Scottish Financial Enterprise

Quarterly Survey of Scotland's Financial Services Industry

Sponsored by Capgemini

Quarter 1, 2006

SCOTTISH FINANCIAL ENTERPRISE

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This survey assesses, on a regular basis, the views of leaders of financial services businesses based in Scotland

Scottish Financial Enterprise – Q1 2006 Survey

Objectives

- To provide a shapshot of the views of financial services companies based in Scotland
- To gain insight into their performance over the last quarter and how this may change in the next
- To show how views differ between sectors
- To understand medium and long-term trends in the industry in Scotland

Quarterly Approach

- Survey is undertaken across the Scottish Financial Enterprise membership base
- Questionnaire is issued to all participants at the end of each quarter
- Results are collated and aggregated by Capgemini for Scottish Financial Enterprise
- Findings refer to this and previous quarters' surveys to measure perceived vs. actual performance
- No weighting is applied to differentiate between responses received from companies of different sizes

Confident outlook maintained as business volumes continue to exceed expectations

Summary results from across the financial services industry

General Business Confidence

- Businesses continue to be confident about prospects for the next quarter
- Confidence is also high for the 12 month forecast: 64% of companies expect their prospects to improve – up on the previous survey
- Asset Servicing companies and Investment Managers continue to be the most confident about prospects over the next 12 months

Business Volumes

- Business volumes exceeded expectations for the majority of companies in Q1 2006 with 68% reporting an increase on levels of business in the previous quarter
- Over 70% of companies reported that business volumes in Q1 2006 were up on the same period a year ago (Q1 2005)

Profitability

- Most survey respondents (63%) reported that profit margins for Q1 2006 were level compared with the previous quarter
- 40% of Investment Managers reported increased profitability in Q1 2006 compared with Q4 2005

Geographical Source of Business

- Turnover from Scotland, the rest of the UK, the rest of Europe and the US exceeded expectations in Q1 2006
- Businesses are pessimistic about short term prospects in the US – four in 10 expect a fall in turnover from this market in Q2 2006

Business Investment

- Three quarters of companies kept business investment level in Q1 2006, but slightly more companies than expected increased it
- Most companies (78%) expect business investment to remain constant in the coming quarter

Employee Levels

- Over a third of businesses increased employee levels during Q1 2006 and even more (41%) are expecting to do so in Q2
- The Asset Servicing sector reported the highest increase with 75% of companies growing headcount in Q1 2006

Other Factors affecting business

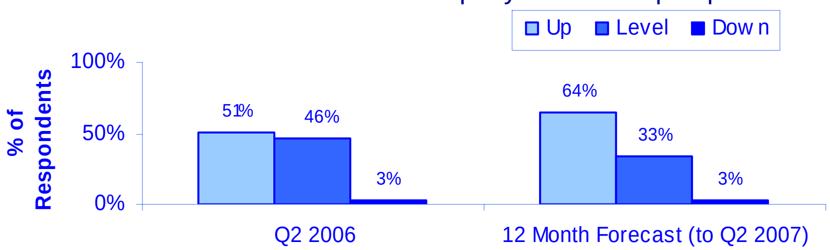
- The availability of professional and management staff is a growing concern and is highlighted by 49% of respondents, up ten percentage points compared with the last survey
- Concerns about competition, level of demand and customer confidence remain, however at slightly lower levels than in Q4 2005

41% of financial services companies expect to increase staffing levels in the next quarter but availability of professional and management staff is a growing concern

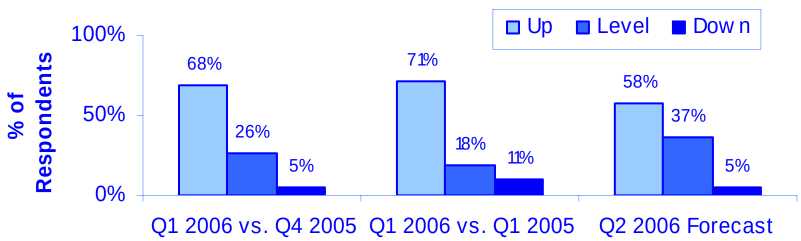
Nearly two thirds of companies expect prospects to continue to improve in the next 12 months

