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UBS Group AG (UBS) Q2 2024 Earnings Call Transcript

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UBS Group AG (NYSE:UBS) Q2 2024 Earnings Conference Call August 14, 2024 3:00 AM ET

Company Participants

Sarah Mackey - Head of Investor Relations
Sergio Ermotti - Group Chief Executive Officer
Todd Tuckner - Group Chief Financial Officer

Conference Call Participants

Giulia Miotto - Morgan Stanley
Andrew Coombs - Citi
Jeremy Sigee - BNP Paribas
Kian Abouhossein - JPMorgan
Anke Reingen - RBC
Chris Hallam - Goldman Sachs
Amit Goel - Mediobanca
Benjamin Goy - Deutsche Bank
Tom Hallett - KBW

Operator

Ladies and gentlemen, good morning. Welcome to the UBS Second Quarter 2024 Results Presentation. The conference must not be recorded for publication or broadcast. [Operator Instructions].

At this time, it's my pleasure to hand over to Sarah Mackey, UBS Investor Relations. Please go ahead, madam.

Sarah Mackey

Good morning, and welcome everyone. Before we start, I would like to draw your attention to our cautionary statement slide at the back of today's results presentation. Please also refer to the risk factors included in our annual report together with additional disclosures in our SEC filings. On Slide 2, you can see our agenda for today.

It's now my pleasure to hand over to Sergio Ermotti, Group CEO.

Sergio Ermotti

Thank you, Sarah, and good morning, everyone. It has been a little over a year since the closing of the acquisition. We made a significant progress, and UBS continues to deliver on all of it. commitments to stakeholders. Putting the needs of clients first during a challenging market environment has allowed us to maintain solid momentum while we fulfill our objective of completing the integration by the end of 2026. As a consequence, not only we have dramatically reduced the execution risk of the integration, we are also well positioned to meet all of our financial targets, hence return to the level of profitability, UBS delivered before being asked to step in and stabilize Credit Suisse.

I'm particularly proud to note that across the combined organization, our people are embracing the pillars, principles and behaviors that drives UBS' culture. This includes client centricity and collaboration, and enable us to successfully manage risk and act with accountability and integrity. I'd like to thank all of my colleagues around the world for their dedication and hard work.

Our second quarter contributed to a strong first half performance, reflecting the strength of our client franchises and disciplined implementation of our strategy and integration plans. Reported net profit for the first half was $2.9 billion, with underlying PBT of $4.7 billion and an underlying return on CET1 capital of 9.2%. We strengthened our capital position and maintained a balance sheet for all season with a CET1 capital ratio of 14.9% and total loss absorbing capacity of around $200 million.

Our parent bank is well capitalized even after withstanding the removal of significant regulatory concessions previously granted to Credit Suisse. As a result, we are executing on our 2024 capital return plans. And as I mentioned last quarter, we are committed to delivering on our mid- to long-term ambitions for dividends and buybacks.

Turning to the integration. We have captured nearly half of our targeted gross cost savings as we restructure our core businesses and wind down noncore and legacy, where we have materially reduced risk-weighted assets over the last 12 months. As part of our derisking efforts, we have also made good progress addressing Credit Suisse's legacy legal issues, including the supply chain finance funds and Mozambique [ph] matters. Following this intense months of execution during which we obtained more than 180 approvals from roughly 80 regulators in more than 40 jurisdictions, we completed the mergers of our parent and Swiss banks and transitioned to a single U.S. intermediate holding company.

This clears the way for the next set of critical milestones that will support the realization of further integration synergies. But let me reiterate something you have heard me say before, we still have a lot of work ahead of us to address Credit Suisse' structural lack of sustainable profitability.

While we are encouraged by the significant progress we have made across the group, the path to restoring profitability to the pre-acquisition levels won't be linear. We're now entering the next phase of our integration, which will be key to realizing the further substantial cost, capital, funding and tax benefits necessary to deliver on our 2026 financial targets. We are following through on our plans amid heightened uncertainties in the markets. These are the moments in which UBS proves its strength, resilience and superior ability to serve and advise clients. This is reflected in the trust that our clients have placed in us every quarter since the close, with a total of $127 billion in net new assets.

We have also remained focused on our strategic objectives to enhance our client offering and leverage the breadth, scale and synergies of our combined franchises. In the Investment Bank, I'm pleased by the client response to the strategic additions we have made to reinforce our capabilities and competitive position. The first half performance is a positive signal that the investments are paying off.

In Global Markets, we saw the highest second quarter on record. And in Global Banking, we have captured sizable market share gains. Importantly, we have achieved these results without compromising on our risk and capital discipline. We are also increasing collaboration across the firm as GWM clients continue to benefit from our IB products and capabilities. This drove the majority of wealth management expansion of client activity this year, particularly in the Americas and APAC.

Another example is our newly created Unified Global Alternatives unit, which combines our alternative investment capabilities across GWM and Asset Management. In fact, this is not just an internal cooperation, we are reshaping the competitive landscape by effectively creating a top 5 global player and limited partner with $250 billion in invested assets across hedge funds, private equity, private credit infrastructure and real estate.

Unified global alternatives will offer our institutional, wholesale, wealth management clients a more comprehensive offering and enhanced access to exclusive co-investment opportunities. It will also provide general partners with a single point of access to the full distribution power of our firm. In Asset Management, we are offsetting margin compression by increasing operational efficiency, which is one of the key focus areas for the business.

In Switzerland, we continue to enjoy the trust of our clients despite a very competitive and, at times, less than constructive environment. With around CHF 30 billion in net new deposits in the last 13 months and approximately CHF 350 billion of loans extended to clients, we continue to maintain our role as an important engine of credit. Since the acquisition, we granted or renewed around CHF 85 billion of loans. Higher interest rates, the cost of increased regulatory capital and liquidity requirements, a changing macroeconomic outlook and, last but not least, the necessity to reprice some loans granted by Credit Suisse at unacceptable risk returns are having an impact on pricing of new credit.

