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Credit Suisse Group AG

Improved capitalisation and higher pre-tax profits on positive operational leverage and lower non-core losses

For Q2 2017[1], Credit Suisse Group AG (CS, Baa2 stable)[2] reported an (unadjusted)[3] net profit of CHF 303 million, up 78% from a year earlier. This corresponds to an annualised return on risk-weighted assets (RWAs) of 47 basis points (bps), compared to 25 bps a year earlier, and an annualised return on equity of 2.8% (2Q16: 1.5%). CS's good quarterly performance was driven by (1) a 8% decrease in operating expenses, with decreases across all divisions apart from International Wealth Management (IWM), (2) a 2% rise in net revenues, as higher revenues from the Swiss Universal Bank (SUB), International Wealth Management and Asia Pacific Wealth Management and Connected offset weaker capital markets revenues and (3) Capital and leverage ratios strengthened in the quarter reflecting the CHF4 billion capital raise, bringing the CET1 ratio to 13.3% of risk-weighted assets (+160 bps), now in line with Moody's GIB[4] median. These results are broadly in line with our expectations.

Revenue rises from wealth management and Swiss operations offset capital markets revenue weakness[5]. Strong revenue increases were recorded across IWM (+10%), SUB (+5%) and Asia Pacific Wealth Management and Connected (+23%). Capital markets revenues were sharply down in Asia Pacific Markets, in both equity and fixed income sales and trading (-47% combined). Revenues were also down in GM's Solutions product (-52%) and in debt underwriting, advisory and other fees (-12% combined) in Investment Banking and Capital Markets (IBCM). These declines were not offset by good results from GM in Credit (+22%) and Equities (+5%), and in IBCM from equity underwriting (+12%).

Credit Suisse continued to make strong progress in reducing its cost base, achieving a further CHF 350 million of net cost savings in the quarter. Operating expenses were lower in all divisions apart from IWM, and reductions were particularly pronounced in the GM division and in the non-core unit. In H1 2017, CS has achieved two-thirds (CHF 0.6 billion) of its >CHF 0.9 billion net cost reduction target for 2017. Credit provisions rose to CHF82 million from a reversal of CHF28 million in the prior year, primarily reflecting lower reversals from the non-core unit and higher credit impairments in the Swiss corporate sector.

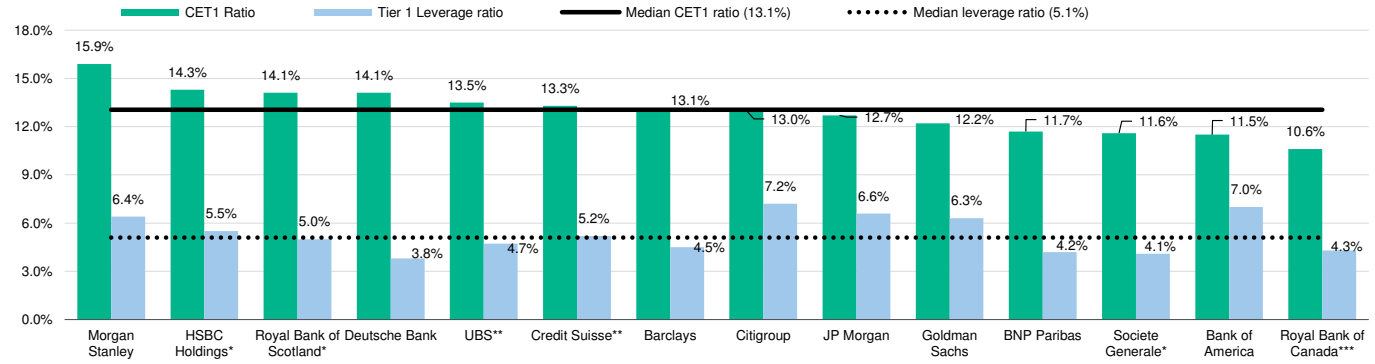
Non-core losses and exposures continued to decline, reducing the impact on pre-tax profits and capital. Non-core losses in the Strategic Resolution Unit (SRU) narrowed by nearly CHF0.2 billion versus 2Q16 and risk-weighted assets and leverage exposures declined by 8% and 13%, respectively versus 1Q17.

Capitalisation and leverage position strengthened, reflecting the CHF4 billion rights issue. The rights issue was the primary driver for a 160 bps increase in the CET1 ratio to 13.3%; which brings CS now in line with the Moody's GIBS peer median (Exhibit 1).

