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Die Performance der Schweizer Privatbanken

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University of St.Gallen

Programm

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Die Performance der Schweizer Privatbanken: Aktuelle Studienergebnisse	Christian Hintermann Leiter Financial Services Transformation, KPMG
Fazit	
Frage- und Diskussionsrunde	
Stehlunch	
Veranstaltungsende	

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Das Umfeld der Schweizer Privatbanken

Philipp Rickert

Leiter Financial Services und Mitglied der Geschäftsleitung

Environment - 2017 development and recent 2018 trends

Environment	2017	2018 trends
Business Development	▪ Continued regulatory and tax implementation ➢ First time exchange under the AEoI in September 2018 regarding year 2017 ➢ Basel IV uncertainties ▪ Focus on strategic adjustments of business portfolios ▪ Disappointing NNM growth on the back of cross-border legacy outflows ▪ Lower one-off impacts in the sense of asset outflows and fines	▪ Ongoing implementation of regulatory and tax transparency requirements ➢ 44 further countries to enter AEoI with CH in 2018 ▪ Refocus on core markets and exit of non-strategic client segments ▪ Increased cross-border M&A deal activity ▪ Potential NNM growth due to largely confined cross-border legacy outflows ▪ Search for differentiation through new themes
Market Environment	▪ Bull markets (International indices grew in excess of 20%) ▪ US interest rates increase of 75bps ▪ EUR appreciation vs CHF and volatile USD due to political uncertainty	▪ Equity market growth slows down ▪ 50 bps US interest rates increase (Dec17-Jun18) ▪ Geopolitical tensions and political uncertainty increasing (Brexit, Italy, US tariffs, Turkey)
Technology & Information Systems	▪ Investment in digitalization, improved client experience and operating efficiency ▪ Upgrade of obsolete legacy systems ▪ Banking platform projects at two large banks	▪ Technology enhancements through digitalization, automation and FinTech (Artificial Intelligence, Data & Analytics, Robo Advisor, Blockchain and Cryptocurrencies, RegTech, Cyber Security)

Bull markets were the main driver of the recovery of the Swiss private banking market in 2017. Rapid advancements in technology, increased regulatory and tax requirements, uncertainty and interest rates increases will nevertheless challenge the Swiss private banking industry in the short to medium term.

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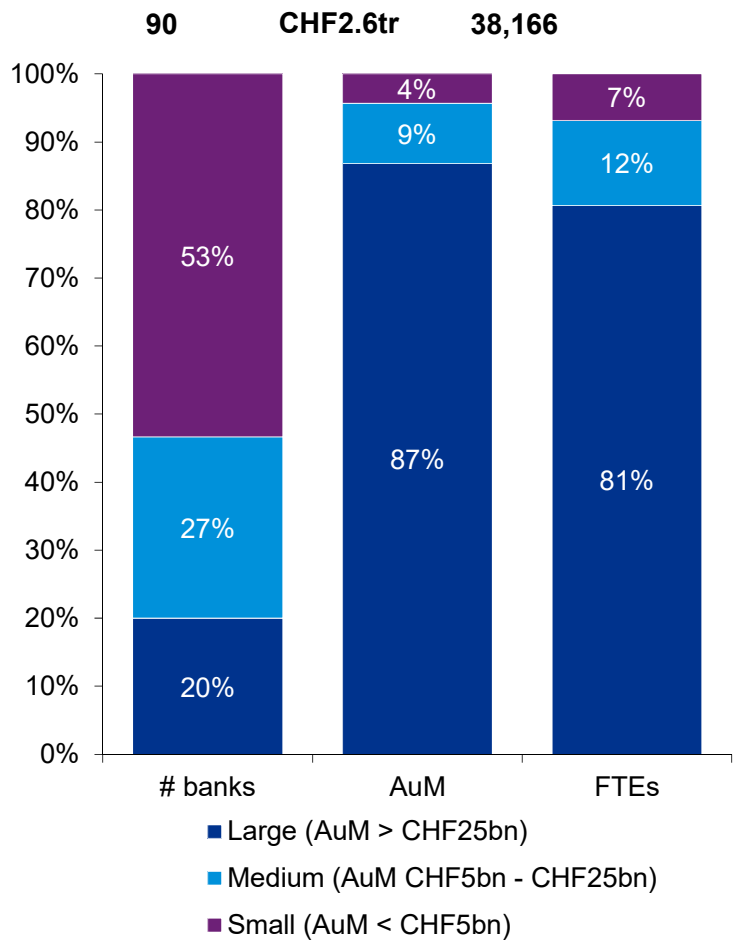
Die Performance der Schweizer Privatbanken

