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UBS vs Credit Suisse

Strategic Evaluation

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Executive Summary

- Market wide banks are facing structural and cyclical factors depressing returns both in the medium and long term
- As a consequence all have engaged in similar tactical actions – cost cutting, de-risking and re-focusing on areas of core competency
- With a recognition of sub-scale presence in FICC, UBS is retrenching and re-defining its investment banking activity to focus on
  - Corporate Clients through advisory and origination
  - Investor Clients through execution, distribution and trading for institutional investors i.e. activities to compliment core wealth management business
- Credit Suisse, on the other hand, remains dedicated to FICC, focusing on those areas with high returns potential and a leading market position; with ~20% revenue contribution from this business, retrenchment appears less palatable to management
- Investor sentiment, however, favours UBS; questions remain over Credit Suisse’s ability to build sufficient scale whilst limiting volatility of returns

Market Context

Bank profitability has and will continue to face significant macroeconomic and regulatory headwinds

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		Description	Primary channels of impact (↓)	Primary channels of impact (↑)
Regulation	Basel III	▪ More stringent capital ratios ▪ Greater RWAs (e.g. CVA, IRC charges) ▪ Liquidity standards (LCR & NSFR)	5	4 7
Regulation	National Regulatory Top-ups	▪ FINMA requirement of – 10% CT1 equity – 3% high-trigger loss absorbing capital – 6% low-trigger loss absorbing capital		7
Regulation	MiFid	▪ Standardisation and central clearing of OTC derivatives ▪ Regulation of internal crossing systems	2	3
Macroeconomic	Eurozone Crisis	▪ Suppressed market (institutional investors) & business (corporates) activity ▪ Increased CoF	1 2	4 5 7
Macroeconomic	Monetary environment	▪ Flattening of yield curve driving down NIM ▪ Low IR environment – subdued equity issuance	1 2 5	4 7
Macroeconomic	Fiscal policies	▪ Long-term reduced government borrowing & expenditure ▪ Household de-leveraging	1 2	

Key:

1 Interest Income
2 Fee Income

less

3 Op Costs
4 Funding Costs
5 Risk Costs

Return

less

7 Opportunity Cost of Capital

Economic Profit

Banks are facing cyclical and structural RoE compression

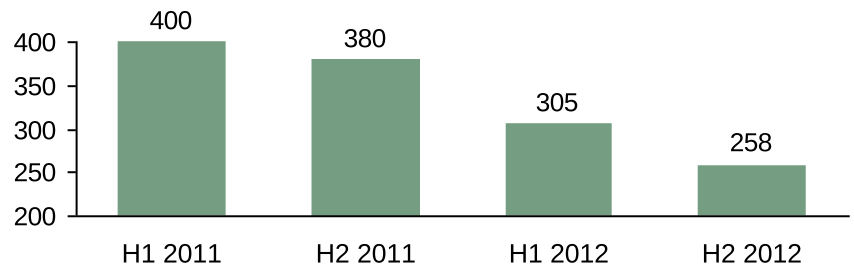
Tactical Actions

In line with the rest of the market, UBS and Credit Suisse have both engaged in tactical cost cutting and de-risking programmes

All units in CHF bn

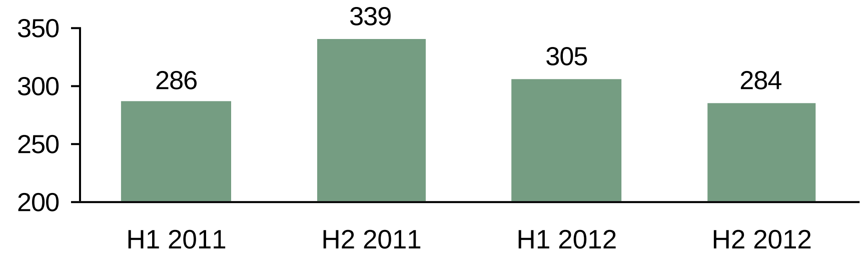
UBS | **CREDIT SUISSE**

De-risking



	H1 2011	H2 2011	H1 2012	H2 2012
RWA / Total Assets	*22.9%*	*18.3%*	*15.4%*	*15.3%*

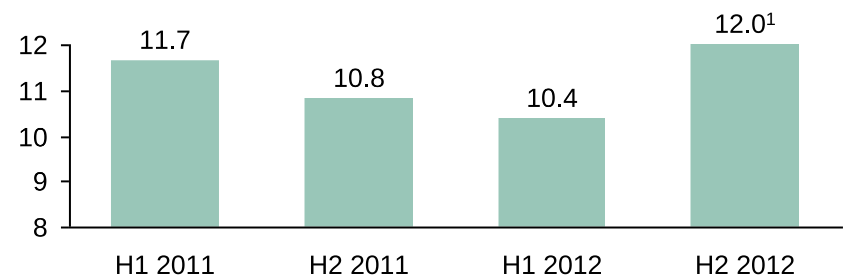
- Successfully de-risking - reduction in RWA/Total Assets



