Italian Banks

Views on "Leave" vote consequences – ISP looks oversold

Equities

Italy
Banks, Ex-S&L

Ignacio Cerezo
Analyst
ignacio.cerezo@ubs.com
+44-20-7568 4409

Francesco Di Giambattista
Analyst
francesco.di-giambattista@ubs.com
+44-20-7568 1070

Small exports do not necessarily make for small impacts

While exports to the UK only account for c5% of total Italian exports, the impact on Italian banks from the "Leave" vote will not necessarily be as small, in our view. We see high uncertainty and volatility affecting banks' ability to grow loans and AUM business already in the short term, while weaker asset quality and lower rates offer additional downside potential depending on the medium-term economic outlook.

Volatility and uncertainty to prove an immediate drag on earnings…

Since our initiation we have been cautious about fee prospects due to difficult market conditions, and the recent bout of volatility is set to exert further pressure on this revenue line. Additionally, the uncertainty that will likely follow the vote could present a difficult environment for loan growth, thus affecting NI, with a strong TLTRO 2 take-up offering a partial offset. Recent widening of BTP-Bund spreads could affect CET1 FL ratios in 2Q through the AFS reserve. We cut our 2016-18E adjusted EPS forecasts by c9% on average for ISP and by c17% for UCI. On the back of lower earnings and not feeling comfortable with a dividend payout above 100%, we cut our 2017E dividend for ISP to €3.5bn (96% payout) from €4.0bn, leaving 2016E unchanged at €3bn.

…asset quality and monetary policy reaction the main downside risks

While implications for the European and Italian economy are still unclear, a deterioration in the outlook could present two risks for Italian banks. The first is a further reduction in interest rates which would have an immediate impact on the mostly-floating balance sheets of Italian banks. The second is asset quality failing to improve thus preventing the reduction of provisions, the main driver of Italian banks' profitability improvement.

PTs cut on lower earnings and higher COE, bur still see value in Intesa

To reflect heightened risks on earnings we increase our COE assumption for both banks by 1pp (to 11% for ISP and 12% for UCI). This combined with earning cuts lead us to revise down our PT for ISP to €2.15 from €2.75 and for UCI to €2.10 from €3.20. We continue to see value in ISP (Buy) especially given the valuation protection it offers at 0.66x P/TBV 2017E and its 13% 2017E dividend yield. UCI, while discounting to a large extent a sizable capital increase, does not offer an attractive risk-reward in our opinion, given lack of clarity on strategy and additional dilution downside risk on further share price declines.

Figure 1: Changes to 2016-17E EPS and target prices

		New EPS		% Change		Target Price		Share Price
€	Rating	2016E	2017E	2016E	2017E	New	Old	
ISP	Buy	0.16	0.21	-11%	-9%	2.15	2.75	1.62
UCI	Neutral	0.28	0.35	-16%	-19%	2.10	3.20	1.88

Source: UBS estimates. Note: share price as of 28 June 2016.

UBS Research THESIS MAP

MOST FAVORED: **Intesa Sanpaolo**

LEAST FAVORED: **UniCredit**

PIVOTAL QUESTIONS

Q: What does the "Leave" vote mean for the fundamentals of Italian banks?
We see mostly three impacts on earnings coming from increased uncertainty and volatility. 1) Placement fees will likely suffer from lower AUM sales, impacted by reduced risk appetite, while management and performance fees will be affected by negative market performance. 2) Loan growth is likely to be lower than previously expected due to a more uncertain economic outlook. This will impact NII, although the strong take-up in the recent TLTRO 2 auction should somewhat offset this. 3) Wider BTP-Bund spread could affect 2Q CET1 ratios FL through the AFS reserve.

Q: What are the main medium-term risks from the "Leave" vote for Italian banks?
We expect risks to the European and Italian economic recovery to pose challenges for the Italian banks. 1) Interest rates could fall further as the ECB exhausts other options to support the economy following a negative impact from the "Leave" vote. 2) Asset quality could fail to improve thus preventing the reduction of provisions, the main driver of Italian banks' profitability improvement.

WHAT'S PRICED IN?

Intesa already pricing in to a large extent the medium-term risks of the "Leave" vote: At 0.66x P/TBV 2017E Intesa shares look to be pricing in to a large extent a reduction of NII due to lower rates and a lack of improvement in provisions. We estimate that UniCredit, at 0.26x P/TBV 2017E, prices in to a large extent a sizable capital increase but not fully the medium-term risks on NII and provisions.

UBS VIEW

Still see value in Intesa, also given valuation protection: While the "Leave" vote has rebased down earnings expectations and medium-term uncertainty is significant, the strong market reaction on Intesa has left the shares trading at 0.66x P/TBV17E thus benefitting from sizeable valuation protection. We are more cautious on UniCredit as, in our view, it does not offer an attractive risk-reward given lack of clarity on strategy and additional dilution downside risk on any further share price decline.

EVIDENCE

Sensitivity to lower rates and lack of asset quality improvement: Regarding potential risks, we have explored the impact for both Intesa and UniCredit from lower rates analysing their balance sheet structure. Moreover we have stressed the profitability of these banks for a lack of improvement of provisions. We have then used these scenarios to determine what is reflected by the current valuations.

Implication and risks from the "Leave" vote for Italian banks

Implications

- **Fees** impacted by lower risk appetite and negative market performance
- **Loan growth** likely to slow on heightened uncertainty
- Wider BTP-Bund spread to affect **capital** through AFS reserve

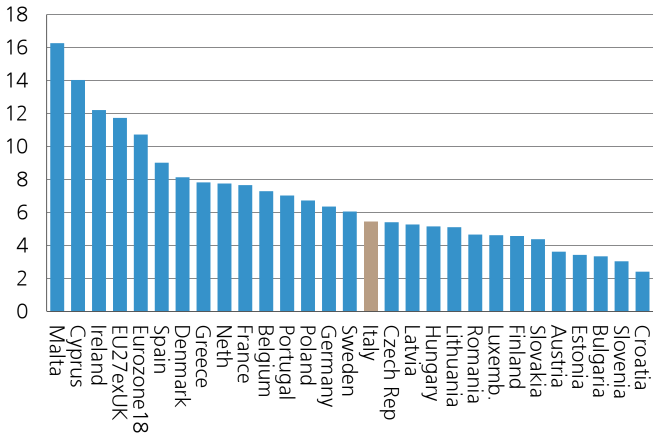
Risks

- **Further fall of interest rates** as ECB exhausts other measures to support European economy
- **Asset quality fails to improve** removing the main driver of improvement of Italian banks' profitability

What does the "Leave" vote mean for earnings?

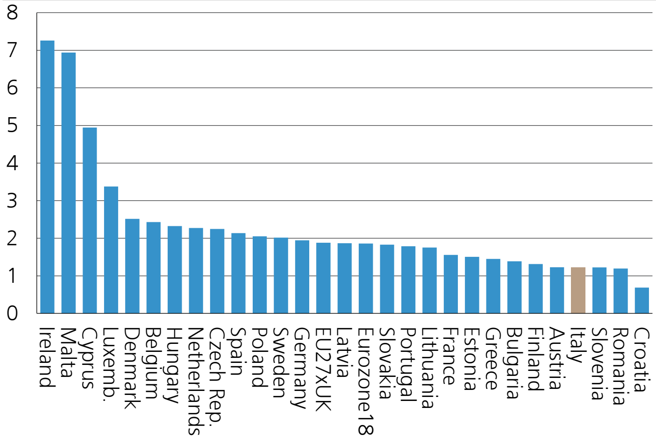
Italy as a country has a relatively limited direct exposure to the UK economy through exports, as Figure 2 and Figure 3 below illustrate (UBS European Economics: "It's 'Leave' - Implications for UK, Europe & markets"). So one could expect that the direct impact on the Italian economy should be limited but second-order impacts remain a key uncertainty. For this reason we do not include in our forecasts any impact due to the deterioration of asset quality or due to potential ECB monetary policy reactions. However we explore these scenarios in the next section.

Figure 2: Final (i.e. direct and indirect) goods and services exports to the UK, % of total final exports, 2011



Source: OECD Trade in Value Added (TiVA) database, UBS.

Figure 3: Final (i.e. direct and indirect) goods and services exports to the UK, % of total value added, 2011



Source: OECD Trade in Value Added (TiVA) database, UBS.

What we do reflect in our estimates now is a likely deterioration in the operating environment for Italian banks mostly due to increased uncertainty, heightened volatility and negative market performance. In particular we identify three areas in which these effects will be observable, in our view:

(1) **Fees**: volatility and negative market performance are likely to have further reduced risk appetite, which in turn should be reflected in subdued AUM flows. Moreover we think that performance fees are unlikely to be meaningful this year.

(2) **NII**: economic uncertainty is likely to lead to a more modest loan growth than what we previously expected and this will affect NII. Somewhat offsetting this will be the strong pick-up of Italian banks in the recent TLTRO 2 auction, which is likely to further compress cost of funding.

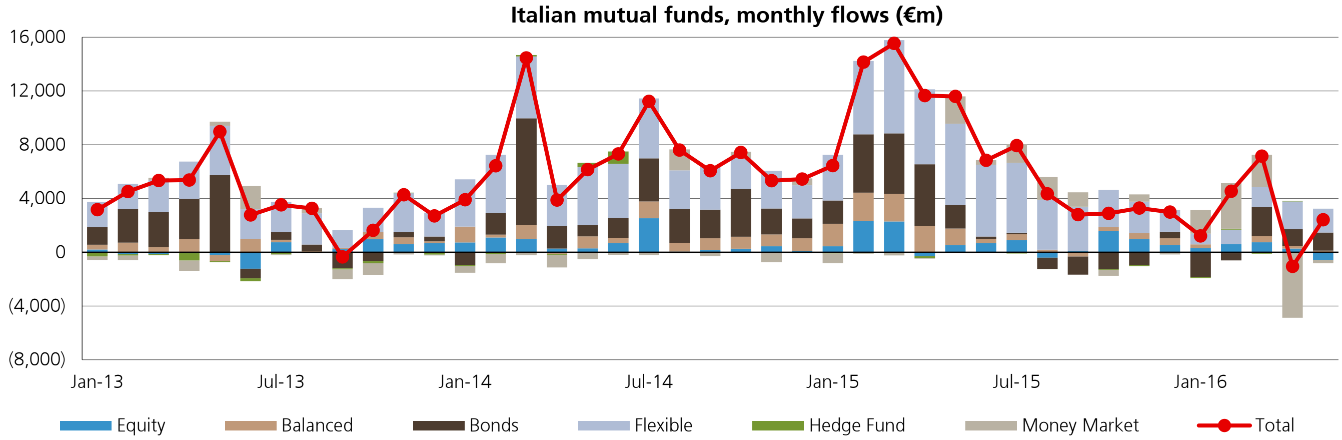
(3) **Capital**: the BTP-Bund spread widened following the outcome of the referendum. This is likely to negatively impact the AFS reserve of Italian banks, and therefore also their CET1 fully loaded, at least in 2Q16.

In this note we change our estimates in relation to (1) and (2) while leaving (3) mostly unchanged given the high volatility that is likely to persist, making it difficult to have a firm view on the AFS reserve.

Fees

In our initiation report (March 2016) we extensively reviewed why the Italian "fees story" was expected to run out of steam, a scenario that largely materialised over 1Q16. The beginning of 2Q16 in terms of mutual funds flows, for the data available so far, has not shown the rebound that was expected by the market despite the improved market conditions versus 1Q16. This plays, in our view, to our thesis of a structural plateauing of the AUM business of Italian banks.

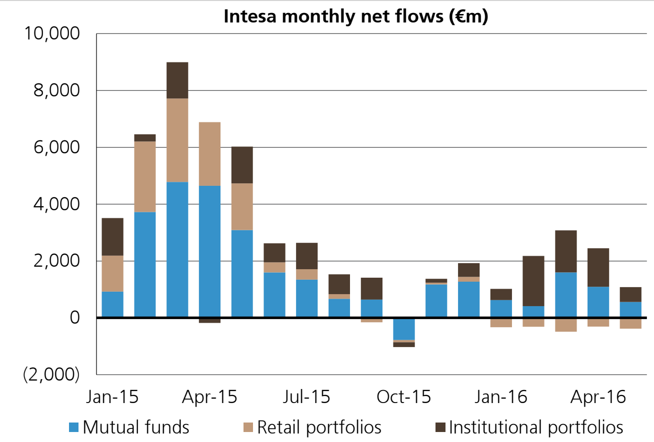
Figure 4: Flows into mutual funds remained subdued also in April and May



Source: Assogestioni and UBS

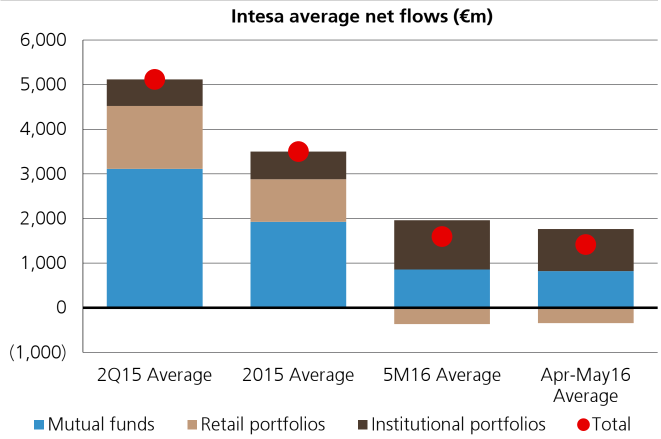
Looking at Intesa, its net flows, similarly to the system, have failed to rebound significantly so far and were mostly supported by institutional portfolios, likely related to unit-linked or hybrid insurance policies.

Figure 5: Intesa's mutual fund flows in May proved particularly weak…



Source: Assogestioni and UBS

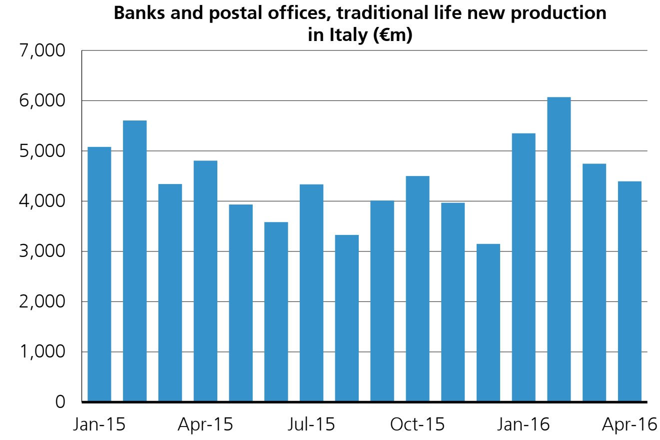
Figure 6: …and mostly supported by institutional portfolios, likely insurance related



Source: Assogestioni and UBS

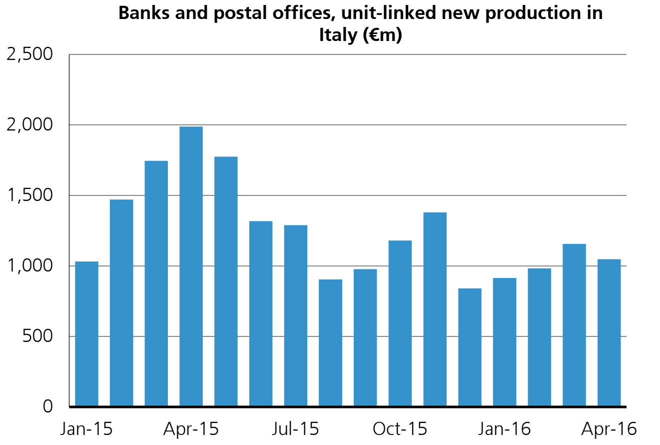
However, at system level, also insurance flows in April did not show a significant improvement versus 1Q16.

