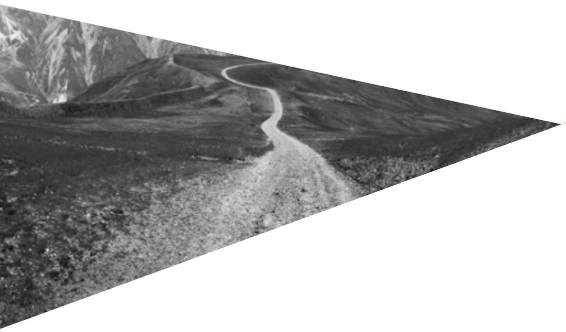
European Banking Barometer – 1H14

Confidence masks challenges



Building a better
working world

Contents

Introduction

We have developed the European Banking Barometer to provide our clients with a benchmark and overview of the macro-economic outlook and its impact on the European banking industry, as well as the priorities banks will focus on over the next six months.

Now in its fifth edition, the latest biannual study consists of 294 interviews with senior bankers across 11 markets: Austria, Belgium, France, Germany, Italy, the Netherlands, the Nordics, Poland, Spain, Switzerland and the UK.

The fieldwork was conducted via an online questionnaire and telephone interviews between March and April 2014. We interviewed respondents from a range of financial institutions covering at least 50%* of banking assets in each market.

A range of bank types were interviewed in each market to help ensure the study was a fair reflection of each country's banking industry. Interviews were not conducted with subsidiaries of member/group banks.

The results in this report are presented in an aggregate market format and shown in percentages. Aggregated European-wide results have been weighted in proportion to countries' banking assets. All country-level data is unweighted.

Please note, some charts may not add up to 100%, and net increase totals may differ slightly from the numbers shown in the charts, as percentages have been rounded to the nearest whole number. Where possible, we have compared and contrasted the data against our *European Banking Barometer – 2H13*.

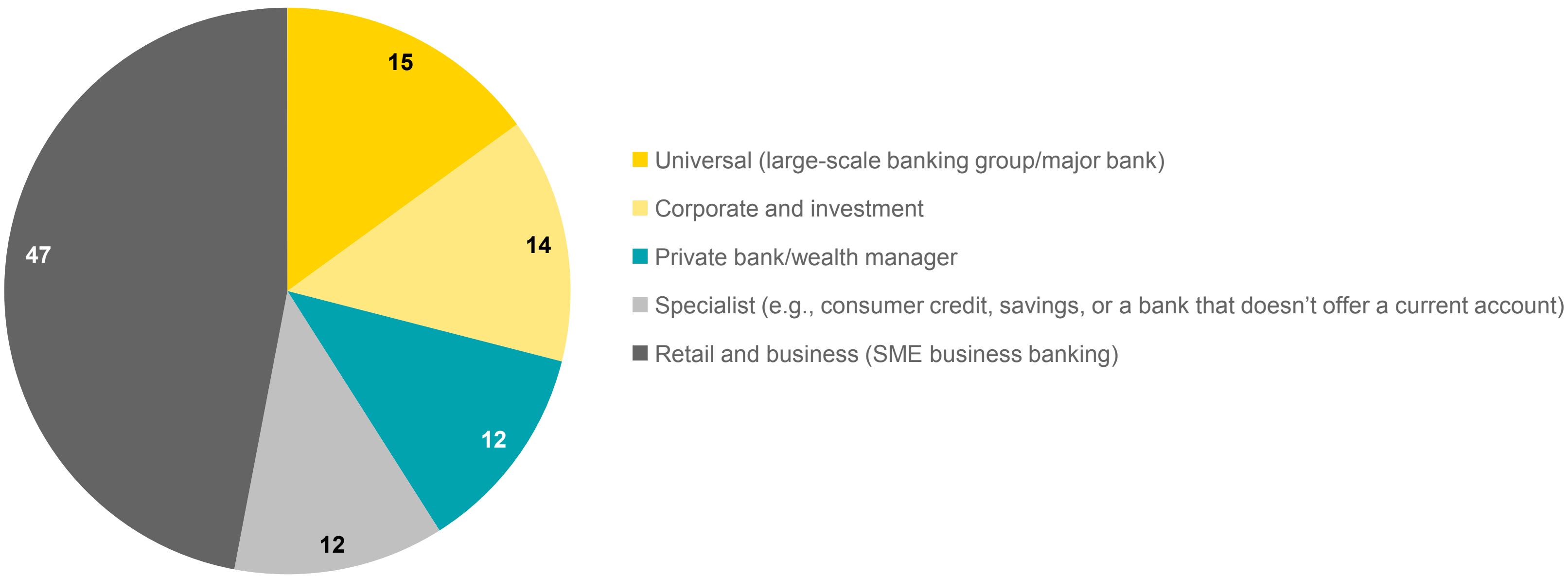
We would like to thank all the research participants for their contributions to the study.

If you would like to take part in our next European Banking Barometer study, please speak to your usual EY contact or refer to your local country contact on page 55.

* Except in Austria, where they represent 45% of banking assets, Italy 39% and the Nordics 42%.

Composition of the survey sample by bank type

Bank type*



* Numbers in the pie chart reflect the percentage of respondents who answered. Percentages were calculated using unweighted data.
Please note that given the structure of the German and Swiss banking markets, respondents in these two countries were provided with country-specific bank types that have been reallocated to our five European bank types as follows:
For Germany, big banks and regional banks were reallocated to universal banks; foreign banks (not headquartered in Germany) were reallocated to corporate and investment banks; private bankers were reallocated to private banks/wealth management; savings banks and cooperative banks were reallocated to retail and business banks; and central building societies, building loan associations and mortgage banks were reallocated to specialist banks.
For Switzerland, major banks were reallocated to universal banks; investment banks were reallocated to corporate and investment banks; private bankers (general or limited partnership) and banks under foreign control were reallocated to private banks/wealth management; cantonal banks, and regional and savings banks were reallocated to retail and business banks; and securities traders were reallocated to specialist banks.

Composition of the survey sample by bank type

Type of bank*

Market	Total	Universal	Corporate and investment	Private bank/ wealth management	Specialist	Retail and business (cooperative)	Retail and business (state owned)	Retail and business (privately owned)
Austria	13	7	2	0	2	2	0	0
Belgium	17	2	3	2	1	3	1	5
France	30	6	5	5	2	3	2	7
Germany	103	6	7	6	7	28	44	5
Italy	20	3	4	2	3	6	0	2
Netherlands	7	3	0	0	2	1	0	1
Nordics	20	4	2	3	8	1	0	2
Poland	12	7	1	0	2	0	2	0
Spain	20	2	1	6	3	0	2	6
Switzerland	17	2	0	5	1	1	3	5
UK	35	3	16	6	4	0	0	6
Europe**	**294**	**45**	**41**	**35**	**35**	**45**	**54**	**39**

* Given the structure of the German and Swiss banking markets, respondents in these two countries were provided with country-specific bank types that have been reallocated to our five European bank types as follows:
For Germany, big banks and regional banks were reallocated to universal banks; foreign banks (not headquartered in Germany) were reallocated to corporate and investment banks; private bankers were reallocated to private banks/wealth management; savings banks and cooperative banks were reallocated to retail and business banks; and central building societies, building loan associations and mortgage banks were reallocated to specialist banks.
For Switzerland, major banks were reallocated to universal banks; investment banks were reallocated to corporate and investment banks; private bankers (general or limited partnership) and banks under foreign control were reallocated to private banks/wealth management; cantonal banks, and regional and savings banks were reallocated to retail and business banks; and securities traders were reallocated to specialist banks.

** European totals in the table reflect the unweighted number of respondents who answered. All European aggregated percentages in the report are weighted in proportion to markets' banking assets, as reported by The Banker database, June 2013. All market level figures in this report reflect unweighted data.

European overview

The gradual recovery of European banks is expected to continue. Most bankers remain positive about the economy and their bank's performance, but the sector isn't out of the woods yet. After a significant swing towards optimism in our previous edition, our latest survey reveals that a few more bankers expect the economy to improve but most only anticipate slight improvement.

Most respondents also expect improved financial performance from their banks but, again, this will only be slight. Investors might hope that a sector with stronger balance sheets, and an increased focus on growth initiatives, would hasten a return to greater profitability. However, with bankers expecting only an average 1.6% increase in return on equity (ROE), and remaining preoccupied by risk and regulatory issues, there is little evidence that this will happen anytime soon.

The recovering economy has yet to translate into a meaningful improvement in bank profitability.

- Economic optimism is now more pronounced, with 64% of respondents expecting their market's economic outlook to improve, compared with 54% in 2H13. Concerns about the exposure of banks to sovereign debt have also stabilized.
- As a result, 60% of respondents expect their bank's financial performance to improve over the next six months. Bankers are positive about the outlook for most business lines, particularly private banking and wealth management where 59% believe the outlook is good – reflecting its capital-light model and the growing wealth of high net worth individuals since the global financial crisis.
- However, with bankers anticipating an average revenue increase of just 2.4%, and cost reduction of a mere 0.5%, any improved financial performance will be modest. EY's analysis suggests that, without more meaningful restructuring, bankers will struggle to achieve even the 1.6% uplift in ROE they are hoping for. Furthermore, we estimate that banks would need to simultaneously reduce costs by about 12% and increase revenues by about 15% just to exceed their cost of equity.

Balance sheets continue to strengthen and more banks are beginning to focus on growth.

- Although most banks will continue to shrink their balance sheets, only 8% anticipate raising additional capital following the Asset Quality Review (AQR) and stress tests. Furthermore, due to the improving economic climate, 23% of banks expect to be able to release reserves, compared with just 14% in our previous survey.

European overview

- Stronger balance sheets will allow banks to focus more on growth. Fifty-seven percent of respondents now expect their banks to launch initiatives to promote growth, compared with 49% in our previous survey. Furthermore, 51% now expect to increase lending to customers, compared with 44% in 2H13.
- Corporate lending policies will continue to loosen for many sectors – with small and medium-sized enterprises (SMEs) expected to benefit most. Forty-five percent of bankers expect lending policies to the SME sector will become less restrictive in the next six months.

Industry restructuring is slowing.

- Compared with the last edition slightly fewer respondents expect to buy or sell assets in the next year. Nevertheless, 65% of banks still expect to see significant consolidation in the industry within the next three years.
- Following significant restructuring across the industry, fewer banks now expect to see further headcount reductions with just 38% of respondents forecasting additional cuts, compared to 42% six months ago. In some markets, such as the UK and the Nordics, banks expect to recruit staff into growth businesses. But in retail banking and back office functions most are expecting more cuts.

But banks are still grappling with the impact of new regulation.

- The top three priorities for banks relate to risk and regulation. Compliance is one of the few business areas where headcount is expected to grow – suggesting that banks continue to struggle with the regulatory burden.
- With regulators increasingly concerned by conduct and consumer protection issues, reputational risk and cybersecurity have emerged as key priorities for banks, especially in Belgium, France, the Netherlands and Switzerland.

They may also struggle to justify expected pay rises.

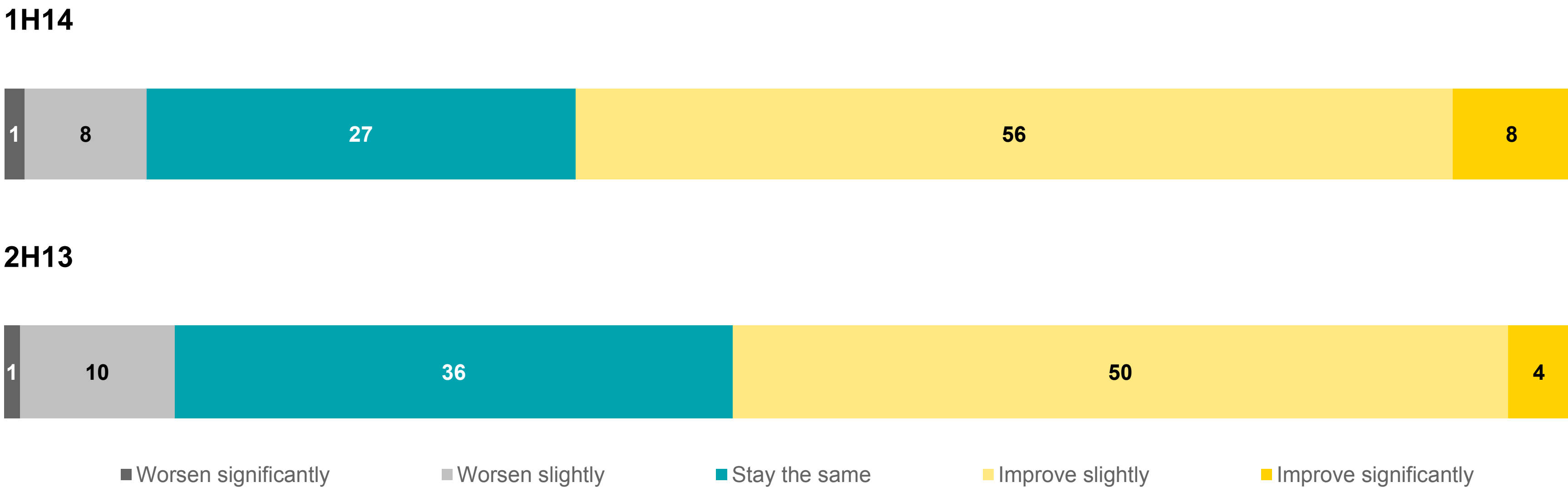
- Twenty-seven percent of respondents expect pay to rise in the coming year. The small minority of respondents anticipating double-digit pay hikes at their banks will need to deliver returns well above the industry average, or risk angering investors.

Section 1

Economic environment

Across Europe, more bankers are becoming optimistic about their market's economic recovery …

How do you expect the general economic outlook in your market to change over the next six months?*

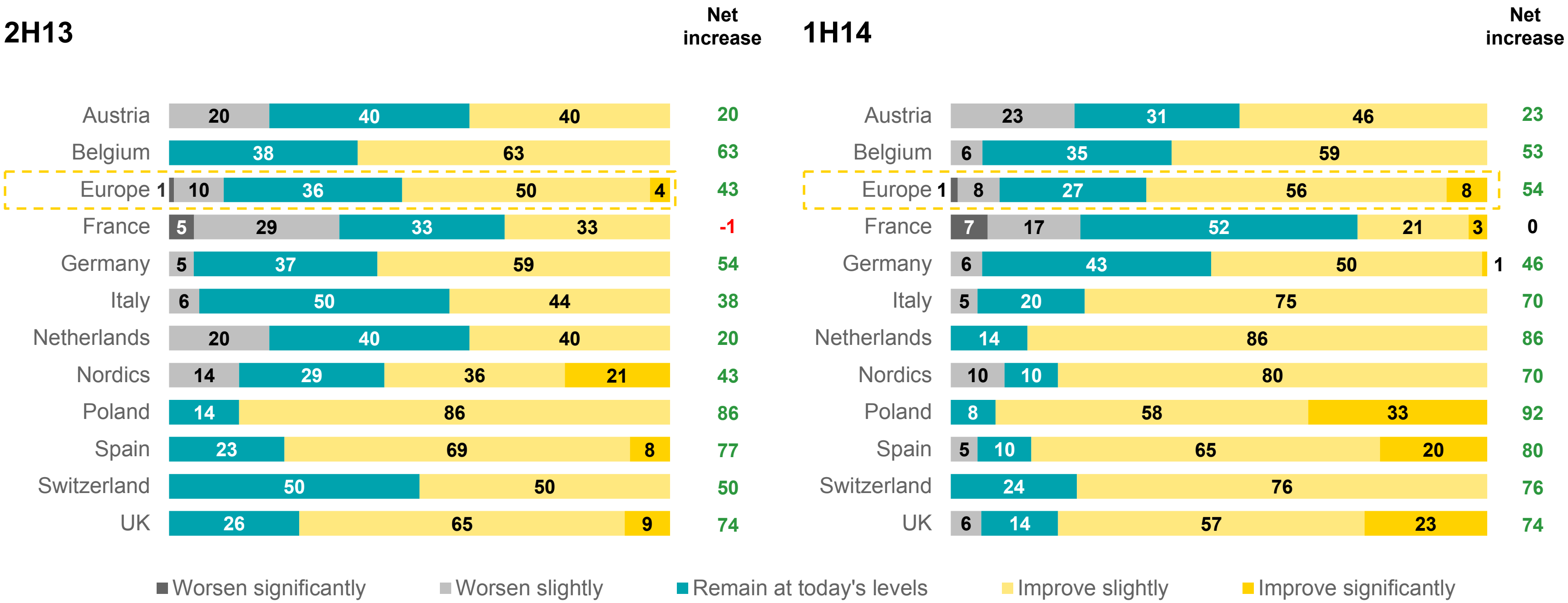


Comments: The economic optimism of European bankers is now even more pronounced than in our *European Banking Barometer – 2H13*. Our previous survey was the first in which a majority (54%) of respondents expected the economic outlook for their country to improve. Even more banks (64%) now anticipate economic recovery. This positivity reflects broader macro-economic improvements; the IMF has recently revised its Eurozone GDP forecast upwards, and the region is expected to see increased demand driven by higher consumption and a revival of investment. Only French bankers remain uncertain about the outlook. The greatest improvement is expected in Italy and the Netherlands – but with both economies contracting in the first quarter, this optimism may be short-lived.

* Numbers reflect the percentage of respondents who answered. Base excludes respondents who answered "Don't know."

… except in France, which is struggling to regain competitiveness and boost exports

How do you expect the general economic outlook in your market to change over the next six months?*



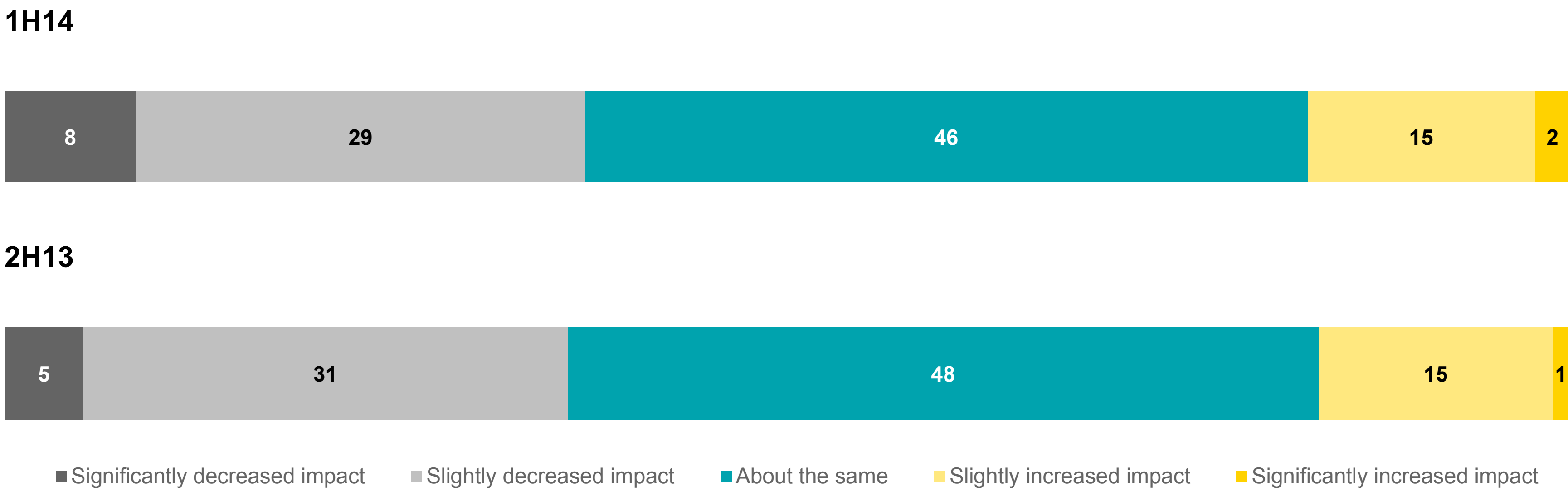
* Numbers reflect the percentage of respondents who answered. Base excludes respondents who answered "Don't know."

