

Spectrum Asset Management

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UBS agrees to purchase Credit Suisse AT1 securities written down to zero

On Sunday March 19, 2023, the Swiss Financial Market Supervisory Authority (FINMA – the Swiss banking regulator) approved the merger of UBS and Credit Suisse, two of the global systemically important financial institutions (G-SIFIs). UBS agreed to purchase Credit Suisse in an all-equity transaction for approximately CHF 3 billion in UBS common shares. FINMA, The Swiss National Bank (SNB) and the Federal Council of the Swiss Confederation all took active part in the discussions and decisions that led to the sale of Credit Suisse. The Swiss Government provided substantial financial support as part of this sale. In its release FINMA stated that this support **“will trigger a complete write-down of the nominal value of all AT1 shares of Credit Suisse in the amount of around CHF 16 billion.”** This is only the second write-down of AT1 securities of a European bank, the first and only other being Banco Popular Espanol SA in 2017.

Without the merger Credit Suisse was a *de facto* failed bank due to a crisis of confidence. Credit Suisse has been weakened from years of challenges, including executive turnover, losses from the Greensill supply chain finance funds and from the investment firm Archegos, as well as profitability struggles with its own investment banking operations. Despite a CHF 4 billion common equity recap in 2022, new management and a fresh strategic plan, the bank’s burdens have become overwhelming.

FINMA said that to facilitate Credit Suisse’s sale to UBS, “further liquidity assistance will be assured” by the SNB and Swiss Federation. The regulator further stated that “the liquidity provided by the SNB will include a loan covered by a federal guarantee. The Swiss Confederation will also provide guarantees for potential losses of certain assets that UBS will acquire as part of the transaction, if these losses exceed a specific threshold.” UBS will receive CHF 9 billion of protection “in case of losses extending beyond the first CHF 5 billion which would be borne by UBS” for non-core assets. In addition, the write-down of Credit Suisse’s CHF 15.8 billion of

AT1 securities by FINMA will strengthen its core capital. Assuming completion of the merger UBS has stated that its CET1 capital will be significantly above its 13% target range.

This transaction more clearly places UBS as a leading global wealth and asset management firm, with approximately US\$ 5 trillion in invested assets. It also strengthens UBS's already solid position in domestic Swiss banking, though it is very possible that this position could be reduced to address market concentration concerns by regulators and the Swiss Government. While the integration of Credit Suisse will be a challenging task for UBS, Spectrum is optimistic that UBS will rise to this challenge. Spectrum continues to view UBS as a sound credit.

Spectrum believes that the liquidity and other support provided to Credit Suisse and UBS will be sufficient to protect the Swiss economy and help ensure the smooth operation of the post-merger bank. Importantly, Spectrum has been selling down positions in Credit Suisse over the past year.

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