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## UBS CALL

By Jacob Brady

On July 11th, it was announced that UBS had actioned their August call and will be redeeming their Additional Tier 1 (AT1) securities at a price of \$100.00. This is a great outcome for noteholders who bought these securities as low as \$87 when IAM first released our Buy recommendation. Below is a summary of the events that took place and the basis of IAM's strong conviction in this trade. In fact, the UBS notes had less than 1.5 years to call (March 2023 – August 2024) and UBS had never missed a call before (either AT1 or T2), further strengthening our conviction to form a Buy recommendation.

Credit Suisse's collapse in March last year sent shockwaves through the global financial system. This was understandable given that Credit Suisse was one of Switzerland's top lenders, had been operating for 167 years, and had previously weathered the Global Financial Crisis. Credit Suisse eventually found itself in a crisis that led to its acquisition by rival UBS, facilitated by the Swiss state to avert a global financial crisis.

One of the fallouts from this was that Credit Suisse's Additional Tier 1 (AT1) securities were written off despite shareholders retaining some value. The deal was put together at immense speed to restore confidence across the European banking sector. Nonetheless, the decision to write down the AT1s to zero led to an aggressive sell-off in the wider European bank AT1 market. Our Head of Credit Strategy, Matt Macreadie, saw this as an overreaction by the market, with similar European banks being affected by a 'guilty by association' scenario, rather than anything specific to their credit profiles, including UBS.

The UBS 4.375% AT1 security was caught up in this sell-off, with the outright yield on these securities widening from 8% to 18% on the events (effectively doubling the yield). This situation demonstrated that in a dislocated market, the quantum of the bid often dictates the price. IAM saw this as an opportunity for investors to take advantage of the heavy sell-off in the European perpetual securities sector while the market was dislocated.

The IAM team's UBS recommendation was based on the following points:

- UBS had always been a much stronger credit than Credit Suisse.
- The Credit Suisse AT1s that were written off were sub-investment grade, whereas UBS's were rated BBB-.
- Credit Suisse's problems began to intensify in Q4 2022, with significant outflows of deposits and assets under management, putting it on a downward trajectory before the crisis.
- The UBS bonds had a high coupon reset margin if they decided not to call, incentivizing them to avoid.
- Post the Credit Suisse/UBS merger, UBS is considered both a Global Systemically Important Bank (G-SIB) and a Domestic Systemically Important Bank (D-SIB).

The chart below shows the UBS sell-off in yields in March 2023 and the rebound once the call has been announced:



Source: Bloomberg

Holding Period Return for investment of \$100,000 from Matt Macreadie's call last year in 2023.

	Settlement Date	Face Value	Price	Gross AUD
<b>Purchase</b>	24-Apr-23	\$ 100,000.00	86.000	-\$ 86,678.80
<b>Coupon</b>	27-Aug-23	\$ 100,000.00		\$ 2,187.50
<b>Coupon</b>	27-Feb-24	\$ 100,000.00		\$ 2,187.50
<b>Sale</b>	14-Jul-24	\$ 100,000.00	100.000	\$ 101,658.65
			TOTAL	\$ 19,354.85
<b>Holding Period Return</b>				<b>22.329%</b>
<b>Total Return</b>				<b>18.337%</b>

With the events playing out as they have, investors were able to achieve 22% returns in an investment-grade-rated security, which is a rare occurrence. We are very pleased with the call announcement - the trade was certainly not without risk, and we are thankful for clients like yourself who had the confidence to follow our recommendation.

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