Christian Hintermann

Leiter Financial Services Transformation

Basis of preparation and methodology

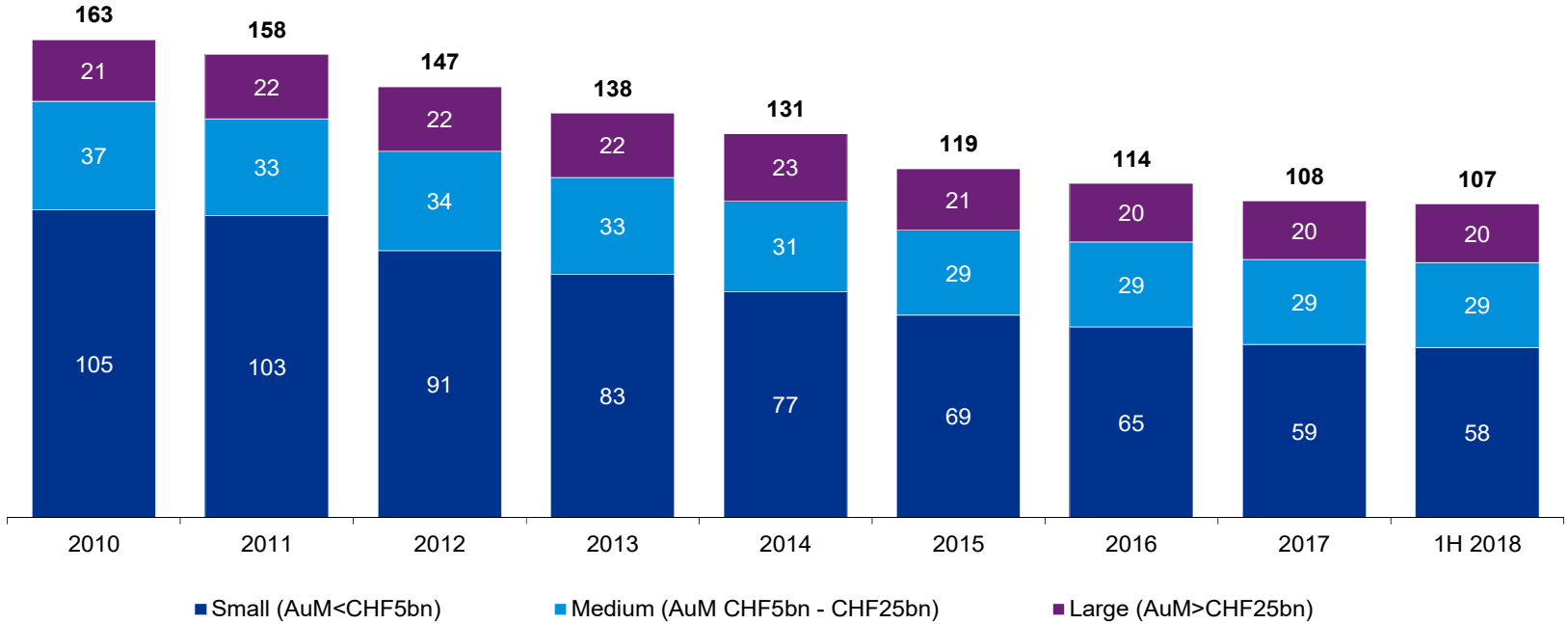
Constant sample dataset – by size



- Annual reports of 90 banks analyzed for the past three years and 80 banks for the past eight years on a constant sample (i.e., the "survivors").
- 83% coverage (90/108 private banks at 31 December 2017)
- Total AuM: CHF2.6 trillion at 31 December 2017
- Excludes UBS, CS and banks for which we do not have annual financial statements over the past three years.
- Quantitative analyses leverages KPMG's Private Banking database.
- KPI calculations are set out in our detailed report.
- In collaboration with the Institute of Business Administration from the University of St.Gallen (HSG)

