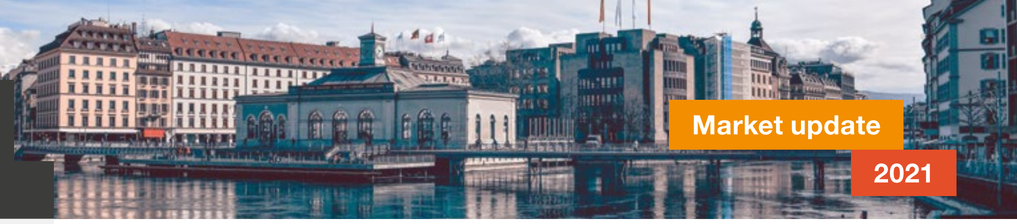
Private Banking Switzerland



82
private banks
in 2020

16
years of data

75
KPIs

86 %
market coverage
# of private banks in 2020

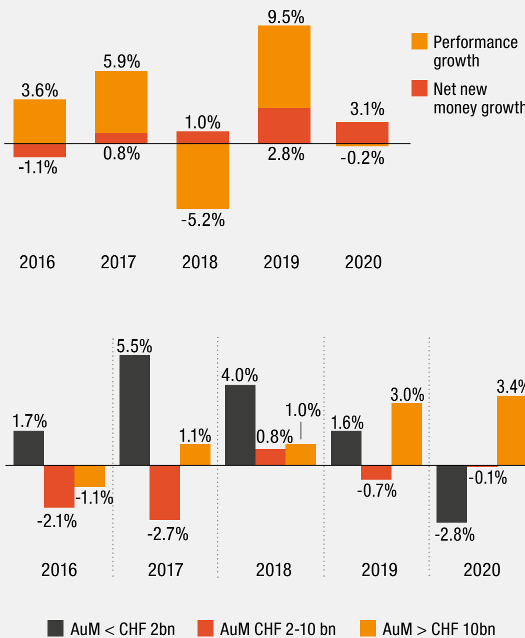
8th
edition since 2010

6
deals in 2020

Swiss Private Banking shows resilience despite COVID-19 pandemic

The year 2020 was dominated by the COVID-19 pandemic, yet the Swiss private banking sector still got off relatively lightly compared to other industries. Thanks to the quick recovery of global markets, Swiss private banks could broadly sustain their assets under management (AuM) base and, as such, worse consequences could be prevented. Despite the pandemic, Swiss private banks generated a record high net new money (NNM) of 3.1%.

However, the operating income margin suffered a decline of 7 basis points (bps) down to 82 bps, predominantly due to an erosion of the net interest income margin. After a strong wave of consolidation among smaller banks in previous years, 2020 has seen a shift in M&A activity towards the mid-sized segment, with a total of 4 transactions out of 6.



Strong NNM inflows in 2020 driven by large banks

At a glance

In 2020, global markets broadly recovered from their slump in March, and hit new highs by year end. However, Swiss private banks could not quite keep up with the strong recovery, and achieved a slight negative performance growth of -0.2%.

Even though the pandemic has led to restrictions on travel and physical meetings with clients, Swiss private banks could achieve the highest NNM growth in more than a decade, at 3.1% in 2020.

Over the last 5 years, large private banks have made a strong turnaround, from NNM growth of -1.1% in 2016 to 3.4% in 2020, which is the highest since the financial crisis in 2007. On the other hand, NNM growth among small banks was -2.8%, and as such moved into negative territory for the first time in the last 5 years. Mid-sized banks have been struggling for a decade, with an average NNM growth near zero.

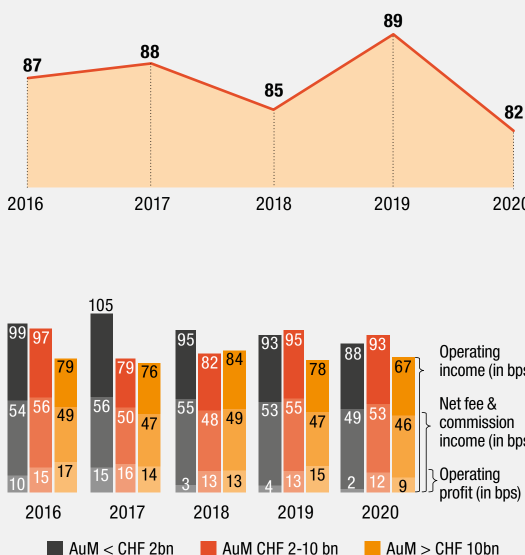
Overall, the private banking sector's AuM grew by 2.8% and reached CHF 2.9 trillion in 2020 based on our sample.

