

European Banking Barometer

Weaker confidence and continued internal focus makes for a poor 2013 outlook

Autumn / Winter 2012

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Introduction

Ernst & Young's European Banking Barometer is a bi-annual study to determine the views of senior bankers across the major banking markets in Europe. The research focuses on the current macro-economic environment and how it will impact their organization and the banking industry as a whole over the next six months.

The Autumn / Winter 2012 Barometer consists of 269 interviews with senior bankers across 11 markets in Europe – Austria, Belgium, France, Germany, Italy, the Netherlands, the Nordics, Poland, Spain, Switzerland and the UK.

The fieldwork, consisting of telephone interviews and online questionnaires, was conducted throughout Autumn 2012 by two external research agencies on Ernst & Young's behalf. The aim was to interview senior bankers at a range of institutions representing at least 50% of the market, defined as assets owned.

Interviews were not conducted with subsidiaries of member / group banks, and a range of bank types were interviewed in each market to ensure a fair reflection of the industry in each country.

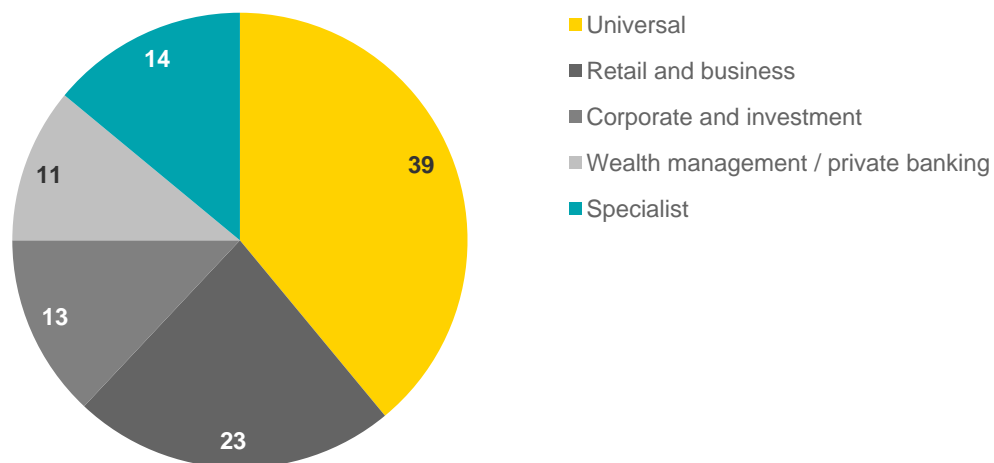
The results are presented in an aggregate format and shown in percentages. Please note that where charts do not add up to 100%, it is because participants either chose not to answer the question or selected 'Don't know' or 'Not applicable' as their answer. Where possible we've compared answers against those given in Spring 2012 but some questions have changed or are new.

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

If you would like to take part in our next European Banking Barometer, please speak to your usual Ernst & Young contact or refer to your local-country contact on pages 50-51 of this booklet.

Composition of the survey sample

Type of bank



* Numbers are percentage of respondents answering.

Specialist bank definition – consumer credit, savings and institutions which don't offer a current account.

Please note that the percentages shown above represent the approximate aggregate distribution of assets for banks interviewed in the following markets: Belgium, France, Italy, the Netherlands, Spain, UK.

Due to data protection laws we are unable to identify which banks have participated in the survey in Austria, Germany, the Nordics, Poland and Switzerland. Consequently we cannot attribute assets to the banks interviewed in those markets.

Composition of the survey sample by bank type

| Country | Total | Universal | Corporate and investment | Private bank / wealth management | Specialist | Retail and business (cooperative) | Retail and business (state owned) | Retail and business (privately owned) |
|-------------|-------|-----------|--------------------------|----------------------------------|------------|-----------------------------------|-----------------------------------|---------------------------------------|
| Europe | 269 | 104 | 35 | 29 | 39 | 18 | 11 | 32 |
| Austria | 10 | 7 | 1 | | | | | 2 |
| Belgium | 6 | 3 | | 1 | 2 | | | |
| France | 27 | 8 | 7 | 5 | 3 | | 1 | 3 |
| Germany | 50 | 29 | 3 | | 10 | 3 | 4 | |
| Italy | 39 | 16 | 4 | 2 | 5 | 4 | | 8 |
| Netherlands | 20 | 2 | 4 | 2 | 5 | 2 | | 5 |
| Nordics | 23 | 6 | 2 | 1 | 2 | 4 | | 8 |
| Poland | 18 | 8 | 3 | | 1 | 3 | 2 | 1 |
| Spain | 27 | 7 | 6 | 5 | 6 | | 1 | 2 |
| Switzerland | 27 | 12 | 1 | 8 | 2 | 1 | 2 | 1 |
| UK | 22 | 6 | 4 | 6 | 2 | 1 | 1 | 2 |

Please note that one German retail and business bank is unclassified and is excluded from the numbers above.

European overview

Further cost cutting measures, restricted lending and consolidation pressures will define an even more cautious banking industry in the next six months.

Cost cutting to bite in first half of 2013 with more job losses as crisis refuses to fade

- ▶ Cost cutting is now second only to compulsory regulation and the risk management agenda in European banks' priority list.
- ▶ Cutting costs, streamlining processes and minimizing non-essential spend are all now in the top five priorities of banks for the next six months.
- ▶ Forty-five percent of European banks expect headcount to decrease in the next six months as they struggle to control costs in the low-growth environment.
- ▶ Banks in the Netherlands and the UK will be worst affected with 70% and 64% of banks respectively expecting to decrease their headcount.
- ▶ Banks in the Nordics are more optimistic but even in this region 22% are expecting to reduce headcount.
- ▶ Most cuts will be in head office functions with 58% of banks expecting cuts in this area.
- ▶ The biggest cuts are expected from the universal and corporate / investment banking sectors, where over half of respondents expect to make headcount reductions.

Growing concerns about the European economy and sovereign debt crisis dominate the industry

- ▶ There are rising concerns about the impact of the Eurozone debt crisis in the next six months.
- ▶ Banks in Spain, France, Switzerland and Italy are most worried.
- ▶ Banks in the Netherlands and Belgium are the least worried.
- ▶ Macro-economic worries continue to dominate the European banking industry with banks split on whether their economy will remain the same (40%) or worsen (42%).
- ▶ The outlook is worse now than when we launched the Spring 2012 edition of the European Banking Barometer.

European overview

Actions in 2013 will result in fewer banks, many of them much smaller, as they struggle with current business models and the capital intensive environment

- ▶ The industry will be reshaped through consolidation, asset sales and joint ventures, with 47% of banks expecting to see significant consolidation happening in their markets within the next three years.
- ▶ Almost all Swiss respondents and 78% of Spanish respondents anticipate consolidation, but just 1 in 10 in the UK, and none in Belgium do.
- ▶ Industry consolidation is most anticipated in wealth management and private banking. Specialist banks are least likely to see consolidation.
- ▶ Some 30% of banks surveyed intend to sell assets in the next six months, with Spanish and UK banks likely to be the most active.
- ▶ Twenty-nine percent of European banks are also likely to consider joint ventures and partnerships going forward.

Banks are placing renewed emphasis on increasing cash reserves and deleveraging

- ▶ Pressure to build capital buffers means that banks are pushing to increase the size of their cash reserves through a mix of actions.
- ▶ Fifty-six percent plan to introduce more incentives to boost customer deposits, heightening the war for deposits in some markets.
- ▶ Fifty-three percent are aiming to reduce the size of their balance sheet.
- ▶ Forty-four percent are intent on reducing their loan-to-deposit ratios.

Credit remains tight across Europe and banks are increasingly nervous about the impact of non-performing loans on their books, which is having a knock-on effect on their lending policies

- ▶ Eighty-five percent of banks expect provisions to remain at their current level or increase in the short-term.
- ▶ Worst hit are Poland, Spain and Italy where 67%, 56% and 54% of respondents respectively expect to increase provisions.
- ▶ Best performing are the Nordics where only 23% expect an increase in provisions, closely followed by 30% in Austria and 32% in the UK.
- ▶ Consumer lending policies are expected to become increasingly restrictive, with 34% of banks expecting a decrease in lending.
- ▶ On the business side, lending to construction, commercial real estate and transport will remain very constrained, with only healthcare and IT seeing some relaxation.

Economic environment

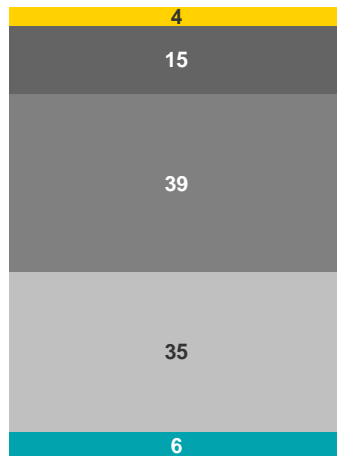


Almost half of European banks expect economic conditions to deteriorate further

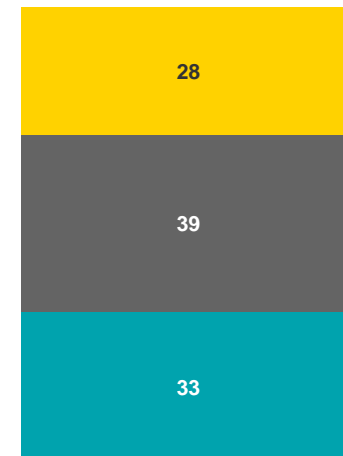
How do you expect the general economic outlook in your country to change over the next six months?*

Autumn 2012

Spring 2012



■ Worsen significantly ■ Worsen slightly ■ Remain the same
■ Improve slightly ■ Improve significantly



■ Worsen ■ Remain the same ■ Improve

Comments: Concerns over the on-going sovereign debt crisis and the implications of continued austerity programs meant few banks saw much hope of economic recovery in the near term. A boost to GDP from hosting the Olympics may have served as a stimulus to UK institutions. British banks had the most profitable outlook with 41% of respondents expecting the economy to improve.

* Numbers are percentage of respondents answering.

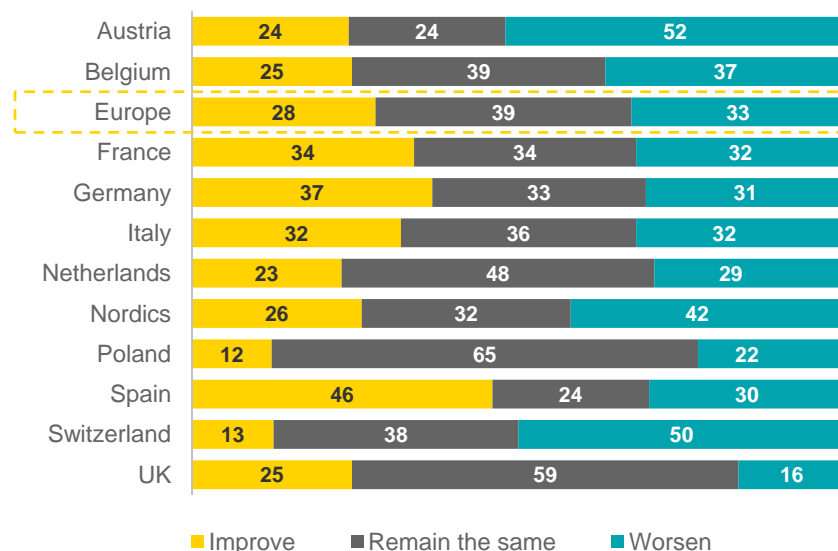
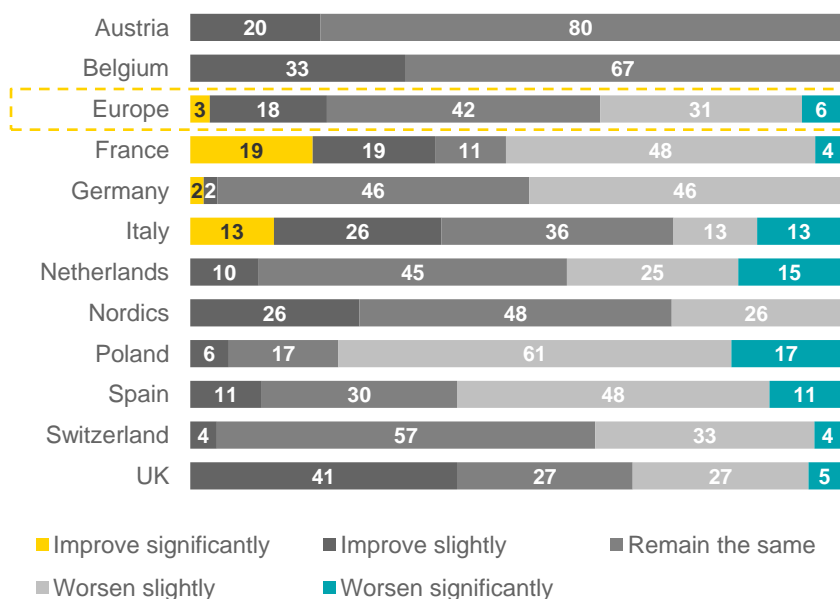
Autumn 2012 responses are based on a five-point scale and spring 2012 responses are based on a three-point scale.

The UK, Italy and France and are the most optimistic on economic prospects

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

Autumn 2012

Spring 2012



* Numbers are percentage of respondents answering.

Autumn 2012 responses are based on a five-point scale and spring 2012 responses are based on a three-point scale.

