

The End of Credit Suisse

What the downfall means

Over the past weekend, Switzerland as a financial center underwent profound change. Orchestrated by the Swiss government and the Swiss National Bank, UBS took over 167-year-old Credit Suisse. Overambitious and misguided managers, toothless risk controls, benign regulators and a generous board of directors all contributed to its demise. Credit Suisse was no longer viable on its own, so the involuntary marriage of the two largest financial institutions in Switzerland, while not a desirable solution, is probably the best of all remaining options. The functioning and immediate stability of the financial system could be ensured, and the crisis of confidence ended for the time being. The consequences are likely to be complex and will materialize over years to come. Below, we outline our thoughts on the significance of this historic takeover for those affected.

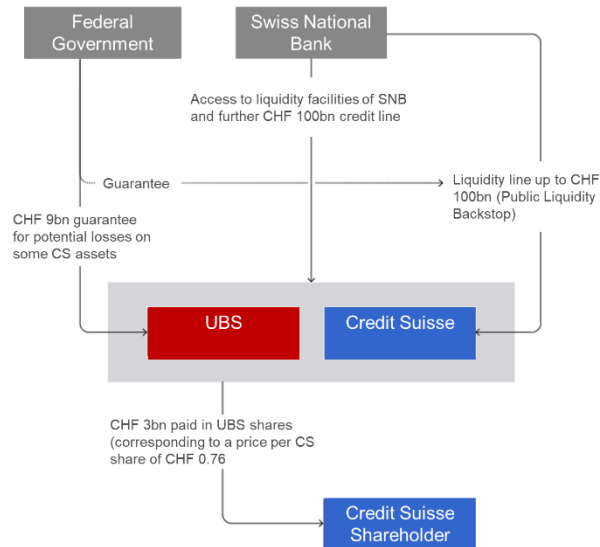


Image: Merger of UBS and Credit Suisse

Source: NZZ, SNB, UBS

Credit Suisse

For clients with business relationships with Credit Suisse, it is important to note that the merger means that all activities can be continued without interruption. Be it salary payments from companies or transfers and cash withdrawals by private clients, accounts and services remain accessible, and deposits and safe-keeping accounts are secure. There is also no danger for investors holding investment funds from Credit Suisse. Securities and investment funds would be separate assets even in the event of bankruptcy and would not fall into the bankruptcy estate. Derivatives and structured products retain counterparty risk, but the combined bank is extremely well capitalized. The main victims of the takeover at Credit Suisse will be the employees. Their prospects have worsened abruptly, and many will (have to) look for new jobs over the next few years. Investors must cope with heavy losses and, in the case of shareholders, reluctantly accept that their rights have been undermined and ignored.



UBS

UBS had the strongest position during these negotiations. And while some aversion to the deal is understandable, chances are good that this acquisition could be paying off in the long run. The takeover of such a large and complex institution is challenging and creates countless redundancies. The integration takes an enormous amount of time, causes high costs, ties up capacities and entails significant execution risks. On the other hand, UBS acquires a direct competitor at a price that corresponds to a fraction of its underlying value. The national and international market position is substantially strengthened, and concessions and guarantees have been obtained from the federal government and the Swiss National Bank.

Switzerland

The image of Switzerland as a financial hub has changed radically, and its long-term perception is likely to suffer. The reputation of Swiss banking has been damaged, and in our opinion several new problems and challenges are emerging:

- In terms of market and competition landscape, the merger of the two largest banks is highly problematic. The "new" UBS holds an extremely dominant position in certain business areas, which is likely to be detrimental to all bank clients in the long term.
- By invoking emergency law, the rights of both the owners of Credit Suisse and UBS were ignored. The protection of minority shareholders was also suspended. In addition, the decision to completely write off certain parts of subordinated debt, which ranks higher in the capital structure than the shareholders, is extremely questionable.
- The "too big to fail" legislation, drafted in the aftermath of the 2008 financial crisis, was written and refined over years to prevent taxpayers from having to shoulder the risks of a bank bailout. Now, these regulations were apparently not applicable to the case at hand. One may therefore ask whether regulators were misguided, or whether Switzerland simply gave in to mounting international pressure. And if the regulations have already failed to take effect here, what will happen if UBS ever finds itself in a similar situation?

The demise of Credit Suisse is a historic debacle. In view of the trust of depositors and investors that had been gambled away and eroded over the years, the bank's end became inevitable. The decision to integrate CS into UBS comes with many question marks, brings great uncertainty, and creates new problems. For the moment, unfortunately, it seems to be the best of the remaining alternatives to ensure the function and stability of the banking system, and to be able to create a minimum of trust. In the long term, however, this may well result in a loss of confidence in Switzerland itself and its stability and rule of law that should not be underestimated.

