Financial Services

Observations

After the highs of 2021, the financial services sector registered a 43% YoY drop to $673B worth of deals in 2022, the lowest value seen in the past five years. Deal volumes also saw a YoY decline of 15% to 8,589 transactions in 2022.

Europe was the most active region in terms of deal value with 2,973 transactions, followed by North America (2,579 deals) in 2022.

Inflation hampers norlife profitability even while boosting prices and top-line growth. The insurance sector should be looking to use M&A to broaden its historical focus from risk and cost reduction to prioritize ongoing innovation, competitive differentiation, and profitable growth.

In the short term, the banking sector is likely to reap benefits from interest rate hikes and higher savings; over the long term, the sector will need to pursue new sources of value beyond product, industry, or business model boundaries. This is likely to drive divestment of noncore assets and investments in new applications for ESG, embedded finance, and digital/fintech assets.

Investment management firms are likely to continue investments and acquisitions in digital transformation with new technologies that improve the client experience, gain operational efficiencies, and potentially generate alpha returns.

Deals volume
Banks are shifting toward integrated cross-selling opportunities. Regulatory convergence is increasingly viewed as a means to increase scrutiny from clients, regulators, investors, and employees on companies’ ESG commitments. This will affect business models for financial institutions.

Growth investments
Banks need to establish alliances outside of their core sector with players from technology, retail, health, and others to cross-sell new services to a wider customer base, introduce new capabilities, and improve utilization of their current assets.

Growth will be required to deliver more stable return on equity (ROE). Divestment of noncore assets from their portfolios, resulting in a skewed balance sheet with legacy products.

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Forces shaping “new normal” conditions

Skewed balance sheets are resulting in declining ROE
• Banks have divested noncore assets from their portfolios, resulting in a skewed balance sheet with legacy products.
• Growth will be required to deliver more stable return on equity (ROE).

Stakeholders demand ESG commitments
• Increased scrutiny from clients, regulators, investors, and employees on companies’ ESG commitments will affect business models for financial institutions.

Regulation will continue to influence the market
• Regulators are expected to respond to rapid developments in the sector with the introduction of new rules, especially in the areas of digital assets, climate, and financial inclusion.
• Regulatory convergence is increasingly desired by central bankers and could have a major impact on competition and market strategies.

Digital assets, blockchain technology, and cybersecurity are increasing in importance
• The introduction of new, disruptive products and technologies has led to banks investing heavily in new technologies and creating alliances with partners that have broader digital capabilities.
• Banks are shifting toward integrated platforms and cloud solutions to improve cybersecurity and enhance analytical capabilities.

CEO priorities

Business model impact

Medium-term responses

1. Cross-selling opportunities
Banks need to establish alliances outside of their core sector with players from technology, retail, health, and others to cross-sell new services to a wider customer base.

2. Growth investments
Banks also need to consider acquiring high-growth, innovative businesses in areas like cybersecurity, fintech platforms, blockchain, AI, and others in adjacencies that could, in time, become the new core.

Short-term responses

1. Divestment of noncore assets
Companies could consider divesting underperforming loan portfolios and noncore divisions to raise capital and improve efficiency.

2. Technology-led business transformation
Investments and acquisitions of new technologies (e.g., digital payments, e-trading platforms) will be critical to position banks to compete in the future.

3. Building resilience
Defensive M&A strategy

4. Unlock value from the ecosystem
Accelerate business model transformation

5. Change the game
Growth investments
Pressure on growth is forcing insurers to...