	H1 2011	H2 2011	H1 2012	H2 2012
RWA / Total Assets	*20.9%*	*21.4%*	*23.3%*	*24.0%*

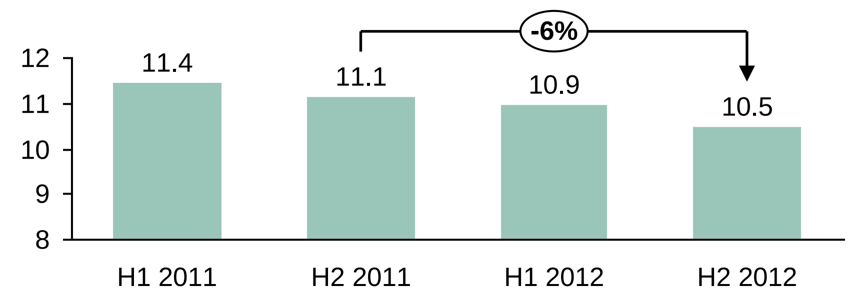
- Absolute reduction in RWAs not matched by its reduction as a proportion of total assets

Cost Cutting



	H1 2011	H2 2011	H1 2012	H2 2012
C:I	*75%*	*88%*	*80%*	*96%[1]*

- Struggling with cost control - C:I and absolute costs higher in 2012 vs. 2011



	H1 2011	H2 2011	H1 2012	H2 2012
C:I	*76%*	*100%*	*89%*	*90%*

- Successfully cost cutting – reduction of 6% in costs
- However, C:I still relatively high at ~90% for 2012

Experiencing mixed results – UBS struggling to control costs and Credit Suisse it's risk profile – both have recognised that a more fundamental business model repositioning is required

1. Adjusted to exclude goodwill impairment of CHF3.0bn and increased litigation cost CHF2.0bn

Long Term Strategy

UBS largely repositioning away from investment banking, redeploying capital in areas of core competency such wealth management

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UBS

	Rev. Contribution *(2012)*	Strategic Actions	Rationale
Investment Bank	Equities 10.2% ECM & DCM 6.8% FICC 5.6% M&A 2.5% **Total 25.1%**	▪ Refocusing on capital-light advisory ▪ Maintaining strong (top 3) equities franchise ▪ Winding down FICC	▪ FICC unattractive – Capital intense – Low mkt. Share – Prior losses ▪ FICC only small part of Group
Wealth M'nt	International 22.2% Swiss 5.5% Americas 24.0& **Total 51.7%**	▪ Focusing on asset gathering to compensate for Swiss outflows ▪ Segments include APAC, emerging markets, UHNW	▪ Growth area, particularly in emerging markets ▪ Relatively capital light ▪ Strong franchise
Retail & Corporate	**Total 14.7%**	▪ Continuing to invest in private client franchise and in transaction banking ▪ Operations consolidated to corporate centre	▪ Stable business with attractive margins e.g. cash management, transaction banking ▪ Deposit funding source
Global Asset M'nt	**Total 7.4%**	▪ Continuing investment, for example in – Alternatives platform – Passive capabilities	▪ Overall market growth (pensions) ▪ Diversified capabilities & distribution channels ▪ Ranked #2 in alternatives globally

Comments

Main differentiation of UBS' strategy is a retrenchment from investment banking activities, particularly from FICC

Key Drivers:

Order of increasing importance

1. **Reputational:** protect Wealth franchise from further reputational damage e.g. LIBOR rigging, rogue trading
2. **Structural:** regulation increasing CoE thus depressing margins
3. **Competitive Position:** lack of scale and significant past losses
4. **Capital Rebate:** RoE boost from rebate if UBS demonstrates a simplified and lower risk business model to FINMA

Long Term Strategy

In comparison, CS has renewed its commitment to investment banking, albeit in areas with strong franchise and potential for scale

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Comments

A Large revenue contribution from investment banking activities, from FICC in particular (48% and 20% respectively); retrenchment a la UBS not viable

B Instead, CS optimising capital usage within IB; focus to be on activities with strong market position and relatively strong return potential e.g.

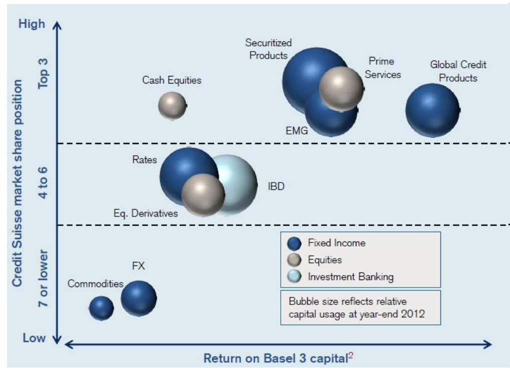
- Building scale in fixed income
- Focusing on prime brokerage

C In addition, private banking and asset management combined to

- Realise revenue & cost synergies
- Ring-fence off from riskier, more volatile IB activities