Of course, those are not always easy discussions to have with clients, but we are constructively engaging with them. And I believe the vast majority understand the rationale. Switzerland is a key pillar of our strategy, and we are fully committed to maintaining our leadership. Swiss clients and the economy benefit from UBS' unparalleled competitive global reach and capabilities. In turn, our business is a unique differentiator when serving clients around the world.

A testament of this symbiosis -- as a testament of the symbiosis, we were recognized by Euromoney as Switzerland's Best Bank for the 10th time since 2012, hence the award Best Bank. As we continue our integration journey in the Swiss business, we believe it will be important to further communicate with all our stakeholders about our approach and strategy. To that end, in September, our Head of Switzerland, Sabine Keller-Busse will present at our flagship Best of Switzerland Conference, which brings together investors and corporate clients.

Looking ahead and more broadly, ongoing geopolitical tensions and anticipation ahead of U.S. elections will likely result in heightened market volatility compared to the first half of the year. In this environment, we have two key priorities. First, we must continue to help clients manage the challenges and opportunities that arise. Second, we must stay focused and not allow short-term market dynamics to distract us from achieving our ultimate goal, which is to continue to execute on the integration and invest strategically to position UBS for long-term value creation.

The management appointments we announced in the second quarter will enable us to continue to progress on this journey. At the same time, we can put even more emphasis on our priorities and prospects for sustainable growth, particularly in the Americas and Asia-Pacific. We are confident this will also help us to deliver better outcomes for our clients and the communities where we live and work.

With that, I hand over to Todd.

Todd Tuckner

Thank you, Sergio, and good morning, everyone. In the second quarter, we delivered strong underlying profitability, and we made further progress in reducing costs and optimizing our balance sheet. Net profit in the quarter was $1.1 billion. Our EPS was $0.34 and our underlying return on CET1 capital was 8.4%. Throughout my remarks today, I'll refer to underlying performance in U.S. dollars and make comparisons to our performance in the first quarter, unless stated otherwise. From the third quarter onwards, we'll revert to making year-on-year comparisons. As by then, the prior year period will fully capture combined performance post the Credit Suisse acquisition.

Turning to Slide 6. Total revenues for the quarter reached $11.1 billion, with top line performance in our core businesses holding up nicely from a strong first quarter, down 2% sequentially. Net interest income headwinds were partially offset by higher recurring fee income in our Wealth and Swiss businesses, and by improving activity in IB Capital Markets. Revenues in our noncore and legacy business were positive in the quarter, albeit $0.6 billion lower versus an exceptional first quarter. On a reported basis, revenues reached $11.9 billion and included $0.8 billion of mainly purchase price allocation adjustments in our core businesses, with an additional $0.6 billion expected in the third quarter.

Underlying operating expenses in the quarter were $9 billion, decreasing by 3%. Excluding litigation and variable and financial adviser compensation tied to production, expenses were also down 3% as we further progressed our cost-cutting and workforce management initiatives despite the intense integration agenda. At the end of the second quarter, we were about 3,500 fewer total staff compared to the end of the first quarter, and 23,000 or 15% fewer since the end of 2022. Integration-related expenses in the quarter were $1.4 billion, resulting in reported operating expenses of $10.3 billion. Credit loss expense was $95 million, driven by a small number of positions in our Swiss corporate loan book.

Our tax expense in the quarter was $293 million, representing an effective rate of 20%, helped by NCL's performance and the initial positive effects of completed legal entity mergers. In the second half of 2024, excluding the effects of any DTA revaluation, we expect the effective tax rate to be around 35%, mainly as expected pretax losses in legacy Credit Suisse entities can't be fully offset against profits elsewhere in the group. The tax rate could benefit if NCL continues to perform better than expected. We continue to expect the ongoing optimization of our legal entity structure to gradually support a return to a normalized tax rate of around 23% by 2026.

Turning to our quarterly cost update on Slide 7. Exiting the second quarter, we achieved an additional $900 million in gross cost saves when compared to three months earlier, bringing the cumulative total since the end of 2022 to $6 billion or around 45% of our total gross cost saves ambition. We estimate that around half of these cost saves benefit our underlying OpEx with the other half reinvested as planned in our technology estate as well as to offset increases in variable and financial adviser compensation tied to production. To date, we've generated around $4 billion of net saves, primarily driven by NCL, which has shed around $3.5 billion of its 2022 cost baseline.

Following the legacy entity mergers, we now turn our focus to the critical client account and platform migration work planned for our core businesses. We started in the fourth quarter with GWM's booking hubs in Hong Kong, Singapore and Luxembourg, followed thereafter by client account transitions in our Swiss booking center, which supports both GWM and P&C. Along with our ongoing cost rundown efforts in noncore and legacy, these initiatives represent the most material drivers of future cost savings as we decommission technology systems, hardware and data centers, while also unlocking further staff capacity.

As I highlighted last quarter, the pace of saves is expected to moderately decelerate from the quarterly run rates observed over the last several quarters, while we prepare for and initially undertake these significant integration activities. We expect to pick up the pace as we implement these transitions throughout 2025 and into 2026, particularly benefiting the cost income ratios of GWM and P&C. The rate at which we are incurring integration-related expenses, which front-run underlying OpEx saves is also indicative of the headway we're making on costs.

In the second half, we expect to book $2.3 billion of integration-related expenses of which $1.1 billion in the third quarter. By the end of this year, we expect to have incurred around 70% of total cost to achieve our 2026 exit rate efficiency targets.

Moving to our balance sheet. In the second quarter, we reduced risk-weighted assets by a further $15 billion, of which $8 billion from the active rundown of positions in our noncore and legacy portfolio, which I will come back to shortly. Over $8 billion of the decline we've seen across the core business divisions, mainly resulting from the financial resource optimization work in GWM and P&C. As I highlighted earlier in the year, this work is addressing sub-hurdle returns on capital deployed, including by reducing deposit and loan volumes.

The upshot is additional capacity to absorb headwinds from regulatory and risk methodology changes, model harmonization between the two banks and the implementation of Basel III final, now confirmed for January 2025. While we continue active dialogue with our supervisor on various aspects of the final rules, at present, we continue to expect the day 1 impact of Basel III final to be around 5% of RWA, driven mainly by FRTB. We'll update our estimates by no later than the fourth quarter as requirements firm.

