Euro Banking Pulse

Profitability and resilience analysis of the top European Banks from 2018
June 2019

ALVAREZ & MARSAL

Foreword

Euro Banking Pulse

Alvarez & Marsal (A&M) is delighted to publish the first edition of the Euro Banking Pulse (The Pulse). This annual report examines the 24 largest European banks in 2018, scoring each of them against key performance indicators (KPIs) linked to both profitability and resilience using proprietary calibration based on the European Banking Authority (EBA) and A&M thresholds.

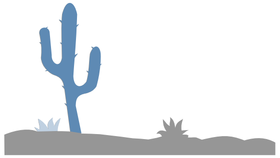
All the data used in this report has been obtained from publicly available sources. The methodology for the calculations is discussed in the glossary.

The Pulse aims to help banking executives and board members stay current on industry trends.

We hope that you will find The Pulse useful and informative.

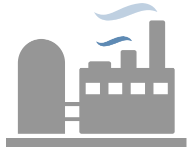
Contents

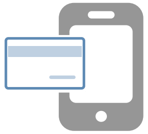
1. European Banking Landscape – the Toughest Battlefield



- Three years of flat to negative interest rates together with very thin credit growth can only mean the revenue pool gets dryer.

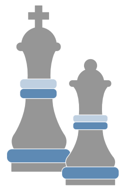
- Five years of headwinds from regulation pushing for more resilience in capital, liquidity and provisions mean higher engine and fuel costs to open shop for business.





- Leaner and innovative business models are eroding the competitive wall created between banks and their customers, forcing revenues to be allocated into digital and marketing defensive play heavy investments.

- Top European banks lack adequate resilience and returns above the expectations of customers, markets and regulators. European banking has become a battle only for the brave.



2. Key Takeaways: Four Kingdoms and One Empty Throne

For the first time A&M has analysed profitability and resilience of the Top 24 banking leaders in Europe, with four groups emerging to compete for success.

	Banks	2018 – Outcome
Battle for the Throne	Credit Agricole, ABN Amro, Credit Mutuel, BBVA, Danske Bank, HSBC, Nordea	▪ Despite leading the European banks in terms of profitability and resilience, no single bank could score high enough to claim the throne. The sweet spot on the A&M map is empty. ▪ Banks need to deliver and have low volatility in KPIs quarter over quarter.
Quest for Profitability	Commerzbank, Barclays, RBS, Standard Chartered	▪ Northern European banks have prioritised building up resilience but are now struggling to generate enough returns. ▪ Banks need to put their profitability agenda on the frontline of decision making.
The Resilience Trail	Santander, Caixa Bank, Banca Intesa, Rabobank, Lloyds Banking Group	▪ A group of banks have identified profit pools but need to build up resilience while demonstrating consistent quarterly performance. ▪ Banks should build up a robust internal capital generating business model and strategies for coming regulatory changes.
Shields up and Strategic Moves	BNP Paribas, Deutsche Bank, BPCE, DZ Bank, Societe Generale	▪ Four banks are falling behind the pack and need to rethink their strategy and restructure parts of their business. ▪ Cost restructuring and lean business models need to be played simultaneously with difficult capital allocation decisions.

3. A&M Scoring Methodology

How the banks are scored

- A&M Score Methodology ranks banks using 13 performance KPIs (see Appendix for definitions) and latest available public information.
- Each bank gets a 1-4 point score (1 best performing and 4 worst performing) using proprietary calibration based on European Banking Authority (EBA) and AM thresholds.

Key Performance Indictors

The 13 KPIs have been aggregated into six families of KPI groups of performance indicators and two general views (profitability and resilience).

General views	KPI Group	Individual KPI
Profitability	Growth	Loan Growth Deposit Growth
	Operating Efficiency	Net Interest Margin (NIM) Operating Income / Assets Cost-to-Income Ratio (C/I)
	Profitability	Return on Equity (RoE) Return on Assets (RoA)
Resilience	Risk	Non-Performing Loan (NPL) ratio Coverage Ratio
	Liquidity	Liquidity Coverage Ratio (LCR) Loan-to-Deposit Ratio (LDR)
	Solvency	CET1 Ratio f.l. Leverage ratio

4. Who we analysed: 24 Largest European Banks

Abbreviation	Bank	Assets € Billion
HSBC	HSBC	2,251
BNP	BNP	2,040
CAI	Credit Agricole	1,854
SAN	Santander	1,459
DB	Deutsche Bank	1,348
SG	Societe Generale	1,309
BPCE	BPCE	1,273
UBS	UBS	958
ING	ING	887
UNI	UniCredit	831
CMUT	Credit Mutuel	801
INTE	Intesa	788

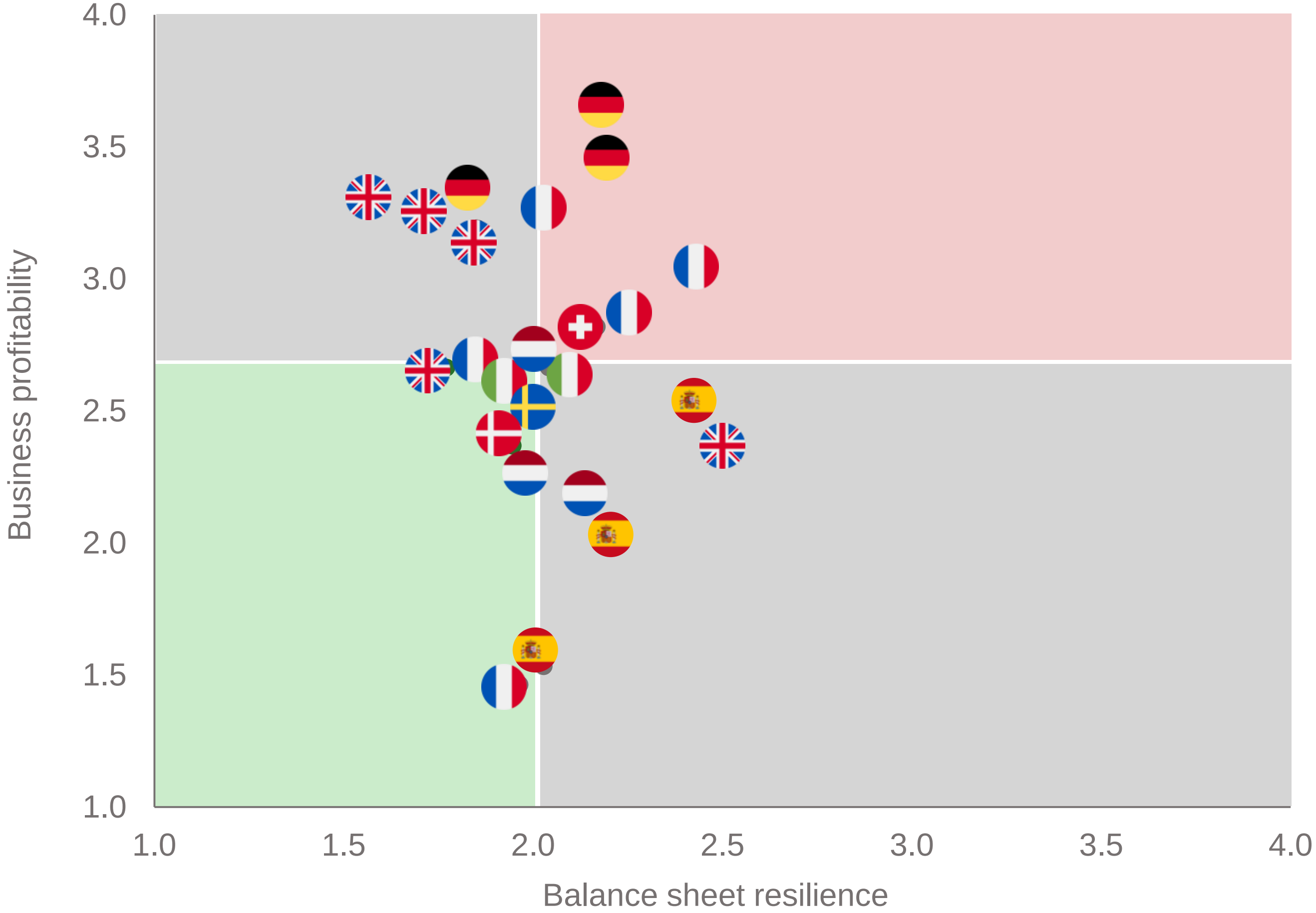
Abbreviation	Bank	Assets € Billion
BARC	Barclays	772
LLOYDS	Lloyds BG	701
RBS	Royal Bank Scotland	694
BBVA	BBVA	677
STANCH	Standard Chartered	635
RaBO	Rabobank	590
Nordea	Nordea	551
DZ	DZ Bank	505
DKB	Danske Bank	465
CoBA	Commerzbank	462
CKB	Caixa Bank	386
ABN	ABN Amro	381

Note 1: Banks are sorted by asset size

5. Country View

Scoring by country based on Profitability and balance sheet resilience.

