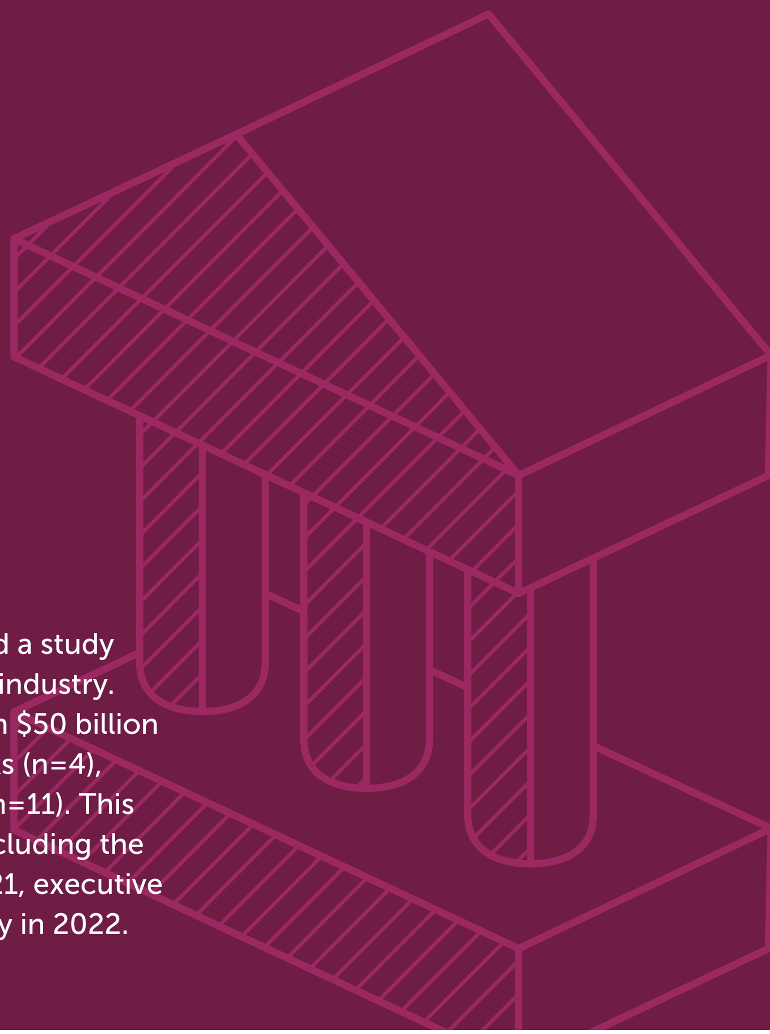
Compensation Advisory Partners

Industry Report // 2021-2022

Banking



Compensation Advisory Partners (CAP) conducted a study of executive compensation trends in the banking industry. The study includes 18 U.S. banks with greater than $50 billion in assets across three groups: Money Center banks (n=4), Custody banks (n=3), and Super Regional banks (n=11). This report summarizes the findings of CAP's study, including the relationship between pay and performance in 2021, executive compensation trends, and outlook for the industry in 2022.

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Key Themes

1 **2021 Pay and Performance Outcomes**

Chief executive officer (CEO) compensation increased 21% at median, primarily through higher incentives. Increases in CEO pay were in line with strong 2021 earnings, which were buoyed by releases of loan loss provisions taken in 2020.

2 **Incentive Plan Design Trends**

All banks in this study considered Diversity, Equity and Inclusion (DE&I) progress as part of the annual incentive decision in 2021, typically evaluated on a qualitative basis.

3 **Special Retention Awards**

The use special one-time long-term incentive awards increased among large financial services companies, including the banks in our study, in 2021. These awards, in some cases, received pushback from shareholders and proxy advisory firms that resulted in lower Say-on-Pay outcomes.

4 **Looking Ahead**

The performance outlook for 2022 is less certain. Results may vary significantly based on business mix and balance sheet makeup.

