New City Agenda

Antony Jenkins: Turning Values into Value

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Introductory Remarks

Peter Vicary-Smith

Group Chief Executive, Which?

Good morning. I would like to introduce the people up here. First of all, I am Peter Vicary Smith; I am the Group Chief Executive of Which? On my left are Lord Sharkey and Lord McFall, who, you all know, are two of the three Chairs of New City Agenda, along with David Davis. On my right is, of course, Antony Jenkins, from whom much more in a moment.

In 2009, Which? got together with Vince Cable, Lord McFall and David Davis to form the Future of Banking Commission, because we felt that in the financial crisis discussions the consumer agenda was not being fully represented. This was before the Vickers Report or Parliament's own investigations, and it came up with three main areas of recommendation: first, to ring fence the investment activities of banks from retail activities; secondly, to increase the level of competition and to encourage new entrants; and, thirdly, that fundamentally a process of a culture of change needed to happen within banks themselves in order for the changes to bed down.

At the time, very little attention was paid to the issue of cultural change, but if you fast-forward through the last seven years to now, there is still much to be done to make the banking sector perform its proper role in the economy and in society. Which? research shows that the level of satisfaction with big banks still hovers at around just 50%. We have had continued reverberations from the mis selling scandals that have plagued the last few years; and, crucially, the market share of the top four banks in current accounts is still 70%, which is actually higher than it was 10 years ago.

Yet much has been done, and I am delighted to introduce Antony Jenkins, who was of course the Chief Executive of Barclays from 2012-15, and was at the forefront of the reforms of his bank. Some bankers only started talking about culture after the LIBOR scandal, but Antony is a notable exception to this rule. Summer 2012 was an important one for Barclays. The bank had been fined £290 million for rigging LIBOR rates; it had just lost its Chief Executive, Bob Diamond; it was facing a significant amount of political and regulatory pressure. That is the environment that greeted Antony when he took the helm.

A few months after he had been appointed as Chief Executive of Barclays, Which? published the findings of an investigation into staff at the UK's biggest banks which worryingly found that despite the financial crisis, staff felt under more pressure to sell than ever before. Under Antony's leadership, Barclays was one of the first to move away from sales based bonuses for bank staff. Instead, staff rewards would depend on customer service and acting with integrity.

Barclays also had a novel approach when we asked to discuss their cultural change programme. When we do this with the other banks, we go to Head Office and we meet with the Head of HR and the Head of Corporate Relations. Instead, Barclays let us meet unsupervised with branch managers and frontline staff to discuss the culture. In the latest numbers we have, we are seeing that 63% of staff at Barclays say they do not feel under undue pressure to sell products.

Barclays also started to introduce the technological changes to meet customer needs that will be such a feature of banking in the future.

To discuss how to turn ‘values’ into ‘value’, please welcome Antony Jenkins.

Turning Values into Value: Why the Financial System Must Reform Itself

Antony Jenkins

Former Chief Executive Officer, Barclays (2012-15)

I. Introduction

Thank you very much, Peter. Just hearing you read that makes me feel exhausted – I had forgotten how hard it was running a big bank. Readers of the website promo for this talk might permit themselves a wry smile when encountering a session on ‘values in banking’. After all, was this not the industry, driven by greed, that brought about the biggest economic recession in human history; that forced the world to the edge of the abyss of a global depression, from which there could be no recovery; that caused millions to lose their jobs and homes; and, through the draconian action of policymakers, accelerated the growth of inequality, as those with few or no assets experienced a reduction in real income while those with assets benefited from a considerable increase in the value of those assets because of quantitative easing? In fact, was this not the industry that was too aggressive, too self serving, and too short term focused?

II. What has changed since the Crisis

1. Continuing Dissatisfaction with the Industry

Now, as somebody who has worked for over 30 years in financial services in many different parts of the world, I have certainly observed all those things. Even the language used by some of those in the industry is anathema to values: a zero-sum game, the greater fool theory, ‘You eat what you kill.’ Eight years on from the end of the Financial Crisis, some would say little has changed. To pick up on Peter’s points, customers are at best ambivalent towards banks. One way to measure this which I particularly like is by Net Promoter Score, which is basically the sum of the people who like you minus the sum of those who hate you. This is used extensively in the worlds of venture capital and private equity to track the power of the customer franchise, but for most of the banks in the UK, and certainly the big ones, these scores are mediocre at best. There are a couple of standouts, but there are also some truly awful Net Promoter Scores, well into minus double digits, and that is quite difficult to do. Of course, we know that the level of complaints in the industry remains stubbornly high.

