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“HSBC and its organisational change”

Student ID: 140007842

Lecturer: Dr Gladius David Kulothungan

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Introduction

The Hong Kong and Shanghai Banking Corporation (HSBC) have been through significant changes in its banking structure in the last few years. From revolution and economic crisis to starting the ring-fencing in the UK. These all resulted the bank to change its business structure and shift its business model to comply with these changes.

HSBC since its opening has expanded rapidly in becoming one of the largest financial services in the world (HSBC, 2012). It started by providing commercial retail services to its clients and structured its business model to meet its customer demand (O'Connor and Walter, 2013). In 2003, HSBC introduced managing for growth strategy aimed at providing better trading, advisory and underwriting services to its clients (Buerkly, 2004). However, social cultural clash and lack of patience resulted the company to fail in achieving its objective (O'Connor and Walter, 2013). Add to that economic crisis of 2007-8 resulted HSBC to change its structure decreasing its involvement in complex trading activities (BIS, 2018).

Also, according to the Financial Services (Banking Reform) Act 2013, UK's large banks started separating their retail banking sector from investment banking (HSBC, 2017). This is known as "Ring Fencing"¹. As a result, large banks including HSBC have significantly changed their structure and business model (BRITTON, DAWKES, DEBBAGE and IDRIS, 2016).

Since 2015, HSBC has started to build an independent institution and established a new ring-fence bank name "HSBC UK" with head office in Birmingham for their personal and its commercial customers (HSBC, 2017). This resulted HSBC to separate its retail banking² from investment banking³ having separated deposits from UK individuals and small business in the ring-fence. The creation of "HSBC UK" was one of the largest projects the company ever experienced before (HSBC, 2017). This resulted the bank to reconfigure core banking payments and platforms infrastructure, transferring bank accounts to new HSBC sort codes, change in company business model and rebranding all UK store branches to HSBC UK (HSBC, 2017).

¹ UK Ring-fencing please visit, <https://www.hsbc.co.uk/1/2/ringfencedbank>

² Also known as consumer banking providing services including checking and saving accounts, personal loans and mortgages.

³ Financial service company that provides advisory-based financial transactions on behalf of its customers and individuals.

This report examines HSBC that has been through significant changes in the last few years. It will analyse the change programmes applying appropriate models and theories and organisational changes that the company experienced above. Thus, first this report starts by providing an overall introduction of HSBC and its business model. Then, the report will describe organisational changes and how HSBC has affected. Next, the HSBC's strategy and change programme will be analysed and examined. Finally, we will conclude stating key outputs from this report.

HSBC History and Its Business Model

The HSBC was established in 1865 in Hong Kong (O'Connor and Walter,2013). HSBC was the inspiration of Thomas Sutherland aiming in creating a local bank in Hong Kong and the China coast with the idea to serve commercial services, globally (O'Connor and Walter,2013). Soon after its opening HSBC developed network of representative offices and agents all around the world as far as North America and Europe (O'Connor and Walter,2013). Now, HSBC is one of the world's largest bank with total assets of \$2.558 billion and around 3900 representative offices in 67 countries, globally (HSBC, 2018).

HSBC since 1865, has experienced different changes including revolutions, economic crisis, and new technologies and has learned to adopt to changes (O'Connor and Walter,2013). These resulted HSBC to develop core strength of resilience, innovation and adoptability (HSBC, 2012). HSBC's ownership structure constitutes of various branches in Asia, Europe, Latin America and North America which all comes under control of parent company "HSBC Holding PLC" (O'Connor and Walter,2013). The company's core strategy is to build long-run customer relationships, control its cost and strength its capital (HSBC, 2012). Since, then the company is reshaping and expanding through targeting developing countries and focusing on global business (HSBC, 2012).

This report will run PESTEL Analysis to analyse and monitor the factors impacted HSBC to change its organisational structure. The PESTEL Analysis is a useful method in identifying factors in their environment which have an impact on their operations (FME, 2013). The PESTEL analysis can be used to look at Political, Economic, Social, Technological, Legal and Environmental issues (FME, 2013).

