might be undecided currently, but have not ruled out M&A outright and would not hesitate to explore opportunities that present themselves at the appropriate time and price.

06

Motivating factors for M&As

A diverse array of factors and pressures are pushing financial institutions to continuously explore acquisitions. In this section, we discuss today's main drivers for M&A, ranging from the need for size to enable economies of scale and to expand the scope of product offerings, to the intention to diversify into emerging markets, and to tap into the many opportunities that have surfaced following the crisis.

Financial institutions interviewed look to M&A as the quickest way to expand their core business lines and capture market share. With the crisis receding, confidence about future economic conditions increasing, and threats against their core businesses greatly diminished, financial players have become more intent on growing market strength inorganically. This pursuit of additional market strength was identified as the main motivating factor for M&As by 82% of respondents.

Here, we note a strong acquire-the-competition drive among institutions in saturated and ultra-competitive markets. In South Korea for example, a banking executive remarked that most Korean banks have significant overlaps in terms of client base. He commented that 'too many banks compete with and cannibalise each other, so M&A would lead to stabilisation in terms of market positions.' Meanwhile, in Taiwan, despite two major financial reforms in recent years, the industry remains severely fragmented. M&A is seen as a

necessity for core banks to incrementally enhance market shares and for a few select players to emerge as true national champions.

The more aggressive drive to acquire market share through M&A can be seen as an outcome of the recent experience of banks which saw significant customer churn, especially in deposits. One executive in Hong Kong opined, 'In times of market instability, it is this strong market sizing that would set the bank apart from its peers. Depositors would feel more assured of the safety of their monies if these are placed in a large, well-known institution.' This sentiment was echoed by other executives in mainland China, Indonesia, Thailand and Australia.

Indeed, the battle for market share has intensified as the crisis has created further market share consolidation among top-tier players. In many countries, particularly Australia,

Malaysia, mainland China, Singapore and Indonesia, the larger financial institutions have become even larger, capturing a disproportionate share of business from their smaller peers. For the large players that we interviewed, M&A will solidify, once and for all, their dominance in the marketplace. Among the mid-sized players, growth through M&A would be the way to regain market share that was lost, even though they face increasing challenges in funding the required acquisitions.

As M&A is completed, and as market share concentration among top financial institutions becomes more obvious, there will be more spirited discussions about whether one can have too large a market share. The growing prominence of domestic giants will highlight not only 'too-big-to-fail' issues, but also systemic risk considerations – both issues gaining prominence worldwide due to the global crisis. For instance, one executive in Australia talked about 'the stratification of the market between big players and then the small players'. This division brings to the fore issues of collusion or unfair pricing power amongst the top-tier institutions. Larger banking institutions might be looked at as unfairly advantaged by greater access to liquidity and lower cost of funds.

This has not escaped the wary eyes of regulators. At the time of publication, anti-competition issues have impacted NAB's acquisition of AXA Australia and New Zealand, with certain divestments by NAB likely to be required in order for the deal to proceed.¹⁹ If the acquisition does not proceed, this potentially allows another player to bid for AXA's established business in the Australia and New Zealand region, with AMP having already bid for the business prior to NAB's interest.

Geographic expansion

The second most important motivation for M&A, as cited by 56% of respondents, is geographic expansion. Firstly, this includes domestic, in-country expansion for countries that are geographically spread out and still have large or under-served populations. Banks and insurers are keen to acquire peers that are geographically prominent in certain regions of the country and which have sufficient distribution networks. This, according to the respondents, was a major push for acquisitions by financial institutions in geographically spread-out markets such as mainland China, Indonesia, India, the Philippines and Vietnam. In mainland China and Vietnam, new cross-province branch licensing guidelines have encouraged further scrutiny of how M&A could help expand the breadth of distribution networks.

Respondents also make strong reference to outbound cross-border geographic expansion, an especially crucial motivating factor for M&A activities of foreign institutions in countries like mainland China, India and Vietnam. These markets show high growth, but still present difficulties for new (or foreign) players to get business licences. As such, acquisition of established peers will provide, 'entry to a market where organic growth is not financially viable or too painstaking', says an executive from an international bank.

Executives are quick to note, however, that the next few years will open up exclusive opportunities for market entry, seen in new financial sector master plans launched in Thailand, Malaysia and Vietnam (discussed earlier). In Taiwan, significant M&A developments are expected to emerge from the expansion of the financial sector MOU (Economic Cooperation Framework Agreement or ECFA) between mainland China and Taiwan, expected to be signed in 2010.²⁰ 'This is a highly anticipated development that would have implications on the ability of Taiwanese firms to scale up businesses in the mainland,' says Peter Yu, Partner at PricewaterhouseCoopers (Taiwan).

What is also interesting is that just as the region's powerhouses are poised to digest acquisitions across several jurisdictions, some global institutions are expected to make new multi-country forays. For example, in 2010, HSBC is set to acquire the retail and SME businesses of RBS in India, mainland China and Malaysia.²¹ The proposed acquisition is awaiting approval from respective country regulators. This acquisition aims to enhance the market position of HSBC in these emerging markets, as it will add the network of ABN AMRO in India in relation to the acquisition of ABN AMRO by RBS.

On the insurance front, Prudential had ambitions to become Asia's number one insurer by acquiring AIA, the Asian business of US giant AIG. Integrating the operations of AIA into Prudential would have placed the latter in a strong leadership position in all the critical growth markets in the Asian region. Unfortunately, Prudential dramatically pulled out from its bid following a mismatch in pricing (AIG had agreed on US\$35.5 billion, but Prudential had later asked for the price to be cut to US\$30.4 billion following fierce opposition from some shareholders),²² highlighting precisely the vulnerability of cross-border deals, where cross-jurisdictional issues, shareholder votes and funding play a crucial role in merger deals materialising or collapsing.

Other drivers

Another motivator for M&A is typically seen in mature markets. Product and customer service enhancement was cited as an M&A motivator by 38% of our respondents. This illustrates that beyond size-building, or market share expansion, there are customer-centric objectives in M&As. These customer-centric considerations, however, would typically be secondary motivators, mentioned together with the two other higher priority drivers discussed earlier.

'The goal for many institutions in these markets is to be a true financial partner of customers, and that means being able to offer the widest array of products and services that a customer might potentially need. This will spur organisations to look at acquiring adjacent businesses and enter new business lines – for example, banks acquiring

19 'NAB stuck in tricky position in effort to get AXA takeover cleared by regulator', Sydney Morning Herald, 11.06.10

20 Source: 'Foreign business groups optimistic on ECFA: official' Focus Taiwan News Channel, www.focustaiwan.tw, 21.05.10.