2. Poor Financial Returns

Life is equally unpleasant for shareholders. If you look at the 2015 financial results for 36 European banks and assume that those banks’ cost of equity is about 12%, only six banks generated returns above that level, with a particularly lamentable performance for most UK banks. Boosters of the industry will claim that these results are a consequence of fines for legacy conduct issues and interest rates. The reality is that the driver of this performance is a structural change in the nature of banking, with regulatory change requiring much higher levels of capital, in a process that is not yet over.

The obvious response is to generate more revenue, which is difficult in the current economic climate, or to cut costs, of which compensation is the most significant. If capitalism were functioning effectively in banking, compensation levels would have been reduced to a level where shareholders were rewarded first. However, because of what economists refer to as rent seeking behaviour, this is not the case. In fact, in banking, the specific term for this called coupon clipping, where employees aim to stay in roles for as many bonus seasons as possible and, effectively, get what they believe is their due, just as you would clip the coupon on a bearer bond. Notwithstanding this, constant rounds of job reductions can hardly make banks an inspiring place to work today, so morale remains low in the industry.

3. Banking and Society – A Failure of Values

Finally, banking is not working for society. Trust in banks has never been lower, with a litany of conduct and other problems and ever escalating fines. While changes in regulation have made improvements to the capital, leverage, and liquidity positions, it is far from clear that risk has been contained in the system. I note that Sir John Vickers will be addressing this forum on the 18th of May on the need for banks to hold more capital. In his new book, The End of Alchemy, the former Governor of the Bank of England, Lord King, eruditely describes the still present danger of maturity and risk transformation.

At its heart, this is a failure of values, resulting in a massive destruction of value for customers who receive mediocre service and expensive products, for shareholders receiving poor returns and for society, which deserves better. At the end of the day, it is the citizen who pays the price for this in the following ways: in the expense of managing their financial lives; in poor returns on their savings, which are held by institutional investors such as life insurance companies and mutual funds who hold bank stocks; and in funding bank bailouts, whether through taxes or losses in the value of equities and debt held by institutional investors on behalf of guess who? The citizen.

4. Generating Value for Society

Does society not deserve a better banking system – one that meets the needs of customers, is cost effective, fair, transparent, and secure, and which delivers reasonable returns to shareholders; one that is driven by a core set of values? This really matters to individuals and society. For individuals, I always reminded staff that there is nothing inherently valuable in banking services. In fact, they are often a chore for the customer, but what these services enable in those customers' lives is profound. Getting a mortgage is time consuming, but buying a home is often life changing. Applying for a business loan may involve a lot of paperwork, but taking that enterprise to the next level by launching a new product, entering a new market or employing more people is profound.

For society, an effective and fair banking system is a necessary condition for sustained and viable economic growth. Without economic growth, it is difficult for our citizens to enjoy a higher quality of life. More economic growth means more and varied employment opportunities, more tax revenues to fund education and healthcare and greater levels of home ownership.

III. Improving the Banking System

1. Five Core Principles

From wrestling over many years with the question of how to improve the banking system, I can assure you that there are no easy answers. This is not about the elimination of the profit motive because surely banks have performed very poorly for their shareholders post 2008. No doubt, better run banks would not have incurred so many charges for past misconduct and would have addressed the fundamental shift in business model required to deliver decent returns to those shareholders if the profit motive were more operative in these institutions. Nor is it inherently about size and complexity, although I do accept that this does not always help. Banks of all shapes and sizes failed during the Crisis, the reason for which was predominantly poorly understood and priced risk, which ultimately crystallised into losses that could not be absorbed by low capital levels.

I would suggest that there are five core principles that, if applied consistently, and with discipline, will produce a more effective banking system, one that society deserves.

2. Serve the Stakeholders

First, banks must serve all stakeholders in the short and the long term. Like all businesses, banks exist to serve their customers, provide rewarding work for their employees, deliver on their responsibilities to society and thus generate acceptable returns to the providers of capital, usually shareholders. These interests are potentially in conflict and must be continuously harmonised in the short and the long term. Where leaders focus excessively on one dimension – such as driving short term profits through aggressive sales techniques, as we saw with Payment Protection Insurance, or over rewarding employees through unjustifiably high levels of compensation – customers and shareholders pay the price in the long term. The reverse is also true, of course, and the harmonisation of these interests over the short and the long term is the key to a successful and sustainable organisation.

