Financial Institutions Ratings
UBS Group AG – AT1 rating report

Security ratings

Outlook	Stable
5.75% EUR 1bn Tier 1 Capital Notes, with 5.125% trigger	BBB
7% USD 1.25bn Tier 1 Capital Notes, with 5.125% trigger	BBB
7.125% USD 1.25bn Tier 1 Capital Notes, with 7% trigger	BBB
6.875% USD 1.575bn Tier 1 Capital Notes, with 7% trigger	BBB
6.875% USD 1.5bn Tier 1 Capital Notes, with 7% trigger	BBB
7.125% USD 1.1bn Tier 1 Capital Notes, with 7% trigger	BBB
5% USD 2bn Tier 1 Capital Notes, with 7% trigger	BBB

Rating rationale

Scope rates at BBB with Stable outlook the above referenced Tier 1 Capital Notes issued by UBS Group AG. While two of the Notes have a 5.125% trigger for permanent write down and five have a 7% trigger, we do not view the risks as being materially different and have not assigned different ratings. The rating is based on the following considerations:

- Senior unsecured debt rating (eligible for TLAC): A+, Stable
- Minimum notches down from senior unsecured debt rating: 4
- Additional notches: 0

In accordance with our rating methodology, the starting point for notching down when rating capital instruments is the senior unsecured debt rating. The minimum four notches reflect the deeply subordinated status of AT1 capital instruments in the priority of claims, their going concern loss absorbing features and investors' exposure to coupon-cancellation risks. At this time, we have not identified any factors which would justify additional notching beyond the minimum four. Please refer to Scope's *Bank Capital Instruments Rating Methodology* published in May 2018 for more details.

We highlight that the securities contain a dividend stopper which is a feature not usually found in CRD IV compliant AT1 securities issued by European banks. The concepts of the combined buffer requirement and the maximum distributable amount also do not apply. Further, the calculation of the capital trigger level is based on CET1 capital as well as Higher-Trigger capital (further details below). Scope considers these features to be beneficial for investors.

The release of this rating report does not constitute a rating action. Last rating action was assigned on 25.09.2017
For further information on the last rating action and regulatory information please click here.

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Issuer credit profile

The Issuer Rating of AA- for UBS reflects the group's resilient business model, which is centred on its market-leading global wealth management franchise and its position as a leading universal bank in its home market of Switzerland. Asset management and investment banking activities further support and complement the overall business franchise. Under various operating conditions, the group's businesses have demonstrated their ability to generate solid earnings.

While the wealth management industry faces challenges such as margin compression, changing customer needs and increasing regulation, the group's strong franchise and long-term focus means that the business continues to grow profitably. The attention to enhancing the client experience and improving efficiency should help UBS mitigate industry headwinds.

Management remains committed to maintaining the group's balance sheet strength. This also means that UBS is well-positioned against relatively demanding Swiss too-big-to-fail requirements which must be met by 1 January 2020. Potential litigation and regulatory costs remain a risk, not only in terms of financial impact but also in terms of reputational damage

Summary terms

Issuer	UBS Group AG
Issue Date	**19 February 2015**
Amount	EUR 1.0bn
Coupon	• 5.75% until first call date, and thereafter at a rate equal to the Mid Market Swap Rate plus 5.287% • Payable annually in arrears on 19 February of each year
Format	Perpetual Tier 1 capital notes, callable 19 February 2022 and every year thereafter
Trigger for Principal Loss Absorption	Consolidated group CET1 capital ratio + Higher-Trigger capital ratio <5.125%, transitional basis
ISIN	CH0271428309

Issue Date	19 February 2015
Amount	USD 1.25bn
Coupon	• 7.00% fixed until first call date, and thereafter at a rate equal to the Mid Market Swap Rate plus 4.866% • Payable annually in arrears on 19 February of each year
Format	Perpetual Tier 1 capital notes, callable 19 February 2025 and every year thereafter
Trigger for Principal Loss Absorption	Consolidated group CET1 capital ratio + Higher-Trigger capital ratio <5.125%, transitional basis
ISIN	CH0271428333

Issue Date	19 February 2015
Amount	USD 1.25bn
Coupon	• 7.125% fixed until first call date, and thereafter at a rate equal to the Mid Market Swap Rate plus 5.464% • Payable annually in arrears on 19 February of each year
Format	Perpetual Tier 1 capital notes, callable 19 February 2020 and every year thereafter
Trigger for Principal Loss Absorption	Consolidated group CET1 capital ratio + Higher-Trigger capital ratio <7%, transitional basis
ISIN	CH0271428317

Issue Date	7 August 2015
Amount	USD 1.575bn
Coupon	• 6.875% fixed until first call date, and thereafter at a rate equal to the Mid Market Swap Rate plus 4.59% • Payable annually in arrears on 7 August of each year
Format	Perpetual Tier 1 capital notes, callable 7 August 2025 and every year thereafter
Trigger for Principal Loss Absorption	Consolidated group CET1 capital ratio + Higher-Trigger capital ratio <7%, transitional basis
ISIN	CH0286864027