Figure 7: Traditional life business continued to be resilient in early 2Q16…



Source: ANIA and UBS

Figure 8: …while unit linked failed to pick up steam

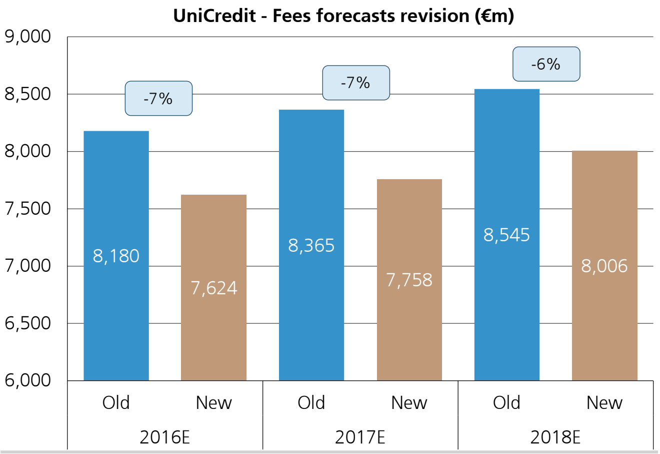


Source: ANIA and UBS

On this backdrop, the "Leave" vote and the volatility it generated are likely in our view to further reduce risk appetite of retail savers thus depressing new AUM flows (which generate upfront fees). At the same time negative market performance should affect the stock of AUM on which management fees are calculated and also reduce performance fees.

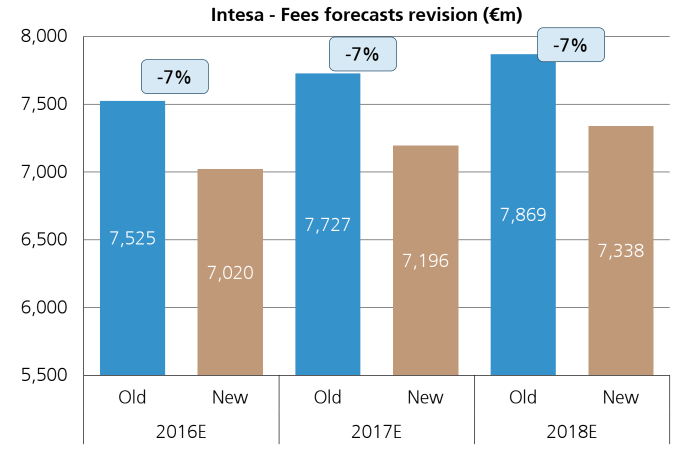
Taking these into consideration we have reduced our fees forecasts over 2016-18E by c7% on average for both UniCredit and Intesa.

Figure 9: UniCredit review of fees forecasts



Source: UBS estimates

Figure 10: Intesa review of fees forecasts



Source: UBS estimates

In detail, for Intesa we reduce by 17% placement fees this year on lower inflows which in turn lead to more pronounced cuts in portfolio management fees in 2017E and 2018E.

Figure 11: Intesa detailed fees estimates

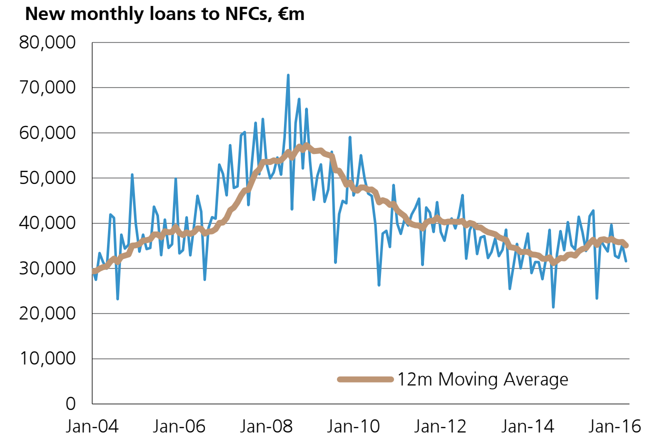
	2015	2016E			2017E			2018E		
€m		New	Old	%	New	Old	%	New	Old	%
Commercial banking activities	2,274	2,237	2,269	-1%	2,264	2,341	-3%	2,301	2,401	-4%
Dealing and placement of securities	*763*	*413*	*496*	*-17%*	*413*	*397*	*4%*	*413*	*357*	*16%*
Currency dealing	*44*	*45*	*45*	*0%*	*45*	*45*	*0%*	*45*	*45*	*0%*
Portfolio management	*2,112*	*1,975*	*2,190*	*-10%*	*2,014*	*2,331*	*-14%*	*2,104*	*2,434*	*-14%*
Distribution of insurance products	*1,232*	*1,369*	*1,424*	*-4%*	*1,439*	*1,512*	*-5%*	*1,412*	*1,519*	*-7%*
Other	*184*	*180*	*180*	*0%*	*171*	*171*	*0%*	*163*	*163*	*0%*
Management, dealing and consultancy	4,335	3,983	4,336	-8%	4,082	4,456	-8%	4,137	4,517	-8%
Other net fee and commission income	887	800	920	-13%	850	930	-9%	900	950	-5%
Net fee and commission income	7,496	7,020	7,525	-7%	7,196	7,727	-7%	7,338	7,869	-7%

Source: Company data and UBS estimates

Net interest income

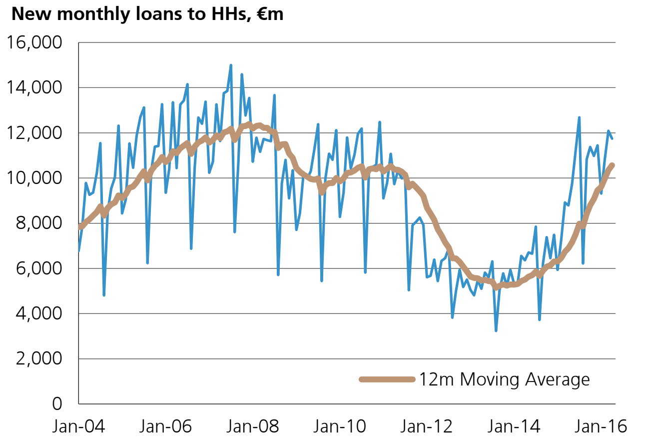
Several Italian banks have started to see preliminary signs of loans growth during 1Q16 supported by strong new production in the households space, while the corporate space remained more subdued. Before the referendum we were cautiously optimistic on the possibility of having some loan growth in the year due to improving macro conditions and the relatively unlevered nature of the private sector in the country (unlike Spain, where a buoyant recovery failed to spur loan growth).

Figure 12: New business with NFCs has stabilised after few months of modest recovery….



Source: Bank of Italy and UBS

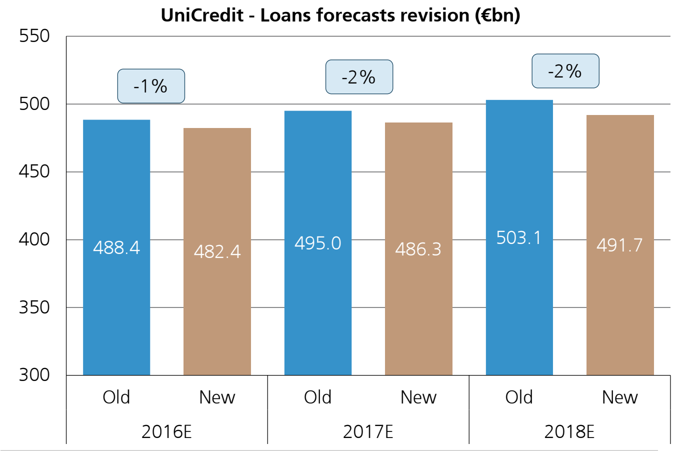
Figure 13: …while new business with HH has been growing fast and is at levels seen before the EZ crisis



Source: Bank of Italy and UBS

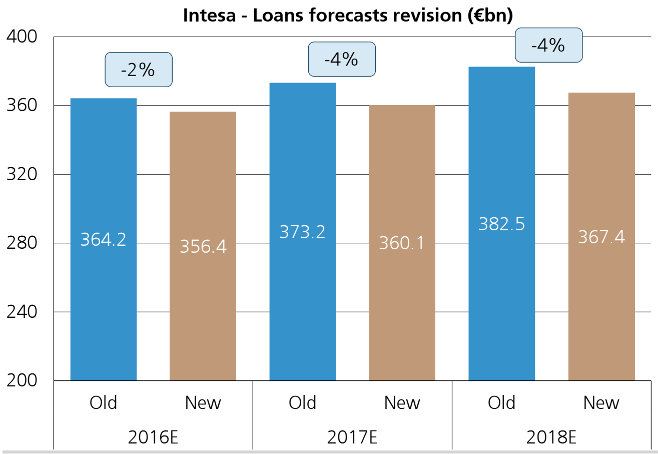
However, we now change our view on loan growth turning more conservative given the likely prolonged period of uncertainty that will follow the "Leave" vote and the negotiations between the UK and the EU. This environment should not prove supportive for long-term borrowing in our view, despite the persistently low interest rates. We reduce our loans forecast by -1% and -2% in 2016E for UniCredit (where we leave unchanged CEE) and Intesa respectively.

Figure 14: UniCredit review of loans forecasts



Source: UBS estimates

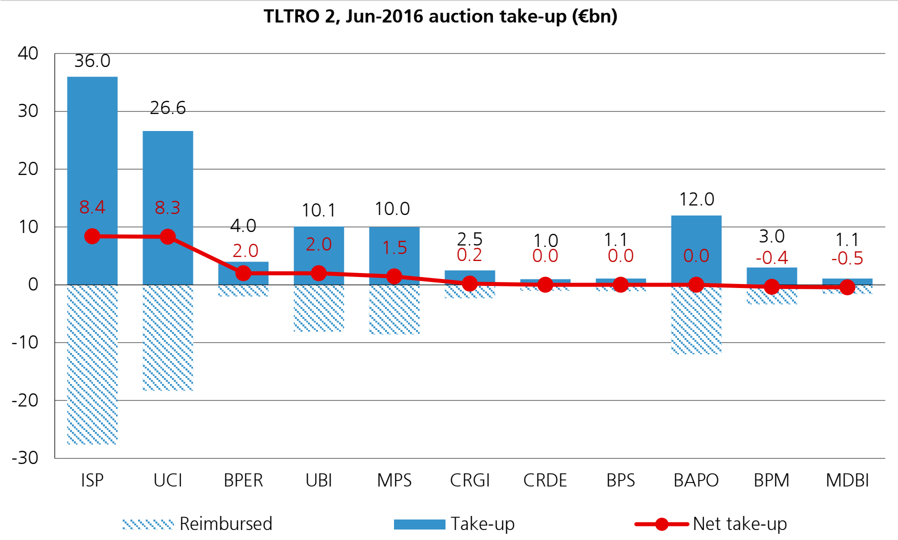
Figure 15: Intesa review of loans forecasts



Source: UBS estimates

However, at the same time as the referendum results the first auction of TLTRO 2 took place, which saw strong participation from the Italian banks (Figure 16). This should be positive for cost of funding as, despite our estimates revision, we still expect loan growth to be sufficient to obtain the -40bps interest rate on these operations.

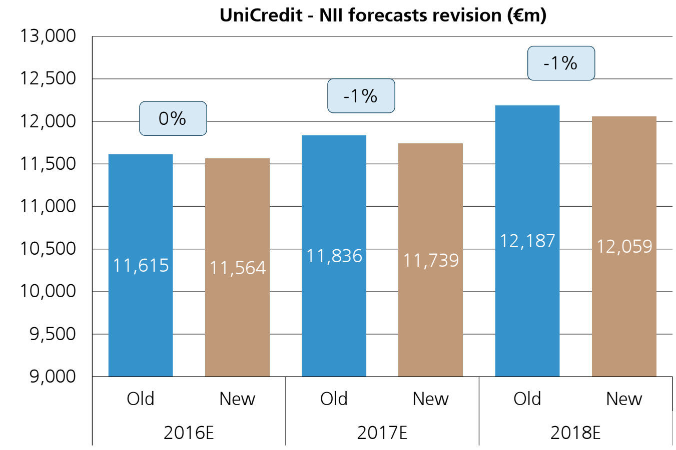
Figure 16: Italian banks took significant advantage of the first TLTRO 2 auction



Source: Reuters, Bloomberg, company data and UBS. Note: UniCredit data refer to Italy, Germany, Austria and CEE.

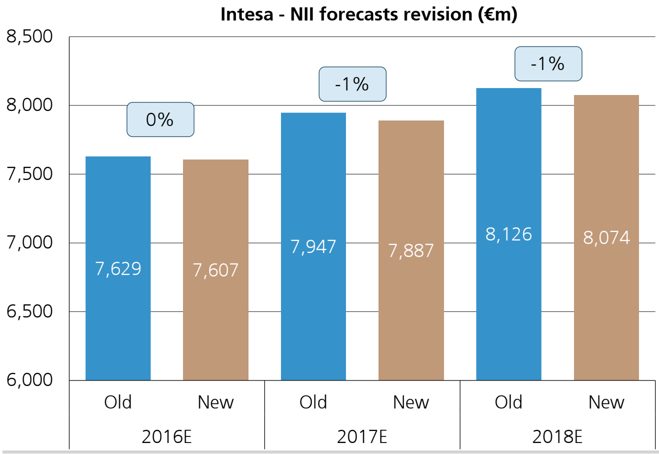
Combining the two factors above, we leave roughly unchanged our 2016E NII forecast while reducing 2017-18E by c1% for both banks.

Figure 17: UniCredit review of NII forecasts



Source: UBS estimates

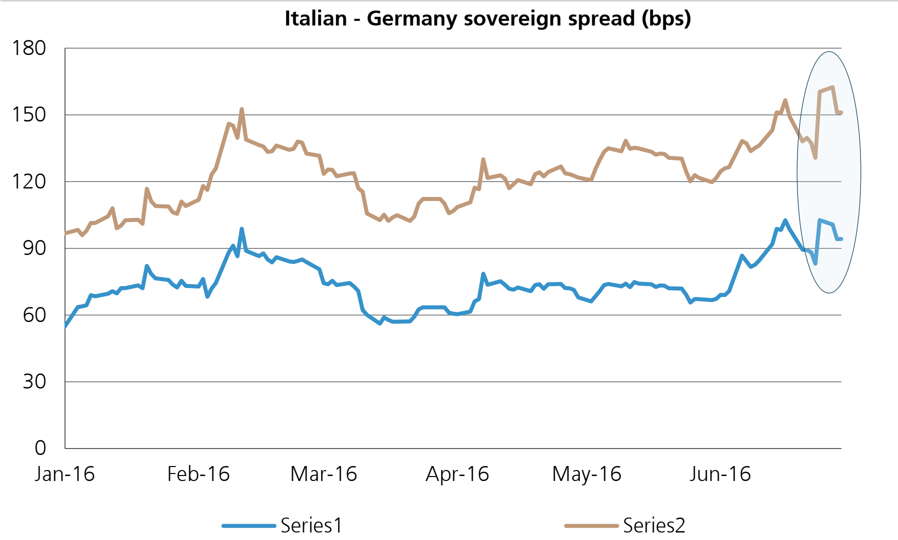
Figure 18: Intesa review of NII forecasts



Source: UBS estimates

Potential upside to NII could come from a higher BTP-Bund spread (Figure 19) as it would allow Italian banks to reduce the loss of yield from the roll-over of their bond portfolios. Clearly, the flip-side of the coin is the reduction of the AFS reserve which will also affect CET1 ratios fully loaded.

Figure 19: The BTP-Bund spread remains wider compared with before the vote results



Source: Bloomberg and UBS

Estimates changes

Intesa

In addition to the changes explained in the previous pages we also add to our figures the impact from the recently announced Visa Europe disposal (c€150m net capital gain). Overall we reduce our adjusted net income forecasts by -11%, -9% and -8% for 2016E, 2017E and 2018E respectively.

