



Clarity on Performance of Swiss Private Banks

The widening gap

August 2015



University of St. Gallen

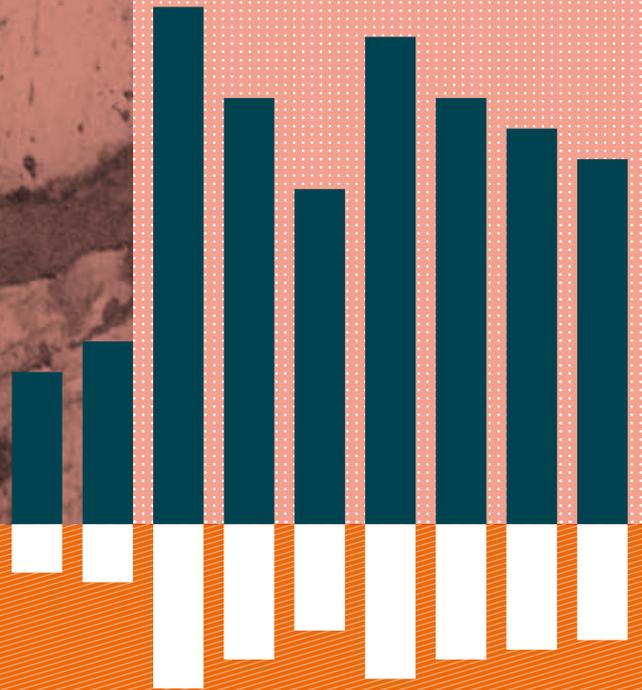
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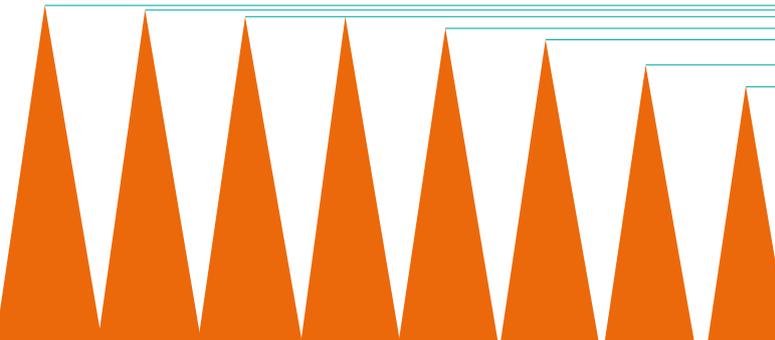
Flight or fight?

18

CEO changes



Hitting pause



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2006 2007 2008 2009 2010 2011 2012 2013 2014 2015

The widening gap

A study by KPMG AG Switzerland

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The growing gap between Swiss private banks

Last year, we categorized Swiss private banks into four distinct clusters based on their profitability over the previous eight years. If last year's results were striking, the outcome of our latest analysis is even more so. The gap between banks is getting wider. The strongest are becoming stronger while those that continue to decline face an urgent need to turn around their fortunes or exit the market.

This polarizing performance did not, however, cause consolidation to accelerate in 2015. While the number of banks in Switzerland did fall further in 2014 and the first half of 2015, it was largely due to liquidations and foreign (especially Anglo-Saxon) banks exiting Switzerland. The execution of M&A agendas was dampened by a general lack of sellers on the market and concern over potential legacy risks.

Despite the current hesitation, it is likely that the face of the industry will change considerably over the next few years. We note how growth is weak and how RoE appears unsustainably low at a median 3.5%. Many Swiss private banks have worked hard to adjust to the „new normal“ of private banking and improve their performance. Although some have managed to better position themselves for the future, more than one-quarter of banks still posted losses before extraordinary items in 2014.

With a significant proportion of banks still needing to determine a clear strategy and once again pursue growth, and banks generally in urgent need of enhancing their financial performances, we would be happy to discuss with you the results of our analysis.

A person is swimming in a pool, with their arm extended and hand on the surface, creating a large splash of water. In the background, a dense city skyline with many tall buildings is visible, slightly out of focus. The overall scene is bright and sunny.

ROE IS UNSUSTAINABLY LOW

Median RoE in 2014 was 3.5% for Swiss private banks as a whole, with 80% of banks reporting an RoE of less than 8%. 26 banks reported losses before extraordinary items. Only 10 banks enjoyed a continuous rise in RoE over the past three years. The industry therefore continues to perform below expectations.

A person is swimming in a pool, with their arm extended and hand cutting through the water, creating a large splash. The background shows a blurred city skyline with tall buildings under a bright sky.

The 9.1% RoE of Strong Performers compares to losses for most banks in Continuing Decline.

Small banks face the biggest challenges, as 41% of them are in Continuing Decline and only 14% are classed as Strong Performers.

STRONG PERFORMERS CONTINUE TO PULL AHEAD

The word "EXIT" is painted in large, bold, black capital letters on a light-colored, textured concrete surface. The letters are slightly weathered and the background shows some small dark spots and grain.

FLIGHT OR FIGHT? BANKS MUST DECIDE

Pressures are intensifying in 2015 on small banks in particular. Many must take a clear decision to either exit the market or stay and change their business and operating models. Time is running out for the necessary changes to be implemented.

AUM GROWTH IS MARKET-DRIVEN, WITH INSIGNIFICANT NNM

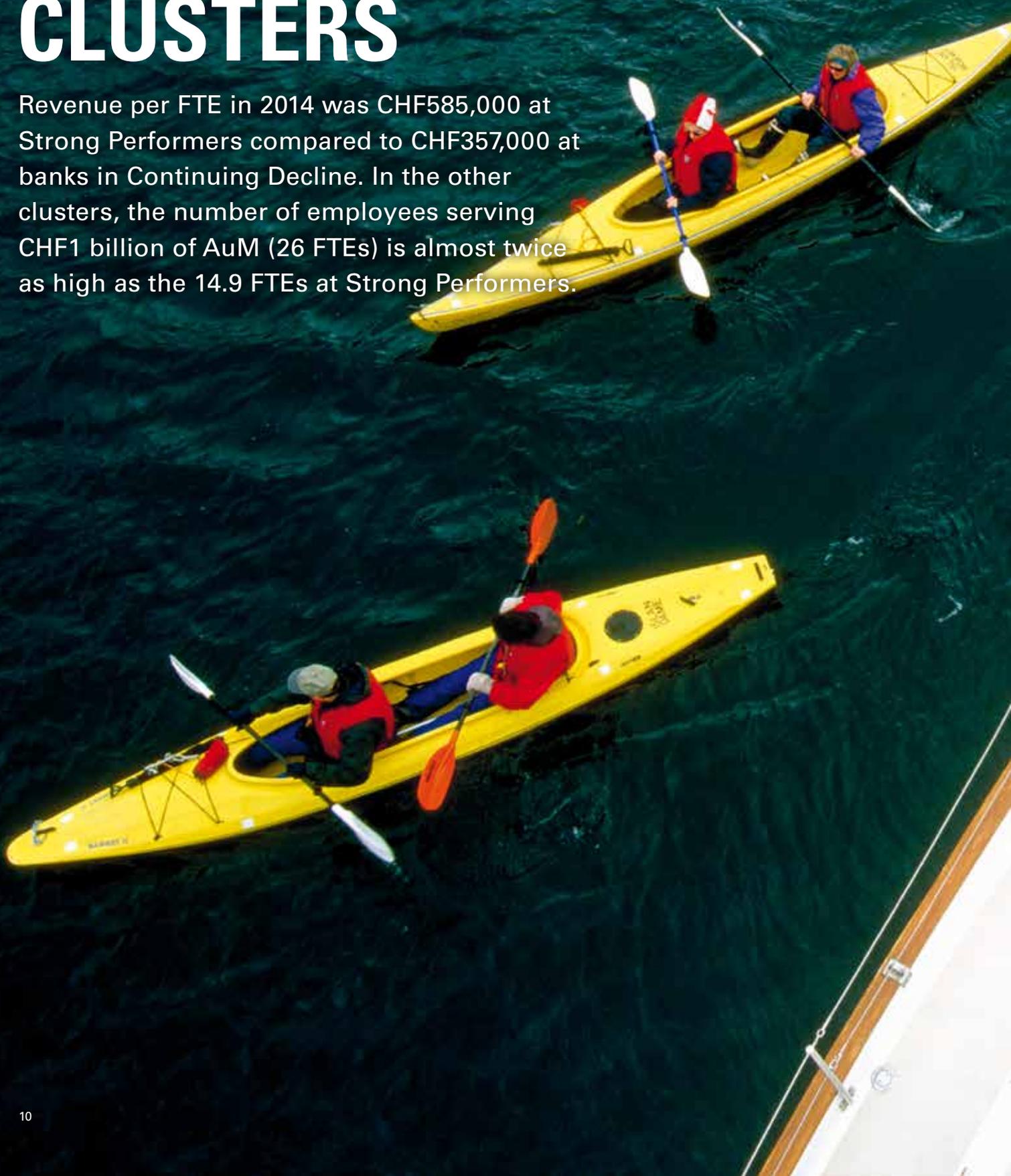
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The 7.3% increase in AuM in 2014 was due to positive market and foreign exchange trends. NNM stood at just 0.5% of AuM. Strong Performers and banks in Turnaround Completed reported net inflows totalling CHF24.9 billion in 2014. Banks in Continuing Decline or Decline Stabilized suffered total net outflows of CHF17.9 billion. The capacity to grow is a clear key success factor.



EFFICIENCY VARIES HUGELY BETWEEN CLUSTERS

Revenue per FTE in 2014 was CHF585,000 at Strong Performers compared to CHF357,000 at banks in Continuing Decline. In the other clusters, the number of employees serving CHF1 billion of AuM (26 FTEs) is almost twice as high as the 14.9 FTEs at Strong Performers.



An aerial photograph of a white sailboat with orange trim on the water. A yellow kayak with a person in a red vest is visible in the upper left. The sailboat's deck has several dark rectangular panels and a white cover. The water is a deep blue-green color.

SIGNIFICANT ACQUISITIONS YIELD BENEFITS FOR ACQUIRERS

Banks that added scale through a significant acquisition saw their net revenue per FTE rise by a median 5.1% and their median RoE rise by 1.4 percentage points in the following one to two years.

Following a busy 2014, caution over legacy risks and an absence of sellers dampened M&A in the first half of 2015. With many banks in Continuing Decline lacking a clear strategy, and exiting Switzerland, however, we expect a further 30% of Swiss private banks to disappear over the coming few years as a result of M&A or liquidations.



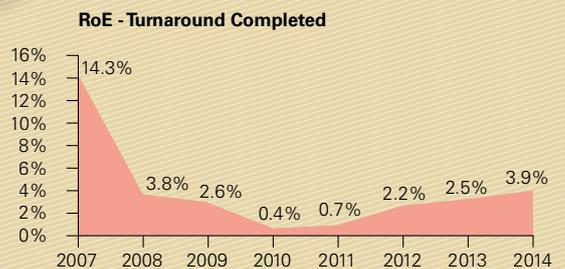
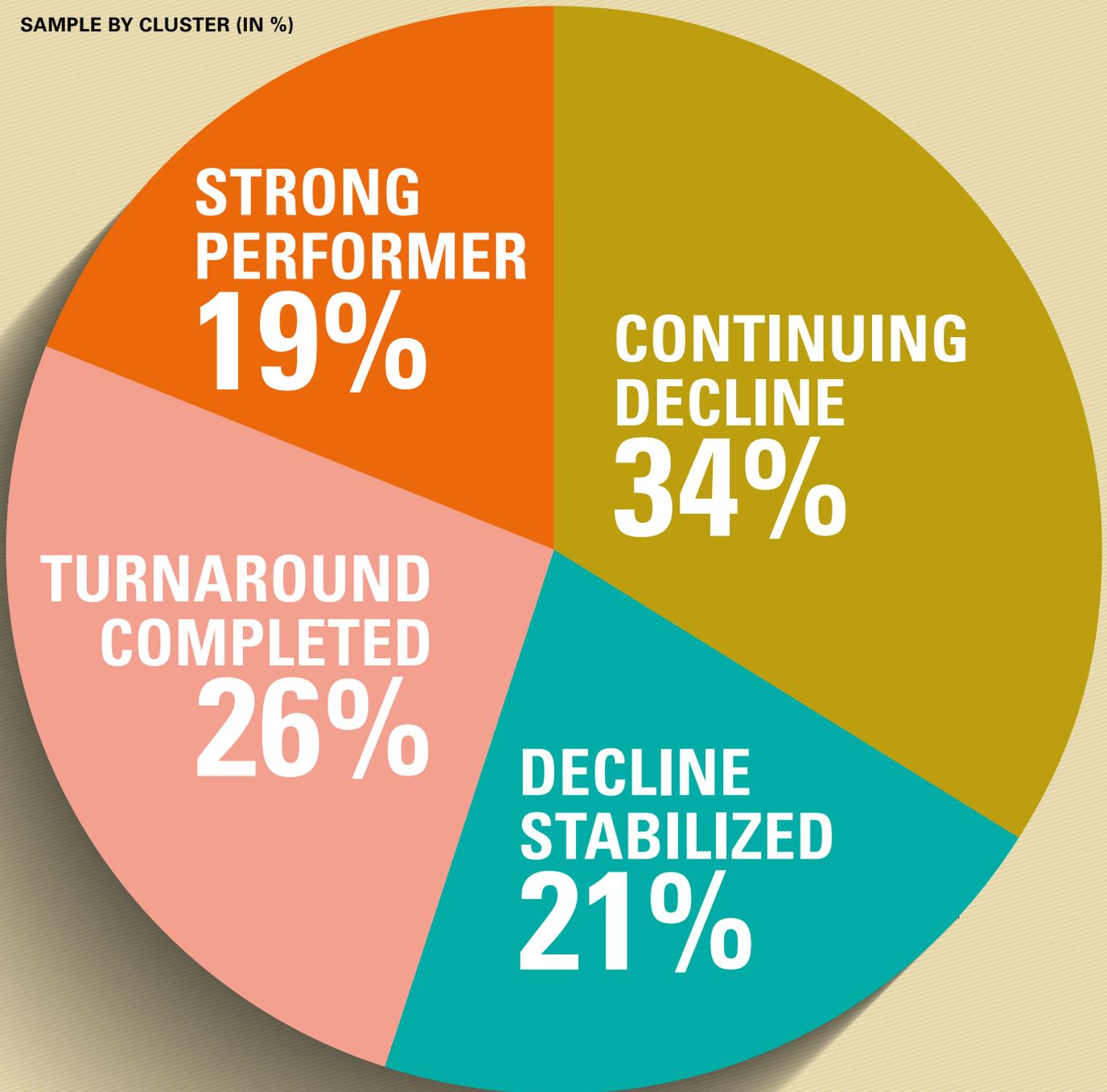
M&A pauses in 2015 but underlying drivers remain strong

An illustration of a man in a dark suit and top hat standing on a white ladder. He is looking out a window that shows a bright blue sky with white clouds. The background is a textured orange and yellow wall. The text is overlaid on a black banner across the top of the image.

