

FINANCIAL SERVICES

Financial Services Executive Survey: Executives Bullish on Recovery

But Significant Challenges Remain

KPMG LLP







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A man with short, graying hair, wearing a dark suit, white shirt, and dark tie, is looking upwards and to the right with a thoughtful expression. He is holding a large, colorful map that is spread out in front of him. The background is a modern office interior with large windows and a white wall.

KPMG's Business Pulse Survey

KPMG LLP, the audit, tax, and advisory firm, surveyed C-suite and other top-level executives in the banking and broader financial services industry during the second quarter of 2010.

Participants were asked about business conditions in their sector, the most significant revenue growth areas, and factors that would impede their sector's recovery. They were also asked to assess the impact of potential regulatory reform on their businesses.

These responses were compared to the findings of a similar survey conducted among executives in the third quarter of 2009.

Key Findings from KPMG's Business Pulse Survey

KPMG's survey included 134 banking/financial services (FS) sector executives from large, U.S.-based companies with \$50 million+ annual revenue. Sixty-nine respondents represented the banking industry, and the remaining 65 were from other financial institutions. Thirty-two executives were from the New York metropolitan area and 102 were from other areas of the United States.

Key findings from the banking/financial services sector:

- More than 60% of respondents said business conditions were better in their sector than a year ago, and more than 75% said they would be better in 2011.
- Half of the executives surveyed plan to add headcount in 2010, and 48% expect the employment picture to be better in 2011.
- More than 50% of the respondents said their companies' ability to get financing and raise capital had improved over the past six months.
- Two-thirds of executives are investing for long-term growth and focusing on traditional services, emerging technologies, and mergers and acquisitions to generate growth.
- Respondents said the three factors most likely to hinder economic recovery in the banking/financial services sector are continuing high unemployment, the distressed real estate market, and increased government regulation.
- Nearly 90 percent of the executives believe systemic risk regulation will be enacted, and more than half expect this type of regulation to most impact their businesses if implemented.



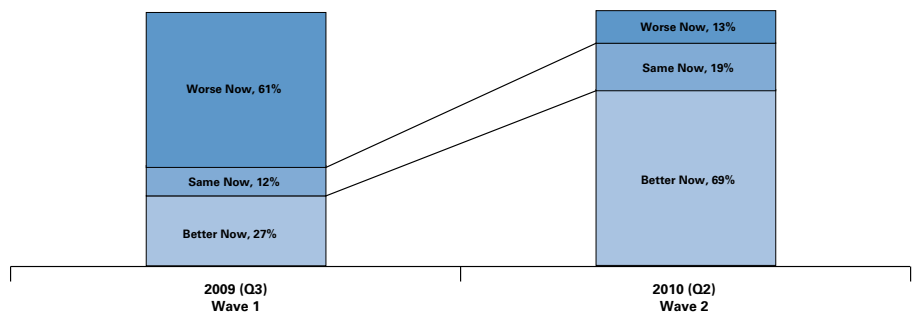


Bullish on Business Conditions

Overall, it is clear from the respondents' assessment of business conditions (revenue, profitability, and employment) that a banking/financial services sector recovery is underway but far from complete, with the expectation that some bumps remain in the road ahead. Also, the current business outlook within the sector has improved considerably from the bleak situation in 2009.

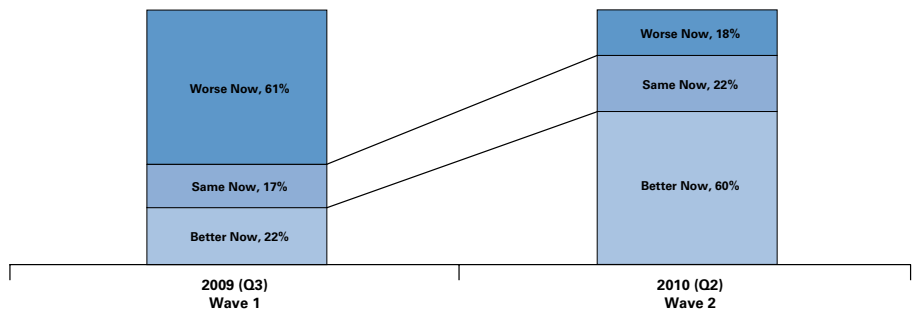
- More than two-thirds (69%) of sector executives say that current business conditions are better now than they were a year ago, a marked improvement from 2009 when only 27% felt this way.

