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BANKING AND FINANCIAL SERVICES

A Look Ahead: Top 10 Trends for Banking M&A

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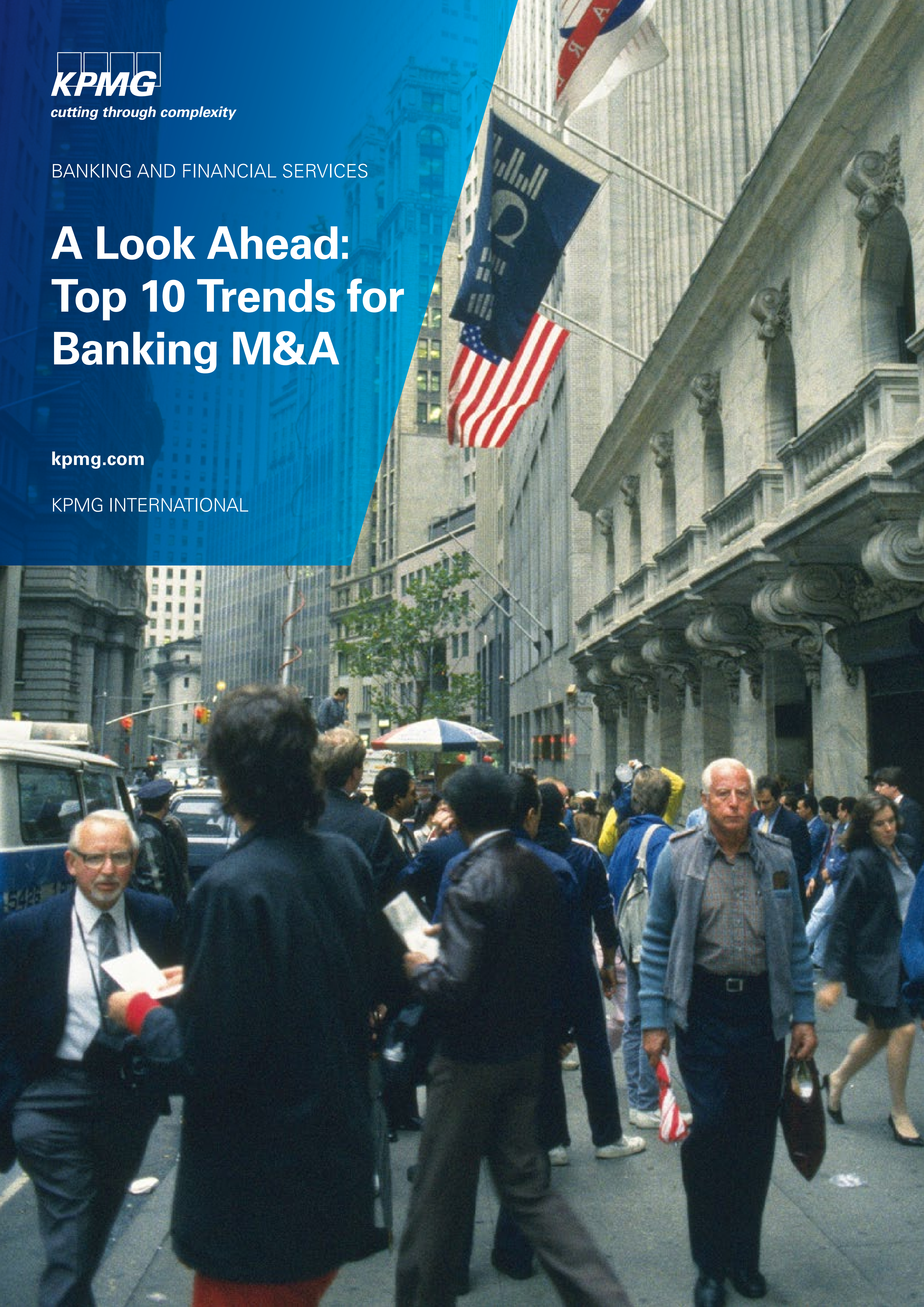

Foreword

Most readers would agree that 2014 was a turbulent year for financial services organizations and markets. Evolving regulatory requirements and scrutiny, new market entrants, changing market dynamics and massive restructurings were commonplace across the globe. And, as a result, 2014 also emerged as a banner year for Merger and Acquisition (M&A) activity.

Given that the pace of change is unlikely to slow any time soon, it is more critical than ever for financial services executives to understand the major trends now emerging and evolving around the world.

That is why, once again, we sat down with KPMG's network of deal-savvy financial services professionals around the world to pull together 10 predictions for what we believe will be the top trends for 2015.

I hope you enjoy the read and if you have any questions concerning these trends or needs arising from them, don't hesitate to contact me.

