Cross-Border Banking
An Accenture Study of Cross-Border Mergers & Acquisitions in Banking

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Introduction

As banks prepare for life in the post-recession world, they once again are turning their attention to mergers and acquisitions as a way to reignite growth. Many banks are hopeful that M&A will allow them to enter new markets, as well as acquire new customers for product and service expansion. And for many institutions, such deals increasingly will involve investing in new partners in other countries.

However, as they pursue cross-border deals, banks will face considerable complexity, not to mention heightened risk. Thus, it is important for these institutions to understand the factors that are critical to executing a deal in a way that minimizes risk and generates sustainable, long-term financial value for the acquiring bank.
CUSTOMER SERVICE
NEW MARKET EXPANSION
Repeat business
Word of mouth marketing
SINGAPORE
MALAYSIA
TEAMWORK
A Study of Cross-Border Deals

To help shed light on these success factors, Accenture recently analyzed 89 publicly announced cross-border deals in the banking industry between 2000 and 2009. Financials for acquired bank companies were sourced from financial statements either published originally by the company or filed by the bank with the local bank regulator. Seventy percent of the deals studied were majority deals, while the remainder involved minority stakes (i.e., a one-time investment of less than 50 percent).

Accenture’s research measured the impact cross-border deals have had on the acquired bank by considering the long-term financial performance of the target, beginning with the fiscal year after the deal was completed and spanning a period of years following deal completion (through fiscal year 2009). This approach provided deeper insight into success attributes for each deal, as well as the factors that correlated most strongly with long-term success or failure. Notably, many of the analyzed deals spanned the period leading up to the global financial crisis and during its most challenging point.

When appraising the success of each deal, Accenture used five key financial metrics to analyze how well the new foreign parent company was able to achieve sustainable financial improvement in managing its new local banking partner over time. These were the equity price performance of the deal one year following completion, annual revenue expansion, post-tax return-on-equity levels, the efficiency ratio, and market value performance of the acquired company. Focused on these five metrics, the analysis revealed some important findings.
The cross-border deals, especially those that assumed 50 percent or more of the target bank’s ownership, often quickly boosted equity returns and the financial performance of the target.

In fact, 69 percent of cross-border deals realized positive equity returns—on average, a 48 percent improvement—with the best-performing deal enjoying a 169 percent return in the first year. By rewarding the acquired company with an early equity price premium, the markets are investing in the long-term potential for a local bank to better create shareholder value in being acquired by a foreign bank. These acquisitions also achieved quick gains in operational performance. For example, 42 percent of majority-stake deals realized profitability improvements in the first year,3 while 53 percent resulted in an improved efficiency ratio. Overall, the average efficiency ratio improvement of majority-stake deals was 5 percent (see Study Chart 1).

The majority-stake deals largely have outperformed the minority-stake deals over time. They also helped achieve sustainable profitability of the local company after the acquisition, and drove sustainable economies of scale and efficiency gains.

In terms of one-year equity returns, 79 percent of majority deals realized positive returns for an average 56 percent improvement, with the best deal generating a 157 percent return. When considering all deals, six of the seven top returning transactions were majority owned, with all having returns of 60 percent or better. In comparison, three of the four worst-returning deals were minority deals, with declines of 24 percent or worse (with one acquisition resulting in more than an 86 percent drop (see Study Chart 2).
Accenture also found that in majority deals, the acquired banks were often able to raise their profitability above pre-acquisition levels. In fact, in a majority of the years following the year it was acquired, the target bank achieved a higher level of profitability and efficiency than the respective levels it managed the fiscal year it was acquired.

Although minority-led deals were less likely to achieve improved profitability in the short-term, they proved to be successful in terms of revenue generation.

Banks focused on strategic outcomes rather than short-term gains, may still realize benefits in the long-run with minority stake ventures. In fact, the minority deals analyzed resulted in an average 19.3 percent compound annual growth rate (CAGR) and they comprised four of the six best-performing deals in terms of average revenue growth (two deals in India and Vietnam). Minority-led deals can drive revenue via improved brand awareness, boosted capital, and transferred technology, expertise and innovation. In this way, many leading international banks begin to make the appropriate investments to better ensure future performance success if they later choose to assume a majority stake in the local institution.

A majority of the cross-border deals have resulted in both short and long-term success for the foreign acquirer—especially those involving emerging-market partners.