B

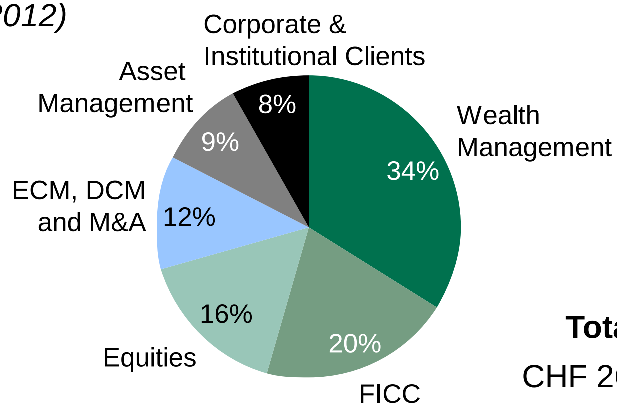
Market share position vs. return on Basel 3 capital by investment bank activity *(2012)*



% of Investment Banking capital base[1]	Optimize risk and capital utilization across the franchise
55%	▪ Majority of capital allocated to market leading businesses ▪ Returns expected to improve driven by planned cost savings and improving market conditions
37%	▪ Optimize capital allocation by product and region as well as cost reductions to improve returns
8%	▪ Further reduction in costs and allocated capital to improve returns ▪ Continue to ensure full suite of products offerings for IB and PB&WM clients

A

Business mix: Revenue contribution by activity *(2012)*



Total[1]
CHF 26.4bn

C

Asset management division into operating model of private bank

Value chain (value capture)

Distribution / Customer Servicing	Asset Allocation / Research	Asset Management	Operations / Platforms
(100bps)	(30bps)	(25bps)	(30bps)

Revenue Synergies

- Additional value capture for Group through leveraging captive asset management manufacturing capabilities

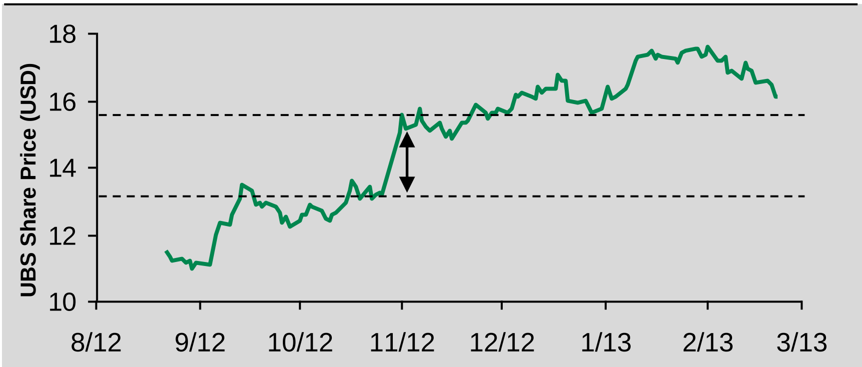
Cost Synergies

- Consolidation of execution, settlement and risk platforms
- Elimination of product overlap

1. Excludes Corporate Center

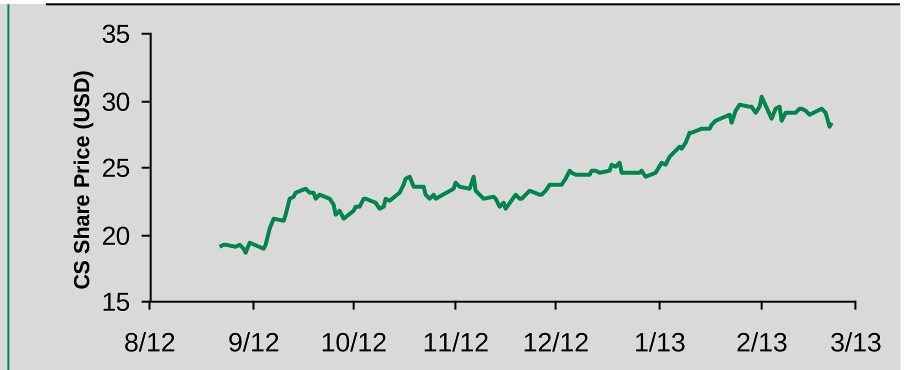
Assessment

Market reception more strongly positive towards UBS' strategy; outstanding concerns on CS' continued 'Universal Bank' focus



- Positive market reception to strategy
  - Share price uplift of 18% upon announcement
  - UBS price trading above book value at 1.23

- Lower revenue volatility moving forward
- Significant scope for shareholder value creation through redeployment of capital to wealth management; growth through
  - Strong franchise with scale
  - Global capabilities; exposure to emerging markets
- **Most positive outcome of strategy would be achieving capital rebate from FINMA; UBS would recognise significant boost in RoE as a result**



- More muted market reception
  - Share price uplift of 2% upon announcement
  - Still trading at below book value at 0.96

- Combined private banking and asset management still at lower scale than that of UBS (CS group AuM of CHF1.3tr vs UBS group AuM of CHF2.2tr)
- W.r.t. the investment bank, concerns around
  - Transparency of book valuation
  - Volatility of revenue stream
  - Ability to build scale (lags behind Barclays, DB, GS, and JPM in terms of revenue)
- **However, CS has realised 60% uplift in FICC revenues in 2012**