

# The Industry Pilot Series™: Financial Services

The Industry Pilot Series™ provides readers with an in-depth overview of key industry sectors. Identifying industries that genuinely interest you is a key, and often overlooked, aspect of effective career planning. Industry Sectors covered thus far include: Financial Services, Healthcare, Homeland Security, and Biotechnology. Excerpts for each are available free at [SilverCareerManagement.com](http://SilverCareerManagement.com).

## FINANCIAL SERVICES

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# Industry Outlook

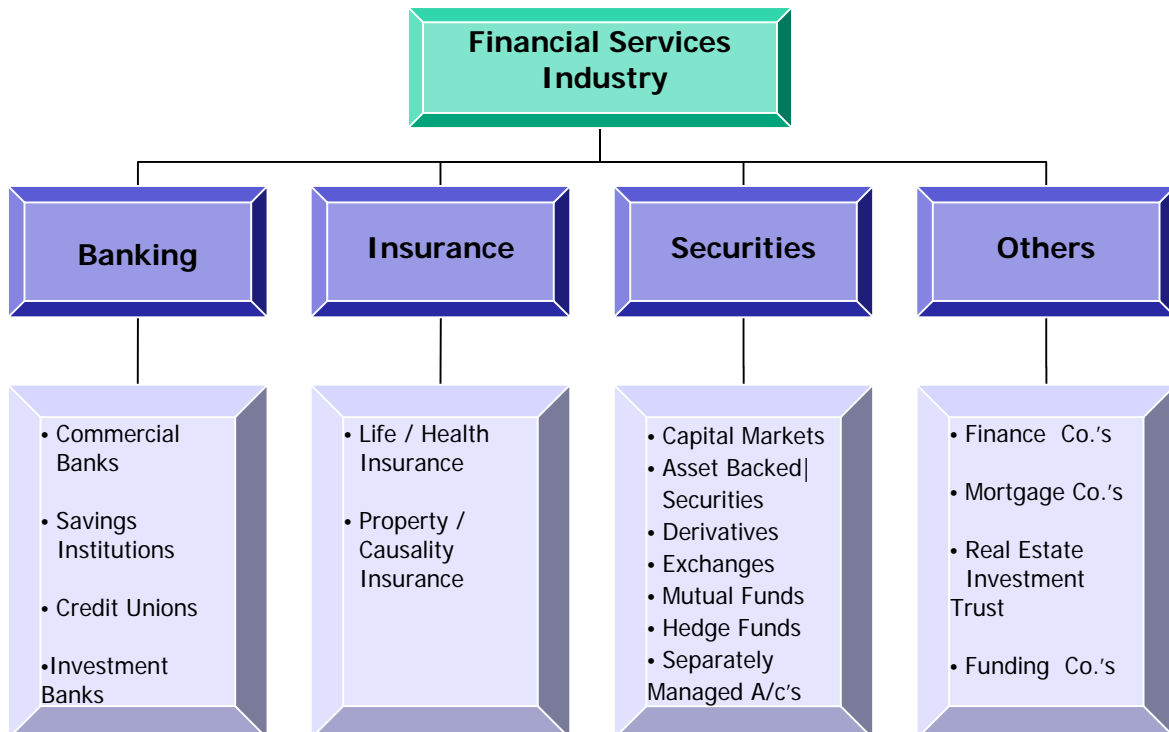
## Financial Services Industry – Overview

In Financial economics, a financial institution acts as an agent that provides financial services for its clients. Common types of financial institutions include banks, insurance, securities, stock brokerages, and similar businesses.

