Banks in turmoil

The Big Read **Credit Suisse Group AG**

How the Swiss ‘trinity’ forced UBS to save Credit Suisse

The takeover of its local rival could end up being a generational boon for UBS. But the government-orchestrated deal has angered many investors

Stephen Morris, **James Fontanella-Khan** and **Arash Massoudi** in London YESTERDAY

The emergency call from the Swiss establishment came at 4pm on Thursday.

Colm Kelleher, a rambunctious Irish banking executive who has been chair of UBS since last April, had been planning to celebrate St Patrick's Day on Friday before watching Ireland play England at rugby on Saturday at a pub in Zurich. He was hoping to see his country win a clean sweep, or "Grand Slam", in the Six Nations Championship.

But even before he took the call, he knew his chances of enjoying an entertaining weekend were slim. The chaos engulfing crosstown rival Credit Suisse, which had become the basket case of European banking after three scandal-ridden years, was now in overdrive.

A day earlier, a SFr50bn ($54bn) liquidity backstop from the Swiss central bank had failed to arrest a crisis of confidence in the lender, whose shares had plunged after Ammar Al Khudairy, the chair of its largest investor Saudi National Bank, bluntly replied "absolutely not" when asked if it would put in any more money.

Global markets were already anxious after US regulators had seized control of Silicon Valley Bank following the withdrawal of $42bn of deposits in a single day. The same was happening at Credit Suisse. It was losing more than SFr10bn of wealthy clients' money daily, adding to SFr111bn that had disappeared after a social-media rumour in October that it was on the verge of bankruptcy.

"For the biggest investor to say I'm not putting another dime in was a huge vote of non-confidence. I could argue that had he not said anything we might have been in a very different situation," says a person close to Credit Suisse's top management.

Credit Suisse chair Axel Lehmann, left, and UBS chair Colm Kelleher gather with Swiss finance minister Karin Keller-Sutter and Swiss president Alain Berset after talks on UBS taking over Credit Suisse © Fabrice Coffrini/AFP/Getty Images

On Wednesday, the so-called "trinity" of the Swiss National Bank, regulator Finma and the minister of finance summoned Credit Suisse chair Axel Lehmann, who was in Saudi Arabia for a conference, and chief executive Ulrich Körner for a call.

In the same meeting where they authorised the SFr50bn backstop, they also delivered another message: "You will merge with UBS and announce Sunday evening before Asia opens. This is not optional," a person briefed on the conversation recalls.

Kelleher found out his weekend plans were ruined on Thursday afternoon. The trinity called UBS and ordered the group to find a solution to save its ailing peer from bankruptcy.

"Resolution [a government-controlled wind-down] would have been a disaster for the financial system and introduced the threat of contagion around the world," says another person involved on the UBS side. "Our interests were also aligned because a failure is not good for the Swiss wealth-management brand. So we said, on the right terms, we would help."

The takeover of its local rival could end up being a once-in-a-generation boon for UBS. But in exchange for taking on a bank wracked with litigation issues and billions of toxic assets, UBS was determined to extract the best deal that it could.

Ireland did win the Grand Slam on Saturday but Kelleher was limited to enjoying a single pint of Guinness at the James Joyce pub in Zurich.

The following account is based on interviews with more than a dozen people involved in a frantic weekend of dealmaking that ended in a storied 167-year-old bank being subsumed into its fierce rival, wiping out certain junior bondholders and putting tens of thousands of jobs around the world in peril.

Last days for an independent Credit Suisse

Intraday share price, from close on Mar 9 2023 (SFr)

FINANCIAL TIMES

Source: Refinitiv

A merger between Zurich’s two largest banks has long been debated and rumoured. Tidjane Thiam, the former Credit Suisse chief executive, repeatedly told colleagues when he was in charge between 2015 to 2020 that it was “the only merger in European banking that makes sense”.

Until last week, the Swiss establishment had always been committed to a two-bank model. In 2008, it opted to rescue UBS with taxpayer money after it suffered dramatic losses in the financial crisis, rather than allow it to be acquired. However, public anger at that arrangement still endures today and a repeat was politically unthinkable.

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"This is no bailout," Swiss finance minister Karin Keller-Sutter stressed when the deal was announced on Sunday night. "This is a commercial solution."

Advisers and code names

When both sides realised a deal was inevitable, they hired advisers. Credit Suisse has long retained Centerview, the investment bank led by Blair Effron who was assisted by Tadhg Flood, but Lehmann and Körner also recruited ex-UBS investment banker Piero Novelli to separately advise the board. Rothschild provided a further fairness opinion to directors.

JPMorgan advised the UBS management team, while Morgan Stanley advised the UBS board. The acquirer gave each bank a tree-based code name: Credit Suisse was Cedar and UBS Ulmus, the Latin word for elm.