Country view helps see trends across a still EU low cross border industry



United Kingdom

U.K. banks score relatively high on resilience based on asset quality but fall short when it comes to profitability due to low returns.

Nordics and Netherlands

Nordic and Dutch Banks are well balanced in profitability and resilience outperforming their peers.

Germany

German banks fall short on profitability based on low returns and high cost-to-income and two banks are in danger zone.

France

Two French local banks are well positioned, but two global banks sit in the danger zone.

Spain

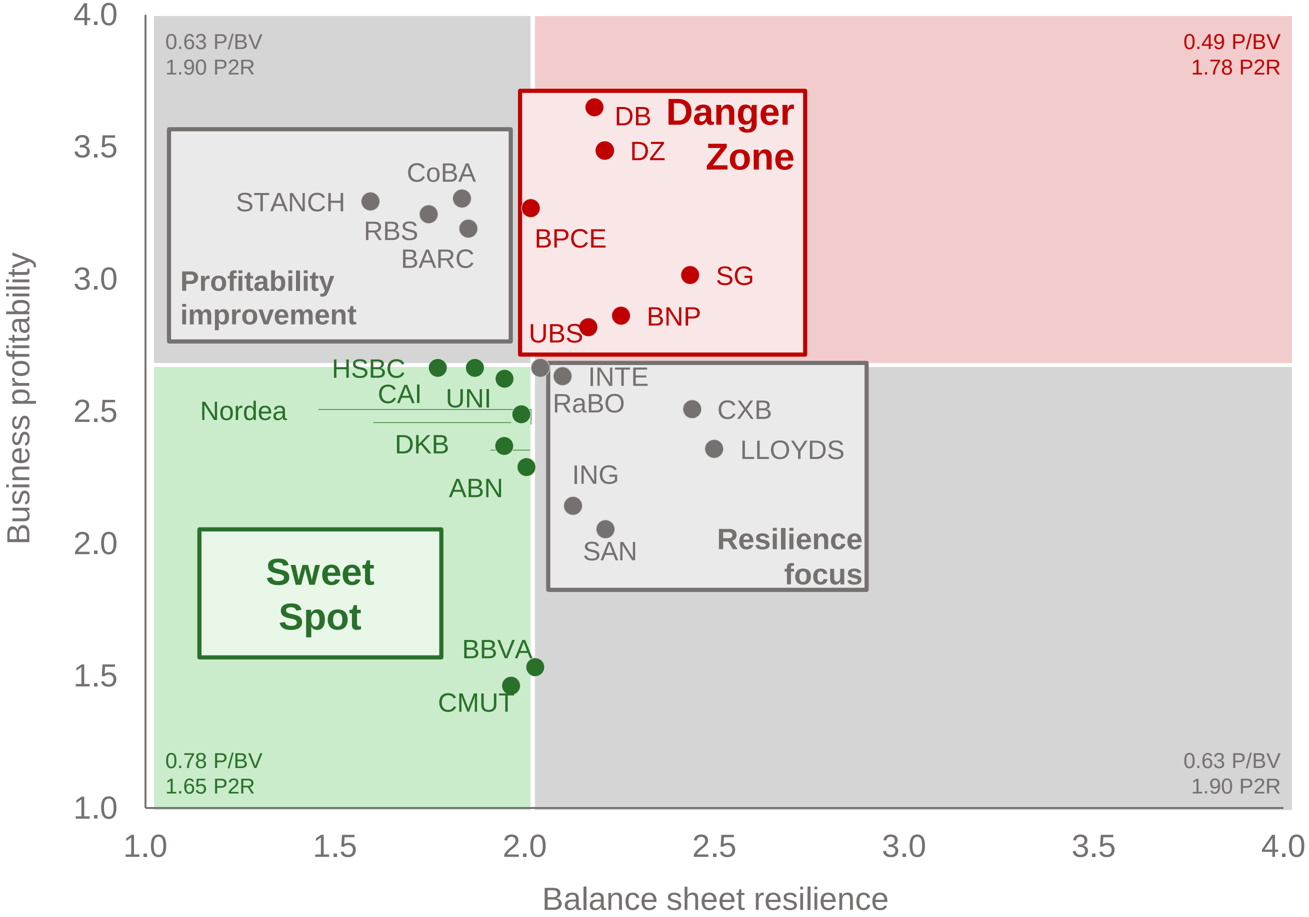
Spanish banks are outperforming in profitability but two of them are still far from their peers in resilience.

Italy and Switzerland

Italian and one Swiss Banks are on a peer average.

5. Profitability and Resilience

A&M's Matrix ranks banks in terms of profitability KPIs and resilience KPIs, showing four clear zones

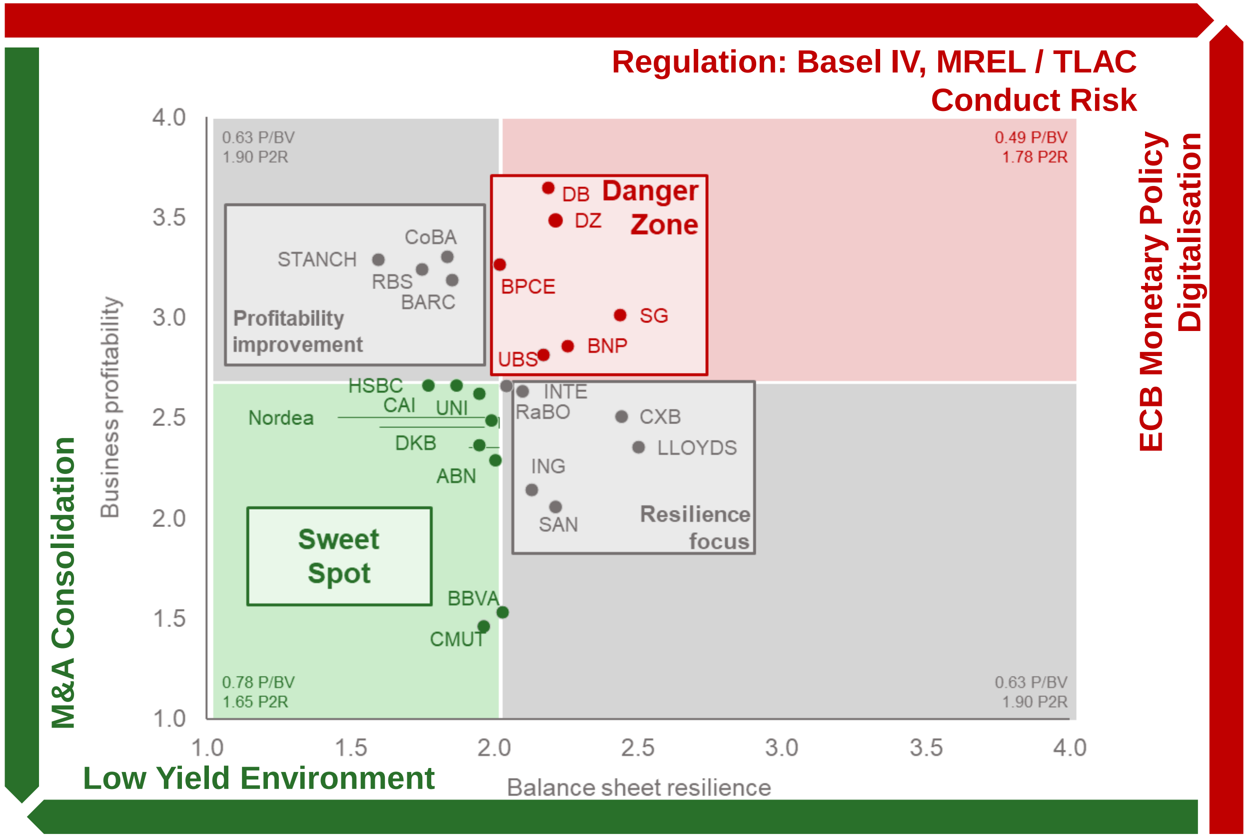


Observations

- The green area defines where banks are achieving above-average profitability and resilience indicators. But the sweet spot is still empty, given that no bank has reached outstanding profitability and resilience and therefore has not yet generated notable economic value.
- The red area includes banks with above-average profitability and resilience; therefore decisions need to be made.
- Banks in grey areas have delivered above-average either on profitability or resilience. They need to focus their efforts on demonstrating that they can be outstanding at both of them at the same time.

