20 October 2022


Large European banks have the lion's share of international banking relative to counterparts in North America and Asia-Pacific. The tectonic geopolitical realignments currently underway, with decidedly Russia but plausibly also China gradually pushing and being pushed away from the West, raise questions about the future of European banks' global strategies in a partially de-globalising marketplace.

In my view, European banks' international positions will not suffer if strategies are cautiously recalibrated to take account of and anticipate emerging geopolitical realities, if challenges are addressed early on.

Even if the de-globalisation process affects the West's relations with China and Russia, it will not generally apply to large developing economies (Brazil, India, South Africa, Indonesia, Turkey), which maintain a neutral position vis-à-vis Russia and are likely to do the same if, or likely when, the West's estrangement from China deepens.

The banks play no active part in geopolitics, but like all businesses are forced to react to them. This does not come naturally, though; banks and financial markets in general find paradigm shifts of this magnitude and impact difficult to assimilate. Precious few decision-makers in the financial services sector were professionally active before globalisation started in earnest, some three and a half decades ago during the latter Gorbachev years of the ex-USSR. So there is neither institutional knowledge nor personal memories of how international financial activities were conducted before that.

In Europe, effective banking deregulation started in the early 1990s, against the backdrop of growing globalisation. And it is deregulation that subsequently enabled European banks to start diversifying in terms of both services and geographies, with several emerging over time as global players. The emerging geopolitical cleavages represent new territory for them.

## China is the elephant in the room

While the focus is now on Russia due to its war on Ukraine, I view the China relationship paradigm shift the most consequential by far and the one banks and the market pay least attention to. Wrongly in my view. In the last few decades, European and other Western banks took it for granted that to have a global footprint and to position themselves for the future, they needed to build and be seen building business in China.

A presence there, even if providing opaque profitability, was seen as a coveted prize to be in the top league globally. This view does not seem to be changing, even now, when the US and UK governments and the EU are shifting their angle on China, which is increasingly seen as a growing geopolitical risk and trade partner not to be trusted. Against such political tides, BNP Paribas has just established an asset management joint venture in China with Agricultural Bank of China.

The Biden Administration is toughening its approach to China by significantly tightening high-tech exports and transfers. More such steps are expected. The EU is also increasingly pointing to China as an economic adversary rather than a partner. The 20th Chinese Communist Party Congress, currently underway, is focusing less on economic reform and much more on boosting security, combatting hegemonism, and warning about the need to reunify with Taiwan, peacefully or otherwise.

Such winds of change should make European banks reflect on whether they should reconsider their China strategies and draw conclusions sooner rather than too late.

Take China's tightening control over Hong Kong, a major global financial centre and an important hub for Western banks. HSBC and Standard Chartered have a massive presence there as they do in mainland China, which places them in a risk category apart from other large Western banks. Reconsidering their China presence may be painful if not managed proactively, which adds substantial political risk to their global franchises.

Many other large European banks pursue Hong Kong and China activities in wholesale and investment banking, and asset and wealth management.

It is not too early for these banks to start planning for contingencies if the geopolitical landscape worsens. Especially if China intervenes militarily in Taiwan, which at the very least will trigger massive economic sanctions from the West.

## Russia should be off-limits

With respect to Russia, most large Western banks have either already exited – Société Générale, Credit Agricole, ING, JP Morgan – or are in the process of exiting – Citigroup. A few, like RBI and UniCredit, are still there, which raises questions about the wisdom of their strategies looking beyond their bottom lines. Does top management have any real visibility as to whether local business loans, investments or tax proceeds end up financing Russia's war and propaganda machine?

It is very unlikely that, once out, Western banks will go back to Russia (or to Belarus) for the foreseeable future. Russia is a global pariah, a dangerously hostile State that seems to find virtue in this situation, as more and more bridges are cut with Western countries. Even if Western sanctions are eased in the future, most likely following a clear change in leadership and political direction, Europe will not allow itself to depend again on Russian fossil fuels.

Excluding Russia from their activities would not represent a significant loss for Western banks, not even from the pure profit angle. Despite what the Putin regime seems to believe, today's Russia is not the USSR, which was much bigger economically and demographically and benefited from the Comecon[1] framework that gave it a degree of economic stability. Russia today is barely the world's 11th largest economy and most exports consist of fossil fuels and weapons. Humpty Dumpty cannot be put together again.

[1] Comecom refers to the Council for Mutual Economic Assistance, created in 1949 to co-ordinate the economic development of the Soviet bloc (Soviet Union and captive countries in Eastern Europe). It was dissolved in 1991.

**This report is published by Scope Group. The content is an independent view not related to Scope's credit ratings.**


## Scope SE & Co. KGaA

Lennéstraße 5
10785 Berlin
info@scopegroup.com

**Scope Ratings GmbH**

Lennéstraße 5
D-10785 Berlin

info@scoperatings.com

**Scope Ratings UK Limited**

52 Grosvenor Gardens
London SW1W 0AU

info@scoperatings.com

**Scope ESG Analysis GmbH**

Lennéstraße 5
D-10785 Berlin

esg@scopegroup.eu

**Scope Analysis GmbH**

Lennéstraße 5
D-10785 Berlin

info@scopeanalysis.com

**Scope Investor Services GmbH**

Lennéstraße 5
D-10785 Berlin

info@scopeinvestors.com

**Scope Hamburg GmbH**

Stadthausbrücke 5

D-20355 Hamburg

info@scopehamburg.com

**www.scopegroup.com**

**www.scoperatings.com**

**www.scopeanalysis.com**

**www.scopeinvestors.com**

**www.scopehamburg.com**


## Disclaimer