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Swiss Financial Center 2018

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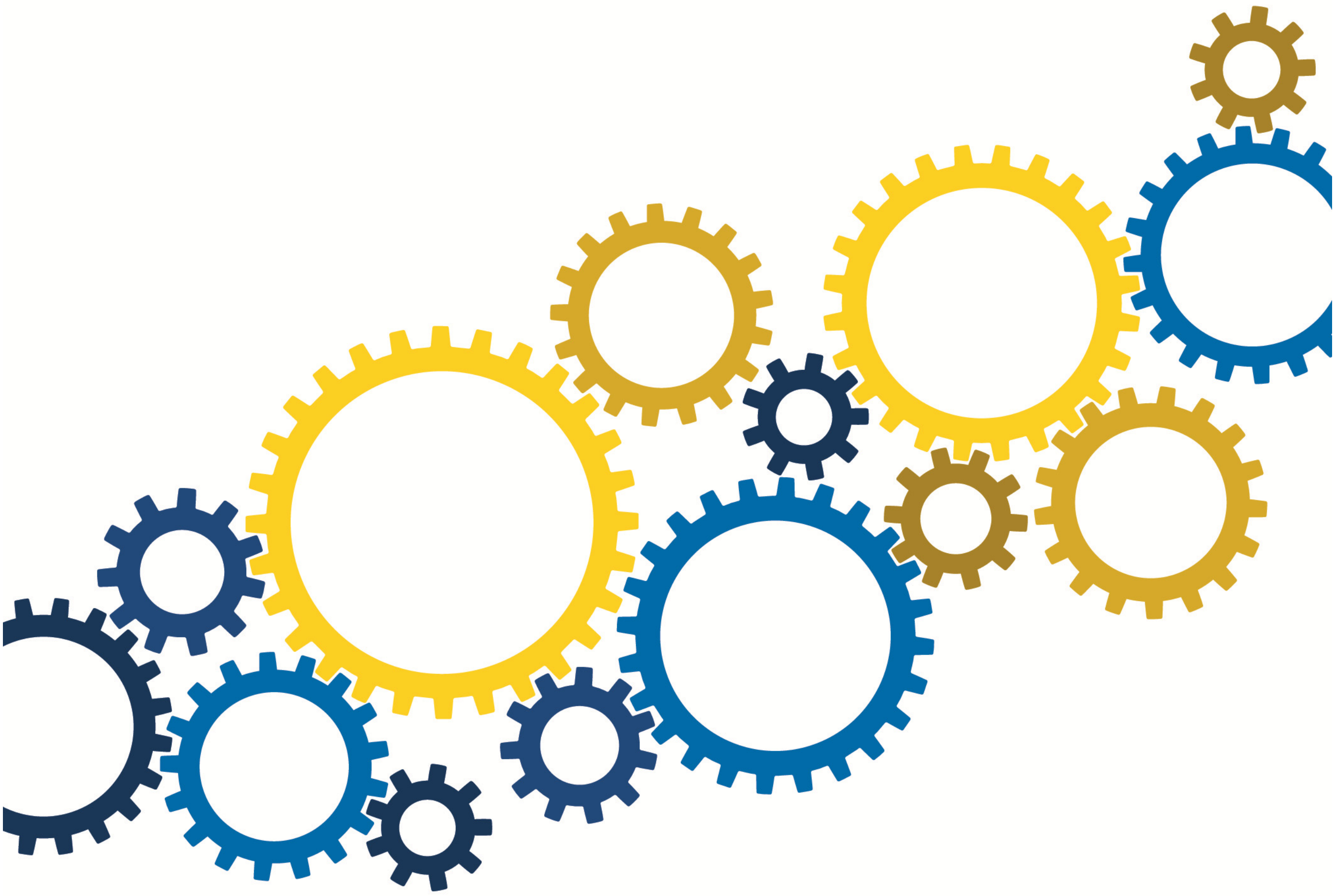
From crisis to growth



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Foreward

Dear readers

We are this year once again publishing a study on the Swiss financial center as we have been doing every two years since 2012. As with our previous publications, our aim is to provide a constructive contribution to the discussion as well as specific proposals as to how the various relevant actors can jointly support the competitiveness of this sector of the economy which is so important for the prosperity of our country, and to further promote it as far as possible.

As in the previous years, we do this by illustrating the key macroeconomic developments and trends and explaining how they affect the institutions active in the Swiss financial center. The recent past has generally proven relatively difficult from a macroeconomic perspective for the financial center. The problem areas primarily include the low interest environment that has been in place for several years and is exerting a significant impact on the core business of the banks. However, this also means that the margins should improve once monetary policy has normalized again. Furthermore, the profitability of financial institutions has been impaired by the wave of regulation in the wake of the financial crisis. The low interest rates in combination with demographic trends also pose a challenge to Swiss pension funds. Our publication therefore for the first time devotes a chapter to the theme of pensions.

The success factors addressed by us and the recommendations derived from them, which we once again subdivide into suggestions for the government, parliament and supervisory authorities on the one hand and those for banks and the rest of the economy on the other, focus on the following topics:

- Improved regulatory processes and implementation of international standards
- Market access, particularly to the key market of the European Union (EU)
- Sustainable finance
- Fintech/digitalization and innovation
- Changes to the Swiss pension system

We hope that this latest study contributes to and provides food for thought regarding the dialogue about Switzerland's locational attractiveness and the competitiveness of its financial center. We look forward to discussing these issues with you.

Yours sincerely
Urs Rohner
Chairman of the Board of Directors
Credit Suisse Group AG

Summary of recommendations by stakeholder group

	Preserve general locational attractiveness	Improved regulatory processes and implementation of international standards	Safeguarding and improvement of market access	Using sustainable finance as an opportunity	Fintech/digitalization and innovation	Changes to the Swiss pension system
Government, parliament and supervisory authorities	• Legal and planning security. • Moderate regulation, observance of economic freedom. • Fiscal attractiveness for natural persons and legal entities (Tax Proposal 17). • Liberal labor law. • Modern and efficient infrastructure. • Close collaboration between universities and the private sector.	• Top-down regulatory process with clear responsibilities for financial market policy by the Federal Council and operational supervisory activities by the FINMA. • Stronger weighting of competitiveness as FINMA target. • Monitoring of regulatory activities of the FINMA by the Federal Council and parliament while upholding the independence of the FINMA. • Consistent implementation of global standards in terms of time and content with the involvement of the Federal Department of Finance.	• Clarification of relationship with the EU through resolving institutional issues. • Initial search with the UK for possibilities to preserve the status quo followed by improvement of market access. • Improvement of bilateral market access to central core markets by means of agreements. • Agreement with the EU with focus on processes for recognition of equivalence. • Safeguarding and expansion of market access to EU/EEA single market in the medium to long term.	• Supporting international developments abroad and promoting voluntary activities of industry at home. • Supporting Swiss industry representatives to help develop these standards at an international level. • Avoiding Swiss special solutions for standards, labels and certifications for sustainable investment or reporting. • Implementing recommendations at federally owned institutions (e.g. public retirement benefits institutions). • Providing platforms for the exchange of knowledge.	• Upholding of competitive neutrality through technology-neutral regulation. • Upholding of integrity and reputation of the financial center with regard to cryptocurrencies and initial coin offerings (ICOs). • Safeguarding of Swiss data protection legislation equivalent to the EU data protection package. • Swift ratification of the E-ID Act by parliament and broad acceptance of E-ID in communications with authorities.	• Long-term safeguarding of Swiss pension funds. • Ilnclusion of new, flexible work models. • Addressing of gaps in private pension provision and identification of adequate solutions. • Expansion of pillar 3a through buy-in option and increase in tax deduction opportunities. • Promotion of sustainable investment models for pension funds. • Flexible design of 1e pension solutions.
Banks and economy	• Contribution to availability of skilled labor, among other things through corresponding investments in education and training. • Adequate contribution to availability of growth capital for the Swiss economy. • Close collaboration of businesses with universities. • Contribution to promotion of financial literacy of the Swiss population.	• Greater involvement in the medium to long-term prioritization of regulatory initiatives through participation on committees for the regular exchange of dialog between private-sector players and authorities. • Inclusion of the sector in defining Switzerland's positions on international standard setting bodies.	• Active assistance in the search for solutions within the scope of the envisaged bodies. • Development of measures for resolving market access issues. • Early identification of market access obstacles.	• Utilizing international developments and helping to shape these wherever possible. • Systematically picking up client interest in sustainable investments through dialog and addressing corresponding opportunities and risks. • Sensitization and regular training sessions for relationship managers. • Addressing therecommendations of the FSB Task Force on Climate-related Financial Disclosures.	• Promotion of innovation and use of new technologies within own company and in collaboration with other companies. • Safeguarding of the financing of new and innovative Fintech enterprises and mentoring of start-ups. • Provision of user-friendly E-ID for private individuals and swift and broad acceptance of E-ID in business transactions.	• Provision of new mortgage models and flexible investment solutions after retirement. • Implementation of new indirect repayment models through pillar 2 extra-mandatory occupational benefits provision. • Provision of well diversified, simple and cost-efficient investment solutions under OPO 2 for all investment horizons. • Support and broad-based launch of 1e pension solutions. • Training of pension fund beneficiaries across all generations.

Source: Credit Suisse

Review

A challenging decade

Since the financial crisis, the Swiss financial center has been confronted with multiple challenges that have weighed on the value creation of most sub-sectors. However, the transformation of the sector has progressed a long way.

Swiss financial sector has seen significant consolidation since the financial crisis

Over the last decade, the Swiss financial industry went through a succession of challenges which triggered a profound transformation of the sector. Due to the pressures on the sector its contribution to Swiss gross domestic product (GDP) declined to around 9% from more than 11% at the height of the global financial boom. Employment in the sector has stagnated since 2009 at around 215'000 full-time equivalents; job losses in banks were compensated by activities auxiliary to financial services. Moreover, the number of banks operating in Switzerland declined from 330 in 2007 to 261 in 2016. Foreign banks significantly reduced their footprint in the Swiss market. In parallel, mergers and acquisitions of (usually smaller) Swiss institutes by larger banks also contributed to the consolidation process and the reduction in number.

Write-offs, higher funding costs...

