Stock Pitch - Intesa Sanpaolo

Financials Sector

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March 11th, 2014

DESAUTELS Capital Management
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Investment Thesis

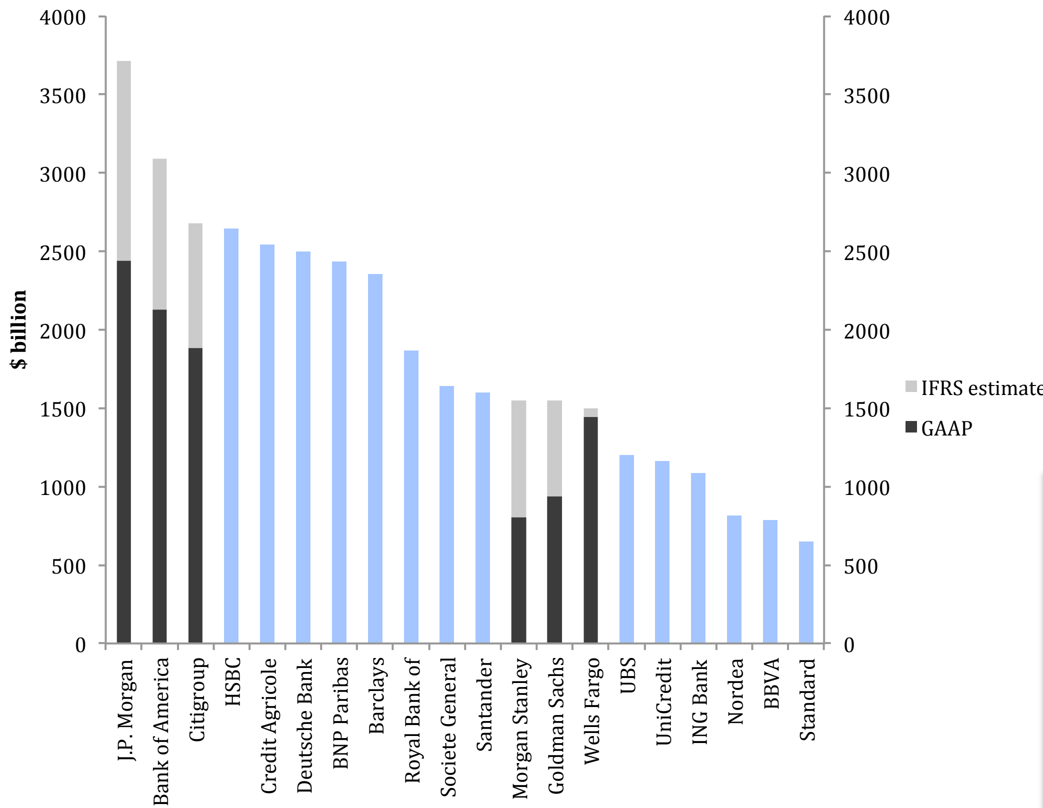
Investment Thesis

Macro Focus: Europe	• European macro situation at a turning point: recovery in view • European banks are better capitalized and stronger fundamentally than the market expects: especially when adjusting for the traditional comparison to American banks • Given the observed discrepancies between bank valuations in different sovereign nations, it seems as though strong banks in weak economies make have been punished more than they deserved
Intesa Sanpaolo: Strong Fundamentals	• Asset Quality Review Tests: we see the upcoming ECB Comprehensive Assessment as a catalyst for the market to give credit to Intesa for its relatively strong capital positions • Strong fundamentally with better than peers efficiency and capital ratios • Positive EPS growth prospects due to – Increase in fees and commissions – Better cost cutting efforts – Cheaper funding mix
Valuation	• Lower-tier bank multiples have the potential to expand to mid-tier and even high-tier levels in the medium term given the signs of a European recovery – Intesa continues to trade at an unwarranted discount to its peers on P/B and P/TB multiples • DDM supports the value proposed by Intesa's dividend to equity holders • **DCM Financials Team price target: €2.94 representing a 29% upside**

Industry Review Summary

European Vs American Banks: Apples to Apples

Differing accounting policies



Differences between GAAP and IFRS cause large changes in stated total bank assets – affecting the perceived capital adequacy of American vs. European banks

- Non-adjusted, US banks seem much more safe than EU banks on almost all metrics…
- … however, when adjusted as under IFRS, data shows a different story: US Banks have a tier 1 leverage ratio of 4.30%, and EU banks a 3.86% leverage ratio – including banks with very low ratios such as Deutsche Bank and UBS. ***If excluded, EU ratios are almost as strong as US ratios***

Altogether, the EU banking assets are much larger than their US counterparts mainly because of the euro-area reliance on bank loans rather than capital markets. Growth prospects in GDP and housing would then positively affect earnings outlooks of the banks

Further, it seems as though a deeper look into EU capital ratios and safety characteristics show similar ratios to the main US banks

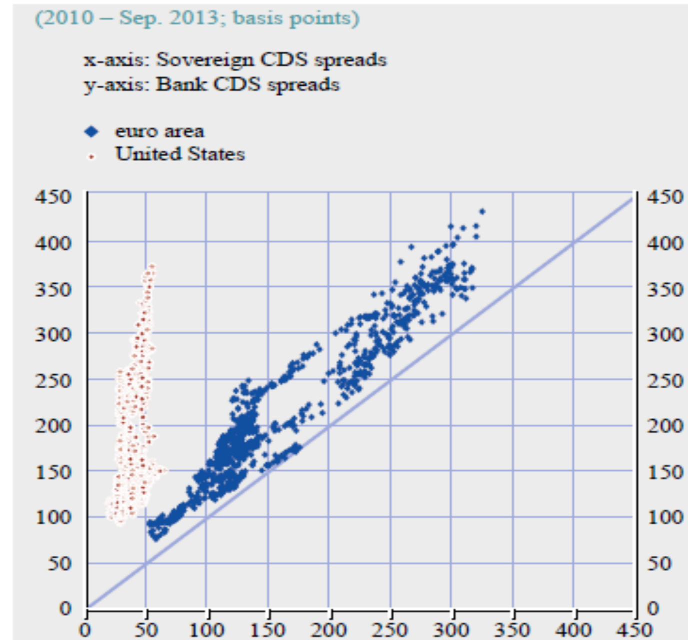
European Vs American Banks: Apples to Apples

CDS Spreads of European & American banks against their respective Sovereign CDS spread

- European Bank CDS spreads exhibit a high correlation to their respective Sovereign CDS spreads (0.91 correlation)
  - American Banks, on the other hand, exhibit no correlation whatsoever
- Indicates a market perception that as default risk increases in a specific country, the default risk of that country's main banks also increases
  - However, most of the large institutions have global operations, and should not be overly dependent on their country of origin
- A paper published by two researchers from University College of Dublin analyzed this relationship further: they suggest that ***sovereign CDS spreads "incorporate more timely information on the default probability of European banks than their corresponding bank CDS Spread"***, and therefore may be better indicators of the actual health of the bank

Altogether, it would seem as though a strong, global bank in a weak – yet improving – economy would have overvalued risk, and could provide significant upside

Sovereign and Bank CDS Spreads: two sides of the same coin?, David Avino & John Cotter

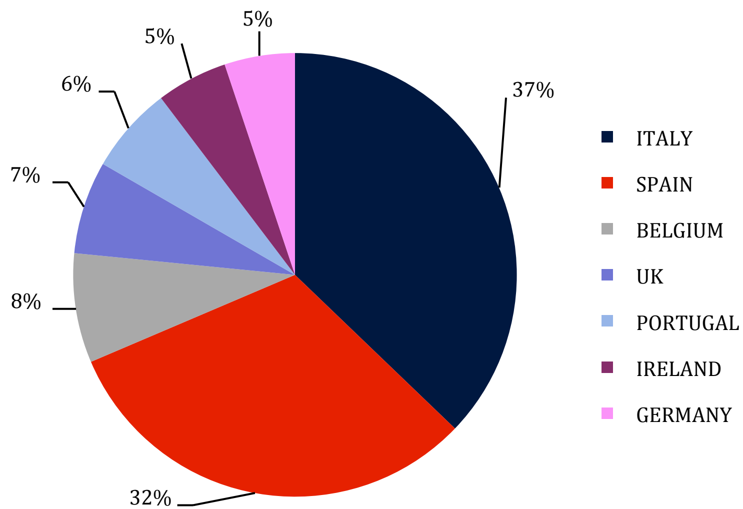


Source: Bloomberg.
Note: Average CDS spreads for euro area and US large and complex banking groups (LCBGs) and countries where LCBGs are located (Belgium, France, Germany, Italy, Spain and the Netherlands).

Banking Structures Report, November 2013, ECB

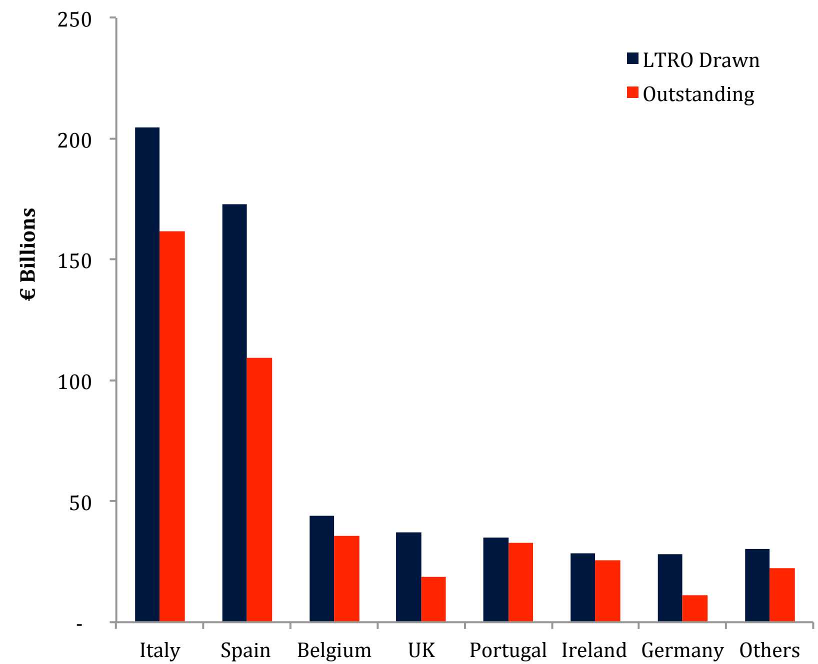
Long-Term Refinancing Operation

LTRO Initially drawn by Country



Source: ECB + Bloomberg

LTRO drawn vs. outstanding by Country



Source: ECB + Bloomberg

Short-term implication for LTRO repayment

LTRO Outstanding by bank

Description	Total LTRO Originally Drawn (EUR)	Outstanding Amount (EUR) - Jan 2014
ITALY		
Intesa Sanpaolo SpA	36,000	-
Banca Monte dei Paschi di Siena SpA	29,000	29,000
UniCredit SpA	26,100	21,100
Cassa Depositi e Prestiti SpA	26,000	26,000
Banco Popolare SC	13,500	13,500
Iccrea Banca SpA	12,600	12,600
Unione di Banche Italiane SCPA	12,000	12,000

Description	Total LTRO Originally Drawn (EUR)	Outstanding Amount (EUR) - Jan 2014
SPAIN		
Santander	37,476	6,476
BBVA	20,000	-
CaixaBank	11,000	3,000

Source: ECB + Bloomberg

- In Italy only Intesa San Paolo repaid in fully the ECB loan
- Focus will be on MPS (risk of nationalization) and main second tier banks (UBI, Banco Popolare)
- In Spain, major lenders have almost repaid their loans. The outstanding € 109B LTRO loans has to be repaid by small regional banks