3. Goals, Purpose, and Values

Secondly, banks must define their goals, purpose, and values. People come to work for a variety of reasons: to support their family, to grow as a professional, to make a difference, to be part of something bigger than themselves. Very few people – though, admittedly, some in financial services – define the value of their work purely in financial terms, which is, of course, both morally bankrupt and soul destroying. There will always be someone who is paid more than you, and, therefore, if money is your only objective, you are doomed to live in a state of constant dissatisfaction.

Setting a clear goal for the organisation and defining an existential purpose supported by well-defined values, is a way of orienting the organisation. Through the use of a balanced scorecard, setting goals for stakeholders over time, this can make it tangible for colleagues in terms of what must be delivered, and how it should be delivered. Behaviour can then be encouraged through performance management systems, promotion mechanisms and compensation structures. At Barclays, we set our goal as becoming the go-to bank; our purpose is helping people achieve their ambitions in the right way, and our values as respect, integrity, service, excellence, and stewardship. All of this was backed up by a set of eight five-year goals – two for each of our stakeholders.

4. Leadership and Culture

Thirdly, banks must build the right leadership and culture. Purpose and values are all very well, but it is really about what you do and not what you say. Barclays famously installed the values on massive, transparent signage in the lobby of the headquarters building, but this was only a communications exercise to drive awareness amongst colleagues. Leadership, and its transmission to the organisation through culture, is the only way to ensure the right outcomes. The behaviours of leaders must be consistent with goals, purpose, and values. The organisation will see in an instant any lack of authenticity and consistency, while culture must be constantly managed and nurtured by the actions of all employees.

This is hard and demanding work. It requires time. I believe that such a journey takes a minimum of five years and probably closer to 10. This of course requires consistency of support from the board and a high level of execution from management. It is also important that leadership address the 'bad actor' problem. In any large organisation, there will be those who act with bad intent, for example, in fraudulently moving money from a customer's account to one they control, or in manipulating reference rates such as LIBOR. Culture alone will not protect against such behaviour, although clearly it will create a less conducive environment for it. A strong culture must be supplemented with effective, protective, and detective controls that root out and appropriately punish the bad actor, established and reinforced by leadership.

5. Courage to Change

Fourthly, have courage. In recent years, one of the most significant learnings for me has been the role of the individual in creating the profound change required to build better banking. As individuals, we are programmed to be suspicious of and resist change. It is an emotional reaction, but much more powerful than any logic that justifies the need for change. One of the reasons organisations generally respond more effectively in a crisis is because the urgency of the crisis overcomes the fear that would usually create inaction. I truly believe I would not have been able to introduce goals, purpose, and values at Barclays had it not been for been for the massive collapse in the reputation of the organisation after the LIBOR scandal of 2012 that Peter referred to in his opening remarks.

Clearly, it is unrealistic to create a permanent sense of crisis to drive profound change, but I believe much more time needs to be spent working with individual leaders to help them understand their own fears and how to overcome them so they can lead change more effectively.

6. The Right Regulation

Finally, society must establish the right regulation. I have argued that it is in the banks' own interest to create a values-based banking system, but it is also right that society should ensure that banks operate appropriately through the setting and policing of regulation. To be clear, this cannot be a substitute for the banks' responsibilities, but it must be a critical last line of defence. While much progress has been made on improving capital and liquidity levels within banks, a process of further optimisation will be required. Further, on conduct regulation, a more comprehensive description of the rights and responsibilities of the customer and the bank is appropriate so each party can clearly benefit from the relationship.

7. Constructing the Right Banking System

In my view, with the implementation of these five principles, it is possible to construct a banking system that serves customers, colleagues, shareholders, and society in the right way. There are some grounds of optimism in this aspiration, and I see this among industry leaders, and their desire to accomplish this. Indeed, a report published last year by the New City Agenda on the culture of British retail banking stated in the preface, 'Every major bank we talked to not only acknowledged the toxicity of previous working cultures, but had programs in place to ensure their business treated customers fairly'. Equally, this report went on to acknowledge that improving culture would take a generation.

The enthusiasm for this change is also not uniform across the industry. There are those who believe the UK should attempt to compete with the very large US universal banks, despite the fact that our economy is only one sixth the size of the US's and that the regulators are like the referee at a football game – as long as they do not see the infraction, it does not matter. While the five principles lay out how to deliver a values based and value creating banking system, it is by no means clear that this will actually happen. In fact, I would be quite depressed by this dystopia were it not for one factor, and that is technology.