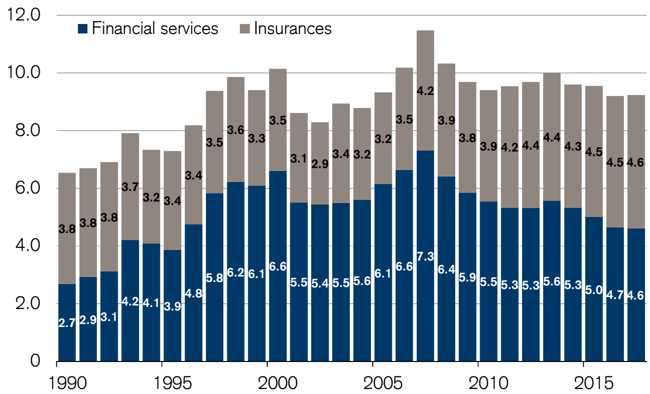
Multiple factors have weighed on the performance of the Swiss financial sector. Firstly, the two big banks had to recognize significant losses on assets which were acquired before the crisis. Second, funding costs rose sharply in the immediate aftermath of the crisis and only began to subside with a time-lag as balance sheets were reduced and equity positions strengthened. Third, international political pressure and the transition to tax transparency led to asset outflows in international wealth management centers, including Switzerland and Luxembourg. Fourth, many Swiss banks bore substantial costs related to the settlement of litigation cases. Fifth, new regulation has forced banks to raise capital from more expensive funding sources, while requiring heightened capital allocations for certain assets, including via the so-called countercyclical capital buffer. Looking forward, although capital costs have subsided, the expected return on each unit of capital is still likely to remain lower than before the financial crisis. At the same time, the strengthened resilience of banks should benefit their position in off-balance sheet activities, especially private banking.

... and the extreme interest rate environment reduced profitability

On top of these pressures, the significant global decline in interest rates, which was further promulgated by exceptionally loose monetary policy globally, reduced the profitability of traditional lending activities, and challenged life insurers as well as private and state pension systems. In Switzerland, negative interest rates have posed a particular challenge to retail banks, although the exemptions granted by the Swiss National Bank (SNB) dampened the negative effects.

Lower GDP contribution of financial services post crisis

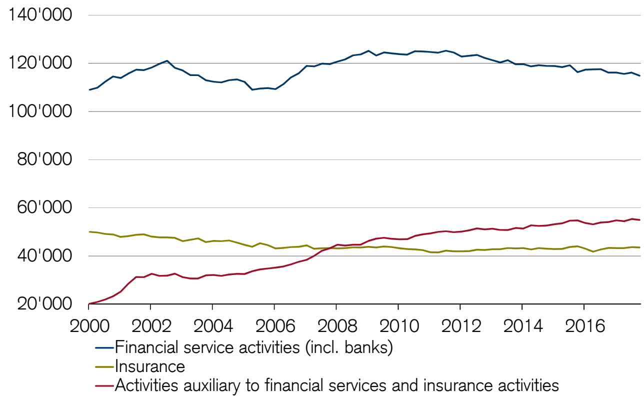
Contribution in % of nominal GDP



Source: SECO, Credit Suisse

Employment fell in banks

Employment in finance and assurance, in full-time equivalent



Source: Federal Statistical Office, Credit Suisse

While lower interest rate stimulated the demand for mortgages and mortgage volumes expanded significantly since the crisis, the profitability in retail banking suffered; net interest income in percent of total assets declined markedly. The contribution of domestically oriented retail banks to GDP was more resilient as a result of the expansion in lending, however possibly at the cost of taking on higher risks.

The insurance sector fared better, but low interest rates affected life insurances

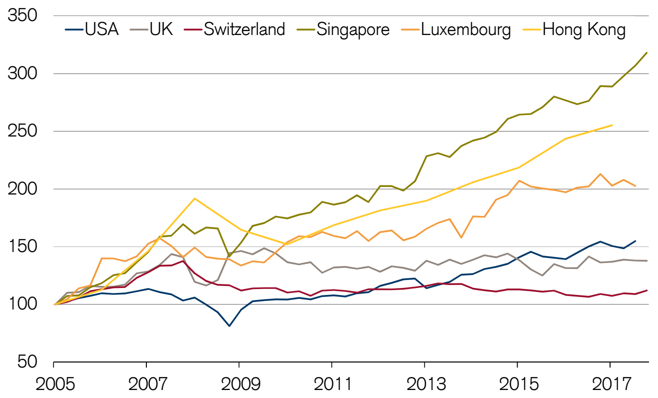
Meanwhile, the Swiss insurance industry which was affected much less by the financial crisis saw its contribution to economic output increasing. This was driven entirely by the non-life and reinsurance businesses, while life insurances saw their contribution to value added declining (see p. 9). This was also in large part due the trend decline in interest rates, which rendered life insurance products less attractive and in part forced companies to retrench from certain activities. In addition, capital requirements for Swiss insurance companies rose as a result of the Swiss Solvency Test (SST) which came into force in 2011. This regulation which is in part stricter than requirements for EU insurance companies also affected life insurance more than other areas of the sector.

Swiss financial center lagged international competitors

Not only has the financial industry lagged Swiss economic growth, but its performance has also been weaker than other international competitors. Not surprisingly, the Asian financial centers have expanded solidly, benefiting from rapid wealth creation in the region. In Europe, the Luxembourg financial sector has also grown strongly, driven by the substantial increase of its funds management business and the solid performance of the insurance sector. On the other hand, the British financial sector has stagnated due to a combination of the problems of domestic banks and the consolidation in global investment banking. Lastly, US banks, insurance companies and fund managers have performed well. They benefited from the decisive support of the US government during the financial crisis as well as from the strong domestic economic recovery.

The Swiss financial sector has been lagging its peers

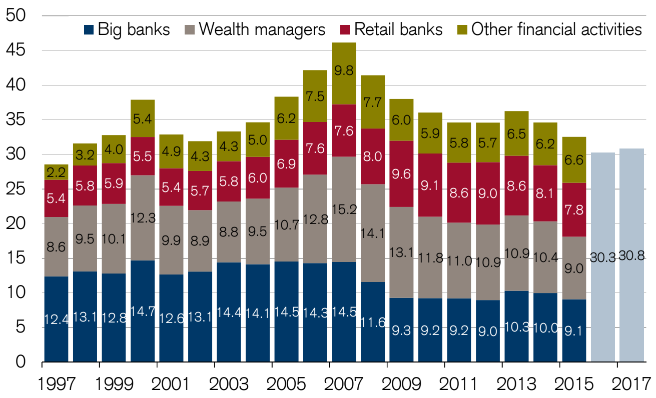
Nominal gross value added (Q1 2005 = 100)



Source: Datastream, National statistical offices, Credit Suisse

Most bank segments have been under pressure

Nominal gross value added of banks, by category (CHF, bn)



Source: Federal Statistical Office, SECO, Credit Suisse. 2016/17: data by category not yet available

The wave of regulation is leaving its mark on the mix of employees

Owing to public pressure and the tightening of regulatory measures resulting from the financial crisis, many financial institutions have had to create additional control mechanisms that have generated correspondingly high demand for staff in the legal and compliance departments and in risk management. The consequences of the wave of regulation over the last ten years are also reflected in the fact that, for example, considerably more lawyers are today working at banks and other financial institutions in order to implement the prescribed legal guidelines internally and monitor their compliance. According to official figures, the share of employees in the entire financial sector dealing with regulatory tasks amounted to around 5% in 2016. This is up from just 3% in 2010 and a mere 2% in 2000. However, this share will be significantly higher again in the banking sector for two reasons: Firstly the financial sector also includes enterprises such as health insurance and (state) accident insurance providers and pension funds that were significantly less affected by new regulatory measures compared with the banking sector, and secondly external consulting companies are often also deployed for the implementation of new regulatory guidelines. However, their employees are not included in the employment statistics of banks.

Looking to the future, a flattening or even reversal of this trend is to be expected as once the new regulations and compliance standards have been introduced, it should increasingly be possible to guarantee their regular application with digital solutions. The ongoing digitalization of various processing operations in the financial center should also lead to a decreased outsourcing of jobs to low-wage countries. The digital bank can furthermore be supported by native robots. However, the general trend toward the creation of IT-affine workforces within and outside financial institutions will barely be over yet.

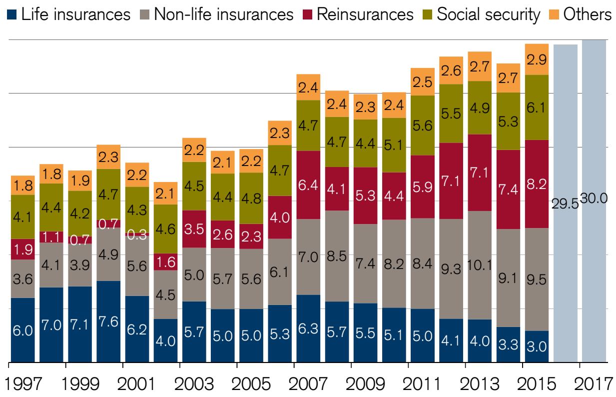
Focus on insurers

Gross value added of insurers

The gross value added of insurers has expanded at more or less the same rate as nominal GDP. However, within the sector, the growth rate varied significantly across sub-sectors. The gross value added of life insurers has declined substantially. The low yield environment has reduced the attractiveness of life insurances and the profitability of the sector. On the other hand, non-life insurers and reinsurers have significantly increased their gross value added. Non-life insurers have benefited from rising household incomes which boost demand for insurance. Demand for reinsurance has been on a rising trend ever since the terrorist attacks of 2001.

Solid expansion of reinsurance

Nominal gross value added of insurers, by category (CHF, bn)



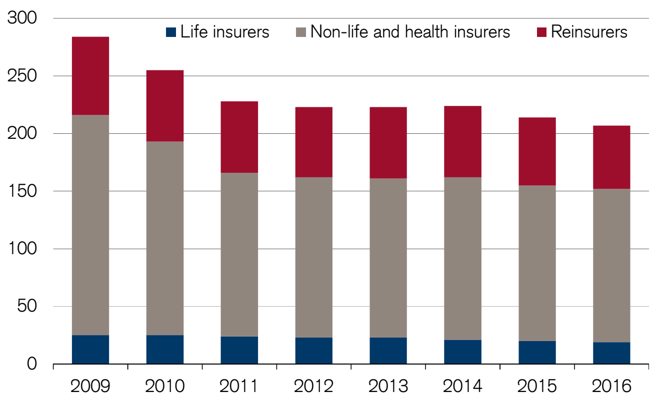
Source: Federal Statistical Office, SECO, Credit Suisse. 2016/17: data by category not yet available.