Given the lower expected profitability of the bank we also review our dividend expectations. **We now expect the bank to pay in 2017E (and onward) a €3.5bn dividend, down from the €4.0bn targeted by the bank that we expected previously. Our 2016E dividend remains unchanged at €3.0bn.**

Figure 20: Intesa detailed estimates review

	2016E			2017E			2018E		
€m	New	Old	%	New	Old	%	New	Old	%
Net interest income	7,607	7,629	0%	7,887	7,947	-1%	8,074	8,126	-1%
Profits of equity-accounted investees	120	120	0%	100	100	0%	120	120	0%
Net fee and commission income	7,020	7,525	-7%	7,196	7,727	-7%	7,338	7,869	-7%
Trading Income	700	700	0%	919	919	0%	965	965	0%
Income from insurance business	1,017	1,017	0%	1,037	1,037	0%	1,058	1,058	0%
Other net operating income/expense	-200	-125	60%	-200	-125	60%	-200	-125	60%
Gross income	**16,264**	**16,866**	**-4%**	**16,939**	**17,605**	**-4%**	**17,355**	**18,012**	**-4%**
Staff costs	-5,255	-5,398	-3%	-5,332	-5,482	-3%	-5,410	-5,568	-3%
Other administrative expenses	-2,675	-2,675	0%	-2,648	-2,648	0%	-2,623	-2,623	0%
Depreciation and amortisation	-735	-735	0%	-758	-758	0%	-783	-783	0%
Total expenses	**-8,665**	**-8,808**	**-2%**	**-8,738**	**-8,888**	**-2%**	**-8,817**	**-8,974**	**-2%**
Pre-impairment income	**7,600**	**8,058**	**-6%**	**8,202**	**8,717**	**-6%**	**8,538**	**9,038**	**-6%**
Net provisions for risks and charges	-150	-150	0%	-120	-120	0%	-100	-100	0%
Net impairment losses on loans	-2,915	-2,915	0%	-2,267	-2,279	-1%	-2,079	-2,100	-1%
Net impairment losses on other assets	-125	-125	0%	-80	-80	0%	-70	-70	0%
Profits (Losses) on investments	1,521	1,302	17%	0	0	-	0	0	-
Profit/(loss) before tax	**5,930**	**6,169**	**-4%**	**5,735**	**6,238**	**-8%**	**6,289**	**6,768**	**-7%**
Income tax	-1,868	-1,943	-4%	-1,835	-1,996	-8%	-2,013	-2,166	-7%
Charges for integration and exit incentives	-65	-65	0%	-50	-50	0%	-50	-50	0%
Effect of purchase price allocation (net of tax)	-104	-104	0%	-89	-89	0%	-74	-74	0%
Goodwill Impairment	0	0	-	0	0	-	0	0	-
Profit/(loss) from disc.operations	-30	-30	0%	-60	-60	0%	-60	-60	0%
Minority interests	-89	-93	-4%	-69	-75	-8%	-75	-81	-7%
Net attributable income	**3,774**	**3,934**	**-4%**	**3,632**	**3,968**	**-8%**	**4,017**	**4,337**	**-7%**
Extraordinary items (post tax)	-1,045	-895	17%	0	0	-	0	0	-
AT1 coupons (post tax)	-107	-107	0%	-160	-160	0%	-215	-215	0%
Adjusted net profit	**2,623**	**2,933**	**-11%**	**3,472**	**3,808**	**-9%**	**3,803**	**4,122**	**-8%**

Source: UBS estimates

UniCredit

For UniCredit we factor in the changes previously discussed leaving all other lines unchanged. This results in adjusted net income cuts of -16%, -19% and -15% for 2016E, 2017E and 2018E respectively.

Figure 21: UniCredit detailed estimates review

	2016E			2017E			2018E		
€m	New	Old	%	New	Old	%	New	Old	%
Net interest income	11,564	11,615	0%	11,739	11,836	-1%	12,059	12,187	-1%
Dividends and similar income	856	856	0%	869	869	0%	882	882	0%
Net fee and commission income	7,624	8,180	-7%	7,758	8,365	-7%	8,006	8,545	-6%
Trading Income	1,347	1,347	0%	1,260	1,416	-11%	1,279	1,437	-11%
Other net operating income/expense	216	216	0%	199	199	0%	202	202	0%
Gross income	**21,607**	**22,214**	**-3%**	**21,825**	**22,685**	**-4%**	**22,428**	**23,253**	**-4%**
Staff costs	-8,155	-8,193	0%	-8,047	-8,088	0%	-7,954	-7,996	-1%
Other administrative expenses	-4,969	-4,988	0%	-4,768	-4,789	0%	-4,636	-4,658	0%
Recovery of expenses	838	839	0%	843	844	0%	849	850	0%
Depreciation and amortisation	-960	-961	0%	-976	-977	0%	-993	-994	0%
Total expenses	**-13,246**	**-13,304**	**0%**	**-12,949**	**-13,010**	**0%**	**-12,733**	**-12,798**	**-1%**
Pre-impairment income	**8,362**	**8,910**	**-6%**	**8,877**	**9,675**	**-8%**	**9,694**	**10,455**	**-7%**
Net impairment losses on loans	-3,555	-3,556	0%	-3,202	-3,215	0%	-2,948	-2,970	-1%
Other Charges & Provisions	-1,393	-1,393	0%	-1,414	-1,414	0%	-1,435	-1,435	0%
Integration costs	-449	-449	0%	-43	-43	0%	-44	-44	0%
Net income from investments	-33	-33	0%	8	8	0%	8	8	0%
Profit/(loss) before tax	**2,932**	**3,479**	**-16%**	**4,226**	**5,012**	**-16%**	**5,276**	**6,015**	**-12%**
Income tax	-842	-1,008	-16%	-1,246	-1,469	-15%	-1,589	-1,783	-11%
Profit/(loss) from disc.operations	15	15	0%	0	0	-	0	0	-
Purchase Price Allocation effect	-113	-113	0%	-93	-93	0%	-73	-73	0%
Goodwill Impairment	0	0	-	0	0	-	0	0	-
Minority interests	-352	-342	3%	-363	-354	3%	-392	-382	3%
Net attributable income	**1,640**	**2,031**	**-19%**	**2,523**	**3,097**	**-19%**	**3,222**	**3,778**	**-15%**
Extraordinary items (post tax)	320	261	23%	30	-32	-195%	31	-35	-188%
AT1 coupons (post tax)	-246	-246	0%	-380	-384	-1%	-512	-522	-2%
Adjusted net profit	**1,714**	**2,046**	**-16%**	**2,173**	**2,680**	**-19%**	**2,741**	**3,222**	**-15%**

Source: UBS estimates

What are the main risks from the "Leave" vote?

Additional risks for Italian banks are expected to come from the impact that the "Leave" vote will have on the European and Italian economies. In particular we see two key risks:

(1) **Further fall in interest rates**: the ECB will likely try to explore other alternatives before cutting rates further should there be a need to provide additional support to the European economy. Nevertheless, if those measures prove ineffective, rate cuts cannot be excluded and that would have detrimental effects on Italian banks' NII.

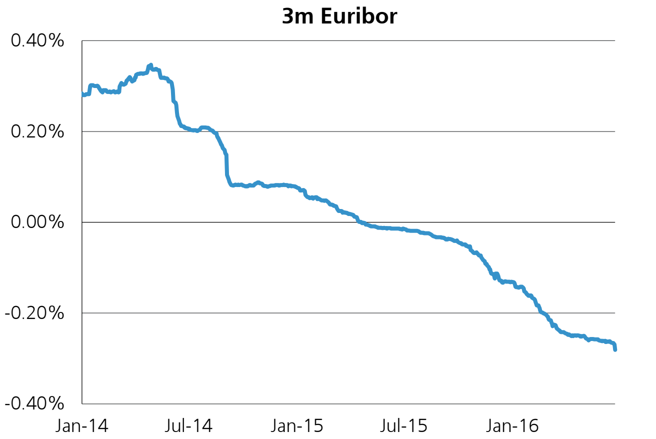
(2) **Asset quality fails to improve**: a reduction in provisions is the key driver of the expected improvement in Italian banks' profitability. Should asset quality fail to improve (e.g. continued or increased flows of new NPLs) provisions would remain sustained and, in a more severe scenario, loss recognition might have to be accelerated.

Further fall in interest rates

Euribor has been declining steadily with hardly any pause over recent years. However the pace of decrease slowed significantly during 2Q16 (Figure 22), leading to expectations that the impact from base rates was already felt for the largest part by Italian banks (which typically have a very frequent rate reset on their assets).

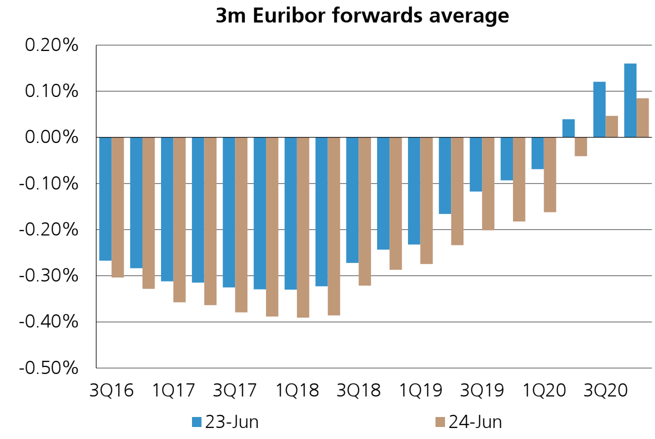
However, following the outcome of the referendum, expectations for a further reduction in Euribor have strengthened (Figure 23). This was likely due to market participants pricing in a higher likelihood of additional ECB actions to support the European economy.

Figure 22: Euribor slowed its decrease in recent months…



Source: Bloomberg

Figure 23: …but forwards decreased following the vote



Source: Bloomberg and UBS

To get a sense of the possible impact of lower rates for UniCredit and Intesa we have performed a simple simulation (Figure 24) to a -50bps reduction to Euro short term rates. ISP looks more exposed than UCI as a percentage of NII (-13% vs -7%) while the impact on net income is similar (-19% vs -23%).

The analysis is by construction very simple, relies on multiple assumptions and has several shortcomings, including that it does not account for into understanding what the market is reflecting in the current valuations, as we will see in the next section.

Figure 24: Simulation of the impact of 50bps rates decrease for UniCredit and Intesa

	UniCredit (ex-CEE)			Intesa		
2017E, €m	Average volumes	% fixed rate	Impact on NII	Average volumes	% fixed rate	Impact on NII
Assets						
Loans	422,629	20%	-1,691	358,252	20%	-1,433
Bonds	154,130	10%	-694	78,685	10%	-354
Liabilities						
Bonds	111,082	0%	555	86,744	0%	434
Deposits	414,622	51%	1,018	266,859	76%	318
Impact on NII			**-811**			**-1,035**
% NII			-7%			-13%
% Net income (net of tax)			**-23%**			**-19%**

Source: UBS estimates. Note: % of volumes that are fixed rate is estimated. For deposits we use the % of deposits excluding term deposits and repos on total deposits at group level. For bonds we apply the same percentage of bonds and repos / total financial assets of 2015 to our 2017E forecast of total financial assets.

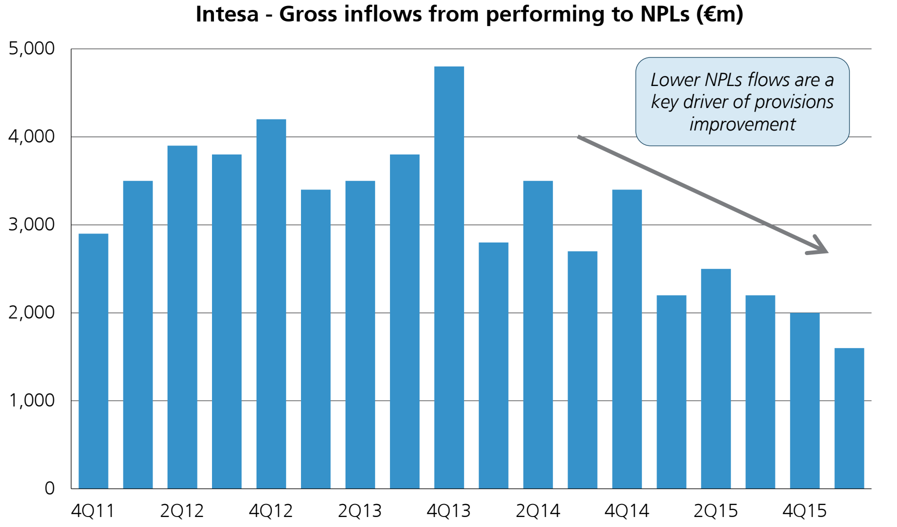
A potential additional risk linked to lower rates and lacklustre loan growth is that competition would likely increase considerably. This should mean that spreads too would come under pressure, effectively doubling the negative impact.

Asset quality fails to improve

The single most important driver of the improving profitability of Intesa and UniCredit (and of the Italian banking space in general) is the reduction in provisions, the first signs of which have been observed in recent quarters.

One of the drivers of this ongoing improvement is the incipient economic recovery which has led to a slowdown in the formation of new NPLs. A key risk from the "Leave" vote could be a deterioration in the economic environment in Europe and in Italy in particular, which could halt or reverse the asset quality improvement process.

Figure 25: Risks to the economic recovery in Italy could translate into risks to banks' profitability by a lack of improvement in provisions



Source: Company data and UBS

To gauge the potential downside risk from this kind of scenario we have assumed that cost of risk remains stable at 2016E level during 2017-18E. In 2017E for Intesa this means a 20bps higher cost of risk which translates into 110bps removed from ROTE.

Figure 26: Intesa would see its 2018E ROTE decrease by 130bps should provisions remain at the level we expect for 2016E

€m	2016E	2017E	2018E
Base case			
Provisions / average net loans (bps)	83	63	57
Provisions	-2,915	-2,267	-2,079
Net profit (reported)	3,774	3,632	4,017
Net profit (adjusted)	2,623	3,472	3,803
ROTE (adjusted)	6.5%	8.5%	9.2%
Downside			
Provisions / average net loans	83	83	83
Provisions	-2,915	-2,957	-3,002
Net profit (reported)	3,774	3,171	3,400
Net profit (adjusted)	2,623	3,011	3,186
ROTE (adjusted)	6.5%	7.4%	7.9%

Source: UBS estimates

For UniCredit in 2017E the lack of improvement adds 8bps to our cost of risk forecast and takes off c60bps of ROTE, on our estimates.

Figure 27: UniCredit would see its 2018E ROTE decrease by 100bps should provisions remain at the level we expect for 2016E

€m	2016E	2017E	2018E
Base case			
Provisions / average net loans (bps)	74	66	60
Provisions	-3,555	-3,202	-2,948
Net profit (reported)	1,640	2,523	3,222
Net profit (adjusted)	1,714	2,173	2,741
ROTE (adjusted)	4.0%	4.9%	5.9%
Downside			
Provisions / average net loans	74	74	74
Provisions	-3,555	-3,600	-3,635
Net profit (reported)	1,640	2,243	2,742
Net profit (adjusted)	1,714	1,893	2,261
ROTE (adjusted)	4.0%	4.3%	4.9%

Source: UBS estimates

Valuation

Higher COE reflects heightened uncertainties

While we do not include in our forecasts the risks described in the previous section we are also aware that these risks increased significantly with the "Leave" vote. To reflect this we increase our COE assumptions for both Intesa and UniCredit. Intesa goes from 10.0% to 11.0%, while UniCredit goes from 11.0% to 12.0%.

Intesa

On the back of lower earnings and higher cost of equity we reduce our price target for Intesa from €2.75 to €2.15.