5. Profitability and Resilience: Future Trends

A more dynamic view shows the Industry trends that lie ahead and set the playing field for the coming years.



Observations

Profitability

- Merger and acquisition (M&A) consolidation moves will be a tailwind to generate opportunities to reduce costs and refocus or divest non-core business.
- Conversely, ECB monetary policy and Digitalisation is eroding the revenue pools of banks that cannot adapt quickly to a low-cost environment.

Resilience

- Capital regulation and new fast-moving risks like conduct mean a need for stronger capital requirements or outstanding risk mitigation techniques.
- Low yields due to ECB monetary policy can help access to the markets given the amount of capital waiting on the side-lines for good investment opportunities.

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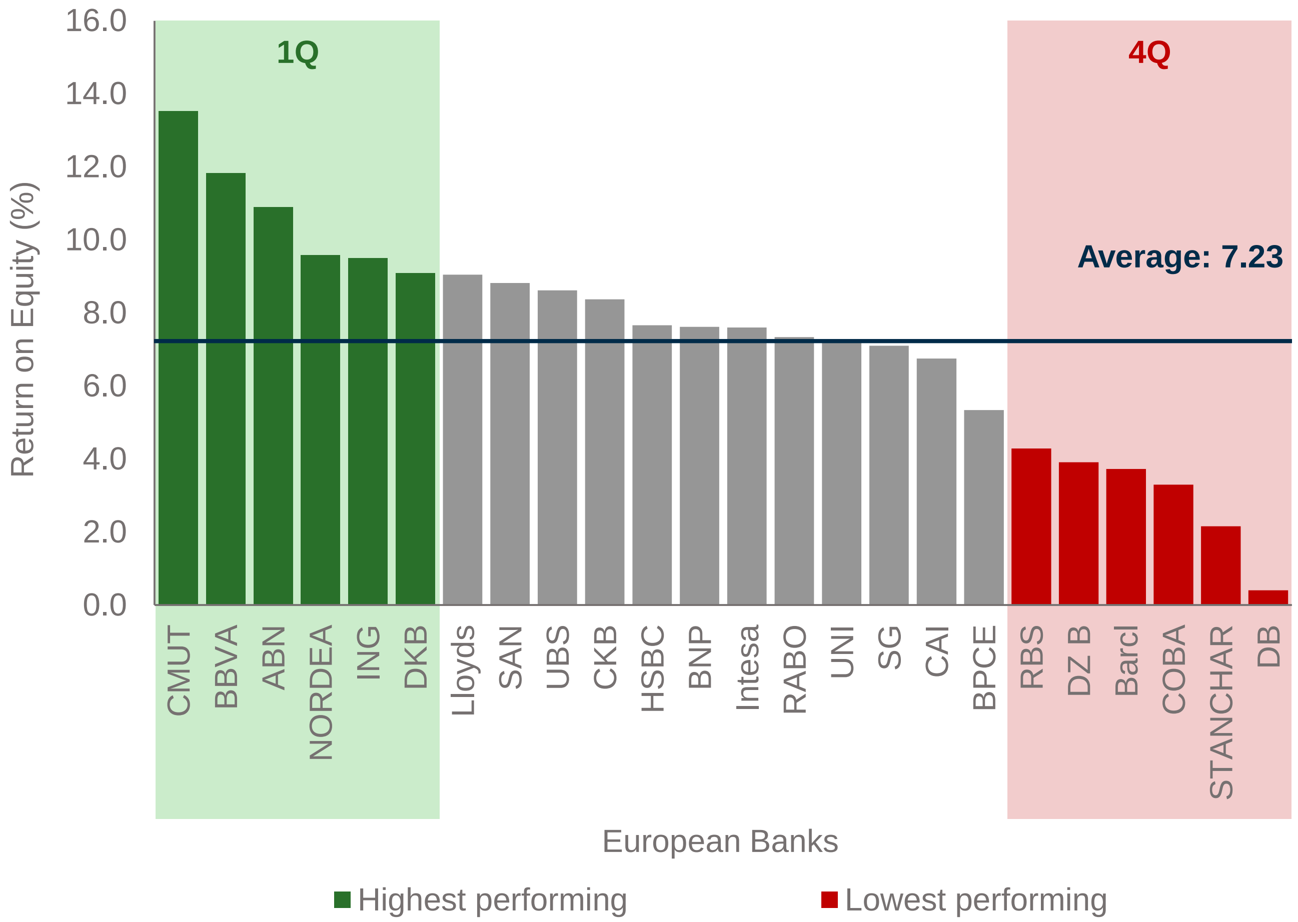
5. Profitability: Return on Equity

RoE

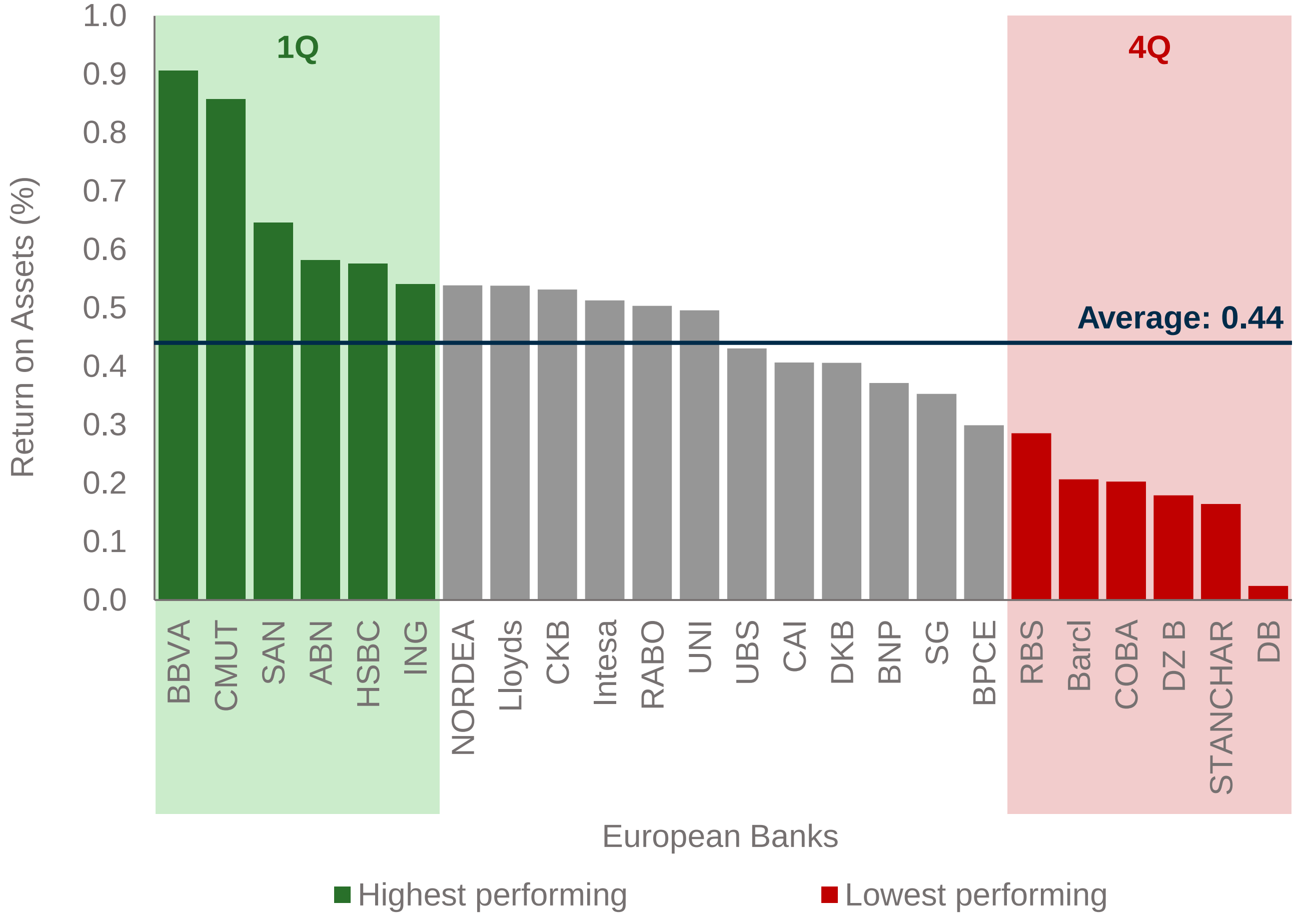


Observations

- The average Return on Equity (ROE) is below 8%, under the cost of capital that sits above 10%.
- Only three banks have delivered over 10% ROE, and six banks have delivered below 6%.
- ROE is the primary indicator of profitability and banks should be able to understand and drill down their individual drivers contributing to low profitability in order to start increasing the ratio.
- CMUT and BBVA have the best ratios and STANCHAR and DB the worst.