We expect consolidation in the banking sector of both Italy and Spain. Middle size banks can be squeezed and face liquidity constraints in the medium-long term

Positioning European Banks

Banks	Basel III	ROE	NPL	Cost/Income	Country
Healthy Institutions					
Svenska Handelsbanken AB	18.8%	14.4%	0.4%	47%	
Swedbank AB	18.0%	13.4%	1.2%	44%	
Skandinaviska Enskilda Banken	15.0%	11.5%	1.2%	54%	
Nordea Bank AB	14.6%	11.5%	2.0%	49%	
DNB ASA	12.5%	11.1%	2.2%	47%	
Credit Suisse Group AG	10.2%	10.6%	0.7%	78%	
Average Institutions					
Danske Bank A/S	12.2%	8.1%	6.8%	60%	
KBC Groep NV	12.5%	14.0%	8.1%	53%	
BNP Paribas SA	10.8%	9.1%	6.5%	66%	
UBS AG	11.9%	4.0%	0.6%	87%	
HSBC Holdings PLC	10.6%	5.0%	3.8%	55%	
Deutsche Bank AG	9.7%	5.5%	2.6%	80%	
Societe Generale SA	9.9%	7.0%	6.5%	70%	
Struggling Institutions					
Barclays PLC	8.4%	11.8%	5.7%	66%	
Banco Bilbao Vizcaya Argentari	8.4%	7.8%	5.7%	51%	
Commerzbank AG	8.6%	0.0%	7.5%	73%	
Erste Group Bank AG	10.0%	8.7%	12.2%	57%	
Intesa Sanpaolo SpA	11.2%	3.0%	12.9%	51%	
Lloyds Banking Group PLC	9.9%	2.2%	8.7%	51%	
Royal Bank of Scotland Group P	9.1%	1.3%	9.1%	66%	
Unicredit SpA	9.8%	1.7%	14.9%	61%	

Macroeconomic Focus: Europe

Bulls

- Potential Acquisitions and consolidation as a result of assessment test
- EU banks exhibit similar capital ratios as American counterparts; perhaps safer than the market believes
- An analysis of the correlations between European Sovereign and Company CDS Spreads indicates an investment opportunity for a strong bank in a weak economy
- Bank margins increase as tapering carry-over affects long-term yields
- ECB rate cut adds stability

Bears

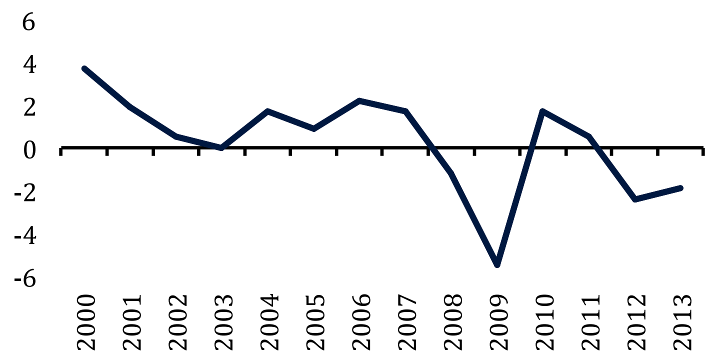
- Tough tests may lead to the extinguishing of several European banks
- 2014 reviews and expectations seem to lead to less bank lending
- ECB's leverage targets could require further deleveraging: still low ratios & compressed NIMs
- Spain, Italy new business lending rates remain high; non-encouraging for growth
- Outstanding LTROs pose significant interest rate risk as a rise in yields will decrease the size of the balance sheet

A strategic focus on strong banks in troubled economies would allow DCM to capitalize on the key themes of 2014

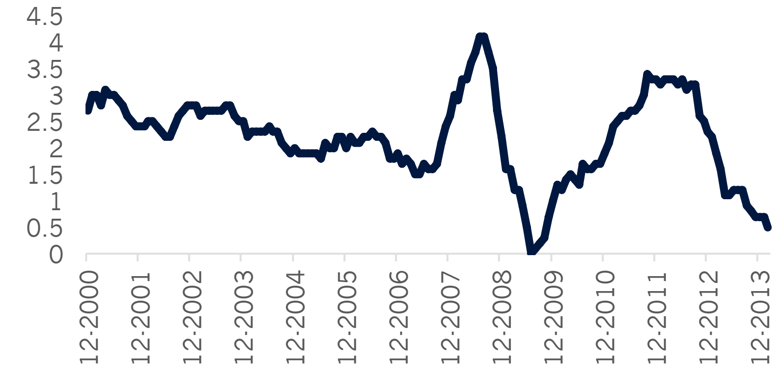
Macro Overview: Italy

Main Macro Economic Indicators

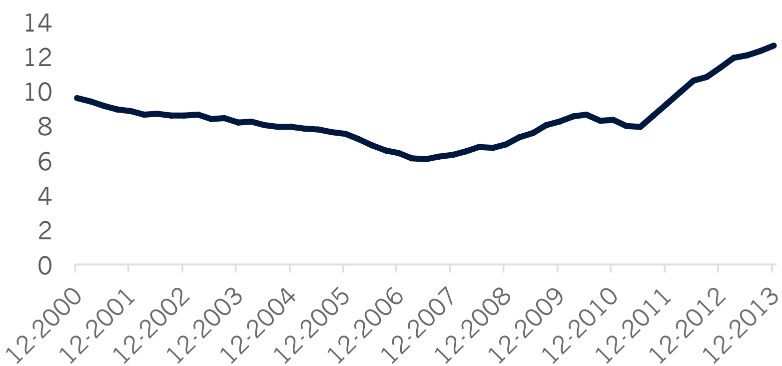
GDP Growth (% YoY)



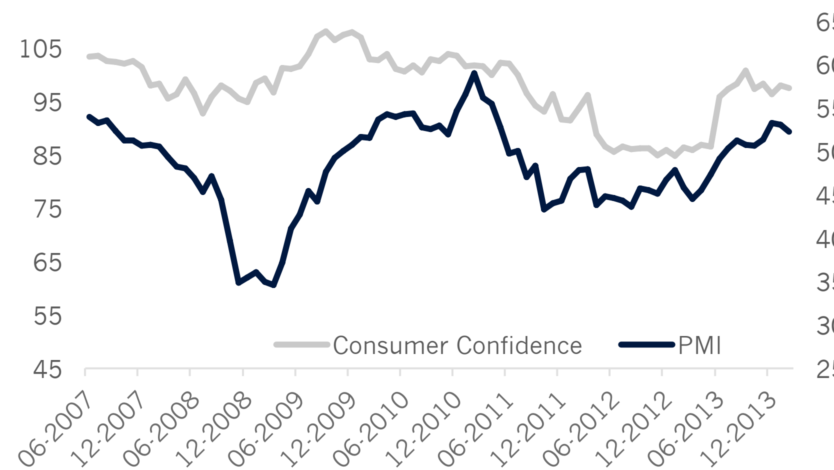
CPI (excl. Tobacco) (% MoM)



Unemployment Rate (% MoM)



PMI and Consumer Confidence



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Evolution of Italian political environment

Berlusconi	Technocrat Government: Monti	Monti's resignation	New Elections	Prime Minister: Letta	Prime Minister: Renzi




...for almost 20 years	Nov 2011	Nov 2012	Feb 2013	March 2013	Feb 2014

Main results:
- Decline in competitiveness
- Lack of implementation of structural reforms
- ...a lot of bunga bunga!!!

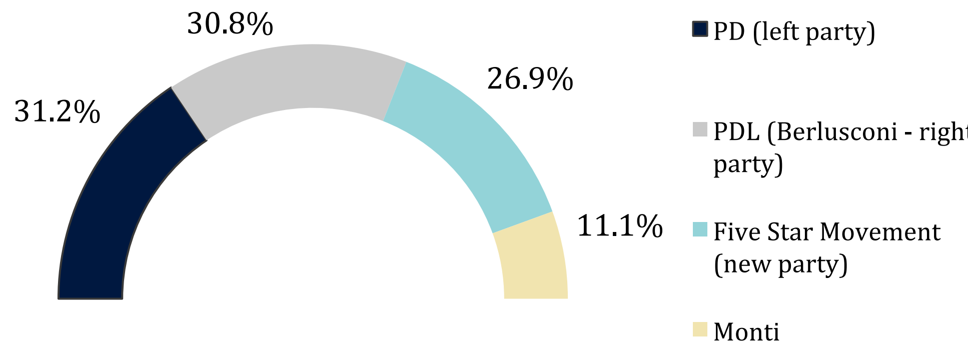
Main results:
- Tax increase
- Austerity, austerity, austerity…

Main results:
- No outright majority
- Fragile stability based on coalitions

Main results:
- ....almost none!

… fragmented results from election in 2013

Overall results (Lower + Upper House)



Prime Minister: Letta

<u>Main results:</u>

- PD gained clear majority of seats in the Lower House
- no clear majority in the Upper House

<u>Solutions:</u>

- New elections
- "Extended coalition" (left + right)

2014: a new prime minister… a new light at the end of the tunnel

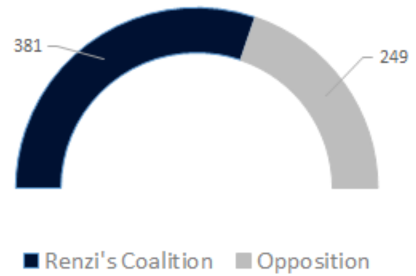
On 24 Feb 2014 Renzi became the new Prime Minister

WHAT'S NEW?

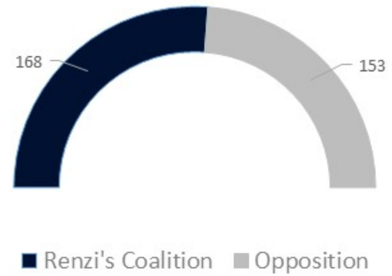
1. Youngest ever Prime Minister (39 years old)
2. First to become Prime Minister without being Member of the Parliament
3. No clear connection with the existing leading parties in Italy
4. Clear agenda of reforms to be implemented
5. More open and able to speak directly to the citizens

Still with a narrow majority on the Upper House (only 7 votes…..)