Figure 28: Intesa detailed target price calculations

€m	2017E
Adjusted earnings	3,472
TBV	41,115
Capital (excess/)shortfall vs 11% "clean" CET1	-4,298
UBS adjusted TBV	36,817
Price target calculation (€)	
UBS adjusted TBVS (€)	2.19
UBS adjusted RoTBV (%)	9.5%
CoE (%)	11%
G rate (%)	0%
FV multiple	0.86
Fair TP (€)	1.90
Capital excess/(shortfall)	0.26
Fair TP (incl. capital excess/shortfall)	**2.15**
Cumulative cash dividends	0.21
Total shareholder return	**2.36**
% vs. share price	*45%*

Source: UBS estimates. Note: price as of 28 June 2016.

UniCredit

On the back of lower earnings and higher cost of equity we reduce our price target for UniCredit from €3.20 to €2.10. Our valuation methodology factors in a capital shortfall of c€5.2bn needed to get the bank at a 12.0% CET1 FL ratio "clean", i.e. excluding company pro-forma.

Figure 29: UniCredit detailed target price calculations

€m	2017E
Adjusted earnings	2,173
TBV	45,218
Capital (excess/)shortfall vs 12% "clean" CET1	5,256
UBS adjusted TBV	50,474
Price target calculation (€)	
UBS adjusted TBVS (€)	8.16
UBS adjusted RoTBV (%)	4.3%
CoE (%)	12%
G rate (%)	0%
FV multiple	0.36
Fair TP (€)	2.94
Capital excess/(shortfall)	-0.85
Fair TP (incl. capital excess/shortfall)	**2.10**
Cumulative cash dividends	0.14
Total shareholder return	**2.23**
% vs. share price	*19%*

Source: UBS estimates. Note: price as of 28 June 2016.

Downside valuation: lower rates and stable provisions

We test in the following pages what the scenarios described in the previous section, i.e. lower rates and stable provisions, would mean for the valuations of both banks. For UniCredit we also try to determine what different capital increase scenarios would mean for the shares.

Intesa

In the case of Intesa, applying both the negative scenarios described previously would imply a 6.3% adjusted ROTE in 2017E; the fair value (including dividends) would be €1.65, just 2% above the current share price.

Figure 30: Intesa detailed downside case calculations

€m	2017E Downside case
Adjusted earnings (Base case)	3,472
2017E cost of risk stable at 2016E level	-469
-50bps rate impact	-704
Adjusted earnings (Downside case)	**2,299**
TBV	39,942
Capital (excess/)shortfall vs 11% "clean" CET1	-3,125
UBS adjusted TBV	36,817
Price target calculation (€)	
UBS adjusted TBVS (€)	2.19
UBS adjusted RoTBV (%)	6.3%
CoE (%)	11%
G rate (%)	0%
FV multiple	0.57
Fair TP (€)	1.26
Capital excess/(shortfall)	0.19
Fair TP (incl. capital excess/shortfall)	**1.44**
Cumulative cash dividends	0.21
Total shareholder return	**1.65**
% vs. share price	*2%*

Source: UBS estimates. Note: price as of 28 June 2016.

UniCredit

In the case of UniCredit applying both the negative scenarios describe previously, the adjusted ROTE would drop to 2.6% in 2017E. This would lead the fair value (including dividends) down to €0.93, 50% below the current share price. The larger sensitivity of the valuation compared to Intesa is due to the lower starting profitability.

Figure 31: UniCredit detailed downside case calculations

€m	2017E Downside case
Adjusted earnings (Base case)	2,173
2017E cost of risk stable at 2016E level	-283
-50bps rate impact	-576
Adjusted earnings (Downside case)	**1,321**
TBV	44,359
Capital (excess/)shortfall vs 12% "clean" CET1	6,114
UBS adjusted TBV	50,474
Price target calculation (€)	
UBS adjusted TBVS (€)	8.17
UBS adjusted RoTBV (%)	2.6%
CoE (%)	12%
G rate (%)	0%
FV multiple	0.22
Fair TP (€)	1.78
Capital excess/(shortfall)	-0.99
Fair TP (incl. capital excess/shortfall)	**0.79**
Cumulative cash dividends	0.14
Total shareholder return	**0.93**
% vs. share price	*-50%*

Source: UBS estimates. Note: price as of 28 June 2016.

In Figure 32 we also explore how the fair value of UniCredit would change under several capital increase scenarios. The key assumption with this scenario analysis is that we assume that the capital increase would happen at the current market prices. Clearly the negative impact of dilution will increase for a lower market cap making the downside risk larger for lower share prices.

Figure 32: UniCredit – Scenario analysis of capital increases (€m)

Capital increase	**0**	**6,000**	**7,000**	**8,000**
New Market Cap	11,613	17,613	18,613	19,613
Dilution of earning	0%	34%	38%	41%
2017E TBV	45,218	51,218	52,218	53,218
2017E Earnings Adj.	2,173	2,173	2,173	2,173
2017E ROTE	**4.9%**	**4.3%**	**4.2%**	**4.1%**
P/TBV 17E	**26%**	**34%**	**36%**	**37%**
2017E CET1R	10.8%	12.3%	12.6%	12.8%
CET1 Target	12.0%	12.0%	12.0%	12.0%
2017E Capital shortfall/(excess)	5,256	-744	-1,744	-2,744
Adj 2017E TBV	50,474	50,474	50,474	50,474
Adj 2017E ROTE	4.3%	4.3%	4.3%	4.3%
COE	12.0%	12.0%	12.0%	12.0%
FV multiple	36%	36%	36%	36%
Fair value	18,182	18,182	18,182	18,182
Capital excess/(shortfall)	-5,256	744	1,744	2,744
Fair value (incl. excess/shortfall)	12,926	18,926	19,926	20,926
Cash dividends	883	883	883	883
Total shareholder return	13,809	19,809	20,809	21,809
Current value (exist. Shareholders)	11,613	11,613	11,613	11,613
Post cap increase at FV (exist. Shareholders)	13,809	13,061	12,983	12,913
Upside (%)	***19%***	***12%***	***12%***	***11%***

Source: UBS estimates. Note: all capital increases assumed to take place at current market prices. Price as of 28 June 2016.

Intesa SanPaolo
Oversold at these levels

Equities

Italy
Banks, Ex-S&L

12-month rating	**Buy**
12m price target	**€2.15**
	Prior: €2.75
Price	**€1.62**

RIC: ISP.MI **BBG:** ISP IM

Trading data and key metrics

52-wk range	€3.60-1.55
Market cap.	€27.2bn/US$30.1bn
Shares o/s	15,846m (ORD)
Free float	76%
Avg. daily volume ('000)	144,621
Avg. daily value (m)	€312.3
Common s/h equity (12/16E)	€47.8bn
P/BV (12/16E)	0.6x
Tier 1 ratio	14%

EPS (UBS, diluted) (€)

	From	To	% ch	Cons.
12/16E	0.17	0.16	-11	0.21
12/17E	0.23	0.21	-9	0.24
12/18E	0.25	0.23	-8	0.26

Ignacio Cerezo
Analyst
ignacio.cerezo@ubs.com
+44-20-7568 4409

Francesco Di Giambattista
Analyst
francesco.di-giambattista@ubs.com
+44-20-7568 1070

Resilient profile and already pricing in most of its key medium-term risks

Intesa has a resilient profile thanks to a solid capital position and best-in-class asset quality in Italy. Moreover we see returns well underpinned by structural efficiency and improving LLPs. We also find that the market is currently reflecting medium-term risks of lower rates and higher provisions, an approach we find too conservative. Despite dividends being likely to fall short of the original company guidance in 2017E, the bank continues to offer an attractive 13% 2017E dividend yield.

We cut 2016E-18E adjusted EPS by 9% on average, mostly on lower fees

We revise our adjusted EPS forecasts by -11%, -9% and -8% for 2016E, 17E and 18E respectively. These changes are driven by lower expectations on fees, on the back of a likely reduction in risk appetite and higher volatility, and lower NII, due to lower loan growth, only partly offset by the support to cost of funding from the recent TLTRO 2 auction pick-up.

Dividends to remain sizeable but 100% payout ratio should prove a constraint

Thanks to its strong capital position (CET1R FL: 13.1%) Intesa has been able to afford generous dividends in the recent years and we do not see this changing in the short/medium term. On the other hand, we do not think that at this stage the bank will be in a position to pay out more than 100% of its earnings, therefore on the back of our revised estimates, we also reduce our 2017E dividend to €3.5bn from €4.0bn previously (company target). Despite this cut the stock offers a 13% 2017E dividend yield. We leave our forecast of €3.0bn dividend for 2016E unchanged.

Valuation: recent price action offers sizeable valuation protection

On the back of lower earnings and higher cost of equity we reduce our price target for Intesa from €2.75 to €2.15. Intesa trades on c.0.66x PTBV17E and 7.8x PE17E. Our Gordon Growth price target is based on 9.5% adjusted ROTE17E, 11% COE (up from 10% previously), €4.3bn excess capital vs. 11% FLCET1 mark.

Highlights (€m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Revenues	16,248	16,828	17,149	16,264	16,939	17,355	17,619	17,954
Profit before tax	2,516	3,263	4,597	5,930	5,735	6,289	6,599	6,930
Net earnings (local GAAP)	(4,550)	1,251	2,739	3,774	3,632	4,017	4,239	4,475
Net earnings (UBS)	457	1,694	2,967	2,623	3,472	3,803	4,024	4,260
Tier 1 ratio %	12.2	13.1	12.9	13.9	14.1	14.3	14.2	14.2
EPS (UBS, diluted) (€)	0.03	0.10	0.18	0.16	0.21	0.23	0.24	0.25

Profitability/valuation	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
ROE (UBS) %	1.0	3.8	6.5	5.5	7.2	7.8	8.2	8.6
P/PPOP (diluted)	3.0	4.6	6.3	3.6	3.3	3.2	3.1	3.0
P/BV x	0.5	0.9	1.1	0.6	0.6	0.6	0.6	0.5
P/BV (UBS) x	0.7	1.0	1.3	0.7	0.7	0.7	0.6	0.6
P/E (UBS, diluted)	53.1	22.4	17.6	10.4	7.8	7.2	6.8	6.4
Net dividend yield %	3.4	3.1	4.5	11.0	12.8	12.8	12.8	12.8

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of €1.62 on 28 Jun 2016 21:34 BST

UBS Research THESIS MAP a guide to our thinking and what's where in this report

PIVOTAL QUESTIONS

Q: What is the impact of the "Leave" vote for Intesa?

We expect earnings to be impacted by c-9% on average over 2016E-18E. Main drivers to be: 1) fees (-7% on average): placement fees to suffer from lower AUM sales, impacted by reduced risk appetite, while management and performance fees to be affected by negative market performance. 2) NII (-1% on average) as loan growth is likely to be lower than previously expected due to higher uncertainty. The strong take-up in the recent TLTRO 2 auction should somewhat offset this. In the medium term, main risks to come from 1) further fall in interest rates; 2) asset quality failing to improve.

Q: Can fees hold up amidst current volatility levels?

No. Despite taking a materially more cautious view than management and the market in our initiation (+4% growth in 16E vs. 7-10%), we have had to cut our fee forecasts twice in three months and now expect a 6% decline. This is due to the larger-than-expected slowdown in AUM inflows and a sharp decline in management commissions, testament to increased client risk aversion and negative market performance. Though we do not yet anticipate the reversal of recent savings migration towards AUM/insurance products, with ISP's dominant position and safe-haven status providing some relative support, recent bouts of volatility do not bode well for renewed fee momentum.

Q: Will Intesa remain an attractive dividend payer?

Yes, even if current dividend targets are not met. Including dividend guidance, AT1 coupons and a mild volume acceleration (+1-2% RWA p.a.), ISP would "use" c.30bps of FL CET1 capital p.a., with a 12.0% ratio by 18E (UBSe). While we welcome management's decision to return the excess capital to shareholders, flexibility to absorb negative regulation or increased volume growth will likely narrow, and hence we have reduced 17E dividend from €4.0bn to €3.5bn, the latter more aligned with the bank's profits. This still implies 13% cash yield by 17E, still making ISP an attractive dividend exposure.

UBS VIEW

Still see value in Intesa, also given valuation protection: While the "Leave" vote has rebased down earnings expectations and medium-term uncertainty is significant, the strong market reaction on Intesa has left the shares trading at 0.66x P/TBV17E thus benefitting from sizeable valuation protection.

EVIDENCE

Sensitivity to lower rates and lack of asset quality improvement: Regarding potential risks, we have explored the impact for Intesa from lower rates analysing its balance sheet structure. Moreover we have stress-tested the profitability of the bank for a lack of improvement in provisions. We have then used these scenarios to determine what is reflected by the current valuations.

WHAT'S PRICED IN?

Intesa shares price in to a large extent already the medium-term risks of the "Leave" vote: At 0.66x P/TBV 2017E Intesa looks to be pricing in to a large extent a reduction in NII due to lower rates and a lack of improvement in provisions.

UPSIDE / DOWNSIDE SPECTRUM

Value drivers	AUM fees 17E (€ mn)	Loan growth 17E	CoR 17E (%)	Euribor rate from current	Net profit 17E (€mn)
€2.33 upside	4,082	2.1%	0.50%	0.00%	3,754
€2.15 base	4,082	1.1%	0.58%	0.00%	3,472
€1.59 downside	3,878	0.0%	0.75%	-0.25%	2,569

Source: UBS estimates

COMPANY DESCRIPTION

Intesa is the largest Italian bank, with a full-fledged commercial offering. ISP also has operations in most Eastern European countries.

UPSIDE / DOWNSIDE SPECTRUM

ISP is trading at €1.62 (as of 28 June)

Value drivers	AUM fees 17E (€ mn)	Loan growth 17E	CoR 17E (%)	Euribor rate from current	Net profit 17E (€mn)
€2.33 upside	4,082	2.1%	0.50%	0.00%	3,754
€2.15 base	4,082	1.1%	0.58%	0.00%	3,472
€1.59 downside	3,878	0.0%	0.75%	-0.25%	2,569

Source: UBS estimates

Risk to the current share price is heavily skewed (21:1) to the upside

ISP is trading at **€1.62** (as of 28 June)

Upside (€2.33): We assume €4.1bn market fees, in line with our base case, but loan growth accelerates to 2.1% and cost of risk declines are larger (50bps). We arrive at €3.75bn of net profit and a 10.3% ROTE (on 11% "clean" CET1 FL).

Base (€2.15): Our base case implies €4.1bn market fees, c1% loan growth and a 58bps COR. That yields €3.47bn of adjusted net profit and a 9.5% ROTE (on 11% "clean" CET1 FL).

Downside (€1.59): We assume market fees stand at €3.9bn, assuming a decrease from 2015 levels (€4.3bn), and cost of risk declines more slowly, standing at 75bps by 17E. Loan growth stands at 0%. Euribor decreases by a further 25bps from current levels. We reach €2.6bn of net profit or a c7% ROTE (on 11% "clean" CET1 FL).

COMPANY DESCRIPTION

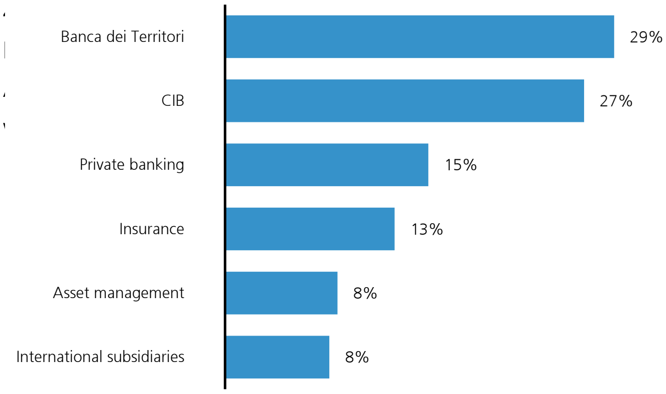
Market Cap	€27.1bn
Shares Outstanding	16,792m
Industry	Banks
Region	Europe
Website	www.group.intesasanpaolo.com

Intesa SanPaolo is the largest bank in Italy in terms of branches and volume market shares. In addition to retail and commercial banking operations, Intesa's divisions include: corporate and investment banking, private banking, asset management, and insurance. The bank has also operations in several CEE countries and Egypt.