Conventional wisdom has held that when a bank acquires in its same market, synergies are created around similar processes, products and customers. Also, buying a local market peer allows for easier integration. This study, however, indicates cross-border M&A can be achieved efficiently and will often lead to sustained profitability when banks acquire outside of their typical markets and move to new geographies and economies. In fact, emerging-market deals have generated a higher level of annual revenue expansion (18.7 percent CAGR) than those completed in developed markets (14.6 percent CAGR). And of the 15 best-performing deals overall in terms of revenue generation, 12 were done in emerging markets. Likewise, the seven best deals in terms of equity returns were completed in emerging markets (see Study Chart 3).
In sum, the Accenture research indicates that cross-border M&A can generate substantial long- and short-term value for global banks—particularly those deals that involve emerging-market partners. In the following pages, Accenture details the reasons why emerging market deals generate such robust value and discusses the cross-border strategies of several leading banks in search of sustainable growth and high performance.
The Performance Potential of Emerging-Market Deals

Among the study’s key findings, perhaps the most compelling is the fact that deals in which a bank acquires another bank in an emerging market have tended to outperform those in which the target firm was located in a developed market. In Accenture’s view, there may be several reasons why this is the case.

Because emerging markets tend to have low penetration of banking services and products, they present banks with a considerably greater opportunity to expand their presence and increase their revenue than in markets in which banking services are more widely available. For example, loan penetration is less than 50 percent in such Central and Eastern European markets as the Czech Republic, Poland, Slovakia and Russia, in such Latin American destinations Argentina, Brazil, Colombia, Mexico, and Peru as well as in Nigeria, Egypt and Indonesia, whereas it is well above 100 percent in the US and UK. Demographic trends should also fuel foreign bank interest toward ramping up investments in emerging markets, where young populations, for example, will likely increase their per capita income over the next few decades. According to a Citi investment study looking at global trends out to 2050, Bangladesh, China, Egypt, India, Indonesia, Iraq, Mongolia, Nigeria, Philippines, Sri Lanka and Vietnam have the most promising growth prospects in terms of GDP per capita.

Furthermore, emerging markets present global banks with the opportunity to acquire operations in developing locales at lower market prices, and then to apply their management expertise to improve those operations rapidly, thus potentially achieving higher rates of return. One factor that supports this opportunity is a rapidly expanding professional class emerging in many developing nations. These individuals often possess advanced business degrees from leading international programs, and are eager to apply their expertise as seasoned, multinational banking executives to local operations back in their home countries. Critically, these local managers also possess an understanding of the nuances of regional culture and language. A common language provides a shared platform for understanding where more sophisticated skills and knowledge can be more efficiently and quickly transferred. Relying on local managers also reduces the need for acquired banks to relocate talent from the parent company.

Emerging markets can also offer a lower cost platform for global banks to do business, especially with lower wages which typically comprise at least 40 percent of a global bank’s cost structure. For example, compared with New York, average occupational wages are much lower in such attractive emerging banking markets as Hong Kong (43.9 percent of New York wages), Singapore (35 percent of New York wages), Buenos Aires (18.2 percent of New York wages) and Mexico City (10.9 percent of New York wages).
At the same time, emerging-market governments often are receptive to foreign investment as they seek out external financing for large-scale capital investments, such as with infrastructure and expanding telecommunication capacity. Consider, for example, that foreign banks are typically among the dominant institutions in the Czech Republic, Chile, Argentina and Mexico.

The growing volume of trade, payments, and communication flowing between emerging markets and the developed world has fueled increased interest in cross-border mergers and acquisitions. Trade between emerging and developing countries is projected to continue to expand rapidly over the next two decades. According to Standard Chartered research, trade between the European Union and China, for example, is projected to grow by nearly 13 percent CAGR through 2030, from $408 billion in 2008 to $5.6 trillion. For the corridor between the EU and Africa, trade is estimated to expand by nearly 14 percent CAGR for the same period. Inter-regional trade worldwide is projected to increase by nearly 10 percent CAGR through 2030.7

Payment flows between emerging and developed countries presents further opportunities for global banks. For example, the World Bank estimates that more than 215 million people, approximately 3 percent of the world’s population, live outside their countries of birth. To help boost the income of poorer households, these migrants sent back to their home countries $414 billion of which $316 billion, or 75 percent, went to developing countries. Over the course of the global financial crisis, the level of remittances being sent home remained steady. This migration of money serves as an important source of capital, trade, investment, knowledge and technology transfer. For global banks it provides them opportunities, for example, to expand mobile and electronic banking services.8
Despite undertaking a number of cross-border transactions, both banks have achieved a steady improvement in their respective efficiency ratios—the product of effectively transferring technology and innovation across borders, centralizing corporate functions and allowing for flexibility in managing local market circumstances. To sustain their growth momentum, especially when faced with economic challenges at home, both BBVA and Santander have more recently been investing in emerging markets outside of Latin America. BBVA has long appreciated the value of investing in high-growth emerging markets. For example, the bank recently increased its holdings in China CITIC bank to 15 percent while developing joint projects in private banking and car finance in Asia. It has also set up a joint company in credit cards with Bank of Baroda, an Indian bank with more than 36 million customers and 3,000 branches. In fact, after its recent purchase of a minority stake in Garanti, a leading Turkish bank, BBVA is projected to earn more than half of its net income from emerging markets, quite a contrast from 2000, when the contribution was 17 percent.