Data on Business Confidence, Volume and Profitability

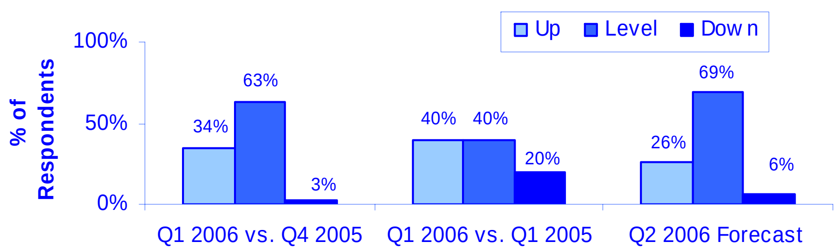
General Business Confidence: What is your overall confidence in your company's business prospects?



Volume: Excluding seasonal variations, how would you rate the level of business?



Profitability: How would you rate your margin?



Comment

General Business Confidence:

- General business confidence for the next quarter remains high
- Just over half of respondents believe that their business prospects will improve in Q2 2006
- Respondents are also optimistic about the 12 month forecast with almost two-thirds expecting prospects to improve

Volume:

- More companies than anticipated experienced growth in business volumes in Q1 2006. 68% reported an increase in volumes in the period – 20 percentage points higher than expectations from the previous survey
- Business levels are up for most respondents compared to the same period last year; 71% of respondents reported an increase
- Most companies expect that volumes will rise or stay level in Q2 2006

Profitability:

- Profitability in Q1 2006 was in line with the forecast in the previous survey, with just over a third of businesses increasing profit levels and nearly two thirds maintaining them in the period
- A similar outlook is predicted for Q2 2006
- 20% of firms reported that margins in Q1 2006 were down on the same period a year ago

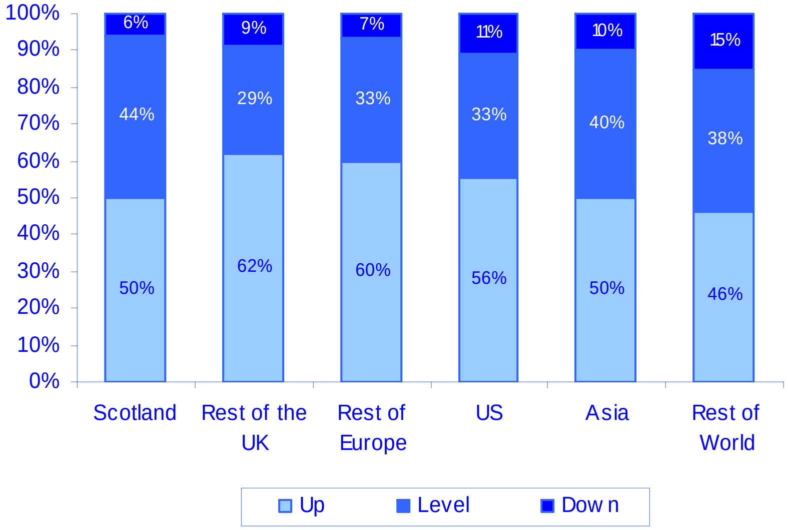
Profitability is in line with expectations, with most businesses expecting to maintain profit levels in the next quarter

Note: Percentages may not add up to 100% due to rounding

More companies than predicted experienced turnover growth in Europe and the US, with Scotland and the rest of the UK exceeding expectations the most

Q1 2006 Source of Turnover

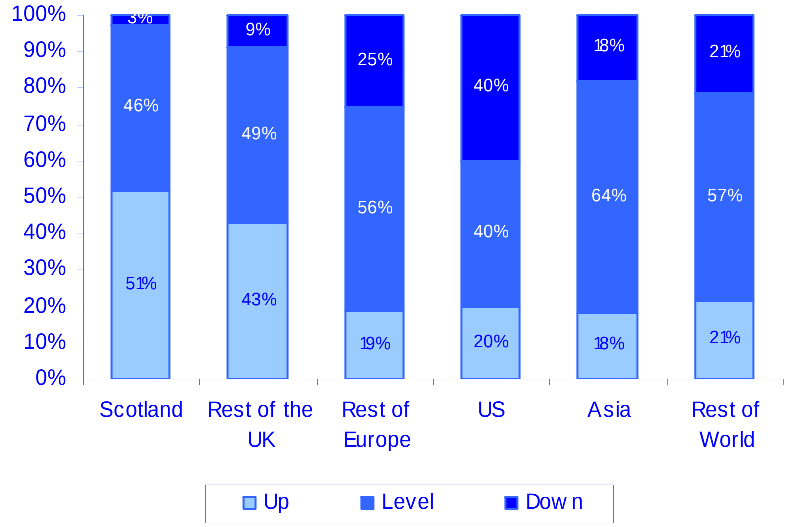
- **How would you rate your turnover that came from each of the following countries in the previous quarter?[1]**