Lower House



Upper House



<u>Challenging but this will be the last opportunity for Italy…. therefore we are optimistic on the future Italian political stability</u>

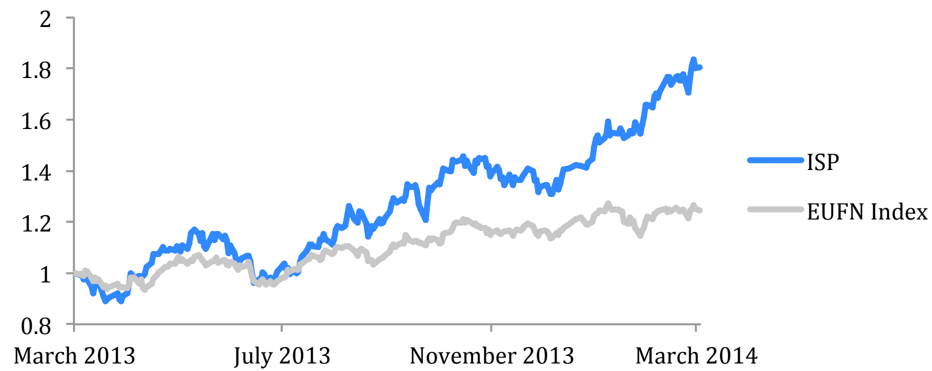
Overview of Selected Opportunities

Company Profile

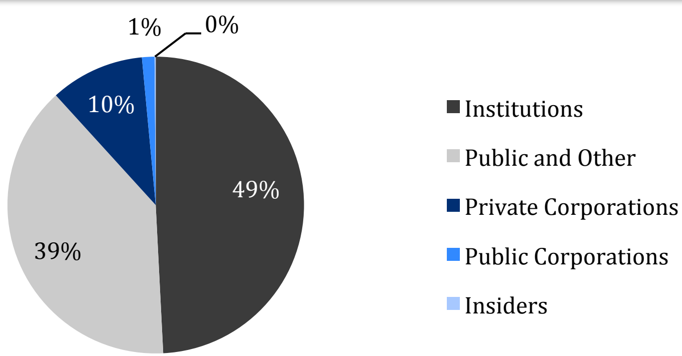
Company Profile

- Operates in 5,302 branches in Italy, 1,332 branches in rest of Europe and 207 branches internationally.
- 94,157 full-time employees
- Banking leader in Italy
- Head office in Turin, Italy
- S&P Credit Rating: BBB

Share Trading Performance LTM



Ownership Breakdown



Management

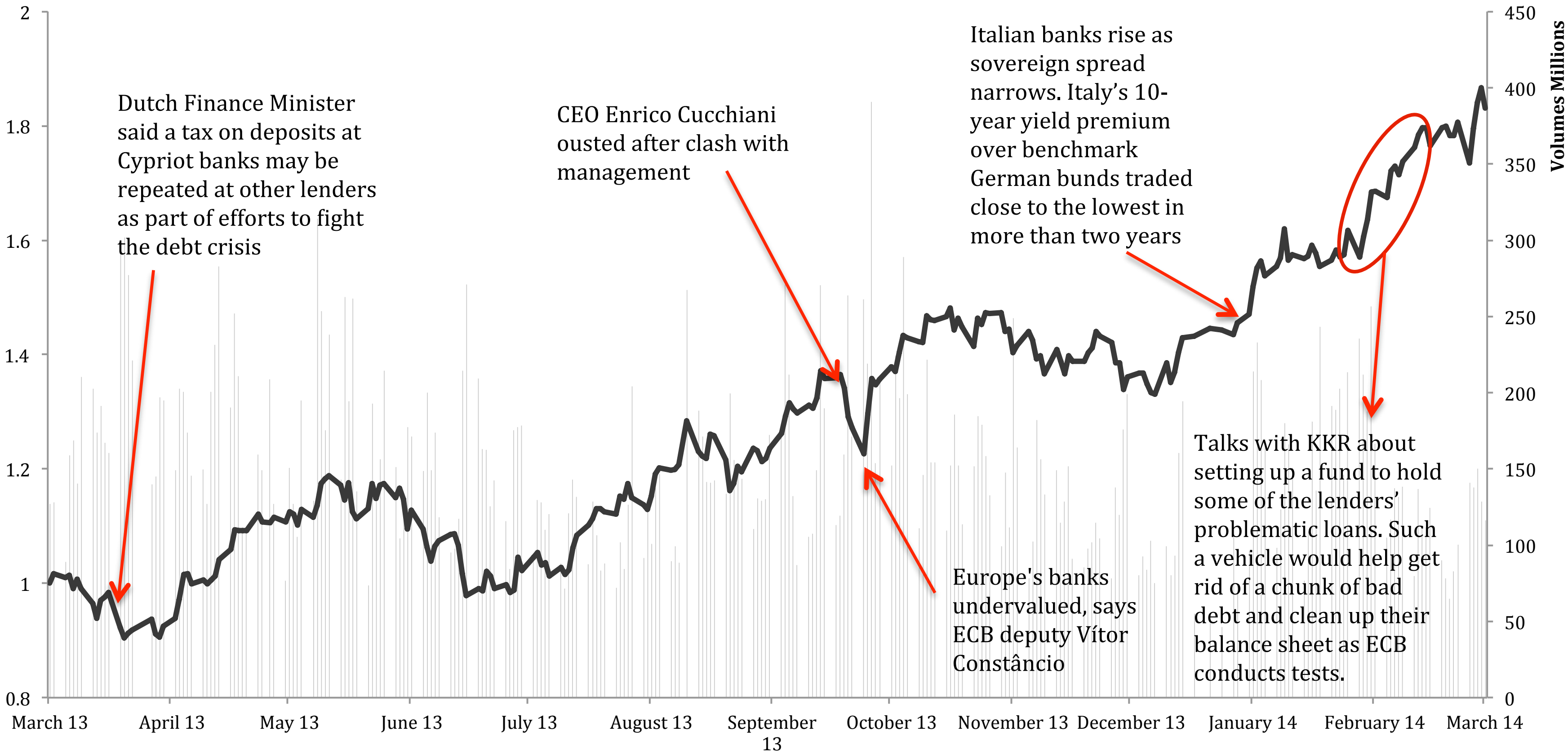
Carlo Messina – CEO since September 2013

- Began professional career in the Finance department of Banca Nazionale del Lavoro in 1987
- Joined Intesa's predecessor Banco Ambrosiano Veneto in 1995 as Manager in charge of the Planning Department

Giovanni Bazoli – Chairman of the Supervisory Board since January 2007

- Lawyer, Professor of Administrative law and institutions of public law until 2003

Stock Trading Analysis



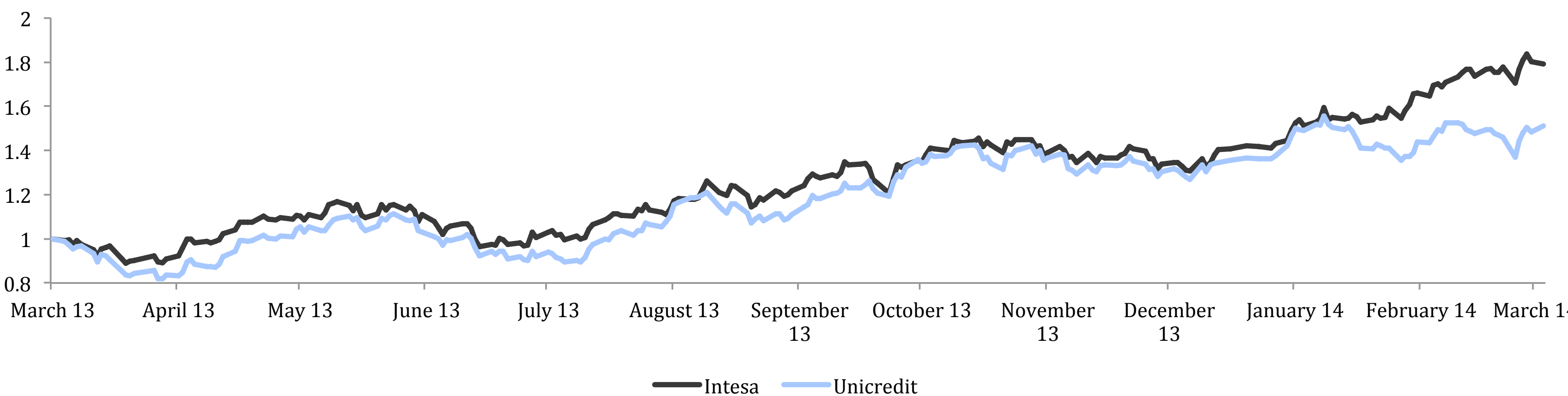
Company Description

INTESA SANPAOLO

- One of the best "cost-cutter" in Europe with a cost-income ratio of 49% (against a staggering 63% at UCG)
- High penetration of investment services with Italian market share of AUM at 18% (vs. 8% for UCG)
- Stronger capital ratios and already repaid LTRO to ECB
- Offers an attractive 1.6% yield and trades at 0.74x P/TB

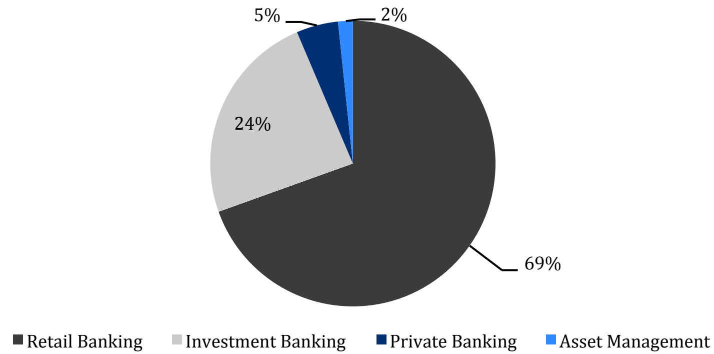
UniCredit

- Strongest Italian NIM at 1.46% (vs. 1.22% for ISP)
- More to gain from repricing of high-cost liabilities in terms of fixed term retail deposits
- Still has a long way to go in terms of share price performance to reach pre-2011 levels
- Offers a yield of 1.5% and trades at 0.73x P/TB