Our leverage ratio denominator decreased by $35 billion in the quarter. This reduction was driven by several factors, including full repayment of the Central Bank ELA facility granted to Credit Suisse, lower lending volumes mainly from our financial resource optimization efforts and the active rundown of our NCL portfolio. We ended the second quarter with an LCR of 212%, reflecting the LOE payment and TLAC of $198 billion.

Turning to Slide 9. Our CET1 capital ratio as of quarter end was 14.9%. The numerator reflects accruals of this year's expected dividend and a reserve for 2024 share repurchases, of which we have executed $467 million of the planned $1 billion as of last Friday. Additionally, our CET1 capital includes all relevant portions of the purchase price allocation adjustments made to Credit Suisse's equity as of the acquisition paid last June. With the 12-month measurement period now concluded, total PPA adjustments against the purchased equity of Credit Suisse amounted to negative $26.5 billion of which about 70% reduced CET1 capital.

Following completion of the parent bank merger earlier in the quarter, next week, we'll report UBS AG's consolidated and standalone capital ratios and other information for the first time on a combined basis. UBS AG's standalone CET1 capital ratio at quarter end is expected at 13.5% on a fully applied basis. To put this capital ratio in perspective, it's important to compare the way we manage our parent bank capital versus Credit Suisse's pre-acquisition practices.

We provide for the complete transition of the risk-weight rule changes applicable to UBS AG subsidiary investments, which overall are valued prudently. Moreover, we don't depend on any affiliate valuation concession from the regulator. This was not the case with Credit Suisse before the takeover where its approach overstated the parent bank's resilience and ultimately limited restructuring optionality. In this context, our merged parent bank already provides for around $20 billion of additional capital resulting from the acquisition, including the progressive add-ons from growth in balance sheet and market share that will be phased in over five years starting in 2026. The result is a parent bank capital buffer of around 100 basis points above the current fully applied requirement by 2030.

Moving to our business divisions and starting with Global Wealth Management on Slide 10. GWM's pretax profit was $1.2 billion on revenues of $5.8 billion, which were up 3% year-over-year on an estimated combined basis. Against the complex economic backdrop, clients sought our differentiated advice and solutions as evidenced by continued strong momentum in net new asset inflows and transactional activity. Overall, we generated $27 billion of net new assets, a growth rate of 2.7%, with positive inflows across all regions. I'm particularly pleased with this result, considering the variety of headwinds to net new asset growth that the business successfully navigated in the quarter, including around $6 billion in seasonal tax outflows in the U.S.

Let me unpack this further. To date, we've retained the vast majority of Credit Suisse's invested assets, notwithstanding that more than 40% of Credit Suisse's wealth advisers have left since October 2022. I would also note that these relationship managers advised on only 20% of assets, meaning that, overall, we've retained the more productive Credit Suisse advisers, a testament to the appeal of our platform. We've also kept around 80% of the first large wave of maturing fixed-term deposits from last year's win-back campaign with the peak in maturities expected in the third quarter.

Furthermore, we made strong progress this quarter in our efforts to increase profitability on sub hurdle relationships. Higher returns come from both driving increased platform revenue and proactively exiting subpar loans. With these actions in the quarter boosting the revenue over RWA margin by around 30 basis points sequentially. Lastly, from a macro standpoint, the equity capital markets, and in particular, IPO activity, ordinarily a significant driver of wealth creation and net new asset generation have only recently started to recover. These dynamics underscore the basis of our short-term annual guidance of $100 billion for 2024 and 2025, and equally, the resilience of our net new asset achievement in the quarter as well as the high level of client conviction in our advice and solutions.

Now on to the details of GWM's financial performance. Revenues declined 2% sequentially as lower NII and the expected sequential drop in transactional activity were partially offset by growth in recurring net fee income, supported by higher average levels of fee-generating assets. Net interest income decreased by 2% sequentially to $1.6 billion, driven by ongoing deposit mix shifts and declining loan volumes, partly offset by our repricing actions, which as mentioned, support higher returns on capital and net interest margin.

Looking towards year-end, we maintain our previous guidance that full-year 2024 NII will be roughly flat versus 4Q '23 annualized. This includes a low to mid-single-digit percentage sequential drop in the third quarter driven by a decrease in volumes, mix shifts in anticipation of falling rates and the impact on our replication portfolios. In arriving at this outlook and in light of recent rates volatility, we're modeling 100 basis points of U.S. dollar policy rate reductions by the end of 2024.

The outlook for net interest income in our U.S. wealth business is expected to be influenced by competitive dynamics affecting the pricing of sweep deposits. By the middle of 4Q '24 we intend to adjust the sweep deposit rates in our U.S. Advisory accounts, which net of offsetting factors, are expected to reduce pretax profits by around $50 million annually.

Looking across our wealth business beyond year-end, we expect an inflection point in GWM net interest income around the time implied forwards reach a structural floor and stabilize, and clients begin to releverage driving loan balances and NII higher. Moreover, it's essential to consider that GWM's diversified and CIO-driven fee-generating business model has proven both its appeal to clients and ability to drive profitable growth even during past periods of low or negative interest rates. Consequently, in addition to increased lending, it's reasonable to expect that lower interest rates will spur increased transactional activity, mandate sales and investments in alternatives across our wealth business.

Recurring net fee income increased by 3% to $3.1 billion from higher client balances. Net sales in our UBS managed account offerings showed continued momentum, contributing to a sequentially higher recurring net fee margin in the quarter. Transaction-based revenues decreased quarter-on-quarter to $1.1 billion, but notably increased around 14% year-on-year on an estimated combined basis, with APAC up around 30% and the Americas up over 20% and broadly flat sequentially versus a strong first quarter. Both regions performed exceptionally well in structured products, as clients sought customized investment opportunities in an environment of low volatility, high interest rates and continued global tech appeal.