Citing a large, higher growth economy, a young population and low bank product penetration, BBVA views Turkey as one of the most attractive markets for retail banking looking forward. Its strategic location also provides BBVA an opportunity to better reach an estimated 400 million customers in neighboring countries, such as Russia and the Ukraine. Turkey’s role as a major trade corridor is underscored by the fact that Turkish exports to Africa, the Middle East and Asia over the second half of last decade rose well over 100 percent to each of those regions. Also, Turkey is still in the early stages of bancarization, the expansion of banking services to a market’s population which has lacked them in the past. BBVA’s experience with microlending and working with the unbanked in Latin America should help it to expand such services in its new markets.

Outside of its home market, Mexico is by far the largest contributor to the BBVA Group’s net profit, at 29 percent at year-end 2010, a decade after BBV Probursa merged with Bancomer to form BBVA Bancomer. Today the bank provides services to more than 16 million customers, manages the largest branch network in Mexico and has achieved top share in a number of product areas, including loans and deposits.
BBVA has also achieved particular success in Colombia, where it has generated long-term, growth and profitability. In 1996, BBVA acquired a 40 percent stake in Colombian bank Banco Ganadero, and by 2001 it had increased that stake to 95 percent. Through a focus on cost-cutting, technology modernization, and productivity improvements, BBVA has reversed several years of losses at Banco Ganadero. Between 2007 and 2009, for example, the acquired bank averaged a 22-percent return on equity.9

For its part, Spain’s Banco Santander, in 2010 achieved double-digit growth in its Latin American business. For the most recent year reported, it earned 43 percent of its profit in Latin America, including 25 percent in Brazil alone and 6 percent in Chile where, in the past decade, it has emerged as the leading provider. Today, Santander serves more than 40 million customers in the region via 5,882 branches and 27,550 ATMS. Customer delivery in the region is complemented by data processing centres located in Querétaro (Mexico), and Campinas in the state of São Paulo, Brazil.10

(Please see sidebars on the successful approaches of BBVA and Santander in managing their cross-border operations).

Of course, it is not only Latin America that provides attractive opportunities for global banks. Central and Eastern Europe also are rich with potential, as Austria’s Erste Group Bank AG can attest.
In 2000, Erste Bank acquired a majority stake in Česká spořitelna, the biggest retail bank in the Czech Republic and a key step in its quest to becoming the largest retail bank in Central Europe. Erste Bank's focus regarding this acquisition has been on achieving optimal group-wide coordination, improved market presence as well as regional and industry-specific customer service coverage. For instance, while local subsidiaries run their own retail and SME businesses, they are supported by group-wide platforms for regional business processes, such as retail cross-selling initiatives, that aim to ensure the adoption of best practices and the exchange of experience across the group. And, as BBVA sought to do in Colombia, Erste Bank also focused on achieving efficiency across its expanding regional footprint through the implementation of automation and efficiency-improvement measures.

By serving 5.3 million clients, via 667 branches and more than 1,300 ATMs, Česká spořitelna is still the dominant retail bank in the Czech market, with leading market share in client base, assets, deposits, retail loans and payment cards where it possessed a 36 percent share in 2010. It manages the largest electronic bank (via internet and phone) with more than 1 million SERVIS 24 customers. The bank has also achieved steady efficiency improvements, witnessed by a competitive 43.6 percent cost-income ratio by year-end 2010.

The Česká spořitelna story is just one example of how the Erste Group has been able to grow and boost its performance via cross-border acquisitions involving emerging markets. In total, the bank’s customer base has grown through more than 10 bank acquisitions in new EU member states between 1997 and 2008, to serve more than 17.7 million customers today: a far cry from the 600,000 it served nearly a quarter century ago.¹¹
Banco Santander has been very successful in cross-border deals. Accenture’s analysis reveals four elements of the bank’s growth strategy that drive this success:

Strategy
Santander’s global management model makes it possible for all of its acquired banks to stay focused on the group’s core business. As part of this model, all Santander banks have the same emphasis on retail and commercial banking, and enjoy global support in terms of risk management, technology, human resources, purchasing and other areas. At the same time, the model is executed by local teams, which are given the flexibility to make decisions about products, prices and priorities that make sense in their own markets.

Efficiency
Santander has a well-regarded approach to achieving efficiency across its global footprint, which it exports to any acquisition it makes. One aspect of this approach is its well-defined global business model, which emphasizes retail and commercial banking, staying close to local customers, and maintaining strict risk management and control.