Contraction slows down

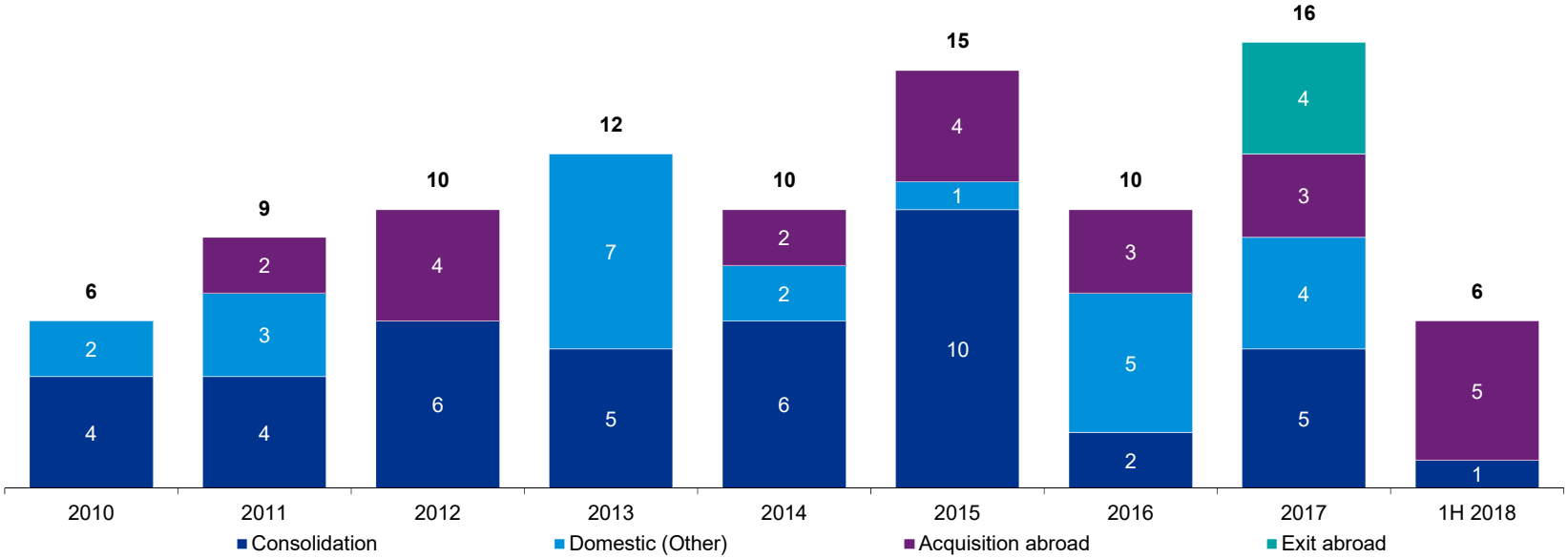
Number of Swiss private banks



- Consolidation slowed down over past 18 months, however it is still creeping on
- Seven banks exited the market within past 18 months
- Time will tell if the positive macro-economic environment will dissuade more owners from selling, or whether rising prices will encourage divestments
- Divided industry: We still expect that a significant number of private banks in the weaker half of the industry will disappear – despite extremely positive macro economic environment many of them couldn't improve performance significantly in 2017

M&A

Number of announced deals (buyer or target is a Swiss private bank)



- With only three deals announced in the first half of the year 2017, activity accelerated in the second half, however, to a record of 16 deals
- Consolidation deals between Swiss private banks paused in 2016 but picked up again with five deals in the second half of 2017; these deals were mainly of small targets
- Only one consolidation deal took place in 1H 2018 being Vontobel's acquisition of Notenstein La Roche, which, however, was the largest such transaction in the past 18 months at CHF16bn AuM
- After years addressing regulatory changes and firefighting, banks have once again started to focus on strategy and repositioning which is visible in the high number of deals abroad in 2017 and 2018 linked to strategic repositioning of banks in certain markets

