

‘The Future of Business and Banking: Is the West getting left behind?’

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Michael Geoghegan, Group Chief Executive, HSBC Holdings plc
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Thank you and good afternoon ladies and gentlemen.

I'd like to start with an observation that I've made time and again during my 37 year career. It is this. Experts are terrible at predicting the future.

I'm sure it was with her usual iron certainty that Margaret Thatcher predicted in 1969, 'no woman in my time will be Prime Minister'. And who could doubt Ken Olsen, when he said eight years later, 'there is no reason for any individual to have a computer in their home'. After all, as the inventor of the minicomputer, he would know.

From social to technological change, we always seem to underestimate the speed of development. But as a businessman and a banker, I think the most dramatic revolution many in the West have miscalculated, is the rapid rise of the world's emerging markets.

As the Group CEO, it is my duty not just to read reports but to understand what is happening locally around the world. So far this year, I've spent over four months on the road. I've visited around 40 countries on six continents. And I've become even more certain that the world's economy is changing. Faster than ever.

In May, I gave a speech in Venice and it brought it all home to me. Venice's 16th century glorious past as the centre of banking has vanished, and it is now no more than a water attraction.

Today the world's centre of economic gravity is unmistakably shifting again. And this time, it's moving towards the East and South. The financial crisis has accelerated things. And the G20 has come of age. Could what happened in Venice now happen to other financial centres around the world? Today, I'd like to take you on a brief tour of the world's emerging regions. Because I firmly believe

that, only by understanding what's happening there, can we ensure that the West doesn't get left behind.

As HSBC's first Group Chief Executive to be based in Hong Kong for 17 years, it seems right to start with Asia.

So, first of all, let's look at China – the home of tomorrow's largest middle class.

Most now agree this will be China's century. We expect China's total trade flows with the rest of the world to grow by some 13 per cent a year over the next five years, to 5 trillion dollars. And I believe the renminbi will become one of the world's top three trading currencies much sooner than many realise.

Even less well understood is the speed with which China is transforming itself from export to retail market.

Here are a few facts.

China has 717 cities with over half a million people.

Over the next five years, its middle class is expected to almost double – from 172 million to 314 million people.

Already consumer behaviour is changing. The Chinese bought more cars than the Americans in 2009, while in the first half of this year, BMW sold more cars in China than the UK.

It goes without saying that many Western businesses have put China at the heart of their strategy. But I'm not so sure that they are moving deep enough, and fast enough – beyond the gateways of Beijing and Shanghai.

China's wealth is becoming increasingly diverse and dispersed. One of the things I've noticed since returning to Hong Kong is the blue sky. Before, the skies were full of smog and the pollution of the factories across the border. Activity has now moved inland. Production and infrastructure development is moving across all of China.

Within the financial sector, things are also changing. Shenzhen is a city of more than ten million. It is now ranked within the top 15 global financial centres in terms of its competitiveness. Yet few in the West had even heard of it a few years ago.

For as long as I've been at HSBC, it has been the leading international bank in China. We are steadily increasing our presence across the country, as fast as regulations allow. We have 102 outlets in 25 cities. And for any company, building out in this way will be vital to reach the Chinese consumers and businesses of tomorrow.

I'd now like to touch on India, one of tomorrow's biggest sources of human capital.

Over the medium term, I think India is going to deliver even faster growth than China. Sure, India has its problems. And you can see in the press the teething problems with the Commonwealth Games. But its fundamentals are also very strong.

India is committed to improving its infrastructure. Earlier this year, India's finance minister called for a doubling of infrastructure spending to 1 trillion dollars by 2017. What's more, India's economy is already much less dependent on exports than China – and more dependent on domestic demand.

But perhaps the biggest reason I'm convinced India will succeed – despite its constraints – is its people.

Asia has taken education and has invested in it. And nowhere are the results more apparent than India. The country has a population of 1.2 billion, and unlike China, it's growing. India churns out a staggering 2.5 million graduates a year. Most of them are fluent in English. And today's Indian graduates will be tomorrow's global business leaders.

The lesson we all need to understand is that you can't run a global organisation with one people strategy. You need to recognise that the challenges of attracting and retaining people in markets like India are different to the West. And that, in emerging markets, it's not salary and benefits, but career development, that's the number one driver which attracts a person to a job – and keeps them there.