Number of insurers

The number of Swiss insurance companies has declined over the last few years, reflecting the consolidation in the sector. As a result of higher concentration and more efficiency, the gross value added of the insurance sector has risen. The sector has become one of the most productive in Switzerland. In 2015, each employee in the insurance sector (in full-time equivalent) generated almost CHF 390'000 (gross value added). In comparison, each employee in the banking sector created CHF 224'000 of value added.

Consolidation in the insurance sector

Number of insurance companies, by category



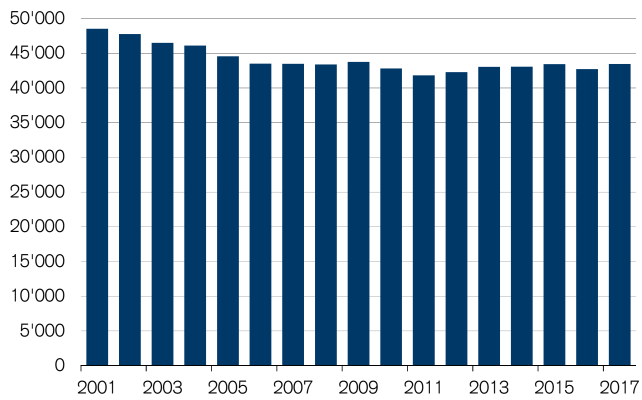
Source: FINMA, Credit Suisse

Employment in insurance sector

Over the last few years, insurer employment remained stable thus growing, at a slower rate than the rest of the economy. In 2017, employment in the insurance sector represented 43'400 full-time equivalents or 1.1% of total employment in Switzerland. Efficiency measures and digitization most likely will limit employment growth in years to come.

Employment has been stable in insurance sector

Employment in insurance sector, in full-time equivalent



Source: Federal Statistical Office, Credit Suisse

Outlook

Back to moderate growth

Barring a renewed economic crisis, most areas of banking are likely to return to a growth mode. Still, low interest rates and moderate growth in Switzerland and neighboring Europe is likely to limit bank revenues. Economic developments in the USA and emerging markets growth will continue to drive internationally oriented banks.

Over the short-term, low interest rates will likely remain a key challenge for domestically oriented banks

For domestically oriented banks, which are heavily dependent on net revenues from interest operations, i.e. the difference between interest received on lending activities and interest paid on clients' deposits, the short-term outlook is challenging. As long as the Swiss National Bank (SNB) keeps its policy rate in negative territory – a situation we expect to continue for around another two years – there is little scope for the liability margin (i.e. the margin on banks' deposit business) to widen. Banks have so far been cautious in passing on negative rates to clients, which has depressed their liability margin. In parallel, while the asset margin (i.e. the margin on banks' lending business) first widened after the introduction of the negative interest rate in January 2015, it has narrowed more recently. This may, in part, be due to some competition e.g. in mortgage lending from non-banks including pension funds and life insurance companies, as well as some direct lending by other companies with large cash positions; there have also been reports of limited and small-scale lending at negative rates by "Fintechs".

Margins would increase moderately if interest rates rise

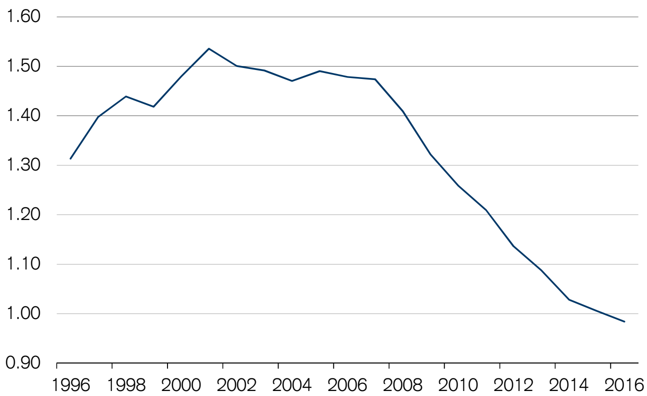
Over the short-term, we expect the margin on traditional borrowing and lending business of domestically oriented banks to remain at about the current low level (see chart). Under our base case that interest rates rise moderately and the yield curve steepens gradually, the margin on interest operations should eventually recover to some extent. However, our estimates suggest that both these developments would improve the margin only moderately. While positive short-term interest rates would help improve the liability margin, there is also a risk that the asset margin will narrow back to levels seen before the introduction of the negative interest rate. For the two big banks, the situation with regard to net interest income is much more difficult to assess. Their balance sheets are more diversified and their interest income is in part dependent on other currencies.

A sharp increase in interest rates would pose the risk of heightened mortgage delinquencies

Despite the drop in their margin, domestically oriented banks have maintained their overall profits, as credit volume has expanded solidly, driven by mortgages (see chart). However, mortgage growth is likely to be slower than it has been in the recent past. First, tighter regulatory requirements, higher real estate prices and (eventually) higher interest rates should reduce demand. Second, we believe that the real estate cycle has peaked in Switzerland, which should further reduce the growth of demand for mortgages. Still, a rise in interest rates would entail risks for

Banks' margins on interest operations have declined

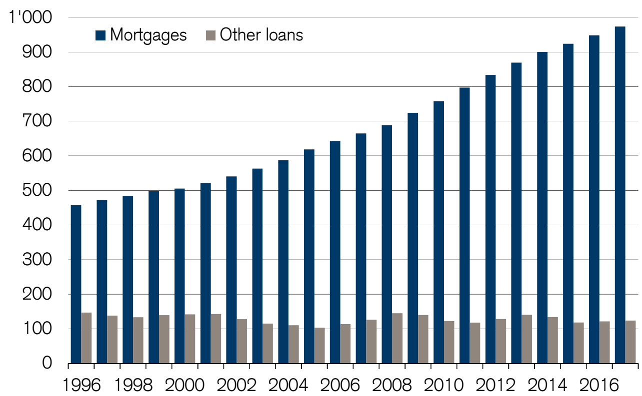
Domestic banks' net interest income as % of total assets



Source: SNB, Credit Suisse

Mortgage growth has been much more dynamic

Domestic credits in CHF to households and corporates



Source: SNB, Credit Suisse

banks, especially if it were significant. If coupled with an economic downturn, delinquencies would likely rise and would need to be reserved for. However, as long as interest rates do not rise all-too sharply or immigration drop off precipitously – both of which we regard as unlikely – this risk seems limited. In addition, the effects would be delayed because 80% of mortgages are at fixed interest rates. Lastly, the SNB would most likely loosen capital requirements for banks in such a case by means of a lowering of the countercyclical capital buffer, which would reduce pressure to call in loans and would thus reduce the risk of a broader credit crunch.

Corporate credit growth is likely to be slow, but delinquencies very low

With the exception of mortgage credits, credit demand from corporates has been subdued for the last decade and despite record low interest rates. Demand was probably low due to the uncertain economic outlook in the aftermath of the global financial crisis and later the euro crisis. Moreover, corporates have relatively high cash positions, further reducing the need for external funding. Therefore, and despite the much more positive economic outlook, we expect stable but weak credit demand from corporates. While this reduces growth opportunities for banks it also suggests that corporate credit delinquencies will remain very low for the foreseeable future.

Downside pressure on wealth management margins should subside

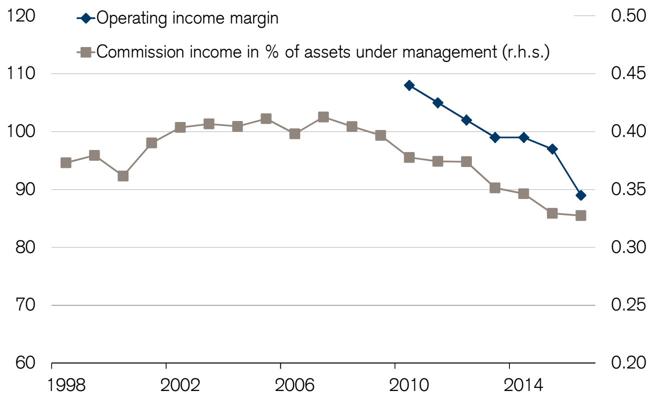
In the wealth management business, margins have declined substantially since the financial crisis (see chart). In the onshore area, heightened competition and regulatory rules have squeezed margins. The lack of trading activity of private clients in the aftermath of the financial crisis likely added to the downside pressure. Broadly speaking, margins in the institutional business are already extremely tight and thus unlikely to decline further. In private banking, intense competition and the further spread of low cost and de facto institutional products such as index funds will tend to further depress margins, while efficiency gains and the regulatory need for advice implemented by the "pay for advice" models should support them. In general, we believe that the downward adjustment of margins should be far slower in future and we might even see a stabilization.

International wealth managed in Switzerland is expected to grow by 3% to 4% p.a.

Meanwhile, assets under management (AuM) have grown substantially since the global financial crisis and despite the outflows related to regularization. We estimate AuM with banks in Switzerland at CHF 6 trn at the end of 2017 (see chart), although we reckon that such estimates depend significantly on what is included under AuM. We further estimate that 46% (CHF 2.7 trn) of AuM are international wealth, i.e. wealth owned by investors domiciled outside of Switzerland. The Boston Consulting Group (BCG), a consultancy, expects international wealth booked in Switzerland to grow by 3% to 4% p.a. until 2021. International wealth managed in Switzerland would thus rise to between CHF 2.9 trn and CHF 3.1 trn over the next 3 years. Over the last 15 years, growth in international wealth has largely come from institutional clients. Back in 2001, international wealth of institutional clients represented only 30% of total international wealth managed by banks in Switzerland. By the end of 2017, this share had climbed to 75%, on our estimates. Conversely, funds of international private clients have declined. As noted above, the increasing weight of institutional clients has been one of the contributors to erosion of margins.