Detailed Considerations

Exhibit 1

Common Equity Tier 1 (CET1) ratio and Tier 1 Leverage Ratio for Global Investment Banks, End-June 2017



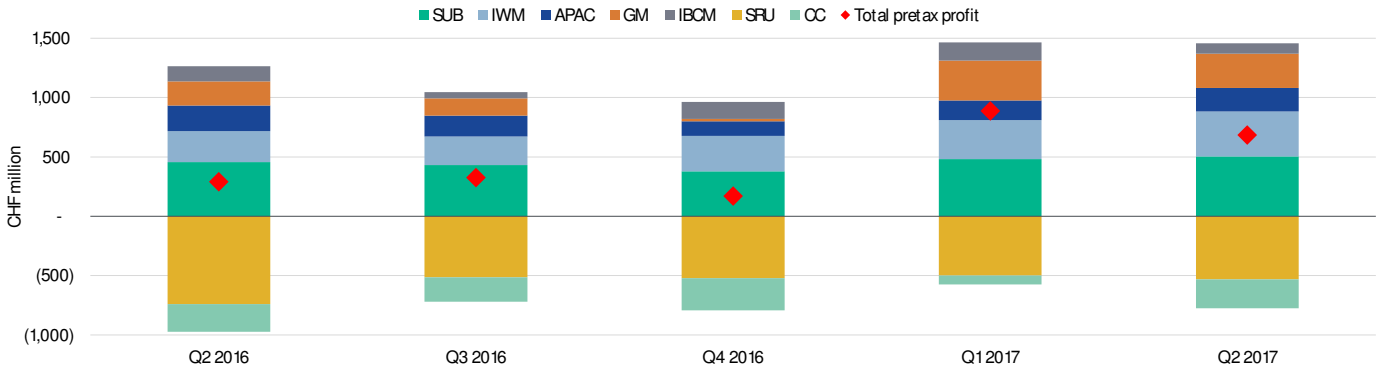
*figures as of end-March 2017, **UBS and CS leverage ratio reflect Common Equity Tier plus Low Trigger Additional Tier 1 and High-Trigger Additional Tier 1 securities
Source: Company results presentations and financials, Moody's

Credit Suisse maintains a sound liquidity position, reporting a daily average Liquidity Coverage Ratio of 165% in 2Q17. Customer deposits increased 1% from 1Q17 to CHF323 billion. Outstanding long-term debt declined to CHF176.7 billion from CHF183.7 billion. In the first six months of the year, Credit Suisse issued CHF6 billion of long-term debt and CHF2 billion of high-trigger Additional Tier 1 instruments to meet Swiss Too-Big-Too-Fail (TBTF) requirements which are fully phased-in by 1 January 2020.

Within the business segments, key operating and financial trends were as follows:

Exhibit 2

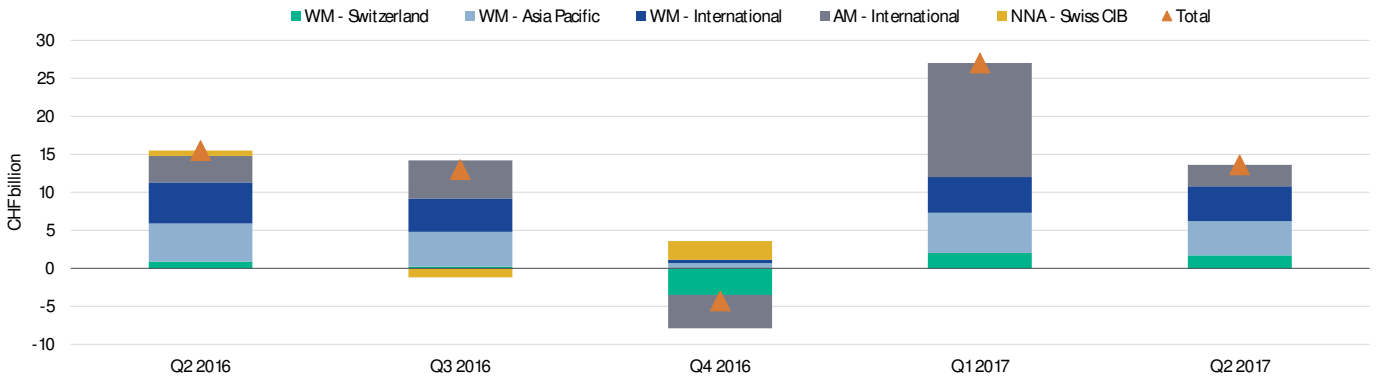
Credit Suisse Adjusted Profit Before Tax by Segment



*SUB: Swiss Universal Bank, IWM: International Wealth Management, APAC Asia Pacific, GM: Global Markets; IBCM: Investment Banking and Capital Markets, SRU: Strategic Resolution Unit, CC: Corporate Center
Source: Company results presentations and financials, Moody's

