Media release

Philipp Fanchini
Media Relations
Tel.: +41 (0) 58 286 36 26
philipp.fanchini@ch.ey.com

EY Banking Barometer 2023: Does the inflection point in interest rates mark a return to normality?

- **Remarkable resilience in a turbulent year for business in 2022**
- **Record 98% of banks expect positive business performance in the longer term due to the inflection point in interest rates**
- **In the short term, though, the inflection point in interest rates is dampening expectations: banks expect defaults on residential mortgages and SME loans**
- **Shortage of skilled staff: one in four banks see culture and leadership as the biggest challenge to attracting people**

Zurich, 10 January 2023 – Banks in Switzerland are going through a period of turning points and facing new challenges. 2022 was a year marked by geopolitical and global economic uncertainties. The optimism with which Swiss banks began the new calendar year after a fantastic 2021 proved to be short-lived as war broke out in Ukraine.

The survey results from the latest EY Banking Barometer indicate that the key issues for banks in the near future are the inflection point in interest rates, inflation, cutting costs, improving efficiency, providing customers with needs-based advice and sustainability. Alongside these challenges, there is also now a newcomer: the search for suitable employees. This is because banks, too, say they are now being hit by a shortage of skilled staff.

These are the findings of the annual EY Banking Barometer 2023. This is the 13th year assurance and advisory firm EY has conducted the study in Switzerland. A total of 100 banks in Switzerland were surveyed for the Banking Barometer in November 2022.

Remarkable resilience

2022 was an extremely turbulent year for business – the environment for Swiss banks was shaped by an outbreak of war on European soil, an energy crisis, a bear market, record inflation and an end to negative interest rates. Despite all the turbulence, Swiss banks remained very resilient. 78% of institutions surveyed saw a distinctly positive trend in operating profit for the financial year.

The share of institutions expecting operating profit to decline in 2022 amounted to 22% (compared with 13% the previous year). It is apparent that asset management banks in particular are now more cautious than they were a year ago as a result of the bear market.

Operating business: cautious about the short term, more positive than ever about the long term

The more defensive outlooks than last year are also reflected in banks' forecasts for the short-term future (one to two years). The short-term "optimism barometer" has fallen to just 78% (down from 87% the previous year). The share of banks expecting a negative business performance in the short term has almost doubled in a year from 13% to 22%. The uncertain environment is leading to gloomier business prospects, at least in the short term.

Taking a long view, however, the picture is completely different: banks in Switzerland are more optimistic about the longer-term future than ever before (a record figure of 98%, up from 86% the previous year). The main reason for this is the long anticipated inflection point in interest rates. "This inflection point allows banks to once again sustainably improve their margin in the key interest rate spread business. This will have many positive effects in the longer term, which will outweigh the short-term adaptation effects," says Patrick Schwaller, Managing Partner, Audit Financial Services at EY in Switzerland.

Inflation and rising interest rates increase credit risk (in the short term)

Banks do not expect inflation to vanish quickly. 74% of them think it will remain above the target of 2% per year for the next one to two years. So it comes as no surprise that there has been a radical shift from previous years in their view of what for them is the most challenging interest rate scenario. 37% identify rapidly rising interest rates as the greatest challenge (compared with 26% the previous year). This mainly applies to regional banks and cantonal banks. According to banks in Switzerland, rising rates are also likely to have an impact on the lending business: of the banks surveyed, 31% (compared with 12% a year earlier) assume impairments of residential mortgages will rise in the short term and 59% (compared with 36% the previous year) anticipate a need for substantially higher provisioning on SME loans. This is considerably more than last year.

“Ultimately, the expected rise in loan defaults should be seen as the turning point on the way back to normality for Swiss banking. Default risk is part of banking. The last few years were an exceptional situation when put in a historical context, driven by negative interest rates and government assistance to companies because of the coronavirus,” says Patrick Schwaller.

Structural change: technological innovation and needs-based customer advice

The latest Banking Barometer shows that Swiss banks see technological innovation as the primary driver of structural change (50%). For 49% of the banks surveyed, it is a change in customer expectations that is driving the transformation. “The banks have coped very well with regulatory changes and negative interest rates in the past few years. But for a sustainable improvement in their ability to generate value in future, greater customer focus is essential,” says Olaf Toepfer, Partner and Head of Banking & Capital Markets at EY in Switzerland.

As in previous years, banks are hoping to be able to grow by systematically tackling sales (45%), improving the customer experience (42%) and with better products (30%). Paradoxically, though, they do not see gaining a better understanding of customers as a priority. “Without a deeper understanding of customers, it will be virtually impossible to offer advice on their increasing needs and so boost customer loyalty and justify fees,” says Olaf Toepfer.

But it is possible to discern a turning point in banks’ attitude towards their fees: by contrast with previous years, only 2% say they plan to raise them (compared with 7% a year earlier).

Efficiency, costs and the effects of the shortage of skilled staff

Last year, 60% of banks said they wanted to concentrate on increasing income and innovation – the highest figure in the past six years. Here, too, a turning point has been reached: now, only 40% of the institutions surveyed say they want to prioritise growth and innovation. However, cost cutting and efficiency gains were up strongly this year, with 36% of banks naming it a focus issue (up from 19% last year). “Given the current economic and geopolitical uncertainties, the shift from a growth focus towards cost discipline and efficiency gains is not really surprising,” says Patrick Schwaller.

Banks in Switzerland are also under pressure when it comes to seeking suitable staff: the shortage of skilled workers is very apparent in the Swiss financial sector. HR activities featured in the survey for the first time this year and shot straight into the top ranks. Asked about the most important themes and activities, banks rate employee recruitment and employee development in places two and three – immediately after cybersecurity, which has been a major theme for years and topped the list for the sixth time in a row.

Enhancing attractiveness with an improved corporate culture

Asked what measures institutions can best use to combat the challenges of recruitment, 41% of those surveyed think the answer lies in aspects of company management. One in four banks named culture and leadership as the greatest challenge, with 16% saying it was strategy and purpose. 20% named developing and training staff and increasing their well-being. Monetary benefits were seen as the least significant (12%). “Banks in Switzerland see culture as a key value driver for recruiting and developing staff – but it takes time to change a culture permanently, and cannot be done at short notice with monetary elements,” says Isabelle Staiger, Partner, People and Workforce at EY in Switzerland.

Sustainability is becoming the industry standard

Taking sustainability aspects into account now seems to be a firm part of the investment business for Swiss banks. In 2022, 96% of banks said they already integrated sustainability in their investment advice or would do so in future. Only 4% of banks (down from 11% a year earlier) stated that they do not take account of sustainability aspects when providing investment advice. Sustainability also appears to be increasingly relevant for commercial lending. At 56% (compared with 46% the previous year), for the first time more than half of banks intend to integrate sustainability factors into their lending to commercial customers.

Despite the ongoing wave of regulation, only 34% of Swiss banks now feel that the status quo in terms of regulations governing sustainability is satisfactory (down from 40% the previous year). “Given the lack of comparability and differing interpretation and implementation from bank to bank, it comes as no surprise that banks are keen to see the existing regulations fleshed out further,” says Corina Grünenfelder, Lead Sustainable Finance Consulting for Financial Services at EY Switzerland.