Credit Suisse's capital increase was never at risk. Were the upheavals during the subscription rights trading period mere hysteria?

The completion of the second part of the capital increase, which Credit Suisse announced last night, comes as no surprise since the sale of the new shares was guaranteed from the outset by the 20 banks that accompanied the transaction.

In the end, according to Credit, almost 873 million new shares were issued with a total value of 2.24 billion Swiss francs ($2.38 billion), corresponding to an uptake of 98.2 percent.

The small residual of the shares that could not be placed with existing shareholders by the end of the exercise period at noon yesterday have been placed with major investors and can be distributed at least at the fixed issue price of the new shares of 2.52 francs. At no time since the start of subscription rights trading did the share price fall below 2.52 francs.
Chairman Must Reassure

Analyst Kian Abouhossein, who monitors Credit Suisse at JP Morgan, wrote the success of the capital injection was already assured on December 6. In early December he said if the share price did not fall below 2.52 francs by the end of the rights trading, it could be assumed the bank's capital increase has been successful.

In the public perception, the capital increase of Switzerland's second-largest bank appeared to be an unmitigated disaster. For nearly two weeks, the share price fell steadily, at times reaching an all-time low of 2.654 francs while the prices for credit default swaps (CDS) for Credit Suisse bonds reached new highs.

The bank felt compelled to send Chairman Axel Lehmann and executives on a road show seeking to calm frayed investor nerves. In the meantime, those behind the scenes at the bank admitted to a certain powerlessness. It was all just psychology anyway, and the hysteria around the capital increase no longer had anything to do with hard facts, they argued. Rightly so?

The Limbic System Takes Over

Shareholders tend to make irrational decisions in difficult market phases, with research showing the stock market can send people on an emotional roller coaster ride, during which the limbic system with its pleasure and pain centers regularly overrides the areas of the brain responsible for planning.

The fact that money is firmly linked to the satisfaction of basic needs creates different emotions. Behavioral finance experts say reason cannot compete with this.

Objective Reasons

The herd instinct in financial markets is well-researched and documented. The impulse of investors to sell when prices are falling instead of balancing their positions by buying more. All of these factors may have played a role in the recent slump in the price of Credit Suisse shares amplified by the breathless reporting, not least by media outside of Switzerland.

While that may have played some part in the case of Credit Suisse, a deeper look shows that investors had a logical basis for their skepticism:

- Recently Lehmann appeared on Swiss television stating asset outflows at Credit Suisse
had stabilized, and in its home market, client funds are even returning. However, there are reports of outflows to competing private banks. If only for the sake of caution, investors must reckon with further bloodletting through the end of the year. Abouhossein expects Credit Suisse will see an outflow of 107 billion francs by the end of the fourth quarter, 80 billion of which will be in the core wealth management business. Beginning in October through the middle of November, the bank experienced outflows of just under 84 billion francs, of which nearly 63 billion were in wealth management.

- The outflows are concerning because less volume generates less income. Credit Suisse urgently needs the money to finance the restructuring of the bank. Recently the bank started offering special conditions to wealthy private clients, such as high interest rates on fixed-term deposits if they continue to do business with the bank. There was also talk of loyalty bonuses. These costs, along with high-interest rates on new bonds that the bank recently issued, could prompt a further turning of the cost screws if developments worsen in order to achieve the targets set for the end of 2025.

- Observers say Credit Suisse's increased financing costs are particularly sensitive for the repositioning of the investment bank, as it is primarily the new trading unit to be built that is being funded with bonds. Outflows in wealth management, which in turn cause CDS prices to rise and make refinancing even more expensive, would therefore lead to a kind of vicious cycle. Only when the new investment banking business regains its footing will it be less dependent on borrowed capital.

**Breakup Scenarios**

The bank's income and costs are currently out of balance and it projects a pre-tax loss of up to 1.5 billion francs in the fourth quarter. If contrary to expectations, the stabilization promised by the bank's management does not materialize afterward, the condition of Credit Suisse could deteriorate rapidly.

JP Morgan's Abouhossein describes a scenario in which the Swiss business is split off from the bank and sold and taken public. Meanwhile, buyers from the industry would have to be found for the asset management and fund business while the investment bank would have to be closed down altogether. This would certainly generate further anxiety among stock market players.