Section 2

European sovereign debt crisis

Despite a stronger economic outlook, concerns about the sovereign debt crisis refuse to diminish completely ...

What level of impact do you think the Eurozone sovereign debt crisis will have on the banking sector in your market over the next six months compared with the previous six months?*

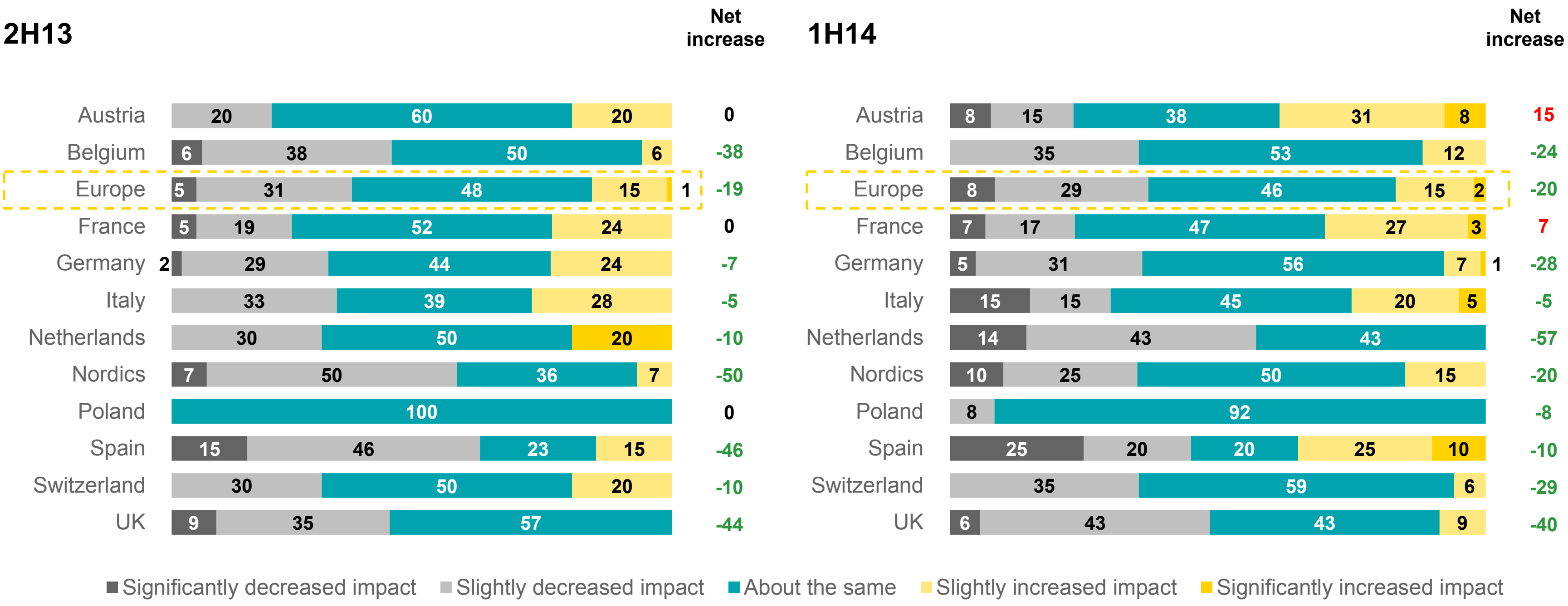


Comments: Concerns about the exposure of the European banking sector to sovereign debt have stabilized. Our *European Banking Barometer – 2H13* showed a remarkable change in the views of respondents on the impact of the sovereign debt crisis as growth returned to the Eurozone. In 1H13, over one-third of respondents expected the impact of the sovereign debt crisis would increase, but that has fallen to one-sixth in our most recent survey, while over one-third now expect its impact to diminish. However, a small group of bankers are likely to remain concerned about sovereign debt until economic growth becomes truly embedded across the Eurozone, or full banking union breaks the link between banks and sovereigns.

* Numbers reflect the percentage of respondents who answered.

… particularly in Austria and France, where more banks expect sovereign debt problems to increase rather than decrease

What level of impact do you think the Eurozone sovereign debt crisis will have on the banking sector in your market over the next six months compared with the previous six months?*



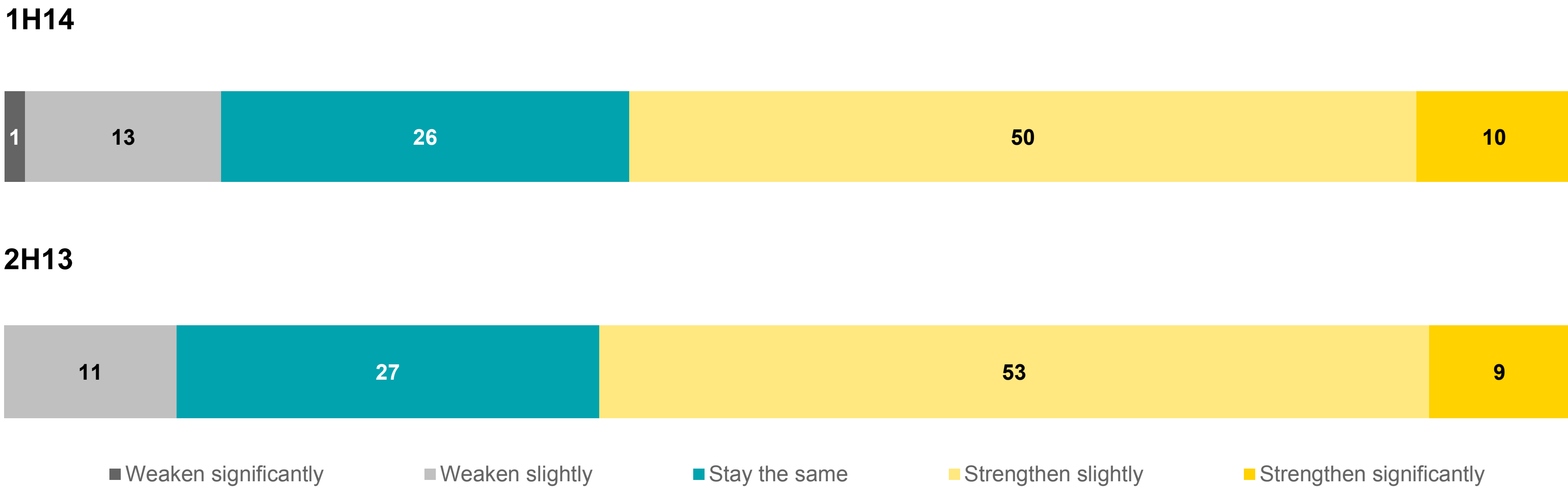
* Numbers reflect the percentage of respondents who answered.

Section 3

Business outlook and focus areas

Most bankers still expect their institution's financial performance to improve …

How do you expect your bank's overall performance to change over the next six months?*

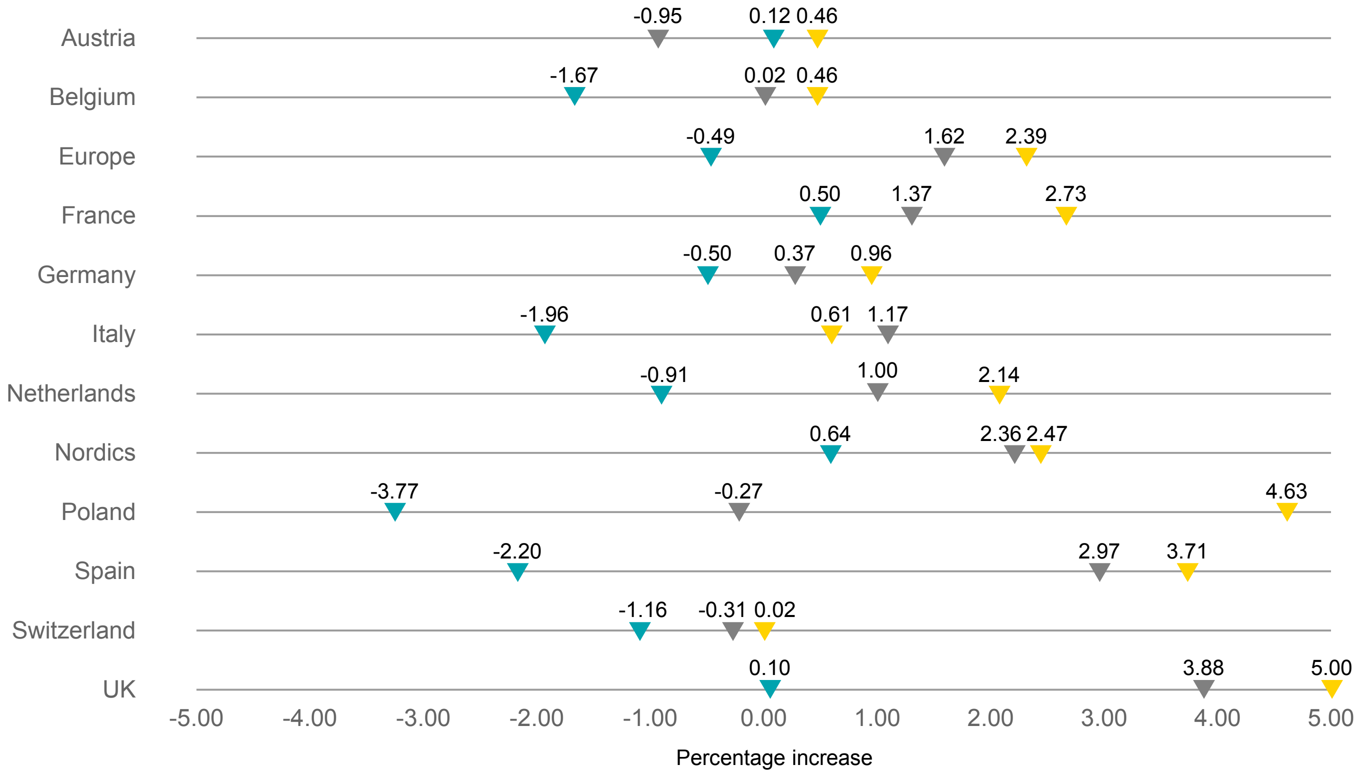


Comments: Sixty percent of banks expect their financial performance to improve over the next six months. With the leading European banks reporting average full year returns on equity of 3.8%, substantial improvements in financial performance will be required for them to achieve returns that exceed their cost of equity. Sluggish economic growth, persistent ultra-low interest rates, and the potential that the European Central Bank (ECB) will launch its own quantitative easing program mean that if banks want to improve their financial performance they will need to grow revenues through non-interest income and continue to reduce costs aggressively. However, with banks expecting to reduce costs by an average of only 0.5% and grow their revenues by an average of just 2.4% they will struggle to achieve even the 1.6% ROE uplift they are anticipating. EY's analysis suggests banks would only achieve an uplift in ROE of 0.6% with their revenue growth and cost reduction expectations. Moreover, European banks would need to reduce costs by about 12% and simultaneously increase revenues by about 15% just to exceed their average FY13 cost of equity (9.7%).

* Numbers reflect the percentage of respondents who answered. Base excludes respondents who answered "Don't know."

… but an inability to increase revenues and cut costs means they will struggle to deliver meaningful ROE growth

How do you expect your bank's performance measures to change over the next six months?*



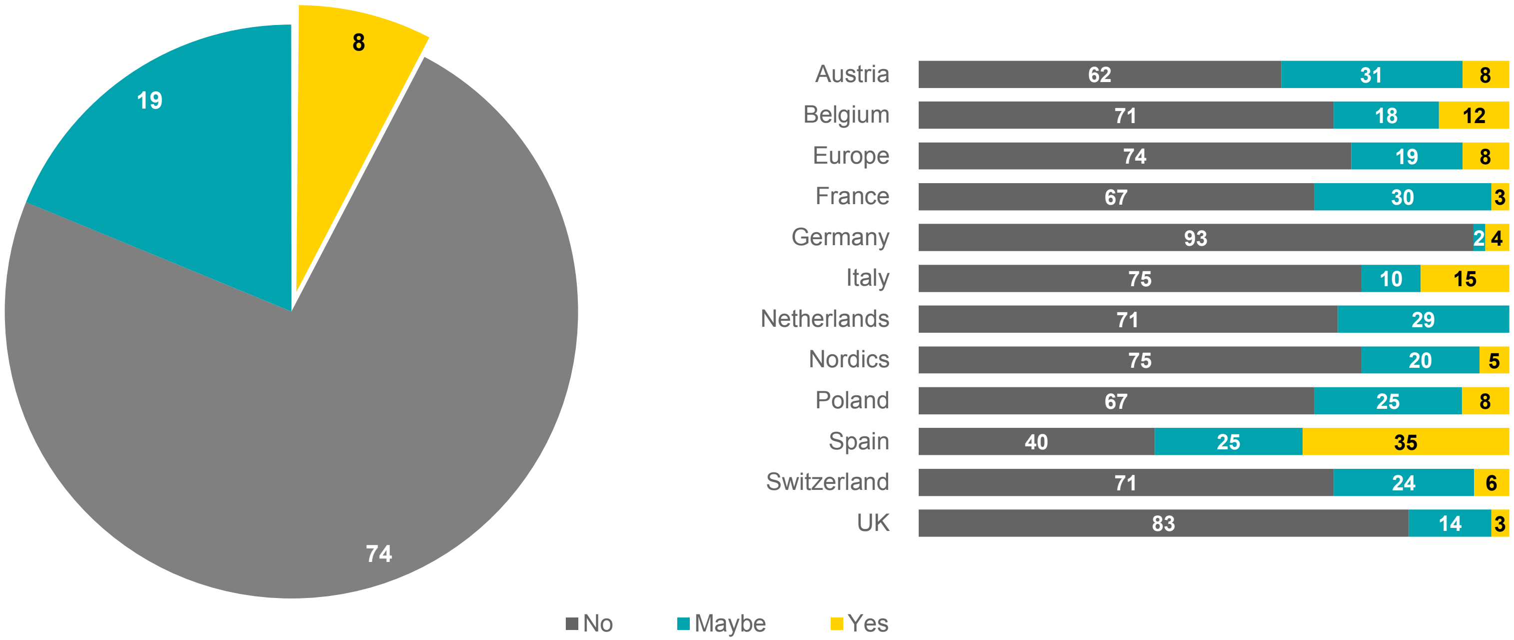
Average percentage change

	Revenue	Cost base	ROE
Austria	**0.46**	**0.12**	**-0.95**
Belgium	**0.46**	**-1.67**	**0.02**
Europe	**2.39**	**-0.49**	**1.62**
France	**2.73**	**0.50**	**1.37**
Germany	**0.96**	**-0.50**	**0.37**
Italy	**0.61**	**-1.96**	**1.17**
Netherlands	**2.14**	**-0.91**	**1.00**
Nordics	**2.47**	**0.64**	**2.36**
Poland	**4.63**	**-3.77**	**-0.27**
Spain	**3.71**	**-2.20**	**2.97**
Switzerland	**0.02**	**-1.16**	**-0.31**
UK	**5.00**	**0.10**	**3.88**

* Numbers reflect the mean percentage change expected. Base excludes respondents who answered "Don't know."

Most banks believe they have already raised sufficient capital to weather the ECB's AQR and stress test

Does your bank plan to raise capital following the ECB's AQR and stress test?*

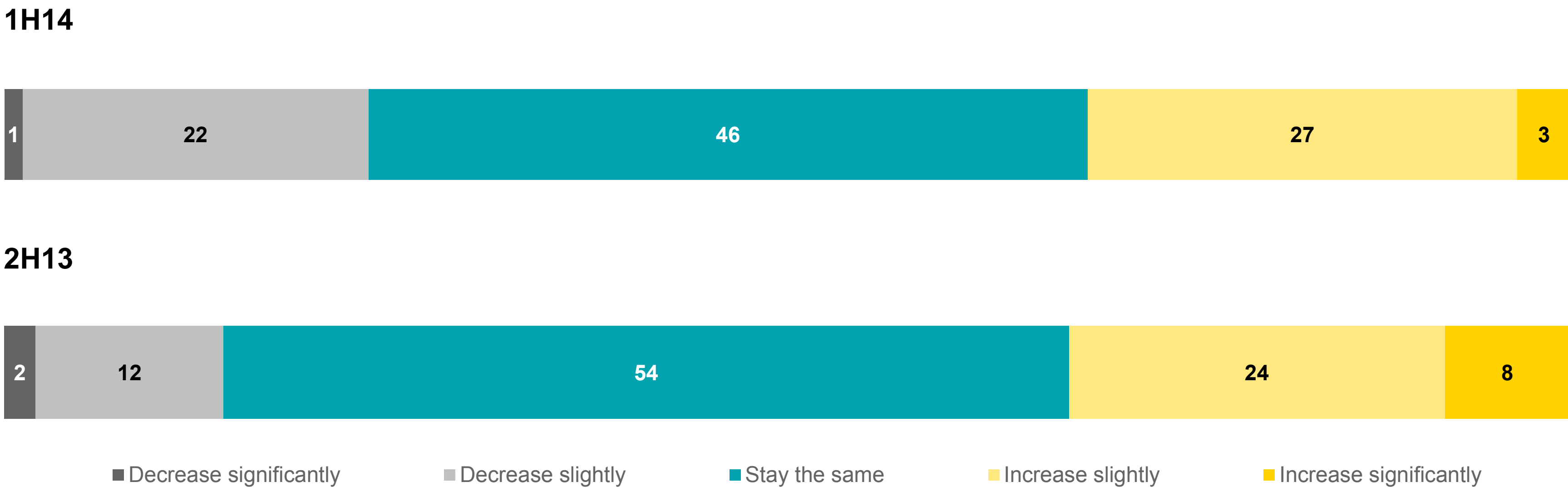


Comments: Just 8% of respondents anticipate raising additional capital following the AQR and stress test. However, the fact that a further 19% think they might have to raise additional capital illustrates a degree of uncertainty and apprehension across the industry about what the AQR will reveal. Several banks have already raised capital levels ahead of the AQR and stress tests. According to Thomson ONE, by the time we completed fieldwork for this survey, Eurozone banks had already raised over US $11 billion of equity this year, compared with just over US $2 billion in the same period in 2013. Since we completed the fieldwork, banks have raised an additional US $24 billion, bringing the total equity raised this year to over US $35 billion.