I would also highlight that our investments in combining GWM and IB markets and solutions capabilities in the Americas are paying off, as evidenced by our transactional revenue performance over the first half of the year, up around 20% versus the same period in 2023. Expenses were roughly flat quarter-on-quarter. Excluding compensation-related effects, underlying operating expenses dropped 2% sequentially. As highlighted earlier, the upcoming client account migration work is expected to be a significant driver of cost reductions in GWM throughout 2025 and into 2026.

Turning to Personal & Corporate Banking on Slide 11. P&C delivered a second quarter pretax profit of CHF 645 million. Revenues were down 4% sequentially driven by an 8% decline in net interest income that was partly offset with increases in recurring net fees and transaction-based revenues. P&C's NII in the quarter was primarily affected by higher liquidity costs, and the SMB's 25 basis point interest rate cut from March as we kept our Swiss clients deposit pricing unchanged.

In the third quarter, we expect NII to tick down sequentially by a low single-digit percentage, mainly due to the effects of the SMB's second 25 basis point rate cut from late June. In U.S. dollar terms, we expect NII to be roughly flat sequentially. Despite these effects as well as higher costs related to the SMB's move earlier in the quarter to raise minimum reserve requirements, we nevertheless reaffirm our full-year 2024 guidance of mid- to high single-digit percentage decline versus 4Q '23 annualized, supported by our balance sheet actions. In arriving at this outlook, we are currently pricing in up to two further Swiss Franc policy rate reductions of 25 basis points each by the end of 2024.

Assuming Swiss franc interest rates stabilize next year as the forward rate curve presently implies, we expect shortly thereafter to see steady volumes and an inflection point in P&C's net interest income. We also expect by then that our balance sheet optimization work will be largely complete, with loan pricing reflecting a more appropriate cost of risk across the Swiss credit book. These efforts are necessary to restore returns on capital deployed and net interest margin in our Swiss business to pre-acquisition levels.

In this respect, we saw net new lending outflows of CHF 3.4 billion this quarter, driven by repricing of sub-hurdle volumes despite having renewed or granted new loans to our Swiss clients of around CHF 30 billion in 2Q. Transaction based revenues were up 2%, mainly from higher credit card usage. Recurring net fee income gained 3% on higher custody assets. Together, these non-NII revenue lines, up 2%, demonstrate the business' effectiveness in staying close to clients and minimizing merger dissynergies.

Credit loss expense was CHF 92 million, driven by a small number of positions in our corporate loan book, as I mentioned earlier. Even with the increased focus on risk-based pricing for maturing loan positions, our Swiss credit portfolio remains a very high quality with an impaired loan ratio of 1.1%, down sequentially, albeit up versus pre-Credit Suisse acquisition levels. For the foreseeable future, we expect CLE to remain at broadly similar levels given increased book size post-merger, the relative strength of the Swiss Franc and some economic softness in the main Swiss export markets.

Operating expenses were flat sequentially. Similar to GWM, future cost reductions in P&C will be closely tied to the client account and platform migration work for booking center Switzerland, planned to commence by the second quarter of 2025.

On Slide 12, pretax profit in Asset Management increased 26% to $228 million. This quarter's results included a gain of $28 million from the initial portion of the sale of our Brazilian real estate fund management business. In the third quarter, we expect to record an additional $60 million in underlying pretax profit on gains from disposals, mainly from closing the residual portions of this transaction. Net new money was negative $12 billion, with continued client demand for our SMA offering in the U.S. and positive contribution from our China JVs, only partly compensating outflows across asset classes, particularly equities.

While our integration efforts to consolidate platforms may constrain AM's net new money performance over the next few quarters, we expect our enhanced global reach and increased scale in alternatives and indexing to at least partially offset these headwinds. Net management fees dropped 5% as outflows in select active products weighed on margins.

Performance fees were roughly stable in the quarter. During 2Q, AM made strong progress in improving operational efficiency, a key focus area I highlighted during the investor update earlier this year. Operating expenses were 9% lower sequentially on reductions across both non-personnel and personnel costs, partially supported by lower variable compensation. Some of the sequential decline in variable comp is expected to normalize in the third quarter.

On to our Investment Bank's performance on Slide 13, which as in prior quarters, I compare on a year-over-year basis. The IB delivered a strong second quarter results with improving capital markets activity supporting an excellent banking quarter. Our markets businesses performed well in an environment reflecting mixed market trends, in particular low volatility in equities, rates and FX, as well as lower cash equity volumes in APAC where we are overweight. Operating profit was $412 million, up from an operating loss of $14 million a year earlier and up 2% sequentially as the Investment Banking backdrop continues to improve.

Investments to deepen our U.S. presence are having a positive impact on revenues as our contributions of Credit Suisse talent across key sectors of banking and markets. Underlying revenues grew by 26% to $2.5 billion, with nearly two-thirds of the increase coming from the Americas. I would highlight that our revenue growth was achieved with broadly similar levels of RWA as the IB continues to manage within the group RWA limit of 25%, excluding NCL. Banking revenues were up 55% as we outperformed global fee pools, both in capital markets and advisory.

Since the end of 2023, we have gained over one percentage point in market share in each of our strategic banking initiatives, including M&A and sponsors in the Americas. Regionally, APAC saw revenues nearly doubled, while the U.S. was up 83%. EMEA declined by 3% against a very strong prior period. Capital markets revenues were up 82% year-over-year with an outstanding LCM performance reflecting an increase in refinancing activity, mainly in the U.S.

Advisory revenues increased by 23% as we leveraged our strong position in APAC to benefit from increased activity and performed well in the Americas. The strength of our fully integrated coverage teams is visible in our ability to win new mandates, where we ranked seventh globally in announced M&A volumes, making for an encouraging deal pipeline. While we expect to continue capturing market share, macro and geopolitical factors are likely to weigh on continued sequential banking revenue growth in the near term.

Revenues in Global Markets reached $1.8 billion, the best second quarter results in over a decade, up 18% year-on-year and driven by the Americas up nearly 40%. Equities revenues were up 17%, driven by both derivatives and cash, where we have seen material gains in market share. FRC was up 20% with broad increases across FX, credit and rates, benefiting from higher client activity, particularly in FX and rates options, partially offset by lower activity and spread compression that affected our rates flow business. Operating expenses rose 12%, predominantly reflecting higher variable compensation linked to improved performance.

