

Half-yearly Report

for the 2016 financial year

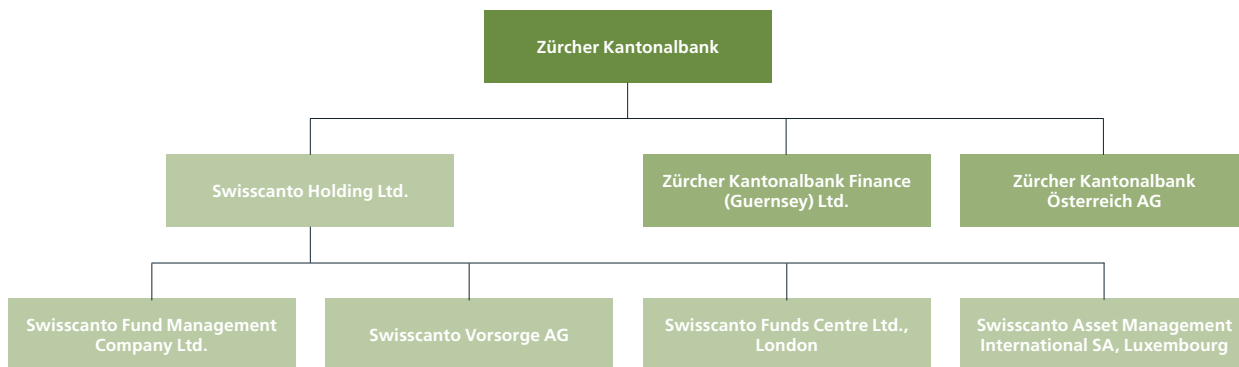
At a glance

About us

Zürcher Kantonalbank is an independent public-law institution of the canton of Zurich. It fulfils a public service mandate that entails providing financial services for the public and assisting the canton in the economic, social and environmental arenas. This mandate requires the bank to be responsible in its use of natural resources and to ensure that its actions comply with the demands of social and environmental sustainability.

As a full-service bank with a strong regional anchoring as well as national and international links, Zürcher Kantonalbank has a leading position in the Greater Zurich area. It has a market penetration of around 50 percent in retail as well as corporate banking. The corporate (endowment) capital provided by the canton is a component of Zürcher Kantonalbank's equity. Should these resources prove inadequate, the canton additionally provides a guarantee for all of the bank's non-subordinated liabilities.

Scope of consolidation



About the figures:

The amounts stated in this report have been rounded. The total may therefore vary from the sum of the individual values.

The following rules apply to the tables:

0	(0 or 0.0) Figure is smaller than half the unit of account used
-	Figure not available or not meaningful
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The Zürcher Kantonalbank in figures (group)

Income statement	in CHF million	1st half 2016	1st half 2015	Change 2016/2015 in %
Result from interest operations		582	583	-0.2
Result from commission business and services		360	315	14.5
Result from trading activities and the fair value option		183	180	1.6
Other result from ordinary activities		23	21	12.3
Operating income		1,149	1,099	4.6
Operating expenses		-684	-676	1.1
Value adjustments on participations and depreciation and amortisation of tangible fixed assets and intangible assets		-65	-49	31.6
Changes to provisions and other value adjustments, and losses		-5	-7	-33.0
Operating result		395	366	8.0
Extraordinary income		2	35	-93.9
Taxes		-4	-7	-38.5
Consolidated profit (result of the period)		393	393	-0.1
Balance sheet (before distribution of net profit)	in CHF million	30.06.2016	31.12.2015	
Total assets		151,611	154,410	-1.8
Mortgage loans		75,399	73,623	2.4
Amounts due in respect of customer deposits		77,762	80,820	-3.8
Provisions		572	584	-2.0
Equity		10,496	10,429	0.6
Key figures	in %	1st half 2016	1st half 2015	
Return on equity (ROE)		7.7	7.9	
Cost/income ratio (CIR) ¹		59.1	61.5	
Common equity Tier 1 ratio (CET1)		15.3	16.1	
Core capital ratio (Tier 1)		16.2	17.1	
Total capital ratio		17.3	18.2	
Leverage ratio ²		7.1	6.4	
Liquidity coverage ratio (LCR) ³		115.6	124.0	
Assets under management	in CHF million	30.06.2016	31.12.2015	
Total assets under management ⁴		260,213	257,505	1.1
Personnel / banking outlets	Number	30.06.2016	31.12.2015	
Headcount after adjustment for part-time employees, as on reporting date		5,172	5,179	-0.1
Banking outlets ⁵		90	91	
Rating agencies	Rating	30.06.2016	31.12.2015	
Fitch		AAA	AAA	
Moody's		Aaa	Aaa	
Standard & Poor's		AAA	AAA	
Scope of consolidation	Share in %	30.06.2016	31.12.2015	
Zürcher Kantonalbank Finance (Guernsey) Ltd.		100	100	
Zürcher Kantonalbank Österreich AG		100	100	
Swisscanto Holding Ltd.		100	100	

