Fitch Revises Credit Suisse Group's Outlook to Stable; Affirms IDR at 'A-'

Fri 29 May, 2020 - 12:19 PM ET

Fitch Ratings - London - 29 May 2020: Fitch Ratings has revised Credit Suisse Group AG’s (CSG) Outlook to Stable from Negative. Its Long-Term Issuer Default Rating (IDR) has been affirmed at 'A-' and Viability Rating (VR) at ‘a-’. A full list of rating actions is below.

The Outlook revision reflects our view that CSG ratings have sufficient headroom to absorb significant shocks under our updated assessment of various possible downside scenarios to our baseline economic forecast. This primarily reflects our assessment of the group's asset quality (a+/negative), capitalisation (a/negative) and funding and liquidity (a/stable), which are all above the group's VR. Reflecting the economic impact of the coronavirus pandemic, CSG’s asset quality and capitalisation will come under pressure in 2020 and into 2021, but these are all scored above CSG’s VR and we do not expect a sustained deterioration that would trigger a downgrade of the VR into the 'bbb' category.

Fitch has also affirmed subsidiaries Credit Suisse AG (CS AG), Credit Suisse (Schweiz) AG (CS Schweiz), Credit Suisse International (CSI), Credit Suisse (USA) Inc (CSUSA), Credit Suisse (Deutschland) AG (CSD) and Credit Suisse Securities Sociedad de Valores SA (CSSSV).
Fitch has also withdrawn the 'A'/'F1' ratings of CS AG's CAD4 billion medium-term note programme, the 'A' long-term rating of CSUSA's USD500 million senior unsecured programme and the 'F1' short-term ratings of CSUSA's commercial paper programmes because the programmes are closed.

**KEY RATING DRIVERS**

**CSG and CS AG**

**IDRs and VRs**

CS AG is the main operating bank of the group and accounts for substantially all of CSG’s consolidated assets. The VRs of CSG and CS AG are assessed on a consolidated basis and reflect the group's strong international wealth management franchise and leading universal-banking presence in Switzerland, as well as improved profitability following the completion of the group's restructuring. They also reflect the group's significant revenue reliance on potentially volatile investment-banking activities and exposure to operational risk inherent in its business model. CSG's VR is equalised with that of CS AG, reflecting moderate double leverage (114% at end-2019), which we expect to remain below 120% and our expectation that the holding company's (holdco) liquidity management will remain prudent.

The Long-Term IDR of CS AG is one notch above its VR due to protection offered to its third-party senior creditors by buffers of subordinated and downstreamed holdco senior debt, which are sustainable in our view given established resolution requirements.

CSG emerged from its restructuring with a lower risk profile and stronger profitability, albeit still moderate for its rating and reliant on capital markets and trading businesses, which generated about 40% of revenue in the 12 months to end-1Q20 (excluding one-off gains). Market volatility has benefitted the group's sales and trading revenue as well as transaction-based income in 1Q20 and may continue to do so in the near term. However, the likely decline of recurring fees and primary capital-market revenues, as well as higher loan impairment charges (LICs) mean, in our view, that achieving 2020 return targets is now unlikely, and that progress towards medium-term profitability objectives will be delayed.
The ratings factor in our expectation that CSG will remain meaningfully profitable in 2020. The mix of CSG's assets under management (AuM), of which only about a third is in the form of equities, should partly cushion the impact of market volatility on AuM volumes and recurring fees. CSG has a good record of managing costs and expects to operate with an adjusted cost base of about CHF16 billion in 2020 (2019: CHF16.9 billion). While we see risks from a potential outsized surge in LICs and further mark-to-market losses in case of a prolonged pandemic and a slower-than-expected economic recovery, we believe further cost cuts are possible to support profitability in a downside scenario.

