

## Company

31 August 2009 | 6 pages

# Unione Banche Italiane (UBI.MI)

 Equity 

## 2Q09 Results – Initial Reaction

- Results Weaker Than Consensus** — UBI posted net profit of €102m in 2Q09, weaker than consensus (c€120m). Operating profit pre provisions is 13% ahead of consensus, due to better costs; but higher bad debt provisions than expected result in operating profit after provisions 5% below consensus.
- Weak NII, Strong Commissions** — NII is down 5% QoQ and 3% weaker than our estimates, mostly due to deposit spread compression and flat volume (up in medium/long term, down in short term). This is the worst performance among Italian banks in our coverage: ISP +3% QoQ, BPM +3%, UCI +1%, BP -3% and MPS -3%. Fee income is up 3% QoQ, also 3% stronger than our estimates, mostly due to securities business and rising AUM. Trading is benefiting from the gains on the exchange offer of hybrids and lower tier 2 securities (c€60m).
- Better Than Expected Costs** — Operating costs are 5% below consensus, mostly due to lower staff costs, while other administrative costs are higher than expected. Staff costs are 3% down QoQ due to lower headcount and also lower variable compensation.
- Provisions Higher Than Expected** — Bad debt provisions are €236m in 2Q (or 97bp on loans), higher than consensus estimates (c€180m). Asset quality indicators are deteriorating due to economic conditions, with total net bad debts up c25% QoQ (and are 3.3% of loans, up from 2.6% in 1Q) mostly due to higher Incagli and restructured loans. Net sofferenze are 1.14% of loans (vs 0.98% in 1Q), net incagli are 1.54% of loans (vs 1.30% 1Q).
- Capital Stronger** — The core tier 1 increases to 7.2% in 2Q from 7.1% in 4Q08, a touch better than our estimates, possibly due to lower RWAs (-3% YTD). UBI's core tier 1 remains the strongest among Italian banks. UBI posted €39m of gains on financial assets mostly due to partial recovery on the Intesa stake devaluation posted in 1Q, given the accounting treatment opted for by UBI.
- 2H Outlook** — “NII will continue to be affected by the evolution of market interest rates” and in 2H will be affected by the changes in overdraft fee regulation. “Net commissions are expected to recover slightly”. “Staff costs are expected to rise slightly compared to first half”, “other administrative expenses and D&A should keep following the trend seen in the first half”. “The cost of credit should stand close to the level reached in the 2H08” (86 bp).
- Conference Call Monday Afternoon** — Management will host a conference call on Monday 31st August at 15:30 Milan time (dial in +39 02 805 88 11).

See Appendix A-1 for Analyst Certification and important disclosures.

<b>Hold/High Risk</b>	<b>2H</b>
Price (28 Aug 09)	€10.99
Target price	€10.80
Expected share price return	-1.7%
Expected dividend yield	2.8%
<b>Expected total return</b>	<b>1.1%</b>
Market Cap	€7,024M
	US\$10,080M

### Price Performance (RIC: UBI.MI, BB: UBI IM)



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## Unione Banche Italiane

### Company description

UBI was created on 1 April 2007 from the merger of BPU and Banca Lombarda. BPU was formed from BP Bergamo (BPB) and BP Commercio Industria (BPCI) in 2003. Banca Lombarda was a local bank in northern Italy. Both banks were strongly rooted in their local area. UBI is the fifth-largest Italian banking group in terms of customer loans. UBI is the second largest 'Popolare' (cooperative) banking group in terms of branches in Italy. UBI is active in all major sectors, from household and corporate lending to asset management, life insurance and corporate advisory.

### Investment strategy

We have a Hold/High Risk (2H) rating on UBI shares. UBI shares suit a defensive investment strategy. The main defensive characteristics of the UBI story are: solid balance sheet, a strong capital position and safer assets. The combination with Banca Lombarda should have a low integration risk and could generate more cost synergies. The stock trades broadly in line with Italian bank sector and in the short term profitability could suffer from deteriorating macroeconomic conditions (pressure on core revenues) and worsening of asset quality.

### Valuation

We have a €10.80 target price for UBI shares, based on a DDM calculation. In valuing UBI, we focus primarily on a DDM valuation using a c10% cost of equity and a c12% sustainable tangible ROE, also taking into account the group's capital position. We cross-check this with a price-to-book methodology. At our target price, the stock would trade at c1.2x price to tangible book valuation, reflecting UBI's defensive business mix and balance sheet characteristics.

### Risks

We have a High Risk rating on UBI shares. Any revenue slippage would impact UBI's profits. Net interest income is the major revenue generator; NII margin and profitability are at risk in the event of movement of the ECB rate and movement in the credit market rates, or of more pricing pressure in Italy. Among the potential risks for the stock, we would highlight: a weaker-than-expected Italian economy, slowdown in dividend payments, deterioration in asset quality, rising provisions, and any speculation indicating UBI as a possible partner in case of a rescue merger of any of its peers. If the impact on the company from any of these factors proves to be more or less negative than we anticipate, the stock could deviate significantly from our target price. The recent management change should not represent a key risk for the stock.

# Appendix A-1

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Analyst: Azzurra Guelfi

Covered since December 6 2007

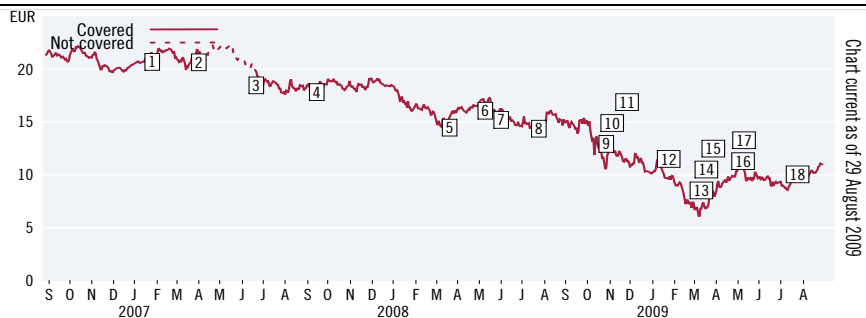


Chart current as of 29 August 2009

Date	Rating	Target Price	Closing Price
1 25-Jan-07	*2M	*23.11	21.46
2 2-Apr-07	Coverage suspended		
3 21-Jun-07	2M	*20.65	19.72
4 14-Sep-07	2M	*19.67	18.23
5 20-Mar-08	2M	*16.72	15.47
6 9-May-08	2M	*17.70	16.84

Date	Rating	Target Price	Closing Price
7 2-Jun-08	*1M	*18.49	16.14
8 24-Jul-08	1M	*17.70	14.86
9 28-Oct-08	1M	*13.77	10.64
10 5-Nov-08	1M	*15.24	12.79
11 26-Nov-08	1M	*13.77	11.22
12 23-Jan-09	1M	*11.31	9.57

Date	Rating	Target Price	Closing Price
13 11-Mar-09	1M	*8.85	6.81
14 18-Mar-09	*1H	8.85	6.93
15 27-Mar-09	1H	*10.03	8.39
16 8-May-09	1H	*13.28	11.29
17 11-May-09	1H	*12.59	10.48
18 24-Jul-09	*2H	*10.80	9.56

\* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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