HSBC Organisational Changes

Managing for Growth (Social)

HSBC with its rapid growth since its opening, in 1998 launched a five-year strategy to further enhance its shareholder value “managing for Value” strategy (Hutchison, 2004). After successful implementation of above strategy, the company introduced “managing for Growth” strategy aimed in becoming one of the largest financial services providing investment banking business (O’Connor and Walter, 2013). The bank due to its strong relationship in commercial banking and brand reputation believed to become successful in this sector. This made HSBC to mix its structure with its retail banking to meet its customer demands and maximise its profit.

Figure 1 illustrate HSBC business mix which clearly shows that HSBC has rapidly expanded its corporate & Investment Banking from 53 percent to 75 percent from 2006 to 2015 (Onaran, 2016). While, its consumer banking has decreased from 42 percent to 23 percent (Onaran, 2016). This suggest that the company saw the profit opportunity and started to invest massively in this sector.

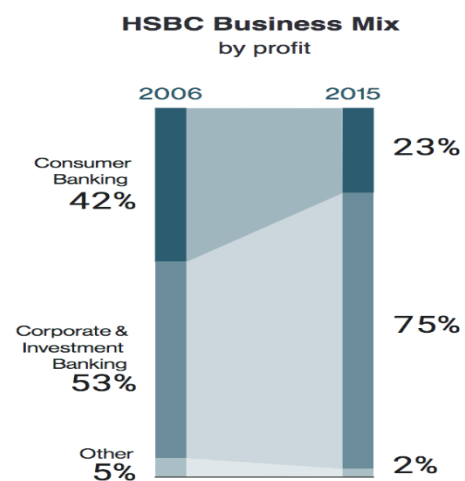


Figure 1 HSBC Business Structure
Source: Bloomberg - Citigroup, HSBC (2015)

Despite its expansion, HSBC failed in achieving its objective in becoming a top rival in global investment banking due to social issues of the organisation (O’Connor and Walter, 2013). Organisations cultural clash and lack of patience were found to be the main reasons behind the failure. In 2013, HSBC hired new 2000 corporate advisory investment bankers (Kynaston and Robert, 2015). However, due to big cultural shock of new recruiters to adopt with HSBC culture and its new investment bank sector resulted the company to make a huge loss (Mollenkamp, 2006). Also, the lack of patience from the management resulted the company to scale back from its objective in 2015 while analyst believed HSBC needed more time till its investment banking mature (O’Connor and Walter, 2013).

Ring-Fencing (Legal)

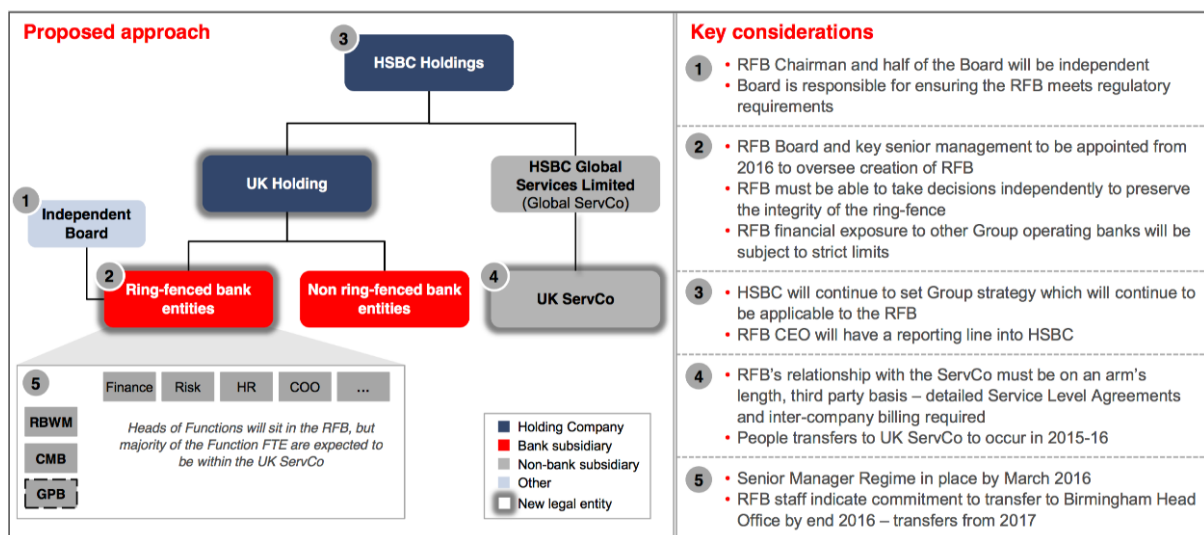
In 2013, the UK's Independent Commission on Banking (ICB) proposed that by 1 January 2019 UK financial services with more than £25 million in deposits for a three years period must separate their retail banking services from their investment and wholesale department (BRITTON, DAWKES, DEBBAGE and IDRIS, 2016). This was proposed aiming to protect retail customers in a wake of another financial crisis. Through this law, two key legislation needed to be achieved; first to separate retail banking from non-ring-fenced parts of the banks and second to hold extra capital in banks' balance sheet and the ability to absorb losses (BRITTON, DAWKES, DEBBAGE and IDRIS, 2016).