¹ Charged: Cost-income ratio (excl. changes in value adjustments for default risk and losses from interest operations).

² Leverage ratio for systemically important banks pursuant to Art. 133 et seq. CAO

³ Monthly averages for second quarter.

⁴ Restated following a change in segmentation of business partners and customer deposits.

⁵ Including branches of Zürcher Kantonalbank Österreich AG in Salzburg and Vienna as well as six automated banks.

Business performance

Zürcher Kantonalbank reports a pleasing result for the Group in the first half of 2016. All earnings components had a positive effect.

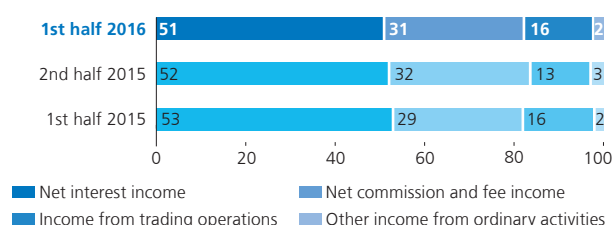
In the first six months of the financial year, Zürcher Kantonalbank exceeded the success of the same period of the previous year by 8 percent, or CHF 29 million. With better-than-expected results from interest income and in the trading business as well as only a few extraordinary components (previous year: property sales), the bank matched the positive half-yearly profit of the previous year of CHF 393 million.

The return on equity was 7.7 percent (1st half 2015: 7.9 percent). The cost/income ratio improved to 59.1 percent (1st half 2015: 61.5 percent).

Diversified income structure

Operating income in the first half of 2016 was CHF 1,148.8 million, representing an increase of CHF 50.0 million, or 4.6 percent, compared to the first half of 2015.

Fig. 1: Income structure of Zürcher Kantonalbank (in %)



The diversified income structure proved successful in the first half of 2016, a period characterised by uncertain and volatile market conditions. With a share of 50.7 percent, interest operations continues to be the bank's most important income stream followed by commission and fees at 31.4 percent. The trading business contributed 15.9 percent to operational income as the third income stream.

Moderate interest result

The Swiss National Bank's negative interest rates remain a major challenge. Nevertheless, in the first half of 2016 the bank was able to achieve interest income of CHF 582.2 million, which was above expectations. The negative interest paid by Zürcher Kantonalbank to the Swiss National Bank amounted to CHF 30.8 million.

Improved income from commission and fees

In the first half of 2016 the bank achieved income of CHF 360.5 million from commission and fees. This corresponds to an increase of CHF 45.7 million, or 14.5 percent, compared to the same period in the previous year, despite challenging conditions overall.

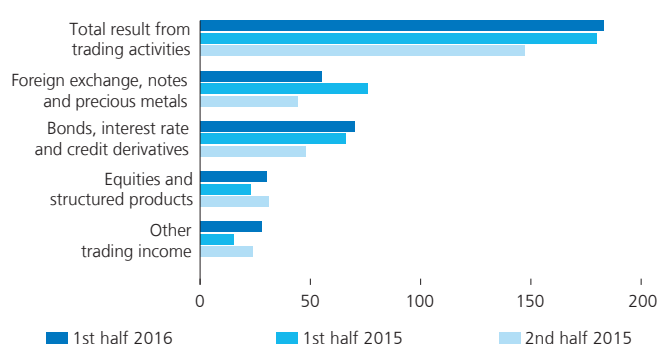
The share from the securities and investment business remains the driving force with regard to income from commission and fees.

