

Discussion on the Market Structure of Foreign Investment Banking

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Abstract

With the rapid development of the economy, the situation of the world securities is also in constant development and change. At present, the development of the securities industry is affected by many different factors. According to the current market situation, investment banks occupy a very high position in the securities industry and play a great role in regulating the development of the securities industry. This kind of role is mainly reflected in the foreign investment banking industry. As for the domestic investment banking industry, this kind of bank investment method didn't play a good market adjustment role. This article starts from the development pattern of investment banks, and comparing the current market development status with foreign investment banking industry, it illustrates the development trend of China's future investment banks.

Keywords

Foreign, Investment Banking, Market Structure, Discussion and Analysis

1. Introduction

In this new era, the investment bank has played a role which becomes more and more important in affecting every aspects of the modern, so it is important and critical to study the market structure of these banks as well as common points and differences between them which may help the governors to find the right developing and reforming directions for their financial system. Besides that, the new technologies and related Artificial Intelligence will totally change the whole traditional financial institutions, which also ask the governors and managers to make clear the true functions and needs in this complicated system, a good reason to make comparisons between different banking systems. In this field, there are few people focusing on this field. They paid more attention about policies

and rules in specific countries instead of making comparisons between different banking systems in different countries, which is the point of this paper. This paper starts from the introduction of US investment banking industry and then it also studies the market structure as well as this industry in China. At last it gives its ideas about this industry and the models in this specific field.

2. The Market Structure of the US Investment Banking Industry

1) The market structure of the US investment banking industry

China is committed to the development of the current national investment bank, but here were various institutional and methodological limitations in the development of China's investment banking business in the past period of time, in which some problems are exposed in the future development of the financial market, so to promote the development of China's financial industry, we need to strengthen the acquisition of some advanced theoretical experience abroad, as well as promote the development of foreign financial groups and large companies, through the necessary research on these cases, China's financial group and business development have laid a good foundation and will play a guiding role in the future development path. According to the analysis of the US investment banking industry, in the development process of this investment bank in the United States, investment banks have experienced changes in terms of various investment and management methods, and gradually promoted to more advanced financial management and management technologies under the impetus of the economic situation. The direction of development has already had a good development position in the current global investment banking business model.

The business model of investment banking in the United States is in the stage of mixed operation. The emergence and application of this business model has taken an extremely effective effect in forming a good investment banking business in the country. After that, the financial and securities industry in the United States was hit hard for several times as time goes by. This financial crisis directly led to the collapse of many banks. This serious financial damage has drawn the widespread attention from the US government, and in the following years, the famous financial market management method was passed in the congress, which has solved the severe hit to the US bank caused by the large-scale financial crisis. Since then, the US investment banks have begun to develop in separate operations. This business model has played a very good market regulation role in the development of the US economic market, and has enabled the US investment banking project to develop into an extremely prosperous stage. Later, with the development of business requirements and the development of the world economic situation, the United States has made corresponding improvements in its business model. The improved investment banking model is in a very high development position in international competition and has greatly advanced the development of the US investment banking program and the US investment banking business is booming.

2) Analysis of the current situation of the investment banking industry's market structure

After analyzing the development history of the investment banking business model in the United States, we carried out the necessary description and research on the existing market structure of the US investment banks, and analyzed the development of various elements of the US investment banking structure and the important role played by the US investment banking market structure. The following is a major analysis of the market structure of US investment banking, as shown in **Figure 1**.