- At least half of respondents reported that turnover increased in Europe (including Scotland/rest of the UK), the US and Asia in Q1 2006
- More companies than expected reported an increase in turnover from Europe (including Scotland/rest of the UK) and the US
- The UK performed particularly well against expectations, with significantly more companies (62%) reporting higher turnover growth from the UK market than was predicted in the last survey (43%)
- Although 20% of businesses expected a drop in turnover in Q1 2006 from Asia, only 10% saw a reduction in this market

Expected Q2 2006 Source of Turnover

- **What change do you expect to see this quarter?[1]**



- Over 90% of respondents expect turnover to be maintained or increased in Scotland and the rest of the UK in Q2 2006
- Most companies expect a level turnover from elsewhere in Europe, Asia and the rest of the world (excluding the US). This is despite many companies experiencing turnover growth in these regions in Q1 2006
- Businesses are pessimistic about short term growth in the US, with 40% of respondents expecting turnover to fall from this market in the coming quarter

Businesses expect turnover to continue to grow in Scotland and the rest of the UK, while they have lower expectations of other geographical markets in the next quarter

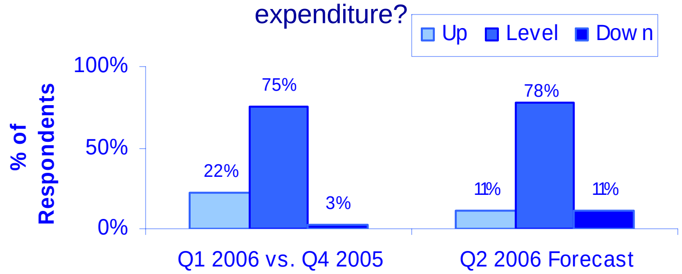
[1] The results only include organisations which generate revenues in the respective region

Note: Percentages may not add up to 100% due to rounding

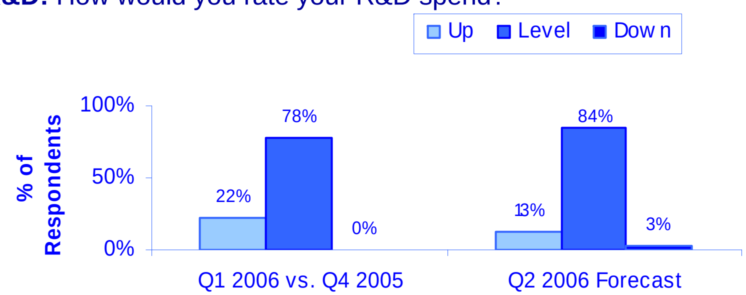
Three quarters of companies kept business investment level in Q1 2006 and slightly more than expected increased it

Data on Business Investment, R&D and Employment Levels

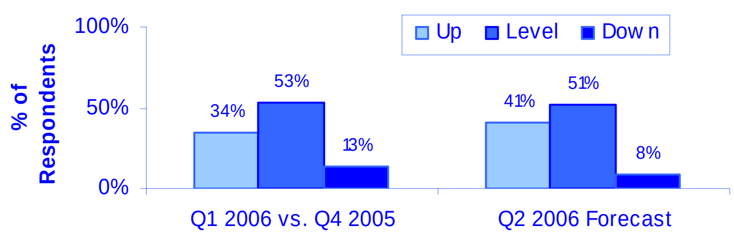
Business Investment: How would you rate your levels of capital expenditure?



R&D: How would you rate your R&D spend?



Employment Levels: Excluding seasonal variations, how does your headcount compare with the previous quarter?