* Numbers reflect the percentage of respondents who answered. Base excludes respondents who answered "Don't know."

Nevertheless, almost one-third of bankers still expect a further increase in loan loss provisions …

Over the next six months, what do you expect your bank's total provisions against loan losses to do?*

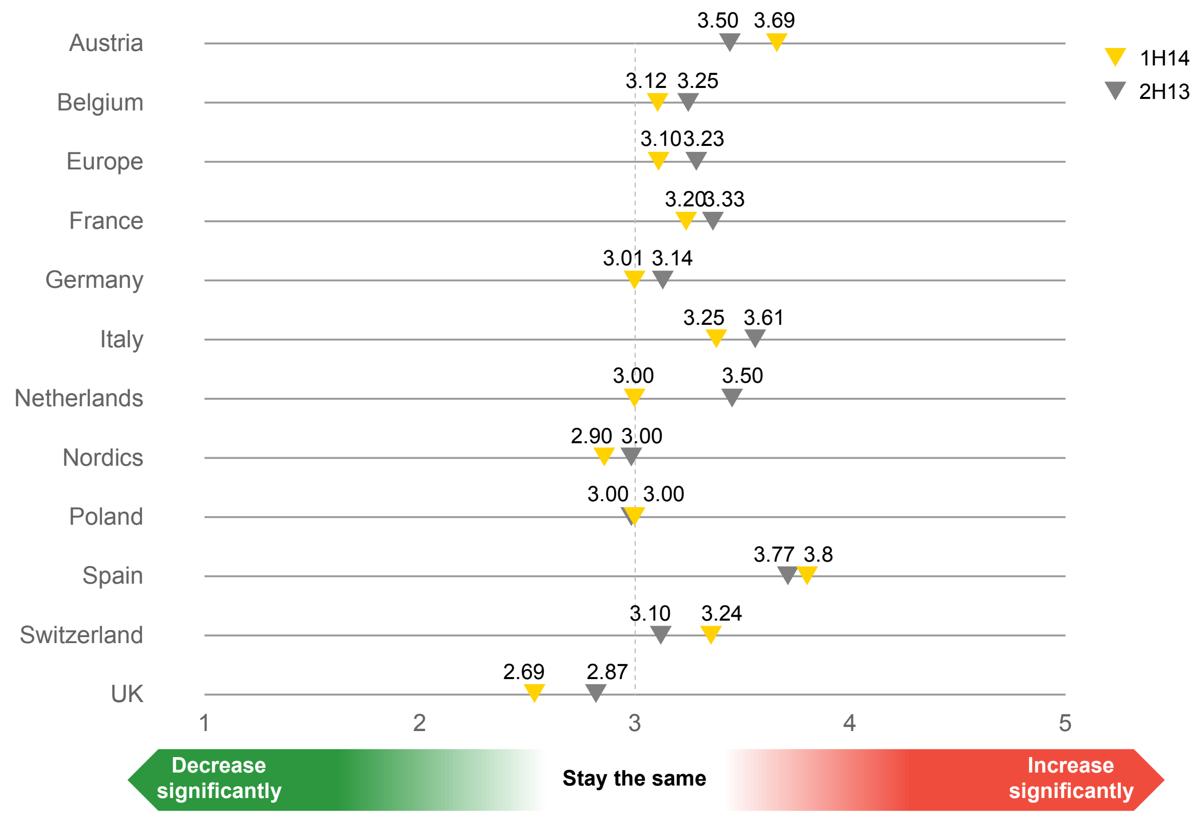


Comments: Slightly fewer banks now expect to raise loan loss provisions (LLPs) than in our last survey. However, despite improving economic indicators, almost a third still expect to raise LLPs in anticipation of the AQR. This is particularly true in Spain, where banks have been required to revalue their real estate portfolios, and in Austria where banks have significant exposure to Eastern Europe. Nevertheless, the improving economic climate across Europe means 23% of banks now expect to be able to release provisions to boost their financial performance, compared with just 14% in our previous survey.

* Numbers reflect the percentage of respondents who answered. Base excludes respondents who answered "Don't know."

… although in the UK strong economic growth means bankers expect to be able to release provisions

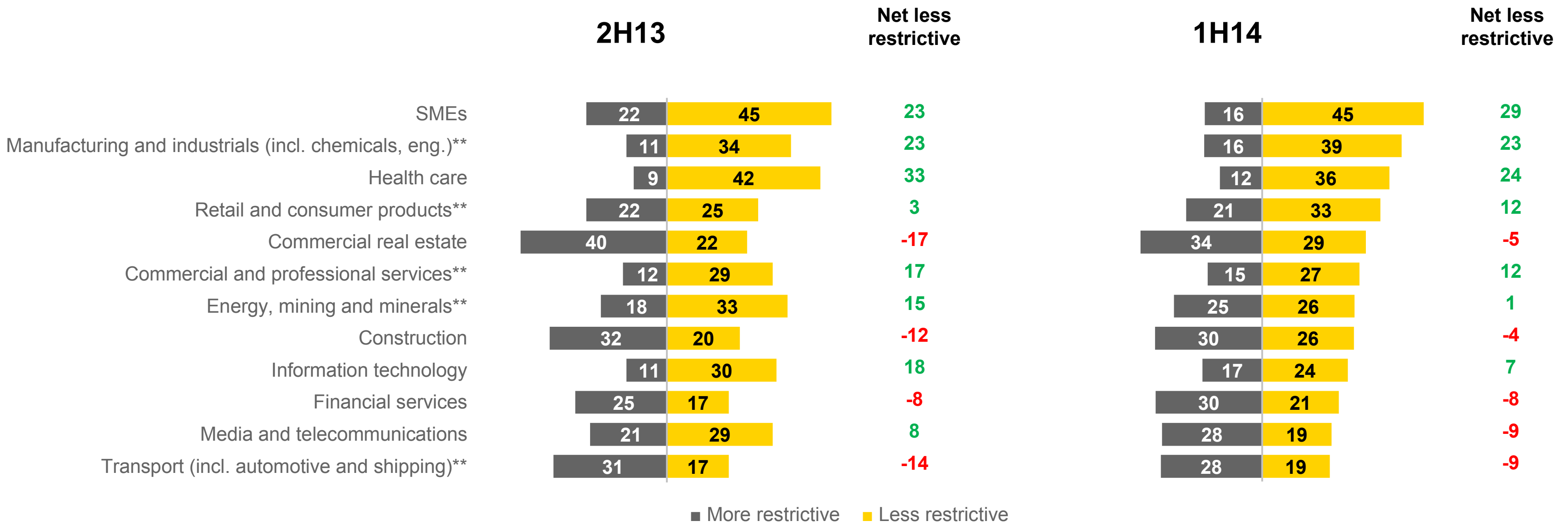
Over the next six months, what do you expect your bank's total provisions against loan losses to do?*



* Numbers reflect the mean scores of respondents who answered on a scale of 1 to 5 where 1 denotes "Decrease significantly" and 5 denotes "Increase significantly." Base excludes respondents who answered "Don't know."

Further easing of corporate lending policies is anticipated for many sectors, reflecting the improved economic outlook

How do you expect the corporate lending policies of banks in your market to change in each of the following sectors over the next six months?*

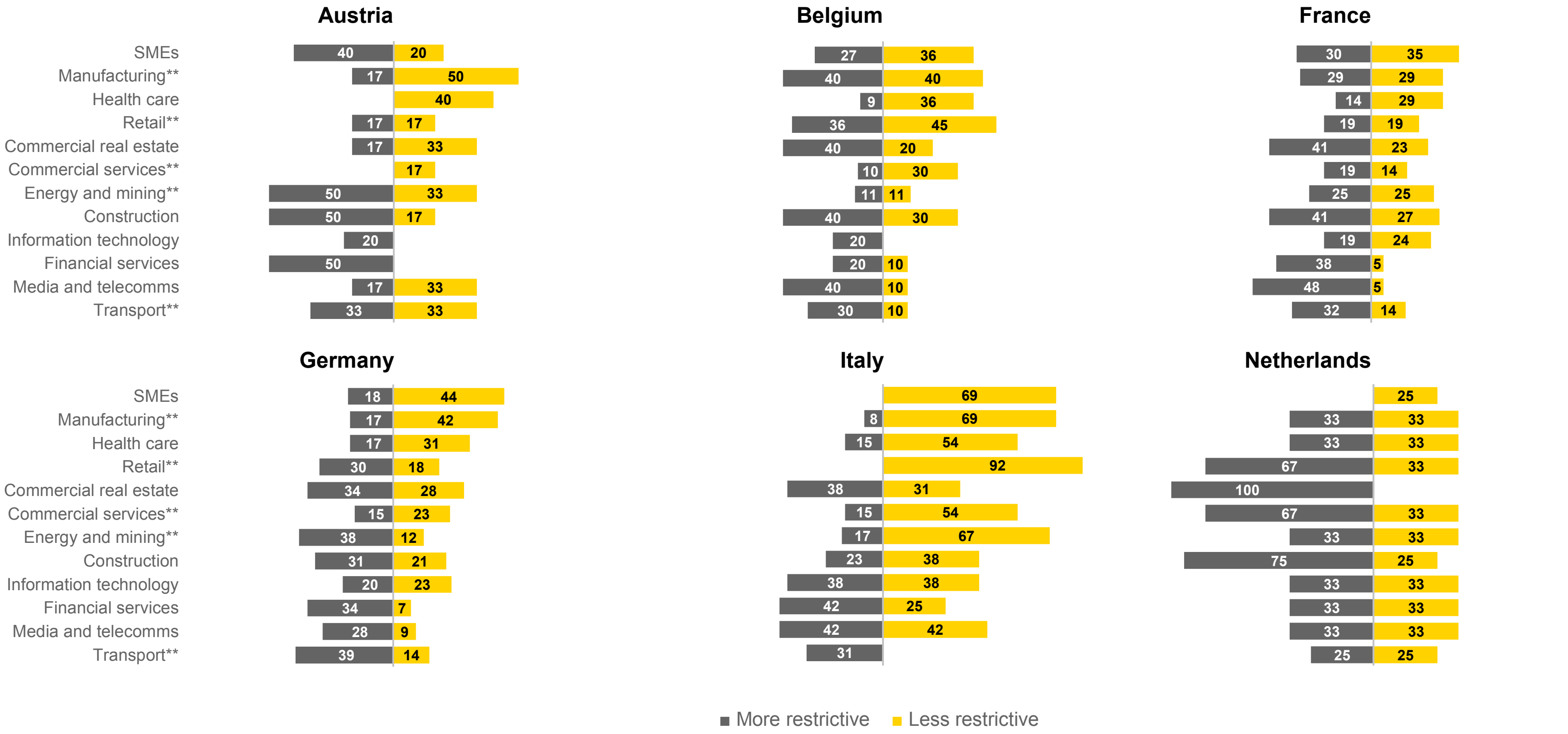


Comments: The prospects for corporate lending continue to improve for most sectors. The outlook is most positive for the SMEs, where 45% of respondents expect lending to be less restrictive. Notably, even the tightening of lending policies to the construction and commercial real estate sectors has slowed dramatically from our previous surveys. Nevertheless, despite banks being more willing to lend, overall access to bank credit remains limited and a further loosening of lending policies will be required for Europe to see a return to loan growth.

* Numbers reflect the percentage of respondents who answered. Respondents answering “Remain unchanged” are not displayed. Base excludes respondents who answered “Don’t know.”
** Energy and mining includes minerals; manufacturing includes industries, chemicals and engineering; commercial services includes professional services; retail includes consumer products and; transport includes automotive and shipping.

Lending to SMEs is expected to be less restrictive in all countries except Austria …

How do you expect the corporate lending policies of banks in your market to change in each of the following sectors over the next six months?*



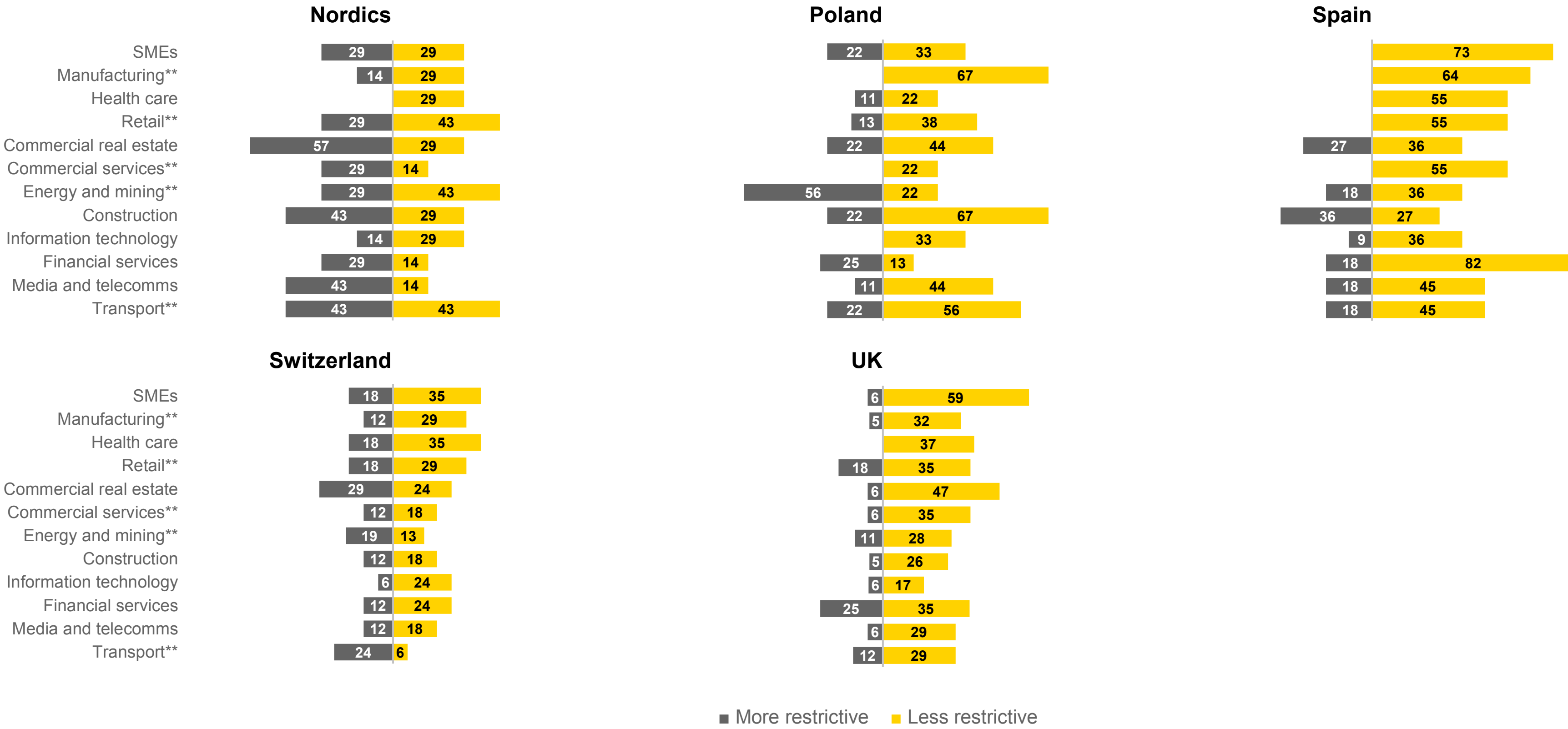
Sector	Austria More	Austria Less	Belgium More	Belgium Less	France More	France Less
SMEs	40	20	27	36	30	35
Manufacturing**	17	50	40	40	29	29
Health care		40	9	36	14	29
Retail**	17	17	36	45	19	19
Commercial real estate	17	33	40	20	41	23
Commercial services**		17	10	30	19	14
Energy and mining**	50	33	11	11	25	25
Construction	50	17	40	30	41	27
Information technology	20		20		19	24
Financial services	50		20	10	38	5
Media and telecomms	17	33	40	10	48	5
Transport**	33	33	30	10	32	14

Sector	Germany More	Germany Less	Italy More	Italy Less	Netherlands More	Netherlands Less
SMEs	18	44		69		25
Manufacturing**	17	42	8	69	33	33
Health care	17	31	15	54	33	33
Retail**	30	18		92	67	33
Commercial real estate	34	28	38	31	100	
Commercial services**	15	23	15	54	67	33
Energy and mining**	38	12	17	67	33	33
Construction	31	21	23	38	75	25
Information technology	20	23	38	38	33	33
Financial services	34	7	42	25	33	33
Media and telecomms	28	9	42	42	33	33
Transport**	39	14	31		25	25

* Numbers reflect the percentage of respondents who answered. Respondents answering "Stay the same" are not displayed. Base excludes respondents who answered "Don't know."
** Energy and mining includes minerals; manufacturing includes industries, chemicals and engineering; commercial services includes professional services; retail includes consumer products and; transport includes automotive and shipping.