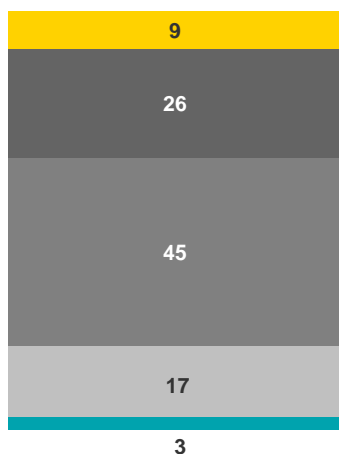
European debt crisis



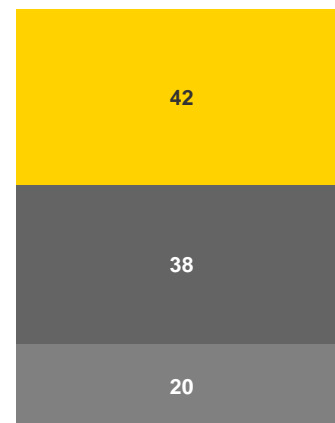
Over a third of respondents expect the impact of the European sovereign debt crisis to increase over the coming months

What level of impact do you think the Eurozone sovereign debt crisis will have on the banking sector in your country over the next six months, in comparison to the previous six months?*

Autumn 2012



Spring 2012



■ Significantly decreased impact
■ About the same
■ Significantly increased impact

■ Slightly decreased impact
■ Slightly increased impact

■ No impact ■ Yes, a minor impact ■ Yes, a substantial impact

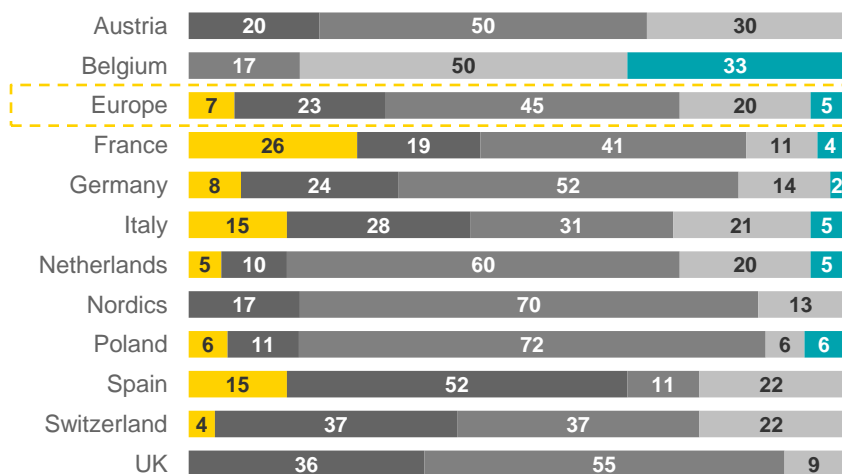
Comments: The sovereign debt crisis has already created turmoil for banks that have had to re-value assets and re-assess capital and liquidity positions. Capital-flight from some countries has also created significant funding gaps. Action by Eurozone countries has so far prevented a default and euro exit, but 35% of respondents still fear the situation will deteriorate.

* Numbers are percentage of respondents answering.

Although there is a slight improvement in sentiment at a European level, there are some notable exceptions

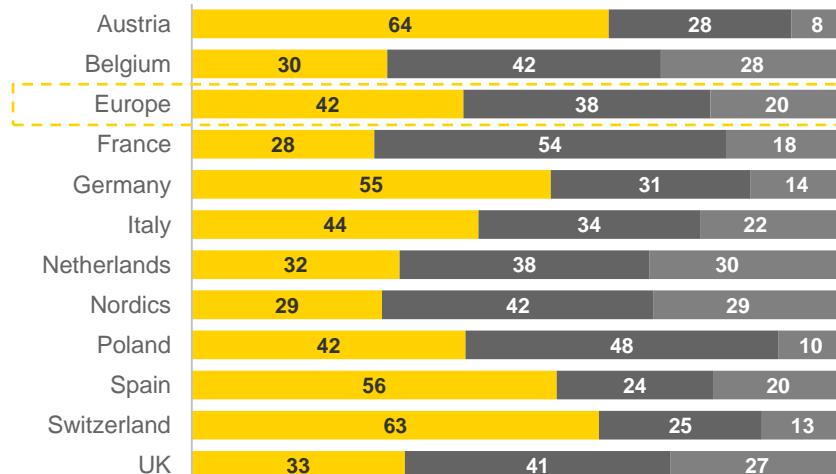
What level of impact do you think the Eurozone sovereign debt crisis will have on the banking sector in your country over the next six months, in comparison to the previous six months?*

Autumn 2012



■ Significantly increased impact
 ■ Slightly increased impact
 ■ About the same
 ■ Slightly decreased impact
 ■ Significantly decreased impact

Spring 2012



■ Yes, a substantial impact ■ Yes, a minor impact ■ No impact

* Numbers are percentage of respondents answering.

Autumn 2012 responses are based on a five-point scale and spring 2012 responses are based on a three-point scale.

Business outlook and focus areas

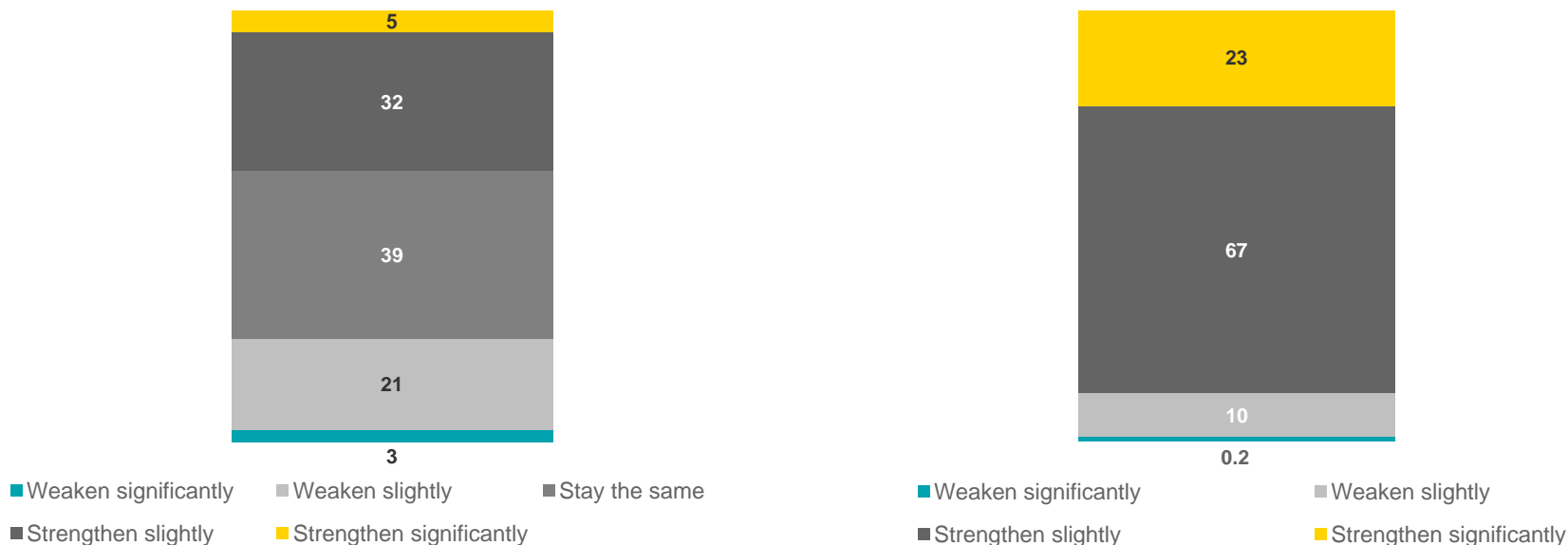


As a result, European banks are more pessimistic about their future performance

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

Autumn 2012

Spring 2012



Comments: More than twice as many respondents are pessimistic about the outlook for their bank compared to Spring 2012. This is driven by expectations that revenues will remain depressed as austerity measures and persisting economic uncertainty continue to suppress demand from corporate and retail customers. Given depressed revenues, stubbornly high costs remain a cause for concern.

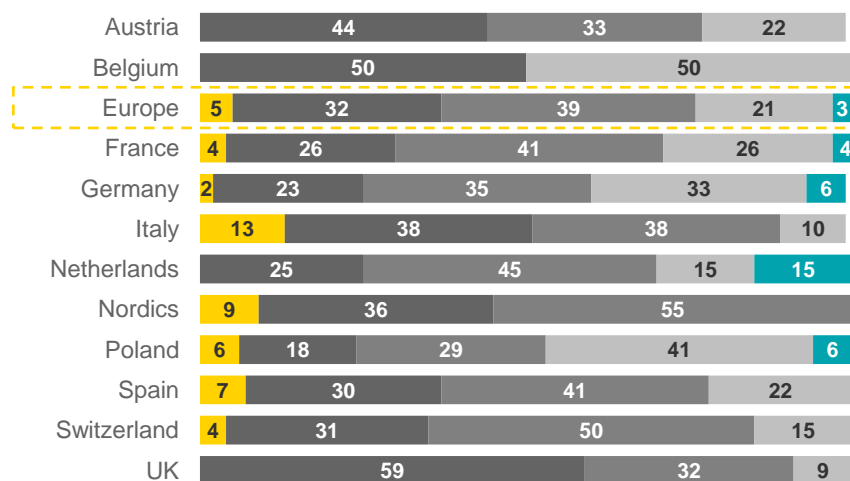
* Numbers are percentage of respondents answering.

Spring 2012 data was based on a four-point scale with no option for 'Stay the same'.

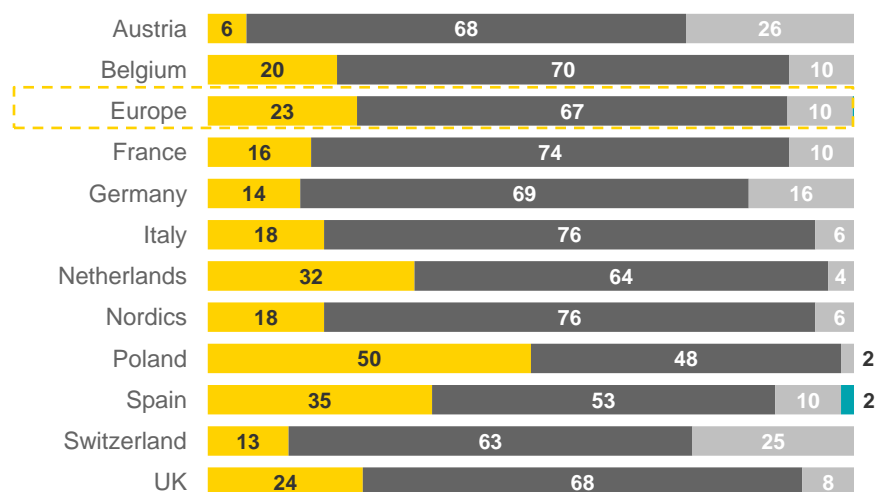
Major changes in sentiment were evident across Europe

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

Autumn 2012



Spring 2012



■ Strengthen significantly
 ■ Strengthen slightly
 ■ Stay the same
■ Weaken slightly
 ■ Weaken significantly

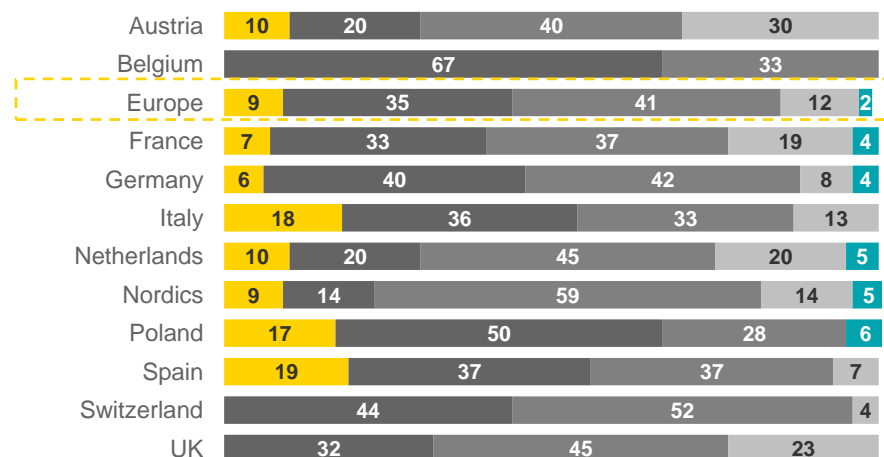
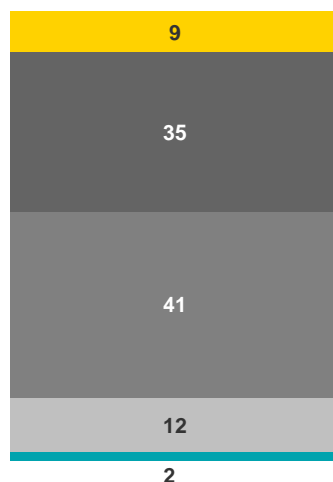
■ Strengthen significantly
 ■ Strengthen slightly
■ Weaken slightly
 ■ Weaken significantly

* Numbers are percentage of respondents answering.
 Spring 2012 data was based on a four-point scale.

Banks are reacting to continued economic uncertainty by increasing loan loss provisions...

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

Autumn 2012



■ Decrease significantly
 ■ Decrease slightly
 ■ Remain at current levels
 ■ Increase slightly
 ■ Increase significantly

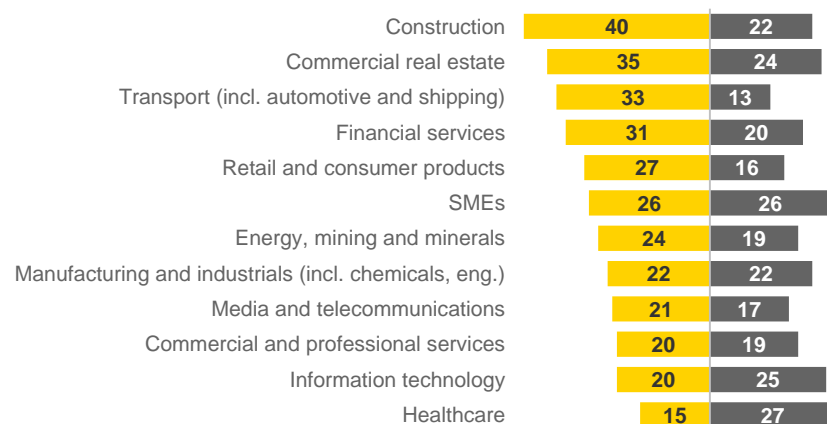
Comments: The economic uncertainty is reflected in 44% of banks expecting loan loss provisions (LLPs) to increase over the next 6 months and a further 41% expecting them to remain at their current (elevated) levels. While LLPs remain high it is unlikely that banks will seek to increase lending significantly, constraining revenue growth and potentially perpetuating the economic malaise.

* Numbers are percentage of respondents answering.

