Prospects for the future remain upbeat:
The financial industry is emerging from the crisis in a stronger position

Survey results
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Despite the global financial and debt crisis and other challenges, Swiss banks remain confident with an upbeat outlook. According to the “Ernst & Young Bank Barometer 2013”, banks are relying on their strengths. The Swiss Private Banking sector is exposed to the greatest competitive pressures facing banks in Switzerland: with regulatory requirements increasing, consolidation is increasingly likely. While respondent banks are taking in their stride Germany’s recent rejection of the withholding tax agreement signed with Switzerland, the Swiss Federal Supreme Court’s ruling on retrocessions and trailer fees in Switzerland, as well as more stringent European regulations in this area, necessitates a fundamental rethink of fee models.

The third annual Ernst & Young Bank Barometer, is based on a survey of 120 managers (executive board members) of various banks across Switzerland, but excluding the major banks. Of the banks surveyed, 36 percent are private banks, 28 percent are foreign banks, 26 percent are regional banks and 10 percent are cantonal banks; 73 percent of the banks are based in the German-speaking part of Switzerland, 22 percent from Western Switzerland (i.e. Geneva area) and 5 percent from Ticino. The telephone survey was conducted in December 2012 on behalf of Ernst & Young by an independent market research institute (Valid Research, Bielefeld).

The following content and the analyses of the banking barometer provide you with an overview around specific aspects that might be relevant to you. The detailed results of the Bank Barometer can be downloaded from our website at www.ey.com/ch.

We hope that you find the results interesting and insightful. Should you have any questions, or if you would like to discuss individual aspects in greater detail, please do not hesitate to contact us. We look forward to hearing from you.
1. Survey design

- Telephone survey conducted by an independent market research institute (Valid Research, Bielefeld) in early December 2012
- Survey of 120 banks in Switzerland (excluding the two major banks)

Breakdown of survey sample

<table>
<thead>
<tr>
<th>Bank type</th>
<th>2011</th>
<th>2012</th>
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<tr>
<td>Private banks²</td>
<td>35 %</td>
<td>36 %</td>
</tr>
<tr>
<td>Foreign banks</td>
<td>15 %</td>
<td>28 %</td>
</tr>
<tr>
<td>Regional banks</td>
<td>35 %</td>
<td>26 %</td>
</tr>
<tr>
<td>Cantonal banks</td>
<td>15 %</td>
<td>10 %</td>
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</tbody>
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¹ Banking categories according to SNB definitions
² Including asset management banks
2. Operational business development

Stable operational development ...

“How would you assess the current operational business development of your organization?” (1/2)

20 percent (previous year: 15 percent) of the banks questioned regard last year’s business as positive, and 58 percent (previous year: 62 percent) rate it as somewhat positive. As in the previous year, only around a quarter of the banks surveyed regard business as negative or somewhat negative.
... in some cases slightly more positive

“How would you assess the current operational business development of your organization?” (2/2)

- Virtually all banking groups assess current business as slightly better than a year ago. Year-on-year, substantially more organizations identify a significant improvement in business, particularly among foreign banks and regional banks.

- A multi-year comparison shows that cantonal banks are increasingly taking a more defensive view of business.
Prospects for the future remain upbeat

“How do you think your organization's operational business will develop in the next 6 months?” (1/2)

- After the significant change of the previous year, the banks questioned have a generally unchanged view of the prospects for future development of their operational business for 2013, with a majority of 70 percent giving a positive or somewhat positive rating. Just under a third of those questioned provided a negative or somewhat negative assessment of business.

- The vast majority of the banks surveyed anticipate declining remuneration for employees and shareholders, but do not expect to have to impose significant redundancies over the months to come.
Regional banks are the most optimistic

“How do you think your organization's operational business will develop in the next 6 months?” (2/2)

A multi-year comparison shows that local regional banks have a relatively stable view of the future and, overall, have the most optimistic outlook.
No significant job redundancies anticipated in the short term

“During the next 6-12 months, do you expect the number of employees in your organization will...”