Business Conditions Compared to a Year Ago



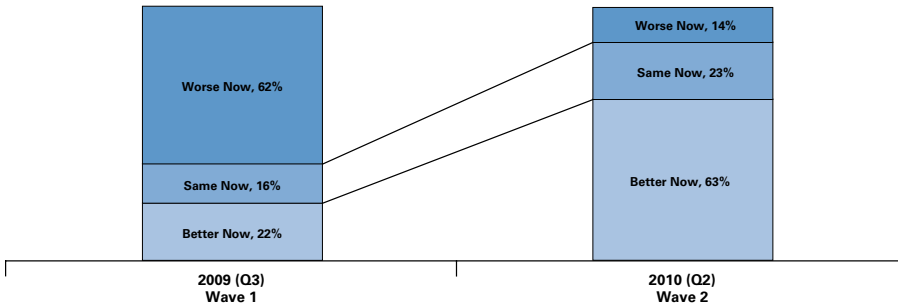
- Quarterly revenue also has substantively improved, with 60% saying that quarterly revenue is better than it was a year ago. This also is a marked improvement over Q3 2009 when only 22% responded that way.

Quarterly Revenue Compared to a Year Ago



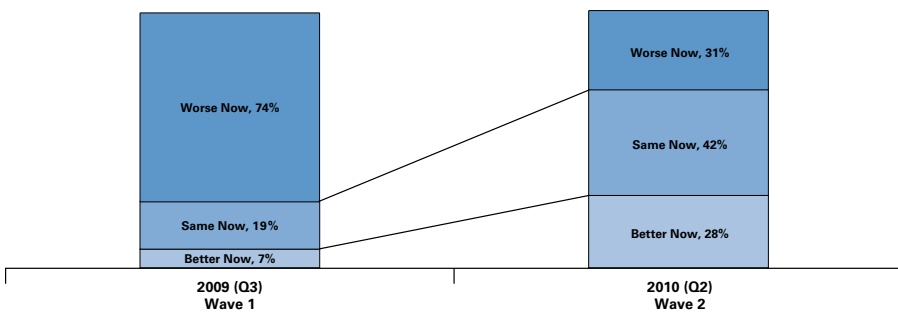
- Likewise, profitability has substantively improved, with 63% saying that current profitability is better than it was a year ago, again a marked improvement over Q3 2009 when only 22% responded that way.

Profitability Compared to a Year Ago



- Even employment—a lagging indicator—has improved versus Q3 2009, though not yet to the point of equilibrium.
 - Roughly a quarter (28%) of the respondents indicated sector employment is better than a year ago. However, nearly a third (31%) still indicate it is worse now than a year ago.
 - Responses indicate that there are signs that the deterioration in employment has leveled off or is starting to reverse, with over 70% of respondents indicating that employment levels were better or the same as last year.

Employment Compared to a Year Ago



- Currently, banking/financial services organizations in the New York metropolitan area are generally more upbeat about revenue and profitability than those in the rest of the United States. Overall, banking executives are less upbeat than other FS executives.

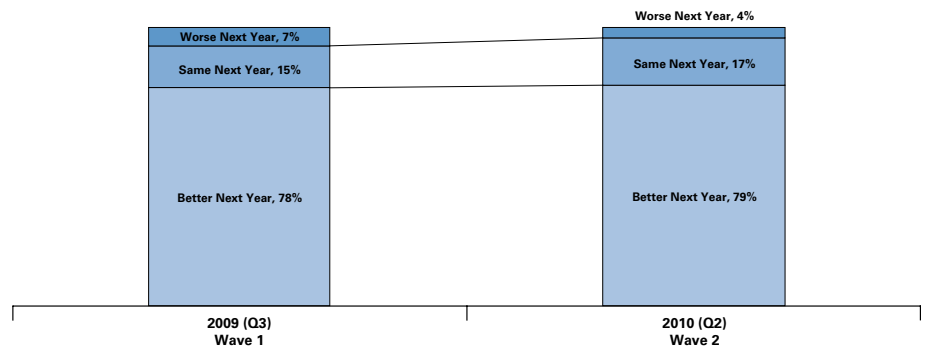




Financial services executives are extremely optimistic about the future, with most indicating that conditions should continue to improve over the next year.