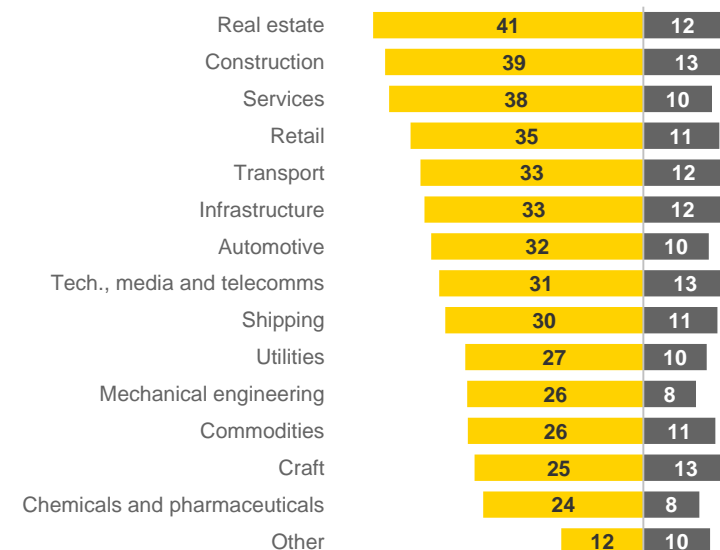
And tightening lending policies

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

Autumn 2012



Spring 2012



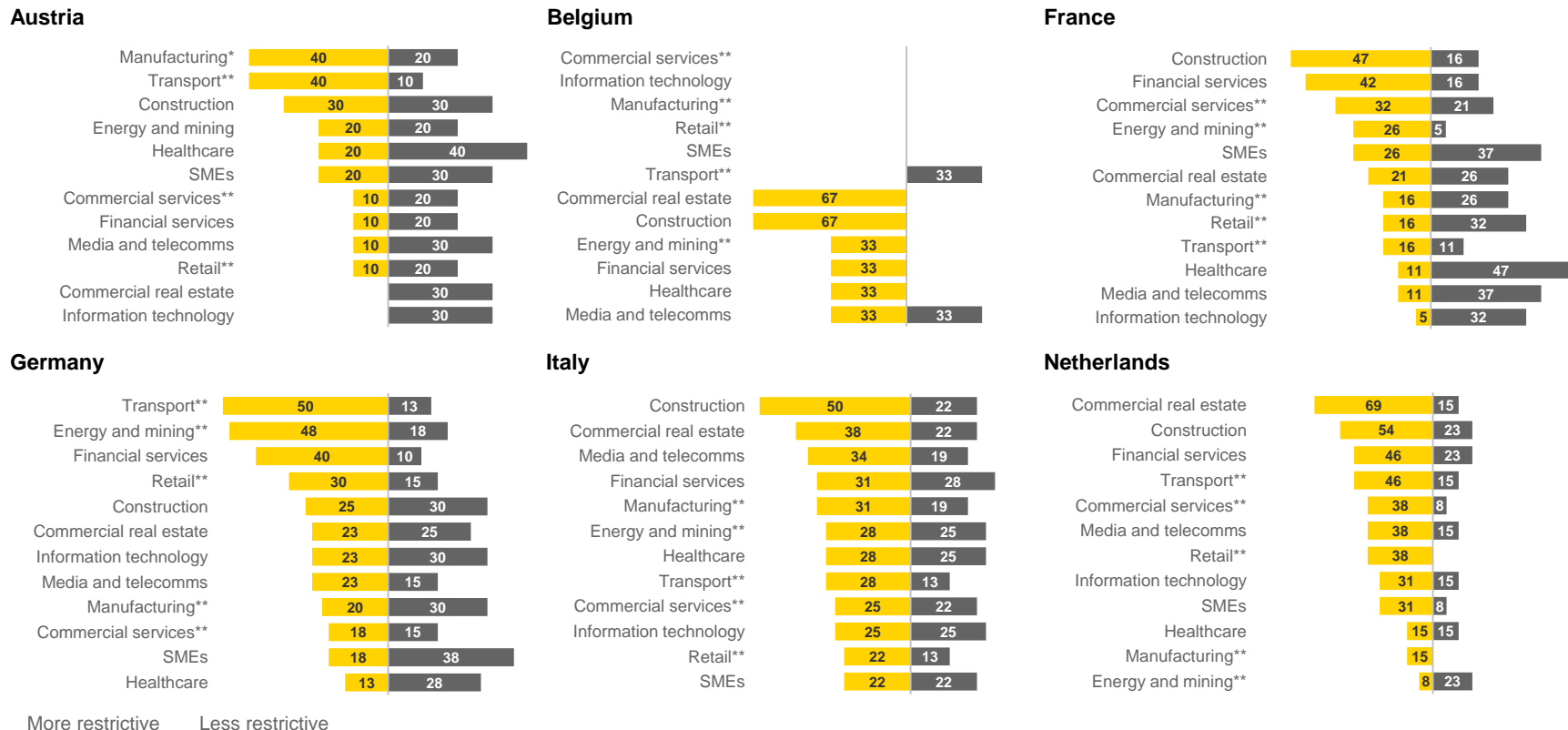
■ More restrictive ■ Less restrictive

Comments: The outlook for lending across a number of industries will weaken in 1H2013, with construction and commercial real estate (CRE) looking particularly pessimistic. In addition to the relatively poor health of these sectors, this also reflects the higher risk-weightings attached to CRE.

* Numbers are percentage of respondents answering.

Construction and property will feel the greatest lending policy tightening in 1H2013

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



* Numbers are percentage of respondents answering.

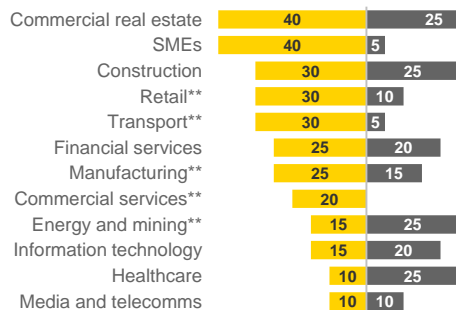
** Manufacturing includes industries, chemicals and engineering; Transport includes automotive and shipping, Retail includes consumer products, Energy and mining includes metals and commercial services includes professional services.

Where totals do not add up to 100%, remaining respondents answered 'Remain unchanged' or 'Don't know'. Where no data is shown all respondents answered 'Remain unchanged' or 'Don't know'.

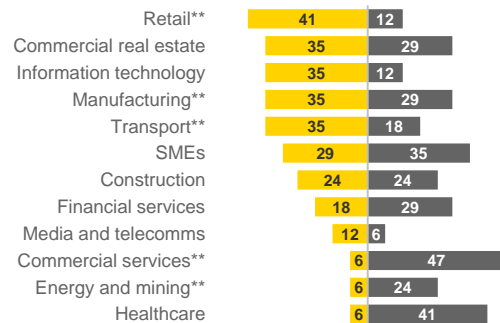
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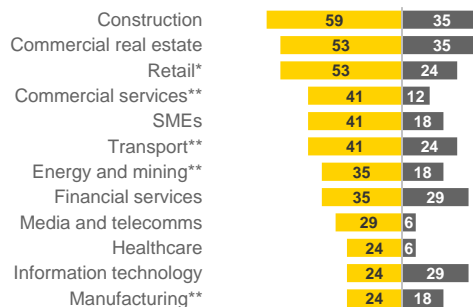
Nordics



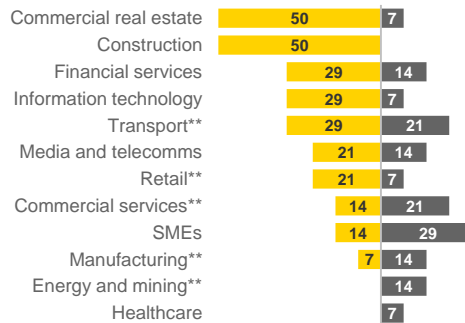
Switzerland



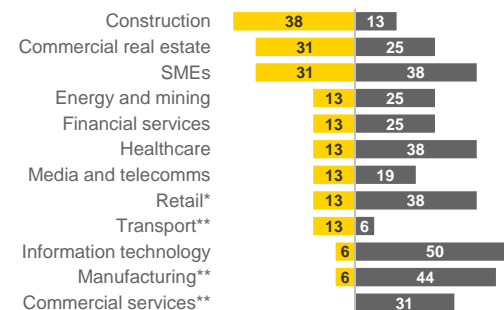
Poland



UK



Spain



More restrictive Less restrictive

* Numbers are percentage of respondents answering.

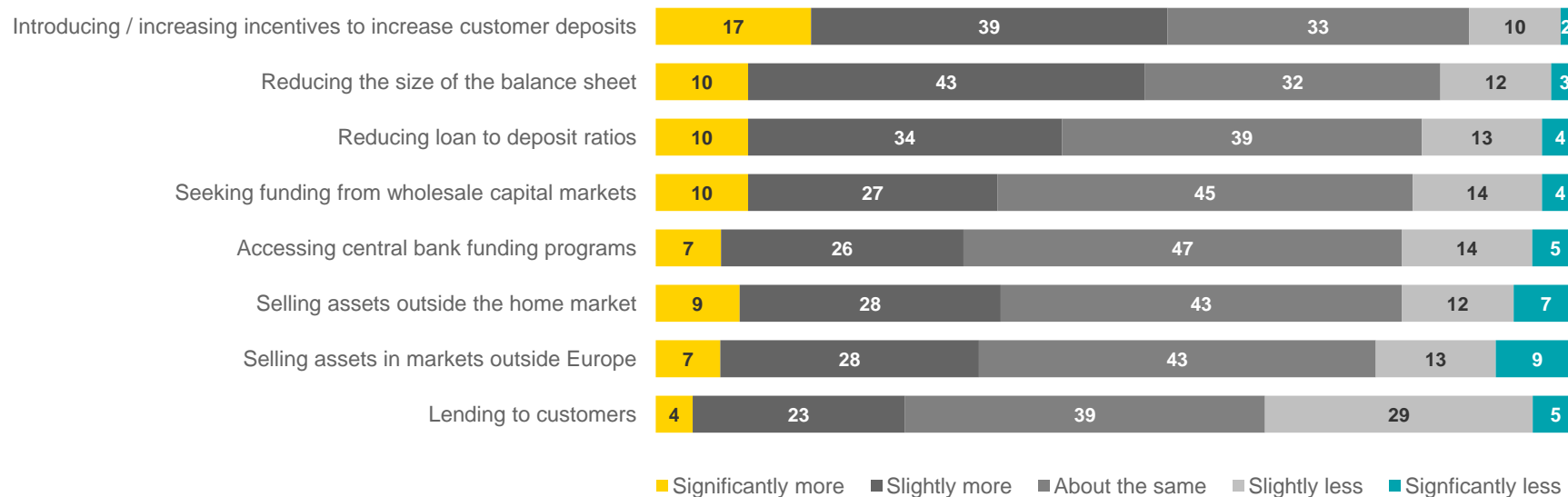
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Where totals do not add up to 100%, remaining respondents answered 'Remain unchanged' or 'Don't know'. Where no data is shown all respondents answered 'Remain unchanged' or 'Don't know'.

As well as shrinking their balance sheets, banks are focused on making them stronger and more stable

How likely are the banks in your market to be engaged in the following activities over the next 6 months?*

Autumn 2012

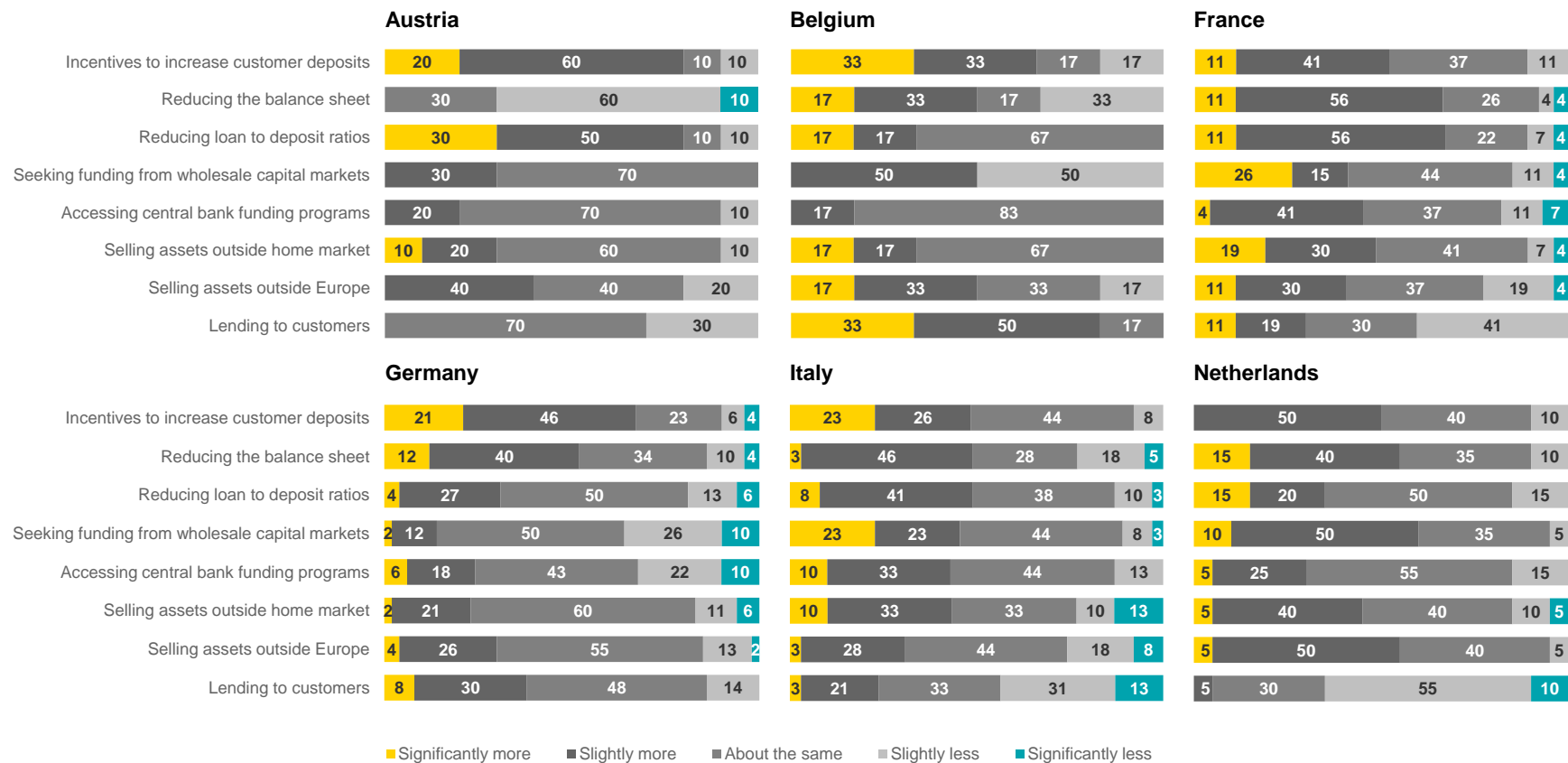


Comments: As banks prepare for Basel III implementation there continues to be a heightened focus on stable deposits and delivering the balance sheet. However, increased competition is likely to push up the cost of these deposits and, given the depressed economy, asset sales may not deliver the required returns.

* Numbers are percentage of respondents answering.