The majority of the banks questioned anticipate that workforce numbers will remain stable over the coming 6-12 months. Only 12 percent of those surveyed expect their headcount to fall in the next year, and 22 percent even predict that their headcount will rise.

The view of private banks has changed significantly, however. In the previous year, 42 percent anticipated that their workforce numbers would increase, while in this year’s survey only 18 percent of private banks share this view.
Has the financial crisis cleansed the industry?

“Do you consider your organization to have been strengthened or weakened by the impact of the financial crisis?”

- A large majority of the banks surveyed (75 percent) express the view that the fundamental consequences of the financial crisis have actually had a strengthening effect on their organizations.
- This applies in particular to cantonal banks which all believe their organizations have emerged stronger from the crisis.
3. Private banking

Private banking sees a significant increase in competition

“In which business area is competition particularly fierce at present?”

- The majority of the banks surveyed identify private banking as the area in which competition is currently fiercest. The proportion of banks expressing this view has increased sharply year-on-year to 60 percent (previous year: 35 percent).
- In particular, regional and cantonal banks operating primarily in the retail banking sector have adjusted their assessment. In the previous year, these banks still considered retail banking to be the business area where competition was most fierce.
Pressure for consolidation remains high

“Do you expect that there will be any consolidation in the banking sector in the next 6-12 months?”

- A clear majority of 92 percent anticipate that the banking sector will see consolidation.
- Private banks and foreign banks, with their primary focus in the area of private banking, expect that this consolidation will take place in the shorter term, while the banks that operate mainly in the retail banking area are of the opinion that consolidation will take place at a later point in time.
Differing opinions on tax agreements

“Do you expect current developments in connection with banking secrecy and final withholding tax to have an overall positive or negative impact on Switzerland's banking industry?” (1/2)

The banks surveyed are divided in their views on current developments in connection with banking secrecy and final withholding tax. Around half of those surveyed are of the opinion that the ultimate effect of these developments will be either somewhat positive, or somewhat negative, respectively.

The euphoria of 2010, when a clear majority (74 percent) expressed a positive opinion, has clearly diminished.
Tax agreement – more optimism from private banks

“Do you expect current developments in connection with banking secrecy and final withholding tax to have an overall positive or negative impact on Switzerland’s banking industry?” (2/2)

- The proportion of the banks surveyed that anticipate an overall positive impact from current developments has increased significantly across all bank types in a year-on-year comparison.
- Small and medium sized private banks in particular increasingly hold the view that developments are positive, while foreign banks tend to a more pessimistic opinion.
Rejection of tax agreement with Germany – even here there is a positive outlook...

“Do you expect that the rejection of the final withholding tax agreement with Germany will have an overall positive or negative impact on your organization?”

The rejection of the tax agreement with Germany is not seen as a catastrophe. On the contrary: a 72 percent of the banks surveyed consider that the overall impact of this development will tend to be positive. This conclusion is based in particular on the short-term avoidance concerning the cost of implementation, and the anticipated reduction in asset outflow. This applies in particular to smaller and medium-sized private banks and banks which operate mainly at a Swiss national market level.
... and no short-term additional measures

“Will your organization take supporting measures in the absence of the final withholding tax agreement with Germany?”

- Around a third of the banks surveyed, according to their statements, will be taking additional supporting measures as a direct result of the rejection of the final withholding tax agreement, such as implementing a “declared money strategy” or extending their due diligence measures for business relationships which are particularly high-risk from a tax perspective.

- However, a 61 percent of those surveyed do not see any immediate need for additional supporting measures directly following the rejection of the final withholding tax agreement.
Asset outflows expected to remain stable

“The new final withholding taxes will lead to an outflow of client assets. How high would be the percentage of outflows estimated for your institute?”

As in the previous year, the banks surveyed do not anticipate significant outflows of client funds, due both to compensation from inflows of new money and the rejection of the tax agreement with Germany.