21 Source: 'HSBC set to buy RBS Asia assets', Reuters, 09.12.09.

22 Source: 'Pru withdraws from 3-month, \$30.4 bn AIA bid', Reuters, 02.06.10.

insurers, wealth management divisions, brokerages, or consumer finance firms,' says Kok-Weng Sam, Partner at PricewaterhouseCoopers (Singapore).

The ability to offer more products and services will not only enhance customer relationships, but will also have top- and bottom-line benefits for the financial institution itself. More lines of businesses will allow them to capitalise on potential up-sell and cross-sell opportunities. Institutions will also endeavour to expand their share of the customer wallet, believing that the more product holdings a customer has with the institution, the more sticky and profitable will be the institution's relationship with the customer.

Taking on multiple core lines of businesses will also enable a smoothening out of revenue streams. Typically for bancassurance for instance, distribution fees represent a comparatively volatile revenue stream for banks, especially if banks keep to open-source distribution platforms. For a bank, having its own insurance product offerings translates into a recurring income stream from management fees and product manufacturing fees. A top-tier bank in Taiwan stated this as a driver for its prized acquisition of an insurance product manufacturer. The acquisition will also be beneficial for the acquired because such insurance product manufacturers typically see lower margins due to the reliance on tied agents, and the bancassurance tie-up with its parent company would allow it to go to market though the bank and enhance its margins. The consolidation of 'adjacent businesses like bancassurance will make the most financial sense,' remarked one executive.

Coincidentally, the aforementioned financial sector master plans will encourage this trend of consolidation of multiple lines of businesses.

Banking master plans such as those in Thailand will push for the creation of universal banks that are able to serve retail, commercial and corporate customers. Single presence rules in other master plans will also force multiple lines of businesses under one holding company to consolidate.

Size is might...

Overall, respondents cite the need to attain critical size, with 91% of respondents agreeing that size provides their bank or insurer with a clear edge over the competition. The pursuit of size is premised on three intended benefits: wider distribution capabilities, cost efficiencies and competitive pricing.

Banks still see the ability to reach the customer as a key competitive factor moving forward, especially as they go into new sources of growth such as micro-finance, SME lending and payments. Success in these three areas is reliant on the breadth of distribution channels. In insurance, one executive notes that the 'ability to attract agents and collaborate with the banks for bancassurance tie-ups are also often correlated to sizing'. It would appear that in the post-crisis world that encourages a financial institution to offer a diverse array of in-house and externally sourced products, size gives an institution the ability to bring advantageous partners into the fold. In asset management, one player in mainland China stated that 'size is important in gaining trust from the market,' allowing the company to work with more customers and thus bid for a bigger slice of market activity.

Size is also crucial for financial institutions, as there are certain fixed overheads that need to be covered regardless. M&A potentially brings efficiencies in terms of reducing operating costs, as well as in increasing throughput, while using the same or only marginally higher resources. Respondents tend to see opportunities for such synergies as being more significant where there is a greater degree of customer overlap and where businesses operate in adjacent businesses. With size comes not only a stronger and more effective branding, but also the ability to leverage cost efficiencies to provide customers with a more competitive pricing. Of course, 'competitive pricing' also alludes to the ability of the organisation to see better margins on account of lower operating costs.

...But pursuit of size is not the end game

However, many institutions are well aware that one of the lessons of the crisis is that size, on its own, does not guarantee success. 'The crisis did warn us about the importance of assets and customer quality, which should be more important than chasing sheer size,' commented an executive from one of mainland China's largest banks. Another player in mainland China said that 'most companies will look at the strength and health of the company as better indications of the quality of the company, not size.'

This principle that size is not necessarily the most important determinant of success will guide institutions in undertaking M&As post-crisis. Other factors such as the quality of customer base, its entrenchment within the market, and the extent of its distribution channels and its network of partners will be seen to imbue value to an institution, and will, in addition to the chase for size, feature in M&A considerations moving forward.

07

Road blocks in store

On the flip side, acquirers recognise the issues that could potentially prevent them from securing an attractive target at a worthy price. This section elaborates on the range of factors and obstacles to fair valuation which respondents say would influence their decision to follow through with an acquisition.

We asked executives whether the way they evaluate acquisitions has changed following lessons learnt from the global upheaval. While some acknowledged that 'the financial crisis has changed the dynamics of valuation and due diligence process somewhat', and 'now more than ever, we are more cautious and have to internalise, define, and carefully articulate what an acquisition brings to the table, be it technology, domain knowledge, or marketing capabilities that are lacking internally,' our sense on the ground was that the way deals were forged has not been dramatically realigned in any shape or form. For the most part, players claimed complete thoroughness in a structured, systematic due diligence approach pre- and post-crisis.

What lies beneath (the numbers)?

So, what does that due diligence to determine the 'fair price' of a target entail? In addition to traditional measures such as net asset value (NAV), enterprise or economic value (EV), price/earnings ratio (PER), price-to-book (P/B), annual premium equivalent (APE) for insurers, cash-flow analysis and expected rate of return, executives interviewed also stressed the need to go beyond dissecting the target's financial performance, into other core areas to determine whether it is worth purchasing.

Other considerations, predominantly intangible, non-quantitative drivers that they are emphasising to estimate the theoretical 'correct' value of a company, include:

- **Determining the quality of the customer base.** Financial institutions looking to expand their customer reach are typically willing to pay a premium for a target with quality customers, defined as one with a stable of large, consistent customer base, or which is able to generate a predictable, recurring annuity-like revenue stream. A respondent from a top-tier bank in Indonesia also cited the ‘geographically dispersed nature of the customers to ensure nationwide reach and brand resonance’ as being crucial in valuing the customer portfolio;
- **Exploring existing strategic partnerships that are lead-generating,** such as the quality of the independent financial advisers (IFAs) of the insurer, or the value of co-marketing collaborations (like the quality of bancassurance partnerships), and how much new businesses such ongoing collaborations can engender; and
- **Questioning the level of technology innovation of the target corporation** as a consideration for its net worth. For instance, is the target a technology leader, quick follower, or perhaps even a laggard adopter? Value placed on this depends on the acquirer’s own technology play within the industry.