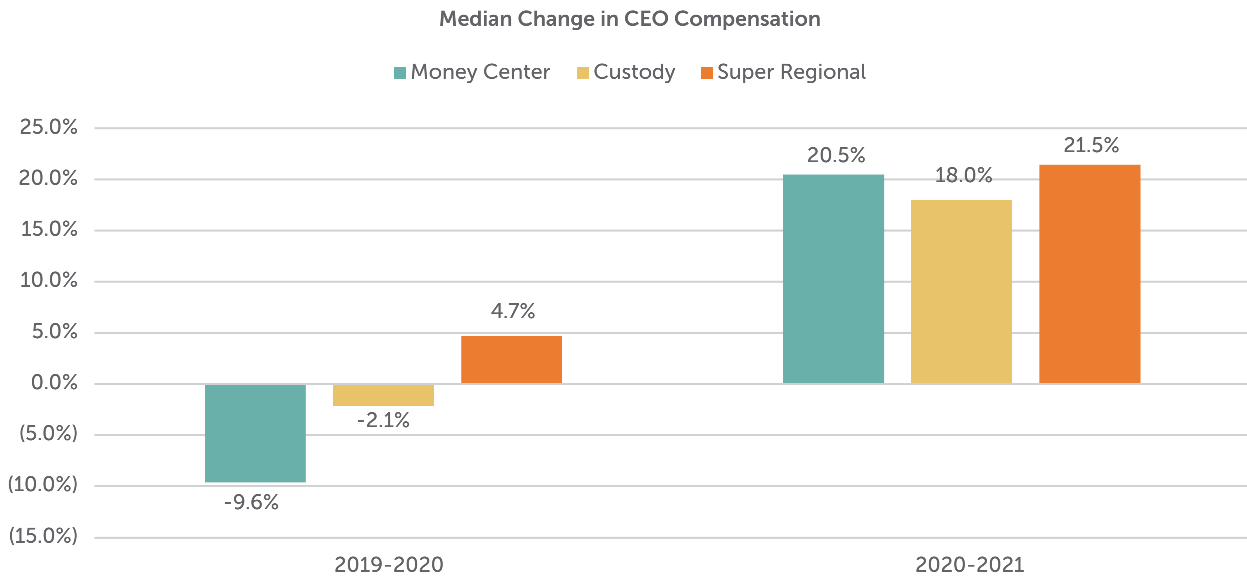
2021 Pay and Performance Outcomes – Significant Pay Increases for Strong Results

The banks in CAP's study had strong bottom line results in 2021. Earnings per share (EPS) and Return on Equity (ROE) improved significantly versus 2020 as the credit environment improved, and banks reversed pandemic-related loan loss provisions from 2020. Over the same period, Pre-Provision Net Revenue (PPNR), which does not include the impact of loan loss provisions, was down at median, though several banks in our study grew PPNR versus 2020 primarily through increases in fee income. 1-year Total Shareholder Return (TSR) was strong over this period. 2021 TSR for the banks in CAP's study was +38 percent, at median, while the S&P 500 returned +29 percent.

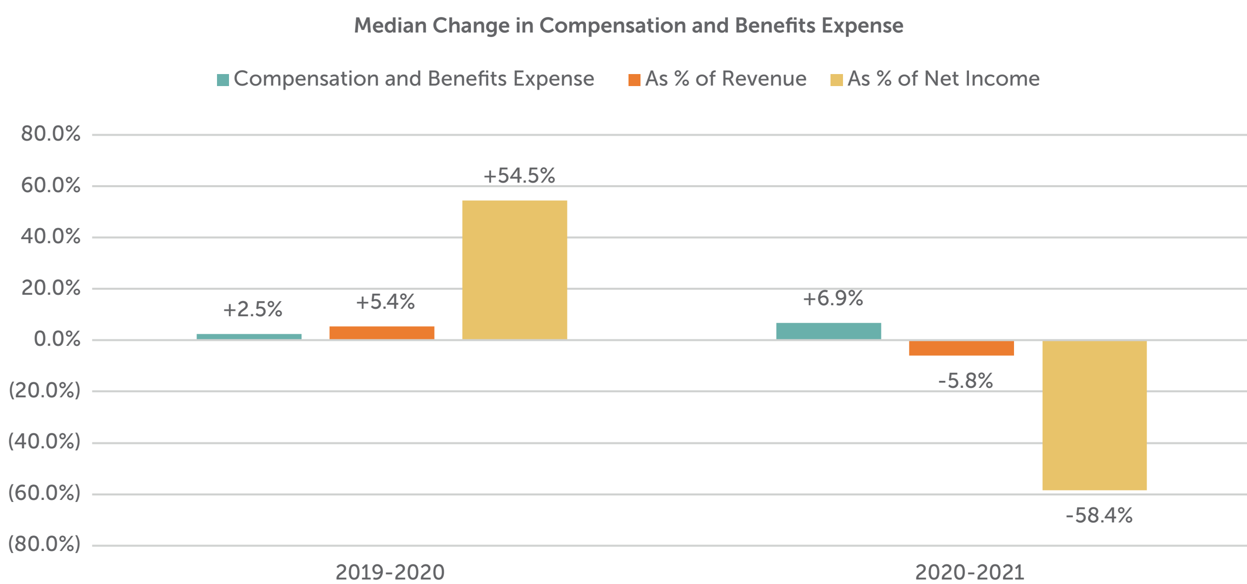
The chart below summarizes median performance results for the banks in CAP's study:

Metric	Median Percent Change	
	Year Ended December 31, 2020	Year Ended December 31, 2021
Earnings per Share	-29.5%	+96.2%
Pre-Provision Net Revenue	-0.2%	-5.2%
Return on Equity (Basis Point Change)	-371 bps	+527 bps
1-Year Total Shareholder Return	-11.4%	+37.6%
3-Year Total Shareholder Return (Cumulative)	-3.9%	+58.7%

Source: S&P Capital IQ Financial Database.