Issue Date	21 March 2016
Amount	USD 1.5bn
Coupon	• 6.875% fixed until first call date, and thereafter at a rate equal to the Mid Market Swap Rate plus 5.4965% • Payable annually in arrears on 22 March of each year
Format	Perpetual subordinated contingent permanent write down securities, callable 22 March 2021 and every year thereafter
Trigger for Principal Loss Absorption	Consolidated group CET1 capital ratio + Higher-Trigger capital ratio <7%, transitional basis
ISIN	CH0317921697

Issue Date	**3 August 2016**
Amount	USD 1bn
Coupon	• 7.125% fixed until first call date, and thereafter at a rate equal to the Mid Market Swap Rate plus 5.883% • Payable annually in arrears on 10 August of each year
Format	Perpetual subordinated contingent permanent write down securities, callable 10 August 2021 and every year thereafter.
Trigger for Principal Loss Absorption	Consolidated group CET1 capital ratio + Higher-Trigger capital ratio <7%, transitional basis
ISIN	CH0331455318

Issue Date	**31 January 2018**
Amount	USD 2bn
Coupon	• 5% fixed until first call date, and thereafter at a rate equal to the Mid Swap Rate plus 2.432% which resets every 5 years thereafter • Payable annually in arrears on 31 January of each year
Format	Perpetual subordinated contingent permanent write down securities, callable 31 January 2023 and every year thereafter.
Trigger for Principal Loss Absorption	Consolidated group CET1 capital ratio + Higher-Trigger capital ratio <7%, transitional basis
ISIN	CH0400441280

Main Risks	
Coupon Cancellation	• Fully discretionary • Mandatory if (1) there are insufficient distributable items or (2) if UBS Group AG is not in compliance with all applicable Swiss minimum capital adequacy requirements on a consolidated basis and/or (3) the regulator has requested the issuer not to make such interest payment.
Principal Loss Absorption	• Following the occurrence of a Trigger Event or a Viability Event, a contingent write-down will occur, and the full principal amount of the Notes will automatically and permanently be written down to zero. • A Trigger Event refers to the sum of the CET1 capital ratio and the Higher-Trigger capital ratio of UBS Group AG being less than 5.125% or 7% as applicable. • A Viability Event refers to (1) the regulator determining that the conversion or write-off of all other capital instruments is an essential requirement to prevent UBS Group AG from becoming insolvent, bankrupt, unable to pay a material part of its debt or ceasing to carry on its business; or (2) UBS Group AG has received an irrevocable commitment of extraordinary support from the public sector without which the group would have become insolvent, bankrupt, unable to pay a material part of its debts as they fall due or unable to carry on its business.

Source: Prospectuses, Scope Ratings

Key risks

A. Coupon cancellation

Key risk: Coupon cancellation

Coupon payments on the Notes are fully discretionary and non-cumulative

Coupon payments on the Notes are fully discretionary and non-cumulative. In addition, they are subject to distribution restrictions. Swiss banks, however, are not bound by CRD IV and therefore the concepts of the combined buffer requirement and the maximum distributable amount do not apply.

Further, unlike with AT1 securities issued by other European banks, the Notes contain a dividend stopper – i.e. if UBS does not pay a coupon, the group shall not recommend to ordinary shareholders any dividend or other distribution in cash or in kind be paid or made on any ordinary shares. Capital returns (such as share buy-backs) are also not permitted.

Conditions under which coupon payments are prohibited

UBS is prohibited from making coupon payments on the Notes in the following circumstances:

- The amount of distributable items is less than the sum of (i) the amount of such interest payment plus (ii) all other payments (except redemptions) made by UBS Group AG on the Notes and on any parity obligations or junior obligations, plus (iii) all payments payable by UBS Group AG on any parity obligations or junior obligations, excluding any portion of such payments already accounted for in determining the amount of such distributable items;
- UBS Group AG is not in compliance with all applicable minimum capital adequacy requirements after paying interest on the Notes;
- FINMA, the regulator, has required UBS not to make such an interest payment.

As UBS Group AG had CHF 37.8bn in distributable items as of end-2017, we do not see this as a constraint for paying coupons. Distributable items are defined as the aggregate of net profits carried forward and freely distributable reserves less any amounts that must be contributed to legal reserves under applicable law. Under Swiss corporate law, share premium is included in general capital reserves.

Applicable requirements

The revised Swiss SRB (systemically relevant bank) framework came into effect in July 2016 and is being phased-in until the end of 2019. Under the framework, the fully applied minimum going concern capital requirement is 14.3% of RWAs, of which at least 10% must be met with CET1 capital and the remainder with high-trigger AT1 securities. In addition, there is a minimum going concern leverage ratio of 5%, of which at least 3.5% must be with CET1 capital and the remainder with high-trigger AT1 instruments.