Simplifying and strengthening the balance sheet will continue to be a priority across Europe

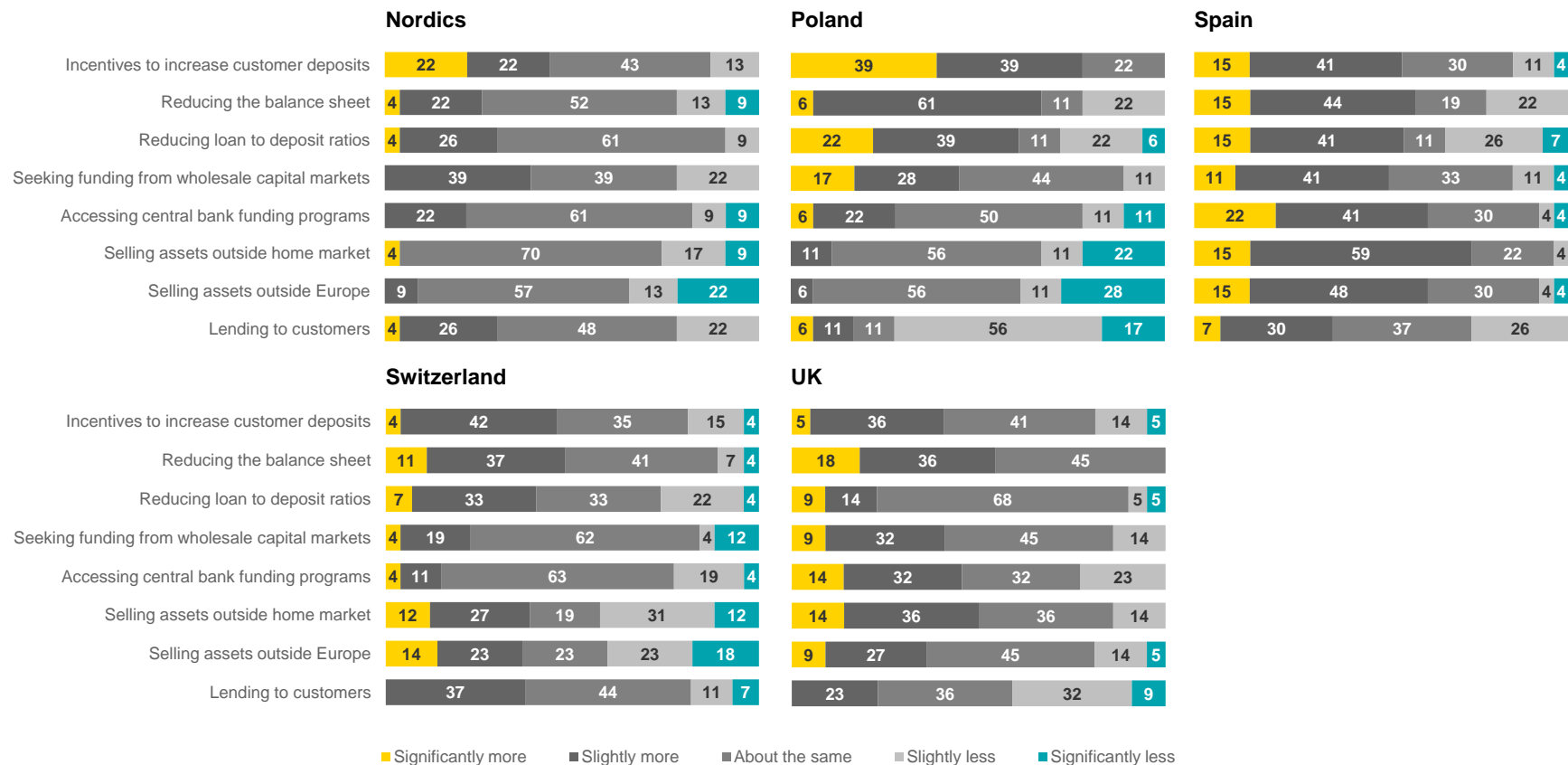
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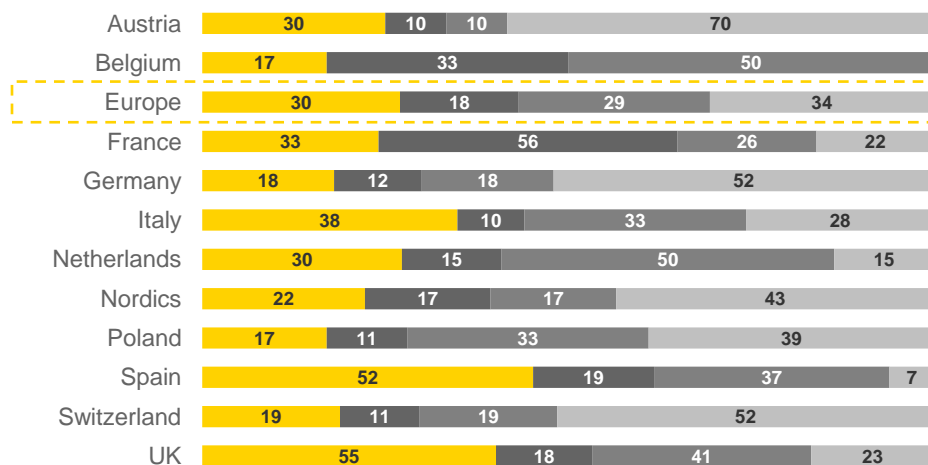
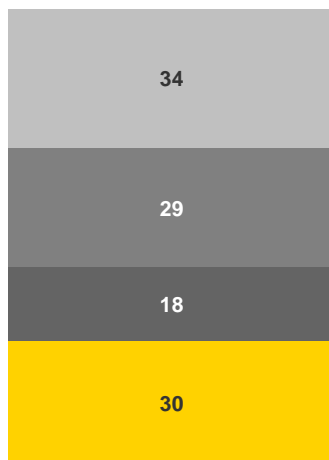


* Numbers are percentage of respondents answering.

Banks will be net sellers of assets in 1H2013

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?*

Autumn 2012



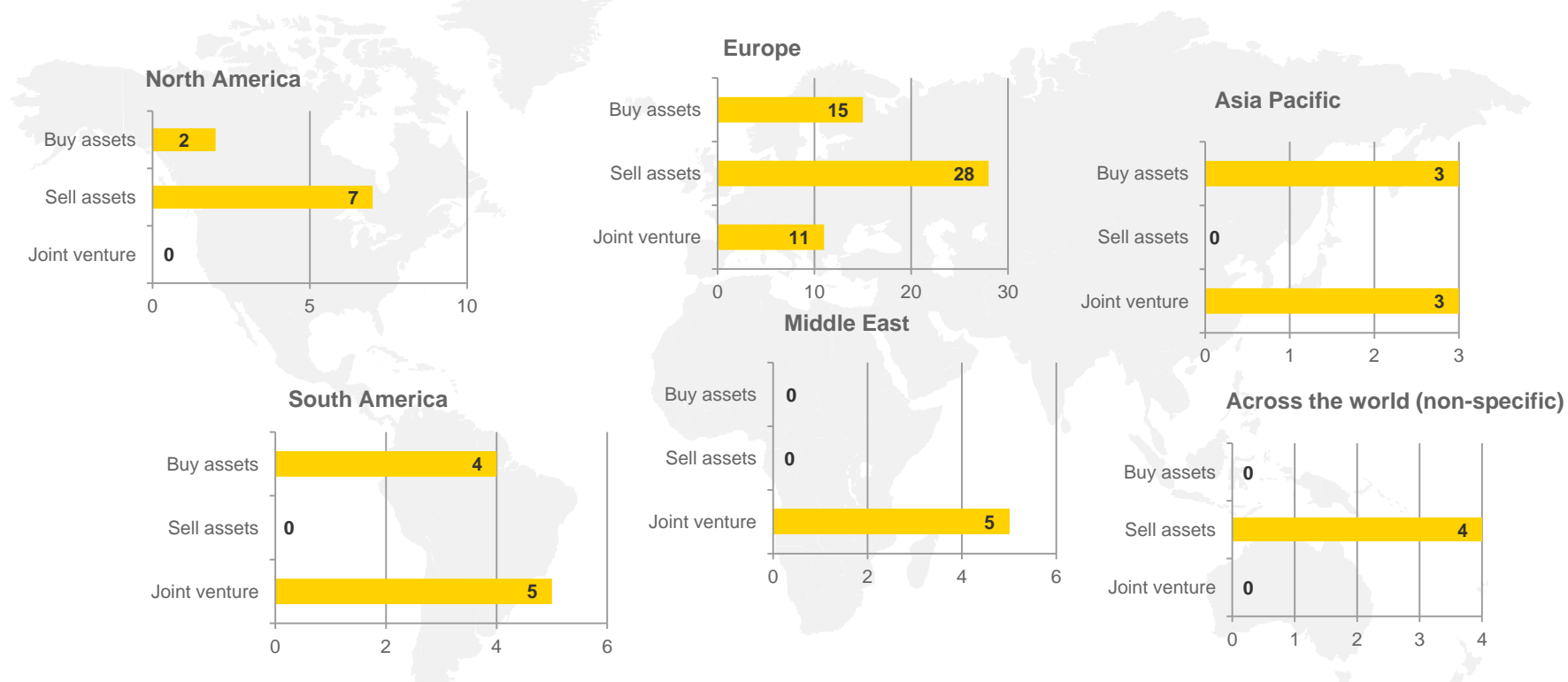
None of these
 Partnerships or joint ventures
 Buy assets
 Sell assets

Comments: Banks will continue to de-leverage during 1H2013 as they sell assets to reduce risk and build capital ahead of Basel III implementation. In some geographies, the selling of assets has also been prompted by competition regulation (e.g., UK) and attempts to stabilize the banking sector (e.g., Spain).

* Numbers are percentage of respondents answering (respondents could select more than one option).
Please note, chart may not add up to 100% due to respondents selecting 'Don't know' or 'Not applicable'.

Banks will seek to dispose of assets primarily in Europe (including CEE)

In which markets is your bank likely to sell / buy assets / consider a joint venture over the next six months?*



Comments: As banks look to strengthen their balance sheets they are more likely to sell assets than acquire new business in the first half of 2013, as they focus on their core markets. Outside Europe, banks are more likely to expand by partnering with local banks, particularly in emerging market regions, although often this is due to regulation requiring joint-ventures for market entry.

* Numbers represent the number of mentions.

Banks are evenly split on consolidation activity going into 2013

Do you expect there to be significant consolidation of the banking sector in your country?*

Autumn 2012

Spring 2012



Comments: Expectations and reasons for consolidation vary significantly between countries. For example, in Switzerland consolidation has been expected for some time, but now seems more likely as banks grapple with the increased regulatory burden and increased compliance and IT costs. In Spain the government has driven consolidation in an attempt to stabilize the banking sector. Conversely, the UK government has sought greater competition and encouraged new entrants to the market – a trend that looks set to continue.

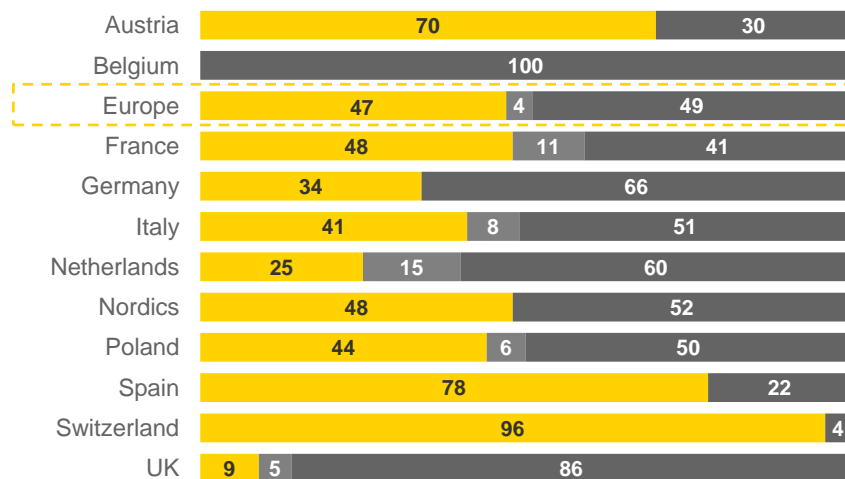
* Numbers are percentage of respondents answering.

Autumn 2012 responses are based on a three-point scale and spring 2012 responses are based on a two-point scale.

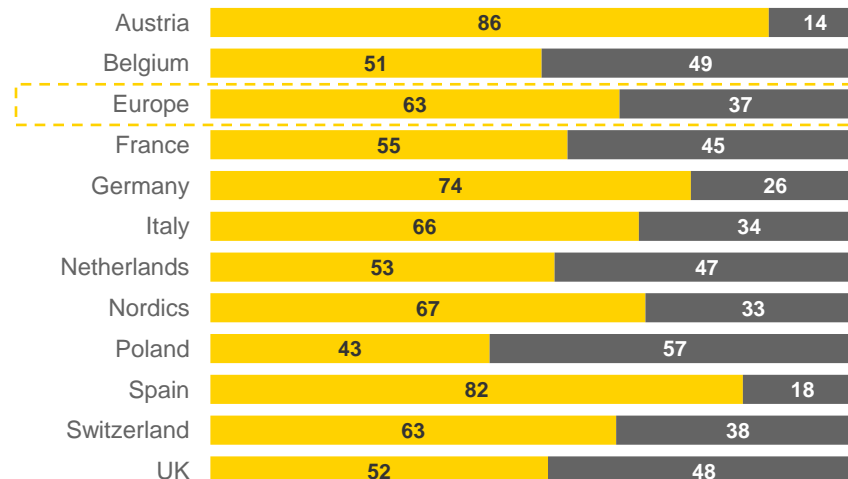
Switzerland, Spain and Austria stand out as markets expecting significant consolidation in 1H2013

Do you expect there to be significant consolidation of the banking sector in your country?*

Autumn 2012



Spring 2012



■ Yes ■ Don't know ■ No

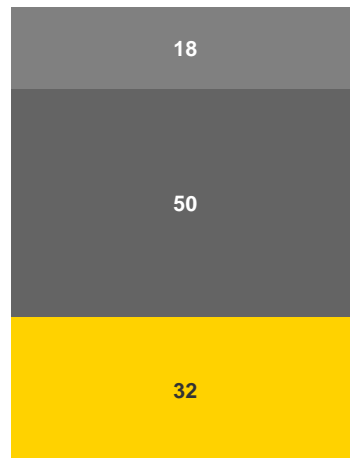
* Numbers are percentage of respondents answering.

Autumn 2012 responses are based on a three-point scale and spring 2012 responses are based on a two-point scale.