- More than three quarters (79%) expect business conditions in the sector to be better one year from now—roughly the same level of optimism seen in Q3 2009.

Expected Business Conditions One Year from Now



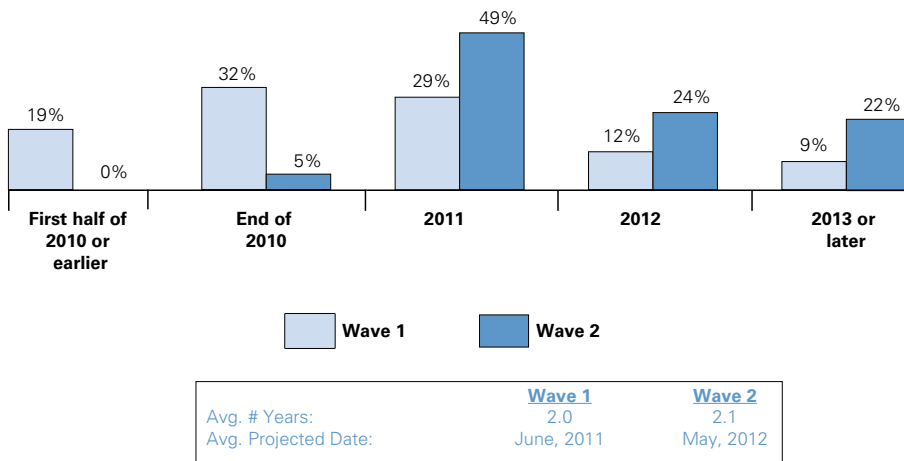
- There is strong optimism that business conditions will continue to get better in 2011:
 - 81% see better revenue.
 - 76% see better profitability.
 - 48% see a better employment picture.
 - Only 10% of respondents expect employment to be worse next year.
- Further, 50% expect their organizations to add headcount in 2010, and nearly half see employee salaries and bonuses increasing.

Time Line for U.S. Economic Recovery Pushed Back

Financial services executives surveyed said, on average, the projected time line for an overall U.S. economic recovery is about two years from now, or May 2012.

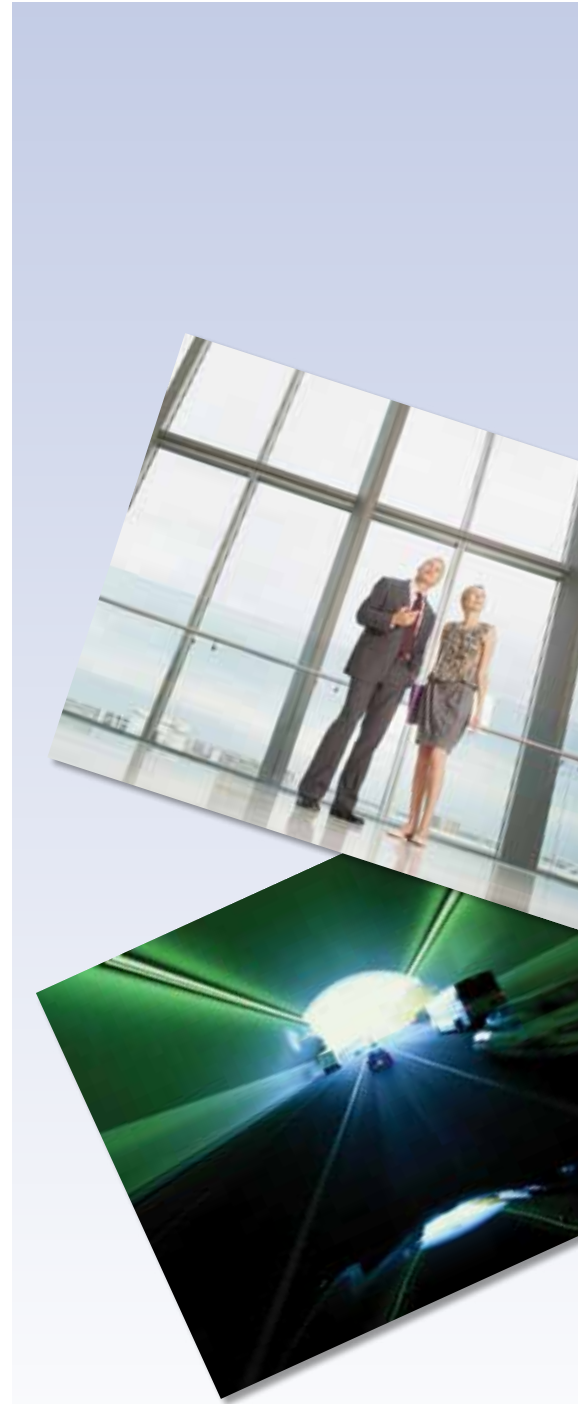
When asked in 2009, executives also projected about a two-year path to recovery, or June 2011. This ultimately means that the date of the expected recovery has been pushed back from their initial projections in 2009.