Obstacles to fair valuation

Once a target is marked for acquisition, danger during execution lies in oversimplifying the valuation process when acquirers, in their enthusiasm to seal a deal, push aside doubts, or sacrifice steps within the due diligence process. Respondents to our survey outlined core risks that could deter an acquisition:

Not knowing the true quality and robustness of the target’s assets: This was the most commonly cited hindrance to fair valuation given by the executives in the survey, especially in the emerging markets in Asia. For instance, a Singapore-based executive commented that due to the lack of data quality in emerging markets, ‘for our recent inaugural foray into Indonesia, we were deliberately targeting a company which was entirely foreign-owned from inception, so that we had better clarity and confidence in the degree of reliability and transparency of their financial and operating data.’ This need to thoroughly investigate the target’s true worth and pay special attention to the degree of liquidity of its assets is particularly imperative for acquirers venturing into unfamiliar geographic territories.

Buyers and sellers having mismatched expectations: Given that we are just climbing out from the depths of a recession, there exists a plethora of expectations on future potential performance of various geographies and institutions across this region. This creates a misalignment between the perceived values of buyers and price expectations of sellers, and when this chasm is too wide to bridge, arriving at a consensus, fair pricing, and determining what each party gets out of the consolidation, becomes a challenge.

A respondent also highlighted how certain transactions might set precedence in shaping potential sellers’ pricing expectations and further contribute to this misaligned expectation. He pointed to Malaysia’s Malaysian Banking (Maybank’s) controversial purchase of Indonesia’s Bank Internasional Indonesia (BII) during the depths of the financial crisis at 4.6 times book value.

Supervisory roadblocks and differing accounting rules: A cross-border acquisition, especially if the deal is sizeable, could raise the eyebrows of local regulators regarding issues ranging from loss of price competition to job losses, and result in them imposing specific measures or a veto of the proposed merger.

Meanwhile, differences in local accounting systems or even variations in interpretation of common rules are another key concern that resonated with several respondents. These variations in accounting rules lead to difficulties in assessing the financial situation of the potential target and the need to reconcile these measurement matrices for financial comparison. Multiple reporting requirements not only pose an execution risk, but also create an ongoing administrative cost post-integration, as the acquirer gets saddled with heavier reporting requirements and has to adapt personnel and reporting systems to suit both accounting requirements.

When deals break down: What could derail post-merger?

A good deal can sometimes turn into an ordeal if acquiring companies get caught up in the need to close the deal at all costs, and not heed warning indicators. As a respondent from Hong Kong aptly summarised:

‘As soon as the ink is dry, and the champagne bottle popped, is when the integration headache and real hard work begins!’

Here, we cite some key areas that warrant close attention post-acquisition to avoid eventual disappointment. As shared by the respondents, issues that could torpedo a merger include:

Underemphasising human resource issues: Human resources issues sometimes get swept under the rug during deal negotiations. This results in the acquirer failing to retain key personnel, neglecting to equalise salaries and benefits, or mismatching staff with job scopes, all of which can quickly mark down synergy projections by a huge percentage.

Moreover, ‘cultural differences, clash or resistance’ were cited by almost all respondents across the region, from Vietnam to Indonesia and Australia, as a definite issue that could throw a spanner in the works during the post-merger integration process. ‘Managing culture is partly about managing people, and when the labour kinks are ironed out, for the majority of the time, the process and technology integration will unfold by itself,’ commented an executive from Singapore.

Elsewhere, in multi-cultural Indonesia, an executive spoke about how ‘in merging an ethnic-Chinese merchant bank with a local, predominantly Malay-staffed, bank, the management team need to identify cultural fault lines and nuances early on in the M&A process and be very aware of cultural intangibles, such as unwritten rules, in the acquired company.’

All in all, respondents concede that the cultural factor may sometimes be seen as a soft issue but could nonetheless be the most challenging to resolve. Nothing can precipitate an exodus of talent like the collision of disparate corporate cultures, and as staff that do not fit into the new corporate culture begin to resign, the consolidated entity would face repercussions such as disruptions in productivity during the handover period, cost from severance package payouts and new recruitment, and issues around shaken shareholder and consumer confidence. At the extreme, another executive commented that cultures that are just too divergent and strong to integrate might even lead to the acquirer having to divest the target at a loss.

Taking too long to integrate the two parts: A common issue stems from acquirers thinking they have a sizeable timing buffer for the integration, and ending up crafting a long timeline and road map to assimilate the culture, operational and technology aspects of both organisations. A respondent from Vietnam spoke of the need to

‘ensure that there are as few disruptions and delays as possible to the day-to-day operations and that customers are not inconvenienced in the interim’

In reality, the time window from deal announcement to completion (typically 12 to 24 months) is extremely crucial. In the course of our interviews, we had several similar comments on how unnecessary postponement to business strategy integration and positioning of key management staff serves only to create uncertainty, high levels of employee anxiety and diminished morale as they remain defensive and uncertain about their future and, in turn, cause workforce or customer defections.

However, as one Australian executive remarked: ‘speed for the sake of speed is wrong, as the end game should be one of value creation, and not merely bringing the two entities together as quickly as possible.’ As such, post-announcement activities need to be prioritised according to which can unlock the most synergistic value.

Swallowing a target that is possibly too large: Sometimes, a potentially game-changing acquisition target comes along and the financial institution attempts to absorb the target – lock, stock and barrel. One of the international organisations taking part in the survey was in the midst of such a milestone deal and confessed that integrating the sizeable target across many differing jurisdictions would be a monumental management exercise, with the need to combine both entities at all levels and dimensions – across people, culture, processes, IT and infrastructure.

In such cases, the senior management team needs to adopt an extremely disciplined approach, as a wavering leadership could easily obliterate whatever projected synergy benefits there may have been. They also need to work their magic and communicate their intentions and ambitions appropriately with the analysts and media community (or as an executive from a Malaysian bank called it, ‘influencing the influencer’, while another mentioned ‘making sure that the media does not hype up integration hiccups’). Acquisitions involving large players mean that public perception needs to be crucially managed, perhaps even more so when the acquirer is a foreign entity.



Outlook: Peering into the horizon

Asian financial institutions generally expect M&A activities to increase in their market over the next 12 months. We shed light on their thoughts on the near-term M&A trends as they continually evolve to respond to changing market dynamics and investment opportunities.

Our survey reveals a consensus view that M&A activity in the region will grow in the next 12 months. Although the level of interest is higher than what we experienced in 2009, it still pales in comparison to the very confident M&A plans seen prior to the crisis. Nonetheless, we are certain that the percentage of respondents being open to acquisitive activities for the next 12 months is higher than the survey statistics depict, by simple virtue of the fact that while some respondents may not be actively seeking acquisitions at this juncture, they may not have ruled them out altogether. Several institutions acknowledged that they would pursue deals when the opportunity presented itself at the appropriate time and price. With the pace of recovery we are seeing in the region pointing to the return of ardent size-building and fierce market share battles, financial institutions would probably have to seek out acquisition opportunities more actively rather than wait for these to present themselves.