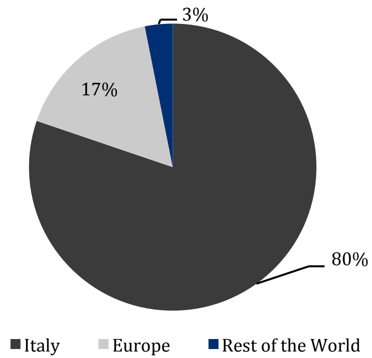


Company Operations

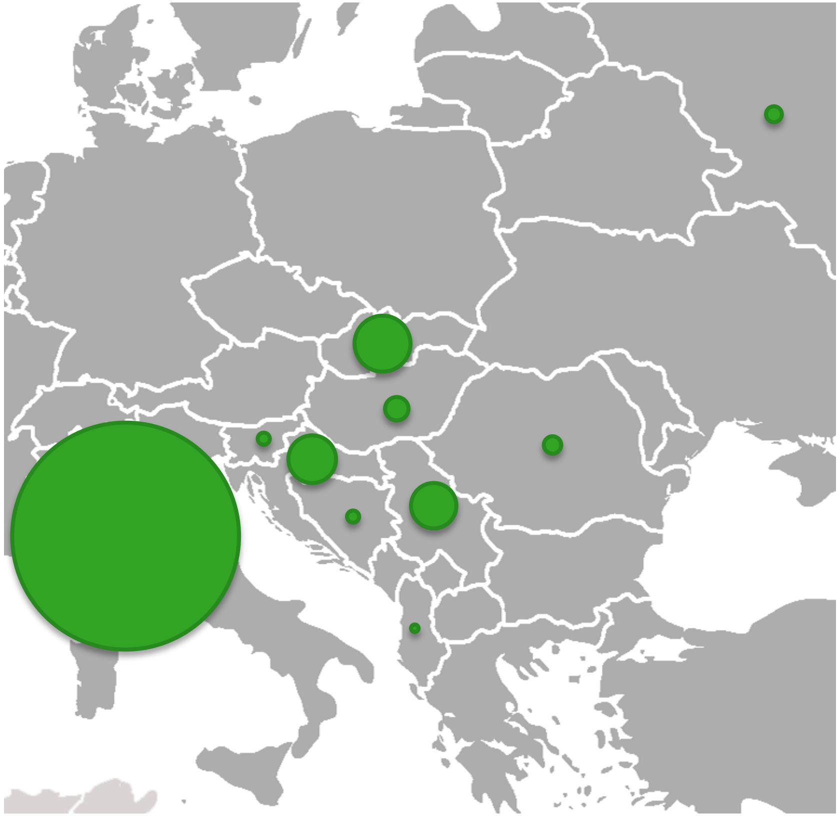
Revenue by Segment



Revenue by Country

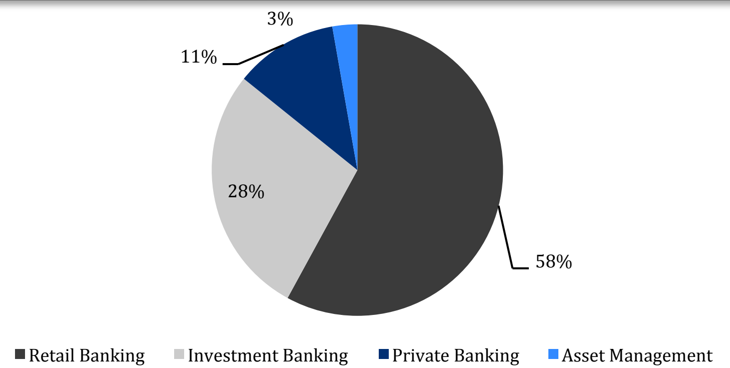


INTESA SANPAOLO

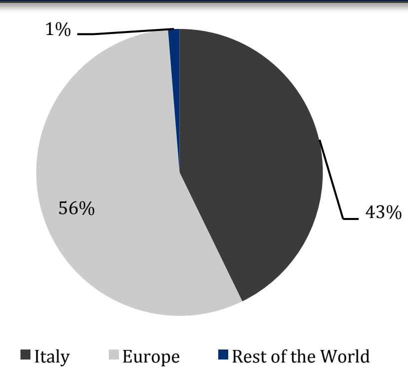


Company Operations

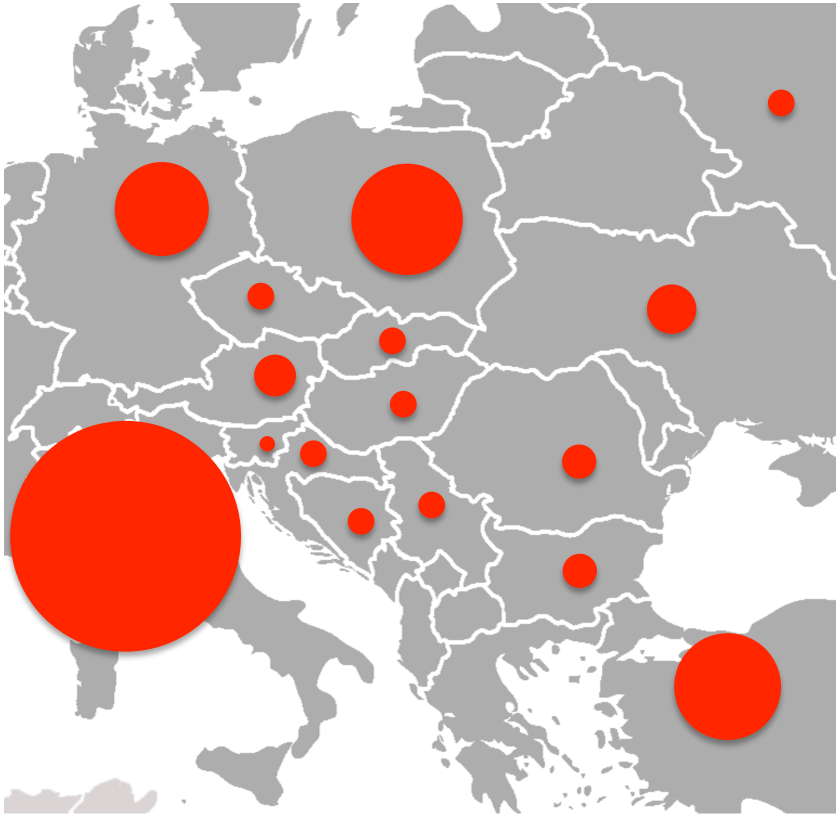
Revenue by Segment



Revenue by Country

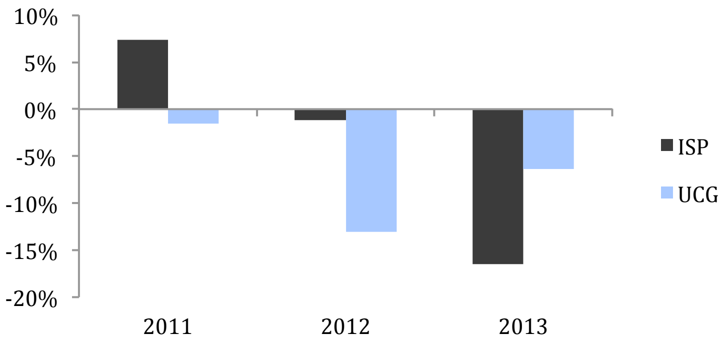


UniCredit

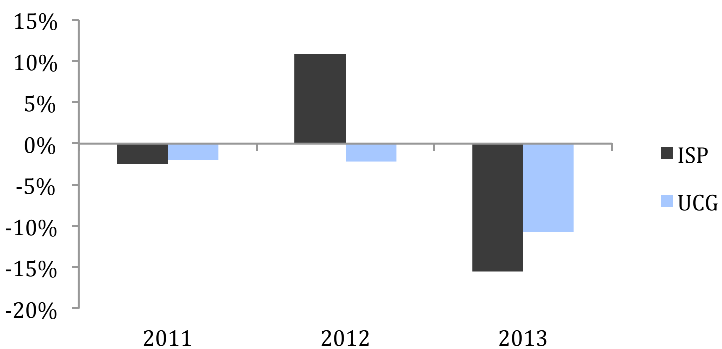


Revenue Trend 1/2

Net Interest Income decline



Net Revenue decline

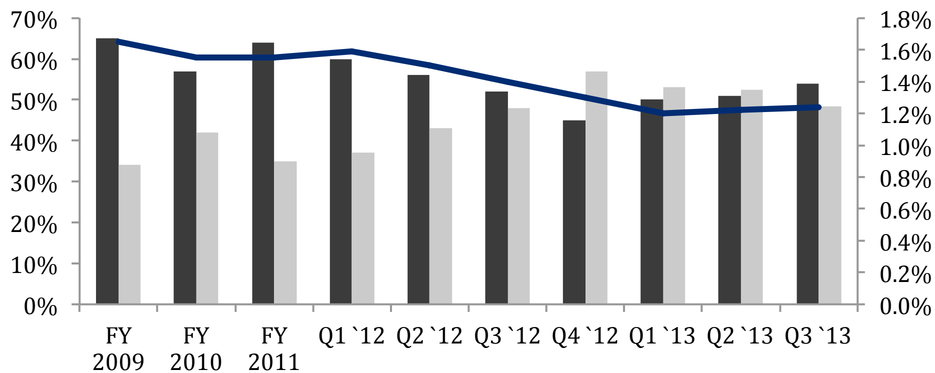


Highlights

- Top line declines associated with:
  - Funding pressures
  - Continued deleveraging
  - Declining benchmark rates (Euribor)
  - Overall decline in economic activity
- Net interest income has been declining at an average of 8% YoY for each of the three years since 2011
- Net revenue performed somewhat better, though partly due to one-off trading gains at both companies. Has been declining at an average of 3% YoY for each of the three years since 2011
- Keep in mind these are recession years in Europe

Revenue Trend 2/2

Net Interest Income broken down



Sub-components of NII

- Overall, NIM declined YoY driven by both a reduction in loan yields as well as an increase in funding costs
- Customer margin (defined as the margin on loans to customers) declined 25bp YoY, while the financial operations margin (defined as the margin on the non-customer loan related activity, including hedging activities) actually increase, but not enough to offset the declining customer margin fall
- In effect, the contribution of financial operations to NII has been increasing over time

EPS growth drivers in the medium term

Continued loan deleveraging should be more than offset by

1. **Increase in fees and commissions**
2. **Better cost cutting efforts**
3. **Cheaper funding mix**

Fees and commissions 1/2

Non-Interest Income growth

- In a period of deleveraging and a zero interest rate environment (ZIRP), Intesa looks toward growing other income line:
  - Fees
  - Commissions
  - Trading

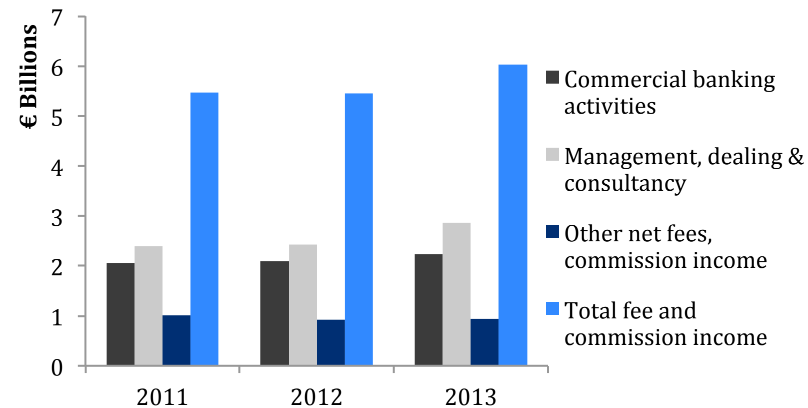
- Unlike Unicredit, they have been able to increase non-interest income by 10.7% YoY, where Unicredit's fees were flat YoY

- Part of this performance is due to Intesa's ability to take advantage of increasing demand for investment products, namely Mutual Funds

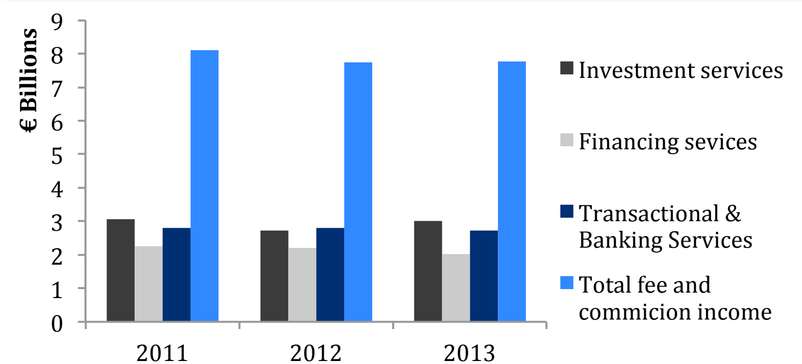
Intesa's market share of mutual funds in Italy: 18%