34% changed CEO twice or more, but returns are far from guaranteed

There is little evidence that changing a private bank's CEO will improve financial performance. Almost half of banks in Continuing Decline changed CEO at least twice in the past nine years, compared to 12% of Strong Performers. Of a total 193 CEOs during 2006 to 2014, only eight were women.

SAMPLE BY CLUSTER (IN %)



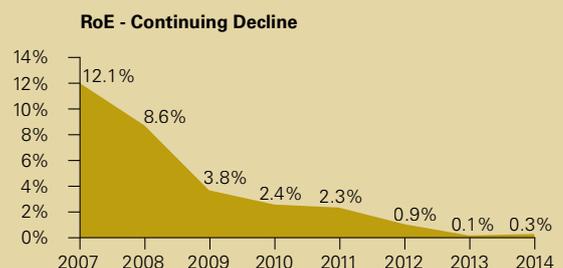
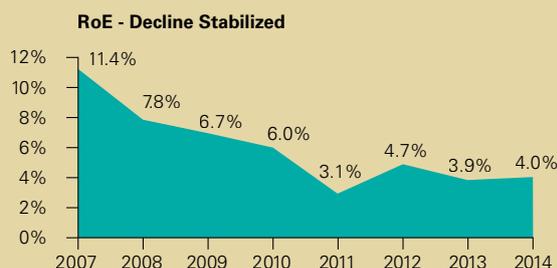
DIVERGING PATHS: BANK PERFORMANCES BECOME EVEN MORE POLARIZED

As in our previous study¹, we categorized banks according to their RoE development. The differences in the profitability of the four clusters – Strong Performers, Decline Stabilized, Turnaround Completed and Continuing Decline – became even more pronounced in 2014, with operational efficiencies and economies of scale driving improvements among Strong Performers.

Growing polarization between banking clusters

Although the profitability of the 17 Strong Performers also suffered during the financial crisis, they have since sustained relatively stable profitability at a median RoE of 9.1% in 2014. For 24 banks in Turnaround Completed, RoE picked up to reach a median of 3.9% in 2014 after an especially weak 2010 and 2011.

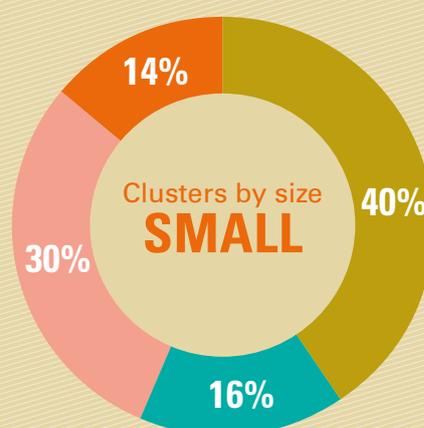
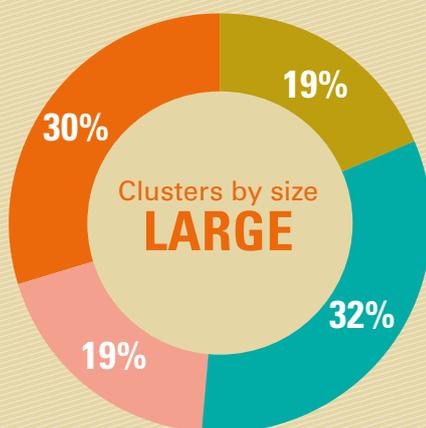
Since 2007, RoE at the 19 Decline Stabilized banks has fallen, though it seems to have stabilized at a low level in 2014 at a median of 4.0%. The 31 banks in Continuing Decline suffered the sharpest deterioration in RoE over this same period and continue to face the test of how to return to profitability. 25 of these 31 banks reported a loss (before extraordinary items) in 2014.



¹ The methodology was slightly amended compared to last year. In particular, the categorization in certain clusters was slightly changed and average values were replaced by median values.

CLUSTERS BY SIZE OF THE BANK (IN %)

- Strong Performer
- Continuing Decline
- Decline Stabilized
- Turnaround Completed



Small banks in our sample appear to be facing the biggest challenges, with 40% of them classed as Continuing Decline. Only 14% of small banks were Strong Performers, compared to 30% of large banks. Interestingly, 38% of the foreign banks were in Continuing Decline.

Strong Performers added most scale in recent years

The steepest rise in AuM between 2008 and 2014 was posted by Strong Performers, from a median of CHF2.7 billion to CHF6.5 billion over this period. This arose from relatively healthy NNM, M&A-related inflows and AuM performance that out-performed their peers. The median value hides the fact that almost one quarter of Strong Performers has AuM of more than CHF30 billion.

Strong Performers generally have greater proportions of client assets invested and USD-denominated deposits. This helped give rise to an AuM performance in 2014 of two percentage points above that of other banks.

Banks in Continuing Decline and in Turnaround Completed have the lowest median AuMs at CHF1.6 billion and CHF2.5 billion respectively. Banks in Continuing Decline have suffered continuous AuM outflows since 2009.

Significant variances in net revenue per FTE

Strong Performers generated higher net revenue per FTE with costs per FTE that are comparable to other banks. In 2014, Strong Performers' median net revenue per FTE was CHF585,000 – this was a substantial 64% above banks in Continuing Decline. Between 2008 and 2014, Strong Performers and banks in Turnaround Completed maintained their net revenue per FTE, whereas banks in Continuing Decline or in Decline Stabilized saw a fall of 20% to 25%. Strong Performers achieved this despite lower net revenue margins of around 81 basis points, which is clearly below the three other clusters.

Cost reductions and operational efficiencies boost Strong Performers

Although overall median operating costs per FTE remained almost unchanged since 2008 at CHF341,000, Strong Performers cut theirs the most (-13%), followed by banks in Decline Stabilized and Turnaround Completed (both -4%). By contrast, banks in Continuing Decline incurred a 4% increase over the past nine years.

Clear differences between the clusters emerge with regard to FTE development. Continuing Decline banks cut their headcounts the most, though these cost-cutting activities do not appear to be yielding results as decreased net revenues offset the cost saving in the same period.

Operating costs per AuM is another area with a clear gap. While operating costs to serve AuM of CHF1 million were CHF5,444 at Strong Performers, it was approximately 50% higher at other clusters. In addition it is striking that the number of employees needed by a bank to service these volumes is around 40% lower at Strong Performers (14.9 FTEs in 2014) compared to other clusters (around 26 FTEs). This reflects the operational efficiency and economies of scale Strong Performers have managed to achieve.

KEY FINDINGS

1. Strong Performers reported higher net revenue per FTE than other clusters. This is due to greater operational efficiencies and economies of scale and is a key contributor to their higher profitability. Their operational efficiency is also reflected in the operating costs to service CHF1 million AuM, which are approximately 50% higher at other clusters.
2. Overall, Strong Performers increased their median AuM by 146% since 2008, driven by higher NNM, M&A-related inflows and AuM performance.
3. The relative success of Strong Performers appears to be based on a more specific focus on core markets, operational efficiencies including outsourcing, and organic and inorganic growth initiatives.
4. While there remain some banks, including some Strong Performers, that still depend on the „Old World“ business model this approach will not survive the changes of the next few years.
5. Despite efforts across clusters to transform business models, improved profitability is most visible at Strong Performers and those in Turnaround Completed. This may be due to them starting the transformation process earlier as well as the size of the original gap between where they were and where they need to be to be successful in the new private banking world.

CEO CHANGES: NO GUARANTEE OF IMPROVED FUTURE PERFORMANCE

When times are bad, the CEO is often expected to step – or be moved – aside. There appears no evidence to suggest that this has any positive effect on the performance of a Swiss private bank. Despite CEO changes, worse performing banks appeared unable to improve their performance.

KEY FINDINGS

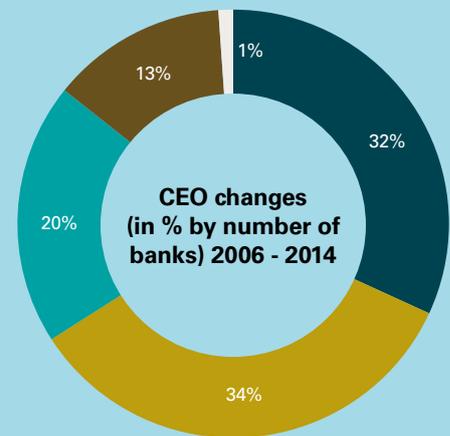
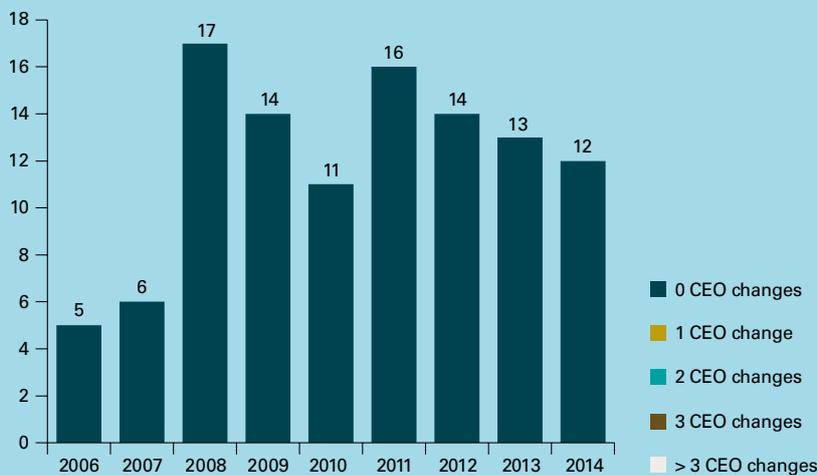
- 1.** Two thirds of banks in our sample changed their CEO at least once in the past nine years. 48% of banks in Continuing Decline changed their CEO at least twice in this period, compared to 12% of Strong Performers.
- 2.** Banks that did not change their CEO - or changed it only once - within the nine years reported higher RoEs than banks who did so twice or more.
- 3.** A CEO change does not necessarily result in staff reductions in the two years following the change.
- 4.** Out of a total 193 CEOs over the period, only eight were women. There are five female CEOs in office at the time of writing.

CEO changes are mainly due to the business environment and individual bank performance

34% of banks changed their CEO at least twice in the past nine years. The timing of the changes was influenced by the financial crisis, with the pre-crisis period seeing far fewer CEO replacements. After a moderate fall in 2009

and 2010, the number of changes in 2011 reverted almost back to 2008 levels. This may be attributed to the negative impact of the debt crisis and growing pressures on Swiss banking secrecy. The rate has steadily declined since 2011.

Number of CEO changes per year

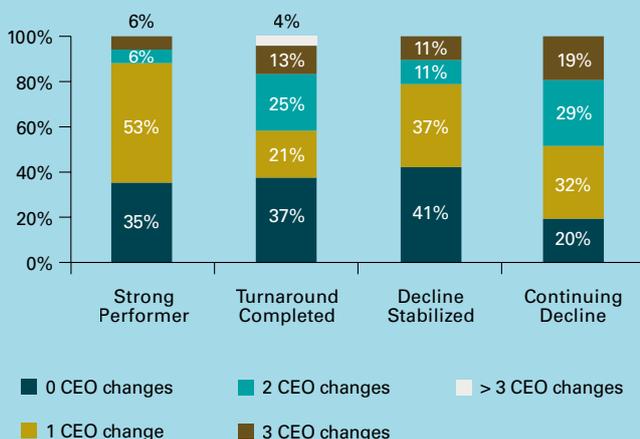


Don't change a winning team

In general, the Continuing Decline cluster saw the most CEO changes. 48% of these banks changed CEO twice or more compared to only one fifth of banks in this cluster keeping the same CEO throughout. Strong Performers

change their CEOs much less frequently - only 12% of them had two or more CEO changes in the past nine years. Banks in Turnaround Completed achieved this state with no, or at most one, CEO change (totaling 58%).

