Credit Suisse taken over amid fears of financial meltdown

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In an emergency action aimed at trying to prevent a meltdown of the European and global financial system, the Swiss government, the Swiss National Bank and the country's financial authority, FINMA, organised the sale of the beleaguered bank Credit Suisse to UBS.

The decision, in which it overrode through executive action a requirement that shareholders vote on any takeover, was announced by the government at a press conference Sunday evening before Asian markets opened today.

It came after a series of measures last week, including a $54 billion liquidity provision by the central bank for Credit Suisse, later extended to around $100 billion, failed to staunch the flow of money out of the bank, reported to be at least $10 billion per day last week.

Announcing the decision, under which UBS will take over Credit Suisse at a cost of $3.25 billion, Swiss president Alain Berset said: "On Friday the liquidity outflows and market volatility showed it was no longer possible to restore market confidence and a swift and stabilising solution was absolutely necessary."

He warned that an "uncontrollable collapse of Credit Suisse would lead to incalculable consequences for the country and the international financial system."

Under the deal, hammered out in series of crisis meetings over the weekend, the Swiss government will provide more than $9 billion to UBS to cover some of the losses it may incur as a result, and the central bank will make available $100 billion to UBS to facilitate it.

However, the Swiss finance minister, Karin Keller-Sutter, claimed it was not a bailout but a "commercial solution."

In her press conference remarks, she pointed to the global implications of the Credit Suisse crisis.

"The bankruptcy would have had huge collateral damage on the Swiss financial market and a risk of contagion internationally. The US and the UK were very grateful for this solution… they really feared a bankruptcy of Credit Suisse."

The same message was delivered by the financial regulator FINMA. It said Credit Suisse had experienced a "crisis of confidence" and there was "a risk of the bank becoming illiquid, even if it remained solvent, and it was necessary for authorities to take action to prevent serious damage to the Swiss and international financial markets."

The forced sale of Credit Suisse is the most significant in the banking system since the crisis of 2008 and it is far from clear that further ramifications have been averted. As the *Financial Times* noted in a comment, "whether it would halt European bank runs is unknowable. Reassurance is a dangerous game in a financial panic. It can easily confirm the fears of investors as allay them."

While it had been weakened by the tens of billions of dollars in losses resulting from the collapse of Archegos Capital and the Greensill financial firm, as well as low profitability in some of its investment activities, the trigger for its demise did not emerge from within Credit Suisse itself.

Rather, its collapse is an expression of the vast shift in the financial landscape over the past year as central banks, led by the US Fed, have rapidly raised interest rates after providing essentially free money for 15 years under various forms of "quantitative easing."

It was set off by the collapse of the US Silicon Valley Bank, when it was taken over by the Federal Deposit Insurance Corporation on March 10 after a $40 billion bank run.

Credit Suisse then came under intense pressure last week after the Saudi National Bank, one of its backers, with 10 percent of its shares, announced it was not going to put in any more capital. The Swiss central bank then offered a $50 billion credit, but this seems to have deepened the crisis rather than alleviating it, leading to the emergency meetings over the weekend.

Credit Suisse has been a globally significant bank for decades, operating in Europe, Asia and the US. At the end of 2022, it had a balance sheet of half a trillion dollars and 50,000 employees around the world, thousands of whom will be laid off because of the USB takeover.

And there are clearly fears that its takeover and the crisis it expresses will be manifested in other parts of the financial system. Coinciding with the Credit Suisse decision, the Fed and five other major central banks announced measures to increase the flow of dollars into the global financial system to ensure adequate liquidity.

The FT reported that one of the concerns of European authorities is that the "heavy losses imposed on Credit Suisse shareholders, and bondholders" holding its debt could "increase stress in the bank funding market this week."

In a joint statement, the central banks said that from today they would hold daily auctions of dollars rather than weekly to "ease strains in global funding markets."

On the other side of the Atlantic, there are indications that, far from abating, the crisis set off by the SVB collapse is intensifying. When markets open today attention will focus on the First Republic Bank, one of the first to suffer "contagion" from the demise of SVB.

Last week, 11 major banks, spearheaded by JPMorgan Chase and its CEO Jamie Dimon, with the collaboration of US Treasury Secretary Janet Yellen, decided to deposit $30 billion between them with First Republic to alleviate concerns that, like SVB, it would have problems meeting depositors' withdrawals.

But so far, at least, the plan does not seem to be working. Despite the $30 billion inflow, shares in the bank plunged more than 30 percent on Friday, bringing the total loss since the SVB collapse to more than 70 percent.

First Republic has the same problem as SVB. The market value of its holdings of US treasuries and other financial assets it invested in, when interest rates were near zero, is now below their book value because of the interest rate hikes initiated by the Fed. This means it would incur significant losses if these assets had to be sold to meet the cash demands of depositors.

Financial analysts are giving First Republic the thumbs down. Julian Wellesley, global analyst at Loomis Sayles, told the *Wall Street Journal*: "It's not clear whether its viable as a stand-alone entity."

Analysts at KBW, a financial firm which monitors bank performance, said the changes in First Republic's balance sheet over the past week were "staggering," and, together with its decision to suspend the dividend on its common stock, painted a "very dire outlook" for the company and shareholders.

In a note on Friday, analysts at the financial firm Wedbush said there would be "minimal, if any" residual value left if the bank ended up being sold because of the markdown in the value of its loans and securities in any sale.

The crisis at SVB, which is clearly present throughout the banking system, especially among the thousands of smaller and middle-sized banks, has prompted calls for the lifting of the level of deposits which are automatically insured from $250,000.

This has found support from growing sections of the political establishment and from banking industry lobbyists.

Democratic Senator Elizabeth Warren, who likes to present herself as some kind of opponent of the ultra-wealthy who would benefit from such a move, told CBS on Sunday she thought lifting the $250,000 cap was a "good move."

Posing the question of where the new limit should be set, she said, "Is it $2 million? Is it $5 million? Is it $10 million?"

Warren attempted to cloak such a measure, benefiting ultra-wealthy investors--one of the depositors with SVB, the venture capitalist Peter Thiel, stood to lose $5 million had the decision not been made to pay uninsured depositors in full—as giving support for small companies and non-profit organisations to pay wages and their utility bills.

Another aspect of the deepening financial crisis, not attracting the same kind of headlines as the crisis of the banks, but no less significant, is the situation in the $22 trillion US Treasury market, the bedrock of the global financial system.

An FT article at the weekend noted that last week the market for US government debt suffered its most volatile period since the crisis of 2008. Daily trading volumes more than doubled "as the failure of SVB sparked a headlong dash into the safety of Treasuries." So far analysts say market functioning has by and large held up. But that could change at any time.

The article cited comments by Priya Misra, head of global rates research at TD Securities, who said, "We're one crisis away from a complete breakdown of Treasury market liquidity."