Unicredit's market share of mutual funds in Italy: 8%

Intesa

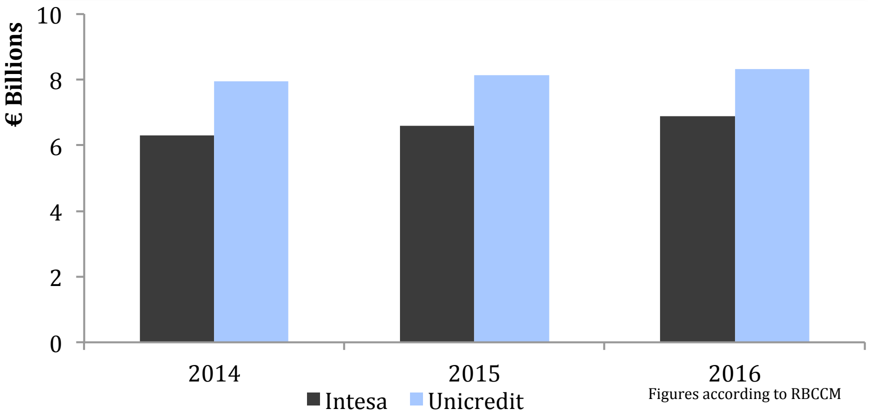


Unicredit



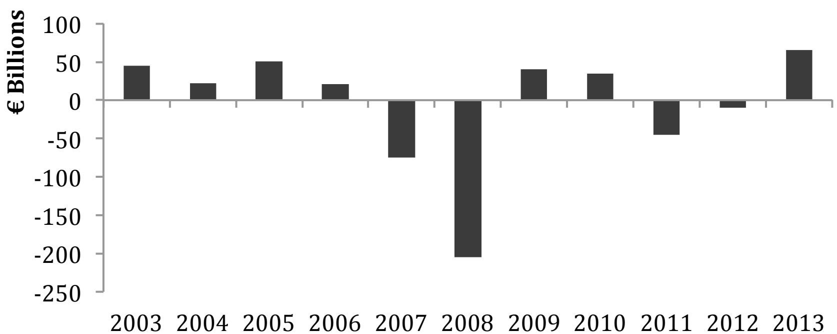
Fees and commissions 2/2

Expected Growth of Total Fee and Commission Income



Figures according to RBCCM

Italian Mutual Funds

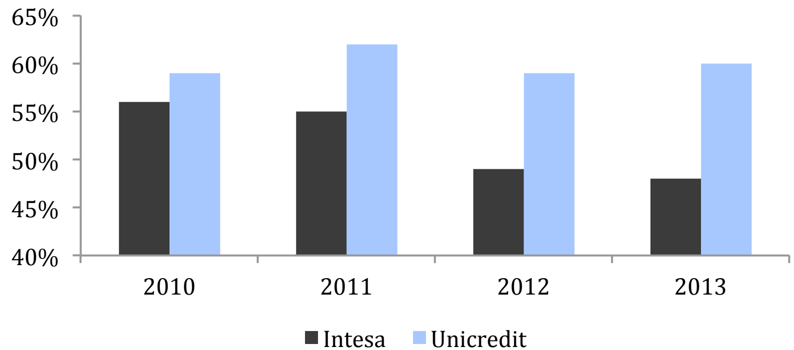


Highlights

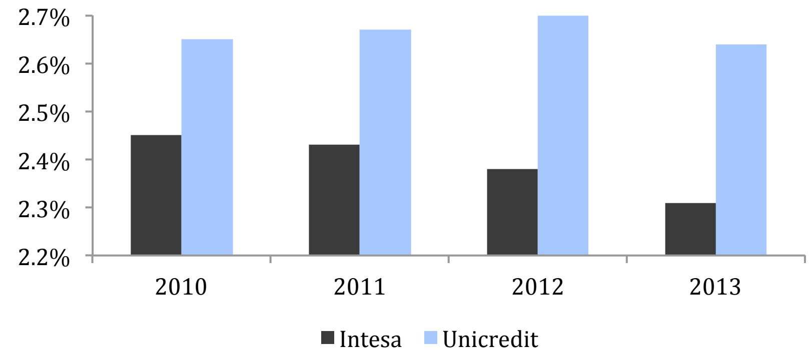
- Based on current trends and historical performance, Intesa's fee income is expected to grow at 4.5% CAGR from 2014-2016, whereas Unicredit's is expected to increase at 2.6% CAGR
- Intesa is in a better position to leverage its operations to further increase its fee income line
- A similar notable episode that combined both debt deleveraging and ZIRP occurred in Japan starting in 1999; during the first three years of this period, Japan's banks' net fees increased by 8%, though one bank increased its fees by as much as 23%
- In 2013, Italian mutual funds have seen inflows of €64.9bn, their highest inflows in the past ten years. Intesa's higher market share in mutual funds should help it capitalise on this trend

Cost cutting efforts 1/3

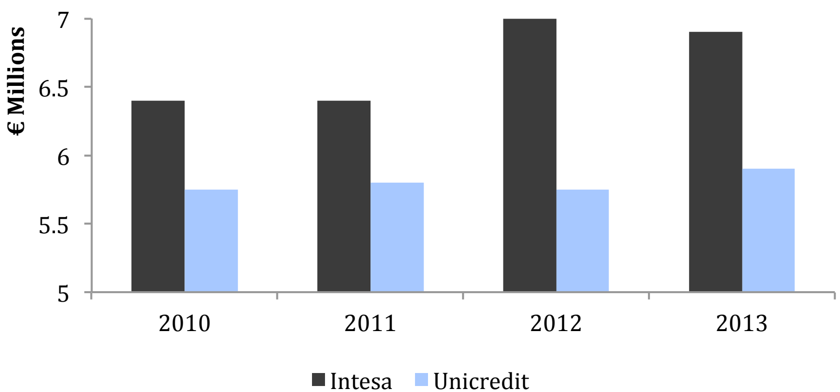
Cost/Income ratio



Cost/Loan ratio



Employee productivity € (Asset/# of employees)



Highlights

- With most of its operations in Italy, Intesa is able to achieve better economies of scale across its major market
- As shown in the top right graph, Intesa's cost/income ratio stood at 49.8% whereas Unicredit's was 60.6%
- Similar story when comparing the banks on the cost/loan metric where Intesa remains more cost effective than its peer

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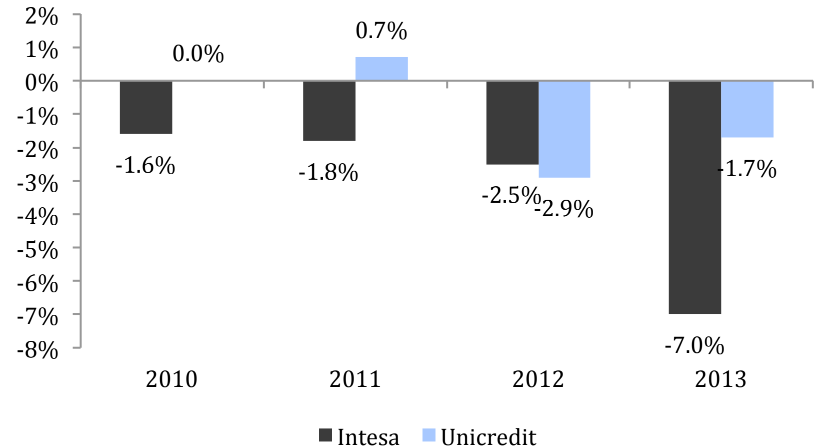
Cost cutting efforts 2/3

Cost cutting efforts and lack of productivity

- In the current environment, both management teams are committed to making cost adjustments one of the key drivers of EPS growth
- As shown in the graph to the left, Intesa's management showed more discipline on costs, achieving an average yearly decline of 5.5% compared to Unicredit's 3.3% yearly figure
- Italian retail banking remains relatively inefficient. We see a potential for increasing efficiency for Italian banks should its productivity converge towards the Eurozone average

Intesa is a better cost-cutting bank

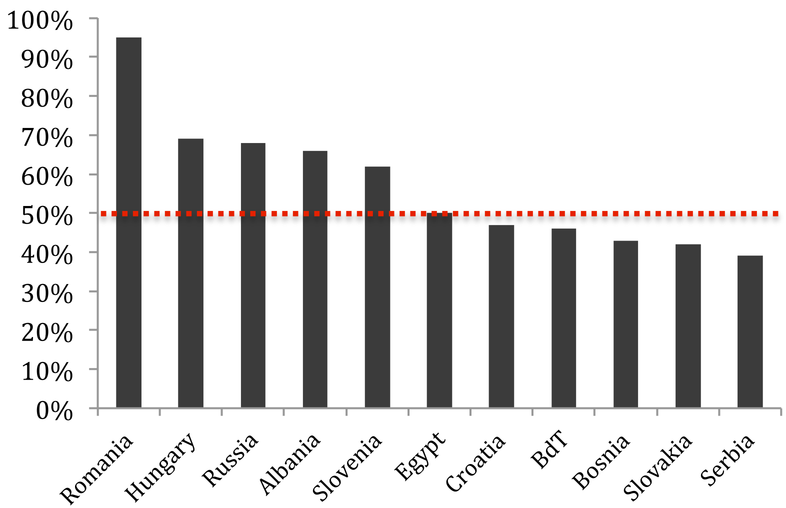


2012	Customers per branch	Assets per bank employee
Italy	1,871	€ 13,604.00
Euro area	1,945	€ 15,076.00
Western Europe best in class	6,793	€ 24,080.00

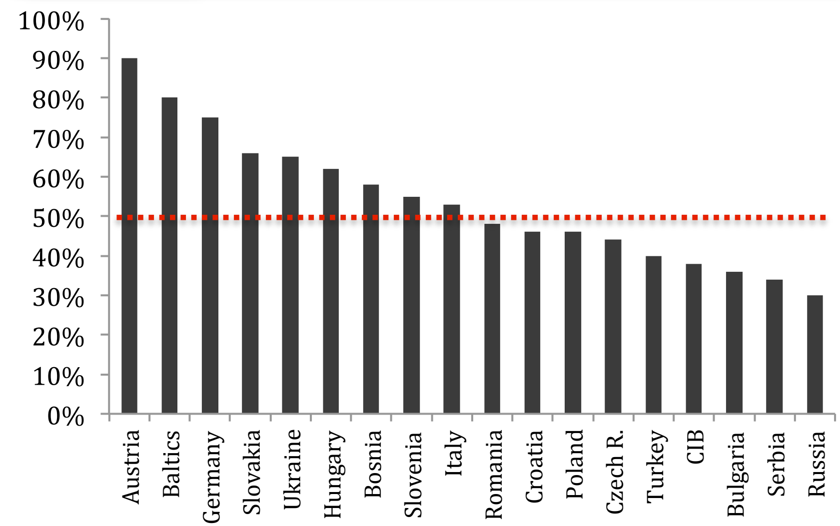
Productivity	Customers per branch	Assets per bank employee	Average
Italy vs Euro Zone	-3.8%	-9.8%	-6.8%
Italy vs Western Europe best in class	-72.5%	-43.5%	-58.0%

Cost Cutting Efforts 3/3

INTESA SANPAOLO



UniCredit

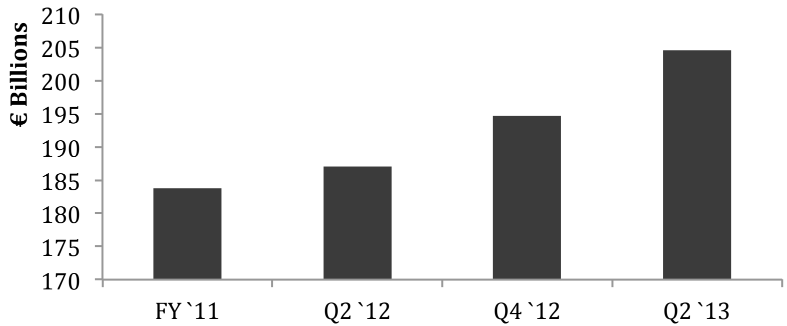


Intesa is in a stronger position to capitalize on cost-cutting efforts due to geographic mix

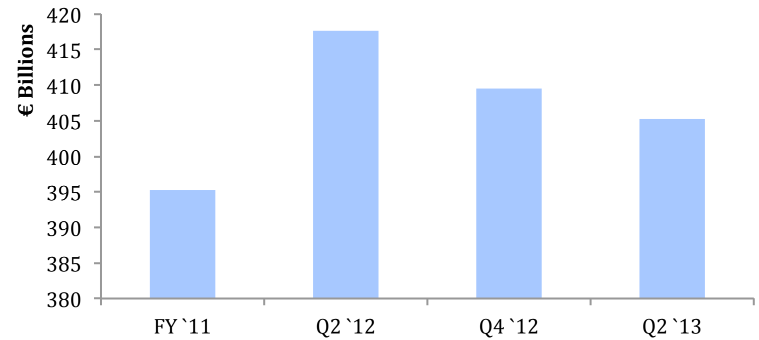
- With most of its operations in Italy, Intesa is able to achieve better economies of scale across its major market
- UniCredit's footprint requires a more fragmented cost base
  - UCG derives most of its income from "high-cost" countries → high structural costs