… and the Netherlands

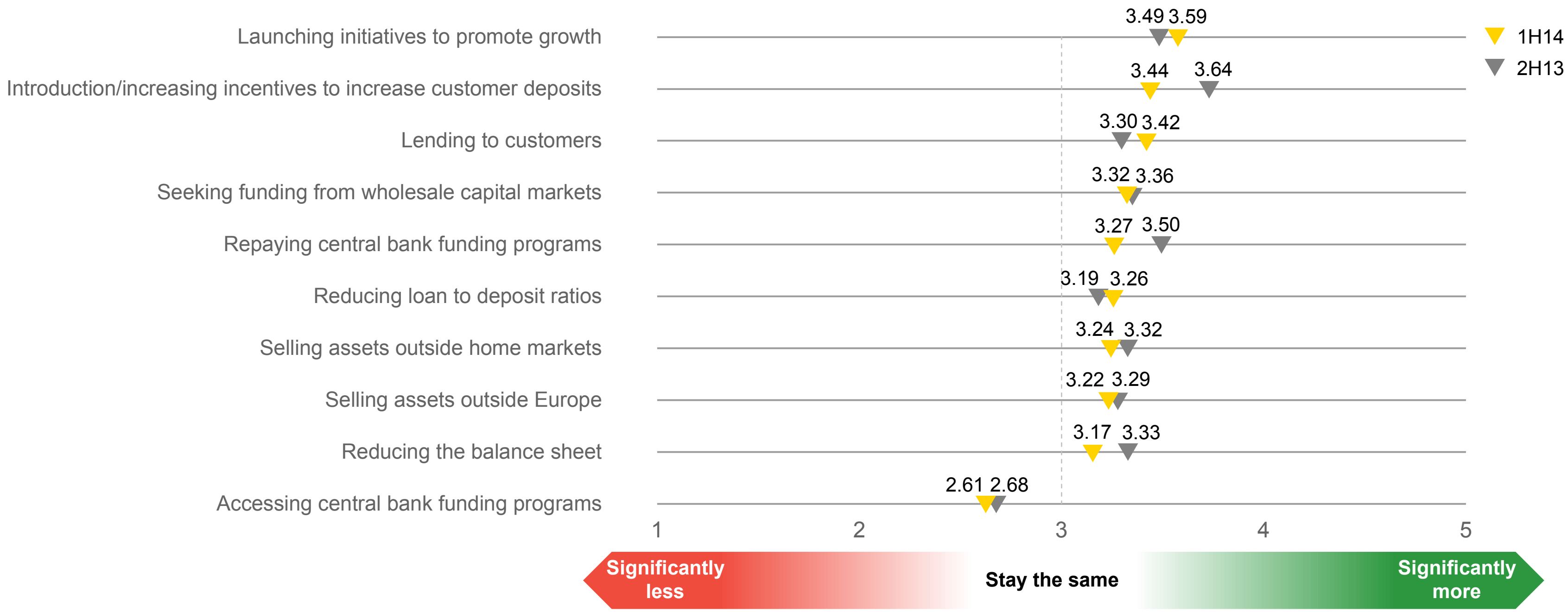
How do you expect the corporate lending policies of banks in your market to change in each of the following sectors over the next six months?*



* Numbers reflect the percentage of respondents who answered. Respondents answering “Stay the same” are not displayed. Base excludes respondents who answered “Don’t know.”
** Energy and mining includes minerals; manufacturing includes industries, chemicals and engineering; commercial services includes professional services; retail includes consumer products and; transport includes automotive and shipping.

An increasingly favorable operating environment means that more bankers are beginning to prioritize growth initiatives

How likely are the banks in your market to be engaged in the following activities over the next six months?*

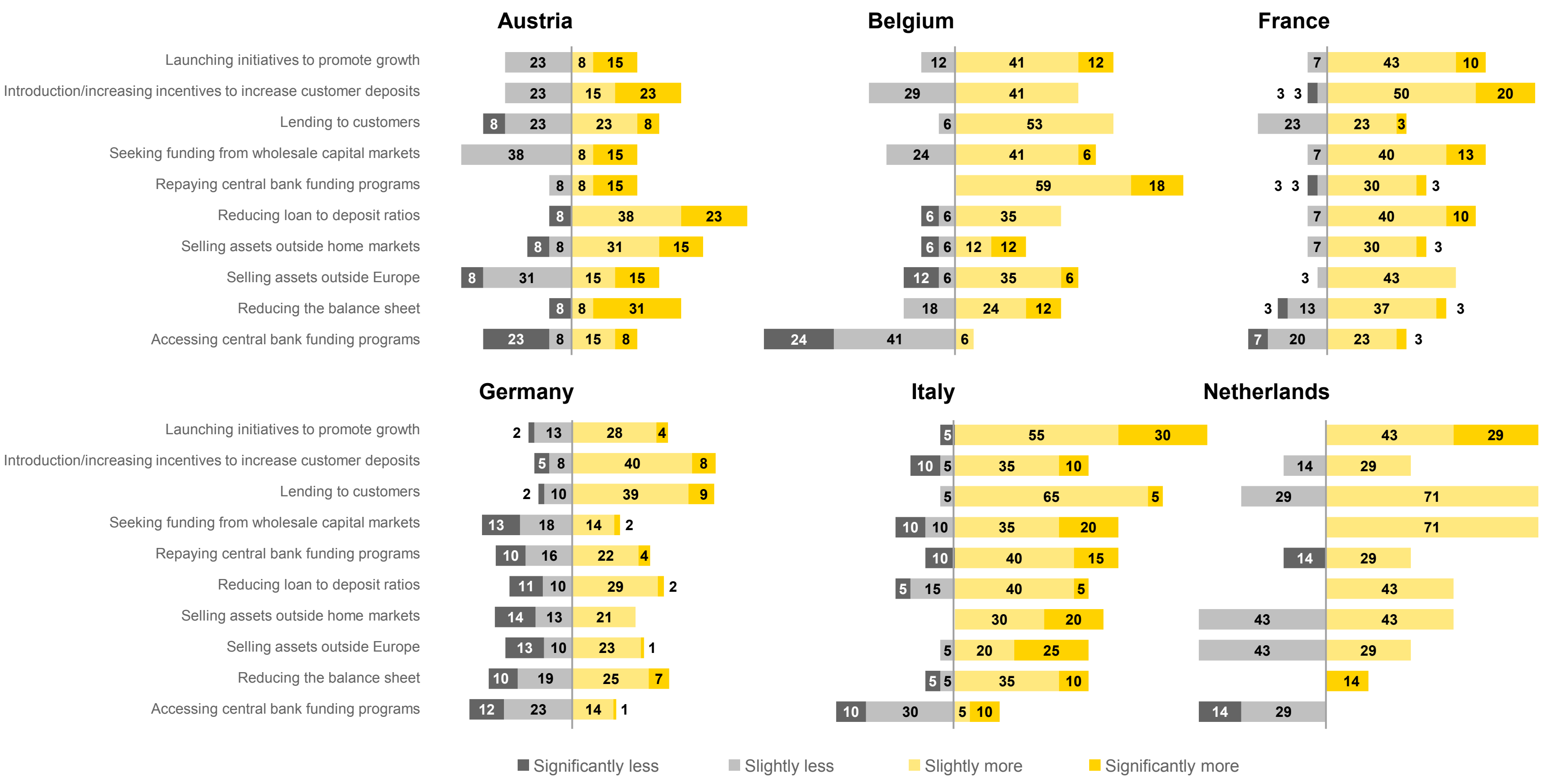


Comments: An improving economy and stronger balance sheets mean the emphasis bankers are placing on growth, first identified in EY's *European Banking Barometer – 2H13*, is now even more prominent. Fifty-seven percent of bankers now anticipate launching initiatives to promote growth, while 51% expect to increase lending to customers – up from 49% and 44%, respectively, in our last survey. Banks in Italy, the Netherlands, Poland and Spain are most focused on growing lending and developing new initiatives to promote growth. That does not mean balance sheets are fully repaired, however, and banks are still recalibrating their funding profiles by repaying central bank funding programs, and turning to deposit funding. Fifty-one percent of bankers expect their banks to introduce incentives to increase customer deposits over the next six months and loan to deposit ratios are also expected to improve.

* Numbers reflect the mean scores of respondents who answered on a scale of 1 to 5 where 1 denotes "Significantly less" and 5 denotes "Significantly more."

They also continue to rebalance their funding profiles by reducing reliance on central banks …

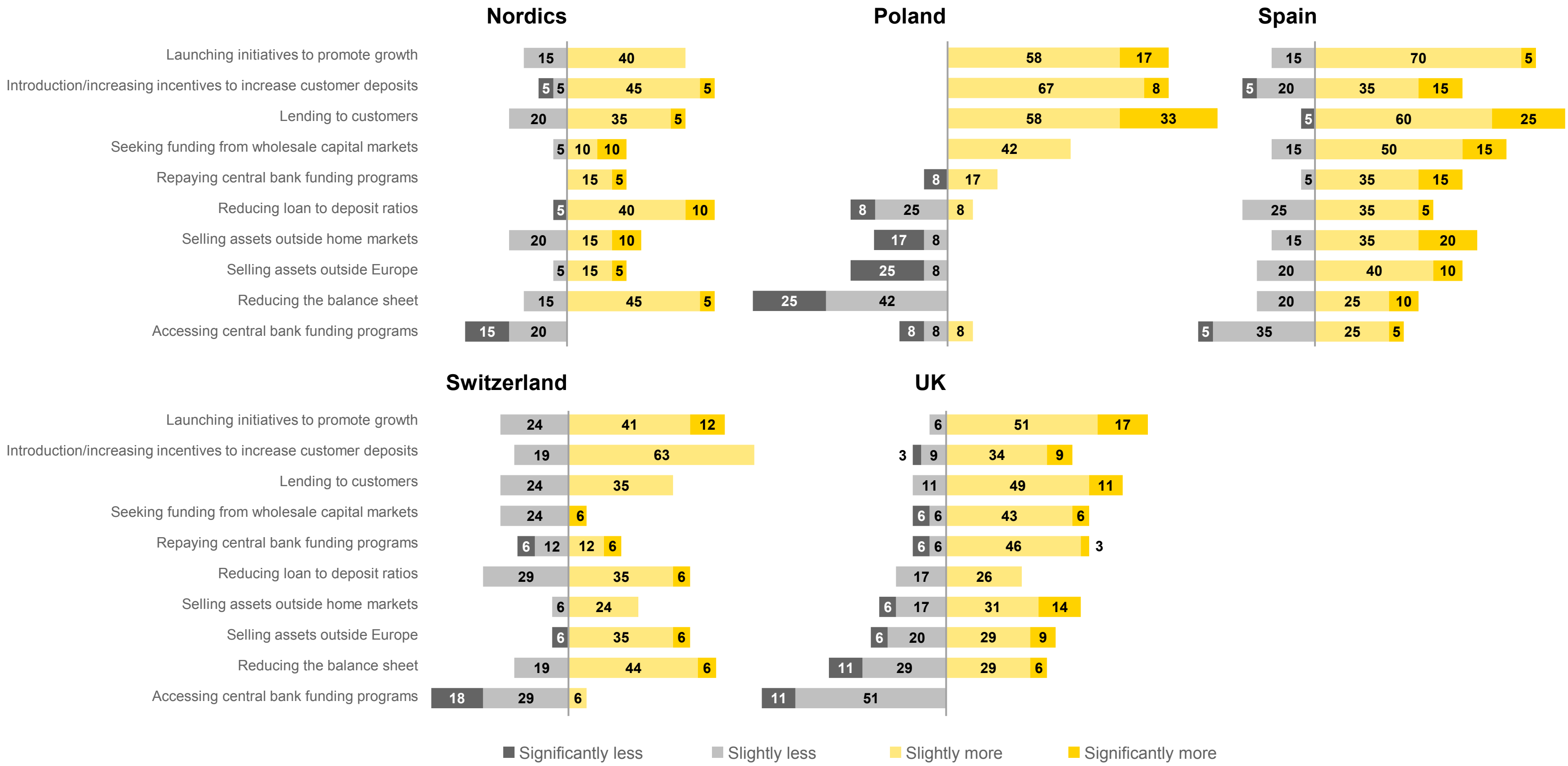
How likely are the banks in your market to be engaged in the following activities over the next six months?*



* Numbers reflect the percentage of respondents who answered.

… and introducing initiatives to increase customer deposits

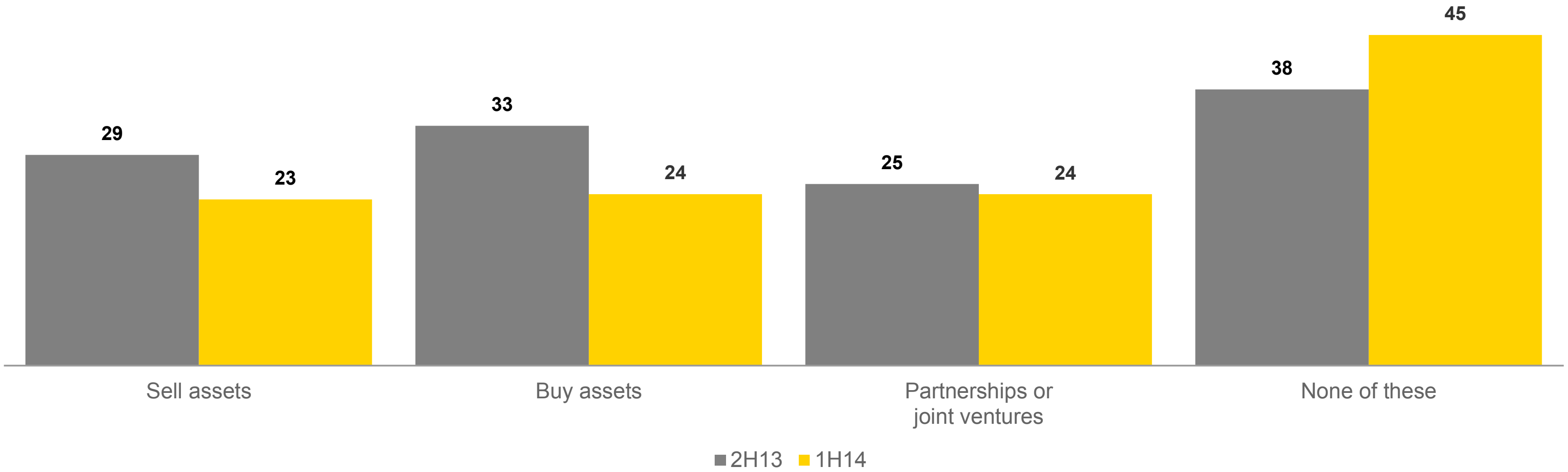
How likely are the banks in your market to be engaged in the following activities over the next six months?*



* Numbers reflect the percentage of respondents who answered.

The current restructuring of the banking sector is slowing, with fewer banks anticipating buying or selling assets …

Which, if any, of the following is your bank likely to consider over the next six months in relation to the countries in which it operates?*

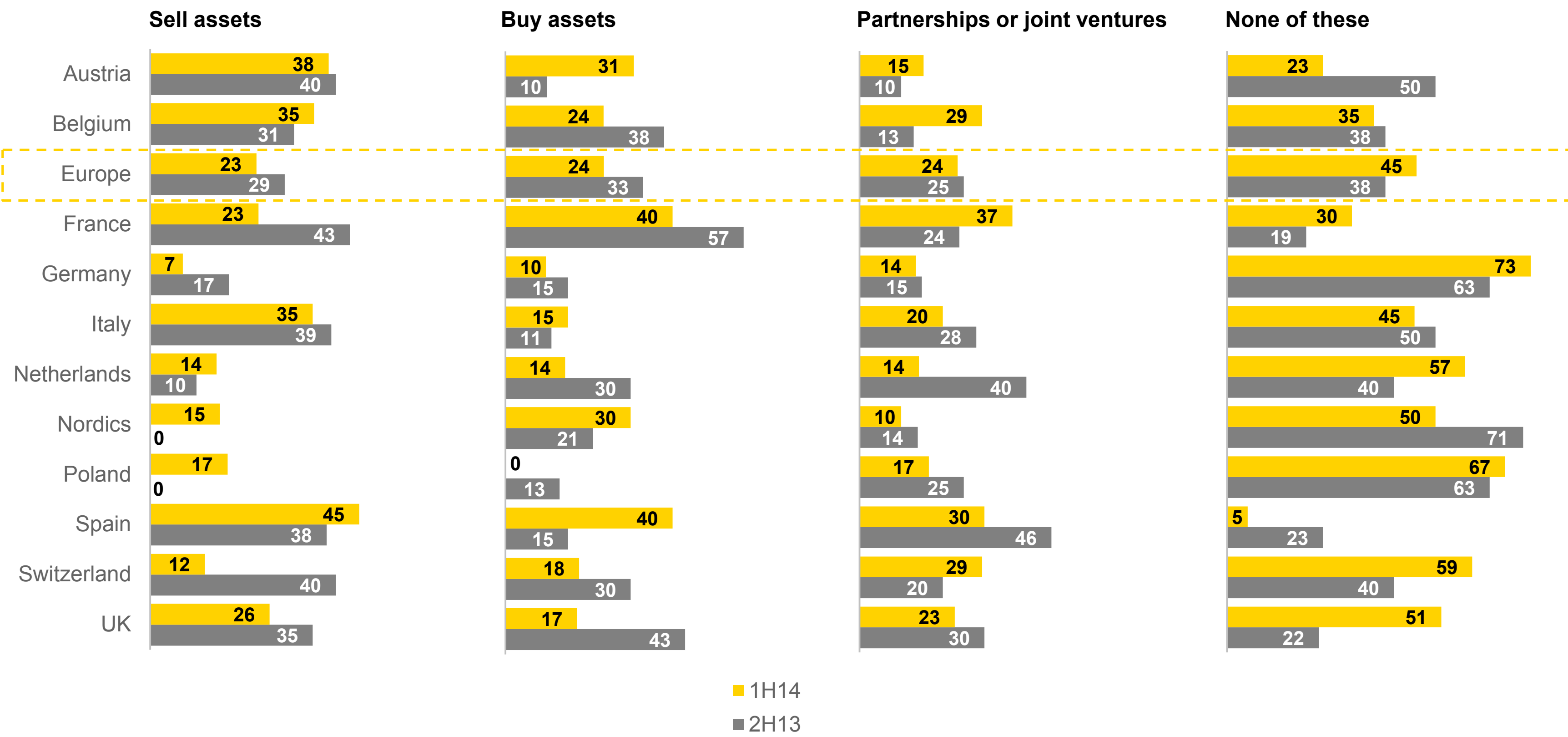


Comments: Over the past five years, many banks have sold assets as they have restructured their businesses to reduce complexity, raise capital or focus on core strengths. As a result, the number of bankers expecting asset sales (and accompanying purchases) has fallen. The majority of remaining asset sales are expected to be in Europe, as most banks have already exited non-core overseas franchises. Most asset purchases will also be in Europe. Where banks are considering overseas expansion, alliances are often the most attractive option. This is not only due to regulatory requirements in these markets, but also because many banks have learned from their previous mistakes of over-expansion. Joint ventures or partnerships can help banks gain exposure to high-growth markets without major upfront investment, as highlighted in EY's 2014 report *Banking in emerging markets: investing for success.*

* Numbers reflect the percentage of respondents who answered. Respondents could select more than one option.