IV. How Technology Can Drive Change

1. Three Phases

I have spoken elsewhere about how we in financial services are approaching an Uber moment, by which I mean a situation in which technology can create a significantly better customer experience and, in doing so, disrupt existing providers within the industry, effectively hollowing out the economics of the incumbents. This is driven by a very significant improvement in the capabilities of technology, and by an equally significant reduction in technology cost. With the arrival of cloud computing, artificial intelligence and natural language, mobile, and distributed ledger, we are now at the point where we can see a true transformation in the industry. I see this operating in three overlapping phases.

2. Explosion of FinTech Startups

In phase one, where we are now, and which I expect to run for three years, we see the launch of literally thousands of FinTech startups, fuelled by plentiful venture capital and human capital attracted to the sector. Across small businesses, student lending, foreign exchange, peer to peer lending and mobile commerce, there is intense activity, but it is also true of bond trading, trade finance, and settlement of non standard securities instruments. The incumbents, meanwhile, having ignored technology and hoped it would go away, have responded by upping their game on such things as mobile banking, making investments in and establishing partnerships with the FinTechs, and setting up accelerators and incubators. However, the incumbents are fundamentally hampered by their legacy infrastructures, which consume about 80% of their technology resource and by intense cultural resistance to new technology.

3. The Struggles of Incumbents

In the second phase between now and about 10 years out, I see some but by no means all the FinTechs starting to gain traction and drawing customers away from banks. Remember that we know from other areas of our lives that we only change behaviour when things are significantly better – say 10 times better – than the status quo. Those who can deliver this 10 times better service will be the winners. For example, if they offer low cost service; excellent user experience; the use of data to make better credit decisions; and highly automated customer service, but with high human intervention for those who want it and will pay for it.

In this phase, our friends in the incumbents will start to struggle; they will still be dealing with regulatory change and low interest rates. Now losing revenues to the FinTechs, profits will come under even more pressure. Further cost cutting will ensue, resulting in significant job losses and branch closures. It is likely that large banks will fragment as they seek to protect the profitability of their operations, leaving behind a zombie core. I estimate in this phase that as many as 20% to 50% of jobs, and up to half or branches, could go in the next 10 years.

4. A Radically New Banking System

The third phase will begin in about five years' time and will last for approximately 15 years. Here, I see new technologies such as distributed ledger and artificial intelligence facilitate building a radically different banking system. With the first, there is the potential to reduce or eliminate the role banks play in intermediation, not just of payments, but of savings, lending, and capital raising as well. This could go as far as to eliminate the need for maturity and risk transformation, resulting in a much more secure system. With the second, the ability to collect and curate all relevant information about you as an individual, and then to present that profile to a range of counterparts for lending, saving, etc. should result in a much lower cost, but also in a more effective banking system.

Imagine ‘Susan’ is checking her favourite social media app using virtual reality. Overnight, her automated financial agent has been checking mortgage offers for a property Susan has identified using the search function of the social media app. Using almost perfect data about Susan – her finances, education, lifestyle, employment prospects and risk tolerance – the agent has identified the best mortgage for Susan. The mortgage happens to be provided by the automated agent of a large life insurance company. The automated agents have already exchanged all the data both parties need to advance the loan, and a smart contract has been created. Once Susan triggers the contract, the loan’s proceeds are disbursed and the title transferred to Susan with the property charge noted. Payments are set up automatically for Susan, but adjusted dynamically above a floor, depending on her expenses in any month. Should Susan experience any financial difficulties, the agent will detect the potential for this and remedial actions will be suggested to Susan. In the worst case – default – a series of actions will be triggered in the smart contract to deal fairly with the situation of lender and borrower.

This is not science fiction. I could introduce you today to companies developing every aspect of the experience I just described. It is only a matter of time until this is a reality. In fact, in this scenario, there is no bank, only intelligent agents acting for each counterparty coupled with distributed ledger technology to record the payment, loan, and change of property ownership. The customer experience should be almost instant and very low cost, and the system itself will be much safer, as all the risk of intermediation is removed.

IV. Conclusion – Customer Experience and the Value of Values

Of course, banks are not going away any time soon. They have millions of customers, powerful brands, and an intimate knowledge of regulation. However, equally, as we have seen in other aspects of our lives, there is nowhere to hide when technology creates transformation, and it is hard to think of an incumbent that has successfully migrated to the new world. In fact, the opposite is true – think Kodak, Nokia, and Blockbuster. In the midst of all this transformation and disruption, values and value creation through values remains paramount. Questions of privacy, control of data and cyber security are profound, as is creating that 10x customer experience. For organisations that can conceive of and build a banking system predicated on the values of truly delivering for society and the customer, great value can be created. Thank you very much.