Stuart Robertson

Global Banking Deal Advisory Lead
KPMG in Switzerland

Did our 2014 predictions come to pass?

	Our M&A predictions for 2014
1	A wave of large Chinese cross-border deals
2	Tectonic shift
3	Empire building deals in Asia
4	The Japanese are back
5	Private Equity will spearhead the advance in shadow banking
6	Continued bear market in Europe and North America
7	From Palo Alto to Wall Street
8	The Asia growth dream
9	Rising losses will trigger portfolio sales
10	The global banking contraction will accelerate

- Prediction realized
- Prediction partially realized
- Prediction not yet realized

Source: KPMG's Global Banking Deal Advisory, 2014

Trend 1
Narrowing pricing gaps in Asia catalyze activity

All signs indicate that M&A activity will remain robust across Asia Pacific in 2015. Further consolidation is likely in many markets as banks look to reduce their costs for regulatory compliance and infrastructure while simultaneously maximizing the capital assets required to finance strong growth.

Overall, we expect activity will primarily focus on domestic rather than cross-border opportunities. As domestic institutions gain strength through consolidation, we may yet still see a regional mega-deal or two in Asia Pacific before the year is out.

This trend is illustrated in how China, as a High Growth Market, will continue to be a major outward investor through 2015. Sellers should be patient, however, as China's banks and investors will likely take a very measured and careful approach in order to ensure their activity remains consistent with their strategic objectives and any relevant stakeholder interests.

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Trend 2
Japan continues to look outward

As concerns mount over the strength of the domestic market, Japanese companies of all types are now looking overseas for new growth opportunities. And in their wake, we expect to see Japan's banks and other financial institutions, such as leasing companies, also continue to expand their overseas presence.

Some will be seeking to support the foreign ambitions of their existing corporate customers. Others will be looking to expand their customer base in overseas markets in order to offset fierce competition and declining demand for lending back home. In particular, we expect to see increased activity by Japanese banks in Southeast Asia, where demand and growth are significant; and in China, India and the US in order to tap into the world's largest financial market.

Having already met the latest global capital requirements, Japan's banks seem to be in a favorable position, as compared to their Western peers, to invest for growth. However, activity may be hampered in the short-term by heightened prices due to the depreciation of the Yen, increased competition in the domestic market and a lack of sufficient resources to properly manage overseas operations.

Trend 3
US activity remains robust

With the past year largely characterized by continued divestments of non-core operations and loss-making subsidiaries, we expect the overall US M&A market to strengthen further in 2015.

In part, this is driven by expectations for continued consolidation among smaller US banks seeking cost and scale efficiencies, as well as ongoing divestitures of businesses and portfolios by larger banks, insurers and non-US financial services companies. In particular, there are expectations for the sale of some banking subsidiaries owned by insurance holding companies.

While activity among the larger banking institutions remains somewhat muted, we expect to see increased deal-making in the investment management sector as buoyant stock market levels help bridge the gap between buyers and sellers. Continued interest from Private Equity – especially in niche markets – is also expected to drive activity over 2015.

The US financial technology market should also see significant M&A activity over the coming year as organizations look for solutions to growing challenges such as regulatory reporting, aging legacy systems and highly fragmented markets (*see Trend 10 for more on this*).

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Trend 4
Focus shifts south

As competition for deals heats up in Asia, many global institutions are now starting to shift their long-term growth lens towards potential new markets to the south.

Africa, in particular, is moving onto the growth agenda. And while few yet seem to have the risk appetite, budget or management resources to execute an Africa strategy this year, we have seen a small number of institutions and PE houses start to take early investment opportunities in the more mature African markets in order to gain first-mover advantage and much-needed experience operating in Africa. A number of global institutions continue to look to Africa to acquire new technology and business models, particularly mobile, for deployment in other markets.

Deal-making in Latin America should also be fairly active, but will largely be dominated by incumbents seeking to consolidate and expand their footprints. Given the strength of these incumbents and the significant diversity and complexity of Latin American markets, we expect to see muted activity by new players seeking to enter the market.

In both Africa and Latin America, as well as many other developing and emerging markets, micro-finance and so-called 'impact investing' will continue to increase in prominence but – for the near-term – will have little impact on deal-making in these markets.

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Trend 5

M&A drives growth for stronger institutions

Following years of asset disposals, reorganizations and cost reductions aimed at shoring up capital, many of the world's stronger banks are now starting to focus on improving the historically-low returns they receive on their equity. This drive for profitable growth is once again pushing M&A to the top of the agenda. Public statements by some of Europe's leading banks suggest that some are prepared to take radical measures to increase ROE and meet regulator demands.

