



# Internationalization strategies of emerging market banks: Challenges and opportunities

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**Abstract** The greatly improved economic fundamentals of the major emerging economies over the last decade have propelled several emerging banks into the ranks of the world's largest. Despite their importance in the global economy, the internationalization of emerging market banks remains an understudied phenomenon. This article examines factors that may influence the internationalization strategies of emerging market banks in the private banking sector, both when going abroad (take-off) and upon arrival in a host country (landing). The private banking sector is of significant interest given its importance in many leading financial centers around the world while undergoing major transformation due to the worldwide financial crisis, several recent scandals, and a fast-changing regulatory environment. We highlight the internationalization strategies of two banks from emerging countries, China and Brazil, and their experience in Switzerland's traditional private banking sector. These two cases highlight factors that may influence successful internationalization such as prior industry experience, existing client base, entry strategy, ownership type, and the liability of foreignness. Our findings offer valuable implications for managers from other emerging economies by providing a better understanding of how emerging market banks expand internationally.

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## 1. Growing wealth in emerging markets

Global wealth continues to grow and to produce an increasingly large number of high net worth

individuals (HNWIs), especially in emerging countries. A dramatic shift in global wealth distribution is currently taking place around the world, mainly in the Asia-Pacific region where the number of HNWIs is growing faster than the rate of GDP in most countries. Many of these individuals are entrepreneurs who demand access to the same investments and services offered to their counterparts in developed countries. Some of this new wealth has found its way to the leading private banking centers

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around the world. Several well-capitalized and well-managed emerging banks are gradually entering a select group of major institutions in international private banking to claim their share of this lucrative sector, encouraged by the fact that more and more of the HNWI universe is composed of citizens and residents from emerging economies. This represents challenges and opportunities for both emerging market banks (EM-banks) and traditional banks.

Banks must be prepared to handle increasingly sophisticated demands from this new emerging entrepreneurial class (including both personal and corporate clients). All major institutions in private banking aspire to provide a global range of products and services and to capture an increasing number of these valuable clients. An attractive option for large emerging banks is to internationalize and gain the necessary private banking knowledge abroad in order to assimilate useful business know-how for the benefit of their offshore and onshore clients (normally the larger share of a bank's wealth management business who benefit from any upgrade in a bank's global brand and reputation).

### 1.1. Increasing international role of emerging market banks

Greatly improved economic fundamentals of the major emerging economies over the last decade have propelled several banks from emerging countries into the ranks of the world's largest (either by assets and/or capital). Of the top 50 banks in the world in 2015 (in total assets), 22 were from emerging countries (Daniels, 2016). Despite growing wealth, most emerging market banks currently provide relatively limited private banking services to their domestic high net worth clients.<sup>1</sup> Historically, clients from emerging markets have invested abroad for a number of reasons: economic volatility and the lack of political stability in their home country, investment diversification, better service, and tax avoidance. Clients from emerging markets have traditionally placed their investments in developed markets, including the usual wealth management capitals around the world, such as Switzerland, and with leading international private banks. Nevertheless, EM-banks are poised to become increasingly important participants in international private banking. As they grow in size,

together with an ever-increasing number of HNWIs and a greater share of wealth created by their compatriots, EM-banks will seek to internationalize and capture a share of the growing business of managing both onshore and offshore emerging wealth.

### 1.2. Emerging market banks and Swiss private banking

The private banking sector is of significant scholarly and business interest as it is undergoing major transformation due to the worldwide financial crisis, several recent scandals, and a fast-changing regulatory environment. Switzerland has been the historic center of international private banking with many family-owned banks as well as large global banks embedded in the local institutional and social fabric. This provides an interesting base from which to explore internationalization strategies, motives, and methods of banks from emerging countries and to better understand the challenges and opportunities they face upon entry into the Swiss bastion of private banking.

The entry of EM-banks into the Swiss private banking sector also represents a timely research topic given the substantial restructuring and concentration of the sector since the 2008 financial crisis. In addition, this sector has faced major upheavals due to increased transnational regulation, pressures by international authorities regarding tax evasion, and the loss of traditional competitive advantages such as bank secrecy. Private banking is currently characterized by overcapacity, a trend captured in the important layoffs that have recently taken place. Indeed, the total number of banks in Switzerland decreased from 283 to 275 in 2014 while the number of foreign banks decreased from 145 to 129 from January 2012 to May 2013 (Kirchfeld & Logutenkova, 2013). The 2014 Annual Report of the Association of Foreign Banks in Switzerland listed 118 foreign banks as members at the end of 2014, representing 42% of all banks in Switzerland. While banks and other financial intermediaries struggle to adapt to the evolution of the sector, additional research is needed to understand the implications of the arrival of emerging banks.

A handful of emerging banks from Brazil, Russia, India, and China (the BRIC countries) have entered the Swiss private banking market. While there are several banks from other emerging economies such as the Persian Gulf and Asian countries, there were, until recently, a total of five banks from BRIC countries in Switzerland: Banco Itau and J. Safra Sarasin from Brazil, Hinduja Bank from India, and Sberbank and Gazprombank from Russia. Another Brazilian

<sup>1</sup> We use the terms wealth management and private banking interchangeably to mean the provision of customized banking services and investment advice to high and ultra-high net worth individuals.

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