… except in Spain and the Nordics where more banks expect to buy and sell assets

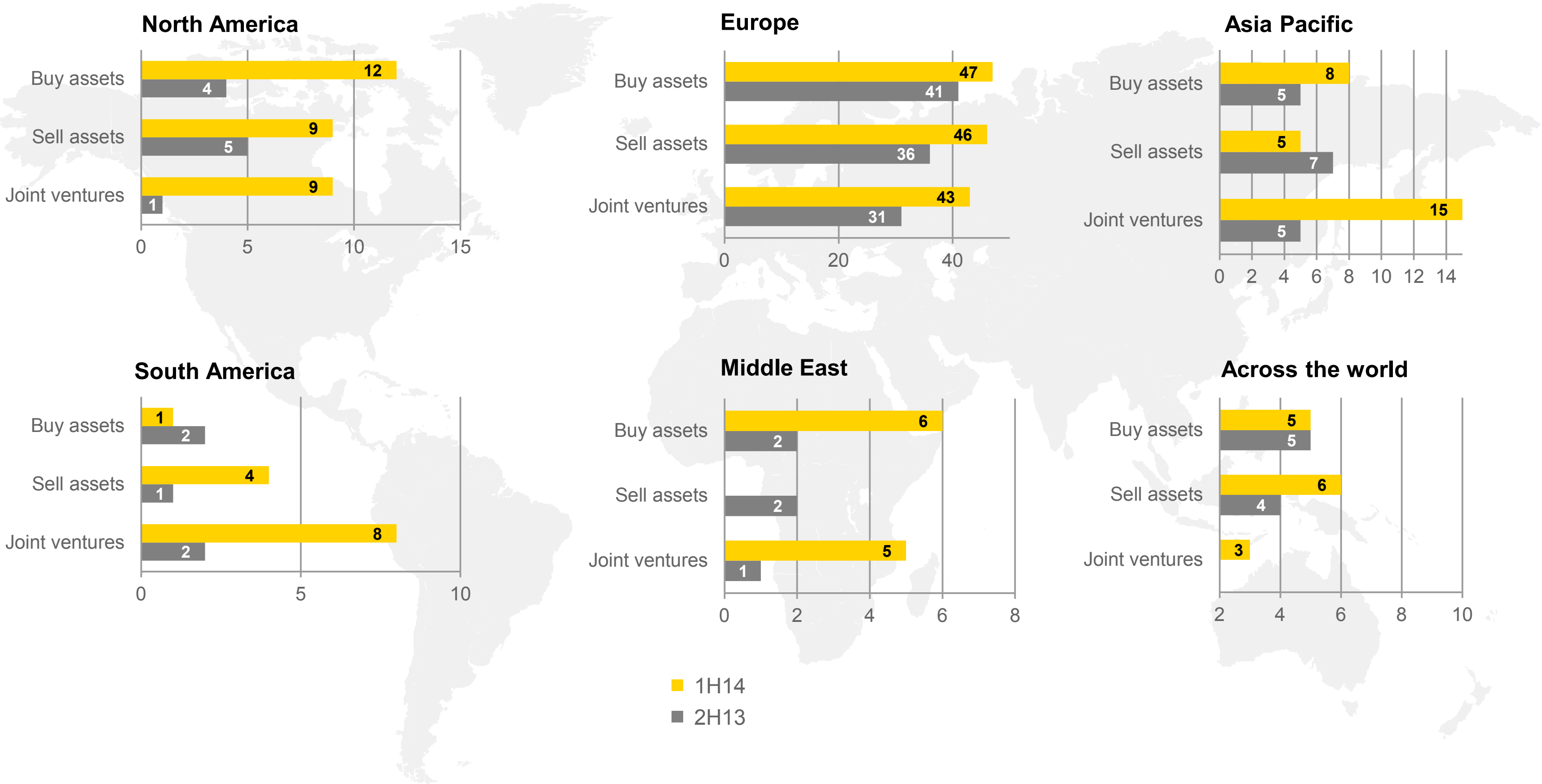
Which, if any, of the following is your bank likely to consider over the next six months in relation to the countries in which it operates?*



* Numbers reflect the percentage of respondents who answered. Respondents could select more than one option.

For banks thinking about expansion, particularly outside of Europe, collaboration is seen as increasingly important

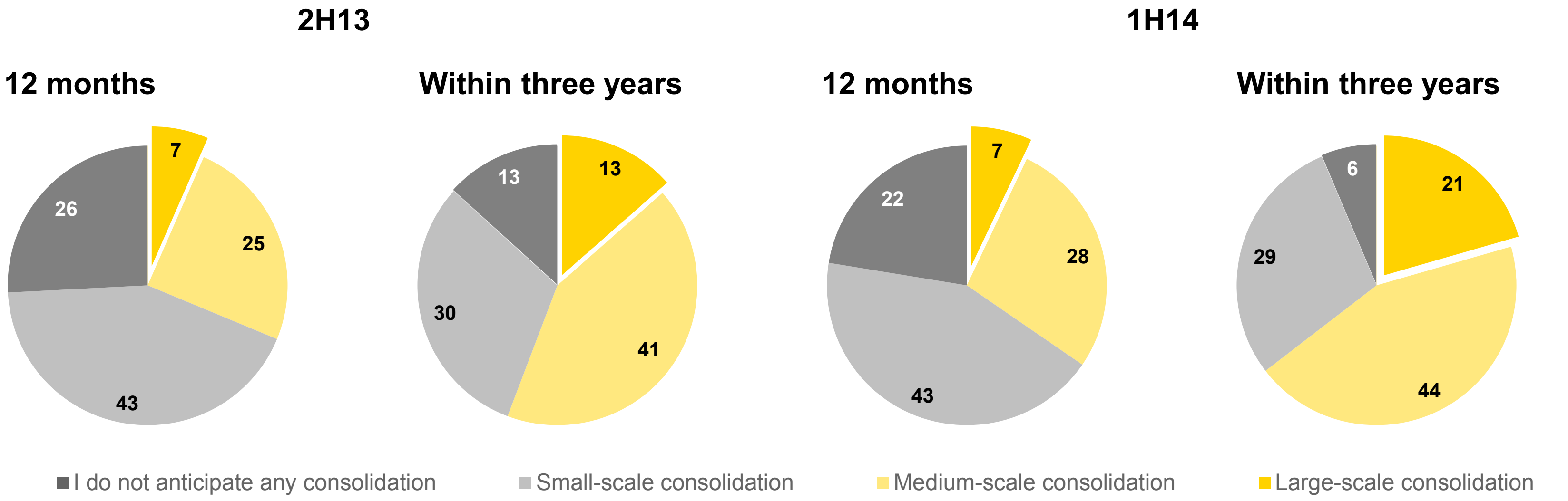
In which regions is your bank likely to sell assets, buy assets or consider joint ventures over the next six months?*



* Numbers represent the total number of mentions for that particular region. Respondents could state more than one region.

Despite a slowdown in industry restructuring, 65% of banks expect significant consolidation within the next three years

To what extent do you anticipate consolidation of the banking industry over the next 12 months and within the next three years?*

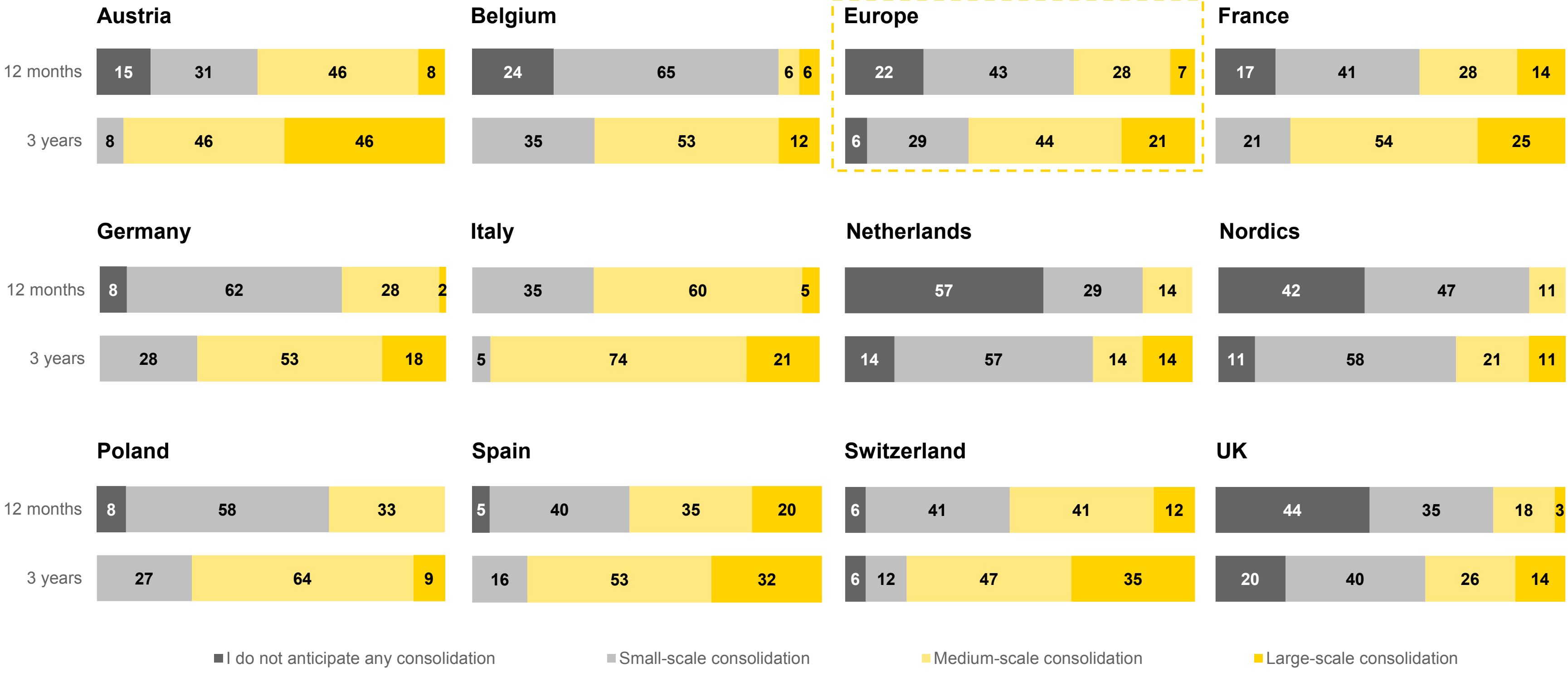


Comments: Despite the significant strides banks have made in strengthening their balance sheets, not only is it still early days for the European economic recovery, but the AQR is in progress. As a result, most institutions remain cautious of major acquisitions in the near term. As a result, only 7% of respondents anticipate large-scale consolidation in the next 12 months – the majority in Spain and France. However, over the next three years 63% of respondents expect medium- or large-scale consolidation. This longer-term consolidation will be focused in countries with a large number of small local banks (such as Spain and Italy) and may be accelerated by the AQR. In countries where the sector is already fairly concentrated (such as the UK), fewer bankers anticipate significant consolidation even in the medium term.

* Numbers reflect the percentage of respondents who answered. 1H14 base excludes respondents who answered “Don’t know.”

Italian banks expect the greatest consolidation of their sector – both in the short and medium term

To what extent do you anticipate consolidation of the banking industry in your market over the next 12 months and within the next three years?*



* Numbers reflect the percentage of respondents who answered. Base excludes respondents who answered "Don't know."

Section 4

Business priorities and product line expectations

Risk and regulation remain at the top of banks' agendas in all markets, but there is a growing division over whether …

Rank the importance of the following agenda items for your organization*

Comments: There are no signs that the regulatory burden for banks is diminishing – and with many European regulators increasingly concerned about banks' conduct, including customer protection, it is no surprise that risk and regulation remain at the top of bankers' priorities. Reputational risk is seen as particularly important. Recent analysis by the LSE revealed that between 2008 and 2012, conduct costs (including provisions and contingent liabilities), for just 10 leading banks in Europe and the US exceeded US $230bn[4] – underscoring the importance of resolving these issues. In this survey we have, for the first time, asked specifically about cybersecurity. This has emerged as a major issue for many financial institutions and is a key concern for banks in Belgium, France, the Netherlands and Switzerland. Beyond risk and regulation, the shift in banks' focus from survival to growth is highlighted by most items related to innovation and growth moving up several places in our ranking. More banks are now moving from preservation to expansion.

* Respondents were asked to rank the importance of activities on a scale of 0 to 10, where 0 denotes "Not at all important" and 10 denotes "Very important." Numbers show the percentage of respondents selecting either 8, 9 or 10. Base excludes respondents answering "Does not apply."

[1] Reputational risk includes tax transparency; compliance with capital markets regulations, i.e., MiFID II/EMIR; and investing in new customer-facing technology, e.g., mobile solutions.

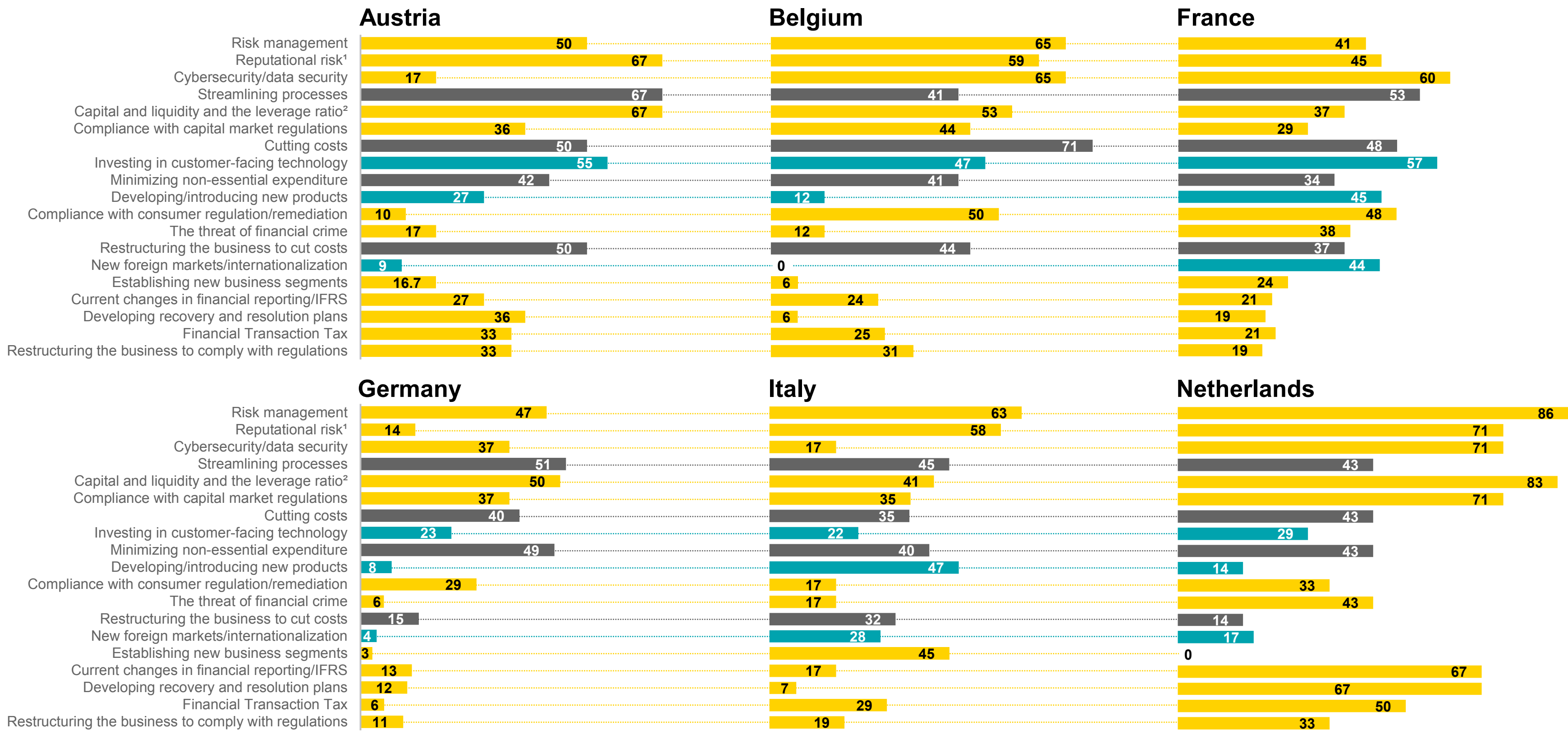
[2] For 2H13 survey, capital and liquidity and the leverage ratio were referred to as "Preparing for Basel III/CRD IV."

[3] Diversity requirements relating to CRD IV – putting in place a policy to promote diversity on management board.

[4] http://blogs.lse.ac.uk/conductcosts/bank-conduct-costs-results/

… their next priority is cost-cutting and efficiency, as in Austria, Germany and the Netherlands …

Rank the importance of the following agenda items for your organization*



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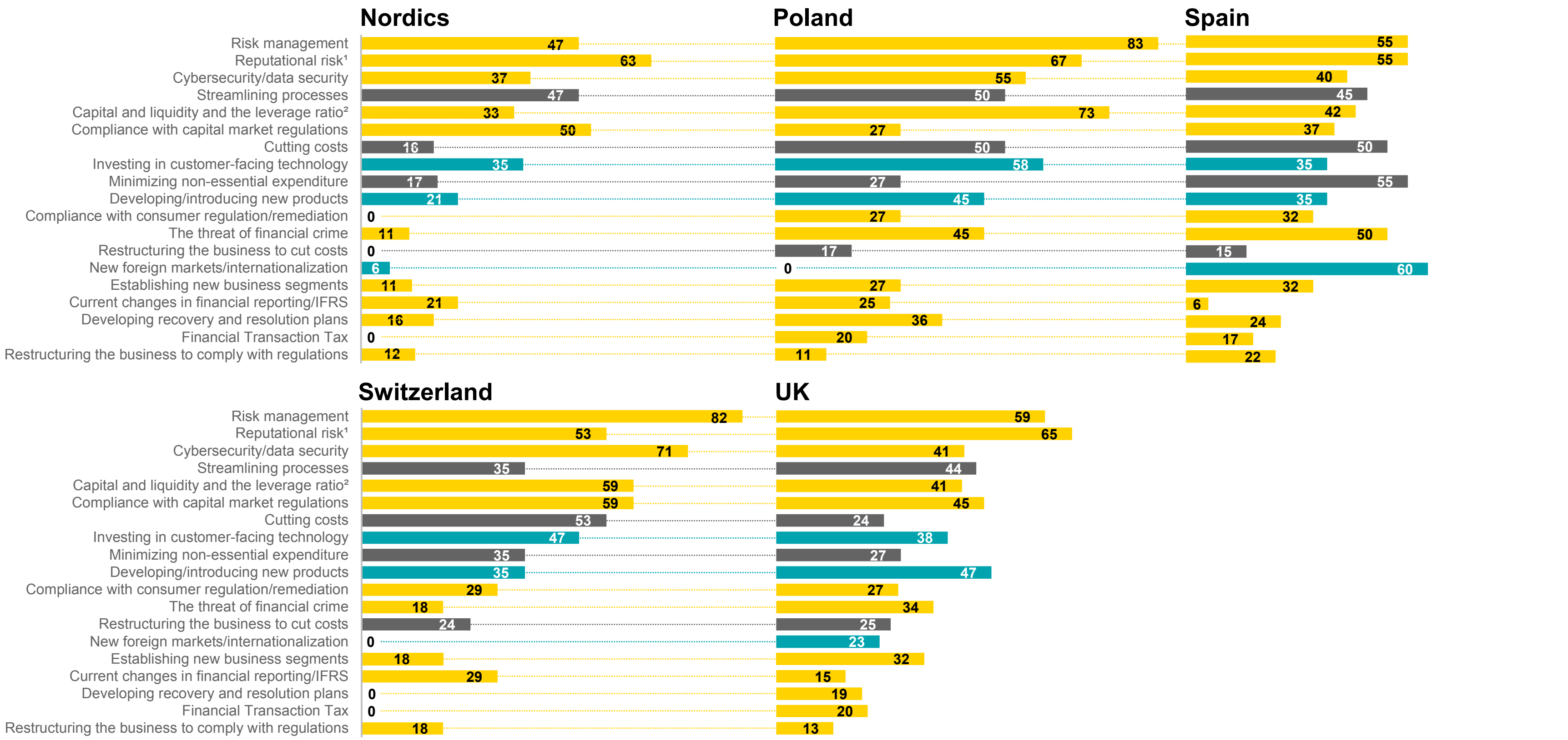
[1] Reputational risk includes tax transparency; compliance with capital markets regulations, i.e., MiFID II/EMIR; and investing in new customer-facing technology, e.g., mobile solutions.