The margin of wealth managers has dropped

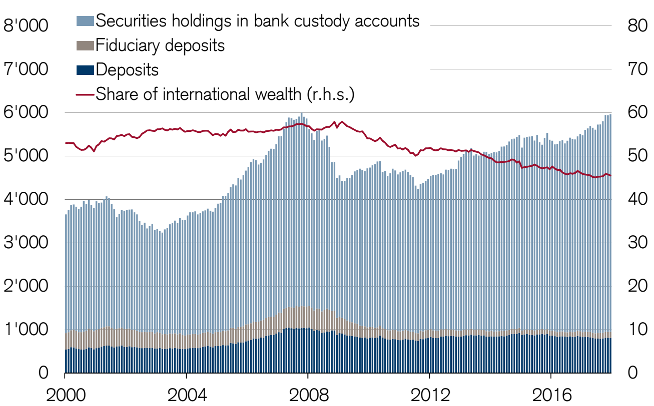
Margin in basis points; commission income in %



Source: KPMG, SNB, Credit Suisse

Estimated assets under management

In CHF (bn); in % (r.h.s.)



Source: SNB, Credit Suisse

The growth of international private banking should recover, with Europe and the Middle East as main focus regions

Looking forward, we believe that the growth of international wealth management should recover, even though the growth of private wealth in Europe is likely to remain more moderate than in fast-growing Asian markets. Moreover, competition for funds is intense in all markets and the lack of an EU-wide access agreement for Swiss banks adds an extra cost layer for Swiss banks. That said, in the area of high or ultra-high net worth individuals these costs are relatively limited. Nevertheless, a formal agreement with the EU as a whole or with additional member countries would enhance growth opportunities to some extent (see p. 25) As regards the international institutional business which is larger in volume, we would expect more or less steady growth in line with the overall funds managed by institutions. As overall wealth grows, Swiss banks should stand to benefit given their strong capitalization, long standing experience in advice for private and corporate clients as well as the safety proposition of Switzerland.

Shifts from high household cash holding into private banking assets are likely to remain limited

Banks in Switzerland manage around CHF 3.3 trn of onshore wealth. Similar to the international business, the share of private investors constitutes a relatively small share of overall assets under management (AuM) – somewhat less than 20% on our estimates. However, in our definition of AuM we exclude sight and savings deposits, which represent a large share of household wealth in Switzerland as elsewhere. Furthermore, slightly more than 20% of AuM are pension fund assets. The rest is split between mutual funds, insurances, social security institutions and commercial clients. Based on our long-term forecasts of financial market returns, we expect a balanced asset allocation in CHF to yield 3.3% p.a. When used as a proxy for the asset allocation of onshore AuM, such a yield could lift onshore AuM to around CHF 3.7 trn by 2021, solely based on market returns. Wealth managers may be able to capture net new assets if households move from holding very high cash levels back into securities; they have been very cautious since the euro crisis and have been net sellers of securities. With banks shielding retail investors from negative interest rates, real returns on current accounts and saving deposits have been fairly high in the past years. If inflation rises somewhat as we expect and nominal interest rates lag that development, the attractiveness of holding large cash balances may diminish. That said risk aversion tends to be quite persistent, and the many uncertainties that households face due to issues such as ageing, health expenditures and job security, is likely to limit the shift from cash to other private banking assets.

What if interest rates remain low for longer

While our main scenario is for a gradual normalization of interest rates and a somewhat steeper yield curve, the resurgence of a recession which would force central banks to lower interest rates again and keep them at very low or negative levels for a longer period of time cannot be excluded. In such an event, banks' margin could again come under pressure. It is not excluded that central banks, and in particular the SNB, would then lower their policy rates to more negative levels and even consider some restrictions on banknotes withdrawal (for example through the introduction of a withdrawal fee). In turn, banks could be forced to pass on the negative rate to more client groups and in particular to retail clients. Moreover, lending from non-banks (e.g. insurances, but also non-financial corporates and Fintech companies) might then further increase competition and put banks' asset margin under added pressure.

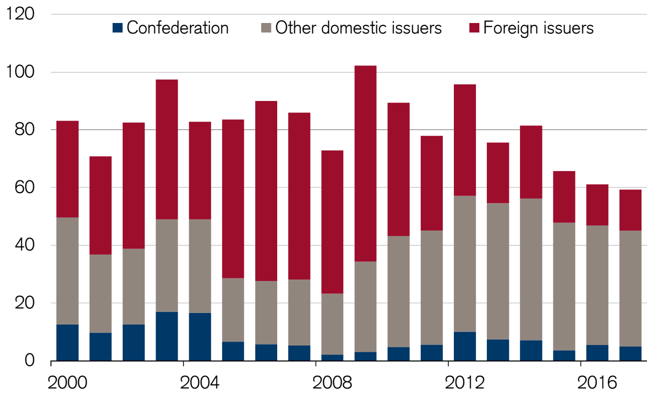
Capital market and Fintech funding

Capital market borrowing of CHF bond issues

New issuance activity in the Swiss franc bond market has declined in recent years, as issuance by foreign issuers has dropped substantially. New issuance activity by domestic corporates has increased, as many companies took advantage of the low interest rate environment to refinance early and to also extend the maturity of their borrowing. We expect growth in the domestic corporate segment to continue in the coming quarters as both existing and first-time issuers may seek to benefit from the current low-yield and tight spread environment as long as it lasts.

New issuance activity has declined

Issues of CHF bonds, in CHF (bn)



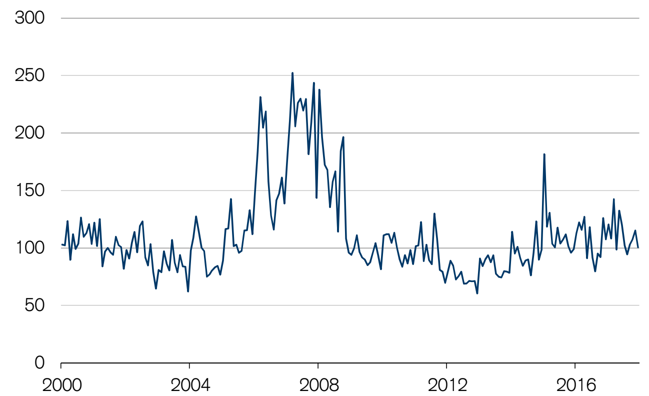
Source: SNB, Credit Suisse

Client activity remained subdued for longer

Commission revenues of wealth managers have also declined on lower client activity. In 2017, securities turnover on the Swiss stock exchange was approximately similar to the turnover of the year 2000, although the market capitalization of the Swiss stock market has increased by 33% since then. One strategy of wealth managers to overcome the decline of commission revenues from trading activity has been to lower trading fees and increase recurring advisory fees, which are dependent on assets under management.

Low client activity also weighing on bank revenues

Securities turnover on the Swiss stock exchange, in CHF (bn)



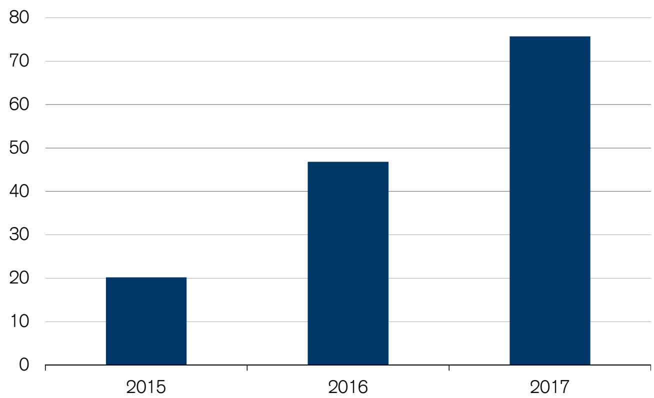
Source: SNB, Credit Suisse

Fintech

According to the Swiss Venture Capital Report published by startupticker.ch, startups in the Fintech sector raised CHF 76 m in 2017, up from CHF 47 m in 2016. We do not see companies in the Fintech sector as direct competitors to banks that threaten their business models, but much more as commercial partners. Companies in the Fintech sector can provide new products to banks or allow banks to outsource services. Since January 2018, regulation regarding public deposits with non-banks has been eased by the FINMA, which should reduce the hurdles for Fintech and additionally foster innovation in Switzerland.

Capital raised by Fintech is rising rapidly

Capital raised by Fintech in Switzerland, in CHF (million)



Source: startupticker.ch, Credit Suisse

Thematic focus

Regulatory environment continuing to change

Four regulatory areas are of special importance in the medium to long term for the further development of the Swiss financial center: improved regulatory processes and efficient implementation of international standards, market access, sustainable finance and digitalization.

Improved regulatory processes and implementation of international standards

Regulation proving effective

2018 marks the tenth anniversary of the outbreak of the financial crisis. The crisis not only shook the global financial system but was also the decisive factor triggering a veritable wave of regulation at both international and national level. A decade later it can now be concluded that the existing far-reaching regulations are proving effective. The international financial system has become more stable, while the Swiss major banks are well on the way toward implementing what by global comparison is a very strict national regime in a timely manner.

Basel III finalized

At the global level the focus is on the extremely comprehensive Basel III set of rules of the Basel Committee on Banking Supervision (BCBS). Following years of discussions between the members of the BCBS, the long expected final components of the Basel III set of rules were approved on 7 December 2017 that are also referred to in the sector due to their far-reaching innovations as Basel IV. The objective of the reforms is to increase the credibility in the calculation of risk-weighted assets (RWA) and improve the comparability of the equity ratios of banks. For this purpose, simpler, more standardized models are being introduced.

The core elements of the reforms can be roughly divided into three areas:

- The standard approaches for the calculation of credit, market and operational risks were revised in order to achieve greater risk sensitivity and comparability among the banks. Furthermore, restrictions in the use of internal models are intended to reduce any variability in the calculation of risk-weighted assets by the banks.
- The introduction of a minimum equity threshold, also known as an “output floor”, serves to reduce the benefits that banks can derive from the use of internal models for calculating their minimum equity requirements.
- Globally systemically important banks (G-SIBs) are now subject to higher requirements concerning their leverage ratio. The new cushion is intended to guarantee that the leverage ratio continues in future to act as a safety net for risk-based requirements.

High importance of international standards for Switzerland

The example of the Basel III set of rules illustrates the importance for the individual countries and jurisdictions of the decisions of international standard setting bodies. Switzerland is often represented on these bodies by the Swiss Financial Market Supervisory Authority (FINMA) and/or the Swiss National Bank (SNB), with the Federal Department of Finance (FDF) also sometimes taking a seat.