Moving to Slide 14. Noncore and legacy's pretax loss in the quarter was $80 million, supported by around $400 million in revenues, principally from gains on physician exits across corporate credit and securitized products and further reductions in the NCL cost base. Underlying OpEx was down 37% sequentially, helped by releases in litigation reserves of $172 million. Excluding litigation, operating expenses declined by 17% as we made strong progress driving down personnel costs and third-party spend.

NCLs six-month pretax profit of $117 million, which far exceeds earlier loss expectations, demonstrates the business' skillful management in derisking its portfolios and rapidly cutting its costs. For the second half of the year, we expect an underlying pretax loss of around $1 billion, reflecting moderate short-term upside to revenues and continued sequential progress on cost reduction, albeit at a slower rate than observed over recent quarters.

Moving to Slide 15. Over the last four quarters, NCL has made impressive progress running down its costs across all lines, cutting its underlying operating expense base by over $2 billion or around 50%. NCL has also excelled in running down its balance sheet positions, significantly contributing to group capital efficiency, releasing $5 billion in capital as a result of its efforts. Additionally, NCL has cut its non-operational risk-weighted assets by almost 60% over the last year, including by another $8 billion this quarter mainly from actively exiting positions across its portfolios, notably in investment grade and high-yield corporate credit, securitized products and macro.

Similarly, NCL's LRD is down by over 60%, since 2Q '23 dropping another $40 billion of leverage exposure this quarter, reflecting lower notionals as well as lower levels of HQLA. In terms of book closures, NCL shuttered another 10% of its active books in the quarter, bringing the total since last June to around 45%. Looking ahead, the progress we're making is visible in the natural roll-off profile, significantly narrowing the gap to our active rundown expectation of around 5% of group RWA by 2026.

Further supporting this and as additional evidence of NCL's proficiency in de-risking its balance sheet and driving down costs, yesterday, we agreed to sell Credit Suisse's U.S. Mortgage Servicing business. This transaction is expected to close in 1Q '25 and would reduce RWA by around $1.3 billion, LRD by around $1.7 billion and annualized costs by around $250 million.

To summarize, the second quarter demonstrated the power, scale, and secular growth potential of our franchise as we delivered strong underlying profitability and continued to make substantial progress across our integration agenda, while reinforcing a balance sheet for all seasons.

With that, let's open for questions.

Question-and-Answer Session

Operator

We will now begin the question-and-answer session for analysts and investors. [Operator Instructions]. The first question is from Giulia Aurora Miotto from Morgan Stanley. Please go ahead.

Giulia Miotto

Hi, good morning. Thank you for taking my questions. I'll ask two, please. So my first one, thank you very much for the guidance on NII in GWM, which was something that the market was looking forward to. Can I just ask a clarification? If you look at the current forward curve, when do you expect NII to bottom exactly? Do you think second half '24 and then we can grow? Or possibly first half '25? So that's the first question.

And then the second question is instead on the capital of the parent. In particular, the CSI, it seems to have a lot of excess capital and upstream impact could reduce the impact -- the potential impact from the proposal in Switzerland. Can we expect UBS to upstream some of that capital? Or how are you thinking about excess capital at the subsidiaries? Thank you.

Todd Tuckner

So regarding the NII guidance, in terms of the implied forward curve, as I mentioned, we ended up pricing in, as you saw modeled for 25 basis point rate cuts through the end of the year. If you look out in terms of when the implied forward curve would suggest bottoming out, probably pricing in more like 7 million, depending on what you're looking at. So I mean, from here. While difficult to speculate, it could be sometime in mid-2025. But I spent time on what I think is really important to recognize is that in a lower NII -- lower interest rate environment, there are significant offsets and tailwinds in the business that we expect to see. And that was a point that we wanted to really ensure is well understood. Because ultimately, transaction revenues, re-leveraging and driving up NII from re-leveraging and also recurring fees from mandate sales all have upside in an environment of lower interest rates.

In terms of the parent bank capital, you mentioned our U.K. Credit Suisse's U.K. subsidiary that has excess capital. Of course, we're working on restructuring on all of our subsidiaries where we can. And ultimately, we will, as appropriate upstream the capital in any of the subsidiaries in order to alleviate the capital at the parent bank.

Giulia Miotto

Thank you.

Operator

The next question is from Andrew Coombs from Citi. Please go ahead.

Andrew Coombs

Good morning. I'd like to just drill down two of the areas where you perhaps delivered ahead of expectations. So firstly, on the non-core, another successful quarter of actively reducing the RWAs, some further gains on some of those position exits. You're now talking about narrowing that gap to the natural runoff. So based on the natural runoff, you'd be at 6%, you're aiming for 5%. So I think that is only another $5 billion implied of active RWA management in that business. And as you alluded to, the close of the U.S. mortgage servicing business will get you some way towards that. Should we assume that the active management within the NCL book is now largely complete or will be largely complete by the end of this year?

And then my second question is just on costs. Previously, I think you expected to be at 50% by end '24. You're now at 55%, guiding by end '24 of the total cost save target. There's an extra $500 million of cost saves that you've realized earlier than expected. Which division is it you view those cost saves are coming through earlier than expected? And in your mind, it's purely just the timing issue, that you commented earlier, as opposed for quantum issue that you're delivering more cost saves than expected? Thank you.

Todd Tuckner

Yes. Thanks a lot, Andrew. So on the second one, in terms of on the cost and the performance and outperformance we're continuing to see, I mean, that's really driven, as I highlighted in my comments, by NCL for sure. NCL has driven the lion's share of the gross cost saves to date. While the other divisions have contributed, it has been really a function of their active rundown of positions, but also the restructuring of various parts of Credit Suisse's GSIB that we've highlighted in the past is an important part of taking out costs, and a lot of those costs reside in NCL.

So they've been really the benefactor of the cost performance. And as we look out towards the end of the year, the additional progress that we anticipate even though, as I suggest, we expect a bit moderate deceleration in the gross cost saves, that's expected to be yielded also by NCL. And as I highlighted, the core business divisions will then -- the ratio of core to non-core, or non-core to core in terms of cost takeout will invert as we get into the second half of the integration agenda, and we'll start to see the significant cost reductions hitting through, in particular, GWM and P&C.