[2] For 2H13 survey, capital and liquidity and the leverage ratio were referred to as "Preparing for Basel III/CRD IV."

… or innovation and growth, as in Spain, Poland and the UK

Rank the importance of the following agenda items for your organization*



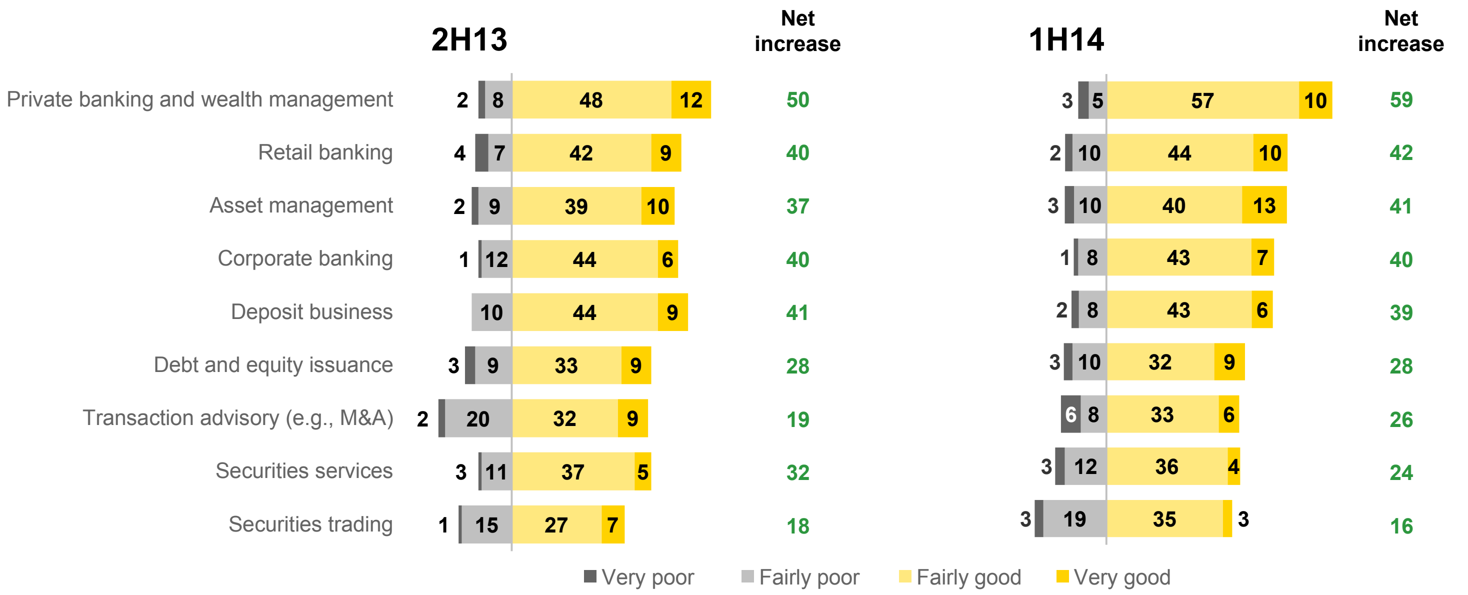
* Respondents were asked to rank the importance of activities on a scale of 0 to 10, where 0 denotes “Not at all important” and 10 denotes “Very important.” Numbers show the percentage of respondents selecting either 8, 9 or 10. Base excludes respondents answering “Does not apply.”

¹ Reputational risk includes tax transparency; compliance with capital markets regulations, i.e., MiFID II/EMIR; and investing in new customer-facing technology, e.g., mobile solutions.

² For 2H13 survey, capital and liquidity and the leverage ratio were referred to as "Preparing for Basel III/CRD IV."

Many bankers continue to anticipate an improved outlook for all business lines …

How do you rate the outlook for your bank over the next six months in each of the following business lines?*



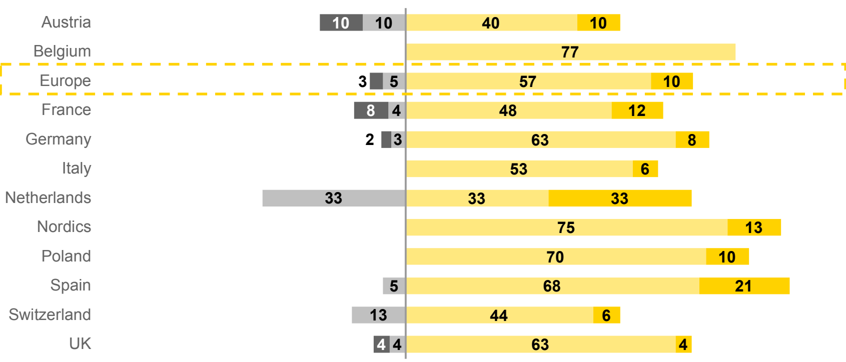
Comments: Bankers remain most optimistic about the outlook for private banking and wealth management. It is a particularly attractive segment, given its capital-light business model, and it is also a growing market. The wealth of EU28 billionaires has almost doubled since 2009 and grew around 23% in the last year alone, and is illustrative of increasing affluence of high net worth individuals. However, while the majority of bankers in all markets expect the outlook to improve for this business, it is also likely to be a very competitive segment. Bankers also expect an improved outlook for retail and corporate banking. With signs of an economic recovery in Europe, respondents are clearly hopeful that both businesses and individuals will look to borrow and invest. The outlook is less positive for securities services and trading; investment banks continue to suffer from the decline in fixed income businesses.

* Numbers reflect the percentage of respondents who answered. Respondents answering "Neither good, nor poor" are not displayed. Base excludes respondents answering "Does not apply" or chose not to answer.

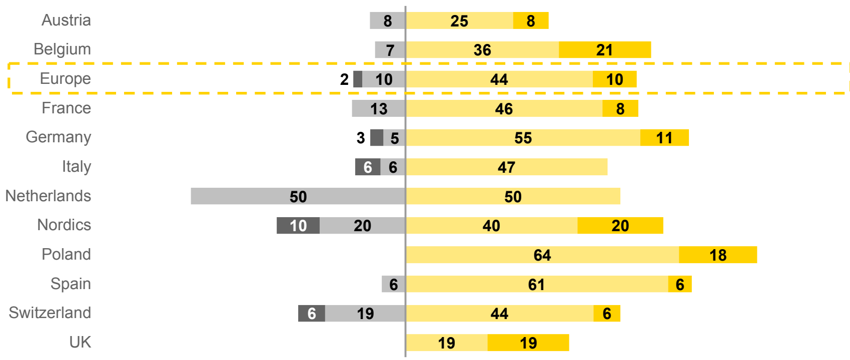
… with the strongest performance expected in wealth management, retail banking …

How do you rate the outlook for your bank over the next six months in each of the following business lines?*

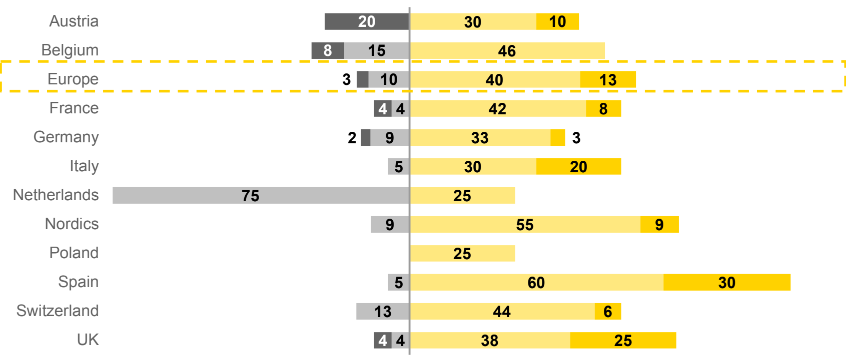
Private banking and wealth management



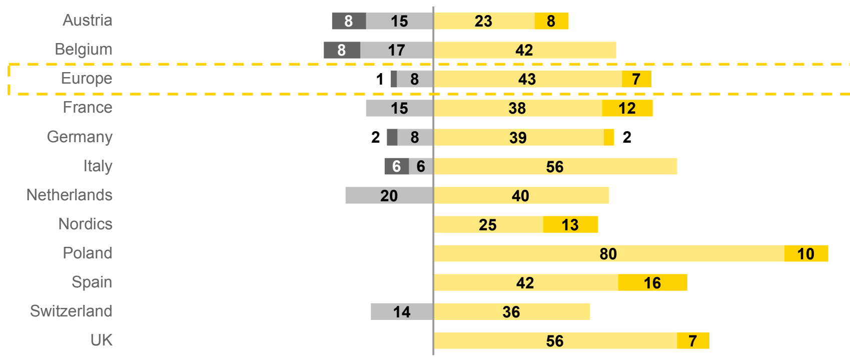
Retail banking



Asset management



Corporate banking



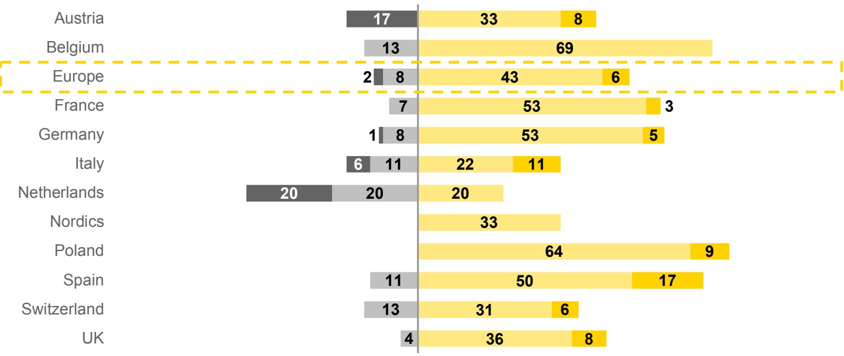
Very poor   Fairly poor   Fairly good   Very good

* Numbers reflect the percentage of respondents who answered. Respondents answering “Neither good, nor poor” are not displayed. Base excludes respondents answering “Does not apply” or chose not to answer.

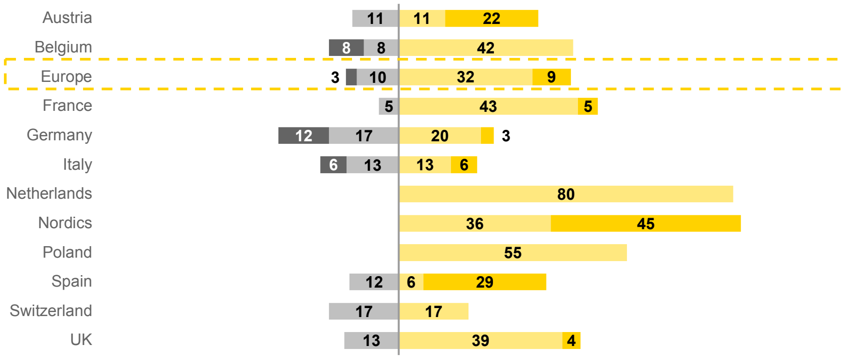
… and asset management. The outlook also remains very positive for corporate banking …

How do you rate the outlook for your bank over the next six months in each of the following business lines?*

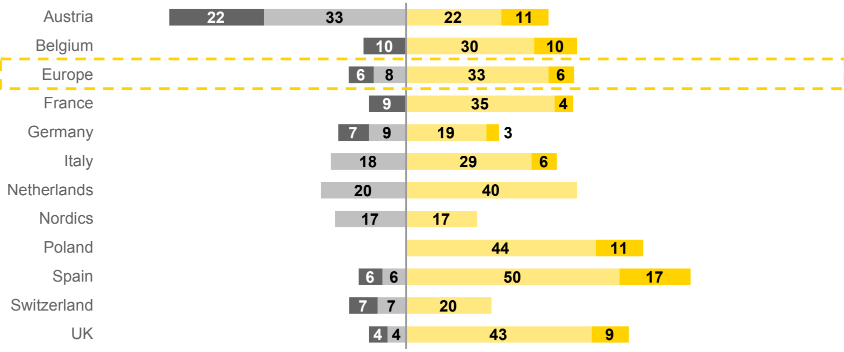
Deposit business



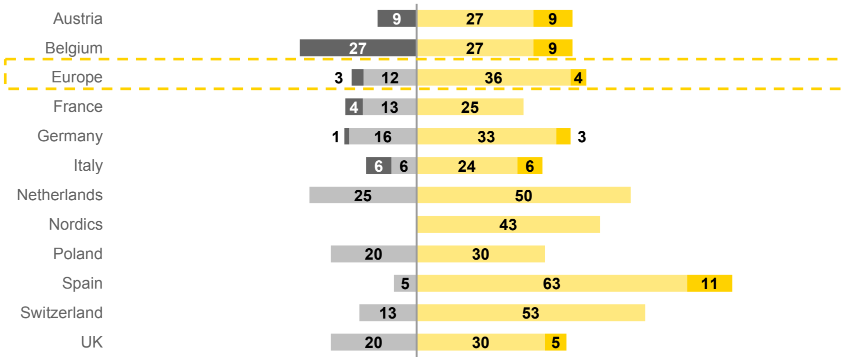
Debt and equity issuance



Transaction advisory



Securities services



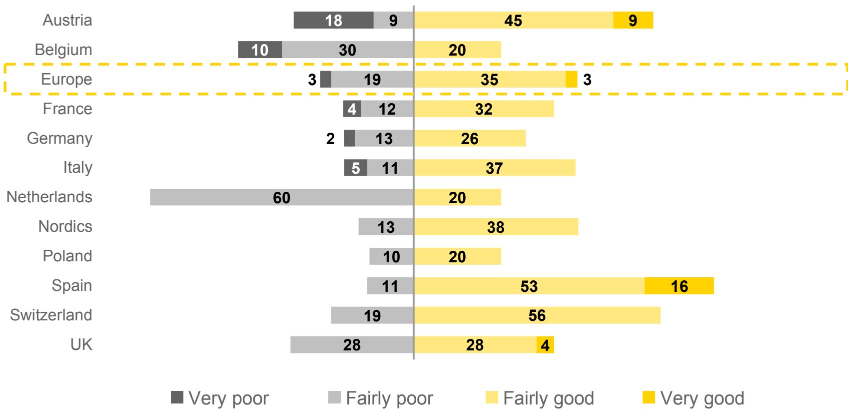
Very poor Fairly poor Fairly good Very good

* Numbers reflect the percentage of respondents who answered. Respondents answering “Neither good, nor poor” are not displayed. Base excludes respondents answering “Does not apply” or chose not to answer.

… but is more mixed for investment banking, with securities trading continuing to struggle

How do you rate the outlook for your bank over the next six months in each of the following business lines?*

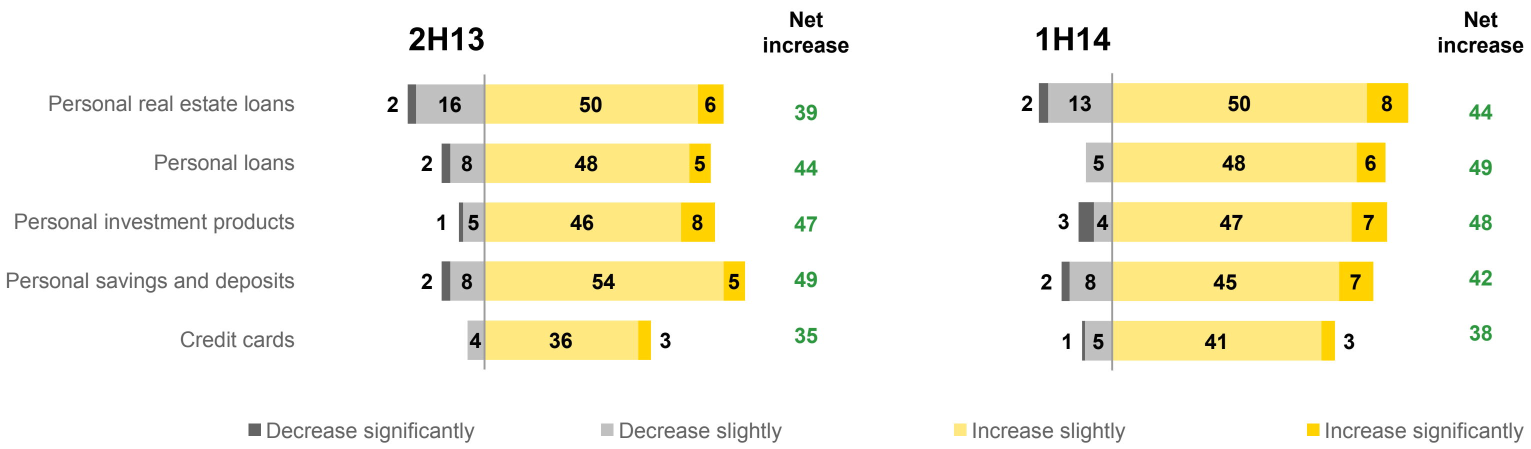
Securities trading



* Numbers reflect the percentage of respondents who answered. Respondents answering "Neither good, nor poor" are not displayed. Base excludes respondents answering "Does not apply" or chose not to answer.