Improved involvement of political institutions necessary

The last few years have shown that there is room for improvement in Switzerland’s representation on such bodies: The political institutions are at present to some extent insufficiently involved in the seeking of a position by the FINMA or SNB before the latter represent Switzerland internationally. A closer involvement of the Federal Council as the body responsible for determining the national financial market policy and implementing international standards in national law would be desirable. This would not jeopardize the independence of either the FINMA or the SNB in the core areas of their activities. Regarding future implementation and regulatory projects in Switzerland, more emphasis needs to be given to the question of needs and the cost-benefit ratio than in the past.

Measures introduced

We are pleased to report that various steps have already been undertaken in this regard, as illustrated, for instance, by the work carried out within a working group of the FDF to strengthen competitiveness. A motion submitted by National Councilor Martin Landolt (BDP/GL) in May 2017 raised three demands:

- a clear separation between the responsibilities of the Federal Council for the financial market policy and strategy and regulation on the one hand and the responsibility of the FINMA for operational supervisory activities on the other;
- more effective safeguarding of the political monitoring and control of the activities of the FINMA – while upholding its independence in terms of concrete supervision;
- optimum structuring of the roles and relationship between the FDF and FINMA in order to ensure the best possible achievement of financial market policy objectives, particularly also with regard to the exercise of international representation and collaboration.

The motion was recommended for adoption by the Federal Council and adopted by the National Council. Discussion in the Council of States is still pending.

Relations of Switzerland with the EU and the United Kingdom / market access

Fundamental clarification of relationship with EU important

A close relationship links Switzerland and the EU. The number of bilateral agreements concluded amounts to over 120 and comprises a broad spectrum of policy areas. These include the two Bilateral I and II agreement packages. The bilateral agreements are of central importance from the perspective of the Swiss economy. However, it is to be expected in the medium to long term that the currently good market access of certain economic sectors to the EU and the European Economic Area (EEA) will erode. The difference between the static bilateral agreements and the further development of EU law will increase over time. The existing agreements therefore need to be updated from time to time in order to uphold their full quality. A fundamental clarification of the relationship with the EU is therefore considerably better for the Swiss economy in the long term than the present state of limbo.

Institutional framework agreement prerequisite for further development

Owing to the complexity of the bilateral agreements, the EU has since 2008 been calling for a comprehensive institutional framework for the relations between the two parties. With this in mind, Switzerland and the EU are discussing mechanisms aimed at ensuring a more uniform and efficient application of existing and future agreements.

Impact of Brexit on Switzerland

Brexit also with consequences for Switzerland

The decision by the United Kingdom to leave the EU has shifted the priorities of the EU to the exit negotiations with the UK. Nevertheless, the Brexit negotiations could open up new opportunities for Switzerland in the medium to long term. The relationship between Switzerland and the UK also needs to be redefined as a result of Brexit. We therefore welcome the strategy of the Federal Council of avoiding gaps in the relationship and advocate close dialog between the two parties.

Core elements of the Basel III reforms

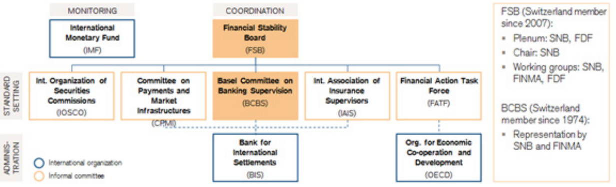
Staggered introduction

Elements	Implementation date
Revised standard approaches for market, credit and operational risks	1 January 2022
Leverage ratio cushion for globally systemically important banks	1 January 2022
Minimum equity threshold ("output floor")	1 January 2022: 50%
	1 January 2023: 55%
	1 January 2024: 60%
	1 January 2025: 65%
	1 January 2026: 70%
	1 January 2027: 72.5% (final calibration)

Source: Basel Committee on Banking Supervision (BCBS), 2017

International standards

Improve involvement of the Federal Council



Source: Credit Suisse, own illustration

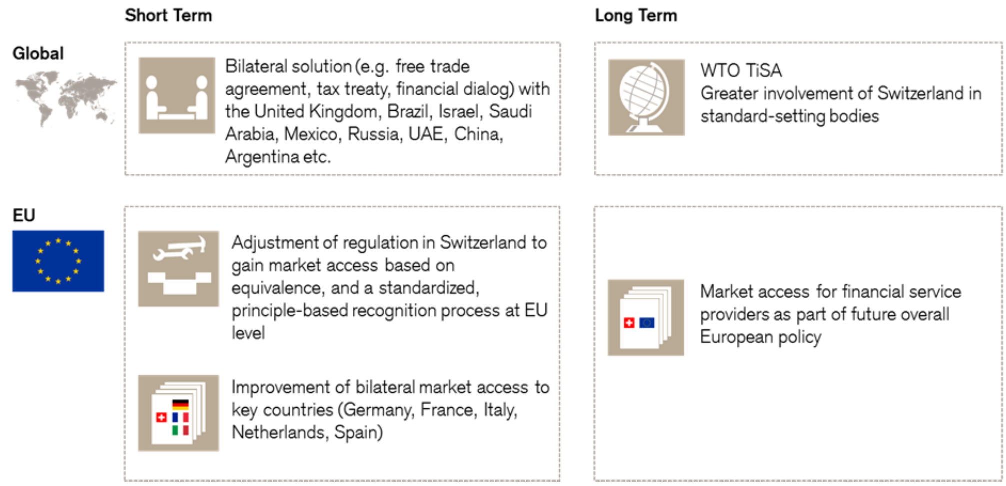
This should aim at securing the status quo and simultaneously addressing a potentially closer relationship following departure from the EU.

Market access

Market access is a core success factor

Swiss financial services providers are globally dependent on good market access conditions as this is the only way for the Swiss financial center to offer clients abroad the best possible products and services.

Market access as an integral component of financial market policy
Multi-stage procedure necessary



Source: Credit Suisse

Focus on EU single market

The focus is placed on the EU and EEA due to their geographical proximity. Based on the third-party rules existing in EU financial market regulation, the European Commission, in consultation with the European supervisory authorities, can grant non-member countries access to the single market as long as it recognizes the regulatory and supervisory framework of such non-member countries as equivalent in the applicable area. In the short term Switzerland therefore requires regulations where necessary and appropriate that are equivalent in effect to those of the EU in order to be able to benefit from the EU single market. This applies particularly in the area of investment protection where Switzerland aims to take account of the core issues of the corresponding EU provisions (MiFID II) with its Financial Services and Financial Institutions Acts (FIDLEG/FINIG). However, the processes for recognition of equivalence, as illustrated by the experience with stock market equivalence, are often political decisions and therefore linked to uncertainties. Greater predictability and planning security would therefore be welcome. In addition, there remains the need for a suitable solution allowing Switzerland in the medium to long term to secure permanently and improve its banks' market access to the EU/EEA. A financial services agreement (FSA) must therefore continue to be pursued as a longer-term strategic option, while at the same time other potential solution approaches are also taken into consideration in view of the political opposition to an FSA.

Bilateral market access also important

As well as the aforementioned need for action regarding the relationship with the United Kingdom, market access to key core markets such as Germany, France, Italy, Spain and the Netherlands also needs to be the subject of bilateral endeavors. Furthermore, bilateral agreements for improving market access also need to be sought with core markets in Central Europe, the Middle East, Asia and Latin America.

Sustainable finance

Importance of sustainable investments has been growing for years

For years, the volume and share of investments made under consideration of environmental, social and governance criteria (ESG) has been growing above average both globally and in Switzerland (see also p. 26, 27 and 34 of our 2016 study). The Swiss financial center is a pioneer in the area of sustainable investment solutions. It is a leader in particular in the areas of impact investing, microfinance and development finance. Its strengths furthermore lie in the high volume of amounts invested (including cross-border investments), the broadly diversified range of players (including foundations with assets under management estimated at CHF 100 billion), the associated know-how and the international network.

High international momentum

International developments such as the UN Sustainable Development Goals (SDG), the work of the G20 Green Finance Study Group, the recommendations of the FSB Task Force on Climate-related Financial Disclosures (TCFD) and the EU Action Plan on Sustainable Finance published in March 2018 are shaping this momentum. These initiatives among other things set out standards governing what counts as a sustainable investment, how climate and other environmental factors are to be systematically integrated into risk management and how the corresponding reporting is to be made comparable. The demographic trend and changed customer preferences (keyword: millennials) furthermore contribute to the development of sustainable finance.

Fintech/digitalization and innovation

Developments and trends

Digitalization has long been accompanying banks

Since the first use of computers by what was then the Union Bank of Switzerland (today's UBS) and the former "Schweizerische Kreditanstalt" (today's Credit Suisse) back in 1956, digitalization has become a constant companion of the financial sector. The latest stage of this development is subsumed under the keyword Fintech[1].

Banks are also Fintech innovators

Alongside highly acclaimed start-ups, established market players such as banks are also significantly active in this area. The banks often pursue innovations in the financial sector in close project collaboration with the Fintechs. The new technical opportunities are used to enhance client satisfaction, expand the range of products and services and increase efficiency. For example, with its "Direct Business" expanded online banking solution, Credit Suisse offers its corporate clients the option of displaying account information of domestic and foreign third-party banks, thereby facilitating liquidity planning. It is also possible to bridge liquidity bottlenecks through capital goods and vehicle leasing paperlessly and in real time. The "Online Relationship Onboarding" service launched in 2017 allows private clients to open an account with Credit Suisse paperlessly. The ID document is checked in a video call and the client accordingly identified.

Use of Fintech at the interface to the client and for internal bank processes and procedures

As well as deployment at the interface to the client, the new technologies above all also open up many new opportunities to be systematically tapped for internal bank processes and procedures. A well-known example is so-called RegTech (regulatory technology) that promotes a more efficient implementation of regulations in the compliance and reporting areas of banks. A special emphasis is also placed on blockchain and other distributed ledger technologies attested much potential by the sector in order to speed up processes, reduce susceptibility to error and increase capital efficiency.