Foreign banks are more optimistic than they were a year ago, with 76 percent anticipating no significant outflow of funds. In the previous year only 41 percent of foreign banks held this view.
4. Lending business

Real estate bubble

“Do you agree with the view of the Swiss National Bank and FINMA that there are currently signs of a bubble developing in the Swiss real estate market?”

Developments over the last three years have shown that more and more of the banks surveyed recognize a real estate bubble in the Swiss property market. At present around 77 percent of the banks questioned see this as a risk (previous year: 65 percent).
"Exception-to-policy" remains a fact

“Do you agree with FINMA’s view that the banking industry is currently granting too many loans on a so called ‹exception-to-policy› basis?”

- Following 57 percent in the previous year, this year 62 percent of those questioned agree with FINMA’s opinion that the banking industry has tended to grant too many Exception-to-Policy “ETP” loans over recent years.
- Year-on-year, agreement has risen among private and foreign banks in particular.
More restrictive lending policy expected

“What developments do you expect with regard to Swiss banks' lending policies in the next 6-12 months?” (1/2)

53 percent of the banks surveyed anticipate a more or somewhat more restrictive lending policy in future. There has been no significant change to the result of the previous year's survey (59 percent).
Cantonal and private banks more restrictive

“What developments do you expect with regard to Swiss banks' lending policies in the next 6-12 months?” (2/2)

- Year-on-year, cantonal and private banks in particular acknowledge that their lending policies will be tightened in the future.
- Regional banks, with their primary focus on local lending business, anticipate no significant change to their lending policy.
Need for value adjustments remains unchanged

“In comparison to the prior year, how great will be the need for risk provisions (value adjustments and provisions) to cover lending business during the next 6-12 months?”

A majority of the banks surveyed (54 percent) anticipate no change to the need for value adjustments in lending business over the next 6-12 months.

Regional banks have a more conservative view, anticipating a growing need for value adjustments.
5. Retrocessions

Claims for restitution anticipated …

“Which consequences do you foresee for the financial services industry resulting from the Swiss Federal Supreme Court’s ruling on retrocessions and trailer fees? To what extent do you agree with the following statement?”

Banks and asset managers will face considerable claims for restitution.

- A clear majority of 77 percent of the banks surveyed anticipate that the Swiss Federal Supreme Court’s ruling on retrocessions and trailer fees will result in banks and asset managers facing in part significant claims for restitution.

- Cantonal banks have the highest rate of agreement with this statement, and private banks the lowest.
... but only in asset management business

“Which consequences do you foresee for the financial services industry resulting from the Swiss Federal Supreme Court’s ruling on retrocessions and trailer fees? To what extent do you agree with the following statement?”

**Banks and asset managers will only face considerable claims for restitution in discretionary asset management business.**

- The majority of the banks surveyed – around 62 percent – anticipate that banks will initially only face such claims for restitution in discretionary asset management business.
- Private banks take a more defensive view in this regard: around half of those questioned do not share this opinion and thus consider that other areas may also be affected by this Tribunal ruling.
No future for distribution fees

“Which consequences do you foresee for the financial services industry resulting from the Swiss Federal Supreme Court’s ruling on retrocessions and trailer fees? To what extent do you agree with the following statement?”

*Distribution fees will eventually disappear.*

- A clear majority (70 percent) consider that current distribution fee models are outdated and no longer have a future. The Tribunal’s ruling and the planned tougher European rules mean that fee models will require a radical overhaul.
- Foreign banks are somewhat more cautious in this regard: An important minority of 42 percent do not anticipate that current distribution fees will eventually disappear.
Bank services will become more transparent ...

“Which consequences do you foresee for the financial services industry resulting from the Swiss Federal Supreme Court’s ruling on retrocessions and trailer fees? To what extent do you agree with the following statement?”

