
THE GREAT BANKING CRISIS OF 2008: Lessons Learned and Outlook for the Future

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AGENDA

- research for book
- key findings and lessons
- the big issue: how to prevent it ‘next time’!



A. OUR RESEARCH

- **in depth, off the record interviews in early 2009 with 25 senior professionals**
- **variety of points of view: bank chairmen and other senior bankers, regulators, rating agencies, management consultants, equity analysts**
- **key questions:**
 - what have we learned to prevent this happening again?
 - what will be the impact of these insights on banks' strategy?
- **subsequent events!**



B. KEY FINDINGS AND LESSONS

1. Before it happened:

- **Macro analysts saw it coming (IMF, trade imbalances, sub-prime lending, etc)**
- **Every financial crisis is different, but MOST have common elements: real estate bubble and excess leverage**



B. KEY FINDINGS AND LESSONS (*cont'*)

2. *Risk management:*

- **don't use statistical models based on historical data that's not relevant**
- **top management MUST understand risk and not delegate responsibility**
- **risk management may be too complex today for normal human beings to understand!**
- **rating agencies offer only a limited support: the model is not likely to change**



B. KEY FINDINGS AND LESSONS (*cont'*)

3. *What is likely to change?*

- **in general, higher capital ratios and new ratios for liquidity; more capital for more risky businesses**
- **bank ROEs will fall to 12-14% vs. 20%+ in the good old days**
- **more collaboration between regulators**
- **more focus on products and clients that generate client deposits: wealth management, SME, etc**
- **fewer 'narrow' banks and SIVs (off balance sheet vehicles)**