Asset quality is a rating strength for CSG and is underpinned by the group's low-risk domestic mortgage lending and Lombard lending to wealth-management clients. The impaired loans ratio remains low, at 0.8% at end-1Q20, despite a material inflow of impaired loans in the quarter in the APAC division and in the corporate loan book. 1Q20 LICs of CHF568 million were already close to twice their normal annual run-rate but remained manageable relative to pre-impairment profit. Slightly over half of this amount (CHF304 million) resulted from the adoption of current expected credit loss provisioning under US GAAP from 1 January 2020 and reflected updates to macroeconomic parameters.

Downside risks arise from the group's non-negligible exposures to sectors that are likely to be particularly hit in the near term, including oil & gas (USD7.7 billion net exposure at end-1Q20, of which USD2.9 billion non-investment grade) and shipping. CSG is a leading participant in the leveraged-finance market with an underwriting exposure of USD7.3 billion at end-1Q20. CSG recorded USD294 million of mark-to-market losses on leveraged finance underwriting in 1Q20 although part of this is likely to have been recovered as credit spreads have tightened since end-March. In addition, the group recorded CHF160 million of mark-to-market losses net of hedges on performing loans carried at fair value in the APAC division. However, the strong starting point implies only remote prospects of asset-quality deterioration jeopardising CSG's 'a-' VR even under various downside scenarios to our baseline.

CSG's CET1 ratio stood at 12.1% at end-1Q20, down from 12.7% at end-2019 due to RWA inflation caused by market volatility and business volume growth. CSG expects to operate with a CET1 ratio of around 11.5% for the remainder of 2020, below its previous guidance of around 12%, as RWAs are likely to increase further despite the group's efforts to mitigate RWA growth. The ratings factor in our expectation that CSG will be able to restore its CET1 ratio to target levels in 2021. Our assessment of group's capitalisation also takes into account its Tier 1 leverage ratio of 5.3% and CET1 leverage ratio of 3.8% at end-1Q20 - without
factoring in the temporary exclusion of central-bank placements from the denominator - which compare well with most European peers'.

The funding profile of CSG benefits from a well-established and diversified deposit base, stemming from its domestic franchise and international wealth-management activities. The group's business model relies on significant, although decreasing, access to confidence-sensitive wholesale funding. Use of short-term unsecured funding is moderate.

The average group liquidity coverage ratio (LCR) decreased to 182% in 1Q20 from 198% in 4Q19. The decrease was due to higher counterparty margin requirements and drawdowns on committed facilities partly offset by long-term debt issuance and deposit growth. CSG’s high-quality liquid assets on average amounted to CHF162 billion in 1Q20, after haircuts (19% of end-1Q20 assets). Continued long-term debt issuance since end-1Q20 is likely to have further boosted the group's liquidity buffer.

CS AG's and CSG's Short-Term IDRs of ‘F1' and 'F2' are the baseline options mapping to their Long-Term IDRs of 'A' and 'A-' respectively. In the case of CS AG, this is because the group's funding and liquidity score of ‘a’ is below the minimum required for the higher Short-Term IDR option under Fitch's criteria. In the case of CSG, this is because the group's liquidity is managed and retained at CS AG level.

SUPPORT RATINGS AND SUPPORT RATING FLOORS

CSG and CS AG's Support Ratings (SRs) and Support Rating Floors (SRFs) reflect our view that senior creditors of both the holding and the operating bank can no longer rely on receiving full extraordinary support from the sovereign if the group becomes non-viable, largely due to progress made in Swiss legislation and regulation to address the 'too big to fail' problem for the two large Swiss banks.

DERIVATIVE COUNTERPARTY RATINGS AND DEBT RATINGS

The Derivative Counterparty Rating (DCR) of CS AG is at the same level as its Long-Term IDR because derivative counterparties in Switzerland have no definitive preferential status over other senior obligations in a resolution.

Senior unsecured debt issued by CS AG and CSG is rated in line with the entities' respective IDRs. Total loss absorption capacity (TLAC)-eligible senior unsecured debt issued by Credit Suisse Group Funding (Guernsey) Limited and guaranteed by CSG is rated in line with the guarantor's IDR.
Subordinated debt and other hybrid securities issued by CS AG and CSG are all notched down from CS AG's and CSG's VRs in accordance with Fitch's assessment of each instrument's loss severity and incremental non-performance risks relative to the VRs.