In 2021, total direct compensation (i.e., the sum of base salary, annual cash bonus, and awarded long-term incentives), increased 21 percent, 18 percent, and 22 percent at median for the money center, custody, and super regional banks, respectively. Banks primarily delivered increases through incentive compensation. 2021 cash bonuses were up 36 percent at median as 2021 results surpassed target performance goals and improved significantly versus 2020 due primarily to the quicker than expected economic recovery and resulting releases of loan loss provisions. Several banks in CAP's study even disclosed making negative adjustments to incentive plan payouts to recognize the benefit of the releases of loan loss provisions. This stands in stark contrast to 2020 where companies generally failed to meet targets set prior to the start of the pandemic and funded bonuses below target and below 2019 bonuses. Long-term incentives also increased significantly at median (i.e., +21 percent), compared to 2020 when banks increased long-term incentives more modestly (i.e., +5 percent at median).



Compensation and benefits expense increased on an absolute basis in both 2020 and 2021. However, as a percentage of revenue and net income, compensation and benefits expense increased in 2020 and decreased in 2021. This likely demonstrates that while 2020 was a challenging performance year, banks maintained a level of compensation necessary to retain key talent. In 2021, banks increased incentives to reward for improved earnings and recognize the intensely competitive talent market, but did so at a reasonable level relative to revenue and earnings growth.

Incentive Plan Design Trends – Focus on DE&I

Most banks in our study did not make changes to annual or long-term incentive plan metrics or structure in 2021. One area that continues to evolve is how banks tie incentives to Environmental, Social, and Governance (ESG) considerations. As companies and shareholders spend more time focusing on ESG strategies, companies are increasingly incorporating ESG metrics into incentive plans to support these strategies. To-date banks have primarily focused on DE&I in incentive plans. All of the banks in our study disclose considering DE&I achievements as part of the incentive decision-making process. Most banks include DE&I in the individual or strategic component of the annual incentive plan and evaluate results on a qualitative basis. Specific metrics include diversity in hiring, use of diverse suppliers, and employee engagement. Several banks in our study also disclose considering other ESG factors (e.g., aligning investing activities to climate commitments) as part of the annual incentive determination.

Special Equity Awards

We noted an increased use of special one-time equity awards among banks in 2021 and 2022 to-date. Such awards are typically reserved for special situations, such as supporting retention and incentivizing significant growth or business transformation. These awards, particularly those that provide executives with the opportunity to earn significant value, are often subject to longer-term vesting periods (i.e., five or more years) and payout based on the achievement of shareholder value creation goals. Shareholders and proxy advisory firms often push back on these types of awards, demonstrated by the decline in Say-on-Pay support in 2022 for many of the banks that granted special equity awards in 2021.

One notable example in our study is JPMorgan. The bank granted awards worth $53 million and $28 million to the CEO and President & COO, respectively, to support retention of these key leaders. The awards consisted of stock appreciation rights that vest after five years. Likely due to the significant value of these awards, both major proxy advisory firms, Institutional Shareholder Services (ISS) and Glass Lewis, recommended that shareholders vote against JPMorgan's Say-on-Pay proposal and JPMorgan failed Say-on-Pay, receiving only 31% support from shareholders.

Looking Ahead to the Second Half of 2022

2021 was a strong earnings year for banks and executive compensation levels reflected that. The outlook for 2022 is less certain and performance results may vary significantly based on business mix and balance sheet makeup. Provision releases, which had a significant positive impact on bank earnings in 2021, will likely not be available to banks in 2022. Additionally, the rising interest rate environment, inflation, and macroeconomic uncertainty are expected to impact bank performance in 2022.

The Federal Reserve has increased interest rates significantly in 2022 and anticipates additional rate hikes in the second half of the year. Rising interest rates are expected to drive higher net interest income but decrease demand for loans. The degree to which the rate environment benefits 2022 earnings will vary by bank based on the sensitivity of the balance sheet to increases in interest rates and the cost of funds.

The volume and value of mergers and acquisitions (M&A) transactions are expected to decline in 2022 due to economic uncertainty, inflation, and rising interest rates. This will adversely impact fee income for investment banking businesses.

In light of these dynamics, the first half of 2022 told a different performance story than 2021. PPNR is slightly up at median, likely due to increased interest rates, and EPS is down at median without the benefit of provision releases. Total shareholder return through the second quarter for the banks in our study is down approximately 20% at median, commensurate with the S&P 500. At the same time, the current talent market is intensely competitive, particularly in key areas for banks such as digital and commercial banking. As we approach the end of 2022, banks will need to balance aligning pay with 2022 performance results and shareholder returns, which may be down versus 2021, with the need to attract and retain critical talent.

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Banks in CAP's Study (n=18)

Money Center Banks

- Bank of America Corporation
- Citigroup, Inc.
- JPMorgan Chase & Co.
- Wells Fargo & Company

Custody Banks

- The Bank of New York Mellon Corporation
- Northern Trust Corporation
- State Street Corporation

Super Regional Banks

- Citizens Financial Group, Inc.
- Comerica, Inc.
- Fifth Third Bancorp
- Huntington Bancshares, Inc.
- KeyCorp
- M&T Bank Corporation
- The PNC Financial Services Group, Inc.
- Regions Financial Corporation
- Truist Financial Corporation
- U.S. Bancorp
- Zions Bancorporation