Positive trading business

In a volatile and challenging market environment and with trading activities clearly focused on the customer business, a pleasing result of CHF 183.1 million was achieved in the income from trading operations (first half 2015: CHF 180.1 million).

Market risks in the trading book (value-at-risk with a 10-day holding period) remained low at an average level of CHF 12 million (average for the first half 2015: CHF 20 million).

Fig. 2: Trading income by segment (in CHF million)



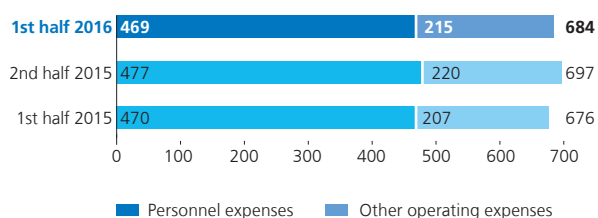
Stable operating expenses

Operating expenses in the first half of this year amounted to CHF 684.1 million. The slight increase compared to the first half of 2015 (up 1.1 percent) can primarily be attributed to the fact that, in the previous year, the acquired Swisscanto Group was only included in the consolidated result from April onwards.

The canton is compensated with CHF 10.5 million for the first six months of 2016 for the state guarantee, which is also included in operating expenses. As such this figure was in line with the compensation for the first half of 2015.

As at 30 June 2016, headcount on a full-time equivalent basis stood at 5,172 (end 2015: 5,179).

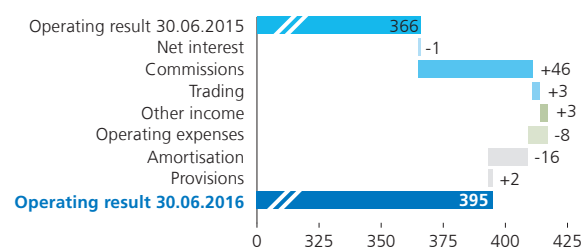
Fig. 3: Development of operating expenses (in CHF million)



Higher operating profit

The positive development in earnings was able to offset the slightly higher operating expenses. This led to an operating result of CHF 394.9 million, around CHF 29.2 million, or 8.0 percent higher than the first half of 2015.

Fig. 4: Development of operating profit (in CHF million)



Slightly increased allowances coupled with lower provisions

Zürcher Kantonalbank assesses default risks as well as all other identifiable risks on a constant basis. Where necessary, the bank creates corresponding allowances and provisions.

The net creation of allowances owing to default risks, and losses from interest operations were in line with expectations and amounted to CHF 9.6 million in the first half this year. The increase compared to the same period in the previous year reflects the ongoing challenging economic environment and the strength of the Swiss franc. Expenditure for provisions and other allowances was CHF 4.8 million, or around 33 percent less than the first half of 2015.

Allowances on participations and amortisation of tangible fixed assets and intangible assets amounted to CHF 65.0 million (first half 2015: CHF 49.4 million). This figure also includes the regular depreciation of

goodwill from the acquisition of the Swisscanto Group, which only had an impact on three out of the first six months of 2015.

Pleasing half-year result

In the first half of 2016 Zürcher Kantonalbank achieved group net income comparable to the same period in the previous year of CHF 392.7 million. Thanks to the high operating income, it clearly exceeded expectations without any notable extraordinary income items.

Stable total assets

As at 30 June 2016, total assets decreased by around 2 percent to CHF 151.6 billion, compared to 31 December 2015.

There was no material change to the balance sheet structure. Mortgage loans are still the largest balance sheet item on the assets side, while customer deposits continued to dominate liabilities. This reflects Zürcher Kantonalbank’s excellent refinancing situation.

High liquidity

The bank held liquid assets of CHF 31.6 billion at the mid-year point (31 December 2015: CHF 32.5 billion), primarily composed of deposits with the Swiss National Bank.

These deposits serve to meet liquidity requirements, which are particularly high for systemically relevant banks such as Zürcher Kantonalbank.

