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Europe finally catching up on the US?

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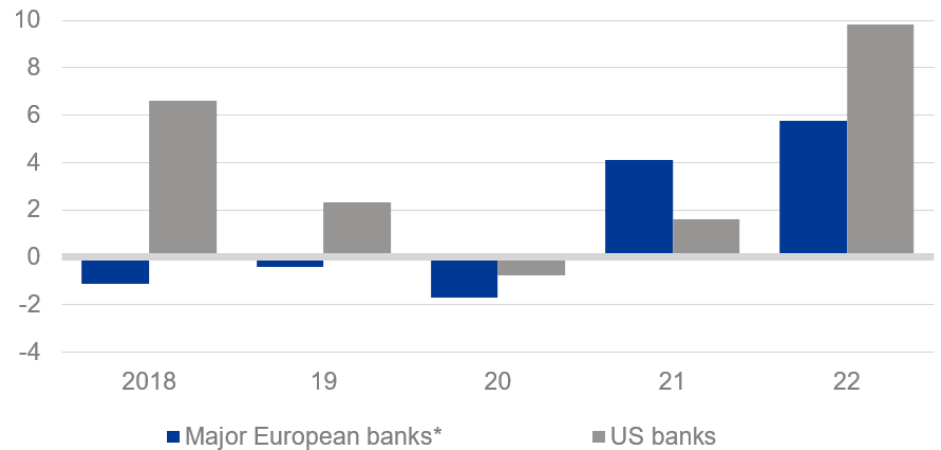
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Deutsche Bank Research Management
Stefan Schneider

For more than a decade, European banks have sought to catch up and narrow the gap to their US peers. For many years, they were not particularly successful, due to a number of reasons: economic growth in the US outpaced that in Europe, interest rates were consistently higher (and never negative) on the other side of the Atlantic, and restructuring and capital raising needs were greater in Europe which constrained the banks' ability to expand their business. In the past few years, however, European banks' performance has indeed improved and they have not just made substantial progress, but also seem well positioned to finally reduce the distance to their US competitors.

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9M revenues, % yoy



* excl. UK institutions

Sources: FDIC, company reports, Deutsche Bank Research

In the first nine months of this year, the major European banks recorded a revenue increase of 6% yoy, driven by an 11% surge in net interest income. Post-tax profits still fell 16% from a strong prior-year figure, due to a rise in loan loss provisions (+16%) and administrative expenses (+6%) as well as one-off effects. In the US, the banking industry as a whole reported an even larger jump in net interest income (+16%), driving up total revenues by 10%. Nevertheless, net income retreated by a similar extent as in Europe (-10%), mainly because of increased loss provisions and higher expenses (not least the result of hefty inflation).





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In some ways, banks' fortunes on both sides of the pond will be shaped by the same factors in the coming months: both regions are expected to soon enter a relatively mild recession (or could be in one already), and the Fed as well as the ECB may continue to hike interest rates to levels not seen since the financial crisis. But the upside might be larger for European banks. They had gotten used to operating even under negative nominal rates, which now seem a feature of the past; and although the peak level may be higher, rates may also start falling more quickly in the US than in the EMU. With elevated inflation likely to persist for longer than many thought initially, European banks are on course to benefit from a fundamental normalisation of interest rates, potentially more so than their US peers.

See also [European banks in a sweet spot](#)



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