Comment

Business Investment

- Most companies kept investment level in Q1 2006 and expect to do so again in the second quarter
- 22% of companies increased their investment levels in Q1 2006, six percentage points above expectations in the previous survey
- Fewer companies reined in capital expenditure in Q1 2006 than was anticipated in the last survey. Only 3% reduced business investment in comparison with the 19% of companies expected

Research and Development

- R&D spend remained level for the majority of companies in Q1 2006. The majority of respondents believe it will stay level in the second quarter
- However, a higher percentage of companies (22%) reported an increase in R&D spend in Q1 2006 compared with those expected in the previous survey (15%)
- No respondents reported a drop in R&D spend, in line with the previous survey's forecast

Employment Levels

- The number of companies reporting employment growth was mostly in line with predictions from the last survey
- Over a third of firms added jobs in Q1 2006 and 41% are expecting to increase staffing levels further in Q2
- Most companies maintained staff levels in Q1 2006 and 13% decreased headcount in the period
- Few companies (8%) are expecting to reduce their headcount in the next quarter

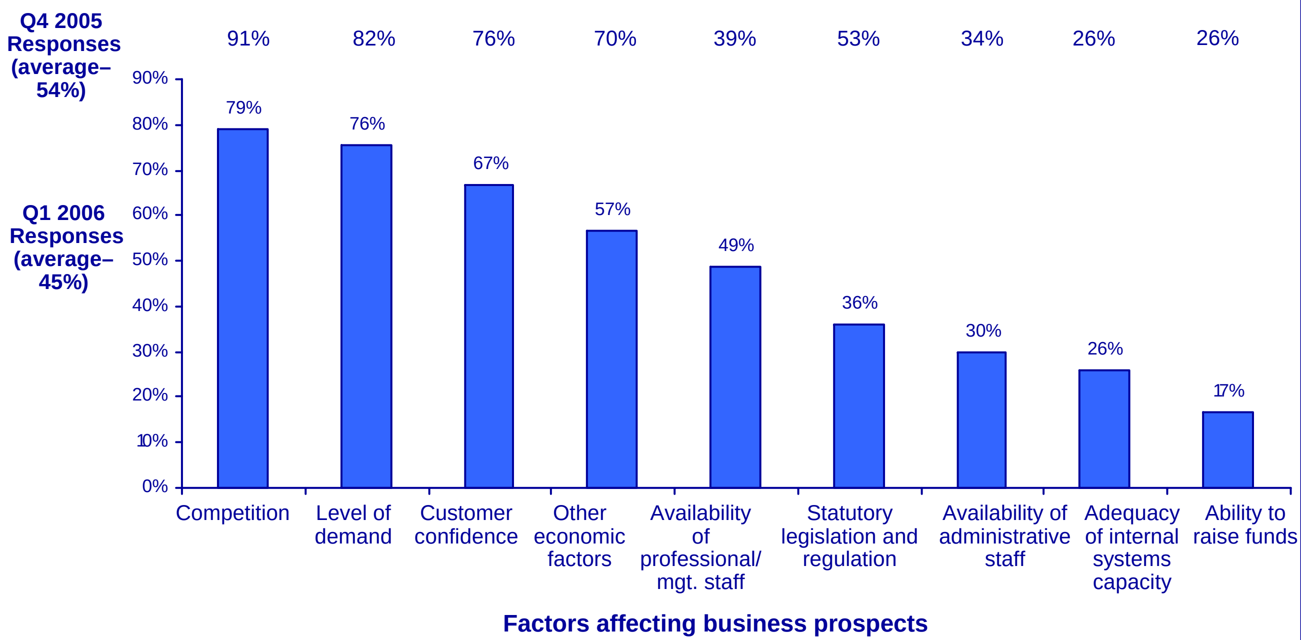
Over a third of businesses increased staffing levels in Q1 2006 and more are expecting to do so in the second quarter

Note: Percentages may not add up to 100% due to rounding

The availability of professional and management staff is an increasing concern for businesses in the next 12 months

Factors perceived to limit development / adversely affecting business in the next 12 months

Which of the following are likely to limit your ability to develop your business in the next 12 months[1]



