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Credit Suisse and AT1 Bonds: A Brief Overview

March 2023

On March 19, UBS, Switzerland's largest bank, agreed to purchase its long-time rival Credit Suisse for around USD 3.25 billion. The deal was brokered by the Swiss government and marks the end of the 166-year-old Credit Suisse's run as one of the world's leading financial institutions.

The bank became a focal point of concern following the collapse of Silicon Valley Bank, in California, and Signature Bank, NY. Credit Suisse's annual report, published just days after regulators announced the closure of Silicon Valley Bank, announced it had found "material weakness" in its financial reporting processes. The report was due to be published a few days earlier but had been delayed following a call with the US Securities and Exchange Commission. The day after the report was published, Saudi National Bank (SNB), Credit Suisse's top shareholder, said it would not invest more in the lender.

The combination of Credit Suisse's annual report and SNB's statement led to a spike in Credit Suisse's credit default swaps, which in turn prompted further panic and accelerated deposit outflows, ultimately resulting in a liquidity crisis. A USD 54 billion loan from the Swiss central bank failed to provide an adequate lifeline, prompting the Swiss authorities to push UBS to agree to the takeover.

What are the details of UBS's acquisition of Credit Suisse?

At 3 billion Swiss francs, UBS is paying around 60% less than Credit Suisse was worth when the markets closed on Friday, March 17. This means that UBS will pay USD 0.82 of one of its shares for each share of Credit Suisse, which were trading at USD 2.01 at closing time on Friday.

The Swiss National Bank pledged a loan of up to 100 billion Swiss francs (USD 108 billion) to support the takeover. Swiss regulator Finma provided further support to UBS by ordering that Credit Suisse's additional tier one (AT1) bonds be written down to zero. This decision was greeted with surprise among Credit Suisse bondholders and led to sharp drops in AT1 bonds in other banks.

What are AT1 bonds, and why are they important?

AT1s are a form of contingent convertible security, or CoCo, which can be converted into equity if a bank falls below a certain capital limit. They were created in the wake of the 2008 global financial crisis as a way to transfer banking risk away from taxpayers and onto bondholders, making it less likely that a stricken bank will need to be bailed out with taxpayer money. AT1s are higher risk than other bonds because if a lender gets in trouble, the bonds can be converted into equity or written down to zero.

Finma's write down of Credit Suisse's AT1 debt to zero is the largest ever loss inflicted on AT1 investors. The move was considered controversial because it ensured that Credit Suisse's shareholders will receive some compensation while its AT1 bondholders will receive nothing. Ordinarily, bondholders rank above shareholders in the capital structure. However, the Credit Suisse AT1 bonds were something of an outlier in this respect because the provision was given for a scenario where regulators could write them down without wiping out shareholders.

There are very few precedents for AT1 bonds to be written down in this way. The most significant was in 2017 when the AT1 debt of Spain's Banco Popular was written down to zero, but in that case the equity was wiped out at the same time.

What does the write down of Credit Suisse's AT1 debt mean for AT1 bonds more broadly?

Following the news of the AT1 write down, CoCo ETFs in other banks were hit by sharp declines as anxiety rippled across markets. However, it seems highly unlikely that other European regulators will write down the AT1 debt of other banks while compensating shareholders. In a statement on Monday, the European Central Bank (ECB) clarified that "common equity instruments are the first ones to absorb losses", and only after that would AT1s be required to be written down. "Additional Tier 1 [AT1] is and will remain an important component of the capital structure of European banks," the statement added.

However, it is likely that because of Finma's action, AT1 bonds—already regarded as higher risk than other debt—will be considered even riskier in the future, at least in the near term. Because AT1 bonds have no natural buyer base (they do not sit in the investment grade index or high yield index), it is possible that previous purchasers of the instruments may in the future prefer to buy shares instead. However, the full impact of Finma's decision on the AT1 bond market more broadly will only become clear over time.

Did T. Rowe Price have any exposure to Credit Suisse AT1 bonds?

As of February 28, 2023, T. Rowe Price had zero exposure to Credit Suisse AT1 bonds in our commingled products.