Bankers expect growth in demand for credit and investment products to persist as the economy recovers …

How do you expect customer demand for retail products at your bank to change over the next six months?*



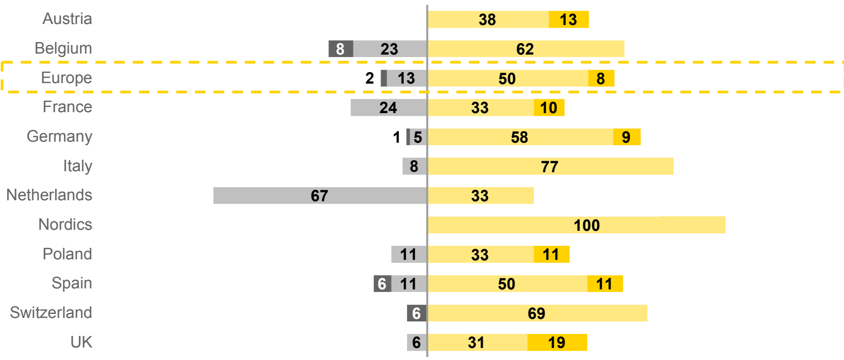
Comments: The improved outlook for retail banking is clearly driven by an anticipated increase in demand for all credit and investment products. The combination of falling unemployment, a more stable economy and ultra-low rates across Europe will allow more individuals – at least for the moment – to take on debt at low interest rates. Fifty-eight percent of banks expect demand to increase for real estate and 51% for personal loans, respectively. Low interest rates are also driving the increased demand for personal investment products. With deposit rates at minimal levels, we expect customers across Europe to look for alternative ways to improve the return on their savings.

* Numbers reflect the percentage of respondents who answered. Respondents answering “Stay the same” are not displayed. Base excludes respondents answering “Does not apply.”

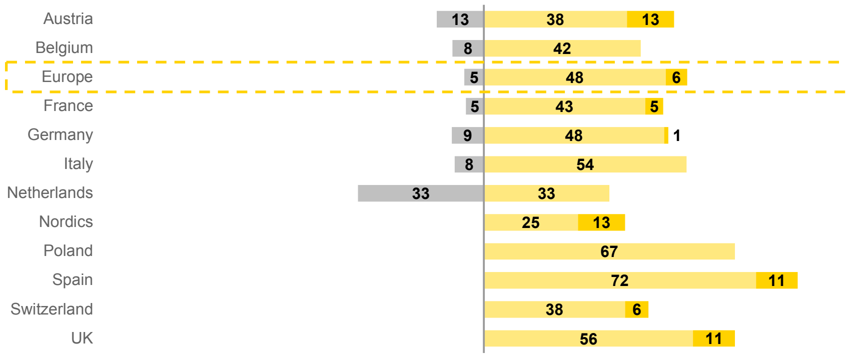
… with much greater demand for real estate loans anticipated in the Nordics and Italy, for personal loans in Spain …

How do you expect customer demand for retail products at your bank to change over the next six months?*

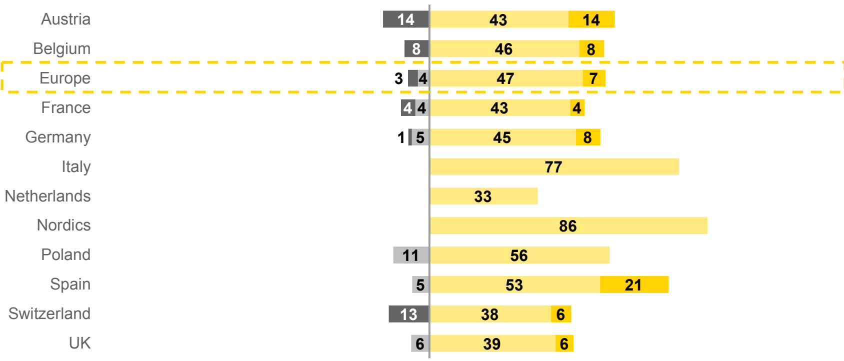
Personal real estate loans



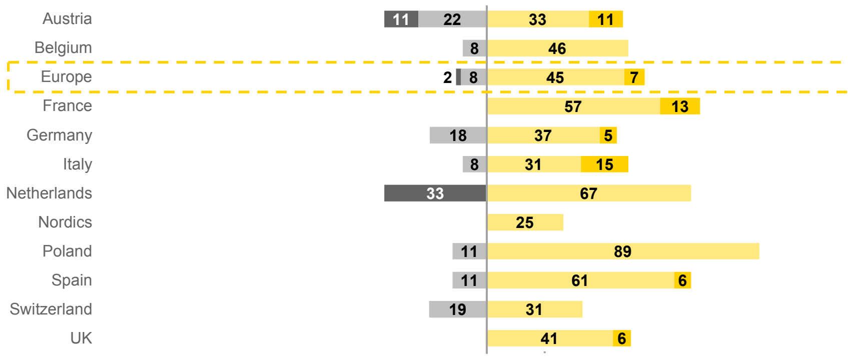
Personal loans



Personal investment products



Personal savings and deposit products



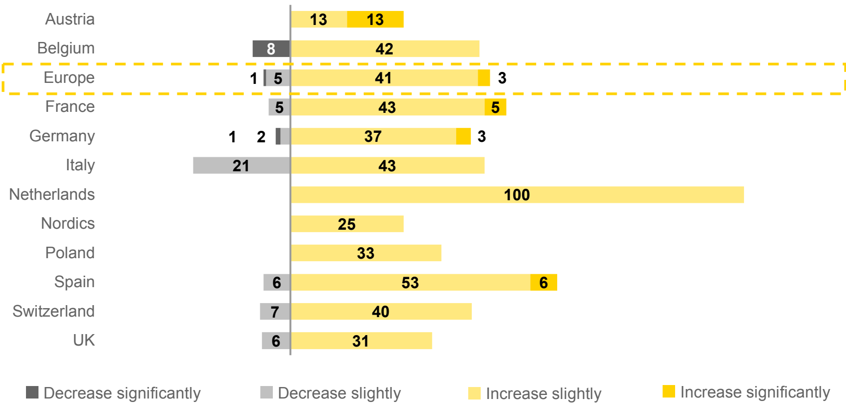
Decrease significantly Decrease slightly Increase slightly Increase significantly

* Numbers reflect the percentage of respondents who answered. Respondents answering “Stay the same” are not displayed. Base excludes respondents answering “Does not apply.”

… the UK and Poland, and for credit cards in the Netherlands

How do you expect customer demand for retail products at your bank to change over the next six months?*

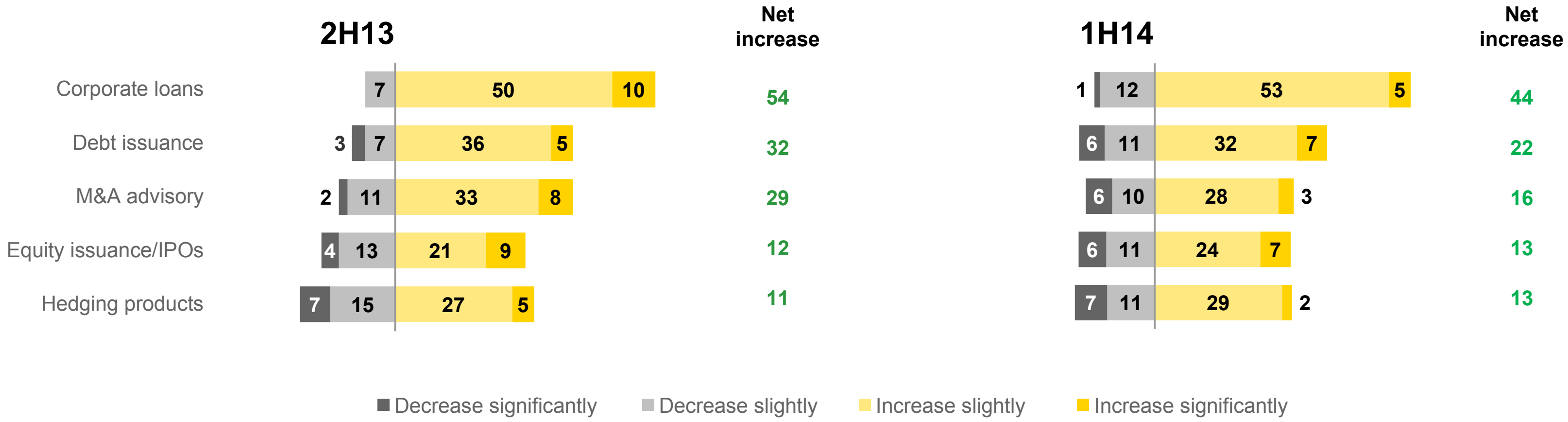
Credit cards



* Numbers reflect the percentage of respondents who answered. Respondents answering "Stay the same" are not displayed. Base excludes respondents answering "Does not apply."

Demand is still expected to increase for corporate products, albeit at a lower rate than in 2H13

How do you expect customer demand for corporate products at your bank to change over the next six months?*

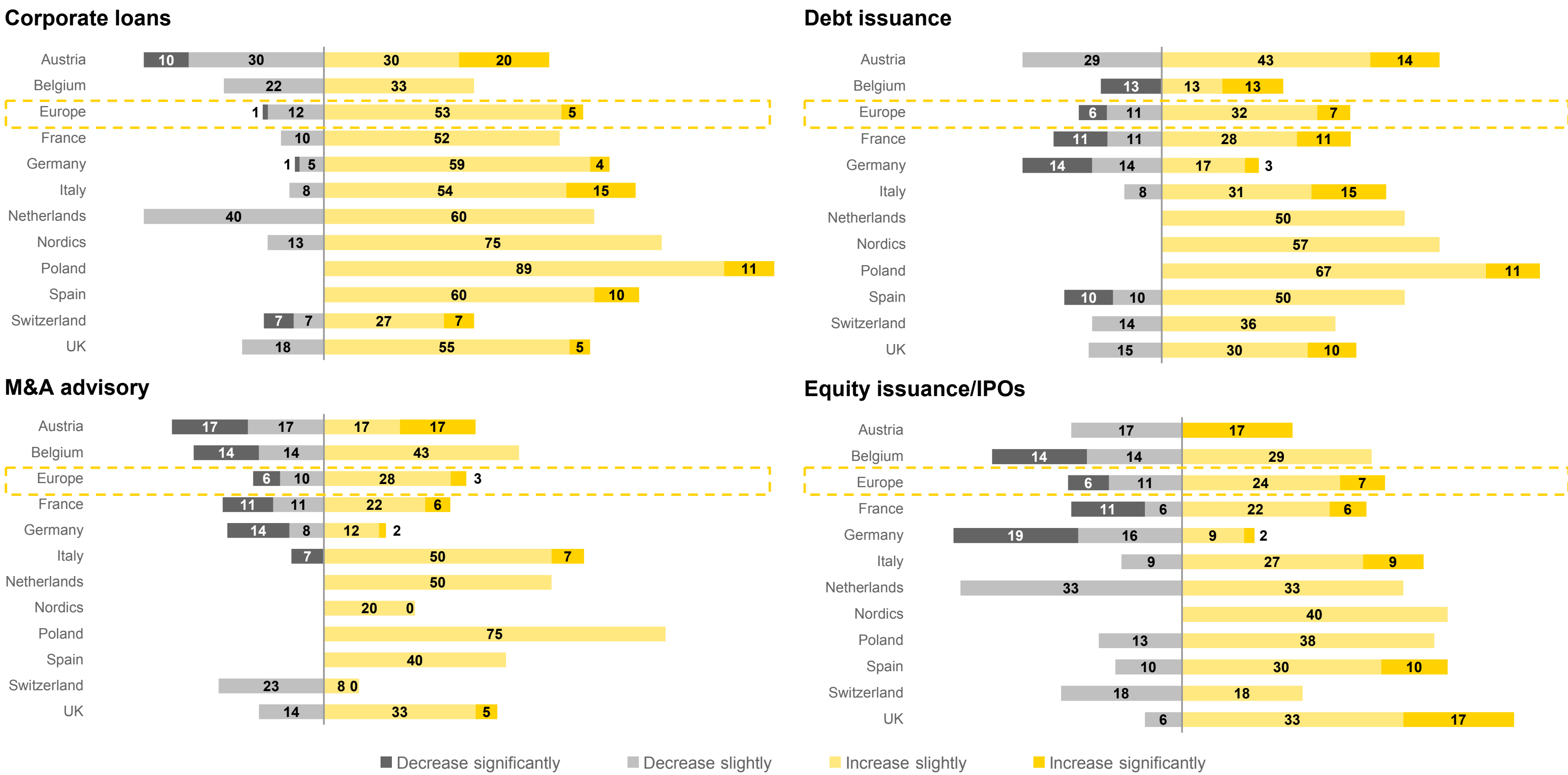


Comments: A more stable economy is also allowing companies to begin to think about expansion. Improvement in the Composite European Purchasing Managers Index, which tracks projected spending and production levels, suggests that European corporations will increase their capital expenditure. This expansion and investment will drive demand for advisory services and financing in the coming months. The greatest rise in demand is expected to be for corporate loans, and is most stark in Poland and the Nordics where 100% and 75% of respondents, respectively, expect this to increase. Demand for capital markets financing is also expected to increase, though much less rapidly, suggesting that a structural shift in the way European companies raise money is some way off.

* Numbers reflect the percentage of respondents who answered. Respondents answering “Stay the same” are not displayed. Base excludes respondents answering “Does not apply.”

Demand for debt, in the form of corporate loans and bonds, is expected to increase in almost all markets …

How do you expect demand for corporate products at your bank to change over the next six months?*

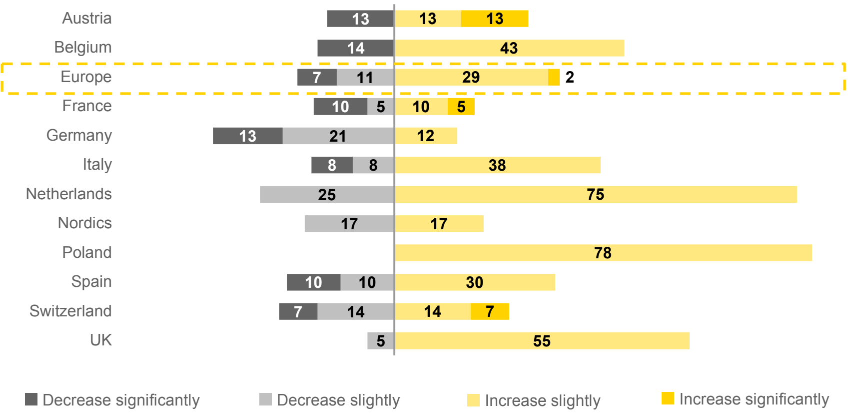


* Numbers reflect the percentage of respondents who answered. Respondents answering “Stay the same” are not displayed. Base excludes respondents answering “Does not apply.”

… but demand for equity financing will be more subdued, especially in Germany and Belgium

How do you expect demand for corporate products at your bank to change over the next six months?*

Hedging products



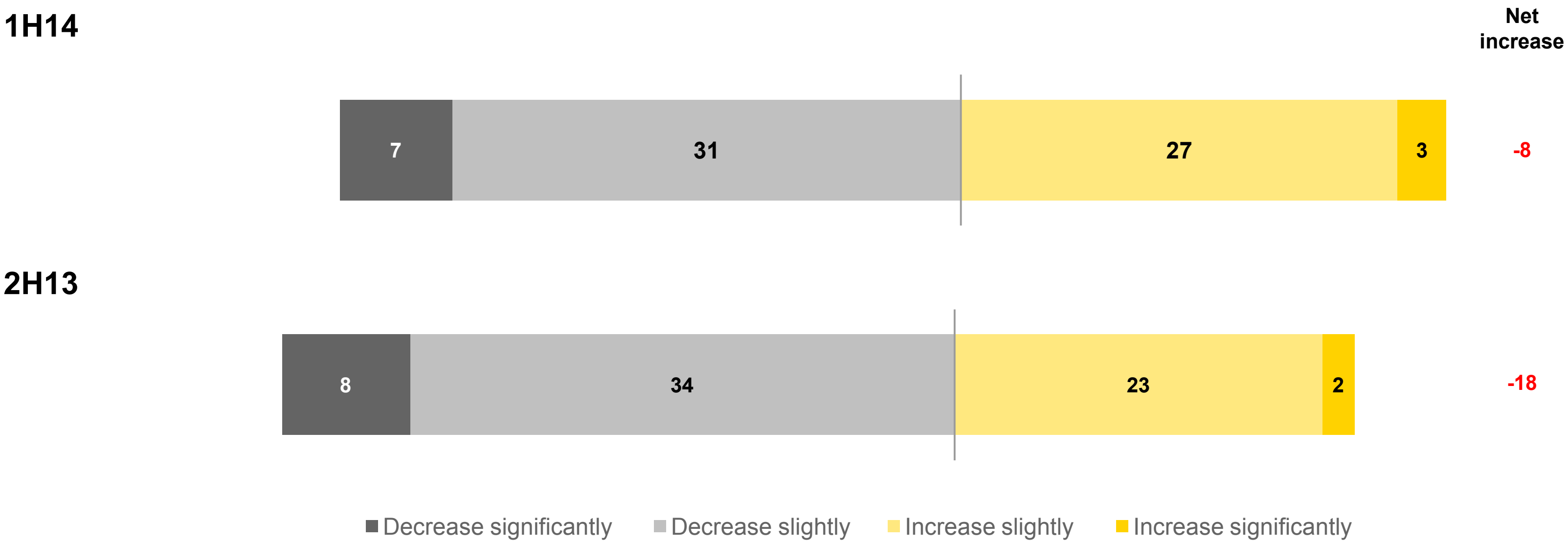
* Numbers reflect the percentage of respondents who answered. Respondents answering "Stay the same" are not displayed. Base excludes respondents answering "Does not apply."

Section 5

Headcount and compensation

A decline is anticipated in overall headcount, but the pace of cuts is expected to slow in most countries ...