Exhibit 3

Net New Assets (NNA) by Region



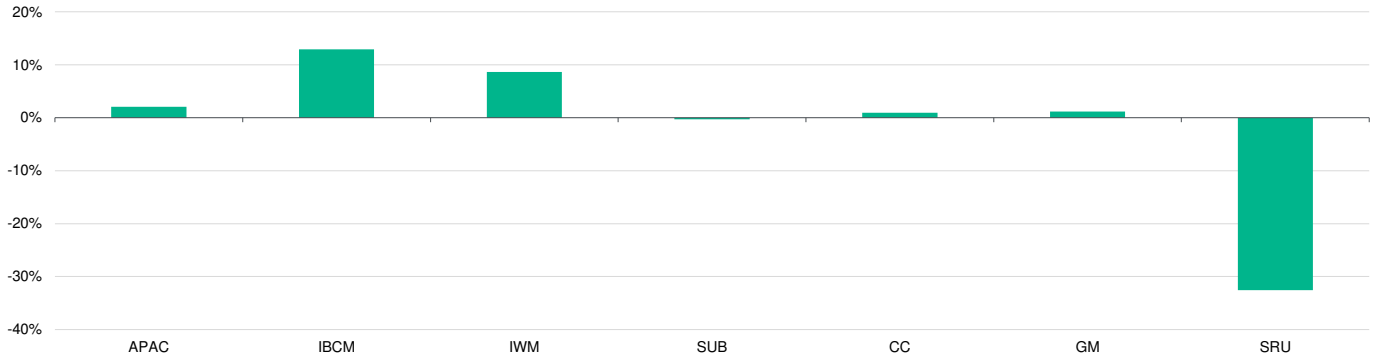
Note: excluding Strategic Resolution Unit and not adjusted for assets managed across businesses, WM: Wealth Management (Private Banking), AM: Asset Management, NNA - Swiss CIB: Net New Assets Swiss Corporate and Institutional Banking

Source: Company financials, Moody's

Exhibit 4

Credit Suisse has re-deployed RWAs freed up from non-core operations and Global Markets into its Asia Pacific, International Wealth Management and Investment Banking and Capital Markets divisions

Percentage Change in RWAs Q2 2017 vs Q2 2016



Source: Company financials, Moody's

Swiss Universal Bank ("SUB") reported adjusted pre-tax profits of CHF 504 million, up 10% versus the same quarter a year ago reflecting higher operational leverage with revenues up 5% and operating expenses down 1%. Credit loss expenses rose to CHF36 million (net of gains from credit hedges) from CHF9 million a year ago. The rise in credit losses related to a few specific corporate exposures. These results underscore the continued progress the bank has made in reducing its cost base to boost profitability under the backdrop of the continued headwinds in Switzerland from negative interest rates and subdued client activity. For the last six quarters, SUB has consistently reported improved year-over-year pre-tax profits. Assets under management (AUM) across SUB increased in the quarter by 1% to CHF 554 billion , reflecting higher asset valuations in AUM in from Private Clients (PC) and Corporate and Institutional Banking (CIB) and higher net new asset (NNA) inflows from Private Clients (PC) .

International Wealth Management ("IWM") reported adjusted pre-tax profits of CHF 378 million for the quarter, up 45% from a year ago . Within IWM, Private Banking adjusted pre-tax income in the quarter was up 56% to CHF307 million as broad based increases in net interest income (+18%),recurring commissions and fees (+11%) and transaction and performance based revenues (+12%) offset higher operating expenses (+2%). The rise in IWM PB net interest income reflected higher loan and deposit margins on both higher average loan and deposit volumes. Asset Management reported a 13% rise in adjusted pre-tax income to CHF 71 million on lower operating expenses and slightly higher revenues. IWM saw good NNA inflows of CHF 7.4 billion during the quarter (2Q16: 8.9 billion), mainly reflecting inflows from emerging markets and Europe and traditional and alternative investments, partly offset by

outflows from joint ventures. Across IWM, the division manages a total CHF 702 billion in assets under management, flat on 1Q17 . Risk-weighted assets increased by 2% in the quarter to CHF36.5 billion.

Asia Pacific ("APAC") reported adjusted pre-tax profits of CHF 199 million in the quarter, an 8% decline compared to the prior year and the third consecutive quarter of year-on-year decline in pre-tax profits. Continued weak performance in APAC Markets overshadowed improved results in APAC Wealth Management and Connected (WM&C). The decline in APAC Markets profits was driven primarily by a continued decline in fixed income sales and trading (-29%) , reflecting lower revenues from developed market rates products , and a decline in equity sales and trading (-40%). Operating expenses in Asia Markets reduced by 18 %, reflecting lower compensation and also the transition of the systematic market making business to IWM AM . APAC WM&C on the other hand reported a strongly improved performance with adjusted pre-tax profits up 78% as net interest income (+13%), recurring fees and commissions (+22%) and transactional based revenues (+27%) increased, more than offsetting higher operating expenses (+6%) . Risk-weighted assets decreased by 2.4% in the quarter to CHF32.3 billion .