Necessary framework conditions

General locational factors are also crucial alongside specific requirements

As in previous phases of technological and social change, the legislator is also confronted today with a certain discrepancy between the underlying legal conditions and new business models. In order to offer the requisite leeway for entrepreneurship also in future, it is necessary to gear the underlying conditions to an increasingly digitalized economy and secure the foundations for future prosperity and employment. The use of new technologies and the market entry of further companies are to be facilitated without exerting an adverse impact on existing providers due to unfair regulation. Although the current technological developments place very specific demands on the legal environment, this should not detract attention from the fact that the requisite underlying conditions for every entrepreneurial activity (legal and planning security, fiscal attractiveness, modern and efficient infrastructure etc.) are also of central importance here. Switzerland's high locational attractiveness at present needs to be preserved and enhanced particularly also in view of the growing locational competition.

[1] The Institute of Financial Services Zug of Lucerne University of Applied Sciences and Arts defines this term as a paraphrase for innovative digital products, services and processes in the financial industry aimed at improving, supplementing or replacing existing offerings. Lucerne University of Applied Sciences and Arts. (2016). *IFZ Fintech Study 2016.*

Financing of start-ups

The Federal Council was already commissioned by a parliamentary motion back in 2013 to examine how the underlying conditions for venture capital could be improved. In the report drawn up in response to the motion, the Federal Council concluded that while the financing of start-ups posed a challenge, the Swiss venture capital market was altogether working well. However, the report also stated that the Swiss venture capital market could be developed further and in this respect made reference to the "Joint Declaration on the Financing of Fast-Growing Start-ups" signed by representatives of the Federal Government and the private sector (among others the Swiss Bankers Association and the Swiss Insurance Association). The voluntary financial support of start-ups lies at the core of this declaration of intent. Concerning public sources of financing, the Federal Council does not currently see any necessity to launch any further programs alongside the cantonal and national schemes already existing. With regard to the fiscal environment, the Federal Council has signaled its readiness to review a potential shift from taxes detrimental to a company's capital and assets to a greater focus on income taxation if commissioned to do so by the parliament.

A further motion called for the investment opportunities of retirement benefits institutions to be adjusted so as to facilitate increased investments in innovative technologies. To this end the motion also proposes the creation of a "Switzerland future fund" to take on the management of such investments at the request of the retirement benefits institutions. In its reply the Federal Council made reference to the investment opportunities in venture capital already existing under current law and objected to government intervention in the investment policy of the retirement benefits institutions.

Credit Suisse established SVC Ltd. for Risk Capital for SMEs back in 2010 in order to support small and medium-sized enterprises (SMEs) in Switzerland with a total of CHF 100 million in venture capital in conjunction with the objective of strengthening Switzerland's position as a center for business and employment. So far around CHF 110 million have been invested in 44 companies and some holdings have since been sold again at a profit. While investments in SMEs from the financial services sector have so far not been envisaged, a new investment cluster for Fintechs was created in March 2018 and additional investment capital of CHF 30 million made available. Companies developing and marketing digital financial innovations are being placed in the foreground here.

Regulation: State of affairs

The administration and parliament have responded to technological changes and the concerns of business and introduced a broad range of measures. The following inventory of the key elements is intended to provide an overview.

Overall economic measures

Analysis of digital suitability of existing laws by the end of 2018

Digital test: On the occasion of the publication of the Federal Council's comprehensive report *Framework Conditions for the Digital Economy* in January 2017, the State Secretariat for Economic Affairs (SECO) was commissioned to carry out a so-called "digital test", i.e. an analysis of the digital suitability of existing laws in order to reveal to the Federal Council by the end of 2018 any need for revision.

Data protection law: Equivalence with EU regulation crucial

Data protection law: Owing to the new data protection package issued by the EU in April 2016, it also became necessary to carry out amendments to Swiss data protection legislation. A corresponding draft revision was presented by the Federal Council on 17 September 2017 and is currently undergoing parliamentary review. Its aim is to adjust data protection to technological and social developments and safeguard the equivalence of the Swiss level of data protection with that in the EU member states in order to enable the cross-border transfer of data also to remain possible in the future.

E-ID: Collaboration of Federal Government and private providers

Electronic identity (E-ID): In addition to conventional means of identification such as passports and ID cards, it is now also to be possible for the identity of a natural person to be proven electronically and accepted by all parties on a day-to-day basis. This should facilitate the further development of both online shops (e.g. delivery against invoice) as well as e-government applications (e.g. completion of tax returns). The Federal Council favors the use of E-ID concepts of private providers and has announced a corresponding communication for the summer of 2018. The role of the Federal Government is intended to lie in defining the legal and technical framework conditions enabling private providers to gain state accreditation. The state accreditation authority is to continue to exercise supervision of the providers. Furthermore, accredited providers are to be capable of verifying ID data held by the government (such as last name, first name, date of birth) via an interface. In February 2018, a group of Swiss companies, including Credit Suisse, founded the company SwissSign Group Ltd. whose objective is to create and implement a digital identity for the Swiss population.

Sector-specific measures

Facilitate crowdfunding and crowdlending without a banking license

Extension of deadline for settlement accounts: In order to avoid the need for a banking license in the case of crowdfunding and crowdlending products for the temporary acceptance of client deposits, the Federal Council decided as of August 2017 to set a new deadline of 60 days in the Banking Ordinance for settlement of the principal business. According to the previous FINMA practice, this deadline was just seven days.

"Sandbox" offers opportunity for testing business model

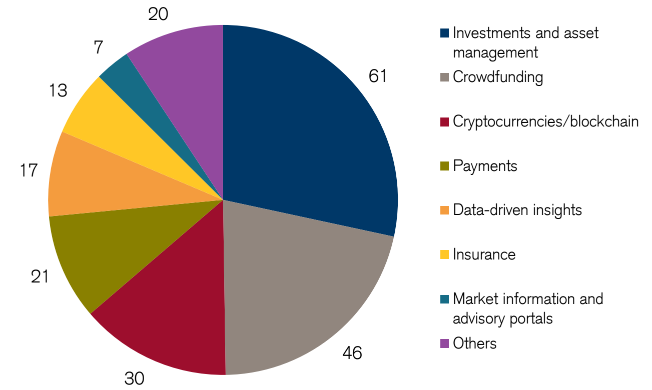
Extension of activity not subject to licensing ("sandbox"): The Federal Council simultaneously decided to extend the existing activity not subject to licensing in order to offer market newcomers the opportunity to test their business model. It will now be possible to accept an unlimited number of deposits from the public up to a total value of CHF 1 million without a banking license.

New licensing category for Fintechs

Licensing for Fintech institutions: A proposal to create a new licensing category for institutions that do not engage in typical banking business but involve certain elements of banking activities (e.g. payment providers or crowdfunding platforms with longer settlement periods) is still currently the subject of parliamentary debate. This new category would apply to institutions that confine themselves to the deposit-taking business (acceptance of deposits from the public) and thus do not engage in any lending with maturity transformation. As a parameter the Federal Council proposes an upper limit on deposits of CHF 100 million. The deposits may be neither invested nor paid interest.

Swiss Fintech landscape

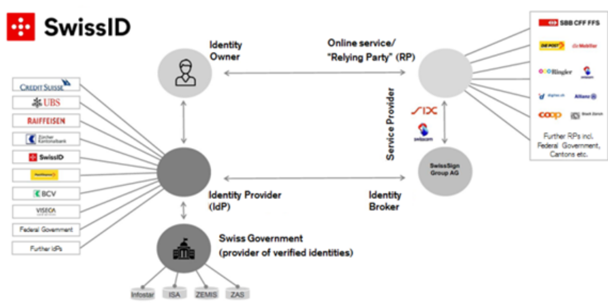
Fintech start-ups by area [number]



Source: Swisscom. (2018). *Swiss FinTech Start-up Map*, March 2018.

How electronic identity (E-ID) works

SwissID: broad-based consortium for E-ID in Switzerland



Source: SwissSign. (2017). *Swiss Digital Identity* press conference.

Simplified opening of business relationship with digital onboarding

FINMA Circular on Digital Onboarding: The Circular that entered into force in 2016 facilitates the establishment of business relationships via electronic channels. Subject to compliance with certain requirements, this therefore permits banks to open a business relationship with a client via video transmission. A partial revision to selectively update the Circular was initiated at the start of 2018.

Clarification of underlying legal conditions regarding blockchain/ICOs

Blockchain/ICOs (Initial Coin Offering) working group: The working group created in January 2018 by the State Secretariat for International Finance is to review the underlying legal conditions in this area in cooperation with the relevant federal authorities and in consultation with the sector and pinpoint any need for action. The objective of this work is to increase the legal security and uphold the integrity of the financial center. The working group is to report to the Federal Council on its work by the end of 2018.

Pension provision in the context of social change

Swiss pension system in upheaval

Demographic developments and new work models are calling for a rethink and political flexibility regarding the Swiss pension systems. Targeted incentives for private pension provision in pillars 2 and 3 and a functioning intergenerational agreement are needed as the basis for further success.

Traditional pension fund business will grow slowly, but new models offer growth opportunities

Growth in the area of pension fund assets which constitute 20% of domestic AuM with Swiss banks is likely to be more limited than for private wealth. The key reason is that the workforce is shrinking relative to the cohort of pensioners and payouts to pensioners remain too high relative to these demographic trends. In the absence of a substantial reform of the Swiss pension system, growth in pension fund assets will be limited. On our estimates, pension fund assets grew by CHF 4 to 5 bn or less than 1% p.a., between 2012 and 2016 on new assets while the rest resulted from capital gains. Looking forward, the reliance on – highly uncertain - market returns rather than on new assets could become even more pronounced. In the case of state pension assets (AHV) and in absence of any reform, we are likely to witness a shrinkage. While onshore institutional asset management volumes will thus remain very large, the growth potential appears limited. That said, given that both the first and the traditional second pillar of the pension scheme are under pressure, it seems likely that new forms of pension saving as well as the so-called third pillar will experience above-average growth, albeit starting from still very low levels.

Low interest rate environment, high minimum conversion rates and demographics exerting pressure on the Swiss pension system

Demographics and interest rate level driving changes to Swiss pension system

The greatest challenges for occupational retirement benefits are posed by the low interest environment (cited by 93% of pension funds canvassed in 2016). The excessively high minimum conversion rate and the demographic change are also among the three main concerns for almost 60% of pension funds. The occupational retirement benefits system is losing its financial balance due to the sluggish adjustment of benefits. Conversion rates and technical interest rates set too high from an actuarial perspective among other things lead to an unforeseen redistribution between the generations in the second pillar. For 2016 we estimate that in 2015 altogether around CHF 5.3 billion were redistributed contrary to the system from active members to pensioners – money that future retirees will lack the longer this continues.