According to the market structure development of the US investment banking industry shown in **Figure 1**, we can see that there are two large investment banks that were in the important position in the US investment banking market. The financial holding group is mainly Citigroup-based, and there are other comprehensive investment banks, such as Merrill Lynch, Goldman Sachs, Morgan Stanley and other 10 banks are in the top position of United States investment banking market. These investment companies and holding companies can provide a full range of services and play an important role in maintaining a stable market structure for the US investment banking industry. However, there are around 10 investment banks which fail to meet their normal targets in terms of capital, strength and customer. The above-mentioned various groups and company industries form a certain regional and specialize in business development companies in a certain business field. The pattern of these investment banking industries has gradually formed during the development of the financial structure for many years. It is of great significance to maintain the country's development in the financial market and to ensure its own stability in the financial market [1]. However, in the future development of the financial market structure, there is a special business field in the world, that is, the company specializing in the acquisition of companies, such as the issuance of underwriting high-risk bonds, for the US investment banking market structure. The development provides a stable guarantee.

3) Status quo of the market structure of Japanese investment banking

Just the same as the analysis of the current situation of the market structure of the investment banking in the United States, when analyzing the market structure of the Japanese investment banking industry, we first analyze and explain the evolution process of the Japanese investment bank. The difference in market concentration between the United States and Japan, as reflected in **Table 1**, is a good illustration of the difference in market investment between the two countries. According to **Table 1**, it can be seen that the top ten companies in the United States occupy 70% - 80% of the market share, while Japan's market concentration, more than 80% market share in the country was occupied by three major security companies. In the history, Japan's investment banking industry has undergone tremendous changes, and after the Japanese investment banking industry has been hit hard, it has gradually expanded its advanced investment management model to promote the good development of the domestic banking

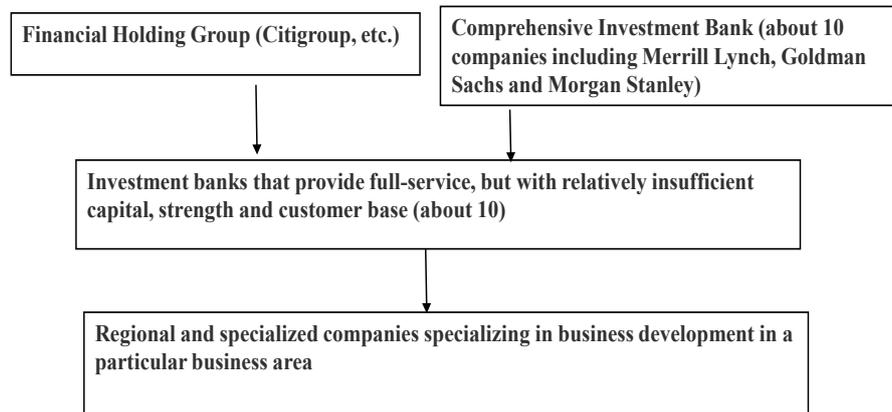


Figure 1. Market structure of the US investment banking industry.

Table 1. Market structure of the US and Japanese investment industries.

National/regional	Comprehensive investment banks with international competitiveness	Market concentration
US	Merrill Lynch, Goldman Sachs, Morgan Stanley	Top 10 companies account for 70% and 80% market share
Japan	Nomura Securities	The country's three major securities companies account for more than 80% of the market share

industry in the world financial market. In the period after the Meiji Restoration, Japan established a multi-currency credit system and a securities market to better occupy a solid position in the future market development. However, although Japan has established a variety of securities market mechanisms to cope with market changes, most of this capital is concentrated in the hands of the chaebol, so Japan will encounter great limitations in the development process. Therefore, in the following period of time, Japan has gradually revised a set of investment bank management methods suitable for its own development by drawing on the practices of the United States and combining with the actual development of the financial market in the country. In the Securities Exchange Act after Japan's revision, the banking industry and the securities industry adopted a method of separate management, and in the long-term after the Second World War, it occupied a relatively large share in the securities business, and basically established a monopoly market structure of the four major securities groups. In the next few years, with the bankruptcy of one of the companies, the remaining three major securities companies re-divided the financial market and established a monopoly position in the Japanese securities market. Then, in the subsequent development of the financial market, the Japanese government launched the financial bang in order to improve the national competitiveness of its securities companies, and through this incident, it has made tremendous changes to its investment banking business model. The original mixed financial business model will be transformed into a future investment banking business model. This activity not only realized the institutional transformation of the Japanese invest-

ment banking business model, but also relaxed the regulation of trading commissions and restrictions on overseas banking activities. In the end, it laid the foundation for Japan's good development in the international financial market, and finally expanded the scope of business management of securities companies, and stabilized the position of Japanese securities management in the international arena.

