A new paradigm for prime brokers

Interview with John Stracquadanio

Scotiabank[TM] is one of a stable of Canadian banks that have decided to enter the prime services space as regulation begins to shake up the established order. Basel III and other regulations are providing new entrants with similar opportunities that arose following the '08 financial crisis as managers adopted a multi-prime approach.

"Regulatory issues impacting the established set of banks are providing opportunities for new players. We are a recipient of this dislocation that is causing a lot of re-pricing conversations between managers and banks," says John Stracquadanio, Head of Prime Services, Scotiabank.

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"Tier one banks are dealing with many different regulatory and other events converging at once and this is impacting the organisational structure of prime services divisions within these banks. The end result," says Stracquadanio, has been:

- "A reduction of existing business that consumes a large amount of the bank's assets.
- Re-pricing that business and assessing whether or not the client has enough non-balance sheet related revenue to meet their required return on assets (ROA) hurdle."

"We are hearing in the market that, in certain cases, the need to shed assets has sparked internal reviews, during which our competitors are identifying clients where ROA hurdles have not been met or, what might previously have been a decent ROA, might no longer work because the cost of funding is higher than it was pre-crisis."

"In other words, the dislocation in '08 led to services potentially being mispriced in the hope that banks could use their balance sheets and widen out their revenue pool. I think what we are seeing now is that the widening of that revenue pool was not as high as expected for banks to meet their net revenue targets," opines Stracquadanio.

Increasingly, the onus is on banks to become more strategic in terms of competing in specific sectors where they are confident they can deliver a tangible edge to clients. This is Scotiabank's approach as it brings forward its expertise in Canadian equities.

"We are not encumbered as a tier one prime broker that's in need of strengthening or reducing its balance sheet. Rather, we are selectively allocating usage at the right pace and with the right returns," notes Stracquadanio.

"It is not inconceivable that the prime brokerage space could, going forward, adopt a more specialist mindset as banks pull back from supporting all types of managers and strategies that revenues just won't support."

"I believe we are entering such an age. I do think there is a place now for specialist prime brokers. Before the crisis there was a universal concept that unless you could do everything you really couldn't do anything. I believe that concept is gone," says Stracquadanio.

"That is what might allow for this continued entry of new players into the prime brokerage space. Less affected banks are getting the chance to compete where they might not have been able to compete in prior years. Each of these new entrants, like Scotiabank, will come with some sort of specialty. It's going to be incumbent on banks to put together what they think their best portfolio of product offering relative to their balance sheet is, as opposed to supporting a massive product offering where they have become incredibly wide in scope but also incredibly shallow."

"I think things are shifting now where prime brokers need to become narrower and deeper."