Outlook

NNM growth has been vastly dominated by large banks in the recent past due to three reasons:

- First, large banks benefited from their global footprint in high-growth markets such as APAC, LATAM and the Middle East.
- Second, clients seek trust in large banks during uncertain times due to their financial stability.
- Third, large banks seem to have adapted better to the restrictions caused by the pandemic compared to small and mid-sized banks. Larger banks have made larger investments in technology, such as new digital client channels, while small banks often lack the necessary resources.

We expect a similar picture for the next few years. Large banks will be able to attract positive NNM inflows between 2%-5% p.a., whereas the small and mid-sized banks will be struggling to attract any NNM inflows in the next few years.



Lower operating income margin mainly due to dip in net interest margin

At a glance

The ongoing margin pressure in the private banking sector is continuing, and led to a new all-time low of the median operating income margin of 82 bps in 2020.

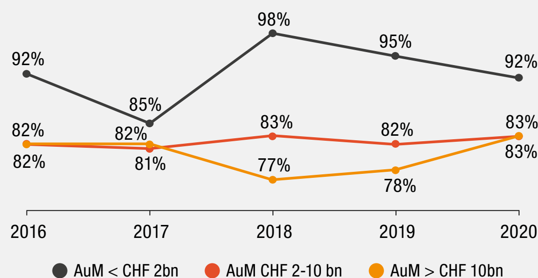
Income margins felt most prominently for large banks, with interest income margins falling from 19 bps in 2019 to a record low of 10 bps in 2020. Total operating income margins for large banks decreased from 78 bps in 2019 to 67 bps in 2020.

In contrast, mid-sized banks were able to broadly stabilise their margins over the last year, with operating income margins well above the 90 bps mark. The most significant reduction in operating income margins occurred in smaller banks, with a decrease from roughly 100 bps in 2016/2017 to 88 bps in 2020.

Outlook

This year's slump in operating income margin was caused by a sharp decline in net interest income margin from 15 bps in 2019 to 11 bps in 2020 as a consequence of the ongoing low interest rate environment with negative interest payments. In fact, large banks operate a more diversified business with larger exposures to loans, which has seen restrained financing activities and deleveraging since the outbreak of the COVID-19 pandemic.

The net fee and commission income (NFCI) margin has historically been the lowest for large banks which have a larger proportion of institutional clients with a lower fee structure. We would expect the net fee and commission income margin to slightly decrease further year by year in the next few years due to the strong competition in the private banking market in Switzerland. The net interest margin will stay at the current low level for the near future, since we don't expect a major increase in the general interest level.



High CIR due to reduced income margins and stable cost basis

At a glance

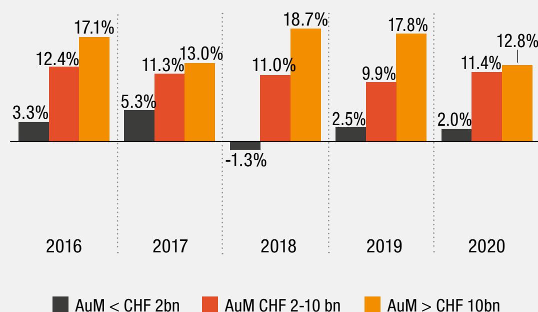
After the median cost/income ratio (CIR) of small banks peaked at 98% in 2018, there has been a gradual recovery down to 92% in 2020, close to the long-term average of 90% since the financial crisis. Despite these improvements, small banks are still reliant on efficiency gains to remain profitable. While the CIR of mid-sized banks remained roughly stable at slightly above 80%, large banks went above the 80% mark again in 2020 primarily due to lower net interest income.