5. Profitability: Return on Assets

ROA

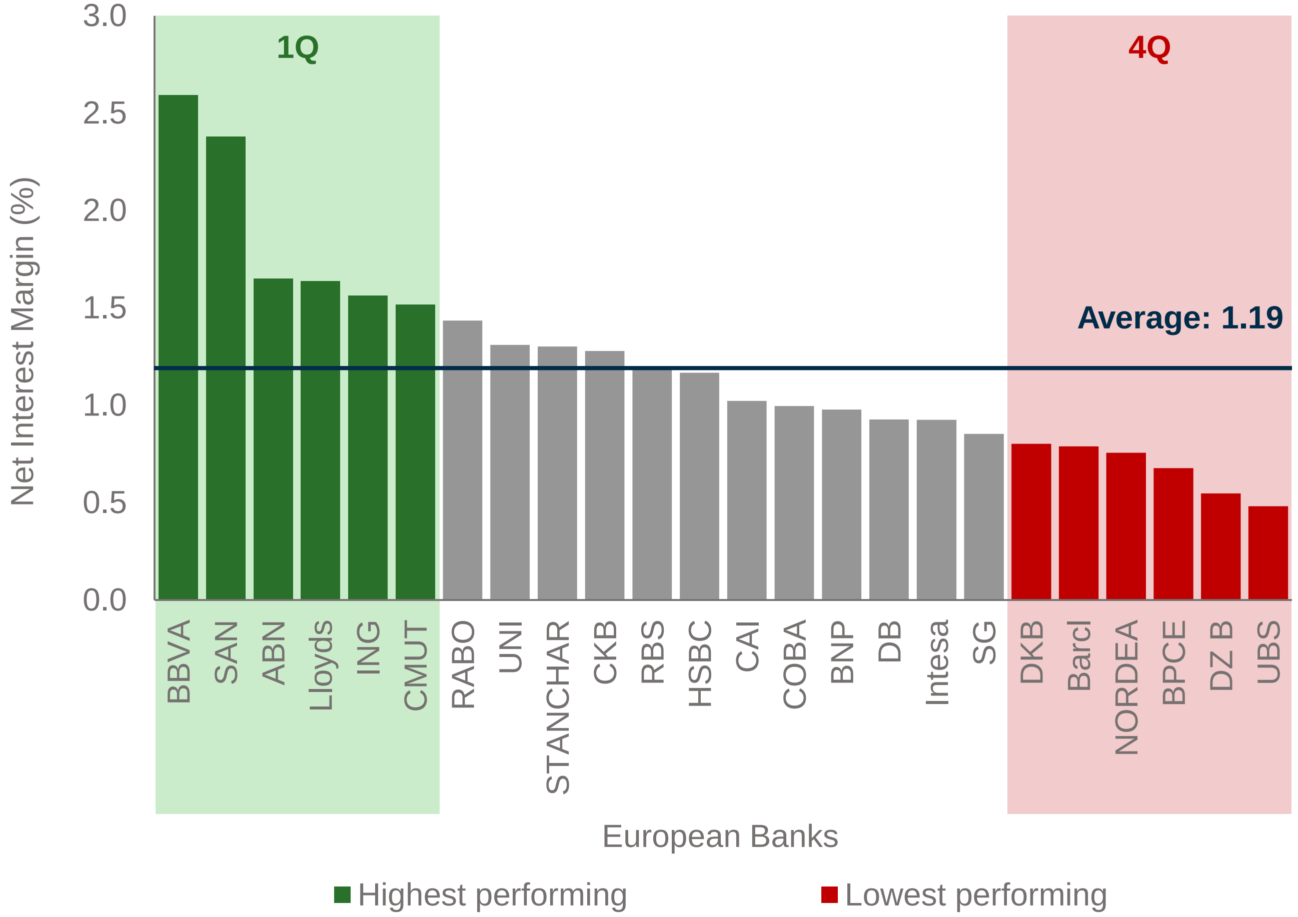


Observations

- Return on Assets (ROA) is on average 0.44 with only two banks over 0.80 and eight banks below 0.30.
- ROA is an old school ratio but has some positive qualities like measuring leverage and returns in a risk level playing-field and can complement other profitability indicators.
- BBVA and CMUT have the best ratios and STANCHAR and DB the worst.

5. Profitability: Net Interest Margin

NIM (%)

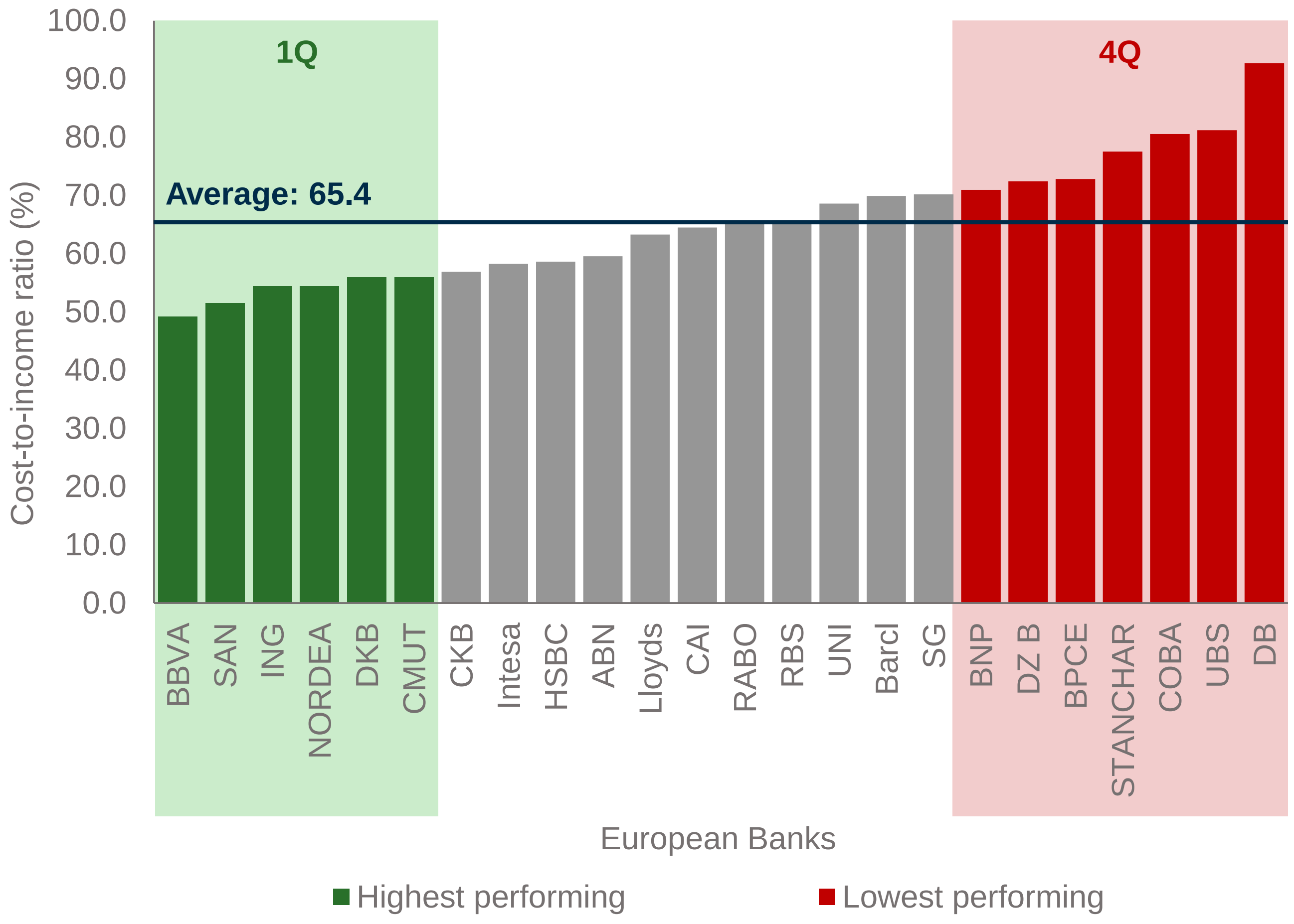


Observations

- Net Interest Margin (NIM) is on average at 1.19 Banks exposed to more high yield economies like Latam or U.K. have a clear head start. European only banks are struggling to beat 1.00%.
- NIM improvement should be back on the priority list given that it is the key revenue pool for all banks. Pricing of new loans has to beat the back-book to start improving the ratio until changes in ECB policy can step in at some point.
- BBVA and SAN have the best ratios and UBS and DZ the worst.