In 2015, we expect to see banks continue to conduct strategic exits, wind-downs and outsourcing deals while, simultaneously, refreshing their regional business footprints and bolstering their core businesses through acquisitions. Given that M&A activity was up 11.8 percent in volume and 12.3 percent in value in 2014, it seems clear that many banks have already started to step up their deal-making activity.

Activity has been buoyant in several countries, including the UK and France, though some attribute this more to a 'sell now while the going is good' attitude than the presence of real value opportunities. Italy and Germany, however, are viewed as the markets with the lowest levels of concentration in Europe and more consolidation should be expected over the next year.

The not unencouraging results that came out of the European Central Bank's Asset Quality Review last year (where just 25 of the 130 banks under review showed potential capital shortfalls) offers additional confidence to the market. As such, we expect this perceptible change of tone at banks to continue as executives and shareholders start to refocus their attention back onto growth.

Trend 6
Funds activity heats up

As wealth and asset managers, alternative fund managers and institutional investors (pension and sovereign funds primarily) start to look for growth through scale and diversification, we expect to see significant consolidation in the Investment Management sector through 2015. The continued shift of power towards distributors is also driving asset managers to seek out assets with attractive client bases and distribution channels.

Over the past year, we have increasingly seen activity pivot from investment banks to alternatives and would therefore expect growing interest in bank channels, either as potential targets or as joint ventures and long-term distribution partners.

At the same time, the shift towards 'outcome-orientated' services in it's place is expected to lead to increased activity as managers look to improve their capability and product offering through both organic and inorganic growth. We expect to see particular interest in both alternative and real assets in Europe and Asia as managers expand their portfolios to support multi-asset propositions.

As the complexity and cost of asset management increases, we also expect to see an increase in transactions, joint ventures and technology partnerships as smaller managers take advantage of synergies and build their internal capabilities.

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Trend 7
Continued restructuring and loan sale activity

While the results of the ECB's Asset Quality Review were generally positive, the exercise did uncover a higher-than-expected overhang of non-performing and non-core portfolios across most of Europe. This, combined with low levels of profitability and low-margin legacy portfolios will likely provide a strong foundation for further M&A activity in the region.

We expect non-core and non-performing portfolio sales to remain robust over the next 12 to 24 months, albeit with a shift away from the UK and Ireland and towards Southern Europe. In particular, real estate loan portfolio sales by Spain's bad bank (SAREB) should continue to attract significant investor interest. We also note that consumer finance is increasingly being hived off by the banks and managed by new entrants into the market.

Increasing portfolios of non-performing assets will also drive activity in the emerging markets. China is expected to increase the number of regional asset management companies active in the local market with many of the national asset management companies now looking at listing on public exchanges in order to attract outside capital. The build-up of non-performing assets in India – coupled with recent regulatory changes – should also become an increasing area of focus for investors and Private Equity houses.

Trend 8
Bancassurance shifts to high growth markets

While the bancassurance market in Europe is largely dormant outside of France, banks and insurers in the emerging markets of Africa and Latin America are increasingly looking to develop mutual distribution channels to expand their reach and reduce their infrastructure costs. And while – even in the high growth markets – there seems to be little appetite for forming combined banking and insurance groups, we expect to see more institutions start to engage in partnerships and distribution agreements.

Similarly, Western banks and those in the more mature Asian markets will continue to accelerate their divestment of non-core insurance businesses in favor of less restrictive distribution agreements. So while we expect bancassurance to continue to play an important role in developing markets, we believe that third-party distribution agreements will continue to be the preferred approach in most markets.

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Trend 9
Private Equity goes on the hunt

As global Private Equity (PE) and Venture Capital (VC) houses start to focus more clearly on financial and business services, we have seen increasing interest and activity across a number of markets. Indeed, alongside their continued interest in EBITDA and balance sheet businesses, many PE and VC houses now include special situation teams in parallel funds roaming across Europe looking for value opportunities from deleveraging banks.

In particular, competition is heating up for underperforming divisions within large financial institutions that can be acquired, re-capitalized and propelled to the 'next level'. We expect to see activity around new divestments in both the UK and Spain, as well as Italy where opportunities should significantly increase over the next year. As noted in Trend 10, PE houses have also demonstrated significant interest in acquiring platforms for growth and organizations with technology-led business models.

PE and VC managers may also start to see new opportunities emerge from the more regulated end of the market as regulator attitudes towards non-traditional owners of financial services organizations starts to move in a more positive direction.

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Trend 10
Competition rises for Financial Technology

Technology and digital channels are widely seen as a key enabler of the growth agenda for financial services organizations around the world. At the same time, new approaches and technologies – such as Data and Analytics – are rapidly emerging to help banks reduce their risk, improve their performance and enhance their growth.