Industry financial statements: Significant increase in profit

Constant sample financial statement - 90 banks					
				2017 vs. 2016	
CHFm	2015	2016	2017	Amount	%
Net interest income	2,861	3,368	3,840	473	*14.0 %*
Net commisison income	10,587	10,285	11,429	1,145	*11.1 %*
Net trading income	2,117	2,069	2,174	105	*5.1 %*
Net other income	793	847	724	(123)	*(14.5)%*
Operating income	16,358	16,568	18,167	1,599	*9.7 %*
Personnel expenses	(8,692)	(8,796)	(9,518)	(722)	*8.2 %*
General and administrative expenses	(3,774)	(3,936)	(4,195)	(260)	*6.6 %*
Operating expenses	(12,466)	(12,731)	(13,713)	(982)	*7.7 %*
Gross profit	3,892	3,837	4,454	617	*16.1 %*
Non-operating result	(2,449)	(1,469)	(1,643)	(175)	*11.9 %*
Net profit	**1,443**	**2,368**	**2,811**	**443**	***18.7 %***
Other key data					
AuM (CHFbn)	2,309	2,427	2,616	190	*7.8 %*
FTEs	35,287	38,183	38,166	(16)	*(0.0)%*
Cost-income ratio (C/I)	*76.2 %*	*76.8 %*	*75.5 %*	*(1.4)%*	*(1.8)%*
Return on equity (RoE)	*3.8 %*	*6.0 %*	*7.1 %*	*1.2 %*	*19.7 %*

- Gross profit rose by 16.1% to CHF4.5bn in 2017 mainly driven by AuM performance and rising US interest rates
- Non-recurrence of fines helped net profit to double from 2015 to 2017
- Operating income and operating expenses grew at almost the same pace. Industry overall didn't succeed to keep costs stable despite growth mainly driven by performance
- Cost-income ratio for the industry remained flat at approximately 76% between 2015 and 2017, despite exceptional income growth. Enough cost discipline?
- Tax expense of the industry rose from CHF426m in 2015 to CHF637m in 2016 and CHF753m in 2017