_In the future, there will be a fundamental and lasting improvement of the transparency of remuneration mechanisms for bank services._

A large majority – 74 percent of the banks surveyed – expect to see a lasting improvement in the transparency of remuneration mechanisms for bank services.
... but the price is unlikely to fall

“Which consequences do you foresee for the financial services industry resulting from the Swiss Federal Supreme Court’s ruling on retrocessions and trailer fees? To what extent do you agree with the following statement?”

*The price of bank services will fall on a lasting basis.*

According to assessments by the banks surveyed, fees for bank services will become more transparent, but the price is unlikely to fall on a lasting basis. A 67 percent majority does not anticipate a price reduction for services provided.

Representatives of foreign banks have a slightly different opinion, with 50 percent of foreign banks expecting somewhat cheaper bank services.
6. Outlook for 2013

Defensive financial market assessment for 2013

“How do you expect the overall situation of the financial markets will develop in the next 6 - 12 months?”

The banks questioned expect the situation on the financial markets to remain relatively challenging in 2013. The number of optimists and pessimists more or less balance each other out, although the number of optimists has risen in a year-on-year comparison.
Broad acceptance of SNB policy

“How do you view the policy of the Swiss National Bank (SNB) on the introduction of a minimum limit for the Euro?”

The policy of the SNB on the introduction of a lower limit for the Euro is still strongly supported by the banks surveyed; 87 percent of those surveyed support the SNB’s monetary policy for the Euro (previous year: 89 percent).
Top topics for 2013: compliance, equity capital and tax transparency

“What are the three most important topics for your organization over the next 6-12 months?”

The banks will be faced with a very large number of issues in 2013. Compliance, capital planning and the implementation of tax transparency measures (FATCA, final withholding tax) are the issues identified most frequently as top topics by the banks surveyed.
7. Outlook for 2020

Banking 2020: No competition outside the sector anticipated

“How do you see banking in 2020? To what extent do you agree with the following statement?”

*Competitors outside the sector (IT, mobile phones, Internet) will threaten the market position of banks.*

- Private banks: 7% completely agree, 23% tend to agree, 45% tend to disagree, 25% completely disagree
- Foreign banks: 6% completely agree, 18% tend to agree, 32% tend to disagree, 44% completely disagree
- Regional banks: 16% completely agree, 22% tend to agree, 39% tend to disagree, 23% completely disagree
- Cantonal banks: 9% completely agree, 18% tend to agree, 37% tend to disagree, 36% completely disagree

- Banks apparently feel relatively secure in their market position. A clear majority (70 percent) of the banks surveyed anticipate that no competitors outside the sector will threaten the current market position they occupy.
- Representatives of regional banks have the highest level of agreement with the statement regarding the potential threat from competitors coming from outside the sector.
Banking 2020: Lower number of bank branches predicted

“How do you see banking in 2020? To what extent do you agree with the following statement?”

*The number of bank branches will decrease considerably.*

- The increasing digitalization of service behavior will also bring about changes in the banking industry. A large majority of the banks surveyed (76 percent) anticipate that the number of bank branches will decrease over the long term.
- As expected, the rate of agreement with this statement is lower among the regional and cantonal banks which focus primarily on local and regional business.
Banking 2020: Decrease in customer loyalty feared

“How do you see banking in 2020? To what extent do you agree with the following statement?”

*The loyalty of bank customers will decrease considerably.*

A 57 percent majority of the banks surveyed anticipate further changes in customer behavior and that, in particular, the loyalty of bank customers to “their” bank will decrease in the future.

Interestingly, the strongest agreement with this statement was voiced by the 64 percent of the representatives from cantonal banks.
Banking 2020: No falling prices anticipated for banking services

“How do you see banking in 2020? To what extent do you agree with the following statement?”

The price of bank services will fall.

- A 56 percent majority does not anticipate a price reduction for bank services.
- Only a small minority (18 percent) of cantonal banks anticipate that the price of bank services will fall, although this figure is around 45 percent among the other bank types.
Banking 2020: Industrialization is a necessity

“How do you see banking in 2020? To what extent do you agree with the following statement?”

The industrialization and sourcing of business processes will increase considerably.