Existing pensions are not affected as the amount of the pensions at the time of entitlement always remains guaranteed by law. According to prevailing law, once the pension has been set, it may no longer subsequently be lowered. If the retirement benefits institution sustains a shortfall, the pensioners can be required to make a contribution to the remedy of such shortfall; however, according to Art. 65d para. 3 lit. b OPA, this may only be levied in the extra-mandatory area and only on the share of current pensions that has arisen in the previous ten years through increases not prescribed by law or the regulations (e.g. inflation adjustments).

Insured members challenged by obligatory pillar 2 lump sum withdrawal

Less guaranteed capital – private provision via pillars 2 and 3 gaining importance

Since the OPA revision back in 2006, persons with higher incomes have been able to choose between different investment strategies. However, these 1e plans have suffered from a design flaw: Insured persons have been allowed to take with them the profits gained when leaving the pension fund while the capital paid in is guaranteed (i.e. the investment losses have been borne by the pension fund). In order to remove this asymmetry, the parliament approved an amendment to the law at the end of 2015 that came into force at the end of 2017 together with the corresponding administrative provision. The insured members now bear the full investment risk. This is accompanied by a more comprehensive duty to provide advice on the part of the retirement benefits institutions vis-à-vis the insured members of the kind already customary today at banks in the private clients business.

Further political debate on the part of the pensions industry desirable

In order to safeguard the pension funds in the long term, we see a need for a more in-depth political debate about minimum conversion and interest rates and raising the retirement age above 65.

One thing is clear: If the current standard of living is to be maintained after retirement, it will be crucial for a majority of the population to start saving for their pension early on in life, as the investment horizon will be all the longer and the ability to sustain a higher investment risk all the greater, thus enhancing the return expectations.

Tied pension provision (pillar 3a)

Tied pension provision is supported by the Federal Government with measures in tax policy and the promotion of home ownership. It enjoys various tax benefits but is tied to statutory provisions. For example, only persons with an earned income subject to AHV contributions can benefit from tied pension provision and 3a pension gaps cannot be closed retrospectively.

Pillar 3a – key features at a glance

- Payments into pillar 3a may be deducted annually from taxable income up to certain maximum amounts
- No withholding or wealth tax during the term
- The pension capital is taxed at a reduced rate separately from other income upon payment
- The pillar 3a market has significantly gained importance in the last 20 years: Tied pension assets invested with banks and insurance companies amounted to over CHF 113 billion at the end of 2016.

Pension plans with selection opportunity for investment strategy (1e plans)

Retirement benefit institutions that exclusively insure wage shares above one and a half times the marginal amount (2018: CHF 126,900) can offer their beneficiaries different investment strategies. The label “1e” is derived from the article with the same name in the Ordinance on Occupational Old Age, Survivors’ and Invalidity Pension Provision (Art. 1e OPO 2).

1e plans – key features at a glance

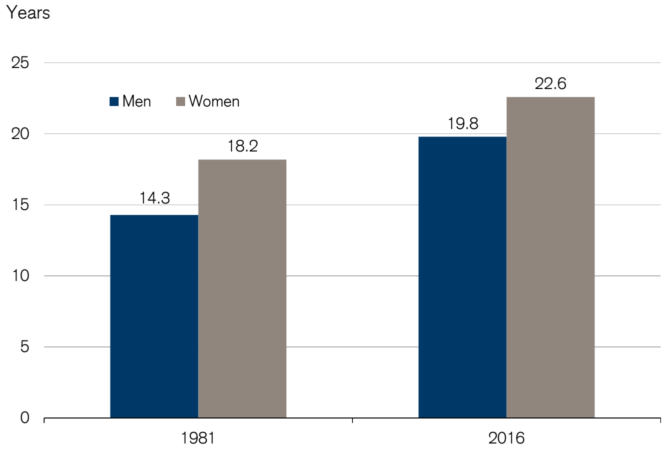
- The principle of collectiveness also applies to 1e plans: If the pension fund commission of a company selects a 1e plan, this applies collectively to all employees.
- Investment returns and losses are passed on in their entirety to the individual insured members: There is no redistribution.
- Since 2017, the insured members have borne the full investment risk. The guarantee of assets invested at the time of departure otherwise applicable to pillar 2 does not apply.
- Affiliated companies can select from up to ten investment strategies. A low-risk strategy must also be offered from among these.
- The insurance principle must be upheld. At least 6% of the contributions are earmarked to finance the risk insurance (disability and death).

Swiss pension system at a glance

Demographics, low interest environment and high conversion rate driving the restructuring of the pension system

The group of those currently older than 65 will grow by seven percentage points in the coming eight years in Switzerland to account for a good quarter of our society, while life expectancy is simultaneously increasing: The life expectancy of women has increased by 4.4 years in the past 35 years and that of men by 4.4 years.
Assuming savings behavior and the retirement age remain unchanged, there would have to be a significant increase in returns in order to finance both a longer lifespan and more retirees. However, based on the current interest situation exactly the opposite is the case.

Fig. 1 Remaining life expectancy at age 65



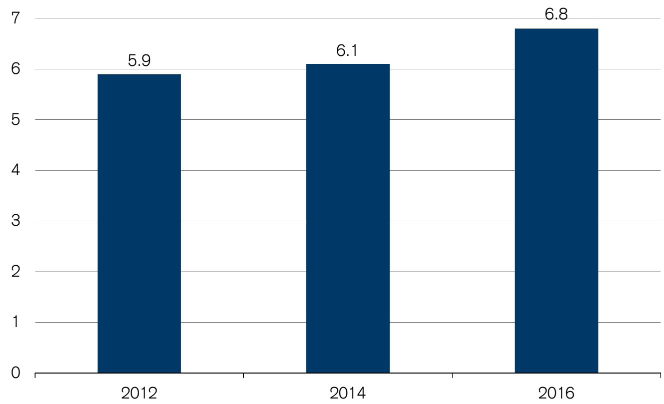
Source: Federal Statistical Office

Trend toward lump sum withdrawals of extra-mandatory assets

Almost CHF 7 billion are withdrawn annually from pillar 2. This is equivalent to an increase of 15% in four years, a trend which is set to gain further strength in the next few years: Over CHF 5 billion were redistributed from active members to pensioners in pillar 2 in 2015 – to the displeasure of many actively insured individuals. 1e plans protect higher earners from this redistribution but imperatively require a lump sum withdrawal. Meanwhile, companies see in lump sum withdrawals a possibility to release themselves from pension obligations. However, not all insured members know how to handle lump sum withdrawals and they are at risk of incurring pension gaps. These need to be identified and closed at an early stage.

Fig. 2 Retirement-related lump-sum withdrawals from pillar 2

CHF billion



Source: Federal Statistical Office

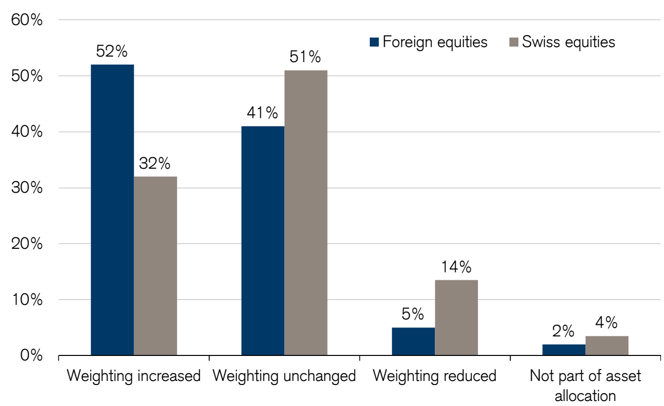
Role of banks as pension partners

The increased emphasis on individual responsibility in pillar 3 and recently also in pillar 2 (1e plans) is inevitably also generating a greater need for advice among insured members. The fact that under the pressure of falling returns retirement benefits institutions are having to take on greater investment risks is additionally fueling this requirement.

The provision of detailed advice about investment risks that takes account of the entire assets has for years been among the core activities of banks. New legal framework conditions (FIDLEG) have additionally increased due diligence requirements. Banks today incur a natural responsibility regarding integrated retirement and asset planning that needs to be upheld.

Fig. 3 Trend towards riskier investments

Share of retirement benefits institutions that have adjusted their equity weighting due to the low interest environment



Source: Credit Suisse

Chapter 3

Recommendations for action

In order to uphold and increase the locational attractiveness of the Swiss financial center, various economic policy measures need to be taken. Many of the proposals from business in this regard have already been under discussion for some time. At the same time, there is a series of specific success factors that are relevant for the financial center. Below we identify the key recommendations for action for various stakeholder groups.

Preserve and further expand high general locational attractiveness

Switzerland is top – but the competition never sleeps

In terms of its general competitiveness, Switzerland regularly occupies leading positions in the corresponding international rankings and ratings. For example, Switzerland currently tops the Global Competitiveness Index of the World Economic Forum (WEF) and comes second in the IMD World Competitiveness Ranking 2017. However, it would be fatal for us to rest on our laurels in view of such distinctions. Instead, we need to uphold and as far as possible further expand Switzerland's locational attractiveness amid the increasingly cut-throat global competition. This is particularly the case in view of the fact that with regard to the locational rankings specific to financial centers, the Swiss centers of Zurich and Geneva have generally been exposed to a downward trend in recent years.