The overall median CIR of the private banking sector increased from 81% in 2019 to 85% in 2020 due to lower margins with a more or less stable asset and cost base.

Outlook

Due to the stable cost basis of the last few years, CIR and the operating profit margin have been predominantly impacted by the dip in net interest margin. Going forward, we consider an average CIR of 80% to be a reference benchmark for the Swiss private banking sector for large and mid-sized banks. For smaller banks, the average CIR amounts to 90% or even above.

Only large and mid-sized banks with a lean operational setup, high cost control and the necessary scalability will be able to achieve a CIR of 70% or below.



Poor returns on regulatory required capital achieved by small banks

At a glance

The Swiss private banking sector's median after-tax return on regulatory required equity (RORE) of 8.0% dropped below the 10% mark for the first time in 2020.

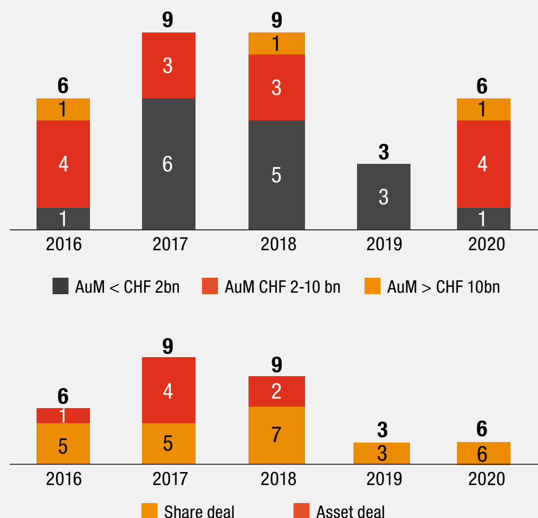
The median return on equity (ROE) in 2020 was even lower at 4.2%, due to the overcapitalisation of Swiss private banks of roughly between two and three times required capital for reputational and marketing reasons. Large banks' RORE decreased most significantly from 17.8% to 12.8% in 2020, due to lower net income generation in the pandemic year.

Mid-sized banks reached a RORE of 11.4% in 2020, and therefore remained slightly above their 5-year average of 11.2%. Small banks continue to struggle, with an all-time-low RORE of 2.0% in 2020.

Outlook

Despite a relatively high CIR of around 80%, Swiss private banks operate a balance sheet-light business with client assets being held off the balance sheet. This leads to lower risk-weighted assets and, in turn, a higher RORE. As a consequence, large and mid-sized banks are still able to cover their cost of capital on a RORE basis.

However, small banks are constantly destroying value, since they clearly missed their cost of capital goals in the past years. The continued decrease in RORE for small banks should put further pressure on consolidation in this segment. However, since the owners of smaller private banks are not always acting in a fully rational way, this consolidation among small banks can still take a few years until these banks are really heavily loss making.



Recent uptick in deals of mid-sized banks

At a glance

Consolidation in the private banking sector has slightly decelerated from an average of 9 transactions p.a. during the tax dispute episode between 2009 and 2016 to around 7 transactions p.a. over the past five years. In 2020, there were 6 private banking transactions, of which the disposal of Reyl & Cie SA was the largest in terms of AuM of around CHF 13.5bn.

After a wave of consolidation among weakly-performing smaller banks, in 2020 we primarily saw transactions with AuM above CHF 2.0bn with mid-sized banks involved as the most prominent group. These banks performed quite healthily, and the reasons for disposal were individual.

Outlook

Due to the increased risk in cross-border regulation, some banks had to redefine their core markets which led to a series of asset deals in the past. The low level of activity in asset deals over the last two years shows that banks have already retrieved from their non-core markets, and are focusing more on their core markets where they want to grow.

In the next few years, we would expect the number of transactions with smaller banks involved to increase again due to further pressure on profitability in this category of banks.

Coming soon

In our next publication, we will shed light on whether the Swiss private banking sector has generated or destroyed economic profit. Get an understanding of what key drivers, strategic initiatives and business models have contributed to the top leaders' economic profit. Stay tuned for more interesting insights about the Swiss private banking sector by subscribing to our distribution list.

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