Gone concern requirements mirror going concern requirements, i.e. 14.3% of RWAs and 5% leverage ratio, and can be met with bail-in debt instruments, CET1 capital, AT1 and Tier 2 securities. At its discretion, FINMA, may reduce gone concern requirements if UBS takes additional steps to improve its resolvability. The combination of going concern and gone concern requirements equates to total loss absorbing capacity (TLAC).

The revised Swiss SRB framework provides for the grandfathering of outstanding low-trigger AT1 securities (including the two Notes with a 5.125% trigger) and low- and high-trigger Tier 2 capital securities. Low-trigger AT1 securities qualify as going concern capital until their first call date and thereafter may be used to meet gone concern requirements. Low- and high-trigger Tier 2 capital securities can be used to meet going concern requirements until the earlier of (i) their maturity or first call date or (ii) 31 December 2019. From 1 January 2020, these instruments may be used to meet gone concern requirements.

As of 1Q 2018, the group had already met the fully applied TLAC RWA requirement of 26.6%; this figure includes a 0.2% countercyclical buffer as well as the impact of a 2% rebate for the gone concern RWA requirement.

UBS is also well positioned against fully applied TLAC leverage ratio requirements (Table 1). By taking further steps to improve its resolvability, UBS seeks to merit further rebates for its gone concern requirements. When the Swiss SRB framework becomes fully phased-in from 2020, UBS aims to operate with a less than 4% gone concern leverage ratio.

Table 1: Total loss absorbing capacity

	Actual 1Q 2018 phase-in	2018 requirement	Actual 1Q 2018 fully-applied	Jan 2020 requirement
RWAs (CHF bn)	254		254	
Going concern capital	20.6%	13.1%	17.3%	14.5%
of which CET1	*13.1%*	*9.7%*	*13.1%*	*10.2%*
Gone concern loss-absorbing capacity	10.8%	7.7%	13.9%	12.3%
Total loss-absorbing capacity	**31.4%**	**20.7%**	**31.2%**	**26.8%**
Leverage ratio denominator (CHF bn)	882		882	
Going concern capital	5.9%	4.0%	5.0%	5.0%
of which CET1	*3.8%*	*2.9%*	*3.8%*	*3.5%*
Gone concern loss-absorbing capacity	3.1%	2.6%	4.0%	4.3%
Total loss-absorbing capacity	**9.0%**	**6.6%**	**9.0%**	**9.3%**

Notes: Gone concern requirements include the impact of rebates – 2% for RWAs and 0.7% for the leverage ratio denominator – which are being phased-in until January 2020. Gone concern requirements do not incorporate any countercyclical buffers.
Source: Company data, Scope Ratings

B. Principal loss absorption

Key risk: Principal loss absorption

The mechanism for loss absorption is permanent write down

The rated securities have one trigger:

- Consolidated group CET1 capital ratio + Higher-Trigger capital ratio <5.125% or <7% on transitional basis, as applicable

We consider the write down risk for the Notes as being quite low (outside of a resolution scenario) considering the sound capital position of the group and the way the trigger metric is determined (sum of CET1 capital ratio and Higher-Trigger capital ratio). As of 1Q 2018, UBS Group AG had a phase-in CET1 ratio of 13.1%.

Included in the calculation of the Higher-Trigger capital ratio are high-trigger AT1 securities. As part of the group's employee compensation program (DCCP), UBS has issued CHF 1.6bn in AT1 securities with a trigger for permanent write down if the phase-in CET1 ratio of the group falls below 10% for grants awarded to the group's executive board members and below 7% for other employees. As the 10% trigger on the DCCP securities is above the triggers on the Notes, they provide some additional protection for investors.

As well, for investors in the two Notes with 5.125% triggers, there is an additional cushion of CHF 8.5bn in high-trigger AT1 securities (equivalent to 3.4% of RWAs).

Nevertheless, under the Swiss Capital Adequacy Ordinance, both high-and-low trigger contingent convertible securities (including the Notes) may be written down or converted before the point of non-viability. Further, FINMA retains a fair degree of discretion in determining the point of non-viability.

Distance to trigger

We expect the sum of UBS Group AG's CET1 capital and Higher-Trigger capital ratio to remain largely above the 5.125% and 7% trigger levels. The group guides to a fully applied CET1 ratio around 13%.

Table 2: Distance to 7% trigger

	2017	Q1 2018	2019
Trigger level	7.0%	7.0%	7.0%
CET1 capital ratio, phase-in	14.9%	13.1%	~13% FL guidance
Gap (%)	**7.9%**	**6.1%**	
Gap (CHF bn)	**18.8**	**15.4**	

Source: Company data, Scope Ratings

Table 3: Distance to 5.125% trigger

	2017	Q1 2018	2019
Trigger level	5.125%	5.125%	5.125%
CET1 capital ratio, phase-in	14.9%	13.1%	~13% FL guidance
Gap (%)	**9.8%**	**7.9%**	
Gap (CHF bn)	**23.3**	**20.1**	

Source: Company data, Scope Ratings

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