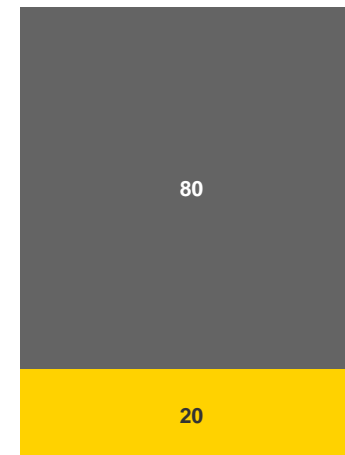
Banks expect most consolidation to happen within the next three years

In what timeframe do you anticipate this consolidation occurring?*

Autumn 2012



Spring 2012



■ More than three years from now ■ Within 1-3 years
■ Within the next 12 months

■ In the medium- to long-term ■ Within the next 12 months

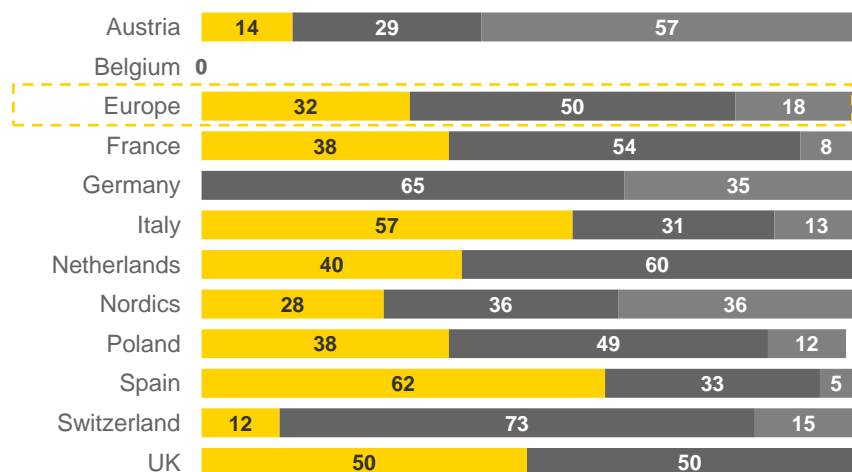
Comments: Regulation and the Eurozone crisis will be key drivers of short-term consolidation but most banks expect consolidation to occur in a 1-3 year timeframe. This reflects both the difficulty in finding acquirers for assets, given more immediate challenges and the reluctance of sellers while asset prices are low.

* Numbers are percentage of respondents answering.
Spring 2012 survey had two options rather than three.
Data calculated using the percentage answering 'Yes'.

Perhaps not surprisingly, Italian and Spanish banks expect big consolidation sooner rather than later

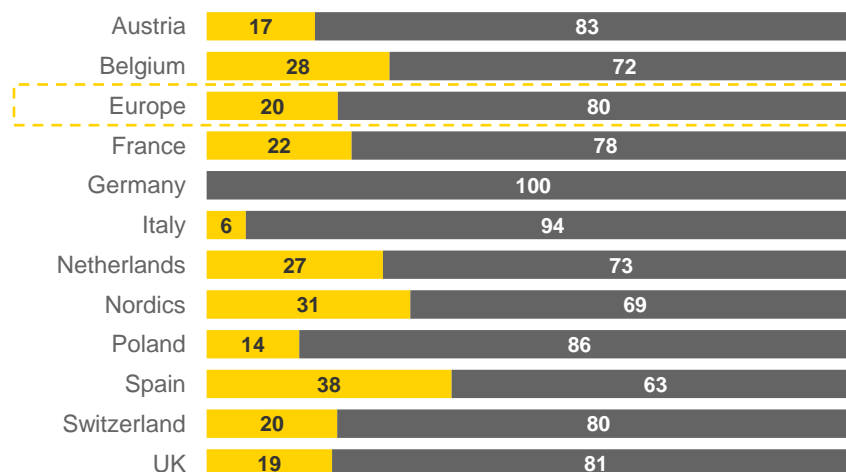
In what timeframe do you anticipate this consolidation occurring?*

Autumn 2012



■ Within the next 12 months ■ Between 1 and 3 years ■ More than 3 years

Spring 2012



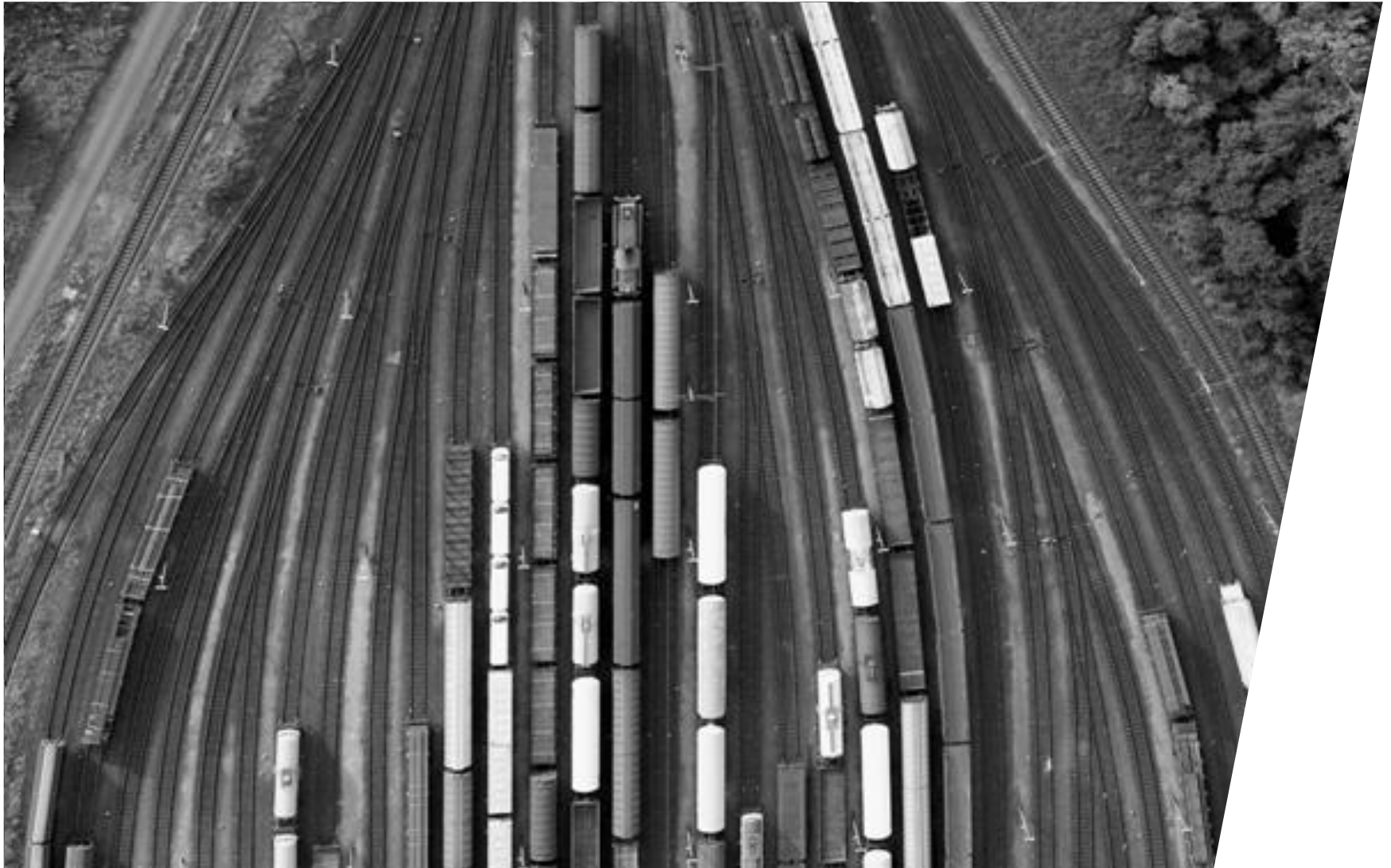
■ Within the next 12 months ■ In the medium- to long-term

* Numbers are percentage of respondents answering.

No respondents from Belgium expected consolidation in the banking sector.

Data calculated using the percentage answering 'Yes'.

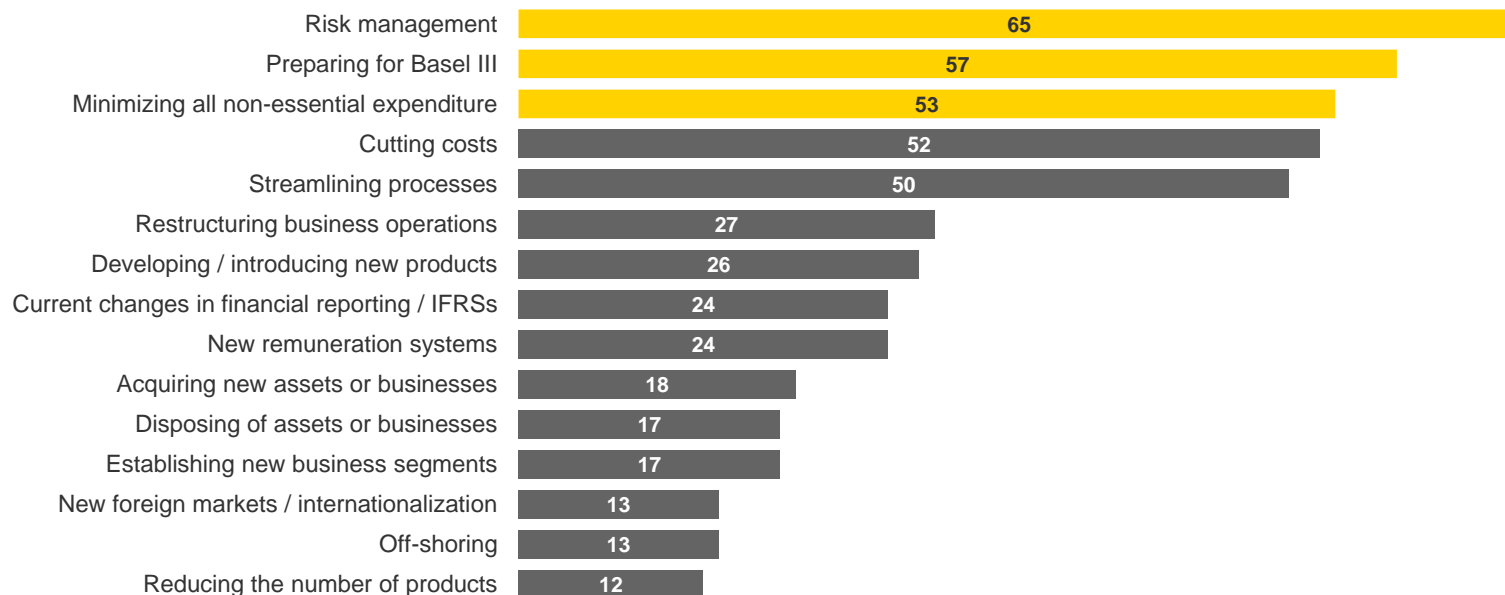
Business priorities and product line expectations



Strengthening balance sheets and cutting costs continue to be key areas of focus for 1H2013

How important are the following activities likely to be for you bank over the next six months?*

Autumn 2012



Comments: Given the economic outlook and the regulatory agenda, it's not surprising that banks will remain focused on the same core areas of risk, regulation and cost. In a low revenue environment the control of costs remains essential and the renewed focus on cost reduction may lead to further job losses.

* Numbers are percentages with score 8 to 10.
Respondents were asked to provide a score between 0 and 10, 0 being not important and 10 being very important.

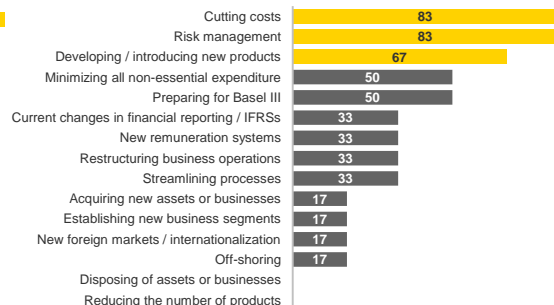
Across Europe, the growth agenda continues to be overshadowed by a focus on risk, region and cost

How important are the following activities likely to be for you bank over the next six months?

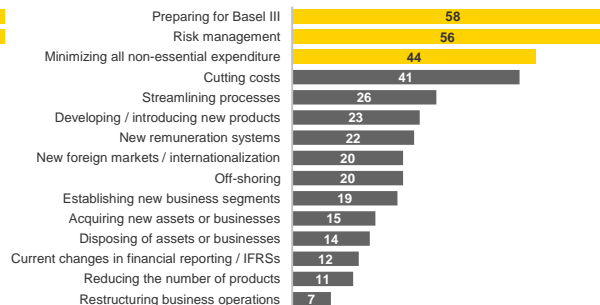
Austria



Belgium



France



Germany



Italy



Netherlands



* Percentages with scores 8 to 10.

Across Europe, the growth agenda continues to be overshadowed by a focus on risk, region and cost

How important are the following activities likely to be for you bank over the next six months?*

Nordics



Poland



Spain



Switzerland



UK

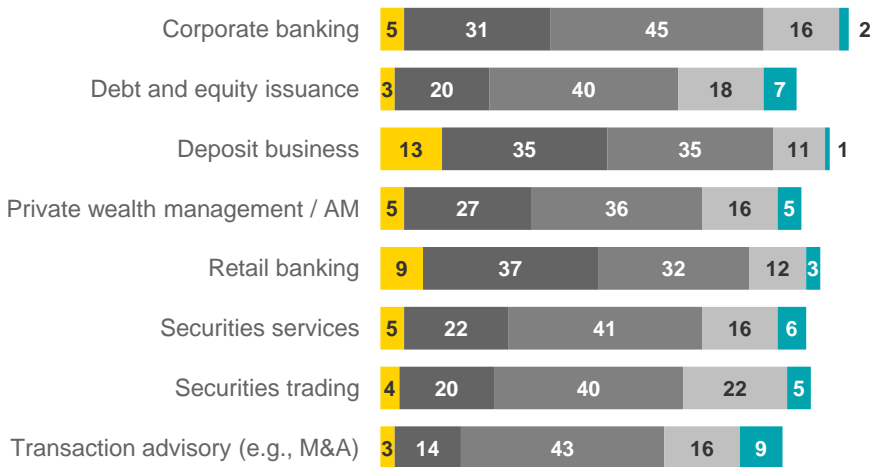


* Percentages with score 8 to 10.

The outlook across all business lines is significantly weaker going into 1H2013

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

Autumn 2012



■ Very good ■ Fairly good ■ Neither good nor poor ■ Fairly poor ■ Very poor

Spring 2012



■ Good ■ Fairly good ■ Fairly poor ■ Poor

Comments: Uncertainty continues to dampen investment banking activity as companies delay major investments and organic expansion. Reflecting this, banks expect deposits to increase, which will at least help those with funding challenges. Investment banks expect tougher conditions in the first half of 2013. Securities grew rapidly to become the principal contributor to investment banking revenues by 2008, but the volatility of returns through the crisis have led a number of banks to shift their focus to steadier business lines. The outlook for transaction advisory was also poor, as companies would rather consolidate or grow organically than expand through acquisition.