Industry financial statements: Reasons to be optimistic

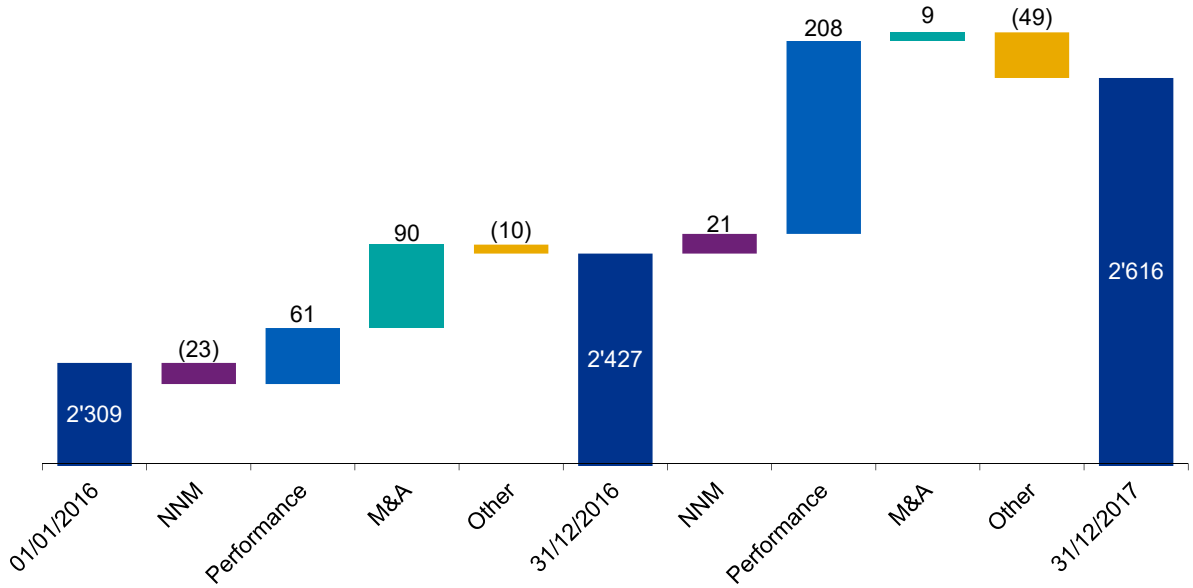
CAGR by size - 90 banks

	CAGR 2017 vs. 2015		
Growth in	**Small**	**Medium**	**Large**
Operating income	*5.7 %*	*(1.7)%*	*6.5 %*
Operating expenses	*3.5 %*	*(1.5)%*	*6.0 %*
Gross profit	*17.4 %*	*(2.1)%*	*7.8 %*
Net profit	*(2.2)%*	*(19.5)%*	*59.8 %*
AuM	*8.7 %*	*0.4 %*	*7.0 %*

- Different development by size clusters, but overall macro-economic and structural reasons to be optimistic about the industry's future performance
  - Continued US interest rate rises and possible interest rate rises in Eurozone and Switzerland
  - Significant implementation costs to comply with new tax and regulatory requirements are largely confined to the past
  - Following the implementation of the AEoI, NNM growth should increase as cross-border legacy outflows recede
  - Enhancing penetration of managed mandates
  - Technology enhancements should improve operational efficiency
- However we stay negative on the future of a significant number of banks in the Lower Mid and Weak performance clusters

AuM development: seeking for new money

Aggregated AuM development (CHFbn)



- AuM grew by 7.8% in 2017 to reach CHF2,616bn which is mainly driven by bullish global equity markets; as 90% of the AuM increase arises from market performance, this may indicate an excessive dependency on external developments
- Disappointing NNM of CHF21.3bn which was barely positive in 2017 following a negative run in 2016; median turned positive with 0.8% (-0.2% in 2016) but is still very low. Second AEoI wave may have impacted 2017 NNM.
- M&A was the biggest contributor to AuM in 2016 (CHF90bn), but minor in 2017 with just CHF9bn (net)
- Other AuM in 2017 represented mainly an outbound strategic transfer of an asset management business to another part of a global banking group