Appealing mortgage growth

Mortgage loans amounted to CHF 75.4 billion, an increase compared to the end of 2015 of CHF 1.8 billion, or 2.4 percent.

Zürcher Kantonalbank continues to focus on quality in its lendings. This is why the affordability calculation is based on an imputed mortgage rate of 5 percent even in the current interest rate environment. The share of fixed mortgages was around 76 percent, which reflects the current market situation.

At CHF 7.3 billion in mid-2016, funds due from customers were down slightly (CHF 7.7 billion at year-end 2015).

Slight decline in customer deposits

Customer deposits include money in savings and investment accounts as well as other liabilities to customers. As at 30 June 2016 these amounted to CHF 77.8 billion compared to CHF 80.8 billion at the end of 2015.

Increase in assets under management

Assets under management grew by CHF 2.7 billion in the first half of the year, to CHF 260.2 billion.

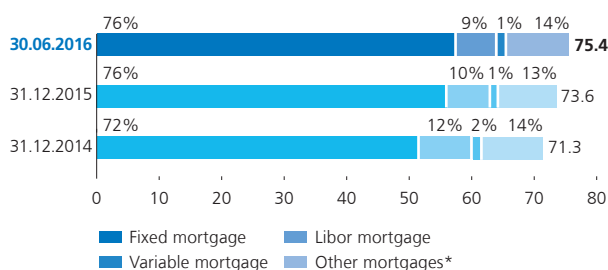
Capital adequacy and liquidity disclosures

The capital adequacy and liquidity disclosures are posted in a separate report on the internet at www.zkb.ch («Disclosures»).

Outlook

Zürcher Kantonalbank is characterised by its broadly diversified business model and its proximity to customers. It continues to be awarded the highest rating by three rating agencies. Zürcher Kantonalbank is well prepared for the second half of the year, which will continue to be defined by economic challenges and uncertainties in international markets. Particular attention will be paid to interest rate and currency trends. Zürcher Kantonalbank still expects a pleasing result for 2016, provided there is no unexpected economic downturn.

Fig. 5: Fixed and variable mortgages (in % and in CHF billion)



* mainly starter mortgages and fixed advances secured by real estate

Group income statement

as at 30 June 2016

<i>in CHF million</i>	1st half 2016	1st half 2015 ¹	Change	Change in %
Result from interest operations				
Interest and discount income	718	713	5	0.7
Interest and dividend income from financial investments	30	33	-2	-7.4
Interest expenses	-156	-162	6	-3.5
Gross result from interest operations	592	584	8	1.4
Changes in value adjustments for default risk and losses from interest operations	-10	-0	-9	-
Subtotal net result from interest operations	582	583	-1	-0.2
Result from commission business and services				
Commission income from securities trading and investment activities	379	313	66	21.0
Commission income from lending activities	26	24	2	9.4
Commission income from other services	62	54	9	16.1
Commission expenses	-106	-76	-31	40.8
Subtotal result from commission business and services	360	315	46	14.5
Result from trading operations and the fair value option	183	180	3	1.6
Other result from ordinary activities				
Result from the disposal of financial investments	0	3	-3	-98.8
Income from participations	12	13	-2	-13.3
– of which from equity-consolidated participations	0	2	-2	-98.3
– of which from other non-consolidated participations	12	12	0	0.3
Result from real estate	5	3	2	47.0
Other ordinary income	8	6	2	40.5
Other ordinary expenses	-1	-5	4	-70.8
Subtotal other result from ordinary activities	23	21	3	12.3
Operating income	1,149	1,099	50	4.6
Operating expenses				
Personnel expenses	-469	-470	1	-0.1
Other operating expenses	-215	-207	-8	4.0
Subtotal operating expenses	-684	-676	-8	1.1
Value adjustments on participations and depreciation and amortisation of tangible fixed assets and intangible assets	-65	-49	-16	31.6
Changes to provisions and other value adjustments, and losses	-5	-7	2	-33.0
Operating result	395	366	29	8.0
Extraordinary income	3	35	-32	-92.0
Extraordinary expenses	-1	-0	-1	-
Taxes	-4	-7	3	-38.5
Consolidated profit (result of the period)	393	393	-1	-0.1

¹ Including Swisscanto Holding Ltd. since 1 April 2015.