This process has resulted in major influences for the banks and the market due to change in regulations. For the banks, the increase in cost due to establishment of new rules and legal entities (HSBC, 2017). The change resulted investment banks to not generate revenue from retail banking as before, thus business models as well as other operating functions must be changed to fit with the reform. Also, customers will be disrupted due to changes in banks terms and condition where their information, account details and services will be changed (BRITTON, DAWKES, DEBBAGE and IDRIS, 2016).

One of the key reasons of structural change is regulations. According to Cook, Shortell, Conrad and Morrissey (1983), regulation is a type of cost that restrain organisations resources and threatens their existence. Thus, the nature and scope of regulation has significant impact in an organisation. HSBC was involved in significant changes from the Financial Services (Banking Reform) Act 2013. To evaluate its impact on the bank this report provides a model "Compliance with Social Legislation (CSL) Model" by Greer and Downey (1982). This model discussed organisations behaviour to restrain forces and if not addressed then consequences and penalty may be enforced. After the financial crisis and introduction of ring-fencing rule HSBC started to change their business model to separate two division of Retail and investment banking (BRITTON, DAWKES, DEBBAGE and IDRIS, 2016).

Since 2015, HSBC started by establishing a new ring-fence bank called "HSBC UK" and the set-up process completed on 1 July 2018 where the legal transfer of businesses and customer accounts took place (Charley, 2017). The new ring-fenced bank serves 14.5 million both business and personal customers, including HSBC all

retail customers in the UK, first direct customers and M&S banks, HSBC most commercial banking customers and private bank clients (Competition & Markets Authority, 2015). In the non-ring-fenced bank, HSBC Bank Plc has been operating targeting all global banking & markets customers within the investment banking division and other relevant financial institutions including UK corporate customers, as well as customers of branches in non-UK countries, as shown in figure 2.



Source: HSBC Ring-fencing Bank Brochure (2017)

	2016	2015	2014
HSBC Holdings Plc	1.82	7.68	7.63

Table 1 HSBC Return On Average Equity

Source: Orbis Bank Focus database

HSBC Simplification of Business Activities (Economic)

The rapid expansion of banks and their activities resulted in enhancement in banks' balance sheet and involvement in certain complex activities (BIS, 2018). One of the main reasons found to be triggered the 2007-8 financial crisis were the complexity with banks commercial and investment banking (BIS, 2018).

The 2007-8 financial crisis resulted in evolution of banking sector. Banks started to change their market capacity and structure and shift their business models (BIS, 2018). The crisis ended strong growth period for the banks in advanced economies. This was mainly due to reduction in business volumes of firms (BIS, 2018). As a result, banks started to expand their business in countries where they were less affected by crisis including large emerging markets (BIS, 2018). Also, banks in developed countries started to change their business model in away to reduce their trading and complex activities and moved towards less capital risk activities including commercial banking (BIS, 2018). This is evident in changes in banks asset portfolio, increase in dependency of customers deposit funding and revenue mix (BIS, 2018).

In the market, the asymmetric competition as some banks with weak retail banking will be affected negatively (Charley, 2017). Banks such as LLOYDS which has a small-scale investment bank will face fewer challenges than HSBC (Charley, 2017). Thus, this results on some banks to incur massive costs which results in lower profitability and default risk (Charley, 2017). The rule also demanded banks to simplify their structure due to the complexity of banks activities. HSBC then started to shift its business model structure moving away from trading and complex activities towards commercial banking activities which requires less capital (HSBC, 2017). Figure 3 shows HSBC bank balance sheet composition showing its re-focus on home market business and retail banking.