Subordinated Tier 2 debt with no coupon deferral options is rated two notches below the VR for loss severity, which is Fitch's baseline notching for this type of debt.

CSG's additional Tier 1 debt with fully flexible coupons is rated four notches below the entity's VR. The notching comprises two notches for loss severity, reflecting the notes' deep subordination, and two notches for incremental non-performance risk relative to the VR, due to fully discretionary coupon omission. We expect the group to maintain adequate buffers above the mandatory coupon omission points of well in excess of 100bp of RWAs.

SUBSIDIARIES

CS SCHWEIZ

CS Schweiz, a subsidiary of CS AG, houses the group's domestic retail and commercial banking activities and broadly corresponds to the group's Swiss Universal Bank business division. Its 'a' VR reflects its low-risk domestic loan book, moderate volumes of trading assets, sound capitalisation and a strong deposit franchise. The VR also reflects its deep integration with CS AG and high fungibility of liquidity and capital between the two entities in the normal course of business.

Its Long-Term IDR of 'A+' is one notch above its VR because of significant buffers of junior and internal bail-in debt that offer protection to senior creditors of CS Schweiz in case of its failure. The Outlook on CS Schweiz's Long-Term IDR mirrors that on the parent because we expect their ratings to remain highly correlated.

The Short-Term IDR of 'F1' is the baseline option mapping to the Long-Term IDR of 'A+' because the funding and liquidity score of CS Schweiz is insufficient to achieve the higher Short-Term IDR under Fitch's criteria. The DCR is at the same level as the Long-Term IDR because derivative counterparties in Switzerland have no definitive preferential status over other senior obligations in a resolution.
CS Schweiz's Support Rating of '1' primarily reflects our view that the entity is an integral part of CS AG, and that its default would constitute significant reputational risk to its parent, increasing CS AG's propensity to provide extraordinary support, if required.

OTHER SUBSIDIARIES

CSI (based in the UK), CSD (based in Germany) and CSSSV (based in Spain) are wholly-owned subsidiaries of CS AG. CSUSA is a US holding company directly held by Credit Suisse Holdings (USA), Inc., the group's US intermediate holding company, which is owned by CS AG. Their SRs and Long-Term IDRs, which are equalised with the Long-Term IDR of CS AG, reflect our view that these entities are extremely likely to be supported by the parent in case of need. We view these entities as integral to the group's business and core to CS AG's strategy, and believe that their default would constitute material reputational damage for the parent. The Outlooks on the Long-Term IDRs mirror that on CS AG.

We use CS AG's Long-Term IDR as the anchor rating because we expect that senior creditors of CSI, CSUSA, CSD and CSSSV will benefit from the parent's junior debt buffers given their high degree of integration with the parent and the group's single point-of-entry resolution strategy. In the case of CSI and CSUSA, this expectation is further underpinned by the regulatory requirement to pre-place sufficient bail-in debt and equity in the subsidiary or by the jurisdiction of the subsidiary.

CSI's and CSSSV's DCRs are at the same level as the entities' Long-Term IDRs because derivative counterparties have no definitive preferential status over other senior obligations in a resolution in the UK (CSI) or in Spain (CSSSV).

CSD's deposit ratings are aligned with the entity's IDRs. In Fitch's opinion, the bank's debt buffers are not likely to afford any obvious incremental probability of default benefit above the group's support benefit factored into the German subsidiary's IDRs. In addition, we have not assigned any uplift for above-average recovery prospects in the event of default due to limited visibility on recoveries in such circumstances.

The entities' Short-Term IDRs of 'F1' are equalised with CS AG's. CSI's and CSUSA's senior unsecured debt ratings are in line with the entities' respective IDRs.