Number of CEO changes by cluster (2006 to 2014)



Fewer changes mean higher median RoE

The median RoE between 2006 and 2014 at banks that had no or only one CEO change was 4.4%. This is almost double that of other banks. Interestingly, CEO changes do not necessarily lead to greater cost-cutting such as staff reductions. Within two years following a CEO change, Strong Performers increased their median FTEs, while the other three bank clusters reported no change or a reduction.

The CEO: Still a male preserve

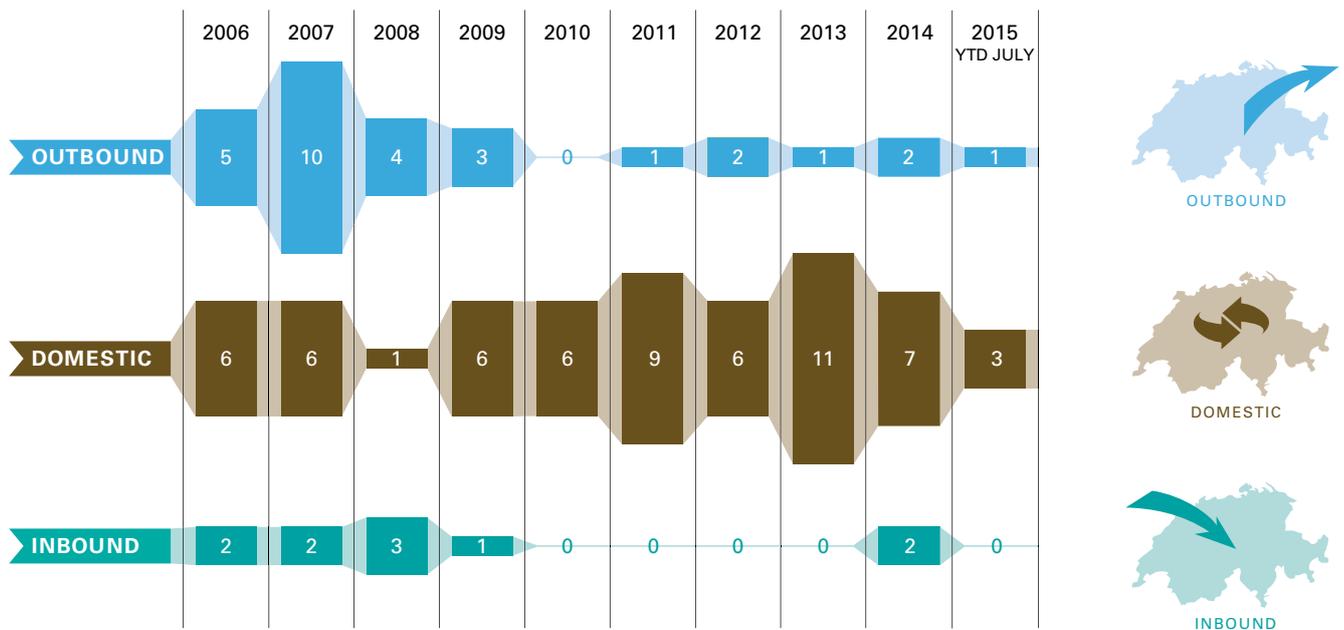
Only eight women took up CEO positions at the banks in our sample between 2006 and 2014. This represents 4.1% of the total number of CEOs who held office over this period. Out of these eight, six held or still hold the position for at least three consecutive years. As of December 31, 2014, 5.5% of bank CEOs were female.



Hitting pause: M&A stalls in 2015 while banks exit the market or fail to commit to strategic change

Various factors conspired to cause a lull in M&A activity in the first half of 2015. Most small private banks remain on the fence regarding their strategic direction. Foreign banks are more decided, but rather than pursuing M&A, Anglo-Saxon banks in particular appear to be exiting the Swiss market.

Number of announced M&A transactions involving a Swiss private bank, 2006 to 2015 YTD



KEY FINDINGS

1. Following a very active 2014, a slowdown in M&A activity in the first seven months of 2015 yielded only four Swiss private banking transactions.
2. Most of Switzerland's small private banks remain undecided whether to pursue a flight or fight strategy.
3. Foreign banks are clearer on their direction, with many pursuing an exit from the Swiss private banking market.
4. We expect a further 30% of Swiss private banks to disappear over the coming few years as a result of M&A or liquidations.

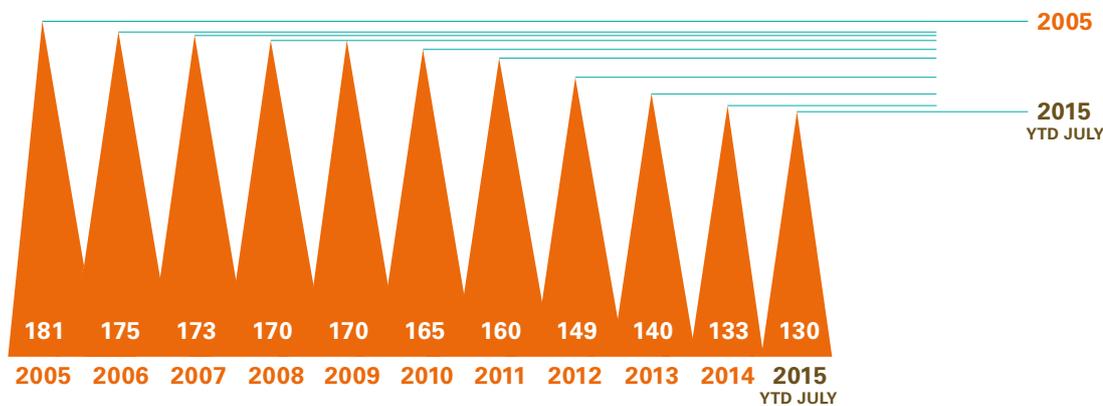
M&A hits the "pause" button in 2015

The seven months to July 2015 saw only four M&A transactions announced, compared to eight for the comparable period in 2014. Several factors drove this downturn. First was the delay in finalizing US Department of Justice Non-Prosecution Agreement negotiations. The resultant uncertainty around the ultimate levels of fines put acquisition funds and plans on delay.

Second was the SNB's removal in January 2015 of the Euro's floor value against the Swiss franc. This led to a significant appreciation of the CHF. The fall in the CHF value of EUR-denominated AuM and revenue negatively impacted banks' values. Owners of banks with a high proportion of EUR-denominated AuM may be waiting for the Euro to strengthen before deciding to sell, allowing them to request a higher price.

Third, management time continues to be diverted from growth towards implementing the increasing volume of regulatory and tax transparency compliance initiatives such as Automatic Exchange of Information (AEOI). Finally, the fact that many private banks (particularly smaller ones) are still determining their strategic direction contributed to a lack of sellers in the market.

Number of Private Banks in Switzerland



Flight or fight? Many of Switzerland's 64 small private banks seem to be undecided

The pressure on small banks to decide on flight (exiting the market) or fight (staying and changing their business and operating models) intensified in 2015. Many small banks have a high proportion of EU clients and, accordingly, EUR AuM and revenue. Depreciation of the EUR hit their profitability further as their mainly Swiss-based operations have a predominantly CHF cost base. In addition, the negative interest environment will reduce the net interest income of the banks even further.

Further, Switzerland agreed in May 2015 to implement the AEOI from 2017. This spells the end to non-tax compliant assets from clients domiciled in countries with which Switzerland will reach an agreement. This will further increase regulatory costs (e.g. one-off costs for the implementation and higher recurring costs), absorb more management time and result in asset outflows and possibly lower revenue margins.

Combined, these factors place even greater pressure on banks to decide between flight and fight.

International departures: Foreign banks exit the Swiss private banking market

The flight from the Swiss private banking market of foreign banks continued in 2015. The trend was especially strong among Anglo-Saxon banks. This included March 2015's announcement of the sale to Union Bancaire Privée (UBP) of Switzerland-based Coutts International, Royal Bank of Scotland's international private banking and wealth management business. July 2015 then saw Royal Bank of

Canada announce the sale of its Swiss private banking subsidiary Royal Bank of Canada (Suisse) to SYZ Group.

Legacy risks put off potential buyers

Potential buyers of Swiss private banks are wary of legacy risks despite banks' cleaning-up efforts and the increase in global regulatory and tax transparency compliance. Buyers require full transparency over all legacy risks if they are to effect a share deal. However, some sellers still struggle to accept that legacy risks need to be indemnified if they wish a share deal to go ahead.

Some buyers prefer to reduce legacy and litigation risk by pursuing asset deals involving the purchase of client relationships and CRMs. However, major challenges such as a higher risk of client attrition have come to light in recent asset deals.

Disappearing act: A further 30% of Swiss private banks will exit over the next few years

When Swiss private banks better understand the impacts on their business of tax transparency initiatives – and when smaller Swiss private banks decide on their strategic direction – we expect the "pause" button to be released and M&A activity to pick up.

Consolidation will also continue through liquidations. The number of Swiss private banks has already fallen from 170 at 31 December 2008 to 130 at 31 July 2015, being a 24% reduction. We believe this trend will continue with another 30% of banks exiting the Swiss private banking market in the next few years.

Private banking transactions 2014 and first seven months of 2015

Announced	Target	Bidder	AUM (CHFbn)	Transaction Type
2015				
July	NSC Asesores	Julius Baer Group	3.0	Share deal
July	RBC (Suisse)	SYZ Group	10.0	Share deal
March	Coutts International	Union Bancaire Privée	32.0	Asset deal
February	Bank La Roche	Notenstein Private Bank	6.5	Asset deal
2014				
November	Banca Arner	IXE Capital	n/a	Share deal
August	LBBW (Switzerland)	Notenstein Private Bank	1.0	Asset deal
August	Vadian Bank	St. Galler Kantonalbank	0.7	Share deal
July	Banque Privée Espírito Santo (portfolio of Iberian and Latin American client assets)	CBH Compagnie Bancaire Helvétique	n/a	Asset deal
July	Leumi Private Bank (Switzerland)	Julius Baer Group	4.2	Asset deal
July	BSI	Banco BTG Pactual	89.4	Share deal
June	HSBC Switzerland (several portfolios of international private clients and external asset managers)	LGT Group	7.7	Asset deal
May	Valartis Bank (Schweiz)	Banque Cramer & Cie	1.8	Share deal
April	Bank Morgan Stanley (Switzerland)	Bank J. Safra Sarasin	10.0	Asset deal
March	GPS Investimentos Financeiros e Participações (increased existing 30% stake to 80%)	Julius Baer Group	6.5	Share deal
January	Falcon Private Bank (Hong Kong branch)	EFG International	0.5	Asset deal

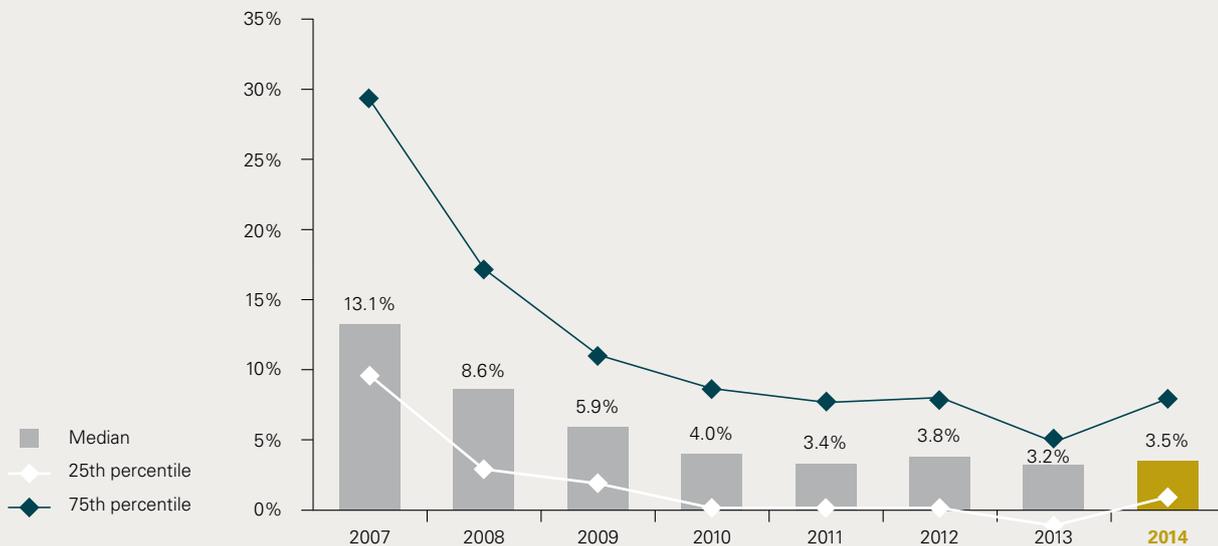


Analysis of performance and trends

Profitability

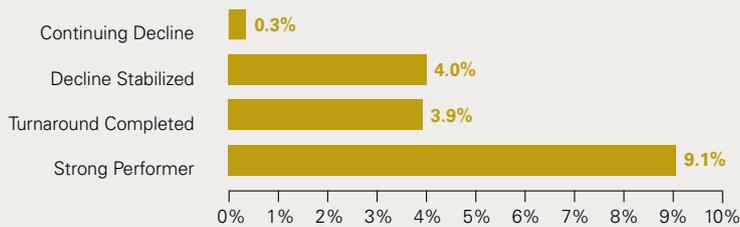
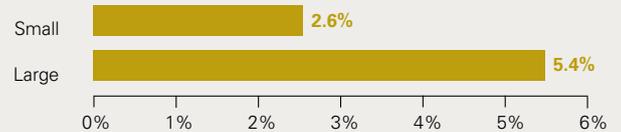
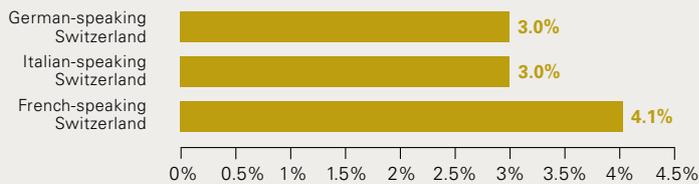
Relatively poor performance persisted throughout 2014. A stable but low RoE of 3.5%, however, hides the increasing polarization of Swiss private banks as they separate into clear winners and losers.

