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The decision-making process in investment banks

Flat structures and decentralized decisions

- ▶ Investment banks are characterised by flat hierarchical structures with only few management levels
- ▶ Decision-making is also decentralised in that decisions on how to advise clients are made at relatively low levels
- ▶ Most other companies have a much more hierarchical structure and key decisions on clients are taken by senior managers
- ▶ We will investigate why investment banks have adopted such a management system

Few management levels

- ▶ The most able employees are promoted to senior positions, but then are less involved in day-to-day decision-making regarding client advice
- ▶ This suggests that advice is given by less able employees, to the detriment of clients
- ▶ We will establish that is not necessarily true and how the flat management structure is suited to the business of investment banks



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Chapter 18.1

The impact of the organisational structure

Discussion of the model results

- ▶ Managers lack the specialist knowledge and might therefore not offer the best advice to clients, making the involvement of senior managers less effective
- ▶ Managers might be better at extracting surplus from clients, but this would not benefit clients, which might find the advice to be of lower quality
- ? If flatter structures are better for investment banks, why are management levels needed at all?
- ! Clients have many needs and will interact with many different teams providing advice; this advice needs to be coordinated and capacities need to be planned

Delegating decisions

- ▶ Decisions in investment banks on how to advise clients are taken at a relatively junior level
- ▶ Senior managers might have better knowledge and their experience might benefit clients
- ▶ We will look into the reason why delegating decision-making to junior employees is beneficial for investment banks



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Chapter 18.2
Delegation of decision-making

Discussion of the model results

- ▶ Employees need to apply their knowledge when working with clients and providing incentives motivates them to exert effort
- ▶ If employees disagree with decisions of senior managers their efforts may reduce, leading to lower benefits to their clients and lower profits to the investment bank
- ? Why would employees disagreeing with decisions be detrimental to the advice given?
- ! Employees might not seek to implement a decision they disagree with and they might implement it only partially; the client might also sense that different opinions exist and be less than satisfied with the advice provided, especially if the advice turns out to be wrong

Summary of key results

- ▶ Flat structures are optimal for investment banks as they allow specialist knowledge to prevail to the benefit of clients, increasing the investment bank's long-term profits
- ▶ Allowing junior employees to make decisions motivates them and allows to identify their ability, leading to higher effort
- ▶ Investment banks rely on the knowledge of those in direct client contact and taking decisions away to higher management levels lowers the quality of advice



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