Industry outlook

Intesa is mostly exposed to its home market, Italy. After several years of economic downturn, which led to a significant deterioration in banks' asset quality, the country is now experiencing the first signs of recovery. This should allow for a continuation of the improving trend in cost of risk, although risks remain. Low rates affected banks' interest margins, but also allowed for strong fee generation in investment services. The sector is likely to enter a consolidation phase, involving in particular small- and medium-sized banks.

Pre-tax profit 2015 split by operating division



Source: Company data, UBS

Intesa SanPaolo (ISP.MI)

Profit & Loss (€m)	**12/13**	**12/14**	**12/15**	**12/16E**	*% ch*	**12/17E**	*% ch*	**12/18E**	**12/19E**	**12/20E**
Net income interest	8,110	8,358	7,812	7,607	-2.6	7,887	3.7	8,074	8,056	8,068
Total non interest income	8,138	8,470	9,337	8,657	-7.3	9,052	4.6	9,280	9,563	9,886
Total income	**16,248**	**16,828**	**17,149**	**16,264**	-5.2	**16,939**	4.2	**17,355**	**17,619**	**17,954**
Total cash expenses	(7,609)	(7,912)	(8,082)	(7,929)	1.9	(7,979)	-0.6	(8,034)	(8,093)	(8,157)
Pre-depreciation operating profit	**8,639**	**8,916**	**9,067**	**8,335**	-8.1	**8,960**	7.5	**9,321**	**9,526**	**9,797**
Depreciation & amort (excl. goodwill)	(689)	(694)	(734)	(735)	-0.2	(758)	-3.2	(783)	(808)	(835)
Operating profit pre provisions	**7,950**	**8,222**	**8,333**	**7,600**	-8.8	**8,202**	7.9	**8,538**	**8,718**	**8,962**
Total provisions	(7,842)	(5,347)	(3,874)	(3,190)	17.6	(2,467)	22.7	(2,249)	(2,119)	(2,033)
Operating profit post provisions	**108**	**2,875**	**4,459**	**4,410**	-1.1	**5,735**	30.1	**6,289**	**6,599**	**6,930**
Income from associates & JVs (pre-tax)	2,408	388	138	(5)	-	0	-	0	0	0
Other pre-tax items	0	0	0	0	-	0	-	0	0	0
Profit before tax (UBS)	**2,516**	**3,263**	**4,597**	**4,405**	-4.2	**5,735**	30.2	**6,289**	**6,599**	**6,930**
Exceptionals (incl goodwill)	0	0	0	1,526	-	0	-	0	0	0
Profit before tax	**2,516**	**3,263**	**4,597**	**5,930**	29.0	**5,735**	-3.3	**6,289**	**6,599**	**6,930**
Tax	(871)	(1,775)	(1,594)	(1,868)	-17.2	(1,835)	1.8	(2,013)	(2,112)	(2,218)
Profit after tax	**1,645**	**1,488**	**3,003**	**4,062**	35.3	**3,900**	-4.0	**4,277**	**4,487**	**4,712**
Other post-tax items	(6,202)	(20)	(205)	(199)	2.9	(199)	0.0	(184)	(169)	(154)
Preference dividends	0	0	0	0	-	0	-	0	0	0
Minorities	7	(217)	(59)	(89)	-50.8	(69)	22.6	(75)	(79)	(83)
Net earnings (local GAAP)	**(4,550)**	**1,251**	**2,739**	**3,774**	37.8	**3,632**	-3.8	**4,017**	**4,239**	**4,475**
Net earnings (before pref divs)	**(4,550)**	**1,251**	**2,739**	**3,774**	37.8	**3,632**	-3.8	**4,017**	**4,239**	**4,475**
Net earnings (UBS)	**457**	**1,694**	**2,967**	**2,623**	-11.6	**3,472**	32.4	**3,803**	**4,024**	**4,260**

Per share (€)	**12/13**	**12/14**	**12/15**	**12/16E**	*% ch*	**12/17E**	*% ch*	**12/18E**	**12/19E**	**12/20E**
EPS (local GAAP, basic)	(0.28)	0.08	0.16	0.22	37.8	0.22	-3.8	0.24	0.25	0.27
EPS (UBS, diluted)	0.03	0.10	0.18	0.16	-11.6	0.21	32.4	0.23	0.24	0.25
PPOP (diluted)	0.48	0.50	0.50	0.45	-8.8	0.49	7.9	0.51	0.52	0.53
Net DPS	0.05	0.07	0.14	0.18	27.2	0.21	16.7	0.21	0.21	0.21
BVPS	2.71	2.66	2.80	2.85	2.0	2.88	1.0	2.90	2.93	2.97
BVPS (UBS)	2.26	2.23	2.37	2.42	2.4	2.45	1.2	2.47	2.50	2.55

Balance sheet (€m)	**12/13**	**12/14**	**12/15**	**12/16E**	*% ch*	**12/17E**	*% ch*	**12/18E**	**12/19E**	**12/20E**
Banking assets (year end)	624,179	647,343	676,496	696,731	3.0	711,524	2.1	731,116	747,057	762,699
Banking assets (average)	648,881	635,761	661,920	686,614	3.7	704,127	2.6	721,320	739,087	754,878
Total assets (year end)	624,179	647,343	676,496	696,731	3.0	711,524	2.1	731,116	747,057	762,699
Risk weighted assets (RWA) (year end)	276,291	269,790	284,319	279,802	-1.6	282,665	1.0	287,417	292,172	297,295
Risk weighted assets (RWA) (average)	287,455	273,041	277,055	282,061	1.8	281,234	-0.3	285,041	289,795	294,733
Customer loans	343,789	339,002	350,010	356,380	1.8	360,124	1.1	367,379	374,634	382,168
Customer loans (average)	360,207	341,396	344,506	353,195	2.5	358,252	1.4	363,752	371,007	378,401
Interest earning assets (average)	598,527	589,658	616,179	642,115	4.2	659,779	2.8	676,971	694,738	710,529
Customer deposits	372,066	359,808	372,183	364,841	-2.0	355,928	-2.4	354,452	357,242	360,059
Common s/h equity (year end)	44,520	44,683	46,899	47,838	2.0	48,310	1.0	48,613	49,137	49,897
Common s/h equity (average)	46,920	44,602	45,791	47,369	3.4	48,074	1.5	48,461	48,875	49,517
Total SHF (equity, pref & MI) (year end)	45,063	45,232	47,716	48,744	2.2	49,285	1.1	49,663	50,266	51,110
Total SHF (equity, pref & MI) (average)	47,485	45,148	46,474	48,230	3.8	49,015	1.6	49,474	49,965	50,688
Net tangible assets	37,612	37,979	40,521	41,549	2.5	42,090	1.3	42,468	43,071	43,915

Balance sheet structure (%)	**12/13**	**12/14**	**12/15**	**12/16E**	*% ch*	**12/17E**	*% ch*	**12/18E**	**12/19E**	**12/20E**
Loans / banking assets (year end)	55.1	52.4	51.7	51.2	-1.1	50.6	-1.1	50.2	50.1	50.1
Deposits / banking assets (year end)	59.6	55.6	55.0	52.4	-4.8	50.0	-4.5	48.5	47.8	47.2
Loans / deposits	92.4	94.2	94.0	97.7	3.9	101.2	3.6	103.6	104.9	106.1
Total SHF / banking assets (year end)	7.2	7.0	7.1	7.0	-0.8	6.9	-1.0	6.8	6.7	6.7

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

Intesa SanPaolo (ISP.MI)

Capital adequacy (€m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Tier 1 capital	33,840	35,245	36,807	38,914	39,908	41,065	41,467	42,128
Total capital	40,940	41,957	44,252	46,359	47,353	48,510	48,912	49,573
Risk weighted assets (RWA) (year end)	276,291	269,790	284,319	279,802	282,665	287,417	292,172	297,295
Core tier 1 ratio %	11.3	12.9	12.5	12.6	12.5	12.4	12.4	12.5
Tier 1 ratio %	12.2	13.1	12.9	13.9	14.1	14.3	14.2	14.2
Total capital ratio %	14.8	15.6	15.6	16.6	16.8	16.9	16.7	16.7
Tangible equity	37,069	37,430	39,704	40,643	41,115	41,418	41,942	42,702
Equity / assets %	7.1	6.9	6.9	6.9	6.8	6.6	6.6	6.5
Tangible equity to tangible assets %	6.0	5.8	5.9	5.9	5.8	5.7	5.7	5.7

Asset quality (€m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Non performing assets	57,342	62,838	63,114	61,236	57,258	53,574	50,713	48,566
Total risk reserves	29,101	32,182	32,295	31,894	30,830	29,595	28,551	27,722
NPLs / loans %	15.4	16.9	16.5	15.8	14.6	13.5	12.6	11.8
NPL coverage %	50.7	51.2	51.2	52.1	53.8	55.2	56.3	57.1
Provision charge / average loans %	2.0	1.3	1.0	0.8	0.6	0.6	0.5	0.5
Net NPAs / shareholders funds %	62.7	67.8	64.6	60.2	53.6	48.3	44.1	40.8

Profitability (%)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Net interest margin (avg assets)	1.25	1.31	1.18	1.11	1.12	1.12	1.09	1.07
Provisions / operating profit	98.6	65.0	46.5	42.0	30.1	26.3	24.3	22.7
ROE (UBS earnings)	1.0	3.8	6.5	5.5	7.2	7.8	8.2	8.6
RoAdjE (UBS earnings & equity)	1.3	4.5	7.7	6.5	8.5	9.2	9.7	10.1
RoRWA (UBS)	0.16	0.70	1.09	0.96	1.26	1.36	1.42	1.47
RoA (UBS earnings)	(0.64)	0.23	0.45	0.59	0.55	0.59	0.61	0.62

Productivity (%)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Cost income ratio	51.1	51.1	51.4	53.3	51.6	50.8	50.5	50.1
Cost / average assets	1.28	1.35	1.33	1.26	1.24	1.22	1.20	1.19
Compensation expense ratio	37.7	38.4	38.9	40.9	39.4	38.8	38.6	38.3

Growth (%)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Revenue	-9.1	3.6	1.9	-5.2	4.2	2.5	1.5	1.9
Operating profit pre provisions	-11.4	3.4	1.4	-8.8	7.9	4.1	2.1	2.8
Net earnings (UBS)	-41.1	271.1	75.1	-11.6	32.4	9.5	5.8	5.9
Net DPS	0.0	40.0	100.0	27.2	16.7	0.0	0.0	0.0
Total assets (year end)	-7.3	3.7	4.5	3.0	2.1	2.8	2.2	2.1
Customer loans	-8.7	-1.4	3.2	1.8	1.1	2.0	2.0	2.0
Customer deposits	-2.2	-3.3	3.4	-2.0	-2.4	-0.4	0.8	0.8

Value (x)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Market cap/revenues	1.5	2.2	3.0	1.7	1.6	1.6	1.5	1.5
Market cap/deposits	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
P/PPOP (diluted)	3.0	4.6	6.3	3.6	3.3	3.2	3.1	3.0
P/E (local GAAP, basic)	NM	30.4	19.0	7.2	7.5	6.8	6.4	6.1
P/E (UBS, diluted)	53.1	22.4	17.6	10.4	7.8	7.2	6.8	6.4
Net dividend yield %	3.4	3.1	4.5	11.0	12.8	12.8	12.8	12.8
P/BV x	0.5	0.9	1.1	0.6	0.6	0.6	0.6	0.5
P/BV (UBS) x	0.7	1.0	1.3	0.7	0.7	0.7	0.6	0.6

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

UniCredit

Attractive valuation offset by high uncertainty and low visibility

Equities

Italy
Banks, Ex-S&L

12-month rating	Neutral *
12m price target	€2.10
	Prior: €3.20
Price	€1.88

RIC: CRDI.MI **BBG:** UCG IM

Trading data and key metrics

52-wk range	€6.38-1.88
Market cap.	€11.4bn/US$12.6bn
Shares o/s	5,967m (ORD)
Free float	100%
Avg. daily volume ('000)	109,590
Avg. daily value (m)	€311.3
Common s/h equity (12/16E)	€49.4bn
P/BV (12/16E)	0.2x
Tier 1 ratio	11%

EPS (UBS, diluted) (€)

	From	To	% ch	Cons.
12/16E	0.34	0.28	-16	0.37
12/17E	0.43	0.35	-19	0.50
12/18E	0.52	0.44	-15	0.60

Ignacio Cerezo
Analyst
ignacio.cerezo@ubs.com
+44-20-7568 4409

Francesco Di Giambattista
Analyst
francesco.di-giambattista@ubs.com
+44-20-7568 1070

Reiterate Neutral due to high uncertainty despite attractive valuation

UniCredit trades at 0.26x P/TBV, one of the lowest valuations across European banks. While we acknowledge that the stock looks cheap at this point, we think to a large extent the share price already reflects a sizeable capital increase, and we remain Neutral on the name. In particular, we are mindful that a clear strategy for the bank in unlikely to be known for at least few months. Moreover the shares are exposed to further dilution risk in the event of any additional negative performance.

We cut 2016E-18E adjusted EPS by 17% on average, mostly on lower fees

We revise our adjusted EPS forecasts by -16%, -19% and -15% for 2016E, 17E and 18E respectively. These changes are mostly driven by lower expectations on fees, on the back of a likely reduction in risk appetite and higher volatility, and lower NII, due to lower loan growth only partly offset by the support to cost of funding from the recent TLTRO 2 auction pick-up.

Capital remains the main concern

We believe UniCredit is likely to consider approaching the market in the coming months to at least have a substantial buffer above its minimum capital requirements. The size of any capital increase would also depend on any potential disposal and on the future strategy of the bank, as investors could be asked for a larger capital increase so that part of the excess capital is used to execute a restructuring plan with the aim of improving returns. The current valuation in our view is discounting to a large extent a sizable (€5+ bn) capital increase. However dilution would increase should the shares sell off further.

Valuation: heavy discount due to significant uncertainty

On the back of lower earnings and higher cost of equity we reduce our price target for UCI from €3.20 to €2.10. UCI trades on 0.26x PTBV and 5.3x PE17E. Our Gordon growth-derived €2.10 PT is based on 4.3% adjusted ROTE17E, 12% COE (up from 11% previously) and €5.3bn capital shortfall.

Highlights (€m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Revenues	23,316	22,552	22,405	21,607	21,825	22,428	23,110	23,738
Profit before tax	(5,220)	4,091	2,671	2,932	4,226	5,276	5,997	6,385
Net earnings (local GAAP)	(13,965)	2,008	1,694	1,640	2,523	3,222	3,697	3,940
Net earnings (UBS)	(6,549)	2,261	1,801	1,714	2,173	2,741	3,211	3,448
Tier 1 ratio %	10.1	10.1	11.0	11.0	11.8	12.6	12.9	13.2
EPS (UBS, diluted) (€)	(1.08)	0.38	0.30	0.28	0.35	0.44	0.52	0.56

Profitability/valuation	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
ROE (UBS) %	(12.1)	4.8	3.8	3.5	4.3	5.3	6.0	6.2
P/PPOP (diluted)	2.8	3.9	4.0	1.4	1.3	1.2	1.1	1.1
P/BV x	0.5	0.7	0.7	0.2	0.2	0.2	0.2	0.2
P/BV (UBS) x	0.6	0.8	0.8	0.3	0.3	0.2	0.2	0.2
P/E (UBS, diluted)	(3.9)	15.5	19.5	6.7	5.3	4.2	3.6	3.4
Net dividend yield %	2.2	2.0	2.1	4.9	7.6	9.7	11.1	11.9

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of €1.88 on 28 Jun 2016 21:34 BST

* Exception to core rating bands; See page 31.