And then -- and just on the first in terms of how we see the natural runoff and the success we've had in the quarter. Of course, we're not counting on extrapolating and we take economic decisions as they arise and the opportunities arise. So difficult to extrapolate the great outcome that we've had to date to suggest a different outcome than the natural roll off. And that's why we continue to disclose it. So that becomes clear.

What is important, and Sergio commented this in his remarks, that the uncertainty delta continues to narrow. And that's what I think is important that, ultimately, while we can't count on anything in particular in terms of what can come off the balance sheet of NCL in terms of extrapolation. What we can say is that the uncertainty delta has narrowed very significantly.

Andrew Coombs

That's clear. Thank you. I guess the follow-on would be just your previous guidance, which for a typical run rate of close to zero revenues from NCL per quarter, and presumably that's unchanged?

Todd Tuckner

Yes. As I said, Andrew, that we see in the long-term, that's for sure the case. In the short term, i.e., the 2H guidance that I offered, we see some modest upside to current book values on the revenue side. So some modest uptake in driving the $1 billion underlying PBT loss guidance that I offered in my comments.

Andrew Coombs

Thank you.

Operator

The next question is from Jeremy Sigee from BNP Paribas. Please go ahead.

Jeremy Sigee

Hi, there. Thank you. Two questions, please. First one just follows on from just exactly what you were talking, about the guidance for the P&L drag from NCL. Obviously, it's going better than expected, which is great to see. What would we expect now? Previously, you were talking about $2 billion P&L drag exit rate in 2025, and then $1 billion exiting 2026. And obviously, it's going much better than that with sort of a $1 billion drag in the second half that you're integrating. What should we expect for 2025 and could the NCL drag be finished within 2025 rather than carrying on into 2026? Any update on that would be really helpful.

And then my second question, just a more sort of specific one on Investment Banking costs. They drifted up a little bit more than revenues in the second quarter. It's not a big move, but the cost/income deteriorated against those strong revenues rather than perhaps you might have hoped it could have improved a little bit. So any comments on the drivers, whether there's any one-offs in there or anything unusual. Just how we should interpret that IB cost number, please.

Todd Tuckner

So, Jeremy, thanks. On the second one, in the comp on IB cost, it's -- the comp quarter, of course, only has Credit Suisse personnel in for a short period of time, just the one month when you look at the year-on-year comp, whereas the current quarter has the people we've added for the full quarter, so that's driving that variance.

Jeremy Sigee

Sorry, I'm speaking Q-on-Q I think the costs are up 3% and the revenues are up 1%. So I was thinking more Q-on-Q?

Todd Tuckner

Yes, on Q-on-Q, it would be just some compensation-related effects that we're hitting through driving the Q-on-Q. But I'd have to go back and look at that. But really, it's more the year-on-year that we've focused on. On the -- in terms of the guidance on the P&L drag in NCL, in terms of what we should expect, look, I mean we're really pleased with the performance we've had to date. As I said in my last comments. There's no way to extrapolate from it, it's a straight line and to assume that that's the pace of which will continue. So our guidance remains. That's where, in terms of the P&L drag at the end of '26 is right now still our best estimate. When we come back and talk about an outlook in the fourth quarter going forward, potentially, we update that and see where we are. But for now, that's our best estimate in terms of where we land.

Jeremy Sigee

Understood. Thank you very much.

Operator

The next question is from Kian Abouhossein from JPMorgan. Please go ahead.

Kian Abouhossein

Yes, thanks for taking my questions. The first one is related to Wealth Management. First of all, thanks again, Todd, for the disclosure. I hope some of the U.S. peers are listening, as this was very helpful relative what I heard before from U.S. peers. Sweep deposits last disclosure was $35.7 billion. I was wondering where we are roughly right now in the U.S. entity. If you could also share with us the Advisory part of that, so we can kind of understand the year adjustment factor, and what rate you are paying now versus what rate you will be paying for the sweep deposits on these Advisory mandates? And in that context, if you could briefly talk about lending, which was down ex-U.S., just to understand how much of that is related to adjustments of your offering to the CS clients versus actual losses in lending.

And then the second question is on legal entity on Page 19, it's a very useful chart. And we talk about further legal entity simplification in the U.S. as well as the U.K. legal entity going into a branch. I was wondering what capital relief you expect from that? Or maybe even in subjective terms, if you can talk a little bit about the changes that will happen, when you describe it to you on the page.

Todd Tuckner

Thanks, Kian, for the question. So on -- in terms of the second one, first the simplification that we talk about is continuing in the U.K. and U.S., but also another parts of the world to continue merging subsidiaries out of existence to create and unlock more capital funding and tax efficiencies. So that's what we're getting too. So we're working all through that. We just, of course, did the big parent bank and Swiss bank mergers. We reparent to the IHC, but now there is still a lot of work that will continue to unlock these benefits. So in terms of capital relief naturally to the extent that and this goes a little bit to the question that was asked earlier in terms of the repatriation of excess capital, say, in a subsidiary. Of course, that is part of the analysis that we go through as we work through it. But it's -- there are contingencies to the timeline in terms of what triggers and what the timing could be to merge some of these entities out of existence.

In terms of GWM, so what I could say on the sweep deposits. First of all, Advisory is about a third of the total that we have in sweeps. So just to give -- to dimension that a bit, is I think that's probably useful to understand. And then as far as the pricing goes, of course, the way we're -- first of all, it's a function of interest rates, because I mentioned we're going to introduce the new rates in advisory in the fourth quarter, because we have to change systems and go through some transitional work to get there. So we have to see also where interest rates are, so in terms of an absolute price that I can offer. But what I can say is that we will, for sure price in the value of the insurance coverage we offer on deposits that benefit from multiple programs, multiple bank programs and reciprocal programs that we've invested in, and that will feature into the price of the rate we ultimately offer.

