RBS restructuring plays on its strengths in capital markets

On 12 January 2012, RBS released preliminary detail of its long-awaited restructuring plan for the Global Banking & Markets division. In summary, over the next three years, RBS will exit cash equities, corporate broking (Hoare Govett), ECM and M&A; the combined income of these units – which RBS says were unprofitable at the time of the announcement - totalled £220m in 9m11. Going forward, RBS will focus on fixed income, FX, debt financing, transaction services, and risk management solutions.

We readily acknowledge that selective exit from businesses is far from easy. There are successful precedents - BZW of old being probably the most relevant example here – but RBS' challenge is arguably greater, not least due to the shifting regulatory landscape, including the UK-specific 'ring-fencing'. That said, our initial view (the bank may release further details with the FY11 results, on 23 February 2012) is that this restructuring could well result in a significantly more competitive capital markets offering, as it emphasises the RBS' considerable existing strengths:

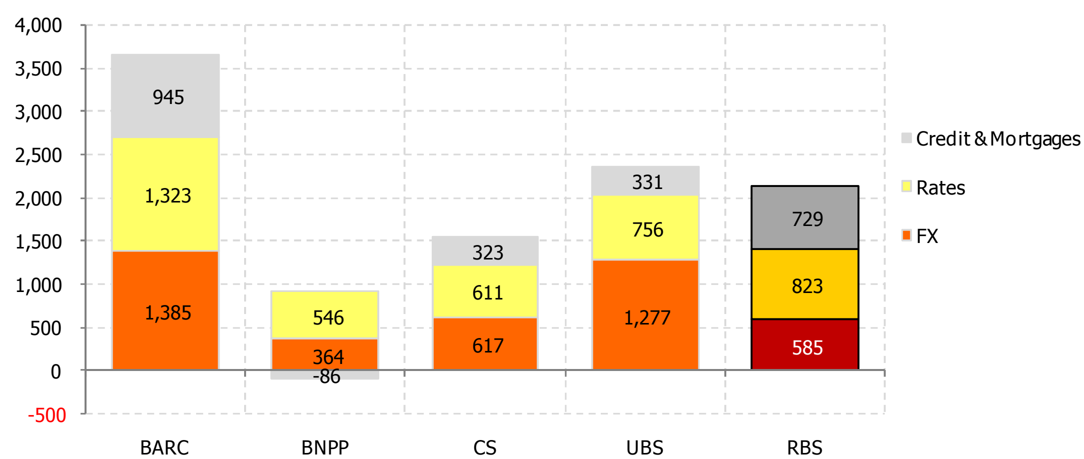
- An efficient FX business that capitalises on cross-divisional FX activity across the RBS group;
- A strong G10 Rates business which includes inflation expertise, an enviable corporate client portfolio, and synergies with leveraged and project finance business units; and
- A well-established retail structured products revenue stream from both Rates and Equity derivatives; we hear this unit has significantly increased its client footprint in Asia in recent times.

The Credit business has historically been less strong than the businesses above. However, focused as it is on flow business, it has avoided the losses in exotic credit sustained by some of its peers. Mortgages are comparably strong, but the future of this market area remains uncertain: e.g. industry wide RMBS revenues waned in 2011.

We expect the integration of the debt origination units with the international component of Global Transaction Services will create an interesting and competitive new model. While banks such as J.P.Morgan and Deutsche Bank have been taking steps to mine the synergies between investment banking and transaction services, the primacy of M&A and ECM business has prevented full integration. We estimate 9m11 revenues for this combined unit (excluding loan portfolio management) to be in the region of £1.8bn.

Below, we provide our initial benchmarking estimate of the new FX, Rates and Credit & Mortgage businesses for RBS and four of its peers. Netting 9m11 global revenues and normalised front office salary & benefits (this being the single largest and most readily product-attributable cost component) highlights RBS as a relatively strong performer, even in this difficult trading period.

Revenue net of front office staff cost: 9m11 (TRIC product definitions, post-writedowns, £m)



Source: Tricumen

Notes & Caveats

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