LA FRANÇAISE
INVESTING TOGETHER

FLASH NEWS

CREDIT SUISSE AND EUROPEAN BANKS

The collapse of three US banks last week has accelerated Credit Suisse liquidity crisis. But what about contagion to other European banks and the European and global banking system as a whole? This note is a summary of the analysis by Jérémie Boudinet, Head of Investment Grade Credit.

IMPORTANT INFORMATION

- **We do not hold any exposure to Credit Suisse** in LFAM open-end or dedicated funds.
- **We have no exposure to** SVB, Silvergate Bank and Signature Ban**k, and have never had any exposure to these banks.**

BACKGROUND

Over the past several years, **Credit Suisse has been involved in several high-profile scandals** raising questions about **its corporate governance practices** and overall corporate culture. Considering this situation, we excluded Credit Suisse from our open-end or dedicated funds due to its history of major operational incidents and business controversies, which revealed weaknesses in its risk management. While these incidents differ in nature and impact, their accumulation suggests that **structural problems persist within the company**.

CREDIT SUISSE: SHAKEN CONFIDENCE SINCE OCTOBER 2022

OCTOBER 2022: The bank announced a net loss of CHF 4 billion for the third quarter and a capital increase plan.

NOVEMBER 2022: Senior HoldCo and Opco bonds have been downgraded.

FEBRUARY 2023: The bank announced a net loss of CHF 7,3 billion for the year 2022, with significant outflows. FINMA launches an investigation into the Chairman's comments on outflows.

MARCH 2023: On 15 March, the main shareholder, a Saudi bank, refused to invest any more in the bank.

WHAT HAS HAPPENED SINCE 19 MARCH 2023?

On 19 March, all of the above, as well as **the stress experienced by the bank in recent days, particularly following the failure of the US regional banks, led FINMA to approve the acquisition of Credit Suisse by UBS**. The deal resulted in the purchase of the bank for CHF 0.76 per share, or a total of CHF 3 billion. Unfortunately, AT1 holders were hit hard by this decision, as the value of their securities fell to zero.

What is **surprising** and precedent-setting here is **the failure of creditor hierarchy against shareholder**. In contrast to the shareholders, the holders of Credit Suisse's AT1 CoCos (CHF 15.8 bn) will see their securities fully written-off. The T2 CoCos (CHF 1.5 bn) will be spared, as will the senior bonds of HoldCo and OpCo.

It should be noted that AT1 instruments with "permanent write-down" now offer less protection than "temporary write-down" or “equity conversion" notes.

Source: La Française AM, as of 19/03/2023.

ARE ANY OTHER BANKS AT RISK?

The recent collapse of Credit Suisse does not mean that other credit institutions are at risk. Credit Suisse's difficulties were specific and self-inflicted, and the collapse of the US regional banks only precipitated the outcome. **European banks**, while they may suffer reputational damage from this case**, have nothing fundamentally in common with Credit Suisse**. It is important to note that **European banks are more solid** thanks to:

- **Stricter and ever-harsher regulation,**
- **Robust capital buffers,**
- **Elevated liquidity ratios,**
- **Stable business models.**

Nevertheless, we should remain vigilant about the potential impact of the current situation on the AT1 market, which could be hit by forced sellers due to outflows in this asset class and the disaffection of occasional buyers for the segment. It should also be noted that **the global financial sector is going through a period of turbulence**, with the disappearance of four banks in less than two weeks, which **requires a careful assessment of the financial health of the entire sector**. In this context, **strong support from central banks and regulators in the event of a liquidity crisis is crucial.**

CONCLUSION

Credit Suisse has faced **difficulties that started several years ago and have worsened in recent months, particularly following the collapse of the SVB, which accelerated its liquidity crisis. In order to avoid a counterparty risk failure, the takeover of Credit Suisse by UBS is seen as the best solution for the European banking system, as it removes its weakest systemic link.**

However, this crisis reminds us that **there are still lessons to be learned**. The banking sector has changed significantly since the 2008 financial crisis, with **banks now much more liquid and capitalized** than before and **regulators more responsive in times of crisis.** The Covid-19 pandemic was a proof of that, as governments, central banks and regulators have responded appropriately to **support the banking system and avoid a major economic crisis. Banks are now being considered as a response to a crisis rather than the cause of it.**

Each bank resolution is different and is ultimately a political rather than a financial decision. Regulators have the ability to bypass resolution texts if necessary (German banks have avoided bail-in in recent years for HSH and NordLB, while Monte dei Paschi was nationalized and recapitalized once more). In the case of Credit Suisse, it was sold with a small recovery for shareholders, but none for AT1 holders.

Finally, as we highlighted in our previous note published last week, it is important **to keep a close eye on the shadow banking sector. In the event of a crisis, illiquid and unlisted assets, such as private equity and private debt, can also have negative impacts on the market. It is therefore crucial to take these assets into account in risk assessments and regulatory measures in order to maintain the stability of the sector.**