- A 65 percent majority share the opinion that the industrialization and sourcing of business processes in banking are a necessity, and will increase considerably by 2020.
- Regional and private banks in particular acknowledge this necessity, whereas the majority of the representatives of cantonal banks surveyed do not anticipate any further increase in the industrialization of business processes.
Banking 2020: Overhaul of remuneration and incentive systems

“How do you see banking in 2020? To what extent do you agree with the following statement?”

There will be a fundamental overhaul and reduction of remuneration and incentive systems in the banking sector.

A large majority – 72 percent – of the banks surveyed anticipate a medium-term overhaul and reduction of the remuneration and incentive systems in the banking sector.

The regional and private banks exhibit the highest rate of agreement with this statement.
8. Key messages

Prospects for the future remain upbeat
2012 was a relatively difficult year for Swiss banks, with many setbacks (the Wegelin affair, the final withholding tax agreement, US-related matters, the Libor scandal, etc.). Despite these adverse conditions, the banks are still upbeat and consider their current operational business development to be somewhat positive as well as relatively confident about the medium-term outlook. The great majority of the banks surveyed anticipate declining remuneration for employees and shareholders, but do not expect to have to impose significant redundancies over the months to come.

Emerging stronger from the financial crisis
A significant majority (75 percent) of the banks surveyed express the view that the fundamental consequences of the financial crisis have actually had a strengthening effect on their organizations. This applies in particular to the cantonal banks.

Increasing pressure on private banking
Pressures on margins, falling profits and constantly rising costs in connection with the implementation of new regulatory requirements are substantially increasing the competitive strain on private banking. Furthermore, private banking continues to be affected by certain issues which have not yet been solved. All bank types identify private banking as the business area with the fiercest competition. Year-on-year, competition has increased considerably.

Rejection by Germany of the withholding tax agreement with Switzerland is not a catastrophe
Generally speaking, there is little consensus among the banks regarding current developments in connection with banking secrecy and final withholding tax. The rejection of the withholding tax agreement by Germany is not perceived as a dramatic development. On the contrary: a substantial majority of the banks surveyed (72 percent) consider that the overall impact of this rejection will tend to be positive. This conclusion is based in particular on the short-term avoidance of related implementation costs, and the anticipated reduction in immediate asset outflows. This applies in particular to smaller and medium-sized private banks and banks which operate mainly at a Swiss national market level.

Real estate bubble may lead to a more restrictive lending policy
A growing majority of the banks surveyed consider the property market to be exhibiting signs of approaching a real estate bubble, and that this situation has worsened in recent months. In addition, the banks confirm that lending has taken place, in part, on an “exception-to-policy” basis. In light of this, the banks anticipate the application of a more restrictive lending policy in future. However, those surveyed expect no change to the allowances policy and a comparatively unchanged need for value adjustments over the next 6 - 12 months.

Greater transparency in remuneration mechanisms
The Swiss Federal Supreme Court’s groundbreaking ruling on retrocessions and trailer fees will have lasting consequences for the financial industry. The majority of respondents anticipate the banking industry facing claims for restitution. Ultimately this will also lead to changes in remuneration mechanisms and improved transparency. The costs of services provided are not, however, expected to fall to any significant extent, although distribution fee models in their current form are likely to disappear.

Difficult financial markets – compliance, equity capital and tax transparency are key areas for 2013
The consequences of the financial crisis will continue to affect banks during 2013. Respondents anticipate that the financial markets will continue to be difficult, with compliance continuing as one of the top topics for the upcoming financial year. Areas of primary focus include the implementation of regulatory requirements, particularly in relation to investment suitability. Other key topics include equity planning and tax transparency.

Banking 2020 – numerous challenges
The banking industry faces some fundamental challenges which will force banks to make long-term changes and adjustments. The banks expect to see further regulation over the years to come, with corresponding implications for costs. As a consequence, banks intend to industrialize their business processes still further. They also anticipate consolidation within the industry, which is likely to lead to a reduction in the number of bank branches.
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