UBS Research THESIS MAP a guide to our thinking and what's where in this report

PIVOTAL QUESTIONS

Q: What is the impact of the "Leave" vote for UniCredit?

We expect earnings to be impacted by c-17% on average over 2016E-18E. Main drivers to be: 1) Fees (-7% on average): placement fees to suffer from lower AUM sales, impacted by reduced risk appetite, while management and performance fees to be affected by negative market performance. 2) NII (-1% on average) as loan growth is likely to be lower than previously expected due to higher uncertainty. The strong take-up in the recent TLTRO 2 auction should somewhat offset this. In the medium term, main risks to come from 1) further fall in interest rates; 2) asset quality failing to improve.

Q: Can UniCredit meet its fee objectives?

No. Representing 35% of revenues in FY15, fees are one of the key pillars of UCI's 15-18E business plan. YE18E guidance implies 7% CAGR, split between commercial and investment services. We fall significantly short on both categories (c1% CAGR), mostly due to more conservative AUM growth (-1% CAGR vs. 12% target), as we anticipate gross inflow to fall over 16-18E from FY15 levels due to structural challenges and increased risk aversion.

Q: How far is UCI from having to raise capital?

UCI's buffer vs SREP is 50bps phased-in and 10bps fully loaded. This has narrowed following 9bps QoQ FL CET1 erosion in Q1 and given management guidance that recent lending growth is likely to continue; we also see added pressure from RWAs, the main source of capital formation last year. Given our expectation of marginal capital generation until the year-end we think management action is likely. In addition to an outright capital increase, other potential options could include a reduction/cancellation of cash dividends, RWA optimisation and asset disposals. Uncertainty on this front relates to a lack of a clear strategy, likely to last at least few months in our view.

UBS VIEW

Attractive valuation offset by high uncertainty and low visibility: We remain cautious on UniCredit as, in our view, it does not offer an attractive risk-reward given lack of clarity on strategy and additional dilution downside risk from any further share price declines.

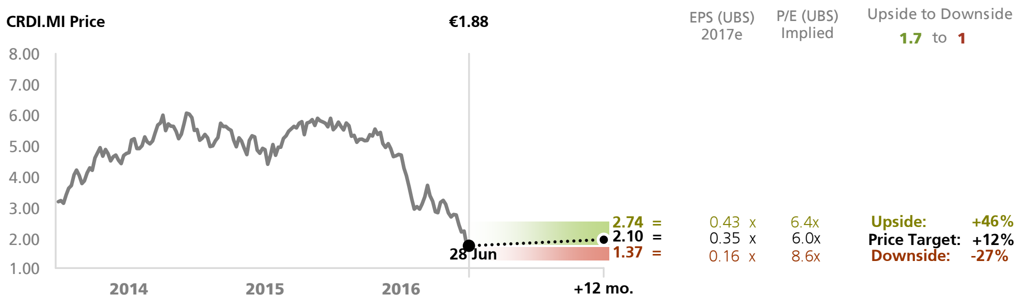
EVIDENCE

Sensitivity to lower rates and lack of asset quality improvement: Regarding potential risks, we have explored the impact on UniCredit of lower rates analysing its balance sheet structure. Moreover we have stress-tested the bank's profitability for a lack of improvement in provisions. We have then used these scenarios to determine what is reflected by the current valuations.

WHAT'S PRICED IN?

Sizable (€5+bn) capital increase priced-in at current prices, but not other risks: UniCredit at 0.26x P/TBV 2017E looks to be pricing in to a large extent a sizeable capital increase, but not fully the medium-term risks on NII (from lower rates) and provisions.

UPSIDE / DOWNSIDE SPECTRUM



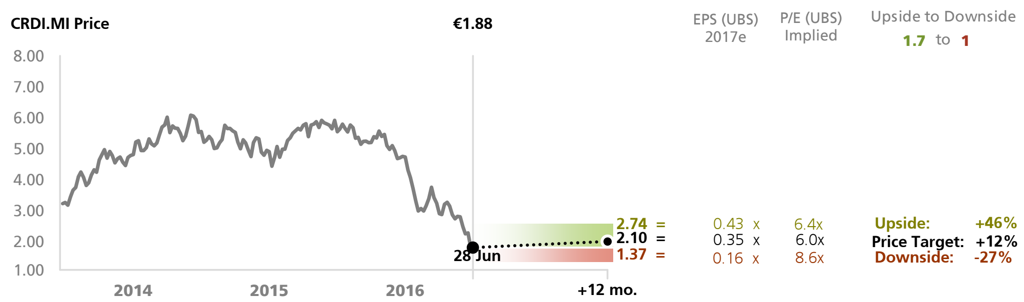
Value drivers	Market fees 17E (€ mn)	Loan growth 17E (%)	CoR 17E (%)	Euribor from current	Net profit 17E (€ mn)
€2.74 upside	3,321	1.6%	0.51%	0.00%	2,629
€2.1 base	3,321	0.8%	0.61%	0.00%	2,173
€1.37 downside	3,155	0.0%	0.68%	-0.25%	1,522

Source: UBS estimates

COMPANY DESCRIPTION

UniCredit is a pan-European commercial bank, with its main operations in Italy, Germany, Austria and an extensive network across the CEE region.

UPSIDE / DOWNSIDE SPECTRUM



UCI is trading at €1.88 (as of 28 June 2016)

Value drivers	Market fees 17E (€ mn)	Loan growth 17E (%)	CoR 17E (%)	Euribor from current	Net profit 17E (€ mn)
€2.74 upside	3,321	1.6%	0.51%	0.00%	2,629
€2.1 base	3,321	0.8%	0.61%	0.00%	2,173
€1.37 downside	3,155	0.0%	0.68%	-0.25%	1,522

Source: UBS estimates

Risk to the current share price is moderately skewed (1.7:1) to the upside

UniCredit is trading at **€1.88** (as of 28 June).

Upside (€2.74): Market fees remain in line with our €3.3bn base case, loan growth doubles to c1.6%, and COR declines accelerate to 51bps. This yields a €2.6bn adjusted net profit and c5.2% ROTE (on 12% "clean" CET1 FL).

Base (€2.10): UCI's market fees in 17E stand at €3.3bn, it grows its loan book by 0.8%, and cost of risk stands at 61bps (from c.80bps in FY15). This implies a €2.17bn adjusted net profit and c4.3% adjusted ROTE (on 12% "clean" CET1 FL).

Downside (€1.37): Market fees decrease to €3.2bn from the €3.6bn figure posted in FY15, loan growth stands at 0% and COR stands at 68bps. Euribor decreases by 25bps from current levels. This yields a €1.5bn adjusted net profit and 3.0% ROTE (on 12% "clean" CET1 FL).

COMPANY DESCRIPTION

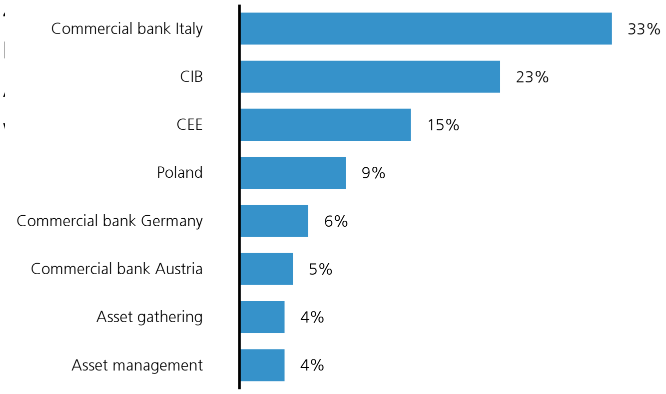
Market Cap	€11.6bn
Shares Outstanding	6,180m
Industry	Banks
Region	Europe
Website	www.unicreditgroup.eu

UniCredit is an Italian-based banking group. The bank is the second largest in Italy, and has sizeable operations in 15 central and eastern European countries. Divisions include corporate and investment banking, asset management and asset gathering.

Industry outlook

UniCredit has a large exposure to its home market, Italy. After several years of economic downturn, which led to a significant deterioration in banks' asset quality, the country is now experiencing the first signs of recovery. This should allow for a continuation of the improving trend in the cost of risk, although risks remain. Low rates affected banks' interest margins, but also allowed for strong fee generation in investment services. The sector is likely to enter a consolidation phase, involving in particular small- and medium-sized banks. UniCredit also has significant exposure to Germany and Austria, as well as CEE.

Pre-tax profit 2015 split by operating division



Source: Company data, UBS

UniCredit (CRDI.MI)

Profit & Loss (€m)	12/13	12/14	12/15	12/16E	% ch	12/17E	% ch	12/18E	12/19E	12/20E
Net income interest	12,303	12,442	11,916	11,564	-3.0	11,739	1.5	12,059	12,402	12,761
Total non interest income	11,014	10,110	10,488	10,043	-4.2	10,086	0.4	10,369	10,707	10,977
Total income	**23,316**	**22,552**	**22,405**	**21,607**	-3.6	**21,825**	1.0	**22,428**	**23,110**	**23,738**
Total cash expenses	(13,016)	(12,611)	(12,690)	(12,285)	3.2	(11,973)	2.5	(11,740)	(11,904)	(12,080)
Pre-depreciation operating profit	**10,301**	**9,941**	**9,715**	**9,322**	-4.1	**9,853**	5.7	**10,687**	**11,206**	**11,658**
Depreciation & amort (excl. goodwill)	(1,238)	(896)	(929)	(960)	-3.4	(976)	-1.6	(993)	(1,013)	(1,034)
Operating profit pre provisions	**9,063**	**9,045**	**8,787**	**8,362**	-4.8	**8,877**	6.2	**9,694**	**10,192**	**10,624**
Total provisions	(15,176)	(5,041)	(6,109)	(5,397)	11.7	(4,659)	13.7	(4,427)	(4,204)	(4,248)
Operating profit post provisions	**(6,113)**	**4,004**	**2,678**	**2,965**	10.7	**4,217**	42.3	**5,268**	**5,989**	**6,377**
Income from associates & JVs (pre-tax)	892	87	(6)	(33)	NM	8	-	8	8	9
Other pre-tax items	0	0	0	0	-	0	-	0	0	0
Profit before tax (UBS)	**(5,220)**	**4,091**	**2,671**	**2,932**	9.8	**4,226**	44.1	**5,276**	**5,997**	**6,385**
Exceptionals (incl goodwill)	0	0	0	0	-	0	-	0	0	0
Profit before tax	**(5,220)**	**4,091**	**2,671**	**2,932**	9.8	**4,226**	44.1	**5,276**	**5,997**	**6,385**
Tax	1,716	(1,297)	(137)	(842)	NM	(1,246)	-48.0	(1,589)	(1,827)	(1,962)
Profit after tax	**(3,504)**	**2,793**	**2,534**	**2,089**	-17.5	**2,979**	42.6	**3,687**	**4,170**	**4,423**
Other post-tax items	(10,079)	(405)	(488)	(98)	80.0	(93)	5.1	(73)	(53)	(33)
Preference dividends	0	0	0	0	-	0	-	0	0	0
Minorities	(382)	(380)	(352)	(352)	0.0	(363)	-3.4	(392)	(420)	(450)
Net earnings (local GAAP)	**(13,965)**	**2,008**	**1,694**	**1,640**	-3.2	**2,523**	53.8	**3,222**	**3,697**	**3,940**
Net earnings (before pref divs)	**(13,965)**	**2,008**	**1,694**	**1,640**	-3.2	**2,523**	53.8	**3,222**	**3,697**	**3,940**
Net earnings (UBS)	**(6,549)**	**2,261**	**1,801**	**1,714**	-4.8	**2,173**	26.8	**2,741**	**3,211**	**3,448**

Per share (€)	12/13	12/14	12/15	12/16E	% ch	12/17E	% ch	12/18E	12/19E	12/20E
EPS (local GAAP, basic)	(2.31)	0.33	0.28	0.27	-4.6	0.41	51.5	0.52	0.60	0.64
EPS (UBS, diluted)	(1.08)	0.38	0.30	0.28	-6.2	0.35	24.8	0.44	0.52	0.56
PPOP (diluted)	1.50	1.50	1.46	1.37	-6.2	1.44	4.5	1.57	1.65	1.72
Net DPS	0.09	0.12	0.12	0.09	-22.6	0.14	53.8	0.18	0.21	0.22
BVPS	7.74	7.91	8.05	7.99	-0.7	8.25	3.2	8.54	8.88	9.22
BVPS (UBS)	6.86	6.98	7.09	7.07	-0.2	7.32	3.5	7.61	7.94	8.29

Balance sheet (€m)	12/13	12/14	12/15	12/16E	% ch	12/17E	% ch	12/18E	12/19E	12/20E
Banking assets (year end)	827,538	844,217	860,433	882,984	2.6	884,471	0.2	887,403	894,771	902,710
Banking assets (average)	877,188	835,878	852,325	871,709	2.3	883,728	1.4	885,937	891,087	898,740
Total assets (year end)	827,538	844,217	860,433	882,984	2.6	884,471	0.2	887,403	894,771	902,710
Risk weighted assets (RWA) (year end)	423,739	409,223	390,599	397,280	1.7	400,945	0.9	405,378	412,666	420,431
Risk weighted assets (RWA) (average)	425,433	416,481	399,911	393,940	-1.5	399,113	1.3	403,161	409,022	416,549
Customer loans	483,684	470,569	473,999	482,377	1.8	486,333	0.8	491,710	501,497	511,832
Customer loans (average)	515,414	477,126	472,284	478,188	1.3	484,355	1.3	489,021	496,604	506,665
Interest earning assets (average)	799,258	769,086	791,120	812,669	2.7	824,441	1.4	826,650	831,800	839,453
Customer deposits	557,764	560,688	584,268	601,379	2.9	602,229	0.1	603,242	609,233	616,705
Common s/h equity (year end)	46,722	47,501	48,198	49,407	2.5	50,976	3.2	52,803	54,855	56,979
Common s/h equity (average)	54,150	47,112	47,850	48,803	2.0	50,192	2.8	51,890	53,829	55,917
Total SHF (equity, pref & MI) (year end)	50,056	50,947	51,597	53,158	3.0	55,090	3.6	57,309	59,781	62,355
Total SHF (equity, pref & MI) (average)	57,651	50,501	51,272	52,377	2.2	54,124	3.3	56,200	58,545	61,068
Net tangible assets	44,729	45,386	45,839	47,445	3.5	49,332	4.0	51,550	54,023	56,596

Balance sheet structure (%)	12/13	12/14	12/15	12/16E	% ch	12/17E	% ch	12/18E	12/19E	12/20E
Loans / banking assets (year end)	58.4	55.7	55.1	54.6	-0.8	55.0	0.7	55.4	56.0	56.7
Deposits / banking assets (year end)	67.4	66.4	67.9	68.1	0.3	68.1	0.0	68.0	68.1	68.3
Loans / deposits	86.7	83.9	81.1	80.2	-1.1	80.8	0.7	81.5	82.3	83.0
Total SHF / banking assets (year end)	6.0	6.0	6.0	6.0	0.4	6.2	3.5	6.5	6.7	6.9

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

UniCredit (CRDI.MI)