In terms of lending balances, ex U.S., the main driver of that, I mean clearly, we've seen deleveraging in a higher interest rate market for outside the U.S., particularly in APAC, for several quarters running. We're looking forward and seeing some signs of tapering there, but we continue to see that. As I highlighted, as rates come down, we do expect that that should taper and then start to see clients re-leverage. But so the rate environment is driving some of that, but the other part of it, perhaps the more significant driver is the financial resource optimization work we're doing that a consequence of that is that loans will roll off on our platform, which is one of the points I highlighted in connection with the net new asset report.

Kian Abouhossein

And Todd, just on sweep, I know that Morgan Stanley has confirmed 2% rate to be paid. Should we look at similar rates? And could you just also remind us of where we are on the sweep volumes at the moment? Last number we saw was 35.7 billion.

Todd Tuckner

Yes. What I could say, Kian, is that the number has come in a little bit, it's driven -- is in also some of the comments I made on mix is driving the 2Q results. So you could assume that number has come a little bit lower. And all I could say, get anything further on the rate is, as mentioned, competitive dynamics will ultimately feature in how we ultimately settle on a price for the sweep deposits. So as I said, I gave some views on considerations that we will factor in. But as far as an absolute price, that's not at this point something that we have settled on.

Kian Abouhossein

Thanks.

Operator

The next question is from Anke Reingen from RBC. Please go ahead.

Anke Reingen

Yes, thank you very much for taking my questions. The first one is just on the Basel IV impact on -- of the $25 billion on the 1st of January '25. I guess you said you will give us a bit more detail potentially before year-end. But I mean, you previously talked about a $15 billion net of yes, non-core run down, do you have a -- can you give us a better indication of how the $25 billion will actually look on the 1st of January 2025? And then sorry, coming back on the NII guidance. Just confirming the P&C reiterating of guidance that's on the U.S. dollar basis rather than Swiss franc. And just conceptually, I mean, I see -- I mean, you now assume more rate cuts than before, but the guidance is reiterated. Can you just maybe highlight what the missing pieces that allows you to reiterate guidance? Thank you very much.

Todd Tuckner

Thanks, Anke. So on Basel III final as mentioned, we still expect $25 billion impact is 5% of risk-weighted assets, so in that range. As you mentioned, we guided in the fourth quarter in our investor update that $15 billion is in the core, $10 billion is in non-core. I think for now, that split remains pretty robust in terms of how we're thinking -- how we're seeing it, and actually we'll continue to work down the NCL portfolio to make that impact lessened over time.

In terms of the NII guidance for P&C, just to -- you asked for clarity on -- it is in Swiss francs, so we're guiding in Swiss francs. We'll offer both in the future to sort of help. As I mentioned, in 3Q, we see a low single-digit down in Swissy, but flat sequentially in USD. And as I mentioned, I think that's a good outcome that we've had a number of headwinds that we've been working through sort of reaffirm the guidance for the full-year is also a function of some management actions that have been taken, including some loan repricing actions that have helped. So those are the drivers of the NII guidance for P&C.

Anke Reingen

Sorry, just to follow-up. So on the 1st of January '25, so the '25 -- I mean, the 5% increase in RWA? Or should it be lower, because some litigation NCL rundown has already kicked in or reduced the impact?

Todd Tuckner

The estimate is on the same basis we gave it in 4Q in terms of the impact, because it's mainly FRDB-driven. So for now, assume the guidance remains. And as I said, if we have an update before we go live with it, of course, we'll come back and provide it.

Anke Reingen

Okay. Thank you very much.

Operator

The next question is from Chris Hallam from Goldman Sachs. Please go ahead.

Chris Hallam

Yes, good morning and thanks for taking my questions. So first, you've guided for banking to generate almost twice the baseline revenues by 2026, assuming supportive markets. So obviously, performance was very strong in the second quarter, but then we had this period of elevated volatility at the start of August. Has that changed anything in terms of how close we are now to supportive markets? And how would you expect the recovery to progress through the second half of this year?

And then second question just on profitability. At the start of the year, you said you'd expect to get to around 45% of the $13 billion gross savings by the end of '24, and you've got there by the end of the first half. And you also guided for a mid-single digit underlying return on core CET1 for this year, mid to high for next year. Consensus is at 6% for this year, 9% for next year. But in the first half, you're already above 9%. So how should we be thinking now about the path for underlying return on core CET1 through 2024 and 2025?

Sergio Ermotti

Thank you, Chris. I'll take the first question. So look, I think of course the market environment is volatile and there are elements of fragility that we see. But what is most important for us is to look through the short-term market dynamics. And I can tell you that I'm very confident that we are building up a very compelling pipeline in terms of mandate that we win, still not announced and things that can be then executed in a normalized market environment. So of course, if we see the kind of volatility we had in a couple of weeks ago, that would not be very helpful for the pipeline. But in general, I stay -- I would say that positive that in respect of our momentum. So a good pipeline and good momentum in winning mandates, but of course, it will also depend on market conditions.

Todd Tuckner

And Chris, on the second. In terms of a return on core CET1 and how it relates to our guidance. So as you mentioned, we initially guided it mid or mid-single digits for '24, mid-to-high for '25. So naturally, if there's an update, we'll bring it to you when we talk about our '25 expectations later this year. In terms of where we are, as Sergio highlighted in his comments, the first six months, we generated an underlying return on CET1 of 9.2%. So obviously, we're comfortably ahead of the target of mid for 2024.

Operator

The next question is from Amit Goel from Mediobanca. Please go ahead.

Amit Goel

Hi, thank you. Thanks for taking my questions. So one, just a follow-up, just to make sure I also heard some of the previous guidance correctly. I think you mentioned the cost of the reprice from sweep to be about $50 million annually. So I mean, I guess, given the one-third advisory disclosure, that would imply only just over 40 bps of incremental cost on that portion and effectively nothing on the rest. So I was just kind of curious, I mean, in a way that you could continue to see outflows, so I'm wondering what the capacity is for the group to replace that funding at similar costs.

And then also just linked to that, if I look then at the total sweep and the cost of sweep, it seems like that the earnings are pretty similar to what Wealth Management Americas generate. So I'm just kind of curious how you think about Wealth Management America's profitability? And with some of these headwinds, how you think you'll get back to that mid-teens operating margin.