Credit Suisse used different monikers: it referred to itself as Como while UBS was Geneva, after the lakes.

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Through the process there was almost no direct contact between the two sides, an arrangement that increasingly infuriated those at Credit Suisse, who were intentionally kept in the dark about the price and terms of the takeover.

Most interaction took place via intermediaries in the Swiss government or regulators over Zoom.

"By Thursday, we were all together in Zurich, and it was clear that the government was going to push one way or the other for a solution by Monday morning, at all costs, to protect Swiss national interest, and banking interest more generally, on a global basis," says the person close to Credit Suisse.

Keller-Sutter, the finance minister, was a key figure throughout the negotiations, including co-ordinating with foreign officials and regulators in the US and Europe.

She was under extreme pressure from global regulators, who had been demanding faster and more decisive action to stop panic spreading in markets. In particular, the US and the French were "kicking the shit out of the Swiss", says one of the people advising UBS. Janet Yellen, the US Treasury secretary, had several conversations with Keller-Sutter over the weekend.

Keller-Sutter over the weekend.

Negotiations over the deal were initially "fairly friendly" but as time progressed the trinity started becoming more aggressive, pushing a transaction that Credit Suisse was vehemently opposed to.

UBS was also reticent. Executives made it clear that it would only participate in the rescue of its rival if the price was cheap and it indemnified them from a raft of regulatory probes into Credit Suisse's culture and controls.

"They [UBS] were always going to try to kill us on price. And we were always going to try to get a premium," says a person close to Credit Suisse.

By Friday evening, when it was revealed that UBS was exploring a state-mandated takeover, Credit Suisse had lost another SFr35bn in client deposits over the preceding three days, according to a banker involved in the deal, and international banks from BNP Paribas to HSBC were cutting ties. Regulators concluded that it would probably not be able to open on Monday.

Another potential bidder, however, was waiting in the wings: Larry Fink's BlackRock.

The US firm's chief executive had convened his inner circle on Thursday and told them a line he has used repeatedly: "To be in the game you've got to play it," one person involved remembers.

Swiss National Bank chair Thomas Jordan, left, and his team leave the Swiss Federal Department of Finance after weekend talks on the Credit Suisse crisis © Fabrice Coffrini/AFP/Getty Images

During the financial crisis, BlackRock bought Barclays's investment arm BGI in 2009 for $15.2bn, a transformational deal that made it the world's biggest asset manager with $2.7tn of assets. Since then, it has grown to dominate the global investment industry and manage $8.6tn.

It spied a similar opportunity in Credit Suisse's troubles.

A BlackRock team led by Rob Kapito, Fink's second-in-command, flew immediately to Zurich and spent hours in a conference room studying various options. On Friday, Fink also turned to Bob Steel, vice-chair of Perella Weinberg Partners, who headed to Zurich.

BlackRock was open to a variety of options, including a partial acquisition or working with others. Such a scenario would potentially have made it easier for Michael Klein, the former Citigroup executive and Credit Suisse board member, to preserve an already arranged deal to merge his advisory boutique with and take control of the Swiss lender's investment bank.

"The most credible alternative was BlackRock . . . But it wasn't what the Swiss government wanted," says a person with direct knowledge of the matter.

By late Friday, BlackRock had indicated it did not want to buy the entire bank. Credit Suisse responded by proposing a minority investment, including some kind of wealth management partnership. BlackRock ultimately decided to halt its work on a bid.

"Fink wasn't really in the mood to piss off UBS as it's one of his biggest customers. So I always thought that at some point, he was going to not be there. He would have to deal with US regulators, which was a tough thing," says a person close to Credit Suisse.

You make fun of dictatorships and then you can change the law over the weekend. What's the difference between Saudi Arabia

Negotiations continued throughout Saturday, with global regulators keen to sign off on the structure of a deal in principle by that evening. Deadlines kept being pushed back as officials scrambled to find the right change of control documentation.

Also slowing down progress was a problem with UBS's email system, which meant

and Switzerland now?

messages were taking a long time to go through. Frazzled supervisors told them instead to pick up the phone.

Growing frustrated with the lack of communication from UBS, Lehmann decided he would write a letter instead to Kelleher and the Swiss authorities. Drafted by general counsel Markus Diethelm — who had joined from UBS in June — it was delivered on Saturday evening and contained a number of reasons for why the planned transaction was unacceptable.

These included the insistence by UBS for walkaway provisions, including a material adverse change clause linked to a spike in its credit default swap spreads.

Lehmann’s communique also carried a threat. He wrote that Credit Suisse’s three biggest shareholders — including two from Saudi Arabia and one from Qatar — had expressed their “extreme discomfort” with the opacity of the deal. They demanded to see a fair price, a vote on the deal and that any get-out clauses be removed. The letter also noted that the Saudis and Qataris were large clients of both banks.