* Numbers are percentage of respondents answering.

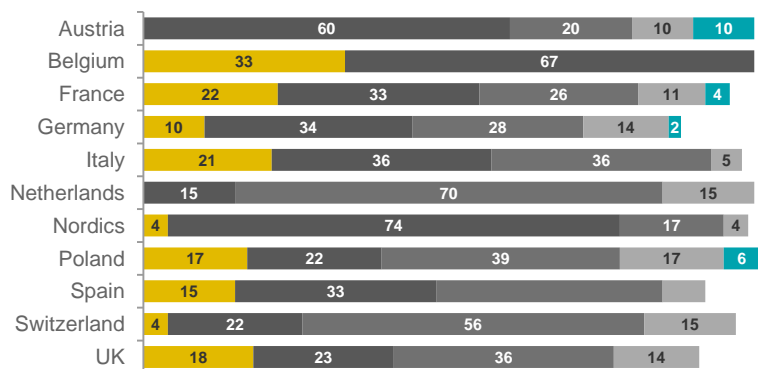
Autumn 2012 responses are based on a five-point scale and spring 2012 responses are based on a four-point scale.

Please note, chart may not add up to 100% due to respondents selecting 'Don't know' or 'Not applicable'.

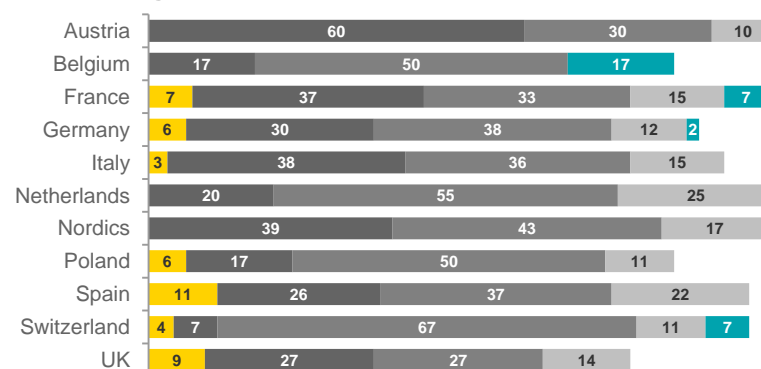
Retail banking and overall deposit-taking offer some relief to an otherwise still challenging outlook

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

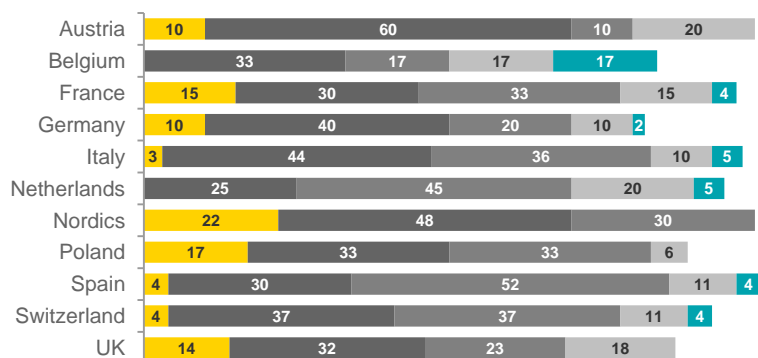
Deposit business



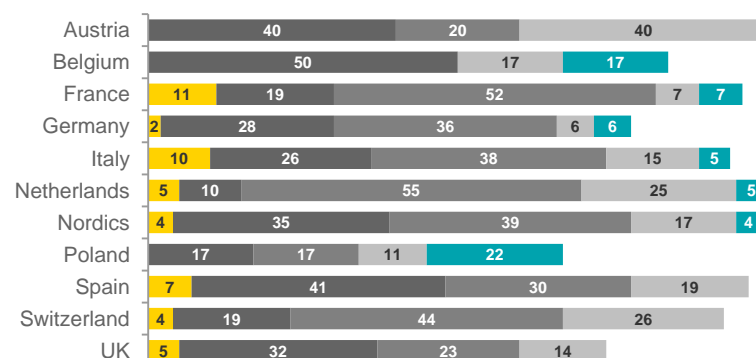
Corporate banking



Retail banking



Private wealth management/ AM

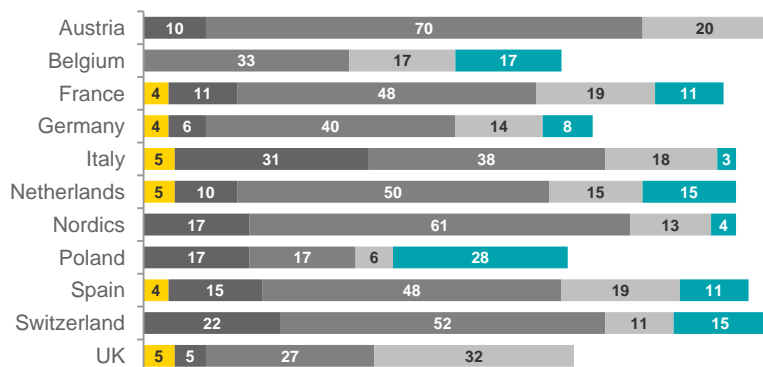


* Numbers are percentage of respondents answering (respondents could select more than one option).
Please note, chart may not add up to 100% due to respondents selecting 'Don't know' or 'Not applicable'.

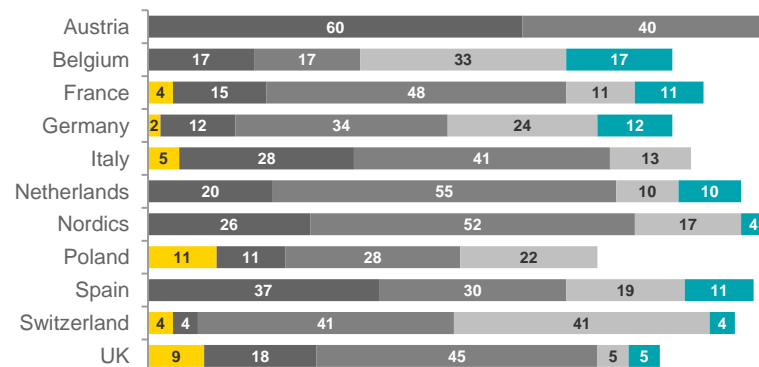
Transaction advisory and securities trading face the weakest prospects in investment banking

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

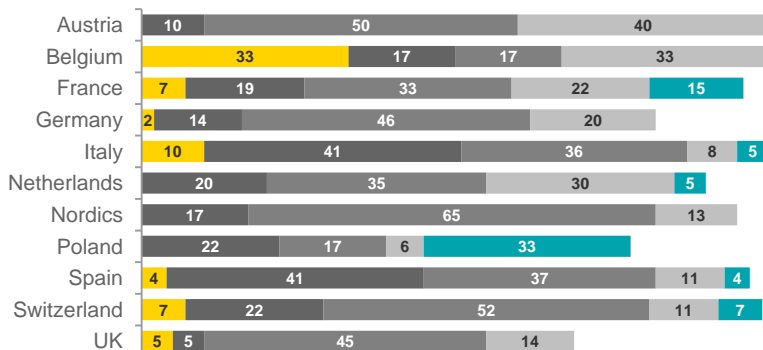
Transaction advisory



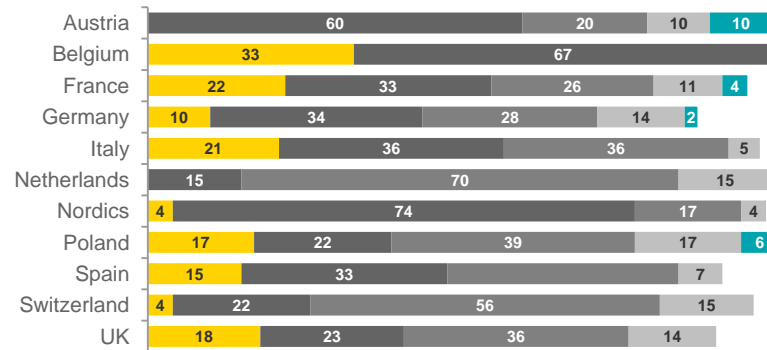
Debt and equity issuance



Securities services



Securities trading



Very good Fairly good Neither good nor poor Fairly poor Very poor

* Numbers are percentage of respondents answering (respondents could select more than one option).
Please note, chart may not add up to 100% due to respondents selecting 'Don't know' or 'Not applicable'.

Although relatively good compared to other business lines, the outlook for retail product lines is marginally weaker than in Spring 2012

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

Autumn 2012

Spring 2012



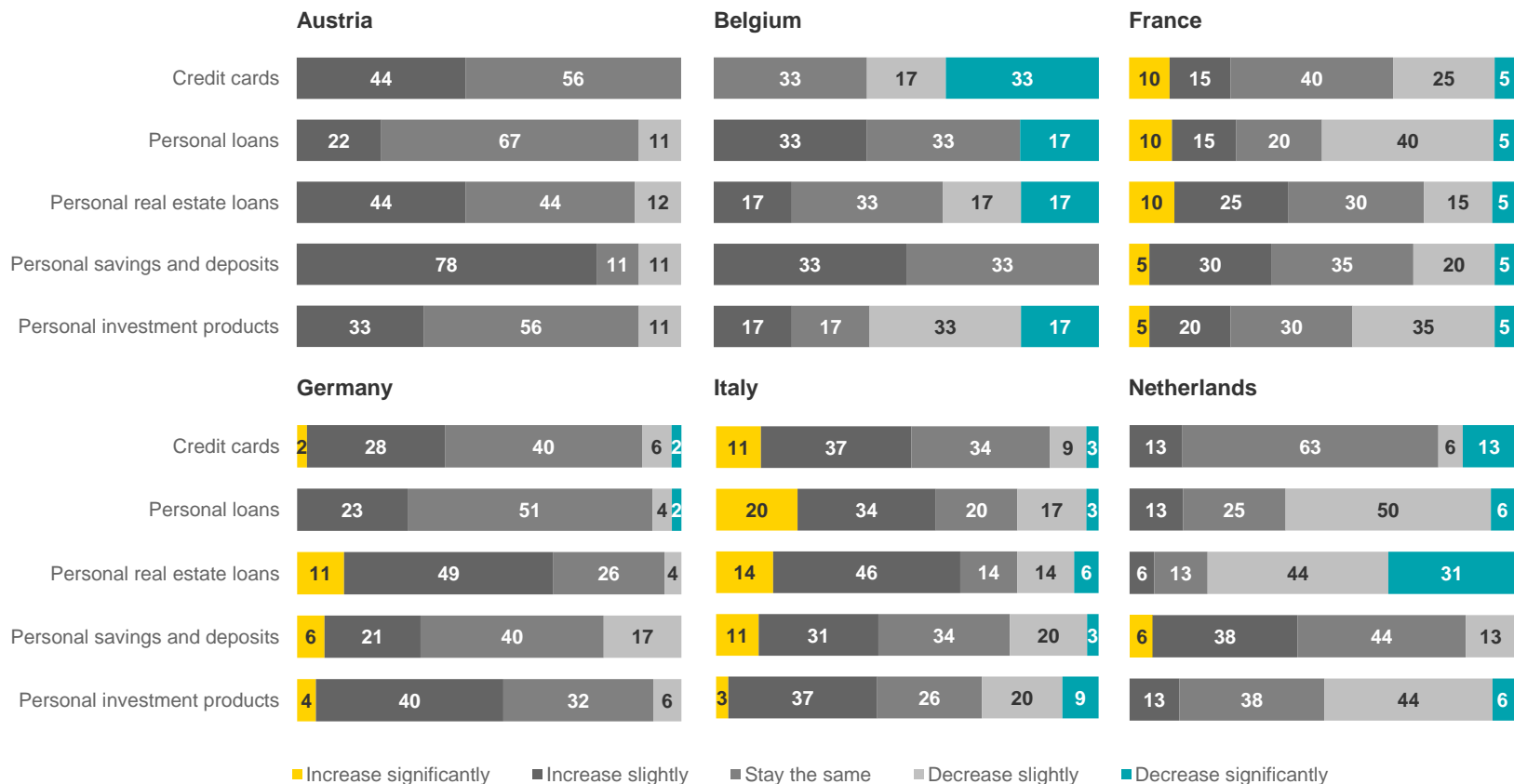
Comments: A slight fall in demand for credit cards and personal loans reflects retail customers attempting to improve their personal balance sheet as the economic recovery remains uncertain. The slight increase in demand for personal savings products shows savers turning away from volatile equity markets. The expectation of increased demand for residential mortgages suggests that the nadir of falling house prices may be passed in some countries, although access to housing finance is likely to remain a challenge for many.

* Numbers are percentage of respondents answering.

Autumn 2012 responses are based on a five-point scale and spring 2012 responses are based on a three-point scale.

Stronger retail mortgage loans are particularly evident in Germany and Italy

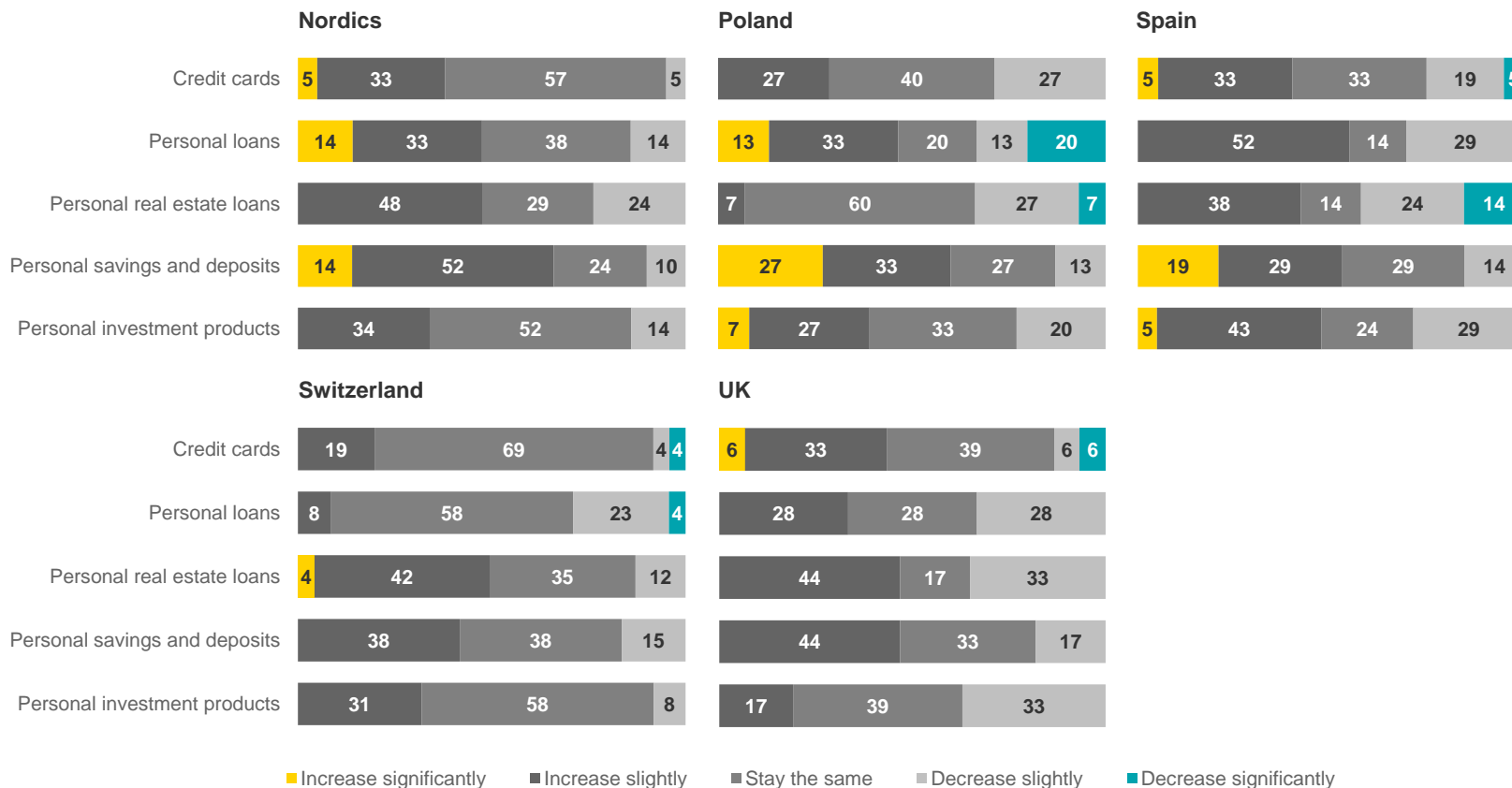
How do you expect customer demand for retail products at your bank to change over the next six months?*



* Numbers are percentage of respondents answering.