And let's be clear – if companies like ours fail to harness this talent, there are now plenty of domestic and regional companies that will.

Next, we're off to Latin America, a market at the heart of tomorrow's south-south trade routes.

Latin America used to be seen as a hotbed of instability. Certainly that was the case when HSBC sent me to Brazil to take over a failing bank in '97.

How things have changed in a decade. Our Brazilian bank is now one of the best-performing of the Group.

Brazil has gone from basket case to bread basket. And there's now a wide grouping of other countries in the region all on a sustainable growth path. Along with Brazil, I'd add economies like Argentina, Chile, Colombia, Peru and Mexico. These nations aren't going to return to the days of 'coups and colonels'.

But the lesson I really want to draw out of the narrative in Latin America is the accelerating 'south-south' story. All emerging regions are doing more business with each other and are less dependent on the West. And it's in Latin America that I've really noticed the speed of change picking up.

Brazil's trade surplus with China has tripled to around 15 billion dollars in four years. Chile has seen a similar trend, supported by its copper reserves.

Now direct investment is following the same pattern. China was the biggest foreign investor in Brazil in the first half of this year. And just recently, two Chinese state oil firms have offered

seven billion dollars for a stake in a Brazilian energy start-up company.

One of the core reasons I moved to HK was to build links between Asia and regions like Latin America. And at HSBC, we are now seeing our business flows increasing between the two regions. We have relocated Chinese bankers to Brazil and moved Brazilian bankers to China so we have expertise in all the right places.

At HSBC, we know that tomorrow's winners will be those who start to follow the south-south routes today.

Continuing the world tour, I'm moving on to Turkey, tomorrow's bridge between Europe and the Middle East.

Let me say a few words about the Middle East first. HSBC has been working in the region for more than a century, so we know the region better than most. It's also where I began my career in the early '70s.

With all the attention the BRICs have been getting lately, I think the Middle East has been overlooked. But I believe all the ingredients and elements for success are still there. A growing population, a talented workforce, an international outlook, and of course massive hydrocarbon resources.

And recovery is now underway in the Emirates. In fact, in a sign of confidence, Dubai has successfully gone back to the international markets to raise fresh funds.

So all the evidence suggests the Middle East will play an increasing role in the global economy. And I believe that deepening our ties with Turkey will be our key to unlocking the Middle East's potential.

Turkey is a market which has been very successful for HSBC recently. And every time I visit I'm struck by the country's growing influence across the wider region. In fact, I believe Turkey has the potential to revolutionise Europe's relationship with the Middle East.

Candidly, I'm perplexed by those who see Turkey as a threat to European Union. With Turkey as a member, the EU would only be stronger. And now, more than ever, the EU cannot afford to pull up the drawbridge. Take the UK as an example. Almost half this country's exports still end up in the rest of Europe. But with anaemic growth there, where is the demand going to come from in the future?

So I believe it is in all our interests to see Turkey's at the heart of tomorrow's Europe.

Next, I want to talk about Africa: tomorrow's new emerging region.

Africa must be the least researched of the world's markets. But that's one of the reasons why we and other brave investors could find some of the best opportunities there.

Africa is still ten to 20 years behind Asia as a consumer market. But there's an interesting dynamic right now. We have moved from a period in which the West supported Africa through aid, to one where emerging economies are actively investing in its future.

Of course, you could take the 'Sarah Palin approach' to Africa. But it's not one country, or even one homogenous market.

What marks out North Africa is its influence throughout the Middle East – through cultural links and a diaspora across the wider region. And at HSBC, we already have a strong presence in markets like Egypt, which we are committed to building.

But it's what's happening in Sub-Saharan Africa that I'm most excited about. This is the one emerging market where HSBC has been under-represented until now. So we've been looking closely at the opportunities there.

You may have read that we've entered into exclusive discussions with Old Mutual about a majority stake in Nedbank, South Africa's fourth largest bank. The deal isn't done yet, but it would be an exciting opportunity for HSBC.

And candidly, this is the time to act. Because you can see the increasing influence of China, Brazil and India across the region – including in the financial sector.

Western-based companies are now catching on too – like Wal-Mart, which has just offered more than 4 billion dollars for one of South Africa's biggest retailers.