Liabilities: Intesa has a cheaper funding mix

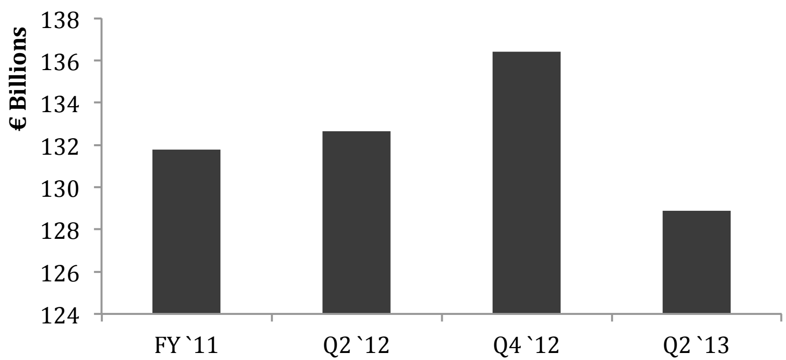
Intesa Current accounts and deposits



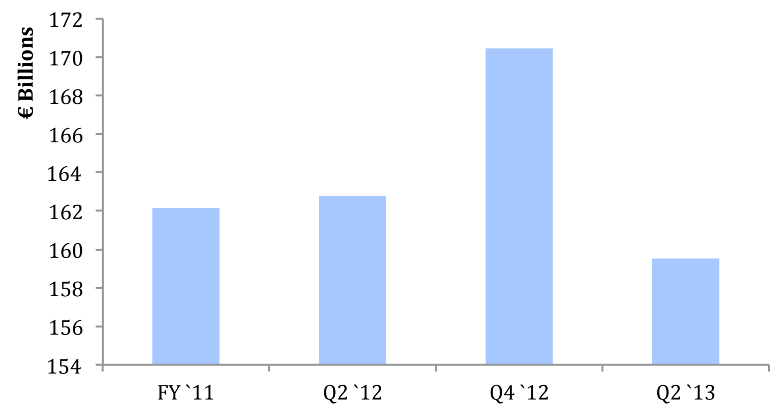
Unicredit Current accounts and deposits



Intesa Bonds

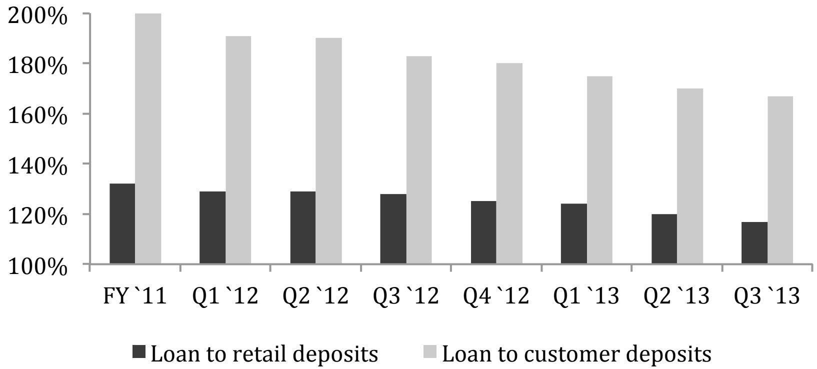


Unicredit Bonds



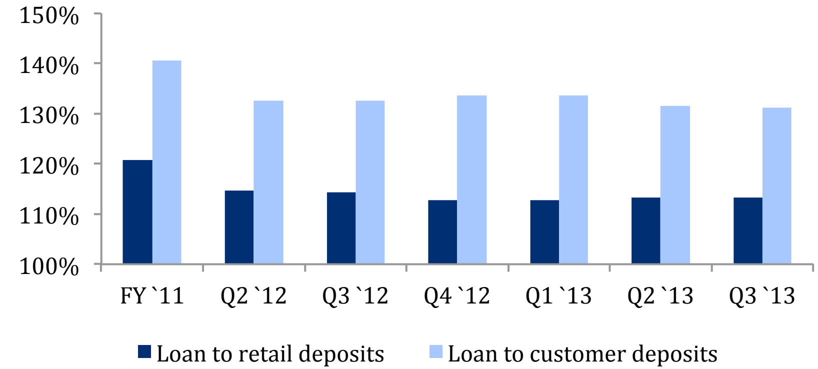
Liabilities: Intesa's loan-to-deposit ratios are improving faster

Intesa LTD ratio



- Intesa's Loan to retail deposits has decreased 15% over the past two years, mainly driven by an increase in deposits. This figure includes retail bonds, a feature of Italian banks where retail bonds are distributed as savings products through branch networks that pay an interest rate closely linked to the Italian sovereign bonds
- Excluding retail bonds and counting only traditional customer deposits, the LTD ratio had decreased even more: 33%

Unicredit LTD ratio



- Unicredit's Loan to retail deposits has decreased 8% over the past two years. This figure is significantly lower than Intesa's, confriming Intesa's stronger optimizing abilities
- Excluding retail bonds and counting only traditional customer deposits, the LTD ratio had decreased even more: 10%

Asset Quality Review/Stress Test

What is it?

- ECB's AQR will evaluate the asset quality of the bank's balance sheets using FY 2013 data to determine the size of NPL's using consistent parameters across countries
  - Definition of non-performing loans: every material exposure 90 days past due will be classified as non-performing even if not recognised as defaulted or impaired (EBA)
- Following the AQR, the banks will undergo a stress test to provide the regulator with information on the bank's ability to sustain losses under a number of stressed scenarios
- As announced by the ECB on February 3rd, the capital thresholds for the baseline and adverse scenarios will be **8%** and **5.5%** of Common Equity Tier 1 capital respectively
- The impact of the scenarios on the loss and default parameters will be calculated and will result in larger provisions

http://www.ecb.europa.eu/press/pr/date/2014/html/pr140203.en.html

Intesa appears more conservative

- The table below compares both the coverage ratio and Texas ratios for both Intesa and Unicredit
  - Coverage ratio: Banks ability to meet its financial obligations; the higher the coverage ratio, the better the ability of the bank to fulfill its obligations to its lenders.
  - Texas ratio: Banks nonperforming loans divided by the sum of tangible equity and existing loan loss provisions; a figure of 100% and above has historically been observed in banks who have low levels of capitalisation, provision levels or both
- As of Q3 '13, the cash coverage ratio is similar across the two banks; however, the Texas ratio at Unicredit is, at 100.7%, substantially higher than Intesa's 87.7%

Coverage ratio (Cash %)	Q1'12	Q3 `12	Q1 `13	Q3 `13
Intesa	43.1%	42.6%	43.3%	44.5%
Unicredit	43.6%	42.7%	44.2%	44.6%

Texas ratio (%)	Q1 `12	Q3 `12	Q1 `13	Q3 `13
Intesa	76.0%	81.8%	84.4%	87.7%
Unicredit	93.4%	97.1%	98.5%	100.7%

Stress Test Impact

Conservative CET1 Ratio of 9%

EURm

Q3 '13	Intesa	Unicredit
NPL	€55,503	€83,862
Coverage ratio	44.5%	44.6%
NPL ratio	14.7%	14.8%
Gross Loans	€377,113	€566,671
CET1 Capital (Basel III)	€31,302	€41,726
RWA (Basel III)	€290,076	€421,719
CET1 Ratio (Basel III)	**10.8%**	**9.9%**

Stress test's impact	Intesa	Unicredit
Additional NPL	€20,554	€11,849
Additional required provisions	€9,147	€5,283
Capital impact from additional NPL	€6,119	€3,534
RWA impact	€4,111	€2,370
Additional NPL (% of Gross Loans)	5.5%	2.1%

Post stress test	Intesa	Unicredit
New NPL	€76,057	€95,711
New NPL ratio	20.2%	16.9%
CET1 Capital (Basel III)	€25,183	€38,192
RWA (Basel III)	€294,187	€424,089
CET1 Ratio (Basel III)	**9.0%**	**9.0%**

Intesa able to absorb more asset quality deterioration

- Intesa has a larger buffer, in nominal, relative and historical terms when compared to Unicredit on potential to absorb further deterioration in asset quality
- As shown in the table, Intesa could "afford" to increase its NPL's by a further €20.5bn, or **5.5%** of NPL before reaching 9% Common Equity Tier 1. To put this into context, NPL's at Intesa have increase 1.9$% during the last year and 4.9% since 2010
- On the other hand, Unicredit could only increase NPL's by € 11.8bn, or **2.1%** of NPL before getting to 9% CT1
- The 9% threshold is a conservative one vis-a-vis the 8% CET1 proposed for the European Central Bank Asset Quality Review

Source: RBBCM Report

Valuation

Comparable Trading Analysis: Lower Tier

Company	Ticker	Market Cap	Beta	Div Yield	Tier 1 Capital	P / B	P / TB	ROE	NPL	Cost / Income
Barclays PLC	BARC	$67,894	1.71	2.6%	8.4%	0.71 x	0.83 x	11.8%	5.7%	65.9%
Banco Bilbao Vizcaya Argentaria, S.A.	BBVA	$72,213	1.41	4.4%	8.4%	1.23 x	1.46 x	7.8%	5.7%	50.8%
Commerzbank AG	CBK	$20,237	1.39	0.0%	8.6%	0.56 x	0.64 x	0.0%	7.5%	72.7%
Erste Group Bank AG	EBS	$15,018	1.36	0.8%	10.0%	0.96 x	1.22 x	8.7%	12.2%	56.8%
Intesa Sanpaolo S.p.A.	ISP	$51,352	1.44	1.6%	11.2%	0.74 x	0.74 x	3.0%	12.9%	50.7%
Lloyds Banking Group plc	LLOY	$96,246	1.33	0.0%	9.9%	1.92 x	2.16 x	2.2%	8.7%	51.2%
The Royal Bank of Scotland Group plc	RBS	$60,965	1.66	0.0%	9.1%	0.63 x	0.79 x	1.3%	9.1%	65.6%
UniCredit S.p.A.	UCG	$46,332	1.86	1.5%	9.8%	0.54 x	0.73 x	1.7%	14.9%	60.9%
Mean				**1.4%**	**9.4%**	**0.91 x**	**1.07 x**	**4.6%**	**9.6%**	**59.3%**
Median				**1.2%**	**9.5%**	**0.73 x**	**0.81 x**	**2.6%**	**8.9%**	**58.9%**
Low				**0.0%**	**8.4%**	**0.54 x**	**0.64 x**	**0.0%**	**5.7%**	**50.7%**
High				**4.4%**	**11.2%**	**1.92 x**	**2.16 x**	**11.8%**	**14.9%**	**72.7%**
Intesa Sanpaolo S.p.A.	**ISP**	**$51,352**	**1.44**	**1.6%**	**11.2%**	**0.74 x**	**0.74 x**	**3.0%**	**12.9%**	**50.7%**

Highlights

- Market is over-punishing ISP for being an Italian bank: As Italy's macro situation improves, P/B and P/TB should expand to comparable average of near 1
- Company Cost/Income ratio as one of the best in the lower to mid tier European Banks
- Dividend yield and ROE should also expand to mid-high tier levels as Europe embarks on its recovery

Implied Valuation

- Implied upside on a P/B and P/TB basis:

Current P/B	0.74x	Current P/TB	0.74x
Mean	0.91x	Mean	1.07x
Current Share Price	2.22	Current Share Price	2.22
Implied Share Price	2.73	Implied Share Price	3.23
Upside	23%	Upside	45%