We expect that a few opportunistic M&As can still take place in the market. For instance, exit of select foreign financial institutions that are facing problems in their home countries would provide acquisition opportunities for domestic institutions and for the emerging super-regional organisations. Furthermore, regional institutions that are small and lack scale are typically still reeling from the downturn, and their exposed vulnerabilities could prompt sharp buyers to acquire these players at favourable price levels. However, interested parties have to act swiftly, given that the number of such potential deals would diminish as clear signs of recovery take hold.

Meanwhile, throughout the region, in addition to a 'back-to-basics' play, financial institutions are pursuing new sources of growth – entering new market segments, broadening product portfolios, expanding business lines and going into new geographies. As such, we see most M&A decisions being articulated in relation to these aspirations for new growth. This would, in turn, change the dynamics of the industry as new players emerge. These include:

- Domestic conglomerates making their first forays into financial services via the acquisition of small banks, and gaining prominence as traditional non-bank players with new financial services subsidiaries;
- Market entry strategies from the likes of consumer finance companies applying for banking licences, or from banks extending themselves both organically and inorganically into new lines of businesses such as wealth management, insurance, micro-finance or Islamic banking, or insurers similarly extending their presence into banking, micro-insurance, or takaful (Islamic insurance); and
- The formation of super-regional institutions, led by banks in Singapore, Australia and Malaysia. Large domestic players in mainland China, South Korea, India and Indonesia are not resting on their laurels but likewise designing their regionalisation strategies. We expect these newly minted regional players to gain strength and compete against international institutions with significant Asia-Pacific focus such as HSBC and Standard Chartered Bank.

All these developments would be done on the back of changes to the rules of competition, especially with the introduction of new financial sector master plans, modifications to regulations governing competition in the banking and insurance sectors, and new capital rules such as Basel III due to be implemented at major financial jurisdictions by the end of 2012.

In conclusion, it is evident that financial services M&A activity has been transformed by the recent crisis, with institutions claiming greater regard for real value, based on real growth from real assets.

Learning from past mistakes, while cautiously tapping into these other avenues of growth, the financial institution of today is moving back to fundamentals, and will build a business on strong balance sheets of loans and deposits, rather than one that is overly dependent on financial leverage or gearing. We see M&A valuations increasingly reflecting this emphasis on real value. Factors such as the quality of customer base, a target's entrenchment within the market, the extent of its distribution channels, and the strength of its network of partners are rightly becoming core considerations moving forward, as opposed to valuations based merely on sheer size.



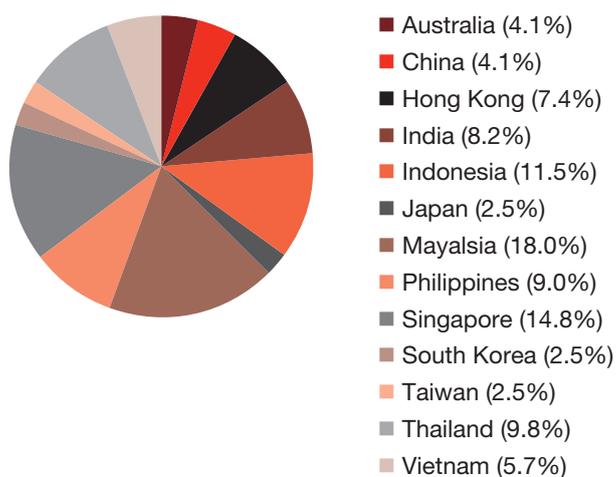
Appendix: Aggregated survey results

This section presents the consolidated findings from face-to-face interviews and web/telephone surveys of senior M&A decision makers or influencers from across 13 territories in Asia-Pacific (number of respondents = 122).

We would like to thank all the executives who participated, for sharing their insights with us.

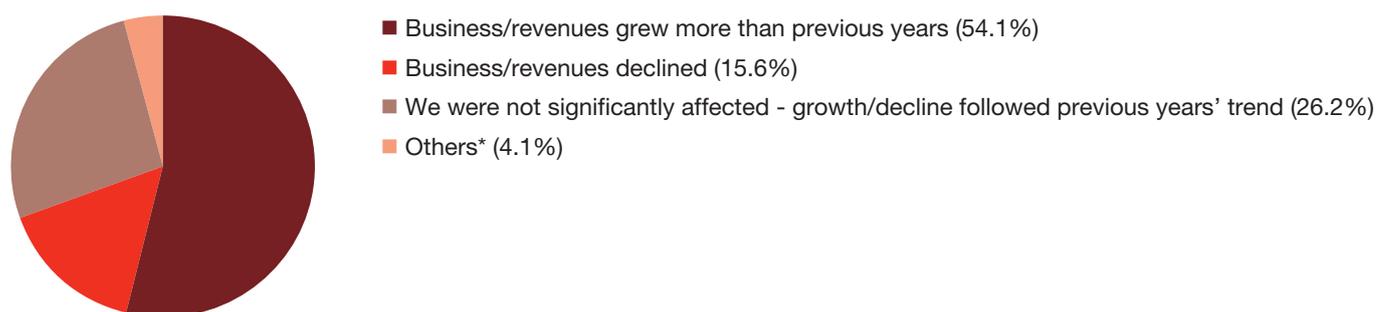
Please note that the totals may not always add up to 100 percent due to rounding. We had 122 respondents from 122 unique organisations, with variations to N (N = number of responses) where multiple responses were permitted, or where questions were follow-ups specific only to a select group of respondents.

Figure 1: Q1: In which country are you currently based?