5. Profitability: Cost-to-Income Ratio

Cost to Income

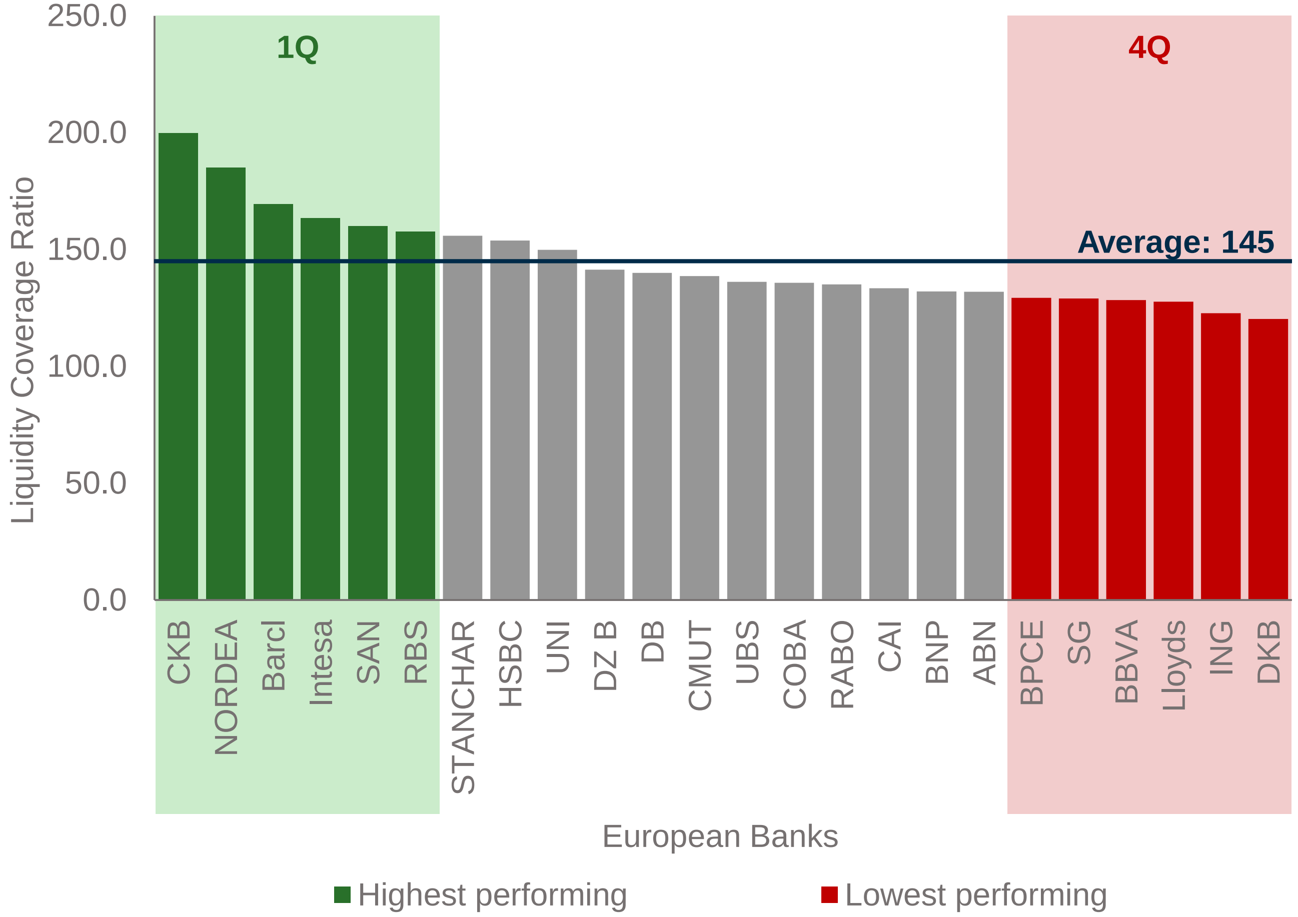


Observations

- Average Cost-to-Income is 65.7 with only one bank below 50.0
- Recurrent revenue enhancement strategies need to help improve the Income side of the ratio, but it can take many quarters to see relevant changes in the revenue pool.
- Acting on costs is not an alternative, but a need given the low interest environment and the legacy of some business and distribution models. As capital allocation played an important role in driving more capital requirements, cost allocation has to be rethought to measure digital and non-digital transformation.
- BBVA and SAN have the best ratios and UBS and DB the worst

5. Balance Sheet Resilience: Liquidity Coverage Ratio

LCR

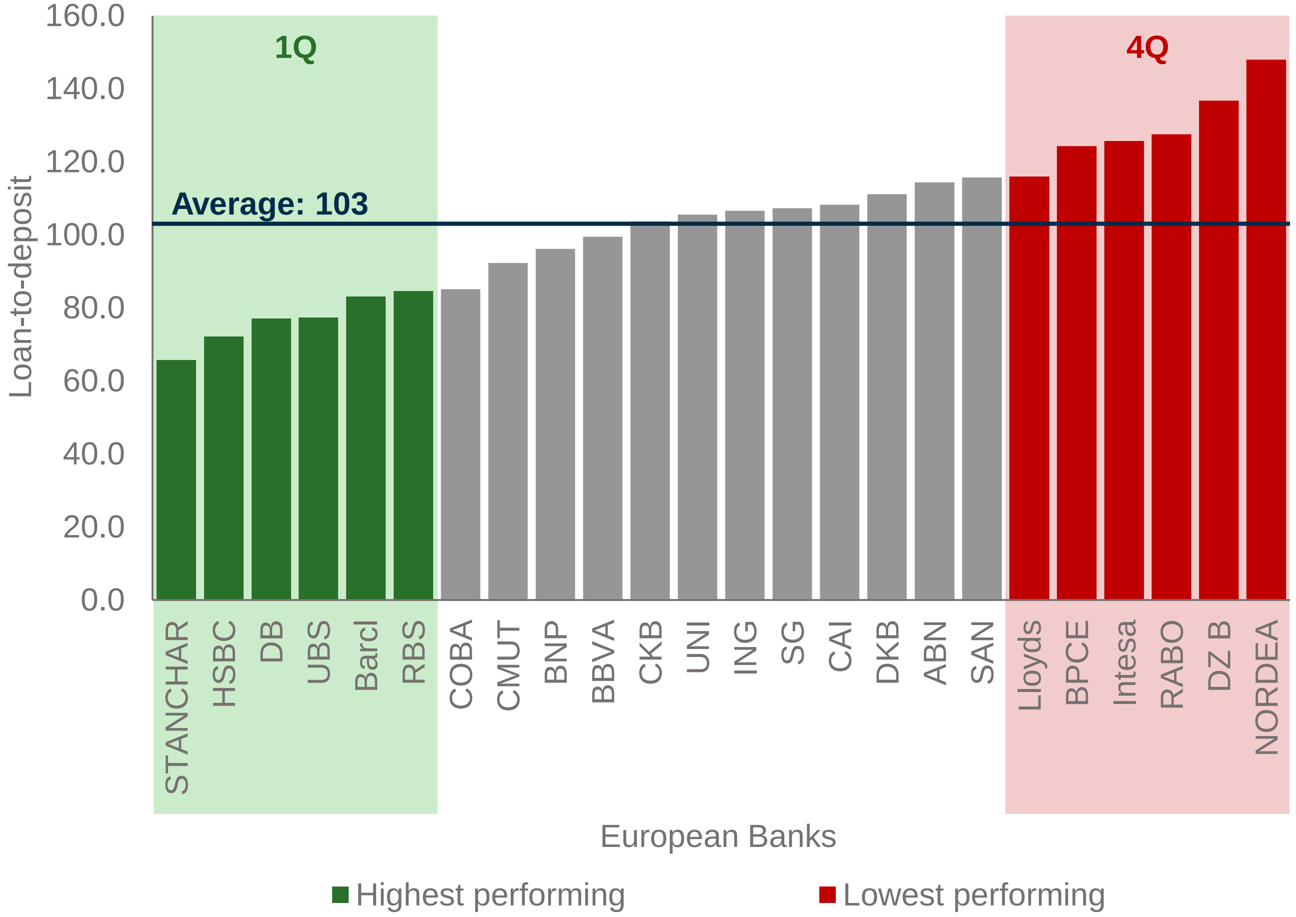


Observations

- Liquidity Coverage Ratio (LCR) has become the ratio for measuring liquidity risk, averaging 145.
- It is true that excess liquidity can mean more resilience, but can also hurt profitability because of a lack of optimisation of funding in a negative interest rate environment.
- Recent Stress Testing of Liquidity (LIST) by the ECB signals that the banks must not forget that the excess liquidity of the ECB Policy is temporary.
- CaixaBank (CKB) and Nordea have the highest ratios, DKB,and DKB have the lowest.