Poland and the Nordics should see strong personal savings and deposits growth in 1H2013

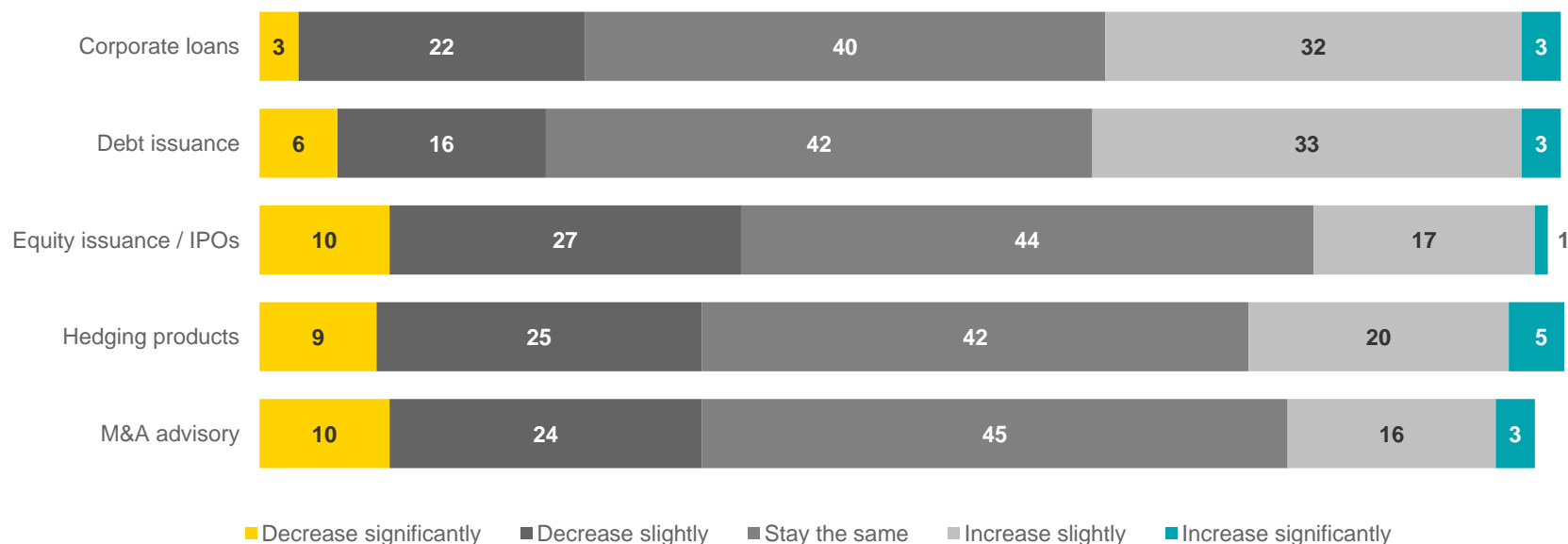
How do you expect customer demand for retail products at your bank to change over the next six months?*



* Numbers are percentage of respondents answering.

Corporate loans and new debt issuance offer banks the most hope in 1H2013

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

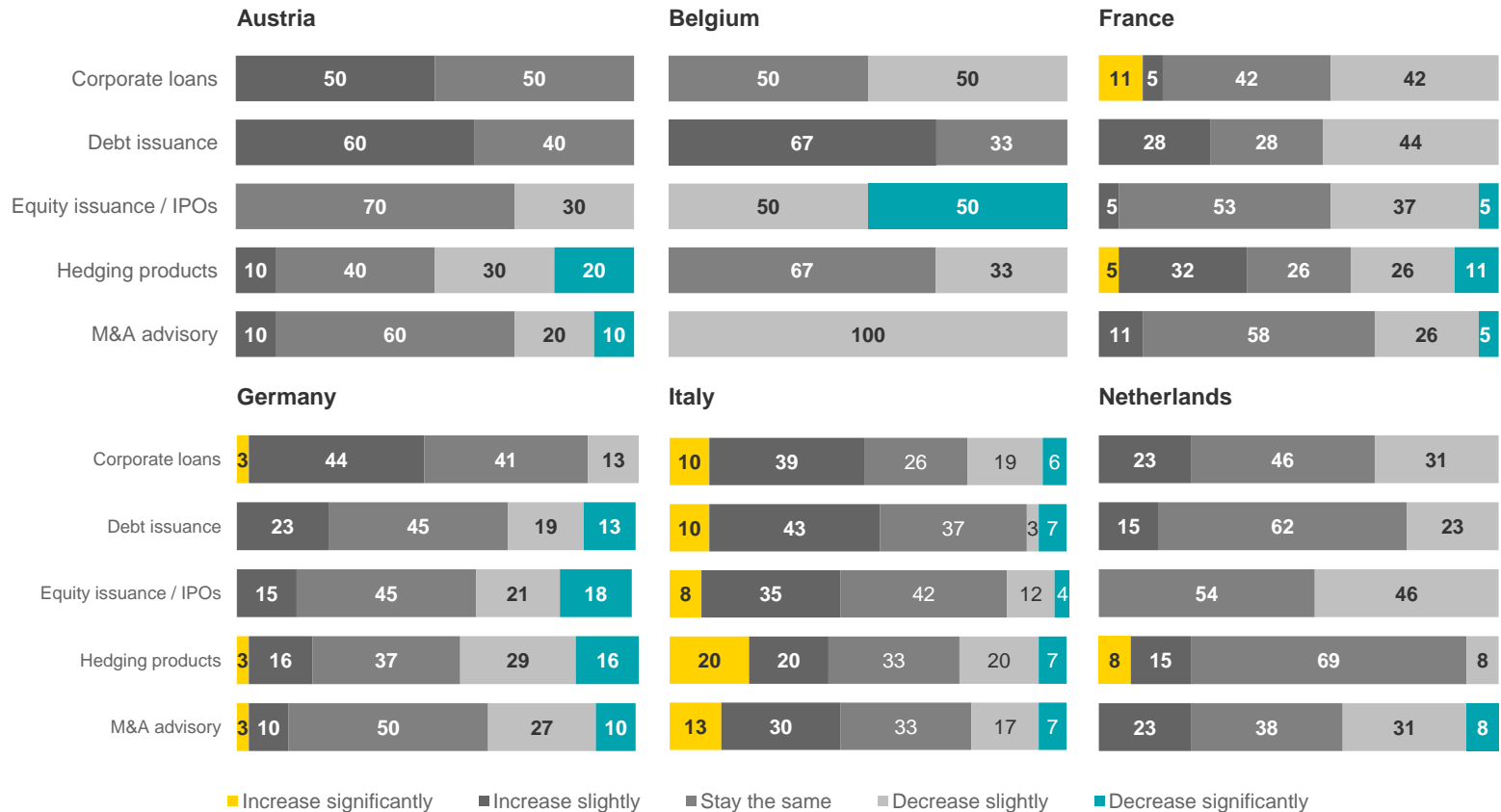


Comments: Equity issuance is expensive, and the recent failure of a number of high-profile IPOs will make many companies reluctant to tap the equity markets. Large corporates remain able to access the debt markets and, although capital market funding of corporates remains less prevalent in Europe compared to the US, it has picked up recently.

* Numbers are percentage of respondents answering.
Please note, chart may not add up to 100% due to respondents selecting 'Not applicable'.

Banks in the UK and, perhaps surprisingly, Italy and Spain, show most signs of optimism in corporate banking

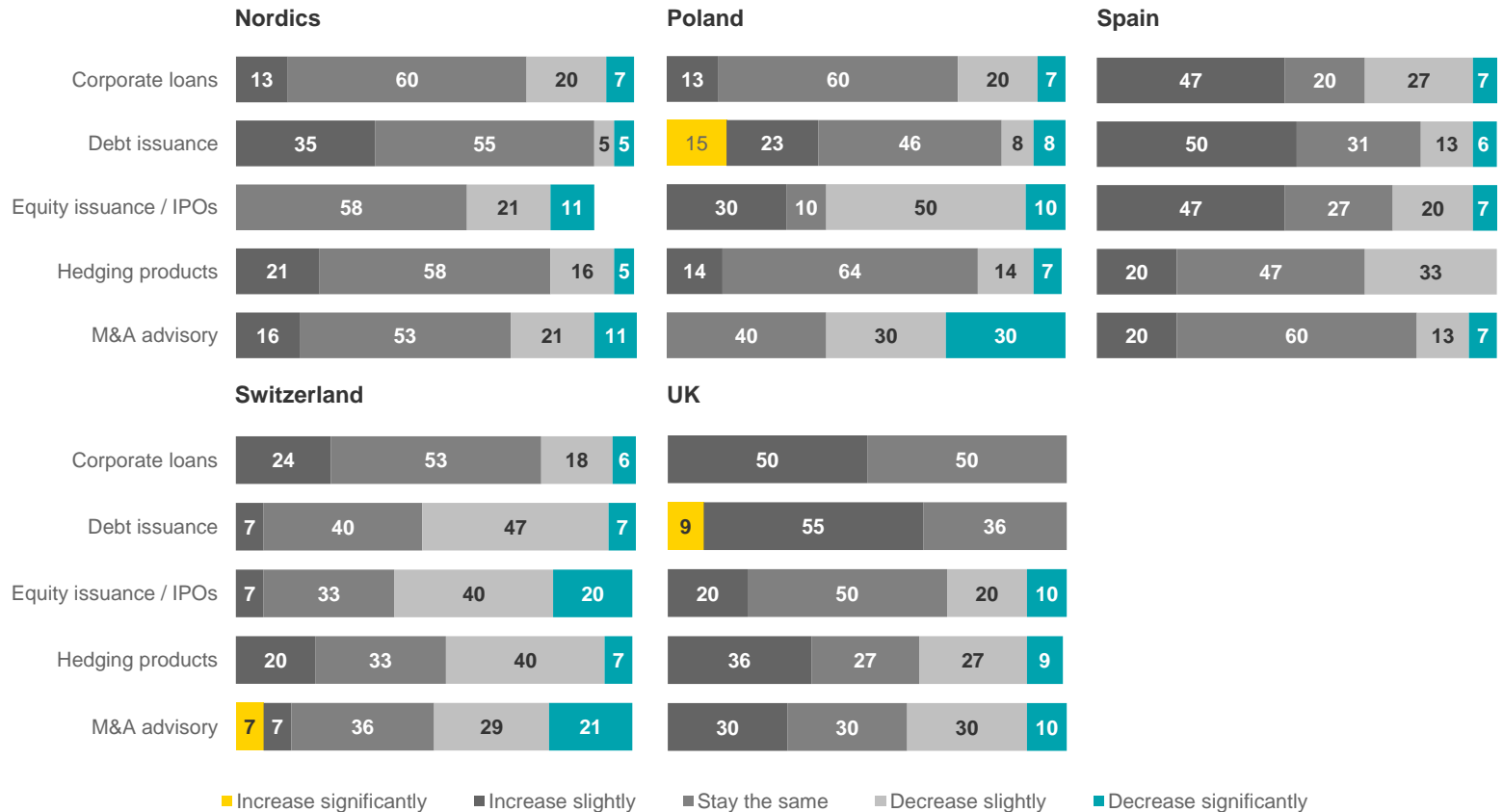
How do you expect demand for corporate products at your bank to change over the next six months?*



* Numbers are percentage of respondents answering.

Banks in the UK and, perhaps surprisingly, Italy and Spain, show most signs of optimism in corporate banking

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



* Numbers are percentage of respondents answering.

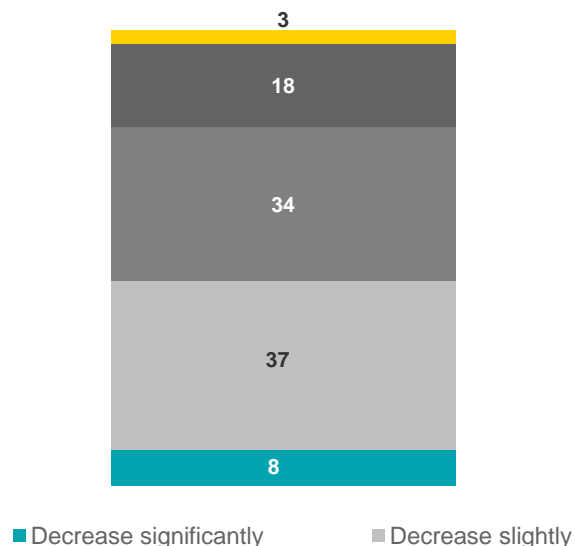
Employment



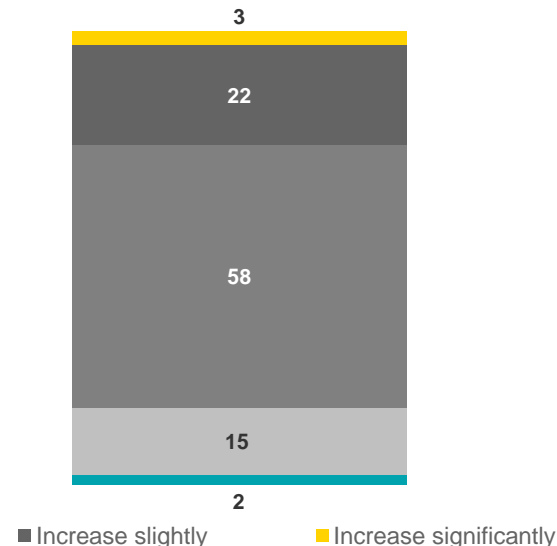
Further job losses are likely as banks continue to cut costs and restructure to focus on core activities

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

Autumn 2012



Spring 2012



Comments: Banks remain focused on cost reduction in 1H2013, and with staff costs a high proportion of over all costs – typically two thirds in an investment banks – a majority of respondents expect head count reductions across the next 6 months. The greatest reductions are expected in the Netherlands and the UK, where a number of redundancy programs have already been announced.

