Industry Analysis

Investment Banks

Q4 2013

Industry Overview

Widely regarded as one of the financial sector's most lucrative industries, the investment bank industry has long enjoyed high returns given its involvement in big-ticket transactions with large business establishments and governments. However, high returns often involve great risks, which could consequently result in tremendous losses. Such is the plight of most investment banks in recent years in light of the 2007-2009 global financial turmoil. And while the financial crisis may already be over for most industries, the financial services sector is not yet out of the woods with a number of investment banks still mired in legal battles over their alleged roles in the demise of some of the largest financial institutions in the U.S.

The investment banks industry is large and far reaching because of the services it provides to the economy and government. An investment bank is a financial institution that assists individuals, corporations, and governments in raising capital by underwriting and acting on their behalf in the issuance of securities. They also assist companies involved in mergers and acquisitions (M&As) and provide ancillary services such as market making, derivatives trading, fixed income instruments, foreign exchange, commodities, and equity securities.

Investment banks trace their roots back to the 1600s when early European merchant banks helped finance foreign trade and accumulated funds for long-term investments overseas. As business and trade crossed the Atlantic, merchant banks became more prominent and served as the financial engines of the 18^{th} and 19^{th} centuries. The success of the merchant banking model was eventually replicated by financial firms across the world and has been transformed into what we know now as investment banking. Despite their troubles in recent years, investment banks remain an important engine of the world economy and continue to fuel the operations of many Western economies.

Market Structure. Unlike commercial and retail banks, investment banks do not take deposits, aligned with the separation between investment banks and commercial banks in the U.S. per the 1933 Glass-Steagall Act until the 1999 Gramm-Leach-Bliley Act. However, other industrialized countries, including G8 countries, have historically not observed such a separation. Trading securities for cash or other securities or promoting securities is the "sell side" of investment banks. Dealing with pension funds, mutual funds, hedge funds, and the investing public is the "buy side"
of investment banks. Many large institutions have both buy and sell side
traditional investment banks side. Companies primarily engaged in the
industry.

Investment banks may involve subscribing investors to security issuanc
M&A consulting. Sales and trading activities involve executing trades or
these are not necessarily investments banking activities, all large investm
issuance of securities in secondary markets. Investment banks also
Research divisions review companies and write reports about their prosp