In response, on Saturday evening Kelleher called his counterpart at Credit Suisse from outside a restaurant to tell him UBS was prepared to offer $1bn in stock for the whole group, about SFr0.25 a share, far below the SFr1.86 closing price on Friday.

The government then informed Credit Suisse it would introduce emergency legislation to strip both sets of shareholders of the right to vote on the deal.

Credit Suisse was outraged and refused to sign. It was opposed to the CDS clause because the optionality of walking away from the deal would have killed it once it was made public. Such a condition would have led to chaos, say people with direct knowledge of the negotiations.

Its Middle Eastern shareholders were also incensed.

“You make fun of dictatorships and then you can change the law over the weekend. What’s the difference between Saudi Arabia and Switzerland now? It’s really bad,” says one person close to one of the three major shareholders.

On Sunday morning, when the terms of the $1bn offer were revealed in the FT, the person said it was greeted in the region with “disbelief”.

Ramping up the pressure

Under pressure to get a deal done before the end of the day, the trinity started to ramp up pressure on both sides, threatening to remove the Credit Suisse board if they did not sign off.

On the other side, UBS was lent on to increase its price and reluctantly agreed, ultimately boosting the offer to $3.25bn in stock. But in return it negotiated more support from the state, including a SFr100bn liquidity line from the SNB and a government loss guarantee of up to SFr9bn, after it had borne the first SFr5bn itself.

At one point, both sides had hardly met face to face, despite their offices essentially facing each other across Zurich's Paradeplatz square © Michael Bulhozer/EPA-EFE/Shutterstock

The final terms were still so favourable to UBS they were "an offer we couldn't refuse", a person on the negotiating team told the FT. An adviser to Credit Suisse described them as "unacceptable and outrageous" and a "total disregard of corporate governance and shareholder rights".

At this point, both sides had hardly met face to face, despite their offices essentially facing each other across Zurich's Paradeplatz square.

In order to make the deal more palatable for Swiss citizens and the bank's equity investors, the government also decided to impose losses on SFr16bn of Credit Suisse's additional tier 1 (AT1) capital bonds. While these are designed to take losses when institutions run into trouble, normally they are not triggered if shareholders receive money as part of a takeover.

However, the small print of the bond documentation allowed Swiss authorities to disregard the normal order of priority and wipe out bondholders.

How Credit Suisse's riskiest class of bonds sunk to zero after UBS takeover

$1.5bn additional tier 1 bond redeeming in 2027, 5.25% coupon (cents per $)

"AT1 holders were sacrificed so the finance ministry could try to save some face with international equity holders after denying them a vote on either side of the transaction," says one of the bankers advising on the takeover.

The details were hammered out so fast, UBS chief executive Ralph Hamers was unable to answer analysts' questions about the treatment of Credit Suisse's debt at a presentation later on Sunday night after the announcement.

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Credit Suisse's board pored over the details of the final proposal and, after a quick consultation with its advisers, informed the trinity that it would accept UBS's $3.25bn offer.

When Keller-Sutter was informed that the deal would indeed go through before the Asian markets opened, the finance minister breathed a sigh of relief, say people briefed about the matter, releasing days of tension over the future of the Swiss and global financial system.

Kelleher, clockwise from centre left, talks with Finma chair Marlene Amstad, Berset, Keller-Sutter, Jordan and Lehmann in front of the press in Bern on Sunday © Peter Klaunzer/EPA-EFE/Shutterstock

A press conference was hastily convened in Bern, where the trinity was joined by the chairs of UBS and Credit Suisse on stage to present a historic deal.

"The failure of a systemically relevant bank would have had severe repercussions," said Keller-Sutter. "Switzerland needs to be aware of its own responsibility beyond its own borders."

Next to her on stage, Credit Suisse's Lehmann was asked, "Who is responsible for this disaster?" He chose to blame Twitter.

"Hindsight is wonderful, and to point a finger — it's a fact that since 2021 . . . we never left the headlines," he responded. "Last autumn we had a social media storm and this had huge repercussions — more in the retail sector than in the wholesale sector. And too much becomes too much."

Kelleher was more blunt.

"It's a historic day, and a day we hoped would not come," he said. "This acquisition is attractive for UBS shareholders but, let us be clear, as far as Credit Suisse is concerned, this is an emergency rescue."

Additional reporting by Owen Walker, Brooke Masters, Laura Noonan and Robert Smith

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The global banking system has been rocked by the collapse of Silicon Valley Bank and Signature Bank and the last minute rescue of Credit Suisse by UBS. Check out the latest analysis and comment here