Evolution
Over the years, Santander has enjoyed international success by growing business organically and through mergers and acquisitions, utilizing efficient technology, and developing distribution strength. In 1986, the bank started its national expansion strategy, first organically, and then inorganically through the acquisitions of Banesto and Central Hispano. From the mid 1990s, it also started an intense inorganic growth strategy in Latin America, acquiring more than 10 banks in 7 countries. Since 2004, Santander conducted several large acquisitions to drive growth in the UK, Latin America, and the US. Most recently, the bank has focused on blending its global management expertise with a robust emphasis on localization.

Execution
Santander’s strong culture of execution has enabled the bank to integrate newly acquired units rapidly while generating cost savings and increased revenue. In addition, the bank’s results-oriented culture gives freedom and autonomy to local managers while encouraging competition between units—resulting in innovative new approaches focused on success within each geography. Finally, Santander’s simple organizational structure creates clear accountability and facilitates quick decision making, which contributes to the power of its growth strategy.

These four pillars of Santander’s growth strategy clearly enable the bank to derive greater business value from its cross-border deals. In fact, for all the majority deals completed by Santander that were analyzed for this study, the bank was able to improve profitability in the first year, as well as achieve a greater level of profitability in 86 percent of the years following acquisition.
Over the past two decades, BBVA has successfully exported its way of doing banking across more than 32 countries. Accenture analyzes key elements of the bank’s organization and strategy that is supporting this expansion:

**BBVA’s global operating model**

BBVA’s operating model is divided into two main global platforms: 1) Global Retail and Business Banking (GR&B) and 2) Wholesale Banking and Asset Management (WB&AM). Generating a majority of the group’s revenues, GR&B is responsible for setting policy, driving operating synergies and disseminating best practices across the group. It also coordinates communication and functionality with Geographic Business Areas, which include Spain & Portugal, Mexico, South America, the USA and Asia. Each Geographic Business Area manages their own IT department that reports to both the global T&O and a local market/unit head. BBVA runs on two retail banking platforms: the ‘global’ platform for Spain (Plataforma Grupo) and Altamira/Alnova for all other geographies (e.g., Latin America, Portugal and the USA). IT support and software development is mainly provided from two hubs: 1) from Madrid for Spain and Portugal, and 2) from Mexico to support Latin America. USA is supported locally. Middleware and front-office hardware, however, is often supported by local markets.

In contrast to the GR&B platform, Wholesale Banking & Asset Management, managed from group headquarters in Spain, is a much more centralized structure to better manage the global needs of large customers.

**Exporting the “high performance” global business model**

BBVA has demonstrated that its “high performance” global business model can also be made to work in Latin America, and therefore, will be looking to export it to other emerging markets.
Conclusion

In an era of uncertain consumer incomes, increasingly burdensome regulation, and greater competition for deposits and customer share-of-wallet, where can banks turn for long-term, sustainable growth? For an increasing number of banks, the answer is cross-border mergers and acquisitions and, in particular, forays into emerging markets.

Recent Accenture research confirms the potential value of this strategy to both acquiring and target banks in terms of profitability and revenue growth. Indeed, many emerging markets are under-banked, and hungry for the products and services that are becoming commoditized in developed markets. In addition, stakes in emerging-market banks can be acquired affordably, and often bring with them a cadre of talented managers that have sophisticated training and education and are eager to apply winning strategies from leading global banks. Plus, the growing volume of payments between emerging markets and the developed world bodes well for the uptake of mobile and electronic banking services in developing countries. All of these factors can add up to considerable returns on investment.

At the same time, partnering with cross-border banks can involve increased complexity and some risk. As described, leading banks such as Banco Santander, BBVA, and Erste Group Bank illuminate the way forward, choosing innovative target banks with strong leadership positions in promising markets, while at the same time achieving efficiency gains. As these leading players demonstrate, cross-border M&A can be a powerful generator of sustainable growth and profitability, and, therefore, an accelerator of high performance.
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End notes

1. The performance data, as reported by Bloomberg, was made available through either the financial filings of local banking subsidiaries of foreign bank companies that continue to trade on a local stock exchange or through annual filings required of the subsidiary by the local regulator.

2. Defined as operating expenses divided by net revenues, as calculated by net interest income plus non-interest income.

3. As defined by the financial performance of the local banking institution a fiscal year following its acquisition by a foreign bank.


9. BBVA Group financial filings and investor presentations, November 2010.


11. Česká spořitelna 2010 annual report; Group fact sheet, March 2011; Group history sheet May 2011; and Dow Jones, 4 January 2011; Erste Group Bank AG financial filings and investor presentations.

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