Time Line for Overall U.S. Economic Recovery



Financial services respondents generally see the sector recovering at the same pace as (38%) or faster than (46%) the economy as a whole. Only 16% feel their sector recovery will lag.

- Banking executives say they are less likely than other FS executives to see a faster-paced sector recovery.
- Respondents representing institutions in the New York metropolitan area indicate that they expect to see a faster-paced recovery than respondents representing institutions in other areas of the United States.



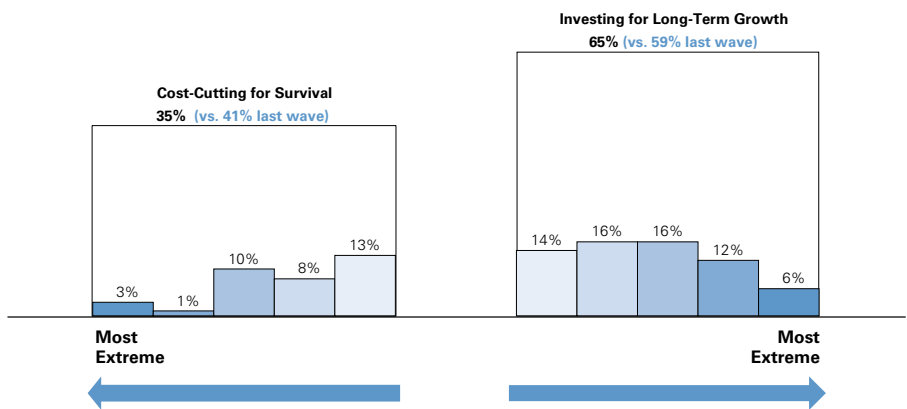


Strategic Emphasis – Investing over Cutting

In terms of strategic emphasis, the banking/financial services sector is more in the mode of “investing for long term growth” (65%) than in a mode of “cost-cutting for survival” (35%).

- More than half of the banking executives (58 percent) and 72 percent of the other FS executives said they were investing for long-term growth. More than half of the institutions in the New York metropolitan area (59 percent) said they were investing for long-term growth. Smaller organizations were the least likely to be investing for long-term growth (56 percent).
- Organizations currently leaning towards an “investing for long-term growth” strategy are much more likely than those who are strategically cost-cutting to view current conditions as improved versus last year. They are also more likely to expect revenue and employment to be better next year as compared to now.

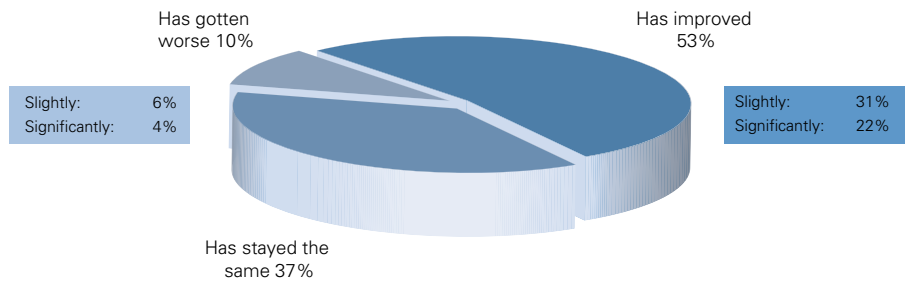
Current Strategic Emphasis



Perspective on Capital, Write-Downs, and Failures

About half of the banking/ financial services sector respondents say that their own companies’ ability to get financing and raise capital has improved over the past six months.