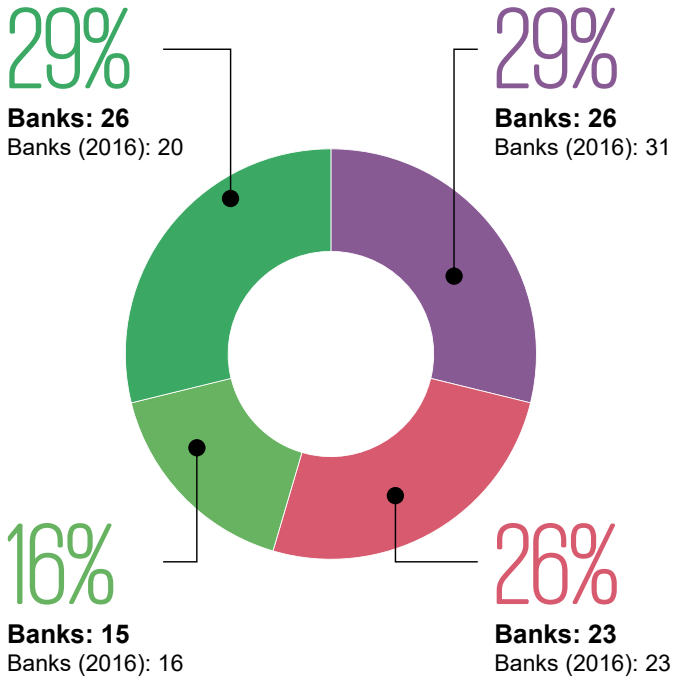
Performance clusters

Strong performers

	2015	2016	2017
Cost-income ratio	65.5%	65.2%	61.7%
RoE	6.0%	6.0%	8.7%

Upper Mid performers

	2015	2016	2017
Cost-income ratio	76.1%	76.3%	73.7%
RoE	5.4%	4.7%	5.9%



Lower Mid performers

	2015	2016	2017
Cost-income ratio	84.8%	86.1%	85.0%
RoE	4.1%	4.4%	3.6%

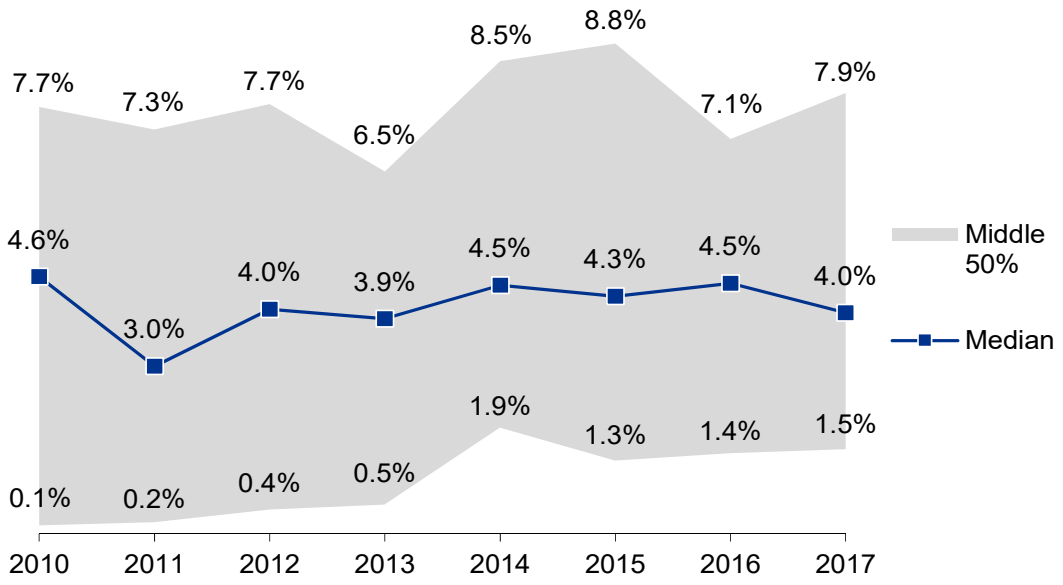
Weak performers

	2015	2016	2017
Cost-income ratio	97.2%	119.6%	101.7%
RoE	0.2%	(2.8)%	(3.0)%

- Divided industry: more strong performers (mainly Swiss headquartered large scale players and small niche players) with improving performance while lower mid and especially weak players stagnate even in positive environment
- Net six banks promoted to Strong and three to Upper Mid in 2017
  - New Strong performers increase in net commission income and/or AuM growth
  - New Upper Mid performers show a reduction in personnel expenses due to internal restructuring
- 13 out of 23 Weak performers incurred operating losses in 2017 despite the extremely positive market environment