Capital adequacy (€m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Tier 1 capital	42,737	41,251	42,897	43,694	47,390	51,257	53,307	55,521
Total capital	57,651	47,919	50,970	51,768	55,463	59,330	61,380	63,594
Risk weighted assets (RWA) (year end)	423,739	409,223	390,599	397,280	400,945	405,378	412,666	420,431
Core tier 1 ratio %	9.6	9.7	10.5	10.5	10.8	11.1	11.4	11.8
Tier 1 ratio %	10.1	10.1	11.0	11.0	11.8	12.6	12.9	13.2
Total capital ratio %	13.6	11.7	13.0	13.0	13.8	14.6	14.9	15.1
Tangible equity	41,395	41,940	42,440	43,694	45,218	47,045	49,097	51,220
Equity / assets %	5.6	5.6	5.6	5.6	5.8	6.0	6.1	6.3
Tangible equity to tangible assets %	5.0	5.0	5.0	5.0	5.1	5.3	5.5	5.7

Asset quality (€m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Non performing assets	83,590	84,360	79,760	76,302	73,534	71,377	69,777	68,356
Total risk reserves	46,772	45,773	43,257	42,338	41,506	40,777	40,374	40,014
NPLs / loans %	15.8	16.3	15.4	14.5	13.9	13.4	12.9	12.4
NPL coverage %	56.0	54.3	54.2	55.5	56.4	57.1	57.9	58.5
Provision charge / average loans %	2.6	0.9	0.9	0.7	0.7	0.6	0.5	0.5
Net NPAs / shareholders funds %	73.6	75.7	70.7	63.9	58.1	53.4	49.2	45.5

Profitability (%)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Net interest margin (avg assets)	1.40	1.49	1.40	1.33	1.33	1.36	1.39	1.42
Provisions / operating profit	167.4	55.7	69.5	64.5	52.5	45.7	41.2	40.0
ROE (UBS earnings)	-12.1	4.8	3.8	3.5	4.3	5.3	6.0	6.2
RoAdjE (UBS earnings & equity)	(15.0)	5.4	4.3	4.0	4.9	5.9	6.7	6.9
RoRWA (UBS)	(1.45)	0.63	0.54	0.52	0.64	0.78	0.89	0.94
RoA (UBS earnings)	(1.28)	0.33	0.30	0.24	0.34	0.42	0.47	0.49

Productivity (%)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Cost income ratio	61.1	59.9	60.8	61.3	59.3	56.8	55.9	55.2
Cost / average assets	1.62	1.62	1.60	1.52	1.47	1.44	1.45	1.46
Compensation expense ratio	48.0	47.6	48.7	49.4	47.6	45.1	44.2	43.6

Growth (%)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Revenue	-8.1	-3.3	-0.7	-3.6	1.0	2.8	3.0	2.7
Operating profit pre provisions	-12.8	-0.2	-2.9	-4.8	6.2	9.2	5.1	4.2
Net earnings (UBS)	-	-	-20.3	-4.8	26.8	26.1	17.1	7.4
Net DPS	11.3	22.3	3.8	-22.6	53.8	27.7	14.7	6.6
Total assets (year end)	-10.7	2.0	1.9	2.6	0.2	0.3	0.8	0.9
Customer loans	-11.6	-2.7	0.7	1.8	0.8	1.1	2.0	2.1
Customer deposits	-3.5	0.5	4.2	2.9	0.1	0.2	1.0	1.2

Value (x)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Market cap/revenues	1.1	1.6	1.6	0.5	0.5	0.5	0.5	0.5
Market cap/deposits	0.0	0.1	0.1	0.0	0.0	0.0	0.0	0.0
P/PPOP (diluted)	2.8	3.9	4.0	1.4	1.3	1.2	1.1	1.1
P/E (local GAAP, basic)	NM	17.5	20.7	7.0	4.6	3.6	3.1	2.9
P/E (UBS, diluted)	(3.9)	15.5	19.5	6.7	5.3	4.2	3.6	3.4
Net dividend yield %	2.2	2.0	2.1	4.9	7.6	9.7	11.1	11.9
P/BV x	0.5	0.7	0.7	0.2	0.2	0.2	0.2	0.2
P/BV (UBS) x	0.6	0.8	0.8	0.3	0.3	0.2	0.2	0.2

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

Intesa SanPaolo Investment case

Intesa is the largest Italian bank, with a fully-fledged commercial offering. ISP also has operations in most Eastern European countries. Intesa has a resilient profile thanks to a solid capital position and best in class asset quality in Italy. Moreover we see returns well underpinned by structural efficiency and improving LLPs. We also find that the market is currently reflecting the medium-term risks of lower rates and higher provisions, an approach we find too conservative. Though likely below company targets, ISP's capital/dividend advantage appears safe, at least until YE17E. We expect the bank to achieve a c9% ROTE in 2017E.

UniCredit Investment case

UniCredit is a pan-European commercial bank, with its main operations in Italy, Germany, Austria and an extensive network across the CEE region. UniCredit trades at one of the lowest valuations across European banks. While we acknowledge that the stock looks cheap at this point, we believe that to a large extent this reflects a sizeable capital increase, and we remain Neutral on the name. In particular, we are mindful that a clear strategy for the bank in unlikely to be known for at least few months. Moreover the shares are exposed to further dilution risk in the event of any additional negative performance. We expect the bank to achieve a c5% ROTE in 2017E.

Valuation Method and Risk Statement

Valuation method: We have used the traditional Gordon growth methodology for valuation. We are advocates of ROTE being the main driver for valuation multiples. We clean profits from non-recurrent items and deduct AT1 coupons to get to our adjusted returns. As COE we use 11.0% for ISP and 12.0% for UCI. To determine whether banks have excess or shortfall of capital, which we value at 1x PTBV, we use an 11% fully loaded CET1 threshold for ISP and 12% for UCI, to reflect its GSIB buffer.

Risks: Intesa and UniCredit are exposed to macro risks, asset quality risks, unexpected changes in interest rates, any slowdown in the savings industry, developments in CEE, risks from insurance activities, regulatory and operational risks, and potential M&A activity with positive or negative implications for shareholders.

Required Disclosures

This report has been prepared by UBS Limited, an affiliate of UBS AG. UBS AG, its subsidiaries, branches and affiliates are referred to herein as UBS.

For information on the ways in which UBS manages conflicts and maintains independence of its research product; historical performance information; and certain additional disclosures concerning UBS research recommendations, please visit www.ubs.com/disclosures. The figures contained in performance charts refer to the past; past performance is not a reliable indicator of future results. Additional information will be made available upon request. UBS Securities Co. Limited is licensed to conduct securities investment consultancy businesses by the China Securities Regulatory Commission. UBS acts or may act as principal in the debt securities (or in related derivatives) that may be the subject of this report.

Analyst Certification: Each research analyst primarily responsible for the content of this research report, in whole or in part, certifies that with respect to each security or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about those securities or issuers and were prepared in an independent manner, including with respect to UBS, and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by that research analyst in the research report.

UBS Investment Research: Global Equity Rating Definitions

12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	49%	32%
Neutral	FSR is between -6% and 6% of the MRA.	38%	26%
Sell	FSR is > 6% below the MRA.	14%	19%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 31 March 2016.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

KEY DEFINITIONS: Forecast Stock Return (FSR) is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months. **Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium). **Under Review (UR)** Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation. **Short-Term Ratings** reflect the expected near-term (up to three months) performance of the stock and do not reflect any change in the fundamental view or investment case. **Equity Price Targets** have an investment horizon of 12 months.

EXCEPTIONS AND SPECIAL CASES: UK and European Investment Fund ratings and definitions are: Buy: Positive on factors such as structure, management, performance record, discount; **Neutral:** Neutral on factors such as structure, management, performance record, discount; **Sell:** Negative on factors such as structure, management, performance record, discount. **Core Banding Exceptions (CBE):** Exceptions to the standard +/-6% bands may be granted by the Investment Review Committee (IRC). Factors considered by the IRC include the stock's volatility and the credit spread of the respective company's debt. As a result, stocks deemed to be very high or low risk may be subject to higher or lower bands as they relate to the rating. When such exceptions apply, they will be identified in the Company Disclosures table in the relevant research piece.

Research analysts contributing to this report who are employed by any non-US affiliate of UBS Securities LLC are not registered/qualified as research analysts with FINRA. Such analysts may not be associated persons of UBS Securities LLC and therefore are not subject to the FINRA restrictions on communications with a subject company, public appearances, and trading securities held by a research analyst account. The name of each affiliate and analyst employed by that affiliate contributing to this report, if any, follows.

UBS Limited: Ignacio Cerezo; Francesco Di Giambattista.

Company Disclosures

Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Intesa SanPaolo[2, 3a, 4, 5, 7, 13]	ISP.MI	Buy	N/A	€1.62	28 Jun 2016
UniCredit[2, 3b, 4, 5, 7, 20]	CRDI.MI	Neutral (CBE)	N/A	€1.88	28 Jun 2016

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date

2. UBS AG, its affiliates or subsidiaries has acted as manager/co-manager in the underwriting or placement of securities of this company/entity or one of its affiliates within the past 12 months.

3a. UBS Limited is advising Intesa Sanpaolo SpA on the sale of the total share capital of its subsidiaries Setefi Services S.p.A. and Intesa Sanpaolo Card d.o.o. (a Croatian company) to a wholly owned subsidiary of Mercury UK Holdco Limited which is controlled by a consortium composed of Advent, Bain Capital and Clessidra

3b. UBS Ltd is advising Santander Asset Management regarding talks with UniCredit Group in relation to a possible combination with its asset management business.

4. Within the past 12 months, UBS AG, its affiliates or subsidiaries has received compensation for investment banking services from this company/entity or one of its affiliates.

5. UBS AG, its affiliates or subsidiaries expect to receive or intend to seek compensation for investment banking services from this company/entity within the next three months.

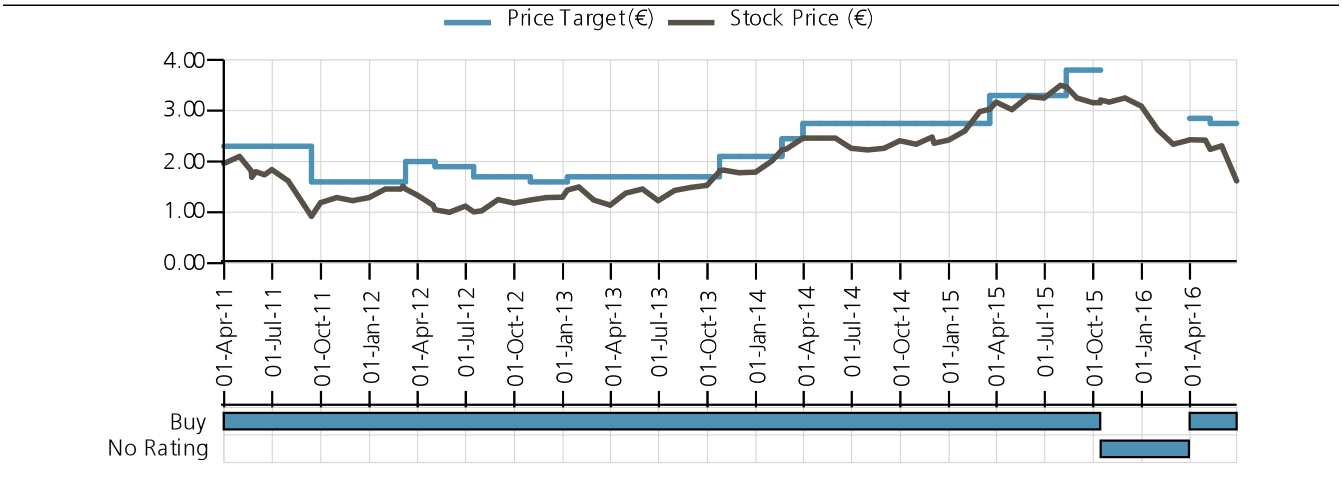
7. Within the past 12 months, UBS Securities LLC and/or its affiliates have received compensation for products and services other than investment banking services from this company/entity.

13. UBS AG, its affiliates or subsidiaries beneficially owned 1% or more of a class of this company`s common equity securities as of last month`s end (or the prior month`s end if this report is dated less than 10 days after the most recent month`s end).

20. Because this security exhibits higher-than-average volatility, the FSR has been set at 15% above the MRA for a Buy rating, and at -15% below the MRA for a Sell rating (compared with 6/-6% under the normal rating system).

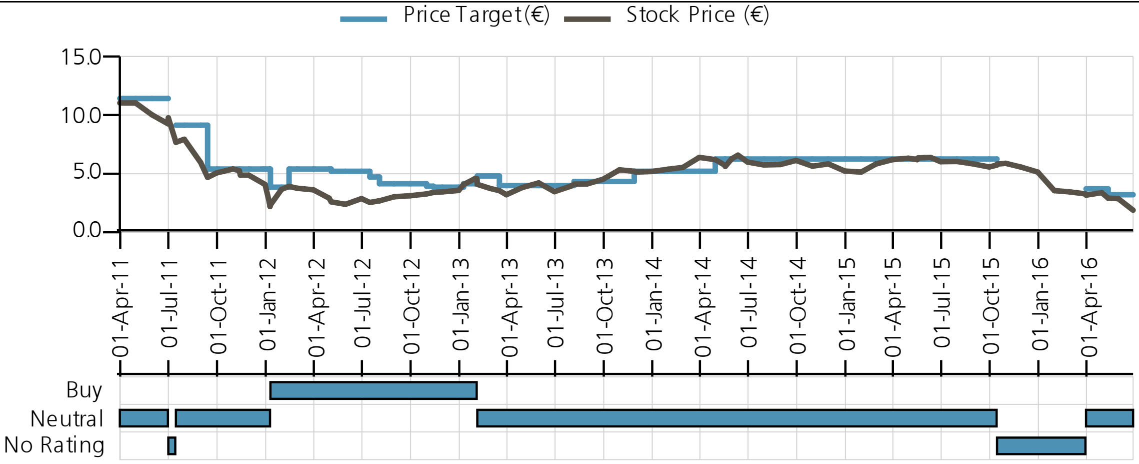
Unless otherwise indicated, please refer to the Valuation and Risk sections within the body of this report. For a complete set of disclosure statements associated with the companies discussed in this report, including information on valuation and risk, please contact UBS Securities LLC, 1285 Avenue of Americas, New York, NY 10019, USA, Attention: Investment Research.

Intesa SanPaolo (€)



Source: UBS; as of 28 Jun 2016

UniCredit (€)



Source: UBS; as of 28 Jun 2016

Global Disclaimer

This document has been prepared by UBS Limited, an affiliate of UBS AG. UBS AG, its subsidiaries, branches and affiliates are referred to herein as UBS.

Global Research is provided to our clients through UBS Neo and, in certain instances, UBS.com (each a "System"). It may also be made available through third party vendors and distributed by UBS and/or third parties via e-mail or alternative electronic means. The level and types of services provided by Global Research to a client may vary depending upon various factors such as a client's individual preferences as to the frequency and manner of receiving communications, a client's risk profile and investment focus and perspective (e.g., market wide, sector specific, long-term, short-term, etc.), the size and scope of the overall client relationship with UBS and legal and regulatory constraints.

All Global Research is available on UBS Neo. Please contact your UBS sales representative if you wish to discuss your access to UBS Neo.

When you receive Global Research through a System, your access and/or use of such Global Research is subject to this Global Research Disclaimer and to the terms of use governing the applicable System.

When you receive Global Research via a third party vendor, e-mail or other electronic means, your use shall be subject to this Global Research Disclaimer and to UBS's Terms of Use/Disclaimer (http://www.ubs.com/global/en/legalinfo2/disclaimer.html). By accessing and/or using Global Research in this manner, you are indicating that you have read and agree to be bound by our Terms of Use/Disclaimer. In addition, you consent to UBS processing your personal data and using cookies in accordance with our Privacy Statement (http://www.ubs.com/global/en/legalinfo2/privacy.html) and cookie notice (http://www.ubs.com/global/en/homepage/cookies/cookie-management.html).

If you receive Global Research, whether through a System or by any other means, you agree that you shall not copy, revise, amend, create a derivative work, transfer to any third party, or in any way commercially exploit any UBS research provided via Global Research or otherwise, and that you shall not extract data from any research or estimates provided to you via Global Research or otherwise, without the prior written consent of UBS.