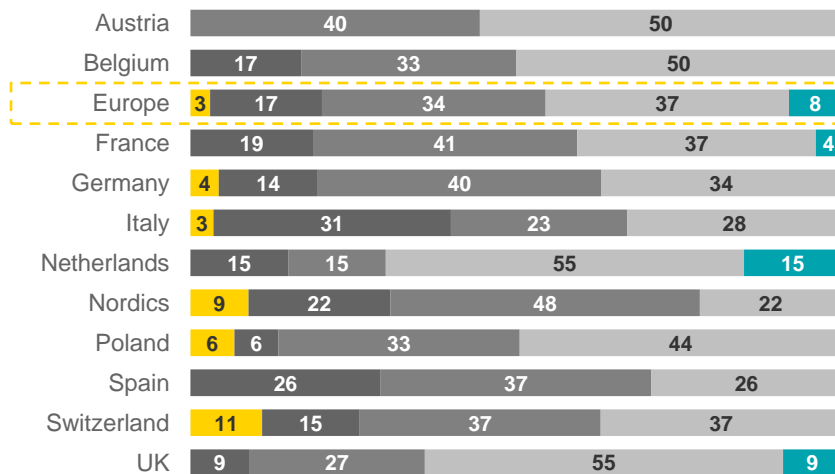
* Numbers are percentage of respondents answering.

The Netherlands and the UK face the strongest headcount reductions

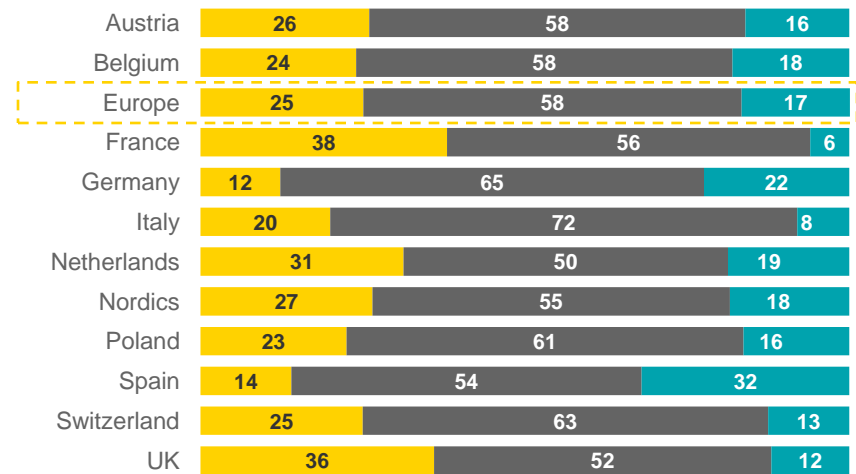
Over the next six months, what do you expect the headcount of your bank to do?*

Autumn 2012

Spring 2012



■ Increase significantly ■ Increase slightly ■ Stay the same
■ Decrease slightly ■ Decrease significantly



■ Increase ■ Stay the same ■ Decrease

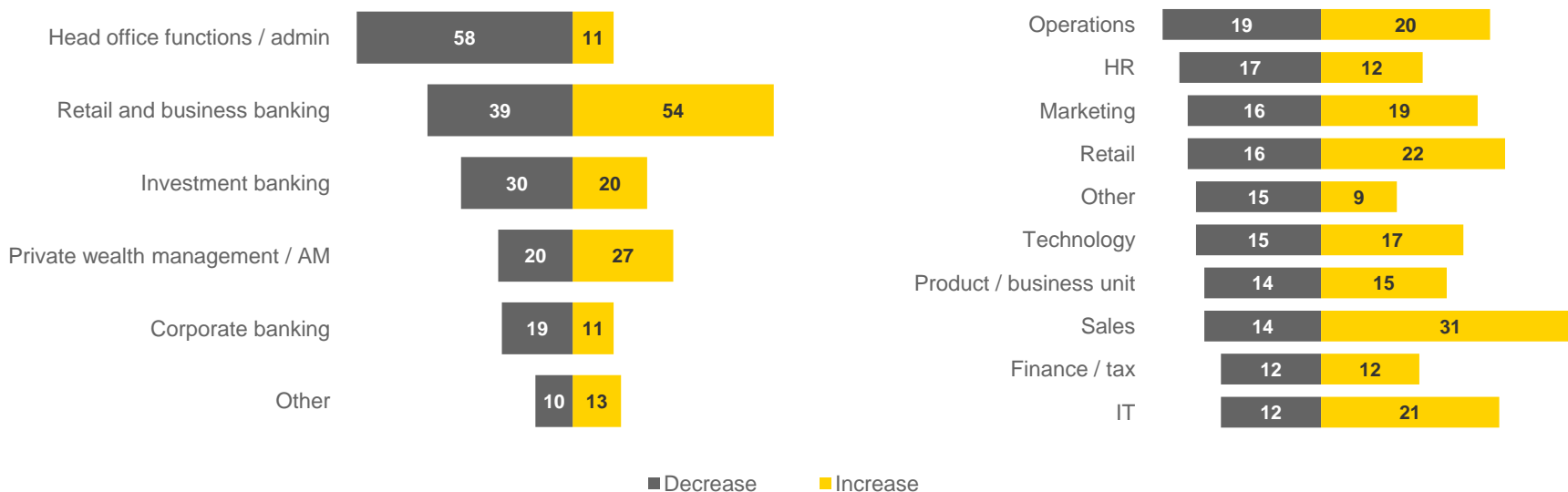
* Numbers are percentage of respondents answering.
 Autumn 2012 responses are based on a five-point scale and spring 2012 responses are based on a three-point scale.

Head office and administrative functions will face the biggest cutbacks

Which areas of the business do you expect headcount to be most impacted?*

Autumn 2012

Spring 2012

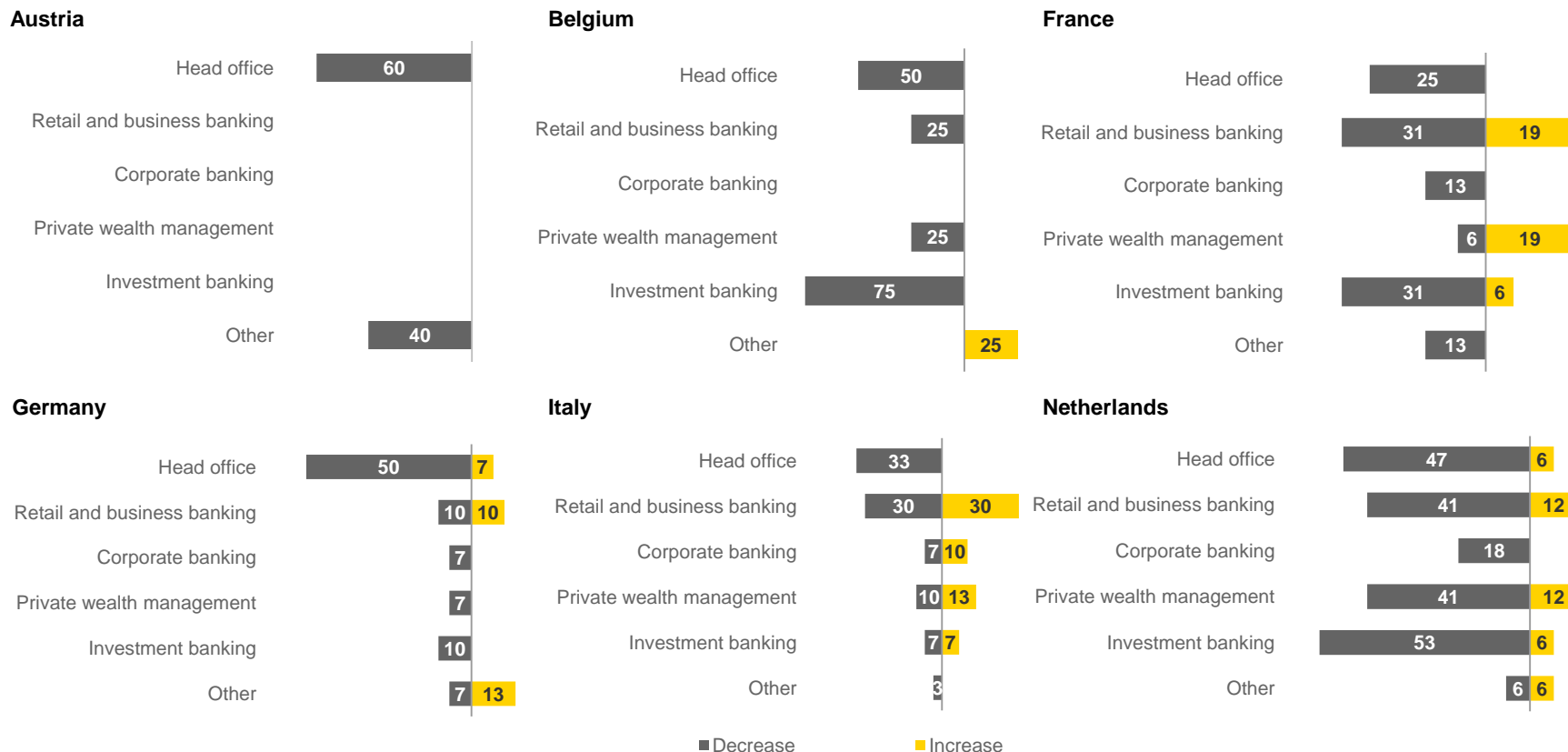


Comments: Retail banking is likely to see an increase in staff numbers over the coming months, in line with bankers' expectations of increased demand for retail products. Investment banking divisions and head office functions will be most impacted as banks are forced to reshape business and operating models.

* Numbers are percentage of respondents answering that headcount would either increase or decrease.

Investment banking will see the largest headcount cutbacks in three countries

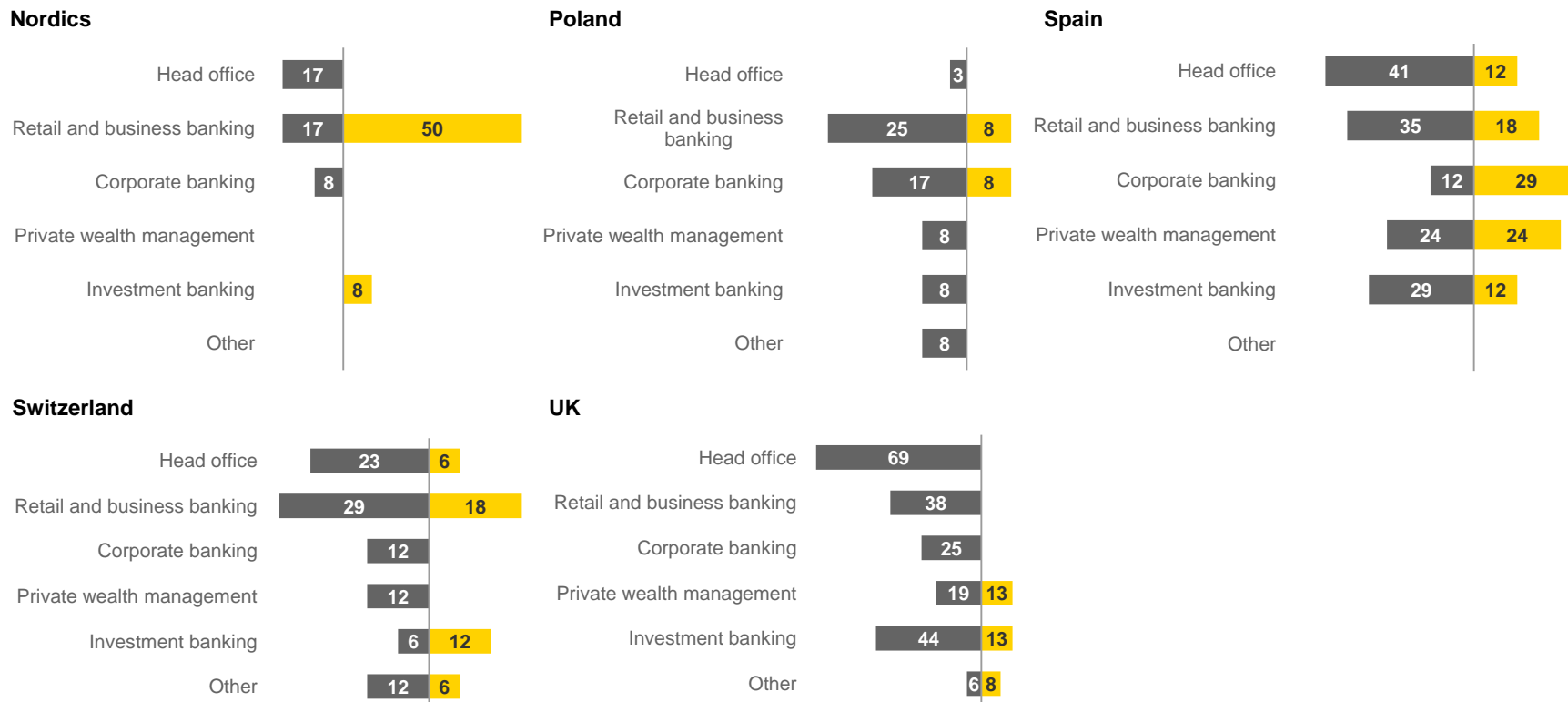
Which areas of the business do you expect headcount increases / decreases to take place?*



* Numbers are percentage of total respondents answering that headcount would either increase or decrease. Where no data is shown respondents thought headcount would stay the same.

Head office and investment banking face the largest employee cut backs

Which areas of the business do you expect headcount increases / decreases to take place?*



* Numbers are percentage of total respondents answering that headcount would either increase or decrease. Where no data is shown respondents thought headcount would stay the same.

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