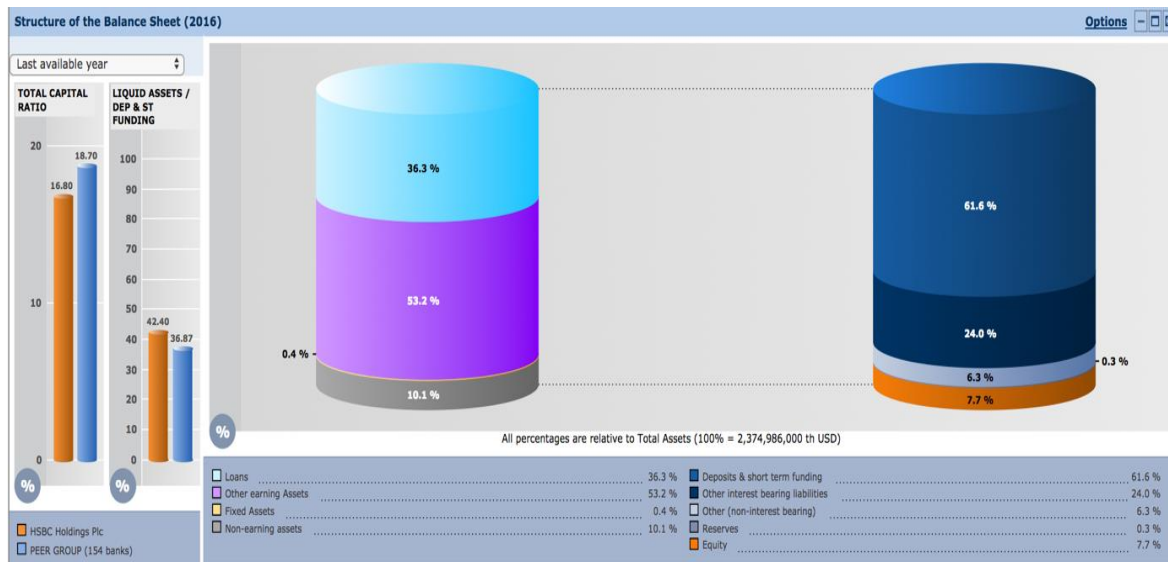


Figure 3 HSBC Business Model Structure 2016
Source: Gakovic and Yardley, 2007

HSBC and Technology (Technological)

In the last few years, HSBC is facing significant competition pressure due to evolution of the financial service industry (HSBC, 2018). There is a rapid increase in the number of fintech companies that provide the financial services to businesses and individuals (EFMA, 2018). Due to less stringent regulation, they are able to provide their services more efficiently and cheaper (EFMA, 2018). Now, new peer-to-peer platforms promotes new decentralised banking where confidentiality and security can be ensured relying on blockchain (FINEXTRA, 2018).

This resulted HSBC to see the opportunity and launching new digital propositions to explore further the open banking to provide additional value-add and better customer service to their clients (HSBC, 2018). For example, HSBC has recently launched a new app in the UK called Connected Money (EFMA, 2018). This digital app allows customer to access and manage their money in a simpler way. In 2018, HSBC reported its strategy in investing on online and mobile banking aiming to improve its customers banking experience and build upon machine learning (HSBC, 2018).

Technology and innovation also resulted HSBC to change its structure and business model. Now, HSBC due to rapid expansion in digitalisation and blockchain reducing its physical branches and increasing its investment in technology (FINEXTRA, 2018). In 2018, HSBC Chief Executive John Flint announced the bank strategy to invest between \$15-\$17 billion in new technology as part of the new growth strategy (FINEXTRA, 2018). They hope that new investment will help in achieving a return on

equity (ROE) of 11 percent by 2020 (FINEXTRA, 2018). In 2017, HSBC shut 117 branches across the UK and rules out on further closures in the next few years. This was due to the rise in internet as chief executive John Flint said on 2018 (This Is Money, 2018).

HSBC is currently on a digital transformation to avoid falling behind from its competitors. One of main problems HSBC is facing through is digital transformation is security and trust (HSBC, 2018). According to HSBC survey in 2017 of 11 different international markets, found that the lack of understanding and trust holding back the adoption of technology (HSBC, 2018). However, despite the drawback technologies are moving towards security too. The CEO of SoftBank Masayoshi Son in its statement stated that one of the main concerns of future technology is security and hacking. Thus, now technological companies are working hard to increase the security to minimise and eliminate the concerns regarding this matter (Lunden, 2016).