Companies’ Ability to Get Financing/Raise Capital over Past 6 Months

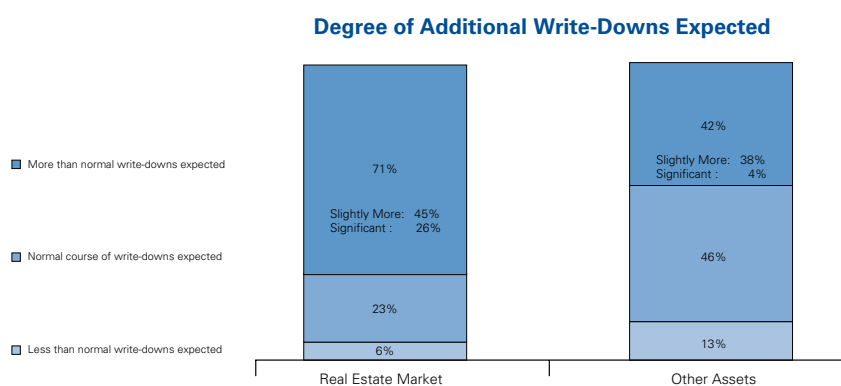


- This is much more the case for respondents representing institutions in the New York metropolitan area than those representing institutions in the rest of the United States.
- Also, organizations strategically investing for long-term growth are much more likely to report that their ability to get financing or raise capital has improved.

The executives surveyed see the bulk of investor capital going to traditional long-only funds (35%) and private equity funds (19%).

In terms of write-downs:

- Most respondents expect above-normal additional write-downs related to the real-estate market (71%), with more than a quarter seeing significantly more (26%).
- Just under half expect above-normal additional write-downs for other assets (42%).



Overall, about 40% of the financial services executives surveyed expect more bank failures in 2010 than in 2009, and over half of the bank executives surveyed (55%) feel this way.

Perspectives on Financial Sector Regulation

When this survey was conducted in April 2010, more than half of the executives (54%) felt that significant banking and financial regulatory change would occur before the end of the year.

- Banking executives see a shorter horizon than other FS executives.

While most respondents do not believe that regulation has the potential to improve trust between clients and advisers, a sizable minority (40%) do believe that regulation is at least somewhat likely to improve trust.

Of the various reforms under consideration:

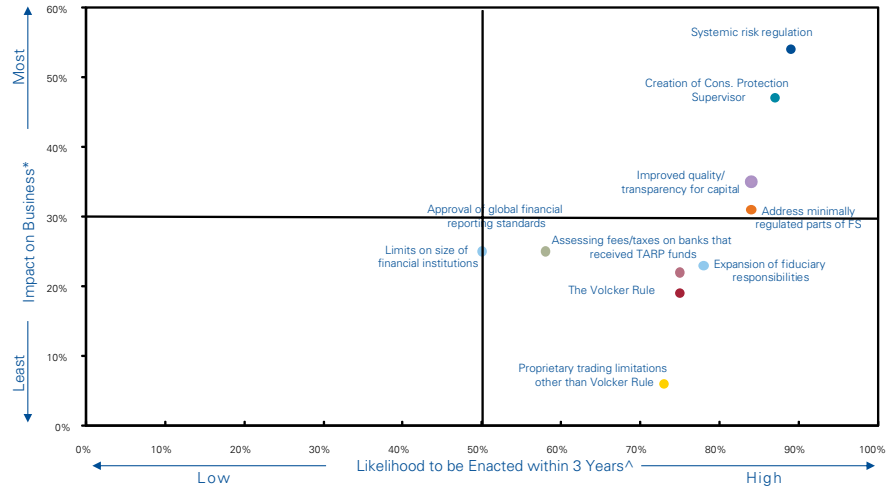
- Systemic risk regulation is the greatest concern. It is seen as most likely to be enacted and cited as likely to most impact their businesses if enacted.