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T. Rowe Price Holdings Brief: Credit Suisse

As of February 28, 2023

T. Rowe Price Holdings of Credit Suisse

As of February 28, 2023

	Fixed Income	Equity
Portfolio Name	**Bonds % of Net Assets**	**Stocks % of Net Assets**
Ultra Short-Term Bond ETF	0.47%	0.00%
Balanced Fund	0.05	0.00
Global Allocation Fund	0.00	0.00
International Bond Fund	0.10	0.00
International Bond Fund (USD Hedged)	0.10	0.00
International Equity Index Fund	0.00	0.07
Limited-Term Bond Portfolio	0.51	0.00
Moderate Allocation Portfolio	0.00	0.00
QM U.S. Bond Index Fund	0.32	0.00
Retirement 2005 Fund	0.01	0.00
Retirement 2010 Fund	0.01	0.00
Retirement 2015 Fund	0.01	0.00
Retirement 2020 Fund	0.00	0.00
Retirement 2025 Fund	0.00	0.00
Retirement 2030 Fund	0.00	0.00
Retirement 2035 Fund	0.00	0.00
Retirement 2040 Fund	0.00	0.00
Retirement 2045 Fund	0.00	0.00
Retirement 2050 Fund	0.00	0.00
Retirement 2055 Fund	0.00	0.00
Retirement 2060 Fund	0.00	0.00
Retirement 2065 Fund	0.00	0.00
Retirement Balanced Fund	0.01	0.00
Retirement Balanced I Fund—I Class	0.01	0.00

Some funds may have exposure that rounds down to 0.00%.
Portfolio weights in Credit Suisse reflect all direct investment types.
The multi-asset and retirement funds shown include weights that are based on the value of positions directly held and indirectly held through the underlying funds.

Portfolio Name	Fixed Income Bonds % of Net Assets	Equity Stocks % of Net Assets
Retirement Blend 2005 Fund	0.05	0.00
Retirement Blend 2010 Fund	0.05	0.00
Retirement Blend 2015 Fund	0.05	0.01
Retirement Blend 2020 Fund	0.05	0.01
Retirement Blend 2025 Fund	0.04	0.01
Retirement Blend 2030 Fund	0.03	0.01
Retirement Blend 2035 Fund	0.02	0.01
Retirement Blend 2040 Fund	0.01	0.01
Retirement Blend 2045 Fund	0.00	0.01
Retirement Blend 2050 Fund	0.00	0.01
Retirement Blend 2055 Fund	0.00	0.01
Retirement Blend 2060 Fund	0.00	0.01
Retirement Blend 2065 Fund	0.00	0.01
Retirement I 2005 Fund—I Class	0.01	0.00
Retirement I 2010 Fund—I Class	0.01	0.00
Retirement I 2015 Fund—I Class	0.01	0.00
Retirement I 2020 Fund—I Class	0.00	0.00
Retirement I 2025 Fund—I Class	0.00	0.00
Retirement I 2030 Fund—I Class	0.00	0.00
Retirement I 2035 Fund—I Class	0.00	0.00
Retirement I 2040 Fund—I Class	0.00	0.00
Retirement I 2045 Fund—I Class	0.00	0.00
Retirement I 2050 Fund—I Class	0.00	0.00
Retirement I 2055 Fund—I Class	0.00	0.00
Retirement I 2060 Fund—I Class	0.00	0.00
Retirement I 2065 Fund—I Class	0.00	0.00
Retirement Income 2020 Fund	0.00	0.00
Spectrum Moderate Allocation Fund	0.00	0.00
Spectrum Moderate Growth Allocation Fund	0.00	0.00
Spectrum Conservative Allocation Fund	0.01	0.00
Spectrum Income Fund	0.02	0.00
Target 2005 Fund	0.01	0.00
Target 2010 Fund	0.01	0.00
Target 2015 Fund	0.01	0.00
Target 2020 Fund	0.01	0.00
Target 2025 Fund	0.00	0.00
Target 2030 Fund	0.00	0.00
Target 2035 Fund	0.00	0.00

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Portfolio Name	Fixed Income Bonds % of Net Assets	Equity Stocks % of Net Assets
Target 2040 Fund	0.00	0.00
Target 2045 Fund	0.00	0.00
Target 2050 Fund	0.00	0.00
Target 2055 Fund	0.00	0.00
Target 2060 Fund	0.00	0.00
Target 2065 Fund	0.00	0.00
Short-Term Bond Fund	0.52	0.00
U.S. Bond Index Portfolio	0.32	0.00
Ultra Short-Term Bond Fund	0.54	0.00

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