RoE development 2007 to 2014



2014 KEY FINDINGS

- Reported RoE remained very low at 3.5% as banks were unable to improve their performance despite a positive development of financial markets.
- There is a significant range in banks' performances, with Strong Performers reporting a RoE of 9.1% and banks in Continuing Decline reporting 0.3%.
- Around half of banks improved their RoE in 2014 - mostly those in Turnaround Completed or Strong Performers.
- The proportion of loss-making banks fell from 39.2% in 2013 to 28.6% in 2014 driven by less provisions for the US Tax Program.
- Large banks reported higher RoE (5.4%) than small banks (2.6%), being a wider gap than in 2013.
- Median RoE of banks that made significant acquisitions between 2010 and 2013 rose by around 1.4 percentage points in the two years following the acquisition.

RoE development 2014**By cluster****By size****By location****RoE remains unsustainably low**

Reported RoE remained relatively stable at a very low 3.5% in 2014 compared to 3.2% in 2013. During 2014, half of banks (47 banks or 52%) reported a rise in RoE (of which 18 saw an increase of greater than five percentage points) while the other half experienced a decline (of which ten saw a fall of greater than five percentage points).

RoE at 25 banks (or 27%) deteriorated in each of the past two years, while at 16 banks (or 18%) RoE increased over the same period. Only nine banks reported a continuous increase in RoE over the past three years.

80% of banks reported an RoE of less than 8%, which is lower than the 8% to 10% that could be expected for a private bank depending on its business model.

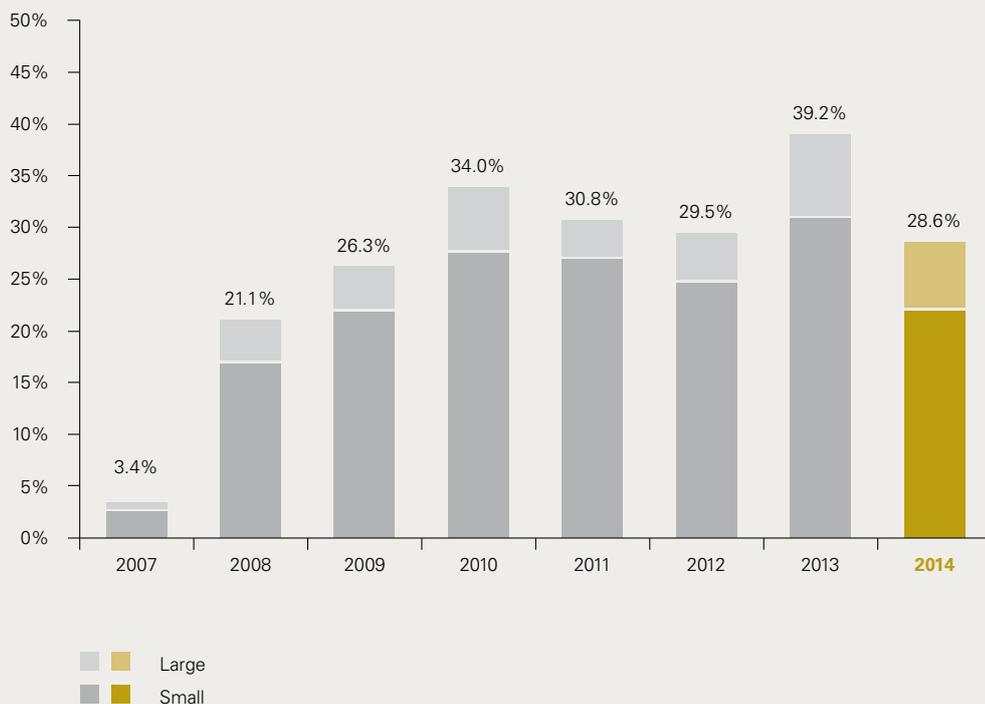
As of December 31, 2014, three banks in our sample had disclosed that they would enter into liquidation. Each had built provisions of CHF4 million to CHF8 million to cover related costs.

Impact of extraordinary items at a very low level

2014 saw among the lowest proportion of extraordinary items in RoE since 2007, at 0.8 percentage points. After removing extraordinary income and expenses, 2014's RoE amounted to 2.7%, being an increase of one percentage point over 2013. This reflects the reduced impact of the US Tax Program provisions and some banks achieving operational improvements.

The effect of extraordinary items on RoE appears significantly higher for banks in Continuing Decline compared to other clusters. This demonstrates that banks in Continuing Decline are more tempted to try to improve their results.

Percentage of loss-making banks 2007 to 2014 (before extraordinary items)



Fewer loss-making banks, but many still remain

In 2014, 26 banks reported a loss before extraordinary items. This was down from 38 in 2013. For 14 of these 38, the loss in 2013 was mainly due to provisions recorded as part of the US Tax Program.

Nine banks (mostly small banks in Continuing Decline) have made constant losses since 2011. A further three reported a loss in 2014 for the first time since 2007 mainly due to higher costs, greater provision requirements or a strong decline in operating income.

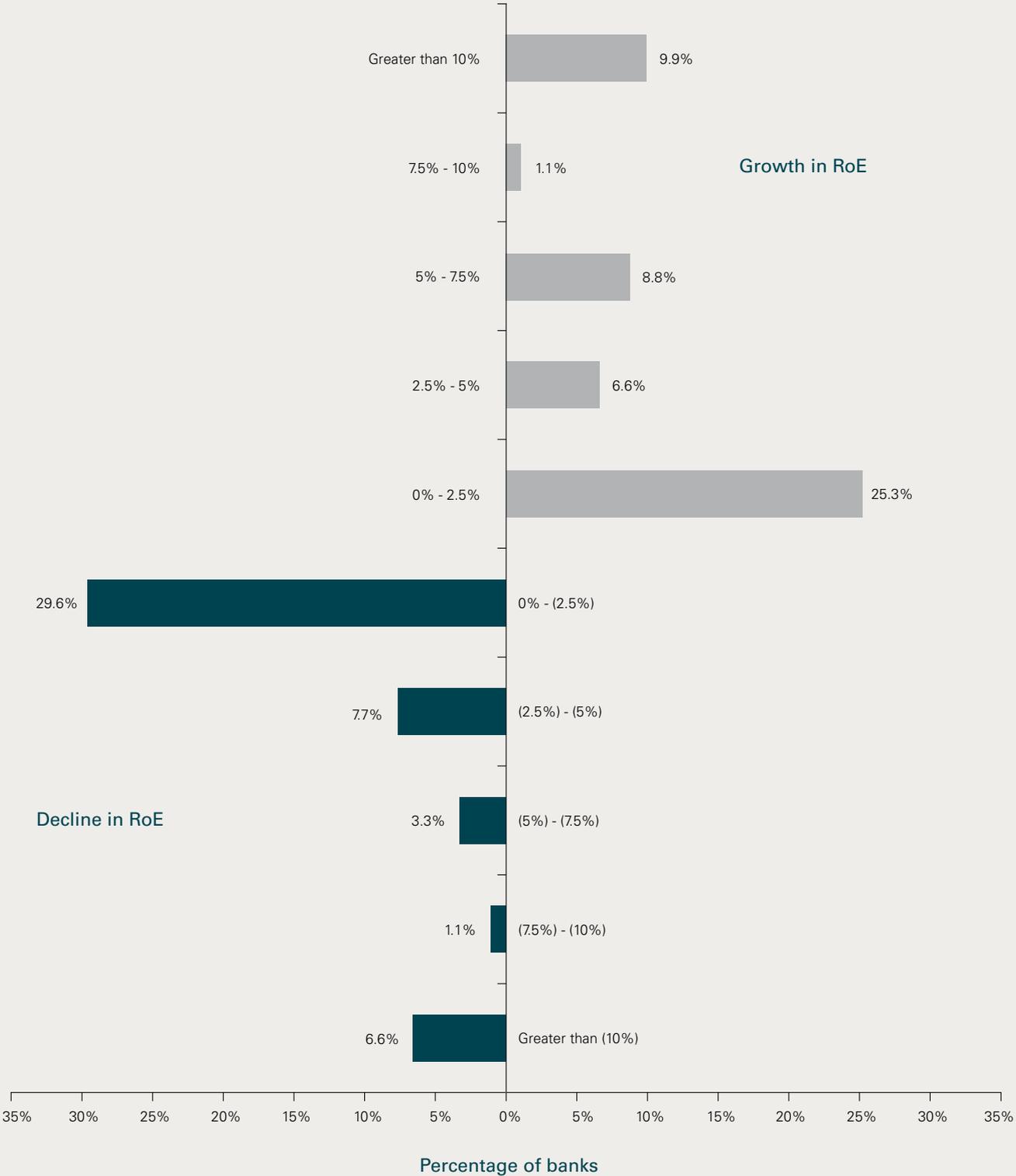
Six banks had been consistently loss making since at least 2009 but returned to profit in 2014. This was primarily through increasing AuM, reduced US tax-related provision requirements and/or the positive result of restructuring effects.

Linking M&A and performance

The median RoE of banks which made significant acquisitions between 2010 and 2013 (each transaction representing at least 10% of their AuM) rose by around 1.4 percentage points in the two years following the acquisition (or one year for acquisitions in 2013).

39 banks that returned their banking license or were acquired in the past five years had suffered from an average decline in RoE of 2.5 percentage points in the two years prior to such a move. 24% had incurred losses in the two years prior to returning their license or being required and 71% were foreign-controlled.

Change in RoE (percentage points) 2013 to 2014



Assets under Management

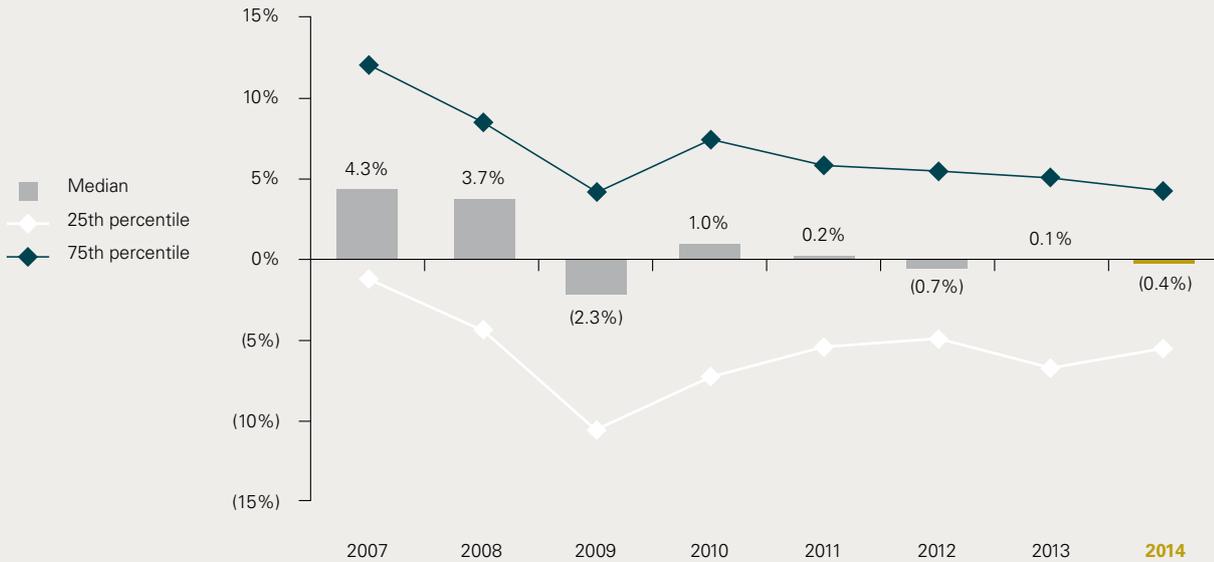
A significant increase in overall AuM was reported in 2014, driven by positive market and foreign exchange impacts. Despite this rise of CHF103 billion or 7.3% in AuM, the industry proved unable to generate substantial NNM, at only CHF7.0 billion or 0.5% of AuM.

Development of gross AuM 2013 to 2014



2014 KEY FINDINGS

- An increase in AuM from CHF1,406 billion to CHF1,509 billion was mainly due to the contribution of positive equity market developments and strong appreciation of the USD.
- No meaningful NNM has been generated since 2009 despite overall growth in global private wealth. This illustrates the erosion of Swiss private banks' market share.
- Strong Performers and banks in Turnaround Completed reported net inflows of CHF24.9 billion in 2014. Banks in Continuing Decline or Decline Stabilized suffered total net outflows of CHF17.9 billion. This highlights the capacity to grow organically as a key success factor.
- A focus on specific client segments and exit of particular markets, as well as repatriations and regularization of legacy cross-border business, drove part of the outflows.
- Strong Performers more than doubled their median AuM between 2008 and 2014, driven by NNM, performance and M&A activity.
- In 2014, eight banks in our sample reported the closure of eight M&A deals with total acquired AuM of CHF19.3 billion.
- Larger banks' market share grew further in 2014 as 27 large banks in our sample represent 88.7% of total AuM (2013: 84.8%).