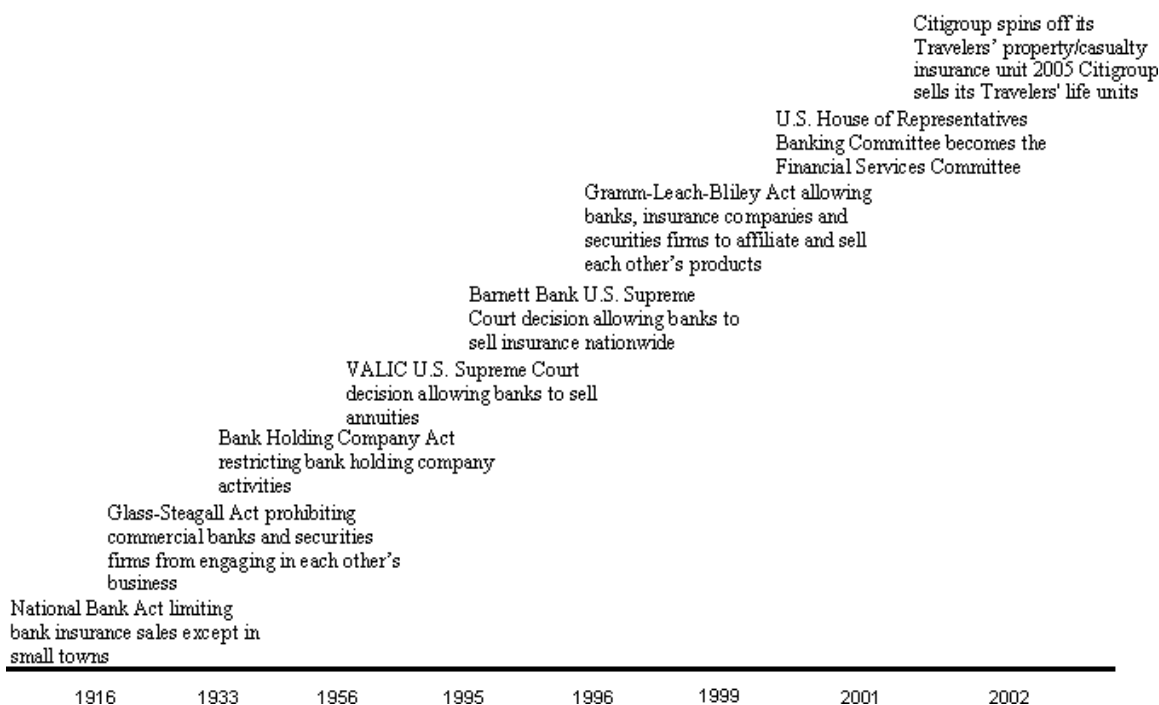
The term financial services became more widespread in the United States partly as a result of the Gramm-Leach-Bliley Financial Services Modernization Act (GLB) of the late 1990s, which enabled different types of companies in the US financial services industry to merge. The Act was passed to spur massive cross sector mergers. Then came the time where many of the leading financial services companies started doing business across sectors. Banks bought specialized securities firms, accounting for 32% of securities industry mergers between 1998 and 2004. Banks also bought insurance agencies and brokers, rather than insurance companies as had been predicted. Insurance companies applied for new thrift charters to open banks instead of buying existing ones. In the USA almost every company which previously described themselves as a bank, insurance company, or brokerage house, now describes themselves in some way as a financial services institution. Say for example companies like Allstate Insurance, Bank of America and E\*TRADE have diversified there business activities have moved that extra mile to offer related financial services.

Today, financial customers can select from an extensive array of financial tools and a wide spectrum of financial services distributors.

Following are the categories that fall under the horizon of financial services:



## Financial Services Industry Deregulation Timeline



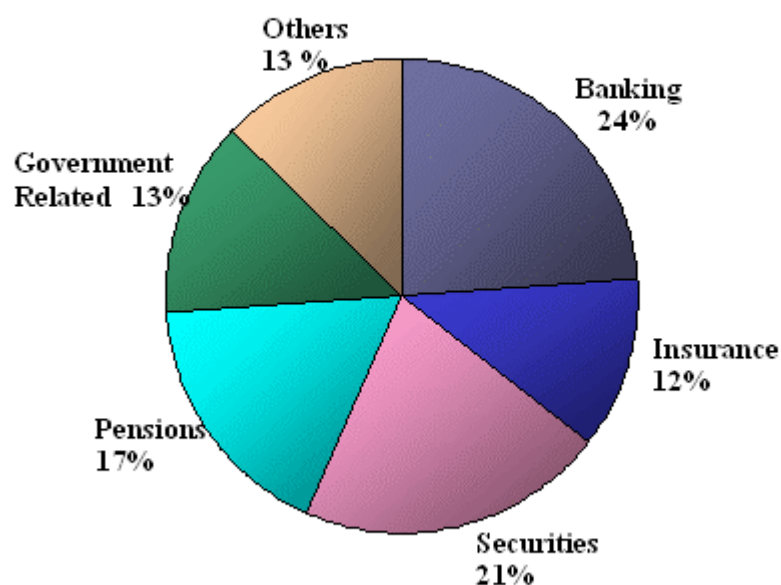
## Assets of Financial Services Sectors by Industry, 2004-2005

Source: Board of Governors of the Federal Reserve System.