2) Analysis of the current situation of the market structure of Japanese investment banking

From the above developing history of the institutional model of the Japanese investment bank, we can achieve a certain understanding of Japan's investment banking business model, and through this understanding of the Japanese business model, we have gained some experience for the development of China's financial industry. The following is an analysis of the current situation of the Japanese investment banking market, as shown in picture 2.

According to the market structure of the Japanese investment banking industry shown in **Figure 2**, we find that there are three major securities groups in Japan's investment banking market: Nomura, Daiwa, and Nikko Securities. These major large securities companies play an important role in Japan's financial market and in realizing the macro-control of the Japanese investment banking industry, and have an increasing influence in the future development process, boosting development of financial securities in Japan. In addition to these large securities companies, there are mainly 10 quasi-large securities companies in the future. As representatives of quasi-large securities companies, these securities companies are mostly based on the merger of some former medium or small companies, and in today's securities market. Aspects occupy a certain important position. In addition, there are some small and medium-sized securities companies in Japan's advanced financial securities market, and the number of these companies is around dozens. Most of them exist for subsidiaries or affiliates of some large securities companies [2].

3) Related formulas for risk assets

a) Utility function $U = E(r) \cdot 1/2AJ'$

b) The combined benefit $rc = yrp + (1 - y)rf$

c) The expected return of the combination $E(rc) = yE(rp) + (1 - y)rf + y(E(rp) - rf)$ Usually only y is a variable, this is a;

Binary one-time function

σC

d) The standard deviation of the combination $\sigma C = y\sigma p$

$Y = \sigma p$

Combine the above two equations $E(rc) = yE(rp) + (1 - y)rf = rf + 2C(E(rp) - r)$. This time σc is a variable;

Σp

This line is the capital allocation line, the slope is "P-, Sharpe ratio"

e) Bring $E(rc) = rf + y(E(rp) - r)\sigma c = y\sigma p$ into utility function.

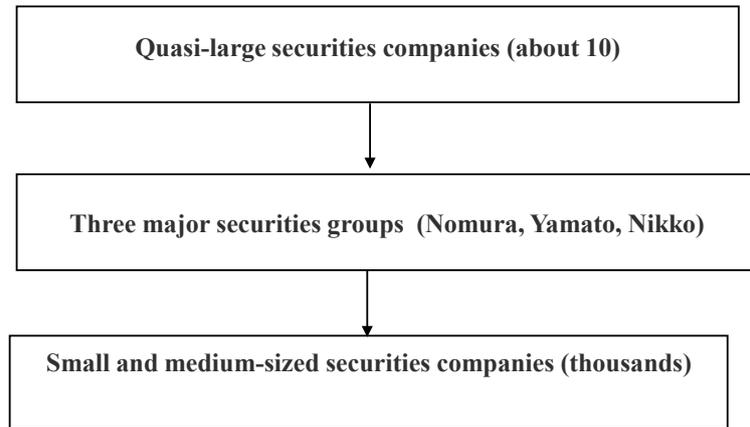


Figure 2. Market pattern of Japanese investment banking.