B. KEY FINDINGS AND LESSONS (*cont'*)

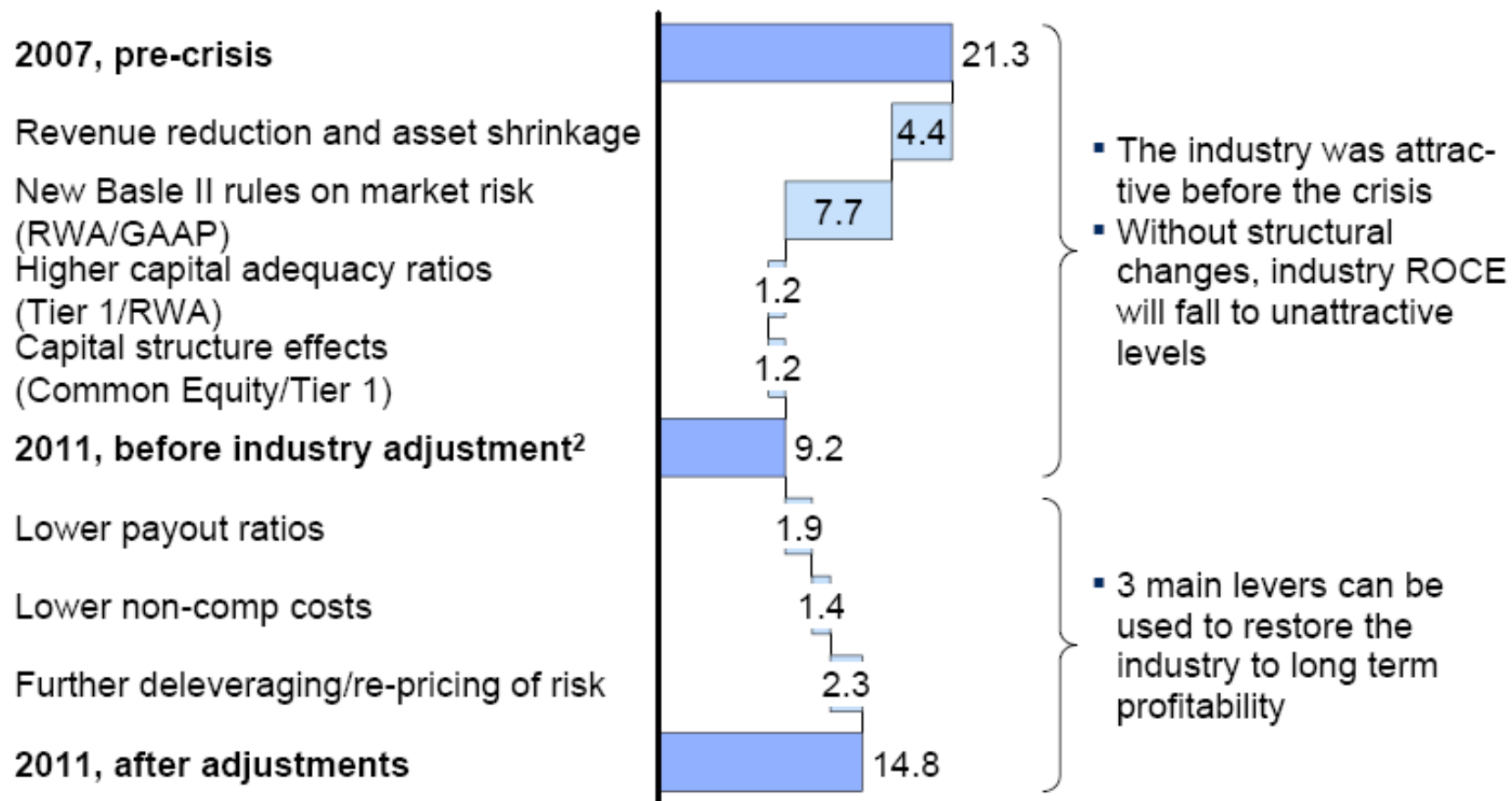
4. *What is NOT likely to change!*

- **investors STILL want earnings growth (as well as lots of other things!) which drives management priorities**
- **in geography preference, rapidly growing emerging markets are still the priority**
- **so leading banks are NOT planning to change their basic strategies!**
- **bank management (strong and risk-oriented) is the key success factor, not the business model!**
 - there is no one ‘best’ model
- **basic banking is STILL a profitable business**



B. KEY FINDINGS AND LESSONS (cont')

Pre-writedown post-tax ROCE¹ of top 15 CIB banks, %



¹ Applying the 2006 tax rate of 26.5%, because the actual 2007 tax rate of 20% was abnormally impacted by writedowns

² Ignores the increase of provisions for loan losses from 0.05% of GAAP assets in 2007 to 0.17% in 2011, which would have a negative impact of ~3% on ROCE and the change in extraordinary losses between 2009 and 2011

SOURCE: Company reports and investor presentations; Global Capital Markets Revenue Pool; Bloomberg; McKinsey analysis



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B. KEY FINDINGS AND LESSONS (*cont'*)

5. *Regulatory lessons and issues*

- **taking a punch bowl away from a party is never easy, especially when everyone's a winner (until 2007)!**
- **dealing with public anger has made life even more difficult!**
- **anticipating the crisis is not the issue: but taking action is!**
- **decisive action pays off: EU bail outs, US stress tests**



B. KEY FINDINGS AND LESSONS (*cont'*)

5. *Regulatory lessons and issues (cont')*

- **the issue of ‘too big to fail’: can it be addressed in practice?**
 - a version of old size and complexity argument: ‘has banking become too complex to be managed by human beings’?!
 - the US regulators close down hundreds of smaller banks every year
- **the issue of the ‘casino bank’ vs. the ‘ordinary, transparent’ bank: what might happen?**



B. KEY FINDINGS AND LESSONS (*cont'*)

5. *Regulatory lessons and issues (cont')*

- **flexible regulation seems to have worked well:**
 - Bank of Spain action on loss reserves and SIVs
 - other action against complex, leveraged investment products
 - successes in Canada, Australia
- **bankers' bonuses: shooting the wrong messenger!**

C. HOW DO WE PREVENT/MINIMIZE THE NEXT CRISIS?

- **not by multiplying the number of regulators and the complexity of their task!**
- **more reliance on SUPERVISORS who know their banks!**
 - the supervisor's key focus: do I trust this management and do I know their business?
- **use outside experts/consultants if necessary for complex problems**
 - example of General Motors break up in the US



C. HOW DO WE PREVENT/MINIMIZE THE NEXT CRISIS? (*cont'*)

- **proactive, flexible and counter-cyclical regulatory action**
 - one size does **NOT** fit all
- **your own experience?**



**WHAT A DIFFERENCE A YEAR MAKES! –
an excerpt from my October 2008 presentation in
Bangor**

WHERE DO WE GO FROM HERE?

- **uncertain outlook for the ‘real’ economy: future losses for the banks?**
- **what will be the future investor model for bank stocks? growth or yield?**
- **reduced attractiveness of investment banking: back to basics?**
- **can regulators achieve the voters’ objectives?**