Political risk and HSBC banking structure (Political)

Since 2015, due to the uncertainties and political risks around UK leaving the EU (Brexit), HSBC is looking over bank's structural review (Pratley, 2015). In 1998, HSBC moved its headquarter to London with purchase of Midland Bank due to the lack of democracy in China and its rules (Pratley, 2015). Now, after Brexit HSBC is on structural review on positioning its location of holding company to maximise shareholder value.

HSBC decision in moving its headquarter to Hong Kong might save them £750 million a year on the bank levy and the Hong-Kong post-handover experience may have softened the bank's decision on relocating to Hong Kong again (Pratley, 2015). However, worries are still the same for future and whether they would be able to enjoy the democracy they have in UK (Akmen, 2018). However, at the same time the uncertainties around Brexit and losing the EU market may result in call for review structure.

In 2018, HSBC called to move its seven offices from London to Paris due to uncertainties around Brexit (Akmen, 2018). These seven offices will take the responsibility to deal with bank's activities in Spain, Italy, Netherlands, Belgium and the Republic of Ireland (Akmen, 2018). They will be transferred from subsidiaries of HSBC UK to HSBC France (Akmen, 2018). These were due to problems that HSBC believed Brexit will bring after UK leaving EU.

Also, HSBC in London has shifted its ownership of its Irish and Polish subsidiaries from its London based entity to its French entity (White, 2018). This will be the same for seven other branches (White, 2018). This move aimed in ensuring HSBC can continue to serve its customers in the Europe (White, 2018). This resulted in change in organisational structure in HSBC Europe and UK branches. Now, due to uncertainties around a “No Deal Brexit” HSBC has been organising its business to continue to serve its customers in Europe as before (White, 2018).

HSBC Environmental Issues

In our rapidly changing environment, we observe the biggest environmental threat in human story and it's the effect of climate change. HSBC structure and strategy are changing to improve their sustainability and invest in project to promote sustainability growth (Makartoff, 2019). HSBC now see the threat and started to invest in benefits of green and blue urban areas globally, empowering employees in becoming sustainable and adopt its business culture to answer the challenges of our climate that is rapidly changing (Makartoff, 2019).

According to Alex Base, HSBC's Global Head of Operational Sustainability, HSBC has recently launched Sustainability training Programme (STP) aiming in teaching its employees to explore sustainable finance and the HSBC's leadership role to empower individuals in taking actions within their day to day activities (Makartoff, 2019).

Conclusion

This report examined and evaluated HSBC bank which has been through in significant changes in the last few years. From, its strategy in expanding its investment banking, structural changes due to economic crisis, ring-fencing as well as technological and political changes.

HSBC, in 2003 to enter and expand its business has invested massively in investment banking to meet its customer needs and maximise its profit. This has resulted the company to mix its business structure and business model with retail banking. However, due to social problems including cultural clash and lack of patience resulted the bank to fail in achieving its objective.

The 2007-8 economic crisis has made majority of banks including HSBC to reduce their involvement in complex activities and moved forward towards the retail

commercial banking. This was due to reduction in deposit money from the individuals which has significantly affected the banks. As a result, HSBC in its strategy change its structure and business model focused more on commercial banking.

Following that, in 2013 as part of the Financial Services (Banking Reform) Act 2013 and introduction of ring fencing where banks in UK had to separate their retail banking from investment banking. This was to reduce banks risk from default in awake of another financial crisis to secure depositors' money. HSBC started to change its structure and in 2018 successfully separated its two sectors under HSBC UK. This was a huge cost for the bank as they had to change the payment and platforms infrastructure having to change around 400,000 IT, rebranded all its UK branches and opened it headquarter in Birmingham.

Also, the uncertainties around political risk and Brexit has resulted the bank to change its strategic model and business structure. HSBC is currently under review on changing it headquarter to Hong Kong to reduce its risk exposure from UK leaving the EU. In 2018, HSBC already relocated its 7 branches to Paris to provide its services to its EU customers.

Finally, the technological advancement has resulted the HSBC to continuously change its structure to meet its customer demands. The introduction of blockchain and new innovations including fintech companies resulted in a competition in the market. HSBC is now continuously evolving itself to meet with new technological advancement to value-add its products and provide better services to its customers.

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