Over the next six months, how do you expect the headcount of your bank to change?*

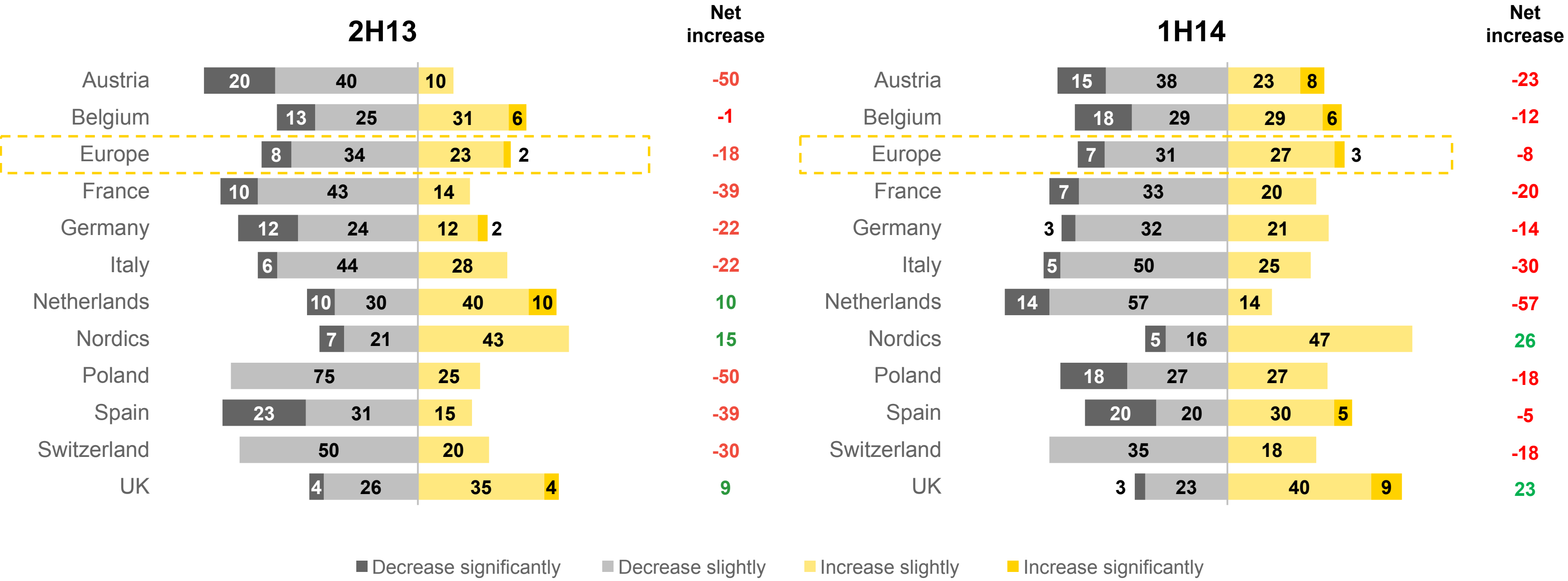


Comments: The number of bankers expecting headcount reductions has fallen and the number expecting job growth has risen. Thirty-eight percent of bankers now expect headcount to fall, compared with 42% in our last survey. Thirty percent of respondents expect headcount to increase, up from 25% in 2H13. A significant number of job losses are anticipated in Austria (53%), France (40%) and Switzerland (35%), where cost-cutting remains a key concern. However, in the Nordics and the UK, where institutions are beginning to focus on growth, 47% and 49% of respondents, respectively, actually expect to increase headcount.

* Numbers reflect the percentage of respondents who answered. Respondents answering “Stay the same” are not displayed. Base excludes respondents answering “Don’t know.”

… and in the Nordics and the UK many bankers now expect staff numbers to increase

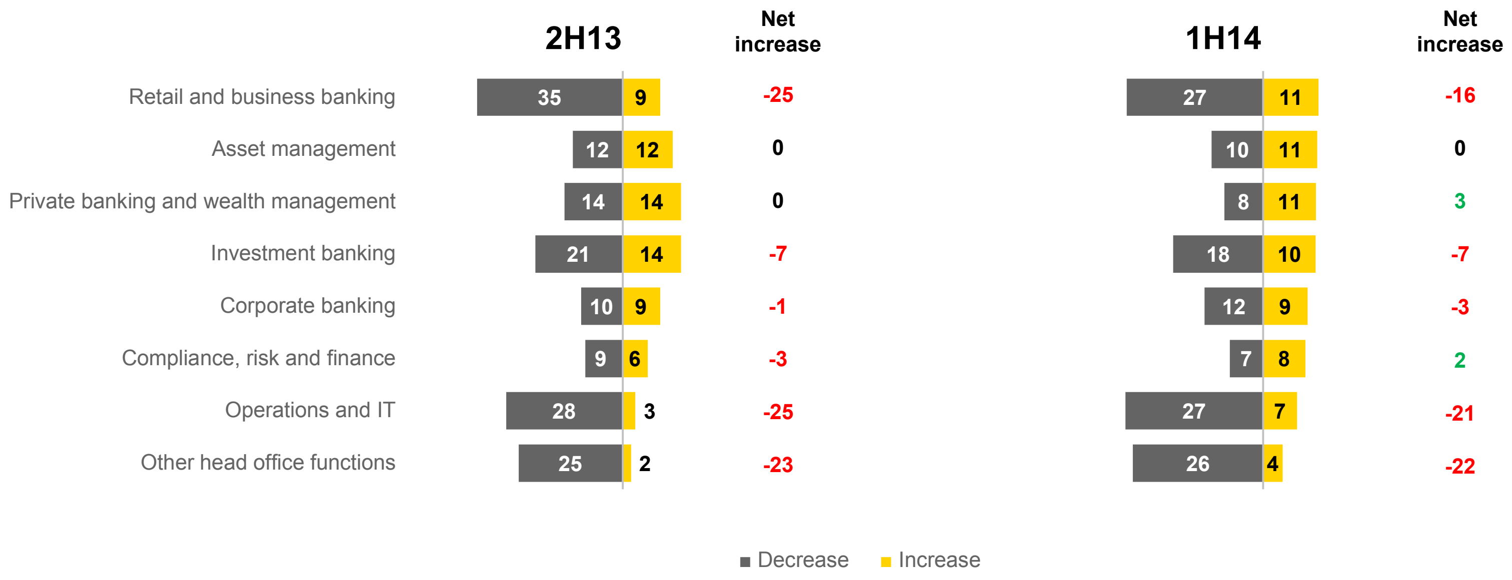
Over the next six months, how do you expect the headcount of your bank to change?*



* Numbers reflect the percentage of respondents who answered. Respondents answering "Stay the same" are not displayed. Base excludes respondents answering "Don't know."

Recruitment will be focused on growth sectors, such as private banking, as well as compliance functions …

In which areas of the business do you expect headcount to increase or decrease?*

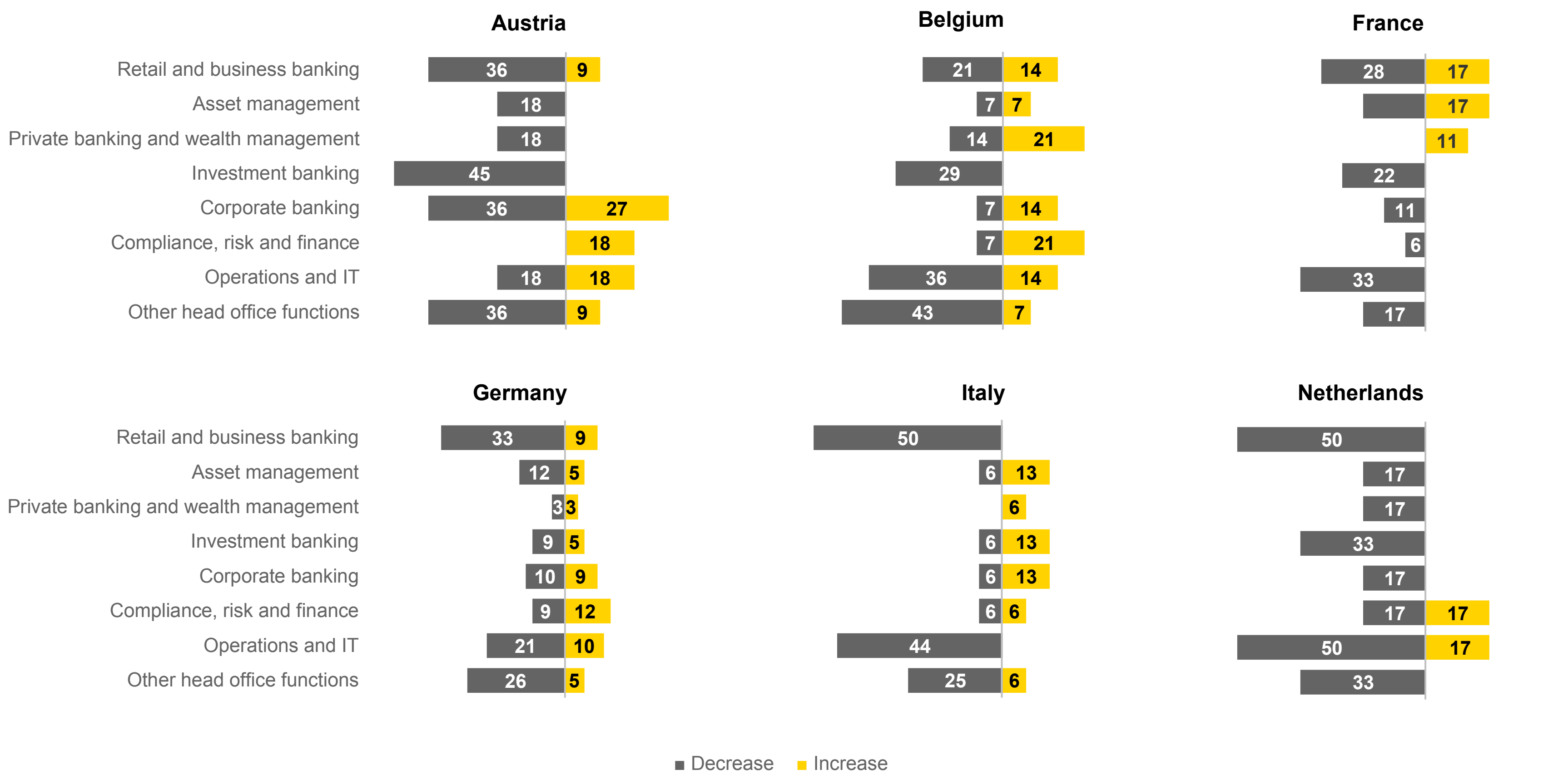


Comments: A seemingly unending wave of regulation and more assertive supervision continues to force banks to recruit staff to strengthen their compliance departments. Banks are also recruiting in growth areas, such as private banking. However, job losses are expected across other parts of the business. The greatest cuts will continue to be in the head office, operations and IT. A majority of bankers in almost all markets expect cuts to these functions. Twenty-seven percent of respondents also anticipate cuts in retail and business banking, with only bankers in the Nordics anticipating overall job growth in this segment; 31% expect headcount to increase and just 15% expect it to decrease. The outlook is also pretty gloomy for investment bankers – only in the UK, Italy, Spain and Poland do more respondents expect investment bank staff numbers to increase rather than decrease.

* Numbers reflect the percentage of respondents who answered. Base excludes respondents answering that headcount would "Stay the same."

… while job cuts in retail banking …

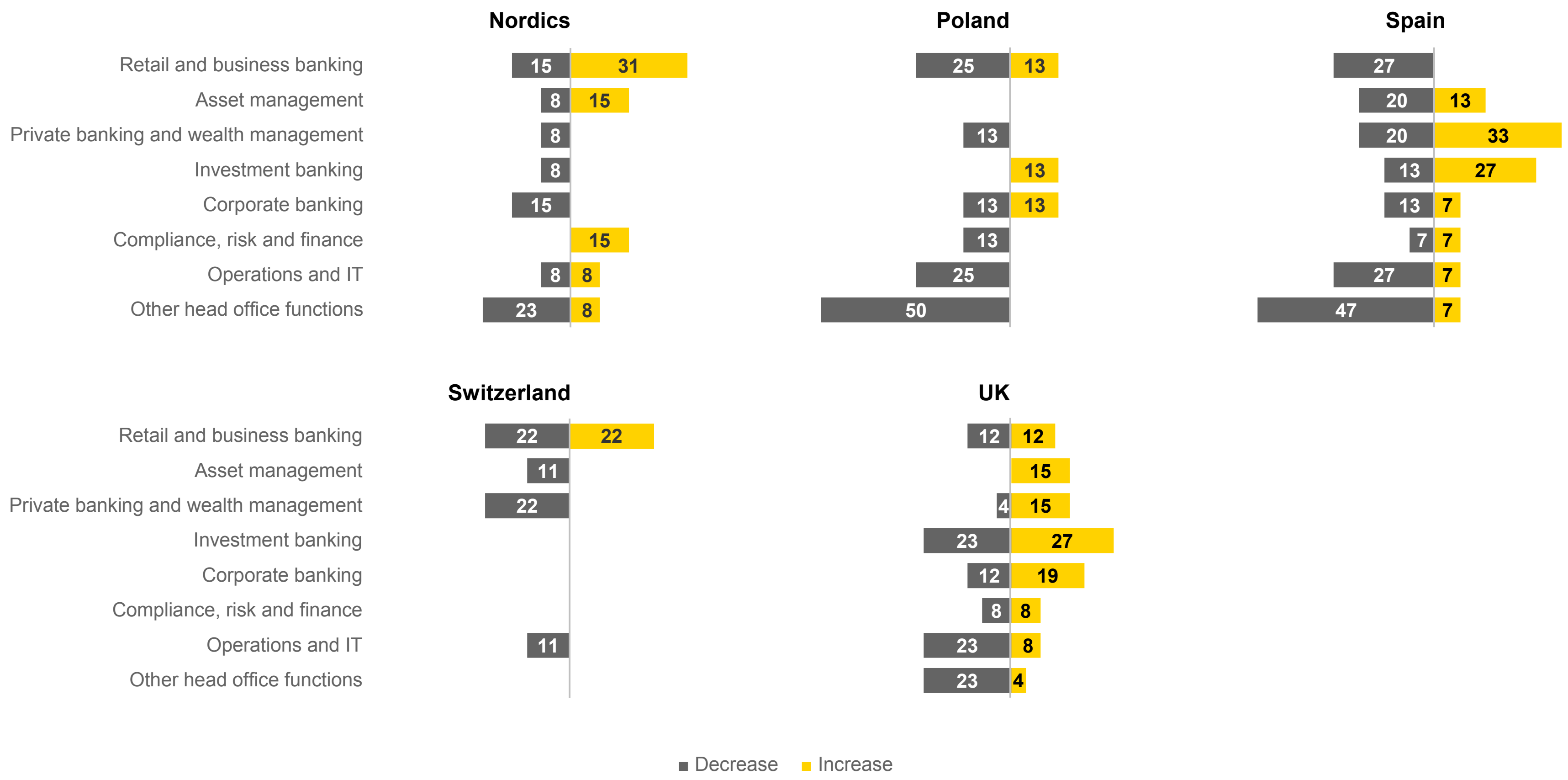
In which areas of the business do you expect headcount to increase or decrease?*



* Numbers reflect the percentage of respondents who answered. Base excludes respondents answering that headcount would "Stay the same."

… and the head office continue unabated

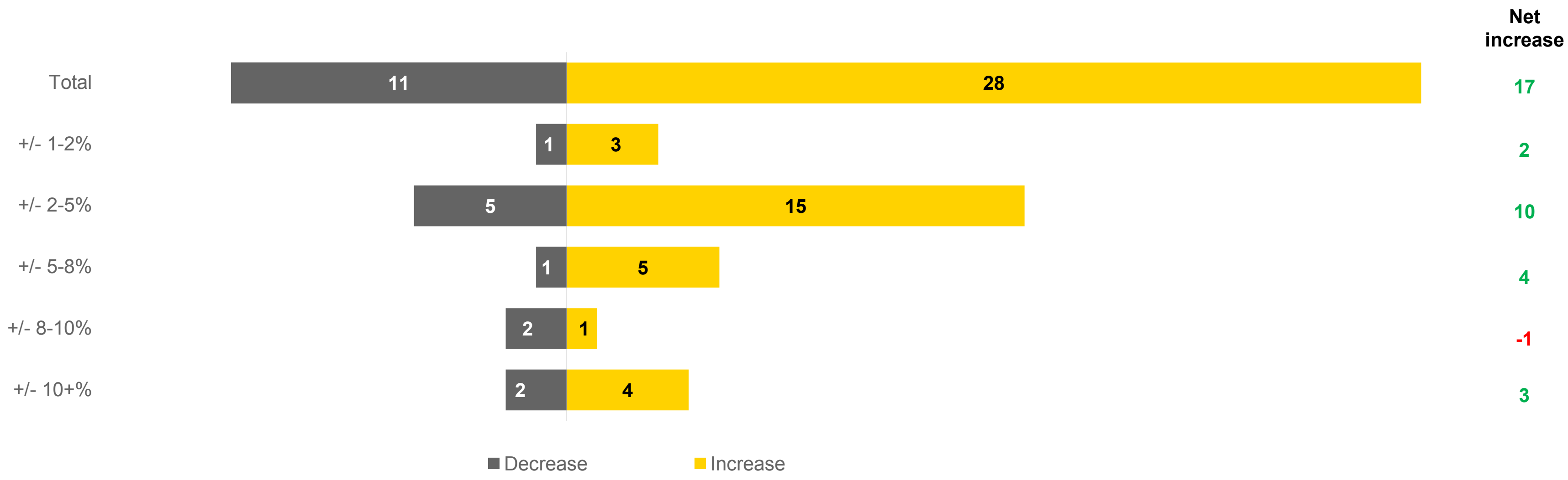
In which areas of the business do you expect headcount to increase or decrease?*



* Numbers reflect the percentage of respondents who answered. Base excludes respondents answering that headcount would "Stay the same."

Even though staff numbers are expected to fall, 28% of bankers expect their pay to increase

Compared to last year (FY13), to what extent will aggregate (i.e., total fixed and performance-related) compensation change at your bank this year (FY14)?



Comments: It is perhaps surprising that, given respondents' expectations of continued industry restructuring and the apparent inability of the sector to meaningfully improve ROE, 25% of banks expect aggregate pay to rise by over 2% in FY14 – above the current rate of inflation in both the euro area and the UK – with 4% expecting double-digit pay rises. There is a risk that with caps on bonuses, some of this rise will become an additional fixed cost for banks at a time when they are struggling to reduce their cost base or grow their revenues. Furthermore, with average ROE expected to remain well below the average cost of equity, banks will need to be able to justify any significant increases for individuals, or risk criticism from shareholders and politicians.

* Numbers reflect the percentage of respondents who answered. Respondents answering "Stay the same" are not displayed. Base excludes respondents answering "Don't know."

While most bankers across Europe expect their pay to stay the same …

Compared to last year (FY13), to what extent will aggregate (i.e., total fixed and performance-related) compensation change at your bank this year (FY14?)?

* Numbers reflect the percentage of respondents who answered. Respondents answering “Stay the same” are not displayed. Base excludes respondents answering “Don’t know.”

… more than 10% of respondents in Spain and the UK expect double-digit increases!

Compared to last year (FY13), to what extent will aggregate (i.e., total fixed and performance-related) compensation change at your bank this year (FY14?)?

* Numbers reflect the percentage of respondents who answered. Respondents answering "Stay the same" are not displayed. Base excludes respondents answering "Don't know."

Section 6

Contacts

Contacts

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