- Other regulations of great concern are related to:
 - Creation of a consumer protection supervisor
 - Improved quality/transparency for capital
 - Addressing minimally regulated parts of financial services

Likelihood of Regulations Being Enacted vs. Impact on Business



Banking executives are more likely than other FS executives to feel that systemic risk regulations and the creation of a consumer protection supervisor will have the most impact on their businesses.

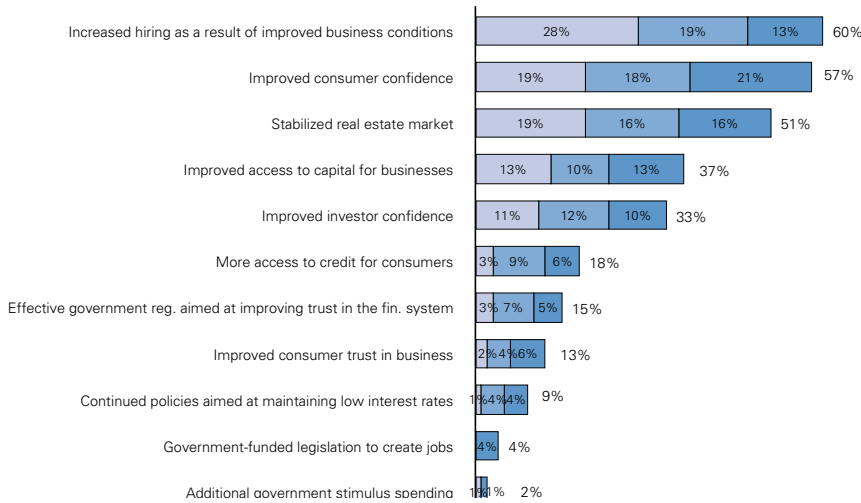
Banking/Financial Services Sector Growth Factors

According to sector executives, the top three most important triggers to accelerate recovery are:

- Increased hiring as a result of improved business conditions
- Improved consumer confidence
- Stabilized real estate market

Most Important Triggers to Accelerate Recovery

Among Total Finance



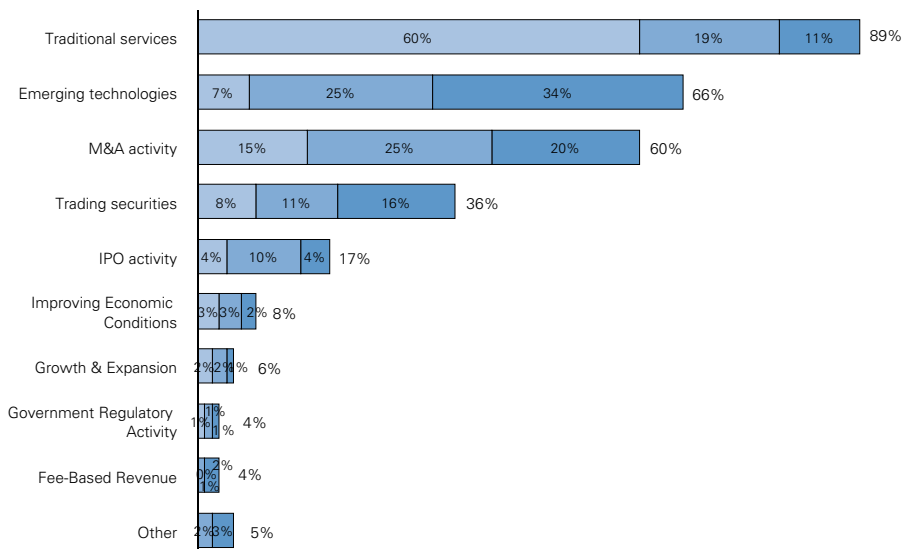
These three factors are especially important for banking executives. For other FS executives, a stabilized real estate market is less of a factor than improved investor confidence.

