

First Read

UniCredit

Placement of 10% of Pekao

Second placement in two days

Following the [placement of 10% of Fineco](#) on Monday, UniCredit placed on Tuesday 10% of Pekao, its listed Polish subsidiary, taking its stake down to 40% though still retaining control. Given the size of the asset and the possibility of reducing its holding further, the strategic reading of Pekao's disposal is less clear compared with Fineco, where we expect UCI to keep majority. We remain on the sidelines given the early stage of the strategic review and not being entirely sure about why these two disposals have been carried out with such immediacy, though we recognise Pekao's sale as another sign of proactivity by the incoming CEO to reduce the size of a potential capital increase.

Moderate capital benefit, but another sign of proactivity

Pekao will continue to be fully consolidated both for accounting and regulatory purposes. We estimate a c12bps capital benefit, coming in similar amount from capital gain (including goodwill reabsorption) and inclusion of new minorities into regulatory capital (likely using a 12% FL CET1 threshold). Implying a Q116 pro-forma FLCET1 ratio of 11.15% (UBSe 10.65%), the capital benefit is not large enough to change UCI's solvency position even when combined with Fineco (8 bps), but helps accelerating an otherwise slow capital formation, and again will likely be seen as a sign of new management's willingness to address the bank's solvency debate. A more bearish reading might suggest UCI's capital position has deteriorated recently and these two disposals are an offset ahead of EBA's stress test.

What a potential full disposal of Pekao would mean

Placing a 10% stake has a clear signalling effect for UCI but also for Pekao, as this will likely prove an overhang for the shares and therefore could hinder UCI's ability to generate attractive capital gains on any additional sale. Assuming a sale at the (estimated) tangible carrying value of the stake, capital benefit should raise to c60bps, with the real benefit of a full disposal being the deconsolidation of €25-30bn RWAs (6-7% of total). This would reduce the 2017E capital shortfall in our valuation by €2.5bn (to €3bn). However, adjusted ROTE would drop to 3.9% (Pekao accounts for 13% of 17E Group earnings), implying moderate enhancement to our valuation.

Valuation

UCI trades on 0.29x PTBV and 6.0x PE17E. Our Gordon growth-derived €2.10 PT is based on 4.3% adjusted ROTE17E, 12% COE and €5.3bn capital shortfall.

Equities

Italy
Banks, Ex-S&L

12-month rating **Neutral ***

12m price target **€2.10**

Price **€2.10**

RIC: CRDI.MI BBG: UCG IM

Trading data and key metrics

52-wk range	€6.38-1.75
Market cap.	€12.7bn/US\$14.0bn
Shares o/s	5,967m (ORD)
Free float	100%
Avg. daily volume ('000)	119,785
Avg. daily value (m)	€312.9
Common s/h equity (12/16E)	€49.4bn
P/BV (12/16E)	0.3x
Tier 1 ratio	11%

EPS (UBS, diluted) (€)

	UBS	Cons.
12/16E	0.28	0.36
12/17E	0.35	0.48
12/18E	0.44	0.57

Ignacio Cerezo

Analyst

ignacio.cerezo@ubs.com

+44-20-7568 4409

Francesco Di Giambattista

Analyst

francesco.di-giambattista@ubs.com

+44-20-7568 1070

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/POP (diluted)	2.8	3.9	4.0	1.5	1.5	1.3	1.3	1.2
P/BV x	0.5	0.7	0.7	0.3	0.3	0.2	0.2	0.2
P/BV (UBS) x	0.6	0.8	0.8	0.3	0.3	0.3	0.3	0.3
P/E (UBS, diluted)	(3.9)	15.5	19.5	7.5	6.0	4.7	4.0	3.8
Net dividend yield %	2.2	2.0	2.1	4.4	6.8	8.7	10.0	10.6

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 €2.10 on 12 Jul 2016 21:34 BST

Forecast returns

Forecast price appreciation	0.0%
Forecast dividend yield	6.8%
Forecast stock return	+6.8%
Market return assumption	5.0%
Forecast excess return	+1.8%

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 12%. To determine whether banks have excess or shortfall of capital, which we value at 1x PTBV, we use a 12% fully loaded CET1 threshold, thus reflecting UniCredit's GSIB buffer.

Risks: UniCredit is exposed to macro risks, asset quality risks, unexpected changes in interest rates, slow-down of the saving industry, developments in CEE, regulatory and operational risks and potential M&A activity with positive or negative implications for shareholders.

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Buy	FSR is > 6% above the MRA.	47%	32%
Neutral	FSR is between -6% and 6% of the MRA.	38%	25%
Sell	FSR is > 6% below the MRA.	15%	21%
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 30 June 2016.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
UniCredit ^{2, 3, 4, 5, 7, 20}	CRDI.MI	Neutral (CBE)	N/A	€2.10	12 Jul 2016

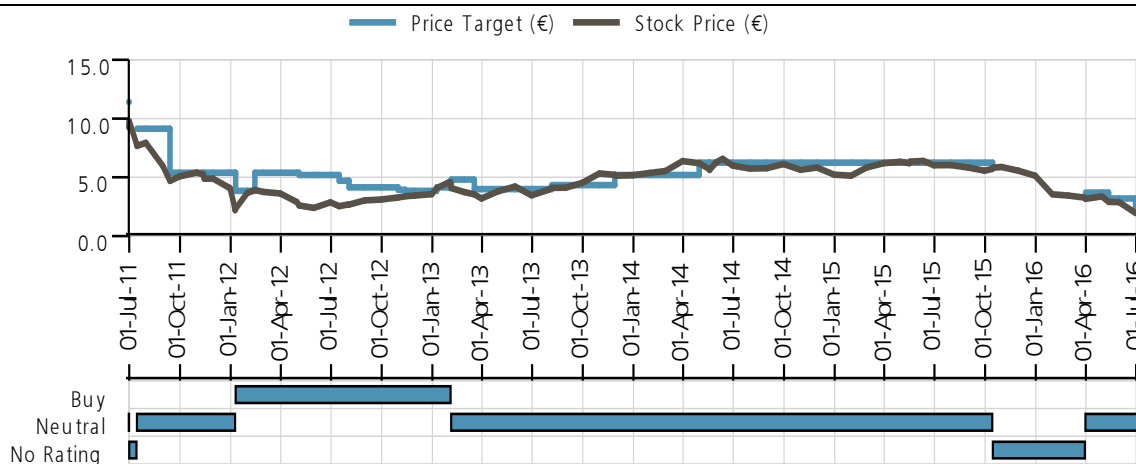
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UniCredit (€)



Source: UBS; as of 12 Jul 2016

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