Not surprisingly, therefore, we have seen increasing interest and deal-making activity in the Financial Technology sector as banks decided whether to build or buy solutions. PE and VC houses have been especially voracious for deals, particularly in areas where technology is disrupting traditional business models or where there is a strong outsourcing opportunity. PE/VC investment in Financial Technology was estimated to have reached almost US$7 billion in 2014.

For their part, banks are also investing in Financial Technology companies, but often taking only a minority stake as a way to gain access to new technologies and the wider Financial Technology ecosystem. This trend will continue in 2015 with some investments being made through captive venture funds or corporate venturing programs. Beyond this, we also expect more variety in how banks engage with external innovators, and with each other, to collaborate and architect new solutions – alliances, consortia, joint ventures and licensing agreements are just some examples of more formalized arrangements.

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To help ensure the highest level of support to satisfy KPMG member firms clients' M&A planning and execution requirements, we have established an integrated global network of multidisciplinary M&A professionals focused on the banking sector.

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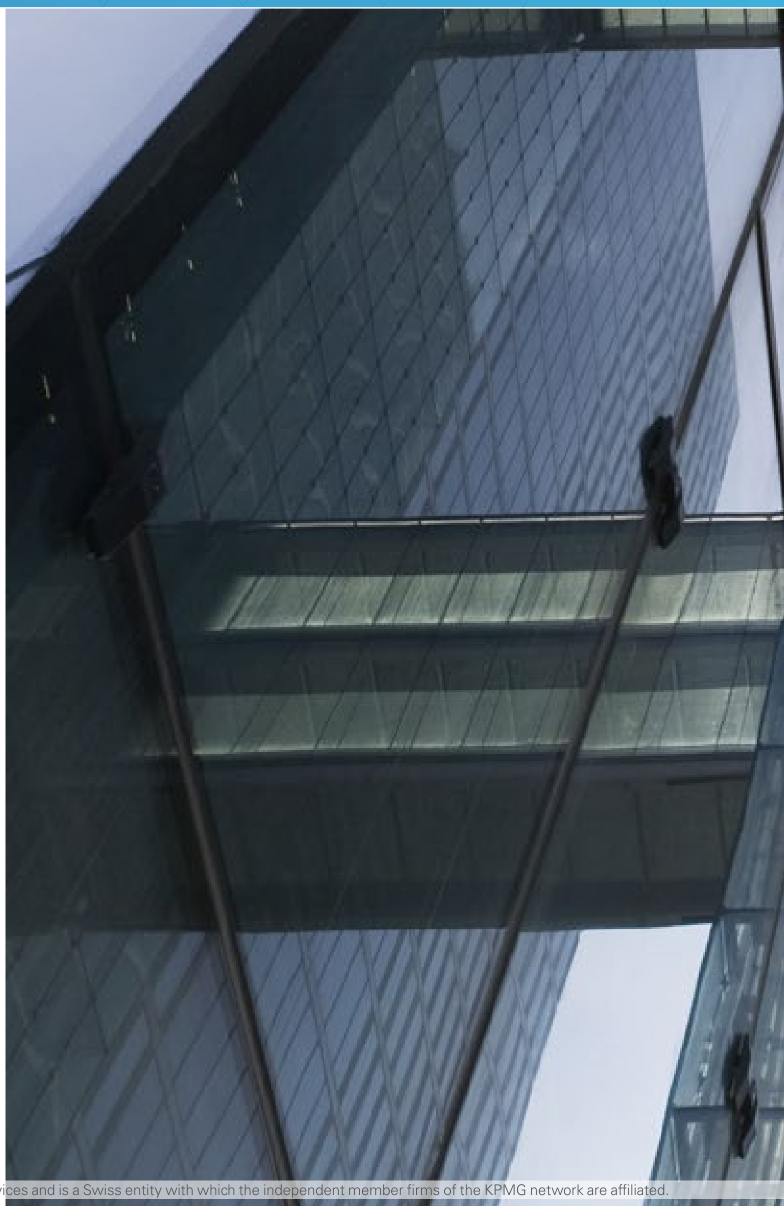
The result is an impressive track-record of M&A deal support and a roster of leading global banks who have turned to us to help ensure their transaction ambitions and activities achieve their strategic business objectives.



Our network of member firms across the world can help you meet your growth objectives:

- achieve corporate growth, realize synergy potential and profit objectives
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- release capital and enhance liquidity from sale of core or non-core businesses
- restructure or wind down of non-core businesses
- implement an optimal separation plan
- tailor M&A advice to ensure a successful outcome when assessing opportunities
- identify a wide pool of potential opportunities in your core markets
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- design and execute an effective post deal integration plan
- establish or enhance your joint venture, including structuring, maximizing protection and improving operating effectiveness.

KPMG's Deal Advisory practice, comprises M&A, debt advisory, valuations, transaction services, strategy and restructuring services.

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