NNM contribution to AuM 2007 to 2014**Extremely low levels of NNM**

The positive market environment and the strengthening of the USD during 2014 drove the increase in AuM from CHF1,406 billion to CHF1,509 billion. The industry's low NNM of CHF7.0 billion (or 0.5% of AuM) reflects the difficulties most banks face in growing their businesses. In particular, 55% of banks reported net outflows, being a similar proportion across small and large banks. One third of banks experienced net outflows of more than 5% of AuM. In addition, 33% of small banks and 22% of large banks suffered net AuM outflows in each of the past three years.

NNM has been consistently very low at or below 1% of AuM for the past six years. Large banks generally reported higher NNM. Banks based in French-speaking Switzerland reported lower NNM in 2014 than those in other regions.

Over the course of 2014, three banks in our sample returned their banking license as a result of financial difficulties or strategic realignments. The net impact on AuM in our sample was a reduction of CHF7.8 billion, where client assets were either terminated or transferred to other group or third party banks.

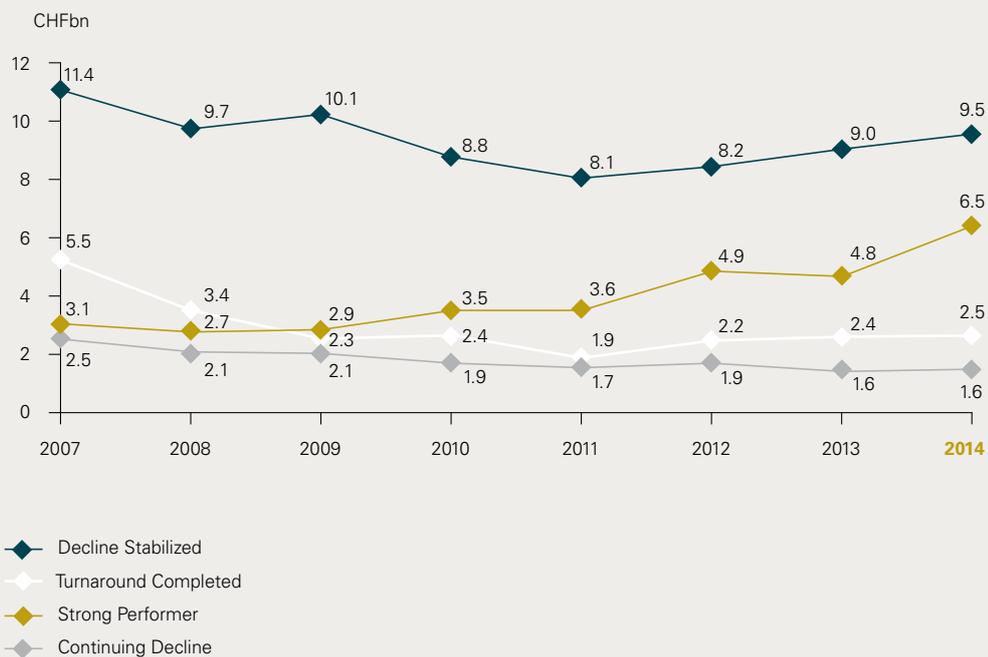
Strong Performers gained scale through NNM, M&A and better AuM performance

The median AuM of Strong Performers more than doubled from CHF2.7 billion in 2008 to CHF6.5 billion in 2014. Over this period, these banks reported total NNM of CHF50.7 billion and M&A-related inflows of CHF108.8 billion. Strong Performers also reported better AuM performance in 2014 at 7.1% compared to 5.1% for other banks. Strong Performers generally have a greater proportion of client assets invested and a higher proportion of deposits denominated in USD.

2014 saw the closure of acquisitions representing AuM totaling CHF19.3 billion

During 2014, eight banks in our sample reported the closure of acquisitions with AuM totaling CHF19.3 billion across eight transactions. 16 banks in our sample were involved as either acquirer or target, which resulted in a slight net increase of CHF4.9 billion in our sample’s AuM. As most of these transactions represent in-market activities (transactions within the sample), it results in a low net market impact. Large and small banks alike made acquisitions during the year.

Median AuM per cluster 2007 to 2014

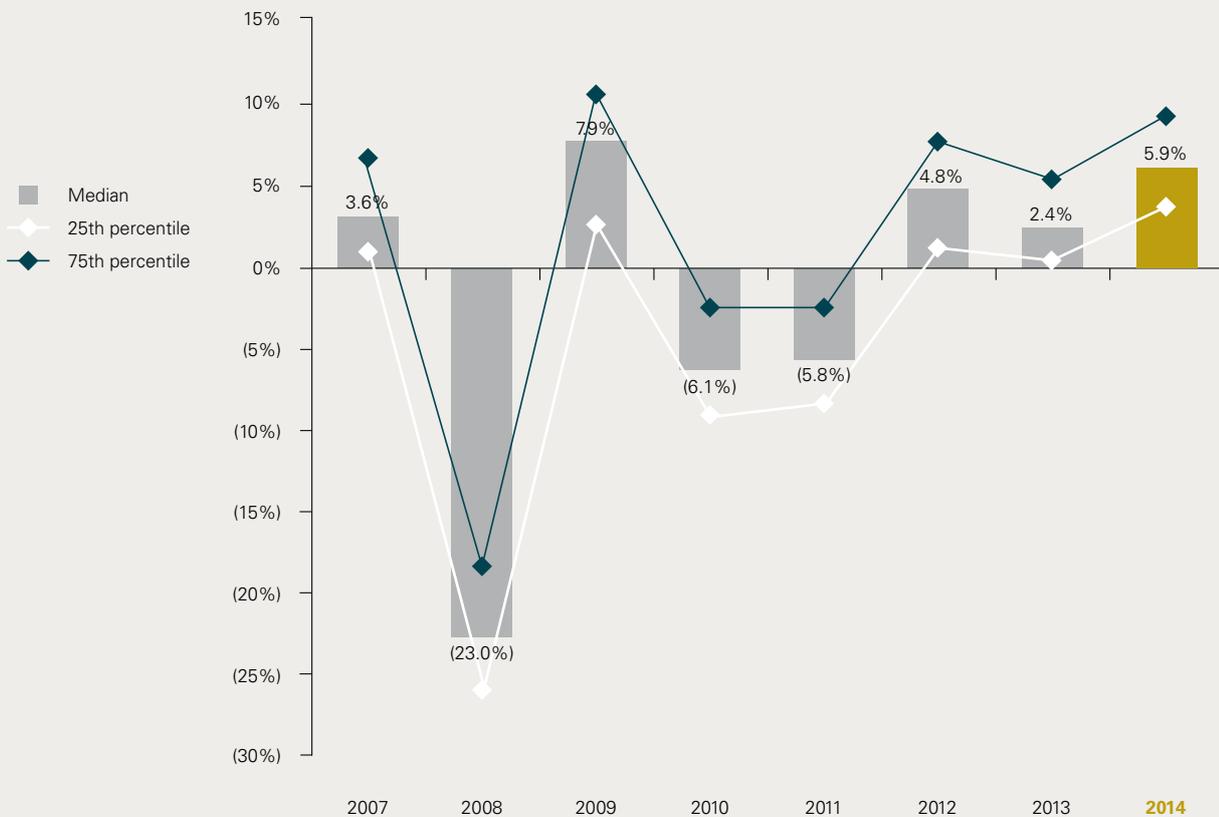


Markets and FX: Strong contribution in 2014, but negative FX effects expected in 2015

With a median performance contribution of 5.9%, 2014 saw the highest market and FX impacts (mainly USD-related) since 2009. The vast majority of banks enjoyed a positive performance in this regard in 2014.

Many banks will be significantly impacted by January 2015's SNB decision to lift the EUR/CHF peg. This is due to Swiss banks seeing a reduction in revenue from EUR-denominated AuM while maintaining costs bases that are largely denominated in CHF.

Performance contribution to AuM 2007 to 2014



Revenue development

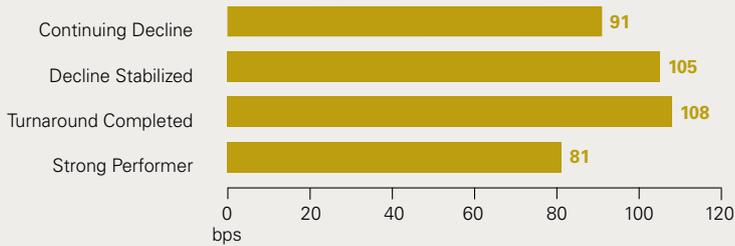
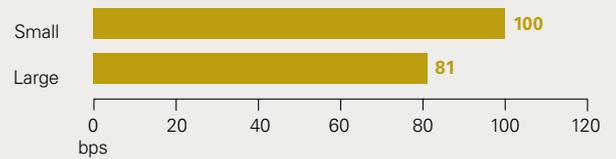
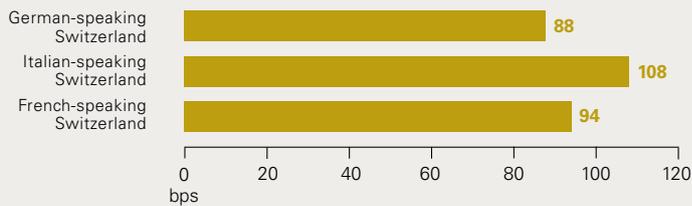
While the erosion of net revenue margins continued, Strong Performers generated higher revenue per FTE than other clusters. Both Strong Performers and banks in Turnaround Completed were able to grow net revenue per FTE without shedding employees, for instance through the positive impact of NNM and M&A transactions. Small banks however suffer from a lack of economies of scale - this is reflected in much lower revenues per FTE despite their higher revenue margin.

Margin development 2007 to 2014



2014 KEY FINDINGS

- The erosion of net revenue margins continued in 2014 by four basis points to 93bps, mainly due to the low interest rate environment and ongoing pressure on commission margins.
- Strong Performers generated lower net revenue margins than other banks. However, their revenue per FTE is higher, demonstrating greater productivity and economies of scale.
- Gross and net profit margins were stable at 17bps and 9bps respectively, mainly thanks to the lower impact of provisions.
- Small banks earned substantially higher net revenue margins (100bps) than large banks (81bps).

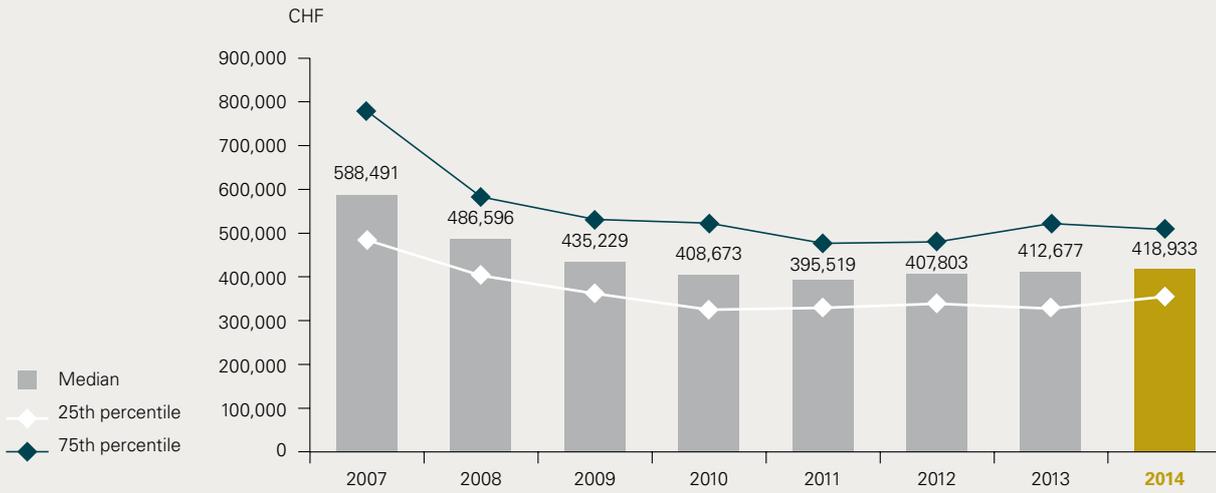
Net revenue margin 2014**By cluster****By size****By location****Further erosion of net revenue margins**

A deterioration of interest and commission margins drove a reduction in 2014's net revenue margins. Direct causes for which banks have been unable to compensate include the lower interest rate environment and ongoing pressure on commissions and fees due to increased competition, changes in customer segments and lower margins on tax compliant client assets. Net revenue margins fell at 61 banks (or 67%) in 2014: higher than 10bps for 22 banks and fell constantly in each of the past three years for 15 banks (or 16%).

While the revenue mix remained relatively stable compared to 2013, small banks tend to generate a larger proportion of their revenue from commission income (67% vs 61% for large banks), while interest income represents a higher proportion of revenues at large banks (21% vs 17% for small banks).