5. Balance Sheet Resilience: Loan-to-deposit

LTD

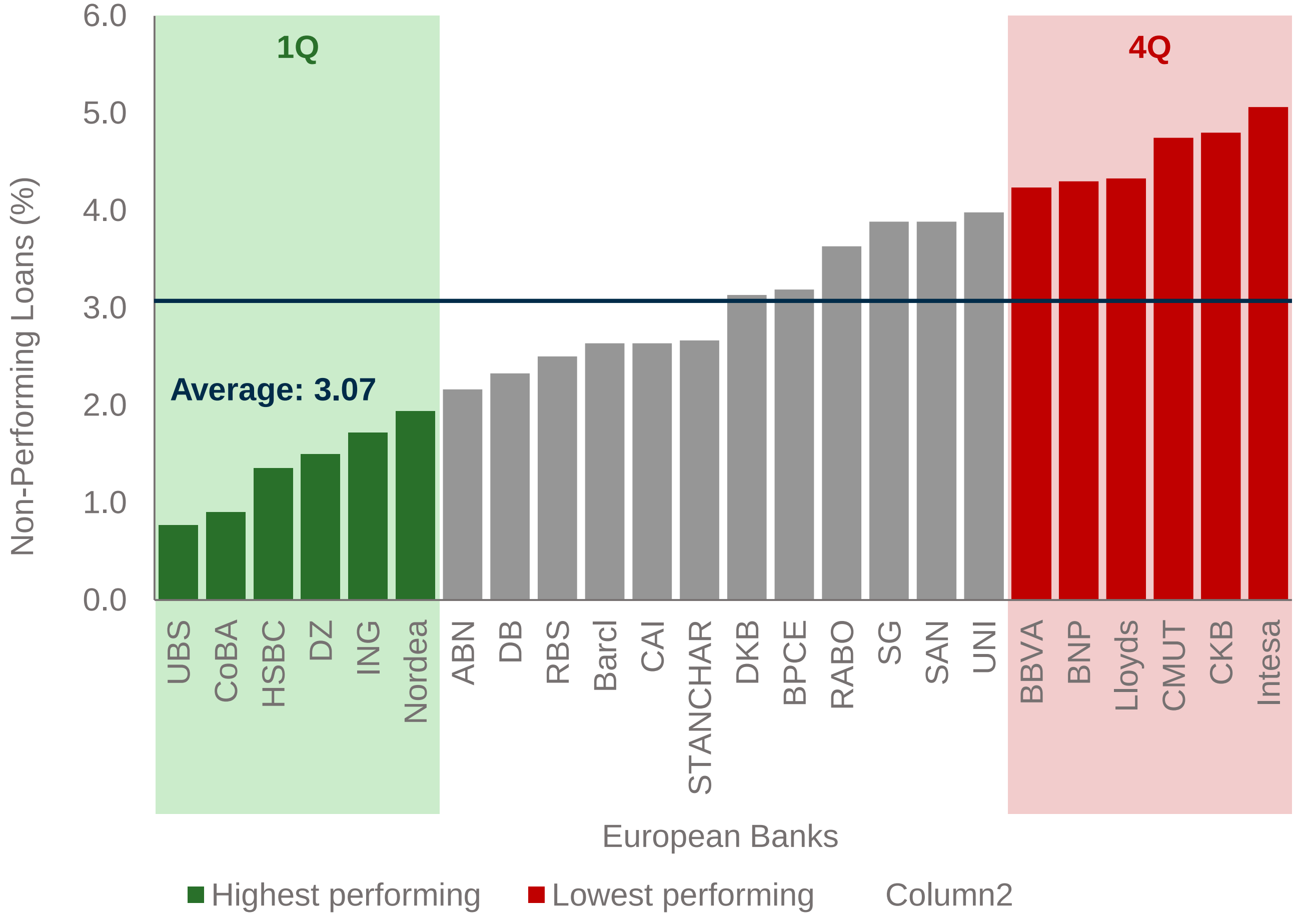


Observations

- Loan-to-Deposit (LTD) is at 103 on average.
- LTD is the perfect complement to LCR to measure the state of liquidity and funding of the industry. No bank is over the 150 danger zone, and 10 Banks are below 100.
- Low LTD means low funding risk, but also can signal underperformance which can hurt profitability in the long run.
- Standard Charter and HSBC have the lowest ratios and DZ Bank and Nordea the highest.

5. Balance Sheet Resilience: Asset Quality

NPL

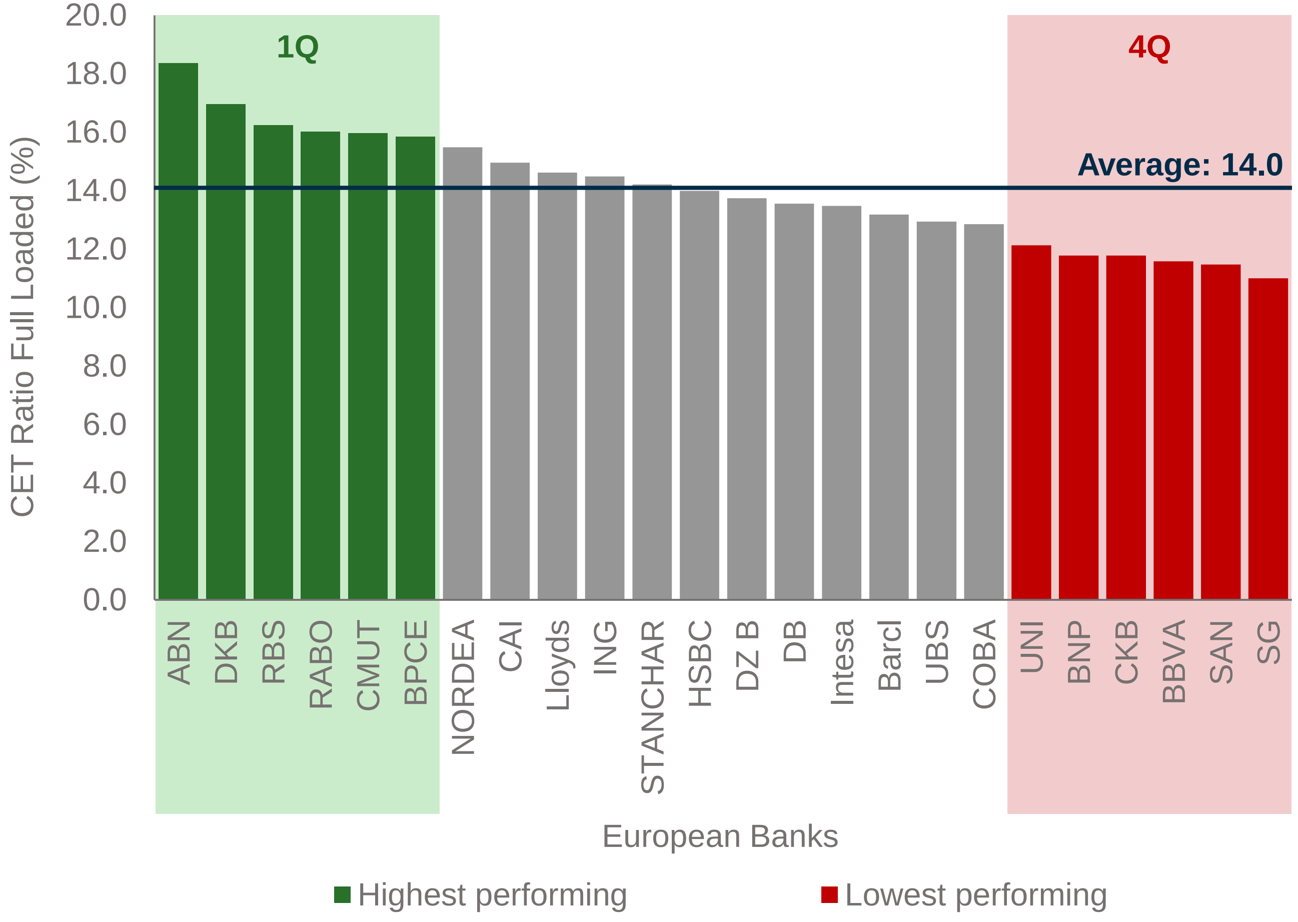


Observations

- Non Performing Ratios (NPL) are on average 3.07 with only one bank over 5%.
- Large banks in many countries have demonstrated their capabilities and drive to the clean up of their balance sheets.
- As the cycle evolves and turns from positive growth to negative growth, having a good starting point in terms of NPLs will be crucial for resilience.
- UBS and Commerzbank have the lowest ratios and CaixaBank and Intesa the highest.