Respondents say the three biggest drivers of their company’s revenue growth over the next three years are:

- Traditional services
- Emerging technologies
- M&A activity

Biggest Drivers of Company’s Revenue Growth: Next 1–3 Years

Among Total Finance



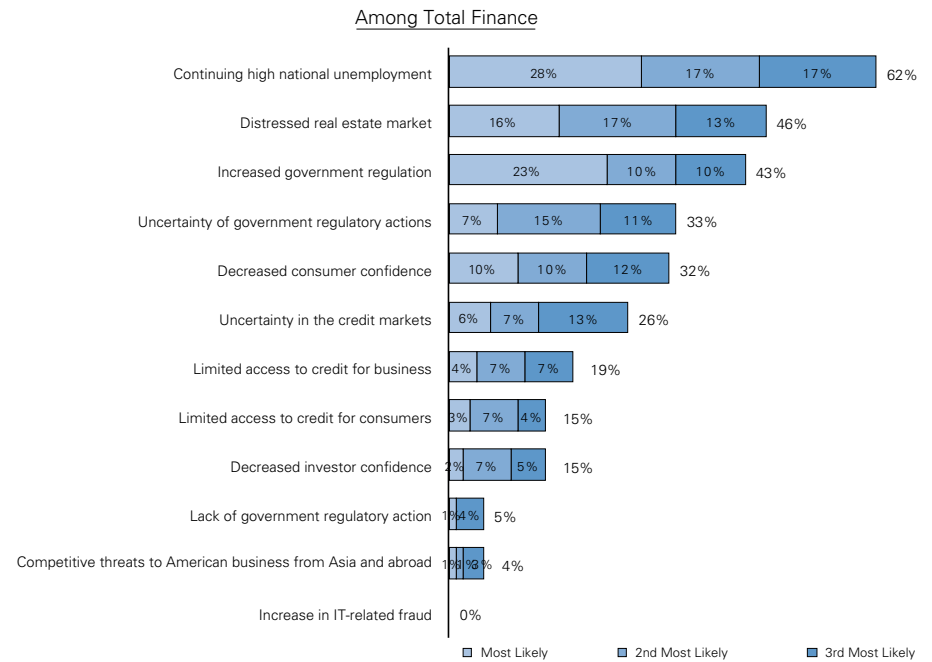


Banking/Financial Services Sector Limiting Factors

Sector executives say the top three factors most likely to hinder recovery are:

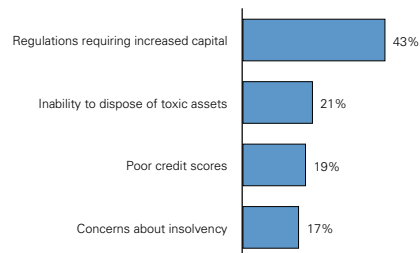
- Continued high national unemployment
- Distressed real estate market
- Increased government regulation

Factors Most Likely to Hinder Recovery



Respondents said the single greatest hindrance to lending in their sector is regulation requiring increased capital; 43% of all financial services sector interviewees, and 49% of those specifically from the banking industry gave this response.

Most Important Hindrance to Lending in the Financial Sector



Conclusion

Despite the uncertainties surrounding impending financial reform, banking and financial services executives are optimistic about their business prospects for 2010 and 2011. Many are investing for long-term growth and, specifically, are focused on traditional services, emerging technologies, and mergers and acquisitions as means to generate growth.

Financial regulation is expected to have a significant impact on the industry. While the impact will vary depending on the final form of legislation, it is likely to have sweeping implications—in areas including governance, risk, compliance, and capital—for financial institutions.

KPMG: A Leader in Serving the Financial Services Industry

While cautious optimism has returned to the financial services industry, the continued challenging environment requires that businesses adjust to and actively manage the changes impacting performance.

Having the right professional services firm—one with the industry depth, knowledge, and insight to help clients address their most pressing issues and achieve their goals—is critical.

For decades, KPMG's global Financial Services practice has been recognized for its presence in and commitment to the industry. Through our international network, we have the global reach and experience to serve clients anywhere in the world. Comprised of Banking and Finance, Insurance, Investment Management, and Real Estate, our Financial Services practice includes professionals with the knowledge, experience, and skills to help our clients address their most pressing challenges, sort through today's complex business problems, and achieve their goals.

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