[1] Note: multiple responses allowed

Commentary

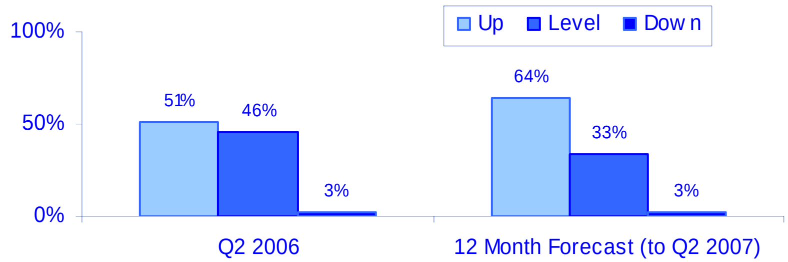
- Competition continues to be the most common factor perceived to limit business development in the next 12 months
- The availability of professional and management staff has grown as a concern since the last survey
- Overall levels of concern have generally reduced slightly since the previous quarter
- Concern about the ability to raise funds has reduced. Only 17% of respondents highlighted it as a limitation in Q1 2006 compared with 65% in Q3 last year

Factors such as competition, level of demand and customer confidence have reduced slightly as areas of concern

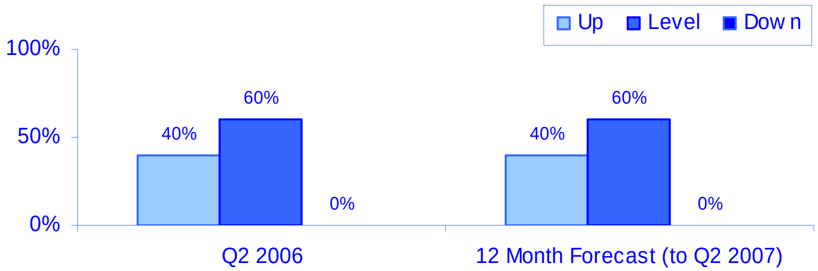
Confidence about prospects is strong in all of the main sectors of Scotland's financial services industry

What is your overall confidence in your company's business prospects?

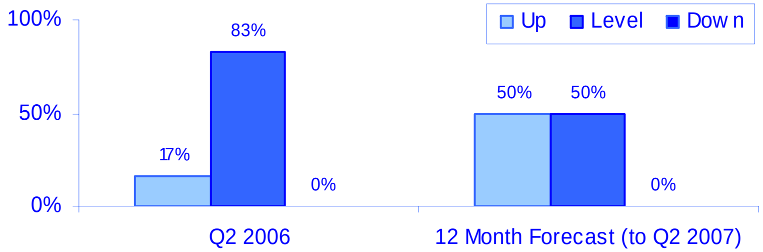
Overall market view



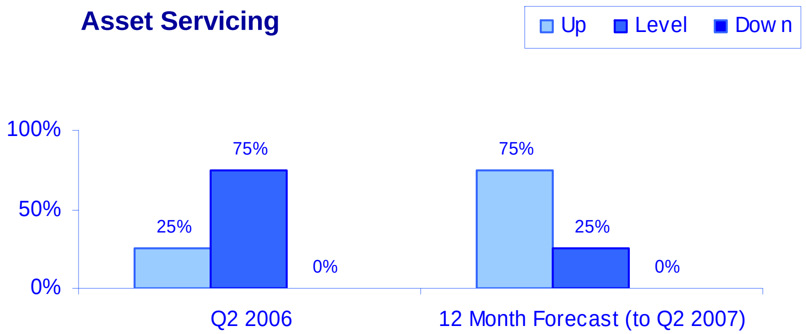
Banks and Building Societies



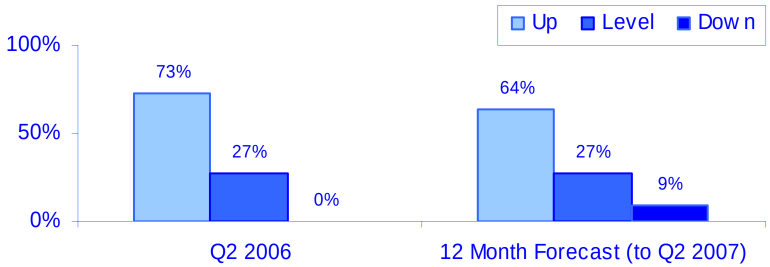
General Insurance, Life Assurance and Pensions