Two third of banks improved RoE in 2017 – yet industry remains divided

RoE

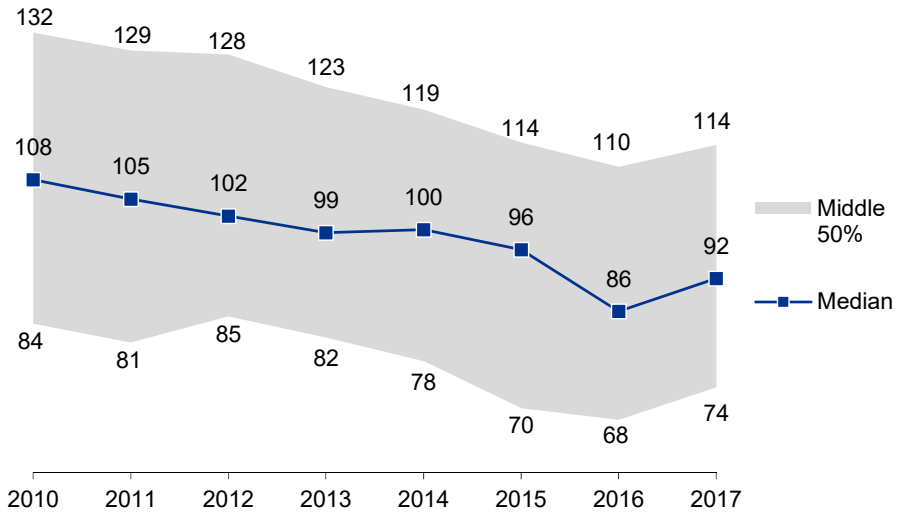


RoE	2015	2016	2017
Improvers	33%	46%	67%
Decliners	67%	54%	33%

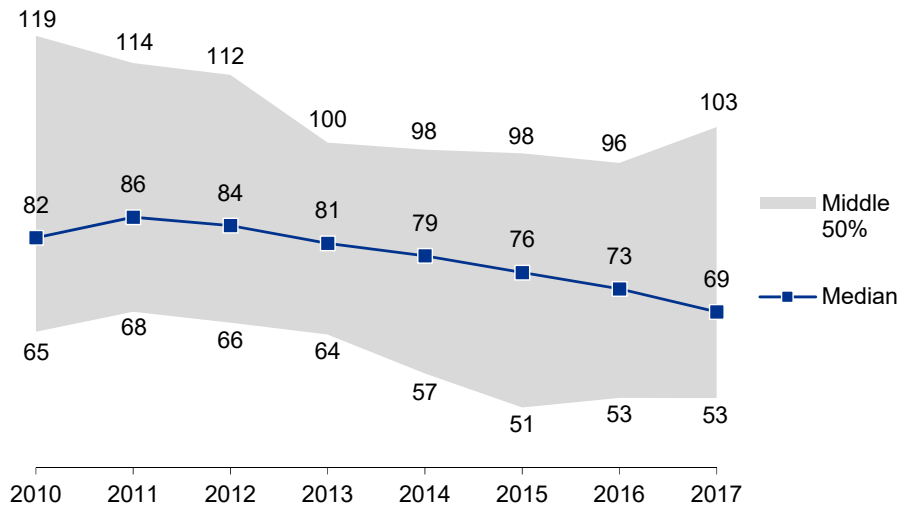
- Bull financial markets helped two-thirds of banks improve their RoE in 2017.
- But the overall picture is one of marked contrasts. While RoE rose significantly at more than 80% of Strong and Upper Mid performers (increase RoE by an average of 1.8 percentage points), fewer than half of Mid and Weak performers saw any improvement. Median decreased by 0.5 percentage points

Operating income margin recovers in 2017, while operating expense margin keeps falling

Operating income margin (bps)



Operating expense margin (bps)

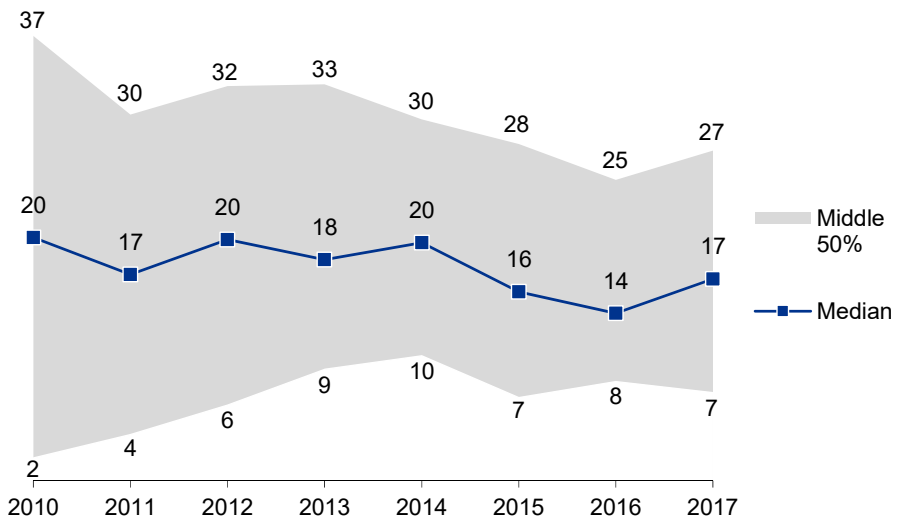


- Following a 10bps fall in 2016, the median operating income margin rebounded by 6bps to 92bps in 2017 due to improved global equity markets and rising US interest rates
- Banks did not manage to increase the percentage of discretionary mandates which remains flat at a median of 21.8%; additionally, the volume of loans also stayed at a low level

