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Swiss banks set for greater consolidation

By Haig Simonian

With two big deals in less than a month, the long-forecast consolidation of Swiss private banking looks as though it has finally arrived.

Last month, a controlling stake in Sarasin, the big Basel-based private bank with SFr106bn ($115bn) in assets under management, was bought for SFr1.04bn by Safra Group, the Brazil-based family-owned bank. Days earlier, Credit Suisse said it would swallow Clariden Leu, an independently run subsidiary that was itself the product of a five-way merger.

Predictions of consolidation are not new. Regulatory burdens have been rising steadily, with spiralling costs for compliance and sophisticated information technology. Bilateral tax agreements reached with Germany and the UK will allow clients to remain anonymous. But banks will have to invest in staff and IT to levy the taxes central to the new accords.

Those arrangements, alongside many countries' crackdown on tax evasion, will shrink clients' assets – a crucial component of bank earnings – as some customers use their balances to pay the one-off penalties. Others may exit Switzerland altogether.

The Swiss financial sector is set to lose SFr47bn ($51bn) in assets and SFr1.1bn ($1.2bn) in revenues, Booz & Co, the strategy consultancy, calculated last week.

Commissions on client activity – a second key earnings source – have plunged as customers sit on their hands amid troubled markets. And the soaring Swiss franc has lowered the local value of foreign denominated accounts, on which the banks levy their annual management fees.

"Given the continuing unfavourable market conditions, many small and mid-sized banks and asset management companies are already operating with cost income ratios of well above 80 per cent. I am convinced the consolidation that has already started will continue at an accelerated pace," said Carlos Amman, Booz's managing partner in Switzerland.

Dealmakers agree. "Scale has become strategically mission critical. To preserve profitability, you need a certain scale," said Marco Illy, a top Credit Suisse investment banker in Switzerland.

Others argue that the reasons behind the recent consolidation are more complex. "Many recent deals have been driven as much by one-off factors as the need for size," said Ray Soudah, founder of Millenium Associates, a M&A boutique closely involved in financial services.

The Sarasin disposal was prompted by majority owner Rabobank's decision to raise cash to protect its prized triple A credit rating. Many observers have long questioned the initial Swiss private bank purchase by a Dutch co-operative bank, whose roots are in agriculture, and thought it was only matter of time before a sale.

Credit Suisse's incorporation of Clariden Leu was similarly based as much on internal factors as market forces. "The lack of clear strategy and poor decision making meant even the merged entity didn't achieve its potential. It's been tragic value destruction," said one former executive, who asked not to be named.

The number of past deals also means the ranks of potential consolidators have thinned. UBS and Credit Suisse are both now focused on building capital and slimming down investment banking amid tougher capital requirements.

Other larger banks also have their hands full. BSI is focused on organic growth in Asia and EFG is concentrating on restoring profitability. Much the same applies to Geneva's main banks. UBP is now integrating ABN Amro, and Pictet and Lombard Odier have traditionally shunned takeovers.

So the action may switch to Switzerland's dozens of smaller and lesser-known banks. Often having less than SFr10bn under management, many are considered too small to remain sustainably profitable.

Julius Baer is the most obvious consolidator. The group bought ING's Swiss operations two years ago and has been a regular bidder since. After being pipped at the post for Sarasin and ABN Amro's Swiss subsidiary, Baer is now expected to be more aggressive. Vontobel, a smaller rival that also tried to buy ABN Amro, is also hungry.

The problem is that many smaller banks are family owned. That can make owners reluctant to sell, whatever the economics. And larger private banks may be wary of buying relatively small banks, which may have a disproportionately large amount of undeclared, and therefore unstable, accounts.

That leaves the door open to mergers among smaller banks, with family pride being overcome by joining forces. “Yes, some people are thinking about that,” said Mr Illy.

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