3. The Enlightenment for the Market Structure of China's Investment Banks

1) The operation of investment banking tends to be mixed

With the changes of the world financial situation, China's investment in the financial industry has undergone changes in various business modes, which have played a significant role in regulating the development and changes of current banking investment projects. According to the current international situation, it can be seen that the mixed operation in bank investment is the general trend. In today's market development, it is gradually replacing other kinds of bank investment methods. In the traditional way of investing in China, the method that has been adopted is to carry out the separation management of investment banks. The financial system of this separate management is widely used in China's financial industry and financial market, and this management method has played an important role in market regulation for a long time. Although there are various ways of investment banking management, China still adheres to the measures of separate operation and separate management, and gradually improves the current financial structure by using these two management and management methods, and strives to use these two operations to make financial markets develop better. Although the current positioning of financial groups is not clear enough in legislation, this is only a theoretical problem. In actual operation, many financial holding groups operated by securities banks have emerged in China. These financial groups in China's current financial market development have played a great role in regulating the financial market. At present, China's economy is in constant development and change. Under the leadership of this economic situation, various laws and regulations are constantly developing and improving. The improvement and development of this kind of legal system has a great role in promoting the boundary of investment banking. When the boundary of the divisional business model is broken, China's development in the investment banking industry will enter an extremely developmental stage which will show a great effect on promoting the development of China's financial market [3].

There have been many changes in China's major investment banks from 2004 to 2005. See **Table 2** for details.

As can be seen from **Table 2**, the development of most of the top companies in 2004 is not smooth. For example, Merrill Lynch ranked 4th in 2004, and ranked 1st in 2005. Name, Goldman Sachs, ranked No. 1 in 2004, ranked third in 2005. It can be seen that the investment banking market has changed greatly under the current market development situation.

2) Constructing a market structure of investment banking with high concentration

The calculation method of the three major competitors in the market share:

The ratio of the sales volume of a company to the total sales of the three largest competitors on the market. For example, if a company's market share is 30%, and the market share of the its three largest competitors is 20%, 10%, 10%, then the relative market share of the company is $30\%/40\% = 75\%$. If the 4 companies each account for 25%, the relative market share of the company is 33%. In general, a company with a relative market share of more than 33% indicates that it has a certain strength in this market.

The development of China's financial securities companies is not smooth, but it has encountered many changes in the development process, and gradually the new financial securities appearance shows in these changes. After undergoing the governance and rectification of securities companies in the previous years, China's financial investment banking industry is gradually moving toward the foreign market structure, and gradually approaching the development direction of the United States, Japan and other countries. However, the development of this economic pattern is not particularly obvious at present, and its performance in China's financial market is not very strong. Therefore, we can say that at present, there is no real investment bank in China. At present, only some institutions such as securities companies and various financial credit companies that undertake some investment banking business in China have such functions.

Table 2. Comparison of financial service revenues of top ten investment banks in the world in 2005.

Company Name	2005 Ranking	2004 Ranking
Merrill Lynch	1	4
Morgan Stanley	2	3
Goldman Sachs Securities	3	1
Citibank	4	2
JPMorgan	5	5
UBS Warburg	6	6
Deutsche Bank	7	8
Nomura Securities	8	10
Lehman Brothers	9	9
Credit Suisse	19	7

Source: information published by China Economic Information Daily.

Therefore, in the future development of the financial securities market, China's investment banking industry will present a financial holding situation in which financial holding groups is the core and other various businesses are relatively single, and based on this situation, the conditions for development have gradually evolved into a further situation. Many investment banks in China have shown a development and prosperity in the current development, and gradually developed from these companies into a corporate structure. The performance of many investment banking industries has shown a good situation, laying a good foundation for the better development of these groups in the future, and gradually increasing the market share of Chinese companies and institutions [4]. At present, based on the development of these financial groups and companies, we can learn from the experience of some large-scale industries abroad, and promote the development of domestically developed industries with reference to the development model of large-scale foreign industries [5].

4. Conclusion

From the above description, we can see the important adjustment role of this investment mode in the securities industry. Market penetration from the transformation process of investment banks will help us better understand investment banking projects, then conduct necessary research and analysis on the current market situation, and finally compare the role of banks in market regulation foreign and domestic investments from various aspects. The investment banking industry should not only run their business under the policies of one country, they also need to shoulder up the responsibility of the society, which can make them a better future.

Conflicts of Interest

The author declares no conflicts of interest regarding the publication of this paper.

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