Comparable Trading Analysis: High & Mid Tier

Company	Ticker	Market Cap	Beta	Div Yield	P / B	P / TB	ROE	NPL	Cost / Income
Svenska Handelsbanken AB (publ)	SHB A	$33,360	0.90	3.4%	1.91 x	2.06 x	14.4%	0.4%	46.8%
Swedbank AB (publ)	SWED A	$30,914	1.53	5.6%	1.80 x	2.06 x	13.4%	1.2%	43.7%
Skandinaviska Enskilda Banken AB (publ)	SEB A	$30,516	1.24	4.5%	1.59 x	1.78 x	11.5%	1.2%	54.4%
Nordea Bank AB (publ)	NDA SEK	$57,445	1.06	4.2%	1.42 x	1.60 x	11.5%	2.0%	48.9%
DNB ASA	DNB	$29,974	1.36	2.5%	1.26 x	1.32 x	11.1%	2.2%	47.2%
Credit Suisse Group AG	CSGN	$51,059	1.04	2.5%	1.05 x	1.29 x	10.6%	0.7%	77.8%
Mean				**3.8%**	**1.51 x**	**1.68 x**	**12.1%**	**1.3%**	**53.1%**
Median				**3.8%**	**1.50 x**	**1.69 x**	**11.5%**	**1.2%**	**48.1%**
Low				**2.5%**	**1.05 x**	**1.29 x**	**10.6%**	**0.4%**	**43.7%**
High				**5.6%**	**1.91 x**	**2.06 x**	**14.4%**	**2.2%**	**77.8%**

Company	Ticker	Market Cap	Beta	Div Yield	P / B	P / TB	ROE	NPL	Cost / Income
Danske Bank A/S	DANSKE	$27,509	1.33	1.4%	1.02 x	1.18 x	8.1%	6.8%	59.8%
KBC Group NV	KBC	$25,382	1.59	0.0%	1.29 x	1.42 x	14.0%	8.1%	52.7%
BNP Paribas SA	BNP	$100,771	1.54	2.6%	0.83 x	0.97 x	9.1%	6.5%	66.3%
UBS AG	UBSN	$79,917	1.25	1.3%	1.46 x	1.68 x	4.0%	0.6%	86.8%
HSBC Holdings plc	HSBA	$194,280	0.92	4.7%	1.09 x	1.32 x	5.0%	3.8%	55.1%
Deutsche Bank AG	DBK	$48,054	1.28	2.2%	0.61 x	0.82 x	5.5%	2.6%	80.1%
Societe Generale Group	GLE	$50,498	1.91	2.1%	0.71 x	0.82 x	7.0%	6.5%	70.1%
Mean				**2.0%**	**1.00 x**	**1.17 x**	**7.5%**	**5.0%**	**67.3%**
Median				**2.1%**	**1.02 x**	**1.18 x**	**7.0%**	**6.5%**	**66.3%**
Low				**0.0%**	**0.61 x**	**0.82 x**	**4.0%**	**0.6%**	**52.7%**
High				**4.7%**	**1.46 x**	**1.68 x**	**14.0%**	**8.1%**	**86.8%**

In the event of a European recovery, mean lower-tier multiples have the possibility of expanding to mid and even high tier levels

DDM: Valuation

Bear

- Continued decrease in loan growth throughout 2014 and 2015 leading to a ‘soft’ European recovery
  - Net Loans CAGR*: 2.7%
- Higher provisions in loan loss reserves for the event of further non-performing loans and defaults
  - Provisions: from 1.5% in 2013 (highest ever) to 1.2% in 2018
- Cost/Income ratio slight improvement
  - From: 44.8% in 2012 to 43.4% in 2018
- NIM experiences slight expansion
  - Expands 30 bps from 2013 to 2018

- **Downside: -31.18%**

Base

- Slight decrease in loan growth throughout 2014 as non-performing loans persist, leading to a European recovery
  - Net Loans CAGR*: 4.1%
  - Total Revenue CAGR*: 3.28%
- Provisions in loan loss reserves moderate decrease to reflect increasing European asset quality
  - Provisions: from 1.5% in 2013 (highest ever) to 1.1% in 2018
- Company is successful in continued cost cutting, Cost/Income ratio improves
  - From 44.8% in 2012 to 42.1% in 2018
- NIM experiences slight expansion
  - Expands 50 bps from 2013 to 2018

- **Upside: + 22.52%**

Bull

- Turnaround in European recovery starting in 2014
  - Net Loans CAGR*: 5%
- Provisions in loan loss reserves decrease to reflect increasing European asset quality
  - Provisions: from 1.5% in 2013 (highest ever) to 1.0% in 2018
- Successful cost cutting leads to Cost/ Income ratio improvement
  - From: 44.8% in 2012 to 40.7% in 2018
- NIM experiences significant expansion
  - Expands 70 bps form 2013 to 2018

- **Upside: + 54.54%**

**All CAGR are for the 5-year forecasted period of 2014 – 2018.*

DDM: Sensitivities

Sensitivities

Effective Tax Rate	Discount Rate (Cost of Equity) 7.94%	8.44%	8.94%	9.44%	9.94%
48.30%	5.72	3.51	2.54	1.99	1.65
46.30%	5.93	3.64	2.63	2.06	1.70
44.3%	6.14	3.76	**2.72**	2.13	1.76
42.30%	6.36	3.89	2.81	2.20	1.81
40.30%	6.57	4.02	2.90	2.27	1.86

Target Dividend Payout Ratio	Discount Rate (Cost of Equity) 7.94%	8.44%	8.94%	9.44%	9.94%
37.00%	5.11	3.42	2.57	2.06	1.72
36.00%	5.57	3.58	2.64	2.09	1.74
35.0%	6.15	3.77	**2.72**	2.13	1.76
34.00%	6.92	3.99	2.81	2.17	1.78
33.00%	8.00	4.26	2.91	2.22	1.80

Average Interest % on Loans	Discount Rate (Cost of Equity) 7.94%	8.44%	8.94%	9.44%	9.94%
5.70%	7.06	4.31	3.10	2.42	1.99
5.60%	6.60	4.04	2.91	2.28	1.87
5.50%	6.14	3.76	**2.72**	2.13	1.76
5.40%	5.69	3.49	2.53	1.98	1.64
5.30%	5.23	3.22	2.33	1.84	1.52

Beta Calculation

- Cost of Equity determined through un-levering and re-levering beta according to lower tier European banks.

Expected Return on the Market	7.85%
30year European Govt Bond Yield	2.52%
Cost of Equity	**9.31%**
Cost of Equity (terminal year)	8.94%

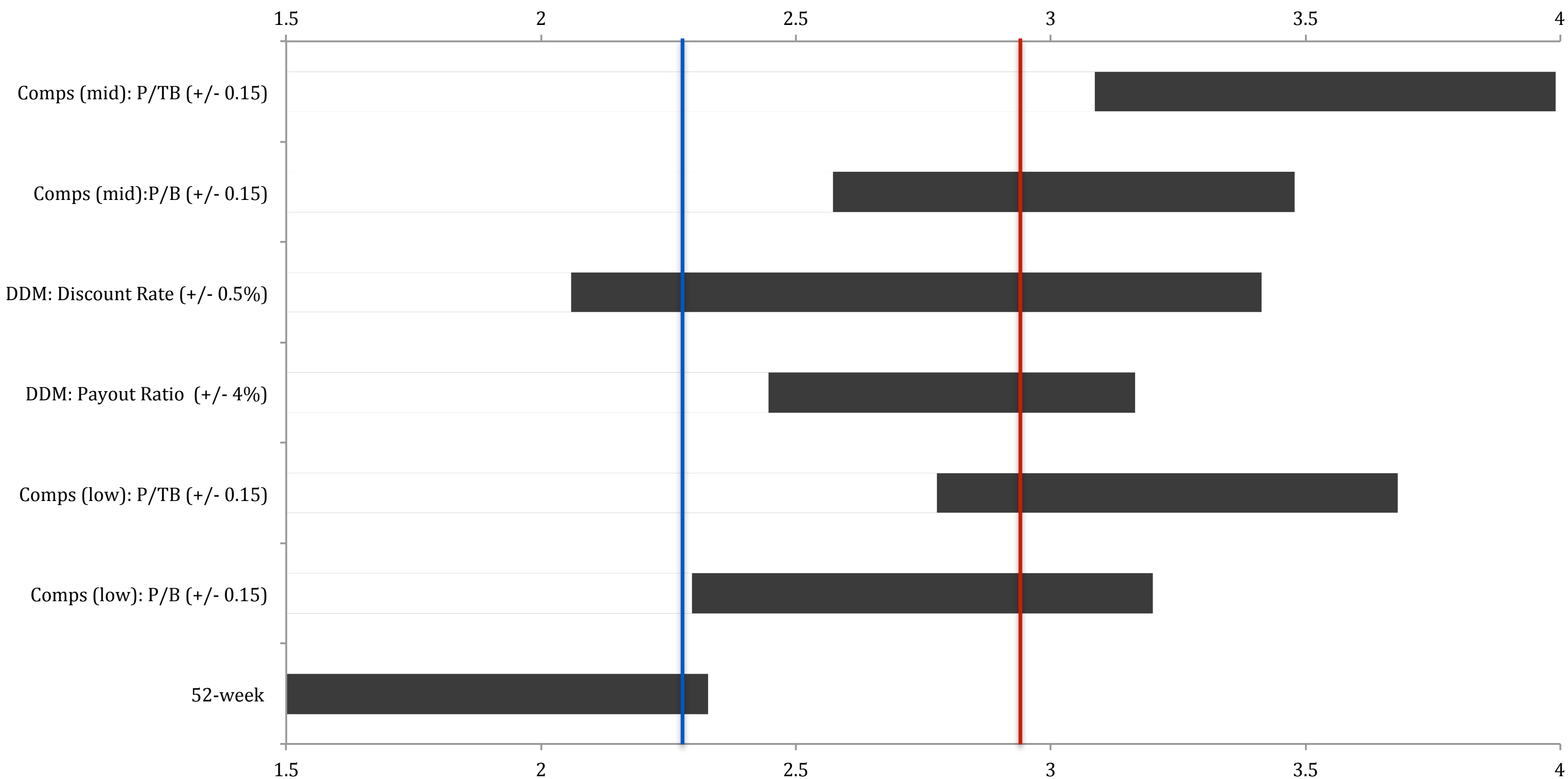
- Cost of Equity of the terminal year is equal to the unlevered beta of the mid-tier Comparables given the reduced default risk at that time
  - *As a proxy, NYU Average Cost of Equity for the US banking sector is 6.62%*
  - *Return on the Market estimated through NYU Country-Specific Analysis drawn from CDS Spreads*

- 5-year Regressions Beta Cost of Equity:

Adjusted Beta	1.336
Expected Return on the Market	7.85%
30year European Govt Bond Yield	2.52%
Cost of Equity	**9.64%**