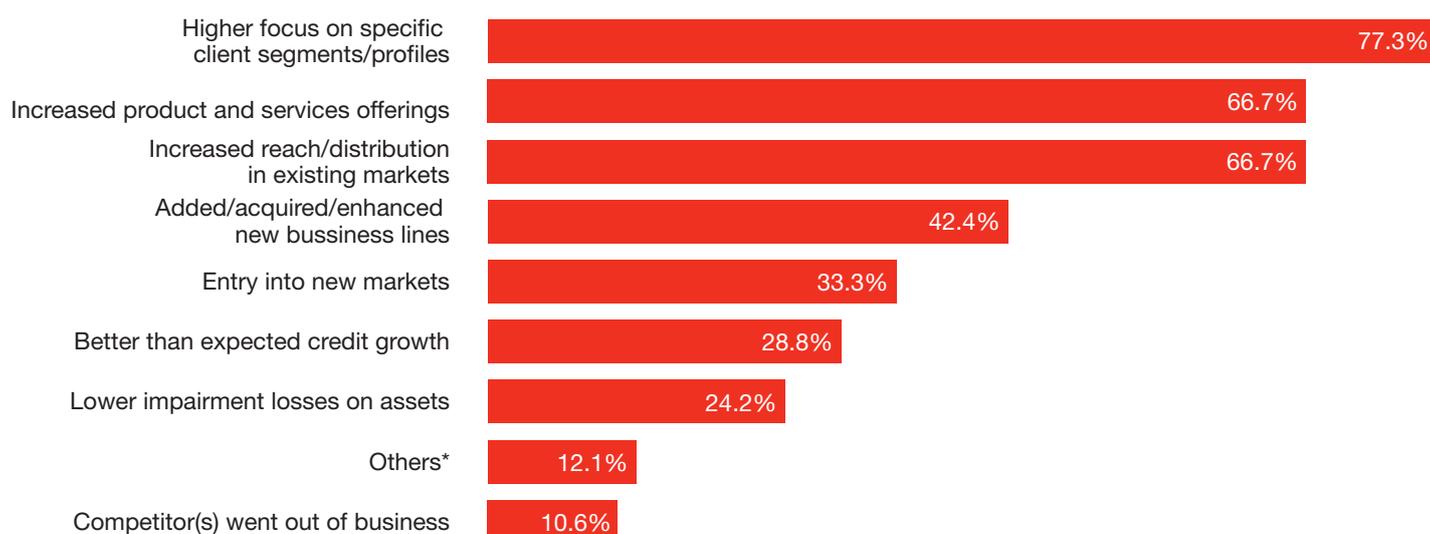
Note: For all subsequent charts and graphs, unless otherwise stated: N = 122 responses from 122 respondents, and the source is PricewaterhouseCoopers/IDC Financial Insights M&A Survey, 2010.

Figure 2: Q2: What changes, either positive or otherwise, have you seen in your organisation as a result of the past financial crisis?



*Others included: The organisation being more cautious and vigilant in credit analysis; having to compete within their traditional segments such as deposits and loans with aggressive foreign players; or re-defining their Asia strategy

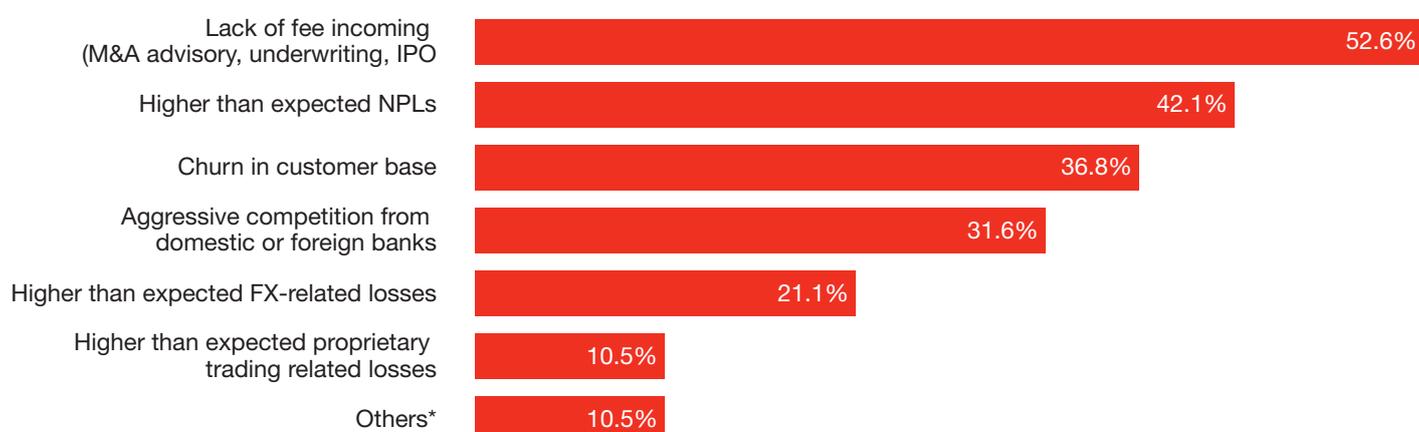
Figure 2.1: Q2.1: If your organisation enjoyed a YoY growth in revenues, what were the triggers for this expansion?



*Others included: Aggressive growth targets which can only be met by supplementing with inorganic expansion; lower than expected NPLs; expansion by virtue of strong brand recognition; sufficient access to funding liquidity; bank was “forced” to re-prioritise transformational projects and this yielded benefits; growth was from other lines of businesses (e.g. Life insurance, brokerage & financial products distribution arm) that performed better YoY

N = 239 (multiple responses allowed) from 66 respondents which saw an increase in revenues in 2009 (i.e. the 54% in Figure 2)

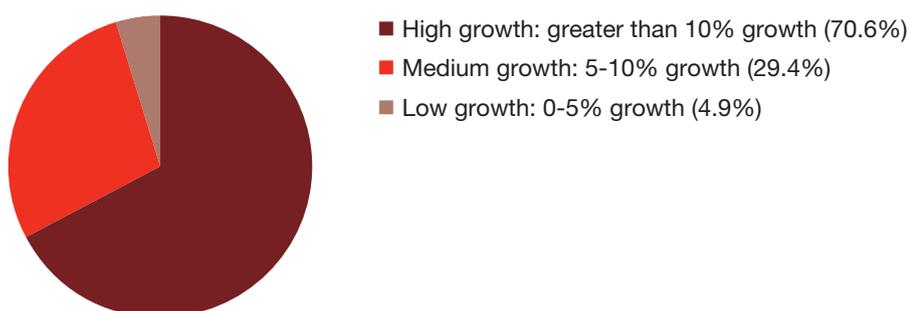
Figure 2.2: Q2.2: If your organisation had YoY fall in revenues, what were the reasons for this decline?



*Others included: The effect from political instability; great losses from sub-prime mortgages and securitisation further exacerbated by significant potential drops in stock markets

N = 39 (multiple responses allowed) from 19 respondents which saw a fall in revenues in 2009 (i.e. the 16% in Figure 2)

Figure 3: Q3: What level of business growth do you expect to see from your organisation in the next 12 months?



Note: None of the respondents selected the “negative growth” option. The 6 respondents (4.9% of total) who cited low growth were from Hong Kong (1), Japan (1), South Korea (2) and Thailand (2)

Figure 4: Q4. Was your organisation planning to take part in, or assess any M&As in the 12 months prior to the crisis (i.e. in the 12 months before Aug 2008)?