Group balance sheet

before distribution of net profit, as at 30 June 2016

<i>in CHF million</i>	30.06.2016	31.12.2015	Change	Change in %
Assets				
Liquid assets	31,590	32,497	-907	-2.8
Amounts due from banks	5,950	6,011	-61	-1.0
Amounts due from securities financing transactions	12,477	14,966	-2,489	-16.6
Amounts due from customers	7,341	7,673	-333	-4.3
Mortgage loans	75,399	73,623	1,776	2.4
Trading portfolio assets	9,671	10,226	-555	-5.4
Positive replacement values of derivative financial instruments	2,528	2,897	-368	-12.7
Other financial instruments at fair value	220	220	0	0.0
Financial investments	4,291	4,320	-29	-0.7
Accrued income and prepaid expenses	387	294	93	31.5
Non-consolidated participations	148	161	-13	-8.0
Tangible fixed assets	822	860	-38	-4.4
Intangible assets	114	124	-10	-7.8
Other assets	672	538	135	25.0
Total assets	151,611	154,410	-2,799	-1.8
Total subordinated claims	242	291	-49	-16.9
- of which subject to mandatory conversion and/or debt waiver	7	8	-1	-17.8
Liabilities				
Amounts due to banks	34,164	34,803	-639	-1.8
Liabilities from securities financing transactions	3,191	2,991	200	6.7
Amounts due in respect of customer deposits	77,762	80,820	-3,058	-3.8
Trading portfolio liabilities	2,268	2,110	158	7.5
Negative replacement values of derivative financial instruments	1,305	2,067	-762	-36.8
Liabilities from other financial instruments at fair value	3,251	4,163	-913	-21.9
Cash bonds	273	269	4	1.6
Bond issues	8,537	7,669	868	11.3
Central mortgage institution loans	7,975	7,716	259	3.4
Accrued expenses and deferred income	547	578	-31	-5.4
Other liabilities	1,270	211	1,059	501.2
Provisions	572	584	-12	-2.0
Bank's capital	2,425	2,425		
Profit reserves	7,686	7,290	396	5.4
Foreign currency translation reserves	-8	-8	-0	1.7
Consolidated profit (result of the period)	393	722	-330	-45.6
Equity	10,496	10,429	66	0.6
Total liabilities	151,611	154,410	-2,799	-1.8
Total subordinated liabilities	1,315	1,310	5	0.3
- of which subject to mandatory conversion and/or debt waiver	1,315	1,310	5	0.3
Off-balance-sheet transactions				
Contingent liabilities	4,097	3,851	246	6.4
Irrevocable commitments	7,391	7,478	-87	-1.2
Obligations to pay up shares and make further contributions	233	147	85	58.1
Credit commitments				

Group statement of changes in equity

<i>in CHF million</i>	Bank's capital	Retained earnings reserve	Group net income	Currency translation reserves	Total equity
Total equity as at 1 January 2015					
Opening amount	1,925	7,566		-4	9,487
Impact of restatement					
Capital increase	500				500
Capital decrease					
Increase in scope of capital consolidation		21			21
Decrease in scope of capital consolidation					
Other contributions / other capital paid in					
Acquisition of own shares					
Disposal of own shares					
Reclassifications					
Profit from sale of own capital shares					
Currency translation effect				-3	-3
Distribution of profit		-280			-280
Revaluation adjustments not affecting net income		-18			-18
Other allocations to reserves for general banking risks					
Other allocation to other reserves					
Group net income			722		722
Total equity as at 31 December 2015	2,425	7,290	722	-8	10,429

<i>in CHF million</i>	Bank's capital	Retained earnings reserve	Group net income	Currency translation reserves	Total equity
Total equity as at 1 January 2016					
Opening amount	2,425	8,012		-8	10,429
Impact of restatement					
Capital increase					
Capital decrease					
Increase in scope of capital consolidation					
Decrease in scope of capital consolidation					
Other contributions / other capital paid in					
Acquisition of own shares					
Disposal of own shares					
Reclassifications					
Profit from sale of own capital shares					
Currency translation effect				-0	-0
Distribution of profit		-326			-326
Revaluation adjustments not affecting net income		0			0
Other allocations to reserves for general banking risks					
Other allocation to other reserves					
Consolidated half-year profit			393		393
Total equity as at 30 June 2016	2,425	7,686	393	-8	10,496

New accounting and valuation principles

In November 2015, the transition from the existing accounting regulations (BAG) to the new accounting rules for banks (ARB) was completed.