Sector	2004	2005
(US\$ Bn)		
<b>Banking</b>		
Commercial banking	\$8,496.6	\$9,236
Savings Institutions	1,649.0	1,788
Credit Unions	654.7	68
<b>Total</b>	<b>10,800.3</b>	<b>11,710</b>
<b>Insurance</b>		
Life insurance companies	\$4,130.3	\$4,380.7
All other insurers	1,166.5	1,265.4
<b>Total</b>	<b>\$5,296.8</b>	<b>\$5,646.1</b>
<b>Securities</b>		

Mutual and closed-end funds	\$7,561.8	\$8,322.8
Securities broker/dealers	1,844.9	2,144.1
<b>Total</b>	<b>9,406.7</b>	<b>10,466.9</b>
<b>Pensions</b>		
Private pension funds	\$4,472.9	\$4,613.3
State and local govt retirement funds	2,572.0	2,721.7
Federal govt retirement funds	1,024.0	1,075.0
<b>Total</b>	<b>8,068.9</b>	<b>8,410.0</b>
<b>Government-related</b>		
Government lending enterprises	\$2,870.4	\$2,805.1
Federally-related mortgage pools	3,542.2	3,677.5
<b>Total</b>	<b>6,412.6</b>	<b>6,482.6</b>
<b>Others</b>		
Finance companies	\$1,456.3	\$1,334.6
Real estate investment trusts	253.3	354.6
Mortgage companies	32.1	32.1
Asset-backed securities issuers	2,413.6	3,059.1
Funding corporations	1,286.3	1,488.0
<b>Total</b>	<b>5,441.6</b>	<b>6,268.4</b>

**Share by Assets of Various Sectors in the Financial Services Industry, 2005.**



*Source: Board of Governors of the Federal Reserve System.*

**Largest U.S. Financial Services Firms By Revenues, 2005 (\$ Bn)**

Rank	Company	Profits as a% of				Industry	Employees
		Revenues	Profits	Revenues	Assets		
1	General Electric	157	16	10%	2%	Diversified financial	316,000
2	Citigroup	131	24	19%	2%	Banking	303,000
3	American Intl. Group	108	10	10%	1%	Insurance	97,000
4	Bank of America Corp.	83	16	20%	1%	Banking	176,638
5	Berkshire Hathaway	81	8.5	10%	4%	Insurance	192,012
6	J.P. Morgan Chase & Co.	79	8.5	11%	1%	Banking	168,847
7	State Farm Insurance Cos.	59	3.2	6%	2%	Insurance	67,943
8	Morgan Stanley	52	4.9	9%	1%	Securities	53,218
9	Merrill Lynch	47	5.1	11%	1%	Securities	54,600
10	MetLife	46	4.7	10%	1%	Insurance	65,500

*Source: Fortune.*

# Sectors in US Financial Services Industry

## Banking

### Overview

Banking is the largest sector in the financial services industry, includes all depository institutions, from commercial banks and thrifts (savings and loan associations and savings banks) to credit unions. In their role as financial intermediaries, banks use the funds they receive from depositors to make loans and mortgages to individuals and businesses, seeking to earn more on their lending activities than it costs them to attract depositors.

Over the past decade, many banks have diversified and expanded into new business lines such as credit cards, stock brokerage and investment management services. They are also moving into the insurance business, selling annuities and life insurance products in particular, often through the purchase of insurance agencies. Banks can be federally or state chartered.

### Size of Global Banking Industry

Worldwide assets of the largest 1,000 banks grew 15.5% in 2005 to reach a record \$60.5 Tn. EU banks held the largest share, 50% at the end of 2005, up from 38% a decade earlier. The growth in Europe's share was mostly at the expense of Japanese banks whose share more than halved during this period from 33% to 13%. The share of US banks also rose, from 10% to 14%. Most of the remainder was from other Asian and European countries.

The US had largest number of banks (7,540 at end-2005) and branches (75,000) in the world. The large number of banks in the US is an indicator of its geographical dispersity and regulatory structure resulting in a large number of small to medium sized institutions in its banking system. Total assets of US banking industry increased by 8.44% over previous year to US\$ 11,710 Bn in 2005.