Credit Suisse New York branch's IDRs and senior unsecured debt ratings are at the same level as those of CS AG because the branch is part of the same legal
entity and, in our view, there are no country risk restrictions. The alignment of
IDRs reflects our view that senior creditors of the branch would be treated
identically to other senior creditors of CS AG.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to negative rating
action/downgrade:

The ratings remain sensitive to the ultimate depth and duration of the
coronavirus shock to the international economy and financial markets, and the
pace of economic recovery once the acute phase of the crisis passes. While CSG's
and CS AG's ratings have sufficient headroom to withstand various downside
scenarios to Fitch's baseline, they could be downgraded if the economic and
financial market disruption arising from the pandemic places severe and
sustained pressure on the group's asset quality, earnings and capitalisation.

We would likely downgrade CSG's and CS AG's ratings if we expect that CSG will
not be able to maintain its CET1 ratio above 11% in 2020 and restore it to target
levels in 2021. This could be due to significantly higher-than-expected
impairment charges due to materially sharper or longer shock to the economy or
large unexpected pre-tax losses in capital-market activities, which could indicate
weaknesses in risk controls.

CSG's ratings are also sensitive to the amount of double leverage at the holdco
and could be downgraded if we expect it to increase and remain above 120%.
CSG's and CS AG's Tier 2 debt and CSG's additional Tier 1 debt would be
downgraded if the entities' VRs are downgraded. CSG's additional Tier 1 debt
could also be downgraded if its non-performance risk relative to the VR
increases, for example if we no longer expect CSG to be able to maintain capital
buffers of at least 100bp of RWAs above mandatory coupon restriction
thresholds.

The Long-Term IDR and VR of CS Schweiz would likely be downgraded if CSG and
CS AG are downgraded given the significant correlation in their credit profiles.
The ratings are also sensitive to deterioration of the standalone profile of CS
Schweiz, and would be downgraded if the economic and financial-market
disruption arising from the pandemic places sustained pressure on earnings and
capitalisation.
The IDRs of other subsidiaries would be downgraded in case of a downgrade of CS AG. They would also be downgraded to the level of CS AG's VR if we no longer expect their senior creditors to benefit from the parent's resolution debt buffers.

DCRs, senior debt and deposit ratings (where assigned) would be downgraded if the respective entities' IDRs are downgraded.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

An upgrade of CSG's and CS AG's ratings is unlikely in the near term given the risks posed by the coronavirus shock but could result from significant progress in meeting the group's profitability ambitions without increasing the risk appetite. CS AG's Short-Term IDR could also be upgraded if the bank's funding and liquidity score is upgraded to 'aa-'.

CSG's and CS AG's Tier 2 debt and CSG's additional Tier 1 debt would be upgraded if the entities' VRs are upgraded.

An upgrade of CS Schweiz would require an upgrade of CS AG and a longer track record of strong and stable earnings and capitalisation.

The ratings of the other subsidiaries are likely to be upgraded if CS AG is upgraded.

DCRs, senior debt and deposit ratings (where assigned) would be upgraded if the respective entities' IDRs are upgraded.

**BEST/WORST CASE RATING SCENARIO**

International scale credit ratings of Financial Institutions issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and
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REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

The ratings of CSI, CSD, CSSSV, CSUSA and Credit Suisse NY branch are directly linked to CS AG. The ratings of Credit Suisse Group Funding (Guernsey) Limited are directly linked to CSG AG.

ESG CONSIDERATIONS

The highest level of ESG credit relevance, if present, is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity(ies), either due to their nature or to the way in which they are being managed by the entity(ies). For more information on Fitch’s ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

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Applicable Criteria

Non-Bank Financial Institutions Rating Criteria (pub. 28 Feb 2020) (including rating assumption sensitivity)
Bank Rating Criteria (pub. 28 Feb 2020) (including rating assumption sensitivity)

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Solicitation Status
Endorsement Policy
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Credit Suisse AG                           EU Issued
Credit Suisse Group AG                     EU Issued
Credit Suisse Group Funding (Guernsey) Limited EU Issued
Credit Suisse International                EU Issued
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