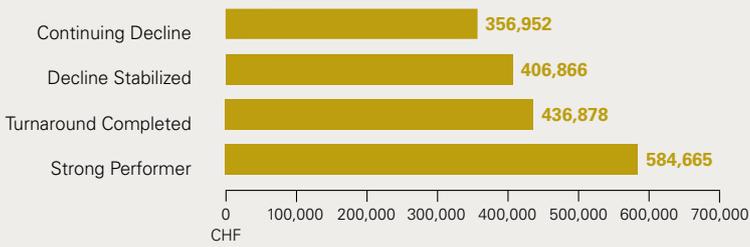
Banks based in Ticino earn higher margins due to a greater proportion of small banks and discretionary mandates as well as typically having smaller clients. However, Ticino's banks suffered the largest fall in net revenue margins from 128bps in 2009 to 108bps in 2014. On the other side of the Gotthard, net revenue margins fell slightly less abruptly by 10bps from 98bps in 2009 to 88bps in 2014.

Net revenues per FTE 2007 to 2014

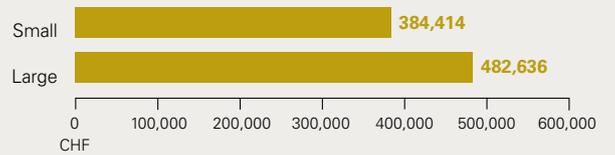


Net revenues per FTE 2014

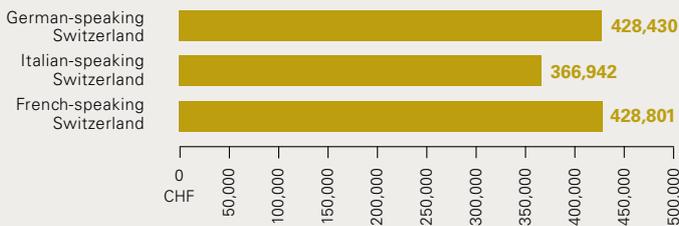
By cluster

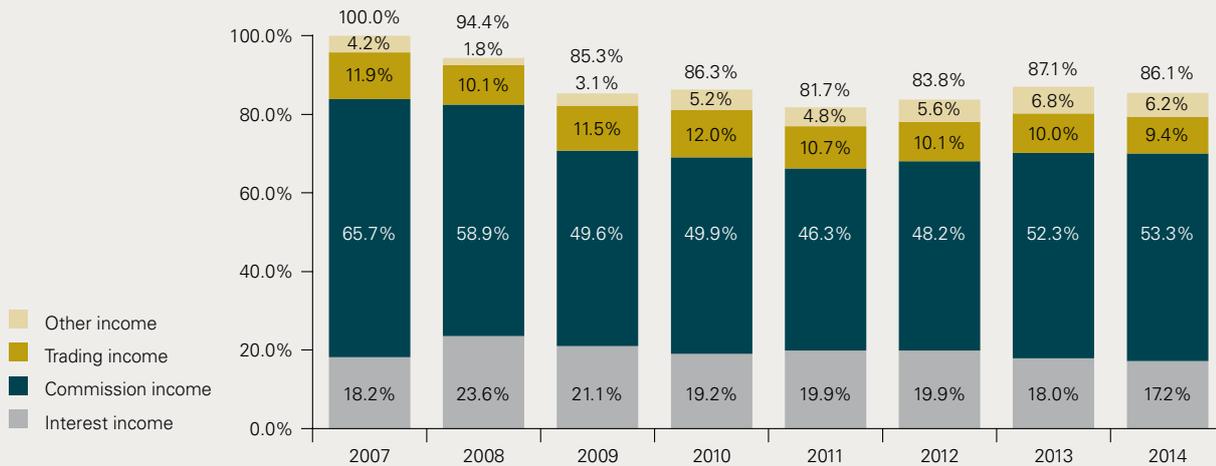


By size



By location



Net revenue development 2007 to 2014 (base: net revenues 2007, constant sample)**Strong Performers: Lower net revenue margins**

The net revenue margin at Strong Performers of 81bps is generally lower than at other banks. They have also seen the second most significant margin decrease since 2008 (-16bps compared to -24bps for banks in Continuing Decline), mainly driven by pressure on commission and fees.

Net revenue per FTE vs headcount protection

In the nine years covered by our study, net revenues per average FTE hit their lowest point in 2011 at CHF396,000. They have since risen by 5.9% to CHF419,000 in 2014. Turnaround Completed banks drove this increase (+14.6%) following a substantial 20.7% decrease between 2008 and 2010. Levels remain far below 2007, however.

A marked difference exists between the four clusters. Strong Performers recorded net revenue per FTE of CHF585,000 compared to CHF357,000 at those in Continuing Decline. Strong Performers and Turnaround Completed banks were able to lower their FTE to AuM billion ratio without materially reducing their employee base. By contrast, banks in Continuing Decline and Stabilized Decline both experienced a decrease in

net revenue per average FTE despite reducing headcount as decline revenues were declining even more than the implemented headcount reductions.

At 100bps, small banks' net revenue margins continued to be significantly higher than larger banks' (81bps). However, net revenue per average FTE is significantly lower (CHF384,000 for small banks vs CHF483,000 for large banks). This illustrates the scale effect as small banks require 26 FTEs to manage CHF1 billion of AuM compared to 17 FTEs for large banks. Net revenue per average FTE also rose more significantly at large banks since 2011 (+9.5%) than at small banks (+3.8%).

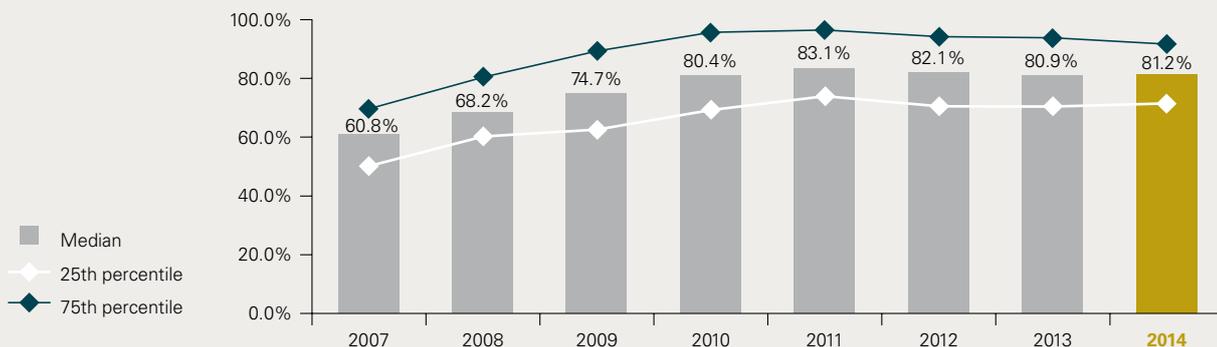
M&A: Positive impact on net revenue per FTE for acquirers

Net revenue per FTE of banks that made significant acquisitions between 2010 and 2013 (representing at least 10% of their AuM) rose by a median 5.1% in the two years following the acquisition (or one year for acquisitions in 2013), reflecting the positive efficiency gains to be had by gaining scale.

Cost development

Greater regulatory compliance costs continued to contribute to the industry's high cost base, with banks being generally unable to improve their cost-income ratios. Cost-saving measures yielded only limited benefits. In the key cost element – personnel expenses – average costs per employee increased slightly and headcount fell only by a limited degree.

Cost-income ratio 2007 to 2014



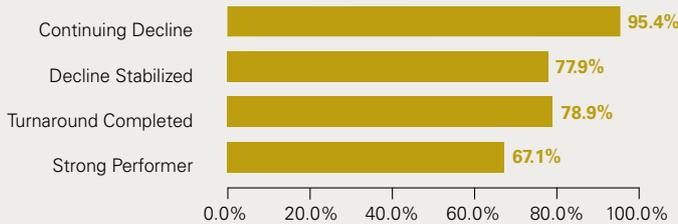
Note: cost-income ratio is calculated excluding depreciation

2014 KEY FINDINGS

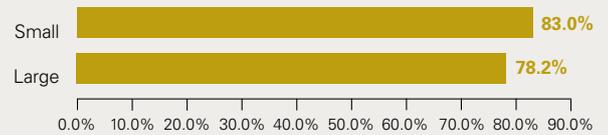
- Cost-income ratio remained high at 81.2% as the industry was unable to reduce its cost base and was further impacted by increased regulatory compliance and remediation costs, including those relating to the US Tax Program.
- An average of 23 FTEs is employed to serve CHF1 billion of AuM, with significant differences between small and large banks, regions, performance clusters and operational set-ups.
- Operating costs to manage CHF1 million of AuM were around CHF7,800, of which 64.7% was personnel costs. This percentage has fallen over the past three years.
- The total number of FTEs in our sample fell slightly from 26,564 in 2013 to 25,987 in 2014.

Cost-income ratio 2014

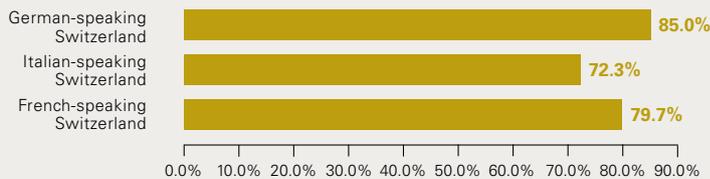
By cluster



By size



By location



Limited impact of cost-saving measures

The slight fall in cost-income ratio observed since 2011 slowed down in 2014 as the ratio remained at a high 81.2%. As in previous years, the benefits of several banks' cost-saving measures have been offset by declining revenues and higher costs of regulatory compliance and remediation programs, which have continued to significantly impact banks' cost bases.

40 banks (or 44%) managed to reduce their cost-income ratios in 2014. These reductions were greater than five percentage points for 21 banks (23% of our sample) and fell continuously in each of the last three years for 11 banks (mostly banks in Turnaround Completed).

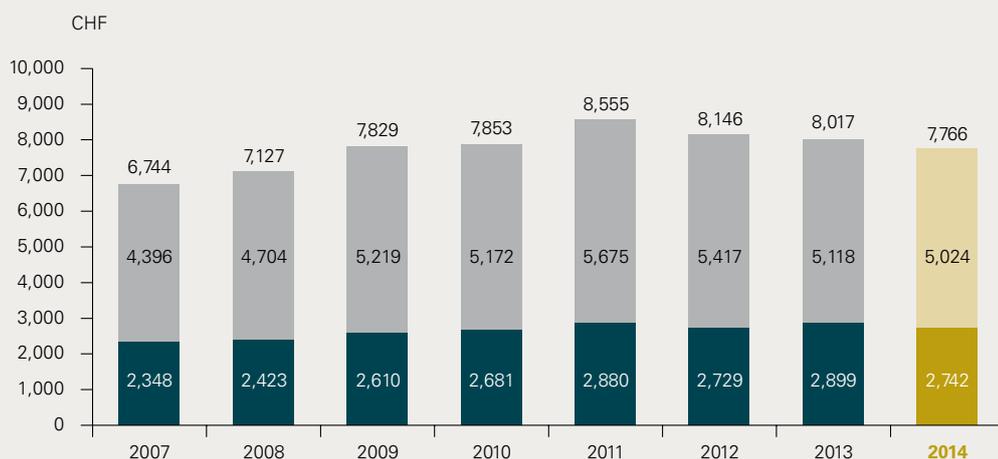
Banks in Turnaround Completed achieved the strongest fall in cost-income ratio (-12 percentage points since 2011) while increasing their headcount by 15.9%. This was achieved through scale (+31.4% in median AuM per bank since 2011) and improved productivity, resulting in higher revenue per FTE (+14.6%) and lower costs per AuM (-22.9%).

Ticino-based banks have generally lower cost-income ratios due to their higher net revenue margins. Operating expenses of CHF7,762 to manage CHF1 million in AuM are comparable to other regions despite lower personnel expenses per employee (CHF181,600) which offset the higher number of employees per AuM (31.9 FTEs per billion CHF of AuM).

Greater efficiencies at Strong Performers

When considering the lower net revenue margin earned by Strong Performers, the difference in cost-income ratio between them and other clusters is striking. The apparently more efficient operational set-up and greater economies of scale of Strong Performers seem to explain their substantially lower number of employees per AuM (14.9 FTEs per billion CHF of AuM vs around 26 FTEs in the other clusters). Personnel costs per employee, however, are 13.1% higher than at banks in Continuing Decline, which suggests that Strong Performers have been able to attract staff that are more productive but also more expensive. Nevertheless, operating costs to serve AuM of CHF1 million were CHF5,444 at Strong Performers – this was approximately 50% higher in other clusters.