DESAUTELS Capital Management Gestion de capitaux

Valuation: Football Field



Price target:	€ 2.94
Upside potential:	29%

DESAUTELS Capital Management
Gestion de capitaux

Risks & Recommendation

Risks & Mitigants

Industry-Wide

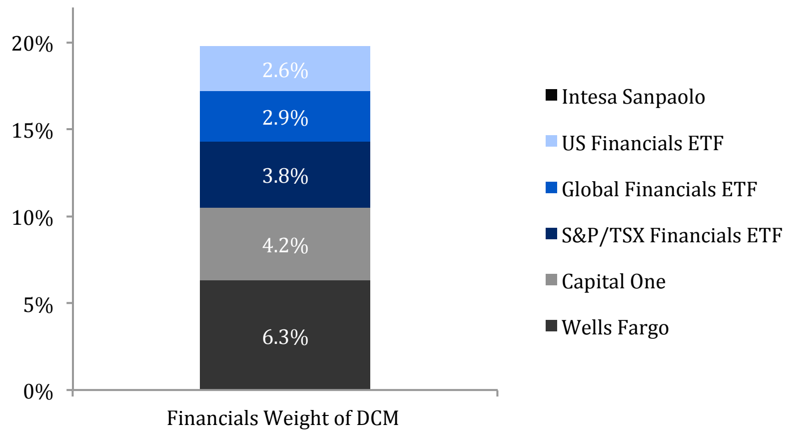
- DCM is more bullish on a European recovery in 2014 than most consensus & estimates – crises such as Ukraine can negatively affect the recovery
  - Mitigated by an encouraging US recovery, several positive indicators, and strong corporate results
  - Intesa's exposure is specific to Italy, so further crises in Eastern Europe will not be of great effect on price
- European Financials also are exposed to risks brought to light by recent events in the industry:
  - Litigation Risk
  - Increased Regulation Risk
  - Duration Risk (Assets and Liabilities)
- An overview of the Italian political landscape reveals a slim political risk as we invest in Italy
  - Compensated by the 2.85% Country Premium incorporated in the discount rate

Company Specific

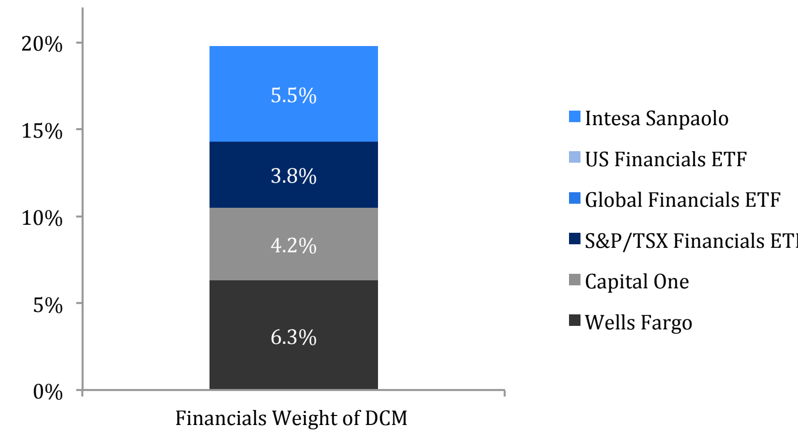
- ISP's exposure to Italy leaves it vulnerable to a fragile economy and population
- Although Intesa boasts strong capital positions and fares better than competitors on theoretical stress tests, the Bank has the possibility of failing the European Assessment Test, which would force it to discontinue operations
  - Mitigated by the 5.5% increase to NPL the bank can sustain, with further deleveraging possible by the talks with KKR

Recommendation: Allocation

Allocation Pre-Intesa



Allocation Post-Intesa



Allocation

- Allocation
  - Liquidate entire Global ETF and US ETF in order to initiate a position in Intesa Sanpaolo of 5.5%
  - With our exposure to both WFC and Capital One, we still remain overweight US as compared to our benchmark
  - With the Global ETF being heavily represented by American Banks (given their size), a move to a strictly European stock would help diversify away a small amount of risk from US, while allowing to benefit more from a gain in European Financials
- Where to buy the stock:
  - Milan Stock exchange
  - US OTC

Investment Thesis

Macro Focus: Europe

- European macro situation at a turning point: recovery in view
- European banks are better capitalized and stronger fundamentally than the market expects: especially when adjusting for the traditional comparison to American banks
- Given the observed discrepancies between bank valuations in different sovereign nations, it seems as though strong banks in weak economies make have been punished more than they deserved

Intesa Sanpaolo: Strong Fundamentals

- Asset Quality Review Tests: we see the upcoming ECB Comprehensive Assessment as a catalyst for the market to give credit to Intesa for its relatively strong capital positions
- Strong fundamentally with better than peers efficiency and capital ratios
- Positive EPS growth prospects due to
  - Increase in fees and commissions
  - Better cost cutting efforts
  - Cheaper funding mix

Valuation

- Lower-tier bank multiples have the potential to expand to mid-tier and even high-tier levels in the medium term given the signs of a European recovery
  - Intesa continues to trade at an unwarranted discount to its peers on P/B and P/TB multiples
- DDM supports the value proposed by Intesa's dividend to equity holders
- **DCM Financials Team price target: €2.94 representing a 29% upside**

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Q&A

Appendix

What's Hidden in the Small Print?

INTESA SANPAOLO

Securitization

- Consolidated SPV's hold **€2.7** bn in assets, mainly residential mortgage loans

Allowances

- Significant staff-related allowances due to cost-cutting efforts. Legal provisions are just under **€1 bn**

Derivatives

- Additional **2.8%** in off-balance sheet non-hedging derivatives

UniCredit

Securitization

- Consolidated SPV's hold **€3.7 bn** in assets, mainly residential mortgage loans

Allowances

- No significant legal disputes; in 2012 there was a reallocation surplus that reduced legal provisions by ~33%

Derivatives

- Additional **8.3%** in off-balance sheet non-hedging derivatives

Appendix A

Exhibit 14: Intesa net interest margin analysis

	2011			2012			
Interest and similar income (EURm)	Interest	Average Balance	Yield / cost	Interest	Average Balance	Yield / cost	2012/11 (Bp)
Financial assets held for trading	617	62,906	0.98%	490	64,997	0.75%	-23
Financial assets at fair value	360	35,529	1.01%	371	36,812	1.01%	-1
Financial assets available for sale	2,297	68,395	3.36%	2,875	89,790	3.20%	-16
Investments held to maturity	108	2,845	3.80%	90	2,215	4.06%	27
Due from banks	740	40,005	1.85%	716	35,343	2.03%	18
Loans to customers	13,871	377,542	3.67%	13,503	376,281	3.59%	-9
TOTAL	19,149	649,933	2.95%	19,700	665,568	2.96%	**1**
Interest and similar expense							
Due to Central Banks	190	27,283	0.70%	363	44,794	0.81%	11
Due to banks	651	38,469	1.69%	546	31,205	1.75%	6
Due to customers	1,480	377,279	0.39%	1,870	371,295	0.50%	11
Securities issued	5,402	179,336	3.01%	5,621	168,605	3.33%	32
TOTAL	7,762	649,933	1.19%	8,418	665,568	1.26%	**7**
NET INTEREST INCOME	**11,387**	**649,933**	**1.75%**	**11,282**	**665,568**	**1.70%**	**-6**
AGGREGATES							
Customer margin	6,986	377,542	1.85%	6,010	376,281	1.60%	**-25**
Financial operations	4,401	272,391	1.62%	5,272	289,287	1.82%	**21**

Note: The analysis uses disclosure at the Group level for both interest income and expense; this includes income and expense from insurance operations and thus are different from the quarterly management view; Therefore, the net interest margin figures differ from the ones in the Dupont table.
Source: Company reports and RBC Capital Markets estimates

Intesa Sanpaolo Market Summary

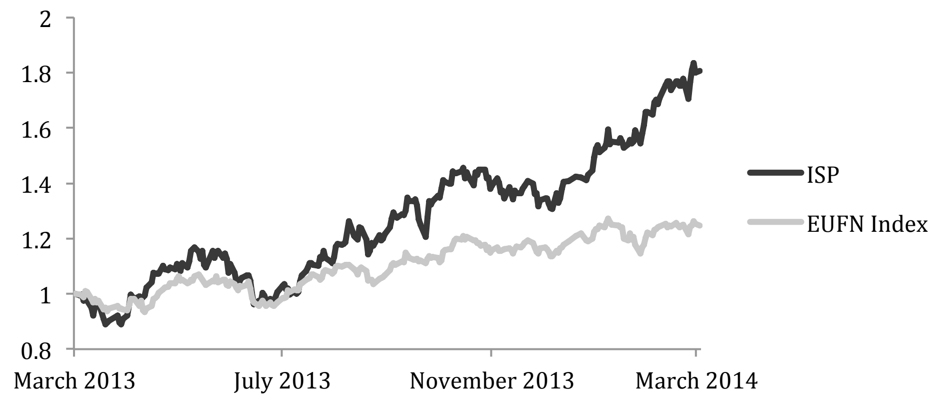
(in € millions except per share data)
Data as at March 7th, 2014

Share Price	**€2.28**
Dividend Yield	*2.20%*
52 Week High	**€2.33**
52 Week Low	**€1.09**
Shares Outstanding (mm)	15,508.4
Equity Market Value	**$37,074.5**

	FY end Dec 31st			
Forecast & Multiples	2012A	2013E (1)	2014E	2015E
Revenue (2)	17,881	16,528	16,815	17,403
growth		*-8%*	*2%*	*3%*
EBITDA (2)	9,622	8,505	9,272	10,221
growth		*-12%*	*9%*	*9%*
EPS	0.10	0.05	0.11	0.17
growth		*-50%*	*120%*	*55%*
P/E	13.00x	42.15x	16.86x	11.85x
P/B	0.43x	0.75x	0.73x	0.71x

All figures in EUR €
(1) Estimates as per analyst consensus - CAP IQ
(2) Revenue & EBITDA figures in millions

Share Trading Performance LTM



Business Segments

Retail Banking

Private Banking

Investment Banking

Asset Management

2014: low political risk for Italy

Political Risk 2014

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Risk and opportunity hotspots in key growth markets

The Political Risk (Dynamic) Index assesses risks that have the potential to undergo change and, in particular, deteriorate rapidly. It is comprised of 30 political risk indices under the four themes of governance framework, political violence, business and macroeconomic risk, and societal forced regime change risk. To further explore root causes and risk analytics, visit www.maplecroft.com.

Political Risk (Dynamic) Index: Top 20 Highest Risk

Rank	Country	Rating	Risk Trend
1	Somalia	Extreme	→
2	Syria	Extreme	↗
3	Afghanistan	Extreme	→
4	Sudan	Extreme	→
5	DR Congo	Extreme	→
6	C.A.R	Extreme	↗
7	Yemen	Extreme	→
8	Libya	Extreme	↗
9	South Sudan	Extreme	→
10	Iraq	Extreme	→
11	Myanmar	Extreme	↘
12	Pakistan	High	→
13	North Korea	High	→
14	Nigeria	High	→
15	Egypt	High	↗
16	Eritrea	High	↗
17	Zimbabwe	High	→
18	Russia	High	→
19	Iran	High	→
20	Chad	High	→

Political Risk (Dynamic) Index: Top 20 Growth Markets

GM Rank	Country	2014 Rank	Rating	Risk Trend
1	India	47	High	↘
2	China	59	High	→
3	Indonesia	62	High	→
4	Malaysia	122	Medium	↘
5	Bangladesh	30	High	→
6	Saudi Arabia	96	Medium	→
7	Philippines	36	High	↘
8	South Korea	157	Medium	→
9	Vietnam	71	High	→
10	Singapore	176	Low	→
11	Peru	104	Medium	→
12	Tanzania	72	Medium	→
13	Turkey	77	Medium	→
14	Qatar	147	Medium	→
15	Iraq	10	Extreme	→
16	USA	168	Low	→
17	Hong Kong	177	Low	→
18	Nigeria	14	High	→
19	Colombia	62	High	→
20	Panama	115	Medium	→

EXTREME RISK	> 0.00 – 1.25	> 1.25 – 2.50
HIGH RISK	> 2.50 – 3.75	> 3.75 – 5.00
MEDIUM RISK	> 5.00 – 6.25	> 6.25 – 7.50
LOW RISK	> 7.50 – 8.75	> 8.75 – 10.00