5. Balance Sheet Resilience: Solvency

CET FL



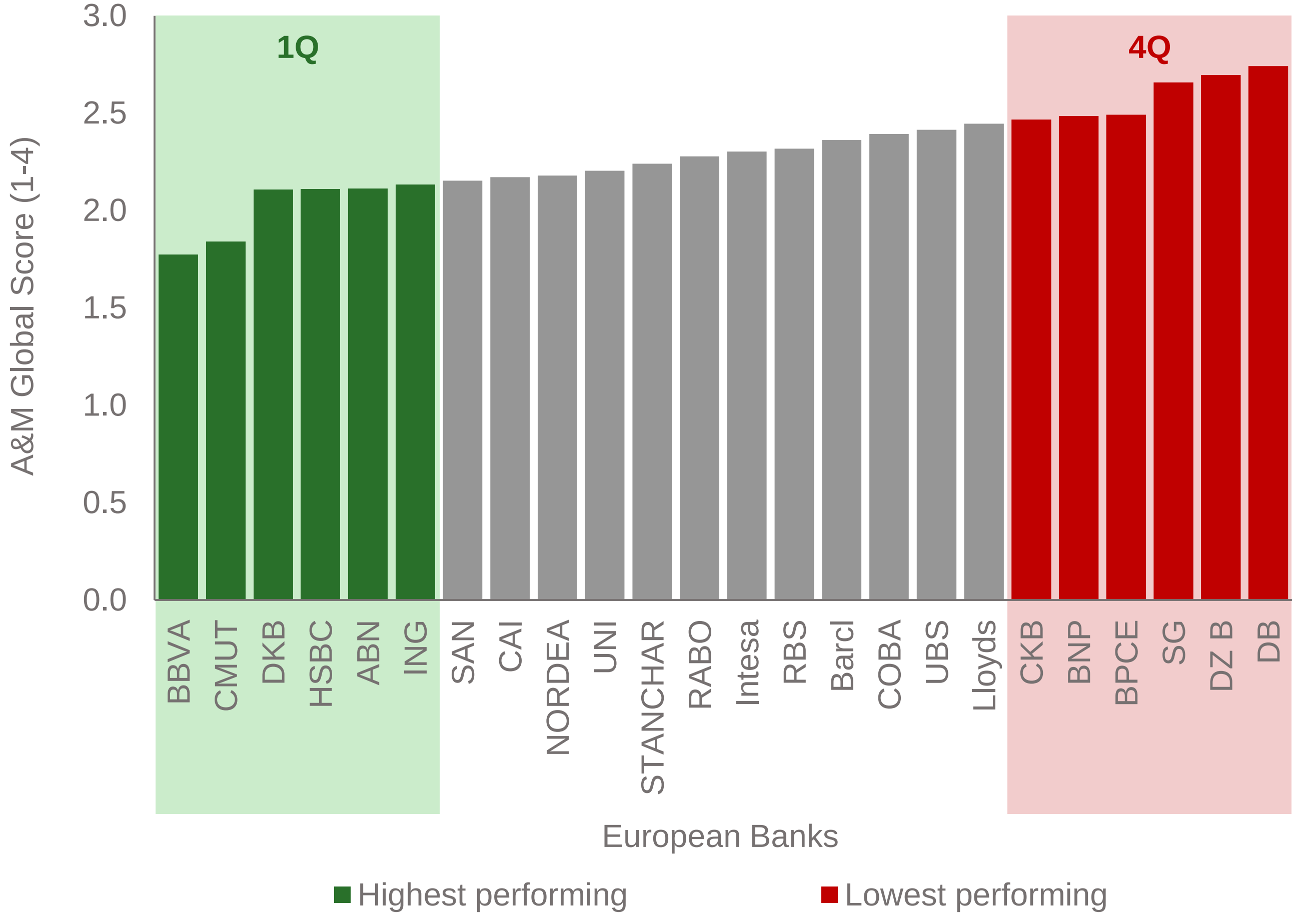
Observations

- Solvency Ratios of CETFL are on average in 14.0.
- Banks are building up solvency levels to anticipate future regulatory changes like BIS IV and MREL.
- Once reached a certain level of CET it will be Internal capital generation capacity the KPIs more observed by the market in order to differentiate between different business models at the same level of resilience.
- ABN and CMUT are the best banks when it comes to CETFL, and Santander and SG the worst.

5. A&M Global Score Ranking

Based on the A&M scoring methodology, which takes into account 13 KPIs across profitability and resilience, below is ranking across the 24 largest banks in Europe.

Global score of the 13 KPIs ranks banks from 1 (best) to 4 (worst)



Highest ranked performers

BBVA, CMUT, DKB, HSBC, ABN, ING rank in the top quartile.

Lowest ranked performers

DB, DZBank, SG, BPCE, BNP, CaixaBank rank among the lower quartile.

6. Score Ranking by Quartiles

	Glob. Score	Profitability			Resilience		
	A&M Score	Revenues	Costs	Returns	Liquidity	A. Quality	Solvency
BBVA	Q1	Q1	Q1	Q1	Q3	Q2	Q2
CMUT	Q1	Q1	Q1	Q1	Q2	Q4	Q1
DKB	Q1	Q4	Q2	Q2	Q4	Q2	Q1
HSBC	Q1	Q3	Q2	Q2	Q1	Q1	Q3
ABN	Q1	Q1	Q1	Q1	Q4	Q4	Q1
ING	Q1	Q3	Q1	Q1	Q4	Q3	Q2
SAN	Q2	Q1	Q1	Q1	Q2	Q2	Q4
CAI	Q2	Q3	Q3	Q3	Q4	Q1	Q2
NORDEA	Q2	Q4	Q2	Q2	Q4	Q3	Q2
UNI	Q2	Q1	Q3	Q3	Q2	Q2	Q2
STANCH	Q2	Q3	Q3	Q3	Q1	Q1	Q2
RABO	Q2	Q3	Q2	Q2	Q4	Q4	Q1
INTESA	Q3	Q3	Q2	Q2	Q3	Q3	Q3
RBS	Q3	Q3	Q3	Q3	Q1	Q4	Q1
BARCL	Q3	Q4	Q3	Q3	Q1	Q1	Q3
COBA	Q3	Q3	Q4	Q4	Q2	Q1	Q3
UBS	Q3	Q1	Q3	Q3	Q2	Q2	Q4
LLOYDS	Q3	Q3	Q2	Q2	Q4	Q4	Q3
CKB	Q4	Q3	Q1	Q1	Q2	Q4	Q4
BNP	Q4	Q4	Q4	Q4	Q3	Q2	Q4
BPCE	Q4	Q3	Q4	Q4	Q4	Q3	Q1
SG	Q4	Q4	Q4	Q4	Q4	Q3	Q4
DZB	Q4	Q4	Q4	Q4	Q4	Q2	Q4
DB	Q4	Q3	Q4	Q4	Q1	Q3	Q4

Highest performing   Lowest performing

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7. Pulse: A&M Scorecard details Top 24 European Banks