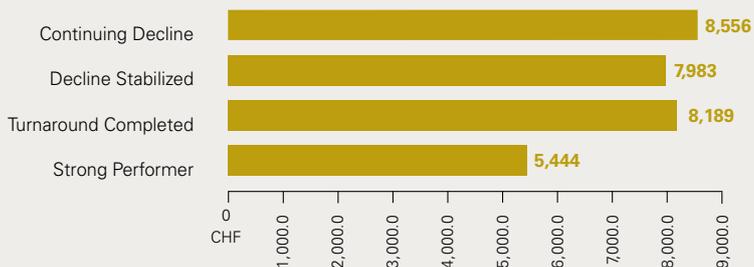
Total operating costs per CHF1 million in AuM 2007 to 2014



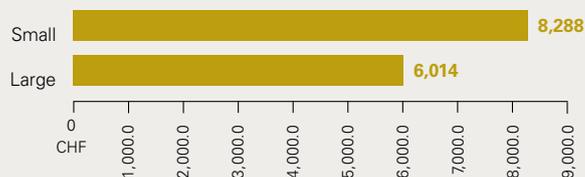
■ Other operating expenses per CHF1 million in gross AuM
 ■ Personnel expenses per CHF1 million in gross AuM

Total operating costs per CHF1 million in AuM 2014

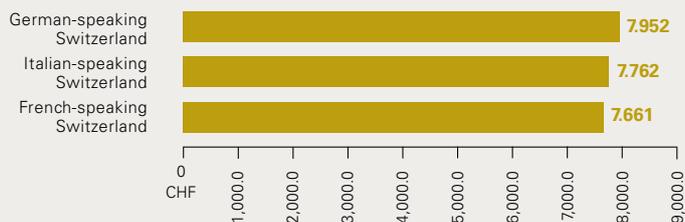
By cluster



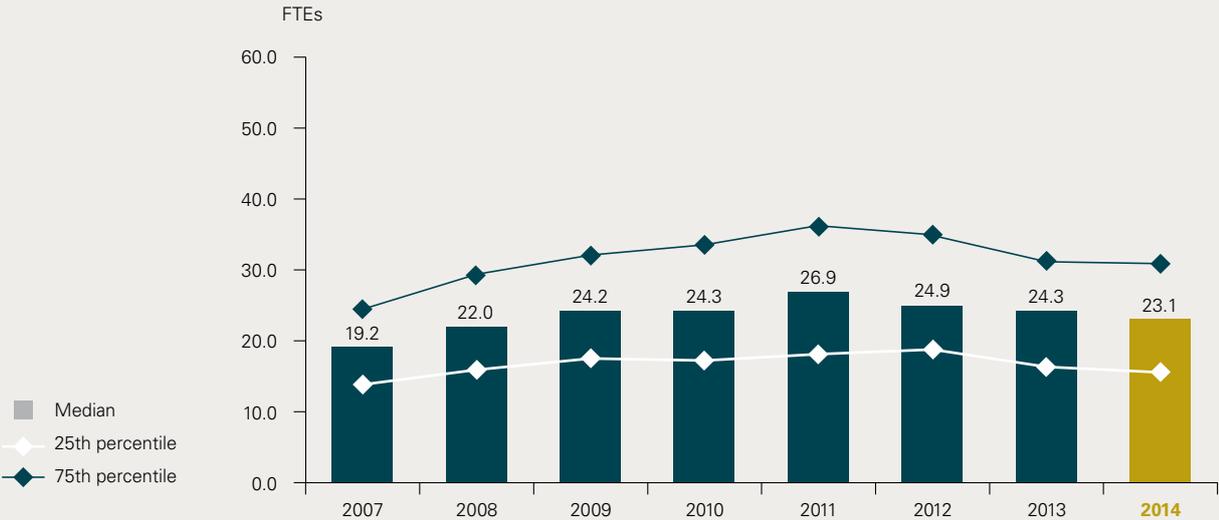
By size



By location

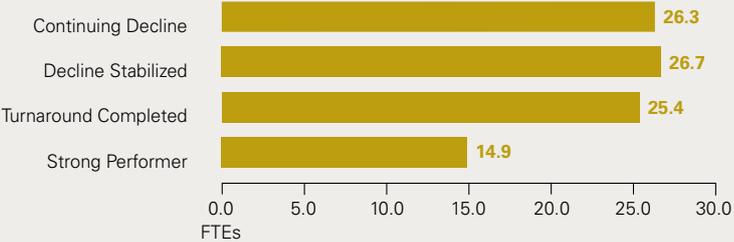


Number of FTEs to serve CHF1 billion in AuM 2007 to 2014

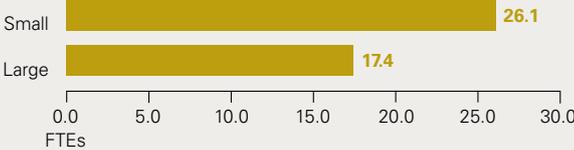


Number of FTEs to serve CHF1 billion in AuM 2014

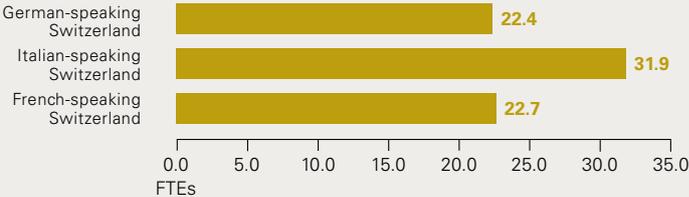
By cluster



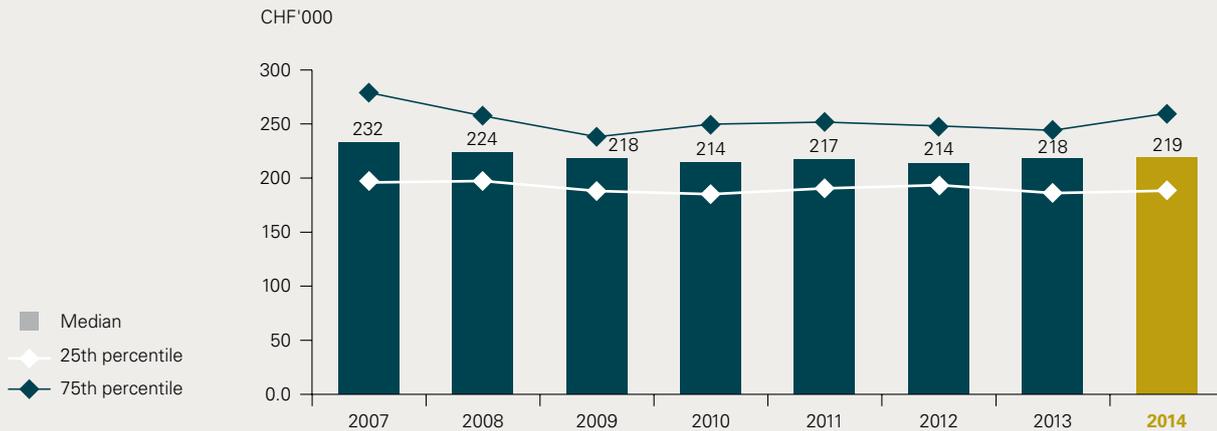
By size



By location



Personnel expenses per FTE 2007 to 2014



US Tax Program continues to hit bank profitability

Due to significant delays regarding the US Tax Program, only 16 banks in our sample had reached an agreement with the US authorities by the end of July 2015. These have agreed to pay penalties totaling CHF424 million (of which CHF211 million is for one individual bank). This represents an average of 3.9% of the maximum US AuM held during the relevant period. Based on available information, five banks in our sample decided to withdraw from the US Tax Program in 2014 following an in-depth analysis.

The impact on the industry's profitability in 2014 is difficult to quantify given the more limited disclosures compared to the prior year. Valuation adjustments, provisions and losses fell from 12.6% in 2013 to 5.2% of gross profit in 2014, although this is relatively higher than in 2012 and before. Some banks released US Tax Program-related provisions booked in 2013. Significant professional fees continued to be incurred in 2014, contributing to the pressure on cost-income ratios.

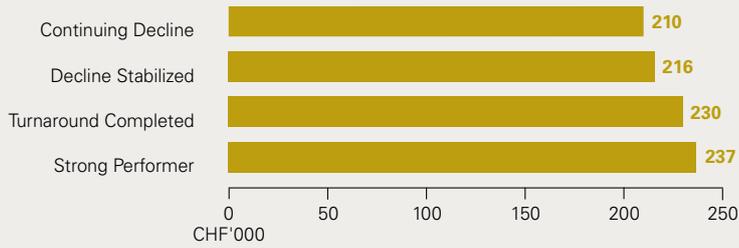
Stable average employee costs despite a slight decrease in employee numbers

The total number of employees in our sample fell by 2.2% to 25,987. Falls were seen at both large banks (-232 FTEs) and small banks (-87 FTEs) as well as at the three banks that returned their licenses (-259 FTEs). Almost one fifth of banks reduced their number of FTEs by more than 5% during 2014, half of them being banks in Continuing Decline. Another quarter added more than 5% of FTEs to its workforce. The proportion of compliance-related personnel also rose significantly in recent years.

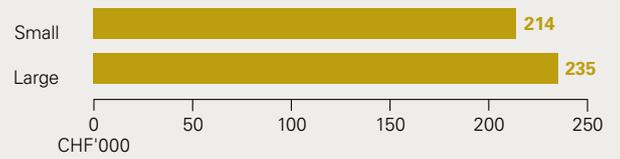
Personnel costs per employee overall remained stable at CHF219,000. This has risen by 5.5% since 2011 at Strong Performers (to CHF237,300 in 2014) and fallen by 3.3% at banks in Continuing Decline (to CHF209,800 in 2014). Personnel costs per employee are generally 9.8% higher at large banks than at small banks and 18.5% lower at Ticino-based banks compared to the rest of Switzerland.

Personnel expenses per FTE 2014

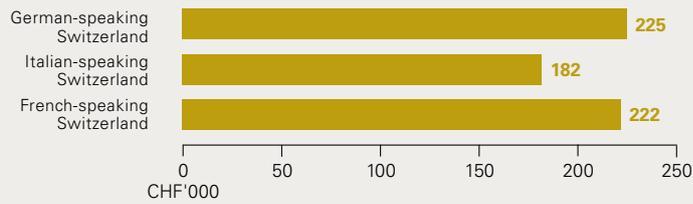
By cluster



By size



By location



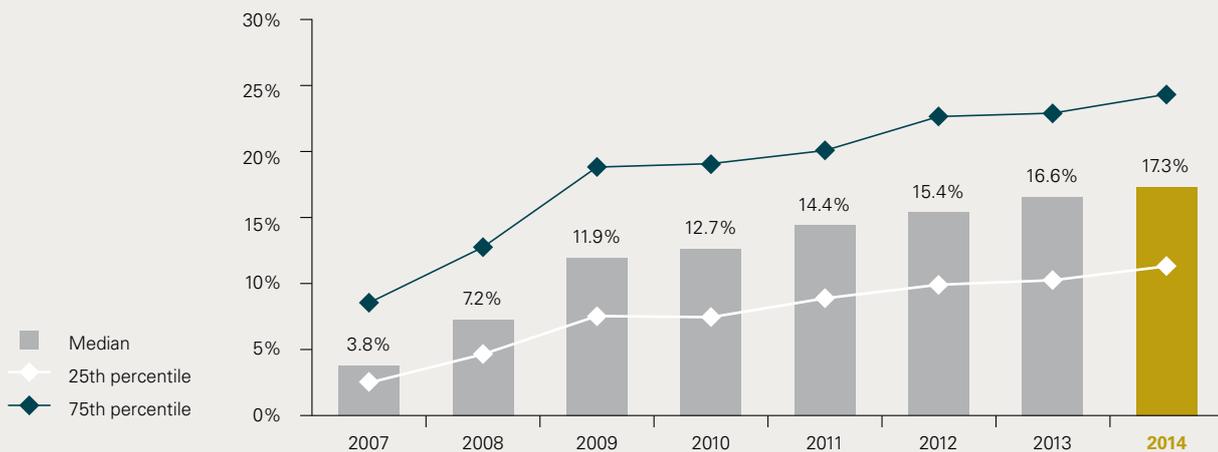
M&A gives rise to observable cost synergies

Banks that made significant acquisitions between 2010 and 2013 (representing at least 10% of their AuM) saw a median reduction in their cost-income ratio and operating expenses to manage CHF1 million in AuM of one percentage point and 1.7% respectively in the two years following the acquisition (or one year for acquisitions in 2013), with significant differences across the transactions.

Balance sheet and regulatory capital

RoE is negatively impacted by the significant excess regulatory capital held by most banks. Only one third of the sample banks paid dividends in the past two years, but with very high payout ratios.

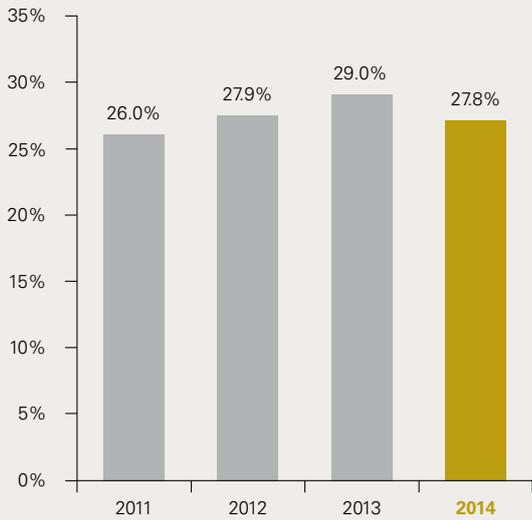
Customer deposits as a percentage of net AuM 2007 to 2014



2014 KEY FINDINGS

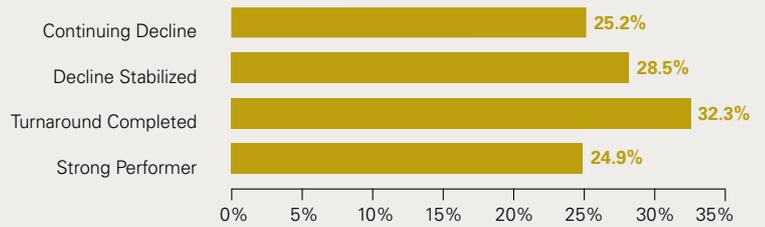
- The significant increase in client deposits was mainly due to the USD/CHF exchange rate development and portfolio reallocations.
- Small banks overtook large banks in terms of capital adequacy levels, though both categories show strong capital positions.
- 2014 was characterized by significant growth in the Lombard and mortgage loan business, driven by the low interest environment and dynamic financial markets.
- Only one third of the sample's banks paid dividends in the past two years, but showed very high payout ratios.