The main dimensions in this connection and the recommendations for action derived from them are:

Government, parliament and supervisory authorities:

- Safeguard legal and associated planning security
- Ensure moderate regulation and observance of economic freedom
- Fiscal attractiveness for natural persons and legal entities (Tax Proposal 17)
- Maintain liberal labor law
- Provide modern and efficient infrastructure (including nationwide 5G networks)
- Close collaboration between state universities as well as research institutions and the private sector

Banks and economy:

- Availability of skilled labor and corresponding investments in the training and education of employees
- Adequate contribution to the availability of capital during all phases of corporate development
- Close collaboration of businesses with innovation drivers such as universities
- Contribution to promotion of financial literacy of the Swiss population

Improved regulatory processes and implementation of international standards

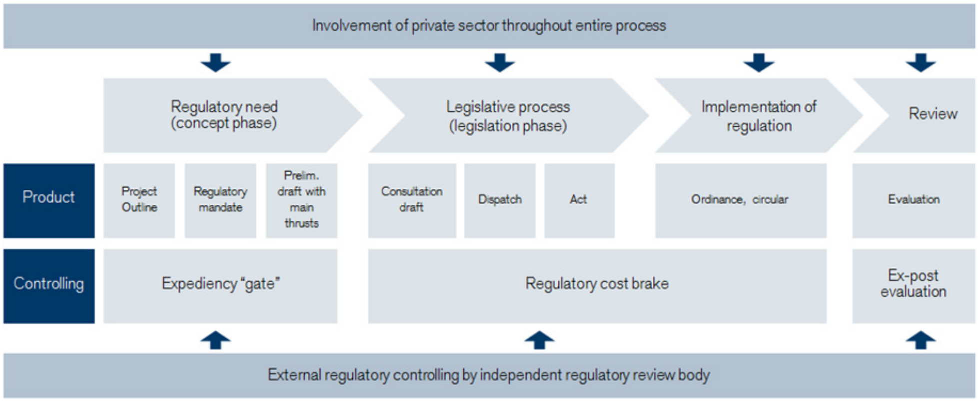
Enhancement of regulatory processes strengthens competitiveness

International standards and government regulations have significantly shaped the environment in which banks operate in recent years. Not least the importance of the FINMA for the issuance of regulations in Switzerland has increased continuously in the past few years. There is therefore a need for an open discussion about how governance can be strengthened in the positioning of Switzerland in international standard setting bodies and whether supervisory and regulatory activities ought not to be more strongly separated (organizationally). For this reason the Landolt motion is to be welcomed. Furthermore, Switzerland needs to consider both extensive regulation controlling including a regulation inspection body and a strengthening of the objectives of competitiveness.

Marching in step with competitors in the implementation of standards in terms of time and content crucial

As far as the concrete implementation of international standards is concerned, the focus is currently on the finalized Basel III reforms. It is essential that this takes place in tandem with the main comparable financial centers in terms of both time and content. The strength of Swiss regulation is its clarity and transparency. Should the introduction of the final Basel III reforms in Switzerland take place ahead of the international time schedule, this would damage the stable and predictable reputation of Swiss regulation and thus also the competitiveness of the Swiss financial center. With this in mind, consistent use of national leeway needs to be made in order to strengthen competitiveness.

Simplified cycle of regulatory process
Improved process strengthens efficiency



Source: Swiss Bankers Association: Policy Paper for a good regulatory policy, own illustration

Government, parliament and supervisory authorities:

- Introduction of a top-down regulatory process with clear responsibilities for financial market policy by the Federal Council and operational supervisory activities by the FINMA. Needs and impact analysis supplemented by an independent regulatory review body
- Stronger weighting of competitiveness of the Swiss financial center and its players as a FINMA target in its regulatory activity
- Effective guarantee of monitoring of regulatory activities of the FINMA by the Federal Council and parliament while upholding the independence of the FINMA
- Consistent implementation of global standards in terms of time and content such as Basel III with the timely involvement of the Federal Department of Finance to avoid regulatory fragmentation and in doing so safeguard a fair level playing field, i.e. strengthening of competition through utilization of national leeway

Banks and economy:

- Greater involvement in the medium to long-term prioritization of regulatory initiatives through participation on committees for the regular exchange of dialog between private-sector players and authorities
- Inclusion of the sector in defining Switzerland's positions on international standard setting bodies

Relations of Switzerland with the EU and the United Kingdom / market access

Clarification of relationship with EU and UK necessary

The EU and its 28 current member states are Switzerland's most important (trading) partners. This strong tie between the EU and Switzerland is based on a closely intertwined economy, Switzerland's geographical location at the heart of Europe and cultural affinities. It is therefore necessary to clarify the long-term relationship with the EU as well as the future relationship with the United Kingdom.

Seek improvements with both the EU and individual countries

For the Swiss financial center as an exporter of services to safeguard its position as a leading financial center, Swiss financial services providers are dependent on good market access conditions. This calls for solutions with both the EU and individual countries (not just in Europe but also on other continents) for which a multi-stage procedure is necessary.

Government, parliament and supervisory authorities:

- Clarification of relationship with the EU, e.g. through resolving institutional issues that are acceptable and bring benefits for both parties
- In an initial step search for solutions with the United Kingdom to preserve the status quo and in a second step improvement of market access

- Improve bilateral market access to central core markets by means of agreements
- Agreement with the EU with the aim of concluding pending processes for recognition of equivalence quickly and on the basis of objective technical criteria
- Safeguard and expand market access to EU/EEA single market in the medium to long term also under consideration of potential new options

Banks and economy:

- Active assistance in the search for solutions within the scope of the envisaged bodies
- Development of measures for resolving market access issues
- Early identification of market access obstacles

Sustainable finance

Switzerland should build on its strengths and avoid going it alone

Switzerland is excellently positioned to further expand its strengths in sustainable finance and benefit from the prevailing trend. This entails utilizing and wherever possible participating in international developments. However, Swiss special solutions, for instance in terms of reporting standards, should be avoided.

Government, parliament and supervisory authorities:

- Support international developments abroad and promote voluntary activities of the industry at home
- Support Swiss industry representatives to help develop these standards at an international level
- Avoid Swiss special solutions (Swiss Finish) for standards, labels and certifications for sustainable investment or reporting
- Implement recommendations at federally owned institutions (e.g. public retirement benefits institutions).
- Provide platforms for the exchange of knowledge

Banks and economy:

- Utilize international developments (as an ‘early adopter’) and help to shape these wherever possible
- Systematically picking up client interest in sustainable investments through dialog and regularly address the corresponding opportunities and risks
- Sensitization and regular training sessions for relationship managers
- Address the recommendations of the Financial Stability Board (FSB) Task Force on Climate-related Financial Disclosures and make use of such disclosures for the assessment of risks and opportunities

Digitalization and innovation

Adjustment of framework conditions to needs of a digitalized economy

Further adjustments will be necessary due to the future development of innovative business models in the financial services sector. Close dialog between companies, associations, interest groups and authorities is called for here in order to ensure a swift and adequate response to changes in the technical and economic environment. Due justice must also be done to the fundamental principles of good regulation (needs, cost-benefit ratio).

Government, parliament and supervisory authorities:

- Upholding of competitive neutrality, among other things through technology-neutral regulation
- Continuous monitoring in the area of cryptocurrencies/ICO and where necessary clarification of legal handling in order to uphold the integrity and reputation of the financial center
- Safeguarding of Swiss data protection legislation equivalent to the EU data protection package; avoidance of a ‘Swiss Finish’
- Swift ratification of the E-ID Act by parliament and broad acceptance of E-ID in communications with authorities

Banks and economy:

- Promotion of innovation and use of new technologies within own company and in collaboration with other companies
- Safeguarding of the financing of new and innovative Fintech enterprises and mentoring of start-ups

- Provision of user-friendly E-ID for private individuals and swift and broad acceptance of E-ID in business transactions

Create the right incentives for a sustainable and affordable pension system

Adjustment of framework conditions of the Swiss pension system to demographic trends and new work models

Compared internationally, Swiss pension funds are unrivaled. To enable the security of pension fund beneficiaries to be guaranteed in the long term, compromises and measures on the part of beneficiaries and insured members are required, both of which call for decisions by the government, parliament and people.

In order to safeguard Swiss pension funds in the long term, we consider an honest political debate concerning the minimum conversion rate and an increase in the retirement age to be imperative.

One thing is clear: If the current standard of living is to be maintained after retirement, prudent planning of private pension provision will be essential for many. The earlier people start saving for their pension, the longer the investment horizon and the greater the investment risk that can be assumed, which in turn enhances the return opportunities.

Government, parliament and supervisory authorities:

- Long-term safeguarding of Swiss pension funds including adjustment of real minimum conversion rate, gradual adjustment of retirement age to demographic trends
- Differentiated consideration of the income situation of retirees with regard to residential property (e.g. affordability).
- Inclusion of new, flexible work models in Swiss pension provision (freelancers and part-time employees).
- Addressing of gaps also in private pension provision and identification of adequate solutions.
- Also facilitate purchase into private pension provision (3a) when there is temporarily no income subject to AHV contributions (parental leave etc.).
- Promotion of sustainable investment models for pension funds.
- Reduction of restrictions for extra-mandatory pension plans in which the insured members bear the investment risks themselves (1e plans): possibility of interest on purchasing potential.

Banks and economy:

- Provision of new mortgage models and flexible investment solutions that do justice to the trend toward lump sum withdrawals.
- Promotion of home ownership: implementation of new indirect repayment models in pillar 2 extra-mandatory occupational benefits provision.
- Provision of well diversified, simple and cost-efficient investment solutions under OPO 2 for all investment horizons.
- Provision of risk clarification in connection with pension plans in which the insured members bear the investment risk (1e plans).
- Training of pension fund beneficiaries across all generations.

Risk warning

Every investment involves risk, especially with regard to fluctuations in value and return. If an investment is denominated in a currency other than your base currency, changes in the rate of exchange may have an adverse effect on value, price or income.

For a discussion of the risks of investing in the securities mentioned in this report, please refer to the following Internet link:
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This report may include information on investments that involve special risks. You should seek the advice of your independent financial advisor prior to taking any investment decisions based on this report or for any necessary explanation of its contents. Further information is also available in the information brochure "Special Risks in Securities Trading" available from the Swiss Bankers Association.

Past performance is not an indicator of future performance. Performance can be affected by commissions, fees or other charges as well as exchange rate fluctuations.

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Investments may have no public market or only a restricted secondary market. Where a secondary market exists, it is not possible to predict the price at which investments will trade in the market or whether such market will be liquid or illiquid.

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Where this report relates to emerging markets, you should be aware that there are uncertainties and risks associated with investments and transactions in various types of investments of, or related or linked to, issuers and obligors incorporated, based or principally engaged in business in emerging markets countries. Investments related to emerging markets countries may be considered speculative, and their prices will be much more volatile than those in the more developed countries of the world. Investments in emerging markets investments should be made only by sophisticated investors or experienced professionals who have independent knowledge of the relevant markets, are able to consider and weigh the various risks presented by such investments, and have the financial resources necessary to bear the substantial risk of loss of investment in such investments. It is your responsibility to manage the risks which arise as a result of investing in emerging markets investments and the allocation of assets in your portfolio. You should seek advice from your own advisers with regard to the various risks and factors to be considered when investing in an emerging markets investment.

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