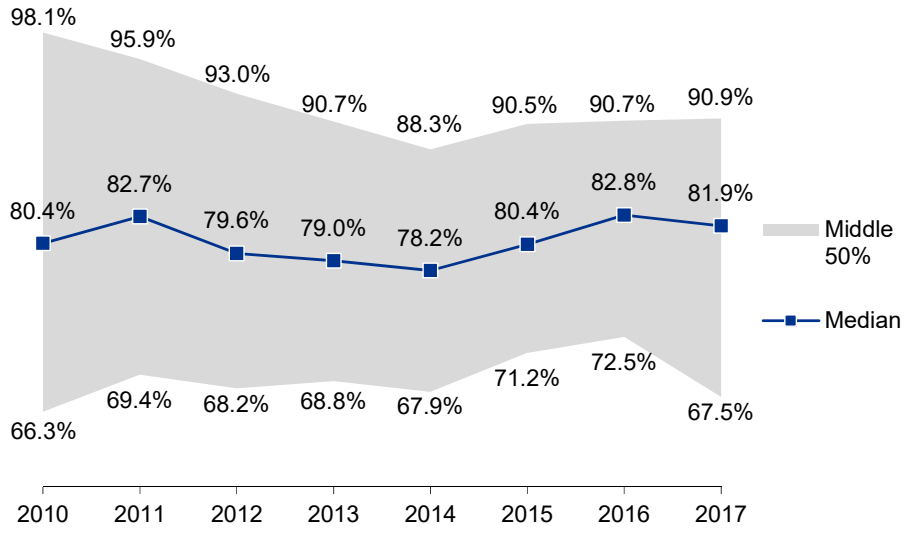
- Operating expense margin decreases for the sixth consecutive year (-4bps)
- Compared to 2016 in which only 43% of the banks showed an improvement to the previous' year performance this ratio has changed to 58% of improvers in 2017

...and so gross profit margin & cost-income ratio improve slightly

Gross profit margin (bps)



Cost-income ratio



- Two-thirds of banks improved their gross profit margin and cost-income (C/I) ratios in 2017, compared to 40% in 2016
- Gross profit margin growth is significant, however, C/I improvement is low as growths in AuM and revenues are partially offset by increasing costs

- Around 80% of the banks in the better half of the industry have managed to improve their C/I ratio significantly; the top quartile even achieved an improvement of 5.0 percentage points totaling in a C/I ratio of 67.5%
- Gaps in C/I ratios are widening – differences of 20% or more percentage points between banks with similar operating models show how some management teams successfully manage their banks

Performance study headlines

- **Recovering, but a sizeable number of banks remain fragile**

  While the future of the industry looks brighter than at any time in the past ten years, more action is needed across the board on NNM, gross income and cost control

- **While the strong get stronger, the weak stagnate**

  Weaker banks failed to improve despite an extremely positive market environment

- **Excessive reliance on market developments**

  Ninety percent of AuM growth in 2017 came from market performance; with only 10% arising from NNM

- **Overcoming a false sense of security**

  Even for profitable banks, improved results are largely driven by market performance, meaning that more challenging conditions could put them into dangerous territory

- **Consolidation creeps on**

  Owners of banks suffering poor key metrics must urgently challenge their current situation and strategy to form a realistic view on what can be changed and whether they should more actively consider selling the bank

- **Firefighting gives way to strategy**

  Having spent years addressing regulatory changes and structural change, banks have once again started to focus on strategy and repositioning

What are the options? Reconfirmed: scale or niche

Strategy	Description	Available for
Building scale	▪ Swiss offshore combined with onshore presence in key markets ▪ Build international / global operating platform ▪ Drive efficiency through scale	max 10 – 15 banks
Niche player	▪ Focus on very specific niche and provide superior service ▪ Outsource / Partner in all areas that are not USP	20 – 30 banks
Optimizing current model / Exit	▪ Cut operating expenses 20-30%, mainly personnel expenses ▪ Consider M&A to increase size ▪ Exit if profitability expectations of shareholders cannot be met	60 – 70 banks

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