## Types of Banks

### Commercial Banks

Commercial banks in US offer a broad array of traditional and nontraditional banking services, including international lending, to the smaller regional and local community banks engaged in more typical banking activities, such as consumer and business lending. Commercial banks receive revenue from many sources including check writing, trust account management fees, investments, loans and mortgages. The number of small commercial banks continues to drop while the number of larger banks grows. There were 256 fewer commercial banks with assets of less than \$100 Mn in 2004 than in the previous year, but 96 more in the \$100 Mn to \$1 Bn asset size, and 21 more in the \$1 Bn or more categories.

## **Savings / Thrift Institutions**

Savings and loan associations and savings banks fall into the category of thrift institutions. Thrifts were originally established to promote personal savings through savings accounts and homeownership through mortgage lending, but now provide a range of services similar to many commercial banks. Savings banks tend to be small and are located mostly in the northeastern states. Like other banking institutions with a significant portion of mortgages on their books, thrifts may belong to the Federal Home Loan (FHL) Bank System. In exchange for holding a certain percentage of their assets in mortgage-backed securities and residential mortgages, these financial institutions may borrow funds from the FHL Bank System at favorable rates.

Thrifts are declining in number from their peak of more than 4,800 in the late 1960's to 1,305 by the end of 2005 mostly due to acquisitions by or conversions to commercial banks or other savings banks.

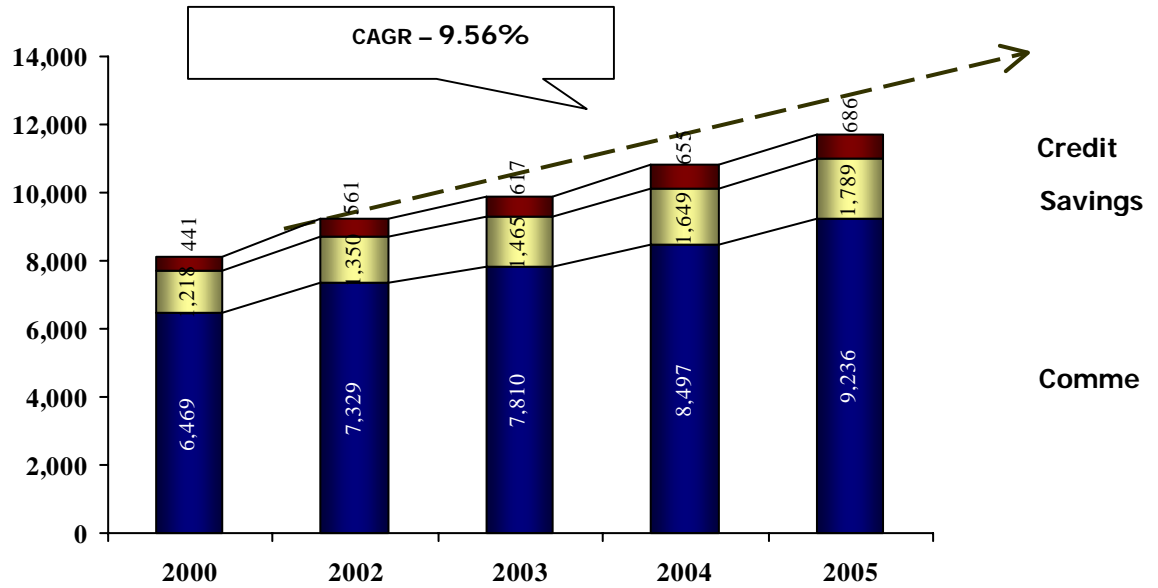
## **Credit Unions**

Credit unions are generally set up by groups of individuals with a common link, such as membership in a labor union, are not-for-profit financial cooperatives that offer personal loans and other consumer banking services. Credit unions now serve more than 80 Mn people in the United States. Individual credit unions are served by 31 federally insured corporate credit unions, which provide investment, liquidity and payment services for their members.

## **Market Size**

The US commercial banking industry -- defined as FDIC (Federal Deposit Insurance Corporation)-insured commercial banks -- experienced robust increases over the past decade due to a multitude of factors including financial modernization, industry consolidation, globalization, deregulation, rapidly developing technology and the rise of new institutions. Growth in this sector was greatly aided in 1999 with the passage by Congress of the financial modernization legislation, which removed barriers and allowed banks to expand their product offerings to include securities and insurance.