Asset Servicing



Investment Managers



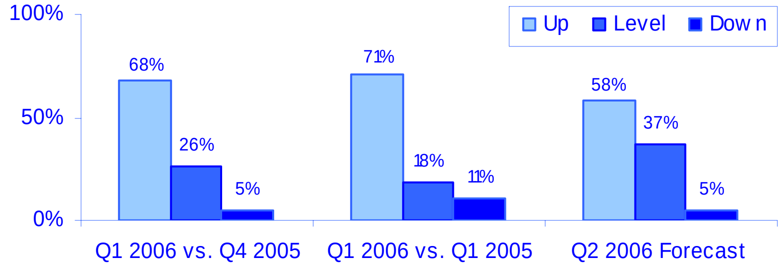
Asset Servicing companies and Investment Managers continue to be the most confident about the next 12 months with the large majority of firms expecting prospects to improve

Note: Percentages may not add up to 100% due to rounding

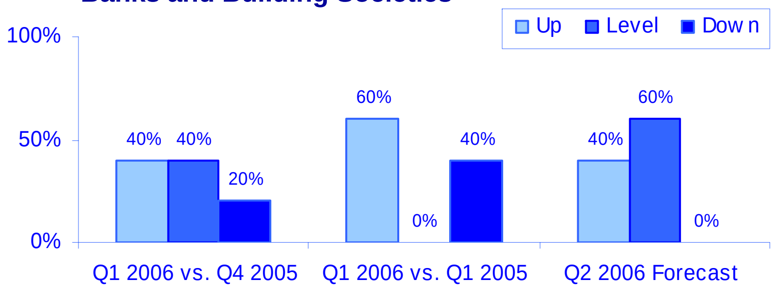
All Asset Servicing companies and most Investment Managers reported volume growth in Q1 2006

How do you rate the level of business?

Overall market view



Banks and Building Societies



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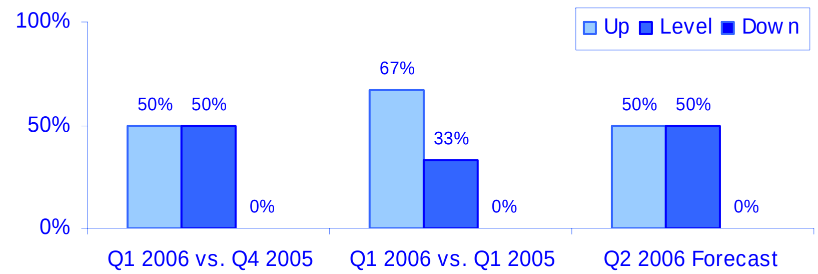
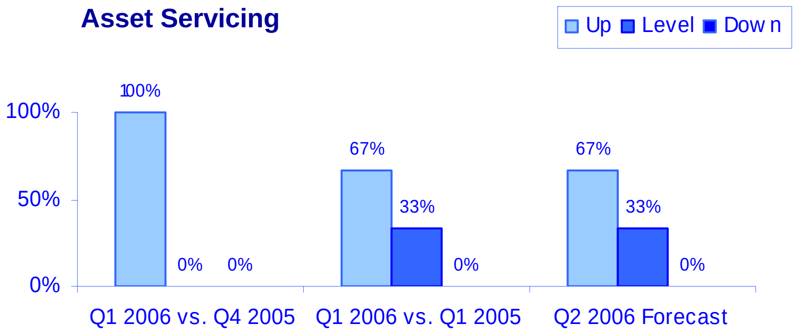
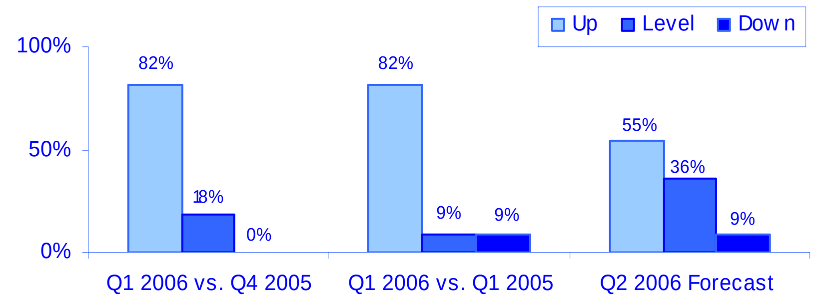