This document is for distribution only as may be permitted by law. It is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or would subject UBS to any registration or licensing requirement within such jurisdiction. It is published solely for information purposes; it is not an advertisement nor is it a solicitation or an offer to buy or sell any financial instruments or to participate in any particular trading strategy. No representation or warranty, either expressed or implied, is provided in relation to the accuracy, completeness or reliability of the information contained in this document ("the Information"), except with respect to Information concerning UBS. The Information is not intended to be a complete statement or summary of the securities, markets or developments referred to in the document. UBS does not undertake to update or keep current the Information. Any opinions expressed in this document may change without notice and may differ or be contrary to opinions expressed by other business areas or groups of UBS. Any statements contained in this report attributed to a third party represent UBS's interpretation of the data, information and/or opinions provided by that third party either publicly or through a subscription service, and such use and interpretation have not been reviewed by the third party.

Nothing in this document constitutes a representation that any investment strategy or recommendation is suitable or appropriate to an investor's individual circumstances or otherwise constitutes a personal recommendation. Investments involve risks, and investors should exercise prudence and their own judgement in making their investment decisions. The financial instruments described in the document may not be eligible for sale in all jurisdictions or to certain categories of investors. Options, derivative products and futures are not suitable for all investors, and trading in these instruments is considered risky. Mortgage and asset-backed securities may involve a high degree of risk and may be highly volatile in response to fluctuations in interest rates or other market conditions. Foreign currency rates of exchange may adversely affect the value, price or income of any security or related instrument referred to in the document. For investment advice, trade execution or other enquiries, clients should contact their local sales representative.

The value of any investment or income may go down as well as up, and investors may not get back the full (or any) amount invested. Past performance is not necessarily a guide to future performance. Neither UBS nor any of its directors, employees or agents accepts any liability for any loss (including investment loss) or damage arising out of the use of all or any of the Information.

Any prices stated in this document are for information purposes only and do not represent valuations for individual securities or other financial instruments. There is no representation that any transaction can or could have been effected at those prices, and any prices do not necessarily reflect UBS's internal books and records or theoretical model-based valuations and may be based on certain assumptions. Different assumptions by UBS or any other source may yield substantially different results.

This document and the Information are produced by UBS as part of its research function and are provided to you solely for general background information. UBS has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient. In no circumstances may this document or any of the Information be used for any of the following purposes:

(i) valuation or accounting purposes;

(ii) to determine the amounts due or payable, the price or the value of any financial instrument or financial contract; or

(iii) to measure the performance of any financial instrument.

By receiving this document and the Information you will be deemed to represent and warrant to UBS that you will not use this document or any of the Information for any of the above purposes or otherwise rely upon this document or any of the Information.

UBS has policies and procedures, which include, without limitation, independence policies and permanent information barriers, that are intended, and upon which UBS relies, to manage potential conflicts of interest and control the flow of information within divisions of UBS and among its subsidiaries, branches and affiliates. For further information on the ways in which UBS manages conflicts and maintains independence of its research products, historical performance information and certain additional disclosures concerning UBS research recommendations, please visit www.ubs.com/disclosures.

Research will initiate, update and cease coverage solely at the discretion of UBS Investment Bank Research Management, which will also have sole discretion on the timing and frequency of any published research product. The analysis contained in this document is based on numerous assumptions. All material information in relation to published research reports, such as valuation methodology, risk statements, underlying assumptions (including sensitivity analysis of those assumptions), ratings history etc. as required by the Market Abuse Regulation, can be found on NEO. Different assumptions could result in materially different results.

The analyst(s) responsible for the preparation of this document may interact with trading desk personnel, sales personnel and other parties for the purpose of gathering, applying and interpreting market information. UBS relies on information barriers to control the flow of information contained in one or more areas within UBS into other areas, units, groups or affiliates of UBS. The compensation of the analyst who prepared this document is determined exclusively by research management and senior management (not including investment banking). Analyst compensation is not based on investment banking revenues; however, compensation may relate to the revenues of UBS Investment Bank as a whole, of which investment banking, sales and trading are a part, and UBS's subsidiaries, branches and affiliates as a whole.

For financial instruments admitted to trading on an EU regulated market: UBS AG, its affiliates or subsidiaries (excluding UBS Securities LLC) acts as a market maker or liquidity provider (in accordance with the interpretation of these terms in the UK) in the financial instruments of the issuer save that where the activity of liquidity provider is carried out in accordance with the definition given to it by the laws and regulations of any other EU jurisdictions, such information is separately disclosed in this document. For financial instruments admitted to trading on a non-EU regulated market: UBS may act as a market maker save that where this activity is carried out in the US in accordance with the definition given to it by the relevant laws and regulations, such activity will be specifically disclosed in this document. UBS may have issued a warrant the value of which is based on one or more of the financial instruments referred to in the document. UBS and its affiliates and employees may have long or short positions, trade as principal and buy and sell in instruments or derivatives identified herein; such transactions or positions may be inconsistent with the opinions expressed in this document.

United Kingdom and the rest of Europe: Except as otherwise specified herein, this material is distributed by UBS Limited to persons who are eligible counterparties or professional clients. UBS Limited is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. **France:** Prepared by UBS Limited and distributed by UBS Limited and UBS Securities France S.A. UBS Securities France S.A. is regulated by the ACPR (Autorité de Contrôle Prudentiel et de Résolution) and the Autorité des Marchés Financiers (AMF). Where an analyst of UBS Securities France S.A. has contributed to this document, the document is also deemed to have been prepared by UBS Securities France S.A. **Germany:** Prepared by UBS Limited and distributed by UBS Limited and UBS Deutschland AG. UBS Deutschland AG is regulated by the Bundesanstalt fur Finanzdienstleistungsaufsicht (BaFin). **Spain:** Prepared by UBS Limited and distributed by UBS Limited and UBS Securities España SV, SA. UBS Securities España SV, SA is regulated by the Comisión Nacional del Mercado de Valores (CNMV). **Turkey:**

Distributed by UBS Limited. No information in this document is provided for the purpose of offering, marketing and sale by any means of any capital market instruments and services in the Republic of Turkey. Therefore, this document may not be considered as an offer made or to be made to residents of the Republic of Turkey. UBS AG is not licensed by the Turkish Capital Market Board under the provisions of the Capital Market Law (Law No. 6362). Accordingly, neither this document nor any other offering material related to the instruments/services may be utilized in connection with providing any capital market services to persons within the Republic of Turkey without the prior approval of the Capital Market Board. However, according to article 15 (d) (ii) of the Decree No. 32, there is no restriction on the purchase or sale of the securities abroad by residents of the Republic of Turkey. **Poland:** Distributed by UBS Limited (spolka z ograniczona odpowiedzialnoscia) Oddzial w Polsce regulated by the Polish Financial Supervision Authority. Where an analyst of UBS Limited (spolka z ograniczona odpowiedzialnoscia) Oddzial w Polsce has contributed to this document, the document is also deemed to have been prepared by UBS Limited (spolka z ograniczona odpowiedzialnoscia) Oddzial w Polsce. **Russia:** Prepared and distributed by UBS Bank (OOO). **Switzerland:** Distributed by UBS AG to persons who are institutional investors only. UBS AG is regulated by the Swiss Financial Market Supervisory Authority (FINMA). **Italy:** Prepared by UBS Limited and distributed by UBS Limited and UBS Limited, Italy Branch. Where an analyst of UBS Limited, Italy Branch has contributed to this document, the document is also deemed to have been prepared by UBS Limited, Italy Branch. **South Africa:** Distributed by UBS South Africa (Pty) Limited (Registration No. 1995/011140/07), an authorised user of the JSE and an authorised Financial Services Provider (FSP 7328). **Israel:** This material is distributed by UBS Limited. UBS Limited is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. UBS Securities Israel Ltd is a licensed Investment Marketer that is supervised by the Israel Securities Authority (ISA). UBS Limited and its affiliates incorporated outside Israel are not licensed under the Israeli Advisory Law. UBS Limited is not covered by insurance as required from a licensee under the Israeli Advisory Law. UBS may engage among others in issuance of Financial Assets or in distribution of Financial Assets of other issuers for fees or other benefits. UBS Limited and its affiliates may prefer various Financial Assets to which they have or may have Affiliation (as such term is defined under the Israeli Advisory Law). Nothing in this Material should be considered as investment advice under the Israeli Advisory Law. This Material is being issued only to and/or is directed only at persons who are Eligible Clients within the meaning of the Israeli Advisory Law, and this material must not be relied on or acted upon by any other persons. **Saudi Arabia:** This document has been issued by UBS AG (and/or any of its subsidiaries, branches or affiliates), a public company limited by shares, incorporated in Switzerland with its registered offices at Aeschenvorstadt 1, CH-4051 Basel and Bahnhofstrasse 45, CH-8001 Zurich. This publication has been approved by UBS Saudi Arabia (a subsidiary of UBS AG), a Saudi closed joint stock company incorporated in the Kingdom of Saudi Arabia under commercial register number 1010257812 having its registered office at Tatweer Towers, P.O. Box 75724, Riyadh 11588, Kingdom of Saudi Arabia. UBS Saudi Arabia is authorized and regulated by the Capital Market Authority to conduct securities business under license number 08113-37. **Dubai:** The information distributed by UBS AG Dubai Branch is intended for Professional Clients only and is not for further distribution within the United Arab Emirates. **United States:** Distributed to US persons by either UBS Securities LLC or by UBS Financial Services Inc., subsidiaries of UBS AG; or by a group, subsidiary or affiliate of UBS AG that is not registered as a US broker-dealer (a **'non-US affiliate'**) to major US institutional investors only. UBS Securities LLC or UBS Financial Services Inc. accepts responsibility for the content of a document prepared by another non-US affiliate when distributed to US persons by UBS Securities LLC or UBS Financial Services Inc. All transactions by a US person in the securities mentioned in this document must be effected through UBS Securities LLC or UBS Financial Services Inc., and not through a non-US affiliate. UBS Securities LLC is not acting as a municipal advisor to any municipal entity or obligated person within the meaning of Section 15B of the Securities Exchange Act (the "Municipal Advisor Rule"), and the opinions or views contained herein are not intended to be, and do not constitute, advice within the meaning of the Municipal Advisor Rule. **Canada:** Distributed by UBS Securities Canada Inc., a registered investment dealer in Canada and a Member-Canadian Investor Protection Fund, or by another affiliate of UBS AG that is registered to conduct business in Canada or is otherwise exempt from registration. **Mexico:** This report has been distributed and prepared by UBS Casa de Bolsa, S.A. de C.V., UBS Grupo Financiero, an entity that is part of UBS Grupo Financiero, S.A. de C.V. and is an affiliate of UBS AG. This document is intended for distribution to institutional or sophisticated investors only. Research reports only reflect the views of the analysts responsible for the reports. Analysts do not receive any compensation from persons or entities different from UBS Casa de Bolsa, S.A. de C.V., UBS Grupo Financiero, or different from entities belonging to the same financial group or business group of such. For Spanish translations of applicable disclosures, please see www.ubs.com/disclosures **Brazil:** Except as otherwise specified herein, this material is prepared by UBS Brasil CCTVM S.A. to persons who are eligible investors residing in Brazil, which are considered to be: (i) financial institutions, (ii) insurance firms and investment capital companies, (iii) supplementary pension entities, (iv) entities that hold financial investments higher than R$300,000.00 and that confirm the status of qualified investors in written, (v) investment funds, (vi) securities portfolio managers and securities consultants duly authorized by Comissão de Valores Mobiliários (CVM), regarding their own investments, and (vii) social security systems created by the Federal Government, States, and Municipalities. **Hong Kong:** Distributed by UBS Securities Asia Limited and/or UBS AG, Hong Kong Branch. **Singapore:** Distributed by UBS Securities Pte. Ltd. [MCI (P) 018/09/2015 and Co. Reg. No.: 198500648C] or UBS AG, Singapore Branch. Please contact UBS Securities Pte. Ltd., an exempt financial adviser under the Singapore Financial Advisers Act (Cap. 110); or UBS AG, Singapore Branch, an exempt financial adviser under the Singapore Financial Advisers Act (Cap. 110) and a wholesale bank licensed under the Singapore Banking Act (Cap. 19) regulated by the Monetary Authority of Singapore, in respect of any matters arising from, or in connection with, the analysis or document. The recipients of this document represent and warrant that they are accredited and institutional investors as defined in the Securities and Futures Act (Cap. 289). **Japan:** Distributed by UBS Securities Japan Co., Ltd. to professional investors (except as otherwise permitted). Where this document has been prepared by UBS Securities Japan Co., Ltd., UBS Securities Japan Co., Ltd. is the author, publisher and distributor of the document. Distributed by UBS AG, Tokyo Branch to Professional Investors (except as otherwise permitted) in relation to foreign exchange and other banking businesses when relevant. **Australia:** Clients of UBS AG: Distributed by UBS AG (Holder of Australian Financial Services License No. 231087). Clients of UBS Securities Australia Ltd: Distributed by UBS Securities Australia Ltd (Holder of Australian Financial Services License No. 231098). This Document contains general information and/or general advice only and does not constitute personal financial product advice. As such, the Information in this document has been prepared without taking into account any investor's objectives, financial situation or needs, and investors should, before acting on the Information, consider the appropriateness of the Information, having regard to their objectives, financial situation and needs. If the Information contained in this document relates to the acquisition, or potential acquisition of a particular financial product by a 'Retail' client as defined by section 761G of the Corporations Act 2001 where a Product Disclosure Statement would be required, the retail client should obtain and consider the Product Disclosure Statement relating to the product before making any decision about whether to acquire the product. The UBS Securities Australia Limited Financial Services Guide is available at: www.ubs.com/ecs-research-fsg. **New Zealand:** Distributed by UBS New Zealand Ltd. The information and recommendations in this publication are provided for general information purposes only. To the extent that any such information or recommendations constitute financial advice, they do not take into account any person's particular financial situation or goals. We recommend that recipients seek advice specific to their circumstances from their financial advisor. **Korea:** Distributed in Korea by UBS Securities Pte. Ltd., Seoul Branch. This document may have been edited or contributed to from time to time by affiliates of UBS Securities Pte. Ltd., Seoul Branch. **Malaysia:** This material is authorized to be distributed in Malaysia by UBS Securities Malaysia Sdn. Bhd (Capital Markets Services License No.: CMSL/A0063/2007). This material is intended for professional/institutional clients only and not for distribution to any retail clients. **India:** Distributed by UBS Securities India Private Ltd. (Corporate Identity Number U67120MH1996PTC097299) 2/F, 2 North Avenue, Maker Maxity, Bandra Kurla Complex, Bandra (East), Mumbai (India) 400051. Phone: +912261556000. It provides brokerage services bearing SEBI Registration Numbers: NSE (Capital Market Segment): INB230951431, NSE (F&O Segment) INF230951431, NSE (Currency Derivatives Segment) INE230951431, BSE (Capital Market Segment) INB010951437; merchant banking services bearing SEBI Registration Number: INM000010809 and Research Analyst services bearing SEBI Registration Number: INH000001204. UBS AG, its affiliates or subsidiaries may have debt holdings or positions in the subject Indian company/companies. Within the past 12 months, UBS AG, its affiliates or subsidiaries may have received compensation for non-investment banking securities-related services and/or non-securities services from the subject Indian company/companies. The subject company/companies may have been a client/clients of UBS AG, its affiliates or subsidiaries during the 12 months preceding the date of distribution of the research report with respect to investment banking and/or non-investment banking securities-related services and/or non-securities services. With regard to information on associates, please refer to the Annual Report at: http://www.ubs.com/global/en/about_ubs/investor_relations/annualreporting.html

The disclosures contained in research documents produced by UBS Limited shall be governed by and construed in accordance with English law.

UBS