Global Markets ("GM") reported an adjusted pretax profit of $300 million, up 44% relative to the same period last year. GM has now reported five consecutive quarters of adjusted pretax profit after recording pretax losses in 4Q15 and 1Q16 when it booked write-downs on inventory and CS subsequently announced a further de-risking and accelerated restructuring of the division. The improved pre-tax profit in 2Q17 reflected lower operating expenses which offset lower revenues. Within the business, lower revenues from Solutions (-52%) reflecting lower client trading activity and lower results from the Systemic Market-Marking Group (SMG) which were partly offset by higher results from Credit (+22%) and Equities (+5%) . The decline in the SMG result partly reflects the transition of this business to IWM AM in 1Q17 . CS made further progress in cost reduction initiatives as operating expenses reduced 16% to $1.25 billion , reflecting lower compensation expenses, lower allocation of group corporate function costs and lower professional service costs . RWAs rose in the quarter by 3% to $54 billion and leverage exposures by 1% to $289 billion , respectively. Global Markets is now operating at CS's leverage exposure cap of $290 billion for the division, however short of its RWA ceiling of $60 billion.

Investment Banking and Capital Markets ("IBCM") reported adjusted pre-tax income of $92 million, a decline of 30% relative to the prior year. The lower revenues (-6%) were only partly offset by lower operating expenses (-1%); correspondingly the cost-income ratio rose to 80% from 76% in Q2 2016. Within revenues, lower debt underwriting revenues (-11%) and Advisory and other fee revenues (-14%) were partly offset by higher equity underwriting revenues (+12%). The debt underwriting results reflected lower investment grade underwriting revenues and derivatives financing revenues, partly offset by higher leveraged finance revenues .

The **Strategic Resolution Unit ("SRU")** reported a (unadjusted) pre-tax loss of CHF 563 million in the quarter, relative to a pre-tax loss of CHF 759 million for the same period last year. In the quarter, CS continued to make good progress in reducing its non-core exposures recording a CHF3 billion reduction (-8%) in risk-weighted assets in the quarter to CHF 38.1 billion and a corresponding reduction in leverage exposures of CHF 11 billion (-13%) to CHF 71.6 billion. Excluding foreign exchange movements in the quarter, the corresponding reductions in RWA and leverage exposures were CHF2 billion and CHF9 billion, respectively. These reductions reflect the reduction of emerging market loan and derivative exposures and the sale or unwind of private equity fund and ship financing exposures and the unwind and restructuring of life insurance and derivative exposures. Credit Suisse guided that it continues to expect the disposal cost in CHF million per unit of risk-weighted assets to increase, but to remain below 3% of risk weighted assets (2Q17: 1.7%) as it seeks to reduce its relatively more leverage-intensive exposures. CS also maintained its RWA target of CHF30 billion by end-2018 when the remaining SRU portfolio is expected to be folded back in to the core business. Within the SRU, CHF 19.6 billion of RWAs is in operational risk.

Corporate Centre reported a pre-tax loss of CHF 245 million in the quarter in line with a loss of CHF 235 million in the in the same period last year (excluding fair value changes in own debt, which Credit Suisse reports in Other Comprehensive Income).

Rating Considerations

We assign a rating of Baa2 to the senior unsecured debt of Credit Suisse Group AG, the group's holding company. We rate the junior deposit and senior unsecured debt of the group's main operating company Credit Suisse AG at A1. The ratings outlook on both Credit Suisse Group and Credit Suisse AG is stable. Credit Suisse AG has a Baseline Credit Assessment (BCA) of baa2.

Endnotes

1 All figures in this report relate to Q2 2017 and comparisons are made to Q2 2016, unless otherwise indicated

2 Credit Suisse Group AG (LT senior unsecured Baa2 stable) is the parent holding company of Credit Suisse AG (LT deposits A1 stable, LT senior unsecured A1 stable, baa2 BCA). BCA: Baseline Credit Assessment

3 Unless indicated otherwise, figures are on a Credit Suisse adjusted basis. Moody's does not adjust for restructuring and litigation expenses whereas Credit Suisse's adjusted figures take out restructuring expenses and major litigation expenses.

4 Global Investment Bank

5 Comparisons versus Q2 2016 are partly complicated because the systemic market making group transferred to IWM from the Global Markets (GM) division and Asia Pacific Markets division in 1Q2017.

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