		SAN	BBVA	ING	BNP	CAI	UNI	SG	DB	DKB	CXB	ABN	CMUT	INTESA	DZ	STANCH	BCPE	NORDEA	RBS	COBA	UBS	RABO	Barcl	HSBC	LLOYDS
Growth	Loan Growth	4.0%	-0.1%	4.3%	4.7%	5.2%	16.6%	0.4%	2.9%	7.6%	0.9%	-1.5%	4.0%	-1.0%	0.1%	3.9%	6.6%	-0.6%	-0.2%	3.6%	-2.6%	1.2%	4.8%	-0.5%	4.0%
	Deposit Growth	0.4%	3.3%	4.6%	4.7%	7.8%	2.8%	1.5%	0.0%	1.2%	-0.8%	-0.2%	4.6%	1.0%	4.7%	5.9%	-6.9%	-4.3%	-0.1%	2.8%	0.1%	-0.5%	5.5%	-1.9%	0.0%
	Score	2.3	2.7	1.7	1.7	1.2	1.7	2.8	2.7	1.8	3.2	3.3	1.7	3.2	2.3	1.7	2.5	3.5	3.3	2.2	3.2	3.0	1.5	3.3	2.5
Liquidity	LCR	160%	128%	123%	132%	133%	150%	129%	140%	120%	200%	132%	139%	163%	141%	156%	129%	185%	158%	136%	136%	135%	169%	154%	128%
	Loan-to-Deposit Ratio (LDR)	116%	99%	107%	96%	108%	106%	107%	77%	111%	104%	114%	92%	126%	137%	66%	124%	148%	85%	85%	77%	128%	83%	72%	116%
	Score	1.5	1.7	2.0	1.7	1.8	1.5	1.8	1.2	2.0	1.5	1.8	1.5	1.7	1.8	1.0	2.0	1.8	1.2	1.3	1.3	1.8	1.2	1.0	1.8
Income & Operating Efficiency	Net Interest Margin (NIM)	2.4%	2.6%	1.6%	1.0%	1.0%	1.3%	0.9%	0.9%	0.8%	1.3%	1.6%	1.5%	0.9%	0.5%	1.3%	0.7%	0.8%	1.2%	1.0%	0.5%	1.4%	0.8%	1.2%	1.6%
	Operating Income / Assets	3.2%	3.3%	1.9%	1.4%	1.6%	2.1%	1.3%	1.8%	1.1%	2.0%	2.1%	2.1%	1.9%	0.9%	1.8%	1.4%	1.3%	1.5%	1.6%	2.2%	1.8%	1.4%	1.7%	1.8%
	Cost-to-Income Ratio (C/I)	51.5%	49.2%	54.3%	70.9%	64.5%	68.6%	70.2%	92.7%	55.9%	56.8%	59.5%	55.9%	58.2%	72.4%	77.5%	72.8%	54.4%	65.7%	80.6%	81.2%	65.2%	69.9%	58.6%	63.3%
	Score	1.8	1.6	2.4	3.7	3.2	3.1	3.7	3.5	2.8	2.7	2.5	2.4	2.8	3.8	3.4	3.7	2.8	3.2	3.6	3.5	3.0	3.5	2.8	2.8
Risk	NPL ratio	3.9%	4.2%	1.7%	4.3%	2.6%	4.0%	3.9%	2.3%	3.1%	4.8%	2.2%	4.7%	5.1%	1.5%	2.7%	3.2%	1.9%	2.5%	0.9%	0.8%	3.6%	2.6%	1.3%	4.3%
	Coverage Ratio	68%	75%	44%	71%	84%	122%	64%	45%	67%	53%	38%	49%	102%	50%	70%	59%	44%	44%	55%	35%	23%	80%	65%	15%
	Score	1.8	1.7	1.9	1.7	1.4	1.7	1.9	2.0	1.8	2.3	2.3	2.5	1.9	1.7	1.4	2.0	1.9	2.1	1.4	1.8	2.6	1.4	1.5	2.7
Profitability	Return on Equity (RoE)	8.8%	11.8%	9.5%	7.6%	6.8%	7.2%	7.1%	0.4%	9.1%	8.4%	10.9%	13.5%	7.6%	3.9%	2.2%	5.3%	9.6%	4.3%	3.3%	8.6%	7.3%	3.7%	7.7%	9.0%
	Return on Assets (RoA)	0.6%	0.9%	0.5%	0.4%	0.4%	0.5%	0.4%	0.0%	0.4%	0.5%	0.6%	0.9%	0.5%	0.2%	0.2%	0.3%	0.5%	0.3%	0.2%	0.4%	0.5%	0.2%	0.6%	0.5%
	Score	2.2	1.2	2.2	2.8	2.8	2.7	2.8	4.0	2.3	2.3	2.0	1.2	2.5	3.7	3.7	3.3	2.2	3.3	3.5	2.5	2.5	3.5	2.5	2.2
Capital	CET1 Ratio f.l.	11.5%	11.6%	14.5%	11.8%	15.0%	12.1%	11.0%	13.6%	17.0%	11.8%	18.4%	16.0%	13.5%	13.7%	14.2%	15.8%	15.5%	16.2%	12.9%	12.9%	16.0%	13.2%	14.0%	14.6%
	Leverage ratio	5.0%	6.4%	5.3%	4.3%	4.7%	5.7%	3.2%	3.5%	3.8%	4.6%	5.2%	5.5%	5.0%	3.6%	5.8%	5.1%	4.8%	5.5%	5.6%	4.1%	5.7%	4.5%	5.2%	3.9%
	Score	3.1	2.5	2.4	3.3	2.3	2.5	3.4	3.0	2.1	3.1	1.8	1.9	2.6	3.0	2.1	2.0	2.1	1.7	2.7	3.1	1.5	2.7	2.6	2.7
SCORE	Score	**2.15**	**1.77**	**2.13**	**2.49**	**2.17**	**2.20**	**2.66**	**2.74**	**2.11**	**2.47**	**2.11**	**1.84**	**2.30**	**2.70**	**2.24**	**2.49**	**2.18**	**2.32**	**2.39**	**2.42**	**2.28**	**2.36**	**2.11**	**2.45**

Best Performers   Worst Performers

8. How A&M can help

Why choose A&M?

1. Uniquely qualified

A&M's senior leaders, many of whom are former senior regulators and financial industry professionals, bring practical approaches that work, versus theoretical approaches that don't in a quick and pragmatic manner.

Global team of more than 200 professionals dedicated to the financial services industry led by 30 Managing Directors located in nine countries.

2. Objective and independent

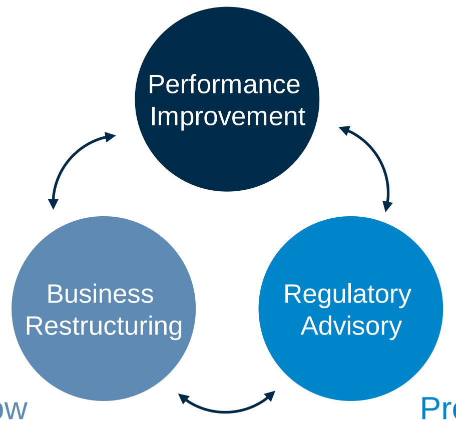
Independently owned which keeps us free from audit conflict, creates independence and provides flexibility on fee arrangements.

3. Comprehensive solutions

A&M's Financial Industry Advisory services team can draw on world-class expertise from across the wider business – over 3,500 people across 4 continents across the firm – providing a 'one-stop' solution for our clients. Practice groups include Restructuring, Tax, Performance Improvement, Valuation, Transaction Advisory and Disputes and Investigations.

Our Financial Industry Advisory Services

Resilient banks
with strong balance sheets that need rebuilding sustainable returns and delivering value to investors



Advising on how to strengthen balance sheets, recapitalize, restructure and deleverage on unprofitable Assets and Businesses

Profitable Banks that need to build up more robust, viable business models serve markets and customers and regain resilience

9. Glossary

	Metric	Abbreviation	Definition
Size	Loans and Advances Growth		YoY growth in EOP gross customer loans
	Deposits Growth		YoY growth in EOP customer deposits
Liquidity	Loan-to-Deposit Ratio	LDR	(EOP gross customer loans / EOP customer deposits)
	Liquidity Coverage Ratio	LCR	Regulatory adjusted Liquid Assets / Outflows
Income and Operating Efficiency	Yield on Credit	YoC	(YTD gross interest income / quarterly average gross loans and advances)
	Cost of Funds	CoF	(YTD interest expense) / (quarterly average interest bearing liabilities)
	Net Interest Margin	NIM	(YTD net interest income) / (YTD average net earning assets) Net earnings assets are defined as total assets excluding tangible and intangible assets.
	Fee Income / Assets	F/A	(YTD operating income / YTD average total assets)
	Operating Revenue / Assets	OI	NIM+F/A
	Cost-to-Income Ratio	C/I	(YTD operating expenses / YTD operating income)
Risk	Non-performing loans ratio	NPL	(Non-performing loans / gross customer loans)
	Coverage Ratio		(Loan loss reserves / non-performing loans)
	Cost of Risk	CoR	(YTD provision for loan losses / YTD gross loans and advances)
Profitability	Return on Equity	RoE	(YTD net income attributable to Parent) / (YTD total equity)
	Return on Assets	RoA	(YTD net income / YTD average assets)
	Risk Adjusted Return on Capital	RARoC	(YTD net income / YTD average CET1)
Capital	CET1 Ratio fully loaded	CET1 FL	(EOP CET1 fully loaded) / (EOP risk-weighted assets)
	Leverage Ratio	LR	Tier1/Total Net Assets

Note: EOP stands for end of period.

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