Asset Servicing



Investment Managers



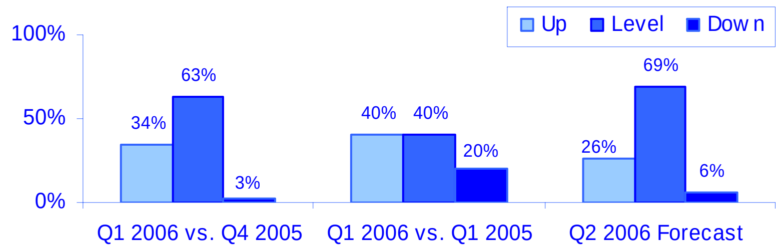
Almost all companies in the main sectors of the industry are expecting business volumes to be up or level in the second quarter of the year

Note: Percentages may not add up to 100% due to rounding

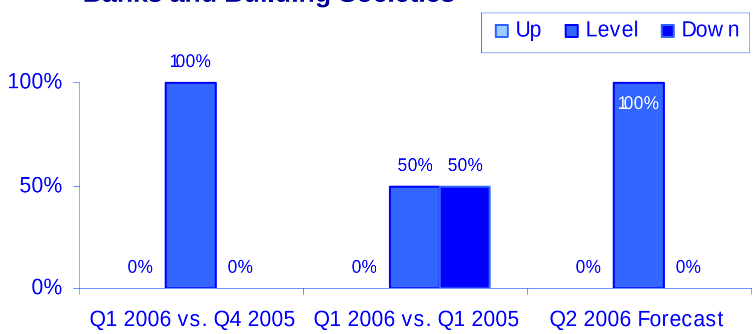
The majority of companies in the main financial services industry sectors reported level profit margins in Q1 2006

How do you rate your profit margin?

Overall market view



Banks and Building Societies



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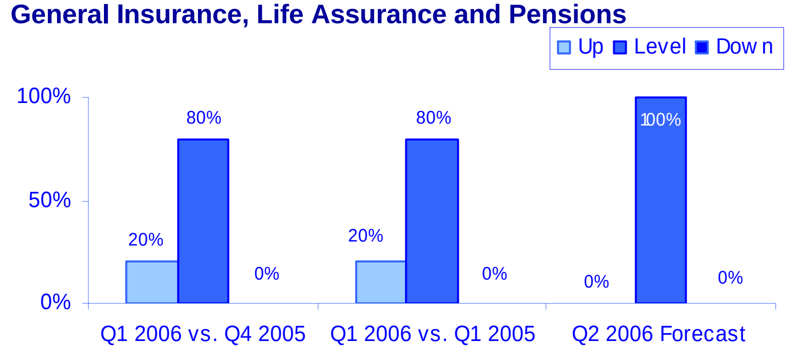
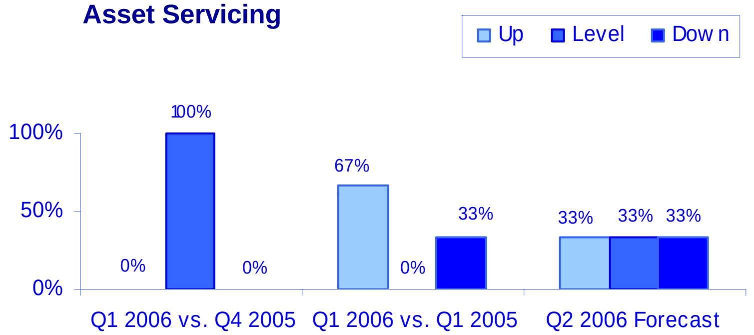
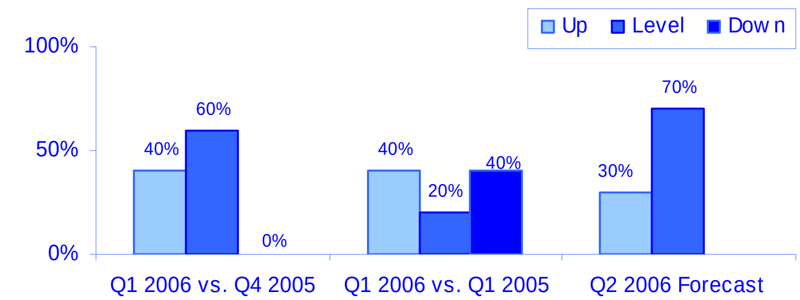