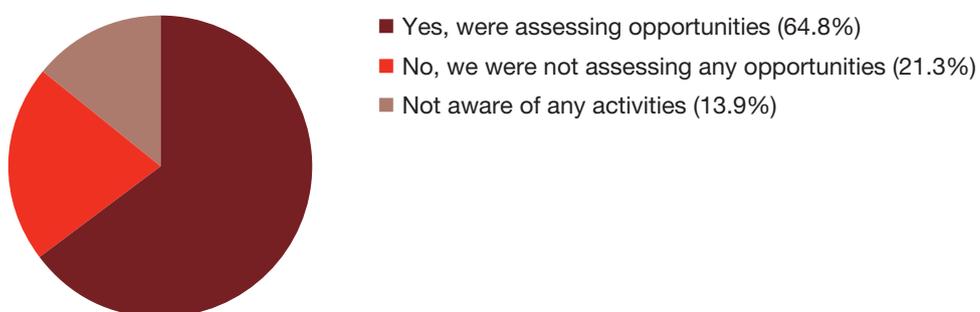
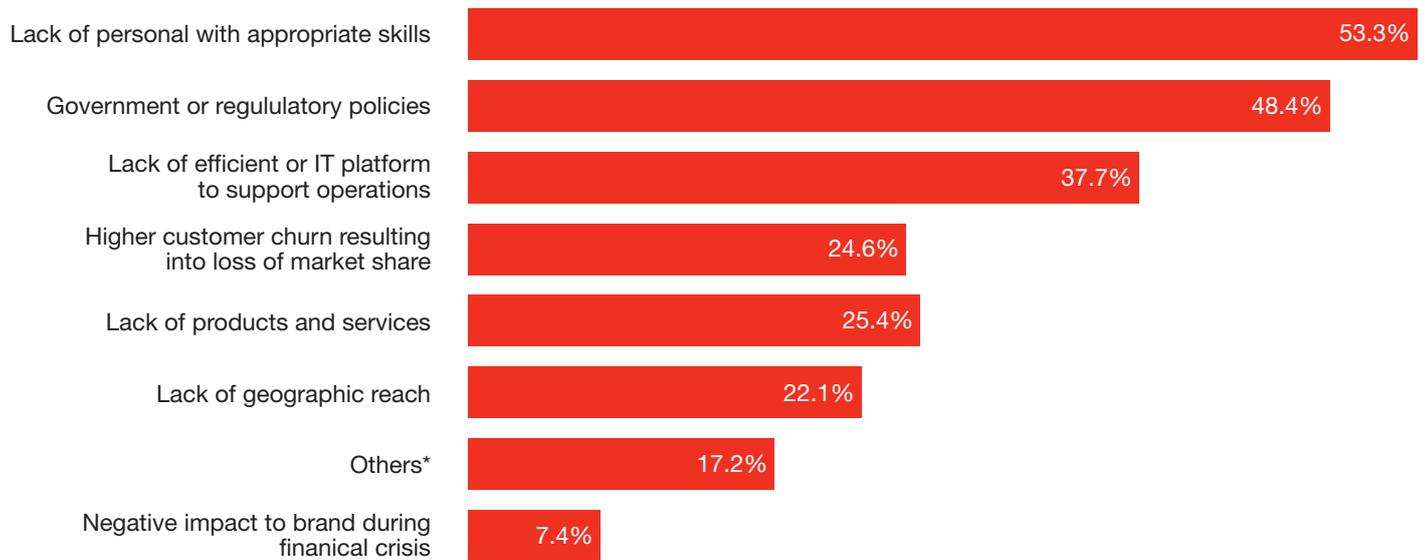


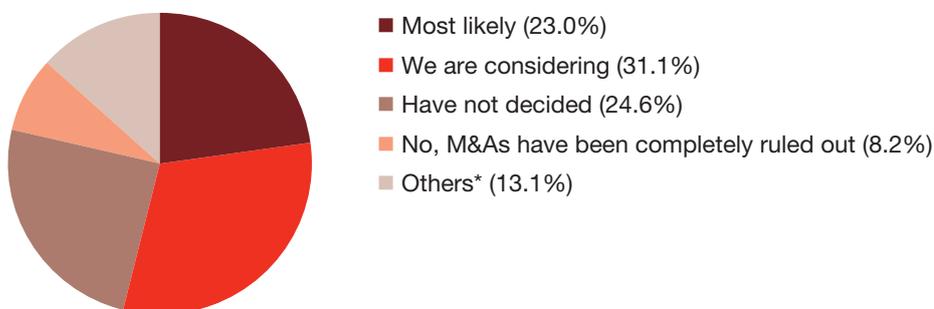
Figure 5: Q5: What are the inhibitors of growth that may prevent your organisation from taking full advantage of the post-crisis economic revival?



*Others included: Limitations to capital funding, and obtaining that funding at the right price; or lack of collaboration internally between the various business unit: asset bubbles with the risk of potential bubbles forming in Mainland China, Hong Kong and Singapore; competition from the other local banks that are likewise ramping up their technology platforms, channel and distribution reach; the EU countries' economic problem which might affect the trade finance business

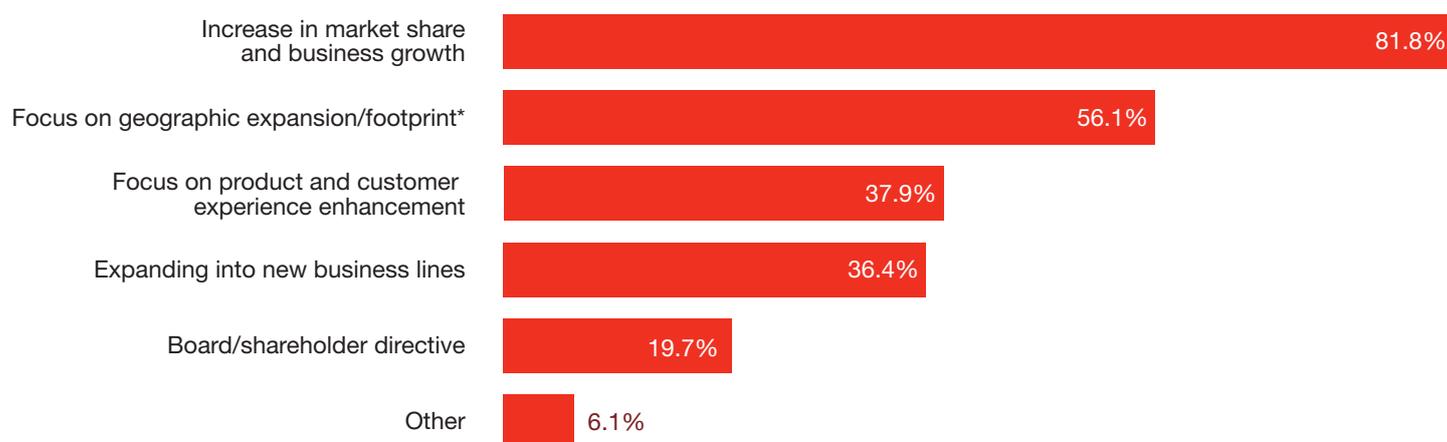
N = 285 (multiple responses allowed) from 122 respondents

Figure 6: Q6: Is your organisation likely to evaluate a merger or make an acquisition in the next 12 months?