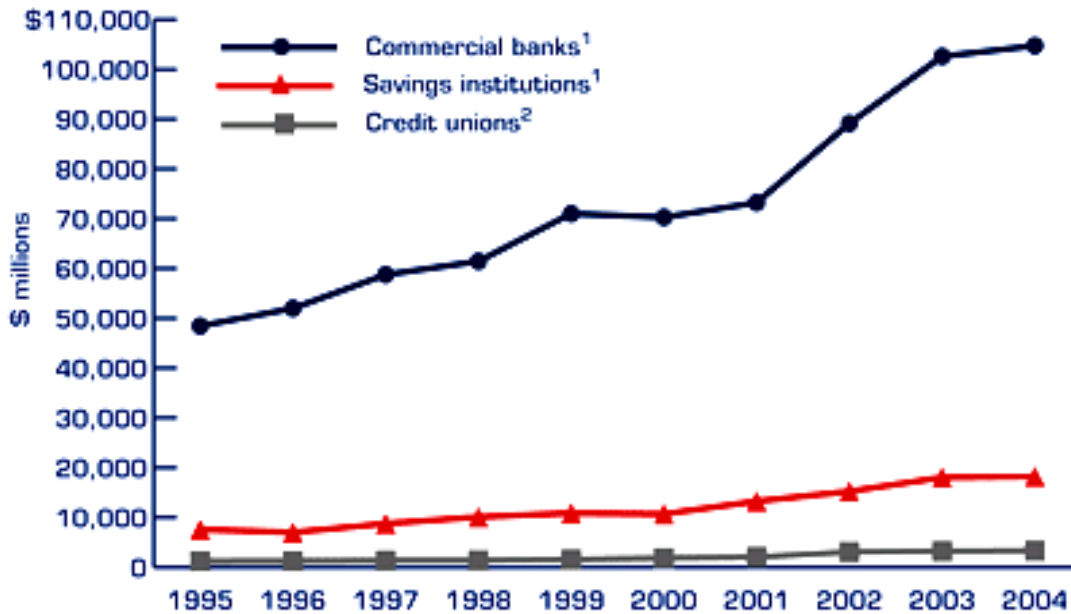
### Financial Assets of Banking Institutions (US\$ Bn)



*Source: Board of Governors of the Federal Reserve System.*

Assets of commercial banks grew 8.7% from 2004 to 2005, faster than savings banks, at 8.5%, and credit unions, at 4.7%.

### Net Income of Savings Institutions, Commercial Banks and Credit Unions, 1995-2004 (\$ Mn)



*Source: Federal Deposit Insurance Corporation; National Credit Union Administration.*

(1) FDIC-insured.

(2) Federally insured state-chartered credit unions.

In 2004 the net income growth of savings institutions and commercial banks slowed to 1.1% and 2.1%, respectively, from double digit growth in the prior two years. Net income growth of credit unions also slowed, from 6.2% from 2002 to 2003, to 2.4% in 2004.

## Insurance

### Overview

The first insurance company in the United States provided fire insurance and was formed in Charles Town (modern-day Charleston), South Carolina, in 1732. Insurance business in US employs about 2.5 Mn people. Life and health insurance in the United States will be about a \$725 Bn in gross revenues business in 2006, compared to only about \$500 Bn in 2002. U.S. life insurance firms hold about \$3.8 Tn in assets. Personal lines comprise another vast sector of insurance. For example, private passenger automobile insurance will be about a \$172 Bn annual premium market, homeowners insurance constituting about a \$50 Bn and that of Property and Casualty insurance premiums will total about \$450 Bn in 2006. Additional sources of insurance company income include annuities and other retirement and investment products.

Insurance is unique in the financial services field because it is regulated primarily at the state level (while banking and investments are regulated primarily by powerful federal agencies such as the Securities and Exchange Commission).

## Size of global insurance industry

Global insurance premiums grew by 9.7% in 2004 to reach \$3.3 Tn. Life insurance premiums grew by 9.8% during the year due to rising demand for annuity and pension products. Non-life insurance premiums grew by 9.4% as premium rates increased. Advanced economies account for the bulk of global insurance. With premium income of \$1,217bn in 2004, North America was the most important region, followed by the EU (\$1,198bn) and Japan (\$492bn). The top four countries accounted for nearly two-thirds of premiums in 2004. The United States and Japan alone accounted for a half of world insurance, much higher than their 7% share of the global population. Emerging markets accounted for over 85% of the world's population but generated only 10% of premiums.

The biggest challenge that the insurance industry is facing today lie in the health coverage sector, where soaring costs, malpractice liability suits and a rapidly aging U.S. population make it extremely difficult for insurers to forecast future costs and appropriately price their products. Meanwhile, health coverage underwriters face growing demand from patients for more

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