Provided that all of this is matched by a commitment to social development, it could bring real change for the people of Africa. And I can't now imagine a world in which they won't have a role to play.

Indeed, as this highlights, tomorrow's growth stories won't just be found in the BRIC countries, but in a whole new generation of emerging economies.

And the name I want to give you today is the CIVETS, named after the cat-like animals found in many parts of the emerging world.

The CIVETS are Colombia, Indonesia, Vietnam, Egypt, Turkey and South Africa. They have large, young, growing populations and dynamic and diverse economies with improving education standards. And each is relatively politically stable.

In summary, this decade will see the world divided into the HIICs and the HOGGs. The 'Heavily Indebted Industrialised Countries' of the West will be the relative backwaters of growth. It is the 'Higher Opportunity, Greater Growth' markets in the East and South that will hog the limelight.

So where does the West go from here?

Above all, it needs to take a long hard look at its competitiveness.

First, we need to reflect on asset values. On my recent staff roadshow to 26 countries, I noticed that only two countries had 'positive money', that is where interest rates were higher than inflation. And they were Brazil and Panama. Until that changes, I don't believe we will get a floor on asset values in the West. We will just keep supporting false markets.

Second, we need to change our mindset. Western companies, particularly in the services sector, need to think differently if they are to make their skills indispensable in servicing the world's new trade flows. Not least, I believe they need to travel more, and to go and live in these markets – as I did. As a nation, the UK also needs to invest in language learning. If we fail to do this, we will simply lose out as business starts to by-pass traditional Western hubs.

Third, we need to make it easier to do business in centres like London and New York, not harder.

The latest research shows that Hong Kong and Singapore are now joining London and New York as truly global financial cities. Above all, the West needs to make sure it doesn't regulate itself out of the financial services business. Let me explain.

Perhaps our greatest lesson we learnt from the crisis was the need for governments and policymakers to work more closely together. Recent months have reminded us that achieving common regulation between different jurisdictions will be extremely difficult. But not impossible. The agreement by the Basel Committee on capital requirements for banks is a good example of what can be achieved when we put our minds collectively to it.

But with such a wide range of different proposals for banking reform on the table, it is critical that policymakers continue to work together.

From levies and taxes to the shape and structure of banks, unilateral policy responses can create obstacles to fair competition. And they ultimately hurt the consumer, by reducing choice and increasing costs. And they can have unintended consequences on the wider economy too. Capital is mobile, and it will go where it can be allocated most efficiently. People are mobile too, and if firms move their activities, some economies could suffer real long-term damage.

Take the debate on the size and structure of banks. It's a very important one, and I'm sure we all recognise the public and political pressure surrounding the discussion in some parts of the

West. But we need to make sure our policy decisions are based on empirical evidence and not simply emotion.

There was no common denominator of size or shape among the banks which failed in the West. Many were relatively small, and the casualties were widely spread. In the UK, the first run on a bank for 100 years happened at Northern Rock, a small lender with a simple business model, built around a residential mortgage business.

If any economy ends up with a financial sector where banks all look the same, then a crisis could more easily take out every institution in the marketplace. We could end up with more individual failures, not less. And all this would have a disastrous impact on the economy.

The financial system benefits from banks that are 'big enough to cope.' Diverse business models can enhance returns for shareholders. They can mitigate systemic risk. And as a result, I believe they can aid financial stability. I believe that HSBC's results throughout the crisis prove this – we remained a profitable and diverse Group that never needed taxpayer money anywhere in the world.

So what matters is not size, but risk. Our focus must be on making banks safer, not smaller. Issues of bank structure are not best tackled by trying to legislate what banks can and cannot do, but through capital requirements and enhanced supervision.

In conclusion, I'd like to say a few words about the UK. I'm certain the City of London can continue to bring huge value to the process of economic development – not least in emerging markets.

But uncertainty is currently the biggest risk to the City's competitiveness. If the UK is to play its part fully, we need to ensure that, with a new government in place, we develop and adopt clear and consistent policy on regulation and the business environment.

If, as some suggest, damage has been done to London's perceived competitiveness since the crisis, this need not be irreversible. But equally, we

must not ignore the signals and hence damage it further – whether because of unilateral policy decisions or benign neglect, and so it is vital that all of us play our parts in the debate on the future of the City of London.

Thank you for listening.