*Others included: The respondents saying that they are always on the lookout and will do so if the opportunity presented itself; or depending on how the economic environment unfolds itself. One of the organisations was itself in the process of being acquired, while another is targeting acquisition opportunities outside of the financial institution.

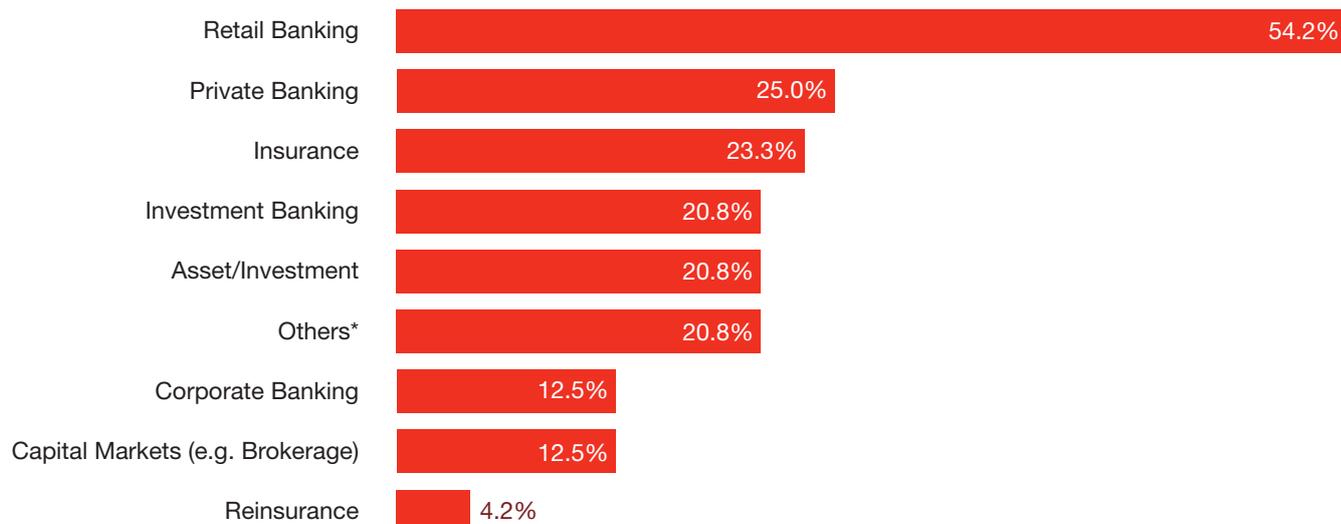
Figure 6.1: Q6.1: If your organisation is evaluating an acquisition in the next 12 months, what would be the primary motive behind the acquisition?



*Focus for geographic expansion was in-country (i.e. other states/provinces), and into new markets like Mainland China and India, and South East Asia (predominantly Indonesia and Malaysia)

N = 157 (multiple responses allowed) from 66 respondents (i.e. those who cited they were “Most likely” or “We are considering” M&As in Figure 6)

Figure 6.2: Q6.2: If the primary motive for acquisition is expanding into new business lines, which of the following areas is your organisation planning to acquire?



*Others included: Remittances and micro-finance operations; investment areas being depend upon the upcoming economic developments

N = 49 (multiple responses allowed) from 24 respondents (i.e. those who cited that a primary motive for acquisition was to “Expand into new business lines” in Figure 6.1)

Figure 7: Q7: Is your organisation likely to make a divestment in the next 12 months?

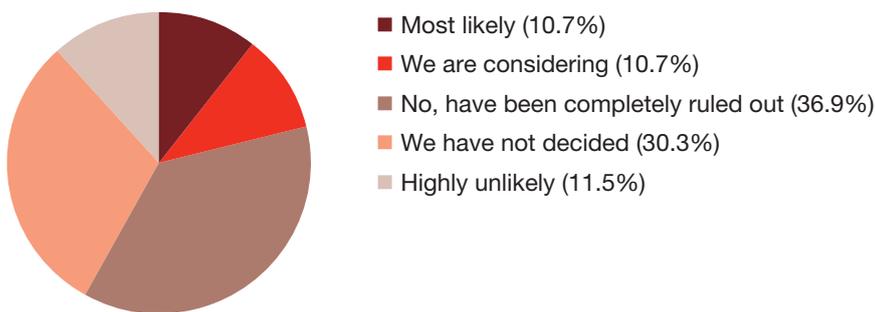
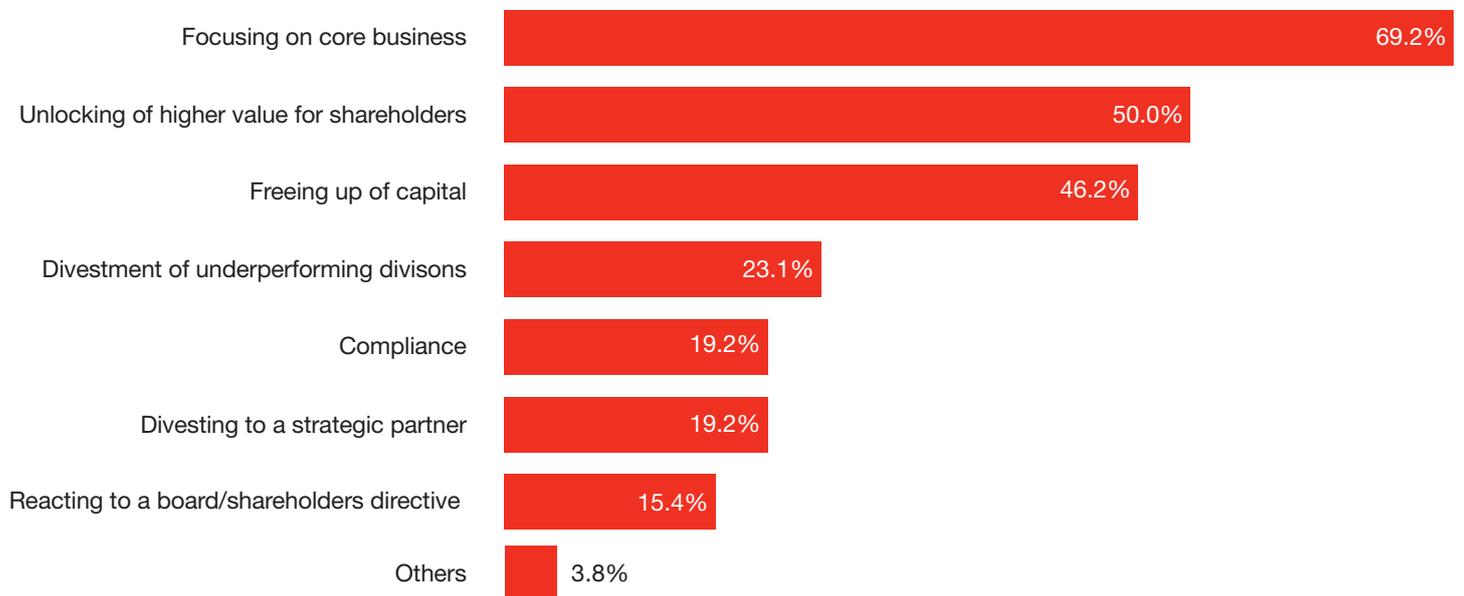