Asset Servicing



Investment Managers



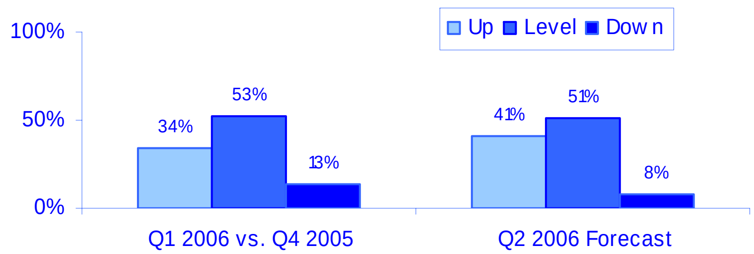
The outlook for Q2 2006 is similar, with some Asset Servicing companies and Investment managers expecting to increase profit margins

Note: Percentages may not add up to 100% due to rounding

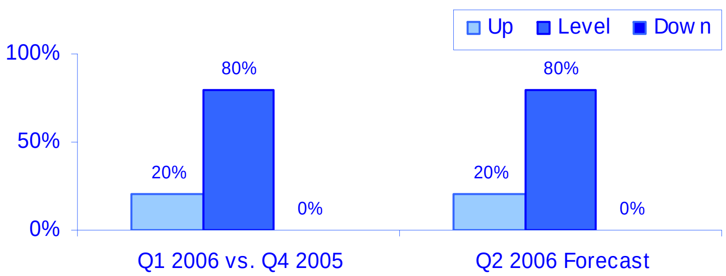
Changes in employment levels varied across the sectors in Q1 2006; 75% of Asset Servicing companies increased staffing levels

How would you rate employment levels?

Overall market view



Banks and Building Societies



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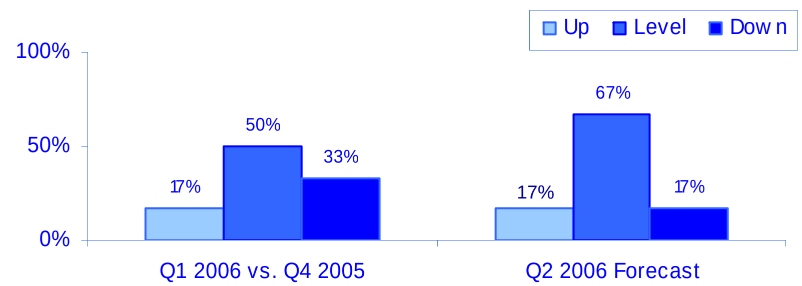
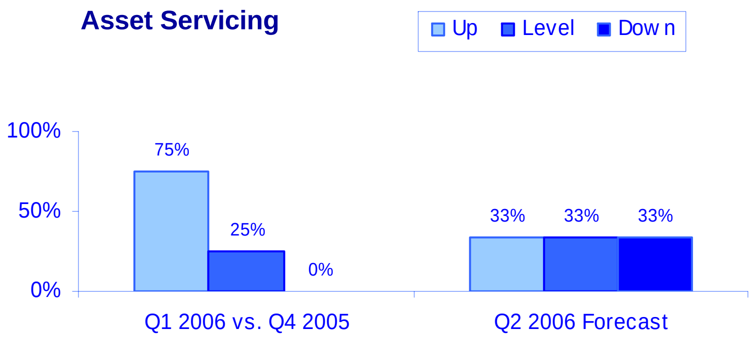
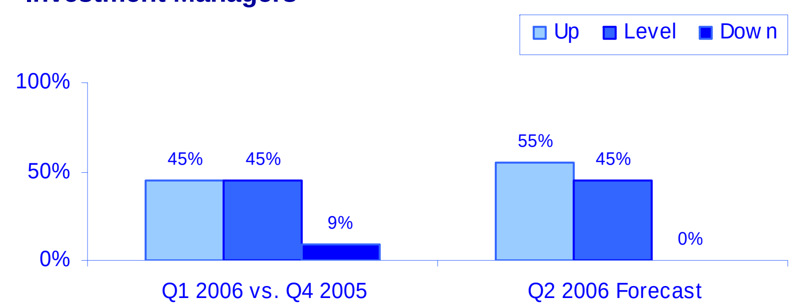


Asset Servicing



Investment Managers



Most companies across the sectors expect to increase or maintain employment levels in the next quarter; 55% of Investment Managers expect to hire more staff

Note: Percentages may not add up to 100% due to rounding