The new accounting rules had an impact on the statement of the half-yearly report. The previous year's figures have been restated accordingly.

The major changes in this context can be summarised as follows:

Allowances for default risks on loans outstanding are now formed via the item of changes in value adjustments for default risks and losses from interest operations and deducted directly from the corresponding asset. Default risks on off-balance-sheet items (e. g. confirmed but not used credit limits), are covered by provisions. Repo/reverse repo transactions and securities lending and securities borrowing transactions are presented in the newly created position of amounts due or obligations from securities financing transactions.

Positive and negative replacement values of derivative financial instruments as well as financial instruments to which the fair value option is applied are also recognised in separate items.

The netting for OTC transactions must also be mentioned. In these transactions, the positive and negative replacement values of derivative financial instruments as well as the associated cash collateral are offset provided that the requirements of the ARB are met.

Short positions in the trading portfolio are recognised under the item "Trading portfolio liabilities". Physical precious metal portfolios that cover liabilities from customers' precious metal accounts are recognised under financial investments and are measured at fair value.

For more details on the applicable accounting and valuation principles, please refer to the Annual Report 2015.

In addition to the changes in connection with the new accounting rules for banks (ARB) mentioned, the following adjustments to the accounting and valuation principles were made:

For the combinations of money market transactions and the currency swaps carried out in the trading business, according to the principle of substance over form, interest income from the specific money market transactions was recorded under trading income, analogous to the currency swaps. The results from these combined transactions are therefore not disclosed in different income statement items but uniformly under result from trading activities. Artificially inflating the income statement and movements between interest income and trading income, which in substance has neither a sound basis nor is it correct from an economic point of view, could therefore be avoided. This effect amounted to CHF 32.5 million in the first half of 2015; the result from trading activities as well as the gross result from interest operations were therefore adjusted accordingly.

Condensed notes

Factors affecting the half-year result 2016

The first half of 2016 was characterised by political uncertainties having an impact on financial markets. The interest rate environment was largely guided by central banks. At the end of January the Bank of Japan (BoJ) announced the introduction of negative interest rates. In March the European Central Bank commenced further easing of its expansive monetary policy. As expected, the Swiss National Bank (SNB) left the interest rates on CHF sight deposits unchanged for the time being.

The equity markets came under pressure at the start of the year. This was primarily a result of the devaluation of the Chinese currency and the associated fear that the global economy might slip into recession. Following the relaxation in this regard in April, the markets benefited from the Fed's potential base rate increases in May. On 23 June the United Kingdom voted to leave the European Union. As expected, the equity markets reacted negatively and put an end to the recovery that had commenced in the spring.

Extraordinary income and expenses

<i>in CHF million</i>	30.06.2016	30.06.2015
Extraordinary income		
Reversal of impairment on other participations	0	8
Gain from sale of other real estate / bank premises	2	25
Income from sale of participations	0	2
Other	0	0
Total	3	35
Extraordinary expenses		
Losses from sale of other real estate / bank premises	0	
Expenses incurred outside the reporting period	1	
Loss from the sale of participations		0
Other	0	0
Total	1	0

In the financial year, no hidden reserves or reserves for general banking risks were reversed and no significant freed-up allowances and provisions were recorded.

Events occurring after the date of the interim financial statements

No significant events affecting the financial position, results of operations and cash flows of the group

occurred between the date of the interim financial statements and the date on which the report was published.

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Imprint

Published by Zürcher Kantonalbank, Bahnhofstrasse 9, CH-8010 Zurich, +41 (0)44 293 93 93

Concept and layout by Partner & Partner AG, Winterthur