

News Release

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REGULATORY OVERKILL SEEN AS MAIN RISK FACING BANKS

The remorseless rise in regulation has become the greatest risk facing the banking sector according to the latest 'Banana Skins' survey conducted by the CSFI, the independent City of London think tank, and sponsored by PricewaterhouseCoopers. The report finds that regulatory overkill saps bank resources, reduces risk diversification and creates a false sense of security.

This finding is based on responses from 440 bankers and close observers of the banking scene in 54 countries, but the threat is perceived to be particularly strong in the EU and North America. Many senior bankers described regulation as "out of control".

The Banana Skins survey, now in its 10th year, ranks banking risks by their perceived severity, and analyses their potential impact on the industry. Other fast-rising risks identified in this year's poll are hedge funds (5th) and electronic fraud (6th), as well as currency risk (7th) due to the current weakness of the US dollar.

Closely linked to overregulation is the high place given in the rankings to corporate governance risk (3rd). Although banks are seen to have weaknesses in this area, this particular 'Banana Skin' also scores strongly because respondents – particularly bankers – perceive it to be part of the regulatory threat.

John Hitchins, UK Banking Leader, PricewaterhouseCoopers, commented:

"Bankers have thrown down a challenge against too much prescriptive regulation. Many are worried that it is beginning to stifle innovation and judgement across the industry. While few challenge the objectives of regulators, there is a clear need for further debate on how these are implemented".

Other high level risks include credit risk (2nd) and derivatives (4th), both of which featured prominently in last year's survey. Unrest in the Middle East also gave a strong boost to commodities (up from 26th to 14th), where potential instability in the oil and gold markets is seen as threatening.

However, broad concerns about macro-economic trends have eased (down from 3rd to 10th), along with fears of political shocks and terrorist attacks, as reflected in the sharp decline of concerns about business continuation (down from 5th to 19th). Worries about the strength of the insurance sector, which featured strongly last time, have also diminished (down from 4th to 11th).

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However the survey found that banks were seen to be less well prepared to handle risk than before. 57% of respondents thought banks were moderately well prepared or better to handle the risks, down from 69% in the previous survey. One reason was the inclusion in this survey of a larger proportion of respondents from emerging market and EU accession countries where bank readiness was seen to be less advanced than in industrial nations. In the advanced banking markets, the considerable risk control work of recent years is considered to be paying off in higher awareness and better systems, though this is offset by fears that banks may be becoming too complacent or process-driven.

David Lascelles, the CSFI's co-director who ran the survey, said:

“It is ironic that people now see the greatest dangers in regulation when new types of risk are emerging all the time: hedge funds, derivatives, electronic fraud. Banks should not be distracted from these risks by box-ticking and form-filling.”

Notes to Editor

1. Full ranking information for Banana Skins 2005. 2004 rankings are in placed in brackets

- 1 Too much regulation (6)
- 2 Credit risk (2)
- 3 Corporate governance (8)
- 4 Derivatives (1)
- 5 Hedge funds (15)
- 6 Fraud (11)
- 7 Currencies (18)
- 8 High dependence on technology (12)
- 9 Risk management techniques (16)
- 10 Macro-economic trends (3)
- 11 Insurance sector problems (4)
- 12 Interest rates (9)
- 13 Money laundering (14)
- 14 Commodities (26)
- 15 Emerging markets (22)
- 16 Grasp of new technology (19)
- 17 Legal risk (-)
- 18 Equities (7)
- 19 Business continuation (5)
- 20 Banking market overcapacity (17)
- 21 Management incentives (20)
- 22 Political shocks (10)
- 23 Retail sales practices (21)
- 24 Rogue trader (23)
- 25 Payment systems (25)
- 26 Back office (24)
- 27 Merger mania (27)
- 28 Environmental risk (30)
- 29 Competition from new entrants (28)
- 30 Too little regulation (-)

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2. Hard copies of Banana Skins 2005 are available from the CSFI (price £25/\$45/€40), 5 Derby Street, London W1J 7AB, +44 (0)20 7493 0173. The report can also be downloaded free from www.csfi.org.uk

3. The CSFI is a non-profit think-tank, founded eleven years ago, which looks at challenges to and opportunities for the financial sector. It has an affiliate organisation in New York, the New York CSFI. For further details of the survey from the CSFI please contact David Lascelles on +44 (0)20 7493 0173 or +44 (0)7710 088658.

4. PricewaterhouseCoopers (www.pwc.com/uk) provides industry-focused assurance, tax and advisory services for public and private clients. More than 120,000 people in 144 countries connect their thinking, experience and solutions to build public trust and enhance value for clients and their stakeholders.

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