Figure 7.1: Q7.1: If your organisation is evaluating a divestment in the next 12 months, what are the three main reasons behind the divestment?



N = 64 (multiple responses allowed) from 26 respondents (i.e. those who cited that they were “Most likely” or “We are considering” divestments in Figure 7)

Figure 8: Q8: In the post economic crisis market, how important do you think size (in terms of assets) of an organisation in giving it a competitive advantage?

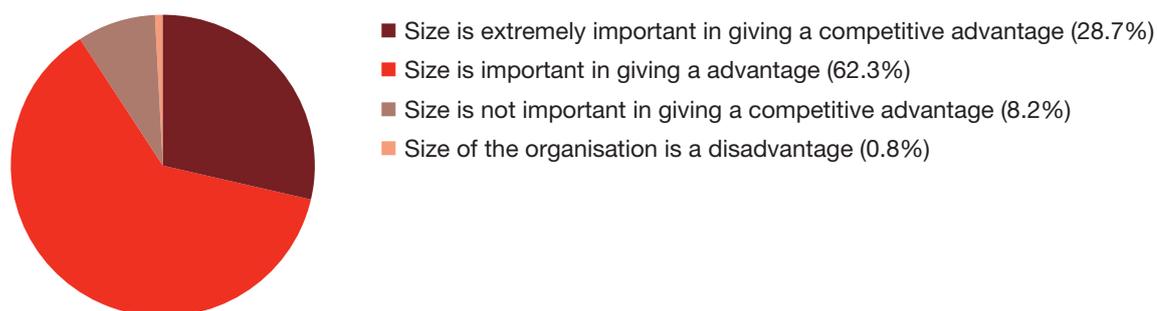
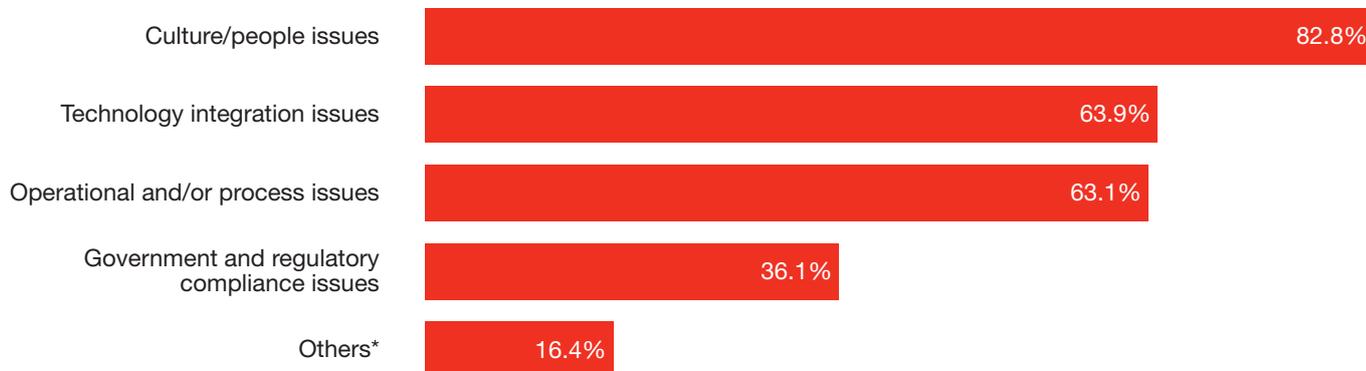


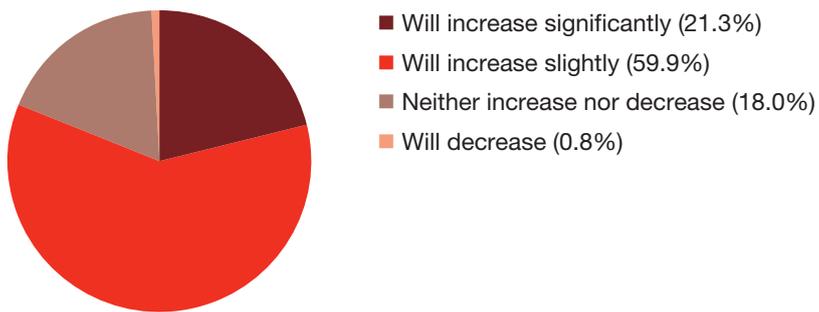
Figure 9: Q9: What challenges does the management team face during or after an M&A?



*Others included: An accurate valuation of the revenues and cost structure of the target during the due diligence process, especially since there might be a lack of financial disclosure and accurate information by the target entity (which is a reality especially in the developing nations in Asia); hidden or undisclosed problems in the target's financials that do not surface till post-acquisition; retaining customers from the acquired institution.

N = 320 (multiple responses allowed) from 122 respondents

Figure 10: Q10: Do you expect M&A activity to increase in your market in the next 12 months?



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