And then secondly, just curious on the parent. Is there any scope to shift exposure from foreign participations to domestic in addition to capital repatriation and whether that can be reflected in participation values, if there is potentially rule change coming? Thank you.

Todd Tuckner

Thanks, Amit. Yes, in terms of the second one, shifting exposure domestically, whether that helps, it's way too early to speculate on how we're going to address and what actions we take. We don't know what the standards are. So -- and where they'll move -- where the standards will move, assuming they move. And so to speculate about what mitigating actions might be available to us is way too early.

In terms of sweeps, yes, I disclosed that the impact on pretax profit is expected to be around $50 million annualized in U.S. Wealth business. I did say that that's net of offsetting factors. So that includes an array of banking initiatives and expense programs across various categories. So there -- I wouldn't take the $50 million as gross income. But actually, as I said, it is a net impact.

And I think, look, I saw interesting that you asked the question and then lead to how we're going to address the pretax margin issues. We -- nothing has changed on that. We're focused on that. We know what we have to do. The sweep deposit issue is a modest hit on that, of course, because it's something we're saying is adverse to PBT. We think it's manageable, and now we're getting on with the work of improving the margins on the basis of how we've described that in the past. So we know we have to do there, and we're taking steps to achieve that.

Operator

The next question is from Benjamin Goy from Deutsche Bank. Please go ahead.

Benjamin Goy

Hi, good morning. I have two questions, please. So the first one on GWM, in particular America, where the cost/income ratio remains above 90%. It was better during low interest rate times. So just wondering with the mix shift from NII and falling more towards most likely, as you see upside to year-end '26 cost/income ratio improvement target? And then secondly, on the capital side, you obviously as the group guidance of 14% CET1, but you see the 12.5% more final constrained. And that's the first half of the question.

The second is with Switzerland being essentially only geography, introducing FRTB and not delaying, do you think that's the final piece of the hurdle in terms of higher capital requirements for you? Thank you.

Sergio Ermotti

Let me take the second part of the question. Of course, the 14% guidance we have right now stays as it is. The 12.5% you mentioned look through fully applied 2030 current requirements. We will see exactly how things develop in the next few quarters in terms of future requirements. From an FRTB standpoint of view, of course, as you mentioned, Switzerland will introduce that on January 1st. It will be short term, a competitive disadvantage. We don't believe -- we believe is manageable short term. Of course, if this -- should other jurisdictions not converge, not to converge to Basel III full implementation over the next couple of years. Then, of course, that would be a little bit more problematic, and we would need to think about how to address this matter. So we remain confident that we will be able to have a level playing field in how we operate and compete globally, but it remains to be seen.

Todd Tuckner

And Benjamin, here's how we think about the -- your cost/income ratio question for GWM, where we have a look through cost/income ratio presently of around 80%. Naturally, when we planned the $13 billion of gross cost saves and the less than 70% cost/income ratio, GWM factors in quite prominently in that piece of work. And that's why I've highlighted that the cost/income ratio will be benefited by the work that's just going to get going in the next quarter or two, which is the client account migration work and platform consolidation starting in APAC and parts of Europe before the Swiss booking center. That will drive significant cost down, and ultimately, which is why I believe that Wealth and P&C will benefit significantly in the latter half of the integration work. So in terms of where we get our cost/income ratio, it will GWM's cost/income ratio in the end will be a big contributor to the group meeting its target of less than 70% by the end of 2026.

Benjamin Goy

Thanks. This was, in particular, on the Americas, the GWM Americas where you probably won't see much of a cost save benefits. But correct me if I'm wrong.

Todd Tuckner

Question was on the Americas. Sorry, I didn't...

Benjamin Goy

Yes. Indeed, from the 90% right now more towards the 85% was it can accelerate with the different revenue mix?

Todd Tuckner

No, look as I said also to the -- before, and I've said previously, we're working towards a mid-teens profit margin over the next couple of years. That's where we know we have to narrow the gap where we are, that's where we are working towards. And that also features into the less than 70% cost/income ratio by the end of '26 getting to that level. So nothing that I've guided to today has changed any of that. We're very focused on taking the steps to achieve that by that -- in that time frame.

Benjamin Goy

Thank you.

Operator

The next question is from Tom Hallett from KBW. Please go ahead.

Tom Hallett

Hi, thank you for taking my questions. I'm just curious what do you assume in terms of loan and deposit growth in the Swiss business NII guide and GWM guide in the second half of the year? And then secondly, how do you see deposit mix shift and deposit betas evolving within that guide as well?

Todd Tuckner

Yes. Thanks, Tom. So in terms of volumes in each of the businesses, I expect loans in both of the businesses through the end of 2024 to come slightly in largely because of the balance sheet work that I highlighted in my comments. So I think, in both cases, loans would come in. I see deposits as well through on the GWM side as well towards the end of the year, I mean, roughly flat at this point. I see P&C growing deposits, whether through the rest of this year, but certainly as we look out over the longer term. So I would say a little bit of downward pressure in terms of loans in large part, just given the balance sheet work that we're doing.

On the deposit side, I see more sort of flat to growing in the near to midterm in terms of the balance sheet. In terms of deposit mix shifts, look, I think in the end, where we've been seeing, as many banks have, the effects of deposit mix and cash sorting and rotation for some period of time. As rates start to come down, we expect that the cash sorting will continue to taper and will be less of an impact in terms of the NII. And that's a little bit of what we're seeing. And our outlook is, just given the fact that we expect our modeling rates coming in, that we are seeing sort of in a way the last vestige of mix shifts as while rates remain a bit higher. So that's how we see the deposit mix shift is evolving.

Tom Hallett

Thank you.

Sergio Ermotti

Okay. There are no more questions. Thank you all for calling in and your questions. And see you in end of October for the Q3 results. Thank you.

Operator

Ladies and gentlemen, the webcast and Q&A session for analysts and investors is over. You may disconnect your lines. We will now take a short break and continue with media Q&A session at 10:45 CET.

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