Total capital ratio 2011 to 2014

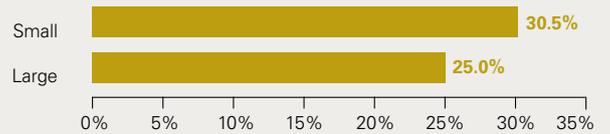


Total capital ratio 2014

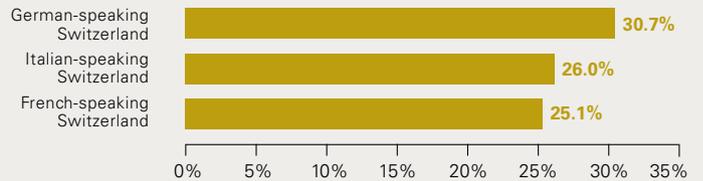
By cluster



By size



By location



Increasing customer deposits driven by USD/CHF exchange rate

Amounts due to customers (presented in CHF) increased in 2014 largely due to the USD/CHF exchange rate development and increased customer deposits in EUR as a result of portfolio reallocations. Deposits have grown relative to net AuM since 2007 from 3.8% to 17.3% in 2014, indicating that customers still have a strong risk awareness. The high cash proportion reduces banks' ability to achieve revenues.

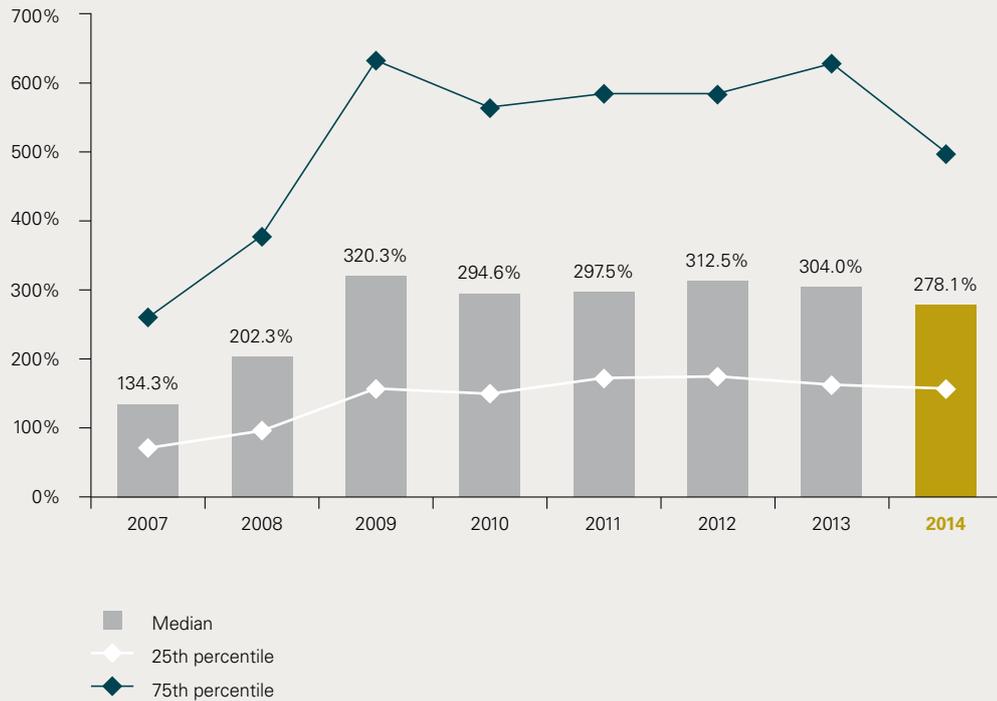
Different trajectories: Total capital ratios of small versus large banks

Small banks strengthened their total capital ratios (Eligible equity/Risk weighted assets) from 27.8% in 2012 to 30.5% by the end of 2014, while large banks show the opposite with slightly declining total capital ratios from a peak of 28.1% in 2012 to 25.0% in 2014.

Banks in Turnaround Completed reported consistently high total capital ratios (32.3% in 2014) in recent years. This might indicate that these banks have reorganized their balance sheet structures and have as a consequence been able to strengthen their capital bases.

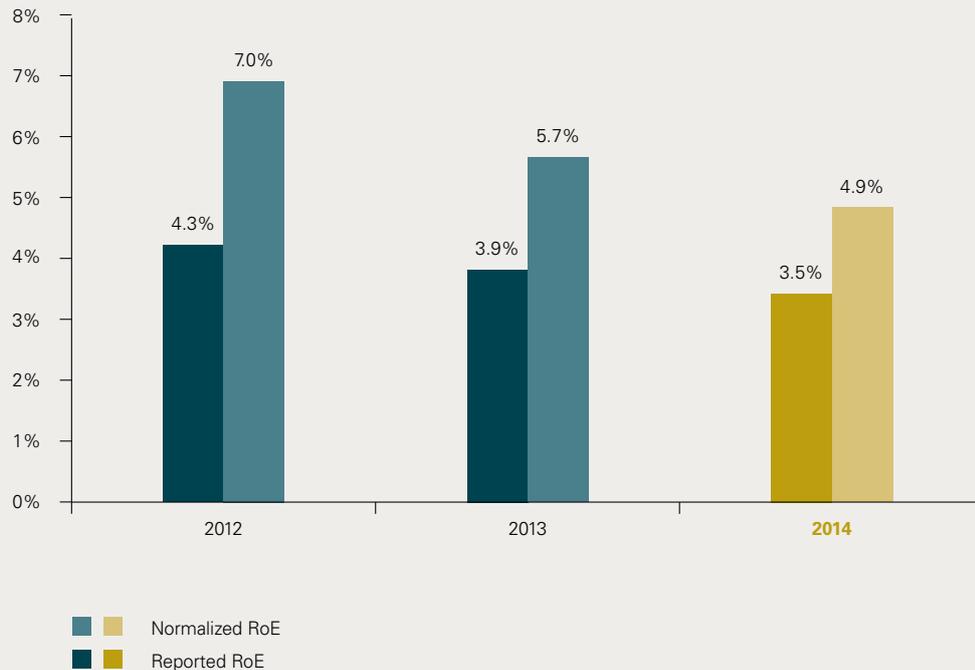
The differences in total capital ratios between the clusters do not significantly distort the reported RoE trends across the clusters.

Customer deposits as a % of customer loans 2007 to 2014



Strong upward trend in Lombard loans and mortgage volumes

Lombard loans and mortgages rose significantly from CHF105.3 billion in 2013 to CHF122.2 billion in 2014 (+16%) following a flat 2012 to 2013. This strong increase resulted in the deposits to loan coverage rate falling from 304.0% in 2013 to 278.1% in 2014, the lowest level since 2008. Although the overall level of cash in clients’ portfolios remained high, this increase is likely due to clients being willing to increase leverage in their portfolios with Lombard loans.

Normalized RoE at a capital ratio of 15% 2012 to 2014

Note: includes 71% (65 out of 91) of the sample banks that published regulatory capital data

RoE declines over three years but improves when adjusted for regulatory excess capital

To quantify the impact of excess capital on RoE, a normalized RoE was calculated for the 65 banks in our sample for which regulatory capital information was available. A target capital ratio of 15% was applied across all banks, taking also into account a minimum capital requirement of CHF20 million.

The median normalized RoE shows a downward development over the past three years, from 7.0% in 2012 to 4.9% in 2014, moving closer to reported RoE. In 2014, 33 banks showed a normalized RoE of less than 5%, 10 banks a normalized RoE of between 5% and 10% and 22 banks of higher than 10%.

One third of banks paid dividends in 2013 and 2014. Payout ratio is extremely high

The median dividend payout ratio as a percentage of the previous year's net profit stood at 84.9% in 2013, declining in 2014 to 73.4% (mainly driven by banks in Continuing Decline). Dividend distribution seems to have recovered significantly in 2015 with a payout ratio of 93.6% based on proposed dividends on 2014's achieved financial results.

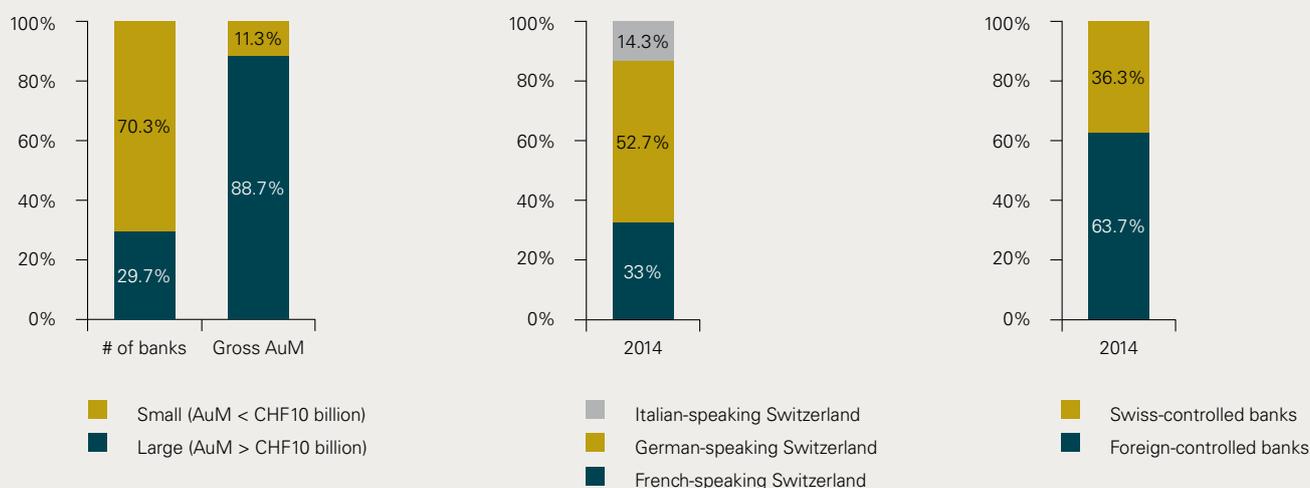
Methodology and basis

The study assessed the annual reports of 91 private banks based in Switzerland (2013: 97), representing AuM of CHF1,508.7 billion and 25,987 FTEs.

Excluded from the dataset were:

- Credit Suisse Group (AuM of CHF874.5 billion) and UBS (AuM of CHF987.0 billion)¹.
- Branch offices of foreign banks.
- “Banquiers privés”, also those having changed their legal form during 2014 as no comparative figures were available to calculate trends.
- Private banking units of cantonal banks and regional banks (separate private banking subsidiaries of cantonal banks were included in the sample).

The dataset Sample composition



In this fragmented market, 70% of the 91 banks managed less than CHF10 billion in AuM in 2014. Conversely, a mere 30% of banks managed 89% of AuM. This distribution gap would be even wider if Credit Suisse Group and UBS were included.

The methodology was further refined this year, which led to some amendments in the analysis and sample. This included a change in the sample, in cluster allocations and the generalized use of medians instead of averages. Some figures presented in this study could therefore differ from last year’s report.

¹ Figures used for Credit Suisse Group pertain specifically to its Wealth Management clients; UBS figures relate to its Wealth Management clients (excluding Wealth Management Americas)

**Example:
percentile chart**

In 2014, one-quarter of banks have a value of more than 16%.

In 2014, one-half of banks have a value of more than 10%, with the other half being below 10%.

In 2014, three-quarters of banks have a value of more than 5%.



In 2014, the total of income amounted to 120% of that of 2007.

Methodology used

The study mainly uses two types of chart:

Median charts: show the median value for the entire sample. In addition, they note the value for each of the 25th and 75th percentiles.

Standardized charts: are based on a constant sample, whereby a base year is selected that represents 100%. Further years in the chart are shown as proportionately greater or lower than the base year.

Due to the differentiated consideration of size, percentile and standardized development, charts could provide contrary statements.

GLOSSARY

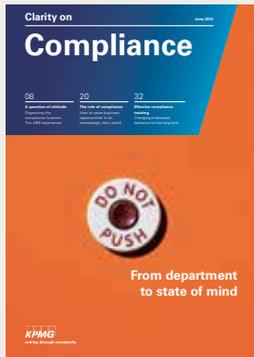
AEol	Automatic Exchange of Information	FX	Foreign exchange
AuM	Assets under Management	M&A	Mergers & Acquisitions
bn	Billion	NNM	Net New Money (excluding M&A-related inflows and outflows)
bps	Basis points	RoE	Return on Equity
CEO	Chief executive officer	SNB	Swiss National Bank
CHF	Swiss francs	USD	US dollars
CRM	Client relationship manager	vs	Versus
EUR	Euros	YTD	Year To Date
FTE	Full Time Equivalents		

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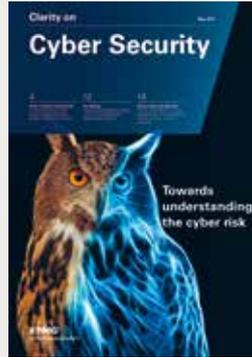
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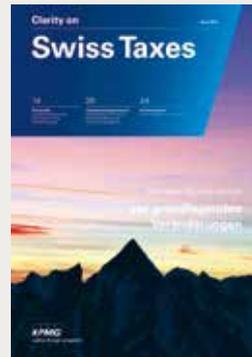
Clarity on **Compliance**



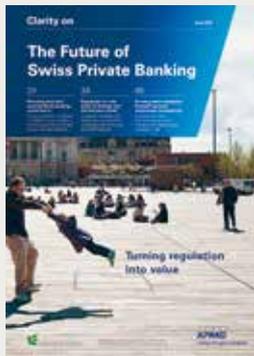
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